



SAN MIGUEL CORPORATION

April 18, 2013

The Philippine Stock Exchange, Inc.
Disclosure Department
3rd Floor, Tower One and Exchange Plaza
Ayala Triangle, Ayala Avenue
Makati City

Attention: **Ms. Janet A. Encarnacion**
Head - Disclosure Department

Gentlemen:

We attach for your reference, a copy of the Offering Memorandum of the Company in connection with the issuance of US\$ denominated bonds in the amount of up to US\$2 billion.

Very truly yours,


MARY ROSE S. TAN
Assistant Corporate Secretary

IMPORTANT NOTICE

NOT FOR DISTRIBUTION TO ANY PERSON OR ADDRESS IN THE UNITED STATES

IMPORTANT: You must read the following before continuing. The following applies to the offering memorandum following this page (the “offering memorandum”), and you are therefore advised to read this carefully before reading, accessing or making any other use of the offering memorandum. In accessing the offering memorandum, you agree to be bound by the following terms and conditions, including any modifications to them any time you receive any information from us as a result of such access.

NOTHING IN THIS ELECTRONIC TRANSMISSION CONSTITUTES AN OFFER OF SECURITIES FOR SALE IN THE UNITED STATES OR ANY OTHER JURISDICTION WHERE IT IS UNLAWFUL TO DO SO. THE SECURITIES HAVE NOT BEEN, AND WILL NOT BE, REGISTERED UNDER THE UNITED STATES SECURITIES ACT OF 1933, AS AMENDED (THE “SECURITIES ACT”), OR THE SECURITIES LAWS OF ANY STATE OF THE UNITED STATES OR OTHER JURISDICTION AND THE SECURITIES MAY NOT BE OFFERED OR SOLD WITHIN THE UNITED STATES, EXCEPT PURSUANT TO AN EXEMPTION FROM, OR IN A TRANSACTION NOT SUBJECT TO, THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT AND APPLICABLE STATE OR LOCAL SECURITIES LAWS.

THIS OFFERING MEMORANDUM MAY NOT BE FORWARDED OR DISTRIBUTED TO ANY OTHER PERSON AND MAY NOT BE REPRODUCED IN ANY MANNER WHATSOEVER, AND IN PARTICULAR, MAY NOT BE FORWARDED TO ANY US ADDRESS. ANY FORWARDING, DISTRIBUTION OR REPRODUCTION OF THIS DOCUMENT IN WHOLE OR IN PART IS UNAUTHORIZED. FAILURE TO COMPLY WITH THIS DIRECTIVE MAY RESULT IN A VIOLATION OF THE SECURITIES ACT OR THE APPLICABLE LAWS OF OTHER JURISDICTIONS.

This Offering Memorandum is not a prospectus for the purposes of the European Union’s Directive 2003/71/EC and amendments thereto (the “Prospectus Directive”). This Offering Memorandum has been prepared on the basis that any offer of the Notes in any Member State of the European Economic Area which has implemented the Prospectus Directive will be made pursuant to an exemption under the Prospectus Directive from the requirement to publish a prospectus for offers of the Notes.

Confirmation of your Representation: This offering memorandum is being sent at your request and by accepting the e-mail and accessing this offering memorandum, you shall be deemed to have represented to us that the electronic mail address that you gave us and to which this e-mail has been delivered is not located in the United States and that you consent to delivery of such offering memorandum by electronic transmission.

You are reminded that this offering memorandum has been delivered to you on the basis that you are a person into whose possession this offering memorandum may be lawfully delivered in accordance with the laws of the jurisdiction in which you are located and you may not, nor are you authorized to, deliver this offering memorandum to any other person.

The materials relating to the offering of securities to which this offering memorandum relates do not constitute, and may not be used in connection with, an offer or solicitation in any place where offers or solicitations are not permitted by law. If a jurisdiction requires that the offering be made by a licensed broker or dealer and the underwriters or any affiliate of the underwriters is a licensed broker or dealer in that jurisdiction, the offering shall be deemed to be made by the underwriters or such affiliate on behalf of SMC (as defined in this offering memorandum) in such jurisdiction.

This offering memorandum has been sent to you in an electronic form. You are reminded that documents transmitted via this medium may be altered or changed during the process of electronic transmission and consequently none of the Australia and New Zealand Banking Group Limited and Standard Chartered Bank (the “Joint Arrangers”), the Dealers (as defined in this offering memorandum), any person who controls any Joint Arranger or any Dealer, or any director, officer, employee or agent of any Joint Arranger or any of the Dealers, or affiliate of any such person accepts any liability or responsibility whatsoever in respect of any difference between this offering memorandum distributed to you in electronic format and the hard copy version available to you on request from the Joint Arrangers and the Dealers.

You are responsible for protecting against viruses and other destructive items. Your use of this e-mail is at your own risk and it is your responsibility to take precautions to ensure that it is free from viruses and other items of a destructive nature.

OFFERING MEMORANDUM



(incorporated with limited liability in the Republic of the Philippines)

US\$2,000,000,000 Medium Term Note Programme

Under the Medium Term Note Programme described in this Offering Memorandum (the “Programme”), San Miguel Corporation (“SMC” or the “Company”), subject to compliance with all relevant laws, regulations and directives, may from time to time issue medium term notes (the “Notes”). Notes may be issued in bearer or registered form. The aggregate nominal amount of Notes outstanding will not at any time exceed US\$2,000,000,000 (or its equivalent in other currencies), subject to increase as described herein.

Approval in-principle has been granted by the Singapore Exchange Securities Trading Limited (the “SGX-ST”) for permission to deal in and quotation for any Notes which will at the time of issue thereof be so listed on the SGX-ST. Such permission will be granted when such Notes have been admitted to the Official List of the SGX-ST. Unlisted series of Notes may also be issued pursuant to the Programme. The relevant Pricing Supplement (as defined herein) in respect of any series of Notes will specify whether or not such Notes will be listed on the SGX-ST (or any other stock exchange). There is no assurance that the application to the Official List of the SGX-ST for the listing of the Notes will be approved. The SGX-ST assumes no responsibility for the correctness of any of the statements made or opinions or reports contained in this Offering Memorandum. Admission of the Notes to the Official List of the SGX-ST is not to be taken as an indication of the merits of the Programme, the Notes, SMC and/or its subsidiaries. Investors are advised to read and understand the contents of this Offering Memorandum before investing. If in doubt, investors should consult their advisers.

The Notes have not been and will not be registered under the United States Securities Act of 1933, as amended (the “Securities Act”) or with any securities regulatory authority of any state or other jurisdiction of the United States, and the Notes may include Bearer Notes (as defined herein) that are subject to U.S. tax law requirements. Subject to certain exceptions, the Notes may not be offered, sold, or, in the case of Bearer Notes, delivered within the United States or, in the case of Notes being offered or sold in reliance on Category 2 of Regulation S of the Securities Act, to, or for the account or benefit of U.S. persons unless an exemption from the registration requirement of the Securities Act is available and in accordance with all applicable securities laws of any state of the United States and any other jurisdiction. Registered Notes are subject to certain restrictions on transfer. See “*Subscription and Sale.*”

This Offering Memorandum is not a prospectus for the purposes of the European Union’s Directive 2003/71/EC and amendments thereto (the “Prospectus Directive”).

The Notes of each Series issued in bearer form (“Bearer Notes”) will be represented on issue by a temporary global note in bearer form (each a “Temporary Bearer Global Note”) or a permanent global note in bearer form (each a “Permanent Bearer Global Note”). Notes in registered form (“Registered Notes”) will be represented by a global note in registered form (each a “Registered Global Note”) and together with any Temporary Bearer Global Notes and Permanent Bearer Global Notes, the “Global Notes”), one Registered Global Note being issued in respect of each Noteholder’s entire holding of Notes in registered form of one Series. Global Notes may be deposited on the relevant issue date with a common depositary on behalf of Euroclear Bank SA/NV (“Euroclear”) and/or Clearstream Banking, société anonyme (“Clearstream”), or with a sub-custodian for the Central Moneymarkets Unit Service (“CMU”) operated by the Hong Kong Monetary Authority. The provisions governing the exchange of interests in Global Notes for other Global Notes and definitive Notes are described in “*Form of the Notes.*”

The Notes may be issued on a continuing basis to one or more of the Dealers specified under “*Summary of the Programme*” and any additional Dealer appointed under the Programme from time to time by SMC (each a “Dealer” and together the “Dealers”), which appointment may be for a specific issue or on an ongoing basis. References in this Offering Memorandum to the “relevant Dealer” shall, in the case of an issue of Notes being (or intended to be) subscribed by more than one Dealer, be to all Dealers agreeing to subscribe such Notes.

Notes issued under the Programme may be rated or unrated. Where an issue of Notes is rated, such rating will be specified in the relevant Pricing Supplement. A rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, change or withdrawal at any time by the assigning rating agency.

SMC may agree with any Dealer that Notes may be issued in a form not contemplated by the Terms and Conditions of the Notes herein, in which event a supplementary Offering Memorandum, if appropriate, will be made available which will describe the effect of the agreement reached in relation to such Notes.

Investing in Notes issued under the Programme involves certain risks and may not be suitable for all investors. Investors should have sufficient knowledge and experience in financial and business matters to evaluate the information contained in this Offering Memorandum and in the applicable Pricing Supplement and the merits and risks of investing in a particular issue of Notes in the context of their financial position and particular circumstances. Investors also should have the financial capacity to bear the risks associated with an investment in Notes. Investors should not purchase Note unless they understand and are able to bear risks associated with Notes. The principal risk factors that may affect the abilities of the Issuer and the Guarantor to fulfill their respective obligations in respect of the Notes are discussed under “Risk Factors” below.

Joint Arrangers

ANZ

Standard Chartered Bank

Dealers

ANZ BofA Merrill Lynch DBS Bank Ltd. Deutsche Bank Standard Chartered Bank

The date of this offering memorandum is April 15, 2013.

SMC confirms that (i) this Offering Memorandum contains all material information with respect to SMC, the SMC Group and the issue of the Notes, (ii) this Offering Memorandum does not contain an untrue statement of material fact or omit to state a material fact that is necessary in order to make the statements made in the Offering Memorandum, in the light of the circumstances under which they were made, not misleading, and there is no other fact or matter omitted from this Offering Memorandum which was or is necessary to enable investors and their professional advisers to make an informed assessment of the assets and liabilities, financial position, profits and losses and prospects of SMC or the SMC Group and of the issue of the Notes, (iii) the statements of intention, opinion, belief or expectation contained in the Offering Memorandum and any other materials used in the issue of the Notes are honestly and reasonably made or held and (iv) all reasonable enquiries have been made to ascertain such facts and to verify the accuracy of all such statements.

Each Tranche (as defined in “*Summary of the Programme*”) of Notes will be issued on the terms set out herein under “*Terms and Conditions of the Notes*” (the “Conditions”) as amended and/or supplemented by a document specific to such Tranche called a pricing supplement (the “Pricing Supplement”). This Offering Memorandum must be read and construed together with any amendments or supplements hereto and with any information incorporated by reference herein and, in relation to any Tranche of Notes, must be read and construed together with the relevant Pricing Supplement. This Offering Memorandum shall be read and construed on the basis that such documents are incorporated in and form part of this Offering Memorandum.

The distribution of this Offering Memorandum and any Pricing Supplement and the offering, sale and delivery of the Notes in certain jurisdictions may be restricted by law. Persons into whose possession this Offering Memorandum comes are required by SMC, the Joint Arrangers, the Dealers and the Trustee to inform themselves about and to observe any such restrictions. None of SMC, the Joint Arrangers, the Dealers or the Trustee represents that this Offering Memorandum or any Pricing Supplement may be lawfully distributed, or that any Notes may be lawfully offered, in compliance with any applicable registration or other requirements in any such jurisdiction, or pursuant to an exemption available thereunder, or assumes any responsibility for facilitating any such distribution or offering. In particular, no action is being taken to permit a public offering of the Notes or the distribution of this Offering Memorandum or any Pricing Supplement in any jurisdiction where action would be required for such purposes. Accordingly, no Notes may be offered or sold, directly or indirectly, and none of this Offering Memorandum, any Pricing Supplement or any advertisement or other offering material may be distributed or published in any jurisdiction, except under circumstances that will result in compliance with any applicable laws and regulations.

There are restrictions on the offer and sale of the Notes, and the circulation of documents relating thereto, in certain jurisdictions and to persons connected therewith. For a description of certain further restrictions on offers, sales and resales of the Notes and distribution of this Offering Memorandum and any Pricing Supplement, see “*Subscription and Sale.*”

No person has been authorized by SMC, the Joint Arrangers, the Dealers or DB Trustees (Hong Kong) Limited (the “Trustee”) to give any information or to make any representation other than those contained in this Offering Memorandum or any other document entered into in relation to the Programme and the sale of Notes and, if given or made, such information or representation should not be relied upon as having been authorized by SMC, the Joint Arrangers, any Dealer, the Trustee or any Agent (as defined in the “*Terms and Conditions of the Notes*”). Neither the delivery of this Offering Memorandum or any Pricing Supplement nor any offering, sale or delivery made in connection with the issue of the Notes shall, under any circumstances, constitute a representation that there has been no change or development reasonably likely to involve a change in the affairs of SMC, the SMC Group or any of them since the date hereof or the date upon which this Offering Memorandum has been most recently amended or supplemented or create any implication that the information contained herein is correct as at any date subsequent to the date hereof or the date upon which this Offering Memorandum has been most recently amended or supplemented or that any other information supplied in connection with the Programme is correct as of any time subsequent to the date on which it is supplied or, if different, the date indicated in the document containing the same.

This Offering Memorandum does not constitute an offer of, or an invitation by or on behalf of SMC, the Joint Arrangers, the Dealers, the Trustee or the Agents to subscribe for or purchase any Notes and may not be used for the purpose of an offer to, or a solicitation by, anyone in any jurisdiction or in any circumstances in which such offer or solicitation is not authorised or is unlawful.

None of the Joint Arrangers, the Dealers or the Trustee has separately verified the information contained herein. Accordingly, no representation or warranty or undertaking, express or implied, is made or given and no responsibility or liability is accepted by the Joint Arrangers, the Dealers, the Trustee or the Agents as to the accuracy, completeness or sufficiency of the information contained or incorporated in this Offering Memorandum or any other information provided by SMC in connection with the Programme, and nothing

contained or incorporated in this Offering Memorandum is, or shall be relied upon as, a promise, representation or warranty by the Joint Arrangers, the Dealers, the Trustee or the Agents. Neither this Offering Memorandum nor any other information supplied in connection with the Programme or any Notes (i) is intended to provide the basis of any credit or other evaluation or (ii) should be considered as a recommendation by SMC, the Joint Arrangers, any of the Dealers, the Trustee or any of the Agents that any recipient of this Offering Memorandum, any Pricing Supplement or any other information supplied in connection with the Programme or any Notes should purchase any Notes. Each potential purchaser of Notes should determine for itself the relevance of the information contained in this Offering Memorandum, any Pricing Supplement or any other information supplied in connection with the Programme or any Notes and its purchase of Notes should be based upon its own investigation and appraisal of the condition (financial or otherwise) of SMC Group and such other investigations with its own tax, legal and business advisers as it deems necessary.

To the fullest extent permitted by law, none of the Joint Arrangers, the Dealers or the Trustee nor any of their respective affiliates or advisors accept any responsibility for the contents of this Offering Memorandum or for any other statement, made or purported to be made by the Joint Arrangers or a Dealer or on its behalf in connection with SMC or the issue and offering of the Notes. Each of the Joint Arrangers, the Dealers, the Trustee and their respective affiliates or advisors accordingly disclaims all and any liability whether arising in tort or contract or otherwise which it might otherwise have in respect of the Offering Memorandum or any such statement.

None of the Joint Arrangers, the Dealers, the Trustee or any of their respective affiliates or advisors undertakes to review the financial condition or affairs of SMC and its subsidiaries during the life of the arrangements contemplated by this Offering Memorandum nor to advise any investor or prospective investor in the Notes of any information coming to the attention of any of the Joint Arrangers, the Dealers, the Trustee or their respective affiliates or advisors.

None of SMC, the Joint Arrangers, the Dealers or the Trustee makes any representation to any investor in the Notes regarding the legality of its investment under any applicable laws. Any investor in the Notes should be able to bear the economic risk of an investment in the Notes for an indefinite period of time.

NOTHING IN THIS OFFERING MEMORANDUM CONSTITUTES AN OFFER OF SECURITIES FOR SALE IN THE UNITED STATES OR ANY OTHER JURISDICTION WHERE IT IS UNLAWFUL TO DO SO. THE NOTES HAVE NOT BEEN AND WILL NOT BE REGISTERED UNDER THE SECURITIES ACT OR WITH ANY SECURITIES REGULATORY AUTHORITY OF ANY STATE OR OTHER JURISDICTION OF THE UNITED STATES, AND THE NOTES MAY INCLUDE BEARER NOTES (AS DEFINED HEREIN) THAT ARE SUBJECT TO U.S. TAX LAW REQUIREMENTS. SUBJECT TO CERTAIN EXCEPTIONS, THE NOTES MAY NOT BE OFFERED, SOLD, OR, IN THE CASE OF BEARER NOTES, DELIVERED WITHIN THE UNITED STATES OR, IN THE CASE OF NOTES BEING OFFERED OR SOLD IN RELIANCE ON CATEGORY 2 OF REGULATION S OF THE SECURITIES ACT, TO, OR FOR THE ACCOUNT OR BENEFIT OF U.S. PERSONS UNLESS AN EXEMPTION FROM THE REGISTRATION REQUIREMENT OF THE SECURITIES ACT IS AVAILABLE AND IN ACCORDANCE WITH ALL APPLICABLE SECURITIES LAWS OF ANY STATE OF THE UNITED STATES AND ANY OTHER JURISDICTION. REGISTERED NOTES ARE SUBJECT TO CERTAIN RESTRICTIONS ON TRANSFER.

The maximum aggregate principal amount of Notes outstanding at any one time under the Programme will not exceed US\$2,000,000,000 (and for this purpose, any Notes denominated in another currency shall be translated into U.S. dollars at the date of the agreement to issue such Notes calculated in accordance with the provisions of the Programme Agreement.) The maximum aggregate principal amount of Notes which may be outstanding at any one time under the Programme may be increased from time to time, subject to compliance with the relevant provisions of the Programme Agreement as defined under “*Subscription and Sale*.”

In making an investment decision, investors must rely on their own examination of the SMC Group and the terms of the offering, including the merits and risks involved. See “*Risk Factors*” for a discussion of certain factors to be considered in connection with an investment in the Notes.

Each person receiving this Offering Memorandum acknowledges that such person has not relied on the Joint Arrangers, Dealers, the Trustee or the Agents, or any person affiliated with the Joint Arrangers, Dealers, the Trustee or the Agents, in connection with its investigation of the accuracy of such information or its investment decision.

IN CONNECTION WITH THE ISSUE OF ANY TRANCHE OF NOTES, THE DEALER OR DEALERS (IF ANY) NAMED AS THE STABILIZING MANAGER(S) (OR ANY PERSON(S) ACTING ON BEHALF OF ANY STABILIZING MANAGER(S) IN THE APPLICABLE PRICING SUPPLEMENT

MAY OVER-ALLOT NOTES OR EFFECT TRANSACTIONS WITH A VIEW TO SUPPORTING THE MARKET PRICE OF THE NOTES AT A LEVEL HIGHER THAN THAT WHICH MIGHT OTHERWISE PREVAIL. HOWEVER, THERE IS NO ASSURANCE THAT THE STABILIZING MANAGER(S) (OR PERSON ACTING ON BEHALF OF A STABILIZING MANAGER) WILL UNDERTAKE STABILIZATION ACTION. ANY STABILIZATION ACTION MAY BEGIN ON OR AFTER THE DATE ON WHICH ADEQUATE PUBLIC DISCLOSURE OF THE TERMS OF THE OFFER OF THE RELEVANT TRANCHE OF NOTES IS MADE AND, IF BEGUN, MAY BE ENDED AT ANY TIME AND MUST END NO LATER THAN THE EARLIER OF 30 DAYS AFTER THE ISSUE DATE OF THE RELEVANT TRANCHE OF NOTES AND 60 DAYS AFTER THE DATE OF THE ALLOTMENT OF THE RELEVANT TRANCHE OF NOTES. ANY STABILIZATION ACTION OR OVERALLOTMENT MUST BE CONDUCTED BY THE STABILIZING MANAGER(S) (OR PERSONS ACTING ON BEHALF OF ANY STABILIZING MANAGER(S)) IN ACCORDANCE WITH ALL APPLICABLE LAWS AND RULES.

This Offering Memorandum has been prepared on the basis that any offer of Notes in any Member State of the European Economic Area which has implemented Directive 2003/71/EC (the “Prospectus Directive”) as amended (which includes the amendments made by Directive 2010/73/EU (the “2010 PD Amending Directive”) to the extent such amendments have been implemented in a relevant Member State of the European Economic Area (each, a Relevant Member State) will be made pursuant to an exemption under the Prospectus Directive, as implemented in that Relevant Member State, from the requirement to publish a prospectus for offers of Notes. Accordingly any person making or intending to make an offer in that Relevant Member State of Notes which are the subject of an offering contemplated in this Offering Memorandum as completed by Final Terms in relation to the offer of those Notes may only do so in circumstances in which no obligation arises for SMC or any Dealer to publish a prospectus pursuant to Article 3 of the Prospectus Directive or supplement a prospectus pursuant to Article 16 of the Prospectus Directive, in each case, in relation to such offer. Neither SMC nor any Dealer has authorized, nor does it authorize, the making of any offer of Notes in circumstances in which an obligation arises for SMC or any Dealer to publish or supplement a prospectus for such offer.

FORWARD-LOOKING STATEMENTS

This Offering Memorandum contains forward-looking statements that are, by their nature, subject to significant risks and uncertainties. These forward-looking statements include, without limitation, statements relating to:

- known and unknown risks;
- uncertainties and other factors which may cause the actual results, performance or achievements of the SMC Group to be materially different from any future results;
- performance or achievements expressed or implied by forward-looking statements; and
- expectations and projections for future operating performance and business prospects.

The words “may,” “will,” “should,” “seek,” “aim,” “believe,” “expect,” “anticipate,” “estimate,” “project,” “intend” and similar words identify forward-looking statements. In addition, all statements other than statements of historical facts included in this Offering Memorandum are forward-looking statements. Statements in the Offering Memorandum as to the opinions, beliefs and intentions of SMC accurately reflect in all material respects the opinions, beliefs and intentions of its management as to such matters as of the date of this Offering Memorandum, although SMC gives no assurance that such opinions or beliefs will prove to be correct or that such intentions will not change. This Offering Memorandum discloses, under the section “Risk Factors” and elsewhere, important factors that could cause actual results to differ materially from SMC’s expectations. All subsequent written and oral forward-looking statements attributable to SMC or persons acting on behalf of SMC are expressly qualified in their entirety by the cautionary statements in this section.

Such forward-looking statements are based on numerous assumptions regarding the present and future business strategies of the SMC Group and the environment in which the SMC Group will operate in the future. Important factors that could cause some or all of the assumptions not to occur or cause actual results, performance or achievements to differ materially from those in the forward-looking statements include, among other things:

- the ability of SMC to successfully implement its strategies;
- changes in laws, rules and regulations, including tax laws and licensing requirements in the Philippines;
- changes in availability and prices of raw materials used in the production processes of the SMC Group;
- the ability of the SMC Group to anticipate and respond to consumer trends;
- the ability of SMC to successfully manage its growth, including acquisitions;
- the condition and changes in the Philippine, Asian or global economies;

- any future political instability in the Philippines;
- competition in the industries in which the SMC Group operates in the Philippines and globally; and
- changes in interest rates, inflation rates and the value of the Philippine Peso against the U.S. dollar and other currencies.

Additional factors that could cause the actual results, performance or achievements of the SMC Group to differ materially from forward-looking statements include, but are not limited to, those disclosed under “*Risk Factors*” and elsewhere in this Offering Memorandum. These forward-looking statements speak only as of the date of this Offering Memorandum. SMC and the Joint Arrangers and Dealers expressly disclaim any obligation or undertaking to release, publicly or otherwise, any updates or revisions to any forward-looking statement contained herein to reflect any change in the expectations of SMC with regard thereto or any change in events, conditions, assumptions or circumstances on which any statement is based.

NON-PFRS FINANCIAL MEASURES

The term “EBITDA” refers to earnings before interest expenses, taxes, depreciation and amortization. In this Offering Memorandum, EBITDA is calculated as net income before: income tax expense, net financing charges (interest income net of interest expense), extraordinary or exceptional items, foreign exchange losses (gains), marked-to-market currency losses (gains) and depreciation and amortization and impairment losses. EBITDA is not a measure determined in accordance with Philippine Financial Reporting Standards (“PFRS”), and prospective investors should not consider EBITDA as an alternative to net income as a measure of operating performance or to cash flow as a measure of free cash flow for management’s discretionary use, as it does not reflect certain cash requirements such as interest payments, tax payments and capital expenditures. The calculation of EBITDA of SMC may be different from the calculations used by other companies, and, as a result, the EBITDA of SMC may not be comparable to other similarly titled measures of other companies.

SMC believes that EBITDA facilitates operating performance comparisons from period to period and from company to company by eliminating potential differences caused by variations in capital structures (affecting interest expense), tax positions (such as the impact on periods or companies of changes in effective tax rates or net operating losses) and the age and book depreciation of tangible assets (affecting relative depreciation expense). In particular, EBITDA eliminates non-cash depreciation expenses that arise from the capital intensive nature of the businesses of the SMC Group. SMC also believes that EBITDA is a supplemental measure of the ability to meet debt service requirements of the SMC Group. Finally, SMC presents EBITDA because it believes it is frequently used by securities analysts and investors in the evaluation of companies in its industry.

BASIS FOR CERTAIN MARKET DATA

Market data and certain industry forecasts and other data used throughout this Offering Memorandum were obtained or derived from internal surveys, market research, governmental data, publicly available information and/or industry publications. Industry publications generally state that the information contained therein has been obtained from sources believed to be reliable, but the accuracy and completeness of such information are not guaranteed and have not been independently verified by SMC or the Joint Arrangers or Dealers or the Trustee or the Agents. Similarly, internal surveys, industry forecasts and market research, while believed to be reliable, have not been independently verified, and none of SMC, the Joint Arrangers, Dealers, the Trustee or the Agents make any representation or warranty, express or implied, as to the accuracy or completeness of such information. In addition, such information may not be consistent with other information compiled within or outside the Philippines.

CONVENTIONS AND CURRENCY PRESENTATION WHICH APPLY TO THIS OFFERING MEMORANDUM

In this Offering Memorandum, references to “US\$” and “U.S. dollars” are to the lawful currency of the United States of America, references to “Pesos” or “P” are to the lawful currency of the Republic of the Philippines, references to “RM” are to the lawful currency of Malaysia and references to “Renminbi”, “RMB” or “CNY” are to the lawful currency of the PRC. All references to dates and times are to Metro Manila dates and times, unless otherwise specified. All references in this Offering Memorandum to the “Government” are to the government of the Republic of the Philippines and all references to the “Philippines” are to the Republic of the Philippines. References to the “United States” or “U.S.” in this Offering Memorandum shall be to the United States of America, its territories and possessions, any State of the United States and the District of Columbia. References to “Hong Kong” are to the Hong Kong Special Administrative Region of the People’s Republic of China. References to the “PRC” are to the People’s Republic of China excluding Hong Kong, the Macau Special Administrative Region of the PRC and Taiwan.

PRESENTATION

The consolidated financial statements of SMC are reported in Philippine Pesos and are prepared based on its accounting policies, which are in accordance with PFRS issued by the Financial Reporting Standards Council of the Philippines. PFRS include statements named PFRS and Philippine Accounting Standards, and Philippine Interpretations from International Financial Reporting Interpretations Committee.

Certain Philippine Peso amounts have been translated into U.S. dollar amounts, based on the prevailing exchange rate on December 28, 2012 of ₱41.05 = US\$1.00, being the closing rate for that date for the purchase of U.S. dollars with Philippine Pesos under the Philippine Dealing System (the “PDS”). Such translations should not be construed as representations that the Philippine Peso or U.S. dollar amounts referred to could have been, or could be, converted into U.S. dollars or Philippine Pesos, as the case may be, at that or any other rate, or at all. Figures in this Offering Memorandum have been subjected to rounding adjustments. Accordingly, figures shown for the same item of information may vary, and figures which are totals may not be an arithmetic aggregate of their components. On April 12, 2013, the closing rate for the purchase of U.S. dollars with Philippine Pesos under the PDS was ₱41.27 = US\$1.00.

ENFORCEABILITY OF CIVIL LIABILITIES

SMC is organized under the laws of the Republic of the Philippines, and a substantial portion of the assets of SMC are located in the Philippines. It may be difficult for investors to effect service of process outside the Philippines upon SMC, with respect to claims pertaining to the offering or the Notes. Moreover, it may be difficult for investors to enforce in the Philippines judgments against SMC obtained outside the Philippines, in any action pertaining to the Notes, particularly with respect to actions for claims to which SMC has not consented to service of process outside the Philippines. In addition, most of the directors and officers of SMC are residents of the Philippines, and all or a substantial portion of the assets of such persons are or may be located in the Philippines. As a result, it may be difficult for investors to effect service of process upon such persons outside the Philippines or enforce against such persons judgments obtained in courts outside the Philippines.

The Philippines is not a party to any international treaty in relation to the recognition or enforcement of foreign judgments. A judgment obtained against SMC in any foreign court may be recognized and enforced by the courts of the Philippines in an independent action brought in accordance with the relevant procedures set forth in the Rules of Court of the Philippines to enforce such judgment. However, such foreign judgment or final order may be rejected in the following instances: (i) such judgment was obtained by collusion or fraud, (ii) the foreign court rendering such judgment did not have jurisdiction over the subject matter of the action in accordance with its jurisdictional rules, (iii) such order or judgment is contrary to Philippine laws that have as their object good customs, public order or public policy, (iv) the defendant did not have notice of the proceedings before the foreign court, or (v) such judgment was based upon a clear mistake of law or fact. Furthermore, Philippine courts have held that a foreign judgment is presumed to be valid and binding in the country from which it issues, until the contrary is shown, and the party contesting the foreign judgment has the burden of overcoming the presumption of its validity.

THE SECURITIES BEING OFFERED OR SOLD HAVE NOT BEEN AND WILL NOT BE REGISTERED WITH THE PHILIPPINE SECURITIES AND EXCHANGE COMMISSION (“PHILIPPINE SEC”) UNDER THE SECURITIES REGULATION CODE OF THE PHILIPPINES (THE “SRC”). ANY FUTURE OFFER OR SALE OF THE NOTES WITHIN THE PHILIPPINES IS SUBJECT TO THE REGISTRATION REQUIREMENTS UNDER THE SRC UNLESS SUCH OFFER OR SALE IS MADE UNDER CIRCUMSTANCES IN WHICH THE NOTES QUALIFY AS EXEMPT SECURITIES OR QUALIFIES AS AN EXEMPT TRANSACTION UNDER THE SRC.

Any offer or sale of the Notes within the Philippines is subject to registration unless such offer or sale is made under circumstances in which the Notes qualify as exempt securities or pursuant to an exempt transaction under the SRC. The offer or sale of the Notes in the Philippines to (a) “primary institutional lenders” pursuant to Rule 9.2(2) B of the amended implementing rules of the SRC, or (b) persons who are “qualified buyers” pursuant to Section 10.1(l) of the SRC, or (c) not more than nineteen (19) persons who are not “qualified buyers” during any twelve-month period pursuant to Section 10.1(k) of the SRC is exempt from registration. SMC has not obtained confirmation from the Philippine SEC that the offer and sale of the Notes within the Philippines qualifies as an exempt transaction. If necessary, SMC will file a notice of exemption from registration with the Philippine SEC pursuant to SRC Rule 10.1(3). Each Joint Arranger and Dealer has represented, warranted and agreed that it has not and will not sell or offer for sale or distribution any Notes in the Philippines except to “primary institutional lenders” pursuant to Rule 9.2(2) B of the amended implementing rules of the SRC or to “qualified buyers” pursuant to Section 10.1(l) of the SRC. Prospective investors should take note of the transfer restrictions set out in Rule 9.2(2) B of the amended implementing rules of the SRC.

DOCUMENTS INCORPORATED BY REFERENCE

This Offering Memorandum should be read and construed in conjunction with:

- (i) each relevant Pricing Supplement;
- (ii) all amendments and supplements from time to time to this Offering Memorandum;
- (iii) any annual or interim financial statements (whether audited or unaudited) of SMC that are appended to or circulated with this Offering Memorandum and are dated as at a date, or for a period ending, subsequent to those financial statements appearing elsewhere in this Offering Memorandum; and
- (iv) filings and announcements posted on the Philippine Stock Exchange (“PSE”),

which shall be deemed to be incorporated in, and to form part of, this Offering Memorandum and which shall be deemed to modify or supersede the contents of this Offering Memorandum to the extent that a statement contained in any such document is inconsistent with such contents.

Copies of all such documents which are so deemed to be incorporated in, and to form part of, this Offering Memorandum will be available for inspection during normal business hours on any weekday (Saturdays, Sundays and public holidays excepted) from the specified office of the Paying Agent set out at the end of this Offering Memorandum.

SUPPLEMENTAL OFFERING MEMORANDUM

SMC has given an undertaking to the Joint Arrangers and the Dealers that in the event of (i) a significant new factor, material mistake or inaccuracy relating to information included in this Offering Memorandum which is capable of affecting the assessment of the Notes arising or being noted, (ii) a change in the condition of the SMC Group which is material in the context of the Programme or the issue of any Notes or (iii) this Offering Memorandum otherwise coming to contain an untrue statement of a material fact or omitting to state a material fact necessary to make the statements contained therein not misleading or if it is necessary at any time to amend this Offering Memorandum to comply with, or reflect changes in, the laws or regulations of the Philippines or any other relevant jurisdiction, SMC shall update, prior to any further issue of Notes, or amend this Offering Memorandum (following consultation with the Joint Arrangers, who will consult with the Dealers) by the publication of a supplement to it or a new Offering Memorandum, in each case in a form approved by the Joint Arrangers and the Dealers.

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SUMMARY

Overview

SMC is one of the most diversified and also one of the largest Philippine conglomerates by market capitalization and total assets, with sales equaling approximately 6.6% of the Philippine gross domestic product (“GDP”) in 2012. Originally founded in 1890 as a single brewery in the Philippines, SMC has transformed itself from a market-leading beverage, food and packaging business with a globally recognized beer brand, into a large and diversified conglomerate with additional market-leading businesses and investments in the fuel and oil, energy, infrastructure, telecommunications, mining and airline industries in the Philippines. SMC has a portfolio of companies that is interwoven into the economic fabric of the Philippines, benefiting from, as well as contributing to, the development and economic progress of the Philippines. The common shares of SMC were listed on the PSE on November 5, 1948, and as of December 31, 2012, SMC had a market capitalization of ₱250.1 billion. The consolidated sales, gross profit and EBITDA of SMC in 2012 were ₱698,868 million, ₱104,136 million and ₱78,071 million, respectively.

Corporate Transformation of SMC

Established in 1890 as a single brewery in the Philippines, the SMC Group has become a Philippine market leader in its established businesses in beverage, food and packaging industries with over 18,000 employees and more than 100 production facilities in the Asia-Pacific region as of December 31, 2012. The extensive portfolio of SMC products includes beer, liquor, non-alcoholic beverages, poultry, animal feeds, flour, meat, dairy products, coffee and various packaging products.

In 2007, in light of the opportunities presented by the global financial crisis, the ongoing program of asset and industry privatization of the Philippine government and the strong cash position of SMC enhanced by recent divestments and the strong cash flow generated by its established businesses, SMC adopted an aggressive business diversification program. The program channeled the resources of SMC into what it believes were attractive growth sectors, aligned with the development and growth of the Philippine economy. SMC believes this strategy will achieve a more diverse mix of sales and operating income, better position SMC to access capital, present different growth opportunities and mitigate the impact of downturns and business cycles.

SMC Businesses

Today, SMC is one of the largest and most diverse business groups in the Philippines. The portfolio of SMC encompasses the following businesses, most of which are market leaders in their respective industries:

Beverage

The beverage business consists of brewing, distilling, selling, marketing and distributing beer, liquor and non-alcoholic beverages. SMC conducts its beverage business through majority owned subsidiaries: San Miguel Brewery Inc. (“SMB”) for beer and Ginebra San Miguel Inc. (“Ginebra”) for liquor and non-alcoholic beverages. San Miguel sells the dominant beer brands in the Philippines, with a total market share of more than 90% according to Canadean data. Its products include *San Miguel Pale Pilsen*, which is the flagship beer of SMB and is sold throughout the world, *San Miguel Super Dry*, *San Mig Light*, *San Mig Strong Ice* and *San Miguel Premium All-Malt*. Other SMC beers include *Cerveza Negra*, *Red Horse*, *Gold Eagle*, *Oktoberfest Brew*, *San Miguel Flavored Beer* and the recently introduced *San Mig Zero*. In addition to its Philippine beer operations, SMB has brewery and sales operations in China, Hong Kong, Thailand, Vietnam and Indonesia, and exports to over 40 countries. SMC produces some of the most recognizable brands in the Philippine liquor market, including *Ginebra San Miguel*, *GSM Blue*, *Gran Matador Brandy*, *Gran Matador Light*, *Antonov Vodka* and *Vino Kulafu*, in addition to having a distillery in Thailand. SMC also has a growing non-alcoholic beverage business which produces non-carbonated, ready-to-drink tea and fruit juice products, primarily under the *Magnolia* brand.

Food

The food business holds numerous market leading positions in the Philippine food industry, offering a broad range of high-quality food products and services to both household and food service customers. The food business is conducted through San Miguel Pure Foods Company Inc. (“San Miguel Pure Foods”). The business is organized into business clusters: Agro-Industrial (poultry, feeds and fresh meats); Value-Added Meats (processed meats); Milling (flour and flour products); and Dairy products, Spreads and Oils (“DSO”), ice cream,

coffee, food service, retail and miscellaneous businesses. SMC has some of the best known brands in the Philippine food industry, such as *Purefoods*, *Magnolia*, *Monterey*, *Star*, *Dari Crème* and *B-Meg*. In addition to its Philippine operations, the food business has operations in Indonesia and Vietnam.

Packaging

The packaging business has one of the largest packaging operations in the Philippines, producing glass, metal, plastic, aluminum cans, paper, flexibles, PET and other packaging products. The packaging business is conducted through the Packaging Group, which comprises San Miguel Yamamura Packaging Corporation (“SMYPC”), San Miguel Yamamura Packaging International Limited (“SMYPIL”), San Miguel Yamamura Asia Corporation (“SMYAC”) and Mindanao Corrugated Fibreboard, Inc. (“Mincorr”). The packaging business is the major source for packaging products for the other businesses of SMC. It also supplies its products to major multinational corporations in the Philippines and customers across the Asia-Pacific region, the United States, Africa, Australia and the Middle East.

Properties

San Miguel Properties, Inc. (“SMPI”) was established in 1990 initially as the corporate real estate arm of SMC. It is the primary property subsidiary of SMC, currently 98.5%-owned by SMC. SMPI is presently engaged in commercial property development, sale and lease of real properties, management of strategic real estate ventures and corporate real estate services.

Fuel and Oil

SMC operates its fuel and oil business through Petron, in which SMC holds a 68.3% interest. Petron refines crude oil and markets and distributes refined petroleum products in the Philippines and Malaysia. In the Philippines, Petron is the largest integrated oil refining and marketing company, with an overall market share of 38.5% of the Philippine oil market in terms of sales volume based on industry data from the Department of Energy of the Philippines (“DOE”) as of December 31, 2012. Petron had a 16.6% share of the Malaysian retail market as of December 31, 2012, according to Metrix Research estimates, the market research consultant appointed by Malaysian retail market participants to compile industry data.

Energy

The energy business of SMC is one of the leaders in the Philippine power generation industry in terms of installed capacity. The energy business of SMC is conducted through SMC Global Power. SMC administers three power plants, located in Sual, Pangasinan (coal-fired), Ilijan, Batangas (natural gas) and San Roque, Pangasinan (hydroelectric), with a combined capacity of 2,545 MW, pursuant to Independent Power Producer Administration (“IPPA”) agreements with the Power Sector Assets and Liabilities Management Corporation (“PSALM”) and National Power Corporation of the Philippines (“NPC”). As of December 31, 2012, SMC was one of the largest IPPAs in the Philippines and held a 22% market share of the total installed power generation capacity for the Luzon power grid and a 17% market share of the national grid according to the Energy Regulatory Commission of the Philippines (the “ERC”). As of December 31, 2012, SMC also owned a 32.04% stake in Meralco, the biggest power distributor and private sector utility in the Philippines, which accounted for more than half of all electricity sales in the Philippines in 2012. SMC also has interests and investments in coal, copper and gold mining.

Infrastructure

The infrastructure business of SMC consists of investments in companies which hold long-term concessions in the Philippines’ infrastructure sector. Current projects include the Tarlac — Pangasinan — La Union expressway (“TPLEX Tollway”), Boracay Airport and the Metro Rail Transit Line 7 (“MRT-7”) Light Rail and Road Project.

SMC, through San Miguel Holdings Corp. (“SMHC”), has a 46.5% investment in Atlantic Aurum Investment BV (“AAI”). AAI has indirect equity interests in Citra Metro Manila Tollways Corporation (“CMMTC”) and South Luzon Tollway Corporation (“SLTC”), which hold the concessions to construct, operate and maintain the Skyway and South Luzon Expressway (“SLEX”), respectively.

SMC operates with partners in its investments in most of these infrastructure concessions.

The following table sets forth the contribution of each of the businesses of SMC to its sales for the periods indicated:

	2010		2011		2012	
	Sales	%	Sales	%	Sales	%
	(P in millions, except percentages)					
Beverage	90,407	36.73	87,076	16.25	90,005	12.88
Food	80,415	32.67	89,549	16.71	95,759	13.70
Packaging	19,268	7.83	18,943	3.54	17,566	2.51
Energy	45,636	18.54	70,737	13.20	73,910	10.58
Fuel and Oil	10,383	4.22	269,116	50.23	420,269	60.14
Infrastructure	9	—	116	0.02	134	0.02
Telecom	38	0.02	238	0.04	1,225	0.18
Consolidated	<u>246,156</u>	<u>100.00</u>	<u>535,775</u>	<u>100.00</u>	<u>698,868</u>	<u>100.00</u>

SMC Strengths

SMC believes that its principal strengths include the following:

Diversified platform with broad exposure to the Philippine economy. The Philippines is the fifth largest economy in Southeast Asia (in terms of GDP in 2012) with consecutive annual positive GDP growth since 1999. The Philippines announced GDP growth of 6.6% in 2012, despite challenging global market conditions. According to IMF estimates, the Philippine economy is expected to grow at 4.8% in 2013. In addition, the Philippine population is young, comparably literate and growing, which provides the Philippine economy with favorable demographics for further growth.

As one of the Philippines' largest (by market capitalization and total assets) conglomerates, with sales equaling approximately 6.6% of the Philippine GDP and 5.0% of the Philippine gross national product ("GNP") in 2012, the SMC Group is broadly exposed to the Philippine economy through its diverse range of businesses spanning the beverage, food, packaging, fuel and oil, energy, telecommunication, infrastructure, property, mining, and airline industries. Recent acquisitions of SMC in the infrastructure, fuel and oil, and airline industries align SMC to key sectors that it believes will benefit from the forecast growth of the Philippine economy.

Market leading positions in key Philippine industries. Many of the businesses of SMC are leaders in their domestic markets.

Beverages: The domestic beer business of SMC has consistently dominated the Philippine beer market, with a market share of over 90% by volume in 2011, according to Canadean data. SMC also produces some of the most recognizable brands in the Philippine liquor market. It also has a growing non-alcoholic beverage business which produces non-carbonated ready to drink tea, fruit juices and water.

Food: San Miguel Pure Foods is a leading Philippine food company with market-leading positions in many key products and offers a broad range of high-quality food products and services to household, institutional and food service customers. San Miguel Pure Foods has some of the most recognizable brands in the Philippine food industry, including *Magnolia* for chicken, ice cream and milk products, *Monterey* for fresh and marinated meats, *Purefoods* for refrigerated processed meats and canned meats, *Star* and *Dari Crème* for margarine, *San Mig Coffee* for coffee and *B-Meg* for animal feeds.

Packaging: The packaging business of SMC is one of the largest packaging operations in the Philippines, producing glass, metal, plastic, aluminum cans, paper, flexibles, PET and other packaging products. The packaging business of SMC is the major source for packaging products for the other businesses of SMC. It also supplies its products to major multinational corporations in the Philippines and customers across the Asia-Pacific region, the United States, Africa, Australia and the Middle East.

Fuel and oil: Petron refines crude oil and markets and distributes refined petroleum products in the Philippines and Malaysia. In the Philippines, Petron is the largest integrated oil refining and marketing company, with an overall market share of 38.5% of the Philippine oil market in terms of sales volume based on industry data from the DOE as of December 31, 2012. Petron had a 16.6% share of the Malaysian retail market as of December 31, 2012, according to Metrix Research estimates, the market research consultant appointed by Malaysian retail market participants to compile industry data.

Energy: SMC is one of the largest IPPAs in the Philippines, holding a 22% market share of the total installed capacity of the Luzon power grid and a 17% market share of the national grid as of December 31, 2012 according to the ERC. SMC administers three power plants, located in Sual, Pangasinan (coal-fired), Ilijan, Batangas (natural gas) and San Roque, Pangasinan (hydroelectric), with a combined capacity of 2,545 MW. SMC and its subsidiaries also hold a 32.04% stake in Meralco, the biggest power distributor and private sector utility in the Philippines, accounting for more than half of all net electricity sales in the Philippines. The energy trading team of SMC comprises pioneers in the Wholesale Electricity Spot Market (“WESM”) trading.

Experienced management team. SMC has an extensive pool of experienced managers, and many senior managers have been with SMC for more than 20 years. The management team has a deep knowledge and understanding of the Philippine operating environment and has been able to effectively manage SMC through periods of crisis and instability in the Philippines. In addition, the management team has recently successfully directed the diversification strategy of SMC, including retaining key management personnel from acquired companies in order to maintain their expertise and leverage their industry experience. The two new businesses of SMC — Petron and SMC Global Power — have provided significant contribution to the performance of SMC for the past two years. In 2012, sales of Petron and SMC Global Power account for 60% and 11% of the total consolidated sales of SMC, respectively. Likewise, the EBITDA contribution of Petron and SMC Global Power accounted for 19% and 32%, respectively.

Operating businesses provide sustainable stream of income and cash flows. The beverage, food and packaging businesses provide SMC with a sustainable stream of income with low capital expenditure requirements. These businesses demonstrated resilience during the global financial crisis and provided SMC with a strong financial base from which to pursue its recent diversification strategy. In 2012, the beverage, food and packaging businesses provided 33%, 11% and 5% of total SMC EBITDA, respectively, and 13%, 13% and 3% of total SMC sales, respectively.

In 2010, SMC generated ₱52,536 million of EBITDA and ₱20,091 million of net income attributable to the parent company with ₱8,518 million of capital expenditure. In 2011, it generated ₱77,150 million of EBITDA and ₱17,518 million of net income attributable to the parent company with ₱26,426 million of capital expenditure. In 2012, it generated ₱78,071 million of EBITDA and ₱27,579 million of net income attributable to the equity holders of the parent company with ₱52,920 million of capital expenditure.

Platform for significant future growth. SMC is well-positioned for significant future growth. In particular, the established businesses of SMC in beverage, food and packaging provide for stable growth annually, while its new businesses are expected to contribute further to this growth.

Beverage: The beverage business of SMC is well-positioned to benefit from increasing affluence and population growth in the Philippines. SMC believes there are significant opportunities in the premium beer market as the Philippine population becomes more affluent. Additionally, the international beer business of SMC is experiencing increased sales through increasing brand recognition in selected overseas markets such as Indonesia, Thailand, Singapore and Hong Kong. SMC intends to expand its liquor business in the southern Philippines and internationally. SMC plans to create rapid deployment task forces, particularly in the southern Philippines, where market penetration is low and where there is no existing dealership system. SMC also plans to increase margins by improving the profitability of its non-alcoholic beverage business by rationalizing its sales and distribution network to reduce costs, searching for alternative raw materials and optimizing bottle cost and usage. The beverage business of SMC plans to introduce new products and new package formats to increase consumer interest and overall market size, as well as address the needs of an increasingly fragmenting market, especially in high growth segments.

Food: SMC aims to become the lowest cost producer by securing a stable raw material supply and developing cheaper alternative raw materials. SMC is also streamlining its operations to improve the profitability of its established business segments such as poultry, feeds, meat and flour, maximize synergies across operations, and improve margins through outsourcing non-core activities.

Packaging: The packaging business of SMC aims to benefit from trade liberalization and globalization in the Asian region by increasing its exports to new markets. In addition, rising environmental awareness provides opportunities for the production of more environmentally friendly products such as heavy metal-free paint glass and recycled PET resin. SMC plans to improve margins by developing alternative sources of raw materials and optimizing recycling efforts to lower its material costs.

Fuel and oil: Petron operates as an integrated oil refining and marketing company in the Philippines and Malaysia, both of which it believes have favorable oil industry dynamics. The Philippines operates under a free market scheme with movements in regional prices reflected in the pump prices on a weekly basis. Malaysia, on the other hand, operates under a regulated environment and implements an automatic pricing mechanism that provides stable returns to fuel retailers. As both the Philippines and Malaysia are importers of finished petroleum products, Petron believes it is well-positioned to benefit from this supply shortfall, giving it a significant competitive advantage against other competitors. SMC plans to continue its service station network expansion and seek growth in complementary non-fuel businesses. SMC also plans to increase the production of higher margin products. Petron is currently embarking on RMP-2, the second phase of a refinery expansion project, which includes further enhancements to the refinery's operational efficiencies, increase in conversion capability and reduction of production of lower-value fuel oils, which is expected to be completed in 2014. In addition to RMP-2 and the expansion of the service station network, Petron is constructing a new cogeneration power plant for the Limay Refinery to replace some of the Limay Refinery's existing turbo and steam generators. The new cogeneration power plant is expected to utilize more efficient technology and generate power at lower costs.

Energy: SMC is planning to expand its power generating capacity over the next five years, and believes its energy business will benefit from both growing demand for electricity in the Philippines, which is forecasted to exceed the growth rates of the Philippine GDP, and shortage in electricity supply, with the industry constrained by aging power generation assets and minimal new capacity. Also, if spot electricity rates move higher as a result of increased demand, the margins of SMC are expected to increase. SMC aims to protect its fuel supply and hedge its exposure to commodity price increases by acquiring coal and oil businesses.

Infrastructure: SMC believes there are significant opportunities in building or purchasing infrastructure assets in a growing economy that has historically under-invested in infrastructure. In addition, SMC believes its operating licenses will provide strong and stable long-term income streams, as well as serve as a barrier to entry to new entrants to the business.

Telecommunications: SMC believes its recent acquisitions in the telecommunications industry provide it with exposure to an industry that is expecting high growth as the Philippine population becomes more affluent and spends more on higher margin services. In particular, SMC is currently refining its telecommunications business strategy, where it plans to take advantage of opportunities in digitization of businesses, the emergence of mobile platforms for businesses and the provision of services to consumers. Moreover, companies recently acquired by SMC have a wide bandwidth of spectrum that would enable SMC to be competitive in both current (2G/3G/4G) and future technologies.

Potential to extract synergies across businesses. SMC believes there are significant opportunities to develop and increase synergies across many of its businesses, including:

Ancillary business opportunities: SMC believes it has opportunities within its existing businesses to secure new growth opportunities in its new businesses by using the relevant areas to conduct business and activities. Potential initiatives of this type include installing SMC Group advertisements and building service stations, retail outlets, rest stops and kiosks along toll roads.

Immediate distribution channel: The extensive retail distribution network of SMC provides an effective platform for roll-out of new products and services. For example, the network of Petron service stations provides an immediate distribution channel for retail sales for SMC beverage and food products.

Economies of scale: SMC believes the size and scale of its distribution network operations will provide significant economies of scale and synergies in production, research and development, distribution, management and marketing. The size and scale of SMC should also result in substantial leverage and bargaining power with suppliers and retailers.

Integration: SMC plans to continue pursuing vertical integration across the established and strategic businesses, such as supplying the fuel and oil and power requirements of its businesses internally.

SMC Business Strategies

The principal strategies of SMC include the following:

Enhance value of established businesses. SMC aims to enhance the value of its established businesses by pursuing operational excellence, brand enhancement, improving product visibility, targeting regions where SMC has lower market share, implementing pricing strategies and pursuing efficiencies.

Continue to diversify into industries that underpin the development and growth of the Philippine economy. In addition to organic growth, SMC intends to continue to seek strategic acquisition opportunities to position itself for the economic growth and industrial development of the Philippines.

Identify and pursue synergies across businesses through vertical integration, platform matching and channel management. SMC intends to create an even broader distribution network for its products and expand its customer base by identifying synergies across its various businesses. In addition, SMC is pursuing plans to integrate its production and distribution facilities for its established and newly acquired businesses to enable additional cost savings and efficiencies.

Invest in and develop businesses with leading market positions. SMC intends to further enhance its market position in the Philippines by leveraging its financial resources and experience to continue introducing innovative products and services. Potential investments to develop existing businesses include constructing new power plants and expanding its power generation portfolio, building additional service and micro-filling stations and expanding food distribution networks. SMC believes its strong domestic market position and brand recognition provide an effective platform to develop markets for its expanding product portfolio. SMC plans to continue to invest in and develop businesses it believes have the potential to gain leading positions in their respective markets.

Adopt world-leading practices and joint development of businesses. SMC intends to develop strategic partnerships with global industry leaders, including, for example, Kirin Holding Company, Limited (“Kirin”) in the beverages and Nihon Yamamura Glass Co. Ltd. (“NYG”) in the packaging businesses. These partnerships provide marketing and expansion opportunities, and they also potentially provide liquidity and opportunities for SMC to divest minority stakes in its businesses creating value for its shareholders.

Recent Developments

Issuance of Bonds by SMB

On April 2, 2012, SMB issued peso-denominated fixed rate bonds worth ₱20 billion. The bonds were issued at the issue price of 100.00% of face value in three series: Series D, E and F Bonds.

The Series E and F Bonds were listed on the Philippine Dealing & Exchange Corp. (“PDEX”) on April 2, 2012, and the Series D Bonds were listed on the PDEX effective October 3, 2012.

Proceeds of the offer were used by SMB to redeem the Series A fixed rate bonds amounting to ₱13.6 billion which matured on April 3, 2012 and the partial repayment of US\$150 million of the US\$300 million term facility on April 27, 2012.

Redemption of 693,500 Preferred Shares of Top Frontier Investment Holdings, Inc. (“Top Frontier”)

On June 18, 2012, Top Frontier redeemed a total of 693,500 preferred shares out of 2,598,040 preferred shares issued to SMC, at the total redemption price of ₱12,899 million, corresponding to the original issue price of such preferred shares.

The SMC Group recognized a gain of ₱945 million from the transaction.

Purchase of SMC Shares by Top Frontier and Master Year Limited (“MYL”)

On June 29, 2012, Top Frontier and MYL purchased 125,234,667 common shares and 368,140,516 common shares of SMC, respectively. The sale was transacted at the PSE through a special block sale at the price of ₱75.00 per share.

As of December 31, 2012, Top Frontier and MYL own approximately 66.30% and 15.52%, respectively, of the outstanding common stock of SMC.

Issuance of Series “2” Preferred Shares

In September 2012, SMC issued 1,067,000,000 Series “2” Preferred Shares at the issue price of ₱75.00 per share and listed the ₱80,025 million worth of Series “2” Preferred Shares on the PSE.

These Series “2” Preferred Shares were issued in three sub-series (2-A, 2-B and 2-C) and are peso-denominated, perpetual, cumulative, non-participating and non-voting.

Dividend rates per annum for are 7.5%, 7.625% and 8% for sub-series 2-A, 2-B and 2-C, respectively.

The bulk of the proceeds from the Series “2” Preferred Shares issuance was used by SMC for the redemption of its outstanding Series “1” Preferred Shares with the balance utilized for general corporate purposes, including short-term debt repayment.

Redemption of the Series “1” Preferred Shares

On October 5, 2012, SMC redeemed the Series “1” Preferred Shares at a redemption price of ₱75.00 per share, in accordance with their terms and conditions. The redemption of these preferred shares was approved by the Board of Directors of SMC on August 13, 2012.

The redemption proceeds of the Series “1” Preferred Shares amounting to ₱72,788 million and all accumulated unpaid cash dividends amounting to ₱1,458 million were paid on October 5, 2012 to the stockholders of record as of September 11, 2012.

Secondary Offering of Common Shares of San Miguel Pure Foods

On November 23, 2012, SMC completed the secondary offering of its shares in San Miguel Pure Foods following the crossing of the shares on the PSE on November 21, 2012. The offer consisted of 25,000,000 common shares, inclusive of an over-allotment of 2,500,000 common shares at a price of ₱240.00 per share.

Net proceeds from the transaction amounted to ₱5,784 million. The SMC Group recognized a net gain of ₱2,419 million from the offering.

Investment in Terramino Holdings, Inc. (“THI”) and CMMTC

On December 28, 2012, SMC, through its wholly-owned subsidiary, SMHC, completed the acquisition of 100% of the outstanding capital of THI for ₱3 million.

With the acquisition of THI, which owns 37.33% of the outstanding capital stock of CMMTC, and the existing 23.5% indirect ownership in CMMTC through AAI, SMHC obtained control and consolidated CMMTC effective December 28, 2012.

Construction of the Grains Terminal in Batangas of Golden Bay Grain Terminal Corporation (“GBGTC”)

As of December 31, 2012, GBGTC incurred ₱1,070 million for the construction of its grains terminal in Batangas. GBGTC is a wholly-owned subsidiary of San Miguel Mills, Inc. (“SMMI”), incorporated in September 2011.

Voluntary Delisting of SMPI and SMB Shares from the PSE and the Buy-back of all of their Publicly Listed Shares through a Tender Offer

On February 5, 2013 and February 15, 2013, the Board of Directors of SMPI and SMB approved and authorized the voluntary delisting of SMPI and SMB shares from the PSE and the buy-back of all their publicly listed shares through a tender offer at the price of ₱134.12 and ₱20.00 per share, respectively.

The tender offer periods for the SMPI and SMB share buy-backs were March 6, 2013 to April 5, 2013 and March 24, 2013 to April 3, 2013, respectively.

Tender Offer for US\$600 Million Exchangeable Bonds

On February 7, 2013, SMC repurchased exchangeable bonds having an aggregate principal amount of US\$259.2 million. The aggregate cash amount paid based on the aggregate principal amount of the exchangeable bonds repurchased, as well as accrued but unpaid interest payable until February 7, 2013, was US\$280.6 million.

On March 26, 2013, SMC repurchased the exchangeable bonds having an aggregate principal amount of US\$60 million. The aggregate cash amount paid based on the aggregate principal amount of the exchangeable bonds repurchased, as well as accrued but unpaid interest payable until March 26, 2013, was US\$71 million. The aggregate principal amount of the exchangeable bonds remaining outstanding following completion of the invitation to tender was US\$259 million.

Issuance of Undated Subordinated Capital Securities by Petron

On February 6, 2013 and March 11, 2013, Petron issued Undated Subordinated Capital Securities at the issue price of 100.0% amounting to US\$500 million and US\$250 million, respectively. At the option of Petron, the securities may be redeemed after five and a half years or on any distribution payment date thereafter. The proceeds were applied by Petron towards capital and other expenditures in respect of RMP-2 and used for general corporate purposes.

SUMMARY FINANCIAL INFORMATION AND OTHER DATA

Prospective purchasers of the Notes to be issued under the Programme should read the summary financial data below together with the financial statements, including the notes thereto, included in this Offering Memorandum. The summary consolidated statements of income data and consolidated statement of cash flows data for the years ended December 31, 2010, 2011 and 2012 and the summary consolidated statement of financial position data as of December 31, 2011 and 2012 are derived from the audited financial statements of SMC, including the notes thereto, which are found elsewhere in this Offering Memorandum.

The summary consolidated statements of income data and consolidated statement of cash flows data for the years ended December 31, 2010, 2011 and 2012 and the summary consolidated statement of financial position data as of December 31, 2011 and 2012 were derived from the consolidated financial statements of SMC, audited by Manabat Sanagustin & Co. and prepared in compliance with PFRS. The information below should be read in conjunction with the consolidated financial statements of SMC and the related notes thereto, which are included elsewhere in this Offering Memorandum. The historical financial condition, results of operations and cash flows of SMC are no guarantee of its future operating and financial performance.

	Years ended December 31,			
	2010	2011	2012	2012
	(P in millions)			(US\$ in millions) (unaudited)
Consolidated Statements of Income Data				
Sales	246,156	535,775	698,868	17,025
Cost of sales	173,929	432,321	594,732	14,488
Gross profit	72,227	103,454	104,136	2,537
Selling and administrative expenses	(37,619)	(47,500)	(51,353)	(1,251)
Interest expense and other financing charges	(16,578)	(27,443)	(29,826)	(727)
Interest income	3,023	4,618	4,254	104
Equity in net earnings (losses) of associates	6,817	2,824	2,691	66
Gain on sale of investments and property and equipment	529	1,046	4,549	111
Other income (charges) — net	7,095	(12)	12,981	316
Income before income tax from continuing operations	35,494	36,987	47,432	1,156
Income tax expense	(11,438)	(8,483)	(8,812)	(215)
Net income	24,056	28,504	38,620	941
Attributable to:				
Equity holders of SMC	20,091	17,518	27,579	672
Non-controlling interests	3,965	10,986	11,041	269
	24,056	28,504	38,620	941

	As of December 31,		
	2011	2012	2012
	(P in millions)		(US\$ in millions) (unaudited)
Consolidated Statements of Financial Position Data			
Assets			
Current Assets			
Cash and cash equivalents	128,975	125,631	3,060
Trade and other receivables — net	84,472	122,599	2,987
Inventories	65,720	80,222	1,954
Current portion of biological assets — net	4,124	3,792	92
Prepaid expenses and other current assets	22,620	31,612	770
	<u>305,911</u>	<u>363,856</u>	<u>8,863</u>
Assets held for sale	2,268	9,373	228
Total current assets	<u>308,179</u>	<u>373,229</u>	<u>9,091</u>
Noncurrent Assets			
Investments and advances — net	166,854	161,625	3,937
Available-for-sale financial assets	2,068	1,570	38
Property, plant and equipment — net	319,626	370,689	9,030
Investment properties — net	2,850	3,780	92
Biological assets — net of current portion	1,812	1,932	47
Goodwill — net	30,990	49,953	1,217
Other intangible assets — net	11,407	34,131	831
Deferred tax assets	8,233	8,826	215
Other noncurrent assets — net	38,517	32,228	785
Total noncurrent assets	<u>582,357</u>	<u>664,734</u>	<u>16,192</u>
Total assets	<u>890,536</u>	<u>1,037,963</u>	<u>25,283</u>
Liabilities and Equity			
Current Liabilities			
Drafts and loans payable	82,588	151,274	3,685
Accounts payable and accrued expenses	61,629	84,665	2,062
Finance lease liabilities — current portion	15,388	15,456	377
Income and other taxes payable	9,041	11,124	271
Dividends payable	2,153	3,247	79
Current maturities of long-term debt — net of debt issue costs	19,453	3,279	80
Liabilities directly associated with assets held for sale	578	—	—
Total current liabilities	<u>190,830</u>	<u>269,045</u>	<u>6,554</u>
Noncurrent Liabilities			
Long-term debt — net of current maturities and debt issue costs	191,967	220,938	5,382
Deferred tax liabilities	11,257	12,084	294
Finance lease liabilities — net of current portion	192,873	179,698	4,378
Other noncurrent liabilities	4,509	6,418	156
Total noncurrent liabilities	<u>400,606</u>	<u>419,138</u>	<u>10,210</u>
Equity			
Equity Attributable to Equity Holders of SMC			
Capital stock — common	16,397	16,408	400
Capital stock — preferred	4,852	10,187	248
Additional paid-in-capital	103,511	177,762	4,330
Revaluation increment	1,443	1,352	33
Cumulative translation adjustments	5,264	5,088	122
Retained earnings:			
Appropriated	24,315	27,219	663
Unappropriated	141,126	154,303	3,759
Treasury Stock	(67,441)	(140,124)	(3,413)
Amounts recognized directly in equity relating to assets held for sale	(53)	—	—
Total Equity Attributable to Equity Holders of SMC	<u>229,414</u>	<u>252,195</u>	<u>6,142</u>
Non-controlling interests	69,686	97,585	2,377
Total equity	<u>299,100</u>	<u>349,780</u>	<u>8,519</u>
Total liabilities and equity	<u>890,536</u>	<u>1,037,963</u>	<u>25,283</u>

	Years ended December 31,			
	2010	2011	2012	2012
	(P in millions)			(US\$ in millions) (unaudited)
Consolidated Statement of Cash Flows Data				
Net cash flows provided by operating activities	45,378	28,660	16,815	410
Net cash flows provided by (used in) investing activities	(126,995)	(66,941)	(58,030)	(1,414)
Net cash flows provided by (used in) financing activities	(2,226)	42,335	38,572	940
Effect of exchange rates changes on cash and cash equivalents	(380)	(181)	(701)	(17)
Net increase/(decrease) in cash and cash equivalents	(84,233)	3,873	(3,344)	(81)
Cash and cash equivalents at beginning of year	209,411	125,188	128,975	3,141
Cash and cash equivalents associated to assets held for sale	—	(86)	—	—
Cash and cash equivalents at end of period	125,188	128,975	125,631	3,060

OTHER FINANCIAL DATA

Calculation of EBITDA⁽¹⁾

	As of and for the years ended December 31,			
	2010	2011	2012	2012
	(P in millions)			(US\$ in millions) (unaudited)
Net income	24,056	28,504	38,620	941
Add (deduct)				
Income tax expense	11,438	8,483	8,812	215
Net financing charges				—
Interest Expense	16,578	27,443	29,826	727
Interest Income	(3,023)	(4,618)	(4,254)	(104)
Gain on sale of Investments	—	(278)	(3,854)	(94)
Other charges (income)	(4,490)	—	—	—
Foreign exchange losses (gains)	(6,097)	823	(11,375)	(277)
Marked-to-market currency losses (gains)	(122)	(689)	1,313	32
Depreciation and amortization and impairment	<u>14,196</u>	<u>17,482</u>	<u>18,983</u>	<u>462</u>
EBITDA	52,536	77,150	78,071	1,902

(1) EBITDA is a measure used by the management of SMC to internally evaluate the performance of its businesses. EBITDA is calculated as net income before: income tax expense, net financing charges (interest income net of interest expense), extraordinary or exceptional items, foreign exchange losses (gains), marked-to-market currency losses (gains) and depreciation and amortization and impairment losses. EBITDA is not a measure determined in accordance with PFRS, and prospective investors should not consider EBITDA as an alternative to net income as a measure of operating performance or to cash flow as a measure of free cash flow for management's discretionary use, as it does not reflect certain cash requirements such as interest payments, tax payments and capital expenditures. The calculation of EBITDA of SMC may be different from the calculations used by other companies, and, as a result, the EBITDA of SMC may not be comparable to other similarly titled measures of other companies.

Calculation of Consolidated Total Indebtedness

	Years ended December 31,	
	2011	2012
	(P in millions)	
Drafts and loans payable	82,588	151,274
Current maturities of long-term debt	19,453	3,279
Long-term debt	<u>191,967</u>	<u>220,938</u>
Consolidated total indebtedness	<u>294,008</u>	<u>375,491</u>

SUMMARY OF THE PROGRAMME

The following summary is qualified in its entirety by the remainder of this Offering Memorandum. This summary must be read as an introduction to this Offering Memorandum and any decision to invest in the Notes should be based on a consideration of the Offering Memorandum as a whole, including any information incorporated by reference. Phrases used in this summary and not otherwise defined shall have the meanings given to them in “Terms and Conditions of the Notes.”

Issuer:	San Miguel Corporation.
Description:	Medium Term Note Programme.
Size:	Up to US\$2,000,000,000 (or the equivalent in other currencies at the date of issue) aggregate nominal amount of Notes outstanding at any one time. The Issuer may increase the aggregate nominal amount of the Programme in accordance with the terms of the Programme Agreement.
Arrangers:	Australia and New Zealand Banking Corporation Limited and Standard Chartered Bank.
Dealers:	<p>Australia and New Zealand Banking Corporation Limited, DBS Bank Ltd., Deutsche Bank AG, Singapore Branch, Merrill Lynch (Singapore) Pte. Ltd, Standard Chartered Bank and any other Dealer appointed in accordance with the Programme Agreement (as defined under “<i>Subscription and Sale</i>”).</p> <p>The Issuer may from time to time terminate the appointment of any dealer under the Programme or appoint dealers either in respect of one or more Tranches or in respect of the whole Programme. References in this Offering Memorandum to “Dealers” are to all persons appointed as a dealer in respect of one or more Tranches or the Programme.</p>
Certain Restrictions:	<p>Each issue of Notes denominated in a currency in respect of which particular laws, guidelines, regulations, restrictions or reporting requirements apply will only be issued in circumstances which comply with such laws, guidelines, regulations, restrictions or reporting requirements from time to time (see “<i>Subscription and Sale</i>”) including the following restriction applicable at the date of this Offering Memorandum.</p> <p>Notes having a maturity of less than one year</p> <p>Notes having a maturity of less than one year will, if the proceeds of the issue are accepted in the United Kingdom, constitute deposits for the purposes of the prohibition on accepting deposits contained in section 19 of the Financial Services and Markets Act 2000 (“FSMA”) unless they are issued to a limited class of professional investors and have a denomination of at least £100,000 or its equivalent, see “<i>Subscription and Sale</i>.”</p>
Trustee:	DB Trustees (Hong Kong) Limited.
Principal Paying Agent, Paying Agent, CMU Lodging Agent, Registrar and Transfer Agent:	Deutsche Bank AG, Hong Kong Branch.
Method of Issue:	The Notes will be issued on a syndicated or non-syndicated basis. The Notes will be issued in series (each a “Series”) having one or more issue dates and on terms otherwise identical (or identical other than in respect of the first payment of interest and/or the issue price), the Notes of each Series being intended to be interchangeable with all other Notes of that Series. Each Series may be issued in tranches (each a “Tranche”) on the same or different issue dates. The specific

	<p>terms of each Tranche (which will be completed, where necessary, with the relevant terms and conditions and, save in respect of the issue date, issue price, first payment of interest and nominal amount of the Tranche, will be identical to the terms of other Tranches of the same Series) will be completed in the pricing supplement (the “Pricing Supplement”).</p>
Issue Price:	<p>Notes may be issued at their nominal amount or at a discount or premium to their nominal amount. Partly Paid Notes may be issued, the issue price of which will be payable in two or more installments.</p>
Form of Notes:	<p>The Notes will be issued in bearer or registered form as described in “Form of the Notes”. Registered Notes will not be exchangeable for Bearer Notes and vice versa.</p>
Clearing Systems:	<p>Clearstream, Euroclear, the CMU and, in relation to any Tranche, such other clearing system as may be agreed between the Issuer, the Principal Paying Agent, the Trustee and the relevant Dealer.</p>
Initial Delivery of Notes:	<p>On or before the issue date for each Tranche, the Global Note representing the Notes may be deposited with a common depositary for Euroclear and Clearstream or deposited with a sub-custodian for the CMU. Global Notes may also be deposited with any other clearing system or may be delivered outside any clearing system provided that the method of such delivery has been agreed in advance by the Issuer, the Trustee, the Principal Paying Agent and the relevant Dealer. Registered Notes that are to be credited to one or more clearing systems on issue will be registered in the name of, or in the name of nominees or a common nominee for, such clearing systems.</p>
Currencies:	<p>Subject to compliance with all relevant laws, regulations and directives, Notes may be issued in any currency agreed between the Issuer and the relevant Dealers.</p>
Maturities:	<p>Subject to compliance with all relevant laws, regulations and directives, any maturity as may be agreed between the Issuer and the relevant Dealer(s).</p>
Specified Denomination:	<p>Notes will be issued in such denominations as may be agreed between the Issuer and the relevant Dealer save that the minimum denomination of each Note will be such as may be allowed or required from time to time by the central banks (or equivalent body) or any laws or regulations applicable to the relevant currency (see “Certain Restrictions” above). Notes offered in a Member State of the European Economic Area must have a minimum denomination of €100,000 (or equivalent) in order to benefit from the exemption set out in Article 3.2(d) of the Prospectus Directive as implemented in that Member State.</p>
Fixed Rate Notes:	<p>Fixed interest will be payable in arrear on such date or dates as may be agreed between the Issuer and the relevant Dealer and on redemption and will be calculated on the basis of such Day Count Fraction as may be agreed between the Issuer and the relevant Dealer.</p>
Floating Rate Notes:	<p>Floating Rate Notes will bear interest determined separately for each Series as follows:</p> <ul style="list-style-type: none"> (i) on the same basis as the floating rate under a notional interest rate swap transaction in the relevant Specified Currency governed by an agreement incorporating the 2006 ISDA Definitions (as published by the International Swaps and Derivatives Association, Inc. and as amended and updated as at the Issue Date of the first Tranche of the Notes of the relevant Series); or

	<p>(ii) on the basis of a reference rate appearing on the agreed screen page of a commercial quotation service; or</p> <p>(iii) on such other basis as may be agreed between the Issuer and the relevant Dealer.</p> <p>Interest periods will be specified in the relevant Pricing Supplement.</p>
Zero Coupon Notes:	Zero Coupon Notes may be issued at their nominal amount or at a discount to it and will not bear interest.
Dual Currency Notes:	Payments (whether in respect of principal or interest and whether at maturity or otherwise) in respect of Dual Currency Notes will be made in such currencies, and based on such rates of exchange as the Issuer and the relevant Dealer may agree and as may be specified in the relevant Pricing Supplement.
Index Linked Notes:	Payments of principal in respect of Index Linked Redemption Notes or of interest in respect of Index Linked Interest Notes will be calculated by reference to such index and/or formula or to changes in prices of securities or commodities or to such other factors as the Issuer and the relevant Dealer may agree and as may be specified in the relevant Pricing Supplement.
Interest Periods and Interest Rates:	The length of the interest periods for the Notes and the applicable interest rate or its method of calculation may differ from time to time or be constant for any Series. Floating Rate Notes and Index Linked Interest Notes may also have a maximum interest rate, a minimum interest rate, or both. The use of interest accrual periods permits the Notes to bear interest at different rates in the same interest period. All such information will be set out in the relevant Pricing Supplement.
Redemption:	<p>The applicable Pricing Supplement will indicate either that the relevant Notes cannot be redeemed prior to their stated maturity (other than in specified installments, if applicable, or for taxation reasons or following an Event of Default) or that such Notes will be redeemable at the option of the Issuer and/or the Noteholders upon giving notice to the Noteholders or the Issuer, as the case may be, on a date or dates specified prior to such stated maturity and at a price or prices and on such other terms as may be agreed between the Issuer and the relevant Dealer.</p> <p>The applicable Pricing Supplement may provide that Notes may be redeemable in two or more installments of such amounts and on such dates as are indicated in the applicable Pricing Supplement.</p> <p>Notes having a maturity of less than one year are subject to restrictions on their denomination and distribution, see “Certain Restrictions — Notes having a maturity of less than one year” above.</p>
Redemption upon Change of Control or Disposal Event:	The terms of the Notes will contain a provision for the early redemption of the Notes at the option of the holders thereof upon the occurrence of a Change of Control or, as the case may be, Disposal Event as further described in Condition 7.5 (<i>Redemption upon a Change of Control</i>) and Condition 7.6 (<i>Redemption upon Disposal Event</i>).
Status of the Notes:	The Notes and any relative Receipts and Coupons are direct, unconditional, unsubordinated and (subject to the provisions of Condition 4.1) unsecured obligations of the Issuer and rank <i>pari passu</i> among themselves, with all other outstanding unsecured and unsubordinated obligations of the Issuer, present and future, but, in the event of insolvency, only to the extent permitted by applicable laws relating to creditors’ rights.

Under Philippine law unsecured debt of a borrower in insolvency or liquidation that is documented by a public instrument, as provided in Article 2244(14) of the Civil Code of the Philippines, ranks ahead of unsecured debt that is not so documented. Debt is treated as documented by a public instrument if it is acknowledged before a notary or any person authorized to administer oaths in the Philippines. The Issuer's debt which is documented by a public instrument contains an explicit waiver by the parties thereto of the preference or priority created, as provided in Article 2244(14) of the Civil Code of the Philippines, and will rank pari passu with the Notes.

Negative Pledge:

The Notes will contain a negative pledge provision as described in Condition 4.1.

Covenants:

The Issuer has agreed in the Trust Deed constituting the Notes and the Terms and Conditions of the Notes related thereto to observe certain covenants, including, among other things, limitation on Indebtedness, limitation on dividend and other payment restrictions affecting Material Subsidiaries and certain other covenants. These covenants and other restrictions are subject to important qualifications and exceptions. See Condition 4 of “*Terms and Conditions of the Notes.*”

Cross Default:

The Conditions will contain a cross default provision as described in Condition 10.

Ratings:

Notes issued under the Programme may be rated or unrated. Where an issue of Notes is to be rated, such rating will be specified in the relevant Pricing Supplement.

A rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, reduction or withdrawal at any time by the assigning rating agency.

Withholding Tax:

All payments of principal and interest in respect of the Notes will be made free and clear of withholding taxes of the Philippines unless the withholding is required by law. In that event, the Issuer will, save in limited circumstances as provided in Condition 8, pay such additional amounts as will result in the Noteholders receiving such amounts as they would have received in respect of such Notes had no such withholding been required.

Governing Law:

The Notes and the Trust Deed and any non-contractual obligations arising out of or in connection with the Notes or the Trust Deed will be governed by, and construed in accordance with, English law.

Listing and Admission to Trading:

Approval in-principle has been granted by the SGX-ST for permission to deal in and quotation of any Notes which are agreed at the time of issue thereof to be so listed on the SGX-ST. Such permission will be granted when such Notes have been admitted to the Official List of the SGX-ST. There is no assurance that the application to the Official List of the SGX-ST will be approved. If the application to the SGX-ST to list a particular series of Notes is approved, such Notes listed on the SGX-ST will be traded on the SGX-ST in a board lot size of at least US\$200,000 (or its equivalent in other currencies).

Unlisted Series of Notes may also be issued pursuant to the Programme. The Notes may also be listed on such other or further stock exchange(s) as may be agreed between the Issuer and the relevant Dealer in relation to each series of Notes. The Pricing Supplement relating to each Series of Notes will state whether or not the Notes of such Series will be listed on any stock exchange(s) and, if so, on which stock exchange(s) the Notes are to be listed.

Selling Restrictions:

There are restrictions on the offer, sale and transfer of the Notes in the United States, the European Economic Area (including the United Kingdom), Japan, Hong Kong, the Philippines, Singapore, the Netherlands and the People's Republic of China and such other restrictions as may be required in connection with the offering and sale of a particular Tranche of Notes, see "*Subscription and Sale*."

United States Selling Restrictions:

Regulation S (Category 1/Category 2), TEFRA C, TEFRA D or TEFRA not applicable, as specified in the applicable Pricing Supplement.

RISK FACTORS

SMC believes that the following factors may affect its ability to fulfil its obligations under the Notes. Most of these factors are contingencies which may or may not occur and SMC is not in a position to express a view on the likelihood of any such contingency occurring.

In addition, factors which are material for the purpose of assessing the market risks associated with the Notes are described below.

SMC believes that the factors described below represent the principal risks inherent in investing in the Notes, but the inability of SMC to pay interest, principal or other amounts on or in connection with the Notes may occur for other reasons which may not be considered significant risks by SMC based on information currently available to it or which it may not currently be able to anticipate. Prospective investors should also read the detailed information set out elsewhere in this Offering Memorandum and reach their own views prior to making any investment decision.

Risks Relating to SMC and the SMC Group

Risks associated with diversification of businesses and acquisition of new businesses

The traditional businesses of SMC comprise primarily beverage, food and packaging products. SMC has embarked on a diversification strategy and has expanded into a number of new businesses, including fuel and oil, energy, infrastructure, mining, telecommunications, airline and other businesses outside of its traditional businesses. SMC has implemented this strategy through a series of acquisitions and investments and intends to continue to pursue its diversification strategy. SMC intends to make further acquisitions and investments to enhance its product and brand portfolio and realize other strategic and cost benefits.

The diversification strategy of SMC involves a number of risks and challenges, including the substantial financial investments required to implement this strategy, diversion of management's time and resources to focus on implementing the strategy and managing a broader scope of businesses and risks inherent in making new acquisitions and investments. Growth through acquisitions involves business risks, including unforeseen contingent risks, latent business liabilities and other challenges that may only become apparent after the acquisition is finalized, such as the successful integration and management of the acquired business by SMC, retention of key personnel, joint sales and marketing efforts, management of a larger business and diversion of management's attention from other ongoing business matters. In addition, there is no assurance that SMC will achieve the anticipated benefits, expected returns, strategic benefits or synergies of an acquisition, or that SMC will be as successful in new businesses as it has been in its traditional businesses. Failure to successfully implement its diversification strategy, to integrate acquired businesses or to realize the anticipated benefits of acquisitions or investments could materially and adversely affect the business, financial condition, results of operations and prospects of SMC.

Ability of the largest shareholders to influence corporate actions

Top Frontier and MYL are the major shareholders of SMC and hold approximately 66.3% and 15.5% of the common shares of SMC, respectively, and collectively control approximately 81.8% of the voting rights of the common shares as of December 31, 2012. Top Frontier and MYL are able to influence the businesses of SMC through their ability to vote on corporate actions that require Board and shareholder approval. Top Frontier and MYL are not obligated to provide SMC with financial support. There can be no assurance that Top Frontier and MYL will influence SMC to pursue actions that are in the best interests of the Noteholders.

Possible disagreements among joint venture partners of SMC

The businesses of some of the subsidiaries and associates of SMC are conducted through joint ventures with other partners, including Kirin for beer, Hormel Foods Corporation for processed meats, and NYG for various packaging products. Cooperation among the joint venture partners on business decisions is crucial to the sound operation and financial success of these joint venture companies. Although SMC believes it maintains good relationships with its joint venture partners, there is no assurance that these relationships will be sustained in the future or that problems will not develop. For example, the joint venture partners of SMC may be unable or unwilling to fulfill their obligations, take actions contrary to its policies or objectives, or may experience financial difficulties. If any of these events occur, the businesses of these joint ventures could be severely disrupted, which could have a material adverse effect on the financial condition and results of operations of SMC.

Dependence on trademarks and proprietary rights

The SMC Group uses various brand names and trademarks, including *San Miguel*, *Ginebra San Miguel*, *Purefoods*, *Magnolia*, *Star*, *Dari Cream*, *B-Meg*, *Petron*, *Gasul* and other intellectual property rights to prepare, package, advertise, distribute and sell its products for its various businesses. Protection of those brands and intellectual property rights is important to maintaining the distinctive corporate and market identities of the SMC Group. If third parties sell products which use counterfeit versions of SMC Group brands or otherwise look like SMC Group brands, consumers may confuse SMC Group products with products that they consider to be inferior. This could negatively affect the brand image and sales of the SMC Group, particularly in the beverage and food businesses. In addition, the SMC Group has been granted numerous trademark registrations covering its brands and products, and has filed, and expects to continue to file, trademark applications seeking to protect newly developed brands and products.

There is no assurance that third parties will not challenge, invalidate or circumvent any existing or future trademarks issued to, or licensed by, the SMC Group. Any failure to protect the proprietary rights of the SMC Group could severely harm the competitive position of the SMC Group, which could materially and adversely affect the business, financial condition, results of operations and prospects, as well as reputation, of the SMC Group. In addition, certain of the intellectual property rights of the SMC Group are licensed and there is no assurance that the relevant licensors will offer to renew the licenses on terms acceptable to the SMC Group or at all. The failure to renew one or more of its material licenses could have a material adverse effect on the ability of the SMC Group to market certain products and on results of operations of the SMC Group.

Manpower complement

Any loss of key personnel, and an inability on the part of the SMC Group to replace such personnel and to train and retain replacement personnel, could materially and adversely affect the ability of the SMC Group to provide products and services to its customers. Continued losses of trained personnel could also result in the SMC Group incurring additional expenses in hiring and training replacement personnel in a competitive job market, and it may take time for these new personnel to reach the level of technical skill and expertise of the personnel they are replacing. In addition, the SMC Group has relied and will continue to rely significantly on the continued individual and collective contributions of its senior management team. If any key personnel of SMC Group are unable or unwilling to continue in their present positions, or if they join a competitor or form a competing business, the SMC Group may not be able to replace them easily, and its business may be significantly disrupted. Any of the foregoing could have a material adverse effect on the business, financial condition and results of operations of the SMC Group.

Labor disruptions

As of December 31, 2012, approximately 28.0% of the employees of the SMC Group were parties to various collective bargaining agreements between SMC and 39 labor unions within the businesses of the SMC Group.

Although the SMC Group has not experienced any strikes, work stoppages or other labor disruptions since 2003, the businesses of SMC have faced labor disruptions in the past. While the SMC Group considers its labor relations to be good, there is no assurance that it will not experience future labor disruptions to its operations due to disputes or other issues with its employees, which could materially and adversely affect its business, financial condition and results of operations.

Changes in the legal and regulatory environment

The businesses and operations of the SMC Group are subject to a number of national and local laws, rules and regulations governing several different industries in the Philippines and other countries where it conducts businesses.

The energy business of SMC, which is conducted through its wholly owned subsidiary, SMC Global Power, is subject to extensive regulation in the Philippines, including the Electric Power Industry Reform Act of 2001 (“EPIRA”). As of December 31, 2012, several bills relevant to the power industry have been filed with both houses of the Congress of the Philippines. Some of the proposed bills, if enacted, would impose additional costs on SMC Global Power, including by requiring direct remittances to local government units of financial benefits set aside for host communities and by redefining the term “host communities” to include all areas that protect and maintain the watersheds that supply a particular dam or hydroelectric power generation facility. Several bills proposing amendments to EPIRA have also been filed, some of which would include changes to the ability of power generators and distributors to pass on costs or allowable system losses to end-users. The enactment and implementation of any such bills or amendments to EPIRA, or other changes to Philippine laws and regulations

relevant to the power industry, could have a material adverse effect on the business, financial condition and results of operations of SMC Global Power, or on the rules and regulations governing the power industry, which could materially reduce its sales and profitability.

The operations of SMC are also subject to various taxes, duties and tariffs. For example, import duties for crude oil and petroleum products for Petron were increased on January 1, 2005 from 3.0% to 5.0% and then decreased back to 3.0% effective as of November 1, 2005. These duties were subsequently reduced to 0% with effect from July 4, 2010 (except for certain types of aviation gas). The Philippine government imposed an additional 12.0% value added tax (“VAT”) on the sale or importation of petroleum products in 2006. Therefore, there is no assurance that taxes applicable to SMC will not be increased again in the future.

As of January 1, 2013, the excise tax rates applicable to SMB products were ₱15.00 per liter (for those with net retail price per liter of ₱50.60 or less) and ₱20.00 per liter (for those with a net retail price per liter of more than ₱50.60). As of the same date, the excise tax rate applicable to Ginebra products was 15% of the net retail price per proof plus ₱20.00 per proof liter. The beer and liquor businesses of SMC, which are conducted through SMB and Ginebra, became subject to higher excise taxes starting in 2013. SMB and Ginebra may be unable to fully pass on to customers any increase in excise taxes, which may adversely affect profit margins.

In addition, the Philippine government may periodically implement measures aimed at protecting consumers from rising prices, which may constrain the ability of the SMC Group to pass on price increases to distributors who sell its products, as well as its customers. Implementation of any such measures could have a material adverse effect on the business, financial condition and results of operations of the SMC Group.

While the SMC Group believes that it has at all relevant times materially complied with all applicable laws, rules and regulations, there is no assurance that changes in laws, rules or regulations or the interpretation thereof, will not result in the SMC Group having to incur substantial additional costs or capital expenditures to upgrade or supplement its existing facilities or being subject to an increased rate of taxation or fines and penalties.

Exposure to safety, health and environmental costs and liabilities

The businesses of the SMC Group span several industries and are subject to a variety of laws, rules and regulations that impose limitations, prohibitions and standards with respect to health and safety as well as the use, discharge, emission, treatment, release, disposal and management of, regulated materials and waste, and hazardous substances. Safety, health and environmental laws and regulations in the Philippines have become increasingly stringent and it is possible that these laws and regulations will become significantly more stringent in the future. The adoption of new safety, health and environmental laws and regulations, new interpretations of existing laws, increased governmental enforcement of environmental laws or other developments in the future may require additional capital expenditures or the incurrence of additional operating expenses in order to comply with such laws and to maintain current operations as well as any costs related to fines and penalties.

Furthermore, if the measures implemented by the SMC Group to comply with these laws and regulations are not deemed sufficient by governmental authorities, compliance costs may significantly exceed current estimates. If the SMC Group fails to meet safety, health and environmental requirements, it may be subject to administrative, civil and criminal proceedings by governmental authorities, as well as civil proceedings by environmental groups and other individuals, which could result in substantial fines and penalties against the SMC Group, as well as orders that could limit or halt its operations. There is no assurance that the SMC Group will not become involved in future litigation or other proceedings or be held responsible in any such future litigation or proceedings relating to safety, health and environmental matters in the future, the costs of which could be material. Environmental compliance and remediation costs at sites on which its facilities are located and related litigation and other proceedings could materially and adversely affect the cash flow, results of operations and financial condition of SMC.

Availability of raw materials

The products and businesses of the SMC Group, specifically the food, beverage, packaging, fuel and oil and energy businesses, depend on raw materials. Most of these raw materials, including some critical raw materials, are procured from third parties. These raw materials are subject to price volatility caused by a number of factors, including changes in global supply and demand, foreign exchange rate fluctuations, weather conditions and governmental controls.

For example, the recent decrease in the supply of global crops has contributed, and may continue to contribute to, higher prices for wheat, malted barley and adjuncts for beer and molasses for liquor, which are among the most important raw materials for the flour and beverage businesses. The beverages operations also depend heavily on the supply of water. Although the beer business uses its own deep wells for water at several breweries, it is still reliant on a third party source for the Polo brewery.

Additionally, the food business may also face disruptions in the supply of major raw materials. For example, there was insufficient local supply of cassava in 2012 due to adverse weather conditions in the Philippines in the latter part of 2011, which prompted some farmers to switch to planting corn rather than cassava for the next cycle. As a result, San Miguel Pure Foods had to purchase and use a greater quantity of higher cost raw materials such as corn.

The packaging business of the SMC Group also needs to obtain sufficient quantities of quality raw materials, including glass, aluminum, paper, plastics and composites in a timely manner and requires a significant amount of electricity in order to maintain its operations.

San Miguel Energy Corporation (“SMEC”), entered into a coal supply contract with PT Bumi Resources Tbk (“Bumi Resources”), Noble Resources Pte. Ltd. and Banpu Public Company Limited Thailand. If PT Bumi Resources Tbk, Noble Resources Pte. Ltd. And Banpu Public Company Limited Thailand were to cease to perform their obligations under the coal supply contract with SMEC, the disruption of coal supply may materially affect the operations of SMEC.

The SMC Group may also face increased costs or shortages in the supply of raw materials due to the imposition of new laws, regulations or policies. For example, in Mindanao in the southern part of the Philippines, a significant portion of the population is Muslim, and consequently all of the poultry processing plants of San Miguel Pure Foods in that region are halal-certified. Legislation has been proposed to require additional halal certification for feedmills that supply poultry farms from which halal products are sourced. If this proposed legislation is enacted and implemented, certain raw materials may have to be eliminated from the poultry feeds of the SMC Group used in this region. This could increase the cost of poultry feeds and the cost of poultry production in the region, which could materially reduce net income and profitability.

Although the SMC Group actively monitors the availability and prices of raw materials, there is no assurance that these items will be supplied in adequate quantities or at the required quality to meet its needs or will not be subject to significant price fluctuations in the future. While the SMC Group may, in certain limited instances, be able to shift to alternative raw materials to produce its products, there is no assurance that it will be able to reduce its reliance on these raw materials in the future. The SMC Group may only have a limited ability to hedge against commodity prices and any hedging activities may not be as effective as planned. Moreover, market prices of raw materials could increase significantly if there are material shortages due to, among other things, competing usage, drastic changes in weather or natural disasters. There is no assurance that any increases in product costs could be passed on to consumers. As a result, any significant shortages or material increase in the market price of such raw materials could have a material adverse effect on the financial and operating performance of the SMC Group.

Changes in consumer preferences and purchasing power

The ability of the SMC Group to successfully develop and launch new products and maintain demand for existing products depends on the acceptance of such products by consumers and their purchasing power and disposable income levels, which may be adversely affected by unfavorable economic developments in the Philippines. A significant decrease in disposable income levels or consumer purchasing power in the target markets of the food and beverage businesses could materially and adversely affect the financial position and financial performance of the SMC Group. Consumer preferences may shift for a variety of reasons, including changes in culinary, demographic and social trends or leisure activity patterns. Concerns about health effects due to negative publicity regarding alcohol consumption, negative dietary effects or other factors may also affect consumer purchasing patterns of food and beverage products. If the marketing strategies of the SMC Group are not successful or do not respond timely or effectively to changes in consumer preferences, the business and prospects of the SMC Group could be materially and adversely affected.

For example, sales of beer are tied closely to the purchasing power and disposable income levels of consumers. In periods of economic uncertainty or downturns, consumers may purchase more hard liquor and less beer or they may purchase fewer alcoholic beverages, either of which could affect the financial performance of SMB. Demand for many of the food products of San Miguel Pure Foods is tied closely to the purchasing power of consumers.

Ability of subsidiaries and associates to distribute dividends

SMC is a holding company that conducts all of its operations through its subsidiaries and associates. As a holding company, the sales of SMC are derived from, among other sources, dividends paid to SMC by its subsidiaries and associates. SMC is reliant on such sources of funds with respect to its obligations and in order to finance its subsidiaries. The ability of the direct and indirect subsidiaries and associates of SMC to pay dividends

to their shareholders (including SMC) is subject to the performance and cash flow requirements of such subsidiaries and associated companies and to applicable law and may be subject to restrictions contained in loans and/or debt instruments of such subsidiaries and may also be subject to the deduction of taxes.

Any restriction or prohibition on the ability of some or all of the subsidiaries or associates of SMC to distribute dividends or make other distributions to SMC, either resulting from regulatory restrictions, debt covenants, operating difficulties or other limitations, could have a negative effect on the cash flow and therefore its financial condition and results of operations of SMC.

Foreign exchange risk

A substantial portion of the sales of the SMC Group is denominated in Philippine Pesos, while a substantial portion of its expenses, including raw materials, crude oil purchases and foreign currency denominated debt service costs, are denominated in U.S. dollars. Moreover, as of December 31, 2010, 2011 and 2012, the percentage of outstanding debt of SMC that was denominated in foreign currencies was 67.0%, 73.7% and 70.2%, respectively.

In addition, the financial reporting currency of SMC is the Philippine Peso, and therefore depreciation of the Philippine Peso would result in an increase the foreign currency denominated expenses of SMC as reflected in its Philippine Peso financial statements, and could also result in foreign exchange losses resulting from the revaluation of foreign currency denominated assets and liabilities, including increases in the Philippine Peso amounts of the foreign currency denominated debt obligations of SMC, thereby adversely affecting its results of operations and financial condition. In addition, there is no assurance that SMC could increase its Peso-denominated product prices to offset increases in costs resulting from any depreciation of the Philippine Peso.

While SMC uses a combination of natural hedges, which involve holding U.S. dollar-denominated assets and liabilities, and derivative instruments to manage its exchange rate risk exposure, its exchange rate exposures are not fully protected. There is no assurance that the value of the Philippine Peso will not decline or continue to fluctuate significantly against the U.S. dollar and any significant future depreciation of the Philippine Peso could have a material adverse effect on the margins, results of operations and financial condition of SMC.

In addition, changes in currency exchange rates may result in significantly higher domestic interest rates, liquidity shortages and capital or exchange controls. This could result in a reduction of economic activity, economic recession, sovereign or corporate loan defaults, lower deposits and an increased cost of funds. The occurrence of any of the foregoing events could have a material adverse effect on the businesses, financial condition, liquidity and results of operations of SMC.

Availability of financing

The expansion and growth plans of the SMC Group are expected to be funded through a combination of internally generated funds and external fund raising activities, including debt and equity financing. The continued access of the SMC Group to debt and equity financing as a source of funding for new projects and acquisitions and for refinancing maturing debt is subject to many factors including: (i) Philippine regulations limiting bank exposure (including single borrower limits) to a single borrower or related group of borrowers; (ii) SMC's compliance with existing debt covenants; (iii) the ability of SMC, its affiliates and subsidiaries to service new debt, (iv) perceptions in the capital markets regarding SMC and the industries in which it operates and other factors, some of which may be outside of its control, including general conditions in the debt and equity capital markets, many of which are outside of its control. For example, political instability, an economic downturn, social unrest, or changes in the Philippine regulatory environment could increase the cost of borrowing of the SMC Group or restrict its ability to obtain debt financing. There is no assurance that the SMC Group will be able to arrange financing on acceptable terms, if at all. Any inability of the SMC Group to obtain financing from banks and other financial institutions or from capital markets would adversely affect the ability of the SMC Group to execute its expansion and growth strategies as well as its financial condition and prospects.

Uninsured losses

The SMC Group may not be fully insured against, and insurance may not be available for, unexpected losses caused by natural disasters, breakdowns or other events that could affect the facilities and processes used by its businesses. Any unexpected losses caused by such events against which it is not fully insured could have a material adverse effect on its businesses, financial condition and results of operations. Any accident at the operations of the SMC Group facilities could result in significant losses. It could suffer a decline in production, receive adverse publicity and be forced to invest significant resources in addressing such losses. There is no assurance that there will not be work-related or other accidents in the future. Furthermore, there is no assurance

that amicable settlements will be secured in the future or that accidents will not result in future litigation or regulatory action against the SMC Group. Such events could materially and adversely affect its financial condition and results of operations.

Outsourcing

SMC outsources most of its beverage, food and packaging manufacturing, production and distribution operations to third party contractors. To ensure the timely production and distribution of its products, the SMC Group continuously monitors the efficiency and manufacturing capabilities of the relevant production facilities. However, from time to time, any of them could experience operational issues that could cause production shortages and distribution delays. If one or more of the contract manufacturers, facility operators or distributors of SMC fails to or is unable to manufacture, produce or distribute products in a timely manner, in sufficient quantities or at satisfactory quality levels, its ability to bring products to the market and its reputation could suffer, which could have a material adverse effect on the businesses and financial performance of SMC, as well as its prospects. In addition, there is no assurance that it will continue to find new contract manufacturers or distributors in line with increased customer demand in the future, which could materially and adversely affect the business and prospects of SMC.

Disruption of operations

The facilities and operations of the SMC Group could be severely disrupted by many factors, including accidents, breakdown or failure of equipment, interruption in power supply, human error, natural disasters and other unforeseen circumstances and problems. For example, San Miguel Pure Foods decided to cease operations at its Marikina plant after it was severely damaged as a result of typhoon “Ondoy” affecting Metro Manila in September 2009. As a result of this closure, and the consequent transfer of production capacities to a Cavite plant and other third party contracted plants, San Miguel Pure Foods was unable to meet volume demand during the relevant period, and its sales were adversely affected during the fourth quarter of 2009. These disruptions could result in product run-outs, facility shutdown, equipment repair or replacement, increased insurance costs, personal injuries, loss of life and unplanned inventory build-up, all of which could have a material adverse effect on the business, financial condition and results of operations of the SMC Group.

Risks Relating to the SMC Beverage Business

Price elasticity of SMB products

The substantial majority of beer drinkers in the Philippines belong to the lower socio-economic classes, where discretionary income is limited. Accordingly, the beer market in the Philippines is highly price elastic. If SMB raises the prices of its products, sales volumes will likely decline or slow down which may result in a lower level of net sales. The price increases in 2011 and 2012 and the sluggish global economy resulted in a slowdown of sales volume growth to approximately 0.4% in 2012 compared to 1.4% in 2011. Price elasticity of demand for products may limit the ability of SMB and Ginebra to pass on increases in excise taxes, raw material costs or other expenses, which may negatively affect the financial results and financial performance of the beverage business.

Increases in excise tax

Alcoholic products, such as beer and other liquor products, are subject to excise taxes, and increases in excise taxes or value added taxes may reduce overall consumption of the products of the beverage business or the profit margins of the beverage business or both. In 2005, the Government raised the excise tax on alcoholic products in the Philippines and set out a schedule for the additional increase by 8% every two years until 2011. Previous increases in excise tax rates have adversely affected the sales volume of the beverage business of SMC.

On December 20, 2012, Republic Act No. 10351 was enacted. This law became effective on January 1, 2013, restructuring the excise taxes on alcohol products in the Philippines and increasing taxes on fermented liquor and distilled spirit products. Although the full effect of Republic Act No. 10351 on the beverage business cannot be fully determined, such additional increases in excise tax may (i) reduce consumption of the beer and liquor products of the beverage business if passed on to the consumers by way of upward price adjustments, (ii) reduce the margins of the beverage business if prices remain unchanged or (iii) have both such effects if additional taxes are not fully passed on to consumers.

Competition in the beverage business

The Philippine alcoholic beverage industry in general is highly competitive, and, while SMB believes that it has the largest market share in the Philippines with respect to beer, SMB cannot assure prospective investors that it

will be able to maintain its current market share for beer, or that it will be able to increase its market share in the future. SMB faces competition from another domestic producer, which sells both its own brand and foreign brands it produces under license, and from foreign brewers. The beverage business also competes with producers of other alcoholic beverages, primarily gin, brandy and recently, alcopops which are close substitutes to beer. In the beer industry, and more generally the alcoholic beverage industry, competitive factors generally include price, product quality, brand awareness and loyalty, distribution coverage, and the ability to respond effectively to shifting consumer tastes and preferences. SMB also competes with other discretionary items, including both other food and beverage products and other goods and services in general. The consolidation of the competitors of SMB, the entrance of a new, larger competitor into the Philippine market, or unanticipated actions or irrational behavior by existing competitors, could lead to downward pressure on prices or a decline in the market share of SMB. Any such event could materially and adversely affect the financial position and financial performance of SMB.

Demand for beverage products

Although the beverage business continuously seeks to enhance the efficiency and manufacturing capabilities of its production facilities, it may, from time to time, experience production difficulties that may cause shortages and delays in deliveries, as is common in the manufacturing industry. There can be no assurance that the beverage business will not experience production difficulties in the future and SMC cannot assure prospective investors that it will be able to increase the efficiency and manufacturing capabilities of its production facilities in line with any increased customer demand in the future. Furthermore, the beverage business of SMC cannot assure prospective investors that it will be able to meet increasing demand for its products without having to incur significant additional capital expenditures in the future.

Risks Relating to the Food Business

Availability and prices of major raw materials

Many of the products and businesses of San Miguel Pure Foods depend on raw materials, most of which are procured from third parties, including purchases of some critical raw materials from both within and outside of the Philippines. These raw materials are subject to price volatility caused by a number of factors, including changes in global supply and demand, foreign exchange rate fluctuations, weather conditions and governmental controls. For example, the prices of corn and soybean meal increased by an average of 12%, based on domestic prices, and 11%, based on Chicago Board of Trade prices, respectively, in 2012 as compared to prices in 2011 due to the severe drought experienced in the United States in 2012.

San Miguel Pure Foods also may face disruptions in the supply of major raw materials. For example, there was insufficient local supply of cassava in 2012 due to adverse weather conditions in the Philippines in the latter part of 2011, which prompted some farmers to switch to planting corn rather than cassava for the next cycle. As a result, San Miguel Pure Foods had to purchase and use a greater quantity of higher cost raw materials such as corn.

Increased costs or shortages in supply of raw materials may also result from the imposition of new laws, regulations or policies. For example, in Mindanao in the southern part of the Philippines, where a significant portion of the population is Muslim, all of the poultry processing plants of San Miguel Pure Foods are halal-certified. Legislation has been proposed to require additional halal certification for feedmills that supply poultry farms from which halal products are sourced. If this proposed legislation is enacted and implemented, certain raw materials may have to be eliminated from the poultry feeds of San Miguel Pure Foods used in this region. This could increase the cost of poultry feeds and the cost of poultry production in the region, which could materially reduce net income and profitability.

There is no assurance that raw materials will be supplied in adequate quantities or at the required quality to meet the needs of San Miguel Pure Foods, or that these raw materials will not be subject to significant price fluctuations in the future. As a result, any significant shortages or material increase in the market price of such raw materials could have a material adverse effect on the financial and operating performance of San Miguel Pure Foods.

Outbreaks of animal disease

The fresh meats and poultry operations of the food business of SMC being operated by San Miguel Pure Foods are subject to risk of losses caused by outbreaks of disease at any of the hog, cattle or poultry farms that it owns or contracts. The livestock industry in the Philippines has experienced outbreaks of disease in the past. In particular, an industry-wide porcine diarrhea epidemic that affected several of the food business facilities of SMC

in the second quarter of 2008 and the third quarter of 2010 and a porcine reproductive and respiratory syndrome outbreak at contract growing facilities in the second and third quarters of 2008 negatively affected growth in the fresh meats operations during those periods.

In addition, several countries around the world have in recent years reported cases of avian influenza, or bird flu. A false positive case of avian flu in 2005 contributed to decreased growth in the Philippine poultry industry in that year. Furthermore, bird flu cases elsewhere in Asia have required producers to destroy their flocks and have restricted producers from transporting or selling their poultry. Any outbreaks could significantly decrease consumer demand for the products of the food business of SMC and severely disrupt the supply and distribution networks for its products.

There is no assurance that the policies and controls of the food business of SMC will be successful in preventing disease outbreaks or recurrences or that any actual or suspected outbreak of bird flu or any other contagious disease affecting the livestock production of the food business of SMC in the Philippines or elsewhere will not occur. Any occurrence of such events could have a material adverse effect on the financial condition and result of operations of San Miguel Pure Foods.

Competition in the food industry

The Philippine food industry is highly competitive. While San Miguel Pure Foods believes that it has the highest market share across several of its product categories, there is no assurance that San Miguel Pure Foods will be able to maintain or grow its current market share. In the food industry, competitive factors generally include price, product quality, brand awareness, distribution coverage, customer service and the ability to respond effectively to shifts in consumer tastes and preferences. Consolidation of the competitors of San Miguel Pure Foods, the entry of new, larger competitors into the Philippine food market or other actions by the competitors of San Miguel Pure Foods could exert downward pressure on prices or cause the market share of San Miguel Pure Foods to decline. Any failure by San Miguel Pure Foods to successfully compete with its competitors could have a material adverse effect on its business, financial condition, results of operations and prospects.

Importation of lower-priced products

San Miguel Pure Foods may face increased competition from less expensive imports to the Philippines as import duties on those products are decreased or eliminated. In particular, the Philippines is a signatory to several free trade agreements, including the Association of Southeast Asian Nations (“ASEAN”) Free Trade Agreement, the ASEAN-China Free Trade Agreement, the ASEAN-Korea Free Trade Area Agreement, the Japan-Philippines Economic Partnership Agreement, the ASEAN-Japan Comprehensive Economic Partnership, the ASEAN-Australia-New Zealand Free Trade Area Agreement and the ASEAN-India Free Trade Area Agreement, each of which may lead to increasingly lower-priced imported products entering the Philippine market. For example, as of January 1, 2010, import duties on certain value-added products, such as instant coffee, were reduced from 5.0% to zero for imports from other ASEAN countries. San Miguel Pure Foods has already experienced the effects of increased competition as a result of the elimination of these lower import duties, and expects that competition from imported products will continue to increase. In addition, any reduction in tariffs on imports from other ASEAN countries, such as Thailand and Vietnam, could give rise to increased competition for the products of San Miguel Pure Foods. Furthermore, there were news reports and statements by the Philippine livestock industry trade associations stating that some pork imports have been incorrectly declared for customs purposes, a practice that San Miguel Pure Foods believes escalated in the first half of 2012, with imported pork cuts such as shoulder and bellies misrepresented as offal, resulting in a tariff rate of 5% instead of either 30% or 40%. San Miguel Pure Foods believes these tariff avoidances led to substantially higher imports of frozen pork, contributing to an oversupply in the market, which resulted in lower average selling prices. Moreover, imports of pork products from China into the Philippines are currently banned under phytosanitary restrictions. If this ban were to be lifted in the future, San Miguel Pure Foods would face competition from lower-priced Chinese imports.

If San Miguel Pure Foods is unable to compete effectively with lower-priced imports, its market share and sales may decrease, and the business, financial condition, results of operations and prospects could be materially and adversely affected.

Growth of supermarkets and consolidation of wholesale buyers

The Philippine retail market has historically been highly fragmented among numerous small neighborhood stores, groceries and more traditional wet markets. Small neighborhood stores service limited geographical areas and purchase relatively small quantities of the products of San Miguel Pure Foods from distributors and larger supermarkets. In recent years, larger supermarkets have begun to gain market share in the Philippines. There is a

risk that the business of San Miguel Pure Foods may become concentrated in fewer and larger customers, which could increase the relative bargaining power of these customers. There is no assurance that supermarkets or one of these larger customers will not exert downward pressure on wholesale prices of the products of San Miguel Pure Foods, which could have a material adverse effect on the financial condition and results of operations of San Miguel Pure Foods.

Exposure to the credit risks of its customers

San Miguel Pure Foods is exposed to the credit risk of its customers, and defaults on material payments owed to San Miguel Pure Foods by customers could significantly reduce the operating cash flows and liquidity of San Miguel Pure Foods, as well as have a material adverse effect on the financial condition and results of operations of San Miguel Pure Foods. Some of the customers of San Miguel Pure Foods could also experience cash flow difficulties or become subject to liquidation, which could in turn lead to San Miguel Pure Foods being unable to collect payments or experiencing long delays in collection. Trade receivables are non-interest bearing and are generally on 30-day terms. As of December 31, 2012, over 54% of trade receivables of San Miguel Pure Foods were due within 30 days. There is no assurance that the exposure of San Miguel Pure Foods to the risk of delayed payments from its customers or defaults in payment by its customers will not increase, or that it will not experience losses or cash flow constraints as a result. If any of these events were to occur, the net income and cash flows of San Miguel Pure Foods could be materially reduced.

Short-term contracts

As is common in the industry in which San Miguel Pure Foods operates, San Miguel Pure Foods does not have long-term contracts with its customers and, consequently, its sales are subject to short-term variability resulting from the seasonality of, and other fluctuations in, demand for its products. The customers of San Miguel Pure Foods have no obligation to place new orders with San Miguel Pure Foods following the expiration of their current obligations, and may cancel, reduce or delay orders for a variety of reasons. The level and timing of orders placed by the customers of San Miguel Pure Foods may vary due to a number of factors including:

- seasonality and other fluctuations in demand for the products of San Miguel Pure Foods;
- the competitiveness of the selling prices of San Miguel Pure Foods in the industry;
- customer satisfaction with the level of service provided by San Miguel Pure Foods; and
- customers' inventory management.

San Miguel Pure Foods has experienced terminations of, and reductions and delays in its customers' orders in the past. If San Miguel Pure Foods does not receive substitute orders, such events could lower its facility utilization rates, which could materially decrease the sales and profitability of San Miguel Pure Foods.

Price controls on certain products

Basic necessities such as fresh pork, beef and poultry meat, milk, coffee and cooking oil, and prime commodities such as flour, dried, processed and canned pork, beef and poultry meat, and other dairy products and swine and poultry feeds may be made subject to price control by the Philippine government. Under the Philippine Republic Act No. 7581, otherwise known as the Price Act ("Price Act"), the President of the Philippines may impose a price ceiling on basic necessities and prime commodities in the event of calamities, emergencies, illegal price manipulation or when the prevailing prices have risen to unreasonable levels.

If the exigent conditions provided for under the Price Act occur, there is no assurance that the President of the Philippines will not exercise the price control powers provided under the Price Act and impose price ceilings on certain products of the food business of SMC which are considered basic necessities and prime commodities under the said law. Any resulting price control, or the continuance thereof, may have a material adverse effect on the business of San Miguel Pure Foods, results of operations and financial performance.

Risks Relating to the Packaging Business

Handling of products

In the past, there have been instances of inferior product quality for products produced by the customers of SMYPC. Most of these instances, such as mishandling of products produced by the customers of the Packaging Group, tampering, vandalism or terrorist activities, were not in the control of SMYPC. Various management systems are in place to prevent the contamination of products packaged by SMYPC during manufacturing, distribution or retail process. There can be no assurance, however, that such management systems will be

effective. Any lack of care or tampering with such products, especially in instances where it is not readily capable of detection, could negatively affect the reputation of the products and have a material adverse effect on the business, financial performance and prospects of the Packaging Group.

Competition and challenges in product development and production processes

In order to compete in the packaging material industry, the packaging business of SMC is required to continually develop and implement product innovations and improve its production technology, processes and efficiencies. The success of the packaging business also depends on its ability to identify and meet changing customer requirements and trends in the industry. Any failure to timely develop and introduce new products, or enhance existing products in response to changing customer requirements or industry standards could have a material adverse effect on the business, financial performance and prospects of SMC.

In addition, research and development of any new technology or production methods require significant capital investments and could take a significant amount of time. Moreover, there is no assurance that the packaging business of SMC will successfully develop such technology and production methods, or that they will be accepted by existing customers or attract new customers, which could have a material adverse effect on the business, financial performance and prospects of SMC.

Risks Relating to the Fuel and Oil Business

Volatility in the price of crude oil

The financial results of Petron are primarily affected by the relationship, or margin, between the prices for its refined petroleum products and the prices for imported crude oil, which generally accounts for a large portion of Petron's total cost of goods sold. For example, in the year ended December 31, 2012, crude oil accounted for approximately 69% of the total cost of goods sold of Petron.

Many factors influence the price of crude oil, including changes in global supply and demand for crude oil, international economic conditions, global conflicts or acts of terrorism, weather conditions, domestic and foreign governmental regulation and other factors over which Petron has no control. Historically, international crude oil prices have been volatile, and they are likely to continue to be volatile in the future. International crude oil prices were especially volatile in the second quarter of 2012. For example, Dubai crude oil prices declined from approximately US\$124/bbl on March 14, 2012 to approximately US\$89/bbl on June 22, 2012.

Petron holds approximately two months and approximately three weeks of crude oil and finished petroleum products inventory in the Philippines and Malaysia, respectively. Accordingly, since Petron accounts for its inventory using the first-in-first-out method, a sharp drop in crude oil prices could adversely affect Petron, as it may require Petron to sell its refined petroleum products produced with higher-priced crude oil at lower prices, as was the case in the second quarter of 2012, causing Petron to report a net loss for that period. Petron may not be able to pass crude oil price fluctuations along to its consumers in a timely manner or at all due to regulatory restrictions or social and competitive concerns. The Philippine government has historically intervened to restrict increases in the prices of petroleum products in the Philippines from time to time. For example, on October 2, 2009, then President Gloria Macapagal-Arroyo declared a state of national calamity in view of the devastation caused by typhoons "Ondoy" and "Pepeng." President Arroyo subsequently issued Executive Order 839 mandating that prices of petroleum products in Luzon be kept at October 15, 2009 levels effective October 23, 2009. As a result of this price freeze, Petron was unable to raise prices for its refined petroleum products, which adversely affected its profitability during the period until the price freeze was lifted on November 16, 2009. Any inability to pass on fluctuations in the price of crude oil may have a material adverse effect on the business, results of operations and financial condition of Petron. In addition, even if Petron were able to pass on increases in the price of crude oil to its customers, demand for its products may decrease as a result of such price increases. Moreover, the Malaysian operations of Petron are subject to government price controls, as the fuel business is regulated by the government. Petron is affected by Malaysian government policies and regulations relating to the marketing of fuel products, including price controls, subsidies and quotas.

Single source of supply

Petron purchases a significant portion of the crude oil for its Philippine operations from Saudi Arabian Oil Company ("Saudi Aramco"), the state-owned national oil company of Saudi Arabia. For example, in 2011 and 2012, Petron purchased approximately 74% and 82%, respectively, of the total crude oil supply requirements of the refinery in Limay, Bataan in the Philippines (the "Limay Refinery") from Saudi Aramco. Under the term contract Petron entered into with Saudi Aramco in 2008, Petron may purchase up to 140 thousand barrels per calendar day ("MBCD") of various Saudi Aramco crudes. Pricing is determined through a formula that is linked

to international industry benchmarks. The contract is automatically renewed annually unless either Petron or Saudi Aramco decides to terminate the contract upon at least 60 days' written notice prior to its expiration date. The contract was most recently renewed on October 28, 2012. The completion of the Refinery Master Plan ("RMP-2"), which is expected to be in 2014, may increase the total crude oil supply requirements of the Limay Refinery, and Petron may be required to purchase more Saudi Aramco crudes to meet such increased demand. The supply of imported crude oil by Saudi Aramco is subject to a variety of factors beyond the control of Petron, including political developments in and the stability of Saudi Arabia and the rest of the Middle East, government regulations with respect to the oil and energy industry in those regions, weather conditions and overall economic conditions in the Middle East. In addition, Petron purchases all of the crude oil supply requirements for its refinery in Port Dickson, Malaysia (the "Port Dickson Refinery"), including purchases under term contracts and spot market purchases, from Concord Energy Pte Ltd ("Concord Energy"). A disruption in the operations of Saudi Aramco, or a decision by either Saudi Aramco or Concord Energy to amend or terminate their respective contracts with Petron, could negatively affect Petron's crude oil supply. If the supply of crude oil from Saudi Aramco or Concord Energy were disrupted, Petron would be required to meet any consequent supply shortfall through other suppliers or spot market purchases. Depending on market conditions at the time of the disruption, such purchases from other suppliers could be at higher prices than the purchases by Petron from Saudi Aramco or Concord Energy, which would adversely affect the financial condition and results of operations of Petron.

While the Limay Refinery and the Port Dickson Refinery are configured to process predominantly light and sweet crude oils, such as Middle East crude oil from Saudi Aramco and Malaysian Tapis crude oil purchased from Concord Energy, respectively, both refineries are capable of processing other crude oils. In line with its crude oil optimization strategy, Petron is exploring the utilization of other crude oils at both refineries. However, there can be no assurance that Petron will be able to convert to other crude oils efficiently or in a timely manner.

If Petron is unable to obtain an adequate supply of crude oil or is only able to obtain such supply at unfavorable prices, its margins and results of operations would be materially adversely affected.

Intensive capital requirements

The business of Petron is capital intensive. Specifically, the processing and refining of crude oil and the purchase, construction and maintenance of machinery and equipment require substantial capital expenditures. The ability of Petron to maintain and increase its sales, net income and cash flows depends upon the timely and successful completion of its planned capital expenditure projects. The current business of Petron strategies involve various upgrades and enhancements to its refineries, primarily the Limay Refinery pursuant to the RMP-2, the construction of new facilities, the continued expansion of its service station network in the Philippines and the rebranding and refurbishing of its service station network in Malaysia. If Petron fails to complete its capital expenditure projects on time, or within budget or at all, or fails to operate them at their designed capacity, it may be unable to increase its sales and profits or to capture additional market share as planned, and the business, financial performance and prospects of Petron could be materially and adversely affected.

In addition, Petron has recently incurred a substantial amount of indebtedness to finance its capital expenditure projects, a significant portion of which is due in five years or less. As the cash resources of Petron will be insufficient to fully finance its planned capital expenditures, the ability of Petron to complete its planned capital expenditure projects and meet its debt servicing obligations will depend in part on its ability to generate sufficient cash flows from its operations and obtain adequate additional financing. There can be no assurance that Petron will be able to generate sufficient cash flows from its operations or obtain adequate financing for its planned capital expenditure projects or to meet its debt servicing obligations, on acceptable terms or at all. Failure by Petron to finance and successfully implement its planned capital expenditure projects could adversely affect its business, financial condition and results of operations.

Significant disruption of refinery operations

The operation by Petron of its refineries could be severely disrupted by many factors, including accidents, breakdown or failure of equipment, interruption in power supply, human error, natural disasters and other unforeseen circumstances and problems. For example, in November 2008, the main electrical facilities in the utilities area of the Limay Refinery were damaged by fire, which necessitated repairs and resulted in higher maintenance and repair costs in 2009. Such disruptions could result in product run-outs, facility shutdown, equipment repair or replacement, increased insurance costs, personal injuries, loss of life and unplanned inventory build-up, all of which could have a material adverse effect on the business and financial performance of Petron.

While Petron has insurance policies covering some of these risks, including business interruption insurance, there is no assurance that they will cover all potential losses, and insurance may not be available for all risks to which Petron is exposed, on commercially reasonable terms or at all. There is no assurance that operational disruptions will not occur in the future or that insurance will adequately cover the full extent of the losses or other financial impact on Petron. The occurrence of any such factors, accidents or uninsurable or inadequately insured loss could result in Petron suffering material losses and have a material adverse effect on the business, financial condition and results of operations of Petron.

Effectively integrating acquired business

In March 2012, Petron completed its acquisition of ExxonMobil's downstream business in Malaysia, extending the portfolio of SMC of oil refining and marketing businesses outside the Philippines. Petron will continue to consider selective opportunities to expand both domestically and outside the Philippines through strategic acquisitions consistent with its focus on increased production of diesel, gasoline, jet fuel, kerosene and LPG ("White Products") and the creation of operational synergies. However, there can be no assurance that Petron will be able to integrate its new business in Malaysia fully in line with its strategy. Any failure to do so could have a material adverse effect on the business, results of operations and financial condition of Petron. Future acquisitions could also give rise to similar integration risks, as well as financial risks.

Product substitution

As a result of high oil prices and environmental concerns, the use of alternative fuels such as natural gas, ethanol and coco-methyl-ester fuel blends have become more attractive to the customers of Petron in recent years. If alternative fuels become more affordable and available than petroleum products, customers may shift from petroleum to these alternative fuels not offered by Petron, resulting in lower sales volumes. In recent years, the Philippine and Malaysian governments have each enacted regulations mandating the inclusion of a specified percentage of alternative fuels in gasoline fuels sold or distributed by every oil company in those countries, and these types of requirements may be increased in the future. If Petron does not respond quickly and effectively to product substitutions or government-mandated product formulations in the future, its business and prospects may be adversely affected.

Regulated fuel business in Malaysia

As in many countries, the fuel business in Malaysia is regulated by the government. The Malaysian government regulates the pricing structure through the automatic pricing mechanism ("APM"), pursuant to which it mandates (i) the prices of certain refined petroleum products, (ii) quotas and (iii) certain fixed amounts for marketing, transportation and distribution costs in relation to the subsidy structure. The Malaysian government subsidizes fuel prices so that increases in international crude oil prices are not borne fully by Malaysian consumers. Petron's financial condition thus depends to a significant degree on the Malaysian government's prompt payment of these fuel subsidies. The Malaysian government has publicly stated that the country's fuel prices will eventually be deregulated and set on a free market basis, as the current subsidy levels are unsustainable. However, no firm timeline has been provided for this deregulation. There can be no assurance that the Malaysian government will not decide to decrease or eliminate its subsidies or narrow their application in the future without a corresponding commensurate increase in or elimination of the price ceiling. A substantial portion of the sales of Petron is derived from sales of refined petroleum products in Malaysia that are subject to price controls. Accordingly, if international crude oil prices remain high or increase further and the Malaysian government decreases or eliminates the refined petroleum product subsidies without increasing or eliminating the mandated refined petroleum product prices, the financial condition and results of operations of Petron would be materially and adversely affected.

In addition, the sale of diesel in Malaysia is subject to a quota system to ensure that subsidized diesel is not sold illegally to industrial or commercial customers at higher, unregulated, prices. Diesel sales that exceed the volumes permitted under the quotas of Petron, or those of its industrial or commercial customers, are not eligible for government subsidies. Accordingly, Petron endeavors to limit diesel sales to volumes covered by the quotas. There can be no assurance that the Malaysian government will increase quotas, grant applications or not decrease the quotas of Petron or those of any of its industrial or commercial customers in the future. A substantial portion of the sales of Petron is derived from sales of diesel in Malaysia that are subject to the quota system. Accordingly, if the Malaysian government decreases or does not increase the quotas of Petron or those of any of its commercial transportation customers, the financial condition and results of operations of Petron would be materially and adversely affected.

Political instability, acts of terrorism or military conflict in Malaysia

Petron may be affected by political and social developments in Malaysia, as well as changes in the political leadership and/or government policies in Malaysia. Such political or regulatory changes may include (but are not limited to) the introduction of new laws and regulations that impose and/or increase restrictions on imports, the conduct of business, the repatriation of profits, the imposition of capital controls, changes in interest rates and the taxation of goods and services. There can be no assurance that any changes in such regulations or policies imposed by the Malaysian government from time to time will not have an adverse effect on the business, financial condition, results of operations and prospects of Petron. In addition, terrorist attacks and other acts of violence or war in Malaysia may negatively affect the Malaysian economy, resulting in a loss of consumer confidence and reduced demand for the products of Petron in Malaysia, which could adversely affect the business, financial condition, results of operations and prospects of Petron.

Insurance claims

Petron uses a combination of self-insurance and reinsurance to cover its properties and certain potential liabilities. The insurance coverage of Petron includes property, marine cargo and third-party liability. The business interruption insurance of Petron has a US\$94.5 million limit that covers losses at its Limay refinery. All of the insurance policies of Petron are provided by its wholly owned subsidiary, Petrogen Insurance Corporation and majority of such insurance coverage is reinsured with leading local and foreign reinsurers through Overseas Ventures Insurance Corporation, a wholly owned subsidiary of Petron. For its Malaysian operations, Petron purchases insurance from Malaysian insurance companies consistent with Malaysian law. Petron estimates the liabilities associated with the risks retained by it, in part by considering historical claims, experience and actuarial assumptions which, by their nature, are subject to a degree of uncertainty and variability. Among the causes of this uncertainty and variability are unpredictable external factors affecting future inflation rates, discount rates, litigation trends, legal interpretations and actual claim settlement patterns.

If the number or severity of claims for which Petron is self-insured increase, or if it is required to accrue or pay additional amounts because the claims prove to be more severe than its original assessments, the financial condition, results of operations and cash flows of Petron may be materially adversely affected.

Risks Relating to the Energy Business

Increased competition in the Philippine power industry

In recent years, the Philippine government has sought to implement measures designed to establish a competitive power market. These measures include the planned privatization of at least 70% of the NPC-owned and-controlled power generation facilities and the grant of a concession to operate transmission facilities, as well as the establishments of the Wholesale Electricity Spot Market (“WESM”). The move towards a more competitive environment could result in the emergence of new and numerous competitors. These competitors may have greater financial resources, and may have more extensive experience than SMC Global Power, giving them the ability to respond to operational, technological, financial and other challenges more quickly than SMC Global Power. These competitors may therefore be more successful than SMC Global Power in acquiring existing power generation facilities or in obtaining financing for and the construction of new power generation facilities. The type of fuel that competitors use for their generation facilities may also allow them to produce electricity at a lower cost and to sell electricity at a lower price. SMC Global Power may therefore be unable to meet the competitive challenges it will face.

The impact of the ongoing restructuring of the Philippine power industry will change the competitive landscape of the industry and such changes are expected to affect the financial position, results of operations and cash flows of SMC Global Power in various ways. For example, the establishment and operation of the WESM has resulted in a more transparent price setting mechanism. Although offtakers such as Meralco will continue to be obligated to pay for capacity and energy at the tariffs set under the terms of their respective offtake agreements, if market-based wholesale prices significantly differ from the contractual tariffs, SMC Global Power could come under pressure to review or renegotiate the terms of such offtake agreements, which may lead to a downward adjustment of tariffs, and the financial condition and results of operations of SMC Global Power could be adversely affected.

To the extent that distribution utilities or industrial offtakers agree to purchase from other generation companies instead of purchasing from SMC Global Power, the ability of SMC Global Power to increase its sales and sell additional electricity to distribution utilities or industrial offtakers through its generation facilities would be adversely affected.

Disruptions in fuel supply

The operations of the Sual Power Plant and the Ilijan Power Plant depend on the availability of fuel, in particular coal and natural gas, respectively. Pursuant to the terms of its IPPA Agreements with PSALM, SMC Global Power is responsible, at its cost, for supplying the Sual Power Plant with the fuel required for its operations. There is no assurance that there will not be any interruption or disruption in, or change in terms of, the fuel supplies to these power plants, or that there will be sufficient fuel in the open market or sufficient transportation capacity available to ensure that these power plants receive sufficient fuel supplies required for their operations on a timely basis or at all. There is also no assurance that SMC Global Power will be able to purchase all of its required fuel supplies from its regular suppliers that produce fuel of acceptable and known quality. Consequently, SMC Global Power could experience difficulties ensuring a consistent quality of fuel, which could negatively affect the stability and performance of these power plants. Such factors, which may include events which are beyond the control of SMC Global Power, could affect the normal operation of these power plants which could have material adverse effect on the business, financial condition and results of operations of SMC Global Power.

Reliance on Independent Power Producers for the operation and maintenance of the IPPA power plants

Power generation involves the use of highly complex machinery and processes and the success of SMC Global Power depends on the effective maintenance of equipment for its power generation assets. Independent Power Producers (“IPPs”) associated with the respective IPPA power plants are responsible for the operation and maintenance of the IPPA power plants.

Although the IPPs’ energy conversion agreements (“ECAs”) or power purchase agreements (“PPAs”) with NPC in respect of the IPPA power plants contain bonus and penalty provisions, these do not eliminate the risk of failure on the part of the IPPs to satisfactorily perform their respective operations and maintenance obligations. Any failure on the part of such IPPs to properly operate and/or adequately maintain their respective power plants could have a material adverse effect on the business, financial condition and results of operations of SMC Global Power.

Operating capacities of IPPA power plants

The administration of power generation plants’ output involves significant risks, including:

- breakdown or failure of power generation equipment, transmission lines, pipelines or other equipment or processes, leading to unplanned outages and operational issues;
- flaws in the equipment design or in power plant construction;
- issues with the quality or interruptions in the supply of key inputs, including fuel or water;
- material changes in legal, regulatory or licensing requirements;
- operator error;
- performance below expected levels of output or efficiency;
- industrial actions affecting power generation assets owned or managed by SMC Global Power or its contractual counterparties;
- pollution or environmental contamination affecting the operation of power generation assets;
- force majeure and catastrophic events including fires, explosions, earthquakes, volcanic eruptions, floods and terrorist acts that could cause forced outages, suspension of operations, loss of life, severe damage and plant destruction;
- planned and unplanned power outages due to maintenance, expansion and refurbishment;
- inability to obtain or the cancellation of required regulatory, permits and approvals; and
- opposition from local communities and special interest groups.

There is no assurance that any event similar or dissimilar to those listed above will not occur or will not significantly increase costs or decrease or eliminate sales derived by SMC Global Power from its power generation assets. While the IPPA Agreements of SMC Global Power provide certain relief in the event the IPPA power plants cannot produce or dispatch electricity, if any of the power generation assets of SMC Global Power is unable to generate or deliver electricity to customers for an extended period of time, the customers of SMC Global Power may be exempt from making certain payments so long as any such events continue. In addition, if

SMC Global Power fails to generate or deliver electricity beyond contractually agreed periods, the counterparties of SMC Global Power in its power supply contracts (“PSCs”) may have a right to terminate those contracts, and replacement contracts may not be entered into on comparable terms or at all. Any of the foregoing could have a material adverse effect on the financial and operating performance of SMC Global Power.

Acquisitions of existing power plants

SMC Global Power actively participates in public auctions of power generation assets that are being privatized by PSALM. SMC Global Power has acquired all of its power generation assets in those auctions, and intends to make additional acquisitions in the future. However, there is no assurance that SMC Global Power will be successful in bidding for other power generation assets in the future. There is also no assurance that those auctions will be conducted according to publicized schedules, as auctions have been postponed and publication of auction guidelines have been delayed in the past. In addition, bids may also not be successful for reasons beyond the control of SMC Global Power, including an auction not attracting the requisite number of bids or bids not meeting minimum reserve prices.

Moreover, a successful bid will not guarantee a successful takeover and operation of a power generation asset. A successful bidder must also satisfy all of the conditions precedent to assuming control under an IPPA Agreement or an asset purchase agreement. Even after a successful takeover, there is no assurance that operations will be a success if, for example, the acquiror discovers pre-existing problems or faults, especially as privatized power generation assets are typically sold on an “as is, where is” basis and are sometimes sold independently of the land on which they are located. Consequently, any unplanned rehabilitation or power generation asset upgrade may disrupt its operations and cause it to miss target operational and financial performance goals. There is also no assurance on the performance or condition of the assets, including generating capacity, or on the adequacy or availability of transmission lines through which electricity output is transmitted. Other related risk factors include strong competition, difficult market conditions, increased operating costs and failure to renew requisite licenses and permits.

Even with extensive due diligence, the acquiror may not be able to ascertain all of the associated risk factors prior to acquisition or taking over operations, and the occurrence of any of these factors could have a material adverse effect on the business, financial performance and prospects of SMC Global Power.

Price fluctuations

From the time WESM for Luzon began operating in June 2006, market prices for electric power have fluctuated substantially. Unlike many other commodities, electric power can only be stored on a very limited basis and generally must be produced concurrently with its use. As a result, power prices are subject to significant volatility from supply and demand imbalances. Long-term and short-term power prices may also fluctuate substantially due to other factors outside of the control of SMC Global Power, including:

- increases and decreases in generation capacity in the markets of SMC Global Power, including the addition of new supplies of power from existing competitors or new market entrants as a result of the development of new generation power plants, expansion of existing power plants or additional transmission capacity;
- changes in power transmission or fuel transportation capacity constraints or inefficiencies;
- electric supply disruptions, including power plant outages and transmission disruptions;
- changes in the demand for power or in patterns of power usage, including the potential development of demand-side management tools and practices;
- climate, weather conditions, natural disasters, wars, embargoes, terrorist attacks and other catastrophic events;
- availability of competitively priced alternative power sources;
- development of new fuels and new technologies for the production of power; and
- changes in the power market and environmental regulations and legislation.

These factors could have a material adverse effect on the business, financial condition and results of operations of SMC Global Power.

Certain tax exemptions and tax incentives

As of December 31, 2012, certain subsidiaries of SMC Global Power — namely, SMEC, as IPPA for the Sual Power Plant, Strategic Power Devt. Corp. (“SPDC”), as IPPA for the San Roque Power Plant, South Premiere Power Corp. (“SPPC”), as IPPA for the Ilijan Power Plant, and Sultan Energy Phils. Corp. (“SEPC”), as

concession holder for the Sultan coal deposit — benefited from certain tax exemptions and tax incentives, such as a four-year income tax holiday on income tax due on sales derived from its power generation activities for SMEC, SPDC and SPPC, deductions from taxable income subject to certain capital requirements and duty-free importation of capital equipment, spare parts and accessories. In addition, SEPC may make use of tax credits equivalent to national internal revenue taxes and duties paid on raw materials and supplies and semi-manufactured products used in producing its export products for a period of ten years from June 2011.

If these tax exemptions or tax incentives that SMC Global Power or any of its subsidiaries are entitled to are revoked or repealed, the income of SMC Global Power from these sources will be subject to the corporate income tax rate, which is 30.0% of net taxable income as of December 31, 2012. As a result, the tax expense of SMC Global Power would increase and its profitability would decrease. There have also been reports in the Philippine press that the Philippine government may in the future discontinue its policy of granting tax incentives for similar types of projects, and there is no assurance that SMC Global Power will be able to obtain and benefit from similar tax incentives for future projects. The expiration, non-renewal, revocation or repeal of these tax exemptions and tax incentives, and any associated impact on SMC Global Power, could have a material adverse effect on the business, financial condition and results of operations of SMC Global Power.

Regulation of the distribution rates of offtakers of SMC Global Power

The primary sources of sales of SMC Global Power are its offtakers, approximately 79% of which are distribution utilities. The ability of distribution utility offtakers to pay SMC Global Power in accordance with the terms of their respective PSCs depends, in large part, on their ability to pass on their generation costs to their customers. The rates these offtakers charge their customers are intended to cover their generation costs, which are subject to periodic review by the ERC.

There is no assurance that the ERC will permit the distribution utility offtakers of SMC Global Power to increase their rates to recover all of their generation costs or that subsequent reviews by the ERC will not result in cancellation of any such increases or require such offtakers to refund payments previously received from their customers or that SMC Global Power will not come under pressure to review or renegotiate its tariffs downward. In addition, there is no assurance that any rate increases approved by the ERC will not be overturned by Philippine courts on appeal. Any restriction on the ability to pass on such costs or any intervention in such rates and tariffs could have a material adverse effect on the business, financial conditions and results of operations of SMC Global Power.

Market limitations under the EPIRA

As of December 31, 2012, SMC Global Power had a 22% market share of the Luzon grid and a 17% market share of the national grid in terms of installed capacity according to the DOE. The EPIRA limits a participant's market share to 30.0% per grid and 25.0% of the national grid by installed capacity. As a result, SMC Global Power may not receive permission to increase its capacity and market share if such increase would cause SMC Global Power to exceed the permitted capacity or market share. An inability to expand and grow the power business could materially and adversely affect the business and prospects of SMC Global Power.

Meralco is controlled by other shareholders

As of December 31, 2012, SMC had a 32.04% equity interest in Meralco, with the remaining equity interest held by other shareholders. The other shareholders of Meralco may be able to elect a majority of the members of the Meralco board of directors and to determine the outcome of other actions requiring a vote of Meralco shareholders, except in very limited cases. There is no assurance that such other shareholders will not take actions in relation to Meralco that are inconsistent with SMC's interests.

Development of greenfield power projects

The development of greenfield power projects involves substantial risks that could give rise to delays, cost overruns, unsatisfactory construction or development or the total or partial loss of the interest of SMC Global Power in the project. Such risks include:

- the inability to secure adequate financing;
- the inability to negotiate acceptable fuel purchase agreements and offtake agreements;
- equipment shortages or quality problems with equipment, material or labor or the breakdown or failure of equipment or processes;
- opposition to the projects of SMC Global Power from local communities or special-interest groups;

- the need to incur significant expenses for preliminary engineering, permits and legal and other expenses before determining whether a project is feasible, economically attractive or capable of being financed;
- engineering and environmental problems;
- construction and operational delays, or unanticipated cost overruns;
- failure by key contractors and vendors to timely and properly perform;
- adverse environmental (including inclement weather) conditions;
- social unrest and terrorism; and
- other fortuitous events.

Any such delays, cost overruns, unsatisfactory construction or development or the total or partial loss of the interests in its projects could have a material adverse effect on the business, financial condition, results of operation and future growth prospects of SMC Global Power.

Development of coal resources

SMC Global Power may not succeed in its endeavors to conduct coal exploration and extraction activities. The strategy includes the acquisition and development of coal mines to provide a source of coal fuel supply for its planned and contemplated greenfield power projects. However, as SMC Global Power is focused primarily on power generation (either through IPPA agreements or as owner of newly acquired or newly constructed power plants), SMC Global Power may not be successful in developing the knowledge, experience or expertise necessary for the successful operation of the coal mines it may develop or acquire, whether on its own or in conjunction with a joint venture partner. In addition, acquisition, development and operation of coal mines will require significant managerial, operational and financial resources.

As with all mining exploration properties or projects, there is a risk that they may not become commercially viable mines due to project delays, cost overruns, changes in market circumstances or a project not producing coal in line with reserve estimates of the expected quality or grade. Consequently, SMC Global Power may not be able to achieve the intended economic benefits of these projects, which in turn could materially and adversely affect SMC Global Power's business, financial condition, results of operations and growth prospects.

In addition, the exploration and exploitation of coal reserves in the Philippines are subject to regulation by the DOE. There is no assurance that SMC Global Power will be successful in securing the requisite exploration permits or operating contracts for development of the coal mines, or in the extraction of coal resources. Any such failure could materially reduce SMC Global Power's sales and profitability.

Risks Relating to SMC Infrastructure Business

Challenges in operating infrastructure business

The ability of SMC to successfully grow and operate its infrastructure business is subject to various risks and uncertainties, including:

- the need to procure materials, equipment and services at reasonable costs and on a timely basis;
- reliance on third party providers and consultants, in particular for those aspects of the business where SMC has limited expertise or experience;
- the possible need to raise additional financing to fund the projects, which SMC may be unable to obtain on satisfactory commercial terms or at all;
- errors or delays in the design, engineering, construction, installation, inspection, commissioning, management or operation of each project; and
- delays or denials of required approvals, including required environmental approvals.

Occurrence of any of the foregoing or a failure by SMC to successfully operate its infrastructure business could have a material adverse effect on its business, financial condition and results of operations.

Inability to secure tariff increases

The commercial success of the infrastructure business and projects of SMC depends in part on the ability of the affiliates of SMC to impose certain tariff increases. While tariffs increases are permitted contractually pursuant to pricing formulas set forth in the applicable concession agreements, tariff increases may not be feasible

commercially due to various factors, including competition and price sensitivity in consumer demand. Any constraint on the ability of the infrastructure business to increase tariffs could have a material adverse effect on SMC's business, financial condition and results of operations.

Decrease in utilization

The commercial success of the infrastructure business of SMC depends on the ability of its projects to maintain or attract increases in utilization. External events may decrease the numbers of vehicles, airplanes or passengers that utilize the infrastructure facilities of SMC. For example, rising oil prices could result in fewer passenger vehicle journeys, which could decrease sales received from road tolls. Higher oil prices could also increase the cost of airfare for consumers, which could decrease passenger numbers at the Boracay airport. Any decrease in utilization or any factor that would decrease patronage could have a material adverse effect on the infrastructure business, financial condition, results of operations and prospects of SMC.

Risks Relating to Other Businesses of SMC

Rapid changes in technology

The telecommunications industry has been characterized recently by rapid technological changes. There is no assurance that these developments will not result in competition from providers of new services or the need for the telecommunications business of SMC to make substantial capital expenditures to upgrade its facilities. The future success of the telecommunications business of SMC will depend, in part, on its ability to anticipate or adapt to such changes and to offer services that meet customer demands on a competitive and timely basis. The telecommunications business of SMC may be unable to obtain new technologies on a timely basis or on satisfactory terms, or implement them in an appropriate or effective manner. Future development of new technologies, services or standards could require significant changes to the telecommunications business model, negatively affect the existing businesses of SMC and necessitate significant new investments. Such strategic initiatives and technological developments could require SMC to incur significant additional capital expenditures. There is no assurance regarding how emerging and future technological changes will affect the operations or the competitiveness of the telecommunications services. Rapid technological changes could materially reduce the sales and profitability of the telecommunications business of SMC, and its results of operations and prospects.

Competition in the telecommunications industry

The market for telecommunication services in the Philippines is characterized by a small number of dominant market players. In the mobile sector, the two major players are Philippine Long Distance Telephone Company and Globe Telecommunications, Inc. SMC expects competition to increase as the Philippine telecommunications industry continues to grow. There is also uncertainty as to the pace and extent of growth in subscriber demand and the extent to which prices for airtime and line rental will change. There is no assurance that SMC will be able to compete successfully against current or future competitors.

The principal competitors of SMC in the Philippines include Philippine Long Distance Telephone Company and Globe Telecommunications, Inc. which are relatively larger companies that may have greater market presence as well as greater engineering resources and experience. Many of the voice and data communications customers of these telecommunications companies may also prefer to use companies that provide multiple services for their telecommunications needs, rather than using those companies controlled by SMC. If SMC is not able to compete successfully with these companies, such inability could have a material adverse effect on the business, financial condition, results of operations and prospects.

Changes in domestic and international banking policies and regulations

The recent global financial crisis has led, and is expected to continue to lead, to significant regulatory and policy changes in the banking and financial sector in various countries, including the Philippines. Changes to policies or regulations governing capital and liquidity ratios, cross-border capital flows, local lending obligations, management compensation and consumer protection could have an impact on various aspects of SMC's banking business. The BSP has issued such regulations affecting the risk-based capital adequacy framework for banks.

The extent and impact of such changes is difficult to anticipate and estimate. There is no assurance that future changes in the legal and regulatory environment for banks in the Philippines and internationally will not materially and adversely affect the growth, capital adequacy and profitability of the banking business of SMC or its future financial performance. In addition, the banking business of SMC could also be materially and adversely affected by changes in international policies, income tax laws and rules and accounting principles, as well as international conventions and standards relating to commercial banking operations.

Risks Relating to the Philippines

Concentration of operations and assets in the Philippines

Historically, the financial condition and results of operations of SMC have been influenced, and will continue to be influenced, to a significant extent by the overall performance of the Philippine economy. In particular, the Philippines has experienced periods of slow or negative growth, high inflation, significant devaluation of the Philippine Peso and the imposition of exchange controls. Currently, approximately 76% of the sales of SMC is derived from business activity in the Philippines.

In addition, demand for many of the products of SMC is tied closely to domestic consumer purchasing power and disposable income levels, which may be adversely affected by unfavorable economic developments in the Philippines. For example, in 2008, the macroeconomic slowdown in the Philippines negatively affected sales volumes in the flour and dairy, spreads and oils businesses of SMC, as consumers prioritized staple commodities such as rice over bread and bread spreads. Similarly, with respect to the beverage business of SMC, unfavorable economic developments may induce consumers of these beverage products of SMC to purchase more private label or economy brands, sales of which produce lower profit margins. As the businesses of SMC expand their product and brand portfolios in higher-priced premium market segments in their respective industries, their businesses and prospects will be increasingly affected by any deterioration in consumer purchasing power. Any decrease in consumer purchasing power and disposable income levels could have a material adverse effect on the financial and operating performance of SMC.

In recent years global financial, credit and currency markets have experienced, and may continue to experience, significant dislocations and liquidity disruptions. Any downturn in the Philippine economy may negatively affect consumer sentiment and general business conditions in the Philippines, which may materially reduce the sales, profitability and cash flows of SMC. Moreover, there is no assurance that current or future government policies will continue to be conducive to sustaining economic growth.

Political instability or acts of terrorism in the Philippines

The Philippines has from time to time experienced political and military instability. In the last few years, there has been political instability in the Philippines, including impeachment proceedings against two former Presidents and a former Chief Justice of the Supreme Court of the Philippines, and public and military protests arising from alleged misconduct by previous administrations. In addition, there is no guarantee that acts of election-related violence will not occur in the future and such events could negatively affect the Philippine economy. An unstable political environment, whether due to the imposition of emergency executive rule, martial law or widespread popular demonstrations or rioting, could negatively affect the general economic conditions and operating environment in the Philippines, which could have a material adverse effect on the business, financial condition and results of operations of SMC. The Philippines has also been subject to a number of terrorist attacks since 2000, and the Philippine armed forces have been in conflict with groups which have been identified as being responsible for kidnapping and terrorist activities in the Philippines. In addition, bombings have taken place in the Philippines, mainly in cities in the southern part of the country. Political instability, acts of terrorism, violent crime and similar events could have a material adverse effect on the business, financial condition, results of operations and prospects of SMC.

Natural catastrophes

The Philippines has experienced a number of major natural catastrophes over the years including typhoons, volcanic eruptions and earthquakes that may materially disrupt and adversely affect the business operations of SMC. There is no assurance that the insurance coverage SMC maintains for these risks will adequately compensate it for all damages and economic losses resulting from natural catastrophes.

Philippine credit rating

International credit rating agencies issue credit ratings for companies with reference to the country in which they are resident. As a result, the sovereign credit ratings of the Philippines directly affect companies that are resident in the Philippines, such as SMC. There is no assurance that Moody's, S&P or other international credit rating agencies will not downgrade the credit rating of the Philippines in the future. Any such downgrade could have a material adverse effect on liquidity in the Philippine financial markets and the ability of the Philippine government and Philippine companies, including SMC, to raise additional financing, and will increase borrowing and other costs.

Foreign exchange controls

The Philippines currently does not have any foreign exchange controls in effect. However, the BSP has statutory authority, with the approval of the President of the Philippines, during a foreign exchange crisis or in times of national emergency, to: (i) suspend temporarily or restrict sales of foreign exchange; (ii) require licensing of foreign exchange transactions; or (iii) require the delivery of foreign exchange to the BSP or its designee banks for the issuance and guarantee of foreign currency-denominated borrowings.

SMC purchases certain critical key inputs from abroad and requires foreign currency to make these purchases. There is no assurance that foreign exchange controls will not be imposed by the Philippine government in the future. Any foreign currency restrictions could severely curtail the ability of SMC to pay for certain key inputs or to meet its foreign currency payment obligations, which could materially and adversely affect its financial condition and results of operations.

Corporate governance, disclosure and financial reporting standards in the Philippines and Singapore

There may be less publicly available information about Philippine public companies, such as SMC, and securities listed on SGX-ST, such as the Notes, than is regularly made available by public companies in other countries. In addition, although SMC complies with the requirements of the Philippine SEC with respect to corporate governance standards, these standards may differ from those applicable in other jurisdictions. For example, the Philippine SEC requires public companies such as SMC to have at least two independent directors. SMC has three independent directors in compliance with Philippine laws, rules and regulations, whereas a greater number of independent directors may be required in other jurisdictions.

Enforcing judgments against SMC

SMC is organized under the laws of the Republic of the Philippines and a substantial portion of its assets are located in the Philippines. It may be difficult for investors to effect service of process outside the Philippines upon SMC with respect to claims pertaining to the offering or the Notes. Moreover, it may be difficult for investors to enforce in the Philippines judgments against it obtained outside the Philippines in any actions pertaining to the offering or the Notes, particularly with respect to actions for claims to which SMC has not consented to service of process outside the Philippines. In addition, most of its directors and officers are residents of the Philippines and all or a substantial portion of the assets of such persons are or may be located in the Philippines. As a result, it may be difficult for investors to effect service of process upon such persons outside the Philippines or enforce against such persons in the Philippines judgments obtained in courts outside the Philippines.

The Philippines is not a party to any international treaty relating to the recognition or enforcement of foreign judgments. Philippine law provides that a judgment or final order of a foreign court is enforceable in the Philippines, unless there is evidence that: (i) such judgment was obtained by collusion or fraud; (ii) the foreign court rendering such judgment did not have jurisdiction over the subject matter of the action in accordance with its jurisdictional rules; (iii) such order or judgment is contrary to Philippine laws on good customs, public order or public policy; (iv) SMC did not have notice of the proceedings before the foreign court; or (v) such judgment was based upon a clear mistake of law or fact.

Risks Relating to Certain Statistical Information in this Offering Memorandum

Certain statistical information in this Offering Memorandum relating to the Philippines, the industries and markets in which the businesses of SMC compete and other data used in this Offering Memorandum was obtained or derived from internal surveys, market research, governmental data, publicly available information and/or industry publications. Industry publications generally state that the information they contain has been obtained from sources believed to be reliable. However, there is no assurance that such information is accurate or complete. Similarly, internal surveys, industry forecasts and market research have not been independently verified by SMC and may not be accurate, complete, up-to-date, balanced or consistent with other information compiled within or outside the Philippines.

Risks Relating to Notes issued under the Programme

Under the terms of certain existing loan financings of SMC and the terms and conditions of the Notes, proceeds from the sale of interests in certain principal subsidiaries leaving SMC with an interest below 50% in such principal subsidiaries must be reinvested or used to prepay such loans and redeem the Notes

Under the terms of certain existing loan financings of SMC (including those arranged by certain of the Dealers) and the terms and conditions of the Notes, SMC must offer to purchase or repay certain financings and the Notes

if the interest of SMC in certain principal subsidiaries falls below 50% as a result of a sale of the interest of SMC in such principal subsidiaries. See “*Terms and Conditions of the Notes*.” The source of funds for any such purchase or payment would be the available cash of SMC or third-party financing. However, SMC may not have sufficient available funds at the time of such event to make purchases or payment of the outstanding Notes. The failure by SMC to make the offer to purchase or repay, or to purchase or repay, the outstanding loans and Notes would constitute an event of default under certain loan financings and the Notes. Such an event of default may, in turn, constitute an event of default under other indebtedness, any of which could cause the related debt to be accelerated after any applicable notice or grace periods. If other debt of SMC were to be accelerated, SMC may not have sufficient funds to redeem the Notes.

The Notes may not be a suitable investment for all investors

Each potential investor in any Notes must determine the suitability of that investment in light of its own circumstances. In particular, each potential investor should:

- (i) have sufficient knowledge and experience to make a meaningful evaluation of the relevant Notes, the merits and risks of investing in the relevant Notes and the information contained or incorporated by reference in this Offering Memorandum or any applicable supplement;
- (ii) have access to, and knowledge of, appropriate analytical tools to evaluate, in the context of its particular financial situation, an investment in the relevant Notes and the impact such investment will have on its overall investment portfolio;
- (iii) have sufficient financial resources and liquidity to bear all of the risks of an investment in the relevant Notes, including where principal or interest is payable in one or more currencies, or where the currency for principal or interest payments is different from the potential investor’s currency;
- (iv) understand thoroughly the terms of the relevant Notes and be familiar with the behavior of any relevant indices and financial markets; and
- (v) be able to evaluate (either alone or with the help of a financial adviser) possible scenarios for economic, interest rate and other factors that may affect its investment and its ability to bear the applicable risks.

Some Notes may be complex financial instruments and such instruments may be purchased as a way to reduce risk or enhance yield with an understood, measured, appropriate addition of risk to the purchaser’s overall portfolios. A potential investor should not invest in Notes which are complex financial instruments unless it has the expertise (either alone or with the help of a financial adviser) to evaluate how the Notes will perform under changing conditions, the resulting effects on the value of such Notes and the impact this investment will have on the potential investor’s overall investment portfolio.

Additionally, the investment activities of certain investors are subject to legal investment laws and regulations, or review or regulation by certain authorities. Each potential investor should consult its legal advisers to determine whether and to what extent (1) Notes are legal investments for it, (2) Notes can be used as collateral for various types of borrowing and (3) other restrictions apply to its purchase of any Notes. Financial institutions should consult their legal advisers or the appropriate regulators to determine the appropriate treatment of Notes under any applicable risk-based capital or similar rules.

The terms and conditions of the Notes contain provisions which may permit their modification without consent of all investors and confer significant discretions on the Trustee which may be exercised without the consent of the Noteholders and without regard to the individual interests of particular Noteholders

The terms and conditions of the Notes contain provisions for calling meetings of Noteholders to consider matters affecting their interests generally. These provisions permit defined majorities to bind all Noteholders including Noteholders who did not attend and vote at the relevant meeting and Noteholders who voted in a manner contrary to the majority.

The terms and conditions of the Notes also provide that the Trustee may agree, without the consent or sanction of Noteholders, Receiptholders or Couponholders, to any modification (except such modifications in respect of which an increased quorum is required pursuant to the terms and conditions of the Notes and the Trust Deed) of, or to the waiver or authorization of any breach or proposed breach of, any of the provisions of the Notes or the Trust Deed or the substitution of another company as principal debtor under any Notes in place of the Issuer, in the circumstances described in Condition 15 (*Meetings of Noteholders, Modification, Waiver and Substitution*).

The priority of debt evidenced by a public instrument

Under Philippine law, in the event of liquidation of a company, unsecured debt of the company (including guarantees of debt) which is evidenced by a public instrument as provided in Article 2244(14) of the Civil Code of the Philippines will rank ahead of unsecured debt of the company which is not so evidenced. Under Philippine law, a debt becomes evidenced by a public instrument when it has been acknowledged before a notary or any person authorized to administer oaths in the Philippines. Although the position is not clear under Philippine law, it is possible that a jurat (which is a statement of the circumstances in which an affidavit was made) may be sufficient to constitute a debt evidenced by a public instrument. Some of the financial indebtedness of SMC is covered by agreements which are embodied in public instruments. However, these agreements contain a waiver by each of the respective lenders of the benefit of preference or priority accorded to public instruments under Article 2244(14) of the Civil Code of the Philippines. The waivers are subject to the condition that all present and future creditors of SMC are *pari passu* and no creditor shall be conferred a superior right on the basis that its credit appear in a public instrument.

If an investor holds Notes which are not denominated in the investor's home currency, he will be exposed to movements in exchange rates adversely affecting the value of his holding. In addition, the imposition of exchange controls in relation to any Notes could result in an investor not receiving payments on those Notes

SMC will pay principal and interest on the Notes in the Specified Currency. This presents certain risks relating to currency conversions if an investor's financial activities are denominated principally in a currency or currency unit (the "Investor's Currency") other than the Specified Currency. These include the risk that exchange rates may significantly change (including changes due to devaluation of the Specified Currency or revaluation of the Investor's Currency) and the risk that authorities with jurisdiction over the Investor's Currency may impose or modify exchange controls. An appreciation in the value of the Investor's Currency relative to the Specified Currency would decrease (1) the Investor's Currency-equivalent yield on the Notes; (2) the Investor's Currency equivalent value of the principal payable on the Notes; and (3) the Investor's Currency equivalent market value of the Notes.

The Philippine government has, in the past, instituted restrictions on the conversion of Philippine Pesos into foreign currency and the use of foreign exchange received by Philippine residents to pay foreign currency denominated obligations. The Monetary Board of the BSP, with the approval of the President of the Philippines, has statutory authority, during a foreign exchange crisis or in times of national emergency, to suspend temporarily or restrict sales of foreign exchange, require licensing of foreign exchange transactions or require delivery of foreign exchange to the BSP or its designee. SMC is not aware of any pending proposals by the Philippine government regarding such restrictions. Although the Philippine government has from time to time made public pronouncements of a policy not to impose restrictions on foreign exchange, there can be no assurance that the Philippine government will maintain such policy or will not impose economic or regulatory controls that may restrict free access to foreign currency. Any such restriction imposed in the future could adversely affect the ability of investors to repatriate foreign currency upon sale of the Notes or receipt of any dividends.

The Notes may have limited liquidity

The Notes constitute a new issue of securities for which there is no existing market. Approval in-principle has been granted for the listing and quotation of the Notes that may be issued pursuant to the Programme and which are agreed at or prior to the time of issue thereof to be so listed on the SGX-ST. The offer and sale of the Notes is not conditioned on obtaining a listing of the Notes on the SGX-ST or any other exchange. Although the Dealers have advised SMC that they currently intend to make a market in the Notes, they are not obligated to do so, and any market-making activity with respect to the Notes, if commenced, may be discontinued at any time without notice in their sole discretion.

No assurance can be given as to the liquidity of, or the development and continuation of an active trading market for, the Notes. If an active trading market for the Notes does not develop or is not maintained, the market price and liquidity of the Notes may be adversely affected. If such a market were to develop, the Notes could trade at prices that may be higher or lower than the price at which the Notes are issued depending on many factors, including:

- prevailing interest rates;
- SMC results of operations and financial condition;
- political and economic developments in and affecting the Philippines;

- the market conditions for similar securities; and
- the financial condition and stability of the Philippine financial sector.

Notes where denominations involve integral multiples: definitive Notes

In relation to any issue of Notes which have denominations consisting of a minimum Specified Denomination (as specified in the applicable Pricing Supplement) plus one or more higher integral multiples of another smaller amount, it is possible that such Notes may be traded in amounts that are not integral multiples of such minimum Specified Denomination. In such a case a holder who, as a result of trading such amounts, holds an amount which is less than the minimum Specified Denomination in his account with the relevant clearing system at the relevant time may not receive a definitive Note in respect of such holding (should definitive Notes be printed) and would need to purchase a principal amount of Notes such that its holding amounts to a Specified Denomination.

Noteholders are required to rely on the procedures of the relevant clearing system and its participants while the Notes are cleared through the relevant clearing system

Notes issued under the Programme will be represented on issue by one or more Global Notes that may be deposited with a common depositary for Euroclear and Clearstream. Except in the circumstances described in each Global Note, investors will not be entitled to receive Notes in definitive form. Each of Euroclear and Clearstream and their respective direct and indirect participants will maintain records of the beneficial interests in each Global Note held through it. While the Notes are represented by a Global Note, investors will be able to trade their beneficial interests only through the relevant clearing systems and their respective participants.

While the Notes are represented by Global Notes, SMC will discharge its payment obligation under the Notes by making payments through the relevant clearing systems. A holder of a beneficial interest in a Global Note must rely on the procedures of the relevant clearing system and its participants to receive payments under the Notes. SMC has no responsibility or liability for the records relating to, or payments made in respect of, beneficial interests in any Global Note.

Holders of beneficial interests in a Global Note will not have a direct right to vote in respect of the Notes so represented. Instead, such holders will be permitted to act only to the extent that they are enabled by the relevant clearing system and its participants to appoint appropriate proxies.

If definitive Notes are issued, holders should be aware that definitive Notes that have a denomination that is not an integral multiple of the minimum Specified Denomination may be illiquid and difficult to trade.

The Notes may be subject to withholding taxes in circumstances where SMC is not obliged to make gross up payments and this would result in holders receiving less interest than expected and could significantly adversely affect their return on the Notes

Under EC Council Directive 2003/48/EC (the “Directive”) on the taxation of savings income, Member States are required to provide to the tax authorities of another Member State details of payments of interest (or similar income) paid by a person within its jurisdiction to an individual resident in that other Member State or to certain limited types of entities established in that other Member State. However, for a transitional period, Luxembourg and Austria are instead required (unless during that period they elect otherwise) to operate a withholding system in relation to such payments (the ending of such transitional period being dependent upon the conclusion of certain other agreements relating to information exchange with certain other countries). A number of non-European Union countries and territories (including Switzerland) have adopted similar measures (a withholding system in the case of Switzerland).

The European Commission has proposed certain amendments to the Directive which may, if implemented, amend or broaden the scope of the requirements described above.

If a payment were to be made or collected through a Member State which has opted for a withholding system and an amount of, or in respect of, tax were to be withheld from that payment, neither SMC nor any Paying Agent nor any other person would be obliged to pay additional amounts with respect to any Note as a result of the imposition of such withholding tax. SMC is required to maintain a Paying Agent in a Member State that is not obliged to withhold or deduct tax pursuant to the Directive.

No prior market for the Notes

The Notes are new issues of securities for which there is currently no trading market. If the Notes are traded after they are issued, they may trade at a discount from their initial offering price, depending on many factors, including prevailing interest rates, the market for similar securities, general economic conditions, and the SMC’s

financial condition, performance and prospects. Although approval in-principle has been received from the SGX-ST for permission to deal in and the listing of the Notes, SMC cannot guarantee that the application to the SGX-ST will be approved or that such listing will be maintained, or that, if listed, a liquid trading market will develop or continue. If an active trading market for the Notes does not develop or continue, the market price and liquidity of the Notes may be adversely affected. SMC may elect to apply for a de-listing of the Notes from any stock exchange or markets of such stock exchange on which they are traded because the maintenance of such listing is or would be unduly burdensome.

The credit ratings assigned to the Notes may not reflect all risks

One or more independent credit rating agencies may assign credit ratings to an issue of Notes. The ratings may not reflect the potential impact of all risks related to structure, market, additional factors discussed above and other factors that may affect the value of the Notes. A credit rating is not a recommendation to buy, sell or hold securities and may be suspended, revised or withdrawn by the rating agency at any time. A reduction or withdrawal of the ratings may adversely affect the market price of the Notes and the ability of SMC to access the debt capital markets.

Risks Relating to Renminbi-denominated Notes

Notes denominated in Renminbi (“Renminbi Notes”) may be issued under the Programme. Renminbi Notes contain particular risks for potential investors.

Renminbi is not freely convertible; there are significant restrictions on remittance of Renminbi into and outward from the PRC

Renminbi is not freely convertible at present. The PRC government continues to regulate conversion between Renminbi and foreign currencies, including the Hong Kong dollar, despite the significant reduction over the years by the PRC government of control over routine foreign exchange transactions under current accounts. Participating banks in Hong Kong have been permitted to engage in the settlement of Renminbi trade transactions under a pilot scheme introduced in July 2009. This represents a current account activity. The pilot scheme was extended in August 2011 to cover all provinces and cities in the PRC and to make Renminbi trade and other current account settlement available in all countries worldwide. Subject to limited exceptions, there is currently no specific PRC regulation on the remittance of Renminbi into the PRC for settlement of capital account. Foreign investors may only remit offshore Renminbi into the PRC for capital account purposes such as shareholders’ loan or capital contribution upon obtaining specific approvals from the relevant authorities on a case by case basis.

There is no assurance that the PRC government will continue to gradually liberalise the control over cross-border Renminbi remittances in the future, that the pilot scheme introduced in July 2009 will not be discontinued or that new PRC regulations will not be promulgated in the future which have the effect of restricting or eliminating the remittance of Renminbi into or outward from the PRC.

Further, if any new PRC regulations are promulgated in the future which have the effect of permitting or restricting (as the case may be) the remittance of Renminbi for payment of transactions categorized as capital account items, then such remittances will need to be made subject to the specific requirements or restrictions set out in such rules. In the event that funds cannot be repatriated outside the PRC in Renminbi, SMC will need to source Renminbi offshore to finance its obligations under the Notes, and its ability to do so will be subject to the overall availability of Renminbi outside the PRC.

Holders of beneficial interests in the Notes denominated in Renminbi may be required to provide certifications and other information (including Renminbi account information) in order to allow such holder to receive payments in Renminbi in accordance with the Renminbi clearing and settlement mechanism for participating banks in Hong Kong.

There is only limited availability of Renminbi outside the PRC, which may affect the liquidity of Renminbi Notes and the ability of SMC to source Renminbi outside the PRC to service such Renminbi Notes

As a result of the restrictions by the PRC Government on cross-border Renminbi fund flows, the availability of Renminbi outside the PRC is limited. Since February 2004, in accordance with arrangements between the PRC Central Government and the Hong Kong Government, licensed banks in Hong Kong may offer limited Renminbi-denominated banking services to Hong Kong residents and designated business customers. The People’s Bank of China (“PBOC”) has also established a Renminbi clearing and settlement mechanism for participating banks in Hong Kong. On July 19, 2010, further amendments were made to the Settlement

Agreement on the Clearing of RMB Business (the “Settlement Agreement”) between the PBOC and Bank of China (Hong Kong) Limited as the RMB clearing bank (the “RMB Clearing Bank”) to further expand the scope of Renminbi business for participating banks in Hong Kong. Pursuant to the revised arrangements, all corporations are allowed to open Renminbi accounts in Hong Kong; there is no longer any limit on the ability of corporations to convert RMB; and there is no longer any restriction on the transfer of Renminbi funds between different accounts in Hong Kong.

However, the current size of Renminbi-denominated financial assets outside the PRC is limited. As of February 2013, the total amount of Renminbi deposits held by institutions authorized to engage in Renminbi banking business in Hong Kong amounted to approximately RMB651.7 billion (source: Hong Kong Monetary Authority Monthly Statistical Bulletin). In addition, participating banks are also required by the Hong Kong Monetary Authority (“HKMA”) to maintain a liquidity ratio at not less than 25%. (computed on the same basis as the statutory liquidity ratio), which further limits the availability of Renminbi that participating banks can utilize for conversion services for their customers. Renminbi business participating banks do not have direct Renminbi liquidity support from the PBOC. They are only allowed to square their open positions with the RMB Clearing Bank after consolidating the RMB trade position of banks outside Hong Kong that are in the same bank group of the participating banks concerned with their own trade position, and the RMB Clearing Bank only has access to onshore liquidity support from the PBOC only for the purpose of squaring open positions of participating banks for limited types of transactions, including open positions resulting from conversion services for corporations relating to cross-border trade settlement, for Hong Kong residents of up to RMB20,000 per person per day and for the designated business customers relating to the RMB received in providing their services. The RMB Clearing Bank is not obliged to square for participating banks any open positions resulting from other foreign exchange transactions or conversion services and the participating banks will need to source Renminbi from the offshore market to square such open positions.

On June 14, 2012, the HKMA introduced a facility for providing Renminbi liquidity to authorized institutions participating in RMB business (“Participating AIs”) in Hong Kong. The facility will make use of the currency swap arrangement between the PBOC and the HKMA. With effect from June 15, 2012, the HKMA will, in response to requests from individual Participating AIs, provide RMB term funds to the Participating AIs against eligible collateral acceptable to the HKMA. The facility is intended to address short-term RMB liquidity tightness which may arise from time to time, for example due to capital market activities or sudden need for RMB liquidity by the Participating AIs’ overseas bank customers.

Although it is expected that the offshore Renminbi market will continue to grow in depth and size, its growth is subject to many constraints as a result of PRC laws and regulations on foreign exchange. There is no assurance that no new PRC regulations will be promulgated or the Settlement Agreement will not be terminated or amended in the future which will have the effect of restricting availability of Renminbi offshore. The limited availability of Renminbi outside the PRC may affect the liquidity of its Renminbi Notes. To the extent SMC is required to source Renminbi in the offshore market to service its Renminbi Notes, there is no assurance that SMC will be able to source such Renminbi on satisfactory terms, if at all.

Investment in Renminbi Notes is subject to exchange rate risks

The value of Renminbi against the U.S. dollar and other foreign currencies fluctuates and is affected by changes in the PRC and international political and economic conditions and by many other factors. Subject to the applicable Pricing Supplement and Terms and Conditions, all payments of interest and principal with respect to Renminbi Notes will be made in Renminbi. As a result, the value of these Renminbi payments in U.S. dollar terms may vary with the prevailing exchange rates in the marketplace. If the value of Renminbi depreciates against the U.S. dollar or other foreign currencies, the value of investment in U.S. dollar or other applicable foreign currency terms will decline.

Payments in respect of Renminbi Notes will only be made to investors in the manner specified in such Renminbi Notes

All payments to investors in respect of Renminbi Notes will be made solely by (i) when Renminbi Notes are represented by global certificates, transfer to a Renminbi bank account maintained in Hong Kong in accordance with prevailing Euroclear and/or Clearstream rules and procedures, or (ii) when Renminbi Notes are in definitive form, transfer to a Renminbi bank account maintained in Hong Kong in accordance with prevailing rules and regulations. SMC cannot be required to make payment by any other means (including, but not limited to, in any other currency, by bank notes, by cheques or drafts or by transferring to a bank account in the PRC).

Risks relating to the structure of a particular issue of Notes

A wide range of Notes may be issued under the Programme. A number of these Notes may have features which contain particular risks for potential investors. Set out below is a description of certain such features:

Notes subject to optional redemption by SMC

An optional redemption feature of Notes is likely to limit their market value. During any period when SMC may elect to redeem Notes, the market value of those Notes generally will not rise substantially above the price at which they can be redeemed. This also may be true prior to any redemption period.

SMC may be expected to redeem Notes when its cost of borrowing is lower than the interest rate on the Notes. At those times, an investor generally would not be able to reinvest the redemption proceeds at an effective interest rate as high as the interest rate on the Notes being redeemed and may only be able to do so at a significantly lower rate. Potential investors should consider reinvestment risk in light of other investments available at that time.

Index Linked Notes and Dual Currency Notes

SMC may issue Notes with principal or interest determined by reference to an index or formula, to changes in the prices of securities or commodities, to movements in currency exchange rates or other factors (each, a “Relevant Factor”). In addition, SMC may issue Notes with principal or interest payable in one or more currencies which may be different from the currency in which the Notes are denominated. Potential investors should be aware that:

- (a) the market price of such Notes may be volatile;
- (b) they may receive no interest;
- (c) payment of principal or interest may occur at a different time or in a different currency than expected;
- (d) they may lose all or a substantial portion of their principal;
- (e) a Relevant Factor may be subject to significant fluctuations that may not correlate with changes in interest rates, currencies or other indices;
- (f) if a Relevant Factor is applied to Notes in conjunction with a multiplier greater than one or contains some other leverage factor, the effect of changes in the Relevant Factor on principal or interest payable likely will be magnified; and
- (g) the timing of changes in a Relevant Factor may affect the actual yield to investors, even if the average level is consistent with their expectations. In general, the earlier the change in the Relevant Factor, the greater the effect on yield.

The historical experience of an index or other Relevant Factor should not be viewed as an indication of the future performance of such Relevant Factor during the term of any Notes. Accordingly, each potential investor should consult its own financial and legal advisers about the risk entailed by an investment in any Notes linked to such a Relevant Factor and the suitability of such Notes in light of its particular circumstances.

Partly-paid Notes

SMC may issue Notes where the issue price is payable in more than one installment. Any failure by an investor to pay any subsequent installment of the issue price in respect of the Notes could result in an investor losing all of his investment.

Variable rate Notes with a multiplier or other leverage factor

Notes with variable interest rates can be volatile investments. If they are structured to include multipliers or other leverage factors, or caps or floors, or any combination of those features or other similar related features, their market values may be even more volatile than those for securities that do not include those features.

Inverse Floating Rate Notes

Inverse Floating Rate Notes have an interest rate equal to a fixed rate minus a rate based upon a reference rate such as LIBOR. The market values of those Notes typically are more volatile than market values of other conventional floating rate debt securities based on the same reference rate (and with otherwise comparable terms). Inverse Floating Rate Notes are more volatile because an increase in the reference rate not only decreases the interest rate of the Notes, but may also reflect an increase in prevailing interest rates, which further adversely affects the market value of these Notes.

Fixed/Floating Rate Notes

Fixed/Floating Rate Notes are Notes which may bear interest at a rate that converts from a fixed rate to a floating rate, or from a floating rate to a fixed rate. Where SMC has the right to effect such a conversion, this will affect the secondary market and the market value of the Notes since SMC may be expected to convert the rate when it is likely to produce a lower overall cost of borrowing. If SMC converts from a fixed rate to a floating rate in such circumstances, the spread on the Fixed/Floating Rate Notes may be less favorable than then prevailing spreads on comparable Floating Rate Notes tied to the same reference rate. In addition, the new floating rate at any time may be lower than the rates on other Notes. If SMC converts from a floating rate to a fixed rate in such circumstances, the fixed rate may be lower than then prevailing rates on its Notes.

Notes issued at a substantial discount or premium

The market values of securities issued at a substantial discount (such as Zero Coupon Notes) or premium to their principal amount tend to fluctuate more in relation to general changes in interest rates than do prices for conventional interest-bearing securities. Generally, the longer the remaining term of the securities, the greater the price volatility as compared to more conventional interest-bearing securities with comparable maturities.

FORM OF THE NOTES

The Notes of each Series will be in either bearer form, with or without interest coupons (“Coupons”) attached, or registered form, without Coupons attached. Bearer Notes will be issued outside the United States to non-U.S. persons in reliance on Regulation S. Registered Notes will be issued outside the United States (and in the case of Notes offered or sold in reliance on Category 2 of Regulation S, to non-U.S. persons) in reliance on Regulation S.

Notes to be listed on the SGX-ST will be accepted for clearance through Euroclear and/or Clearstream and may also be accepted for clearance through the CMU and/or any other clearing system as specified in the applicable Pricing Supplement.

Bearer Notes

Each Tranche of Bearer Notes will be initially issued in the form of either a Temporary Bearer Global Note or a Permanent Bearer Global Note (collectively, the “Bearer Global Notes” and each a “Bearer Global Note”) as indicated in the applicable Pricing Supplement, which, in either case, will be delivered on or prior to the original issue date of the Tranche to either (i) a common depository (the “Common Depository”) for Euroclear and Clearstream or (ii) a sub-custodian for the Hong Kong Monetary Authority (“HKMA”), as operator of the CMU. Whilst any Bearer Note is represented by a Temporary Bearer Global Note, payments of principal, interest (if any) and any other amount payable in respect of the Notes due prior to the Exchange Date (as defined below) will be made against presentation of the Temporary Bearer Global Note only to the extent that certification (in a form to be provided) to the effect that the beneficial owners of interests in such Bearer Note are not U.S. persons or persons who have purchased for resale to any U.S. person, as required by U.S. Treasury regulations, has been received by Euroclear and/or Clearstream and/or Deutsche Bank AG, Hong Kong Branch (the “CMU Lodging Agent”) and (in the case of a Temporary Bearer Global Note delivered to a Common Depository for Euroclear and Clearstream) Euroclear and/or Clearstream, as applicable, has given a like certification (based on the certifications it has received) to the Principal Paying Agent (as defined under “*Terms and Conditions of the Notes*”).

On and after the date (the “Exchange Date”) which, for each Tranche in respect of which a Temporary Bearer Global Note is issued, is 40 days after a Temporary Bearer Global Note is issued, interests in such Temporary Bearer Global Note will be exchangeable (free of charge) upon a request as described therein either for (i) interests in a Permanent Bearer Global Note of the same Series or (ii) definitive Bearer Notes of the same Series with, where applicable, receipts, interest coupons and talons attached (as indicated in the applicable Pricing Supplement and subject, in the case of definitive Bearer Notes, to such notice period as is specified in the applicable Pricing Supplement), in each case against certification of beneficial ownership as described above, unless such certification has already been given. The CMU may require that any such exchange for a Permanent Bearer Global Note is made in whole and not in part and in such event, no such exchange will be effected until all relevant account holders (as set out in a CMU Instrument Position Report (as defined in the rules of the CMU) or any other relevant notification supplied to the CMU Lodging Agent by the CMU) have so certified. The CMU may require the issue and deposit of such Permanent Bearer Global Note with its sub-custodian without permitting the withdrawal of the Temporary Bearer Global Note so exchanged, although any interests thereon exchanged shall have been properly effected in its records.

The holder of a Temporary Bearer Global Note will not be entitled to collect any payment of interest, principal or other amount due on or after the Exchange Date unless, upon due certification, exchange of the Temporary Bearer Global Note for an interest in a Permanent Bearer Global Note or for definitive Bearer Notes is improperly withheld or refused. Payments of principal, interest (if any) or any other amounts on a Permanent Bearer Global Note will be made through Euroclear and/or Clearstream against presentation or surrender (as the case may be) of the Permanent Bearer Global Note without any requirement for certification.

In respect of a Bearer Global Note held through the CMU, any payments of principal, interest (if any) or any other amounts shall be made to the person(s) for whose account(s) interests in the relevant Bearer Global Note are credited (as set out in a CMU Instrument Position Report or any other relevant notification supplied to the CMU Lodging Agent by the CMU) and, save in the case of final payment, no presentation of the relevant Bearer Global Note shall be required for such purpose.

The applicable Pricing Supplement will specify that a Permanent Bearer Global Note will be exchangeable (free of charge), in whole but not in part, for definitive Bearer Notes with, where applicable, receipts, interest coupons and talons, attached upon either (i) not less than 60 days’ written notice (a), in the case of Notes held by a Common Depository for Euroclear and/or Clearstream, from Euroclear and/or Clearstream (acting on the instructions of any holder of an interest in such Permanent Bearer Global Note) to the Principal Paying Agent as described therein and/or (b), in the case of Notes held through the CMU, from the relevant account holders therein to the CMU Lodging Agent as described therein, or (ii) only upon the occurrence of an Exchange Event.

For these purposes, “Exchange Event” means that (i) an Event of Default (as defined in Condition 10.1) has occurred and is continuing, (ii) SMC has been notified that both Euroclear and Clearstream and, in the case of Notes cleared through the CMU, the CMU have been closed for business for a continuous period of 14 days (other than by reason of holiday, statutory or otherwise) or have announced an intention permanently to cease business or have in fact done so and, in any case, no successor clearing system satisfactory to the Trustee is available or (iii) SMC has or will become subject to adverse tax consequences which would not be suffered were the Notes in definitive form and a certificate to such effect signed by two authorized signatories of SMC has been given to the Trustee. SMC will promptly give notice to Noteholders in accordance with Condition 14 if an Exchange Event occurs. In the event of the occurrence of an Exchange Event, (a) in the case of Notes held by a Common Depositary for Euroclear and/or Clearstream, Euroclear and/or Clearstream on their behalf (acting on the instructions of any holder of an interest in such Permanent Bearer Global Note) or, (b) in the case of Notes held through the CMU, the relevant account holders therein or, in either case, the Trustee may give notice to the Principal Paying Agent or, as the case may be, the CMU Lodging Agent requesting exchange and, in the event of the occurrence of an Exchange Event as described in (iii) above, SMC may also give notice to the Principal Paying Agent or, as the case may be, the CMU Lodging Agent requesting exchange. Any such exchange shall occur not later than 45 days after the date of receipt of the first relevant notice by the Principal Paying Agent or, as the case may be, the CMU Lodging Agent.

The following legend will appear on all Bearer Notes which have an original maturity of more than 365 days and on all receipts and interest coupons relating to such Notes:

“ANY UNITED STATES PERSON (AS DEFINED IN THE INTERNAL REVENUE CODE OF THE UNITED STATES) WHO HOLDS THIS OBLIGATION WILL BE SUBJECT TO LIMITATIONS UNDER THE UNITED STATES INCOME TAX LAWS, INCLUDING THE LIMITATIONS PROVIDED IN SECTIONS 165(j) AND 1287(a) OF THE INTERNAL REVENUE CODE.”

The sections referred to provide that United States holders, with certain exceptions, will not be entitled to deduct any loss on Bearer Notes, receipts or interest coupons and will not be entitled to capital gains treatment of any gain on any sale, disposition, redemption or payment of principal in respect of such Notes, receipts or interest coupons.

Notes which are represented by a Bearer Global Note will only be transferable in accordance with the rules and procedures for the time being of Euroclear, Clearstream or the CMU, as the case may be.

For the purpose of any payments made in respect of a Bearer Global Note, the relevant place of presentation shall be disregarded in the definition of “Payment Day” set out in Condition 6.6.

Registered Notes

The Registered Notes of each Tranche will initially be represented by a Registered Global Note. Prior to expiry of the distribution compliance period (as defined in Regulation S), if any, applicable to each Tranche of Notes, beneficial interests in a Registered Global Note may not be offered or sold to, or for the account or benefit of, a U.S. person save as otherwise provided in Condition 2.1 and may not be held otherwise than through Euroclear or Clearstream or the CMU and such Registered Global Note will bear a legend regarding such restrictions on transfer.

Registered Global Notes will (i) be deposited with, and registered in the name of a nominee of, a Common Depositary for Euroclear and Clearstream or (ii) be deposited with a sub-custodian for and registered in the name of the HKMA as operator of the CMU, as specified in the applicable Pricing Supplement. Persons holding beneficial interests in Registered Global Notes will be entitled or required, as the case may be, under the circumstances described below, to receive physical delivery of definitive Notes in fully registered form.

Payments of principal, interest and any other amount in respect of the Registered Global Notes will, in the absence of provision to the contrary, be made to the person shown on the Register (as defined in Condition 6.4) as the registered holder of the Registered Global Notes. None of SMC, the Trustee, the Principal Paying Agent, any Paying Agent or the Registrar will have any responsibility or liability for any aspect of the records relating to or payments or deliveries made on account of beneficial ownership interests in the Registered Global Notes or for maintaining, supervising or reviewing any records relating to such beneficial ownership interests.

Payments of principal, interest or any other amount in respect of the Registered Notes in definitive form will, in the absence of provision to the contrary, be made to the persons shown on the Register on the relevant Record Date (as defined in Condition 6.4) immediately preceding the due date for payment in the manner provided in that Condition.

All payments in respect of Notes represented by a Registered Global Note will be made to, or to the order of, the person whose name is entered on the Register at the close of business on the clearing system business day (being a day on which the relevant clearing system is open for business) immediately prior to the date for payment.

Interests in a Registered Global Note will be exchangeable (free of charge), in whole but not in part, for definitive Registered Notes without receipts, interest coupons or talons attached only upon the occurrence of an Exchange Event. For these purposes, “Exchange Event” means that (i) an Event of Default has occurred and is continuing, (ii) SMC has been notified that both Euroclear and Clearstream and, in the case of Notes cleared through the CMU, the CMU have been closed for business for a continuous period of 14 days (other than by reason of holiday, statutory or otherwise) or have announced an intention permanently to cease business or have in fact done so and, in any case, no successor clearing system satisfactory to the Trustee is available or (iii) SMC has or will become subject to adverse tax consequences which would not be suffered were the Notes in definitive form and a certificate to such effect from two Authorized Signatories of SMC has been given to the Trustee. SMC will promptly give notice to Noteholders in accordance with Condition 14 if an Exchange Event occurs. In the event of the occurrence of an Exchange Event, (a) in the case of Notes registered in the name of a nominee for a Common Depositary for Euroclear and/or Clearstream, Euroclear and/or Clearstream or any person acting on their behalf (acting on the instructions of any holder of an interest in such Registered Global Note) and/or, (b) in the case of Notes held through the CMU, the relevant account holders therein, may give notice to the Registrar or, as the case may be, the CMU Lodging Agent requesting exchange and, in the event of the occurrence of an Exchange Event as described in (iii) above, SMC may also give notice to the Registrar or, as the case may be, the CMU Lodging Agent requesting exchange. Any such exchange shall occur not later than 10 days after the date of receipt of the first relevant notice by the Registrar or, as the case may be, the CMU Lodging Agent.

Notices

While the Notes are represented by a Global Note and such Global Note is deposited with a common depositary for Euroclear or Clearstream or CMU, notices to the Noteholders may be given by delivery of the relevant notice to Euroclear or Clearstream or CMU and, in any case, such notices shall be deemed to have been given to the Noteholders in accordance with Condition 14 on the date of delivery to Euroclear or Clearstream or CMU.

Transfer of Interests

Interests in a Registered Global Note may, subject to compliance with all applicable restrictions, be transferred to a person who wishes to hold such interest in another Registered Global Note. No beneficial owner of an interest in a Registered Global Note will be able to transfer such interest, except in accordance with the applicable procedures of Euroclear, Clearstream and the CMU, in each case to the extent applicable. **Registered Notes are also subject to the restrictions on transfer set out therein and will bear a legend regarding such restrictions. See “Subscription and Sale.”**

General

Pursuant to the Agency Agreement (as defined under “*Terms and Conditions of the Notes*”), the Principal Paying Agent or, as the case may be, the CMU Lodging Agent shall, if applicable, arrange that, where a further Tranche of Notes is issued which is intended to form a single Series with an existing Tranche of Notes, the Notes of such further Tranche shall be assigned a common code and ISIN and, where applicable, a CMU instrument number which are different from the common code, ISIN and CMU instrument number assigned to Notes of any other Tranche of the same Series until at least the expiry of the distribution compliance period (as defined in Regulation S) applicable to the Notes of such Tranche.

For so long as any of the Notes is represented by a Global Note held on behalf of Euroclear, Clearstream or the CMU, each person (other than Euroclear, Clearstream or the CMU) who is for the time being shown in the records of Euroclear, Clearstream or the CMU as the holder of a particular nominal amount of such Notes (in which regard any certificate or other document issued by Euroclear, Clearstream or the CMU as to the nominal amount of such Notes standing to the account of any person shall be conclusive and binding for all purposes save in the case of manifest error) shall be treated by SMC, the Trustee, the Agents and their respective agents as the holder of such nominal amount of such Notes for all purposes other than with respect to the payment of principal or interest on such nominal amount of such Notes, for which purpose the bearer of the relevant Bearer Global Note or the registered holder of the relevant Registered Global Note shall be treated by SMC, the Trustee, the Agents and their respective agents as the holder of such nominal amount of such Notes in accordance with and subject to the terms of the relevant Global Note and the expressions “Noteholder” and “holder of Notes” and related expressions shall be construed accordingly. Notwithstanding the above, if a Note (whether in global or definitive form) is held through the CMU, any payment that is made in respect of such Note shall be made at the direction of the bearer or the registered holder to the person(s) for whose account(s) interests in such Note are credited as being held through the CMU in accordance with the CMU Rules (as defined in the Agency Agreement) at the relevant time as notified to the CMU Lodging Agent by the CMU in a relevant CMU

Instrument Position Report or any other relevant notification by the CMU (which notification, in either case, shall be conclusive evidence of the records of the CMU as to the identity of any accountholder and the principal amount of any Note credited to its account, save in the case of manifest error) and such payments shall discharge the obligation of SMC in respect of that payment under such Note.

Any reference herein to Euroclear and/or Clearstream and/or the CMU shall, whenever the context so permits, be deemed to include a reference to any additional or alternative clearing system specified in the applicable Pricing Supplement or otherwise approved by SMC, the Principal Paying Agent, the Trustee and, as applicable, the Registrar. No Noteholder, Receiptholder or Couponholder (as defined under “*Terms and Conditions of the Notes*”) shall be entitled to proceed directly against SMC unless the Trustee, having become bound so to proceed, fails so to do within a reasonable period and the failure shall be continuing.

For so long as any Notes are listed on the SGX-ST and the rules of the SGX-ST so require, SMC shall appoint and maintain a paying agent in Singapore, where such Notes may be presented or surrendered for payment or redemption, in the event that the Global Note(s) representing such Notes is exchanged for definitive Notes. In addition, in the event that the Global Note(s) is exchanged for definitive Notes, an announcement of such exchange will be made by or on behalf of SMC through the SGX-ST and such announcement will include all material information with respect to the delivery of the definitive Notes, including details of the paying agent in Singapore.

TERMS AND CONDITIONS OF THE NOTES

The following are the Terms and Conditions of the Notes which will be incorporated by reference into each Global Note (as defined below) and each definitive Note, in the latter case only if permitted by the relevant stock exchange or other relevant authority (if any) and agreed by the Issuer and the relevant Dealer at the time of issue but, if not so permitted and not so agreed, such definitive Note will have endorsed thereon or attached thereto such Terms and Conditions. The applicable Pricing Supplement in relation to any Tranche of Notes may specify other terms and conditions which shall, to the extent so specified or to the extent inconsistent with the following Terms and Conditions, replace or modify the following Terms and Conditions for the purpose of such Notes. The applicable Pricing Supplement (or the relevant provisions thereof) will be endorsed upon, or attached to, each Global Note and definitive Note. Reference should be made to "Form of the Notes" for a description of the content of Pricing Supplements which will specify which of such terms are to apply in relation to the relevant Notes.

This Note is one of a Series (as defined below) of Notes issued by San Miguel Corporation (the **Issuer**), and constituted by a trust deed dated April 15, 2013 (such trust deed as modified and/or supplemented and/or restated from time to time, the **Trust Deed**) made between the Issuer and DB Trustees (Hong Kong) Limited (the **Trustee**, which expression shall include any additional or successor Trustee).

References herein to the **Notes** shall be references to the Notes of this Series and shall mean:

- (i) in relation to any Notes represented by a global Note (a **Global Note**), units of each Specified Denomination in the currency specified therein or, if none is specified, the currency in which the Notes are denominated (the **Specified Currency**);
- (ii) any Global Note in bearer form (a **Bearer Global Note**);
- (iii) any Global Note in registered form (a **Registered Global Note**);
- (iv) definitive Notes in bearer form (**Definitive Bearer Notes**, and together with Bearer Global Notes, the **Bearer Notes**) issued in exchange for a Bearer Global Note; and
- (v) definitive Notes in registered form (**Definitive Registered Notes**, and together with Registered Global Notes, the **Registered Notes**), whether or not issued in exchange for a Registered Global Note.

The Notes, the Receipts (as defined below) and the Coupons (as defined below) have the benefit of an agency agreement dated April 15, 2013 (such agency agreement as amended and/or supplemented and/or restated from time to time, the **Agency Agreement**) and made between the Issuer, the Trustee, Deutsche Bank AG, Hong Kong Branch as principal paying agent (the **Principal Paying Agent**, which expression shall include any successor principal paying agent), as CMU lodging agent (the **CMU Lodging Agent**, which expression shall include any successor CMU lodging agent), any additional paying agents appointed in accordance with the Agency Agreement (together with the Principal Paying Agent and the CMU Lodging Agent, the **Paying Agents**, which expression shall include any additional or successor paying agents), as transfer agent (the **Transfer Agent**, which expression shall include any additional or successor transfer agents appointed in accordance with the Agency Agreement) and as registrar (the **Registrar**, which expression shall include any successor registrar and, together with the Paying Agents, the CMU Lodging Agent and Transfer Agents, the **Agents**). For the purposes of these Terms and Conditions (the **Conditions**), all references (other than in relation to the determination of interest and other amounts payable in respect of the Notes) to the Principal Paying Agent shall, with respect to a Series of Notes to be held in the CMU (as defined below), be deemed to be a reference to the CMU Lodging Agent and all such references shall be construed accordingly.

Interest bearing Definitive Bearer Notes (unless otherwise indicated in the applicable Pricing Supplement) have interest coupons (**Coupons**) and, if indicated in the applicable Pricing Supplement, talons for further Coupons (**Talons**) attached on issue. Any reference herein to Coupons or coupons shall, unless the context otherwise requires, be deemed to include a reference to Talons or talons. Definitive Bearer Notes repayable in installments have receipts (**Receipts**) for the payment of the installments of principal (other than the final installment) attached on issue. Registered Notes and Global Notes do not have Receipts, Coupons or Talons attached on issue.

The Pricing Supplement for this Note (or the relevant provisions thereof) is attached to or endorsed on this Note and supplements these Conditions and may specify other terms and conditions which shall, to the extent so specified or to the extent inconsistent with these Conditions, replace or modify these Conditions for the purposes of this Note. References to the **applicable Pricing Supplement** are to the Pricing Supplement (or the relevant provisions thereof) attached to or endorsed on this Note.

The Trustee acts for the benefit of the Noteholders (which expression shall mean (in the case of Bearer Notes) the holders of the Notes and (in the case of Registered Notes) the persons in whose name the Notes are registered

and shall, in relation to any Notes represented by a Global Note, be construed as provided below), the holders of the Receipts (the **Receiptholders**) and the holders of the Coupons (the **Couponholders**, which expression shall, unless the context otherwise requires, include the holders of the Talons), in accordance with the provisions of the Trust Deed.

As used herein, **Tranche** means Notes which are identical in all respects (including as to listing and admission to trading) and **Series** means a Tranche of Notes together with any further Tranche or Tranches of Notes which are (i) expressed to be consolidated and form a single series and (ii) identical in all respects (including as to listing) except for their respective Issue Dates, (unless this is a Zero Coupon Note) Interest Commencement Dates and/or Issue Prices.

Copies of the Trust Deed and the Agency Agreement are available for inspection during normal business hours at the registered office for the time being of the Trustee (being Level 52, International Commerce Centre, 1 Austin Road West, Kowloon, Hong Kong) and at the specified office of each of the Principal Paying Agent, the other Paying Agents and the CMU Lodging Agent. Copies of the applicable Pricing Supplement are obtainable during normal business hours at the specified office of each of the Paying Agents save that, if this Note is an unlisted Note of any Series, the applicable Pricing Supplement will only be obtainable by a Noteholder holding one or more unlisted Notes of that Series and such Noteholder must produce evidence satisfactory to the Issuer, the Trustee and the relevant Agent as to its holding of such Notes and identity. The Noteholders, the Receiptholders and the Couponholders are deemed to have notice of, and are entitled to the benefit of, and are bound by, all the provisions of the Trust Deed, the Agency Agreement and the applicable Pricing Supplement which are applicable to them. The statements in these Conditions include summaries of, and are subject to, the detailed provisions of the Trust Deed and the Agency Agreement.

Words and expressions defined in the Trust Deed and the Agency Agreement or used in the applicable Pricing Supplement shall have the same meanings where used in these Conditions unless the context otherwise requires or unless otherwise stated and provided that, in the event of inconsistency between the Trust Deed and the Agency Agreement, the Trust Deed will prevail and, in the event of inconsistency between the Trust Deed or the Agency Agreement and the applicable Pricing Supplement, the applicable Pricing Supplement will prevail.

1. FORM, DENOMINATION AND TITLE

1.1 Form and Denomination

The Notes may be in bearer form and/or in registered form and, in the case of definitive Notes, will be serially numbered, in the currency (the **Specified Currency**) and the denominations (the **Specified Denomination(s)**) specified in the applicable Pricing Supplement. Notes of one Specified Denomination may not be exchanged for Notes of another Specified Denomination and Bearer Notes may not be exchanged for Registered Notes and *vice versa*.

This Note may be a Fixed Rate Note, a Floating Rate Note, a Zero Coupon Note, an Index Linked Interest Note, a Dual Currency Interest Note or a combination of any of the foregoing, depending upon the Interest Basis shown in the applicable Pricing Supplement.

This Note may be an Index Linked Redemption Note, an Installment Note, a Dual Currency Redemption Note, a Partly Paid Note or a combination of any of the foregoing, depending upon the Redemption/Payment Basis shown in the applicable Pricing Supplement.

Definitive Bearer Notes are issued with Coupons and (if applicable) Receipts and Talons attached, unless they are Zero Coupon Notes in which case references to Coupons and Couponholders in these Conditions are not applicable.

1.2 Title

Subject as set out below, title to the Bearer Notes, Receipts and Coupons will pass by delivery. Title to Registered Notes will pass upon registration of transfers in the books of the Registrar in accordance with the provisions of the Agency Agreement. The Issuer, the Trustee, the Principal Paying Agent, any Paying Agent, the Registrar and the Transfer Agent will (except as otherwise ordered by a court of competent jurisdiction or required by law) deem and treat the bearer of any Bearer Note, Receipt or Coupon and any person in whose name a Registered Note is registered as the absolute owner thereof (whether or not overdue and notwithstanding any notice of ownership or writing thereon or notice of any previous loss or theft thereof) for all purposes but, in the case of any Global Note, without prejudice to the provisions set out in the next succeeding paragraph.

For so long as any of the Notes is represented by a Global Note held by a common depositary on behalf of Euroclear Bank SA/NV (**Euroclear**) and/or Clearstream, Banking, société anonyme (**Clearstream**,

Luxembourg) and/or a sub-custodian for the Central Moneymarkets Unit Service (the **CMU**) operated by the Hong Kong Monetary Authority (the **HKMA**), each person (other than Euroclear, Clearstream, Luxembourg or the CMU) who is for the time being shown in the records of Euroclear, Clearstream, Luxembourg or the CMU as the holder of a particular nominal amount of such Notes (in which regard any certificate or other document issued by Euroclear, Clearstream, Luxembourg or the CMU as to the nominal amount of such Notes standing to the account of any person shall be conclusive and binding for all purposes save in the case of manifest error) shall be treated by the Issuer, the Trustee and any agent as the holder of such nominal amount of such Notes for all purposes other than with respect to the payment of principal or interest on such nominal amount of such Notes, for which purpose the bearer or registered holder of the relevant Global Note shall be treated by the Issuer, the Trustee and any agent as the holder of such nominal amount of such Notes in accordance with and subject to the terms of the relevant Global Note and the expressions **Noteholder** and **holder of Notes** and related expressions shall be construed accordingly. In determining whether a particular person is entitled to a particular nominal amount of Notes, as aforesaid, the Trustee may rely on such evidence and/or information and/or certification as it shall, in its absolute discretion, think fit and, if it does so rely, such evidence and/or information and/or certification shall, in the absence of manifest error, be conclusive and binding on all concerned.

Notwithstanding the above, if a Note (whether in global or definitive form) is held through the CMU, any payment that is made in respect of such Note shall be made at the direction of the bearer or the registered holder to the person(s) for whose account(s) interests in such Note are credited as being held through the CMU in accordance with the CMU Rules (as defined in the Agency Agreement) at the relevant time as notified to the CMU Lodging Agent by the CMU in a relevant CMU Instrument Position Report (as defined in the Agency Agreement) or any other relevant notification by the CMU (which notification, in either case, shall be conclusive evidence of the records of the CMU as to the identity of any accountholder and the principal amount of any Note credited to its account, save in the case of manifest error) (**CMU Accountholders**) and such payments shall discharge the obligation of the Issuer in respect of that payment under such Note.

Notes which are represented by a Global Note will be transferable only in accordance with the rules and procedures for the time being of Euroclear, Clearstream, Luxembourg and/or the CMU, as the case may be. References to Euroclear and/or Clearstream, Luxembourg and/or the CMU shall, whenever the context so permits, be deemed to include a reference to any additional or alternative clearing system specified in the applicable Pricing Supplement or as may otherwise be approved by the Issuer, the Trustee and the Principal Paying Agent.

2. TRANSFERS OF REGISTERED NOTES

2.1 Transfers of Interests in Registered Global Notes

Transfers of beneficial interests in Registered Global Notes will be effected by Euroclear Clearstream, Luxembourg or the CMU, as the case may be, and, in turn, by other participants and, if appropriate, indirect participants in such clearing systems acting on behalf of beneficial transferors and transferees of such interests. A beneficial interest in a Registered Global Note will, subject to compliance with all applicable legal and regulatory restrictions, be exchangeable for Registered Notes in definitive form only in the authorised denominations set out in the applicable Pricing Supplement and only in accordance with the rules and operating procedures for the time being of Euroclear Clearstream, Luxembourg or the CMU, as the case may be, and in accordance with the terms and conditions specified in the Trust Deed and the Agency Agreement. Transfers of a Registered Global Note registered in the name of a nominee for Euroclear, Clearstream, Luxembourg or the CMU shall be limited to transfers of such Registered Global Note, in whole but not in part, to another nominee of Euroclear, Clearstream, Luxembourg or the CMU or to a successor of Euroclear, Clearstream, Luxembourg or the CMU or such successor's nominee.

2.2 Transfers of Registered Notes Generally

Registered Notes may not be exchanged for Bearer Notes and *vice versa*.

Upon the terms and subject to the conditions set forth in the Trust Deed and the Agency Agreement, a Definitive Registered Note may be transferred in whole or in part (in the authorised denominations set out in the applicable Pricing Supplement). In order to effect any such transfer: (i) the holder or holders must (a) surrender the Definitive Registered Note for registration of the transfer of the Definitive Registered Note (or the relevant part of the Definitive Registered Note) at the specified office of the Registrar or any Transfer Agent, with the form of transfer thereon duly executed by the holder or holders thereof or his or their attorney or attorneys duly authorised in writing and (b) complete and deposit such other certifications

as may be required by the relevant Transfer Agent and (ii) the Registrar or, as the case may be, the relevant Transfer Agent must, after due and careful enquiry, be satisfied with the documents of title and the identity of the person making the request. Any such transfer will be subject to such reasonable regulations as the Issuer, the Trustee, the Registrar, or as the case may be, the relevant Transfer Agent may prescribe (such initial regulations being set out in Schedule 6 to the Agency Agreement), subject to changes as may be agreed between the Issuer, the Registrar and the Trustee. Subject as provided above, the Registrar or, as the case may be, the relevant Transfer Agent will, within three business days (being for this purpose a day on which banks are open for business in the city where the specified office of the Registrar or, as the case may be, the relevant Transfer Agent is located) of the request (or such longer period as may be required to comply with any applicable fiscal or other laws or regulations) authenticate and deliver, or procure the authentication and delivery of, at its specified office to the transferee or (at the risk of the transferee) send by uninsured mail to such address as the transferee may request, a new Definitive Registered Note of a like aggregate nominal amount to the Definitive Registered Note (or the relevant part of the Definitive Registered Note) transferred. In the case of the transfer of part only of a Definitive Registered Note, a new Definitive Registered Note in respect of the balance of the Definitive Registered Note not transferred will be so authenticated and delivered or (at the risk of the transferor) sent to the transferor.

2.3 Registration of Transfer upon Partial Redemption

In the event of a partial redemption of Notes under Condition 7.3, the Issuer shall not be required to register the transfer of any Registered Note, or part of a Registered Note, that is called for partial redemption.

2.4 Costs of Registration

Registration of transfers will be effected without charge by or on behalf of the Issuer, the Registrar or the relevant Transfer Agent, but upon payment (or the giving of such indemnity as the Registrar or the relevant Transfer Agent may reasonably require) in respect of any tax or other governmental charges which may be imposed in relation to it provided that the Issuer shall not be responsible for any documentary stamp tax payable on the transfer of Notes effected in the Philippines unless the Issuer is the counterparty directly liable for that documentary stamp tax.

2.5 Closed Periods

No Noteholder may require the transfer of a Definitive Registered Note to be registered (i) during the period of 15 days ending on the due date for redemption of, or payment of any Installment Amount or interest in respect of, that Note and (ii) during the period of seven days ending on (and including) any Record Date (as defined in Condition 6.4).

3. STATUS

The Notes and any relative Receipts and Coupons are direct, unconditional, unsubordinated and (subject to the provisions of Condition 4.1) unsecured obligations of the Issuer and rank *pari passu* among themselves, with all other outstanding unsecured and unsubordinated obligations of the Issuer, present and future, but, in the event of insolvency, only to the extent permitted by applicable laws relating to creditors' rights.

Under Philippine law unsecured debt of a borrower in insolvency or liquidation that is documented by a public instrument, as provided in Article 2244(14) of the Civil Code of the Philippines, ranks ahead of unsecured debt that is not so documented. Debt is treated as documented by a public instrument if it is acknowledged before a notary or any person authorised to administer oaths in the Philippines. The Issuer's debt which is documented by a public instrument contains an explicit waiver by the parties thereto of the preference or priority created, as provided in Article 2244(14) of the Civil Code of the Philippines, and will rank pari passu with the Notes.

4. COVENANTS

4.1 Negative Pledge

So long as any of the Notes remains outstanding (as defined in the Trust Deed):

- (a) the Issuer will not, and will procure that its Material Subsidiaries will not, create or permit to subsist any mortgage, charge, pledge, lien or other form of encumbrance or security interest (**Security**) upon the whole or any part of the property, assets or revenues, present or future of the Issuer or, as the case may be, any of its Material Subsidiaries, to secure any Public Debt of the Issuer or any of its Material

Subsidiaries or any guarantee of or indemnity in respect thereof, unless, at the same time or prior thereto, the Issuer's obligations under the Notes (A) are secured equally and rateably therewith to the satisfaction of the Trustee (having received an opinion from independent financial, legal or tax advisors of recognized international standing), or (B) have the benefit of such other security, guarantee, indemnity or other arrangement as shall be approved by an Extraordinary Resolution (which is defined in the Trust Deed as, *inter alia*, a resolution duly passed by a majority of not less than three-fourths of the votes cast thereon) of the Notes; and

- (b) the Issuer will not incur or permit to arise any debt which ranks ahead of the Notes by virtue of being evidenced by a public instrument as provided for by Article 2244(14) of the Civil Code of the Philippines, or any successor Philippine law providing for preferences or priority in respect of such debt.

The foregoing prohibition shall not apply to any Security to secure:

- (i) any project debt in the nature of Public Debt Incurred by the Issuer or any of its Material Subsidiaries in respect of which (A) there is no recourse to any other member of the Group and (B) the Issuer or, as the case may be, the relevant Material Subsidiary has no actual or contingent liability of any nature, whether as principal, guarantor, surety or otherwise, except in respect of the granting of Security over the assets of the Issuer or, as the case may be, the relevant Material Subsidiary (1) in respect of which such project debt relates and (2) the amount of project debt in the nature of Public Debt outstanding at any time does not exceed 15 per cent. of the consolidated total assets of the Issuer and its Subsidiaries as set out in the most recent set of financial statements delivered to the Trustee in accordance with Condition 4.4(a); and
- (ii) any Public Debt of any Person outstanding at the time such Person becomes, or becomes a part of, a Material Subsidiary of the Issuer; provided that such Public Debt is not Incurred in contemplation of or in connection with the transactions or series of transactions pursuant to which such Person became a Material Subsidiary.

4.2 Limitation on Indebtedness

The Issuer will not, and will not permit any of its Subsidiaries to, Incur any Indebtedness; provided, however, that the Issuer and any of its Subsidiaries may incur Indebtedness if on the Transaction Date, after giving effect to the Incurrence of such Indebtedness, but not giving any effect to the receipt or application of proceeds therefrom:

- (i) the Leverage Ratio is equal to or less than 5.5 to 1.0; and
- (ii) no Event of Default or Potential Event of Default will have occurred or be continuing or would occur as a consequence of incurring the Indebtedness or transactions relating to such incurrence.

4.3 Limitation on Dividend and Other Restrictions Affecting Material Subsidiaries

- (a) Except as provided below, the Issuer will not, and will not permit any Material Subsidiary to, create or otherwise cause or permit to exist or become effective any encumbrance or restriction on the ability of any Material Subsidiary to:
 - (i) pay dividends or make any other distributions on any Capital Stock of such Material Subsidiary owned by the Issuer or any other Material Subsidiary;
 - (ii) pay any Indebtedness or other obligation owed to the Issuer or any other Material Subsidiary;
 - (iii) make loans or advances to the Issuer or any other Material Subsidiary; or
 - (iv) sell, lease or transfer any of its property or assets to the Issuer or any other Material Subsidiary.
- (b) The provisions of Condition 4.3(a) do not apply to any encumbrances or restrictions:
 - (i) existing in agreements as in effect on the Issue Date and any extensions, refinancings, renewals or replacements of any of the foregoing agreements; provided that the encumbrances and restrictions in any such extension, refinancing, renewal or replacement, taken as a whole, are no more restrictive than those encumbrances or restrictions that are then in effect and that are being extended, refinanced, renewed or replaced;
 - (ii) existing under or by reason of applicable law (including any statute, rule, regulation or government order);

- (iii) in respect of any Person which becomes, or becomes a part of, a Material Subsidiary after the Issue Date, any restrictions on such Person as may be in existence on the date such Person becomes, or becomes a part of, a Material Subsidiary of the Issuer; provided that such restrictions were not imposed in contemplation or in connection with the transactions or series of transactions pursuant to which such Person becoming, or becoming a part of, a Material Subsidiary of the Issuer; or
- (iv) contained in the terms and conditions of, or any document constituting, any Preferred Stock, Hybrid Securities or similar capital instruments issued by the Issuer or any of its Material Subsidiaries.

4.4 Provision of Financial Statements and Reports

- (a) So long as any of the Notes remains outstanding, the Issuer will furnish to the Trustee, which will furnish to the Noteholders upon request to the Trustee, as soon as they are available but in any event not more than 15 calendar days after they are filed with the Philippine Stock Exchange, Inc. or any other securities exchange on which the Issuer's Common Stock is at anytime listed for trading, true and correct copies of any financial or other report in the English language (and an English translation of any financial or other report in any other language) filed with such exchange; provided that, if at any time the Common Stock of the Issuer ceases to be listed for trading on the Philippine Stock Exchange, Inc. or any other recognized securities exchange, the Issuer will file with the Trustee, which will furnish to the Noteholders upon request to the Trustee:
 - (i) as soon as they are available, but in any event within 120 calendar days after the end of the fiscal year of the Issuer, copies of its financial statements (on a consolidated basis) in respect of such financial year (including a statement of income, balance sheet and cash flow statement) audited by a member firm of an internationally recognized firm of independent accountants; and
 - (ii) as soon as they are available, but in any event within 60 calendar days after the end of each quarterly period (other than the final period of a fiscal year) of the Issuer, copies of its unaudited financial statements (on a consolidated basis) in respect of such quarterly period or (in the case of the second quarter of each financial year) the relevant semi-annual period (including at least a statement of income, balance sheet and cash flow statement).
- (b) In addition, so long as any of the Notes remains outstanding, the Issuer will provide (i) with each set of financial statements delivered to the Trustee in accordance with Conditions 4.4(a)(i) and (ii) an Officers' Certificate confirming compliance with all of the Issuer's obligations under the Notes and the Trust Deed and stating the Leverage Ratio with respect to the most recent Relevant Period (and showing in reasonable detail the calculation of the Leverage Ratio, including the arithmetic computations of each component of the Leverage Ratio), (ii) at any other time within 30 days of the written request of the Trustee, an Officers' Certificate confirming that, as at a date not more than seven days before delivering such Officers' Certificate (the **certification date**), there did not exist and had not existed since the certification date of the previous Officers' Certificate (or, in the case of the first Officers' Certificate, the Issue Date) any Event of Default or any Potential Event of Default (or if such exists or existed specifying the same) and (iii) as soon as possible and in any event within 14 days after the Issuer becomes aware or should reasonably become aware of the occurrence of an Event of Default or Potential Event of Default, an Officers' Certificate setting forth the details of the Event of Default or Potential Event of Default and the action which the Issuer proposes to take with respect thereto. The Trustee shall be entitled to accept such certificates as sufficient evidence thereof, in which event it shall be conclusive and binding on the Noteholders.

4.5 Definitions

Set forth below are defined terms used in the covenants and other provisions of the Trust Deed. Reference is made to the Trust Deed for other capitalized terms used in these Conditions for which no definition is provided.

Board of Directors means the board of directors elected or appointed by the stockholders of the Issuer to manage the business of the Issuer.

Capital Stock means, with respect to any Person, any and all shares, interests, participations or other equivalents (however designated, whether voting or non-voting) in equity of such Person, whether outstanding on the Issue Date or issued thereafter, including, without limitation, all Common Stock and Preferred Stock.

Common Stock shall mean, with respect to any Person, any and all shares, interests or participations in, and other equivalents (however designated and whether voting or non-voting) of such Person's common stock or ordinary shares, whether or not outstanding at the date of the Trust Deed, and include, without limitation, all series and classes of such common stock or ordinary shares.

Consolidated EBITDA means, in respect of any Relevant Period, the consolidated net income of the Group (excluding items between any or all of the Issuer and its Consolidated Subsidiaries):

- (i) before any provision on account of taxation;
- (ii) before any interest, commission, discounts or other fees incurred or payable, received or receivable by the Issuer or any of its Consolidated Subsidiaries in respect of Indebtedness;
- (iii) before any items treated as exceptional or extraordinary items;
- (iv) before any amount attributable to the amortization of intangible assets and depreciation of tangible assets;
- (v) excluding income attributable to or generated by the Ring-Fenced Subsidiaries; and
- (vi) excluding the contributions of Replacement Subsidiaries which have not been designated as "Replacement Subsidiaries" pursuant to Condition 7.6,

and so that no amount shall be included or excluded more than once.

In any Relevant Period which includes a fiscal quarter in which an acquisition or a disposal of a company or companies is made by any member of the Group (a **Relevant Event**), pro forma financial information will be prepared and used for the purposes of the computation of Consolidated EBITDA on the basis that the acquired company(ies) were acquired or, as the case may be, the disposed company(ies) were disposed, by the Group as at the beginning of that Relevant Period, and the financial statements therefrom prepared will be on the basis that the financial statements of the acquired company(ies) were consolidated or, as the case may be, the financial statements of the disposed company(ies) were not consolidated, with that of the Group as at the beginning of the Relevant Period.

Consolidated Net Indebtedness means, at any date, Consolidated Total Indebtedness less the aggregate amount (without duplication) of freely available, unencumbered cash and cash equivalents on the consolidated balance sheet of the Group at such time. For the avoidance of doubt, any cash proceeds raised from an Incurrence of Indebtedness shall be excluded from the computation of Consolidated Net Indebtedness for the purposes of computing the Leverage Ratio in respect of such Incurrence of Indebtedness only and not in respect of any other Incurrence of Indebtedness.

Consolidated Subsidiary of any Person means, a Subsidiary which for financial reporting purposes, in accordance with PFRS, is accounted for by such Person as a consolidated subsidiary.

Consolidated Total Indebtedness means, at any date, the aggregate (without duplication) of all Indebtedness of the Group as at such date and including all obligations of the IPPAs (under their respective IPPA Agreements) owned or acquired by the Group which are Guaranteed pursuant to a standby letter of credit or other credit support document, issued on behalf of the administrator of the relevant IPPA (but excluding (A) items between any or all of the Issuer and its Consolidated Subsidiaries which would be excluded in a consolidated balance sheet of the Group prepared as of such date in accordance with PFRS, (B) the Project Debt and (C) all obligations of the IPPAs (under their respective IPPA Agreements) which represent periodic financial lease payments to PSALM or any other counterparty to an IPPA Agreement).

Disqualified Stock means any class or series of Capital Stock of any Person that by its terms (or by the terms of any security into which it is convertible or for which it is exchangeable) or otherwise is (a) required to be redeemed prior to the Stated Maturity of the relevant Series of Notes, (b) redeemable at the option of the holder of such class or series of Capital Stock at any time prior to the Stated Maturity of the relevant Series of Notes or (c) convertible into or exchangeable for Capital Stock referred to in clause (a) or (b) above or Indebtedness of any Person having a scheduled maturity prior to the Stated Maturity of the relevant Series of Notes; provided that any class or series of debt securities or Preferred Stock convertible or exchangeable into Common Stock, the terms of which allow for a cash payment in lieu of Common Stock upon conversion or exchange in the event that the issue or distribution of Common Stock to the holder thereof will cause such Person to violate foreign ownership regulations applicable in the Philippines from time to time shall not constitute Disqualified Stock provided that any such cash payments are made with the proceeds of the sale of Capital Stock of such Person to an unaffiliated Person.

Guarantee means any obligation, contingent or otherwise, of any Person directly or indirectly guaranteeing any Indebtedness or other obligation of any other Person, and without limiting the generality of the foregoing, any obligation, direct or indirect, contingent or otherwise, of such Person (i) to purchase or pay (or advance or supply funds for the purchase or payment of) such Indebtedness or other obligation of such other Person (whether arising by virtue of partnership arrangements, or by agreements to keep-well, to purchase assets, goods, securities or services, to take-or-pay, or to maintain financial statement conditions or otherwise) or (ii) entered into for the purpose of assuring in any other manner the obligee of such Indebtedness or other obligation of the payment thereof or to protect such obligee against loss in respect thereof (in whole or in part), provided that the term **Guarantee** shall not include endorsements for collection or deposit in the ordinary course of business. The term **Guarantee** used as a verb has a corresponding meaning.

Group means the Issuer and its Subsidiaries, taken as a whole.

Hybrid Securities means any Indebtedness of a Person that:

- (i) is subordinated in right of payment to any unsecured and unsubordinated obligation of such Person;
- (ii) does not have a fixed redemption date and either (A) is perpetual or (B) only matures on the date on which the corporate term of such Person expires (as the corporate term is extended from time to time); and
- (iii) is recorded as “equity” pursuant to PFRS or the applicable generally accepted accounting principles for the purposes of the consolidated financial statements of the Issuer or any of its Material Subsidiaries, as the case may be.

Incur means, with respect to any Indebtedness or Capital Stock of any Person, to incur (by merger, conversion, exchange or otherwise), create, issue, assume, guarantee or otherwise become liable for or with respect to, or become responsible for, the payment of, contingently or otherwise, such Indebtedness or Capital Stock; provided that (a) any Indebtedness of a Person existing at the time such Person becomes a Subsidiary (whether by merger, consolidation, acquisition or otherwise) will be deemed to be Incurred by such Subsidiary at the time it becomes a Subsidiary and (b) the accretion of original issue discount shall not be considered an Incurrence of Indebtedness solely for the purpose of determining compliance with Condition 4.2 “Limitation on Indebtedness” amortization of original issue discount shall not be deemed to be an Incurrence of Indebtedness, provided that in the case of Indebtedness sold at a discount, the amount of such Indebtedness Incurred shall at all times be the aggregate principal amount at Stated Maturity. The terms **Incurrence**, **Incurred** and **Incuring** have meanings correlative with the foregoing.

Indebtedness means, with respect to any Person at any date of determination (without duplication):

- (i) all obligations of such Person for borrowed money;
- (ii) all obligations of such Person evidenced by bonds, debentures, notes or other similar instruments, including, with respect to the Issuer, all Series of Notes;
- (iii) all obligations of such Person to pay the deferred purchase price of property or services, except trade accounts payable arising in the ordinary course of business;
- (iv) all obligations of such Person as lessee which are capitalized in accordance with PFRS;
- (v) all Indebtedness (of any Person) secured by a Lien on any asset of such first-mentioned Person, whether or not such Indebtedness is otherwise an obligation of such first-mentioned Person;
- (vi) all obligations of such Person in respect of any Disqualified Stock of such Person (provided that such Disqualified Stock (1) falls within paragraph (a) of the definition thereof in this Condition 4.5, or (2) falls within paragraph (b) of the definition thereof in this Condition 4.5 and the Person entitled to exercise the option to require redemption of such Disqualified Stock has exercised or given notice to exercise such option, or (3) falls within paragraph (c) of the definition thereof in this Condition 4.5 and has been converted into Debt having a scheduled maturity prior to the Stated Maturity of the relevant Series of Notes);
- (vii) all non-contingent obligations of such Person to reimburse any bank or other Person in respect of amounts paid under a letter of credit, Guarantee or similar instrument;
- (viii) all Indebtedness of others Guaranteed by such Person;
- (ix) all indebtedness of such Person for or in respect of receivables sold or discounted (other than on a non-recourse basis); and

- (x) all indebtedness of such Person for or in respect of any interest rate swap, currency swap, forward foreign exchange transaction, cap, floor, collar or option transaction or any other treasury transaction or any combination thereof or any other transaction designed to protect against fluctuations in any rate or price (**Hedging Obligations**) (and the amount of the indebtedness in relation to any such transaction described herein shall be calculated by reference to the mark-to-market valuation of such transaction at the relevant time), but excluding all indebtedness Incurred by such Person pursuant to Hedging Obligations entered into solely to protect such Person from fluctuations in interest rates, currencies or the price of fuel and not for speculation provided that such Hedging Obligations do not increase the Indebtedness of such Person outstanding at any time other than as a result of fluctuations in interest rates, foreign currency exchange rates or fuel prices or by reason of fees, indemnities and compensation payable thereunder.

IPPA means an independent power producer administrator.

IPPA Agreement means each independent power producer administration agreement entered into between an IPPA and PSALM or any party, including a transferee of such IPPA Agreement.

Issue Date means, in respect of a Series of Notes, the date on which the Notes of that Series (other than, additional Notes created pursuant to Condition 17) are originally issued.

Leverage Ratio means, on any Transaction Date, the ratio of (1) Consolidated Net Indebtedness as at such Transaction Date to (2) Consolidated EBITDA of the Issuer for the then most recent Relevant Period prior to such Transaction Date for which consolidated financial statements of the Issuer (which the Issuer shall use its reasonable best efforts to compile in a timely manner) are available pursuant to Condition 4.4.

Lien means with respect to any property or asset, any mortgage, lien, pledge, charge, security interest, encumbrance or other preferential arrangement of any kind in respect of such property or asset, including, without limitation, any preference or priority under Article 2244(14) of the Philippine Civil Code, and the right of a vendor, lessor, or similar party under any conditional sales agreement, capital lease or other title retention agreement relating to such property or asset, and any other right of or arrangement with any creditor to have its claims satisfied out of any assets, or the proceeds therefrom, prior to any general creditor of the owner thereof.

Material Subsidiaries means (a) San Miguel Brewery Inc., (b) Petron Corporation, (c) a Replacement Subsidiary (as defined in Condition 7.6) replacing any of San Miguel Brewery Inc., Petron Corporation or a Replacement Subsidiary and (d) at any time, a Subsidiary of the Issuer:

- (i) whose net income (consolidated in the case of a Subsidiary which itself has Subsidiaries) or whose total assets (consolidated in the case of a Subsidiary which itself has Subsidiaries) represent in each case (or, in the case of a Subsidiary acquired after the end of the financial period to which the then latest audited consolidated accounts of the Issuer and its Subsidiaries relate, are equal to) not less than 25 per cent. of the consolidated net income of the Issuer, or, as the case may be, consolidated total assets, of the Issuer and its Subsidiaries taken as a whole, all as calculated respectively by reference to the then latest audited accounts (consolidated or, as the case may be, unconsolidated) of such Subsidiary and the then latest audited consolidated accounts of the Issuer and its Subsidiaries, provided that, in the case of a Subsidiary of the Issuer acquired after the end of the financial period to which the then latest audited consolidated accounts of the Issuer and its Subsidiaries relate, the reference to the then latest audited consolidated accounts of the Issuer and its Subsidiaries for the purposes of the calculation above shall, until consolidated accounts for the financial period in which the acquisition is made have been prepared and audited as aforesaid, be deemed to be a reference to such first-mentioned accounts as if such Subsidiary had been shown in such accounts (as if the acquisition was made on the first day of the relevant financial period) by reference to its then latest relevant audited accounts, adjusted as deemed appropriate by the Issuer;
- (ii) to which is transferred the whole or substantially the whole of the undertaking and assets of a Subsidiary of the Issuer which immediately prior to such transfer was a Material Subsidiary, provided that the transferor Subsidiary shall upon such transfer forthwith cease to be a Material Subsidiary and the transferee Subsidiary shall cease to be a Material Subsidiary pursuant to this subparagraph (ii) on the date on which the consolidated accounts of the Issuer and its Subsidiaries for the financial period current at the date of such transfer have been prepared and audited as aforesaid but so that such transferor Subsidiary or such transferee Subsidiary may be a Material Subsidiary on or at any time after the date on which such consolidated accounts have been prepared and audited as aforesaid by virtue of the provisions of subparagraph (i) above or, prior to or after such date, by virtue of any other applicable provision of this definition; or

(iii) to which is transferred an undertaking or assets which, taken together with the undertaking or assets of the transferee Subsidiary, generated (or, in the case of the transferee Subsidiary being acquired after the end of the financial period to which the then latest audited consolidated accounts of the Issuer and its Subsidiaries relate, generate net income equal to) not less than 25 per cent. of the consolidated net income of the Issuer and its Subsidiaries taken as a whole, or represent (or, in the case aforesaid, are equal to) not less than 25 per cent. of the consolidated total assets of the Issuer and its Subsidiaries taken as a whole, all as calculated as referred to in subparagraph (i) above, provided that the transferor Subsidiary (if a Material Subsidiary) shall upon such transfer forthwith cease to be a Material Subsidiary unless immediately following such transfer its undertaking and assets generate (or, in the case aforesaid, generate net income equal to) not less than 25 per cent. of the consolidated net income of the Issuer and its Subsidiaries taken as a whole, or its assets represent (or, in the case aforesaid, are equal to) not less than 25 per cent. of the consolidated total assets of the Issuer and its Subsidiaries taken as a whole, all as calculated as referred to in subparagraph (i) above, and the transferee Subsidiary shall cease to be a Material Subsidiary pursuant to this subparagraph (iii) on the date on which the consolidated accounts of the Issuer and its Subsidiaries for the financial period current at the date of such transfer have been prepared and audited but so that such transferor Subsidiary or such transferee Subsidiary may be a Material Subsidiary on or at any time after the date on which such consolidated accounts have been prepared and audited as aforesaid by virtue of the provisions of subparagraph (i) above or, prior to or after such date, by virtue of any other applicable provision of this definition.

Officer means the executive director, senior vice president or one of the executive officers of the Issuer.

Officers' Certificate means a certificate signed by two Officers.

Person means any individual, corporation, partnership, limited liability company, joint venture, trust, unincorporated organization or government or any agency or political subdivision thereof.

PFRS means Philippine Financial Reporting Standards.

Potential Event of Default means any event that after notice or passage of time or both would be, an Event of Default (as defined in Condition 10.1).

Preferred Stock as applied to the Capital Stock of any Person means Capital Stock of any class or classes that by its term is preferred as to the payment of dividends, or as to the distribution of assets upon any voluntary or involuntary liquidation or dissolution of such Person, over any other class of Capital Stock of such Person.

Project Debt means debt incurred by a Ring-Fenced Subsidiary in relation to project finance (including aircraft financing) in respect of which there is no recourse to the Issuer or any other member of the Group, and in respect of which neither the Issuer nor any other member of the Group has any actual or contingent liability of any nature, whether as principal, guarantor, surety or otherwise, except in respect of the granting of liens over shares in such Ring-Fenced Subsidiary.

PSALM means Power Section Asset and Liabilities Management Corporation or its successors.

Public Debt means any present or future indebtedness in the form of, or represented by, bonds, notes, debentures, loan stock or other securities that are at the time, or are capable of being, quoted, listed or ordinarily dealt in on any stock exchange, over-the-counter or other securities market, in each case having an original maturity of more than one year from the date of issue.

Relevant Period means a period of twelve calendar months ending on the last day of any quarter of any of the Issuer's fiscal years.

Ring-Fenced Subsidiary means any entity that satisfies the following conditions:

- (i) such entity, to the extent directly owned by the Issuer or a member of the Group (other than another Ring-Fenced Subsidiary), is a limited liability company or a corporation organized and existing under the laws of the Philippines;
- (ii) such entity shall not be a Material Subsidiary;
- (iii) the Issuer has delivered a written notification to the Trustee designating such entity as a "Ring-Fenced Subsidiary";
- (iv) no member of the Group (other than that Ring-Fenced Subsidiary) shall be contingently liable for any Indebtedness of such entity or its Subsidiaries, except in respect of the granting of liens over shares in such Ring-Fenced Subsidiary; and

- (v) all transactions conducted between any member of the Group and such entity or its Subsidiaries must be on an arm's length basis and on normal commercial terms,

and each Subsidiary of any such entity shall also be a "Ring-Fenced Subsidiary".

Stated Maturity means, (i) with respect to any Indebtedness, the date specified in such debt security as the fixed date on which the final installment of principal of such Indebtedness is due and payable as set forth in the documentation governing such Indebtedness and (ii) with respect to any scheduled installment of principal of or interest on any Indebtedness, the date specified as the fixed date on which such installment is due and payable as set forth in the documentation governing such Indebtedness.

Subsidiary of a company means, in relation to the Issuer, any company (i) in which the Issuer holds a majority of the voting rights or (ii) of which the Issuer is a member and has the right to appoint or remove a majority of the board of directors or (iii) of which the Issuer is a member and controls a majority of the voting rights, and includes any company which is a Subsidiary of a Subsidiary of the Issuer.

Transaction Date means, with respect to the Incurrence of any Indebtedness, the date such Indebtedness is to be Incurred.

5. INTEREST

5.1 Interest on Fixed Rate Notes

Each Fixed Rate Note bears interest from (and including) the Interest Commencement Date at the rate(s) per annum equal to the Rate(s) of Interest. Interest will be payable in arrear on the Interest Payment Date(s) in each year up to (and including) the Maturity Date.

If the Notes are in definitive form, except as provided in the applicable Pricing Supplement, the amount of interest payable on each Interest Payment Date in respect of the Fixed Interest Period ending on (but excluding) such date will amount to the Fixed Coupon Amount. Payments of interest on any Interest Payment Date will, if so specified in the applicable Pricing Supplement, amount to the Broken Amount so specified.

As used in these Conditions, **Fixed Interest Period** means the period from (and including) an Interest Payment Date (or the Interest Commencement Date) to (but excluding) the next (or first) Interest Payment Date.

Except in the case of Notes in definitive form where an applicable Fixed Coupon Amount or Broken Amount is specified in the applicable Pricing Supplement, interest shall be calculated in respect of any period by applying the Rate of Interest to:

- (A) in the case of Fixed Rate Notes which are represented by a Global Note, the aggregate outstanding nominal amount of the Fixed Rate Notes represented by such Global Note (or, if they are Partly Paid Notes, the aggregate amount paid up); or
- (B) in the case of Fixed Rate Notes in definitive form, the Calculation Amount;

and, in each case, multiplying such sum by the applicable Day Count Fraction, and rounding the resultant figure to the nearest sub-unit of the relevant Specified Currency, half of any such sub-unit being rounded upwards or otherwise in accordance with applicable market convention. Where the Specified Denomination of a Fixed Rate Note in definitive form is a multiple of the Calculation Amount, the amount of interest payable in respect of such Fixed Rate Note shall be the product of the amount (determined in the manner provided above) for the Calculation Amount and the amount by which the Calculation Amount is multiplied to reach the Specified Denomination, without any further rounding.

Day Count Fraction means, in respect of the calculation of an amount of interest in accordance with this Condition 5.1:

- (a) if **Actual/Actual (ICMA)** is specified in the applicable Pricing Supplement:
 - (i) in the case of Notes where the number of days in the relevant period from (and including) the most recent Interest Payment Date (or, if none, the Interest Commencement Date) to (but excluding) the relevant payment date (the **Accrual Period**) is equal to or shorter than the Determination Period during which the Accrual Period ends, the number of days in such Accrual Period divided by the product of (I) the number of days in such Determination Period and (II) the number of Determination Dates (as specified in the applicable Pricing Supplement) that would occur in one calendar year; or

- (ii) in the case of Notes where the Accrual Period is longer than the Determination Period during which the Accrual Period ends, the sum of:
 - (A) the number of days in such Accrual Period falling in the Determination Period in which the Accrual Period begins divided by the product of (x) the number of days in such Determination Period and (y) the number of Determination Dates that would occur in one calendar year; and
 - (B) the number of days in such Accrual Period falling in the next Determination Period divided by the product of (x) the number of days in such Determination Period and (y) the number of Determination Dates that would occur in one calendar year;
- (b) if **30/360** is specified in the applicable Pricing Supplement, the number of days in the period from (and including) the most recent Interest Payment Date (or, if none, the Interest Commencement Date) to (but excluding) the relevant payment date (such number of days being calculated on the basis of a year of 360 days with 12 30-day months) divided by 360; or
- (c) if **Actual/365 (Fixed)** is specified in the applicable Pricing Supplement, the actual number of days in the Accrual Period divided by 365.

In these Conditions:

Determination Period means each period from (and including) a Determination Date to (but excluding) the next Determination Date (including, where either the Interest Commencement Date or the final Interest Payment Date is not a Determination Date, the period commencing on the first Determination Date prior to, and ending on the first Determination Date falling after, such date); and

sub-unit means, with respect to any currency other than euro, the lowest amount of such currency that is available as legal tender in the country of such currency and, with respect to euro, one cent.

5.2 Interest on Floating Rate Notes and Index Linked Interest Notes

(a) *Interest Payment Dates*

Each Floating Rate Note and Index Linked Interest Note bears interest from (and including) the Interest Commencement Date and such interest will be payable in arrear on either:

- (i) the Specified Interest Payment Date(s) in each year specified in the applicable Pricing Supplement; or
- (ii) if no Specified Interest Payment Date(s) is/are specified in the applicable Pricing Supplement, each date (each such date, together with each Specified Interest Payment Date, an Interest Payment Date) which falls the number of months or other period specified as the Specified Period in the applicable Pricing Supplement after the preceding Interest Payment Date or, in the case of the first Interest Payment Date, after the Interest Commencement Date.

Such interest will be payable in respect of each Interest Period (which expression shall, in these Conditions, mean the period from (and including) an Interest Payment Date (or the Interest Commencement Date) to (but excluding) the next (or first) Interest Payment Date).

In these Conditions, if a Business Day Convention is specified in the applicable Pricing Supplement and (x) if there is no numerically corresponding day on the calendar month in which an Interest Payment Date should occur or (y) if any Interest Payment Date would otherwise fall on a day which is not a Business Day, then, if the Business Day Convention specified is:

- (A) in any case where Specified Periods are specified in accordance with Condition 5.2(a)(ii) above, the Floating Rate Convention, such Interest Payment Date (a) in the case of (x) above, shall be the last day that is a Business Day in the relevant month and the provisions of (ii) below shall apply *mutatis mutandis* or (b) in the case of (y) above, shall be postponed to the next day which is a Business Day unless it would thereby fall into the next calendar month, in which event (i) such Interest Payment Date shall be brought forward to the immediately preceding Business Day and (ii) each subsequent Interest Payment Date shall be the last Business Day in the month which falls the Specified Period after the preceding applicable Interest Payment Date occurred; or
- (B) the Following Business Day Convention, such Interest Payment Date shall be postponed to the next day which is a Business Day; or
- (C) the Modified Following Business Day Convention, such Interest Payment Date shall be postponed to the next day which is a Business Day unless it would thereby fall into the next calendar month,

in which event such Interest Payment Date shall be brought forward to the immediately preceding Business Day; or

- (D) the Preceding Business Day Convention, such Interest Payment Date shall be brought forward to the immediately preceding Business Day.

In these Conditions, **Business Day** means a day which is both:

- (a) a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in each Additional Business Center specified in the applicable Pricing Supplement; and
- (b) either (i) in relation to any sum payable in a Specified Currency other than euro and Renminbi, a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in the principal financial center of the country of the relevant Specified Currency (which, if the Specified Currency is Australian dollars or New Zealand dollars, shall be Sydney and Auckland, respectively); (ii) in relation to any sum payable in euro, a day on which the Trans-European Automated Real-Time Gross Settlement Express Transfer (TARGET2) System or any successor system (the **TARGET2 System**) is open; or (iii) in relation to any sum payable in Renminbi, a day (other than a Saturday, Sunday or public holiday) on which commercial banks in Hong Kong are generally open for business and settlement of Renminbi payments in Hong Kong.

(b) Rate of Interest

The Rate of Interest payable from time to time in respect of Floating Rate Notes and Index Linked Interest Notes will be determined in the manner specified in the applicable Pricing Supplement.

(i) ISDA Determination for Floating Rate Notes

Where ISDA Determination is specified in the applicable Pricing Supplement as the manner in which the Rate of Interest is to be determined, the Rate of Interest for each Interest Period will be the relevant ISDA Rate plus or minus (as indicated in the applicable Pricing Supplement) the Margin (if any). For the purposes of this sub-paragraph (i), **ISDA Rate** for an Interest Period means a rate equal to the Floating Rate that would be determined by the Principal Paying Agent under an interest rate swap transaction if the Principal Paying Agent were acting as Calculation Agent for that swap transaction under the terms of an agreement incorporating the 2006 ISDA Definitions, as published by the International Swaps and Derivatives Association, Inc. and as amended and updated as of the Issue Date of the first Tranche of the Notes (the **ISDA Definitions**) and under which:

- (A) the Floating Rate Option is as specified in the applicable Pricing Supplement;
- (B) the Designated Maturity is a period specified in the applicable Pricing Supplement; and
- (C) the relevant Reset Date is either (a) if the applicable Floating Rate Option is based on the London interbank offered rate (**LIBOR**), the Euro-zone interbank offered rate (**EURIBOR**) or the Hong Kong interbank offered rate (**HIBOR**), the first day of that Interest Period or (b) in any other case, as specified in the applicable Pricing Supplement.

For the purposes of this sub-paragraph (i), **Floating Rate**, **Calculation Agent**, **Floating Rate Option**, **Designated Maturity** and **Reset Date** have the meanings given to those terms in the ISDA Definitions.

Unless otherwise stated in the applicable Pricing Supplement the Minimum Rate of Interest shall be deemed to be zero.

(ii) Screen Rate Determination for Floating Rate Notes

Where Screen Rate Determination is specified in the applicable Pricing Supplement as the manner in which the Rate of Interest is to be determined, the Rate of Interest for each Interest Period will, subject as provided below, be either:

- (A) the offered quotation; or
- (B) the arithmetic mean (rounded if necessary to the fifth decimal place, with 0.000005 being rounded upwards) of the offered quotations,

(expressed as a percentage rate per annum) for the Reference Rate which appears or appear, as the case may be, on the Relevant Screen Page as of 11.00 a.m. (Relevant Financial Center time) on

the Interest Determination Date in question plus or minus (as indicated in the applicable Pricing Supplement) the Margin (if any), all as determined by the Principal Paying Agent. If five or more of such offered quotations are available on the Relevant Screen Page, the highest (or, if there is more than one such highest quotation, one only of such quotations) and the lowest (or, if there is more than one such lowest quotation, one only of such quotations) shall be disregarded by the Principal Paying Agent for the purpose of determining the arithmetic mean (rounded as provided above) of such offered quotations.

The Agency Agreement contains provisions for determining the Rate of Interest in the event that the Relevant Screen Page is not available or if, in the case of (A) above, no such offered quotation appears or, in the case of (B) above, fewer than three such offered quotations appear, in each case as at the time specified in the preceding paragraph.

(c) *Minimum and/or Maximum Rate of Interest*

If the applicable Pricing Supplement specifies a Minimum Rate of Interest for any Interest Period, then, in the event that the Rate of Interest in respect of such Interest Period determined in accordance with the provisions of paragraph (b) above is less than such Minimum Rate of Interest, the Rate of Interest for such Interest Period shall be such Minimum Rate of Interest.

If the applicable Pricing Supplement specifies a Maximum Rate of Interest for any Interest Period, then, in the event that the Rate of Interest in respect of such Interest Period determined in accordance with the provisions of paragraph (b) above is greater than such Maximum Rate of Interest, the Rate of Interest for such Interest Period shall be such Maximum Rate of Interest.

(d) *Determination of Rate of Interest and Calculation of Interest Amounts*

The Principal Paying Agent, in the case of Floating Rate Notes, and the Calculation Agent, in the case of Index Linked Interest Notes, will at or as soon as practicable after each time at which the Rate of Interest is to be determined, determine the Rate of Interest for the relevant Interest Period. In the case of Index Linked Interest Notes, the Calculation Agent will notify the Principal Paying Agent of the Rate of Interest for the relevant Interest Period as soon as practicable after calculating the same.

The Principal Paying Agent will calculate the amount of interest (the **Interest Amount**) payable on the Floating Rate Notes or Index Linked Interest Notes for the relevant Interest Period by applying the Rate of Interest to:

- (A) in the case of Floating Rate Notes or Index Linked Interest Notes which are represented by a Global Note, the aggregate outstanding nominal amount of the Notes represented by such Global Note (or, if they are Partly Paid Notes, the aggregate amount paid up); or
- (B) in the case of Floating Rate Notes or Index Linked Interest Notes in definitive form, the Calculation Amount;

and, in each case, multiplying such sum by the applicable Day Count Fraction, and rounding the resultant figure to the nearest sub-unit of the relevant Specified Currency, half of any such sub-unit being rounded upwards or otherwise in accordance with applicable market convention. Where the Specified Denomination of a Floating Rate Note or an Index Linked Interest Note in definitive form is a multiple of the Calculation Amount, the Interest Amount payable in respect of such Note shall be the product of the amount (determined in the manner provided above) for the Calculation Amount and the amount by which the Calculation Amount is multiplied to reach the Specified Denomination, without any further rounding.

Day Count Fraction means, in respect of the calculation of an amount of interest in accordance with this Condition 5.2:

- (i) if **Actual/Actual (ISDA)** or **Actual/Actual** is specified in the applicable Pricing Supplement, the actual number of days in the Interest Period divided by 365 (or, if any portion of that Interest Period falls in a leap year, the sum of (I) the actual number of days in that portion of the Interest Period falling in a leap year divided by 366 and (II) the actual number of days in that portion of the Interest Period falling in a non-leap year divided by 365);
- (ii) if **Actual/365 (Fixed)** is specified in the applicable Pricing Supplement, the actual number of days in the Interest Period divided by 365;
- (iii) if **Actual/365 (Sterling)** is specified in the applicable Pricing Supplement, the actual number of days in the Interest Period divided by 365 or, in the case of an Interest Payment Date falling in a leap year, 366;

- (iv) if **Actual/360** is specified in the applicable Pricing Supplement, the actual number of days in the Interest Period divided by 360;
- (v) if **30/360, 360/360** or **Bond Basis** is specified in the applicable Pricing Supplement, the number of days in the Interest Period divided by 360, calculated on a formula basis as follows:

$$\text{Day Count Fraction} = \frac{[360 \times (Y_2 - Y_1)] + [30 \times (M_2 - M_1)] + (D_2 - D_1)}{360}$$

where:

- Y1** is the year, expressed as a number, in which the first day of the Interest Period falls;
- Y2** is the year, expressed as a number, in which the day immediately following the last day of the Interest Period falls;
- M1** is the calendar month, expressed as a number, in which the first day of the Interest Period falls;
- M2** is the calendar month, expressed as a number, in which the day immediately following the last day of the Interest Period falls;
- D1** is the first calendar day, expressed as a number, of the Interest Period, unless such number is 31, in which case D1 will be 30; and
- D2** is the calendar day, expressed as a number, immediately following the last day included in the Interest Period, unless such number would be 31 and D1 is greater than 29, in which case D2 will be 30;

- (vi) if **30E/360** or **Eurobond Basis** is specified in the applicable Pricing Supplement, the number of days in the Interest Period divided by 360, calculated on a formula basis as follows:

$$\text{Day Count Fraction} = \frac{[360 \times (Y_2 - Y_1)] + [30 \times (M_2 - M_1)] + (D_2 - D_1)}{360}$$

where:

- Y1** is the year, expressed as a number, in which the first day of the Interest Period falls;
- Y2** is the year, expressed as a number, in which the day immediately following the last day of the Interest Period falls;
- M1** is the calendar month, expressed as a number, in which the first day of the Interest Period falls;
- M2** is the calendar month, expressed as a number, in which the day immediately following the last day of the Interest Period falls;
- D1** is the first calendar day, expressed as a number, of the Interest Period, unless such number would be 31, in which case D1 will be 30; and
- D2** is the calendar day, expressed as a number, immediately following the last day included in the Interest Period, unless such number would be 31, in which case D2 will be 30; and

- (vii) if **30E/360 (ISDA)** is specified in the applicable Pricing Supplement, the number of days in the Interest Period divided by 360, calculated on a formula basis as follows:

$$\text{Day Count Fraction} = \frac{[360 \times (Y_2 - Y_1)] + [30 \times (M_2 - M_1)] + (D_2 - D_1)}{360}$$

where:

- Y1** is the year, expressed as a number, in which the first day of the Interest Period falls;
- Y2** is the year, expressed as a number, in which the day immediately following the last day of the Interest Period falls;
- M1** is the calendar month, expressed as a number, in which the first day of the Interest Period falls;
- M2** is the calendar month, expressed as a number, in which the day immediately following the last day of the Interest Period falls;
- D1** is the first calendar day, expressed as a number, of the Interest Period, unless (i) that day is the last day of February or (ii) such number would be 31, in which case D1 will be 30; and

D2 is the calendar day, expressed as a number, immediately following the last day included in the Interest Period, unless (i) that day is the last day of February but not the Maturity Date or (ii) such number would be 31, in which case D2 will be 30.

(e) Notification of Rate of Interest and Interest Amounts

The Principal Paying Agent will cause the Rate of Interest and each Interest Amount for each Interest Period and the relevant Interest Payment Date to be notified to the Issuer, the Trustee and any stock exchange on which the relevant Floating Rate Notes or Index Linked Interest Notes are for the time being listed and notice thereof to be published in accordance with Condition 14 as soon as possible after their determination but in no event later than the fourth London Business Day thereafter. Each Interest Amount and Interest Payment Date so notified may subsequently be amended (or appropriate alternative arrangements made by way of adjustment) without prior notice in the event of an extension or shortening of the Interest Period. Any such amendment will be promptly notified to each stock exchange on which the relevant Floating Rate Notes or Index Linked Interest Notes are for the time being listed and to the Noteholders in accordance with Condition 14. For the purposes of this paragraph, the expression **London Business Day** means a day (other than a Saturday or a Sunday) on which banks and foreign exchange markets are open for business in London.

(f) Determination or Calculation by Trustee

If for any reason at any relevant time the Principal Paying Agent or, as the case may be, the Calculation Agent defaults in its obligation to determine the Rate of Interest or the Principal Paying Agent defaults in its obligation to calculate any Interest Amount in accordance with sub-paragraph (b)(i) or subparagraph (b)(ii) above or as otherwise specified in the applicable Pricing Supplement, as the case may be, and in each case in accordance with paragraph (d) above, the Trustee shall (or shall, at the expense of the Issuer, appoint an agent to) determine the Rate of Interest at such rate as, in its absolute discretion (having such regard as it shall think fit to the foregoing provisions of this Condition, but subject always to any Minimum Rate of Interest or Maximum Rate of Interest specified in the applicable Pricing Supplement), it shall deem fair and reasonable in all the circumstances or, as the case may be, the Trustee shall calculate the Interest Amount(s) in such manner as it shall deem fair and reasonable in all the circumstances and each such determination or calculation shall be deemed to have been made by the Principal Paying Agent or the Calculation Agent, as applicable.

(g) Certificates to be Final

All certificates, communications, opinions, determinations, calculations, quotations and decisions given, expressed, made or obtained for the purposes of the provisions of this Condition 5, whether by the Principal Paying Agent or, if applicable, the Calculation Agent or the Trustee (or its agent), shall (in the absence of wilful default, gross negligence, fraud or manifest error) be binding on the Issuer, the Trustee, the Principal Paying Agent, the Registrar, the Calculation Agent (if applicable), the other Paying Agents, the Transfer Agents and all Noteholders, Receiptholders and Couponholders and (in the absence as aforesaid) no liability to the Issuer, the Noteholders, the Receiptholders or the Couponholders shall attach to the Principal Paying Agent or, if applicable, the Calculation Agent, the Registrar, the other Paying Agents, the Transfer Agents or the Trustee in connection with the exercise or non-exercise by any of them of their powers, duties and discretions pursuant to such provisions.

5.3 Interest on Dual Currency Interest Notes

The rate or amount of interest payable in respect of Dual Currency Interest Notes shall be determined in the manner specified in the applicable Pricing Supplement.

5.4 Interest on Partly Paid Notes

In the case of Partly Paid Notes (other than Partly Paid Notes which are Zero Coupon Notes), interest will accrue as aforesaid on the paid-up nominal amount of such Notes and otherwise as specified in the applicable Pricing Supplement.

5.5 Accrual of Interest

Each Note (or in the case of the redemption of part only of a Note, that part only of such Note) will cease to bear interest (if any) from the date for its redemption unless, upon due presentation thereof, payment of

principal is improperly withheld or refused. In such event, interest will continue to accrue until whichever is the earlier of:

- (a) the date on which all amounts due in respect of such Note have been paid; and
- (b) as provided in the Trust Deed.

6. PAYMENTS

6.1 Method of Payment

Subject as provided below:

- (a) payments in a Specified Currency other than euro and Renminbi will be made by credit or transfer to an account in the relevant Specified Currency maintained by the payee with, or, at the option of the payee, by a cheque in such Specified Currency drawn on, a bank in the principal financial center of the country of such Specified Currency (which, if the Specified Currency is Australian dollars or New Zealand dollars, shall be Sydney and Auckland, respectively);
- (b) payments in euro will be made by credit or transfer to a euro account (or any other account to which euro may be credited or transferred) specified by the payee or, at the option of the payee, by a euro cheque; and
- (c) payments in Renminbi will be made by transfer to a Renminbi account maintained by or on behalf of the Noteholder with a bank in Hong Kong.

Payments will be subject in all cases to any fiscal or other laws and regulations applicable thereto in the place of payment, but without prejudice to the provisions of Condition 8.

6.2 Presentation of Bearer Notes, Receipts and Coupons

Payments of principal in respect of Definitive Bearer Notes not held in the CMU will (subject as provided below) be made in the manner provided in Condition 6.1 above only against presentation and surrender (or, in the case of part payment of any sum due, endorsement) of Definitive Bearer Notes, and payments of interest in respect of Definitive Bearer Notes will (subject as provided below) be made as aforesaid only against presentation and surrender (or, in the case of part payment of any sum due, endorsement) of Coupons, in each case at the specified office of any Paying Agent outside the United States (which expression, as used herein, means the United States of America (including the States and the District of Columbia and its possessions)).

Payments of installments of principal (if any) in respect of Definitive Bearer Notes not held in the CMU, other than the final installment, will (subject as provided below) be made in the manner provided in Condition 6.1 above against presentation and surrender (or, in the case of part payment of any sum due, endorsement) of the relevant Receipt in accordance with the preceding paragraph. Payment of the final installment will be made in the manner provided in Condition 6.1 above only against presentation and surrender (or, in the case of part payment of any sum due, endorsement) of the relevant Bearer Note in accordance with the preceding paragraph. Each Receipt must be presented for payment of the relevant installment together with the Definitive Bearer Note to which it appertains. Receipts presented without the Definitive Bearer Note to which they appertain do not constitute valid obligations of the Issuer. Upon the date on which any Definitive Bearer Note becomes due and repayable, unmatured Receipts (if any) relating thereto (whether or not attached) shall become void and no payment shall be made in respect thereof.

Fixed Rate Notes in definitive bearer form not held in the CMU (other than Dual Currency Notes, Index Linked Notes or Long Maturity Notes (as defined below)) should be presented for payment together with all unmatured Coupons appertaining thereto (which expression shall for this purpose include Coupons falling to be issued on exchange of matured Talons), failing which the amount of any missing unmatured Coupon (or, in the case of payment not being made in full, the same proportion of the amount of such missing unmatured Coupon as the sum so paid bears to the sum due) will be deducted from the sum due for payment. Each amount of principal so deducted will be paid in the manner mentioned above against surrender of the relative missing Coupon at any time before the expiry of 10 years after the Relevant Date (as defined in Condition 8) in respect of such principal (whether or not such Coupon would otherwise have become void under Condition 9) or, if later, five years from the date on which such Coupon would otherwise have become due, but in no event thereafter.

Upon any Fixed Rate Note in definitive bearer form becoming due and repayable prior to its Maturity Date, all unmatured Talons (if any) appertaining thereto will become void and no further Coupons will be issued in respect thereof.

Upon the date on which any Floating Rate Note, Dual Currency Note, Index Linked Note or Long Maturity Note in definitive form not held in the CMU becomes due and repayable, unmatured Coupons and Talons (if any) relating thereto (whether or not attached) shall become void and no payment or, as the case may be, exchange for further Coupons shall be made in respect thereof. A **Long Maturity Note** is a Fixed Rate Note (other than a Fixed Rate Note which on issue had a Talon attached) whose nominal amount on issue is less than the aggregate interest payable thereon provided that such Note shall cease to be a Long Maturity Note on the Interest Payment Date on which the aggregate amount of interest remaining to be paid after that date is less than the nominal amount of such Note.

In the case of Definitive Bearer Notes held in the CMU, payment will be made to the person(s) for whose account(s) interest in the relevant Definitive Bearer Note are credited as being held with the CMU in accordance with the CMU Rules at the relevant time as notified to the CMU Lodging Agent by the CMU in a relevant CMU Instrument Position Report or any relevant notification by CMU, which notification shall be conclusive evidence of the records of CMU (save in the case of manifest error) and payment made in accordance thereof shall discharge the obligations of the Issuer in respect of that payment.

If the due date for redemption of any Definitive Bearer Note is not an Interest Payment Date, interest (if any) accrued in respect of such Note from (and including) the preceding Interest Payment Date or, as the case may be, the Interest Commencement Date shall be payable only against surrender of the relevant Definitive Bearer Note.

6.3 Payments in respect of Bearer Global Notes

Payments of principal and interest (if any) in respect of Bearer Notes represented by any Bearer Global Note will (subject as provided below) be made in the manner specified above in relation to Definitive Bearer Notes or otherwise in the manner specified in the relevant Bearer Global Note (i) in the case of a Bearer Global Note lodged with the CMU, to the person(s) for whose account(s) interests in the relevant Bearer Global Note are credited as being held by the CMU in accordance with the CMU Rules at the relevant time as notified to the CMU Lodging Agent by the CMU in a relevant CMU Instrument Position Report or any relevant notification by the CMU, which notification shall be conclusive evidence of the records of the CMU (save in the case of manifest error) and payment made in accordance thereof shall discharge the obligations of the Issuer in respect of that payment, or (ii) in the case of a Bearer Global Note not lodged with the CMU, against presentation or surrender of such Bearer Global Note at the specified office of any Paying Agent outside the United States. A record of each payment made against presentation or surrender of any Bearer Global Note, distinguishing between any payment of principal and any payment of interest, will be made (in the case of a Bearer Global Note not lodged with the CMU) on such Bearer Global Note either by the Paying Agent to which it was presented or in the records of Euroclear and Clearstream, Luxembourg, as applicable or (in the case of a Bearer Global Note lodged with the CMU) on withdrawal of such Bearer Global Note by the CMU Lodging Agent, and in such case, such record shall be prima facie evidence that the payment in question has been made.

6.4 Payments in respect of Registered Notes

Payments of principal (other than installments of principal prior to the final installment) in respect of each Registered Note (whether or not in global form) will be made against presentation and surrender (or, in the case of part payment of any sum due, endorsement) of the Registered Note at the specified office of the Registrar or any of the Paying Agents. Such payments will be made by transfer to the Designated Account (as defined below) of the holder (or the first named of joint holders) of the Registered Note appearing in the register of holders of the Registered Notes maintained by the Registrar (the **Register**) (i) where in global form, at the close of the business day (being for this purpose, in respect of Notes clearing through Euroclear and Clearstream, Luxembourg, a day on which Euroclear and Clearstream, Luxembourg are open for business and, in respect of Notes clearing through the CMU, a day on which the CMU is open for business) before the relevant due date, and (ii) where in definitive form, at the close of business on the second business day (being for this purpose a day on which banks are open for business in the city where the specified office of the Registrar is located) before the relevant due date. Notwithstanding the previous sentence, if (i) a holder does not have a Designated Account or (ii) the principal amount of the Notes held by a holder is less than U.S.\$250,000 (or its approximate equivalent in any other Specified Currency), payment (in the case of a currency other than Renminbi) will instead be made by a cheque in the Specified Currency drawn on a Designated Bank (as defined below). For these purposes, **Designated Account** means the account (which, in the case of a payment in Japanese yen to a non resident of Japan, shall be a non resident account and, in the case of a payment in Renminbi, means the Renminbi account maintained by or on behalf of the payee with a bank in Hong Kong, details of which appear on the Register at the close of business on

the fifth business day before the due date for payment) maintained by a holder with a Designated Bank and identified as such in the Register and **Designated Bank** means (in the case of payment in a Specified Currency other than euro and Renminbi) a bank in the principal financial center of the country of such Specified Currency (which, if the Specified Currency is Australian dollars or New Zealand dollars, shall be Sydney and Auckland, respectively), (in the case of a payment in euro) any bank which processes payments in euro and (in the case of a payment in Renminbi) a bank in Hong Kong.

Payments of interest and payments of installments of principal (other than the final installment) in respect of each Registered Note (in the case of a Specified Currency other than Renminbi) will be made on the due date by a cheque in the Specified Currency drawn on a Designated Bank and mailed by uninsured mail on the Business Day in the city where the specified office of the Registrar is located immediately preceding the relevant due date to the holder (or the first named of joint holders) of the Registered Note appearing in the Register (i) where in global form, at the close of the business day (being for this purpose, in respect of Notes clearing through Euroclear and Clearstream, Luxembourg, a day on which Euroclear and Clearstream, Luxembourg are open for business and, in respect of Notes clearing through CMU, a day on which CMU is open for business) before the relevant due date, and (ii) where in definitive form, at the close of business on the fifth day (in the case of Renminbi) and on the fifteenth day (in the case of a currency other than Renminbi) (whether or not such fifth day or fifteenth day is a Business Day) before the relevant due date (the **Record Date**) at his address shown in the Register on the Record Date and at his risk. Payments of interest and payments of installments of principal (other than the final installment) in Renminbi shall be made by transfer to the registered account of the payee. Upon application of the holder to the specified office of the Registrar not less than three business days in the city where the specified office of the Registrar is located before the due date for any payment of interest in respect of a Registered Note, the payment may be made by transfer on the due date in the manner provided in the preceding paragraph. Any such application for transfer shall be deemed to relate to all future payments of interest (other than interest due on redemption) and installments of principal (other than the final installment) in respect of the Registered Notes which become payable to the holder who has made the initial application until such time as the Registrar is notified in writing to the contrary by such holder. Payment of the interest due in respect of each Registered Note on redemption and the final installment of principal will be made in the same manner as payment of the principal amount of such Registered Note.

In the case of Definitive Registered Note or Registered Global Note held through the CMU, payment will be made at the discretion of the registered holder to the CMU Accountholders and such payment shall discharge the obligation of the Issuer in respect of that payment.

Holders of Registered Notes will not be entitled to any interest or other payment for any delay in receiving any amount due in respect of any Registered Note as a result of a cheque posted in accordance with this Condition arriving after the due date for payment or being lost in the post. No commissions or expenses shall be charged to such holders by the Registrar in respect of any payments of principal or interest in respect of the Registered Notes.

None of the Issuer, the Trustee, the Registrar, any Transfer Agent or any Paying Agent will have any responsibility or liability for any aspect of the records relating to, or payments made on account of, beneficial ownership interests in the Registered Global Notes or for maintaining, supervising or reviewing any records relating to such beneficial ownership interests.

6.5 General Provisions Applicable to Payments

The holder of a Global Note (if the Global Note is not lodged with the CMU) or (if the Global Note is lodged with the CMU) the person(s) for whose account(s) interests in such Global Note are credited as being held through the CMU in accordance with the CMU Rules as notified to the CMU Lodging Agent by the CMU in a relevant CMU Instrument Position Report or any other relevant notification by CMU (which notification, in either case, shall be conclusive evidence of the records of the CMU save in the case of manifest error), shall be the only person(s) entitled to receive payments in respect of Notes represented by such Global Note and the Issuer will be discharged by payment to, or to the order of, the holder of such Global Note or such person(s) for whose account(s) interests in such Global Note are credited as being held in the CMU, as the case may be, in respect of each amount so paid. Each of the persons shown in the records of Euroclear, Clearstream, Luxembourg or the CMU, as the beneficial holder of a particular nominal amount of Notes represented by such Global Note must look solely to Euroclear, Clearstream, Luxembourg or the CMU, as the case may be, for his share of each payment so made by the Issuer in respect of such Global Note to, or to the order of, the holder of such Global Note.

Notwithstanding the foregoing provisions of this Condition, if any amount of principal and/or interest in respect of the Bearer Notes is payable in U.S. dollars, such U.S. dollar payments of principal and/or interest in respect of such Notes will be made at the specified office of a Paying Agent in the United States only if:

- (a) the Issuer has appointed Paying Agents with specified offices outside the United States with the reasonable expectation that such Paying Agents would be able to make payment in U.S. dollars at such specified offices outside the United States of the full amount of principal and interest on the Bearer Notes in the manner provided above when due;
- (b) payment of the full amount of such principal and interest at all such specified offices outside the United States is illegal or effectively precluded by exchange controls or other similar restrictions on the full payment or receipt of principal and interest in U.S. dollars; and
- (c) such payment is then permitted under United States law without involving, in the opinion of the Issuer, adverse tax consequences to the Issuer.

6.6 Payment Day

If the date for payment of any amount in respect of any Note, Receipt or Coupon is not a Payment Day, the holder thereof shall not be entitled to payment until the next following Payment Day in the relevant place and shall not be entitled to further interest or other payment in respect of such delay. For these purposes, **Payment Day** means any day which (subject to Condition 10) is:

- (a) a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in:
 - (i) in the case of Notes in definitive form only, the relevant place of presentation; and
 - (ii) each Additional Financial Center specified in the applicable Pricing Supplement; and
- (b) either (A) in relation to any sum payable in a Specified Currency other than euro and Renminbi, a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in the principal financial center of the country of the relevant Specified Currency which, if the Specified Currency is Australian dollars or New Zealand dollars, shall be Sydney and Auckland, respectively; (B) in relation to any sum payable in euro, a day on which the TARGET2 System is open; or (C) in relation to any sum payable in Renminbi, a day (other than a Saturday, Sunday or public holiday) on which banks and foreign exchange markets are open for business and settlement of Renminbi payments in Hong Kong.

6.7 Interpretation of Principal and Interest

Any reference in these Conditions to principal in respect of the Notes shall be deemed to include, as applicable:

- (a) any additional amounts which may be payable with respect to principal under Condition 8 or under any undertaking or covenant given in addition thereto, or in substitution therefor, pursuant to the Trust Deed;
- (b) the Final Redemption Amount of the Notes;
- (c) the Early Redemption Amount of the Notes;
- (d) the Optional Redemption Amount(s) (if any) of the Notes;
- (e) in relation to Notes redeemable in installments, the Installment Amounts;
- (f) in relation to Zero Coupon Notes, the Amortized Face Amount (as defined in Condition 7.8); and
- (g) any premium and any other amounts (other than interest) which may be payable by the Issuer under or in respect of the Notes.

Any reference in these Conditions to interest in respect of the Notes shall be deemed to include, as applicable, any additional amounts which may be payable with respect to interest under Condition 8 or under any undertaking or covenant given in addition thereto, or in substitution therefor, pursuant to the Trust Deed.

7. REDEMPTION AND PURCHASE

7.1 Redemption at Maturity

Unless previously redeemed or purchased and cancelled as specified below, each Note (including each Index Linked Redemption Note and Dual Currency Redemption Note) will be redeemed by the Issuer at its

Final Redemption Amount specified in, or determined in the manner specified in, the applicable Pricing Supplement in the relevant Specified Currency on the Maturity Date.

7.2 Redemption for Tax Reasons

The Notes may be redeemed at the option of the Issuer in whole, but not in part, at any time (if this Note is neither a Floating Rate Note nor an Index Linked Interest Note) or on any Interest Payment Date (if this Note is either a Floating Rate Note or an Index Linked Interest Note), on giving not less than 15 and not more than 30 days' notice to the Trustee, the Registrar (if applicable) and the Principal Paying Agent and, in accordance with Condition 14, the Noteholders (which notice shall be irrevocable), if:

- (a) on the occasion of the next payment due under the Notes, the Issuer has or will become obliged to pay Additional Amounts as provided or referred to in Condition 8 as a result of any change in, or amendment to, the laws or regulations of a Tax Jurisdiction (as defined in Condition 8) or any change in the application or official interpretation of such laws or regulations, which change or amendment becomes effective on or after the date on which agreement is reached to issue the first Tranche of the Notes for such Series; and
- (b) such obligation cannot be avoided by the Issuer taking reasonable measures available to it,

provided that no such notice of redemption shall be given earlier than 90 days prior to the earliest date on which the Issuer would be obliged to pay such Additional Amounts were a payment in respect of the Notes then due.

Prior to the publication of any notice of redemption pursuant to this Condition, the Issuer shall deliver to the Trustee to make available at its specified office to the Noteholders an Officers' Certificate stating that the Issuer is entitled to effect such redemption and setting forth a statement of facts showing that the conditions precedent to the right of the Issuer so to redeem have occurred and an opinion of independent legal advisers of recognized standing to the effect that the Issuer has or will become obliged to pay such additional amounts as a result of such change or amendment; and the Trustee shall be entitled without further action or enquiry to accept the certificate and the opinion as sufficient evidence of the satisfaction of the conditions precedent set out above, in which event the certificate shall be conclusive and binding on the Noteholders, the Receiptholders and the Couponholders.

Notes redeemed pursuant to this Condition 7.2 will be redeemed at their Early Redemption Amount referred to in Condition 7.8 below together (if any) with interest accrued to (but excluding) the date of redemption.

7.3 Redemption at the Option of the Issuer (Issuer Call)

If Issuer Call is specified as being applicable in the applicable Pricing Supplement, the Issuer may, having given:

- (a) not less than 15 days nor more than 30 days' notice to the Noteholders in accordance with Condition 14; and
- (b) not less than 15 days before the giving of the notice referred to in (a) above, notice to the Trustee, the Principal Paying Agent and, in the case of a redemption of Registered Notes, the Registrar,

(which notice shall be irrevocable and shall specify the date fixed for redemption), redeem all or some only of the Notes then outstanding on any Optional Redemption Date(s) and at the Optional Redemption Amount(s) specified in, or determined in the manner specified in, the applicable Pricing Supplement together, if appropriate, with interest accrued to (but excluding) the relevant Optional Redemption Date. Any such redemption must be of a nominal amount not less than the Minimum Redemption Amount and/or not more than the Maximum Redemption Amount, in each case as may be specified in the applicable Pricing Supplement. In the case of a partial redemption of Notes (or, as the case may be, parts of Registered Notes), the Notes to be redeemed (**Redeemed Notes**) will be selected in such place as the Trustee may approve and in such manner as it deems fit, in the case of Redeemed Notes represented by definitive Notes, and in accordance with the rules of Euroclear and/or Clearstream, Luxembourg and/or the CMU (as appropriate), in the case of Redeemed Notes represented by a Global Note, not more than 30 days prior to the date fixed for redemption (such date of selection being hereinafter called the **Selection Date**). In the case of Redeemed Notes represented by definitive Notes, the Issuer will ensure that a list of the serial numbers of such Redeemed Notes will be published in accordance with Condition 14 not less than 15 days prior to the date fixed for redemption. The aggregate nominal amount of Redeemed Notes represented by definitive Notes or represented by a Global Note shall in each case bear the same proportion to the aggregate nominal amount of all Redeemed Notes as the aggregate nominal amount of definitive Notes outstanding and Notes

outstanding represented by such Global Note, respectively, bears to the aggregate nominal amount of the Notes outstanding, in each case on the Selection Date, provided that, if necessary, appropriate adjustments shall be made to such nominal amounts to ensure that each represents an integral multiple of the Specified Denomination. No exchange of the relevant Global Note will be permitted during the period from (and including) the Selection Date to (and including) the date fixed for redemption pursuant to this Condition 7.3 and notice to that effect shall be given by the Issuer to the Noteholders in accordance with Condition 14 at least five days prior to the Selection Date.

7.4 Redemption of the Notes at the Option of the Noteholders (Investor Put)

(a) If Investor Put is specified as being applicable in the applicable Pricing Supplement

If Investor Put is specified as being applicable in the applicable Pricing Supplement with respect to Notes only, upon the holder of any Notes giving to the Issuer in accordance with Condition 14 not less than 15 nor more than 30 days' notice (which shall be irrevocable), the Issuer will, upon the expiry of such notice, redeem, subject to, and in accordance with, the terms specified in the applicable Pricing Supplement, such Note, on the Optional Redemption Date(s) and at the Optional Redemption Amount(s) together, if appropriate, with interest accrued to (but excluding) the relevant Optional Redemption Date.

(b) Put Option Exercise Procedures

To exercise the right to require redemption of a Note the holder of the Note must:

- (i) if the Note is in definitive form and held outside Euroclear, Clearstream, Luxembourg and the CMU, deliver, to the specified office of any Paying Agent (in the case of Bearer Notes) or the Registrar (in the case of Registered Notes), at any time during the normal business hours of such Paying Agent or, as the case may be, the Registrar falling within the notice period, a duly signed and completed notice of exercise in the form (for the time being current) obtainable from any specified office of any Paying Agent, Transfer Agent or the Registrar (a **Put Notice**) accompanied by the definitive Note, to the specified office of any Paying Agent in the case of Bearer Notes, or of any Transfer Agent or the Registrar in the case of Registered Notes or, as the case may be, the Registrar and in which the holder must specify a bank account (or, if payment is required to be made by cheque, an address) to which payment is to be made under this Condition, and in the case of Registered Notes, the nominal amount thereof to be redeemed and, if less than the full nominal amount of the Registered Notes so surrendered is to be redeemed, an address to which a new Registered Note in respect of the balance of such Registered Notes is to be sent subject to and in accordance with the provisions of Condition 2. If the Note is in definitive bearer form, the Put Notice must be accompanied by the Note or evidence satisfactory to the Paying Agent concerned that this Note will, following delivery of the Put Notice, be held to its order or under its control; and
- (ii) if this Note is represented by a Global Note or is in definitive form and held through Euroclear or Clearstream, Luxembourg or the CMU, to exercise the right to require redemption of this Note, the holder of this Note must, within the notice period, give notice to the Principal Paying Agent (in the case of Bearer Notes) or the Registrar (in the case of Registered Notes) of such exercise in accordance with the standard procedures of Euroclear and Clearstream, Luxembourg or the CMU (which may include notice being given on his instruction by Euroclear or Clearstream, Luxembourg or the CMU or any common depositary, as the case may be, for them to the Principal Paying Agent (in the case of Bearer Notes) or the Registrar (in the case of Registered Notes) by electronic means or notice being given to the CMU Lodging Agent) in a form acceptable to Euroclear and Clearstream, Luxembourg or the CMU and the CMU Lodging Agent, as the case may be, from time to time and, if this Note is represented by a Global Note held through Euroclear or Clearstream, Luxembourg, at the same time present or procure the presentation of the relevant Global Note to the Principal Paying Agent (in the case of Bearer Notes) or the Registrar (in the case of Registered Notes) for notation accordingly.

Any Put Notice or other notice given in accordance with the standard procedures of Euroclear and Clearstream, Luxembourg and the CMU given by a holder of any Note pursuant to this Condition 7.4 shall be irrevocable except where, prior to the due date of redemption, an Event of Default has occurred and the Trustee has declared the Notes to be due and payable pursuant to Condition 10, in which event such holder, at its option, may elect by notice to the Issuer to withdraw the notice given pursuant to this Condition 7.4.

7.5 Redemption upon a Change of Control

Following the occurrence of a Change of Control (as defined below), the holder of each Note will have the right at such holder's option, to require the Issuer to redeem all, but not some only, of that holder's Notes on the Change of Control Redemption Date (as defined in Condition 7.7) at 101 per cent. of their Early Redemption Amount together with accrued interest.

The Trustee shall not be required to take any steps to ascertain whether a Change of Control or any event which could lead to the occurrence of a Change of Control has occurred and will not be liable to any person for any failure to do so.

The Issuer shall give notice to Noteholders and the Trustee in accordance with Condition 14 by not later than 14 days following the first day on which it becomes aware of the occurrence of a Change of Control, which notice shall specify the procedure for exercise by holders of their rights to require redemption of the Notes pursuant to this Condition and shall give brief details of the Change of Control.

For the purposes of this Condition 7.5:

Affiliate means, with respect to any Person, any other Person (a) directly or indirectly controlling, controlled by, or under direct or indirect common control with, such Person, or who is a director or officer of such Person or (b) any subsidiary of such Person or of any Person referred to in clause (a) of this definition. For purposes of this definition, **control** (including, with correlative meanings, the terms **controlling**, **controlled by** and **under common control with**), as applied to any Person, means the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of such Person, whether through the ownership of voting securities, by contract or otherwise.

Change of Control means the occurrence of any of the following:

- (i) the Permitted Holders cease to be the beneficial owners of at least 35 per cent. of the total voting power of the Voting Stock of the Issuer; or
- (ii) the Permitted Holders cease to be the largest beneficial owners of the total voting power of the Voting Stock of the Issuer; or
- (iii) the Issuer consolidates with or merges into or sells or transfers all or substantially all of its assets to any Person or Persons (other than any of the Permitted Holders where such Permitted Holder assumes all of the obligations of the Issuer under the Trust Deed, the Agency Agreement and the Notes or such sale or transfer of such assets in accordance with Condition 7.6) unless the consolidation, merger, sale or transfer will not result in the other Person or Persons acquiring control over the Issuer or the successor entity; or
- (iv) individuals who on the Issue Date constituted the Board of Directors of the Issuer (together with any new directors nominated or elected by a vote of at least a majority of the members of the Board of Directors of the Issuer then in office who were members of the Board of Directors of the Issuer on the Issue Date or whose election was previously so nominated or elected) cease for any reason to constitute a majority of the members of the Board of Directors of the Issuer then in office.

Permitted Holders mean, (i) Top Frontier Investment Holdings, Inc., (ii) Master Year Limited and (iii) any Affiliate of, or any Person who is a Related Person with respect to, those mentioned in (i) or (ii) above.

Related Person with respect to any Person means:

- (i) any controlling stockholder or a majority (or more) owned Subsidiary of such Person, or, in the case of an individual, any spouse or immediate family member of such Person, any trust created for the benefit of such individual or such individual's estate, executor, administrator, committee or beneficiaries; or
- (ii) any trust, corporation, partnership or other entity, the beneficiaries, stockholders, partners, owners or Persons beneficially holding a majority (or more) controlling interest of which consist of such Person and/or such other Persons referred to in the immediately preceding paragraph.

Voting Stock means, with respect to any Person, Capital Stock of any class or kind ordinarily having the power to vote for the election of directors, managers or other voting members of the governing body of such Person.

7.6 Redemption upon Disposal Event

Following the occurrence of a Disposal Event (as defined below), the holder of each Note will have the right at such holder's option, to require the Issuer to redeem all, but not some only, of that holder's Notes on the

Disposal Event Redemption Date (as defined in Condition 7.7) at 100 per cent. of their Early Redemption Amount together with accrued interest.

The Trustee shall not be required to take any steps to ascertain whether a Disposal Event or any event which could lead to the occurrence of a Disposal Event has occurred and will not be liable to any person for any failure to do so.

The Issuer shall give notice to Noteholders and the Trustee in accordance with Condition 14 by not later than 14 days following the first day on which it becomes aware of the occurrence of a Disposal Event, which notice shall specify the procedure for exercise by holders of their rights to require redemption of the Notes pursuant to this Condition and shall give brief details of the Disposal Event.

For the purposes of this Condition 7.6:

Disposal occurs when, as a result of a sale, transfer or other disposal of Capital Stock of a Material Subsidiary, the Issuer ceases to be the beneficial owner of more than 50.0 per cent. of the total voting power of the Voting Stock of such Material Subsidiary.

Disposal Event means the occurrence of a Disposal, unless:

- (i) no Indebtedness (whether in whole or in part) of the Issuer becomes (or becomes capable of being declared) due and payable prior to its stated maturity pursuant to the terms of such Indebtedness as a result of such Disposal; and
- (ii) within 365 days of the occurrence of a Disposal, the Group acquires a majority stake in a Replacement Subsidiary or majority stakes in Replacement Subsidiaries (provided that no member of the Group shall, as a result of any such acquisition, acquire or incur any Project Debt); and (X) based on the latest annual audited financial statements of such Replacement Subsidiary or Replacement Subsidiaries provided by the Issuer to the Trustee, such Replacement Subsidiary or Replacement Subsidiaries contribute Replacement EBITDA that is equal to or greater than that portion of Consolidated EBITDA attributable to the shares in the relevant Material Subsidiary disposed of in the Disposal, and (Y) the business or series of businesses to be acquired are in food and packaging, beverages, financial services, energy, power, oil and gas, mining, infrastructure, telecommunication services and such other businesses as may be approved by the Board of Directors of the Issuer and, as may be required by law, approved by the stockholders of the Issuer.

Replacement EBITDA means, in respect of any Relevant Period, the net operating income of the Replacement Subsidiary:

- (i) before any provision on account of taxation;
- (ii) before any interest, commission, discounts or other fees incurred or payable, received or receivable by the Replacement Subsidiary in respect of Indebtedness;
- (iii) before any items treated as exceptional or extraordinary items; and
- (iv) before any amount attributable to the amortization of intangible assets and depreciation of tangible assets,

and so that no amount shall be included or excluded more than once.

Replacement Subsidiary means any entity that satisfies the following conditions:

- (i) such entity has been acquired by the Issuer or a Subsidiary of the Issuer pursuant to this Condition 7.6;
- (ii) such entity is not a Ring-fenced Subsidiary; and
- (iii) the Issuer has delivered a written notification to the Trustee designating such entity as a “Replacement Subsidiary”.

For the avoidance of doubt, the Issuer may only designate an entity as a “Replacement Subsidiary” once, provided that the Issuer may designate one or more entities as the “Replacement Subsidiary” of a Material Subsidiary which is divested.

Each Subsidiary of any Replacement Subsidiary referred to above shall also be a **Replacement Subsidiary**.

7.7 Procedures for Redemption upon a Change of Control or a Disposal Event

To exercise the right to require redemption of the Notes pursuant to Condition 7.5 or 7.6, the holder of this Note must, if this Note is in definitive form and held outside Euroclear, Clearstream, Luxembourg and the

CMU, deliver, to the specified office of any Paying Agent (in the case of Bearer Notes) or the Registrar (in the case of Registered Notes), at any time during the normal business hours of such Paying Agent or, as the case may be, the Registrar by not later than the 60th day following a Change of Control or, as the case may be, an occurrence of a Disposal Event, or, if later, the 60th day following the date upon which notice thereof is given to Noteholders by the Issuer in accordance with Condition 14, a duly completed and signed notice of redemption in the form (for the time being current) obtainable from any specified office of any Paying Agent or, as the case may be, the Registrar (the **Change of Control Redemption Notice** (in the case of redemption of the Notes pursuant to Condition 7.5) or the **Disposal Event Redemption Notice** (in the case of redemption of the Notes pursuant to Condition 7.6)) and in which the holder must specify a bank account (or, if payment is required to be made by cheque, an address) to which payment is to be made under this Condition. If such Note is a Definitive Bearer Note, the Change of Control Redemption Notice or, as the case may be, the Disposal Event Redemption Notice must be accompanied by this Note or evidence satisfactory to the Paying Agent concerned that this Note will, following delivery of the Change of Control Redemption Notice or, as the case may be, the Disposal Event Redemption Notice, be held to its order or under its control. If this Note is represented by a Global Note or is in definitive form and held through Euroclear or Clearstream, Luxembourg or the CMU, to exercise the right to require redemption of this Note, the holder of this Note must, within the notice period, give notice to the Principal Paying Agent (in the case of Bearer Notes) or the Registrar (in the case of Registered Notes) of such exercise in accordance with the standard procedures of Euroclear and Clearstream, Luxembourg or the CMU (which may include notice being given on his instruction by Euroclear or Clearstream, Luxembourg or the CMU or any common depositary, as the case may be, for them to the Principal Paying Agent (in the case of Bearer Notes) or the Registrar (in the case of Registered Notes) by electronic means or notice being given to the CMU Lodging Agent) in a form acceptable to Euroclear and Clearstream, Luxembourg or the CMU and the CMU Lodging Agent, as the case may be, from time to time and, if this Note is represented by a Global Note held through Euroclear or Clearstream, Luxembourg, at the same time present or procure the presentation of the relevant Global Note to the Principal Paying Agent (in the case of Bearer Notes) or the Registrar (in the case of Registered Notes) for notation accordingly.

Any Change of Control Redemption Notice or Disposal Event Redemption Notice, once delivered, shall be irrevocable and the Issuer shall redeem the Notes the subject of Change of Control Redemption Notices or, as the case may be, Disposal Event Redemption Notices delivered as aforesaid on the Change of Control Redemption Date or the Disposal Event Redemption Date, respectively.

For the purposes of these Conditions:

Change of Control Redemption Date shall be the fourteenth day after the expiry of such period of 60 days after the later of a Change of Control or the date upon which notice of Change of Control is given to the Noteholders by the Issuer in accordance with Condition 14 as referred above.

Disposal Event Redemption Date shall be the fourteenth day after the expiry of such period of 60 days after the later of a Disposal Event or the date upon which notice of Disposal Event is given to the Noteholders by the Issuer in accordance with Condition 14 as referred above.

7.8 Early Redemption Amounts

For the purpose of Conditions 7.2, 7.5 and 7.6 above and Condition 10, each Note will be redeemed at its Early Redemption Amount calculated as follows:

- (a) in the case of a Note with a Final Redemption Amount equal to the Issue Price, at the Final Redemption Amount thereof;
- (b) in the case of a Note (other than a Zero Coupon Note but including an Installment Note and Partly Paid Note) with a Final Redemption Amount which is or may be less or greater than the Issue Price or which is payable in a Specified Currency other than that in which the Note is denominated, at the amount specified in, or determined in the manner specified in, the applicable Pricing Supplement or, if no such amount or manner is so specified in the applicable Pricing Supplement, at its nominal amount; or
- (c) in the case of a Zero Coupon Note, at an amount (the **Amortized Face Amount**) calculated in accordance with the following formula:

$$\text{Early Redemption Amount} = \text{RP} \times (1 + \text{AY})^y$$

where:

RP means the Reference Price;

AY means the Accrual Yield expressed as a decimal; and

- y is the Day Count Fraction specified in the applicable Pricing Supplement which will be either (i) 30/360 (in which case the numerator will be equal to the number of days (calculated on the basis of a 360-day year consisting of 12 months of 30 days each) from (and including) the Issue Date of the first Tranche of the Notes to (but excluding) the date fixed for redemption or (as the case may be) the date upon which such Note becomes due and repayable and the denominator will be 360) or (ii) Actual/360 (in which case the numerator will be equal to the actual number of days from (and including) the Issue Date of the first Tranche of the Notes to (but excluding) the date fixed for redemption or (as the case may be) the date upon which such Note becomes due and repayable and the denominator will be 360) or (iii) Actual/365 (in which case the numerator will be equal to the actual number of days from (and including) the Issue Date of the first Tranche of the Notes to (but excluding) the date fixed for redemption or (as the case may be) the date upon which such Note becomes due and repayable and the denominator will be 365).

7.9 Installments

Installment Notes will be redeemed in the Installment Amounts and on the Installment Dates. In the case of early redemption, the Early Redemption Amount will be determined pursuant to Condition 7.8 above.

7.10 Partly Paid Notes

Partly Paid Notes will be redeemed, whether at maturity, early redemption or otherwise, in accordance with the provisions of this Condition and the applicable Pricing Supplement.

7.11 Purchases

Subject to applicable laws, the Issuer or any Subsidiary of the Issuer may at any time purchase Notes (provided that, in the case of definitive Bearer Notes, all unmatured Receipts, Coupons and Talons appertaining thereto are purchased therewith) at any price in the open market or otherwise. Such Notes may be held, reissued, resold or, at the option of the Issuer, surrendered to any Paying Agent and/or the Registrar for cancellation.

7.12 Cancellation

All Notes which are redeemed will forthwith be cancelled (together with all unmatured Receipts, Coupons and Talons attached thereto or surrendered therewith at the time of redemption). All Notes so cancelled and any Notes purchased and cancelled pursuant to Condition 7.11 above (together with all unmatured Receipts, Coupons and Talons cancelled therewith) shall be forwarded to the Principal Paying Agent (which shall notify the Registrar of such cancelled Notes in the case of Registered Notes) and may not be reissued or resold.

7.13 Late Payment on Zero Coupon Notes

If the amount payable in respect of any Zero Coupon Note upon redemption of such Zero Coupon Note pursuant to Conditions 7.1, 7.2, 7.3, 7.4, 7.5 or 7.6 above or upon its becoming due and repayable as provided in Condition 10 is improperly withheld or refused, the amount due and repayable in respect of such Zero Coupon Note shall be the amount calculated as provided in Condition 7.8(c) above as though the references therein to the date fixed for the redemption or the date upon which such Zero Coupon Note becomes due and payable were replaced by references to the date which is the earlier of:

- (i) the date on which all amounts due in respect of such Zero Coupon Note have been paid; and
- (ii) five days after the date on which the full amount of the moneys payable in respect of such Zero Coupon Note has been received by the Trustee or the Principal Paying Agent or the Registrar and notice to that effect has been given to the Noteholders in accordance with Condition 14.

8. TAXATION

8.1 Payment without Withholding

All payments of principal, premium and interest by or on behalf of the Issuer in respect of the Notes, Receipts and Coupons shall be made free and clear of, and without withholding or deduction for, any taxes, duties, assessments or governmental charges of whatever nature imposed, levied, collected, withheld or assessed by or within the Philippines or any political subdivision or any authority thereof or therein having power to tax, unless such withholding or deduction is required by law. Where such withholding or deduction is made by the Issuer at the rate of up to and including 20 per cent., the Issuer will increase the amounts paid

by it to the extent required, so that the net amount received by the holders of the Notes, Receipts or Coupons equals the amounts which would otherwise have been receivable by them had no such withholding or deduction been required. In the event that the Issuer makes a deduction or withholding required by law in excess of 20 per cent., the Issuer shall pay such additional amounts (the **Additional Amounts**) as will result in receipt by the holders of the Notes, Receipts or Coupons of such amounts as would have been received by them had no such withholding or deduction been required, except that no such Additional Amounts shall be payable in respect of any Note, Receipt or Coupon:

- (a) **Other connection:** to or on behalf of a holder who is liable to such taxes, duties, assessments or governmental charges in respect of such Note, Receipt or Coupon by reason of his having some connection with a Tax Jurisdiction other than the mere holding of such Note, Receipt or Coupon or where the withholding or deduction could be avoided under the laws of the Tax Jurisdiction by the holder making a declaration of non-residence or other similar claim for exemption to the appropriate authority which such holder is legally capable and competent of making but fails to do so following a timely request by the Issuer; or
- (b) **Surrender more than 30 days after the Relevant Date:** presented for payment more than 30 days after the Relevant Date (as defined below) except to the extent that the holder of it would have been entitled to such Additional Amounts on surrendering the relevant Note, Receipt or Coupon for payment on the last day of such period of 30 days assuming that day to have been a Payment Day (as defined in Condition 6.6); or
- (c) **Payment to individuals:** where such withholding or deduction is imposed on a payment to an individual and is required to be made pursuant to European Council Directive 2003/48/EC on the taxation of savings income or any law implementing or complying with, or introduced in order to conform to, such Directive; or
- (d) **Payment by another Paying Agent:** (except in the case of Registered Notes) presented for payment by or on behalf of a holder who would have been able to avoid such withholding or deduction by presenting the relevant Note, Receipt or Coupon to another Paying Agent in a Member State of the European Union.

8.2 Interpretation

As used herein:

- (i) **Relevant Date** in respect of any Note, Receipt or Coupon means the date on which payment in respect of it first becomes due or (if any amount of the money payable is improperly withheld or refused) the date on which payment in full of the amount outstanding is made or (if earlier) the date seven days after that on which notice is duly given to the Noteholders in accordance with Condition 14 that, upon further surrender of the relevant Note, Receipt or Coupon being made in accordance with the Conditions, such payment will be made, provided that payment is in fact made upon such surrender; and
- (ii) **Tax Jurisdiction** means the Philippines or any political subdivision or any authority thereof or therein having power to tax.

9. PRESCRIPTION

The Notes (whether in bearer or registered form), Receipts and Coupons will become void unless presented for payment within a period of 10 years (in the case of principal) and five years (in the case of interest) after the Relevant Date (as defined in Condition 8.2) therefor.

There shall not be included in any Coupon sheet issued on exchange of a Talon any Coupon the claim for payment in respect of which would be void pursuant to this Condition or Condition 6.2 or any Talon which would be void pursuant to Condition 6.2.

10. EVENTS OF DEFAULT AND ENFORCEMENT

10.1 Events of Default

If any of the following events (each an **Event of Default**) occurs and is continuing the Trustee at its discretion may, and if so requested in writing by the holders of at least 25 per cent. in nominal amount of the Notes then outstanding or if so directed by an Extraordinary Resolution of the Noteholders shall (subject in each case to being indemnified, secured and/or prefunded to its satisfaction), give notice in writing to the

Issuer that each Note is, and each Note shall thereupon immediately become, due and repayable at its Early Redemption Amount together with accrued interest as provided in the Trust Deed:

- (a) **Non-Payment:** there is failure to pay the principal, premium (if any) or interest on any of the Notes when due and, in the case of failure to pay interest, such failure continues for a period of seven (7) days; or
- (b) **Breach of Other Obligations:** the Issuer defaults in the performance or observance of, or compliance with, any one or more of its other obligations under the Conditions or the Trust Deed, which default is incapable of remedy or, if in the opinion of the Trustee capable of remedy, is not in the opinion of the Trustee remedied within 30 days after notice of such default shall have been given to the Issuer by the Trustee; or
- (c) **Cross-Default:** (i) any other present or future Indebtedness of the Issuer or any of its Material Subsidiaries for or in respect of moneys borrowed or raised becomes (or becomes capable of being declared) due and payable prior to its stated maturity by reason of any event of default or the like (howsoever described), or (ii) any such indebtedness is not paid when due or, as the case may be, within any originally applicable grace period, or (iii) the Issuer or any of its Material Subsidiaries fails to pay when due any amount payable by it under any present or future guarantee for, or indemnity in respect of, any moneys borrowed or raised, provided that the aggregate amount the relevant indebtedness, guarantees and indemnities in respect of one or more events mentioned above in this subparagraph (c) exceeds U.S.\$25,000,000 or its equivalent (on the basis of the amount of U.S. dollars obtained by converting foreign currency into U.S. dollars with the applicable foreign currency as quoted by the Bangko Sentral ng Pilipinas); or
- (d) **Judgment, Decree or Order:** a final judgment, decree or order has been entered against the Issuer or any Material Subsidiary of the Issuer by a court of competent jurisdiction from which no appeal may be made or is taken for the payment of money in excess of U.S.\$25,000,000 or its equivalent (on the basis of the amount of U.S. dollars obtained by converting foreign currency into U.S. dollars with the applicable foreign currency as quoted by the Bangko Sentral ng Pilipinas) and any relevant period specified for payment of such judgment, decree or order shall have expired without it being satisfied, discharged or stayed; or
- (e) **Enforcement Proceedings:** a distress, attachment, execution or other legal process is levied, enforced or sued out on or against any material part of the property, assets or revenues of the Issuer or any Material Subsidiary of the Issuer and is not discharged or stayed within 30 days of having been so levied, enforced or sued; or
- (f) **Security Enforced:** a secured party takes possession, or a receiver, manager or other similar officer is appointed, of the whole or any material part of the undertaking, asset or revenues of the Issuer or any of its Material Subsidiaries and is not discharged within 60 days; or
- (g) **Insolvency:** the Issuer or any Material Subsidiary of the Issuer (i) is (or is deemed by law or a court to be) insolvent or bankrupt or unable to pay its debts, (ii) stops, suspends or threatens to stop or suspend payment of all or a material part of (or of a particular type of) its debts, (iii) proposes or makes any agreement for the deferral, rescheduling or other readjustment of all of (or all of a particular type of) its debts (or of any part which it will or might otherwise be unable to pay when due), (iv) proposes or makes a general assignment or an arrangement or composition with or for the benefit of the relevant creditors in respect of any of such debts, or (v) a moratorium is agreed or declared in respect of or affecting all or any part of (or of a particular type of) the debts of the Issuer or any Material Subsidiary of the Issuer; or
- (h) **Winding-up:** an order of a court of competent jurisdiction is made or an effective resolution passed for the winding-up or dissolution or administration of the Issuer or any Material Subsidiary of the Issuer, or the Issuer or any Material Subsidiary of the Issuer ceases or threatens to cease to carry on all or substantially all of its business or operations, except for the purpose of and followed by (i) a reconstruction, amalgamation, reorganization, merger or consolidation (x) on terms approved by a resolution of the Noteholders, or (y) in the case of a Material Subsidiary, whereby the undertaking and assets of the Material Subsidiary are transferred to or otherwise vested in the Issuer or another Material Subsidiary pursuant to a merger of the Material Subsidiary with the Issuer or such other Material Subsidiary or by way of a voluntary winding-up or dissolution where there are surplus assets in such Material Subsidiary and such surplus assets attributable to the Issuer and/or any other Material Subsidiary are distributed to the Issuer and/or any such other Material Subsidiary or (ii) a merger or

consolidation with respect to the Issuer which is not, in the opinion of the Trustee, materially prejudicial to the interests of the Noteholders; or

- (i) **Bankruptcy Proceedings:** proceedings shall have been initiated against the Issuer or any Material Subsidiary of the Issuer under any applicable bankruptcy, insolvency or reorganization law and such proceedings shall not have been discharged or stayed within a period of 60 days; or
- (j) **Validity:** the Issuer shall contest in writing the validity or enforceability of any of the Notes or shall deny generally in writing the liability of the Issuer under any of the Notes; or
- (k) **Analogous Events:** any event occurs, which, in the opinion of the Trustee, under the laws of any relevant jurisdiction has an analogous effect to any of the events referred to in any of the foregoing paragraphs (g), (h) and (i) of this Condition 10.1.

10.2 Enforcement

The Trustee may at any time, at its discretion and without notice, take such proceedings against the Issuer as it may think fit to enforce the provisions of the Trust Deed, the Notes, the Receipts and the Coupons, but it shall not be bound to take any such proceedings or any other action in relation to the Trust Deed, the Notes, the Receipts or the Coupons unless (i) it shall have been so directed by an Extraordinary Resolution of the Noteholders or so requested in writing by the holders of at least 25 per cent. in nominal amount of the Notes then outstanding and (ii) it shall have been indemnified, secured and/or prefunded to its satisfaction.

No Noteholder, Receiptholder or Couponholder shall be entitled to proceed directly against the Issuer unless the Trustee, having become bound so to proceed, fails so to do within a reasonable period and the failure shall be continuing.

11. REPLACEMENT OF NOTES, RECEIPTS, COUPONS AND TALONS

Should any Note, Receipt, Coupon or Talon be lost, stolen, mutilated, defaced or destroyed, it may be replaced subject to applicable laws, regulations and relevant stock exchange regulations at the specified office of the Principal Paying Agent or (where applicable) or of the Registrar (in the case of Registered Notes) upon payment by the claimant of such costs and expenses as may be incurred in connection therewith and on such terms as to evidence and indemnity as the Issuer and the Principal Paying Agent may reasonably require. Mutilated or defaced Notes, Receipts, Coupons or Talons must be surrendered before replacements will be issued.

12. PAYING AGENTS, REGISTRAR AND TRANSFER AGENTS

The names of the initial Paying Agents, the initial Registrar and the other initial Transfer Agents and their initial specified offices are set out below.

The Issuer is entitled, with the prior written approval of the Trustee (such approval not to be unreasonably withheld or delayed), to vary or terminate the appointment of the Principal Paying Agent, Paying Agent, Registrar or Transfer Agents and/or appoint additional or other Paying Agents, Registrars or Transfer Agents and/or approve any change in the specified office through which any Agent acts, provided that:

- (a) there will at all times be a Principal Paying Agent and a Registrar;
- (b) so long as the Notes are listed on any stock exchange, there will at all times be a Paying Agent, which may be the Principal Paying Agent, and Transfer Agent with a specified office in the place required by the rules and regulations of the relevant stock exchange or any other relevant authority;
- (c) there will at all times be a Paying Agent in a Member State of the European Union that is not obliged to withhold or deduct tax pursuant to European Council Directive 2003/48/EC or any law implementing or complying with, or introduced in order to conform to, such Directive; and
- (d) so long as any Notes are listed on the Singapore Exchange Securities Trading Limited (the **SGX-ST**) and the rules of the SGX-ST so require, if the Notes are issued in definitive form, there will at all times be a Paying Agent in Singapore unless the Issuer obtains an exemption from the SGX-ST.

In addition, the Issuer shall with the prior written approval of the Trustee (such approval not to be unreasonably withheld or delayed) forthwith appoint a Paying Agent having a specified office in New York City in the circumstances described in Condition 6.5. Any variation, termination, appointment or change referred to in the preceding paragraph and/or any appointment referred to in this paragraph shall only take effect (other than in the case of insolvency, when it shall be of immediate effect) after not less than 30 nor

more than 45 days' prior notice thereof shall have been given to the Noteholders in accordance with Condition 14.

In acting under the Agency Agreement, the Paying Agents, the Registrar and the Transfer Agents act solely as agents of the Issuer and, in certain circumstances specified therein, of the Trustee and do not assume any obligation to, or relationship of agency or trust with, any Noteholders, Receiptholders or Couponholders. The Agency Agreement contains provisions permitting any entity into which any Agent is merged or converted or with which it is consolidated or to which it transfers all or substantially all of its assets to become the successor agent.

13. EXCHANGE OF TALONS

On and after the Interest Payment Date on which the final Coupon comprised in any Coupon sheet matures, the Talon (if any) forming part of such Coupon sheet may be surrendered at the specified office of the Principal Paying Agent or any other Paying Agent in exchange for a further Coupon sheet including (if such further Coupon sheet does not include Coupons to (and including) the final date for the payment of interest due in respect of the Note to which it appertains) a further Talon, subject to the provisions of Condition 9.

14. NOTICES

Notices to holders of Registered Notes will be deemed to be validly given if sent by first class mail or (if posted to an overseas address) by air mail to them at their respective addresses as recorded in the Register and will be deemed to have been validly given on the fourth day after the date of such mailing and, in addition, for so long as any Registered Notes are listed on a stock exchange or are admitted to trading by another relevant authority and the rules of that stock exchange or relevant authority so require, such notice will be published in a daily newspaper of general circulation in the place or places required by those rules.

All notices regarding the Bearer Notes will be deemed to be validly given if published in a leading daily newspaper of general circulation in Asia or such other English language daily newspaper with general circulation in Asia. It is expected that such publication will be made in the *Asian Wall Street Journal*. The Issuer shall also ensure that notices are duly published in a manner which complies with the rules and regulations of any stock exchange (or any other relevant authority) on which the Notes are for the time being listed. Any such notice will be deemed to have been given on the date of the first publication or, where required to be published in more than one newspaper, on the date of the first publication in all required newspapers. If publication as provided above is not practicable, a notice will be given in such other manner, and will be deemed to have been given on such date, as the Trustee shall approve.

Until such time as any definitive Notes are issued, there may, so long as any Global Notes representing the Notes are held in their entirety on behalf of (i) Euroclear and/or Clearstream, Luxembourg, be substituted for such mailing and such publication in such newspaper(s) the delivery of the relevant notice to Euroclear and/or Clearstream, Luxembourg for communication by them to the holders of the Notes or (ii) the CMU, be substituted for such publication in such newspaper(s) the delivery of the relevant notice to the persons shown in a CMU Instrument Position Report issued by the CMU on the first business day preceding the date of dispatch of such notice as holding interests in the relevant Global Note and, in the case of both (i) and (ii) above, such notice shall be deemed to have been given to the Noteholders on the date of delivery to Euroclear or Clearstream, Luxembourg or the CMU as the case may be. In addition, in the case of both (i) and (ii) above, for so long as any Notes are listed on a stock exchange and the rules of that stock exchange (or any other relevant authority) so require, such notice will be published in a daily newspaper of general circulation in the place or places required by the rules of that stock exchange (or any other relevant authority). Any such notice shall be deemed to have been given to the holders of the Notes on the day on which the said notice was given to Euroclear and/or Clearstream, Luxembourg and/or the persons shown in the CMU Instrument Position Report.

Notices to be given by any Noteholder shall be in writing and given by lodging the same, together (in the case of any Note in definitive form) with the relative Note or Notes, with the Principal Paying Agent (in the case of Bearer Notes) or the Registrar (in the case of Registered Notes). Whilst any of the Notes are represented by a Global Note, such notice may be given by any holder of a Note to the Principal Paying Agent or the Registrar through Euroclear and/or Clearstream, Luxembourg, and/or, in the case of Notes lodged with the CMU, by delivery by such holder of such notice to the CMU Lodging Agent in Hong Kong, as the case may be, in such manner as the Principal Paying Agent, the Registrar, the CMU Lodging Agent and Euroclear and/or Clearstream, Luxembourg and/or the CMU, as the case may be, may approve for this purpose.

Receiptholders and Couponholders will be deemed for all purposes to have notice of the contents of any notice given to Noteholders in accordance with this Condition 14.

15. MEETINGS OF NOTEHOLDERS, MODIFICATION, WAIVER AND SUBSTITUTION

15.1 Meeting of Noteholders

The Trust Deed contains provisions for convening meetings of the Noteholders to consider any matter affecting their interests, including the sanctioning by Extraordinary Resolution of a modification of the Notes, the Receipts, the Coupons or any of the provisions of the Trust Deed. Such a meeting may be convened by the Issuer or the Trustee and shall be convened by the Issuer if required in writing by Noteholders holding not less than ten per cent. in nominal amount of the Notes for the time being remaining outstanding. The quorum at any such meeting for passing an Extraordinary Resolution is two or more persons holding or representing in the aggregate not less than 50 per cent. in nominal amount of the Notes for the time being outstanding, or at any adjourned meeting two or more persons being or representing Noteholders whatever the nominal amount of the Notes so held or represented, except that at any meeting the business of which includes the modification of certain provisions of the Notes, the Receipts, the Coupons or the Trust Deed (including, *inter alia*, modifying the date of maturity of the Notes or any date for payment of interest thereon, reducing or cancelling the amount of principal or the rate of interest payable in respect of the Notes or altering the currency of payment of the Notes, the Receipts or the Coupons), the quorum shall be two or more persons holding or representing in the aggregate not less than 66 2/3 per cent. in nominal amount of the Notes for the time being outstanding, or at any adjourned such meeting two or more persons holding or representing in the aggregate not less than 25 per cent. in nominal amount of the Notes for the time being outstanding. An Extraordinary Resolution passed at any meeting of the Noteholders shall be binding on all the Noteholders, whether or not they are present at the meeting, and on all Receiptholders and Couponholders.

The Trust Deed provides that a resolution in writing signed by or on behalf of the holders of not less than 90 per cent. in principal amount of the Notes outstanding shall for all purposes be as valid and effective as an Extraordinary Resolution passed at a meeting of Noteholders duly convened and held. Such a resolution in writing may be contained in one document or several documents in the same form, each signed by or on behalf of one or more Noteholders.

15.2 Modifications and Waivers

The Trustee may agree, without the consent or sanction of the Noteholders, Receiptholders or Couponholders, to any modification (except such modifications in respect of which an increased quorum is required as mentioned above) of, or to the waiver or authorisation of any breach or proposed breach of, any of the provisions of the Notes or the Trust Deed, where, in any such case, it is not, in the opinion of the Trustee, materially prejudicial to the interests of the Noteholders so to do or may agree, without any such consent as aforesaid, to any modification which is of a formal, minor or technical nature or to correct a manifest error. Any such modification shall be binding on the Noteholders, the Receiptholders and the Couponholders and, unless the Trustee agrees otherwise, any such modification shall be notified by the Issuer to the Noteholders in accordance with Condition 14 as soon as practicable thereafter.

In connection with the exercise by it of any of its trusts, powers, authorities and discretions (including, without limitation, any modification, waiver, authorisation, determination or substitution), the Trustee shall have regard to the general interests of the Noteholders as a class but shall not have regard to any interests arising from circumstances particular to individual Noteholders, Receiptholders or Couponholders (whatever their number) and, in particular but without limitation, shall not have regard to the consequences of any such exercise for individual Noteholders, Receiptholders or Couponholders (whatever their number) resulting from their being for any purpose domiciled or resident in, or otherwise connected with, or subject to the jurisdiction of, any particular territory or any political sub-division thereof and the Trustee shall not be entitled to require, nor shall any Noteholder, Receiptholder or Couponholder be entitled to claim, from the Issuer, the Trustee or any other person any indemnification or payment in respect of any tax consequences of any such exercise upon individual Noteholders, Receiptholders or Couponholders except to the extent already provided for in Condition 8 and/or any undertaking or covenant given in addition to, or in substitution for, Condition 8 pursuant to the Trust Deed.

15.3 Substitution of Issuer

The Trustee may, without the consent of the Noteholders, the Receiptholders or the Couponholders at any time, agree with the Issuer to the substitution in place of the Issuer (or of the previous substitute under this

Condition) as the principal debtor under the Notes, the Receipts, the Coupons and the Trust Deed of any entity owned or controlled by the Issuer, subject to (a) the Notes being unconditionally and irrevocably guaranteed by the Issuer, (b) the Trustee being satisfied that (having received an opinion from independent financial, legal or tax advisors of recognized international standing) the interests of the Noteholders will not be materially prejudiced by the substitution and (c) certain other conditions set out in the Trust Deed being complied with.

15.4 General

Any such modification, waiver, authorisation, determination or substitution shall be binding on the Noteholders, the Receiptholders and the Couponholders and, unless the Trustee otherwise agrees, any such modification or substitution shall be promptly notified to Noteholders by the Issuer in accordance with Condition 14.

16. INDEMNIFICATION OF THE TRUSTEE AND TRUSTEE CONTRACTING WITH THE ISSUER

The Trust Deed contains provisions for the indemnification of the Trustee and for its relief from responsibility, including provisions relieving it from taking action unless indemnified and/or provided with security and/or prefunded to its satisfaction.

The Trust Deed also contains provisions pursuant to which the Trustee is entitled, *inter alia*, (a) to enter into transactions or arrangements with the Issuer and to act as trustee for the holders of any other securities issued or guaranteed by, or relating to, the Issuer, (b) to exercise and enforce its rights, comply with its obligations and perform its duties under or in relation to any such transactions and arrangements or, as the case may be, any such trusteeship without regard to the interests of, or consequences for, the Noteholders, Receiptholders or Couponholders and (c) to retain and not be in any way liable to account for any profit made or any other amount or benefit received thereby or in connection therewith.

17. FURTHER ISSUES

The Issuer shall be at liberty from time to time without the consent of the Noteholders, the Receiptholders or the Couponholders to create and issue further notes having terms and conditions the same as the Notes or the same in all respects save for the amount and date of the first payment of interest thereon and so that the same shall be consolidated and form a single Series with the outstanding Notes.

18. CONTRACTS (RIGHTS OF THIRD PARTIES) ACT 1999

No rights are conferred on any person under the Contracts (Rights of Third Parties) Act 1999 to enforce any term of this Note, but this does not affect any right or remedy of any person which exists or is available apart from that Act.

19. GOVERNING LAW AND SUBMISSION TO JURISDICTION

19.1 Governing Law

The Trust Deed, the Agency Agreement, the Notes, the Receipts and the Coupons and any non-contractual obligations arising out of or in connection with the Trust Deed, the Agency Agreement, the Notes, the Receipts and the Coupons are governed by, and shall be construed in accordance with, English law.

19.2 Submission to Jurisdiction

The Issuer has in the Trust Deed agreed, for the exclusive benefit of the Trustee, the Noteholders, the Receiptholders and the Couponholders, that the courts of England are to have exclusive jurisdiction to settle any disputes which may arise out of or in connection with the Trust Deed, the Notes, the Receipts and/or the Coupons (including a dispute relating to any non-contractual obligations arising out of or in connection with the Trust Deed, the Notes, the Receipts and/or the Coupons) and that accordingly any suit, action or proceedings (together referred to as **Proceedings**) arising out of or in connection with the Trust Deed, the Notes, the Receipts and/or the Coupons (including a dispute relating to any non-contractual obligations arising out of or in connection with the Trust Deed, the Notes, the Receipts and/or the Coupons) may be brought in the English courts.

The Issuer has in the Trust Deed irrevocably and unconditionally waived and agreed not to raise any objection which it may have now or hereafter to the laying of the venue of any Proceedings (including any Proceedings relating to any non-contractual obligations arising out of or in connection with the Trust Deed, the Notes, the Receipts and the Coupons) arising out of or in connection with the Trust Deed, the Notes, the

Receipts and the Coupons in the courts of England and any claim that any such Proceedings have been brought in an inconvenient forum and has further irrevocably and unconditionally agreed in the Trust Deed that a judgment in any such Proceedings brought in the English courts shall be conclusive and binding upon it and may be enforced in the courts of any other jurisdiction.

19.3 Appointment of Process Agent

The Issuer has, in the Trust Deed, irrevocably and unconditionally appointed Law Debenture Corporate Services Limited at its specified office for the time being at Fifth Floor, 100 Wood Street, London EC2V 7EX as its agent for service of process in England in respect of any Proceedings and has undertaken that in the event of such agent ceasing so to act it will appoint such other person as the Trustee may approve as its agent for that purpose.

FORM OF PRICING SUPPLEMENT

The form of Pricing Supplement that will be issued in respect of each Tranche, subject only to the deletion of non-applicable provisions, is set out below:

[Date]

SAN MIGUEL CORPORATION

**Issue of [Aggregate Nominal Amount of Tranche] [Title of Notes]
under its U.S.\$2,000,000,000
Medium Term Note Programme**

This document constitutes the Pricing Supplement relating to the issue of Notes described herein. Terms used herein shall be deemed to be defined as such for the purposes of the Conditions (the **Conditions**) set forth in the Offering Memorandum dated April 15, 2013. This Pricing Supplement contains the final terms of the Notes and must be read in conjunction with such Offering Memorandum. Full information on the Issuer and the offer of the Notes is only available on the basis of the combination of this Pricing Supplement and the Offering Memorandum.

[N.B. If the Issuer has prepared any unaudited, but reviewed, condensed consolidated financial statements dated as at a date, or for a period ending, subsequent to the financial statements appearing in the latest Offering Memorandum, ensure that such financial statements are provided to potential investors of the relevant series of Notes as soon as practicable upon announcement of the deal.]

[The following alternative language applies if the first tranche of an issue which is being increased was issued under an Offering Memorandum with an earlier date.]

Terms used herein shall be deemed to be defined as such for the purposes of the Conditions (the **Conditions**) set forth in the Offering Memorandum dated April 15, 2013. This Pricing Supplement contains the final terms of the Notes and must be read in conjunction with the Offering Memorandum dated [current date], save in respect of the Conditions which are extracted from the Offering Memorandum dated [original date] and are attached hereto.]

[Include whichever of the following apply or specify as “Not Applicable” (N/A). Note that the numbering should remain as set out below, even if “Not Applicable” is indicated for individual paragraphs or sub-paragraphs. Italics denote directions for completing the Pricing Supplement.]

[If the Notes have a maturity of less than one year from the date of their issue, the minimum denomination may need to be £100,000 or its equivalent in any other currency.]

1. Issuer: San Miguel Corporation
2. (i) Series Number: []
(ii) Tranche Number: []
(iii) Date on which the Notes will be consolidated and form a single Series: The Notes will be consolidated and form a single Series with [identify earlier Tranches] on [the Issue Date/exchange of the Temporary Bearer Global Note for interests in the Permanent Bearer Global Note, as referred to in paragraph 25 below, which is expected to occur on or about [date]][Not Applicable]
3. Specified Currency or Currencies: []
4. Aggregate Nominal Amount:
(i) Series: []
(ii) Tranche: []
5. (i) Issue Price: [] per cent. of the Aggregate Nominal Amount [plus accrued interest from [insert date] (if applicable)]
(ii) [Net proceeds: []
[Delete for unlisted issuances.]

- (iii) [Reasons for the offer] []
(N.B. If proceeds are intended for a specific use, consider specifying such use. If the Issuer pays to certain private banks a commission based on the principal amount of the Notes purchased by private bank clients, please consider specifying such arrangement in here.)
6. (i) Specified Denominations: (in the case of Registered Notes, this means the minimum integral amount in which transfers can be made) []
(N.B. Notes to be admitted to trading on a regulated market within the European Economic Area must have a minimum denomination of €100,000 (or equivalent) in order to benefit from Transparency Directive exemptions in respect of wholesale securities. Similarly, Notes issued in a Member State must have a minimum denomination of €100,000 (or equivalent) in order to benefit from the wholesale exemption set out in Article 3.2(d) of the Prospectus Directive in that Member State.)
(N.B. Where multiple denominations above [€100,000] or equivalent are being used the following sample wording should be followed: “[€100,000] and integral multiples of [€ 1,000] in excess thereof up to and including [€ 199,000]. No Notes in definitive form will be issued with a denomination above [€199,000].”)
(N.B. If an issue of Notes is (i) NOT admitted to trading on an European Economic Area exchange; and (ii) only offered in the European Economic Area in circumstances where a prospectus is not required to be published under the Prospectus Directive the [€100,000] minimum denomination is not required.)
- (ii) Calculation Amount: []
(If there is only one Specified Denomination, insert the Specified Denomination.
If there is more than one Specified Denomination, insert the highest common factor. Note: There must be a common factor in the case of two or more Specified Denominations.)
7. (i) Issue Date: []
(ii) Interest Commencement Date: [specify/Issue Date/Not Applicable]
(N.B. An Interest Commencement Date will not be relevant for certain Notes, for example Zero Coupon Notes.)
8. Maturity Date: [Fixed rate — specify date/Floating rate — Interest Payment Date falling in or nearest to [specify month]]¹
9. Interest Basis: [[] per cent. Fixed Rate]
[[LIBOR/EURIBOR/HIBOR] +/- [] per cent. Floating Rate]
[Zero Coupon]

¹ Note that for Renminbi and Hong Kong dollar denominated Fixed Rate Notes where the Interest Payment Dates are subject to modification it will be necessary to use the second option here.

- [Index Linked Interest]
[Dual Currency Interest]
[specify other]
(further particulars specified below)
10. Redemption/Payment Basis: [Redemption at par]
[Index Linked Redemption]
[Dual Currency Redemption]
[Partly Paid]
[Installment]
[specify other]
11. Change of Interest Basis or Redemption/Payment Basis: [Specify details of any provision for change of Notes into another Interest Basis or Redemption/Payment Basis]
12. Put/Call Options: [Investor Put]
[Issuer Call]
[(further particulars specified below)]
13. Date of [Board] approval for issuance of Notes: [] [and [], respectively]] (*N.B. Only relevant where Board (or similar) authorization is required for the particular tranche of Notes*)
14. Listing: [Singapore/specify other/None]
15. Method of distribution: [Syndicated/Non-syndicated]

PROVISIONS RELATING TO INTEREST (IF ANY) PAYABLE

16. Fixed Rate Note Provisions [Applicable/Not Applicable]
(If not applicable, delete the remaining sub-paragraphs of this paragraph)
- (i) Rate[(s)] of Interest: [] per cent. per annum [payable [annually/semi-annually/quarterly/other (*specify*)] in arrear]
(*If payable other than annually, consider amending Condition 5*)
- (ii) Interest Payment Date(s): [[] in each year up to and including the Maturity Date]/[specify other]²
(*N.B.: This will need to be amended in the case of long or short coupons*)
- (iii) Fixed Coupon Amount(s): (*Applicable to Notes in definitive form*) [] per Calculation Amount³
- (iv) Broken Amount(s): (Applicable to Notes in definitive form) [] per Calculation Amount, payable on the Interest Payment Date falling [in/on] []
- (v) Day Count Fraction: [30/360 or Actual/ Actual (ICMA) or Actual/365 (Fixed)]⁴ or [specify other]]

² Note that for certain Hong Kong dollar denominated Fixed Rate Notes and Renminbi denominated Fixed Rate Notes, the Interest Payment Dates are subject to modification and the following words should be added: “provided that if any Interest Payment Date falls on a day which is not a Business Day, the Interest Payment Date will be the next succeeding Business Day unless it would thereby fall in the next calendar month in which event the Interest Payment Date shall be brought forward to the immediately preceding Business Day. For these purposes, “**Business Day**” means a day, other than a Saturday or a Sunday on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and currency deposits) in Hong Kong and [].”

³ For Renminbi or Hong Kong dollar denominated Fixed Rate Notes where the Interest Payment Dates are subject to modification the following alternative wording is appropriate: “Each Fixed Coupon Amount shall be calculated by multiplying the product of the Rate of Interest and the Calculation Amount by the Day Count Fraction and rounding the resultant figure to the nearest CNY0.01, CNY0.005 being rounded upwards in the case of Renminbi denominated Fixed Rate Notes and to the nearest HK\$0.01, HK\$0.005 being rounded upwards in the case of Hong Kong dollar denominated Fixed Rate Notes.”

⁴ Applicable to Hong Kong dollar denominated Fixed Rate Notes and Renminbi denominated Fixed Rate Notes.

- (vi) Determination Date(s): [] in each year
[Insert regular interest payment dates, ignoring issue date or maturity date in the case of a long or short first or last coupon]
(N.B.: This will need to be amended in the case of regular interest payment dates which are not of equal duration)
(N.B.: Only relevant where Day Count Fraction is Actual/Actual (ICMA))
- (vii) Other terms relating to the method of calculating interest for Fixed Rate Notes: [None/Give details]
17. Floating Rate Note Provisions [Applicable/Not Applicable]
(If not applicable, delete the remaining sub-paragraphs of this paragraph)
- (i) Specified Period(s)/Specified Interest Payment Dates: []
- (ii) Business Day Convention: [Floating Rate Convention/Following Business Day Convention/Modified Following Business Day Convention/Preceding Business Day Convention/*[specify other]*]
- (iii) Additional Business Centre(s): []
- (iv) Manner in which the Rate of Interest and Interest Amount is to be determined: [Screen Rate Determination/ISDA Determination/*specify other*]
- (v) Party responsible for calculating the Rate of Interest and Interest Amount (if not the Principal Paying Agent): []
- (vi) Screen Rate Determination:
- Reference Rate and Relevant Financial Centre: Reference Rate:
[] month [LIBOR/EURIBOR/*specify other Reference Rate*]
Relevant Financial Centre:
[London/Brussels/*specify other Relevant Financial Centre*]
- Interest Determination Date(s): []
(Second London business day prior to the start of each Interest Period if LIBOR (other than Sterling, Hong Kong dollar or euro LIBOR), first day of each Interest Period if Sterling LIBOR or Hong Kong dollar LIBOR or HIBOR and the second day on which the TARGET2 System is open prior to the start of each Interest Period if EURIBOR or euro LIBOR)
- Relevant Screen Page: []
(In the case of EURIBOR, if not Reuters EURIBOR01 ensure it is a page which shows a composite rate or amend the fallback provisions appropriately)

- (vii) ISDA Determination:
- Floating Rate Option: []
 - Designated Maturity: []
 - Reset Date: []
- (In the case of a LIBOR or EURIBOR based option, the first day of the Interest Period)*
- (viii) Margin(s): [+/-] [] per cent. per annum
- (ix) Minimum Rate of Interest: [] per cent. per annum
- (x) Maximum Rate of Interest: [] per cent. per annum
- (xi) Day Count Fraction: [Actual/Actual or Actual/ Actual (ISDA)
Actual/365 (Fixed)
Actual/365 (Sterling)
Actual/360
30/360, 360/360 or Bond Basis
30E/360 or Eurobond Basis
30E/360 (ISDA)
Other]
(See Condition 5 for alternatives)
- (xii) Fallback provisions, rounding provisions and any other terms relating to the method of calculating interest on Floating Rate Notes, if different from those set out in the Conditions: []
18. Zero Coupon Note Provisions [Applicable/Not Applicable]
(If not applicable, delete the remaining sub-paragraphs of this paragraph)
- (i) Accrual Yield: [] per cent. per annum
 - (ii) Reference Price: []
 - (iii) Any other formula/basis of determining amount payable: []
 - (iv) Day Count Fraction in relation to Early Redemption Amounts and late payment: [30/360]
[Actual/360]
[Actual/365]
19. Index Linked Interest Note Provisions [Applicable/Not Applicable]
(If not applicable, delete the remaining sub-paragraphs of this paragraph)
- (i) Index/Formula: [give or annex details]
 - (ii) Calculation Agent: []
 - (iii) Party responsible for calculating the Rate of Interest (if not the Calculation Agent) and Interest Amount (if not the Principal Paying Agent): []
 - (iv) Provisions for determining Coupon where calculation by reference to Index and/or Formula is impossible or impracticable: *[need to include a description of market disruption or settlement disruption events and adjustment provisions]*
 - (v) Specified Period(s)/Specified Interest Payment Dates: []

- (vi) Business Day Convention: [Floating Rate Convention/Following Business Day Convention/Modified Following Business Day Convention/Preceding Business Day Convention/*specify other*]
- (vii) Additional Business Centre(s): []
- (viii) Minimum Rate of Interest: [] per cent. per annum
- (ix) Maximum Rate of Interest: [] per cent. per annum
- (x) Day Count Fraction: []
20. Dual Currency Interest Note Provisions [Applicable/Not Applicable]
- (If not applicable, delete the remaining sub-paragraphs of this paragraph)*
- (i) Rate of Exchange/method of calculating Rate of Exchange: [give or annex details]
- (ii) Party, if any, responsible for calculating the principal and/or interest due (if not the Principal Paying Agent): []
- (iii) Provisions applicable where calculation by reference to Rate of Exchange impossible or impracticable: *[need to include a description of market disruption or settlement disruption events and adjustment provisions]*
- (iv) Person at whose option Specified Currency(ies) is/are payable: []

PROVISIONS RELATING TO REDEMPTION

21. Issuer Call: [Applicable/Not Applicable]
- (If not applicable, delete the remaining sub-paragraphs of this paragraph)*
- (i) Optional Redemption Date(s): []
- (ii) Optional Redemption Amount and method, if any, of calculation of such amount(s): [[] per Calculation Amount/*specify other/see Appendix*]
- (iii) If redeemable in part:
- (a) Minimum Redemption Amount: []
- (b) Maximum Redemption Amount: []
- (iv) Notice periods (if other than as set out in the Conditions): []
- (N.B. If setting notice periods which are different to those provided in the Conditions, the Issuer is advised to consider the practicalities of distribution of information through intermediaries, for example, clearing systems and custodians, as well as any other notice requirements which may apply, for example, as between the Issuer and the Principal Paying Agent or the Trustee.)*
22. Investor Put: [Applicable/Not Applicable]
- (If not applicable, delete the remaining sub-paragraphs of this paragraph)*
- (i) Optional Redemption Date(s): []

- (ii) Optional Redemption Amount and method, if any, of calculation of such amount(s): [[] per Calculation Amount/specify other/see Appendix]
- (iii) Notice periods (if other than as set out in the Conditions): []

(N.B. If setting notice periods which are different to those provided in the Conditions, the Issuer is advised to consider the practicalities of distribution of information through intermediaries, for example, clearing systems and custodians, as well as any other notice requirements which may apply, for example, as between the Issuer and the Principal Paying Agent or the Trustee.)

23. Final Redemption Amount: [[] per Calculation Amount/specify other/see Appendix]
24. Early Redemption Amount payable on redemption for taxation reasons, upon change of control or on event of default and/or the method of calculating the same (if required or if different from that set out in Condition 7.8): [[] per Calculation Amount/specify other/see Appendix]

GENERAL PROVISIONS APPLICABLE TO THE NOTES

25. Form of Notes: [Bearer Notes:
- [Temporary Bearer Global Note exchangeable for a Permanent Bearer Global Note which is exchangeable for Definitive Notes [on 60 days' notice given at any time/only upon an Exchange Event]*]
- [Temporary Bearer Global Note exchangeable for Definitive Notes on and after the Exchange Date]
[Permanent Bearer Global Note exchangeable for Definitive Notes [on 60 days' notice given at any time/only upon an Exchange Event]*]
- *(Ensure that this is consistent with the wording in the "Form of the Notes" section in the Offering Memorandum and the Notes themselves. N.B. The exchange upon notice/at any time options should not be expressed to be applicable if the Specified Denomination of the Notes in paragraph 6 includes language substantially to the following effect: "[€ 100,000] and integral multiples of [€ 1,000] in excess thereof up to and including [€ 199,000]." Furthermore, such Specified Denomination construction is not permitted in relation to any issue of Notes which is to be represented on issue by a Temporary Bearer Global Note exchangeable for Definitive Notes.)*
- [Registered Notes:
- [Registered Global Note ([U.S.\$[] nominal amount) [registered in the name of a nominee for a common depositary for Euroclear and Clearstream, Luxembourg/registered in the name of the HKMA as operator of the CMU]]

26. Additional Financial Centre(s) or other special provisions relating to Payment Dates: [Not Applicable/give details]
(Note that this paragraph relates to the place of payment and not Interest Period end dates to which sub-paragraphs 17(iii) and 19(vii) relate)
27. Talons for future Coupons or Receipts to be attached to Definitive Bearer Notes (and dates on which such Talons mature): [Yes/No. If yes, give details]
28. Details relating to Partly Paid Notes: amount of each payment comprising the Issue Price and date on which each payment is to be made and consequences of failure to pay, including any right of the Issuer to forfeit the Notes and interest due on late payment: [Not Applicable/give details. N.B.: a new form of Temporary Bearer Global Note and/or Permanent Bearer Global Note may be required for Partly Paid issues.]
29. Details relating to Installment Notes:
- (i) Installment Amount(s): [Not Applicable/give details]
- (ii) Installment Date(s): [Not Applicable/give details]
30. Other terms or special conditions: [Not Applicable/give details]

DISTRIBUTION

31. (i) If syndicated, names and addresses of Managers and commitments: [Not Applicable/give names and addresses and commitments]
- (ii) Date of Subscription Agreement: []
- (iii) Stabilizing Manager(s) (if any): [Not Applicable/give name]
32. If non-syndicated, name of relevant Dealer: [Not Applicable/give name and address]
33. Total commission and concession: [] per cent. of the Aggregate Nominal Amount
34. U.S. Selling Restrictions: Reg. S (Category 1/Category 2); [TEFRA D/TEFRA C/TEFRA not applicable]
35. Additional selling restrictions: [Not Applicable/give details]

OPERATIONAL INFORMATION

36. Any clearing system(s) other than Euroclear or Clearstream, Luxembourg and the relevant identification number(s): [CMU/Not Applicable/give name(s) and number(s)]
37. Delivery: Delivery [against/free of] payment
38. Additional Paying Agent(s) (if any): []
- ISIN: []
- Common Code: []

(insert here any other relevant codes such as a CMU instrument number)

[LISTING APPLICATION

This Pricing Supplement comprises the final terms required for the issue of Notes described herein pursuant to the U.S.\$2,000,000,000 Medium Term Note Programme of San Miguel Corporation].

RESPONSIBILITY

The Issuer accepts responsibility for the information contained in this Pricing Supplement.

Signed on behalf of the Issuer:

Signed on behalf of the Issuer:

By: _____
Duly authorized

By: _____
Duly authorized

USE OF PROCEEDS

The net proceeds from the issue of each Tranche of Notes will be used for refinancing, working capital and general corporate purposes of the SMC Group. If, in respect of any particular issue, there is a particular identified use of proceeds, this will be stated in the applicable Pricing Supplement.

CAPITALIZATION AND INDEBTEDNESS

The following table sets out the consolidated capitalization, indebtedness and cash and cash equivalents of SMC as of December 31, 2012. This table should be read in conjunction with the audited consolidated financial statements and the notes thereto of SMC, included elsewhere in this Offering Memorandum.

	As of December 31, 2012	
	₱	US\$(⁽¹⁾) (unaudited)
	(in millions)	
Cash and cash equivalents	125,631	3,060
Short-term indebtedness		
Drafts and loans payable	151,274	3,685
Current maturities of long-term debt	3,279	80
Total short-term debt	154,553	3,765
Long-term indebtedness		
Total long-term debt	220,938	5,382
Equity		
Equity attributable to equity holders of SMC		
Capital Stock — common	16,408	400
Capital Stock — preferred	10,187	248
Additional paid-in capital	177,762	4,330
Revaluation increment	1,352	33
Cumulative translation adjustments	5,088	124
Retained Earnings(⁽²⁾)	181,522	4,422
Treasury Stock	(140,124)	(3,413)
	252,195	6,144
Non-controlling interests	97,585	2,377
Total shareholders' equity	349,780	8,521
Total capitalization(⁽³⁾)	570,718	13,903

(1) The translations from Philippine Pesos to U.S. dollars have been made on the basis of the prevailing exchange rate on December 28, 2012 of ₱41.05 = US\$1.00, being the closing rate for that date for the purchase of U.S. dollars with Philippine Pesos under the PDS.

(2) Retained earnings reflect appropriated amounts plus unappropriated amounts.

(3) Total capitalization, computed as the sum of long-term debt and total shareholders' equity.

Except as described above, there has been no material change in the capitalization of SMC since December 31, 2012.

SELECTED FINANCIAL INFORMATION AND OTHER DATA

Prospective purchasers of the Notes should read the selected financial and other data below together with the financial statements, including the notes thereto, included in this Offering Memorandum. The selected consolidated statements of income data and consolidated statement of cash flows data for the years ended December 31, 2010, 2011 and 2012 and the selected consolidated statement of financial position data as of December 31, 2011 and 2012 are derived from the audited financial statements of SMC, including the notes thereto, which are found elsewhere in this Offering Memorandum.

The selected consolidated statements of income data and consolidated statement of cash flows data for the years ended December 31, 2010, 2011 and 2012 and the selected consolidated statement of financial position data as of December 31, 2011 and 2012 were derived from the consolidated financial statements of SMC, audited by Manabat Sanagustin & Co. and prepared in compliance with PFRS. The information below should be read in conjunction with the consolidated financial statements of SMC and the related notes thereto, which are included elsewhere in this Offering Memorandum. The historical financial condition, results of operations and cash flows of SMC are no guarantee of its future operating and financial performance.

	Years ended December 31,			
	2010	2011	2012	2012
	(P in millions)			(US\$ in millions) (unaudited)
Consolidated Statements of Income Data				
Sales	246,156	535,775	698,868	17,025
Cost of sales	173,929	432,321	594,732	14,488
Gross profit	72,227	103,454	104,136	2,537
Selling and administrative expenses	(37,619)	(47,500)	(51,353)	(1,251)
Interest expense and other financing charges	(16,578)	(27,443)	(29,826)	(727)
Interest income	3,023	4,618	4,254	104
Equity in net earnings (losses) of associates	6,817	2,824	2,691	66
Gain on sale of investments and property and equipment	529	1,046	4,549	111
Other income (charges) — net	7,095	(12)	12,981	316
Income before income tax from continuing operations	35,494	36,987	47,432	1,156
Income tax expense	(11,438)	(8,483)	(8,812)	(215)
Net income	24,056	28,504	38,620	941
Attributable to:				
Equity holders of SMC	20,091	17,518	27,579	672
Non-controlling interests	3,965	10,986	11,041	269
	24,056	28,504	38,620	941

	As of December 31,		
	2011	2012	2012
	(P in millions)		(US\$ in millions) (unaudited)
Consolidated Statements of Financial Position Data			
Assets			
Current Assets			
Cash and cash equivalents	128,975	125,631	3,060
Trade and other receivables — net	84,472	122,599	2,987
Inventories	65,720	80,222	1,954
Current portion of biological assets — net	4,124	3,792	92
Prepaid expenses and other current assets	22,620	31,612	770
	305,911	363,856	8,863
Assets held for sale	2,268	9,373	228
Total current assets	308,179	373,229	9,091
Noncurrent Assets			
Investments and advances — net	166,854	161,625	3,937
Available-for-sale financial assets	2,068	1,570	38
Property, plant and equipment — net	319,626	370,689	9,030
Investment properties — net	2,850	3,780	92
Biological assets — net of current portion	1,812	1,932	47
Goodwill — net	30,990	49,953	1,217
Other intangible assets — net	11,407	34,131	831
Deferred tax assets	8,233	8,826	215
Other noncurrent assets — net	38,517	32,228	785
Total noncurrent assets	582,357	664,734	16,192
Total assets	890,536	1,037,963	25,283
Liabilities and Equity			
Current Liabilities			
Drafts and loans payable	82,588	151,274	3,685
Accounts payable and accrued expenses	61,629	84,665	2,062
Finance lease liabilities — current portion	15,388	15,456	377
Income and other taxes payable	9,041	11,124	271
Dividends payable	2,153	3,247	79
Current maturities of long-term debt — net of debt issue costs	19,453	3,279	80
Liabilities directly associated with assets held for sale	578	—	—
Total current liabilities	190,830	269,045	6,554
Noncurrent Liabilities			
Long-term debt — net of current maturities and debt issue costs	191,967	220,938	5,382
Deferred tax liabilities	11,257	12,084	294
Finance lease liabilities — net of current portion	192,873	179,698	4,378
Other noncurrent liabilities	4,509	6,418	156
Total noncurrent liabilities	400,606	419,138	10,210
Equity			
Equity Attributable to Equity Holders of SMC			
Capital stock — common	16,397	16,408	400
Capital stock — preferred	4,852	10,187	248
Additional paid-in-capital	103,511	177,762	4,330
Revaluation increment	1,443	1,352	33
Cumulative translation adjustments	5,264	5,088	122
Retained earnings:			
Appropriated	24,315	27,219	663
Unappropriated	141,126	154,303	3,759
Treasury Stock	(67,441)	(140,124)	(3,413)
Amounts recognized directly in equity relating to assets held for sale	(53)	—	—
Total Equity Attributable to Equity Holders of SMC	229,414	252,195	6,142
Non-controlling interests	69,686	97,585	2,377
Total equity	299,100	349,780	8,519
Total liabilities and equity	890,536	1,037,963	25,283

	Years ended December 31,			
	2010	2011	2012	2012
	(P in millions)			(US\$ in millions) (unaudited)
Summary Consolidated Statement of Cash Flows Data				
Net cash flows provided by operating activities	45,378	28,660	16,815	410
Net cash flows provided by (used in) investing activities	(126,995)	(66,941)	(58,030)	(1,414)
Net cash flows provided by (used in) financing activities	(2,226)	42,335	38,572	940
Effect of exchange rates changes on cash and cash equivalents	(380)	(181)	(701)	(17)
Net increase/(decrease) in cash and cash equivalents	(84,223)	3,873	(3,344)	(81)
Cash and cash equivalents at beginning of year	209,411	125,188	128,975	3,141
Cash and cash equivalents associated to assets held for sale	—	(86)	—	—
Cash and cash equivalents at end of period	125,188	128,975	125,631	3,060

OTHER FINANCIAL DATA

Calculation of EBITDA⁽¹⁾

	As of and for the years ended December 31,			
	2010	2011	2012	2012
	(P in millions)			(US\$ in millions) (unaudited)
Net income	24,056	28,504	38,620	941
Add (deduct)				
Income tax expense	11,438	8,483	8,812	215
Net financing charges				—
Interest Expense	16,578	27,443	29,826	727
Interest Income	(3,023)	(4,618)	(4,254)	(104)
Gain on sale of Investments	—	(278)	(3,854)	(94)
Other charges (income)	(4,490)	—	—	—
Foreign exchange losses (gains)	(6,097)	823	(11,375)	(277)
Marked-to-market currency losses (gains)	(122)	(689)	1,313	32
Depreciation and amortization and impairment	<u>14,196</u>	<u>17,482</u>	<u>18,983</u>	<u>462</u>
EBITDA	52,536	77,150	78,071	1,902

(1) EBITDA is a measure used by the management of SMC to internally evaluate the performance of its businesses. EBITDA is calculated as net income before: income tax expense, net financing charges (interest income net of interest expense), extraordinary or exceptional items, foreign exchange losses (gains), marked-to-market currency losses (gains) and depreciation and amortization and impairment losses. EBITDA is not a measure determined in accordance with PFRS, and prospective investors should not consider EBITDA as an alternative to net income as a measure of operating performance or to cash flow as a measure of free cash flow for management's discretionary use, as it does not reflect certain cash requirements such as interest payments, tax payments and capital expenditures. The calculation of EBITDA of SMC may be different from the calculations used by other companies, and, as a result, the EBITDA of SMC may not be comparable to other similarly titled measures of other companies.

Calculation of Consolidated Total Indebtedness

	Years ended December 31,	
	2011	2012
	(P in millions)	
Drafts and loans payable	82,588	151,274
Current maturities of long-term debt	19,453	3,279
Long-term debt	<u>191,967</u>	<u>220,938</u>
	<u>294,008</u>	<u>375,491</u>

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with the section entitled "Selected Financial Information and Other Data" and SMC's consolidated financial statements, including the notes thereto, included elsewhere in this Offering Memorandum.

RESULTS OF OPERATIONS

2012 Compared to 2011

SMC

SMC's consolidated sales increased by 30.4% in 2012 to ₱698.9 billion, compared to ₱535.8 billion in 2011. This was on the back of solid contributions from the major businesses of SMC, of which 70% was derived from the new businesses whose sales grew by 46% over 2011 levels. The core businesses, on the other hand, posted a healthy 4% year on year increase.

SMC's operating income in 2012 was ₱52.8 billion, compared to ₱56.0 billion in 2011, primarily due to the volatility in crude oil prices which affected Petron, and higher raw material costs for the food business operated by San Miguel Pure Foods.

Consolidated net income before minority interest increased by 35.5%, to ₱38.6 billion in 2012, from ₱28.5 billion in 2011. The increase was primarily a result of higher gains from the other investments of SMC, coupled with favorable foreign exchange rates. Net income attributable to equity holders of the parent company increased by 57.4% to ₱27.6 billion.

Beverage Business

SMB's beverage business delivered strong growth in 2012, primarily due to favorable selling prices and increased sales volumes. Total sales grew by 5.1% to ₱75.6 billion and consolidated volumes increased by 0.4% to 224.8 million cases in 2012, compared to total sales of ₱71.9 billion and consolidated volumes of 223.8 million cases in 2011. SMB had operating income of ₱22.4 billion in 2012, compared to ₱20.5 billion in 2011. Net income was ₱14.4 billion in 2012, compared to ₱12.0 billion in 2011.

Beer—Domestic

SMB's domestic operations recorded sales of ₱61.2 billion in 2012, an increase of 5.0% compared to ₱58.3 billion in 2011. The increase was primarily due to higher selling prices and a moderate increase in volumes, reaching 186.3 million cases in 2012, an increase of 0.7% compared to 185.0 million cases in 2011. As a result, operating income increased by 7.8% to ₱21.9 billion in 2012, from ₱20.3 billion in 2011, supported by improvements in operational efficiencies and strong marketing programs.

Beer—International

Sales of international beer operations increased by 5.7% to ₱14.4 billion in 2012, from ₱13.6 billion in 2011. The increase was primarily due to sales growth in Indonesia, Thailand, Hong Kong and the export business. Sales volumes of 38.5 million cases was slightly lower by 0.8% from 38.8 million cases in 2011. As a result, operating income increased by 173.1% to ₱489 million in 2012, from ₱179.2 million in 2011, helped by higher selling price and cost management efforts.

Export sales increased by 11.4% in 2012 compared to 2011, mainly due to strong sales volumes boosted by higher sales to South Korea, Malaysia, Maldives, Japan, Qatar and stable sales volumes to Taiwan and the United States. New markets were tapped in 2012, such as Angola, Australia, Bahrain, Canada and South Africa.

Ginebra

The year 2012 continued to be a challenging year for Ginebra due to on-going competitive pressures. In spite of the competitive environment, Flagship Ginebra San Miguel increased its sales volume by 19% against the previous year — a result of the company's deliberate strategy to play on its core strengths through its *Lahing Ginebra*, *Ikaw Na* and *Ginumanfest* campaigns. These initiatives brought domestic volumes almost within those of 2011, ending at 23.8 million cases.

Operating loss was trimmed down to ₱566 million in 2012, from almost ₱891 million in 2011, boosted higher contribution margins from lower alcohol cost.

Food Business

San Miguel Pure Foods' consolidated sales increased by 6.9% to ₱95.8 billion in 2012, from ₱89.6 billion in 2011. San Miguel Pure Foods' sales growth was attributed to increased sales volumes across all major segments, driven by higher demand, the launch of around 50 new products, and the continued expansion of its distribution network.

Operating income was ₱5.3 billion in 2012, from ₱6.1 billion in 2011, lower by 14.4%, mainly due to raw material cost challenges experienced by its agro-industrial business experienced in 2012. Net income increased by 3.0% to ₱4.2 billion in 2012, from ₱4.1 billion in 2011. The increase in net income in 2012 compared to 2011 was primarily a result of strong results from the value-added meats cluster and income from investments. Operating profitability improved in 2012 through increased use of cheaper raw materials substitutes and by channeling food products to more stable-priced segments.

Packaging Business

The consolidated sales of SMC's packaging business reached ₱24.5 billion in 2012, a 1.4% increase from the 2011 sales of ₱24.1 billion. This is a result of successful penetration programs in both the domestic and international markets. As a result, operating income for the packaging business grew by 6.4% to ₱2.3 billion in 2012, compared to ₱2.2 billion in 2011.

Fuel and Oil

Petron's sales grew by 55.0% to ₱424.8 billion in 2012, from ₱274.0 billion in 2011, primarily as a result of consolidation of its Malaysian operations, as well as increased sales from domestic operations due to increased volumes and favorable selling prices. Sales volumes increased to 74.3 million barrels in 2012. Philippine operations sold 47.7 million barrels in 2012, and domestic sales increased by approximately 8% in 2012 compared to 2011. The Philippine operations registered a 3% sales growth compared to 2011, given higher volumes and prices. Operating income decreased by 38.5% to ₱9.4 billion in 2012, from ₱15.3 billion in 2011, as a result of price volatility in crude oil and petroleum products. Both Philippine and Malaysian operations posted losses in the second quarter of 2012 when Dubai crude oil fell from a high of US\$124 per barrel to US\$89 per barrel. As a result, Petron's net income decreased by 73.2% to ₱2.3 billion in 2012, from ₱8.5 billion in 2011.

Energy Business

SMC operates its energy business through its wholly owned subsidiary, SMC Global Power, together with its subsidiaries. Sales increased by 4.5% to ₱74.7 billion in 2012, from ₱71.4 billion in 2011. Total power generated increased by 5.3% to 15.3 million MWh in 2012, from 14.5 million MWh in 2011. Capacity utilization was 71% in 2012 compared to 67% in 2011 due to higher bilateral requirements despite various forced outages. Operating income increased by 2.4% to ₱17.1 billion in 2012, from ₱16.7 billion in 2011.

2011 Compared to 2010

SMC

SMC's consolidated sales in 2011 increased by 117.7% to ₱535.8 billion from ₱246.2 billion in 2010. During 2011, the growth of SMC Group's core businesses was aided by sales growth for our newer businesses, specifically energy and fuel and oil. Correspondingly, SMC's operating income in 2011 increased by 61.7% to ₱56.0 billion, from ₱34.6 billion in 2010. Consolidated net income before minority interest increased by 18.5% to ₱28.5 billion in 2011, from ₱24.1 billion in 2010.

Beverage Business

SMB's beverage business delivered strong growth in 2012, primarily due to favorable selling prices and increased sales volumes. Total sales increased by 6.4% to ₱71.9 billion and consolidated volumes reached 223.8 million cases in 2011, compared to total sales of ₱67.6 billion and consolidated volumes of 220.7 million cases in 2010.

SMB had operating income of ₱20.5 billion in 2011, compared to ₱18.6 billion in 2010, or an increase of 10.4%. Net income was ₱12.0 billion in 2011, compared to ₱11.8 billion in 2010, or an increase of 1.7%.

Beer—Domestic

SMB's domestic operations recorded sales of ₱58.3 billion in 2011, an increase of 5.2% compared to ₱55.4 billion 2010. The increase was primarily due to price increase and higher volumes reaching 185.0 million cases

in 2011, an increase of 0.7% compared to 183.6 million cases in 2010. As a result, operating income grew by 8% to ₱20.3 billion in 2011, from ₱18.8 billion in 2010.

Beer—International

Sales of international beer operations increased by 11.8% to ₱13.6 billion in 2011 compared to ₱12.2 billion in 2010, primarily due to sales growth in North China, Hong Kong, Indonesia and exports. Total sales volume was 38.8 million cases in 2011, compared to 37.1 million cases in 2010, or an increase of 4.6%. As a result, operating income increased by 173.9% to ₱179.2 million in 2011, from ₱243 million operating loss in 2010. Export sales grew by 25.8% in 2011 compared to 2010, mainly due to strong sales volume.

Ginebra

Amid competitive pressure and a shift in consumer preferences, sales decreased by 33.4% to ₱15.1 billion in 2011, from ₱22.7 billion in 2010. Ginebra ended with an operating loss of ₱890.7 million in 2011, from ₱1.5 billion operating income in 2010 as a result of relatively lower volumes and higher fixed costs.

Food Business

Consolidated sales of San Miguel Pure Foods increased by 11.4% to ₱89.6 billion in 2011, from ₱80.4 billion in 2010. San Miguel Pure Foods, sales growth was a result of strong sales volume and better average selling prices across most segment units.

Despite increased raw material costs during 2011, San Miguel Pure Foods consolidated operating income increased by 4.0% to ₱6.1 billion in 2011, from ₱5.9 billion in 2010. Net income increased by 7.6% to ₱4.1 billion in 2011, from ₱3.8 billion in 2010. The increase in net income in 2011 compared to 2010 was primarily a result of rationalization of low-margin products and cost reduction programs.

Packaging Business

Consolidated sales of SMC's packaging business increased by 2.9% to ₱24.1 billion in 2011, from ₱23.4 billion in 2010. Sales growth was primarily a result of improving customer penetration in domestic and international markets, with international sales accounting for an increasing proportion of total sales. Operating income for the packaging business increased by 7.9% to ₱2.2 billion in 2011 from ₱2.0 billion in 2010, in spite of higher fuel and raw material costs and competitive pricing in overseas markets.

Fuel and Oil

Petron's sales increased by 19.6% to ₱274.0 billion in 2011, from ₱229.1 billion in 2010, despite weak demand due to higher fuel prices and aggressive competition. Operating income increased by 18.6% to ₱14.8 billion in 2011, compared to ₱12.5 billion in 2010, as a result of a better product mix that included sales from high-margin petrochemical feedstocks such as propylene, benzene, toluene and mixed xylene. As a result, Petron's net income increased by 7.1% to ₱8.5 billion in 2011, from ₱7.9 billion in 2010.

Energy Business

SMC operates its energy business through its wholly owned subsidiary, SMC Global Power, together with its subsidiaries. Sales increased by 8.0% to ₱71.4 billion in 2011, from ₱66.1 billion in 2010. Total power generated increased by 30.7% to 14.5 million MWh in 2011, from 11.1 million MWh in 2010, primarily as a result of the full operation of Ilijan and San Roque power plants and overall improvement in net capacity factor. As a result, operating income increased by 3.3% to ₱16.7 billion in 2011, from ₱16.2 billion in 2010.

LIQUIDITY AND CAPITAL RESOURCES

As of December 31, 2012, SMC had cash and cash equivalents of ₱125.6 billion. As of the same date, SMC had total outstanding short-term borrowings of ₱151.3 billion in the form of bank loans and short-term commercial paper facilities.

As of December 31, 2012, SMC had total outstanding long-term borrowings of ₱224.2 billion. SMC obtained these borrowings from various financial institutions and investors, both in the Philippines and abroad. The debt agreements contain, among other provisions, covenants relating to merger and consolidation, maintenance of certain financial ratios, working capital requirements, restrictions on loans and guarantees, disposal of a substantial portion of assets, significant changes in the ownership or control of subsidiaries, payments of dividends and redemption of capital stock. See note 23 to SMC's consolidated financial statements included elsewhere in this Offering Memorandum for more detailed information. As of the date of this Offering Memorandum, SMC is in discussions regarding refinancing of its US\$1 billion loan facility which was entered into in 2010.

BUSINESS

Overview

SMC is one of the most diversified and also one of the largest conglomerates by market capitalization and total assets, with sales equaling approximately 6.6% of the Philippine GDP in 2012. Originally founded in 1890 as a single brewery in the Philippines, SMC has transformed itself from a market-leading beverage, food and packaging business with a globally recognized beer brand, into a large and diversified conglomerate with additional market-leading businesses and investments in the fuel and oil, energy, infrastructure, telecommunications, mining and airline industries in the Philippines. SMC has a portfolio of companies that is interwoven into the economic fabric of the Philippines, benefiting from, as well as contributing to, the development and economic progress of the Philippines. The common shares of SMC were listed on the PSE on November 5, 1948, and as of December 31, 2012, SMC had a market capitalization of ₱250.1 billion. The consolidated sales, gross profit and EBITDA of SMC in 2012 were ₱698,868 million, ₱104,136 million and ₱78,071 million, respectively.

Corporate Transformation of SMC

Established in 1890 as a single brewery in the Philippines, the SMC Group has become a Philippine market leader in its established businesses in beverage, food and packaging industries with over 18,000 employees and more than 100 production facilities in the Asia-Pacific region as of December 31, 2012. The extensive portfolio of SMC products includes beer, liquor, non-alcoholic beverages, poultry, animal feeds, flour, meat, dairy products, coffee and various packaging products.

In 2007, in light of the opportunities presented by the global financial crisis, the ongoing program of asset and industry privatization of the Philippine government and the strong cash position of SMC enhanced by recent divestments and the strong cash flow generated by its established businesses, SMC adopted an aggressive business diversification program. The program channeled the resources of SMC into what it believes were attractive growth sectors, aligned with the development and growth of the Philippine economy. SMC believes this strategy will achieve a more diverse mix of sales and operating income, better position SMC to access capital, present different growth opportunities and mitigate the impact of downturns and business cycles.

Since January 1, 2008, SMC, either directly or through its subsidiaries, has made a series of acquisitions in the fuel and oil, energy, infrastructure, mining, telecommunications, banking and airline industries in the past four years, as outlined below:

Fuel and Oil: On December 15, 2010, SMC completed the exercise of its option to acquire equity in Sea Refinery Corporation, which, in turn, has equity interests in Petron. As of December 31, 2012, SMC owned approximately 68.3% of the outstanding and issued shares of Petron. On March 30, 2012, an affiliate of SMC, Petron Oil & Gas International Sdn Bhd, completed the acquisition of 65% of Esso Malaysia Berhad, a publicly listed company in Malaysia, 100% of ExxonMobil Malaysia Sdn Bhd, and 100% of ExxonMobil Borneo Sdn Bhd. Subsequently, these three companies were renamed Petron Malaysia Refining & Marketing Bhd, Petron Fuel International Sdn Bhd and Petron Oil (M) Sdn Bhd, respectively. As of December 31, 2012, Petron owned 73.37% of Petron Malaysia Refining and Marketing Bhd.

Energy: SMC acquired a 27.0% interest in power distributor Meralco through SMC Global Power on October 27, 2008. This interest stood at 32.04% as of December 31, 2012. In addition, SMC has administration rights for three power plants in Sual, Ilijan and San Roque under IPPA agreements which commenced on November 6, 2009, June 26, 2010 and January 26, 2010, respectively, and which will expire on October 24, 2024, June 4, 2022 and May 26, 2028, respectively.

Infrastructure: SMC acquired a 35.0% interest in PIDC, which is developing the 88.6-kilometer Tarlac-Pangasinan-La Union expressway, on September 11, 2009. SMC also acquired a 93.0% interest in TADHC (formerly known as Caticlan International Airport Development Corporation) on April 29, 2010, and a 51.0% interest in Universal LRT, the concession holder for the MRT-7 rail and road project, on November 8, 2010. In October 2011, SMHC acquired a 46.5% stake in AAI, a company which has an 80.0% stake in SLTC, which holds a 30-year concession (valid until 2035) to operate the 36.0 km SLEX, one of the three major expressways that link Metro Manila to key southern provinces; and acquired a 50.51% stake in CMMTC. On the December 28, 2012, SMC through its wholly owned subsidiary, SMHC, completed the acquisition of 100% of THI, thus obtaining control and consolidating CMMTC. SMC, through Petron, has a 35.0% interest in Manila North Harbor Port Inc., which Petron purchased from Harbour Centre Port Terminal, Inc. in January 2011.

Mining: SMC acquired a 100.0% interest in the concession holders of DAMI and BERI on January 29, 2010 and Sultan on May 13, 2010. SMC also has a 3.99% interest in Indophil, which indirectly holds a 15.0% interest in an

entity with rights to explore, develop, and operate the Tampakan gold and copper project, which was acquired on October 15, 2010.

Telecommunications: On July 8, 2009, SMC, through Vega, acquired a 32.7% equity interest in Liberty, which was increased to 41.5% in 2010, in partnership with G.S.P.C. Qtel Westbay Holding (26.75%), Wi-Tribe Asia Limited (5.90%) and White Dawn Solutions Holdings, Inc. (18.36%), with the remaining shares owned by the public. In 2010, SMC acquired 100.0% of BellTel, a full-service telecommunications company which is licensed to provide a range of services throughout the Philippines. In 2010, SMC, through Vega, acquired 100% of the outstanding and issued shares of stock of AGNP, the beneficial owner of approximately 40.0% of Eastern ETPI. On October 20, 2011, SMC through its wholly owned subsidiary, SMESI, acquired an additional 37.7% of the outstanding and issued shares of stock of ETPI, bringing its total indirect equity interests in ETPI to 77.7% as of December 31, 2012.

Banking: SMC, through SMPI, made a series of acquisitions of BOC shares in 2007 and 2008. However, SMPI, together with the other stockholders of BOC, executed a share purchase agreement dated May 8, 2012 with CIMB Bank Berhad for the sale of a 58% equity interest in BOC. As of December 31, 2012, the share purchase was still pending completion.

Airlines: On April 3, 2012, SMC, through SMEII, acquired a 49.0% equity interest in each of Trustmark Holdings Corporation and Zuma Holdings and Management Corporation, the holding companies of PAL (through PAL Holdings, Inc.) and Air Phil, respectively.

Businesses of SMC

Today, SMC is one of the largest and most diverse business groups in the Philippines. The portfolio of SMC encompasses the following businesses, most of which are market leaders in their respective industries:

Beverage

The beverage business consists of brewing, distilling, selling, marketing and distributing beer, liquor and non-alcoholic beverages. SMC conducts its beverage business through majority owned subsidiaries: San Miguel Brewery Inc. SMB for beer and Ginebra for liquor and non-alcoholic beverages. San Miguel sells the dominant beer brands in the Philippines, with a total market share of more than 90% according to Canadean data. Its products include *San Miguel Pale Pilsen*, which is the flagship beer of SMB and is sold throughout the world, *San Miguel Super Dry*, *San Mig Light*, *San Mig Strong Ice* and *San Miguel Premium All-Malt*. Other SMC beers include *Cerveza Negra*, *Red Horse*, *Gold Eagle*, *Oktoberfest Brew*, *San Miguel Flavored Beer* and the recently introduced *San Mig Zero*. In addition to its Philippine beer operations, SMB has brewery and sales operations in China, Hong Kong, Thailand, Vietnam and Indonesia, and exports to over 40 countries. SMC produces some of the most recognizable brands in the Philippine liquor market, including *Ginebra San Miguel*, *GSM Blue*, *Gran Matador Brandy*, *Gran Matador Light*, *Antonov Vodka* and *Vino Kulafu*, in addition to having a distillery in Thailand. SMC also has a growing non-alcoholic beverage business which produces non-carbonated, ready-to-drink tea and fruit juice products, primarily under the *Magnolia* brand.

Food

The food business holds numerous market leading positions in the Philippine food industry, offering a broad range of high-quality food products and services to both household and food service customers. The food business is conducted through San Miguel Pure Foods. The business is organized into business clusters: Agro-Industrial (poultry, feeds and fresh meats); Value-Added Meats (processed meats); Milling (flour and flour products); and DSO, ice cream, coffee, food service, retail and miscellaneous businesses. SMC has some of the best known brands in the Philippine food industry, such as *Purefoods*, *Magnolia*, *Monterey*, *Star*, *Dari Crème* and *B-Meg*. In addition to its Philippine operations, the food business has operations in Indonesia and Vietnam.

Packaging

The packaging business has one of the largest packaging operations in the Philippines, producing glass, metal, plastic, aluminum cans, paper, flexibles, PET and other packaging products. The packaging business is conducted through the Packaging Group, which comprises SMYPC, SMYPIL, SMYAC and Mincorr. The packaging business is the major source for packaging products for the other businesses of SMC. It also supplies its products to major multinational corporations in the Philippines and customers across the Asia-Pacific region, the United States, Africa, Australia and the Middle East.

Properties

SMPI was established in 1990 initially as the corporate real estate arm of SMC. It is the primary property subsidiary of SMC, currently 98.5%-owned by SMC. SMPI is presently engaged in commercial property development, sale and lease of real properties, management of strategic real estate ventures and corporate real estate services.

Fuel and Oil

SMC operates its fuel and oil business through Petron, in which SMC holds a 68.3% interest. Petron refines crude oil and markets and distributes refined petroleum products in the Philippines and Malaysia. In the Philippines, Petron is the largest integrated oil refining and marketing company, with an overall market share of 38.5% of the Philippine oil market in terms of sales volume based on industry data from the DOE as of December 31, 2012. Petron had a 16.6% share of the Malaysian retail market as of December 31, 2012, according to Metrix Research estimates, the market research consultant appointed by Malaysian retail market participants to compile industry data.

Energy

The energy business of SMC is one of the leaders in the Philippine power generation industry in terms of installed capacity. The energy business of SMC is conducted through SMC Global Power. SMC administers three power plants, located in Sual, Pangasinan (coal-fired), Ilijan, Batangas (natural gas) and San Roque, Pangasinan (hydroelectric), with a combined capacity of 2,545 MW, pursuant to IPPA agreements with PSALM and NPC. As of December 31, 2012, SMC was one of the largest IPPAs in the Philippines and held a 22% market share of the total installed power generation capacity for the Luzon power grid and a 17% market share of the national grid according to the ERC. As of December 31, 2012, SMC also owned a 32.04% stake in Meralco, the biggest power distributor and private sector utility in the Philippines, which accounted for more than half of all electricity sales in the Philippines in 2012. SMC also has interests and investments in coal, copper and gold mining.

Infrastructure

The infrastructure business of SMC consists of investments in companies which hold long-term concessions in the Philippines' infrastructure sector. Current projects include TPLEX Tollway, Boracay Airport and MRT-7 Light Rail and Road Project.

SMC, through SMHC, has a 46.5% investment in AAI. AAI has indirect equity interests in CMMTC and SLTC, which hold the concessions to construct, operate and maintain the Skyway and SLEX, respectively.

SMC operates with partners in its investments in most of these infrastructure concessions.

The following table sets forth the contribution of each of the businesses of SMC to its sales for the periods indicated:

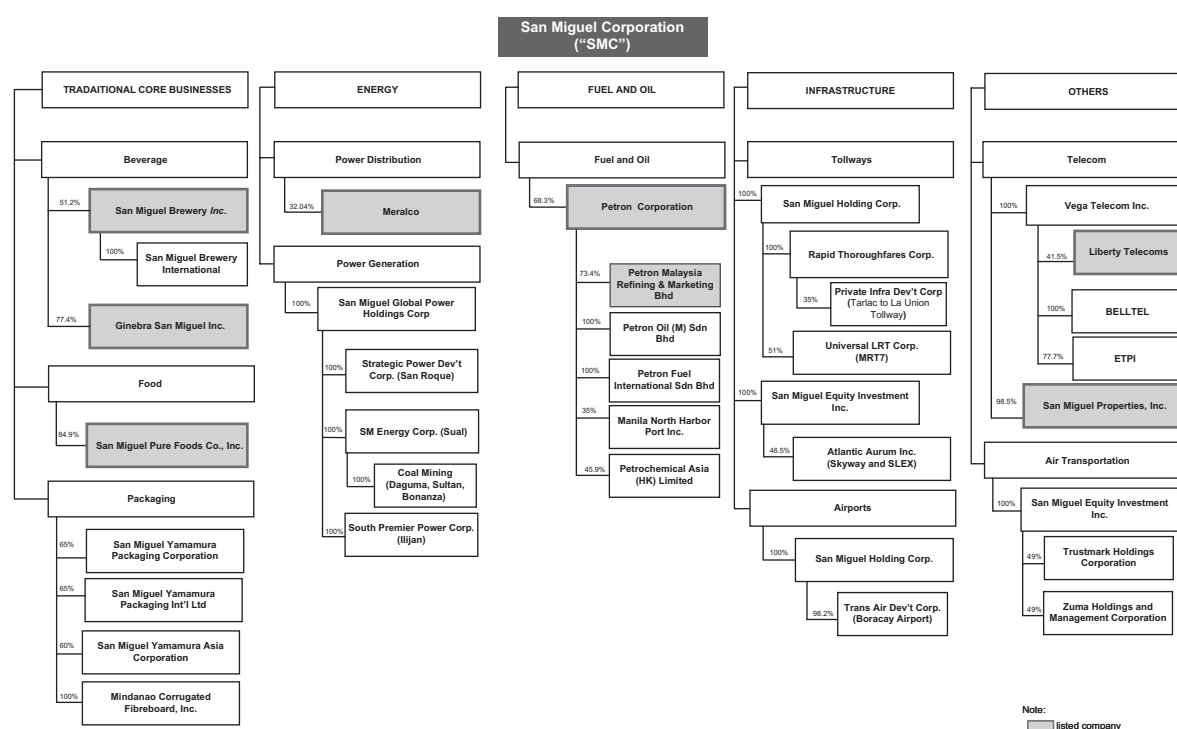
	2010		2011		2012	
	Sales	%	Sales	%	Sales	%
	(P in millions, except percentages)					
Beverage	90,407	36.73	87,076	16.25	90,005	12.88
Food	80,415	32.67	89,549	16.71	95,759	13.70
Packaging	19,268	7.83	18,943	3.54	17,566	2.51
Energy	45,636	18.54	70,737	13.20	73,910	10.58
Fuel and Oil	10,383	4.22	269,116	50.23	420,269	60.14
Infrastructure	9	—	116	0.02	134	0.02
Telecom	38	0.02	238	0.04	1,225	0.18
Consolidated	246,156	100.00	535,775	100.00	698,868	100.00

The foreign operations of SMC in 2012 contributed about 24.1% of consolidated sales. National sales are broken down by market as follows:

Market	% to Consolidated Sales		
	2010	2011	2012
Philippines	90.0	95.0	75.9
Malaysia	1.2	0.6	20.8
Indonesia	2.4	1.3	1.0
China	2.5	1.3	1.0
Vietnam	1.5	0.8	0.5
Others	2.5	1.1	0.8
	<u>100.00</u>	<u>100.00</u>	<u>100.00</u>

Corporate Organization

Set forth below is SMC's corporate organizational chart as of the date of this Offering Memorandum.



Strengths of SMC

SMC believes that its principal strengths include the following:

Diversified platform with broad exposure to the Philippine economy. The Philippines is the fifth largest economy in Southeast Asia (in terms of GDP in 2012) with consecutive annual positive GDP growth since 1999. The Philippines announced GDP growth of 6.6% in 2012, despite challenging global market conditions. According to IMF estimates, the Philippine economy is expected to grow at 4.8% in 2013. In addition, the Philippine population is young, comparably literate and growing, which provides the Philippine economy with favorable demographics for further growth.

As one of the Philippines' largest (by market capitalization and total assets) conglomerates, with sales equaling approximately 6.6% of the Philippine GDP and 5.2% of the Philippine GNP in 2012, the SMC Group is broadly exposed to the Philippine economy through its diverse range of businesses spanning the beverage, food, packaging, fuel and oil, energy, telecommunication, infrastructure, property, mining, and airline industries. Recent acquisitions of SMC in the infrastructure, fuel and oil, and airline industries align SMC to key sectors that it believes will benefit from the forecast growth of the Philippine economy.

Market leading positions in key Philippine industries. Many of the businesses of SMC are leaders in their domestic markets.

Beverages: The domestic beer business of SMC has consistently dominated the Philippine beer market, with a market share of over 90% by volume in 2011, according to Canadian data. SMC also produces some of

the most recognizable brands in the Philippine liquor market. It also has a growing non-alcoholic beverage business which produces non-carbonated ready to drink tea, fruit juices and water.

Food: San Miguel Pure Foods is a leading Philippine food company with market-leading positions in many key products and offers a broad range of high-quality food products and services to household, institutional and food service customers. San Miguel Pure Foods has some of the most recognizable brands in the Philippine food industry, including *Magnolia* for chicken, ice cream and milk products, *Monterey* for fresh and marinated meats, *Purefoods* for refrigerated processed meats and canned meats, *Star* and *Dari Crème* for margarine, *San Mig Coffee* for coffee and *B-Meg* for animal feeds.

Packaging: The packaging business of SMC is one of the largest packaging operations in the Philippines, producing glass, metal, plastic, aluminum cans, paper, flexibles, PET and other packaging products. The packaging business of SMC is the major source for packaging products for the other businesses of SMC. It also supplies its products to major multinational corporations in the Philippines and customers across the Asia-Pacific region, the United States, Africa, Australia and the Middle East.

Fuel and oil: Petron refines crude oil and markets and distributes refined petroleum products in the Philippines and Malaysia. In the Philippines, Petron is the largest integrated oil refining and marketing company, with an overall market share of 38.5% of the Philippine oil market in terms of sales volume based on industry data from the DOE as of December 31, 2012. Petron had a 16.6% share of the Malaysian retail market as of December 31, 2012, according to Metrix Research estimates, the market research consultant appointed by Malaysian retail market participants to compile industry data.

Energy: SMC is one of the largest IPPAs in the Philippines, holding a 22% market share of the total installed capacity of the Luzon power grid and a 17% market share of the national grid as of December 31, 2012 according to the ERC. SMC administers three power plants, located in Sual, Pangasinan (coal-fired), Ilijan, Batangas (natural gas) and San Roque, Pangasinan (hydroelectric), with a combined capacity of 2,545 MW. SMC and its subsidiaries also hold a 32.04% stake in Meralco, the biggest power distributor and private sector utility in the Philippines, accounting for more than half of all net electricity sales in the Philippines. The energy trading team of SMC comprises pioneers in WESM trading.

Experienced management team. SMC has an extensive pool of experienced managers, and many senior managers have been with SMC for more than 20 years. The management team has a deep knowledge and understanding of the Philippine operating environment and has been able to effectively manage SMC through periods of crisis and instability in the Philippines. In addition, the management team has recently successfully directed the diversification strategy of SMC, including retaining key management personnel from acquired companies in order to maintain their expertise and leverage their industry experience. The two new businesses of SMC — Petron and SMC Global Power — have provided significant contribution to the performance of SMC for the past two years. In 2012, sales of Petron and SMC Global Power accounted for 60% and 11% of the total consolidated sales of SMC, respectively. Likewise, in 2012 the EBITDA contribution of Petron and SMC Global Power accounted for 19% and 32%, respectively.

Operating businesses provide sustainable stream of income and cash flows. The beverage, food and packaging businesses provide SMC with a sustainable stream of income with low capital expenditure requirements. These businesses demonstrated resilience during the global financial crisis and provided SMC with a strong financial base from which to pursue its recent diversification strategy. In 2012, the beverage, food and packaging businesses provided 33%, 11% and 5% of total SMC EBITDA, respectively, and 13%, 13% and 3% of total SMC sales, respectively.

In 2010, SMC generated ₱52,536 million of EBITDA and ₱20,091 million of net income attributable to the parent company with ₱8,518 million of capital expenditure. In 2011, it generated ₱77,150 million of EBITDA and ₱17,518 million of net income attributable to the parent company with ₱26,426 million of capital expenditure. In 2012, it generated ₱78,071 million of EBITDA and ₱27,579 million of net income attributable to the parent company with ₱52,920 million of capital expenditure.

Platform for significant future growth. SMC is well-positioned for significant future growth. In particular, the established businesses of SMC in beverage, food and packaging provide for stable growth annually, while its new businesses are expected to contribute further to this growth.

Beverage: The beverage business of SMC is well-positioned to benefit from increasing affluence and population growth in the Philippines. SMC believes there are significant opportunities in the premium beer market as the Philippine population becomes more affluent. Additionally, the international beer business of SMC is experiencing increased sales through increasing brand recognition in selected overseas markets such as Indonesia, Thailand, Singapore and Hong Kong. SMC intends to expand its liquor business in the

southern Philippines and internationally. SMC plans to create rapid deployment task forces, particularly in the southern Philippines, where market penetration is low and where there is no existing dealership system. SMC also plans to increase margins by improving the profitability of its non-alcoholic beverage business by rationalizing its sales and distribution network to reduce costs, searching for alternative raw materials and optimizing bottle cost and usage. The beverage business of SMC plans to introduce new products and new package formats to increase consumer interest and overall market size, as well as address the needs of an increasingly fragmenting market, especially in high growth segments.

Food: SMC aims to become the lowest cost producer by securing a stable raw material supply and developing cheaper alternative raw materials. SMC is also streamlining its operations to improve the profitability of its established business segments such as poultry, feeds, meat and flour, maximize synergies across operations, and improve margins through outsourcing non-core activities.

Packaging: The packaging business of SMC aims to benefit from trade liberalization and globalization in the Asian region by increasing its exports to new markets. In addition, rising environmental awareness provides opportunities for the production of more environmentally friendly products such as heavy metal-free paint glass and recycled PET resin. SMC plans to improve margins by developing alternative sources of raw materials and optimizing recycling efforts to lower its material costs.

Fuel and oil: Petron operates as an integrated oil refining and marketing company in the Philippines and Malaysia, both of which it believes have favorable oil industry dynamics. The Philippines operates under a free market scheme with movements in regional prices reflected in the pump prices on a weekly basis. Malaysia, on the other hand, operates under a regulated environment and implements an automatic pricing mechanism that provides stable returns to fuel retailers. As both the Philippines and Malaysia are importers of finished petroleum products, Petron believes it is well-positioned to benefit from this supply shortfall, giving it a significant competitive advantage against other competitors. SMC plans to continue its service station network expansion and seek growth in complementary non-fuel businesses. SMC also plans to increase the production of higher margin products. Petron is currently embarking on RMP-2, the second phase of a refinery expansion project, which includes further enhancements to the refinery's operational efficiencies, increase in conversion capability and reduction of production of lower-value fuel oils, which is expected to be completed in 2014. In addition to RMP-2 and the expansion of the service station network, Petron is constructing a new cogeneration power plant for the Limay Refinery to replace some of the Limay Refinery's existing turbo and steam generators. The new cogeneration power plant is expected to utilize more efficient technology and generate power at lower costs.

Energy: SMC is planning to expand its power generating capacity over the next five years, and believes its energy business will benefit from both growing demand for electricity in the Philippines, which is forecasted to exceed the growth rates of the Philippine GDP, and shortage in electricity supply, with the industry constrained by aging power generation assets and minimal new capacity. Also, if spot electricity rates move higher as a result of increased demand, the margins of SMC are expected to increase. SMC aims to protect its fuel supply and hedge its exposure to commodity price increases by acquiring coal and oil businesses.

Infrastructure: SMC believes there are significant opportunities in building or purchasing infrastructure assets in a growing economy that has historically under-invested in infrastructure. In addition, SMC believes its operating licenses will provide strong and stable long-term income streams, as well as serve as a barrier to entry to new entrants to the business.

Telecommunications: SMC believes its recent acquisitions in the telecommunications industry provide it with exposure to an industry that is expecting high growth as the Philippine population becomes more affluent and spends more on higher margin services. In particular, SMC is currently refining its telecommunications business strategy, where it plans to take advantage of opportunities in digitization of businesses, the emergence of mobile platforms for businesses and the provision of services to consumers. Moreover, companies recently acquired by SMC have a wide bandwidth of spectrum that would enable SMC to be competitive in both current (2G/3G/4G) and future technologies.

Potential to extract synergies across businesses. SMC believes there are significant opportunities to develop and increase synergies across many of its businesses, including:

Ancillary business opportunities: SMC believes it has opportunities within its existing businesses to secure new growth opportunities in its new businesses by using the relevant areas to conduct business and activities. Potential initiatives of this type include installing SMC Group advertisements and building service stations, retail outlets, rest stops and kiosks along toll roads.

Immediate distribution channel: The extensive retail distribution network of SMC provides an effective platform for roll-out of new products and services. For example, the network of Petron service stations provides an immediate distribution channel for retail sales for SMC beverage and food products.

Economies of scale: SMC believes the size and scale of its distribution network operations will provide significant economies of scale and synergies in production, research and development, distribution, management and marketing. The size and scale of SMC should also result in substantial leverage and bargaining power with suppliers and retailers.

Integration: SMC plans to continue pursuing vertical integration across the established and strategic businesses, such as supplying the fuel and oil and power requirements of its businesses internally.

Business Strategies of SMC

The principal strategies of SMC include the following:

Enhance value of established businesses. SMC aims to enhance the value of its established businesses by pursuing operational excellence, brand enhancement, improving product visibility, targeting regions where SMC has lower market share, implementing pricing strategies and pursuing efficiencies.

Continue to diversify into industries that underpin the development and growth of the Philippine economy. In addition to organic growth, SMC intends to continue to seek strategic acquisition opportunities to position itself for the economic growth and industrial development of the Philippines.

Identify and pursue synergies across businesses through vertical integration, platform matching and channel management. SMC intends to create an even broader distribution network for its products and expand its customer base by identifying synergies across its various businesses. In addition, SMC is pursuing plans to integrate its production and distribution facilities for its established and newly acquired businesses to enable additional cost savings and efficiencies.

Invest in and develop businesses with leading market positions. SMC intends to further enhance its market position in the Philippines by leveraging its financial resources and experience to continue introducing innovative products and services. Potential investments to develop existing businesses include constructing new power plants and expanding its power generation portfolio, building additional service and micro-filling stations and expanding food distribution networks. SMC believes its strong domestic market position and brand recognition provide an effective platform to develop markets for its expanding product portfolio. SMC plans to continue to invest in and develop businesses it believes have the potential to gain leading positions in their respective markets.

Adopt world-leading practices and joint development of businesses. SMC intends to develop strategic partnerships with global industry leaders, including, for example, Kirin in the beverages and NYG in the packaging businesses. These partnerships provide marketing and expansion opportunities, and they also potentially provide liquidity and opportunities for SMC to divest minority stakes in its businesses creating value for its shareholders.

Recent Developments

Issuance of Bonds by SMB

On April 2, 2012, SMB issued peso-denominated fixed rate bonds worth ₱20 billion. The bonds were issued at the issue price of 100.00% of face value in three series: Series D, E and F Bonds.

The Series E and F Bonds were listed on the Philippine Dealing & Exchange Corp. (“PDEX”) on April 2, 2012, and the Series D Bonds were listed on the PDEX effective October 3, 2012.

Proceeds of the offer were used by SMB to redeem the Series A fixed rate bonds amounting to ₱13.6 billion which matured on April 3, 2012 and the partial repayment of US\$150 million of the US\$300 million term facility on April 27, 2012.

Redemption of 693,500 Preferred Shares of Top Frontier Top Frontier

On June 18, 2012, Top Frontier redeemed a total of 693,500 preferred shares out of 2,598,040 preferred shares issued to SMC, at the total redemption price of ₱12,899 million, corresponding to the original issue price of such preferred shares.

The SMC Group recognized a gain of ₱945 million from the transaction.

Purchase of SMC Shares by Top Frontier and MYL

On June 29, 2012, Top Frontier and MYL purchased 125,234,667 common shares and 368,140,516 common shares of SMC, respectively. The sale was transacted at the PSE through a special block sale at the price of ₱75.00 per share.

As of December 31, 2012, Top Frontier and MYL own approximately 66.30% and 15.52%, respectively, of the outstanding common stock of SMC.

Issuance of Series “2” Preferred Shares

In September 2012, SMC issued 1,067,000,000 Series “2” Preferred Shares at the issue price of ₱75.00 per share and listed the ₱80,025 million worth of Series “2” Preferred Shares on the PSE.

These Series “2” Preferred Shares were issued in three sub-series (2-A, 2-B and 2-C) and are peso-denominated, perpetual, cumulative, non-participating and non-voting.

Dividend rates per annum for are 7.5%, 7.625% and 8% for sub-series 2-A, 2-B and 2-C, respectively.

The bulk of the proceeds from the Series “2” Preferred Shares issuance was used by SMC for the redemption of its outstanding Series “1” Preferred Shares with the balance utilized for general corporate purposes, including short-term debt repayment.

Redemption of the Series “1” Preferred Shares

On October 5, 2012, SMC redeemed the Series “1” Preferred Shares at a redemption price of ₱75.00 per share, in accordance with their terms and conditions. The redemption of these preferred shares was approved by the Board of Directors of SMC on August 13, 2012.

The redemption proceeds of the Series “1” Preferred Shares amounting to ₱72,788 million and all accumulated unpaid cash dividends amounting to ₱1,458 million were paid on October 5, 2012 to the stockholders of record as of September 11, 2012.

Secondary Offering of Common Shares of San Miguel Pure Foods

On November 23, 2012, SMC completed the secondary offering of its shares in San Miguel Pure Foods following the crossing of the shares on the PSE on November 21, 2012. The offer consisted of 25,000,000 common shares, inclusive of an over-allotment of 2,500,000 common shares at a price of ₱240.00 per share.

Net proceeds from the transaction amounted to ₱5,784 million. The SMC Group recognized a net gain of ₱2,419 million from the offering.

Investment in THI and CMMTC

On December 28, 2012, SMC, through its wholly-owned subsidiary, SMHC, completed the acquisition of 100% of the outstanding capital of THI for ₱3 million.

With the acquisition of THI, which owns 37.33% of the outstanding capital stock of CMMTC, and the existing 23.5% indirect ownership in CMMTC through AAI, SMHC obtained control and consolidated CMMTC effective December 28, 2012.

Construction of the GBGTC

As of December 31, 2012, GBGTC incurred ₱1,074 million for the construction of its grains terminal in Batangas. GBGTC is a wholly-owned subsidiary of SMMI, incorporated in September 2011.

Voluntary Delisting of SMPI and SMB Shares from the PSE and the Buy-back of all of their Publicly Listed Shares through a Tender Offer

On February 5, 2013 and February 15, 2013, the Board of Directors of SMPI and SMB approved and authorized the voluntary delisting of SMPI and SMB shares from the PSE and the buy-back of all their publicly listed shares through a tender offer at the price of ₱134.12 and ₱20.00 per share, respectively.

The tender offer periods for the SMPI and SMB share buy-backs were March 6, 2013 to April 5, 2013 and March 24, 2013 to April 3, 2013, respectively.

Tender Offer for US\$600 Million Exchangeable Bonds

On February 7, 2013, SMC repurchased exchangeable bonds having an aggregate principal amount of US\$259.2 million. The aggregate cash amount paid based on the aggregate principal amount of the exchangeable bonds repurchased, as well as accrued but unpaid interest payable until February 7, 2013, was US\$280.6 million.

On March 26, 2013, SMC repurchased the exchangeable bonds having an aggregate principal amount of US\$60 million. The aggregate cash amount paid based on the aggregate principal amount of the exchangeable bonds repurchased, as well as accrued but unpaid interest payable until March 26, 2013, was US\$71 million. The aggregate principal amount of the exchangeable bonds remaining outstanding following completion of the invitation to tender was US\$259 million.

Issuance of Undated Subordinated Capital Securities by Petron

On February 6, 2013 and March 11, 2013, Petron issued Undated Subordinated Capital Securities at the issue price of 100.0% amounting to US\$500 million and US\$250 million, respectively. At the option of Petron, the securities may be redeemed after five and a half years or on any distribution payment date thereafter. The proceeds were applied by Petron towards capital and other expenditures in respect of RMP-2 and used for general corporate purposes.

BEVERAGE BUSINESS

The beverage business of SMC had sales of ₱90,160 million in 2012. The beverage business of SMC can be divided into beer, liquor and non-alcoholic operations. The beer of SMC operations are conducted principally through its 51.0% owned subsidiary, SMB, which includes brewery operations in the Philippines, as well as in Hong Kong, China, Vietnam, Thailand and Indonesia. The liquor and non-alcoholic operations are conducted through its 77.4% owned subsidiary, Ginebra. Ginebra has two distilleries, located in the Philippines and Thailand. The following table sets forth certain information with respect to the domestic beer and liquor sales of SMC in 2012:

	<u>Sales</u>	<u>%</u>
	<u>(₱ in millions, except percentages)</u>	
Beer ⁽¹⁾	75,580	84%
Liquor and Non-Alcoholic Beverages	14,559	16%
Total	<u>90,139</u>	<u>100%</u>

Note:

(1) Excludes ₱21.0 million of international beer sales.

Beer Business

In 2012, the domestic beer operations of SMB were the largest contributor and accounted for 84% of the sales of the beverage business of SMC. SMB markets its beer primarily under the San Miguel brand. San Miguel beer brands include *San Miguel Pale Pilsen*, which is the flagship beer of SMB, as well as *San Miguel Super Dry*, *San Mig Light*, *San Mig Strong Ice*, *Red Horse*, *Gold Eagle*, *Cerveza Negra*, *Oktoberfest Brew*, *San Miguel Premium All-Malt*, *San Miguel Flavored Beer* and the recently introduced *San Mig Zero*.

Philippine Beer Industry

The Philippines is the third largest beer market in Southeast Asia and the sixth largest beer market in greater Asia by sales volume. In 2012, sales volume for beer in the Philippines was 16.8 million hectoliters, according to Canadean data.

Beer consumption is closely tied to consumer income and tends to grow and contract with the economy. Consumer income has been improving in recent years supported by favorable Philippine economic performance. SMB believes there is a positive correlation between per capita GDP and beer consumption in the Philippines, as illustrated in the following figure.

	2011 Real GDP per capita (₱ in thousands) ⁽¹⁾⁽²⁾	2011 Beer consumption per capita (Liters per person) ⁽²⁾
Mindanao	37	12
Visayas	41	15
South Luzon Area	59	9
Central Luzon Area	48	15
Greater Manila Area	175	36
National Average	63	15

Notes:

(1) Real GDP per capita based on 2000 prices.

(2) According to the NSCB.

The beer market in the Philippines is highly concentrated. According to Canadean, SMC had more than 90% share of the market in 2011. The other key local brewery is Asia Brewery Inc. (“ABI”), which sells beer brands such as *Beer na Beer* and *Colt 45*. Imported beer comprises a small proportion of the market and its distribution is normally limited to upscale hotels, bars, restaurants and supermarkets in Metro Manila.

The Philippines is composed of over 7,100 islands which makes distribution highly complex and expensive and represents a significant barrier to market entry for new brewers looking to distribute nationally. In the medium-term, the Philippine beer market is expected to grow at a CAGR of 4.7% from 2011 to 2016 according to Euromonitor.

Competitive Strengths

SMB believes that the principal strengths of its beer business include the following:

Highly recognizable beer brand domestically as well as in Southeast Asia. SMB had a total Philippine market share of 90% in 2011, producing all the top four beer brands in the country, namely *San Miguel Pale Pilsen*, *Red Horse*, *San Mig Light* and *Gold Eagle*, according to Canadean data.

Highly efficient distribution system. SMB believes that it has the largest and most efficient distribution system for beer in the Philippines with almost half a million on-premise and off-premise outlets nationwide.

Strong cost leadership. SMB also maintains a strong cost leadership position through high productivity and efficiency, as well as cost control measures, which facilitate pricing flexibility and greater profit growth by maintaining margins.

Business Strategies

The principal strategies of SMB for its domestic and international beer operations are as follows:

Domestic Operations

Assert market leadership. Although SMB already has a very strong position in the Philippine beer market, it intends to increase its market share by intensifying defense programs via targeted sales and marketing efforts in the regions and localities in which it believes its market share is lower than the national average. SMB intends to accomplish this by selecting specific products and adapting their value propositions to the needs of consumers. SMB also intends to increase its product visibility through tactical and creative consumer promotions and improve outlet penetration through persuasive selling and trade incentives. Similarly, SMB intends to increase its share of the overall market for alcoholic beverages. This effort will focus on those specific regions and localities in which hard liquor sales are higher, and similar to the efforts to increase market share in the beer segment, will include brand- and package-specific marketing campaigns, persuasive selling and incentives for dealers and retailers.

Further grow the overall market for beer. SMB also plans to increase its sales volume by increasing the total market for beer sales. The primary strategies of SMB to achieve this include the following:

Segmented pricing strategy. SMB intends to keep its products affordable for the middle and lower socio-economic sectors by maintaining a moderate pricing strategy for its products in the popular and economy

markets, where sales are highly price elastic. For the more upscale, or upper popular market, where sales are less price elastic, SMB plans to sustain the higher price positioning of its specialty brands, supported by image building activities to strengthen their premium positioning and improve their profitability. Amid the global economic turmoil, SMB intends to manage and align the timing and magnitude of price increases for all its products to sustain volume growth as well as cover increases in tax rates on beer and higher material costs. With the forecasted buoyant Philippine economic growth, SMB intends to pursue this segmented pricing strategy to protect its gains and to sustain the general uptrend for the industry as evidenced by the increasing market share and sales of SMB.

Enhancing the value proposition of its products. SMB intends to enhance its products' value proposition by adapting product qualities to the different needs of consumers. This allows SMB to take advantage of segment-specific growth opportunities, increasing sophistication and changing lifestyles of Philippine consumers and to maintain its market leadership position. SMB plans to maintain the iconic status of its flagship *San Miguel Pale Pilsen* brand and strengthen its value through an integrated approach of national brand-building campaigns and retail promotional and marketing efforts. SMB intends to implement new programs and initiatives catering to the younger segment of the market to protect its core customers and strengthen the appeal and preference for the brand among new drinkers. SMB expects to further grow main brands *San Miguel Pale Pilsen*, *Red Horse*, and *San Mig Light* through the introduction of new thematic campaigns, special events and volume generating programs aligned with the respective positioning of these brands in the market. For the specialty brands of SMB, including *San Miguel Premium All-Malt*, *Cerveza Negra*, *San Miguel*, *Super Dry*, and *San Mig Strong Ice*, SMB plans to increase its efforts relating to on-premise channels by matching these brands with appropriate on-premise outlets and through event sponsorships, party series and tie-ups with other companies. Specialty brands will also be promoted in targeted off-premise channels through increased visibility and promotions. For *San Miguel Flavored Beer*, SMB will highlight its benefits as a fruit-flavored beer to further tap the younger and female drinkers while health conscious segment will be tapped via *San Mig Zero*.

Increase size of the upper premium and premium segment and tap emerging consumer segments and channels. The upper premium and premium markets for beer in the Philippines are relatively small segments, but they play important roles in brand-building and overall market development. The segments offer promising prospects, underpinned by rising consumer incomes, increasing consumer sophistication, rapidly changing drinker habits and preferences, as well as increasing urbanization. SMB intends to further develop the higher-priced segments of the beer industry by offering higher-priced and higher-margin products catering to these segments. For example, in August 2008, SMB launched *San Miguel Premium All-Malt* and *Oktoberfest Brew*, a seasonal beer, which are marketed to the upper premium and upper popular segments, respectively. In December 2010, SMB launched *San Miguel Flavored Beer* to tap into female and younger drinkers. In December 2012, SMB introduced a new beer brand, *San Mig Zero*, catering to a new breed of health conscious drinkers. With this strategy, SMB aims to take advantage of opportunities in segmenting the market as well as preempting the incursion of foreign and local brands. Relative to other Asian countries, the Philippine beer market offers greater potential with regard to premium pricing of brands given the current relatively narrow price gap between the premium and upper popular brands. In addition to the upscale segment, SMB intends to continuously tap new growth segments such as the business process outsourcing sector, overseas Filipino workers, and tourism sector through initiatives tailor-made for these segments and utilization of channels which cater to these markets. SMB also recognizes the importance of fast-growing modern trade channels such as large supermarket chains, hypermarkets and modern convenience stores in marketing and carrying its products to consumers, especially in urban areas. Accordingly, SMB is focusing on sales and marketing programs for identified products to these fast growing segments of the market.

Intensify trade execution and innovation. SMB intends to further expand its trade reach and increase the visibility and availability of its products in retail outlets by accelerating point-of-sale promotions and merchandising programs for both on- and off-premise outlets to increase sales and outlet yield. In pursuing this strategy, SMB will focus on improving the efficiency of its trade operations, including trade penetration levels and adherence to suggested retail prices in all distribution channels by strengthening per-outlet management, intensifying route assisting activity and adopting alternative distribution models such as pedicabs and tricycles, which help to deliver the products of SMB to remote areas. SMB also intends to raise its frequency of calls to retail outlets. SMB intends to strengthen management of the dealers' territories through intensified retail-based servicing and territorial reconfiguration.

Increase sales through special events and promotions. SMB intends to pursue volume-generating trade initiatives such as "occasion-creation programs" as well as innovative consumer promotions and campaigns, including sponsorship of town fiestas, trademark events such as *San Miguel Beer Oktoberfest*, *Red Horse*

Muziklaban and Summer—Sarap MagBabad. These events aim to make the beer drinking experience more relevant and meaningful to the consumer.

Develop new products and packaging innovations. SMB plans to introduce new products and new package formats. SMB believes this strategy can increase consumer interest and overall market size, as well as address the needs of an increasingly fragmenting market, especially in high growth segments. For example, to increase consumer interest, in May 2007, SMB introduced *San Miguel Pale Pilsen* in paper label bottles. In 2008, SMB launched new products *San Miguel Premium All-Malt* in the upper premium segment and the *Oktoberfest Brew* (seasonal brew) in the upper popular segment as well as introduced secondary packaging, such as Christmas-themed shrink-wrap (6-pack) for *San Miguel Premium All-Malt* and clear shrink-wrap (6-pack) for *San Miguel Pale Pilsen*, *San Mig Light*, *San Miguel Super Dry* and *San Mig Strong Ice*. To attract more entry-point drinkers, SMB introduced *San Miguel Flavored Beer* in lemon and apple flavors in late 2010, its first flavored alcoholic malt beverage. In addition, *San Miguel Pale Pilsen* in 330ml bottles with paper label packaging was released in selected upscale outlets in 2011 to further boost awareness and consumption of the brand. In December 2012, *San Mig Zero*, a zero carbohydrate, low calorie and low alcohol beer was introduced to cater to health-conscious, calorie counting individuals. SMB intends to pursue packaging innovations and capitalize on the market trends toward convenience packaging and premium products as well as the increasing sophistication of consumers. SMB is developing packaging improvements for existing brands as well as convenience pack formats consistent with faster-paced lifestyles and addressing the various activities and interest of consumers

Improve resource allocation and value creation in the supply chain. SMB aims to improve resource allocation and cost management by ensuring an appropriate mix of advertising and promotions that would generate higher sales for SMB. In support of value creation in the supply chain, SMB intends to broaden its base for suppliers and materials to drive down costs without sacrificing quality. Third party service providers will also be managed more effectively, anchored on stronger partnership and shared objectives. Process and productivity improvements will be vigorously pursued in the different stages and areas of production, distribution and promotions to deliver products of superior quality while protecting profitability.

International Operations

The international operations of the beer business of SMC are primarily conducted through San Miguel Brewing International Ltd. (“SMBIL”), a wholly owned subsidiary of SMB. In the international beer business, the overall objective of SMBIL is to achieve strong volume and profit growth, which it aims to accomplish through market-specific programs that cater to local tastes and preferences while maintaining an integrated and consistent campaign for San Miguel beer brands in the region. In particular, key strategies include the following:

Strengthening the portfolio of local and international brands. SMBIL intends to further push the appropriate combination of local and international brands in its operating units to capitalize on the varied preferences of consumers in the international markets and pursue a healthy, profitable brand mix.

Accelerating the expansion of the San Miguel brand. SMBIL aims to accelerate the growth of San Miguel beer brands, primarily *San Miguel Pale Pilsen* and *San Mig Light*, consistent with the thrust of SMB to promote San Miguel as the lead brand in the portfolio of SMC in international markets. This will be done primarily through consumer and trade promotions and the development of new advertising campaigns and creative merchandising materials.

Improving sales and distribution management. Supporting the volume expansion and portfolio thrust is the objective of improving the efficiency of sales and distribution. This involves strengthening the management of dealers/wholesalers, as well as the conduct of outlet and channel-specific programs such as bar games, sportsviewing parties and promotions aligned with the respective brands’ positioning. Likewise, outlet coverage is to be expanded to cover unserved territories and grab market share from competition.

Cost reduction and efficiency improvements. To increase cost competitiveness of SMBIL, efficiency programs and cost containment measures will be implemented in the different aspects of the business such as logistics, manufacturing, sales, procurement and marketing. Processes are regularly evaluated for optimization, capability-building and development of potential synergies, where applicable, among the different units. For example, SMBIL intends to reduce freight and distribution costs through improvements in sourcing and ordering of stock as well as implementation of packaging improvements, lower cost formulation and procurement of materials on a regional scale, among others.

Selected operating metrics for the beer business of SMB for 2010, 2011 and 2012 are set forth in the table below:

	For the year ended December 31,		
	2010	2011	2012
	(P in millions, except percentages)		
Sales	67,575	71,910	75,580
Gross profit	33,070	35,091	37,560
Gross profit margin ⁽¹⁾	48.9%	48.8%	49.7%
EBITDA ⁽²⁾	21,522	23,536	25,774
EBITDA margin ⁽³⁾	31.9%	32.7%	34.0%
Net income before tax	15,235	17,369	20,976
Net income before tax margin ⁽⁴⁾	22.5%	24.2%	27.8%

Notes:

(1) Gross profit margin is calculated by sales less cost of sales divided by sales.

(2) EBITDA is calculated as net income before: income tax expense, net financing charges (interest income net of interest expense), extraordinary or exceptional items, foreign exchange losses (gains), marked-to-market currency losses (gains) and depreciation and amortization and impairment losses.

(3) EBITDA margin is calculated by EBITDA divided by sales.

(4) Net income before tax margin is calculated by net income before income tax divided by sales.

Domestic Beer Sales

In the Philippines, SMB markets its beer primarily under the San Miguel brand. San Miguel branded beer products include *San Miguel Pale Pilsen*, which is the flagship beer of SMB, as well as *San Miguel Super Dry*, *San Mig Light*, *San Mig Strong Ice*, *San Miguel Premium All-Malt*, *San Miguel Flavored Beer* and *San Mig Zero*. Other beers are marketed under the brand names *Cerveza Negra*, *Red Horse*, *Gold Eagle* and *Oktoberfest Brew*, a seasonal beer. SMB also sells *Cali*, the only domestically produced malt-based non-alcoholic drink, available in three variants: *Cali Pineapple*, *Cali Ice* and *Cali Light*. The quality of SMB beer products has been recognized by a number of organizations. Over the years, SMB brands have been awarded by Monde Selection, an independent institute that rates the quality of alcoholic beverages. In 2012, Monde Selection awarded SMB beer products with six gold medals and three silver medals, raising its total awards over the years to one grand gold award and 43 gold medals, 25 silver medals, two bronzes, two international high quality trophies and one crystal prestige award.

SMB beer products compete in the premium/upper premium, upper popular, popular and economy market segments in the Philippines. The following table sets forth the major beer brands of SMB in the Philippines and the market segments in which they compete.

Market segment	Brands
Premium/Upper Premium	<i>San Miguel Premium All-Malt</i> <i>San Miguel Super Dry</i> <i>Cerveza Negra</i>
Upper Popular	<i>San Mig Strong Ice</i> <i>San Mig Light</i> <i>San Miguel Flavored Beer</i> <i>San Mig Zero</i> <i>Oktoberfest Brew</i> (seasonal)
Popular	<i>San Miguel Pale Pilsen</i> <i>Red Horse Beer</i>
Economy	<i>Gold Eagle</i>
Non-Alcoholic	<i>Cali</i>

The share of upscale brand sales of SMB (which includes the premium/upper premium and upper popular market segments) to total SMB sales has been steadily increasing from 2% in 2000 to 12% in 2012. In contrast, the share of SMB economy brand sales (which includes the popular, economy and non-alcoholic market segments) as a percentage of total sales has been decreasing. These trends primarily reflect shifts in consumer preferences given improvements in income, increased urbanization and changes in lifestyle.

International Beer Sales

In addition to its domestic sales, SMB exports its beer products to over 40 countries, with key markets in countries such as the United Arab Emirates, Japan, Taiwan, Malaysia, Singapore and the United States. Exports of SMB are primarily sold under various San Miguel brands as well as under private labels.

SMB also has brewery operations in Hong Kong, China, Vietnam, Thailand, and Indonesia through SMBIL. These breweries have a combined annual capacity of 7.1 million hectoliters and sell their products locally as well as in various export markets.

Grupo Mahou San Miguel of Madrid, Spain has the rights to the San Miguel brand for beer in Europe, and is not affiliated with either SMB or SMC.

Production and Raw Materials

Due to the high cost of shipping within the Philippines relative to product cost as well as the importance of maintaining freshness and other distribution considerations, SMB maintains a system of regional breweries rather than a central consolidated brewing facility. SMB currently owns and operates six production facilities and one bottling plant in the Philippines. These facilities are located in the Philippines' three main island groups of Luzon, Visayas and Mindanao, and are located close to the intended end-markets in order to reduce transportation costs.

The following table indicates the capacity and utilization rate as of SMB facilities as of December 31, 2012:

<u>Production facility</u>	<u>Capacity</u> <u>(in millions of hl)</u>
Polo and Sta. Rosa	4.6
San Fernando	5.9
Mandaue	3.3
Bacolod	1.0
Davao	2.0
Total	16.8

The Polo Brewery is located north of Metro Manila and serves the Metro Manila and Southern Luzon markets. Established in 1947, it is the oldest operating brewery of SMC. The Polo Brewery underwent a modernization program during the 1990s to upgrade its brew house facilities. The San Fernando Brewery is located in Pampanga province north of Metro Manila and serves Central and Northern Luzon. It was built in 1981 and was expanded and upgraded in the late 1980s and early 1990s. The Mandaue Brewery, located on the island of Cebu, serves part of the Visayas region and Mindanao. This brewery was built in 1968 and its facilities were expanded and modernized in the 1990s. The Bacolod Brewery was built in 1990 on the island of Negros and modernized in 2005 and 2006. It serves Negros and the island of Panay. The Davao Brewery was built in 1995 and serves the Mindanao market. While production at each brewery is typically targeted to serve the geographical area around it, the distribution system can shift production from one brewery to other regions if operational issues or demand changes require. SMB transports finished beer from the Polo Brewery for bottling into the Sta. Rosa plant which was established in 2011.

The main raw materials for brewing beer include malted barley, hops, water and yeast. Adjuncts, such as sugar and non-malted grains including rice, corn grits and food starch from cassava, can also be used in conjunction with malted barley, which is generally more expensive. All of these commodities have experienced, and are expected to continue to experience, price fluctuations.

SMB procures key raw materials for its beer operations through a procurement group that uses standardized procurement procedures. Malted barley and hops are generally sourced from the North America, Australia and Europe. Adjuncts are generally sourced within the Philippines. SMB enters into supply contracts with key raw material suppliers with terms ranging from approximately one year to five years. Each of these contracts typically provide for a pre-determined fixed and formula price for the duration of the contract. In addition, depending on considerations such as price trends and the quality of raw materials, SMB also makes spot purchases on the open market. To ensure the quality of its products, SMB closely monitors the quality of its raw materials.

The following table sets forth the raw material costs of SMB for the periods indicated:

	<u>2010</u>	<u>2011</u>	<u>2012</u>
	<u>(in ₱ per kilogram)</u>		
Malt price	25.80	22.90	25.14
Corn price	19.95	20.92	20.94

SMB mostly sells its products in returnable glass bottles of varying sizes and shapes, as well as in aluminum cans and kegs. As of December 31, 2012, approximately 95% of the glass bottles used by SMB were returned bottles. The returnable glass bottle is by far the most important and popular package for beer in the Philippines, accounting for 99% of the sales of SMB as of December 31, 2012. SMB enjoys wide distribution across all trade channels, from supermarkets, grocery and convenience stores to sari-sari (“mom and pop”) stores and on-premise outlets throughout the country. These returnable glass bottles are used for up to 60 cycles typically over a span of approximately 10 years. Retail outlets selling the products of SMB collect deposits on these bottles when customers buy the beer and return the deposit when the bottles are returned. New glass bottles are purchased from time to time to support accelerating sales and to replace broken and scuffed bottles. The existing system for returnable glass bottles shields SMB from rising packaging costs triggered by increasing fuel and aluminum prices. Cans are less popular mainly because they are more expensive, although the volume of cans has been increasing in recent years with greater availability. Kegs for draft beer, which come in 15, 30 and 50 liter sizes, are limited and represent a decreasing share of the market.

All water supply used by SMB in its production is provided by deep wells, except for water used at the Polo Brewery, which is supplied by Maynilad Water Services, Inc., a third party water company serving parts of Metro Manila.

The following table sets forth the major raw materials and packaging supplies used in the business of SMB and the source countries for these items.

Key materials	Sources
Malted barley	Australia, Europe, North America
Hops	USA, Germany
Adjuncts	
Corn grits	Philippines
Sugar	Philippines
Food starch (from cassava)	Thailand, Vietnam
Rice	Philippines
Packaging Materials	
Bottles	Philippines
Crowns	Philippines
Aluminum cans	Philippines
Plastic cases	Philippines
Cartons	Philippines
Labels	Philippines, Malaysia

Each of the breweries of SMB is equipped with automated facilities capable of packaging products in a variety of packages to meet market preferences, including bottles, cans and kegs. Most of those packaging materials are produced by the packaging business of SMB.

Research and Development

SMB employs state-of-the-art brewing technology. Its highly experienced brewmasters and quality assurance practitioners provide technical leadership and direction to continuously improve and maintain high standards in product quality, process efficiency, cost effectiveness and manpower competence. Brewing technology and processes are constantly updated and new product development is ensured through continuing research and development. A research and development group is housed in the technical center building of the Polo Brewery. Research and development activities are primarily undertaken in a pilot plant located in the Polo Brewery.

SMB also has a central analytical laboratory, or “CenLab,” located in the technical center building of the Polo Brewery. The laboratory is equipped with modern equipment necessary for strategic raw materials (hops, malted barley, adjuncts) analysis and validation, beer product evaluation and new raw material accreditation. Specialized equipment includes gas chromatography, high performance liquid chromatography, atomic absorption spectroscopy, protein analyzer, and laboratory scale mashing/milling system for malt analysis. Analytical methods and validation procedures are constantly reviewed and updated, and these are standardized across all the beer laboratories of SMB. CenLab runs proficiency tests for brewery laboratories and malted barley suppliers to ascertain continuous reliability and quality of analytical test results. CenLab is also tasked with ensuring compliance of all systems with international standards, specifically ISO 17025-2005. Research and development expenses accounted for approximately 0.10%, 0.09% and 0.09% of SMB’s net sales in 2010, 2011 and 2012, respectively.

Domestic Marketing, Sales and Distribution

SMB markets, sells and distributes its beer products principally in the Philippines. Many of the products of SMB have strong market positions in the Philippines. SMB believes it maintains the most extensive distribution network in the Philippine beverage market. The beer products of SMB are distributed and sold at almost half a million outlets, including off-premise outlets such as supermarkets, grocery stores, sari-sari stores, and convenience stores, as well as on-premise outlets such as bars, restaurants, hotels and beer gardens.

As of December 31, 2012, SMB had 51 sales offices and 499 dealers throughout the Philippines. Generally, it takes five days or less for a bottle of beer to travel from production in the brewery to a sales outlet anywhere in the country. Beer is transported from the breweries by a variety of methods, mainly through third-party haulers and, in certain circumstances, by a fleet of boats contracted by SMB.

Dealers generally provide their own warehouse facilities and trucks, considerably reducing investment requirements for SMB. SMB has gradually reduced the number of its dealers to improve distribution efficiency resulting in increased volume sales. SMB has also increased the support that it provides to its dealers, including software support with respect to streamlining logistics, promotional support and financial management training. SMB enters into written distribution agreements with its dealers that specify the territory in which the dealer is permitted to sell the products of SMB, the brands that the dealer is permitted to sell, the performance standards applicable to the dealer, procedures to be followed by the dealer in connection with the distribution rights and circumstances upon which distribution rights may be terminated. The sales force of SMB designs and awards strategic sales territories to dealers based on research of the specific territory covered. Distribution rights, performance standards and sales procedures are developed by SMB and implemented in tandem with dealers to ensure high quality of services. As dealers are given exclusivity over defined geographic areas that SMB actively monitors and enforces, and based on performance, these franchises are heavily sought after by potential dealers.

Marketing Activities

SMB actively pursues marketing initiatives to promote new and existing products, as well as to maintain and enhance brand awareness of its existing products. These initiatives include media advertisements featuring well-known Philippine celebrities, sponsorship of special events, conducting various consumer and trade promotions and other merchandising activities. SMB also uses television, radio, print and online advertisements, outdoor billboards and posters that can be placed on the walls of retail outlets and restaurants, bars and other on-premise outlets. SMB operates a beer delivery business, “632-BEER,” which provides free beer delivery service for parts of Metro Manila. Advertising and promotion expenses of SMB were ₱3,112 million in 2012.

SMB holds major events and sponsors numerous music events as part of its marketing efforts. *San Miguel Beer Oktoberfest* has been the brand’s flagship event for over three decades. This seasonal festival of beer and activities takes place from September to December at numerous locations simultaneously across the Philippines. Popular bands and celebrities, including San Miguel beer endorsers, are on hand to entertain the crowds. SMB also holds *San Miguel Pale Pilsen’s* nationwide SMB Sarap Magbaband Summer Campaign, which is an annual get-together of games, concerts and parties at the country’s popular beaches. In addition to *San Miguel Pale Pilsen*, *Red Horse* is also often a major sponsor of concerts, with the brand affiliated with Muziklaban, the country’s biggest annual rock challenge, a band competition. For *San Mig Light*, SMB conducts music party initiatives such as “Party All Night” events and “Bucket Nights” promotion in selected bars and restaurants. SMB offers Beer Tasting bar tours to upscale outlets for *San Miguel Premium All-Malt*, *San Miguel Super Dry* and *Cerveza Negra*.

Competition

SMB faces direct competition from ABI, which sells beer and other alcoholic products as well as non-alcoholic beverages. ABI competes mainly on the basis of price and leverages on its wider product portfolio to push its brands (e.g. *Beer na Beer*, *Colt 45* and *Tanduay Ice*) in the market. Its alcopop brand, *Tanduay Ice*, mainly competes with *San Mig Light*, while *Colt 45* targets *Red Horse* drinkers. It distributes its products through a network of dealers and wholesalers and has marketing arms which provides specific services to ABI (e.g., hauling and routing).

Competition from imported beers is minimal.

SMB competes with producers of other alcoholic beverages, primarily gin, rum, brandy and alcopops. In the beer industry — and more generally the alcoholic beverages industry — competitive factors generally include price, product quality, brand awareness and loyalty, distribution coverage, and the ability to respond effectively to shifting consumer tastes and preferences. SMB believes that its market leadership, size and scale of operations, and extensive distribution network create high entry barriers and provide SMB with a competitive advantage.

Liquor Business

In 2012, the liquor operations of SMC had sales of ₱14,559 million, accounting for 16% of the beverages sales of SMC and 2.05% of total sales. The liquor operations of SMC are conducted through its 77.4%-owned subsidiary, Ginebra. Ginebra was founded in 1902 as a family-owned distillery and listed on the PSE in 1995. It trades under the symbol “GSML.”

Today, Ginebra operates two distilleries and six liquor bottling facilities. To augment the bottling capacity of these facilities, Ginebra also entered into toll manufacturing agreements with third parties to produce liquor products, located in Polo, Valenzuela and Calamba, Laguna.

Among its subsidiaries are (1) Distileria Bago, Inc. (“DBI”), an entity with a distillery located at Bago City, Negros Occidental, that converts sugar cane molasses into alcohol, which entity became a wholly owned subsidiary of Ginebra in 1996; and (2) Agricrops Industries, Inc., which was incorporated in 2000 as a wholly owned subsidiary of Ginebra to primarily engage in the production of cassava starch milk, an alternative raw material for the production of alcohol.

To support its entry into the regional markets, Ginebra entered into a share purchase agreement with the Thai Life Group of Companies covering shares in Thai San Miguel Liquor Co., Ltd., and owned 44.9% of such company as of December 31, 2012.

Philippine Liquor Industry

The majority of domestic sales of liquor are made to those segments of the population seeking economy products. While quality and drinkability of liquor are important, popular pricing strategies are essential, especially for new products. Local manufacturers enjoy a competitive advantage in terms of price as demand is highly price sensitive. The performance of the liquor industry is highly dependent on the economy, especially for imported brands.

Domestic brands, namely *Ginebra*, *Tanduay*, and *Emperador* continue to dominate the market, accounting for a 93% share of total industry volume sales in 2012, according to the 2012 Retail Trade Audit Report from Nielsen. The products sold consist mainly of gin and brandy.

Competitive Strengths

Ginebra believes that its principal strengths include the following:

Market leading brands. Ginebra has market leading brands in *Ginebra San Miguel Gin*, *GSM Blue Gin* and *Vino Kulafu*.

Streamlined distribution network. Ginebra has a streamlined distribution network with direct shipments to a diversified base of large dealers assigned to specific geographic areas.

Strong Cost Leadership. Ginebra has established and has led the establishment of a diversified raw material base.

Business Strategies

Principal strategies of Ginebra include the following:

Expand distribution. Ginebra is installing distributors and setting up direct selling operations particularly in Southern Philippines, where market penetration is low and where only a few dealers cover the area. *Ginebra San Miguel* is introducing new product offerings to serve the dynamic consumer market in key areas in Northern Philippines.

Secure raw material sources. Ginebra has embarked on initiatives to search for alternative raw materials to complement molasses, which is under threat from increasing prices and decreasing availability as it is used as a raw material for the Philippine government’s clean fuel program. Cassava has proven to be a reliable substitute for molasses and its supply sustainability is currently being developed. Ginebra will also import more crude alcohol as an alternative if proven to be more cost efficient at certain points in time.

Grow Non-Alcoholic Business. Ginebra is broadening its distribution of non-alcoholic beverages to the “at-work” and school markets. It has also recently embarked on the distribution of energy drinks, one of the fastest growing segments in the Non-Alcoholic Beverage business market.

Selected operating data for the liquor business of Ginebra are set forth in the table below for the periods indicated:

	For the year ended December 31,		
	2010	2011	2012
	(P in millions, except percentages)		
Sales	22,688	15,113	14,559
Gross profit	5,109	3,137	3,461
Gross profit margin ⁽¹⁾	22.5%	20.8%	23.8%
EBITDA ⁽²⁾	2,060	(362)	153
EBITDA margin ⁽³⁾	9.1%	(2.4)%	1.1%
Net income before tax	1,337	(1,349)	1,159
Net income before tax margin ⁽⁴⁾	5.9%	(8.9)%	(8.0)%

Notes:

- (1) Gross profit margin is calculated by sales minus cost of sales divided by sales.
- (2) EBITDA is calculated as net income before: income tax expense, net financing charges (interest income net of interest expense), extraordinary or exceptional items, foreign exchange losses (gains), marked-to-market currency losses (gains) and depreciation and amortization and impairment losses.
- (3) EBITDA margin is calculated by EBITDA divided by sales.
- (4) Net income before tax margin is calculated by net income before income tax divided by sales.

Ginebra Sales

Ginebra is one of the leaders in the Philippine liquor market, and produces, markets and sells some of the most recognizable brands in the Philippine liquor market, including *Ginebra San Miguel*, *GSM Blue*, *Gran Matador Brandy*, *Antonov Vodka* and *Vino Kulafu*.

Ginebra offers a range of liquor in the premium, popular and economy market segments, including gin, brandy, Chinese wine, vodka, tequila and whisky. Ginebra also produces and sells non-carbonated ready-to-drink tea and fruit juices primarily under the *Magnolia* brand. The following table sets forth the sales of the principal product categories for the periods indicated:

	For the years ended December 31,					
	2010		2011		2012	
	(P in millions, except percentages)					
Gin	14,506	63.9%	11,346	75.1%	11,684	80.3%
Brandy	4,653	20.5%	1,186	7.8%	243	1.7%
Chinese wine	827	3.6%	774	5.1%	811	5.6%
Others (including <i>Magnolia</i> branded beverages)	2,601	11.5%	1,751	11.6%	1,784	12.2%
Exports	102	0.5%	56	0.4%	37	0.2%
Total	22,689	100%	15,113	100%	14,559	100%

The following table sets forth Ginebra's principal products and brands:

Segment	Product	
Premium	<i>Ginebra San Miguel Premium Gin</i>	<i>Don Enrique Mixkila</i>
	<i>Antonov Vodka</i>	<i>Antonov Vodka Apple</i>
Upper Popular	<i>St. George Premium Whisky</i>	<i>Solera Gran Reserva</i>
Popular	<i>GSM Blue</i>	<i>Gran Matador Solera</i>
Economy	<i>Vino Kulafu</i>	<i>Anejo Rum</i>
	<i>Ginebra San Miguel Red</i>	
Non-Alcoholic	<i>Magnolia Health Tea</i>	<i>Magnolia Pure Water</i>
	<i>Magnolia Life Drink</i>	<i>Magnolia Powdered Iced Tea</i>
	<i>Magnolia Fruit Drink Mix</i>	

The quality of the products of Ginebra has been recognized by a number of organizations, including the Monde Selection of Belgium which has awarded quality medals to various Ginebra brands in past years.

Consumer preferences in the Philippine liquor market vary largely by geographical region. As a general matter, consumers in northern Philippines prefer gin and brandy, while consumers in southern Philippines prefer rum. As brandy is becoming more popular in both northern and southern Philippines, Ginebra launched *Gran Matador Brandy* in 2003.

Currently, Ginebra is focused on new product development and market diversification. For example, in 2005, Ginebra launched *Solera Gran Reserva*, *Ginebra San Miguel Premium Gin*, *Antonov Vodka* and *Don Enrique Mixkila* to target the premium and upper popular segments. In 2012, Ginebra launched *Ginebra San Miguel* flavored gin, three varieties of *Antonov Vodka* mixed drink, *GSM Blue Light* and *GSM Blue* flavors to cater to the shifting consumer preference towards ready-to-drink flavored alcoholic beverages and beverages with lower alcohol content.

Exports and Overseas Operations

The primary export markets of Ginebra are Thailand, Taiwan, Korea, Japan, China and the Middle East. Ginebra is currently evaluating the possibility of exporting to the United States and India. Competition in the export markets is intense. The competitors of Ginebra include a number of international liquor producers, some of which may have greater production, marketing, financial and other resources than Ginebra.

In addition to exports of liquor, Ginebra sells and distributes liquor in Thailand through a joint venture.

Raw Materials and Production

Alcohol is the main raw material used in the production of liquor. Ginebra produces most of its alcohol at its distillery plant in Bago City, Negros Occidental. Alcohol is produced primarily from molasses, which is purchased from a variety of third-party suppliers pursuant to supply contracts as well as on the open market. Recently, as the price for molasses has increased, Ginebra has been considering alternative raw materials from which it can distill alcohol, such as cassava starch milk. In particular, Ginebra recently constructed a cassava starch milk plant in the Philippines to enable it to use this alternative raw material for the production of alcohol.

Ginebra owns one distillery, five liquor bottling plants and one cassava starch milk plant, and has engaged three toll bottlers strategically located throughout the Philippines and one bottling and distillery plant in Thailand. The following table sets forth the capacity, production volume and utilization rate of each of the currently operating distillery and production facilities of Ginebra in 2012:

<u>Facility</u>	<u>Capacity</u> <u>(in millions of hl)</u>	<u>Production</u> <u>(in millions of hl)</u>	<u>Utilization rate</u>
<i>Distillery</i>			
DBI Distillery Plant	0.851	0.603	70.79%
Thailand Distillery	0.225	0.195	86.77%
<i>Liquor Bottling Plant</i>			
Cabuyao	1.53	0.451	29.42%
Santa Barbara	1.90	0.642	33.87%
Cebu	1.18	0.199	16.91%
Ligao	0.40	0.115	28.99%
Cauayan	0.40	0.177	45.50%

The liquor products of Ginebra are primarily packaged in glass bottles. In 2012, the packaging business produced the majority of the new glass bottle requirements of Ginebra. In addition to using new glass bottles, Ginebra maintains a network of bottle suppliers in the Philippines that recycles second-hand bottles back to the plants of Ginebra. In 2012, approximately 64% of the bottles used by Ginebra were recycled bottles. Even with the additional cost of maintaining a quality control system for the safety of recycled bottles, the cost of recycled bottles is approximately half of the cost of new bottles. Because the cost of recycled bottles is lower than that of new bottles, bottling costs for any particular product are generally expected to decrease over time as a result of the increased use of recycled bottles.

Distribution

Ginebra distributes its products by shipping directly to dealers. Ginebra has recently streamlined its distribution network by reorganizing its network of dealers by assigned geographic areas. The reorganization was designed to enhance the efficiency of the distribution network by having fewer, but larger, dealers. Ginebra had 119 dealers for its liquor products and nine sales offices for its nonalcoholic beverage products as of year-end 2012. Ginebra utilizes third party services in the warehousing and delivery of its products.

Recently, it had embarked on a program to install more distributors, including in the Southern Philippines. It also maintains an organization for direct selling operations to gain better control of market operations. The Sales unit has a Key Accounts Group to handle modern trade and on-premise outlets in key cities.

Marketing and Competition

Ginebra markets its products through a variety of channels, including television, radio, billboard and print advertisements, as well as special event sponsorships, consumer promotions and trade promotions. The advertising and promotion expenses of Ginebra were approximately ₱1.3 billion in 2012, accounting for 12% of the cost of sales of Ginebra.

Most of products of Ginebra target the Popular and Economy market segments. The major competitors of Ginebra in these segments include Emperador Distillers Inc. and Tanduay Distillers Inc.

In the premium market segment, the major competitors of Ginebra include Gilbey's and Absolut. As Ginebra endeavors to create a niche in the premium market segment with the introduction of premium brand names, Ginebra will continue to rely on its competitive advantages including price, quality and extensive distribution network.

Regulation and Taxation of Beverages

Philippine national and local laws and regulations require a license to sell alcoholic beverages and prohibit the sale of alcoholic beverages to persons below 18 years of age or within a certain distance from schools and churches. Advertising and marketing of alcoholic beverages is largely unregulated in the Philippines. SMB and Ginebra, however, aim to promote responsible drinking habits through their advertising and marketing programs, and have both formulated and adopted an Advertising & Marketing Code of Ethics for Alcoholic Beverages.

In the Philippines, excise tax is payable by the producer, and the tax rate varies depending on the type of alcoholic beverage being produced, with more expensive products being subject to higher rates.

With the enactment of R.A. 10351, SMB products are subject to the following excise tax rates:

Product	Effective date of tax rates					
	January 1, 2013	January 1, 2014	January 1, 2015	January 1, 2016	January 1, 2017	January 1, 2018
Fermented liquors						
where the net retail price (excluding the excise and value added tax) per liter of volume capacity is:						
(a) ₱50.60 or less	₱15.00	₱17.00	₱19.00	₱21.00	₱23.50	Effective January 1, 2018, the specific tax rate shall be increased by 4% every year thereafter
(b) More than ₱50.60	₱20.00	₱21.00	₱22.00	₱23.00	₱23.50	

Ginebra products are subject to the following excise tax rates:

Product	Effective date of tax rates					
	January 1, 2013	January 1, 2014	January 1, 2015	January 1, 2016	January 1, 2017	January 1, 2018
Distilled Spirits						
(a) Ad Valorem Tax Rate						
Based on the net retail price per proof (excluding the excise and value added tax) . .	15%	15%	20%		20%	20%
(b) Specific Tax	₱20.00	₱20.00	₱20.00		₱20.80	₱21.63
Per proof liter						₱22.50
				Effective January 1, 2016, the specific tax rate shall be increased by 4% every year thereafter		

FOOD BUSINESS

SMC operates its food business through San Miguel Pure Foods and its subsidiaries and is a leading player in the Philippine food industry, offering a broad range of high-quality food products and services to both household and food service customers. The performance of San Miguel Pure Foods is closely correlated to domestic economic growth, as well as to trends and developments in each segment within the industry. San Miguel Pure Foods has been listed on the PSE since 1971. SMC completed the secondary offering of its shares in San Miguel Pure

Foods following the crossing of the shares through the PSE on November 21, 2012 and San Miguel Pure Foods currently has a 15% public float.

The food business of SMC is organized into the following business clusters and their contribution to the sales of San Miguel Pure Foods in 2010, 2011 and 2012 is shown in the table below:

	2010		2011		2012	
	Sales	% of Sales	Sales	% of Sales	Sales	% of Sales
	(₱ in millions)		(₱ in millions)		(₱ in millions)	
Agro-Industrial	52,300	66.0	56,982	63.6	61,877	64.6
Value-Added Meats	11,534	14.6	12,103	13.5	13,665	14.3
Milling	7,155	9.0	8,354	9.3	8,425	8.8
Others	8,281	10.4	12,152	13.6	11,820	12.3
Total	79,270	100.0	89,591	100.0	95,787	100.0

San Miguel Pure Foods has some of the best known and well-regarded brands in the Philippines food industry, such as *Magnolia*, *Purefoods*, *Monterey*, *Star*, *Dari Crème* and *B-Meg*. The wide range of food products of San Miguel Pure Foods includes the following:

Business	Major products
Agro-Industrial	
Poultry	Branded products are sold under the <i>Magnolia</i> Fresh Chicken label and include fresh-chilled whole chickens, a variety of chicken cut-ups, ready-to-cook and ready-to-eat products
Feeds	Hog, poultry (layer/broiler), gamefowl, aquatic, duck and other customized feeds
Fresh Meats	Pork and beef carcasses, various pork cuts, beef cuts, marinated meats, lamb products, live hogs and cattle
Value-Added Meats	Refrigerated meat products, include hotdogs, bacon, hams, chicken nuggets and a line of local Philippine products and canned products such as corned beef, luncheon meat, sausages, spreads and ready-to-eat viands
Milling	A full range of basic, specialty and customized flour products, and flour premixes
Dairy, Spreads and Oils	Bread spreads, cheese, milk, ice cream, jelly-based snacks and cooking oils
Emerging Businesses	Coffee, food distribution service and retail franchise management.

As of December 31, 2012, San Miguel Pure Foods operates 34 company-owned production facilities and over 2,000 third-party owned facilities.

Philippine Food and Agriculture Industry

According to the National Statistics Office, there was a general upward movement in food prices in the Philippines in 2012, taking into consideration a number of typhoons and natural calamities, which led to the disruption of the production of raw materials.

The sufficient supply of chicken in the markets generally observed during 2012 resulted to the slower annual increments in the meat index in the three areas: Philippines, 1.4% in 2012 from 2.2% in 2011, National Capital Region (“NCR”), 1.6% in 2012 from 2.0% in 2011, and Areas Outside NCR (“AONCR”), 1.3% in 2012 from 2.3% in 2011.

Upward annual price adjustments in milk and cheese products were seen in many regions including NCR. Moreover, decreases in the number of chicken layers lowered the production of eggs thereby limiting supplies in the markets. Thus, the annual average growth of the milk, cheese and eggs index in the Philippines increased to 3.3% in 2012 from 2.7% in 2011; NCR, 3.6% in 2012 from 2.0% in 2011; and AONCR, 3.2% in 2012 from 2.9% in 2011.

Competitive Strengths

San Miguel Pure Foods believes that its principal strengths include the following:

Portfolio of well recognized brands known for quality. San Miguel Pure Foods has successfully developed a strong portfolio of well-recognized brands known for quality in the Philippines, including *Magnolia* for chicken, ice cream and milk products, *Monterey* for fresh and marinated meats, *Purefoods* for refrigerated processed meats and canned meats, *Star* and *Dari Crème* for margarine, *San Mig Coffee* for coffee and *B-Meg* for animal feeds. As a testament to the strength of its brands in the Philippines, San Miguel Pure Foods has established market-leading positions in several segments and product categories. San Miguel Pure Foods has continuously enhanced brand recognition and trust with consumers by consistently maintaining high product quality, as well as through active and targeted marketing and promotional campaigns. Through these efforts, San Miguel Pure Foods has not only developed leading brands for traditionally branded food segments, but has also established successful branding for traditionally commoditized product segments such as *Magnolia* for poultry, *Monterey* for fresh meats, *B-Meg* for feeds, and *King and Queen* for flour. San Miguel Pure Foods believes that its well-recognized brands have allowed it to develop strong customer loyalty resulting in repeat purchases that provide it with greater pricing power relative to its competitors. In addition, the multi-brand strategy of San Miguel Pure Foods allows it to broaden its product reach to customers more easily than its competitors given its significant brand recognition and reputation for quality.

Broad and diverse portfolio catering to different customer needs and preferences. San Miguel Pure Foods offers one of the widest arrays of food products in the Philippines. San Miguel Pure Foods produces food products for household, institutional and food service customers and derives its sales from several different product segments, including poultry, fresh meats, refrigerated processed meats and canned meats, basic flour and flour premixes, dairy, spreads and oils, and coffee. San Miguel Pure Foods also produces animal and aquatic feeds. The product diversity of San Miguel Pure Foods reduces its dependence on any single product segment and makes it more resilient to changes in competitive dynamics or raw material price fluctuations that may impact one product segment more than another. Its diverse product portfolio also provides marketing and product synergies across segments, as products can complement each other and provide an integrated, one-stop solution for customers' everyday food needs.

Extensive market penetration and multi-channel distribution network. San Miguel Pure Foods operates and manages one of the most extensive distribution networks across the Philippines, with its products available in every major city, and it believes that this provides a significant competitive advantage. To maximize market penetration, San Miguel Pure Foods has a multi-channel distribution network that supplies its products to supermarkets and traditional retail outlets, trade, food service channels and franchised stores. For the value-added meats business, it centrally manages sales and distribution through San Miguel Integrated Sales, which is responsible for selling San Miguel Pure Foods value-added products to both modern trades, such as major supermarket chains, hypermarkets, groceries, convenience stores, and general trades, market traders and "sari-sari" stores (small neighborhood stores). For its feeds, poultry, fresh meats and flour businesses, San Miguel Pure Foods maintains business-specific sales forces to service trade channels and manage its distributors and dealers. Great Food Solutions of San Miguel Pure Foods, on the other hand, manages sales to key food service customers, such as hotels, restaurants, bakeshops, fast-food and pizza chains. Meanwhile, the distribution advantage of the feeds business lies in the location of its production facilities, which are strategically located close to its primary markets or the major sources of its raw materials. San Miguel Pure Foods believes that its multi-channel distribution platform has allowed it to maximize customer reach and has been one of the key factors to its success in building and developing its market-leading positions.

"Farm to plate" and "asset light" vertical integration allowing for higher efficiency, profitability and operational synergies. San Miguel Pure Foods has a vertically integrated business model across the entire food value chain from plantations and feed production to meat processing and distribution of branded products. For example, San Miguel Pure Foods works with farmers and consolidators to provide raw materials (such as cassava and corn) for its feeds business, which, in turn, provides feeds for its poultry and hog farms. Output from these farms is then processed and distributed to customers, including through the retail formats of San Miguel Pure Foods, such as *Magnolia* chicken stations and *Monterey* meat shops. San Miguel Pure Foods believes that its "farm to plate" integrated business model allows it to derive synergies and extract margins along the entire food value chain, which improves operating efficiency and profitability. San Miguel Pure Foods also believes that this integrated business model results in further benefits from economies of scale, as it is able to consolidate raw materials purchases, integrate production functions and share sales and distribution networks, brands and support functions. Moreover, the integrated business model of San Miguel Pure Foods also provides it with enhanced operational flexibility and allows it to quickly adapt and augment its products in line with prevailing market and consumer tastes. Lastly, San Miguel Pure Foods believes that its integrated business model allows San Miguel

Pure Foods to maintain its strict quality standards by ensuring that high quality inputs are used and best practices are implemented at each stage of the production process.

Experienced management and technical teams. San Miguel Pure Foods has a strong and deep management team with a proven track record and an average of more than 20 years of industry and management experience. The management team is well accustomed to the Philippine operating environment and has effectively managed San Miguel Pure Foods both in times of strong economic growth as well as through periods of economic downturn and political instability. The strength and depth of the experience of the management team of San Miguel Pure Foods have been demonstrated by their successful implementation of a range of efficiency programs and product innovations, which has resulted in continued profitability and market leadership for San Miguel Pure Foods over the years.

The “San Miguel” brand reputation and ownership. San Miguel Pure Foods believes that it benefits from the strong market position of SMC as one of the largest and strongest conglomerates in the Philippines, as well as its extensive range of product offerings in its other businesses such as beverages and fuel and oil, particularly with respect to consumers’ and retailers’ positive perception of the “San Miguel” name. San Miguel Pure Foods believes that SMC is highly regarded in the Philippine business community and believes that it benefits from the strong business reputation of SMC. Operationally, San Miguel Pure Foods has realized synergies from its relationship with SMC, including increased market penetration of its *San Mig Food Ave* outlets by leveraging on current locations of Petron, the supply of products and customized food solutions to PAL, an SMC affiliate, and the sourcing of raw materials such as brewer’s spent grain and yeast from SMB.

Business Strategies

San Miguel Pure Foods plans to maintain its market-leading position and expand its business operations by implementing the following three-pronged business strategy:

Enhance product offering and distribution.

Focus on increasing stable-priced and value-added product offerings. San Miguel Pure Foods categorizes its product portfolio into three groups: (i) value-added products; (ii) stable-priced products; and (iii) commodity products. Value-added products include processed meats, dairy, breads/spreads, oils, ice cream and coffee. These products are typically branded and command higher selling prices than stable-priced and commodity products. Stable-priced products include flour premixes and bakery ingredients and poultry and fresh meats products that are distributed through the differentiated stable-priced sales channels of San Miguel Pure Foods. These products include (i) minimally processed branded products sold through *Magnolia* chicken stations and *Monterey* meat shops, (ii) branded products that have undergone further processing, such as marinated meats, ready-to-cook and ready-to-eat products sold through *Magnolia* chicken stations and *Monterey* meat shops and (iii) non-branded customized products sold to food service clients. Commodity products include (i) feeds, (ii) live chickens and hogs, (iii) fresh-chilled and frozen whole chicken, and chicken, pork and beef cuts sold through wet markets and supermarkets and (iv) basic flour products. San Miguel Pure Foods has limited pricing power for its commodity products due to the lack of product differentiation, while it believes that its stable-priced and value-added products are able to command higher and more stable prices and margins due to (i) strong brand equity with customers, (ii) processing or customization to cater to specific needs or tastes and/or (iii) sale through its branded distribution outlets, where cleanliness, convenience and quality assurance allow for premium pricing and higher margins. San Miguel Pure Foods has made a concerted effort to improve its product mix by shifting away from commodity products, which generally have lower and more volatile margins, and into value-added and stable-priced products, which it believes have higher and more consistent margins. San Miguel Pure Foods has successfully implemented several initiatives to improve its product mix towards a higher percentage of stable-priced and value-added products and it plans to continue with these and new initiatives to further improve its product mix in this respect. Through these initiatives, San Miguel Pure Foods has significantly increased the proportion of value-added and stable-priced products in its product offerings over the past 10 years. In 2012, the contribution of value-added and stable-priced products already accounted for approximately half of the total sales of San Miguel Pure Foods as compared to approximately one-fourth in 2000. To increase profitability and address the ongoing trend of consumers increasingly demanding greater product variety and sophistication, convenience and quality, San Miguel Pure Foods intends to continue increasing the proportion of stable-priced and value-added products that it sells through the continuation of the initiatives discussed above and potentially expanding into fast growing markets and product categories, both in the Philippines and other countries in Southeast Asia.

Continuous investment in brand equity. San Miguel Pure Foods aims to continue building its brand equity through advertising and promotional activities. San Miguel Pure Foods advertises on television, radio and

billboards, as well as in print and the web. In 2012, San Miguel Pure Foods launched advertising campaigns featuring celebrity endorsers and a grassroots educational campaign to promote safe and quality meats. San Miguel Pure Foods also regularly participates in major events throughout the country such as fiestas and food fairs. As part of its brand-building activities, San Miguel Pure Foods maintains a professional basketball team in the Philippine Basketball Association, the premiere basketball league in the country. In the past, the team carried the banners of Purefoods Tender Juicy and B-Meg Llamados, among others. Currently, the team is called San Mig Coffee Mixers.

Improve profitability through cost leadership.

San Miguel Pure Foods believes that it can increase its margins by adopting a multi-faceted approach of managing input costs with respect to its raw materials and optimizing its production efficiency.

Continue sourcing alternative raw materials. The use of alternative raw materials, from grains and by-products used as feeds ingredients, to alternative protein sources and flavors for processed meats, is critical to cost management given the volatile nature of global commodity supply and prices. San Miguel Pure Foods expects to continue to expand its raw material supply base and identify alternative raw materials that are critical to cost management given the volatility of the global commodity market. One key breakthrough is the use of cassava as a substitute for corn, a key feed ingredient. San Miguel Pure Foods has implemented a program to encourage farmers to plant cassava and other crops that can be used as feeds ingredients. In 2011, San Miguel Pure Foods encouraged local farmers to develop approximately 50,000 hectares of cassava plantations, which satisfied about 50% of the cassava requirements of San Miguel Pure Foods during the year. San Miguel Pure Foods will continue to focus on developing alternative raw materials to manage its cost base. San Miguel Pure Foods is currently using and expects to increase usage of imported cassava by-product as a lower cost alternative to corn and cassava as a feeds ingredient. The strong research and development team of San Miguel Pure Foods is responsible for the continued effort in identifying cost improvements while maintaining product quality standards.

Focus on efficiency improvements. San Miguel Pure Foods has been focused on increasing the efficiency of existing operations and implementing targeted initiatives in its businesses. For example, the adoption of climate controlled housing system for its poultry and hog farms has increased production cycles per farm per year, improved feeds-consumed-to-weight-gained ratio and resulted in better harvest recovery. Additionally, upon the expected commencement of its operations in the second half of 2013, the Mabini bulk grain terminal is expected to enable San Miguel Pure Foods to ship grains through larger vessels, concurrently lowering freight costs and addressing grain handling requirements for the feeds and flour operations. In addition, San Miguel Pure Foods intends to continuously review its product portfolio to rationalize unprofitable products from its portfolio. Consistent with this, San Miguel Pure Foods aims to enhance the price stability of its sales streams and margins by increasing the percentage of sales of products that have historically performed well and which San Miguel Pure Foods believes will continue to do so.

Continue harvesting synergies through further integration of the businesses. San Miguel Pure Foods intends to continue to maximize vertical integration, simplify its organizational structure and standardize its business processes to achieve operational synergies and prepare for future growth. Recent improvements include the establishment of a shared service delivery center for finance, which is able to serve all of the business segments of San Miguel Pure Foods and perform transaction processing activities, reducing administrative expenses. It also intends to further progress in the development of a world class supply chain that will result in reduced inventory days level and improved service levels.

Explore additional growth opportunities.

San Miguel Pure Foods believes the Philippine market is still underserved in certain product categories and there are opportunities to improve its distribution network, particularly in remote areas in Visayas and Mindanao. It also intends to enter into new product categories and expand its existing production capabilities to support its growing range of product offerings, which will help enable San Miguel Pure Foods to meet the changing consumer needs. San Miguel Pure Foods expects to continue sourcing potential acquisition targets in food or food-related businesses, including strategic acquisitions in fast-growing emerging Asian countries, as part of its growth strategy. Such growth opportunities in food or food related businesses may also be pursued jointly with SMC, particularly in situations where the transactions might be too large for San Miguel Pure Foods to undertake by itself.

Selected operating data for the business of San Miguel Pure Foods are set forth in the table below for the periods indicated:

	For the year ended December 31,		
	2010	2011	2012
	(P in millions, except percentages)		
Sales	79,270	89,591	95,787
Gross profit	15,979	16,174	17,838
Gross profit margin ⁽¹⁾	20.2%	18.1%	18.6%
EBITDA ⁽²⁾	7,893	8,276	8,638
EBITDA margin ⁽³⁾	10.0%	9.2%	9.0%
Net income before tax	5,713	5,958	5,885
Net income before tax margin ⁽⁴⁾	7.2%	6.7%	6.1%

Notes:

(1) Gross profit margin is calculated by sales less cost of sales, divided by sales.

(2) EBITDA is calculated as net income before: income tax expense, net financing charges (interest income net of interest expense), extraordinary or exceptional items, foreign exchange losses (gains), marked-to-market currency losses (gains) and depreciation and amortization and impairment losses.

(3) EBITDA margin is calculated by EBITDA divided by sales.

(4) Net income before tax margin is calculated by net income before income tax divided by sales.

Agro-Industrial Cluster

Poultry

The poultry business of San Miguel Pure Foods includes the breeding, producing and marketing of broilers, mostly for retail. The broad range of products is sold under the *Magnolia Fresh Chicken* brand (including fresh, chilled, frozen and cut-up products) and through *Magnolia* Chicken Stations (including easy-to-cook and ready-to-eat products). San Miguel Pure Foods also sells customized products to food service clients and supermarket house brands, and live chickens to dealers.

As of December 31, 2012, San Miguel Pure Foods contracted with tolled growing farms with an estimated annual capacity of 330 million birds. The vertically controlled poultry operations of San Miguel Pure Foods also include 34 owned and tolled processing plants and an extensive network of cold storage warehouses and distribution facilities.

The poultry business of San Miguel Pure Foods faces local competition from numerous independent broiler producers and a small number of larger integrators. San Miguel Pure Foods believes that one of those larger competitors held less than one half of the market share in 2012 at 21%, while another held approximately 6% of the Philippine broiler market in 2012. San Miguel Pure Foods also sometimes faces competition from low-priced imports from the United States and Canada, as well as new competitors as a result of frequent supply shortages and high prices in recent years.

Feeds

The Philippine feeds industry comprises three segments: (a) the home-mix segment which comprises small to medium-scale farms producing their own feeds; (b) the intra segment which includes large, integrated livestock and poultry farms producing their own feeds; and (c) the commercial segment which produces branded feeds for third parties. Much like the poultry industry, the Philippine feeds industry has been transformed from a fragmented, backyard industry into a more concentrated and efficient industry with a small number of dominant feedmillers.

San Miguel Pure Foods believes it is the largest producer of feeds in the Philippines, producing feeds for (i) the poultry business of San Miguel Pure Foods, (ii) the fresh meats business of San Miguel Pure Foods and (iii) the commercial feeds market of San Miguel Pure Foods, which accounted for 42%, 11% and 46%, respectively, of the feeds business volumes of San Miguel Pure Foods in 2012. The commercial products of San Miguel Pure Foods include hog feeds, layer feeds, broiler feeds, gamefowl feeds, aquatic feeds, branded concentrates and customized feeds sold under various brands including *B-Meg*, *Pureblend*, *Bonanza* and *Jumbo*.

San Miguel Pure Foods is refocusing its efforts on developing small and medium-sized farms, producing specialty and customized feeds, and increasing its participation in the aquatic feeds industry. San Miguel Pure Foods is also focusing on raw material cost efficiencies. Raw materials used in the feeds business of San Miguel Pure Foods are mostly provided through the business procurement group, while some local ingredients are

sourced directly from suppliers and traders accredited by San Miguel Pure Foods and on the open market. San Miguel Pure Foods developed cassava as a strategic alternative ingredient to corn in animal feeds. The proportion of cassava in animal feeds can be adjusted upward or downward depending on the relative price of corn and other feed ingredients. Cassava is safe, relatively low-priced and widely available in the Philippines.

To protect against unexpected price increases, San Miguel Pure Foods participates in both physical and financial hedging for certain imported raw materials such as soybean meal and maintains strategic buying programs for corn. San Miguel Pure Foods also uses by-products from SMB (including brewer's spent grain and yeast) and the poultry dressing plants (including offal and feathers) as raw materials for feeds production. San Miguel Pure Foods contracts with five tolled rendering facilities that convert animal by-products into a protein ingredient for feeds and expect to add rendering plants in the future. Compound feeds are manufactured at six San Miguel Pure Foods-owned facilities and 32 third-party owned and operated feeds plants, strategically located throughout the Philippines. Most of these plants are capable of producing pelleted and crumble format feeds, and three plants have extrusion capabilities to produce aquatic floating feeds.

San Miguel Pure Foods owns several research and development facilities which analyze average daily weight gain, feed conversion efficiency and other performance parameters. Results of these analyses are immediately applied to the commercial feed formulations to minimize costs and maximize animal growth. These research facilities include a bio assay-focused research facility, a metabolizable energy-focused research facility, a research facility for tilapia, three hog research farms, three broiler research farms, a fry production facility and various hatching facilities for tilapia breeding. The commercial feeds business of San Miguel Pure Foods sells its products through several distribution channels, with approximately 80% of products sold through authorized distributors within a defined territory and 20% sold directly to hog, poultry and aquatic farm operators. The commercial feeds business has more than 18 sales offices across the Philippines, which are supported by an expert sales team focused on developing new markets.

San Miguel Pure Foods believes its commercial feeds business currently holds the largest market share in the Philippines, which has approximately 300 registered small players and a major domestic producers such as Univet Nutrition and Animal Healthcare Co., and Universal Robina Corporation. San Miguel Pure Foods faces increasing competition from foreign feeds manufacturers and competes with five national companies and numerous regional feed mills. While San Miguel Pure Foods caters to all segments of the feeds market, the majority of its sales come from the higher value segments rather than the lower priced commodities segments.

Fresh Meats

The Philippine fresh meats industry remains highly fragmented notwithstanding attempts to modernize the industry. Consolidation of the fresh meats industry is expected to increase in the future as larger players continue to invest in new technologies.

The fresh meats business of San Miguel Pure Foods breeds, grows and slaughters hogs and cattle and produces and trades pork and beef products. It sells a wide variety of products in the Philippines under the well-recognized *Monterey* brand name. In 1993, the fresh meats business introduced Monterey neighborhood meat shops as part of the strategy to differentiate its products from those of its competitors. The fresh meats business produces its hogs using a three-site system, which separates breeding, nursery and growing into isolated facilities to minimize losses from disease outbreaks or recurrences.

The fresh meats product portfolio includes pork and beef in carcass and primals formats for franchisees, poultry distributors, the value-added meats business and the food service customers, pork and beef retail cuts sold in membership shopping club outlets operated by S&R and live hogs and cattle sold to traders. Pork, beef and lamb retail cuts and marinated products are sold in Monterey Meatshops through franchisees.

Based on the sow levels in 2012, the market share of San Miguel Pure Foods in the Philippine pork industry was estimated to be 4% in 2012, according to the Bureau of Agricultural Statistics, which placed the total sow population in the Philippines at 1.53 million in 2012.

San Miguel Pure Foods pioneered the use of the vertically controlled pork and beef production system in the Philippines, controlling the entire value chain from selection of genetic stocks to its meat shop operations. Most of the production facilities are third party owned and operated. In 2012, San Miguel Pure Foods owned two hog farms operated by third parties, and contracted with over 51 third party owned and operated farms for breeding, nursery and growing operations, owned three third party operated cattle farms, owned a slaughter plant and contracted ten third party owned and operated slaughter plants.

San Miguel Pure Foods purchases hog genetic stocks from two major multinational breeding companies, Pig Improvement Company ("PIC") and TOPIGS, and breeds its own parent stocks in company- and third party-

owned farms. San Miguel Pure Foods imports feeder cattle for beef from Australia, which currently accounts for 45% of its feeder cattle population. Boxed beef from Australia, New Zealand and Brazil is also imported to augment overall beef supply.

The fresh meats business of San Miguel Pure Foods distributes its products through a variety of channels, including supermarkets, neighborhood meat shops, poultry distributors, live sales and to the value added meats and food service businesses. It adopted a strategy focusing on the modern trade market to accelerate pork sales by introducing a Monty's supermarket meat shop in 1990 and stand-alone Monterey meat shops in neighborhoods in 1993. As of December 31, 2012, approximately 543 meat shops are in operation across the Philippines. To reduce selling costs, almost all of these meat shops were recently converted to franchised operations and certain functions, such as inventory monitoring and staffing, are now undertaken by qualified operators and franchisees. As part of its strategy to increase sales volumes, improve profitability and customer service in these shops, the fresh meats business of San Miguel Pure Foods provides marketing support to franchisees and actively seeks entrepreneurs to become franchisees.

The fresh meats business of San Miguel Pure Foods primarily competes with one large competitor, which has its own vertically controlled operations, from breeding to retailing in supermarkets. It also competes with several commercial-scale and numerous small-scale hog farms that supply live hogs to traders, who in turn supply hog carcasses to wet markets and supermarkets. While the majority of fresh meat purchases in the Philippines continue to be made in the more traditional, outdoor wet markets, San Miguel Pure Foods views its competition as being with larger producers selling in the smaller, but more profitable, modern trade channels.

Value-Added Meats Cluster

San Miguel Pure Foods value-added meats business is a key player in three segments of the Philippine processed meats industry: (a) a 61% share of the hotdogs segment with estimated market size of 103 million kilograms; (b) a 70% share of the nuggets segment with an estimated market size of 4.8 million kilograms; and (c) a 56% share of the premium canned meats segment with an estimated market size of 10.7 million kilograms based on 2012 market readings from the Nielsen and Kantar Worldpanel RTA Report. The value-added meats business of San Miguel Pure Foods produces both refrigerated meats and canned meats. Its refrigerated meat products include hotdogs, bacon, hams, nuggets and a line of local Philippine products, which are sold under the *Purefoods*, *Tender Juicy*, *Purefoods Star*, *Vida*, *Beefies*, *Magnolia*, *Tender Cuts* and *Monterey* brands. Canned products, such as corned beef, luncheon meats, sausages, and ready-to-eat viands, are sold under the *Purefoods*, *Star* and *UlamKing* brands

The value-added meats business of San Miguel Pure Foods sources most of its raw materials through the business procurement group, which strives to secure prices lower than prevailing market or published rates. The procurement group maintains a pool of San Miguel Pure Foods-accredited suppliers for local and imported raw materials, which are regularly audited for quality by a quality assurance team.

The value-added meats business of San Miguel Pure Foods operates its own processing plant in Cavite. The plant manufactures hotdogs, hams, burgers, bacon, dry sausages, meat toppings, cold cuts and nuggets. In 2012, San Miguel Pure Foods expanded its production capacity, with further expansion to be completed by the end of 2013. The Marikina plant of San Miguel Pure Foods was severely damaged by Typhoon Ondoy and is not intended to be reopened since it ceased operations in October 2009. San Miguel Pure Foods has received a substantial portion of the insurance claims for the typhoon damages at the Marikina plant. San Miguel Pure Foods has instead contracted additional toll packers to replace its capacity to pre-storm levels. To augment its production capacity and meet volume demands, the value-added meats business maintains toll manufacturing agreements with various suppliers, one of which operates a halal-accredited manufacturing facility allowing San Miguel Pure Foods to sell halal corned beef products to the Middle East and predominantly Muslim countries.

The value-added meats products of San Miguel Pure Foods are distributed by the integrated sales operations and food service business. The sales operations group generally distributes products through modern and general trade markets, as well as exports to Asia, North America and Europe. The food service business distributes products through food service operators, such as hotels, restaurants, fast food chains, food kiosks and carts. These sales groups are assisted by the logistics group, which manages planning, technical logistics services, warehousing and transportation. These distribution functions tap into a variety of distribution channels, including wet markets, supermarkets, groceries, convenience stores and sari-sari stores, as well as institutional food service clients and Filipino communities abroad.

In recent years, the value-added meats business of San Miguel Pure Foods has faced increased competition from both established local players, which are employing aggressive pricing and promotion schemes, and from new entrants to the market. To maintain its leadership position, San Miguel Pure Foods has responded by continuing innovation, increasing advertising and promotions, and introducing new product lines.

Milling Cluster

While rice has traditionally been the primary source of carbohydrates in the Philippines, bread and noodles have become increasingly popular alternatives in recent years, which have helped drive growth in the Philippine flour industry. In addition, large bakery chains are expanding rapidly in the Philippines at the expense of smaller, more traditional neighborhood bakeries. These larger chains often place greater emphasis on the quality of the flour they use, providing an opportunity for flour producers to sell customized, higher margin flour products.

San Miguel Pure Foods believes its flour business is the largest producer, seller and distributor of flour in the Philippines by volume with a 16% market share for 2012 (according to data from the Philippine Association of Flour Millers), offering a variety of flour products, including bread flour, noodle flour, biscuit and cracker flour, all-purpose flour, cake flour, whole wheat flour, customized flour, and flour premixes. San Miguel Pure Foods started the trend of using customized flours for products such as noodles and pandesal, a soft bread commonly eaten in the Philippines during breakfast. The flour products are sold under 18 brand names, and San Miguel Pure Foods enjoys strong brand loyalty among its institutional clients and other intermediaries, such as bakeries. Sales of the flour business of San Miguel Pure Foods were ₱8,425 million in 2012.

San Miguel Pure Foods owns and operates the largest flour milling facilities in the Philippines, as well as the Philippines' first flour technology center. The center develops customized flour blends and new flour-based products. San Miguel Pure Foods is expanding its pre-mix facilities to cater to growing customer needs. It owns and operates two deep water ports next to its two flour milling facilities, which are located in Mabini and Tabangao, Batangas in Luzon. The ports have a combined wheat unloading capacity of over 7,500 metric tons per day, generating substantial savings in loading, transporting and unloading costs. The principal raw material used by the flour business is wheat, the majority of which is sourced from the United States and Canada. San Miguel Pure Foods monitors worldwide wheat prices daily to determine its long-term and short-term buying strategies to control costs in its flour business.

The marketing strategy of San Miguel Pure Foods focuses on making available the widest array of differentiated flour products in the Philippine market. The flour business' sales team of approximately 30 people contact customers to determine their specific flour product needs. For customized products, the research and development team and the sales team work with the customers to develop individual formulations, and bakery technicians conduct field baking tests and demonstrations. San Miguel Pure Foods manages a nationwide distribution network servicing close to 80 dealers, who distribute flour and other bakery ingredients to major flour users as well as to small, backyard users across the Philippines. The flour business competes on price, quality and distribution, primarily with a small number of large competitors. Currently, most of the competitors produce lower priced, lower quality flours. In the future, San Miguel Pure Foods may face increased competition in the higher quality, higher margin segment and from international and regional flour producers. The flour business differentiates itself by focusing on higher quality, higher priced flours, making it more difficult for its competitors to enter those markets and compete.

Dairy, Spreads and Oils ("DSO") Cluster

The DSO business manufactures and markets a variety of bread spreads, milk, ice cream, jelly-based snacks and cooking oils generating sales of ₱6,607 million in 2012, with bread spreads make up the largest portion of this business accounting for approximately 74%. The bread spreads of San Miguel Pure Foods includes butter, refrigerated and non-refrigerated margarines and cheeses sold primarily under its *Magnolia Gold*, *Dari Creme*, *Star* and *Cheezee* brands. San Miguel Pure Foods' dairy products include flavored and unflavored milks under the *Magnolia* and *Chocolait* brands, ice cream under the *Magnolia* brand and jelly snacks and fruit jams under the *JellyAce*, *Sugarland* and *Magnolia* brands. The cooking oil products of San Miguel Pure Foods are sold under the *Magnolia* brand.

All of the raw materials required by the DSO business are sourced from third parties with approximately 51% of dairy materials such as cheese curds, rennet, casein, and milk powders imported mostly from New Zealand, and vegetable oils sourced locally.

San Miguel Pure Foods produces bread spreads products at its own facilities, including pasteurization, blending, chilling and packing for bread spreads and cooking, filling, pre-packing and end-packing for cheeses. All manufacturing activities for the milk, ice cream, jelly-based snacks and cooking oil lines are outsourced to third parties (two tollers for milk; two tollers for jelly-based snacks; and three tollers for cooking oil), who are required to meet the quality standards of San Miguel Pure Foods.

San Miguel Pure Foods manages a variety of support activities for its DSO business, including logistics, research and development, marketing, quality assurance, planning, information management and finance. The largest

distribution channel for the DSO business is supermarkets, and others include groceries, sari-sari stores, market stalls, bakeries, wholesale outlets and convenience stores. San Miguel Integrated Sales serves as the distribution arm of the DSO business for both modern and general trade channels. Food chain and other institutional distribution channels for the DSO business include bakeshops, food manufacturing companies, restaurants, hotels, pizza chains, burger joints and hospitals. The majority of the DSO business' distribution channels are in the greater Manila and Luzon areas, which have seen substantial growth in consumption. The DSO business recently began further developing regional distribution channels through exports.

In terms of domestic market share relative to volume, the DSO products of San Miguel Pure Foods represent 43% of the butter segment, 87% of the refrigerated margarine segment, 95% of the non-refrigerated margarine segment, 22% of the cheese segment and 10% of the ice cream segment, based on 2012 statistics from Nielsen. San Miguel Pure Foods DSO business faces intense competition in many of its product segments, particularly milk and cheese including from multinational companies such as Kraft, Nestle, Unilever and New Zealand Milk, as well as domestic companies such as San Pablo. In recent years, many of the competitors of San Miguel Pure Foods have increased advertising and promotional spending to protect their market shares.

Emerging Businesses Cluster

Coffee

The coffee business of San Miguel Pure Foods in the Philippines is a joint venture with a Singaporean partner, Super Coffee Corporation Pte. Ltd. ("SCCPL"), and is 70% owned by San Miguel Pure Foods. The joint venture commenced operations in 2005 and sells coffee products under the *San Mig Coffee* brand. In 2012, the coffee business of San Miguel Pure Foods had sales of ₱952 million and an estimated market share of 4% by volume in the Philippine coffee mix market according to Nielsen. All of the coffee business' raw materials procurement, manufacturing and pre-packing are handled by the Singaporean partner of San Miguel Pure Foods, with certain subsidiaries of SMC managing repacking and distribution in the Philippines.

Food Services

The food services business of San Miguel Pure Foods was established in 2002 and is the largest food services provider in the Philippines. It distributes and markets generic and customized food service products, including value-added meats, fresh meats, poultry, dairy, oil, flour and coffee. The food service business of San Miguel Pure Foods receives a percentage of the selling price of the products as a development fee. The business' key strategies include selling customized solutions, direct marketing to its customers and focused relationship management. The food service business of San Miguel Pure Foods had sales in 2012 of ₱397 million.

Indonesia Regional Business

The business of San Miguel Pure Foods in Indonesia is a joint venture with Penderyn formed in 1995 that produces a variety of halal-certified and non-halal processed meats for the Indonesian market. The joint venture is 75.0% owned by San Miguel Pure Foods. The Indonesian business of San Miguel Pure Foods had sales in 2012 of ₱693 million, and its retail value share of the Indonesian chilled processed meats market was approximately 30% by volume in 2012, according to Euromonitor.

Vietnam Regional Business

The Vietnam food business is a joint venture between San Miguel Pure Foods, which holds 51%, and Hormel, which holds 49%. San Miguel Pure Foods acquired its 51% interest in the Vietnam business from SMC in July 2010, prior to which San Miguel Pure Foods provided management services to the Vietnam food business. The Vietnam food business primarily engages in live hog farming and producing feeds and processed meats and generated sales of ₱2,140 million in 2012.

PACKAGING BUSINESS

The packaging business of SMC began operations in 1938 with the establishment of a glass plant that supplied glass bottles for the beer and non-alcoholic beverage products of SMC. The packaging business of SMC is conducted through SMYPC, a joint venture of SMC and NYG, one of the largest glass and plastic packaging corporations in Japan. SMYPC owns and operates 17 domestic packaging facilities, while SMYPIL is also 65% owned by SMC and 35% owned by NYG. SMYAC is a domestic glass packaging subsidiary and is 60% owned by SMC and 40% owned by NYG. In addition, SMC manufactures paper corrugated cartons through Mincorr, a wholly-owned subsidiary of SMC.

The Packaging Group has one of the largest packaging operations in the Philippines with diversified businesses producing glass, metal, plastic, paper, flexible, PET and other packaging products. The Packaging Group is a major source of packaging products for the other business segments of SMC. The Packaging Group also supplies packaging products to customers in the Asia-Pacific region, the United States, Africa, Australia and the Middle East, as well as to major multinational corporations in the Philippines, including Coca Cola Bottling Company, Nestle Philippines and Pepsi Cola Products Philippines. In 2012, the packaging business had sales of ₱15 billion, of which approximately 46% were sales from international markets.

Philippine Packaging Industry

According to the data from Euromonitor, the total Philippine Packaging sector for beverage applications grew at a compounded growth rate (“CAGR”) 3.7% from 2008 to 2012, while for food applications, the CAGR was 2.9%.

The usage growth rate for glass containers, (which is the largest business of the Packaging Group) for beverage applications has been 3.8% while that for food applications registered at 2.4% from 2008 to 2012. Although the growth of glass containers may be tempered by the increasing popularity of lightweight, unbreakable and more affordable packaging types such as PET and flexibles (which the Packaging Group also produces), the glass packaging industry will likely benefit from creation of a free trade area amongst ASEAN nations. Among the likely positive impact of the free trade area will be the ability for container manufacturers, such as the Packaging Group, to expand their business in ASEAN economies.

PET bottles for beverages has shown some of the fastest growth rates in the 2008 to 2012 period as this packaging format recorded an average annual growth of 4.4%. The Packaging Group has large available capacities and ready know-how to exploit future prospects in this packaging format.

Flexible packaging is considered to be the most affordable packaging type and is therefore used by many consumer products to capture mass markets. It is used extensively in confectionery, dried processed food and sweet and savory snacks and has captured brand manufacturers of canned/preserved food and baby food. Flexible packaging for food grew at 3.0% over the 2008 to 2012 period while that for beverages grew by 1.3%.

Folding cartons used for food grew by an average growth of 3.3% over the same five-year period. Metal packaging for beverages has shown very slow progress, with an average growth rate of only 0.8% from 2008 to 2012.

Competitive Strengths

The Packaging Group believes that its strengths include the following:

Market leader. The Packaging Group is a market leader in all its product formats in the domestic packaging industry, producing glass, plastics, metal, metal caps, aluminum cans, composites and woven products.

Widest portfolio of packaging products. The Packaging Group provides customer with various packaging format options that can cater to different market segments. Likewise, its ability to offer primary, secondary and tertiary packaging ensures the alignment of all packaging requirements.

State-of-the-art manufacturing facilities. The Packaging Group maintains state-of-the-art manufacturing facilities including the only food grade PET recycling facility in Asia and best practices in manufacturing and quality procedures.

Synergies from partnerships with key global packaging companies. The Packaging Group gains synergies from its partnerships with global packaging players such as NYG, Fuso Machine and Mold Mfg. Co., Ltd., Kaito Chemical Industry Co., Ltd., United Resource Recovery Corporation and Can-Pack S.A.

Business Strategies

The strategies of the Packaging Group include the following:

Network and Client Optimization. The Packaging Group intends to optimize and leverage on its significant regional network of facilities and alliances as a gateway to enter into new markets. It is also evaluating opportunities with its international clientele on potentially providing packaging services to them in markets where these customers have a presence and are new to the Packaging Group. There is also a focus on entering into longer term contracts with key customers to enhance earnings stability.

Product Diversification. The Packaging Group plans to enter new markets and market segments with new products such as personal care (plastic tubes), pharmaceuticals (plastic pharma bottles), semi-conductors and

electronics (anti-static bags), paint (pails), food tubs, lug caps, deep draw caps, slim cans, PET wide-mouth jars and various converted can ends.

Marketing Environmentally Friendly Products. The Packaging Group expects the future consumer trend to move towards environmentally friendly products and environmentally sound manufacturing systems. Hence, the Packaging Group plans to increase investments into eco-friendly facilities, processes and products such as the PET recycling plant, use of scrap laminates as fillers in pallets, toluene-free flexible packaging and accreditation with various international standards and agencies. In recent years, the Packaging Group has made significant investments to improve and upgrade its manufacturing facilities to a standard higher than established government regulations. For example, the Packaging Group acquired an electrostatic precipitator, a pollution-abating device that cost more than ₱100 million.

Selected operating data for the packaging business is provided below for the periods indicated:

	For the year ended December 31,		
	2010	2011	2012
	(₱ in millions, except percentages)		
Sales	23,440	24,114	24,460
Gross profit	5,948	6,194	6,594
Gross profit margin ⁽¹⁾	25.4%	25.7%	27.0%
EBITDA ⁽²⁾	3,840	4,115	4,145
EBITDA margin ⁽³⁾	16.4%	17.1%	16.9%
Net income before tax	1,799	2,025	1,607
Net income before tax margin ⁽⁴⁾	7.7%	8.4%	6.6%

Notes:

(1) Gross profit margin is calculated by sales less cost of sales divided by sales.

(2) EBITDA is calculated as net income before: income tax expense, net financing charges (interest income net of interest expense), extraordinary or exceptional items, foreign exchange losses (gains), marked-to-market currency losses (gains) and depreciation and amortization and impairment losses.

(3) EBITDA margin is calculated by EBITDA divided by sales.

(4) Net income before tax margin is calculated by net income before income tax divided by sales.

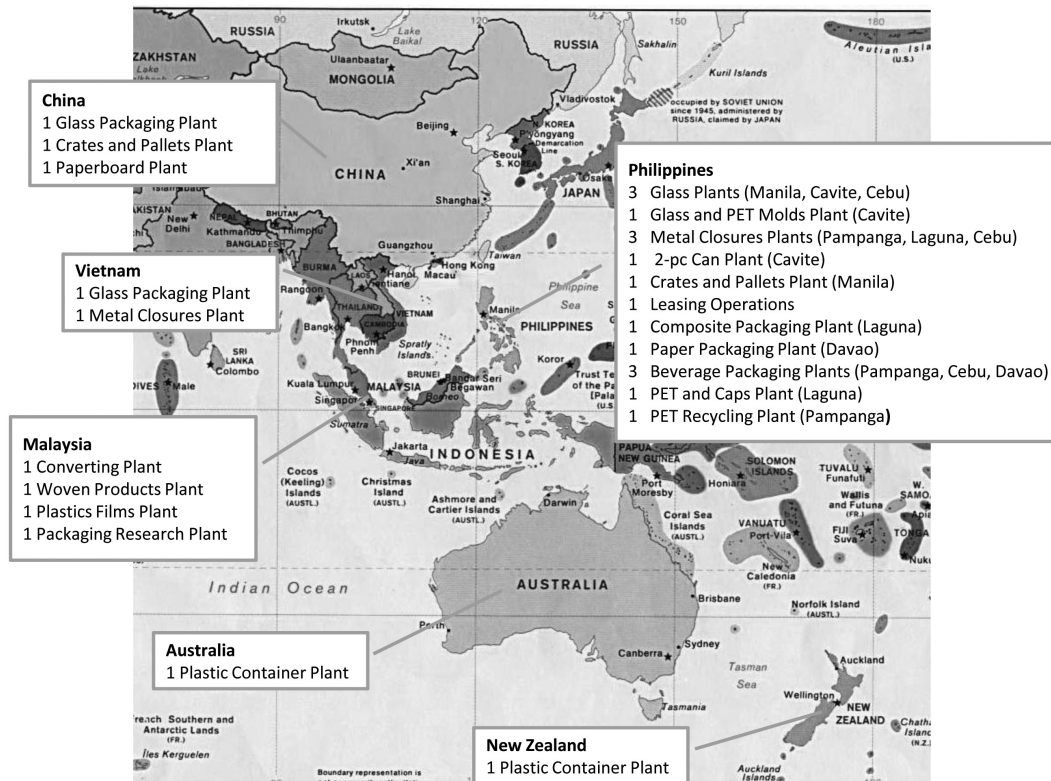
A description of the businesses of the Packaging Group is as follows:

- **Glass:** This business is the largest supplier in the glass packaging industry segment and serves many of the country's leading beverage, food and healthcare companies according to Company data.
- **Metal:** The metal business is the second largest business in the Packaging Group. It manufactures metal caps, crowns, resealable caps and two piece aluminum beverage cans for a wide spectrum of industries that include beer, soft drinks and food.
- **Composites/Flexible Packaging:** The composites/flexible packaging business manufactures flexible packaging such as anti-static/electrostatic discharge bags, plastic films, industrial laminates, trademarked Envirotuff radiant barrier and woven bags. Its customers include companies in the food, beverages, personal care, chemical and healthcare industries.
- **PET:** The PET business produces PET preforms and bottles, plastic caps and handles, and offers filling services, serving the beer, liquor, non-alcoholic beverages, food, pharmaceutical, personal care and industrial applications industries.
- **Paper:** The paper packaging business produces corrugated cartons and partition boxes. In addition, SMC also manufactures corrugated cartons and other paper-based packaging products through its wholly owned subsidiary, Mincorr. The paper packaging business serves a broad range of beverage, food and agricultural industries.
- **Plastics:** The plastics business produces bread and food trays, industrial containers, crates, pallets, poultry flooring, pails and tubs to companies in the beer and beverages industries as well as chicken and agricultural industries.

Production

The Packaging Group owns and operates three glass container packaging plants, a glass and PET mold plant, three metal closures packaging plants, one two-piece can plant, one plastics packaging plant, a leasing operations, one composites packaging plant, one paper packaging plant, four PET packaging plants, and a PET recycling plant. All plants are strategically located throughout the Philippines. It also owns and operates eleven overseas packaging facilities: three in China (producing glass, plastic and paperboard packaging products); two in Vietnam (glass and

metal); four in Malaysia (composite, plastic films, woven and a research center); one in Australia (plastic); and one in New Zealand (plastic). The plant facilities of the Packaging Group are shown below:



PROPERTY DEVELOPMENT

Established in 1990 initially as the corporate real estate arm of SMC, SMPI is currently an established developer of residential and commercial real estate in the Philippines. SMPI is 98.5% owned by SMC and is primarily engaged in the development, sale and lease of real property. SMPI is also engaged in leasing and managing the real estate assets of SMC. The development track record of SMPI includes economic to middle-income housing (Buenavista Homes in Cebu and The Legacy in Parañaque City), high end residential (San Miguel Village) and landmark commercial buildings (SMC corporate headquarters and the Ortigas Center). SMPI had net tangible assets of ₱19,817 million as of December 31, 2012.

FUEL AND OIL

SMC operates its fuel and oil business through its 68.3% ownership of the common stock of Petron. Petron refines crude oil and markets and distributes refined petroleum products in the Philippines and Malaysia. In the Philippines, Petron is the largest integrated oil refining and marketing company, with an overall market share of 38.5% of the Philippine oil market in terms of sales volume based on industry data from the DOE as of December 31, 2012. Petron had a 16.6% share of the Malaysian retail market as of December 31, 2012, according to Metrix Research estimates, the market research consultant appointed by Malaysian retail market participants to compile industry data.

Through its network of 2,015 retail service stations in the Philippines as of December 31, 2012, Petron sells gasoline, diesel and kerosene to motorists and to the public transport sector. Petron also sells its liquefied petroleum gas (“LPG”) brands *Gasul* and *Fiesta Gas* to households and other consumers through its extensive dealership network. Petron also manufactures lubricants and greases, which are sold through its service stations and sales centers. Petron owns and operates a fuels additive blending plant in the Subic Bay Freeport Zone in the Philippines, which has a tolling agreement with Innospec, Limited (“Innospec”), a global fuel additives supplier. Regional customers of Innospec and Petron’s own requirements are served from the output of the Subic additive blending plant.

In recent years, Petron has diversified into petrochemicals, adding a mixed xylene recovery unit to the Limay Refinery complex in 2000 and a propylene recovery unit in 2008. Its benzene-toluene extraction unit became operational in May 2009. In March 2010, Petron acquired a 40% stake in Petrochemical Asia (Hong Kong) Ltd (“PAHL”), owner of Philippine Polypropylene Inc. (“PPI”), which was diluted to 33% when PAHL issued new

shares to another investor in June 2010. In December 2012, Petron converted certain loans it had made to PAHL into additional equity, which increased its stake in PAHL to 45.9%. PPI owns a polypropylene plant located in Mariveles, Bataan in the Philippines. On March 30, 2012, Petron completed its acquisition of the integrated downstream business of ExxonMobil in Malaysia for an aggregate purchase price of US\$577.3 million. The acquired assets and operations form an integrated downstream business. With this acquisition, Petron has extended its portfolio of oil refining and marketing businesses outside the Philippines. Petron now owns and operates the 88,000 bpd Port Dickson Refinery, eight product terminals and a network of approximately 555 retail service stations in Malaysia, which are being rebranded under the Petron brand, a process that is expected to be completed in 2014. The acquisition is providing Petron with potential synergies in terms of manpower skills and technical knowledge, as well as potential product swap arrangements with suppliers who operate in both the Philippine and Malaysian markets. As of December 31, 2012 the acquired entities had a combined total asset value of ₱59.9 billion (based on an exchange rate of RM 1.00 = ₱13.4).

The products of Petron are primarily sold to customers in the Philippines and Malaysia, but, in line with its efforts to increase its presence in the regional market, Petron also exports various petroleum products and petrochemical feedstocks, including low-sulfur waxy residue (“LSWR”), high-sulfur fuel oil, naphtha, mixed xylene, benzene, toluene and propylene, to customers in the Asia-Pacific region. Petron also engages in the businesses of insurance, marketing and leasing, and intends to support its core business through further investments, such as the upgrading and enhancement of its refineries, primarily the Limay Refinery pursuant to the RMP-2, the construction of a new cogeneration power plant for the Limay Refinery and continued retail network expansion.

Philippine Petroleum Industry

The Philippine oil industry had been deregulated since 1998 and is currently dominated by Petron, and two other oil companies — Shell and Caltex — with more than 100 industry market participants. Petron and Shell operate the only refineries in the country. The rest of the industry market participants are importers of finished petroleum products or purchase finished petroleum products from other market participants in the local market.

The petroleum industry is heavily affected by volatile crude prices, strict environmental requirements and a more value-conscious breed of consumers. While pricing remains a primary driver of sales in all sectors, a shift towards total customer solutions has also been noted. Based on the exchange data of DOE, the country’s total petroleum demand almost stood flat in the past 10 years. Increasing fuel prices put pressure on demand, largely noted in fuel oil, with users shifting to alternative energy sources such as coal.

Deregulation saw the entry of more than 100 other industry market participants, rendering the petroleum business more competitive. In the reseller sector, competition has shifted from the major oil players to the growing new player sector. According to the DOE, the count of new player outlets has been increasing from 695 in 2001 to about 1,900 in 2012. New players collectively built around 200 outlets in 2012, compared with major oil players’ estimated combined 270. Aggressive expansion of new players is fueled by attractive dealer package, healthy gasoline margins, and flexible product sourcing. In the industrial sector, investments such as depot construction continue to pour in from all players aimed at increasing market share and tapping new markets.

Malaysian Petroleum Industry

The fuel business in Malaysia is regulated by the Malaysian government. The Malaysian government regulates the pricing structure through the automatic pricing mechanism (“APM”), pursuant to which it mandates (i) the prices of certain refined petroleum products, (ii) quotas and (iii) certain fixed amounts for marketing, transportation and distribution costs in relation to the subsidy structure.

According to the National Energy Balance, the final consumption of petroleum products in Malaysia in 2010 totaled 24,403 thousand tons of oil equivalent (“ktoe”). Out of the final consumption in 2010, the largest components were motor petrol (39.2%), diesel (34.4%) and LPG (12.0%). In terms of regional breakdown, nearly 85% of petroleum product sales were in Peninsular Malaysia, with Sabah and Sarawak accounting for the remainder.

Over the last decade, Malaysia has been a net importer of gasoline, predominantly from Singapore. It has also been a net importer of diesel and fuel oil. Conversely, Malaysia has been a net exporter of certain products, including LPG, naphtha and jet fuel/kerosene. Exports have predominantly been to countries in Asia, including India, Japan, Singapore, South Korea and Thailand.

The oil industry is dominated by Shell and Petronas, followed by Petron.

Competitive Strengths

Petron believes that its principal competitive strengths include the following:

Operations in the Philippine and Malaysian markets, which have favorable industry dynamics. Petron operates as an integrated oil refining and marketing company in the Philippines and Malaysia, both of which Petron believes have favorable oil industry dynamics. The Philippines operates under a free market scheme with movements in regional prices reflected in the pump prices on a weekly basis. Malaysia, on the other hand, operates under a regulated environment and implements an automatic pricing mechanism that provides stable returns to fuel retailers. Both economies are projected to experience strong economic growth to 2015, according to Economist Intelligence Unit. This growth is expected to contribute to increased domestic demand for refined products and lead to a potential supply shortfall. As both the Philippines and Malaysia are net importers of finished petroleum products, Petron believes it is well-positioned to benefit from this supply shortfall with its production capacities of 180,000 and 88,000 bpd in the Philippines and Malaysia, respectively, giving it a significant competitive advantage against other competitors.

Market leadership in the Philippine downstream sector. With an overall market share of approximately 38.5% of the domestic oil market based on industry data as of December 31, 2012, Petron believes it is the leader in the Philippine oil industry, ahead of the other two major oil companies operating in the country. Petron also believes it has the largest sales volumes in the retail, industrial and LPG market segments. Based on the DOE industry data for 2012, it has the following approximate market shares: 34.5% of the retail trade market; 41.7% of the industrial market; 41.8% of the LPG market; and 37.5% of the lubricants and greases market. In the Philippines, Petron owns and operates the largest oil refinery complex. With 180,000 bpd capacity, the refinery of Petron has a capacity that is 70,000 bpd higher compared to the only other operating refinery. Petron believes it has the most extensive distribution system in the Philippines, which allows it to operate and serve its customers across the country. This distribution system covers a network of over 30 depots, terminals, and airport installations that reaches most key points of the Philippines. Given the challenges of distribution across the Philippine archipelago, this capability plays a significant role in securing the leading position of Petron in the Philippines. Since 2011, Petron has focused on expanding its distribution network to accommodate increasing demand across the country, and will continue to invest to expand its network. The multisectoral approach of Petron to marketing through retail, LPG and bulk industrial customer operations also plays a large role in its unmatched success in the Philippines downstream sector. As of December 31, 2012, Petron maintains 2,015 service stations nationwide, more than any other market participant, and intends to grow this number to serve the increased production from RMP-2. Petron believes it is the leader in the LPG segment with more than 800 branch stores. Petron's industrial sales covers more than 1,100 direct industrial accounts, including the National Power Corporation of the Philippines.

Established position in the regulated Malaysian market. Petron has recently acquired an established position in the Malaysian downstream sector through its acquisition of ExxonMobil's downstream business in Malaysia, which has a recognized health, safety and environmental track record. This provides both geographic diversification to its portfolio, an additional platform to expand its business and added stability to its operations. In Malaysia, the 88,000 bpd of Petron refinery represents 16.4% the total refining capacity of Malaysia. In addition, the acquired marketing and distribution infrastructure in Malaysia also puts it in a position to capture a growing share of the market. The network of Petron in Malaysia includes 555 service stations, 262 convenience stores and eight product terminals in both Peninsular and East Malaysia as of December 31, 2012. Petron also has presence in the aviation business, with a 20% ownership of a multi-product pipeline to Kuala Lumpur International Airport. Likewise, Petron participates in the 12kg and 14kg bottled LPG segment with a market share of 12.3% as of December 31, 2012, according to Metrix Research. In addition, Malaysia is a regulated market with subsidies, quotas and the automatic pricing mechanism, which provides for a fixed oil company margin and a fixed operating cost recovery. This regulated environment provides stability to the Malaysian operations of Petron.

Experienced management team and employees. Petron has an experienced team of managers with substantial relevant experience in refining operations and development of service stations. The management team of Petron in the Philippines and Malaysia has more than 20 years of management experience while average tenure of employees in Petron is approximately 14 years for the Philippines and 12.5 years for Malaysia. The management team has extensive experience in the oil industry and has successfully managed Petron through periods of crisis and instability in the Philippines as well as through the various changes Petron has undergone, including changes in ownership, privatization and industry deregulation. In addition, Petron has a team of employees skilled in managing the various aspects of its business, including a highly experienced management team at the Limay Refinery, a focused sales and marketing team, which includes a group that has years of experience in service station engineering and construction, and a research and development team that has overseen years of product

development and production process improvement. Petron is also committed to the development of its employees by adopting on-going training and development programs to ensure that operations will be run by well-equipped and capable employees.

Business Strategies

The principal strategies of Petron are set out below.

Further increase its market share in the Philippines and in Malaysia. Petron is the largest integrated oil refining and marketing company in the Philippines, with an overall share of approximately 38.5% of the Philippine oil market in terms of sales volume based on industry data as of December 31, 2012 from the DOE. Petron is also a strong market participant in Malaysia. According to Metrix Research estimates, as of December 31, 2012, Petron has a 16.6% market share of the Malaysian retail segment. Petron intends to utilize its leading market position and extensive distribution network as a platform for maximizing its sales potential. It believes that such platform is an advantage of Petron over most of its competitors in the Philippines. Petron believes that both markets are still underserved and intends to grow its market position by: (i) increasing its retail outlets for fuels and LPG to capture industry growth and improve market penetration; (ii) introducing new products with differentiated and superior qualities; (iii) developing and expanding its logistical facilities, including the addition of new aviation facilities in tourist destinations; (iv) building more LPG re-filling and auto-LPG facilities; (v) continuing to expand its non-fuel businesses by leasing additional service station spaces to food chains, coffee shops and other consumer services to provide “value conscious” customers with a one-stop full service experience; and (vi) intensifying its dealer and sales personnel training to support the retail business and continuing service station network expansion of Petron. In line with these plans, Petron intends to continue its aggressive service station expansion program in the Philippines and rebranding and refurbishing its service stations in Malaysia. In addition, Petron seeks to maintain and further develop its significant position in both markets by reinforcing business relationships with existing customers such as through enhanced loyalty programs in the Philippines and Malaysia. These loyalty programs are aimed at maximizing patronage of the service stations and allied businesses of Petron.

Focus on production of high margin refined products and petrochemicals. Over the years, Petron has made significant investments in conversion and petrochemical facilities and is focused on increasing production of White Products and petrochemicals while minimizing production of low margin fuel products. In recent years it has focused increasingly on the production of new higher margin petrochemical feedstocks, such as propylene, mixed xylene, toluene and benzene, and shifted production from lower margin fuel oils to higher margin products. This is a core area of focus for Petron going forward and is a direct result of proactive investment in high margin products and petrochemicals. At the Limay Refinery, in order to increase its ability to produce more high margin products Petron has invested in RMP-2, a US\$2 billion turn-key project expected to be completed in 2014. The project involves upgrades to the Limay Refinery by adding new facilities to increase the capability of Petron to convert low-margin fuel oil into a broader range of White Products and petrochemical products and process heavier, more sour (and therefore lower cost) crudes. Petron expects that post completion of RMP-2, the Limay Refinery will run at close to full capacity, with production expected to increase from an average of 100 thousand bpd currently to 170-177 thousand bpd. The refinery will also be able to produce petcoke, which may be used as fuel for the power plant, lowering power generation costs of Petron. The upgrade is expected to increase sales and reduce costs and place the utilization, processing and energy efficiency of the Limay Refinery at par with more advanced refineries in the region and improve its competitiveness. Once fully implemented, RMP-2 will make Petron the only oil company in the Philippines capable of producing Euro IV-standard fuels, the global clean air standard. As of December 31, 2012, approximately half of the engineering design, procurement activities and construction had been completed. Petron intends to continue to evaluate opportunities for increasing its production of downstream petrochemicals, such as the processing of propylene, ethylene, xylene, benzene or toluene into derivatives or finished products.

Continue investments to increase operational efficiencies and widen market reach. Petron has undertaken a number of strategic projects aimed at increasing operational efficiency and profitability. In addition to RMP-2 and the expansion of its service station network, Petron is constructing a new cogeneration power plant for the Limay Refinery to replace some of the Limay Refinery’s existing turbo and steam generators. The new cogeneration power plant will utilize more efficient technology and generate power at lower costs. The new cogeneration power plant will have a total of 140 MW power generation capacity and 800 metric tonnes per hour (“MTH”) steam generation capacity, which will completely fulfill the Limay Refinery’s current and expected future electricity and steam requirements. The first phase for the cogeneration power plant, which consists of two boilers and two circulating fluidized boilers, is expected to be commissioned in the first half of 2013. The second phase, which is expected to be completed in 2014 is expected to fulfill all of the electricity and steam requirements of the Limay Refinery, including the increased demand arising from RMP-2. The power plant will

initially utilize coal as fuel and will switch to petcoke once the Limay Refinery commences its planned petcoke production in 2014. The project cost is estimated at approximately US\$500 million. These initiatives are intended to reduce costs and increase the reliability of power and steam supply, sourcing flexibility and cost efficiency of the Limay Refinery. Petron also intends to pursue cost-efficient opportunities to enhance efficiency and reduce production costs through supply chain improvements and enhancements to its existing facilities. In particular, Petron expects to increase the efficiency of its existing supply chain through a range of initiatives, including: (i) optimizing its crude oil mix to produce more profitable products from the existing refining configuration and expanding its crude oil supply sources in addition to its major crude oil suppliers; (ii) reducing inventory levels in the Philippines by sourcing feedstock from suppliers located near the Limay Refinery; (iii) enhancing receiving and storage facilities to attain greater sourcing flexibility and support new growth areas; (iv) managing crude oil freight costs and availability of terminal-compliant vessels with contracts of affreightment that guarantee cost competitiveness with the spot market; and (v) reducing distribution costs through rationalization of the depot network, joint operations with other companies and optimized utilization of its marine and tank truck fleet. Petron also expects to continue utilizing operational synergies with network, products and services of SMC.

Selective synergistic acquisitions. In addition to organic growth, Petron will continue to consider selective opportunities to expand both within and outside the Philippines through strategic acquisitions consistent with its focuses on the Philippine market and creation of operational synergies. Petron will consider any acquisition opportunity carefully, and any potential acquisition would undergo extensive review and evaluation procedures to ensure that it would be beneficial to the business of Petron as a whole. For example, in March 2010, Petron acquired a 40% stake in PAHL, which was subsequently diluted to 33% in June 2010 and increased to 45.9% in December 2012. PAHL owns PPI, which owns a polypropylene plant located approximately five kilometers from the Limay Refinery. The polypropylene plant's primary feedstock, propylene, is supplied by the Limay Refinery. Through its investment in PAHL, Petron shares in the incremental value derived from converting propylene into polypropylene resin. In addition, on March 30, 2012 Petron completed its acquisition of ExxonMobil's downstream business in Malaysia, extending its portfolio of oil refining and marketing businesses outside the Philippines.

Selected operating data for the business of Petron are set forth in the table below for the periods indicated:

	For the year ended December 31,		
	2010	2011	2012
	(P in millions, except percentages)		
Sales	229,094	273,956	424,795
Gross profit	19,814	23,130	18,819
Gross profit margin ⁽¹⁾	8.6%	8.4%	4.4%
EBITDA ⁽²⁾	15,968	18,553	14,623
EBITDA margin ⁽³⁾	7.0%	6.8%	3.4%
Net income before tax	10,299	11,121	2,950
Net income before tax margin ⁽⁴⁾	4.5%	4.1%	0.7%

Notes:

(1) Gross profit margin is calculated by sales less cost of sales divided by sales.

(2) EBITDA is calculated as net income before: income tax expense, net financing charges (interest income net of interest expense), extraordinary or exceptional items, foreign exchange losses (gains), marked-to-market currency losses (gains) and depreciation and amortization and impairment losses.

(3) EBITDA margin is calculated by EBITDA divided by sales.

(4) Net income before tax margin is calculated by net income before income tax divided by sales.

Production Facilities

Philippines

Petron owns and operates a petroleum refinery complex located in Limay, Bataan, which has a crude distillation capacity of 180,000 bpd. The Limay Refinery has three crude distillation units, a vacuum pipestill unit, a petrofluidized catalytic cracking unit, a propylene recovery unit, a continuous catalyst regeneration platformer unit, a powerformer unit, two naphtha hydrotreaters, two LPG treaters, an isomerization unit, a mixed xylene recovery unit, a benzene-toluene extraction unit, a kerosene merox treater, two gas oil hydrotreater units, a sulfur recovery unit, waste water treatment facilities, eight steam generators, five turbo generators, flare and safety relieving facilities, bulk asphalt receiving facilities, several crude storage tanks, as well as several refined petroleum products storage tanks. The refinery also has its own piers and two offshore berthing facilities, one of which is used for receiving crude and can accommodate very large crude carriers.

The Limay Refinery is capable of producing a broad range of petroleum products such as LPG, gasoline, jet fuel, diesel and fuel oil. In 2000, the Limay Refinery expanded into petrochemical production with the commercial operation of its mixed-xylene plant. The Limay Refinery started producing propylene in 2008 with the commissioning of its propylene recovery unit, which has a demonstrated capacity of 130,000 tons per year of polymer-grade propylene. The benzene-toluene extraction became operational in May 2009 and is designed to produce benzene and toluene at respective capacities of 24,000 and 158,000 tons per year.

In early 2011, PPI, in which Petron currently has a 45.9% indirect interest, commissioned a rehabilitated polypropylene plant in Mariveles, Bataan, to capture the incremental margin from converting the Limay Refinery's propylene production into polypropylene. The facility has the capacity to produce 160,000 metric tons of polypropylene resin annually, and Petron has entered into an offtake agreement with PPI pursuant to which PPI is entitled to purchase 100% of the propylene production of the Limay Refinery.

Petron also completed a fuel additive blending plant in the Subic Freeport Zone in July 2008 with a capacity of 12,000 MT a year, which serves the fuel additive requirements of a leading global additives manufacturer in the Asia-Pacific region and operates as that manufacturer's exclusive blender for customers. Currently, Petron is upgrading its refinery referred to as RMP-2 and is constructing a cogeneration plant.

Malaysia

In Malaysia, Petron owns a petroleum refinery complex located in Port Dickson, Negeri Sembilan. The Port Dickson Refinery has a crude oil distillation capacity of 88,000 bpd. Its facilities include a crude oil distillation unit, a naphtha hydrotreating unit with a processing capacity of 26,000 bpd, two semi-regeneration reformer units with a combined processing capacity of 19,000 bpd and a kerosene hydrotreating unit with a processing capacity of 12,000 bpd. The Port Dickson Refinery also has waste water treatment facilities, a steam generator, a cooling water plant, flare and safety relieving facilities, five crude oil storage tanks with a total capacity of approximately one million barrels, 20 refined petroleum products storage tanks and five spheres for LPG storage with a total capacity of approximately 1.1 million barrels. The Port Dickson Refinery produces a range of products, including LPG, gasoline, jet fuel, diesel and LSWR. With the exception of LSWR, these products are intended to meet domestic demand in Malaysia. Petron exports its LSWR under a term contract with Concord Energy. Crude oil for the Port Dickson Refinery (predominantly light low-sulfur crude oil) is received at the Port Dickson Refinery by means of a single buoy mooring ("SBM") and crude pipeline facilities that are jointly owned with Shell through an unincorporated joint venture. The SBM is operated by Shell, and Petron shares the operating costs equally with Shell. Petron also pays a levy of one-third of the overhead and administrative charges incurred by Shell in connection with the operation of the SBM.

Refining Process and Quality Improvement Initiatives

The Limay Refinery

Petron has been implementing various programs and initiatives to achieve key performance indices on reliability, efficiency and safety in its refinery. These programs include the Reliability Availability and Maintenance ("RAM") program and the profitability improvement program ("PIP"), which were developed and implemented in coordination with KBC Market Services ("KBC"), an international consultant. The RAM program resulted in improved operational availability and lower maintenance cost through higher plant reliability and a longer turnaround cycle of four to five years from the previous two years. The PIP likewise significantly improved White Products recovery, particularly diesel and LPG.

The Continuous Improvement Program of Petron was one of the finalists for the 2008 Peoples Program of the Year award sponsored by the People Management Association of the Philippines. In 2009, The Limay Refinery achieved its Integrated Management System ("IMS") certification issued by TÜV-SÜD-PSB, an internationally recognized certification and inspection body. The IMS is an integration of three management systems: (1) Quality ISO 9001:2000, (2) Environment ISO 14001:2004, and (3) Health and Safety OHSAS 18001:2007. The benefits of an IMS for the Limay Refinery include: standardized and more systematized quality, environmental, health and safety work procedures, instructions and practices; improved quality, productivity, environment, health and safety performance through continual improvement and compliance with legal requirements; customer satisfaction; and hazard and injury free working environment, and environmentally friendly operations.

The Port Dickson Refinery

The Port Dickson Refinery utilizes various management systems in support of its operations. These systems include the safety management system ("SMS"), the loss prevention system ("LPS"), the reliability management

system and additional plant optimization initiatives for improved plant efficiency. The Port Dickson Refinery adopted the LPS to prevent or reduce losses and incidents using behavior-based tools and other safety management techniques. The Port Dickson Refinery's SMS provides a structured approach to the management of risks related to safety, security, health and the environment ("SSHE") and compliance with local SSHE regulations and laws. The Port Dickson Refinery has accumulated more than ten consecutive years without any lost-time injury for employees or contractors and has received an award from the Malaysian Society for Occupational Safety and Health ("MSOSH"), as well as the Prime Minister Hibiscus Award for good environmental performance. To increase plant reliability, the Port Dickson Refinery adopted the reliability management system, which utilizes a risk-based equipment strategy and aims to improve mechanical efficiency through routine work planning, scheduling and execution. The Port Dickson Refinery continuously seeks improvement in the areas of process optimization, flaring, oil loss and energy conservation through the use of advanced process computer control and an integrated plant information system.

Operating Sites

Petron owns the largest integrated petroleum refinery complex in the Philippines located in Limay, Bataan. It operates a network of terminals and depots as bulk storage and distribution points throughout the Philippines, as well as LPG plants in its Pasig terminal, San Fernando depot and Legaspi depot and a number of terminals in Malaysia. Its airport installations serve the fuel requirements of the airline industry and other aviation accounts. Petron moves its products, mainly by sea, to more than 30 depots, terminals and airport installations situated throughout the Philippines, representing the most extensive distribution network in the Philippines. The network comprises 12 depots and terminals in Luzon, eight in Visayas and seven in Mindanao, as well as two airport installations in Luzon, one in Visayas and two in Mindanao. Depots and terminals have marine receiving facilities, multiple product storage tanks for liquid fuels and LPG, drummed products storage, and warehouses for packaged products, such as lubricants and greases.

Petron's Malaysian distribution operation network includes eight product terminals (of which seven are active and one is idle) located in strategic locations across Peninsular and East Malaysia. The Port Dickson terminal is located at the Port Dickson Refinery, and the other terminals are located near major fuel product market areas.

Petron entered into commercial leases with the Philippine National Oil Company ("PNOC") for parcels of land occupied by its Limay Refinery, depots, terminals and certain of its service stations. The lease agreements include upward escalation adjustment of the annual rental rates. In 2009, Petron renewed its lease with PNOC (through New Ventures Realty Corporation ("NVRC")) for the continued use of the Limay Refinery land for 30 years starting January 1, 2010 (renewable upon agreement of the parties for another 25 years). Petron is currently in negotiations with PNOC for the early renewal of leases for 22 terminals, depots and sales offices and 68 service stations that will expire in August 2018. Expenses relating to the PNOC leases paid directly to PNOC and through NVRC amounted to ₱160 million in 2011 and ₱161 million in 2012.

Petron leases 103 parcels of land for service stations and depots from NVRC. Total expenses relating to the NVRC leases amounted to ₱308.8 million in 2011 and ₱288.0 million in 2012.

Petron also leases land for its service stations from third parties. As of December 31, 2012, there were leases covering 604 service stations: 438 in Luzon, 82 in Visayas and 84 in Mindanao. Payments under these leases amounted to ₱494.4 million in 2011 and ₱553.3 million in 2012.

In Malaysia, the land on which Petron's retail service stations are based is either owned by Petron or leased from third parties. As of December 31, 2012, Petron owned 161 parcels of land for service stations and leased 273 additional parcels of land for its service stations from third parties. Payments under these leases amounted to approximately RM 15 million in 2011 and approximately RM 6 million in 2012. The Port Dickson Refinery occupies a 604 acre site. Petron holds freehold title to 430 acres of this site and leases the remaining 174 acres pursuant to a 99-year lease that expires in 2060.

Raw Materials and Utilities

Philippine Operations

The main raw material used in the production process of Petron is crude oil. Petron acquires crude oil from foreign sources, through a combination of short-term purchase contracts and spot market purchases. In 2012, the Limay Refinery of Petron purchased approximately 82% of its total crude oil supply requirements from Saudi Aramco. Under the term contract that Petron entered into with Saudi Aramco in 2008, Petron may purchase up to 140,000 bpd of various Saudi Aramco crudes. Pricing is determined through a formula that is linked to international industry benchmarks. Payment for Saudi Aramco crude shipments is on open account basis secured by an irrevocable standby letter of credit consistent with the standard practice of Saudi Aramco for its customers

in Asia. The contract is automatically renewed annually unless either Petron or Saudi Aramco decides to terminate the contract upon at least 60-days written notice prior to its expiration date. The contract was most recently renewed on October 28, 2012. In 2011 and 2012, Petron also purchased approximately 3% and 5%, respectively, of its total crude oil for the Limay Refinery from Petronas pursuant to a one-year contract for Malaysian crude oil. Pricing is determined through a formula that is linked to international industry benchmarks. The contract is renewable subject to mutual agreement of the parties. Several other crude oils are purchased on a spot basis from various suppliers.

Although the Limay Refinery is configured to process predominantly light and sweet crudes, most of which are Middle East crudes, it is capable of processing other types of crude oil. In line with its crude optimization strategy, Petron is exploring utilization of various types of crude oil, other than those supplied by Saudi Aramco and Petronas, to provide additional value to Petron.

For low sulfur fuel oil ("LSFO"), Petron imports the bulk of its requirements from Singapore under a term supply contract and occasional spot LSFO purchases are sourced from different companies. LSFO is used for blending regular fuel oil grade for the domestic market and for refinery fuel to meet emission control standards. Petron also markets LSFO to other local industrial accounts. Petron also has a term contract for the supply of group I base oils (SN500, SN150 and BS150). This contract is renewable annually and pricing is calculated using a formula based on an international standard price benchmark for base oils. The group I base oils are the main feedstock of Petron for the production of automotive, industrial and marine lubricants. Petron is the sole buyer of all the ethanol produced by San Carlos Bioenergy, Inc. pursuant to a supply contract based on a formula price. The balance of the ethanol requirements of Petron is sourced from imports. Ethanol is blended with gasoline to comply with the Biofuels Act of 2006 initially requiring at least 5% bioethanol of the total annual volume of gasoline fuel sold by every oil company. By 2012, all gasoline grades have been mandated by DOE to contain 10% bioethanol, with the implementation of Research Octane Number ("RON") 91 and RON 100 still under consideration.

Petron also imports LPG, aviation gasoline, asphalt and some gasoline blending components. These imports are necessary as Petron does not produce asphalt and aviation gasoline, while its production of LPG is insufficient to meet domestic demand. Occasional imports of diesel, finished gasoline and jet fuel are also necessary during the Refinery's maintenance. Pricing is usually based on Mean of Platts Singapore.

The principal utilities required for the production process of Petron are water, electricity and steam. Deep wells (ground water) provide the water requirements of the Limay Refinery. Petron purchases approximately 40% of the electricity requirements of the Limay Refinery from the national grid. The balance is generated within the Limay Refinery from its existing generators. Petron is also building a new cogeneration power plant for its Limay Refinery. Upon completion, the new cogeneration power plant will have a power generation capacity of 140 MW and steam generation capacity of 400 metric tons per hour ("MTH"), which is expected to completely fulfill the Limay Refinery's electricity and steam requirements, including the increased demand arising from the full implementation of RMP-2. The new cogeneration power plant will be connected to the national grid, and Petron expects that any excess capacity generated by the new power plant will be sold to the grid.

Malaysian Operations

The main raw material used in the Port Dickson Refinery's production process is crude oil. Petron acquires crude oil for the Port Dickson Refinery from local sources, through a combination of term purchase contracts and spot purchases. Petron has entered into a term contract with Concord Energy, a crude oil and refined products trading company headquartered in Singapore. Pursuant to this contract, Petron may purchase up to 70 MBCD during the first five years and 65 MBCD during the next five years of Tapis crude oil and Terengganu Condensate. Pricing is determined through a formula that is linked to international industry benchmarks. The contract is for ten years, effective from April 1, 2012.

Petron purchases all of the crude oil supply requirements for the Port Dickson Refinery, including purchases under term contracts and spot market purchases, from Concord Energy. Although the Port Dickson Refinery is configured to process predominantly Tapis crude oil, which is a light and sweet crude oil, it is capable of processing other crude oils. In line with its crude oil optimization strategy, Petron is exploring the utilization of other crude oils for use in the Port Dickson Refinery's production.

Petron buys palm oil methyl ester ("POME") from Malaysian government-approved local suppliers for its biodiesel mix. POME is the bio-component of the biodiesel mix sold to domestic customers in Malaysia as a replacement for diesel. Petron produces a biodiesel mix comprising 5% POME and 95% diesel to comply with the current requirement under the Malaysian Biofuel Industry Act of 2007. The biodiesel program under the Malaysian Biofuel Industry Act of 2007 is being implemented in stages throughout Malaysia, and at present it covers only the central region, although it will be extended to other parts of the country by 2014.

Petron also imports LPG, diesel, gasoline and some gasoline blending components. These imports, which Petron purchases through term purchase contracts and in the spot market from Concord Energy, are necessary as Petron does not produce enough refined products to meet domestic demand in Malaysia. Pricing is usually based on Mean of Platts Singapore.

The principal utilities required for the production process of Petron are water, electricity and steam. The Port Dickson Refinery's clean water requirements for the process units are sourced from the local municipal cooling water source. Water for firefighting purposes is sourced from a natural lagoon located within the Port Dickson Refinery complex. The Port Dickson Refinery's electricity requirements are purchased from the Malaysian national electricity provider, while the Port Dickson Refinery's fire and waste heat boilers supply steam for the steam generators and other process units.

Sales and Marketing

The Philippines

In the retail market, Petron had 2,015 retail service stations throughout the Philippines as of December 31, 2012, representing approximately 34% of the country's total gasoline station count of approximately 5,900. Most of these stations are located in Luzon, where demand is heaviest. Petron can employ any of three types of service station operating structures in the Philippines, namely: company-owned-company-operated service stations ("COCO"), company-owned-dealer-operated service stations ("CODO") and dealer-owned-dealer-operated service stations ("DODO"). For COCOs, Petron buys or leases the land and also owns the service station structures and equipment. COCOs are operated by a subsidiary, Petron Marketing Corporation. Similarly, for CODOs, Petron buys or leases the land and owns the service station structures and equipment, but third party dealers operate the CODOs. For DODOs, third party dealers operate the service station, buy or lease the land, build service station structures according to Petron specifications, and lease the service station equipment from Petron. As of December 31, 2012, of the 2,015 retail service stations of Petron in the Philippines, approximately 28% were CODOs, and approximately 72% were DODOs.

Petron also services approximately 40% of the Philippine industrial sector, which includes major manufacturing, aviation, and marine accounts, according to the DOE. Petron is the biggest market participant in the Philippine LPG market, according to the Petroleum Institute of the Philippines. Petron had set up more than 800 branch stores through its *Gasul* and *Fiesta Gas* LPG dealers as of December 31, 2012. It has also gained headway in the field of alternative fuels through its auto-LPG program, Petron Xtend, and auto-LPG facilities are already installed in 21 service stations throughout the Philippines. In 2011, Petron started supplying the LPG requirements of all SMC plants such as San Miguel Yamamura and Rightpak. Petron also commissioned seven mini-refilling plants in the Philippines in 2012 to broaden the reach of the Petron's LPG products and make them accessible to more Filipinos.

To augment lubricants and greases sales, Petron Lubes had a network of 18 Car Care Centers, 25 Petron Sales Centers, 18 Motorcycle Centers and 16 Lubes & Specialties Centers throughout the Philippines as of December 31, 2012. Petron also leverages its expanded LPG outlet network, utilizing its branch stores as outlets for lubricants and specialty products. Petron is also expanding into blending and export of fuel additives, leveraging its technology partnership with Innospec, a global fuel additives supplier. Petron also provides technical services to Innospec's customers, and is able to tap the customer base of Innospec in Asia to broaden the market for its own lubricant brands.

In line with its efforts to increase its presence in the regional market, Petron also exports various petroleum products and petrochemical feedstocks, including high-sulfur fuel oil, naphtha, mixed xylene, benzene, toluene and propylene, to customers in the Asia-Pacific region. These products are sold through accredited traders and to end-users under term or spot contracts.

Malaysia

The fuels marketing business of Petron in Malaysia is divided into retail business and commercial sales. The retail business markets fuel and other retail products through a dealer network comprising 555 retail service stations located throughout Peninsular and East Malaysia, which are being rebranded under the Petron brand, a process that is expected to be completed in 2014. In Malaysia, Petron uses the CODO and DODO operating structures for its retail service stations. As of December 31, 2012, of the 555 retail service stations of Petron in Malaysia, approximately 75% were CODOs, and approximately 25% were DODOs. Approximately 260 of the service station sites have convenience stores, which generate non-fuel sales and improve traffic in the service stations. Approximately 60% of CODOs in Malaysia have convenience stores in respect of which Petron owns the equipment and runs national promotions, but the dealer owns the inventory and manages the operations.

Approximately 50% of DODOs in Malaysia have convenience stores that are fully owned and managed by the dealers.

Since acquiring its Malaysian operations in March 2012, Petron has been actively pursuing initiatives to improve customer service and promote customer loyalty at its Malaysian retail service stations. Petron has continued to operate the existing loyalty card programs at its Malaysian retail service stations, and these programs will be rebranded as part of the general rebranding of Petron's Malaysian retail service station network.

The commercial sales of Petron are divided into four segments: industrial and aviation fuels, wholesale fuels, LPG and lubricants and specialties. The industrial and aviation segment sells diesel, gasoline and jet fuel to unbranded mini-stations and power plants, as well as to the manufacturing, plantation, transportation and construction sectors. Sales to the mini-stations are priced according to the APM. Many power plants in Malaysia run on natural gas and use diesel as alternative fuel when there are gas curtailments. Petron sells diesel to such power plants on an ad-hoc basis at spot prices. The pricing of these sales is determined through a formula that is linked to international industry benchmarks. Sales of diesel to the manufacturing, plantation and construction sectors are not regulated by the Malaysian government, and the pricing of these sales is subject to market supply and demand. Sales of diesel to selected transportation sectors are priced according to the APM. Since sales to these transportation sectors are subject to a quota system in Malaysia, the sales of Petron to these transportation sectors are subject to volume limits. Petron is also one of the three major jet fuel suppliers in Malaysia and sells jet fuel at Kuala Lumpur International Airport ("KLIA") pursuant to a throughput agreement with the Kuala Lumpur Aviation Fuelling System, the operator of the KLIA's storage and hydrant facility.

The Malaysian wholesale segment consists of sales, primarily of diesel, gasoline and kerosene, to Petron-appointed resellers, which sell the products to industrial customers. Petron markets LPG in 12-kg and 14-kg cylinders for domestic use through two company-owned-dealer-operated redistribution centers, 17 dealer-owned-dealer-operated stockists and 160 dealers. LPG redistribution centers are owned by Petron and distribute bottled LPG to dealers. Stockists are dealer-owned and are smaller in size than redistribution centers. Dealers generally collect bottled LPG directly from redistribution centers and stockists for onward sale to domestic consumers. Sales of LPG in 14-kg cylinders or less are subsidized under the APM.

Petron established a lubricants and specialties segment in April 2012 to introduce Petron lubricants and greases into the Malaysian market. A wide range of automotive lubricants is sold through Petron's extensive network of service stations in Malaysia.

Petron also participates in sales to car and motorcycle workshops, as well as to the industrial market through its appointed distributors. In addition, Petron exports LSWR and naphtha from the Port Dickson Refinery. LSWR is exported under a term contract with Concord Energy, and naphtha is sold through accredited traders under spot contracts. Petron awards these contracts based on a tender process.

Capital Expenditures

Petron has upgraded the Limay Refinery and expanded its retail service station network in the Philippines over the past several years and intends to continue to increase investments in these areas in order to optimize operational efficiency, reduce costs and increase market share, and Petron is also investing in its recently acquired Malaysian operations. Specifically, Petron intends to (i) complete the implementation of RMP-2 which will enable the Limay Refinery to further enhance its operational efficiencies and convert its current fuel oil production into White Products production, significantly increase production of petrochemicals and make Petron the only oil company in the Philippines capable of producing Euro IV-standard fuels, the global clean air standard, (ii) complete the construction of a new cogeneration power plant for the Limay Refinery, (iii) continue the expansion of its retail service station network in the Philippines, (iv) enhance the facilities at the Port Dickson Refinery to increase its utilization of heavier, more sour crude oil and to enable it to produce Euro 4M-standard fuels and (v) complete the rebranding and refurbishing of its retail service station network in Malaysia. Petron intends to finance these plans with net cash flows provided by operating activities as well as equity and debt to be determined at the time of financing.

The estimated consolidated capital expenditures of Petron for 2013 are ₱51.9 billion, allocated as follows: approximately 72% for the implementation of RMP-2, approximately 13% for the cogeneration power plant project, approximately 2% for retail service station network expansion in the Philippines, approximately 1% for enhancing the facilities at the Port Dickson Refinery and approximately 3% for rebranding and refurbishing its retail service station network in Malaysia. As of December 31, 2012, Petron has spent an aggregate of approximately ₱58 billion on RMP-2, the cogeneration power plant and the Philippine retail service station expansion program. Petron expects to continue to make substantial capital expenditures after 2013 to complete the major projects described above and for other purposes. These capital expenditures are expected to be funded

by a combination of net cash flows provided by operating activities, proceeds from Petron's undated subordinated capital securities issued in the first quarter of 2013 and external financing sources.

The capital expenditures of Petron may change as projects are reviewed or contracts entered into and are subject to various factors, including market conditions, the general state of the Philippine economy, the operating performance and cash flow of Petron and its ability to obtain financing on terms satisfactory to management.

Competition

The Philippines

In the Philippines, Petron operates in a deregulated business environment, selling its products to individual, commercial and industrial customers. The enactment of the Downstream Oil Industry Deregulation Law in 1998 effectively removed the rate-setting function of the Philippine government through what was then known as the Energy Regulatory Board, leaving price-setting to market forces. It also opened the oil industry to free competition. The Philippine oil industry is dominated by three major Philippine oil companies: Petron, Shell and Chevron (formerly Caltex Philippines), which, based on industry data from the DOE for the year ended December 31, 2012, together constitute 73.1% of the Philippine market based on sales volume. Deregulation has seen the entry of more than 100 other industry market participants, rendering the petroleum business more competitive. Petron and Shell operate the only refineries in the country. The rest of the industry market participants are importers of finished petroleum products or purchase finished petroleum products from other market participants in the local market. In the Philippines, Petron competes with other industry market participants on the basis of price, product quality, customer service, operational efficiency and distribution network, with price being the most important competitive factor. Providing total customer solutions has increased in importance as consumers became more conscious of value.

Petron participates in the reseller (service station), LPG, industrial and lube sectors, through its network of service stations, terminals and bulk plants, dealers and distributors throughout the Philippines. In the reseller sector, competition is most dynamic among the major firms, as seen through the construction of service stations by Shell, Chevron, Total Philippines, Phoenix Petroleum, Seoil and other new participants in major thoroughfares. The small market participants also continue to grow, with station count increasing from 695 in 2001 to approximately 1,900 stations as of December 31, 2012. Participants in the reseller and LPG sectors continue to resort to aggressive pricing and discounting in order to expand their market share. The number of LPG importers in the Philippines increased from three, prior to deregulation, to about seven, with new entrants having more flexible and bigger import receiving capacities. Although Petron is the biggest participant in the Philippine LPG sector, the new participants in this sector, led by Liquigaz, had a collective market share of 58.2% as of December 31, 2012. In the industrial sector, the major market participants continue to invest heavily in order to increase their market share and tap new markets. In the lubricants sector, intense competition among over 50 brands, including global brands such as Castrol, Mobil, Shell and Caltex, continues.

Brands compete for limited shelf space, which has led to the penetration of previously unutilized markets, such as auto-dealerships in malls. Petron is the leader in the Philippine oil industry, with an overall market share of 38.5% of the Philippine oil market, ahead of the other two major Philippine oil companies, which have market shares of 24.6% and 10.0%, in each case in terms of sales volume based on industry data from the DOE for the year ended December 31, 2012. Approximately 100 smaller oil market participants, which started operations after the deregulation of the oil industry in 1998, account for the remaining market share. Petron is the leader in terms of sales volume in the retail, industrial and LPG market segments and a strong second, as compared with the market shares of the two other major Philippine oil companies, in the lubricants and greases market segment based on industry data from the DOE for the year ended December 31, 2012.

Petron believes that its competitive advantages include organization, technology, assets, resources and infrastructure. Petron continues to implement initiatives aimed at improving operational efficiencies, managing costs and risks, and maximizing utilization of its assets and opportunities.

Malaysia

In the retail service station business, the Malaysian operations of Petron compete with four other main participants in the market, namely: subsidiaries of Petroliam Nasional Berhad ("Petronas"), Royal Dutch Shell plc, Caltex and BHPetrol. Of these competitors, Petronas and Shell also have refinery operations in Malaysia. The Malaysian government regulates the pricing of gasoline and diesel at retail service stations through the APM. Petron continues to face intense competition in the Malaysian industrial and wholesale markets from other local and multi-national oil companies. Petron uses its local production from the Port Dickson Refinery and its strategic terminal locations across Malaysia to remain competitive in these segments. Besides the mini-stations,

fisheries and some selected transportation sectors, which are governed by the APM, other sectors do not benefit from the subsidies provided for under the APM. Competition in diesel sales is very intense, as Malaysian refiners generally prefer to sell locally rather than to export. The aviation market is also very competitive, as the three local refiners offload their jet fuel through the multi-product pipeline to KLIA. Sales of jet fuel at the other Malaysian airports are supplied by the oil companies having the necessary storage and logistics capability, and Petron does not participate in sales to these airports. In the LPG segment, the APM applies only for sales of LPG in 14-kg or smaller cylinders. Competition in this market is driven by supply economics, dealer network efficiency and customer service. Petron, being well established, remains competitive in this segment. The industry is currently lobbying for a review of the APM for LPG sales in Malaysia to reflect rising import costs, which have adversely affected suppliers who are reliant solely on LPG imports. The lubricants and specialties market is dominated by the traditional global brands as well as Petronas. Petron has the advantage of an extensive network of service stations to market its products and to provide brand presence. Price is a major competitive factor in this market. Petron believes that it is well positioned to compete in this market, due to its efficient blending plant and supply chain.

Health, Safety and Environmental Matters

The Philippines

Petron is subject to a number of employee health and safety regulations in the Philippines. For example, Petron is subject to the occupational safety and health standards promulgated by the Department of Labor and Employment of the Philippines (the “DOLE”). Petron has a Corporate Technical and Engineering Services Group (“CTESG”) responsible for formulating, implementing and enforcing the employee health and safety policies of Petron, as well as ensuring compliance with applicable laws and regulations. Petron has conducted training and skills development for employees, contractors and other business partners. The training programs were designed to raise awareness and impart vital knowledge in connection with oil spill response, fire-fighting and basic safety. The terminals and depots of Petron have oil spill contingency plans, which can be executed whenever necessary. All of Petron’s terminals and depots were given the 2011 Safety Milestone Award by the DOLE’s Bureau of Working Conditions of DOLE for safety achievements in 2010.

Petron is also subject to various Philippine environmental protection laws and regulations. For example, Petron is subject to extensive regulation by the Philippine Department of Environment and Natural Resources (“DENR”). Among others, these DENR regulations require Petron to designate and appoint a DENR-accredited pollution control officer for every installation, to engage DENR-accredited transporters and treaters of hazardous waste, to secure environmental compliance certificates, discharge permits, permits to operate air pollution sources and hazardous waste generators, and to submit regular monitoring reports. The CTESG of Petron provides technical assistance and consultancy services on areas of environmental management and engineering and securing of permits during project planning, design and implementation. It is also responsible for formulating and implementing an environmental management system (“EMS”) based on ISO 14001 standards in the Limay Refinery and Petron’s depots, terminals and service stations. A number of the service stations of Petron in Davao and General Santos are now implementing EMS, a first in the Philippine oil industry. The CTESG, with assistance from external environmental instructors, regularly conducts environmental awareness training for Petron’s employees, contractors and service station dealers. The training module is accredited by the DENR’s Environmental Management Bureau. In addition, the CTESG conducts an annual compliance audit of the facilities of Petron to ensure compliance with applicable environmental laws and regulations, as well as with internal policies, and advises the senior management of critical environmental issues. As part of its advocacy functions, the CTESG is also actively involved in public stakeholder consultations during the drafting of Philippine environmental protection laws and regulations. Petron also actively participates in local and regional oil spill response consortiums, including the Waterborne Industry System and Oil Spill Response Ltd. As of December 31, 2012, Petron is in material compliance with applicable environmental laws in the Philippines.

Malaysia

Petron is subject to local safety, health and environmental regulation in Malaysia, including (i) the Occupational Safety and Health Act 1994, as amended, and regulations made pursuant thereto, which are administered by the Malaysian Department of Safety and Health, (ii) the Environmental Quality Act 1974, as amended, and regulations made pursuant thereto, which are administered by the Malaysian Department of Environment and (iii) the Fire Services Act 1988, as amended, and regulations made pursuant thereto, which are administered by the Fire Rescue and Services Department. Petron has a corporate safety, security, health and environment department that is responsible for formulating, implementing and enforcing the safety, health and environmental policies of Petron in Malaysia, coordinating and conducting relevant programs to raise the level of awareness of SSHE and ensuring compliance with applicable laws and regulations. For more than ten years, the Port Dickson

Refinery and the terminals and other businesses of Petron in Malaysia have attained good safety performance without any lost-time injury for employees or contractors. The Port Dickson Refinery and Malaysian terminals of Petron have been awarded annual recognition of their safety and health performance by the MSOSH for more than five consecutive years. The Port Dickson Refinery has also been awarded the Prime Minister Hibiscus Award for good environmental performance. As prescribed by local regulatory requirements, the Port Dickson Refinery and the Malaysian terminals of Petron have established emergency response and oil spill contingency plans. For more than fifteen years, the Malaysian operations of Petron have actively participated in local and regional oil spill response consortiums, such as the Petroleum Industries of Malaysia Mutual-Aid Group and Oil Spill Response Ltd. Petron strives to achieve and sustain good SSHE performance in Malaysia through the implementation of various key programs including (i) the SMS, which provides a structured approach to the management of risks related to personal and operational risks as well as to ensuring regulatory compliance, and (ii) the LPS, which was adopted to prevent or reduce losses and incidents using behavior-based tools and other safety management techniques.

ENERGY BUSINESS

SMC operates its energy business through its wholly owned subsidiary, SMC Global Power (together with its subsidiaries SMEC, SPPC and SPDC). SMC Global Power is one of the market leaders in the Philippine power generation industry in terms of installed capacity. Incorporated in 2008, SMC Global Power, through its subsidiaries, has successfully bid for the privatization of electrical power generation plants in the Philippines, which are administered pursuant to IPPA agreements with PSALM, an entity owned by the Philippine government.

SMC Global Power administers a portfolio of three operating power plants under IPPA agreements with a combined capacity of 2,545 MW as of December 31, 2012.

As of December 31, 2012, SMC Global Power had total assets of ₱270,538 million and sales in 2012 of ₱74,656 million.

Philippine Power Generation Industry

The current framework of the Philippine power sector is governed by the EPIRA, which was enacted in 2001. The Philippine power industry, following the passage of the EPIRA, is undergoing major reforms. The EPIRA aims to improve the power sector in the Philippines by ensuring and accelerating total electrification of the country and providing a fairer and competitive landscape for power sector participants, resulting in a more efficient and transparent industry. Among other things, the EPIRA requires:

- the creation of the ERC, which is an independent quasi-judicial regulatory body under the EPIRA;
- separation of the industry into generation, transmission, distribution and supply sectors;
- break-up and privatization of generation assets of the NPC, and the privatization of transmission assets by PSALM;
- eventual removal of the monopoly distribution utilities currently hold on retailing electricity within their franchise areas to allow retail competition; and
- retail competition and open access to distribution networks.

On June 6, 2011, the ERC announced that the final stage of electricity reform, the “open access regime,” will commence on December 26, 2011 in Luzon and Visayas. Under the open access regime, all electricity end-users with an average monthly peak demand of 1 MW for the 12 months preceding December 26, 2011, as certified by the ERC, will have the right to choose their own electricity suppliers. However, to date, the “open access” has not yet been implemented. The Philippine power industry has evolved into a competitive market with clear separation among generation, transmission, distribution and supply. Under the EPIRA, cross ownership is not allowed in the transmission sector with the generation and distribution sector.

The following tables summarizes the power supply and demand outlook from 2012 to 2030 in Philippines based on the DOE Power Development Plan, 2009-2030:

Grid	Dependable capacity (MW)⁽¹⁾	Peak demand (MW) 2008	Average annual growth rate	Committed capacity (MW)	Critical period	Required additional capacity (MW) 2009-2030	Indicative new capacity (MW) 2009-2030
Luzon	10,030	6,822	4.5	600	2011	11,900	3,449
Visayas	1,505	1,176	4.6	654	2009	5,150	182
Mindanao	1,682	1,228	4.6	100	2010	2,500	581
Philippines	13,217	9,226	4.6	1,354		16,550	4,211

Note:

(1) Maximum capacity a power plant can sustain over a specified period as modified for seasonal limitation and other plant-specific factors such as required maintenance

SMC believes this increase in demand will lead to electricity shortages, which will increase prices in the WESM and thereby enabling SMC Global Power to sell electricity at higher prices, as well as providing opportunities to build new generation capacity to meet the projected shortage.

IPPA Framework

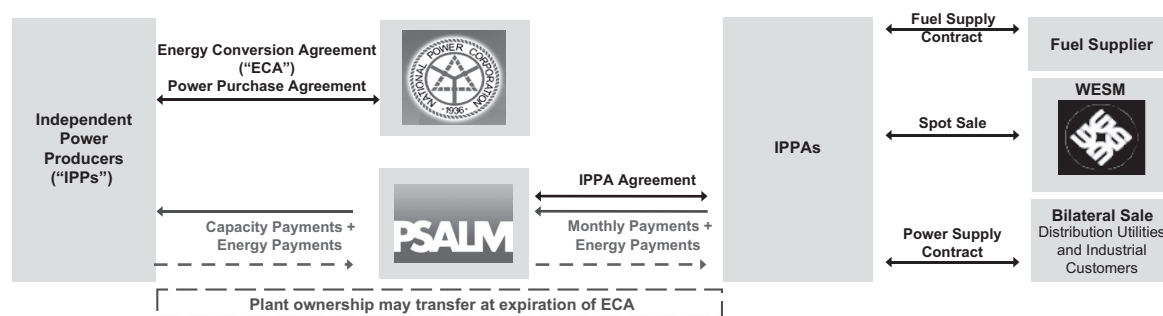
PSALM, together with NPC, has ECAs or other PPAs in place with various IPPs in the Philippines. Under the EPIRA, PSALM is required to achieve, through open and competitive bidding, the transfer of the management and control of at least 70% of the total energy output of the IPP plants under contract with NPC to IPPAs pursuant to IPPA agreements, such as those held by SMC Global Power.

Under IPPA agreements, the IPPAs have the right to sell the electricity generated by such IPP in the wholesale electricity spot market and also by entering into PSCs with specific customers and will, in general, manage procurement of the fuel supply to the associated IPP. IPPAs pay PSALM a fixed monthly payment and a variable energy or generation fee the amount of which depends on the dispatch and performance of the IPP. IPPA agreements provide relief for IPPAs such as SMC Global Power in the event the associated IPPs are unable to dispatch for a certain period of time not due to the fault of the IPPA. PSALM/NPC in turn pays the IPPs capacity and energy payments based on their respective ECAs or PPAs. In some cases, IPPA agreements provide the IPPA with the right to acquire ownership of the power plants or generation facilities from the IPPs at the end of the terms of the ECAs or PPAs. Under the IPPA agreements of SMC Global Power, it has the right to acquire the Sual Power Plant in October 2024, the Ilijan Power Plant in June 2022 and the San Roque Power Plant in May 2028 or on some earlier date due to certain events such as changes in applicable law or non-performance by the IPP.

The IPPA framework is intended to provide successful bidders a way to enter and trade in the WESM for a minimal capital outlay without the expense of building a new power plant and for IPPAs to enjoy the benefits normally attributed to owners of power generation plants, including controlling the fuel and its dispatch, trading, and contracting of the power plant, without maintenance costs or capital upgrades, which remain with the IPPs. Also, many of the risks of owning a power plant are explicitly managed through the contract. If there is an extended outage at the power generation plants, for example, there is up to a 50% discount on the monthly fees, and PSALM bears the force majeure risks to the power generation plants. The IPPA framework also permits an IPPA to assume the role of NPC as an offtaker of power generated by IPPs without affecting NPCs underlying agreements with the IPP.

IPPAAs are permitted to trade in the WESM, and are also free to enter into bilateral contracts and seek other markets for the balance of their contracted capacities and energy, as well as enter into other forms of financial hedging instruments if desired to manage their position in and exposure to the market.

Set forth below is a general illustration of the IPPA framework.



Notes:

- (1) The Ilijan Power Plant and the San Roque Power Plant do not have fuel supply agreements.
- (2) SMC GP is only responsible for fuel supply in the Sual Power Plant.

Competitive Strengths

Leading power company in the Philippines with a strong platform for future growth. SMC Global Power is one of the largest power companies in the Philippines based on the contracted capacity of its existing power portfolio. SMC Global Power is the IPPA for the Sual, Ilijan and San Roque power plants, which have a combined contracted capacity attributable to SMC Global Power of 2,545 MW. Based on the market's total installed capacity, SMC Global Power, on a contracted capacity basis for the Sual, Ilijan and San Roque power plants, has a 17% market share of the power supply of the national grid of the Philippines, and a 22% market share of the Luzon grid, in each case as of December 31, 2012, based on industry data from the DOE.

The IPPA business model provides SMC Global Power with the benefit of having the right to sell electricity generated by the IPPs without having to incur large upfront capital expenditures for the power plant construction, or to bear any related development risk. As an IPPA, SMC Global Power determines the amount of power to be produced by the IPP for supply to the customers of the IPPA and sells the power generated by the IPPs either pursuant to offtake agreements directly with customers or through the WESM. This business model provides SMC Global Power the ability to manage both market and price risk by entering directly into bilateral contracts with established customers while capturing potential upside through the sale of excess capacity through the WESM when spot market prices are attractive.

The experience of SMC Global Power in acting as an IPPA, and its history of power plant ownership and operation, have enabled SMC Global Power to gain expertise in the Philippine power generation industry. With this experience, SMC Global Power believes it is in a strong position to participate in the expected future growth of the Philippine power market, through both the development of greenfield power projects and the acquisition of existing power generation capacity of selected NPC-owned power generation plants that are scheduled for privatization as asset sales or under the IPPA framework.

SMC Global Power is also in a strong position to pursue vertical integration by developing its own coal supply source (upstream vertical integration) and expansion of its sales to a broader range of customers (downstream vertical integration), including retail customers. SMC Global Power has already acquired coal exploration, production and development rights over approximately 17,000 hectares of land in Mindanao. Capitalizing on changes in the Philippine regulatory structure, SMC Global Power holds a retail electricity supplier license from the ERC. Once open access and retail competition is implemented, the electricity supplier license will allow SMC Global Power to enter into offtake agreements with customers with power requirements of at least 1 MW.

Flexible and diversified power portfolio. SMC Global Power manages the capacity of a balanced portfolio of some of the newest and largest power plants in the Philippines, which benefit from diversified fuel sources. The IPPA power plants have an average age of 10 years. Based on Philippine power industry data from the DOE, in terms of installed capacity in the Philippines, the Sual power plant is the largest coal-fired power plant, the Ilijan power plant is the largest natural gas-fired power plant and the San Roque power plant is one of the largest and newest hydro-electric power plants.

The existing power portfolio of SMC Global Power consists of natural gas-fired (Ilijan power plant), which represents 47.2% of the contracted capacity of SMC Global Power, coal-fired (Sual power plant), which represents 39.3% of the contracted capacity of SMC Global Power, and hydro-powered (San Roque power plant), which represents 13.6% of the contracted capacity of SMC Global Power. Power generated by the Sual and Ilijan power plants is primarily sold to customers pursuant to offtake agreements, while power generated by the San Roque power plant is sold through the WESM.

SMC Global Power believes that the size and diversity of the feedstock of its power portfolio reduces its exposure to specific risks associated with any one type of power plant, to fluctuations in electricity demand, and to variations in fuel costs and regulatory concerns that are linked to any one type of power plant. The fuel diversity of the portfolio is expected to mitigate the impact of sudden fuel price increases and supply shortages. SMC Global Power believes that its management of the capacity of this large diverse portfolio of power plants allows it to respond efficiently to market requirements at each point of the electricity demand cycle. This diversity helps it to improve the profitability of its portfolio by flexibly dispatching electricity in response to market demand and fuel cost competitiveness. SMC Global Power is permitted to enter into bilateral contracts and to trade in the WESM for the balance of its contracted capacities and energy. By managing the IPPA power plants as a single portfolio and actively managing the energy output of the plants, SMC Global Power seeks to offer more competitive electricity rates compared to other power companies with smaller and less diverse portfolios.

Established relationships with world class partners. The IPPA power plants are owned, operated and maintained by world-class partners, including Marubeni Corporation, Tokyo Electric Power Corporation, Korea Electric Power Corporation and Mitsubishi Corporation. Since entering the power business, SMC Global Power has established relationships with recognized international fuel suppliers, including Bumi Resources, Noble Resources Pte. Ltd. and Banpu Public Company Limited Thailand, as well as with its customers, including Meralco, its largest customer. SMC Global Power believes that these established relationships provide a strong foundation for its existing business and an excellent base of potential partners for future expansion.

Well-positioned to capitalize on the anticipated growth of the Philippine electricity market. Over the period from 2010 to 2030, growth in demand for electricity in the Philippines is expected to exceed the growth rate of the Philippines' GDP, according to the DOE Power Development Plan published in January 2013, with peak demand for electricity in Luzon, Visayas and Mindanao expected to reach an average annual growth rate of 4.13%, 4.52% and 4.75%, respectively. The DOE projects that power consumption in Luzon, Visayas and Mindanao will require aggregate additional capacities of 1,500 MW, 100 MW and 400 MW, respectively, by 2018, while only approximately 1,019 MW, 310 MW and 588 MW are currently expected to be provided by committed power projects in Luzon, Visayas and Mindanao, respectively. Construction of new power plants on average takes a minimum of three years. Given the gap between projected electricity demand and committed power projects, SMC Global Power expects that there will be a power supply shortage in the medium term until new capacity is built.

SMC Global Power believes it is well-positioned to benefit from continued growth in the Philippine electricity market and power supply shortage. SMC Global Power has a defined roadmap to increase capacity by developing greenfield power projects and bidding for selected NPC-owned power generation plants that are scheduled for privatization. SMC Global Power is already in the construction stage for two clean coal greenfield power projects. In addition, as a leading power company in the Philippines with a large customer base, SMC Global Power believes that it is in a strong position to leverage its relationships with its existing customers to service their expected increased electricity demands.

Experienced management, trading and marketing teams. The senior management of SMC Global Power has extensive experience in the Philippine power industry, and SMC Global Power believes that they have a deep understanding of the Philippine electricity markets with respect to the operational, financial, regulatory, and business development aspects of the operation and management of power plants. The senior management team of SMC Global Power has strong professional relationships with key industry participants, such as the DOE, PSALM, NPC, National Transmission Corporation ("TransCo")/ National Grid Corporation of the Philippines ("NGCP"), Philippine Electricity Market Corporation ("PEMC") and ERC, as well as other government offices and agencies. The employees of SMC Global Power include experienced energy traders who pioneered WESM trading and marketing executives who have established strong relationships with the extensive customer base of NPC. The members of the Executive Committee of SMC Global Power have on average more than 25 years of experience in executive management, including strengths in key areas of engineering and finance. The executive and senior management have displayed a strong track record of growth and delivery since SMC Global Power commenced operations in November 2009.

Business Strategies

Optimize the generation capacity of the IPPA power plants, leverage operational synergies and expand its customer base. SMC Global Power intends to actively manage its sales and optimize the operations of its IPPA power plants in order to achieve a balanced mix of power sales through (1) contractual arrangements with electricity customers including distribution utilities, industrial and commercial customers, (2) sales through the WESM and (3) participation in the retail electricity supply market. This approach is intended to improve

certainty and predictability of sales from contracted sales and capture sales upside from the WESM. The objective of SMC Global Power is to supply customers based on the least cost while dispatching according to the requirements of the IPPA agreements, and to sell available excess energy of the IPPA power plants through the WESM at favorable prices. As such, SMC Global Power seeks to maximize profitability through effective fuel cost risk management and dispatch decisions relating to its IPPA power plants. For 2012, sales through bilateral arrangements to sales through the WESM for the Sual, Ilijan and San Roque power plants were 92%-8%, 95%-5% and 50%-50%, respectively.

Specifically, in case of high prices in the WESM, SMC Global Power can sell the excess output of the IPPA power plants to the WESM after delivering the contractual amounts required under its offtake agreements. Alternatively, in case of low prices in the WESM, SMC Global Power can minimize the generation output of its power plants and deliver the contractual amounts required under its offtake agreements either with output from the San Roque power plant or with energy purchased from the WESM. In the event of tripping or shutdown of either the Sual or Ilijan power plant, SMC Global Power can maximize the dispatch of its remaining units by lowering the bid prices so that the bilateral contract quantity requirements will be served without buying at high prices from the WESM.

Grow its power portfolio through development and acquisition of power generation capacity. SMC Global Power intends to utilize its strong platform, extensive relationships and experienced management team to address the growing demand for power in the Philippines. SMC Global Power plans to continue its strategic development of greenfield power projects in parallel with its plan to acquire existing power generation capacity by bidding for selected NPC-owned power generation plants that are scheduled for privatization as asset sales or under the IPPA framework. SMC Global Power seeks to capitalize on regulatory and infrastructure developments by scheduling the construction of greenfield power projects to coincide with the planned improvements in the interconnectivity of the Luzon and Visayas grids, as well as the eventual interconnectivity and implementation of WESM in Mindanao. In addition, SMC Global Power seeks to maintain the cost competitiveness of these new projects by strategically locating them in high-demand areas and in proximity to the grid. SMC Global Power is considering the expansion of its power portfolio of new capacity nationwide through greenfield power projects over the next ten years, depending on market demand. SMC Global Power plans to carry out the expansion of its power portfolio in phases across Luzon, Visayas and Mindanao. SMC Global Power plans to use clean coal technology for its planned and contemplated greenfield power projects.

Pursue vertical integration. SMC Global Power intends to continue to expand into businesses along the power sector value chain that complement its current power generation business. As part of this strategic growth and expansion, SMC Global Power has acquired coal exploration, development and production rights over approximately 17,000 hectares of land in Mindanao. If SMC Global Power is able to develop these assets and commence mining operations successfully, SMC Global Power expects these assets will provide a source of coal fuel supply for its planned and contemplated greenfield power projects. SMC Global Power intends to develop these coal mines in Mindanao in parallel with its planned greenfield power projects and is targeting coal production around the same time as when the greenfield power projects become operational. In addition, SMC Global Power has a 6.13% equity stake in Meralco, the largest distribution utility in the Philippines, and one of the most significant customers of SMC Global Power, and through this investment (together with the 21.46% equity interests of SMC and the 5.24% equity interests of San Miguel Pure Foods in Meralco), SMC Global Power has developed an understanding of the electricity distribution market in the Philippines, particularly in the Luzon region. Moreover, with the expected implementation of open access, SMC Global Power believes it is in a strong position to capitalize on the retail electricity selling opportunity due to its current strong industry position in both Luzon and the Philippines as a whole. SMC Global Power has obtained a retail electricity supplier license to expand its customer base and diversify its sales. Once open access and retail competition is fully implemented, the electricity supplier license will allow SMC Global Power to enter into offtake agreements with customers with power requirements of at least 1 MW, which may include other SMC subsidiaries. SMC Global Power believes that such vertical integration will provide it with a competitive advantage in the Philippine power market.

Certain Operating Data

SMC Global Power receives income from the sale of electricity by its administered and owned power generation facilities to a variety of customers, including Meralco, electric cooperatives, industrial customers and the WESM. In 2012, the three power plants for which SMC Global Power has IPPA agreements generated 15,250 giga-watt hours (“GWh”) of electricity. As of December 31, 2012, the attributable installed capacity of SMC Global Power was powered 39.3% by coal, 47.2% by gas and 13.6% by hydro power.

The table below summarizes certain operating metrics in respect of the three power generation facilities owned or administered by SMC Global Power as of December 31, 2012:

Project	Placed in service	Date SMC global power assumed operations	Operator	Installed capacity (MW)	Fuel	Energy generation (GWh) ⁽¹⁾		Capacity utilization (%)		Availability factor (%)	
						2011	2012	2011	2012	2011	2012
Sual	10/25/1999	11/6/2009	TeaM Energy	2 x 500 ⁽¹⁾	Coal	5,406	6,034	62%	69%	84.68	86.80
Ilijan	6/5/ 2002	6/26/ 2010	KEPCO	2 x 600	Gas	7,964	8,223	76%	78%	94.25	93.98
San Roque . . .	5/1/ 2003	1/26/2010	Marubeni-Kansai Electric	345	Hydro-electric	1,041	994	34%	33%	97.16	96.77

Note:

(1) Installed capacity is 2 x 647 MW but contracted capacity of the Sual Power Plant is 2 x 500 MW.

The table below sets forth the sales, gross profit margin, EBITDA margin and net income before tax margin of SMC Global Power for the periods indicated:

	For the year ended December 31,		
	2010	2011	2012
	(P in millions, except percentages)		
Sales ⁽¹⁾	66,136	70,591	74,656
Gross profit	17,259	19,672	18,811
Gross profit margin ⁽²⁾	26.1%	27.9%	25.2%
EBITDA ⁽³⁾	21,759	23,719	25,010
EBITDA margin ⁽⁴⁾	32.9%	33.6%	33.5%
Net income before tax	19,759	6,402	15,648
Net income before tax margin ⁽⁵⁾	29.9%	9.1%	21.0%

Notes:

(1) Sales for 2010 include Limay operations. The Limay operation was sold on August 2011.

(2) Gross profit margin is calculated by sales less cost of power sold over sales.

(3) EBITDA is calculated as net income before: income tax expense, net financing charges (interest income net of interest expense), extraordinary or exceptional items, foreign exchange losses (gains), marked-to-market currency losses (gains) and depreciation and amortization and impairment losses.

(4) EBITDA margin is calculated by EBITDA divided by sales.

(5) Net income before tax margin is calculated by net income before income tax divided by sales.

In addition, SMC Global Power, through its subsidiaries DAMI, BERI and SEPC, owns various coal properties that are in the exploration phase.

SMC Global Power, through its subsidiaries, derives a substantial portion of its sales from PSCs with established offtakers. The DOE forecasted in its Power Development Plan, 2009-2030 that peak demand will grow at an average annual rate of 4.30%, 4.90% and 5.20% per year between 2009 and 2018 in Luzon, Visayas and Mindanao, respectively, with aggregate peak demand expected to reach 10,393.0 MW, 1,887.0 MW and 2,031.0 MW by 2018 in Luzon, Visayas and Mindanao, respectively. SMC Global Power expects these factors, and the scarcity of new capacity expected to come online over the next two to three years, to support dispatch for it as well as other existing generators.

Power Generation Facilities

Sual Power Plant

The Sual Power Plant is a 2 x 647 MW coal-fired thermal power plant located in Sual, Pangasinan on the Lingayen Gulf that commenced commercial operations in October 1999, and is the largest coal-fired thermal power plant in the Philippines in terms of installed capacity. The Sual Power Plant was built by CEPA Pangasinan Electric Limited pursuant to an ECA with NPC under a 25-year Build- Operate-Transfer (“BOT”) scheme that expires on October 24, 2024. In 2007, TeaM Sual Corporation (“TeaM Energy”), which is a joint venture between Marubeni Corporation and Tokyo Electric Power Corporation, acquired the Sual Power Plant.

SMC Global Power, through its subsidiary SMEC, assumed administration of the Sual Power Plant on November 6, 2009 in accordance with an IPPA agreement (the “Sual IPPA agreement”) entered into with PSALM. PSALM remains responsible under an ECA to remunerate the IPP of the Sual Power Plant for the electricity it produces.

Sual IPPA

PSALM, NPC and SMC Global Power entered into the Sual IPPA agreement pursuant to which SMC Global Power has the right to manage, control, trade, sell or otherwise deal in the electrical generation capacity of the Sual Power Plant, while SMC Global Power must supply and deliver, at its own cost, fuel required by the power plant and necessary for it to generate the electricity required to be produced under the ECA between NPC and TeaM Energy (the “Sual ECA”). In addition, SMC Global Power must pay fixed monthly payments comprising both a U.S. Dollar and Philippine Peso component. These fixed monthly payments are reduced proportionately in any month that the Sual Power Plant is unable to produce power for an entire day (a “Non-Delivering Day”) (for reasons not attributable to SMC Global Power) and reduced further in proportion to the number of Non-Delivering Days in that month.

In addition, SMC Global Power must pay monthly energy fees that are periodically adjusted for inflation and that consist of (i) a fixed base energy rate for power actually delivered by the Sual Power Plant comprising both a U.S. Dollar and Philippine Peso component plus (ii) a variable energy rate for power actually delivered by the Sual Power Plant, in U.S. Dollars only, that takes into account the cost and efficiency of fuel supplied to the Sual Power Plant as well as the efficiency (unit heat rate) of the Sual Power Plant, which is measured on an annual basis.

The Sual IPPA agreement also requires SMC Global Power to maintain a performance bond in favor of PSALM equivalent to US\$58.0 million, and perform the obligations of NPC in its PSCs, including the obligation to procure electricity at its own cost to meet deficiencies, in cases where the Sual Power Plant is unable to supply the contracted power.

Under the Sual IPPA agreement, SMEC has the right to acquire the Sual Power Plant in October 2024, which is the end of the cooperation period between NPC and TeaM Energy under the Sual ECA, or on some earlier date due to certain events such as changes in law or non-performance by TeaM Energy under the Sual ECA.

Power Offtakers

The PSCs of the Sual Power Plant require its offtakers to take or pay for, within a contract year, a mutually agreed minimum energy quantity (“MEQ”). Such offtakers may exceed the MEQ, but any consumption in excess of the MEQ may be subject to additional charge.

The pricing for PSCs assigned by PSALM to SMC Global Power is based on the prevailing rate structure of NPC as approved by the ERC. Currently, the NPC rate structure consists of two basic charges and two cost adjustment mechanism charges. The basic charges, which are based at a premium over the costs structures of NPC as of its 2007 audited financial statements, consist of the generation charge designed into time-of-use rates and the franchise and benefits to host communities charge. These are fixed charges and remain constant regardless of the movements in the prices of the different fuels used by NPC in generating electricity, as well as movements in foreign exchange rates and inflationary effects.

The cost adjustments, on the other hand, pertain to (a) the Deferred Accounting Adjustment (“DAA”) charges under the Generation Rate Adjustment Mechanism and the Incremental Currency Exchange Rate Adjustment or (b) the Automatic Cost Adjustment Mechanism (“ACA”) charge under the Automatic Cost Recovery Mechanism. The Generation Rate Adjustment Mechanism and Incremental Currency Exchange Rate Adjustment DAAs allow for the recovery of incremental costs (or the refund of savings), if any, pertaining to previous months’ actual operations and any new level of DAA may only be implemented upon prior application to and approval by the ERC. On the other hand, the ACA is a month-to-month adjustment implemented automatically by PSALM/NPC subject to review, evaluation, confirmation and approval by the ERC.

For power offtake agreements entered into by SMEC directly with new offtakers on a bilateral basis (or with those offtakers under previously assigned offtake agreements which have expired), pricing is based on a reasonable return over the cost structure of SMEC and benchmarked to the basic rates of NPC. The components for pricing comprise a Basic Energy Rate (“BER”), also on a time-of-use basis, and a monthly Basic Energy Rate Adjustment (“BERA”) charge similar to the ACA charge of NPC.

The components for the BERA include adjustments for fuel, foreign exchange and inflation costs. Any changes to the level of the BER and/or the BERA are not affected by movements in the charges of NPC.

Fuel Supply

SMC Global Power has a coal supply agreement with Bumi Resources for the supply and delivery of coal to SMC Global Power, which SMC Global Power in turn supplies to the Sual Power Plant. The agreement is effective until December 2014, subject to renewal for a further five years as may be mutually agreed between the parties.

Under the coal supply agreement, Bumi Resources is required to supply a total of 33 shipments, each comprising 65,000 metric tons during 2010. However, for the years 2011 to 2014, the amount of coal to be supplied by Bumi Resources will depend on the election of SMC Global Power in accordance with the provisions of the coal supply agreement.

Pricing under the coal supply agreement is subject to adjustment based on certain standards applicable to the quality or grade of the coal delivered by Bumi Resources. For the years 2011 to 2014, Bumi Resources and SMC Global Power are required to negotiate on an annual basis and mutually agree upon the price for the coal supplied by Bumi Resources for the following year, failing which, the price to be used will be equivalent to the Global Coal Newcastle Monthly Index of the month prior to the date of the shipment multiplied by 1.04 until such time as the coal price for the relevant contract year is settled between the parties.

Operations and Maintenance

Under the Sual ECA, TeaM Energy is required, at its own cost, to be responsible for the management, operation, maintenance, including the supply of consumables and spare parts, and the repair of the Sual Power Plant until the date of transfer (to NPC or to SMC Global Power, as the case may be), and shall use its best endeavors to ensure that during such period the Sual Power Plant is in good operating condition and capable of converting fuel supplied by SMC Global Power under the Sual IPPA Agreement, into electricity in a safe and reliable manner.

Ilijan Power Plant

The Ilijan Power Plant commenced commercial operations on June 5, 2002, and is located on a 60-acre site at Arenas Point, Barangay Ilijan, Batangas City. The Ilijan Power Plant was constructed and is owned by KEPCO Ilijan Corporation pursuant to a 20-year ECA with NPC under a BOT scheme that expires on June 4, 2022. NPC supplies natural gas to the Ilijan Power Plant from the Malampaya field in Palawan. The Ilijan Power Plant consists of two blocks with a rated capacity of 600 MW each.

The power plant can also run on diesel oil stored on site. On April 16, 2010, SMC successfully bid for the appointment to be the IPPA for the Ilijan Power Plant and received a notice of award on May 5, 2010. On June 10, 2010, SMC and SPPC, a wholly owned subsidiary of SMC Global Power, entered into an assignment agreement with assumption of obligations whereby SMC assigned all of its rights and obligations with respect to the Ilijan Power Plant to SPPC, which assumed administration of the Ilijan Power Plant on June 26, 2010 in accordance with an IPPA agreement with PSALM ("Ilijan IPPA agreement").

Ilijan IPPA

PSALM, NPC and SMC Global Power (through SPPC) entered into the Ilijan IPPA agreement pursuant to which SMC Global Power has the right to manage, control, trade, sell or otherwise deal in the electrical generation capacity of the Ilijan Power Plant. SMC Global Power must pay fixed monthly payments comprising both a U.S. Dollar and Philippine Peso component. In addition, SMC Global Power must pay monthly generation payments comprising a "must pay" amount for electricity sold up to a given volume (the "Must Pay Volume") and a variable amount for electricity sold in excess of the Must Pay Volume. The "must pay" amount in a given month is the sum of: 80% of the statutory rate SMC Global Power charges Meralco for supplying electrical power under the offtake agreement between SMC Global Power and Meralco for the given month multiplied by a factor equal to the volume sold (the "T1 Volume"), where the T1 Volume cannot exceed the Must Pay Volume; and 80% of the price for the electrical power sold to WESM during the month, multiplied by a factor equal to the Must Pay Volume less the T1 Volume, where such factor may not be less than zero.

The variable amount of the monthly generation payment is payable for electricity sold in excess of the Must Pay Volume for that month and is calculated as a base rate plus an index based on the cost of natural gas, the U.S. Dollar/Philippine Peso exchange rate and the efficiency of the Ilijan Power Plant.

The Ilijan IPPA agreement also requires SMC Global Power to maintain a performance bond in favor of PSALM equivalent to US\$60 million, and perform the obligations of NPC in its PSCs, including the obligation to procure electricity at its own cost to meet deficiencies, in cases where the Ilijan Power Plant is unable to supply the contracted power.

Under the Ilijan IPPA agreement, SMC Global Power has the right to acquire the Ilijan Power Plant in June 2022, which is the end of the cooperation period between NPC and KEPCO Ilijan Corporation under the ECA with KEPCO Ilijan Corporation, or on some earlier date due to certain events such as changes in law or non-performance by KEPCO Ilijan Corporation under the ECA.

Power Offtakers

The Ilijan Power Plant PSCs generally require its offtakers to take or pay for, within a contract year, a mutually agreed MEQ, and such offtakers would be allowed to exceed up to 20% of its MEQ. Any power taken in excess 20% of the MEQ is subject to a premium on the base tariff rate imposed by SMC Global Power.

For PSCs assigned by NPC to SMC Global Power in respect of the Ilijan Power Plant, the pricing structure is similar to that provided under the PSCs assigned by NPC to SMC Global Power in respect of the Sual Power Plant. Likewise, pricing for PSCs entered into by SMC Global Power with new offtakers on a bilateral basis for the Ilijan Power Plant (or with those offtakers under previously assigned PSCs which have expired), is based on the BER and the BERA structure.

Fuel Supply

NPC is responsible for securing the natural gas and diesel fuel supply to the Ilijan Power Plant. Under a fuel supply and management agreement with Shell Exploration B.V. and Occidental Philippines, Inc., NPC supplies natural gas to the Ilijan Power Plant through a 480 km undersea pipeline from the Camago-Malampaya field in Palawan to the Shell Refinery in Tabangao. From there, the natural gas is transported through a 16-in-diameter onshore pipeline running 15 km to the power plant.

Operations and Maintenance

KEPCO Ilijan Corporation currently owns and is responsible for the operations and maintenance of the Ilijan Power Plant for 20 years effective from June 5, 2002. KEPCO Ilijan Corporation is majority owned by the Korea Electric Power Corporation (“KEPCO”), with its partners, Mitsubishi Corporation and TeaM Energy. KEPCO Ilijan Corporation is a stock corporation incorporated in the Philippines, in accordance with the Corporation Code and the Foreign Investment Act of 1991 (the “FIA”). Under the ECA for the Ilijan Power Plant, KEPCO Ilijan Corporation shall operate the Ilijan Power Plant in accordance with the operating criteria and guidelines provided therein, including output of 1,200 MW guaranteed net contracted capacity, base load operation, spinning reserve capability, a minimum stable load of not more than 30% of the unit rated generating capacity, and a ramp rate of not less than 5% of the rate unit generator capacity per minute.

San Roque Power Plant

The 345 MW San Roque multi-purpose hydroelectric power plant in San Manuel, Pangasinan commenced operations on May 1, 2003 and is a peaking plant that was constructed by a consortium composed of Marubeni Corporation, Sithe Philippines Holdings, Ltd., and Italian-Thai Development Public Company Limited pursuant to a PPA with NPC under a BOT scheme (the “San Roque PPA”).

The San Roque Power Plant utilizes the Agno River for power generation and irrigation and contributes to flood control and water quality improvement for the surrounding region, and comprises three power generation units of 115 MW each. The San Roque Power Plant provides an annual energy generation of 1,065 GWh from the 345 MW hydroelectric power plant, the irrigation of approximately 34,450 hectares of agricultural land, storage of water that would otherwise flood the Pangasinan plains, and improvement of water quality of the Agno River which, otherwise, would pollute the downstream rivers.

On December 15, 2009, SPDC, a wholly owned subsidiary of SMC Global Power, successfully bid for the appointment to be the IPPA for the San Roque Power Plant and received a notice of award on December 28, 2009. SPDC assumed administration of the San Roque Power Plant on January 26, 2010 in accordance with an IPPA agreement with PSALM (the “San Roque IPPA agreement”). PSALM remains responsible under a PPA to remunerate the IPP of the San Roque Power Plant for the electricity it produces.

San Roque IPPA

PSALM, NPC and SMC Global Power (through SPDC) entered into the San Roque IPPA agreement pursuant to which SMC Global Power has the right to manage, control, trade, sell or otherwise deal in the electrical generation capacity of the San Roque Power Plant, while NPC, which owns and operates the dam and related facilities thereof, may be requested to obtain and maintain water rights necessary for the testing and operation of the power plant. SMC Global Power is required to assist PSALM so that the San Roque Power Plant can draw water from the Agno River required by the power plant and necessary for it to generate the electricity required to be produced under the San Roque PPA of NPC with San Roque Power Corporation (“SRPC”). In addition, SMC Global Power must pay fixed monthly payments comprising both a U.S. Dollar and Philippine Peso component. These fixed monthly payments are reduced when there is a Non-Delivering Day for reasons not attributable to SMC Global Power. In addition, SMC Global Power has a Must Pay Volume fee of ₱1.30 per kWh. The Must Pay Volume fee is a fixed amount, payable to PSALM upon receipt of the billing.

The San Roque IPPA agreement also requires SMC Global Power to maintain a performance bond in favor of PSALM equivalent to US\$20 million and perform the obligations of NPC in its PSCs, including the obligation to procure electricity at its own cost to meet deficiencies, in cases where the San Roque Power Plant is unable to supply the contracted power.

Under the San Roque IPPA agreement, SMC Global Power has the right to acquire the San Roque Power Plant in May 2028, which is the end of the cooperation period between NPC and SRPC under the San Roque PPA, or on some earlier date due to certain events such as changes in law or nonperformance by SRPC under the San Roque PPA.

Power Offtakers

Since the San Roque Power Plant is a peaking plant, all of its output is traded on the WESM and SPDC has no PSC with any party. Under the terms of the San Roque PPA, power and energy are delivered to SMC Global Power at the delivery point (the high voltage side of the step-up transformers) located at the perimeter fence of the San Roque Power Plant site. SMC Global Power is responsible for contracting with the NGCP to wheel power from the delivery point.

Water Rights

The generated output energy of the San Roque Power Plant is limited by the Irrigation Diversion Requirements set by the National Irrigation Administration. Water allocation is usually dictated by rule curve that is derived from historical data of river flows and water demands. A rule curve shows the minimum water level requirement in the reservoir at a specific time to meet the particular needs for which the reservoir is designed. The rule curve must generally be followed except during periods of extreme drought and when public interest requires. In general, the rule curve dictates the following:

- **Water Level Above The Upper Rule Curve** — All demands for water supply and irrigation are met and electricity can be generated at the full capacity of the turbine units. Excess inflow is discharged through the spillway. Water released through the spillway is controlled and regulated by the NPC Dam Office personnel.
- **Between Upper And Lower Rule Curves** — All demands for water supply and irrigation are satisfied. Generation of electricity is limited to the released water for water supply and irrigation. Further water releases for power generation are allowed provided that the auxiliary units are utilized first before main units.
- **Water Level Below Lower Rule Curve** — The remaining water in the reservoir is reserved for water supply and irrigation. Generation of electricity is limited to these water releases. No further water release for power generation is allowed.

In 2010, the water level in the San Roque Power Plant dam has consistently been below the rule curve. However, the National Irrigation Administration permitted the San Roque Power Plant to continue operations during this time due to downstream irrigation requirements caused by drought during the same period.

Generally, the output energy of San Roque Power Plant is high during planting seasons which covers the months of December through April (dry planting season) and July through September (wet planting season). The water releases from the dam, and thus, energy generation, during the dry planting season is much higher due to the absence of rain. The water rights of NPC are used by the San Roque Power Plant and NPC, until the date of transfer of the San Roque Power Plant to NPC (or SMC Global Power, as the case may be), must obtain such renewals or extensions as may be required to maintain the water rights in full force and effect at all times. NPC derives its water rights from a permit granted by the National Water Resources Board.

Operations and Maintenance

SRPC is responsible for the operations and maintenance of the San Roque Power Plant for 25 years effective May 1, 2003. SRPC is owned by Marubeni and Kansai-Electric and is a stock corporation incorporated in the Philippines, in accordance with the Corporation Code and the FIA.

Under the San Roque PPA, SRPC is responsible for the management, operation, maintenance and repair of the San Roque Power Plant at its own cost until transfer to NPC or SMC Global Power, as the case may be. As operator, SRPC is entitled to conduct the normal inspection, regular maintenance, repair and overhaul for a period of 15 days for each unit comprising the San Roque Power Plant. In addition, SRPC has the right to enter into contracts for the supply of materials and services, including contracts with NPC; appoint and remove consultants and professional advisers; purchase replacement equipment; appoint, organize and direct staff; manage and supervise the power plant; establish and maintain regular inspection, maintenance and overhaul procedures; and otherwise run the power plant within the operating parameters set out in the San Roque PPA.

The operating fee is the product of the contracted capacity for the contract year in kW, which is nominated annually, multiplied by ₱250 per kW per month. This fee is in addition to the capital recovery fee and covers the fixed operating and maintenance costs of the power structures and equipment.

Meralco

SMC directly and indirectly holds shares of Meralco representing approximately 32.04% of the issued and outstanding common shares of Meralco. Meralco is the Philippines' largest distributor of electrical power and is the only distributor of electric power for Metro Manila. Meralco holds the power distribution franchise for approximately 22 cities and 89 municipalities in the Philippines. The common shares of Meralco are listed on the PSE.

The value of the Meralco investment, based on the closing market price for Meralco common stock of ₱60.60 as of December 28, 2012, is approximately ₱96,428 million.

Related Coal Investments

SMC Global Power has invested in certain coal mining assets in the Philippines. Such assets are in a preliminary stage of exploration and no results as to their actual viabilities were available as of December 31, 2012. The mines of SMC Global Power are not expected to provide fuel for any of its power plants since the Sual Power Plant runs on high-performance coal, and high-performance coal is not found naturally in the Philippines.

Competition

SMC Global Power is one of the largest IPPAs in the country, with a 17% share of the power supply of the national grid, and a 22% market share of the Luzon grid. Its main competitors are the Lopez Group and the Aboitiz Group. The Lopez Group holds significant interests in First Gen Corporation and Energy Development Corporation, while the Aboitiz Group holds interests in Aboitiz Power Corporation and Hedcor, Inc, among others.

With the Philippine government committed to privatizing the majority of PSALM-owned power generation facilities and the establishment of WESM, the generation facilities of SMC Global Power will face competition from other power generation plants that supply the grid during the privatization phase. Multi-nationals that currently operate in the Philippines and could potentially compete against SMC Global Power in the privatization process include Korea Electric Power Corporation, Marubeni, Tokyo Electric Power Corporation, AES Corporation and Sumitomo, among others. Several of these competitors have greater financial resources, and have more extensive operational experience and other capabilities than SMC Global Power, giving them the ability to respond to operational, technological, financial and other challenges more quickly than SMC Global Power. SMC Global Power will face competition in both the development of new power generation facilities and the acquisition of existing power plants, as well as competition for financing for these activities. The performance of the Philippine economy and the potential for a shortfall in the Philippines' energy supply have attracted many potential competitors, including multinational development groups and equipment suppliers, to explore opportunities in the development of electric power generation projects within the Philippines. Accordingly, competition for and from new power projects may increase in line with the long-term economic growth in the Philippines.

Safety, Health and Environmental Regulation and Initiatives

Power generation operations are subject to extensive, evolving and increasingly stringent safety, health and environmental laws and regulations. These laws and regulations include the Philippine Clean Air Act, The Philippine Clean Water Act of 2004 (the "Clean Water Act"), Toxic Substances and Hazardous and Nuclear Waste Control Act of 1990, and Occupational Safety and Health Standard of 1989 of the DOLE, as amended. Such legislation addresses, among other things, air emissions, wastewater discharges as well as the generation, handling, storage, transportation, treatment and disposal of toxic or hazardous chemicals, materials and waste. It also regulates workplace conditions within power plants and employee exposure to hazardous substances. The Occupational Safety and Health Standard, meanwhile, was formulated to safeguard the workers' social and economic well-being as well as their physical safety and health.

The management of SMC Global Power believes that the IPPs for each of the IPPA power plants comply in all material respects with all applicable safety, health and environmental laws and regulations.

Insurance

Pursuant to the IPPA arrangements of SMC Global Power, the IPPs associated with the IPPA power plants are responsible for maintaining insurance for all of the facilities, equipment and infrastructure for the power plants of

SMC Global Power, with the exception of the dam and spillway of the San Roque Power Plant, for which NPC retains responsibility for insuring.

INFRASTRUCTURE BUSINESS

SMC has made investments in the Philippines' infrastructure sector through SMHC consisting of investments in concessions for toll roads, an airport and a light rail system, certain details of which are set forth in the table below:

	<u>% SMC ownership interest</u>	<u>Expected project cost</u> (in millions)		<u>Concession length</u>	<u>Construction period</u>
TPLEX Tollway	35% ⁽¹⁾	₱21,600	US\$502.33 ⁽⁴⁾	35 years	48 months
Boracay Airport	98.2%	₱ 5,600	US\$130.23 ⁽⁴⁾	25 years	66 months
MRT-7 Light Rail Project	51% ⁽²⁾	₱68,100	US\$ 1,540 ⁽⁴⁾	25 years	42 months
SLEX	37.22% ⁽⁵⁾	None ⁽³⁾		25 years	
Skyway	60.83% ⁽⁶⁾	None ⁽³⁾		25 years	

Notes:

- (1) Ownership through Private Infra Dev Corporation, through Rapid Thoroughfares, Inc.
- (2) Ownership through ULC BVI through SMHC equity interest.
- (3) All major capex have been completed prior to equity acquisition.
- (4) Conversion rate used US\$1.00 = ₱43.00.
- (5) Indirect ownership of SMHC in South Luzon Tollway Corporation.
- (6) Indirect ownership of SMHC in CMMTC.

Philippine Infrastructure Industry

Under the current administration, the Philippine government has accelerated the implementation of a number of key infrastructure projects. It has created the Public-Private Partnership Center as it recognizes the essential role of the private sector as the main engine for national growth and development. In accordance with this, pertinent incentives will be provided to stimulate private resources for the purpose of financing the construction, operation and maintenance of infrastructure and development projects normally undertaken by the Philippine government.

Private sector investors will be selected through open competition under fair and transparent terms. All interested investors will be given a level playing field with reasonable returns and appropriate sharing of risks without compromising the protection of public interests. Through this program, end users will be provided with adequate, safe, efficient, reliable, and reasonably-priced infrastructure services.

Currently, the list of infrastructure projects under the PPP include:

- (i) *Rail Sector* — Light Rail Transit Line 1 Cavite Extension, Integrated Luzon Railway Project*, Automatic Fare Collection System for Lines 1, 2 and 3;
- (ii) *Road Sector* — NAIA Expressway Phase II, NLEX-SLEX Connector Road, Cavite and Laguna Expressway, Plaridel Bypass Toll Road*;
- (iii) *Airport Sector* — Laguindingan Airport, Mactan- Cebu International Airport Passenger Terminal Building, New Bohol (Panglao) Airport; and
- (iv) *Others* — Batangas-Manila Natural Gas Pipeline Project*.¹

The government has increased infrastructure spending to boost domestic growth and has allocated ₱328 billion under the national budget for 2013 for Public Sector Infrastructure Budget, a great portion of which is dedicated to the share of the Government in the PPP projects.²

Competitive Strengths

Synergies with the established businesses of SMC. The strengths of SMC in its established businesses could be leveraged to ensure successful execution of infrastructure projects.

¹ From the PPP Center list as of March 2013. Projects with * are undergoing procurement procedures for advisors and are estimated to be rolled out early 2014.

² Department of Budget and Management's publication of Public Sector Infrastructure Budget.

Brand strength and size. SMC is among the largest and most widely recognized companies in the Philippines with a continuing commitment in the involvement for the development of the country.

Ability to finance acquisitions. Infrastructure projects require long-term and project financing. SMC has an advantage in financing its PPP projects due to its long operating history as a publicly listed company and the trust built up with investors, its size and balance sheet strength and its recognition in the international capital markets.

Business Strategies

Focusing on the improvement of infrastructure projects in the Philippines. SMC believes there are significant opportunities in building and participating in infrastructure projects in a growing economy that has historically under-invested in infrastructure. SMC intends to take advantage of these opportunities to expand its infrastructure operations through participation in the PPP project initiatives of the Government.

Potential to extract synergies across businesses. Areas and projects being developed by the infrastructure business of SMC present opportunities for its other businesses. For example, the TPLEX, the Boracay Airport and the MRT-7 rail and the road projects are expected to complement and present opportunities for fuel and oil, energy, and telecommunications businesses of SMC, as well as improve the distribution network for food and beverage business of SMC.

Operations

TPLEX Tollway

The Philippine government, through the National Economic Development Authority, which administers the National Economic Plan, has proposed and is implementing a 20-year plan to significantly expand the expressway/tollway system from and around Metro Manila. A significant part of that plan is the construction of an 88.58 km two-lane toll expressway from Tarlac, through Pangasinan to La Union, north of Manila (“TPLEX”). The TPLEX expressway is expected to be integrated with other major expressways (including the North Luzon Expressway and Subic-Clark-Tarlac Expressway) to expand the road/expressway network in and around Metro Manila by 325 kilometers. Construction commenced on the expressway in July 2010. The initial Subic-Clark-Tarlac Expressway to Gerona (section 1a, 16.11 kilometers) is projected to be completed by 2013, with revenue collection projected to commence immediately after, while the remainder of the expressway is projected to be completed by in additional three phases, starting with Gerona to Carmen (section 1b, 32.48 km) by April 2014, Carmen to Urdaneta (section 2, 9.47 km) by August 2014 and finally Urdaneta to Rosario, La Union (section 3, 30.41 km) by December 2015.

In August 2009, SMC made its first infrastructure investment by acquiring a 35% stake in PIDC. PIDC holds the 35-year build-transfer-operate concession for TPLEX. PIDC is a joint venture among D.M. Consunji, Inc. (32.21%), D.M. Wenceslao & Associates, Inc (11.67%) and eight other contractor shareholders. D.M. Consunji, Inc. has constructed large projects in the Philippines for over 50 years, including hotels, malls, convention centers and the MRT-3 Metro Rail Transit system. SMC has an option to increase its interest in PIDC to up to 51%.

The project cost for the development of TPLEX is estimated at ₱21,600 million, which will be funded by a combination of debt (45.80%), equity (40.80%) and Philippine government subsidy (13.40%) which is available at the start of construction of Section 3 of TPLEX. The current equity funding commitment of SMC is ₱2,686 million, with ₱1,917 million having already been provided. On September 12, 2011, Rapid Thoroughfares Inc. paid ₱1,111 million as deposit for future stock subscription to 1,111,228 common shares of PIDC. One of the conditions for the issuance of the subscribed shares of Rapid Thoroughfares Inc. is the approval of the SEC and the Toll Regulatory Board of the increase in the authorized capital stock of PIDC. The SEC has approved the increase in authorized capital stock of PIDC, and the approval of the Toll Regulatory Board is currently pending.

Boracay Airport

As of December 31, 2012, SMC had a 98.2% stake in Caticlan International Airport Development Corp. (subsequently renamed Trans Aire Development Holdings Corporation). TADHC holds a 25-year build-rehabilitate-operate-transfer concession granted by the Republic of the Philippines, through the Department of Transportation and Communications of the Philippines (“DOTC”), to develop and operate Boracay Airport. The remaining interest was held by Akean Resorts Corporation, a non-affiliated entity.

Boracay airport is the principal gateway to Boracay Island, a popular resort for passengers traveling from Manila. Due to a short runway, the airport currently is able to accommodate only turbo propeller airplanes. The airport

has experienced rapid growth in passenger volumes in the last decade, growing on average 23.3% a year from 1991. In 2012, approximately 738,000 tourists passed through Boracay Airport.

The planned expansion of the airport is expected to be completed in a number of stages and involves:

- upgrading and extending the runway, which is currently 950 meters long and 30 meters wide, to 2,600 meters long and 45 meters wide to accommodate larger international and domestic aircraft;
- upgrading of the Boracay Airport and its facilities to comply with International Civil Aviation Organization standards and the Manual of Standards for Aerodromes of the Civil Aviation Authority of the Philippines (“CAAP”);
- conducting extensive landscape remediation to lower hills at one end of the runway;
- replacing the current 1,000 square meter terminal with a new world class passenger and cargo terminal;
- improving road networks around Boracay Airport and its facilities; and
- upgrading air navigational systems.

The endorsement of the Director General of CAAP for the preparation of the Detailed Design Engineering (“DDE”) has already been obtained. The DDE is now being prepared by an international airport design firm.

The concession agreement is valid for 25 years, ending in 2035. On January 15, 2012, the passenger terminal fee was increased from ₱20 to ₱200.

MRT-7 Light Rail and Road Project

In October 2010, SMC acquired a 51% stake in Universal LRT, which holds the BOT concession for MRT-7, a planned expansion of the metro rail system in Manila, home to over 10 million inhabitants. MRT-7 is one of several rail extension projects to the existing metro rail system which services Metro Manila. It is expected to take three and a half years from the start of the construction. This includes a 22 km six-lane highway that will connect the North Luzon Expressway to the intermodal transport terminal in San Jose del Monte City, Bulacan and a 22 km mostly elevated MRT with 14 stations that will start from San Jose del Monte City, Bulacan and end at the integrated LRT-1 / MRT-3 / MRT-7 station at North EDSA. Universal LRT will operate and manage the system for 25 years while gradually transferring ownership of the system to the Philippine government in proportion to payments of semi-annual capacity fees. Under the Build-Gradual-Transfer-Operate-Maintain-and-Manage scheme, the Philippine government will pay US\$2.69 billion over 20 years through amortized payments. The project is estimated to cost US\$1,540 million, based on National Economic Development Authority (“NEDA”) approval on October 15, 2012, which is to be funded 25% by equity and 75% by debt. To date, the Performance Undertaking has yet to be released by the Department of Finance of the Philippines. The said Performance Undertaking is a written confirmation of the Philippine government that it will perform its obligations under the concession agreement for the MRT-7 project.

SLEX and Skyway

SMHC has acquired 46.53% stake in AAI, a company which has obtained ownership of the following: (i) 80% stake in South Luzon Tollway Corporation, which holds a 30-year concession (valid until 2035) to operate the 36-kilometer South Luzon Expressway (“SLEX”); and (ii) 50.51% stake in CMMTC, a company which holds a 25-year concession to operate the 16.38-kilometer (Stages 1 and 2) South Metro Manila Skyway Project which links the EDSA and Alabang. SLEX is one of the three major expressways that links Metro Manila to key southern provinces.

SMHC has a 60% equity interest in Alloy Manila Toll Expressways Inc. which has a 30% interest in Manila Toll Expressway Systems, Inc. (“MATES”). MATES is the operating and maintenance company for the SLEX.

OTHER OPERATIONS AND INVESTMENTS

Copper and Gold Mining

SMC through Coastal View Exploration Corporation (“**Coastal View**”) acquired in October 2010 a 10.10% stake in Indophil which holds a 37.50% beneficial ownership in Sagittarius Mines Inc., which in turn holds a 40% controlling equity stake in a joint venture to explore, develop and operate the Tampakan mine in the Philippines. The mine is estimated to have 2.5 billion metric tonnes of 0.60% copper and 0.2 grams per ton gold. If proven, the mine would be one of the world’s largest underdeveloped copper-gold deposits, potentially the Philippines’ largest mine and the world’s fifth largest copper mine by 2016. Currently, Coastal View has a 3.99% stake in Indophil pursuant to dilution from the latter’s subsequent rights offerings.

Telecommunications

SMC has made investments in the Philippines' telecommunications sector through acquisitions of stakes in Liberty, BellTel and ETPI.

Liberty Telecom

As of December 31, 2012, SMC owned 41.48% of Liberty Telecommunications Holdings Inc., in partnership with G.S.P.C. Qtel Westbay Holding (26.75%), Wi-Tribe Asia Limited (5.90%) and White Dawn Solutions Holdings, Inc. (18.36%), with the remaining shares owned by the public. Liberty is a telecommunications carrier offering services including nationwide telephone service, data communications, inter-exchange carrier services and international voice and data connectivity services.

BellTel

SMC acquired 100% of BellTel in 2010, a full-service telecommunications company which is licensed to provide a range of services throughout the Philippines. The telecommunication license of BellTel authorizes it to provide data services throughout the Philippine archipelago and telephony to all central business districts and special economic zones. BellTel was one of the first companies to deploy point-to-multipoint fixed wireless access technologies delivering multiple product offerings. BellTel has also entered into strategic alliances with operators of underutilized telecommunications infrastructures, such as hybrid fiber-coaxial and fiber optic networks, giving it several cost-effective last mile options for rapid service deployment. In addition, BellTel holds licenses in the 1.7, 3.5 and 24 GHz spectra, which enable it to provide a wide array of wireless broadband products and services.

ETPI

In 2011, SMC, through Vega, acquired 100% of the outstanding and issued shares of stock of AGNP, the beneficial owner of approximately 40.0% of ETPI. On October 20, 2011, SMC through its wholly owned subsidiary, SMESI, acquired an additional 37.7% of the outstanding and issued shares of stock of ETPI, bringing its total indirect equity interests in ETPI to 77.7% as of December 31, 2012. ETPI is a provider of voice, data and internet services to the corporate, government and business process outsourcing market.

Banking

SMC through SMPI made a series of acquisitions of BOC shares in 2007 and 2008 and has a current ownership of 39.9%. However, SMPI, together with the other stockholders of BOC, executed a share purchase agreement dated May 8, 2012 with CIMB Bank Berhad for the sale of a 58% equity interest in BOC. As of December 31, 2012, the share purchase was still pending completion.

Airline

On April 3, 2012, SMC, through SMEII, acquired a 49% equity interest each in Trustmark Holdings Corporation and Zuma Holdings and Management Corporation, the holding companies of PAL and Air Phil, respectively. The investment provides an opportunity for SMC to diversify into an industry which has synergies with the existing businesses of SMC. Such investment will likewise augment and supplement the ongoing enhancement of the operations of PAL and Air Phil, and the implementation of the fleet modernization programs with the end in view of enhancing the efficiency, competitiveness and profitability of PAL and Air Phil.

EMPLOYEES

As of December 31, 2012, the SMC Group had over 18,000 employees. Substantially all of the employees are based in the Philippines and other areas in the Asia-Pacific region. As of December 31, 2012, the approximate number of employees in each of the businesses is set forth below:

<u>Business</u>	<u>Number of employees</u>
Beverages	5,903
Food	3,754
Energy	65
Packaging	3,159
Fuel and Oil (Petron)	2,689
Infrastructure	3
Other Operations and Investments	2,702
Total	18,275

As of December 31, 2012, approximately 28.0% of the employees were parties to various collective bargaining agreements. Employees of SMC are not members of any labor unions. On the other hand, a total of 39 labor unions represent the employees of the subsidiaries of SMC. Since 2003, the SMC Group has not experienced any strikes or work stoppages. The SMC Group considers its relationship with its employees to be good.

In addition to the statutory benefits, SMC initiates benefits to provide for the increased security of its employees in the following areas: health care, leaves, miscellaneous benefits, loans and financial assistance applicable to a variety of uses, retirement benefits, and survivor security and death benefits.

Within the ensuing 12 months, SMC may require additional hiring of employees to support its business expansion, the number of which cannot be determined.

COMPLIANCE WITH ENVIRONMENTAL LAWS

SMC is in compliance with environmental laws, except where such non-compliance will not have a material adverse effect on the business of SMC. On an annual basis, operating expenses incurred by SMC to comply with environmental laws are not significant or material relative to the total costs and sales of SMC.

INSURANCE

SMC has several all-risk policies that cover its facilities and inventories against a variety of risks, including, among others, liability arising from fire, lightning, catastrophic perils (typhoon, flood, earthquake, and volcanic eruption), explosion, civil commotion, riot/strike, malicious damage, other perils. Certain policies cover machinery breakdown, terrorism and sabotage, and business interruption for selected facilities.

In addition to the all-risk policy, SMC maintains various general liability and product liability insurance policies covering its Philippine and international operations. The products liability and insurance policy insures against injuries to third parties for all of the products of SMC that are exported.

SMC also has marine cargo insurance policies to cover domestic and international shipment of goods and equipment. All insurance policies are procured at the SMC level except for Petron and certain international companies. The SMC policies are secured with leading Philippine insurance companies that are generally re-insured with Class “A” international re-insurance companies.

LEGAL PROCEEDINGS

The SMC and its subsidiaries are parties to a variety of legal proceedings arising out of the ordinary course of business, including legal proceedings with respect to labor, product liability and other matters. SMC and its subsidiaries are vigorously defending all litigation pending against them. While the results of the litigation cannot be predicted with certainty, SMC believes that the final outcome of the proceedings will not have a material adverse effect on its financial condition and results of operations.

SMC has initiated the appropriate actions to contest an assessment imposed by the SEC-Corporation Finance Department of a fine in connection with the filing of the Statement of Initial Beneficial Ownership and Statement of Changes in the Beneficial Ownership (SEC Form 23-A and B, respectively) under the SRC.

Legal Proceedings Involving SMC

In March 1986, SMC agreed to purchase Common Shares registered in the names of the Coconut Industry Investment Fund (CIIF) companies pursuant to a stock purchase agreement, with payment to be made in four installments. After the first installment was paid, the Philippine Presidential Commission on Good Government (“PCGG”), which is authorized to recover certain assets of the late Philippine President Ferdinand Marcos, sequestered all of the CIIF companies’ Common Shares, including those that had been sold to SMC.

On March 26, 1986, SMC entered into a compromise agreement with the CIIF companies and United Coconut Planters Bank (the administrator of the CIIF), pursuant to which the sale of Common Shares covered by the first payment installment was recognized as valid as among those parties. As a result, in 1991, the Compromise Agreement was implemented and 25.45 million Common Shares of SMC previously registered in the names of the CIIF companies reverted into treasury shares. On September 14, 2000, the Philippine Supreme Court upheld a resolution of the Philippine Anti-Graft Court (*Sandiganbayan*) that required SMC to deliver the 25.45 million treasury shares to the PCGG and pay PCGG the corresponding dividends. After consultation by SMC with its financial and legal advisors regarding this resolution of the Anti-Graft Court, SMC did not deliver the 25.45 million treasury shares to PCGG. An extensive discussion on this matter is contained in the Notes to the Financial Statements of SMC under the heading “Equity”, which is included in this Offering Memorandum.

On June 30, 2011, the PCGG filed with the Supreme Court an Urgent Motion to Direct the SMC to comply with the resolution of the September 14, 2000 resolution of the Anti-Graft Court. On March 30, 2012, SMC filed a Comment on the said Urgent Motion in compliance with the Supreme Court's Resolution dated December 13, 2011. There are no new developments on this matter as of the date of this Offering Memorandum.

Deficiency Excise Tax

On April 12, 2004 and May 26, 2004, SMC was assessed by the BIR for deficient excise tax payments in the amount of ₱907 million for one of its beer products for the period from November 1999 to January 2004. SMC contested the assessment before the Philippine Court of Tax Appeals ("CTA") in September 2004.

On October 18, 2011, the CTA (1st Division) rendered its decision cancelling and setting aside the deficiency excise tax assessments against SMC, granting the latter's claim for refund and ordering the BIR Commissioner to refund or issue a tax credit certificate in its favor in the amount of ₱781 million, representing erroneously, excessively and/or illegally collected and overpaid excise taxes during the period from February 1, 2004 to November 30, 2005. A motion for reconsideration filed by the BIR Commissioner on the aforesaid decision has been denied and the Commissioner elevated the decision to CTA *En Banc* for review, which was dismissed in a Decision dated October 24, 2012. The subsequent Motion for Reconsideration filed by the Commissioner was likewise denied.

Legal Proceedings Involving Petron

Assessments Involving Tax Credit Certificates

In 1998, the BIR issued a deficiency excise tax assessment against Petron. The assessment relates to Petron's use of ₱659 million worth of Tax Credit Certificates ("TCCs") from 1993 to 1997. The TCCs were transferred to Petron by suppliers as payment for fuel purchases. The BIR appealed the ruling of the CTA that Petron was a qualified transferee of the TCCs and that the collection by the BIR of the alleged deficiency excise taxes was contrary to law. On March 21, 2012, the Court of Appeals promulgated a decision in favor of Petron and against the BIR, which decision affirmed the ruling of the CTA.

The BIR elevated the case to the Supreme Court through a petition for review on *certiorari* dated December 5, 2012, which petition remains pending as of the date of this Offering Memorandum.

Pandacan Terminal Operations

In November 2001, the City of Manila enacted Ordinance No. 8027 reclassifying the areas occupied by the oil terminals of Petron, Shell and Chevron from industrial to commercial. This reclassification made the operation of the oil terminals in Pandacan, Manila illegal. However, in June 2002, Petron, together with Shell and Chevron, entered into a Memorandum of Understanding ("MOU") with the City of Manila and the DOE, agreeing to scale down operations, recognizing that this was a sensible and practical solution to reduce the economic impact of Ordinance No. 8027. In December 2002, the Social Justice Society ("SJS") filed a petition with the Supreme Court seeking enforcement of Ordinance No. 8027. In April 2003, Petron filed a petition with the Regional Trial Court ("RTC") to annul Ordinance No. 8027 and enjoin its implementation. On the basis of a *status quo* order issued by the RTC, Mayor of Manila ceased implementation of Ordinance No. 8027.

The City of Manila subsequently issued the Comprehensive Land Use Plan and Zoning Ordinance ("Ordinance No. 8119"), which granted Petron and other non-conforming establishments a seven-year grace period to vacate.

However, on March 7, 2007, in the case filed by SJS, the Supreme Court rendered a decision (the "March 7 Decision") directing the Mayor of Manila to immediately enforce Ordinance No. 8027. On March 12, 2007, Petron, Shell and Chevron, filed motions with the Supreme Court seeking intervention and reconsideration of the March 7 Decision.

In its February 13, 2008, resolution (the "February 13 Resolution"), the Supreme Court declared Ordinance No. 8027 valid, and dissolved all existing injunctions against the implementation of the Ordinance No. 8027, and directed Petron, Shell and Chevron to submit their relocation plans to the RTC. Petron, Shell and Chevron have sought reconsideration of the February 13 Resolution. In compliance with the February 13 Resolution, Petron, Shell and Chevron have submitted their relocation plans to the RTC.

In May 2009, the Mayor of Manila approved Ordinance No. 8187 ("Ordinance No. 8187"), which repealed Ordinance No. 8027 and Ordinance No. 8119 and permitted the continued operations of the oil terminals in Pandacan.

On August 24, 2012, the RTC of Manila ruled that Section 23 of Ordinance No. 8119 relating to the reclassification of subject oil terminals had already been repealed by Ordinance No. 8187; hence any issue

pertaining thereto had become moot and academic. The RTC of Manila also declared Section 55 of Ordinance No. 8119 null and void for being in conflict with the Water Code. Nonetheless, the RTC upheld the validity of all other provisions of Ordinance No. 8119.

On September 25, 2012, Petron sought clarification and partial consideration of the August 24 decision of the RTC and prayed for the nullification of the entire Ordinance No. 8119. In an order dated December 18, 2012, the RTC of Manila denied the motion filed by Petron. Petron filed a notice of appeal on January 23, 2013. In an order dated February 6, 2013, the RTC of Manila ordered the records to be forwarded to the Court of Appeals. As of the date of this Offering Memorandum, the said appeal remains pending.

With regard to Ordinance No. 8187, petitions were filed before the Supreme Court, seeking for its nullification and the enjoinder of its implementation. As of the date of this Offering Memorandum, these petitions remain pending.

Oil Spill Incident in Guimaras

On August 11, 2006, *MT Solar I*, a third party vessel contracted by Petron to transport approximately two million liters of industrial fuel oil, sank 13 nautical miles southwest of Guimaras, an island province in the Western Visayas region of the Philippines. In separate investigations by the Philippine Department of Justice (“DOJ”) and the Special Board of Marine Inquiry (“SBMI”), both agencies found the owners of *MT Solar I* liable. The DOJ found Petron not criminally liable, but the SBMI found Petron to have overloaded the vessel. Petron has appealed the findings of the SBMI to the DOTC and is awaiting its resolution. Petron believes that SBMI can impose administrative penalties on vessel owners and crew, but has no authority to penalize other parties, such as Petron, which are charterers.

In 2009, complaints for violation of the Philippine Clean Water Act of 2004 (Republic Act No. 9275, the Clean Water Act) and homicide and less serious physical injuries were filed against Petron. Complainants claim that their exposure to and close contact with waters along the shoreline and mangroves affected by the oil spill has caused them major health problems. On February 13, 2012, an Information was filed against the owner and the Captain of *MT Solar I* and the former President and Chairman of Petron for violation of the Clean Water Act. On March 28, 2012, the court dismissed the information for lack of probable cause and for lack of jurisdiction over the offense charged. The Provincial Prosecutor and the private prosecutor filed a motion for reconsideration of this March 28 Order of the court. On August 13, 2012, the court issued an order denying the said motion for reconsideration.

Other complaints for non-payment of compensation for the clean-up operations during the oil spill were filed by a total of 1,063 plaintiffs who allegedly did not receive any payment of their claims for damages arising from the oil spill. The total claims for both cases amount to ₱292 million. As of December 31, 2012, the cases were under mediation for possible amicable settlement among the parties.

HEDGING TRANSACTIONS

The outstanding derivative instruments of SMC such as commodity and currency options, forwards and swaps are intended mainly for risk management purposes. SMC uses derivatives to manage its exposures to foreign currency, interest rate and commodity price risks arising from the operating and financing activities of SMC.

REGULATION

Various laws and government agencies in the Philippines regulate different aspects of SMC's businesses.

SMC

Regulation of SMC as a Publicly Listed Company

Pursuant to the Securities Regulation Code, the Philippine SEC regulates the Philippine securities market, including securities exchanges, securities trading, securities brokers and dealers, and public companies. The Securities Regulation Code prescribes disclosure and governance requirements for public companies. Likewise, public companies whose securities are listed on the PSE must comply with the relevant disclosure, continuing listing and trading regulations imposed by the PSE.

As part of the continuing listing requirements imposed by the PSE, at least 10% of a listed company's issued and outstanding shares, exclusive of any treasury shares, must at all times be held by the public. A listed company that does not comply with the prescribed minimum public ownership may be subject to the imposition of additional annual listing maintenance fees, calculated based on the percentage shortfall in the public float and the period of non-compliance. If such non-compliance persists, the PSE may impose a trading suspension on the listed company's securities and delisting procedures may be initiated by the PSE against such listed company.

The minimum public float prescribed by the PSE is different from minimum public float requirements imposed under special laws for other regulated entities, such as entities engaged in power generation, telecommunications and banks. In such cases, the minimum public float prescribed under such laws will govern.

Foreign Investment Laws and Restrictions

Retail Trade Liberalization Act

Philippine Republic Act No. 8762, otherwise known as the Retail Trade Liberalization Act of 2000 ("R.A. 8762"), was enacted into law on March 7, 2000. R.A. 8762 liberalized the Philippine retail industry to encourage Filipino and foreign investors to forge an efficient and competitive retail trade sector in the interest of empowering the Filipino consumer through lower prices, high quality goods, better services, and wider choices. Prior to the passage of R.A. 8762, retail trade was limited to Filipino citizens or corporations that are 100% Filipino-owned.

"Retail Trade" is defined by R.A. 8762 to cover any act, occupation, or calling of habitually selling direct to the general public any merchandise, commodities, or goods for consumption. The law provides that foreign-owned partnerships, associations and corporations formed and organized under the laws of the Philippines may, upon registration with the Philippine SEC and the Philippine Department of Trade and Industry ("DTI") or in case of foreign-owned single proprietorships, with the DTI, engage or invest in the retail trade business, in accordance with the following categories:

- Category A — Enterprises with paid-up capital of the equivalent in Philippine Pesos of less than US\$2.5 million shall be reserved exclusively for Filipino citizens and corporations wholly owned by Filipino citizens.
- Category B — Enterprises with a minimum paid-up capital of the equivalent in Philippine Pesos of US\$2.5 million may be wholly owned by foreigners except for the first two years after the effectiveness of R.A. 8762 during which period foreign participation was limited to not more than 60% of total equity.
- Category C — Enterprises with a paid-up capital of the equivalent in Philippine Pesos of US\$7.5 million or more may be wholly owned by foreigners, provided, that in no case shall the investments for establishing a store in Categories B and C be less than the equivalent in Philippine Pesos of US\$830,000; and
- Category D — Enterprises specializing in high-end or luxury products with a paid up capital of the equivalent in Philippine Pesos of US\$250,000 per store may be wholly owned by foreigners.

No foreign retailer is allowed to engage in retail trade in the Philippines unless all the following qualifications are met:

- A minimum of US\$200 million net worth in its parent corporation for categories B and C, and US\$50 million net worth in its parent corporation for category D;
- Five retail branches or franchises in operation anywhere around the world unless such retailer has at least one store capitalized at a minimum of US\$25 million;
- Five-year track record in retail; and
- Only nationals from, or judicial entities formed or incorporated in, countries which allow the entry of Filipino retailers, shall be allowed to engage in retail trade in the Philippines.

The implementing rules of R.A. 8762 define a foreign retailer as an individual who is not a Filipino citizen, or a corporation, partnership, association, or entity that is not wholly owned by Filipinos, engaged in retail trade. The DTI is authorized to pre-qualify all foreign retailers, subject to the provisions of R.A. 8762, before they are allowed to conduct business in the Philippines.

Foreign Investment Act of 1991

The FIA liberalized the entry of foreign investment into the Philippines. Under the FIA, in domestic market enterprises, foreigners can own as much as 100% equity except in areas specified in the Ninth Regular Foreign Investment Negative List (the “Negative List”). This Negative List enumerates industries and activities which have foreign ownership limitations under the FIA and other existing laws. Among SMC’s current businesses and activities, land ownership, telecommunications, banking, mining and the operation of public utilities are nationalized activities.

In connection with the ownership of private land, the Philippine constitution states that no private land shall be transferred or conveyed except to citizens of the Philippines or to corporations or associations organized under the laws of the Philippines at least 60% of whose capital is owned by such citizens. Likewise, under the Philippine constitution, only citizens of the Philippines or corporations or associations organized under the laws of the Philippines at least 60% of whose capital is owned by such citizens may be granted a franchise to operate a public utility, which includes telecommunications.

For the purpose of complying with nationality laws, the term Philippine National is defined under the FIA as any of the following:

- a citizen of the Philippines;
- a domestic partnership or association wholly owned by citizens of the Philippines;
- a corporation organized under the laws of the Philippines of which at least 60% of the capital stock outstanding and entitled to vote is owned and held by citizens of the Philippines;
- a corporation organized abroad and registered to do business in the Philippines under the Corporation Code, of which 100% of the capital stock outstanding and entitled to vote is wholly owned by Filipinos; or
- a trustee of funds for pension or other employee retirement or separation benefits, where the trustee is a Philippine National and at least 60% of the fund will accrue to the benefit of Philippine Nationals.

For as long as the percentage of Filipino ownership of the capital stock of the corporation is at least 60% of the total shares outstanding and voting, the corporation shall be considered as a 100% Filipino-owned corporation. A corporation with more than 40% foreign equity may be allowed to lease land for a period of 25 years, renewable for another 25 years.

Local Government Code

The Philippine Republic Act No. 7160 (the “Local Government Code”) establishes the system and powers of provincial, city, municipal, and barangay governments in the country. The Local Government Code general welfare clause states that every local government unit shall exercise the powers expressly granted, those necessarily implied, as well as powers necessary, appropriate, or incidental for its efficient and effective governance, and those which are essential to the promotion of the general welfare.

Local government units exercise police power through their respective legislative bodies. Specifically, the local government unit, through its legislative body, has the authority to enact such ordinances as it may deem necessary and proper for sanitation and safety, the furtherance of the prosperity, and the promotion of the morality, peace, good order, comfort, convenience, and general welfare of the locality and its inhabitants. Ordinances can reclassify land, order the closure of business establishments, and require permits and licenses from businesses operating within the territorial jurisdiction of the local government unit.

BEVERAGE BUSINESS

The FDDC Act

The Foods, Drugs and Devices, and Cosmetics Act, as amended by the Food and Drug Administration Act of 2009 (the “FDDC Act”), establishes standards and quality measures in relation to the manufacturing and branding of food products to ensure the safe supply thereof to and within the Philippines. The Food and Drug Administration (the “FDA”) is the governmental agency under the Department of Health (the “DOH”) tasked to implement and enforce the FDDC Act.

The FDDC Act prohibits, among others, (i) the manufacture, importation, exportation, sale, offering for sale, distribution or transfer, non-consumer use, promotion, advertisement or sponsorship of any food products which are adulterated or misbranded or which, although requiring registration pursuant to the FDDC Act, are not registered with the FDA; and (ii) the manufacture, importation, exportation, transfer or distribution of any food product by any person or entity without a license to operate from the FDA. Any person found in violation of any of the provisions of the FDDC Act shall be subject to administrative penalties or imprisonment or both. Furthermore, the FDA has the authority to seize such food products found in violation of the FDDC Act as well as ban, recall and withdraw any food product found to be grossly deceptive, unsafe, or injurious to the consuming public.

Pursuant to FDDC Act, food manufacturers are required to obtain a license to operate as such. Under existing regulations of the FDA, registration with the FDA of locally produced food products for local market distribution is optional, except where such food products are intended to be advertised to the public. For imported food and food products, however, registration is mandatory.

To ensure the safe supply of food products to and within the Philippines, the DOH has promulgated guidelines on current good manufacturing practices in manufacturing, packing, repacking or holding food. These guidelines, which are continually updated by the DOH to align with similar international standards, embody the minimum operating standards, procedures and requirements prescribed by the DOH in respect of the operations and facilities of those establishments engaged in the manufacture, packing, repacking or holding of food products.

The Consumer Act

The Consumer Act of the Philippines (the “Consumer Act”) seeks to: (i) protect consumers against hazards to health and safety; (ii) protect against deceptive, unfair and unconscionable sales acts and practices; (iii) provide information and education to facilitate sound choice and the proper exercise of rights by the consumer; (iv) provide adequate rights and means of redress; and (v) involve of consumer representatives in the formulation of social and economic policies.

The provisions of the Consumer Act are principally enforced by the DTI. However, with respect to food products, the DOH is the government agency responsible for the implementation of the said law.

The Consumer Act regulates such matters as (i) consumer product quality and safety; (ii) the production, sale, distribution and advertisement of food, drugs, cosmetics and devices as well as substances hazardous to the consumer’s health and safety; (iii) fair, honest consumer transactions and consumer protection against deceptive, unfair and unconscionable sales acts or practices; (iv) practices relative to the use of weights and measures; (v) consumer product and service warranties; (vi) compulsory labeling, and fair packaging; (vii) liabilities for defective products and services; (viii) consumer protection against misleading advertisements and fraudulent sales promotion practices; and (ix) consumer credit transactions.

The Consumer Act establishes quality and safety standards with respect to the composition, contents, packaging, labeling and advertisement of products and prohibits the manufacture for sale, offer for sale, distribution, or importation of products which are not in conformity with applicable consumer product quality or safety standards promulgated thereunder. The Consumer Act also prohibits any false, deceptive or misleading advertisement for the purpose of inducing the purchase of consumer products. An advertisement is considered false, deceptive or misleading if it does not conform to the law or is misleading in a material respect. Specific advertising requirements are prescribed for food.

Any person found to be in violation of the provisions of the Consumer Act shall be subject to administrative penalties or imprisonment or both. As part of its authority under the Consumer Act, the DOH has the authority to order the recall, ban, or seizure from public sale or distribution of food products found to be injurious, unsafe or dangerous to the general public.

Excise taxes on alcoholic products, such as beer and liquor

The National Internal Revenue Code of 1997 (the “Tax Code”) provides for excise taxes on alcohol products, including distilled spirits, wines and fermented liquor. In general, excise taxes on alcohol products accrue upon the production of such products, and must be paid before removal thereof from the production site. For imported brands or products, the excise tax is paid upon arrival in the Philippines at the port of entry.

On December 20, 2012, Republic Act No. 10351 (“R.A. 10351”) was enacted, restructuring the imposable excise tax on alcohol products in the country. R.A. 10351 increases the taxes on fermented liquor and distilled spirit products and unifies the tax system for local and imported products. The new tax system includes a tax based on volume and a tax based on the net retail price (ad valorem tax).

To enforce the provisions of the Tax Code on the collection and payment of excise taxes on alcohol products, establishments subject to such taxes are required to obtain a permit to sell such products from the Bureau of Internal Revenue of the Philippines (the “BIR”).

Net retail price as the term is used in R.A. 10351 means the price at which the distilled spirits or fermented liquor is sold on retail in at least five major supermarkets in Metro Manila (for brands marketed nationally), excluding the amount intended to cover the applicable excise tax and the value-added tax. For distilled spirits or fermented liquor which is marketed outside Metro Manila, the net retail price means the price at which the distilled spirits or fermented liquor is sold in at least five major supermarkets in the region, excluding the amount intended to cover the applicable excise tax and the value-added tax.

Understatement of the suggested net retail price of the distilled spirits or fermented liquor by as much as 15% of the actual net retail price shall render the manufacturer or importer liable for additional excise tax equivalent to the tax due on the difference between the understated suggested net retail price and the actual net retail price.

Any brewer, manufacturer or importer who misdeclares or misrepresents any required pertinent data or information will be penalized by a summary cancellation or withdrawal of its permit to engage in business as brewer, manufacturer or importer of fermented liquor or distilled spirits.

Any corporation, association or partnership liable for any of the acts or omissions in violation of R.A. 10351 shall be fined treble the amount of deficiency taxes, surcharges and interest which may be assessed.

To implement R.A. 10351, the BIR issued Revenue Regulations No. 17-2012, and in relation thereto certain revenue memorandum circulars. Pursuant to Revenue Memorandum Circular No. 3-2013, the BIR clarified that all end-products, such as ethyl alcohol, ethanol or other similar products or mixtures are separate and distinct distilled spirits apart from the alcohol products enumerated in the definition of the term distilled spirits (i.e., whisky, brandy, rum, gin, vodka, and other similar products or mixtures) and the same will be subject to a separate and distinct excise tax prescribed under R.A. 10351. Subsequently, in Revenue Memorandum Circular No. 18-2013, the BIR amended Revenue Memorandum Circular No. 3-2013 and clarified that importation of ethyl alcohol or ethanol intended for re-sale or for compounded liquors or the domestic sale of ethanol to manufacturers of compounded liquors shall be subject to excise tax under R.A. 10351 unless a surety bond is posted by the importer or the distillery in addition to the importer’s bond or the manufacturer’s bond, as the case may be, prescribed under Section 160 of the Tax Code. Any excise tax already paid pursuant to Revenue Memorandum Circular No. 3-2013 shall not be entitled to tax credit/refund or shall not be deducted from the total excise tax due on compounded liquors.

Excise Taxes on Distilled Spirits

Excise taxes on distilled spirits, such as whisky, brandy, rum, gin and vodka, are based on the alcohol content or proof liter (a proof liter is a liter of proof spirits which term refers liquor containing one-half of its volume of alcohol of a specific gravity at a specific temperature specified in R.A. 10351), as follows:

Product	Effective date of tax rates					
	January 1, 2013	January 1, 2014	January 1, 2015	January 1, 2016	January 1, 2017	January 1, 2018

(a) Ad Valorem Tax Rate

Based on the net retail price
per proof (excluding the
excise and value added tax) . .

15%	15%	20%	20%	20%	20%
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(b) Specific Tax	₱20.00	₱20.00	₱20.00	₱20.80	₱21.63	₱22.50
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Per proof liter

Effective January 1, 2016, the specific tax rate shall be increased by 4% every year thereafter

Excise Taxes on Fermented Liquor

Excise taxes on fermented liquor, such as beer, lager beer, ale and porter, are determined per liter of volume capacity in relation to the net retail price (excluding the excise tax and VAT thereon), as follows:

Product	Effective date of tax rates					January 1, 2018
	January 1, 2013	January 1, 2014	January 1, 2015	January 1, 2016	January 1, 2017	
Fermented liquors						
where the net retail price (excluding the excise and value added tax) per liter of volume capacity is:						
(a) ₱50.60 or less	₱15.00	₱17.00	₱19.00	₱21.00	₱23.50	Effective January 1, 2018, the specific tax rate shall be increased by
(b) More than ₱50.60	₱20.00	₱21.00	₱22.00	₱23.00	₱23.50	4% every year thereafter

FOOD BUSINESS

As a producer of various food products, the food business of SMC is subject to regulation by the FDA and the DOH under the FDDC Act and the Consumer Act. In addition, the food business of SMC is subject to the laws discussed below.

The Livestock and Poultry Feeds Act

The Livestock and Poultry Feeds Act and its implementing rules and regulations (the “Livestock and Poultry Feeds Act”), regulates and controls the manufacture, importation, labeling, advertising and sale of livestock and poultry feeds. The Bureau of Animal Industry is the governmental office under the DA tasked to implement and enforce the Livestock and Poultry Feeds Act.

Under the Livestock and Poultry Feeds Act, any entity desiring to engage in the manufacture, importation, exportation, sale, trading or distribution of feeds or other feed products must first register with the Bureau of Animal Industry. There must be a separate registration for each type and location of feed establishment. Furthermore, the Livestock and Poultry Feeds Act provides that no feeds or feed products may be manufactured, imported, exported, traded, advertised, distributed, sold, or offered for sale, or held in possession for sale in the Philippines unless the same has been registered with the Bureau of Animal Industry. There must also be a separate registration for each type, kind, and form of feed or feed product. Feeds and feed products produced through toll manufacturing shall be registered with the company that owns the same. All commercial feeds must comply with the nutrient standards prescribed by the DA. Registration of feed and feed products and feed establishments is required to be renewed on a yearly basis.

The Livestock and Poultry Feeds Act also provides branding, labeling and advertising requirements for feeds and feed products and the establishment of in-house quality control laboratories by manufacturers and traders of feed and feed products. Any person found in violation of the provisions of the Livestock and Poultry Feeds Act shall be subject to administrative penalties or imprisonment or both.

The Meat Inspection Code

The Meat Inspection Code of the Philippines (the “Meat Inspection Code”) establishes quality and safety standards for the slaughter of food animals and the processing, inspection, labeling, packaging, branding and importation of meat (including, but not limited to, pork, beef and chicken meat) and meat products. The National Meat Inspection Service, a specialized regulatory service attached to the DA, serves as the national controlling authority on all matters pertaining to meat and meat product inspection and meat hygiene to ensure meat safety and quality from farm to table. It has the power to accredit meat establishments and exporters, importers, brokers, traders and handlers of meat and meat products. On the other hand, the different local government units, in accordance with existing laws, policies, rules and regulations and quality and safety standards of the DA, have the authority to regulate the construction, management and operation of slaughterhouses, meat inspection, and meat transport and post-abattoir control within their respective jurisdictions, and to collect fees and charges.

The Meat Inspection Code covers all meat establishments (including, but not limited to, slaughterhouses, poultry dressing plants, meat processing plants and meat shops) where food animals are slaughtered, prepared, processed, handled, packed, stored, or sold. It requires the inspection of food animals before they are allowed for slaughter

in licensed private slaughterhouses in which meat or meat products thereof are to be sold. A post-mortem examination is also required for carcasses and parts thereof of all food animals prepared as articles of commerce which are capable of use as human food. Only meat or meat products from meat establishments that have passed inspection and have been so marked may be sold or offered for sale to the public.

The Meat Inspection Code provides for labeling, branding and packaging requirements for meat and meat products to enable consumers to obtain accurate information and ensure product traceability. It also requires all meat establishments to (i) comply with the Animal Welfare Act of 1998 for the adequate protection of food animals awaiting slaughter and all pollution control and environmental laws and regulations relating to the disposal of carcasses and parts thereof; and (ii) adopt good manufacturing practices and sanitation standard operating procedures for the production, storage and distribution of its meat products. Any person found in violation of the provisions of the Meat Inspection Code shall be subject to administrative penalties or fines. Furthermore, any carcasses, parts of carcasses or products of carcasses found to have been prepared, handled, packed, stored, transported or offered for sale as human food not in accordance with the provisions of the Meat Inspection Code, shall be confiscated and disposed of at the expense of the person found to be in violation thereof.

The Price Act

The Price Act covers basic necessities such as fresh pork, beef and poultry meat, milk, coffee and cooking oil, and prime commodities such as flour, dried, processed and canned pork, beef and poultry meat, other dairy products and swine and poultry feeds. The Price Act is primarily enforced and implemented by the DA and the DTI in relation to such products.

Under the Price Act, the prices of basic commodities may be automatically frozen or placed under price control in areas declared as disaster areas, under emergency or martial law or in a state of rebellion or war. Unless such price freeze is lifted by the President of the Philippines at an earlier time, prices shall remain frozen for a maximum of sixty days. The President of the Philippines may likewise impose a price ceiling on basic necessities and prime commodities in cases of calamities, emergencies, illegal price manipulation or when the prevailing prices have risen to unreasonable levels. The implementing government agencies of the Price Act are given the authority to issue suggested retail prices, whenever necessary, for certain basic necessities and/or prime commodities for the information and guidance of concerned trade, industry and consumer sectors. The Price Act prohibits and penalizes illegal price manipulation through cartels, hoarding or profiteering. Any person found in violation of the provisions of the Price Act shall be subject to administrative penalties or imprisonment or both.

The Philippine Food Fortification Act

The Philippine Food Fortification Act of 2000 (the “PFF Act”) provides for the mandatory fortification of wheat flour, cooking oil and other staple foods and the voluntary fortification of processed food products. The fortification of food products is required to be undertaken by the manufacturers, importers and processors thereof. The FDA is the government agency responsible for the implementation the PFF Act with the assistance of the different local government units tasked to monitor foods mandated to be fortified which are available in public markets, retail stores and food service establishments and to check if the labels of fortified products contain nutrition. Any person in violation of the PFF Act shall be subject to administrative penalties.

Furthermore, the FDA may refuse or cancel the registration or order the recall of food products in violation of the law.

FUEL AND OIL BUSINESS

Philippines

Downstream Oil Industry Deregulation Act

The Downstream Oil Deregulation Act of 1998 (the “Oil Deregulation Act”), provides the regulatory framework for the Philippines’ downstream oil industry.

Under the Oil Deregulation Act, any person may import or purchase any quantity of crude oil and petroleum products from foreign and domestic sources, lease or own and operate refineries and other downstream oil facilities, and market such crude oil and petroleum products either in a generic name or in its own trade name, or use the same for its own requirement after prior notice to the DOE. The same law declared the liberalization and deregulation of the downstream oil industry as a policy of the state in order to ensure a truly competitive market under a regime of fair prices, adequate and continuous supply of environmentally clean and high quality petroleum products.

To ensure the attainment of these objectives, the DOE, in consultation with relevant government agencies, promulgated the implementing rules and regulations of the Oil Deregulation Act in March 1998 through DOE Department Circular No. 98-03-004.

The DOE is the lead Philippine government agency overseeing the oil industry. With the enactment of the Oil Deregulation Act, however, the regulatory functions of the DOE were significantly reduced. Deregulating the downstream oil industry effectively removed the rate-setting function of the then Energy Regulatory Board, leaving price-setting to market forces. The DOE's current function is primarily to monitor prices and violations under the law, which includes prohibited acts such as cartelization and predatory pricing.

Other functions of the DOE under the Oil Deregulation Act include the following:

- monitoring and publishing the daily international crude oil prices, following the movements of domestic oil prices, monitoring the quality of petroleum and stopping the operation of businesses involved in the sale of petroleum products which do not comply with national standards of quality;
- monitoring the refining and manufacturing processes of local petroleum products to ensure clean and safe technologies are applied;
- maintaining a periodic schedule of present and future total industry inventory of petroleum products to determine the level of supply;
- immediately acting upon any report from any person of an unreasonable rise in prices of petroleum products; and
- in times of national emergency, when the public interest so requires, during the emergency and under reasonable terms, temporarily taking over or directing the operations of any person or entity engaged in the industry.

The implementing rules of the Oil Deregulation Act also require establishments engaged in downstream oil operations to submit periodic reports to the DOE in respect of the following activities or projects relating to petroleum products: (a) refining, processing, including recycling and blending; (b) storing or transshipment; (c) distribution or operation of petroleum carriers; (d) gasoline stations; (e) LPG refilling plant; (f) bunkering from freeports and special economic zones; and (g) importations of petroleum products and additives. In addition, such establishments are required to register with the DOE any fuel additive prior to its use in a product.

Other Regulations Applicable to Petroleum Operations

Philippine government approval of petroleum products and services is generally not required. However, petroleum products refined at Petron's refinery are subject to Philippine National Standards specifications. The DTI, through the Bureau of Products Standards, ensures that all products comply with the specifications of the Philippine National Standards.

Marine Pollution and Oil Spillage

Philippine maritime laws and regulations are enforced by two Philippine government agencies: the Maritime Industry Authority ("MARINA") and the Philippine Coast Guard. Both are agencies under the DOTC.

The MARINA is responsible for integrating the development, promotion, and regulation of the maritime industry in the Philippines. It exercises jurisdiction over the development, promotion, and regulation of all enterprises engaged in the business of designing, constructing, manufacturing, acquiring, operating, supplying, repairing, and/or maintaining vessels, or their component parts, of managing and/or operating shipping lines, shipyards, dry docks, marine railways, marine repair ships, shipping and freight forwarding agencies, and similar enterprises.

To address issues on marine pollution and oil spillage, the MARINA mandated the use of double-hull vessels for transporting black products beginning at the end of 2008 and by 2011 for White Products in certain circumstances.

The Philippine Coast Guard, in a 2005 Memorandum, provided implementing guidelines based on the International Convention for the Prevention of Pollution from Ships, ("MARPOL 73/78"). The guidelines provide that oil companies in major ports or terminals/depots are required to inform the Philippine Coast Guard through its nearest station of all transfer operations of oil cargoes in their respective areas. Furthermore, oil companies and tanker owners are required to conduct regular team trainings on managing oil spill operations including the handling and operations of marine pollution combating equipment. A dedicated oil spill response team is required to be organized to react to land and ship-originated oil spills.

Moreover, both the Clean Water Act of 2004 (the "Clean Water Act", which is discussed more fully below) and the Oil Pollution Compensation Act of 2007 provide that the spiller or the person who causes the pollution has the primary responsibility of conducting clean-up operations at its own expense.

Reduction of Air Emissions

The Clean Air Act of 1999 (the “Clean Air Act”) provides for air quality standards and regulations against air pollution. It provides that the Philippine DENR shall have authority to issue permits as it may determine necessary for the prevention and abatement of air pollution. The permits shall cover emission limitations for regulated air pollutants to help attain and maintain the ambient air quality standards. Under the implementing rules and regulations of the Clean Air Act, all sources of air pollution are required to obtain a valid permit to operate while new or modified sources must first obtain valid authority to construct. The DENR, together with other government agencies and the different local government units, is tasked to implement the Clean Air Act.

In relation to petroleum operations, the Clean Air Act imposes more stringent fuel specifications over a period of time to reduce emission that pollutes the air. The Clean Air Act mandates the sulfur and benzene content for gasoline and automotive diesel. Under the law, oil firms are mandated to lower the sulfur content of automotive diesel oils to 0.05% by January 1, 2004 nationwide. The law also regulates the use of any fuel or fuel additives. Furthermore, the Clean Air Act prohibits a manufacturer, processor or trader of any fuel or additive to import, sell, offer for sale, or introduce into commerce such fuel or additive unless these have been registered with the DOE. All the requirements of the law have been implemented, starting with the phase-out of leaded gasoline in Metro Manila in April 2000 and all over the country in December 2000.

The Biofuels Act

The Biofuels Act aims to reduce the dependence of the transport sector on imported fuel and mandates that, starting February 2009, at least 5% bioethanol shall comprise the total annual volume of gasoline fuel sold by every oil company. Oil companies are allowed to blend the different premium gasoline grades with 10% ethanol to be sold in selected areas to achieve the 5% of total gasoline volume requirement. The requirement to sell ethanol blended gasoline commenced on February 9, 2009. For diesel engines, the mandated biodiesel blend in the country was increased from 1% to 2% starting February 2009.

In 2008, guidelines governing the biofuel feedstock production and biofuel blends production, distribution and sale were issued by various Philippine government agencies. The guidelines provide for responsibilities of oil companies in the sourcing and blending of biodiesel and bioethanol with diesel and gasoline. The guidelines mandate that oil companies should source biofuels only from biofuel producers accredited by the DOE or from biofuel distributors registered with the DOE. Moreover, unless authorized by DOE to import in case of shortage of supply of locally-produced bioethanol as provided for under the Biofuels Act, an oil company’s failure to source its biofuels from accredited biofuels producers and/or registered biofuel distributors would constitute a prohibited act.

Relevant Tax-related Regulations

Taxes and duties applicable to the oil industry have had periodic and unpredictable changes over the last several years. The import duty on crude oil was increased on January 1, 2005 from 3% to 5%, but was later reduced to 3% effective as of November 1, 2005.

Under Executive Order No. 527 dated May 12, 2006, upon certification by the DOE that the trigger price levels provided therein have been reached, the 3% import duty on crude oil shall be adjusted to 2%, 1% or 0%. Subsequently, Executive Order No. 850, which took effect on January 1, 2010, modified the rates of duty on certain imported articles in order to implement the Philippines’ commitment to eliminate tariffs on certain products under the Common Effective Preferential Tariff Scheme for the ASEAN free trade area. Under the ASEAN Trade in Goods Agreement, crude oil and refined petroleum products imported from ASEAN Member States are levied zero rates. To address the tariff distortion between ASEAN and non-ASEAN Member States brought about by the implementation of the zero duty under Executive Order No. 850 and to provide a level playing field for local refiners to compete with importers, the President of the Philippines issued Executive Order No. 890, which also imposed zero duty effective as of July 4, 2010 for imported crude oil and refined petroleum products, except certain types of aviation gas, from non-ASEAN member states.

The Philippine Republic Act No. 9337 (the “Expanded VAT Law”) imposed a VAT of 10% on certain goods and services, including petroleum products and its raw materials, particularly the sale and importation thereof. The rate was further increased to 12% effective February 1, 2006. The Expanded VAT Law also limited the input VAT tax credit to only 70% of the output VAT. Subsequently, however, Republic Act No. 9361, which was approved on November 21, 2006, removed the 70% ceiling on the credit of input VAT to output VAT. As of November 1, 2005, the implementation date of the Expanded VAT Law, excise taxes on diesel, bunker fuel and kerosene were lifted and excise taxes for regular gasoline were lowered to 84.35 per liter of volume capacity.

Malaysia

Petroleum Development Act, 1974

The Petroleum Development Act, 1974 (the “PDA”), which came into force on October 1, 1974, and the Petroleum Regulation 1974, which was enacted pursuant to the PDA (the “Petroleum Regulation”), are the primary legislation governing downstream oil activities in Malaysia. Pursuant to the Petroleum Regulation, two government bodies are vested with powers to regulate all downstream activities, namely:

- (a) the Ministry of International Trade and Industry (“MITI”), which is responsible for the issuance of licenses for the processing and refining of petroleum and the manufacture of petrochemical products; and
- (b) the Ministry of Domestic Trade, Cooperative and Consumerism (“MDTCC”), which is responsible for regulating the marketing and distribution of petroleum products.

Petron has obtained specific licenses from the MITI for the production of Petron’s products. Specific licenses are required pursuant to Section 6 of the PDA for the business of processing or refining petroleum or manufacturing petrochemical products from petroleum at the Port Dickson Refinery. Contravention of the provisions of the PDA or failure to comply with any term or condition of any permission granted thereunder is an offense and is subject to a fine not exceeding RM1 million or imprisonment for a term not exceeding five years or both.

Petroleum (Safety Measures) Act, 1984

The storage and handling of crude oil and oil products and the utilization of equipment and/or appliances used in the downstream oil industry in Malaysia are controlled and governed by the Petroleum (Safety Measures) Act, 1984 (the “PSMA”) and the regulations made thereunder. The PSMA also regulates the transportation of petroleum by road, railway, water, air and pipeline. A unit of the MDTCC known as The Petroleum Safety Unit has been established to administer the PSMA.

Biofuel Industry Act, 2007

The Biofuel Industry Act, 2007 (the “MBIA”) was enacted on July 18, 2007. The MBIA provides for the mandatory use of biofuel, the licensing of activities relating to biofuel and other matters connected and incidental thereto. The MBIA is designed to regulate the biofuel industry in Malaysia and to promote the mandatory use of Malaysia’s domestic palm biodiesel, which is a blend of 5% POME and 95% diesel. The MBIA empowers the Minister of Plantation Industries and Commodities to prescribe (a) the percentage by volume of palm ole and/or methyl ester to be blended in any fuel or (b) the activities in which the use of (i) palm ole and/or methyl ester, (ii) palm ole and/or methyl ester blended with any other fuel or (iii) any other biofuel is to be made mandatory. The MBIA limits the percentage of POME that can be used in a biodiesel mix to a maximum of 5%. The MBIA is being implemented in stages. The first stage, which covers the Klang Valley only, is ongoing, and the second stage, which applies only to subsidized diesel sold at retail service stations, is expected to be implemented throughout Malaysia by the end of 2013.

Sale and Pricing of Refined Petroleum Products

Control of Supplies Act, 1961

The Control of Supplies Act, 1961 (the “CSA”) was enacted primarily to regulate, prohibit and control the movement of controlled articles in Malaysia. The CSA also regulates the distribution of any controlled article and limits the quantity of any controlled article that may be acquired or held by any person. Petrol, motor spirit, or motor gasoline of all grades, diesel fuel and LPG have all been classified as controlled articles under the CSA. Pursuant to the Control of Supplies Regulations 1974, issued pursuant to the CSA, a license is required for any person to deal, by wholesale or retail, in any scheduled article (including petrol, motor spirit, or motor gasoline of all grades, diesel fuel and LPG) or to manufacture any scheduled article. A separate license is required for each place of business where the scheduled article is manufactured or sold. The Controller of Supplies has the authority to enforce the rules and regulations provided in the CSA and related regulations.

Price Control and Anti Profiteering Act, 2011

The Price Control and Anti Profiteering Act, 2011 (the “PCAPA”) replaced the Price Control Act, 1946 and came into force on April 1, 2011. The PCAPA provides for the control of prices of goods, whereby the Malaysian government may, among other things, determine the maximum, minimum or fixed prices for the manufacture, production, wholesale or retail of goods. The Malaysian government generally mandates fixed prices for (a) sales of formulated unleaded gasoline fuel with an octane index of 95 (“Mogas 95”), (b) diesel sales to retail customers, as well as to the commercial transportation and fisheries sectors, and (c) LPG sales to retail

customers, to ensure that increases in international crude oil prices are not borne fully by consumers of such products in Malaysia. Subject to a quota, the Malaysian government subsidizes sales of these products using a formula known as the automatic pricing mechanism. A subsidy is payable to the seller pursuant to the APM if the mandated price of the relevant product is less than the total built-up cost of such product. Conversely, a sales tax is payable by the seller if the mandated price of the relevant product exceeds the total built-up cost of such product.

The sale of diesel in Malaysia is subject to a quota system to ensure that subsidized diesel is not sold illegally to industrial customers at higher, unregulated, prices.

Environmental Laws

Environmental Quality Act, 1974

The Environmental Quality Act, 1974 (the “EQA”) governs the prevention, abatement and control of pollution and enhancement of the environment in Malaysia and covers, among other things, oil spills and pollutants on land and in Malaysian waters. The EQA, which was introduced by the Malaysian government to promote environmentally sound and sustainable development restricts atmospheric, noise, soil and inland-water pollution without a license, prohibits the discharge of oil and waste into Malaysian waters without a license and prohibits open burning. The Department of Environment (the “MDOE”) is the regulatory body with responsibility for administering the EQA and any regulations and orders made thereunder. The MDOE will also have responsibility for monitoring the implementation of and compliance with Euro 4M standards in Malaysia, which are the Malaysian equivalent of Euro IV-standard fuels. It is currently expected that Malaysian downstream oil companies will be required to comply with Euro 4M standards by 2016.

Other Regulatory Requirements

Petron has a general duty pursuant to the Occupational Safety and Health Act, 1994 and the regulations made thereunder to (a) provide and maintain plants and systems of work that are, to the extent practicable, safe and without risks to health, (b) provide information, instruction, training and supervision to ensure, to the extent practicable, the safety and health of Petron’s employees at work and (c) provide a working environment that is, to the extent practicable, safe, without risk to health and adequate with respect to facilities related to employee welfare at work. Petron also has a duty to ensure, to the extent practicable, that other persons who are not its employees are not affected by, and are not exposed to risks to their safety or health by, the conduct of its business. As Petron employs more than 100 employees in Malaysia, it must employ a safety and health officer, who is tasked with ensuring the due observance of statutory obligations with respect to workplace health and safety and the promotion of safe work conduct at the workplace.

ENERGY BUSINESS

Organization and Operation of the Power Industry

The EPIRA established a framework for the organization and operation of the electric power industry in connection with its restructuring, with the industry divided into four sectors: generation, transmission, distribution and supply. The following diagram shows the current structure of the electric power industry under the EPIRA.

Since the enactment of the EPIRA in 2001, the Philippine power industry has undergone and continues to undergo significant restructuring. Through the EPIRA, the Philippine government began to institute major reforms with the goal of fully privatizing all aspects of the power industry. The principal objectives of the EPIRA are:

- to ensure and accelerate the total electrification of the country;
- to ensure the quality, reliability, security and affordability of the supply of electric power;
- to ensure transparent and reasonable prices of electricity in a regime of free and fair competition and full public accountability to achieve greater operational and economic efficiency and enhance the competitiveness of Philippine products in the global market;
- to enhance the inflow of private capital and to broaden the ownership base of the power generation, transmission and distribution sectors;
- to ensure fair and non-discriminatory treatment of public and private sector entities in the process of restructuring the electric power industry;

- to protect the public interest as it is affected by the rates and services of electric utilities and other providers of electric power;
- to ensure socially and environmentally compatible energy sources and infrastructure;
- to promote the utilization of indigenous and new and renewable energy resources in power generation in order to reduce dependence on imported energy;
- to provide for an orderly and transparent privatization of the assets and liabilities of NPC;
- to establish a strong and purely independent regulatory body and system to ensure consumer protection and enhance the competitive operation of the electricity market; and
- to encourage the efficient use of energy and other modalities of demand side management.

With a view to implementing these objectives, the DOE, in consultation with the relevant government agencies, electric power industry participants, non-government organizations and electricity consumers, promulgated the EPIRA's Implementing Rules and Regulations (the "IRR") on February 27, 2002.

The IRR governs the relations between, and respective responsibilities of, the different electric power industry participants as well as the particular governmental authorities involved in implementing the structural reforms in the industry, namely the DOE, NPC, National Electrification Administration ("NEA"), ERC and PSALM.

Reorganization of the Electric Power Industry

Of the many changes initiated by the EPIRA, of primary importance is the reorganization of the electric power industry by segregating the industry into four sectors: (1) the generation sector; (2) the transmission sector; (3) the distribution sector; and (4) the supply sector. The goal is for the generation and supply sectors to be fully competitive and open, while the transmission and distribution sectors will remain regulated. Prior to the EPIRA, the industry was regulated as a whole, with no clear distinctions between and among the various sectors and/or services.

The Generation Sector

The EPIRA provides that power generation is not a public utility operation. Thus, generation companies are not required to secure franchises, and there are no restrictions on the ability of non-Filipinos to own and operate generation facilities. However, generation companies must obtain a certificate of compliance from the ERC, as well as health, safety and environmental clearances from appropriate government agencies under existing laws.

Generation companies are also subject to the ERC's rules and regulations on abuse of market power and anticompetitive behavior. The ERC may impose fines and penalties for violation of the EPIRA and the IRR policy on market power abuse, cross-ownership and anti-competitive behavior.

The goal of the EPIRA is for the generation sector to be open and competitive, while the private sector is expected to take the lead in introducing additional generation capacity. Generation companies will compete either for contracts with various suppliers and private distribution utilities, or through spot sale transactions in the WESM. Competition will be based largely on pricing, subject to availability of transmission lines to wheel electricity to the grid and/or buyers. Recovery by distribution utilities of their purchased power cost is subject to review by the ERC to determine reasonableness of the cost and to ensure that the distribution utilities do not earn any revenue therefrom. Upon commencement of retail competition and Open Access, generation rates, except those intended for such end-users who may not choose their supplier of electricity, as determined by the ERC (the "Captive Market"), will cease to be regulated.

The generation sector converts fuel and other forms of energy into electricity. It consists of the following: (i) NPC-owned-and-operated generation facilities; (ii) NPC-owned plants, which consist of plants operated by IPPs, as well as IPP-owned-and-operated plants, all of which supply electricity to NPC; and (iii) IPP-owned-and-operated plants that supply electricity to customers other than NPC.

Under the EPIRA, generation companies are allowed to sell electricity to distribution utilities or to retail electricity suppliers through either bilateral contracts or the WESM as described below. Once the regime of retail competition and Open Access is implemented, generation companies may likewise sell electricity to eligible end-users. The ERC issued a resolution on January 24, 2007 prescribing the timeline for full retail competition and Open Access in Luzon. Pursuant to section 31 of the EPIRA, such implementation is subject to the fulfillment of five conditions. Four of these conditions have been substantially fulfilled, namely: (1) the establishment of WESM; (2) unbundling of transmission and distribution wheeling charges; (3) initial implementation of the cross-subsidy removal scheme; and (4) privatization of at least 70% of the total capacity of NPC's generating

assets in Luzon and Visayas, with the successful asset turnover of the rebidding for the 600 MW Calaca coal-fired power plant in August 2009. To date, the one condition that remains unsatisfied is the transfer of the management and control of at least 70% of the total energy output of power plants under contract with NPC to the IPPAs. No generation company is allowed to own more than 30% of the installed generating capacity of the Luzon, Visayas or Mindanao grids and/or 25% of the national installed generating capacity. Also, no generation company associated with a distribution utility may supply more than 50% of the distribution utility's total demand under bilateral contracts, without prejudice to the bilateral contracts entered into prior to the effectiveness of the EPIRA.

Historically, the generation sector has been dominated by NPC. To introduce and foster competition in the sector, and, more importantly, to lessen the debt of NPC, the EPIRA mandates the total privatization of the generation assets and IPP contracts of NPC, which exclude the assets devoted to missionary electrification through NPC's small power utilities group. NPC is directed to transfer ownership of all the assets for privatization to a separate entity, PSALM, which is specially tasked to manage the privatization. Beginning early 2004, PSALM has been conducting public bidding for the generation facilities owned by NPC.

As of March 31, 2011, PSALM has privatized 25 operating/generating power facilities with an aggregate rated capacity of 3,468.23 MW accounting for 91.8% of the total 3,778.23 MW total rated capacity of NPC generating assets in the Luzon and Visayas grids. Major generation assets include the 748 MW Tiwi-Makban geothermal power plant, the 600 MW Calaca coal-fired thermal power plant, the 600 MW Masinloc coal-fired thermal power plant, the 360 MW Magat hydroelectric power plant and the 305 MW Palinpinon-Tongonan geothermal power plant. In addition, as of March 31, 2011, IPPA Agreements covering generation assets with an aggregate rated capacity of 4,213.75 MW, or approximately 85.9% of the total energy output of power plants under contract with NPC and IPPAs have been awarded. These include IPPA Agreements for the 1,000 MW Sual coal-fired power plant, the 700 MW Pagbilao coal-fired power plant, the San Roque Power Plant, the 70 MW Bakun hydroelectric power plant, the 40 MW Benguet hydroelectric power plant and the 1,200 MW Ilijan combined-cycle gas-fired power plant.

Section 47(j) of the EPIRA prohibits NPC from incurring any new obligations to purchase power through bilateral contracts with generation companies or other suppliers. Also, NPC is only allowed to generate and sell electricity from generating assets and IPP contracts that have not been disposed of by PSALM.

The Transmission Sector

Pursuant to the EPIRA, NPC has transferred its transmission and sub-transmission assets to TransCo, which was created pursuant to the EPIRA to assume, among other functions, the electrical transmission function of the NPC. TransCo's principal function is to ensure and maintain the reliability, adequacy, security, stability and integrity of the nationwide electrical grid in accordance with the Philippine Grid Code ("Grid Code"). TransCo is also mandated to provide open and non-discriminatory access to its transmission system to all electricity users.

The transmission of electricity through the transmission grid is subject to transmission wheeling charges. As the transmission of electric power is a regulated common carrier business, TransCo's transmission wheeling charges are subject to regulation and approval by the ERC.

The EPIRA also requires the privatization of TransCo through an outright sale of, or the grant of a concession over, the transmission assets while TransCo's subtransmission assets are to be offered for sale to qualified distribution utilities. In December 2007, NGCP, comprising a consortium of Monte Oro Grid Resources, Calaca High Power Corporation and State Grid Corporation of China, won the concession contract to operate, maintain and expand the TransCo assets with a bid of US\$3.95 billion. NGCP was officially granted the authority to operate the country's sole transmission system on January 15, 2009.

The Grid Code establishes the basic rules, requirements, procedures and standards that govern the operation, maintenance and development of the Philippine grid, or the high-voltage backbone transmission system and its related facilities. The Grid Code identifies and provides for the responsibilities and obligations of three key independent functional groups, namely: (a) the grid owner, or TransCo; (b) the system operator, or NGCP as the current concessionaire of TransCo; and (c) the market operator, or the PEMC. These functional groups, as well as all users of the grid, including generation companies and distribution utilities, must comply with the provisions of the Grid Code as promulgated and enforced by the ERC.

In order to ensure the safe, reliable and efficient operation of the Philippine grid, the Grid Code provides for, among others, the following regulations:

- the establishment of a grid management committee, which is tasked with the monitoring of the day-to-day operation of the grid;

- performance standards for the transmission of electricity through the grid, as well as the operation and maintenance thereof, which standards shall apply to TransCo, NGCP, distribution utilities and suppliers of electricity;
- technical and financial standards and criteria applicable to users of the grid, including generation companies and distribution utilities connected or seeking to connect thereto; and
- other matters relating to the planning, management, operation and maintenance of the grid.

The Distribution Sector

The distribution of electric power to end-users may be undertaken by private distribution utilities, cooperatives, local government units presently undertaking this function, and other duly authorized entities, subject to regulation by the ERC. The distribution business is a regulated public utility business requiring a franchise from the Philippine congress, although franchises relating to electric cooperatives remained under the jurisdiction of the NEA until the end of 2006. All distribution utilities are also required to obtain a certificate of public convenience and necessity from the ERC to operate as public utilities.

All distribution utilities are also required to submit to the ERC a statement of their compliance with the technical specifications prescribed in the Philippine Distribution Code (which provides the rules and regulations for the operation and maintenance of distribution systems), the Distribution Services and Open Access Rules and the performance standards set out in the IRR of the EPIRA.

The distribution sector is and will continue to be regulated by the ERC, with distribution and wheeling charges, as well as connection fees from its consumers, subject to ERC approval. Likewise, the retail rate imposed by distribution utilities for the supply of electricity to its captive consumers is subject to ERC approval. In addition, as a result of the Philippine government's policy of promoting free competition and Open Access, distribution utilities are required to provide universal and non-discriminatory access to their systems within their respective franchise areas following commencement of retail Open Access.

The Distribution Code establishes the basic rules and procedures that govern the operation, maintenance, development, connection and use of the electric distribution systems in the Philippines. The Distribution Code defines the technical aspects of the working relationship between the distributors and all the users of the distribution system, including distribution utilities, embedded generators and large customers. All such electric power industry participants in distribution system operations are required to comply with the provisions of the Distribution Code as promulgated and enforced by the ERC.

To ensure the safe, reliable and efficient operation of distribution systems in the Philippines, the Distribution Code provides for, among others, the following regulations:

- technical, design and operational criteria and procedures to be complied with by any user who is connected or seeking connected to a distribution system;
- performance and safety standards for the operation of distribution systems applicable to distributors and suppliers; and
- other matters relating to the planning, development, management, operation and maintenance of distribution systems.

The Supply Sector

The supply of electricity refers to the sale of electricity directly to end-users. The supply function is currently being undertaken solely by franchised distribution utilities. However, upon commencement of retail Open Access, the supply function will become competitive. The business is not considered a public utility operation and suppliers are not required to obtain franchises. However, the supply of electricity to a market of end-users who have a choice on their supplier of electricity ("Contestable Market") is considered a business with a public interest dimension. As such, the EPIRA requires all suppliers of electricity to the Contestable Market to obtain a license from the ERC and they are subject to ERC's rules and regulations on the abuse of market power and other anti-competitive or discriminatory behavior.

Once retail competition and Open Access are implemented as mandated by the EPIRA, it is expected that the Contestable Markets may choose where to source their electric power requirements and can negotiate with suppliers for their electricity. The EPIRA also contemplates that certain end-users will directly source power through the WESM or by entering into contracts with generation companies. This will encourage competition at the retail level and it is planned that retail competition will gradually increase over time, provided that supply companies are sufficiently creditworthy to be suitable offtakers for generation companies.

Role of the ERC

The ERC is the independent, quasi-judicial regulatory body created under the EPIRA that replaced the Energy Regulatory Board. The ERC plays a significant role in the restructured industry environment, consisting of, among others, promoting competition, encouraging market development, ensuring consumer choice and penalizing abuse of market power by industry participants.

Among the primary powers and functions of the ERC are:

- to determine, fix and approve, after conducting public hearings, transmission and distribution and wheeling charges and retail rates and to fix and regulate the rates and charges to be imposed by distribution utilities and their captive end-users, including self-generating entities;
- to grant, revoke, review or modify the certificates of compliance required of generation companies and the licenses required of suppliers of electricity in the Contestable Market;
- to enforce the Grid Code and Distribution Code, which shall include performance standards, the minimum financial capability standards, and other terms and conditions for access to and use of transmission and distribution facilities;
- to enforce the rules and regulations governing the operations of the WESM and the activities of the WESM operator to ensure a greater supply and rational pricing of electricity;
- to ensure that the electric power industry participants and NPC functionally and structurally unbundled their respective business activities and rates and to determine the levels of cross-subsidies in the existing and retail rates until the same is removed in accordance with the different sectors;
- to set a lifeline rate for marginalized end-users;
- to promulgate rules and regulations prescribing the qualifications of suppliers which shall include, among others, their technical and financial capability and creditworthiness;
- to determine the electricity end-users comprising the Contestable and Captive Markets;
- to fix user fees to be charged by TransCo/NGCP for ancillary services to all electric power industry participants or self-generating entities connected to the grid;
- to review all power purchase contracts executed between NPC and IPPs, including the distribution utilities;
- to monitor and adopt measures to discourage or penalize abuse of market power, cartelization and any anticompetitive or discriminatory behavior by any electric power industry participant;
- to review and approve the terms and conditions of service of TransCo/NGCP and any distribution utility or any changes therein;
- to perform such other regulatory functions as are appropriate and necessary in order to ensure the successful restructuring and modernization of the electric power industry; and
- to have original and exclusive jurisdiction over all cases that involve the contesting of rates, fees, fines and penalties imposed in the exercise of its powers, functions and responsibilities and over all cases involving disputes between and among participants or players in the energy industry relating to the foregoing powers, functions and responsibilities.

Role of the DOE

In accordance with its mandate to supervise the restructuring of the electric power industry, the DOE exercises, among others, the following functions:

- preparation and annual updating of the Philippine Energy Plan and the Philippine Power Development Program, and thereafter integrate the latter into the former;
- ensuring the reliability, quality and security of the supply of electric power;
- exercise of supervision and control over all government activities pertaining to energy projects;
- encouragement of private investment in the power industry and promotion of the development of indigenous and renewable energy sources for power generation;
- facilitation of reforms in the structure and operation of distribution utilities for greater efficiency and lower costs;
- promotion of incentives to encourage industry participants, including new generating companies and end-users, to provide adequate and reliable electric supply;

- education of the public (in coordination with NPC, ERC, NEA and the Philippine Information Agency) on the restructuring of the industry and the privatization of NPC assets; and
- establishment of the WESM in cooperation with electric power industry participants, and formulating rules governing its operations.

Role of the Joint Congressional Power Commission

The Joint Congressional Power Commission created pursuant to the EPIRA consists of 14 members selected from the members of the Philippine senate and house of representatives. Its responsibilities and functions include, among others, the following:

- monitoring and ensuring the proper implementation of the EPIRA;
- endorsement of PSALM's initial privatization plan for approval by the President of the Philippines;
- ensuring transparency in the public bidding procedures adopted for the privatization of NPC's generation and transmission assets;
- evaluation of the adherence of industry participants to the objectives and timelines under the EPIRA; and
- recommendation of necessary remedial legislation or executive measures to correct the inherent weaknesses in the EPIRA.

Competitive Market Devices

Wholesale Electricity Spot Market

The EPIRA mandates the establishment of the WESM, which is a pre-condition for the implementation of retail competition and Open Access, within one year from its effectiveness. The WESM provides a venue whereby generators may sell power, and at the same time suppliers and wholesale consumers can purchase electricity where no bilateral contract exists between the two.

On June 28, 2002, the DOE, in cooperation with electric power industry participants, promulgated detailed rules for the WESM. These rules set the guidelines and standards for participation in the market, reflecting accepted economic principles and providing a level playing field for all electric power industry participants, and procedures for establishing the merit order dispatch for each time (hourly) trading period. These rules also provide for a mechanism for setting electricity prices that are not covered by bilateral contracts between electricity buyers and sellers.

On November 18, 2003, upon the initiative of the DOE, the PEMC was incorporated as a non-stock, non-profit corporation with membership comprising an equitable representation of electricity industry participants and chaired by the DOE. The PEMC acts as the autonomous market group operator and the governing arm of the WESM. The PEMC was tasked to undertake the preparatory work for the establishment of the WESM, pursuant to Section 30 of the EPIRA and in accordance with the WESM Rules. Its primary purpose is to establish, maintain, operate and govern an efficient, competitive, transparent and reliable market for the wholesale purchase of electricity and ancillary services in the Philippines in accordance with relevant laws, rules and regulations. Although the long-term goal is to have an interconnected WESM in Luzon and Visayas, WESM in the Visayas grid is still under trial operation status. Moreover, while WESM intends to operate both energy and reserve markets, only the former has already been launched. Having completed its application for the reserve market's pricing methodology, PEMC has indicated that the Visayas grid commenced operations on December 26, 2010.

The WESM became operational in the Luzon grid on June 26, 2006. Prior to the commencement of the Luzon WESM commercial operations, the ERC issued the enforcement of 90% cap on the bilateral supply contracts of distribution utilities to address other issues that may arise during the commercial operations of the WESM. The ERC is responsible for monitoring the 90% cap on power sourced from bilateral PSCs of distribution utilities' total monthly demand. Any distribution utility that violates the 90% cap will not be allowed to recover the costs pertaining to the volume in excess of the cap from its customers.

As of September 26, 2010, there were 77 entities registered as WESM members.

Retail Competition and Open Access

The EPIRA likewise provides for a system of Open Access on transmission and distribution wires, whereby TransCo/NGCP and distribution utilities may not refuse the use of their wires by qualified persons, subject to the

payment of distribution and wheeling charges. Conditions for the commencement of such Open Access system are as follows:

- establishment of the WESM;
- approval of unbundled transmission and distribution wheeling charges;
- initial implementation of the cross-subsidy removal scheme;
- privatization of at least 70% of the total capacity of generating assets of NPC in Luzon and Visayas; and
- transfer of the management and control of at least 70% of the total energy output of power plants under contract with NPC to the IPPAs.

The Philippine government expects retail competition and Open Access to be implemented in phases. As far as Luzon is concerned, the WESM began operations in June 2006 and retail competition has already been introduced, with end-users who comprise the Contestable Market for this purpose already identified.

Open Access in Luzon is expected to commence soon. As of March 31, 2011, PSALM has privatized 25 operating/generating power facilities with an aggregate rated capacity of 3,468.23 MW, accounting for 91.8% of the 3,778.23 MW total rated capacity of NPC's generating assets in the Luzon and Visayas grids. In addition, as of March 31, 2011, IPPA Agreements covering generation assets with an aggregate rated capacity of 4,213.75 MW or approximately 85.92% of the total energy output of power plants under contract with NPC and IPPAs have been awarded.

Upon implementation of Open Access, the various contracts entered into by utilities and suppliers may potentially be stranded. Stranded contract cost refers to the excess of the contracted cost of electricity under eligible contracts of NPC over the actual selling price of the contracted energy output of such contracts in the market. Under the EPIRA, recovery of stranded contract cost may be allowed provided that such contracts were approved by the Energy Regulatory Board (now the ERC) as of December 31, 2000.

Unbundling of Rates and Removal of Cross Subsidies

The EPIRA mandates that distribution and wheeling charges be unbundled from retail rates and that rates reflect the respective costs of providing each service. The EPIRA also states that cross-subsidies shall be phased out within a period not exceeding three years from the establishment by the ERC of a universal charge, which shall be collected from all electricity end-users. However, the ERC may extend the period for the removal of the cross-subsidies for a maximum of one year if it determines that there will be a material adverse effect upon the public interest or an immediate, irreparable and adverse financial effect on a distribution utility.

These arrangements are now in place, in satisfaction of the conditions for retail competition and Open Access.

The EPIRA likewise provides for a socialized pricing mechanism called a lifeline rate to be set by the ERC for marginalized or low-income captive electricity consumers who cannot afford to pay the full cost of electricity. These end-users are exempt from the cross-subsidy removal for a period of ten years, unless extended by law.

Implementation of the PBR

On December 8, 2008, the ERC issued the Rules for Setting Distribution Wheeling Rates that apply to privately owned distribution utilities entering performance-based regulation ("PBR") for the third entry points, which set out the manner in which the new PBR rate-setting mechanism for distribution-related charges will be implemented. PBR is intended to replace the return-on-rate-base regulation ("RORB") that has historically determined the distribution charges paid by the distribution companies' customers. Under the PBR, the distribution-related charges that distribution utilities can collect from customers over a four-year regulatory period will be set by reference to projected revenues which are reviewed and approved by the ERC and used by the ERC to determine a distribution utility's efficiency factor. For each year during the regulatory period, a distribution utility's distribution charge is adjusted upwards or downwards taking into consideration the utility's efficiency factor set against changes in overall consumer prices in the Philippines. The ERC has also implemented a performance incentive scheme whereby annual rate adjustments under PBR will also take into consideration the ability of a distribution utility to meet or exceed service performance targets set by the ERC, such as the average duration of power outages, the average time to provide connections to customers and the average time to respond to customer calls, with utilities being rewarded or penalized depending on their ability to meet these performance targets.

Reduction of Taxes and Royalties on Indigenous Energy Resources

To equalize prices between imported and indigenous fuels, the EPIRA mandates the President of the Philippines to reduce the royalties, returns and taxes collected for the exploitation of all indigenous sources of energy,

including but not limited to, natural gas and geothermal steam, so as to effect parity of tax treatment with the existing rates for imported coal, crude oil, bunker fuel and other imported fuels. Following the promulgation of the IRR, then President Arroyo enacted Executive Order No. 100 to equalize the taxes among fuels used for power generation. This mechanism, however, is yet to be implemented.

Government Approval Process

As set forth in the EPIRA, power generation is not considered a public utility operation. Thus, an entity engaged or intending to engage in the generation of electricity is not required to secure a franchise. However, no person or entity may engage in the generation of electricity unless such person or entity has complied with the standards, requirements and other terms and conditions set by the ERC and has received a certificate of compliance from the ERC to operate facilities used in the generation of electricity. A certificate of compliance is valid for a period of five years from the date of issuance.

In addition to the certificate of compliance requirement, a generation company must comply with technical, financial and environmental standards. A generation company must ensure that all its facilities connected to the grid meet the technical design and operational criteria of the Grid Code and Distribution Code promulgated by the ERC. In this connection, the ERC has issued guidelines setting the minimum financial capability standards for generation companies. Under the guidelines, a generation company is required to meet a minimum annual interest cover ratio or debt service capability ratio of 1.5x throughout the period covered by its certificate of compliance. For certificate of compliance applications and renewals, the guidelines require the submission to the ERC of, among other things, comparative audited financial statements, a schedule of liabilities, and a five-year financial plan. For the duration of the certificate of compliance, the guidelines also require a generation company to submit audited financial statements and forecast financial statements to the ERC for the next two financial years, as well as other documents. The failure by a generation company to submit the requirements prescribed by the guidelines may be grounds for the imposition of fines and penalties.

Upon the introduction of retail competition and Open Access, the rates charged by a generation company will no longer be regulated by the ERC, except rates for Captive Markets (which are determined by the ERC). In addition, since the establishment of the WESM, generation companies are now required to comply with the membership criteria and appropriate dispatch scheduling as prescribed under the WESM Rules.

In the course of developing a power plant, other permits, approvals and consents must also be obtained from relevant national, provincial and local government authorities, relating to, among others, site acquisition, construction and operation, including environmental licenses and permits.

PACKAGING BUSINESS

Safety and Quality Regulations under the Consumer Act

The DTI is tasked to implement the Consumer Act with respect to labels and packaging of consumer products other than food products, and regulates product labeling, proper and correct description of goods, product labels with foreign characters/languages, data/information on product contents and origins and other similar matters.

Manufacturers, distributors, importers or repackers of consumer products are required to indicate in their labels or packaging, a parallel translation in the English or Filipino language of the nature, quality and quantity and other relevant prescribed information or instructions of such consumer products in a manner that cannot be easily removed, detached or erased. In addition to the information required to be displayed in the principal and secondary panels, DTI Administrative Order No. 01-08 mandates that all consumer products sold in the Philippines, whether manufactured locally or imported shall indicate and specify the (i) country of manufacture; (ii) required information of consumption duration safety; (iii) warranty of the manufacturer; (iv) weight content prior to packaging; (v) consumer complaint desk address; and (vi) all other information necessary for giving effect to a consumer's right to information.

The packaging of consumer products must not cause the purchaser to be deceived as to the contents, size, quantity, measurement or fill of the product. For consumer products which are packaged in such a way that the contents cannot be seen or inspected upon purchase, samples or labeling describing the product inside the package, in words, in pictorial or graphical representation or by similar means, shall be provided for the inspection of the purchaser. Such sample or description should accurately represent the product in the package.

With respect to the packaging and repackaging of food products, such activities are regulated by the DOH and the FDA as discussed above. Establishments engaged in these activities are required to comply with, among others, the current guidelines on good manufacturing practice in manufacturing, packing, repacking, or holding food promulgated by the DOH.

OTHER BUSINESSES

Banking Business

Bangko Sentral ng Pilipinas

The BSP is the central bank of the Republic of the Philippines. It was rechartered on July 3, 1993, pursuant to the provisions of the 1987 Philippine constitution and the New Central Bank Act of 1993 (the “New Central Bank Act”). The BSP was established on January 3, 1949, as the country’s central monetary authority. Among its functions is the management of foreign currency reserves, by maintaining sufficient international reserves to meet any foreseeable net demands for foreign currencies in order to preserve the international stability and convertibility of the Philippine Peso.

Pursuant to the New Central Bank Act and the General Banking Law of 2000 (the “General Banking Law”), the Monetary Board of the BSP (the “Monetary Board”) was vested with the power to regulate and supervise financial intermediaries in the Philippines.

The BSP Manual of Regulations for Banks (2009) (the “Manual”) is the principal source of rules and regulations to be complied with and observed by banks in the Philippines. The Manual contains regulations that include those relating to the organization, management and administration, deposit and borrowing operations, loans, investments and special financing program, and trust and other fiduciary functions, of the relevant bank. Supplementing the Manual are rules and regulations promulgated in various circulars, memoranda, letters and other directives issued by the Monetary Board.

The Manual and other BSP rules and regulations are principally implemented by the Supervision and Examination Sector (the “SES”) of the BSP. The SES is responsible for ensuring the observance of applicable laws and rules and regulations by banking institutions operating in the Philippines (including Philippine government credit institutions, their subsidiaries and affiliates, non-bank financial intermediaries, and subsidiaries and affiliates of non-bank financial intermediaries performing quasi-banking functions).

Minimum capitalization

Under the Manual, commercial banks are required to have capital accounts of at least ₱2,800 million. This minimum level of capitalization may be changed by the Monetary Board from time to time. Currently, the BSP requires only minimum capital accounts of ₱2,400 million for commercial banks.

Capital Adequacy Requirements

The Manual provides that the risk-based capital ratio of a bank, expressed as a percentage of qualifying capital to risk-weighted assets, must not be less than 10%. The ratio is required to be maintained daily on both a solo basis (head office plus branches) and a consolidated basis (parent bank plus subsidiary financial allied undertakings, but excluding insurance companies). The qualifying capital refers to the sum of tier 1 and tier 2 or supplementary capital of the bank, less deductions of the value of certain assets. The risk-weighted assets, on the other hand, are determined by assigning risk weights to amounts of on-balance sheet assets and to credit equivalent amounts of off-balance sheet items (including derivative contracts), subject to certain deductions.

The BSP issued a memorandum to all banks on December 13, 2004, mandating commercial and universal banks to comply with the Basel Committee on Banking Supervision’s revised International Convergence of Capital Measurement and Capital Standards, (“Basel II”), by July 2007. Basel III which was adopted by the Basel Committee on Banking Supervision in September 2010 and is expected to be implemented by the BSP, will require a more stringent capital adequacy structure to be adopted in stages prior to 2019.

Reserve Requirements

Under the New Central Bank Act, the BSP requires banks to maintain cash reserves and liquid assets in proportion to deposits in prescribed ratios. If a bank fails to meet this reserve during a particular week on an average basis, it must pay a penalty to the BSP on the amount of any deficiency.

Commercial banks are required to maintain regular reserves of 8% against Philippine Peso demand, savings and time deposits, negotiable order of withdrawal accounts, deposit substitutes, and Unit Investment Trust Funds and other similarly managed funds.

In addition to the foregoing regular reserve requirements, commercial banks are required to set up liquidity reserves against Philippine Peso demand, savings and time deposits and deposit substitute liabilities, Unit Investment Trust Funds and trust and other fiduciary activities equivalent to 11%.

Loan Limit to a Single Borrower

Under the General Banking Law and its implementing regulations, the total amount of loans, credit accommodations and guarantees that may be extended by a bank to any borrower shall at no time exceed 25% of the net worth of such bank (or 35% of the net worth of the bank in the event that certain types and levels of security are provided). This ceiling may be adjusted by the Monetary Board from time to time.

Loans to Directors, Officers, Stockholders and Related Interests of a Bank

The amount of individual outstanding loans, other credit accommodations and guarantees to the directors, officers, stockholders and related interests of a bank (“DOSRI”) should not exceed an amount equivalent to their unencumbered deposits and book value of DOSRI’s paid-in capital investment. In the aggregate, outstanding loans, other credit accommodations and guarantees to DOSRI generally should not exceed 100% of net worth or 15% of the total loan portfolio, whichever is lower. In no case shall the total unsecured loans, other credit accommodations and guarantees to DOSRI exceed 30% of the aggregate ceiling or of the outstanding loans, other credit accommodations and guarantees, whichever is lower. For the purpose of determining compliance with the ceiling on unsecured loans, other credit accommodations and guarantees, banks shall be allowed to average their ceiling on unsecured loans, other credit guarantees and guarantees every week.

On January 31, 2007, the BSP issued Circular No. 560, which provides that total outstanding loans, other credit accommodations and guarantees to each of the bank’s subsidiaries and affiliates shall not exceed 10% of the net worth of the bank and the unsecured loans, other credit accommodations and guarantees to each of said subsidiaries and affiliates shall not exceed 5.0% of the bank’s net worth. In the aggregate, outstanding loans, other credit accommodations and guarantees to all subsidiaries and affiliates shall not exceed 20% of the net worth of the bank. BSP Circular No. 560 further provides that these subsidiaries and affiliates should not be a related interest of any of the directors, officers and/or stockholders of the lending institution, except where such director, officer, or stockholder sits on the board of directors or is appointed as an officer of such corporation as representative of the bank. However, loans, other credit accommodations and guarantees secured by assets considered as non-risk under existing BSP regulations as well as interbank call loans shall be excluded in determining compliance with these prescribed ceilings.

Telecommunications Business

Telecommunications services in the Philippines are considered as a public service and are governed by specific regulations and laws. The principal laws governing the telecommunications industry are the 1936 Commonwealth Act No. 146, as amended, commonly referred to as the “Public Service Act”, and the Public Philippine Telecommunications Policy Act (the “Public Telecommunications Policy Act”).

The Public Service Act seeks to protect the public against unreasonable charges and poor, inefficient service by public utilities and prevent ruinous competition. The Public Telecommunications Policy Act sets forth the current telecommunications policy objectives of the Philippine government. It also seeks to develop and maintain a viable, efficient, reliable and universal telecommunications infrastructure which ensures that telecommunications services are available in unserved or under-served areas, and sets out the functions, powers and responsibilities of the National Telecommunications Commission (“NTC”) of the Philippine department of transportation and communications.

The NTC regulates the telecommunications industry under the provisions of the Public Service Act, Executive Order No. 59 (“E.O. 59”), Executive Order No. 109 (“E.O. 109”) and Republic Act No. 7925 (“R.A. 7925”). Under these laws, a telecommunications service provider is required to, among others: (i) secure a certificate of public convenience and necessity (“CPCN”) or provisional authority from the NTC for those services it intends to offer which are deemed regulated services under relevant laws, as well as rates sought to be charged, insofar as deemed regulated; (ii) observe the provisions of E.O. 109 and R.A. 7925 which impose an obligation to rollout 700,000 fixed lines as a condition to the grant of by the NTC of provisional authorities for cellular and international gateway services; and (iii) observe the regulations of the NTC on interconnection of public telecommunications networks, and the payment to the NTC of annual supervision and permit fees.

Among the specific functions of the NTC is the granting of permits for the use of radio frequencies for cellular telephone and telegraph systems and radio communications systems, as well as the sub-allocation of frequencies of bands allocated by the international telecommunications union to the specific services. The NTC is required to exercise these functions consistent with the national policy that radio frequency spectrum is a scarce public resource that must be administered in the public interest and in accordance with international agreements and conventions to which the Philippines is a party. It is the policy of the government to allocate frequencies to

service providers that will use them efficiently and effectively to meet public demand for telecommunications service and that seek out and utilize new and cost-effective technologies.

All telecommunications service providers are required to obtain a legislative franchise from the Philippine congress. Under the Philippine constitution, only citizens of the Philippines or corporations or associations organized under the laws of the Philippines at least 60% of whose capital is owned by such citizens may be granted a franchise to operate a public utility, which includes telecommunications service providers. The Philippine constitution provides that no franchise to operate a public utility may be exclusive in character or have a term longer than 50 years. The Philippine constitution also requires that any franchise must be granted subject to amendment, alteration or repeal by the Philippine congress when required to serve the common good. Under the Public Telecommunications Policy Act, legislative franchises are also subject to an equality clause by which any advantage, favor, privilege, exemption or immunity granted under franchises issued on or after the date of enactment of the Public Telecommunications Policy Act automatically becomes part of all previously granted franchises. The equality clause, however, does not apply to the territory covered by the franchise, the life span of the franchise or the type of service authorized by the franchise.

In addition to a legislative franchise, those seeking to operate a telecommunication service are required by law to obtain a CPCN from the NTC. This certificate is a grant of final authority to own, operate and maintain a public telecommunications facility or service. Its term cannot be shorter than five years nor longer than the life of the legislative franchise.

Pending the grant of a CPCN, an applicant may request in its application or petition, the issuance of a provisional authority, or file a motion, in the same proceedings for the CPCN, for the grant of a provisional authority to operate a telecommunications service. The provisional authority may be granted if the NTC is satisfied, based on the application for the CPCN and the attached supporting documents, that the applicant is prima facie entitled to a CPCN. The grant of provisional authority, however, is without prejudice to the final decision of the NTC on the application for a CPCN. A provisional authority is usually granted for a period of 18 months. If a CPCN is not issued prior to the expiration of the provisional authority, the applicant may request the renewal or extension of the provisional authority by filing a motion in the same proceedings for its CPCN application. As a matter of practice, the NTC grants requests for renewal or extension of a provisional authority once it is satisfied that the applicant has substantially complied with the conditions of the provisional authority and appears to be capable of fulfilling its commitments.

Compulsory Interconnection and Cross-Subsidization

The Public Telecommunications Policy Act requires carriers to interconnect their networks with other networks with the objective of creating a seamless nationwide network. The Government first adopted compulsory interconnection with the issuance of E.O. 59 on February 24, 1993 by then President Fidel V. Ramos. Pursuant to this legislation, the NTC issued Memorandum Circular No. 14-7-2000, dated July 14, 2000, implementing the rules and regulations for the interconnection of networks of authorized public telecommunication of networks of authorized public telecommunications entities. This memorandum circular provides a general framework for interconnection of public telecommunications networks and public telecommunications services, regardless of the supporting technologies employed.

Interconnection costs and access charges are determined through bilateral negotiation among telecommunication carriers. The NTC may on its own initiative intervene in any of these negotiations and mediate between the parties at any time. Additionally, if the parties do not come to an agreement after 90 days from commencement of negotiation, the NTC may, upon application of one of the parties, commence mediation proceedings. If the parties fail to come to an agreement in the course of mediation, the NTC is authorized to intervene and impose interconnection terms and conditions. The NTC has promoted a policy allowing international and domestic toll and cellular interconnect services to subsidize local exchange operators to allow them to earn a rate of return comparable with other segments of the telecommunications industry. This reflects the policy under the Public Telecommunications Policy Act of providing cross-subsidies to local exchange operators when they interconnect with local exchanges of other carriers. This cross-subsidy is required to be imputed in the interconnection fee negotiated by the operators and the carriers and is payable under the interconnection arrangement. Carriers that are required to operate local exchanges as a result of being previously granted licenses to provide international and/or cellular services are also required to cross- subsidize the operations of other local exchange operators that are linked with them.

Local Exchange Service Roll-out Requirements

On July 12, 1993, then President Fidel V. Ramos issued E.O. 109 to implement the Philippine government's objective of improving the provision of local exchange carrier services. To implement E.O. 109, the NTC issued

regulations which required all authorized operators of international gateway facilities to install at least 300,000 local exchange lines within three years from the date of the grant of a provisional authority for local exchange carrier service. In providing local exchange carrier services, operators of international gateway facilities are required to maintain a ratio of at least one rural exchange line for every 10 urban exchange lines installed. These regulations also required all authorized cellular operators to install at least 400,000 local exchange lines within five years from the date when the regulations took effect. Operators that provide both international gateway facility and cellular services are required to install a minimum of 700,000 lines. In implementing E.O. 109, the NTC divided the country into 11 service areas. The NTC assigned to each international gateway facility and cellular operator a designated area in which the operator is required to provide local exchange services. Failure to meet the minimum lines obligation may be grounds for cancellation of an operator's CPCN or provisional authority after due notice and hearing. Since 1997, the NTC has permitted additional telecommunications companies to provide local exchange lines in the designated service areas.

The local exchange service roll-out requirements under E.O. 109 were adopted by the Philippine congress in the Public Telecommunications Policy Act. However, under the said law, the period of time within which cellular operators are required to comply with their roll-out requirements was changed from five years from the date of issuance of the implementing regulations to three years from the date of issuance of the provisional authority to operate a local exchange service.

3G Radio Frequency Allocation

On October 31, 2000 then President Joseph Estrada signed Executive Order No. 307 which provides that 3G radio frequency spectrum and other parts of the radio frequency spectrum not yet allocated be allocated by auction, subject to the terms and conditions as approved by a 3-member joint committee.

The NTC issued Memorandum Circular 06-08-2005 on August 23, 2005 to reallocate certain frequency bands to support the development and deployment of telecommunications networks and services for broadband wireless access for fixed, nomadic and mobile networks.

In January 2006, the NTC, through a public bidding, sold four of the five frequencies available for the cellular telephone 3G radio frequency under the standards provided by NTC Memorandum Circular 07-08- 2005, which outlined the procedure for the allocation and assignment of 3G radio frequency bands. An entity intending to operate a 3G mobile telecommunications system is required to file its application for authority or CPCN and must possess the following minimum qualifications, including (i) a congressional franchise, (ii) minimum paid-up capital stock of 8100.0 million for new public telecommunications entities, (iii) a debt to equity ratio of 70:30 with total investment in the cellular mobile telecommunications system or 3G networks of at least 8400.0 million and (iv) proof of technical capability to install, operate and maintain the proposed cellular mobile telecommunications system or 3G networks.

The last remaining frequency remains unsold because of legal action resorted to by some of the losing bidders.

In July 19, 2007, the NTC reallocated the band 410-430 MHz for broadband wireless access in addition to the frequency bands in MC 06-08-2005. On March 13, 2010, the NTC published MC 01-03-2010 which introduced a stricter standard for the allocation of radio frequency bands to discourage frequency hoarding by existing telecommunications companies.

Public Ownership

In order to diversify the ownership base of public utilities, the Public Telecommunications Policy Act requires a telecommunications entity with regulated types of services to make a public offering through the stock exchanges of at least 30% of its aggregate common stock by the later of the following (i) the fifth anniversary of the date the law became effective; and (ii) the fifth anniversary of the date of the entity's commencement of commercial operations.

Tariffs

The Public Service Act and the Public Telecommunications Policy Act give the NTC the authority to regulate telecommunications tariffs and approve all rates charged by operators of telecommunication services, other than paging, public repeater network services and value-added services. The NTC is also authorized to establish rates for telecommunications services that are fair and reasonable. In making its determination, the NTC is required to consider socio-economic factors and financial, technical and commercial criteria, including the cost of property and equipment, depreciation, working capital and the operator's rate of return on its investment. Telecommunications companies are free to set rates, within a range established by the NTC, for services in which the NTC deems there to be sufficient competition, such as international long distance and cellular

communications. Pursuant to NTC circulars, the rates for special features on telephone networks, cellular mobile telephone service and national and international leased line services have been deregulated.

The NTC may approve an application to increase tariffs after due notice and hearing upon the petition of an operator. The NTC may, however, grant provisional authority to increase rate upon filing and compliance with requirements of publications and notice to affected parties, provided all documents required to justify the increase are submitted and a formal hearing is held within 30 days from the grant of the provisional authority. An operator may apply to the NTC to have rates reduced through an administrative process involving the submission of only supporting documentation without the necessity of a hearing.

The NTC also permits some operators to use a currency exchange rate mechanism which allows, but does not oblige, operators to increase and requires operators to decrease, monthly charges depending on the Philippine Peso-to-U.S. dollar exchange rate. Under the currency exchange rate mechanism, a telecommunications operator, which at the time of application to the NTC had U.S. dollar or other foreign currency denominated debt, is allowed to adjust telephone tariffs to reflect Philippine Peso-U.S. dollar exchange rate fluctuations. Following a grant of authorizations by the NTC to an operator, currency exchange tariff adjustments are not required to be approved by the NTC. The permitted rate adjustment may be different for every operator.

Acts Requiring NTC Approval

Under the Public Service Act, certain acts of telecommunications entities require prior approval from the NTC, including: (i) increase in capital stock; (ii) the sale, transfer, alienation, mortgage, encumbrance or lease of all or substantially all of their assets or of authorizations to operate telecommunications service; and (iii) issuance of bonds or evidence of indebtedness payable more than one year following their dates of issuance.

Nationality Restrictions on Telecommunications Operators

The Philippine constitution prohibits non-Philippine persons from owning more than 40% of the capital of any public utility, which includes telecommunications service providers. It also provides that representation of non-Philippine citizens on the board of directors of any public utility is limited to their proportionate share of the utility's capital stock.

Infrastructure Business

Government Procurement Reform Act

Under the Republic Act 9184 ("Government Procurement Reform Act"), which took effect on January 26, 2003 all procurement activities of the Philippine government, its departments, bureaus, offices and agencies, including state universities and colleges, government-owned and/or controlled corporations, government financial institutions and local government units shall be done through public, open and competitive bidding. The said law covers all procurement activities by all branches and instrumentalities of the Philippine government, in relation to infrastructure projects, including goods and services, regardless of the source of funds, whether local or foreign.

Each procuring entity (i.e., the relevant Philippine government agency or instrumentality) is required to establish a bids and awards committee, composed of at least five but not more than seven members. The committee shall advertise and/or post the invitation to bid, conduct pre-procurement and pre-bid conferences, determine the eligibility of prospective bidders, receive bids, conduct the evaluation of bids, undertake post-qualification proceedings, recommend award of contracts to the head of the procuring entity or his duly authorized representative.

The Government Procurement Reform Act requires a winning bidder, as a measure of guarantee for the faithful performance of and compliance of its obligations under the contracts, to post a performance security prior to the signing of any awarded contract. The failure to do the same within the period stipulated in the bidding documents may disqualify the bidder.

Build-Operate-Transfer Law

Under Republic Act No. 6957 (the "BOT Law"), which took effect on October 9, 1990, all government infrastructure agencies, including government-owned and controlled corporations and local government units, were authorized to enter into contract with any duly prequalified private contractor for the financing, construction, operation and maintenance of any financially viable infrastructure facilities through private initiative and investment: the Build-Operate-Transfer ("BOT") or Build-Transfer ("BT").

Republic Act No. 7718 ("RA 7718") amended the original BOT Law and authorized variations of the contractual arrangements or schemes that may be entered into by the Government with qualified private parties. RA 7718

also introduced the concept of unsolicited proposals, by virtue of which all government infrastructure agencies, including government-owned-and-controlled corporations and local government units are allowed to accept unsolicited proposals for projects which (i) involve a new concept or technology, (ii) are not part of the list of priority projects identified by the agency, including any projects which may have been identified in the Comprehensive and Integrated Infrastructure Program (“CIIP”), and (iii) do not involve direct government guarantees, subsidies or equity. The CIIP is a list of priority infrastructure projects, including the proposed timeline and scope of work, which is prepared by the NEDA and the Office of the President for projects appropriate for purely private investment, public-private partnership and purely public investment.

The BOT Law embodies the basic principle of PPP in infrastructure development and has been cited as instrumental in increasing private investment in infrastructure, especially in the areas of power, telecommunications, airports and water utilities.

Guidelines and Procedures for Entering into Joint Venture Agreements

Pursuant to Executive Order No. 423 dated April 30, 2005, NEDA issued the 2008 Guidelines and Procedures for entering into Joint Venture Agreements. The guidelines govern transactions in the nature of a joint venture between private sector and the Philippine government, which covers all government-owned and/or controlled corporations, government corporate entities, government instrumentalities with corporate powers, government financial institutions, state universities and colleges. Excluded from the application of the guidelines are local government units and transactions of government financial institutions in the ordinary course of business. The guidelines provide for the parameters for entering into joint venture agreements, which should involve investments made only in activities directly and immediately related to and in furtherance of the primary corporate purpose of the investing government entity. Further, the joint venture should be clear in its intent to undertake a specific activity and should not crowd out the private sector.

Under the guidelines, the preferred mode of implementing a joint venture agreement is through a special purpose joint venture company to be formed by the government and the private sector which shall be registered as a stock corporation in compliance with the ownership and nationality requirements under Philippine law (if applicable). The Philippine government must have proportionate representation to the board of such joint venture company. The joint venture company shall be permitted to derive income from the authorized activities under the agreement and is further encouraged to stipulate a fixed period for the participation of the participating agency or instrumentality of the Philippine government. The selection of a partner may be made through competitive selection or negotiated agreements.

Regulation of Toll Operations

The Toll Regulatory Board (the “TRB”), created by virtue of Presidential Decree No. 1112, is the government agency authorized to regulate toll operations in the Philippines and exercises close supervision, monitoring and regulation of the construction, operation and maintenance of toll facilities, such as but not limited to national highways, roads, bridges and public thoroughfares, including collection of toll fees and rates that may be charged for the use of said facilities.

The TRB currently has the power to (i) issue, modify and proclaim the rates of the toll that will be charged the direct users of toll facilities and upon notice and hearing, to approve or disapprove petitions for the increases and (ii) grant authority to operate a toll facility and to issue the necessary toll operation certificate.

Civil Aviation

Pursuant to the Civil Aviation Authority Act of 2008 (the “Civil Aviation Authority Act”), the CAAP was created as an attached agency of the department of transportation and communications, with jurisdiction over the restructuring of the civil aviation system of the Philippines and the promotion, development and regulation of the technical, operational, safety and aviation security function. The creation of the CAAP was intended to update and strengthen the international framework of the country’s civil aviation industry and meet the standards set by the international civil aviation organization.

In the exercise and performance of its powers and duties, the CAAP shall consider the following, as being in the public interest and in accordance with public convenience and necessity: (i) the development and utilization of the air potential of the Philippines; (ii) the encouragement and development of an air transportation system properly adapted to the present and future of foreign and domestic commerce of the Philippines; (iii) the regulation of air transportation in such manner as to support sound economic condition in such transportation and to improve the relations between air carriers; (iv) ensuring the safety, quality, reliability and affordability of air transport service for the riding public; and (v) the encouragement and development of a viable and competitive

Philippine aviation industry. Further, the CAAP board of directors is responsible for the planning, development, construction, operation, maintenance or expansion of airports.

Mining Business

The Philippine constitution

Under the Constitution of the Philippines, all minerals, among other natural resources, are owned by the Government. The Constitution gives the Government full control and supervision over the exploration, development and utilization of natural resources. In exercising its powers, the Government may enter into mineral production sharing agreements, co-production agreements and joint venture agreements with Philippine nationals. These agreements may be for a term of up to 25 years, renewable for another term of up to 25 years with the consent of the Government, and on such other terms and conditions as may be permitted by law. In addition, the President of the Philippines may enter into agreements with corporations that are not Philippine nationals involving financial or technical assistance for large-scale exploration, development and utilization of mineral resources.

Nationality requirement to undertake mining and mining related activities

Except for financial or technical assistance agreements (“FTAA”), the exploration for and exploitation of minerals in the Philippines under mineral and operating agreements with the Government may only be conducted by Philippine nationals as defined under the FIA.

Forms of mining tenure

Under Republic Act No. 7942 or the “Philippine Mining Act,” the Government may grant exploration permits to qualified applicants and enter into mineral agreements with qualified independent contractors who are Philippine nationals and FTAAAs with qualified corporations that need not be Philippine nationals. The Government’s activities under the Philippine Mining Act are administered by the Mines and Geosciences Bureau (“MGB”) of the DENR.

- (a) Exploration permit. An exploration permit grants the permit holder the right to enter, occupy and explore for minerals in a specified area.
- (b) Mineral agreement. There are three types of mineral agreement:
 - Mineral Production Sharing Agreement (“MPSA”) — An agreement pursuant to which the Philippine government grants to the contractor the exclusive right to conduct mining operations within a contract area and shares in the gross output from the operations. The Government’s share consists of an excise tax of 2% of the gross revenue from mining. In addition, if an MPSA covers an area that lies within a mineral reservation, the contractor is required to pay the Government a further royalty of not less than 5% of gross revenues from the sales of minerals from the properties. The contractor under an MPSA is required to provide all the necessary financing, technology, management and personnel.
 - Co-Production Agreement (“CA”) — A co-production agreement is similar to an MPSA except that the Government makes an agreed contribution to the mining operations conducted by the contractor.
 - Joint Venture Agreement (“JVA”) — Under a joint venture agreement, the Government and the contractor form a joint venture company and the Government grants to the company the exclusive right to conduct mining operations within a contract area. In addition to its equity participation, the Government is entitled to an agreed share of the gross revenues from the sales of minerals from the properties.
- (c) FTAA. An FTAA is an agreement between the Government and the contractor involving financial or technical assistance for large-scale exploration, development and utilization of mineral resources.

An exploration permit or a mineral agreement may be assigned to another qualified person subject to the approval of the Secretary of the DENR upon the recommendation of the Director of the MGB. An FTAA may be assigned to another qualified person subject to the approval of the President of the Philippines upon recommendation of the Secretary of the DENR and the Director of the MGB.

On July 6, 2012, President Benigno S. Aquino III signed Executive Order No. 79 (“E.O. 79”) to implement reforms in the mining sector. Under E.O. 79, certain areas were identified wherein applications for mineral contracts, concessions, and agreements shall not be allowed. Mining contracts, agreements, and concessions approved before the effectivity of E.O. 79 will continue to be valid, binding, and enforceable so long as the same strictly comply with existing laws, rules, and regulations and the terms and conditions of the grant thereof. Furthermore, no new mineral agreements shall be entered into until a legislation rationalizing existing revenue

sharing schemes and mechanisms (the “New Mining Legislation”) shall have taken effect. With respect to pending applications for mineral agreements in areas closed to mining, the implementing rules and regulations of E.O. 79 issued by the DENR (“Administrative Order No. 2012-07”) provides for a categorical denial as regards these pending mining applications, *i.e.*, such pending applications are deemed denied upon the effectivity of E.O. 79. The DENR may, nevertheless, continue to grant and issue exploration permits under existing laws, rules, and guidelines. The grantees of such permits shall have the rights under the said laws, rules, and guidelines over the approved exploration area and shall be given the right of first option to develop and utilize the minerals in their respective exploration area upon the approval of the declaration of mining project feasibility and the effectivity of the New Mining Legislation. The grant of mining rights and tenements over areas with known and verified mineral resources and reserves, including those owned by the Government and all expired tenements, shall be undertaken through competitive public bidding.

The Philippine Mining Act provides for the annual mandatory relinquishment of areas granted to the permit holder or contractor under an exploration permit, mineral agreement or FTAA such that, following the exploration stage, unless otherwise approved by the Government, the final mining area is generally limited to 5,000 hectares for metals and 2,000 hectares for non-metals.

No mining rights may be granted in relation to ancestral lands claimed or occupied by indigenous cultural communities under a claim of time immemorial possession, except with the prior consent of such communities. If such consent is obtained, the holder of the mining rights must pay a negotiated royalty to the affected communities of not less than 1% of the gross revenue from sales of mineral products extracted from the lands.

The Philippine Mining Act grants the contractor certain easement rights to enter and occupy lands owned, occupied or leased by other persons for purposes of conducting mining operations or installing or building structures required for such operations, upon payment of just compensation and subject to compliance with certain requirements under the Philippine Mining Act.

In addition to the Government’s share under the mineral agreements described above, each permit holder and contractor is required to pay an annual occupation fee payable to the local government where the onshore mining area is located or to the MGB for offshore areas, computed as follows: (a) for areas outside a mineral reservation, ₱75 per hectare or a fraction thereof under an exploration permit mineral agreement or FTAA, and (b) for areas inside a mineral reservation, ₱100 per hectare or a fraction thereof under any exploration permit, mineral agreement or FTAA.

Mineral Processing and Ore Transport Permits

A mineral processing permit is required to process minerals, except when an approved work program under an MPSA already includes such processing. Likewise, an ore transport permit is required to transport mineral products.

Final Mine Rehabilitation/Decommissioning Plan

Five years before the final decommissioning of a contract area, the holder of a mineral agreement or FTAA must submit final rehabilitation and/or decommissioning plans, including details of its financial requirements up to post-decommissioning over a 10-year period for monitoring purposes.

Local Communities

The holder of a mineral agreement or FTAA is required to assist (i) in the development of the local communities to promote the general welfare of the local inhabitants, and (ii) in the development of mining technology and geosciences as well as manpower training and development. The holder of a mineral agreement or FTAA is also required to allot annually a minimum of 1% of its direct milling and mining costs for such purposes.

All applicants for exploration permits, mineral agreements and FTAA are required to obtain the support of local barangays. A “barangay” is the smallest local government unit in the Philippines. This support usually consists of an endorsement or approval of the project in the form of a resolution.

EISS and ECCs

The EISS Law and the ECC are discussed below under “Environmental Matters”.

The Philippine Mining Act specifically requires an ECC to be obtained based on an environmental impact assessment and procedure, except during the exploration period. It also requires the submission of an EPEP as described below.

EPEP

An Environmental Protection and Enhancement Program (“EPEP”) is a comprehensive and strategic environmental management plan for the life of the mining project.

EPEPs are prepared pursuant to the provisions of the Philippine Mining Act and DENR Administrative Order No. 96-40, as amended, and cover the environmental programs necessary for the development and mining of the deposits in the approved MPSA contract area for the next 25 years. An EPEP must provide a description of the expected and considered acceptable impact and should set out life-of-mine environmental protection and enhancement strategies based on best practices in environmental management in mining. It must include a statement on post-mining land use potential for various types of disturbed land (including pits, waste dumps and infrastructure sites) and extend to the completion of the commitments in the rehabilitation of the disturbed land in a technically, socially and environmentally competent manner. The program must be based on practical and achievable options and demonstrated practice. Finally, the program must include implementation schedules, environmental compliance guarantees, monitoring, reporting and cost provisions. Where proposed practices are unproven, a research program to prove the impact control and rehabilitation technology is required.

In addition, each year an annual EPEP must be prepared based on the approved EPEP and must be implemented during the year for which it is submitted. It must address, among other things, exploration, development, utilization, rehabilitation, regeneration, revegetation and reforestation of mineralized areas, slope stabilization of mined-out areas, waste dumps (including acid mine drainage control), tailings-covered areas, aquaculture, watershed development, water conservation and socio-economic development.

Annual obligations under the approved overall EPEP include (i) the submission of an annual EPEP to the Mine Rehabilitation Fund Committee created pursuant to the implementing rules of the Philippine Mining Act in the relevant area, and (ii) the submission of an annual social development and management program to the MGB.

OTHER REGULATORY MATTERS

Registration under the Board of Investments

Under the Omnibus Investments Code, a Board of Investments-registered enterprise may enjoy certain incentives provided such enterprise invests in preferred areas of investment enumerated in the Investment Priorities Plan annually prepared by the Government. However, prior to registration with the BOI, the enterprise must first satisfy the minimum equity required to finance the project applied equivalent to 25% of the estimated project cost, or as may be prescribed by the Board of Investments.

Such incentives may include: (i) income tax holiday; (ii) additional deduction for labor expenses; (iii) tax exemption on imported capital equipment; (iv) tax credit on domestic capital equipment; (v) exemption from contractor’s tax; (vi) simplification of customs procedure; (vii) unrestricted use of consigned equipment; (viii) employment of foreign nationals; (ix) tax exemption on imported spare parts; and (x) exemption from wharfage dues and export duties and fees.

Intellectual Property

Under the Intellectual Property Code of the Philippines (the “Intellectual Property Code”), the rights to a trademark are acquired through registration with the Bureau of Trademarks of the Intellectual Property Office of the Philippines, which is the principal government agency involved in the registration of brand names, trademarks, patents and other registrable intellectual property materials. Once the mark has been duly registered, the Intellectual Property Office issues a certificate of registration to the owner of the mark, which shall serve as prima facie evidence of (i) the validity of registration, (ii) the registrant’s ownership of the mark, and (iii) the registrant’s exclusive right to use the mark in connection with the goods or services and those that are related thereto as specified in the certificate.

Registration of a trademark is valid for an initial period of ten years; thereafter, it may be renewed for ten-year periods by the registrant upon payment of the prescribed fee and upon the filing of a request with the Intellectual Property Office for such purpose within six months prior to the date of expiration of registration.

Advertising Regulations

The Consumer Act protects consumers from misleading advertisement and fraudulent sales and promotion practices. Any false, deceptive or misleading advertisement for the purpose of inducing or which is likely to induce, directly or indirectly, the purchase of consumer products or services is prohibited.

In addition, any advertisement involving signs or signboard structures is covered by the national building code of the Philippines and requires securing prior permit for the installation or attachment of any sign to the structure.

The Advertising Board of the Philippines (the “AdBoard”), a non-stock, non-profit corporation, is an umbrella of organizations involved in the advertising industry which has the power to impose sanctions on its members who broadcast advertisements without prior clearance of the AdBoard. Further, it has adopted a code of ethics and is guided by the Advertising Content Regulation Manual of Procedures and the Standards of Trade Practices and Conduct Manual.

Labor and Employment

The DOLE is the Philippine government agency mandated to formulate policies, implement programs and services, and serve as the policy-coordinating arm of the Executive Branch in the field of labor and employment. The DOLE has exclusive authority in the administration and enforcement of labor and employment laws such as the Labor Code of the Philippines and the Occupational Safety and Health Standards, as amended, and such other laws as specifically assigned to it or to the Secretary of the DOLE.

Social Security System, PhilHealth and the Pag-IBIG Fund

An employer, or any person who uses the services of another person in business, trade, industry or any undertaking is required under the Social Security Act of 1997 to ensure coverage of employees following procedures set out by the law and the Social Security System (“SSS”). Under the said law, an employer must deduct from its employees their monthly contributions based on a given schedule, pay its share of contribution and remit these to the SSS within a period set by law and/ or SSS regulations.

Employers are likewise required to ensure enrollment of its employees in a National Health Program administered by the Philippine Health Insurance Corporation (“PhilHealth”) a government corporation attached to the DOH tasked with ensuring sustainable, affordable and progressive social health insurance pursuant to the provisions of the National Health Insurance Act of 1995. Under the Home Development Mutual Fund Law of 2009, all employees who are covered by the Social Security Act of 1997 must also be registered with and covered by the Home Development Mutual Fund, more commonly referred to as the Pag-IBIG Fund.

Foreign Exchange Regulations

Since 1992, the foreign exchange rules and regulations of the BSP have been liberalized. Under present regulations, as a general rule, foreign exchange may be freely sold and purchased outside the Philippine banking system. If foreign loans are to be serviced with foreign exchange purchased from the Philippine banking system, the proceeds of such loans intended to fund local costs should be inwardly remitted and sold within the Philippine banking system or deposited in foreign currency deposit units or offshore accounts. However, amounts intended to finance foreign exchange costs need not be inwardly remitted, but may either be paid directly to the supplier/beneficiary concerned or deposited in an offshore account. The Manual of Regulations on Foreign Exchange Transactions provides, inter alia, that the foreign exchange payment obligations on only those private sector foreign currency loans which have been duly approved by and registered with the BSP may use foreign exchange purchased from within the Philippine banking system.

For purposes of the foregoing, the Philippine banking system comprises banks operating under Philippine banking laws (principal of which is the General Banking Law of 2000, Republic Act No. 8791) and subsidiaries or affiliates of Philippine banks organized as foreign exchange corporations which buy, own or sell foreign exchange. The Philippine foreign exchange market outside the Philippine banking system comprises the market made by various entities, such as Philippine corporations with foreign currency revenues, non-Philippine banks and individuals and other non-bank entities owning foreign exchange or deposits in FCDUs.

Registration of Foreign Loans and Foreign Investments

Approval from the BSP for the issuance and guarantee of offshore borrowings is not required. However, as described above, receiving such approval and registration will allow a borrower to access the Philippine banking system to obtain U.S. dollars to service such debt obligations rather than other sources of U.S. dollars such as the non-banking system or foreign currency revenue streams. SMC has not sought the approval of, or registered the issue of the Notes with, the BSP as it considers it will have sufficient U.S. dollars to pay interest and principal (if any) on the Notes without having to access the Philippine banking system. See “*Risk Factors — Risks Relating to the Notes — SMC has not obtained BSP approval for the Notes.*”

ENVIRONMENTAL MATTERS

The operations of the businesses of SMC are subject to various laws, rules and regulations that have been promulgated for the protection of the environment.

EISS Law

The Philippine Environmental Impact Statement System (the “EISS Law”), which is implemented by the DENR, is the general regulatory framework for any project or undertaking that is either (a) classified as environmentally critical or (b) is situated in an environmentally critical area. It requires an entity that will undertake any such declared environmentally critical project or operate in any such declared environmentally critical area to submit an Environmental Impact Statement (“EIS”) which is a comprehensive study of the significant impacts of a project on the environment. The EIS serves as an application for the issuance of an Environmental Compliance Certificate (“ECC”), if the proposed project is environmentally critical or situated in an environmentally critical area, otherwise, for the issuance of a Certificate of Non-Coverage. An ECC is a Philippine government certification that, among others, (i) the proposed project or undertaking will not cause significant negative environmental impact; (ii) the proponent has complied with all the requirements of the EISS in connection with the project; and (iii) the proponent is committed to implement its approved Environmental Management Plan in the EIS. In general, only projects that pose potential significant impact on the environment shall be required to secure an ECC. The proponent of a project for which an ECC is issued and determined by the DENR to pose a significant public risk or necessitate rehabilitation or restoration shall be required to establish an environmental guarantee fund. Such fund is intended to meet any damage caused by, as well as any rehabilitation and restoration measures in connection with, the said project.

The Clean Water Act

The Clean Water Act and its implementing rules and regulations provide for water quality standards and regulations for the prevention, control, and abatement of pollution of the country’s water resources. The Clean Water Act requires owners or operators of facilities that discharge regulated effluents (such as wastewater from manufacturing plants or other commercial facilities) to secure a discharge permit from the DENR which authorizes the owners and operators to discharge waste and/or pollutants of specified concentration and volumes from their facilities into a body of water or land resource for a specified period of time. The DENR, together with other government agencies and the different local government units, is tasked to implement the Clean Water Act and to identify existing sources of water pollutants, as well as strictly monitor pollution sources which are not in compliance with the effluent standards provided in the law.

The Clean Air Act

As previously discussed in this Offering Memorandum, enterprises that operate or utilize air pollution sources are required to obtain an Authority to Construct or a Permit to Operate from the DENR with respect to the construction or the use of air pollutants. The issuance of the said permits seek to ensure that regulations of the DENR with respect to air quality standards and the prevention of air pollution are achieved and complied with by such enterprises.

The Renewable Energy Act

Republic Act No. 9513, also known as the Renewable Energy Act of 2008 aims to promote development and commercialization of renewable and environment-friendly energy resources such as biomass, solar, and wind through various tax incentives. Some of the tax incentives granted to renewable energy developers under the said law include (i) a seven-year income tax holiday; (ii) duty free importation of renewable energy machinery, equipment, and materials; (iii) special realty tax rates on equipment and machinery; (iv) zero percent VAT rate for power generated from these energy sources; and (v) the imposition of a reduced corporate tax of 10% on its net taxable income after the income tax holiday.

Other Environmental Laws

Other regulatory environmental laws and regulations applicable to SMC’s businesses include the following:

- The Toxic Substances and Hazardous and Nuclear Waste Control Act of 1990, which regulates, restricts or prohibits the (i) importation, manufacture, processing, handling, storage, transportation, sale, distribution, use and disposal of chemical substance and mixtures that present unreasonable risk or injury to health or the environment, and (ii) entry into the Philippines or the keeping in storage of hazardous wastes which include by-products, process residue, contaminated plant or equipment or other substances from manufacturing operations. The said law is implemented by the DENR.
- The Ecological Solid Waste Management Act of 2000, which provides for the proper management of solid waste which includes discarded commercial waste and non-hazardous institutional and industrial waste. The said law prohibits, among others, the transporting and dumping of collected solid wastes in areas other than

prescribed centers and facilities. The National Solid Waste Management Commission, together with other government agencies and the different local government units, are responsible for the implementation and enforcement of the said law.

- The Code on Sanitation of the Philippines (the “Sanitation Code”), which provides for sanitary and structural requirements in connection with the operation of certain establishments such as food establishments which include such places where food or drinks are manufactured, processed, stored, sold or served. Under the Sanitation Code, which is implemented by the DOH, food establishments are required to secure sanitary permits prior to operation which shall be renewable on a yearly basis.

DIRECTORS AND EXECUTIVE OFFICERS

Board of Directors

The table below sets forth each member of the Board of Directors of SMC as of the date of this Offering Memorandum.

<u>Name</u>	<u>Age</u>	<u>Citizenship</u>	<u>Position</u>
Eduardo M. Cojuangco, Jr.	77	Filipino	Chairman and Chief Executive Officer
Ramon S. Ang	59	Filipino	Vice Chairman, President and Chief Operating Officer
Estelito P. Mendoza	83	Filipino	Director
Leo S. Alvez	70	Filipino	Director
Joselito F. Campos, Jr.	62	Filipino	Director
Ferdinand K. Constantino	61	Filipino	Director
Menardo R. Jimenez	80	Filipino	Director
Roberto V. Ongpin	76	Filipino	Director
Alexander J. Poblador	59	Filipino	Director
Eric O. Recto	49	Filipino	Director
Thomas A. Tan	59	Filipino	Director
Iñigo Zobel	56	Filipino	Director
Winston F. Garcia	54	Filipino	Independent Director
Reynato S. Puno	72	Filipino	Independent Director
Margarito B. Teves	69	Filipino	Independent Director

Eduardo M. Cojuangco, Jr. is the Chairman and Chief Executive Officer of the Company, a position he has held since July 7, 1998. He is also the Chairman of the Executive Committee of the Company. He also holds the following positions: Chairman and Chief Executive Officer of Ginebra San Miguel, Inc. and Chairman of San Miguel Pure Foods Company, Inc. He is also the Chairman of ECJ & Sons Agricultural Enterprises, Inc. and the Eduardo Cojuangco, Jr. Foundation, Inc., and a Director of Caiñaman Farms, Inc. and Petron Corporation. He is a former Director of Manila Electric Company (February 2009-May 2009). He attended the University of the Philippines — Los Baños College of Agriculture and California Polytechnic College in San Luis, Obispo, U.S.A.

Ramon S. Ang is the Vice Chairman since January 28, 1999, President and Chief Operating Officer since March 6, 2002 of the Company. He is also a Member of the Executive Committee and Nomination and Hearing Committee of the Company. He also holds, among others, the following positions: Chairman of San Miguel Brewery Inc. and San Miguel Brewery Hong Kong Limited, Petron Corporation, Sea Refinery Corporation, SMC Global Power Holdings Corp., San Miguel Foods, Inc., San Miguel Yamamura Packaging Corporation, San Miguel Properties, Inc., and Anchor Insurance Brokerage Corporation; Vice Chairman of Ginebra San Miguel, Inc. and San Miguel Pure Foods Company, Inc.; Director of Top Frontier Investment Holdings Inc.; Chairman of Liberty Telecoms Holdings Inc., Philippine Diamond Hotel & Resort, Inc., Philippine Oriental Realty Development, Inc., Atea Tierra Corporation and Cyber Bay Corporation; Vice Chairman and Director of Manila Electric Company; and an Independent Director of Philweb Corporation. He is also the President and Chief Operating Officer of PAL Holdings, Inc., Philippine Airlines, Inc., and Director of Air Philippines Corporation. Mr. Ang has held directorships in various domestic and international subsidiaries of SMC in the last five years. He has a Bachelor of Science degree in Mechanical Engineering from Far Eastern University.

Estelito P. Mendoza has been a Director of the Company since April 21, 1998. He is a member of the Executive Committee, Audit Committee, and the Chairman of the Nomination and Hearing Committee of the Company. He is also a Director of Petron Corporation, Manila Electric Company, Philippine National Bank and Philippine Airlines, Inc., and Chairman of Prestige Travel, Inc. Atty. Mendoza, a former Solicitor General, Minister of Justice, Member of the Batasang Pambansa and Governor of the Province of Pampanga, heads the E.P. Mendoza Law Office. He is also a former Chairman of Dutch Boy Philippines, Inc. and Alcorn Petroleum and Minerals Corporation, and Director of East-West Bank. He graduated from the University of the Philippines College of Law *cum laude*. He also holds a Master of Laws degree from Harvard Law School.

Leo S. Alvez has been a Director of the Company since February 27, 2002 and a Member of the Audit Committee of the Company. He is also a Director of Ginebra San Miguel, Inc. and San Miguel Pure Foods Company, Inc. Ret. Major General Alvez is a former Security Consultant to the Prosecution Panel of the Senate Impeachment Trial of President Joseph Estrada (2000-2001), Vice Commander of the Philippine Army (1998), and Division Commander of the 7th Infantry Division (1996-1998). He is a graduate of the Philippine Military Academy and has a Masters in Business Administration degree from the University of the Philippines.

Joselito D. Campos, Jr. has been a Director since May 31, 2010. He is a member of the Executive Compensation Committee. He is the President and Chief Executive Officer of Del Monte Philippines, Inc. He is also the Chairman and Chief Executive Officer of the NutriAsia, Inc., Chairman of Fort Bonifacio Development Corp. and Chairman of Ayala Greenfield Development Corp. He was the former Chairman and Chief Executive Officer of United Laboratories, Inc. and its regional subsidiaries and affiliates. He is also the Honorary Consul in the Philippines for the Republic of Seychelles. He is Chairman of the Metropolitan Museum of Manila and a Trustee of the Asia Society in the Philippines, the Philippines-China Business Council, the Philippine Center for Entrepreneurship and a member of the WWF (World Wildlife Fund) Philippines. He graduated with a degree in BS Commerce, major in International Business from the University of Santa Clara, California and a Masters in Business Administration from Cornell University, New York.

Ferdinand K. Constantino has been a Director of the Company since May 31, 2010. He is a member of the Executive Committee, Audit Committee, Executive Compensation Committee and Nomination and Hearing Committee. He is Senior Vice President, Chief Finance Officer and Treasurer of the Company. He also holds, among others, the following positions: President of Anchor Insurance Brokerage Corporation; and a Director of San Miguel Brewery Inc., San Miguel Yamamura Packaging Corporation, SMC Global Power Holdings Corp., Top Frontier Investment Holdings Inc., Petron Corporation, Ginebra San Miguel Inc. and San Miguel Foods Inc. He is also the Chairman of San Miguel Foundation, Inc. He is also a Director of PAL Holdings, Inc., and Philippine Airlines, Inc. Mr. Constantino previously served San Miguel Corporation as Chief Finance Officer of the San Miguel Beer Division (1999-2005) and as Chief Finance Officer and Treasurer of San Miguel Brewery Inc. (2007-2009); Director of San Miguel Pure Foods Company, Inc. (2008-2009); Director of San Miguel Properties, Inc. (2001-2009); and Chief Finance Officer of Manila Electric Company (2009). He has held directorships in various domestic and international subsidiaries of SMC during the last five years. He holds a degree in AB Economics from the University of the Philippines and completed academic requirements for an MA Economics degree.

Menardo R. Jimenez has been a Director of the Company since February 27, 2002 and the Chairman of the Executive Compensation Committee and a Member of the Executive Committee of the Company. He is also a Director of San Miguel Pure Foods Company, Inc., and Magnolia, Inc. His other positions include: Chairman of the United Coconut Planters Bank; President and Chief Executive Officer of Albay-Agro Industrial Corporation; Director of Majent Management and Development Corporation, M. A. Jimenez Enterprises, Inc., Television International Corporation; Chairman of Fibers Trading, Inc., CBTL Holdings, Inc., and Meedson Properties Corporation; and a Director of Mabuhay Philippines Satellite Corporation, CCC Insurance Corporation and Pan-Phil Aqua Culture Corporation. He is a graduate of Far Eastern University with a degree of Bachelor of Science in Commerce and is a certified public accountant.

Roberto V. Ongpin has been a Director of the Company since September 1, 2009. He is a member of the Nomination and Hearing Committee and Executive Committee of the Company. He also holds the following positions: Director of Petron Corporation, Top Frontier Investment Holdings Inc., PAL Holdings, Inc., Philippine Airlines, Inc. and Ginebra San Miguel, Inc.; Chairman of PhilWeb Corporation, ISM Communications Corporation, Alphaland Corporation, Atok-Big Wedge Co., Inc., and Acentic GmbH; Non-Executive Director of Forum Energy PLC (UK) and Shangri-la Asia Limited (Hong Kong); and Deputy Chairman of South China Morning Post (Hong Kong). He is a graduate of the Ateneo de Manila University with a degree in BS Business Administration *cum laude* and is a certified public accountant. He also holds a Masters in Business Administration degree from Harvard Business School.

Alexander J. Poblador has been a Director of the Company since September 1, 2009 and a member of the Nomination and Hearing Committee of the Company. He is the Founding Partner and Chairman of the Executive Committee of Poblador Bautista & Reyes Law Office. Atty. Poblador is a practicing lawyer, specializing in the fields of commercial litigation, international arbitration, real estate finance and project development, bankruptcy and corporate reorganization. He is a graduate of the University of the Philippines with a degree in Bachelor of Laws *cum laude*, class valedictorian, and Bachelor of Arts in Political Science *cum laude*. He also holds a Masters of Laws degree from the University of Michigan, at Ann Arbor, School of Law (De Witt Fellow).

Eric O. Recto has been a Director since May 31, 2010. He is a member of the Executive Compensation Committee of the Company. He is the President and Director of Top Frontier Investment Holdings Inc; the Chairman of Philippine Bank of Communications; a Director of Manila Electric Company; Vice Chairman of Philweb Corporation, Atok-Big Wedge Corporation and Alphaland Corporation; and President of ISM Communications Corporation. He was previously Undersecretary of the Department of Finance, in charge of both the International Finance Group and the Privatization Office and a member of the Central Bank Board of Liquidators from 2002 to 2005. He is graduate of the University of the Philippines with a degree in BS Industrial Engineering and holds a Masters in Business Administration degree from Cornell University, New York.

Thomas A. Tan was elected as a Director of the Company on June 14, 2012. He is the President and General Manager of SMC Shipping and Lighterage Corporation and President of Saturn Cement Corporation. He obtained a degree in Bachelor of Science, major in Physics in 1974 from the Ateneo de Manila University and a Masters in Business Management from the Asian Institute of Management in 1976. He is likewise a Director of other affiliates of the Company.

Iñigo Zobel has been a Director of the Company since October 2009 and was an Independent Director of the Company from May 5, 1999 until October 2009. He also holds the following positions: Chairman of Top Frontier Investment Holdings Inc.; Vice Chairman of SMC Global Power Holdings Corp.; President and Chief Operating Officer of E. Zobel, Inc.; President of Ayala España S.A.; Calatagan Golf Club, Inc. and Hacienda Bigaa, Inc.; and a Director of Calatagan Resort, Inc., Calatagan Bay Realty, Inc., Calatagan Golf Club, Inc., and MERMAC, Inc., among others. He is also a Director of PAL Holdings, Inc. and Philippine Airlines, Inc., and President and Chief Operating Officer of Air Philippines Corporation. He was previously the President of Diamond Star Agro Products, Inc. (1985-2007) and formerly an Independent Director of San Miguel Brewery Inc., San Miguel Pure Foods Company, Inc., San Miguel Properties, Inc., and Ginebra San Miguel, Inc. He attended Santa Barbara College, California, United States.

Winston F. Garcia has been a Director of the Company since February 1, 2001, and a Member of the Audit Committee and Executive Compensation Committee of the Company. Atty. Garcia was President and General Manager of the Government Service Insurance System and was Vice Chairman of its Board of Trustees. He also held the following positions: Chairman of the National Reinsurance Corporation of the Philippines, GSIS Mutual Fund, Inc., Asean Forum, Incorporated and Philippine Social Security Association; Director of Philippine National Construction Corporation, and Philippine Health Insurance Corporation; Board Member of Asean Social Security Association; and a Member of the International Insurance Society, Inc., International Social Security Association, and Federation of Afro Insurers and Reinsurers. Atty. Garcia has been a practicing lawyer since 1983. He is a graduate of the San Beda College of Law, and has a Bachelor of Arts in Philosophy from the University of Santo Tomas and Associate in Arts degree in Southwestern University.

Reynato S. Puno was elected to the Board as an Independent Director of the Company on January 20, 2011 and a member of the Executive Compensation Committee and Nomination and Hearing Committee of the Company. He was the Chief Justice of the Supreme Court from December 6, 2006 until his retirement on May 17, 2010. He joined the Supreme Court as an Associate Justice on June 1993 and was previously Associate Justice of the Court of Appeals (1986 to 1993), Appellate Justice of the Intermediate Appellate Court (1983), Assistant Solicitor General (1974-1982) and City Judge of Quezon City (1972-1974). He also served as Deputy Minister of Justice from 1984-1986. He completed his Bachelor of Laws from the University of the Philippines in 1962, and has a Master of Laws degree from the University of California in Berkeley (1968) and a Master in Comparative Law degree from the Southern Methodist University, Dallas, Texas (1967).

Margarito B. Teves was elected as an Independent Director of the Company on June 14, 2012 and is the Chairman of the Audit Committee. He is also an Independent Director of Alphaland Corporation and Atok-Big Wedge Corporation. He is also the Managing Director of The Wallace Business Forum and Chairman of Think Tank Inc. He was Secretary of the Department of Finance of the Philippine government from 2005 to 2010, and was previously President and Chief Executive Officer of the Land Bank of the Philippines from 2000 to 2005, among others. He holds a Master of Arts in Development Economics from the Center for Development Economics, Williams College, Massachusetts and is a graduate of the City of London College, with a degree of Higher National Diploma in Business Studies which is equivalent to a Bachelor of Science in Business Economics.

Senior Management

The table below sets forth the executive officers of SMC as of the date of this Offering Memorandum.

<u>Name</u>	<u>Age</u>	<u>Citizenship</u>	<u>Position</u>
Ferdinand K. Constantino	61	Filipino	Senior Vice President — Chief Finance Officer
Virgilio S. Jacinto	56	Filipino	Senior Vice President — General Counsel, Compliance Officer and Corporate Secretary
Joseph N. Pineda	49	Filipino	Senior Vice President — Deputy Chief Finance Officer
Aurora T. Calderon	58	Filipino	Senior Vice President — Senior Executive Assistant to the Office of the President and Chief Operating Officer
Francisco S. Alejo III	64	Filipino	President, San Miguel Pure Foods Company, Inc.
Ferdinand A. Tumpalan	52	Filipino	President, San Miguel Yamamura Packaging Corp.
Roberto N. Huang	65	Filipino	President, San Miguel Brewery Inc.
Bernard D. Marquez	44	Filipino	President, Ginebra San Miguel Inc.
Carlos Antonio M. Berba	48	Filipino	Managing Director, San Miguel Brewery International Limited
Alan T. Ortiz	58	Filipino	President, SMC Global Power
Lubin B. Nepomuceno	61	Filipino	President, Petron Corporation
Lorenzo G. Formoso III	51	Filipino	Vice President and Head of Infrastructure and New Business

Virgilio S. Jacinto is the Corporate Secretary, Senior Vice-President and General Counsel and Compliance Officer of SMC (since October, 2010). He is a Director of San Miguel Brewery Inc. and Petron Corporation. He was formerly the Vice President and First Deputy General Counsel from 2006 to 2010 and appointed as SMC General Counsel in 2010. He was Director and Corporate Secretary of United Coconut Planters Bank, Partner at Villareal Law Offices and Associate at SyCip, Salazar, Feliciano & Hernandez Law Office. Mr. Jacinto is an Associate Professor at the University of the Philippines, College of Law. He obtained his law degree from the University of the Philippines where he is the class salutatorian and placed sixth in the 1981 bar examinations. He holds a Master of Laws degree from Harvard Law School. He holds various directorships in various local and offshore subsidiaries of SMC.

Joseph N. Pineda is the Senior Vice President and Deputy Chief Finance Officer of SMC. He is also OIC of Treasury since 2010. He was formerly Vice President prior to his promotion on July 27, 2010 and has been the Deputy Chief Finance Officer since December 2005. He was previously Special Projects Head of SMC since January 2005. Mr. Pineda has a degree of Bachelor of Arts in Economics from San Beda College and obtained units towards a Masters in Business Administration degree from De La Salle University. In addition, Mr. Pineda holds directorships in various SMC domestic and international subsidiaries.

Aurora T. Calderon is the Senior Vice President-Senior Executive Assistant to the President and Chief Operating Officer of SMC since January 20, 2011. Previous to her appointment, she was a consultant of the Company reporting to the Chief Operating Officer since 1998. She is also a member of the board of directors of Petron Corporation, Petron Marketing Corporation, Petron Freeport Corporation, SMC Global Power Holdings Corp., Sea Refinery Corporation, Thai San Miguel Liquor Co., Ltd., NVRC, Las Lucas Construction and Development Corp., and Kankiyo Corporation. She is also Director of PAL Holdings, Inc., Philippine Airlines, Inc., Trustmark Holdings Corporation, Zuma Holdings and Management Corporation, and Air Philippines Corporation. She is the President and the Director of Total Managers, Inc. and was a Director of Meralco (2009). A certified public accountant, Ms. Calderon graduated from the University of the East with a degree in BS Business Administration, major in Accountancy, *magna cum laude*. In addition, Ms. Calderon holds directorships in various SMC domestic and international subsidiaries.

Francisco S. Alejo III is the President (since 2005) and a Director (since 2001) of San Miguel Pure Foods Company Inc. He also holds the following positions: Vice Chairman of San Miguel Foods, Inc.; President of The Purefoods-Hormel Company, Inc., Magnolia, Inc. and San Miguel Super Coffeemix Co., Inc.; and Chairman and President of Sugarland Corporation and Star Dari, Inc.

Ferdinand A. Tumpalan has been President of San Miguel Yamamura Packaging Corporation since 2005. He is also President of San Miguel Yamamura Asia Corporation, San Miguel Paper Packaging Corporation, Mindanao Corrugated Fibreboard Inc. and SMC Yamamura Fuso Molds Corporation. He is a former President of the Packaging Products Division of SMC in 2005.

Roberto N. Huang is the President of San Miguel Brewery. He also served as General Manager of San Miguel Brewery Inc. (2007-2009); Director of Ginebra San Miguel Inc. (2004-2008), San Miguel Pure Foods Company, Inc. (2004-2008); President of San Miguel Beverages, Inc. (2007-2008); and President of Coca-Cola Bottlers Philippines, Inc., Cosmos Bottling Corporation and Philippine Beverage Partners, Inc. (2003-2007).

Bernard D. Marquez is the President of Ginebra San Miguel Inc. since May 12, 2011 and is a member of the Executive Committee and Nomination and Hearing Committee of GSMI. He is currently a director of Thai San Miguel Liquor Co., Ltd (“TSML”). He previously held the following positions: General Manager of TSML (January 2010-April 2011); Business Manager of the non-alcoholic beverage business of Ginebra San Miguel Inc. (July-December 2009); Assistant Vice President and Business Manager of San Miguel Beverages, Inc. (March 2007-June 2009) and Assistant Vice President and Business Planning and Development Manager of Coca-Cola Bottlers Philippines, Inc. (August 2004-February 2007).

Carlos Antonio M. Berba has been Managing Director of San Miguel Brewery International Ltd. since 2008. He is also currently Director of San Miguel Brewery Hong Kong Limited (Hong Kong) and a Commissioner of PT Delta Djarkarta Tbk (Indonesia) (“PT Delta”). He previously served SMC as President of the San Miguel Beer Division (2006); and Vice President, CFO for International Beer Operations and Director for Business Planning and Information Management, San Miguel Beer Division (2002-2006).

Alan T. Ortiz is the President and Chief Operating Officer of SMC Global Power Holdings Corp. since August 31, 2010 and a member of its Audit Committee and Nomination and Hearing Committee following his election on September 2, 2011. Previously, he was a Director of the Manila Electric Company. He is currently the Managing Partner of CEOs Inc., a Director and Treasurer of Global Resource for Outsourced Workers, Inc., and an Assistant Professor in the Department of Economics/Political Science of the Ateneo de Manila University.

Lubin B. Nepomuceno is the President of Petron Corporation since February 19, 2013. He is also a member of its Executive Committee and Compensation Committee. He holds various board and executive positions in Petron and has held various board and executive positions in various SMC domestic and international subsidiaries. He holds a Bachelor of Science degree in Chemical Engineering and a Masters in Business Administration degree from De La Salle University.

Lorenzo G. Formoso III is the Vice President of the Company since August 12, 2010 and Head of the Infrastructure and New Businesses. Previously, he was a consultant of the Company for Infrastructure, Transportation and Telecommunications from July 2009 to August 2010. He was previously Assistant Secretary of the Department of Transportation and Communication of the Philippine Government from September 2006 to June 2009 and Deputy Commissioner of the Commission on Information and Communications Technology. He obtained his Juris Doctor degree from University of California, Davis School of Law and a degree in Bachelor of Arts in Philosophy from the University of the Philippines.

Board Committees

Executive Committee

The Executive Committee is currently composed of six directors, which includes the Chairman of the Board of Directors and Chief Executive Officer, and the Vice-Chairman of the Board of Directors, President and Chief Operating Officer. Mr. Eduardo M. Cojuangco, Jr. sits as Chairman of the Committee.

The Committee acts within the power and authority granted upon it by the Board of Directors and is called upon when the Board of Directors is not in session to exercise the powers of the latter in the management of the Company, with the exception of the power to appoint any entity as general managers or management or technical consultants, to guarantee obligations of other corporations in which the Company has lawful interest, to appoint trustees who, for the benefit of the Company, may receive and retain such properties of the company or entities in which it has interests and to perform such acts as may be necessary to transfer ownership of such properties to trustees of the Company, and such other powers as may be specifically limited by the Board of Directors or by law.

Audit Committee

The Audit Committee is currently composed of five members with two independent directors as members, Mr. Margarito B. Teves, who also sits as Committee Chairman, and Mr. Winston Garcia.

The Audit Committee reviews and monitors, among others, the integrity of all financial reports and ensures their compliance with both the internal financial management manual and pertinent accounting standards, including regulatory requirements. It also performs oversight financial management functions and risk management,

approves audit plans, directly interfaces with internal and external auditors, and elevates to international standards the accounting and auditing processes, practices, and methodologies of the Company.

The Audit Committee has adopted an Audit Committee Charter in compliance with SEC Memorandum Circular No. 4 Series of 2012.

Nomination and Hearing Committee

The Nomination and Hearing Committee is currently composed of six voting directors — one of whom is independent, Mr. Reynato S. Puno — and one non-voting member in the person of the Corporate Human Resources Head of the Company. Atty. Estelito P. Mendoza is the Chairman of the Committee.

Among others, the Nomination and Hearing Committee screens and shortlists candidates for Board directorship in accordance with the qualifications and disqualifications for directors set out in the Manual on Corporate Governance of the Company (the “Manual”), the Amended Articles of Incorporation and Amended By-laws of the Company and applicable laws, rules and regulations.

Executive Compensation Committee

The Executive Compensation Committee of the Company is composed of six directors, two of whom are independent in the persons of Mr. Winston F. Garcia and Mr. Reynato S. Puno. Mr. Menardo R. Jimenez is Chairman of the Committee.

The Executive Compensation Committee advises the Board of Directors in the establishment of formal and transparent policies and practices on directors and executive remuneration and provides oversight over remuneration of senior management and other key personnel — ensuring consistency with the culture, strategy and control environment of the Company.

It designates the amount of remuneration, which shall be in a sufficient level to attract and retain directors and officers who are needed to run the Company successfully.

Significant Employees

The Company has no individual employee who is not an executive officer but who is expected to make a significant contribution to the business.

Corporate Governance

Manual on Corporate Governance

The Manual was approved by the Board of Directors on August 16, 2002 and amended on March 30, 2010. The monitoring of the implementation of the evaluation system of SMC to measure and determine the level of compliance of the Board of Directors and top level management with the Manual is vested by the Board of Directors in the Compliance Officer.

Compliance and Monitoring System

The Compliance Officer is appointed by the Board of Directors. He is responsible for monitoring compliance by the Company with the provisions and requirements of the Manual and the rules and regulations of the relevant regulatory agencies, and ensures adherence to corporate principles and best practices. The Compliance Officer holds the position of a Vice President or its equivalent and has direct reporting responsibilities to the Chairman of the Board of Directors. The Compliance Officer has certified that the Company has substantially adopted all the provisions of the Manual on Corporate Governance.

Pursuant to its commitment to good governance and business practice, the Company continues to review and strengthen its policies and procedures, giving due consideration to developments in the area of corporate governance which it determines to be in the best interests of the Company and its stockholders.

RELATED PARTY TRANSACTIONS

SMC and its subsidiaries, in their ordinary course of business, have entered into transactions with affiliates and other related parties, principally consisting of advances and sale and purchase of services and/or products. Transactions with related parties are entered into on an arm's length basis. See note 34 to SMC's consolidated financial statements included elsewhere in this Offering Memorandum for more detailed information.

TOP FRONTIER SHAREHOLDING IN SMC

On November 27, 2009, Top Frontier acquired 857,115,914 common shares from the San Miguel Corporation Retirement Plan for ₱64,284 million, at ₱75.00 per share.

On January 7, 2010, Top Frontier entered into a share purchase agreement with Q-Tech Alliance Holdings Inc. ("Q-Tech") to acquire 327,000,000 common shares for ₱66.00 per share. As a consequence of entering into such agreement, Top Frontier was required under the Securities Regulation Code of the Philippines (the "Securities Regulation Code") to make a tender offer for all SMC shares held by other parties as the acquisition would result in Top Frontier acquiring 35.0% or more of the issued and outstanding shares of SMC in one or more transactions within a 12-month period. On April 8, 2010 such tender offer closed and a total of 79,460,178 common shares were tendered for ₱75.00 per share, for a total consideration of ₱5,959.5 million. Such tendered shares were crossed in the PSE on April 13, 2010 together with the 327,000,000 common shares acquired from Q-Tech under the share purchase agreement.

Following the tender offer, Top Frontier acquired in the open market a total of 1,942,906 common shares for ₱75 per share.

On March 16, 2011, Top Frontier acquired an additional 301,666,675 common shares for ₱21,117 million, at ₱70.00 per share pursuant to an option it acquired in the share purchase agreement, dated as of January 7, 2010, with Q-Tech.

On May 5, 2011, Top Frontier made a Secondary Offering involving 110,320,000 common shares of SMC priced at ₱110 per share.

On December 1, 2011, it sold 9,000,000 common shares of SMC through the exchange priced at ₱119.12 per share.

Pursuant to an agreement entered into on November 20, 2009, Top Frontier acquired an option from the group of 44 companies associated with Eduardo M. Cojuangco, Jr., the Chairman of SMC, to acquire 476,722,639 Class A and 16,652,544 Class B common shares held by such companies for ₱37,003 million, at an option strike price of ₱75.00 per share.

On June 18, 2012, Top Frontier redeemed a total of 693,500 preferred shares out of 2,598,040 preferred shares issued to SMC at a total redemption price of ₱12.9 billion, corresponding to the original issue price of such preferred shares.

On June 29, 2012, Top Frontier exercised the option on the 125,234,667 common shares of SMC. The sale was transacted at the PSE through a special block sale at the price of ₱75.00 per share.

As of December 2012, Top Frontier held 1,573,100,340 common shares representing approximately 66.3% of the issued and outstanding SMC common shares.

Master Year Limited shareholding in SMC

On June 29, 2012, Master Year Limited purchased a total of 368,140,516 common shares of SMC. The sale was transacted at the PSE through a special block sale at the price of ₱75.00 per share.

As of December 2012, Master Year Limited held 368,140,516 common shares representing approximately 15.52% of the issued and outstanding SMC common shares.

SMC SHAREHOLDING IN TOP FRONTIER

SMC acquired 2,401,960 common shares of Top Frontier, having a par value of ₱100.00 per share, representing an approximately 49% equity interest in the issued and outstanding common shares of Top Frontier, on January 7, 2010. Such shares were purchased from Top Frontier's unissued capital stock for ₱44,676 million.

SMC also holds 2,598,040 preferred shares of Top Frontier, representing 100% of the issued and outstanding preferred shares of Top Frontier. On January 7, 2010, SMC paid the total consideration for such shares of ₱48,324 million as a deposit for future subscription for these preferred shares. The preferred shares were issued to SMC on October 22, 2010 after the Philippine SEC approved Top Frontier's application for an increase in its authorized capital stock on August 6, 2010.

The preferred shares are entitled to receive dividends at a fixed annual rate of 3% of the issue price on a cumulative basis having a par value of ₱100.00 per share. The preferred shares are non-voting and participating and are redeemable in whole or in part, at the sole option of Top Frontier, at their issue price of ₱18,600 per share, plus any accrued and unpaid dividends.

SMC's RETIREMENT PLAN

SMC's total advances to the San Miguel Corporation Retirement Plan ("SMC Retirement Fund") were ₱5,997 million and ₱5,755 million as of December 31, 2011 and 2012, respectively, which accrue interest at 5.8% per annum.

MERALCO

SMC had sales of electricity to Meralco of ₱43,990 million in 2012.

SMC held a 32.04% equity interest in Meralco as of December 31, 2012.

VEGA

Vega had advances to LTHI totaling ₱431 million as of December 31, 2012 for the purpose of working capital.

BOC

SMC had outstanding receivables from BOC totaling ₱3 million as of December 31, 2012.

PETRON

SMC advanced certain monies to the Petron Corporation Employees' Retirement Plan ("PCERP") for some investment opportunities.

SMEC

As of December 31, 2012, SMC had advances to SMEC totaling ₱36 million for the purpose of management services.

BOOK-ENTRY CLEARANCE SYSTEMS

The information set out below is subject to any change in or reinterpretation of the rules, regulations and procedures of Euroclear, Clearstream or CMU (together, the “Clearing Systems”) currently in effect. The information in this section concerning the Clearing Systems has been obtained from sources that SMC believes to be reliable, but none of SMC, the Trustee, any Dealer, any Arranger or any other party to the Agency Agreement takes any responsibility for the accuracy thereof. Investors wishing to use the facilities of any of the Clearing Systems are advised to confirm the continued applicability of the rules, regulations and procedures of the relevant Clearing System. None of SMC, the Trustee, or any other party to the Agency Agreement will have any responsibility or liability for any aspect of the records relating to, or payments made on account of, beneficial ownership interests in the Notes held through the facilities of any Clearing System or for maintaining, supervising or reviewing any records relating to, or payments made on account of, such beneficial ownership interests.

The relevant Pricing Supplement will specify the Clearing System(s) applicable for each Series.

The Clearing Systems

Euroclear and Clearstream

Euroclear and Clearstream each holds securities for participating organizations and facilitates the clearance and settlement of securities transactions between their respective participants through electronic book-entry changes in accounts of such participants. Euroclear and Clearstream provide to their respective participants, among other things, services for safekeeping, administration, clearance and settlement of internationally-traded securities and securities lending and borrowing. Euroclear and Clearstream also deal with domestic securities markets in several countries through established depository and custodial relationships. Euroclear and Clearstream have established an electronic bridge between their two systems across which their respective participants may settle trades with each other. Euroclear and Clearstream customers are world-wide financial institutions, including underwriters, securities brokers and dealers, banks, trust companies and clearing corporations.

CMU

The CMU is a central depository service provided by the Central Moneymarkets Unit of the HKMA for the safe custody and electronic trading between the members of this service (“CMU Members”) of capital markets instruments (“CMU Instruments”) which are specified in the CMU Service Reference Manual as capable of being held within the CMU. The CMU is only available for CMU Instruments issued by a CMU Member or by a person for whom a CMU Member acts as agent for the purposes of lodging instruments issued by such persons. Membership of the CMU is open to all members of the Hong Kong Capital Markets Association, “authorized institutions” under the Banking Ordinance (Cap. 155) of Hong Kong and other domestic and overseas financial institutions at the discretion of the HKMA.

Compared to clearing services provided by Euroclear and Clearstream, the standard custody and clearing service provided by the CMU is limited. In particular (and unlike the European clearing systems), the HKMA does not as part of this service provide any facilities for the dissemination to the relevant CMU Members of payments (of interest or principal) under, or notices pursuant to the notice provisions of, CMU Instruments. Instead, the HKMA advises the CMU Lodging Agent (or a designated paying agent) of the identities of the CMU Members to whose accounts payments in respect of the relevant CMU Instruments are credited, whereupon the CMU Lodging Agent (or the designated paying agent) will make the necessary payments of interest or principal or send notices directly to the relevant CMU Members.

Similarly, the HKMA will not obtain certificates of non-U.S. beneficial ownership from CMU Members or provide any such certificates on behalf of CMU Members. The CMU Lodging Agent will collect such certificates from the relevant CMU Members identified from an instrument position report obtained by request from the HKMA for this purpose.

An investor holding an interest through an account with either Euroclear or Clearstream in any Notes held in the CMU will hold that interest through the respective accounts which Euroclear and Clearstream each have with the CMU.

Book-Entry Ownership

Bearer Notes

SMC has made applications to Euroclear and Clearstream for acceptance in their respective book-entry systems in respect of any Series of Bearer Notes. SMC may also apply to have Bearer Notes accepted for clearance

through the CMU. In respect of Bearer Notes, a Temporary Bearer Global Note and/or a Permanent Bearer Global Note will be deposited with a common depositary for Euroclear and Clearstream or a sub-custodian for the CMU. Transfers of interests in a Temporary Bearer Global Note or a Permanent Bearer Global Note will be made in accordance with the normal market debt securities operating procedures of the CMU, Euroclear and Clearstream.

Registered Notes

SMC has made applications to Euroclear and Clearstream for acceptance in their respective book-entry systems in respect of the Notes to be represented by a Registered Global Note. Each Series of Registered Notes will have an International Securities Identification Number (“ISIN”) and a Common Code. Investors in Notes of such Series may hold their interests in a Registered Global Note through Euroclear or Clearstream. Registered Global Notes may also be deposited with a sub-custodian for the HKMA as operator of the CMU.

Transfers of Notes Represented by Registered Global Notes

Transfers of any interests in Notes represented by a Registered Global Note within Euroclear, Clearstream and the CMU will be effected in accordance with the customary rules and operating procedures of the relevant clearing system. Euroclear, Clearstream and the CMU have each published rules and operating procedures designed to facilitate transfers of beneficial interests in Registered Global Notes among accountholders of Euroclear, Clearstream and the CMU. However, they are under no obligation to perform or continue to perform such procedures and such procedures may be discontinued or changed at any time. None of SMC, the Trustee, the Paying Agents, the Registrar or any Dealer will be responsible for any performance by Euroclear, Clearstream or the CMU or their respective accountholders of their respective obligations under the rules and procedures governing their operations and none of them will have any liability for any aspect of the records relating to or payments made on account of beneficial interests in the Notes represented by Registered Global Notes or for maintaining, supervising or reviewing any records relating to such beneficial interests.

TAXATION

The statements herein regarding taxation are based on the laws in force as of the date of this Offering Memorandum and are subject to any changes in law occurring after such date, which changes could be made on a retroactive basis. The following summary does not purport to be a comprehensive description of all of the tax considerations that may be relevant to a decision to purchase, own or dispose of the Notes and does not purport to deal with the tax consequences applicable to all categories of investors, some of which (such as dealers in securities or commodities) may be subject to special rules. Prospective purchasers of Notes are advised to consult their own tax advisors concerning the overall tax consequences of their ownership of Notes.

As used in this section, the term “resident alien” refers to an individual whose residence is within the Philippines and who is not a citizen thereof; a “non-resident alien” is an individual whose residence is not within the Philippines and who is not a citizen of the Philippines. A non-resident alien who is actually within the Philippines for an aggregate period of more than 180 days during any calendar year is considered a “non-resident alien doing business in the Philippines,” otherwise, such non-resident alien who is actually within the Philippines for an aggregate period of 180 days or less during any calendar year is considered a “non-resident alien not doing business in the Philippines.” A “resident foreign corporation” is a non-Philippine corporation engaged in trade or business within the Philippines; and a “non-resident foreign corporation” is a non-Philippine corporation not engaged in trade or business within the Philippines.

Documentary Stamp Tax

Under the National Internal Revenue Code of 1997 as amended (the “Tax Code”), the issuance of the Notes by SMC is subject to a documentary stamp tax at the rate of one Philippine Peso (₱1.00) for each two hundred Philippine Pesos (₱200.00), or fractional part thereof, of the issue price of the Notes.

No documentary stamp tax is imposed on the subsequent sale or disposition of the Notes, trading of the Notes in a secondary market or through an exchange. However, if there is a renewal or continuance of the Notes by altering or otherwise, documentary stamp tax is payable anew.

Interest on the Notes

The Tax Code provides that interest-bearing obligations of Philippine residents are Philippine sourced income subject to Philippine income tax. Interest income derived by Philippine citizens and resident aliens from the Notes are thus subject to income tax, which is withheld at source, at the rate of 20.0% based on the gross amount of interest. Generally, interest on the Notes received by non-resident aliens engaged in trade or business in the Philippines is subject to a 20.0% final withholding tax while that received by non-resident aliens not engaged in trade or business is subject to a final withholding tax rate of 25.0%. Interest income received by domestic corporations and resident foreign corporations from the Notes is subject to a final withholding tax at the rate of 20.0%. Interest income received by non-resident foreign corporations from the Notes, which are considered foreign loans, is subject to a 20.0% final withholding tax. “Foreign loans” are loan contracts, including all debt items, whether in kind or in cash, which are denominated and payable in foreign currency or in kind, entered into by a Philippine resident, corporate or otherwise, as a borrower, with a non-resident, as a lender.

Therefore, to the extent that the holder of the Notes is a non-resident foreign corporation, the Notes will be considered foreign loans.

While interest paid on the Notes is subject to Philippine withholding taxes as described above, the payment of such taxes with respect to interest on the Notes will generally be made by SMC without deduction of any amounts therefor from the interest to be remitted to the holders of the Notes. The holders will generally receive the same amounts they would have received had no such withholding taxes been imposed. See “*Terms and Conditions of the Notes — Taxation.*” The effect of such contract or provision is to make the Notes “tax-free covenant bonds.” With respect to interest on tax-free covenant bonds, SMC is required to withhold a tax equal to 30.0% of the interest if such interest is payable to a non-resident alien or to a citizen or resident of the Philippines.

Any tax treaty in force between the Philippines and the country of residence of a non-resident holder of the Notes may provide for reduced withholding tax rates on interest. Most tax treaties to which the Philippines is a party generally provide for a reduced tax rate of 15.0% in cases where the interest arises in the Philippines and is paid to a resident of the other contracting state. A majority of tax treaties to which the Philippines is a party generally provide for a reduced tax rate of 10.0%, in cases where the interest is derived by a resident of the other contracting state from Philippine sources with respect to public issues of bonded indebtedness. However, most tax treaties also provide that the reduced withholding tax rate will not apply if the recipient of the interest, who is a resident of the other contracting state, carries on business in the Philippines through a permanent establishment and the holding of the Notes is effectively connected with such permanent establishment.

Preferential tax rates under applicable income tax treaties may be availed of if an application for tax treaty relief is filed with, and approved by, Philippine tax authorities.

Sale or Other Disposition of the Notes

Any gain realized from the sale, exchange or retirement of the Notes will, as a rule, form part of the gross income of the sellers, for purposes of computing the relevant taxable income subject to the applicable regular income tax rates: (1) variable rates based on net annual taxable income, the highest of which is 32.0% of net taxable income of Philippine citizens, resident aliens and non-resident aliens engaged in trade or business in the Philippines, (2) 25.0% final withholding tax for sellers who are non-resident aliens not engaged in trade or business in the Philippines, (3) 30.0% of net taxable income of domestic corporations and resident foreign corporations and (4) 30.0% final withholding tax for sellers which are non-resident foreign corporations. If the Notes are sold by a seller, who is an individual and who is not a dealer in securities, who has held the Notes for a period of more than 12 months prior to the sale, only 50.0% of any capital gain will be recognized and included in the seller's gross taxable income.

However, any such gain may not be subject to Philippine income tax if the seller is a foreign corporation or an individual who is not a Philippine citizen, and the sale of the Notes is deemed to have taken place outside the Philippines.

Moreover, under the Tax Code, any gain realized from the sale, exchange or retirement of bonds, debentures and other certificates of indebtedness with an original maturity date of more than five years (as measured from the date of issuance of such bonds, debentures or other certificates of indebtedness) shall not be subject to income tax.

Finally, any gain arising from such sale, regardless of the original maturity date of the bonds, may be exempt from Philippine income tax pursuant to various income tax treaties to which the Philippines is a party, and subject to procedures prescribed by the BIR for the availment of tax treaty benefits.

Estate and Donor's Tax

Notes issued by a corporation organized or constituted in the Philippines in accordance with Philippine laws are deemed to have a Philippine situs and their transfer by way of succession or donation is subject to Philippine estate and gift taxes.

The transfer by a deceased person, whether a Philippine resident or a non-Philippine resident, to his heirs of the Notes shall be subject to an estate tax which is levied on the net estate of the deceased at progressive rates ranging from 5.0% to 20.0%, if the net estate is over ₱200,000.00. A Noteholder shall be subject to donor's tax based on the net gift on the transfer of the Notes by gift at either (i) 30.0%, where the donee or beneficiary is a stranger, or (ii) progressive rates ranging from 2.0% to 15.0% if the net gifts made during the calendar year exceed ₱100,000.00 and where the donee or beneficiary is not a stranger. For this purpose, a "stranger" is a person who is not a: (a) brother, sister (whether by whole or half-blood), spouse, ancestor or lineal descendant; or (b) relative by consanguinity in the collateral line within the fourth degree of relationship.

The estate or donor's taxes payable in the Philippines may be credited with the amount of any estate or donor's taxes imposed by the authority of a foreign country, subject to limitations on the amount to be credited, and the tax status of the donor. The estate tax and the donor's tax, in respect of the Notes, shall not be collected (a) if the deceased, at the time of death, or the donor, at the time of the donation, was a citizen and resident of a foreign country which, at the time of his death or donation, did not impose a transfer tax of any character in respect of intangible personal property of citizens of the Philippines not residing in that foreign country; or (b) if the laws of the foreign country of which the deceased or donor was a citizen and resident, at the time of his death or donation, allows a similar exemption from transfer or death taxes of every character or description in respect of intangible personal property owned by citizens of the Philippines not residing in the foreign country.

In case the Notes are transferred for less than an adequate and full consideration in money or money's worth, the amount by which the fair market value of the Notes exceeded the value of the consideration may be deemed a gift and may be subject to donor's taxes.

EU Directive on the Taxation of Savings Income

Under EC Council Directive 2003/48/EC on the taxation of savings income (the "Directive"), Member States are required to provide to the tax authorities of another Member State details of payments of interest (or similar income) paid by a person within its jurisdiction to an individual resident in that other Member State or to certain

limited types of entities established in that other Member State. However, for a transitional period, Luxembourg and Austria are instead required (unless during that period they elect otherwise) to operate a withholding system in relation to such payments (the ending of such transitional period being dependent upon the conclusion of certain other agreements relating to information exchange with certain other countries). A number of non-EU countries and territories including Switzerland have adopted similar measures (a withholding system in the case of Switzerland).

The European Commission has proposed certain amendments to the Directive, which may, if implemented, amend or broaden the scope of the requirements described above.

SUBSCRIPTION AND SALE

The Dealers have, in a programme agreement dated April 15, 2013 as amended and/or supplemented from time to time (the “Programme Agreement”), agreed with SMC a basis on which they or any of them may from time to time agree to subscribe Notes. Any such agreement will extend to those matters stated under “*Form of the Notes*” and “*Terms and Conditions of the Notes*.” Under the terms of the Programme Agreement, SMC will pay each relevant Dealer a commission as agreed between them in respect of Notes subscribed by it. SMC has agreed to reimburse the Arrangers for certain of its expenses incurred in connection with the establishment of the Programme and any future update of the Programme and the Dealers for certain of their activities in connection with the Programme.

SMC has agreed to indemnify the Dealers against certain liabilities in connection with the offer and sale of the Notes. The Programme Agreement entitles the Dealers to terminate any agreement that they make to subscribe Notes in certain circumstances prior to payment for such Notes being made to SMC.

The Dealers and certain of their affiliates may have performed certain investment banking and advisory services for SMC and/or its affiliates from time to time for which they have received customary fees and expenses and may, from time to time, engage in transactions with and perform services for SMC and/or its affiliates in the ordinary course of their business.

In connection with each Tranche of Notes issued under the Programme, the Dealers or certain of their affiliates may purchase Notes and be allocated Notes for asset management and/or proprietary purposes but not with a view to distribution. Further, the Dealers or their respective affiliates may purchase Notes for its or their own account and enter into transactions, including credit derivatives, such as asset swaps, repackaging and credit default swaps relating to such Notes and/or other securities of SMC or its subsidiaries or affiliates at the same time as the offer and sale of each Tranche of Notes or in secondary market transactions. Such transactions would be carried out as bilateral trades with selected counterparties and separately from any existing sale or resale of the Tranche of Notes to which a particular Pricing Supplement relates (notwithstanding that such selected counterparties may also be purchasers of such Tranche of Notes).

United States

1.1 In respect of Notes offered or sold in reliance on Regulation S Category 1 (as defined in Rule 903(b)(1) under the Securities Act) as specified in the applicable Pricing Supplement, the Notes have not been and will not be registered under the Securities Act or the securities laws of any state in the United States, and may not be offered, sold or resold within the United States except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act. Each Dealer has represented and agreed that it has not offered, sold or resold, and will not offer or sell, any such Notes constituting part of its allotment in the United States except in accordance with Rule 903(b)(1) of Regulation S under the Securities Act.

In respect of Notes offered or sold in reliance on Regulation S Category 2 (as defined in Rule 903(b)(2) under the Securities Act) as specified in the applicable Pricing Supplement, the Notes have not been and will not be registered under the Securities Act or the securities laws of any state in the United States, and may not be offered, sold or resold within the United States or to, or for the account or benefit of, any “U.S. person” (as defined in Rule 902(k) under the Securities Act) except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act. Each Dealer has represented and agreed that it has not offered and sold any such Notes, and will not offer and sell any such Notes (i) as part of their distribution at any time and (ii) otherwise until 40 days after the completion of the distribution of all Notes of the Tranche of which such Notes are a part, as determined and certified as provided below, except in accordance with Rule 903(b)(2) of Regulation S under the Securities Act. Each Dealer who has purchased Notes of a Tranche hereunder (or in the case of a sale of a Tranche of Notes issued to or through more than one Dealer, each of such Dealers as to the Notes of such Tranche purchased by or through it or, in the case of a syndicated issue, the relevant Lead Manager) shall determine and certify to the Principal Paying Agent the completion of the distribution of the Notes of such Tranche. On the basis of such notification or notifications, the Principal Paying Agent has agreed to notify such Dealer/Lead Manager of the end of the distribution compliance period with respect to such Tranche. Each Dealer has also agreed that, at or prior to confirmation of the sale of the Notes, it will have sent to each distributor, dealer or person receiving a selling concession, fee or other remuneration that purchases Notes from it during the distribution compliance period, a confirmation or notice to substantially the following effect:

“The Securities covered hereby have not been registered under the U.S. Securities Act of 1933, as amended (the Securities Act), or with any securities regulatory authority of any state or other

jurisdiction of the United States, and may not be offered, sold or resold within the United States or to, or for the account or benefit of, any “U.S. person” (as defined in Rule 902(k) under the Securities Act) (i) as part of their distribution at any time or (ii) otherwise until 40 days after the completion of the distribution of the Securities as determined and certified by the relevant Dealer, in the case of a non-syndicated issue, or the Lead Manager, in the case of a syndicated issue, and except in either case in accordance with Regulation S under the Securities Act. Terms used above have the meanings given to them by Regulation S.”

Terms used in this paragraph 1.1 have the meanings given to them by Regulation S.

- 1.2 Each Dealer has further represented and agreed that it, its affiliates or any persons acting on its or their behalf have not engaged and will not engage in any “directed selling efforts” (as defined in Rule 902(c) under the Securities Act) with respect to any Note, and it and they have complied and will comply with the offering restrictions requirement of Regulation S.
- 1.3 In addition in respect of Bearer Notes where TEFRA D is specified in the applicable Pricing Supplement:
 - (a) except to the extent permitted under U.S. Treas. Reg. Section 1.163-5(c)(2)(i)(D) (the “D Rules”), each Dealer (i) has represented and agreed that it has not offered or sold, and agrees that during the restricted period it will not offer or sell, Notes in bearer form to a person who is within the United States or its possessions or to a United States person, and (ii) has represented that it has not delivered and agreed that it will not deliver within the United States or its possessions definitive Notes in bearer form that are sold during the restricted period;
 - (b) each Dealer has represented and agreed that it has and agreed that throughout the restricted period it will have in effect procedures reasonably designed to ensure that its employees or agents who are directly engaged in selling Notes in bearer form are aware that such Notes may not be offered or sold during the restricted period to a person who is within the United States or its possessions or to a United States person, except as permitted by the D Rules;
 - (c) if it is a United States person, each Dealer has represented and agreed that it is acquiring Notes in bearer form for purposes of resale in connection with their original issuance and if it retains Notes in bearer form for its own account, it will only do so in accordance with the requirements of U.S. Treas. Reg. Section 1.163-5(c)(2)(i)(D)(6); and
 - (d) with respect to each affiliate that acquires Notes in bearer form from a Dealer for the purpose of offering or selling such Notes during the restricted period, such Dealer has repeated and confirmed the representations and agreements contained in subparagraphs 1.3(a), 1.3(b) and 1.3(c) on such affiliate’s behalf.

Terms used in this paragraph 1.3 have the meanings given to them by the U.S. Internal Revenue Code of 1986 and Treasury regulations promulgated thereunder, including the D Rules.

- 1.4 In respect of Bearer Notes where TEFRA C is specified in the applicable Pricing Supplement, such Bearer Notes must be issued and delivered outside the United States and its possessions in connection with their original issuance. Each Dealer has represented and agreed that it has not offered, sold or delivered, and will not offer, sell or deliver, directly or indirectly, such Bearer Notes within the United States or its possessions in connection with their original issuance. Further, each Dealer has represented and agreed in connection with the original issuance of such Bearer Notes that it has not communicated, and will not communicate, directly or indirectly, with a prospective purchaser if such purchaser is within the United States or its possessions and will not otherwise involve its U.S. office in the offer or sale of such Bearer Notes.

Terms used in this paragraph 1.4 have the meanings given to them by the U.S. Internal Revenue Code of 1986 and Treasury regulations promulgated thereunder.

- 1.5 Each issue of Index Linked Notes or Dual Currency Notes shall be subject to such additional U.S. selling restrictions as SMC and the relevant Dealer may agree as a term of the issue and purchase of such Notes, which additional selling restrictions shall be set out in the applicable Pricing Supplement. The relevant Dealer has agreed that it shall offer, sell and deliver such Notes only in compliance with such additional U.S. selling restrictions.

Public Offer Selling Restriction under the Prospectus Directive

In relation to each Member State of the European Economic Area which has implemented the Prospectus Directive (each, a “Relevant Member State”), each Dealer has represented and agreed, and each further Dealer appointed under the Programme will be required to represent and agree, that with effect from and including the date on which the Prospectus Directive is implemented in that Relevant Member State (the “Relevant

Implementation Date”) it has not made and will not make an offer of Notes which are the subject of the offering contemplated by this Offering Memorandum as completed by the Pricing Supplement in relation thereto to the public in that Relevant Member State except that it may, with effect from and including the Relevant Implementation Date, make an offer of such Notes to the public in that Relevant Member State:

- (a) if the Pricing Supplement in relation to the Notes specify that an offer of those Notes may be made other than pursuant to Article 3(2) of the Prospectus Directive in that Relevant Member State (a “Non-exempt Offer”), following the date of publication of a prospectus in relation to such Notes which has been approved by the competent authority in that Relevant Member State or, where appropriate, approved in another Relevant Member State and notified to the competent authority in that Relevant Member State, provided that any such prospectus has subsequently been completed by the Pricing Supplement contemplating such Non-exempt Offer, in accordance with the Prospectus Directive, in the period beginning and ending on the dates specified in such prospectus or pricing supplement, as applicable and SMC has consented in writing to its use for the purpose of that Non-exempt offer;
- (b) at any time to any legal entity which is a qualified investor as defined in the Prospectus Directive;
- (c) at any time to fewer than 100 or, if the Relevant Member State has implemented the relevant provision of the 2010 PD Amending Directive, 150, natural or legal persons (other than qualified investors as defined in the Prospectus Directive), subject to obtaining the prior consent of the relevant Dealer or Dealers nominated by SMC for any such offer; or
- (d) at any time in any other circumstances falling within Article 3(2) of the Prospectus Directive,

provided that no such offer of Notes referred to in (b) to (d) above shall require SMC or any Dealer to publish a prospectus pursuant to Article 3 of the Prospectus Directive or supplement a prospectus pursuant to Article 16 of the Prospectus Directive.

For the purposes of this provision, the expression “an offer of Notes to the public” in relation to any Notes in any Relevant Member State means the communication in any form and by any means of sufficient information on the terms of the offer and the Notes to be offered so as to enable an investor to decide to purchase or subscribe the Notes, as the same may be varied in that Member State by any measure implementing the Prospectus Directive in that Member State, the expression “Prospectus Directive” means Directive 2003/71/EC (and amendments thereto, including the 2010 PD Amending Directive, to the extent implemented in the Relevant Member State), and includes any relevant implementing measure in the Relevant Member State and the expression “2010 PD Amending Directive” means Directive 2010/73/EU.

United Kingdom

Each Dealer has represented and agreed, and each further Dealer appointed under the Programme will be required to represent and agree, that:

- (a) in relation to any Notes which have a maturity of less than one year (i) it is a person whose ordinary activities involve it in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of its business and (ii) it has not offered or sold and will not offer or sell any Notes other than to persons whose ordinary activities involve them in acquiring, holding, managing or disposing of investments (as principal or as agent) for the purposes of their businesses or who it is reasonable to expect will acquire, hold, manage or dispose of investments (as principal or agent) for the purposes of their businesses where the issue of the Notes would otherwise constitute a contravention of Section 19 of the FSMA by SMC;
- (b) it has only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of Section 21 of the FSMA) received by it in connection with the issue or sale of any Notes in circumstances in which Section 21(1) of the FSMA does not apply to SMC; and
- (c) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to any Notes in, from or otherwise involving the United Kingdom.

The Netherlands

Each Dealer has represented and agreed, and each further Dealer appointed under the Programme will be required to represent and agree, that any Notes will only be offered in The Netherlands to Qualified Investors (as defined in the EU Prospectus Directive), unless such offer is made in accordance with the Dutch Financial Supervision Act (*Wet op het financieel toezicht*).

Japan

The Notes have not been and will not be registered under the Financial Instruments and Exchange Act of Japan (Act No. 25 of 1948, as amended; the “FIEA”) and each Dealer has represented and agreed, and each further Dealer appointed under the Programme will be required to represent and agree, that it will not offer or sell any Notes, directly or indirectly, in Japan or to, or for the benefit of, any resident of Japan (as defined under Item 5, Paragraph 1, Article 6 of the Foreign Exchange and Foreign Trade Act (Act No. 228 of 1949, as amended)), or to others for re-offering or resale, directly or indirectly, in Japan or to, or for the benefit of, a resident of Japan, except pursuant to an exemption from the registration requirements of, and otherwise in compliance with, the FIEA and any other applicable laws, regulations and ministerial guidelines of Japan.

Hong Kong

In relation to each Tranche of Notes, each Dealer has represented and agreed, and each further Dealer appointed under the Programme will be required to represent and agree, that:

- (i) it has not offered or sold and will not offer or sell in Hong Kong, by means of any document, any Notes (except for Notes which are a “structured product” as defined in the Securities and Futures Ordinance (Cap. 571) of Hong Kong (the “Securities and Futures Ordinance”)) other than (i) to “professional investors” as defined in the Securities and Futures Ordinance and any rules made under that Ordinance; or (ii) in other circumstances which do not result in the document being a “prospectus” as defined in the Companies Ordinance (Cap. 32) of Hong Kong or which do not constitute an offer to the public within the meaning of that Ordinance; and
- (ii) it has not issued or have in its possession for the purposes of issue and will not issue or have in its possession for the purposes of issue, any advertisement, invitation or document relating to the Notes, whether in Hong Kong or elsewhere, which is directed at, or the contents of which are likely to be accessed or read by, the public in Hong Kong (except if permitted to do so under the securities laws of Hong Kong) other than with respect to Notes which are or are intended to be disposed of only to persons outside Hong Kong or only to “professional investors” as defined within the Securities and Futures Ordinance and any rules made under that Ordinance.

Singapore

The Offering Memorandum has not been registered as a prospectus with the Monetary Authority of Singapore, and the Notes will be offered pursuant to exemptions under the Securities and Futures Act, Chapter 289 of Singapore (the “Securities and Futures Act”). Accordingly, each Dealer has represented and agreed, and each further Dealer appointed under the Programme will be required to represent and agree, that it has not offered or sold or made the subject of an invitation for subscription or purchase nor may the Offering Memorandum or any other document or material in connection with the offer or sale or invitation for subscription or purchase of any Notes be circulated or distributed, whether directly or indirectly, to the any person in Singapore other than (a) to an institutional investor pursuant to Section 274 of the Securities and Futures Act, (b) to a relevant person under Section 275(1) of the Securities and Futures Act, or any person pursuant to Section 275(1A) of the Securities and Futures Act, and in accordance with the conditions specified in Section 275 of the Securities and Futures Act or (c) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the Securities and Futures Act.

Where the Notes are subscribed or purchased under Section 275 of the Securities and Futures Act by a relevant person which is:

- (a) a corporation (which is not an accredited investor (as defined in Section 4A of the Securities and Futures Act)) the sole business of which is to hold investments and the entire share capital of which is owned by one or more individuals, each of whom is an accredited investor;
- (b) a trust (where the trustee is not an accredited investor) whose sole purpose is to hold investments and each beneficiary is an individual who is an accredited investor,

securities (as defined in Section 239(1) of the Securities and Futures Act) of that corporation or the beneficiaries’ rights and interest (howsoever described) in that trust shall not be transferable for 6 months after that corporation or that trust has acquired the Notes pursuant to an offer under Section 275 of the Securities and Futures Act except:

- (i) to an institutional investor or to a relevant person defined in Section 275(2) of the Securities and Futures Act or to any person arising from an offer referred to in Section 275(1A) or Section 276(4)(i)(B) of the Securities and Futures Act; or

- (ii) where no consideration is or will be given for the transfer; or
- (iii) where the transfer is by operation of law; or
- (iv) pursuant to Section 276(7) of the Securities and Futures Act or Regulation 32 of the Securities and Futures (Offers of Investments) (Shares and Debentures) Regulations.

The Philippines

The Notes being offered or sold have not been and will not be registered with the Philippine SEC under the SRC. Any offer or sale of the Notes within the Philippines is subject to registration unless such offer or sale is made under circumstances in which the Notes qualify as exempt securities or pursuant to an exempt transaction under the SRC. The offer or sale of the Notes in the Philippines to (a) “primary institutional lenders” pursuant to Rule 9.2(2) B of the amended implementing rules of the SRC, or (b) persons who are “qualified buyers” pursuant to Section 10.1(l) of the SRC, or (c) not more than nineteen (19) persons who are not “qualified buyers” during any twelve-month period pursuant to Section 10.1(k) of the SRC is exempt from registration. SMC has not obtained confirmation from the Philippine SEC that the offer and sale of the Notes within the Philippines qualifies as an exempt transaction. If necessary, SMC will file a notice of exemption from registration with the Philippine SEC pursuant to SRC Rule 10.1(3).

Each Joint Arranger and Dealer has represented, warranted and agreed that it has not and will not sell or offer for sale or distribution any Notes in the Philippines except to “primary institutional lenders” pursuant to Rule 9.2(2) B of the amended implementing rules of the SRC or to “qualified buyers” pursuant to Section 10.1(l) of the SRC.

The People’s Republic of China

Each Dealer has represented and agreed, and each further Dealer appointed under the Programme will be required to represent and agree, that it has not offered or sold and will not offer or sell any of the Notes in the People’s Republic of China (for such purposes, not including Hong Kong, Macau SAR or Taiwan) or to residents of the People’s Republic of China unless such offer or sale is made in compliance with all applicable laws and regulations of the People’s Republic of China.

General

Each Dealer has represented and agreed and each further Dealer appointed under the Programme will be required to represent and agree that it will (to the best of its knowledge and belief) comply with all applicable securities laws and regulations in force in any jurisdiction in which it purchases, offers, sells or delivers Notes or possesses or distributes the Offering Memorandum and will obtain any consent, approval or permission required by it for the purchase, offer, sale or delivery by it of Notes under the laws and regulations in force in any jurisdiction to which it is subject or in which it makes such purchases, offers, sales or deliveries and none of the Issuer, the Trustee and any other Dealer shall have any responsibility therefor.

None of SMC, the Trustee or any of the Dealers represent that Notes may at any time lawfully be sold in compliance with any applicable registration or other requirements in any jurisdiction, or pursuant to any exemption available thereunder, or assumes any responsibility for facilitating such sale.

With regard to each Tranche, the relevant Dealer will be required to comply with any additional restrictions agreed between SMC and the relevant Dealer and set out in the applicable Pricing Supplement.

GENERAL INFORMATION

- (1) **Listing of Notes:** Approval in-principle has been granted by the SGX-ST for permission to deal in and for quotation of any Notes which are agreed at the time of issue thereof to be so listed on the SGX-ST. There is no assurance that the application to the Official List of the SGX-ST for the listing of the Notes will be approved. Admission to the Official List of the SGX-ST and quotation of any Notes on the SGX-ST is not to be taken as an indication of the merits of the Programme, the Notes, SMC or SMC's subsidiaries. The SGX-ST assumes no responsibility for the correctness of any of the statements made or opinions or reports contained herein.
- (2) **Authorizations:** SMC has obtained all necessary consents, approvals and authorizations in connection with the establishment of the Programme. The establishment of the Programme was authorized by resolutions of the board of directors of SMC dated April 11, 2013.
- (3) **No Material Adverse Change:** Other than as disclosed in this Offering Memorandum, there has been no material adverse change in the financial or trading position or prospects of SMC since December 31, 2012.
- (4) **Litigation:** Save as disclosed in this Offering Memorandum, SMC is not involved in any litigation or arbitration proceedings that the Guarantor believes are material in the context of the Notes nor is SMC aware that any such proceedings are pending or threatened.
- (5) **Bearer Notes, Receipts, Coupons and Talons:** Each Bearer Note having a maturity of more than one year, Receipt, Coupon and Talon will bear the following legend: "Any United States person (as defined in the Internal Revenue Code of the United States) who holds this obligation will be subject to limitations under the United States income tax laws, including the limitations provided in Sections 165(j) and 1287(a) of the Internal Revenue Code."
- (6) **Clearing of the Notes:** The Notes may be accepted for clearance through Euroclear, Clearstream and the CMU. The appropriate ISIN and common code or CMU Instrument Number in relation to the Notes of each Tranche will be specified in the relevant Pricing Supplement. If the Notes are to be cleared through any additional or alternative Clearing System, the appropriate information will be specified in the applicable Pricing Supplement.
- (7) **Available Documents:** For so long as Notes may be issued pursuant to this Offering Memorandum, the following documents will be available, during normal business hours on any weekday (Saturdays, Sundays and public holidays excepted), for inspection at the specified office of the Paying Agent at Level 52, International Commerce Centre, 1 Austin Road West, Kowloon, Hong Kong:
 - (i) the Trust Deed (which includes the form of the Global Notes, the Notes in definitive form, the Coupons, the Receipts and the Talons);
 - (ii) the Agency Agreement;
 - (iii) the Programme Agreement;
 - (iv) the Amended Articles of Incorporation and Amended By-Laws of SMC;
 - (v) SMC's audited consolidated financial statements for the years ended December 31, 2011 and 2012;
 - (vi) filings and announcements posted on the PSE;
 - (vii) each Pricing Supplement (save that a Pricing Supplement related to an unlisted Series of Notes will only be available for inspection by a holder of any such Notes and such holder must produce evidence satisfactory to SMC or the Trustee as to its holding of Notes and identity); and
 - (viii) a copy of this Offering Memorandum together with any supplement to this Offering Memorandum and any other documents incorporated herein or therein referenced.
- (8) **Independent Auditors:** The audited consolidated financial statements of SMC as of and for each of the years ended December 31, 2010, 2011 and 2012 appearing in this Offering Memorandum, have been audited by KPMG Manabat Sanagustin & Co., independent auditors, as set forth in their reports appearing herein.

GLOSSARY

In this Offering Memorandum, unless the context otherwise requires, the following terms shall have the meanings set forth below.

AAI	Atlantic Aurum Investments BV
ACA	Automatic Cost Adjustment Mechanism
AGNP	A.G.N. Philippines, Inc.
Air Phil	Air Philippines Corporation
ASEAN	The Association of Southeast Asian Nations, including Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Vietnam
BellTel	Bell Telecommunication Philippines, Inc.
BERI	Bonanza Energy Resources, Inc.
BOC	Bank of Commerce
BOT	Build-Operate-Transfer
BIR	Bureau of Internal Revenue of the Philippines
bpd	Barrels per day
BSP	Bangko Sentral ng Pilipinas, the Central Bank of the Philippines
BSP Rate	The weighted average rate for the purchase of U.S. dollars with Philippine Pesos, as published by the BSP
Bumi Resources	PT Bumi Resources TBK
CA	Co-Production Agreement
CAAP	Civil Aviation Authority of the Philippines
Captive Market	A market of end-users who do not have a choice of their supplier of electricity, as determined by the ERC
CIIP	Comprehensive and Integrated Infrastructure Program
Clean Air Act	The Philippine Clean Air Act of 1999
Clean Water Act	The Philippine Clean Water Act of 2004
CMMTC	Citra Metro Manila Tollways Corporation
COCO	Company-owned-company-operated service stations
CODO	Company-owned-dealer-operated service stations
Concord Energy	Concord Energy Pte Ltd
Contestable Market	A market of end-users who have a choice on their supplier of electricity
Corporation Code	Batas Pambansa Blg. 68, otherwise known as the Corporation Code of the Philippines
DA	Department of Agriculture of the Philippines
DAMI	Daguma Agro Minerals, Inc.
DENR	Department of Environment and Natural Resources of the Philippine
Distribution Code	The Philippine Distribution Code
DODO	Dealer-owned-dealer-operated service stations
DOE	Department of Energy of the Philippines
DOH	Department of Health of the Philippines, including the FDA

DOLE	Department of Labor and Employment of the Philippines
DSO	Dairy products, spreads and oils
DTI	Department of Trade and Industry of the Philippines
EBITDA	Earnings before interest, taxes, depreciation and amortization
ECA	Energy conversion agreement
ECC	Environmental Compliance Certificate
EIS	Environmental Impact Statement
EISS Law	Philippine Environmental Impact Statement System
EPEP	Environmental Protection and Enhancement Program
EPIRA	Philippine Republic Act No. 9136, otherwise known as the Electric Power Industry Reform Act of 2001
ERC	Energy Regulatory Commission of the Philippines
ETPI	Eastern Telecommunications Philippines, Inc.
Expanded VAT Law	The Philippine Republic Act No. 9337
FDA	Food and Drug Administration of the Philippines
FDDC Act	The Philippine Foods, Drugs and Devices and Cosmetics Act, as amended by the Food and Drug Administration Act of 2009
FIA	Foreign Investment Act of 1991
FSMA	Financial Services and Markets Act 2000
FTAA	financial or technical assistance agreements
GBGTC	Golden Bay Grain Terminal Corporation
GDP	Gross domestic product
Ginebra	Ginebra San Miguel Inc., including, as the context requires, its subsidiaries
GNP	Gross national product
Grid Code	The Philippine Grid Code
GWh	Giga-watt hours
hl	Hecto-liters, equivalent to 100 liters
Ilijan Power Plant	Natural gas fired combined cycle power plant with installed capacity of 2 x 600 MW located in Ilijan, Batangas
Indophil	Indophil Resources NL
IMS	Integrated Management System
IPP	Independent power producer
IPPA	Independent power producer administrator
IPPA Agreement	Independent power producer administration agreement
ISO	International Organization for Standardization
JVA	Joint Venture Agreement
Kirin	Kirin Holding Company, Limited
Liberty	Liberty Telecoms Holdings, Inc. including, as the context requires, its subsidiaries
Limay Refinery	Petron's refinery located in Limay, Bataan

Livestock and Poultry Feeds Act	The Philippine Livestock and Poultry Feeds Act, including its implementing rules and regulations
LPG	Liquefied petroleum gas
LSFO	Low sulfur fuel oil
Magnolia	Magnolia Inc.
MARINA	Maritime Industry Authority of the Philippines
Meat Inspection Code	The Meat Inspection Code of the Philippines
MEQ	Minimum energy quantity
Meralco	Manila Electric Company
MGB	Mines and Geosciences Bureau
Mincorr	Mindanao Corrugated Fibreboard, Inc.
MPSA	Mineral Production Sharing Agreement
Monetary Board	The Monetary Board of the BSP
MRT-7	Metro Rail Transit Line 7
Must Pay Volume	The monthly generation payments SMC Global Power “must pay” for electricity sold up to a given volume
MW	megawatt or megawatts, as the context may require
MYL	Master Year Limited
NEA	National Electrification Administration of the Philippines
Negative List	Ninth Regular Foreign Investment Negative List issued by the Office of the President of the Philippines on October 29, 2012
NGCP	National Grid Corporation of the Philippines
Nielsen	A.C. Nielsen
Non-Delivering Day	Any day that a power plant is unable to produce power for an entire day, for reasons not attributable to SMC Global Power
NPC	National Power Corporation of the Philippines
NSCB	National Statistical Coordination Board of the Philippines
NSO	National Statistics Office of the Republic of the Philippines
NTC	National Telecommunications Commission of the Philippines
NVRC	New Ventures Realty Corporation
NYG	Nihon Yamamura Glass Co. Ltd.
Oil Deregulation Act	The Philippine Republic Act No. 8479, otherwise known as the Downstream Oil Industry Deregulation Act of 1998
Open Access	System of allowing qualified persons to use the transmission and/or distribution systems and associated facilities of distribution utilities subject to the payment of transmission and/or distribution wheeling rates approved by the ERC
Packaging Group	SMYPC, SMYPIL and its subsidiaries, SMYAC and Mincorr
PAHL	Petrochemical Asia (Hong Kong) Ltd
PAL	Philippine Airlines, Inc.
PBR	Performance-based regulation
PEMC	Philippine Electricity Market Corporation

Peso or ₱	Philippine Peso, the lawful currency of the Republic of the Philippines
PET	Polyethylene terephthalate
Petron	Petron Corporation
PFF Act	The Philippine Food Fortification Act of 2000
PFRS	Philippine Financial Reporting Standards
PhilHealth	Philippine Health Insurance Corporation
Philippine SEC	The Philippine Securities and Exchange Commission
PIDC	Private Infra Dev Corporation
PNOC	Philippine National Oil Company
Port Dickson Refinery	Petron's refinery located in Port Dickson, Malaysia
PPA	Power purchase agreement
PPI	Philippine Polypropylene Inc.
PPP	Public-Private Partnership
Price Act	Philippine Republic Act No. 7581
PSALM	Power Sector Assets and Liabilities Management Corporation
PSC	Power supply contract
PSE	The Philippine Stock Exchange, Inc.
Q-Tech	Q-Tech Alliance Holdings Inc.
RAM	Reliability, Availability and Maintenance program
RMP-2	Phase 2 of the Refinery Master Plan of Petron
San Miguel Pure Foods	San Miguel Pure Foods Company Inc., including, as the context requires, its subsidiaries
San Roque Power Plant	Hydroelectric multipurpose power plant with installed capacity of 345 MW located in San Manuel, Pangasinan
San Roque PPA	NPC's PPA with SRPC pertaining to the San Roque Power Plant
Saudi Aramco	Saudi Arabian Oil Company
SEPC	Sultan Energy Phils. Corp.
SGX-ST	Singapore Exchange Securities Trading Limited
Skyway	Metro Manila Skyway Project, an elevated expressway
SLEX	South Luzon Expressway
SLTC	South Luzon Tollway Corporation
SMB	San Miguel Brewery Inc. including, as the context requires, its subsidiaries
SMBIL	San Miguel Brewing International Ltd.
SMC, the Company or the Parent Company	San Miguel Corporation
SMC Global Power	SMC Global Power Holdings Corp. including, as the context requires, its subsidiaries
SMC Group	SMC and its subsidiaries
SMC Retirement Fund	San Miguel Corporation Retirement Plan
SMEC	San Miguel Energy Corporation

SMEII	San Miguel Equity Investments Inc.
SMHC	San Miguel Holdings Corp.
SMMI	San Miguel Mills, Inc.
SMPI	San Miguel Properties, Inc. including, as the context requires, its subsidiaries
SMYAC	San Miguel Yamamura Asia Corporation
SMYPC	San Miguel Yamamura Packaging Corporation including, as the context requires, its subsidiaries
SMYPIL	San Miguel Yamamura Packaging International Limited including, as the context requires, its subsidiaries
SPDC	Strategic Power Devt. Corp.
SPPC	South Premiere Power Corp.
SRPC	San Roque Power Corporation
Sual ECA	NPC's ECA with TeaM Energy pertaining to the Sual Power Plant
Sual Power Plant	2 x 500 MW Coal-fired power plant located in Sual, Pangasinan
T1 Volume	80% of the statutory rate SMC Global Power charges Meralco for supplying electrical power under the offtake agreement between SMC Global Power and Meralco for the given month multiplied by a factor equal to the volume sold
TADHC	Trans Aire Development Holdings Corp.
Tax Code	The Philippine National Internal Revenue Code of 1997, as amended
TeaM Energy	Team Sual Corporation
Terms and Conditions	Terms and conditions of the Notes
THI	Terramino Holdings, Inc.
Top Frontier	Top Frontier Investment Holdings, Inc.
TransCo	National Transmission Corporation
TPLEX	Tarlac — Pangasinan — La Union expressway
TRB	Toll Regulatory Board of the Philippines TransCo National Transmission Corporation
Universal LRT	Universal LRT Corporation (BVI) Limited
VAT	Value Added Tax
Vega	Vega Telecom, Inc.
WESM	Wholesale Electricity Spot Market
White Products	Diesel, gasoline, jet fuel, kerosene and LPG

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Audited Consolidated Financial Statements as of and for the years ended December 31, 2012, 2011 and 2010

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SAN MIGUEL CORPORATION AND SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2012, 2011 and 2010



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REPORT OF INDEPENDENT AUDITORS

The Board of Directors and Stockholders
San Miguel Corporation
No. 40 San Miguel Avenue
Mandaluyong City

We have audited the accompanying consolidated financial statements of San Miguel Corporation and Subsidiaries, which comprise the consolidated statements of financial position as at December 31, 2012 and 2011, and the consolidated statements of income, consolidated statements of comprehensive 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, 2012, and notes, comprising a summary of significant accounting policies and other explanatory information.

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, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

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 about whether the consolidated financial statements are free from material misstatement.

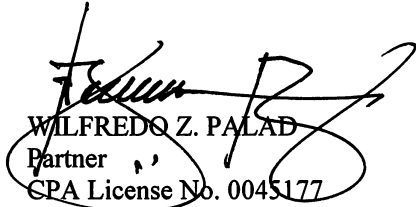
An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the consolidated 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 consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of San Miguel Corporation and Subsidiaries as at December 31, 2012 and 2011, and its consolidated financial performance and its consolidated cash flows for each of the three years in the period ended December 31, 2012, in accordance with Philippine Financial Reporting Standards.

MANABAT SANAGUSTIN & CO., CPAs



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Partner
CPA License No. 0045177

SEC Accreditation No. 0027-AR-3, Group A, valid until January 4, 2015

Tax Identification No. 106-197-186

BIR Accreditation No. 08-001987-6-2010

Issued June 30, 2010; valid until June 29, 2013

PTR No. 3669525MC

Issued January 2, 2013 at Makati City

March 21, 2013

Makati City, Metro Manila

SAN MIGUEL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
(In Millions)

	<i>Note</i>	December 31	
		2012	2011
ASSETS			
Current Assets			
Cash and cash equivalents	9, 41, 42	P 125,631	P128,975
Trade and other receivables — net	4, 10, 34, 40, 41, 42	122,599	84,472
Inventories	4, 11	80,222	65,720
Current portion of biological assets — net	18	3,792	4,124
Prepaid expenses and other current assets	4, 12, 35, 41, 42	31,612	22,620
		363,856	305,911
Assets held for sale	5, 8, 13	9,373	2,268
Total Current Assets		373,229	308,179
Noncurrent Assets			
Investments and advances — net	4, 5, 13	161,625	166,854
Available-for-sale financial assets	14, 41, 42	1,570	2,068
Property, plant and equipment — net	4, 16, 35	370,689	319,626
Investment properties — net	4, 17	3,780	2,850
Biological assets — net of current portion	4, 18	1,932	1,812
Goodwill — net	4, 5, 19, 39	49,953	30,990
Other intangible assets — net	4, 5, 19	34,131	11,407
Deferred tax assets	4, 25	8,826	8,233
Other noncurrent assets — net	4, 20, 34, 36, 40, 41, 42	32,228	38,517
		664,734	582,357
Total Noncurrent Assets		P1,037,963	P890,536
LIABILITIES AND EQUITY			
Current Liabilities			
Loans payable	21, 34, 41, 42	P 151,274	P 82,588
Accounts payable and accrued expenses	5, 13, 22, 34, 36, 41, 42	84,665	61,629
Finance lease liabilities — current portion	4, 35, 41, 42	15,456	15,388
Income and other taxes payable		11,124	9,041
Dividends payable	37	3,247	2,153
Current maturities of long-term debt — net of debt issue costs	23, 41, 42	3,279	19,453
		269,045	190,252
Liabilities directly associated with assets held for sale	8	—	578
Total Current Liabilities		269,045	190,830
Noncurrent Liabilities			
Long-term debt — net of current maturities and debt issue costs	23, 41, 42	P 220,938	P191,967
Deferred tax liabilities	25	12,084	11,257
Finance lease liabilities — net of current portion	4, 35, 41, 42	179,698	192,873
Other noncurrent liabilities	4, 5, 24, 34, 36, 41, 42	6,418	4,509
Total Noncurrent Liabilities		419,138	400,606

Forward

	<i>Note</i>	December 31	
		2012	2011
Equity	23, 26, 37, 38, 40		
Equity Attributable to Equity Holders of the Parent Company			
Capital stock — common		16,408	16,397
Capital stock — preferred		10,187	4,852
Additional paid-in capital		177,762	103,511
Revaluation increment		1,352	1,443
Cumulative translation adjustments		5,088	5,264
Retained earnings:			
Appropriated		27,219	24,315
Unappropriated		154,303	141,126
Treasury stock		(140,124)	(67,441)
		<u>252,195</u>	<u>229,467</u>
Amounts recognized directly in equity relating to assets held for sale	8	—	(53)
		<u>252,195</u>	<u>229,414</u>
Non-controlling Interests	2	<u>97,585</u>	<u>69,686</u>
Total Equity		<u>349,780</u>	<u>299,100</u>
		<u>₱1,037,963</u>	<u>₱890,536</u>

See Notes to the Consolidated Financial Statements.

SAN MIGUEL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 2012, 2011 AND 2010
(In Millions, Except Per Share Data)

	<i>Note</i>	2012	2011	2010
SALES	34	₱698,868	₱535,775	₱246,156
COST OF SALES	27	594,732	432,321	173,929
GROSS PROFIT		104,136	103,454	72,227
SELLING AND ADMINISTRATIVE EXPENSES ...	28	(51,353)	(47,500)	(37,619)
INTEREST EXPENSE AND OTHER FINANCING CHARGES	21, 23, 31, 35	(29,826)	(27,443)	(16,578)
INTEREST INCOME	32	4,254	4,618	3,023
EQUITY IN NET EARNINGS OF ASSOCIATES ...	13	2,691	2,824	6,817
GAIN ON SALE OF INVESTMENTS AND PROPERTY AND EQUIPMENT	6, 13, 14, 16, 17	4,549	1,046	529
OTHER INCOME (CHARGES) — Net	33	12,981	(12)	7,095
INCOME BEFORE INCOME TAX		47,432	36,987	35,494
INCOME TAX EXPENSE	25, 43	8,812	8,483	11,438
NET INCOME		₱ 38,620	₱ 28,504	₱ 24,056
Attributable to:				
Equity holders of the Parent Company		₱ 27,579	₱ 17,518	₱ 20,091
Non-controlling interests		11,041	10,986	3,965
		₱ 38,620	₱ 28,504	₱ 24,056
Earnings Per Common Share Attributable to Equity Holders of the Parent Company	38			
Basic		₱ 9.05	₱ 4.97	₱ 6.18
Diluted		₱ 8.99	₱ 4.94	₱ 6.14

See Notes to the Consolidated Financial Statements.

SAN MIGUEL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
FOR THE YEARS ENDED DECEMBER 31, 2012, 2011 AND 2010
(In Millions)

	<i>Note</i>	<u>2012</u>	<u>2011</u>	<u>2010</u>
NET INCOME		<u>₱38,620</u>	<u>₱28,504</u>	<u>₱24,056</u>
GAIN (LOSS) ON EXCHANGE DIFFERENCES ON				
TRANSLATION OF FOREIGN OPERATIONS		(1,785)	356	(653)
SHARE IN COMPREHENSIVE INCOME (LOSS) OF				
ASSOCIATES	13	400	645	(422)
NET GAIN (LOSS) ON AVAILABLE-FOR-SALE FINANCIAL				
ASSETS	14	(462)	(1,236)	447
INCOME TAX BENEFIT (EXPENSE)		<u>1</u>	<u>—</u>	<u>(45)</u>
OTHER COMPREHENSIVE LOSS — NET OF TAX		(1,846)	(235)	(673)
TOTAL COMPREHENSIVE INCOME — NET OF TAX		<u>₱36,774</u>	<u>₱28,269</u>	<u>₱23,383</u>
Attributable to:				
Equity holders of the Parent Company		<u>₱27,403</u>	<u>₱17,417</u>	<u>₱19,611</u>
Non-controlling interests		<u>9,371</u>	<u>10,852</u>	<u>3,772</u>
		<u>₱36,774</u>	<u>₱28,269</u>	<u>₱23,383</u>

See Notes to the Consolidated Financial Statements.

SAN MIGUEL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

FOR THE YEARS ENDED DECEMBER 31, 2012, 2011 AND 2010

(In Millions)

Equity Attributable to Equity Holders of the Parent Company													
Note	Capital Stock		Additional Paid-in Capital	Revaluation Increment	Cumulative Translation Adjustment		Retained Earnings		Treasury Stock	Total	Non-controlling Interests	Total Equity	
	Common	Preferred			Translation Reserve	Fair Value Reserve	Appropriated	Unappropriated					
As of January 1, 2012													
		P16,397	P 4,852	P103,511	P1,443	P5,662	(P451)	P24,315	P141,126	(P67,441)	P229,414	P69,686	P299,100
	Loss on exchange differences on translation of foreign operations	—	—	—	—	(103)	—	—	—	—	(103)	(1,682)	(1,785)
13	Share in comprehensive income of associates	—	—	—	—	—	400	—	—	—	400	—	400
14	Net gain (loss) on available-for-sale financial assets	—	—	—	—	—	(473)	—	—	—	(473)	12	(461)
	Other comprehensive loss	—	—	—	—	(103)	(73)	—	27,579	—	(176)	(1,670)	(1,846)
	Net income	—	—	—	—	—	—	—	—	—	27,579	11,041	38,620
	Total comprehensive income (loss)	—	—	—	—	(103)	(73)	—	27,579	—	27,403	9,371	36,774
26	Issuance of common shares	11	—	118	—	—	—	—	—	—	129	—	129
26	Issuance of Series “2” preferred shares	—	5,335	73,903	—	—	—	—	—	—	79,238	—	79,238
26	Conversion of exchangeable bonds from treasury shares	—	—	43	—	—	—	—	—	105	148	—	148
26	Redemption of Series “1” preferred shares	—	—	—	—	—	—	—	(72,788)	(72,788)	(72,788)	—	(72,788)
40	Stock options	—	—	187	—	—	—	—	—	—	187	—	187
5, 6, 13	Net addition to non-controlling interests and others	—	—	—	(91)	53	—	—	—	—	(38)	26,705	26,667
26	Appropriations — net	—	—	—	—	—	—	2,904	(2,904)	—	—	—	—
37	Cash dividends	—	—	—	—	—	—	—	—	—	—	—	—
	Common	—	—	—	—	—	—	—	(4,148)	—	(4,148)	(6,024)	(10,172)
	Preferred	—	—	—	—	—	—	—	(7,350)	—	(7,350)	(2,153)	(9,503)
26	As of December 31, 2012	P16,408	P10,187	P177,762	P1,352	P5,612	(P524)	P27,219	P154,303	(P140,124)	P252,195	P97,585	P349,780

Forward

Equity Attributable to Equity Holders of the Parent Company

<i>Note</i>	Cumulative Translation									
	Capital Stock			Additional Paid-in Capital	Revaluation Increment	Adjustment		Retained Earnings		Total
	Common	Preferred				Translation Reserve	Fair Value Reserve	Appropriated	Unappropriated	
As of January 1, 2011	<u>₱16,343</u>	<u>₱4,852</u>		<u>₱101,406</u>	<u>₱1,391</u>	<u>₱5,241</u>	<u>₱ 124</u>	<u>₱ 5,671</u>	<u>₱150,544</u>	<u>₱216,031</u>
Gain (loss) on exchange differences on translation of foreign operations	—	—		—	—	474	—	—	—	474
Share in comprehensive income of associates	—	—		—	—	—	645	—	—	645
Net loss on available-for-sale financial assets	—	—		—	—	—	(1,220)	—	—	(1,220)
Other comprehensive income (loss)	—	—		—	—	474	(575)	—	—	(101)
Net income	—	—		—	—	—	—	—	17,518	17,518
Total comprehensive income (loss)	—	—		—	—	474	(575)	—	—	—
Issuance of common shares	54	—		894	—	—	—	—	—	948
Conversion of exchangeable bonds from treasury shares	—	—		30	—	—	—	—	—	87
Reissuance of treasury shares	—	—		928	—	—	—	—	—	2,971
Stock options	—	—		253	—	—	—	—	—	253
Addition to non-controlling interests	—	—		—	52	—	—	—	—	52
Appropriations — net	—	—		—	—	—	—	18,644	(18,644)	—
Cash dividends	—	—		—	—	—	—	—	—	—
Common	—	—		—	—	—	—	—	(2,469)	(2,469)
Preferred	—	—		—	—	—	—	—	(5,823)	(5,823)
	<u>54</u>	<u>—</u>		<u>2,105</u>	<u>52</u>	<u>474</u>	<u>(575)</u>	<u>18,644</u>	<u>(9,418)</u>	<u>13,436</u>
Amounts recognized directly in equity relating to assets held for sale	—	—		—	—	(53)	—	—	—	(53)
As of December 31, 2011	<u>₱16,397</u>	<u>₱4,852</u>		<u>₱103,511</u>	<u>₱1,443</u>	<u>₱5,662</u>	<u>(₱451)</u>	<u>₱24,315</u>	<u>₱141,126</u>	<u>₱229,414</u>
										<u>₱69,686</u>
										<u>₱299,100</u>

Forward

Equity Attributable to Equity Holders of the Parent Company

Note	Capital Stock		Additional Paid-in Capital	Revaluation Increment	Cumulative Translation Adjustment			Retained Earnings		Treasury Stock	Total	Non-controlling Interests	Total Equity
	Common	Preferred			Translation Reserve	Fair Value Reserve	Appropriated	Unappropriated					
As of January 1, 2010	₱16,150	₱4,852	₱99,085	₱18	₱5,737	₱108	₱5,497	₱151,911	(₱69,541)	₱213,817	₱27,121	₱240,938	
Loss on exchange differences on translation of foreign operations	—	—	—	—	(496)	—	—	—	—	(496)	(157)	(653)	
Share in comprehensive loss of associates	—	—	—	—	—	(422)	—	—	—	(422)	—	(422)	
Net gain (loss) on available-for-sale financial assets, net of tax	—	—	—	—	—	438	—	—	—	438	(36)	402	
Other comprehensive income (loss)	—	—	—	—	(496)	16	—	—	—	(480)	(193)	(673)	
Net income	—	—	—	—	—	—	—	20,091	—	20,091	3,965	24,056	
Total comprehensive income (loss)	—	—	—	—	(496)	16	—	20,091	—	19,611	3,772	23,383	
Issuance of common shares	193	—	2,121	—	—	—	—	—	—	2,314	—	2,314	
Stock options	—	—	200	—	—	—	—	—	—	200	—	200	
Net addition to non-controlling interests	—	—	—	(23)	—	—	—	—	—	(23)	24,877	24,854	
Appropriations — net	—	—	—	—	—	—	174	(174)	—	—	—	—	
Cash dividends	—	—	—	—	—	—	—	(15,584)	—	(15,584)	(4,976)	(20,560)	
Common Preferred	—	—	—	—	—	—	—	(5,700)	—	(5,700)	—	(5,700)	
Acquisition of subsidiary and others	—	—	—	1,396	—	—	—	—	—	1,396	—	1,396	
As of December 31, 2010	₱16,343	₱4,852	₱101,406	₱1,391	₱5,241	₱124	₱5,671	₱150,544	(₱69,541)	₱216,031	₱50,794	₱266,825	

SAN MIGUEL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2012, 2011 AND 2010
(In Millions)

	<i>Note</i>	2012	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES				
Income before income tax		₱ 47,432	₱ 36,987	₱ 35,494
Adjustments for:				
Depreciation, amortization and others — net	7, 29	5,169	19,305	9,457
Interest expense and other financing charges	31	29,826	27,443	16,578
Interest income	32	(4,254)	(4,618)	(3,023)
Equity in net earnings of associates	13	(2,691)	(2,824)	(6,817)
Gain on sale of investments and property and equipment	33	(4,549)	(1,046)	(5,019)
Operating income before working capital changes		70,933	75,247	46,670
Changes in noncash current assets, certain current liabilities and others	39	(27,939)	(19,335)	13,175
Cash generated from operations		42,994	55,912	59,845
Interest paid		(16,987)	(14,434)	(5,155)
Income taxes paid		(9,192)	(12,818)	(9,312)
Net cash flows provided by operating activities		16,815	28,660	45,378
CASH FLOWS FROM INVESTING ACTIVITIES				
Acquisition of subsidiaries, net of cash and cash equivalents acquired	39	(19,729)	(775)	(18,978)
Additions to investments and advances	13	(23,159)	(16,338)	(99,762)
Additions to property, plant and equipment	7, 16	(52,920)	(26,426)	(8,518)
Payment of other liabilities	13	(2,122)	(24,485)	—
Decrease (increase) in other noncurrent assets and others		7,917	(6,356)	(4,586)
Proceeds from sale of investments and property and equipment	6, 8, 13, 16, 17	24,568	1,347	1,175
Interest received		2,466	3,455	3,674
Dividends received from associates	13	4,949	2,637	—
Net cash flows used in investing activities		(58,030)	(66,941)	(126,995)
CASH FLOWS FROM FINANCING ACTIVITIES				
Proceeds from:				
Short-term borrowings		₱ 752,957	₱ 492,117	₱ 685,768
Long-term borrowings		59,671	55,399	72,937
Payments of:				
Short-term borrowings		(699,213)	(483,672)	(703,376)
Long-term borrowings		(59,667)	(14,025)	(29,196)
Proceeds from issuance of Series “2” preferred shares	26	79,238	—	—
Redemption of Series “1” preferred shares	26	(72,788)	—	—
Payment of finance lease liabilities		(17,393)	(11,781)	(4,798)
Cash dividends paid	37	(10,609)	(6,801)	(21,118)
Proceeds from issuance of capital stock	26	129	948	2,314
Proceeds from reissuance of treasury stock	26	—	2,971	—
Dividends paid to non-controlling shareholders		(7,969)	(7,650)	(4,883)
Increase in non-controlling interests		—	—	126
Net proceeds from issuance of preferred shares of subsidiaries	6	14,216	14,829	—
Net cash flows provided by (used in) financing activities		38,572	42,335	(2,226)

Forward

	<i>Note</i>	2012	2011	2010
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS		(701)	(181)	(380)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS		(3,344)	3,873	(84,223)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR		128,975	125,188	209,411
CASH AND CASH EQUIVALENTS ASSOCIATED TO ASSETS HELD FOR SALE	8	—	(86)	—
CASH AND CASH EQUIVALENTS AT END OF YEAR	9	<u>₱125,631</u>	<u>₱128,975</u>	<u>₱125,188</u>

See Notes to the Consolidated Financial Statements.

SAN MIGUEL CORPORATION AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Amounts in Millions, Except Per Share Data and Number of Shares)

1. Reporting Entity

San Miguel Corporation (SMC or the Parent Company) was incorporated in the Philippines. The accompanying consolidated financial statements comprise the financial statements of the Parent Company and its Subsidiaries (collectively referred to as the “Group”) and the Group’s interests in associates and jointly controlled entities. The Parent Company is a public company under Section 17.2 of the Securities Regulation Code and its shares are listed on the Philippine Stock Exchange (PSE). The Group is primarily engaged in the production, processing and marketing of beverage, food and packaging products, power generation and distribution, mining, fuel and oil, infrastructure, telecommunications, and management and development of real estate properties.

The registered office address of the Parent Company is No. 40 San Miguel Avenue, Mandaluyong City.

2. Basis of Preparation

Statement of Compliance

The consolidated financial statements have been prepared in compliance with Philippine Financial Reporting Standards (PFRS). PFRS are based on International Financial Reporting Standards (IFRS) issued by International Accounting Standards Board (IASB). PFRS include statements named PFRS, Philippine Accounting Standards (PAS) and Philippine Interpretations from International Financial Reporting Interpretations Committee (IFRIC), issued by the Financial Reporting Standards Council (FRSC).

The accompanying consolidated financial statements were authorized for issue by the Board of Directors (BOD) on March 21, 2013.

Basis of Measurement

The consolidated financial statements of the Group have been prepared on a historical cost basis of accounting, except for the following:

- derivative financial instruments, financial assets at fair value through profit or loss (FVPL) and available-for-sale (AFS) financial assets are measured at fair value;
- defined benefit asset (liability) is measured as the net total of the fair value of the plan assets, less unrecognized actuarial gains (losses) and the present value of the defined benefit obligation; and
- agricultural produce are measured at fair value less estimated costs to sell at the point of harvest.

Functional and Presentation Currency

The consolidated financial statements are presented in Philippine peso, which is the Parent Company’s functional currency. All financial information are rounded off to the nearest million (₱000,000), except when otherwise indicated.

Basis of Consolidation

The consolidated financial statements include the accounts of the Parent Company and its subsidiaries. The major subsidiaries include the following:

	Percentage of Ownership		Country of Incorporation
	2012	2011	
Beverage Business:			
San Miguel Brewery Inc. (SMB) and subsidiaries [including Iconic Beverages, Inc., Brewery Properties Inc. (BPI) and subsidiary, San Miguel Brewing International Ltd. (SMBIL) and subsidiaries {including San Miguel Brewery Hong Kong Limited (SMBHK) and subsidiaries, PT Delta Djakarta Tbk ^(a) and a subsidiary, San Miguel (Baoding) Brewery Company. Limited ^(a) , San Miguel Brewery Vietnam Ltd. ^(a) , San Miguel Beer (Thailand) Ltd. (SMBTL) and San Miguel Marketing (Thailand) Ltd.}]	51.00	51.00	Philippines

Forward

SAN MIGUEL CORPORATION AND SUBSIDIARIES
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	Percentage of Ownership		Country of Incorporation
	2012	2011	
Ginebra San Miguel, Inc. (GSMI) and subsidiaries [including Distileria Bago, Inc., East Pacific Star Bottlers Phils Inc. (EPSBPI) ^(b) , Ginebra San Miguel International, Ltd. (GSMIL), Ginebra San Miguel International Holdings Ltd. (GSMIHL), Global Beverage Holdings Ltd. (GBHL) and Siam Holdings Ltd. (SHL)]	77.36	77.63	Philippines
San Miguel Foods and Beverage International Limited (SMFBIL) and subsidiaries [including PT San Miguel Indonesia Foods & Beverages (PTSMIFB) ^(a) , San Miguel (Thailand) Co. Ltd. (SMTCL) ^(c) , San Miguel (Guangdong) Foods & Beverages Co. Ltd. ^(a) , San Miguel (Vietnam) Co. Ltd. (SMVCL) ^(d) , PT San Miguel Marketing Indonesia ^(a) , and San Miguel (Malaysia) Sdn. Bhd.]	100.00	100.00	British Virgin Islands (BVI)
Food Business:			
San Miguel Pure Foods Company, Inc. (SMPFC) and subsidiaries [including San Miguel Foods, Inc. (SMFI), San Miguel Mills, Inc. (SMMI) and subsidiaries (including Golden Avenue Corp. (GAC) ^(e) and Golden Bay Grain Terminal Corporation (GBGTC) ^(f)), The Purefoods-Hormel Company, Inc., Magnolia, Inc. (Magnolia) and subsidiaries including Golden Food and Dairy Creamery Corporation (GFDCC) ^(g) , San Miguel Super Coffeemix Co., Inc., PT San Miguel Pure Foods Indonesia and San Miguel Pure Foods International, Limited (SMPFIL) and subsidiary, San Miguel Pure Foods Investment (BVI) Limited (SMPFI) and subsidiary, San Miguel Hormel (Vn) Co. Ltd. ^(h)]	84.92	99.92	Philippines
Packaging Business:			
San Miguel Yamamura Packaging Corporation (SMYPC) and subsidiaries, SMC Yamamura Fuso Molds Corporation and Can Asia, Inc. (CAI) ⁽ⁱ⁾ . . .	65.00	65.00	Philippines
San Miguel Yamamura Packaging International Limited (SMYPIL) and subsidiaries [including San Miguel Phu Tho Packaging Co. Ltd. ^(a) , Zhaoqing San Miguel Yamamura Glass Co., Ltd., Foshan San Miguel Packaging Co. Ltd., PT San Miguel Yamamura Utama Indoplas (SMYUI) ^(j) , San Miguel Yamamura Packaging & Printing Sdn. Bhd., San Miguel Yamamura Woven Products Sdn. Bhd., Packaging Research Centre Sdn. Bhd., San Miguel Yamamura Plastic Films Sdn. Bhd. and San Miguel Yamamura Knox Pty. Ltd. (SMYK) ^(a) and subsidiaries]	65.00	65.00	BVI
Mindanao Corrugated Fibreboard, Inc. ^(a)	100.00	100.00	Philippines
San Miguel Yamamura Asia Corporation (SMYAC)	60.00	60.00	Philippines
Power Generation and Distribution Business:			
SMC Global Power Holdings Corp. (SMC Global) and subsidiaries [including San Miguel Energy Corporation (SMEC) and subsidiaries, South Premiere Power Corp. (SPPC), Strategic Power Devt. Corp. (SPDC), San Miguel Electric Corp. (SMELCO) and PanAsia Energy Holdings, Inc. (PanAsia) ^(k)]	100.00	100.00	Philippines
Mining Business:			
Clariden Holdings, Inc. (Clariden) and subsidiaries [including V.I.L. Mines, Incorporated and Asia-Alliance Mining Resources Corp. (AAMRC) ^(l)]	100.00	100.00	Philippines

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	Percentage of Ownership		Country of Incorporation
	2012	2011	
Fuel and Oil Business:			
SEA Refinery Corporation (SRC) and subsidiary, Petron Corporation (Petron) and subsidiaries [including Petron Marketing Corporation (PMC), Petron Freeport Corporation, Petrogen Insurance Corporation (Petrogen), Overseas Ventures Insurance Corporation (OVINCOR) ^(a) , Petron Singapore Trading Pte. Ltd., New Ventures Realty Corporation (NVRC) and subsidiaries, Petron Global Limited (BVI) (PGL), Petron Oil & Gas International Sdn. Bhd. (POGI) including Petron Fuel International Sdn Bhd, Petron Oil (M) Sdn Bhd and Petron Malaysia Refining & Marketing Bhd. (collectively Petron Malaysia) ^(a, m) , Petron Finance (Labuan) Limited and Limay Energen Corp. (LEC)]	100.00	100.00	Philippines
Infrastructure Business:			
San Miguel Holdings Corp. (SMHC) and subsidiaries [including Rapid Thoroughfares Inc. (Rapid), Trans Aire Development Holdings Corp. (TADHC) ^(a) , Universal LRT Corporation (BVI) Limited (ULC BVI) ^(a) , Terramino Holdings, Inc. (THI) and subsidiary ^(a, n) , Citra Metro Manila Tollways Corporation (CMMTC) ^(a, o) and Alloy Manila Toll Expressways Inc. (AMTEX) ^(a, p)]	100.00	100.00	Philippines
Telecommunications Business:			
Vega Telecom, Inc. (Vega) and subsidiaries [including Two Cassandra-CCI Conglomerates, Inc. (TCCI) ^(a) , Perchpoint Holdings Corp. (PHC) ^(a) and Power Smart Capital Limited (PSCL) ^(a) [collectively own Bell Telecommunication Philippines, Inc. (BellTel) ^(a)] and A.G.N. Philippines, Inc. (AGNP)]	100.00	100.00	Philippines
Eastern Telecommunications Philippines, Inc. (ETPI) and subsidiary ^(q) , Telecommunications Technologies Phils., Inc. (TTPI)	77.70	77.70	Philippines
Real Estate Business:			
San Miguel Properties, Inc. (SMPI) and subsidiaries [including Excel Unified Land Resources Corporation, First HQ Ayala Business Centers, Inc., SMPI Makati Flagship Realty Corp. (SMPI Flagship) ^(r) , SMC Originals, Inc. (SMC Originals) ^(s) and Integrated Geosolutions, Inc. (IGI) ^(a)]	99.68	99.68	Philippines
Others:			
SMC Stock Transfer Service Corporation	100.00	100.00	Philippines
ArchEn Technologies Inc.	100.00	100.00	Philippines
SMITS, Inc. ^(a) and subsidiary	100.00	100.00	Philippines
Anchor Insurance Brokerage Corporation (AIBC)	58.33	58.33	Philippines
SMC Shipping and Lighterage Corporation (SMCSLC) and subsidiaries [including MG8 Terminal Inc. (MG8) ^(t) , SMC Cebu Shipyard Land, Inc. (SMCCSLI) ^(u) and Mactan Shipyard Corporation (MSC) ^(v)]	70.00	70.00	Philippines
Challenger Aero Air Corp.	100.00	100.00	Philippines
Pacific Central Properties, Inc. (PCPI)	100.00	100.00	Philippines
San Miguel Equity Securities Inc. (SMESI) ^(w)	100.00	100.00	Philippines
San Miguel Equity Investments Inc. (SMEII) ^(x)	100.00	100.00	Philippines

(a) The financial statements of these subsidiaries were audited by other auditors.

(b) Consolidated to GSMI effective January 27, 2012 (Note 5).

(c) Sold on February 15, 2012 (Note 8).

(d) The State Securities Commission of Vietnam issued on May 31, 2012 an order of dissolution of SMVCL.

(e) Consolidated to SMMI effective June 2012. Formerly Cobertson Realty Corporation (CRC) (Note 5).

(f) Incorporated on November 8, 2011 (Note 5).

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- (g) Consolidated to Magnolia effective September 12, 2011 (Note 5).
- (h) Formerly San Miguel Pure Foods (Vn) Co. Ltd. (SMPFVN)(Note 6).
- (i) Incorporated on November 12, 2012 (Note 6).
- (j) Sold in January 2012 (Note 8).
- (k) Sold on August 26, 2011 (Note 5).
- (l) Consolidated to Clariden effective September 6, 2012 (Note 5).
- (m) Consolidated to Petron effective March 30, 2012 (Note 5).
- (n) Consolidated effective December 28, 2012 (Note 5).
- (o) Consolidated effective December 28, 2012. 37.33% owned by THI and 23.50% owned through Atlantic Aurum Investments BV (Atlantic) in 2012 (Note 5).
- (p) Consolidated to SMHC effective February 2012 (Note 5).
- (q) Consolidated effective October 20, 2011. 40% owned by AGNP in 2011 and 37.7% owned by SMESI in 2011 (Note 6).
- (r) Formerly SMPI-Government Service Insurance System Joint Venture Corporation (SMPI-GSIS JVC)(Note 6).
- (s) Formerly Highriser Group, Inc. (Note 6).
- (t) Incorporated on March 16, 2011 (Note 6).
- (u) Formerly Keppel Cebu Shipyard Land, Inc. (KCSLI). Consolidated to SMCSLC effective May 26, 2011 (Note 5).
- (v) Incorporated on August 18, 2011 (Note 6).
- (w) Incorporated on March 28, 2011 (Note 6).
- (x) Incorporated on March 23, 2011 (Note 6).

A subsidiary is an entity controlled by the Group. Control exists when the Group has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefit from its activities. In assessing control, potential voting rights that are presently exercisable or convertible are taken into account. The financial statements of the subsidiaries are included in the consolidated financial statements from the date when the Group obtains control, and continue to be consolidated until the date when such control ceases.

The consolidated financial statements are prepared for the same reporting period as the Parent Company, using uniform accounting policies for like transactions and other events in similar circumstances. Intergroup balances and transactions, including intergroup unrealized profits and losses, are eliminated in preparing the consolidated financial statements.

Non-controlling interests represent the portion of profit or loss and net assets not held by the Group and are presented in the consolidated statements of income, consolidated statements of comprehensive income and within equity in the consolidated statements of financial position, separately from the Group's equity attributable to equity holders of the Parent Company.

Non-controlling interests include the interests not held by the Group in SMB, GSMI, SMPFC, SMYPC, SMYPIL, SMYAC, SMPI, ETPI, AIBC, SMCSLC, Petron, TADHC, ULC BVI and IGI in 2012 and 2011 and AAMRC, CMMTC and AMTEX in 2012.

3. Significant Accounting Policies

The accounting policies set out below have been applied consistently to all periods presented in the consolidated financial statements, except for the changes in accounting policies as explained below.

Adoption of Amendments to Standards

The FRSC approved the adoption of a number of amendments to standards as part of PFRS.

Effective 2012, the Group has adopted the amendments to PFRS 7, *Disclosures — Transfers of Financial Assets*, which require additional disclosures about transfers of financial assets. The amendments require disclosure of information that enables users of the consolidated financial statements to understand the relationship between transferred financial assets that are not derecognized in their entirety and the associated liabilities; and to evaluate the nature of, and risks associated with, the entity's continuing involvement in the derecognized financial assets. The amendments are effective for annual periods beginning on or after July 1, 2011. The adoption of these amendments did not have an effect on the consolidated financial statements.

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Additional disclosures were included in the consolidated financial statements, where applicable.

New or Revised Standards, Amendments to Standards and Interpretations Not Yet Adopted

A number of new or revised standards, amendments to standards and interpretations are effective for annual periods beginning after January 1, 2012, and have not been applied in preparing the consolidated financial statements. Except as otherwise indicated, none of these is expected to have a significant effect on the consolidated financial statements of the Group. The Group does not plan to adopt these standards early.

The Group will adopt the following new or revised standards, amendments to standards and interpretations on the respective effective dates:

- Presentation of Items of Other Comprehensive Income (*Amendments to PAS 1, Presentation of Financial Statements*). The amendments: (a) require that an entity presents separately the items of other comprehensive income that would be reclassified to profit or loss in the future, if certain conditions are met, from those that would never be reclassified to profit or loss; (b) do not change the existing option to present profit or loss and other comprehensive income in two statements; and (c) change the title of the consolidated statement of comprehensive income to consolidated statement of profit or loss and other comprehensive income. However, an entity is still allowed to use other titles. The amendments do not address which items are presented in other comprehensive income or which items need to be reclassified. The requirements of other PFRS continue to apply in this regard. The adoption of the amendments is required for annual periods beginning on or after January 1, 2013. The adoption of the amendments is not expected to have an effect on the consolidated financial statements.
- Disclosures: Offsetting Financial Assets and Financial Liabilities (*Amendments to PFRS 7*). These amendments include minimum disclosure requirements related to financial assets and financial liabilities that are: (a) offset in the consolidated statements of financial position; or (b) subject to enforceable master netting arrangements or similar agreements. They include a tabular reconciliation of gross and net amounts of financial assets and financial liabilities, separately showing amounts offset and not offset in the consolidated statements of financial position. The adoption of the amendments is required to be retrospectively applied for annual periods beginning on or after January 1, 2013. The adoption of the amendments is not expected to have an effect on the consolidated financial statements.
- PFRS 10, *Consolidated Financial Statements*, introduces a new approach to determining which investees should be consolidated and provides a single model to be applied in the control analysis for all investees. An investor controls an investee when: (a) it is exposed or has rights to variable returns from its involvement with that investee; (b) it has the ability to affect those returns through its power over that investee; and (c) there is a link between power and returns. Control is reassessed as facts and circumstances change. PFRS 10 supersedes PAS 27 (2008), *Consolidated and Separate Financial Statements*, and Philippine Interpretation Standards Interpretation Committee (SIC) 12, *Consolidation — Special Purpose Entities*. The adoption of the new standard is required for annual periods beginning on or after January 1, 2013.

The adoption of the new standard may result to changes in consolidation conclusion in respect of the Group's investees and may lead to changes in the current accounting for these investees.

- PFRS 11, *Joint Arrangements*, focuses on the rights and obligations of joint arrangements, rather than the legal form (as is currently the case). The new standard: (a) distinguishes joint arrangements between joint operations and joint ventures; and (b) eliminates the option of using the equity method or proportionate consolidation for jointly controlled entities that are now called joint ventures as it always requires the use of equity method. PFRS 11 supersedes PAS 31, *Interests in Joint Ventures*, and Philippine Interpretation SIC 13, *Jointly Controlled Entities — Non-monetary Contributions by Venturers*. The adoption of the new standard is required for annual periods beginning on or after January 1, 2013.

The effect of the adoption of the new standard will result to the elimination of the option to use proportionate consolidation, which is the current practice of the Group.

- PFRS 12, *Disclosure of Interests in Other Entities*, contains the disclosure requirements for entities that have interests in subsidiaries, joint arrangements (i.e., joint operations or joint ventures), associates and/or unconsolidated structured entities. The new standard provides information that enables users to evaluate: (a) the nature of, and risks associated with, an entity's interests in other entities; and (b) the effects of those

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interests on the entity's financial position, financial performance and cash flows. The adoption of the new standard is required for annual periods beginning on or after January 1, 2013.

The Group is currently assessing the disclosure requirements for interests in subsidiaries, joint arrangements, associates and unconsolidated structured entities in comparison with the existing disclosure.

- Consolidated Financial Statements, Joint Arrangements and Disclosure of Interests in Other Entities: Transition Guidance (*Amendments to PFRS 10, PFRS 11, and PFRS 12*). The amendments: (a) simplify the process of adopting PFRS 10 and 11, and provide relief from the disclosures in respect of unconsolidated structured entities; (b) simplify the transition and provide additional relief from the disclosures that could have been onerous depending on the extent of comparative information provided in the consolidated financial statements; and (c) limit the restatement of comparatives to the immediately preceding period; this applies to the full suite of standards. Entities that provide comparatives for more than one period have the option of leaving additional comparative periods unchanged. In addition, the date of the initial application is now defined in PFRS 10 as the beginning of the annual reporting period in which the standard is applied for the first time. The adoption of the amendments is required for annual periods beginning on or after January 1, 2013.

The Group is currently assessing whether there is a change in the consolidation conclusion for its investees.

- PFRS 13, *Fair Value Measurement*, replaces the fair value measurement guidance contained in individual PFRS with a single source of fair value measurement guidance. It defines fair value, establishes a framework for measuring fair value and sets out disclosure requirements for fair value measurements. It explains how to measure fair value when it is required or permitted by other PFRS. It does not introduce new requirements to measure assets or liabilities at fair value nor does it eliminate the practicability exceptions to fair value measurements that currently exist in certain standards. The adoption of the new standard is required for annual periods beginning on or after January 1, 2013. The adoption of the new standard is not expected to significantly change the Group's methodologies in determining fair values.
- PAS 19, *Employee Benefits* (Amended 2011), includes the following requirements: (a) actuarial gains and losses are recognized immediately in other comprehensive income; this change will remove the corridor method and eliminate the ability of entities to recognize all changes in the defined benefit obligation and in plan assets in profit or loss, which is currently allowed under PAS 19; and (b) expected return on plan assets recognized in profit or loss is calculated based on the rate used to discount the defined benefit obligation. The adoption of the amendments is required to be retrospectively applied for annual periods beginning on or after January 1, 2013.

The effect on the Group's consolidated financial statements of the retrospective application of the amendments to PAS 19 beginning January 1, 2013 is estimated to increase retirement assets and retirement liabilities by ₱3,048 and ₱5,536, respectively, decrease other comprehensive income by ₱1,028 and a corresponding decrease to the opening balance of retained earnings amounting to ₱714.

- PAS 28, *Investments in Associates and Joint Ventures* (2011), supersedes PAS 28 (2008). PAS 28 (2011) makes the following amendments: (a) PFRS 5, *Noncurrent Assets Held for Sale and Discontinued Operations*, applies to an investment, or a portion of an investment, in an associate or a joint venture that meets the criteria to be classified as held for sale; and (b) on cessation of significant influence or joint control, even if an investment in an associate becomes an investment in a joint venture or *vice versa*, the entity does not remeasure the retained interest. The adoption of the amendments is required for annual periods beginning on or after January 1, 2013. The adoption of the amendments is not expected to have an effect on the consolidated financial statements.
- *Improvements to PFRS 2009-2011* contain amendments to 5 standards with consequential amendments to other standards and interpretations, of which, the adoption is not expected to have an effect on the consolidated financial statements.
- Comparative Information beyond Minimum Requirements (*Amendments to PAS 1*). These amendments clarify the requirements for comparative information that are disclosed voluntarily and those that are mandatory due to retrospective application of an accounting policy, or retrospective restatement or reclassification of items in the consolidated financial statements. An entity must include comparative information in the related notes to the consolidated financial statements when it voluntarily provides comparative information beyond the minimum required comparative period. The additional comparative

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period does not need to contain a complete set of consolidated financial statements. On the other hand, supporting notes for the third balance sheet (mandatory when there is a retrospective application of an accounting policy, or retrospective restatement or reclassification of items in the consolidated financial statements) are not required. The adoption of the amendments is required for annual periods beginning on or after January 1, 2013.

- **Presentation of the Opening Statement of Financial Position and Related Notes (*Amendments to PAS 1*).** The amendments clarify that: (a) the opening consolidated statement of financial position is required only if there is: (i) a change in accounting policy; (ii) a retrospective restatement; or (iii) a reclassification which has a material effect upon the information in that consolidated statement of financial position; (b) except for the disclosures required under PAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*, notes related to the opening consolidated statement of financial position are no longer required; and (c) the appropriate date for the opening consolidated statement of financial position is the beginning of the preceding period, rather than the beginning of the earliest comparative period presented. This is regardless of whether an entity provides additional comparative information beyond the minimum comparative information requirements. The amendments explain that the requirements for the presentation of notes related to additional comparative information and those related to the opening consolidated statement of financial position are different, because the underlying objectives are different. Consequential amendments have been made to PAS 34, *Interim Financial Reporting*. The adoption of the amendments is required for annual periods beginning on or after January 1, 2013.
- **Classification of Servicing Equipment (*Amendments to PAS 16, Property, Plant and Equipment*).** The amendments clarify the accounting of spare parts, stand-by equipment and servicing equipment. The definition of 'property, plant and equipment' in PAS 16 is now considered in determining whether these items should be accounted for under this standard. If these items do not meet the definition, then they are accounted for using PAS 2, *Inventories*. The adoption of the amendments is required for annual periods beginning on or after January 1, 2013.
- **Income Tax Consequences of Distributions (*Amendments to PAS 32, Financial Instruments Presentation*).** The amendments clarify that PAS 12, *Income Taxes* applies to the accounting for income taxes relating to: (a) distributions to holders of an equity instrument; and (b) transaction costs of an equity transaction. This amendment removes a perceived inconsistency between PAS 32 and PAS 12. Before the amendment, PAS 32 indicated that distributions to holders of an equity instrument are recognized directly in equity, net of any related income tax. However, PAS 12 generally requires the tax consequences of dividends to be recognized in profit or loss. A similar consequential amendment has also been made to Philippine Interpretation IFRIC 2, *Members' Share in Co-operative Entities and Similar Instruments*. The adoption of the amendments is required for annual periods beginning on or after January 1, 2013.
- **Segment Assets and Liabilities (*Amendments to PAS 34*).** This is amended to align the disclosure requirements for segment assets and segment liabilities in interim consolidated financial statements with those in PFRS 8, *Operating Segments*. PAS 34 now requires the disclosure of a measure of total assets and liabilities for a particular reportable segment. In addition, such disclosure is only required when: (a) the amount is regularly provided to the chief operating decision maker; and (b) there has been a material change from the amount disclosed in the last annual consolidated financial statements for that reportable segment. The adoption of the amendments is required for annual periods beginning on or after January 1, 2013.
- **Offsetting Financial Assets and Financial Liabilities (*Amendments to PAS 32*).** The amendments clarify that: (a) an entity currently has a legally enforceable right to set-off if that right is: (i) not contingent on a future event; and (ii) enforceable both in the normal course of business and in the event of default, insolvency or bankruptcy of the entity and all counterparties; and (b) gross settlement is equivalent to net settlement if and only if the gross settlement mechanism has features that: (i) eliminate or result in insignificant credit and liquidity risk; and (ii) process receivables and payables in a single settlement process or cycle. The adoption of the amendments is required to be retrospectively applied for annual periods beginning on or after January 1, 2014. The adoption of the amendments is not expected to have an effect on the consolidated financial statements.
- **PFRS 9, *Financial Instruments* (2010) and (2009).** PFRS 9 (2009) introduces new requirements for the classification and measurement of financial assets. Under PFRS 9 (2009), financial assets are classified and measured based on the business model in which they are held and the characteristics of their contractual cash

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flows. PFRS 9 (2010) introduces additions relating to financial liabilities. The IASB currently has an active project to make limited amendments to the classification and measurement requirements of PFRS 9 and add new requirements to address the impairment of financial assets and hedge accounting. PFRS 9 (2010 and 2009) is effective for annual periods beginning on or after January 1, 2015.

The Group is still evaluating the possible financial impact of the adoption of PFRS 9 and does not plan to adopt this standard early.

- Philippine Interpretation IFRIC 15, *Agreements for the Construction of Real Estate*, applies to the accounting for revenue and associated expenses by entities that undertake the construction of real estate directly or through subcontractors. It provides guidance on the recognition of revenue among real estate developers for sales of units, such as apartments or houses, 'off plan'; i.e., before construction is completed. It also provides guidance on how to determine whether an agreement for the construction of real estate is within the scope of PAS 11, *Construction Contracts*, or PAS 18, *Revenue*, and the timing of revenue recognition. The Philippine Securities and Exchange Commission (SEC) issued a notice dated August 5, 2011 that defers the adoption of this interpretation indefinitely.

Financial Assets and Financial Liabilities

Date of Recognition. The Group recognizes a financial asset or a financial liability in the consolidated statements of financial position when it becomes a party to the contractual provisions of the instrument. In the case of a regular way purchase or sale of financial assets, recognition is done using settlement date accounting.

Initial Recognition of Financial Instruments. Financial instruments are recognized initially at fair value of the consideration given (in case of an asset) or received (in case of a liability). The initial measurement of financial instruments, except for those designated as at FVPL, includes transaction costs.

The Group classifies its financial assets in the following categories: held-to-maturity (HTM) investments, AFS financial assets, financial assets at FVPL and loans and receivables. The Group classifies its financial liabilities as either financial liabilities at FVPL or other financial liabilities. The classification depends on the purpose for which the investments are acquired and whether they are quoted in an active market. Management determines the classification of its financial assets and financial liabilities at initial recognition and, where allowed and appropriate, re-evaluates such designation at every reporting date.

Determination of Fair Value. The fair value for financial instruments traded in active markets at the reporting 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 ask prices are not available, the price of the most recent transaction provides evidence of the current fair value as long as there is no 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 techniques. Valuation techniques include the discounted cash flow method, 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 the fair value (a 'Day 1' profit) in profit or loss unless it qualifies for recognition as some other type of asset. In cases where data used is not observable, the difference between the transaction price and model value is only recognized in profit or loss 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

Financial Assets at FVPL. A financial asset is classified as at FVPL if it is classified as held for trading or is designated as such upon initial recognition. Financial assets are designated as at FVPL if the Group manages such investments and makes purchase and sale decisions based on their fair value in accordance with the Group's documented risk management or investment strategy. Derivative instruments (including embedded derivatives), except those covered by hedge accounting relationships, are classified under this category.

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Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term.

Financial assets may be designated by management at initial recognition at FVPL, when any of the following criteria is met:

- the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or recognizing gains or losses on a different basis;
- the assets are part of a group of financial assets which are managed and their performances are evaluated on a fair value basis, in accordance with a documented risk management or investment strategy; or
- the financial instrument contains an embedded derivative, unless the embedded derivative does not significantly modify the cash flows or it is clear, with little or no analysis, that it would not be separately recognized.

The Group carries financial assets at FVPL using their fair values. Attributable transaction costs are recognized in profit or loss as incurred. Fair value changes and realized gains or losses are recognized in profit or loss. Fair value changes from derivatives accounted for as part of an effective accounting hedge are recognized in other comprehensive income and presented in the consolidated statements of changes in equity. Any interest earned shall be recognized as part of "Interest income" account in the consolidated statements of income. Any dividend income from equity securities classified as at FVPL shall be recognized in profit or loss when the right to receive payment has been established.

The Group's derivative assets and financial assets at FVPL are classified under this category (Note 12).

The combined carrying amounts of financial assets under this category amounted to ₱238 and ₱315 as of December 31, 2012 and 2011, respectively (Note 42).

Loans and Receivables. Loans and receivables are non-derivative financial assets with fixed or determinable payments and maturities 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 financial assets or financial assets at FVPL.

Subsequent to initial measurement, loans and receivables are carried at amortized cost using the effective interest rate method, less any impairment in value. Any interest earned on loans and receivables shall be recognized as part of "Interest income" in the consolidated statements of income on an accrual basis. 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 periodic amortization is also included as part of "Interest income" account in the consolidated statements of income. Gains or losses are recognized in profit or loss when loans and receivables are derecognized or impaired, as well as through the amortization process.

Cash includes cash on hand and in banks which are stated at face value. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value.

The Group's cash and cash equivalents, trade and other receivables, option deposit and noncurrent receivables and deposits are included in this category (Notes 9, 10, 12 and 20).

The combined carrying amounts of financial assets under this category amounted to ₱264,096 and ₱240,918 as of December 31, 2012 and 2011, respectively (Note 42).

HTM Investments. HTM investments are quoted non-derivative financial assets with fixed or determinable payments and fixed maturities for which the Group's management has the positive intention and ability to hold to maturity. Where the Group sells other than an insignificant amount of HTM investments, the entire category would be tainted and reclassified as AFS financial assets. After initial measurement, these investments are measured at amortized cost using the effective interest rate method, less impairment in value. Any interest earned on the HTM investments shall be recognized as part of "Interest income" account in the consolidated statements of income on an accrual basis. 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 periodic amortization is also included as part of "Interest income" account in the consolidated statements of income. Gains or losses are recognized in profit or loss when the HTM investments are derecognized or impaired, as well as through the amortization process.

The Group has no investments accounted for under this category as of December 31, 2012 and 2011.

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AFS Financial Assets. AFS financial assets are non-derivative financial assets that are either designated in this category or not classified in any of the other financial asset categories. Subsequent to initial recognition, AFS financial assets are measured at fair value and changes therein, other than impairment losses and foreign currency differences on AFS debt instruments, are recognized in other comprehensive income and presented in the “Fair value reserve” account in the consolidated statements of changes in equity. The effective yield component of AFS debt securities is reported as part of “Interest income” account in the consolidated statements of income. Dividends earned on holding AFS equity securities are recognized as dividend income when the right to receive payment has been established. When individual AFS financial assets are either derecognized or impaired, the related accumulated unrealized gains or losses previously reported in equity are transferred to and recognized in profit or loss.

AFS financial assets also include unquoted equity instruments with fair values which cannot be reliably determined. These instruments are carried at cost less impairment in value, if any.

The Group’s investments in equity and debt securities are classified under this category (Notes 12 and 14).

The carrying amounts of financial assets under this category amounted to ₱1,621 and ₱2,068 as of December 31, 2012 and 2011, respectively (Note 42).

Financial Liabilities

Financial Liabilities at FVPL. Financial liabilities are classified under this category through the fair value option. Derivative instruments (including embedded derivatives) with negative fair values, except those covered by hedge accounting relationships, are also classified under this category.

The Group carries financial liabilities at FVPL using their fair values and reports fair value changes in profit or loss. Fair value changes from derivatives accounted for as part of an effective accounting hedge are recognized in other comprehensive income and presented in the consolidated statements of changes in equity. Any interest expense incurred is recognized as part of “Interest expense and other financing charges” account in the consolidated statements of income.

The Group’s derivative liabilities are classified under this category (Note 22).

The carrying amounts of financial liabilities under this category amounted to ₱315 and ₱118 as of December 31, 2012 and 2011, respectively (Note 42).

Other Financial Liabilities. This category pertains to financial liabilities that are not designated or classified as at FVPL. After initial measurement, other financial liabilities are carried at amortized cost using the effective interest rate method. Amortized cost is calculated by taking into account any premium or discount and any directly attributable transaction costs that are considered an integral part of the effective interest rate of the liability.

The Group’s liabilities arising from its trade or borrowings such as loans payable, accounts payable and accrued expenses, long-term debt, finance lease liabilities and other noncurrent liabilities are included under this category (Notes 21, 22, 23, 24 and 35).

The combined carrying amounts of financial liabilities under this category amounted to ₱658,947 and ₱566,041 as of December 31, 2012 and 2011, respectively (Note 42).

Debt Issue Costs

Debt issue costs are considered as an adjustment to the effective yield of the related debt and are deferred and amortized using the effective interest rate method. When a loan is paid, the related unamortized debt issue costs at the date of repayment are recognized in profit or loss.

Derivative Financial Instruments and Hedging

Freestanding Derivatives

For the purpose of hedge accounting, hedges are classified as either: a) fair value hedges when hedging the exposure to changes in the fair value of a recognized asset or liability or an unrecognized firm commitment (except for foreign currency risk); b) cash flow hedges when hedging exposure to variability in cash flows that is either attributable to a particular risk associated with a recognized asset or liability or a highly probable forecast transaction or the foreign currency risk in an unrecognized firm commitment; or c) hedges of a net investment in foreign operations.

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At the inception of a hedge relationship, the Group formally designates and documents the hedge relationship to which the Group wishes to apply hedge accounting and the risk management objective and strategy for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk. Such hedges are expected to be highly effective in achieving offsetting changes in fair value or cash flows and are assessed on an ongoing basis to determine that they actually have been highly effective throughout the financial reporting periods for which they were designated.

Fair Value Hedge. Derivatives classified as fair value hedges are carried at fair value with corresponding change in fair value recognized in profit or loss. The carrying amount of the hedged asset or liability is also adjusted for changes in fair value attributable to the hedged item and the gain or loss associated with that remeasurement is also recognized in profit or loss.

When the hedge ceases to be highly effective, hedge accounting is discontinued and the adjustment to the carrying amount of a hedged financial instrument is amortized immediately.

The Group discontinues fair value hedge accounting if the hedging instrument expired, sold, terminated or exercised, the hedge no longer meets the criteria for hedge accounting or the Group revokes the designation.

The Group has no outstanding derivatives accounted for as fair value hedges as of December 31, 2012 and 2011.

Cash Flow Hedge. Changes in the fair value of a hedging instrument that qualifies as a highly effective cash flow hedge are recognized in other comprehensive income and presented in the consolidated statements of changes in equity. The ineffective portion is immediately recognized in profit or loss.

If the hedged cash flow results in the recognition of an asset or a liability, all gains or losses previously recognized directly in equity are transferred from equity and included in the initial measurement of the cost or carrying amount of the asset or liability. Otherwise, for all other cash flow hedges, gains or losses initially recognized in equity are transferred from equity to profit or loss in the same period or periods during which the hedged forecasted transaction or recognized asset or liability affects profit or loss.

When the hedge ceases to be highly effective, hedge accounting is discontinued prospectively. The cumulative gain or loss on the hedging instrument that has been reported directly in equity is retained in equity until the forecasted transaction occurs. When the forecasted transaction is no longer expected to occur, any net cumulative gain or loss previously reported in equity is recognized in profit or loss.

The Group has no outstanding derivatives accounted for as a cash flow hedge as of December 31, 2012 and 2011.

Net Investment Hedge. The Group has no hedge of a net investment in a foreign operation as of December 31, 2012 and 2011.

For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value of derivatives are taken directly to profit or loss during the year incurred.

Embedded Derivatives

The Group assesses whether embedded derivatives are required to be separated from host contracts when the Group becomes a party to the contract.

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 as at FVPL. Reassessment only occurs if there is a change in the terms of the contract that significantly modifies the cash flows that would otherwise be required.

Derecognition of Financial Assets and Financial Liabilities

Financial Assets. A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognized when:

- the rights to receive cash flows from the asset have expired;

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- 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 rights 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 substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Group has transferred its rights to receive cash flows from an asset 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 Liabilities. A financial liability is derecognized when the obligation under the liability is discharged, cancelled or expired. When 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. The difference in the respective carrying amounts is recognized in profit or loss.

Impairment of Financial Assets

The Group assesses at the reporting date whether 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 have occurred after the initial recognition of the asset (an incurred loss event) and that loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated.

Assets Carried at Amortized Cost. For assets carried at amortized cost such as loans and receivables, 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 no objective evidence of impairment has been identified for a particular financial asset that was individually assessed, the Group includes the asset as part of a group of financial assets pooled according to their credit risk characteristics and collectively assesses the group for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognized are not included in the collective impairment assessment.

Evidence of impairment for specific impairment purposes may include indications that the borrower or a group of borrowers is experiencing financial difficulty, default or delinquency in principal or interest payments, or may enter into bankruptcy or other form of financial reorganization intended to alleviate the financial condition of the borrower. For collective impairment purposes, evidence of impairment may include observable data on existing economic conditions or industry-wide developments indicating that there is a measurable decrease in the estimated future cash flows of the related assets.

If there is objective evidence of impairment, the amount of 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) discounted at the financial asset’s original effective interest rate (i.e., the effective interest rate computed at initial recognition). Time value is generally not considered when the effect of discounting the cash flows is not material. If a loan or receivable has a variable rate, the discount rate for measuring any impairment loss is the current effective interest rate, adjusted for the original credit risk premium. For collective impairment purposes, impairment loss is computed based on their respective default and historical loss experience.

The carrying amount of the asset shall be reduced either directly or through the use of an allowance account. The impairment loss for the period shall be recognized in profit or loss. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to 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 amount of the asset does not exceed its amortized cost at the reversal date.

AFS Financial Assets. If an AFS financial asset is impaired, an amount comprising the difference between the cost (net of any principal payment and amortization) and its current fair value, less any impairment loss on that

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financial asset previously recognized in profit or loss, is transferred from equity to profit or loss. Reversals in respect of equity instruments classified as AFS financial assets are not recognized in profit or loss. Reversals of impairment losses on debt instruments are recognized in profit or loss, if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognized in profit or loss.

In the case of an unquoted equity instrument or of a derivative asset linked to and must be settled by delivery of an unquoted equity instrument, for which its fair value cannot be reliably measured, the amount of impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows from the asset discounted using the historical effective rate of return on the asset.

Classification of Financial Instruments Between Debt and Equity

From the perspective of the issuer, a financial instrument is classified as debt instrument if it provides for a contractual obligation to:

- deliver cash or another financial asset to another entity;
- exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavorable to the Group; or
- satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity shares.

If the Group does not have an unconditional right to avoid delivering cash or another financial asset to settle its contractual obligation, the obligation meets the definition of a financial liability.

Offsetting Financial Instruments

Financial assets and financial liabilities are offset and the net amount is reported in the consolidated statements of financial position 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 statements of financial position.

Inventories

Finished goods, goods in process and materials and supplies are valued at the lower of cost and net realizable value.

Costs incurred in bringing each inventory to its present location and conditions are accounted for as follows:

Finished goods and goods in process	—	at cost which includes direct materials and labor and a proportion of manufacturing overhead costs based on normal operating capacity but excluding borrowing costs; finished goods include unrealized gain (loss) on fair valuation of agricultural produce; costs are determined using the moving-average method.
Petroleum products (except lubes and greases, waxes and solvents), crude oil, and other products	—	at cost which includes duties and taxes related to the acquisition of inventories; costs are determined using the first-in, first-out method.
Lubes and greases, waxes and solvents	—	at cost which includes duties and taxes related to the acquisition of inventories; costs are determined using the moving-average method.
Materials, supplies and others	—	at cost using the moving-average method.
Coal	—	at cost using the first-in, first-out method.

Net realizable value of finished goods is the estimated selling price in the ordinary course of business, less the estimated costs necessary to make the sale.

Net realizable value of goods in process is the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs necessary to make the sale.

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For petroleum products, crude oil, and tires, batteries and accessories (TBA), the net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs to complete and/or market and distribute.

Net realizable value of materials and supplies, including coal is the current replacement cost.

Containers (i.e., returnable bottles and shells) are stated at deposit values less any impairment in value. The excess of the acquisition cost of the containers over their deposit value is presented under deferred containers included under "Other noncurrent assets" account in the consolidated statements of financial position and is amortized over the estimated useful lives of two to ten years. Amortization of deferred containers is included under "Selling and administrative expenses" account in the consolidated statements of income.

Biological Assets and Agricultural Produce

The Group's biological assets include breeding stocks, growing hogs, cattle and poultry livestock and goods in process which are grouped according to their physical state, transformation capacity (breeding, growing or laying), as well as their particular stage in the production process.

Breeding stocks are carried at accumulated costs net of amortization and any impairment in value while growing hogs, cattle and poultry livestock and goods in process are carried at accumulated costs. The costs and expenses incurred up to the start of the productive stage are accumulated and amortized over the estimated productive lives of the breeding stocks. The Group uses this method of valuation since fair value cannot be measured reliably. The Group's biological assets have no active market and no active market for similar assets prior to point of harvest are available in the Philippine poultry and hog industries. Further, the existing sector benchmarks are determined to be irrelevant and the estimates (i.e., revenues due to highly volatile prices, input costs, efficiency values) necessary to compute for the present value of expected net cash flows comprise a wide range of data which will not result to a reliable basis for determining the fair value.

The carrying amounts of the biological assets are reviewed for impairment when events or changes in circumstances indicate that the carrying amounts may not be recoverable.

The Group's agricultural produce, which consists of grown broilers and marketable hogs and cattle harvested from the Group's biological assets, are measured at their fair value less estimated costs to sell at the point of harvest. The fair value of grown broilers is based on the quoted prices for harvested mature grown broilers in the market at the time of harvest. For marketable hogs and cattle, the fair value is based on the quoted prices in the market at any given time.

The Group in general, does not carry any inventory of agricultural produce at any given time as these are either sold as live broilers, hogs and cattle or transferred to the different poultry or meat processing plants and immediately transformed into processed or dressed chicken and carcass.

Amortization is computed using straight-line method over the following estimated productive lives of breeding stocks:

	<u>Amortization Period</u>
Hogs — sow	3 years or 6 births, whichever is shorter
Hogs — boar	2.5 - 3 years
Cattle	2.5 - 3 years
Poultry breeding stock	40 - 44 weeks

Business Combination

Business combinations are accounted for using the acquisition method as at the acquisition date, which is the date on which control is transferred to the Group. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, the Group takes into consideration potential voting rights that are currently exercisable.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date through profit or loss.

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The Group measures goodwill at the acquisition date as: a) the fair value of the consideration transferred; plus b) the recognized amount of any non-controlling interests in the acquiree; plus c) if the business combination is achieved in stages, the fair value of the existing equity interest in the acquiree; less d) the net recognized amount (generally fair value) of the identifiable assets acquired and liabilities assumed. When the excess is negative, a bargain purchase gain is recognized immediately in profit or loss. Subsequently, goodwill is measured at cost less any accumulated impairment in value. Goodwill is reviewed for impairment, annually or more frequently, if events or changes in circumstances indicate that the carrying amount may be impaired.

The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are generally recognized in profit or loss. Costs related to the acquisition, other than those associated with the issue of debt or equity securities that the Group incurs in connection with a business combination, are expensed as incurred. Any contingent consideration payable is measured at fair value at the acquisition date. If the contingent consideration is classified as equity, then it is not remeasured and settlement is accounted for within equity. Otherwise, subsequent changes to the fair value of the contingent consideration are recognized in profit or loss.

- *Goodwill in a Business Combination*

Goodwill acquired in a business combination is, from the acquisition date, allocated to each of the cash-generating units, or groups of cash-generating units that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities are assigned to those units or groups of units. Each unit or group of units to which the goodwill is so allocated:

- represents the lowest level within the Group at which the goodwill is monitored for internal management purposes; and
- is not larger than an operating segment determined in accordance with PFRS 8.

Impairment is determined by assessing the recoverable amount of the cash-generating unit or group of cash-generating units, to which the goodwill relates. Where the recoverable amount of the cash-generating unit or group of cash-generating units is less than the carrying amount, an impairment loss is recognized. Where goodwill forms part of a cash-generating unit or group of cash-generating units 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 based on the relative values of the operation disposed of and the portion of the cash-generating unit retained. An impairment loss with respect to goodwill is not reversed.

- *Intangible Assets Acquired in a Business Combination*

The cost of an intangible asset acquired in a business combination is the fair value as at the date of acquisition, determined using discounted cash flows as a result of the asset being owned.

Following initial recognition, intangible asset is carried at cost less any accumulated amortization and impairment losses, if any. The useful life of an intangible asset is assessed to be either finite or indefinite.

An intangible asset with finite life is amortized over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset with a finite useful life are reviewed at least at each reporting date. A change in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for as a change in accounting estimates. The amortization expense on intangible asset with finite life is recognized in profit or loss.

- *Loss of Control*

Upon the loss of control, the Group derecognizes the assets and liabilities of the subsidiary, any non-controlling interests and the other components of equity related to the subsidiary. Any surplus or deficit arising on the loss of control is recognized in profit or loss. If the Group retains any interest in the previous subsidiary, then such interest is measured at fair value at the date that control is lost. Subsequently, it is accounted for as an equity-accounted investee or as an AFS financial asset depending on the level of influence retained.

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Transactions Under Common Control

Transactions under common control entered into in contemplation of each other and business combination under common control designed to achieve an overall commercial effect are treated as a single transaction.

Transfers of assets between commonly controlled entities are accounted for using book value accounting.

Non-controlling Interests

The acquisitions of non-controlling interests are accounted for as transactions with owners in their capacity as owners and therefore no goodwill is recognized as a result of such transactions. Any difference between the purchase price and the net assets of the acquired entity is recognized in equity. The adjustments to non-controlling interests are based on a proportionate amount of the net assets of the subsidiary.

Investments in Associates

The Group's investments in associates are accounted for under the equity method of accounting from the date when they become associates. An associate is an entity in which the Group has significant influence and which is neither a subsidiary nor a joint venture. Significant influence is presumed to exist when the Group holds between 20 to 50 percent of the voting power of another entity.

Under the equity method, the investment in an associate is initially recognized at cost and the carrying amount is increased or decreased to recognize the Group's share in the profit or loss of the associate after the date of acquisition. The Group's share in the profit or loss of the associate is recognized as "Equity in net earnings of associates" account in the Group's consolidated statements of income. Dividends received from an associate reduce the carrying amount of the investment. Adjustments to the carrying amount may also be necessary for changes in the Group's proportionate interest in the associate arising from changes in the associate's other comprehensive income. The Group's share of those changes is recognized in other comprehensive income.

Goodwill relating to an associate is included in the carrying amount of the investment and is not amortized.

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 associate. Profits and losses resulting from transactions between the Group and the associate are eliminated to the extent of the interest in the associate.

Upon acquisition of the investment, any difference between the cost of the investment and the investor's share in the net fair value of the associate's identifiable assets, liabilities and contingent liabilities is accounted for in accordance with PFRS 3, *Business Combination*. Consequently:

- a. goodwill that forms part of the carrying amount of an investment in an associate is not recognized separately and therefore is not tested for impairment separately. Instead, the entire amount of the investment in an associate is tested for impairment as a single asset when there is objective evidence that the investment in an associate may be impaired.
- b. any excess of the Group's share in the net fair value of the associate's identifiable assets, liabilities and contingent liabilities over the cost of the investment is excluded from the carrying amount of the investment and is instead included as income in the determination of the Group's share in the associate's profit or loss in the period in which the investment is acquired.

The Group discontinues applying the equity method when its investment in an associate is reduced to zero. Additional losses are provided only to the extent that the Group has incurred obligations or made payments on behalf of the associate to satisfy obligations of the associate that the Group has guaranteed or otherwise committed. If the associate subsequently reports profits, the Group resumes applying the equity method only after its share of the profits equals the share of net losses not recognized during the period the equity method was suspended.

The financial statements of the associates are prepared for the same reporting period as the Parent Company. The accounting policies of the associates conform to those used by the Group for like transactions and events in similar circumstances.

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Interest in Joint Venture

The Group generally recognizes its interest in joint venture using proportionate consolidation. The Group combines its share in each of the assets, liabilities, income and expenses of the joint venture with similar items, line by line, in its consolidated financial statements. The financial statements of the joint venture are prepared for the same reporting period as the Parent Company, using uniform accounting policies for like transactions and other events in similar circumstances. Adjustments are made to bring into line any dissimilar accounting policies that may exist.

The joint venture is proportionately consolidated until the date when the Group ceases to have joint control over the joint venture.

Property, Plant and Equipment

Property, plant and equipment, except land, are stated at cost less accumulated depreciation and amortization and any accumulated impairment in value. Such cost includes the cost of replacing part of the property, plant and equipment at the time that cost is incurred, if the recognition criteria are met, and excludes the costs of day-to-day servicing. Land is stated at cost less any impairment in value.

The initial cost of property, plant and equipment comprises of its construction cost or purchase price, including import duties, taxes and any directly attributable costs in bringing the asset to its working condition and location for its intended use. Cost also includes any related asset retirement obligation (ARO). Expenditures incurred after the asset has been put into operation, such as repairs, maintenance and overhaul costs, are normally recognized as expense in the period the costs are incurred. Major repairs are capitalized as part of property, plant and equipment only when it is probable that future economic benefits associated with the items will flow to the Group and the cost of the items can be measured reliably.

Construction in progress (CIP) represents structures under construction and is stated at cost. This includes the costs of construction and other direct costs. Borrowing costs that are directly attributable to the construction of plant and equipment are capitalized during the construction period. CIP is not depreciated until such time that the relevant assets are ready for use.

Depreciation and amortization, which commences when the assets are available for their intended use, are computed using the straight-line method over the following estimated useful lives of the assets:

	<u>Number of Years</u>
Land improvements	5 - 50
Buildings and improvements	2 - 50
Power plants	3 - 43
Refinery and plant equipment	5 - 16
Service stations and other equipment	1 ½ - 10
Machinery and equipment	3 - 40
Telecommunications equipment	3 - 25
Transportation equipment	5 - 10
Tools and small equipment	2 - 10
Office equipment, furniture and fixtures	2 - 10
Molds	2 - 5
Leasehold improvements	5 - 50
	or term of the lease, whichever is shorter

The remaining useful lives, residual values, and depreciation and amortization methods are reviewed and adjusted periodically, if appropriate, to ensure that such periods and methods of depreciation and amortization are consistent with the expected pattern of economic benefits from the items of property, plant and equipment.

The carrying amounts of property, plant and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying amounts may not be recoverable.

Fully depreciated assets are retained in the accounts until they are no longer in use.

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An item of property, plant and equipment is derecognized when either it has been disposed of or when it is permanently withdrawn from use and no future economic benefits are expected from its use or disposal. Any gain or loss arising from the retirement and disposal of an item of property, plant and equipment (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in profit or loss in the period of retirement and disposal.

Investment Properties

Investment properties consist of properties held to earn rentals and/or for capital appreciation but not for sale in the ordinary course of business, use in the production or supply of goods or services or for administrative purposes. Investment properties, except for land, are measured at cost including transaction costs less accumulated depreciation and amortization and any accumulated impairment in value. The carrying amount includes the cost of replacing part of an existing investment property at the time the cost is incurred, if the recognition criteria are met, and excludes the costs of day-to-day servicing of an investment property. Land is stated at cost less any impairment in value.

Depreciation and amortization, which commences when the assets are available for their intended use, are computed using the straight-line method over the following estimated useful lives of the assets:

	<u>Number of Years</u>
Land improvements	5 - 50
Buildings and improvements	2 - 50
Machinery and equipment	3 - 40
Tools and small equipment	2 - 5

The useful lives, residual values and depreciation and amortization method are reviewed and adjusted, if appropriate, at each reporting date.

Investment property is derecognized either when it has been disposed of or when it is permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gains and losses on the retirement and disposal of investment property are recognized in profit or loss in the period of retirement and disposal.

Transfers are made to investment property when, and only when, there is a change in use, evidenced by ending of owner-occupation or commencement of an operating lease to another party. Transfers are made from investment property when, and only when, there is a change in use, evidenced by commencement of the owner-occupation or commencement of development with a view to sell.

For a transfer from investment property to owner-occupied property or inventories, the cost of property for subsequent accounting is its carrying amount at the date of change in use. If the property occupied by the Group as an owner-occupied property becomes an investment property, the Group accounts for such property in accordance with the policy stated under property, plant and equipment up to the date of change in use.

Intangible Assets

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is its fair value as at the date of acquisition. Subsequently, intangible assets are measured at cost less accumulated amortization and any accumulated impairment losses. Internally generated intangible assets, excluding capitalized development costs, are not capitalized and expenditures are recognized in profit or loss in the year in which the related expenditures are incurred. The useful lives of intangible assets are assessed to be either finite or indefinite.

Intangible assets with finite lives are amortized over the useful life and assessed for impairment whenever there is an indication that the intangible assets may be impaired. The amortization period and the amortization method used for an intangible asset with a finite useful life are reviewed at least at each reporting date. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for by changing the amortization period or method, as appropriate, and are treated as changes in accounting estimates. The amortization expense on intangible assets with finite lives is recognized in profit or loss consistent with the function of the intangible asset.

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Amortization is computed using straight-line method over the following estimated useful lives of other intangible assets with finite lives:

	<u>Number of Years</u>
Computer software and licenses	2 - 8
Airport concession rights	25
Toll road concession rights	30
Mining rights	19 - 30
Leasehold rights	20 or term of the lease, whichever is shorter
Land use rights	25 - 50 or term of the lease, whichever is shorter

The Group assessed the useful lives of licenses and trademarks and brand names to be indefinite. Based on an analysis of all the relevant factors, there is no foreseeable limit to the period over which the assets are expected to generate cash inflows for the Group.

Licenses and trademarks and brand names with indefinite useful lives are tested for impairment annually either individually or at the cash-generating unit level. Such intangibles are not amortized. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is made on a prospective basis.

Gains or losses arising from the disposal of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset, and are recognized in profit or loss when the asset is derecognized.

Service Concession Arrangements

Public-to-private service concession arrangements where: (a) the grantor controls or regulates what services the entities in the Group must provide with the infrastructure, to whom it must provide them, and at what price; and (b) the grantor controls (through ownership, beneficial entitlement or otherwise) any significant residual interest in the infrastructure at the end of the term of the arrangement are accounted for under Philippine Interpretation IFRIC 12, *Service Concession Arrangements*. Infrastructures used in a public-to-private service concession arrangement for its entire useful life (whole-of-life assets) are within the scope of this Interpretation if the conditions in (a) are met.

This Interpretation applies to both: (a) infrastructure that the entities in the Group construct or acquire from a third party for the purpose of the service arrangement; and (b) existing infrastructure to which the grantor gives the entity in the Group access for the purpose of the service arrangement.

Infrastructures within the scope of this Interpretation are not recognized as property, plant and equipment of the Group. Under the terms of contractual arrangements within the scope of this Interpretation, an entity acts as a service provider. An entity constructs or upgrades infrastructure (construction or upgrade services) used to provide a public service and operates and maintains that infrastructure (operation services) for a specified period of time.

An entity recognizes and measures revenue in accordance with PAS 11 and PAS 18 for the services it performs. If an entity performs more than one service (i.e., construction or upgrade services and operation services) under a single contract or arrangement, consideration received or receivable shall be allocated by reference to the relative fair values of the services delivered, when the amounts are separately identifiable.

When an entity provides construction or upgrade services, the consideration received or receivable by the entity is recognized at its fair value. An entity accounts for revenue and costs relating to construction or upgrade services in accordance with PAS 11. Revenue from construction contracts is recognized based on the percentage-of-completion method, measured by reference to the proportion of costs incurred to date, to estimated total costs for each contract. The applicable entities account for revenue and costs relating to operation services in accordance with PAS 18.

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An entity recognizes a financial asset to the extent that it has an unconditional contractual right to receive cash or another financial asset from or at the direction of the grantor for the construction services. An entity recognizes an intangible asset to the extent that it receives a right (a license) to charge users of the public service.

When the applicable entities have contractual obligations to fulfill as a condition of its license: (a) to maintain the infrastructure to a specified level of serviceability, or (b) to restore the infrastructure to a specified condition before it is handed over to the grantor at the end of the service arrangement, it recognizes and measures these contractual obligations in accordance with PAS 37, *Provisions, Contingent Liabilities and Contingent Assets*, i.e., at the best estimate of the expenditure that would be required to settle the present obligation at the reporting date.

In accordance with PAS 23, *Borrowing Costs*, borrowing costs attributable to the arrangement are recognized as an expense in the period in which they are incurred unless the applicable entities have a contractual right to receive an intangible asset (a right to charge users of the public service). In this case, borrowing costs attributable to the arrangement are capitalized during the construction phase of the arrangement.

Intangible Asset — Airport Concession Right

The Group's intangible asset — airport concession right pertains to the right granted by the Republic of the Philippines (ROP) to TADHC: (a) to operate the Caticlan Airport (the Airport Project, known as the Boracay Airport starting 2011) as expressly stated in the Concession Agreement (CA) (Note 35), (b) the right to design and finance the development of the Airport Project, and operate and maintain the Boracay Airport during the concession period and (c) the present value of the annual franchise fee, as defined in the CA, payable to the ROP over the concession period of 25 years. Except for the portion that relates to the annual franchise fee, which is recognized immediately as intangible asset, the right is earned and recognized by the Group as the project progresses (Note 4).

Intangible asset is carried at cost, as determined above, less accumulated amortization and any accumulated impairment losses.

The intangible asset — airport concession right is amortized using the straight-line method over the remaining concession period, and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method are reviewed at least at each reporting date. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and are treated as changes in accounting estimates. The amortization expense is recognized in profit or loss in the expense category consistent with the function of the intangible asset.

An intangible asset is derecognized on disposal or when no further economic benefits are expected from its use or disposal.

Gain or loss from derecognition of the intangible asset — airport concession right is measured as the difference between the net disposal proceeds and the carrying amount of the asset, and is recognized in profit or loss.

Intangible Asset — Toll Road Concession Rights

The Group's intangible asset — toll road concession rights represent the costs of construction and development of Stage 1 and Stage 2 of the South Metro Manila Skyway (SMMS or the Skyway Project), including borrowing costs during the construction period. Toll road concession rights are recognized initially at the fair value of the construction services. Following initial recognition, the toll road concession rights are carried at cost less accumulated amortization and any impairment losses. Subsequent expenditures or replacement of part of it, are normally charged to profit or loss as these are incurred, to maintain the expected future economic benefits embodied in the toll road concession rights. Expenditures that will contribute to the increase in revenue from toll operations are recognized as intangible asset.

From 1999 to April 26, 2011, toll road concession rights pertaining to Stage 1, which was fully operational, were amortized on a straight-line basis over the 30-year concession period. At the start of the operation of the Integrated Stage 1 and Stage 2 on April 26, 2011, the intangible asset — toll road concession rights pertaining to unamortized balance of Stage 1 and total costs of Stage 2 were amortized over the 30-year concession period. The amortization period and method are reviewed when there are changes in the expected term of the contract or

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the expected pattern of consumption of future economic benefits embodied in the asset. These changes are treated as changes in accounting estimates. The amortization expense on the asset is recognized in profit or loss.

The carrying value of the intangible asset — toll road concession rights is reviewed for impairment annually when the asset is not yet in use or more frequently when an indication of impairment arises during the reporting year.

The intangible asset — toll road concession rights will be derecognized upon turnover to the ROP. There will be no gain or loss upon derecognition of intangible asset — toll road concession rights as these are expected to be fully amortized upon turnover to the ROP.

Intangible Asset — Mining Rights

The Group's intangible asset — mining rights that are acquired by the Group and have finite lives are measured at costs less accumulated amortization and any accumulated impairment losses.

Subsequent expenditures are capitalized only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditures are recognized in profit or loss as incurred.

Amortization of intangible asset — mining rights is recognized in profit or loss on a straight-line basis over the estimated useful lives. The estimated useful lives of intangible asset — mining rights pertain to the period from commercial operations to the end of the operating contract. Amortization method and useful lives are reviewed at each reporting date and adjusted as appropriate.

Deferred Exploration and Development Costs

Deferred exploration and development costs comprise of expenditures which are directly attributable to:

- Researching and analyzing existing exploration data;
- Conducting geological studies, exploratory drilling and sampling;
- Examining and testing extraction and treatment methods; and
- Compiling pre-feasibility and feasibility studies.

Deferred exploration and development costs also include expenditures incurred in acquiring mineral rights, entry premiums paid to gain access to areas of interest and amounts payable to third parties to acquire interests in existing projects.

Exploration assets are reassessed on a regular basis and tested for impairment provided that at least one of the following conditions is met:

- the period for which the entity has the right to explore in the specific area has expired during the period or will expire in the near future, and is not expected to be renewed;
- substantive expenditure on further exploration for and evaluation of mineral resources in the specific area is neither budgeted nor planned;
- such costs are expected to be recouped in full through successful development and exploration of the area of interest or alternatively, by its sale; or
- exploration and evaluation activities in the area of interest have not yet reached a stage which permits a reasonable assessment of the existence or otherwise of economically recoverable reserves, and active and significant operations in relation to the area are continuing, or planned for the future.

If the project proceeds to development stage, the amounts included within deferred exploration and development costs are transferred to property, plant and equipment under mine development costs.

Impairment of Non-financial Assets

The carrying amounts of investments and advances, property, plant and equipment, investment properties, deferred containers, biological assets — net of current portion, other intangible assets with finite useful lives and idle assets are reviewed for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. Licenses and trademarks and brand names with indefinite useful lives are tested

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for impairment annually either individually or at the cash-generating unit level. If any such indication exists, and if the carrying amount exceeds the estimated recoverable amount, the assets or cash-generating units are written down to their recoverable amounts. The recoverable amount of the asset is the greater of fair value less costs to sell and value in use. The fair value less costs to sell is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less costs of disposal. 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 assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognized in profit or loss in those expense categories consistent with the function of the impaired asset.

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 profit or loss. After such a reversal, the depreciation and amortization 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.

Cylinder Deposits

The liquefied petroleum gas cylinders remain the property of the Group and are loaned to dealers upon payment by the latter of an amount equivalent to 100% of the acquisition cost of the cylinders.

The Group maintains the balance of cylinder deposits at an amount equivalent to three days worth of inventory of its biggest dealers, but in no case lower than ₱200 at any given time, to take care of possible returns by dealers.

At the end of each reporting date, cylinder deposits, shown under "Other noncurrent liabilities" account in the consolidated statements of financial position, are reduced for estimated non-returns. The reduction is credited directly to profit or loss.

Provisions

Provisions are recognized when: (a) the Group has a present obligation (legal or constructive) as a result of past events; (b) it is probable (i.e., more likely than not) that an outflow of resources embodying economic benefits will be required to settle the obligation; and (c) a reliable estimate can be made of the amount of the obligation. 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 assessment of the time value of money and 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. Where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement shall be recognized when, and only when, it is virtually certain that reimbursement will be received if the entity settles the obligation. The reimbursement shall be treated as a separate asset. The amount recognized for the reimbursement shall not exceed the amount of the provision. Provisions are reviewed at each reporting date and adjusted to reflect the current best estimate.

Infrastructure restoration obligation (IRO) represents the present value of the Group's obligation to keep the rehabilitated and upgraded Boracay Airport at a serviceability level acceptable to the ROP through continuous maintenance and restoration prior to its turnover to the ROP at the end of the concession period.

Share Capital

Common Shares

Common shares are classified as equity. Incremental costs directly attributable to the issue of common shares and share options are recognized as a deduction from equity, net of any tax effects.

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Preferred Shares

Preferred shares are classified as equity if they are non-redeemable, or redeemable only at the Parent Company's option, and any dividends thereon are discretionary. Dividends thereon are recognized as distributions within equity upon approval by the Parent Company's BOD.

Preferred shares are classified as a liability if they are redeemable on a specific date or at the option of the shareholders, or if dividend payments are not discretionary. Dividends thereon are recognized as interest expense in profit or loss as accrued.

Treasury Shares

Own equity instruments which are reacquired are carried at cost and are deducted from equity. No gain or loss is recognized on the purchase, sale, reissuance or cancellation of the Parent Company's 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 Recognition

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Group and the amount of revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognized:

Revenue from Sale of Goods

Revenue from sale of goods in the course of ordinary activities is measured at the fair value of the consideration received or receivable, net of returns, trade discounts and volume rebates. Revenue is recognized when the significant risks and rewards of ownership of the goods have passed to the buyer, which is normally upon delivery and the amount of revenue can be measured reliably.

Revenue from Power Generation

Revenue from power generation is recognized in the period actual capacity is generated and transmitted to the customers, net of related discounts.

Revenue from Telecommunications Services

Revenue from telecommunications services includes the value of all services provided and are recognized when earned and are stated net of the share of other telecommunications administrations, if any, under existing correspondence and interconnection agreements.

Inbound revenue represents settlements from telecommunications providers who sent traffic to the Group's network. Inbound revenue is based on agreed payment accounting rates with other carriers. Interconnection charges are based on the rates agreed with other carriers.

Both the inbound revenue and interconnection charges are accrued based on actual volume of traffic. Adjustments are made on the recorded amount for discrepancies between the traffic volume based on the Group's records and the records of the other carriers. These adjustments are recognized as they are determined and agreed with the other carriers.

Installation fees received from landline subscribers are also credited to operating revenues. The related labor costs on installation are recognized in profit or loss.

Revenue from Airport Operations

Landing, take-off and parking fees are recognized upon rendering of the service which is the period from landing up to take-off of aircrafts.

Terminal fees are recognized upon receipt of fees charged to passengers on departure.

Construction revenue related to the Group's recognition of intangible asset on the right to operate the Boracay Airport, which is the consideration receivable from ROP relative to the Airport Project, is earned and recognized

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as the Airport Project progresses. The Group recognizes the corresponding amount as intangible asset as it recognizes the construction revenue. The Group assumes no profit margin in earning the right to operate the Boracay Airport.

The Group uses the cost to cost percentage of completion method to determine the appropriate amount of revenue to be recognized in a given period. The stage of completion is measured by reference to the costs incurred related to the Airport Project up to the end of the reporting period as a percentage of total estimated cost.

Revenue from Toll Operations

Revenue from toll operations is recognized upon the use by the road users of the toll road and the toll is paid by way of cash or charges against an E-Pass account.

Construction revenue is recognized by reference to the stage of completion of the construction activity at the reporting date. When it is probable that the total contract costs will exceed total contract revenue, the expected loss is recognized as an expense immediately.

Revenue from Agricultural Produce

Revenue from initial recognition of agricultural produce is measured at fair value less estimated costs to sell at the point of harvest. Fair value is based on the relevant market price at the point of harvest.

Others

Interest income is recognized as the interest accrues, taking into account the effective yield on the asset.

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

Rent income from investment properties is recognized on a straight-line basis over the term of the lease. Lease incentives granted are recognized as an integral part of the total rent income over the term of the lease.

Gain or loss on sale of investments in shares of stock is recognized if the Group disposes of its investment in a subsidiary, associate, AFS financial assets and financial assets at FVPL. Gain or loss is computed as the difference between the proceeds of the disposed investment and its carrying amount, including the carrying amount of goodwill, if any.

Cost and Expense Recognition

Costs and expenses are recognized upon receipt of goods, utilization of services or at the date they are incurred.

Expenses are also recognized when decrease in future economic benefit related to a decrease in an asset or an increase in a liability that can be measured reliably has arisen. Expenses are recognized on the basis of a direct association between costs incurred and the earning of specific items of income; on the basis of systematic and rational allocation procedures when economic benefits are expected to arise over several accounting periods and the association can only be broadly or indirectly determined; or immediately when an expenditure produces no future economic benefits or when, and to the extent that future economic benefits do not qualify, or cease to qualify, for recognition as an asset.

Share-based Payment Transactions

The cost of Long-term Incentive Plan for Stock Options (LTIP) is measured by reference to the option fair value at the date when the options are granted. The fair value is determined using Black-Scholes option pricing model. In valuing LTIP transactions, any performance conditions are not taken into account, other than conditions linked to the price of the shares of the Parent Company. The cost of Employee Stock Purchase Plan (ESPP) is measured by reference to the market price at the time of the grant less subscription price.

The cost of share-based payment transactions is recognized, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date when the relevant employees become fully entitled to the award (the "vesting date"). The cumulative expenses recognized for share-based payment transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Parent Company's best estimate of the number of equity instruments that will

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ultimately vest. Where the terms of a share-based 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 modification, which increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee 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.

Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement and requires an assessment of whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset. A reassessment is made after the 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 specific 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 gives rise to the reassessment for scenarios (a), (c) or (d), and at the date of renewal or extension period for scenario (b) above.

Finance Lease

Finance leases, which transfer to the Group 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. Obligations arising from plant assets under finance lease agreement are classified in the consolidated statements of financial position as finance lease liabilities.

Lease payments are apportioned between financing charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Financing charges are recognized in profit or loss.

Capitalized leased assets are depreciated over the estimated useful lives of the assets when there is reasonable certainty that the Group will obtain ownership by the end of the lease term.

Operating Lease

Group as Lessee. Leases which do not transfer to the Group substantially all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognized as an expense in profit or loss on a straight-line basis over the lease term. Associated costs such as maintenance and insurance are expensed as incurred.

Group as Lessor. Leases where the Group does not transfer substantially all the risks and benefits of ownership of the assets are classified as operating leases. Rent income from operating leases is recognized as income on a straight-line basis over the lease term. Initial direct costs incurred in negotiating an operating lease are added to the carrying amount of the leased asset and recognized as an expense over the lease term on the same basis as rent income. Contingent rents are recognized as income in the period in which they are earned.

Borrowing Costs

Borrowing costs are capitalized if they are directly attributable to the acquisition or construction of a qualifying asset. Capitalization of borrowing costs commences when the activities to prepare the asset are in progress and

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expenditures and borrowing costs are being incurred. Borrowing costs are capitalized until the assets are substantially ready for their intended use. If the carrying amount of the asset exceeds its recoverable amount, an impairment loss is recognized.

Research and Development Costs

Research costs are expensed as incurred. Development costs incurred on an individual project are carried forward when their future recoverability can be reasonably regarded as assured. Any expenditure carried forward is amortized in line with the expected future sales from the related project.

The carrying amount of development costs is reviewed for impairment annually when the related asset is not yet in use. Otherwise, this is reviewed for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable.

Retirement Costs

The Parent Company and majority of its subsidiaries have separate funded, noncontributory retirement plans, administered by the respective trustees, covering their respective permanent employees.

Retirement costs are actuarially determined using the projected unit credit method. This method reflects service rendered by employees up to the date of valuation and incorporates assumptions concerning employees' projected salaries. Retirement cost includes current service cost, interest cost, expected return on plan assets, amortization of unrecognized past service costs, recognition of actuarial gains and losses, effect of asset limit and effect of any curtailments or settlements. Past service cost is recognized as an expense on a straight-line basis over the average period until the benefits become vested. Past service cost is recognized immediately as an expense, if the benefits are vested immediately following the introduction of, or changes to the plan. Actuarial gains and losses are recognized as income or expense when the net cumulative unrecognized actuarial gains and losses at the end of the previous reporting year exceed the greater of 10% of the present value of the defined benefit obligation and the fair value of plan assets at that date. These gains or losses are recognized over the expected average remaining working lives of the employees participating in the plan.

The defined benefit liability is the aggregate of the present value of the defined benefit obligation and actuarial gains and losses not recognized, reduced by past service costs not yet recognized, and the fair value of plan assets out of which the obligations are to be settled directly. If such aggregate is negative, the resulting asset is measured at the lower of such aggregate, or the aggregate of cumulative unrecognized net actuarial losses and past service costs, and the present value of any economic benefits available in the form of reductions in the future contributions to the plan.

If the asset is measured at the aggregate of cumulative unrecognized net actuarial losses and past service costs, and the present value of any economic benefits available in the form of reductions in the future contributions to the plan, net actuarial losses of the current period and past service costs of the current period are recognized immediately to the extent that they exceed any reduction in the present value of those economic benefits. If there is no change or an increase in the present value of the economic benefits, the entire net actuarial losses of the current period and past service costs of the current period are recognized immediately. Similarly, net actuarial gains of the current period after the deduction of past service costs of the current period, exceeding any increase in the present value of the economic benefits stated above, are recognized immediately, if the asset is measured at the aggregate of cumulative unrecognized net actuarial losses and past service costs, and the present value of any economic benefits available in the form of reductions in the future contributions to the plan. If there is no change or a decrease in the present value of the economic benefits, the entire net actuarial gains of the current period after the deduction of past service costs of the current period are recognized immediately.

Foreign Currency

Foreign Currency Translations

Transactions in foreign currencies are translated to the respective functional currencies of Group entities at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortized cost in the functional currency at the

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beginning of the year, adjusted for effective interest and payments during the year, and the amortized cost in foreign currency translated at the exchange rate at the reporting date.

Nonmonetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date the fair value was determined. Nonmonetary items in a foreign currency that are measured in terms of historical cost are translated using the exchange rate at the date of the transaction.

Foreign currency differences arising on retranslation are recognized in profit or loss, except for differences arising on the retranslation of AFS financial assets, a financial liability designated as a hedge of the net investment in a foreign operation that is effective, or qualifying cash flow hedges, which are recognized in other comprehensive income.

Foreign Operations

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated to Philippine peso at exchange rates at the reporting date. The income and expenses of foreign operations, excluding foreign operations in hyperinflationary economies, are translated to Philippine peso at average exchange rates for the period.

Foreign currency differences are recognized in other comprehensive income, and presented in the foreign currency translation reserve ("Translation reserve") in the consolidated statements of changes in equity. However, if the operation is not a wholly-owned subsidiary, then the relevant proportionate share of the translation difference is allocated to the non-controlling interests. When a foreign operation is disposed of such that control, significant influence or joint control is lost, the cumulative amount in the translation reserve related to that foreign operation is reclassified to profit or loss as part of the gain or loss on disposal. When the Group disposes of only part of its interest in a subsidiary that includes a foreign operation while retaining control, the relevant proportion of the cumulative amount is reattributed to non-controlling interests. When the Group disposes of only part of its investment in an associate or joint venture that includes a foreign operation while retaining significant influence or joint control, the relevant proportion of the cumulative amount is reclassified to profit or loss.

When the settlement of a monetary item receivable from or payable to a foreign operation is neither planned nor likely in the foreseeable future, foreign exchange gains and losses arising from such a monetary item are considered to form part of a net investment in a foreign operation and are recognized in other comprehensive income, and presented in the "Translation reserve" in the consolidated statements of changes in equity.

Taxes

Current Tax. Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred Tax. Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

Deferred tax liabilities are recognized for all taxable temporary differences, except:

- where the deferred tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- with respect to taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

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Deferred tax assets are recognized for all deductible temporary differences, carryforward benefits of unused tax credits — Minimum Corporate Income Tax (MCIT) and unused tax losses — Net Operating Loss Carry Over (NOLCO), to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward benefits of MCIT and NOLCO can be utilized, except:

- where the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- with respect to deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

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

The measurement of deferred tax reflects the tax consequences that would follow the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

In determining the amount of current and deferred tax, the Group takes into account the impact of uncertain tax positions and whether additional taxes and interest may be due. The Group believes that its accruals for tax liabilities are adequate for all open tax years based on its assessment of many factors, including interpretation of tax laws and prior experience. This assessment relies on estimates and assumptions and may involve a series of judgments about future events. New information may become available that causes the Group to change its judgment regarding the adequacy of existing tax liabilities; such changes to tax liabilities will impact tax expense in the period that such a determination is made.

Current tax and deferred tax are recognized in profit or loss except to the extent that it relates to a business combination, or items recognized directly in equity or in other comprehensive 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.

Value-added Tax (VAT). Revenues, expenses and assets are recognized net of the amount of VAT, except:

- where the tax incurred on a purchase of assets or services is not recoverable from the taxation authority, in which case the tax is recognized as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- receivables and payables that are stated with the amount of tax included.

The net amount of tax recoverable from, or payable to, the taxation authority is included as part of “Prepaid expenses and other current assets” or “Income and other taxes payable” accounts in the consolidated statements of financial position.

Assets Held for Sale

Noncurrent assets, or disposal groups comprising assets and liabilities, that are expected to be recovered primarily through sale rather than through continuing use, are classified as held for sale. Immediately before classification as held for sale, the assets, or components of a disposal group, are remeasured in accordance with the Group’s accounting policies. Thereafter, the assets or disposal groups are generally measured at the lower of their carrying amount and fair value less costs to sell. Any impairment loss on a disposal group is allocated first to goodwill, and then to the remaining assets and liabilities on *pro rata* basis, except that no loss is allocated to inventories, financial assets, deferred tax assets, employee benefit assets, investment properties or biological

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assets, which continue to be measured in accordance with the Group's accounting policies. Impairment losses on initial classification as held for sale and subsequent gains and losses on remeasurement are recognized in profit or loss. Gains are not recognized in excess of any cumulative impairment losses.

Intangible assets, property, plant and equipment and investment properties once classified as held for sale are not amortized or depreciated. In addition, equity accounting of equity-accounted investees ceases once classified as held for sale.

Discontinued Operations

A discontinued operation is a component of the Group's business that represents a separate major line of business that has been disposed of or is held for sale, or is a subsidiary acquired exclusively with a view to resale. Classification as a discontinued operation occurs upon disposal or when the operation meets the criteria to be classified as held for sale. When an operation is classified as a discontinued operation, the comparative consolidated statements of income are re-presented as if the operation had been discontinued from the start of the comparative period and the results of discontinued operation are shown separately from the results of continuing operation.

Related Parties

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or significant influence. Related parties may be individuals or corporate entities. Transactions between related parties are on an arm's length basis in a manner similar to transactions with non-related parties.

Basic and Diluted Earnings per Common Share (EPS)

Basic EPS is computed by dividing the net income for the period attributable to equity holders of the Parent Company, net of dividends on preferred shares, by the weighted average number of issued and outstanding common shares during the period, with retroactive adjustment for any stock dividends declared.

Diluted EPS is computed in the same manner, adjusted for the effects of the shares issuable to employees and executives under the Parent Company's LTIP, which are assumed to be exercised at the date of grant.

Where the effect of the assumed conversion of shares issuable to employees and executives under the Parent Company's stock purchase and option plans would be anti-dilutive, diluted EPS is not presented.

Operating Segments

The Group's operating segments 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 operating segments is presented in Note 7 to the consolidated financial statements. The Chief Executive Officer (the "chief operating decision maker") reviews management reports on a regular basis.

The measurement policies the Group used for segment reporting under PFRS 8, are the same as those used in the consolidated financial statements. There have been no changes from prior periods in the measurement methods used to determine reported segment profit or loss. All inter-segment transfers are carried out at arm's length prices.

Segment revenues, expenses and performance include sales and purchases between business segments. Such sales and purchases are eliminated in consolidation.

Contingencies

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

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Events After the Reporting Date

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

4. Significant Accounting Judgments, Estimates and Assumptions

The preparation of the Group's consolidated financial statements in accordance with PFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the amounts of assets, liabilities, income and expenses reported in the consolidated financial statements at the reporting date. However, uncertainty about these judgments, estimates and assumptions could result in an outcome that could require a material adjustment to the carrying amount of the affected asset or liability in the future.

Judgments and estimates are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Revisions are recognized in the period in which the judgments and estimates are revised and in any future period affected.

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:

Finance Lease — Group as Lessee. In accounting for its Independent Power Producer Administration (IPPA) Agreements with Power Sector Assets and Liabilities Management Corporation (PSALM), the Group's management has made a judgment that the IPPA Agreements are agreements that contain a lease. SMYK also entered into leases of machinery and equipment and transportation equipment needed for business operations. In addition, Thai San Miguel Liquor Co. Ltd. (TSML) and Thai Ginebra Trading (TGT), the Group's joint ventures in Thailand, entered into lease agreements with a Thai bank covering transportation equipment. The Group's management has made a judgment that it has substantially acquired all the risks and rewards incidental to ownership of the power plants, machinery and equipment and transportation equipment. Accordingly, the Group accounted for the agreements as finance lease and recognized the power plants, machinery and equipment, transportation equipment and finance lease liabilities at the present value of the agreed monthly payments (Notes 16 and 35).

Finance lease liabilities recognized in the consolidated statements of financial position amounted to ₱195,154 and ₱208,261 as of December 31, 2012 and 2011, respectively (Note 35). The combined carrying amount of power plants, machinery and equipment and transportation equipment under finance lease amounted to ₱198,562 and ₱203,756 as of December 31, 2012 and 2011, respectively (Notes 16 and 35).

Operating Lease Commitments — Group as Lessor/Lessee. The Group has entered into various lease agreements either as a lessor or a lessee. The Group had determined that it retains all the significant risks and rewards of ownership of the properties leased out on operating leases while the significant risks and rewards for properties leased from third parties are retained by the lessors.

Rent income recognized in the consolidated statements of income amounted to ₱1,139, ₱412 and ₱267 in 2012, 2011 and 2010, respectively (Note 35).

Rent expense recognized in the consolidated statements of income amounted to ₱3,024, ₱2,575 and ₱1,812 in 2012, 2011 and 2010, respectively (Notes 27, 28 and 35).

Applicability of Philippine Interpretation IFRIC 12

Airport Concession Right. In accounting for the Group's transactions in connection with its CA with the ROP, significant judgment was applied to determine the most appropriate accounting policy to use. Management used Philippine Interpretation IFRIC 12 as guide and determined that the CA is within the scope of the interpretation since it specifically indicated that the ROP will regulate what services the Group must provide and at what prices those will be offered, and that at the end of the concession period, the entire infrastructure, as defined in the CA, will be transferred to the ROP. Reference was made to the terms of the CA in determining the consideration receivable from the ROP in exchange for the fulfillment of the Group's obligations under the CA (Note 35).

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Management determined that the consideration receivable is an intangible asset in the form of a license to operate the Boracay Airport; i.e. license to charge fees to users. Judgment was further exercised by management in determining the components of the cost of acquiring the right. Further reference to the terms of the CA (Note 35) was made to determine such costs and it identified the following as the components: (i) total Airport Project cost; (ii) present value of total franchise fees over 25 years and its subsequent amortization; and, (iii) present value of IRO.

Management also exercised judgment in determining the timing and manner of recognition of these costs. The Airport Project cost is recognized as part of intangible assets as the construction progresses. The cost to cost method was used as management believes that the actual cost of construction is most relevant in determining the amount that should be recognized as cost of the intangible asset at each reporting date as opposed to the percentage of completion approach.

The present value of the IRO will be recognized as part of intangible assets upon completion of the Airport Project and to be amortized simultaneously with the cost related to the Airport Project because only at that time would significant maintenance of the Boracay Airport would also commence. However, since the Group had already started the maintenance of the rehabilitated Boracay Airport, the entire present value of the annual estimated costs had already been recognized in CIP — airport concession arrangements and portion of which representing the actual amount incurred in the current year for the maintenance of the Boracay Airport had been recognized as part of the cost of intangible assets and also subjected to amortization.

The present value of the obligation to pay annual franchise fees over 25 years has been immediately recognized as part of intangible assets because the right related to it has already been granted and is already being enjoyed by the Group as evidenced by its taking over the operations of the Boracay Airport during the last quarter of 2010. Consequently, management has started amortizing the related value of the intangible asset and the corresponding obligation has likewise been recognized.

Difference in judgment with respect to the accounting treatment of the transactions would materially affect the assets, liabilities and operating results of the Group.

Toll Road Concession Rights. The Group has assessed that it is covered by Philippine Interpretation IFRIC 12 and qualifies under the intangible asset model with respect to the operation of the toll roads, including the right to verify and audit the toll road revenue, to check the structures and collection facilities and to implement policies and procedures for the operations and management of the toll roads.

Recognition of Profit Margin on the Airport Project Concession Arrangement. The Group has not recognized any profit margin on the construction of the Airport Project as it believes that the fair value of the intangible asset reasonably approximates the cost. The Group also believes that the profit margin of its contractors on the rehabilitation of the existing airport and its subsequent upgrade is enough to cover any difference in the fair value and carrying amount of the intangible asset.

Classification of Redeemable Preferred Shares. Based on the features of TADHC's preferred shares, particularly mandatory redemption, management determined that the shares are in substance a financial liability. Accordingly, it was classified as part of "Other noncurrent liabilities" account in the consolidated statements of financial position (Note 24).

Determining Fair Values of Financial Instruments. Where the fair values of financial assets and financial liabilities recognized in the consolidated statements of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The Group uses judgments to select from a variety of valuation models and make assumptions regarding considerations of liquidity and model inputs such as correlation and volatility for longer dated financial instruments. The input to these models is taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair value.

Contingencies. The Group currently has several tax assessments, legal and administrative claims. The Group's estimate of the probable costs for the resolution of these assessments and claims has been developed in consultation with in-house as well as outside legal counsel handling the prosecution and defense of these matters and is based on an analysis of potential results. The Group currently does not believe that these tax assessments, legal and administrative claims will have a material adverse effect on its financial position and financial performance. It is possible, however, that future financial performance could be materially affected by changes in the estimates or in the effectiveness of strategies relating to these proceedings. No accruals were made in relation to these proceedings (Note 45).

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Estimates and Assumptions

The key estimates and assumptions used in the consolidated financial statements are based upon management's evaluation of relevant facts and circumstances as of the date of the consolidated financial statements. Actual results could differ from such estimates.

Allowance for Impairment Losses on Trade and Other Receivables. Provisions are made for specific and groups of accounts, where objective evidence of impairment exists. The Group evaluates these accounts on the basis of factors that affect the collectibility of the accounts. These factors include, but are not limited to, the length of the Group's relationship with the customers and counterparties, the customers' current credit status based on third party credit reports and known market forces, average age of accounts, collection experience and historical loss experience. The amount and timing of recorded expenses for any period would differ if the Group made different judgments or utilized different methodologies. An increase in allowance for impairment losses would increase the recorded selling and administrative expenses and decrease current assets.

The allowance for impairment losses amounted to ₱6,387 and ₱5,225 as of December 31, 2012 and 2011, respectively. The carrying amounts of trade and other receivables amounted to ₱122,599 and ₱84,472 as of December 31, 2012 and 2011, respectively (Note 10).

Allowance for Inventory Losses. The Group provides an allowance for inventory losses whenever net realizable value becomes lower than cost due to damage, physical deterioration, obsolescence, changes in price levels or other causes.

Estimates of net realizable value are based on the most reliable evidence available at the time the estimates are made of the amount the inventories are expected to be realized. These estimates take into consideration fluctuations of price or cost directly relating to events occurring after the reporting date to the extent that such events confirm conditions existing at the reporting date. The allowance account is reviewed periodically to reflect the accurate valuation in the financial records.

The allowance for inventory losses amounted to ₱1,030 and ₱1,154 as of December 31, 2012 and 2011, respectively. The carrying amount of inventories amounted to ₱80,222 and ₱65,720 as of December 31, 2012 and 2011, respectively (Note 11).

Fair Value of Agricultural Produce. The Group determines the fair value of its agricultural produce based on most recent market transaction price provided that there has been no significant change in economic circumstances between the date of the transactions and the reporting date. Costs to sell are estimated based on the most recent transaction and is deducted from the fair value in order to measure the fair value of agricultural produce at point of harvest.

Unrealized gain on fair valuation of agricultural produce, included in the cost of inventories, amounted to ₱89 and ₱69 in 2012 and 2011, respectively (Note 11).

Financial Assets and Financial Liabilities. The Group carries certain financial assets and financial liabilities at fair value which requires extensive use of accounting estimates and judgments. Significant components of fair value measurement were determined using verifiable objective evidence (i.e., foreign exchange rates, interest rates, volatility rates). The amount of changes in fair value would differ if the Group utilized different valuation methodologies and assumptions. Any change in the fair value of these financial assets and financial liabilities would affect profit or loss and equity.

Fair values of financial assets and financial liabilities are discussed in Note 42.

Estimated Useful Lives of Investment Properties, Property, Plant and Equipment and Deferred Containers. The Group estimates the useful lives of investment properties, property, plant and equipment and deferred containers 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 deferred containers are reviewed periodically and are updated if expectations differ from previous estimates due to physical wear and tear, technical or commercial obsolescence and legal or other limits on the use of the assets.

In addition, estimation of the useful lives of investment properties, property, plant and equipment and deferred containers is based on collective assessment of industry practice, internal technical evaluation and experience with similar assets. It is possible, however, that future financial performance could be materially affected by

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changes in estimates brought about by changes in factors mentioned above. The amounts and timing of recorded expenses for any period would be affected by changes in these factors and circumstances. A reduction in the estimated useful lives of investment properties, property, plant and equipment and deferred containers would increase recorded cost of sales and selling and administrative expenses and decrease noncurrent assets.

Investment properties, net of accumulated depreciation and amortization amounted to ₱3,788 and ₱2,926 as of December 31, 2012 and 2011, respectively (Note 17). Property, plant and equipment, net of accumulated depreciation and amortization amounted to ₱379,794 and ₱330,949 as of December 31, 2012 and 2011, respectively (Note 16). Accumulated depreciation and amortization of investment properties amounted to ₱1,361 and ₱1,536 as of December 31, 2012 and 2011, respectively (Note 17). Accumulated depreciation and amortization of property, plant and equipment amounted to ₱140,657 and ₱111,940 as of December 31, 2012 and 2011, respectively (Note 16).

Deferred containers, net of accumulated amortization, included as part of “Other noncurrent assets” account in the consolidated statements of financial position amounted to ₱6,214 and ₱5,035 as of December 31, 2012 and 2011, respectively (Note 20).

Fair Value of Investment Properties. The fair value of investment properties presented for disclosure purposes is based on market values, being the estimated amount for which the property can be exchanged between a willing buyer and seller in an arm’s length transaction, or based on a most recent sale transaction of a similar property within the same vicinity where the investment property is located.

In the absence of current prices in an active market, the valuations are prepared by considering the aggregate estimated future cash flows expected to be received from leasing out the property. A yield that reflects the specific risks inherent in the net cash flows is then applied to the net annual cash flows to arrive at the property valuation.

Estimated fair values of investment properties amounted to ₱6,078 and ₱5,594 as of December 31, 2012 and 2011, respectively (Note 17).

Estimated Useful Lives of Intangible Assets. The useful lives of intangible assets are assessed at the individual asset level as having either a finite or indefinite life. Intangible assets are regarded to have an indefinite useful life when, based on analysis of all of the relevant factors, there is no foreseeable limit to the period over which the asset is expected to generate net cash inflows for the Group.

Intangible assets with finite useful lives amounted to ₱26,907 and ₱4,121 as of December 31, 2012 and 2011, respectively (Note 19).

Estimated Useful Lives of Intangible Asset — Airport and Toll Road Concession Rights. The Group estimates the useful lives of intangible assets arising from the airport and toll road concession rights based on the period over which the assets are expected to be available for use, which is 25 and 30 years, respectively. The Group has not included any renewal period on the basis of uncertainty as of the reporting date of the probability of securing renewal contract at the end of the original contract term.

Impairment of Goodwill, Licenses and Trademarks and Brand Names with Indefinite Useful Lives. The Group determines whether goodwill, licenses and trademarks and brand names are impaired at least annually. This requires the estimation of the value in use of the cash-generating units to which the goodwill is allocated and the value in use of the licenses and trademarks and brand names. Estimating value in use requires management to make an estimate of the expected future cash flows from the cash-generating unit and from the licenses and trademarks and brand names and to choose a suitable discount rate to calculate the present value of those cash flows.

The carrying amount of goodwill amounted to ₱49,953 and ₱30,990 as of December 31, 2012 and 2011, respectively (Note 19).

The combined carrying amounts of licenses and trademarks and brand names amounted to ₱7,224 and ₱7,286 as of December 31, 2012 and 2011, respectively (Note 19).

Acquisition Accounting. The Group accounts for acquired businesses using the acquisition method of accounting which requires that the assets acquired and the liabilities assumed are recognized at the date of acquisition based on their respective fair values.

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The application of the acquisition method requires certain estimates and assumptions especially concerning the determination of the fair values of acquired intangible assets and property, plant and equipment as well as liabilities assumed at the date of the acquisition. Moreover, the useful lives of the acquired intangible assets and property, plant and equipment have to be determined. Accordingly, for significant acquisitions, the Group obtains assistance from valuation specialists. The valuations are based on information available at the acquisition date.

The Group's acquisitions have resulted in goodwill and other intangible assets with indefinite and finite lives. The combined carrying amounts of goodwill and other intangible assets with indefinite and finite lives arising from business combinations amounted to ₱19,554 and ₱929 in 2012 and 2011, respectively (Notes 5 and 39).

Recoverability of Deferred Exploration and Development Costs. A valuation allowance is provided for estimated unrecoverable deferred exploration and development costs based on the Group's assessment of the future prospects of the mining properties, which are primarily dependent on the presence of economically recoverable reserves in those properties.

The Group's mining activities are all in the exploratory stages as of December 31, 2012. All related costs and expenses from exploration are currently deferred as exploration and development costs to be amortized upon commencement of commercial operations. The Group had not identified any facts and circumstances which suggest that the carrying amount of the deferred exploration and development costs exceeded the recoverable amounts as of December 31, 2012 and 2011.

Deferred exploration and development costs included as part of "Other noncurrent assets" account in the consolidated statements of financial position amounted to ₱232 and ₱103 as of December 31, 2012 and 2011, respectively (Note 20). There were no impairment losses recognized in 2012, 2011 and 2010.

Realizability of Deferred Tax Assets. The Group reviews its deferred tax assets at each reporting date and reduces the carrying amount to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax assets to be utilized. The Group's assessment on the recognition of deferred tax assets on deductible temporary difference and carryforward benefits of MCIT and NOLCO is based on the projected taxable income in the following periods.

Deferred tax assets amounted to ₱8,826 and ₱8,233 as of December 31, 2012 and 2011, respectively (Note 25).

Impairment of Non-financial Assets. PFRS requires that an impairment review be performed on investments and advances, property, plant and equipment, investment properties, deferred containers, biological assets — net of current portion, other intangible assets with finite useful lives and idle assets when events or changes in circumstances indicate that the carrying amount may not be recoverable. Determining the recoverable amounts of these assets requires the estimation of cash flows expected to be generated from the continued use and ultimate disposition of such assets. While it is believed that the assumptions used in the estimation of fair values reflected in the consolidated financial statements are appropriate and reasonable, significant changes in these assumptions may materially affect the assessment of recoverable amounts and any resulting impairment loss could have a material adverse impact on the financial performance.

Accumulated impairment losses on property, plant and equipment and investment properties amounted to ₱9,113 and ₱11,399 as of December 31, 2012 and 2011, respectively (Notes 16 and 17). The combined carrying amounts of investments and advances, property, plant and equipment, investment properties, deferred containers, biological assets — net of current portion, other intangible assets with finite useful lives and idle assets amounted to ₱572,053 and ₱501,284 as of December 31, 2012 and 2011, respectively (Notes 13, 16, 17, 18, 19 and 20).

Present Value of Defined Benefit Obligation. The present value of the retirement liability depends on a number of factors that are determined on an actuarial basis using a number of assumptions. These assumptions are described in Note 36 to the consolidated financial statements and include discount rate, expected return on plan assets and salary increase rate. Actual results that differ from the assumptions are accumulated and amortized over future periods and therefore, generally affect the recognized expense and recorded obligation in such future periods.

The assumption of the expected return on plan assets is determined on a uniform basis, taking into consideration the long-term historical returns, asset allocation and future estimates of long-term investment returns.

The Group determines the appropriate discount rate at the end of each reporting period. It is the interest rate that should be used to determine the present value of estimated future cash outflows expected to be required to settle

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the retirement liabilities. In determining the appropriate discount rate, the Group considers the interest rates on government bonds that are denominated in the currency in which the benefits will be paid. The terms to maturity of these bonds should approximate the terms of the related retirement liability.

Other key assumptions for retirement liabilities are based in part on current market conditions.

While it is believed that the Group's assumptions are reasonable and appropriate, significant differences in actual experience or significant changes in assumptions may materially affect the Group's retirement liabilities.

The Group has net cumulative unrecognized actuarial gain amounting to ₱1,495 and ₱9,348 as of December 31, 2012 and 2011, respectively (Note 36).

Asset Retirement Obligation. The Group has ARO arising from leased service stations, depots, blending plant and franchised store and locator. Determining ARO requires estimation of the costs of dismantling, installations and restoring leased properties to their original condition. The Group determined the amount of ARO by obtaining estimates of dismantling costs from the proponent responsible for the operation of the asset, discounted at the Group's current credit-adjusted risk-free rate ranging from 4.29% to 10.20% depending on the life of the capitalized costs. While it is believed that the assumptions used in the estimation of such costs are reasonable, significant changes in these assumptions may materially affect the recorded expense or obligation in future periods.

The Group also has an ARO arising from its refinery. However, such obligation is not expected to be settled for the foreseeable future and therefore a reasonable estimate of fair value cannot be determined. Thus, the ARO included under "Other noncurrent liabilities" account in the consolidated statements of financial position amounting to ₱997 and ₱1,061 as of December 31, 2012 and 2011, respectively, covers only the Group's leased service stations and depots (Note 24).

Present Value of Annual Franchise Fee and IRO — Airport Concession Arrangements. Part of the amount recognized as intangible asset — airport concession rights as of December 31, 2012 and 2011 pertains to the present value of the annual franchise fee payable to the ROP over the concession period. The recognition of the present value of the IRO is temporarily lodged in CIP — airport concession arrangements until the completion of the Airport Project.

The present values of the annual franchise fee and IRO were determined based on the future value of the obligations discounted at the Group's internal borrowing rate which is believed to be a reasonable approximation of the applicable credit-adjusted risk-free market borrowing rate. The present value of annual franchise fee already recognized in the intangible asset is presented in Note 19 while the carrying amount of IRO recognized in CIP — airport concession arrangements is presented in Note 12. A significant change in such internal borrowing rate used in discounting the estimated cost would result in a significant change in the amount of liabilities recognized with a corresponding effect on profit or loss.

Percentage of Completion — Airport Concession Arrangements. The Group determines the percentage of completion of the contract by computing the proportion of actual contract costs incurred to date, to the latest estimated total Airport Project cost. The Group reviews and revises, when necessary, the estimate of Airport Project cost as it progresses, to appropriately adjust the amount of construction cost and revenue recognized at the end of each reporting period (Note 12).

5. Business Combinations

Fuel and Oil

- ***SRC and Petron***

The Parent Company entered into an option agreement with SEA Refinery Holdings B.V. (SEA BV) (the "Option Agreement") dated December 24, 2008, as amended, on March 4, 2010, pursuant to which SEA BV granted the Parent Company an option to acquire up to 100% of its interests in SEA BV's wholly-owned subsidiary, SRC, consisting of: (i) 16,000,000 common shares of SRC, representing 40% of the outstanding common shares of SRC on or before April 30, 2010; and (ii) 24,000,000 common shares of SRC, representing 60% of the outstanding common shares of SRC on or before December 23, 2010. SRC owns 4,696,885,564 common shares of Petron (representing approximately 50.1% of the outstanding common shares of Petron). The Parent Company conducted a tender offer as a result of its intention to exercise the option to acquire 100% of

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SRC from SEA BV. A total of 184,702,538 Petron common shares tendered were crossed at the PSE on June 8, 2010, which is equivalent to approximately 1.97% of the issued and outstanding common shares of Petron.

On June 15, 2010, the Parent Company executed the Deed of Absolute Sale for the purchase of the 16,000,000 common shares of SRC from SEA BV.

On August 31, 2010, the Parent Company purchased an additional 1,517,637,398 common shares of Petron from SEA BV through a special block sale crossed at the PSE. Said shares comprise approximately 16.188% of the outstanding common shares of Petron.

On October 18, 2010, the Parent Company also acquired from the public a total of 530,624 common shares of Petron, representing approximately 0.006% of the outstanding common shares of Petron.

On December 15, 2010, the Parent Company exercised its option to acquire the remaining 60% of SRC from SEA BV pursuant to the Option Agreement. With the exercise of the option, the Parent Company beneficially owns approximately 68.26% of the outstanding common shares of Petron.

The Group recognized goodwill amounting to ₱22,025 in 2010, as a result of the acquisition (Notes 19 and 39).

• *Petron Malaysia*

On March 30, 2012, the Parent Company through POGI, Petron's indirect offshore subsidiary, completed the acquisition of 65% of Esso Malaysia Berhad (EMB), and 100% of ExxonMobil Malaysia Sdn Bhd (EMMSB) and ExxonMobil Borneo Sdn Bhd (EMBSB) for an aggregate purchase price of US\$577 or ₱25,928. POGI also served the notice of Mandatory General Offer (MGO) to acquire the remaining 94,500,000 shares representing 35% of the total voting shares of EMB for RM3.59 per share from the public. As a result of the MGO, POGI acquired an additional 22,679,063 shares from the public and increased its interest in EMB to 73.4%.

On April 23, 2012, the Companies Commission of Malaysia (CCM) approved the change of name of EMMSB to Petron Fuel International Sdn Bhd and of EMBSB to Petron Oil (M) Sdn Bhd.

On July 11, 2012, CCM approved the change of name of EMB to Petron Malaysia Refining & Marketing Bhd.

From the date of acquisition, Petron Malaysia has contributed revenue of ₱142,190 and profit of ₱120 to the Group's financial performance.

Petron has elected to measure non-controlling interest at proportionate interest in identifiable net assets.

The following summarizes the recognized amounts of assets acquired and liabilities assumed at the acquisition date:

	<u>2012</u>
Assets	
Cash and cash equivalents	₱ 5,633
Trade and other receivables — net	12,811
Inventories	13,160
Prepaid expenses and other current assets	307
Property, plant and equipment — net	14,930
Deferred tax assets	36
Other noncurrent assets — net	6,488
Liabilities	
Loans payable	(4,195)
Accounts payable and accrued expenses	(18,294)
Income and other taxes payable	(64)
Long-term debt — net of debt issue cost	(10,123)
Deferred tax liabilities	(1,116)
Other noncurrent liabilities	(700)
Total Identifiable Net Assets at Fair Value	₱ 18,873

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The fair value of the trade and other receivables amounts to ₱12,811. The gross amount of trade receivables is ₱12,857, of which ₱46 is expected to be uncollectible at the acquisition date (Note 10).

Goodwill was recognized based on the provisional amounts of net assets acquired as follows:

	<u>Note</u>	<u>2012</u>
Total cash consideration transferred		₱ 25,928
Non-controlling interest measured at proportionate interest in identifiable net assets		3,584
Total identifiable net assets at fair value		(18,873)
Goodwill	19, 39	₱ 10,639

Movement of goodwill is as follows:

	<u>Note</u>	<u>2012</u>
Goodwill at acquisition date		₱10,639
Translation adjustments		(439)
Goodwill at end of year	19	₱10,200

Goodwill arising from the acquisition is attributable to the benefit of expected synergies, revenue growth, future market development and the assembled workforce of Petron. These benefits are not recognized separately from goodwill because they do not meet the recognition criteria for identifiable intangible assets.

The Group is currently completing the purchase price allocation exercise on the acquisition of Petron Malaysia. The identifiable net assets at fair value are based on provisional amounts as at the acquisition date, which is allowed under PFRS 3, within 12 months from the acquisition date.

• **LEC**

On August 3, 2010, Petron together with Two San Isidro SIAI Assets, Inc. (Two San Isidro), formed LEC with an authorized capital stock of ₱3,400. Out of its authorized capitalization, ₱850 was subscribed, of which ₱213 was paid-up by Petron. Petron then owned 40% of LEC, while Two San Isidro owned the remaining 60%. In 2011, Petron infused ₱1,147 into LEC to fully pay its 40% equity share.

In January 2012, LEC became a wholly-owned subsidiary of Petron when it purchased the 60% equity share of Two San Isidro.

The primary purpose of LEC is to build, operate, maintain, sell and lease power generation plants, facilities, equipment and other related assets and generally engage in the business of power generation and sale of electricity generated by its facilities.

From the date of acquisition, LEC has contributed profit of ₱28 to the Group's financial performance.

The following summarizes the recognized amounts of assets acquired and liabilities assumed at the acquisition date:

	<u>2012</u>
Assets	
Cash and cash equivalents	₱3,514
Trade and other receivables	2
Prepaid expenses and other current assets	39
Other noncurrent assets — net	35
Liabilities	
Accounts payable and accrued expenses	(10)
Income and other taxes payable	(144)
Total Identifiable Net Assets at Fair Value	₱3,436

The fair value of the trade and other receivables amounts to ₱2. None of the receivables has been impaired and it is expected that the full amount can be collected.

Total identifiable net assets at fair value is equal to the consideration of the purchase made by Petron.

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• *Parkville Estates Development Corp. (PEDC)*

In April 2012, the Parent Company through NVRC, a subsidiary of Petron, acquired 100% of the outstanding capital stock of PEDC for a total consideration of ₱132.

The following summarizes the recognized amounts of the asset acquired and liabilities assumed at the acquisition date:

	<u>2012</u>
Asset	
Property, plant and equipment — net	₱117
Liabilities	
Accounts payable and accrued expenses	(5)
Total Identifiable Net Asset at Fair Value	<u>₱112</u>

Goodwill was recognized based on the provisionary amounts of net asset acquired as follows:

	<u>Note</u>	<u>2012</u>
Total cash consideration transferred		₱ 132
Total identifiable net asset at fair value		(112)
Goodwill	19, 39	<u>₱ 20</u>

• *Mariveles Landco Corporation (MLC)*

On July 26, 2012, the Parent Company, through NVRC, a subsidiary of Petron, acquired 60% of MLC's shares of stock for a total consideration of ₱30.

NVRC has elected to measure non-controlling interest at proportionate interest in identifiable net assets.

The following summarizes the recognized amounts of assets acquired and liabilities assumed at the acquisition date:

	<u>2012</u>
Assets	
Trade and other receivables	₱10
Prepaid expenses and other current assets	2
Property, plant and equipment — net	64
Liabilities	
Accounts payable and accrued expenses	(58)
Other noncurrent liabilities	(36)
Total Identifiable Net Liabilities at Fair Value	<u>(₱18)</u>

The fair value of the trade and other receivables amounts to ₱10. None of the receivables has been impaired and it is expected that the full amount can be collected.

Goodwill was recognized based on the provisionary amounts of net liabilities acquired as follows:

	<u>Note</u>	<u>2012</u>
Total cash consideration transferred		₱30
Non-controlling interest measured at proportionate interest in identifiable net liabilities		(7)
Total identifiable net liabilities at fair value		18
Goodwill	19, 39	<u>₱41</u>

Infrastructure

• *THI and CMMTC*

On December 28, 2012, the Parent Company, through its wholly-owned subsidiary, SMHC, acquired 100% of the outstanding capital stock of THI for ₱3.

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THI has 37.33% equity interest in CMMTC, a company primarily engaged in the business of designing, constructing and financing of toll roads. CMMTC holds the toll road concession rights representing the costs of construction and development of Stage 1 and Stage 2 of the SMMS. In addition, pursuant to a build-and-transfer scheme duly approved by the appropriate Philippine Authorities, two major infrastructure projects have been designated as “flagship” or preferred infrastructure projects by CMMTC, namely: (1) the proposed Metro Manila Skyway (MMS) which is a system of elevated roadway, commencing at the end-point of the South Luzon Expressway (SLEX) in Alabang, Muntinlupa, and culminating at the end-point of the North Luzon Expressway in Balintawak, Calocan City, thereby serving as an interconnection of the above-mentioned expressways; and (2) the proposed Metro Manila Tollways (or Circumferential Road 6 or simply C-6).

THI also has 100% equity interest in Assetvalues Holding Company Inc. (AVHCI). AVHCI is engaged in the business of investing in real and personal properties, stocks, bonds and other securities or evidence of indebtedness of any corporation, association or entity. AVHCI has 15.43% equity interest in Skyway O&M Corporation (SOMCO), the operator of SMMS.

An option agreement was entered into by SMHC, Padma Fund L.P. (Padma) and THI wherein Padma, or its nominated assignee, obtained the rights to purchase and acquire up to 49% equity ownership interest in THI. The option is exercisable within 2 years from the acquisition by SMHC of all the outstanding shares of THI or until December 28, 2014. The option price paid by Padma amounting to US\$0.25 or ₱10 is presented as part of “Other noncurrent liabilities” account in the 2012 consolidated statement of financial position.

With the acquisition of THI, which owns 37.33% of the outstanding capital stock of CMMTC, and the existing 23.5% indirect ownership in CMMTC through Atlantic, SMHC obtained control and consolidated CMMTC effective December 28, 2012.

SMHC has elected to measure non-controlling interest at proportionate interest in identifiable net assets.

The following summarizes the recognized amounts of assets acquired and liabilities assumed at the acquisition date:

	<u>2012</u>
Assets	
Cash and cash equivalents	₱ 2,785
Trade and other receivables — net	259
Prepaid expenses and other current assets	290
Investments and advances	13,970
Property, plant and equipment — net	14
Investment properties — net	1
Other intangible assets — net	20,601
Other noncurrent assets	2
Liabilities	
Loans payable	(11,158)
Accounts payable and accrued expenses	(665)
Income and other taxes payable	(546)
Current maturities of long-term debt — net of debt issue costs	(1,692)
Long-term debt — net of current maturities and debt issue costs	(6,796)
Deferred tax liabilities	(331)
Other noncurrent liabilities	(2,780)
Total Identifiable Net Assets at Fair Value	₱ 13,954

The fair value of the trade and other receivables amounts to ₱259. The gross amount of trade receivables is ₱758, of which ₱499 is expected to be uncollectible at the acquisition date (Note 10).

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Goodwill was recognized as a result of the acquisition as follows:

	<u>Note</u>	<u>2012</u>
Total cash consideration transferred		P 3
Investment cost of THI		13,922
Equity interest held before business combination		3,236
Total consideration transferred		17,161
Non-controlling interest measured at proportionate interest in identifiable net assets		5,393
Total identifiable net assets at fair value		(13,954)
Goodwill	19, 39	P 8,600

• **AMTEX**

In February 2012, the Parent Company through its wholly-owned subsidiary, SMHC, acquired 60% of the outstanding capital stock of AMTEX for a total consideration of P90. AMTEX is a company engaged in the business of operating and maintaining toll road facilities and providing related services such as technical advisory services in the operation and maintenance of toll road and toll road facilities.

With the acquisition of the 60% equity interest by SMHC and the existing 18.61% indirect ownership through Atlantic, the Group effectively owns 78.61% of AMTEX and consolidated AMTEX effective February 2012.

From the date of acquisition, AMTEX has contributed profit of P36 to the Group's financial performance.

SMHC has elected to measure non-controlling interest at proportionate interest in identifiable net assets.

The following summarizes the recognized amounts of assets acquired and liabilities assumed at the acquisition date:

	<u>2012</u>
Assets	
Cash and cash equivalents	P 22
Trade and other receivables — net	6
Prepaid expenses and other current assets	17
Investments and advances	120
Property, plant and equipment — net	2
Investment properties — net	71
Deferred tax assets	1
Liabilities	
Accounts payable and accrued expenses	(94)
Other noncurrent liabilities	(40)
Total Identifiable Net Assets at Fair Value	P105

The fair value of the trade and other receivables amounts to P6. None of the receivables has been impaired and it is expected that the full amount can be collected.

Goodwill was recognized as a result of the acquisition as follows:

	<u>Note</u>	<u>2012</u>
Total cash consideration transferred		P 90
Non-controlling interest measured at proportionate interest in identifiable net assets		42
Total identifiable net assets at fair value		(105)
Goodwill	19, 39	P 27

• **ULC BVI**

In 2010, the Parent Company, through its wholly-owned subsidiary, SMHC, signed a Share Sale and Purchase Agreement (the "Agreement") with ULC BVI, pursuant to the authority of the BOD of the Parent Company. Under the terms of the Agreement, SMHC acquired 51% equity interest in ULC BVI, the corporation which

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holds the exclusive right, obligation and privilege to finance, design, construct, supply, complete and commission the Metro Rail Transit Line 7 Project (the MRT 7 Project) by virtue of the CA dated June 18, 2008 with the ROP, through the Department of Transportation and Communications (DOTC) (Note 35). Closing of the Agreement was held on November 8, 2010.

The Group recognized goodwill amounting to ₱1,464 in 2010, as a result of the acquisition (Notes 19 and 39).

• *TADHC*

In 2010, the Parent Company, through its wholly-owned subsidiary, SMHC, executed a Share Sale and Purchase Agreement relating to the purchase of the rights, title and interests to a total of 2,025,000 common shares of CIADC (the CIADC Shares). Deeds of Assignment of Shares were executed covering the CIADC Shares. SMHC paid ₱855 for the acquisition of CIADC Shares, of which the balance of ₱170 is payable as follows: (i) ₱100, two years after the closing of the transaction; and (ii) ₱70, one year from the date of the previous payment.

CIADC (currently TADHC) holds the exclusive rights, obligations and privileges to finance, design, construct, operate and maintain the Boracay Airport by virtue of the CA, dated June 22, 2009, with the ROP, through the DOTC and the Civil Aviation Authority (Note 35).

The current portion of the Group's outstanding payable related to the purchase amounting to ₱70 and ₱100 as of December 31, 2012 and 2011, respectively, is included under "Accounts payable and accrued expenses" account (Note 22), while the noncurrent portion amounting to ₱70 as of December 31, 2011, is reported as part of "Other noncurrent liabilities" account in the consolidated statements of financial position (Note 24).

The Group recognized goodwill amounting to ₱967 in 2010, as a result of the acquisition (Notes 19 and 39).

Telecommunications

• *AGNP*

In 2010, the Parent Company through its wholly-owned subsidiary, Vega, executed a Share Purchase Agreement (the "Agreement") with ISM Communications Corporation (ISM Corp.), for the purchase of 100% of the outstanding and issued shares of stock of AGNP for ₱1,600.

AGNP is the registered and beneficial owner of approximately 40% of ETPI. ETPI's products and services included wireless access, services for high-end internet cafes, a new data center, business application and special packages for small and medium enterprises and corporations, besides the traditional bandwidth and connectivity solutions. The acquisition of ETPI through AGNP, would complement the internet broadband service of Liberty Telecoms Holdings, Inc. (LTHI), in which the Group holds 41.48% interest.

Upon the signing of the Agreement, Vega paid ₱320 as initial payment. Under the Agreement, the outstanding balance of ₱1,280 is payable in two installments. The first payment amounting to 50% of the outstanding balance was paid on December 29, 2011.

The current portion of the Group's outstanding payable related to the purchase of AGNP shares amounting to ₱640 as of December 31, 2012 and 2011, is included as part of "Accounts payable and accrued expenses" account in the consolidated statements of financial position (Note 22).

Total identifiable assets at fair value on the acquisition date pertains to its investment in ETPI amounting to ₱1,600, which is also equal to the total consideration of the purchase made by Vega.

• *SMESI*

On March 28, 2011, the Parent Company incorporated SMESI, a wholly-owned subsidiary, with an initial authorized capital stock of ₱100 divided into 100,000,000 shares and paid-up capital of ₱25.

• *ETPI*

On October 20, 2011, the Parent Company through its wholly-owned subsidiary, SMESI, executed a Share Purchase Agreement (the Agreement) with ISM Corp., for the purchase of 37.7% of the outstanding and issued shares of stock of ETPI for ₱1,508. The acquisition of ETPI was authorized by the BOD of the Parent Company during the meetings held on December 16, 2010 and September 22, 2011.

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Upon signing of the Agreement, SMESI paid ₱302 as initial payment. Under the Agreement, the outstanding balance of ₱1,206 is payable in two installments. The first payment amounting to ₱98 is payable no earlier than December 31, 2012 while the remaining balance is to be settled no earlier than December 31, 2013.

The current portion of the Group's outstanding payable related to the purchase of ETPI shares amounting to ₱98 as of December 31, 2012 is included as part of "Accounts payable and accrued expenses" account (Note 22) while the noncurrent portion amounting to ₱1,108 and ₱1,206 as of December 31, 2012 and 2011, respectively, is included as part of "Other noncurrent liabilities" account in the consolidated statements of financial position (Note 24).

With the acquisition of the 37.7% by SMESI and of the 40% ownership by AGNP, the Parent Company obtained control and consolidated ETPI effective October 20, 2011.

The following summarizes the recognized amounts of assets acquired and liabilities assumed at the acquisition date:

	<u>2011</u>
Assets	
Cash and cash equivalents	₱ 415
Trade and other receivables — net	371
Inventories	19
Prepaid expenses and other current assets	100
Available-for-sale financial assets	4
Property, plant and equipment — net	2,582
Other noncurrent assets	229
Liabilities	
Accounts payable and accrued expenses	(412)
Income and other taxes payable	(119)
Deferred tax liabilities	(91)
Total Identifiable Net Assets At Fair Value	<u>₱3,098</u>

The fair value of the trade and other receivables amounts to ₱371. The gross amount of trade receivables is ₱439, of which ₱68 is expected to be uncollectible at the acquisition date (Note 10).

Goodwill was recognized as a result of the acquisition as follows:

	<u>Note</u>	<u>2011</u>
Cash		₱ 302
Deferred consideration		1,206
Equity interest held before business combination	13	1,625
Total consideration transferred		3,133
Non-controlling interest measured at proportionate interest in identifiable net assets		691
Total identifiable net assets at fair value		(3,098)
Goodwill	19, 39	<u>₱ 726</u>

Goodwill arising from the acquisitions is attributable to the benefit of expected synergies with the Group's telecommunication business, revenue growth, and future development. None of the goodwill recognized is expected to be deductible for tax purposes.

• *TCCI, PHC and PSCL*

In 2010, the Parent Company through its wholly-owned subsidiary, Vega, completed the acquisition of 100% equity interests in TCCI, PHC and PSCL, which collectively own 100% of the outstanding capital stock of BellTel.

BellTel is a grantee of a franchise to install, operate and maintain local exchange networks and Wireless Local Loop (WLL) in several areas including special economic zones, inter-exchange networks, nationwide Very Small Aperture Terminal (VSAT) network, international gateway facilities and cellular mobile telecommunications network (Note 35).

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The Group recognized other intangible assets — license amounting to ₱5,221 in 2010, as a result of the acquisition (Notes 19 and 39).

Food

• *GAC*

In June 2012, following the approval of its BOD, SMMI, a wholly-owned subsidiary of SMPFC, acquired from CRC's individual stockholders, the subscribed capital stock of CRC equivalent to 25,000 shares for ₱358. CRC is a Philippine company engaged in the purchase, acquisition, development or use for investment, among others, of real and personal property, to the extent permitted by law. As such, CRC became a subsidiary of SMMI and was consolidated into SMPFC through SMMI.

The following summarizes the recognized amounts of the asset acquired and liabilities assumed at the acquisition date:

	<u>2012</u>
Asset	
Property, plant and equipment — net	₱400
Liabilities	
Accounts payable and accrued expenses	<u>(42)</u>
Total identifiable net asset at fair value	<u>₱358</u>

Total identifiable net assets at fair value, is equal to the consideration of the purchase made by SMMI.

Subsequently, SMMI subscribed to an additional 45,000 CRC shares with a par value of ₱1,000.00 per share and paid ₱45.

In December 2012, following the approval of the BOD and stockholders of CRC to change the latter's corporate name, the SEC issued the Certificates of Filing of Amended Articles of Incorporation and Amended By-laws reflecting the change in corporate name of CRC to Golden Avenue Corp.

• *GFDCC*

In September 2011, the Parent Company through Magnolia, a wholly-owned subsidiary of SMPFC, acquired the subscription rights of certain individuals in GFDCC for ₱105. GFDCC is a company engaged in the toll manufacturing of ice cream products. As such, GFDCC became a subsidiary and was consolidated into SMPFC through Magnolia.

The following summarizes the recognized amounts of assets acquired and liabilities assumed at the acquisition date:

	<u>2011</u>
Assets	
Cash and cash equivalents	₱ 7
Trade and other receivables — net	25
Prepaid expenses and other current assets	37
Property, plant and equipment — net	308
Liabilities	
Accounts payable and accrued expenses	(22)
Current maturities of long-term debt — net of debt issue costs	(25)
Long-term debt — net of current maturities and debt issue costs	(185)
Other noncurrent liabilities	<u>(46)</u>
Total Identifiable Net Assets at Fair Value	<u>₱ 99</u>

The fair value of the trade and other receivables amounts to ₱25. None of the receivables has been impaired and it is expected that the full amount can be collected.

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Goodwill was recognized as a result of the acquisition as follows:

	<u>Note</u>	<u>2011</u>
Total cash consideration transferred		P 105
Total identifiable net assets at fair value		(99)
Goodwill	19, 39	<u><u>P 6</u></u>

Beverage

• *EPSBPI*

On January 27, 2012, the Parent Company, through its subsidiary, GSMI, acquired 100% of the outstanding capital stock of EPSBPI for P200. EPSBPI is a company primarily engaged in the manufacturing and bottling of alcoholic and non-alcoholic beverages.

From the date of acquisition, EPSBPI has contributed loss of P35 to the Group's financial performance.

The following summarizes the recognized amounts of assets acquired and liabilities assumed at the acquisition date:

	<u>2012</u>
Assets	
Cash and cash equivalents	P 57
Trade and other receivables — net	18
Inventories	4
Prepaid expenses and other current assets	24
Property, plant and equipment — net	1,063
Other noncurrent assets	97
Liabilities	
Accounts payable and accrued expenses	(489)
Long-term debt	(800)
Deferred tax liabilities	(1)
Total Identifiable Net Liabilities at Fair Value	<u><u>(P27)</u></u>

The fair value of the trade and other receivables amounts to P18. None of the receivables has been impaired and it is expected that the full amount can be collected.

Goodwill was recognized as a result of the acquisition as follows:

	<u>Note</u>	<u>2012</u>
Total consideration transferred		P200
Total identifiable net liabilities at fair value		27
Goodwill	19, 39	<u><u>P227</u></u>

Goodwill arising from the acquisition is attributable to the benefit of expected synergies with the Group's beverage business, revenue growth, and future development specifically on tolling services with third parties.

Power Generation and Distribution

• *SMC Global*

On August 9, 2010, the Parent Company subscribed to the remaining unissued common shares of SMC Global equivalent to 75% ownership interest for P3,240. A bargain purchase gain amounting to P4,490 was recognized as a result of the acquisition and presented as part of "Other income (charges)" account in the 2010 consolidated statement of income (Note 33).

• *Acquisition of Non-controlling Interests*

On September 3 and 8, 2010, the Parent Company acquired the remaining 25% ownership in SMC Global, making it a wholly-owned subsidiary. A cash consideration of P1,080 was paid to the non-controlling interest

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shareholders. The carrying amount of SMC Global's net assets on the date of acquisition was ₱10,111, and the carrying amount of the additional interest acquired was ₱2,528. The difference of ₱1,448 between the consideration and the carrying amount of the interest acquired has been recognized in "Revaluation increment" account in the consolidated statements of changes in equity.

• ***SMEC, PanAsia, SPPC and SPDC***

On May 17, 2010, the BOD of the Parent Company approved the sale of its entire 40% ownership interest in SMEC and SPDC and 100% ownership in PanAsia and SPPC. On September 21, 2010, the Parent Company and SMC Global executed a Deed of Absolute Sale of Shares whereby the former's entire interest in SMEC, PanAsia, SPPC and SPDC were sold for a total price of ₱7.15. Following such sale, SMEC, PanAsia, SPPC and SPDC became wholly-owned subsidiaries of SMC Global.

On June 17, 2011, the BOD of SMC Global approved the sale of its 100% ownership interest in PanAsia to Millenium Holdings, Inc. (MHI). On June 24, 2011, SMC Global signed a Share Purchase Agreement with MHI subject to certain closing conditions, which includes among others, the Board of Investments (BOI) approval of the transaction. The approval by the BOI was obtained on August 18, 2011. The Group recognized a gain of ₱278 for the said sale, presented as part of "Gain on sale of investments and property and equipment" account in the consolidated statements of income.

An initial payment of ₱25 was received by SMC Global in 2011 and the balance of ₱600 was recognized at present value discounted at applicable rate of similar instruments. As of December 31, 2012, the current portion of the receivable amounting to ₱98 is included as part of "Trade and other receivable — net" account (Note 10) and the noncurrent portion amounting to ₱396 is included as part of "Other noncurrent assets" account in the consolidated statements of financial position (Note 20). The discount is amortized over the collection period and recognized as part of "Interest income" account in the consolidated statements of income. Interest income amounted to ₱21 and ₱7 in 2012 and 2011, respectively.

• ***Coal Mining Companies***

On various dates in 2010, SMEC acquired 100% ownership interest in Daguma Agro-Minerals, Inc. (DAMI), Bonanza Energy Resources, Inc. (BERI) and Sultan Energy Phils. Corp. (SEPC). DAMI, BERI and SEPC are mining companies with coal properties covered by Coal Operating Contract (COC) No. 126, COC No. 138 and COC No. 134, respectively, issued by the Department of Energy (DOE). The COCs of these entities met the contractual/legal criterion and qualified as intangible assets under PFRS 3. Accordingly, the Group recognized other intangible asset — mining rights amounting to ₱1,719 in 2010 as a result of the acquisition (Notes 19 and 39).

As of December 31, 2012, DAMI, SEPC and BERI are in the exploratory stages of their mining activities. All related costs and expenses from exploration are currently recognized as deferred exploration and development costs to be amortized upon commencement of commercial operations included as part of "Other noncurrent assets" account in the consolidated statements of financial position (Note 20).

The Group had not identified any facts and circumstances which suggest that the carrying amount of the deferred exploration and development costs exceeds recoverable amounts as of December 31, 2012.

Mining

• ***Clariden***

On November 11, 2011, the Parent Company acquired 100% of the outstanding capital stock of Clariden for a total consideration of ₱5. Clariden's primary purpose is to acquire by purchase, exchange, assignment or otherwise, and to sell, assign, transfer, exchange, lease, let, develop, mortgage, pledge, deal in and operate, enjoy and dispose of, all properties of every kind and description and whenever situated and to the extent permitted by law.

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The following summarizes the recognized amounts of assets acquired and liabilities assumed at the acquisition date:

	<u>2011</u>
Assets	
Cash and cash equivalents	P 36
Trade and other receivables	41
Investments and advances — net	274
Liabilities	
Accounts payable and accrued expenses	(16)
Other noncurrent liabilities	(527)
Total Identifiable Net Liabilities at Fair Value	<u>(P 192)</u>

The fair value of the trade and other receivables amounts to P41. None of the receivables has been impaired and it is expected that the full amount can be collected.

Mining rights were recognized as a result of the acquisition as follows:

	<u>Note</u>	<u>2011</u>
Total cash consideration transferred		P 5
Total identifiable net liabilities at fair value		192
Other Intangible Asset — Mining Rights	19, 39	<u>P197</u>

• *AAMRC*

On September 6, 2012, the Parent Company, through its wholly-owned subsidiary, Clariden, acquired 1,140,000 shares representing 60% ownership of the outstanding capital stock of AAMRC for a total consideration of P275. AAMRC is a company primarily engaged in the business of operating iron mines, and of prospecting, exploration and mining, milling, concentrating, smelting, treating, refining and processing of metals for market.

From the date of acquisition, AAMRC has contributed loss of P0.28 to the Group's financial performance.

The following summarizes the recognized amounts of assets acquired at the acquisition date:

	<u>2012</u>
Assets	
Trade and other receivables — net	P 70
Other noncurrent assets	233
Total Identifiable Assets at Fair Value	<u>P303</u>

The fair value of the trade and other receivables amounts to P70. None of the receivables has been impaired and it is expected that the full amount can be collected.

Real Estate

• *SMPI Flagship*

The Parent Company, through SMPI, entered into a Joint Venture Agreement (JVA) with GSIS to establish the SMPI-GSIS JVC which holds ownership and title to the real property owned by GSIS primarily to develop the property into a first class high-rise service apartment and manage and operate the same.

Under the JVA, GSIS has the option to sell to SMPI all the shares of stock of the SMPI-GSIS JVC issued in the name of GSIS and its nominees under certain terms and conditions (Note 35).

On June 7, 2011, GSIS exercised its option by executing a Deed of Absolute Sale over all its shares of stock representing 48% equity in the SMPI-GSIS JVC in favor of SMPI. The total consideration for the sale amounted to P399. As such, SMPI-GSIS JVC became a wholly-owned subsidiary of SMPI.

On March 12, 2012, the BOD of SMPI-GSIS JVC approved the change in corporate name to SMPI Makati Flagship Realty Corp. The SEC approved the change in corporate name in January 2013.

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Others

• ***KCSLI***

On May 26, 2011, SMCSLC executed an Asset and Share Purchase Agreement relating to the purchase of 100% of the issued shares of KCSLI through which SMCSLC obtained an indirect ownership over a parcel of land, certain fixed assets, foreshore leases and land use rights.

On August 18, 2011, SMCSLC incorporated MSC. MSC's primary purpose is to engage in the business of construction, building, fabrication, repair, conversion or extension of ships, boats and other kinds of vessels and marine equipment, machineries and structures including offshore rigs. MSC leases the land owned by KCSLI.

The following summarizes the recognized amounts of assets acquired at the acquisition date:

	<u>2011</u>
Assets	
Cash and cash equivalents	P 5
Property, plant and equipment — net	<u>821</u>
Total Identifiable Assets at Fair Value	<u>P826</u>

Total identifiable assets at fair value on the acquisition date, is equal to the consideration of the purchase made by SMCSLC.

On May 23, 2012, the SEC approved the change in corporate name of Keppel Cebu Shipyard Land, Inc. to SMC Cebu Shipyard Land, Inc.

If the foregoing acquisitions have occurred on January 1, 2012, management estimates that consolidated revenue would have been P753,108, and consolidated net income for the year would have been P43,228. In determining these amounts, management has assumed that the fair value adjustments, determined provisionally, that arose on the date of acquisition would have been the same if the acquisition had occurred on January 1, 2012.

6. Investments in Subsidiaries

The following are the developments relating to the Parent Company's investments in subsidiaries in 2012 and 2011:

Fuel and Oil

• ***PGL***

On February 24, 2012, the Parent Company through Petron, acquired PGL, a company incorporated in the British Virgin Islands. PGL has issued an aggregate of 31,171,180 common shares with a par value of US\$1.00 per share to Petron. PGL issued 150,000,000 cumulative, non-voting, non-participating and non-convertible preferred shares series A and 200,000,000 cumulative, non-voting, non-participating and non-convertible preferred shares series B at an issue price equal to the par value of each share of US\$1.00 to a third party investor.

Infrastructure

• ***SMHC***

On April 13, 2012, the BOD and stockholders of SMHC resolved and approved the increase in authorized capital stock from P1,000 divided into 1,000,000 shares to P5,000 divided into 5,000,000 shares, both with a par value of P1,000.00 per share. The application for the Amendment of Articles of Incorporation for the increase in authorized capital stock was filed with the SEC on December 28, 2012 and was approved on February 11, 2013.

• ***TADHC***

On September 7, 2012, the BOD and stockholders of TADHC resolved and approved the increase in authorized capital stock from P810 divided into 7,900,000 common shares and 200,000 preferred shares, both with a par value of P100.00 per share, to P1,520 divided into 15,000,000 common shares and 200,000 preferred shares, both with a par value of P100.00 per share. The request for the Amendment of Articles of Incorporation for the increase in authorized capital stock was filed with the SEC on December 28, 2012 and was approved on February 25, 2013.

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On October 30, 2012, SMHC executed a Subscription Agreement with TADHC for the subscription of additional 5,840,724 common shares out of the existing shares. Total subscription paid amounted to ₱728 which also includes full settlement of previous subscription amounting to ₱144. SMHC also paid ₱124 as advances for the subscription of additional 1,775,000 common shares from the increase in capital stock of TADHC under the Subscription Agreement.

Food

• ***SMPFC***

a) **Issuance of Preferred Shares**

On January 20, 2011, the SEC favorably considered SMPFC's Registration Statement covering the registration of 15,000,000 preferred shares with a par value of ₱10.00 per share.

On January 26, 2011, the PSE approved, subject to certain conditions, the application of SMPFC to list up to 15,000,000 preferred shares with a par value of ₱10.00 per share to cover SMPFC's follow-on preferred shares offering at an offer price of ₱1,000.00 per share and with a dividend rate determined by management on the dividend rate setting date.

On February 10, 2011, the SEC issued the order for the registration of SMPFC's 15,000,000 preferred shares with a par value of ₱10.00 per share and released the Certificate of Permit to Offer Securities for Sale.

On February 11, 2011, SMPFC's BOD approved the terms of the preferred shares offer (Terms of the Offer) and the amendment of the Articles of Incorporation of SMPFC to reflect the additional optional redemption features of the preferred shares to align with the Terms of the Offer. The stockholders of SMPFC approved the said amendment during its annual meeting on May 13, 2011.

A summary of the Terms of the Offer is set out below.

SMPFC, through the underwriters and selling agents, offered 15,000,000 cumulative, non-voting, non-participating and non-convertible preferred shares at an offer price of ₱1,000.00 per share during the period from February 14 to 25, 2011. The dividend rate was set at 8% per annum with dividend payment dates on March 3, June 3, September 3 and December 3 of each year calculated on a 30/360-day basis, as and if declared by the BOD. The preferred shares are redeemable in whole or in part, in cash, at the sole option of SMPFC, at the end of the 5th year from issuance date or on any dividend payment date thereafter, at the price equal to the issue price plus any accumulated and unpaid cash dividends. Optional redemption of the preferred shares prior to the 5th year from issuance date was provided under certain conditions (i.e., accounting, tax or change of control events). Unless the preferred shares are redeemed by SMPFC on its 5th year anniversary, the dividend rate shall be adjusted thereafter to the higher of the dividend rate of 8% or the ten-year PDST-F rate prevailing on the optional redemption date plus 3.33% per annum.

On March 3, 2011, SMPFC's 15,000,000 preferred shares with par value of ₱10.00 per share were listed with the PSE.

On June 2, 2011, the SEC issued the Certificate of Filing of Amended Articles of Incorporation approving the additional redemption features of the preferred shares of SMPFC.

b) **Investment in Manila Electric Company (Meralco)**

In August 2011, SMPFC entered into a Share Purchase Agreement with the Parent Company covering the sale by the latter of its 5.2% shareholdings in Meralco comprising of 59,090,909 common shares for a total consideration of ₱13,000 (Note 13).

c) **Secondary offering of SMPFC common shares**

On November 23, 2012, the Parent Company completed the secondary offering of a portion of its common shares in SMPFC following the crossing of such shares at the PSE on November 21, 2012. The offer consisted of 25,000,000 common shares, inclusive of an over-allotment of 2,500,000 common shares at a price of ₱240.00 per share (the "Offer Shares"). The Offer Shares were offered and sold to Maybank ATR Kim Eng Capital Partners, Inc., Standard Chartered Securities (Singapore) Pte. Limited and UBS AG, Hong Kong Branch. The Parent Company granted UBS AG an option, exercisable in whole or in part for 30 days

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from and including the Closing date, to procure purchasers for or purchase up to 2,500,000 additional common shares (approximately 11% of the total number of Offer Shares), solely to cover over-allotments under the offer, if any. The option was exercised by UBS AG within the allowable period. The Group recognized a net gain of ₱2,419 from the offering, presented as part of “Gain on sale of investments and property and equipment” account in the consolidated statements of income.

The completion of the secondary offering resulted in the increase of SMPFC’s public ownership from 0.08% to 15.08% of its outstanding common shares.

- ***SMPFIL***

In July 2010, the Parent Company, through its wholly-owned subsidiary, SMFBIL, sold to SMPFIL, a wholly-owned subsidiary of SMPFC, its 51% interest in SMPFI for US\$18.6. SMPFI owns 100% of SMPFVN. In May 2011, SMPFC increased its investment in SMPFIL amounting to US\$16.8.

As approved by the State Securities Commission of Vietnam on September 30, 2011, SMPFVN was renamed to San Miguel Hormel (Vn) Co., Ltd.

- ***SMFI***

In August 2010, the SEC approved the merger of Monterey Foods Corporation (Monterey) into SMFI, with SMFI as the surviving corporation, following the approvals of the merger by the respective BOD and stockholders of Monterey and SMFI in June 2010 and July 2010, respectively. The merger became effective on September 1, 2010. SMFI’s request for confirmation of the tax-free merger, filed in September 2010, is still pending with the Bureau of Internal Revenue (BIR) as of March 21, 2013.

In April 2012, SMPFC transferred to SMFI, a 99.97% — owned subsidiary of SMPFC, its food service business under the Great Food Solutions division. Total net assets transferred amounted to ₱289.

- ***SMMI***

In September 2011, the Parent Company, through SMMI, a wholly-owned subsidiary of SMPFC, formed GBGTC with an authorized capital stock of ₱2,000. GBGTC is a Philippine company with the purpose of providing and rendering general services connected with and incidental to the operation and management of port terminals engaged in handling and/or trading grains, among others.

In November 2011, following the approval by the SEC of the incorporation of GBGTC, SMMI subscribed to 5,000,000 GBGTC shares for a total subscription value of ₱500 and paid an initial consideration amounting to ₱125.

In February and April 2012, SMMI paid in full the remaining balance of the subscription value amounting to an aggregate of ₱375.

In July 2012, SMMI subscribed to an additional 7,000,000 GBGTC shares with a par value of ₱100.00 per share. Total payment made by SMMI for the additional subscription amounted to ₱500 as of December 31, 2012.

GBGTC has not yet started commercial operations as of December 31, 2012.

Beverage

- ***SMB***

Following the SEC’s denial of all requests made (including the request of SMB) for the extension of the grace period for listed companies to comply with the PSE’s minimum public ownership and the PSE’s imposition of a trading suspension on the common shares of SMB effective January 1, 2013 as a result of such denial, the BOD of SMB approved on February 15, 2013, the voluntary delisting of SMB’s common shares from the PSE. A petition for the same was thereafter filed by SMB with the PSE on February 20, 2013. To comply with the PSE requirements on voluntary delisting, SMB undertook a tender offer to buy back all of the common shares held by the public (other than those held by its major stockholders and directors) at an offer price of ₱20.00 per common share. The tender offer commenced on March 4, 2013 and will end on April 3, 2013. The acceptance and payment by SMB of all validly tendered common shares is set on April 12, 2013.

The date of effectivity of the voluntary delisting of the SMB shares is on May 15, 2013.

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Power Generation and Distribution

• ***SMC Global***

On July 29, 2011, the BOD and stockholders of SMC Global approved the increase in authorized capital stock from ₱1,000, divided into 10,000,000 shares at ₱100.00 par value per share, to ₱2,000, divided into 2,000,000,000 shares at ₱1.00 par value per share. Out of the increase in authorized capital stock, the Parent Company subscribed to 250,000,000 shares and paid the amount of ₱62.5 on August 4, 2011. The SEC approved the increase in the authorized capital stock of SMC Global on August 25, 2011.

• ***SMELCO***

On February 8, 2011, the Parent Company incorporated SMELCO, a wholly-owned subsidiary, with an authorized capital stock of ₱1,000 divided into 10,000,000 shares and paid-up capital of ₱250.

On August 22, 2011, SMELCO was granted a Retail Electricity Supplier's (RES) license by the Energy Regulatory Commission (ERC), pursuant to Section 29 of Republic Act (RA) No. 9136 or the Electric Power Industry Reform Act of 2001, which requires all suppliers of electricity to the contestable market to secure a license from the ERC. The term of the RES License is for a period of 5 years from the time it was granted and renewable thereafter.

On August 31, 2011, the Parent Company sold its 100% shareholdings in SMELCO to SMC Global for ₱250.

• ***DAMI***

DAMI, a coal mining company with coal property covered by Coal Operating Contract (COC) No. 126 issued by the DOE, dated November 19, 2002, is located in Barangay Ned, Lake Sebu, South Cotabato consisting of two (2) coal blocks with a total area of two thousand (2,000) hectares, more or less. As of February 13, 2013, COC No. 126 has an In-situ coal resources (measured plus indicative coal resources) of about 94 million metric tons based on exploratory drilling and additional in-fill drilling conducted by DAMI.

• ***SEPC***

SEPC, a coal mining property with coal property covered by COC No. 134 issued by the DOE dated February 23, 2005, is located in Lake Sebu, South Cotabato and Sen. Ninoy Aquino, Sultan Kudarat consisting of seven (7) coal blocks with a total aggregate area of 7,000 hectares, more or less. As of February 13, 2013, COC No. 134 has an In-situ coal resources (measured plus indicative coal resources) of about 35 million metric tons based on exploratory drilling and confirmatory drilling conducted by SEPC.

• ***BERI***

BERI, a coal mining company with coal property covered by COC No. 138 issued by the DOE dated May 26, 2005 is located in Maitum, Sarangani Province and Barangay Ned, Lake Sebu, South Cotabato consisting of eight (8) coal blocks with a total area of 8,000 hectares, more or less, and has an In-situ coal resources (measured plus indicative coal resources) of about 22 million metric tons as of February 13, 2013 based on initial exploratory drilling conducted by SMEC geologists in Maitum, Sarangani. The exploratory drilling to be conducted on 4 coal blocks of BERI located in Barangay Ned, Lake Sebu Municipality is projected to contain 30 million metric tons based on a geological setting and initial exploratory drilling conducted in Maitum.

On March 26, 2008, February 9, 2009 and December 15, 2009, the DOE approved the conversion of the COC for Exploration to COC for Development and Production of DAMI, SEPC and BERI, respectively, effective on the following dates:

<u>Subsidiary</u>	<u>COC no.</u>	<u>Effective date</u>	<u>Term*</u>
DAMI	126	November 19, 2008	10 years
SEPC	134	February 23, 2009	10 years
BERI	138	May 26, 2009	10 years

* The term is followed by another 10-year extension, and thereafter, renewable for a series of 3-year periods not exceeding 12 years under such terms and conditions as may be agreed upon with the DOE.

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In May 2011, SEPC, DAMI and BERI separately wrote a letter to the DOE requesting for a moratorium on suspension of the implementation of the production timetable as specified in the Five-Year Development and Productive Work Progress of COC Nos. 126, 134 and 138 due to the newly enacted Environment Code of South Cotabato. This local ordinance prohibits open pit mining and other related activities, hence, constrained these companies into implementing the production timetable without violating this local ordinance. On April 27, 2012, the DOE granted SEPC, DAMI and BERI's request for a moratorium on their work commitments from the effective dates of their respective COCs when these were converted to Development/Production Phase until December 31, 2012.

Mining

• *Clariden*

On June 8, 2012, the BOD and stockholders of Clariden resolved and approved the increase in authorized capital stock of Clariden from ₱5 divided into 50,000 shares to ₱1,000 divided into 10,000,000 shares both with a par value of ₱100.00 per share. The application for the Amendment of Articles of Incorporation for the increase in authorized capital stock was filed with the SEC on December 28, 2012 and was approved on February 22, 2013.

Packaging

• *CAI*

On November 12, 2012, the Parent Company through SMYPC, incorporated CAI, a wholly-owned subsidiary, with an authorized capital stock of ₱1,000 divided into 10,000,000 shares and paid-up capital of ₱63. CAI is primarily engaged to carry on trade or operation as a manufacturer, buyer, importer, exporter, contractor, dealer, broker, commission merchant, agent or representative of all kinds of packaging products, and to render services to its clients and customers as may be necessary for the assembling, packaging and/or repacking of their respective products, particularly aluminum cans and ends.

CAI has not yet started commercial operations as of December 31, 2012.

On January 1, 2013, SMYPC spun-off its Metal Container Plant to be sold to and operated by CAI.

On January 15, 2013, the 35% equity interest in CAI was purchased by a foreign company, a corporation duly organized and existing under the laws of Poland.

As of January 2013, CAI is 65% owned by SMYPC.

Real Estate

• *SMPI*

On December 28, 2012, SMPI received a letter from the PSE imposing trading suspension until June 30, 2013 due to failure to comply with the minimum public ownership requirement.

On February 5, 2013, the BOD approved the filing of the petition for voluntary delisting and conduct of a tender for the acquisition of common share held by SMPI's minority shareholders. On March 4, 2013, SMPI filed with the PSE the petition for voluntary delisting with May 6, 2013 as the effective date of delisting of the SMPI common shares from the PSE. To comply with the PSE requirements on voluntary delisting, SMPI undertook a tender offer to buy back all of the common shares held by the public (other than those held by its major stockholders and directors) at an offer price of ₱134.12 per common share. The tender offer commenced on March 6, 2013 and will end on April 5, 2013. The acceptance and payment by SMPI of all validly tendered common shares is set on April 15, 2013.

• *SMPI Flagship and SMC Originals*

On July 30, 2012, the BOD and stockholders of SMPI Flagship resolved and approved the increase in authorized capital stock of SMPI Flagship from ₱625 divided into 625,000,000 shares to ₱1,308 divided into 1,308,000,000 shares both with a par value of ₱1.00 per share. The request for the Amendment of Articles of Incorporation for the increase in authorized capital stock was filed with the SEC on October 16, 2012 and was approved on October 31, 2012.

SMPI Flagship has not yet started commercial operations as of December 31, 2012.

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On October 9, 2012, the BOD of Highriser Group, Inc. approved the change of corporate name to SMC Originals, Inc. The approval from the SEC was obtained in January 2013.

Others

• ***MG8***

On March 16, 2011, SMCSLC incorporated MG8, a wholly-owned subsidiary, with an initial authorized capital stock of ₱10 divided into 100,000 shares and paid-up capital of ₱10.

• ***SMEII***

On March 23, 2011, the Parent Company incorporated SMEII, a wholly-owned subsidiary, with an initial authorized capital stock of ₱100 divided into 100,000,000 shares and paid-up capital of ₱25.

On March 28, 2012, the BOD and stockholders of SMEII resolved and approved the increase in authorized capital stock of SMEII from ₱100 divided into 100,000,000 shares to ₱14,300 divided into 14,300,000,000 shares both with a par value of ₱1.00 per share. The application for the Amendment of Articles of Incorporation for the increase in authorized capital stock was filed with the SEC on December 28, 2012. On January 30, 2013, the SMEII BOD and stockholders approved to further increase its authorized capital stock to ₱21,425 divided into 21,425,000,000 shares with a par value of ₱1.00 per share. The application with the SEC was amended to reflect the foregoing change which was approved by the SEC on March 4, 2013.

7. Segment Information

Operating Segments

The reporting format of the Group's operating segments is determined based on the Group's risks and rates of return which are affected predominantly by differences in the products and services produced. The operating businesses are organized and managed separately according to the nature of the products produced and services provided, with each segment representing a strategic business unit that offers different products and serves different markets.

The Group's reportable segments are beverage, food, packaging, power generation and distribution, fuel and oil, infrastructure and telecommunications.

The beverage segment produces and markets alcoholic and nonalcoholic beverages.

The food segment includes, among others, feeds production, poultry and livestock farming, processing and selling of poultry and meat products, processing and marketing of refrigerated and canned meat products, manufacturing and marketing of flour products, premixes and flour-based products, dairy-based products, breadfill, desserts, cooking oil, importation and marketing of coffee and coffee-related products.

The packaging segment is involved in the production and marketing of the following packaging products, among others, glass containers, glass molds, polyethylene terephthalate (PET) bottles and preforms, PET recycling, plastic closures, corrugated cartons, woven polypropylene, kraft sacks and paperboard, pallets, flexible packaging, plastic crates, plastic floorings, plastic films, plastic trays, plastic pails and tubs, metal closures and two-piece aluminum cans, woven products, industrial laminates and radiant barriers. It is also involved in crate and plastic pallet leasing, PET bottle filling graphics design, packaging research and testing, packaging development and consultation, contract packaging and trading.

The power generation and distribution segment is engaged in power generation and distribution and mining. The power generation assets supply electricity to a variety of customers, including Meralco, electric cooperatives, industrial customers and the Philippine Wholesale Electricity Spot Market (WESM).

The fuel and oil segment is engaged in refining and marketing of petroleum products.

The infrastructure segment is engaged in the business of construction and development of various infrastructure projects such as airports, roads, highways, toll roads, freeways, skyways, flyovers, viaducts and interchanges.

The telecommunications segment is engaged in rendering all types of domestic and international telecommunications services.

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Segment Assets and Liabilities

Segment assets include all operating assets used by a segment and consist primarily of operating cash, receivables, inventories, biological assets, and property, plant and equipment, net of allowances and impairment. Segment liabilities include all operating liabilities and consist primarily of accounts payable and accrued expenses and other noncurrent liabilities, excluding interest payable. Segment assets and liabilities do not include deferred taxes.

Inter-segment Transactions

Segment revenues, expenses and performance include sales and purchases between operating segments. Transfer prices between operating segments are set on an arm's length basis in a manner similar to transactions with third parties. Such transfers are eliminated in consolidation.

Major Customer

The Group does not have a single external customer from which sales revenue generated amounted to 10% or more of the total revenues of the Group.

Operating Segments

Financial information about reportable segments follows:

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For the years ended December 31, 2012, 2011 and 2010

	Beverage		Food		Packaging		Power generation and distribution		Fuel and Oil		Infrastructure		Telecommunications		Others		Eliminations		Consolidated											
	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011										
Other Information																														
Segment assets	P97,230	P83,076	P81,412	P50,985	P43,612	P43,267	P34,077	P31,954	P32,112	P255,516	P260,418	P238,591	P265,507	P172,173	P158,984	P30,210	P3,141	P2,642	P 9,679	P 5,881	P203,193	P 227,709	P216,157	(P130,803)	(P152,050)	(P144,272)	P 805,943	P767,912	P634,774	
Investments in and advances to associates	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—
Goodwill, trademarks and brand names																														
Other assets																														
Assets held for sale																														
Deferred tax assets																														
Consolidated Total Assets																														
Segment liabilities	P19,453	P21,196	P20,945	P14,029	P10,505	P14,755	P 4,716	P 5,380	P 13,360	P 13,675	P 16,769	P 42,649	P 23,684	P 19,633	P18,631	P3,003	P 580	P19,529	P18,829	P11,723	P102,836	P 110,393	P130,931	(P146,494)	(P141,900)	(P135,218)	P 88,709	P 64,117	P 85,498	
Loans payable																														
Long-term debt																														
Finance lease liabilities																														
Income and other taxes payable																														
Dividends payable and others																														
Liabilities directly associated with assets held for sale																														
Deferred tax liabilities																														
Consolidated Total Liabilities																														

SAN MIGUEL CORPORATION AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Amounts in Millions, Except Per Share Data and Number of Shares)

For the years ended December 31, 2012, 2011 and 2010																				
	Beverage		Food		Packaging		Power generation and distribution		Fuel and oil		Infrastructure		Telecommunications		Others		Eliminations		Consolidated	
	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011
Capital expenditures	P 1,101	P2,954	P 598	P 599	P1,161	P1,347	P 4,772	P 620	P 586	P41,848	P18,794	P 364	P 7	P 394	P72	P —	P1,680	P2,005	P3,231	P —
Depreciation and amortization of property, plant and equipment (Note 29)	2,366	2,168	884	895	1,575	1,688	1,611	5,194	5,432	2,468	4,690	3,566	210	12	6	537	181	55	790	707
Noncash items other than depreciation and amortization of property, plant and equipment	1,217	1,271	717	1,193	1,309	1,338	257	(111)	(30)	(8,386)	600	357	(748)	161	1,660	8	4	26	91	29
Loss on impairment of goodwill, property, plant and equipment, and other noncurrent assets	(1,427)	77	4,333	19	6	51	348	—	—	—	—	—	—	—	—	—	—	—	—	—
																			1	(1,059)
																				128 4,384

SAN MIGUEL CORPORATION AND SUBSIDIARIES
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8. Assets Held for Sale

a) Bank of Commerce (BOC)

On May 8, 2012, the Parent Company through SMPI, together with the other stockholders of BOC, executed a Share Purchase Agreement with Commerce International Merchant Bankers (CIMB Bank), a subsidiary of CIMB Group Sdn Bhd. of Malaysia, covering the sale of up to 65,083,087 fully paid ordinary shares, equivalent to a 58% equity interest in BOC for a total consideration of up to approximately ₱12,000. Under the provisions of the agreement, the completion of the sale is subject to certain closing conditions, inclusive of the mandatory approvals from the Monetary Board of the Bangko Sentral ng Pilipinas (BSP) and the Bank of Negara Malaysia. On November 7, 2012, the Bank of Negara Malaysia approved CIMB Bank's proposed acquisition of BOC subject to the attainment of the relevant approvals from the BSP.

The Monetary Board of the BSP, based on its letter dated November 20, 2012, approved the proposed acquisition.

The sale, however, was not consummated in 2012 pending the compliance of certain provisions of the Share Purchase Agreement.

Accordingly, the carrying amount of the investment as of December 31, 2012 of ₱8,785 representing 44,817,164 common shares was reclassified to "Assets held for sale" account in the 2012 consolidated statement of financial position.

b) Petron Mega Plaza and PMCs Treats

Petron has properties consisting of office units located at Petron Mega Plaza with a floor area of 21,216 square meters covering the 28th — 44th floors and 206 parking spaces amounting to ₱823. On December 1, 2010, the BOD approved the sale of these properties to provide cash flows for various projects. Accordingly, the investment properties were presented as "Assets held for sale" as of December 31, 2010. On May 2, 2011, Petron sold the 32nd floor (with total floor area of 1,530 square meters) and 10 parking spaces, with a total book value of ₱57. In September 2011, it was reclassified back to "Investment properties" account in view of the fact that the remaining floors are no longer held for sale and have already been tenanted.

During the latter part of 2012, a prospective buyer tendered an offer to purchase the remaining Petron Mega Plaza units and parking spaces. The management made a counter offer in December 2012 effectively rendering the Petron Mega Plaza units and parking spaces with a carrying amount of ₱588 as "Assets held for sale" as of December 31, 2012. The negotiation is on its final phase and the sale is expected to be consummated by the second quarter of 2013.

As of December 31, 2012, the fair market value of the Petron Mega Plaza office units and parking spaces amounted to ₱1,141.

The buildings for stand-alone convenience stores and locators held by PMC with a carrying amount of ₱10 as of December 31, 2011 were reclassified back to "Property, plant and equipment — net" account in 2012, in view of the fact that the remaining filling stations are no longer held for sale and have not met the qualifications to be classified as such.

c) SMTCL

On December 7, 2011, the Parent Company through SMFBIL, signed a Share Sale and Purchase Agreement to sell all its outstanding shares in SMTCL to Pepsi Thai Trading Co., for a purchase price of US\$35. The sale was completed on February 15, 2012 and the Group recognized a net gain of ₱63 from the sale.

d) SMYUI

In 2011, the Parent Company through SMYPIL and Nihon Yamamura Glass Co., Ltd. (NYG), entered into a non-binding Memorandum of Understanding (MOU), wherein NYG offered to buy 51% equity interest in SMYUI. On December 2, 2011, the BOD of SMYPIL unanimously accepted NYG's offer and approved the share sale transaction as contemplated in the MOU. The disposal was completed in January 2012 and the Group recognized a net gain of ₱22 from the sale.

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The major classes of SMTCL and SMYUI's assets and liabilities held for sale are as follows:

	<u>Note</u>	<u>2011</u>
Assets Held for Sale		
Cash and cash equivalents	9	P 86
Trade and other receivables — net		21
Inventories		53
Prepaid expenses and other current assets		30
Property, plant and equipment — net	16	1,900
		<u>P2,090</u>
Liabilities Directly Associated with Assets Held for Sale		
Accounts payable and accrued expenses		P 58
Income and other taxes payable		9
Current maturities of long-term debt — net of debt issue costs		341
Other noncurrent liabilities		170
		<u>P 578</u>

- e) Included in the “Assets held for sale” account presented in the consolidated statement of financial position as of December 31, 2011, are building and land use rights of SMVCL in Amata Industrial Zone, Vietnam amounting to P168, which were sold to Pepsico International Vietnam on February 23, 2012. The Group recognized a net gain of P256 from the sale.

9. Cash and Cash Equivalents

Cash and cash equivalents consist of:

	<u>Note</u>	<u>2012</u>	<u>2011</u>
Cash in banks and on hand		P 31,362	P 30,125
Short-term investments		94,269	98,850
	41, 42	<u>P125,631</u>	<u>P128,975</u>

Cash in banks earns interest at the respective bank deposit rates. Short-term investments include demand deposits which can be withdrawn at anytime depending on the immediate cash requirements of the Group and earn interest at the respective short-term investment rates.

Cash and cash equivalents included in the “Assets held for sale” account in the consolidated statement of financial position amounted to P86 as of December 31, 2011 (Note 8).

10. Trade and Other Receivables

Trade and other receivables consist of:

	<u>Note</u>	<u>2012</u>	<u>2011</u>
Trade		P 52,495	P44,631
Non-trade	5, 13, 40	54,917	31,830
Amounts owed by related parties	34, 36	21,574	13,236
		<u>128,986</u>	89,697
Less allowance for impairment losses	4	6,387	5,225
	41, 42	<u>P122,599</u>	<u>P84,472</u>

Trade receivables are non-interest bearing and are generally on a 30 to 45-day term.

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The movements in the allowance for impairment losses are as follows:

	<i>Note</i>	<u>2012</u>	<u>2011</u>
Balance at beginning of year		₱5,225	₱4,519
Charges for the year		575	1,017
Amounts written off		(125)	(214)
Acquisition of subsidiaries	5	545	68
Transferred to assets held for sale		—	(12)
Translation adjustments and others		167	(153)
Balance at end of year		<u>₱6,387</u>	<u>₱5,225</u>

As of December 31, 2012 and 2011, the aging of receivables is as follows:

<u>2012</u>	<u>Trade</u>	<u>Non-trade</u>	<u>Amounts owed by related parties</u>	<u>Total</u>
Current	₱40,539	₱25,973	₱21,574	₱ 88,086
Past due:				
Less than 30 days	4,091	11,675	—	15,766
30-60 days	2,939	564	—	3,503
61-90 days	1,148	798	—	1,946
Over 90 days	3,778	15,907	—	19,685
	<u>₱52,495</u>	<u>₱54,917</u>	<u>₱21,574</u>	<u>₱128,986</u>

<u>2011</u>	<u>Trade</u>	<u>Non-trade</u>	<u>Amounts owed by related parties</u>	<u>Total</u>
Current	₱35,387	₱19,282	₱13,236	₱67,905
Past due:				
Less than 30 days	3,280	546	—	3,826
30-60 days	1,378	915	—	2,293
61-90 days	641	186	—	827
Over 90 days	3,945	10,901	—	14,846
	<u>₱44,631</u>	<u>₱31,830</u>	<u>₱13,236</u>	<u>₱89,697</u>

Various collaterals for trade receivables such as bank guarantees, time deposit and real estate mortgages are held by the Group for certain credit limits.

The Group believes that the unimpaired amounts that are past due by more than 30 days are still collectible based on historical payment behavior and extensive analyses of the underlying customer credit ratings. There are no significant changes in their credit quality.

The amounts owed by related parties include receivables amounting to ₱21,574 and ₱13,236 as of December 31, 2012 and 2011, respectively (Note 34).

11. Inventories

Inventories consist of:

	<u>2012</u>	<u>2011</u>
Finished goods and goods in process (including petroleum products)	₱58,469	₱46,763
Materials and supplies (including coal)	20,559	17,656
Containers	1,194	1,301
	<u>₱80,222</u>	<u>₱65,720</u>

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The cost of finished goods and goods in process amounted to ₱58,696 and ₱46,879 as of December 31, 2012 and 2011, respectively.

If the Group used the moving-average method (instead of the first-in, first-out method, which is the Group's policy), the cost of petroleum, crude oil and other petroleum products would have decreased by ₱921 and ₱379 as of December 31, 2012 and 2011, respectively.

The cost of materials and supplies amounted to ₱21,155 and ₱18,516 as of December 31, 2012 and 2011, respectively.

Containers at deposit value amounted to ₱1,401 and ₱1,479 as of December 31, 2012 and 2011, respectively.

Finished goods and goods in process include net unrealized gain of ₱89 and ₱69 on fair valuation of agricultural produce as of December 31, 2012 and 2011, respectively (Note 4). The fair value of agricultural produce less costs to sell, which formed part of finished goods inventory, amounted to ₱550 and ₱753 as of December 31, 2012 and 2011, respectively, with corresponding costs at point of harvest amounting to ₱461 and ₱684, respectively.

12. Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets consist of:

	<i>Note</i>	2012	2011
Prepaid taxes and licenses		₱21,458	₱16,113
Raw land inventory and real estate projects		3,703	3,925
Option deposit	<i>13, 41, 42</i>	1,026	—
CIP — airport concession arrangements	<i>4</i>	652	318
Prepaid insurance		404	290
Prepaid rent		304	287
Financial assets at FVPL	<i>41, 42</i>	147	194
Derivative assets	<i>41, 42</i>	91	121
AFS financial assets — current portion	<i>41, 42</i>	51	—
Others		3,776	1,372
		<u>₱31,612</u>	<u>₱22,620</u>

“Others” consist of prepayments for various operating expenses.

CIP — airport concession arrangements includes the Group's accumulated costs incurred on the design of the upgrade component of the development of the Boracay Airport, cost of a parcel of land earmarked for such upgrade, capitalized borrowing cost and the present value of the obligation to maintain and restore the Boracay Airport (IRO) prior to its transfer to the ROP at the end of the concession period (Note 35). This will be transferred and recognized as cost of construction upon commencement of the construction of the new terminal and runway (Note 4). The interest expense related to the accretion of the IRO amounting to ₱4 in 2012 and 2011 and ₱1 in 2010, was recognized as part of “Interest expense and other financing charges” account in the consolidated statements of income (Note 31).

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13. Investments and Advances

Investments and advances consist of:

	<i>Note</i>	<u>2012</u>	<u>2011</u>
Investments in Associates — at Equity			
Acquisition Cost:			
Balance at beginning of year		₱159,241	₱152,016
Additions		21,530	9,199
Reclassification to investment in subsidiaries	5	(3,495)	(1,600)
Reclassification to assets held for sale	8	(8,211)	—
Redemption		(12,899)	—
Reclassifications and others		502	(374)
		<u>156,668</u>	<u>159,241</u>
Accumulated Equity in Net Earnings (Losses):			
Balance at beginning of year		(746)	(217)
Equity in net earnings		2,691	2,824
Dividends		(6,472)	(3,973)
Redemption		945	—
Reclassification to investment in subsidiaries	5	(933)	(25)
Reclassification to assets held for sale	8	(574)	—
Share in other comprehensive income		400	645
Reclassifications and others		(189)	—
Balance at end of year		<u>(4,878)</u>	<u>(746)</u>
		151,790	158,495
Advances		<u>9,835</u>	<u>8,359</u>
		<u>₱161,625</u>	<u>₱166,854</u>

The carrying amounts of investments in associates are as follows:

	Country of incorporation	<u>2012</u>		<u>2011</u>	
		Percentage of ownership	Amount	Percentage of ownership	Amount
Top Frontier Investment Holdings, Inc. (Top Frontier)	Philippines	49.00	₱ 76,364	49.00	₱ 90,345
Meralco	Philippines	32.04	47,575	33.19	46,439
Trustmark Holdings Corporation (Trustmark) and Zuma Holdings and Management Corporation (Zuma)	Philippines	49.00	18,861	—	—
Atlantic	Netherlands	46.53	3,142	46.53	6,068
LTHI	Philippines	41.48	2,196	41.48	2,828
Private Infra Dev Corporation (PIDC)	Philippines	35.00	1,545	35.00	1,544
Petrochemical Asia (HK) Limited (PAHL)	Hong Kong	46.00	866	33.00	441
Manila North Harbour Port Inc. (MNHPI)	Philippines	35.00	775	35.00	704
Northpine Land, Inc.	Philippines	20.00	293	20.00	249
Manila Toll Expressway Systems, Inc.	Philippines	30.00	103	—	—
SOMCO	Philippines	40.00	48	—	—
LEC*	Philippines	—	—	40.00	1,360
Bank of Commerce (BOC)**	Philippines	—	—	39.93	8,517
Others	Philippines	—	22	—	—
			<u>₱151,790</u>		<u>₱158,495</u>

* Reclassified to investments in subsidiaries in 2012 (Note 5).

** Reclassified to "Assets held for sale" account in the 2012 consolidated statement of financial position (Note 8).

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Following are the unaudited condensed and combined financial information of the associates:

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Total assets	₱677,039	₱587,629	₱552,700
Total liabilities	422,782	309,418	261,599
Revenue	394,135	271,340	253,289
Net income	10,290	12,173	19,290

a. Top Frontier

On January 6, 2010, the Parent Company acquired a 49% stake via equity infusion in Top Frontier consisting of its subscription to 2,401,960 common shares of Top Frontier from its unissued capital stock. On January 7, 2010, the Parent Company paid ₱48,324 as deposit for future subscription in connection with the option granted to the Parent Company to apply the same to the subscription of 2,598,040 non-voting, redeemable, participating preferred shares of Top Frontier upon the increase in its authorized capital stock, amendment of its Articles of Incorporation and Top Frontier's compliance with its obligations related to the aforementioned investment.

The application for the increase in the authorized capital stock of Top Frontier was approved by the SEC on August 6, 2010.

The stock certificates covering the investment of the Parent Company in the 2,598,040 preferred shares of Top Frontier were issued in the name of the Parent Company on October 22, 2010.

The preferred shares are entitled to preferential dividends at a fixed rate per annum of 3% of the issue price which will be payable quarterly in arrears and in cash. The dividends on the preferred shares are cumulative from and after the issue date of the preferred shares.

The preferred shares are non-voting and participating. These are redeemable in whole or in part, at the sole option of Top Frontier, equal to its issue price plus any accrued and unpaid preferential dividends, upon notice to the holders.

On June 18, 2012, Top Frontier redeemed a total of 693,500 preferred shares out of the 2,598,040 preferred shares issued to the Parent Company, at the total redemption price of ₱12,899. The Group recognized a gain of ₱945 from the transaction included as part of "Gain on sale of investments and property and equipment" account in the consolidated statements of income.

b. Meralco

The Parent Company increased its beneficial interest in Meralco to 33.19% upon its acquisition of SMC Global in 2010, which owns 69,059,538 common shares of Meralco.

The purchase price of the Meralco shares purchased from GSIS in 2008 was ₱27,087, plus fixed term interest. The Parent Company paid a downpayment of ₱5,417 with the balance payable in 3 years. In January and August 2011, the Parent Company paid in full the remaining balance of its liability related to the acquisition of Meralco shares of stock from GSIS amounting to an aggregate of ₱21,909.

On August 12, 2011, the BOD of the Parent Company approved the sale of a portion of its investment in Meralco to SMPFC, comprising of 59,090,909 common shares or approximately 5.2% of the outstanding capital stock of Meralco at ₱220.00 per share. The purchase price of the shares was based on the average trading price of Meralco shares for the period from January 1 to July 31, 2011, with a discount of 12%.

In January 2011, SMC Global paid the Development Bank of the Philippines and the Social Security System ₱2,576, as consideration for the acquisition of Meralco shares of stock.

The current portion of the Group's outstanding payable related to the purchase of Meralco shares amounted to ₱2,122 as of December 31, 2011, included under "Accounts payable and accrued expenses" account (Note 22). The remaining balance of its payable was paid in full on January 31, 2012.

On May 14, 2012, the Group received the stock certificate for the property dividend from Meralco consisting of 1,042,801,676 common shares of stock of Rockwell Land Corporation, with a book value of ₱1,522. On July 27, 2012, the Group sold through the PSE its Rockwell Land Shares at ₱2.01 per share and recognized a gain of

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₱571 included as part of “Gain on sale of investments and property and equipment” account in the consolidated statements of income.

The fair value of the Group’s investment in Meralco amounted to ₱96,428 and ₱90,656 as of December 31, 2012 and 2011, respectively.

c. Trustmark and Zuma

On April 3, 2012, the Parent Company, through SMEII, signed Investment Agreements with the Lucio Tan Group to subscribe to the unissued common shares equivalent to 49% of the outstanding capital stock of Trustmark and Zuma for a total consideration of ₱21,506.

With the acquisition of the 49% equity interests in Trustmark and Zuma, SMEII indirectly owns 47.88% and 48.98% beneficial interests in Philippine Airlines, Inc. (PAL) and Air Philippines Corporation (AirPhil), respectively. PAL, the national flag carrier of the Philippines, and Airphil are primarily engaged in the business of air transportation for the carriage of passengers and cargo within and outside the Philippines.

d. Atlantic

On October 11, 2011, the Parent Company, through its wholly-owned subsidiary SMHC, entered into a Sale and Purchase Agreement of Shares with PT Matra Sarana Arsitama, a corporation organized and existing under the laws of the Republic of Indonesia, for the purchase of 16,022,041 Class B common shares, representing 46.53% of the outstanding capital stock of Atlantic for US\$132 or ₱5,871. Atlantic has indirect equity interests in the companies holding the concessions to construct, operate and maintain the SLEX Project.

On December 29, 2011, SMHC entered into an Option Agreement with Padma, a corporation organized and existing under the laws of Cayman Island, for the option to purchase up to 53.47% of the outstanding capital stock of Atlantic, comprising of 47,369 Class A common shares and 18,364,461 Class B common shares. SMHC paid US\$40 or ₱1,754 as option deposit for the option to purchase the shares. SMHC has the option to purchase the shares for a period of 25 calendar days from the execution of the Option Agreement or until January 23, 2012, or such date as may be agreed upon by the Parties in writing. The option deposit shall be returned upon the issuance of a written notice by SMHC confirming that the option shall not be exercised. As of December 31, 2011, the option deposit was presented as part of “Trade and other receivables” account in the consolidated statements of financial position (Note 10). The option deposit was returned to SMHC on January 26, 2012.

On May 24, 2012, SMHC and Padma entered into another Option Agreement granting SMHC an option to acquire 4.47% equity interest in Atlantic and up to 100% of the outstanding capital stock of certain corporations where Padma holds ownership interest for US\$25 or ₱1,026. The option is exercisable at any time from execution of the Agreement or such other date as may be agreed upon by parties in writing. The option deposit shall be returned upon the issuance of a written notice by SMHC confirming that the option shall not be exercised.

As of December 31, 2012, the option deposit was presented as part of “Prepaid expenses and other current assets” account in the consolidated statements of financial position (Note 12).

e. LTHI

Vega, a wholly-owned subsidiary of the Parent Company, has a 41.48% stake in LTHI representing 643,700,669 common shares and 587,951,737 preferred shares. The preferred shares are voting, non-redeemable and participating.

The fair value of the Group’s investment in LTHI amounted to ₱3,277 and ₱3,508 as of December 31, 2012 and 2011, respectively.

f. PIDC

Rapid, a wholly-owned subsidiary of SMHC, has a 35% equity interest in PIDC, a consortium of construction companies behind the Tarlac-Pangasinan-La Union Expressway Project. As of December 31, 2012 and 2011, Rapid has an unpaid subscription amounting to ₱769 included as part of “Accounts payable and accrued expenses” account in the consolidated statements of financial position (Note 22).

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On September 12, 2011, Rapid advanced ₱1,111 as deposit for future stock subscription to 1,111,228 common shares of PIDC, included as part of “Investments and advances” account in the consolidated statements of financial position. As of March 21, 2013, one of the conditions for the issuance of the subscribed shares to Rapid has not yet been met.

g. PAHL

The Parent Company, through its subsidiary Petron, had a 33% stake in PAHL, a company incorporated in Hong Kong which indirectly owns, among other assets, a 160,000 metric ton-polypropylene production plant in Mariveles, Bataan.

On December 31, 2012, PAHL issued to Petron 135,652,173 ordinary B shares which increased Petron’s ownership in PAHL to 46%.

h. MNHPI

On January 3, 2011, Petron entered into a Share Sale and Purchase Agreement with Harbour Centre Port Terminal, Inc. for the purchase of 35% of the outstanding and issued capital stock of MNHPI.

i. BOC

SMPI has made series of acquisitions of BOC shares from 2007 to 2010 and has acquired a total of 36,779,899 shares equivalent to 32.77% equity ownership interest in BOC as of December 31, 2010.

In 2010, SMPI made advance payments to certain stockholders of BOC amounting to ₱221 for the acquisition of additional shares sufficient to increase its equity interest in BOC to 33.86%. These advances were presented under “Investments and advances” account in the consolidated statements of financial position as of December 31, 2011 and were not considered in the determination of SMPI’s percentage equity interest in BOC.

In 2011, SMPI acquired an additional 7.16% of the outstanding capital stock of BOC for a total consideration of ₱1,490, by way of Deed of Sale of Shares with Assignment of Subscription Rights from Valiant Ventures and Development Holdings, Inc. consisting of: (i) 2,800,000 outstanding and issued common shares of stock; and (ii) the subscription rights to 5,237,265 common shares of stock. The acquisition by SMPI resulted in an increase in its equity interest to 39.93% as of December 31, 2011.

In 2011, SMPI, through the Parent Company, started negotiating for the sale of a portion of its ownership interest in BOC to CIMB Bank, a financial institution incorporated in Malaysia. As of December 31, 2011, the contracting parties have not yet finalized the agreement due to price consideration and other pending pertinent documents. Further, the investment account is not presented under “Assets held for sale” account since this transaction requires approval from BSP and the possibility of obtaining such approval is uncertain as of December 31, 2011.

As of December 31, 2011, SMPI still has pending share purchase transactions with other stockholders of BOC for the acquisition of additional shares which will further increase SMPI’s equity interest in BOC to 41.02%. Pending consummation of the share purchase transactions, the advance payments made by SMPI to the sellers amounting to ₱221, which were placed under escrow, were presented under “Investments and advances” account in the 2011 consolidated statement of financial position. Accordingly, this was not also considered in the determination of the Company’s percentage of equity ownership interest in BOC.

In July 2011, SMPI’s management received a letter from the sellers stating their intention to cancel the sale of BOC shares. In 2012, SMPI’s management decided to accept the offer for the cancellation of the share purchase agreement since the sellers can no longer fulfill certain conditions in the agreement. As of December 31, 2012, SMPI has yet to receive the advance payment placed under the escrow fund. As a result of the cancellation of the purchase agreement, the advance payment, including accumulated interest income from the escrow fund, was reclassified to “Trade and other receivables” account in the 2012 consolidated statement of financial position.

Share in BOC’s accumulated fair value gains amounted to ₱258 and ₱129 in 2012 and 2011, respectively, and are presented as part of “Share in comprehensive income (loss) of associates” account in the consolidated statements of comprehensive income.

In November 2012, SMPI, through the Parent Company, obtained the approval for the proposed acquisition from Bank Negara Malaysia and from BSP which are the regulatory agencies governing the operations of financial

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institutions in Malaysia and Philippines, respectively. The sale, however, was not consummated in 2012 pending the compliance of certain provisions of the sale and purchase agreement. Accordingly, the investment was reclassified from “Investment and advances” account to “Assets held for sale” account in the 2012 consolidated statement of financial position.

The Management of SMPI determined that the carrying amount of the investment in BOC as of December 31, 2012 is fully recoverable based on the agreed selling price of the investment with CIMB, thus, no impairment loss was recognized in 2012.

Certain accounting policies applied by BOC in the preparation of its financial statements are not in accordance with PFRS. In computing for the equity in net earnings (losses) and comprehensive income (losses) of BOC, SMPI made adjustments to the audited financial statements of BOC to conform BOC’s accounting policies with PFRS and make them consistent with the Group’s accounting policies. The adjustments made by SMPI relate to the correction of: (a) inadequate reserves on non-performing assets, investment properties and financial assets; (b) deferral of losses on sale of non-performing loans; (c) realization of revaluation increment through depreciation; and (d) misstatement in the values of structured financial instruments and certain investment properties. No impairment loss on the investment was recognized in 2011 and 2010.

BOC is required to meet certain ratios under BSP regulations to manage the risks inherent in the banking business. As of December 31, 2012, 2011 and 2010, BOC has complied with the statutory and regulatory capital requirements which were computed based on the regulatory accounting policies that differ from PFRS in some aspects. BOC’s retained earnings as of December 31, 2012, 2011 and 2010 is restricted from being declared as dividend to common stockholders to the extent of the amount of cumulative cash dividend in arrears of ₱320 declared by BOC’s BOD on December 16, 2008 in favor of stockholders of certain redeemed preferred shares. The dividend declaration is pending approval from BSP as of December 31, 2012.

j. Advances

Primeria Commercio Holdings, Inc. (PCHI)

SMPI provided US dollar-denominated deposits to PCHI, a future investee of SMPI, amounting to ₱794 as of December 31, 2012 and 2011. The deposits will be applied against future subscriptions of SMPI to the shares of stock of PCHI.

Telecommunications Company

In 2011, Vega has made deposits to a telecommunications company, a future investee, amounting to ₱5,958 as of December 31, 2012 and 2011, to be applied against future stock subscriptions.

Cement Company

In 2012, SMYPC provided a deposit for future subscription on the shares of stocks of a cement company amounting to ₱1,500 as of December 31, 2012. This deposit will be applied against future subscription of SMYPC to the shares of stocks of the cement company.

On March 1, 2013, SMYPC fully settled the ₱3,500 subscription payment for the purchase of 104,500,000 common shares of stock of the cement company.

As of March 21, 2013, SMYPC owns 35% equity interest in the cement company’s capital stock.

AAMRC

In 2011, Clariden has made deposits for the acquisition of AAMRC’s shares of stock amounting to ₱274. On September 6, 2012, Clariden completed the acquisition of the 60% equity interest in AAMRC and was consolidated into the Group. In 2012, the ₱274 deposit was reclassified from “Investments and advances” account in the consolidated statements of financial position to investment in subsidiaries.

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14. Available-for-Sale Financial Assets

Available-for-sale financial assets consist of:

	<i>Note</i>	<u>2012</u>	<u>2011</u>
Government and other debt securities		₱ 804	₱ 924
Equity securities		505	877
Proprietary membership shares and others		312	267
	<i>41, 42</i>	1,621	2,068
Less: current portion	<i>12</i>	51	—
	<i>41, 42</i>	₱1,570	₱2,068

Government Securities

Petrogen's government securities are deposited with the Bureau of Treasury in accordance with the provisions of the Insurance Commission, for the benefit and security of its policyholders and creditors. These investments bear fixed annual interest rates ranging from 6.00% to 8.875% in 2012 and 2011.

Ovincor's ROP9 bonds are maintained at the HSBC Bank Bermuda Limited and carried at fair value with fixed annual interest rates of 8.250% to 8.875%.

As of December 31, 2012 and 2011, the fair value of Ovincor's ROP9 Bonds amounted to ₱625 and ₱692, respectively.

Equity Securities

The Parent Company executed a Share Placement Agreement with Indophil Resources NL (Indophil) to subscribe to 48,016,960 common shares (Placement Shares) equivalent to approximately 10.1% of the currently issued common shares of Indophil, on a fully diluted basis.

Indophil is an Australian company listed in the Australian Stock Exchange, which owns a 37.5% beneficial interest in Sagittarius Mines, Inc. (SMI). SMI has the rights to the Tampakan gold and copper mine in South Cotabato.

On October 15, 2010, the Placement Shares were issued in the name of Coastal View Exploration Corporation (Coastal View), a subsidiary of SMHC. The total consideration for the purchase of the Placement Shares was Australian dollar (A\$)41.3 (approximately US\$40) or A\$0.86 per Placement Share.

As of December 31, 2012 and 2011, Coastal View's stake in Indophil is at 3.99% as a result of the additional share issuances made by Indophil.

As of December 31, 2012 and 2011, the fair value of the investment in Indophil amounted to ₱491 and ₱862, respectively.

15. Investments in Joint Ventures

GSMI, through GSMIL, has an existing Joint Venture (JV) with Thai Life Group of Companies (Thai Life) covering the ownership and operations of TSML. TSML is a limited company organized under the laws of Thailand in which GSMIL owns 40% ownership interest. TSML holds a license in Thailand to engage in the business of manufacturing alcohol and manufacturing, selling and distributing brandy, wine and distilled spirits products both for domestic and export markets.

With the acquisition by SHL, a wholly-owned subsidiary of GSMI, of the 49% ownership interest in Siam Wine Liquor Co., Ltd. (SWL) and SWL's acquisition of shares representing 10% ownership of the outstanding capital stock of TSML, GSMI group's share in TSML increased from 40% to 44.9%. The acquisition was funded through advances made by GSMI to GBHL, a wholly-owned subsidiary of GSMI, which has an existing loan agreement with SWL for the same amount.

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The Group's share in the assets, liabilities, income and expenses of TSML included in the Group's consolidated financial statements as of December 31 is shown below:

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Current assets	₱297	₱484	₱516
Noncurrent assets	735	806	894
Current liabilities	358	425	436
Noncurrent liabilities	142	269	309
Revenue	444	452	657
Cost of sales	535	600	817
Operating expenses	67	85	76
Other income	1	4	12
Net loss	157	229	224

The Group's share in the cash flows of TSML for the years ended December 31 is as follows:

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Net cash flows used in operating activities	(₱38)	(₱209)	(₱373)
Net cash flows provided by investing activities	72	87	—
Net cash flows provided by (used in) financing activities	127	(40)	(106)

GSMI, through its wholly-owned subsidiary GSMIHL, has an existing 40% ownership interest in TGT, which was formed as another joint venture with Thai Life. TGT functions as the selling and distribution arm of TSML.

With the acquisition of SWL of the 10% ownership interest in TGT, GSMI group's share in TGT increased from 40% to 44.9%. The acquisition was funded through advances made by GSMI to GBHL which has an existing loan agreement with SWL for the same amount.

The Group's share in the assets, liabilities, income and expenses of TGT included in the Group's consolidated financial statements as of December 31 is shown below:

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Current assets	₱ 44	₱ 65	₱ 51
Noncurrent assets	—	3	14
Current liabilities	14	14	15
Noncurrent liabilities	—	—	2
Revenue	113	171	232
Cost of sales	1	2	17
Operating expenses	39	83	111
Other income	9	1	1
Net income	82	87	105

The Group's share in the cash flows of TGT for the years ended December 31 is as follows:

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Net cash flows provided by operating activities	₱105	₱70	₱159
Net cash flows provided by investing activities	3	12	15
Net cash flows used in financing activities	—	(2)	(14)

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16. Property, Plant and Equipment

Property, plant and equipment consist of:

	Land and land improvements	Buildings and improvements	Power plants	Refinery and plant equipment	Service stations and other equipment	Machinery and equipment	Telecommunications equipment	Transportation equipment	Tools and small equipment	Office equipment, furniture and fixtures	Molds	Leasehold improvements	Construction in progress	Total
Cost:														
December 31, 2010	P15,277	P32,224	P214,899	P37,286	P 5,319	P85,763	P1,002	P 8,615	P2,327	P4,194	P 702	P1,237	P 6,097	P414,942
Additions	1,121	1,201	596	524	831	4,394	39	2,308	277	461	227	224	14,223	26,426
Disposals/reclassifications/acquisition of subsidiaries	285	(177)	(1,176)	—	(80)	(2,182)	6,353	(41)	(70)	207	(120)	90	682	3,771
Transfer to assets held for sale	(202)	(729)	—	—	—	(1,615)	—	(3)	(8)	(52)	—	—	(4)	(2,613)
Currency translation adjustments	(73)	143	—	—	—	304	—	1	(19)	(4)	—	—	11	363
December 31, 2011	16,408	32,662	214,319	37,810	6,070	86,664	7,394	10,880	2,507	4,806	809	1,551	21,009	442,889
Additions	627	216	—	116	1,348	2,253	190	1,501	209	360	236	44	45,820	52,920
Disposals/reclassifications/acquisition of subsidiaries	4,258	7,817	—	11,298	7,159	(1,612)	(58)	(91)	(135)	184	(338)	114	(164)	28,432
Currency translation adjustments	(228)	(1,025)	—	(480)	(301)	(1,603)	—	(33)	(35)	(64)	(4)	(2)	(15)	(3,790)
December 31, 2012	21,065	39,670	214,319	48,744	14,276	85,702	7,526	12,257	2,546	5,286	703	1,707	66,650	520,451
Accumulated depreciation and amortization:														
December 31, 2010	2,462	10,732	5,611	16,545	3,742	46,652	678	2,389	1,691	3,585	510	555	—	95,152
Additions	158	1,056	5,427	2,027	504	3,790	166	668	219	304	203	121	—	14,643
Disposals/reclassifications/acquisition of subsidiaries	(5)	385	(410)	7	(25)	(1,412)	4,562	(110)	(81)	(110)	(76)	(22)	—	2,703
Transfer to assets held for sale	—	(94)	—	—	—	(415)	—	—	(2)	(51)	—	—	—	(562)
Currency translation adjustments	(3)	21	—	—	—	5	—	—	(17)	(4)	1	1	—	4
December 31, 2011	2,612	12,100	10,628	18,579	4,221	48,620	5,406	2,947	1,810	3,724	638	655	—	111,940
Additions	149	1,385	5,185	2,337	977	3,926	444	817	194	343	195	96	—	16,048
Disposals/reclassifications/acquisition of subsidiaries	(51)	3,857	—	7,510	4,132	(809)	(30)	(103)	(145)	243	(220)	(12)	—	14,372
Currency translation adjustments	(13)	(377)	—	(330)	(178)	(690)	—	(28)	(27)	(55)	(3)	(2)	—	(1,703)
December 31, 2012	2,697	16,965	15,813	28,096	9,152	51,047	5,820	3,633	1,832	4,255	610	737	—	140,657

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	Land and land improvements	Buildings and improvements	Power plants	Refinery and plant equipment	Service stations and other equipment	Machinery and equipment	Telecommunications equipment	Transportation equipment	Tools and small equipment	Office equipment, furniture and fixtures	Molds	Leasehold improvements	Construction in progress	Total
Accumulated impairment losses:														
December 31, 2010	P 412	P 3,829	P —	P —	P —	P 7,403	P —	P 12	P 20	P 41	P —	P —	P —	P 11,717
Additions for the year	—	6	—	—	—	52	45	—	—	—	—	—	—	103
Disposals/reclassifications/acquisition of subsidiaries	(27)	(149)	—	—	—	(685)	—	—	(1)	—	—	—	—	(862)
Transfer to assets held for sale	—	—	—	—	—	(46)	—	—	—	—	—	—	—	(46)
Currency translation adjustments	—	126	—	—	—	283	—	1	1	—	—	—	—	411
December 31, 2011	385	3,812	—	—	—	7,007	45	13	20	41	—	—	—	11,323
Additions (reversal) for the year	—	(1,502)	—	—	—	(4)	—	—	—	—	—	1	—	(1,505)
Disposals/reclassifications/acquisition of subsidiaries	—	(48)	—	—	—	(14)	—	—	(6)	(1)	—	—	—	(69)
Currency translation adjustments	—	(235)	—	—	—	(404)	—	(1)	(1)	(3)	—	—	—	(644)
December 31, 2012	385	2,027	—	—	—	6,585	45	12	13	37	—	1	—	9,105
Net book value:														
December 31, 2011	P13,411	P16,750	P203,691	P19,231	P1,849	P31,037	P1,943	P7,920	P677	P1,041	P171	P896	P21,009	P319,626
December 31, 2012	P17,983	P20,678	P198,506	P20,648	P5,124	P28,070	P1,661	P8,612	P701	P994	P93	P969	P66,650	P370,689

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Total depreciation, amortization and impairment losses/reversal recognized in profit or loss amounted to ₱14,543, ₱14,746 and ₱11,725 in 2012, 2011 and 2010, respectively (Notes 29 and 33). These amounts include annual amortization of capitalized interest amounting to ₱14, ₱13 and ₱14 in 2012, 2011 and 2010, respectively.

The Group has interest amounting to ₱895 and ₱219 which were capitalized in 2012 and 2011, respectively. The capitalization rates used to determine the amount of interest eligible for capitalization were 5.71% and 5.65% in 2012 and 6.76% and 4.97% in 2011. As of December 31, 2012 and 2011, the unamortized capitalized borrowing costs amounted to ₱997 and ₱314, respectively.

The combined carrying amounts of power plants, machinery and equipment and transportation equipment under finance lease amounted to ₱198,562 and ₱203,756 as of December 31, 2012 and 2011, respectively (Notes 4 and 35).

• ***Limay Power Plant***

On January 18, 2010, the physical possession of the Limay Power Plant was turned over and transferred to PanAsia. The Limay Power Plant started commercial operations on February 16, 2010.

In July 2010, with the consent of PSALM, PanAsia's option to acquire the land was assigned to PCPI. Accordingly, PCPI assumed all the rights and obligations under the original contract between PanAsia and PSALM. On September 30, 2010, PCPI exercised the option and acquired ownership of the land.

On August 26, 2011, SMC Global sold its 100% ownership interest in PanAsia to MHI.

• ***SMVCL***

On August 25, 2011, SMVCL sold its machinery and equipment in Amata Industrial Zone, Vietnam for US\$19 and recognized a gain amounting to ₱273, included as part of "Gain on sale of investments and property and equipment" account in the 2011 consolidated statement of income.

On February 23, 2012, SMVCL sold its building and land use rights in Amata Industrial Zone, Vietnam for US\$12 and recognized a gain amounting to ₱256 included as part of "Gain on sale of investments and property and equipment" account in the 2012 consolidated statement of income.

• ***PTSMIFB***

On September 28, 2012, PTSMIFB sold its land use rights, building and machinery for US\$27 and recognized a gain amounting to ₱45, included as part of "Gain on sale of investments and property and equipment" account in the 2012 consolidated statement of income.

• ***Sumilao Property***

Land and land improvements include a 144-hectare property in Sumilao, Bukidnon, acquired by SMFI in 2002, which later became the subject of a petition for revocation of conversion order filed by MAPALAD, a group of Sumilao farmers, with the Department of Agrarian Reform (DAR), and appealed to the Office of the President (OP). Total acquisition and development costs amounted to ₱37.

To settle the land dispute, a Memorandum of Agreement (MOA) was executed among SMFI, MAPALAD, OP and DAR on March 29, 2008. The MOA provided for the release of a 50-hectare portion of the property to qualified farmer-beneficiaries, and the transfer of additional 94 hectares outside of the property to be negotiated with other Sumilao landowners. Under the MOA, SMFI shall retain ownership and title to the remaining portion of the property for the completion and pursuit of the hog farm expansion.

SMFI fully complied with all the provisions of the MOA in the last quarter of 2010. To formally close the pending cases filed by MAPALAD with the Supreme Court and OP, SMFI forwarded in November 2010 to the Sumilao farmers' counsels the draft of the Joint Manifestation and Motion for Dismissal of the cases pending with the Supreme Court and the OP for their concurrence. Pursuant to the Joint Manifestation and Motion for Dismissal dated March 3, 2011 filed by SMFI and NQSR Management and Development Corporation, the original owner of the Sumilao property, the Supreme Court and the OP, in a Resolution dated March 15, 2011 and in an Order dated April 6, 2011, respectively, dismissed the appeal of MAPALAD on the DAR's denial of their petition for the revocation of the conversion order.

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17. Investment Properties

The movements in investment properties are as follows:

	<i>Note</i>	Land and land improvements	Buildings and improvements	Machinery and equipment	Tools and small equipment	Construction in progress	Total
Cost:							
December 31, 2010		₱ 2,158	₱ 600	₱1,015	₱ 9	₱ —	₱ 3,782
Additions/reclassifications		403	995	2	—	398	1,798
Disposals		(1,012)	(70)	—	—	—	(1,082)
Currency translation adjustments		(36)	—	—	—	—	(36)
December 31, 2011		1,513	1,525	1,017	9	398	4,462
Additions and acquisition of subsidiary/reclassifications	5	1,088	45	82	—	442	1,657
Transferred to assets held for sale	8	—	(928)	—	—	—	(928)
Currency translation adjustments		(20)	(22)	—	—	—	(42)
December 31, 2012		2,581	620	1,099	9	840	5,149
Accumulated depreciation and amortization:							
December 31, 2010		87	233	929	9	—	1,258
Additions		11	102	7	—	—	120
Disposals/reclassifications		2	168	(12)	—	—	158
December 31, 2011		100	503	924	9	—	1,536
Additions		9	111	42	—	—	162
Disposals/reclassifications		—	—	24	—	—	24
Transferred to assets held for sale	8	—	(350)	—	—	—	(350)
Currency translation adjustments		(3)	(8)	—	—	—	(11)
December 31, 2012		106	256	990	9	—	1,361
Accumulated impairment losses:							
December 31, 2010		356	35	—	—	—	391
Disposals/reclassifications		(304)	—	—	—	—	(304)
Currency translation adjustments		(11)	—	—	—	—	(11)
December 31, 2011		41	35	—	—	—	76
Disposals/reclassifications		(31)	(33)	—	—	—	(64)
Currency translation adjustments		(2)	(2)	—	—	—	(4)
December 31, 2012		8	—	—	—	—	8
Net book value:							
December 31, 2011		<u>₱ 1,372</u>	<u>₱ 987</u>	<u>₱ 93</u>	<u>₱—</u>	<u>₱398</u>	<u>₱ 2,850</u>
December 31, 2012		<u>₱ 2,467</u>	<u>₱ 364</u>	<u>₱ 109</u>	<u>₱—</u>	<u>₱840</u>	<u>₱ 3,780</u>

No impairment loss was recognized in 2012, 2011 and 2010.

There are no other direct selling and administrative expenses other than depreciation and amortization and real property taxes arising from investment properties that generated income in 2012, 2011 and 2010.

On June 10, 2011, SMBTL sold its Bangpho property in Bang Sue District, Bangkok Metropolis for THB815 (₱1,050). The property's original cost is THB506 (₱706). The Group recognized a gain of ₱344, included as part of "Gain on sale of investments and property and equipment" account in the 2011 consolidated statement of income.

Estimated fair values of investment properties amounted to ₱6,078 and ₱5,594 as of December 31, 2012 and 2011, respectively (Note 4).

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18. Biological Assets

Biological assets consist of:

	<u>2012</u>	<u>2011</u>
Current:		
Growing stocks	₱3,150	₱3,228
Goods in process	642	896
	<u>3,792</u>	<u>4,124</u>
Noncurrent:		
Breeding stocks — net	1,932	1,812
	<u>₱5,724</u>	<u>₱5,936</u>

The amortization of breeding stocks recognized in profit or loss amounted to ₱1,311, ₱1,186 and ₱1,081 in 2012, 2011 and 2010, respectively (Note 29).

Growing stocks pertain to growing broilers, hogs and cattle and goods in process pertain to hatching eggs.

The movements in biological assets are as follows:

	<u>2012</u>	<u>2011</u>
Cost:		
Balance at beginning of year	₱ 6,295	₱ 5,010
Increase (decrease) due to:		
Production	27,233	17,159
Purchases	483	11,687
Mortality	(565)	(477)
Sales	(7,242)	(6,087)
Harvest	(18,788)	(19,989)
Reclassifications	(1,085)	(1,010)
Currency translation adjustments	(118)	2
Balance at end of year	<u>6,213</u>	<u>6,295</u>
Accumulated amortization:		
Balance at beginning of year	359	264
Additions	1,311	1,186
Disposals	(91)	(81)
Reclassifications	(1,085)	(1,010)
Currency translation adjustments	(5)	—
Balance at end of year	<u>489</u>	<u>359</u>
Net book value	<u>₱ 5,724</u>	<u>₱ 5,936</u>

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19. Goodwill and Other Intangible Assets

The movements in goodwill are as follows:

	<u>Note</u>	<u>2012</u>	<u>2011</u>
Balance at beginning of year		₱30,990	₱30,251
Additions	5, 39	19,554	732
Currency translation adjustments and others		(591)	7
Balance at end of year		<u>₱49,953</u>	<u>₱30,990</u>

The movements in other intangible assets with indefinite useful lives are as follows:

	<u>Licenses</u>	<u>Trademarks and brand names</u>	<u>Total</u>
Cost:			
December 31, 2010	₱7,138	₱430	₱7,568
Currency translation adjustments	(94)	2	(92)
December 31, 2011	7,044	432	7,476
Currency translation adjustments	(57)	(19)	(76)
December 31, 2012	<u>6,987</u>	<u>413</u>	<u>7,400</u>
Accumulated impairment losses:			
December 31, 2010 and 2011	—	190	190
Currency translation adjustments	—	(14)	(14)
December 31, 2012	<u>—</u>	<u>176</u>	<u>176</u>
Net book value:			
December 31, 2011	<u>₱7,044</u>	<u>₱242</u>	<u>₱7,286</u>
December 31, 2012	<u>₱6,987</u>	<u>₱237</u>	<u>₱7,224</u>

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The movements in other intangible assets with finite useful lives are as follows:

	<i>Note</i>	Toll road concession rights	Leasehold rights	Land use rights	Mining rights	Airport concession rights	Licenses	Others	Total
Cost:									
December 31, 2010		₱ —	₱ —	₱1,817	₱1,800	₱ 91	₱203	₱ 816	₱ 4,727
Additions and acquisition of subsidiaries	5, 39	—	—	3	197	111	34	362	707
Disposals and reclassifications		—	—	(118)	—	1	—	19	(98)
Currency translation adjustments		—	—	25	—	—	(2)	1	24
December 31, 2011		—	—	1,727	1,997	203	235	1,198	5,360
Additions and acquisition of subsidiaries	5, 39	29,039	1,915	—	—	93	176	481	31,704
Disposals and reclassifications		—	(58)	(202)	(10)	(1)	(84)	366	11
Currency translation adjustments		—	(78)	(114)	—	—	(2)	(21)	(215)
December 31, 2012		29,039	1,779	1,411	1,987	295	325	2,024	36,860
Accumulated amortization and impairment losses:									
December 31, 2010		—	—	410	—	1	62	652	1,125
Additions and acquisition of subsidiaries	5,3339	—	—	46	—	9	8	54	117
Disposals and reclassifications		—	—	(22)	—	1	(1)	12	(10)
Currency translation adjustments		—	—	7	—	—	—	—	7
December 31, 2011		—	—	441	—	11	69	718	1,239
Additions and acquisition of subsidiaries	5,39	8,438	16	30	—	9	25	151	8,669
Disposals and reclassifications		—	—	(11)	—	(7)	7	96	85
Currency translation adjustments		—	—	(28)	—	—	—	(12)	(40)
December 31, 2012		8,438	16	432	—	13	101	953	9,953
Net book value:									
December 31, 2011		₱ —	₱ —	₱1,286	₱1,997	₱192	₱166	₱ 480	₱ 4,121
December 31, 2012		₱20,601	₱1,763	₱ 979	₱1,987	₱282	₱224	₱1,071	₱26,907

Intangible asset — airport concession rights represent the present value of the annual franchise fee payable to the ROP over 25 years discounted using 9% internal borrowing rate, net of accumulated amortization (Notes 4, 12 and 24).

Intangible asset — toll road concession rights represent the costs incurred for the construction of the toll roads (Note 3).

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Goodwill, licenses and trademarks and brand names with indefinite lives and mining rights with finite lives acquired through business combinations have been allocated to individual cash-generating units, for impairment testing as follows:

	2012			2011		
	Goodwill	Licenses, trademarks and brand names	Mining rights	Goodwill	Licenses, trademarks and brand names	Mining rights
Fuel and oil	₱32,286	₱ —	₱ —	₱22,025	₱ —	₱ —
Infrastructure	11,065	—	—	2,438	—	—
Food	2,927	225	—	2,942	229	—
Packaging	1,894	—	—	2,026	—	—
Beverage	994	1,778	—	772	1,836	—
Power generation and distribution and mining	—	—	1,987	—	—	1,997
Telecommunications	726	5,221	—	726	5,221	—
Others	61	—	—	61	—	—
Total	<u>₱49,953</u>	<u>₱7,224</u>	<u>₱1,987</u>	<u>₱30,990</u>	<u>₱7,286</u>	<u>₱1,997</u>

The recoverable amount of goodwill has been determined based on a valuation using cash flow projections covering a five-year period based on long range plans approved by management. Cash flows beyond the five-year period are extrapolated using a constant growth rate determined per individual cash-generating unit. This growth rate is consistent with the long-term average growth rate for the industry. The discount rate applied to after tax cash flow projections ranged from 6% to 14% in 2012 and 2011. The discount rate also imputes the risk of the cash-generating units compared to the respective risk of the overall market and equity risk premium.

Impairment loss on goodwill amounting to ₱461 was recognized and included as part of “Other income (charges)” account in the 2010 consolidated statement of income in 2010. No impairment losses were recognized in 2012 and 2011 (Note 33).

The recoverable amount of trademarks and brand names has been determined based on a valuation using cash flow projections covering a five-year period based on long range plans approved by management. Cash flows beyond the five-year period are extrapolated using a determined constant growth rate to arrive at its terminal value. The range of the growth rates used is consistent with the long-term average growth rate for the industry. The discount rate applied to after tax cash flow projections ranged from 7.4% to 16% and 8.9% to 14.5% in 2012 and 2011, respectively.

Management assessed that impairment loss in the value of trademarks and brand names amounting to ₱64 was recognized and included as part of “Other income (charges)” account in the 2010 consolidated statement of income. No impairment losses were recognized in 2012 and 2011 (Note 33).

Management believes that any reasonably possible change in the key assumptions on which the recoverable amount is based would not cause its carrying amount to exceed its recoverable amount.

The calculations of value in use are most sensitive to the following assumptions:

- *Gross Margins.* Gross margins are based on average values achieved in the period immediately before the budget period. These are increases over the budget period for anticipated efficiency improvements. Values assigned to key assumptions reflect past experience, except for efficiency improvement.
- *Discount Rates.* The Group uses the weighted-average cost of capital as the discount rate, which reflects management’s estimate of the risk specific to each unit. This is the benchmark used by management to assess operating performance and to evaluate future investments proposals.
- *Raw Material Price Inflation.* Consumer price forecast is obtained from indices during the budget period from which raw materials are purchased. Values assigned to key assumptions are consistent with external sources of information.

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20. Other Noncurrent Assets

Other noncurrent assets consist of:

	<i>Note</i>	2012	2011
Noncurrent receivables and deposits — net	34, 36, 40, 41, 42	P14,840	P27,471
Deferred containers — net	4	6,214	5,035
Project development costs		2,135	2,218
Retirement assets	36	903	299
Others		8,136	3,494
		<u>P32,228</u>	<u>P38,517</u>

Noncurrent receivables and deposits include amounts owed by related parties amounting to P11,032 and P24,509 as of December 31, 2012 and 2011, respectively (Note 34).

Project development costs consist of capitalized expenditures related to the development of the MRT 7 Project (Note 35). These include manpower costs, engineering service costs, financing fees, technology development and consultancy service costs, overhead costs and other project related costs.

“Others” include noncurrent prepaid rent and insurance, catalysts, deferred exploration and development costs and idle assets. Deferred exploration and development costs amounted to P232 and P103 as of December 31, 2012 and 2011, respectively (Note 4). Idle assets amounted to P906 and P986 as of December 31, 2012 and 2011, respectively (Notes 4 and 33).

21. Loans Payable

Loans payable consist of:

	<i>Note</i>	2012	2011
Parent Company			
Peso-denominated		P 9,325	P15,133
Subsidiaries			
Peso-denominated		96,700	63,577
Foreign currency-denominated		45,249	3,878
	41, 42	<u>P151,274</u>	<u>P82,588</u>

Loans payable mainly represent unsecured peso and foreign currency-denominated amounts payable to local and foreign banks. Interest rates for peso-denominated loans range from 3.25% to 5.75% and 3.10% to 5.13% in 2012 and 2011, respectively. Interest rates for foreign currency-denominated loans range from 3.28% to 14.19% and 1.5% to 20% in 2012 and 2011, respectively.

Loans payable include interest bearing amounts payable to a related party amounting to P9,045 and P3,360 as of December 31, 2012 and 2011, respectively (Note 34).

Loans payable of the Group are not subject to covenants and warranties.

22. Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses consist of:

	<i>Note</i>	2012	2011
Trade		P54,954	P39,398
Non-trade		20,596	12,638
Payables on the purchase of shares of stock	5, 13	808	2,862
Subscriptions payable	13, 34	769	769
Amounts owed to related parties	34	571	326
Retirement liabilities	36	103	85
Others		6,864	5,551
	41, 42	<u>P84,665</u>	<u>P61,629</u>

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Derivative liabilities included under “Others” amounted to ₱315 and ₱118 as of December 31, 2012 and 2011, respectively (Notes 41 and 42).

Non-trade payables include freight payable, contract growers/breeders’ fees, guarantee deposits, utilities, rent and other expenses payable to third parties, as supported by invoices, which were not paid in the month in which they are incurred.

The current portion of IRO included in “Non-trade” amounted to ₱11 and ₱2 as of December 31, 2012 and 2011.

“Others” include interest payable and accruals for payroll, materials, repairs and maintenance, advertising, handling, contracted labor, supplies and various other payables.

23. Long-term Debt

Long-term debt consists of:

	<u>2012</u>	<u>2011</u>
Parent Company		
Unsecured term notes:		
Foreign currency-denominated:		
Floating interest rate based on LIBOR plus margin, with maturities up to 2015 (a)	₱40,444	₱43,011
Fixed interest rate with maturities up to 2014 (b)	24,133	25,754
Peso-denominated:		
Floating interest rate based on PDST-F plus margin, with maturities up to 2012, 2014 and 2015 (c)	9,047	9,445
	73,624	78,210
Subsidiaries		
Bonds:		
Peso-denominated:		
Fixed interest rate of 8.25%, 8.875% and 10.50% maturing in 2012, 2014 and 2019, respectively (d)	25,015	38,534
Fixed interest rate of 6.05%, 5.93% and 6.60% maturing on 2017, 2019 and 2022, respectively (e)	19,813	—
Foreign currency-denominated:		
Fixed interest rate of 7% maturing in 2016 (f)	12,210	13,012
Unsecured term notes:		
Peso-denominated:		
Fixed interest rate of 7% maturing in 2017 (g)	19,830	19,803
Fixed interest rate of 8.14% and 9.33% maturing in 2014 and 2016, respectively (h)	9,810	9,840
Fixed interest rate of 8.5% maturing in 2017 (i)	8,488	—
Fixed interest rate of 6.3212% and 7.1827% maturing in 2018 and 2021 (j)	3,530	3,563
Fixed interest rate of 6.175% and 6.145% maturing in 2016 (k)	1,500	1,494
Fixed interest rate of 6.50% and 7.25% maturing in 2012 and 2014, respectively (l)	1,268	2,220
Fixed interest rate of 7.89% and 7.25% maturing in 2015 (m)	1,239	1,495
Fixed interest rate of 5.4885% maturing in 2015 (n)	796	794
Fixed interest rate of 6.73% maturing in 2012 (o)	—	154
Floating interest rate based on PDST-F plus margin, with maturities up to 2015 (n)	3,680	3,673
Floating interest rate based on PDST-F plus margin or BSP overnight rate plus margin, whichever is higher, with maturities up to 2019 (p)	3,482	—
Floating interest rate based on PDST-F plus margin, with maturities up to 2022 (q)	751	—
Floating interest rate based on PDST-F plus margin, with maturities up to 2018 (r)	686	—
Floating interest rate based on PDST-F plus margin, fully paid in 2012 (s)	—	1,200
Floating interest rate based on PDST-R1 plus margin or BSP overnight rate plus margin, whichever is higher, preterminated in 2012 (t)	—	204

Forward

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	<u>2012</u>	<u>2011</u>
Foreign currency-denominated:		
Floating interest rate based on LIBOR plus margin, with maturities up to 2016 (u)	₱ 11,922	₱ 3,419
Floating interest rate based on LIBOR plus margin, with maturities up to 2017 (v)	10,921	—
Floating interest rate based on LIBOR plus margin, with maturities up to 2014 (w)	8,184	8,713
Floating interest rate based on LIBOR plus margin, with maturities up to 2015 (x)	6,069	12,906
Floating interest rate based on LIBOR plus margin, with maturities up to 2015 (y)	1,227	—
Floating interest rate based on THBFIX plus margin, with maturities up to 2014 (z)	172	297
Floating interest rate based on LIBOR plus margin, fully paid in 2012 (aa)	—	11,889
	<u>150,593</u>	<u>133,210</u>
	<u>224,217</u>	<u>211,420</u>
Less current maturities	<u>3,279</u>	<u>19,453</u>
	<u>₱220,938</u>	<u>₱191,967</u>

- a. The amount represents drawdown by the Parent Company in 2011 from the US\$1,000 loan facility used to refinance its existing financial indebtedness and for general working capital purposes.

Unamortized debt issue costs related to these loans amounted to ₱606 and ₱829 as of December 31, 2012 and 2011, respectively.

- b. The amount represents the Parent Company's US\$600 Exchangeable Bonds (the Bonds) issued on May 5, 2011 and listed in the Singapore Exchange Securities Trading Limited (SGX-ST) on the same date. The Bonds bear interest at the rate of 2.00% per annum, payable semi-annually in arrears every 5th of May and November of each year, with the first interest payment made on November 5, 2011. Unless the Bonds have been previously redeemed, repurchased, cancelled or exchanged, the Parent Company will redeem the Bonds at its principal amount on May 5, 2014.

The Bonds are exchangeable for common shares from the treasury shares of the Parent Company (Note 26). The number of common shares to be delivered in exchange of a Bond will be determined by dividing the principal amount of the Bond to be exchanged (translated into Philippine Peso at the fixed rate of ₱43.34=US\$1.00) by the initial exchange price of ₱137.50 per share, subject to adjustment in certain circumstances.

As of December 31, 2012, a total of US\$5.6 worth of exchangeable bonds representing 2,176,055 common shares of the Parent Company were exchanged at issue prices ranging from ₱109.80 to ₱113.24 (Note 26).

Unamortized bond issue costs as of December 31, 2012 and 2011 amounted to ₱267 and ₱462, respectively.

- c. The amount represents drawdown by the Parent Company used for general financing and corporate requirements.

Unamortized debt issue costs related to these loans amounted to ₱3 and ₱5 as of December 31, 2012 and 2011, respectively.

- d. The amount represents SMB's peso-denominated fixed rate bonds (Bonds) worth ₱38,800 which were sold to the public pursuant to a registration statement that was rendered effective by the SEC on March 17, 2009 and are listed on the Philippine Dealing & Exchange Corp. (PDEX) for trading.

The Bonds were issued in three (3) series: Series A Bonds with a fixed interest rate of 8.25% per annum; Series B Bonds with a fixed interest rate of 8.875% per annum; and Series C Bonds with a fixed interest rate of 10.50% per annum.

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In February 2012, SMB obtained the consent of bondholders of its ₱38,800 Bonds representing 76.92% of the aggregate principal amount of the ₱38,800 Bonds to maintain a minimum interest coverage ratio of 4.75:1 in lieu of a minimum current ratio of 1:1.

The Series A bonds with an aggregate principal amount of ₱13,590 matured on April 3, 2012 and was accordingly redeemed by SMB on the said date.

Unamortized debt issue costs related to these bonds amounted to ₱97 and ₱167 as of December 31, 2012 and 2011, respectively.

- e. The amount represents SMB's peso-denominated fixed rate bonds (Bonds) worth ₱20,000, which were sold to the public pursuant to a registration statement that was rendered effective by the SEC on March 16, 2012. The Bonds were issued on April 2, 2012 at the issue price of 100.00% of face value in three (3) series: Series D Bonds with fixed interest rate of 6.05% per annum; Series E Bonds with a fixed interest rate of 5.93% per annum; and Series F Bonds with a fixed interest rate of 6.60% per annum. The proceeds of the Bonds were used to refinance its existing financial indebtedness and for general working capital purposes.

The Series E Bonds and Series F Bonds were listed on PDEX on April 2, 2012 while the Series D Bonds was listed for trading on the PDEX effective October 3, 2012.

Unamortized debt issue costs related to these bonds amounted to ₱187 as of December 31, 2012.

- f. The amount represents US\$300, 7%, 5-year bond issued by SMC Global in 2011 under the Regulations of the US Securities Act of 1933, as amended. The unsecured bond issue is listed in the SGX-ST.

Unamortized bond issue costs as of December 31, 2012 and 2011 amounted to ₱105 and ₱140, respectively.

- g. The amount represents ₱20,000 peso-denominated notes issued by Petron in 2010. The principal and interest will be translated into and paid in US dollars based on the average representative market rate at the applicable rate calculation date at the time of each payment. The notes bear interest of 7% per annum, payable semi-annually in arrears on May 10 and November 10 of each year. The notes will mature on November 10, 2017.

Unamortized debt issue cost related to this note amounted to ₱171 and ₱197 as of December 31, 2012 and 2011, respectively.

- h. The amount represents Fixed Rate Corporate Notes (FXCN) issued by Petron amounting to ₱5,200 and ₱4,800. The ₱5,200 five-year notes bear a fixed rate of 8.14% per annum with one-time payment of principal in June 2014. The ₱4,800 seven-year notes bear a fixed rate of 9.33% per annum with 6 principal payments of ₱48 per year commencing in June 2010 and a one-time payment of ₱4,512 in June 2016.

Unamortized debt issue cost related to these notes amounted to ₱46 and ₱64 as of December 31, 2012 and 2011, respectively.

- i. The amount represents CMMTC's syndicated loans amounting to ₱8,721 in 2012 (Note 5). The syndicated loans were entered into by CMMTC with various banks which were used to finance CMMTC's capital expenditures.

Unamortized debt issue cost related to these loans amounted to ₱233 as of December 31, 2012.

- j. The amount represents FXCN issued by Petron in 2011 consisting of Series A Notes amounting to ₱690 having a maturity of 7 years from the issue date and Series B notes amounting to ₱2,910 having a maturity of 10 years from the issue date. The notes are subject to fixed interest coupons of 6.3212% per annum for the Series A notes and 7.1827% per annum for the Series B notes. The net proceeds from the issuance were used for general corporate requirements.

Unamortized debt issue cost related to these notes amounted to ₱33 and ₱37 as of December 31, 2012 and 2011, respectively.

- k. The amount represents drawdown by SMCSLC in 2011, from a local bank, which was used for working capital requirements.

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Unamortized debt issue cost related to this loan amounted to ₱6 as of December 31, 2011.

- l. The amount represents syndicated loans obtained by SMYAC which were used for capital expenditures.

Unamortized debt issue costs related to these loans amounted to ₱2 and ₱4 as of December 31, 2012 and 2011, respectively.

- m. The amount represents drawdown by GSMI, from a local bank, which was used for working capital requirements.

Unamortized debt issue costs related to these loans amounted to ₱4 and ₱5 as of December 31, 2012 and 2011, respectively.

- n. The amount represents corporate notes which SMFI offered for sale and subscription to the public. These are Philippine peso-denominated fixed rate and floating rate corporate notes with principal amounts of ₱800 and ₱3,700, respectively. Both types of notes have a term of 5 years and 1 day beginning on December 10, 2010 and ending on December 11, 2015. The fixed rate note bears interest rate of 5.4885% per annum, while the floating rate note bears interest rate based on 3-month PDST-F plus an agreed margin. Proceeds from the issuance of the notes were used to fund expansion and investment in new businesses by SMFI and for general corporate financing purposes.

Unamortized debt issue costs related to these bonds amounted to ₱24 and ₱33 as of December 31, 2012 and 2011, respectively.

- o. The amount represents a club loan agreement entered into by Petron amounting to ₱1,000. The loan was fully paid on January 31, 2012.
- p. The amount represents the loan agreement entered into by SMYPC with BOC amounting to ₱3,500 used for general financing and corporate requirements maturing on October 11, 2019 (Note 34).

Unamortized debt issue costs related to the loan amounted to ₱18 as of December 31, 2012.

- q. The amount represents the balance of the first drawdown of ₱755 from a loan agreement entered into by TADHC with BOC amounting to ₱3,300, used for financing the Airport Project. The loan is payable in twenty-eight quarterly installments commencing on the twelfth quarter (Note 34).

Unamortized debt issue costs related to these loans amounted to ₱4 as of December 31, 2012.

- r. The amount represents EPSBPI's loan balance of ₱686 (Note 5). The unsecured loan facility was entered into by EPSBPI which was used to finance EPSBPI's construction of its bottling facilities. The loan is payable in equal quarterly installments starting February 18, 2012 bearing an interest rate equivalent to the higher of benchmark rate (three-month PDST-F rate) plus a one percent spread or the overnight rate (BSP overnight reverse repo rate on interest rate settling date).
- s. The amount represents a three-year term facility agreement entered into by Petron amounting to ₱1,800. The loan is subject to quarterly repricing and the principal amount is amortized in twelve quarterly installments of ₱150 starting March 2011 up to December 2013. The loan was obtained to finance Petron's general corporate requirements. The loan was fully paid on June 14, 2012.
- t. The amount represents GFDCC's loan balance of ₱204 in 2011 (Note 5). The unsecured loan facility was entered into by GFDCC with BOC which was used to finance GFDCC's capital expenditures. In December 2012, GFDCC preterminated the loan facility and paid BOC the remaining balance including applicable interest (Note 34).
- u. The amount represents the US\$480 term loan facility signed and executed by Petron on September 30, 2011. The facility is amortized over 5 years with a 2-year grace period and is subject to a floating interest rate plus a fixed spread. The loan proceeds will be used to finance the capital expenditure requirements of the Refinery Master Plan Phase 2 (RMP-2) Project. The first drawdown of US\$80 was made on November 25, 2011. Petron availed of the remaining US\$400 of the term loan facility on February 15, 2012. A partial payment of US\$180 was made on June 29, 2012.

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Unamortized debt issue costs related to the loan amounted to ₱393 and ₱71 as of December 31, 2012 and 2011, respectively.

- v. The amount represents a five-year term loan facility signed by Petron on October 31, 2012, amounting to US\$485 with a syndicate of nine banks. The proceeds will be used partly to finance the capital expenditure requirements of RMP-2 Project. Amortization in seven equal amounts will start in November 2014, with final amortization due in November 2017. An initial drawdown of US\$100 was made on November 9, 2012. Subsequent drawdown of US\$35 and US\$140 were made in December 2012. The remaining balance of US\$210 was drawn in the first quarter of 2013.

Unamortized debt issue costs related to this loan facility amounted to ₱367 as of December 31, 2012.

- w. The amount represents the US\$200, syndicated 3-year term loan facility which SMC Global has drawn on September 30, 2011. Pursuant to the Facility Agreement signed on March 31, 2011, the amount of the loan drawn will bear interest at the rate of the LIBOR plus margin, payable in arrears on the last day of the interest period. The facility agreement has a final maturity date of September 2014.

Unamortized debt issue costs related to the loan amounted to ₱26 and ₱55 as of December 31, 2012 and 2011, respectively.

- x. The amount represents an unsecured loan facility agreement entered into by SMB with an aggregate amount of US\$300, used to finance SMB's acquisition of the international beer and malt-based beverage business from the Parent Company. Interest rates for the foreign currency-denominated loan range from 2.31% to 2.40% and from 2.33% to 2.41% in 2012 and 2011, respectively.

In 2011, SMB obtained approval of all its lenders for its US\$300 Term Facility to maintain a minimum interest coverage ratio of 4.75:1 in lieu of a minimum current ratio of 1:1.

On April 13, 2012, SMB made a partial prepayment of its US\$300 Term Facility in the amount of US\$100. A subsequent partial pre-payment was made on April 27, 2012 in the amount of US\$50.

Unamortized debt issue costs related to this loan facility amounted to ₱89 and ₱246 as of December 31, 2012 and 2011, respectively.

- y. The amount represents US\$30 long-term loan drawn by SMBHK from BOC for working capital requirements (Note 34).

Unamortized debt issue costs related to this loan facility amounted to ₱4 as of December 31, 2012.

- z. The amount represents GSMI's 44.9% share of the unsecured, long-term, interest-bearing loan of TSML from Thai local and foreign banks used to finance TSML's plant construction and start-up operations. This loan is carried at amortized cost. It bears annual interest rate at the aggregate of applicable Thailand Baht floating-rate fix (THBFIX) and 1.75% per annum. TSML and the creditor entered into an agreement that changed the rate of interest to a fixed rate of 6.41% for the period from January 1 to June 30, 2010. The loan is payable every six (6) months at 5% and 10%, of the outstanding loan facilities starting March 14, 2009.
- aa. The amount represents drawdown by Petron from the US\$355 loan facility for general corporate purposes and refinancing of peso-denominated debts. Floating interest rate for the loan is 1, 3 or 6-month LIBOR plus a spread of 2.15%. Principal repayment is in 9 equal semi-annual installments of US\$39 beginning June 1, 2011. The loan was fully paid on June 1, 2012.

Unamortized debt issue costs related to this loan facility amounted to ₱233 as of December 31, 2011.

The debt agreements contain, among others, covenants relating to merger and consolidation, maintenance of certain financial ratios, working capital requirements, restrictions on loans and guarantees, disposal of a substantial portion of assets, significant changes in the ownership or control of subsidiaries, payments of dividends and redemption of capital stock.

As of December 31, 2012 and 2011, the Group is in compliance with the covenants of the debt agreements.

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	<i>Note</i>	<u>2012</u>	<u>2011</u>
Balance at beginning of year		₱ 2,555	₱2,334
Additions and reclassification		1,358	974
Amortization	31	(1,234)	(753)
Balance at end of year		<u>₱ 2,679</u>	<u>₱2,555</u>

Repayment Schedule

As of December 31, 2012, the annual maturities of long-term debt are as follows:

<u>Year</u>	<u>Gross amount</u>	<u>Debt issue costs</u>	<u>Net</u>
2013	₱ 3,373	₱ 94	₱ 3,279
2014	67,919	932	66,987
2015	70,918	965	69,953
2016	30,084	241	29,843
2017	29,004	237	28,767
2018 and thereafter	25,598	210	25,388
Total	<u>₱226,896</u>	<u>₱2,679</u>	<u>₱224,217</u>

Contractual terms of the Group's interest-bearing loans and borrowings and exposure to interest rate, foreign currency and liquidity risks are discussed in Note 41.

24. Other Noncurrent Liabilities

Other noncurrent liabilities consist of:

	<i>Note</i>	<u>2012</u>	<u>2011</u>
Payables on the purchase of shares of stock	5	₱1,108	₱1,276
ARO	4	997	1,061
Retirement liabilities	36	1,310	1,054
Obligation to ROP — service concession agreement	4,19,35	74	76
IRO	4	45	46
Redeemable preferred shares	4	13	12
Cash bonds, cylinder deposits and others	34	2,871	984
	41, 42	<u>₱6,418</u>	<u>₱4,509</u>

Redeemable preferred shares represent the preferred shares of TADHC. The preferred shares are cumulative, non-voting, redeemable and with liquidation preference. The shares are preferred as to dividends, which are given in the form of coupons, at the rate of 90% of the applicable base rate (i.e., one year PDST-F). The dividends are cumulative from and after the date of issue of the preferred shares, whether or not in any period the amount is covered by available unrestricted retained earnings.

The preferred shares will be mandatorily redeemed at the end of the ten-year period from and after the issuance of the preferred shares by paying the principal amount, plus all unpaid coupons (at the sole option of TADHC, the preferred shares may be redeemed earlier in whole or in part).

In the event of liquidation, dissolution, bankruptcy or winding up of the affairs of TADHC, the holders of the preferred shares are entitled to be paid in full, an amount equivalent to the issue price of such preferred shares plus all accumulated and unpaid dividends up to the current dividend period or proportionately to the extent of the remaining assets of TADHC, before any assets of TADHC will be paid or distributed to the holders of the common shares.

“Others” include amounts owed to related parties amounting to ₱66 as of December 31, 2012 (Note 34).

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25. Income Taxes

Deferred tax assets and liabilities arise from the following:

	<u>2012</u>	<u>2011</u>
Allowance for impairment losses on trade and other receivables and inventory	₱ 2,225	₱ 1,913
NOLCO	2,026	1,371
MCIT	519	65
Undistributed net earnings of foreign subsidiaries	(5,395)	(7,669)
Unrealized intercompany charges and others	(2,633)	1,296
	<u>(₱ 3,258)</u>	<u>(₱ 3,024)</u>

The above amounts are reported in the consolidated statements of financial position as follows:

	<u>Note</u>	<u>2012</u>	<u>2011</u>
Deferred tax assets	4	₱ 8,826	₱ 8,233
Deferred tax liabilities		(12,084)	(11,257)
		<u>(₱ 3,258)</u>	<u>(₱ 3,024)</u>

The undistributed earnings of foreign subsidiaries and cumulative translation adjustments for which deferred tax liabilities have not been recognized amounted to ₱6,114 and ₱4,976 as of December 31, 2012 and 2011, respectively.

As of December 31, 2012, the NOLCO and MCIT of the Group that can be claimed as deduction from future taxable income and deduction from corporate income tax due, respectively, are as follows:

<u>Year incurred/paid</u>	<u>Carryforward benefits up to</u>	<u>NOLCO</u>	<u>MCIT</u>
2010	December 31, 2013	₱2,228	₱ 1
2011	December 31, 2014	1,244	68
2012	December 31, 2015	3,281	450
		<u>₱6,753</u>	<u>₱519</u>

The components of income tax expense are shown below:

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Current	₱9,248	₱12,240	₱11,517
Deferred	(436)	(3,757)	(79)
	<u>₱8,812</u>	<u>₱ 8,483</u>	<u>₱11,438</u>

The reconciliation between the statutory income tax rate on income before income tax and the Group's effective income tax rate is as follows:

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Statutory income tax rate	30.00%	30.00%	30.00%
Increase (decrease) in income tax rate resulting from:			
Interest income subject to final tax	(2.69)%	(3.75)%	(2.56)%
Equity in net earnings of associates	(1.70)%	(2.29)%	(5.76)%
Gain on sale of investments subject to final or capital gains tax	(2.50)%	(0.23)%	—
Loss (gain) on derivatives	0.80%	(0.15)%	(0.56)%
Others, mainly income subject to different tax rates — net	(5.33)%	(0.65)%	11.10
Effective income tax rate	<u>18.58%</u>	<u>22.93%</u>	<u>32.22%</u>

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26. Equity

a. Developments Relating to the Parent Company's Equity

Amendments to the Articles of Incorporation

On July 23, 2009, during the Parent Company's annual stockholders' meeting, the stockholders approved the amendments to the Parent Company's Articles of Incorporation providing for the declassification of the common shares of the Company. The authorized capital stock of the Parent Company amounting to ₱22,500 was divided into 2,034,000,000 Class "A" common shares, 1,356,000,000 Class "B" common shares and 1,110,000,000 Series "1" preferred shares, and defined the terms and features of the Series "1" preferred shares. The preferred shares are peso-denominated, perpetual, cumulative and non-voting with an issue price of ₱75.00 per share and a dividend rate of 8% per annum computed in reference to the issue price. The SEC approved the amendments to the Amended Articles of Incorporation of the Parent Company on August 20, 2009.

During the April 18, 2012 and June 14, 2012 meetings of the Parent Company's BOD and stockholders, respectively, the BOD and stockholders approved the amendments to the Parent Company's Articles of Incorporation to increase the authorized capital stock of the Parent Company from ₱22,500 to ₱30,000 as follows: (a) the increase in the number of the common shares from 3,390,000,000 common shares to 3,790,000,000, or an increase of 400,000,000 common shares; and (b) the creation and issuance of 1,100,000,000 Series "2" preferred shares with a par value ₱5.00 per share.

On September 21, 2012, the SEC approved the amendment to the Articles of Incorporation of the Parent Company to increase the authorized capital stock, and consequently creating the Series "2" Preferred Shares.

Exchange of Capital Stock

On July 23, 2009, the stockholders of the Parent Company approved the Offer by the Parent Company to exchange existing common shares of up to approximately 35% of the issued and outstanding capital stock of the Parent Company with Series "1" preferred shares. The exchange ratio was one (1) common share for one (1) Series "1" preferred share and the qualified shareholders of record as of July 2, 2009, were vested with the right to participate on the exchange.

On October 5, 2009, the Parent Company completed the exchange of 476,296,752 Class "A" common shares and 396,876,601 Class "B" common shares for Series "1" preferred shares.

Series "1" Preferred Shares

On October 15, 2009, the Parent Company's BOD approved the issuance, through private placement, of up to 226,800,000 Series "1" preferred shares.

On December 22, 2009, the Parent Company issued 97,333,000 Series "1" preferred shares to qualified buyers and by way of private placement to not more than 19 non-qualified buyers at the issue price of ₱75.00 per Series "1" preferred share.

Series "2" Preferred Shares

On June 26, 2012, the Parent Company filed with the SEC a Notice of Filing of Registration Statement for the registration of up to 1,067,000,000 Series "2" Preferred Shares with par value of ₱5.00 per share, to be offered by way of public offering, inclusive of shares for oversubscription.

b. Capital Stock

Common Shares

On July 27, 2010, the Parent Company's BOD approved the offer to issue approximately 1,000,000,000 common shares (from unissued capital stock and treasury shares) at a price of not less than ₱75.00 per share.

Effective August 26, 2010, all Class "A" common shares and Class "B" common shares of the Parent Company were declassified and are considered as common shares without distinction, as approved by the SEC. Both shall be available to foreign investors, subject to the foreign ownership limit.

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As of December 31, 2012, the Parent Company has a total of 38,999 common stockholders.

The movements in the number of issued and outstanding shares of common stock are as follows:

	<i>Note</i>	2012	2011	2010
Balance at beginning of year		3,279,334,575	3,268,594,254	3,229,944,942
Issuances during the year	40	2,211,715	10,740,321	38,649,312
Issued shares at end of year		3,281,546,290	3,279,334,575	3,268,594,254
Less treasury shares		908,892,669	910,303,273	938,648,724
Issued and outstanding shares at end of year		<u>2,372,653,621</u>	<u>2,369,031,302</u>	<u>2,329,945,530</u>

Preferred Shares

I. Series “1” Preferred Shares

Series “1” preferred shares have a par value of ₱5.00 per share and are entitled to receive cash dividends upon declaration by and at the sole option of the Parent Company’s BOD at a fixed rate of 8% per annum calculated in respect of each Series “1” preferred share by reference to the Issue Price thereof in respect of each dividend period. Unless the Series “1” preferred shares are redeemed by the Parent Company, the dividend rate will be adjusted at the end of the fifth year after the date of issue.

Series “1” preferred shares are non-voting except as provided for under the Corporation Code. The Series “1” preferred shares are redeemable in whole or in part, at the sole option of the Parent Company, at the end of three years from the issue date at ₱75.00 plus any accumulated and unpaid cash dividends.

All shares rank equally with regard to the Parent Company’s residual assets, except that holders of preferred shares participate only to the extent of the issue price of the shares plus any accumulated and unpaid cash dividends.

On October 3, 2011 and December 8, 2010, the Parent Company listed 97,333,000 and 873,173,353 Series “1” preferred shares worth ₱7,300 and ₱65,488, respectively.

As of December 31, 2011, the Parent Company has 970,506,353 outstanding Series “1” preferred shares and has a total of 954 preferred stockholders.

On August 13, 2012, the BOD of the Parent Company approved the redemption of Series “1” preferred shares at a redemption price of ₱75.00 per share. The redemption took effect on October 5, 2012 and accordingly, the proceeds of the shares and all accumulated unpaid cash dividends were paid on the same date to stockholders of record as of September 11, 2012.

II. Series “2” Preferred Shares

Series “2” preferred shares consisting of 1,067,000,000 shares were fully subscribed at the issue price of ₱75.00 per share. The Series “2” preferred shares were issued in three sub-series (Subseries “2-A”, Subseries “2-B” and Subseries “2-C”) and are peso-denominated, perpetual, cumulative, non-participating and non-voting.

The Parent Company has the redemption option starting on the 3rd, 5th and 7th year and every dividend payment thereafter, with a “step-up” rate effective on the 5th, 7th and 10th year, respectively, if the shares are not redeemed. Dividend rates are 7.500%, 7.625% and 8.000% per annum for Subseries “2-A”, “2-B” and “2-C”, respectively.

Bulk of the proceeds from the issuance of Series “2” preferred shares were used by the Parent Company to redeem the Series “1” Preferred Shares as well as for general corporate purposes, including short-term debt repayment.

On September 28, 2012, the Parent Company listed the Series “2” preferred shares at the PSE.

As of December 31, 2012, the Parent Company has 1,067,000,000 outstanding Series “2” preferred shares and has a total of 461 preferred stockholders.

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c. Treasury Shares

1. Common shares

The movements in the number of common shares held in treasury are as follows:

	<i>Note</i>	2012	2011	2010
Balance at beginning of year		910,303,273	938,648,724	938,648,724
Reissuance of treasury shares during the year		—	(27,580,000)	—
Conversion of exchangeable bonds	23	(1,410,604)	(765,451)	—
Balance at end of year		<u>908,892,669</u>	<u>910,303,273</u>	<u>938,648,724</u>

Treasury shares, totaling 65,475,371 common shares, are stated at acquisition cost amounting to ₱4,053, while 873,173,353 common shares were acquired through the exchange of common shares to preferred shares on a one-for-one basis at ₱75.00 per share amounting to ₱65,488.

1. A portion of the total treasury shares of the Parent Company came from 25,450,000 common shares, with an acquisition cost of ₱481, [net of the cost of the 1,000,000 shares paid to Presidential Commission on Good Government (PCGG) as arbitral fee pursuant to the Compromise Agreement, as herein defined] which were reverted to treasury in 1991 upon implementation of the Compromise Agreement and Amicable Settlement (Compromise Agreement) executed by the Parent Company with the United Coconut Planters Bank (UCPB) and the Coconut Industry Investment Fund (CIIF) Holding Companies in connection with the purchase of the Parent Company shares under an agreement executed on March 26, 1986.

Certain parties have opposed the Compromise Agreement. The right of such parties to oppose, as well as the propriety of their opposition, has been the subject matters of cases before the Sandiganbayan and the Supreme Court.

On September 14, 2000, the Supreme Court upheld a Sandiganbayan resolution requiring the Parent Company to deliver the 25,450,000 common shares that were reverted to treasury in 1991 to the PCGG and to pay the corresponding dividends on the said shares (the “Sandiganbayan Resolution”).

On October 10, 2000, the Parent Company filed a motion for reconsideration with the Supreme Court to be allowed to comply with the delivery and payment of the dividends on the treasury shares only in the event that another party, other than the Parent Company, is declared owner of the said shares in the case for forfeiture (Civil Case) filed by the Philippine government (Government).

On April 17, 2001, the Supreme Court denied the motion for reconsideration.

On September 19, 2003, the PCGG wrote the Parent Company to deliver to the PCGG the stock certificates and cash and stock dividends under the Sandiganbayan Resolution upheld by the Supreme Court. The Parent Company referred the matter to its external financial advisor and external legal counsel for due diligence and advice. The external financial advisor presented to the BOD on December 4, 2003 the financial impact of compliance with the resolution considering “with and without due compensation” scenarios, and applying different rates of return to the original amount paid by the Parent Company. The financial advisor stated that if the Parent Company is not compensated for the conversion of the treasury shares, there will be: (a) a negative one-off EPS impact in 2003 of approximately 17.5%; (b) net debt increase of approximately ₱2,100; and (c) a negative EPS impact of 6.9% in 2004. The external legal counsel at the same meeting advised the BOD that, among others, the facts reviewed showed that: (a) the compromise shares had not been validly sequestered; (b) no timely direct action was filed to nullify the transaction; (c) no rescission can be effected without a return of consideration; and (d) more importantly, requiring the Parent Company to deliver what it acquired from the sellers without a substantive ground to justify it, and a direct action in which the Parent Company is accorded full opportunity to defend its rights, would appear contrary to its basic property and due process rights. The external legal counsel concluded that the Parent Company has “legal and equitable grounds to challenge the enforcement” of the Sandiganbayan Resolution.

On January 29, 2004, the external legal counsel made the additional recommendation that the Parent Company should file a Complaint-in-Intervention in the Civil Case (now particularly identified as SB Civil Case No. 0033-F), the forfeiture case brought by the Government involving the so-called CIIF block of the

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Parent Company shares of stock of which the treasury shares were no longer a portion. The Complaint-in-Intervention would pray that any judgment in the Civil Case forfeiting the CIIF block of the Parent Company shares of stock should exclude the treasury shares.

At its January 29, 2004 meeting, the BOD of the Parent Company unanimously decided to: (a) deny the PCGG demand of September 19, 2003, and (b) authorize the filing of the Complaint-in-Intervention. Accordingly, the external legal counsel informed the PCGG of the decision of the Parent Company and the Complaint-in-Intervention was filed in the Civil Case.

In a Resolution dated May 6, 2004, the Sandiganbayan denied the Complaint-in-Intervention. The external legal counsel filed a Motion for Reconsideration, which was denied by the Sandiganbayan in its Decision dated November 28, 2007.

The external legal counsel advised that because the Sandiganbayan had disallowed the Parent Company's intervention, the Sandiganbayan's disposition of the so-called CIIF block of the Parent Company shares in favor of the Government cannot bind the Parent Company, and that the Parent Company remains entitled to seek the nullity of that disposition should it be claimed to include the treasury shares.

The external legal counsel also advised that the Government has, in its own court submissions: (i) recognized the Parent Company's right to the treasury shares on the basis that the Compromise Agreement is valid and binding on the parties thereto; and (ii) taken the position that the Parent Company and UCPB had already implemented the Compromise Agreement voluntarily, and that the PCGG had conformed to the Agreement and its implementation. The Executive Committee of the Parent Company approved the recommendation of external legal counsel on January 18, 2008 which was ratified by the BOD on March 6, 2008.

On July 23, 2009, the stockholders of the Parent Company approved the amendment of the Articles of Incorporation to issue Series "1" preferred shares, and the offer to exchange common shares to Series "1" preferred shares. The PCGG, with the approval of the Supreme Court in its Resolution dated September 17, 2009, converted the sequestered common shares in the Parent Company in the name of the CIIF Holding Companies, equivalent to 24% of the outstanding capital stock, into Series "1" preferred shares. On February 11, 2010, the Supreme Court, amending its Resolution dated September 17, 2009, authorized the PCGG to exercise discretion in depositing in escrow, the net dividend earnings on, and/or redemption proceeds from, the Series "1" preferred shares of the Parent Company, either with the Development Bank of the Philippines/Land Bank of the Philippines or with the UCPB. All dividends accruing to the Series "1" preferred shares are remitted to the escrow account established with UCPB. On October 5, 2012, the Parent Company redeemed all Series "1" preferred shares including those Series "1" preferred shares in the name of the CIIF Holding Companies. Proceeds of such redemption with respect to Series "1" preferred shares in the name of the CIIF Holding Companies, including all accumulated dividends were paid to the National Treasury. As of October 5, 2012, CIIF Holding Companies are no longer stockholders of the Parent Company.

On June 30, 2011, the PCGG filed with the Supreme Court relating to an Urgent Motion to Direct the Parent Company to comply with the Sandiganbayan Resolution (the "Urgent Motion"). On March 30, 2012, the Parent Company filed a Comment on the Urgent Motion in compliance with the Supreme Court's Resolution dated December 13, 2011 which was received by the Parent Company on February 22, 2012, directing the Parent Company to file its Comment on the Urgent Motion. As of December 31, 2012, there are no new developments on the Urgent Motion.

In the meantime, the Parent Company has available cash and shares of stock for the dividends payable on the treasury shares, in the event of an unfavorable ruling by the Supreme Court.

2. On May 5, 2011, the Parent Company completed the secondary offering of its common shares. The offer consists of 110,320,000 shares of stock of the Parent Company consisting of 27,580,000 common shares from treasury shares of the Parent Company and 82,740,000 common shares of Top Frontier. In addition, Top Frontier sold to ATR Kim Eng Capital Partners, Inc., BDO Capital & Investment Corporation and SB Capital Investment Corporation an additional 27,580,000 Offer Shares. The Parent Company likewise granted Credit Suisse (Singapore) Pte., Standard Chartered Securities (Singapore) Pte. Limited, Goldman Sachs (Singapore) Pte., and UBS AG an option, exercisable in whole or in part for thirty (30) days from the

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date of allotment of Offer Shares in the international offer, to procure purchasers for up to 7,880,000 additional Common Shares, solely to cover over-allotments under the Offer, if any. The 7,880,000 common shares which were not utilized were reverted to treasury shares. The Offer Shares were priced at ₱110.00 per share on April 20, 2011.

3. Also on May 5, 2011, US\$600 worth of exchangeable bonds of the Parent Company sold to overseas investors were simultaneously listed at the SGX-ST. The exchangeable bonds have a maturity of three years, a coupon of 2% per annum and a conversion premium of 25% of the offer price. The exchangeable bonds will be exchangeable for common shares from the treasury shares of the Parent Company. The initial exchange price for the exchange of the exchangeable bonds into Common Shares is ₱137.50 per share.

On December 5, 2011, 765,451 common shares were delivered to the bondholders of the Parent Company's exchangeable bonds who exercised their exchange rights under the terms and conditions of the bonds at an exchange price of ₱113.24 per share. Subsequently on December 8, 2011 and February 10, 2012, the delivered common shares of stock of the Parent Company were transacted and crossed at the PSE via a special block sale in relation to the issuance of common shares pursuant to the US\$600 exchangeable bonds of the Parent Company.

On various dates in 2012, additional 1,410,604 common shares were delivered to the bondholders of the Parent Company's exchangeable bonds who exercised their exchange rights under the terms and conditions of the bonds at exchange prices ranging from ₱109.80 to ₱113.24 per share. Of the 1,410,604 common shares delivered, 1,094,832 common shares of stock of the Parent Company were transacted and crossed at the PSE on various dates via a special block sale in relation to the issuance of common shares pursuant to the US\$600 exchangeable bonds of the Parent Company.

As of December 31, 2012, US\$5.6 worth of exchangeable bonds were already exchanged to equity into common shares (Note 23).

II. Series "1" Preferred Shares

On August 13, 2012, the BOD of the Parent Company approved the redemption of Series "1" preferred shares at a redemption price of ₱75.00 per share. On October 5, 2012, 970,506,353 Series "1" preferred shares were held in treasury and were no longer outstanding but remain unissued as of December 31, 2012.

d. Unappropriated Retained Earnings

The Group's unappropriated retained earnings includes the accumulated earnings in subsidiaries and equity in net earnings of associates amounting to ₱45,787, ₱44,000 and ₱55,565 in 2012, 2011 and 2010, respectively. Such amounts are not available for declaration as dividends until declared by the respective investees.

The Parent Company's unappropriated retained earnings is restricted in the amount of ₱140,124, ₱67,441 and ₱69,541 as of December 31, 2012, 2011 and 2010, respectively, representing the cost of shares held in treasury.

e. Appropriated Retained Earnings

The BOD of certain subsidiaries approved additional appropriations amounting to ₱5,904, ₱18,650 and ₱201 in 2012, 2011 and 2010, respectively, to finance future capital expenditure projects. Reversal of appropriations amounted to ₱3,000, ₱6 and ₱27 in 2012, 2011 and 2010, respectively.

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27. Cost of Sales

Cost of sales consists of:

	<i>Note</i>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Inventories		₱468,805	₱315,700	₱ 88,347
Energy fees		33,150	30,263	15,875
Taxes and licenses		30,803	30,219	23,343
Fuel and oil		13,269	11,947	10,657
Depreciation, amortization and impairment	29	13,166	12,625	7,287
Contracted services		7,476	6,592	5,929
Freight, trucking and handling		6,842	5,563	5,504
Communications, light and water		5,602	5,252	4,585
Personnel	30	4,981	4,532	3,827
Power purchase		4,452	4,416	4,791
Repairs and maintenance		3,424	2,255	1,962
Rent	4, 35	756	879	517
Others		2,006	2,078	1,305
		<u>₱594,732</u>	<u>₱432,321</u>	<u>₱173,929</u>

28. Selling and Administrative Expenses

Selling and administrative expenses consist of:

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Selling	₱28,999	₱24,222	₱18,239
Administrative	22,354	23,278	19,380
	<u>₱51,353</u>	<u>₱47,500</u>	<u>₱37,619</u>

Selling expenses consist of:

	<i>Note</i>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Freight, trucking and handling		₱ 7,737	₱ 6,665	₱ 5,922
Advertising and promotions		7,108	5,528	4,977
Personnel	30	6,880	5,844	4,180
Depreciation, amortization and impairment	29	2,239	1,434	419
Rent	4, 35	2,233	1,650	1,200
Taxes and licenses		524	484	271
Professional fees		487	313	131
Supplies		422	897	326
Communications, light and water		396	347	193
Others		973	1,060	620
		<u>₱28,999</u>	<u>₱24,222</u>	<u>₱18,239</u>

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Administrative expenses consist of:

	<i>Note</i>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Personnel	30	₱10,077	₱10,965	₱ 8,090
Depreciation, amortization and impairment	29	4,638	3,387	2,403
Professional fees		2,016	2,083	1,802
Taxes and licenses		1,119	1,197	803
Advertising and promotion		1,105	1,178	1,201
Repairs and maintenance		833	690	681
Communications, light and water		745	627	715
Supplies		682	436	755
Freight, trucking and handling		269	343	513
Research and development		119	146	333
Rent	4, 35	35	46	95
Others	40	716	2,180	1,989
		<u>₱22,354</u>	<u>₱23,278</u>	<u>₱19,380</u>

“Others” consist of entertainment and amusement, gas and oil, and other operating and administrative expenses.

29. Depreciation, Amortization and Impairment

Depreciation, amortization and impairment are distributed as follows:

	<i>Note</i>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Cost of sales:				
Property, plant and equipment	7,16	₱12,021	₱11,436	₱ 6,192
Deferred containers, biological assets and others	18,20	1,145	1,189	1,095
	27	<u>13,166</u>	<u>12,625</u>	<u>7,287</u>
Selling and administrative expenses:				
Property, plant and equipment	7,16	4,027	3,207	1,685
Deferred containers and others	20,33	2,850	1,614	1,137
	28	<u>6,877</u>	<u>4,821</u>	<u>2,822</u>
		<u>₱20,043</u>	<u>₱17,446</u>	<u>₱10,109</u>

“Others” include amortization of computer software, land use rights, licenses and investment properties.

30. Personnel Expenses

Personnel expenses consist of:

	<i>Note</i>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Salaries and wages		₱11,009	₱10,086	₱ 7,997
Retirement costs (benefits)	36	(282)	1,019	285
Other employee benefits		11,211	10,236	7,815
		<u>₱21,938</u>	<u>₱21,341</u>	<u>₱16,097</u>

Personnel expenses are distributed as follows:

	<i>Note</i>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Cost of sales	27	₱ 4,981	₱ 4,532	₱ 3,827
Selling expenses	28	6,880	5,844	4,180
Administrative expenses	28	10,077	10,965	8,090
		<u>₱21,938</u>	<u>₱21,341</u>	<u>₱16,097</u>

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31. Interest Expense and Other Financing Charges

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Interest expense	₱26,878	₱25,698	₱13,870
Other financing charges	2,948	1,745	2,708
	<u>₱29,826</u>	<u>₱27,443</u>	<u>₱16,578</u>

Amortization of debt issue costs included in “Other financing charges” amounted to ₱1,234, ₱753 and ₱1,808 in 2012, 2011 and 2010, respectively (Note 23).

Interest expense on loans payable, long-term debt and finance lease liabilities is as follows:

	<u>Note</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Loans payable	21	₱ 5,421	₱ 7,392	₱ 3,035
Long-term debt and finance lease liabilities	23,35	21,457	18,306	10,835
		<u>₱26,878</u>	<u>₱25,698</u>	<u>₱13,870</u>

32. Interest Income

Interest income consists of:

	<u>Note</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Interest from short-term investments, cash in banks and others		₱2,731	₱3,545	₱2,899
Interest on amounts owed by related parties	34,36	1,523	1,073	124
		<u>₱4,254</u>	<u>₱4,618</u>	<u>₱3,023</u>

33. Other Income (Charges)

Other income (charges) consists of:

	<u>Note</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Foreign exchange gains (losses)	41	₱11,375	(₱ 823)	₱ 6,097
Reversal (loss) on impairment of goodwill, trademarks and brand names, property, plant and equipment and idle assets (a, b)	16,19,20	1,060	(36)	(4,233)
PSALM monthly fees reduction		918	445	395
Gain on acquisition of a subsidiary	5,39	—	—	4,490
Gains (losses) on derivatives — net	42	(1,270)	182	660
Others (c, d)		898	220	(314)
		<u>₱12,981</u>	<u>(₱ 12)</u>	<u>₱ 7,095</u>

- a. In 2011 and 2010, the Group recognized impairment loss on noncurrent assets of SMBHK and San Miguel (Guangdong) Brewery Company Limited (SMGB). Over the past two years, the business performance of SMBHK and SMGB had been adversely affected by factors such as economic downturns, fierce market competition, counterfeit products and poor weather conditions.

SMBHK

The Group’s noncurrent assets relating to the manufacturing operations in SMBHK comprise mainly of the production plant, an office building and a warehouse (the SMBHK CGU). The recoverable amount of the SMBHK CGU has been determined using the value in use calculation derived on the cash flow projections based on the business forecasts approved by management covering a period of five years on which cash flows beyond the covered periods are extrapolated using a steady growth rate of 2%. This growth rate does not exceed the long-term average growth rate for SMBHK.

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Key assumptions used for value in use calculation are as follows:

	<u>2011</u>	<u>2010</u>
Sales volume growth rate	1.1 -12.4%	1.7 -12.6%
Gross contribution rate	38 -41%	40 -43%
Pre-tax discount rate	9.75%	9.85%

In 2011, the Group's results in SMBHK were fairly consistent with the forecasts made in 2010.

In 2012, there was a change in the estimates used to determine the SMBHK CGU's recoverable amount as the Group was able to determine fair value less costs to sell based on a reliable estimate of the amount obtainable from the sale in an arm's length transaction between knowledgeable and willing parties for most of the assets belonging to the SMBHK CGU, due to recent comparable transaction data becoming available. The fair value less costs to sell of the SMBHK CGU was greater than the value-in-use as of December 31, 2012. Hence, the Group reversed the amount of ₱1,448, a part of previously recognized impairment losses in respect of SMBHK CGU. The reversal is only to the extent that the revised carrying amount of individual assets does not exceed the smaller of respective fair value less costs to sell as of December 31, 2012 and what would have been determined had no impairment loss been recognized in prior years.

SMGB

In 2012, 2011 and 2010, the Group noted that the decline in demand for its products in mainland China compared to previous sales forecasts, fierce market competition and the operating losses that consequently arose, were indications that noncurrent assets of the operations in mainland China, comprising mainly of the production plant located in Shunde, Guangdong Province and other tangible assets may be impaired. The Group recognized an impairment loss amounting to ₱20 in 2012.

The estimates of recoverable amount of the SMGB CGU were based on the assets' fair values less costs to sell, determined by reference to the observable market prices for similar assets. The assessment was made by LCH (Asia-Pacific) Surveyor Limited, an independent firm of surveyors who are members of the Hong Kong Institute of Surveyors which was engaged by the Group.

Based on the Group's assessment of the recoverable amounts of the CGUs to which these assets belong, the carrying amounts of the assets in the CGUs were written down (up) by (₱1,428) and ₱30, as of December 31, 2012 and 2011, respectively, presented as follows:

	<u>Note</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Selling and administrative expenses	28	₱ —	₱ —	₱ 151
Other charges (income)		(1,428)	30	4,182
		<u>(₱ 1,428)</u>	<u>₱ 30</u>	<u>₱ 4,333</u>

In 2010, a reversal of an impairment loss amounting to ₱235 was made with respect to land use rights, as there has been a favorable change in the estimates used to determine the recoverable amount.

- b. In 2010, the Group recognized impairment loss on idle assets amounting to ₱51 and reversed the Group's 2009 impairment loss on land amounting to ₱46, computed as the difference between the carrying amount of the assets and their fair value based on reports by qualified property appraisers, less costs to sell.
- c. On January 11, 2011, SMPI entered into a contract with the Philippine Foundation of Blessed Mary Mother of the Poor, Inc. (the "Foundation"), a non-profit religious organization, for the donation of a 33-hectare parcel of land located in Alfonso, Cavite (the "Donated Property"). The land title of the Donated Property was transferred in the name of the Foundation on April 28, 2011.

In accordance with the Deed of Donation, the Donated Property shall be used and devoted exclusively by the Foundation for the construction, operation and maintenance of its project, the Montemaria Oratory of the Blessed Virgin Mary (the "Montemaria Project"). The Montemaria Project will consist of a Shrine of the Blessed Virgin Mary, churches and chapels, Way of the Cross and such other structures and facilities for Roman Catholic religious purposes, and socio-civic and non-profit activities and program of the Foundation.

Further, the Deed of Donation requires that the Montemaria Project must be at least 50% completed by 2015 and fully completed by 2020. If the Foundation will not be able to comply with this requirement, the Donated Property will revert back to SMPI.

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On February 8, 2012, SMPI received a letter from the Foundation conveying its intention of returning portion of the Donated Property. SMPI's BOD is yet to decide on the appropriate action for the said request. As of December 31, 2012, portion of the Donated Property has not yet been returned to SMPI pending the final resolution of the Foundation's new set of Board of Trustees.

As of December 31, 2012, the Foundation has not yet started with the development of Montemaria Project.

- d. "Others" consist of rent income, commission income, dividend income from AFS financial assets, changes in fair value of financial assets at FVPL, gain on settlement of ARO and insurance claims.

34. Related Party Disclosures

The Parent Company, certain subsidiaries and their shareholders, and associates in the normal course of business, purchase products and services from one another. Transactions with related parties are made at normal market prices and terms. An assessment is undertaken at each financial year by examining the financial position of the related party and the market in which the related party operates.

	<i>Note</i>	<i>Year</i>	<i>Revenue from related parties</i>	<i>Purchases from related parties</i>	<i>Amounts owed by related parties</i>	<i>Amounts owed to related parties</i>	<i>Terms</i>	<i>Conditions</i>
Retirement plans . . .	10, 20, 36	2012	₱ —	₱ —	₱21,601	₱ —	On demand; Interest bearing	Unsecured; No impairment
		2011	—	—	29,139	—		
		2010	—	—	26,569	1,800		
Associates	10, 22, 24	2012	53,210	481	10,680	61	On demand; Non-interest bearing	Unsecured; No impairment
		2011	33,013	494	7,741	60		
		2010	17,103	490	7,323	43		
	21, 23	2012	—	—	—	9,045	Less than 1 to 10 years Interest bearing	Unsecured
		2011	—	—	—	3,360		
JVC	20	2012	—	—	118	—	On demand; Non-interest bearing	Unsecured; No impairment
		2011	—	—	118	—		
Shareholders in subsidiaries	10, 22, 24	2012	—	34	183	557	On demand; Non-interest bearing	Unsecured; No impairment
		2011	—	—	19	—		
		2010	—	—	11	—		
Others	10, 22	2012	—	—	24	18	On demand; Non-interest bearing	Unsecured; No impairment
		2011	51	1,487	728	266		
		2010	43	105	9	712		
Total		2012	₱53,210	₱ 515	₱32,606	₱9,681		
Total		2011	₱33,064	₱1,981	₱37,745	₱3,686		
Total		2010	₱17,146	₱ 595	₱33,912	₱2,555		

- a. Amounts owed by related parties consist of trade and non-trade receivables and share in expenses.
- b. Amounts owed to related parties consist of trade payables and professional fees.
- c. The amounts owed to associates include interest bearing loans to BOC included as part of "Loans payable" and "Long-term debt" accounts in the consolidated statements of financial position.
- d. The compensation of key management personnel of the Group, by benefit type, follows:

	2012	2011	2010
Short-term employee benefits	₱ 447	₱475	₱ 408
Share-based payments	17	29	31
Retirement benefits	(251)	(52)	(147)
	₱ 213	₱452	₱ 292

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Some of the personnel performing key management functions in certain subsidiaries are employed by the Parent Company. This is covered by a management agreement executed by and between the Parent Company and the subsidiaries. The salaries and benefits of these personnel are billed to the subsidiaries through management fees, with details as follows:

	<u>Note</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Short-term employee benefits		₱31	₱ 7	₱30
Share-based payments	40	22	25	24
Retirement costs	36	1	—	—
	28, 30	<u>₱54</u>	<u>₱32</u>	<u>₱54</u>

35. Significant Agreements and Lease Commitments

Significant Agreements:

Power

Independent Power Producer (IPP) Administration (IPPA) Agreements

As a result of the biddings conducted by PSALM for the Appointment of the IPP Administrator for the Contracted Capacity of the following power plants, the Group was declared the winning bidder through the following subsidiaries:

<u>Subsidiary</u>	<u>Power plant</u>	<u>Contracted capacity</u>	<u>Location</u>	<u>Date awarded</u>	<u>Effective date</u>
SMEC	Sual Coal — Fired Power Station (Sual Power Plant)	2 x 500 MW	Sual, Pangasinan Province	September 1, 2009	November 6, 2009
SPDC	San Roque Multi-Purpose Hydroelectric Power Plant (San Roque Power Plant)	345 MW	San Roque, Pangasinan Province	December 28, 2009	January 26, 2010
SPPC	Ilijan Natural Gas — Fired Combined Cycle Power Plant (Ilijan Power Plant)	1,200 MW	Ilijan, Batangas City	May 5, 2010	June 26, 2010

The IPPA Agreements are with the conformity of National Power Corporation (NPC), a government-owned and controlled corporation created by virtue of RA No. 6395, as amended, whereby NPC confirms, acknowledges, approves and agrees to the terms of the Agreement and further confirms that as long as it remains the IPP Counterparty it will comply with its obligations and exercise its rights and remedies under the original agreement with the IPP at the request and instruction of PSALM.

The IPPA Agreements include, among others, the following common salient rights and obligations:

- i. The right and obligation to manage and control the contracted capacity of the power plant for its own account and at its own cost and risks;
- ii. The right to trade, sell or otherwise deal with the capacity (whether pursuant to the spot market, bilateral contracts with third parties or otherwise) and contract for or offer related ancillary services, in all cases for its own account and at its own risk and cost. Such rights shall carry the rights to receive revenues arising from such activities without obligation to account therefore to PSALM or any third party;
- iii. The right to receive a transfer of the power plant in case of buy-out or termination of the Agreement for no consideration;

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- iv. The right to receive an assignment of NPC interest to existing short-term bilateral power supply contracts;
- v. The obligation to supply and deliver, at its own cost, fuel required by the IPP and necessary for the Sual Power Plant to generate the electricity required to be produced by the IPP;
- vi. Maintain the performance bond in full force and effect with a qualified bank; and
- vii. The obligation to pay PSALM the monthly payments and generation fees in respect of all electricity generated from the capacity, net of outages for SMEC.
- viii. Relative to the IPPA Agreements, SMEC, SPDC and SPPC have to pay PSALM monthly fees for 15 years until October 1, 2024, 18 years until April 26, 2028 and 12 years until June 26, 2022, respectively. SMEC, SPDC and SPPC renewed their performance bonds in US dollar amounting to US\$58, US\$20 and US\$60, which will expire on November 3, 2013, January 25, 2013 and June 16, 2013, respectively.

In view of the nature of the IPPA Agreements, the arrangement has been accounted for as finance lease.

Market Participation Agreements (MPA)

SMEC, SPDC and SPPC have entered into MPA with the Philippine Electricity Market Corporation (PEMC) to satisfy the conditions contained in the Philippine WESM Rules on WESM membership and to set forth the rights and obligations of a WESM member.

Under the WESM Rules, the cost of administering and operating the WESM shall be recovered through a charge imposed on all WESM members or transactions, as approved by ERC.

The Group purchases power from WESM during periods when the power generated from power plants is not sufficient to meet customers' power requirements.

Power Supply Agreements

SMEC and SPPC have Power Supply Agreements with various counterparties including related parties, to supply or sell electricity produced by the power plants. All agreements provide for renewals or extensions subject to mutually agreed terms and conditions by both parties.

The customers are billed based on the time-of-use per kilowatt hour. However, as stipulated in the contracts, each customer has to pay the minimum charge based on the contracted power using the basic energy charge and adjustments if customer has not fully taken or failed to consume the contracted power.

SMEC and SPPC also purchase power from WESM and other power generation companies during periods when the power generated from power plant is not sufficient to meet customers' power requirements.

In 2012, 2011 and 2010, all customers are above their minimum contracted power requirements.

Coal Supply Agreement

SMEC renewed the Supply Agreement for Steaming Coal with PT Bumi Resources Tbk's subsidiary PT Kaltim Prima Coal, BANPU Public Company Limited Thailand and Noble Resources Pte. Ltd. (the Coal Suppliers) through Topcoal Trading Corporation for the coal requirements of the Sual Power Plant. Under the agreement, the parties shall negotiate and agree on the contract price of the coal at least 30 days prior to the delivery. On August 18, 2011, the parties desired to further extend the Agreement which may be further extended upon mutual agreement of the parties. On October 1, 2012, the Coal Supply Agreement was assigned to SMEC by Topcoal with the consent of the Coal Suppliers.

Fuel and Oil

Supply Agreement

Petron has assigned all its rights and obligations to Petron Singapore Trading Pte. Ltd. (as Assignee) to have a term contract to purchase Petron's crude oil requirements from Saudi Arabian American Oil Company (Saudi Aramco), based on the latter's standard Far East selling prices. The contract is for a period of one year from October 28, 2008 to October 27, 2009 with automatic one-year extensions thereafter unless terminated at the option of either party, within 60 days written notice. Outstanding liabilities of Petron for such purchases are included as part of "Accounts payable and accrued expenses" account in the consolidated statements of financial position as of December 31, 2012 and 2011 (Note 22). The contract is extended until October 27, 2013.

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Petron Malaysia has a service level agreement with Concord Energy Ltd. (Concord Energy). Under this agreement, effective until March 31, 2013, Concord Energy shall act as Petron Malaysia's commercial trader in relation to all spot & term transactions for the import & export of Crude Oil and Refined Petroleum Products. This shall exclude domestic sale and purchase. This covers the monthly purchase of Tapis Blend Crude Oil & Terengganu Condensate from ExxonMobil Exploration and Production Malaysia.

Supply Contract with NPC and PSALM

Petron entered into various fuel supply contracts with NPC and PSALM. Under these contracts, Petron supplies the bunker fuel and diesel fuel oil requirements of selected NPC plants and PSALM plants, and NPC-supplied IPP plants.

Infrastructure

Concession Agreements

• TADHC

In 2009, the ROP awarded TADHC the Airport Project through a Notice of Award (NOA) issued on May 15, 2009. The Project is proposed to be implemented through a Contract-Add-Operate and Transfer Arrangement, a variant of the Build-Operate-Transfer (BOT) contractual arrangement under RA No. 6957, as amended by RA No. 7718, otherwise known as the BOT Law, and its Revised Implementing Rules and Regulations.

On June 22, 2009, TADHC entered into a CA with the ROP, through the DOTC and Civil Aviation Authority of the Philippines. Based on the CA, TADHC has been granted with the concession of the Airport Project which includes the extension or expansion of the Boracay Airport. Subject to existing law, the CA also grants to TADHC the franchise to operate and maintain the Boracay Airport up to the end of the concession period, which is for a period of 25 years, and to collect the fees, rentals and other charges as may be agreed from time to time based on the Parametric Formula as defined in the CA.

The following are the salient features of the CA:

1. The operations and management of the Boracay Airport shall be transferred to TADHC, provided that the ROP shall retain the operations and control of air traffic services, national security matters, immigration, customs and other governmental functions and the regulatory powers insofar as aviation security, standards and regulations are concerned at the Boracay Airport.
2. As concessionaire, TADHC shall have full responsibility in all aspect of the operation and maintenance of the Boracay Airport and shall collect the regulated and other fees generated from it and from the end users. To guarantee faithful performance of its obligation in respect to the operation and maintenance of the Boracay Airport, TADHC shall post in favor of the ROP an Operations and Maintenance Performance Security (OMPS) amounting to ₱25, which must be valid for the entire concession period of 25 years. As of December 31, 2012 and 2011, TADHC has yet to pay the OMPS since it is payable only after the completion of the construction of the Airport Project.
3. Immediately upon receiving the Notice to Commence Implementation (NCI) and provided all conditions precedent in the CA are fulfilled and waived, TADHC shall start all the activities necessary to upgrade and rehabilitate the Boracay Airport into a larger and more technologically advanced aviation facility to allow international airport operations.
4. TADHC shall finance the cost of the Airport Project, while maintaining a debt-to-equity ratio of 70:30, with debt pertaining to third party loans. TADHC's estimated capital commitment to develop the Airport Project amounts to ₱2,500, including possible advances to the ROP for the right of way up to the amount of ₱466. Such ratio is complied with as TADHC fully issued its authorized capital stock as a leveraged to the loan obtained from third party.
5. TADHC shall also post a ₱250 Work Performance Security in favor of the ROP as guarantee for faithful performance by TADHC to develop the Airport Project. This performance security shall be partially released by the ROP from time to time to the extent of the percentage of completion of the Project. TADHC has paid ₱1 premium both in 2012 and 2011, for the Work Performance Security. The unamortized portion was presented as part of the "Prepaid expenses and other current assets" account in the consolidated statements of financial position as of December 31, 2012 and 2011 (Note 12).

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6. In consideration for allowing TADHC to operate and manage the Boracay Airport, TADHC shall pay ROP ₱8 annually. The first payment shall be made immediately upon the turnover by the ROP of the operations and management of the Boracay Airport to TADHC, and every year thereafter until the end of the concession period. The operations and management of the Boracay Airport was turned over to TADHC on October 16, 2010.

After fulfillment of all contractual and legal requirements, the CA became effective on December 7, 2009. The NCI issued to TADHC by the DOTC was accepted by TADHC on December 18, 2009. The CA may be renewed or extended for another 25 years upon written agreement of the parties through the execution of a renewal or extension contract.

In accordance with the license granted by the ROP, as expressly indicated in the CA, TADHC presently operates the Boracay Airport. TADHC completed the rehabilitation of the existing airport terminal building and facilities on June 25, 2011, but has not started the construction of the new terminal and extension of the runway as of December 31, 2012, pending completion of the acquisition of the right of way.

• *ULC BVI*

In 2008, the ROP awarded ULC BVI the financing, design, construction, supply, completion, testing, commissioning and operation and maintenance of the MRT 7 Project through a NOA issued on January 31, 2008. The MRT 7 Project is proposed to be an integrated transportation system, under a Build-Gradual Transfer-Operate, Maintain and Manage (BGTOM) scheme which is a modified Build-Transfer-Operate (BTO) arrangement under RA No. 6957, as amended by RA No. 7718, otherwise known as the BOT Law, and its Revised Implementing Rules and Regulations, to address the transportation needs of passengers and to alleviate traffic in Metro Manila, particularly traffic going to and coming from North Luzon.

On June 18, 2008, ULC BVI entered into a CA (MRT 7 Agreement) with the ROP, through the DOTC, for a 25-year concession period, subject to extensions as may be provided for under the CA and by law. Based on the CA, ULC BVI has been granted the right to finance, construct and operate and maintain (O&M) the proposed MRT 7 Project, which consists of 44-kilometer of road and rail transportation from the Bocaue exit on the North Luzon Expressway to LRT 1 and Metro Rail Transit 3 at North Avenue — Epifanio delos Santos Avenue.

The following are the salient features of the CA:

1. The MRT 7 Project cost shall be financed by ULC BVI through debt and equity at a ratio of approximately 75:25 and in accordance with existing BSP regulations on foreign financing components, if any. Based on the CA, ULC BVI's estimated capital commitment to develop the MRT 7 Project amounts to US\$1,235.60. ULC BVI shall endeavor to have signed the financing agreements not later than 18 months from the signing of the CA.
2. ULC BVI shall post a Performance Security for Construction and O&M in favor of the ROP as guarantee for faithful performance by ULC BVI to develop the MRT 7 Project. This performance security for O&M shall be reduced every year of the concession period to the amounts as specified in the CA.
3. In the event that the MRT 7 Project is not completed by the end of the grace period, which is 100 calendar days following the project completion target as defined in the CA, ULC BVI shall pay the ROP liquidated damages of US\$0.1 for every calendar day of delay.
4. As payment for the gradual transfer of the ownership of the assets of the MRT 7 Project, the ROP shall pay ULC BVI a fixed amortization payment on a semi-annual basis in accordance with the schedule of payment described in the CA. The ROP's amortization payment to ULC BVI shall start when the MRT 7 Project is substantially completed.
5. Net passenger revenue shall be shared by the ROP and ULC BVI on a 30:70 basis.
6. All rail-based revenues above 11.90% internal rate of return of ULC BVI for the MRT 7 Project over the cooperation period, which means the period covering the construction and concession period, shall be shared equally by ULC BVI and the ROP at the end of the concession period. All rail-based revenues above 14% internal rate of return shall wholly accrue to the ROP.
7. The ROP grants the ULC BVI exclusive and irrevocable commercial development rights (including the right to lease or sublease or assign interests in, and to collect and receive any and all income from, but not limited

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to, advertising, installation of cables, telephone lines, fiber optics or water mains, water lines and other business or commercial ventures or activities over all areas and aspects of the MRT 7 Project with commercial development potentials) from the effectivity date of the CA until the end of the concession period, which can be extended for another 25 years, subject to the ROP's approval. In consideration of the development rights granted, ULC BVI or its assignee shall pay the ROP 20% of the net income before tax actually realized from the exercise of the development rights.

The Group has determined that the provisions of Philippine Interpretation IFRIC 12 apply to this CA and will be accounted for under the financial asset model. As of March 21, 2013, construction of the MRT 7 Project has not yet started.

Toll Operation Agreement

• ***CMMTC***

On June 10, 1994, the Philippine National Construction Corporation (PNCC), the franchise holder for the construction, operation and maintenance (O&M) of the proposed Metro Manila Expressway, including any and all extensions, linkages or stretches such as the proposed MMS, and PT Citra Lamtoro Gung Persada (CITRA) as joint proponents, submitted to the Philippine Government through the Toll Regulatory Board (TRB), the Joint Investment Proposal covering not only the proposed MMS but also the planned Metro Manila Tollways. The said proposal embodied, among others, CITRA in cooperation with PNCC, committed itself to finance, design and construct MMS in three stages, consisting of the SMMS, the North Metro Manila Skyway and the Central Metro Manila Skyway with the Metro Manila Tollways as the fourth stage. The Joint Investment Proposal was approved by the TRB on November 27, 1995, and the Supplemental Toll Operation Agreement (STOA) was executed on the same date by and among CMMTC, PNCC and the ROP through the TRB. Under the approved Joint Investment Proposal and the STOA, the design and the construction of the SMMS and the financing thereof, shall be the primary and exclusive privilege, responsibility and obligation of CMMTC as Investor. On the other hand, the O&M of the same shall be the primary and exclusive privilege, responsibility and obligation of PNCC, through its wholly-owned subsidiary, the PNCC Skyway Corporation (PSC).

On July 18, 2007, the STOA was amended to cover, among others, the implementation of Stage 2 of the SMMS; the functional and financial integration of Stage 1 and Stage 2 of the SMMS upon the completion of the construction of Stage 2; and the grant of right to CMMTC to nominate to the TRB a qualified party to perform the O&M of the Project Roads to replace PSC. CMMTC, PNCC and PSC then entered into a Memorandum of Agreement for the successful and seamless turnover of the O&M responsibilities for the SMMS from PSC to SOMCO.

The following are the salient features of the STOA:

1. The Project Roads shall be owned by the Philippine Government, without prejudice to the rights and entitlement of the Investor and the Operator to the toll revenues, and the legal transfer of ownership to the Philippine Government shall be deemed to occur automatically on a continuous basis in accordance with the progress of construction.
2. The 30-year franchise period for the Stage 1 of the SMMS and for the Integrated Stage 1 and Stage 2 of the SMMS commenced on October 10, 1999 and April 25, 2011, respectively.
3. The toll fees collected are allocated between CMMTC and SOMCO in accordance with the Revenue Sharing Agreement entered by both parties on March 30, 2012. Under the STOA, CMMTC may file an application to adjust the toll rates which shall be of two kinds, namely periodic and interim adjustments. Periodic adjustments are made every two years. Interim adjustment will be granted upon the occurrence of force majeure, or a significant currency devaluation. A currency devaluation shall be deemed "significant" if it results in a depreciation of the value of the Philippine peso relative to the US dollar by at least 10%. The applicable exchange rate shall be the exchange rate between the currencies in effect as of the date of approval of the prevailing preceding toll rate.

The Group has determined that the provisions of Philippine Interpretation IFRIC 12 apply to this STOA and will be accounted for under the intangible asset model.

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Telecommunications

Franchise with National Telecommunications Commission (NTC)

▪ ***BellTel***

In 1994, the Philippine Congress passed RA No. 7692 which granted a franchise to BellTel to install, operate and maintain telecommunications systems throughout the Philippines and for other purposes.

On October 28, 1997, the NTC, under NTC Case No. 94-229, granted a Provisional Authority (PA) to BellTel, valid for eighteen (18) months, or until April 27, 1999, to install, operate and maintain the following telecommunication services, to wit:

- international gateway facility;
- inter-exchange carrier facility;
- VSAT system nationwide;
- telephone systems in the selected cities and municipalities in the Luzon area;
- WLL telephone systems in the cities of Muntinlupa, Las Piñas, Pasig, Mandaluyong, Makati, Pasay, Parañaque, Taguig and Marikina; and in the municipalities of Pateros and San Juan; and
- telephone systems in all economic zones identified under RA No. 7916.

Since then, this PA had been extended several times, the latest extension of which is valid until December 22, 2010 as contained in NTC's order dated September 19, 2009. BellTel applied for an extension of the PA on January 28, 2011. On March 5, 2012, NTC approved the extension of the PA for another three years, expiring on March 5, 2015.

In an Order dated October 19, 2007 (CCC Case No. 94-223), the NTC granted BellTel a PA, valid for 18 months or until April 19, 2009, to install, operate and maintain a Mobile Telecommunication Network as set forth in the said Order. This PA was later extended for a period of three (3) years or until April 17, 2012 as per NTC Order dated August 14, 2009.

On April 17, 2012, NTC approved another three (3) year extension of the PA until April 17, 2015.

▪ ***ETPI***

On October 3, 2002, RA No. 9172 entitled "An Act Renewing and Amending the Franchise Granted to ETPI (Eastern Extension Australasia and China Telegraph Company Limited) under RA No. 808, as Amended" extended for another twenty-five years ETPI's legislative franchise to construct, install, establish, operate and maintain for commercial purposes and in the public interest, throughout the Philippines and between the Philippines and other countries and territories, the following telecommunications services:

- wire and/or wireless telecommunications systems, including but not limited to mobile, cellular, paging, fiber optic, multi-channel distribution system, local multi-point distribution system, satellite transmit and receive systems, switches, and their value-added services such as, but not limited to, transmission of voice, data, facsimile, control signs, audio and video, information services bureau and all other telecommunications systems technologies as are at present available or will be made available through technological advances or innovations in the future; and
- construct, acquire, lease and operate or manage transmitting and receiving stations, lines, cables or systems, as is, or are, convenient or essential to efficiently carry out the purpose of the franchise.

▪ ***TTPI***

TTPI has an approved congressional franchise granted under RA No. 7671, as amended by RA No. 7674, to install, operate and maintain telecommunications systems throughout the Philippines.

On September 25, 1996, the NTC granted TTPI a PA to install, operate and maintain Local Exchange Carrier services in the provinces of Batanes, Cagayan, Isabela, Kalinga, Apayao, Nueva Vizcaya, Ifugao and Quirino and the cities of Manila and Caloocan as well as the municipality of Navotas in order to commence compliance with the requirements of Executive Order (EO) No. 109 (s. 1993), which required ETPI to put up a minimum of

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300,000 Local Exchange Carrier lines. TTPI is allowed to deploy Public Calling Offices in municipalities and barangays within its authorized service area in lieu of rolling out Local Exchange Carrier lines.

On January 18, 2006, the NTC granted TTPI a Certificate of Public Convenience and Necessity (CPCN) to install, operate and maintain Local Exchange Carrier services in the cities of Manila and Caloocan, as well as in the provinces of Cagayan and Isabela. In addition, in a letter dated August 14, 2006, the NTC confirmed that TTPI has already completely served the remaining areas it needs to serve under the PA of September 25, 1996. On January 8, 2010, TTPI was granted a CPCN to install, operate and maintain Local Exchange Carrier services in the municipality of Navotas and the provinces of Cagayan, Isabela, Apayao, Batanes, Ifugao, Kalinga, Nueva Vizcaya and Quirino.

On September 25, 1996, October 16, 2006 and December 23, 2008, NTC issued separate PAs in favor of TTPI to install, operate and maintain Local Exchange Carrier services in the remaining cities and municipalities of Metro Manila, in the provinces of Cavite, Laguna, Batangas, Rizal and Quezon (CALABARZON) and in the provinces of Apayao, Batanes, Ifugao, Kalinga, Nueva Vizcaya and Quirino.

Properties

SMPI-GSIS Put Option

The Put Option between SMPI and GSIS can be exercised within a period of 10 years. The option exercise price is equivalent to ₱300 plus interest.

Any dividends declared and paid to stockholders prior to the exercise of the Put Option by GSIS will be deducted from interest provided above upon exercise of the option.

On June 7, 2011, GSIS has exercised the put option and transferred all its ownership interest to SMPI for a total consideration of ₱399, making SMPI-GSIS JVC a wholly-owned subsidiary of SMPI.

Lease Commitments:

a. Finance Leases

Group as Lessee

a. IPPA Agreements

The IPPA Agreements are with the conformity of NPC, a government-owned and controlled corporation created by virtue of RA No. 6395, as amended, whereby NPC confirms, acknowledges, approves and agrees to the terms of the Agreement and further confirms that for as long as it remains the IPP Counterparty it will comply with its obligations and exercise its rights and remedies under the original agreement with the IPP at the request and instruction of PSALM.

Relative to the IPPA Agreements, SMEC, SPDC and SPPC have to pay PSALM monthly fees for 15 years until October 1, 2024, 18 years until April 26, 2028 and 12 years until June 26, 2022, respectively.

The IPPA Agreements provide the Group with a right to receive a transfer of the power station in case of buyout or termination.

In accounting for the Group's IPPA Agreements with PSALM, the Group's management has made a judgment that the IPPA Agreement is an agreement that contains a finance lease. The Group's management has also made a judgment that it has substantially acquired all the risks and rewards incidental to ownership of the power plants. Accordingly, the Group recognized the capitalized asset and related liability of ₱198,506 and ₱195,102 in 2012 and ₱203,691 and ₱208,187 in 2011, respectively, (equivalent to the present value of the minimum lease payments using the Group's incremental borrowing rates for US dollar and Philippine peso payments) as "Property, plant and equipment" and "Finance lease liabilities" in the consolidated statements of financial position (Note 16).

The Group's incremental borrowing rates are as follows:

	<u>US Dollar</u>	<u>Philippine Peso</u>
SMEC	3.89%	8.16%
SPPC	3.85%	8.05%
SPDC	3.30%	7.90%

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The discount determined at inception of the agreement is amortized over the period of the IPPA Agreement and recognized as part of "Interest expense and other finance charges" account in the consolidated statements of income (Note 31). Interest expense in 2012, 2011 and 2010 amounted to ₱11,331, ₱11,531 and ₱5,299, respectively.

The future minimum lease payments for each of the following periods are as follows:

	<u>Dollar payments</u>	<u>Peso equivalent of Dollar payments</u>	<u>Peso payments</u>	<u>Total</u>
2012				
Not later than one year	US\$ 212	₱ 8,687	₱ 10,130	₱ 18,817
More than one year and not later than five years	960	39,397	45,954	85,351
Later than five years	1,937	79,540	92,839	172,379
	<u>3,109</u>	<u>127,624</u>	<u>148,923</u>	<u>276,547</u>
Less: Future finance charges on finance lease liabilities	636	26,118	55,327	81,445
Present values of finance lease liabilities	<u>US\$2,473</u>	<u>₱101,506</u>	<u>₱ 93,596</u>	<u>₱195,102</u>
	<u>Dollar payments</u>	<u>Peso equivalent of Dollar payments</u>	<u>Peso payments</u>	<u>Total</u>
2011				
Not later than one year	US\$ 193	₱ 8,438	₱ 9,212	₱ 17,650
More than one year and not later than five years	918	40,263	43,971	84,234
Later than five years	2,191	96,035	104,951	200,986
	<u>3,302</u>	<u>144,736</u>	<u>158,134</u>	<u>302,870</u>
Less: Future finance charges on finance lease liabilities	730	31,985	62,698	94,683
Present values of finance lease liabilities	<u>US\$2,572</u>	<u>₱112,751</u>	<u>₱ 95,436</u>	<u>₱208,187</u>

The present values of minimum lease payments for each of the following periods are as follows:

	<u>Dollar payments</u>	<u>Peso equivalent of Dollar payments</u>	<u>Peso payments</u>	<u>Total</u>
2012				
Not later than one year	US\$ 187	₱ 7,659	₱ 7,778	₱ 15,437
More than one year and not later than five years	769	31,576	28,967	60,543
Later than five years	1,517	62,271	56,851	119,122
	<u>US\$2,473</u>	<u>₱101,506</u>	<u>₱93,596</u>	<u>₱195,102</u>
	<u>Dollar payments</u>	<u>Peso equivalent of Dollar payments</u>	<u>Peso payments</u>	<u>Total</u>
2011				
Not later than one year	US\$ 176	₱ 7,721	₱ 7,643	₱ 15,364
More than one year and not later than five years	764	33,486	29,945	63,431
Later than five years	1,632	71,544	57,848	129,392
	<u>US\$2,572</u>	<u>₱112,751</u>	<u>₱95,436</u>	<u>₱208,187</u>

b. Machinery and Equipment

The Group's finance leases cover machinery and equipment needed for business operations. The agreements do not allow subleasing. As of December 31, 2012 and 2011, the net carrying amount of the leased equipment was ₱55 and ₱64, respectively (Note 16).

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The Group's share in the minimum lease payments for these finance lease liabilities are as follows:

	<u>Minimum lease payable</u>	<u>Interest</u>	<u>Principal</u>
2012			
Within one year	₱21	₱2	₱19
After one year but not more than 2 years	35	3	32
	<u>₱56</u>	<u>₱5</u>	<u>₱51</u>
	<u>Minimum lease payable</u>	<u>Interest</u>	<u>Principal</u>
2011			
Within one year	₱25	₱1	₱24
After one year but not more than 2 years	53	3	50
	<u>₱78</u>	<u>₱4</u>	<u>₱74</u>

c. Transportation Equipment

The Group's finance leases also cover transportation equipment needed for business operations. These agreements do not allow subleasing. Some leases provide the Group with the option to purchase the equipment at a beneficial price. As of December 31, 2012 and 2011, the net carrying amount of leased transportation equipment was ₱1. As of December 31, 2012, the minimum lease payable due after one year amounted to ₱1.

b. Operating Leases

Group as Lessor

The Group has entered into lease agreements on its investment property portfolio, consisting of surplus office spaces (Note 17). The non-cancellable leases have remaining terms of between three to fourteen years. All leases include a clause to enable upward revision of the rental charge on an annual basis based on prevailing market conditions.

As of December 31, 2012, 2011 and 2010, the future minimum lease receipts under non-cancellable operating leases are as follows:

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Within one year	₱340	₱311	₱370
After one year but not more than five years	494	318	541
After five years	69	45	52
	<u>₱903</u>	<u>₱674</u>	<u>₱963</u>

Rent income recognized in profit or loss amounted to ₱1,139, ₱412 and ₱267 in 2012, 2011 and 2010, respectively (Note 4).

Group as Lessee

The Group leases a number of office, warehouse and factory facilities under operating leases. The leases typically run for a period of one to sixteen years. Some leases provide an option to renew the lease at the end of the lease term and are being subjected to reviews to reflect current market rentals.

As of December 31, 2012, 2011 and 2010, non-cancellable operating lease rentals are payable as follows:

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Within one year	₱ 1,418	₱ 885	₱ 875
After one year but not more than five years	3,230	2,551	2,424
More than five years	7,680	7,486	7,196
	<u>₱12,328</u>	<u>₱10,922</u>	<u>₱10,495</u>

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Rent expense recognized in profit or loss amounted to ₱3,024, ₱2,575 and ₱1,812 in 2012, 2011 and 2010, respectively (Notes 4, 27 and 28).

36. Retirement Plans

The Parent Company and majority of its subsidiaries have funded, noncontributory, defined benefit retirement plans covering all of their permanent employees (collectively, the Retirement Plans). Contributions and costs are determined in accordance with the actuarial studies made for the Retirement Plans. Annual cost is determined using the projected unit credit method. Majority of the Group's latest actuarial valuation date is December 31, 2012. Valuations are obtained on a periodic basis.

Majority of the Retirement Plans are registered with the Bureau of Internal Revenue as tax-qualified plans under Republic Act No. 4917, as amended. The control and administration of the Group's Retirement Plans are vested in the Board of Trustees of each Retirement Plan. The Board of Trustees of the Group's Retirement Plans exercises voting rights over the shares and approve material transactions. The Retirement Plans' accounting and administrative functions are undertaken by the Parent Company's Retirement Funds Office.

Retirement benefits recognized in profit or loss by the Parent Company amounted to ₱590, ₱212 and ₱371 in 2012, 2011 and 2010, respectively, while retirement costs charged by the subsidiaries amounted to ₱308, ₱1,231 and ₱656 in 2012, 2011 and 2010, respectively. The Group's annual contribution to the Retirement Plans consists of payments covering the current service cost and amortization of past service costs.

The components of retirement costs (benefits) recognized in profit or loss in 2012, 2011 and 2010 and the amounts recognized in the consolidated statements of financial position as of December 31, 2012 and 2011 are as follows:

	2012	2011	2010
Current service cost	₱ 1,045	₱ 922	₱ 652
Interest cost	1,195	1,303	1,082
Expected return on plan assets	(1,755)	(3,951)	(1,170)
Net actuarial loss (gain)	(766)	2,754	(282)
Effect of curtailment	(1)	(9)	3
Net retirement costs (benefits)	(₱ 282)	₱ 1,019	₱ 285
Actual return (loss) on plan assets	(₱ 3,164)	(₱14,056)	₱25,621

The retirement costs (benefits) are recognized in the following line items in the consolidated statements of income:

	Note	2012	2011	2010
Cost of sales		₱ 175	₱ 143	₱143
Selling and administrative expenses		(457)	876	142
	30	(₱ 282)	₱1,019	₱285

The reconciliation of the assets and liabilities recognized in the consolidated statements of financial position is as follows:

	Note	2012	2011
Present value of defined benefit obligation		₱24,575	₱20,700
Fair value of plan assets		25,560	29,208
		(985)	(8,508)
Unrecognized actuarial gain	4	1,495	9,348
Net retirement liabilities		₱ 510	₱ 840

In 2012, net retirement assets and liabilities included as part of "Other noncurrent assets" account amounted to ₱903 (Note 20) and under "Accounts payable and accrued expenses" and "Other noncurrent liabilities" accounts amounted to ₱103 and ₱1,310, respectively (Notes 22 and 24).

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In 2011, net retirement assets and liabilities included as part of “Other noncurrent assets” account amounted to ₱299 (Note 20) and under “Accounts payable and accrued expenses” and “Other noncurrent liabilities” accounts amounted to ₱85 and ₱1,054, respectively (Notes 22 and 24).

The movements in the present value of defined benefit obligation are as follows:

	2012	2011
Balance at beginning of year	₱20,700	₱18,386
Benefit obligation of newly acquired subsidiaries	986	170
Interest cost	1,195	1,303
Current service cost	1,045	922
Benefits paid	(1,233)	(1,312)
Actuarial losses	2,002	1,245
Effect of curtailment	(2)	(10)
Translation adjustments	(118)	(4)
Balance at end of year	₱24,575	₱20,700

The movements in the fair value of the plan assets are as follows:

	2012	2011
Balance at beginning of year	₱29,208	₱ 43,964
Plan assets of newly acquired subsidiaries	—	255
Expected return on plan assets	1,755	3,951
Contributions by employer	727	318
Benefits paid	(1,159)	(1,271)
Actuarial losses	(4,919)	(18,007)
Translation adjustments	(52)	(2)
Balance at end of year	₱25,560	₱ 29,208

The carrying amounts of the Group’s retirement fund approximate fair values as of December 31, 2012 and 2011.

The Group’s plan assets consist of the following:

	In Percentages	
	2012	2011
Marketable securities and shares of stock	71.87	80.90
Interest in pooled funds		
Fixed income portfolio	5.79	5.04
Stock trading portfolio	3.33	2.52
Investment in Real estate	0.38	0.37
Others	18.63	11.17

Investments in Marketable Securities

As of December 31, 2012, the plan assets include 20,304,067 common shares, 35,586,770 Series “2”, Subseries “2-A” and 38,077,020 Series “2”, Subseries “2-B” preferred shares of the Parent Company with fair market value per share of ₱105.40, ₱75.00 and ₱75.00, respectively.

As of December 31, 2012, the Group’s plan assets include 1,499,181,997 common shares of Petron with fair market value per share of ₱10.46.

As of December 31, 2012, the Group’s plan assets include 34,166,985 common shares of GSMI with fair market value per share of ₱17.80.

As of December 31, 2012, the Group’s plan assets include 32,220,400 common shares of SMB with fair market value per share of ₱29.30.

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The Group's Retirement Plans recognized a loss on the investment in marketable securities of SMC and its subsidiaries amounting to ₱4,932 in 2012.

Dividend income from the investment in shares of stock of SMC and its subsidiaries amounted to ₱341 in 2012.

Investment in Shares of Stock

Investment in shares of stock includes the investment of the Retirement Plans in the common shares of BOC and PAHL, accounted for under the equity method.

a. BOC

As of December 31, 2012, San Miguel Corporation Retirement Plan's (SMCRP) investment in BOC amounting to ₱4,593 is at 39.94% equity interest, representing 44,774,271 common shares.

In 2012, the Retirement Plan recognized its share from the net income of BOC amounting to ₱278.

b. PAHL

As of December 31, 2012, Petron Corporation Employees Retirement Plan's (PCERP) investment in PAHL amounting to ₱1,919 (US\$44) represents 54.1% equity interest, composed of 273,000,000 Class A shares and 102,142,858 Class B shares.

In 2012, the Retirement Plan recognized its share from the net loss of PAHL amounting to ₱90.

c. BPI

As of December 31, 2012, the Group's plan assets also include investment in BPI representing 2,389,494 preferred shares.

Interest in Pooled Funds

Investments in pooled funds were established mainly to put together a portion of the funds of the retirement funds of the Group to be able to draw, negotiate and obtain the best terms and financial deals for the investments resulting from big volume transactions.

As of December 31, 2012, approximately 14% and 56% of the Retirement Plan's investments in pooled funds in stock trading portfolio and fixed income portfolio, respectively include investments in shares of stock of the Parent Company and its subsidiaries.

The Board of Trustees approved the percentage of asset to be allocated for fixed income instruments and equities. The Retirement Plan has set maximum exposure limits for each type of permissible investments in marketable securities and deposit instruments. The Board of Trustees may, from time to time, in the exercise of its reasonable discretion and taking into account existing investment opportunities, review and revise such allocation and limits.

Investment in Real Estate

As of December 31, 2012, the Group Retirement Plans have investments in real estate properties.

Others

Others include the Group Retirement Plans' investment in trust account, government securities, bonds and notes, cash and cash equivalents and receivables which earn interest. Investment in trust account represents funds entrusted to a financial institution for the purpose of maximizing the yield on investible funds.

The overall expected rate of return is determined based on historical performance of the investments.

The principal actuarial assumptions used to determine retirement benefits are as follows:

	In percentages	
	2012	2011
Discount rate	3.4 - 6.8	1.5 - 6.3
Salary increase rate	4.0 - 8.0	2.5 - 7.0
Expected return on plan assets	5.0 - 9.0	5.0 - 9.0

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The historical information for the current and previous four annual periods is as follows:

	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>	<u>2008</u>
Present value of the defined benefit obligation	₱24,026	₱ 20,700	₱ 18,386	₱12,362	₱11,080
Fair value of plan assets	25,560	29,208	43,964	15,178	10,232
Deficit (excess) in the plan	(1,534)	(8,508)	(25,578)	(2,816)	848
Experience adjustments on plan liabilities	860	1,492	(132)	927	6
Experience adjustments on plan assets	(4,907)	(18,007)	24,451	5,232	(295)

The Group expects to contribute ₱945 to its defined benefit plans in 2013.

As of December 31, 2012 and 2011, the outstanding balances of the Group's receivables from the retirement plans are as follows:

- a. The current portion of Petron's advances to PCERP amounting to ₱4,747 as of December 31, 2012 is included as part of "Trade and other receivables — net" account (Note 10), while the noncurrent portion amounting to ₱10,770 and ₱23,247 as of December 31, 2012 and 2011, respectively, is included as part of "Other noncurrent assets" account in the consolidated statements of financial position (Notes 20 and 34). The advances are subject to interest of 4% in 2012 and 2011.
- b. The Parent Company has advances to SMCRP amounting to ₱5,997 and ₱5,755 as of December 31, 2012 and 2011, respectively, included as part of "Trade and other receivables — net" account in the consolidated statements of financial position (Note 10). The advances are subject to interest of 5.75% in 2012 and 2011.
- c. GSMI has advances to GSMIRP amounting to ₱77 and ₱137 as of December 31, 2012 and 2011, respectively, included as part of "Trade and other receivables — net" account in the consolidated statements of financial position (Note 10). The advances are subject to interest of 5.75% in 2012 and 2011.

Transactions with retirement plans are made at normal market prices and terms. Outstanding balances as of December 31, 2012 and 2011 are unsecured and settlements are made in cash. There have been no guarantees provided for any retirement plan receivables. The Group has not made any provision for impairment losses relating to the receivables from retirement plans for the years ended December 31, 2012, 2011 and 2010.

37. Cash Dividends

Cash dividends declared by the Parent Company's BOD to common shareholders amounted to ₱1.75 per share and ₱1.05 per share in 2012 and 2011, respectively.

Cash dividends declared by the Parent Company's BOD to Series "1" preferred shareholders amounted to ₱6.00 per share in 2012 and 2011.

On November 14, 2012, the Parent Company's BOD declared cash dividend at ₱1.40625, ₱1.4296875 and ₱1.50 per share, payable on January 4, 2013 to all Series "2" — Subseries "2-A", Subseries "2-B" and Subseries "2-C" preferred shareholders, respectively, as of December 20, 2012.

On January 17, 2013, the Parent Company's BOD declared cash dividend at ₱1.40625, ₱1.4296875 and ₱1.50 per share, payable on April 4, 2013 to all Series "2" — Subseries "2-A", Subseries "2-B" and Subseries "2-C" preferred shareholders, respectively, as of March 20, 2013.

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38. Basic and Diluted Earnings Per Share

Basic and Diluted EPS is computed as follows:

	<u>Note</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Income attributable to equity holders of the Parent Company		₱27,579	₱17,518	₱20,091
Dividends on preferred shares for the period	37	(6,127)	(5,823)	(5,823)
Net income attributable to common shareholders of the Parent				
Company (a)		₱21,452	₱11,695	₱14,268
Weighted average number of common shares outstanding (in millions)				
— basic (b)		2,370	2,353	2,310
Effect of dilution — common	40	16	16	14
Weighted average number of common shares outstanding (in millions)				
— diluted (c)		2,386	2,369	2,324
Earnings per common share attributable to equity holders of the Parent				
Company				
Basic (a/b)		₱ 9.05	₱ 4.97	₱ 6.18
Diluted (a/c)		₱ 8.99	₱ 4.94	₱ 6.14

39. Supplemental Cash Flow Information

Supplemental information with respect to the consolidated statements of cash flows is presented below:

- a. Changes in noncash current assets, certain current liabilities and others are as follows (amounts reflect actual cash flows rather than increases or decreases of the accounts in the consolidated statements of financial position):

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Trade and other receivables	(₱25,614)	(₱9,600)	₱12,305
Inventories	(922)	(10,129)	2,178
Prepaid expenses and other current assets	(8,956)	(5,670)	(3,686)
Loans payable	(231)	15	107
Accounts payable and accrued expenses	7,069	5,233	7,581
Income and other taxes payable and others	715	816	(5,310)
	(₱27,939)	(₱19,335)	₱13,175

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b. Acquisition of subsidiaries (Note 5)

	<i>Note</i>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Cash and cash equivalents		₱ 12,011	₱ 463	₱ 42,729
Trade and other receivables — net		12,844	437	32,953
Inventories		13,164	19	35,315
Prepaid expenses and other current assets		679	137	4,599
Asset held for sale		—	—	823
Available-for-sale financial assets		—	4	—
Investments and advances — net		168	274	16,092
Property, plant and equipment — net		16,590	3,711	175,650
Investment properties — net		412	—	121
Other intangible assets — net		20,601	—	7,097
Deferred tax assets		37	—	430
Other noncurrent assets — net		6,735	229	25,619
Loans payable		(15,353)	—	(34,987)
Accounts payable and accrued expenses		(19,325)	(450)	(28,114)
Income and other taxes payable		(754)	(119)	(1,267)
Current maturities of long-term debt — net of debt issue costs		(11,815)	(25)	(9,193)
Long-term debt — net of current maturities and debt issue costs		(7,596)	(185)	(43,452)
Deferred tax liabilities		(1,448)	(91)	(2,539)
Other noncurrent liabilities		(853)	(1,779)	(151,777)
Non-controlling interests		(9,040)	(691)	(25,518)
Net assets		17,057	1,934	44,581
Cash and cash equivalents		(12,011)	(463)	(42,729)
Goodwill in subsidiaries	4, 5, 19	19,554	732	24,456
Investment at equity		(4,871)	(1,625)	(1,444)
Other intangible asset — mining rights	4, 5, 19	—	197	—
Revaluation increment		—	—	(1,396)
Gain on acquisition of a subsidiary	5, 33	—	—	(4,490)
Net cash flows		₱ 19,729	₱ 775	₱ 18,978

40. Share-Based Transactions

ESPP

Under the ESPP, 80,396,659 shares (inclusive of stock dividends declared) of the Parent Company's unissued shares have been reserved for the employees of the Group. All permanent Philippine-based employees of the Group, who have been employed for a continuous period of one year prior to the subscription period, will be allowed to subscribe at 15% discount to the market price equal to the weighted average of the daily closing prices for three months prior to the offer period. A participating employee may acquire at least 100 shares of stock through payroll deductions.

The ESPP requires the subscribed shares and stock dividends accruing thereto to be pledged to the Parent Company until the subscription is fully paid. The right to subscribe under the ESPP cannot be assigned or transferred. A participant may sell his shares after the second year from the exercise date. The current portion of subscriptions receivable amounted to ₱259 and ₱286 as of December 31, 2012 and 2011, respectively, presented as part of "Non-trade" under "Trade and other receivables" account in the consolidated statements of financial position (Note 10). The noncurrent portion of ₱776 and ₱1,343 as of December 31, 2012 and 2011, respectively, is presented as part of "Noncurrent receivables and deposits" under "Other noncurrent assets" account in the consolidated statements of financial position (Note 20).

The ESPP also allows subsequent withdrawal and cancellation of participants' subscriptions under certain terms and conditions. The shares pertaining to withdrawn or cancelled subscriptions shall remain issued shares and shall revert to the pool of shares available under the ESPP.

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The table below shows the number and weighted average exercise prices of grants:

	2011	
	Number of shares	Weighted average exercise price
Subscribed during the year	8,754,400	₱95.11
Cancelled during the year Class "A"	(408,150)	65.98
Cancelled during the year Class "B"	(1,100)	70.50

There were no shares offered under ESPP in 2012.

The average market price of the common shares granted in 2011 was ₱111.90 per share.

The average remaining contractual life of the ESPP subscribed in 2011 was 0.69 and 1.69 years as of December 31, 2012 and 2011, respectively.

LTIP

The Parent Company also maintains LTIP for the executives of the Group. The options are exercisable at the fair market value of the Parent Company shares as of date of grant, with adjustments depending on the average stock prices of the prior three months. A total of 54,244,905 shares, inclusive of stock dividends declared, are reserved for the LTIP over its 10-year life. The LTIP is administered by the Executive Compensation Committee of the Parent Company's BOD.

On December 16, 2010, the Parent Company approved the grant of stock options to 732 executives consisting of 2,402,081 shares.

There were no LTIP offered to executives in 2012 and 2011.

Options to purchase 15,888,431 shares and 16,039,416 shares in 2012 and 2011, respectively, were outstanding at the end of each year. Options which were exercised and cancelled totaled 3,061,093 shares and 3,023,807 shares in 2012 and 2011, respectively.

The stock options granted under the LTIP cannot be assigned or transferred by a participant and are subject to a vesting schedule. After one complete year from the date of the grant, 33% of the stock option becomes vested. Another 33% is vested on the second year and the remaining option lot is fully vested on the third year.

Vested stock options may be exercised at any time, up to a maximum of eight years from the date of grant. All unexercised stock options after this period are considered forfeited.

A summary of the status of the outstanding share stock options and the related weighted average exercise price under the LTIP is shown below:

	2012		2011	
	Number of share stock options	Weighted average exercise price	Number of share stock options	Weighted average exercise price
Class "A"				
Balance at beginning of year	13,633,452	₱68.09	15,541,940	₱66.36
Exercised during the year	(1,563,043)	55.66	(1,496,639)	53.67
Expired during the year	(613,449)	68.01	(411,849)	55.34
Balance at end of year	<u>11,456,960</u>	<u>69.79</u>	<u>13,633,452</u>	<u>68.09</u>
Class "B"				
Balance at beginning of year	6,113,417	₱70.52	7,228,736	₱69.66
Exercised during the year	(648,672)	65.87	(898,532)	64.73
Expired during the year	(235,929)	70.39	(216,787)	66.06
Balance at end of year	<u>5,228,816</u>	<u>71.10</u>	<u>6,113,417</u>	<u>70.52</u>

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Effective August 26, 2010, all Class “A” common shares and Class “B” common shares of the Parent Company were declassified and considered as common shares without distinction. However, as of December 31, 2012 and 2011, the number of the outstanding share stock options and related weighted average exercise price under LTIP were presented as Class “A” and Class “B” common shares to recognize the average exercise price of stock options granted prior to August 26, 2010.

The fair value of equity-settled share options granted is estimated as at the date of grant using Black-Scholes option pricing model, taking into account the terms and conditions upon which the options were granted. Expected volatility is estimated by considering average share price volatility.

The range of exercise prices for options outstanding was ₱40.50 to ₱120.33 as of December 31, 2012 and 2011.

The average remaining contractual life of the LTIP was 1.16 year as of December 31, 2011 for Class “A” common shares and 0.50 year as of December 31, 2011 for Class “B” common shares.

The average remaining contractual life of the LTIP was 1.00 year as of December 31, 2012.

Share-based payment charged to operations, included under “Administrative expenses — others” account, amounted to ₱242, ₱303 and ₱315 in 2012, 2011 and 2010, respectively (Note 28).

41. Financial Risk Management Objectives and Policies

Objectives and Policies

The Group has significant exposure to the following financial risks primarily from its use of financial instruments:

- Interest Rate Risk
- Foreign Currency Risk
- Commodity Price Risk
- Liquidity Risk
- Credit Risk

This note presents information about the Group’s exposure to each of the foregoing risks, the Group’s objectives, policies and processes for measuring and managing these risks, and the Group’s management of capital.

The Group’s principal non-trade related financial instruments include cash and cash equivalents, option deposit, AFS financial assets, financial assets at FVPL, short-term and long-term loans, and derivative instruments. These financial instruments, except financial assets at FVPL and derivative instruments, are used mainly for working capital management purposes. The Group’s trade-related financial assets and financial liabilities such as trade and other receivables, noncurrent receivables and deposits, accounts payable and accrued expenses, finance lease liabilities and other noncurrent liabilities arise directly from and are used to facilitate its daily operations.

The Group’s outstanding derivative instruments such as commodity and currency options, forwards and swaps are intended mainly for risk management purposes. The Group uses derivatives to manage its exposures to foreign currency, interest rate and commodity price risks arising from the Group’s operating and financing activities.

The BOD has the overall responsibility for the establishment and oversight of the Group’s risk management framework. The BOD has established the Risk Management Committee, which is responsible for developing and monitoring the Group’s risk management policies. The committee reports regularly to the BOD on its activities.

The Group’s risk management policies are established to identify and analyze the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group’s activities. The Group, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

The Group’s Audit Committee oversees how management monitors compliance with the Group’s risk management policies and procedures and reviews the adequacy of the risk management framework in relation to the risks faced by the Group. The Group’s Audit Committee is assisted in its oversight role by Internal Audit. Internal Audit undertakes both regular and ad hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee.

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The BOD constituted the Group's Audit Committee to assist the BOD in fulfilling its oversight responsibility of the Group's corporate governance process relating to the: a) quality and integrity of the Group's financial statements and financial reporting process and the Group's systems of internal accounting and financial controls; b) performance of the internal auditors; c) annual independent audit of the Group's financial statements, the engagement of the independent auditors and the evaluation of the independent auditors' qualifications, independence and performance; d) compliance by the Group with legal and regulatory requirements, including the Group's disclosure control and procedures; e) evaluation of management's process to assess and manage the Group's enterprise risk issues; and f) fulfillment of the other responsibilities set out by the BOD. The Audit Committee shall also prepare the reports required to be included in the Group's annual report.

The Group's accounting policies in relation to derivatives are set out in Note 3 to the consolidated financial statements.

Interest Rate Risk

Interest rate risk is the risk that future cash flows from a financial instrument (cash flow interest rate risk) or its fair value (fair value interest rate risk) will fluctuate because of changes in market interest rates. The Group's exposure to changes in interest rates relates primarily to the Group's long-term borrowings and investment securities. Investments acquired or borrowings issued at fixed rates expose the Group to fair value interest rate risk. On the other hand, investment securities acquired or borrowings issued at variable rates expose the Group to cash flow interest rate risk.

The Group manages its interest cost by using an optimal combination of fixed and variable rate debt instruments. Management is responsible for monitoring the prevailing market-based interest rate and ensures that the mark-up rates charged on its borrowings are optimal and benchmarked against the rates charged by other creditor banks.

On the other hand, the Group's investment policy is to maintain an adequate yield to match or reduce the net interest cost from its borrowings pending the deployment of funds to their intended use in the Group's operations and working capital management. However, the Group invests only in high-quality securities while maintaining the necessary diversification to avoid concentration risk.

In managing interest rate risk, the Group aims to reduce the impact of short-term fluctuations on the Group's earnings. Over the longer term, however, permanent changes in interest rates would have an impact on profit or loss.

The management of interest rate risk is also supplemented by monitoring the sensitivity of the Group's financial instruments to various standard and non-standard interest rate scenarios. Interest rate movements affect reported equity in the following ways:

- retained earnings arising from increases or decreases in interest income or interest expense as well as fair value changes reported in profit or loss, if any;
- fair value reserves arising from increases or decreases in fair values of AFS financial assets reported as part of other comprehensive income; and
- hedging reserves arising from increases or decreases in fair values of hedging instruments designated in qualifying cash flow hedge relationships reported as part of other comprehensive income.

The sensitivity to a reasonably possible 1% increase in the interest rates, with all other variables held constant, would have decreased the Group's profit before tax (through the impact on floating rate borrowings) by ₱981 and ₱962 in 2012 and 2011, respectively. A 1% decrease in the interest rate would have had the equal but opposite effect. These changes are considered to be reasonably possible given the observation of prevailing market conditions in those periods. There is no impact on the Group's other comprehensive income.

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Interest Rate Risk Table

As of December 31, 2012 and 2011, the terms and maturity profile of the interest-bearing financial instruments, together with its gross amounts, are shown in the following tables:

December 31, 2012	<1 year	1-2 years	>2-3 years	>3-4 years	>4-5 years	>5 years	Total
Fixed Rate							
Philippine peso-denominated	₱ 2,282	₱ 31,054	₱ 3,038	₱ 7,817	₱ 24,681	₱ 23,194	₱ 92,066
Interest rate	6.3212% - 9.33%	6.3212% - 9.33%	5.4885% - 9.33%	6.1451% - 9.33%	6.05% - 7%	5.93% - 10.5%	
Foreign currency-denominated (expressed in Philippine peso)	—	24,400	—	12,315	—	—	36,715
Interest rate		2%		7%			
Floating Rate							
Philippine peso-denominated	514	914	11,664	1,097	1,098	2,404	17,691
Interest rate	PDST-F + margin	PDST-F + margin	PDST-F + margin	PDST-F + margin or BSP overnight rate + margin, whichever is higher	PDST-F + margin or BSP overnight rate + margin, whichever is higher	PDST-F + margin or BSP overnight rate + margin, whichever is higher	
Foreign currency-denominated (expressed in Philippine peso)	577	11,551	56,216	8,855	3,225	—	80,424
Interest rate	LIBOR + margin, THBFIX + margin	LIBOR + margin, THBFIX + margin	LIBOR + margin	LIBOR + margin	LIBOR + margin		
	₱ 3,373	₱ 67,919	₱ 70,918	₱ 30,084	₱ 29,004	₱ 25,598	₱ 226,896

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December 31, 2011	<1 year	1-2 years	>2-3 years	>3-4 years	>4-5 years	>5 years	Total
Fixed Rate							
Philippine							
peso-denominated	₱ 15,040	₱ 513	₱ 29,284	₱ 1,270	₱ 6,048	₱ 26,230	₱ 78,385
Interest rate	6.3212% - 9.33%	6.3212% - 9.33%	6.3212% - 9.33%	5.4895% - 9.33%	6.145% - 9.33%	6.3212% - 10.5%	
Foreign currency-							
denominated (expressed in							
Philippine peso)	—	—	26,216	-	13,152	—	39,368
Interest rate			2%		7%		
Floating Rate							
Philippine							
peso-denominated	1,025	875	1,104	11,550	—	—	14,554
Interest rate	PDST-F + margin	PDST-F + margin	PDST-F + margin	PDST-F + margin			
Foreign currency-							
denominated (expressed in							
Philippine peso)	3,577	4,115	13,323	59,656	997	—	81,668
Interest rate	LIBOR + margin, THBFIX + margin	LIBOR, + margin, THBFIX + margin	LIBOR + margin, THBFIX + margin	LIBOR + margin	LIBOR + margin		
	₱ 19,642	₱ 5,503	₱ 69,927	₱ 72,476	₱ 20,197	₱ 26,230	₱ 213,975

Foreign Currency Risk

The Group's functional currency is the Philippine peso, which is the denomination of the bulk of the Group's revenues. The Group's exposure to foreign currency risk results from significant movements in foreign exchange rates that adversely affect the foreign currency-denominated transactions of the Group. The Group's risk management objective with respect to foreign currency risk is to reduce or eliminate earnings volatility and any adverse impact on equity. The Group enters into foreign currency hedges using a combination of non-derivative and derivative instruments such as foreign currency forwards, options or swaps to manage its foreign currency risk exposure.

Short-term currency forward contracts (deliverable and non-deliverable) and options are entered into to manage foreign currency risks arising from importations, revenue and expense transactions, and other foreign currency-denominated obligations. Currency swaps are entered into to manage foreign currency risks relating to long-term foreign currency-denominated borrowings.

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Information on the Group's foreign currency-denominated monetary assets and liabilities and their Philippine peso equivalents is as follows:

	2012		2011	
	US Dollar	Peso equivalent	US Dollar	Peso equivalent
Assets				
Cash and cash equivalents	US\$ 864	₱ 35,447	US\$1,386	₱ 60,759
Trade and other receivables	1,332	54,686	567	24,879
Prepaid expenses and other current assets	28	1,138	—	—
AFS financial assets	12	491	20	862
Noncurrent receivables	59	2,445	44	1,918
	<u>2,295</u>	<u>94,207</u>	<u>2,017</u>	<u>88,418</u>
Liabilities				
Loans payable	1,103	45,249	88	3,878
Accounts payable and accrued expenses	1,213	49,747	661	28,990
Long-term debt (including current maturities)	2,853	117,139	2,761	121,036
Finance lease liabilities	2,474	101,507	2,574	112,751
Other noncurrent liabilities	251	10,291	10	434
	<u>7,894</u>	<u>323,933</u>	<u>6,094</u>	<u>267,089</u>
Net foreign currency-denominated monetary liabilities	<u>(US\$5,599)</u>	<u>(₱229,726)</u>	<u>(US\$4,077)</u>	<u>(₱178,671)</u>

The Group reported net foreign exchange gains (losses) amounting to ₱11,375, (₱823) and ₱6,097 in 2012, 2011 and 2010, respectively, with the translation of its foreign currency-denominated assets and liabilities (Note 33). These mainly resulted from the movements of the Philippine peso against the US dollar as shown in the following table:

	<u>Philippine Peso to US Dollar</u>
December 31, 2012	41.05
December 31, 2011	43.84
December 31, 2010	43.84

The management of foreign currency risk is also supplemented by monitoring the sensitivity of the Group's financial instruments to various foreign currency exchange rate scenarios. Foreign exchange movements affect reported equity in the following ways:

- retained earnings arising from increases or decreases in unrealized and realized foreign exchange gains or losses;
- translation reserves arising from increases or decreases in foreign exchange gains or losses recognized directly as part of other comprehensive income; and
- hedging reserves arising from increases or decreases in foreign exchange gains or losses of the hedged item and the hedging instrument.

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The following table demonstrates the sensitivity to a reasonably possible change in the US dollar exchange rate, with all other 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 (due to translation of results and financial position of foreign operations) as of December 31, 2012 and 2011:

	₱1 decrease in the US Dollar exchange rate		₱1 increase in the US Dollar exchange rate	
	Effect on income before income tax	Effect on equity	Effect on income before income tax	Effect on equity
2012				
Cash and cash equivalents	(₱566)	(₱695)	₱ 566	₱ 695
Trade and other receivables	(223)	(1,265)	223	1,265
Prepaid expenses and other current assets	(28)	(20)	28	20
AFS financial assets	—	(12)	—	12
Noncurrent receivables	(36)	(48)	36	48
	<u>(853)</u>	<u>(2,040)</u>	<u>853</u>	<u>2,040</u>
Loans payable	322	1,006	(322)	(1,006)
Accounts payable and accrued expenses	567	1,044	(567)	(1,044)
Long-term debt (including current maturities)	2,823	2,007	(2,823)	(2,007)
Finance lease liabilities	2,473	1,731	(2,473)	(1,731)
Other noncurrent liabilities	126	212	(126)	(212)
	<u>6,311</u>	<u>6,000</u>	<u>(6,311)</u>	<u>(6,000)</u>
	<u>₱ 5,458</u>	<u>₱ 3,960</u>	<u>(₱ 5,458)</u>	<u>(₱ 3,960)</u>
	₱1 decrease in the US Dollar exchange rate		₱1 Increase in the US Dollar exchange rate	
	Effect on income before income tax	Effect on equity	Effect on income before income tax	Effect on equity
2011				
Cash and cash equivalents	(₱1,219)	(₱1,020)	₱ 1,219	₱ 1,020
Trade and other receivables	(199)	(508)	199	508
AFS financial assets	—	(20)	—	20
Noncurrent receivables	(25)	(36)	25	36
	<u>(1,443)</u>	<u>(1,584)</u>	<u>1,443</u>	<u>1,584</u>
Loans payable	6	86	(6)	(86)
Accounts payable and accrued expenses	322	563	(322)	(563)
Long-term debt (including current maturities)	2,761	1,933	(2,761)	(1,933)
Finance lease liabilities	2,572	1,800	(2,572)	(1,800)
Other noncurrent liabilities	7	8	(7)	(8)
	<u>5,668</u>	<u>4,390</u>	<u>(5,668)</u>	<u>(4,390)</u>
	<u>₱ 4,225</u>	<u>₱ 2,806</u>	<u>(₱4,225)</u>	<u>(₱2,806)</u>

Exposures to foreign exchange rates vary during the year depending on the volume of overseas transactions. Nonetheless, the analysis above is considered to be representative of the Group's currency risk.

Commodity Price Risk

Commodity price risk is the risk that future cash flows from a financial instrument will fluctuate because of changes in commodity prices. The Group enters into various commodity derivatives to manage its price risks on strategic commodities. Commodity hedging allows stability in prices, thus offsetting the risk of volatile market fluctuations. Through hedging, prices of commodities are fixed at levels acceptable to the Group, thus protecting raw material cost and preserving margins. For hedging transactions, if prices go down, hedge positions may show marked-to-market losses; however, any loss in the marked-to-market position is offset by the resulting lower physical raw material cost.

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The Parent Company enters into commodity derivative transactions on behalf of its subsidiaries and affiliates to reduce cost by optimizing purchasing synergies within the Group and managing inventory levels of common materials.

Commodity Swaps, Futures and Options. Commodity swaps, futures and options are used to manage the Group's exposures to volatility in prices of certain commodities such as fuel oil, crude oil, aluminum, soybean meal and wheat.

Commodity Forwards. The Group enters into forward purchases of various commodities. The prices of the commodity forwards are fixed either through direct agreement with suppliers or by reference to a relevant commodity price index.

Liquidity Risk

Liquidity risk pertains to the risk that the Group will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset.

The Group's objectives to manage its liquidity risk are as follows: a) to ensure that adequate funding is available at all times; b) to meet commitments as they arise without incurring unnecessary costs; c) to be able to access funding when needed at the least possible cost; and d) to maintain an adequate time spread of refinancing maturities.

The Group constantly monitors and manages its liquidity position, liquidity gaps and surplus on a daily basis. A committed stand-by credit facility from several local banks is also available to ensure availability of funds when necessary. The Group also uses derivative instruments such as forwards and swaps to manage liquidity.

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The table below summarizes the maturity profile of the Group's financial assets and financial liabilities based on contractual undiscounted payments used for liquidity management as of December 31, 2012 and 2011.

<u>2012</u>	<u>Carrying amount</u>	<u>Contractual cash flow</u>	<u>1 year or less</u>	<u>> 1 year - 2 years</u>	<u>> 2 years - 5 years</u>	<u>Over 5 years</u>
Financial Assets						
Cash and cash equivalents	₱125,631	₱125,631	₱125,631	₱ —	₱ —	₱ —
Trade and other receivables — net	122,599	122,599	122,599	—	—	—
Option deposit (included under “Prepaid expenses and other current assets” account in the consolidated statements of financial position)	1,026	1,026	1,026	—	—	—
Derivative assets (included under “Prepaid expenses and other current assets” account in the consolidated statements of financial position)	91	91	91	—	—	—
Financial assets at FVPL (included under “Prepaid expenses and other current assets” account in the consolidated statements of financial position)	147	147	147	—	—	—
AFS financial assets (including current portion presented under “Prepaid expenses and other current assets” account in the consolidated statements of financial position)	1,621	1,735	181	1,155	399	—
Noncurrent receivables and deposits — net (included under “Other noncurrent assets” account in the consolidated statements of financial position)	14,840	14,840	—	14,840	—	—
Financial Liabilities						
Loans payable	151,274	151,882	151,882	—	—	—
Accounts payable and accrued expenses (excluding current retirement liabilities and IRO)	84,236	84,236	84,236	—	—	—
Derivative liabilities (included under “Accounts payable and accrued expenses” account in the consolidated statements of financial position)	315	315	315	—	—	—
Long-term debt (including current maturities)	224,217	267,303	15,017	77,136	145,243	29,907
Finance lease liabilities (including current portion)	195,154	276,600	18,836	19,421	65,964	172,379
Other noncurrent liabilities (excluding noncurrent retirement liabilities, IRO and ARO)	4,066	4,071	342	3,457	30	242

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2011	Carrying amount	Contractual cash flow	1 year or less	> 1 year - 2 years	> 2 years - 5 years	Over 5 years
Financial Assets						
Cash and cash equivalents	₱128,975	₱128,975	₱128,975	₱ —	₱ —	₱ —
Trade and other receivables — net	84,472	84,472	84,472	—	—	—
Derivative assets (included under “Prepaid expenses and other current assets” account in the consolidated statements of financial position)	121	121	121	—	—	—
Financial assets at FVPL (included under “Prepaid expenses and other current assets” account in the consolidated statements of financial position)	194	194	194	—	—	—
AFS financial assets	2,068	2,136	85	1,254	797	—
Noncurrent receivables and deposits — net (included under “Other noncurrent assets” account in the consolidated statements of financial position)	27,471	28,021	1,610	26,030	381	—
Financial Liabilities						
Loans payable	82,588	83,078	83,078	—	—	—
Accounts payable and accrued expenses (excluding current retirement liabilities and IRO)	61,424	61,424	61,424	—	—	—
Derivative liabilities (included under “Accounts payable and accrued expenses” account in the consolidated statements of financial position)	118	118	118	—	—	—
Long-term debt (including current maturities)	211,420	252,614	30,092	15,206	177,748	29,568
Finance lease liabilities (including current portion)	208,261	295,587	17,675	28,483	48,443	200,986
Other noncurrent liabilities (excluding noncurrent retirement liabilities, IRO and ARO)	2,348	2,357	257	1,620	47	433

Credit Risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group’s trade and other receivables and investment securities. The Group manages its credit risk mainly through the application of transaction limits and close risk monitoring. It is the Group’s policy to enter into transactions with a wide diversity of creditworthy counterparties to mitigate any significant concentration of credit risk.

The Group has regular internal control reviews to monitor the granting of credit and management of credit exposures.

Trade and Other Receivables

The Group’s exposure to credit risk is influenced mainly by the individual characteristics of each customer. However, management also considers the demographics of the Group’s customer base, including the default risk of the industry and country in which customers operate, as these factors may have an influence on the credit risk.

Goods are subject to retention of title clauses so that in the event of default, the Group would have a secured claim. Where appropriate, the Group obtains collateral or arranges master netting agreements.

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The Group has established a credit policy under which each new customer is analyzed individually for creditworthiness before the Group's standard payment and delivery terms and conditions are offered. The Group ensures that sales on account are made to customers with appropriate credit history. The Group has detailed credit criteria and several layers of credit approval requirements before engaging a particular customer or counterparty. The Group's review includes external ratings, when available, and in some cases bank references. Purchase limits are established for each customer and are reviewed on a regular basis. Customers that fail to meet the Group's benchmark creditworthiness may transact with the Group only on a prepayment basis.

The Group establishes an allowance for impairment losses that represents its estimate of incurred losses in respect of trade and other receivables. The main components of this allowance include a specific loss component that relates to individually significant exposures, and a collective loss component established for groups of similar assets in respect of losses that have been incurred but not yet identified. The collective loss allowance is determined based on historical data of payment statistics for similar financial assets.

Investments

The Group recognizes impairment losses based on specific and collective impairment tests, when objective evidence of impairment has been identified either on an individual account or on a portfolio level.

Financial information on the Group's maximum exposure to credit risk as of December 31, 2012 and 2011, without considering the effects of collaterals and other risk mitigation techniques, is presented below.

	<i>Note</i>	2012	2011
Cash and cash equivalents	9	₱125,631	₱128,975
Trade and other receivables — net	10	122,599	84,472
Option deposit	12	1,026	—
Derivative assets	12	91	121
Financial assets at FVPL	12	147	194
AFS financial assets	12, 14	1,621	2,068
Noncurrent receivables and deposits — net	20	14,840	27,471
		₱265,955	₱243,301

The credit risk for cash and cash equivalents, option deposit, derivative assets, financial assets at FVPL and AFS financial assets is considered negligible, since the counterparties are reputable entities with high quality external credit ratings.

The Group's exposure to credit risk arises from default of counterparty. Generally, the maximum credit risk exposure of trade and other receivables and noncurrent receivables and deposits is its carrying amount without considering collaterals or credit enhancements, if any. The Group has no significant concentration of credit risk since the Group deals with a large number of homogenous trade customers. The Group does not execute any credit guarantee in favor of any counterparty.

Financial and Other Risks Relating to Livestock

The Group is exposed to financial risks arising from the change in cost and supply of feed ingredients and the selling prices of chicken, hogs and cattle and related products, all of which are determined by constantly changing market forces such as supply and demand and other factors. The other factors include environmental regulations, weather conditions and livestock diseases for which the Group has little control. The mitigating factors are listed below.

- The Group is subject to risks affecting the food industry, generally, including risks posed by food spoilage and contamination. Specifically, the fresh meat industry is regulated by environmental, health and food safety organizations and regulatory sanctions. The Group has put into place systems to monitor food safety risks throughout all stages of manufacturing and processing to mitigate these risks. Furthermore, representatives from the government regulatory agencies are present at all times during the processing of dressed chicken, hogs and cattle in all dressing plants and meat plants and issue certificates accordingly. The authorities, however, may impose additional regulatory requirements that may require significant capital investment at short notice.

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- The Group is subject to risks relating to its ability to maintain animal health status considering that it has no control over neighboring livestock farms. Livestock health problems could adversely impact production and consumer confidence. However, the Group monitors the health of its livestock on a daily basis and proper procedures are put in place.
- The livestock industry is exposed to risk associated with the supply and price of raw materials, mainly grain prices. Grain prices fluctuate depending on the harvest results. The shortage in the supply of grain will result in adverse fluctuation in the price of grain and will ultimately increase the Group's production cost. If necessary, the Group enters into forward contracts to secure the supply of raw materials at reasonable price.

Other Market Price Risk

The Group's market price risk arises from its investments carried at fair value (financial assets at FVPL and AFS financial assets). The Group manages its risk arising from changes in market price by monitoring the changes in the market price of the investments.

Capital Management

The primary objective of the Group's capital management is to ensure that it maintains a strong credit rating and healthy capital ratios in order to support its businesses and maximize shareholder value.

The Group manages its capital structure and makes adjustments in the light of changes in economic conditions. To maintain or adjust the capital structure, the Group may adjust the dividend payment to shareholders, pay-off existing debts, return capital to shareholders or issue new shares.

The Group defines capital as paid-in capital stock, additional paid-in capital and retained earnings, both appropriated and unappropriated. Other components of equity such as treasury shares and cumulative translation adjustments are excluded from capital for purposes of capital management.

The BOD has overall responsibility for monitoring capital in proportion to risk. Profiles for capital ratios are set in the light of changes in the Group's external environment and the risks underlying the Group's business, operation and industry.

The Group monitors capital on the basis of debt-to-equity ratio, which is calculated as total debt divided by total equity. Total debt is defined as total current liabilities and total noncurrent liabilities, while equity is total equity as shown in the consolidated statements of financial position.

The Group, except for BOC which is subject to certain capitalization requirements by the BSP, is not subject to externally imposed capital requirements.

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42. Financial Assets and Financial Liabilities

The table below presents a comparison by category of carrying amounts and fair values of the Group's financial instruments as of December 31, 2012 and 2011:

	2012		2011	
	Carrying amount	Fair value	Carrying amount	Fair value
Financial Assets				
Cash and cash equivalents	₱125,631	₱125,631	₱128,975	₱128,975
Trade and other receivables — net	122,599	122,599	84,472	84,472
Option deposit (included under “Prepaid expenses and other current assets” account in the consolidated statements of financial position)	1,026	1,026	—	—
Derivative assets (included under “Prepaid expenses and other current assets” account in the consolidated statements of financial position)	91	91	121	121
Financial assets at FVPL (included under “Prepaid expenses and other current assets” account in the consolidated statements of financial position)	147	147	194	194
AFS financial assets (including current portion presented under “Prepaid expenses and other current assets” account in the consolidated statements of financial position)	1,621	1,621	2,068	2,068
Noncurrent receivables and deposits — net (included under “Other noncurrent assets” account in the consolidated statements of financial position)	14,840	14,840	27,471	27,471
Financial Liabilities				
Loans payable	151,274	151,274	82,588	82,588
Accounts payable and accrued expenses (excluding current retirement liabilities and IRO)	84,236	84,236	61,424	61,424
Derivative liabilities (included under “Accounts payable and accrued expenses” account in the consolidated statements of financial position)	315	315	118	118
Long-term debt (including current maturities)	224,217	239,625	211,420	228,523
Finance lease liabilities (including current portion)	195,154	195,154	208,261	208,261
Other noncurrent liabilities (excluding noncurrent retirement liabilities, IRO and ARO)	4,066	4,066	2,348	2,348

The following methods and assumptions are used to estimate the fair value of each class of financial instruments:

Cash and Cash Equivalents, Trade and Other Receivables, Option Deposit and Noncurrent Receivables and Deposits. The carrying amount of cash and cash equivalents, trade and other receivables and option deposit approximates fair value primarily due to the relatively short-term maturities of these financial instruments. In the case of noncurrent receivables and deposits, the fair value is based on the present value of expected future cash flows using the applicable discount rates based on current market rates of identical or similar quoted instruments.

Derivatives. The fair values of forward exchange contracts are calculated by reference to current forward exchange rates. In the case of freestanding currency and commodity derivatives, the fair values are determined based on quoted prices obtained from their respective active markets. Fair values for stand-alone derivative instruments that are not quoted from an active market and for embedded derivatives are based on valuation models used for similar instruments using both observable and non-observable inputs.

Financial Assets at FVPL and AFS Financial Assets. The fair values of publicly traded instruments and similar investments are based on quoted market prices in an active market. For debt instruments with no quoted market prices, a reasonable estimate of their fair values is calculated based on the expected cash flows from the instruments discounted using the applicable discount rates of comparable instruments quoted in active markets. Unquoted equity securities are carried at cost less impairment.

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Loans Payable and Accounts Payable and Accrued Expenses. The carrying amount of loans payable and accounts payable and accrued expenses approximates fair value due to the relatively short-term maturities of these financial instruments.

Long-term Debt, Finance Lease Liabilities and Other Noncurrent Liabilities. The fair value of interest-bearing fixed-rate loans is based on the discounted value of expected future cash flows using the applicable market rates for similar types of instruments as of reporting date. Discount rates used for Philippine peso-denominated loans range from 0.5% to 4.3% and 1.7% to 5.4% as of December 31, 2012 and 2011, respectively. The discount rates used for foreign currency-denominated loans range from 0.2% to 0.8% and 0.3% to 1.0% as of December 31, 2012 and 2011, respectively. The carrying amounts of floating rate loans with quarterly interest rate repricing approximate their fair values.

Derivative Financial Instruments

The Group's derivative financial instruments according to the type of financial risk being managed and the details of freestanding and embedded derivative financial instruments are discussed below.

The Group enters into various currency and commodity derivative contracts to manage its exposure on foreign currency and commodity price risk. The portfolio is a mixture of instruments including forwards, swaps and options.

Derivative Instruments Not Designated as Hedges

The Group enters into certain derivatives as economic hedges of certain underlying exposures. These include freestanding and embedded derivatives found in host contracts, which are not designated as accounting hedges. Changes in fair value of these instruments are accounted for directly in profit or loss. Details are as follows:

Freestanding Derivatives

Freestanding derivatives consist of commodity and currency derivatives entered into by the Group.

Currency Forwards

The Group has outstanding foreign currency forward contracts with aggregate notional amount of US\$963 and US\$220 as of December 31, 2012 and 2011, respectively, and with various maturities in 2013 and 2012. The net positive (negative) fair value of these currency forwards amounted to (P217) and P40 as of December 31, 2012 and 2011, respectively.

Commodity Swaps

The Group has outstanding swap agreements covering its aluminum requirements, with various maturities in 2013 and 2012. Under the agreement, payment is made either by the Group or its counterparty for the difference between the agreed fixed price of aluminum and the price based on the relevant price index. The outstanding equivalent notional quantity covered by the commodity swaps is 525 and 845 metric tons as of December 31, 2012 and 2011, respectively. The net positive (negative) fair value of these swaps amounted to P2 and (P13) as of December 31, 2012 and 2011, respectively.

The Group has outstanding swap agreements covering its oil requirements, with various maturities in 2013 and 2012. Under the agreement, payment is made either by the Group or its counterparty for the difference between the hedged fixed price and the relevant monthly average index price. The outstanding equivalent notional quantity covered by the commodity swaps is 0.5 and 1.8 million barrels as of December 31, 2012 and 2011, respectively. The positive fair value of these swaps amounted to P30 and P147 as of December 31, 2012 and 2011, respectively.

Commodity Options

The Group has outstanding bought and sold options covering its wheat requirements with notional quantities of 85,457 and 47,083 metric tons as of December 31, 2012 and 2011, respectively. These options can be exercised at various calculation dates in 2013 and 2012 with specified quantities on each calculation date. The net negative fair value of these options amounted to P41 and P5 as of December 31, 2012 and 2011, respectively.

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The Group has outstanding bought and sold options covering its soybean meal requirements with notional quantity of 7,439 metric tons as of December 31, 2011. These options can be exercised at various calculation dates in 2012 with specified quantities on each calculation date. The negative fair value of these options amounted to ₱5 as of December 31, 2011. There were no outstanding options on the purchase of soybean meal as of December 31, 2012.

The Group has outstanding commodity options covering its crude oil requirements with notional quantity of 0.2 and 1.3 million barrels as of December 31, 2012 and 2011, respectively. These call and put options can be exercised at various calculation dates in 2013 and 2012 with specified quantities on each calculation date. The net positive fair value of these options amounted to ₱15 and ₱47 as of December 31, 2012 and 2011, respectively.

Embedded Derivatives

The Group's embedded derivatives include currency derivatives (forwards and options) embedded in non-financial contracts.

Embedded Currency Forwards

The total outstanding notional amount of currency forwards embedded in non-financial contracts amounted to US\$182 and US\$201 as of December 31, 2012 and 2011, respectively. These non-financial contracts consist mainly of foreign currency denominated purchase orders, sales agreements and capital expenditures. The embedded forwards are not clearly and closely related to their respective host contracts. The net positive (negative) fair value of these embedded currency forwards amounted to ₱38 and (₱2) as of December 31, 2012 and 2011, respectively.

Embedded Currency Options

The total outstanding notional amount of currency options embedded in non-financial contracts amounted to US\$14 and US\$24 as of December 31, 2012 and 2011, respectively. These non-financial contracts consist mainly of sales agreements. These embedded options are not clearly and closely related to their host contracts. The net negative fair value of these embedded currency options amounted to ₱6 and ₱11 as of December 31, 2012 and 2011, respectively.

The Group recognized marked-to-market gains (losses) from freestanding and embedded derivatives amounting to (₱1,270), ₱182 and ₱660 in 2012, 2011 and 2010, respectively.

Fair Value Changes on Derivatives

The net movements in fair value of all derivative instruments for the years ended December 31, 2012 and 2011 are as follows:

	<u>2012</u>	<u>2011</u>
Balance at beginning of year	₱ 3	₱178
Net change in fair value of non-accounting hedges	<u>(1,270)</u>	<u>182</u>
	(1,267)	360
Less fair value of settled instruments	<u>(1,043)</u>	<u>357</u>
Balance at end of year	<u>(₱224)</u>	<u>₱ 3</u>

Fair Value Hierarchy

Financial assets and financial liabilities measured at fair value in the consolidated statements of financial position are categorized in accordance with the fair value hierarchy. This hierarchy groups financial assets and financial liabilities into three levels based on the significance of inputs used in measuring the fair value of the financial assets and financial liabilities.

The table below analyzes financial instruments carried at fair value by valuation method as of December 31, 2012 and 2011. The different levels have been defined as follows:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;

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- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly; and
- Level 3: inputs for the asset or liability that are not based on observable market data.

<u>2012</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Total</u>
Financial Assets			
Derivative assets	P —	P 91	P 91
Financial assets at FVPL	147	—	147
AFS financial assets	741	880	1,621
Financial Liabilities			
Derivative liabilities	—	315	315
<u>2011</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Total</u>
Financial Assets			
Derivative assets	P 2	P 119	P 121
Financial assets at FVPL	194	—	194
AFS financial assets	1,069	999	2,068
Financial Liabilities			
Derivative liabilities	10	108	118

The Group has no financial instruments valued based on Level 3 as of December 31, 2012 and 2011. During the year, there were no transfers between Level 1 and Level 2 fair value measurements, and no transfers into and out of Level 3 fair value measurements.

43. Registration with the BOI

▪ SMC Global

SMEC, SPDC, SPPC and PanAsia are registered with the BOI as administrator/ operator of their respective power plant on a pioneer status with non-pioneer incentives and were granted Income Tax Holiday (ITH) for four (4) years without extension beginning August 1, 2010, subject to compliance with certain requirements under their registrations. The ITH incentives availed was limited only to the sale of power generated from the power plants. On August 26, 2011, SMC Global sold its 100% ownership in PanAsia to MHI (Note 5).

▪ SMPFC

Certain operations of consolidated subsidiaries of SMPFC are registered with the BOI as pioneer and non-pioneer activities. As registered enterprises, these subsidiaries are subject to some requirements and are entitled to certain tax and non-tax incentives which are considered in the computation of the income tax expense.

GBGTC

GBGTC was registered with the BOI under Registration No. 2012-223 on a non-pioneer status as a New Operator of Warehouse for its grain terminal project in Mabini, Batangas on October 19, 2012.

Under the terms of GBGTC's BOI registration and subject to certain requirements as provided in the Omnibus Investments Code of 1987, GBGTC is entitled to incentives which include, among others, ITH for a period of four (4) years from July 2013 or actual start of commercial operations, whichever is earlier, but in no case earlier than the date of registration.

SMFI

SMFI's (formerly Monterey) Sumilao Hog Project (Sumilao Project) was registered with the BOI under Registration No. 2008-192, in accordance with the provisions of the Omnibus Investments Code of 1987 on a pioneer status as New Producer of Hogs on July 30, 2008. As a BOI-registrant, the Sumilao Project is entitled to incentives which include, among others, ITH for a period of six (6) years, extendable under certain conditions to eight (8) years, from February 2009 or actual start of commercial operations, whichever is earlier, but in no case earlier than the date of registration.

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PF-Hormel

The existing registration of PF-Hormel with the BOI was made on May 18, 2006 in accordance with the provisions of the Omnibus Investments Code of 1987 as a new producer of processed meat products on a non-pioneer status. Under the terms of this new registration, PF-Hormel is entitled to certain tax incentives, including ITH for four (4) years from July 2007, or from the actual start of commercial operations, whichever comes first, but in no case earlier than the date of registration.

PF-Hormel's new registered activity with the BOI commenced commercial operations in July 2007 and began to avail tax incentives since then.

▪ **Petron**

Mixed Xylene, Benzene, Toluene (BTX) and Propylene Recovery Units

On October 20, 2005, Petron registered with the BOI under the Omnibus Investments Code of 1987 (EO 226) as: (1) a non-pioneer, new export producer status of Mixed Xylene; (2) a pioneer, new export producer status of Benzene and Toluene; and (3) a pioneer, new domestic producer status of Propylene. Under the terms of its registration, Petron is subject to certain requirements principally that of exporting at least 70% of the production of the mentioned petrochemical products every year (except for the requirement on the export of the production of Toluene which, in 2012, was reduced to 50%) except for the produced Propylene.

As a registered enterprise, Petron is entitled to the following benefits on its production of petroleum products used as petrochemical feedstock:

- a. ITH: (1) for four (4) years from May 2008 or actual start of commercial operations, whichever is earlier, but in no case earlier than the date of registration for Mixed Xylene subject to base figure of 120,460 metric tons per year representing Petron's highest attained production volume for the last three (3) years; (2) for six (6) years from May 2008 or actual start of commercial operations, whichever is earlier, but in no case earlier than the date of registration for Benzene and Toluene; and (3) for six (6) years from December 2007 or actual start of commercial operations, whichever is earlier, but in no case earlier than the date of registration for Propylene;
- b. Tax credit equivalent to the national internal revenue taxes and duties paid on raw materials and supplies and semi-manufactured products used in producing its export product and forming parts thereof for ten (10) years from start of commercial operations;
- c. Simplification of customs procedures;
- d. Access to Customs Bonded Manufacturing Warehouse (CBMW) subject to Customs rules and regulations provided firm exports at least 70% of production output of Mixed Xylene, Benzene and 50% of Toluene;
- e. Exemption from wharfage dues, any export tax, duty, imposts and fees for a ten-year period from date of registration;
- f. Importation of consigned equipment for a period of ten (10) years from the date of registration subject to the posting of re-export bond;
- g. Exemption from taxes and duties on imported spare parts and consumable supplies for export producers with CBMW exporting at least 70% production of Mixed Xylene, Benzene and 50% of Toluene; and
- h. Petron may qualify to import capital equipment, spare parts, and accessories at zero percent (one percent for Propylene) duty from date of registration up to June 5, 2006 pursuant to EO No. 313 and its Implementing Rules and Regulations.

Mixed Xylene entitlement period ended in April 2012 and the registration for Mixed Xylene was cancelled on August 10, 2012.

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Fluidized Bed Catalytic Cracker (PetroFCC) Unit

On December 20, 2005, the BOI approved Petron's application under RA 8479 for new investment at its Bataan Refinery for the PetroFCC. Subject to Petron's compliance with the terms and conditions of registration, the BOI is extending the following major incentives:

- a. ITH for five (5) years without extensions or bonus year from December 2008 or actual start of commercial operations, whichever is earlier, but in no case earlier than the date of registration subject to a rate of exemption computed based on the percentage (%) share of product that are subject to retooling;
- b. Minimum duty of three percent (3%) and VAT on imported capital equipment and accompanying spare parts;
- c. Tax credit on domestic capital equipment shall be granted on locally fabricated capital equipment. This shall be equivalent to the difference between the tariff rate and the three percent (3%) duty imposed on the imported counterpart;
- d. Importation of consigned equipment for a period of five (5) years from date of registration subject to posting of the appropriate re-export bond; provided that such consigned equipment shall be for the exclusive use of the registered activity;
- e. Exemption from wharfage dues, any export tax, duty, imports and fees for a ten-year period from date of registration;
- f. Exemption from taxes and duties on imported spare parts for consigned equipment with bonded manufacturing warehouse;
- g. Exemption from real property tax on production equipment or machinery; and
- h. Exemption from contractor's tax.

70 MW Coal-Fired Power Plant (Limay, Bataan)

On November 3, 2010, Petron registered with the BOI as new operator of a 70 MW Coal-Fired Power Plant on a pioneer status with non-pioneer incentives under the Omnibus Investments Code of 1987 (EO No. 226). Subject to Petron's compliance with the terms and conditions of registration, the BOI is extending the following major incentives:

- a. ITH for four (4) years from July 2012 or actual start of commercial operations, whichever is earlier, but in no case earlier than the date of registration limited to the revenue generated from the electricity sold to the grid;
- b. Importation of consigned equipment for a period of ten (10) years from the date of registration subject to the posting of re-export bond; and
- c. Petron may qualify to import capital equipment, spare parts and accessories at zero percent (0%) duty from date of registration up to June 16, 2011 pursuant to EO No. 528 and its Implementing Rules and Regulations.

RMP-2 Project

On June 3, 2011, the BOI approved Petron's application under RA No. 8479 as an Existing Industry Participant with New Investment in Modernization/Conversion of Bataan Refinery's RMP-2. The BOI is extending the following major incentives:

- a. ITH for five (5) years without extension or bonus year from July 2015 or actual start of commercial operations, whichever is earlier, but in no case earlier than the date of registration based in the formula of the ITH rate of exemption;
- b. Minimum duty of three percent (3%) and VAT on imported capital equipment and accompanying spare parts;
- c. Importation of consigned equipment for a period of five (5) years from date of registration subject to posting of the appropriate re-export bond; provided that such consigned equipment shall be for the exclusive use of the registered activity;

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- d. Tax credit on domestic capital equipment shall be granted on locally fabricated capital equipment which is equivalent to the difference between the tariff rate and the three percent (3%) duty imposed on the imported counterpart;
- e. Exemption from real property tax on production equipment or machinery; and
- f. Exemption from contractor's tax.

Yearly certificates of entitlement have been timely obtained by Petron to support its ITH credits.

▪ **SMYAC**

SMYAC is registered with the BOI as a new domestic producer of glass containers for the new production facility (Phase I) and as expanding producer of glass containers for the expansion of the existing production facility (Phase II), both on a non-pioneer status under the Omnibus Investments Code of 1987.

As a registered enterprise, SMYAC is entitled to the following benefits:

- ITH;
 - i. Phase I — for a period of four (4) years from February 2007 or actual start of commercial operations, whichever is earlier, but in no case earlier than March 23, 2005, the date of registration; and
 - ii. Phase II — for a period of three (3) years from August 2007 or actual start of commercial operations, whichever is earlier, but in no case earlier than March 23, 2005, the date of registration.

SMYAC's entitlement for ITH for Phase I expired in August 2010 while the entitlement for ITH for Phase II was extended until November 2012.

44. Events After the Reporting Date

a. Investment in Excelon Asia Holding Corporation (EAHC), New Manila Properties Inc. (NMPI) and Philnico Holdings Limited (PHL)

On January 11, 2013, Clariden entered into separate Deeds of Absolute Sale of Shares for the purchase of the outstanding capital stock of the following companies:

Clariden purchased 1,000,000 shares representing 100% equity interest in NMPI for a total consideration of ₱283. NMPI is a company primarily engaged in the business of real estate development.

Clariden purchased 120,000 shares representing 100% equity interest in EAHC for a total consideration of ₱343. The primary purpose of EAHC is to acquire by purchase, exchange, assign, gift or otherwise, and to sell, assign, transfer, exchange, lease, let, develop, mortgage, pledge, traffic, deal in and with otherwise operate, enjoy, and dispose of, all properties of every kind and description and whenever situated and as to the extent permitted by law.

Clariden purchased 8,704 shares representing 100% equity interest in PHL for a total consideration of ₱56.

b. Issuance of Undated Subordinated Capital Securities by Petron

On February 6, 2013, Petron issued undated subordinated capital securities at the issue price of 100% amounting to US\$500 (the February 6 Issuance). On March 11, 2013, Petron further issued undated subordinated capital securities at the issue price of 104.25% amounting to US\$250 which were consolidated, and formed a single series, with the February 6 Issuance. At the option of the issuer, the securities may be redeemed after five and a half years or on any distribution payment date thereafter. The proceeds will be applied by Petron towards capital and other expenditures in respect of RMP-2 and used for general corporate purposes. The securities were listed on the Hong Kong Stock Exchange.

c. Tender Offer for US\$600 Exchangeable Bonds

Pursuant to the resolution of the BOD of the Parent Company approved during its regular meeting held last January 17, 2013 authorizing management to refinance its existing financial obligations under such terms and conditions which are favorable and advantageous to the Parent Company, the Parent Company solicited from the

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holders of the outstanding US\$600, 2.0% Exchangeable Bonds due 2014, listed on the SGX-ST, their consent to tender their bonds for repurchase (Invitation to Tender). The bonds are exchangeable for common shares of stock of the Parent Company, to be issued out of the Parent Company's treasury shares.

To afford the investing public and existing shareholders of the Parent Company sufficient time to be apprised of, and to evaluate, the Invitation to Tender, the Parent Company filed a request with the PSE for a suspension of the trading in the Parent Company's common shares for a period of six (6) trading days. Given the foregoing request of the Parent Company, the PSE implemented the trading suspension of SMC common shares from January 23, 2013 to January 30, 2013.

The Parent Company delivered the notices relating to the Invitation to Tender to the SGX-ST in the afternoon of January 22, 2013 (Singapore time), and the Invitation to Tender commenced in the morning of, and end in the evening of, January 29, 2013.

On February 7, 2013, the Parent Company has repurchased Bonds having an aggregate principal amount of US\$259. The aggregate cash amount paid by the Parent Company based on the aggregate principal amount of the Bonds repurchased, as well as accrued but unpaid interest payable until February 7, 2013, is US\$281. The aggregate principal amount of the Bonds remaining outstanding following completion of the Invitation to Tender is US\$332.

45. Other Matters

a. Contingencies

The Group is a party to certain lawsuits or claims (mostly labor related cases) filed by third parties which are either pending decision by the courts or are subject to settlement agreements. The outcome of these lawsuits or claims cannot be presently determined. In the opinion of management and its legal counsel, the eventual liability from these lawsuits or claims, if any, will not have a material effect on the consolidated financial statements of the Group.

▪ Deficiency Excise Tax

On April 12, 2004 and May 26, 2004, the Parent Company was assessed by the BIR for deficiency excise tax on "San Mig Light", one of its beer products. The Parent Company contested the assessments before the Court of Tax Appeals (CTA) (1st Division) under CTA case numbers 7052 and 7053.

In relation to the aforesaid contested assessments, the Parent Company, on January 31, 2006, filed with the CTA (1st Division), under CTA case number 7405, a claim for refund of taxes paid in excess of what it believes to be the excise tax rate applicable to it.

The above assessment cases (CTA case numbers 7052 and 7053) and claim for refund (CTA case number 7405), which involve common questions of fact and law, were subsequently consolidated and jointly tried.

On November 27, 2007, the Parent Company filed with the CTA (3rd Division), under CTA case number 7708, a second claim for refund, also in relation to the contested assessments, as it was obliged to continue paying excise taxes in excess of what it believes to be the applicable excise tax rate.

On January 11, 2008, the BIR addressed a letter to the Parent Company, appealing to the Parent Company to settle its alleged tax liabilities subject of CTA case numbers 7052 and 7053 "in order to obviate the necessity of issuing a Warrant of Dstraint and Garnishment and/or Levy." The Parent Company's external legal counsel responded to the aforesaid letter and met with appropriate officials of the BIR and explained to the latter the unfairness of the issuance of a Warrant of Dstraint and Garnishment and/or Levy against the Parent Company, especially in view of the Parent Company's pending claims for refund. As of March 21, 2013, the BIR has taken no further action on the matter.

On July 24, 2009, the Parent Company filed its third claim for refund with the CTA (3rd Division), under CTA case number 7953, also in relation to the contested assessments. This case is still undergoing trial.

On January 7, 2011, the CTA (3rd Division) under CTA case number 7708 rendered its decision in this case, granting the Parent Company's petition for review on its claim for refund and ordering respondent Commissioner of Internal Revenue to refund or issue a tax credit certificate in favor of the Parent Company in the amount of

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₱926, representing erroneously, excessively and/or illegally collected and overpaid excise taxes on “San Mig Light” during the period from December 1, 2005 up to July 31, 2007. This decision was elevated by the BIR Commissioner to the CTA En Banc and was denied in the case docketed as CTA EB No. 755. The Office of the Solicitor General filed with the Second Division of the Supreme Court a Petition for Review.

On October 18, 2011, the CTA (1st Division) rendered its joint decision in CTA case numbers 7052, 7053 and 7405, cancelling and setting aside the deficiency excise tax assessments against the Parent Company, granting the latter’s claim for refund and ordering the BIR Commissioner to refund or issue a tax credit certificate in its favor in the amount of ₱781, representing erroneously, excessively and/or illegally collected and overpaid excise taxes on “San Mig Light” during the period from February 1, 2004 to November 30, 2005. A motion for reconsideration filed by the BIR Commissioner on the aforesaid decision has been denied and the Commissioner elevated the decision to CTA En Banc for review, which was docketed as CTA EB No. 873, the same was dismissed in a Decision dated October 24, 2012. The subsequent Motion for Reconsideration filed by the Commissioner was likewise denied.

In the meantime, effective October 1, 2007, the Parent Company spun off its domestic beer business into a new company, SMB. SMB continued to pay the excise taxes on “San Mig Light” at the higher rate required by the BIR.

On September 28, 2009, SMB filed a claim for refund with the CTA (3rd Division) under CTA case number 7973; on December 28, 2010, its second claim for refund with the CTA (1st Division) under case number 8209; on December 23, 2011, its third claim for refund with the CTA (3rd Division) under case number 8400, and last December 2012, SMB filed its fourth claim for refund with CTA. All of these cases are undergoing trial.

▪ *Tax Credit Certificates Cases*

In 1998, the BIR issued a deficiency excise tax assessment against Petron relating to Petron’s use of ₱659 worth of Tax Credit Certificates (“TCCs”) to pay certain excise tax obligations from 1993 to 1997. The TCCs were transferred to Petron by suppliers as payment for fuel purchases. Petron contested the BIR’s assessment before the CTA. In July 1999, the CTA ruled that as a fuel supplier of BOI-registered companies, Petron was a qualified transferee of the TCCs and that the collection by the BIR of the alleged deficiency excise taxes was contrary to law. On March 21, 2012, the Court of Appeals promulgated a decision in favor of Petron and against the BIR affirming the ruling of the CTA striking down the assessment issued by the BIR to Petron. On April 19, 2012, a motion for reconsideration was filed by the BIR, which was denied by the CTA in its Resolution dated October 10, 2012. The BIR elevated the case to the Supreme Court through a petition for review on *certiorari* dated December 5, 2012.

▪ *Pandacan Terminal Operations*

In November 2001, the City of Manila enacted Ordinance No. 8027 reclassifying the areas occupied by the oil terminals of Petron, Pilipinas Shell Petroleum Corporation (Shell) and Chevron Philippines Inc. (Chevron) from industrial to commercial. This reclassification made the operation of the oil terminals in Pandacan, Manila illegal. However, in June 2002, Petron, together with Shell and Chevron, entered into an MOU with the City of Manila and the DOE, agreeing to scale down operations, recognizing that this was a sensible and practical solution to reduce the economic impact of Ordinance No. 8027. In December 2002, in reaction to the MOU, the Social Justice Society (SJS) filed a petition with the Supreme Court against the Mayor of Manila asking that the latter be ordered to enforce Ordinance No. 8027. In April 2003, Petron filed a petition with the Regional Trial Court (RTC) to annul Ordinance No.8027 and enjoin its implementation. On the basis of a *status quo* order issued by the RTC, Mayor of Manila ceased implementation of Ordinance No. 8027.

The City of Manila subsequently issued the Comprehensive Land Use Plan and Zoning Ordinance (Ordinance No. 8119), which applied to the entire City of Manila. Ordinance No. 8119 allowed Petron (and other non-conforming establishments) a seven-year grace period to vacate. As a result of the passage of Ordinance No. 8119, which was thought to effectively repeal Ordinance No. 8027, in April 2007, the RTC dismissed the petition filed by Petron questioning Ordinance No. 8027.

However, on March 7, 2007, in the case filed by SJS, the Supreme Court rendered a decision (the March 7 Decision) directing the Mayor of Manila to immediately enforce Ordinance No. 8027. On March 12, 2007, Petron, together with Shell and Chevron, filed motions with the Supreme Court seeking intervention and

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reconsideration of the March 7 Decision. In the same year, Petron also filed a petition before the RTC of Manila praying for the nullification of Ordinance No. 8119 on the grounds that the reclassification of the oil terminals was arbitrary, oppressive and confiscatory, and thus unconstitutional, and that the said Ordinance contravened the provisions of the Water Code of the Philippines (Presidential Decree No. 1067, the Water Code). On February 13, 2008, Petron, Shell and Chevron were allowed by the Supreme Court to intervene in the case filed by SJS but their motions for reconsideration were denied. The Supreme Court declared Ordinance No. 8027 valid and dissolved all existing injunctions against the implementation of the Ordinance No. 8027.

In May 2009, Manila City Mayor Alfredo Lim approved Ordinance No. 8187, which repealed Ordinance No. 8027 and Ordinance No. 8119 and permitted the continued operations of the oil terminals in Pandacan.

On August 24, 2012, the RTC of Manila ruled that Section 23 of Ordinance No. 8119 relating to the reclassification of subject oil terminals had already been repealed by Ordinance No. 8187; hence any issue pertaining thereto had become moot and academic. The RTC of Manila also declared Section 55 of Ordinance No. 8119 null and void for being in conflict with the Water Code. Nonetheless, the RTC upheld the validity of all other provisions of Ordinance No. 8119. On September 25, 2012, Petron sought clarification and partial consideration of the August 24 decision and prayed for the nullification of the entire Ordinance No. 8119. In an order dated December 18, 2012, the RTC of Manila denied the motion filed by Petron. Petron filed a notice of appeal on January 23, 2013. In an order dated February 6, 2013, the RTC of Manila ordered the records to be forwarded to the Court of Appeals.

With regard to Ordinance No. 8187, petitions were filed before the Supreme Court, seeking for its nullification and the enjoinder of its implementation. Petron filed a manifestation on November 30, 2010 informing the Supreme Court that, without prejudice to its position in the cases, it had decided to cease operation of its petroleum product storage facilities in Pandacan within 5 years or not later than January 2016 due to the many unfounded environmental issues being raised that tarnish the image of Petron and the various amendments being made to the zoning ordinances of the City of Manila when the composition of the local government changes that prevented Petron from making long-term plans. In a letter dated July 6, 2012 (with copies to the offices of the Vice Mayor and the City Council of Manila), Petron reiterated its commitment to cease the operation of its petroleum product storage facilities and transfer them to another location by January 2016.

▪ *Oil Spill Incident in Guimaras*

On August 11, 2006, MT Solar I, a third party vessel contracted by Petron to transport approximately two million liters of industrial fuel oil, sank 13 nautical miles southwest of Guimaras, an island province in the Western Visayas region of the Philippines. In separate investigations by the Philippine Department of Justice (DOJ) and the Special Board of Marine Inquiry (SBMI), both agencies found the owners of MT Solar I liable. The DOJ found Petron not criminally liable, but the SBMI found Petron to have overloaded the vessel. Petron has appealed the findings of the SBMI to the DOTC and is awaiting its resolution. Petron believes that SBMI can impose administrative penalties on vessel owners and crew, but has no authority to penalize other parties, such as Petron, which are charterers.

In 2009, complaints for violation of the Philippine Clean Water Act of 2004 (Republic Act No. 9275, the Clean Water Act) and homicide and less serious physical injuries were filed against Petron. Complainants claim that their exposure to and close contact with waters along the shoreline and mangroves affected by the oil spill has caused them major health problems. On February 13, 2012, an Information was filed against the owner and the Captain of MT Solar 1 and the former President and Chairman of Petron for violation of the Clean Water Act. On March 28, 2012, the court dismissed the information for lack of probable cause and for lack of jurisdiction over the offense charged. The Provincial Prosecutor and the private prosecutor filed a motion for reconsideration of this March 28 Order of the court. On August 13, 2012, the court issued an order denying the said motion for reconsideration.

Other complaints for non-payment of compensation for the clean-up operations during the oil spill were filed by a total of 1,063 plaintiffs who allegedly did not receive any payment of their claims for damages arising from the oil spill. The total claims for both cases amount to ₱292. Both cases are still pending as of December 31, 2012.

• *Generation Payments to PSALM*

SPPC disputed the claims of PSALM for generation payments. The claims arose from differing interpretations of certain provisions in the IPPA Agreement related to generation payments, the fees payable to PSALM for the

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generation of power to customers. SPPC's management is in discussions with PSALM to secure a common understanding through amicable means. However, management and its legal counsel assessed that SPPC's bases for the amounts due to PSALM are consistent with the terms of the Ilijan IPPA Agreement. The outcome of these claims is uncertain; accordingly, the amount cannot be presently determined.

b. Top Frontier

On November 27, 2009, Top Frontier acquired 857,115,914 common shares of the issued and outstanding common shares of the Parent Company for a total of ₱64,284.

To acquire an additional 327,000,000 Class "B" common shares of the Parent Company under the SPA with Q-Tech Alliance Holdings, Inc. (Q-Tech), Top Frontier conducted a tender offer before such acquisition pursuant to the 35% threshold under the mandatory provisions of the Securities Regulation Code.

On April 8, 2010, such tender offer closed and a total of 47,700,679 Class "A" and 31,759,499 Class "B" common shares were tendered for ₱75.00 per share, for a total consideration of ₱5,959. Such tendered shares were crossed in the PSE on April 13, 2010 together with the 327,000,000 common shares acquired from Q-Tech under the SPA.

Following the tender offer, Top Frontier acquired in the open market a total of 1,942,906 common shares for ₱75.00 per share.

The SPA with Q-Tech also provides a grant of call option to Top Frontier for the purchase of 301,666,675 Class "B" common shares of the Parent Company at ₱70.00 per share. The call option may be exercised by Top Frontier until March 31, 2011 or such later date as may be mutually agreed upon by the parties in writing. On March 8, 2011, Top Frontier has notified Q-Tech of its intention to exercise the call option within the period specified in the SPA. On March 16, 2011, Top Frontier exercised its call option with Q-Tech at ₱70.00 per share plus transactions costs for a total of ₱21,133.

Pursuant to an Agreement entered into by Top Frontier on November 20, 2009, Top Frontier acquired an option from the group of 44 companies to acquire 476,722,639 Class "A" and 16,652,544 Class "B" common shares of the Parent Company at ₱75.00 per share for which Top Frontier paid an amount of US\$200 as advances. The call option may be exercised by Top Frontier until November 12, 2012. Any further extension of the term of the option period shall require the written consent and approval of both parties.

The option agreement with the group of 44 companies also provides Top Frontier the rights, with prior written notice to the 44 companies, to assign, transfer and convey its rights to and interest in the option in favor of a third party provided: (i) such assignment, transfer and conveyance made by Top Frontier is consummated during the option period; (ii) the assignee of the option is acceptable to the group of 44 companies; and (iii) the terms and conditions of the agreement shall be valid, binding and enforceable on the assignee.

On June 14, 2012, the BOD of Top Frontier approved the assignment of its rights to exercise the option covering 368,140,516 common shares of the Parent Company in favor of Master Year Limited (MYL), one of the shareholders of Top Frontier.

Also, on June 14, 2012, the BOD of Top Frontier approved the exercise of the option covering the remaining 125,234,667 common shares of the Parent Company. On June 29, 2012, Top Frontier exercised the option on the 125,234,667 common shares of the Parent Company. The sale was transacted at the PSE thru a special block sale at the price of ₱75.00 per share.

As discussed in Note 26, the Parent Company completed the secondary offering of its common shares which includes 110,320,000 shares of stock held by Top Frontier. The Offer Shares were priced at ₱110.00 per share on April 20, 2011.

On December 1, 2011, Top Frontier sold 9,000,000 SMC common shares transacted through the PSE.

As of December 31, 2012 and 2011, Top Frontier had total shareholdings of 1,573,100,340 and 1,447,865,673 common shares of the Parent Company, respectively. Out of the 1,573,100,340 common shares of the Parent Company held by Top Frontier as of December 31, 2012, 225,987,648 shares are lodged in the Philippine Depository and Trust Company.

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c. MYL

On June 29, 2012, MYL purchased a total of 368,140,516 common shares of the Parent Company. The sale was transacted at the PSE thru a special block sale at the price of ₱75.00 per share.

d. Commitments

Amount authorized but not yet disbursed for capital projects as of December 31, 2012 is approximately ₱14,100.

e. Foreign Exchange Rates

The foreign exchange rates used in translating the US dollar accounts of foreign subsidiaries and associates to Philippine peso were closing rates of ₱41.05 and ₱43.84 in 2012 and 2011, respectively, for consolidated statements of financial position accounts; and average rates of ₱42.24, ₱43.31 and ₱45.12 in 2012, 2011 and 2010, respectively, for income and expense accounts.

f. Certain amounts in prior year have been reclassified for consistency with the current period presentation. These reclassifications had no effect on the reported results of operations for any period.

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