

DMCI HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 1997, 1996 AND 1995

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

The Stockholders and the Board of Directors
DMCI Holdings, Inc.

We have audited the accompanying consolidated balance sheets of DMCI Holdings, Inc. and subsidiaries as of December 31, 1997 and 1996, and the related consolidated statements of income and cash flows for each of the two years in the period ended December 31, 1997, and the ten months ended December 31, 1995. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1 to the consolidated financial statements, the Company was incorporated and started commercial operations on March 8, 1995.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of DMCI Holdings, Inc. and subsidiaries as of December 31, 1997 and 1996, and the results of their operations and their cash flows for each of the two years in the period ended December 31, 1997, and the ten months ended December 31, 1995, in conformity with generally accepted accounting principles.

PTR No. 1263516
January 15, 1998
Makati City

April 23, 1998

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

The Stockholders and the Board of Directors
DMCI Holdings, Inc.
DACON Building, 2281 Pasong Tamo Extension
Makati City

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LAURA SUAREZ ACUZAR
Partner
CPA Cert. No. 23390
PTR No. 1263516
January 15, 1998
Makati City

April 23, 1998

DMCI HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	December 31	
	1997	1996
ASSETS		
Current Assets		
Cash and cash equivalents	₱1,714,795,772	₱308,243,134
Marketable equity securities – net (Note 3)	31,131,229	50,432,591
Receivables – net (Notes 4 and 17)	5,381,334,126	3,465,879,932
Costs and estimated earnings in excess of billings on uncompleted contracts (Note 5)	38,182,542	52,270,172
Inventories (Note 6)	394,713,515	232,797,043
Prepaid expenses	40,742,380	34,801,577
Total Current Assets	7,600,899,564	4,144,424,449
Real Estate Held for Sale and Development (Notes 7 and 12)	2,155,517,703	1,073,121,637
Investments (Notes 8 and 12)	2,831,271,880	2,673,757,318
Property, Plant and Equipment - net (Notes 9 and 11)	4,537,347,137	1,782,875,008
Deferred Charges and Other Assets – net (Note 10)	290,265,729	77,797,906
	₱17,415,302,013	₱9,751,976,318
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Notes payable (Note 11)	₱292,136,554	₱128,365,515
Accounts payable and accrued expenses (Note 13)	3,322,929,043	1,224,811,699
Income tax payable	44,611,629	69,950,363
Acceptances and trust receipts payable (Notes 9 and 23)	475,434,489	257,077,910
Loans payable (Note 12)	416,823,490	344,575,504
Dividends payable (Note 19)	24,000,000	–
Subscriptions payable (Note 8)	90,000,000	90,000,000
Payables to affiliated companies (Note 17)	204,001,852	108,784,258
Deferred income tax – net (Note 16)	592,538,660	392,889,245
Total Current Liabilities	5,462,475,717	2,616,454,494
Billings in Excess of Costs and Estimated Earnings on Uncompleted Contracts (Note 5)	2,241,866,674	1,484,920,351
Non-Current Liabilities – net of current maturities of ₱72,539,360 (Note 15)	188,297,593	–
Subscriptions Payable - net of current portion of ₱90,000,000 (Note 8)	192,528,850	180,000,000
Customers' Deposits	117,042,324	–
Deferred Revenues and Credits (Notes 1 and 14)	534,789,349	211,089,427
Minority Interest	504,719,942	45,942,723
Stockholders' Equity		
Capital stock (Note 19)	2,257,894,000	1,127,747,000
Additional paid-in capital (Notes 8 and 19)	4,970,010,161	2,643,443,387
Retained earnings (Notes 8 and 20)	945,677,403	1,442,378,936
	8,173,581,564	5,213,569,323
	₱17,415,302,013	₱9,751,976,318

See accompanying Notes to Consolidated Financial Statements.

DMCI HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 1997 AND 1996
AND THE TEN MONTHS ENDED DECEMBER 31, 1995*

	1997 (One Year)	1996 (One Year)	1995 (Ten Months)
REVENUES			
Construction contracts	₱8,273,342,694	₱5,386,635,976	₱3,203,837,920
Coal sales (Note 21)	421,233,388	-	-
Real estate:			
Current year sales	-	920,957,863	278,537,220
Improvement revenues on prior years' sales	167,555,003	-	-
Merchandise sales	148,229,583	322,114,511	204,152,825
Equity in net earnings of unconsolidated affiliated companies (Note 8)	64,631,318	73,123,296	7,971,486
Interest and others	617,401,214	193,922,782	122,833,326
	9,692,393,200	6,896,754,428	3,817,332,777
COSTS AND EXPENSES			
Contract costs and expenses	6,882,463,877	4,452,836,176	2,589,836,462
Cost of coal sold	678,199,100	-	-
Real estate:			
Cost of current year sales	-	177,839,766	32,334,436
Improvement costs on prior years' sales	100,438,024	-	-
Cost of merchandise sold	122,028,800	258,966,533	163,144,108
General and administrative	586,625,544	360,521,094	272,592,838
Provisions for probable losses on assets and other charges (Notes 8 and 23)	347,432,306	131,529,154	-
	8,717,187,651	5,381,692,723	3,057,907,844
INCOME BEFORE INCOME TAX	975,205,549	1,515,061,705	759,424,933
PROVISION FOR INCOME TAX (Note 16)			
Current	176,045,823	305,984,351	149,797,681
Deferred	198,375,940	145,713,415	104,744,794
	374,421,763	451,697,766	254,542,475
INCOME BEFORE MINORITY INTEREST AND PREACQUISITION EARNINGS	600,783,786	1,063,363,939	504,882,458
MINORITY INTEREST	102,261,681	(13,039,639)	(10,404,277)
INCOME BEFORE PREACQUISITION EARNINGS	703,045,467	1,050,324,300	494,478,181
PREACQUISITION EARNINGS (Note 2)	-	-	(102,423,545)
NET INCOME	₱703,045,467	₱1,050,324,300	₱392,054,636
Earnings Per Common Share **			
Basic	₱0.28	₱0.47	₱0.24
Diluted (Note 19)	₱0.26	₱0.47	₱0.24

* The Company was incorporated and started commercial operations on March 8, 1995.

** Recomputed based on issued common shares after stock dividends declared on June 30, 1997.

See accompanying Notes to Consolidated Financial Statements.

DMCI HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 1997 AND 1996
AND THE TEN MONTHS ENDED DECEMBER 31, 1995*

	1997 (One Year)	1996 (One Year)	1995 (Ten Months)
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	P703,045,467	P1,050,324,300	P392,054,636
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation, depletion and amortization	772,999,509	284,161,800	112,359,040
Provisions for:			
Deferred income tax	198,375,940	145,713,415	104,744,794
Decline in value of marketable equity securities	19,301,362	19,806,462	-
Income (losses) applicable to minority interest	(102,261,681)	13,039,639	10,404,277
Equity in net earnings of unconsolidated affiliated Companies	(64,631,318)	(73,123,296)	(7,971,486)
Preacquisition earnings	-	-	102,423,545
Gain on sale of:			
Investments	(9,556,967)	(649,285,023)	(267,935,147)
Property, plant and equipment	(4,486,245)	-	-
Changes in operating assets and liabilities:			
Increase in:			
Receivables - net	(1,927,475,230)	(1,653,900,325)	(1,600,890,180)
Inventories - net	(161,916,472)	(129,605,050)	(103,191,993)
Prepaid expenses	(5,940,803)	(16,261,962)	(18,539,615)
Increase (decrease) in:			
Accounts payable and accrued expenses	2,098,117,344	644,549,520	636,212,830
Acceptances and trust receipts payable	218,356,579	113,067,075	144,010,835
Income tax payable	(25,338,734)	11,217,011	58,733,352
Payables to affiliated companies	212,259,918	77,592,873	31,191,385
Billings in excess of costs and estimated Earnings on uncompleted contracts - net	771,033,953	864,637,245	568,012,934
Deferred income tax - net	-	-	142,431,036
Net cash provided by operating activities	2,691,882,622	701,933,684	304,050,243
CASH FLOWS FROM INVESTING ACTIVITIES			
Proceeds on sale of:			
Investments	41,613,038	5,887,800	-
Property, plant and equipment	9,159,005	-	-
Real estate - net	-	677,715,743	300,129,654
Additions to:			
Property, plant and equipment	(3,192,574,004)	(1,233,144,546)	(975,894,096)
Real estate held for sale and development	(1,010,148,080)	(406,798,598)	(348,468,993)
Investments	(113,175,887)	(1,702,158,628)	(357,577,284)
Other assets	(202,700,822)	(41,802,092)	(38,756,438)
Marketable equity securities	-	(70,239,053)	-
Funds held by custodian bank	(12,851,015)	2,118,285,671	(2,174,560,112)
Net cash used in investing activities	(4,480,677,765)	(652,253,703)	(3,595,127,269)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from issuance of capital stock - net	2,328,966,774	-	3,398,775,857
Contributions from minority interest	573,062,375	-	22,998,807
Availments of:			
Non-current liabilities	188,297,593	-	-
Notes payable	163,771,039	-	-
Bank loans	-	84,965,515	43,400,000
Dividends paid on preferred shares	(48,000,000)	-	-
Dividends paid to minority interest	(10,750,000)	(500,000)	-
Net cash provided by financing activities	3,195,347,781	84,465,515	3,465,174,664
NET INCREASE IN CASH AND CASH EQUIVALENTS	1,406,552,638	134,145,496	174,097,638
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	308,243,134	174,097,638	-
CASH AND CASH EQUIVALENTS AT END OF PERIOD	P1,714,795,772	P308,243,134	P174,097,638

* The Company was incorporated and started commercial operations on March 8, 1995.

See accompanying Notes to Consolidated Financial Statements.

DMCI HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Organization

The Company was incorporated and started commercial operations on March 8, 1995 primarily to engage in construction contracting, real estate development and infrastructure project development. The Company's construction contracting business is conducted through its wholly owned subsidiary, D.M. Consunji, Inc. (DMCI) and through Atlantic, Gulf and Pacific Company of Manila, Incorporated (AG&P); a 40% owned subsidiary which was acquired on October 10, 1996; whereas its real estate and infrastructure project development activities are conducted through DMCI Project Developers, Inc. (PDI), another wholly owned subsidiary. PDI was incorporated on April 27, 1995 and commenced commercial operations in July 1995.

Merger of PDI with its Subsidiaries

On June 17, 1997, the Securities and Exchange Commission (SEC) approved the merger among PDI and its eight (8) wholly owned subsidiaries in accordance with the terms and conditions of the Plan of Merger executed by the parties. The Plan of Merger provided for, among others the merger among Bahag-Hari Land Developers, Inc., Bambang Development Corporation, Ususan Development Corporation, Tagig Land Development Corporation, Hagonoy Development Corporation, Matina Realty and Development Corporation, Marimar Land Developers, Inc., Kamagong Realty and Land Development Corporation and PDI. In 1996, these companies were included as consolidated subsidiaries of PDI.

Semirara Coal Corporation (Semirara)

On March 6, 1997, Voest-Alpine Machinery, Construction & Engineering GmbH (VA M.C.E.) and the Company entered into a Second Sale and Purchase Agreement, superseding an earlier agreement on January 17, 1997. Under the terms stipulated in the revised agreement, as further amended on March 24, 1997, VA M.C.E. agreed to sell and the Company agreed to purchase the following for a total consideration of ₱940 million:

- (a) The 50,324,378,294 common shares of Semirara held by VA M.C.E. representing approximately 40% of Semirara's outstanding common stock;
- (b) Semirara's outstanding restructured loan payable to VA M.C.E. totalling ₱2,464,615,842 consisting of (1) "Fixed Loan" liability of ₱977,985,553 or AS368,800,646 (approved on December 12, 1995 by Semirara's stockholders for conversion to common stock; actually converted to 97,798,555,306 common shares at ₱0.01 par value per share as approved by the SEC on April 11, 1997) and (2) the ₱1,486,630,289 or AS560,611,769 loan subject to yearly repayment of fifty percent (50%) of Semirara's yearly net cash inflow during the five (5) year period starting 1996 up to 2000 (of which ₱250,000,000 was also approved for conversion to common stock by Semirara's stockholders on December 12, 1995; actually converted to 25 billion common shares at ₱0.01 par value per share as approved by the SEC on April 11, 1997). The remaining balance of the ₱1,486,630,289 loan subject to yearly repayment; net of the ₱250 million loan that was converted to equity, amounting to ₱1,236,630,289 was reflected as long-term debt in Semirara's December 31, 1997 financial statements.

However,

in line with Semirara's quasi-reorganization as approved by Semirara's board of directors on September 10, 1997, ₱986,630,289 of the ₱1,236,630,289 loan balance will be contributed by the Company as Semirara's additional paid-in capital.

- (c) Semirara's outstanding liabilities to VA M.C.E. as of March 6, 1997 in the amount of AS48 million, representing the purchase price of spare parts and equipment components made available by VA M.C.E. to Semirara under an open account arrangement. As of December 31, 1997 the balance of Semirara's liabilities covered by this arrangement amounted to about AS22 million or about of ₱70 million.

The excess, in the amount of ₱420 million, of the Company's share in the net assets of Semirara that was acquired over the cost of its investment in Semirara was reflected as negative goodwill and included in the "Deferred Revenues and Credits" account in the liabilities section of the consolidated balance sheets.

2. Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements included the accounts of the Company and its wholly owned subsidiaries, DMCI, PDI; and Semirara, a 66.08% owned subsidiary which was acquired on April 17, 1997. The financial statements of DMCI included the accounts of its consolidated subsidiaries; namely, DMCI International, Inc. (DII, 100% owned), DMCI-Laing Construction, Inc. (DLCI, 60% owned which was incorporated on April 18, 1997), Obayashi Philippines Corporation (56% owned), Asia Industries Materials Handling Equipment Corporation (53% owned), Beta Electric Corporation (50.1% owned), and Acotec Panel Manufacturing, Inc. (50.1% owned which was incorporated on January 15, 1997). The financial statements of PDI included the accounts of its wholly owned subsidiary Pasong Tamo Properties, Inc. as of December 31, 1997 and 1996.

Inasmuch as the Company was incorporated only on March 8, 1995, DMCI became a wholly owned subsidiary only on June 20, 1995. Accordingly, the Company and its subsidiaries' consolidated net income for the year ended December 31, 1995 was reduced by DMCI's net income from January 1, 1995 to June 19, 1995 of ₱102,423,545, which was reflected in the consolidated statements of income as "Preacquisition Earnings."

All significant intercompany transactions and balances among the subsidiaries are eliminated in consolidation.

Revenue and Cost Recognition

Construction. Revenues from construction contracts are recognized on the percentage of completion method of accounting and are measured principally on the basis of the estimated completion of a physical proportion of the contract work. Contracts to manage, supervise, or coordinate the construction activity of others and those contracts wherein the materials and services are supplied by contract owners are recognized only to the extent of the contracted fee revenue.

Contract costs included all direct material and labor costs and those indirect costs related to contract performance. Expected losses on contracts are recognized immediately when it is probable that the total contract costs will exceed total contract revenues. The amount of such loss is determined irrespective of whether or not work has commenced on the contract; the stage of completion of contract activity; or the amount of profits expected to arise on other contracts which are not treated as a single construction contract. Changes in contract performance, contract conditions and estimated profitability, including those arising from contract penalty provisions, and final contract settlements which may result in revisions to estimated costs and gross margins are recognized in the year in which the changes are determined. Profit incentives are recognized as revenues when their realization is reasonably assured.

The asset, "Costs and estimated earnings in excess of billings on uncompleted contracts," represents total costs incurred and estimated earnings recognized in excess of amounts billed. The liability, "Billings in Excess of Costs and Estimated Earnings on Uncompleted Contracts," represents billings in excess of total contract costs incurred and estimated earnings recognized. Contract retentions are included in the contracts receivable account in the consolidated balance sheets.

Real Estate. Real estate sales, which consisted primarily of the sale of condominium units, where PDI has material obligations under the sales contracts to provide improvements after the property is sold are accounted for under the percentage-of-completion method. Under this method, the gain on sale is recognized as the related obligations are fulfilled. Revenues allocable to the unfulfilled obligations are deferred and presented as part of the "Deferred Revenues and Credits" account in the liabilities section of the consolidated balance sheets. If any of the criteria under the percentage-of-completion method is not met, the deposit method is applied until such criterion is met.

Under the deposit method, revenue recognition is deferred until the conditions for recording a sale are met. Pending recognition of sale, cash received from buyers are considered as "Customers' Deposits" and shown in the liabilities section of the consolidated balance sheets.

Real estate costs that relate to the acquisition, development, improvement and construction of the real estate projects are capitalized. Interest costs are capitalized while the development and construction of the real estate projects is in progress.

Cash Equivalents

All highly liquid instruments maturing within three (3) months or less from the date of acquisition are considered as cash equivalents.

Marketable Equity Securities

Investments in current marketable equity securities are carried at the lower of aggregate cost or market value determined at balance sheet date. The amount by which the aggregate cost of the marketable equity securities exceeds market value is accounted for as a valuation allowance. Changes in the valuation allowance to reduce the carrying amount of current marketable equity securities to market or to recognize any recoveries in market value are reflected in income for the period.

Inventories

Inventories are stated at the lower of cost or market. The cost of coal inventory is determined using the weighted average production cost method; construction materials, supplies, and spare parts held for sale by the first-in, first-out method; installation materials, supplies and parts by the moving average method; and equipment units held for sale by the specific identification method.

Real Estate Held for Sale and Development

Real estate held for sale and development is carried at the acquisition costs of the real estate properties plus the costs incurred for the development, improvement and construction of the real estate projects.

Investments

Investments in the shares of stock of the following investee companies that are at least 20% owned, are accounted for by the equity method:

<u>Investee Company</u>	<u>Percentage of Ownership</u>	
	<u>1997</u>	<u>1996</u>
Integrated Asia Corporation	50.10 *	50.10
Contech Products Corporation	50.00 **	—
Bachy Soletanche Philippines Corporation (Bachy)	49.00	49.00
Vulcan Materials Corporation	49.00	49.00
Atlantic, Gulf, & Pacific Company of Manila, Incorporated (AG&P - see Note 8)	40.00	40.00
Subic Water and Sewerage Company, Inc. (Subic Water)	40.00 **	—
Monarca Greenworld Corporation (Monarca)	35.00 **	—
Universal Rightfield Property Holdings, Inc. Inc. (URPHI - see Note 8)	34.93	34.93
Constress Philippines, Inc.	33.10	33.10
Freyssinet Philippines, Inc.	33.06	33.06
Freyssinet (Davao), Inc.	33.06	33.06
Freyssinet Glassfiber & Lightweight Concrete, Inc.	33.06	33.06
Freyssinet Manila, Inc.	33.06	33.06
Freyssinet Post Tensioning & Systems, Inc.	33.06	33.06
Freyland Properties, Inc.	26.10	26.10
Montecito Properties, Inc.	25.00	25.00
Metro Tagaytay Land Co., Inc. (Metro Tagaytay)	22.00	22.00

* Corporate life shortened to February 15, 1998; excluded from the consolidated financial statements as of and for the year ended December 31, 1997. (See Note 8)

** Newly organized subsidiaries in 1997

Under the equity method, investments in shares of stock are carried at cost adjusted principally for the Company's equity in the net earnings or losses of the investee companies from dates of acquisition. Equity in net earnings or losses is also adjusted for the straight-line amortization of the difference between the cost of the investments and the Company's equity in the underlying net assets of the investee companies at dates of acquisition. Any increase or decrease in the Company's ownership percentage and equity in the net assets of the subsidiaries or affiliated companies, resulting from issuances of shares of stocks by the subsidiaries or affiliated companies, are credited or charged to additional paid-in capital. Unrealized intercompany profits are eliminated to the extent of the Company's proportionate share thereof.

Other investments in shares of stock are carried at cost.

An allowance is set up for any substantial and presumably permanent decline in the carrying value of such investments.

Investments in real estate are carried at cost less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the properties.

Property, Plant and Equipment

Property, plant and equipment are carried at cost less accumulated depreciation, depletion and amortization. Substantially all of the property, plant and equipment of Semirara acquired up to April 30, 1997, except mining properties and mine exploration and development costs which are stated at cost, are stated at appraised values as determined by an independent firm of appraisers as of that date. Subsequent additions are stated at cost. Depreciation and amortization of property, plant and equipment, except for continuous mining equipment, and mining properties are computed on the straight-line method over the estimated useful lives of the properties (or the life of the mine, whichever is shorter). Depreciation of continuous mining equipment and depletion of mining properties are calculated on the unit of production method.

Minor repairs and maintenance costs are charged to income as incurred; significant renewals and improvements are capitalized. When assets are retired or otherwise disposed of, the cost, revaluation increment and the related accumulated depreciation and amortization on cost and on the revaluation increment are removed from the accounts and any resulting gain or loss is reflected in income for the period.

Deferred Mine Exploration and Development Costs

Expenditures for mine exploration and development activities on mining properties are deferred as incurred. These deferred costs are charged to expense when the results of the exploration activities are determined to be negative or not commercially viable. When exploration results are positive or commercially viable, the exploration expenses and subsequent development expenses are capitalized and carried under the "Deferred Mine Exploration and Development Costs" account until the start of commercial production. Such costs are accordingly transferred to the "Property, Plant and Equipment" account and amortized using the straight-line method over the lives of the respective mine's estimated recoverable reserves.

Stripping Costs

Stripping costs are capitalized and amortized based on the difference between the actual stripping ratio (ratio of waste moved to coal mined) and the standard stripping ratio established in accordance with the survey conducted on the mine.

Excess of Net Assets Acquired Over Costs

The excess of net assets acquired over the costs of investment in shares of stock is amortized on a straight-line basis over five (5) years.

Income Taxes

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial reporting bases of assets and liabilities and their related tax bases. Deferred tax assets and liabilities are measured using the tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on the deferred tax assets and liabilities arising from any change in the applicable income tax rates is included in the provision for deferred income tax for the period.

An allowance is provided for deferred tax assets which are not reasonably expected to be realized in the future. Any change in the valuation allowance on deferred tax assets is included in the computation of the provision for deferred income tax for the period.

Construction contracts existing as of December 31, 1997 are reported for income tax purposes using the completed contract method. However, as provided for under Republic Act No. 8424, effective January 1, 1998, construction contracts will be reported for income tax purposes under the percentage of completion method (see Note 16).

Foreign Currency Transactions

Exchange gains or losses arising from foreign currency transactions are credited or charged to operations.

Retirement Costs

Retirement costs are determined using the projected unit credit method for DMCI and attained age cost method for Semirara. Effective January 1, 1997, in compliance with ASC Statement No. 24, "Retirement Benefits Costs," past service costs are amortized over the expected working lives of employees. In previous years, past service costs were amortized over ten (10) years.

Pre-operating Costs and Expenses

Expenses incurred prior to the start of the Company and PDI's commercial operations are capitalized and amortized over five (5) years.

Costs and expenses incurred by Semirara prior to the start of its commercial operations, net of incidental revenues earned, are capitalized and allocated between the Unong and Panian Mines in relation to these mines' respective estimated reserves. The allocated preoperating costs and expenses are separately amortized upon the start of commercial production of the mine, using the straight-line method over the lives of the respective mine's estimated recoverable reserves.

Earnings Per Common Share

Earnings per common share is computed by dividing net income after deducting the preferred dividend requirements, by the weighted average number of common shares and common stock equivalents outstanding during the period adjusted to give retroactive effect to any stock dividends declared during the period. Common stock equivalents consist of shares potentially issuable upon conversion of the convertible preferred shares. Fully diluted earnings per share assumed the conversion of the outstanding convertible preferred shares.

3. Marketable Equity Securities

Marketable equity securities are presented net of allowance for decline in value of ₱39,107,824 as of December 31, 1997 and ₱19,806,462 as of December 31, 1996. The market value of the marketable equity securities as of December 31, 1997 and 1996 amounted to ₱31,131,229 and ₱50,432,591, respectively, and ₱28,018,106 as of April 23, 1998.

4. Receivables

Receivables consisted of:

	1997	1996
Contracts:		
Construction contracts (including retention receivable on uncompleted contracts of ₱947,026,726 in 1997 and ₱650,634,622 in 1996)	₱2,597,477,310	₱1,988,571,773
Real estate contracts	97,387,486	262,222,149
Trade	184,599,592	122,180,890
Subcontractors and suppliers	1,070,849,715	533,667,046
Installment receivables	400,000,000	353,333,998
Related parties: (see Note 8)		
Notes receivable from AG&P (see Note 8)	782,360,673	-
Other affiliated companies	131,337,620	125,741,643
Others	477,695,077	219,005,663
	5,741,707,473	3,604,723,162
Less allowance for doubtful accounts	360,373,347	138,843,230
	₱5,381,334,126	₱3,465,879,932

The balance of "Real estate contracts receivable" as of December 31, 1997 and 1996 included the uncollected balance amounting to about ₱50 million and ₱262 million, respectively, of the sales proceeds in 1996 amounting to ₱418 million of PDI's allocated units in a real estate project. As of April 23, 1998, the outstanding real estate contracts receivable as of December 31, 1997 was fully collected. In 1997, PDI also executed a Memorandum of Agreement with two (2) third parties whereby PDI assigned to said third parties for a consideration of about ₱194.7 million its rights

and interest in a real estate project. As of December 31, 1997, the unpaid balance of the consideration amounted to about ₱34.1 million.

In 1996, DMCI sold certain property which are no longer used in its operations for a total consideration of about ₱675 million and realized a gain of about ₱645 million. On February 28, 1998, DMCI entered into a Memorandum of Agreement (MOA) with the buyer of the said real estate property for the settlement of the unpaid balance of the selling price amounting to about ₱355 million as of that date. The MOA stipulated that the unpaid balance of ₱355 million and the agreed amount of interest accruing on such obligation of about ₱45 million or an aggregate amount of ₱400 million (presented as "Installment receivables" included in the "Receivables – net" account in the assets section of the consolidated balance sheets) shall be settled through installment payments totalling ₱175 million up to 1998. The remaining balance of the installment receivables of about ₱225 million will be credited as equity contribution by DMCI to a joint venture corporation that the parties have agreed to establish for the development of the subject real estate property. As of April 23, 1998, DMCI has already collected ₱49.5 million of the installment receivable.

The notes receivable from AG&P of about ₱782.4 million bear interest at 15% per annum and an additional 12% per annum on such overdue amount computed from maturity date to the date that the overdue amount is paid in full. As of December 31, 1997, the maturity dates of the foregoing promissory notes ranged from April 13, 1997 to February 5, 1998. The loans are collateralized by a participation on the mortgage trust indenture covering substantially all of AG&P's existing property, plant and equipment. As of December 31, 1997, about ₱779.4 million of the outstanding notes receivable had already matured and was due for payment. On January 21, 1998, the Company agreed to align the interest rate of 15% per annum to the interest rate charged by AG&P's creditor banks and waived the 12% penalty which was supposed to be charged on the unpaid loans beyond the 90-day term as provided for in the promissory notes.

5. Costs, Estimated Earnings, and Billings on Uncompleted Contracts

The details of the costs, estimated earnings, and billings on uncompleted contracts are as follows:

	1997	1996
Total costs incurred	₱9,593,461,965	₱6,495,085,324
Add estimated earnings (net of estimated contract losses of ₱27,633,609 in 1996)	2,337,490,563	1,455,846,558
	11,930,952,528	7,950,931,882
Less total billings (including unliquidated advances from contract owners of ₱2,359,140,008 in 1997 and ₱1,596,627,519 in 1996)	14,134,636,660	9,383,582,061
	(₱2,203,684,132)	(₱1,432,650,179)

The foregoing balances are reflected in the accompanying consolidated balance sheets under the following accounts:

	1997	1996
Costs and estimated earnings in excess of billings on uncompleted contracts	₱38,182,542	₱52,270,172
Billings in excess of costs and estimated earnings on uncompleted contracts	(2,241,866,674)	(1,484,920,351)
	(₱2,203,684,132)	(₱1,432,650,179)

6. Inventories

The details of inventories are as follows:

	1997	1996
Construction and installation materials, parts and supplies	₱271,184,164	₱131,722,144
Coal inventory	29,647,675	-
Equipment units and spare parts held for sale	20,649,865	104,824,785
	321,481,704	236,546,929
Less allowance for inventory obsolescence	59,090,844	9,289,386
	262,390,860	227,257,543
Equipment units, materials and spare parts in transit	132,322,655	5,539,500
	₱394,713,515	₱232,797,043

7. Real Estate Held for Sale and Development

Real estate held for sale and development consisted of the following:

	1997	1996
Real estate under development	₱452,489,354	₱52,689,437
Land held for future development (see Note 12)	1,703,028,349	1,020,432,200
	₱2,155,517,703	₱1,073,121,637

PDI has a Memorandum of Agreement with URPHI starting February 15, 1996 for the development of a real estate project. The agreement stipulated that PDI contributed certain parcels of land at an agreed valuation of about ₱60 million which URPHI shall develop into high-rise, mixed used condominiums. The total committed contribution by PDI under this agreement amounted to about ₱1 billion. As of December 31, 1997, the total cost incurred by PDI on the said real estate project amounted to about ₱288 million which amount was included as part of the "Real estate under development" account.

As of December 31, 1997 and 1996, the estimated cost to complete PDI's real estate projects amounted to about ₱750 million and ₱95 million, respectively.

8. Investments

The details of this account are as follows:

	1997	1996
Shares of Stock:		
At equity:		
Acquisition cost:		
Balance at beginning of year	₱1,453,049,900	₱270,573,119
Additions during the year (subscriptions payable of which amounted to ₱182,529,100 in 1997 and ₱270,000,000 in 1996)	62,737,480	1,182,476,781
Disposals during the year	(27,462,350)	-
Balance at end of year	1,488,325,030	1,453,049,900
Accumulated equity in net earnings:		
Balance at beginning of year	100,502,554	28,041,259
Equity in net earnings	64,631,318	72,461,295
Balance at end of year	165,133,872	100,502,554
	1,653,458,902	1,553,552,454
At cost (subscriptions payable of which Amounted to ₱99,999,750 in 1997)	206,512,804	61,858,803
	1,859,971,706	1,615,411,257
Deposits on Future Subscriptions	300,000,000	325,373,200
Investments in and Advances to Real Estate Joint Ventures (see Note 17)	391,514,780	440,836,455
Real Estate Properties:		
Land (see Note 12)	257,653,491	255,591,013
Condominium units- net of accumulated depreciation of ₱3,264,585 in 1997 and ₱3,332,384 in 1996	22,131,903	36,545,393
	279,785,394	292,136,406
	₱2,831,271,880	₱2,673,757,318

The Company's share in the undistributed earnings of its subsidiaries and affiliated companies included in retained earnings amounting to about ₱674 million as of December 31, 1997 is not currently available for dividend declaration by the Company until actually distributed by such subsidiaries and affiliated companies.

AG&P

On October 10, 1996, the Company, together with Buenaventura Filamor Echaz Financial Services (BFE), entered into a Memorandum of Agreement (amended on October 29, 1996) with AGP Industrial Corporation (AGPI) and Marubeni Corporation (Marubeni), AG&P's major existing shareholders as of such date, wherein which, the Company and BFE will invest ₱400 million into AG&P in exchange for 51% of its outstanding capital stock. The Company and BFE had fully paid the ₱400 million investment on January 7, 1997, and on February 26, 1997, were issued 1,144,877 Class A shares and 555,123 Class B shares by AG&P, both at a par value of ₱100 per share or an aggregate par value of ₱170 million as partial consideration for the investment.

The Agreement also provided that the Company and BFE, subject to their business judgment, shall extend such advances, credit facilities or other funds to AG&P totalling ₱800,000,000, to be secured by AG&P's real estate properties, to enable AG&P to pay its trade creditors, or otherwise service its debt obligations. As of December 31, 1997, the Company's advances to AG&P which were included in the "Notes receivable from AG&P" account in the consolidated balance sheets amounted to about ₱782 million excluding accrued interest thereon (see Note 4) amounting to about ₱23 million. For the year ended December 31, 1997, total interest income accrued on the notes receivable from AG&P amounted to about ₱96 million.

Also, on October 29, 1996, AG&P, AGPI and Marubeni (collectively referred to hereafter as "existing shareholders") together with the Company and BFE (collectively referred to hereafter as "investors") executed a Shareholders' Agreement whereby the parties have agreed, among others, on the following: (a) any of the investors or the existing shareholders of AG&P who may wish to transfer, sell or assign or otherwise dispose of all or any part of its shares to a bona fide third party shall first offer such shares to each of the other shareholders of AG&P by written notice except for the type of transfers specifically allowed under the Shareholders' Agreement; (b) restriction on the declaration of dividends until AG&P has fully paid the advances made by any shareholder to AG&P, and (c) vote in favor of and cause their respective nominee directors to vote in favor of a merger between AG&P and AGPI on an audited book-value for book-value basis without any premium added to the value of either corporation.

In furtherance of and to fully implement Section 6 of the Memorandum of Agreement dated October 10, 1996 relating to the merger between AG&P and AGPI, the contracting parties and Trans-Philippines Investment Corporation (TPIC), the majority shareholder of AGPI, also executed an Agreement to Approve Merger. The Agreement to Approve Merger provided that the Company and BFE recognize the debt to equity conversion of TPIC's advances to AGPI into AGPI's shares that will take place prior to the merger. As contained in the Agreement to Approve Merger, AGPI shall be the surviving corporation after the merger; with 51% of its outstanding capital stock owned effectively by both the Company and BFE, 9.8% of its shares owned by Marubeni Corporation and 38.4% owned by the shareholders of AGPI before the merger. AGPI's corporate name will subsequently be changed to "Atlantic, Gulf & Pacific Company of Manila, Incorporated."

On April 25, 1997, a Supplementary Agreement to the Agreement to Approve Merger dated October 10, 1996 was executed by representatives of AGPI, Marubeni, TPIC, BFE, and the Company which provided that the Company and BFE shall cause the settlement of AGPI's payables to TPIC amounting to about ₱176 million as of February 28, 1997 plus any accrued interest thereon, in the following manner: (a) the Company and BFE shall identify a third party who shall effect payment to TPIC of the total amount of ₱110,356,428 of TPIC's receivables from AGPI. The third party purchaser shall be willing to convert the purchased receivables into 2,829,652 shares of AGPI at ₱39 per share; prior to the merger of AG&P and AGPI, with all the transaction costs to be borne by the third party; (b) AG&P shall lend ₱30.1 million to AGPI which amount shall be used by AGPI to pay a portion of the balance of its liabilities to TPIC; and (c) the remaining balance of AGPI's payables to TPIC amounting to about ₱36 million as of February 28, 1997 plus interest and any other payable of AGPI to TPIC after said date shall be converted by TPIC into shares of stock of AGPI at ₱39 per share prior to the merger.

On September 29, 1997, TPIC, the majority shareholder of AGPI, rescinded the October 10, 1996 Agreement to Approve Merger and the related April 25, 1997 Supplementary Agreement to the Agreement to Approve Merger after the Company claimed through its July 23, 1997 letter to AGPI, TPIC and Marubeni that the signatory to the Supplementary Agreement to Agreement to Approve Merger dated April 25, 1997 who represented the Company in this transaction was not authorized by the Company. The rescission was accepted by the Company on October 15, 1997 and by BFE on October 28, 1997. However, in spite of TPIC's rescission of the foregoing merger agreements, AGPI in its March 23, 1998 letter to the Company and BFE called for the following within seven (7) days from receipt of letter: (a) fulfillment by the Company and BFE of their obligations under the foregoing agreements particularly, the settlement of AGPI's obligations to TPIC, and (b) execution of the required statutory and contractual actions/formalities in order to realize the contemplated merger of AGPI and AG&P.

On March 31, 1998, the Company sent a reply to AGPI and stated its position on the foregoing matters as follows: (a) that both the Supplementary Agreement to the Agreement to Approve Merger and the Agreement to Approve Merger were rescinded by AGPI through TPIC in the letters dated September 16 and 29, 1997; (b) that the Company recognized the rescission of both Agreements in separate letters addressed to AGPI and TPIC dated October 15 and 28, 1997; and (c) that the Company recognized such rescission even as it reiterated that the Company is not a party to the Supplementary Agreement to the Agreement to Approve Merger, inasmuch as the signatory to such agreement, as mentioned in the preceding paragraph, was not authorized by the Company to represent it in the transaction. As of April 23, 1998, there were no additional documents executed with respect to the foregoing matters.

On March 17, 1997, the SEC approved the increase in AG&P's authorized capital stock from ₱315 million Class A shares (divided into 3,150,000 shares at ₱100 par value per share) and ₱135 million Class B shares (divided into 1,350,000 shares at ₱100 par value per share) to ₱450 million Class A shares (divided into 4,500,000 shares at ₱100 par value per share) and ₱150 million Class B shares (divided into 1,500,000 shares at ₱100 par value per share). On the basis of such increase in authorized capital stock additional 1,065,955 Class A shares and 55,301 Class B shares; both at ₱100 par value per share or an aggregate value of ₱112,125,600 were issued to the Company, BFE and other shareholders in full consideration of their ₱400 million investment in AG&P as mentioned in the foregoing paragraphs.

URPHI

On May 3, 1996, the SEC approved the merger of Universal Petroleum Equity and Property Ventures, Inc. (Universal Property), Rightfield and URPHI as provided for in the Plan of Merger executed by the parties. The Plan of Merger provided for, among others, the: (a) merger of Universal Property and Rightfield into URPHI, with URPHI as the surviving corporation; (b) cessation of the corporate existence of Universal Property and Rightfield upon approval by the SEC of the merger, and thereupon, all rights, privileges, powers, franchises, properties and all liabilities of Universal Property and Rightfield as of May 3, 1996 shall be vested in URPHI. The Plan of Merger further stipulated that subject to the surrender by the registered owners of Rightfield of their corresponding certificates of stock to URPHI, the outstanding shares of

Rightfield, except those owned by Universal Property, and Universal Property shall be exchanged with shares of stock of URPHI at the ratio of three (3) shares of URPHI for every one (1) share of Universal Property and Rightfield, as determined on the basis of the amount of the net assets as of November 30, 1995 of Rightfield and Universal Property to be absorbed by URPHI.

As a result of the merger, PDI's equity amounting to ₱568,423,087, in the resulting net assets of URPHI as of May 3, 1996 (inclusive of subscriptions receivable amounting to ₱393,743,750), net of goodwill recognized by URPHI of ₱463,224,010 as a result of the merger transaction, exceeded by ₱269,990,985 the carrying value of PDI's investment of ₱298,432,102. The excess of the PDI's equity in the net assets of URPHI over the carrying value of its investment of ₱269,990,985 was recognized and included in the "Additional paid-in capital" account in the stockholders' equity section of the consolidated balance sheets.

Subic Water

On January 22, 1997, PDI subscribed to 3,262,300 shares at a par value of ₱10 per share or an aggregate value of ₱32,623,200 in Subic Water, a joint venture company with Subic Bay Metropolitan Authority, a government corporation, Olongapo City Water District, and Biwater International Limited, a company organized under the laws of England. Subic Water was organized primarily to engage in the provision, establishment, operation and maintenance of water and sewerage facilities and systems in the Subic Special Economic and Free Port Zone. The agreement provided that the total initial authorized capital stock of Subic Water shall be ₱250,000,000 consisting of 25,000,000 shares with a par value of ₱10.00 per share, of which, the total initial subscribed and paid-up capital within three (3) years from the effective date of the agreement (as defined in the Joint Venture Agreement executed by the parties on November 24, 1996 to be the date on which certain conditions stipulated in the agreement shall have been complied with) shall be ₱187,200,000. The Joint Venture Agreement stipulated that the Company shall have an equity participation equivalent to 40% in Subic Water amounting to ₱74,880,000 based on the foregoing initial subscribed and paid up capital. The balance of the Company's committed subscription to Subic Water of ₱42,256,800 is expected to be paid on or before the second anniversary of the said effective date.

Metro Tagaytay

In accordance with the subscription agreement dated November 15, 1996 executed between PDI and Metro Tagaytay with the consent of Landco Asset Management, Inc. and Metro Pacific Corporation, PDI subscribed to 785,714 shares out of the unissued capital stock of Metro Tagaytay for a total subscription price of ₱330 million. As of December 31, 1997, PDI had already paid ₱150 million of the subscription price with the remaining balance of ₱180 million to be paid in two (2) equal annual installments of ₱90 million each up to 1999.

North Luzon Railways Corporation (Northrail)

On June 10, 1995, the Bases Conversion Development Authority (BCDA), a government corporation, Philippine National Railways (PNR), and a consortium comprised of foreign investors and local partners (Consortium) entered into a Joint Venture Agreement to undertake the construction of a double-track railway system from Metro Manila to Clark (as Phase I) with an extension to Subic Bay Freeport Zone (as Phase II), and a possible extension to San Fernando, La Union (as Phase III), and finally to Laoag, Ilocos Norte and to San Jose City (as Phase IV), and hereinafter referred to as the "Project." The said Joint Venture Agreement also provided for the incorporation of Northrail, initially as a wholly owned corporation of BCDA, the primary purpose

of which, among others, is to construct, operate and manage a railroad system to serve Northern and Central Luzon; and to develop, construct, manage, own, lease, sublease and operate establishments and facilities of all kinds related to the railroad system. On February 6, 1996, pursuant to an amendment to the Joint Venture Agreement, as discussed above, DMCI/PDI was included as a strategic partner to the project on the basis of its qualifications for the implementation of the Project. Consequently, on February 8, 1996, the partners in the Joint Venture Agreement, including DMCI/PDI, entered into a Memorandum of Agreement to set up the mechanics for raising the seed capitalization needed by Northrail to accelerate the implementation of the Project. The amounts contributed by the joint venture partners are committed to be converted into equity when Northrail is privatized. As of December 31, 1997 and 1996, DMCI/PDI has already contributed ₱300 million to Northrail. Such contribution is presented under "Deposits on Future Subscriptions" in the "Investments" account in the consolidated balance sheets.

Asian Hospital, Inc. (AHI)

On December 9, 1997 the Company subscribed to 133,333,000 shares of the capital stock of AHI at a subscription price of ₱1 per share or a total subscription price of ₱133,333,000, representing 11.11% of the total outstanding capital stock of AHI. As of December 31, 1997, the Company has already paid ₱33,333,250 out of the total amount subscribed. The payment of the remaining unpaid subscription of ₱99,999,750 is subject to certain conditions provided for by the subscription agreement which have to be complied with by AHI.

Integrated Asia Corporation (Integrated Asia)

On February 10, 1998, the stockholders of Integrated Asia ratified the shortening of the corporate life of Integrated Asia to February 15, 1998, the immediate cessation of its operations, separation of employees and pursuance of legal action to enforce claims against third parties. Furthermore, the stockholders of Integrated Asia also ratified the creation of a Board of Liquidators for the purpose of prosecuting and defending suits by and against Integrated Asia; to enable it to settle and close its affairs; and to dispose of and convey its property for the purpose of paying its debts. For the year ended December 31, 1997, DMCI recognized losses of about ₱105 million, net of amounts which can be recovered from the assets of Integrated Asia (included in the "Provisions for probable losses on assets and other charges" account in the consolidated statements of income), arising from claims against Integrated Asia which were guaranteed and subsequently paid by DMCI.

Freyssinet Group of Companies

On March 6, 1998, the stockholders and the board of directors of Freyssinet Philippines, Inc. (FPI), Freyssinet Post Tensioning & Systems, Inc., Freyssinet Manila, Inc., Freyssinet Glassfiber & Lightweight Concrete, Inc., Freyland Properties, Inc. and Pacopandana Construction & Development Corporation (hereinafter collectively referred to as the Freysinnet Group of Companies) approved the merger of the Freyssinet Group of Companies with FPI as the surviving corporation. As of April 23, 1998, the merger of the Freyssinet Group of Companies is still subject to the approval of the SEC.

9. Property, Plant and Equipment

Property, plant and equipment consisted of:

	1997		1996
	At Appraised Values (Cost Plus Appraisal Increase)	Appraisal Increase	At Cost
Land and improvements	₱579,970,677	₱-	₱321,952,182
Buildings and building improvements	465,830,189	115,153,527	41,779,814
Construction equipment and tools	2,613,605,474	-	1,849,730,366
Transportation equipment	125,938,519	-	107,736,918
Machinery and other equipment	6,404,702	-	12,472,063
Office furniture, fixtures and equipment	146,164,970	-	99,831,373
Mining fixed assets of Semirara:			
Continuous mining and other equipment	3,134,223,637	879,072,830	-
Power plants	679,662,585	376,789,456	-
Roads and bridges	266,532,545	166,247,770	-
Mining properties	68,548,387	-	-
Mining exploration and development costs	97,983,793	-	-
Leasehold and other improvements	64,036,549	-	11,283,008
	8,248,902,027	1,537,263,583	2,444,785,724
Less accumulated depreciation, depletion and amortization	3,729,867,499	348,516,355	719,523,222
	4,519,034,528	1,188,747,228	1,725,262,502
Construction in progress	12,589,621	-	-
Equipment in transit	5,722,988	-	57,612,506
	₱4,537,347,137	₱1,188,747,228	₱1,782,875,008

Under the terms of the agreements covering DMCI's liabilities under trust receipts amounting to ₱34,187,953 as of December 31, 1997, certain equipment have been released to DMCI in trust for a local bank. DMCI is accountable to the bank for the trusted equipment.

Depreciation, depletion and amortization charged to operations (including depreciation on appraisal increase of about ₱107 million in 1997), aggregated to about ₱773 million in 1997, ₱284 million in 1996 and ₱112 million in 1995.

10. Deferred Charges and Other Assets

The details of deferred charges and other assets are as follows:

	1997	1996
Deferred Charges:		
Preoperating expenses	₱773,562,526	₱7,724,247
Mining rights – Panian Mine	181,451,613	–
Stripping costs	175,860,926	–
Mine exploration and development costs	52,191,605	–
Others	15,617,146	38,208,810
	1,198,683,816³	45,933,057
Less allowance for losses on preoperating expenses, stripping and deferred exploration and development costs and amortization of preoperating expenses	946,445,904	–
	252,237,912	45,933,057
Assets not used in operations – net of accumulated depreciation of ₱148,480,028	454,183	–
Funds held by custodian bank	13,174,805	323,790
Deposits and others	24,398,829	31,541,059
	₱290,265,729	₱77,797,906

The Company has a Custodianship Agreement with a local bank wherein which the Company maintains a Sinking Fund Account comprised of cash or money market instruments gradually set aside in order to cover the future redemption of the 2,400,000 redeemable, convertible, preferred shares by April 7, 2000 (Final Redemption Date) (see Note 19). The annual deposits to the Sinking Fund is in accordance with an approved schedule of payments. As of December 31, 1997, the balance of the Sinking Fund Account amounted to about ₱13.2 million.

11. Notes Payable

Notes payable consisted of the following:

	1997	1996
Bank loans:		
DMCI and subsidiaries	₱166,781,744	₱128,365,515
Semirara	95,010,061	–
Notes payable of Semirara to a supplier	17,183,191	–
Current maturities of long-term notes payable (see Note 15)	13,161,558	–
	₱292,136,554	₱128,365,515

As of December 31, 1997 and 1996, the bank loans of DMCI and subsidiaries are unsecured and bear interest at prevailing market rates. As of December 31, 1996, a portion of the bank loans totalling to about ₱91 million was secured by joint suretyship agreements by certain stockholders and other affiliated companies and was subsequently paid in March 1998. The remaining balance of the December 31, 1996 bank loans of about ₱37 million was fully paid in 1997. The Semirara bank loans of ₱95,010,061 represent the unpaid balance of the ₱330 million bridge financing loan facility obtained from a local bank. Such loans bear interest at prevailing market rates and are secured by a chattel mortgage on certain machinery and equipment of Semirara and a deed of suretyship by DMCI.

The notes payable of ₱17,183,191 represent short-term obligations to a supplier arising from acquisition of certain mining equipment and equipment parts and supplies. These obligations, which bear interest at prevailing market rates are secured by the related equipment acquired.

Total interest paid by the Company and its subsidiaries for all their obligations for the years ended December 31, 1997 and 1996, and the ten months ended December 31, 1995 amounted to ₱57,811,268, ₱18,344,763 and ₱28,469,253, respectively, including capitalized interest of ₱19,244,590 in 1995.

12. Loans Payable

Loans payable as of December 31, 1997 and 1996 of ₱416.8 million and ₱344.6 million, respectively, represent the balance of the obligations of PDI to various real estate property sellers for the acquisitions of certain parcels of land (reflected in consolidated balance sheets as "Real Estate Held for Sale and Development" [see Note 7] and "Investments" [see Note 8]). The terms of the deeds of absolute sale covering these acquisitions provided that these obligations are payable only after certain conditions have been complied with; among others, (a) presentation by the property sellers of the original Transfer Certificates of Title covering the purchased parcels of land; (b) submission of a Certificate of Non-Delinquency of real estate taxes; and, (c) physical turnover of the acquired parcels of land to PDI. As of April 23, 1998, about ₱17 million of the loans payable balance was already paid.

Also, included in this account is a loan payable of PDI amounting to ₱29,578,668, which, as stipulated in the terms of the deed of absolute sale between PDI and the seller, shall be paid in proportion to the area of the acquired property that has been cleared by the property owner of all squatters and illegal structures.

13. Accounts Payable and Accrued Expenses

The details of the accounts payable and accrued expenses account are as follows:

	1997	1996
Payable to VA M.C.E. (Note 1)	₱790,000,000	₱-
Subcontractors	745,973,116	336,252,263
Suppliers	690,703,632	497,630,289
Payable to the Department of Energy (DOE) and local government units	52,944,512	-
Accrued expenses and other payables	1,043,307,783	390,929,147
	₱3,322,929,043	₱1,224,811,699

Semirara has an existing Coal Operating Contract with the DOE (formerly Ministry of Energy) dated July 11, 1977, as amended on January 16, 1981, for the exploration, development, mining and utilization of coal over Semirara Island, Antique, under the terms and conditions provided therein and pursuant to the provisions of Presidential Decree No. 972, otherwise known as the Coal Development Act of 1976. The contract is for a maximum period of 35 years (inclusive of the developmental stage and renewals) up to July 2012. The contract also provided for the manner and basis of sharing the gross proceeds from coal production between the Company and the DOE. The liabilities to the DOE under this contract and to the different local government units in the province of Antique, under the provisions of the Local Government Code of 1991, amounted to about ₱53 million as of December 31, 1997.

14. Deferred Revenues and Credits

The details of this account are as follows:

	1997	1996
Excess of net assets acquired over cost of investment in Semirara – net of Amortization (see Note 1)	₱335,720,958	₱-
Deferred revenues	199,068,391	211,089,427
	₱534,789,349	₱211,089,427

As of December 31, 1997, Semirara's deferred revenues of ₱155,533,968 represent the balance of NPC's payments for the unlifted coal totalling to 150,000 MT Selectively Mined Coal (Select) priced at ₱178,615,000 and 31,034 MT Run-of-Mine (ROM) priced at ₱27,951,825 that formed part of the minimum contracted quantity which NPC agreed to purchase for the years 1990 and 1991, respectively, under the Coal Supply Agreement between Semirara and NPC effective during those years. On September 28, 1990, Semirara entered into a Memorandum of Agreement (MOA) with NPC relative to the 150,000 MT Select coal, whereby Semirara agreed to provide NPC 150,000 MT Select coal or its ROM coal equivalent, free of cost to NPC, over a period of seven (7) consecutive years in equal tonnage beginning 1993 or when Calaca II power plant starts operations, whichever is earlier. As of December 31, 1997, total coal lifted under the said MOA totalled 42,856 MT Select coal equivalent or its peso equivalent of ₱51,031,496. On December 20, 1991, Semirara also entered into a Memorandum of Agreement with NPC relative to the 31,034 MT of ROM coal as earlier mentioned wherein which Semirara agreed not to exercise its

right of forfeiture over the said coal tonnage and instead, upon 30 days of NPC's written notice, make available for NPC's lifting 31,034 MT of ROM coal on an FOB Semirara basis. The lifting for the said coal tonnage which was previously scheduled on September 27, 1997 based on NPC's written notice dated June 10, 1997, was rescheduled to the first quarter of 1998 as advised by NPC on September 26, 1997.

15. Non-Current Liabilities

Non-current liabilities as of December 31, 1997 consisted of the following:

Accounts payable – foreign suppliers	₱229,249,214
Notes payable	31,587,739
	260,836,953
Less current maturities	72,539,360
	₱188,297,593

The non-current accounts payable of Semirara represents foreign currency denominated obligations to certain foreign suppliers related to the importations of various mining equipment, spare parts and accessories. These obligations which are payable in various installments up to 2001, bear interest based on LIBOR plus a certain spread and are covered by usance letters of credit issued by local banks.

The notes payable of ₱31,587,739 represent U.S. dollar-denominated long-term obligations of Semirara to a foreign supplier arising from acquisitions of certain mining equipment, parts and supplies. These notes payable bear interest at prevailing market rates; are collateralized by the mining equipment acquired and are payable in twelve (12) equal quarterly installments up to September 2000.

16. Income Taxes

The significant components of the Company and its subsidiaries' deferred income tax assets and liabilities are as follows:

	1997	1996
Deferred tax asset on:		
Allowance for losses on preoperating expenses, stripping and deferred exploration and development costs	₱304,274,757	₱-
Unrealized foreign exchange loss- net	196,531,090	109,104
Allowance for doubtful accounts	84,995,943	48,595,131
Allowance for inventory obsolescence	51,567,259	3,251,285
Accrued expenses and others	41,844,278	6,932,262
Excess of tax over book real estate revenues	5,929,075	29,594,399
Unamortized past service cost contribution	5,418,318	955,345
Total deferred tax assets	₱90,560,720	89,437,526
Less valuation allowance	(572,044,734)	-
Net deferred tax assets	118,515,986	89,437,526
Deferred tax liability on:		
Excess of book over tax income pertaining to uncompleted construction contracts	(710,219,414)	(480,867,554)
Others	(835,232)	(1,459,217)
Total deferred tax liabilities	(711,054,646)	(482,326,771)
	(₱592,538,660)	(₱392,889,245)

The reconciliation of the provision for income tax computed at the statutory income tax rate to the provision for income tax shown in the consolidated statements of income for the years ended December 31, 1997 and 1996 and the ten months ended December 31, 1995 follows:

	1997	1996	1995
Provision for income tax computed at the statutory income tax rate of 35%	₱341,321,943	₱530,271,596	₱265,798,726
Addition to (reduction in) income tax expense resulting from:			
Interest income subjected to final tax at a lower rate	(55,170,956)	(52,177,526)	(6,695,097)
Nontaxable equity in net earnings of unconsolidated affiliates	(22,620,961)	(25,593,154)	(7,971,015)
Net effect of the change in the statutory income tax rate from 35% in 1997 to 34% in 1998, 33% in 1999 and 32% in 2000 and thereafter	(6,109,155)	-	-
Others – net	(7,366,541)	(803,150)	3,409,861
Effect of tax loss position of a subsidiary	124,367,433	-	-
Provision for income tax	₱374,421,763	₱451,697,766	₱254,542,475

Income taxes paid by the Company and its subsidiaries for the years ended December 31, 1997 and 1996, and the ten months ended December 31, 1995 amounted to ₱200,869,805, ₱294,767,340 and ₱105,545,487, respectively.

On December 11, 1997, Republic Act No. 8424 entitled “An Act Amending the National Internal Revenue Code, As Amended, and For Other Purposes” (Act), was passed into law effective January 1, 1998. Among others, the Act included the following significant revisions to the current rules of taxation:

- (a) Change in the corporate income tax rate to 34% in 1998, 33% in 1999 and 32% in 2000 and onwards;
- (b) Mandatory use of the percentage of completion method in reporting income from long-term construction contracts whereas previously, the use of the completed contract method was allowed;
- (c) Imposition of minimum corporate income tax of 2% of gross income, as defined;
- (d) Imposition on the employer of a final tax on grossed up monetary value of fringe benefits granted to employees (except rank and file) at the following rates: 34% in 1998; 33% in 1999 and 32% in 2000 and onwards;
- (e) Reduction of the interest expense allowed as deductible expense by an amount equivalent to a certain percentage of the interest income subjected to final tax as follows: 41% starting January 1, 1998, 39% starting January 1, 1999, and 38% starting January 1, 2000 and onwards; and,
- (f) Introduction of a three-year net operating loss carryover.

17. Related Party Transactions

Starting January 1, 1996, the Company has management agreements with DMCI and PDI wherein which the Company renders general and special management services to DMCI and PDI for a fee. These agreements are effective for a period of five (5) years, renewable for another five (5) years upon mutual agreement of the contracting parties. The management fees received by the Company pursuant to the agreements were eliminated from the accounts in the process of consolidation.

The Company and its subsidiaries' transactions with affiliated companies consisted of interest-bearing notes receivable from AG&P (see Notes 4 and 8), coal sales, rentals of equipment and cash and operating advances.

The effects of the foregoing transactions are shown under appropriate accounts in the financial statements.

18. Retirement Plan

DMCI and Semirara have funded and formal noncontributory defined retirement plans covering their regular employees. Retirement benefits are computed principally based on member's latest monthly salary per year of service. Total retirement costs charged to operations amounted to about ₱24 million in 1997 and ₱763,000 in 1996.

As of January 1, 1997, the date of the most recent actuarial valuations, the actuarial accrued retirement benefits amounted to ₱188 million while the fair market value of the plan assets amounted to about ₱235 million. As of December 31, 1997, DMCI has no unfunded past service cost liability while Semirara has unrecognized retirement liability at the adoption of SFAS No. 24 amounting to about ₱39 million. The principal actuarial assumptions used to determine retirement benefits were an investment yield of 10% per year compounded annually and annual salary increases of also 10% and normal retirement age of 60 years or 30 years of service, whichever comes earlier. The actuarial valuations are made at least every two (2) or three (3) years. The subsidiaries' annual contributions to the retirement plan consisted of payments covering the normal service costs for the year and payment towards funding the unfunded actuarial liability for Semirara.

19. Capital Stock

The movement of the Company's capital stock and additional paid-in capital is accounted as follows:

	No. of Shares		Issued		Additional Paid-in Capital
	Authorized	Unissued	No. of Shares	Amount	
Cumulative, convertible preferred stock- ₱1 par value:					
Balance as of December 31, 1996	100,000,000	100,000,000	-	₱-	₱-
Issuance of shares	-	(2,400,000)	2,400,000	2,400,000	2,326,566,774
Balance as of December 31, 1997	100,000,000	97,600,000	2,400,000	₱2,400,000	₱2,326,566,744
Common stock- ₱1 par value:					
Balance as of December 31, 1996	1,650,000,000	522,253,000	1,127,747,000	₱1,127,747,000	₱2,373,452,402
Increase in authorized common stock	4,250,000,000	4,250,000,000	-	-	-
100% stock dividends	-	(1,127,747,000)	1,127,747,000	1,127,747,000	-
Balance as of December 31, 1997	5,900,000,000	*3,644,506,000	2,255,494,000	₱2,255,494,000	₱2,373,452,402
Excess of equity in net assets over carrying value of investment in URPHI (see Note 8)	-	-	-	₱-	₱269,990,985
	6,000,000,000		2,257,894,000	₱2,257,894,000	₱4,970,010,161

* As of December 31, 1997, 224,719,200 common stocks are potentially issuable upon the exercise of preferred shareholders of their rights to conversion.

Preferred Shares

On September 27, 1996, the SEC approved the conversion of 100,000,000 unissued common shares of the Company to 100,000,000 redeemable, convertible, non-voting, non-participating, and cumulative preferred shares, both at a par value of ₱1.00 each.

On January 31, 1997, the SEC authorized the Company to offer in a primary offering out of the unissued authorized preferred stock, 2,400,000 preferred shares due April 7, 2002 (Final Redemption Date), with a par value of ₱1.00 per share at an issue price of ₱1,000 per share. subject to, among others, the following terms and conditions: (a) the shares shall bear dividends at the following annual rates, payable semestraly in arrears and in cash, with the first dividend payment to commence at the end of the first semester from the date of the issuance of the shares (the "Issue Date"): Year 1, 4.0%; Year 2, 5.0%; and Years 3 to 5, 7.2% ; (b) the shareholder may convert the preferred shares to common shares to be issued by the Company from its unissued authorized capital stock, commencing on the sixth (6th) month from Issue Date and ending thirty (30) calendar days before Final Redemption Date at a conversion price computed at the average market price of the common shares as traded at the PSE for a period of fifteen (15) consecutive trading days immediately preceding one (1) day prior to the start of the Offer Period, plus a conversion premium of ten percent (10%), subject to certain adjustments due to the occurrence of certain events; and, (c) unless previously redeemed, purchased, cancelled, or converted, the preferred shares shall be redeemed by the Company at the end of five (5) years from the Issue Date. Early redemption is also allowed under certain terms and conditions. Also, on February 13, 1997, the SEC issued a Permit to Offer Share for Sale for the underlying 150,000,000 unissued common shares with a par value of ₱1.00 per share or an aggregate value of ₱150 million, which will be subsequently issued upon the exercise by the preferred shareholders of their right to conversion. The preferred shares were listed with the PSE on April 7, 1997.

The excess amounting to ₱2,326,566,774 of the offer price over the par value of the Company's preferred shares of stock, net of the cost related to the offering was credited to the "Additional paid-in capital" account in the consolidated balance sheets.

Accordingly, the first cash dividend payment on the preferred shares amounting to ₱48,000,000 (2.0% semi-annual rate on ₱2,400,000,000, representing 2,400,000 shares at the issue price of ₱1,000 per share) was made on October 7, 1997, while the second cash dividend payment of ₱48,000,000 will be made on April 7, 1998. As of December 31, 1997, the unpaid dividends that was accrued amounted to ₱24 million.

Increase in Authorized Capital and Stock Dividend

On May 27, 1997, the SEC approved the increase in the Company's authorized capital stock from ₱1,750,000,000 (divided into 1,650,000,000 common shares and 100,000,000 preferred shares, both at ₱1.00 par value per share) to ₱6 billion (divided into 5,900,000,000 common shares and 100,000,000 preferred shares, both at ₱1.00 par value per share). The SEC also approved the issuance of 1,127,747,000 common shares of ₱1.00 par value per share or an aggregate par value of ₱1,127,747,000 to cover the 100% stock dividends that was declared to stockholders of record of common shares of stock as of June 18, 1997.

Also on May 27, 1997, the SEC licensed the issuance of additional 74,719,200 common shares, with a par value of ₱1.00 per share, to cover the additional underlying shares of convertible preferred shares at the adjusted conversion price of ₱10.68 per share. The adjustment of the conversion price was made in order to reflect the dilutive effect of the 100% stock dividend declared, so as to meet the conversion requirement of the preferred shares.

Reacquisition of Preferred Shares

On January 27, 1998, the Company's Board of Directors approved the reacquisition of its outstanding preferred shares. On March 11, 1998, the Company purchased 260,290 shares of its issued preferred stocks at the prevailing market price of ₱580 per share or a total cost of ₱151,191,578, inclusive of incidental expenses.

20. Retained Earnings

The movement of the Company's retained earnings is as follows:

	1997	1996
Balance at beginning of year	₱1,442,378,936	₱392,054,636
Transactions during the year:		
Net income for the year	703,045,467	1,050,324,300
Cash dividends on preferred shares - 4% per share (Note 19)	(72,000,000)	-
Common stock dividend – 100% (Note 19)	(1,127,747,000)	-
Balance at end of year	₱945,677,403	₱1,442,378,936

21. **Coal Supply Agreement with National Power Corporation**

Semirara has an existing Coal Supply Agreement (Agreement) with NPC dated May 19, 1995, whereby the Company agreed to sell and NPC agreed to buy from the Company the coal requirements of NPC for its two (2) 300 megawatt coal-fired thermal power plants at Calaca, Batangas (Calaca I & II). As provided for in the said Agreement, the annual contracted quantity which the Company agreed to supply and which NPC agreed to buy are as follows: (a) 600,000 MT to a maximum of 900,000 MT, commencing on July 1, 1995 until March 31, 1996; (b) 1,050,000 MT to a maximum of 1,500,000 MT, after March 31, 1996 until March 31, 1997 or until Unong mine is declared depleted by the Company. In case Unong mine is not declared depleted by the Company by March 31, 1997, the annual minimum contracted quantity of 1,050,000 MT shall be reduced to 900,000 MT starting April 1, 1997. However, upon declaration by the Company that the Unong mine is depleted, the Company shall supply NPC and NPC shall buy from the Company an annual minimum of 700,000 MT to a maximum of 1,200,000 MT.

The Agreement also provided for, among others, the pricing determination of which the base price per MT of coal is determined every January 1 and July 1 and is computed based on a formula, a significant variable of which is the Import Parity Price of NPC's three (3) imported shipments received immediately before the pricing period as defined in the Agreement. This base price is subject to adjustment for penalty or bonus which is to be determined on a per delivery basis, based on a set of coal quality standards as also stipulated in the Agreement. This Agreement is effective for 15 years up to May 2010.

22. **Commitment and Contingencies**

The Company and its subsidiaries are contingently liable for guarantees arising in the ordinary course of business, including letters of guarantee for performance, surety and warranty bonds for various construction projects amounting to about ₱9.5 billion as of December 31, 1997. In addition, the Company issued corporate guarantees in behalf of AG&P and Semirara amounting to ₱727.8 million and ₱192.5 million, respectively, to secure purchase orders placed by Semirara with various suppliers, and to secure the performance bonds of various projects awarded to AG&P. DMCI also issued corporate guarantees to secure the performance and guarantee bonds for projects of certain affiliates amounting to about ₱1.7 billion as of December 31, 1997.

There are pending legal cases against the Company and its subsidiaries as of December 31, 1997 that are being contested by the Company and its legal counsel. Management and its legal counsel believe that the final resolutions of these claims will not have a material effect on the Company's financial position and operating results.

The Company and its subsidiaries lease a portion of their office premises, renewable under such terms and conditions that may be agreed upon with the lessors. The approximate minimum annual rentals on such leases after December 31, 1996 are not material to the Company and its subsidiaries' results of operations.

On March 30, 1998, the Company together with its affiliated companies and a third party executed a Memorandum of Agreement whereby the Company: (a) will assist in the development of a project by securing a revolving credit line in the amount of ₱70 million to ensure availability of funds for the project, (b) complete the re-development and renovation of the project within a period of twelve (12) months from date of the signing of the MOA; and (c) make arrangements for the use of materials and equipment of DMCI. The MOA stipulated that the Company together with the other parties shall place under custodianship with a local bank, its investment in 140 shares of stock of the project which shall be sold, under certain terms and conditions, to generate funds that will be used in the project's development. The agreement also provided that the Company shall provide various ways to compensate its affiliates for the amount already advanced by them into the project of about ₱23 million.

As of December 31, 1997, unused letters of credit amounted to about ₱192 million.

23. Recent Economic Events

The Philippines is currently experiencing an economic slowdown, which has been characterized by volatile foreign-currency exchange rates, high interest rates and declining stock prices. The Company's operations particularly in the construction contracting and real estate development, might be adversely affected through a sharp increase in the cost of construction and other materials and possible reduction in the volume of business activity. The Company's coal mining operations in Semirara might also be adversely affected through sharp increases in the cost of importations of machinery and equipment, spare parts and supplies. The prevailing high interest rates could further increase the cost and hinder the availability of funding for Semirara's operations. However, Semirara's financial exposure, particularly under a scenario of deteriorating peso to dollar exchange rate, might be partly mitigated through the corresponding expected increase in the base price per MT of Semirara's coal sales to NPC resulting from a deterioration of the peso to dollar exchange rate. The base price per MT of coal is determined using a pricing formula as stipulated in the Coal Supply Agreement (see Note 21), a significant variable of which is the Import Parity Price of NPC's three (3) imported shipments received immediately before the pricing period as defined in the agreement.

Furthermore, effective July 11, 1997, the Bangko Sentral ng Pilipinas has allowed the exchange rate between the Philippine peso and the US dollar to move within a wider range. The exchange rate of the Philippine peso against the US dollar depreciated to ₱29.45 to US\$1.00 on this date. As of December 31, 1997, the exchange rate further depreciated to ₱40.116 to US\$1.00. The resulting net foreign exchange losses incurred by the subsidiaries in 1997 (₱50.1 million of which was capitalized) from its net foreign currency denominated liabilities as of December 31, 1997 of about \$15 million (₱629 million) amounted to about ₱155.3 million. On April 23, 1998, the exchange rate of the Philippine peso against the US dollar slightly strengthened to ₱37.87 to the US\$1.00.

It is not possible to determine the future effects of a continuation of the present economic slowdown may have on the Company's and its subsidiaries' liquidity and future earnings, including the effect on Semirara's transactions with NPC. The ultimate outcome of the foregoing matters cannot presently be determined. The related effects of these uncertainties will be reported in the financial statements as they become known and estimable.