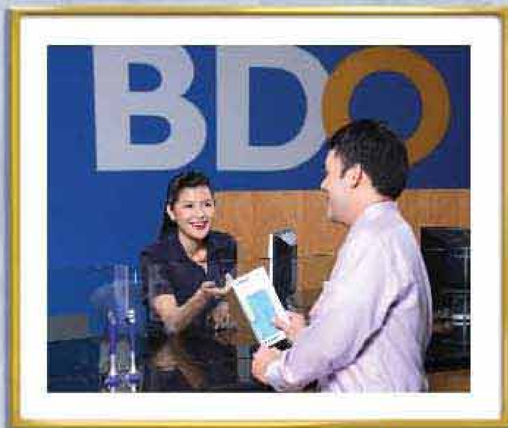
SM INVESTMENTS CORPORATION

www.sminvestments.com

50TH ANNIVERSARY ISSUE

INVESTOR

ANNUAL REPORT 2007



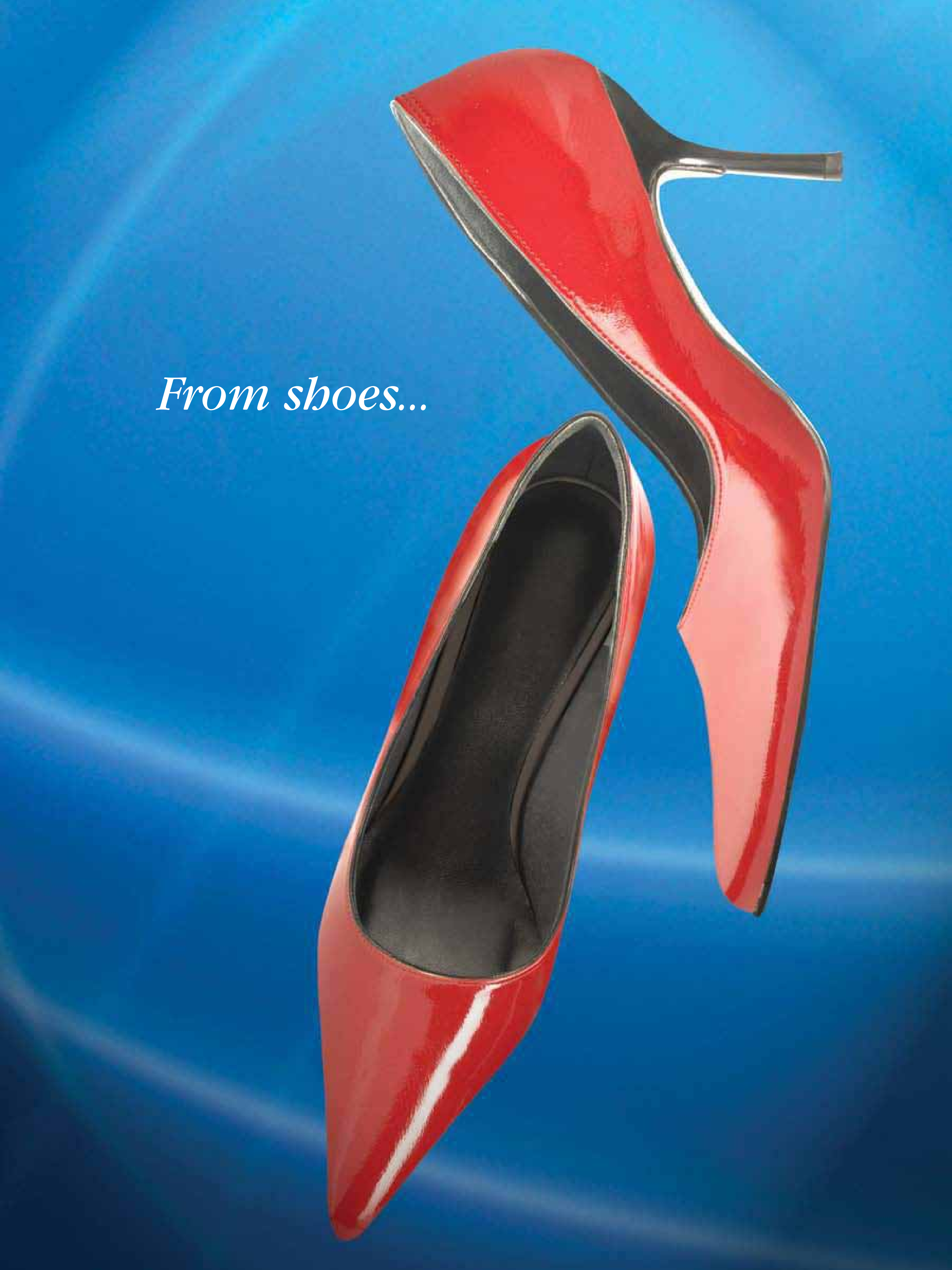
BANKING

MALL OPERATIONS

PROPERTY

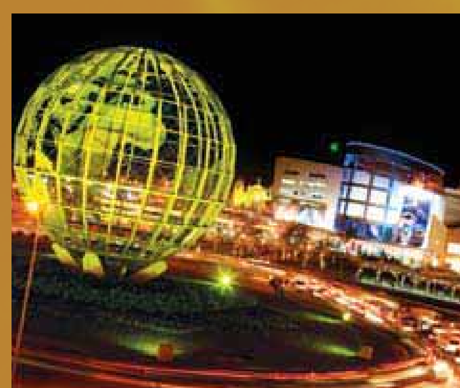
50 Years of Serving Millions

SM celebrating 50 years


From shoes...

...to a diverse range of products and services!

RETAIL
MERCHANDISING



BANKING

MALL
OPERATIONS

RETAIL MERCHANDISING

SM Department Stores (93%)
Super Value, Inc. (100%)
Super Shopping Market, Inc. (100%)
Pilipinas Makro (50%)

MALL OPERATIONS

SM Prime Holdings, Inc. (53%)

BANKING

Banco De Oro Unibank, Inc. (44%)
China Banking Corporation (20%)

** Figures in parenthesis represent SM's effective ownership as of yearend 2007*

PROPERTY

Vision

SM ATTAINS GROWTH IN NEW INITIATIVES THROUGH THOUGHT LEADERSHIP, RISK MANAGEMENT, AND A THOROUGH UNDERSTANDING OF ITS MARKET AND BUSINESS ENVIRONMENT.

Innovation

SM MAINTAINS GROWTH IN ITS ONGOING ENDEAVORS THROUGH STRATEGIC DIFFERENTIATION, OPERATIONAL AGILITY AND PRUDENT INCORPORATION OF ADVANCED TECHNOLOGIES AND METHODOLOGIES.

Value

SM SUSTAINS GROWTH INTO THE FUTURE THROUGH FINANCIAL DISCRETION, METHODICAL EXPANSION, AND A RELATIONSHIP OF RESPONSIBILITY AND INTEGRITY TOWARDS ITS STAKEHOLDERS.

This is SM Investments Corporation.

PROPERTY

Shoemart, Inc. (64.9%)
  Mall of Asia Complex (100%)
SM Development Corporation (59%)
Highlands Prime, Inc. (32%)
Costa Del Hamilo, Inc. (99%)
Taal Vista Hotel (100%)

CELEBRATING 50 YEARS OF SERVING MILLIONS

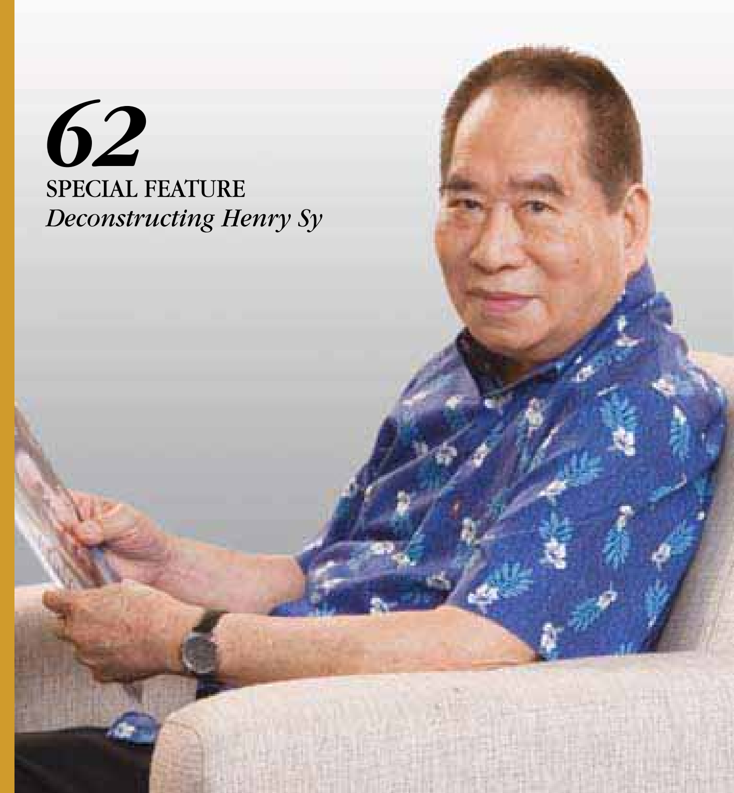
FROM SMALL BEGINNINGS IN 1958 TO ONE OF THE LARGEST IN THE PHILIPPINES, **SHOEMART** THEN, AND **SM** NOW HAS EVOLVED INTO A COMPANY WITH DOMINANT INTERESTS IN RETAILING, MALL OPERATIONS, AND BANKING SERVICES; AND ONE THAT IS FAST EMERGING IN PROPERTY DEVELOPMENT. DIVERSE AS THEY MAY SEEM, **SM** AND ITS SUBSIDIARIES OPERATE AS A HIGHLY SYNERGISTIC GROUP BOUND BY THE VISION AND PROGRESSIVE BUSINESS ACUMEN OF ITS FOUNDER, MR. HENRY SY, SR.

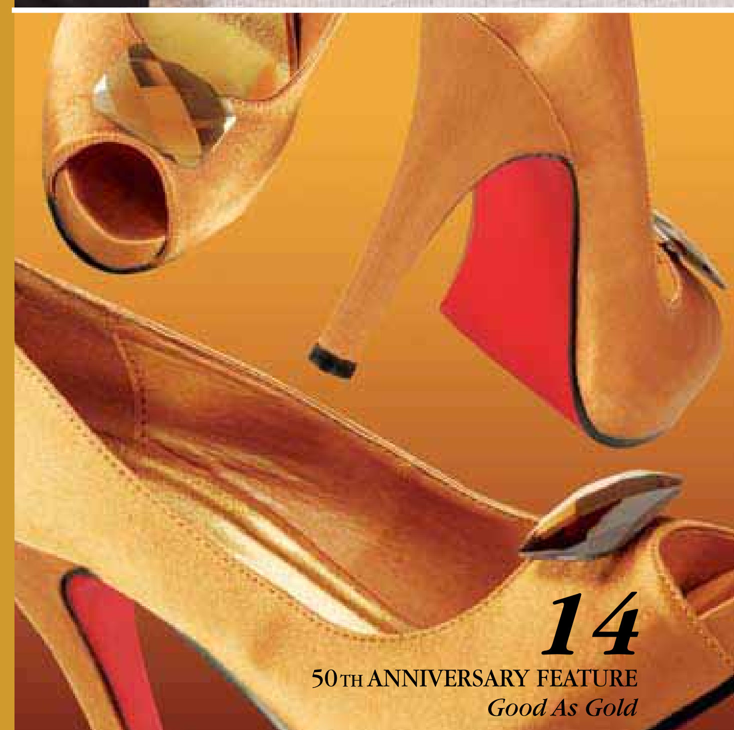
OVER THE LAST FIFTY YEARS, **SM** HAS BUILT A STRONG NAME AND REPUTATION THAT HAS SPREAD ACROSS THE COUNTRY AND PERHAPS, EVEN ACROSS THE GLOBE WITH THE MILLIONS OF FILIPINOS IT HAS SERVED. TO THESE MILLIONS, **SM** HAS BECOME AN ICON OF GROWTH, OF INNOVATION, AND OF COMMITMENT TO VALUE CREATION. IT HAS BECOME A NAME THAT FILIPINOS CAN BE PROUD OF.

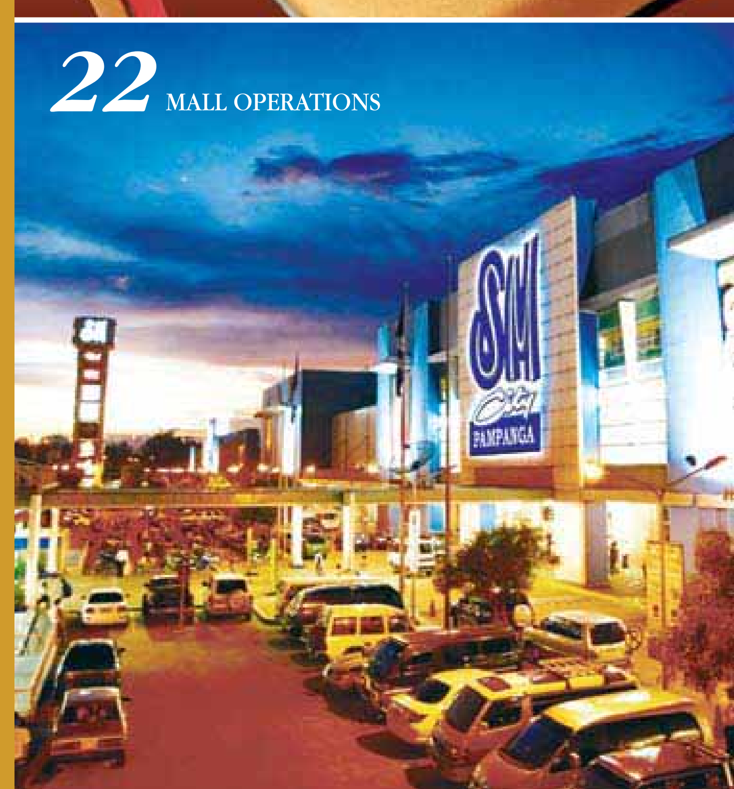
50TH ANNIVERSARY ISSUE INVESTOR

About the Cover

AS SM CELEBRATES ITS 50TH ANNIVERSARY,
we honor the man who started it all, Mr. Henry Sy, Sr. —a man who dared to dream big, even as a child who migrated from Jinjiang, China. He made his dreams become a reality in the Philippines where he spent most of his life growing up, facing many challenges, building a family and building SM, from a small shoe business known then as Shoemart. Mr. Sy continues to dream. He now shares his vision with his family and together, they take SM to a new level of growth and progress. Dominant in three core businesses, namely retailing, mall operations and banking, SM goes all out into property development to harness the value of its existing assets and to further contribute to nation building in areas such as residential, commercial, tourism and hotel investment.





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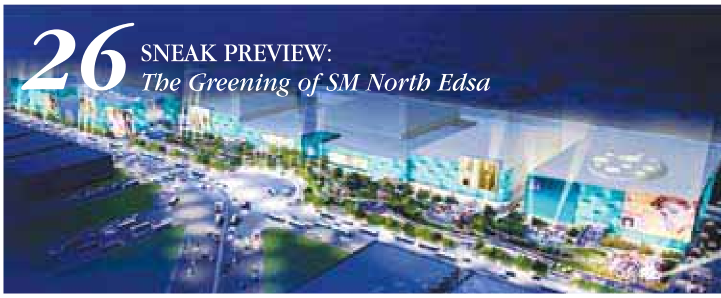
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Message To Stockholders

TO OUR FELLOW STOCKHOLDERS

TODAY, SM STANDS PROUDLY AS ONE OF THE LARGEST HOLDING COMPANIES IN THE PHILIPPINES, WITH BUSINESS INTERESTS IN RETAIL, MALL OPERATIONS, BANKING AND REAL ESTATE DEVELOPMENT THAT OFFER A DIVERSE RANGE OF PRODUCTS AND SERVICES.

ON THE EVE OF SM'S 50TH YEAR IN BUSINESS WE LOOK BACK TO WHERE WE STARTED IN 1958 FROM A SHOE STORE OPERATION IN MANILA. Drawing from the strength of a vision to sell a pair of shoes to every Filipino, Shoemart became a byword until our stores, which had been selling much more than just shoes in the Seventies, came to be known as SM.

Today, SM stands proudly as one of the largest holding companies in the Philippines, with business interests in retail, mall operations, banking and real estate development that offer a diverse range of products and services. Taking stock of what SM has accomplished over the last fifty years and how SM has touched the lives of millions, we come to the realization that what had been a dream is now pleasantly fulfilled.

It comes as no surprise that SM means many things to different sectors of Philippine society:

To many Filipino families, SM malls are a place to spend precious family time, shopping, dining, and finding good entertainment, all in the pleasurable comfort of well-planned and well-designed buildings and shops.

To the tens of thousands of our employees, SM is a conducive workplace to learn, earn, develop a diverse range of jobs and careers, and build a global network of professionals. As of end 2007, SM's employees numbered well over 70,000 nationwide in all of its subsidiaries and affiliates.

To the local communities where our businesses are located, SM continues to be a catalyst for economic growth. It is a significant conduit for trade to flourish, for small and medium-scale enterprises to thrive, for new jobs to be generated, and for property values to rise exponentially.

To local governments, SM plays a major role in enhancing local businesses, and in providing a venue for more taxpayers to prosper.

To the underprivileged sector, SM, through SM Foundation, is a sanctuary offering health and medical assistance, free college education to the least privileged but deserving students, and for many other activities geared to raise their standards of living.

From a business perspective, SM is a company that now generates over ₱122 billion in revenues with assets worth over ₱234 billion, a feat accomplished in just five decades, from an initial investment of only ₱1 million.

SM has become a dominant force today in three of its core businesses. It has the most number of retail branches with 73 stores nationwide; its malls have grown to 30, including three of the largest malls in the world; and its banks are the country's second and ninth largest in terms of resources. Moreover, spanning the years, SM has accumulated a huge landbank—a critical foundation for its strong emergence in the property, tourism, and hotel businesses.

All these were accomplished while SM stayed focused on its vision to give value to all its stakeholders and serve the needs of Filipinos. SM has grown from a foundation of hard work, in unrelenting pursuit of excellence and growth, while overcoming seemingly insurmountable odds along the way.

With a positive and long-term view of Philippine business, your Board and Management will be guided by the same corporate values as we aim to further transform SM into a world-class institution. While adhering to international best practice, SM will continue to focus on satisfying the requirements of its customers, even if it means going the extra mile.

World class also means exploring new horizons and platforms for growth. Toward that objective, SM is venturing into select areas in China for its mall operations through its subsidiary, SM Prime Holdings, Inc.

In celebrating SM's fifty years of dramatic growth, we thank you, our stakeholders, for believing in our vision, and for giving SM your continued firm support. We also thank our officers and employees for helping us carry out our plans with pride, industry, and enthusiasm. We value your partnership which inspires us to aspire for even greater goals in the next fifty years.

HENRY SY, SR.
Chairman

TERESITA SY-COSON
Vice-Chairperson

HENRY SY, JR.
Vice-Chairman

President's Report

Harley Sy at
SM Department Store
Men's Shoes Section

SM INVESTMENTS CORPORATION
HAD ANOTHER GOOD YEAR IN 2007. ALL ITS FOUR CORE BUSINESSES COMPLETED THEIR EXPANSION PLANS AND DELIVERED ENCOURAGING FINANCIAL RESULTS, AMID A STRONGER DOMESTIC ECONOMY.

FOR FULL YEAR 2007, YOUR MANAGEMENT DELIVERED A 14% GROWTH IN NET INCOME TO ₱12.0 BILLION, WITH NET RECURRING INCOME ACTUALLY GROWING BY 25%. THE MAIN GROWTH DRIVERS FOR THE YEAR WERE RETAIL AND PROPERTY, BOTTOMLINES OF WHICH GREW BY 30% AND 88% RESPECTIVELY.

Consolidated revenues increased by 38% to ₱122.5 billion as revenues from the retail businesses expanded by 43%, and rental income from mall operations, expanded by 13%. We also saw ticket sales of cinemas and amusement facilities growing by 13% to ₱2.5 billion. Meanwhile, revenues from real estate operations increased by 142% to ₱3.2 billion.

SM's operating income totaled ₱20.8 billion, rising by 28% and resulting in an operating margin of 17%. EBITDA increased by 28% to ₱25.1 billion, for an EBITDA margin of 20%.

Excluding the banks' revenues, which are not consolidated, the bulk of SM's revenues come from retail merchandising, which accounted for 84%, followed by shopping malls and real estate, which contributed 10% and 3%, respectively.

The picture varies as the banks' earnings are equitized, reflecting the fact that they now contribute the most to the group's net income. Earnings from BDO and China Bank accounted for 31% of net income. They are followed by mall operations with a 30% income contribution, retail with 28% and property with 11%.

The retail group opened a total of 6 stores in 2007. Two of these were SM Department Stores located in Bacolod and Taytay. Another two were SM Hypermarkets inaugurated in Muntinlupa and in Taytay. The last two were SM Supermarkets in Bacolod and in Morong, Rizal with the latter under the Save More brand. These brought the total number of SM retail outlets to 71 as of end 2007.

SM Prime Holdings which runs the SM shopping malls, likewise saw 2007 as a growth year. SM Prime inaugurated three new malls, in Bacolod, in Taytay, and in Muntinlupa. It also expanded an equal number of its existing malls, which are SM City Pampanga, SM City Cebu, and SM Mall of Asia. The latter saw the opening of the Science Discovery Center and Planetarium and a state-of-the-art SM Bowling Center.

Consequently, SM Prime had by yearend 2007 a total of 30 malls nationwide, with a combined gross floor area of 3.9 million square meters, an average occupancy of 96%, and an average pedestrian count of two and a half million daily. All these attest to SM Prime's deeply entrenched position and market leadership in the mall business.

SM's real estate and property group, though comparatively young, exhibited rapid growth and expansion in residential, commercial, tourism, and hotel investments.

SM Development Corporation, SM's main residential arm, rolled out three new residential projects, with two located in Quezon City and the other in Muntinlupa. The units from these projects and the other two launched earlier are selling very well and drawing not just from the name of SM, but more so with the quality of the buildings that are being rolled out by SMDC.

"With the positive developments that SM experienced in 2007, it is with enthusiasm that I look forward to 2008, a milestone year celebrating the 50th founding anniversary of SM."

Mall of Asia Complex, which is SM's main commercial property vehicle, saw the completion of the SMX Convention Center in November 2007. It is now the largest privately owned exhibition and convention center in the country with most of

"I am optimistic that 2008 shall also be an opportunity for further growth and expansion for the SM Group."

its space pre-booked three months ahead. Another major development within the complex, the OneE-comCenter has also been completed and will be occupied by tenants in the first quarter of 2008. OneE-comCenter which is already 90% leased is a building primarily designed for business process outsourcing companies.

Hamilo, SM's doorway into tourism, successfully launched its first project at Pico de Loro Cove in May 2007. Construction of a lagoon, a Beach and Country Club and four condominium buildings are now underway, with club shares and units selling well in the market.

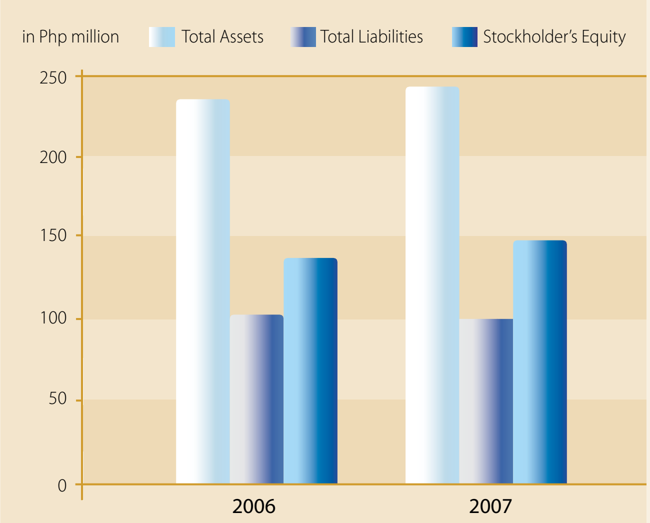
Also last year, the newest leg in the property group which is hotel investments commenced various projects such as the 132-room expansion of the landmark Taal Vista Hotel in Tagaytay City, and the refurbishment of the Sofitel Cebu Hotel.

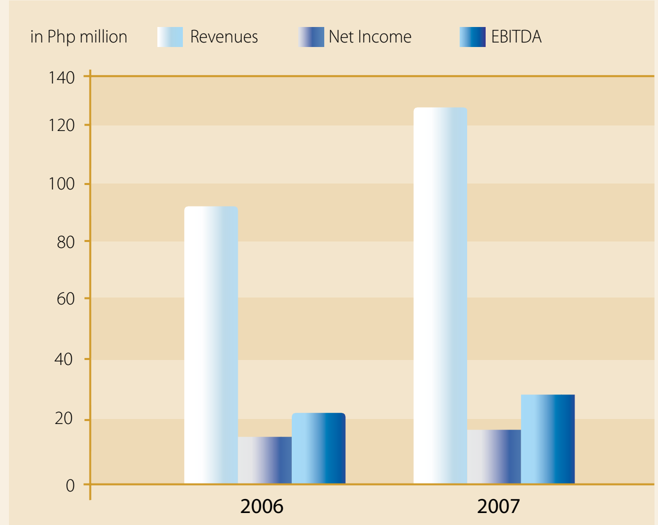
In banking and financial services, Banco De Oro Unibank, Inc. (BDO), the country's second largest bank in terms of assets, forged ahead and kept within its timelines for integrating its operations with those of Equitable PCI Bank. China Banking Corp. (China Bank), on the other hand, acquired Manila Banking Corporation which promises to also increase its number of branches. China Bank maintained its profitability with its well-niched market position.

Other noteworthy finance-related initiatives undertaken by SM in 2007 include the issuance of five-year convertible bonds worth US$300 million and ₱4.5 billion five-year redeemable preferred shares. Both issuances were highly successful resulting in oversubscriptions prompting the company to expand the offer size.

With the positive developments that SM experienced in 2007, it is with enthusiasm that I look forward to 2008, a milestone year celebrating the 50th founding anniversary of SM. As I personally thank all our customers, shareholders, management and employees, tenants and suppliers, and all our other stakeholders for their continued support all throughout 2007, I am optimistic that 2008 shall also be an opportunity for further growth and expansion for the SM Group.

HARLEY T. SY
President



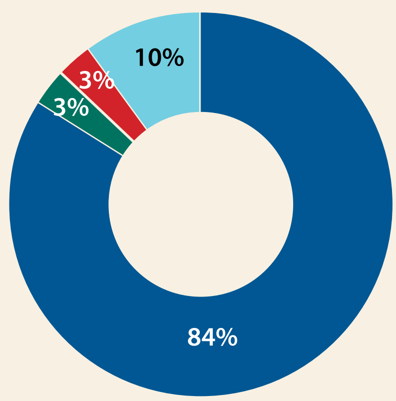


BALANCE SHEET HIGHLIGHTS		
(Php Bn)	Jan - Dec 2007	% Chg
Total Assets	234.5	3.3%
Current Assets	75.7	27.0%
Non-current Assets	158.8	-5.2%
Current Liabilities	38.5	-26.5%
Non-current Liabilities	54.9	25.1%
Total Liabilities	93.4	-2.9%
Stockholder's Equity	141.1	7.8%
Book Value per share (Php)	178.2	5.4%
INCOME STATEMENT HIGHLIGHTS		
(Php Bn) except EPS	Jan - Dec 2007	% Chg
Revenues	122.5	38.1%
Gross Profit	20.8	27.8%
Other Income/(Expenses)	-0.2	-107.6%
Net Profit Before Tax	20.6	9.3%
Net Income	12.0	13.7%
Minority Interest	4.1	-12.2%
Basic EPS (Pesos)	19.67	9.1%
FINANCIAL RATIOS	2007	2006
Current Ratio (x)	1.97:1.00	1.14:1.00
Return on Equity (%)	11.3%	11.6%
Debt/Equity Ratio (%)	30:70	34:66
Net Debt (Php Bn)	22.4	17.7
Net Debt/Equity (%)	17:83	15:85
Revenue Growth (%)	38.1%	64.4%
Net Income Growth (%)	13.7%	31.7
Interest Cover (x)	6.8	4.2
EBITDA (Php Bn)	25.1	19.6
EBITDA Margin (%)	20.5%	22.1%
Net Margin (%)	9.8	12.0%
REVENUE PROFILE*	%	
Shopping Malls	10%	
Real Estate	3%	
Banking, Financial Services	3%	
Retail Merchandising	84%	
INCOME PROFILE	%	
Shopping Malls	30%	
Real Estate	11%	
Banking, Financial Services	31%	
Retail Merchandising	28%	

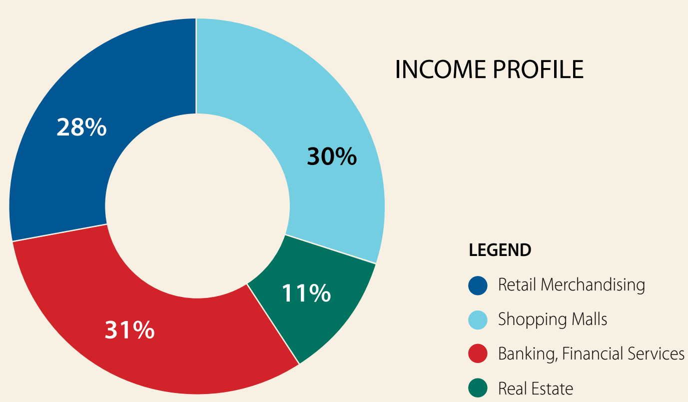
** Revenues from bank affiliates are not consolidated*

SMIC SHARE PRICE CHART (January to December 2007)

REVENUE PROFILE*



INCOME PROFILE



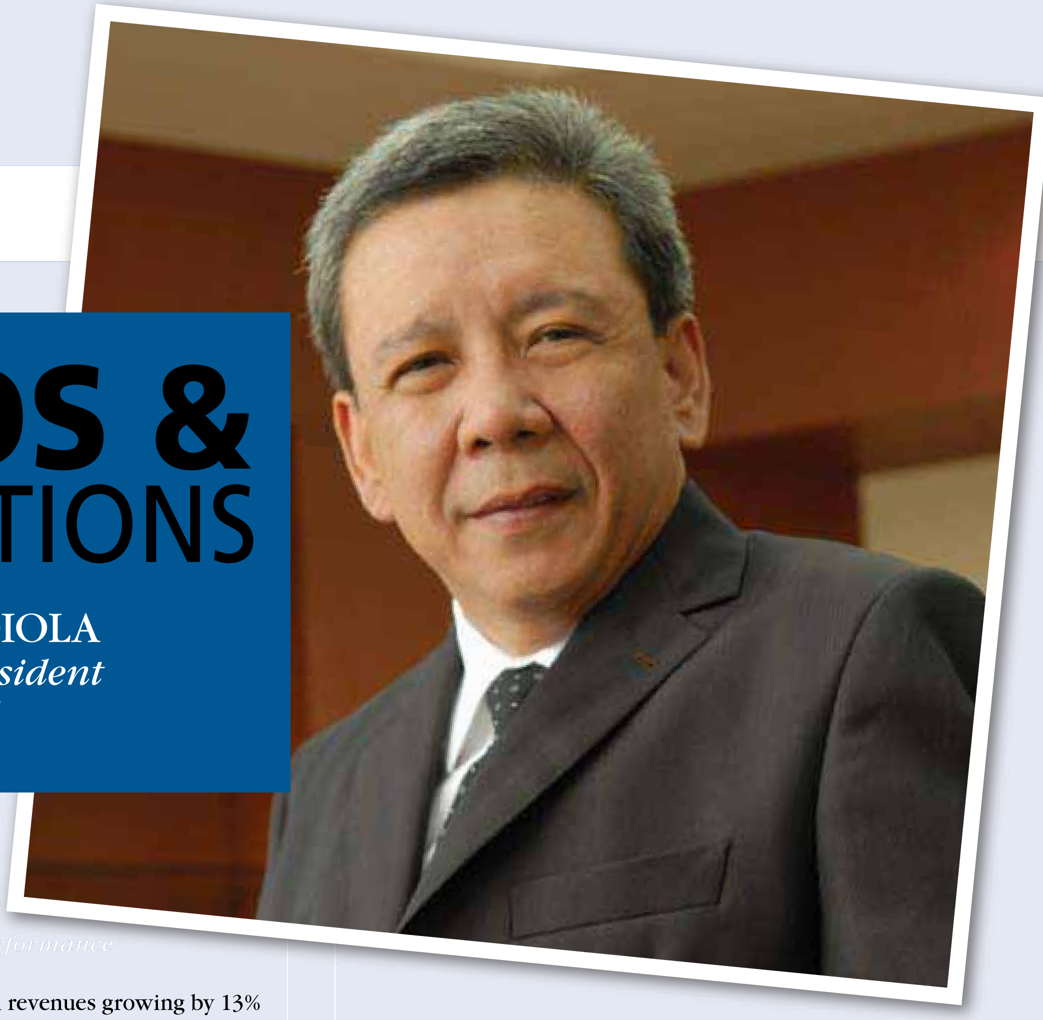
Retail Merchandising

The retail group of SM performed beyond expectations in 2007 growing its profits by 30% to ₱3.3 billion, on the strength of all three store formats. Profits of SM Department Stores increased by 14% to ₱1.3 billion. SM Supermarkets which is operated by Super Value, Inc. saw profits increase by 48% to ₱1.4 billion. SM Hypermarkets, which is under Super Shopping Market, Inc., grew its profits by 38% to ₱0.6 billion. The sector's revenues, on the other hand, increased by 13% to ₱94.1 billion.

The strong profit growth in retail may be attributed to a mix of factors. Average same store sales grew by approximately 4.8%, higher than those of previous years as the many stores that opened in 2006 and 2007 began to mature, coupled with greater efficiencies and economies of scale. It may be recalled that in 2006, the retail group opened a total of 12 stores including large stores in Mall of Asia, and North EDSA thereby increasing selling space by 16.3% during the year. Of the total, four were department stores, four were supermarkets, and four were hypermarkets. In 2007, six stores were opened for an additional 3.4% increase in selling space. Of the total, two were department stores, two were supermarkets, and two were hypermarkets.

In 2008, another 10 stores are expected to open in various parts of the country with three more department stores, five supermarkets and four to five hypermarkets with a planned capital expenditure of ₱1.5 billion.

SM
celebrating 50 years
SM
We've got it all for you!
DEPARTMENT STORE
MAKATI • CUBAO • HARRISON • NORTH EDSA • STA. MESA • ORTIGAS • LAS PIÑAS • BACOOR • FAIRVIEW • SAN LAZARO • MANILA • PAMPANGA • MANDURRIAO • DELGADO • CEBU
DAVAO • CAGAYAN DE ORO • BICUTAN • LUCENA • BAGUIO • MARILAO • DASMARIÑAS • BATANGAS • STA. ROSA • SUCAT • CLARK • MALL OF ASIA • LIPA • BACOLOD • TAYTAY



TRENDS & EXPECTATIONS

JORGE MENDIOLA
Senior Vice President
SM Retail

How would you describe the performance of all SM stores in 2007?
The stores performed very well with revenues growing by 13% to ₱94 billion. Net income increased at a much faster rate of 30% to ₱3.3 billion for a higher net margin of 3.5% from 3% the previous year.

What do you think were the main growth drivers for your improved revenues? Was it driven by the better economy or was it also because of innovation and expansion?
It was both. The economy improved the market's buying capacity. At the same time, we improved on efficiencies, particularly at the back office through shared services in IT, warehousing, and product distribution. These initiatives did wonders in bringing down not just our costs, but also, the cost of our suppliers. In turn, we are able to further enhance supplier relationships.

How much did you expand in 2007 for all three store formats?
We opened two department stores, two hypermarkets and one supermarket.

What innovations did the market see from SM stores?
We continued to focus on improving customer relations by providing more personalized services both at the selling areas and at the counters. We do this by enhancing staff orientation and training.

One of the most visible transformations in SM stores is the look, feel and design of the stores. One could also notice a much more customer friendly environment in all the stores? What is the strategy behind this change?
We want our stores to always look fresh and inviting for our customers. We look after comfort and convenience because we try our best to make shopping a pleasant and memorable experience. In 2007, we introduced a new look for the Megamall department store by engaging the services of a New York-based designer. So far, feedback has been very positive.

For our supermarkets and hypermarkets, we are projecting a friendlier and more uplifting atmosphere. We look at the latest trends in international store layout and design which include color schemes and ambience.

Having started with selling shoes 50 years ago, we are again curious how many pairs of shoes your group sold in 2007?
The department stores sold about 19 million pairs, while the supermarkets and hypermarkets put together sold about 2.7 million pairs of footwear, which include slippers and sandals. That comes to a total of 21.7 million pairs which is equivalent to one pair sold for every four Filipinos. SM continues to be the largest shoe retailer in the country.

What are your growth targets for 2008?
We are bracing ourselves for a more challenging business environment in 2008 given the unabated increase in oil prices, which will inevitably result in higher inflation. There is also the issue of the strong peso which is affecting the Peso incomes of overseas Filipino Workers. We are closely monitoring the domestic consumer situation.

How many stores do you plan to open and where will they be located?
We will continue to expand our number of stores by three for department stores, two to three for hypermarkets and five for supermarkets. The latter will be more aggressive in pursuing stand alone stores in residential communities.

What is your capex plan for 2008? Will the whole amount be internally generated?
We are looking to spend about ₱1.5 billion for expansion. As in the past, the funds will be internally generated.

Good as Gold

ON ITS GOLDEN YEAR, SM LOOKS BACK AT WHAT STARTED IT ALL

SHOES ARE PART OF A PERSON'S BASIC NECESSITIES. But for a person with style, shoes can also become a fashion statement. Here in the Philippines, one man with a steadfast vision capitalized on shoes and started to build his business empire from selling them.

From annual sales of approximately 200,000 pairs of shoes when ShoeMart opened in Carriedo in 1958, the shoe business of SM stores have flourished over the years, having sold 21.7 million pairs of footwear for full year 2007.

We talked to the man behind what was then known as ShoeMart. Mr. Henry Sy, Sr. shares with us how shoes started it all for him and how the SM conglomerate came to be fifty years hence.

Building From A Dream

It all started with a dream. *"When I began selling shoes in Manila right after the Second World War, I thought then that if I sold a pair of shoes to every Filipino, even with very low margins, I would be a successful businessman,"* Mr. Sy said.

In plain and uncluttered logic, yet fraught with business acumen, Mr. Sy encapsulated the vision that drove him to achieve his dreams.

He started to lay the groundwork to turn his dreams into reality by trading shoes that were brought in by American soldiers in the war's aftermath. Filipinos then, devastated by the conflict, were in dire need of basic necessities, with shoes very much included in their list.

His profitable though informal trading of shoes went on until 1948, when he opened a modest, nameless shoe store in Manila's Quiapo district.

Ahead of His Time

The success of his first shoe store enabled him shortly thereafter to open two more outlets together with some business partners. He curiously named his three stores Plaza, Paris, and Park Avenue. At a time when organized retail in the country was still relatively new, Mr. Sy already had notions of brand management.

"I intentionally gave the stores names that started with the letter P. I felt it was a good way for them to be identified and remembered. It was a branding initiative," Mr. Sy disclosed.

MR. SY METICULOUSLY CHOSE THE MOST ATTRACTIVE SALESLADIES AND PERSONALLY TRAINED THEM TO BE ATTENTIVE TO THE NEEDS OF EACH AND EVERY CUSTOMER.

SHOEMART ANNOUNCEMENT OF MAKATI STORE OPENING

Innovations Paid Off

His innovative ideas paid off. Within a decade, in 1958, he consolidated his holdings in the three shoe stores and instead set up a bigger, better footwear retail outlet with a single partner, and aptly named it ShoeMart.

"It was again part of my desire to innovate and bring about change. I felt that the name ShoeMart, would right away be associated with footwear, and would therefore attract a lot of buyers," Mr. Sy added.

"We all got very excited when ShoeMart opened. Many famous people in Manila came to visit the store including the likes of Isabel Preysler and Jacob Zobel. We sold ₱5,000 worth of shoes that day when shoes would cost an average of only ₱4.50 to ₱4.75 each," says Mr. Sy's eldest daughter and SM Vice Chairperson Mrs. Teresita Sy-Coson. *"Back then, my Dad, was very hands on in choosing the type and styles of the shoes that would be sold in the store,"* she added.

The name change was just a start of several other effective innovations.

Mr. Sy said, *"When I put up ShoeMart, I noticed that buyers would always bargain and ask for discounts. At times, they would even walk out of the door irritated if they didn't get the discount they wanted, in the hope that we would go after them and give the price they wanted.*

"I felt that this whole exercise of asking for 'tawad' (discount) was very time consuming for both the buyer and seller. That's why I introduced the concept of fixed pricing. It was more efficient and saved a lot of time. In the beginning, buyers couldn't accept the fact that they could no longer bargain. It took almost a year before the concept was fully accepted by our customers."

"I took a hands-on approach in choosing our sales ladies. For me, they were one of the most important aspects of the business. I considered them a powerful marketing force. I personally interviewed each applicant and I designed their training program myself."

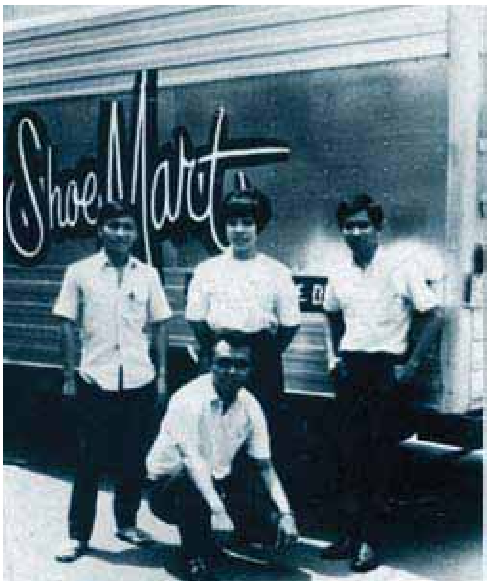
[redacted]

Another change he implemented in ShoeMart was dressing up show windows and using glass counters. He made his store visually attractive, luring in more interested customers.

And, of course, there were the ShoeMart sales ladies in their blue nifty uniforms. He meticulously chose the most attractive ladies who he trained to be always properly groomed and attentive to the needs of each and every customer.

"I took a hands-on approach in choosing our sales ladies. For me, they were one of the most important aspects of the business. I considered them a powerful marketing force. I personally interviewed each applicant and I designed their training program myself," Mr. Sy said.

Mrs. Sy-Coson noted, *"The sales ladies in ShoeMart actually looked like flight stewardesses."*



SHOEMART EMPLOYEES POSE IN FRONT OF A SHOEMART UTILITY VEHICLE.

A MUCH YOUNGER IMELDA MARCOS CUTS THE RIBBON FOR A SHOEMART STORE OPENING. SHE IS JOINED BY MR. SY ON THE EXTREME LEFT, TESSIE SY AND FELICIDAD SY ON THE EXTREME RIGHT.

For him, the sales ladies must be attractive with a pleasing personality, and must smile a lot. He interviewed many beautiful women, but noted that many were lacking in personality. It was also important for them to skillfully answer the customers' queries about the shoes that ShoeMart sold.

And with hardly any technology available in stock and inventory management, the salesladies had to be trained to use hand signals when asking for shoes which the customers wanted to fit. These signals were transmitted to a 'barker' standing on a platform at the center of the store. Using a large old-fashioned microphone that hung from the ceiling, the barker translated the hand signals and passed on the orders to the people manning the stockroom in the attic. In a few seconds, the boxes of shoes dropped through a hole from the ceiling where the salesladies waited with their arms outstretched and ready for the catch.

"It was quite a spectacle to watch." Mr. Sy continued, *"It was a very memorable system we developed."*

When asked who developed such a system for ShoeMart, Mr. Sy replied, *"I solicited ideas from our employees. I encouraged them to submit their ideas to me. They face customers the whole day that is why they know what is effective and what is not. I listen to their suggestions."*

Intimate Understanding of Shoes

"I acquired a deep knowledge of shoes," Mr. Sy claims, an assertion for sure no one would question. *"Show me a pair of shoes and I can tell right away what's wrong with it,"* he mused.

"I had to know very well the shoes I was selling because fashion changes very fast. I had to master the different designs, colors, and styles. I researched on shoes. I read advertisements and articles in newspapers and magazines, and looked at what kinds of shoes people were wearing.

"I solicited ideas from our employees. I encouraged them to submit their ideas to me. They face customers the whole day that is why they know what is effective and what is not. I listen to their suggestions."

[redacted]

"I also had to look for reputable shoe manufacturers and suppliers. They had to be reliable. The price and quality of their shoes must pass my standards," Mr. Sy added.

Not surprisingly, Mr. Sy tapped the able craftsmen of Marikina, considered then and now as the shoe capital of the Philippines.

"Marikina supplied close to 70% of the shoes we were selling at ShoeMart, while about 30% were imported. I would bring my own designs to Marikina and the shoemakers there would manufacture them for me. Sometimes, I would also go to Sta. Rosa, Laguna," Mr. Sy said.

"ShoeMart was one of the major shoe buyers in Marikina. I would like to think that we contributed to the growth of Marikina," he added.

To augment his inventory, Mr. Sy also had to travel a lot to look for foreign suppliers. He went to the United States, and

MR. SY SURROUNDED BY SM SALESLADIES.

A MUCH YOUNGER HENRY SY BELIEVES IN DRESSING AND GROOMING HIMSELF WELL WHEN PROMOTING HIS BUSINESS.

visited great cities in Europe such as Paris and Milan. There, he attended footwear trade fairs where he got wind of the latest trends in shoes.

"Back then, the shoe industry abroad was very different and more sophisticated than in the Philippines. For instance, many other countries have four seasons, whereas here, we only have the wet and dry seasons. Obviously, Filipinos will not buy winter footwear.

"Nonetheless, there were a lot of buying opportunities. In fact, I had the best of both worlds. Apart from buying them at big discounts every end of season, I also had the chance to select the styles I felt would be saleable in the Philippines."

"It was not easy, as I had to develop a unique ability to know how to buy shoes. I had to persevere in spite of the difficulties," Mr. Sy said.

This dogged determination proved to be a key to his success.

Because of Mr. Sy's untiring efforts, ShoeMart steadily grew in the sixties and in the seventies. It first expanded to the emerging financial center called Makati, the business potential of which he already foresaw. That became a hit. Thereafter, ShoeMart put up another branch in Cubao, Quezon City. It was also around this time that ShoeMart became more than just a shoe store. It turned into a full-blown, highly successful department store, selling a wide range of consumer goods.

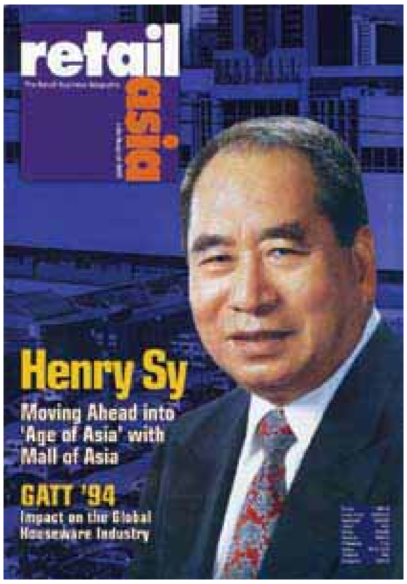
Universal Branding

The name again changed, this time evolving simply into SM, for much better recall and a more universal brand. In fact, SM today has become a byword in many places all over the country.

"I started off with shoes. But by traveling to different countries, I got new ideas about expanding my merchandise. It was also timely because I was running out of shoes to sell. My local suppliers could not meet my demand. That made me go into selling clothes, handbags and accessories. This made me go into the department store business. With hard work and self-discipline, the business prospered," Mr. Sy shared.

> ***"Shoes could change someone's personality. Make someone wear casual shoes and somehow, she will also act in a casual manner. But let a woman put on heels, there would be a change in gait. She will surely walk with more bearing."***

Many other things prospered under the astute management of Mr. Sy, basically building one successful venture after another, capitalizing on the strength and the network of older but well-kept businesses. Hence from department stores, he built a mall in the mid-eighties, and kept building over the years. To date, SM has 30 malls. His bank, acquired many years ago as Acme Savings Bank, likewise grew to become the BDO of today having served the needs of SM's suppliers and tenants, and acquiring other banks at the start of this decade.



MR. HENRY SY, SR. ON THE COVER OF RETAIL ASIA, JULY/AUGUST 1995 ISSUE

FROM JUST OVER 200,000 PAIRS IN 1958, SM SOLD OVER 21.7 MILLION PAIRS OF FOOTWEAR IN 2007

SM Shoe Business Today

Amid SM's successful diversification and expansion, shoes and other footwear still form a big part of its business. From Mr. Sy's selling a handful of shoes from American soldiers right after the Second World War, the sales numbers attained nowadays are staggering.

"We sold approximately 19 million pairs of shoes in 2007, while the supermarkets and hypermarkets sold another 2.7 million pairs of footwear," declared Jorge T. Mendiola, senior vice president of SM Department Stores.

"That's about 15% of the total sales of all SM department stores all over the country. Sales of our shoes grew 5% in 2007, and we expect to achieve the same growth rate in 2008," Mr. Mendiola added.

"In our case, revenues from one particular type of footwear, Beachwalk slippers, grew 73% in 2007," said Mr. Robert Kwee, executive vice president of SM Hypermarkets.

Continuing the tradition of Mr. Sy, both Mr. Mendiola and Mr. Kwee still look at quality, pricing, and supplier reliability when sourcing the shoes and footwear they sell.

"For us, the suppliers' reliability and consistency in their deliveries count a lot. We prefer suppliers who are able to regularly replenish our stocks, because replenishment is always a challenge," Mr. Kwee said.

Similar to what Mr. Sy did half a century ago, SM's shoe buyers today go to trade fairs abroad to observe market trends.

"We send people abroad to find out what the latest trends and styles in footwear are. We talk to local fashion consultants, and we even surf the internet," Mr. Mendiola stated.

Together, SM department stores and hypermarkets do their selection of merchandise on 'buying days', when various suppliers present their products at the company's head office. Mr. Sy would, from time to time, still join the buying exercise.

"We are very meticulous when it comes to choosing our shoes. We even have what we call 'fitters', who actually wear the shoes offered by the suppliers. It is better to scrutinize shoes when real persons, and not just mannequins, wear them," Mr. Mendiola continued.

This commitment to quality has made SM the dominant footwear retailer in the country today.

"We prominently display our shoes at the front portion of our hypermarkets. Since we are part of the SM group, shoes must be given importance in all our branches," Mr. Kwee stressed.

"The shoe section of an SM Department Store occupies a large floor area. As a matter of fact, I don't know of any other store that allocates such a big selling area just for shoes," Mr. Mendiola added.

Weight in gold

After starting off in a most inconspicuous manner, yet reaching the pinnacle of Philippine retailing, Mr. Sy may think that shoes are worth every bit of their weight in gold. For him and for SM, shoes may well be as good as gold.

Interestingly, Mr. Sy views shoes more than just simple merchandise or a source of profit. He also looks at shoes from a different perspective.

"Shoes could change someone's personality. Make someone wear casual shoes and somehow, she will also act in a casual manner. But let a man wear formal dress shoes or make a woman put on heels, there would be a change in their gait. They will surely walk with more bearing," Mr. Sy observed.

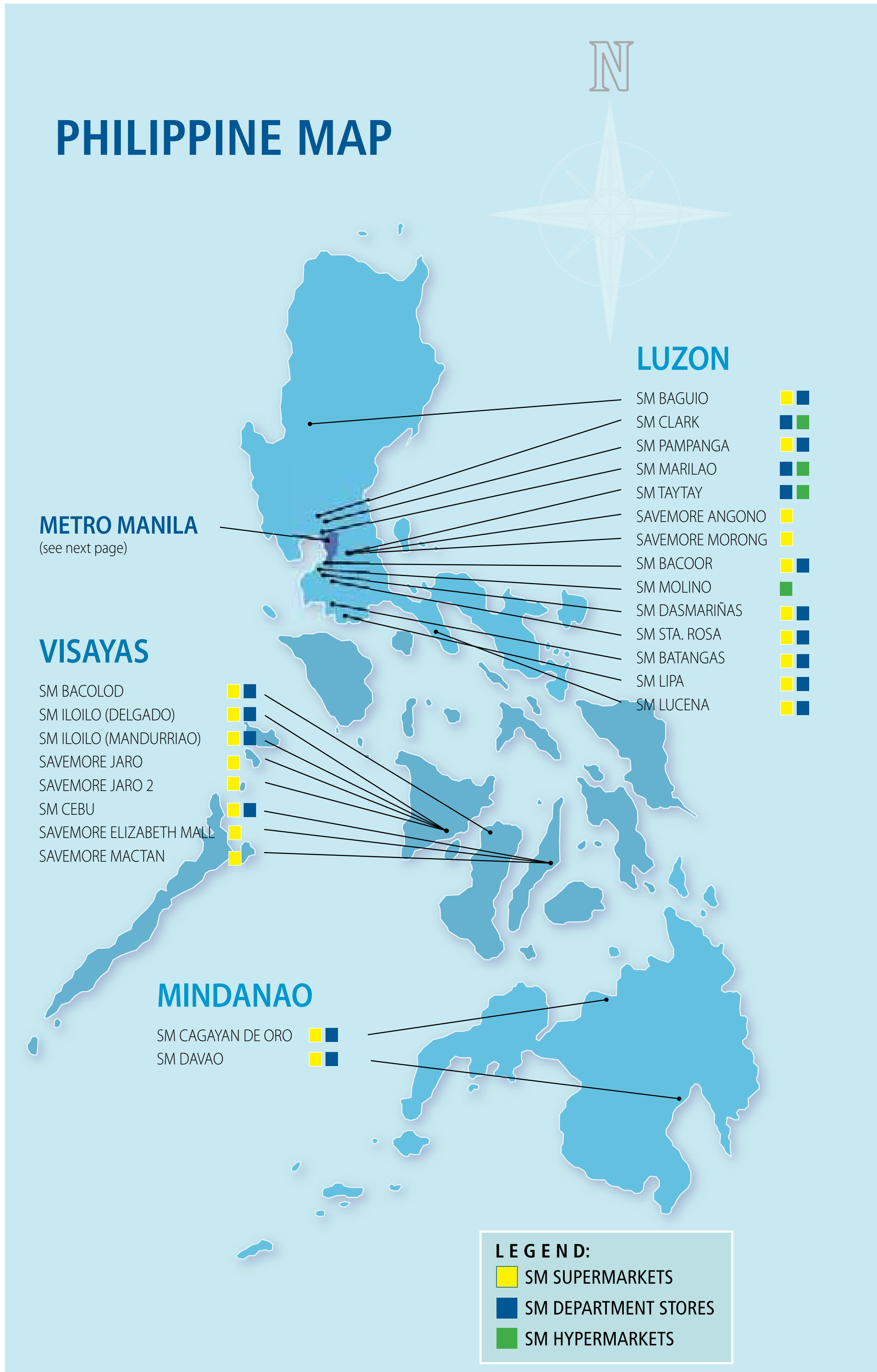
"I love shoes. That's why I went into the shoe business," Mr. Sy aptly concluded.

SM Store Locations At A Glance

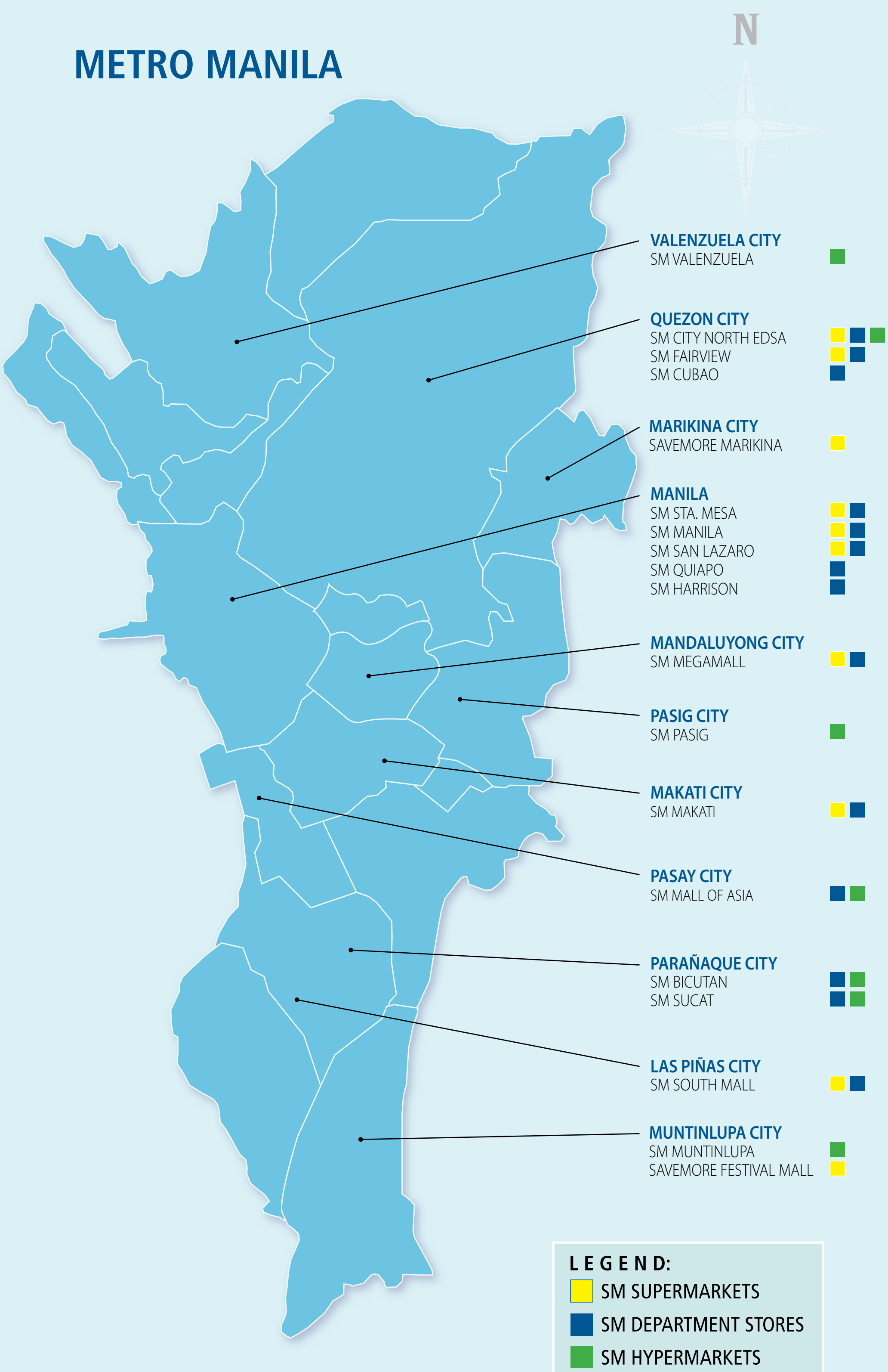
SM DEPARTMENT STORES

BRANCH	DATE OPENED
SM Quiapo	March 1972
SM Makati	September 1975
SM Cubao	October 1980
SM Harrison	October 1984
SM North EDSA (Q.C.)	November 1985
SM Sta. Mesa (Q.C.)	September 1990
SM Ortigas (Mandaluyong City)	June 1991
SM Cebu	November 1993
SM Las Piñas	April 1995
SM Bacoor (Cavite)	July 1997
SM Fairview (Q.C.)	October 1997
SM Mandurriao (Iloilo City)	June 1999
SM Manila	April 2000
SM Pampanga	November 2000
SM Davao	November 2001
SM Cagayan de Oro	November 2002
SM Bicutan	November 2002
SM Lucena	October 2003
SM Baguio	November 2003
SM Marilao (Bulacan)	November 2003
SM Dasmariñas (Cavite)	May 2004
SM Batangas	November 2004
SM Delgado (Iloilo City)	December 2004
SM San Lazaro (Manila)	July 2005
SM Sucat (Parañaque City)	November 2005
SM Sta. Rosa (Laguna)	February 2006
SM Clark (Pampanga)	May 2006
SM Mall of Asia (Pasay City)	May 2006
SM Lipa (Batangas)	September 2006
SM Bacolod	March 2007
SM Taytay	November 2007

Total Net Selling Area (2007) - 362,371 sqm.



METRO MANILA



SM SUPERMARKETS

BRANCH	DATE OPENED
North EDSA (Q.C.)	December 1985
Sta. Mesa (Q.C.)	September 1990
Megamall (Mandaluyong City)	July 1991
Southmall (Las Piñas City)	April 1995
Bacoor (Cavite)	April 1995
Fairview (Q.C.)	October 1997
Manila	April 2000
North Reclamation (Cebu City)	August 1998
Mandurriao (Iloilo City)	June 1999
San Fernando (Pampanga)	November 2000
Davao	November 2001
Cagayan De Oro	November 2002
Lucena	October 2003
Baguio	November 2003
San Lorenzo (Makati City)	February 2004
Dasmariñas (Cavite)	May 2004
Batangas City	November 2004
Delgado (Iloilo City)	December 2004
San Lazaro (Manila)	July 2005
Sta.Rosa (Laguna)	February 2006
Lipa City (Batangas)	September 2006
Bacolod	March 2007
STAND ALONE SUPERMARKETS (SAVEMORE)	
Jaro (Iloilo City)	October 1998
Marikina City	April 1999
Mactan (Cebu)	June 2002
Elizabeth Mall (Cebu)	December 2003
Festival Mall (Alabang)	February 2004
Jaro 2 (Iloilo City)	August 2006
Angono (Rizal)	November 2006
Morong (Rizal)	December 2007

Total Gross Selling Area (2007) - 153,120 sqm.

SM HYPERMARKETS

BRANCH	DATE OPENED
Sucat (Parañaque City)	May 2001
Bicutan (Parañaque City)	November 2002
Marilao (Bulacan)	November 2003
Valenzuela	October 2005
Molino (Bacoor, Cavite)	November 2005
Clark (Pampanga)	May 2006
Mall of Asia (Pasay City)	May 2006
North EDSA (Q.C.)	June 2006
Pasig	August 2006
Taytay (Rizal)	November 2007
Muntinlupa	November 2007

Total Gross Selling Area (2007) - 83,574 sqm.

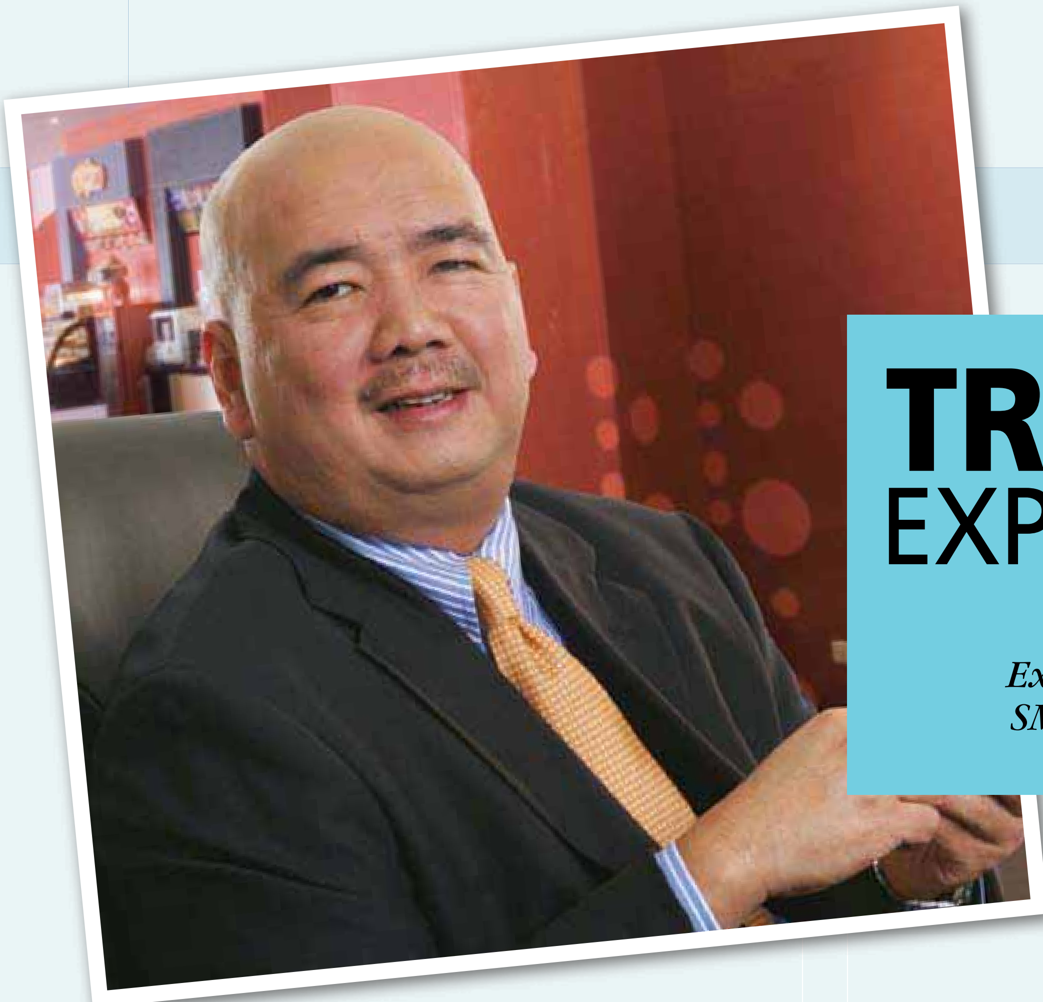
Mall Operations

SM's mall operations, which is run by its 53%-owned subsidiary SM Prime Holdings, Inc. (SMPH or SM Prime) delivered its usual strong and steady performance with revenues growing by 16% to ₱15.3 billion and profits increasing 10% to ₱6 billion. EBITDA stood at ₱11.0 billion for a 16% increase over last year's level. Income from operations rose to ₱8.7 billion, 14% higher compared to ₱7.7 billion in 2006 resulting in an operating margin of 57%.

SM Prime opened three new malls and expanded an equal number of existing malls in 2007. New malls that opened include SM City Bacolod, SM City Taytay, and SM Supercenter Muntinlupa. The mall expansions were in SM City Pampanga, SM City Cebu, and SM Mall of Asia. All these developments added 353,000 square meters (sqm) to SM Prime's total gross floor area (GFA) for a total GFA of 3.9 million sqm, which is now the country's largest. The malls enjoyed an average 97% occupancy in 2007 and saw an average daily pedestrian count of 2.5 million.

The planned expansion in 2008 includes three new malls in Rosales (province of Pangasinan), Baliuag (province of Bulacan), and in Marikina City (Metro Manila). It also includes expanding its large malls along EDSA such as SM Megamall and SM North EDSA, along with SM Fairview. All these are estimated to cost around ₱6 billion.


SM
City
PAMPANGA



TRENDS & EXPECTATIONS

JEFFREY C. LIM
Executive Vice President
SM Prime Holdings, Inc.

The Philippine economy did very well in 2007. Did that translate to a better performance for the malls?
The company achieved a 14% growth in operating income of ₱8.7 billion. Operating revenues also registered a 16% growth while net income grew at 10%, softened by the increase in interest expense and corporate income taxes. Meanwhile, EBITDA grew by 16% to ₱11.0 billion translating to a healthy EBITDA margin of 72%.

2007 reaffirmed SM Prime's dominance in mall operations as it opened three new malls and expanded an equal number of its existing malls.

How much of your growth could be attributed to the economy and how much from expansion?
Out of the total increase in rental revenue of 17%, same-store sales contributed 7% while new malls and expansion of existing malls contributed 10%.

Average occupancy of your malls is 97%. How do you manage to maintain it at this level? How do you also manage to keep the foot traffic very high in the malls?
We constantly introduce innovations in our malls to suit the needs of our customers which have become more discerning and demanding. We continuously improve infrastructure and conduct maintenance procedures. We also cater to the needs of our disabled customers and those with special needs.

How did the Mall of Asia perform in 2007? Is it doing better than expected?
Mall of Asia is doing better than we expected. It is now 100% leased and is SM Prime's third best performing mall in terms of revenues. Average daily foot traffic in MOA is between 200,000 to 300,000 during weekdays, and up to 500,000 to 1,000,000 during weekends.

Are there plans to further expand Mall of Asia anytime soon?
There are no immediate plans for expansion after the opening of the Science Discovery Center in 2007.

What are your expansion plans for 2008?
For 2008, we have three new malls lined up: SM Supercenter Rosales with a gross floor area (GFA) of 31,000 sqm., SM City Baliuag with 61,000 sqm. and SM City Marikina with 122,000 sqm. The expansion of existing malls include SM City Fairview Annex 3 with an additional GFA of 29,000 sqm., and SM Megamall with an additional 15,000 sqm. All these will expand our gross floor area by 258,000 sqm. to 4.2 million sqm. We are also expanding our very first mall, SM North EDSA.

How much will your expansion plan cost and what will your source of funding be?
The planned capital expenditures for 2008 is ₱6 billion. This will be funded from a mix of internally generated funds and external borrowings.

You announced the acquisition of the SM malls in China. What is the rationale for this acquisition?
The move will allow SM Prime to gain a foothold in China's fast-rising economy and use this as a platform for long-term growth outside the Philippines. As expansion continues in the Philippines, China will provide SM Prime's shareholders the opportunity to tap and take advantage of high growth areas.

How much is the acquisition cost for the China malls and what was the method of valuation used in determining the cost?
The net acquisition price of ₱10.8 billion was arrived at based on a 20% discount to the gross appraised value of the China properties of ₱18.4 billion, minus outstanding liabilities of ₱3.9 billion. The valuation of the China malls was based on the discounted cash flows and net appraised values.

What is the payment scheme for the China malls?
The malls will be acquired through a share swap arrangement. SM Prime will issue 913 million new shares to the Sy Family valued at ₱11.86 per share. The issue price, on the other hand, was based on SM Prime's 30-day, volume-weighted average price as of November 13, 2007. This means that instead of cashing in on the assets, the original owner of the malls which is the Sy Family will increase its stake in SM Prime. This ensures full alignment of interests of the SM Group with that of SM Prime's minority shareholders.

Aside from China, are there any other countries you are looking at for further expansion?
We are looking at opportunities in other countries but everything is exploratory at this time.

SNEAK PREVIEW

The Greening of SM North EDSA

(Excerpted from SM Prime Annual Report)

SM NORTH EDSA, SM PRIME'S VERY FIRST MALL IS about to turn green. Construction is now underway to create a 400-meter long "Skygarden" with a gross floor area of approximately 31,000 square meters. It's a haven where shoppers and visitors of SM North EDSA can stroll along a landscaped and covered path, pleasantly lined with tropical trees, flowering plants, and shrubs. The Skygarden will stretch from one end of the mall to the other so that it will have a number of entryways leading to different sections of the mall.

It will be decorated with a lagoon, an aviary for bird lovers, an amphitheater for shows and special events, cafés, casual dining, and novelty shops. A waterfall will cascade from the Skygarden at level four down to ground level facing EDSA—a piece of art that promises to create a calming and colorful scene, especially at night when various lights provide an added dimension to the falls and the pond beneath. Below the Skygarden will be a transport depot for buses and added parking space for shoppers.

"This project is the first to be introduced to any SM mall as we honor SM North EDSA, being our very first, by sprucing it up with natural elements. This is part of SM Prime's commitment toward enhancing the environment, and bringing nature and the beauty that comes with it closer to our customers," said Mr. Hans T. Sy, President of SM Prime.

It may be recalled that SM Prime built its very first mall in 1983 on the north end of a main thoroughfare in Metro Manila called EDSA, the

acronym for Epifanio De Los Santos Avenue. Back then, the lot that was purchased in 1978 was no better than a vacant swamp remotely located from the center of the metropolis. SM Prime's Chairman, Mr. Henry Sy, Sr. saw the potential of the place, standing at the crossroad for regional traffic coming to and from the northern provinces of Luzon.

Mr. Sy took his inspiration to build SM North EDSA from the first few malls built in the U.S., which he thought Filipinos will want to have. Ironically, many thought his plan was ill-timed because the construction of the North EDSA mall happened when divisive political issues were prevalent in the country. The mall opened in 1985 with a gross floor area of 125,000 square meters, at the height of one of the country's worst crises.

"We had a tough time getting tenants to fill up the place. It was a risky period in our country's history. So, we opened with only the SM Department Store and another small shop as the mall's tenants," said Mrs. Teresita Sy-Coson, Vice Chairperson of SM Investments Corporation.

But to everyone's surprise and those of many skeptics, crowds came and filled the mall. *"It was an instant success,"* noted Mrs. Sy-Coson.

As more tenants came in and entertainment concepts were introduced to the mall such as cinemas, SM North EDSA came to be known as one that institutionalized the "one-stop shopping concept" and was the first to introduce "malling" as a pastime in the Philippines.

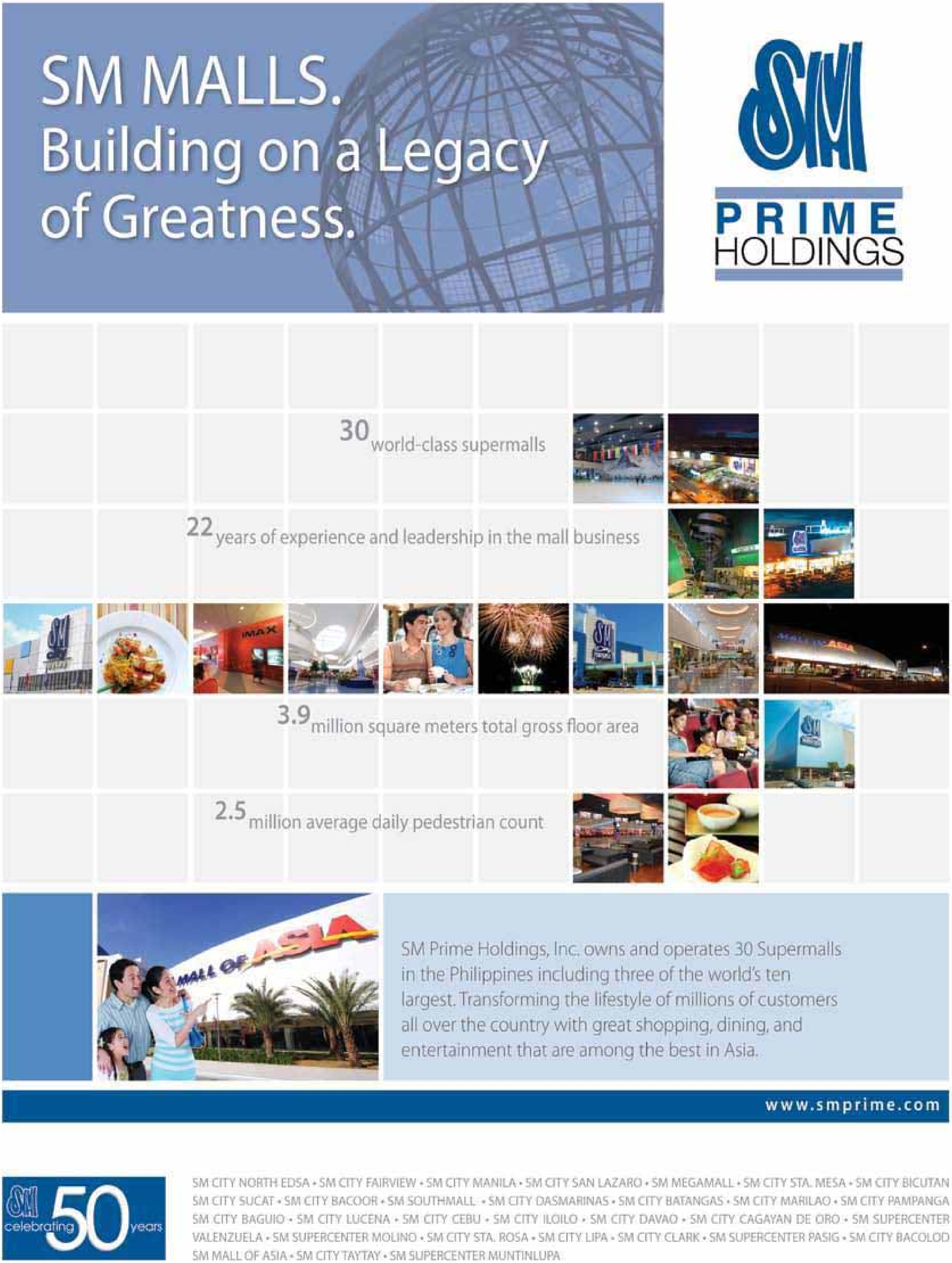
Businesses and real estate thrived where SM North EDSA was built, that over a period of 20 years, it has seen four expansions including The Block which opened in 2006. It continues to draw an average foot traffic of about 400,000 per day giving enough scope for SM Prime to undertake yet another expansion.

By the time this current project is completed to include the Skygarden and the Annex building expansion, SM North EDSA's gross floor area will quadruple to 456,000 square meters from its original size, and make it the country's largest, and among the most successful malls in the world.

In addition, it will carry the distinction of being the first mall to truly influence and revolutionize the malling experience for Filipinos.

This speaks of SM's ability to build, expand and sustain its malls, allowing each and every area to establish its own identity and grow within its surrounding community.

CLOCKWISE FROM LEFT
SM North EDSA now;
SM North EDSA in 1985;
The Block; the "Skygarden" in perspective


SM MALLS.
Building on a Legacy of Greatness.
SM
PRIME HOLDINGS
30 world-class supermalls
22 years of experience and leadership in the mall business
3.9 million square meters total gross floor area
2.5 million average daily pedestrian count
MALL OF ASIA
SM Prime Holdings, Inc. owns and operates 30 Supermalls in the Philippines including three of the world's ten largest. Transforming the lifestyle of millions of customers all over the country with great shopping, dining, and entertainment that are among the best in Asia.
www.smprime.com
SM celebrating 50 years
SM CITY NORTH EDSA • SM CITY FAIRVIEW • SM CITY MANILA • SM CITY SAN LAZARO • SM MEGAMALL • SM CITY STA. MESA • SM CITY BICUTAN
SM CITY SUCAT • SM CITY BACOOR • SM SOUTHMALL • SM CITY DASMARINAS • SM CITY BATANGAS • SM CITY MARILAO • SM CITY PAMPANGA
SM CITY BAGUIO • SM CITY LUCENA • SM CITY CEBU • SM CITY ILOILO • SM CITY DAVAO • SM CITY CAGAYAN DE ORO • SM SUPERCENTER
VALENZUELA • SM SUPERCENTER MOLINO • SM CITY STA. ROSA • SM CITY LIPA • SM CITY CLARK • SM SUPERCENTER PASIG • SM CITY BACOLOD
SM MALL OF ASIA • SM CITY TAYTAY • SM SUPERCENTER MUNTINLUPA

Mall Trivia

(as of 31 December 2007)

30 Malls Nationwide

3.9 million sqm.
Total Gross Floor Area

9,144 Mall Tenants

883 Food Tenants

543 Food Court Tenants

20,707 Food Court Seats

2,277 Kiosks and Carts

185 Movie Screens

124,426 Cinema Seats

124 Bowling Lanes

48,267 Parking Slots

2.5 million
Average Daily Pedestrian Count

WORLD'S LARGEST
SHOPPING MALLS*

SHOPPING MALL	YEAR OPENED	GLA Square feet (Square meters)	TOTAL AREA Square feet (Square meters)
South China Mall Dongguan, China	2005	7.1-million (660,000)	9.6-million (892,000)
Jin Yuan (Golden Resources Shopping Mall) Beijing, China	2004	6.0-million (560,000)	7.3-million (680,000)
SM Mall of Asia Pasay City, Philippines	2006	4.2-million (386,000)**	
West Edmonton Mall Edmonton, Alberta, Canada	1981	3.8-million (350,000)	5.3-million (570,000)
Cevahir Istanbul Istanbul, Turkey	2005	3.8-million (348,000)	4.5-million (420,000)
SM City North EDSA Quezon City, Philippines	1985	3.6-million (332,000)**	
SM Megamall Mandaluyong City, Philippines	1991	3.6-million (332,000)**	
Berjaya Times Square Kuala Lumpur, Malaysia	2005	3.4-million (320,000)	7.5-million (700,000)
Beijing Mall Beijing, China	2005	3.4-million (320,000)	4.7-million (440,000)
Zhengjia Plaza (Grandview Mall) Guangzhou, China	2005	3.0-million (280,000)	4.5-million (420,000)
SM City Cebu Cebu City, Philippines	1991	2.9-million (267,000)	

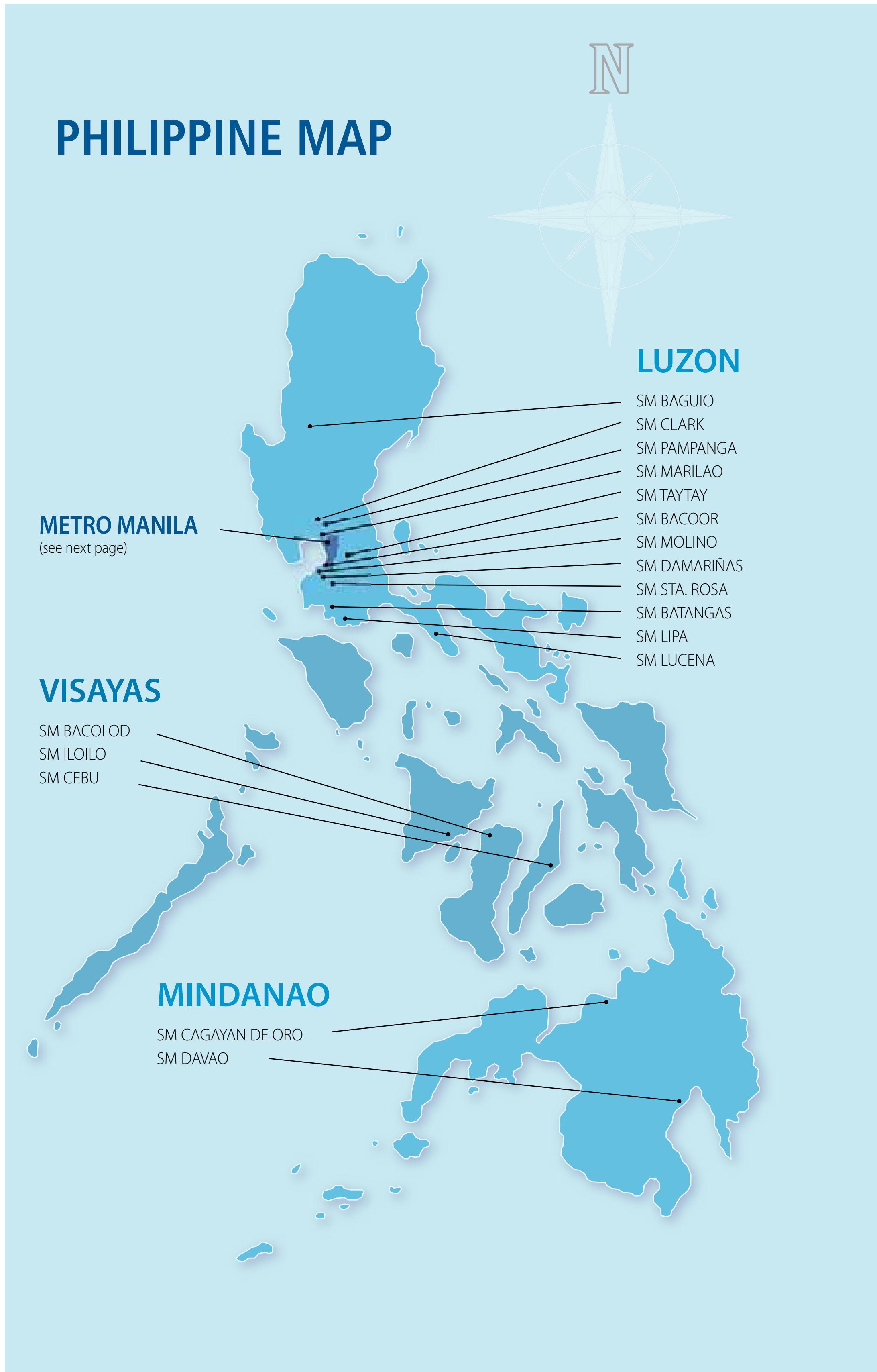
* *American Studies at Eastern Connecticut State University, Shopping Mall and Shopping Center Studies, Last revised Feb. 1, 2008.*

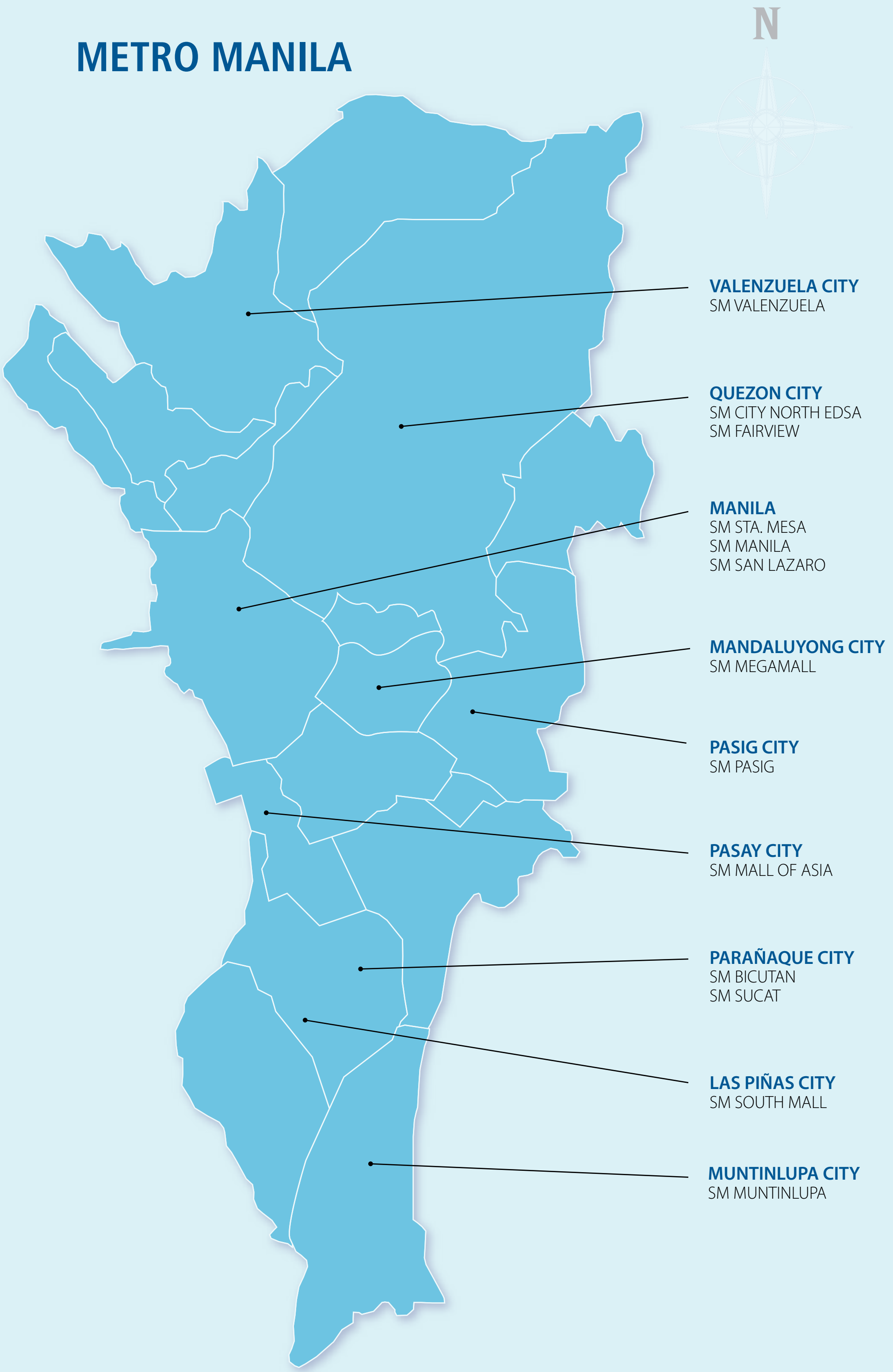
** *Cited as "gross floor area," which may be somewhat greater than the comparable gross leasable area.*

SM Mall Locations At A Glance

PROVINCIAL

MALL Address	DATE OPENED Gross Floor Area (In sqm.)
CEBU North Reclamation Area Cebu City	**November 1993** 268,611 sqm.
BACOOR Tirona Highway cor. Aguinaldo Highway, Bacoor, Cavite	**July 1997** 116,892 sqm.
ILOILO Benigno Aquino Avenue Diversion Road, Manduriao, Iloilo City.	**June 1999** 101,735 sqm.
PAMPANGA Brgy. San Jose, City of San Fernando Pampanga	**November 2000** 129,102 sqm.
DAVAO Quimpo Blvd. cor. Tulip Drive Ecoland, Matina, Davao City	**November 2001** 75,440 sqm.
CAGAYAN DE ORO Masterson Avenue cor. Coranvia Carmen, Cagayan de Oro	**November 2002** 56,011 sqm.
LUCENA Dalahican Road cor. Maharlika Highway, Lucena City	**October 2003** 78,655 sqm.
BAGUIO Luneta Hill, Upper Session Road Baguio City	**November 2003** 105,331 sqm.
MARILAO McArthur Highway, Brgy. Lias Marilao, Bulacan	**November 2003** 88,654 sqm.
DASMARIÑAS Barrio Pala-pala Dasmariñas, Cavite	**May 2004** 79,792 sqm.
BATANGAS Pallocan West Batangas City	**November 2004** 76,819 sqm.
MOLINO Brgy. Molino, Bacoor Cavite City	**November 2005** 48,710 sqm.
STA. ROSA Barrio Tagapo, Sta. Rosa Laguna	**February 2006** 79,325 sqm.
CLARK M.A. Roxas Highway, Clark Special Economic Zone Angeles City, Pampanga	**May 2006** 98,824 sqm.
LIPA Ayala Highway, Lipa City Batangas	**September 2006** 72,035 sqm.
BACOLOD Rizal St., Bacolod City Negros Occidental	**March 2007** 61,413 sqm.
TAYTAY Manila East Road, Brgy. Dolores Taytay, Rizal	**November 2007** 91,920 sqm.





METRO MANILA

MALL Address	**DATE OPENED** Gross Floor Area (In sqm.)
SM CITY NORTH EDSA EDSA cor. North Avenue Quezon City	**November 1985** 331,861 sqm.
STA. MESA Magsaysay Avenue corner Araneta Avenue, Sta. Mesa, Manila	**September 1990** 133,327 sqm.
MEGAMALL EDSA cor. Julia Vargas Avenue Ortigas Center, Mandaluyong City	**June 1991** 331,679 sqm.
SOUTHMALL Alabang Zapote Road Las Piñas City	**April 1995** 205,120 sqm.
FAIRVIEW Quirino Highway cor. Regalado Avenue Greater Lagro, Fairview, Quezon City	**October 1997** 154,183 sqm.
MANILA Concepcion Avenue cor. Arroceros and San Marcelino Sts., Manila	**April 2000** 166,554 sqm.
SUCAT Sucat Road Parañaque City	**July 2001** 98,106 sqm.
BICUTAN Doña Soledad Avenue cor. West Service Road, Parañaque City	**November 2002** 112,737 sqm.
SAN LAZARO Cor. Felix Huertas St. and A. H. Lacson Ext., Sta. Cruz, Manila	**July 2005** 178,516 sqm.
VALENZUELA Mc Arthur Highway Brgy. Karuhatan, Valenzuela City	**October 2005** 70,616 sqm.
MALL OF ASIA SM Central Business Park J.W. Diokno Blvd., Pasay City	**May 2006** 407,101 sqm.
PASIG Frontera Verde Ortigas, Pasig City	**August 2006** 29,017 sqm.
MUNTINLUPA Manila South Road, Brgy. Tunasan Muntinlupa City	**November 2007** 53,986 sqm.

Banking

The 2007 profits of BDO Unibank, Inc. (BDO) grew modestly by 2% to ₱6.5 billion after incurring one-off expenses related to the merger with Equitable PCI Bank (EPCI), and the absorption of American Express Savings Bank.

BDO spent an additional ₱2 billion to integrate its operations in treasury, commercial and consumer lending, branch management, asset management and information technology, among others. It also redesigned its branches to achieve one look and one image.

The merger resulted in catapulting BDO's industry ranking to second spot from fifth in terms of resources. In a sector where size matters, BDO is expected to achieve greater efficiencies, wider market reach, and increased profitability over the medium term.

Even if low-cost deposits increased by 14% in 2007, BDO's total deposits decreased by 5.2% to ₱445 billion, as clients shifted to high-cost special deposit accounts. As a result, net loans also contracted slightly by 0.3% to ₱312 billion as the shift affected other receivables, such as interbank loans and reverse repurchase agreements. Gross customer loans, however, expanded by 15%.

For 2008, BDO expects to substantially complete its integration with EPCI as well as redeploy some of the redundant branches. This will optimize the benefit from the merger as it results in further broadening the bank's market reach.

China Banking Corp. (China Bank), on the other hand, also reported modest growth of 4% to ₱3.7 billion, resulting mainly from extraordinary gains in 2006. In addition, it also began consolidating the operations of its recent acquisition, Manila Banking Corporation.

This acquisition will provide China Bank a new platform for growth by accelerating the bank's plan for branch network expansion.

Apart from the acquisition, China Bank is also accelerating its introduction of a new technology platform, a customer information system, and the upgrading of computer hardware and tellering systems.


CHINABANK
TELLER 3
TELLER 2
TELLER 1

TRENDS & EXPECTATIONS

NESTOR V. TAN
President
Banco De Oro Unibank, Inc.

Why was your profit growth in 2007 lower than your historical average?
Banco De Oro Unibank, Inc. (BDO) recorded an audited net income of ₱6.5 billion in 2007, representing a 2% growth over the pro-forma 2006 level of ₱6.4 billion. This was lower than BDO's historical average profit growth rate primarily due to extraordinary expenses related to the BDO-EPCI integration and the settlement of taxes under the BIR's tax abatement program.

Do you expect any further costs of consolidation to affect future earnings?
We expect additional integration-related costs of about ₱1 billion to be reflected in the 2008 P&L. Integration efforts are still ongoing and are expected to be "substantially" completed only by mid-2008.

How is the merger with EPCI coming along?
The integration is slightly ahead of plan. The Bank's immediate priorities after the legal merger took effect on May 31, 2007 were first, to complete the integration of the branches and systems of BDO and EPCI; second, to attain the established business targets; and third, to establish "one-bank, one-face, one-consistent-service" to customers quickly. These were intended to allow BDO to maximize merger synergies and capitalize on the complementary strengths of both banks. Prior to this, BDO had already upgraded its information technology capability and the Automated Teller Machines of the two institutions were interconnected.

The Bank rationalized and consolidated its product offerings under the "BDO" trademark following a new branding strategy implemented in July 2007. Similarly, BDO's subsidiaries and affiliates, including those overseas, are now being rationalized.

The conversion and integration of the branch network into the BDO system is ongoing and is expected to be completed by the middle of 2008. This process also involves the optimization of the expanded branch network, particularly in growth areas outside Metro Manila, through a redeployment strategy aimed at improving access to our target customers.

What immediate benefits are you drawing from the consolidation with EPCI?
The BDO-EPCI merger substantially enhanced and expanded the combined operational scale and distribution platform of the Bank. From being a niche player, BDO is now a full-service entity offering a complete array of products and services, i.e. Retail Banking, Lending (Corporate, Commercial, SME and Consumer), Treasury, Trust, Credit Cards, Corporate Cash Management and Remittances. Through its subsidiaries, the Bank offers Leasing and Financing, Investment Banking, Private Banking, Bancassurance, Insurance Brokerage and Stock Brokerage services. With the enhanced operational scale and bigger distribution network, these business lines are now among the industry leaders in their respective segments.

BDO

When do you expect to see and feel the benefits of consolidation?
We anticipate the financial impact of the synergies from the merger and the cost benefit will be fully realized by 2010. However, some benefits will be seen on the revenue and business development side by mid-2008.

Post-integration by mid-2008, BDO plans to re-engineer its operations to reflect the scale, scope and service requirements of the combined entity. This will involve the realization of cost benefits after Phase 1 integration to include manpower rationalization and redeployment, automation of manual processes and streamlining of backroom operations. Going forward, this would eventually lead to improved profitability and sustained outperformance of industry growth rates.

What was your rationale for acquiring American Express Savings Bank?
BDO acquired the business to consolidate its position in the credit card market and at the same time strengthen its hold on the mass affluent market. When BDO acquired the American Express business in the Philippines, it included the American Express Philippines US Dollar and Peso Card portfolios as well as the consumer banking services of American Express Savings Bank (AESB). Concurrent with the sale, BDO also entered into a partnership agreement with American Express that allows BDO to issue American Express Cards in the Philippines.

Do you see the Philippine credit market growing further in the Philippines?
We see the aggregate Philippine credit market growing at a sustainable pace similar to 2007's growth rate of 7.8% (ex-Reverse Repurchase Agreement).

We expect stronger growth to come from consumer lending given rising GDP/capita, sustained OFW remittances, relatively low interest rates and longer repayment terms and the still low consumer loan penetration vs. regional peers.

We anticipate middle-market lending to expand further as the "underground" economy is tapped particularly in the provincial areas.

Did the sub-prime crisis in the US affect, in any manner, the bank's performance?
BDO has no direct exposure to US subprime mortgages, though the Bank has some exposure to CDOs. As the CDOs are marked-to-market on a periodic basis, the impact is periodically reflected in the Bank's income statement through mark-to-market gains or losses.

What can your depositors and other clients expect from BDO in 2008?
Our depositors and clients can continue to expect BDO's noted customer focus and willingness to explore non-traditional ways of providing banking services. With the expanded branch (665 domestic branches) and ATM (more than 1,200 nationwide) networks, the Bank now has a stronger platform to serve its clients, reach new markets and distribute a wider product set. The Bank's longer operating hours and weekend operating schedule in select areas also provide customers continued accessibility to banking services.

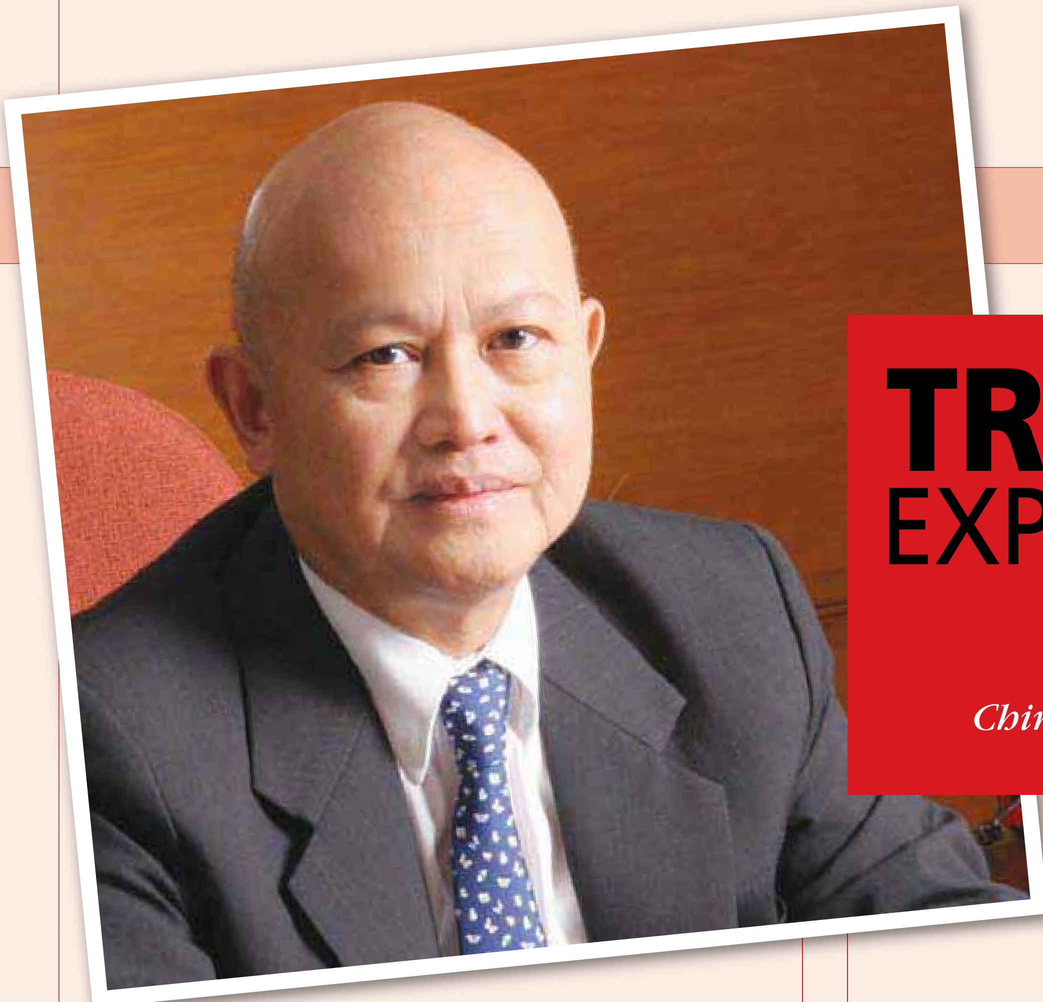
What are the expected growth drivers for BDO in 2008?
Key growth drivers for BDO would be consumer and commercial lending, low-cost deposit generation and fee-based income from branch banking, trust banking, remittances, credit cards, cash management and bancassurance.

What challenges do you expect to face?
While major challenges exist, BDO hopes that its underlying businesses can continue exhibiting above-industry growth while ensuring that integration remains on track and is competed by mid-2008. In terms of banking operations, Philippine banks vie for limited lending opportunities in a low interest-rate environment. This is compounded by efforts of the Monetary Authority to control growth in money supply, resulting in distortions in market rates and added pressure on funding cost. Concerns on the US economy will affect emerging markets' ability to sustain the growth rates recorded in recent years, leading to a possible global slowdown.

Where do you see the Philippine economy going in 2008 and what can you do to take full advantage of the opportunities?
The Philippine economy remains resilient amid an expected US economic slowdown, elevated oil prices and domestic political jitters. While we expect GDP growth to slow down to 6.1% in 2008 from 7.3% in 2007, the economy will remain supported by private consumption and increased government spending. Increased investments and good prospects for services (BPO boom and tourism) and agriculture are also seen to compensate for the weakness in manufacturing and exports.

For BDO, this means an opportunity to tap sectors that are expected to do well; such as retail trade and consumer-based industries, business process outsourcing, property, construction and allied industries, and infrastructure

Do you expect to become the industry leader, in terms of total assets, anytime soon?
We do not have specific targets to become the industry leader in terms of assets, though we aspire to be a major banking player able to generate above-industry performance and provide consistent, above-average returns to shareholders.



TRENDS & EXPECTATIONS

PETER S. DEE
President
China Banking Corporation

How was China Bank's performance in 2007?
The operating environment for the banking industry in 2007 was a sharp contrast to those in the previous years, characterized by record-low interest rates that led to margin compression across most business lines. Coupled with the expected decline in trading gain opportunities, China Bank was able to surmount these challenges in sustaining its creditable financial performance, with a net income of ₱3.7 billion, a 4% growth from last year's ₱3.5 billion. This translated to a return on equity of 15.6% and return on assets of 2.3%, still among the best in the industry.

Did you see any significant shifts in loan demand in 2007? If so, how did you adjust to those shifts to optimize your bank's efficiency and profitability?
The trends in loans growth were as expected, with the consumer sector recording the fastest growth. China Bank growth in net loans and receivables of 22.3% was more than double that of the banking industry, with significant gains in the SME/middle market and corporate segments as well. We are on track with the goal of doubling the share of consumer lending to the total loan portfolio from 10% to 20% in three years. Consumer loans have relatively better yields compared to the corporate sector.

What is your lending mix in the consumer sector? What is the most promising product?
Of the total consumer lending of ₱13.7 billion, 59% came from housing loans, 21% from contract-to-sell (CTS) financing and 20% from vehicle financing. Housing loans remain the most promising product increasing by 45% in 2007 and accounting for 62% of the total growth in consumer loans.

Did the sub-prime crisis in the US affect, in any manner, the bank's performance?
China Bank has no exposures to CDOs and similar instruments and is therefore not directly affected by the US sub-prime crisis. However, the Bank and the Philippine banking industry will be affected indirectly through its effects on the global financial markets. How to deal with the impact of such repercussions will be among the key issues for 2008, with its potential for altering the financial landscape in significant ways.

How much was your acquisition cost for Manila Bank and what was the method of valuation applied to arrive at the cost?
Following the Memorandum of Agreement (MOA) signed with the majority shareholders of Manila Bank on June 21, 2007, China Bank acquired 7.7 million Manila Bank shares at ₱214.7 per share for an aggregate price of ₱1.7 billion, representing 87.5% of Manila Bank's total subscribed capital stock. The Manila Bank shares were acquired at book value based on unaudited adjusted capital funds as of December 31, 2006. Following a tender offer to the remaining shareholders of Manila Bank at the same price which expired January 15, 2008 and separate acquisitions, China Bank's equity interest in Manila Bank has reached 91.82%.

What benefits do you expect from this acquisition?
The Manila Bank acquisition provides China Bank with a platform for higher growth. It has accelerated the bank's plan for branch expansion. Manila Bank has 75 branch licenses of which 27 are operating. The 26 operating Manila Bank branches were fully integrated into the China Bank network by February 2008. The thrift bank license will be retained at the Ayala Avenue head office and will be renamed China Bank Savings, Inc., pending the necessary regulatory approval. This will result to a total branch network by 2010 of 270 (excluding a number of savings bank branches), a network size that will provide China Bank the footprint to become a major industry player with a wider geographic reach and a larger customer base.

What is the progress of the merger as of end December 2007?
China Bank took effective control of Manila Bank on September 3, 2007 with the appointment of China Bank officers as members of the Board of Directors of Manila Bank. The China Bank Board of Directors approved on October 3, 2007 the approval to change the corporate name of Manila Bank to China Bank Savings, Inc. with China Bank Savings as the business/trade name, subject to approval by the Securities and Exchange Commission (SEC).

What bank-wide innovations and improvements do you intend to implement in 2008?
Major investments for sustainable growth are needed for the Bank to achieve its stretch goals in 2008. These include investing in robust technology platforms such as a new core banking system; new ATM switch/card system; a new IVRS (phone banking) system; a new Treasury System; a new Remittance System; a full roll out of the Loans Origination System (LOS), especially for the consumer banking. A major initiative also involves the Customer Information project to enable total relationship management. Underpinning the computerization projects is the streamlining of transaction processes, which will enable the handling of the significant increases in business volume with greater efficiency, lower cost and better customer service. Meanwhile, key interim upgrades were recently done to handle immediate growth needs such as upgrade of the IBM mainframe hardware, implementation of the newest version of the Dimension/Bank Way core banking system and upgrade to the Browser-based Tellering system. The Bank will also implement the business center concept in the branch network.

How many new branches will you open this year and where will these be located?
Subject to BSP approval, the Bank plans to open 56 branches in 2008 mainly Metro Manila locations. The Savings Bank will open 2 new branches.

What do you think will be CHIB's major growth drivers this year?
Major growth drivers are the significant growth in lending across all segments and the continued growth in low-cost CASA deposits. In addition, we expect significant contributions from fee-based revenues such as bancassurance, private banking, remittance business, trade and FX.

What challenges do you expect to face?
Apart from the decidedly guarded global outlook compared to the previous years, inflation risk driven by record-level prices of oil and other key commodities has become a key concern. The key challenges facing the banking industry continue to be low interest rates and accompanying narrower spreads. Post-Basel 2 compliance, local banks have adjusted their balance sheets and strengthened their capital bases with ROP positions no longer carrying zero capital risk weight.

Where do you see the Philippine economy going in 2008 and what steps will you take to take full advantage of the opportunities?
The key challenges in 2008 will be the global economic slowdown, continued volatility in oil prices, uptrend in non-oil commodity prices, continued global financial turbulence and high domestic liquidity. For the Philippines, the peso remained strong due to the weakening US dollar and continued OFW remittances. Monetary policy is expected to be focused on keeping inflation pressures in check.

With this environment, China Bank continues to aim to become No. 1 among second-tier banks in terms of profitability, competitiveness, being the "bank of choice" in our market segments, most admired by competitors and consistently delivering shareholder value. The Bank believes this can be achieved thru major transformation in its systems, processes, structure, support and most especially the development and empowerment of its people.

ASIAN BANKER ACHIEVEMENT AWARDS 2007

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Teresita Sy-Coson

Nestor V. Tan

The Asian Banker Woman of the Year In Financial Services

TERESITA SY-COSON
Chairperson
Banco De Oro Unibank, Inc.

TERESITA "TESSIE" SY-COSON HAS MANAGED TO EMERGE FROM THE SHADOW OF HER FATHER HENRY SY, ONE OF THE PHILIPPINES' MOST SUCCESSFUL BUSINESSMEN, TO BECOME ONE OF THE MOST INNOVATIVE AND INFLUENTIAL WOMEN IN BANKING IN THE ASIA PACIFIC.

Entering banking in 1984 through her family's investment in Banco De Oro, Sy-Coson learned the banking business slowly, finally taking a full interest in 1995 when she saw opportunities to take the business to the top. The bank set out on a buying spree that included the acquisition of several small banks, mainly the country operations of foreign banks, and culminated in the acquisition of Equitable PCI Bank, the country's third largest, carrying it out of the family-run era and into a new phase of professional management.

During the year-long battle for PCI Bank, Sy-Coson used her position as the chairman of Equitable PCI Bank to fight off a contentious board and skeptical investors to sell a grand vision of well-run two banks with complimentary strengths that could bring additional scale and efficiency into the system. The merger of the two banks, the largest in Philippine banking history, was approved in April 2007, with the merged entity called Banco de Oro-EPCI. During the process, she has set the stage for the country's financial services sector to embrace a large scale transition to operational efficiency and excellence, and inevitably further consolidation.

The Asian Banker Leadership Achievement Awards 2007, Philippines

TERESITA SY-COSON
Chairperson
Banco De Oro Unibank, Inc.

NESTOR TAN
President
Banco De Oro Unibank, Inc.

IN 2006, THE PHILIPPINES' SLEEPY FINANCIAL SERVICES INDUSTRY WAS WOKEN UP BY THE MERGER OF BANCO DE ORO AND EQUITABLE PCI BANK THAT CREATED A COMPETITOR TO BE RECKONED WITH FOR THE COUNTRY'S TWO BIGGEST BANKS.

The architect of the deal, Teresita "Tessie" Sy-Coson had, through sheer tenacity, managed a difficult board on one hand and prickly institutional investors on the other to fulfill her vision of a strong, consolidated banking industry. With Banco De Oro president Nestor Tan at her side as an operational enforcer and no-nonsense business manager, the merger between the profitable Equitable PCI Bank and the well-run Banco De Oro proceeded according to the plan of these two ambitious bankers.

Sy-Coson is the vice chairman of SM Investments, director of SM Prime Holdings, and president of SM Mart, Inc. Tan is a career banker who has worked for 15 years at banks like Mellon Bank, Banker's Trust, and Barclays. He joined Banco De Oro as executive vice president in 1997 and became president the following year.

INDUSTRY RANKING: Philippine Commercial Banks

ASSETS

	Bank	4Q07 Php mn	Market Share (%)
1	Metrobank	706,889	14.6
2	**BDO**	621,303	12.9
3	BPI	617,002	12.8
4	Landbank	382,502	7.9
5	DBP	241,157	5.0
6	PNB	240,161	5.0
7	RCBC	238,879	4.9
8	Citibank	211,427	4.4
9	Union	186,714	3.9
10	**China Bank**	174,900	3.6

LOANS AND RECEIVABLES (NET)

	Bank	4Q07 Php mn	Market Share (%)
1	Metrobank	369,648	16.1
2	**BDO**	304,881	13.3
3	BPI	304,753	13.3
4	Landbank	165,505	7.2
5	Citibank	141,210	6.1
6	DBP	118,675	5.2
7	Union	114,819	5.0
8	RCBC	113,003	4.9
9	**China Bank**	90,137	3.9
10	PNB	78,532	3.4

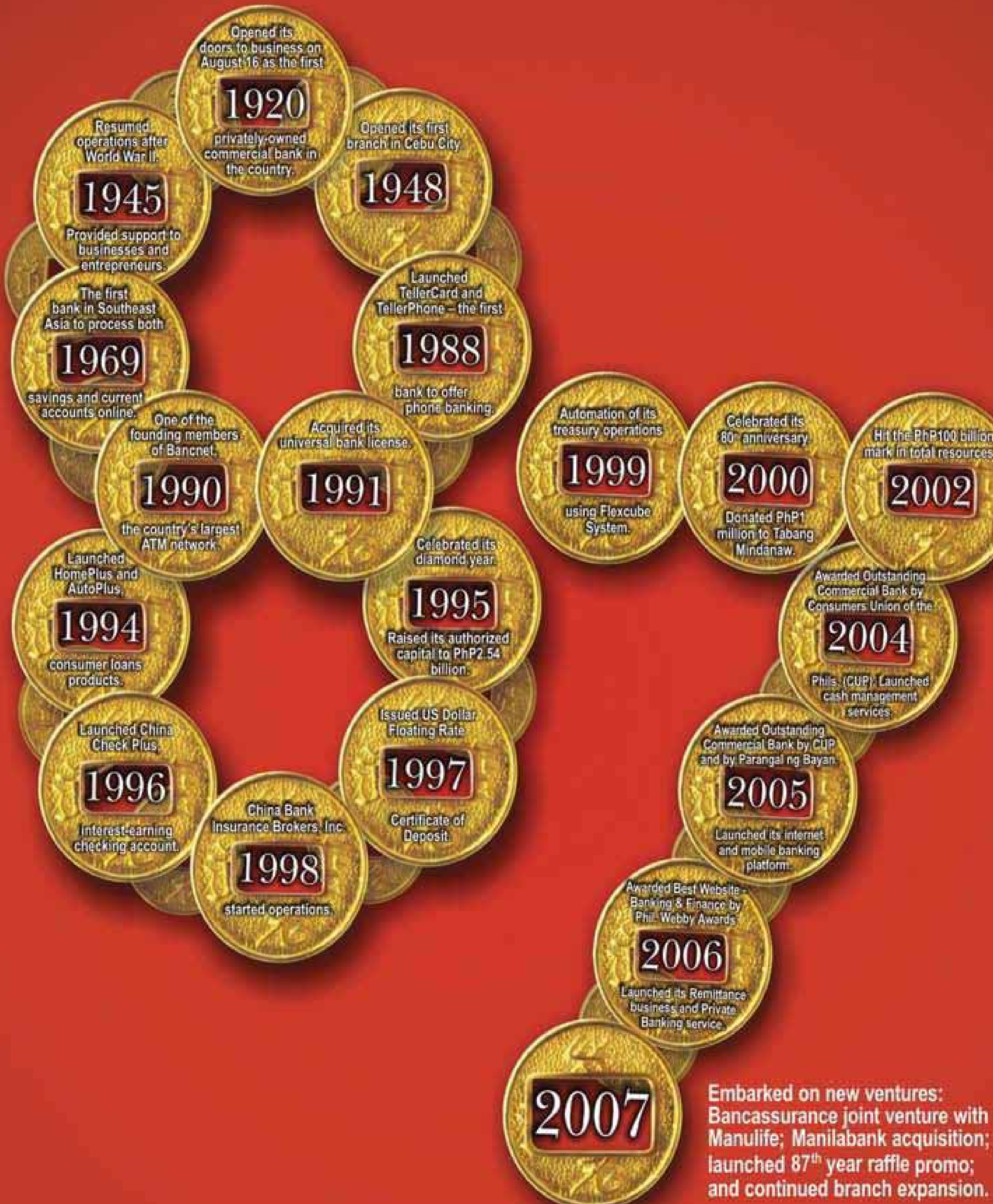
DEPOSITS

	Bank	4Q07 Php mn	Market Share (%)
1	Metrobank	530,201	15.5
2	BPI	514,118	15.1
3	**BDO**	444,413	13.0
4	Landbank	287,364	8.4
5	PNB	179,275	5.3
6	RCBC	175,780	5.2
7	Citibank	147,416	4.3
8	**China Bank**	140,468	4.1
9	Allied	117,400	3.4
10	Union	107,102	3.1

BRANCH NETWORK

	Bank	4Q07
1	BPI	829
2	Metrobank	706
3	**BDO**	666
4	PNB	324
5	Allied	303
6	RCBC	296
7	UCPB	212
8	Union	186
9	**China Bank**	166
10	Security	114

* Based on BDO's Highlights of the Philippine Commercial Banking System as of 4Q07



Embarked on new ventures: Bancassurance joint venture with Manulife; Manilabank acquisition; launched 87th year raffle promo; and continued branch expansion.

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Property

SM now has four divisions in the property business namely residential development, commercial development, tourism development, and hotel investments.

All these four legs are designed to diversify SM's holdings and spread the risks attached to the cyclical nature and keen competition in specific areas such as residential and commercial development. It is also designed to take advantage of the country's competitiveness in Tourism, one sector that up to now has found minimal support from large-scale investors.

As most of its businesses are in infancy, the financial performance of the property group in 2007 continued to be driven largely by the sale of residential condominium units while the projects in other sectors take shape. Net income grew 88% in 2007 to ₱1.1 billion, from revenues of ₱3.2 billion, up 142%.

Residential Development

SM's main residential arm, SM Development Corporation (SMDC), has been able to book more of the units sold in Chateau Elysee, which was approximately 65% complete as of end 2007, and Mezza which was 35% complete. Chateau has sold 78% of its units, while Mezza has sold 80%. SMDC introduced three other projects namely Lindenwoods, Berkeley, and Grass, all of which have been successfully pre-selling its units.

Commercial Development

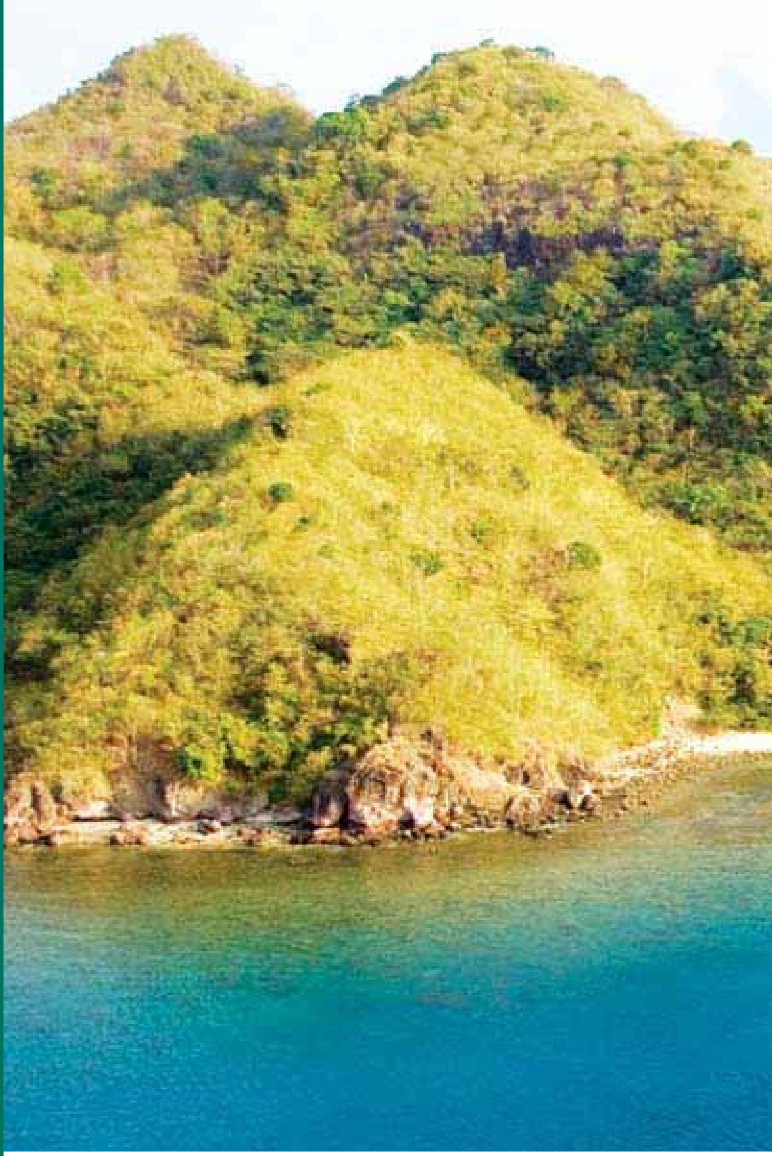
For commercial development, the Mall of Asia Complex saw the completion of its two buildings in 2007, namely SMX Convention Center and OneE-com Center. SMX is the largest private-owned exhibition and convention center. Market response to SMX has been strong with most of the space already pre-booked three months ahead from the time it opened. OneE-com, on the other hand, was 90% leased by yearend 2007 with tenants expected to move in by first quarter of 2008.

Tourism Development

In tourism, Hamilo was off to a good start as its first offering of condominium units in Pico de Loro was warmly received. Pre-sales breached the ₱1 billion mark even before the year ended. Sales will be booked as construction progresses up to 2009.

Hotel Investment

The property group added another leg with its new but aggressive hotel investment group. From having only 128 rooms in its portfolio in 2007, the group expects to grow its number of rooms by 630 in 2008 through Taal Vista Hotel and Sofitel Cebu, a five-star facility right next to SM City Cebu. The group also announced it will build a hotel in Mall of Asia Complex with 500 upmarket guest rooms to be managed by Radisson, and 80 luxury suites to be managed by Regent, both from the Carlson Group.



TRENDS & EXPECTATIONS

JOSEFINO C. LUCAS
Executive Vice President
SM Property Group

How did the property group perform in 2007? Were targets met both in terms of sales and development?
Overall, the group exceeded 2007 targets. For instance, the full-year sales reservations for Pico de Loro, which was launched in May of 2007, reached ₱1.1 billion. We saw the same strong sales performance in SM Development Corporation (SMDC), the company in charge of our primary residential condominium projects. Construction and development of projects of the property group commenced in the same year as scheduled.

Could your good performance be attributed mainly to strong market conditions or were there methods applied to the business to optimize the market's response to all your product offerings?
Favorable market conditions contributed to the brisk take up in general. But more than having a buoyant market, the product positioning of our projects in terms of price, location, design features, and strong commitment to project delivery enhanced sales generation.

The residential condominium business appears to be the most competitive with many players putting up a number of buildings, especially in Metro Manila. How are you dealing with the competition? What is SM's competitive edge?
Competition is becoming keener and more players have entered the market. The SM brand carries significant goodwill that makes our projects well accepted by our target market. Notwithstanding, each development of the property group represents a well-crafted product line that caters and responds appropriately to the demands of the marketplace.

Do you have new projects to launch in the residential sector?
The new residential projects to be launched by SMDC are Sea Residences, Field Residences, Air Residences, and possibly Wind Residences.

How much will these projects cost?
They will cost approximately Php9.0 billion.

As far as the commercial sector is concerned, what was the rationale behind naming your 60-hectare reclaimed property as Mall of Asia Complex?
This district became more popular after the SM Mall of Asia opened, with "MOA" understood to be the place or general location of Mall of Asia. As such, we are capitalizing on the mall's brand recognition and name recall. It was decided that calling the district as the Mall of Asia Complex would be the best way of giving it a name.

How is the SMX Convention Center faring thus far?
Since its opening in November 2007, the SMX Convention Center has been able to book events, conventions, exhibits and conferences on a continuing basis. The reservations have extended almost until the end of 2008 and for major conventions until 2009. We are gearing to position SMX to capture international events in the coming years by partnering with international marketing groups and organizers.

When will OneE-comCenter open its doors for business? What is the occupancy rate of the building?
OneE-com has informally opened its doors for business and we have been handing over the premises to various tenants for fit-outs. We have close to 90% occupancy to date with a mix of BPOs/call centers and traditional offices. Progressively over the months of 2008, the different floors will be physically occupied upon completion of leasehold improvements.

What type of locators were you able to attract as tenants of OneE-com?
Majority of the locators are BPOs and call centers who occupy large floor areas from one quadrant of 1,600 square meters (sqm.) to an entire floor of 9,000 sqm. The others are traditional offices such as international shipping and logistics companies, services and the like. The ground floor has food and retail stores as well as banks as tenants.

What projects will you be unveiling at the Mall of Asia Complex this year?
Currently under construction is the SM property group's Showroom Building which will showcase the model units of its various projects. This will also serve as its venue for regular project exhibits, launches and buyers' events. The construction of the Radisson/Regent Hotels will commence this year as well as that of Microtel. In the pipeline is the TwoE-comCenter adjacent to OneE-com.

You launched the Pico de Loro Cove project in Hamilo Coast in May 2007. How are sales efforts coming along?
Sales take up remains strong. We had ₱1.1 billion worth of reservations in 2007 and 2008 sales are picking up in the first quarter. We also opened a model unit showroom in SM Makati and organized a renewed sales and marketing campaign for 2008.

What is the profile of the market in Hamilo? Are you also selling to OFWs and foreign nationals?
Hamilo's market consists mostly of Metro Manila residents who belong to the higher income and upper middle-income segments. Most are professionals and businessmen in the ages of mid- to late-thirties and up. We have about less than 10% coming from the international sales divided between the US and Europe/Middle East, not really that significant a number.

What was the rate of completion at Pico de Loro as of end 2007? When do you expect full completion of the project?
Pico de Loro's completion is expected by 2012 although that involves several building projects and infrastructure elements. Development is phased; hence completion of the different buildings will be in phases. Beginning 2009, the first two building clusters will be handed over followed by others in succession. The Beach Club satellite building should be operational by yearend and the Main Club by late 2009.

What other plans do you have in Hamilo apart from Pico de Loro?
The planning of the entire 5,700 hectares is ongoing and this process will enable us to craft the overall development plan and land uses of the property. We envision the creation of various components to include a town center, resort village parks and festival grounds, resort entertainment center, resort residential communities, ferry terminal and boat club, water sport and outdoor sports complex, hotels, golf club and village, and exclusive beach villages among others.

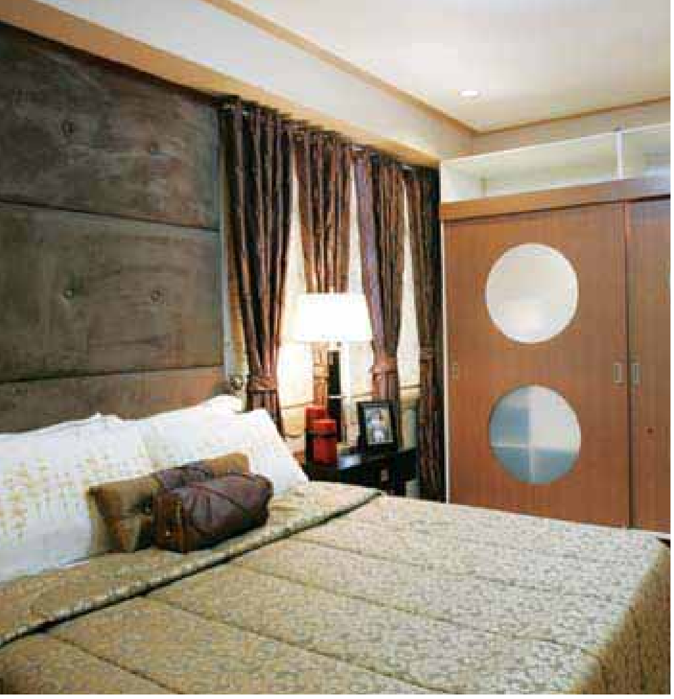
From owning a small hotel in Tagaytay, all of a sudden SM has so many plans to launch larger and upscale hotels. What is the rationale behind this move?
The hotel business complements SM's foray into tourism. Having geographically reached major and secondary urban centers of the country through its retail and mall developments, SM's presence in these areas has created opportunities for product expansion along the hospitality business it has nurtured from the Taal Vista Hotel experience.

Will hotel development be a long-term strategy for SM or is the move seen as a one-off opportunity?
The development of SM hotels is a realization of Mr. Henry Sy, Sr.'s vision on and belief in the progress of Philippine tourism. It is an integral part of realizing his vision on tourism to its full potential, and thus it shall be for the long-haul.

Where do you see the country's property sector going in 2008? What would its growth drivers be and what challenges do you expect it to face?
We see continued growth of the property sector in 2008 as we anticipate sustained economic growth for the country. Drivers will still be OFW remittances, BPO and call center expansion, a relatively low interest rate environment and improved access to financing. Expansion across all sectors poses challenges in terms of being able to build a strong organization, ability to compete against growing competition, eliminating build-out risks and maintaining cost efficiency and quality.

Do you expect the sector to be affected by the sub-prime lending issue that's strongly affecting many countries in the U.S. and Europe?
It will have an effect but it will vary among the property players depending on their exposure to the US market. But by and large, the huge potential of the overseas Filipino market will remain for years to come.

How do you plan to cope with the challenges for the year?
Keep the organization sharp and lean. Continue to innovate and aspire for market leadership. Anticipate, mitigate risks and manage costs effectively.



PROJECT BRIEF *as of Dec. 31, 2007*	Chateau Elysée	Mezza Residences	Lindenwood	Berkeley Residences	Grass Residences*
Year Started	Nov 03	Sept 06	Sept 06	Jan 08	Mar 08
Year of Completion	Oct 09	Sept 09	Mar 08	Dec 10	Jun 13
% Complete	25.5%	50.32%	72.96%	0%	0%

** % Sold based on Phase 1 only*

Strong Commitment and Solid Reputation Attract Homebuyers to SM Residences

RESIDENTIAL DEVELOPMENT HAS BECOME A mainstay at SM. With five ongoing projects, three of which were launched only in 2007, they are seeing very good market take up. In most cases, units are going faster than industry with strong pre-sales well before the project rises above ground.

At the helm of this property unit is Henry *"Bigboy"* Sy, Jr., whose goal is to offer five-star quality homes within the financial reach of millions of Filipinos. The vehicle for making it a reality is SM Development Corporation, SM Investments Corporation's housing arm.

"Affordable with a touch of class is how he envisions these homes to be," says SMDC President Rogelio Cabuñag. Generous amenities, strategic locations, distinctive and impressive architectural themes, and affordability, he adds, are the hallmarks of SMDC's developments.

SM's housing projects are known for wide lawns, high ceilings, huge swimming pools—welcome assets that break away from developments' token amenities. *"The bright idea to provide as much space as we can came from Mr. Sy, Jr. himself,"* says SMDC Marketing Executive Bernadette Ramos.

SMDC was incorporated in 1974 as an asset management company. From Ayala Fund, Inc., a name-change to SM Fund, Inc. was made in 1986 after SM Investments Corporation took over majority ownership. It was renamed SMDC in 1996.

Its first housing project, Chateau Elysée, was launched in 2003. With the success of the charming French Mediterranean-inspired condoville, SMDC established itself as a fast-rising star in the property development market. Individuals and their families, a good number of whom come from Southern Manila and the OFW sector, have found

THIS PAGE, UPPER RIGHT
Lindenwood Clubhouse

OPPOSITE PAGE FROM TOP
Berkeley Residences, Grass Residences, Chateau Elysée, and Mezza Residences in Sta. Mesa.

their dream homes in the mid-rise condominium in Parañaque. "High-quality though very affordable" is how they proudly describe their new homes.

By the time Mezza Residences, a mixed-use four-tower condominium in Sta. Mesa, was launched in 2006, SMDC had proven its worth among the hordes of happy SM homeowners. The high-rise Mezza is a market winner, having sold 80% of its units, selling even faster than Chateau Elysée.

The robust growth achieved by the company in 2007 demonstrates the public's trust and confidence in the SM name.

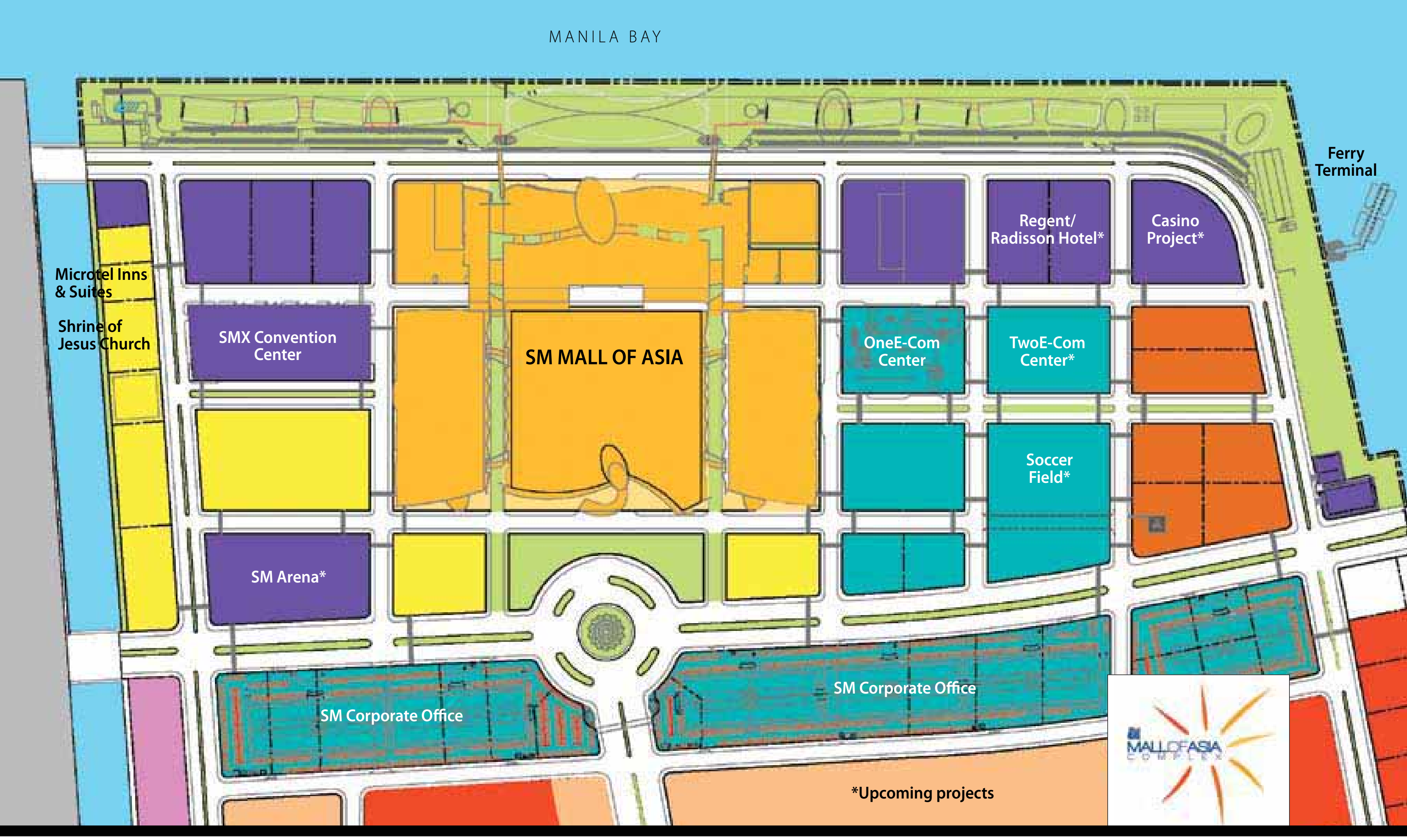
Work is proceeding a-pace for the three projects launched in 2007: Lindenwood, a lifestyle community in Susana Heights, Muntinlupa City, patterned after American country homes; Berkeley Residences, a vertical development designed for students in the university area, and young professionals in Katipunan, Quezon City; and Grass Residences, a three-tower condominium project showcasing trendy green architecture in North EDSA.

"SMDC is set to launch two more projects this year," Mr. Cabuñag says. One is Sea Residences within the Mall of Asia Complex, and the other is Field Residences in Sucat, Parañaque.

All housing projects are expected to be warmly welcomed by the market the way Chateau Elysée and Mezza are. Asked what the secret to the company's success is, Mr. Cabuñag says, *"We deliver what we commit."*

For SMDC independent director Atty. Ricardo J. Romulo, SMDC's best competitive advantage may be summed up in two words: solid reputation. *"When SMDC builds, the public knows the company will finish it in grand style."*

SM DEVELOPMENT CORPORATION



A New City Rising at the Mall of Asia Complex

SYNERGY HAS BECOME A POPULAR BUZZWORD IN THE WORLD OF big business. And for the savvy, it has become a successful strategy in bringing their enterprises to the next level.

We see that happening at SM's Mall of Asia Complex. On the 60-hectare mixed-use development in Pasay City, one can experience the growing, dynamic interplay of different businesses ranging from office, retail, institutional, residential and leisure.

Currently, the Complex is home to the SM Mall of Asia, the SMX Convention Center, OneE-ComCenter, OneEsplanade, San Miguel by the Bay, the SM Corporate Offices and the Shrine of Jesus Church.

With an initial investment of ₱2.5 billion to reclaim and develop the infrastructure of the land, the once lifeless and empty coastal property is taking shape and transforming into a thriving business and tourism complex. With its current roster of buildings, Mall of Asia Complex is now teeming with events, business activities, trade and commerce, domestic and international tours, and new construction projects.

Soon to be part of the Complex are the Microtel Inns & Suites, the Regent Manila Bay, the Radisson Hotel Manila Bay, the SM Arena, the SM Land Showroom, a football field and the SM Ferry, with the latter becoming operational by 2009.

All these developments in one area produce a robust environment for more activities to eventually thrive in one Complex. For instance, a guest may fly in to attend a conference at SMX, stay at any of the soon to be completed hotels and indulge in the many retail and dining outlets that the SM Mall of Asia and the other developments have to offer.

MALL OF ASIA
COMPLEX

But what sets Mall of Asia Complex apart from all the rest as a mixed-use development is its one-of-a-kind proposition: the Manila Bay. Compared to other commercial districts, the Complex gives locators the unique opportunity to enjoy a scenic view of the bay and its magnificent sunsets.

Masterplanned by international design firm Arquitectonica, the Mall of Asia Complex is now one of a few destinations in the city that is boosting the country's tourism industry and redefining Manila's place among the new and exciting urban centers of Asia. With the large influx of tourists and vacationing OFWs putting the SM Mall of Asia on top of their itineraries, we expect greater things to happen as SM adds more of its planned projects in the area.

As one of the largest malls in the world, SM Mall of Asia has become a major attraction for many visitors. The mall boasts of having over 900 retail and food outlets and a few pioneering establishments such as the IMAX theatre with the largest IMAX screen in the world, the first Olympic-sized skating rink in the country, and the Science Discovery Center, a 3,000-sqm. interactive display highlighting different facets of science and technology.

The SM Mall of Asia extends to the San Miguel by the Bay, the 1.5 kilometer outdoor strip allocated to house dining and entertainment establishments. The entire stretch of the strip, which faces the bay, also has jogging paths and bike trails.

Another crowd drawer of the Complex is the SMX Convention Center, which was inaugurated in November 2007. The Philippines' largest privately run exhibition and convention center, the 46,600-sqm. structure is now the venue of choice of a wide variety of events spanning from intimate wedding or birthday receptions to international conventions and exhibitions. SMX's success can be viewed from its fully booked status three months ahead.

Another addition to the Mall of Asia Complex is the newly-opened OneE-ComCenter. As the country's fast rising hub for business and commerce, several major companies have already taken advantage of its leading-edge design and facilities. The 105,857 square-meter OneE-comCenter is a 10-storey building which is connected to the SM Mall of Asia via a pedestrian bridge. Designed for the modern office, OneE-ComCenter includes e-commerce, contact centers, business process outsourcing (BPO) companies, customer relationship management (CRM) services and specialized office uses. OneE-com is now 90% leased to various tenants, mostly call center and business process outsourcing operations.

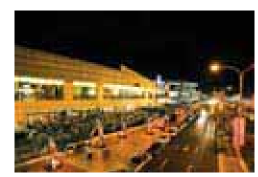
Soon to rise on the Complex is the SM Arena – a sprawling indoor facility for big-time sports and entertainment events that can seat over 16,000 spectators. This expansive arena is expected to also be the venue of choice of major concerts of well-known international artists in the music and entertainment industries.

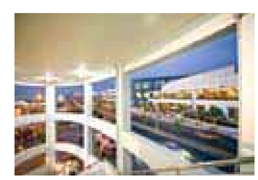
Likewise in the pipeline are the construction of the SM Ferry, which will feature a modern commercial ferry terminal to service guests and tourists who wish to travel to SM's Hamilo Coast in Nasugbu, Batangas, in Cavite City, or in Bataan.

Meanwhile, Microtel Inns and Suites hotel group is now putting up a 150-room hotel strategically located near the SMX Convention Center and the Mall of Asia by November 2008.

SM is also constructing its own hotel in the area with 500 4-star rooms to be managed by the Carlson Group's Radisson, and 80 5-star rooms to be managed by the Regent also of the Carlson Group. The two-in-one hotel is scheduled for completion in early 2010.

With the new structures continuing to add to the vibrancy of the Mall of Asia Complex, the synergy at display is just a glimpse of things to come. Within the next five to seven years, we see the landscape of Mall of Asia Complex changing rapidly where a new city is indeed rising.





SM Mall of Asia

One E-Com

SMX Convention Center

2007 WORLD PYRO OLYMPICS:

Setting Manila's Skyline on Fire

FOR TWO SUCCESSIVE WEEKENDS IN JANUARY 2007, HORDES OF SPECTATORS EXCITEDLY TROOPED TO MALL OF ASIA COMPLEX.

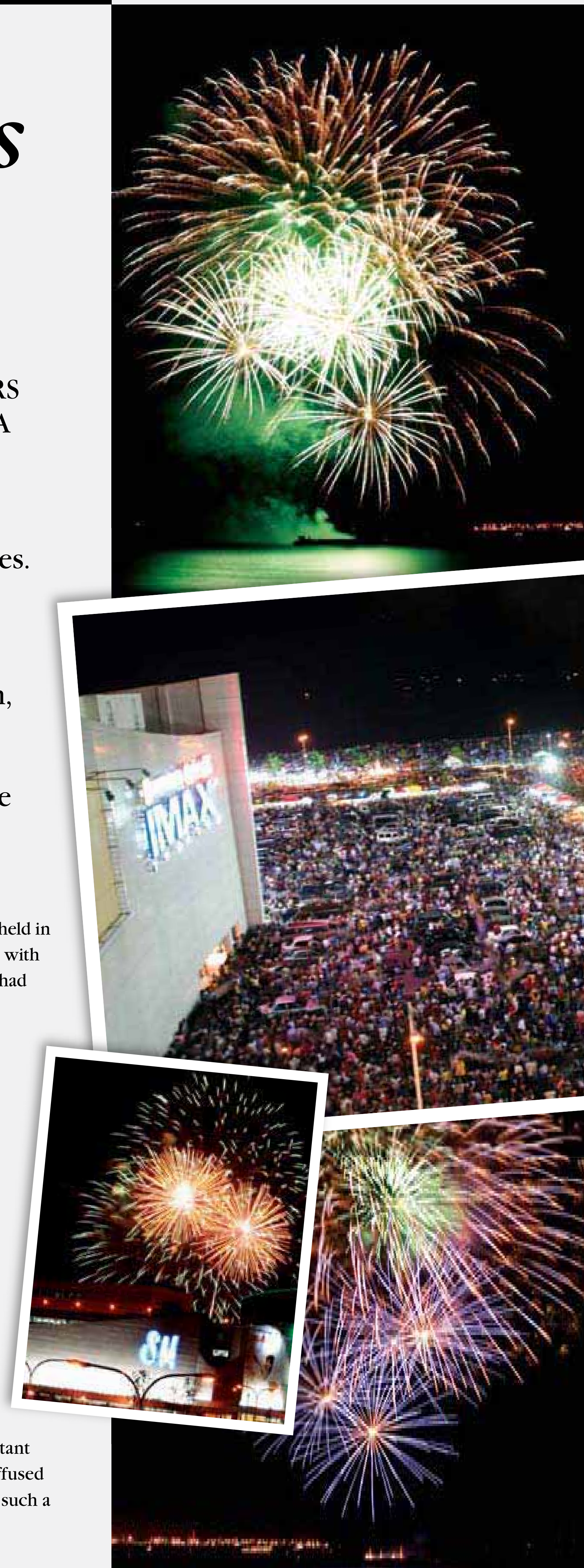
Their purpose? To witness one of the greatest pyrotechnics or fireworks competitions ever staged in the Philippines.

The jaw-dropping event was the World Pyro Olympics (WPO), which brought in seasoned pyrotechnic experts from Australia, Canada, China, Denmark, Germany, Poland, Spain, United Kingdom, and the US. Each of these countries tried to outdo each other in a 30-minute production of the most spectacular fireworks display they could mount. The Philippines, as the host country, came in as a guest participant fielding in its own magnificent finale.

This was the second WPO competition held in the country and at the Mall of Asia Complex, with SM as its host. The first competition in 2005 had Australia emerging as the overall champion. The one held in early 2007 had the United Kingdom as the grand prize winner.

Filipinos by tradition have always sought the awe and excitement provided by fireworks, which are used to liven up weddings, fiestas, holidays, and most especially, New Year's Eve. In fact, not even a presidential decree in the seventies that tried to ban the manufacture and use of pyrotechnics effectively prevented Filipinos from lighting up and enjoying a fiery spectacle and the booming sounds they create.

It is no surprise then that the Mall of Asia Complex teemed with spectators causing a humongous traffic jam in the Metropolis. While the traffic became an irritant to many commuters, tensions were soon diffused by the awesome displays and the pride that such a competition brought for most Filipinos.



CLOCKWISE FROM LEFT
Entries from: Spain, China, USA, and Poland. Humongous crowds gathered to watch the spectacle at the Mall of Asia Complex

SM OPENS SMX, the Country's Largest Convention Center

SM INVESTMENTS CORPORATION INAUGURATED on November 5, 2007, the SMX Convention Center, the country's largest center for exhibits, trade shows, conventions, banquets and other high-density events.

The ₱1.8-billion SMX Convention Center, which broke ground in March 2006, is situated at the heart of Mall of Asia Complex adjacent to the country's largest mall, the SM Mall of Asia. The highlight of the opening was the unveiling of the mural painted by internationally-renowned artist, Juvenal Sanso. *(See related story.)*

Even prior to its opening, SMX has confirmed bookings for events up to end December 2007. SM President Harley Sy said, *"We are pleased to open SMX Convention Center, which is yet another landmark at the Mall of Asia Complex. With this facility, SM is offering a unique and superior Philippine venue for major domestic and international events. SMX is one of many other buildings we are developing to transform the Mall of Asia Complex into a premier business and tourism destination in the Philippines."*

SM Executive Vice President for Property Josefino Lucas said, *"We take pride in offering SMX to the convention and exhibition market. It is equipped with world-class provisions such as concierge services, wireless broadband facilities, flexible hall areas and support services for large-scale exhibits, conventions, or other special-themed events. No other building in the country can match its capability to hold huge gatherings in a single venue."*

The three-storey structure has a gross floor area of 46,647 square meters (sqm.) with basement parking that can accommodate up to 400 cars. The leasable area is 34,743 sqm.

Level One holds the main lobby, the exhibition area, commercial shops at the perimeter, and a delivery bay for up to 15 cargo trucks. The main lobby features a pre-function area of 1,879 sqm. with a Concierge, electronic billboard monitors, and VIP and Press Rooms. The exhibition area has a floor space of 9,130 sqm. that can seat more than 5,000 people. The area can be divided into four halls for smaller exhibits or shows.

Level Two is a commercial strip with shops and has a pedestrian bridgeway leading to the Mall of Asia.

Level Three is the convention center with a floor space of 7,100 sqm. This can be divided into five function rooms. There is also a pre-function lobby with 2,500 sqm. of space and 9 meeting rooms with a total area of 810 sqm.

Ms. Annie Garcia, President of Shopping Center Management Corporation (SCMC), an SM subsidiary that manages the convention center said, *"With the inclusion of SMX to the already vibrant convention center industry, we hope to further contribute positive economic gains, increase foreign exchange earnings from international delegates, contribute greater to government revenues and make significant employment generation not only in our industry but also in the hotel and transport sectors, manufacturers, vendors and conference-related specialists."*

Just a few months after it's opening, the SMX Convention Center is slowly establishing itself as "the place where the world meets." It has been the venue of choice for numerous local and international events. One remarkable event recently held at the SMX was the 50th anniversary celebration of SM, attended by around 2,000 guests which included the country's business luminaries.

With its grand architectural design and world-class facilities, the SMX Convention Center is truly a unique offering that Filipinos can be proud of.

THIS PAGE
The facade and the high ceiling hallways of SMX Convention Center

OPPOSITE PAGE FROM TOP
Major Events At SMX: Vice President Noli de Castro leads a toast on the opening of SMX; On the launch of SM's 50th Anniversary, Teresita Sy-Coson gives her keynote; Mr. Sy enters the hall with his four sons; Betty and Henry, Jr. pose before the camera.

Sanso Mural in SMX Hails 70-year Friendship with Henry Sy

A GRAND MURAL BY RENOWNED PHILIPPINE-BASED SPANISH PAINTER JUVENAL SANSO, ENTITLED "TIDE OF FORTUNE" WAS UNVEILED DURING THE OPENING OF THE SMX CONVENTION CENTER AT THE MALL OF ASIA COMPLEX.

The painting is significant because it celebrates the long-standing personal friendship of Sanso and SM chairman and founder Mr. Henry Sy, Sr.

Sy and Sanso became childhood friends and developed a strong bond through the Second World War years, the early years of liberation, and as they were starting their respective careers. Through hard work and determination both men have achieved amazing and inspiring successes in life.

Sanso was first daunted by the task when the idea of creating a large mural was brought up to him. "I told them I was 77 years old and was not sure whether I would be able to finish it in time for the opening," he said. However, reassurances from the Sy family and Sanso's own affection for them prevailed as Sanso went on to finish the mural in three months.

"Tide of Fortune" is inspired by water, a recurring theme in his works, and significantly, symbolic of SMX's location at the Manila Bay area and most important, of the tides of fortune that had defined his relationship with the Sy family. It depicts the pristine waters and uncluttered rocks of their youth, combining his memory of boyhood outings with Sy in Batangas as well as painting in Brittany many years later.

ABOVE
"TIDE OF FORTUNE" is inspired by water, a recurring theme in his works, and significantly, symbolic of SMX's location by the Manila Bay area and most importantly, of the tides of fortune that had defined his relationship with the Sy family.

BOTTOM
Vice President Noli de Castro honors the life-long friendship of Henry Sy, Sr. and Juvenal Sanso, while Hans Sy shares the moment.

The brand new OneE-comCenter building is fast becoming the country's prime hub for businesses and commerce, with major companies enjoying its leading-edge design and facilities.

OneE-com Opens for Business

Located within the SM Group's Mall of Asia Complex, the 105,857 square-meter complex is a 10-storey building designed for the modern office, including e-commerce, contact centers, business process outsourcing (BPO) companies, customer relationship management (CRM) services, and specialized office uses.

Designed by international firm Arquitectonica and FSLim and Associates, OneE-comCenter features a 5th level courtyard and an expansive office floor plate of 9,000 square meters with two and a half levels for parking with 600 slots. On the 11th floor is a sports and activity center consisting of a full-size basketball court and six badminton courts.

"The OneE-comCenter has been designed to provide today's businesses with all the modern amenities required in their everyday operations," said Josefino Lucas, executive vice president for commercial properties and resorts for SM Investments Corporation (SMIC).

"This is part of SMIC's overall plans of developing the Mall of Asia Complex into a foremost business and entertainment district in the Philippines," Mr. Lucas added.

The OneE-comCenter is equipped with multi-telco redundancy entry points, 100% back-up power supply, and a zoned chiller system air-conditioning to meet the exacting needs of companies with 24/7 operations.

The layout of the four block building features major entrances and lobbies for every quadrant ensuring easy access and a smooth flow of people in and out of the offices.

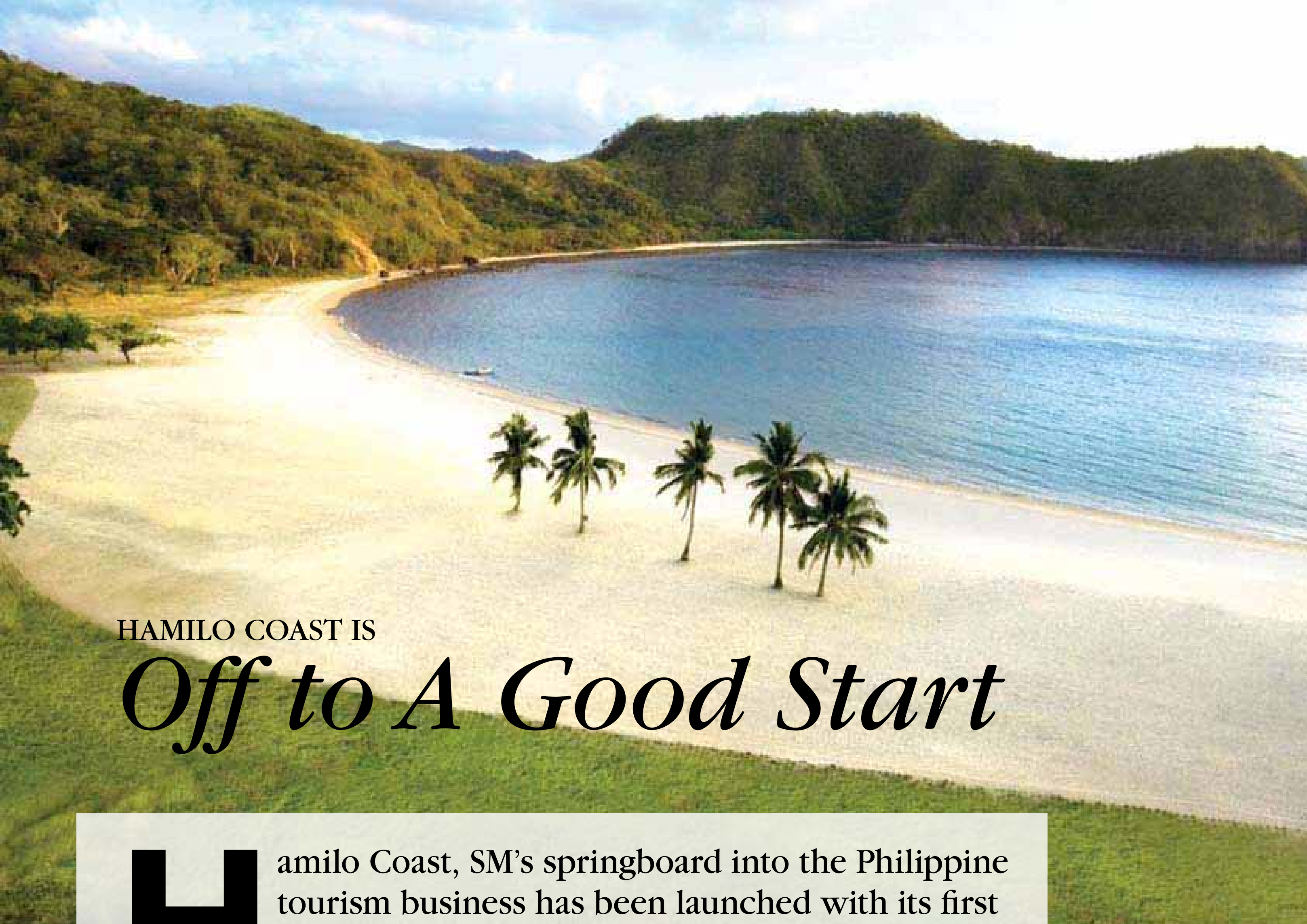
OneE-com also connects to the Mall of Asia through a bridgeway from the second-level car park, giving employees and tenants a convenient way to visit the mall's numerous shops and retail outlets.

These significant features, along with its strategic proximity to Manila's international airport, key seaports, hotels and other major commercial and residential districts, make OneE-comCenter an ideal office location for many.

Current tenants of OneE-comCenter include American President Lines, Maersk, ACS, TRG and EXL Services, a first time BPO investor in the Philippines.

The corporate offices of SM Investments Corp. and Watsons are also located in OneE-comCenter. Businesses on the first level include the Cyberzone, Fitness First Gym, Banco de Oro, HSBC Savings Bank, 7-11, McDonald's, Bacolod Chicken Inasal, CW Lifestyle Bistro Café, Starbucks and Blenz Coffee from Canada.

THIS PAGE FROM LEFT
Reception area; External corridor; Facade of OneE-comCenter



PROPERTY

Tourism

HAMILO COAST IS

Off to A Good Start

Hamilo Coast, SM's springboard into the Philippine tourism business has been launched with its first project, Pico De Loro Cove, a 40-hectare property with a two-kilometer white sand beach.

The seven-billion peso, mixed-use project is now being developed in phases over a five- to seven-year period. First on the agenda are the beach and country club and the 11 residential condominium buildings surrounding a manmade saltwater lagoon. Units for sale will have varying sizes of 28 square meters (sqm.) for a studio to 138 sqm. for a penthouse unit. The second phase will include the construction of townhouse clusters and a four-star hotel.

Jacana was launched in May 2007 with two condominium buildings having a total of 246 units. As of yearend, 80% of the units were pre-sold even as construction was only 14% complete. Full completion of Jacana is expected in the first quarter of 2009. In September 2007, Myna's two buildings were launched with 246 units. As of yearend, Myna was 43% pre-sold and construction was just 3% complete. Like Jacana, Myna will be completed in the fourth quarter of 2009.

The construction of the beach and country club is also underway. (See related story.) Sales of its shares began in late 2007, but by yearend, the market already absorbed 134 shares, confirming the market's favorable response to the project. The club will be completed in 2008.

Pico de Loro Cove will offer a complete package for an eco-leisure community that will be surrounded with all the elements of a clean, natural environment, while indulging in secure and comfortable homes, and the amenities of a beach and country club, and eventually, a few retail shops and food outlets.

The development also aims to foster environmental/cultural appreciation and conservation. These include efforts such as recycling of energy and water supplies, as well as the use of alternative energy sources. Units will be strategically laid out to minimize the use of airconditioning. Low impact four to six-storey condominium buildings are designed to blend with the natural environment, retaining most of the land's natural forests and foliage so that flora and fauna can continue to thrive.

Pico de Loro is just one of thirteen coves that are being developed in Hamilo Coast, a 1,700 hectare property in Nasugbu, Batangas. The success of Pico de Loro will signal a more aggressive pursuit to unfold SM's vision of building an integrated network of communities in Hamilo Coast, a proof of SM's commitment to make tourism a major part of its property portfolio.

Hamilo COAST

pico de loro Cove

PICO DE LORO BEACH & COUNTRY CLUB:

Interactive Living with Nature

NESTLED WITHIN HAMILO COAST'S LUXURIANT foliage and clear waters is Pico de Loro Beach & Country Club—envisioned to be the premier leisure and resort facility in the country. Pico de Loro Beach & Country Club aims to promote wellness through healthy interaction with nature accomplished through environmental preservation and enhancement.

Pico de Loro Beach & Country Club, an exclusive seaside development, also aims to provide wellness through its natural environment and specially designed programs and facilities for members. It will serve as an enclave of premier recreational pursuits: fun land and water activities, leisure interests, and dining.

Its membership-by-invitation policy makes for a highly exclusive retreat and lifestyle experience. A total of 4,000 proprietary shares are now being sold with 3,200 individual shares and 800 corporate shares. Handpicked and carefully selected, the demographics of the membership base will generate a community with exclusive tastes and special interests.

The Club's design and architecture take on a "tropical contemporary" style which provides a sense of lightness and minimalism to otherwise bulky structural elements of other clubs. Following the lead of master planner Cadiz-ML Design, a team of renowned specialists in design, architecture, environmental sustainability, and hotel and restaurant management have been contracted to bring a fresh take on the Club's contemporary style. The team comprises of R. Villarosa Architects for architectural design; Manny Samson and Associates for interior design; ADI Limited for landscape design; and Raintree Partners as Club operator.

Construction is in full swing with the Beach Club slated for a soft opening in July 2008 and the Country Club in September 2009.

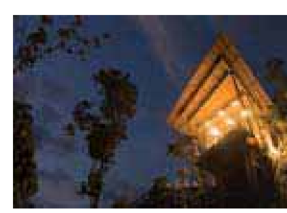
The Beach Club covers the sports, recreation and leisure requirements of members.

The Country Club crowns the area as an impressive contemporary structure featuring an unparalleled view of the swimming pools, lagoon and beach front. The main building is comprised of two structures. The section to the left contains the banquet rooms, a library, bowling and billiards hall, children's room, and game room. The section on the opposite side exudes the energy of active sports with its basketball court, squash courts, badminton courts, covered tennis courts, a gym and locker rooms.

Valued members will have their fill of delightful meals set amidst scenic views of the lagoon and breathtaking sunsets. Al fresco dining, juice and snack bars, and coffee shops will offer lush and refreshing cuisine to complement the beach resort experience.

There will be an eco-adventure challenges for members who are nature and sports lovers. Hiking, biking, and walking trails entice with breathtaking views, while the Pico de Loro swimways draw campers and snorkeling enthusiasts.

As the first development in the 1,800-hectare Hamilo Coast, Pico de Loro lays the groundwork for a sophisticated seaside lifestyle experience. Pico de Loro Beach & Country Club promises its members exquisite encounters with the best of nature.

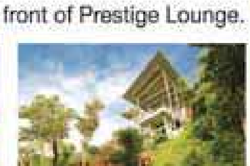


FROM LEFT
Pico de Loro Country Club, Beach Club, and Pico Point Sales Office at night.

• Pico de Loro Cove

• Boardwalk

• Pico de Loro Beach & Country Club



• Pico Point


Building communities in Tagaytay Highlands and Midlands that celebrate the complete sense of being home...
HIGHLANDS PRIME, INC.
The Woodridge
at Tagaytay Highlands
THE HORIZON
at Tagaytay Midlands
THE WOODLANDS POINT
AT TAGAYTAY HIGHLANDS
THE HILLSIDE AT TAGAYTAY HIGHLANDS
The Woodridge Park
at Tagaytay Highlands
PUEBLO REAL
TAGAYTAY MIDLANDS
SM Corporate Offices, Building A, J.W. Diokno Boulevard,
Mall of Asia Complex, Pasay City 1300, Philippines
www.highlandsprime.com
A Subsidiary of SM INVESTMENTS CORPORATION

SM Takes Tourism to Next Level with New Hotel Group

TAAL VISTA HOTEL
MANAGED BY FUEGO HOTELS & PROPERTIES

THERE'S NO TURNING BACK FOR SM WHICH HAS gone big into the sophisticated world of hotels. A new division in SM called SM Hotels is tasked with developing SM's budding hotel business. From having just 128 rooms in Taal Vista Hotel, SM's Hotels will have 660 rooms under its portfolio by the end of 2008 and 1,394 guest rooms by the first half of 2010. And just where did all these rooms come from?

THIS PAGE
Facade and lobby lounge of Taal Vista Hotel

OPPOSITE PAGE FROM TOP
SM Senior Executives Harley Sy (extreme right), Betty Sy (second from left), and Merril Yu (extreme left) join representatives of the Carlson Group; Taal Vista Hotel interiors

To start with, SM is already in the middle of expanding its own Taal Vista Hotel, a landmark structure in Tagaytay that it acquired back in 1988. It sits atop a cliff that overlooks the famous Taal Volcano, nestled within the scenic and serene Taal Lake. It is a perfect backdrop for romantic weddings and weekend getaways which the hotel is well known for. Its proximity to Metro Manila being just an hour to an hour-and-a-half away makes it an easy destination even for weekday dinners and business conferences. The ₱650 million expansion is adding another wing to the hotel with 132 rooms and a new ballroom that can seat up to 1,000 guests.

Add to that, the unveiling of Cebu City's first upscale hotel, The Sofitel Cebu Hotel. Scheduled to open at the end of this year, the hotel adds a crowning touch to the city skyline reflecting a ₱2.6 billion investment. Sofitel is the flagship brand among Accor Group's umbrella of hotels. Accor is a leader in hotels operating over 3,800 hotels with 450,000 rooms in 90 countries. Apart from Sofitel, Accor's other hotel chains are Pullman, Novotel, Mercure, Suitehotel, and All Seasons.

Merril Yu, Senior Vice President and in-charge of SM Hotels said, *"We welcome this partnership with Accor to operate Sofitel, Cebu as a major step in SM's bid to invest in the Philippine hotel and tourism business. It excites us to offer no less than a five-star facility in the Visayas region, which continues to be one of the country's major sources of exports and is a prime tourism destination for its many beaches, dive spots and other interesting sites."*

Next in the pipeline is a structure that will break ground in the second half of 2008. Set in an ideal location facing the Manila Bay, and is just a stone's throw away from the SM Mall of Asia will be a two hotels-in-one hotel building totaling 580 guestrooms. The ₱2.4 billion building has been designed to have one hotel with 500 upmarket guestrooms to be managed by Radisson, and another hotel, The Regent with 80 luxury suites, including a 400 sqm presidential suite. The two hotels will boast world class amenities such as business centers, swimming pools, fine-dining restaurants, and extensive function facilities.

Both Radisson and Regent are under the Carlson group, which is another leading global leader providing corporate solutions and consumer services in the marketing, travel, and hospitality industries.

Mr. Yu said, *"This hotel project is a much anticipated addition to the rapidly developing Mall of Asia Complex. The two hotels' prime location creates a vibrant customer base for us, given their proximity to the country's largest mall, the SM Mall of Asia, and to SMX Convention Center, which today is the country's largest privately owned venue for trade shows and other high-density events."*

Meanwhile, a resort hotel is on the drawing board for Hamilo's Pico de Loro, envisioned to be an upscale hotel with 154 guest rooms. Negotiations are now underway to appoint its hotel manager.

But plans don't end with the 1,394 guest rooms now in the pipeline. The Hotel Investments Group of SM is busy with other plans that it may soon announce. As a new leg in the property business of SM, it is positioned as a progressive development group that will optimize multiple investment vehicles in travel and tourism, consequently adding value to the existing businesses of SM.

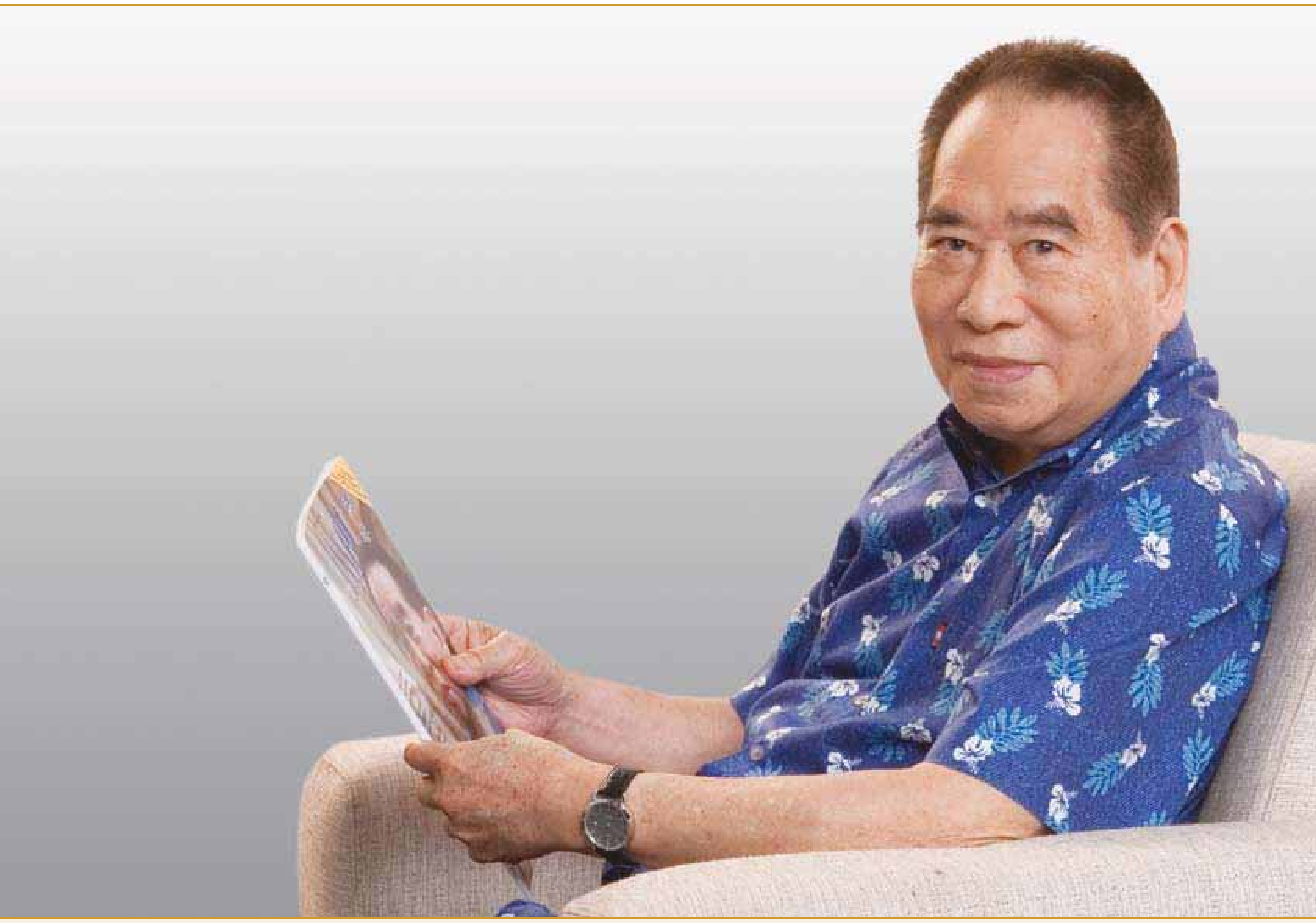
THE Asset 財資

"We always think ahead of what is going to happen. Planning is very important. If you don't have a plan, you won't have a direction."

Deconstructing Henry Sy

(Excerpted from the Asset July/August 2007 issue)

BY DANIEL YU



SPECIAL FEATURE

In June 2007, Henry Sy completed his group's takeover of Equitable PCI Bank catapulting the combined banking entity to become the largest in the Philippines. With a sprawling business empire that also spans retailing, malls and properties, he is riding high on the country's economic resurgence. The going has not always been this good for the economy but for Sy every crisis has been an opportunity not to be missed.

"A lot of people want to put up hotels. But they have to give us a fair income. They want us to provide everything for them to come in. But right now it is too one-sided," complains Henry Sy. *"They don't provide any guarantee. They have a fixed income, which includes a lot of entertainment. We don't mind. But what will we get at the end of the year?"*

IT IS MID-AFTERNOON ON A TUESDAY IN EARLY JULY 2007 and the founder and chairman of SM Investments, one of the largest conglomerates in the Philippines with a market value of US$5.8 billion, is at his residence in Forbes Park, the most expensive gated community in the country. Sy is discussing his most audacious project yet and the fulfillment of a decade-old dream—transforming a 60-hectare reclaimed property that faces the scenic Manila Bay to become SM BayCity (now known as Mall of Asia Complex) the newest business and tourism district.

It is a more combative Sy, a side that is not often revealed. At 83, Sy, who walks with the help of a cane but still wears his trademark Hawaiian shirt, asserts that he is trying to "take it easy" spending more time at home, though home also doubles as his semi-office, where he receives visitors—including business associates and bankers.

Three years ago, Sy lived in a high-rise luxury apartment along Ayala Avenue in the heart of the Makati business district. Preferring for their father to stay in a house with a garden, his six children led by Teresita, Sy's eldest, initiated the buying of the Forbes property when it was put up for sale. The original structure was torn down and a new house was constructed to his specification. *"This is a small house; very simple and quite comfortable,"* he says.

It is hard to imagine though when he is not taking it easy. In the past year, his SM (ShoeMart) group has been involved in a flurry of activity that has consolidated its position in the Philippines from retailing to mall operations, banking and property riding high on the country's economic resurgence and just as Sy reaches the apogee of his career.

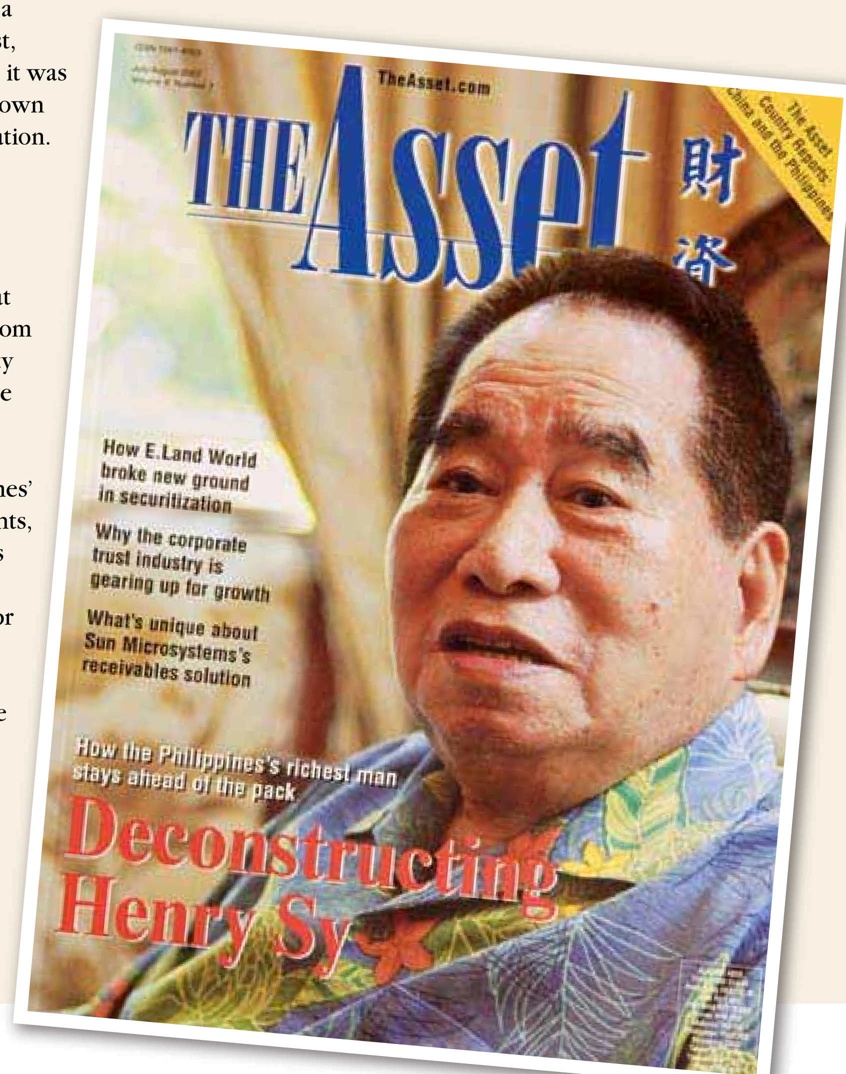
Following its listing in March 2005, which raised US$528 million and was then the Philippines' largest initial public offering (IPO), SM Investments, the holding company of Sy's business empire, has opened one shopping mall every three months, —including four in 2006, increasing its gross floor area by 23% to 3.6 million square metres. In May last year, it inaugurated its biggest one—the SM Mall of Asia —which at nearly four hectares is the country's biggest and the world's third largest.

And not just by far the largest mall operator and retailer in the Philippines, Sy has also joined the ranks of the country's leading banking magnates as well. In September 2006, SM cleared the remaining hurdle to the long drawn-out takeover of Equitable PCI Bank by its banking unit, Banco de Oro (BDO), paying ₱8.7 billion (US$180 million) for the 12.7% stake held by GSIS, the government pension fund. That acquisition triggered a ₱34.5 billion tender offer. In June 2007, the merger was completed catapulting the combined entity to become the second largest bank in the country with total assets of close to US$13 billion.

In the same month, the mid-sized China Bank, in which SM Investments is the single largest shareholder with a 16.28% stake, announced that it was acquiring the 87.5% stake held by the Puyat family in Manila Bank.

Combining the BDO and China Bank groups, the total assets of over ₱805 billion (end-2006) is well ahead of the current market leader, Metrobank, controlled by the Ty family (₱641.5 billion); and the country's oldest bank, Bank of the Philippine Islands (₱581 billion), controlled by the Ayala family.

Sy has set his sights on tourism, an industry that has become his latest passion. In March 2007, SM Investments launched the 1,700 hectares Hamilo Coast in Nasugbu, Batangas



> *"You cannot stop a leader if someone wants to become one. But it is important that the power is divided among the siblings."*

facing the South China Sea, its first large-scale tourism development where it has committed to spend ₱5.5 billion in the next five years in the first phase of its development.

His group also has a nearly 11% stake worth US$500 million in San Miguel Corporation, the largest food and beverage company in Southeast Asia. With San Miguel now in play following the government's intention to dispose of its 24% stake later this year, Sy's SM is in a happy predicament of either cashing in on a sale jointly with the government to a strategic investor or itself making a bid to take over San Miguel.

It is an extraordinary outcome for a journey that began 70 years ago when Sy first arrived in the Philippines from Jinjiang, China, speaking not a word of English or Tagalog, the local dialect. That journey took him from helping in his father's store, which was making ₱40 a month, to starting out on his own as a small-time shoe retailer in post-war Philippines and to becoming the country's business icon with the SM malls—usually designed as no-frills rectangular concrete structures—ubiquitous in the major urban centres.

Ranked as the richest man in the Philippines with a total wealth of US$4 billion last year according to Forbes, a US-based business publication, Sy's incredible fortune comes not from any particular manner of doing business but more from exceptional foresight in spotting business possibilities—often decades ahead —and then applying his mind, energy and resources to making them happen.

"A lot of people are surprised with the number of businesses we are in," says Sy. "*We are practically in everything—department stores, construction materials, electronics and others. You cannot just depend on what is happening; you should always be ahead. Many of the things that we do are not according to market trends."*

This sense of adventure and with it his gumption —from convincing his mother to allow him to join his father in the Philippines when he was just 12 years old to his first trip to America in 1955—have enabled Sy to make bold bets that have turned up trumps.

Sy describes this first trip to New York as his *"biggest chance"*. The 1950s Eisenhower era in post-war America was also the period marking the return of the feel-good consumer society in the US following the traumatic Depression and the war years; of rock and roll and Elvis Presley; and the emergence of suburbia living as GI troops returned home.

At the time, the trip from Manila to New York took 46 hours with stops in Guam, Wake Island, Honolulu, San Francisco, and Chicago. *"I did not know anyone when I went on my first trip,"* says Sy. *"Shopping malls in the US were just being developed; I saw so many things and I knew they could be adapted to the Philippines."* That first trip was to leave a lasting impression.

Fast forward to the early 1980s—possibly the darkest period for the Philippines. It was the aftermath of the second oil crisis and the country was reeling from the its effects. In 1981, Dewey Dee, a former industrialist, absconded to Canada leaving in his wake more than ₱600 million in debt, which shut down the commercial paper market and led to a banking crisis. Two years later, a political crisis added to the country's economic woes with the assassination of Benigno Aquino, Jr., the opposition leader. Interest rates shot up to 45%.

Dire Situation

SY RECALLS BEING AT THE FORMER HILTON HOTEL (now Manila Pavillon) in downtown Manila where businessmen used to congregate. *"A lot of people were talking about running away,"* he remembers. The situation was dire. Inflation was at over 17%; the peso exchange rate to the US dollar was tumbling. It came as a complete surprise then when he approached an official of the GSIS, the government pension fund, whom he had known casually at the Hilton gatherings, and asked him: *"I am interested in buying your property."*

Sy was referring to a piece of land along the north of EDSA, the main thoroughfare in Metro Manila, which he had been eyeing whenever he was en route to Baguio, the summer capital of the Philippines. *"Apart from the hollow blocks fencing it, and with a big sign that says 'private property' there was no development,"* Sy says. *"It was hardly a business or commercial location."* At first,

SPECIAL FEATURE

"Our structure is to have the family in control. And they (the children) are all in positions of responsibility."

he says, the GSIS executive felt slighted by Sy's direct approach. *"We did not even have any small talk first,"* Sy recalls. GSIS then had its hands full, including dealing with Philippine Airlines (PAL) which it had taken over at the behest of then President Ferdinand Marcos and which was on the brink of financial collapse.

THAT INITIAL MISSTEP COULD HAVE SCUPPERED what would later turn out to be his first SM Mall project. *"That official was really not happy and I thought I knew him well."* Sy says he had to somehow appease him; he explained that he was not criticizing the fund and that he was just keen to acquire the property—as GSIS may need the cash to shore up PAL. In the end, the official calmed down and a deal was struck.

Launching what was then one of the biggest construction projects, SM North EDSA, it was no surprise that many thought he was crazy. The year that it opened in 1985, the Philippines' GDP had shrunk by 7% after having declined by 7.3% in the previous year—the two worst years in the country's recent history. Inflation touched over 47% in 1984 and 23% in 1985. Three months following its grand opening in November, the Marcos regime collapsed.

Sy describes this first mall project as *"one of those opportunities." "I had putting up a shopping mall in mind. But at the same time, you need a large location; you need investments. But during the construction period no one believed me—that it would be a viable business location."* Within a few weeks of opening the mall, Sy says that commuters who were passing through from the north of Manila as well as the south started visiting the shopping mall.

Of course, nothing is ever that simple. It would take Sy the next five years to perfect his mall strategy during which time he did not venture to build a new one. *"We always think ahead of what is going to happen,"* he says. *"Planning is very important; if you don't have a plan, you won't have a direction."*

But Sy continued to acquire land and properties most notable of which included a historic hotel, the Taal Vista Lodge, in Tagaytay and a prime site in Baguio, which used to be the Pines Hotel and now the location for SM Baguio, completed in November 2003.

Now, 27 malls later with average daily foot traffic of two million visitors in all the malls, generating some ₱13.2 billion in revenues, net profit of over ₱5.4 billion and with an EBITDA (earnings before interest, taxes, depreciation and amortization) margin of 71% at the end of last year, Sy has transformed the landscape of retailing in the country and made himself and his family fabulously wealthy.

His push into tourism is in part to strengthen the operations of his shopping malls. As a strategy, Sy believes that it made sense to put up tourism infrastructure such as hotels and amusement facilities next to the malls as to attract more visitors. But he is also a staunch believer that the country—with its beautiful coastline and mountains; and its people —warm, gentle and smiling – are the main draw and they will make the Philippines the best destination for tourism.

It has not always worked as planned. Sy's first attempt to link a hotel complex next to his SM Mall in Cebu was hit by the Asian financial crisis. The 400-room hotel was nearly completed and was supposed to have been operated by the Sheraton group. Rather than going ahead with its opening, Sy decided to complete the structure but without the fittings and wait for a better time to open it. *"That was not a cheap development,"* Sy points out. The architect hired, Wimberly Allison Tong & Goo, is one of the world's leading leisure and entertainment design firms with prestige projects such as the Sheraton Maui Hotel, Hotel Bora Bora and The Mansion at MGM Grand in Las Vegas.

Sy says his decision to delay the hotel's opening is not because of any issues relating to the financing. *"We have to make sure that we hand it over to somebody who will take care of the property,"* he says. SM is now set to open the facility after it signed a deal in May 2007 with the Paris-based Accor Group to operate a Sofitel. The hotel opening is expected in the next 12 to 14 months. In its SM BayCity (Mall of Asia Complex) development, Sy has tapped the Carlson Group to operate a Radisson Plaza.

Sy does not give up easily. Indeed, he says that he has never walked away from a deal he has set his sights on. But before going into battle, he believes it is important to have both the faith and the resources in place. *"You have to be strong otherwise with a little push, you are out,"* he says. *"You must also be ready from A to Z."*

This may explain how SM doggedly pursued its goal to acquire Equitable PCI Bank, a takeover saga that started in 2004 and became the Philippines' largest M&A deal in 2006. SM's first big break was in August 2005 when the Sy family succeeded in convincing the Go family, founders of Equitable, to sell its 24.76% stake at ₱56.50 a share for a total of ₱10.2 billion.

The next phase quickly turned messy as both GSIS and the Romualdez family, which held large blocks of shares in Equitable PCI Bank, made it plain that they opposed the merger that SM had proposed in January 2006. SM had offered a share swap of one Equitable share for every 1.6 BDO share, which was rejected by the two camps.

Legal issues relating to SM's previous attempts to acquire additional shares from another pension fund, the Social Security System, also hounded the deal. Months of M&A posturing to buy the stake held by SM Investments in Equitable PCI Bank at ₱79.50 a share, entertained and enthralled a market that had not witnessed the likes of a corporate battle for a long time.

IN THE END, IT WAS A MATTER of price. In September 2006, GSIS agreed to the sale of its stake to SM Investments at ₱92 a share raising Sy's stake to 46.7% and paving the way for a tender offer for the remainder of shares not owned by the SM group. Through the twists and turns and ups and downs, Teresita, Sy's eldest was in the driver's seat—testing her mettle in a very public manner—unusual for the Sy family, which has preferred to do its deals in private.

But it also marks the coming out of the children, especially Teresita. For long, quietly and diligently working under the shadow of their larger-than-life father, the six siblings are now very much in control of the day-to-day activity of the SM group. Indeed, when pressed on why he seemed so determined to acquire Equitable PCI Bank, Sy says: *"It is not just me; it is also my children."*

The children—Teresita, Elizabeth, Henry Jr., Hans, Herbert and Harley—have been handling different parts of the Sy empire. Teresita plays a big part on the banking side while Elizabeth is much more involved in the tourism and leisure business; Henry Jr. takes care of the group's real estate activity while Hans handles mall operations as well as engineering and construction; Herbert takes charge of the supermarket operations while the youngest, Harley looks after the finances and is also the president of SM Investments.

Sy views the family as vital to SM group's long-term success and he does not intend to change it. *"Our structure is designed to have the family in control,"* he says. *"And they [the children] are all in positions of responsibility. We have to put the right person in the right position."*

Like many family businesses in Asia, Sy sees the family as providing continuity and stability in the activity of the group. Hiring professional managers is fine, he says, *"[but] you have to be careful as there is no certainty they will stay."*

Sy is also of the view that in-laws should not be involved in the family business. *"The reality is that there are good in-laws and there are bad ones. When siblings quarrel, they eventually make up. With in-laws, it is more difficult to handle because pride is involved—not [necessarily] because they are not good in [their] business. I am happy to help them [the in-laws]—that's ok. We help others so why not help your in-laws?"*

While he is still involved in running the group, Sy's role is now much more strategic—providing direction and the vision, and managing his children—how they can work together. *"It is the hardest job,"* says Sy, perhaps only half in jest. *"But that is the only way to keep the family business."* He says a lot of people are watching and trying to find out how he is doing it. And he is showing them.

Will any of his children become his successor? *"You cannot stop a leader if someone wants to become one,"* says Sy. But it is important that *"power is divided among the siblings."* A family board, which meets almost weekly, is now in place and handles many of these issues. Sy says he is happy with the set-up. *"It proves that [a family-led business] is possible,"* he adds. *"It is still working."*

As a brand, the SM malls may not be perceived in the same way as the upscale malls of rival Ayala, perhaps a reflection of Sy's humble beginnings—selling shoes, the most basic of needs. But this is part of Sy's business sense. Painted on fine china that sits proudly in an ante-room, in his own writing and in Chinese words—fortune comes when you satisfy people's needs. It is also a strategy, which has drawn and touched the lives of the greatest number of Filipinos, especially the middle class. And it is this group of up-and-coming consumers, through the billions of dollars of overseas worker remittances flowing into the country and the rise of call centres and BPOs (business process outsourcing), which now have seen a dramatic rise in income—and shopping power. And when Sy builds the next mall, they will come.

Corporate Governance

SM INVESTMENTS CORPORATION (SM) FIRMLY BELIEVES IN AND ADHERES TO SOUND CORPORATE GOVERNANCE. THE COMPANY GIVES UTMOST PRIORITY TO CORPORATE TRANSPARENCY AND PUBLIC ACCOUNTABILITY IN ALL OF ITS UNDERTAKINGS.

AS SUCH, SM DEVELOPED AND FOLLOWS A REVISED MANUAL ON CORPORATE GOVERNANCE (CG MANUAL). THE BOARD OF DIRECTORS AND MANAGEMENT OF SM COMMIT THEMSELVES TO THE PRINCIPLES AND BEST PRACTICES CONTAINED IN THE CG MANUAL, AND ACKNOWLEDGE THAT THESE TENETS GUIDE THE ATTAINMENT OF THEIR CORPORATE GOALS.

PRESENTED BELOW ARE HIGHLIGHTS OF SM'S CG MANUAL.

Objective

The CG Manual shall institutionalize the principles of good corporate governance in the entire organization.

The Board of Directors and Management, employees, and shareholders believe that good corporate governance is a necessary component of what constitutes sound strategic business management and therefore undertake every effort necessary to create awareness for it within the organization.

Compliance System

COMPLIANCE OFFICER

To ensure adherence to corporate principles and best practices, the Chairman of the Board designated a Compliance Officer who holds the position of at least a Vice President or its equivalent. The Compliance Officer has direct reporting responsibilities to the Chairman of the Board and performs the following duties:

- Monitors compliance with the provisions and requirements of the CG Manual
- Appears before the Philippine Securities and Exchange Commission (SEC)
- Determines violations of the CG Manual and recommends penalty
- Issues a yearly certification on the extent of SM's compliance with the CG Manual and explains any deviation, and
- Identifies, monitors, and controls compliance risks.

BOARD OF DIRECTORS

Compliance with the principles of good corporate governance starts with the Board of Directors, which is currently composed of seven directors, one of whom is an independent director.

It is the Board's responsibility to foster SM's long-term success and secure its sustained competitiveness in a manner consistent with its fiduciary responsibility, which it shall exercise in the best interest of the company, its shareholders, and other stakeholders. The Board conducts itself with utmost honesty and integrity in the discharge of its duties, functions, and responsibilities.

General Responsibility

A director's office is one of trust and confidence. He acts in a manner characterized by transparency, accountability, and fairness.

Specific Duties And Functions

To ensure a high standard of best practice for SM and its stakeholders, the Board:

- Installs a process of selection to ensure a mix of competent directors and officers
- Determines SM's vision and mission and strategies to carry out its objectives
- Ensures that SM complies with all relevant laws, regulations, and codes of best business practices
- Identifies SM's major and other stakeholders, and formulates a clear policy on communicating or relating with them through an effective investor relations program
- Adopts a system of internal checks and balances
- Identifies key risk areas and key performance indicators and monitors these factors with due diligence
- Properly discharges Board functions by meeting regularly. Independent views during Board meetings are given due consideration and all such meetings are duly recorded
- Keeps Board authority within the powers of the institution as prescribed in the Articles of Incorporation, By-Laws and in existing laws, rules, and regulation.

Duties and Responsibilities of a Director

A director has the following duties and responsibilities:

- Conducts fair business transactions with SM and ensures that personal interests do not bias Board decisions
- Devotes time and attention necessary to properly discharge his duties and responsibilities
- Acts judiciously
- Exercises independent judgment
- Has a working knowledge of the statutory and regulatory requirements affecting SM, including the contents of its Articles of Incorporation and By-Laws, the requirements of the SEC, and where applicable, the requirements of other regulatory agencies
- Observes confidentiality
- Ensures the continuing soundness, effectiveness, and adequacy of SM's control environment.

BOARD COMMITTEES

To aid in complying with the principles of good corporate governance, the Board has constituted the following Committees:

NOMINATION COMMITTEE

The Board created a Nomination Committee, which has at least three voting directors (one of whom must be independent) and one non-voting member in the person of the HR Director or Legal Manager.

The Nomination Committee pre-screens and shortlists all candidates nominated to become a member of the board of directors, in accordance with stipulated qualifications and disqualifications.

The company gives utmost priority to corporate transparency and public accountability in all of its undertakings.

COMPENSATION AND REMUNERATION COMMITTEE

The Compensation and Remuneration Committee is composed of at least three members, one of whom is an independent director, and has the following duties and responsibilities:

- Establishes a formal and transparent procedure for developing a policy on executive remuneration and for fixing the remuneration packages of corporate officers and directors, and provide oversight over remuneration of senior management and other key personnel ensuring that compensation is consistent with SM's culture, strategy, and control environment
- Designates the amount of remuneration, which shall be in a sufficient level to attract and retain directors and officers who are needed to run the company successfully
- Develop a form on Full Business Interest Disclosure as part of the pre-employment requirements for all incoming officers, which among others compel all officers to declare under the penalty of perjury all their existing business interests or shareholdings that may directly or indirectly conflict in their performance of duties once hired
- Disallow any director to decide his or her own remuneration
- Provide in SM's annual reports, information, and proxy statements a clear, concise, and understandable disclosure of compensation of its executive officers for the previous fiscal year and the ensuing year
- Review the existing Human Resources Development or Personnel Handbook, to strengthen provisions on conflict of interest, salaries and benefits policies, promotion and career advancement directives and compliance of personnel concerned with all statutory requirements that must be periodically met in their respective posts.

AUDIT AND COMPLIANCE COMMITTEE

The Audit and Compliance Committee is composed of at least three members of the Board, one of whom shall be an independent director. Each member has adequate understanding, at least, or competence, at most, of the company's financial management systems and environment.

The Audit Committee has the following duties and responsibilities:

- Checks all financial reports against its compliance with both the internal financial management handbook and pertinent accounting standards, including regulatory requirements
- Performs oversight financial management functions specifically in the areas of managing credit, market, liquidity, operational, legal and other risks of SM, and crisis management
- Pre-approves all audit plans, scope, and frequency one month before the conduct of an external audit
- Performs direct interface functions with the internal and external auditors
- Elevates to international standards the accounting and auditing processes, practices, and methodologies
- Develops a transparent financial management system that will ensure the integrity of internal control activities throughout the company through a step-by-step procedures and policies handbook, which will be used by the entire organization.

THE CORPORATE SECRETARY

The Corporate Secretary has the following duties and responsibilities:

- Gathers and analyzes all documents, records, and other information essential to the conduct of his duties and responsibilities to the company
- Gets a complete schedule of the agenda at least for the current year and puts the Board on notice before every meeting
- Assists the Board in making business judgment in good faith and in the performance of their responsibilities and obligations
- Attends all Board meetings and maintains records of those meetings
- Submits to the SEC, at the end of every fiscal year, an annual certification on the attendance of the directors during Board meetings.

EXTERNAL AUDITOR

An external auditor is selected and appointed by the stockholders upon recommendation of the Audit Committee. If an external auditor believes that the statements made in the company's annual report, information sheet, or proxy statement filed during his engagement are incorrect or incomplete, he shall present his views in those reports.

INTERNAL AUDITOR

SM has in place an independent internal audit function which is performed by an Internal Auditor, through which its Board, senior management, and stockholders are provided with reasonable assurance that its key organizational and procedural controls are effective, appropriate, and complied with. The Internal Auditor reports to the Audit Committee.

SPOTLIGHT

Meet SM's Money Man
Jose T. Sio

Jose T. Sio was featured in the Cover Story of CFO Asia in November 2007

AMONG THE MANY STRENGTHS OF SM IS ITS STRONG AND SOUND FINANCIAL POSITION. AMONG THOSE RESPONSIBLE FOR KEEPING THE COMPANY'S FINANCES AND PROFITABILITY IN CHECK IS SM'S CFO, KNOWN BY MANY AS JTS. WE SAT WTIH HIM AND GOT A FEW OF HIS INSIGHTS.

When did you assume the position of chief financial officer (CFO) for the company?
I became CFO of SM Investments Corporation (SMIC) when it was listed at the Philippine Stock Exchange in 2005. Prior to the company's public listing, I was already supervising its treasury and accounting departments. At that time, I was also the CFO of SM Prime Holdings, Inc.

What are your specific roles and responsibilities as a CFO?
As CFO, I make sure that the company safeguards its assets. I also maximize its financial potential. I ensure that the company is ready and liquid enough to finance its expansion programs.

Which among your past work experiences greatly helped in your current work as a CFO?
I think it's my work with Sycip, Gorres, Velayo & Co. (SGV), where I was the senior audit partner. As such, I led the auditing of various local and international companies, some of which were conglomerates. Also, my work exposure abroad, primarily in the US and Taiwan helps a lot.

What process do you employ in managing the company's resources?
I follow a hands-on process or management system. Under that kind of process, I make sure that everybody in the organization understands the objective and the mission of their respective departments, in relation to the broader vision of the company.

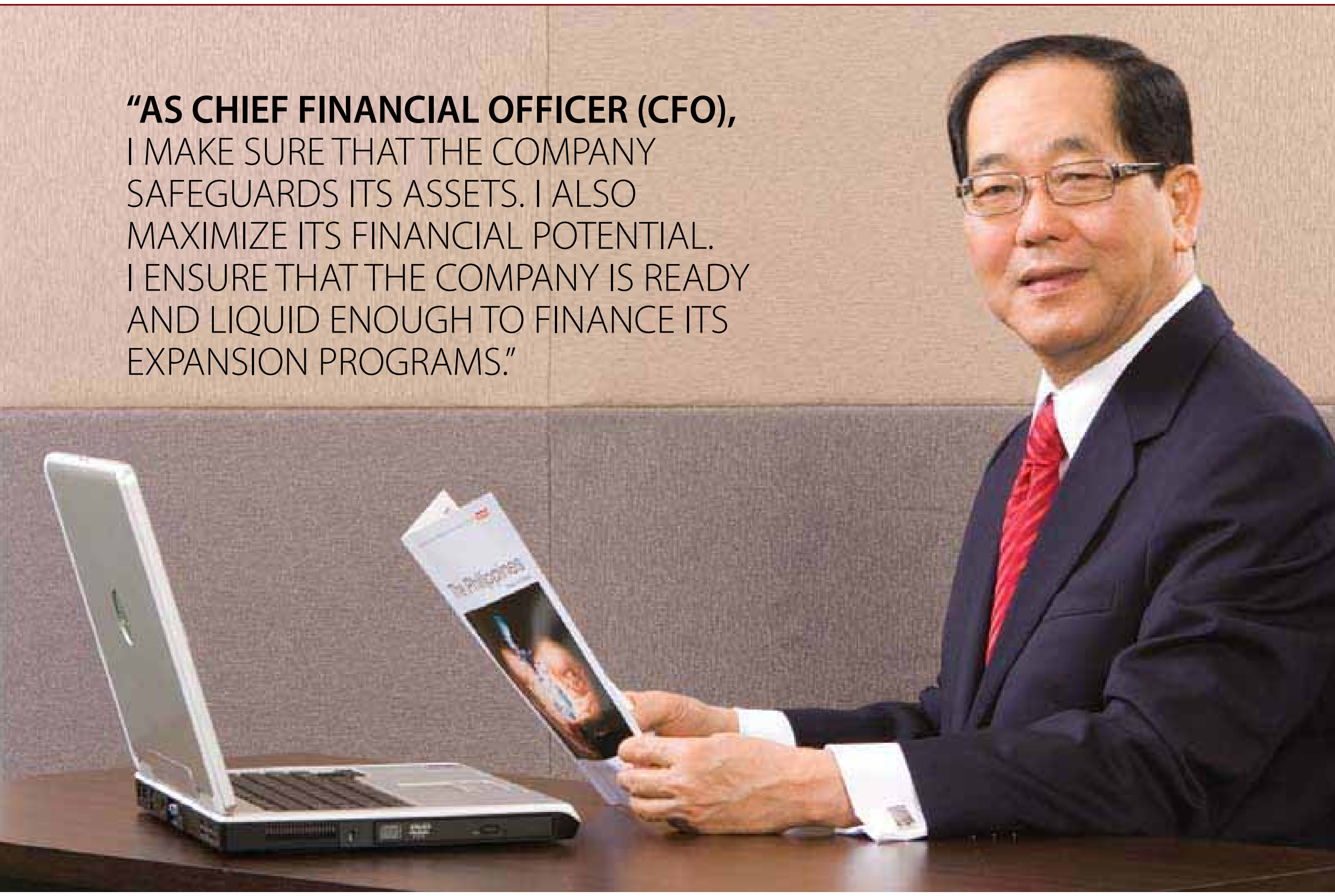
Also, there is a need for constant communication with various department heads. I want to know what's going on in each of the departments to avoid surprises. That way, potential problems are known beforehand and solutions are developed.

When reviewing the available options for financing, what factors do you consider before finally selecting an option?
There are various kinds of financing, and each financing scheme will have its own set of advantages and disadvantages. So a company should know what they really need, whether or not it's for long, medium, or short-term financing.

All these have an impact on the kind of financing that you will choose. So it is not just a matter of which financing is the cheapest, but also the quality of the services and the type of financing that are being offered by banks or other financial institutions.

What would you consider as your greatest contribution to the company?
I think my greatest contribution applies not only to SMIC but to the SM Group as well. I feel that I have substantially built up the Group's goodwill and I have raised its standards to a level that is acceptable in the international market. Consequently, we were able to go through several public listings.

I also feel that I have greatly contributed in looking for the right financing option and source for its expansion. Furthermore, I feel that I have contributed to improving the professionalism within the Group, especially by bringing in highly professional employees.



"AS CHIEF FINANCIAL OFFICER (CFO), I MAKE SURE THAT THE COMPANY SAFEGUARDS ITS ASSETS. I ALSO MAXIMIZE ITS FINANCIAL POTENTIAL. I ENSURE THAT THE COMPANY IS READY AND LIQUID ENOUGH TO FINANCE ITS EXPANSION PROGRAMS."

CORPORATE GOVERNANCE

Spotlight

Thus far, how would you describe your experience as the company's CFO?

I would say that I am very satisfied with the work that I have done for SMIC. I appreciate the fact that I am trusted by the company. I am also thankful that in the SM environment, you are given an opportunity to excel within your field of expertise.

It satisfies me more when I look at the company's accomplishments over the last ten years, from where it was then to where it is today.

As a CFO, what are your views on corporate governance?

To me, corporate governance is very important. Of course, we should always be transparent and fair with all our stakeholders. But I think beyond that, corporate governance should have four aspects: one is for our shareholders, we should be transparent to them and we should earn adequate income for them. Second is for our suppliers. We should be fair to them and view them as our partners. The third aspect is for our creditors. We should make sure that we pay them on time and we must not take advantage of them. Fourth is for our workforce, we should always treat them fairly and professionally.

How big a role does a CFO have in terms of corporate governance?

I think the CFO has a very big role in ensuring that good corporate governance is practiced. This is because most if not all transactions within the corporation are monetary in nature. You produce, you sell, and then you collect, so it's all based on money or cash. And one of the CFO's major responsibilities is to safeguard the company's resources, including the cash.

In addition, transparency falls under my jurisdiction as the CFO because the company's financial management, especially the financial statements and reports are my responsibilities. So, the CFO is a key driver to a company's good corporate governance.

What initiatives have you undertaken to pursue sound corporate governance?

One is to inculcate within ourselves good corporate governance. We want our executives to be good role models for transparency to the rest of the workforce. They must also exercise fair judgment in all aspects of their work. This way, good corporate governance will trickle down and everyone in the organization eventually practices it.

We also lead by example and we avoid conflicts of interest in our organization. We want each transaction to be transparent to everyone. It is not only known to one, but to all. We also make sure that in our frequent conversations, in our regular contact with the various executives, corporate governance is discussed.

Also, SM's Board of Directors appointed two consultants. Mr. Stephen CuUnjieng, MacQuarie's Vice Chairman for ASEAN Corporate Finance, is now the Board's consultant for international capital markets. Mr. Ricardo Manabat, on the other hand, was appointed as consultant for corporate governance. Mr. Manabat is currently the Chairman and CEO of KPMG in the Philippines. Both consultants are tasked with advising the Board of ways to further improve SM's capital market transactions for Mr. CuUnjieng and further strengthen SM's corporate governance practices for Mr. Manabat.

Do you see the traditional roles and responsibilities of a CFO changing in the near future?

I think it's now changing more and more. You will see that the CFO will be more involved, not only in the traditional fields of treasury and accounting, but in the other aspects of the business such as risk management, investments, and expansion programs, as well.

CFOs will also have a deeper involvement in the company's day to day operations.

How was the past year (2007) for the company?

2007 was a good year. We saw during the year just passed the fruits of what we have been doing for the last five years. It started to bear fruits and this will continue in 2008 and beyond. We also saw in 2007 a big boost in our property division, both in implementing projects and in increasing its human resources.

How do you view 2008?

2008 will be a little difficult on the macro level because of what is happening worldwide, especially in the US. But the feeling is that if the US government will continue to make the correct decisions, the US economy will start to normalize and correct itself.

On the micro level, I am not worried because I know SM can withstand the shocks. It has been shown and proven in the past that the SM Group thrives and sees opportunities during crises. Furthermore, we have a very strong balance sheet, and a very hands-on management team. We can adapt to any changing environment.

SM'S CONVERTIBLE BONDS:
A Landmark Offering

THE EARLY PART OF 2007 WITNESSED SM INVESTMENTS CORPORATION (SM) EMBARK ON YET ANOTHER MILESTONE INITIATIVE. In mid January, SM's board of directors announced its approval to issue US$200 million worth of five-year convertible bonds or CBs. Simply defined, CBs are bonds or 'IOUs' that could be exchanged for shares of stock of the issuing company, subject to predetermined terms and conditions, such as price and date.

SM's issuance of the CBs, with the Citigroup and Macquarie Securities Asia Ltd. serving as joint lead issue managers, was the largest ever made by a Philippine company and the country's first in over a decade, indelibly marking it as a historic financial undertaking.

SM's convertible bonds was awarded by international publication, FinanceAsia as the "Best Philippines Deal for 2007."

The company issued the bonds at a time when its stock price was hitting all-time highs due to a series of positive corporate developments such as the consolidation into the company of the assets and operations of SM Supermarkets and SM Hypermarkets. In addition, it came at the heels of the approval, by the stockholders of SM subsidiary Banco De Oro and Equitable PCI Bank, of the two financial institutions' merger.

As a result, investors from various parts of the globe eagerly reacted to the CBs, making the bonds oversubscribed. Mr. Jose T. Sio, SM's Executive Vice President and Chief Financial Officer said, *"The issue was 10 times oversubscribed, allowing SM to command the best terms to date for the issue."* This overwhelming response prompted SM to expand the amount to US$300 million, from the original offer size of US$200 million, through the use of what is called the 'green shoe' option.

SM earmarked the proceeds of the CBs to refinance a portion of its maturing obligations and for general corporate purposes. Mr. Sio further explained, *"SM embarked on several large scale property projects necessitating substantial capital expenditure. Thus, the bond proceeds will be utilized for, among others, Mall of Asia Complex, which is a 60-hectare emerging business district along Manila Bay and is the home of SM's flagship mall, the Mall of Asia, and for SM's Hamilo Coast, which is an eco-tourism network of coastal resort communities south of Manila."*

This is SM's third year in a row to receive the Best Philippine Deal Award from Finance Asia. The first was in 2005 which involved the initial public offering of SM Investments Corporation. The second was in 2006 which involved the issuance of US$115 million in Global Depository Receipts for Banco de Oro with the objective of creating greater liquidity of the shares for foreign investors.

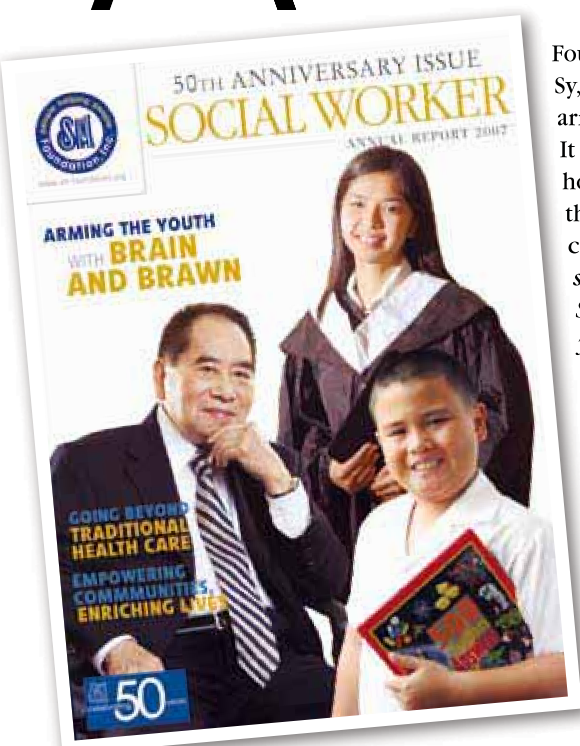
SM's US$ 300 million Convertible Bond issue garnered the 2007 Best Philippines Deal Award from FinanceAsia.

CREATING WAYS FOR PEOPLE TO HELP PEOPLE:

SM and Filipino Bayanihan

(An excerpt from the SM Foundation Annual Report)

ARMED WITH DEEP COMMITMENT, SINCERITY AND A PASSION FOR service, SM Foundation, Inc. (SMFI) strives to live up to its mission to help thousands of disadvantaged who are deprived of opportunities for a brighter future.



Instituted in March 1983 by SM Founder and Chairman Henry *"Tatang"* Sy, Sr., SMFI is the social action arm of the SM group of companies. It aspires to uplift lives by taking a holistic approach in responding to the social needs of underprivileged communities. *"This is our way of sharing the many blessings that the SM Group has received for so many years,"* Tatang says.

For more than two decades, SMFI unceasingly envisions itself as a channel for shoppers, employees, government and non-government organizations, media and companies to reach out to the needy. Now, on its golden anniversary, SM intensifies corporate social responsibility by allocating ₱50 million more for its projects—almost doubling the budget for CSR.

The Foundation sets its eyes on the following four core advocacies: Education, Health and Medical missions, Mall-based Outreach, and Community projects.

Education advocacy, formally established in 1993, provides quality education to underprivileged but deserving students through the College Scholarship Program. To date, SMFI has produced 974 graduates coming from communities where SM malls are located all over the country: the National Capital Region, Pampanga, Baguio, Batangas, Bulacan, Lucena, Cavite, Laguna, Rizal, Bacolod, Cebu, Iloilo, Davao and Cagayan de Oro.

Advancing public education's furtherance and modernization, SM Prime Holdings Inc. using SMFI as its vehicle has built 17 schoolbuildings in public schools and has donated close to three million books supported by the Mall-based Outreach Donate-A-Book program.

Encouraging health, multi-sectoral coordination and community participation, the Health advocacy program, since 2001, has already conducted 315 medical and dental missions benefiting over 200,000 individuals. The Foundation acquired two Mobile Clinics in 2001 and 2007. Stationed in SM malls, they are equipped with up-to-date medical technologies to perform basic diagnostic tests for shoppers and by-standers. Aiming to not only heal but also provide a therapeutic environment for patients, SMFI has built a total of 36 wellness centers including pediatric activity centers, health centers, elderly centers and hospice units.

A series of quarterly mall-based programs—Share Your Extras, Donate-A-Book, Gamot Para Sa Kapwa and Make A Child Happy—enable shoppers, private companies and organizations to share what they have. Collection centers in the malls gather clothing, books, medicines and toys to be distributed in depressed communities. Book and medicine donations are channeled through SMFI's Education and Health missions.

SM Kabalikat Sa Kabuhayan Livelihood Program provides hands-on hybrid vegetable and fruit training to farmers and conducts Trade Fairs for micro entrepreneurs to showcase their businesses and marketing competencies and to tie-up with mainstream suppliers, thus improving standards of living.

Underscoring the importance of spiritual well-being, SM fervently supports the religious community by constructing and renovating churches. Conducting its own religious activities and celebrating Sunday masses in all SM malls, SM brings spirituality to the multitude.

In partnership with Gawad Kalinga, SM has built over 80 houses in the SM Gawad Kalinga Village for homeless families.

Special projects allow for the Foundation to render quick-response to victims of disasters with Operation: Tulong Express. Providing basic assistance and distributing donations from shoppers and sponsors, the Foundation has aided victims of tragedies such as the mudslide in Southern Leyte, the evacuation of thousands of families in Albay due to a seismic activity, and a medical mission for the affected families of the Guimaras oil spill, among other calamities.

People helping people is the philosophy that guides SM Foundation and its social soldiers—acknowledging the biblical precept that we are, indeed, our brothers' keepers.

ENABLING THE DISABLED: *A Look Into the Heart of SM Malls*

(An Interview with Ms. Annie Garcia)

WHO WOULD EVER THINK THAT SM, WHICH IS MORE KNOWN FOR ITS stores and malls, will someday be invited to an international forum that tackles programs for Persons With Disabilities or PWDs?

Well, that opportunity came by last June 2007, when SM Supermalls presented its plans and programs for PWDs at a conference that was sponsored by no less than the United Nations Economic and Social Commission for Asia and the Pacific (UNESCAP). The event was held in Bangkok, Thailand where delegates from both developed and developing countries acclaimed SM's initiatives.

We talked to Ms. Annie Garcia, the President of SM Prime's Shopping Center Management Corporation who gave us a moving story about the heart of SM Malls.

Beginnings

According to Ms. Annie S. Garcia, President of Shopping Center Management Corporation, an SM subsidiary that manages SM Malls, it was five years ago that the company more vigorously implemented measures for, and heightened their sensitivity to, the special needs of PWDs.

Ms. Garcia shares a poignant story:

"From the beginning, SM Malls had always been compliant with the requirements of the handicapped, in as much as we had to conform to the National Building Code of the Philippines. It was in the law, and we followed it. But there was an incident some time in 2003 that sort of elevated our consciousness regarding PWDs.

"One day, a mother and her autistic son were accidentally separated from each other in one of our malls. The frantic mother went to the customer service counter and reported the incident. The mall's entire security staff was alerted by radio and a search was started. Initially, amidst the confusion and the crowds, the son could not be found.

"Later on, however, one of the mall guards saw a boy repeatedly banging his head against a display window. Fortunately and to the great relief of the mother, that boy, all safe and sound, proved to be her son."

Going Beyond The Stereotype

The incident made Ms. Garcia and the rest of the mall management realize that persons with disabilities go beyond those who could not see, walk, or hear.

Ms. Garcia continues, *"It opened our eyes to the fact that there are other forms of disability, which we as operators of the malls must be aware of. There is a wide range of conditions such as autism, Down Syndrome, and attention deficit hyperactivity disorder or ADHD, each having its own special requirement. We thereafter consulted various organizations like the National Down Syndrome Society and the Philippine Autism Society to gain much-needed knowledge on these conditions."*

Commitment To Serve And Understand

The challenge then was how to make the mall environment more PWD-friendly. Thus, committees were formed to ensure the welfare of all mall-goers with special needs. Aside from the handicapped, committees were formed for women, children, the elderly, and even for breastfeeding.

From then on, efforts to address the needs of PWDs went way beyond the perfunctory. As a matter of fact, a deep culture of service and understanding for PWDs evolved within the company.

With this culture and thinking spreading across the malls, various innovations and retrofitting were undertaken.

For instance, the malls adjusted their toilet facilities, parking areas, corridors, and pay phones, among others, to better suit PWDs. SM supermarkets and hypermarkets inside the malls established priority checkout lanes for the handicapped, and even for senior citizens. Signages and stickers, which request the public to give priority to PWDs, were installed in elevators and ramps.

Consequently, SM malls created a "nonhandicapping" or barrier-free environment for PWDs.

The steps taken and the improvements put in place made the malls adhere better to the Magna Carta for the Disabled, the lead government agency for which is the Department of Social Welfare and Development (DSWD).

"We used to just make a listing of handicap facilities our malls had. And these

> *"What is truly important for us is that our efforts and advocacy allow us to welcome everyone to our malls. We do not exclude anyone from experiencing our malls just because of their disabilities. We are able to serve all members of a family, and it is a service that comes from the heart."*

Ms. Annie Garcia
President of Shopping Center Management Corporation

were just the standard facilities enumerated in the Building Code.

"We have, however, taken a more pro-active posture. Our committees often meet and discuss what enhancements to our existing facilities must be done. Regular, comprehensive audits are undertaken. We consult with the DSWD, local governments, and the various PWD associations. We make sure that SM malls under construction will have facilities that effectively address the needs of the disabled. Our architects, engineers, and designers are now more attuned to these special needs," Ms. Garcia added.

Training The Company's Greatest Asset

In its sincere desire to further enhance its service to PWDs, SM went beyond the improvement of its physical facilities and infrastructure. It focused on its most important asset – its human resources.

SM mall employees had to be aware of and be able to identify the different types of disabilities. More important, they had to know how to properly relate to people who have these disabilities. The mall workforce had to be trained and sensitized.

Ms. Garcia said, *"We instituted a training program not only for our own employees, but also for those of our tenants. These training sessions educate our workforce on how to properly assist PWDs. We even came up with a video presentation, which must first be viewed by a new employee, before his or her ID card is released. The video serves as a convenient, cost-effective training tool and is disseminated to all our malls."*

Frontline staff such as security guards, cashiers, and janitors are gathered at least once a month to make sure that their information and education on PWD-related issues are current. From time to time, guest speakers, such as members of the National Council for the Welfare of Disabled Persons (NCWDP), are invited to share their expertise on these issues.

Innovating Beyond The Expected

Today, as earlier related by Ms. Garcia, SM goes beyond the minimum legal requirements for PWDs. Other related issues and concerns are addressed as well inside SM malls.

For instance, there is the women's sector, and a truly noteworthy innovation implemented for them is the setting up of breastfeeding stations in SM malls. Nursing mothers could now attend to their babies in the privacy and convenience inside these stations. At times, the SM malls also become venues for publicly discussing relevant topics such as breast cancer.

These are innovations that have made a positive and lasting impact.

Payback

When asked what sort of payback SM gets from the initiatives it has done for PWDs, Ms. Garcia replies, *"The payback goes beyond the financial. The pride we get in knowing that we are of true service to the disabled is in itself rewarding for us.*

"Of course, there are the recognition and honors we receive, such as the UNESCAP invitation to speak in their forum. We also received the government's Apolinario Mabini Award, which cited the SM Mall of Asia as the most disabled-friendly mall for 2007.

"But what is truly important for us is that our efforts and advocacy allow us to welcome everyone to our malls. We do not exclude anyone from experiencing our malls just because of their disabilities. We are able to serve all members of a family, and it is a service that comes from the heart.

"That for me is the payback," Ms. Garcia concludes.

Awards And Citations

SM Investments Corporation

Corporate Governance Asia
"Asia's Best Companies for Corporate Governance"

The Asset
Best in Corporate Governance
in the Philippines (3rd)

Finance Asia
Best Philippines Deal-US$300 Million
Convertible Bonds
Best Managed Company (2nd)
Most Committed to Corporate Governance (4th)
Best Investor Relations (4th)
Consistent Good Dividends (4th)

Management Association of the Philippines
Best Conglomerate Award for 2006 Annual Reports
Best Annual Report Awards—Finalist

SM Retail

Retail Asia Magazine
Philippines Top Retailer, October 2007

Philippine Retailers Association
SM Cebu Department Store, Outstanding Filipino Retailer in the Full Line Department Store Category, December 2007

SM Prime Holdings, Inc.

Management Association of the Philippines
Best Annual Report Awards—Finalist

Philippine Retailers Association
SM Mall of Asia, Shopping Center of the Year

Globe Business
SM Mall of Asia, Hot Zone of the Year

National Council for the Welfare of Disabled Persons
SM Mall of Asia, Most Disabled Friendly Mall (NCR)

The Philippine Business for the Environment
SM Supermalls, for organizing its Earth Day 2007 Recyclables collection events

Quezon City Chamber of Commerce and Industry
Awarded as one of the Top Taxpayers in Quezon City

The People and Municipal Government of Mexico, Pampanga
SM City Pampanga, No. 1 Taxpayer and Largest Employer in the Municipality of Mexico

Presentor at UN Economic and Social Commission for Asia and the Pacific (UNESCAP) for plans and programs for persons with disabilities

BDO

Euromoney
Best Bank

The Asian Banker
- Bank of the Year in the Philippines
- Asian Banking Leadership - Philippines—Teresita Sy-Coson, Nestor V. Tan
- Asian Banker Woman of the Year—Teresita Sy-Coson

Finance Asia
Best Investment House (BDO Capital)

SM Development Corporation

Management Association of the Philippines
Best Annual Report Awards—Finalist

China Banking Corporation

Consumers Union of the Philippines
Outstanding Commercial Bank

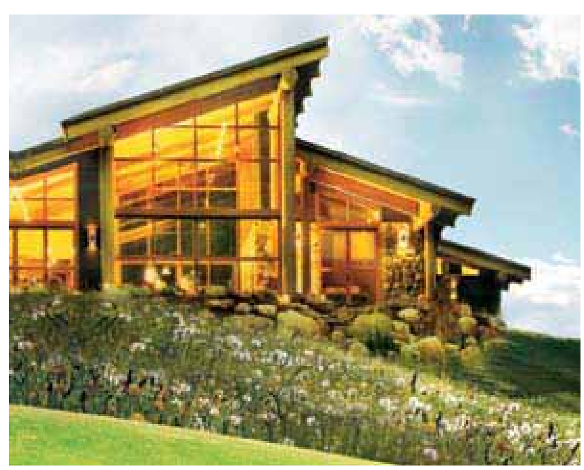
10th Philippine Web Awards
People's Choice Awardee

Management Association of the Philippines
Best Annual Report Awards—Finalist

Western Union Money Transfer and eBusiness Services, Inc.
Best Bank Sub-Agent Partner Award

Tahanang Walang Hagdanan, Inc.
Kaibigan ng Kalikasan

Coin Recirculation Project of the Bangko Sentral ng Pilipinas and Dept. of Education
Gawad Barya Citation



Highlands Prime, Inc.

Housing and Land Use Regulatory Board
Leading Developer for Condominium Development, May 2007

Housing and Land Use Regulatory Board
Best Condominium Design

Management Association of the Philippines
Best Annual Report Awards—Finalist

FACES
Board of Directors

Henry Sy, Sr., Chairman

Teresita Sy-Coson, Vice Chairperson

Henry T. Sy, Jr., Vice Chairman

HENRY SY, SR. HAS SERVED AS CHAIRMAN OF THE BOARD OF DIRECTORS OF SM SINCE 1960. He is the founder of the SM Group and is currently Chairman Emeritus of Banco De Oro Unibank, Inc., Honorary Chairman of China Banking Corporation, Chairman of SM Prime, Shoemart, Inc., SM Development Corporation and Highlands Prime, Inc., among others. Mr. Sy opened the first ShoeMart store in 1958 and has been at the forefront of SM Group's diversification into shopping malls, retail merchandising, financial services, and real estate development and tourism businesses.

TERESITA T. SY HAS SERVED AS VICE CHAIRPERSON OF SM SINCE 1979. She has varied experiences in retail merchandising, mall development and banking businesses. A graduate of Assumption College, she was actively involved in Shoemart's development. At present, she is the Chairperson of Banco De Oro Unibank, Inc., a Director of SM Prime and President of Shoemart, Inc. She also holds board positions in several companies of SM.

HENRY T. SY, JR. HAS SERVED AS VICE CHAIRMAN OF SM SINCE 1979. He is also the Vice Chairman of SM Development Corporation, Highlands Prime, Inc., Belle Corporation and Pico De Loro Beach and Country Club, Inc. and Director of SM Prime Holdings, Inc. and Banco De Oro Unibank, Inc. He is responsible for the real estate acquisitions and development activities of SM which include the identification, evaluation, and negotiation for potential sites as well as the input of design ideas. He graduated with a management degree from De La Salle University. He also holds board positions in several SM companies.

HARLEY T. SY, PRESIDENT, HAS SERVED AS DIRECTOR OF SM SINCE 1993. He is a Director of China Banking Corporation. He is also an Executive Vice President of ShoeMart, Inc. and a Senior Vice President of SM Prime. He is also a director of other companies within the SM Group. He holds a degree in Finance from De La Salle University.

JOSE T. SIO, EXECUTIVE VICE PRESIDENT AND CHIEF FINANCIAL OFFICER, HAS SERVED AS DIRECTOR OF SM SINCE 2005. He is also a Director of China Banking Corporation, Generali Pilipinas Holding Company, Inc. and SM Keppel Land, Inc. as well as other companies within the SM Group and adviser to the Board of Directors of Banco De Oro Unibank, Inc. Mr. Sio holds a master's degree in Business Administration from New York University, is a certified public accountant and was a senior partner at Sycip, Gorres, Velayo & Co.

GREGORY L. DOMINGO, EXECUTIVE DIRECTOR, HAS SERVED AS DIRECTOR OF SM SINCE 2005. He holds a master's degree in Operations Research from Wharton School, University of Pennsylvania as well as a master's degree in Business Management from the Asian Institute of Management. He has served as Undersecretary of the Department of Trade and Industry and Vice Chairman of the Board of Investments and as Board Member of

Harley T. Sy, Director

Gregory L. Domingo, Director

Jose T. Sio, Director

Vicente S. Perez, Independent Director

several government-owned and controlled corporations. He was also formerly President of Carmelray-JTCI Corporation and Managing Director of Chemical Bank in New York and Chase Manhattan Bank in Manila.

VICENTE S. PEREZ, JR.*, HAS SERVED AS INDEPENDENT DIRECTOR OF SM SINCE 2005. His career has ranged from international banker, debt trader, investment bank partner, private equity investor to Cabinet Secretary. He is one of the founding principals of Next Century Partners, a private equity firm. He was the youngest and one of the longest serving Secretaries of the Department of Energy. He had also briefly served as Undersecretary for Industry and Investments at the Department of Trade and Industry. He obtained his master's degree in Business Administration from the Wharton School of the University of Pennsylvania, and his bachelor's degree in Business and Economics from the University of the Philippines.

BOARD COMMITTEES

Compensation or Remuneration Committee

Teresita Sy-Coson	Chairperson
Harley T. Sy	Member
Jose T. Sio	Member
Vicente S. Perez, Jr. *(Independent Director)*	Member

Nomination Committee

Henry T. Sy, Jr.	Chairman
Harley T. Sy	Member
Vicente S. Perez, Jr. *(Independent Director)*	Member
Gregory L. Domingo	Member
Atty. Corazon I. Morando	Member

Audit Committee

Vicente S. Perez, Jr. *(Independent Director)*	Chairman
Henry T. Sy, Jr.	Member
Jose T. Sio	Member
Gregory L. Domingo	Member
Serafin U. Salvador	Member

Compliance Committee

Atty. Corazon I. Morando	Chairperson
Atty. Felicitas A. Arroyo	Member
Atty. Antonio C. Pacis	Member
Jose T. Sio	Member

* *Independent Director- in compliance with the Guidelines set forth by SRC (Securities Regulation Code) Rule 38 regarding the Nomination and Election of Independent Director.*

FACES
Executive Officers

SM Corporate Executives

HARLEY T. SY
President
SM Investments Corporation

JOSE T. SIO
Executive Vice President
Chief Financial Officer
SM Investments Corporation

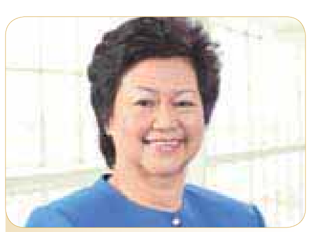
MA. RUBY LL. CANO
Vice President
Financial Controller
SM Investments Corporation

CECILIA R. PATRICIO
Vice President
Corporate Tax
SM Investments Corporation

GRACE F. ROQUE
Vice President
Finance
SM Investments Corporation

CORAZON P. GUIDOTE
Vice President
Investor Relations
SM Investments Corporation

DOREEN T. ROJO
Vice President
Mergers and Acquisitions
SM Investments Corporation



CORAZON I. MORANDO
Consultant
Legal and Corporate Affairs /
Assistant Corporate Secretary

MARIANNE M. GUERRERO
Senior Vice President
Legal Department
SM Investments Corporation

EPITACIO B. BORCELIS
Vice President
Legal Department
SM Investments Corporation

Retail Merchandising

HERBERT T. SY
President
SM Supermarkets

JORGE T. MENDIOLA
Senior Vice President
Operations
SM Department Stores

ROBERT S. KWEE
Executive Vice President
SM Hypermarkets

RICKY A. LIM
Senior Vice President, Controllership
SM Retail

Mall Operations

HANS T. SY
President
SM Prime Holdings, inc.

ELIZABETH T. SY
Senior Vice President
Marketing
SM Prime Holdings, Inc.

JEFFREY C. LIM
Executive Vice President
Chief Financial Officer
SM Prime Holdings, Inc.

ANNIE S. GARCIA
President
Shopping Center
Management Corporation

Banking

TERESITA SY-COSON
Chairperson
Banco De Oro Unibank, Inc.

NESTOR V. TAN
President
Banco De Oro Unibank, Inc.

JESUS A. JACINTO
Vice Chairman
Banco De Oro Unibank, Inc.

GILBERT U. DEE
Chairman
China Banking Corporation

PETER S. DEE
President and CEO
China Banking Corporation

RICARDO R. CHUA
Executive Vice President
and COO
China Banking Corporation

ALEXANDER C. ESCUCHA
First Vice President
China Banking Corporation

Property

HENRY T. SY, JR.
Vice Chairman
SM Investments Corporation

JOSEFINO C. LUCAS
EVP, Commercial Properties
and Resorts Group
SM Investments Corporation

MERRIL F. YU
Senior Vice President
Hotel Investments Group
SM Investments Corporation

JOSE B. AMANTOY, JR.
Vice President
Property Group
SM Investments Corporation

CARLOS V. CHIKIAMCO
Vice President
Real Property
SM Investments Corporation

SANDRA D. GARCIA
Vice President, Marketing
Property Group
SM Investments Corporation

EFREN L. TAN
Vice President, Sales
Property Group
SM Investments Corporation

ROGELIO R. CABUÑAG
President
SM Development Corporation

ANTONIO A. HENSON
President
Highlands Prime, Inc.

SM INVESTMENTS CORPORATION AND SUBSIDIARIES

Financial Statements

SM INVESTMENTS CORPORATION AND SUBSIDIARIES

MANAGEMENT DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Calendar Year Ended December 31, 2007 and 2006

Results of Operation
(amounts in billion pesos)

Accounts	12 / 31 / 2007	12 / 31 / 2006	% Change
Revenue	₱122.5	₱88.7	38.1%
Cost and Expenses	101.7	72.4	40.4%
Income from Operations	₱20.8	₱16.3	27.8%
Other Income (Charges)	(0.2)	2.6	-107.6%
Provision for Income Tax	4.5	3.6	24.5%
Minority Interest	4.1	4.7	-12.2%
Net Income	₱12.0	₱ 10.6	13.7%

Consolidated revenues grew by 38% to ₱122.5 billion, as against last year's P88.7 billion. Income from operations stood at P20.8 billion, increasing by 28% from last year's P16.2 billion. Operating income margin and Net profit margin is at 17.0% and 9.8%, respectively. Net income for the year ended December 31, 2007 increased by 13.7% to ₱12.0 billion compared to P10.6 billion of the same period last year.

Retail Sales accounts for the largest part of the revenue, comprising 80% of the total revenues for the year. Consolidated Retail sales expanded by 43.6% to ₱98.2 billion for the year ended December 31, 2007. The retail sales in 2007 include the full-year operations of SM Supermarkets and SM Hypermarkets, which were acquired only in June 2006. The sales contribution of the Supermarket and Hypermarket operations accounted for 49.4% of the total sales for the year. In 2007, the SM retail group opened two new department stores, two new hypermarkets, one new supermarket and one new SaveMore branch.

Location of New retail branches in 2007:

	SM Department Stores	SM Supermarkets	SM Hypermarkets
1	SM City Bacolod	SM City Bacolod	SM Supercenter Muntinlupa
2	SM City Taytay	Morong, Rizal	SM City Taytay

As of December 31, 2007, SM Investments' retail subsidiaries have 31 branches of SM Department stores, 29 branches of SM Supermarkets, and 11 branches of SM Hypermarkets.

Real estate sales for the year ended December 31, 2007, derived mainly from condominium projects of SMDC, increased sharply by 321.6% to P2,019.9 million. The robust sales attained by SMDC in 2007 came mainly from two of its five ongoing projects, the Chateau Elysee and the Mezza Residences. Chateau Elysee is a six-cluster, six-storey French-Mediterranean inspired residential development near SM City Bicutan in Paranaque while Mezza Residences is a 38-storey four-tower high rise condominium across SM City Sta. Mesa, Quezon City. In 2007, SMDC rolled out three new projects, namely the Lindenwood, Berkeley and Grass Residences. Lindenwood Residences is a residential subdivision in Muntinlupa. Berkeley Residences is a 35-storey condominium building along Katipunan Avenue, Quezon City. The third project, Grass Residences, is a three-tower condominium that will occupy a 3.6-hectare property near SM North EDSA in Quezon City.

Rental revenue from malls grew by 11% to P10.0 billion in 2007. This is largely due to rentals from new SM Supermalls opened in 2006 and 2007, namely, SM City Sta. Rosa, SM City Clark, SM Mall of Asia, The Block at SM City North Edsa, SM Supercenter Pasig, SM City Lipa, SM City Bacolod, SM City Taytay and SM Supercenter Muntinlupa. The new malls opened with a total gross floor area of almost 1 million square meters. Currently, these new malls have an average occupancy level of 96%. Same store rental growth is at 7%.

Cinema ticket sales and amusement revenues registered an increase of 13.0% from P2.3 billion last year to ₱2.5 billion this year due to more cinemas and the IMAX Theatre. For 2007, major blockbuster films shown were "Spiderman 3," "Transformers," "Harry Potter 5," "Ang Cute ng Ina Mo," and "One More Chance."

Equity in net earnings of associates increased by 25.3% to ₱3.4 billion in 2007 from ₱2.8 billion in 2006, primarily due to the increase in the effective ownership and in the net income of certain non-consolidated subsidiaries.

Dividend income amounted to ₱1.04 billion for the year 2007 compared to ₱1.03 billion in 2006.

Gain on sale of investments and properties decreased significantly to ₱28.7 million in 2007 from ₱4.8 billion in 2006. In 2006, there were gains realized from the sale of certain shares of stock and from the sale of Banco De Oro Global Depositary Receipts Offering. Please see Note 12 to the audited consolidated financial statements.

The 7.1% increase in net unrealized mark-to-market gain on investments from ₱529.0 million in 2006 compared to ₱566.7 million in 2007 was mainly due to the restatement of investments in listed company shares, to reflect the market to market valuation.

Total cost and expenses rose by 40.4% to ₱101.8 billion for the year ended December 31, 2007 compared to 2006. Cost of sales increased 46.1% to ₱80.2 billion primarily brought about by the full year effect of the supermarket and hypermarket operations in 2007 and the increased sales volume of the retail subsidiaries and real estate operations. Cost of Sales of the supermarket and hypermarket accounted for 51% of total retail cost of sales. Operating expenses increased by 22.7% in 2007 to ₱21.6 billion due to expenses associated to newly opened malls, department stores, supermarkets and hypermarkets.

The increase in interest expense by 7.0% to ₱3.7 billion in 2007 from ₱3.4 billion in 2006 and increase in interest income by 11.1% to ₱2.8 billion in 2007 from ₱2.5 billion in 2006 is mainly due to the issuance of US$300 million convertible bonds and ₱3.5 billion preferred shares by the parent company in 2007.

Provision for income tax increased by 24.5% to ₱4.5 billion for the year 2007 from ₱3.6 billion in 2006 due to the increase in taxable income.

Financial Position
(amounts in billion pesos)

Accounts	12 / 31 / 2007	12 / 31 / 2006	% Change
Current assets	₱75.7	₱59.6	27.0%
Noncurrent assets	158.8	167.5	-5.2%
Total assets	₱234.5	₱227.1	3.3%
Current liabilities	₱38.5	₱52.3	-26.5%
Noncurrent Liabilities	54.9	43.8	25.1%
Total Liabilities	₱93.4	₱96.2	-2.9%
Stockholders' Equity	₱141.1	₱130.9	7.8%
Total Liabilities and Stockholders' Equity	₱234.5	₱227.1	3.3%

On the Balance Sheet side, consolidated total assets as of December 31, 2007 amounted to ₱234.5 billion, higher by 3.3% from ₱227.1 billion in previous year. On the other hand, consolidated total liabilities slightly decreased by 2.9% to P93.4 billion in 2007 from ₱96.2 billion in previous year.

Total current assets increased by 27.0% to ₱75.7 billion as of December 31, 2007 from ₱59.6 billion as of last year mainly due to the reclassification of certain available for sale investments from noncurrent assets, and increase in receivables, merchandise inventories and other current assets.

Total consolidated noncurrent assets decreased by 5.2% to ₱158.8 billion as of December 31, 2007. The decrease in this account is due to several factors namely: (a) decrease in Investments in shares of stocks of associates, (b) increase in Investment Properties, mainly due to construction activities related to completed mall projects like SM City Sta. Rosa, SM City Clark, SM Mall of Asia, The Block at SM North Edsa, SM Supercenter Pasig, SM City Lipa and SM City Bacolod. Ongoing mall projects are SM City Taytay, SM City Cebu Annex, and SM Supercenter Muntinlupa and (c) reclassification of certain available for sale investments to current assets.

Total consolidated current liabilities decreased by 26.5% to ₱38.5 billion as of December 31, 2007, primarily due to the payment of the 5-year US$300 Million Global Notes of the parent company which matured in October 2007 and other short-term bank loans of both the parent company and its subsidiaries. The remaining notes payable of ₱8.1 billion representing 80% balance of Company's obligation for the EPCIB tender offer was reclassified to current.

Total Noncurrent Liabilities increased to ₱54.9 billion, due to the issuance of the US$300 million convertible bonds and preferred shares. The details of these transactions are further discussed in Notes 12 and 19 to the audited consolidated financial statements.

Total Stockholders' equity amounted to ₱141.1 billion as of December 31, 2007, while total Equity attributable to equity holders of the parent amounted to ₱108.9 billion. See Note 20 to the audited consolidated financial statements for further discussion regarding the stockholders' equity.

<u>Acquisitions made in 2007</u>

On July 27, 2007, Orkam Holding Asia N.V. sold its 40% equity in Rappel to Forsyth Equity Holdings, Inc. (Forsyth). On October 3, 2007, Forsyth sold the said shares to SMIC, which increased SMIC's direct ownership in Rappel from 40% to 80%. Rappel is an unlisted company engaged in the business of investing, purchasing, acquiring and owning real or personal property, including shares of stock, bonds and other forms of securities.

SMIC and Rappel directly owns 10% and 50% interests in Pilipinas Makro, Inc. (Makro), respectively. Makro is an unlisted company engaged in buying and selling of food and non-food items to registered customers at wholesale and/or retail under a warehouse club format. As a result of the acquisition of an additional 40% interest in Rappel, Makro also became a subsidiary of SMIC through the 60% direct and indirect ownership.

See Note 5 (Business Combinations) of the Notes to the Consolidated Financial Statements.

The Company has no known direct or contingent financial obligation that is material to the Company operations, including any default or acceleration of an obligation. The Company has no off-balance sheet transactions, arrangements, obligations during the reporting year and as of the balance sheet date.

There are no known trends, events, material changes, seasonal aspects or uncertainties that are expected to affect the company's continuing operations.

Key Performance Indicators

The following are the major financial ratios of the Company for the years ended December 31, 2007 and 2006:

Accounts	12 / 31 / 2007	12 / 31 / 2006
Current Ratio	1.97 : 1.00	1.14 : 1.00
Debt-equity Ratio	30% : 70%	34% : 66%
Return on Equity (annualized)	11.3%	11.6%
Net Income to Revenue	10%	12%
Revenue Growth	38.1%	64.4%
Net Income Growth	14%	32%
EBITDA	₱25.1B	₱19.6B

The manner by which the Company calculates the foregoing indicators is as follows:

Current Ratio	Current Assets / Current Liabilities
Debt – Equity Ratio	Total Interest Bearing Debt / Total Equity Attributable to Equity Holders of the Parent + Total Interest Bearing Debt
Return on Equity	Net Income / Average Equity Attributable to Equity Holders of the Parent
Net Income to Revenue	Net Income / Total Revenue
Revenue Growth	Total Revenues (Current Period) / Total Revenues (Prior Period)
Net Income Growth	Net Income (Current Period) / Net Income (Prior Period)
EBITDA	Income from operations + Depreciation & Amortization

SM INVESTMENTS CORPORATION AND SUBSIDIARIES

STATEMENT OF MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS

The management of SM Investments Corporation is responsible for all information and representations contained in the consolidated balance sheets as at December 31, 2007 and 2006 and the consolidated statements of income, consolidated statements of changes in equity and consolidated statements of cash flows for the years ended December 31, 2007 and 2006, and the nine months ended December 31, 2005, and a summary of significant accounting policies and other explanatory notes. The consolidated financial statements have been prepared in accordance with Philippine Financial Reporting Standards and reflect amounts that are based on the best estimates and informed judgment of management with an appropriate consideration to materiality.

In this regard, management maintains a system of accounting and reporting which provides for the necessary internal controls to ensure that transactions are properly authorized and recorded, assets are safeguarded against unauthorized use or disposition and liabilities are recognized. The management likewise discloses to the Company's Audit Committee and to its external auditor: (i) all significant deficiencies in the design or operation of internal controls that could adversely affect its ability to record, process and report financial data; (ii) material weaknesses in the internal controls; and, (iii) any fraud that involves management or other employees who exercise significant roles in internal controls.

The Board of Directors reviews the consolidated financial statements before such statements are approved and submitted to the stockholders of the Company.

SyCip Gorres Velayo & Co., the independent auditors appointed by the Board of Directors and stockholders, has audited the consolidated financial statements of the Company in accordance with Philippine Standards on Auditing and has expressed their opinion on the fairness of presentation upon completion of such audit, in their report to the Board of Directors and stockholders.

Henry Sy, Sr.	**Harley T. Sy**	**Jose T. Sio**
Chairman of the Board	Chief Executive officer	Chief Financial Officer

SM INVESTMENTS CORPORATION AND SUBSIDIARIES

INDEPENDENT AUDITORS' REPORT

The Stockholders and the Board of Directors
SM Investments Corporation

SGV & Co

We have audited the accompanying consolidated financial statements of SM Investments Corporation and Subsidiaries, which comprise the consolidated balance sheets as at December 31, 2007 and 2006, and the consolidated statements of income, consolidated statements of changes in stockholders' equity and consolidated statements of cash flows for the years ended December 31, 2007 and 2006 and the nine months ended December 31, 2005, and a summary of significant accounting policies and other explanatory notes. We did not audit the financial statements of 13 and 14 consolidated subsidiaries in 2007 and 2006, respectively. The accompanying consolidated financial statements include the accounts of such consolidated subsidiaries which reflect total assets amounting to ₱14,267.9 million (6.08% of total assets) and ₱40,286.7 million (17.74% of total assets) as of December 31, 2007 and 2006, respectively, and net income amounting to ₱3,322.3 million (20.61% of net income), ₱6,076.9 million (39.87% of net income) and ₱1,429.5 million (12.63% of net income) for the periods ended December 31, 2007, 2006 and 2005, respectively. We also did not audit the financial statements of three associates in 2007 and 2006, the investments of which are reflected in the accompanying consolidated financial statements using the equity method of accounting and amounted to ₱35,370.7 million and ₱9,822.2 million as of December 31, 2007 and 2006, respectively. The Company's equity in the net earnings of such associates for the years ended December 31, 2007 and 2006 and the nine months ended December 31, 2005 amounted to ₱2,642.8 million, ₱1,046.3 million and ₱1,145.3 million, respectively. The financial statements of these subsidiaries and associates were audited by other auditors whose unqualified reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for these companies, is based solely on the reports of the other auditors.

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 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 and the reports of the other auditors are sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, based on our audits and the reports of the other auditors, the consolidated financial statements present fairly, in all material respects, the financial position of SM Investments Corporation and Subsidiaries as of December 31, 2007 and 2006, and their financial performance and their cash flows for the years ended December 31, 2007 and 2006 and the nine months ended December 31, 2005 in accordance with Philippine Financial Reporting Standards.

SYCIP GORRES VELAYO & CO.

Melinda Gonzales-Manto
Partner
CPA Certificate No. 26497
SEC Accreditation No. 0085-AR-1
Tax Identification No. 123-305-056
PTR No. 0017602, January 3, 2008, Makati City

March 5, 2008

SM INVESTMENTS CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

December 31, 2007 and 2006

	2007	2006
ASSETS		
Current Assets		
Cash and cash equivalents (Notes 7, 17, 19, 21, 28 and 29)	₱15,574,971,433	₱21,037,492,714
Time deposits and short-term investments (Notes 8, 19, 21, 28 and 29)	4,130,250,000	7,825,188,000
Investments held for trading and sale (Notes 3, 9, 11, 19, 21, 28 and 29)	33,125,710,073	16,959,734,059
Receivables - net (Notes 3, 10, 21, 28 and 29)	14,158,842,397	7,287,814,474
Merchandise inventories - at cost (Notes 3 and 22)	5,958,301,914	4,488,187,321
Input taxes and other current assets - net (Note 15)	2,748,665,020	1,981,157,885
Total Current Assets	75,696,740,837	59,579,574,453
Noncurrent Assets		
Available-for-sale investments - net (Notes 3, 11, 21, 28 and 29)	5,765,388,907	34,526,871,725
Investments in shares of stock of associates (Notes 3 and 12)	42,478,948,920	46,546,777,199
Property and equipment - net (Notes 3, 13 and 17)	18,397,832,331	12,300,930,057
Investment properties - net (Notes 3, 14 and 19)	63,767,977,656	56,421,608,280
Land and development (Notes 3 and 15)	3,890,953,068	1,836,350,808
Time deposits (Notes 8, 19, 21, 28 and 29)	4,128,000,000	–
Intangibles (Notes 2, 3, 5 and 16)	11,794,650,329	11,240,180,011
Other noncurrent assets (Notes 3, 10, 12, 16, 25, 28 and 29)	8,563,945,618	4,620,971,626
Total Noncurrent Assets	158,787,696,829	167,493,689,706
	₱234,484,437,666	₱227,073,264,159
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Bank loans (Notes 17, 21, 28 and 29)	₱3,037,560,267	₱13,319,576,097
Accounts payable and other current liabilities (Notes 18, 21, 28 and 29)	25,003,786,393	18,240,321,118
Income tax payable	1,236,402,605	848,188,273
Current portion of long-term debt (Notes 19, 21, 28 and 29)	833,350,952	17,629,400,122
Current portion of notes payable (Notes 12, 28 and 29)	8,118,761,498	1,746,898,971
Derivative liabilities (Notes 28 and 29)	236,937,197	–
Dividends payable (Notes 28 and 29)	20,416,956	556,008,628
Total Current Liabilities	38,487,215,868	52,340,393,209
Noncurrent Liabilities		
Long-term debt - net of current portion (Notes 19, 21, 28 and 29)	42,832,528,656	22,970,657,371
Notes payable - net of current portion (Notes 12 and 29)	–	12,332,385,033
Defined benefit liability (Note 25)	495,514,295	478,577,517
Deferred tax liabilities (Note 26)	3,474,207,497	2,627,883,460
Derivative liabilities (Notes 28 and 29)	3,053,977,715	1,042,500,665
Tenants' deposits and others (Notes 27, 28 and 29)	5,008,344,147	4,389,520,295
Total Noncurrent Liabilities	54,864,572,310	43,841,524,341
Equity Attributable to Equity Holders of the Parent (Note 28)		
Capital stock (Note 20)	6,110,230,380	5,860,000,000
Additional paid-in capital (Note 20)	35,030,709,537	35,030,709,537
Cost of common shares held by subsidiaries (Note 20)	(10,695,000)	(55,213,502)
Net unrealized gain on available-for-sale investments (Notes 11 and 12)	7,952,663,654	11,261,528,843
Retained earnings (Note 20):		
Appropriated	5,000,000,000	5,000,000,000
Unappropriated	54,804,637,119	46,206,903,642
Total Equity Attributable to Equity Holders of the Parent	108,887,545,690	103,303,928,520
Minority Interests	32,245,103,798	27,587,418,089
Total Stockholders' Equity	141,132,649,488	130,891,346,609
	₱234,484,437,666	₱227,073,264,159

See accompanying Notes to Consolidated Financial Statements.

SM INVESTMENTS CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

For The Years Ended December 31, 2007 and 2006 and The Nine Months Ended December 31, 2005

	December 31, 2007 (One Year)	December 31, 2006 (One Year)	December 31, 2005 (Nine Months - Note 30)
REVENUE			
Sales:			
Merchandise	₱98,223,355,533	₱68,401,569,764	₱39,152,692,213
Real estate	2,019,863,263	479,055,252	232,188,876
Rent (Notes 3, 14, 21 and 27)	11,088,662,896	9,804,324,538	8,323,506,121
Equity in net earnings of associates (Note 12)	3,456,684,195	2,758,843,422	2,079,267,626
Cinema ticket sales, amusement and others	2,543,087,596	2,250,326,516	1,877,347,517
Dividend income	1,037,624,922	1,034,343,716	1,077,831,319
Gain on sale of available-for-sale investments and fair value changes on investments held for trading and derivatives - net (Notes 9, 11 and 29)	481,919,905	2,220,001,892	595,304,482
Management fees (Note 21)	266,004,137	290,855,338	268,478,195
Others	3,419,416,306	1,500,074,942	359,157,491
	122,536,618,753	88,739,395,380	53,965,773,840
COST AND EXPENSES			
Cost of sales:			
Merchandise (Note 22)	79,015,823,031	54,685,342,080	30,560,093,042
Real estate	1,160,640,060	199,427,085	135,165,819
Selling, general and administrative expenses (Note 23)	21,583,083,563	17,594,679,955	10,805,040,773
	101,759,546,654	72,479,449,120	41,500,299,634
OTHER INCOME (CHARGES)			
Interest expense (Notes 17, 19, 21, 24 and 28)	(3,681,354,139)	(3,442,071,078)	(2,455,502,507)
Interest income (Notes 21 and 24)	2,817,307,572	2,535,713,725	2,656,700,652
Foreign exchange gain - net (Note 28)	593,861,129	462,750,431	103,694,310
Gain on sale of investments in shares of stock, investment properties and property and equipment (Notes 2, 12, 13 and 14)	74,565,437	3,010,548,347	15,932,917
Excess of share in net assets of an associate over cost of investment (Note 12)	–	–	904,183,856
	(195,620,001)	2,566,941,425	1,225,009,228
INCOME BEFORE INCOME TAX	20,581,452,098	18,826,887,685	13,690,483,434
PROVISION FOR INCOME TAX (Note 26)			
Current	4,164,744,319	3,300,523,777	2,083,273,249
Deferred	299,463,876	285,200,291	285,292,403
	4,464,208,195	3,585,724,068	2,368,565,652
NET INCOME	₱16,117,243,903	₱15,241,163,617	₱11,321,917,782
ATTRIBUTABLE TO:			
Equity holders of the Parent (Note 31)	₱12,018,223,857	₱10,571,856,399	₱8,029,241,507
Minority interests	4,099,020,046	4,669,307,218	3,292,676,275
	₱16,117,243,903	₱15,241,163,617	₱11,321,917,782
Earnings Per Common Share (Note 31)			
Basic	₱19.67	₱18.06	₱14.53
Dilutive	₱17.31	₱18.06	₱14.53

See accompanying Notes to Consolidated Financial Statements.

SM INVESTMENTS CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

For the Years Ended December 31, 2007 and 2006 and the Nine Months Ended December 31, 2005

	Equity Attributable to Equity Holders of the Parent		
	Capital Stock (Note 20)	Additional Paid-in Capital (Note 20)	Cost of Common Shares Held by Subsidiaries (Note 20)
Balance at December 31, 2006	₱5,860,000,000	₱35,030,709,537	(₱55,213,502)
Net income for the year	–	–	–
Loss due to changes in fair value of available-for-sale investments	–	–	–
Transferred to income and expenses	–	–	–
Share in net gain on available-for-sale investments of associates	–	–	–
Total income for the year	–	–	–
Acquisition of common shares held by subsidiaries	–	–	(1,621,786)
Disposal of common shares held by subsidiaries	–	–	32,757,300
Shares held by a deconsolidated subsidiary	–	–	13,382,988
Cash dividends - ₱5.41 a share	–	–	–
Stock dividends	250,230,380	–	–
Minority interest arising from acquisition of subsidiaries (see Note 5)	–	–	–
Decrease in previous year's minority interest	–	–	–
Effect on minority interest of disposal of a subsidiary	–	–	–
Sale of treasury stock pertaining to minority interest	–	–	–
Cash dividends received by minority interests	–	–	–
Balance at December 31, 2007	₱6,110,230,380	₱35,030,709,537	(₱10,695,000)
Balance at December 31, 2005	₱5,300,000,000	₱23,382,709,537	(₱500,000,000)
Net income for the year	–	–	–
Gain due to changes in fair value of available-for-sale investments	–	–	–
Transferred to income and expenses	–	–	–
Share in net gain on available-for-sale investments of associates	–	–	–
Total income for the year	–	–	–
Issuance of common shares	560,000,000	11,648,000,000	–
Disposal of common shares held by subsidiaries	–	–	479,305,000
Acquisition of common shares held by subsidiaries	–	–	(34,518,502)
Cash dividends - ₱4.70 a share	–	–	–
Cash dividends received by minority interests	–	–	–
Balance at December 31, 2006	₱5,860,000,000	₱35,030,709,537	(₱55,213,502)
Balance at March 31, 2005	₱5,300,000,000	₱23,382,709,537	(₱500,000,000)
Effect of change in accounting for financial instruments	–	–	–
Net share from fair value adjustments of associates during the period	–	–	–
Balance at April 1, 2005	5,300,000,000	23,382,709,537	(500,000,000)
Net income for the period	–	–	–
Net gain from fair value adjustments during the period	–	–	–
Net share from fair value adjustments of associates during the period	–	–	–
Total income for the period	–	–	–
Reversal of appropriation for long-term expansion and improvement projects	–	–	–
Cash dividends - ₱3.50 a share	–	–	–
Cash dividends received by minority interests	–	–	–
Balance at December 31, 2005	₱5,300,000,000	₱23,382,709,537	(₱500,000,000)

See accompanying Notes to Consolidated Financial Statements.

Net Unrealized Gain on Available-for-Sale Investments (Notes 11 and 12)	Appropriated Retained Earnings (Note 20)	Unappropriated Retained Earnings (Note 20)	Total	Minority Interests	Total Stockholders' Equity
₱11,261,528,843	₱5,000,000,000	₱46,206,903,642	₱103,303,928,520	₱27,587,418,089	₱130,891,346,609
–	–	12,018,223,857	12,018,223,857	4,099,020,046	16,117,243,903
(3,225,093,687)	–	–	(3,225,093,687)	(163,263,349)	(3,388,357,036)
(89,665,776)	–	–	(89,665,776)	(48,320,533)	(137,986,309)
5,894,274	–	–	5,894,274	12,015,362	17,909,636
(3,308,865,189)	–	12,018,223,857	8,709,358,668	3,899,451,526	12,608,810,194
–	–	–	(1,621,786)	–	(1,621,786)
–	–	–	32,757,300	–	32,757,300
–	–	–	13,382,988	–	13,382,988
–	–	(3,170,260,000)	(3,170,260,000)	–	(3,170,260,000)
–	–	(250,230,380)	–	–	–
–	–	–	–	2,104,916,951	2,104,916,951
–	–	–	–	(70,680,774)	(70,680,774)
–	–	–	–	(76,378,450)	(76,378,450)
–	–	–	–	144,834,145	144,834,145
–	–	–	–	(1,344,457,689)	(1,344,457,689)
₱7,952,663,654	₱5,000,000,000	₱54,804,637,119	₱108,887,545,690	₱32,245,103,798	₱141,132,649,488
₱7,038,286,318	₱5,000,000,000	₱38,126,047,243	₱78,347,043,098	₱23,615,982,476	₱101,963,025,574
–	–	10,571,856,399	10,571,856,399	4,669,307,218	15,241,163,617
4,570,178,495	–	–	4,570,178,495	1,967,351,739	6,537,530,234
(987,438,547)	–	–	(987,438,547)	(543,564,329)	(1,531,002,876)
640,502,577	–	–	640,502,577	39,755,988	680,258,565
4,223,242,525	–	10,571,856,399	14,795,098,924	6,132,850,616	20,927,949,540
–	–	–	12,208,000,000	–	12,208,000,000
–	–	–	479,305,000	–	479,305,000
–	–	–	(34,518,502)	–	(34,518,502)
–	–	(2,491,000,000)	(2,491,000,000)	–	(2,491,000,000)
–	–	–	–	(2,161,415,003)	(2,161,415,003)
₱11,261,528,843	₱5,000,000,000	₱46,206,903,642	₱103,303,928,520	₱27,587,418,089	₱130,891,346,609
₱–	₱10,000,000,000	₱26,797,289,270	₱64,979,998,807	₱21,002,364,686	₱85,982,363,493
4,332,183,838	–	154,516,466	4,486,700,304	2,440,414,245	6,927,114,549
170,605,372	–	–	170,605,372	36,227,284	206,832,656
4,502,789,210	10,000,000,000	26,951,805,736	69,637,304,483	23,479,006,215	93,116,310,698
–	–	8,029,241,507	8,029,241,507	3,292,676,275	11,321,917,782
1,893,708,186	–	–	1,893,708,186	(405,252,159)	1,488,456,027
641,788,922	–	–	641,788,922	52,322,795	694,111,717
2,535,497,108	–	8,029,241,507	10,564,738,615	2,939,746,911	13,504,485,526
–	(5,000,000,000)	5,000,000,000	–	–	–
–	–	(1,855,000,000)	(1,855,000,000)	–	(1,855,000,000)
–	–	–	–	(2,802,770,650)	(2,802,770,650)
₱7,038,286,318	₱5,000,000,000	₱38,126,047,243	₱78,347,043,098	₱23,615,982,476	₱101,963,025,574

SM INVESTMENTS CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

For The Years Ended December 31, 2007 and 2006 and the Nine Months Ended December 31, 2005

	December 31, 2007 (One Year)	December 31, 2006 (One Year)	December 31, 2005 (Nine Months - Note 30)
CASH FLOWS FROM OPERATING ACTIVITIES			
Income before income tax	₱20,581,452,098	₱18,826,887,685	₱13,690,483,434
Adjustments for:			
Depreciation and amortization (Note 23)	4,293,157,520	3,355,058,496	2,283,024,304
Interest expense (Note 24)	3,681,354,139	3,442,071,078	2,455,502,507
Equity in net earnings of associates (Note 12)	(3,456,684,195)	(2,758,843,422)	(2,079,267,626)
Interest income (Note 24)	(2,817,307,572)	(2,535,713,725)	(2,656,700,652)
Dividend income	(1,037,624,922)	(1,034,343,716)	(1,077,831,319)
Provisions for impairment losses and others (Note 23)	818,255,424	1,596,489,245	–
Unrealized foreign exchange loss (gain)	(747,957,558)	(1,064,025,038)	39,386,633
Gain on sale of available-for-sale investments and fair value changes on investments held for trading and derivatives - net (Notes 9, 11 and 29)	(481,919,905)	(2,220,001,892)	(595,304,482)
Gain on sale of investments in shares of stock, investment properties and property and equipment (Notes 2, 12, 13 and 14)	(74,565,437)	(3,010,548,347)	(15,932,917)
Excess of share in net assets of an associate over cost of investment	–	–	(904,183,856)
Income before working capital changes	20,758,159,592	14,597,030,364	11,139,176,026
Decrease (increase) in:			
Receivables	(6,372,576,898)	(1,418,133,926)	(1,081,484,345)
Merchandise inventories	(685,534,470)	(168,890,284)	280,524,369
Input taxes and other current assets	(612,939,553)	(595,666,091)	(436,498,464)
Increase (decrease) in:			
Accounts payable and other current liabilities	4,220,287,075	862,454,240	1,562,347,186
Defined benefit liability	17,520,476	166,759,032	(71,569,911)
Tenants' deposits and others	583,900,256	1,140,788,264	807,079,855
Net cash generated from operations	17,908,816,478	14,584,341,599	12,199,574,716
Income tax paid	(3,797,919,888)	(3,402,961,108)	(2,072,925,713)
Net cash provided by operating activities	14,110,896,590	11,181,380,491	10,126,649,003
CASH FLOWS FROM INVESTING ACTIVITIES			
Proceeds from sale of:			
Investments held for trading	15,699,644,734	4,798,336,290	3,557,224,601
Available-for-sale investments	2,749,207,785	2,174,153,339	–
Investments in shares of stock	64,682,477	10,193,165,348	599,940
Investment properties	63,427,659	59,618,827	7,489,551
Property and equipment	3,844,188	316,155,540	1,945,280
Additions to:			
Investments held for trading	(9,867,103,023)	(4,574,027,022)	(2,256,262,463)
Property and equipment (Note 13)	(8,880,204,220)	(9,446,754,607)	(9,881,775,004)
Investment properties (Note 14)	(3,213,596,829)	(338,306,259)	(2,840,043,098)
Available-for-sale investments	(588,134,016)	(1,111,797,033)	(11,208,928,648)

(Forward)

	December 31, 2007 (One Year)	December 31, 2006 (One Year)	December 31, 2005 (Nine Months - Note 30)
Interest received	₱2,393,071,632	₱2,554,375,159	₱2,801,379,239
Dividends received	1,533,897,059	1,153,377,663	1,710,451,221
Net cash received from (used in) acquisition of subsidiaries (Note 5)	(926,021,051)	1,649,500,526	–
Net cash from deconsolidated subsidiary	(19,322,393)	–	–
Decrease (increase) in:			
Investments in shares of stock of associates	103,973,939	(8,457,493,567)	(10,056,755,430)
Land and development	(2,054,602,260)	(560,059,180)	(198,407,843)
Time deposits	(961,062,000)	4,322,913,206	1,353,471,818
Other noncurrent assets	(2,253,092,262)	(2,113,152,778)	(606,740,512)
Net cash provided by (used in) investing activities	(6,151,388,581)	620,005,452	(27,616,351,348)
CASH FLOWS FROM FINANCING ACTIVITIES			
Availments of:			
Long-term debt	33,365,887,716	6,200,000,000	8,847,058,986
Bank loans	13,243,463,292	19,203,402,675	15,242,069,510
Payments of:			
Long-term debt	(25,421,103,553)	(3,467,999,530)	(8,961,928,211)
Bank loans	(23,521,587,247)	(15,548,257,328)	(17,868,820,510)
Dividends	(4,719,512,959)	(3,021,755,684)	(872,971,058)
Interest	(3,663,866,086)	(4,676,627,236)	(2,744,542,716)
Notes payable	(1,746,898,971)	–	–
Decrease in minority interests	(1,241,130,310)	(697,871,605)	(767,608,564)
Proceeds from termination of interest rate and structured swaps (Note 29)	510,351,575	–	–
Disposal of common shares held by subsidiaries (Note 20)	46,140,288	479,305,000	–
Acquisition of common shares held by subsidiaries (Note 20)	(1,621,786)	(34,518,502)	–
Net cash used in financing activities	(13,149,878,041)	(1,564,322,210)	(7,126,742,563)
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	(272,151,249)	(374,506,695)	(310,289,414)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(5,462,521,281)	9,862,557,038	(24,926,734,322)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	21,037,492,714	11,174,935,676	36,101,669,998
CASH AND CASH EQUIVALENTS AT END OF PERIOD	₱15,574,971,433	₱21,037,492,714	₱11,174,935,676

See accompanying Notes to Consolidated Financial Statements.

SM INVESTMENTS CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Corporate Information

SM Investments Corporation (SMIC or Parent Company) was incorporated in the Philippines. Its registered office address is SM Corporate Offices, Building A, J.W. Diokno Boulevard, Mall of Asia Complex, Pasay City 1300.

The Parent Company and its subsidiaries (collectively referred to as the Group) and its associates are involved primarily in shopping mall development, retail merchandising, real estate development and tourism and financial services.

The Parent Company's shares of stock are publicly traded in the Philippine Stock Exchange (PSE).

The accompanying consolidated financial statements were authorized for issue by the Board of Directors (BOD) on March 5, 2008.

2. Basis of Preparation

The consolidated financial statements of the Group have been prepared on the historical cost basis, except for derivative financial instruments, investments held for trading and available-for-sale (AFS) investments, which have been measured at fair value. The consolidated financial statements are presented in Philippine peso, which is the Group's functional and presentation currency under Philippine Financial Reporting Standards (PFRS). All values are rounded to the nearest peso, except when otherwise indicated.

<u>Statement of Compliance</u>
The consolidated financial statements have been prepared in compliance with PFRS. PFRS includes statements named PFRS and Philippine Accounting Standards (PAS), including interpretations, issued by the Financial Reporting Standards Council (FRSC).

<u>Changes in Accounting Policies</u>
The accounting policies adopted are consistent with those of the previous financial periods, except for the following new PFRS and Philippine Interpretations from International Financial Reporting Interpretations Committee (IFRIC), which the Group has adopted starting January 1, 2007:

- PFRS 7, *Financial Instruments: Disclosures,* requires disclosures that enable users of financial statements to evaluate the significance of the Group's financial instruments and the nature and extent of risks arising from those financial instruments. The adoption of this standard resulted in additional disclosures such as aging analysis of receivables, credit risk concentrations, contractual maturity analysis of financial liabilities and market sensitivity analysis (see Notes 10 and 28).

  FRSC has approved an amendment to the transition provisions of PFRS 7 that gives transition relief with respect to the presentation of comparative information for the new risk disclosures about the nature and extent of risks arising from financial instruments in paragraphs 31 to 42 of PFRS 7. Accordingly, the Group did not present comparative information with respect to the new risk disclosures.

- Philippine Interpretation IFRIC 8, *Scope of PFRS 2,* requires PFRS 2, *Share-based Payment,* to be applied to any arrangements in which the entity cannot identify specifically some or all of the goods received, in particular where equity instruments are issued for consideration which appears to be less than fair value. As the Group did not have this type of arrangement, the interpretation had no impact on the financial position or performance of the Group.

• Philippine Interpretation IFRIC 9, *Reassessment of Embedded Derivatives,* establishes that the date to assess the existence of an embedded derivative is the date an entity first becomes a party to the contract, with reassessment only if there is a change to the contract that significantly modifies the cash flows. The interpretation had no significant impact on the financial position or performance of the Group.

• Philippine Interpretation IFRIC 10, *Interim Financial Reporting and Impairment,* requires that an entity must not reverse an impairment loss recognized in the interim period in respect of goodwill and AFS equity investments. As the Group had no impairment losses related to goodwill and AFS equity investments previously reversed, the interpretation had no impact on the financial position or performance of the Group.

<u>Future Changes in Accounting Policies</u>
The Group did not early adopt the following standards, interpretations and amendments that have been approved but are not yet effective:

• PFRS 8, *Operating Segments,* becomes effective for financial years beginning on or after January 1, 2009, and will replace PAS 14, *Segment Reporting.* It adopts a management approach to reporting segment information. The information reported would be that which management uses internally for evaluating the performance of operating segments and allocating resources to those segments. Such information may be different from that reported in the consolidated balance sheets and consolidated statements of income and companies will need to provide explanations and reconciliations of the differences. The Group will assess the impact of this standard to its current manner of reporting segment information when it adopts the standard on January 1, 2009.

• Revised PAS 1, *Presentation of Financial Statements,* becomes effective for financial years beginning on or after January 1, 2009. The standard separates owner and non-owner changes in equity. The statement of changes in equity will include only details of transactions with owners, with all non-owner changes in equity presented as a single line. In addition, the standard introduces the statement of comprehensive income, which presents all items of income and expense recognized in profit or loss, together with all other items of recognized income and expense, either in one single statement, or in two linked statements. The revision also includes changes in titles of some of the financial statements to reflect their function more clearly, although not mandatory for use in the financial statements. The Group is currently assessing the impact of the revised standard on its consolidated financial statements when it adopts the standard on January 1, 2009.

• PAS 23, *Amendment to Borrowing Costs,* becomes effective for financial years 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. The adoption of this amendment will have no impact on the consolidated financial statements since it is the Group's current policy to capitalize borrowing costs related to a qualifying asset.

• Philippine Interpretation IFRIC 11, *PFRS 2 - Group and Treasury Share Transactions,* becomes effective for financial years beginning on or after March 1, 2007. This 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. As the Group currently does not have any stock option plan, this interpretation will not have any impact on its consolidated financial statements.

• Philippine Interpretation IFRIC 12, *Service Concession Arrangements*, becomes effective for financial years beginning on or after January 1, 2008. This interpretation covers contractual arrangements arising from public-to-private service concession arrangements if control of the assets remains in public hands but the private sector operator is responsible for construction activities, as well as for operating and maintaining the public sector infrastructure. This interpretation will have no impact on the Group's consolidated financial statements as this is not relevant to its current operations.

- Philippine Interpretation IFRIC 13, *Customer Loyalty Programmes,* becomes effective for financial years beginning on or after July 1, 2008. This interpretation 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. As such schemes currently exist in the Group's retail merchandising segment, the Group will assess the impact of this interpretation to its financial position or performance when it adopts the interpretation on January 1, 2009.

- Philippine Interpretation IFRIC 14, *PAS 19 - The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*, becomes effective for annual periods beginning on or after January 1, 2008. This interpretation 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*. As some of the subsidiaries' defined benefit plans are currently in surplus, the Group will assess the impact of this interpretation to its financial position or performance when it adopts the interpretation on January 1, 2008.

Basis of Consolidation

The consolidated financial statements include the accounts of the Parent Company and the following subsidiaries which were all incorporated in the Philippines:

	Effective Percentage of Ownership	
Company	2007	2006
Shopping Mall Development -		
SM Prime Holdings, Inc. (SM Prime) and Subsidiaries	53	52
Retail Merchandising:		
Supervalue, Inc. (SVI)[a]	100	100
Super Shopping Market, Inc. (SSMI)[a]	100	100
Marketwatch Investments Co., Inc. (Marketwatch) and Subsidiaries*	100	100
MH Holdings, Inc. (MH Holdings) and Subsidiaries*	100	100
Sanford Investments Corporation (Sanford) and Subsidiary*	100	100
Henfels Investments Corporation (Henfels) and Subsidiaries*	99	99
HMS Development Corporation (HMS) and Subsidiaries*	99	99
Romer Mercantile, Inc. (Romer) and Subsidiaries*	99	99
SM Retail, Inc. (SM Retail)*	99	99
Rappel Holdings, Inc. (Rappel) and Subsidiary (see Note 5)	80	–
Shoe Mart, Incorporated (Shoemart)	65	65
SM Mart, Inc.	65	65
Real Estate Development and Tourism:		
Mountain Bliss Resort and Development Corporation and Subsidiary*[d]	100	100
SM Land, Inc. and Subsidiary*[b]	99	99
Intercontinental Development Corporation (ICDC)*	72	97
Bellevue Properties, Inc.*	62	62
SM Development Corporation (SMDC) and Subsidiary	59	53
Multi-Realty Development Corporation (MRDC)* (see Note 12)	–	91
Financial Services -		
Primebridge Holdings, Inc. (Primebridge)*	80	98
Others -		
Asia-Pacific Computer Technology Center, Inc. (APCTC)*[c] (see Notes 5 and 12)	52	–

* *The financial statements of these subsidiaries were audited by other independent auditors.*

a *Acquired by the Group in June 2006.*

b *Incorporated on October 20, 2006 and has not yet started commercial operations.*

c *Acquired additional interest in July 2007, thereby gaining control.*

d *Has not yet started commercial operations.*

On December 28, 2007, SMIC sold its 12.5 million equity shares in MRDC. The sale decreased SMIC's ownership in MRDC from 91% to 45%, thus, in the consolidated financial statements as of December 31, 2007, MRDC is no longer accounted for as a subsidiary but as an associate (see Note 12). MRDC owns 20% and 28% interest in Primebridge and ICDC, respectively. Thus, the sale also resulted in the decrease in SMIC's effective percentage of ownership in Primebridge (98% to 80%) and ICDC (97% to 72%).

In December 2007, SMIC acquired a total of 42.7 million additional SM Prime shares, which is equivalent to 0.34% of the total outstanding common stock of SM Prime, at an average price of ₱10.40 a share or for a total cost of ₱444.3 million. The acquisition of such minority interest resulted in goodwill amounting to ₱307.4 million (see Note 16).

In 2007 and 2006, Shoemart sold 4.80 million and 45.15 million shares of SM Prime, respectively. The gain from the sale amounted to ₱37.4 million and ₱263.7 million, respectively, included under "Gain on sale of investments in shares of stocks, investment properties and property and equipment" account in the consolidated statements of income.

The financial statements of the subsidiaries are prepared for the same reporting period as the Parent Company using consistent accounting policies.

All intragroup balances, income and expenses resulting from intragroup transactions are eliminated in full.

Subsidiaries are fully consolidated from the date of acquisition, being the date when the Group obtains control, and continue to be consolidated until the date that such control ceases.

Minority interests represent the portion of profit or loss and net assets not held by the Group and are presented separately in the consolidated statements of income and within stockholders' equity in the consolidated balance sheets, separately from equity attributable to equity holders of the Parent. Acquisitions of minority interest are accounted for using parent-entity method, whereby the difference is recognized as goodwill.

3. Significant Accounting Judgments, Estimates and Assumptions

The preparation of the consolidated financial statements requires management to make judgments, estimates and assumptions that affect the reported amounts of revenue, expenses, assets and liabilities, and the disclosure of contingent liabilities, at the reporting date. However, uncertainty about these estimates and assumptions could result in outcomes that could require a material adjustment to the carrying amount of the affected asset or liability in the future.

Judgments

In the process of applying the Group's accounting policies, management has made the following judgments, apart from those involving estimations, which have the most significant effect on the amounts recognized in the consolidated financial statements.

Revenue Recognition on Real Estate. Selecting an appropriate revenue recognition method for a particular real estate sales transaction requires certain judgments based on the buyer's commitment on the sale which may be ascertained through the significance of the buyer's initial investment and completion of development. The buyer's commitment is evaluated based on collections, credit standing of the buyer and location of the property. The completion of development is determined based on engineer's judgment and estimates on the physical portion of contract work done if the development is beyond the preliminary stage.

Operating Lease Commitments - Group as Lessor. The Group has entered into commercial property leases in its investment property portfolio. The Group has determined, based on an evaluation of the terms and conditions of the arrangements, that it retains all the significant risks and rewards of ownership of the properties and thus accounts for the contracts as operating leases.

Rent income amounted to ₱11,088.7 million, ₱9,804.3 million and ₱8,323.5 million for the periods ended December 31, 2007, 2006 and 2005, respectively (see Note 14).

Operating Lease Commitments - Group as Lessee. The Group has entered into various lease agreements as a lessee. Management has determined that all the significant risks and benefits of ownership of these properties, which the Group leases under operating lease arrangements, remain with the lessor. Accordingly, the leases were accounted for as operating leases.

Rent expense amounted to ₱1,793.6 million, ₱1,493.7 million and ₱1,068.9 million for the periods ended December 31, 2007, 2006 and 2005, respectively (see Note 23).

Impairment of AFS Investments - Significant and Prolonged Decline in Fair Value. The Group determines that an AFS investment is impaired when there has been a significant or prolonged decline in the fair value below its cost. The Group determines that a decline in fair value of greater than 20% of cost is considered to be a significant decline and a decline for a period of more than twelve months is considered to be a prolonged decline. This determination of what is significant or prolonged requires judgment. In making this judgment, the Group evaluates, among other factors, the normal volatility in price. In addition, impairment may be appropriate when there is evidence of deterioration in the financial health of the investee, industry and sector performance.

Estimates and Assumptions

The key assumptions concerning the future and other key sources of estimation uncertainty at balance sheet date that have a significant risk of causing material adjustments to the carrying amounts of assets and liabilities within the next financial year are discussed below:

Impairment of Receivables. The Group maintains an allowance for doubtful accounts at a level considered adequate to provide for potential uncollectible receivables. The level of allowance is evaluated by the Group on the basis of factors that affect the collectibility of the accounts. These factors include, but are not limited to, the length of the Group's relationship with the customers and counterparties, average age of accounts and collection experience. The Group performs a regular review of the age and status of these accounts, designed to identify accounts with objective evidence of impairment and provide the appropriate allowance for doubtful accounts. The review is accomplished using a combination of specific and collective assessment. The amount and timing of recorded expenses for any period would differ if the Group made different judgments or utilized different methodologies. An increase in allowance for doubtful accounts would increase the recorded selling, general and administrative expenses and decrease current assets.

Receivables, including noncurrent portion of receivables from real estate buyers, net of allowance for doubtful accounts, amounted to ₱15,036.4 million and ₱7,287.8 million as of December 31, 2007 and 2006, respectively (see Notes 10 and 16).

Impairment of AFS Investments - Calculation of Impairment Losses. The computation for the impairment of AFS debt instruments requires an estimation of the present value of the expected future cash flows and the selection of an appropriate discount rate. In the case of AFS equity instruments, the Group expands its analysis to consider changes in the investee's industry and sector performance, legal and regulatory framework, changes in technology, and other factors that affect the recoverability of the Group's investments.

The carrying values of AFS investments amounted to ₱35,942.0 million and ₱42,104.8 million as of December 31, 2007 and 2006, respectively (see Note 11).

Net Realizable Value of Merchandise Inventories. The Group writes down merchandise inventories to net realizable value, through the use of an allowance account, whenever the net realizable value of merchandise inventories becomes lower than cost due to damage, physical deterioration, obsolescence, changes in price levels or other causes.

Estimates of net realizable value are based on the most reliable evidence available at the time the estimates are made of the amount the merchandise inventories are expected to be realized. These estimates take into consideration fluctuations of price or cost directly relating to events occurring after balance sheet date to the extent that such events confirm conditions existing at balance sheet date. The allowance account is reviewed on a regular basis to reflect the accurate valuation in the financial records.

In 2007 and 2006, the Group assessed that the net realizable value of merchandise inventories is higher than cost, hence the Group did not recognize any losses on writedown of merchandise inventories. The carrying value of merchandise inventories amounted to ₱5,958.3 million and ₱4,488.2 million as of December 31, 2007 and 2006, respectively.

Estimated Useful Lives of Property and Equipment and Investment Properties. The useful life of each of the Group's property and equipment and investment properties is estimated based on the period over which the asset is expected to be available for use. Such estimation is based on a collective assessment of industry practice, internal technical evaluation and experience with similar assets. The estimated useful life of each asset is reviewed periodically and updated if expectations differ from previous estimates due to physical wear and tear, technical or commercial obsolescence and legal or other limitations on the use of the asset. It is possible, however, that future financial performance could be materially affected by changes in the amounts and timing of recorded expenses brought about by changes in the factors mentioned above. A reduction in the estimated useful life of any property and equipment and investment properties would increase the recorded selling, general and administrative expenses and decrease noncurrent assets.

The total carrying values of property and equipment and investment properties amounted to ₱82,165.8 million and ₱68,722.5 million as of December 31, 2007 and 2006, respectively (see Notes 13 and 14).

Impairment of Investments in Shares of Stock of Associates. Impairment review of investments in shares of stock of associates is performed when events or changes in circumstances indicate that the carrying value may not be recoverable. This requires management to make an estimate of the expected future cash flows from the investments and to choose a suitable discount rate in order to calculate the present value of those cash flows.

Allowances for impairment losses as of December 31, 2006 amounted to ₱430.0 million and none as of December 31, 2007. The carrying values of investments in shares of stock of associates amounted to ₱42,478.9 million and ₱46,546.8 million as of December 31, 2007 and 2006, respectively (see Note 12).

Impairment of Goodwill. The Group determines whether goodwill is impaired at least annually. This requires an estimation of the value in use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and choose a suitable discount rate to calculate the present value of those cash flows.

The carrying value of goodwill as of December 31, 2007 and 2006 amounted to ₱5,669.9 million and ₱5,115.4 million, respectively (see Note 16).

Impairment of Trademarks and Brand Names with Indefinite Lives. The Group determines whether trademarks and brand names are impaired at least annually. This requires an estimation of the value in use of the assets. Estimating the value in use requires management to make an estimate of the expected future cash flows from the trademarks and brand names and also to choose a suitable discount rate in order to calculate the present value of those cash flows.

The carrying value of trademarks and brand names amounted to ₱6,124.8 million as of December 31, 2007 and 2006 (see Note 16).

Impairment of Other Nonfinancial Asset with Definite Lives. The Group assesses at each reporting date whether there is an indication that an item of property and equipment, investment properties and land and development may be impaired. Determining the value of the assets, which requires the determination of future cash flows expected to be generated from the continued use and ultimate disposition of such assets, requires the Group to make estimates and assumptions that can materially affect the consolidated financial statements. Future events could cause the Group to conclude that property and equipment, investment properties and land and development are impaired. Any resulting impairment loss could have a material impact on the financial position and performance of the Group.

The preparation of the estimated future cash flows involves judgment and estimations. While the Group believes that its assumptions are appropriate and reasonable, significant changes in these assumptions may materially affect the Group's assessment of recoverable values and may lead to future additional impairment charges.

The total carrying values of property and equipment, investment properties and land and development amounted to ₱86,056.8 million and ₱70,558.9 million as of December 31, 2007 and 2006, respectively (see Notes 13, 14 and 15).

Purchase Price Allocation in Business Combinations. Purchase method requires extensive use of accounting estimates and judgments to allocate the purchase price to the fair market values of the acquiree's identifiable assets and liabilities at acquisition date. It also requires the acquirer to recognize goodwill. The Group's acquisitions have resulted in goodwill and trademarks and brand names with indefinite lives.

The total carrying values of goodwill and trademarks and brand names with indefinite useful lives arising from business combinations as of December 31, 2007 and 2006 amounted to ₱11,794.7 million and ₱11,240.2 million, respectively (see Note 16).

Realizability of Deferred Tax Assets. The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax assets to be utilized. The Group's assessment on the recognition of deferred tax assets on deductible temporary differences and carryforward benefits of minimum corporate income tax (MCIT) and net operating loss carryover (NOLCO) is based on the projected taxable income in the following periods. Based on the projection, not all deductible temporary differences and carryforward benefits of MCIT and NOLCO will be realized. Consequently, only a portion of the Group's deferred tax assets was recognized.

Deferred tax assets recognized in the consolidated balance sheets as of December 31, 2007 and 2006 amounted to ₱1,439.3 million and ₱353.8 million, respectively, while the unrecognized deferred tax assets as of December 31, 2007 and 2006 amounted to ₱2,458.2 million and ₱2,789.1 million, respectively (see Notes 16 and 26).

Present Value of Defined Benefit Obligation. The present value of the pension obligations depends on a number of factors that are determined on an actuarial basis using a number of assumptions. These assumptions include, among others, discount rate, expected rate of return on plan assets and rate of salary increase. Actual results that differ from the Group's assumptions are accumulated and amortized over future periods and therefore, generally affect the recognized expense and recorded obligation in such future periods.

The assumption of the expected return on plan assets is determined on a uniform basis, taking into consideration the long-term historical returns, asset allocation and future estimates of long-term investment returns.

The Group determines the appropriate discount rate at the end of each year. It is the interest rate that should be used to determine the present value of estimated future cash outflows expected to be required to settle the pension obligations. In determining the appropriate discount rate, the Group considers the interest rates on government bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating the terms of the related pension liability.

Other key assumptions for pension obligations are based in part on current market conditions.

While it is believed that the Group's assumptions are reasonable and appropriate, significant differences in actual experience or significant changes in assumptions may materially affect the Group's pension and other pension obligations.

The Group has a net cumulative unrecognized actuarial loss amounting to ₱321.9 million, ₱226.2 million and ₱82.6 million as of December 31, 2007, 2006 and 2005, respectively (see Note 25).

Fair Value of Financial Assets and Liabilities. The Group carries certain financial assets and liabilities at fair value, which requires extensive use of accounting estimates and judgments. The significant components of fair value measurement were determined using verifiable objective evidence (i.e., foreign exchange rates, interest rates, volatility rates). The amount of changes in fair value would differ if the Group utilized different valuation methodologies and assumptions. Any changes in the fair value of these financial assets and liabilities would directly affect profit and loss and equity.

The fair value of financial assets and liabilities are discussed in Note 29.

Contingencies. The Group is currently involved in legal and administrative proceedings. The Group's estimate of the probable costs for the resolution of these proceedings has been developed in consultation with outside legal counsel handling defense in these matters and is based upon an analysis of potential results. The Group currently does not believe that these proceedings will have a material adverse effect on its financial position and performance. It is possible, however, that future financial performance could be materially affected by changes in the estimates or in the effectiveness of strategies relating to these proceedings. No accruals were made in relation to these proceedings (see Note 32).

4. Summary of Significant Accounting Policies

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 are subject to an insignificant risk of change in value.

Financial Assets and Liabilities

Date of Recognition. The Group recognizes a financial asset or a financial liability in the consolidated balance sheets when it becomes a party to the contractual provisions of the instrument. In the case of a regular way purchase or sale of financial assets, recognition and derecognition, as applicable, is done using settlement date accounting.

Initial Recognition of Financial Instruments. Financial instruments are recognized initially at fair value, which is the fair value of the consideration given (in case of an asset) or received (in case of a liability). The initial measurement of financial instruments, except for those designated at fair value through profit and loss (FVPL), includes transaction cost.

Subsequent to initial recognition, the Group classifies its financial instruments in the following categories: financial assets and financial liabilities at FVPL, loans and receivables, held-to-maturity (HTM) investments, AFS financial assets and other financial liabilities. The classification depends on the purpose for which the instruments are acquired and whether they are quoted in an active market. Management determines the classification at initial recognition and, where allowed and appropriate, re-evaluates this classification at every reporting date.

Determination of Fair Value. The fair value of financial instruments traded in active markets at balance sheet 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 Profit. Where the transaction price in a non-active market is different from the fair value of other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable market, the Group recognizes the difference between the transaction price and fair value (a Day 1 profit) in the consolidated statements 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 consolidated statements of income when the inputs become observable or when the instrument is derecognized. For each transaction, the Group determines the appropriate method of recognizing 'Day 1' profit amount.

Financial Assets

Financial Assets at FVPL. Financial assets at FVPL include financial assets held for trading and financial assets designated upon initial recognition as at FVPL.

Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. Gains or losses on investments held for trading are recognized in the consolidated statements of income under "Gain on sale of available-for-sale investments and fair value changes on investments held for trading and derivatives" account.

Financial assets may be designated by management at initial recognition as at FVPL when any of the following criteria is met:

- the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or recognizing gains or losses on a different basis; or

- the assets are part of a group of financial assets, financial liabilities or both which are managed and their performance are evaluated on a fair value basis, in accordance with a documented risk management or investment strategy; or

- the financial instrument contains an embedded derivative, unless the embedded derivative does not significantly modify the cash flows or it is clear, with little or no analysis, that it would not be separately recorded.

The Group's investments held for trading (see Note 9) and derivative assets (see Notes 16 and 29) are classified under this category.

The carrying values of financial assets under this category amounted to ₱3,296.3 million and ₱10,300.8 million as of December 31, 2007 and 2006, respectively (see Note 29).

Loans and Receivables. Loans and receivables are nonderivative financial assets with fixed or determinable payments that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not designated as AFS financial assets or financial assets at FVPL. Loans and receivables are carried at cost or amortized cost, less impairment in value. Amortization is determined using the effective interest method. Loans and receivables are included in current assets if maturity is within 12 months from balance sheet date. Otherwise, these are classified as noncurrent assets.

The Group's cash and cash equivalents, time deposits, short-term investments and receivables, including noncurrent portion of receivables from real estate buyers, are classified under this category (see Notes 7, 8, 10 and 16).

The carrying values of financial assets under this category amounted to ₱38,869.7 million and ₱36,150.5 million as of December 31, 2007 and 2006, respectively (see Note 29).

HTM Investments. HTM investments are quoted nonderivative financial assets with fixed or determinable payments and fixed maturities for which the Group's management has the positive intention and ability to hold to maturity. Where the Group sells other than an insignificant amount of HTM investments, the entire category would be tainted and reclassified as AFS securities. After initial measurement, these investments are measured at amortized cost using the effective interest 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 consolidated statements of income when the HTM investments are derecognized or impaired, as well as through the amortization process. Assets under this category are classified as current assets if maturity is within 12 months from balance sheet date and as noncurrent assets if maturity date is more than a year from balance sheet date.

The Group has no investments classified under this category.

AFS Financial Assets. AFS financial assets are nonderivative financial assets that are designated in this category or are not classified in any of the other categories. Subsequent to initial recognition, AFS financial assets are carried at fair value in the consolidated balance sheets. Changes in the fair value of such assets are reported as net unrealized gain on AFS investments in the stockholders' equity section of the consolidated balance sheets until the investment is derecognized or the investment is determined to be impaired. On derecognition or impairment, the cumulative gain or loss previously reported in equity is transferred to the consolidated statements of income. Interest earned on holding AFS investments are recognized in the consolidated statements of income using the effective interest rate. Assets under this category are classified as current assets if expected to be realized within 12 months from balance sheet date and as noncurrent assets if maturity date is more than a year from balance sheet date.

The Group's investments in shares of stock, redeemable preferred shares, government bonds and club shares are classified under this category (see Note 11).

The carrying values of financial assets under this category amounted to ₱35,942.0 million and ₱42,104.8 million as of December 31, 2007 and 2006, respectively (see Note 29).

Financial Liabilities

Financial Liabilities at FVPL. Financial liabilities are classified in this category if these result from trading activities or derivative transactions that are not accounted for as accounting hedges, or when the Group elects to designate a financial liability under this category.

The Group's derivative liabilities arising from issuance of convertible bonds and future sale of AFS investments in San Miguel Corporation (SMC) common shares and derivative financial instruments with negative fair values are included under this category (see Notes 11, 19 and 29).

The carrying values of financial liabilities under this category amounted to ₱3,290.9 million and ₱1,042.5 million as of December 31, 2007 and 2006, respectively (see Note 29).

Other Financial Liabilities. This category pertains to financial liabilities that 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.

Financial liabilities are recognized initially at fair value and are subsequently carried at amortized cost, taking into account the impact of applying the effective interest method of amortization (or accretion) for any related premium, discount and any directly attributable transaction costs.

The Group's bank loans, accounts payable and other current liabilities, dividends payable, notes payable, long-term debt and tenants' deposits are classified under this category (see Notes 17, 18, 19 and 29).

The carrying values of financial liabilities under this category amounted to ₱84,854.7 million and ₱91,184.8 million as of December 31, 2007 and 2006, respectively (see Note 29).

<u>Classification of Financial Instruments Between Debt and Equity</u>
A financial instrument is classified as debt if it provides for a contractual obligation to:

- deliver cash or another financial asset to another entity; or

- exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavorable to the Group; or

- satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity shares.

If the Group does not have an unconditional right to avoid delivering cash or another financial asset to settle its contractual obligation, the obligation meets the definition of a financial liability.

<u>Redeemable Preferred Shares</u>
In determining whether a preferred share is a financial liability or an equity instrument, the Group assesses the particular rights attaching to the share to determine whether it exhibits the fundamental characteristic of a financial liability. A preferred share that provides for mandatory redemption by the Group for a fixed or determinable amount at a fixed or determinable future date, or gives the holder the right to require the Group to redeem the instrument at or after a particular date for a fixed or determinable amount, is a financial liability.

The redeemable preferred shares of the Group exhibit the characteristics of a financial liability and are thus recognized as a liability under "Long-term debt" account in the 2007 consolidated balance sheet, net of transaction costs. The corresponding dividends on the shares are charged as interest expense in the 2007 consolidated statement of income.

Transaction costs are amortized over the maturity period of the preferred shares using effective interest rate method.

<u>Debt Issue Costs</u>
Debt issue costs are deducted against long-term debt and are amortized over the terms of the related borrowings using the effective interest method.

<u>Derivative Financial Instruments and Hedging</u>

Freestanding Derivative. The Group uses derivative financial instruments such as long-term currency swaps, foreign currency call options, interest rate swaps and nondeliverable forwards to hedge the risks associated with foreign currency and interest rate fluctuations. Such derivative financial instruments are initially recognized at fair value on the date on which the derivative contract is entered into and are subsequently re-measured at fair value. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

The Group's derivative instruments provide economic hedges under the Group's policies but are not designated as accounting hedges. Consequently, any gains or losses arising from changes in fair value are taken directly to profit or loss for the year.

Embedded Derivative. The Group assesses whether embedded derivatives are required to be separated from host contracts when the Group first becomes party to the contract. An embedded derivative is separated from the host contract and accounted for as a derivative if all of the following conditions are met: a) the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract; b) a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and c) the hybrid or combined instrument is not recognized at fair value through profit or loss. Reassessment only occurs if there is a change in the terms of the contract that significantly modifies the cash flows that would otherwise be required.

Derecognition of Financial Assets and Liabilities

Financial Assets. A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognized when:

- the rights to receive cash flows from the asset have expired;

- the Group retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; or

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

When the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset, the asset is recognized to the extent of the Group's continuing involvement in the asset.

Financial Liabilities. A financial liability is derecognized when the obligation under the liability is discharged or cancelled or expired.

When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such 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 profit and loss.

Impairment of Financial Assets
The Group assesses at each balance sheet date whether a financial asset or a group of financial assets is impaired.

Assets Carried at Amortized Cost. If there is objective evidence that an impairment loss on loans and receivables carried at amortized cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition). The carrying amount of the asset shall be reduced through the use of an allowance account. The amount of the loss shall be recognized in the consolidated statements of income.

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

Assets Carried at Cost. If there is objective evidence that an impairment loss has been incurred in 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, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset.

AFS Financial Assets. If an AFS financial asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortization) and its current fair value, less any impairment loss previously recognized in profit or loss, is transferred from equity to the consolidated statements of income. Reversals in respect of equity instruments classified as AFS are not recognized in profit. Reversals of impairment losses on debt instruments are reversed through profit or loss, if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognized in profit or loss.

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

Merchandise Inventories
Merchandise inventory is valued at the lower of cost or net realizable value. Cost, which includes all costs directly attributable to acquisition, such as purchase price and transport costs, is primarily determined using the weighted average method. Net realizable value is the estimated selling price in the ordinary course of business, less estimated costs necessary to make the sale.

Land and Development and Condominium Units for Sale
Land and development and condominium units for sale (included under "Input taxes and other current assets" account in the consolidated balance sheets) are stated at the lower of cost or net realizable value. Net realizable value is the selling price in the ordinary course of business, less costs of completion and the estimated cost to make the sale. Cost includes those costs incurred for development and improvement of the properties.

Investments in Shares of Stock of Associates
The Group's investments in shares of stock of associates are accounted for under the equity method of accounting. An associate is an entity in which the Group has significant influence and which is neither a subsidiary nor a joint venture.

Under the equity method, the investment in an associate is carried in the consolidated balance sheets at cost plus post-acquisition changes in the Group's share in net assets of the associate. Goodwill relating to an associate is included in the carrying amount of the investment and is not amortized. After application of the equity method, the Group determines whether it is necessary to recognize any additional impairment loss with respect to the Group's net investment in the associate. The consolidated statements of income reflect the share in the results of operations of the associate. Where there has been a change recognized directly in the equity of the associate, the Group recognizes its share in any changes and discloses this, when applicable, in the consolidated statements of changes in stockholders' equity. Profits and losses resulting from transactions between the Group and the associate are eliminated to the extent of the interest in the associate.

An investment in an associate is accounted for using the equity method from the date when it becomes an associate. On acquisition of the investment, any difference between the cost of the investment and the investor's share in the net fair value of the associate's identifiable assets, liabilities and contingent liabilities is accounted for in accordance with PFRS 3, *Business Combinations*. Consequently:

a. goodwill relating to an associate is included in the carrying amount of the investment. However, amortization of that goodwill is not permitted and is therefore not included in the determination of the Group's share in the associate's profits or losses.

b. any excess of the Group's share in the net fair value of the associate's identifiable assets, liabilities and contingent liabilities over the cost of the investment is excluded from the carrying amount of the investment and is instead included as income in the determination of the Group's share in the associate's profit or loss in the period in which the investment is acquired.

The Group discontinues applying the equity method when its investment in an associate is reduced to zero. Additional losses are provided only to the extent that the Group has incurred obligations or made payments on behalf of the associate to satisfy obligations of the investee that the Group has guaranteed or otherwise committed. If the investee subsequently reports profits, the Group resumes applying the equity method only after its share of the profits equals the share of net losses not recognized during the period the equity method was suspended.

The financial statements of the associates are prepared for the same reporting period as the Parent Company. The accounting policies of the associates conform to those used by the Group for like transactions and events in similar circumstances.

Property and Equipment

Property and equipment, except land, is stated at cost less accumulated depreciation and amortization and any accumulated impairment in value. Such cost includes the cost of replacing part of the property and equipment at the time that cost is incurred, if the recognition criteria are met, and excludes the costs of day-to-day servicing. Land is stated at cost less any impairment in value.

The initial cost of property and equipment consists of its purchase price, including import duties, taxes and any directly attributable costs necessary in bringing the asset to its working condition and location for its intended use. Cost also includes any related asset retirement obligation and interest incurred during the construction period on funds borrowed to finance the construction of the projects. Expenditures incurred after the item has been put into operation, such as repairs, maintenance and overhaul costs, are normally recognized as expense in the period such costs are incurred. In situations where it can be clearly demonstrated that the expenditures have improved the condition of the asset beyond the originally assessed standard of performance, the expenditures are capitalized as additional cost of property and equipment.

Depreciation and amortization are calculated on a straight-line basis over the following estimated useful lives of the assets:

Buildings, condominium units and improvements	5-25 years
Store equipment and improvements	5-10 years
Data processing equipment	5 years
Furniture, fixtures and office equipment	3-10 years
Machinery and equipment	5-10 years
Leasehold improvements	5-10 years or term of the lease, whichever is shorter
Transportation equipment	5-10 years

The residual values, useful lives and method of depreciation and amortization of the assets are reviewed and adjusted, if appropriate, at each financial year-end.

The carrying values of property and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Fully depreciated assets are retained in the accounts until they are no longer in use and no further depreciation is credited or charged to current operations.

When each major inspection is performed, its cost is recognized in the carrying amount of the property and equipment as a replacement if the recognition criteria are satisfied.

An item of property and equipment is derecognized when either it has been disposed or when it is permanently withdrawn from use and no future economic benefits are expected from its use or disposal. Any gains or losses arising on the retirement and disposal of an item of property and equipment are recognized in the consolidated statements of income in the period of retirement or disposal.

Construction in Progress

Construction in progress represents structures under construction and is stated at cost. This includes cost of construction, property and equipment, and other direct costs. Cost also includes interest on borrowed funds incurred during the construction period. Construction in progress is not depreciated until such time that the relevant assets are completed and are ready for use.

Investment Properties

Investment properties, except land, are measured initially at cost, including transaction costs, less accumulated depreciation and amortization and accumulated impairment in value. The carrying amount includes the cost of replacing part of an existing investment property at the time that cost is incurred if the recognition criteria are met, and excludes the costs of day-to-day servicing of an investment property. Land is stated as cost less any impairment in value.

Depreciation and amortization are calculated on a straight-line basis over the following estimated useful lives of the assets:

Buildings and improvements	35 years
Building equipment, furniture and others	3-15 years

The residual values, useful lives and method of depreciation and amortization of the assets are reviewed and adjusted, if appropriate, at each financial year-end.

Investment property is derecognized when either it has been disposed or when it is permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gains or losses on the retirement or disposal of an investment property are recognized in the consolidated statements of income in the period of retirement or disposal.

Transfers are made to investment property when, and only when, there is a change in use, evidenced by ending of owner-occupation, commencement of an operating lease to another party or ending of construction or development. Transfers are made from investment property when, and only when, there is a change in use, evidenced by commencement of owner-occupation or commencement of development with a view to sell.

For a transfer from investment property to owner-occupied property or inventories, the cost of property for subsequent accounting is its carrying value at the date of change in use. If the property occupied by the Group as an owner-occupied property becomes an investment property, the Group accounts for such property in accordance with the policy stated under property and equipment up to the date of change in use.

Business Combinations

Business combinations are accounted for using the purchase method of accounting. The cost of acquisition is the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the acquirer, in exchange for control over the net assets of the acquired company, plus any directly attributable costs. The identifiable assets, liabilities and contingent liabilities that satisfy certain recognition criteria have to be measured initially at their fair values at acquisition date, irrespective of the extent of any minority interest.

Goodwill

Goodwill acquired in a business combination is initially measured at cost being the excess of the cost of the business combination over the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities. Following initial recognition, goodwill is measured at cost less any accumulated impairment in value.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units. Each unit or group of units to which the goodwill is so allocated:

- represents the lowest level within the Group at which the goodwill is monitored for internal management purposes; and

- is not larger than a segment based on either the Group's primary or the Group's secondary reporting format determined in accordance with PAS 14, *Segment Reporting.*

Goodwill is reviewed for impairment, annually or more frequently, if events or changes in circumstances indicate that the carrying value may be impaired.

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units), to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognized. Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operation within that unit is disposed, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed and the portion of the cash-generating unit retained.

When the Group acquires a business, embedded derivatives separated from the host contract by the acquiree are not reassessed on acquisition unless the business combination results in a change in the terms of the contract that significantly modifies the cash flows that would otherwise be required under the contract.

Negative goodwill, which is not in excess of the fair values of acquired identifiable nonmonetary assets of subsidiaries and associates, is charged directly to income. Transfers of assets between commonly controlled entities are accounted for under historical cost accounting.

When a business combination involves more than one exchange transaction (occurs in stages), each exchange transaction is treated separately by the acquirer, using the cost of the transaction and fair value information at the date of each exchange transaction, to determine the amount of goodwill associated with that transaction. Any adjustment to fair values relating to the previously held interest is a revaluation and is accounted for as such.

When subsidiaries are sold, the difference between the selling price and the net assets plus goodwill is recognized in the consolidated statements of income.

Intangible Assets

The cost of trademarks and brand names acquired in a business combination is the fair value as at the date of acquisition. The Group assessed the useful life of the trademarks and brand names to be indefinite because based on an analysis of all of the relevant factors, there is no foreseeable limit to the period over which the asset is expected to generate cash inflows for the Group.

Trademarks and brand names with indefinite useful lives are tested for impairment annually either individually or at the cash generating unit level. Such intangible assets are not amortized. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is made on a prospective basis.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognized in the consolidated statements of income when the asset is derecognized.

Impairment of Non-financial Assets with Definite Lives

The carrying values of property and equipment, investment properties, land and development and investments in shares of stock of associates are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable. If any such indication exists, and if the carrying value exceeds the estimated recoverable amount, the assets or cash-generating units are written down to their recoverable amounts. The recoverable amount of the asset is the greater of fair value less costs to sell or value in use. The fair value less costs to sell is the amount obtainable from the sale of an asset in an arm's-length transaction between knowledgeable, willing parties, less costs of disposal. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognized in the consolidated statements of income in those expense categories consistent with the function of the impaired asset.

An assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. If that is the case, the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation and amortization, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in profit or loss. After such a reversal, the depreciation or amortization charge is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

Revenue

Revenue is recognized when it is probable that the economic benefits associated with the transaction will flow to the Group and the amount of the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognized:

Sale of merchandise inventories. Revenue is recognized when the significant risks and rewards of ownership of the goods have passed to the buyer, which is normally upon delivery.

Sale of Real Estate. Revenue and costs from sale of completed projects are accounted for using the full accrual method. The percentage of completion method is used to recognize income from sale of projects where the Group has material obligations under the sales contract to complete the project after the property is sold. Under this method, sale is recognized as the related obligations are fulfilled, measured principally on the basis of the estimated completion of a physical portion of the contract work. Any excess of collections over the recognized receivables is included in "Accounts payable and other current liabilities" in the consolidated balance sheets.

Real estate costs that relate to the acquisition, development, improvement and construction of the condominium units are capitalized. The capitalized costs of condominium units are charged to operations when the related revenue are recognized.

For income tax purposes, full recognition is applied when at least 25% of the selling price has been collected in the period of sale. Otherwise, the installment method is applied.

Rent. Revenue is recognized on a straight-line basis over the lease term or based on the terms of the lease, as applicable.

Sale of Cinema and Amusement Tickets. Revenue is recognized upon receipt of cash from the customer which coincides with the rendering of services.

Gain on Sale of Investments in Shares of Stock and Available-for-Sale Investments. Revenue is recognized upon delivery of the securities to and confirmation of the sale by the broker.

Dividend. Revenue is recognized when the Group's right as a shareholder to receive the payment is established.

Management Fees. Revenue is recognized when earned in accordance with the terms of the agreements.

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

Management Fees

Management fees are recognized as expense in accordance with the terms of the agreements.

Pensions Benefits

The cost of providing benefits under the defined benefit plans is determined separately for each plan using the projected unit credit actuarial valuation method. This method reflects service rendered by employees to the date of valuation and incorporates assumptions concerning employees' projected salaries. Pension cost includes current service cost, interest cost, expected return on plan assets, amortization of unrecognized past service costs, recognition of actuarial gains (losses) and effect of any curtailments or settlements. Past service cost is amortized over a period until the benefits become vested. The portion of the actuarial gains and losses is recognized when it exceeds the "corridor" (10% of the greater of the present value of the defined benefit obligation or fair value of the plan assets) at the previous reporting date, divided by the expected average remaining working lives of active plan members.

The defined benefit liability is the aggregate of the present value of the defined benefit obligation and actuarial gains and losses not recognized, reduced by past service cost not yet recognized and the fair value of plan assets, out of which the obligations are to be settled directly. If such aggregate is negative, the asset is measured at the lower of such aggregate or the aggregate of cumulative unrecognized net actuarial losses and past service cost and the present value of any economic benefits available in the form of refunds from the plan or reductions in the future contributions to the plan.

If the asset is measured at the aggregate of cumulative unrecognized net actuarial losses and past service cost, and the present value of any economic benefits available in the form of refunds from the plan or reductions in the future contributions to the plan, net actuarial losses of the current period and past service cost of the current period are recognized immediately to the extent that they exceed any reduction in the present value of those economic benefits. If there is no change or if there is an increase in the present value of the economic benefits, the entire net actuarial losses of the current period and past service cost of the current period are recognized immediately. Similarly, net actuarial gains of the current period after the deduction of past service cost of the current period exceeding any increase in the present value of the economic benefits stated above are recognized immediately if the asset is measured at the aggregate of cumulative unrecognized net actuarial losses and past service cost and the present value of any economic benefits available in the form of refunds from the plan or reductions in the future contributions to the plan. If there is no change or if there is a decrease in the present value of the economic benefits, the entire net actuarial gains of the current period after the deduction of past service cost of the current period are recognized immediately.

Foreign Currency-denominated Transactions

The consolidated financial statements are presented in Philippine peso, which is the Group's functional and presentation currency. Transactions in foreign currencies are initially recorded in the functional currency rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are restated at the functional currency rate of exchange at balance sheet date. All differences are taken to the consolidated statements of income.

Leases

The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement and requires an assessment of whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Group as Lessee. Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalized at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are reflected in the consolidated statements of income.

Capitalized leased assets are depreciated over the shorter of the estimated useful life of the asset and the lease term, if there is no reasonable certainty that the Group will obtain ownership by the end of the lease term.

Leases which do not transfer to the Group substantially all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognized as expense in the consolidated statements of income on a straight-line basis over the lease term. Associated costs, such as maintenance and insurance, are expensed as incurred.

Group as Lessor. Leases where the Group does not transfer substantially all the risks and benefits of ownership of the asset are classified as operating leases. Lease income from operating leases are recognized as income on a straight-line basis over the lease term. Initial direct costs incurred in negotiating an operating lease are added to the carrying amount of the leased asset and recognized over the lease term on the same basis as rental income. Contingent rents are recognized as revenue in the period in which they are earned.

Provisions

Provisions are recognized when the Group 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. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as interest expense. Where the Group expects a provision to be reimbursed, the reimbursement is recognized as a separate asset but only when the receipt of the reimbursement is virtually certain.

Borrowing Costs

Borrowing costs are generally expensed as incurred. Borrowing costs are capitalized if they are directly attributable to the acquisition or construction of a qualifying asset. Capitalization of borrowing costs commences when the activities to prepare the asset are in progress and expenditures and borrowing costs are being incurred. Borrowing costs are capitalized until the assets are substantially ready for their intended use. If the carrying amount of the asset exceeds its recoverable amount, an impairment loss is recognized. Borrowing costs include interest charges and other costs incurred in connection with the borrowing of funds used to finance the construction in progress.

Taxes

Current Tax. Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted as at balance sheet date.

Deferred Tax. Deferred tax is provided using the balance sheet liability method on temporary differences at balance sheet 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, except:

- where the deferred tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- with respect to taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognized for all deductible temporary differences and carryforward benefits of MCIT and NOLCO, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward benefits of MCIT and NOLCO can be utilized, except:

- where the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- with respect to deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilized. Unrecognized deferred tax assets are reassessed at each balance sheet date and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at balance sheet date.

Income tax relating to items recognized directly in equity is recognized in equity and not in the consolidated statements of income.

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

Value Added Tax. Revenue, expenses and assets are recognized net of the amount of tax, except:

- where the tax incurred on a purchase of assets or services is not recoverable from the taxation authority, in which case the tax is recognized as part of the cost of acquisition of the asset or as part of the expense item as applicable; and

- receivables and payables that are stated with the amount of tax included.

The net amount of tax recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the consolidated balance sheets.

Business Segments

The Group is organized and managed separately according to the nature of business. The three major operating businesses of the Group are shopping mall development, retail merchandising, and real estate development and tourism. These operating businesses are the basis upon which the Group reports its primary segment information presented in Note 6 to the consolidated financial statements.

Basic/Diluted Earnings Per Common Share (EPS)

Basic EPS is computed by dividing the net income for the period attributable to equity holders of the Parent by the weighted-average number of issued and outstanding common shares during the period, with retroactive adjustment for any stock dividends declared.

For the purpose of computing diluted EPS, the net income for the period attributable to equity holders of the Parent and the weighted-average number of issued and outstanding common shares are adjusted for the effects of all dilutive potential ordinary shares.

Contingencies

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

Subsequent Events

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

5. Business Combinations

Acquisition of Rappel

On July 27, 2007, Orkam Holding Asia N.V. sold its 40% equity in Rappel to Forsyth Equity Holdings, Inc. (Forsyth). On October 3, 2007, Forsyth sold the said shares to SMIC, which increased SMIC's direct ownership in Rappel from 40% to 80%. Rappel is an unlisted company engaged in the business of investing, purchasing, acquiring and owning real or personal property, including shares of stock, bonds and other forms of securities.

SMIC and Rappel directly owns 10% and 50% interests in Pilipinas Makro, Inc. (Makro), respectively. Makro is an unlisted company engaged in buying and selling of food and non-food items to registered customers at wholesale and/or retail under a warehouse club format. As a result of the acquisition of an additional 40% interest in Rappel, Makro also became a subsidiary of SMIC through the 60% direct and indirect ownership.

The fair values of the identifiable assets and liabilities of Rappel, which were determined only provisionally because fair values were not currently available as at the date of acquisition, and the corresponding carrying amounts immediately before the acquisition are as follows:

	Fair Value	Carrying Value
Cash and cash equivalents	₱221,670	₱221,670
Investment in Makro	1,713,181,750	1,713,181,750
	1,713,403,420	1,713,403,420
Trade and other payables	(245,411)	(245,411)
Net assets	1,713,158,009	1,713,158,009
% of ownership acquired	40%	40%
Net assets acquired	685,263,204	₱685,263,204
Goodwill arising from acquisition (see Note 16)	243,171,074	
Total consideration	₱928,434,278	

The acquisition cost and the net cash outflow on the acquisition are as follows:

Acquisition Cost:	
Cash paid	₱928,166,527
Costs associated with the acquisition	267,751
	₱928,434,278

Cash outflow on acquisition:	
Net cash acquired with the subsidiary	₱221,670
Cash paid	(928,434,278)
Net cash outflow	(₱928,212,608)

From the date of acquisition, Rappel has contributed ₱22.3 million loss to the net income of the Group. If the combination had taken place at the beginning of 2007, the consolidated net income attributable to the equity holders of the Parent for the year ended December 31, 2007 would have been ₱11,991.5 million and the consolidated revenue would have been ₱132,152.3 million.

Acquisition of APCTC

On June 26, 2007, SMIC acquired additional 18,210 common shares of APCTC, which is equivalent to 15.10% of the issued and outstanding capital of APCTC. The acquisition increased SMIC's interest in APCTC from 36.69% to 51.79%, thereby gaining control. APCTC is an unlisted company engaged in selling computer and its peripherals and providing computer training and education services to college students.

The total cost of the acquisition, which was paid in cash, was ₱1.8 million. At acquisition date, the fair value of the net liabilities acquired amounted to ₱2.1 million, resulting in recognition of goodwill of ₱3.9 million. The amount of cash and cash equivalents acquired from APCTC amounted to ₱4.0 million, thus, the net cash inflow from the acquisition amounted to ₱2.2 million.

The acquisition cost of the initial 36.69% interest approximates the fair value of the net assets acquired, hence, no goodwill was recognized therefrom.

Acquisition of SVI and SSMI

On December 13, 2005, the BOD approved SMIC's acquisition of 100% of the outstanding common shares of SVI and 81% of the outstanding common shares of SSMI in exchange for SMIC common shares with a valuation based on the 30-day volume weighted average price of SMIC.

On June 9, 2006, SMIC executed the relevant documents for the exchange of SVI and SSMI shares of stock for 56,000,000 shares of SMIC common stock to be issued upon the approval by the Philippine Securities and Exchange Commission (SEC) and the PSE.

On June 28, 2006, the PSE approved the listing of 56,000,000 new shares in connection with the share-for-share swap transaction with SVI and SSMI. On November 6, 2006, the Philippine SEC approved the valuation and confirmed that the issuance of the shares is exempt from registration requirements. Pursuant to the agreements entered into among SMIC, SVI and SSMI, the 56,000,000 shares were exchanged for 2,000,000 common shares (100%) of SVI and 810,000 common shares (81%) of SSMI at a total swap price of ₱13,104.0 million. The listing of the shares was completed on November 17, 2006. As a result of the acquisition, SVI and SSMI became wholly-owned subsidiaries of SMIC (see Note 20).

Acquisition of SVI
SVI is an unlisted company engaged in the business of buying and selling, at retail, all kinds of goods.

The fair values of the identifiable assets and liabilities of SVI as at the date of acquisition and the corresponding carrying amounts immediately before the acquisition were as follows:

	Fair Value	Carrying Value
Cash and cash equivalents	₱1,502,552,535	₱1,502,552,535
Receivables	404,043,452	404,043,452
Merchandise inventories	2,418,482,931	2,269,680,194
Prepaid expenses and other current assets	305,457,492	305,457,492
Investments and advances - net	23,395,332	23,395,332
Property and equipment - net	1,536,704,443	1,374,146,398
Other noncurrent assets	55,075,715	55,075,715
Trademarks and brand names (see Note 16)	4,876,521,000	–
	11,122,232,900	5,934,351,118
Trade and other payables	(3,566,325,511)	(3,566,325,511)
Income tax payable	(106,664,453)	(106,664,453)
Deferred tax liability	(1,511,723,714)	–
	(5,184,713,678)	(3,672,989,964)
Net assets	5,937,519,222	₱2,261,361,154
Goodwill arising from acquisition (see Note 16)	4,538,525,166	
Total consideration	₱10,476,044,388	

The total cost of the acquisition was ₱10,476.0 million, consisting of issuance of equity instruments and costs directly attributable to the acquisition. The Group issued 47,900,000 shares with a fair value of ₱218 each, being the weighted average price on a 30-day calendar volume of the shares of SMIC at the date of exchange.

Cost:	
Shares issued, at fair value	₱10,442,200,000
Costs associated with the acquisition	33,844,388
	₱10,476,044,388

Cash inflow on acquisition:	
Net cash and cash equivalents acquired with the subsidiary	₱1,502,552,535
Cash paid	(33,844,388)
Net cash inflow	₱1,468,708,147

Acquisition of SSMI
SSMI is an unlisted company engaged in the business of trading, importing and exporting goods, food items and other general merchandise on a wholesale and/or retail basis.

The fair values of the identifiable assets and liabilities of SSMI as at the date of acquisition and the corresponding carrying amounts immediately before the acquisition were follows:

	Fair Value	Carrying Value
Cash and cash equivalents	₱205,532,070	₱205,532,070
Receivables	49,662,503	49,662,503
Merchandise inventories	543,079,944	466,711,087
Prepaid expenses and other current assets	35,756,036	35,756,036
Investments and advances - net	80,400	80,400
Property and equipment - net	605,621,788	595,629,177
Other noncurrent assets	117,310,654	117,310,654
Trademarks and brand names (see Note 16)	1,248,241,000	–
	2,805,284,395	1,470,681,927
Trade and other payables	(987,150,570)	(987,150,569)
Income tax payable	(62,892,931)	(62,892,931)
Deferred tax liability	(377,470,083)	–
	(1,427,513,584)	(1,050,043,500)
Net assets	1,377,770,811	₱420,638,427
Goodwill arising on acquisition (see Note 16)	412,768,880	
Total consideration	₱1,790,539,691	

The total cost of the acquisition was ₱1,790.5 million, consisting of issuance of equity instruments and costs directly attributable to the acquisition. The Group issued 8,100,000 shares with a fair value of ₱218 each, being the weighted average price on a 30-day calendar volume of the shares of SMIC at the date of exchange.

Cost:	
Shares issued, at fair value	₱1,765,800,000
Fair value of investment of SVI in SSMI	19,000,000
Costs associated with the acquisition	5,739,691
	₱1,790,539,691

Cash inflow on acquisition:	
Net cash and cash equivalents acquired with the subsidiary	₱205,532,070
Cash paid	(24,739,691)
Net cash inflow	₱180,792,379

From the date of acquisition, SVI and SSMI have contributed ₱692.8 million (before eliminating intercompany expenses totaling ₱1,532.3 million) to the net income of the Group for the year ended December 31, 2006. If the combination had taken place at the beginning of 2006, the consolidated net income of the Group for the year ended December 31, 2006 would have been ₱15,755.2 million and the consolidated revenue would have been ₱103,805.9 million.

The Business Enterprise Residual Method was used to value the intangible assets related to the acquisitions of SVI and SSMI. The total business enterprise value reflects the market value of an entity's capitalization and is determined by discounting the free cash flow projections based on the financial budgets approved by senior management covering a period of 10 years. The significant valuation assumptions used were average annual growth rate on net sales and discount rate which was based on the weighted average cost of capital. The discount rates used were 11.99% for SVI and 10.83% for SSMI.

The fair values of the identifiable assets and liabilities, except trademarks and brand names, were deducted from the business enterprise value to determine the residual value attributable to all intangible assets. The fair values of trademarks and brand names of SVI and SSMI were determined using the Relief-from-Royalty Method. The royalty rate used was 3.5%, which is the prevailing royalty rate in the retail assorted category where the two entities fall at acquisition date. The total fair value of trademarks and brand names was deducted from the residual value to determine the value of the goodwill.

6. Segment Information

Business Segments

The business segment is determined as the primary segment reporting format as the Group's risks and rates of return are affected predominantly by differences in the products and services produced. The operating businesses are organized and managed separately according to the nature of the products and services provided, with each segment representing a strategic business unit that offers different products and serves different markets.

The Group conducts its business principally in the following segments: shopping mall development, retail merchandising, and real estate development and tourism.

The shopping mall development segment develops, conducts, operates and maintains the business of modern commercial shopping centers and all businesses related thereto such as the conduct, operation and maintenance of shopping center spaces for rent, amusement centers, or cinema theaters within the compound of the shopping centers.

The retail merchandising segment is engaged in the retail/wholesale trading of merchandise, such as dry goods, wearing apparels, food and other merchandise.

The real estate development and tourism segment is involved in the development and transformation of major residential, commercial, entertainment, and tourism districts through sustained capital investments in buildings and infrastructure.

Segment Assets and Liabilities

Segment assets and segment liabilities do not include deferred tax assets and deferred tax liabilities, respectively.

Inter-segment Transactions

Transfer prices between business segments are set on an arm's length basis similar to transactions with related parties. Segment revenue, segment expenses and segment results include transfers between business segments. Such transfers are eliminated in consolidation.

Business Segment Data

	December 31, 2007 (One Year)					
	Shopping Mall Development	Retail Merchandising	Real Estate Development and Tourism	Others	Eliminations	Consolidated
	(In Thousands)					
Revenue	₱15,333,199	₱105,306,419	₱3,200,850	₱7,899,231	(₱9,203,080)	₱122,536,619
Segment results:						
Income before income tax	₱8,911,052	₱7,139,210	₱1,317,740	₱5,895,043	(₱2,681,593)	₱20,581,452
Provision for income tax	(2,625,244)	(1,539,502)	(195,212)	(113,863)	9,613	(4,464,208)
Net income	₱6,285,808	₱5,599,708	₱1,122,528	₱5,781,180	(₱2,671,980)	₱16,117,244
Net income attributable to:						
Equity holders of the Parent	₱5,974,986	₱5,592,210	₱1,122,528	₱5,781,180	(₱6,452,680)	₱12,018,224
Minority interests	310,822	7,498	–	–	3,780,700	4,099,020
Segment assets (excluding deferred tax)	₱67,394,349	₱55,137,914	₱16,606,759	₱100,524,855	(₱6,618,778)	₱233,045,099
Segment liabilities (excluding deferred tax)	₱26,805,687	₱22,375,997	₱6,679,489	₱41,882,551	(₱7,866,143)	₱89,877,581
Net cash flows provided by (used in):						
Operating activities	₱9,807,065	₱4,901,246	(₱1,924,717)	₱33,725	₱1,293,578	₱14,110,897
Investing activities	(3,151,160)	(338,385)	(245,779)	1,967,698	(4,383,763)	(6,151,389)
Financing activities	(11,889,772)	(2,506,098)	1,124,630	(3,040,606)	3,161,968	(13,149,878)
Other information:						
Investments in shares of stock of associates	₱–	₱2,043,482	₱–	₱40,435,467	₱–	₱42,478,949
Equity in net earnings of associates	–	369,976	–	3,086,708	–	3,456,684
Capital expenditures	5,977,412	2,938,199	2,626,842	2,605,950	–	14,148,403
Depreciation and amortization	2,362,952	1,670,771	9,999	249,436	–	4,293,158

	December 31, 2006 (One Year)					
	Shopping Mall Development	Retail Merchandising	Real Estate Development and Tourism	Others	Eliminations	Consolidated
			(In Thousands)			
Revenue	₱13,479,214	₱47,706,249	₱1,322,188	₱5,532,603	₱20,699,141	₱88,739,395
Segment results:						
Income before income tax	₱8,003,138	₱8,412,352	₱563,210	₱3,189,829	(₱1,341,641)	₱18,826,888
Provision for income tax	(2,253,233)	(1,313,674)	(45,744)	(61,144)	88,071	(3,585,724)
Net income	₱5,749,905	₱7,098,678	₱517,466	₱3,128,685	(₱1,253,570)	₱15,241,164
Net income attributable to:						
Equity holders of the Parent	₱5,448,922	₱7,098,678	₱517,466	₱3,128,685	(₱5,621,894)	₱10,571,857
Minority interests	300,983	–	–	–	4,368,324	4,669,307
Segment assets (excluding deferred tax)	₱70,760,000	₱44,758,440	₱18,863,522	₱100,501,424	(₱8,163,886)	₱226,719,500
Segment liabilities (excluding deferred tax)	₱33,442,512	₱19,037,892	₱10,362,657	₱41,353,668	(₱10,642,695)	₱93,554,034
Net cash flows provided by (used in):						
Operating activities	₱7,282,710	₱5,916,739	₱1,619,388	₱13,600,926	(₱17,238,383)	₱11,181,380
Investing activities	(5,227,155)	2,151,252	(5,368,036)	(14,695,470)	23,759,414	620,005
Financing activities	2,331,556	(5,726,207)	4,698,190	1,815,383	(4,683,244)	(1,564,322)
Other information:						
Investments in shares of stock of associates	₱–	₱1,170,082	₱6,989,685	₱38,387,010	₱–	₱46,546,777
Equity in net earnings of associates	–	242,854	112,403	2,403,586	–	2,758,843
Capital expenditures	6,791,388	2,017,460	697,354	838,918	–	10,345,120
Depreciation and amortization	1,855,352	1,222,943	8,550	268,213	–	3,355,058

	December 31, 2005 (Nine Months - see Note 30)					
	Shopping Mall Development	Retail Merchandising	Real Estate Development and Tourism	Others	Eliminations	Consolidated
			(In Thousands)			
Revenue	₱11,491,252	₱43,224,754	₱767,440	₱8,353,631	(₱9,871,303)	₱53,965,774
Segment results:						
Income before income tax	₱6,964,617	₱4,765,873	₱748,723	₱8,501,007	(₱7,289,737)	₱13,690,483
Provision for income tax	(1,714,896)	(615,288)	(19,132)	(19,250)	–	(2,368,566)
Net income	₱5,249,721	₱4,150,585	₱729,591	₱8,481,757	(₱7,289,737)	₱11,321,917
Net income attributable to:						
Equity holders	₱4,972,906	₱4,084,540	₱722,781	₱8,481,757	(₱10,232,743)	₱8,029,241
Minority interests	276,815	66,045	6,810	–	2,943,006	3,292,676
Segment assets (excluding deferred tax)	₱59,321,168	₱41,006,188	₱12,465,527	₱115,618,699	(₱58,700,151)	₱169,711,431
Segment liabilities (excluding deferred tax)	₱25,589,541	₱13,214,407	₱4,627,184	₱33,829,737	(₱9,708,807)	₱67,552,062
Net cash flows provided by (used in):						
Operating activities	₱6,273,848	₱3,466,439	₱1,572,598	(₱2,741,598)	₱1,555,362	₱10,126,649
Investing activities	(10,728,283)	562,787	(2,658,948)	(12,948,288)	(1,843,619)	(27,616,351)
Financing activities	(1,882,045)	(2,809,464)	373,820	(7,095,304)	4,286,250	(7,126,743)
Other information:						
Investments in shares of stock of associates	₱–	₱936,757	₱20,491	₱27,784,696	₱–	₱28,741,944
Equity in net earnings of associates	–	230,672	685	1,847,911	–	2,079,268
Capital expenditures	10,403,059	853,795	1,492,528	170,844	–	12,920,226
Depreciation and amortization	1,519,580	616,953	7,891	138,600	–	2,283,024

7. Cash and Cash Equivalents

This account consists of:

	2007	2006
Cash on hand and in banks (see Note 21)	₱4,223,347,681	₱4,575,992,141
Temporary investments (see Notes 17, 19 and 21)	11,351,623,752	16,461,500,573
	₱15,574,971,433	₱21,037,492,714

Cash in banks earn interest at the respective bank deposit rates. Temporary investments are made for varying periods of up to three months depending on the immediate cash requirements of the Group, and earn interest at the respective temporary investment rates.

8. Time Deposits and Short-term Investments

This account consists of:

	2007	2006
Time deposits:		
Pledged (see Note 19)	₱7,804,208,398	₱6,815,170,000
Not pledged	451,791,602	1,010,018,000
	8,256,000,000	7,825,188,000
Short-term investments	2,250,000	–
	8,258,250,000	7,825,188,000
Less current portion	4,130,250,000	7,825,188,000
Noncurrent portion	₱4,128,000,000	₱–

Time deposits as of December 31, 2007 amounting to US$200.0 million (₱8,256.0 million) bear annual interest ranging from 5.0% to 5.3%. The current portion of the time deposits, which amounted to US$100.0 million (₱4,128.0 million), will mature in October 2008 while the noncurrent portion, which also amounted to US$100.0 million (₱4,128.0 million), is due in October 2010.

Time deposits as of December 31, 2006 amounting to US$159.6 million (₱7,825.2 million), which bear annual interest of 7.1%, matured in October 2007.

A portion of the time deposits amounting to US$189.1 million (₱7,804.2 million) and US$139.0 million (₱6,815.2 million) as of December 31, 2007 and 2006, respectively, was used as collateral for a loan obtained by SMIC (see Note 19).

9. Investments Held for Trading and Sale

This account consists of:

	2007	2006
Investments held for trading:		
Shares of stock	₱2,506,275,272	₱1,980,684,348
Bonds (see Note 28)	442,776,480	7,401,164,280
	2,949,051,752	9,381,848,628
Available-for-sale investments (see Note 11):		
Shares of stock	29,722,878,541	7,316,933,931
Bonds	453,779,780	260,951,500
	30,176,658,321	7,577,885,431
	₱33,125,710,073	₱16,959,734,059

The Group recognized ₱566.7 million, ₱529.0 million and ₱418.7 million unrealized gain from fair value adjustments of investments held for trading as of December 31, 2007, 2006 and 2005, respectively. Gain on sale of investments held for trading amounted to ₱35.8 million, ₱283.6 million and ₱156.0 million for the periods ended December 31, 2007, 2006 and 2005, respectively. The amounts are included under "Gain on sale of available-for-sale investments and fair value changes on investments held for trading and derivatives" account in the consolidated statements of income.

10. Receivables

This account consists of:

	2007	2006
Trade:		
Tenants (see Note 21)	₱2,067,882,499	₱1,785,547,343
Banks, credit cards and others	1,981,882,633	1,464,893,956
Real estate buyers	1,683,041,800	486,097,720
Due from related parties (see Note 21)	6,526,144,634	1,610,359,078
Management fees (see Note 21)	450,505,721	201,733,010
Accrued interest (see Note 21)	268,418,253	662,437,737
Dividends	118,924,269	–
Others	1,951,428,932	1,085,939,682
	15,048,228,741	7,297,008,526
Less allowance for doubtful accounts	11,796,185	9,194,052
	15,036,432,556	7,287,814,474
Less noncurrent portion of receivables from real estate buyers (see Note 16)	877,590,159	–
Current portion	₱14,158,842,397	₱7,287,814,474

The terms and conditions of the above receivables are as follows:

- Trade receivables from tenants, banks, credit cards and others and management fee receivables are noninterest-bearing and normally collectible on a 30 to 90 days' term. Receivables from real estate buyers mainly consist of receivables subject to financing from banks and other financial institutions.
- The terms and conditions relating to related party receivables are further discussed in Note 21.
- Accrued interest relates mostly to short-term time deposits that will mature within the next financial year. Interests on time deposits are collected at respective maturity dates.
- Other receivables are normally collectible within the next financial year.

The aging analysis of receivables as of December 31, 2007 is as follows:

	Neither past due	Past due but not impaired				
	nor impaired	31-90 days	91-120 days	Over 120 days	Impaired	Total
Trade:						
Tenants	₱1,751,463,622	₱298,298,590	₱–	₱9,194,052	₱8,926,235	₱2,067,882,499
Banks, credit cards and others	1,981,882,633	–	–	–	–	1,981,882,633
Real estate buyers:						
Current	1,344,991,987	42,785,868	15,877,347	94,071,236	–	1,497,726,438
Noncurrent	1,900,140,225	–	–	–	–	1,900,140,225
Due from related parties	6,526,144,634	–	–	–	–	6,526,144,634
Management fees	450,505,721	–	–	–	–	450,505,721
Accrued interest	268,418,253	–	–	–	–	268,418,253
Dividends	118,924,269	–	–	–	–	118,924,269
Others	1,948,558,982	–	–	–	2,869,950	1,951,428,932
	₱16,291,030,326	₱341,084,458	₱15,877,347	₱103,265,288	₱11,796,185	16,763,053,604
Less unrecognized portion of trade receivable from real estate buyers due to percentage of completion method						1,714,824,863
Net receivables before allowance for doubtful accounts						₱15,048,228,741

The movements in allowance for doubtful accounts per classification follow:

	Tenants	Other Receivables	Total
As of January 1, 2007	₱8,926,235	₱267,817	₱9,194,052
Provision for the year	–	2,602,133	2,602,133
As of December 31, 2007	₱8,926,235	₱2,869,950	₱11,796,185

The provision in 2007 resulted from a specific impairment assessment performed by a subsidiary. There was no movement in the allowance for doubtful accounts in 2006.

The receivables, other than those identified as impaired, are assessed by the Group's management as good and collectible.

11. Available-for-Sale Investments

This account consists of investments in:

	2007	2006
Shares of stock:		
Listed	₱32,709,216,717	₱35,347,943,061
Unlisted (net of allowance for probable losses of ₱45,131,638)	304,528,812	435,095,738
Redeemable preferred shares (see Note 21)	2,218,254,419	5,270,194,577
Government bonds	704,897,280	1,046,853,780
Club shares	5,150,000	4,670,000
	35,942,047,228	42,104,757,156
Less current portion (see Note 9)	30,176,658,321	7,577,885,431
Long-term portion	₱5,765,388,907	₱34,526,871,725

Investments in listed shares of stock include investments in SMC amounting to ₱20,021.6 million and ₱22,906.1 million as of December 31, 2007 and 2006, respectively. The investments consist of 339.3 million shares and carried initially at ₱19,852.9 million.

On October 31, 2007, SMIC and San Miguel Corporation Retirement Plan (SMCRP) executed a stock purchase agreement (the Agreement), wherein SMIC agreed to sell through the PSE its 339.3 million SMC common shares (sale shares) to SMCRP at an agreed price, payable on or before October 31, 2008, extendable for additional two (2) months up to December 31, 2008, subject to interest.

Under the terms of the Agreement, all rights to, interests and title in and ownership of the sale shares shall remain with SMIC, provided that upon receipt of the agreed consideration, the voting rights shall be transferred to SMCRP. Also, all dividends and other benefits, except for stock dividends, declared by SMC in relation to the sale shares shall accrue fully to SMIC. All stock dividends declared by SMC in relation to the sale shares shall accrue to SMIC and SMCRP proportionately to the consideration paid by SMCRP.

Should any part of the total consideration remain unpaid as of December 31, 2008, any payments made by SMCRP, including any stock dividends accruing to SMCRP, shall be forfeited in favor of SMIC as liquidated damages for the failure of SMCRP to consummate the contemplated transaction.

The agreement contains an embedded derivative which is further discussed in Note 29.

The account also includes investments of SM Prime in redeemable preferred shares issued by local entities with annual dividend rates of 6.5% to 8.25% in 2007 and 6.5% to 10.46% in 2006 (see Note 21). The preferred shares have preference over the issuer's common shares in the payment of dividends and in the distribution of assets in case of dissolution and liquidation. The shares are mandatorily redeemable in 2009 up to 2011. Preferred shares amounting to ₱1,500.0 million and ₱1,000.0 million, with an annual dividend rate of 10.46%, were early redeemed in July 2007 and August 2007, respectively.

Investments in government bonds were purchased with fixed interest rates ranging from 10.625% to 15.625%. These investments are peso-denominated and will mature on various dates starting April 1, 2008 until September 8, 2010.

The movements in net unrealized gain on AFS investments for the years ended December 31, 2007 and 2006 are as follows:

	2007	2006
Balance at beginning of year	₱11,261,528,843	₱7,038,286,318
Gain (loss) due to changes in fair value of AFS investments	(3,225,093,687)	4,570,178,495
Transferred to income and expenses	(89,665,776)	(987,438,547)
Share in net gain of associates (see Note 12)	5,894,274	640,502,577
Balance at end of year	₱7,952,663,654	₱11,261,528,843

Gain on disposal of AFS investments recognized under "Gain on sale of available-for-sale investments and fair value changes on investments held for trading and derivatives" account in the consolidated statements of income amounted to ₱138.0 million, ₱1,531.0 million and ₱20.5 million for the periods ended December 31, 2007, 2006 and 2005, respectively. The amounts are inclusive of the share of the minority interest.

12. Investments in Shares of Stock of Associates

The details of and movements in this account are as follows:

	2007	2006
Acquisition cost:		
Balance at beginning of year	₱37,175,626,751	₱21,601,741,605
Additions	2,879,051,231	18,485,302,297
Disposals/reclassifications	(10,771,252,248)	(2,911,417,151)
Balance at end of year	29,283,425,734	37,175,626,751
Accumulated equity in net earnings:		
Balance at beginning of year	9,801,150,448	7,140,201,904
Equity in net earnings	3,456,684,195	2,758,843,422
Dividends received	(615,196,406)	(659,705,475)
Accumulated equity in net earnings of investments sold/reclassified	534,975,313	(118,447,968)
Share in unrealized gain on AFS investments of associates - net	17,909,636	680,258,565
Balance at end of year	13,195,523,186	9,801,150,448
	42,478,948,920	46,976,777,199
Allowance for probable losses:		
Balance at beginning of year	430,000,000	–
Additions	–	430,000,000
Reclassification	(430,000,000)	–
Balance at end of year	–	430,000,000
	₱42,478,948,920	₱46,546,777,199

The Group recognized its share in the net gains on AFS investments of the associates amounting to ₱17.9 million, ₱680.3 million and ₱694.1 million, inclusive of the share of the minority interest amounting to ₱12.0 million, ₱39.8 million and ₱52.3 million, respectively, for the periods ended December 31, 2007, 2006 and 2005, respectively. The net unrealized gain was recognized directly as a separate component of the stockholders' equity.

The reclassification of ₱430.0 million provision for probable losses relates to the acquisition of Makro through Rappel (see Note 5).

The major associates of the Group are as follows:

Company	Effective Percentage of Ownership 2007	2006	Principal Activities
MRDC* (see Note 2)	45	–	Real estate and tourism
Sodexho Pass, Inc.*	40	40	Retail merchandising
Banco de Oro Unibank, Inc. (BDO)*	38	33	Financial services
Highlands Prime, Inc. (Highlands Prime)	24	24	Real estate and tourism
China Banking Corporation (China Bank)	20	19	Financial services
Equitable PCI Bank (EPCIB) [a]	–	42	Financial services
APCTC* (see Note 5)	–	37	Education
Rappel (see Note 5)	–	40	Retail merchandising

* *The financial statements of these associates were audited by other independent auditors.*
[a] *Merged with BDO in May 2007.*

In 2005, SMIC acquired 24.03% interest in EPCIB for a total consideration of ₱9,945.8 million. The acquisition enabled SMIC to have a four member representation in the BOD of EPCIB. The fair values of the net assets acquired were finalized in 2006. The comparative information has been restated to reflect the necessary adjustment. Negative goodwill amounting to ₱904.2 million, which was determined based on the excess of SMIC's interest in the underlying fair values of the identifiable assets and liabilities over the cost of acquisition, was accounted for as a negative goodwill and recognized as income for the nine months ended December 31, 2005.

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On August 29, 2006, SMIC and other related companies filed a Tender Offer with the Philippine SEC to acquire up to around 322.3 million shares representing 44.32% of the total outstanding common shares of EPCIB at ₱92 a share. The payment terms of the offer are as follows: 10% on October 2, 2006, 10% on June 2, 2007, 10% on February 2, 2008, and the remaining balance to be paid on October 2, 2008. The negotiated sale of 78.8 million shares representing 10.84% was also consummated with EBC Investments Inc. (EBCII) under the same terms and conditions of the Tender Offer.

The Tender Offer and the negotiated sale generated participation from shareholders with total shares of 377.7 million equivalent to 51.96% of EPCIB's total shares outstanding. The sellers included EBCII with 10.84% shareholdings, Government Service Insurance System (GSIS) with 13.55%, Social Security System (SSS) with 25.84%, and other individual shareholders with 1.73%.

The participation of SSS was conditional on the favorable outcome of its pending case in the Supreme Court. In accordance with the agreement on such conditional sale, the payments corresponding to the shares owned by SSS are placed in an escrow account. The payments due on October 2, 2006 and June 2, 2007 for the 187.8 million shares for SSS totaling to ₱3,456.4 million were deposited in an escrow account, included under "Other noncurrent assets" in the consolidated balance sheets. Under the agreement, the succeeding installments totaling ₱13,825.7 million are payable in 2008 as follows:

Due Date	Amount
February 2008	₱1,728,216,238
October 2008	12,097,513,660
	₱13,825,729,898

In November 2007, the Supreme Court dismissed with finality the legal proceedings because it found the case moot and academic. An entry of judgment of this dismissal order was issued on January 10, 2008. SSS sold its EPCIB shares to a related party of the Group on January 18, 2008, in accordance with the regulations set by Bangko Sentral ng Pilipinas (BSP).

Excluding the SSS shares, SMIC and MRDC purchased on October 2, 2006 a total of 189.9 million shares for a total consideration of ₱17,469.0 million. By virtue of the merger, the promissory notes issued to EBCII amounting to ₱5,800.2 million as of December 31, 2007 were assigned to BDO. The promissory notes were collateralized by a portion of investments available for sale, in compliance with the requirements of BSP.

SMIC and MRDC paid 20% and 10% of the total consideration as of December 31, 2007 and 2006, respectively. The balance, which is recorded at present value, is payable as follows:

Notes Payable	2007	2006
Current portion	₱8,118,761,498	₱1,746,898,971
Long-term portion	–	12,332,385,033
	₱8,118,761,498	₱14,079,284,004

The balance of ₱8,118.8 million as of December 31, 2007 pertains to the amount payable by SMIC only.

The Group's share in the identifiable assets and liabilities of EPCIB as a result of the Tender Offer was finalized in 2007, which resulted to a positive goodwill amounting to ₱5,016.6 million. Positive goodwill is determined based on the excess of the cost of acquisition over SMIC's interest in the underlying fair values of the identifiable assets and liabilities.

In August 2006, SMIC purchased 60 million shares of BDO at ₱32 a share for a total consideration of ₱1,920.0 million payable in four equal installments which matured on August 31, 2007. The Parent Company's share in the identifiable assets and liabilities of BDO was finalized in 2007, which resulted to a positive goodwill amounting to ₱1,504.0 million. Positive goodwill is determined based on the excess of the cost of acquisition over SMIC's interest in the underlying fair values of the identifiable assets and liabilities.

On April 20, 2007 and May 27, 2007, the BSP and Philippine SEC, respectively, approved the merger of BDO and EPCIB, with BDO as the surviving entity. The merger, which took effect on May 31, 2007, was effected through a swap whereby BDO issued 1.8 of its shares for every EPCIB share. The Plan of Merger was approved by the shareholders of BDO and EPCIB in separate meetings on December 27, 2006.

In January 2006, SMIC and other affiliates entered into a Memorandum of Agreement with BDO wherein the latter purchased the investments in BDO Card.

On January 25, 2006, February 14, 2006 and May 15, 2006, Primebridge offered and sold 9,399,700 global depositary receipts (GDRs), each representing 20 shares of BDO's common stock with a par value of ₱10 a share. The proceeds from the issuance of the 9,399,700 GDRs amounted to US$120,012,035.

The GDRs constitute an offering in the United States only to qualified institutional buyers under Rule 144A of the U.S. Securities Act of 1993 (the "Securities Act") and an offering outside the United States under Regulation S of the Securities Act. The average offered price for each GDR is US$12.77. As part of the offering, Primebridge shall, while remaining as the registered holder of BDO shares underlying the GDRs, transfer all rights and interests in BDO shares underlying the GDRs to the depository, and the holders of the GDRs are entitled to receive dividends paid on the shares. However, GDR holders will have no voting rights or other direct rights of a shareholder with respect to BDO shares under the GDRs.

The detailed carrying values of the Group's investments in associates as of December 31 are as follows:

	2007	2006
BDO	₱34,944,448,736	₱9,822,156,685
China Bank	5,561,275,204	5,180,773,936
Highlands Prime	1,546,991,837	1,516,156,435
MRDC (see Note 2)	426,233,143	–
EPCIB	–	29,415,666,796
Makro (see Note 5)	–	612,023,347
	₱42,478,948,920	₱46,546,777,199

The condensed financial information of significant associates are shown below:

	2007	2006
		(In Thousands)
BDO:		
Total resources	₱617,421,476	₱304,473,488
Total liabilities	556,880,848	280,044,704
Interest income	37,603,306	19,299,367
Interest expense	16,166,574	10,965,047
Net income	6,570,330	3,128,294
China Bank:		
Total resources	174,380,262	156,244,479
Total liabilities	150,121,395	131,262,185
Interest income	11,075,373	11,188,586
Interest expense	4,824,245	5,069,007
Net income	3,681,858	3,529,577
Highlands Prime:		
Total current assets	1,592,103	1,330,559
Total noncurrent assets	1,984,072	2,013,855
Total current liabilities	408,524	294,969
Revenue from real estate sales	715,117	345,462
Cost of real estate sold	427,248	213,195
Net income	124,881	85,275
MRDC:		
Total current assets	38,775	–
Total noncurrent assets	9,729,843	–
Total noncurrent liabilities	10,100,970	–
Dividend income	96,505	–
Net loss	386,283	–
EPCIB:		
Total resources	–	345,142,515
Total liabilities	–	297,661,203
Interest income	–	19,639,118
Interest expense	–	8,676,323
Net income	–	3,265,184
Makro:		
Total current assets	–	2,073,867
Total noncurrent assets	–	4,964,556
Total current liabilities	–	3,547,694
Net sales	–	11,499,459
Cost of sales	–	10,370,794
Net loss	–	468,153

As of December 31, the fair values of investments in associates which are listed in the PSE are as follows:

	2007	2006
BDO	₱54,944,756,477	₱14,805,620,214
China Bank	10,819,560,840	8,885,984,320
Highlands Prime	1,507,661,520	1,346,126,358
EPCIB	–	32,316,618,135

13. Property and Equipment

The movements in this account follow:

	Land	Buildings, Condominium Units and Improvements	Store Equipment and Improvements	Data Processing Equipment
Cost				
Balance at December 31, 2005	₱9,830,554	₱1,015,177,966	₱2,342,122,542	₱1,271,406,743
Additions	–	109,587,751	327,728,426	296,228,040
Acquired business - SVI/SSMI	–	426,165,226	74,142,027	1,217,294,769
Reclassifications	(5,288,213)	(263,082,996)	249,448,671	(272,720,207)
Disposals/retirements	–	(26,587,166)	(10,873,174)	(7,484,659)
Balance at December 31, 2006	4,542,341	1,261,260,781	2,982,568,492	2,504,724,686
Additions	–	30,973,014	278,902,434	486,830,103
Acquired business - Rappel/APCTC	2,198,974,825	2,691,515,204	1,401,155,314	–
Reclassifications	–	(20,226,539)	(74,142,027)	13,296,657
Disposed business - MRDC	–	–	–	–
Disposals/retirements	–	–	(789,765)	(59,179,790)
Balance at December 31, 2007	₱2,203,517,166	₱3,963,522,460	₱4,587,694,448	₱2,945,671,656
Accumulated Depreciation and Amortization				
Balance at December 31, 2005	₱–	₱352,035,238	₱1,037,598,743	₱870,114,513
Additions	–	99,503,644	321,657,729	234,921,826
Acquired business - SVI/SSMI	–	40,774,674	71,262,048	664,948,771
Reclassifications	50	(97,718,297)	–	(9,318,542)
Disposals/retirements	–	(4,302,385)	(8,982,279)	(2,482,171)
Balance at December 31, 2006	50	390,292,874	1,421,536,241	1,758,184,397
Additions	–	132,516,920	528,782,021	290,624,280
Acquired business - Rappel/APCTC	–	968,649,556	1,023,700,573	–
Reclassifications	–	–	(71,546,075)	(5,863,973)
Disposed business - MRDC	–	–	–	–
Disposals/retirements	–	(8,641)	(545,906)	(59,778,716)
Balance at December 31, 2007	₱50	₱1,491,450,709	₱2,901,926,854	₱1,983,165,988
Net Book Value				
As of December 31, 2007	₱2,203,517,116	₱2,472,071,751	₱1,685,767,594	₱962,505,668
As of December 31, 2006	₱4,542,291	₱870,967,907	₱1,561,032,251	₱746,540,289

Furniture, Fixtures and Office Equipment	Machinery and Equipment	Leasehold Improvements	Transportation Equipment	Construction in Progress	Total
₱389,333,325	₱231,135,913	₱568,280,132	₱265,064,551	₱13,601,859,914	₱19,694,211,640
168,481,794	144,362,613	140,663,659	310,791,505	7,948,910,819	9,446,754,607
596,013,582	1,159,520,457	780,893,163	90,246,580	9,353,165	4,353,628,969
22,729,111	67,524,607	44,289,761	(3,062,208)	(14,670,035,311)	(14,830,196,785)
(2,893,301)	(78,633,699)	(5,238)	(134,584,822)	–	(261,062,059)
1,173,664,511	1,523,909,891	1,534,121,477	528,455,606	6,890,088,587	18,403,336,372
160,989,474	69,651,090	351,859,995	10,914,085	7,490,084,025	8,880,204,220
105,242,312	219,795,810	–	12,005,994	–	6,628,689,459
–	–	110,168,515	–	(5,593,073,508)	(5,563,976,902)
(2,221,936)	(1,493,306)	–	(759,717)	–	(4,474,959)
(1,212,087)	(1,968,242)	(430,808)	(4,881,818)	–	(68,462,510)
₱1,436,462,274	₱1,809,895,243	₱1,995,719,179	₱545,734,150	₱8,787,099,104	₱28,275,315,680
₱212,910,924	₱141,099,619	₱268,270,291	₱209,295,768	₱–	₱3,091,325,096
113,624,134	169,042,532	132,867,386	17,056,599	–	1,088,673,850
206,300,672	836,927,092	313,405,280	77,684,201	–	2,211,302,738
–	–	–	82,243	–	(106,954,546)
(1,300,724)	(30,288,442)	–	(134,584,822)	–	(181,940,823)
531,535,006	1,116,780,801	714,542,957	169,533,989	–	6,102,406,315
176,244,145	65,195,601	381,892,528	74,513,787	–	1,649,769,282
79,732,118	196,057,975	–	5,606,995	–	2,273,747,217
718,460	(19,118)	(258,027)	128,831	–	(76,839,902)
(2,202,337)	(1,210,036)	–	(759,717)	–	(4,172,090)
(365,322)	(1,432,236)	(414,834)	(4,881,818)	–	(67,427,473)
₱785,662,070	₱1,375,372,987	₱1,095,762,624	₱244,142,067	₱–	₱9,877,483,349
₱650,800,204	₱434,522,256	₱899,956,555	₱301,592,083	₱8,787,099,104	₱18,397,832,331
₱642,129,505	₱407,129,090	₱819,578,520	₱358,921,617	₱6,890,088,587	₱12,300,930,057

The construction in progress account includes shopping mall complex under construction of SM Prime. In 2007, shopping mall complex under construction mainly pertains to costs incurred for the development of SM City Marikina and SM North Edsa Expansion. In 2006, shopping mall complex under construction mainly pertains to costs incurred for the development SM City Bacolod, SM City Cebu Expansion, SM City Marikina, SM City Taytay and SM City Supercenter Muntinlupa.

Construction contracts with various contractors related to the construction of the above-mentioned projects amounted to ₱3,048 million and ₱3,812 million as of December 31, 2007 and 2006, respectively, inclusive of overhead, cost of labor and materials and all other costs necessary for the proper execution of the works. The outstanding contracts as of December 31, 2007 and 2006 are valued at ₱1,303 million and ₱1,979 million, respectively.

Interest capitalized to shopping mall under construction amounted to ₱1,131 million and ₱1,285.4 million in 2007 and 2006, respectively. Capitalization rates used were 9.01% in 2007 and 10.04% in 2006.

14. Investment Properties

The movements in this account follow:

	Land	Buildings and Improvements	Building Equipment, Furniture and Others	Total
Cost				
Balance at December 31, 2005	₱14,167,753,012	₱32,077,120,824	₱6,730,360,666	₱52,975,234,502
Additions	336,061,338	2,244,921	–	338,306,259
Reclassifications	546,356,134	13,421,293,550	2,309,464,268	16,277,113,952
Disposals	(296,997,390)	(1,273,871)	–	(298,271,261)
Balance at December 31, 2006	14,753,173,094	45,499,385,424	9,039,824,934	69,292,383,452
Additions	1,192,934,885	1,014,470,114	1,006,191,830	3,213,596,829
Reclassifications	505,120,444	5,540,105,351	576,112,235	6,621,338,030
Disposed business - MRDC	(26,094,840)	(7,206,051)	–	(33,300,891)
Disposals	(37,564,024)	–	–	(37,564,024)
Balance at December 31, 2007	16,387,569,559	52,046,754,838	10,622,128,999	79,056,453,396
Accumulated Depreciation, Amortization and Impairment Losses				
Balance at December 31, 2005	600,000,000	6,371,506,102	3,252,095,909	10,223,602,011
Impairment loss	351,995,000	–	–	351,995,000
Additions	–	1,416,559,120	758,844,659	2,175,403,779
Reclassifications	–	119,774,382	–	119,774,382
Balance at December 31, 2006	951,995,000	7,907,839,604	4,010,940,568	12,870,775,172
Additions	–	1,723,625,516	699,570,054	2,423,195,570
Reclassifications	–	(508,858)	508,858	–
Disposed business - MRDC	–	(5,495,002)	–	(5,495,002)
Balance at December 31, 2007	951,995,000	9,625,461,260	4,711,019,480	15,288,475,740
Net Book Value				
As of December 31, 2007	**₱15,435,574,559**	**₱42,421,293,578**	**₱5,911,109,519**	**₱63,767,977,656**
As of December 31, 2006	₱13,801,178,094	₱37,591,545,820	₱5,028,884,366	₱56,421,608,280

The impairment test conducted in 2006 for certain properties of the Group resulted in the recording of impairment charges of ₱352.0 million. Impairment reviews carried out in 2007 showed that no impairment charge is required.

If the investment properties were measured using the fair value model, the carrying amounts as of December 31 would be as follows:

	2007	2006
Land	₱137,808,262,300	₱109,533,208,853
Buildings and improvements	95,730,379,506	50,181,286,371
Building equipment, furniture and others	13,944,515,000	10,143,961,109
	₱247,483,156,806	₱169,858,456,333

The fair values were determined by independent appraisers based on appraisal reports made on various dates. The fair value represents the amount at which the assets can be exchanged between a knowledgeable, willing seller and a knowledgeable, willing buyer in an arm's length transaction at the date of valuation in accordance with International Valuation Standards.

Rent income from investment properties, which is primarily attributable to SM Prime, amounted to ₱11,088.7 million, ₱9,804.3 million and ₱8,323.5 million for the periods ended December 31, 2007, 2006 and 2005, respectively.

15. Land and Development and Condominium Units for Sale

Land and development, which amounted to ₱3,891.0 million as of December 31, 2007 and ₱1,836.4 million as of December 31, 2006, include land and cost of the condominium projects.

On February 24, 2006, SMDC entered into a joint venture agreement (JVA) with BDO to develop certain properties of BDO located in Quezon City into the "Mezza Residences" (Mezza Project), a residential/commercial condominium project. Under the agreement, SMDC and BDO agreed to share the net saleable area of the Mezza Project on an agreed sharing percentage, among others. As of December 31, 2006, the payable to BDO arising from the sales of condominium units under this agreement amounted to ₱26.0 million.

In October 2006, SMDC started the construction of the Mezza Project. As of December 31, 2007 and 2006, it has a market take up of 74.6%, valued at ₱3,073.2 million, and 4.9%, valued at ₱260.7 million, respectively. Total estimated cost to complete the Mezza project amounted to ₱1,772.0 million as of December 31, 2007.

On August 2, 2007, the BOD of SMDC authorized the negotiation with BDO for the purchase of BDO's rights and interests in the JVA. On August 28, 2007, SMDC confirmed its interest in purchasing BDO's rights and interests and BDO has agreed to the terms and agreements on which the sale shall commence. As of December 31, 2007, SMDC has made 4 monthly non-withdrawable deposits in an escrow account totalling ₱369.7 million. The sale of BDO's right and interests was finalized on February 15, 2008.

In 2003, SMDC commenced the construction of its condominium project - the "Chateau Elysee". The "Chateau Elysee" is a French Mediterranean-inspired condoville in Parañaque City composed of six clusters. Cluster one of the project broke ground on September 29, 2003, with market take-up of 99% and 96%, valued at ₱379.9 million and ₱364.4 million as of December 31, 2007 and 2006, respectively. Construction of Cluster two started in 2005, with market take-up of 91% and 73%, valued at ₱468.2 million and ₱370.4 million as of December 31, 2007 and 2006, respectively. Construction of Cluster three started in 2006, with market take-up of 90% and 23%, valued at ₱556.3 million and ₱155.1 million as of December 31, 2007 and 2006, respectively. Construction of Clusters one, two and three were already completed as of December 31, 2007. Construction of Cluster six started in 2007, with market take-up of 20%, valued at ₱156.8 million as of December 31, 2007. Total estimated cost to complete Cluster six amounted to ₱376.9 million as of December 31, 2007.

Condominium units for sale amounted to ₱86.4 million and ₱90.0 million as of December 31, 2007 and 2006, respectively. The amounts were included under "Input taxes and other current assets" account in the consolidated balance sheets.

On June 30, 2004, SMDC entered into a JVA with GSIS for the development of a residential condominium project (the Project) on a parcel of land (the Property) owned by GSIS. Under the JVA, GSIS shall contribute all its rights, title and interest in and to the Property in consideration of its receipt of allocated units, which is 15% of the value of the total saleable units in the Project, in return for its contribution. In turn, SMDC shall provide financing for the implementation of the Project in consideration of its receipt of 85% of the value of the total saleable units in the Project, in return for its contribution.

On July 14, 2005, SMDC submitted to GSIS a Letter of Intent to change the Property subject for development. On September 7, 2005, the GSIS Board of Trustees approved the proposal of SMDC to change the Property subject for development. Under the amended JVA agreement, the Property will now be 14,430 square meters, more or less, a portion of the Tree Park Area of the GSIS-Baguio Convention Center.

Under the amended JVA, in the event of a decrease in the investment commitment not below the amount of ₱1,100.0 million, there will be no adjustment in the sharing or allocation percentage of both parties as agreed upon based on the original JVA. In case the reduction goes lower than ₱1,100.0 million, there shall be a corresponding adjustment in the sharing or allocation percentage of both parties, which shall be subject to the agreement of both parties.

As of December 31, 2007, the development of the Project has not yet started.

16. Intangibles and Other Noncurrent Assets

These accounts consist of:

	2007	2006
Intangibles:		
Trademarks and brand names (see Note 5)	₱6,124,762,000	₱6,124,762,000
Goodwill	5,669,888,329	5,115,418,011
	₱11,794,650,329	₱11,240,180,011
Other noncurrent assets:		
Escrow fund (see Note 12)	₱3,524,743,951	₱1,778,216,237
Deferred tax assets (see Note 26)	1,439,338,317	353,764,486
Deposits and advance rentals	1,402,596,267	1,135,098,321
Receivables from real estate buyers (see Note 10)	877,590,159	–
Derivative assets (see Note 29)	347,248,200	918,945,584
Defined benefit asset (see Note 25)	45,829,870	111,123,090
Others	926,598,854	323,823,908
	₱8,563,945,618	₱4,620,971,626

Trademarks and brand names acquired in a business combination in 2006 were assessed to have an indefinite useful life. The Relief-from-Royalty method was used in determining the recoverable amount of trademarks and brand names for impairment testing. The royalty rate used was 3.5%, which is the prevailing royalty rate in the retail assorted category where SVI and SSMI fall. As of December 31, 2007 and 2006, no impairment loss was identified.

The movements in goodwill are as follows:

	2007	2006
Cost		
Balance at beginning of year	₱5,207,037,613	₱255,743,567
Additions (see Notes 2 and 5)	554,470,318	4,951,294,046
Balance at end of year	5,761,507,931	5,207,037,613
Accumulated Impairment Losses		
Balance at beginning of year	91,619,602	–
Provision	–	91,619,602
Balance at end of year	91,619,602	91,619,602
Net Book Value	₱5,669,888,329	₱5,115,418,011

The recoverable amount of goodwill has been determined using the cash flow projections based on the financial budgets approved by senior management covering a 5-year period. The pre-tax discount rates applied to cash flow projections ranged from 13.34% to 14.84%. The discount rates were determined based on the yield of a 20-year government bonds at the beginning of the forecasted year. The discount rates also imputes the risk of the cash-generating units compared to the respective risk of the overall market, and equity risk premium. Management assessed the impairment loss in the value of goodwill to be none in 2007 and ₱91.6 million in 2006.

Deposits and advance rentals pertain substantially to the lease agreements entered into by SM Prime for certain parcels of land where some of its malls are constructed. The lease agreements provide that the security deposits will be applied to future rentals. Consequently, the said deposits and advance rentals are not remeasured at amortized cost.

"Others" account pertains mostly to advances for project developments of SMDC.

17. Bank Loans

This account consists of:

	2007	2006
Parent Company:		
U.S. dollar-denominated loans	₱–	₱3,473,775,500
Peso-denominated loans	–	1,500,000,000
Subsidiaries:		
U.S. dollar-denominated loans	190,920,000	5,787,991,500
Peso-denominated loans	2,846,640,267	2,557,809,097
	₱3,037,560,267	₱13,319,576,097

The US dollar-denominated loans amounting to US$4.6 million (₱190.9 million) as of December 31, 2007 and US$188.9 million (₱9,261.8 million) as of December 31, 2006 bear annual interest rates ranging from 4.90% to 5.45% and 5.45% to 6.1% in 2007 and 2006, respectively. The peso-denominated loans bear annual interest rates ranging from 5.00% to 6.50% and 5.35% to 7.40% in 2007 and 2006, respectively.

A portion of these loans is collateralized by temporary investments and property and equipment in accordance with the regulations of the BSP. The carrying values of the collaterals approximate the amounts of the loans.

18. Accounts Payable and Other Current Liabilities

This account consists of:

	2007	2006
Trade	₱15,255,407,160	₱10,662,259,415
Accrued expenses and others (see Note 21)	5,494,005,160	2,409,545,510
Due to related parties (see Note 21)	1,955,988,741	1,504,052,187
Nontrade	1,519,515,807	1,810,492,573
Accrued interest (see Note 21)	553,893,696	698,297,290
Gift checks redeemable	224,975,829	195,674,143
Payable to Cambridge	–	960,000,000
	₱25,003,786,393	₱18,240,321,118

The terms and conditions of the above financial liabilities are as follows:

- Trade payables are noninterest-bearing and are normally settled on a 30 to 60 days' term.
- Accrued expenses pertain to accrued and unpaid selling, general and administrative expenses which are normally settled within the next financial year.
- Accrued interest pertains to unpaid interest on bank loans and long-term debt which are normally settled quarterly or semi-annually.
- Nontrade payables are expected to be settled within the next financial year.
- Gift checks are redeemable at face value.
- Payable to Cambridge represents the unpaid purchase price of BDO shares acquired by SMIC in August 2006. The amount matured on August 31, 2007.
- The terms and conditions relating to related party payables are further discussed in Note 21.

19. Long-term Debt

This account consists of:

	2007			2006		
	Gross Amount	Debt Issue Cost	Net Amount	Gross Amount	Debt Issue Cost	Net Amount
Parent Company:						
U.S. dollar-denominated:						
Convertible Bonds	₱11,260,034,544	(₱123,414,962)	₱11,136,619,582	₱–	₱–	₱–
Five-year notes	-	-	-	10,885,542,540	(63,156,258)	10,822,386,282
Peso-denominated:						
Bank loans collateralized with time deposits	6,000,000,000	(28,934,582)	5,971,065,418	5,980,000,000	–	5,980,000,000
Preferred shares	3,500,000,000	(19,550,618)	3,480,449,382	–	–	–
Other bank loans	6,500,000,000	(27,425,829)	6,472,574,171	5,990,000,000	(37,226,120)	5,952,773,880
Subsidiaries:						
U.S. dollar-denominated -						
Five-year syndicated loan	6,192,000,000	(88,026,478)	6,103,973,522	7,354,500,000	(107,134,794)	7,247,365,206
Peso-denominated:						
Five-year floating rate notes	4,000,000,000	(29,494,201)	3,970,505,799	–	–	–
Five-year bilateral loans	3,250,000,000	(20,982,666)	3,229,017,334	3,000,000,000	(24,678,808)	2,975,321,192
Five-year syndicated loans	1,125,000,000	(10,233,100)	1,114,766,900	1,950,000,000	(17,559,221)	1,932,440,779
Five-year and seven-year fixed rate notes	-	-	-	3,000,000,000	(27,457,346)	2,972,542,654
Other bank loans	2,200,000,000	(13,092,500)	2,186,907,500	2,734,000,000	(16,772,500)	2,717,227,500
	44,027,034,544	(361,154,936)	43,665,879,608	40,894,042,540	(293,985,047)	40,600,057,493
Less current portion	840,625,000	(7,274,048)	833,350,952	17,700,542,540	(71,142,418)	17,629,400,122
Noncurrent portion	₱43,186,409,544	(₱353,880,888)	₱42,832,528,656	₱23,193,500,000	(₱222,842,629)	₱22,970,657,371

Parent Company

Convertible Bonds
The US$300.0 million (financial liability component amounted to ₱11,260.0 million) Convertible Bonds (the Bonds) were issued on March 19, 2007 and will mature on March 20, 2012. The Bonds carry a zero coupon with a yield to maturity of 3.5%.

The Bonds are convertible, at the option of the holders, into SMIC's common shares at any time, on or after June 30, 2007 until the close of business on March 13, 2012, unless previously redeemed, converted, or purchased and cancelled. Conversion price is the equivalent of ₱453.39 a share, after giving effect to the 4.27% stock dividend declared on April 25, 2007 (see Note 20). On March 19, 2010, the bondholders may avail of the early redemption option at the fixed price of 110.97%. The Bonds will be redeemed upon maturity at 118.96% of the principal amount.

The bonds contain embedded derivatives which are further discussed in Note 29.

Five-Year Notes
The US$300.0 million (₱16,775.7 million) notes were issued on October 15, 2002 and matured on October 16, 2007. The interest on the notes was payable semi-annually in arrears at a fixed rate of 8.00% annually.

Bank Loans Collateralized with Time Deposits
On October 16, 2007, SMIC obtained a five-year term loan amounting to ₱6,000.0 million, which bears interest at the three-month Philippine Dealing System Treasury - Fixing (PDST-F) rate plus a margin of 0.375% per annum, payable quarterly in arrears. The loan is collateralized by SMIC's time deposits amounting to US$189.1 million (₱7,804.2 million) (see Note 8) and several parcels of land included under, "Investment properties" account.

The peso-denominated loans as of December 31, 2006 amounting to ₱5,980.0 million bear annual interest ranging from 7.11% to 12.07% per annum. The loans were collateralized by SMIC's time deposits amounting US$139.0 million (₱6,815.2 million) (see Note 8). The entire loans matured in October 2007.

Preferred Shares
On August 6, 2007 and November 6, 2007, SMIC issued Series 1 and Series 2 of nonconvertible, non-participating, non-voting preferred shares amounting to ₱3,300.0 million and ₱200.0 million, respectively. Each share has a par value of ₱10 a share and an offer price of ₱10,000 a share.

The Series 1 preferred shares carry a fixed dividend rate of 7.5% per annum, payable semi-annually in arrears, while the Series 2 preferred shares carry a dividend rate based on 3-month PDST-F rate plus a margin of 75 basis points (bps). The dividend rights are cumulative. The preferred shares rank ahead of the common shares in the event of liquidation.

The preferred shares are redeemable on August 6, 2012 at redemption price, which consists of (1) 100% of the offer price; (2) all unpaid cash dividends accruing thereon, if any, and/or in the event no cash dividends are declared for the relevant period, an amount equivalent to the sum of the cash dividends on the preferred shares had dividends been declared and paid for the relevant period; and (3) any charges on unpaid amounts due then outstanding. SMIC has an option to early redeem the preferred shares subject to certain conditions.

Other Peso Bank Loans

This account includes the following:

	2007	2006
Seven-year term loans	₱5,000,000,000	₱–
Five-year term loan	1,000,000,000	1,000,000,000
Series “A” Floating rate notes	500,000,000	500,000,000
Series “B” Fixed rate notes	–	4,000,000,000
Series “C” Fixed rate notes	–	490,000,000
	₱6,500,000,000	₱5,990,000,000

In October 2007, SMIC obtained two seven-year term loans at a principal amount of ₱2,000.0 million each, wherein one bears a fixed interest of 6.90% and the other bears a floating interest based on three-month PDST-F plus a margin of 0.125% per annum. On November 23, 2007, SMIC also availed another seven-year term loan amounting to ₱1,000.0 million, which bears a fixed interest of 6.91% annually, payable quarterly.

On October 11, 2006 and November 8, 2006, SMIC obtained five-year term loans amounting to ₱600.0 million and ₱400.0 million, respectively, which bear fixed interest rate of 7.59% and 6.65%, respectively.

The five-year Series A and B notes bear interest at the three-month Treasury Bill rate plus a spread of 1.00% per annum, payable quarterly in arrears, and 9.95% per annum, payable semi-annually in arrears, respectively, and have a maturity date of October 28, 2010. The seven-year Series C notes bear interest at 10.39% per annum, payable semi-annually in arrears. The Series C notes are also subject to the periodic payment of amortization starting October 28, 2006 up to October 28, 2012. On October 30, 2007, Series B and C notes were prepaid by SMIC.

Subsidiaries

US dollar-denominated Five-Year Syndicated Loan

The US$150.0 million (₱6,192.0 million) unsecured loan was obtained by SM Prime on October 18, 2004 and will mature on October 18, 2009. The loan is a five-year bullet term loan which carries interest rate based on London Inter-Bank Offered Rate (LIBOR) plus a certain percentage. On May 18, 2007, the original facility agreement was amended which effectively reduced the interest rate by 1% (see Note 29).

Philippine Peso-denominated Five-Year Floating Rate Notes

This represents a five-year bullet term loan obtained by SM Prime on June 18, 2007 and July 9, 2007 amounting to ₱4,000.0 million and will mature on June 19, 2012. The loan carries an interest rate based on PDST-F plus an agreed margin.

Philippine Peso-denominated Five-Year Bilateral Loans

This consists of a ₱3,000.0 million five-year bullet term loan obtained by SM Prime on June 21, 2006 that will mature on June 21, 2011, and a ₱250 million five-year term loan obtained by two subsidiaries of SM Prime on September 28, 2007 and November 6, 2007 to finance the construction of a project called San Miguel by the Bay. The ₱250.0 million five-year term loan is payable in quarterly installments of ₱15.6 million starting December 2008 up to September 2012. Both loans carry an interest rate based on PDST-F plus an agreed margin.

Philippine Peso-denominated Five-Year Syndicated Loans

This includes a five-year syndicated term loan obtained by SM Prime on November 21, 2003 originally amounting to ₱1,700.0 million, payable in equal quarterly installments of ₱106.0 million starting February 2005 up to November 2008 and bears a fixed interest rate of 8% payable quarterly. Starting April 2007, the fixed interest rate of 8% was reduced to 7.0625%. The outstanding balance of the loan as of December 31, 2007 and 2006 amounted to ₱425.0 million and ₱850.0 million, respectively.

In 2004, Consolidated Prime Dev. Corp. and Premier Southern Corp., both wholly-owned subsidiaries of SM Prime, obtained a five-year term loan originally amounting to ₱1,600.0 million to finance the construction of shopping malls. The five-year term loan is payable in equal quarterly installments of ₱100.0 million starting October 2005 up to July 2009 and bears a fixed interest rate of 9.66% payable quarterly in arrears. Starting April 2007, the fixed interest rate of 9.66% was reduced to 6.75%. The outstanding balance of the loan as of December 31, 2007 and 2006 amounted to ₱700.0 million and ₱1,100.0 million, respectively.

Philippine Peso-denominated Five-Year and Seven-Year Fixed Rate Notes

This represents a five-year and seven-year fixed rate notes obtained by SM Prime on July 8, 2005 amounting to ₱1,500.0 million each. The loans bear fixed interest rates of 10.535% and 11.562%, and will mature on July 8, 2010 and 2012, respectively. The ₱3,000.0 million notes were prepaid in June 2007 (see Note 29).

Other Bank Loans

This account consists of the following:

- Ten-year bullet fixed rate loan obtained on August 16, 2006 amounting to ₱1,200.0 million. The loan carries a fixed interest rate of 9.75% and will mature on August 16, 2016.
- Five-year bullet loan obtained on October 2, 2006 amounting to ₱1,000.0 million and will mature on October 2, 2011. The loan carries an interest rate based on PDST-F plus an agreed margin.
- Two-year and five-year unsecured loans obtained on December 1, 2004 amounting to ₱466.0 million and ₱534.0 million, respectively. The loans bear fixed interest rates of 10.87% and 12.54%, respectively. The ₱466.0 million loan matured on December 1, 2006. The ₱534.0 million loan, with an original maturity date of December 1, 2009, was prepaid on June 1, 2007. The related unamortized cost charged off to profit or loss amounted to ₱1.0 million.

As of December 31, 2007 and 2006, investments held for trading and temporary investments totaling ₱1,388 million and ₱1,761 million are pledged to secure the loans in compliance with the requirements of the BSP. In accordance with the loan agreement, SM Prime has the option to substitute the pledged investments with other assets as collateral, in accordance with the regulations of the BSP (see Note 21).

Debt Issue Cost

The movements in unamortized debt issue costs in 2007 and 2006 are as follows:

	2007	2006
Balance at beginning of year	₱293,985,047	₱384,965,914
Additions	255,427,871	43,830,726
Amortization	(188,257,982)	(134,811,593)
Balance at end of year	₱361,154,936	₱293,985,047

Repayment Schedule

The repayments of long-term debt are scheduled as follows:

	Gross Loan	Debt Issue Cost	Net
2008	₱840,625,000	(₱7,274,048)	₱833,350,952
2009	6,554,500,000	(91,579,280)	6,462,920,720
2010	562,500,000	(3,332,404)	559,167,596
2011	5,062,500,000	(23,307,666)	5,039,192,334
2012	24,806,909,544	(201,750,613)	24,605,158,931
2014	5,000,000,000	(24,568,425)	4,975,431,575
2016	1,200,000,000	(9,342,500)	1,190,657,500
Total	₱44,027,034,544	(₱361,154,936)	₱43,665,879,608

The loan agreements provide certain restrictions and requirements principally with respect to maintenance of required financial ratios and material change in ownership or control. As of December 31, 2007 and 2006, the Group is in compliance with the terms of its loan covenants.

Time deposits amounting to ₱8,256.0 million as of December 31, 2007 are intended to be used for payment of the long-term debt maturing in 2012. Time deposits amounting to ₱6,815.2 million were used to pay long-term debt which matured in 2007 (see Note 8).

20. Stockholders' Equity

Capital Stock

The details of and movements in SMIC's common stock, with a par value of ₱10 a share, are as follows:

	Number of Shares			
	Authorized		Issued and Subscribed	
	2007	2006	2007	2006
Balance at beginning of year	600,000,000	600,000,000	586,000,000	530,000,000
Additions	100,000,000	–	–	–
Reclassification to preferred stock (see Note 19)	(10,000,000)	–	–	–
Stock dividends	–	–	25,023,038	–
Subscriptions (see Note 5)	–	–	–	56,000,000
Balance at end of year	690,000,000	600,000,000	611,023,038	586,000,000

On April 25, 2007, the BOD approved the increase in SMIC's authorized capital stock from ₱6,000.0 million, consisting of 590,000,000 common shares and 10,000,000 non-voting, cumulative and redeemable preferred shares both with a par value of ₱10 a share, to ₱7,000.0 million, consisting of 690,000,000 common shares and 10,000,000 non-voting, cumulative and redeemable preferred shares both with par value of ₱10 a share. On the same day, the stockholders, which represent at least two-thirds of the outstanding capital stock of SMIC, approved via a written assent the amendment of the articles of incorporation to increase the authorized capital stock. The Philippine SEC approved the increase in the authorized capital stock on June 14, 2007.

On December 12, 2006, the BOD approved an amendment to the Articles of Incorporation of SMIC to reclassify 10 million of its unissued shares into preferred shares. On January 16, 2007, the amendment was approved via written assent of the stockholders representing at least two-thirds of the outstanding capital stock of SMIC. The Philippine SEC approved the reclassification of unissued shares on March 5, 2007. The terms of the preferred shares are further discussed in Note 19.

As discussed in Note 5, on June 28, 2006, the PSE approved the listing of 56,000,000 new shares in connection with the share-for-share swap transaction with SVI and SSMI. On November 6, 2006, the Philippine SEC approved the valuation and confirmed that the issuance of the shares is exempt from registration requirements. Pursuant to agreements entered into among SMIC, SVI and SSMI, the 56,000,000 shares were exchanged for 2,000,000 common shares (100%) of SVI and 810,000 common shares (81%) of SSMI at a total swap price of ₱13,104 million. The listing of the shares was completed on November 17, 2006.

On June 27, 2007, the PSE approved the application of SMIC to list additional 30,694,870 common shares to cover the issuance of convertible bonds.

Cost of Common Shares Held by Subsidiaries

Certain subsidiaries hold common shares of the Parent Company. This is presented as "Cost of common shares held by subsidiaries" and is treated as a reduction in equity as shown in the consolidated balance sheets and consolidated statements of changes in stockholders' equity.

The movements are as follows:

	No. of Shares	Cost a Share	Total Cost
Balance as of December 31, 2005	2,000,000	₱250	₱500,000,000
Acquisitions	113,820	303	34,518,502
Disposals	(1,917,220)	250	(479,305,000)
Balance as of December 31, 2006	196,600	281	55,213,502
Acquisitions	5,000	324	1,621,786
Disposal	(114,800)	285	(32,757,300)
Shares held by a deconsolidated subsidiary	(45,899)	292	(13,382,988)
Stock dividends	3,706	–	–
Balance as of December 31, 2007	44,607	240	₱10,695,000

Retained Earnings

On April 25, 2007, the BOD approved the declaration of the following dividends:

a. Cash dividends of 54.1% of the par value or ₱5.41 a share for a total amount of ₱3,170.3 million in favor of stockholders of record as of May 25, 2007. This was paid on June 21, 2007.

b. Stock dividends of 4.27% equivalent to 25,023,038 million common shares to all stockholders as of June 28, 2007. This shall constitute the minimum subscription and paid capital requirement to the increase in the authorized capital stock of ₱1,000.0 million as discussed above.

On April 27, 2006, the BOD approved the declaration of cash dividends of 47% of the par value or ₱4.70 a share for a total amount of ₱2,491.0 million in favor of the stockholders of record as of May 26, 2006. This was paid on June 22, 2006.

The balance of retained earnings includes the accumulated equity in net earnings of subsidiaries and associates amounting to ₱44,157.3 million and ₱36,947.6 million as of December 31, 2007 and 2006, respectively. The amount is not available for dividends distribution until such time that the Parent Company receives the dividends from the respective subsidiaries and associates.

21. Related Party Transactions

Terms and Conditions of Transactions with Related Parties

Transactions with related parties are made at normal market prices. For the periods ended December 31, 2007, 2006 and 2005, the Group did not make any provision for doubtful accounts relating to amounts owed by related parties. An assessment is undertaken at each financial year by examining the financial position of the related party and the market in which the related party operates.

Rent

The Parent Company and a subsidiary have existing lease agreements for office and commercial spaces with related companies. Total rent income amounted to ₱1,734.9 million, ₱1,929.1 million and ₱1,968.5 million for the periods ended December 31, 2007, 2006 and 2005, respectively.

Management Fees

The Group pays management fees to Shopping Center Management Corporation, Leisure Center, Inc., West Avenue Theaters Corporation and Family Entertainment Center, Inc. for the management of the office and mall premises. Total management fees amounted to ₱481.1 million, ₱409.7 million and ₱328.6 million for the periods ended December 31, 2007, 2006 and 2005, respectively.

The Parent Company and a subsidiary also receive management fees from related companies for management and consultancy services. The annual management fees are based on a certain percentage of the related companies' net income as defined in the management contracts. Total management fees earned amounted to ₱266.0 million, ₱290.9 million and ₱268.5 million for the periods ended December 31, 2007, 2006 and 2005, respectively.

Cash Placements and Loans

The Group has certain bank accounts and cash placements that are maintained with BDO and China Bank. Such accounts earn interest based on prevailing market interest rates.

SM Prime has investments in preferred shares of BDO (see Note 11).

The Group also availed of bank loans and long-term debt from BDO and China Bank and pays interest based on prevailing market interest rates (see Notes 17 and 19).

Others

The Group, in the normal course of business, has outstanding receivables from and payables to related companies as of balance sheet date which are unsecured and normally settled in cash.

The consolidated balance sheets include the following amounts resulting from the above transactions with related parties:

	2007	2006
	(In Thousands)	
Cash and cash equivalents (see Note 7)	₱12,737,986	₱17,113,237
Time deposits (see Note 8)	8,256,000	7,825,188
Investments held for trading (see Note 9)	2,506,275	2,480,684
Available-for-sale investments (see Note 11)	5,737,104	7,009,174
Receivables:		
Due from related parties (see Note 10)	6,526,145	2,110,359
Tenants (see Note 10)	1,952,803	1,692,862
Management fees (see Note 10)	450,506	201,733
Accrued interest (see Note 10)	165,432	519,248
Bank loans (see Note 17)	1,353,720	2,141,399
Accounts payable and other current liabilities:		
Due to related parties (see Note 18)	1,955,989	1,504,052
Management fees (see Note 18)	61,547	19,279
Accrued interest (see Note 18)	67,198	181,520
Long-term debt:		
Current portion of long-term debt (see Note 19)	300,000	6,280,000
Long-term debt - net of current portion (see Note 19)	6,500,000	5,824,000

Compensation of Key Management Personnel of the Group

The aggregate compensation and benefits to key management personnel of the Group for the periods ended December 31, 2007, 2006 and 2005 are as follows:

	December 31, 2007 (One Year)	December 31, 2006 (One Year)	December 31, 2005 (Nine Months, see Note 30)
Short-term employee benefits	₱176,892,610	₱158,491,960	₱76,203,123
Pension benefits	81,426,925	5,429,048	3,672,382
	₱258,319,535	₱163,921,008	₱79,875,505

22. Cost of Sales - Merchandise

This account consists of:

	December 31, 2007 (One Year)	December 31, 2006 (One Year)	December 31, 2005 (Nine Months, see Note 30)
Merchandise inventories at beginning of period	₱4,488,187,321	₱1,357,734,162	₱1,638,258,531
Add purchases	80,485,937,624	57,815,795,239	30,279,568,673
Total goods available for sale	84,974,124,945	59,173,529,401	31,917,827,204
Less merchandise inventories at end of period	5,958,301,914	4,488,187,321	1,357,734,162
	₱79,015,823,031	₱54,685,342,080	₱30,560,093,042

23. Selling, General and Administrative Expenses

This account consists of:

	December 31, 2007 (One Year)	December 31, 2006 (One Year)	December 31, 2005 (Nine Months, see Note 30)
Personnel cost	₱5,187,189,811	₱4,060,696,837	₱2,760,727,016
Depreciation and amortization	4,293,157,520	3,355,058,496	2,283,024,304
Light and water	2,649,912,859	2,106,954,775	1,715,000,276
Taxes and licenses	1,805,180,974	1,472,372,281	858,071,806
Rent (see Note 27)	1,793,638,601	1,493,726,132	1,068,944,091
Outside services	1,031,871,400	721,517,987	505,946,306
Provision for impairment losses and others (see Notes 12, 14, 15 and 16)	818,255,424	1,596,489,245	–
Professional fees (see Note 21)	815,810,813	764,946,150	469,544,961
Repairs and maintenance	621,493,721	456,310,863	272,940,521
Supplies	452,261,240	316,196,579	172,025,499
Advertising and promotions	408,492,506	380,338,666	178,175,167
Pension expense (see Note 25)	224,994,763	145,132,125	55,084,618
Transportation and travel	146,527,324	72,929,367	55,627,846
Entertainment, representation and amusement	142,734,913	63,446,203	30,588,393
Insurance	118,782,519	126,214,054	95,610,023
Miscellaneous	1,072,779,175	462,350,195	283,729,946
	₱21,583,083,563	₱17,594,679,955	₱10,805,040,773

24. Interest Income and Interest Expense

The details of the sources of interest income and interest expense follow:

	December 31, 2007 (One Year)	December 31, 2006 (One Year)	December 31, 2005 (Nine Months, see Note 30)
Interest income on:			
Temporary investments	₱815,820,658	₱930,174,149	₱1,091,312,326
Investments held for trading	576,474,156	872,368,911	813,335,614
Time deposits	498,033,393	733,170,665	749,839,290
AFS investments	8,006,566	–	–
Others	918,972,799	–	2,213,422
	₱2,817,307,572	₱2,535,713,725	₱2,656,700,652
Interest expense on:			
Long-term debt	₱1,947,393,492	₱2,619,249,409	₱1,702,974,876
Bank loans	1,117,012,606	553,170,052	752,427,577
Accretion on notes payable	610,106,884	264,127,324	–
Others	6,841,157	5,524,293	100,054
	₱3,681,354,139	₱3,442,071,078	₱2,455,502,507

25. Pension Benefits

The Group has funded defined benefit pension plans covering all regular and permanent employees. The benefits are based on employees' projected salaries and number of years of service.

The following tables summarize the components of net benefit expense recognized by the Parent Company; SM Prime; SMDC; SM Mart, Inc.; SVI; Makro; Mainstream Business, Inc. and Market Strategic Firm, Inc. (subsidiaries of HMS); Major Shopping Management Corp., Metro Main Star Asia Corp. and Meridien Business Leader, Inc. (subsidiaries of Henfels); Madison Shopping Plaza, Inc. and Multi-Stores Corp. (subsidiaries of Marketwatch); Metro Manila Shopping Mecca Corp. and Mandurriao Star, Inc. (subsidiaries of MH Holdings); Mercantile Stores Group, Inc. and Mindanao Shopping Destination Corp. (subsidiaries of Romer); and Manila Southern Associates, Inc. (a subsidiary of Sanford) in the consolidated statements of income and the funded status and amounts recognized in the consolidated balance sheets for the plan.

Net Benefit Expense (Recognized in "Selling, General and Administrative Expenses")

	December 31, 2007 (One Year)	December 31, 2006 (One Year)	December 31, 2005 (Nine Months, see Note 30)
Current service cost	₱169,007,391	₱52,677,485	₱21,879,161
Interest cost on benefit obligation	103,881,353	84,008,875	53,062,008
Expected return on plan assets	(68,864,735)	(25,526,079)	(22,774,233)
Recognized actuarial loss (gain)	5,039,493	(54,953)	(6,138,762)
Net benefit expense	₱209,063,502	₱111,105,328	₱46,028,174

Defined Benefit Liability

	2007	2006
Present value of obligation	₱1,414,110,610	₱927,399,534
Fair value of plan assets	485,954,198	398,380,497
Unfunded status	928,156,412	529,019,037
Unrecognized actuarial loss	(432,642,117)	(50,441,520)
Defined benefit liability	₱495,514,295	₱478,577,517

Changes in the Present Value of the Defined Benefit Obligation

	December 31, 2007	December 31, 2006	December 31, 2005
Defined benefit obligation at beginning of period	₱927,399,534	₱544,375,691	₱379,014,334
Current service cost	169,007,391	52,677,485	21,879,161
Interest cost	103,881,353	84,008,875	53,062,008
Reclassifications from (to) defined benefit assets	224,655,140	(88,095,530)	–
Transfer from (to) related parties	(306,419,304)	(2,503,645)	95,995,421
Defined benefit obligation acquired in business combinations	26,258,700	243,793,790	–
Defined benefit obligation of a disposed subsidiary	(1,364,861)	–	–
Benefits paid	(36,929,094)	(18,641,047)	(77,002,592)
Actuarial loss on obligations	225,253,463	111,783,915	71,427,359
Other adjustments	82,368,288	–	–
Defined benefit obligation at end of period	₱1,414,110,610	₱927,399,534	₱544,375,691

Changes in the Fair Value of Plan Assets

	December 31, 2007	December 31, 2006	December 31, 2005
Fair value of plan assets at beginning of period	₱398,380,497	₱257,867,951	₱189,785,275
Actual contributions	174,028,769	127,991,041	120,063,694
Expected return on plan assets	68,864,735	25,526,079	22,774,233
Reclassifications from (to) defined benefit assets	192,128,922	(87,807,051)	–
Transfer from (to) related parties	(306,419,304)	(2,503,645)	95,995,421
Plan assets acquired in business combinations	26,445,000	46,524,171	–
Plan assets of a disposed subsidiary	(954,996)	–	–
Benefits paid	(36,929,094)	(18,641,047)	(77,002,592)
Actuarial gain (loss) on plan assets	3,721,308	49,422,998	(93,748,080)
Other adjustments	(33,311,639)	–	–
Fair value of plan assets at end of period	₱485,954,198	₱398,380,497	₱257,867,951

Unrecognized Actuarial Gain (Loss)

	December 31, 2007 (One Year)	December 31, 2006 (One Year)	December 31, 2005 (Nine Months, see Note 30)
Net cumulative unrecognized actuarial gain (loss) at beginning of period	(₱50,441,520)	₱25,310,745	₱196,624,946
Actuarial loss on obligations	(225,253,463)	(111,783,915)	(71,427,359)
Actuarial gain (loss) on plan assets	3,721,308	49,422,998	(93,748,080)
Reclassifications to defined benefit assets	(163,263,708)	(13,336,395)	–
Actuarial loss arising from business combinations	(2,270,394)	–	–
Actuarial gain of a disposed subsidiary	(173,833)	–	–
Recognized actuarial loss (gain)	5,039,493	(54,953)	(6,138,762)
Net cumulative unrecognized actuarial gain (loss) at end of period	(₱432,642,117)	(₱50,441,520)	₱25,310,745

Certain subsidiaries have defined benefit assets as of December 31, 2007 and 2006. The following tables summarize the components of net benefit expense recognized by Shoemart, SSMI, and SM Retail as included in the consolidated statements of income and the funded status and amounts as included in the consolidated balance sheets.

Net Benefit Expense (recognized in "Selling, General and Administrative Expenses")

	December 31, 2007 (One Year)	December 31, 2006 (One Year)	December 31, 2005 (Nine Months, see Note 30)
Current service cost	₱16,284,843	₱17,645,046	₱2,552,051
Interest cost on benefit obligation	3,751,339	17,805,332	4,441,128
Expected return on plan assets	(7,026,145)	(16,848,984)	(2,736,690)
Effect of asset limit	–	10,565,295	–
Recognized actuarial loss	2,921,224	4,860,108	4,799,955
Net benefit expense	₱15,931,261	₱34,026,797	₱9,056,444

Defined Benefit Asset (recorded as part of "Other Noncurrent Assets", see Note 16)

	2007	2006
Present value of obligation	₱486,055,471	₱270,382,911
Fair value of plan assets	642,661,528	216,263,138
Unfunded (overfunded) status	(156,606,057)	54,119,773
Amount not recognized due to asset limit	–	10,565,293
Unrecognized actuarial gain (loss)	110,776,187	(175,808,156)
Defined benefit asset	(₱45,829,870)	(₱111,123,090)

Changes in the Present Value of the Defined Benefit Obligation

	December 31, 2007	December 31, 2006	December 31, 2005
Defined benefit obligation at beginning of period	₱270,382,911	₱53,785,187	₱42,774,674
Current service cost	16,284,843	17,645,046	2,552,051
Interest cost	3,751,339	17,805,332	4,441,128
Reclassifications from (to) defined benefit obligation	(224,655,140)	88,095,530	–
Transfer from (to) related parties	608,258,888	(400,435)	(100,184,910)
Defined benefit obligation acquired in business combinations	–	2,398,064	–
Benefits paid	(641,833)	(12,634,671)	(2,338,819)
Actuarial loss (gain) on obligations	(174,811,827)	103,688,858	106,541,063
Other adjustments	(12,513,710)	–	–
Defined benefit obligation at end of period	₱486,055,471	₱270,382,911	₱53,785,187

Changes in the Fair Value of Plan Assets

	December 31, 2007	December 31, 2006	December 31, 2005
Fair value of plan assets at beginning of period	₱216,263,138	₱39,845,811	₱28,053,053
Reclassifications from (to) defined benefit obligation	(192,128,922)	87,807,051	–
Fair value of plan assets of SSMI	–	12,755,325	–
Expected return on plan assets	7,026,145	16,848,984	2,736,690
Actual contributions	8,412,552	56,107,496	9,828,889
Transfer to related parties	608,258,888	(400,435)	(100,184,910)
Benefits paid	(641,833)	(12,634,671)	(2,338,819)
Actuarial gain (loss) on plan assets	(398,390)	15,933,577	101,750,908
Other adjustments	(4,130,050)	–	–
Fair value of plan assets at end of period	₱642,661,528	₱216,263,138	₱39,845,811

Unrecognized Actuarial Loss (Gain)

	December 31, 2007	December 31, 2006	December 31, 2005
Net cumulative unrecognized actuarial loss at beginning of period	₱175,808,156	₱107,876,935	₱107,886,735
Actuarial loss (gain) on:			
Obligations	(174,811,827)	103,688,858	106,541,063
Plan assets	398,390	(15,933,577)	(101,750,908)
Reclassifications to defined benefit obligation	(163,263,708)	(13,336,395)	–
Actuarial gain arising from business combinations	–	(1,627,557)	–
Adjustment on asset limit	54,014,026	–	–
Recognized actuarial loss	(2,921,224)	(4,860,108)	(4,799,955)
Net cumulative unrecognized actuarial loss (gain) at end of period	(₱110,776,187)	₱175,808,156	₱107,876,935

The principal assumptions used in determining pension benefit obligations for the Group's plan are shown below:

	2007	2006
Discount rate	8%-12%	8%-12%
Expected rate of return on assets	6%	12%
Future salary increases	10%	10%

The Group expects to contribute about ₱496.2 million to its defined benefit pension plan in 2008.

The plan assets are composed mainly of cash and cash equivalents, loans, common trust funds, investments in government securities and other similar debt instruments.

26. Income Tax

The details of the Group's deferred tax assets and liabilities are as follows:

	2007	2006
Deferred tax assets (included under "Other noncurrent assets" account in the consolidated balance sheets):		
Unrealized foreign exchange loss	₱594,886,232	₱3,972,849
NOLCO	328,484,889	–
Defined benefit liability	282,758,682	234,309,716
MCIT	90,632,028	16,686,584
Mark-to-market loss on investments	28,763,130	28,100,074
Deferred income on sale of real estate	5,841,976	25,747,329
Others	107,971,380	44,947,934
	₱1,439,338,317	₱353,764,486
Deferred tax liabilities:		
Trademarks and brand names	₱1,796,268,296	₱1,785,347,642
Capitalized interest	707,197,402	558,122,284
Unrealized foreign exchange gain	548,977,320	26,232,766
Unrealized gross profit on sale of real estate	215,636,080	60,878,726
Unrealized marked-to-market gain on investments	25,830,949	138,502,864
Unamortized past service cost and defined benefit asset	3,830,668	16,295,113
Others	176,466,782	42,504,065
	₱3,474,207,497	₱2,627,883,460

The Group's consolidated deferred tax assets as of December 31, 2007 and 2006 have been reduced to the extent that part or all of the deferred tax assets may no longer be utilized in the future.

As of December 31, 2007, the Parent Company assessed that it will have sufficient taxable profit in future periods against which a deductible temporary difference arising from unrealized foreign exchange loss can be utilized. Accordingly, the Parent Company recognized deferred tax asset amounting to ₱551.8 million.

As of December 31, 2006, deferred tax assets were not recognized on the temporary deductible differences and carryforward benefits of MCIT and NOLCO of the Parent Company and a certain subsidiary as it is not probable that sufficient taxable profit will be available against which the deductible temporary differences and carryforward benefits of MCIT and NOLCO can be utilized.

The components of deductible temporary differences of certain balance sheet items and the carryforward benefits of unused MCIT and NOLCO, for which no deferred tax assets have been recognized in the consolidated balance sheets, are as follows:

	2007	2006
NOLCO	₱2,249,016,420	₱5,040,145,065
Allowance for doubtful accounts	2,130,524,408	1,312,268,984
Allowance for probable losses	951,995,000	951,995,000
Accretion on notes payable	874,234,208	264,127,324
MCIT	200,537,765	124,497,302
Net unrealized foreign exchange loss	143,321,365	–
Defined benefit liability	121,892,194	44,621,749
	₱6,671,521,360	₱7,737,655,424

As of December 31, 2007, the Group's MCIT and NOLCO are as follows:

Date Incurred	Carryforward Benefit Up To	MCIT	NOLCO
March 31, 2005	March 31, 2008	₱21,897,366	₱1,540,600,323
December 31, 2005	December 31, 2008	19,264,154	538,872,750
December 31, 2006	December 31, 2009	73,782,260	169,543,347
December 31, 2007	December 31, 2010	85,593,985	–
		₱200,537,765	₱2,249,016,420

MCIT amounting to ₱20,469,309 and ₱14,664,574 expired in 2007 and 2006, respectively.

NOLCO applied as deduction from gross income in 2007 amounted to ₱2,776,455,951. NOLCO amounting to ₱14,672,694 and ₱1,213,097,740 expired on December 31, 2007 and March 31, 2006, respectively.

The reconciliation between the statutory tax rates and the Group's effective tax rates on income before income tax is as follows:

	December 31, 2007 (One Year)	December 31, 2006 (One Year)	December 31, 2005 (Nine Months, see Note 30)
Statutory income tax rates	35%	35%	33%
Add (deduct) income tax effects of reconciling items:			
Equity in net earnings of associates	(6)	(5)	(5)
Interest income subjected to final tax	(2)	(4)	(7)
Dividend income exempt from tax	(2)	(2)	(3)
Provisions	1	3	–
Nondeductible interest expense	1	2	3
Net unrealized mark-to-market gain on investments held for trading	(1)	(2)	(1)
Gain on sale of shares of stock	–	(6)	–
Negative goodwill	–	–	(2)
Others	(3)	(4)	(4)
Change in unrecognized deferred tax assets	(1)	2	3
Effective income tax rates	22%	19%	17%

The deferred income taxes and the provision for current income tax include the effect of the change in tax rates. Under Republic Act No. 9337, regular corporate income tax rate for domestic corporations and resident and nonresident foreign corporations is increased to 35% (from 32%) beginning November 1, 2005 and the rate will be reduced to 30% beginning January 1, 2009. The regular corporate income tax rate shall be applied by multiplying the number of months covered by the new rate with the taxable income of the corporation during the year, divided by 12.

27. Lease Agreements

The lease agreements of SM Prime and its subsidiaries with their tenants are generally granted for a term of one year, with the exception of some of the larger tenants operating nationally, which are granted initial lease terms of five years, renewable on an annual basis thereafter. Upon inception of the lease agreement, tenants are required to pay certain amounts of deposits. Tenants likewise pay either a fixed monthly rent, which is calculated by reference to a fixed sum per square meter of area leased, or pay rent on a percentage rental basis, which comprises of a basic monthly amount and a percentage of gross sales or a minimum set amount, whichever is higher.

SM Prime and its subsidiaries also lease certain parcels of land where some of their malls are constructed. The terms of the lease are for periods ranging from 15 to 50 years, renewable for the same period under the same terms and conditions. Rental payments generally are computed based on a certain percentage of the gross rental income or a certain fixed amount, whichever is higher.

28. Financial Risk Management Objectives and Policies

The Group's principal financial instruments, other than derivatives, comprise bank loans, long-term debt, AFS investments, investments held for trading and cash and cash equivalents. The main purpose of these financial instruments is to raise financing for the Group's operations. The Group has various other financial assets and liabilities such as receivables and accounts payable and other current liabilities, which arise directly from its operations.

The Group also enters into derivative transactions, principally interest rate swaps, cross currency swaps, call options and nondeliverable forwards. The purpose is to manage the interest rate and currency risks arising from the Group's operations and its sources of finance.

The main risks arising from the Group's financial instruments are interest rate risk, foreign currency risk, liquidity risk, credit risk and equity price risk. The BOD reviews and agrees policies for managing each of these risks. The Group's accounting policies in relation to derivatives are set out in Note 4.

Interest Rate Risk

The following table sets out the carrying amount, by maturity, of the Group's financial instruments that are exposed to interest rate risk as of December 31, 2007:

	Below 1 Year	1-2 Years	2-3 Years	3-5 Years	Over 5 Years
Liabilities:					
Long-term Debt					
Fixed Rate:					
US$300 million convertible bonds	–	–	–	272.8	–
Interest rate	–	–	–	3.50%	–
Peso Loans:					
Redeemable preferred shares – Series 1	–	–	–	3,300.0	–
Interest rate	–	–	–	7.51%	–
Five-year syndicated loans	825.0	300.0	–	–	–
Interest rate	6.75% to 7.06%	6.75% to 7.06%	–	–	–
Other bank loans	–	–	–	1,000.0	4,200.0
Interest rate	–	–	–	6.65% to 7.58%	6.90% to 9.75%
Variable Rate:					
US$ five-year syndicated loan	–	150.0	–	–	–
Interest rate	–	LIBOR + margin %	–	–	–
Series "A" floating rate note	–	–	500.0	–	–
Interest rate	–	–	3-month T-bill rate + margin %	–	–
Bank loans collateralized with time deposits	–	–	–	6,000.0	–
Interest rate	–	–	–	3-month PDST-F + margin %	–
Five-year bilateral loans	15.6	62.5	62.5	3,109.4	–
Interest rate	3-month PDST-F + margin %	3-month PDST-F + margin %	3-month PDST-F + margin %	3-month PDST-F + margin %	–
Five-year floating rate notes	–	–	–	4,000.0	–
Interest rate				3-month PDST-F + margin %	
Redeemable preferred shares - Series 2	–	–	–	200.0	–
Interest rate				3-month PDST-F + margin %	–
Other loans	–	–	–	1,000.0	2,000.0
Interest rate	–	–	–	3-month PDST-F + margin %	3-month PDST-F + margin %

The following table sets out the carrying amount, by maturity, of the Group's financial instruments that are exposed to interest rate risk as of December 31, 2006:

	Below 1 Year	1-2 Years	2-3 Years	3-5 Years	Over 5 Years
Liabilities:					
Long-term Debt					
Fixed Rate:					
US$ five-year notes	222.0	–	–	–	–
Interest rate	8.00%	–	–	–	–
Peso Loans:					
Series "B" fixed rate note	–	–	–	4,000.0	–
Interest rate	–	–	–	9.95%	–
Series "C" fixed rate note	10.0	10.0	10.0	20.0	440.0
Interest rate	10.39%	10.39%	10.39%	10.39%	10.39%
Fixed rate Notes				1,500.0	1,500.0
Interest rate				10.54%	11.56%
Syndicated loans	825.0	825.0	300.0	–	–
Interest rate	8.0% to 9.66%	8.0% to 9.66%	8.0% to 9.66%	–	–
Other bank loans	–	–	534.0	1,000.0	1,200.0
Interest rate	–	–	12.54%	6.65% to 7.58%	9.75%
Variable Rate:					
US$ five-year syndicated loan	–	–	150.0	–	–
Interest rate	–	–	LIBOR + margin %	–	–
Series "A" floating rate note	–	–	–	500.0	–
Interest rate	–	–	–	T-bill rate + margin %	–
Loan with pledged time deposits	5,980.0	–	–	–	–
Interest rate	7.41% to 12.07%	–	–	–	–
Five-year bilateral loan	–	–	–	3,000.0	–
Interest rate	–	–	–	Mart 1 + margin %	–
Other loans	–	–	–	1,000.0	–
Interest rate	–	–	–	Mart 1 + margin %	–

Total		Total (Net of Debt Issue Cost)		Fair Value	
In Dollars	In Pesos	In Dollars	In Pesos	In Dollars	In Pesos
(In Millions)					
272.8	11,260.0	269.8	11,136.6	275.5	11,373.7
79.9	3,300.0	79.5	3,281.3	85.0	3,508.1
27.3	1,125.0	27.0	1,114.8	27.6	1,140.7
126.0	5,200.0	125.4	5,175.9	136.3	5,626.4
150.0	6,192.0	147.9	6,104.0	150.0	6,192.0
12.1	500.0	12.0	497.1	12.1	500.0
145.3	6,000.0	144.6	5,971.1	145.3	6,000.0
78.7	3,250.0	78.2	3,229.0	78.7	3,250.0
96.9	4,000.0	96.2	3,970.5	96.9	4,000.0
4.8	200.0	4.8	199.1	4.8	200.0
72.7	3,000.0	72.3	2,986.5	72.6	3,000.0

Total		Total (Net of Debt Issue Cost)		Fair Value	
In Dollars	In Pesos	In Dollars	In Pesos	In Dollars	In Pesos
(In Millions)					
222.0	10,885.5	220.7	10,822.4	220.7	10,885.5
81.6	4,000.0	81.0	3,970.2	91.5	4,484.2
10.0	490.0	9.9	486.3	11.7	575.6
61.2	3,000.0	60.6	2,972.5	74.0	3,627.1
39.8	1,950.0	39.4	1,932.4	41.4	2,030.9
55.8	2,734.0	55.5	2,722.0	63.0	3,089.7
150.0	7,354.5	147.8	7,247.4	152.2	7,460.7
10.2	500.0	10.1	496.3	10.4	510.6
122.0	5,980.0	122.0	5,980.0	122.0	5,980.0
61.2	3,000.0	60.7	2,975.3	61.2	3,000.0
20.4	1,000.0	20.3	995.2	20.4	1,000.0

Fixed rate financial instruments are subject to fair value interest rate risk while floating rate financial instruments are subject to cash flow interest rate risk.

Repricing of floating rate financial instruments is mostly done in intervals of three months or six months. Interest on fixed rate financial instruments is fixed until maturity of the instrument.

The Group's policy is to manage its interest cost using a mix of fixed and variable rate debts. The Group's policy is to keep between 50% and 60% of its borrowings at fixed rates of interest. To manage this mix in a cost-efficient manner, the Group enters into interest rate swaps, in which the Group agrees to exchange, at specified intervals, the difference between fixed and variable rate interest amounts calculated by reference to an agreed-upon notional principal amount. These swaps are designated to economically hedge the underlying debt obligations. As of December 31, 2007 and 2006, after taking into account the effect of interest rate swaps, approximately 47% and 56%, respectively, of the Group's borrowings are kept at a fixed rate of interest.

Interest Rate Risk Sensitivity Analysis. The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant of the Group's equity after income tax as of December 31, 2007 and income before income tax for the year then ended (through the impact of floating rate financial liabilities and debt securities classified as FVPL and AFS investments):

	Increase (Decrease) in Basis Points			
	100	50	(50)	(100)
Effect on:				
Income before income tax	(₱224,712,783)	(₱110,693,585)	₱110,687,514	₱224,818,444
Equity after income tax	(136,170,320)	(65,203,299)	62,579,802	133,179,813

Foreign Currency Risk

The Group's exposure to foreign currency risk arises as the Parent Company has significant investments and debt issuance which are denominated in US dollars. To manage its foreign exchange risk, stabilize cash flows, and improve investment and cash flow planning, the Group enters into foreign currency swaps contracts aimed at reducing and/or managing the adverse impact of changes in foreign exchange rates on financial performance and cash flows.

The following table shows the Group's foreign currency-denominated monetary assets and liabilities and their peso equivalents as of December 31, 2007:

	US$	Ph₱
Current assets:		
Cash and cash equivalents	$30,237,762	₱1,248,214,815
Time deposits	100,000,000	4,128,000,000
Investments held for trading	10,726,175	442,776,504
AFS investments	30,930,507	1,276,811,329
Receivables	2,704,513	111,642,297
Noncurrent assets:		
Time deposits	100,000,000	4,128,000,000
AFS investments	50,000,000	2,064,000,000
Total foreign currency-denominated monetary assets	324,598,957	13,399,444,945
Current liabilities -		
Current portion of long-term debt	4,639,208	191,506,506
Noncurrent liabilities -		
Long-term debt - net of current portion	353,940,682	14,610,671,353
Total foreign currency-denominated monetary liabilities	358,579,890	14,802,177,859
Net foreign currency-denominated monetary liabilities	$33,980,933	₱1,402,732,914

As of December 31, 2007, approximately 32.3%, (50.7% on December 31, 2006 and 49.0% on December 31, 2005) of the Group's total consolidated bank loans and debt were denominated in US dollars. Thus, a strengthening of the Philippine peso against the US dollar will decrease both the principal amount of the foreign currency-denominated debt and interest expense on the Group's debt in Philippine peso terms.

The Group has recognized in its consolidated statements of income foreign exchange gain of ₱593.9 million, ₱462.8 million and ₱103.7 million on its net foreign-currency denominated assets and liabilities for the periods ended December 31, 2007, 2006 and 2005, respectively. This resulted from the movements of the Philippine peso against the US dollar as shown in the following table:

	Peso to US Dollar
March 31, 2005	54.94
December 31, 2005	53.09
December 31, 2006	49.03
December 31, 2007	41.28

Foreign Currency Risk Sensitivity Analysis. The following table demonstrates the sensitivity to a reasonably possible change in US dollar to Philippine peso exchange rate, with all other variables held constant, of the Group's equity after income tax as of December 31, 2007 and income before income tax for the year then ended (due to changes in the fair value of monetary assets and liabilities).

	Increase (Decrease) in ₱ to US$ Rate			
	₱1.50	₱1.00	(₱1.00)	(₱1.50)
Effect on income before income tax	₱149,326,398	₱99,550,932	(₱99,550,932)	(₱149,326,398)
Effect on equity after income tax	117,275,459	78,183,640	(78,183,640)	(117,275,459)

The increase in ₱ to US$ rate means stronger peso against the U.S. dollar while a decrease in ₱ to US$ rate means stronger U.S. dollar against the peso.

Liquidity Risk

Liquidity risk arises from the possibility that the Group may encounter difficulties in raising funds to meet commitments from financial instruments or that a market for derivatives may not exist in some circumstance.

The Group seeks to manage its liquidity profile to be able to finance capital expenditures and service maturing debts. To cover its financing requirements, the Group intends to use internally generated funds and proceeds from debt and equity issues and sales of certain assets.

As part of its liquidity risk management program, the Group regularly evaluates its projected and actual cash flow information and continuously assesses conditions in the financial markets for opportunities to pursue fund-raising initiatives. These initiatives may include bank loans, export credit agency-guaranteed facilities, and debt capital and equity market issues.

The table below summarizes the maturity profile of the Group's financial liabilities as of December 31, 2007 based on the contractual undiscounted payments:

	On demand	Less than 1 year	2 to 5 years	More than 5 years	Total
Bank loans	₱–	₱2,874,033,812	₱239,340,267	₱–	₱3,113,374,079
Accounts payable and other current liabilities	733,231,447	24,270,554,946	–	–	25,003,786,393
Notes payable	–	8,508,888,420	–	–	8,508,888,420
Long-term debt (including current portion)	–	871,309,760	45,180,667,523	8,168,580,219	54,220,557,502

(Forward)

	On demand	Less than 1 year	2 to 5 years	More than 5 years	Total
Derivative liabilities					
(including current portion)	₱–	₱236,937,197	₱3,053,977,715	₱–	₱3,290,914,912
Dividends payable	–	20,416,956	–	–	20,416,956
Tenants' deposits and others	–	–	5,083,225,637	47,699,700	5,130,925,337
	₱733,231,447	₱36,782,141,091	₱53,557,211,142	₱8,216,279,919	₱99,288,863,599

Credit Risk

The Group trades only with recognized, creditworthy third parties. It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing basis with the result that the Group's exposure to bad debts is not significant. Given the Group's diverse base of customers, it is not exposed to large concentrations of credit risk.

With respect to credit risk arising from the other financial assets of the Group, which comprise of cash and cash equivalents, time deposits and short-term investments, investments held for trading, AFS investments and certain derivative instruments, the Group's exposure to credit risk arises from default of the counterparty, with a maximum exposure equal to the carrying amount of these instruments, without considering the effects of collateral.

Since the Group trades only with recognized third parties, there is no requirement for collateral.

Credit Risk Exposure and Concentration. The table below shows the maximum exposure to credit risk of the Group per business segment as of December 31, 2007, without considering the effects of collaterals and other credit risk mitigation techniques.

	Shopping Mall Development	Retail Merchandising	Real Estate Development and Tourism	Others	Total
Cash and cash equivalents	₱2,114,940,506	₱12,177,018,907	₱430,753,127	₱852,258,893	₱15,574,971,433
Time deposits and short-term investments (including noncurrent portion)	–	–	–	8,258,250,000	8,258,250,000
Investments held for trading	149,688,504	–	2,506,275,272	293,087,976	2,949,051,752
AFS investments	2,218,254,419	7,687,792,366	3,368,802,018	22,667,198,425	35,942,047,228
Receivables (including noncurrent portion of receivables from real estate buyers)	2,530,072,957	4,419,607,980	1,845,279,992	6,241,471,627	15,036,432,556
Derivative assets (included under "Other noncurrent assets" account in the 2007 consolidated balance sheet)	347,248,200	–	–	–	347,248,200
	₱7,360,204,586	₱24,284,419,253	₱8,151,110,409	₱38,312,266,921	₱78,108,001,169

The total financial assets under "Others" business segment relate primarily to the Parent Company's financial assets. The balances presented are net of intercompany eliminations.

As of December 31, 2007, these financial assets, except for certain receivables and AFS investments, are generally viewed by management as good and collectible considering the credit history of the counterparties. Past due or impaired financial assets are very minimal in relation to the Group's total financial assets.

Equity Price Risk

The Group's exposure to equity price pertains to its investments in quoted equity shares which are either classified as investments held for trading and AFS investments in the consolidated balance sheets. Equity price risk arises from the changes in the levels of equity indices and the value of individual stocks traded in the stock exchange. The Group has no equity risk exposure on stocks that are not traded.

The effect on income before tax and equity (as a result of change in fair value of investments held for trading and AFS investments as of December 31, 2007) due to a possible change in equity indices, with all other variables held constant is as follows.

	Change in Equity Price	Effect on Income Before Income Tax	Effect on Equity After Income Tax
Investments held for trading	+0.09%	₱2,029,740	₱2,029,740
	-0.09%	(2,029,740)	(2,029,740)
AFS investments	+0.09%	–	12,054,885
	-0.09%	–	(12,054,885)

Capital Management

The primary objective of the Group's capital management is to ensure that it maintains a strong credit rating and healthy capital ratios in order to support its business and maximize shareholder value.

The Group manages its capital structure and makes adjustments to it, in the light of changes in economic conditions. To maintain or adjust the capital structure, the Group may adjust the dividend payment to shareholders, pay-off existing debts, return capital to shareholders or issue new shares.

The Group monitors its capital gearing by measuring the ratio of interest-bearing debt to total capital and net interest-bearing debt to total capital. Interest-bearing debt includes all short-term and long-term debt while net interest-bearing debt includes all short-term and long-term debt net of cash and cash equivalents, investments in bonds held for trading and time deposits. The Group's policy is to keep the gearing ratio at 50:50. As of December 31, 2007 and 2006, the Group's ratio of interest-bearing debt to total capital were 30:70 and 34:66, respectively, and the ratio of net interest-bearing debt to total capital were 17:83 and 15:85, respectively.

As of December 31, 2007 and 2006, the Group's ratio of interest-bearing debt to total capital and ratio of net interest-bearing debt to total capital were as follows:

Interest-bearing debt to total capital

	2007	2006
Bank loans	₱3,037,560,267	₱13,319,576,097
Current portion of long-term debt	833,350,952	17,629,400,122
Long-term debt - net of current portion	42,832,528,656	22,970,657,371
Total interest-bearing debt (a)	46,703,439,875	53,919,633,590
Total equity attributable to parent equity holders	108,887,545,690	103,303,928,520
Total interest-bearing debt and equity attributable to parent equity holders (b)	₱155,590,985,565	₱157,223,562,110
Gearing ratio (a/b)	30%	34%

Net interest-bearing debt to total capital

	2007	2006
Bank loans	₱3,037,560,267	₱13,319,576,097
Current portion of long-term debt	833,350,952	17,629,400,122
Long-term debt - net of current portion	42,832,528,656	22,970,657,371
Less cash and cash equivalents, time deposits and short-term investments and investments in bonds held for trading	(24,275,997,913)	(36,263,844,994)
Total net interest-bearing debt (a)	22,427,441,962	17,655,788,596
Total equity attributable to parent equity holders	108,887,545,690	103,303,928,520
Total net interest-bearing debt and equity attributable to parent equity holders (b)	₱131,314,987,652	₱120,959,717,116
Gearing ratio (a/b)	17%	15%

29. Financial Assets and Liabilities

Fair Value of Financial Instruments

The following table sets forth the carrying values and estimated fair values of financial assets and liabilities by category and by class recognized as of December 31, 2007 and 2006. There are no material unrecognized financial assets and liabilities as of December 31, 2007.

	2007		2006	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial Assets				
Financial Assets at FVPL:				
Investments held for trading:				
Shares of stock	₱2,506,275,272	₱2,506,275,272	₱1,980,684,348	₱1,980,684,348
Bonds	442,776,480	442,776,480	7,401,164,280	7,401,164,280
Derivative assets (included under "Other noncurrent assets" account in the consolidated balance sheets)	347,248,200	347,248,200	918,945,584	918,945,584
	3,296,299,952	3,296,299,952	10,300,794,212	10,300,794,212
Loans and Receivables:				
Cash and cash equivalents	15,574,971,433	15,574,971,433	21,037,492,714	21,037,492,714
Time deposits and short-term investments (including noncurrent portion)	8,258,250,000	8,676,448,824	7,825,188,000	8,035,953,995
Receivables (including noncurrent portion of receivables from real estate buyers in 2007)	15,036,432,556	15,036,432,556	7,287,814,474	7,287,814,474
	38,869,653,989	39,287,852,813	36,150,495,188	36,361,261,183
AFS Investments:				
Shares of stock	33,013,745,529	33,013,745,529	35,783,038,799	35,783,038,799
Redeemable preferred shares	2,218,254,419	2,218,254,419	5,270,194,577	5,270,194,577
Government bonds	704,897,280	704,897,280	1,046,853,780	1,046,853,780
Club shares	5,150,000	5,150,000	4,670,000	4,670,000
	35,942,047,228	35,942,047,228	42,104,757,156	42,104,757,156
	₱78,108,001,169	₱78,526,199,993	₱88,556,046,556	₱88,766,812,551
Financial Liabilities				
Financial Liabilities at FVPL -				
Derivative liabilities (including current portion in 2007)	₱3,290,914,912	₱3,290,914,912	₱1,042,500,665	₱1,042,500,665
Other Financial Liabilities:				
Bank loans	3,037,560,267	3,037,560,267	13,319,576,097	13,319,576,097
Accounts payable and other current liabilities	25,003,786,393	25,003,786,393	18,240,321,118	18,240,321,118
Long-term debt (including current portion and net of unamortized debt issue cost)	43,665,879,608	46,028,012,312	40,600,057,493	42,644,271,716
Notes payable (including current portion in 2006)	8,118,761,498	8,252,535,856	14,079,284,004	14,684,442,077
Dividends payable	20,416,956	20,416,956	556,008,628	556,008,628
Tenants' deposits	5,008,344,147	4,724,735,699	4,389,520,295	4,340,216,653
	84,854,748,869	87,067,047,483	91,184,767,635	93,784,836,289
	₱88,145,663,781	₱90,357,962,395	₱92,227,268,300	₱94,827,336,954

The following methods and assumptions were used to estimate the fair value of each class of financial instrument for which it is practicable to estimate such value:

Investments Held for Trading. The fair values are the quoted market prices of the instruments at balance sheet date.

Derivative Assets. The fair values of the nondeliverable forwards, cross currency swaps and interest rate swaps are based on quotes obtained from counterparties.

Cash and Cash Equivalents. The carrying amount reported in the consolidated balance sheets approximates fair value due to the short-term nature of the transactions.

Time Deposits and Short-term Investments. The estimated fair value is based on the discounted value of future cash flows using the prevailing interest rates. The discount rates used range from 3.07% to 3.66% as of December 31, 2007 and 5.04% as of December 31, 2006.

Receivables. The net carrying value approximates the fair value due to the short-term maturities of the current portion of receivables and regular repricing of interest rates on long-term receivables.

AFS Investments. The fair value of investments that are actively traded in organized financial markets is determined by reference to quoted market bid prices at the close of business at balance sheet date. For investment in debt instruments, such as the investments in mandatorily redeemable preferred shares where there is no active market, the fair value is based on the present value of future cash flows discounted at prevailing interest rates. The discount rates used ranged from 4.33% to 7.95% and 6.97% to 7.98% as of December 31, 2007 and 2006, respectively. For unquoted equity securities, the carrying amounts (cost less allowance for impairment losses) approximate fair value due to the unpredictable nature of future cash flows and lack of suitable methods for arriving at reliable fair value.

Bank Loans. The carrying value approximates fair value because of recent and regular repricing (i.e., quarterly) based on market conditions.

Accounts Payable and Other Current Liabilities and Dividends Payable. The carrying value reported in the consolidated balance sheets approximates the fair value due to the short-term maturities of these liabilities.

Long-term Debt. Fair value is based on the following:

Debt Type	Fair Value Assumptions
Fixed Rate Loans	Estimated fair value is based on the discounted value of future cash flows using the applicable rates for similar types of loans. Discount rates used range from 4.19% to 7.36% and 5.94% to 7.35% as of December 31, 2007 and 2006, respectively.
Variable Rate Loans	For variable rate loans that reprice every three months, the carrying value approximates the fair value because of recent and regular repricing based on current market rates. For variable rate loans that reprice every six months, the fair value is determined by discounting the principal amount plus the next interest payment using the prevailing market rate for the period up to the next repricing date. Discount rates used was 6.99% as of December 31, 2006.

Notes Payable and Tenant's Deposits. The estimated fair value is based on the discounted value of future cash flows using the applicable rates. The discount rates used range from 4.18% to 5.17% and 5.40% to 5.67% as of December 31, 2007 and 2006, respectively, for notes payable and 5.86% to 6.76% and 6.60% to 6.69% as of December 31, 2007 and 2006, respectively, for tenants' deposits.

Derivative Liabilities. The fair values of the cross currency swaps and nondeliverable forwards are based on quotes obtained from counterparties. The fair value of the options relating to issuance of convertible bonds was obtained from a third party. The fair value of the call options arising from the future sale of SMC common shares was computed using Black-Scholes Merton model.

Derivative Financial Instruments

To address the Group's exposure to market risk for changes in interest rates primarily to long-term floating rate debt obligations and manage its foreign exchange risks, the Group entered into various derivative transactions such as interest rate swaps, cross and foreign currency swaps, currency options and nondeliverable forwards. These derivative instruments provide economic hedges under the Group's policies but are not designated as accounting hedges. Changes in the fair values of derivative instruments not designated as hedges are recognized immediately in the consolidated statements of income.

Derivative Assets (Included under "Other Noncurrent Assets")

	2007	2006
Parent -		
Fixed to floating interest rate swaps	₱–	₱153,005,532
Subsidiary:		
Nondeliverable forwards	272,130,520	–
Foreign currency call options	54,940,698	39,722,488
Floating to fixed interest rate swaps	20,176,982	149,199,858
Fixed to floating interest rate swaps	–	577,017,706
	₱347,248,200	₱918,945,584

Derivative Liabilities

	2007	2006
Current		
Parent -		
Call options arising from future sale of SMC common shares	₱236,937,197	₱–
Noncurrent		
Parent -		
Options arising from convertible bonds	₱1,285,459,199	₱–
Subsidiary:		
Cross currency swap	1,496,387,996	1,042,500,665
Nondeliverable forwards	272,130,520	–
	₱3,053,977,715	₱1,042,500,665

The table below shows information on the Group's cross currency and interest rate swaps presented by maturity profile:

	2007	
	<1 year	>1-<2 years
Cross-Currency Swaps		
Floating-Fixed:		
Notional amount	$70,000,000	$70,000,000
Receive-floating rate	6 months	6 months
	LIBOR+margin%	LIBOR+margin%
Pay-fixed rate	12.58-12.75%	12.58-12.75%
Weighted swap rate	₱56.31	₱56.31
Interest Rate Swap		
Floating-Fixed:		
Notional amount	$80,000,000	$80,000,000
Receive-floating rate	6 months	6 months
	LIBOR+margin%	LIBOR+margin%
Pay-fixed rate	5.34%	5.34%

2006						
	<1 year	>1-<2 years	>2-<3 years	>3-<4 years	>4-<5 years	>5 years
Subsidiary						
Cross-Currency Swaps						
Floating-Fixed:						
Notional amount	$70,000,000	$70,000,000	$70,000,000			
Receive-floating rate	6 months	6 months	6 months			
	LIBOR+margin%	LIBOR+margin%	LIBOR+margin%			
Pay-fixed rate	12.58-12.75%	12.58-12.75%	12.58-12.75%			
Weighted swap rate	₱56.31	₱56.31	₱56.31			
Interest Rate Swap						
Floating-Fixed:						
Notional amount	$80,000,000	$80,000,000	$80,000,000			
Receive-floating rate	6 months	6 months	6 months			
	LIBOR+margin%	LIBOR+margin%	LIBOR+margin%			
Pay-fixed rate	5.34%	5.34%	5.34%			
Fixed - Floating:						
Notional amount	₱3,750,000,000	₱3,750,000,000	₱3,750,000,000	₱3,750,000,000	₱1,500,000,000	₱1,500,000,000
Receive-fixed rate	10.54-11.56%	10.54-11.56%	10.54-11.56%	10.54-11.56%	11.56%	11.56%
Pay-floating rate	3 months	3 months	3 months	3 months	3 months	3 months
	Mart 1+margin %	Mart 1+margin %	Mart 1+margin %	Mart 1+margin %	Mart 1+margin %	Mart 1+margin %
Parent						
Interest Rate Swap:						
Fixed - Floating:						
Notional amount	₱1,500,000,000	₱1,500,000,000	₱1,500,000,000	₱1,500,000,000		
Receive-fixed rate	9.951%	9.951%	9.951%	9.951%		
Pay-floating	3 months	3 months	3 months	3 months		
	Mart 1+margin %	Mart 1+margin %	Mart 1+margin %	Mart 1+margin %		

Options Arising from Convertible Bonds. The Parent Company's convertible bonds contain multiple embedded derivatives such as short call equity option, long call option and short put option.

Short call equity option pertains to the option of the bondholders to convert the Bonds into SMIC's common shares prior to maturity. If a bondholder exercised its conversion option, the Parent Company can choose either to settle the Bonds in cash or issue common shares, and such option on the part of the Parent Company is a long call option.

The Bonds are denominated in US dollar while the currency of the underlying asset is denominated in Philippine peso. The contracting parties have fixed the exchange rate at ₱48.37 to US$1. Considering the exposure of the Parent Company, the option was assessed as short put option. In addition, the bondholder may require the Parent Company to redeem all or some of the Bond at 110.79% of the principal amount on March 19, 2010, and such option is also considered a short put option.

As of December 31, 2007, the fair value of the options, which is shown as a noncurrent liability in the consolidated balance sheets, amounted to ₱1,285.5 million. The Group recognized unrealized mark-to-market gain of ₱675.2 million, which is reflected under "Gain on sale of available-for-sale investments and fair value changes on investments held for trading and derivatives" in the consolidated statements of income.

Call Options Arising from Future Sale of SMC Common Shares. The stock purchase agreement discussed in Note 11 grants SMCRP the right but not the obligation to pay the remaining balance of the total consideration. Such option is an embedded derivative, which is valued using Black-Scholes Merton model. As of December 31, 2007, the option, which is shown as a current liability in the consolidated balance sheets, has a carrying value of ₱236.9 million. The Group recognized unrealized mark-to-market loss of ₱146.5 million, which is reflected under "Gain on sale of available-for-sale investments and fair value changes on investments held for trading and derivatives" in the 2007 consolidated statement of income.

Cross Currency Swaps. In 2004, SM Prime entered into cross currency swap agreements with an aggregate notional amount of US$70.0 million and weighted average swap rate of ₱56.31 to US$1. Under these agreements, SM Prime effectively swaps the principal amount and interest of these US dollar-denominated five-year syndicated loan into Philippine peso-denominated loans with payments up to October 2009. As of December 31, 2007 and 2006, the cross currency swaps have negative fair values of ₱1,496.4 million and ₱1,042.5 million, respectively.

Interest Rate Swaps. Also in 2004, SM Prime entered into US dollar interest rate swap agreements with an aggregate notional amount of US$80.0 million. Under these agreements, SM Prime effectively swaps the floating rate U.S. dollar-denominated five-year syndicated loan into fixed rate loans with semi-annual payment intervals up to October 2009. As of December 31, 2007 and 2006, the floating to fixed interest rate swaps have positive fair values of ₱20.2 million and ₱149.2 million, respectively.

In 2005, SM Prime also entered into Philippine peso interest swap agreements with an aggregate notional amount of ₱3,750.0 million. Under these agreements, SM Prime effectively swaps these fixed rate Philippine peso-denominated five-year and seven-year syndicated fixed rate notes into floating rate loans based on Mart 1 plus an agreed margin with semi-annual payment intervals up to July 2012. As of December 31, 2006, the fixed to floating interest rate swaps have positive fair values of ₱577.0 million. As discussed in Note 19, in June 2007, as a result of the prepayment of the underlying obligation, the related interest rate swap was also terminated with net proceeds amounting to ₱438.4 million and realized loss of ₱138.6 million.

In 2005, SMIC had an interest rate swap agreement with BDO for a notional amount of ₱795.1 million. Under this agreement, SMIC will pay BDO a floating rate based on three-month Mart 1 plus 25 basis points on a quarterly basis. In return, SMIC will receive a fixed interest of 10% every quarter. The agreement was terminated in May and June 2006.

In 2006, SMIC entered into interest rate swap agreements with an aggregate notional amount of ₱1,500.0 million. Under these agreements, SMIC effectively swaps the fixed rate Philippine peso-denominated loans into floating rate loans based on Mart 1 plus an agreed margin with semi-annual payment intervals up to October 2010. Also in 2006, SMIC entered into structured swap agreement with notional amount of ₱990.0 million and maturing in October 2007. Under the swap agreement, SMIC receives a fixed rate of 3.38% every quarter starting January 2007. On the other hand, it pays an amount based on the agreed terms if the spot rate on interest payment date is above the strike price of ₱54/$1, or pays nothing if the spot rate on payment date is equal to or below the strike price. As of December 31, 2006, the fixed to floating interest rate swap and structured swap have positive fair value amounting to ₱123.6 million and ₱29.4 million, respectively. The interest rate swap was preterminated in June 2007, which resulted in a realized loss of ₱61.3 million, while the structured swap had matured in October 2007, which also resulted in a realized loss of ₱19.7 million.

Foreign Currency Call Options. To manage the interest expense on the loans and the hedging costs of the cross currency swaps mentioned above, SM Prime entered into the following cost reduction trades:

Trade Date	Start Date	Notional Amount	Strike Rate	Premium (p.a.)	Payment Dates
January 25, 2007	January 25, 2007	₱3,942,000,000	₱52 (US$1.00)	1.00%	October 18, 2007 April 18, 2008
June 27, 2007	April 18, 2007	₱3,942,000,000	₱49 (US$1.00)	1.00%	October 18, 2007 April 18, 2008 June 30, 2008
June 27, 2007	February 15, 2007	₱1,200,000,000	₱49 (US$1.00)	1.00%	February 15, 2008 June 30, 2008

In these trades, SM Prime will receive a premium equivalent to 1.0% savings per annum on the notional amounts. However, should the USD/PHP exchange rate trade above the strike price on the two dates, SM Prime will have to pay a penalty based on an agreed formula. As of December 31, 2007 and 2006, the positive fair value of the currency option is ₱54.9 million and ₱39.7 million, respectively.

Nondeliverable Forwards. In 2007, SM Prime entered into forward contracts to sell ₱ and buy US$ with different counterparties at an aggregate notional amount of US$180.0 million. As of December 31, 2007, the outstanding aggregate notional amount is US$160.0 million. The average forward rates range from ₱41.05 to ₱46.53, which mature in various dates in 2008. Also in 2007, SM Prime entered into forward contracts to sell US$ and buy ₱ with different counterparties at an aggregate notional amount of US$180.0 million. As of December 31, 2007, the outstanding aggregate notional amount is US$160.0 million. The average forward rates range from ₱41.31 to ₱46.68, which mature in various dates in 2008. As of December 31, 2007, the net fair value of the above forward contracts is immaterial. SM Prime recognized derivative asset and derivative liability amounting to ₱272.1 million from these forward contracts.

Foreign Currency Swaps. In 2005, SMIC also entered into short-term foreign currency swaps from three days up to three months with banks to hedge against foreign exchange rate risks. The marked-to-market gain of the outstanding foreign currency swaps with a notional amount of ₱106.1 million as of December 31, 2005 amounted to ₱0.1 million. As of December 31, 2007 and 2006, SMIC has no outstanding short-term foreign currency swaps.

The loss on derivative transactions amounted to ₱38.9 million and ₱123.6 million for the years ended December 31, 2007 and 2006, respectively. The loss on derivative transactions is included under "Gain on sale of available-for-sale investments and fair value changes on investments held for trading and derivatives" in the consolidated statements of income.

Fair Value Changes on Derivatives

The net movements in fair value changes of all derivative instruments as of December 31 are as follows:

	2007	2006
Balance at beginning of year	(₱123,555,081)	₱–
Net change in fair value:		
Premium on options embedded in convertible bonds and future sale of SMC shares	(2,051,167,405)	–
Recognized in profit or loss	(38,920,988)	(123,555,081)
Fair value of derivatives on settled contracts	(730,023,238)	–
Balance at end of year	(₱2,943,666,712)	(₱123,555,081)

30. Change in Accounting Period

On August 13, 2005 and September 6, 2005, the Philippine SEC and the Bureau of Internal Revenue, respectively, approved the change in the Parent Company's accounting period from a fiscal year ending March 31 to December 31. The amounts presented in the December 31, 2005 consolidated statements of income, changes in stockholders' equity and cash flows, and related notes are for nine months and, accordingly, are not comparable with those in the years ended December 31, 2007 and 2006.

31. Earnings Per Common Share (EPS) Computation

	December 31, 2007 (One Year)	December 31, 2006 (One Year)	December 31, 2005 (Nine Months, see Note 30)
Net income attributable to common equity holders of the Parent			
Net income attributable to common equity holders of the Parent for basic earnings (a)	₱12,018,223,857	₱10,571,856,399	₱8,029,241,507
Effect on net income of convertible bonds, net of tax	(1,164,492,144)	–	–
Net income attributable to common equity holders of the Parent adjusted for the effect of dilution (b)	10,853,731,713	10,571,856,399	8,029,241,507
Weighted average number of common shares outstanding			
Weighted average number of common shares outstanding for the period (c)	611,023,038	585,232,753	552,631,000
Dilutive effect of convertible bonds	16,002,779	–	–
Weighted average number of common shares outstanding for the period adjusted for the effect of dilution (d)	627,025,817	585,232,753	552,631,000
Basic EPS (a/c)	₱19.67	₱18.06	₱14.53
Diluted EPS (b/d)	₱17.31	₱18.06	₱14.53

32. Other Matters

a. On August 1, 2007, the BOD approved to designate Shoemart as the holding entity for the various property projects of the SM Group. On October 8, 2007, the respective BOD of SMIC and Shoemart entered into an agreement whereby SMIC agreed to swap its 1,823,841,965 SMDC common shares in exchange for 372,212 Shoemart common shares based on an independent valuation of the respective shares by Macquarie Securities (Asia) Pte Limited. On January 24, 2008, the Philippine SEC approved the valuation of the shares of stock of SMDC as consideration for the additional issuance of 372,212 shares.

b. In 1988, the Parent Company acquired the former Baguio Pines Hotel properties from the Development Bank of the Philippines (DBP) and purchased the Taal Vista Lodge (the Lodge) from the Taal & Tagaytay Management Corp., the original purchaser of the Lodge from DBP.

Previously, in 1984, certain minority stockholders of Resort Hotel Corp. (RHC), the previous owner of the former Baguio Pines Hotel properties and the Lodge, filed with the Regional Trial Court (RTC) of Makati a derivative suit against the DBP questioning the foreclosure by the DBP of these properties. The Parent Company was impleaded as a party defendant in 1995. The RTC of Makati voided the foreclosure by the DBP on the mortgaged properties.

The DBP and the Parent Company have appealed the RTC's decision with the Court of Appeals. On May 25, 2007, the Court of Appeals issued a decision completely reversing and setting aside the February 13, 2004 decision of the RTC Makati and, consequently, dismissing the said RTC case. The appellees (certain minority stockholders of RHC) filed a Motion for Reconsideration with the Court of Appeals and on November 9, 2007, the Court of Appeals issued a resolution denying the appellees' Motion for Reconsideration. Recently, the appellees filed a Petition for Review on Certiorari before the Supreme Court appealing the decision of the Court of Appeals reversing the said decision of the RTC Makati. DBP believes that all the legal requirements on the foreclosure of the mortgages were complied with and the said foreclosures of mortgages are legal and binding.

c. On November 13, 2007, the BOD of SM Prime approved the acquisition of 100% of the outstanding common shares of Affluent Capital Enterprises (Affluent) and MegaMake Enterprise Limited (MegaMake), holding companies of the three SM Malls in China, in exchange for SM Prime's common shares with a valuation based on the 30-day volume weighted average price of SM Prime.

On January 2, 2008, SM Prime executed the relevant documents for the exchange of Affluent and MegaMake shares of stock valued at ₱10,827 million. Subject to the approval by the Philippine SEC and the PSE, SM Prime will issue 372,492,882 new common shares to Oriental Land Development Limited for and in exchange of 100% equity of MegaMake and 540,404,330 new common shares to Grand China International Limited for and in exchange of 100% equity of Affluent. As of March 5, 2008, the transaction is still pending approval by the Philippine SEC and the PSE.

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Stockholder Inquiries	SM Investments Corporation common stock is listed and traded in the Philippine Stock Exchange under the symbol **'SM'** Inquiries regarding dividend payments, account status, address changes, stock certificates, and other pertinent matters may be addressed to the company's transfer agent: Stock Transfer Service, Inc. 8th Floor, Phinma Plaza, 39 Plaza Drive, Rockwell Center, Makati City 1200 Philippines Tel. (632) 898.7555 Fax (632) 898.7597
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SEC Form 17-A

The Financial information in this report, in the opinion of Management, substantially conforms with the information required in the "17-A Report" submitted to the Securities and Exchange Commission. Copies of this report may be obtained free of charge upon written request addressed to the Office of the Corporate Secretary.

Institutional Investor Inquiries

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