# COVER SHEET

PW-343

LT GROUP, INC.
(Formerly TANDUAY HOLDINGS, INC.)
and Subsidiaries

(Company's Full Name)

11th Floor Unit 3 Bench Tower
30th St. cor Rizal Drive Crescent
Park West 5 Bonifacio Global City
Taguig City

(Business Address: No. StreetCity/Town/Province)

| **Mr. Nestor C. Mendones** | **817-8710** |
|---|---|
| (Contact Person) | (Company Telephone Number) |

| 1 2 | 3 1 | 17-Q | 0 5 | 0 2 |
|---|---|---|---|---|
| *Month* | *Day* | (Form Type) | *Month* | *Day* |
| (Calendar Year) | | | (Annual Meeting) | |

(Secondary License Type, If Applicable)

Dept. Requiring this Doc.

Amended Articles Number/Section

Total Amount of Borrowings

Total No. of Stockholders

Domestic

Foreign

To be accomplished by SEC Personnel concerned

File Number

LCU

Document ID

Cashier

STAMPS

Remarks: Please use BLACK ink for scanning purposes.

SECURITIES AND EXCHANGE COMMISSION

SEC FORM 17-Q

QUARTERLY REPORT PURSUANT TO SECTION 17 OF THE SRC AND
SECTION 141 OF THE CORPORATION CODE OF THE PHILIPPINES

SEC Central Receiving and Records Division
HRAD
AUG 14 2013
BY:
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1. For the quarterly period ended June 30, 2013

2. SEC Identification Number PW-343

3. BIR Tax Identification No. 121-145-650-000

4. Exact name of registrant as specified in its charter LT GROUP, INC.

5. Province, country or other jurisdiction of incorporation or organization Philippines

6. Industry Classification Code: (SEC Use Only)

7. Address of registrant's principal office — Postal Code
11/F Unit 3 Bench Tower, 30th St. corner Rizal drive
Crescent Park West 5 Bonifacio Global City Taguig City — 1634

8. Registrant's telephone number, including area code (632) 817-8710

9. Former name, former address, and former fiscal year, if changed since last report.

**TANDUAY HOLDINGS, INC.**

10. Securities registered pursuant to Sections 8 and 12 of the SRC, or 4 and 8 of the RSA

| Title of Each Class | Number of Shares of common stock Outstanding and Amount of Debt Outstanding |
|---|---|
| Common shares, ₱1.00 par value | 10,821,388,889 |

11. Are any or all of the securities listed on the Philippine Stock Exchange?

    Yes [/] No [ ]

12. Indicate by check mark whether the registrant:

    (a) has filed all reports required to be filed pursuant to Section 17 of the Securities Regulation Code (SRC) and Section 26 and 141 of the Corporation Code of the Philippines, during the preceding 12 months (or for such shorter period the registrant was required to file such reports)

    Yes [/] No [ ]

    (b) has been subject to such filing requirements for the past 90 days

    Yes [/] No [ ]

## PART I - FINANCIAL INFORMATION

### Item 1. Financial Statements

The unaudited interim condensed financial statements of LT Group, Inc. (the Company) and its subsidiaries as of and for the period ended June 30, 2013 (with comparative figures as of December 31, 2012 and for the period June 30, 2012) are filed as part of this form 17-Q as Annex "A".

### Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The information required by Part IV, Paragraph a (2) (B) of SRC 12 is attached hereto as Annex "B"

## PART II – OTHER INFORMATION

Not Applicable – There are no disclosures not made under SEC form 17-C

## SIGNATURES

Pursuant to the requirements of the Securities and Regulation Code, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

| | |
|---|---|
| **NESTOR C. MENDONES** | **JOSE GABRIEL D. OLIVES** |
| Deputy CFO | Chief Finance Officer |
| August 14, 2013 | August 14, 2013 |

**Annex "A"**

# LT GROUP, INC.
# (Formerly Tanduay Holdings, Inc.)
# AND SUBSIDIARIES

Consolidated Financial Statements
For the Six Months Ended June 30, 2013

LT Group, Inc.
*[Formerly Tanduay Holdings, Inc. (a Subsidiary of Tangent Holdings Corporation)]*
and Subsidiaries

**Unaudited Interim Condensed Consolidated Financial Statements**
**As at June 30, 2013**
**(with comparative figures as at December 31, 2012**
**And Six Months Ended June 30, 2013 and 2012)**

# LT GROUP, INC.
**[Formerly Tanduay Holdings, Inc.**
**(a Subsidiary of Tangent Holdings Corporation)]**
## AND SUBSIDIARIES

## UNAUDITED INTERIM CONSOLIDATED BALANCE SHEETS
**JUNE 30, 2013**
**(WITH COMPARATIVE FIGURES AS OF DECEMBER 31, 2012)**
**(Amounts in Thousands)**

| | **June 30, 2013** | December 31, 2012 (As Restated- Notes 5,2 and 25) |
|---|---|---|
| **ASSETS** | | |
| **Current Assets** | | |
| Cash and cash equivalents (Note 4) | **₱172,298,994** | ₱124,214,998 |
| Financial assets at fair value through profit or loss | **9,517,104** | 11,398,591 |
| Available for sale (AFS) financial assets(Note 8) | **80,081,154** | 6,335,811 |
| Loans and receivables (Note 5) | **109,342,421** | 139,467,391 |
| Due from related parties (Note 4) | **32,326,105** | 16,362,465 |
| Inventories (Note 6) | **9,589,715** | 10,964,286 |
| Prepayments and other current assets (Note 7) | **5,597,313** | 3,447,706 |
| **Total Current Assets** | **418,752,806** | 312,191,248 |
| **Noncurrent Assets** | | |
| Loans and receivables - net of current portion (Note 5) | **141,200,640** | 122,410,493 |
| Available-for-sale (AFS) financial assets (Note 8) | **18,835,304** | 91,598,467 |
| Investments in associate and joint venture (Note 9) | **14,182,208** | 13,911,250 |
| Property, plant and equipment: | | |
| At appraised values | **38,358,422** | 38,553,539 |
| At cost | **4,831,083** | 4,686,170 |
| Investment properties | **24,203,605** | 23,618,305 |
| Net retirement plan assets (Note 15) | **1,201,074** | 1,173,073 |
| Deferred income tax assets (Note 19) | **1,896,459** | 2,659,973 |
| Other noncurrent assets (Note 10) | **4,152,194** | 3,423,426 |
| **Total Noncurrent Assets** | **248,860,989** | 302,034,696 |
| **TOTAL ASSETS** | **₱667,613,794** | ₱614,225,944 |
| **LIABILITIES AND EQUITY** | | |
| **Current Liabilities** | | |
| Deposit liabilities | **₱360,761,886** | ₱358,462,436 |
| Financial liabilities at fair value through profit or loss | **5,314,955** | 389,817 |
| Bills and acceptances payable | **7,047,186** | 17,256,919 |
| Short-term debts (Note 12) | **–** | 1,870,000 |
| Accounts payable and accrued expenses (Note 11) | **10,686,084** | 11,967,174 |
| Income tax payable | **327,618** | 236,672 |
| Customers' deposits | **2,872,036** | 2,626,388 |
| Current portion of long-term debts (Note 12) | **8,960,854** | 6,988,449 |
| Current portion of due to related parties (Note 14) | **49,913,392** | 37,018,854 |
| Other current liabilities | **25,835,442** | 21,638,888 |
| **Total Current Liabilities (Carried Forward)** | **471,719,453** | 458,455,597 |

| | June 30, 2013 | December 31, 2012 (As Restated- Notes 2 and 25) |
|---|---|---|
| **Total Current Liabilities (Brought Forward)** | **₱471,719,453** | ₱458,455,597 |
| **Noncurrent Liabilities** | | |
| Deposit liabilities - net of current portion | **20,898,768** | 24,805,196 |
| Financial liabilities at fair value through profit or loss | **–** | 6,196,070 |
| Bills and acceptances payable | **–** | 328,654 |
| Long-term debts - net of current portion (Note 12) | **7,440,020** | 13,359,510 |
| Due to related parties | **221,395** | – |
| Accrued retirement benefits (Note 15) | **947,728** | 855,818 |
| Deferred income tax liabilities (Note 19) | **1,486,442** | 2,312,806 |
| Other noncurrent liabilities | **9,099,264** | 7,216,494 |
| **Total Noncurrent Liabilities** | **40,093,617** | 55,074,548 |
| **Total Liabilities** | **511,813,070** | 513,530,145 |
| **Equity** | | |
| Attributable to equity holders of the parent company (Notes 1, 20, and 25): | | |
| Capital stock | **10,821,389** | 8,981,389 |
| Capital in excess of par | **35,920,636** | 1,173,772 |
| Other equity components | **25,903,848** | 15,676,536 |
| Retained earnings | **41,692,339** | 36,940,311 |
| | **114,338,212** | 62,772,008 |
| Non-controlling interests (Notes 20 and 25) | **41,462,512** | 37,923,791 |
| **Total Equity** | **155,800,724** | 100,695,799 |
| **TOTAL LIABILITIES AND EQUITY** | **₱667,613,794** | ₱614,225,944 |

*See accompanying Notes to Interim Consolidated Financial Statements.*

# LT GROUP, INC.
## [Formerly Tanduay Holdings, Inc.
## (a Subsidiary of Tangent Holdings Corporation)]
# AND SUBSIDIARIES

# INTERIM CONSOLIDATED STATEMENTS OF INCOME
## (Amounts in Thousands, Except for Basic/Diluted Earnings Per Share)

| | **Six Months Ended June 30** | | For the Quarter Ending June 30 | |
|---|---|---|---|---|
| | **2013** | 2012 | 2013 | 2012 |
| **REVENUE** (Notes 3 and 16) | | | | |
| Banking | **₱18,484,258** | ₱15,483,673 | ₱8,173,349 | ₱7,028,498 |
| Beverage | **6,169,090** | 6,909,707 | 3,080,249 | 3,082,507 |
| Distilled spirits | **4,882,726** | 5,765,177 | 1,914,624 | 3,060,652 |
| Tobacco (Notes 1 and 9) | **157,209** | 1,241,085 | – | 597,133 |
| Property development | **2,154,174** | 824,816 | 994,340 | 264,585 |
| | **31,847,457** | 30,224,458 | 14,162,562 | 14,033,375 |
| **COST OF SALES** (Notes 3 and 16) | **13,114,755** | 14,694,000 | 5,958,396 | 7,060,265 |
| **GROSS INCOME** | **18,732,702** | 15,530,458 | 8,204,166 | 6,973,110 |
| **EQUITY IN NET EARNINGS OF AN ASSOCIATE** (Note 9) | **2,249,559** | 3,144,343 | 682,843 | 1,630,699 |
| | **20,982,261** | 18,674,801 | 8,887,009 | 8,603,809 |
| **OPERATING EXPENSES** | | | | |
| Selling expenses (Note 17) | **1,389,056** | 1,434,585 | 657,332 | 659,903 |
| General and administrative expenses (Note 18) | **11,187,341** | 11,380,607 | 5,400,778 | 5,274,435 |
| | **12,576,397** | 12,815,192 | 6,058,110 | 5,934,338 |
| **OPERATING INCOME** | **8,405,864** | 5,859,609 | 2,828,899 | 2,669,471 |
| **OTHER INCOME (CHARGES)** | | | | |
| Finance costs (Notes 12 and 13) | **(216,372)** | (324,017) | (98,823) | (161,136) |
| Finance income (Notes 4, 8 and 13) | **122,059** | 78,689 | 108,767 | 6,109 |
| Foreign exchange gains | **701,589** | 665,910 | 738,396 | 302,040 |
| Others - net | **2,264,060** | 1,900,526 | 907,555 | 926,170 |
| | **2,871,336** | 2,321,108 | 1,655,895 | 1,073,183 |
| **INCOME BEFORE INCOME TAX** | **11,277,200** | 8,180,717 | 4,484,794 | 3,742,654 |
| **PROVISION FOR INCOME TAX** (Note 19) | | | | |
| Current | **1,806,471** | 1,215,800 | 811,089 | 479,312 |
| Deferred | **(40,838)** | (100,780) | (37,851) | (24,496) |
| | **1,765,633** | 1,115,020 | 773,238 | 454,816 |
| **NET INCOME** | **₱9,511,567** | ₱7,065,697 | ₱3,711,556 | ₱3,287,838 |
| **Net Income Attributable To:** | | | | |
| Equity holders of the parent company | **₱6,138,807** | ₱5,189,677 | ₱2,371,498 | ₱2,406,874 |
| Non-controlling interests | **3,372,759** | 1,876,021 | 1,340,058 | 880,964 |
| | **₱9,511,566** | ₱7,065,698 | ₱3,711,556 | ₱3,287,838 |
| **Basic/Diluted Earnings Per Share** (Note 21) | **₱0.64** | ₱0.60 | | |

*See accompanying Notes to Interim Consolidated Financial Statements.*

## LT GROUP, INC.
**[Formerly Tanduay Holdings, Inc.**
**(a Subsidiary of Tangent Holdings Corporation)]**
## AND SUBSIDIARIES

## INTERIM CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
**(Amounts in Thousands)**

| | Six Months Ended June 30 | |
|---|---|---|
| | **2013** | 2012 |
| **NET INCOME** | **₱9,511,566** | ₱7,065,698 |
| **OTHER COMPREHENSIVE INCOME** | | |
| Cumulative translation adjustment | **75,108** | 377,828 |
| Net changes in fair value of AFS financial assets, net of deferred income tax effect (Note 8) | **16,745,039** | 5,418,788 |
| Cumulative amount of unrecognized actuarial gains and losses | **1,558,368** | (4,766) |
| | **18,378,515** | 5,791,850 |
| **TOTAL COMPREHENSIVE INCOME** | **₱27,890,081** | ₱12,857,548 |
| **Total Comprehensive Income Attributable To:** | | |
| Equity holders of the parent company | **₱18,000,382** | ₱9,443,727 |
| Non-controlling interests | **9,889,699** | 3,413,821 |
| | **₱27,890,081** | ₱12,857,548 |

*See accompanying Notes to Interim Condensed Consolidated Financial Statements.*

# LT GROUP, INC.
## [Formerly Tanduay Holdings, Inc.
## (a Subsidiary of Tangent Holdings Corporation)]
# AND SUBSIDIARIES

# INTERIM CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
## FOR THE SIX MONTHS ENDED JUNE 30, 2013 AND 2012
### (Amounts in Thousands)

| | Attributable to Equity Holders of the Parent Company (Notes 20 and 25) | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | **Capital Stock** | **Capital in Excess of Par** | **Deposit for Future Stock Subscription** | **Other Equity Components** | **Retained Earnings** | **Treasury Shares** | **Total** | **Non-Controlling Interests (Notes 1 and 25)** | **Total** |
| **BALANCES AT DECEMBER 31, 2011, AS PREVIOUSLY STATED** | **₱3,583,250** | **₱–** | **₱1,639,401** | **₱6,926,626** | **₱23,297,289** | **(₱150,889)** | **₱35,295,677** | **₱4,644,869** | **₱39,940,546** |
| Effect of restatements (Note 25) | – | – | – | 9,507,334 | 12,794,152 | – | 22,301,486 | 28,756,221 | 51,057,707 |
| **BALANCES AT DECEMBER 31, 2011, AS RESTATED** | 3,583,250 | – | 1,639,401 | 16,433,960 | 36,091,441 | (150,889) | 57,597,163 | 33,401,090 | 90,998,253 |
| Net income for the year, as restated | – | – | – | – | 5,189,677 | – | 5,189,677 | 1,876,021 | 7,065,698 |
| Other comprehensive income, as restated | – | – | – | 3,304,920 | – | – | 3,304,920 | 1,537,800 | 4,842,720 |
| Total comprehensive income (loss) for the year, as restated | – | – | – | 3,304,920 | 5,189,677 | – | 8,494,597 | 3,413,821 | 11,908,418 |
| Transfer of portion of revaluation increment on property, plant and equipment realized through depreciation and disposal, as restated | – | – | – | (298,071) | 298,071 | – | – | – | – |
| **BALANCES AT JUNE 30, 2012, AS RESTATED** | **₱3,583,250** | **₱–** | **₱1,639,401** | **₱19,440,809** | **₱41,579,189** | **(₱150,889)** | **₱66,091,760** | **₱36,814,911** | **₱102,906,671** |
| **BALANCES AT DECEMBER 31, 2012, AS PREVIOUSLY STATED** | **₱8,981,389** | **₱1,173,772** | **₱–** | **₱5,263,424** | **₱31,337,931** | **₱–** | **₱46,756,516** | **₱5,853,550** | **₱52,610,066** |
| Effect of restatements (Note 25) | – | – | – | 10,413,112 | 5,602,380 | – | 16,015,492 | 32,070,241 | 48,085,733 |
| **BALANCES AT DECEMBER 31, 2012, AS RESTATED** | 8,981,389 | 1,173,772 | – | 15,676,536 | 36,940,311 | – | 62,772,009 | 37,923,791 | 100,695,799 |
| Net income for the year, as restated | – | – | – | – | 6,138,807 | – | 6,138,807 | 3,372,759 | 9,511,566 |
| Other comprehensive income, as restated | – | – | – | 10,987,521 | – | | 10,987,521 | 165,962 | 11,153,483 |
| Total comprehensive income for the year, as restated | – | – | – | 10,987,521 | 6,138,807 | – | 17,126,328 | 3,538,721 | 20,665,049 |
| Issuance of capital stock | 1,840,000 | 34,746,864 | – | – | – | – | 36,586,864 | – | 36,586,864 |
| Declaration of dividends | – | – | – | – | (1,684,850) | – | (1,684,850) | – | (1,684,850) |
| Transfer of portion of revaluation increment on property, plant and equipment realized through depreciation and disposal | – | – | – | (298,701) | 298,071 | – | – | – | – |
| Acquisition of shares of subsidiaries from noncontrolling shareholders | – | – | – | (462,140) | – | – | (462,140) | – | (462,140) |
| **BALANCES AT JUNE 30, 2013, AS RESTATED** | **₱10,821,389** | **₱35,920,636** | **₱–** | **₱25,903,848** | **₱41,692,339** | **₱–** | **₱114,338,212** | **₱41,462,512** | **₱155,800,724** |

*See accompanying Notes to Interim Condensed Consolidated Financial Statements.*

## LT GROUP, INC.
**[Formerly Tanduay Holdings, Inc.**
**(a Subsidiary of Tangent Holdings Corporation)]**
## AND SUBSIDIARIES

## INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS
**(Amounts in Thousands)**

| | Six Months Ended June 30 | |
|---|---|---|
| | **2013** | 2012 |
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | |
| Income before income tax | **₱11,277,199** | ₱8,180,717 |
| Adjustments for: | | |
| Depreciation and amortization (Notes 11, 12 and 13) | **1,759,625** | 1,744,385 |
| Provision for doubtful accounts | **793,420** | 1,017,849 |
| Gain on disposal of: | | |
| Property and equipment | **(251,403)** | (292,296) |
| Investment properties | **(290,505)** | – |
| Equity in net earnings of an associate (Note 10) | **(2,249,559)** | (3,144,343) |
| Finance costs (Notes 17 and 18) | **216,372** | 324,017 |
| Finance income (Notes 5 and 6) | **(122,059)** | (78,689) |
| Unrealized foreign exchange gain | **(701,589)** | (665,910) |
| Operating income before changes in working capital | **10,431,501** | 7,085,730 |
| Decrease (increase) in: | | |
| Financial assets at fair value through profit or loss | **1,881,487** | (1,088,001) |
| Receivables-net | **10,483,501** | (28,224,605) |
| Inventories | **1,374,571** | (272,517) |
| Derivative assets | **–** | 198,273 |
| Other current assets and noncurrent assets | **(2,425,894)** | (385,166) |
| Increase (decrease) in: | | |
| Accounts payable and other liabilities | **4,237,130** | (12,059,261) |
| Customers' deposits | **245,648** | (352,135) |
| Financial liabilities at fair value through profit or loss | **(1,270,932)** | (2,478) |
| Other liabilities | **6,079,324** | 1,457,876 |
| Deposit liabilities | **(1,606,978)** | (7,264,216) |
| Interest received | **122,059** | 78,689 |
| Income taxes paid, including creditable withholding and final taxes | **(1,398,400)** | (1,089,833) |
| Dividends received from associate | **2,036,503** | 2,046,212 |
| Net cash from (used in) operating activities | **30,189,520** | (39,871,432) |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | |
| Net proceeds from sale (acquisition of): | | |
| AFS financial assets (Note 9) | **(771,249)** | 10,316,624 |
| Property, plant and equipment (Note 11) | **(1,756,089)** | (40,934) |
| Investment properties (Note 12) | **(294,795)** | (3,543,412) |
| Advances received from affiliates (Note 18) | **–** | 3,710,674 |
| Other noncurrent assets | **–** | (1,843,204) |
| Net cash from (used in) investing activities | **(2,822,133)** | 8,599,748 |

(Forward)

| | Six Months Ended June 30 | |
|---|---|---|
| | **2013** | 2012 |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | |
| Proceeds from (payments of) bill and acceptance payable | **(₱10,538,387)** | ₱154,007 |
| Proceeds from issuance of shares | **36,586,864** | 1,295,000 |
| Advances from affiliates | **–** | 16,690,570 |
| Payment of short term debts | **(6,117,306)** | (1,771,648) |
| Proceeds from long term debts | **300,221** | 5,384,593 |
| Finance cost | **(216,372)** | (324,017) |
| Deposit for future subscription | **–** | (1,395,016) |
| Net cash from financing activities | **20,015,020** | 20,033,489 |
| **EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS** | **701,589** | 665,910 |
| **NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS** | **48,083,996** | (10,572,285) |
| **CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR** | **124,214,998** | 132,520,686 |
| **CASH AND CASH EQUIVALENTS AT END OF YEAR** (Note 5) | **₱172,298,994** | ₱121,948,401 |

*See accompanying Notes to Interim Consolidated Financial Statements.*

## LT GROUP, INC.
**[Formerly Tanduay Holdings, Inc.**
**(a Subsidiary of Tangent Holdings Corporation)]**
## AND SUBSIDIARIES

## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. **Corporate Information, Corporate Restructuring, and Authorization for Issue of the Interim Consolidated Financial Statements**

Corporate Information

LT Group, Inc. [formerly Tanduay Holdings, Inc. (THI); referred to as "LTG" or the "Company"] was incorporated in the Philippines and registered with the Philippine Securities and Exchange Commission (SEC) on May 25, 1937 under the name "The Manila Wine Merchants, Inc." to engage in the trading business. On November 17, 1947, the Company's shares of stock were listed in the Philippine Stock Exchange (PSE). The Company's corporate life is 50 years from the date of incorporation and was extended for another 50 years from and after May 27, 1987. On September 22, 1995, the Philippine SEC approved the change in Company's name to "Asian Pacific Equity Corporation" and the change in its primary purpose to that of a holding company. On July 30, 1999, the Company acquired Twin Ace Holdings Corp., now known as Tanduay Distillers, Inc. (TDI), a producer of distilled spirits, through a share swap with Tangent Holdings Corporation (Tangent). The share swap resulted in THI wholly owning TDI and Tangent increasing its ownership in THI to 97.0%. On November 10, 1999, the Philippine SEC approved the change in the Company's corporate name from "Asian Pacific Equity Corporation" to "Tanduay Holdings, Inc". On September 24, 2012, THI's stockholders approved the amendment in its Articles of Incorporation and By-Laws to reflect the change in its corporate name from "Tanduay Holdings, Inc." to "LT Group, Inc." which was approved by the Philippine SEC on September 28, 2012. The Company's primary purpose is to engage in the acquisition by purchase, exchange, assignment, gift or otherwise; and to hold, own and use for investment or otherwise; and to sell, assign, transfer, exchange, lease, let, develop, mortgage, enjoy and dispose of, any and all properties of every kind and description and wherever situated, as to and to the extent permitted by law.

After a series of restructuring activities in 2012 and 2013, LTG has expanded and diversified its investments to include the beverages, tobacco, property development and banking businesses, all belonging to Mr. Lucio C. Tan and his family and assignees (collectively referred to as the "Controlling Shareholders"). These business segments in which LTG and subsidiaries (collectively referred to as "the Group") operate are described in Note 3 to the interim condensed consolidated financial statements.

As of June 30, 2013 and December 31, 2012, LTG is 74.36%-owned by its ultimate parent company, Tangent, which is also incorporated in the Philippines, As of June 30, 2013 and December 31, 2012, respectively.

The official business address of the head office is 11th Floor, Unit 3 Bench Tower, 30th St. Corner Rizal Drive Crescent Park West 5 Bonifacio Global City, Taguig City.

*Capital Raising of LTG*

On October 26, 2011, LTG's BOD approved a capital raising exercise via the 2-tranche Placing and Subscription Transaction involving (i) the sale by Tangent of 398,138,889 shares in LTG to the public at an offer price of ₱4.22 each (the "Placing Tranche") and (ii) the subscription at a price equivalent to the offer price offered to the public at the Placing Tranche, as maybe adjusted to account for the expenses of the Placing Tranche (the "Subscription Tranche").

The capital raising exercise is intended to fund LTG's expansion of its distilled spirits segment's plant capacity, increase in operational efficiency and rationalization of operations, and at the same time offer the investing public the opportunity to participate in LTG's growth. In December 2011, Tangent sold the said shares, thereby reducing its ownership interest in LTG from 97% to 86%. In accordance with the Subscription Tranche, Tangent agreed to subscribe to 398,138,889 new common shares from LTG's unissued capital stock for a total consideration of ₱1,639.4 million. On May 2, 2012, LTG's BOD and stockholders approved the conversion of the deposit for future stock subscription into issued common shares of LTG, which resulted to an increased ownership of Tangent in LTG, from 86% to 87% as of that date.

On July 27, 2012, LTG's BOD and stockholders approved the amendments in the Articles of Incorporation to reflect the increase in LTG's authorized capital stock from ₱5.0 billion divided into 5,000,000,000 shares with a par value of ₱1.00 per share to ₱25.0 billion divided into 25,000,000,000 shares with a par value of ₱1.00 per share. On the same date, LTG's BOD and stockholders also approved the issuance of 5,000,000,000 shares to Tangent in support of the increase in authorized capital stock and the waiver of rights/public offering in relation to the said shares to be issued to Tangent. On September 28, 2012, upon approval by the SEC of the increase in authorized capital stock, Tangent increased its ownership interest to 95.25%.

In December 2012, Tangent sold 508,544,100 shares to the public, thus, decreasing its ownership interest to 89.59% as of December 31, 2012.

In April 2013, Tangent sold 1.84 million shares to the public and agreed to subsidiaries to the same number of shares newly issued by LTG. The entire proceeds from the sale of LTG's shares was used by Tangent as payment for the subscription to new shares amounting to ₱36.6 billion, net of stock issuance costs (see note 20). As a result of the planning and subscription transaction, Tangent ownership in LTG decreased to 74.36%.

On September 24, 2012, LTG's stockholders approved the 2-tranche Placement and Subscription Transaction involving the sale by Tangent of up to, but not exceeding 3,000,000,000 common shares of LTG registered in its name to investors by way of a follow-on offering at a placing price to be determined through a book building exercise to be hereafter conducted (the "Placing Tranche") and the subsequent subscription by Tangent using the proceeds of the Placing Tranche (net of expenses incurred in the Placing Tranche) to new shares of LTG in an amount equivalent to the number of shares sold during the Placing Tranche at an issue price equivalent to the placing price (the "Subscription Tranche"). The total number of the shares subject of the Placing Tranche shall be determined based on investor demand as determined through a book building exercise, provided the same shall not exceed 3,000,000,000 shares and the total number of subscription shares shall not exceed the shares sold in the Placing Tranche. The BOD was granted authority to determine such other terms and conditions of the transaction as may be most beneficial to LTG, including (but not limited to) the timing of the same and total funds to be raised therefrom. Further, the subscription shares shall be listed with the PSE.

Corporate Restructuring

*Consolidation of Businesses under LTG*

In preparation for, and prior to the completion of the capital raising exercise approved by the stockholders on September 24, 2012 as discussed above, the Group has undergone certain transactions to transfer certain businesses of the Controlling Shareholders to LTG. This restructuring exercise was approved by LTG's BOD on July 31, 2012. In support of LTG's restructuring activities, Tangent contributed cash amounting to ₱5.0 billion in exchange for LTG's 5,000,000,000 common shares.

The significant transactions that occurred as of December 31, 2012 are as follows:

a. Consolidation of the beverage business and acquisition of Asia Brewery, Incorporated (ABI)

   On May 24, 2012, ABI's BOD approved the subscription to 400,000,000 shares of Interbev Philippines, Inc. (Interbev) at ₱1.00 par value per share by way of conversion of ABI advances to equity investment in Interbev. On the same date, ABI's BOD approved the acquisition of 125,000,000 shares of Packageworld, Inc. (Packageworld) at ₱1.00 par value per share through cash infusion. Effective June 29, 2012, upon approval by the Philippine SEC of Interbev's and Packageworld's application for the increase in capital stock, ABI became a stockholder of Interbev and Packageworld with 80.0% and 33.3% ownership interests, respectively. On June 24, 2012 and July 19, 2012, ABI's BOD approved the resolutions to buy out 100.0% of the outstanding shares of Waterich Resources Corporation (Waterich) and the remaining ownership interests in Interbev and Packageworld owned by the Controlling Shareholders, respectively. To effect the buyout transactions, ABI and the Controlling Shareholders executed the deeds of sale of shares of Waterich on June 24, 2012 and the deeds of assignment of ABI's advances to Packageworld and Interbev on July 25, 2012. Thus, Waterich, Interbev and Packageworld became wholly-owned subsidiaries of ABI.

   On July 19, 2012, ABI's BOD authorized ABI to issue 800,000,000 shares to LTG from its authorized but unissued capital stock and 1,000,000,000 shares from the proposed increase in its authorized capital stock with par value of ₱1.00 per share. In August 2012, ABI issued the remaining authorized but unissued capital stock to LTG, thus, making ABI an 80.0%-owned subsidiary. On October 10, 2012, SEC approved ABI's application to increase its authorized capital stock, thus, increasing LTG's ownership interest in ABI to 90.0%. In December 2012, LTG acquired the shares of ABI which are owned by Shareholdings, Inc. (Shareholdings), a company belonging to the Controlling Shareholders, and certain stockholders, thus, increasing LTG's ownership interest in ABI to 99.99%.

b. Acquisition of Fortune Tobacco Corporation (FTC)

   On July 31, 2012, LTG's BOD approved the acquisition of at least 83.0% of FTC through a cash subscription to 1,646,489,828 shares at its par value of ₱1.00 per share. FTC has 49.6% ownership in PMFTC, Inc. (PMFTC), a company incorporated and domiciled in the Philippines which operates the combined businesses contributed by FTC and Philip Morris Philippines Manufacturing, Inc. (PMPMI) (see Note 10).

   On September 26, 2012, LTG subscribed to 346,489,828 new shares of FTC with a par value of ₱1.00 per share, which was paid in cash by LTG in the amount of ₱346.5 million resulting in 49.5% interest of LTG in FTC.

   On September 28, 2012, LTG subscribed in cash an additional 1,300,000,000 common shares of FTC with a par value of ₱1.00 per share, which was issued to LTG on October 10, 2012 upon approval of the Philippine SEC of FTC's application to increase its authorized capital stock. Thus, LTG increased its direct ownership interest in FTC to 82.32% while diluting ownership interest of Shareholdings in FTC from 98.0% to 17.33%.

   On October 30, 2012, LTG's BOD approved the acquisition of up to 100% of equity interests in FTC.

c. Acquisition of Eton Properties Philippines, Inc. (Eton)

Prior to restructuring in 2012, Paramount Landequities, Inc. (Paramount) and Saturn Holdings, Inc. (Saturn) have ownership interest of 55.07% and 42.39%, respectively, in Eton, a listed company incorporated and registered with the Philippine SEC and is primarily engaged in real estate development.

On September 17, 2012, LTG's BOD approved the assumption by LTG of certain liabilities of Paramount from Step Dragon Co. Ltd. and Billinge Investments Ltd., BVI-based companies, and Saturn from Penick Group Ltd., also a BVI-based company, amounting to ₱1,350.8 million and ₱521.3 million, respectively.

On September 25 and September 26, 2012, LTG subscribed to 1,350,819,487 common shares of Paramount and 490,000,000 common shares of Saturn, respectively, with a par value of ₱1.00 per share and will be issued to LTG out of an increase in Paramount's and Saturn's authorized capital stock. LTG paid the subscription in full by way of conversion into equity of LTG's advances to Paramount and Saturn amounting to ₱1,350.8 million and ₱490.0 million, respectively. On the same dates, Paramount and Saturn filed its application for increase in authorized capital with the Philippine SEC in order to accommodate LTG's investment.

Upon SEC's approval on October 10, 2012, Paramount and Saturn became subsidiaries of LTG with 98.18% and 98.99% ownership interests, respectively, thus, giving LTG a 98.0% effective ownership in Eton.

On October 30, 2012, LTG entered into deeds of sale of shares with the Controlling Shareholders of Paramount and Saturn for the remaining issued and outstanding shares of the said companies. Thus, Paramount and Saturn became wholly owned subsidiaries of LTG.

On December 8, 2012, Paramount made a tender offer to buy back shares of Eton traded in the PSE resulting in the increase in its ownership interest from 55.07% to 56.86%, thus, increasing LTG's effective ownership interest in Eton to 99.3%.

On December 21, 2012, the PSE approved the request of Eton to be delisted from the official registry of the stock exchange starting January 2, 2013, thereby suspending the trading of Eton shares by December 26, 2012.

The following transactions happened during the six months ended June 30, 2013:

a. Merger of PNB and Allied Bank

On March 6, 2012, PNB held a Special Stockholders' Meeting approving the amended terms of the Plan of Merger of PNB with Allied Bank. Under the approved amended terms, merger will be effected via a share-for-share exchange with PNB as the surviving entity. PNB will issue to Allied Bank shareholders 130 Parent Company common shares for every Allied Bank common share and 22.763 PNB common shares for every Allied Bank preferred share. As of January 17, 2013, PNB has received all the necessary approvals from SEC and foreign regulatory agencies to effectuate the merger. On February 9, 2013, PNB completed its planned merger with Allied Bank (the merger of PNB and Allied Bank will be referred to herein as "Merged PNB") as approved and confirmed by the Board of Directors of PNB and Allied Bank on January 22 and January 23, 2013, respectively.

The merger of PNB and Allied Bank was accounted for using the pooling of interests method by the Company since both entities are under the common control of Mr. Tan.

b. Acquisition of Bank Holding Companies

On February 11, 2013, LTG's BOD approved the acquisition of indirect ownership interest in the Merged PNB through the investment in the 27 holding companies which have collective ownership interest in the Merged PNB of 59.8% (collectively referred to as "Bank Holding Companies"). LTG's acquisition of the Bank Holding Companies will be effected by way of subscription to the increase in authorized shares of the Bank Holding Companies and acquisition of the Bank Holding Companies' shares owned by the Controlling Shareholders.

In various dates in February and March 2013, upon approval of the SEC for the increase in authorized capital stock of certain Bank Holding Companies, LTG has acquired between 80% to 100% ownership of these Bank Holding Companies. The transactions were consummated through conversion of LTG's advances from the Bank Holding Companies in exchange for the shares acquired. As of June 30, 2013, LTG obtained majority ownership over certain Bank Holding Companies which collectively own direct ownership interest of 45.5% of the Merged PNB. As of August 13, 2013, LTG is currently obtaining the requisite regulatory approval to increase its stake in PNB to 59.8%.

c. Acquisition of FTC's Non-controlling Interest

In September and October 2012, as a result of LTG's subscription to new shares issued by FTC, LTG acquired direct ownership interest in FTC of 82.32% while diluting the ownership interest of Shareholdings in FTC from 98.0% to 17.33%. In February 2013, LTG increased its effective ownership interest in FTC to 99.58% through the following:

- Acquired subscription right to 453,500,000 shares of Shareholdings, which represents 90.7% ownership interest in Shareholdings or equivalent to 15.7% indirect ownership interest in FTC;
- Assumed certain liabilities of Shareholdings from Controlling Shareholders amounting to ₱1.5 billion, which was used as payment for the subscription of 1,500,000,000 out of the unissued capital stock of Shareholdings thereby increasing the ownership interest in Shareholdings to 97.7% (equivalent to 1.2% indirect ownership in FTC);
- Acquired additional 0.34% direct ownership interest in FTC through purchase of FTC's 104,330,633 outstanding shares held by the Controlling Shareholders.

The business combination of LTG and the merged PNB and Allied Bank (merged PNB) and the acquisition of noncontrolling interest in FTC (through Shareholdings) were also accounted for using the pooling of interests method. Thus, the December 31, 2012 comparative financial information were restated to include the accounts of the merged PNB at their carrying values and to present the net assets attributed to the noncontrolling interest in FTC as part of the equity attributable to the Parent Company as if the noncontrolling interest had been acquired at the beginning of the earliest period presented.

Authorization for Issue of the Unaudited Interim Condensed Consolidated Financial Statements

The unaudited interim condensed consolidated financial statements as at June 30, 2013 and December 31, 2012 and for the six months ended June 30, 2013 and 2012 were authorized for issue by the BOD on August 13, 2013.

2. **Summary of Significant Accounting and Financial Reporting Policies**

Basis of Preparation and Statement of Compliance

The unaudited interim condensed consolidated financial statements have been prepared under the historical cost basis, except for AFS financial assets, land and land improvements, plant buildings and building improvements, and machineries and equipment that have been measured at fair value. The unaudited interim condensed consolidated financial statements are presented in Philippine peso (Peso), the functional currency of LTG. All values are rounded to the nearest Peso, except when otherwise indicated.

The interim condensed consolidated financial statements do not include all the information and disclosures required in the annual financial statements, and should be read in conjunction with the Group's annual consolidated financial statements as at and for the year ended December 31, 2012 and the interim condensed consolidated financial statements as at and for the six months ended June 30, 2013.

The Group shall apply the same accounting policies in its interim condensed consolidated financial statements as are applied in its annual consolidated financial statements, except for accounting policy changes made after the date of the most recent annual consolidated financial statements that are to be reflected in the next annual consolidated financial statements. Measurements for interim reporting purposes shall be made on a year-to-year basis.

Basis of Consolidation

The unaudited interim condensed consolidated financial statements include the financial statements of LTG and the following subsidiaries:

| | Percentage of Ownership | | | | |
|---|---|---|---|---|---|
| | June 30 | | | | |
| | **2013** | | 2012* | | Country of |
| Subsidiaries | **Direct** | **Indirect** | **Direct** | **Indirect** | Incorporation |
| **Distilled Spirits** | | | | | |
| TDI and subsidiaries | **100.0** | **–** | 100.0 | – | Philippines |
| Absolut Distillers, Inc. (ADI) | **–** | **95.0** | – | 95.0 | Philippines |
| Asian Alcohol Corporation (AAC) | **–** | **96.0** | – | 96.0 | Philippines |
| Tanduay Brands International, Inc. (TBI) ** | **100.0** | **–** | 100.0 | – | Philippines |
| **Beverages** | | | | – | Philippines |
| ABI and subsidiaries | **99.9** | **–** | 99.9 | – | Philippines |
| Agua Vida Systems, Inc. | **–** | **100.0** | – | 99.9 | Philippines |
| Interbev | **–** | **100.0** | – | 99.9 | Philippines |
| Waterich | **–** | **100.0** | – | 99.9 | Philippines |
| Packageworld | **–** | **100.0** | – | 99.9 | Philippines |
| **Tobacco** | | | | | |
| Shareholdings, Inc. | **97.7** | **–** | 97.7 | – | Philippines |
| FTC | **82.3** | **17.3** | 82.3 | – | Philippines |
| **Property Development** | | | | | |
| Saturn*** | **100.0** | **–** | 100.0 | – | Philippines |
| Paramount and subsidiaries*** | **100.0** | **–** | 100.0 | – | Philippines |
| Eton | **–** | **99.3** | – | 99.3 | Philippines |
| Belton Communities, Inc. (BCI) | **–** | **99.3** | – | 99.3 | Philippines |
| Eton City, Inc. (ECI) | **–** | **99.3** | – | 99.3 | Philippines |
| FirstHomes, Inc. (FHI) | **–** | **99.3** | – | 99.3 | Philippines |
| **Banking** | | | | | |
| Bank Holding Companies (Note 18) | Various | – | Various | – | Various |
| PNB and Subsidiaries**** | – | **45.5** | – | 45.5 | Philippines |
| PNB Capital and Investment Corporation (PNB Capital) | – | **100.0** | – | 100.0 | Philippines |

(Forward)

| Subsidiaries | Percentage of Ownership June 30 2013 Direct | Indirect | 2012* Direct | Indirect | Country of Incorporation |
|---|---|---|---|---|---|
| PNB Forex, Inc. | – | **100.0** | – | 100.0 | Philippines |
| PNB Holdings Corporation (PNB Holdings) | – | **100.0** | – | 100.0 | Philippines |
| General Insurers, Inc. (Gen) | – | **100.0** | – | 100.0 | Philippines |
| PNB Securities, Inc. (PNB Securities) | – | **100.0** | – | 100.0 | Philippines |
| PNB Corporation - Guam | – | **100.0** | – | 100.0 | USA |
| PNB International Investments Corporation (PNB IIC) | – | **100.0** | – | 100.0 | USA |
| PNB Remittance Centers, Inc. | – | **100.0** | – | 100.0 | USA |
| PNB RCI Holding Co. Ltd. | – | **100.0** | – | 100.0 | USA |
| PNB Remittance Co. (Canada) | – | **100.0** | – | 100.0 | Canada |
| PNB Europe PLC | – | **100.0** | – | 100.0 | United Kingdom |
| PNB Global Remittance & Financial Co. (HK) Ltd. (PNB GRF) | – | **100.0** | – | 100.0 | Hong Kong |
| PNB Italy SpA | – | **100.0** | – | 100.0 | Italy |
| Tanzanite Investments (SPV-AMC), Inc. | – | **100.0** | – | 100.0 | Philippines |
| Tau Portfolio Investments (SPV-AMC), Inc. | – | **100.0** | – | 100.0 | Philippines |
| Omicron Asset Portfolio (SPV-AMC), Inc. | – | **100.0** | – | 100.0 | Philippines |
| Japan - PNB Leasing and Finance Corporation (Japan-PNB Leasing)* | – | **90.0** | – | 90.0 | Philippines |
| PNB Equipment Rentals | – | **90.0** | – | 90.0 | Philippines |
| Allied Savings Bank (ASB) | – | **70.0** | – | 70.0 | Philippines |
| Allied Bank Philippines (UK) Plc (ABUK) | – | **70.0** | – | 70.0 | United Kingdom |
| Allied Commercial Bank (ACB) | – | **36.0** | – | 36.0 | People's Republic of China |
| Allied Banking Corporation (Hongkong) Limited (ABCHKL) | – | **36.0** | – | 36.0 | Hong Kong |
| Allied Forex Corporation | – | **70.0** | – | 70.0 | Philippines |
| PNB Life Insurance, Inc. (PLII) | – | **53.0** | – | 53.0 | Philippines |
| Allied Leasing and Finance Corporation (ALFC) | – | **40.0** | – | 40.0 | Philippines |
| Oceanic Holdings (BVI) Ltd. (OHBVI) | – | **19.0** | – | 19.0 | United States of America |

* *Effective percentage of ownership in 2012 was restated to reflect pooling of interest as if the newly acquired subsidiaries have always been combined.*

** *Incorporated on May 6, 2003 to handle the marketing of TDI's products in the export market, TBI has not yet started commercial operations.*

*** *In July 2011, upon approval by the Philippine SEC of the asset-for-share swap which was filed in 2009, Paramount acquired 1.6 billion unissued shares of Eton, which is equivalent to 55.07% ownership interest in Eton. The acquisition resulted to dilution of Saturn and the non-controlling ownership interest in Eton from 94.4% and 5.6% as of December 31, 2010 to 42.39% and 2.54% as of December 31, 2011, respectively.*

**** *Represents the effective ownership interest of LTG through the collective ownership of the Bank Holding Companies in the merged PNB. Subsidiaries of Merged PNB pertain to the 18 subsidiaries of PNB and Allied Bank, respectively, prior to the merger.*

Subsidiaries are entities over which an entity within the Group has the power to govern the financial and operating policies of the entities, or generally have an interest of more than one-half of the voting rights of the entities. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether an entity within the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. Control is achieved where an entity within the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. They are deconsolidated from the date on which control ceases. A change in the ownership interest of a subsidiary, without loss of control, is accounted for as an equity transaction.

The interim consolidated financial statements are prepared using uniform accounting policies for like transactions and other events in similar circumstances. Adjustments, where necessary, are made to ensure consistency with the policies adopted by the Group.

Inter-company transactions, balances and unrealized gains on transactions between group companies are eliminated. Unrealized losses are also eliminated but are considered as an impairment indicator of the assets transferred.

*Non-controlling interest*
Non-controlling interest represents equity in a subsidiary not attributable, directly or indirectly, to the equity holders of LTG and subsidiaries. Non-controlling interest represents the portion of profit or loss and the net assets not held by the Group. Transactions with non-controlling interest are accounted for as equity transaction.

Non-controlling interest shares in losses even if the losses exceed the non-controlling equity interest in the subsidiary.

If the Group loses control over a subsidiary, it derecognizes assets (including goodwill) and liabilities of the subsidiary, the carrying amount of any non-controlling interest and the cumulative translation differences recorded in equity; recognizes the fair value of the consideration received, any investment retained, and any surplus or deficit in profit or loss; and reclassifies the parent's share of components previously recognized in other comprehensive income to profit or loss or retained earnings, as appropriate.

<u>Business Combination and Goodwill</u>
Business combinations are accounted for using the acquisition method. As of the acquisition date, the acquirer shall recognize, separately from goodwill, the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value, and the amount of any non-controlling interest in the acquiree. For each business combination, the acquirer has the option to measure the non-controlling interest in the acquiree either at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition-related costs are expensed as incurred.

When a business is acquired, the financial assets and financial liabilities assumed are assessed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value as at the acquisition date through profit or loss.

Any contingent consideration to be transferred by the acquirer will be recognized at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration which is deemed to be an asset or liability will be recognized in accordance with PAS 39 either in profit or loss or as a charge to other comprehensive income. If the contingent consideration is classified as equity, it shall not be remeasured until it is finally settled within equity.

Goodwill is initially measured at cost being the excess of the aggregate of the consideration transferred and the amount recognized for non-controlling interest over the fair values of net identifiable assets acquired and liabilities assumed. If this consideration is lower than the fair value of the net assets of the subsidiary acquired, the difference is recognized in profit or loss.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. 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 (CGU) that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units.

Where goodwill forms part of a CGU and part of the operation within that unit is disposed of, 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 of and the portion of the CGU retained.

A CGU to which goodwill has been allocated shall be tested for impairment annually, and whenever there is an indication that the unit may be impaired, by comparing the carrying amount of the unit, including the goodwill, with the recoverable amount of the unit. If the recoverable amount of the unit exceeds the carrying amount of the unit, the unit and the goodwill allocated to that unit shall be regarded as not impaired. If the carrying amount of the unit exceeds the recoverable amount of the unit, the Group shall recognize the impairment loss. Impairment losses relating to goodwill cannot be reversed in subsequent periods.

The Group performs its impairment test of goodwill on an annual basis every December 31 or earlier whenever events or changes in circumstances indicate that goodwill may be impaired.

*Common control business combinations*
Where there are business combinations in which all the combining entities within the Group are ultimately controlled by the same ultimate parent (i.e., Controlling Shareholders) before and after the business combination and that the control is not transitory ("business combinations under common control"), the Group accounts such business combinations similar to a pooling of interests. The assets and liabilities of the acquired entities and that of the Group are reflected at their carrying values. The difference in the amount recognized and the fair value of the consideration given, is accounted for as an equity transaction, i.e., as either a contribution or distribution of equity. Further, when a subsidiary is disposed in a common control transaction, the difference in the amount recognized and the fair value consideration received, is also accounted for as an equity transaction. The Group recorded the difference as other equity reserves and presented as separate component of equity in the consolidated balance sheets. Comparatives shall be restated to include balances and transactions as if the entities had been acquired at the beginning of the earliest period presented as if the companies had always been combined.

Changes in Accounting Policies and Disclosures

The accounting policies adopted in the preparation of the interim consolidated financial statements are consistent with those followed in the preparation of the Group's annual consolidated financial statements for the year ended December 31, 2012, except for the adoption of new standards and interpretations effective as of January 1, 2013.

The Group applies, for the first time, certain standards and amendments that require restatement of previous financial statements. These include PFRS 10, *Consolidated Financial Statements*, PFRS 11, *Joint Arrangements*, PAS 19 (Revised 2011), *Employee Benefits*, PFRS 13, *Fair Value Measurement* and amendments to PAS 1, *Presentation of Financial Statements*. As required by PAS 34, the nature and the effect of these changes are disclosed below. In addition, the application of PFRS 12, *Disclosure of Interest in Other Entities* would result in additional disclosures in the annual consolidated financial statements.

Several other new standards and amendments apply for the first time in 2013. However, they do not impact the annual consolidated financial statements of the Group or the interim consolidated financial statements of the Group.

The nature and the impact of each new standard/amendment are described below:

- PAS 1, *Presentation of Items of Other Comprehensive Income - Amendments to PAS 1*, introduces a grouping of items presented in other comprehensive income (OCI). Items that could be reclassified (or recycled) to profit or loss at a future point in time (e.g., net gain on hedge of net investment, exchange differences on translation of foreign operations, net movement on cash flow hedges and net loss or gain on available-for-sale financial assets) now have to be presented separately from items that will never be reclassified (e.g., actuarial gains and losses on defined benefit plans and revaluation of land and buildings). The amendment affected presentation only and had no impact on the Group's financial position or performance.

- PAS 1, *Clarification of the Requirement for Comparative Information (Amendment)*, clarifies the difference between voluntary additional comparative information and the minimum required comparative information. An entity must include comparative information in the related notes to the financial statements when it voluntarily provides comparative information beyond the minimum required comparative period. The additional voluntarily comparative information does not need to be presented in a complete set of financial statements.

  An opening balance sheet (known as the 'third balance sheet') must be presented when an entity applies an accounting policy retrospectively, makes retrospective restatements, or reclassifies items in its financial statements, provided any of those changes has a material effect on the balance sheet at the beginning of the preceding period. The amendment clarifies that a third balance sheet does not have to be accompanied by comparative information in the related notes. Under PAS 34, the minimum items required for interim consolidated financial statements do not include a third balance sheet.

- PAS 32, *Tax Effects of Distributions to Holders of Equity Instruments (Amendment) - Amendment to PAS 32, Financial Instruments: Presentation* clarifies that income taxes arising from distributions to equity holders are accounted for in accordance with PAS 12 *Income Taxes*. The amendment removes existing income tax requirements from PAS 32 and requires entities to apply the requirements in PAS 12 to any income tax arising from distributions to equity holders. The amendment did not have an impact on the interim consolidated financial statements for the Group, as there is no tax consequences attached to cash or non-cash distribution.

- PAS 34, *Interim Financial Reporting and Segment Information for Total assets and Liabilities (Amendment),* clarifies the requirements in PAS 34 relating to segment information for total assets and liabilities for each reportable segment to enhance consistency with the requirements in PFRS 8, *Operating Segments*. Total assets and liabilities for a reportable segment need to be disclosed only when the amounts are regularly provided to the chief operating decision maker and there has been a material change in the total amount disclosed in the entity's previous annual consolidated financial statements for that reportable segment. The Group provides this disclosure as total segment assets were reported to the chief operating decision maker (CODM). As a result of this amendment, the Group now also includes disclosure of total segment liabilities as these are reported to the CODM (See Note 4).

- PAS 19, *Employee Benefits (Revised 2011) (PAS 19R),* includes a number of amendments to the accounting for defined benefit plans, including actuarial gains and losses that are now recognized in other comprehensive income (OCI) and permanently excluded from profit and loss; expected returns on plan assets that are no longer recognized in profit or loss, instead, there is a requirement to recognize interest on the net defined benefit liability (asset) in profit or loss, calculated using the discount rate used to measure the defined benefit obligation, and; unvested past service costs are now recognized in profit or loss at the earlier of when the amendment occurs or when the related restructuring or termination costs are recognized. Other amendments include new disclosures, such as, quantitative sensitivity disclosures.

  In case of the Group, the transition to PAS 19R had an impact on the net defined benefit plan obligations due to the difference in accounting for interest on plan assets and unvested past service costs. The Group obtained services of actuaries to compute the impact of this standard upon its adoption. The December 31, 2012 consolidated balance sheets and June 30, 2012 interim consolidated statement of income were restated to include the impact of the adoption of PAS 19R (see Note 25).

- PFRS 7, *Financial Instruments: Disclosures - Offsetting Financial Assets and Financial Liabilities - Amendments to IFRS 7*, requires an entity to disclose information about rights to set-off financial instruments and related arrangements (e.g., collateral agreements). The disclosures would provide users with information that is useful in evaluating the effect of netting arrangements on an entity's financial position. The new disclosures are required for all recognized financial instruments that are set off in accordance with PAS 32. The disclosures also apply to recognized financial instruments that are subject to an enforceable master netting arrangement or similar agreement, irrespective of whether the financial instruments are set off in accordance with PAS 32.

Required disclosures which the Group retrospectively applied are detailed below:

Financial assets

| June 30, 2013 | | | | | | |
|---|---|---|---|---|---|---|
| | **[a]** | **[b]** | **[c]** | **[d]** | | **[e]** |
| | | | | **Effect of remaining rights of set-off (including rights to set off financial collateral) that do not meet PAS 32 offsetting criteria** | | |
| **Financial assets recognized at end of reporting period by type** | **Gross carrying amounts (before offsetting)** | **Gross amounts offset in accordance with the offsetting criteria** | **Net amount presented in consolidated balance sheets [a-b]** | **Financial instruments** | **Fair value of financial collateral** | **Net exposure [c-d]** |
| Derivative assets | **₱20,000,155** | **₱19,574,108** | **₱426,047** | **₱–** | **₱–** | **₱426,047** |
| Securities held under agreements to resell | **20,120,000** | **–** | **20,120,000** | **–** | **20,273,741** | **–** |
| Total | **₱40,120,155** | **₱19,574,108** | **₱20,546,047** | **₱–** | **₱20,273,741** | **₱426,047** |

| December 31, 2012 | | | | | | |
|---|---|---|---|---|---|---|
| | [a] | [b] | [c] | [d] | | [e] |
| | | | | Effect of remaining rights of set-off (including rights to set off financial collateral) that do not meet PAS 32 offsetting criteria | | |
| Financial assets recognized at end of reporting period by type | Gross carrying amounts (before offsetting) | Gross amounts offset in accordance with the offsetting criteria | Net amount presented in consolidated balance sheets [a-b] | Financial instruments | Fair value of financial collateral | Net exposure [c-d] |
| Derivative assets | ₱13,918,337 | ₱13,526,872 | ₱391,465 | ₱295,260 | ₱– | ₱96,205 |
| Securities held under agreements to resell | 18,300,000 | – | 18,300,000 | – | 18,874,894 | – |
| Total | ₱32,218,337 | ₱13,526,872 | ₱18,691,465 | ₱295,260 | ₱18,874,894 | ₱96,205 |

Financial liabilities

| June 30, 2013 | | | | | | |
|---|---|---|---|---|---|---|
| | **[a]** | **[b]** | **[c]** | **[d]** | | **[e]** |
| | | | | **Effect of remaining rights of set-off (including rights to set off financial collateral) that do not meet PAS 32 offsetting criteria** | | |
| **Financial assets recognized at end of reporting period by type** | **Gross carrying amounts (before offsetting)** | **Gross amounts offset in accordance with the offsetting criteria** | **Net amount presented in consolidated balance sheets [a-b]** | **Financial instruments** | **Fair value of financial collateral** | **Net exposure [c-d]** |
| Derivative liabilities | **₱28,998,463** | **₱28,274,340** | **₱724,123** | **₱–** | **₱–** | **₱724,123** |
| Securities sold under agreements to repurchase** | – | – | – | – | – | – |
| Bills payable | **201,125** | **–** | **201,125** | **–** | **2,524,774** | **–** |
| Total | **₱29,199,588** | **₱28,274,340** | **₱925,248** | **₱–** | **₱2,524,774** | **₱724,123** |

| | December 31, 2012 | | | | | |
|---|---|---|---|---|---|---|
| | [a] | [b] | [c] | [d] | | [e] |
| | | | | Effect of remaining rights of set-off (including rights to set off financial collateral) that do not meet PAS 32 offsetting criteria | | |
| Financial assets recognized at end of reporting period by type | Gross carrying amounts (before offsetting) | Gross amounts offset in accordance with the offsetting criteria | Net amount presented in consolidated balance sheets [a-b] | Financial instruments | Fair value of financial collateral | Net exposure [c-d] |
| Derivative liabilities | ₱12,162,897 | ₱11,879,146 | ₱283,751 | ₱– | ₱– | ₱283,751 |
| Securities sold under agreements to repurchase** | 2,971,471 | – | 2,971,471 | 21,141 | 3,509,709 | – |
| Bills payable | 2,948,934 | – | 2,948,934 | – | 4,756,800 | – |
| Total | ₱18,083,302 | ₱11,879,146 | ₱6,204,156 | ₱21,141 | ₱8,266,509 | ₱283,751 |

*** Included in bills and acceptances payable in the consolidated balance sheets.*

The amounts disclosed in column (d) include those rights to set-off amounts that are only enforceable and exercisable in the event of default, insolvency or bankruptcy. This includes amounts related to financial collateral both received and pledged, whether cash or non-cash collateral, excluding the extent of over-collateralization.

- PFRS 10, *Consolidated Financial Statements* and PAS 27, *Separate Financial Statements*, establish a single control model that applies to all entities including special purpose entities. PFRS 10 replaces the parts of previously existing PAS 27, *Consolidated and Separate Financial Statements* that dealt with consolidated financial statements and SIC-12, *Consolidation - Special Purpose Entities*. PFRS 10 changes the definition of control such that an investor controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. To meet the definition of control in PFRS 10, all three criteria must be met, including: (a) an investor has power over an investee; (b) the investor has exposure, or rights, to variable returns from its involvement with the investee; and (c) the investor has the ability to use its power over the investee to affect the amount of the investor's returns. The Company assessed that all subsidiaries as of December 31, 2012, upon adoption of PFRS 10, will remain to be consolidated and that there are no new consolidated entity as of December 31, 2012 which need to be consolidated in 2013. For the new acquisitions in the period ended June 30, 2013, the Company concluded that PNB, a 45.5% subsidiary, shall be consolidated.

  Before the effectivity of PFRS 10, Opal Portfolio Investment (SPV-AMC) (OPII) is consolidated by the Group based on the provisions of SIC 12. Under SIC 12, control over an SPE may exist even in cases where an entity owns little or none of the SPE's equity, such as when an entity retains majority of the residual risks related to the SPE in order to obtain benefits from its activities. Beginning January 1, 2013, the Group adopted PFRS 10 which supersedes SIC 12. PFRS 10 establishes control as the basis for determining which entities are consolidated in the consolidated financial statements. Based on management's assessment, the Group should no longer consolidate OPII since it failed to demonstrate control over OPII. Thus, the 2012 financial statements were restated to retroactively effect the deconsolidation of Opal in accordance with the transition provision of PFRS 10 (see Note 25).

- PFRS 11, *Joint Arrangements* and PAS 28, *Investment in Associates and Joint Ventures*, replaces PAS 31, *Interests in Joint Ventures* and SIC-13, *Jointly-controlled Entities - Non-monetary contributions by Venturers*. PFRS 11 removes the option t*o account for jointly controlled entities (JCE*s) using proportionate consolidation. Instead, JCEs that meet t*he definition of a joint venture under P*FRS 11 must be accounted for using the equity method. The application of this new standard does not have an impact on the financial position of the

Group since its investments in associates and joint venture is currently accounted for under the equity method.

- PFRS 12, *Disclosure of Interests in Other Entities*, sets out the requirements for disclosures relating to an entity's interests in subsidiaries, joint arrangements, associates and structured entities. None of these disclosure requirements are applicable for interim consolidated financial statements, unless significant events and transactions in the interim period requires that they are provided. Accordingly, the Group has not made such disclosures.

- PFRS 13, *Fair Value Measurement,* establishes a single source of guidance under PFRS for all fair value measurements. PFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under PFRS when fair value is required or permitted. The application of PFRS 13 has not materially impacted the fair value measurements carried out by the Group. PFRS 13 also requires specific disclosures on fair values, some of which replace existing disclosure requirements in other standards, including PFRS 7, *Financial Instruments: Disclosures*. Some of these disclosures are specifically required for financial instruments by PAS 34.16A(j), thereby affecting the interim condensed consolidated financial statements for the period (See Note 22).

In addition to the above-mentioned amendments and new standards, PFRS 1, *First-time Adoption of International Financial Reporting Standards* was amended with effect for reporting periods starting on or after January 1, 2013. The Group is not a first-time adopter of PFRS, therefore, this amendment is not relevant to the Group. The Group has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

New Accounting Standards, Amendments and
Interpretations Effective Subsequent to 2013

The Group will adopt the following standards, amendments and interpretations enumerated below when these become effective. Except as otherwise indicated, the Group does not expect the adoption of these new and amended PFRSs and Philippine Interpretations to have significant impact on its financial statements. The relevant disclosures will be included in the notes to the interim condensed consolidated financial statements when these become effective.

*Effective 2014*

- PAS 32, *Financial Instruments: Presentation - Offsetting Financial Assets and Financial Liabilities*, clarifies the meaning of "currently has a legally enforceable right to set-off" and also the application of the PAS 32 offsetting criteria to settlement systems (such as central clearing house systems) which apply gross settlement mechanisms that are not simultaneous. The amendments to PAS 32 are to be retrospectively applied for annual periods beginning on or after January 1, 2014.

*Effective in 2015*

- PFRS 9, *Financial Instruments - Classification and Measurement*, as issued, reflects the first phase on the replacement of PAS 39 and applies to the classification and measurement of financial assets and liabilities as defined in PAS 39, *Financial Instruments: Recognition and Measurement*. Work on impairment of financial instruments and hedge accounting is still ongoing, with a view to replacing PAS 39 in its entirety. PFRS 9 requires all financial assets to be measured at fair value at initial recognition. A debt financial asset may, if the fair value option (FVO) is not invoked, be subsequently measured at amortized cost if it is held within a business model that has the objective to hold the assets to collect the contractual cash flows and its contractual terms give rise, on specified dates, to cash flows that are solely payments of principal and interest on the principal outstanding. All other debt instruments are subsequently measured at fair value through profit or loss. All equity financial assets are measured at fair value either through other comprehensive income (OCI) or profit or loss. Equity financial assets held for trading must be measured at fair value through profit or loss. For FVO liabilities, the amount of change in the fair value of a liability that is attributable to changes in credit risk must be presented in OCI. The remainder of the change in fair value is presented in profit or loss, unless presentation of the fair value change in respect of the liability's credit risk in OCI would create or enlarge an accounting mismatch in profit or loss. All other PAS 39 classification and measurement requirements for financial liabilities have been carried forward into PFRS 9, including the embedded derivative separation rules and the criteria for using the FVO.

The Group has made an initial high-level evaluation of the impact of the adoption of this standard. The Group decided not to early adopt PFRS 9 for its 2012 reporting ahead of its effectivity date on January 1, 2015 and therefore the consolidated financial statements as of December 31, 2012 do not reflect the impact of the said standard. Based on this evaluation, loans and receivables and other financial liabilities, both carried at amortized cost, will not be significantly affected. Upon adoption, these financial instruments shall continue to be carried at amortized cost, thus, the standard would have no impact to the Group's financial position and performance. Further, the Group's investments in equity securities classified as available-for-sale investments would be affected by the adoption of this standard. These investments shall be carried at fair value either through other comprehensive income or through profit or loss upon adoption of this standard.

The Group shall conduct another impact assessment at the end of the 2013 reporting period using the consolidated financial statements as of and for the year ended December 31, 2012. Given the proposed amendments on PFRS 9 and the status of its other phases, the Group at present, does not plan to early adopt in 2013 financial reporting. It plans to reassess its current position once the phases of PFRS 9 on impairment and hedge accounting become effective.

The Group's decision whether to early adopt PFRS 9 for its 2013 financial reporting will be disclosed in the consolidated financial statements as of and for the year ending December 31, 2013.

*Effectivity to be determined*

- Philippine Interpretation IFRIC 15, *Agreements for the Construction of Real Estate*, covers accounting for revenue and associated expenses by entities that undertake the construction of real estate directly or through subcontractors. This Interpretation requires that revenue on construction of real estate be recognized only upon completion, except when such contract qualifies as construction contract to be accounted for under PAS 11, *Construction Contracts*, or involves rendering of services in which case revenue is recognized based on stage of completion. Contracts involving provision of services with the construction materials and where the risks and reward of ownership are transferred to the buyer on a continuous basis will also be accounted for based on stage of completion. The adoption of this Philippine Interpretation may significantly affect the determination of the revenue from real estate sales and the corresponding costs, and the related contracts receivables, deferred income tax assets and retained earnings accounts. The adoption of this Philippine Interpretation will be accounted for retrospectively, and will result to restatement of prior period financial statements. The Group is currently assessing the impact of this amendment on its financial position or performance.

## 3. **Segment Information**

The Group's 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's identified operating segments classified as business groups, which are consistent with the segments reported to LTG's BOD, its Chief Operating Decision Maker (CODM), are as follows:

- Distilled Spirits, which is involved in manufacturing, compounding, bottling, importing, buying and selling of rum, spirit beverages, and liquor products. The Group conducts its distilled spirits business through TDI and its consolidated subsidiaries.
- Beverage, which is engaged in brewing and soft drinks and bottled water manufacturing in the Philippines. It also operates other plants, which includes commercial glass division and corrugated cartons production facility, to support the requirements of its brewing, bottled water and non-beer products operations. The Group conducts its beverage business through ABI, Interbev, Waterich and Packageworld.
- Tobacco, which is a supplier and manufacturer of cigarettes, casings, tobacco, packaging, labels and filters. The Group conducts its tobacco business through FTC's interest in PMFTC.
- Property Development, which is engaged in ownership, development, leasing and management of residential properties, including but not limited to, all kinds of housing projects, commercial, industrial, urban or other kinds of real property; acquisition, purchasing, development and selling of subdivision lots. The Group conducts its property development business through Eton and its consolidated subsidiaries.
- Banking, as a result of the acquisition of the Merged PNB, the Group reports "Banking Segment" as an additional segment. The Banking Segment provides full range of banking and other financial services to corporate, middle-market and retail customers, the National Government (NG), local government units (LGUs) and government-owned and controlled corporations (GOCCs) and various government agencies, including deposit-taking, lending, bills discounting, foreign exchange dealing, investment banking, fund transfers or remittance servicing and full range of retail banking and trust services.
- Others, consist of various holding companies (LTG, Paramount and Saturn) that provide financing for working capital and capital expenditure requirements of the operating businesses of the Group.

The BOD reviews the operating results of the business units to make decisions on resource allocation and assesses performance. Segment revenue and segment expenses are measured in accordance with PFRS. The presentation and classification of segment revenues and segment expenses are consistent with the consolidated statements of income. Finance costs (including interest expense) and income taxes are managed per business segment.
The Group has only one geographical segment as all of its assets are located in the Philippines. The Group operates and derives principally all of its revenue from domestic operations. Thus, geographical business segment information is not presented.

Further, the measurement of the segments is the same as those described in the summary of significant accounting and financial reporting policies, except for TDI investment properties which are carried at fair value in TDI consolidated financial statements, TDI's investment property is adjusted at the consolidated level to carry it at cost in accordance with the Group's policy. In addition, the business combination involving PNB and Allied Bank were accounted for under purchase method in the books of PNB. This was accounted for under the pooling of interests method by the Company since both banks and the Company are under the common control of Mr.

Tan.

Segment assets are resources owned and segment liabilities are obligations incurred by each of the operating segments excluding intersegment balances which are eliminated.

Segment revenue and expenses are those directly attributable to the segment except that intersegment revenue and expense are eliminated only at the consolidated level. Transfer prices between operating segments are on an arm's length basis in a manner similar to transactions with third parties.

The components of capital expenditures reported to the CODM are the acquisitions of property, plant and equipment during the period.

The segments of the Group have no significant customer which contributes 10% or more of their segment revenues.

The following tables present the information about the Group's operating segments:

For the six months ended June 30, 2013:

| | Banking | Distilled Spirits | Beverage | Tobacco | Property Development | Others | Eliminations and Adjustments | Total |
|---|---|---|---|---|---|---|---|---|
| | | | | | *(In Thousands)* | | | |
| Segment revenue: | | | | | | | | |
| External customers | ₱18,484,258 | ₱4,882,726 | ₱6,169,090 | ₱157,209 | ₱2,154,174 | ₱– | ₱– | ₱31,847,457 |
| Inter-segment | 22,573 | – | 650,331 | – | – | – | (672,904) | – |
| | 18,506,831 | 4,882,726 | 6,819,421 | 157,209 | 2,154,174 | – | (672,904) | 31,847,457 |
| Cost of sales | 3,478,705 | 3,870,471 | 4,812,076 | 154,396 | 1,472,325 | – | (673,217) | 13,114,756 |
| Gross profit | 15,028,126 | 1,012,255 | 2,007,345 | 2,813 | 681,849 | – | 313 | 18,732,701 |
| Equity in net earnings of an associate | – | – | – | 2,249,559 | – | – | – | 2,249,559 |
| | 15,028,126 | 1,012,255 | 2,007,345 | 2,252,372 | 681,849 | – | 313 | 20,982,260 |
| Selling expenses | – | 264,378 | 932,181 | 300 | 192,197 | – | – | 1,389,056 |
| General and administrative expenses | 9,923,192 | 451,566 | 384,846 | 19,299 | 272,469 | 159,969 | (24,000) | 11,187,341 |
| Operating income | 5,104,934 | 296,311 | 690,318 | 2,232,773 | 217,183 | (159,969) | 24,313 | 8,405,863 |
| Finance costs | – | (208,365) | (31,909) | – | (5,599) | – | 29,501 | (216,372) |
| Finance income | – | 5,698 | 755 | 29,146 | 21,372 | 94,903 | (29,814) | 122,059 |
| Foreign exchange gains (losses) | 692,032 | 1,987 | – | 1,075 | (4) | 6,498 | – | 701,589 |
| Other income (charges) | 1,630,648 | (118,136) | 6,465 | 366,155 | 73,823 | 15,267,463 | (14,962,359) | 2,264,060 |
| Income before income tax | 7,427,614 | (22,505) | 665,629 | 2,629,149 | 306,775 | 15,208,895 | (14,938,359) | 11,277,199 |
| Provision for income tax | 1,398,628 | 50,510 | 182,948 | 12,468 | 102,331 | 18,749 | – | 1,765,634 |
| Segment profit | ₱6,028,986 | (₱73,015) | ₱482,681 | ₱2,616,681 | ₱204,444 | ₱15,190,146 | (₱14,938,359) | ₱9,511,565 |

Other financial information of the operating segments as of June 30, 2013 is as follows:

| | Banking | Distilled Spirits | Beverage | Tobacco | Property Development | Others | Eliminations and Adjustments | Total |
|---|---|---|---|---|---|---|---|---|
| | | | | | *(In Thousands)* | | | |
| Assets: | | | | | | | | |
| Current assets | ₱362,442,743 | ₱9,233,176 | ₱6,244,966 | ₱19,932,178 | ₱9,059,621 | ₱92,628,864 | (₱63,251,632) | ₱436,289,916 |
| Noncurrent assets | 184,154,860 | 7,398,455 | 14,738,811 | 16,850,428 | 8,976,631 | 73,069,859 | (56,328,057) | 248,860,987 |
| | ₱546,597,603 | ₱16,631,631 | ₱20,983,777 | ₱36,782,606 | ₱18,036,252 | ₱165,698,723 | (₱119,579,689) | ₱685,150,903 |
| Liabilities: | | | | | | | | |
| Current liabilities | ₱449,719,632 | ₱2,754,437 | ₱12,449,178 | ₱15,478,143 | ₱7,207,275 | ₱63,565,666 | (₱61,917,767) | ₱489,256,564 |
| Noncurrent liabilities | 29,810,832 | 5,645,737 | 1,582,698 | – | 3,887,386 | 527,661 | (1,360,699) | 40,093,615 |
| | ₱479,530,464 | ₱8,400,174 | ₱14,031,876 | ₱15,478,143 | ₱11,094,661 | ₱64,093,327 | (₱63,278,466) | ₱529,350,179 |

The following tables present the information about the Group's operating segments:

For the six months ended June 30, 2012:

| | Banking | Distilled Spirits | Beverage | Tobacco | Property Development | Others | Eliminations and Adjustments | Total |
|---|---|---|---|---|---|---|---|---|
| | | | | | *(In Thousands)* | | | |
| Segment revenue: | | | | | | | | |
| External customers | ₱15,483,673 | ₱5,765,177 | ₱6,909,707 | ₱1,241,085 | ₱824,816 | ₱– | ₱– | ₱30,224,458 |
| Inter-segment | – | – | – | – | – | – | – | – |
| | 15,483,673 | 5,765,177 | 6,909,707 | 1,241,085 | 824,816 | – | | ₱30,224,458 |
| Cost of sales | 3,807,576 | 4,406,012 | 4,864,455 | 1,139,298 | 476,660 | – | – | 14,694,001 |
| Gross profit | 11,676,097 | 1,359,165 | 2,045,252 | 101,787 | 348,156 | – | – | 15,530,457 |
| Equity in net earnings of an associate | – | – | – | 3,144,343 | – | – | – | 3,144,343 |
| | 11,676,097 | 1,359,165 | 2,045,252 | 3,246,130 | 348,156 | – | – | 18,674,800 |
| Selling expenses | – | 293,015 | 957,173 | 300 | 184,097 | – | – | 1,434,585 |
| General and administrative expenses | 10,226,759 | 277,373 | 410,771 | 190,856 | 249,490 | 25,358 | – | 11,380,607 |
| Operating income | 1,449,338 | 788,777 | 677,308 | 3,054,974 | (85,431) | (25,358) | – | 5,859,608 |
| Finance costs | – | (209,603) | (63,828) | – | (50,585) | – | – | (324,016) |
| Finance income | – | 6,581 | 261 | 25,013 | 30,804 | 16,029 | – | 78,688 |
| Foreign exchange gains (losses) | 651,573 | (1,803) | – | 2,919 | 17,448 | (4,227) | – | 665,910 |
| Other income (charges) | 1,779,594 | 15,351 | 8,852 | 5,510 | 67,219 | 24,000 | – | 1,900,526 |
| Income before income tax | 3,880,505 | 599,303 | 622,593 | 3,088,416 | (20,545) | 10,444 | – | 8,180,716 |
| Provision for income tax | 710,038 | 199,266 | 191,551 | – | 12,500 | 1,664 | – | 1,115,019 |
| Segment profit | ₱3,170,467 | ₱400,037 | ₱431,042 | ₱3,088,416 | (₱33,045) | ₱8,780 | ₱– | ₱7,065,697 |

Other financial information of the operating segments as of December 31, 2012 (restated) is as follows:

| | Banking | Distilled Spirits | Beverage | Tobacco | Property Development | Others | Eliminations and Adjustments | Total |
|---|---|---|---|---|---|---|---|---|
| | | | | | *(In Thousands)* | | | |
| Assets: | | | | | | | | |
| Current assets | ₱268,802,881 | ₱9,542,269 | ₱6,570,152 | ₱18,119,568 | ₱10,523,262 | ₱17,739,113 | (₱19,105,997) | ₱312,191,248 |
| Noncurrent assets | 257,557,350 | 6,594,709 | 14,925,326 | 16,521,113 | 7,234,916 | 45,757,754 | (46,556,472) | 302,034,696 |
| | ₱526,360,231 | ₱16,136,978 | ₱21,495,478 | ₱34,640,681 | ₱17,758,178 | ₱63,496,867 | (₱65,662,469) | ₱614,225,944 |
| Liabilities: | | | | | | | | |
| Current liabilities | ₱410,218,562 | ₱2,183,662 | ₱13,387,910 | ₱862,603 | ₱8,456,795 | ₱39,021,423 | (₱15,675,358) | ₱458,455,597 |
| Noncurrent liabilities | 47,929,426 | 5,647,048 | 1,635,686 | – | 2,559,362 | 10,975 | (2,707,949) | 55,074,548 |
| | ₱458,147,988 | ₱7,830,710 | ₱15,023,596 | ₱862,603 | ₱11,016,157 | ₱39,032,398 | (₱18,383,307) | ₱513,530,145 |

## 4. Cash and Cash Equivalents

| | June 30, 2013 | December 31, 2012 |
|---|---|---|
| | *(In Thousands)* | |
| Cash and other cash items | **₱9,257,075** | ₱14,158,519 |
| Cash equivalents | | |
| Due from *Bangko Sentral ng Pilipinas* (BSP) | **119,474,009** | 63,258,002 |
| Due from other banks | **17,208,423** | 10,425,722 |
| Interbank loans receivable and securities purchased resale agreement and Securities held under agreement to resell | **26,359,487** | 36,372,755 |
| | **₱172,298,994** | ₱124,214,998 |

## 5. Loans and Receivables

| | June 30, 2013 | December 31, 2012 |
|---|---|---|
| | *(In Thousands)* | |
| Finance receivables | **₱237,269,508** | ₱248,056,794 |
| Trade receivables | **10,630,964** | 10,907,164 |
| Other receivables | **2,642,589** | 2,913,926 |
| | **250,543,061** | 261,877,884 |
| Noncurrent portion | **(141,200,640)** | (122,410,493) |
| | **₱109,342,421** | ₱139,467,391 |

## 6. Inventories

| | June 30, 2013 | December 31, 2012 |
|---|---|---|
| | *(In Thousands)* | |
| Consumer goods: | | |
| Alcohol | **₱2,499,009** | ₱2,790,260 |
| Beverage | **1,724,512** | 1,516,184 |
| Tobacco (Note 10) | **–** | 153,366 |
| | **4,223,521** | 4,459,810 |
| Real estate inventories | **4,321,600** | 5,495,441 |
| Fuel, Materials and supplies | **1,044,594** | 1,009,035 |
| | **₱9,589,715** | ₱10,964,286 |

7. **Other Current Assets**

| | **June 30, 2013** | December 31, 2012 |
|---|---|---|
| | *(In Thousands)* | |
| Advances to contractors | **₱847,504** | ₱404,594 |
| Creditable withholding tax (CWT) | **591,243** | 465,954 |
| Input VAT | **521,797** | 425,220 |
| Prepaid Commission | **312,684** | 385,402 |
| Prepaid importation charges | **141,566** | 49,413 |
| Excise tax | **115,177** | 157,208 |
| Others | **3,067,342** | 1,559,915 |
| | **₱5,597,313** | ₱3,447,706 |

Others include other prepayments which are individually not significant as to the amounts.

8. **Trading and Investment Securities**

| | **June 30, 2013** | December 31, 2012 |
|---|---|---|
| | *(In Thousands)* | |
| AFS financial assets: | | |
| Government securities | **₱79,438,214** | ₱78,456,034 |
| Other debt securities | **17,261,041** | 17,261,041 |
| Equity securities | | |
| Quoted | **1,923,979** | 1,923,979 |
| Unquoted | **293,224** | 293,224 |
| | **98,916,458** | 97,934,278 |
| Noncurrent portion | **(18,835,304)** | (91,598,467) |
| | **₱80,081,154** | ₱6,335,811 |
| Financial assets at fair value through profit or loss (FVPL): | | |
| Derivative assets | **₱299,759** | ₱148,761 |
| Held for trading | **4,621,395** | 10,002,074 |
| Designated at FVPL | **4,595,950** | 1,247,756 |
| | **₱9,517,104** | ₱11,398,591 |

9. **Investments in Associate and Joint Venture**

The Group has the power to participate in the financial and operating policy decisions in PMFTC, a 49.6%-owned associate, which does not constitute control or joint control. The Group also has 50.0% interest in ABI Pascual Holdings Private Limited (ABI Pascual Holdings), which is a joint controlled entity.

The Group's investments in its associate and joint venture are accounted for using equity method of accounting as follows:

| | **2013** | 2012 |
|---|---|---|
| | *(In Thousands)* | |
| PMFTC | **₱14,157,056** | ₱13,886,098 |
| ABI Pascual Holdings and Others | **25,152** | 25,152 |
| | **₱14,182,208** | ₱13,911,250 |

* *For the period February 25 to December 31, 2010.*

Investment in PMFTC
Details of investment in PMFTC are as follows:

| | December 31 | |
|---|---|---|
| | **2013 (Six Months)** | 2012 (One Year) |
| | *(In Thousands)* | |
| Acquisition cost | **₱13,483,541** | ₱13,483,541 |
| Accumulated equity in net earnings: | | |
| Balance at beginning of period | **402,557** | (1,860,154) |
| Equity in net earnings | **2,249,559** | 6,498,972 |
| Less cash dividends | **(1,978,601)** | (4,236,261) |
| Balance at end of period | **673,515** | 402,557 |
| | **₱14,157,056** | ₱13,886,098 |

Investment in Joint Venture
On February 15, 2012, ABI and Corporation Empresarial Pascual, S. L. (CEP), an entity organized and existing under the laws of Spain, agreed to form ABI Pascual Holdings, a jointly controlled entity organized and domiciled in Singapore. In accordance with the Agreement, ABI and CEP (the "venturers") each will hold 50% interest in ABI Pascual Holdings. Further, the arrangement requires unanimous agreement for financial and operating decisions among venturers.

On November 21, 2012, ABI Pascual Holdings created ABI Pascual Foods Incorporated (ABI Pascual Foods), an operating company, incorporated and domiciled in the Philippines, that will develop a business of marketing and distributing certain agreed products. As part of the joint venture agreement, the venturers also agreed to execute a product distribution agreement.

As of June 30, 2013 and December 31, 2012, ABI has an investment in ABI Pascual Holdings amounting to ₱20.1 million, while ABI Pascual Holdings has an investment in ABI Pascual Foods amounting to ₱40.2 million. As of August 13, 2013, the joint venture has not started operations.

10. **Other Noncurrent Assets**

| | **June 30, 2013** | December 31, 2012 |
|---|---|---|
| | *(In Thousands)* | |
| Deferred input VAT | **₱123,912** | ₱591,050 |
| Goodwill | **163,735** | 163,735 |
| Refundable deposits | **132,474** | 135,190 |
| Software costs | **20,446** | 45,538 |
| Other noncurrent assets | **3,711,627** | 2,487,913 |
| | **₱4,152,194** | ₱3,423,426 |

Others include assets held by SPV, real estate under JV agreements, deferred reinsurance premiums and various assets which are individually not significant.

11. **Accounts Payable and Accrued Expenses**

| | **June 30, 2013** | December 31, 2012 |
|---|---|---|
| | *(In Thousands)* | |
| Accrued expenses | **₱5,229,084** | ₱6,807,952 |
| Trade payables | **2,329,238** | 2,115,158 |
| Retention payable | **640,432** | 746,373 |
| Deposit liability on returnable containers | **387,392** | 612,718 |
| Nontrade payables | **542,663** | 548,487 |
| Output value added tax | **128,235** | 385,519 |
| Other payables | **1,429,040** | 750,967 |
| | **₱10,686,084** | ₱11,967,174 |

12. **Short Term and Long Term Debts**

Short-term Debts
At various dates in 2013 and 2012, the Group obtained unsecured short-term loans from various local banks to meet its working capital requirements. The loans, which are payable in lump sum on various dates, are subject to annual interest rates ranging from 5.0% to 6.0% and 3.5% to 7.0% in 2013 and 2012, respectively. As of June 30, 2013 and December 31, 2012, outstanding short term debts amounted ₱1.87 billion.

Long-term Debts

| | **June 30, 2013** | December 31, 2012 |
|---|---|---|
| | *(In Thousands)* | |
| Bonds payable | **₱4,975,286** | ₱4,968,295 |
| Unsecured term loans and notes payable | **11,410,932** | 15,360,906 |
| Obligation under finance lease | **14,656** | 18,758 |
| | **16,400,874** | 20,347,959 |
| Less current portion | **8,960,854** | 6,988,449 |
| | **₱7,440,020** | ₱13,359,510 |

*TDI's ₱5.0 billion bonds payable*
On November 24, 2009, TDI's and LTG's BOD approved and confirmed the issuance of the retail bonds amounting to ₱5.0 billion due in 2015 at 8.055% per annum, payable quarterly, to be used for general corporate purposes, including debt refinancing. On February 12, 2010, TDI completed the bond offering and issued the Retail Bonds with an aggregate principal amount of ₱5.0 billion, which will mature on February 13, 2015. Bond issue cost incurred amounted to ₱66.7 million. As of December 31, 2012, 2011 and 2010, unamortized bond issue cost amounted to ₱31.7 million, ₱44.9 million and ₱56.9 million, respectively (presented as a reduction from the principal loan balance).

The proceeds from the bond issuance was used to preterminate and fully pay the outstanding balance of TDI's syndicated loan on February 15, 2010 amounting to ₱4.2 billion.

The bond provides that TDI may at any time purchase any of the bonds at any price in the open market or by tender or by contract at any price, without any obligation to purchase bonds pro-rata from all bondholders and the bondholders shall not be obliged to sell. Any bonds so purchased shall be redeemed and cancelled and may not be re-issued.

The bond also provides for certain negative covenants on the part of TDI such as:

- TDI shall not create or suffer to exist any lien, security interest or other charge or encumbrance, upon or with respect to any of its properties, whether now owned or hereafter acquired.
- TDI shall not assign any right to receive income for the purpose of securing any other debt, unless at the same time or prior thereto, its obligations under the bond agreement are forthwith secured equally and ratably therewith.
- TDI shall not have the benefit of such other security as shall not be materially less beneficial to the bondholders.
- TDI shall maintain, based on the most recent audited financial statements prepared in accordance with PFRS, a maximum debt-to-equity ratio of 1.75 times and a minimum current ratio of 2.0 times.

As of June 30, 2013 and December 31, 2012, TDI is compliant with these terms and conditions.

*Unsecured term loans of Eton*
On December 10, 2009, Eton entered into an unsecured term loan agreement with Allied Bank to finance the construction of Eton’s investment properties. The loan amounting to ₱300.00 million bears fixed interest rate of 6.66%. Principal repayments are due annually for at least 10.00% of the total principal amount with final repayment in 2012.

Eton obtained additional loans from Allied Bank on various dates for purposes of financing its working capital requirements totaling to ₱990.0 million in 2010 and ₱1,120.0 million in 2011 with interest rates ranging from 5.18% to 6.57% and 6.0%, respectively. Principal repayments are due annually for at least 5.00% of the total principal amount with final payments due in 2013 and 2014, respectively.

*Notes payable of Eton*
Notes payable include various notes from BDO which arose from assigning Eton’s contracts receivables on a with recourse basis in 2012, 2011 and 2010 (see Note 6). These notes bear interest based on Philippine Dealing System Treasury Fixing rate for one year plus 1.5% net of gross receipts tax, which ranges from 6.00% to 6.66% in 2012 and 2011 and 6.34% to 6.92% in 2010, subject to annual repricing. Interest is due monthly in arrears during the first two years of the term and thereafter, interest shall be collected with the principal covering the term of three years or the term of the contracts to sell, whichever comes first.

Interest on loans payable from general borrowings capitalized as part of investment properties and real estate inventories amounted to ₱77.0 million and ₱10.4 million in 2012. Capitalization rate in 2012 was 5.83%.

## 13. Finance Costs and Finance Income

Details of finance costs and finance income (other than the banking segment) are as follows:

| | Six Months Ended June 30 | |
|---|---|---|
| | **2013** | 2012 |
| | *(In Thousands)* | |
| Finance costs: | | |
| Short-term debts | **₱21,472** | ₱23,952 |
| Long-term debts: | **2,323** | 43,277 |
| Security deposit (Note 29) | **181,217** | 218,178 |
| Others | **11,360** | 38,610 |
| Finance costs | **₱216,372** | ₱324,017 |
| Finance income: | | |
| Cash in banks and cash equivalents | **₱21,288** | ₱56,114 |
| Receivables | **100,771** | 20,815 |
| Due from related parties | **–** | 1,760 |
| | **₱122,059** | ₱78,689 |

## 14. Related Party Transactions

The Company has transacted with its subsidiaries and associates and other related parties as follows:

| **Parent Company, Subsidiaries, Associate and Joint Venture** | **Entities Under Common Control** | |
|---|---|---|
| *Parent Company* | *Other Bank Holding Companies* | *Other Entities Under Common Control* |
| Tangent | All Seasons Realty Corp. [3 | Ascot Holdings, Inc. |
| | Dynaworld Holdings Inc. [(3)] | Pol Holdings, Inc. |
| *Subsidiaries* | Fil-Care Holdings Inc. [(3)] | Sierra Holdings & Equities, Inc. |
| TDI and Subsidiaries | Kentwood Development Corp. [(3)] | Grand Cargo and Warehousing Services., Inc. |
| ADI | La Vida Development Corp. [(3)] | Northern Corporation Tobacco Redrying Co., Inc. |
| AAC | Profound Holdings Inc. [(3)] | Basic Holdings Corporation |
| TBI | Purple Crystal Holdings, Inc. [(3)] | Dominium Realty & Construction Corp |
| ABI and Subsidiaries | Safeway Holdings & Equities Inc. [(3)] | Foremost Farms Inc. |
| Agua Vida | Society Holdings Corp. [(3)] | Grandspan Development Corp. |
| Interbev | Total Holdings Corp. [(3)] | Himmel Industries Inc. |
| Waterich | | Lapu Lapu Packaging |
| Packageworld | | Lucky Travel Corporation |
| Saturn | | Philippine Airlines, Inc. |
| Paramount and Subsidiaries | | Rapid Movers & Forwarders Co. Inc. |
| Eton | | Upright Profits Ltd. |
| Belton | | Dyzum Distillery Inc. |
| Eton City | | Parity Packaging Corp. |
| FirstHomes | | Heritage Holdings Corp. |
| Bank Holding Companies:[(2)] | | Maxell Holdings, Corp. |
| Allmark Holdings Corp. [(2)] | | Networks Holdings & Equities, Inc. |
| Dunmore Development Corp. [(2)] | | Cube Factor Holdings, Inc. |
| Kenrock Holdings Corp. [(2)] | | Trustmark Holdings Corporation |
| Leadway Holdings, Inc. [(2)] | | Polima International Limited |
| Multiple Star Holdings Corp. [(2)] | | Cosmic Holdings Corp. |
| Pioneer Holdings & Equities, Inc.[(2)] | | Negros Biochem Corporation |
| Donfar Management Ltd. [(2)] | | Shareholdings [(3)]. |
| Fast Return Enterprises Ltd. [(2)] | | Grandway Konstruct, Inc. |
| Mavelstone International Ltd. [(2)] | | Harmonic Holdings Corp. |

(Forward)

| Parent Company, Subsidiaries, Associate and Joint Venture | Entities Under Common Control |
|---|---|
| Uttermost Success, Ltd. [(2)] | Proton Realty & Development Corporation |
| Ivory Holdings, Inc. [(2)] | Billinge Investments Limited |
| Merit Holdings & Equities Corp. [(2)] | Step Dragon Co. Limited |
| True Success Profits Ltd. [(2)] | High Above Properties Ltd. |
| Key Landmark Investments Ltd. [(2)] | Penick Group Limited |
| Fragile Touch Investments Ltd. [(2)] | In Shape Group Ltd. |
| Caravan Holdings, Corp. [(2)] | Hibersham Assets Ltd. |
| Solar Holdings Corp. [(2)] | Orient Legend Developments Ltd. |
| PNB and Subsidiaries [(1)] | Complete Best Development Ltd. |
| | Cormack Investments Ltd |
| *Associate* | Link Great International Ltd. |
| PMFTC | Bright Able Holdings Ltd. |
| *Joint Venture* | |
| ABI Pascual Holdings | |
| ABI Pascual Foods | |

[(1)] *As of June 30, 2013, LTG has 45.5% effective ownership interest over the merged PNB (see Note 1).*
[(2)] *In various dates in February and March 2013, LTG acquired these holding companies through subscription of unissued shares of the holding companies.*
[(3)] *Bank holding companies to be acquired by LTG to increase ownership interest in PNB to 59.88%.*

The interim consolidated statements of income include the following revenue and other income-related (costs and other expenses)-related account balances arising from transactions with related parties:

| | Nature | Six Months Ended June 30 | |
|---|---|---|---|
| | | **2013** | 2012 |
| | | *(In Thousands)* | |
| **Associate** | Sales | **₱1,523** | ₱– |
| **Entities Under Common Control** | Sales | **5,220** | 11,316 |
| | Purchases | **(30,288)** | (33,782) |
| | Management and professional fee | **(120,632)** | (218,198) |
| | Shared cost | **(480)** | (508) |
| | Freight and handling | **(2,506)** | (3,086) |
| | Rent | **(12,600)** | (12,600) |
| | Transportation and travel | **(81)** | – |

The consolidated balance sheet includes the following account balances with related parties:

| | Financial Statement Account | Terms and Conditions | June 30, 2013 | December 31, 2012 |
|---|---|---|---|---|
| | | | *(In Thousands)* | |
| **Parent Company** | Due from related parties | On demand; non-interest bearing except for the ₱9.9 million and ₱391.2 million in 2011 and 2010, respectively, which are subject to 10% interest | **₱11,113,148** | ₱5,681,578 |
| | Due to related parties | On demand; non-interest bearing | **(33,481,655)** | (28,407,180) |
| **Stockholders** | Due from related parties | On demand; non-interest bearing | **–** | 1,776,483 |
| | Due to related parties | On demand; non-interest bearing | **(218,386)** | – |
| (Forward) | | | | |

| | Financial Statement Account | Terms and Conditions | June 30, 2013 | December 31, 2012 |
|---|---|---|---|---|
| | | | *(In Thousands)* | |
| Associate | Receivables - net | 30 to 90 days terms; non-interest bearing | **₱1,690** | ₱366,418 |
| | Due from related parties | On demand; non-interest bearing | **310,224** | 2,772 |
| | Account payable and other liabilities | 30 to 90 days terms; non-interest bearing | **–** | (56,152) |
| Entities Under Common Control | Cash and cash equivalents | On demand; earn rates at bank deposit rates | **6,802,038** | 173 |
| | Receivables - net | 30 to 60 days terms; non-interest bearing | **666,975** | 6,513,720 |
| | Due from related parties | On demand; non-interest bearing | **20,902,733** | 8,901,632 |
| | Available-for-sale financial assets | Shares of stocks; no impairment | **255,200** | 1,186,486 |
| | Account payable and other liabilities | 30 to 60 days terms; non-interest bearing | **(537,606)** | (653,842) |
| | Short-term debt | On demand; non-interest bearing | **(250,000)** | – |
| | Due to related parties | On demand; non-interest bearing | **(16,213,351)** | (8,611,674) |
| | Long-term debt | On demand; non-interest bearing | **(500,000)** | – |

** The volume of transactions of the year ended December 31, 2012 are discussed in the annual consolidated financial statements.*

The outstanding related party balances are unsecured and settlement occurs in cash, unless otherwise indicated. The Group has not recorded any impairment of receivables relating to amounts owed by related parties. This assessment is undertaken each financial year through examining the financial position of the related parties and the market in which these related parties operate.

## 15. Retirement Benefits

The Group has funded, noncontributory defined benefit retirement plans, administered by a trustee, covering all of its permanent employees. As of December 31, 2012, 2011 and 2010, the Group is in compliance with Article 287 of the Labor Code, as amended by Republic Act No. 7641. Details of the Group's net retirement plan assets and liabilities are as follows:

| | June 30, 2013 | December 31, 2012 (Restated, Notes and 25) |
|---|---|---|
| | *(In Thousands)* | |
| Net retirement plan assets: | | |
| FTC | **₱1,181,149** | ₱1,206,389 |
| Allied Bank* | **–** | 139,389 |
| AAC | **19,925** | – |
| TDI | **–** | 9,214 |
| | **₱1,201,074** | ₱1,354,992 |

(Forward)

| | June 30, 2013 | December 31, 2012 (Restated, Notes 2 and 25) |
|---|---|---|
| | *(In Thousands)* | |
| Accrued retirement benefits: | | |
| PNB** | **₱4,040,994** | ₱1,386,796 |
| ABI and Subsidiaries | **784,858** | 481,390 |
| Eton | **42,401** | 23,120 |
| TDI | **91,322** | – |
| AAC | – | 16,603 |
| LTG | **10,865** | 8,543 |
| ADI | **18,282** | 4,388 |
| | **₱4,988,722** | ₱1,920,840 |

* *"Includes ₱140.1 million as of December 31, 2012 presented under "Other assets" ₱0.7 million as of December 31, 2012 presented under "Other liabilities.""*
***Presented under "Other noncurrent liabilities."*

The principal assumptions used in determining retirement benefits cost for the Group's plans as of June 30, 2013 and December 31, 2012 are as follows:

| | |
|---|---|
| Discount rates per annum | 5.16% to 6.85% |
| Expected annual rates of return on plan assets | 2.3% to 8.5% |
| Future annual increase in salary | 5.0% to 10.0% |

<u>Transactions with Retirement Plans</u>
Management of the retirement funds of the banking segment is handled by the PNB Trust Banking Group (TBG). As of June 30, 2013 and December 31, 2012, the retirement fund of the Group includes 7,833,795 shares of PNB classified under HFT. No limitations and restrictions are provided and voting rights over these shares are exercised by a trust officer or any of its designated alternate officer of TBG.

As of June 30, 2013 and December 31, 2012, AFS and HTM investments include government and private debt securities and various funds. Deposits with other banks pertain to Special Deposit Accounts (SDA) placement with BSP.

The retirement funds of the other companies in the Group are maintained by PNB, as the trustee bank.

PNB's retirement funds have no investments in debt or equity securities of the companies in the Group.

## 16. Revenue and Cost of Sales

Revenue consists of:

| | Six Months Ended June 30 | |
|---|---|---|
| | **2013** | 2012 |
| | *(In Thousands)* | |
| Sale of consumer goods | **₱11,209,025** | ₱13,915,969 |
| Banking revenue | **18,484,258** | 15,483,673 |
| Real estate sales | **2,154,174** | 824,816 |
| | **₱31,847,457** | ₱30,224,458 |

Banking revenue consists of:

| | Six Months Ended June 30 | |
|---|---|---|
| | **2013** | 2012 |
| | *(In Thousands)* | |
| Interest income | **₱9,557,512** | ₱10,710,029 |
| Trading and securities gains | **7,278,326** | 3,334,090 |
| Service fees and commission income | **1,648,420** | 1,439,554 |
| | **₱18,484,258** | ₱15,483,673 |

Cost of sales consists of:

| | Six Months Ended June 30 | |
|---|---|---|
| | **2013** | 2012 |
| | *(In Thousands)* | |
| Cost of consumer goods sold: | | |
| Materials used and changes in inventories | **₱4,752,102** | ₱6,358,004 |
| Taxes and licenses | **827,796** | 1,234,781 |
| Fuel and power | **486,261** | 653,904 |
| Depreciation and amortization | **662,053** | 605,957 |
| Personnel costs | **583,471** | 601,552 |
| Repairs and maintenance | **210,357** | 202,796 |
| Freight and handling | **95,372** | 135,484 |
| Occupancy | **47,500** | 38,438 |
| Others | **521,699** | 578,848 |
| | **8,186,611** | 10,409,764 |
| Cost of real estate sales | **1,380,747** | 476,660 |
| Cost of rental income | **91,578** | – |
| Cost of banking services | **3,455,819** | 3,807,576 |
| Cost of sales | **₱13,114,755** | ₱14,694,000 |

Other expenses include insurance, utilities and outside services which are not significant as to amounts.

Cost of banking services consist of:

| | Six Months Ended June 30 | |
|---|---|---|
| | **2013** | 2012 |
| | *(In Thousands)* | |
| Interest expense on: | | |
| Deposit liabilities | **₱2,285,072** | ₱2,578,015 |
| Bills payable and other borrowings | **777,624** | 873,422 |
| Services and commission expense | **393,123** | 356,139 |
| | **₱3,455,819** | ₱3,807,576 |

## 17. Selling Expenses

| | Six Months Ended June 30 | |
|---|---|---|
| | **2013** | 2012 |
| | *(In Thousands)* | |
| Advertising and promotions | **₱588,224** | ₱604,085 |
| Depreciation and amortization | **324,493** | 360,423 |
| Personnel costs | **54,699** | 53,159 |
| Materials and consumables | **40,901** | 46,996 |
| Repairs and maintenance | **28,342** | 36,212 |
| Travel and transportation | **22,592** | 21,336 |
| Occupancy | **17,930** | 27,762 |
| Others | **311,875** | 284,612 |
| | **₱1,389,056** | ₱1,434,585 |

Others include occupancy fees, fuel and oil, insurance, donations, membership and subscription dues, which are individually not significant as to amounts.

## 18. General and Administrative Expenses

| | Six Months Ended June 30 | |
|---|---|---|
| | **2013** | 2012 |
| | *(In Thousands)* | |
| Personnel costs | **₱3,568,398** | ₱3,666,576 |
| Taxes and licenses | **1,313,531** | 1,131,329 |
| Depreciation and amortization | **773,079** | 778,005 |
| Occupancy | **699,828** | 699,648 |
| Management, consulting and professional fees | **202,211** | 251,806 |
| Repairs and maintenance | **53,797** | 41,499 |
| Materials and consumables | **44,810** | 35,618 |
| Outside services | **43,083** | 90,282 |
| Communication, light and water | **31,924** | 30,376 |
| Entertainment, amusement and recreations | **19,945** | 4,542 |
| Travel and transportation | **13,384** | 15,308 |
| Insurance | **3,987** | 2,747 |
| Others | **4,419,364** | 4,632,871 |
| | **₱11,187,341** | ₱11,380,607 |

Others include expense items mostly relating to banking operations, which are individually not significant as to amounts.

## 19. Income Taxes

Income taxes include the corporate income tax, discussed below, and final taxes paid which represents final withholding tax on gross interest income from government securities and other deposit substitutes and income from the FCDU transactions. These income taxes, as well as the deferred tax benefits and provisions, are presented as ‘Provision for income tax’ in the statements of income.

Under Philippine tax laws, PNB and its certain subsidiaries are subject to percentage and other taxes (presented as Taxes and Licenses in the statements of income) as well as income taxes. Percentage and other taxes paid consist principally of gross receipts tax and documentary stamp tax.

FCDU offshore income (income from non-residents) is tax-exempt while gross onshore income (income from residents) is generally subject to 10% income tax. In addition, interest income on deposit placement with other FCDUs and offshore banking units (OBUs) is taxed at 7.50%. RA No. 9294 provides that the income derived by the FCDU from foreign currency transactions with non-residents, OBUs, local commercial banks including branches of foreign banks is tax-exempt while interest income on foreign currency loans from residents other than OBUs or other depository banks under the expanded system is subject to 10.00% income tax.

Provision for current income tax consists of:

| | **Six Months Ended June 30** | |
|---|---|---|
| | **2013** | 2012 |
| | *(In Thousands)* | |
| Regular corporate income tax/ minimum corporate income tax | **₱1,786,146** | ₱1,207,587 |
| Final tax | **20,325** | 8,213 |
| Provision for current income tax | **₱1,806,471** | ₱1,215,800 |

20. **Equity**

Capital Stock

Authorized and issued capital stock of the Company are as follows:

| | **June 30, 2013** | December 31, 2012 |
|---|---|---|
| | *(In Thousands)* | |
| *Number of shares* | | |
| Authorized capital stock at ₱1 par value | **25,000,000** | 25,000,000 |
| Issued capital stock at ₱1 par value: | | |
| At beginning of the period | **₱8,981,389** | ₱3,583,250 |
| Issuance | **1,840,000** | 5,398,139 |
| At end of the period | **₱10,821,389** | ₱8,981,389 |

a. Track record of registration:

| Date | Number of Shares Licensed | Issue/Offer Price |
|---|---|---|
| August 1948 | 100,000 | ₱1.00 |
| November 1958 | 500,000 | 1.00 |
| December 1961 | 1,000,000 | 1.00 |
| March 1966 | 2,000,000 | 1.00 |
| – | 6,000,000 | 1.00 |
| October 1995 | 247,500,000 | 1.00 |

b. As discussed in Note 1, in July 2012, the Company received from Tangent ₱5.0 billion cash in exchange for LTG's 5,000,000,000 common shares. Costs related to the share issuance amounted to ₱67.5 million and is presented as a deduction to additional paid in capital.

c. In April 2013, LTG issued 1.84 billion shares for the net proceeds of ₱36.6 billion, net of offering expenses amounting to ₱1.1 billion which were charged against capital in excess of par in 2013.

Retained Earnings and Dividends
On June 19, 2013, the BOD approved the declaration and distribution of cash dividends of ₱0.15 per share to all stockholders of record of the Company as of July 3, 2013. The cash dividend was authorized to be paid not later than July 20, 2013. Amount paid was ₱1.6 billion in July 2013.

As of June 30, 2013 and December 31, 2012, retained earnings include undistributed earnings, representing accumulated earnings of subsidiaries and equity in net earnings of associate, which are not available for dividend declaration until received in the form of dividends from the subsidiaries and associates.

Retained earnings are further restricted for the payment of dividends to the extent of the cost of the shares held in treasury and deferred income tax assets recognized as of June 30, 2013 and December 31, 2012.

## 21. Basic/Diluted Earnings Per Share

Basic/diluted earnings per share were calculated as follows:

| | Six Months Ended June 30 | |
|---|---|---|
| | **2013** | 2012 |
| | *(In Thousands)* | |
| Net income attributable to equity holders of the parent company | **₱6,138,807** | ₱5,189,677 |
| Divided by weighted-average number of shares | **9,511,566** | 8,715,963 |
| Basic/diluted EPS for net income attributable to equity holders of the parent company | **₱0.64** | ₱0.60 |

EPS is calculated using the consolidated net income attributable to equity holders of the parent company divided by the weighted average number of shares, wherein the 5,000,000,000 additional shares issued in 2012 to effect and fund the group restructuring were recognized as if these shares were issued at the beginning of the earliest period presented (see Note 1).

## 22. Financial Risk Management Objectives and Policies

Risk Management Strategies
The Group's financial risk management strategies are handled on a group-wide basis, side by side with those of the other related companies within the Group. The Group's management and the BODs of the various companies comprising the Group review and approve policies for managing these risks. Management closely monitors the funds and financial transactions of the Group. Funds

are normally deposited with affiliated local banks and financial transactions are normally dealt with companies belonging to the Group (see Note 18).

The Group's banking segment's activities are principally related to the development, delivery, servicing and use of financial instruments. Risk is inherent in these activities but it is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is critical to the banking segment's continuing profitability.

The banking segment monitors its processes associated with the following overall risk categories:

- Credit Risk
- Market Risk
- Liquidity Risk
- Operational Risk
- Information Security and Technology Risk

Further, the banking segment is also cognizant of the need to address various other risks through the primary divisions presented above. The following are also taken into consideration as part of the overall Enterprise Risk Management (ERM) Framework:

- Counterparty Risk
- Business Risk
- Strategic Risk
- Compliance Risk
- Legal Risk
- Reputational Risk
- Concentration Risk
- Country Risk
- Risks arising from PNB's shareholdings and equity interests

Managing the level of these risks as provided for by the baking segment's ERM framework is critical to its continuing profitability. The Risk Oversight Committee (ROC) of the banking segment's BOD determines the risk policy and approves the principles of risk management, establishment of limits for all relevant risks, and the risk control procedures. The ROC is also responsible for the risk management of the banking segment.

The RMG provides the legwork for the ROC in its role of formulating the risk management strategy, the management of regulatory capital, the development and maintenance of the internal risk management framework, and the definition of the governing risk management principles. The mandate of the RMG involves:

- Implementing the risk management framework of identifying, measuring, controlling and monitoring the various risk taking activities of the Group, inherent in all financial institutions;
- Providing services to the risk-taking units and personnel in the implementation of risk mitigation strategies; and
- Establishing recommended limits based on the results of its analysis of exposures.

<u>Financial Risk Management Policy</u>
The Group's principal financial instruments comprise of short-term and long-term debts and cash and cash equivalents. The main purpose of these financial instruments is to ensure adequate funds

for the Group's operations and capital expansion. Excess funds are invested in available-for-sale financial assets with a view to liquidate these to meet various operational requirements when needed. The Group has various other financial assets and financial liabilities such as receivables and accounts payable and accrued expenses which arise directly from its operations.

The main risks arising from the use of financial instruments are liquidity risk, counterparty risk, credit risk and market risks (consisting of foreign exchange risk, cash flow interest rate risk and equity price risk),

Credit and Concentration Risk

The Group manages its credit risk by transacting with counterparties of good financial condition and selecting investment grade securities. The Group trades only with recognized, creditworthy third parties. In addition, receivable balances are monitored on an on-going basis with the result that the Group's exposure to bad debts is not significant. Management closely monitors the fund and financial condition of the Group. Funds are normally deposited with affiliated banks, and financial transactions are normally dealt with related parties. These strategies, to an extent, mitigate the Group's counterparty risk. he Group manages its credit risk at various levels (i.e., strategic level, portfolio level down to individual transaction).

In addition, credit risk of Property development group is managed primarily through analysis of receivables on a continuous basis. The credit risk for contracts receivables is mitigated as the Group has the right to cancel the sales contract without the risk for any court action and can take possession of the subject property in case of refusal by the buyer to pay on time the contracts receivables due. This risk is further mitigated because the corresponding title to the property sold under this arrangement is transferred to the buyers only upon full payment of the contract price.

For the banking segment, managing credit risk also involves monitoring of migration risk, concentration risk, country risk and settlement risk. The credit risk management of the entire loan portfolio is under the direct oversight of the ROC and Executive Committee. Credit risk assessment of individual borrower is performed by the business sector and remedial sector. Risk management is embedded in the entire credit process, i.e., from credit origination to remedial management (if needed).

Among the tools used by the banking segment in identifying, assessing and managing credit risk include:

- Documented credit policies and procedures: sound credit granting process, risk asset acceptance criteria, target market and approving authorities;
- System for administration and monitoring of exposure;
- Pre-approval review of loan proposals;
- Post approval review of implemented loans;
- Work out system for managing problem credits;
- Regular review of the sufficiency of valuation reserves;
- Monitoring of the adequacy of capital for credit risk via the Capital Adequacy Ratio (CAR) report;
- Monitoring of breaches in regulatory and internal limits;
- Credit Risk Management Dashboard;
- Diversification;
- Internal Risk Rating System for corporate accounts;
- Credit Scoring for retail accounts; and
- Active loan portfolio management undertaken to determine the quality of the loan portfolio and identify the following:

a. portfolio growth
b. movement of loan portfolio (cash releases and cash collection for the month)
c. loss rate
d. recovery rate
e. trend of nonperforming loans (NPLs)
f. concentration risk (per classified account, per industry, clean exposure, large exposure, contingent exposure, currency, security, facility, demographic, etc)

Continuous changes have been made in the policies, procedures, system and quality of people. The baking segment has moved one step further by collecting data on risk rating of loan borrowers with an asset size of ₱15.0 million and above as initial requirement in PNB's model for internal Probability of Default (PD) and Loss Given Default (LGD).

*Credit-related commitments of the banking segment*
The exposures represent guarantees, standby letters of credit (LCs) issued by the banking segment and documentary/commercial LCs which are written undertakings by the banking segment. To mitigate this risk, the banking segment requires hard collaterals, as discussed under *Collateral and other credit enhancement*, for standby LCs lines while commercial LCs are collateralized by the underlying shipments of goods to which they relate.
*Derivative financial instruments of the banking segment*
Credit risk arising from derivative financial instruments is, at any time, limited to those with positive fair values, as recorded in the consolidated balance sheets.

*Collateral and other credit enhancement*
As a general rule, character is the single most important consideration in granting loans. However, collaterals are requested to mitigate risk. The loan value and type of collateral required depend on the assessment of the credit risk of the borrower or counterparty. The Group follows guidelines on the acceptability of types of collateral and valuation parameters.

The main types of collateral obtained are as follows:

- For corporate accounts - cash, guarantees, securities, physical collaterals (e.g., real estate, chattels, inventory, etc.); as a general rule, commercial, industrial and residential lots are preferred
- For retail lending - mortgages on residential properties and vehicles financed

The disposal of the foreclosed properties is handled by the Asset Management Sector which adheres to the general policy of disposing assets at the highest possible market value.

Management regularly monitors the market value of the collateral and requests additional collateral in accordance with the underlying agreement. The existing market value of the collateral is considered during the review of the adequacy of the allowance for credit losses. Generally, collateral is not held over loans and advances to banks except for reverse repurchase agreements. The Group is not permitted to sell or repledge the collateral in the absence of default by the owner of the collateral.

*Excessive risk concentration*
Concentrations arise when a number of counterparties are engaged in similar business activities having similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Group's performance to developments affecting a particular

industry or geographical location. Such credit risk concentrations, if not properly managed, may cause significant losses that could threaten the Group's financial strength and undermine public confidence. Concentration risk per business segment could arise on the following:

- Distilled spirits segment's sale of alcoholic beverage pertains mainly to four main customers with sales to them comprising about 99% of total distilled spirits sales.
- Beverage segment annual sales pertain mainly to 13 parties with sales to them comprising about 100% of the total beverage sales.
- Tobacco and property development segments are not exposed to concentration risk because it has diverse base of counterparties.
- Banking segment analyzes the credit risk concentration to an individual borrower, related group of accounts, industry, geographic, internal rating buckets, currency, term and security.

For the banking segment risk concentration monitoring purposes, the financial assets are broadly categorized into (1) loans and receivables and (2) trading and financial investment securities. To mitigate risk concentration, the Group constantly checks for breaches in regulatory and internal limits. Clear escalation process and override procedures are in place, whereby any excess in limits are covered by appropriate approving authority to regularize and monitor breaches in limits.

*Credit quality per class of financial assets used by the Group except for the banking segment*

"Standard grade" accounts consist of financial assets from trusted parties with good financial condition. "Substandard grade" accounts, on the other hand, are financial assets from other counterparties with relatively low defaults. The Group did not regard any financial asset as "high grade" in view of the erratic cash flows or uncertainty associated with the financial instruments. "Past due but not impaired" are items with history of frequent default, nevertheless, the amount due are still collectible. Lastly, "Impaired financial assets" are those that are long-outstanding and have been provided with allowance for doubtful accounts.

*Credit quality per class of financial assets of the banking segment*
The credit quality of financial assets is assessed and managed using external and internal ratings. For receivable from customers classified as business loans, the credit quality is generally monitored using the 14-grade Credit Risk Rating (CRR) System which is integrated in the credit process particularly in loan pricing and allocation of valuation reserves. The model on risk ratings is assessed and updated regularly.

Validation of the individual internal risk rating is conducted by the Credit Management Division to maintain accurate and consistent risk ratings across the credit portfolio. The rating system has two parts, namely, the borrower's rating and the facility rating. It is supported by a variety of financial analytics, combined with an assessment of management and market information such as industry outlook and market competition to provide the main inputs for the measurement of credit or counterparty risk.

The CRRs of PNB's Receivables from customers classified as business loans are defined below:

*CRR 1 - Excellent*
Loans receivables rated as excellent include borrowers which are significant in size, with long and successful history of operations, an industry leader, with ready access to all equity and debt markets and have proven its strong debt service capacity.

*CRR 2 - Super Prime*
Loans receivables rated as super prime include borrowers whose ability to service all debt and meet financial obligations remains unquestioned.

*CRR 3 - Prime*
Under normal economic conditions, borrowers in this rating have good access to public market to raise funds and face no major uncertainties which could impair repayment.

*CRR 4 - Very Good*
Loans receivables rated as very good include borrowers whose ability to service all debts and meet financial obligations remain unquestioned, but current adverse economic conditions or changing circumstances have minimal impact on payment of obligations.

*CRR 5 - Good*
Loans receivables rated as good include borrowers with good operating history and solid management, but payment capacity could be vulnerable to adverse business, financial or economic conditions.

*CRR 6 - Satisfactory*
These are loans receivables to borrowers whose ability to service all debt and meet financial obligations remains unquestioned, but with somewhat lesser capacity than in CRR 5 accounts.
*CRR 7 - Average*
These are loans receivables to borrowers having ability to repay the loan in the normal course of business activity, although may not be strong enough to sustain a major setback.

*CRR 8 - Fair*
These are loans receivables to borrowers possessing the characteristics of borrowers rated as CRR7 with slightly lesser quality in financial strength, earnings, performance and/or outlook.

*CRR 9 - Marginal*
These are performing loans receivables from borrowers not qualified as CRRs 1-8. The borrower is able to withstand normal business cycles, although any prolonged unfavorable economic and/or market period would create an immediate deterioration beyond acceptable levels.

*CRR 10 - Watchlist*
This rating includes borrower where the credit exposure is not at risk of loss at the moment but the performance of the borrower has weakened and, unless present trends are reversed, could eventually lead to losses.

*CRR 11 - Special Mention*
These are loans that have potential weaknesses that deserve management's close attention. These potential weaknesses, if left uncorrected, may affect the repayment of the loan and thus increase credit risk to PNB.

*CRR 12 - Substandard*
These are loans or portions thereof which appear to involve a substantial and unreasonable degree of risk to PNB because of unfavorable record or unsatisfactory characteristics.

*CRR 13 - Doubtful*
These are loans or portions thereof which have the weaknesses inherent in those classified as CRR 12 with the added characteristics that existing facts, conditions and values make collection or liquidation in full highly improbable and in which substantial loss is probable.

*CRR 14 - Loss*
These are loans or portions thereof which are considered uncollectible or worthless.

PNB is using the Credit Scoring for evaluating borrowers with assets size below ₱15.0 million. Credit scoring details the financial capability of the borrower to pay for any future obligation.
GOCCs and LGUs are rated using the "means and purpose" test whereby borrowers have to pass the two major parameters, namely:

- "Means" test - the borrower must have resources or revenues of its own sufficient to service its debt obligations.
- "Purpose" test - the loan must be obtained for a purpose consistent with the borrower's general business.

LGU loans are backed-up by assignment of Internal Revenue Allotment. Consumer loans are covered by mortgages in residential properties and vehicles financed. Fringe benefit loans are repaid through automatic salary deductions and exposure is secured by mortgage on house or vehicles financed.

*Impairment assessment*
The main consideration for impairment assessment includes whether there are known difficulties in the cash flow of the counterparties. The Group assesses impairment in two ways: individually and collectively.

The two methodologies applied by the Group in assessing and measuring impairment/credit losses include:

a. Specific (individual) assessment
   The Group assesses each individually significant credit exposure or advances for any objective evidence of impairment.

   Among the items and factors considered by the Group when assessing and measuring specific impairment/credit allowances are:

   - the going concern of the borrower's business;
   - the ability of the borrower to repay its obligations during financial crises;
   - the projected receipts or expected cash flows;
   - the availability of other sources of financial support;
   - the existing realizable value of collateral; and
   - the timing of the expected cash flows.

   The impairment/credit allowances, if any, are evaluated every quarter or as the need arises in view of favorable or unfavorable developments.

b. Collective assessment
   Loans and advances that are not individually significant (e.g., credit cards, housing loans, car loans, development incentives loans, fringe benefit loans) and individually significant loans and advances where there is no apparent evidence of individual impairment are collectively assessed for impairment. A particular portfolio is reviewed every quarter to determine its corresponding appropriate allowances.

Impairment losses are estimated by taking into consideration the following information:

- historical losses of the portfolio;
- current adverse economic conditions that have direct impact on the portfolio;
- losses which are likely to occur but has not yet occurred; and
- expected receipts and recoveries once impaired.

The amount of loss is recognized in the consolidated statement of income with a corresponding reduction in the carrying value of the loans and receivables through an allowance account.

Liquidity Risk and Fund Management

The Group's objective is to maintain a balance between continuity of funding and sourcing flexibility through the use of available financial instruments. The Group manages its liquidity profile to meet its working and capital expenditure requirements and service debt obligations. As part of the liquidity risk management program, the Group regularly evaluates and considers the maturity of its financial assets (e.g., trade receivables, other financial assets) and resorts to short-term borrowings whenever its available cash or matured placements is not enough to meet its daily working capital requirements. To ensure availability of short-term borrowings, the Group maintains credit lines with banks on a continuing basis.

The Group relies on budgeting and forecasting techniques to monitor cash flow concerns. The Group also keeps its liquidity risk minimum by prepaying, to the extent possible, interest bearing debt using operating cash flows.

The baking segment's liquidity management involves maintaining funding capacity to accommodate fluctuations in asset and liability levels due to changes in PNB's business operations or unanticipated events created by customer behavior or capital market conditions. The baking segment seeks to ensure liquidity through a combination of active management of liabilities, a liquid asset portfolio composed substantially of deposits in primary and secondary reserves, and the securing of money market lines and the maintenance of repurchase facilities to address any unexpected liquidity situations.

Liquidity risk of the banking segment is monitored and controlled primarily by a gap analysis of maturities of relevant assets and liabilities reflected in the maximum cumulative outflow (MCO) report, as well as an analysis of available liquid assets. The MCO focuses on a 12-month period wherein the 12-month cumulative outflow is compared to the acceptable MCO limit set by the BOD. Furthermore, an internal liquidity ratio has been set to determine sufficiency of liquid assets over deposit liabilities. Liquidity is monitored by the baking segment on a daily basis through the Treasury Group. Likewise, the RMG monitors the static liquidity via the MCO under normal and stressed scenarios.

Market Risks (other than Banking Segment)

The Group's operating, investing, and financing activities are directly affected by changes in foreign exchange rates and interest rates. Increasing market fluctuations in these variables may result in significant equity, cash flow and profit volatility risks for the Group. For this reason, the Group seeks to manage and control these risks primarily through its regular operating and financing activities.

Management of financial market risk is a key priority for the Group. The Group generally applies sensitivity analysis in assessing and monitoring its market risks. Sensitivity analysis enables management to identify the risk position of the Group as well as provide an approximate quantification of the risk exposures. Estimates provided for foreign exchange risk, cash flow interest rate risk, price interest rate risk and equity price risk are based on the historical volatility for each market factor, with adjustments being made to arrive at what the Group considers to be reasonably possible.

*Equity Price Risk*
Equity price risk is the risk that the fair value of equities will decrease as a result of changes in the levels of equity indices and value of individual stocks. In 2013 and 2012, changes in fair value of equity instruments held as AFS equity instruments dues to a reasonably possible change in equity interest, with all other variables held constant, will increase other comprehensive income by ₱16.8 million if equity prices will increase by 5.2%. An equal change in the opposite direction would have decreased in equity by the same amount.

*Foreign Exchange Risk*
The Group's foreign currency risk related to its US$-denominated cash in banks and cash equivalents and due to and from related parties. Management closely monitors the fluctuations in exchange rates so as to anticipate the impact of foreign currency risks associated with the financial instruments. The Group currently does not enter into derivative transactions to hedge its currency exposure.

*Interest Rate Risk*
Interest rate risk arises from the possibility that changes in interest rates would unfavorably affect future cash flows from financial instruments. As of June 30, 2013 and December 31, 2012, certain long-term debts of the Group such as the bonds payable and the secured and unsecured loans are not exposed to the risk in changes in market interest rates since the debts are issued at fixed rates. As of June 30, 2013, the Group's exposure pertains mainly to short-term debts and long-term notes payable. Repricing of floating rate financial instruments is mostly at interval of three months or six months for the short-term debts and annually for the notes payable.

<u>Market Risk of the Banking Segment</u>
Market risk of the banking segment is the risk to earnings or capital arising from adverse movements in factors that affect the market value of instruments, products, and transactions in an institutions' overall portfolio. Market risk arises from market making, dealing, and position taking in interest rate, foreign exchange and equity markets. The succeeding sections provide discussion on the impact of market risk on the banking segment's trading and structural portfolios.

*Trading market risk*
Trading market risk exists in the banking segment as the values of its trading positions are sensitive to changes in market rates such as interest rates, foreign exchange rates and equity prices. PNB is exposed to trading market risk in the course of market making as well as from taking advantage of market opportunities. The banking segment adopts the Parametric Value-at-Risk (VaR) methodology (with 99% confidence level, and one day holding period for FX and equity price risks VaR and ten day holding period for interest rate risk VaR) to measure the banking segment's trading market risk. Volatilities are updated monthly and are based on historical data for a rolling 260-day period. The RMG reports the VaR utilization and breaches to limits to the risk taking personnel on a daily basis and to the ALCO and Executive Committee on a monthly basis. All risk reports discussed in the EXCOM meeting are noted by the BOD. The VaR figures are backtested to validate the robustness of the VaR model.

*Objectives and limitations of the VaR methodology*
The VaR models are designed to measure market risk in a normal market environment. The models assume that any changes occurring in the risk factors affecting the normal market environment will follow a normal distribution. The use of VaR has limitations because it is based on historical volatilities in market prices and assumes that future price movements will follow a

statistical distribution. Due to the fact that VaR relies heavily on historical data to provide information and may not clearly predict the future changes and modifications of the risk factors, the probability of large market moves may be underestimated if changes in risk factors fail to align with the normal distribution assumption. VaR may also be under- or over- estimated due to the assumptions placed on risk factors and the relationship between such factors for specific instruments. Even though positions may change throughout the day, the VaR only represents the risk of the portfolios at the close of each business day, and it does not account for any losses that may occur beyond the 99.00% confidence level.

*VaR assumptions/parameters*
VaR estimates the potential loss on the current portfolio assuming a specified time horizon and level of confidence at 99.00%. The use of a 99.00% confidence level means that, within a one day horizon, losses exceeding the VaR figure should occur, on average, not more than once every one hundred days.

*VaR limits*
Since VaR is an integral part of the banking segment's market risk management, VaR limits have been established annually for all financial trading activities and exposures. Calculated VaR compared against the VaR limits are monitored. Limits are based on the tolerable risk appetite of PNB. VaR is computed on an undiversified basis; hence, PNB does not consider the correlation effects of the three trading portfolios.

There is no instance that the aggregate daily losses were greater than the total VaR (in millions).

**Structural Market Risk**

<u>Non-trading Market Risk</u>
*Interest rate risk*
The banking segment seeks to ensure that exposure to fluctuations in interest rates are kept within acceptable limits. Interest margins may increase as a result of such changes but may be reduced or may create losses in the event that unexpected movements arise.

Repricing mismatches will expose the banking segment to interest rate risk. The banking segment measures the sensitivity of its assets and liabilities to interest rate fluctuations by way of a "repricing gap" analysis using the repricing characteristics of its consolidated balance sheet positions tempered with approved assumptions. To evaluate earnings exposure, interest rate sensitive liabilities in each time band are subtracted from the corresponding interest rate assets to produce a "repricing gap" for that time band. The difference in the amount of assets and liabilities maturing or being repriced over a one year period would then give the banking segment an indication of the extent to which it is exposed to the risk of potential changes in net interest income. A negative gap occurs when the amount of interest rate sensitive liabilities exceeds the amount of interest rate sensitive assets. Vice versa, positive gap occurs when the amount of interest rate sensitive assets exceeds the amount of interest rate sensitive liabilities.

During a period of rising interest rates, a company with a positive gap is better positioned because the company's assets are refinanced at increasingly higher interest rates increasing the net interest margin of the company over time. During a period of falling interest rates, a company with a positive gap would show assets repricing at a faster rate than one with a negative gap, which may restrain the growth of its net income or result in a decline in net interest income.

For risk management purposes, the repricing gap covering the one year period is multiplied by an assumed change in interest rates to yield an approximation of the change in net interest income that would result from such an interest rate movement. The banking segment's BOD sets a limit on the level of earnings at risk (EaR) exposure tolerable to the banking segment. Compliance to the EaR limit is monitored monthly by the RMG. This EaR computation is accomplished monthly, with a quarterly stress test.

As one of the long-term goals in the risk management process, the Group has set the adoption of the economic value approach in measuring the interest rate risk in the banking book to complement the earnings approach currently used.

*Foreign currency risk*
Foreign exchange is the risk to earnings or capital arising from changes in foreign exchange rates. The Group takes on exposure to effects of fluctuations in the prevailing foreign currency exchange rates on its financials and cash flows.

Foreign currency liabilities generally consist of foreign currency deposits in the banking segment's FCDU books, accounts made in the Philippines or which are generated from remittances to the Philippines by Filipino expatriates and overseas Filipino workers who retain for their own benefit or for the benefit of a third party, foreign currency deposit accounts with the banking segment and foreign currency-denominated borrowings appearing in the regular books of the banking segment.

Foreign currency deposits are generally used to fund the banking segment's foreign currency-denominated loan and investment portfolio in the FCDU. Banks are required by the BSP to match the foreign currency liabilities with the foreign currency assets held through FCDUs. In addition, the BSP requires a 30.00% liquidity reserve on all foreign currency liabilities held through FCDUs. Outside the FCDU, the banking segment has additional foreign currency assets and liabilities in its foreign branch network.

The Group's policy is to maintain foreign currency exposure within acceptable limits and within existing regulatory guidelines. The Group believes that its profile of foreign currency exposure on its assets and liabilities is within conservative limits for a financial institution engaged in the type of business in which the Group is involved.

The table below summarizes the exposure to foreign exchange rate risk. Included in the table are the assets and liabilities at carrying amounts, categorized by currency (in millions).

*Prepayment risk*
Prepayment risk in PNB is deemed to be relatively low. PNB projects prepayment ratio by way of using historical data on loan prepayment rate. PNB's loans prepayment rate is less than 1.41%, 1.09% and 1.03% of the total loan portfolio in 2012, 2011 and 2010, respectively. In view of this, management believes that 1.41% is not material enough to warrant a separate set of cash flow analyses. All calculations related to asset and liability management (e.g., as net interest margin analysis) take into account the contractual terms of the financial instrument.

*Capital management and management of insurance and financial risks*
Although life insurance companies are in the business of taking risks, PLII limits its risk exposure only to measurable and quantifiable risks. The main objective of PLII's risk management policies is to ensure that PLII remains financially viable and capable in paying its liabilities.

There are many risks associated in the life insurance business such as insurance risks, investment risks, asset depreciation and other business risks. These risks are managed separately to ensure that PLII is not exposed to risks that are unnecessary or risks with no commensurate expected benefits or returns.

*Governance framework*
PLII has established a risk management function with clear terms of reference and with the responsibility for developing policies on market, credit, liquidity, insurance and operational risks. It also supports the effective implementation of policies at the overall company and individual business unit levels. The chief financial officer (CFO) and Internal Audit Department performs procedures to identify various risks. The results of the procedures are reported to the BOD and necessary actions are taken to mitigate the risks identified.

The policies define PLII's identification of risk and its interpretation, limit structure to ensure the appropriate quality and diversification of assets, alignment of underwriting and reinsurance strategies to the corporate goals and specific reporting requirements.

*Regulatory framework*
Regulators are interested in protecting the rights of the policyholders and maintain close vigil to ensure that PLII is satisfactorily managing affairs for their benefit. At the same time, the regulators are also interested in ensuring that PLII maintains appropriate solvency position to meet liabilities arising from claims and that the risk levels are at acceptable levels.

The operations of PLII are subject to the regulatory requirements of the Insurance Commission (IC). Such regulations not only prescribe approval and monitoring of activities but also impose certain restrictive provisions (e.g., margin of solvency to minimize the risk of default and insolvency on the part of the insurance companies to meet the unforeseen liabilities as these arise, fixed capitalization requirements, risk-based capital requirements).

*Capital management*
PLII manages its capital in accordance with the mandates of the IC being its regulator. Under the requirements of the IC and the Code, PLII should meet the minimum levels set for the following capital requirements: Margin of Solvency (MOS), Minimum Statutory Net Worth and Paid-up Capital, and the Risk-Based Capital (RBC). PLII regularly monitors its compliance with these capital requirements. Since PLII is now 100.00% Filipino-owned, the capital requirements have reduced significantly and PLII's current capital now well exceeds the minimum requirements.

Further, government bonds amounting to at least 25.00% of the Minimum Paid-up Capital are free from liens and encumbrances, and deposited under the IC, in accordance to Section 203 of the Code.

*a) MOS*
Under the Code, a life insurance company doing business in the Philippines shall maintain at all times a MOS equal to ₱0.50 million or ₱2.00 per thousand of the total amount of insurance in force as of the preceding calendar year in all policies (except term insurance), whichever is higher. The MOS shall be the excess of the value of its admitted assets as defined under the same Code, exclusive of the minimum paid-up capital, over the amount of its liabilities, unearned premiums, and reinsurance reserves.

The final amounts of the MOS can be determined only after the accounts of PLII have been examined by the IC specifically as to admitted and non-admitted assets as defined in the Code. The 2013 and 2012 MOS will be known only after the IC completes its examination of the accounts of PLII.

If an insurance company fails to meet the minimum required MOS, the IC is authorized to suspend or revoke all certificates of authority granted to such companies, its officers and agents, and no new business shall be done by and for such company until its authority is restored by the IC.

b) *Minimum statutory net worth and paid up capital*
Department of Finance issued Order 27-06 provides for the capitalization requirements for life, non-life and reinsurance companies. Under this order, the minimum statutory net worth and minimum paid-up capital requirements vary depending on the level of the foreign ownership in the insurance company. The statutory net worth shall include PLII's paid-up capital, capital in excess of par value, contingency surplus, retained earnings and revaluation increments as may be approved by the IC.

The required minimum statutory net worth and minimum paid-up capital for PLII, being a wholly-owned Filipino life insurance company is ₱500.00 million and ₱250.00 million, respectively, in 2013 and 2012. PLII has complied with the minimum statutory net worth and paid-up capital requirements based on PLII's own calculation.

c) *RBC requirement*
Insurance Memorandum Circular (IMC) No. 6-2006 provides for the risk-based capital framework for the life insurance industry to establish the required amounts of capital to be maintained by the companies in relation to their investment and insurance risks. Every life insurance company is annually required to maintain a minimum RBC ratio of 100.00% and not fail the trend test. Failure to meet the minimum RBC ratio shall subject the insurance company to the corresponding regulatory intervention which has been defined at various levels.

The RBC ratio shall be calculated as net worth divided by the RBC requirement. Net worth shall include PLII's paid-up capital, contributed and contingency surplus and unassigned surplus. Revaluation and fluctuation reserve accounts shall form part of net worth only to the extent authorized by the IC. The RBC requirement is the ratio of the number of insurers which are able to meet the corresponding RBC Hurdle Rate requirement for a given year to the total number of insurers in the industry.

The final amount of RBC ratio can be determined only after the accounts of PLII have been examined by the IC specifically as to admitted and non-admitted assets as defined under the same Code.

d) *Consolidated compliance framework*
IMC 10-2006 integrated the compliance standards for the fixed capitalization and risk-based capital framework.

Subsequent to year 2006, the fixed capitalization requirement for a given year may be suspended for insurers that comply with the required RBC hurdle rate, provided that the industry complies with the required Industry RBC Ratio Compliance Rate. The IMC provides the annual schedule of progressive rates for the Industry RBC Ratio Compliance Rates and the

RBC Hurdle Rates from 2007 to 2011. For the review year 2012 which shall be based on the 2011 synopsis, the industry RBC Ratio Compliance Rate is 100.0% and the RBC Hurdle Rate is 250.00%. For the review year 2011 which shall be based on the 2010 synopsis, the Industry RBC Ratio Compliance Rate is 90.00% and the RBC Hurdle Rate is 250.00%. Failure to achieve one of the rates will result in the imposition of the fixed capitalization requirement for the year under review.

e) *Unimpaired capital requirement*
IMC 22-2008 provided for the purposes of determining compliance with the law, rules and regulations requiring that the paid-up capital should remain intact and unimpaired at all times, the consolidated balance sheet should show that the net worth or stockholders' equity is at least equal to the actual paid-up capital.

PLII has complied with all of the above capital requirements in 2013 and 2012.

Insurance Risk

*Nature of risk*

The risk under any one insurance contract is the possibility that the insured event occurs. This event may be death, or in the case of some riders, disability, accidental injury, or contraction of critical illness. By the very nature of an insurance contract, this risk is random and unpredictable.

For a portfolio of insurance contracts where the theory of probability is applied to pricing, the principal risk that PLII faces under its insurance contracts is that future claim on death, accident, disability, and critical illness claims exceed the future premiums plus the carrying amount of the insurance liabilities. This could occur if the frequency and magnitude of claims is greater than the assumption used in calculating PLII's liability. Occurrence of insured events is random and the actual number of claims will vary from year to year from the mortality assumptions made during product pricing. However, the law of large number is expected to be applicable as the pool of risk increases in volume and aggregate claims becomes more predictable.

Experience shows that the larger the portfolio of similar insurance contracts, the smaller is the relative variability compared to the expected. Insurance risks generally vary by gender and age of the insured as these factors correlate greatly with the incidence rates of the insured events. Because of this, a more diverse demographic profile of insured lives may be more desirable since a more diverse risk profile reduces variability.

To minimize insurance risks, PLII strictly adheres to prudent underwriting standards in assessing insurance applications. These underwriting standards include a schedule of medical and non-medical requirements for specific range of ages and sum assured. Some policyholders are charged with additional premium in the form of flat or multiple extra premiums due to extra risks resulting from the applicant's occupation, health and lifestyle. Applications for insurance may be denied or postponed for certain substandard cases. To guard against anti-selection, insurance applications that do not establish insurable interest are rejected. Statements of assets and liabilities may also be required from the applicant to justify the sum assured applied for, and his ability to pay the premium.

*Frequency of claims*

For contracts where death is the insured risk, the most significant factors that could increase the overall frequency of claims are epidemics or wide spread changes in lifestyle resulting in earlier or more claims than expected. In the Philippines, higher-than-expected claims also arise from typhoons, landslides, and other geologic events.

For contracts with Discretionary Participating Feature (DPF), a portion of the insurance risk is effectively shared with the policy owner, as policy dividends may be reduced due to adverse claims and investment experience.

For unit-linked insurance policies where the cost of insurance charges is not guaranteed, insurance risk is borne mostly by the policyholders. PLII has the right to alter these charges based on its mortality experience and hence minimize its exposure to mortality risk. Delays in implementing increases in charges and market or regulatory restraints over the extent of the increases may reduce its mitigating effect.

PLII manages these risks through its underwriting strategy and reinsurance arrangements. The underwriting strategy is intended to ensure that the risks underwritten are pooled into a sufficiently large portfolio. Medical selection is also included in the underwriting procedures with premiums varied to reflect the health condition and family medical history of the applicants. PLII has a retention limit of ₱2.50 million on any standard risk. PLII reinsures the excess of the insured benefit over ₱2.50 million for standard risks (from a medical point of view) under an excess of loss reinsurance arrangement. PLII's risk retention is lower for medically impaired or substandard lives, which involves higher risks. PLII also has a Catastrophe Reinsurance agreement, which protects PLII in case of a catastrophic event resulting to multiple death claims.

Categories and Fair Value of Financial Instruments

The following tables present a comparison by category of the carrying amounts and fair values of the Group's financial instruments:

| | **June 30, 2013** | | December 31, 2012 | |
|---|---|---|---|---|
| | **Carrying Value** | **Fair Value** | Carrying Value | Fair Value |
| | | | *(In Thousands)* | |
| **Financial Assets** | | | | |
| Loans and Receivables: | | | | |
| Cash in bank and cash equivalents | **₱9,257,075** | **₱9,257,075** | ₱14,158,687 | ₱14,158,687 |
| Trade receivables | **10,630,964** | **10,630,964** | 10,907,164 | 10,907,164 |
| Other receivables | **5,241,339** | **5,241,339** | 1,781,632 | 1,781,632 |
| Due from related parties | **32,326,105** | **32,326,105** | 16,362,465 | 16,362,465 |
| Refundable deposits | – | – | 135,190 | 135,190 |
| | **₱57,455,483** | **₱57,455,483** | ₱43,345,138 | ₱43,345,138 |
| **Financial Liabilities** | | | | |
| Short term debts | **₱–** | **₱–** | ₱1,870,000 | ₱1,870,000 |
| Accounts payable and other liabilities | **13,284,834** | **13,284,834** | 11,967,174 | 11,967,174 |
| Long-term debts | **16,400,874** | **16,821,134** | 20,347,197 | 20,347,197 |
| Due to related parties | **49,913,392** | **49,913,392** | 37,018,854 | 37,018,854 |
| | **₱79,599,100** | **₱80,019,360** | ₱71,203,225 | ₱71,203,225 |

The following methods and assumptions are used to estimate the fair value of each class of financial instruments:

*Cash and cash equivalents*

The carrying amounts of cash and cash equivalents approximate fair value. The carrying amounts of receivables approximate fair value due to their short-term settlement period.

*Loans and receivables*

For loans with fixed interest rates, fair values are estimated by discounted cash flow methodology, using the Group's current market lending rates for similar types of loans. For loans with floating interest rates, with repricing frequencies on a quarterly basis, the Group assumes that the carrying amount approximates fair value. Where the repricing frequency is beyond three months, the fair value of floating rate loans is determined using the discounted cash flow methodologies.

*Other current financial instruments*
The historical cost carrying amounts of refundable deposits, accounts payable, accrued expenses and due to related parties approximate their fair values due to the short-term nature of these accounts.

*Debt securities*
Fair values are generally based upon quoted market prices. If the market prices are not readily available, fair values are obtained from independent parties offering pricing services, estimated using adjusted quoted market prices of comparable investments or using the discounted cash flow methodology.

*Equity securities*
Fair values of quoted equity securities are based on quoted market prices. While fair values of unquoted equity securities are the same as the carrying value since the fair value could not be reliably determined due to the unpredictable nature of future cash flows and the lack of suitable methods of arriving at a reliable fair value.

*Long-term obligations and short-term, fixed rate notes payable*
The fair value of long-term obligations (whether fixed or floating) is generally based on the present value of expected cash flows with discount rates that are based on risk-adjusted benchmark rates (in the case of floating rate liabilities with annual repricing, the carrying value approximates the fair value in view of the recent and regular repricing based on current market rates). The discount rates used for the unsecured debts are 5.03%, 5.03% and 5.20% in 2012, 2011 and 2010, respectively. The fair value of bonds payable is determined by reference to latest transaction price at the end of reporting period.

The carrying value of the short-term bank loans and secured debts approximates its fair value due to their short-term settlement period (i.e., effect of discounting is minimal). The carrying value of the notes payable approximate their fair value since the notes carry interest rates based on market.

*Derivative instruments*
Fair values are estimated based on quoted market prices or acceptable valuation models.
*Time deposit liabilities and subordinated debt including designated at FVPL*
Fair value is determined using the discounted cash flow methodology.

The fair value information are analyzed by source of inputs on fair valuation as follows:

- Quoted prices in active markets for identical assets (Level 1);
- Those involving inputs other than quoted prices included in Level 1 that are observable for the asset, either directly (as prices) or indirectly (derived from prices) (Level 2); and
- Those inputs for the asset that are not based on observable market data (unobservable inputs) (Level 3).

The Banking segment held the following assets and liabilities measured at recurring and non-recurring fair value measurements and their corresponding level in fair value hierarchy:

| | June 30, 2013 | | | |
|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Total** |
| **Recurring Fair Value Measurements** | | | | |
| **Financial Assets** | | | | |
| Financial assets at FVPL: | | | | |
| Held-for-trading | **₱4,621,081** | **₱314** | **₱–** | **₱4,621,395** |
| Designated at FVPL | **2,108,218** | **-** | **2,487,732** | **4,595,950** |
| | **₱6,729,299** | **₱314** | **₱2,487,732** | **₱9,217,345** |
| AFS investment: | **₱80,600,620** | **₱–** | **₱–** | **₱80,600,620** |
| | **₱80,600,620** | **₱–** | **₱–** | **₱80,600,620** |
| **Financial Liabilities** | | | | |
| Financial liabilities at FVPL: | | | | |
| Designated at FVPL | **₱ 2,103,100** | **₱–** | **₱2,487,732** | **₱4,590,832** |
| Derivative liabilities | **723,823** | **300** | **–** | **724,123** |
| | **₱2,826,923** | **₱300** | **₱2,487,732** | **₱5,314,955** |

| | December 31, 2012 | | | |
|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Total** |
| **Recurring Fair Value Measurements** | | | | |
| **Financial Assets** | | | | |
| Financial assets at FVPL: | | | | |
| Held-for-trading | **₱2,379,852** | **₱395,457** | **₱–** | **₱2,775,309** |
| Designated at FVPL | **–** | **1,247,756** | **–** | **1,247,756** |
| | **₱2,379,852** | **₱1,643,213** | **₱–** | **₱4,023,065** |
| AFS investment: | **₱65,057,234** | **₱1,940,245** | **₱–** | **₱66,997,479** |
| | **₱65,057,234** | **₱1,940,245** | **₱–** | **₱66,997,479** |
| **Financial Liabilities** | | | | |
| Financial liabilities at FVPL: | | | | |
| Designated at FVPL | **₱–** | **₱–** | **₱6,196,070** | **₱6,196,070** |
| Derivative liabilities | **–** | **283,751** | **–** | **283,751** |
| | **₱–** | **₱283,751** | **₱6,196,070** | **₱6,479,821** |

The following table presents a comparison of the carrying amounts and fair values of assets and liabilities except those where carrying values approximate or equals their fair values (amounts in thousands):

| | **June 30, 2013** | | December 31, 2012 | |
|---|---|---|---|---|
| | **Carrying Value** | **Fair Market Value** | Carrying Value | Fair Market Value |
| **Financial Assets** | | | | |
| Loans and Receivables | | | | |
| Receivables from customers: | **₱ 221,314,057** | **₱ 225,048,840** | ₱126,461,612 | ₱128,324,420 |
| Unquoted debt securities | **11,347,718** | **12,546,271** | 3,859,268 | 5,131,586 |
| **Financial Liabilities** | | | | |
| Financial liabilities at amortized cost | | | | |
| Deposit liabilities: | | | | |
| Time | **44,801,526** | **44,954,680** | 19,908,821 | 20,134,885 |
| Subordinated debt | **9,946,090** | **10,968,660** | 9,938,816 | 10,956,745 |

The above assets and liabilities are measured at Level 2.

## 23. Capital Management

The main thrust of the Group's capital management policy is to ensure that the Group complies with externally imposed capital requirements, maintains a good credit standing and has a sound capital ratio to be able to support its business and maximize the value of its shareholders equity. The Group is also required to maintain debt-to-equity ratios to comply with certain loan agreements and covenants in 2013 and 2012.

The Group's dividend declaration is dependent on the availability of earnings and operating requirements. The Group manages its capital structure and makes adjustment to it, in light of changes in economic conditions. To maintain or adjust capital structure, the Group may adjust the dividend payment to shareholders, return capital to shareholders or issue new shares. No changes were made in the objectives, policies or processes in 2013 and 2012.

The Group considers its total equity reflected in the consolidated balance sheets as its capital. The Group monitors its use of capital and the Group's capital adequacy by using leverage ratios, specifically, debt ratio (total debt/total equity and total debt) and debt-to-equity ratio (total debt/total equity). Included as debt are the Group's total liabilities while equity pertains to total equity as shown in the consolidated balance sheets.

The table below shows the leverage ratios of the Group:

| | **2013** | 2012 |
|---|---|---|
| | *(In Thousands, except ratios)* | |
| Total liabilities | **₱511,813,070** | ₱513,530,145 |
| Total equity | **155,800,724** | 100,695,799 |
| Total liabilities and equity | **₱667,613,794** | ₱614,225,944 |
| Debt ratio | **0.77** | 0.84 |
| Debt-to-equity ratio | **3.29** | 5.10 |

## 24. Agreements, Commitments and Contingencies

Agreements

a. The Group's projects namely, Eton Cyberpod Corinthian and Eton Centris, were registered with PEZA on August 27, 2008 and September 19, 2008, respectively, as non-pioneer "ecozone developer/operator". The locations are created and designated as Information Technology Park.

b. The Group has three Board of Investment (BOI)-registered projects namely, Belton Place (BP), Eton Emerald Lofts (EEL) and One Archers Place (OAP).

   BP is registered with BOI as a new developer of low-cost housing project on a Non-Pioneer status under the Omnibus Investments Code of 1987 (Executive Order No. 226) on September 15, 2008. This registration entitles the Group to four years ITH from November 2008 or actual commercial operations or selling, whichever is earlier but in no case earlier than the date of registration. The ITH shall be limited only to the revenue generated from this project. Revenue with selling price exceeding ₱3.0 million shall not be covered by ITH.

Likewise, on September 23, 2008, two other projects of the Group namely, OAP and EEL, were registered with the BOI as a new developer of low-cost housing project on a Non-Pioneer status. These two projects shall enjoy the same benefits as BP.

Contingencies

In the ordinary course of business, the Group is a party to various litigations related mainly to trademark infringement, probable claims and tax refund and other cases. The timing of the cash outflows of these provisions is uncertain as it depends upon the outcome of the Group's negotiations and/or legal proceedings, which are currently ongoing with the parties involved.

Disclosure on additional details beyond the present disclosures may seriously prejudice the Group's position and strategy. Thus, as allowed by PAS 37, *Provisions, Contingent Liabilities and Contingent Assets*, only general descriptions were provided.

Trust Operations

Securities and other properties held by the banking segment in fiduciary or agency capacities for its customers are not included in the accompanying consolidated balance sheets since these are not assets of the banking segment. In connection with the trust functions of the banking segment, government securities are deposited with the BSP in compliance with trust regulations.

## 25. Restatements

Below are the restatements on the Group's consolidated balance sheets as of December 31, 2012:

a. The business combinations in 2013 involving LTG and its subsidiaries were accounted using the pooling of interest (see Note 1).

b. Effect of the adoption of PFRS 10 and PAS 19 R (see Note 2).

| | December 31, 2012 | | | |
|---|---|---|---|---|
| | As Previously Reported | Effect of Restatements due to business combinations | Effect of Restatements due to adoption of new standards | As Restated |
| | | *(In Thousands)* | | |
| **ASSETS** | | | | |
| **Current Assets** | | | | |
| Cash and cash equivalents | ₱8,906,360 | ₱115,308,638 | ₱– | ₱124,214,998 |
| Financial assets at fair value through profit or loss | – | 11,398,591 | – | 11,398,591 |
| Available-for-sale financial assets | – | 6,335,811 | – | 6,335,811 |
| Loans and receivables | 11,090,291 | 127,126,025 | 1,251,075 | 139,467,391 |
| Due from related parties | 20,540,635 | (4,178,170) | – | 16,362,465 |
| Inventories | 10,964,286 | – | – | 10,964,286 |
| Other current assets | 2,718,823 | 2,906,173 | (2,177,290) | 3,447,706 |
| **Total Current Assets** | 54,220,395 | 258,897,068 | (926,215) | 312,191,248 |

(Forward)

| | December 31, 2012 | | | |
|---|---|---|---|---|
| | As Previously Reported | Effect of Restatements due to business combinations | Effect of Restatements due to adoption of new standards | As Restated |
| | | *(In Thousands)* | | |
| **Noncurrent Assets** | | | | |
| Loans and receivables - net of current portion | ₱874,290 | ₱121,536,203 | ₱– | ₱122,410,493 |
| Available-for-sale financial assets | 765,926 | 90,832,541 | – | 91,598,467 |
| Investment in associate and joint venture | 13,906,189 | 5,061 | – | 13,911,250 |
| Property, plant and equipment: | | | | |
| At appraised values | 17,022,509 | 21,531,030 | – | 38,553,539 |
| At cost | 3,122,299 | 1,563,871 | – | 4,686,170 |
| Investment properties | 4,567,826 | 19,050,479 | – | 23,618,305 |
| Net retirement plan assets | 1,215,603 | – | (42,530) | 1,173,073 |
| Deferred income tax assets | 660,598 | 1,956,310 | 43,065 | 2,659,973 |
| Other noncurrent assets | 1,243,075 | 2,180,351 | – | 3,423,426 |
| **Total Noncurrent Assets** | 43,378,315 | 258,655,846 | 535 | 302,034,696 |
| **TOTAL ASSETS** | ₱97,598,710 | ₱517,552,914 | (₱925,680) | ₱614,225,944 |
| **LIABILITIES AND EQUITY** | | | | |
| **Current Liabilities** | | | | |
| Deposit liabilities | ₱– | ₱358,462,436 | ₱– | ₱358,462,436 |
| Financial liabilities at fair value through profit or loss | – | 389,817 | – | 389,817 |
| Bills and acceptances payable | – | 17,256,919 | – | 17,256,919 |
| Short-term debts | 1,870,000 | 4,247,306 | – | 6,117,306 |
| Accounts payable and other liabilities | 7,805,513 | 4,161,661 | – | 11,967,174 |
| Income tax payable | 236,519 | 153 | – | 236,672 |
| Customers' deposits | 2,626,388 | – | – | 2,626,388 |
| Current portion of long-term debts | 2,741,143 | – | – | 2,741,143 |
| Current portion of due to related parties | 20,503,550 | 16,515,304 | – | 37,018,854 |
| Other current liabilities | – | 21,650,833 | (11,945) | 21,638,888 |
| **Total Current Liabilities** | 35,783,113 | 422,684,429 | (11,945) | 458,455,597 |
| **Noncurrent Liabilities** | | | | |
| Deposit liabilities - net of current portion | – | 24,805,196 | – | 24,805,196 |
| Financial liabilities at fair value through profit or loss | – | 6,196,070 | – | 6,196,070 |
| Bills and acceptances payable | – | 328,654 | – | 328,654 |
| Long-term debts - net of current portion | 5,873,432 | 7,486,078 | – | 13,359,510 |
| Accrued retirement benefits | 534,044 | (436,548) | 758,322 | 855,818 |
| Deferred tax liabilities | 1,329,722 | 1,049,310 | (66,226) | 2,312,806 |
| Other noncurrent liabilities | 1,468,333 | 5,748,161 | – | 7,216,494 |
| **Total Noncurrent Liabilities** | 9,205,531 | 45,176,921 | 692,096 | 55,074,548 |
| **Total Liabilities** | 44,988,644 | 467,861,350 | 680,151 | 513,530,145 |
| **Equity** | | | | |
| Equity attributable to equity holders of the parent company: | | | | |
| Capital stock | 8,981,389 | – | – | 8,981,389 |
| Capital in excess of par | 1,173,772 | – | – | 1,173,772 |
| Other comprehensive income | 4,993,008 | 10,675,819 | (2,411,506) | 13,257,321 |
| Other equity reserves | 270,416 | 850,285 | – | 1,120,701 |
| Retained earnings | 31,337,931 | 5,448,573 | 1,452,321 | 38,238,825 |
| | 46,756,516 | 16,974,677 | (959,185) | 62,772,008 |
| Non-controlling interests | 5,853,550 | 32,716,887 | (646,646) | 37,923,791 |
| **Total Equity** | 52,610,066 | 49,691,564 | (1,605,831) | 100,695,799 |
| **TOTAL LIABILITIES AND EQUITY** | ₱97,598,710 | ₱517,552,914 | (₱925,680) | ₱614,225,944 |

## 26. Seasonality of Operations

The sales of the beverage segment are affected by the weather, generally being higher in the hot, dry months from March through June and lower during the wetter monsoon months or July through October. Beverage products also tend to experience a period of higher sales around the Christmas and New Year holiday period in late December through early January. The beverage segment adjusts its production levels to reflect its historical experience of seasonal varieties. In addition, the Philippines is at risk from typhoons during the monsoon period. Typhoons usually result in substantially reduced sales in the affected area, and have, in the past, interrupted production at the beverage segment's plants in affected areas. While these factors lead to a natural seasonality in our sales, unreasonable weather could also significantly affect sales and profitability compared to previous comparable periods.

Demand for rum, spirit beverages and liquor products are not significantly influences by seasons of the year. The increase in peso sales was due to increase in selling price during the period. The seasonality does not significantly influence production and inventory levels are adjusted for these movements in demands. Seasonality does not impact the revenue or cost recognition policies of the Group.

This information is provided to allow for a proper appreciation of the results, however management have concluded that this does not constitute "highly seasonal" as considered by PAS 34, *Interim Financial Reporting*.

There are no seasonal aspects that had a material effect on the financial position or condition and results of operations of the distilled spirits and tobacco segments.

## 27. The Nature and Amount of Items Affecting Assets, Liabilities, Equity, Net Income, or Cash Flows that are Unusual Because of their Nature, Size or Incidence

Other than those disclosed in Note 1 related to the Group restructuring, there are no unusual items that will significantly affect the assets, liabilities, equity, net income or cash flows.

## 28. The Nature and Amount of Changes in Estimates of Amounts Reported in Prior Interim Period of the Current Year or Changes in Estimates of Amounts Reported in Prior Years, if those Changes Have a Material Effect in the Current Interim Period

There are no significant changes in estimated reported in prior interim periods of the current period or changes in estimated reported in prior years, which are considered to have material effect on the interim consolidated financial statements.

**LT GROUP, INC. AND SUBSIDIARIES**
**SELECTED EXPLANATORY NOTES**
**As at June 30, 2013 and December 31, 2012**
**And for the Six Months Ended June 30, 2013 and 2012**
(As required under Par. 7 (d) Selected Explanatory Notes Required Under SRC Rule 68, as Amended 2011)

i.) The Company's interim consolidated financial reports are in compliance with Generally Accepted Accounting Principles. The same accounting policies and methods of computation are followed in the interim financial statements as compared with the most recent annual financial statements.

The Company's interim consolidated financial statements have been prepared in accordance with Philippine Financial Reporting Standards (PFRS).

ii.) Explanatory comments about the seasonality or cyclicality of interim operation;

Beverage Segment is affected by seasonality of operations.

The sales of the beverage segment are affected by the weather, generally being higher in the hot, dry months from March through June and lower during the wetter monsoon months or July through October. Beverage products also tend to experience a period of higher sales around the Christmas and New Year holiday period in late December through early January. The beverage segment adjusts its production levels to reflect its historical experience of seasonal varieties. In addition, the Philippines is at risk from typhoons during the monsoon period. Typhoons usually result in substantially reduced sales in the affected area, and have, in the past, interrupted production at the beverage segment's plants in affected areas. While these factors lead to a natural seasonality in our sales, unreasonable weather could also significantly affect sales and profitability compared to previous comparable periods. This information is provided to allow for a proper appreciation of the results, however management have concluded that this does not constitute "highly seasonal" as considered by PAS 34, *Interim Financial Reporting*. There are no seasonal aspects that had a material effect on the financial position or condition and results of operations of the distilled spirits and tobacco segments.

iii.) The nature and amount of items affecting assets, liabilities, equity, net income, or cash flows that is unusual because of their nature, size, or incidents.

After a series of restructuring activities in 2012 and 2013, the Company was able to consolidate certain businesses of the controlling stockholder to LTG. The current portfolio comprises interests in the following companies:

- **Distilled Spirits**—the Company conducts its distilled spirits business through its 100%-owned subsidiary TDI.
- **Beverage**—the Company conducts its beverage business through its 99.9%-owned subsidiary, Asia Brewery, Inc. (ABI).
- **Tobacco**—the Company conducts its tobacco business through its 99.6% ownership in Fortune Tobacco Corporation (FTC), which in turn owns 49.6% of PMFTC, a company formed in 2010 as a result of business combination between Philip Morris Philippines Manufacturing, Inc. (PMPMI) and FTC.
- **Property Development**—the Company conducts its property development business through Paramount Landequities, Inc. and Saturn Holdings, Inc. resulting to an effective ownership of 99.3% in Eton Properties Philippines, Inc. (ETON).

- **Banking**—the Company conducts its banking business through the 17 local holding companies resulting to an effective ownership of 45.5% in Philippine National Bank (PNB) and Allied Banking Corporation (ABC) as of June 30, 2013.

The material items affecting assets, liabilities, equity, net income, or cash flows that are unusual because of their nature, size, or incidents are included in the Management discussion and analysis of the report.

iv.) Nature and amount of changes in estimates of amounts reported in prior interim periods of the current financial year or changes in estimates of amounts reported in prior financial years, if those changes have a material effect in the current interim period

Not Applicable. There were no changes in estimates of amounts reported in prior interim periods of the current financial year or changes in estimates of amounts reported in prior financial years.

v.) Issuances, repurchases, and repayments of debt and equity securities.

On April 17, 2013, the Company executed the Placing Agreement for the placing transaction with Tangent offering shares of 1.840 billion shares including 240 million shares for the over-allotment option. The offer price was set at ₱20.50.

On May 9, 2013, Tangent subscribed and paid the 1.840 billion shares thereby increasing LTG's total and outstanding shares from 8.9 billion to 10.8 billion shares.

vi.) Dividends paid (aggregate or per share) separately for ordinary shares and other shares.

On June 19, 2013, the Board of Directors of LTG approved the declaration and distribution of cash dividends of ₱0.15 per share to all stockholders of record as of July 3, 2013. The dividends were paid on July 29, 2013.

On December 20, 2011, the Board of Directors of LTG approved the declaration and distribution of cash dividends of ₱ 0.20 to all stockholders of record as of January 5, 2012. The said cash dividends were paid on February 1, 2012.

vii.) Segment revenue and segment result for business segments or geographical segments, whichever is the issuer's primary basis of segment.

Please refer to Note 4 – Segment Information, in the interim consolidated financial statements.

viii.) Material events subsequent to the end of the interim period that have not been reflected in the financial statements for the interim period;

*Acquisition of Philippine National Bank (PNB) and Allied Banking Corporation (ABC)*
On February 11, 2013, LTG's BOD approved the acquisition of indirect ownership interest in the Merged PNB through the investment in the 27 holding companies which have collective ownership interest in the Merged PNB of 59.8% (collectively referred to as "Bank Holding Companies"). LTG's acquisition of the Bank Holding Companies will be effected by way of subscription to the increase in authorized shares of the Bank Holding Companies and acquisition of the Bank Holding Companies' shares owned by the Controlling Shareholders.

In various dates in February and March 2013, upon approval of the SEC for the increase in authorized capital stock of certain Bank Holding Companies, LTG has acquired between 80% to

100% ownership of these Bank Holding Companies. The transactions were consummated through conversion of LTG's advances from the Bank Holding Companies in exchange for the shares acquired. As of June 30, 2013, LTG obtained majority ownership over certain Bank Holding Companies which collectively own direct ownership interest of 45.5% of the Merged PNB. As of August 13, 2013, LTG is currently obtaining the requisite regulatory approval to increase its stake in PNB to 59.8%.

ix.) The effect of changes in the composition of the issuer during the interim period, including business combinations, acquisition or disposal of subsidiaries and long-term investments, restructurings, and discontinuing operations.

The banks were now included in the interim report to the extent of 45.5%. The pooling of interest method was used for the business combination.

x.) Changes in contingent liabilities or contingent assets since the last annual balance sheet date.

Not Applicable. The Company has no contingent liabilities or assets.

xi.) Existence of material contingencies and any other events or transactions that are material to an understanding of the current interim period.

***Banks***

PNB

In the normal course of business, the PNB Group makes various commitments and incurs certain contingent liabilities that are not presented in the financial statements including several suits and claims which remain unsettled. No specific disclosures on such unsettled assets and claims are made because any such specific disclosures would prejudice the PNB Group's position with the other parties with whom it is in dispute. Such exemption from disclosures is allowed under PAS 37, *Provisions, Contingent Liabilities and Contingent Assets.* The PNB Group and its legal counsel believe that any losses arising from these contingencies which are not specifically provided for will not have a material adverse effect on the financial statements.

Allied Bank

Allied Bank is a party in legal proceedings which arise in the ordinary course of its business activities. Allied Bank believes that none of such legal proceedings arising in the ordinary course, either individually or in the aggregate, are expected to have a material adverse effect on Allied Bank or its consolidated financial condition.

On June 19, 1986, the PCGG sequestered shares of stock in Allied Bank. In response, Allied Bank and concerned stockholders instituted a special civil action (G.R. No. 75643) before the Supreme Court praying for the nullification of the above writs of sequestration. On February 15, 1990, the Supreme Court referred the action, together with related parties, to the Sandiganbayan, the Philippine anti-graft court, for appropriate disposition. In its Joint Decision of March 2, 2006, the Sandiganbayan nullified the writs of sequestration over, among others, shares of stock of Allied Bank. With its motion for reconsideration of the decision having been denied, the PCGG appealed to the Supreme Court through a petition for review. The Supreme Court affirmed the decision of the Sandiganbayan on December 7, 2007, and PCGG's motion for reconsideration was thereafter denied. On January 29, 2008, the Supreme Court ruled with finality on the lifting of the writs of sequestration.

On December 19, 2008, the Republic of the Philippines, through the office of the Solicitor General, filed before the Sandiganbayan Civil Case No. 0005, entitled *Republic v. Lucio Tan, et. al.*, an Application for the Issuance of a Temporary Restraining Order and/or Writ of

Preliminary Injunction, seeking to enjoin the merger of Allied Bank and PNB. The Sandiganbayan, in its Resolution of March 19, 2009, however, denied said application. On January 2010, Allied Bank received the Resolution of December 18, 2009 issued by the Sandiganbayan denying the motion for reconsideration of the Office of the Solicitor General.

On February 20, 2012, the PCGG again filed before the SEC its opposition to the merger, the primary basis of which was the pending resolution of the "ill-gotten wealth" case filed against Dr. Lucio C. Tan, identified as Civil Case No. 0005. The PCGG alleged the following: i.) there was no compliance with Sec. 77 of the Corporation Code; ii.) there was a violation of Sec. 2 of EO No. 2 Series of 1986; and iii.) there was no prior approval from the Sandiganbayan. Since there has been no determination or resolution on Civil Case No. 0005, it was alleged that the Republic of the Philippines will be disadvantaged by the proposed merger. By denying the issuance of the Temporary Restraining Order the SEC noted that the Sandiganbayan impliedly gave its approval for the merger.

On June 11, 2012, the Sandiganbayan finally issued its resolution dismissing the "ill-gotten wealth" case against Dr. Lucio C. Tan and finally disposing of Civil Case No. 0005. The SEC on the other hand, issued its order on September 6, 2012 denying the opposition of the PCGG to the merger of Allied Bank and PNB.

The PCGG requested that Dr. Lucio C. Tan's shares of Allied Bank be tagged pending further appeals. Allied Bank complied with the request, tagging a total of 354,419 common shares in Allied Bank. Upon completion of the merger between Allied Bank and PNB, wherein the Allied Bank share were exchanged for PNB shares, the PNB shares thus received by Dr. Lucio C. Tan were also tagged.

On October 30, 2012, the PCGG filed a petition G.R. No. 203592 before the Supreme Court to overturn the Sandiganbayan's resolution dismissing the case against Dr. Lucio C. Tan. On March 18, 2013, the Republic of the Philippines filed a motion before the Supreme Court requesting that Allied Bank and all of its assets be placed in court custody, asserting that Allied Bank shares were substantially diluted as part of its merger with PNB and demanding an explanation for this dilution, and requesting the substitution of PNB in lieu of Allied Bank when appropriate. The Supreme Court has not yet taken action with respect to this motion and the petition remains pending.

***<u>Beverage</u>***

ABI maintains a legal department whose main function is to pursue collection cases and handle litigation arising from labor disputes. As of June 30, 2013, ABI does not have any significant legal proceedings either against it or in pursuit of another party besides those arising from the ordinary course of business.

***<u>Distilled Spirits</u>***

In the ordinary course of business, TDI is a party to various legal actions that it believes are routine and incidental to the operation of its business. In the opinion of TDI's management, the outcome and potential liability of these aforementioned legal actions are not likely to have a materially adverse effect on TDI's business, financial condition and results of operations.

Legal actions that may have a materially adverse effect on TDI's business, financial condition and results of operations include a P100 million civil infringement suit filed by GSMI, a cease and desist order filed by the DENR against AAC and a realty tax assessment from the Provincial Assessor of Negros Occidental.

- **GSMI Litigation**
  On August 15, 2003, GSMI filed a trademark infringement lawsuit with the Regional Trial Court ("RTC") of Mandaluyong City, challenging TDI's launch of *GinebraKapitan*(now called "*Gin Kapitan*"), a gin product which allegedly has a "confusing similarity" with GSMI's principal gin product. GSMI obtained a temporary restraining order ("TRO") preventing TDI from using the *GinebraKapitan*name. The TRO was nullified with finality by the Supreme Court of the Philippines (the "Supreme Court") in November 2009 and TDI was allowed to continue to use the brand name *GinebraKapitan*. The Supreme Court ruled that there was no basis for the issuance of an injunction restraining TDI from using *GinebraKapitan*as a trademark for its gin products. The IPO also ruled in favor of TDI by declaring that GSMI could not claim ownership over the Ginebra name, as it was generic in nature.

  On July 31, 2012, the RTC of Mandaluyong City dismissed the charges of infringement and unfair competition against TDI. The court also sustained TDI's position that Ginebra is a generic name, free for all to use. The RTC also sustained TDI's claim that there is no confusing similarity between GSMI's *Ginebra San Miguel* brand and TDI's *GinebraKapitan*brand. GSMI's motion for reconsideration of the decision was denied.

- **DENR Administrative Proceedings**
  On July 22, 2008, the DENR issued a cease and desist order against AAC upon the request of the Pollution Adjudication Board ("PAB") for failure to meet environmental standards. AAC immediately filed and was granted a temporary lifting order in exchange for agreeing to implement immediate and long-term remedial measures. Despite AAC's implementation of remedial measures, the residents and local government of Pulupandan, where AAC's distillation plant is located, protested against AAC operations and at one point took measures to barricade access to the plant. AAC temporarily suspended operations in June 2009 when an essential water pipeline was damaged allegedly during a road improvement project by the local government. AAC obtained a renewal for its temporary lifting order from the PAB and as a result AAC was able to obtain a permit from the Pulupandan local government to fix its damaged water pipeline. Further, AAC has removed and transferred its new distillery columns, which were to be used for its previous expansion plans, to ADI's plant in Batangas where expansion will now instead be pursued. As of the date of this Offering Circular, while there is nothing that would prevent AAC from operating its distillation plant, AAC is currently evaluating whether or not to recommence operations.

- **Realty Tax Assessments**
  On August 25, 2010, AAC received a Notice of Assessment from the Provincial Assessor of Negros Occidental representing deficiency realty taxes for the period from 1997 to 2009 totaling P263.7 million. AAC formally protested the assessment on multiple grounds. As of June 30, 2013, the case remains pending.

***Property Development***

Eton is involved in litigation in the normal course of its business, and it believes none of these litigations, if resolved unfavorably, would have a material adverse effect on its operations.

***Tobacco***

- **Sandiganbayan case against Tan Companies**
  On June 6, 2011, a motion was submitted by the Government seeking to include PMFTC and its directors/officers as additional defendants in the forfeiture case pending before the Sandiganbayan against Mr. Lucio C. Tan, FTC, et al. since 1987. The Government claims

that by transferring the assets owned by FTC to PMFTC as a result of the business combination, the FTC assets have been removed beyond the reach of the Government and the court. The Sandiganbayan denied this motion with finality on August 2011, ruling that they are not necessary or indispensable parties under the law. In a decision in June 2012, the Sandiganbayan also dismissed the forfeiture case against all the defendants for failure of the Government to prove that the assets that formed the subject of the case were ill-gotten wealth. The Government's motion for reconsideration was likewise denied in September 2012. The Government is currently appealing this decision to the Supreme Court.

**Annex "B"**

# LT GROUP, INC.
# (Formerly Tanduay Holdings, Inc.)
# AND SUBSIDIARIES

Management Discussion and Analysis of
Financial Condition and Results of Operations

## PART I - FINANCIAL INFORMATION

### Item 1. Financial Statements.

The financial statements are filed as part of this Form 17-Q

### Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

**RESULTS OF OPERATIONS**

The consolidated net income of LT Group, Inc (LTG) for the six months ended June 30, 2013 amounted to ₱9.5 billion, a significant increase of 34.6% or ₱2.4 billion from ₱7.1 billion the previous period while net income attributable to equity holders of LTG increased from ₱5.2 billion to ₱6.1 billion. The growth in net income mainly came from the banking segment, which reported a net income higher by ₱2.9 billion compared with last year. The property and beverage segments also contributed to the growth with an improvement in their net income by ₱237.5 million and ₱ 43.3million, respectively. The tobacco segment reported lower earnings and the distilled spirits reported a net loss, but these were outweighed by the good performances of the other 3 segments.

Consolidated revenues grew by 5.4% from ₱30.2 billion in 2012 to ₱31.8 billion for the same six-month period ended June 30, 2013. Although the revenues of the beverage, distilled spirits, and tobacco segments declined by 10.7%, 15.3% and 87.3%, respectively, these were offset by the 19.4% higher revenues of the banking segment and 161.2% increase of the property development sector. The impact of the new excise tax law was finally seen in both beverage and distilled spirits' lower sales volume. And while revenues of the tobacco segment declined due to the transfer of its operations to PMFTC, it was also affected by higher excise taxes which resulted to lower equity in net earnings in PMFTC. The declines were offset by the banking sector due to higher trading and investment securities gains as it took advantage of the good equity market of the Philippines. The property showed better revenues on account of higher percentage of completion of its residential and condominium projects.

Cost of sales declined by 10.8% from ₱14.7 billion for the period ended June 30, 2012 to ₱13.1 billion for the same period in 2013, mainly due to the bank's lower interest expenses on deposit liabilities. Lower volumes also caused the decline in cost of sales of the beverages, distilled spirits and tobacco segments by 1.1%, 12.2% and 86.4%, respectively. Property development reported 208.9% higher cost of sales mainly resulting from higher percentage of completion on construction projects.

Operating expenses decreased by 1.9%, due to lower selling and general expenses by 3.2% and 1.7%, respectively.

Provision for income tax increased by 58%, on account of the group's higher revenues.

#### Banking

The banking segment's consolidated net income almost doubled from ₱3.2 billion for the six-month period ended June 30, 2012 to ₱6 billion this year. The banking segment attributed its improved performance to the country's strong and favorable economic environment that created numerous business opportunities which drove a more robust trading and investment market.

Net interest income for 2013 was ₱6.5 billion, or 10.5% lower than last year's ₱7.3 billion. Interest income declined by 10.6% or ₱1.1 billion, mainly as a result of PNB's sale of certain investment securities and lower yields on certain investments. Interest expense also decreased by 10.6% or ₱365.9

million to ₱3.1 billion in 2013, on account of lower average rates on deposits and lesser payables for the banks. Net interest margin ratio declined to 2.5% from 3.0% a year ago.

Net service fees and commission income grew by 15.9% from ₱1.1 billion in 2012 to ₱1.3 billion for the same period in 2013.

The biggest contribution to the growth of income is the gain in trading and investment securities which increased by 118.3%. It more than doubled and grew from ₱3.3 billion in 2012 to ₱7.3 billion in 2013, mainly attributed to trading gains on investment securities. Foreign exchange gains increased by 6.2%, from ₱651.6 million in 2012 to ₱692.0 million in 2013. On the other hand, both net gain on sale or exchange of assets and miscellaneous income both declined by 13.8% and 7.3%, from ₱291.6 million in 2012 to ₱251.4 million in 2013 and from ₱1.5 billion in 2012 to ₱1.4 billion in 2013, respectively.

Operating expenses declined by 3%, from ₱10.2 billion in 2012 to ₱9.9 billion in 2013, with the bulk coming from lower provision for impairment and credit losses which declined by 22.1% from ₱ 1,017.8 million in 2012 to ₱793.1 million in 2013.

Provision for income tax for the six months ended June 30, 2013 increased by 97.0%, from ₱710.0 million in 2012 to ₱1,398.6 million in 2013 due to higher revenues during the current period.

**Beverage**

Net income of the beverage segment grew by 12.0% from ₱431.0 million for the six months ended June 30, 2012 to ₱482.7 million for the same period ended June 30, 2013.

Revenues declined by 1.3% or ₱90.3 million from ₱6.9 billion for the six month period ended June 30, 2012 to ₱6.8 billion for the same period this year, primarily due to lower sales volume of ABI's products that were affected by the excise tax increase like beer, Tanduay Ice and commercial bottles. This negated the increase in revenues from bottled water energy drinks and dairy products.Alcoholic drinks like beer and alcopops declined by 14% and 46% on account of the 7% to 11% average increase in selling prices to cover the increase in excise tax. Volumes for bottled water and Vitamilk increased by 17% and 9% while sales of energy drinks declined by 5.8% due to increase in selling prices by 10.4%.

Cost of sales, in line with the movement of revenues, decreased by 1.1% from ₱4.9 billion in 2012 to ₱4.8 billion in 2013.

Operating expenses decreased by 3.7% or ₱50.9 million from ₱1.4 billion in 2012 to ₱1.3 billion in 2013, with both selling & general and administrative expenses declining by 2.6% and 6.3%, respectively. Lower selling expenses was due to the reclassification of depreciation, while the decrease in general and administrative expenses was due to the reclassification of management and professional fees coupled with lower retirement benefit costs.

The decrease by 50.0% in other charges was due to the settlement of bank loans amounting to ₱1.87 billion which lowered interest expense by ₱31.9 million.

**Distilled Spirits**

The net revenues of the distilled spirits segment is lower by 15.3% or ₱0.9 billion from ₱5.8 billion in 2012 to ₱4.9 billion in 2013. The effects of higher excise taxes on alcoholic beverages continue to affect the segment, resulting in a 25% decline in sales volume in the second quarter which negated the

10% increase in average selling prices. The top 3 products are Tanduay Five Years, Tanduay Light and ESQ, with each having 64%, 17% and 10% of the product mix, respectively.

The economic situation in Southern Philippines, a predominantly agriculture-based area and a Tanduay stronghold, has not yet fully recovered from the impact of bad weather conditions.

Movement of cost of sales is consistent with revenues. A decrease of 12.2% from ₱4.4 billion in 2012 to ₱3.9 billion in 2013 was reported, also as a result of decline in sales volume. Gross profit is lower, from 24% to 21% due to increase in cost of alcohol and excise tax.

Operating expenses grew by 25.5% from ₱570.4 million in 2012 to ₱715.9 million in 2013, with the 62.8% increase in general and administrative expenses offsetting the 9.8% decrease in selling expenses. The general and administrative expenses was higher by ₱174.2 million mainly due to separation benefits in connection with the closing of the Quiapo plant effective April 1, 2013.

Other charges increased by 68.3% or ₱129.3 million in 2013 primarily as a result of the one-off ₱120 million fair value adjustment on the claim for refund of excess taxes paid. This amount will be reverted to the principal amount each year and booked as income over the expected recovery period of the claim.

Core income of the distilled spirits segment is ₱150 million. But with the one-off expenses, the segment incurred a net loss of ₱75.0 million in 2013 from the net income of ₱400.0 million in 2012.

**Property Development**

The property development segment posted a 718.7% increase in net income from a net loss ₱33.0 million for the six months ended June 30, 2012 to ₱204.4 million for the period ended June 30, 2013.

Revenues increased by 161.2% from ₱824.8 million in June 2012 to ₱2.2 billion in June 2013. The positive movement was primarily due to the higher percentages of completion of its projects. While revenues from leasing increased by 18.3% this year, a big chunk of the higher revenues came from the segment's residential projects, mainly high rise condominiums Eton Tower Makati in the Makati central business district and 8 Adriatico in Manila, horizontal projects 68 Roces, West Wing Residences and West Wing Villas at North Belton Communities and mid-rise buildings in The Manors at North Belton Communities in Quezon City. The West Wing Residences in Eton City, the segment's flagship township project in Sta. Rosa Laguna, is also ongoing. Plan to increase leasing income was reflected in the construction of CentrisCyperpod Three, the third Business Process Outsourcing (BPO) office building in Eton Centris in Quezon City.

Cost of sales followed the pattern of revenues as it increased by 208.9% from ₱476.7 million in 2012 to ₱1,472.3 million in 2013, also on account of higher completion percentages on its residential and condominium projects as well as higher construction costs.

Operating expenses increased by 7.2% from ₱433.6 million in 2012 to ₱464.7 million this year. Selling expenses grew by 4.4%, as a result of higher commissions, while general and administrative expenses increased by 9.2%, mainly on account of higher taxes and licenses on bank loans, occupancy and repairs and maintenance expenses.

**Tobacco**

The tobacco segment's net income declined from ₱3.1 billion in 2012 to ₱2.6 billion for the six months period ending June 30, 2013, primarily as a result of 28.5% lower equity in net earnings from PMFTC.

The tobacco segment ceased its manufacturing operations, effective January 1, 2013, after completing its Contract Manufacturing Agreement (CMA) with JTI in December 2012 and transferred the CMA to PMFTC, FTC's 49.6%-owned subsidiary. Consequently, revenues declined by 87.3% from ₱ 1,241.1 million in 2012 to ₱157.2 million in 2013, mainly on account of the segment's sale of all its remaining inventories to JTI and PMFTC on February.

A drop of 86.4% was seen in cost of sales, from ₱1,139.3 million in 2012 to ₱154.2 million in 2013, on account of the termination of FTC's manufacturing operations which also resulted in the decrease in operating expenses by ₱171.6 million, from ₱191.2 million in 2012 to ₱19.6 million in 2013.

## FINANCIAL CONDITION

LT Group's total consolidated assets as of June 30, 2013 increased by 11.5% to ₱667.6 billion from ₱614.2 billion as of December 31, 2012 attributable mainly to the increase in current assets by 34.1% offsetting the 17.6% decrease in non-current assets.

The increase in current assets by ₱106.6 billion was mainly on account of the reclassification of Available-for-sale Financial Assets from noncurrent to current and net acquisitions of various securities of the banking segment, and higher cash and cash equivalents. The increase in cash and cash equivalents by 38.7% resulted primarily from higher deposits with BSP of the banking segment and the proceeds coming from the equity offering by LT Group. Other movements in current assets are lower banking loans and receivables which went down by 9.1% on account of the decline in interbank lending to various foreign banks, lower financial assets and decline in inventories of the distilled spirits segment.

Total noncurrent assets decreased by ₱53.1 billion, mainly on account of the abovementioned reclassification of Available-for-sale Financial Assets. Loans and receivables grew by 15.4% on account of new loan releases and corporate accounts in the banking segment.

Consolidated total liabilities as of June 30, 2013 decreased by ₱1.7 billion from ₱513.5 billion as of December 31, 2012 to ₱511.8 billion as of June 30, 2013. Total current liabilities increased by 2.9% due mainly to the reclassification of due to related parties to current as a result of the assignment of some payables to Tangent Holdings Corporation. Import bills payables declined by 59.2% as a result of the banking segment's settlement of various borrowings. Short-term debts was lower by 100% due to payments made by the beverage segment during the period. The 27.1% decrease in noncurrent liabilities is primarily due to the aforementioned reclassification of due to related parties. Deferred income tax liabilities declined by 35.8%.

LTG's consolidated total equity increased by 54.7% from ₱100.7 billion to ₱155.8 billion for the period ended June 30, 2013. This was primarily attributable to the Company's share offering in April 2013 which raised ₱37.7 billion.

**LTGI's top five (5) key performance indicators are described as follows:**

**1.) Revenue**

Revenues for June 30, 2013 is higher by 5% from last year's amount of ₱30.2 billion.

**2.) Net Income**

Consolidated Net Income for June 2013 amounted to ₱9.5 billion higher by 35% from last period's ₱7 billion.

**3.) Current Ratio**

Current ratio increased from 0.68:1 in December 2012 to 0.89:1 in June 2013.

**4.) Debt to Equity Ratio**

Debt-to-equity ratio declined from 5.10:1 in December 2012 to 3:29:1 in June 2013.

**5.) Earnings/ (Loss) Per Share**

LTGI's earnings per share attributable to holders of the parent company for June 2013 and June 2012 are ₱0.601 and ₱0.600, respectively.

The manner by which the Company calculates the above indicator is as follows:

Debt to equity ratio – Total Liabilities / Total Equity
Current ratio – Current assets / Current Liabilities
Earnings per share – Net Income attributable to holders of parent company / Common shares outstanding

Trends, Uncertainties or Contingencies That will Affect Liquidity In The Next Twelve Months:

(I) On September 24, 2012, the Company's stockholders approved the 2-tranche Placement and Subscription Transaction involving the sale by Tangent of up to, but not exceeding 3,000,000,000 common shares of the Company registered in its name to investors by way of a follow-on offering at a placing price to be determined through a book building exercise to be hereafter conducted (the "Placing Tranche") and the subsequent subscription by Tangent using the proceeds of the Placing Tranche (net of expenses incurred in the Placing Tranche) to new shares of the Company in an amount equivalent to the number of shares sold during the Placing Tranche at an issue price equivalent to the placing price (the "Subscription Tranche"). The total number of the shares subject of the Placing Tranche shall be determined based on investor demand as determined through a book building exercise, provided the same shall not exceed 3,000,000,000 shares and the total number of subscription shares shall not exceed the shares sold in the Placing Tranche. The BOD was granted authority to determine such other terms and conditions of the transaction as may be most beneficial to the Company, including (but not limited to) the timing of the same and total funds to be raised therefrom.

On April 17, 2013, the Placing Agreement for the placing transaction had been executed. The offer shares consist of 1,600,000,000 shares of the Company and up to 240,000,000 shares for the over-allotment option. The offer price for the offer shares had been set at P20.50 per offer share. The Placing and Subscription Transaction allows the Company to raise capital in a most expeditious and efficient manner with the least cost, for the growth and expansion of its subsidiaries. The transaction is also intended to strengthen and broaden the capital base of the Company, as well as to promote a wider dispersion of the common shares to a broad spectrum of public institutional investors, and to comply with the requirement for a minimum public ownership of a listed company on the Philippine Stock Exchange (PSE).

On April 23 and 26, 2013, net proceeds amounting to P37billion were received by the Company. LTG intends to use the proceeds of the Subscription as follows:

a. Up to 35% of the proceeds for organic growth initiatives at ABI, TDI and ETON;
b. Up to 30% of the proceeds to support growth of the banking business;
c. Up to 30% of the proceeds for repayment of certain indebtedness of certain LTG companies as part of the LTG's corporate reorganization; and
d. Any remainder for general corporate purposes.

Except for the above transaction, there are no other trends or any known demands, commitments, events or uncertainties that will result in or that are reasonably likely to result in the Group's increasing or decreasing liquidity in any material way. The Group is not in default or breach of any note, loan, lease or other indebtedness or financing arrangement requiring it to make payments. The Company does not have any liquidity problems.

(i) There are no events that will trigger direct or contingent financial obligation that is material to the company and its subsidiaries, including any default or acceleration of an obligation.

(ii) There are no known material off-balance sheet transactions, arrangements, obligations (including contingent obligations), and other relationships of the company and its subsidiaries with unconsolidated entities or other persons created during the reporting period.

(iii) The Group has on-going and planned capital expenditure projects as follows:

***Distilled Spirits***

**Expansion of Absolut Distillers**

In September 2012, TDI increased ADI's capacity of 75,000 liters of ethyl alcohol per day to 175,000 liters per day with the addition of new distillation columns, expected to be fully operational by the second quarter of 2013. The project also includes the construction of an alcohol ageing plant with a capacity of 30,000 barrels. The upgrades will provide TDI with more high grade alcohol to be used in the production of new products for Luzon and export markets. The upgrades will also eliminate third party costs relating to the conversion of low grade alcohol to high grade alcohol and ensure a steady supply of high grade alcohol.

**Expansion of Negros Plant**

TDI has embarked on an additional expansion consisting of the construction of a finished goods and raw materials warehouse, and a new bottle sorting facility, all of which are expected to be completed in 2014.

**Rehabilitation of Asian Alcohol Plant**

TDI is currently contemplating possible other options for the plant, including shifting to production of ethanol or leasing the plant to a third party. The rehabilitation of the AAC Plant is currently under evaluation.

***Beverage***

In December, 2012, ABI commissioned a Polyethylene Terephthalate (PET) bottling plant at its Cagayan de Oro complex which is capable of producing both bottled water and carbonated softdrinks at a rated capacity of 15,000 bottles per hour. The fully integrated plant includes a water distillation facility to produce Absolute distilled water and a blow moulding equipment to produce all the PET bottle requirements of the plant. The new facility will be used to serve the growing demand for bottled water and carbonated softdrinks (CSD) in PET in the Mindanao and Visayas area and will result in substantial FTH savings.

The Company undertook major capex projects for its glass manufacturing and beer production facilities in order to improve production efficiencies.

In 2012, investments were made in returnable containers to both replace fully depreciated bottles/crates and to support increasing sales of Cobra Energy Drinks, Beer and alcopop drinks.

Various projects for 2013 also includes replenishment of returnable containers, rebuilding of glass furnace 4 and investment in cold fill and hot fill PET line fillers.

***Banks***

The Bank has commitments for capital expenditures. The Bank plans to purchase the hardware and software requirements needed for the implementation of information technology priority projects.Expected sources of funds for the projects will come from sale of acquired assets and funds generated from the Bank's operations.

(v.) Aside from the impact on the new law, R.A. 10351, which modified the applicable excise tax rates on alcohol and tobacco products including cigarettes effective January 1, 2013, the company has no known trends, events or uncertainties that have had or that are reasonably expected to have a material favorable or unfavorable impact on net sales, revenue or income from continuing operations.

(vi.) There are no other significant elements of income or loss that did not arise from the company's continuing operations.

(vii) The causes for any material change from period to period which shall include vertical and horizontal analyses of any material item;

Results of our Horizontal (H) and Vertical analyses (V) showed the following material changes:

1. Cash – H- 39%; V- 5%
2. Available-for-sale financial assets - current – H- 1164%; V- 11%
3. Financial assets at fair value through profit or loss – H- (17%)
4. Loans and receivables - current – H- (22%); V- (6%)
5. Due from related parties – H- 99%
6. Inventories – H- (13%)
7. Other non-current assets- H- 62%
8. Loans and receivables-noncurrent – H- 15%
9. Available-for-sale financial assets - noncurrent – H- (79%); V- (12%)
10. Deferred tax assets- H- (29%)
11. Other non-current assets- H- 21%
12. Financial liabilities at fair value through profit or loss – current – H- 1263%
13. Bills and acceptances payable - current – H- (59%)
14. Short term bank debts – H - (100%)

15. Accounts payable and accrued expense – H- (11%)
16. Income tax payable- H- 38%
17. Customer's deposit – H- 9%
18. Current portion of long-term debt – H- 227%
19. Current portion of due to related parties – H- 35%
20. Other current liabilities- H- 19%
21. Deposit liabilities – noncurrent – H- (16%)
22. Financial liabilities at fair value through profit or loss - noncurrent – H- (100%)
23. Long-term debt – net of current portion – H- (44%)
24. Accrued retirement liabilities- H- 11%
25. Deferred tax liabilities- H- (36%)
26. Other noncurrent liabilities- H- 22%
27. Capital stock- H- 20%
28. Capital in excess of par-H- 2960%; V- 5%
29. Other equity components- H- 225%
30. Retained earnings- H- (7%)
31. Non-controlling interests- H- 9%
32. Banking Revenue – H- 19%; V- 7%
33. Distilled Spirit Revenue– H- (15%)
34. Beverage Revenue - (11%)
35. Property development Revenue – H- 161%
36. Tobacco Revenue – H- (87%)
37. Equity in net earnings of associate-H- (28%)
38. Finance cost – H- (33%)
39. Finance income – H- 55%
40. Foreign exchange gains – H- 5%
41. Others-net – H- 19%
42. Net income- H- 35%; V- 6%
43. Total Comprehensive income – H- 135%

(viii) There are no seasonal aspects that have a material effect on the financial condition or results of operations of the Company.

**LT GROUP, INC. and SUBSIDIARIES**
**AGING OF ACCOUNTS RECEIVABLE**
**As of June 30, 2013 (Unaudited)**
(In thousands)

| TYPE OF ACCOUNTS RECEIVABLE | | TOTAL | CURRENT | 31-60 days | 61-90 days | 91-120 days | over 120 days |
|---|---|---|---|---|---|---|---|
| (a) Trade Receivable | | 254,388,778 | 4,228,604 | 1,948,233 | 1,553,731 | 71,250,714 | 175,407,495 |
| Less: Allowance for Doubtful Accounts | | 6,690,117 | - | - | - | - | 6,690,117 |
| NET TRADE RECEIVABLE | P | 247,698,660 | 4,228,604 | 1,948,233 | 1,553,731 | 71,250,714 | 168,717,377 |
| (b) Non-Trade Receivables | | 3,440,441 | 41,469 | 42,519 | 6,608 | 14,238 | 3,335,607 |
| Less: Allowance for Doubtful Accounts | | 596,041 | - | - | - | - | 596,041 |
| NET NON-TRADE RECEIVABLE | P | 2,844,401 | 41,469 | 42,519 | 6,608 | 14,238 | 2,739,567 |
| **NET RECEIVABLES** | P | 250,543,061 | 4,270,074 | 1,990,752 | 1,560,339 | 71,264,952 | 171,456,944 |

| ACCOUNTS RECEIVABLE DESCRIPTION | NATURE OF DESCRIPTION | COLLECTION PERIOD |
|---|---|---|
| Accounts Receivable - Trade | Sale of liquor, beer products, beverages, cigarettes and lease contract receivables | 30 to 90 days |
| Accounts Receivable - Non-Trade | Downpayment on various suppliers, advances to affiliates, officers and employees, other receivables | - |

**LT GROUP, INC. and Subsidiaries**
**FINANCIAL SOUNDNESS INDICATORS**

| | 30-Jun-13 | 31-Dec-12 |
|---|---|---|
| CURRENT RATIO | 0.89 | 0.68 |
| DEBT TO EQUITY RATIO | 3.29 | 5.10 |
| ASSET TO EQUITY RATIO | 4.29 | 6.10 |

| | 30-Jun-13 | 30-Jun-12 |
|---|---|---|
| INTEREST RATE COVERAGE RATIO | 53.12 | 26.25 |
| SOLVENCY RATIO | 0.69 | 0.43 |
| **PROFITABILITY RATIOS:** | | |
| PROFIT MARGIN | 0.19 | 0.17 |
| RETURN ON ASSET (ROA) | 0.009 | 0.008 |
| RETURN ON EQUITY (ROE) | 0.039 | 0.052 |