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| | Month | | | |
|--------------------------------|------------|------------------------|---------------------|--------------------|
| | Period End | Average ⁽¹⁾ | High ⁽²⁾ | Low ⁽³⁾ |
| 2012 | | | | |
| September | Php41.74 | Php41.73 | Php41.45 | Php42.03 |
| October | 41.21 | 41.43 | 41.21 | 41.82 |
| November | 40.89 | 41.11 | 40.88 | 41.32 |
| December | 41.08 | 41.02 | 40.86 | 41.19 |
| 2013 | | | | |
| January | 40.67 | 40.71 | 40.57 | 40.90 |
| February | 40.66 | 40.67 | 40.60 | 40.74 |
| March (through March 22, 2013) | 40.82 | 40.70 | 40.59 | 40.82 |

Source: Philippine Dealing System Reference Rate

⁽¹⁾ Calculated by using the average of the exchange rates during the month.

⁽²⁾ Highest exchange rate for the month.

⁽³⁾ Lowest exchange rate for the month.

This report contains conversions of Philippine peso amounts into U.S. dollars for your convenience. Unless otherwise specified, these conversions were made at the Philippine Dealing System Reference Rate as at December 31, 2012 of Php41.08 to US\$1.00. You should not assume that such Philippine peso amounts represent such U.S. dollar amounts or could have been or could be converted into U.S. dollars at the rate indicated, or at any particular rate. As at March 22, 2013, the exchange rate quoted through the Philippine Dealing System was Php40.82 to US\$1.00. Unless otherwise specified, the weighted average exchange rate of the Philippine peso to the U.S. dollar for a given year used in the following discussions in this report was calculated using the average of the daily exchange rates quoted through the Philippine Dealing System during the year.

Capitalization and Indebtedness

Not applicable.

Reasons for the Offer and Use of Proceeds

Not applicable.

Risk Factors

You should carefully consider all of the information in this annual report, including the risks and uncertainties described below. If any of the following risks actually occurs, it could have a material adverse effect on our business, financial condition or results of operations and the trading price of our ADSs could decline and you could lose all or part of your investment.

Risks Relating to Us

We face competition from well-established telecommunications operators and may face competition from new entrants, which may have a material adverse effect on our business, results of operations, financial condition and prospects.

In 1993, the Philippine government liberalized the Philippine telecommunications industry and opened the Philippine telecommunications market to new entrants. At present, following the acquisition of the Digitel Group by PLDT, the number of major players in the industry has been reduced to three major LECs, 8 international gateway facility, or IGF, providers and two major cellular operators in the country. Many entrants into the Philippine telecommunications market have entered into strategic alliances with foreign telecommunications companies, which provide them access to technology and funding support, as well as service innovations and marketing strategies. We cannot assure you that the number of providers of telecommunications services will not increase in the future or that competition for customers will not cause our cellular and fixed line subscribers to switch to other operators, or otherwise cause us to increase our marketing expenditures or reduce our rates, resulting in a reduction in our profitability.

Competition in the cellular telecommunications industry is particularly intense, with network coverage, quality of service, product offerings, and price dictating subscriber preference. Recently, operators have grown more

aggressive in maintaining and growing market share, especially in light of a maturing market. Our principal cellular competitor, Globe, has introduced aggressive marketing campaigns and promotions, such as unlimited voice and SMS offers. In the same way, Smart and DMPI are also continuously innovating their product and conducting promotions, which may affect its cellular revenue growth. Specifically, in response to the unlimited voice and text offers by Globe, Smart introduced promotions allowing Smart and *Talk 'N Text* subscribers to avail of unlimited on-network (Smart-to-Smart) voice calls or unlimited on-network (Smart-to-Smart) text messages at a fixed rate. DMPI, on the other hand, strengthened its unlimited plans through improved handset bundle offerings. Due to competition from other well-established telecommunications operators, we cannot assure you that the additional marketing expenses incurred by us for these promotions, nor can we assure you that, in response to rate pressures from our competitors, the potential loss of customers, decrease in rates or the increase in capital expenditures required for our continued capacity expansion necessary to accommodate the continued increases expected in call and text volumes as a result of unlimited voice and text offers, will not have a material adverse effect on our business, results of operations, financial condition and prospects.

The cellular telecommunications industry may not continue to grow.

The majority of our total revenues are currently derived from the provision of cellular services to customers in the Philippines. As a result, we depend on the continued development and growth of this industry. The cellular penetration rate in the country, however, has already reached an estimated 105%, counting for multiple SIM card ownership, thus the industry may well be considered mature. Further growth of the market depends on many factors beyond our control, including the continued introduction of new and enhanced cellular devices, the price levels of cellular handsets, consumer tastes and preferences and amount of disposable income of existing and potential subscribers. Any economic, technological or other developments resulting in a reduction in demand for cellular services or otherwise cause Philippine cellular telecommunications industry to stop growing or reduce the rate of its growth, could materially harm our business and prospects.

Our results of operations have been, and may continue to be, adversely affected by competition in, and the introduction of new services, which could put additional pressures on the traditional international and national long distance services.

The international long distance business has historically been one of our major sources of revenue. However, due to competition, the steep decline in international settlement rates that are paid to us by foreign telecommunications carriers for termination of international calls on our network, and the growing popularity of the so-called “over-the-top” service providers that offer social networking, instant messaging and VoIP services, revenues generated from our international long distance business have declined in recent years.

Revenues from international long distance services could continue to decline in the future for a variety of reasons, such as:

- increases in competition from other domestic and international telecommunications providers;
- advances in technology;
- the growing popularity of alternative providers offering “over-the-top” services like social networking, instant messaging, internet telephony, also known as VoIP services; or
- alternative providers of broadband capacity.

The continued high cellular penetration in the Philippines and the prevalence of SMS have negatively impacted our national long distance business in recent years. Moreover, net settlement payments between PLDT and other foreign telecommunications carriers for origination and termination of international call traffic between the Philippines and other countries, which have been our predominant source of foreign currency revenues, have been declining in recent years. A continued decline in our foreign currency revenues could increase our exposure to risks from any possible future declines in the value of the Philippine peso against the U.S. dollar. As a result, we cannot assure you that we will be able to adequately increase our other revenues to make up for any adverse impact of a further decline in our net settlement payments. We cannot assure you that we can generate new revenue streams to fully offset the declines in our traditional fixed line long distance businesses, thus, our revenues and profitability could be materially reduced and our growth and prospects could suffer.

Our business is significantly affected by governmental laws and regulations, including regulations in respect of our franchises, rates and taxes, and laws relating to anti-competitive practices and monopoly.

We operate our business under franchises, each of which is subject to amendment, termination or repeal by the Philippine Congress. Additionally, PLDT operates pursuant to various provisional authorities and CPCNs, which have been granted by the NTC and will expire between now and 2028. See Item 4. "Information on the Company - Licenses and Regulations" for a description of our licenses. Some of PLDT's CPCNs and provisional authorities have already expired. However, PLDT filed applications for extension of these CPCNs and provisional authorities prior to their respective expiration dates and is therefore entitled to continue to conduct its business under its existing CPCNs and provisional authorities pending the NTC's decisions on these applications. Because PLDT filed the applications for extension on a timely basis, we expect that these applications will be granted. However, we cannot assure you that the NTC will grant these applications. Smart also operates its cellular, international long distance, national long distance and global mobile personal communications via satellite services as well as international private leased circuits pursuant to CPCNs, which will expire upon the expiration of its franchise. Smart's franchise is due to expire on March 27, 2017, 25 years after the date on which its current franchise was granted. DMPI's CPCN to operate and maintain a nationwide CMTS is for a period coterminous with the life of its existing franchise which is valid until December 11, 2027, 25 years after the date of its issuance.

The NTC also regulates the rates we are permitted to charge for services that have not yet been deregulated, such as local exchange services. We cannot assure you that the NTC will not impose additional obligations on us that could lead to the revocation of our licenses if not adhered to and/or to the reduction in our total revenues or profitability. In addition, the NTC could adopt changes to the regulations governing our interconnection with other telecommunications companies or the rates and terms upon which we provide services to our customers. The occurrence of any of which could materially reduce our revenues and profitability.

The PLDT Group is also subject to a number of national and local taxes. We cannot assure you that the PLDT Group will not be subject to new and/or additional taxes and that the PLDT Group would be able to impose additional charges or fees on its customers to compensate for the imposition of such taxes. There are bills in the 15th Philippine Congress that propose to tax telecommunications services. HB No. 138 proposes to impose a 7% Computer Education Tax on receipts from cellular phone calls to be borne by cellular phone companies that will be used in the creation of a special computer literacy education fund for public schools. HB Nos. 1030 and 1279 propose to require cellular phone companies to set up local assembly and packaging plants for the manufacture of cellular phone units to give the government, by way of appropriate tax schemes, a share in the profits derived from the business. For more details on relevant proposed regulations affecting our business, see Item 4. "Information on the Company - Licenses and Regulations - Material Effects of Regulation on our Business". If any of these bills are enacted into law, such legislation could materially reduce our profitability and have a material adverse effect on our results of operations and financial condition. We cannot assure you that the PLDT Group will be able to impose additional charges or fees on its customers to compensate for the imposition of such taxes or charges, or for the loss of fees and/or charges.

Moreover, as one of the leading telecommunications service providers in the Philippines for fixed line, cellular and broadband services, we are subject to laws and regulations relating to anti-competitive practices and anti-monopoly. For example, Section 700 of NTC Memorandum Circular No. 8-9-95 requires us to seek the approval of the NTC with respect to rates of non-deregulated services in order to ensure that a healthy competitive environment is fostered within the industry. Also, Article II, Section 4 (g) of Republic Act, or R.A., No. 7925 makes it the policy of the government to pursue a fair and reasonable interconnection of authorized public network operators and other providers of telecommunications services in order to achieve a viable, efficient, reliable and universal telecommunications services. The executive branch of the government has also exhibited strong interest in enforcing anti-competitive and anti-monopolistic measures with the signing by the President of the Philippines of Executive Order, or E.O., No. 45 on June 9, 2011. E.O. No. 45 designated the Department of Justice, or the DOJ, as the Competition Authority and established the Office for Competition under it, to among others, investigate violations of competition laws and prosecute violators thereof. The DOJ's Department Circular No. 11 implementing E.O. No. 45 took effect on March 1, 2013. While our business practices have not in the past been found to have violated any laws and regulations related to anti-competition and anti-monopoly, we cannot assure you that the relevant governmental regulators will not, in the future, find our business practices to have an anti-competitive effect on the Philippines telecommunications industry, nor can we assure you that we will not be found to have violated the relevant laws and regulations relating to anti-competition and anti-monopoly in the future. For example, prior to the acquisition of the Digitel Group, there were four major LECs (PLDT, Digitel, Innove and BayanTel) and three cellular service providers (Smart, DMPI and Globe) in the Philippines. On October 26, 2011, we completed the acquisition of the

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Digitel Group, the operator of *Sun Cellular*, one of the two other major cellular service providers in the Philippines. As a result of the acquisition, the number of LECs and cellular service providers in the Philippines was reduced to three and two, respectively, leaving Globe as our sole major competitor in the cellular service market. In order to mitigate the apparent anti-competitive effect of the acquisition, we agreed, as part of the NTC's decision to grant its consent for the acquisition, to divest ourselves of the frequency spectrum and associated licenses held by CURE, one of Smart's subsidiaries. Any future expansion in our services, particularly in our cellular services, could subject us to additional conditions in the granting of our provisional authorities by the NTC and to increased regulatory scrutiny, which could harm our reputation and business, and which could have a material adverse effect on our growth and prospects. In addition, the occurrence of any such event could impose substantial costs or cause interruptions or considerable delays in the provision, development or expansion of our services. Delay or failure to receive any required franchises, licenses or regulatory approvals could result in the suspension of our services or abandonment of any planned expansions, thereby affecting our business, results of operations, financial condition and prospects.

The NTC may implement proposed changes in existing regulations and introduce new regulations, which may result in increased competition and/or changes in rates, each of which could have a material adverse effect on our revenues and profitability.

The NTC may regulate the rates and manner in which we operate and charge our customers. Examples of recent regulatory action affecting our business are provided below.

On July 23, 2009 the NTC issued Memorandum Circular No. 05-07-2009 mandating cellular operators, including Smart and DMPI, to bill subscribers on a maximum six-second per pulse basis instead of the previous per minute basis. The NTC granted Smart and DMPI the provisional authority to charge new rates for the CMTS service and also directed Smart and DMPI to implement a six-second per pulse billing scheme on December 5, 2009. The implementation of this billing scheme is now pending with the Philippine Supreme Court after Smart and CURE filed their petitions for review of the decision of the Court of Appeals on March 15, 2012 and March 12, 2012, respectively.

On October 24, 2011, the NTC issued Memorandum Circular No. 02-10-2011 directing the reduction of interconnection charges for SMS between two separate networks from Php0.35 to Php0.15 per SMS. The NTC has interpreted this circular to require a reduction in SMS charges charged to end users. Therefore, it initiated administrative cases against the mobile operators for the latter's failure to implement reduced SMS charges.

The NTC may call on carriers, other industry players and the public in general to public hearings with respect to certain proposed regulations affecting the industry in general or solicit comments from said parties with respect to consultative documents issued by the NTC on major industry issues, like the August 2006 significant market power, or SMP, obligations, which were revived again during the pendency of PLDT's acquisition of the Digitel Group in 2011. Under the said consultative documents, for example, certain obligations are proposed to be imposed on carriers with SMP by using a roadmap which consists of the following critical processes: (1) defining markets to be used as basis for regulatory intervention; (2) determining if one or several operators in the defined markets have the degree of market power that merit regulatory intervention; (3) identifying appropriate SMP obligations to achieve policy objectives; and (4) determining conditions that justify withdrawal of regulation.

On July 15, 2011, the NTC issued Memorandum Circular No. 7-7-2011 which required broadband service providers to specify the minimum broadband/internet connection speed and service reliability and the service rates in advertisements, flyers, brochures and service agreements. The said Memorandum Circular also set the minimum service reliability of broadband service to 80%.

On December 19, 2011, the NTC issued a Decision in NTC ADM Case 2009-048 which lowered the interconnection charge to/from LEC and to/from CMTS to Php2.50 per minute, from Php4.00 per minute for LEC to CMTS and Php3.00 per minute from CMTS to LEC, making it in parity with each other. PLDT and Smart separately filed their respective Motions for Reconsideration alleging among others that interconnection, including the rates thereof, should be by law a product of bilateral negotiations between the parties and the Decision is unconstitutional as it is an invalid exercise by the NTC of its quasi-legislative powers and violates the constitutional guarantee against non-impairment of contracts.

A summary of the existing material regulations on our business is set forth in Item 4. “- Information on the Company - Material Effects of Regulation on our Business”. Due to the regulatory power of the NTC, as described above, we cannot assure you that the NTC will not impose changes to the current regulatory framework in the future, which could lead to increased competition or negatively affect the rates we can charge for our services. Any of these events could have a material adverse effect on our business, results of operations and prospects.

The franchise of Smart and DMPI may be revoked due to their failure to conduct a public offering of their shares.

In order to diversify the ownership base of public utilities, the Public Telecommunications Policy Act of the Philippines, or R.A. 7925, requires a telecommunications entity with regulated types of services to make a public offering through the stock exchanges, representing at least 30% of its aggregate common shares within a period of five years from: (a) the date the law first becomes effective; or (b) the entity’s first start of commercial operations, whichever date is later. As of the latest practicable date, Smart and DMPI have yet to conduct a public offering of their shares. Consequently, the Philippine Congress may revoke the franchise of Smart and DMPI for their failure to comply with the requirement under R.A. 7925 on the public offering of their shares. A *quo warranto* case may also be filed against Smart and DMPI by the Office of the Solicitor General of the Philippines for the revocation of the respective franchises of Smart and DMPI on the ground of violation of R.A. 7925.

Although the position taken by Smart and DMPI is that such provision is merely directory and that the policy underlying the requirement for telecommunication entities to conduct a public offering should be deemed to have been achieved when PLDT acquired a 100% equity interest in Smart in 2000 and Digitel, which is now majority-owned by PLDT, owned 100% equity interest in DMPI, since PLDT was then and continues to be a publicly listed company, there can be no assurance that the Philippine Congress will agree with such position. In September 2004, Senate Bill No. 1675 was filed seeking to declare that a telecommunications entity shall be deemed to have complied with the requirement of making a public offering of its shares if two-thirds of its outstanding voting stock are owned and controlled directly or indirectly, by a listed company. However, we cannot assure you that such bill will be enacted or that the Philippine Congress will not revoke the franchise of Smart and DMPI or the Office of Solicitor General of the Philippines will not initiate a *quo warranto* proceeding against Smart and DMPI for the revocation of their respective franchises for failure to comply with the provision under R.A. 7925 on the public offering of shares, the occurrence of any of which could have a material adverse effect on our business, results of operations, financial condition and prospects.

If we fail to effect the divestment of CURE in accordance with the terms of, or in a manner contemplated under the NTC’s approval of our acquisition of the Digitel Group, the NTC may revoke its approval of any relevant franchises, licenses or permits held by Smart, any of which could significantly disrupt our operations and have a material adverse effect on our business, results of operations, financial condition and prospects.

As part of the NTC’s decision to grant its consent to our acquisition of the Digitel Group, we agreed to divest ourselves of the frequency spectrum and associated franchises, licenses and permits held by CURE. Under the terms of the order issued by the NTC on October 26, 2011, (i) CURE must sell its *Red Mobile* business to Smart; and (ii) Smart will sell all of its rights and interests in CURE whose remaining assets will consist of its congressional franchise, certain frequency spectrum and related permits. For a detailed description of the divestment of CURE, see Item 4. “Information on the Company - Development Activities (2010-2012) - Divestment of CURE.”

In compliance with the commitments in the divestment plan, CURE completed the sale and transfer of its *Red Mobile* business to Smart on June 30, 2012 for a total consideration of Php18 million through a series of transactions, such that, except for assets necessary to pay off obligations due after June 30, 2012 and certain tax assets, CURE’s only remaining assets as at June 30, 2012 were its congressional franchise, the 10 MHz of 3G frequency in the 2100 band and related permits.

In a letter dated September 10, 2012, Smart informed the NTC that the minimum cost recovery amount, or CRA, to enable the PLDT Group to recover its investment in CURE, includes, among others, the total cost of equity investments in CURE, advances from Smart for operating requirements, and advances from stockholders and associated funding costs. Smart also informed the NTC that the divestment will be undertaken through an auction sale of CURE’s shares of stock to the winning bidder and submitted CURE’s audited financial statements as at June 30, 2012 to the NTC. See *Note 2 - Summary of Significant Accounting Policies - Divestment of CURE* and *Note 13 - Business Combinations and Acquisition of Noncontrolling Interests - Digitel’s Acquisition* to the accompanying audited consolidated financial statements in Item 18 for further discussion.

However, we cannot assure you that we will be able to effect the divestment of CURE within the time or in a manner contemplated under the order issued by the NTC. If we fail to effect the divestment of CURE in accordance with the terms of, or in a manner contemplated under the NTC's approval of our acquisition of the Digitel Group, the NTC may revoke its approval or any relevant franchises, licenses or permits held by Smart, any of which could significantly disrupt our operations and have a material adverse effect on our business, results of operations, financial condition and prospects.

Rapid changes in telecommunications technology may adversely affect the economics of our existing businesses and the value of our assets, increase our required capital expenditures and create new competition.

The global telecommunications industry has been characterized by rapid technological changes, and the Philippine market is not an exception. We cannot assure you that these developments will not result in competition from providers of new telecommunications services or the need to make substantial capital expenditures to transform our existing network infrastructure. Furthermore, the NTC has issued to Smart and our competitors licenses covering 3G cellular services, for which we have made significant investments in the rolling-out of these services. We are also continuing to upgrade our fixed-line network to a next generation, all-IP network and rolling out a wireless broadband network in order to expand our capability to provide broadband services, as well as upgrade and modernize our wireless cellular network in order to achieve greater operating and cost-efficiencies. However, these projects require and will continue to require significant capital expenditures over the next few years.

In addition, we now face growing competition not just from other telecommunications operators, but also from the so-called "over-the-top" service providers that offer social networking, instant messaging and VoIP services.

Our future success will depend on our ability to anticipate and adapt to these changes and to offer services that meet demands of our customers on a competitive and timely basis. However, we may be unable to obtain new technologies on a timely basis or on satisfactory terms or implement them in an appropriate or effective manner. Future development of new technologies, services or standards could require significant changes to our business model, negatively impact our existing businesses or necessitate new investments. In addition, new products and services may be expensive to develop and may result in increased competition. Such strategic initiatives and technological developments could require us to incur significant additional capital expenditures. As a result, we cannot assure you that we would be able to adopt or successfully implement new technologies, nor can we assure you that future technological changes will not adversely affect our operations or the competitiveness of our services.

We may not be successful in our acquisitions of, and investments in, other companies and businesses, and may therefore be unable to fully implement our business strategy.

As part of our growth strategy and as growth slows or reverses in our traditional fixed line and cellular businesses, we make acquisitions and investments in companies or businesses to enter new businesses or defend our existing markets. Since 2010, we have made a number of significant acquisitions, investments in businesses within and ancillary to the telecommunications sector, including an investment in shares of Meralco through PCEV in 2010, the acquisition of the Digitel Group in 2011 and an investment in PDRs of MediaQuest, the ultimate parent company of Signal TV, a direct-to-home pay-TV business, in 2012 and other smaller investments in various businesses. These acquisitions and investments are further discussed in Item 4. "Information on the Company - Development Activities (2010-2012)". The success of our acquisitions and investments depends on a number of factors, such as:

- our ability to identify suitable opportunities for investment or acquisition;
- our ability to reach an acquisition or investment agreement on terms that are satisfactory to us or at all;
- the extent to which we are able to exercise control over the acquired company;
- the economic, business or other strategic objectives and goals of the acquired company compared to those of the PLDT Group, as well as the ability to execute the identified strategies in order to generate fair returns on the investment; and
- our ability to successfully integrate the acquired company or business with our existing businesses.

Any of our contemplated acquisitions and investments may not be consummated due to reasons or factors beyond our control. Even if any contemplated acquisitions and investments are consummated, we may not be able to realize any or all of the anticipated benefits of such acquisitions and investments and we cannot assure you that the consummation of such acquisitions and investments will not result in losses for us for a prolonged period of time. Moreover, if we are unsuccessful in our contemplated acquisitions and investments, we may not be able to fully implement our business strategy to maintain or grow certain of our businesses and our results of operations and financial position could be materially and adversely affected.

If we are unable to install and maintain telecommunications facilities and equipment in a timely manner, we may not be able to maintain our current market share and the quality of our services, which could have a material adverse effect on our results of operations and financial condition.

Our business requires the regular installation of new, and the maintenance of existing, telecommunications transmission and other facilities and equipment, which are being undertaken. The installation and maintenance of these facilities and equipment are subject to a number of risks and uncertainties, such as:

- shortages of equipment, materials and labor;
- work stoppages and labor disputes;
- interruptions resulting from inclement weather and other natural disasters;
- unforeseen engineering, environmental and geological problems; and
- unanticipated cost increases.

Any of these factors could give rise to delays or cost overruns in the installation of new facilities or equipment or could prevent us from properly maintaining the equipment used in our networks, and hence could affect our ability to maintain existing services and roll-out new services, for example, which could have a material adverse effect on our results of operations and financial condition.

Our businesses depend on the reliability of our network infrastructure which is subject to physical, technological and other risks.

We depend, to a significant degree, on an uninterrupted operation of our network to provide our services. We also depend on robust information technology systems to enable us to conduct our operations. The development and operation of telecommunications networks are subject to physical, technological and other risks, which may cause interruptions in service or reduced capacity for customers. These risks include but not limited to:

- physical damage;
- power loss;
- capacity limitation;
- cable theft;
- software defects; and
- breaches of security by computer viruses, break-ins or otherwise.

The occurrence of any of these risks could have a material adverse effect on our ability to provide services to customers. While we are undertaking initiatives to prevent and/or mitigate the occurrence of said risks, including the preparation of a disaster recovery plan that aims to allow restoration of service at the earliest possible time from occurrence of an incident, there can be no assurance that these risks will not occur or that our initiatives will be effective should such risks occur.

We are exposed to cybersecurity risks, which may include the gaining of unauthorized access, data corruption, possible theft of intellectual property, stakeholder information or other sensitive data, the occurrence of any of which could significantly disrupt our business and have a material adverse effect on our results of operations and stakeholder confidence.

Over the years, our continued dependence on the latest digital technologies in conducting our operations exposes our business to risks associated with cyber incidents. These cyber incidents may range from unintentional events to deliberate attacks. These may be carried out by parties with the intention to bring about something as simple as plain disruption of our operations to something as destructive as breaching our network security. To date, we have not been subject to cyber attacks or other cyber incidents which, individually or in the aggregate, resulted in material impact on our operations or financial condition. However, some network attacks can cause our telecommunications services of internal systems to be unavailable. Others can disrupt our business communication, such as SPAM. Moreover, others can cause the disclosure of confidential information, such as brute force attack.

In order to minimize our exposure to cybersecurity risks, we have deployed a multi-layered defense from the network to the host and up to the application level, so that if one defensive measure fails, there are other defensive measures which will continue to provide protection. However, we cannot assure you that any of such defenses will be effective against or neutralize the effects of any cyber incidents resulting from unintentional cyber security breaches or deliberate attacks on our network infrastructure or computer systems, nor can we assure you that our business will not be significantly disrupted in the event of such security breach or attack. If we fail to timely and effectively prevent the occurrence of any such cybersecurity incidents, or fail to promptly rectify any such incidents, our business could be significantly disrupted, our results of operations could be materially and adversely affected, and the confidence of our stakeholders could be lost.

Our businesses require substantial capital investment, which we may not be able to finance.

Our projects under development and the continued maintenance and improvement of our networks and services, including Smart's projects, networks, platforms and services, require substantial ongoing capital investment. Our consolidated capital expenditures totaled Php36,396 million and Php31,207 million in 2012 and 2011, respectively. Our 2013 budget for consolidated capital expenditures is approximately Php29 billion, of which approximately Php13 billion is budgeted to be spent by Smart, approximately Php12 billion is budgeted to be spent by PLDT, approximately Php3 billion is budgeted to be spent by Digitel, and the balance represents the budgeted capital spending of our other subsidiaries. PLDT's capital spending is intended principally to finance the continued build-out and upgrade of its broadband data and IP infrastructures and for its fixed line data services and the maintenance of its network. Smart's capital spending is focused on building out its coverage, leveraging the capabilities of its newly modernized network, expanding its transmission network, increasing international bandwidth capacity and expanding its 3G and wireless broadband networks in order to enhance its data /broadband capabilities. Smart is also enhancing its network and platforms infrastructure and systems to support solutions deployment, campaign analytics and service delivery platform to enable customized and targeted services. Digitel's capital spending is intended principally to finance its mainstream services and integration with the PLDT Group network of its core and transmission network to increase penetration, particularly in provincial areas to achieve greater business benefits from a closely synergized environment.

Future strategic initiatives could require us to incur significant additional capital expenditures. We may be required to finance a portion of our future capital expenditures from external financing sources, which have not yet been fully arranged. There can be no assurance that financing for new projects will be available on terms acceptable to us, or at all. If we cannot complete our development programs or other capital projects on time due to our failure to obtain the required financing, our growth, results of operations, financial condition and prospects could be materially and adversely affected.

Our debt instruments contain restrictive covenants which require us to maintain certain financial tests and our indebtedness could impair our ability to fulfill our financial obligations, service our other debt and carry out new financings.

As at December 31, 2012, we had consolidated total indebtedness of Php115,792 million, or US\$2,819 million, and a consolidated ratio of debt to equity of 0.8 times, calculated as total debt on a consolidated basis divided by total equity attributable to equity holders of PLDT. Our existing debt instruments contain covenants which, among other things, require PLDT to maintain certain financial ratios and other financial tests, calculated on the basis of PFRS on a consolidated and non-consolidated basis, and limit our ability to incur indebtedness. For a description of some of these covenants, see Item 5. "Operating and Financial Review and Prospects - Liquidity and Capital Resources - Financing Activities - Debt Covenants."

Our indebtedness and the requirements and limitations imposed by our debt covenants could have important consequences. For example, we may be required to dedicate a substantial portion of our cash flow to payments on our indebtedness, which could reduce the availability of our cash flow to fund working capital, capital expenditures and other general corporate requirements.

The principal factors that can negatively affect our ability to comply with the financial ratios and other financial tests under our debt instruments are depreciation of the Philippine peso relative to the U.S. dollar, poor operating performance of PLDT and our consolidated subsidiaries, impairment or similar charges in respect of investments or other long-lived assets that may be recognized by PLDT and its consolidated subsidiaries, and increases in our interest expenses. Approximately 45% of our total consolidated debts were denominated in foreign currencies as at December 31, 2012, principally in U.S. dollars, many of these financial ratios and other tests are expected to be negatively affected by any weakening of the Philippine peso.

We have maintained compliance with all of our financial ratios and covenants, as measured under PFRS, under our loan agreements and other debt instruments. However, if negative factors adversely affect our financial ratios, we may be unable to maintain compliance with these ratios and covenants or unable to incur new debt. Inability to comply with the financial ratios and covenants or raise new financing could result in a declaration of default and acceleration of maturities of some or all of our indebtedness.

If we are unable to meet our debt service obligations or comply with our debt covenants, we could be forced to restructure or refinance our indebtedness, seek additional equity capital or sell assets. An inability to effect these measures successfully could result in a declaration of default and an acceleration of maturities of some or all of our indebtedness, which could have a material adverse effect on our business, results of operations and financial condition.

Our results of operations and our financial position could be materially and adversely affected if the Philippine peso significantly fluctuates against the U.S. dollar.

A substantial portion of our indebtedness, related interest expenses, our capital expenditures and a portion of our expenses are denominated in U.S. dollars and other foreign currencies, whereas most of our revenues are denominated in Philippine pesos. As at December 31, 2012, approximately 45% of our total consolidated indebtedness was foreign currency-denominated, of which approximately 38% of our total consolidated indebtedness was unhedged.

A depreciation of the Philippine peso against the U.S. dollar would increase the amount of our U.S. dollar-denominated debt obligations and operating and interest expenses in Philippine peso terms. In the event that the Philippine peso depreciates against the U.S. dollar, we may be unable to generate enough funds through operations and other means to offset the resulting increase in our obligations in Philippine peso terms. Moreover, a depreciation of the Philippine peso against the U.S. dollar may result in our recognition of significant foreign exchange losses, which could materially and adversely affect our results of operations. A depreciation of the Philippine peso could also cause us not to be in compliance with the financial covenants imposed on us by our lenders under certain loan agreements and other indebtedness. Further, fluctuations in the Philippine peso value and of interest rates impact the mark-to-market gains/losses of certain of our financial debt instruments, which were designated as non-hedged items.

On the other hand, approximately 27% and 16% of the PLDT Group's consolidated service revenues and expenses, respectively, are either denominated in U.S. dollars and/or are linked to the U.S. dollar. In this respect, an appreciation of the weighted average exchange rate of the Philippine peso against the U.S. dollar decreases our revenues and expenses, and consequently, affects our cash flow from operations in Philippine peso terms.

The Philippine peso has been subject to significant fluctuations in recent years. From 2003 to 2004, the Philippine peso depreciated from a high of Php52.02 on May 8, 2003 to a low of Php56.44 on October 14, 2004. While the Philippine peso appreciated in 2005, 2006 and 2007, it depreciated in 2008 to a low of Php49.98 and closed at Php47.65 as at December 31, 2008. From 2009 to 2012, the Philippine peso appreciated from Php47.26 as at January 5, 2009 to Php41.08 as at December 31, 2012 and a high of Php40.86 on December 5, 2012. However, we cannot assure you that the Philippine peso will not depreciate and be subject to significant fluctuations going forward, due to a range of factors, including:

- political and economic developments affecting the Philippines, including the level of remittances from overseas Filipino workers;

- global economic and financial trends;
- the volatility of regional currencies, particularly the Japanese yen;
- any interest rate increases by the Federal Reserve Bank of the United States; and
- changes in the value of the U.S. dollar relative to Philippine peso, resulting from events such as higher demand for U.S. dollars by both banks and domestic businesses to service their maturing U.S. dollar obligations or foreign exchange traders including banks covering their short U.S. dollar positions, among others.

Our subsidiaries could be limited in their ability to pay dividends to us due to internal cash requirements and their creditors having superior claims over their assets and cash flows, which could materially and adversely affect our financial condition.

A majority of our total revenues and cash flow from operations is derived from our subsidiaries, particularly Smart. Smart has significant internal cash requirements for debt service, capital expenditures and operating expenses and as a result, may be financially unable to pay any dividends to PLDT. Although Smart has been making dividend payments to PLDT regularly since December 2002, there can be no assurance that PLDT will continue to receive these dividends or other distributions, or otherwise be able to derive liquidity from Smart or any other subsidiary or investee in the future.

Creditors of our subsidiaries generally have priority claims over our subsidiaries' assets and cash flows. We and our creditors will effectively be subordinated to the existing and future indebtedness and other liabilities, including trade payables, of our subsidiaries, except that we may be recognized as a creditor with respect to loans we have made to subsidiaries. If we are recognized as a creditor of a subsidiary, our claim will still be subordinated to any indebtedness secured by assets of the subsidiary and any indebtedness of the subsidiary otherwise deemed superior to the indebtedness we hold.

We may have difficulty meeting our debt payment obligations if we do not continue to receive cash dividends from our subsidiaries and our financial condition could be materially and adversely affected as a result.

A significant number of PLDT's shares are held by three shareholders, which may not act in the interests of other shareholders or stakeholders in PLDT.

The First Pacific Group and its Philippine affiliates had beneficial ownership of approximately 26% in PLDT's outstanding common stock as at February 28, 2013, taking into account shares purchased from JG Summit Holdings, or JGSHI, pursuant to an option agreement in connection with the Digital acquisition. See Item 4. "Information on the Company - Historical Background and Development." This is the largest block of PLDT's common stock that is directly or indirectly under common ownership.

Pursuant to publicly available filings made with the PSE, as at February 28, 2013, NTT Communications and NTT DOCOMO together beneficially owned approximately 20% of PLDT's outstanding common stock, taking into account shares purchased from JGSHI pursuant to an option agreement in connection with the Digitel acquisition. See Item 4. "Information on the Company - Historical Background and Development" for further discussion. First Pacific and certain of its affiliates, or the FP Parties, NTT Communications, NTT DOCOMO and PLDT entered into a Cooperation Agreement, dated January 31, 2006, pursuant to which, among other things, certain rights of NTT Communications under the Stock Purchase and Strategic Investment Agreement dated September 28, 1999, or the Strategic Agreement, and the Shareholders Agreement dated March 24, 2000, or the Shareholders Agreement, were extended to NTT DOCOMO. See Item 7. "Major Shareholders and Related Party Transactions" for further details regarding the shareholdings of NTT Communications and NTT DOCOMO in PLDT. As a result of the Cooperation Agreement, NTT Communications and NTT DOCOMO, in coordination with each other, have contractual veto rights over a number of major decisions and transactions that PLDT could make or enter into, including:

- capital expenditures in excess of US\$50 million;
- any investments, if the aggregate amount of all investments for the previous 12 months is greater than US\$25 million in the case of all investments to any existing investees and US\$100 million in the case of all investments to any new or existing investees, determined on a rolling monthly basis;

- any investments in a specific investee, if the cumulative value of all investments made by us in that investee is greater than US\$10 million in the case of an existing investee and US\$50 million in the case of a new investee;
- issuance of common stock or stock that is convertible into common stock;
- new business activities other than those we currently engage in; and
- merger or consolidation.

Moreover, as a result of the Shareholders Agreement, the Cooperation Agreement and their respective stockholdings, the FP Parties and/or, NTT Communications and/or NTT DOCOMO are able to influence our actions and corporate governance, including:

- elections of PLDT's directors; and
- approval of major corporate actions, which require the vote of common stockholders.

Additionally, pursuant to amendments effected by the Cooperation Agreement to the Stock Purchase and Strategic Investment Agreement and the Shareholders Agreement, upon NTT Communications and NTT DOCOMO and their respective subsidiaries owning in the aggregate 20% or more of PLDT's shares of common stock and for as long as they continue to own in the aggregate at least 17.5% of PLDT's shares of common stock then outstanding, NTT DOCOMO has additional rights under the Stock Purchase and Strategic Investment Agreement and Shareholders Agreement, including that:

- NTT DOCOMO is entitled to nominate one additional NTT DOCOMO nominee to the board of directors of each of PLDT and Smart;
- PLDT must consult NTT DOCOMO no later than 30 days prior to the first submission to the board of PLDT or certain of its committees of any proposal of investment in an entity that would primarily engage in a business that would be in direct competition or substantially the same business opportunities, customer base, products or services with business carried on by NTT DOCOMO, or which NTT DOCOMO has announced publicly an intention to carry on;
- PLDT must procure that Smart does not cease to carry on its business, dispose of all of its assets, issue common shares, merge or consolidate, or effect winding up or liquidation without PLDT first consulting with NTT DOCOMO no later than 30 days prior to the first submission to the board of PLDT or Smart, or certain of its committees; and
- PLDT must first consult with NTT DOCOMO no later than 30 days prior to the first submission to the board of PLDT or certain of its committees for the approval of any transfer of Smart's common capital stock by any member of the PLDT Group to any person who is not a member of the PLDT Group.

The FP Parties and/or NTT Communications and/or NTT DOCOMO may exercise their respective influence over these decisions and transactions in a manner that could be contrary to the interests of other shareholders or stakeholders in PLDT.

Failure to maintain effective internal control over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act of 2002 could adversely impact investor confidence and the market price of our common shares and ADSs, and have a material adverse effect on our business, our reputation, financial condition and results of operations.

Effective internal control over financial reporting is necessary for us to provide reasonable assurance with respect to our financial reports and to effectively prevent fraud. If we are unable to provide reasonable assurance with respect to our financial reports and effectively prevent fraud, our reputation and results of operations could be harmed.

We are required to comply with various Philippine and U.S. laws and regulations on internal control. For example, pursuant to Section 404 of the Sarbanes-Oxley Act of 2002, beginning with the Annual Report on

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Form 20-F for the calendar year ended December 31, 2006, we have been required to include a report by our management on our internal control over financial reporting in our Annual Reports on Form 20-F that contains an assessment by our management on the effectiveness of our internal control over financial reporting. In addition, an independent registered public accounting firm must express an opinion on our internal control over financial reporting based on its audits.

However, internal control over financial reporting may not prevent or detect misstatements because of its inherent limitations, including the possibility of human error, the circumvention or overriding of controls, or fraud. Therefore, even effective internal control over financial reporting can provide only reasonable assurance with respect to the preparation and fair presentation of financial statements. If we fail to maintain the adequacy of our internal control over financial reporting, including our failure to implement required new or improved controls, or if we experience difficulties in their implementation, our business and operating results could be harmed, we could fail to meet our reporting obligations and there could be a material adverse effect on our business, our reputation, financial condition and results of operations, and the market prices of our common shares and ADSs could decline significantly.

Risks Relating to the Philippines

PLDT's business may be adversely affected by political or social or economic instability in the Philippines.

The Philippines is subject to political, social and economic volatility that, directly or indirectly, could have a material adverse impact on our ability to sustain our business and growth.

For example, in 2012, the then Chief Justice of the Supreme Court of the Philippines was impeached and the proceedings have raised concerns about the judicial system in the country.

The Philippine economy continues to face several long-term challenges, including reliance on energy imports and foreign demand for overseas Filipino workers.

We cannot assure you that the political environment in the Philippines will be stable or that the current or any future government will adopt economic policies that are conducive to sustained economic growth or which do not impact adversely on the current regulatory environment for the telecommunications and other companies.

If foreign exchange controls were to be imposed, our ability to meet our foreign currency payment obligations could be adversely affected.

The Philippine government has, in the past, instituted restrictions on the conversion of the Philippine peso into foreign currencies and the use of foreign exchange received by Philippine companies to pay foreign currency-denominated obligations. The Monetary Board of the BSP has statutory authority, with the approval of the President of the Philippines, during a foreign exchange crisis or in times of national emergency, to:

- suspend temporarily or restrict sales of foreign exchange;
- require licensing of foreign exchange transactions; or
- require the delivery of foreign exchange to the BSP or its designee banks.

We cannot assure you that foreign exchange controls will not be imposed in the future. If imposed, these restrictions could materially and adversely affect our ability to obtain foreign currency to service our foreign currency obligations.

The occurrence of natural catastrophes could materially disrupt our operations.

The Philippines has experienced a number of major natural catastrophes over the years, including typhoons, floods, volcanic eruptions and earthquakes that may materially disrupt and adversely affect our business operations. The frequency and severity of the occurrence of natural catastrophes and challenges may be further exacerbated through effects of the ongoing global climate change. We cannot assure you that we are fully capable to deal with these situations and that the insurance coverage we maintain will fully compensate us for all the damages and economic losses resulting from these catastrophes.