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

Financial Statements

December 31, 2008 and 2007 and
Years Ended December 31, 2008, 2007 and 2006

and

Independent Auditors' Report

SyCip Gorres Velayo & Co.

SGV & Co
Ernst & Young

SyCip Gorres Velayo & Co.
6760 Ayala Avenue
1226 Makati City
Philippines

Phone: (632) 891 0307
Fax: (632) 819 0872
www.sgv.com.ph

BOA/PRC Reg. No. 0001
SEC Accreditation No. 0012-FR-1

INDEPENDENT AUDITORS' REPORT

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

We have audited the acFunding financial statements of Philequity Peso Bond Fund, Inc. (an open-end mutual fund Fund), which comprise the statements of assets and liabilities as at December 31, 2008 and 2007, and the statements of income, statements of changes in net assets attributable to unitholders and statements of cash flows for each of the three years in the period then ended December 31, 2008, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

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

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 of December 31, 2008 and 2007, and its financial performance and its cash flows for each of the three years in the period then ended December 31, 2008 in accordance with Philippine Financial Reporting Standards.

SYCIP GORRES VELAYO & CO.

Christian G. Lauron
Partner
CPA Certificate No. 95977
SEC Accreditation No. 0790-A
Tax Identification No. 210-474-781
PTR No. 1566435, January 5, 2009, Makati City

April 1, 2009

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

STATEMENTS OF ASSETS AND LIABILITIES

	December 31	
	2008	2007
ASSETS		
Cash and Cash Equivalents (Note 4)	**₱1,616,916**	₱11,390,170
Financial Assets at Fair Value through Profit or Loss (Note 5)	**140,573,647**	177,857,981
Receivables (Note 6)	**6,757,219**	6,914,479
	148,947,782	196,162,630
LIABILITIES		
Accrued Expenses and Other Liabilities	**110,507**	52,052
NET ASSETS ATTRIBUTABLE TO UNITHOLDERS (Note 7)	**₱148,837,275**	₱196,110,578
Net Asset Value Per Share (Note 7)	**₱2.230**	₱2.177

See acFunding Notes to Financial Statements.

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

STATEMENTS OF INCOME

		Years Ended December 31	
	2008	2007	2006
INVESTMENT INCOME			
Interest income (Notes 3, 5 and 6)	**₱15,005,109**	₱12,650,120	₱16,008,104
Gain (loss) on sale of financial assets at fair value through profit or loss (FVPL)	**(10,034,601)**	(1,565,934)	8,739,227
Dividends	**1,006,261**	865,419	1,161,906
Gain (loss) on changes in fair value of financial assets at FVPL (Note 5)	**204,146**	(714,224)	5,185,276
Other Income	**100**	–	–
	6,181,015	11,235,381	31,094,513
EXPENSES			
Documentary stamp tax	**476,528**	12,154	290,251
Professional fees	**196,453**	257,475	172,900
Taxes and licenses	**126,449**	220,064	71,673
Dues and fees	**20,000**	52,600	530
Others (Note 9)	**85,464**	153,285	56,485
	904,894	695,578	591,839
INVESTMENT INCOME BEFORE INCOME TAX	**5,276,121**	10,539,803	30,502,674
PROVISION FOR INCOME TAX (Note 8)	**–**	–	–
INCREASE IN NET ASSETS FROM OPERATIONS ATTRIBUTABLE TO UNITHOLDERS	**₱5,276,121**	₱10,539,803	₱30,502,674

See acFunding Notes to Financial Statements.

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

STATEMENTS OF CHANGES IN NET ASSETS ATTRIBUTABLE TO UNITHOLDERS

	Years Ended December 31		
	2008	2007	2006
NET ASSETS ATTRIBUTABLE TO UNITHOLDERS AT BEGINNING OF YEAR	**₱196,110,578**	₱191,453,879	₱176,643,547
INCREASE IN NET ASSETS FROM OPERATIONS ATTRIBUTABLE TO UNITHOLDERS	**5,276,121**	10,539,803	30,502,674
TRANSACTIONS WITH UNITHOLDERS (Note 7)			
Proceeds from subscriptions of shares	**206,924,841**	4,184,220	115,027,408
Payments for redemptions of shares	**(259,474,265)**	(10,067,324)	(130,719,750)
	(52,549,424)	(5,883,104)	(15,692,342)
NET INCREASE (DECREASE) IN NET ASSETS ATTRIBUTABLE TO UNITHOLDERS	**(47,273,304)**	4,656,699	14,810,332
NET ASSETS ATTRIBUTABLE TO UNITHOLDERS AT END OF YEAR (Note 7)	**₱148,837,274**	₱196,110,578	₱191,453,879

See acFunding Notes to Financial Statements.

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

STATEMENTS OF CASH FLOWS

	Years Ended December 31		
	2008	2007	2006
CASH FLOWS FROM OPERATING ACTIVITIES			
Investment income before income tax	**₱5,276,121**	₱10,539,803	₱30,502,674
Adjustments for:			
Interest income	**(15,005,109)**	(12,650,120)	(16,008,104)
Loss (gain) on sale of financial assets at fair value through profit or loss (FVPL)	**10,034,601**	1,565,934	(8,739,227)
Dividend income	**(1,006,261)**	(865,419)	(1,161,906)
Loss (gain) on change in fair value of financial assets at FVPL (Note 5)	**204,147**	714,224	(5,185,276)
Loss before working capital changes	**(496,501)**	(695,578)	(591,839)
Proceeds from sale of financial assets at FVPL	**312,690,079**	90,017,698	92,326,370
Acquisitions of financial assets at FVPL	**(285,644,493)**	(106,099,752)	(73,138,288)
Increase in receivables	**(789,047)**	–	–
Increase (decrease) in accrued expenses and other liabilities	**58,455**	(2,068,857)	6,762
Net cash generated from (used for) operations	**25,818,493**	(18,846,489)	18,603,005
Interest received	**15,970,189**	13,407,651	17,350,856
Dividends received	**987,488**	1,159,781	885,416
Income taxes paid	**–**	–	(23,906)
Net cash provided by (used in) operating activities	**42,776,170**	(4,279,057)	36,815,371
CASH FLOW FROM INVESTING ACTIVITY			
Increase in notes receivable	**–**	–	(4,000,000)
CASH FLOWS FROM FINANCING ACTIVITIES			
Payments for redemptions of shares	**(259,474,265)**	(10,067,324)	(130,719,750)
Proceeds from subscriptions of shares	**206,924,841**	4,184,220	115,027,408
Net cash used in financing activities	**(52,549,424)**	(5,883,104)	(15,692,342)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	**(9,773,254)**	(10,162,161)	17,123,029
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	**11,390,170**	21,552,331	4,429,302
CASH AND CASH EQUIVALENTS AT END OF YEAR (Note 4)	**₱1,616,916**	₱11,390,170	₱21,552,331

See acFunding Notes to Financial Statements.

NOTES TO FINANCIAL STATEMENTS

1. Corporate Information

Philequity Peso Bond Fund, Inc. (the Fund) was incorporated in the Philippines and registered with the Securities and Exchange Commission (SEC) on February 24, 1999 as an open-end mutual fund 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 Securities and Exchange Commission (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.

The acFunding financial statements of the Fund were approved and authorized for issue by the Board of Directors (BOD) on April 1, 2009.

2. Summary of Significant Accounting Policies

Statement of Compliance
The financial statements have been prepared on a historical cost basis, except for financial assets at fair value through profit and loss (FVPL) that have been measured at fair value. The financial statements are presented in Philippine Peso, the Fund's functional and presentation currency. All values are rounded to the nearest peso, except when otherwise indicated.

Basis of Preparation
The acFunding financial statements have been prepared in compliance with Philippine Financial Reporting Standards (PFRS).

Changes in Accounting Policies
The accounting policies adopted are consistent with those of the previous financial year except for the adoption of the following amendments to existing standards that become effective on July 1, 2008 and Philippine Interpretations which became effective on January 1, 2008:

- Amendments to Philippine Accounting Standards (PAS) 39, *Financial Instruments: Recognition and Measurement* and PFRS 7, *Financial Instruments: Disclosure - Reclassification of Financial Assets*
  The amendment to PAS 39 introduces the possibility of reclassification of securities out of the trading category in rare circumstances and reclassification to the loans and receivables category if there is intent and ability to hold the securities for the foreseeable future or to held-to-maturity (HTM) if there is intent and ability to hold the securities until maturity. It also

allows the transfers of certain financial assets from AFS to loans and receivables and HTM. The amendment to PFRS 7 introduces the disclosures relating to these reclassifications. This interpretation does not have any impact on the Fund because there was no reclassification made.

- Philippine Interpretation IFRIC-11, *PFRS 2-Group and Treasury Share Transactions,* requires arrangements whereby an employee is granted rights to an entity's equity instruments to be accounted for as an equity-settled scheme by the entity even if (a) the entity chooses or is required to buy those equity instruments (e.g., treasury shares) from another party, or (b) the shareholders of the entity provide the equity instruments needed. It also provides guidance on how subsidiaries, in their separate financial statements, account for such schemes when their employees receive rights to the equity instruments of the parent. This Interpretation is not relevant to the Fund.

- Philippine Interpretation IFRIC-12, *Service Concession Arrangements*, covers contractual arrangements arising from private entities providing public services. This interpretation is not relevant to the Fund.

- Philippine Interpretation IFRIC-13, *Customer Loyalty Programmes*, requires customer loyalty award credits to be accounted for as a separate component of the sales transaction in which they are granted and therefore part of the fair value of the consideration received is allocated to the award credits and deferred over the period that the award credits are fulfilled. This Interpretation has no impact to the Fund as no such schemes currently exist.

- Philippine Interpretation IFRIC-14, *The Limit on a Defined Benefit Asset, Minimum Funding Requirement and their Interaction,* provides guidance on how to assess the limit on the amount of surplus in a defined benefit scheme that can be recognized as an asset under PAS 19, *Employee Benefits*. This interpretation is not relevant to the Fund since no employee benefits currently exist.

Cash and Cash Equivalents

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

Financial Instruments

Date of Recognition

Financial instruments are recognized in the statement of assets and liabilities when the Fund becomes a party to the contractual provisions of the instrument. Purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace are recognized using the trade date accounting.

Initial recognition of financial instruments

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

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

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

'Day' 1 difference
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 observable market, the Fund recognizes the difference between the transaction price and fair value (a 'Day 1' difference) in the statement of income unless it qualifies for recognition as some other type of asset. In cases where use is made of data which is not observable, the difference between the transaction price and model value is only recognized in the statement of 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' difference amount.

Financial assets and financial liabilities at FVPL
Financial assets and liabilities at FVPL include financial assets and liabilities held for trading purposes and financial assets and liabilities designated upon initial recognition as at FVPL. Financial assets and liabilities are classified as held for trading if they are acquired for the purposes of selling and repurchasing in the near term.

Financial assets or 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; or
- 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 liabilities at FVPL are recorded in the statement of assets and liabilities at fair value. Subsequent changes in fair value are recognized in the statement of income on financial assets and liabilities designated at FVPL. Interest earned or incurred is recorded in interest income or expense, respectively.

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 positive intention and ability to hold to maturity. Where the Fund sell other than an insignificant amount of HTM investments, the entire category would be tainted and reclassified as AFS investments. After initial measurement, these investments are subsequently measured at amortized cost using the effective interest rate method, less impairment in value. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the effective interest rate. Gains and losses are recognized in the statement of income when the HTM investments are derecognized and impaired, as well as through the amortization process. The effects of restatement on foreign currency-denominated HTM investments are also recognized in the statement of income.

Loans and receivables
Loans and receivables are nonderivative 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 other financial assets or designated as AFS investment or financial assets at FVPL. Loans and receivables are included in current assets if maturity is within 12 months from the statement of assets and liabilities date. Otherwise, these are classified as noncurrent assets. Classified under loans and receivables are cash and cash equivalents and receivables.

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

Classified under loans and receivables are cash and cash equivalents and receivables.

AFS Investments
AFS investments are those which are designated as such or do not qualify to be classified as designated 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. AFS investments are included in current assets if management intends to sell these financial assets within 12 months from statement of assets and liabilities date. Otherwise, these are classified as noncurrent assets.

After initial measurement, AFS investments are subsequently measured at fair value. The effective yield component of AFS debt securities, as well as the impact of restatement on foreign currency-denominated AFS debt securities, is reported as income. The unrealized gains and losses arising from the fair valuation of AFS investments are excluded, net of tax, from reported income and are reported as 'Net unrealized gain (loss) on AFS investments' in the equity section of the balance sheet.

When the security is disposed of, the cumulative gain or loss previously recognized in equity is recognized as 'Trading gains - net' in the statement of income. Where the Fund holds more than one investment in the same security, these are deemed to be disposed of on a first-in first-out basis. Interest earned on holding AFS investments are reported as 'Interest income' using the EIR. Dividends earned on holding AFS investments are recognized in the statement of income when the right of the payment has been established. The losses arising from impairment of such investments are recognized as 'Provision for credit and impairment losses' in the statement of income.

Financial liabilities carried at amortized cost
Financial liabilities are classified in this category if these are not held for trading or not designated as at FVPL upon the inception of the liability. These include liabilities arising from operations or borrowings.

These instruments are initially recognized at fair value, less directly attributable transaction costs. After initial recognition, other financial liabilities are subsequently measured at amortized cost using the effective interest method. Amortized cost is calculated by taking into account any related issue costs, discount or premium. Gains or losses are recognized in the statement of income when the liabilities are derecognized, as well as through the amortization process.

Classified under other financial liabilities are accrued expenses and other liabilities.

<u>Derecognition of Financial Assets and Liabilities</u>
Financial asset
A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognized when:
- the rights to receive cash flows from the asset have expired;
- 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 the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

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 liability
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 statement of income.

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

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

If there is objective evidence that an impairment loss has been incurred, the amount of loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows (excluding future credit losses that have not been incurred). The carrying amount of the asset is reduced through use of an allowance account and the amount of loss is charged to the statement of income. Interest income continues to be recognized based on the original effective interest rate of the asset. The financial assets, together with the associated allowance accounts, are written off when there is no realistic prospect of future recovery and all collateral has been realized.

If, in a subsequent year, the amount of the estimated impairment loss decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is reduced by adjusting the allowance account. If a future write-off is later recovered, any amounts formerly charged are credited to the ‘Provision for impairment and credit losses’ in the statement of income.

The present value of the estimated future cash flows is discounted at the financial asset’s original effective interest rate. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate, adjusted for the original credit risk premium. The calculation of the present value of the estimated future cash flows of a collateralized financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

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

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. Estimates of changes in future cash flows reflect, and are directionally consistent with changes in related observable data from period to period (such as changes in unemployment rates, property prices, commodity prices, payment status, or other factors that are indicative of incurred losses in the group and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Fund to reduce any differences between loss estimates and actual loss experience.

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

AFS Investments
For AFS investments, the Fund assesses at each statement of asset and liabilities date whether there is objective evidence that a financial asset or group of financial assets is impaired.

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

In the case of debt instruments classified as AFS investment, impairment is assessed based on the same criteria as financial assets carried at amortized cost. Future interest income is based on the reduced carrying amount and is accrued based on the rate of interest used to discount future cash flows for the purpose of measuring impairment loss. Such accrual is recorded as part of "Interest income" in the statement of income. If, in subsequent year, the fair value of a debt instrument increased and the increase can be objectively related to an event occurring after the impairment loss was recognized in the statement of income, the impairment loss is reversed through the statement of income.

<u>Offsetting Financial Instruments</u>
Financial assets and liabilities are offset and the net amount reported in the statement of assets and liabilities if, and only if, there is a currently enforceable legal right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously. This is not generally the case with master netting agreements, and the related assets and liabilities are presented gross in the statement of assets and liabilities.

<u>Provisions</u>
Provisions, if any, 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.

<u>Revenue</u>
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. The following specific recognition criteria must also be met before revenue is recognized:

Gain on sale of financial assets at FVPL
Gain on sale of financial assets at FVPL is determined at the time of sale transaction measured as the difference between the net sales proceeds and the net book value.

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

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

<u>Income Taxes</u>
Current Tax
Current tax liabilities for the current and prior periods are measured at the amount expected to be paid to the tax authority. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted at the statement of assets and liabilities date.

Deferred Tax
Deferred tax is provided, using the statement of assets and liabilities liability method, on all temporary differences at the statement of assets and liabilities 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 carry-forward benefits of minimum corporate income tax (MCIT) over regular corporate income tax and net operating loss carryover (NOLCO), to the extent that it is probable that taxable income will be available against which the deductible temporary differences and carry-forward benefits of MCIT and NOLCO can be utilized.

The carrying amount of deferred tax assets is reviewed at statement of assets and liabilities 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 statement of assets and liabilities 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 the tax rate that is expected to apply to the year when the asset is realized or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted at the statement of assets and liabilities date.

Net Asset Value (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.

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

Subsequent Events
Any post year-end events that provide additional information about the Fund’s position at statement of assets and liabilities date (adjusting event) are reflected in the financial statements. Post year-end events that are not adjusting events, if any, are disclosed when material to the financial statements.

Future Changes in Accounting Policies
The Fund will adopt the following standards and interpretations enumerated below when these become effective. Except as otherwise indicated, the Fund does not expect the adoption of the new and amended PFRS and Philippine Interpretations to have significant impact on the Financial Statements.

Effective in 2009
Amendment to PAS 1, *Amendment on Statement of Comprehensive Income* (effective for annual periods beginning on or after January 1, 2009)
In accordance with the amendment to PAS 1, the statements of changes in equity shall include only transactions with owners, while all non-owner changes will be presented in equity as a single line with details included in a separate statement. Owners are defined as holders of instruments classified as equity.

In addition, the amendment to PAS 1 provides for the introduction of a new statement of comprehensive income that combines all items of income and expenses recognized in the statement of income together with 'other comprehensive income'. The revision specify what is included in other comprehensive income, such as gains and losses on AFS investments, actuarial gains and losses on defined benefit pension plans and changes in the asset revaluation reserve.

Entities can choose to present all items in one statement, or to present two linked statements, a separate statement of income and a statement of comprehensive income. Adoption of this amendment will not have a significant impact on the Fund except for the presentation of a statement of comprehensive income and additional disclosures to be included in the financial statements.

PAS 23, *Borrowing Costs (Revised)* (effective for annual periods beginning on or after January 1, 2009)
The Standard has been revised to require capitalization of borrowing costs when such costs relate to a qualifying asset. A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale. In accordance with the transitional requirements in the Standard, this change in accounting for borrowing costs shall be accounted for prospectively. Accordingly, borrowing costs will be capitalized on qualifying asset with a commencement date after January 1, 2009.

Amendments to PAS 32, *Financial Instruments: Presentation and* PAS 1, *Presentation of Financial Statements - Puttable Financial Instruments and Obligations Arising on Liquidation* (effective for annual periods beginning on or after January 1, 2009)
The Standards have been amended to allow a limited scope exception for puttable financial instruments to be classified as equity if they fulfill a number of specified criteria.

PFRS 1, *First-time Adoption of PFRS - Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate*
The amended PFRS 1 allows an entity, in its separate financial statements, to determine the cost of investments in subsidiaries, jointly controlled entities or associates (in its opening PFRS financial statements) as one of the following amounts: a) cost determined in accordance with PAS 27; b) at the fair value of the investment at the date of transition to PFRS, determined in accordance with PAS 39; or c) previous carrying amount (as determined under generally accepted accounting principles) of the investment at the date of transition to PFRS.

PFRS 2, *Share-based Payment - Vesting Condition and Cancellations* (effective for annual periods beginning on or after January 1, 2009)
The standard has been revised to clarify the definition of a vesting condition and prescribes the treatment for an award that is effectively cancelled. It defines a vesting condition as a condition that includes an explicit or implicit requirement to provide services. It further requires non-vesting conditions to be treated in a similar fashion to market conditions. Failure to satisfy a non-vesting condition that is within the control of either the entity or the counterparty is accounted for as cancellation. However, failure to satisfy a non-vesting condition that is beyond the control of either party does not give rise to a cancellation.

PFRS 8, *Operating Segments* (effective for annual periods beginning on or after January 1, 2009)
This PFRS adopts a management approach to reporting segment information. PFRS 8 will replace PAS 14, *Segment Reporting*, and is required to be adopted only by entities whose debt or equity instruments are publicly traded, or are in the process of filing with the SEC for purposes of issuing any class of instruments in a public market.

Philippine Interpretation IFRIC-13*, Customer Loyalty Programmes* (effective for annual periods beginning on or after July 1, 2008)
This Interpretation requires loyalty credits to be accounted for as a separate component of the sales transaction in which they are granted.

Philippine Interpretation IFRIC 16, *Hedges of a Net Investment in a Foreign Operation* (effective for annual periods beginning on or after October 1, 2008)
This Interpretation is to be applied prospectively. IFRIC 16 provides guidance on identifying foreign currency risks that qualify for hedge accounting in the hedge of a net investment, where within the group the hedging instruments can be held in the hedge of a net investment, and how an entity should determine the amount of foreign currency gains or losses, relating to both the net investment and the hedging instrument, to be recycled on disposal of the net investment.

<u>*Effective in 2010*</u>
Amendment to PAS 39, *Financial Instruments: Recognition and Measurement - Eligible hedged items*
Amendment to PAS 39 will be effective on July 1, 2009, which addresses only the designation of a one-sided risk in a hedged item, and the designation of inflation as a hedged risk or portion in particular situations. The amendment clarifies that an entity is permitted to designate a portion of the fair value changes or cash flow variability of a financial instrument as a hedged item.

PAS 27, *Consolidated and Separate Financial Statements (Revised)* (effective for annual periods beginning on or after July 1, 2009)
This revised Standard establishes that change in the ownership interest of a subsidiary that does not result in loss of control will be accounted for as an equity transaction. Where change in ownership of interest results in the loss of control of a subsidiary, any retained interest will be re-measured to fair value and will impact gain or loss recognized on disposal. Moreover, any losses incurred by the subsidiary will be allocated between the controlling and non-controlling interests, even if the losses exceed the non-controlling equity investment in the subsidiary. Consequently, the parent will no longer show the excess losses as part of its own equity. The Fund has yet to assess the impact of these amendments on the financial statements.

PFRS 3, *(Revised) Business Combinations* (effective for annual periods beginning on or after July 1, 2009)
The Standard has been revised to include combinations of mutual entities and combinations without considerations. It also introduces a number of changes in accounting for business combinations that will impact the amount of goodwill recognized, the results in the period that an acquisition occurs and future revenues reported. The Fund has yet to assess the impact of these amendments on the financial statements.

Philippine Interpretation IFRIC - 17, *Distribution of Non-cash Assets to Owners*
This Interpretation covers accounting for two types of non-reciprocal distributions of assets by an entity to its owners acting in their capacity as owners. The two types of distribution are:

a. distributions of non-cash assets (e.g., items of property, plant and equipment, businesses as defined in PFRS 3, ownership interests in another entity or disposal groups as defined in PFRS 5); and
b. distributions that give owners a choice of receiving either non-cash assets or a cash alternative.

This Interpretation addresses only the accounting by an entity that makes a non-cash asset distribution. It does not address the accounting by shareholders who receive such a distribution

Philippine Interpretation IFRIC - 18, *Transfers of Assets from Customers*
This Interpretation covers accounting for transfers of items of property, plant and equipment by entities that receive such transfers from their customers. Agreements within the scope of this Interpretation are agreements in which an entity receives from a customer an item of property, plant and equipment that the entity must then use either to connect the customer to a network or to provide the customer with ongoing access to a supply of goods or services, or to do both. This Interpretation also applies to agreements in which an entity receives cash from a customer when that amount of cash must be used only to construct or acquire an item of property, plant and equipment and the entity must then use the item of property, plant and equipment either to connect the customer to a network or to provide the customer with ongoing access to a supply of goods or services, or to do both.

Effective in 2012
Philippine Interpretation IFRIC 15, *Agreement for 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. This 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.

<u>Improvements to PFRSs</u>
In May 2008, the International Accounting Standards Board (IASB) issued its first omnibus of amendments to certain standards, primarily with a view of removing inconsistencies and clarifying wordings. The Fund has not yet adopted the following relevant amendments and anticipates that these changes will have no material effect in the financial statements.

PFRS 5, *Non-current Assets Held for Sale and Discontinued Operations*

- When a subsidiary is held for sale, all of its assets and liabilities will be classified as held for sale under PFRS 5, even when the entity retains a non-controlling interest in the subsidiary after the sale.

PFRS 7, *Financial Instruments: Disclosures*

- Removal of the reference to 'total interest income' as a component of finance costs.

PAS 1, *Presentation of Financial Statements*

- Assets and liabilities classified as held for trading are not automatically classified as current in the statement of assets and liabilities.

PAS 10, *Events after the Reporting Period*

- Clarification that dividends declared after the end of the reporting period are not obligations.

PAS 16, *Property, Plant and Equipment*

- The amendment replaces the term 'net selling price' with 'fair value less costs to sell' to be consistent with PFRS 5, *Non-current Assets Held for Sale and Discontinued Operations*, and PAS 36, *Impairment of Assets*.
- Items of property, plant and equipment held for rental that are routinely sold in the ordinary course of business after rental, are transferred to inventory when rental ceases and they are held for sale. Proceeds of such sales are subsequently shown as revenue. Cash payments on initial recognition of such items, the cash receipts from rents and subsequent sales are all shown as cash flows from operating activities.

PAS 18, *Revenue*

- Replacement of the term 'direct costs' with 'transaction costs' as defined in PAS 39.

PAS 19, *Employee Benefits*

- Revises the definition of 'past service costs' to include reductions in benefits related to past services ('negative past service costs') and to exclude reductions in benefits related to future services that arise from plan amendments. Amendments to plans that result in a reduction in benefits related to future services are accounted for as curtailment.

- Revises the definition of 'return on plan assets' to exclude plan administration costs if they have already been included in the actuarial assumptions used to measure the defined benefit obligation.
- Revises the definition of 'short-term' and 'other long-term' employee benefits to focus on the point in time at which the liability is due to be settled.
- Deletes the reference to the recognition of contingent liabilities to ensure consistency with PAS 37, *Provisions, Contingent Liabilities and Contingent Assets*.

PAS 23, *Borrowing Costs*

- Revises the definition of borrowing costs to consolidate the types of items that are considered components of 'borrowing costs', i.e., components of the interest expense calculated using the effective interest rate method.

PAS 28, *Investment in Associates*

- If an associate is accounted for at fair value in accordance with PAS 39, only the requirement of PAS 28 to disclose the nature and extent of any significant restrictions on the ability of the associate to transfer funds to the entity in the form of cash or repayment of loans applies.
- An investment in an associate is a single asset for the purpose of conducting the impairment test. Therefore, any impairment test is not separately allocated to the goodwill included in the investment balance.

PAS 36, *Impairment of Assets*

- When discounted cash flows are used to estimate 'fair value less cost to sell' additional disclosure is required about the discount rate, consistent with disclosures required when the discounted cash flows are used to estimate 'value in use'.

PAS 38, *Intangible Assets*

- Expenditure on advertising and promotional activities is recognized as an expense when the Group either has the right to access the goods or has received the services. Advertising and promotional activities now specifically include mail order catalogues.
- Deletes references to there being rarely, if ever, persuasive evidence to support an amortization method for finite life intangible assets that results in a lower amount of accumulated amortization than under the straight-line method, thereby effectively allowing the use of the unit of production method.

PAS 39, *Financial Instruments: Recognition and Measurement*

- Changes in circumstances relating to derivatives - specifically derivatives designated or de-designated as hedging instruments after initial recognition - are not reclassifications.
- When financial assets are reclassified as a result of an insurance Fund changing its accounting policy in accordance with paragraph 45 of PFRS 4, *Insurance Contracts*, this is a change in circumstance, not a reclassification.

- Removes the reference to a 'segment' when determining whether an instrument qualifies as a hedge.
- Requires use of the revised effective interest rate (rather than the original effective interest rate) when re-measuring a debt instrument on the cessation of fair value hedge accounting.

PAS 40, *Investment Properties*

- Revises the scope (and the scope of PAS 16, *Property, Plant and Equipment*) to include property that is being constructed or developed for future use as an investment property. Where an entity is unable to determine the fair value of an investment property under construction, but expects to be able to determine its fair value on completion, the investment under construction will be measured at cost until such time as fair value can be determined or construction is complete.

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. Future events may occur which will 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. Functional Currency

The Fund has determined that its functional currency is Philippine Peso. The Philippine Peso is the currency of the primary economic environment in which the Fund operates. It is the currency that mainly influences the operating income and expense of providing the services.

b. Fair Value of Financial Instruments

Where the fair values of financial assets and liabilities recorded in the statement of assets and liabilities cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The input to these models is taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values. The judgments include considerations of liquidity and model inputs such as correlation and volatility for longer dated financial instruments.

Estimates

a. Impairment of AFS Investments

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

4. Cash and Cash Equivalents

This account consists of:

	2008	2007
Cash in banks	**₱312,685**	₱117,123
Short-term deposits	**1,304,231**	11,273,047
	₱1,616,916	₱11,390,170

Cash in banks earn interest at the respective bank deposit rates. Short-term deposits 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.

As of December 31, 2008, 2007 and 2006, interest income earned on short-term deposits and cash in banks amounted to ₱3.8 million, ₱0.7, and ₱0.8 million, respectively.

5. Financial Assets at Fair Value Through Profit of Loss

This account consists of:

	2008	2007
Investments in:		
Government and corporate debts		
Corporate bonds	**₱75,396,115**	₱85,109,834
Treasury notes	**50,166,067**	72,244,143
Treasury bonds	**–**	5,501,679
Preferred shares of stock	**15,011,465**	15,002,325
	₱140,573,647	₱177,857,981

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.

Investments in government and corporate debts and preferred shares are designated as 'Financial assets at FVPL' and are carried at fair values. The Fund incurred gain (loss) on market valuation on these investments amounting ₱0.2 million and ₱0.7 million in 2008 and 2007, respectively.

As of December 31, 2008, 2007 and 2006, interest income earned on government and corporate debts amounted to ₱10.6 million, ₱11.3 million and ₱15.2, respectively.

6. Receivables

This account consists of:

	2008	2007
Notes receivable	**₱4,000,000**	₱4,000,000
Interest receivable	**1,890,945**	2,856,025
Dividend receivable	**77,227**	58,454
Other receivable	**789,047**	–
	₱6,757,219	₱6,914,479

Notes receivable relates to a short-term loan granted to A-1 Financial Services, Inc. which bear interest of 20%, for a period of one year. In 2008, these loans are renewed until November 2009. Total interest income recognized in relation to the loan amounted to ₱0.6 million in 2008 and 2007.

7. Net Assets Attributable to Unitholders and Capital Management

The details and movements of this account are as follows:

	2008	2007	2006
Capital stock - ₱1 par value			
Authorized	**₱100,000,000**	100,000,000	₱100,000,000
Issued:			
Balance at the beginning of the year	**90,065,250**	92,892,492	98,667,242
Issuances	**95,273,968**	1,980,744	58,520,937
Redemptions	**(118,604,035)**	(4,807,986)	(64,295,687)
Balance at the end of the year	**66,735,183**	90,065,250	92,892,492
Additional paid-in capital:			
Balance at beginning of year	**65,366,964**	67,107,274	59,498,605
Issuance in excess of par value	**111,650,873**	2,203,476	56,506,471
Redemptions	**(135,273,303)**	(3,943,786)	(48,897,802)
Balance at the end of the year	**41,744,534**	65,366,964	67,107,274
Retained earnings:			
Balance at the beginning of the year	**40,678,364**	31,454,113	18,477,700
Increase in net assets from operations attributable to unitholders	**5,276,121**	10,539,803	30,502,674
Excess of the redemption cost over the original selling price	**(5,596,927)**	(1,315,552)	(17,526,261)
Balance at the end of the year	**40,357,558**	40,678,364	31,454,113
	₱148,837,275	₱196,110,578	₱191,453,879

Movements of number of shares are as follows:

	2008	2007	2006
Authorized - ₱1 par value	**₱100,000,000**	₱100,000,000	₱100,000,000
Issued:			
Balance at beginning of year	**90,065,250**	92,892,492	98,667,242
Issuances	**95,273,968**	1,980,744	58,520,937
Redemptions	**(118,604,035)**	(4,807,986)	(64,295,687)
Balance at end of year	**₱66,735,183**	₱90,065,250	₱92,892,492

As an open-end mutual fund Fund, the Fund stands ready at any time to redeem the outstanding capital stock at NAV per share.

NAV per share is computed as follows:

	2008	2007	2006
Net assets attributable to unitholders	**₱148,837,275**	₱196,110,578	₱191,453,879
Number of shares outstanding	**66,735,183**	90,065,250	92,892,492
NAV per share	**₱2.230**	₱2.177	₱2.061

Capital Management
The primary objective of the Fund's capital management is to ensure that the return objectives stated in its prospectus are achieved. Due to the Fund's nature as an open-end mutual fund 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 investors or 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. As a mutual fund, the Fund stands ready to redeem shares from shareholders at any time upon the request of the latter at the prevailing NAV per share of the Fund. As discussed in Note 10, the investment restrictions stated in Note 10, as mandated by the SEC and the Investment Fund Act are the main limitations which the Fund must adhere to in investing the capital provided by various shareholders. Moreover, the Investment Fund Act states that "investment companies are allowed to borrow or incur debt provided that there is at all times a 300% asset coverage for all its borrowings. In the event that the asset coverage falls below 300%, the investment Fund has three days within which to reduce its debt to bring the asset coverage back to at least 300%."

As of December 31, 2008 and 2007, the Fund does not have any outstanding debt. 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: date of transaction +3days
b) Redemptions from shareholders: maximum date of transaction +7 days, as prescribed by the Investment Fund Act Rule 35-1

8. Income Tax

Republic Act No. 9337, *An Act Amending National Internal Revenue Code*, provides that the RCIT rate shall be 35.00% until December 31, 2008. Starting January 1, 2009, the RCIT rate shall be 30.00%.

The regulations also impose the MCIT of 2% on modified gross income and allow a NOLCO. The NOLCO and the excess of the MCIT over the RCIT may be applied against taxable income and the income tax liability, respectively, over a three year period from the year of inception.

The Fund did not recognize deferred tax asset on NOLCO amounting to ₱0.2 million and ₱0.4 million as of December 31, 2008 and 2007, respectively. Management believes that these deductible temporary differences cannot be utilized against taxable income before their expiration.

The balance of NOLCO as of December 31, 2008 and 2007 may be used by the Fund as additional deduction against future taxable income. The balances of NOLCO, with their corresponding expiry dates, are as follows:

Year Incurred	Amount	Expired	Balance	Expiry Year
2006	₱591,839	₱–	₱591,839	2009
2007	573,326	–	573,326	2010
2008	651,488	–	651,488	2011
	₱1,816,653	₱–	₱1,816,653	

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 statement of income is summarized as follows:

	2008	2007	2006
Income tax at statutory tax rate	**₱1,846,642**	₱3,688,931	₱10,675,936
Tax effects of:			
Interest income subjected to final tax	**(4,688,144)**	(4,427,542)	(5,602,836)
Realized loss on sale of debt instruments exempt from tax	**3,037,124**	548,077	(3,058,730)
Dividend income exempt from tax	**(352,192)**	(302,897)	(406,667)
Change in unrecognized deferred tax assets	**195,447**	200,664	207,144
Loss (gain) on change in fair value of financial assets at FVPL	**(71,451)**	249,978	(1,814,847)
Effect of change in tax rate	**32,574**		
Nondeductible expense	**–**	42,789	–
	₱–	₱–	₱–

9. **Related Party Disclosures**

Parties are considered to be related if one party has the ability to 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.

As of December 31, 2008 and 2007, seven shares of the Fund are held by directors. The Fund has an existing agreement with Philequity Management, Inc. (PMI), one of the subsidiaries of the iVantage Corporation, a listed Fund who has a major investment in the Fund. Pursuant to the terms of the agreement, the Fund pays the following for services rendered by PMI:

a. Annual management fee of a maximum of 1.5% of the monthly average NAV of the Fund's assets. The NAV shall be determined in accordance with the procedures agreed upon by both parties. As of December 31, 2008 and 2007, the payment of management fee has not yet been made effective by the Fund and PMI.

b. Sales commission of a maximum of 3.5% of the cost of investment for every sale of the Fund's shares of stock. Sales commission amounted to ₱63,037 and ₱25,915 in 2008 and 2007, respectively, are included in 'Other expenses' in the statement of income.

The Fund has no key management personnel. The key management functions are being handled by PMI, at no cost to the Fund.

10. Financial Risk Management Objectives and Policies

The Fund's principal financial instruments comprised of cash and cash equivalents, financial assets through FVPL 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 interest and dividend receivables and accrued expenses and other liabilities, which arise directly from its operations.

Governance Framework

The Fund has established a risk management function 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, limit structure to ensure the appropriate quality and diversification of assets to the corporate goals and specify reporting requirements.

Regulatory Framework

The operations of the Fund are also subject to the regulatory requirements of the SEC. Such regulations not only prescribe approval and monitoring of activities but also impose certain restrictive provisions (e.g. investment portfolios, capital requirements, etc.).

Financial Risk

The Fund is exposed to financial risk through its financial assets and liabilities. The most important components of this financial risk are credit risk, liquidity risk, and market risk. The BOD reviews and approves policies for managing these risks and they 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.

The Fund manages the level of credit risk it accepts through a comprehensive credit risk policy setting out the assessment and determination of what constitutes credit risk for the Fund; setting up of exposure limits by each counterparty or group of counterparties, geographical and industry segments; right of offset where counterparties are both debtors and creditors; guidelines on obtaining collateral and guarantees; reporting of credit risk exposures and breaches to the monitoring authority; monitoring compliance with credit risk policy and review of credit risk policy for pertinence and changing environment.

The Fund further restricts its credit risk exposure by entering into master netting arrangements with counterparties with which it transacts significant volumes of transactions. Although, such arrangements do not generally result in offset of assets and liabilities, as transactions are usually settled on gross basis. However, the credit risk associated with such balances is reduced in the event of a default, when such balances are settled on a net basis. The situation may however change substantially within a short period following the date of the statement of assets and liabilities because the exposure is affected by transactions subject to the arrangement.

In respect of investment securities, if any, the Fund secures satisfactory credit quality by setting maximum limits of portfolio securities with a single or group of issuers. The Fund also transacts only with institutions with high credit worthiness.

The Fund sets the maximum amounts and limits that may be advanced to or placed with individual corporate counterparties, which are set by reference to their long-term ratings.

The following table provides information regarding the gross maximum exposure to credit risk exposure of the Fund as of December 31, 2008 and 2007, without considering the effects of collaterals and other credit risk mitigation techniques:

	2008	2007
Financial assets at FVPL		
Government and corporate debts		
Corporate bonds	**₱75,396,115**	₱85,109,834
Treasury notes	**50,166,067**	72,244,143
Treasury bonds	**–**	5,501,679
Preferred shares of stock	**15,011,465**	15,002,325
Loans and receivables		
Cash and cash equivalents	**1,616,916**	11,390,170
Receivables		
Notes receivable	**4,000,000**	4,000,000
Interest receivable	**1,890,945**	2,856,025
Dividends receivable	**77,227**	58,454
Other receivable	**789,047**	–
	₱148,947,782	₱196,162,630

As of December 31, 2008 and 2007, these financial assets are viewed by management as high grade considering the collectibility of the receivables and the credit history of the counterparties. There are no past due or impaired financial assets as of December 31, 2008 and 2007.

The Fund has no significant credit concentration risk with a single counterparty or group of counterparties, geographical and industry segments as of December 31, 2008 and 2007.

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; or counterparty failing on repayment of a contractual obligation; or inability to generate cash inflows as anticipated.

The Fund is exposed to daily cash redemptions of redeemable participating shares. It therefore invests the majority of its assets in investments that are traded in an active market and can be readily disposed of; it invests only a limited proportion of its assets in investments not actively traded on a stock exchange. The Fund is exposed to the risk of being unable to meet its payment obligations to redeeming shareholders when they fall under normal and stress circumstances.

To limit this risk, the Fund strictly complies with Investment Fund Act Rule 35-1 (Rule) which requires all Investment Companies/Mutual Funds to invest at least 10% of its net assets in liquid assets. This Rule defines such assets as (a) treasury notes or bills, certificates of indebtedness issued by the Bangko Sentral ng Pilipinas 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, 2008 and 2007 and their respective percentages to total net assets of the Fund:

	2008	2007
Investments in corporate bonds	50.66%	43.40%
Treasury notes	33.71	9.88
Preferred shares	10.09	7.65
Cash and cash equivalents	1.09	5.81
Treasury bonds	–	29.77
Notes receivable	2.69	2.04
Total investments	98.24%	98.55%

The table below analyzes financial assets and liabilities of the Fund into their relevant maturity groups based on the remaining period at the date of statement of assets and liabilities to their contractual maturities.

	2008			
	Up to a Year	**2–5 Years**	**Over 5 Years**	**Total**
Financial Assets				
Financial assets at FVPL				
Government and corporate bonds				
Corporate bonds	**₱–**	**₱75,396,115**	**₱–**	**₱75,396,115**
Treasury notes	**50,166,067**	–	–	**50,166,067**
Treasury bonds	–	–	–	**-**
Preferred shares	**15,011,465**	–	–	**15,011,465**
Loans and receivables				
Cash and cash equivalents	**1,616,916**	–	–	**1,616,916**
Receivables				
Notes receivable	**4,000,000**	–	–	**4,000,000**
Interest receivable	**1,890,945**	–	–	**1,890,945**
Dividend receivable	**77,227**	–	–	**77,227**
Other receivable	**789,047**	–	–	**789,047**
	₱73,551,667	**₱75,396,115**	**₱–**	**₱148,947,782**
Financial liabilities				
Financial liabilities at amortized cost -				
Accrued expenses and other				
current liabilities	**₱110,507**	**₱–**	**₱–**	**₱110,507**

	2007			
	Up to a Year	2-5 Years	Over 5 Years	Total
Financial Assets				
Financial assets at FVPL				
Government and corporate bonds				
Corporate bonds	₱–	₱85,109,835	₱–	₱85,109,835
Treasury notes	–	13,685,375	58,378,768	72,244,143
Treasury bonds	–	5,501,679	–	5,501,768
Preferred shares	–	15,002,325	–	15,002,325
Loans and receivables				
Cash and cash equivalents	₱11,390,170	₱–	₱–	₱11,390,170
Receivable				
Notes receivable	4,000,000	–	–	4,000,000
Interest receivable	2,856,025	–	–	2,856,025
Dividend receivable	58,454	–	–	58,454
Other receivable	–	–	–	–
Total financial assets	₱18,304,649	₱119,299,214	₱58,378,768	₱196,162,720
Financial liabilities				
Financial liabilities at amortized cost -				
Accrued expenses and other				
current liabilities	₱52,052	₱–	₱–	₱52,052

It is unusual for a Fund to predict the requirements of funding with absolute certainty as theory of probability is applied on contracts to ascertain the likely provision and the time period when such liabilities will require settlement. The amounts and maturities in respect of liabilities are thus based on management's best estimate based on statistical techniques and past experience.

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). As an illustration, when the country's general political and economic situations are perceived to be in turmoil, the stock market, in general, experience lack of trading interest that will consequently result in thin volume trading and narrow price volatility. Such situations generally will trigger a downward momentum for both the stock prices and trading volumes until the political and economic condition normalize. As a consequence, these instances can result to the redemption prices of redeemed shares being less than the prices at which the shares were originally purchased. Investors who redeem their shares during this time may not recover the full cost of their investments.

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 off-set 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 effectivity 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, 2008 and 2007, as measured by its annualized daily standard deviation is lower than the volatility of the said Index:

Volatility of investment portfolio	**2008**	2007
PMMF (the Fund)	**0.02%**	2.8%
HSBC Local Bond Index	**6.94%**	3.3%

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 notes 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.

- *Fair Value Interest Rate Risk*
  Fair value interest rate risk is the risk that the value of financial instruments will fluctuate because of changes in market interest rates. The Fund's fixed rate investments are exposed to such risk.

  The following table shows the information relating to the Fund's exposure to fair value interest rate risk as of December 31, 2008:

	Weighted Average Rate	**Up to a Year**	**2–5 Years**	**Over 5 Years**	**Total**
Government and corporate bonds					
Corporate bonds	**7.00**	**₱–**	**₱75,396,115**	**₱–**	**₱75,396,115**
Treasury notes	**6.00**	**50,166,067**	**–**	**–**	**50,166,067**
Preferred shares	**6.95**	**15,011,465**			**15,011,465**

  The following table shows the information relating to the Fund's exposure to fair value interest rate risk as of December 31, 2007:

	Weighted Average Rate	**Up to a Year**	**2–5 Years**	**Over 5 Years**	**Total**
Government and corporate bonds					
Corporate bonds	7.54	₱–	₱85,109,835	₱–	₱85,109,835
Treasury notes	6.63	–	13,865,374	58,378,769	72,244,143
Treasury bonds	6.13	–	5,501,679	–	5,501,679
Preferred shares	5,44		15,002,325	–	15,002,325

- *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.

  The following table shows the information relating to the Fund's exposure to cash flow interest rate risk as of December 31, 2008 and 2007:

	2008				2007			
	Up to a Year	**2–5 Years**	**Over 5 Years**	**Total**	Up to a Year	2–5 Years	Over 5 Years	Total
Notes receivable	**₱4,000,000**	**–**	**–**	**₱4,000,000**	₱4,000,000	–	–	₱4,000,000
Cash and cash equivalents	**1,304,231**	**–**	**–**	**1,304,231**	11,273,047	–	–	11,273,047

The sensitivity to a reasonably possible change in market interest rates of the Fund's profit before tax is approximated via the modified duration formula. Standard analysis of measurable change assumes a ±100 basis point movement in yields in 2008 and 2007. The following table demonstrates the sensitivity to a reasonably possible change in interest rates for the year ended December 31, 2008 and 2007, with all other variables held constant, of the Fund's income before income tax.

2008		2007	
Change in Price	**Effect on Income Before Income Tax**	Change in Price	Effect on Income Before Income Tax
+0.88%	**₱1,304,304**	+3.21%	₱6,291,417
–0.88%	**(1,304,304)**	–3.21%	(6,291,417)

There is no other impact on the Fund's net assets attributable to unitholders other than those already affecting income before income tax.

11. **Fair Value of Financial Instruments**

Set out below is a comparison by category of carrying amounts and fair values of the Fund's financial assets and liabilities that are carried in the financial statements as of December 31, 2008 and 2007:

	2008		2007	
	Carrying Value	**Fair Value**	Carrying Value	Fair Value
Financial Assets				
Financial assets at FVPL				
Government and corporate bonds				
Corporate bonds	**₱75,396,115**	**₱75,396,115**	₱85,109,834	₱85,109,834
Treasury notes	**50,166,067**	**50,166,067**	72,244,143	72,244,143
Treasury bonds	–	–	5,501,679	5,501,679
Preferred shares	**15,011,465**	**15,011,465**	15,002,325	15,002,325
Total financial assets at FVPL	**140,573,647**	**140,573,647**	177,857,981	177,857,981
Loans and receivables:				
Cash and cash equivalents	**1,616,916**	**1,616,916**	11,390,170	11,390,170
Notes receivable	**4,000,000**	**4,000,000**	4,000,000	4,000,000
Interest and dividend receivables	**2,757,219**	**2,757,219**	2,914,479	2,914,479
	8,374,135	**8,374,135**	18,304,649	18,304,649
	₱148,947,782	**₱148,947,782**	₱196,162,630	₱196,162,630
Financial Liabilities				
Financial liabilities at amortized cost				
Accrued expenses and other liabilities	**₱110,507**	**₱110,507**	₱52,052	₱52,052

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

Financial assets at FVPL
Fair values are generally based on quoted market prices. If market prices are not readily available or if the securities are not traded in an active market, fair values are estimated using either values obtained from independent parties offering pricing services or adjusted quoted market prices of comparable investments or using the discounted cash flow methodology.

Cash and cash equivalents, interest and dividend receivables, notes receivable and accrued expenses and other liabilities
Due to the short-term nature of the instrument, the fair value approximates the carrying value.