

PHILEQUITY PSE INDEX FUND, INC.  
*(An Open-End Mutual Fund Company)*

Financial Statements  
December 31, 2003 and 2002 and  
Years Ended December 31, 2003, 2002 and 2001

and

Report of Independent Auditors

COVER SHEET

A1998-16221

SEC Registration Number

PHILEQUITYPSEINDEXFUND, INC. (An Open-End Mutual Fund Company)

(Company's Full Name)

2103-B, East Tower, Philippine Stock Exchange Centre, Exchange Road, Ortigas Center, Pasig City

(Business Address: No. Street City/Town/Province)

Violeta O. Luym

(Contact Person)

635-3963

(Company Telephone Number)

1231

Month Day (Fiscal Year)

A A F S

(Form Type)

Month Day

(Annual Meeting)

(Secondary License Type, If Applicable)

Dept. Requiring this Doc.

Amended Articles Number/Section

8

Total No. of Stockholders

Total Amount of Borrowings

Domestic

Foreign

To be accomplished by SEC Personnel concerned

File Number

LCU

Document ID

Cashier

STAMPS

Remarks: Please use BLACK ink for scanning purposes.

**Report of Independent Auditors**

The Stockholders and the Board of Directors  
Philequity PSE Index Fund, Inc.  
2103-B, East Tower  
Philippine Stock Exchange Centre  
Exchange Road, Ortigas Center  
Pasig City

We have audited the accompanying statements of assets and liabilities of Philequity PSE Index Fund, Inc. (an open-end mutual fund company) as of December 31, 2003 and 2002, and the related statements of operations, changes in net assets and cash flows for each of the three years in the period ended December 31, 2003. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Philequity PSE Index Fund, Inc. as of December 31, 2003 and 2002, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2003 in conformity with accounting principles generally accepted in the Philippines.

J. J. M. SEBASTIAN  
Partner  
CPA Certificate No. 61687  
SEC Accreditation No. 0097-A  
Tax Identification No. 104-597-500  
PTR No. 7012885  
January 5, 2004  
Makati City

February 4, 2004

## **Report of Independent Auditors**

The Stockholders and the Board of Directors  
Philequity PSE Index Fund, Inc.

We have audited the accompanying statements of assets and liabilities of Philequity PSE Index Fund, Inc. (an open-end mutual fund company) as of December 31, 2003 and 2002, and the related statements of operations, changes in net assets and cash flows for each of the three years in the period ended December 31, 2003. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Philequity PSE Index Fund, Inc. as of December 31, 2003 and 2002, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2003 in conformity with accounting principles generally accepted in the Philippines.

PTR No. 7012885  
January 5, 2004  
Makati City

February 4, 2004

**PHILEQUITY PSE INDEX FUND, INC.****(An Open-End Mutual Fund Company)****STATEMENTS OF ASSETS AND LIABILITIES**

	<b>December 31</b>	
		2002
	2003	(As restated - Note 2)
<b>ASSETS</b>		
<b>Investments in Listed Securities</b> - net of unrealized depreciation of ₱3,232,349 in 2003 and ₱8,250,025 in 2002 (Note 3)	<b>₱19,010,060</b>	<b>₱12,255,879</b>
<b>Cash and Cash Equivalents</b> (Note 4)	<b>1,960,134</b>	<b>3,416,177</b>
<b>Receivables</b>	<b>153,023</b>	<b>81,736</b>
<b>Deferred Tax Assets</b> - net (Notes 2 and 6)	<b>—</b>	<b>—</b>
	<b>21,123,217</b>	<b>15,753,792</b>
<b>LIABILITY</b>		
<b>Accrued Expense</b>	<b>40,000</b>	<b>80,000</b>
<b>NET ASSETS</b> (Note 5)	<b>₱21,083,217</b>	<b>₱15,673,792</b>

*See accompanying Notes to Financial Statements.*

**PHILEQUITY PSE INDEX FUND, INC.**  
**(An Open-End Mutual Fund Company)**

**STATEMENTS OF OPERATIONS**

	<b>Years Ended December 31</b>		
		2002	2001
		(As restated -	(As restated -
	<b>2003</b>	Note 2)	Note 2)
<b>INVESTMENT INCOME</b>			
Dividends	<b>₱311,299</b>	₱314,547	₱197,443
Interest	<b>206,899</b>	193,567	434,943
	<b>518,198</b>	508,114	632,386
<b>EXPENSES</b>			
Taxes and licenses	<b>77,903</b>	57,064	8,702
Professional fees	<b>40,000</b>	46,361	110,329
Net realized loss on sale of investments in listed securities (Note 3)	<b>—</b>	29,785	2,820,932
Others	<b>8,546</b>	11,091	458
	<b>126,449</b>	144,301	2,940,421
<b>NET INVESTMENT INCOME (LOSS)</b> (Notes 5 and 6)	<b>391,749</b>	363,813	(2,308,035)
<b>CHANGES IN UNREALIZED DEPRECIATION OF INVESTMENTS IN LISTED SECURITIES</b> (Note 5)			
Balance at end of year	<b>(3,232,349)</b>	(8,250,025)	(6,164,185)
Balance at beginning of year	<b>(8,250,025)</b>	(6,164,185)	(4,105,911)
<b>UNREALIZED APPRECIATION (DEPRECIATION) OF INVESTMENTS IN LISTED SECURITIES</b> (Note 5)	<b>5,017,676</b>	(2,085,840)	(2,058,274)
<b>NET INCREASE (DECREASE) IN NET ASSETS</b>	<b>₱5,409,425</b>	(₱1,722,027)	(₱4,366,309)

*See accompanying Notes to Financial Statements.*

**PHILEQUITY PSE INDEX FUND, INC.****(An Open-End Mutual Fund Company)****STATEMENTS OF CHANGES IN NET ASSETS**

<b>Years Ended December 31</b>			
		2002	2001
		(As restated -	(As restated -
	2003	Note 2)	Note 2)
<b>FROM INVESTING ACTIVITIES</b>			
Net investment income (loss) (Note 5)	<b>₱391,749</b>	₱363,813	(₱2,308,035)
Net change in unrealized appreciation (depreciation) of investments in listed securities (Note 5)	<b>5,017,676</b>	(2,085,840)	(2,058,274)
<b>NET INCREASE (DECREASE) IN NET ASSETS</b>	<b>5,409,425</b>	(1,722,027)	(4,366,309)
<b>NET ASSETS AT BEGINNING OF YEAR</b>			
Balance at beginning of year, as previously reported	<b>15,954,058</b>	17,796,292	22,282,743
Effect of change in accounting policy for organization costs (Note 2)	<b>(280,266)</b>	(400,473)	(520,615)
Balance at beginning of year, as restated	<b>15,673,792</b>	17,395,819	21,762,128
<b>NET ASSETS AT END OF YEAR (Note 5)</b>	<b>₱21,083,217</b>	₱15,673,792	₱17,395,819

*See accompanying Notes to Financial Statements.*

**PHILEQUITY PSE INDEX FUND, INC.**  
**(An Open-End Mutual Fund Company)**

**STATEMENTS OF CASH FLOWS**

	<b>Years Ended December 31</b>		
	<b>2003</b>	<b>2002</b> (As restated - Note 2)	<b>2001</b> (As restated - Note 2)
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net investment income (loss)	<b>₱391,749</b>	₱363,813	(₱2,308,035)
Adjustments for:			
Dividends	<b>(311,299)</b>	(314,547)	(197,443)
Interest income	<b>(206,899)</b>	(193,567)	(434,943)
Net realized loss on sale of investments in listed securities	—	29,785	2,820,932
Operating loss before working capital changes	<b>(126,449)</b>	(114,516)	(119,489)
Decrease (increase) in:			
Investments in listed securities	<b>(1,736,505)</b>	(2,774,217)	(10,549,957)
Receivables	—	642,135	(642,135)
Increase (decrease) in accrued expense	<b>(40,000)</b>	(65,845)	65,845
Net cash used for operations	<b>(1,902,954)</b>	(2,312,443)	(11,245,736)
Dividends received	<b>226,889</b>	266,553	202,157
Interest received	<b>220,022</b>	204,359	492,932
Proceeds from sale of investments in listed securities	—	371,092	3,502,787
<b>NET DECREASE IN CASH AND CASH EQUIVALENTS</b>	<b>(1,456,043)</b>	(1,470,439)	(7,047,860)
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>	<b>3,416,177</b>	4,886,616	11,934,476
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR (Note 4)</b>	<b>₱1,960,134</b>	₱3,416,177	₱4,886,616

*See accompanying Notes to Financial Statements.*



**PHILEQUITY PSE INDEX FUND, INC.**  
**(An Open-End Mutual Fund Company)**

---

**NOTES TO FINANCIAL STATEMENTS**

---

**1. Corporate Information**

Philequity PSE Index Fund, Inc. (the Fund) is incorporated in the Philippines. It was registered with the Securities and Exchange Commission on February 22, 1999 as an open-end mutual fund company, the purpose of which is, among others, to engage in the sale of its capital stock and investing such proceeds in shares of stock that comprise the Philippine Stock Exchange (PSE) Composite Index.

The Fund did not employ any personnel in 2003 and 2002. The Fund's administrative and accounting functions are undertaken by Philequity Management, Inc. (PMI) without any charge. The registered office address of the Fund is 2103-B East Tower, Philippine Stock Exchange Centre, Exchange Road, Ortigas Center, Pasig City.

The financial statements of the Fund for the year ended December 31, 2003 were authorized for issue by the Board of Directors on February 4, 2004.

---

**2. Summary of Significant Accounting Policies**

Basis of Preparation

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the Philippines under the historical cost convention, except for investments in listed securities which are stated at market value.

Changes in Accounting Policies

On January 1, 2003, the Fund adopted the following Statements of Financial Accounting Standards (SFAS)/International Accounting Standards (IAS):

- SFAS 10/IAS 10, "Events After the Balance Sheet Date," which prescribes the accounting policies and disclosures related to adjusting and non-adjusting subsequent events. Additional disclosures required by the standard were included in the financial statements, principally the date of authorization for the release of the financial statements.
- SFAS 37/IAS 37, "Provisions, Contingent Liabilities and Contingent Assets," which provides the criteria for the recognition and bases for measurement of provisions, contingent liabilities and contingent assets. It also specifies the disclosures that should be included with respect to these items. Adoption of this standard has no effect on the Fund's financial statements.
- SFAS 38/IAS 38, "Intangible Assets," which establishes the criteria for the recognition and measurement of intangible assets. It also requires that expenditures on research, start-up, training, advertising and relocation be expensed as incurred. Accordingly, the Fund changed its method of accounting for organization costs and reversed its unamortized organization costs to conform with the standard. Previously, such expenses were deferred and amortized. The change in accounting policy has been accounted for retroactively and comparative financial statements for 2002 and 2001 have been restated. The change increased net investment income in 2002 by ₱120,207 and in 2001 by ₱120,142. Net assets as of January 1, 2003, 2002 and 2001 has been decreased by ₱280,266, ₱400,473 and ₱520,615, the

unamortized organization costs prior to 2003, 2002 and 2001, respectively, net of applicable deferred income tax.

For income tax purposes, organization costs will be amortized over 5 years.

#### Investments in Listed Securities

Investments in listed securities are stated based on the current market quotations of the PSE. The difference between the aggregate cost of investments in listed securities and the market value at balance sheet date is shown as “Unrealized appreciation (depreciation) of investments in listed securities”. The net difference between the selling price and the cost of listed securities sold, which is computed based on the moving average cost of all the shares of each security held at the time of sale, is shown as “Net realized gain or loss on sale of investments in listed securities” in the statements of operations.

#### Cash and Cash Equivalents

Cash includes cash in bank. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash with original maturities of three months or less and that are subject to an insignificant risk of change in value.

#### Revenue

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Fund and the revenue can be measured reliably. Revenues are recognized on the following bases:

- a. Gain or loss from sale of investments in listed securities, determined at the time of sale of such investments;
- b. Interest, on a time proportion basis taking into account the effective yield on the asset; and,
- c. Dividend, when the Fund’s right to receive the payment is established.

#### Net Asset Value Per Share

Net asset value per share is computed by dividing net assets (total assets less total liabilities) by the number of shares issued and outstanding.

#### Income Tax

Deferred income tax is provided using the liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to: (a) temporary differences between the financial reporting bases of assets and liabilities and their related tax bases; and (b) net operating loss carryover (NOLCO). Deferred tax assets and liabilities are measured using the tax rate applicable to taxable income in the years in which those temporary differences are expected to be recovered or settled and NOLCO is expected to be applied. A valuation allowance is provided for deferred tax assets when it is more likely than not that some or all of the deferred tax assets will not be realized in the future.

#### Subsequent Events

Post year-end events that provide additional information about the Fund’s position at the balance sheet date (adjusting events), are reflected in the financial statements. Post year-end events that are not adjusting events are disclosed in the notes to financial statements when material.

### New Accounting Standard Effective Subsequent to 2003

The Accounting Standards Council has approved SFAS 12/IAS 12, "Income Taxes," which prescribes the accounting treatment for income taxes. It requires the recognition of a deferred tax liability and, subject to certain conditions, asset for all temporary differences with certain exceptions. The standard provides for the recognition of a deferred tax asset when it is probable that taxable income will be available against which the deferred tax asset can be used. It also provides for the recognition of deferred tax liability with respect to asset revaluations. The Fund will adopt the standard in 2004 and, based on current circumstances, believes that the effect of adoption will not be material.

### 3. Investments in Listed Securities

This account consists of investments in the following:

	2003			2002		
	Number of Shares	Cost	Market Value	Number of Shares	Cost	Market Value
Philippine Long Distance Telephone Company	3,140	₱2,833,856	₱3,045,800	3,140	₱2,833,856	₱847,800
Globe Telecom, Inc.	2,875	1,925,930	2,472,500	1,825	1,125,261	816,687
San Miguel Corporation "A"	36,290	1,807,938	1,977,805	36,290	1,807,938	2,177,400
Bank of the Philippine Islands	36,720	1,887,384	1,707,480	36,720	1,887,384	1,230,120
Ayala Corporation	264,600	2,387,184	1,375,920	264,600	2,387,184	1,137,780
San Miguel Corporation "B"	20,770	1,135,892	1,329,280	13,870	703,153	915,420
Ayala Land, Inc.	196,800	1,594,856	1,200,480	196,800	1,594,856	895,440
SM Prime Holdings, Inc.	184,000	1,273,697	1,196,000	175,000	1,212,255	831,250
Metropolitan Bank & Trust Company	30,600	1,445,244	841,500	28,700	1,391,589	904,050
Equitable PCI Bank, Inc.	13,700	411,370	458,950	11,200	320,926	302,400
Petron Corporation	165,000	317,286	372,900	165,000	317,286	257,400
ABS-CBN Holdings Corporation	14,400	468,628	360,000	7,200	266,400	115,200
Jollibee Foods Corporation	17,900	275,040	326,675	17,900	275,040	326,675
Aboitiz Equity Ventures, Inc.	96,000	214,446	292,800	96,000	214,446	216,960
JG Summit Holdings, Inc.	133,200	470,230	279,720	133,200	470,230	186,480
Ginebra San Miguel, Inc.	5,700	178,632	182,400	5,700	178,632	199,500
First Philippine Holdings Corporation	9,480	210,524	177,750	9,480	210,524	76,788
Manila Electric Company "B"	7,120	698,455	172,660	7,120	698,455	62,656
Philippine National Bank	6,700	452,760	162,475	6,700	452,760	157,450
Manila Electric Company "A"	10,600	825,781	159,000	10,600	825,781	86,920
Megaworld Corporation	142,500	131,439	148,200	142,500	131,439	82,650
Filinvest Land, Inc.	138,750	296,310	141,525	138,750	296,310	115,163
Union Cement Corporation	130,000	103,811	140,400	80,000	56,766	36,000
International Container Terminal Services, Inc.	40,000	128,956	132,000	40,000	128,956	96,800
Metro Pacific Corporation	330,000	225,033	92,400	330,000	225,033	52,800
Lepanto Consolidated Mining Company "B"	325,000	96,157	91,000	175,000	47,874	36,750
Digital Telecommunications Philippines, Inc.	110,000	79,148	77,000	110,000	79,148	44,000
Belle Corporation	84,000	157,394	46,200	84,000	157,394	29,400
Ionics, Inc.	9,500	141,349	13,680	9,500	141,349	9,120
Benpres Holdings Corporation	70,000	58,791	33,600	70,000	58,791	7,700
DMCI Holdings, Inc.	8,000	8,888	1,960	8,000	8,888	1,120
		<b>₱22,242,409</b>	<b>₱19,010,060</b>		<b>₱20,505,904</b>	<b>₱12,255,879</b>

As of February 4, 2004, the market value of investments in listed securities held as of December 31, 2003 amounted to ₱18,991,742.

Details of sale of investments in listed securities are as follows:

	2003	2002	2001
Proceeds from sale of investments	₱—	₱371,092	₱3,502,787
Less cost of securities sold	—	400,877	6,323,719
	<b>₱—</b>	<b>₱29,785</b>	<b>₱2,820,932</b>

#### 4. Cash and Cash Equivalents

This account consists of:

	2003	2002
Cash in bank	<b>₱224,778</b>	₱198,934
Short-term deposits	<b>1,735,356</b>	3,217,243
	<b>₱1,960,134</b>	₱3,416,177

Cash in bank earns interest at the prevailing bank deposit rates. Short-term deposits are made for varying periods of between one day and three months depending on the immediate cash requirements of the Fund, and earn interest at the prevailing short-term deposit rates.

#### 5. Net Assets

This account consists of:

	2003	2002 (As restated - Note 2)	2001 (As restated - Note 2)
Capital stock - ₱1 par value			
Authorized - 100,000,000 shares			
Issued - 25,000,000 shares	<b>₱25,000,000</b>	₱25,000,000	₱25,000,000
Retained earnings (deficit):			
Balance at beginning of year, as previously reported	<b>(795,917)</b>	(1,039,523)	1,388,654
Effect of change in accounting policy for organization costs (see Note 2)	<b>(280,266)</b>	(400,473)	(520,615)
Balance at beginning of year, as restated	<b>(1,076,183)</b>	(1,439,996)	868,039
Net investment income (loss), as previously reported	<b>391,749</b>	243,606	(2,428,177)
Effect of change in accounting policy for organization costs (see Note 2)	–	120,207	120,142
Net investment income (loss), as restated	<b>391,749</b>	363,813	(2,308,035)
Balance at end of year	<b>(684,434)</b>	(1,076,183)	(1,439,996)
Unrealized depreciation of investments in listed securities:			
Balance at beginning of year	<b>(8,250,025)</b>	(6,164,185)	(4,105,911)
Net change in unrealized appreciation (depreciation) of investments in listed securities	<b>5,017,676</b>	(2,085,840)	(2,058,274)
Balance at end of year	<b>(3,232,349)</b>	(8,250,025)	(6,164,185)
	<b>₱21,083,217</b>	₱15,673,792	₱17,395,819
Net asset value per share	<b>₱0.843</b>	₱0.627	₱0.696

## 6. Income Tax

The components of net deferred tax assets are as follows:

	2003	2002 (As restated - Note 2)	2001 (As restated - Note 2)
Tax effects of:			
NOLCO	<b>₱230,724</b>	₱177,424	₱102,312
Organization costs (see Note 2)	<b>51,218</b>	89,685	128,152
	<b>281,942</b>	267,109	230,464
Less valuation allowance	<b>281,942</b>	267,109	230,464
	<b>₱-</b>	<b>₱-</b>	<b>₱-</b>

As of December 31, 2003, the NOLCO that can be claimed as deduction from normal taxable income follows:

Year Incurred	Expiry Year	Amount
2001	2004	₱239,631
2002	2005	234,723
2003	2006	246,657
		<b>₱721,011</b>

NOLCO amounting to ₱80,095 was written off in 2003.

The reconciliation of income (loss) before income tax multiplied by the statutory income tax rate to the provision for income tax is as follows:

	2003	2002 (As restated - Note 2)	2001 (As restated - Note 2)
Income tax at statutory tax rate	<b>₱125,360</b>	₱116,420	(₱738,571)
Change in valuation allowance	<b>40,463</b>	36,645	38,237
Tax effect of:			
Dividend income exempt from tax	<b>(99,615)</b>	(100,655)	(63,182)
Interest income subjected to final tax	<b>(66,208)</b>	(61,941)	(139,182)
Net realized loss on sale of investments in listed securities	-	9,531	902,698
	<b>₱-</b>	<b>₱-</b>	<b>₱-</b>