Philequity Peso Bond Fund, Inc.
(An Open-End Mutual Fund Company)

Financial Statements
December 31, 2011 and 2010
and Years Ended December 31, 2011, 2010 and 2009

and

Independent Auditors' Report

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SEC Accreditation No. 0012-FR-2

INDEPENDENT AUDITORS' REPORT

The Stockholders and the Board of Directors
Philequity Peso Bond Fund, Inc.

Report on the Financial Statements

We have audited the accompanying financial statements of Philequity Peso Bond Fund, Inc. (an open-end mutual fund company), which comprise the statements of financial position as at December 31, 2011 and 2010, and the statements of comprehensive income, statements of changes in equity and statements of cash flows for each of the three years in the period ended December 31, 2011, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Philippine Financial Reporting Standards and for such internal controls as management determines is necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these 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 financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Philequity Peso Bond Fund, Inc. as at December 31, 2011 and 2010, and its financial performance and its cash flows for each of the three years in the period ended December 31, 2011 in accordance with Philippine Financial Reporting Standards.

Report on the Supplementary Information Required Under Revenue Regulations 19-2011 and 15-2010

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information required under Revenue Regulations 19-2011 and 15-2010 in Note 17 to the financial statements is presented for purposes of filing with the Bureau of Internal Revenue and is not a required part of the basic financial statements. Such information is the responsibility of the management of Philequity Peso Bond Fund, Inc. The information has been subjected to the auditing procedures applied in our audit of the basic financial statements. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

SYCIP GORRES VELAYO & CO.

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PTR No. 3174802, January 2, 2012, Makati City

April 10, 2012

PHILEQUITY PESO BOND FUND, INC.
(An Open-End Mutual Fund Company)

STATEMENTS OF FINANCIAL POSITION

	December 31	
	2011	2010
ASSETS		
Cash and cash equivalents (Note 6)	**₱19,993,980**	₱144,828,073
Financial assets at fair value through profit or loss (Note 7)	**313,141,362**	317,115,621
Loans and receivables (Note 8)	**5,687,640**	88,541,146
Other assets	**89,523**	–
	₱338,912,505	₱550,484,840
LIABILITIES AND EQUITY		
Liabilities		
Accrued expense and other liabilities (Note 9)	**₱284,330**	₱864,771
Income tax payable	**–**	308,091
	284,330	1,172,862
Equity		
Capital stock (Note 10)	**99,359,684**	94,701,523
Additional paid-in capital	**112,600,833**	91,670,421
Deposits for future stock subscription (Note 10)	**56,294,445**	304,247,976
Retained earnings	**70,373,213**	58,692,058
	338,628,175	549,311,978
	₱338,912,505	₱550,484,840
Net Asset Value Per Share (Note 10)	**₱2.7944**	₱2.5916

See accompanying Notes to Financial Statements.

PHILEQUITY PESO BOND FUND, INC.
(An Open-End Mutual Fund Company)

STATEMENTS OF COMPREHENSIVE INCOME

	Years Ended December 31		
	2011	2010	2009
INVESTMENT INCOME			
Interest income (Notes 6, 7 and 8)	**₱19,913,537**	₱8,696,202	8,357,027
Net unrealized gain on changes in fair value of financial assets at fair value through profit and loss (Note 7)	**10,003,914**	5,521,033	1,022,881
Net realized gain on sale (loss) of financial assets at fair value through profit and loss	**509,279**	65,386	(226,496)
Dividend income	–	–	855,271
Other income	–	–	168,750
	30,426,730	14,282,621	10,177,433
EXPENSES			
Taxes and licenses	**878,022**	919,408	184,271
Professional fees	**421,915**	189,200	189,200
Dues and fees	**20,000**	20,000	20,000
Others (Note 12)	**159,928**	183,947	73,822
	1,479,865	1,312,555	467,293
INVESTMENT INCOME BEFORE INCOME TAX	**28,946,865**	12,970,066	9,710,140
PROVISION FOR INCOME TAX (Note 13)	**3,798,638**	516,230	1,294,159
NET INVESTMENT INCOME	**25,148,227**	12,453,836	8,415,981
OTHER COMPREHENSIVE INCOME	–	–	–
TOTAL COMPREHENSIVE INCOME	**₱25,148,227**	₱12,453,836	8,415,981
EARNINGS PER SHARE (Note 16)	**₱0.2574**	₱0.1956	₱0.1454

See accompanying Notes to Financial Statements.

PHILEQUITY PESO BOND FUND, INC.
(An Open-End Mutual Fund Company)

STATEMENTS OF CHANGES IN EQUITY

	Number of Shares Outstanding (Note 10)	Capital Stock (Note 10)	Additional Paid-in Capital	Retained Earnings	Deposits for Future Stock Subscription	Total Equity
Balance at January 1, 2011	**94,701,523**	**₱94,701,523**	**₱91,670,421**	**₱58,692,058**	**₱304,247,976**	**₱549,311,978**
Shares issued during the year	**250,537,682**	**250,537,682**	**391,533,498**	**–**	**–**	**642,071,180**
Shares redeemed during the year	**(245,879,521)**	**(245,879,521)**	**(370,603,086)**	**(13,467,072)**	**(247,953,531)**	**(877,903,210)**
Total comprehensive income	**–**	**–**	**–**	**25,148,227**	**–**	**25,148,227**
Balance at December 31, 2011	**99,359,684**	**₱99,359,684**	**₱112,600,833**	**₱70,373,213**	**₱56,294,445**	**₱338,628,175**
Balance at January 1, 2010	56,806,942	₱56,806,942	₱31,644,005	₱46,504,974	₱–	₱134,955,921
Shares issued during the year	49,384,085	49,384,085	77,124,784	–	304,247,976	430,756,845
Shares redeemed during the year	(11,489,504)	(11,489,504)	(17,098,368)	(266,752)	–	(28,854,624)
Total comprehensive income	–	–	–	12,453,836	–	12,453,836
Balance at December 31, 2010	94,701,523	₱94,701,523	₱91,670,421	₱58,692,058	₱304,247,976	₱549,311,978
Balance at January 1, 2009	66,735,183	₱66,735,183	₱41,744,534	₱40,357,558	₱–	₱148,837,275
Shares issued during the year	2,519,037	2,519,037	3,308,252	–	–	5,827,289
Shares redeemed during the year	(12,447,278)	(12,447,278)	(13,408,781)	(2,268,565)	–	(28,124,624)
Total comprehensive income	–	–	–	8,415,981	–	8,415,981
Balance at December 31, 2009	56,806,942	₱56,806,942	₱31,644,005	₱46,504,974	₱–	₱134,955,921

See accompanying Notes to Financial Statements.

PHILEQUITY PESO BOND FUND, INC.
(An Open-End Mutual Fund Company)

STATEMENTS OF CASH FLOWS

	Years Ended December 31		
	2011	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES			
Investment income before income tax	**₱28,946,865**	₱12,970,066	₱9,710,140
Adjustments for:			
Net unrealized loss (gain) on changes in fair value of financial assets at fair value through profit or loss (Note 7)	**(10,003,914)**	(5,521,033)	1,022,881
Amortization of premium of unquoted debt securities	**1,653,833**	321,546	61,956
Changes in operating assets and liabilities:			
Decrease (increase) in:			
Financial assets at fair value through profit or loss	**13,978,173**	(240,220,945)	37,997,689
Loans and receivables	**(100,327)**	(3,636,673)	806,579
Other assets	**(89,523)**	–	–
Increase (decrease) in accrued expenses and other liabilities	**(580,441)**	741,537	12,727
Net cash generated from (used for) operations	**33,804,666**	(235,345,502)	49,611,972
Income taxes paid	**(4,106,729)**	(253,501)	(1,248,797)
Net cash provided by (used in) operating activities	**29,697,937**	(235,599,003)	48,363,175
CASH FLOW FROM INVESTING ACTIVITIES			
Proceeds from maturity of unquoted debt securities	**77,000,000**	–	–
Proceeds from sale of unquoted debt securities	**4,300,000**	9,711,592	–
Acquisitions of unquoted debt securities	**–**	(58,869,493)	–
Net cash provided by (used in) investing activities	**81,300,000**	(49,157,901)	–
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from subscriptions of shares	**642,071,180**	430,756,845	5,827,289
Payments for redemptions of shares	**(877,903,210)**	(28,854,624)	(28,124,624)
Net cash provided by (used in) financing activities	**(235,832,030)**	401,902,221	(22,297,335)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	**(124,834,093)**	117,145,317	26,065,840
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	**144,828,073**	27,682,756	1,616,916
CASH AND CASH EQUIVALENTS AT END OF YEAR (Note 6)	**₱19,993,980**	₱144,828,073	₱27,682,756
OPERATIONAL CASH FLOWS FROM INTEREST			
Interest received	**₱21,416,515**	₱5,436,742	₱8,359,288

See accompanying Notes to Financial Statements.

NOTES TO FINANCIAL STATEMENTS

1. Corporate Information

Philequity Peso Bond Fund, Inc. (the Fund) is incorporated in the Philippines and is registered with the Securities and Exchange Commission (SEC) on February 24, 1999 as an open-end mutual fund. The Fund is engaged in, among others, selling its capital stock and investing the related proceeds in high-yield debt instruments.

On June 29, 2007, the board of directors (BOD) approved the change of the corporate name of the Fund from Philequity Money Market Fund, Inc. to Philequity Peso Bond Fund, Inc. Subsequently, on August 24, 2007, the SEC approved the change of the corporate name of the Fund.

The registered address of the Fund is 2004-A East Tower, Philippine Stock Exchange Centre, Exchange Road, Ortigas Center, Pasig City.

Philequity Management, Inc. (PEMI) serves as the fund manager of the Fund.

The financial statements of the Fund were approved and authorized for issue by the BOD on April 10, 2012.

2. Summary of Significant Accounting Policies

<u>Basis of Preparation</u>
The accompanying financial statements of the Fund have been prepared on a historical cost basis, except for financial assets at fair value through profit or loss (FVPL) that have been measured at fair value. The financial statements are presented in Philippine Peso, the Fund's functional currency, and all values are rounded to the nearest peso except when otherwise indicated.

<u>Presentation of Financial Statements</u>
The Fund presents its statement of financial position in order of liquidity. An analysis regarding recovery (asset) or settlement (liability) within 12 months from the reporting date (current) and beyond 12 months from the reporting date (noncurrent) is presented in Note 11.

<u>Statement of Compliance</u>
The financial statements of the Fund have been prepared in compliance with Philippine Financial Reporting Standards (PFRS).

<u>Changes in Accounting Policies and Disclosures</u>
The accounting policies adopted are consistent with those of the previous financial year except for the following new and amended Philippine Accounting Standards (PAS), PFRS and Philippine Interpretations which were adopted as of January 1, 2011. The following new and amended standards did not have any impact on the accounting policies, financial position or performance of the Fund:

New and amended standards and interpretations
PAS 24, *Related Party Transactions* (Amendment)
The amendment clarifies the definitions of a related party. The new definitions emphasize a symmetrical view of related party relationships and clarify the circumstances in which persons and key management personnel affect related party relationships of an entity. In addition, the amendment introduces an exemption from the general related party disclosure requirements for transactions with government and entities that are controlled, jointly controlled or significantly influenced by the same government as the reporting entity.

PAS 32, *Financial Instruments: Presentation* (Amendment)
The amendment alters the definition of a financial liability in PAS 32 to enable entities to classify rights issues and certain options or warrants as equity instruments. The amendment is applicable if the rights are given pro rata to all of the existing owners of the same class of an entity's non-derivative equity instruments, to acquire a fixed number of the entity's own equity instruments for a fixed amount in any currency.

Improvements to PFRSs 2010
The amendments to PFRS were issued primarily with a view to remove inconsistencies and clarify wordings. There are separate transitional provisions for each standard. The adoption of the amendments resulted in changes in accounting policies but did not have any impact on the financial position or performance of the Fund.

- PFRS 3, *Business Combination*
- PFRS 7, *Financial Instruments: Disclosures*
- PAS 1, *Presentation of Financial Statements*
- PAS 27, *Consolidated and Separate Financial Statements*
- PAS 34, *Interim Financial Statements*
- Philippine Interpretation IFRIC13, *Customer Loyalty Programmes*
- Philippine Interpretation IFRIC 19, *Extinguishing Financial Liabilities with Equity Instruments*

Summary of Significant Accounting Policies

<u>Cash and Cash Equivalents</u>
This includes cash in banks and cash equivalents. Cash equivalents represent short-term, highly liquid investments that are readily convertible to known amounts of cash with original maturities of three months or less from dates of placements and which are subject to an insignificant risk of changes in value.

<u>Financial Instruments - Initial Recognition and Subsequent Measurement</u>
Date of recognition
Financial instruments within the scope of PAS 39, *Financial Instruments: Recognition and Measurement*, are recognized in the statement of financial position when the Fund becomes a party to the contractual provisions of the instrument. Purchases or sales of financial assets that require delivery of assets and liabilities within the time frame established by regulation or convention in the marketplace are recognized on the settlement date.

Initial recognition of financial instruments
Financial instruments are initially recognized at fair value of the consideration given. The initial measurement of financial instruments includes transaction costs, except for financial instruments at FVPL. The Fund classifies its financial assets in the following categories: financial assets at FVPL, available-for-sale (AFS) investments, held-to-maturity (HTM) investments and loans and receivables. Financial liabilities are classified either as financial liabilities at FVPL or other financial liabilities carried at amortized cost or cost.

The classification depends on the purpose for which the investments were acquired and whether they are quoted in an active market. Management determines the classification of its investments at initial recognition and, where allowed and appropriate, re-evaluates such designation at every reporting date.

As of December 31, 2011 and 2010, the Fund has financial assets at FVPL and loans and receivables.

Determination of fair value
At date of initial recognition and at every reporting date, the fair value of financial instruments that are traded in active markets 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 has not been a significant change in economic circumstances since the time of the transaction.

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

'Day 1' profit or loss
Where the transaction price in a non-active market is different from 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 an observable market, the Fund recognizes the difference between the transaction price and fair value (a 'Day 1' profit or loss) in the profit or loss in the statement of comprehensive income unless it qualifies for recognition as some other type of asset. In cases where fair value is determined using data which is not observable, the difference between the transaction price and model value is only recognized in the profit or loss in the statement of comprehensive income when the inputs become observable or when the instrument is derecognized. For each transaction, the Fund determines the appropriate method of recognizing the 'Day 1' profit or loss amount.

Financial assets and financial liabilities at FVPL
Financial instruments at FVPL include financial assets and financial liabilities that are:
- acquired and held for trading purposes;
- designated upon initial recognition as at FVPL; and
- stand-alone or bifurcated embedded derivative financial instruments not designated as effective hedging instruments.

Financial assets and financial liabilities are classified as held for trading if they are acquired for purposes of selling and repurchasing in the near term.

Financial assets and financial liabilities may be designated by management on initial recognition at FVPL when the following criteria are met:

- The designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or liabilities or recognizing gains or losses on them on a different basis;
- The assets and liabilities are part of a group of financial assets, liabilities or both which are managed and their performance 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 recorded.

Financial assets and financial liabilities at FVPL are recorded in the statement of financial position at fair value. Changes in fair value are recognized in the profit or loss in the statement of comprehensive income. Interest earned or incurred is recorded in interest income or expense, respectively.

As of December 31, 2011 and 2010, the Fund's financial assets at FVPL comprise of government securities and corporate bonds.

Derivatives recorded at FVPL
Derivative financial instruments are initially recognized at fair value on the date in which a derivative transaction is entered into or bifurcated, and are subsequently re-measured at fair value. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

An embedded derivative is a component of a hybrid (combined) instrument that also includes a non-derivative host contract, with the effect that some of the cash flows of the combined instrument vary in a way similar to a stand-alone derivative. An embedded derivative is separated from the host contract and accounted for as derivative if all the following conditions are met:

- the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristic of the host contract;
- a separate instrument with the same terms as the embedded derivative would meet the definition of the derivative; and
- the hybrid or combined instrument is not measured at fair value with fair value changes charged through profit or loss.

The Fund assesses whether embedded derivatives are required to be separated from host contracts when the Fund first becomes party to the contract. Reassessment only occurs if there is a change in the terms of the contracts that significantly modifies the cash flows.

As of December 31, 2011 and 2010, the Fund does not have any outstanding derivatives at FVPL nor any stand-alone or bifurcated embedded derivatives.

AFS investments
AFS investments are non-derivative financial assets which are designated as such or do not qualify to be classified as financial assets at FVPL, HTM investments or loans and receivables. They are purchased and held indefinitely, and may be sold in response to liquidity requirements or changes in market conditions.

After initial measurement, AFS investments are subsequently measured at fair value. AFS investments are measured at fair value with gains and losses being recognized as other comprehensive income until the investment is derecognized or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in other comprehensive income is included under investment income in the profit or loss in the statement of comprehensive income.

The Fund evaluates its AFS investments whether the ability and intention to sell them in the near term is still appropriate. When the Fund is unable to trade these financial assets due to inactive markets and management's intent significantly changes to do so in the foreseeable future, the Fund may elect to reclassify these financial assets in rare circumstances. Reclassification to loans and receivables is permitted when the financial asset meets the definition of loans and receivables and has the intent and ability to hold these assets for the foreseeable future or maturity.

The Fund has no outstanding AFS investments as of December 31, 2011 and 2010.

HTM investments
HTM investments are quoted non-derivative financial assets with fixed or determinable payments and fixed maturities for which the Fund's management has the intention and ability to hold to maturity. After initial measurement, these investments are subsequently measured at amortized cost using the effective interest rate (EIR) method, less impairment in value. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the EIR. Gains and losses are recognized in the profit or loss in the statement of comprehensive income when the HTM investments are derecognized and impaired, as well as through the amortization process.

If the Fund were to sell more than an insignificant amount of HTM investments before maturity (other than in specific circumstances), the entire category would be tainted and reclassified as AFS investment. Furthermore, the Fund would be prohibited to classify any financial assets as HTM investments for the following two years.

As of December 31, 2011 and 2010, the Fund has no outstanding HTM investments.

Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments and fixed 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 classified as financial assets held-for-trading designated at FVPL or classified as AFS securities.

After initial measurement, the loans and receivables are subsequently measured at amortized cost using the EIR method, less allowance for impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the EIR. The amortization is included under 'Interest income' in the profit or loss in the statement of comprehensive income. The losses arising from impairment of such loans and receivables are also recognized as 'Provision for (reversal of) impairment and credit losses' in the profit or loss in the statement of comprehensive income.

As of December 31, 2011 and 2010, the Fund has outstanding loans and receivables.

Other financial liabilities
Issued financial instruments or their components, which are neither held for trading nor designated at FVPL, are classified as other financial liabilities, where the substance of the contractual arrangement results in the Fund having an obligation either to deliver cash or another financial asset to the holder, or to 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. The components of issued financial instruments that contain both liability and equity elements are accounted for separately, with the equity component being assigned the residual amount after deducting from the instrument as a whole the amount separately determined as the fair value of the liability component on the date of issue.

After initial measurement, other financial liabilities are subsequently measured at amortized cost using the EIR method. Amortized cost is calculated by taking into account any discount or premium on the issue and fees that are an integral part of the EIR.

Other financial liabilities include liabilities arising from operations or borrowings which consist of accrued expenses and other liabilities.

<u>Derecognition of Financial Assets and Liabilities</u>
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 where:

- the rights to receive cash flows from the asset have expired;
- the Fund 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 Fund has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of ownership and retained control over the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control over the asset.

Where the Fund has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognized to the extent of the Fund'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 original carrying amount of the asset and the maximum amount of consideration that the Fund could be required to repay.

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

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

Financial assets carried at amortized cost
If there is objective evidence that an impairment loss on financial assets carried at amortized cost (i.e. receivables) has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original EIR. Time value is generally not considered when the effect of discounting is not material. The carrying amount of the asset is reduced through the use of an allowance account. The amount of the loss shall be recognized in profit or loss in the statement of comprehensive income. The asset, together with the associated allowance accounts, is written-off when there is no realistic prospect of future recovery.

The Fund first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed 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 assessment of impairment.

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 in the statement of comprehensive income to the extent that the carrying value of the asset does not exceed its amortized cost at the reversal date.

Offsetting Financial Instruments
Financial assets and liabilities are offset and the net amount reported in the statement 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.

Capital Stock and Redeemable Shares
A puttable financial instrument is classified as an equity instrument if it has all of the following features:

- It entitles the holder to a pro-rata share of the Fund's net assets in the event of the Fund's liquidation;
- The instrument is in the class of instruments that is subordinate to all other classes of instruments;
- All financial instruments in the class of instruments that is subordinate to all other classes of instruments have identical features;
- The instrument does not include any contractual obligation to deliver cash or another financial asset other than the holder's right to a pro-rata share of the Fund's net assets; and
- The total expected cash flows attributable to the instrument over the life of the instrument are based substantially on the profit or loss, the change in the recognized net assets or the change in the fair value of the recognized and unrecognized net assets of the Fund over the life of the instrument.

In addition to the instrument having all the above features, the Fund must have no other financial instrument or contract that has:

- Total cash flows based substantially on the profit or loss, the change in the recognized net assets or the change in the fair value of the recognized and unrecognized net assets of the Fund; and
- The effect of substantially restricting or fixing the residual return to the puttable instrument holders.

The Fund continuously assesses the classification of the redeemable shares. If the redeemable shares cease to have all the features or meet all the conditions set out above, the Fund will reclassify them as financial liabilities and measure them at fair value at the date of reclassification, with any differences from the previous carrying amount recognized in equity. If the redeemable shares subsequently have all the features and meet the conditions set out above, the Fund will reclassify them as equity instruments and measure them at the carrying amount of the liabilities at the date of the reclassification.

The issuance, acquisition and resale of redeemable shares are accounted for as equity transactions. Upon sale of shares, the consideration received is included in equity. Redemptions are recorded as charges against equity.

Deposits for Future Stock Subscription
Deposits for future stock subscription are recorded based on the subscription amount received. These are subscriptions received from prospective investors for the Fund's shares, which are yet to be issued, pending approval by the SEC. This will be reclassified to 'Capital stock' and 'Additional paid-in capital' upon approval by the SEC for the Fund to issue additional redeemable shares.

The Fund presents this as equity since it issues a fixed number of shares for a fixed amount.

Share Issuance Costs
Share issuance costs such as sales load fee are deducted against 'Additional paid-in capital'. If 'Additional paid-in capital' is not sufficient to absorb the share issuance costs, any excess is charged against 'Retained earnings'.

Retained Earnings
The amounts in retained earnings include accumulated investment income from previous periods reduced by excess of redemption costs over the original issuance price of redeemed shares.

Net Asset Value (NAV) Per Share
NAV per share is computed by dividing net assets (total assets less total liabilities) by the total number of redeemable shares outstanding as of reporting date.

Revenue Recognition
Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Fund and the revenue can be reliably measured, regardless of when payment is being made. Revenue is measured at the fair value of the consideration received or receivable, taking into account contractually defined terms of payment. The Fund assesses its revenue arrangements against specific criteria in order to determine if it is acting as principal or agent. The following specific recognition criteria must also be met before revenue is recognized:

Interest income
Interest is recognized as the interest accrues taking into account the effective yield on the asset.

Net realized gain or loss on sale of financial assets at FVPL
Net realized gain or loss on sale of financial assets at FVPL is determined at the time of the sale transaction calculated as the difference between the net sales proceeds and the acquisition cost of the debt security.

Net unrealized gain or loss on changes in fair value of financial assets at FVPL
Net unrealized gain or loss on changes in fair value of financial assets at FVPL is determined as the change due to revaluation of investments as of reporting date.

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

Expense Recognition
Expenses are recognized when a decrease in future economic benefits related to a decrease in an asset or an increase of a liability has arisen that can be measured reliably. Expenses are recognized when incurred.

Provisions
Provisions are recognized when the Fund has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. Where the Fund expects some or all of a provision to be reimbursed, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain that the expense relating to any provision is presented in the profit or loss in the statement of comprehensive income, net of any reimbursement.

If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and where appropriate, the risks specific to the liability. Increase in provision due to time value of money is recorded as interest expense.

Contingent Liabilities and Contingent Assets
Contingent liabilities are not recognized in the statement of financial position but are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote. Contingent assets are not recognized in the statement of financial position but are disclosed when an inflow of economic benefits is probable.

Earnings per Share
Earnings per share is calculated by dividing net investment income after tax for the year by the weighted average number of outstanding shares of stock during the year.

Related Party Transactions
Parties are considered to be related if one party has the ability to, directly or indirectly, control the other party or exercise significant influence over the other party in making financial and operating decisions. These include: (a) individuals owning, directly or indirectly through one or more intermediaries, control, or are controlled by, or under common control with, the Fund; (b) associates; and, (c) individuals owning, directly or indirectly, an interest in the voting power of the Fund that gives them significant influence over the Fund and close members of the family of any such individual. Transactions are based on terms agreed by related parties.

Income Taxes
Current income tax
Current income tax liabilities for the current and prior periods are measured at the amounts expected to be paid to the tax authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted at the reporting date.

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

Deferred tax liabilities are recognized for all taxable temporary differences. Deferred tax assets are recognized for all deductible temporary differences and carryforward benefits of unused tax credits from the excess of minimum corporate income tax (MCIT) over regular corporate income tax (RCIT), and unused net operating loss carryover (NOLCO), to the extent that it is probable that sufficient taxable income will be available against which the deductible temporary differences and carryforward of unused tax credits from excess MCIT and unused NOLCO can be utilized. Deferred tax assets, however, are not recognized on temporary differences that arise 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 income nor taxable income.

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 income 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 income will allow the deferred tax assets to be recovered.

Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period 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.

Deferred tax relating to items recognized outside profit or loss is recognized outside profit or loss. Deferred tax items are recognized in correlation to the underlying transaction either in profit or loss or other comprehensive income.

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

Events After the Reporting Date
Post-year-end events that provide additional information about the Fund's assets and liabilities at reporting date (adjusting events) are reflected in the financial statements. Events after the reporting date that are not adjusting events are disclosed in the notes to financial statements, when material.

Standards Issued but not yet Effective
Standards issued but not yet effective up to date of issuance of the Fund's financial statements are listed below. This listing of standards and interpretations issued, which the Fund reasonably expects to be applicable at a future date. The Fund intends to adopt those standards when they become effective.

Effective in 2012

- PFRS 7, *Financial Instruments: Disclosures - Enhanced Derecognition Disclosure Requirements*
  The amendment becomes effective for annual periods beginning on or after July 1, 2011. The amendment requires additional disclosure about financial assets that have been transferred but not derecognized to enable the user of the Fund's financial statements to understand the relationship with those assets that have not been derecognized and their associated liabilities. In addition, the amendment requires disclosures about continuing involvement in derecognized assets to enable the user to evaluate the nature of, and risks associated with, the entity's continuing involvement in those derecognized assets. The amendment affects disclosure only and has no impact on the Fund's financial position or performance.

- PAS 12, *Income Taxes* (Amendment) - *Deferred Tax: Recovery of Underlying Assets*
  The amendment becomes effective for annual periods beginning on or after January 1, 2012. The amendment clarified the determination of deferred tax on investment property measured at fair value. The amendment introduces a rebuttable presumption that deferred tax on investment property measured using the fair value model in PAS 40 should be determined on the basis that its carrying amount will be recovered through sale. Furthermore, it introduces the requirement that deferred tax on non-depreciable assets that are measured using the revaluation model in PAS 16, *Property, Plant and Equipment*, always be measured on a sale basis of the asset. The Fund has no investment property which would be affected by these amendments.

Effective in 2013

- PAS 1, *Financial Statement Presentation - Presentation of Items of Other Comprehensive Income*
  The amendment becomes effective for annual periods beginning on or after July 1, 2012. The amendments to the standard change the grouping of items presented in other comprehensive income. Items that could be reclassified (or 'recycled') to profit or loss at a future point in time (for example, upon derecognition or settlement) would be presented separately from items that will never be reclassified. The amendment affects presentation only and there is no impact on the Fund's financial position or performance.

- PAS 19, Employee Benefits (Amendment)
  The amendment becomes effective for annual periods beginning on or after January 1, 2013. Amendments range from fundamental changes such as removing the corridor mechanism and the concept of expected returns on plan assets to simple clarifications and re-wording. The Fund has no employee benefits which would be affected by these amendments.

- PAS 27, *Separate Financial Statements* (as revised in 2011)
  The amendment becomes effective for annual periods beginning on or after January 1, 2013. As a consequence of the new PFRS 10, *Consolidated Financial Statements* and PFRS 12, *Disclosure of Interests in Other Entities*, what remains in the standard is limited to accounting for subsidiaries, jointly controlled entities, and associates in separate financial statements. As the Fund has no subsidiaries, this amendment has no impact on its financial position or performance.

- PAS 28, *Investments in Associates and Joint Ventures* (as revised in 2011)
  The amendment becomes effective for annual periods beginning on or after January 1, 2013. As a consequence of the new PFRS 11, *Joint Arrangements*, and PFRS 12, the standard has been renamed PAS 28, *Investments in Associates and Joint Ventures*, and describes the application of the equity method to investments in joint ventures in addition to associates. As the Fund has no associates or joint venture investments, this amendment has no impact on its financial position or performance.

- PFRS 7, *Financial instruments: Disclosures - Offsetting Financial Assets and Financial Liabilities*
  The amendments to PFRS 7 are to be retrospectively applied for annual periods beginning on or after January 1, 2013. These amendments require an entity to disclose information about rights of set-off and related arrangements (such as collateral agreements). The new disclosures are required for all recognized financial instruments that are set off in accordance with PAS 32. These disclosures also apply to recognized financial instruments that are subject to an enforceable master netting arrangement or 'similar agreement', irrespective of whether they are set-off in accordance with PAS 32. The amendments require entities to disclose, in a tabular format unless another format is more appropriate, the following minimum quantitative information. This is presented separately for financial assets and financial liabilities recognized at the end of the reporting period:
  a) The gross amounts of those recognized financial assets and recognized financial liabilities;
  b) The amounts that are set off in accordance with the criteria in PAS 32 when determining the net amounts presented in the statement of financial position;
  c) The net amounts presented in the statement of financial position;

d) The amounts subject to an enforceable master netting arrangement or similar agreement that are not otherwise included in (b) above, including:
   i. Amounts related to recognized financial instruments that do not meet some or all of the offsetting criteria in PAS 32; and
   ii. Amounts related to financial collateral (including cash collateral); and
e) The net amount after deducting the amounts in (d) from the amounts in (c) above.

The amendment affects disclosures only and has no impact on the Fund's financial position and performance.

- PFRS 10, *Consolidated Financial Statements*
  This standard becomes effective for annual periods beginning on or after January 1, 2013. It replaces the portion of PAS 27, *Consolidated and Separate Financial Statements* that addresses the accounting for consolidated financial statements. It also includes the issues raised in Standing Interpretations Committee (SIC) - 12, *Consolidation - Special Purpose Entities*. It establishes a single control model that applies to all entities including special purpose entities. The changes introduced by the standard will require management to exercise significant judgment to determine which entities are controlled, and therefore required to be consolidated by a parent, compared with the requirements that were in PAS 27. This amendment has no impact on the Fund's financial position or performance.

- PFRS 11, *Joint Arrangements*
  This standard becomes effective for annual periods beginning on or after January 1, 2013. It replaces PAS 31, *Interests in Joint Ventures* and SIC-13, *Jointly-controlled Entities - Non-monetary Contributions by Venturers*. It removes the option to account for jointly controlled entities (JCEs) using proportionate consolidation. Instead, JCEs that meet the definition of a joint venture must be accounted for using the equity method. The application of this new standard will not impact the financial position or performance of the Fund.

- PFRS 12, *Disclosure of Involvement with Other Entities*
  This standard becomes effective for annual periods beginning on or after January 1, 2013. It includes all of the disclosures that were previously in PAS 27 related to consolidated financial statements, as well as all of the disclosures that were previously included in PAS 31 and PAS 28. These disclosures relate to an entity's interests in subsidiaries, joint arrangements, associates and structured entities. A number of new disclosures are also required.

- PFRS 13, *Fair Value measurement*
  This standard becomes effective for annual periods beginning on or after January 1, 2013. It establishes a single source of guidance under PFRS for all fair value measurements. It does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under PFRS when fair value is required or permitted. The Fund is currently assessing the impact that on its financial position and performance.

Effective 2014

- PAS 32, *Financial Instruments: Presentation* - *Offsetting Financial Assets and Financial liabilities*
  The amendments to PAS 32 are to be retrospectively applied for annual periods beginning on or after January 1, 2014. These amendments to PAS 32 clarify the meaning of "currently has a legally enforceable right to set-off" and also clarify the application of the PAS 32 offsetting criteria to settlement systems (such as central clearing house systems) which apply gross settlement mechanisms that are not simultaneous. While the amendment is expected not to have any impact on the net assets of the Fund, any changes in offsetting is expected to impact leverage ratios and regulatory capital requirements. The Fund is currently assessing the impact of the amendments to PAS 32.

Effective 2015

- PFRS 9, *Financial Instruments: Classification and Measurement*
  The standard is effective for annual periods beginning on or after January 1, 2015. The standard as issued reflects the first phase on the replacement of PAS 39 and applies to classification and measurement of financial assets and financial liabilities as defined in PAS 39. The subsequent phases will address hedge accounting and impairment of financial assets. The completion of this project is expected during the first half of 2012. The adoption of the first phase of PFRS 9 will have an effect on the classification and measurement of the Fund's financial assets but will potentially have no impact on classification and measurements of financial liabilities. The Fund will quantify the effect in conjunction with the other phases, when issued, to present a comprehensive picture.

- Philippine Interpretation IFRIC-15, *Agreement for the Construction of Real Estate*
  This Interpretation covers accounting for revenue and associated expenses by entities that undertake the construction of real estate directly or through subcontractors. The Interpretation requires that revenue on construction of real estate be recognized only upon completion, except when such contract qualifies as construction contract to be accounted for under PAS 11, *Construction Contracts*, or involves rendering of services in which case revenue is recognized based on stage of completion. Contracts involving provision of services with the construction materials and where the risks and rewards of ownership are transferred to the buyer on a continuous basis will also be accounted for based on stage of completion. The SEC and the Financial Reporting Standards Council (FRSC) have deferred the effectivity of this interpretation until the final Revenue standard is issued by the International Accounting Standards Board (IASB) and an evaluation of the requirements of the final Revenue standard against the practices of the Philippine real estate industry is completed. The application of this interpretation will not impact the financial position or performance of the Fund.

3. **Significant Accounting Judgments and Estimates**

The preparation of the financial statements in accordance with PFRS requires the Fund to make estimates and assumptions that affect the reported amounts of assets, liabilities, income and expenses and disclosure of contingent assets and contingent liabilities, if any. Future events may occur which may cause the assumptions used in arriving at the estimates to change. The effects of any change in estimates are reflected in the financial statements as they become reasonably determinable.

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.

Judgments

a. *Going concern*
The management of the Fund has made an assessment of its ability to continue as a going concern and is satisfied that it has the resources to continue in business for the foreseeable future. The Fund is not aware of any material uncertainties that may cast significant doubts upon the Fund's ability to continue as a going concern. Therefore, the financial statements continue to be prepared on a going concern basis.

b. *Classification of financial instruments*
The Fund exercises judgment in classifying a financial instrument, or its component, on initial recognition either as a financial asset, a financial liability or an equity instrument in accordance with the substance of the contractual arrangement and the definitions of a financial asset, financial liability or equity instrument. The substance of a financial instrument, rather than its legal form, governs its classification in the statement of financial position.

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

c. *Fair values of financial instruments*
Where the fair values of financial assets and liabilities recorded in the statement of financial position cannot be derived from active markets, they are determined using various valuation techniques. The inputs to these models are taken from observable market data where possible, but where deriving from observable market is not feasible, a degree of judgment is required in determining fair values. The judgments include considerations of liquidity risk, credit risk and volatility. Changes in assumptions about these factors could affect the reported fair value of financial instruments.

d. *Impairment of financial assets*
In determining whether an impairment loss should be recorded in profit or loss, the Fund assesses as to whether there is any objective evidence of impairment as a result of one or more events that has occurred after initial recognition of the asset and that loss event or events has an impact on the estimated future cash flows of the financial assets or the group of financial assets that can be reliably estimated. This observable data may include adverse changes in payment status of borrowings in a group, or national or local economic conditions that correlate with defaults of assets in the portfolio.

Estimates

The key assumptions concerning the future and other key sources of estimation and uncertainty as of reporting date that have the most significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year is as follows:

Recognition of deferred tax assets
The Fund assesses the carrying amounts of deferred tax assets at the reporting date and reduces deferred tax assets 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. Significant management judgment is required to determine the amount of deferred tax assets that can be recognized, based upon the likely timing and level of future taxable income together with future tax planning strategies.

4. Financial Risk Management Objectives and Policies

The Fund's principal financial instruments comprised of cash and cash equivalents, financial assets at FVPL and loans and receivables. The main purpose of these financial instruments is to seek long-term capital appreciation through investments in peso-denominated government securities, commercial paper, corporate bonds, promissory notes and other debt instruments of varying tenors. The Fund has various other financial assets and liabilities such as loans and receivable and accrued expenses and other liabilities, which arise directly from its operations.

Governance Framework
The Fund has established a risk management function under Treasury department with clear terms of reference and with the responsibility for developing policies on market, credit, liquidity and operational risk. It also supports the effective implementation of policies.

The policies define the Fund's identification of risk and its interpretation, setting of limits structure to ensure the appropriate quality and diversification of assets, and specification of reporting requirements.

Regulatory Framework
The operations of the Fund are subject to the regulatory requirements of the SEC and are governed by the provision in its prospectus that incorporated relevant investment rules and regulation by regulators such as Investment Company Act (ICA) and Anti-Money Laundering Law.

The Fund's investment activities are guided by the following limitations/restrictions indicated in its prospectus:
- Unless the applicable Philippine laws, rules, regulations, and orders of the SEC provide otherwise, the Fund shall not sell securities short nor invest in any of the following: margin purchase of securities, commodity futures contract, precious metals and unlimited liability investments.
- The Fund shall not incur any further debt or borrowings unless at the time of its incurrence or immediately thereafter, there is a net asset coverage of at least 300.00% for all its borrowings, or such net asset coverage as the Philippine laws and regulations may prescribe. In the event that such asset coverage shall fall below 300.00%, the Fund shall within three days thereafter or such period as the applicable Philippine laws and regulations may require, reduce the amount of borrowings to an extent that the net asset coverage shall be at least 300.00% or the coverage required by law.
- Unless permitted by applicable Philippine laws, rules or regulations, the Fund shall not participate in an underwriting or selling group in connection with the public distribution of securities, except its own capital stock.
- The Fund shall not invest in real estate properties and developments.

- The Fund shall not invest in any company for the purposes of exercising control or management.
- The Fund shall not issue or sell senior securities of which it is the issuer.
- The Fund shall not extend loans to individuals. Loans or credit extensions to corporations shall be limited to commercial papers and bonds registered with the SEC, or subject of a grant of exemption therefrom, and which have been preapproved by the BOD.
- The Fund shall not invest in the securities of other investment companies.
- The Fund shall not purchase from or sell to any of its officers or directors, or to any of the officers or directors of its investment adviser/s, manager or distributor/s or firm/s of which any of them are members, any security other than the capital stock of the Fund.
- The total operational expenses of the Fund shall not exceed 10.00% of its total investment fund, total net worth or total NAV as shown in the previous year's audited financial statements, or such other limitations as may be prescribed by the applicable Philippine laws or regulations.

Risk Management Policies
The Fund is exposed to financial risk through its financial assets and liabilities. The most significant components of financial risk are credit risk, liquidity risk and market risk. The BOD reviews and approves policies for managing the aforementioned risks and are summarized below:

Credit Risk
Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss.

Maximum exposure to credit risk
The Fund's maximum exposure to credit risk is limited to the carrying value of its financial assets as of reporting date. The Fund does not hold any collateral or other credit enhancements that will mitigate credit risk exposure.

An analysis of the maximum exposure to credit risk is shown below:

	2011	2010
Financial assets at FVPL (Note 7):		
Government securities	**₱257,562,480**	₱263,105,937
Corporate bonds	**55,578,882**	54,009,684
Loans and receivables:		
Cash and cash equivalents (Note 6)	**19,993,980**	144,828,073
Receivables (Note 8):		
Accrued interest receivable	**5,682,501**	5,531,646
Due from related parties	**139**	50,667
Other receivables	**5,000**	5,000
Unquoted debt securities	**–**	82,953,833
	₱338,822,982	₱550,484,840

Credit quality per class of financial assets
As of December 31, 2011 and 2010, these financial assets are viewed by management as high grade and there are no past due or impaired financial assets as of December 31, 2011 and 2010.

The Fund's basis in grading its financial assets follows:

High grade cash and cash equivalents are short-term placements and working cash fund placed, invested, or deposited in local banks belonging to the top twenty banks in terms of resources and profitability.

High grade accounts are accounts considered to be of high value. The counterparties have a remote likelihood of default and have consistently exhibited good paying habits.

Standard grade accounts are active accounts with propensity of deteriorating to mid-range age buckets. These accounts are typically not impaired as the counterparties generally respond to credit actions and update their payments accordingly.

Substandard grade accounts are accounts which have probability of impairment based on historical trend. These accounts show propensity to default in payment despite regular follow-up actions and extended payment terms.

Liquidity risk
Liquidity or funding risk is the risk that an entity will encounter difficulty in raising funds to meet commitments associated with financial instruments. Liquidity risk may result from either the inability to sell financial assets quickly at their fair values; counterparties failing to repay a contractual obligation; or the inability to generate cash inflows as anticipated.

The Fund is exposed to daily cash redemptions of redeemable participating shares. The Fund is exposed to the risk of being unable to meet its payment obligations to redeeming shareholders. It therefore invests the majority of its assets in investments that are traded in an active market and can be readily liquidated.

To limit this risk, the Fund strictly complies with ICA Rule 35-1 which requires all Investment Companies/Mutual Funds to invest at least ten percent of its net assets in liquid/semi-liquid assets. This Rule defines such assets as (a) Treasury notes or bills, certificates of indebtedness issued by the Bangko Sentral ng Pilipinas (BSP) which are short-term, and other government securities; and (b) savings or time deposits with government or commercial banks in the name of the Fund.

The following table sets out the different investments as of December 31, 2011 and 2010 and their respective percentages to total net assets of the Fund:

	2011	2010
Government securities	**76.06%**	47.90%
Corporate bonds	**16.41**	24.93
Cash and cash equivalents	**5.90**	26.37
	98.37%	99.20%

The table below analyzes financial assets and liabilities of the Fund as of December 31, 2011 and 2010 into their relevant maturity groups based on remaining contractual undiscounted cash flows as of December 31, 2011 and 2010:

	2011						
	On demand	**Less than one month**	**1 to 3 months**	**3 to 12 months**	**1 to 5 years**	**More than 5 years**	**Total**
Financial Assets							
Financial assets at FVPL:							
Government securities	**₱–**	**₱748,989**	**₱–**	**₱6,677,361**	**₱159,415,000**	**₱200,735,000**	**₱367,576,350**
Corporate bonds	**–**	**1,751**	**27,641**	**36,241,087**	**21,887,806**	**1,177,000**	**59,335,285**
Loans and receivables:							
Cash and cash equivalents	**489,332**	**19,506,490**	**–**	**–**	**–**	**–**	**19,995,822**
Receivables:							
Accrued interest receivable	**–**	**5,630,852**	**23,128**	**28,521**	**–**	**–**	**5,682,501**
Due from related parties	**–**	**139**	**–**	**–**	**–**	**–**	**139**
Other receivables	**–**	**5,000**	**–**	**–**	**–**	**–**	**5,000**
	₱489,332	**₱25,893,221**	**₱50,769**	**₱42,946,969**	**₱181,302,806**	**₱201,912,000**	**₱452,595,097**
Financial Liabilities							
Accrued expenses and other liabilities*	**₱–**	**₱281,982**	**₱–**	**₱–**	**₱–**	**₱–**	**₱281,982**
Redeemable shares	**338,628,175**	**–**	**–**	**–**	**–**	**–**	**338,628,175**
Net Asset (liability)	**(₱338,138,843)**	**₱25,611,239**	**₱50,769**	**₱42,946,969**	**₱181,302,806**	**₱201,912,000**	**₱113,684,940**

**Excludes government-related payables*

	2010						
	On demand	Less than one month	1 to 3 months	3 to 12 months	1 to 5 years	More than 5 years	Total
Financial Assets							
Financial assets at FVPL							
Government securities	₱–	₱628,630	₱–	₱7,764,496	₱148,754,866	₱206,760,879	₱363,908,871
Corporate bonds	–	1,978	27,641	1,227,227	45,372,461	14,014,812	60,644,119
Loans and receivables:							
Cash and cash equivalents	370,605	144,504,113	–	–	–	–	144,874,718
Receivables:							
Unquoted debt securities	–	–	1,342,579	84,247,125	–	–	85,589,704
Accrued interest receivable	–	3,694,375	1,627,674	209,597	–	–	5,531,646
Due from related parties	–	50,667	–	–	–	–	50,667
Other receivables	–	5,000	–	–	–	–	5,000
	₱370,605	₱148,884,763	₱2,997,894	₱93,448,445	₱194,127,327	₱220,775,691	₱ 660,604,725
Financial Liabilities							
Accrued expenses and other liabilities*	₱–	₱123,826	₱–	₱–	₱–	₱–	₱123,826
Redeemable shares	549,311,978	–	–	–	–	–	549,311,978
Net Asset (liability)	(₱548,941,373)	₱148,760,937	₱2,997,894	₱93,448,445	₱194,127,327	₱220,775,691	₱111,168,921

**Excludes government-related payables*

As of December 31, 2011 and 2010, all financial liabilities of the Fund subject to liquidity risk are contractually payable at their face amounts. The Fund considers its cash equivalents, financial assets at FVPL and loans receivables as liquidity risk management tools. These financial instruments may be liquidated or sold by the Fund anytime the need for immediate funding arises.

Market Risk
Market risk is the risk of change in fair value of financial instruments from fluctuation in foreign exchange rates (currency risk), market interest rates (interest rate risk) and market prices (price risk), whether such change in price is caused by factors specific to the individual instrument or its issuer or factors affecting all instruments traded in the market.

The Fund is exposed to the risk that the value of the Fund's financial assets will be adversely affected by the fluctuations in the price level or volatility of one or more of the said assets. The two main components of the risks recognized by the Fund are systematic risk and unsystematic risk.

Systematic risk is the variability in price caused by factors that affect all securities across all markets (e.g. significant economic or political events). Unsystematic risk on the other hand, is the variability in price caused by factors which are specific to the particular issuer (corporation) of the shares of stock. Through proper portfolio diversification, this risk can be minimized as losses on one particular stock may be offset by gains in another.

To further mitigate these risks, the Fund ensures that the investment portfolio is adequately diversified taking into consideration the size of the portfolio. The effectiveness of the diversification of the portfolio may be evaluated by comparing the volatility of the portfolio versus the volatility of the HSBC Local Bond Index (Index) for the Philippines, which is a basket of all outstanding Peso-denominated government bonds. As shown below, the portfolio volatility of the investment portfolio as of December 31, 2011 and 2010, as measured by its annualized daily standard deviation is higher than the volatility of the said Index:

Volatility of investment portfolio	**2011**	2010
The Fund	**4.18%**	3.32%
HSBC Local Bond Index	**3.55%**	5.32%

a. *Interest Rate Risk*
Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments. The Fund's exposure to market risk for changes in interest rates relates primarily to the Fund's financial assets at FVPL, cash and cash equivalent and loans and receivables.

The Fund's market risk policy requires it to manage interest rate risk by maintaining appropriate mix of fixed and variable rate instruments. The policy also requires it to manage the maturities of interest-bearing financial assets.

i. *Fair value interest rate risk*
Fair value interest rate risk is the risk that the value of a financial instrument will fluctuate because of changes in market interest rates. The Fund's fixed rate investments and receivables in particular are exposed to such risk.

Refer to table below for simulation of measurable changes as of December 31, 2011, 2010 and 2009 using modified duration at 100 basis points as an approximation:

	Effect on Pre-Tax Income		
Basis points change in interest rates	**2011**	2010	2009
+100	**(₱16,310,710)**	(₱10,446,175)	(₱939,839)
–100	**17,807,334**	10,878,821	960,139

ii. *Cash flow interest rate risk/reinvestment risk*
Cash flow interest rate risk is the risk that cash flows from a financial instrument will fluctuate because of changes in market interest rates. The Fund's floating rate investments are exposed to such risk.

As of December 31, 2011 and 2010, the Fund does not have significant exposure to cash flow interest rate risk as the Fund does not have any floating rate financial instruments.

5. Fair Value of Financial Instruments

Fair value is defined as the amount at which the financial instrument could be exchanged in a current transaction between knowledgeable willing parties in an arm's length transaction, other than in a forced liquidation or sale. Fair values are obtained from quoted market prices, discounted cash flows models and option pricing models, as appropriate.

The following table sets forth the carrying values and estimated fair values of financial assets and liabilities recognized as of December 31, 2011 and 2010.

	2011		2010	
	Carrying Value	**Fair Value**	Carrying Value	Fair Value
Financial Assets				
Financial assets at FVPL:				
Government securities	**₱257,562,480**	**₱257,562,480**	₱263,105,937	₱263,105,937
Corporate bonds	**55,578,882**	**55,578,882**	54,009,684	54,009,684
	313,141,362	**313,141,362**	317,115,621	317,115,621
Loans and receivables:				
Cash and cash equivalents	**19,993,980**	**19,993,980**	144,828,073	144,828,073
Receivables:				
Accrued interest receivable	**5,682,501**	**5,682,501**	5,531,646	5,531,646
Due from related parties	**139**	**139**	50,667	50,667
Other receivables	**5,000**	**5,000**	5,000	5,000
Unquoted debt securities	**–**	**–**	82,953,833	84,429,071
	25,681,620	**25,681,620**	233,369,219	234,844,457
	₱338,822,982	**₱338,822,982**	₱550,484,840	₱551,960,078
Financial Liabilities				
Accrued expenses and other liabilities*	**₱281,982**	**₱281,982**	₱123,826	₱123,826

**Excludes government-related payables*

Fair values of financial assets and liabilities are estimated as follows:

Cash and cash equivalents, accrued interest receivable, due from related parties and other receivables
The carrying amounts approximate the fair values due to short-term maturity.

Financial assets at FVPL
Fair values are estimated using either values obtained from independent parties offering pricing services, quoted market prices of comparable investments or using the discounted cash flow method.

Accrued expenses and other liabilities
The carrying amounts approximate fair values considering that these are due and demandable.

Fair value hierarchy
The Fund uses the following hierarchy for determining and disclosing the fair value of financial instruments measured at fair value:

Level 1: quoted (unadjusted) prices in active markets for identified assets or liabilities.
Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly.
Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

As of December 31, 2011 and 2010, the Fund has financial assets at FVPL with carrying amount of ₱257.6 million and ₱263.1 million, respectively, which are classified as Level 1 and ₱55.6 million and ₱54.0 million classified as Level 2. In 2011 and 2010, there were no transfers among the three levels in the fair value hierarchy.

6. Cash and Cash Equivalents

This account consists of:

	2011	2010
Cash in banks	**₱489,332**	₱370,605
Short-term placements	**19,504,648**	144,457,468
	₱19,993,980	₱144,828,073

Cash in banks earn interest at the respective bank deposit rates. Short-term placements are made for varying periods of up to three months depending on the immediate cash requirements of the Fund, and earn interest at the respective short-term deposit rates. The Fund earns interest rates per annum ranging from 1.75% to 4.25%, and 1.75% to 4.03% and 1.75% to 4.25% in 2011, 2010 and 2009, respectively.

In 2011, 2010 and 2009, interest income earned on short-term placements and cash in banks amounted to ₱0.7 million, ₱1.0 million and ₱0.9 million, respectively.

7. Financial Assets at Fair Value Through Profit or Loss

This account consists of investments in:

	2011	2010
Government securities	**₱257,562,480**	₱263,105,937
Corporate bonds	**55,578,882**	54,009,684
	₱313,141,362	₱317,115,621

Investments in government securities and corporate bonds are designated as 'Financial assets at FVPL' and are carried at fair value. Part of the risk management process of the Fund is the analysis and monitoring of the real economic position including those investments that are not actively traded. Moreover, the performance of the Fund is being measured or evaluated on a fair value basis.

Changes in market value are included as 'Net unrealized gain (loss) on changes in fair value of financial assets at FVPL' in the statements of comprehensive income.

The Fund recognized gain on market valuation on these investments amounting to ₱10.0 million, ₱5.5 million and ₱1.0 million in 2011, 2010 and 2009, respectively.

As of December 31, 2011, 2010 and 2009, government securities bear an annual coupon interest rate ranging from 6.35% to 8.15%, from 4.63% to 7.00% and from 7.00% to 8.50%, respectively. As of December 31, 2011, 2010 and 2009, corporate bonds bear an annual coupon interest rate ranging from 7.38% to 9.10%.

In 2011, 2010 and 2009, interest income earned on government securities and corporate bonds amounted to ₱16.6 million, ₱5.4 million and ₱5.4 million, respectively.

8. Loans and Receivables

This account consists of:

	2011	2010
Accrued interest receivable	**₱5,682,501**	₱5,531,646
Due from related parties	**139**	50,667
Other receivables	**5,000**	5,000
Unquoted debt securities	**–**	82,953,833
	₱5,687,640	₱88,541,146

Unquoted debt securities pertain to investment in private bond that is not quoted in an active market and was acquired at a premium over its face amount. The said bond matured in September 2011.

Interest income on unquoted debt securities, presented in the statements of comprehensive income amounted to ₱2.6 million, ₱2.3 million and ₱2.1 million in 2011, 2010 and 2009, respectively.

9. Accrued Expenses and Other Liabilities

This account consists of:

	2011	2010
Financial liabilities:		
Accounts payable	**₱158,215**	₱50,000
Accrued expenses	**98,784**	67,600
Due to PEMI (Note 14)	**24,983**	6,226
	281,982	123,826
Nonfinancial liabilities:		
Withholding tax payable	**₱1,313**	₱610
Documentary stamp tax payable	**1,035**	740,335
	2,348	740,945
	₱284,330	₱864,771

Accounts payable includes payable to shareholders for the unpaid redemption proceeds, and subscriptions without confirmation from the investors. Subscription is confirmed by submitting the required subscription documents. Once confirmed, these subscriptions are reclassified to equity.

Due to PEMI pertains to sales load fees and exit fees to be remitted by the Fund the following month.

10. Equity

Capital Stock
The Fund's capital stock consists of 100,000,000 authorized shares at ₱1 par value common stock. As of December 31, 2011 and 2010, it has 99,359,684 and 94,701,523 shares issued and outstanding, respectively.

NAV Per Share
As an open-end mutual fund company, the Fund stands ready at any time to redeem the outstanding capital stock at NAV per share. NAV per share is computed by dividing net assets (total assets less total liabilities) by the number of shares issued and outstanding as of reporting date.

The shares are entitled to payment of a proportionate share of the Fund's NAV on the redemption date or upon winding up of the Fund. The Fund's issued and outstanding shares are redeemed at their NAV calculated in accordance with redemption requirements. The total expected cash outflow on redemption of all the shares equals the Fund's equity. Issuance, repurchase and resale of redeemable shares is based on the prevailing NAV per share at the date of the transaction.

	2011	2010
NAV attributable to holders of redeemable shares	**₱338,628,175**	₱549,311,978
Number of shares outstanding*	**121,180,257**	211,958,338
NAV per share	**₱2.7944**	₱2.5916

* *Includes equivalent number of shares in the deposits for future stock subscription totaling 21,820,573 and 117,256,815 shares as of December 31, 2011 and 2010, respectively.*

Total deposits for future stock subscription as of December 31, 2011 and 2010 amounted to ₱56.3 million and ₱304.2 million, respectively. On March 16, 2011, the BOD approved the proposal to amend the Articles of Incorporation to increase its authorized capital stock from 100,000,000 common shares to 500,000,000. As of December 31, 2011, the Fund is in the process of preparing the application documents to file the increase in authorized capital stock with SEC.

Capital Management
The Fund's investment objective is to seek long-term capital appreciation through investment primarily in various debt securities issued by the Philippine government and corporations, while taking into consideration the liquidity and safety of its investments to protect the interest of its investors.

Due to the Fund's nature as an open-end mutual fund, its capital, consisting entirely of common shares, is variable and increases or decreases depending on the volume of subscriptions and redemptions made by its various shareholders. The maximum number of shares that can be issued is determined by the Fund's authorized capital but may be increased by the Fund upon approval by the SEC. The investment restrictions of the Fund are discussed in Note 4.

As of December 31, 2011 and 2010, the Fund does not have any outstanding debt on its statement of financial position. Any liabilities reflected therein are short-term in nature and generally reflect amounts that are due for settlement with its counterparties or its investors within the standard settlement periods prescribed for each transaction:

a) Stock purchases: three days after date of transaction; and
b) Redemptions from shareholders: maximum of seven days after date of transaction as prescribed by the ICA Rule 35-1.

As of December 31, 2011 and 2010, the number of shareholders of the Fund's redeemable shares is 159 and 115, respectively.

There are no changes made in the objectives and policies during the years ended December 31, 2011 and 2010.

Minimum Capital Requirement
As an investment company registered with the SEC, the Fund must continually comply with the minimum subscribed and paid-up capital of ₱50.0 million as required under Section 12. *Structure and Capitalization of Investment Companies* of ICA.

As of December 31, 2011 and 2010, the Fund has complied with the externally imposed capital requirement.

11. Maturity Analysis

The following table shows an analysis of assets and liabilities and analyzed according to whether they are expected to be recovered or settled within one year from reporting date:

	2011			2010		
	Up to a Year	**More than One Year**	**Total**	Up to a Year	More than One Year	Total
Financial Assets						
Cash and cash equivalents	**₱19,993,980**	**₱–**	**₱19,993,980**	₱144,828,073	₱–	₱144,828,073
Financial assets at FVPL:						
Government securities	**–**	**257,562,480**	**257,562,480**	–	263,105,937	263,105,937
Corporate bonds	**34,500,312**	**21,078,570**	**55,578,882**	–	54,009,684	54,009,684
Receivables (Note 8):						
Accrued interest receivable	**5,682,501**	**–**	**5,682,501**	5,531,646	–	5,531,646
Due from PEMI	**139**	**–**	**139**	50,667	–	50,667
Other Receivables	**5,000**	**–**	**5,000**	5,000	–	5,000
Unquoted debt securities	**–**	**–**	**–**	82,953,833	–	82,953,833
	60,181,932	**278,641,050**	**338,822,982**	233,369,219	317,115,621	550,484,840
Nonfinancial Assets						
Other assets	**89,523**	**–**	**89,523**	–	–	–
	₱60,271,455	**₱278,641,050**	**₱338,912,505**	₱233,369,219	₱317,115,621	₱550,484,840

(Forward)

	2011			2010		
	Up to a Year	**More than One Year**	**Total**	Up to a Year	More than One Year	Total
Financial Liabilities						
Accrued expenses and other liabilities	**₱281,982**	**₱–**	**₱281,982**	₱123,826	₱–	₱123,826
Nonfinancial Liabilities						
Withholding tax payable	**1,313**	**–**	**1,313**	610	–	610
Documentary stamp tax payable	**1,035**	**–**	**1,035**	740,335	–	740,335
Income tax payable	**–**	**–**	**–**	308,091	–	308,091
	₱284,330	**₱–**	**₱284,330**	₱1,172,862	₱–	₱1,172,862

12. Other expenses

Breakdown of other expenses is as follows:

	2011	2010	2009
Trustee Fee	**₱108,040**	₱29,636	₱19,567
Directors' Fee	**30,000**	75,294	10,000
Others	**21,888**	79,017	44,255
	₱159,928	₱183,947	₱73,822

13. Income Tax

Provision from income tax consists of:

	2011	2010	2009
Final	**₱3,462,816**	₱208,139	₱45,362
RCIT	**335,822**	308,091	1,248,797
	₱3,798,638	₱516,230	₱1,294,159

Republic Act (RA) No. 9337, *An Act Amending National Internal Revenue Code*, provides that RCIT rate shall be 35.00% until December 31, 2008. Starting January 1, 2009, the RCIT rate shall be 30.00%. The National Internal Revenue Code (NIRC) of 1997 also provides for rules on the imposition of a 2.00% MCIT on modified gross income. The MCIT and NOLCO may be applied against the Fund's income tax liability and taxable income, respectively, over a three-year period from the year of inception. Moreover, starting July 1, 2008, the Optional Standard Deduction (OSD) equivalent to 40.00% of gross income may be claimed as an alternative deduction in computing for the RCIT.

As of December 31, 2011, 2010 and 2009, the Fund has no available NOLCO and MCIT.

The reconciliation between the Fund's provision for income tax computed at the statutory income tax rates to the provision for income tax shown in the statements of comprehensive income is summarized as follows:

	2011	2010	2009
Income tax at statutory tax rate	**₱8,684,060**	₱3,891,020	₱2,913,042
Tax effects of:			
Interest income subjected to final tax	**(1,731,464)**	(1,698,864)	(624,398)
Net unrealized gain on change in fair value of financial assets at FVPL	**(3,001,174)**	(1,656,310)	(306,864)
Net realized gain on sale of debt instruments exempt from tax	**(152,784)**	(19,616)	67,949
Applied NOLCO	**–**	–	(544,996)
Dividend income exempt from tax	**–**	–	(256,581)
Excess of MCIT over RCIT	**–**	–	40,391
Nondeductible expense	**–**	–	5,616
	₱3,798,638	₱516,230	₱1,294,159

14. **Related Party Disclosures**

The Fund has an existing Agreement with PEMI, the Fund manager. Pursuant to the terms of the Management and Distribution Agreement, the Fund shall pay an annual management fee of a maximum of 1.50% of the average NAV of the Fund. The NAV shall be determined in accordance with the procedures agreed upon by both parties. PEMI had waived charges for management fee amounting to ₱2.2 million, ₱1.9 million and ₱1.5 million in 2011, 2010 and 2009, respectively. Also, the Fund shall remit to PEMI sales commission of a maximum of 3.50% of the gross investment based on tiered-front end sales schedule which is included as 'Due to PEMI'.

As of December 31, 2011 and 2010, 'Due to PEMI' amounted to ₱24,983 and ₱6,226, respectively, included as part of 'Accrued expenses and other liabilities' account in the statements of financial position.

The Fund has no key management personnel. The key management functions are being handled by PEMI.

As of December 31, 2011 and 2010, seven shares of the Fund are held by directors.

15. **Segment Reporting**

For management reporting purposes, the Fund is organized into one main operating segment, which invests in debt instruments. All of the Fund's activities are interrelated, and each activity is dependent on the others. Accordingly, all significant operating decisions are based upon analysis of the Fund as one segment. The financial results from this segment are equivalent to the financial statements of the Fund as a whole.

The table below analyzes the Fund's revenue streams per investment type:

	2011	2010	2009
Financial assets at FVPL	**₱27,096,044**	₱10,770,633	₱6,451,091
Unquoted debt securities	**2,599,271**	2,510,104	2,875,155
Short-term placements and cash in banks	**731,415**	1,001,884	851,187
	₱30,426,730	₱14,282,621	₱10,177,433

16. **Earnings Per Share**

	2011	2010	2009
Net investment income (a)	**₱25,148,227**	₱12,453,836	₱8,415,981
Weighted average number of outstanding shares of stock (b)	**97,706,043**	63,664,064	57,870,509
Earnings per share (a/b)	**₱0.2574**	₱0.1956	₱0.1454

As of December 31, 2011 and 2010, there were no potential common shares with dilutive effect on the basic earnings per share.

17. **Supplementary Information Required Under Revenue Regulations No. 19-2011 and 15-2010**

Supplementary Information Required Under Revenue Regulation No. 19-2011
On December 9, 2011, the Bureau of Internal Revenue (BIR) issued RR No. 19-2011 which prescribes the new annual income tax forms that will be used for filing effective taxable year 2011. Specifically, companies are required to disclose certain tax information in their respective notes to financial statements.

In its 2011 filing for income tax return, the Fund disclosed the following information on taxable income and deductions using the revised format required under RR 19-2011:

Sales/Receipts/Fees	₱–
Cost of sales/services	–
Non-operating and taxable other income	2,599,271
Itemized deductions	(1,479,865)
	₱1,119,406

The details of itemized deductions are as follow:

Taxes and licenses	₱878,022
Professional fees	421,915
Trustee fee	108,040
Directors fee	30,000
Dues and fees	20,000
Others	21,888
	₱1,479,865

Supplementary Information Required Under RR No. 15-2010
The Fund also reported and/or paid the following types of taxes for the year:

Taxes and licenses
In 2011, the Fund reported and/or paid the following taxes and licenses fees:

Documentary stamp tax	₱775,572
Municipal permits	95,912
Community tax	3,889
Fire safety clearance	2,034
Annual registration	500
Barangay clearance	115
	₱878,022

Withholding taxes
As of December 31, 2011, total remittances and balance of withholding taxes follow:

	Total remittances	Balance
Expanded withholding taxes	₱19,665	₱1,313
Final withholding taxes	3,462,816	–
	₱3,482,481	₱1,313