Pictured from left to right :

Joseph Donato N. Pangilinan
Director

Miguel L. Romero
Director

Antonino L. Alindogan
Chairman
(March 7, 2006 to July 11, 2006)

Reynaldo G. David
President & CEO

Board of

Alexander R. Magno
Director

Rey Magno Teves
Director

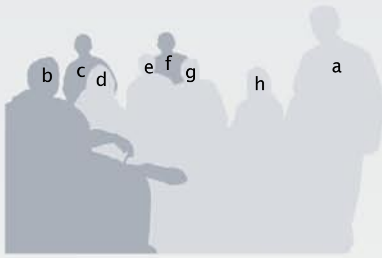
Floro F. Oliveros
Director

Ricardo G. Nepomuceno Jr.†
Director

Fernando T. Barican
Director

Directors

Management



(a) Reynaldo G. David
President and CEO

(b) Edgardo F. Garcia
Chief Operating Officer

(c) Alberto B. Reyno
First Senior Vice President

(d) Benilda A. Tejada
First Senior Vice President

(e) Jesus S. Guevara II
Executive Vice President

(f) Armando O. Samia
Executive Vice President

(g) Rolando S. C. Geronimo
Senior Executive Vice President

(h) Elizabeth P. Ong
Senior Executive Vice President

Committee

SENIOR BANK OFFICERS

PRESIDENT & CEO

Reynaldo G. David
President & CEO

SENIOR EXECUTIVE VICE PRESIDENT

Edgardo F. Garcia
Deputy CEO

Rolando S.C. Geronimo
Operations Sector

Elizabeth P. Ong
Program Development Sector
(Retired on June 30, 2006)

Panser E. Tumangan
Office of the President / CEO
(Retired on December 31, 2005)

EXECUTIVE VICE PRESIDENT

Jesus S. Guevara II
Marketing Branches Sector

Armando O. Samia
Marketing Head Office Sector

Ma. Theresa L. Quirino
Treasury

FIRST SENIOR VICE PRESIDENT

Alberto B. Reyno
Trust Services

Benilda A. Tejada
Office of the Legal Counsel

SENIOR VICE PRESIDENT

Ma. Luisa D. J. Catanghal
Transaction Processing

Corazon D. Conde
Program Development

Ambrocio P. De Leon
Office of the President / CEO

Cecilia M. Dimagiba
Financial Institutions
(Retired on March 31, 2006)

Marietto A. Enecio
Program Evaluation

Juliana N. Gamilla
Office of the President & CEO

Jose L. Gonzaga, Jr.
AMO - Mindanao

Ma. Teresa M. Jesudason
Financial Institutions

Jesus D. Macalincag
Training Center

Cynthia B. Macaraeg
Corporate Banking I

Eufemia C. Mendoza
Program Development I

Rosalina DL.P. Magat
Corplan, Budget & Special Projects

Articer O. Quebal
Remittance Center

B. Brillo L. Reynes
Small & Medium Enterprises

Valentina R. Ricasio
Business Development & Marketing II

Romeo D. Roderos
Asset Management

Nelly Y. Rosario
Credit Review & Policy Supervision

Dolores A. Santiago
Accounting

Wilfredo L. Teodoro
Factoring

Don D. Villamayor
Office of the Legal Counsel

FIRST VICE PRESIDENT

Estrella R. Aclan
Human Resource Management

Cresenciana R. Bundoc
AMO - North Luzon

Antolina G. Butalid
AMO - National Capital Region

Denis Gary B. Ditching
Compliance Monitoring

Ma. Corazon R. Gamallo
Risk Management

Evelyn D. Guerrero
Investment Banking III

Emmanuel A. Lopez
Asset Management

Clarito D.L. Magsino
Process Management

Eduardo T. Mendoza
Property & Security Management

Belen D.G. Olano
Corporate Banking II

Myra C. Reinoso
Internal Audit

Amelia S. San Juan
Investment Banking I

Angelita S. Villarosa
Internal Audit
(Retired on September 1, 2006)

VICE PRESIDENT

Dinah T. Avila
Cash Management
(Retired on June 30, 2006)

Joel Pablo Q. Bunag
Asset Management

Maribeth A. De Leon
Asset Management

Leonora A. Fernandez
Corporate Affairs

Elizabeth C. Florentino
Marketing Branches Sector

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RMC Makati

Timoteo P. Olarte
AMO - Visayas

Mario P. Pagaragan, Jr.
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Lutgarda B. Peralta
Office of the Corporate Secretary

Orlando B. Pineda
Trust Services

Mercedes A. Quianzon
Disbursement & Securities Management

Rolando S. Rojas
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Marissa V. Soriano
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PRODUCTS AND SERVICES

LOANS AND CREDIT FACILITIES

Eligible Borrowers

Single proprietorships, registered partnerships, cooperatives, associations, private corporations, private financial institutions, local government units, non-government organizations.

Acceptable Collaterals

Generally acceptable collaterals for loans are registered first mortgage on titled real estate properties, buildings, machinery and equipment and other mortgageable assets which are already owned by the applicant or to be acquired partly or fully with proceeds of the loan applied for. Hold-out on savings and time deposits as well as government security placements are also considered as acceptable collaterals.

In some cases, the Bank also accepts the guarantees of the following as part of collaterals: Quedan and Rural Credit Guarantee Corporation (QUEDANCOR), Small Business Guarantee and Finance Corporation (SBGFC), Philippine Export-Import Credit Agency (PHILEXIM), and Home Guaranty Corporation (HGC).

Interest Rate and Other Charges

The rate of interest and other charges for loans and other credit accommodations are generally market-based.

Debt-Equity Requirements

The debt-equity requirements of the Bank would depend on the type of project to be financed taken in conjunction with the Bank's assessment of the risk factors for a particular borrower.

Types of Projects Financed

1. Industrial
   a. Large manufacturing and non-manufacturing industries
   b. Small and medium manufacturing and non-manufacturing industries
   c. Industrial Estate Projects

2. Public Utilities
   a. Land, air and water transportation
   b. Telecommunications
   c. Power generation and distribution
   d. Water supply and distribution

3. Community development
   a. Housing
   b. Hospitals
   c. Schools
   d. Infrastructure
   e. Eco-tourism

4. Agro-industrial
   a. Post-harvest facility
   b. Agri-business

5. Focused Lending Programs
   a. Environmental
      - Pollution control and abatement
      - Waste minimization and recycling
      - Efficient use and/or management of natural resources
      - Occupational health and safety
      - Establishment of Environmental Management System (EMS) and certification under ISO 14000
   b. Micro-financing
   c. Lending program for franchises
   d. Program towards obtaining ISO 9000 certification
   e. New and renewable energy (NRE) projects
   f. Technology development and commercialization
   g. LGU financing program
   h. Sustainable Logistics Development Program
      - Road/RORO Terminal System
      - Bulk Grains
      - Cold Chain

6. Other Programs
   a. Factoring
   b. Loans against Hold Out on Deposit

TRADE PRODUCTS

1. Import
   a. Import Letter of Credit
   b. Domestic Letter of Credit
   c. International Standby Letter of Credit
   d. Domestic Standby Letter of Credit
   e. Collection
      - Document Against Payment
      - Document Against Acceptance
   f. Open Account
   g. Banker's Acceptance
   h. Trust Receipt
   i. Shipping Guarantee or Shipside Bond Guarantee for Good Transported at sea or waterways
   j. Advance Release for Air Transported Good
   k. Outward Remittances – Commercial Trade

2. Export
   a. Export Negotiation under Letter of Credit, Document against Payment (Cash against Documents) or Documents against Acceptance
      - Export Bills Purchase - For Clean Negotiation (Note: assessment is on the standing of the issuing bank
      - Export Bills Purchase – For Discrepant Documents (Note: requires credit evaluation and approval based on the creditworthiness of the client)
      - Export Bills Send for Collection
   b. Bills Discounting
   c. Inward Remittances – Commercial Trade
   d. Export Advance or Export Packing Loan (Note: requires credit evaluation and approval based on the creditworthiness of the client)

TRADE SERVICES

1. Opening bank or issuing bank
2. Advising
3. Negotiating
4. Confirming
5. Paying
6. Collection of Custom Duties

INVESTMENT BANKING SERVICES

1. Financial advisory and investment consultancy
2. Financial packaging/instrument design for debt and/or equity requirements
3. Securities underwriting/issue management
4. Arrangement for bond flotation and mergers, acquisitions, divestments, loan syndications, project finance, joint ventures and privatizations
5. Underwriting for debt or equity requirements

DEPOSIT PRODUCTS AND CASH SERVICES

1. Deposits
   a. Current Account
      - Regular
      - Interest-Earning
   b. Savings Account
      - Regular Savings
      - Option Savings
      - Special Savings
      - Dollar Savings
      - Savings Deposit for the Youth
      - Savings Deposit In-Trust-For
      - Pensioners' Special Savings
      - Direct Deposit for US Veteran Pensioners
      - DOLE-SSS-DBP Maginhawang Manggagawa Savings
      - Philhealth-DBP ADA
      - Teachers' Savings
      - Treasurer In-Trust-For (TITF) Savings
   c. Time Deposit
      - Peso
      - Dollar
      - Special Investors Resident Visa (SIRV)
   d. ATM Services

2. Fund transfer services
   a. Manager's check
   b. Demand draft
   c. Telegraphic transfer
   d. Foreign Exchange Dealership
   e. Foreign Exchange Remittance
   f. Agent of Asia United Bank Inward Remittance Service
   g. Domestic Fund Transfer thru Real Time Gross Settlement (RTGS)
   h. Domestic Fund Transfer thru Electronic Peso Clearing Settlement (EPCS)

3. Special/Other Services
   a. Acceptance of Payments/Remittances for SSS
   b. Servicing of the Government's Modified Disbursement Scheme
   c. Servicing of the Payroll of the Department of Education Teachers
   d. Acceptance of Collections of the National Collection Officer for Remittance to the Bureau of Treasury
   e. Authorized Agent Bank of the Bureau of Internal Revenue
   f. Payroll/Remittance Servicing
   g. Deposit Pick-Up/Withdrawal Arrangement
   h. Servicing of Payments of PLDT Subscribers
   i. Acceptance of Debit Bills Enrollments
   j. Acceptance of Sunday Payments

TRUST PRODUCTS AND SERVICES

1. Investment Management Account
2. Unit Investment Trust Fund – Gintong Sikap Secure Fund
3. Traditional Trust Services
   a. DBP Kabalikat Retirement Plan
   b. Revocable Trust Account
   c. Life Insurance Trust
   d. Mortgage Trust Indenture
   e. Custodianship
   f. Escrow Agency
   g. Stock and Transfer Agency
   h. Registry and Paying Agency
   i. Loan Agency
   j. Debt Service Reserve Agent
   k. Public Trusteeship
   l. LGU Bonds Trusteeship
   m. Sinking Fund Management

TREASURY PRODUCTS AND SERVICES

1. Interbank borrowing/lending
2. Government Securities dealership
   a. TBills
   b. RTBs
   c. NFA Bonds
   d. Pag-ibig Bonds
3. Forex Securities dealership
4. Deposits
   a. Special Savings Deposits
   b. Option Savings
   c. Dollar Time Deposit

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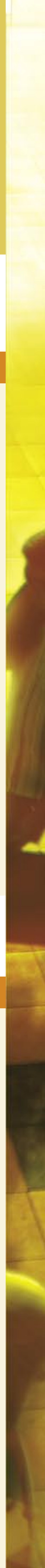
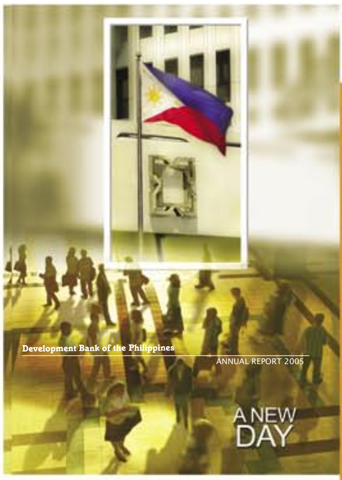


CONCEPT & DESIGN: MODE MATRIX MANILA INC.

Development Bank of the Philippines

ANNUAL REPORT 2005

A NEW DAY



OUR COVER

Nothing perks up a brand new morning than a stress-free sleep in the evening. At the close of the day, realizing that you have accomplished so much and feeling good that you have hurdled all obstacles with ease, waking up to the promise of a new day comes naturally.

This is the inspiration for this year's annual report. Capping the first half of the decade with a high note – the Development Bank of the Philippines faces the next half of the decade full of optimism and excitement.

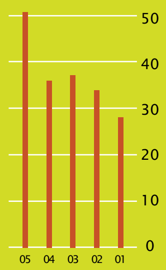
This year's cover design captures a workforce on its way to the office – excited, motivated, energized, with spring in their steps – juxtaposed with a fuzzy facade of the DBP logo and the Philippine flag are highlighted to suggest that these people are working for the bank and the country.

Inspired by its performance in the past, DBP is looking forward to help the country secure a brighter tomorrow. After achieving its financial targets, DBP is now poised to refine its organization to make it more relevant and efficient in the years to come.

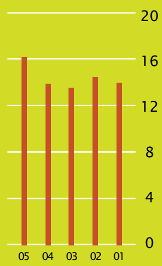
Contents

Financial Highlights*
(in Million Pesos)

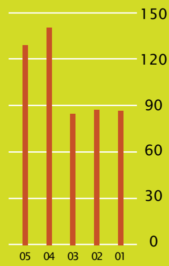
Year	Total Deposits
2005	50,775
2004	36,439
2003	37,404
2002	34,177
2001	28,068



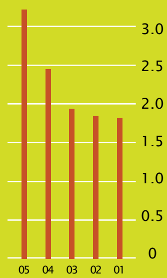
Year	Gross Income
2005	16,170
2004	13,980
2003	13,549
2002	14,505
2001	14,013



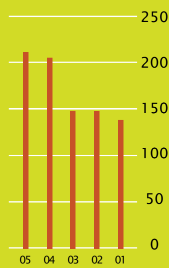
Year	Total Borrowings
2005	129,966**
2004	141,530**
2003	85,615
2002	87,811
2001	87,425



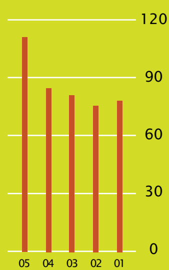
Year	Net Income
2005	3,212
2004	2,441
2003	1,949
2002	1,847
2001	1,837



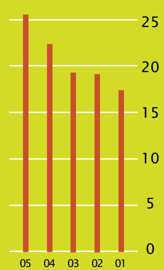
Year	Total Resources
2005	212,889
2004	206,078
2003	148,755
2002	148,643
2001	138,911



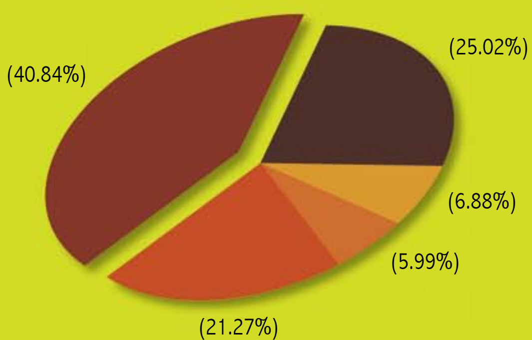
Year	Total Loans
2005	111,534
2004	85,033
2003	82,328
2002	76,369
2001	78,652



Year	Total Capital Funds
2005	25,484
2004	22,419
2003	19,241
2002	19,105
2001	17,408



Loan Portfolio by Priority Areas



Developmental Loans:	(in Million Pesos)
Infrastructure and Logistics	21,711
Environmental Development	5,976
Social Services Development	5,196
Micro and SME Development	18,460
Total - Developmental Loans	51,343
Commercial Loans	35,451
Grand Total	P86,794***

* Non-consolidated
** Revalued based on new PAS and BSP requirements
*** Excludes interbank loans of P24,740 million

MESSAGE OF Her Excellency

We are a great people.

We have honest students and honest cops.

We have scaled the heights of Mount Everest;

dominated the Southeast Asian games;

we have won international beauty titles;

and of course punched our way to triumph in the boxing world.

Our people compete and win every day in every imaginable job

throughout the world. Individually, we've taken the world on and won;

together, we must take on the challenge of creating

a new, peaceful, humane and competitive nation and prevail.

State of the Nation Address
July 24, 2006

GLORIA MACAPAGAL-ARROYO
President
Republic of the Philippines

REPORT OF THE BOARD of Directors

The Board of Directors is happy to report that 2005 was a year of great achievements and robust gains for the Development Bank of the Philippines.

By every measure, 2005 defines a watershed year, a fitting culmination to the year-on-year milestones and successes of the Bank that began in 2001.

Guided by the visionary and stable leadership of the Board, these gains are the product of the hard work, the diligence and the commitment of the entire DBP family.

Our work over the past five years have borne the good fruits of a solid balance sheet, strong profitability, and a banking orientation that is aligned with the development thrusts of government in infrastructure and logistics, micro and small and medium enterprises, social services in housing, education and migrant workers, and the protection of the environment.

The Bank's balance sheet shows solid growth in its loan portfolio, from P77 billion in 2001 to P87 billion in 2005, with a non-performing loans (NPL) ratio of 7.44 percent against the industry average of 8.51 percent, and an NPL coverage of 95.9 percent against an industry average of 78.9 percent.

The strong profits of the Bank showed in its P3.2 billion net income in 2005, up from P1.8 billion in 2001. As a consequence, the government in 2005 received P1.606 billion in dividends from the Bank, up from the P756 million in dividends declared in 2001. Return on equity after loan loss provisions improved markedly to 14.80 percent in 2005, from 10.89 percent in 2001.

Beyond all these measures of institutional strength, however, the Board takes special pride in underscoring the new ground that we have broken as a development bank

As we strengthened our treasury operations to improve profitability, the Bank also ensured a more equitable distribution of our credit programs in the regions, paying particular attention to supporting enterprises in the war-torn areas of Mindanao and the poverty stricken provinces in the Visayas.

As we improved our capacity to cut the "big deals" and worked in tandem with the largest banks in the industry, we also initiated a microfinance program to support projects that have direct and immediate palpable impact on the lives of the poor.

As we improved the efficiency of our use of official development assistance, we also initiated a unique reforestation program, the DBP Forest Program, where more than P50 million were released to plant trees on 3,906 hectares, working with NGOs, POs, not only for forest cover but also for sustainable livelihood and biodiversity. The Program was conferred the Most Outstanding Environmental Developmental Project Award from the Association of Development Financial Institutions in Asia and the Pacific (ADFIAP).

As we increased our wholesale lending to private financial institutions, we expanded lending to local governments especially for programs that will have immediate effects on the quality of life of our people, such as the Palengke ng Bayan, bagsakan facilities, bulk water production and waste treatment plants.

As we broadened our participation in major industrial ventures, we likewise expanded our factoring facility to assist small and medium enterprises, specially with both backward and forward linkages to the major corporate entities.

As we nurtured a larger presence in our country's power infrastructure, we also supported investments in new and sustainable energy sources.

As we worked the traditional areas of the DBP's banking strength, we also ventured into the frontiers of opportunities to enhance our institutional capacity that would bolster national development efforts.

Unprecedented is the Bank's Sustainable Logistics Development Program, which soon came to be the Strong Republic Nautical Highway. The RO-RO, as it is popularly known, has transformed what was once a vision into the reality of linking the many islands of our country through moving bridges.

Transforming visions of development into reality. This summarizes what the Bank has done, from 2001 to 2005.

And the best part of it is, the Bank has succeeded in making development financing a profitable undertaking.

That is what development banking is all about.

There are two aspects to the enduring brand of our development banking. The first is the corporate culture of the Bank. The year 2005 witnessed a number of calamities that befell our country. DBP took to the task of delivering immediate relief not as something beyond the call of duty but as an integral element of our development banking purpose.

The other is the Corporate Governance that we have put in place and continue to implement. As this annual report sees print, the DBP has just been adjudged by the Institute of Corporate Governance to have had the best Corporate Governance in the entire public corporate sector for the year 2005.

DBP has achieved much. But what we are proudest of, is the fact that we have served the Filipino people.

VITALIANO N. NAÑAGAS II *
Chairman

** Until February 22, 2006*

REPORT TO THE President

Dear Madame President:

I am very pleased to present to you, Madame President, our last year's performance as contained in the 2005 Annual Report of the Development Bank of the Philippines. Our report's theme, "A New Day," captures the exhilarating feeling of the DBP employee who did quite well during a particularly challenging year. His optimism and excitement prime him to take on the greater responsibilities ahead.

We continued to apply the twin measures of development impact and financial sustainability in our self-assessment, Madame President. The Bank tracked its development directions along four priority thrusts: Infrastructure and Logistics, Environment, MSMEs (Micro, Small and Medium Enterprises), and Social Services. We deemed these thrusts to be closely aligned with your 10-Point Legacy Agenda for growth, and they are also where our fund sourcing activities had encouraging results. Developmental loans accounted for close to 60% of our loan portfolio in 2005.

Profitability hit a new high in 2005. This is one of the outcomes of the organizational refinements we undertook in early 2005. The formation of the Financial Markets Sector allowed the Bank to effectively harness the strengths of its balance sheet and to exploit emerging opportunities in domestic and global financial markets. Treasury operations helped build up the Bank's resource base and delivered additional revenue flows.

In my view, Madame President, DBP's strong income performance in 2005 did not only respond well to the challenge posed by the fiscal sector. It also prepared the Bank for the imminent rediscovery of the private sector business confidence.

DEVELOPMENT THRUSTS

DBP maintained the same priority development areas in 2004, namely Infrastructure & Logistics, Environment, MSMEs (Micro, Small and Medium Enterprises) and Social Services. Since these are well-aligned with National Government thrusts, we directed our financing programs and marketing efforts in 2005 to projects consistent with these priorities. Aside from identifying the right projects, however, the more compelling work was to establish strategic partnerships to pursue them.

Infrastructure & Logistics

The Sustainable Logistics Development Program (SLDP) continued to be the backbone of the Bank's Infrastructure and Logistics development area. Total approved projects for SLDP in 2005 amounted to P3.86 billion made up of 10 projects for the Road-RORO Terminal System, 31 for Cold Chain and 146 projects for the Grains Highway. Another 33 projects, amounting to P1.19 billion, were in the pipeline.

The Central Nautical Highway took shape in 2005 as a major alternative artery to the Eastern and Western nautical highways. It traverses the Luzon provinces of Quezon, Sorsogon, Masbate and Cebu in the Visayas, and links up with the latter's RORO route to Cagayan de Oro in Mindanao. The Luzon leg of the Western nautical highway also branched out to Palawan from its take-off point in Manila via Batangas and Mindoro. We also held discussions with the Department of Transportation and Communications (DOTC), Philippine Ports Authority (PPA), the concerned local government units (LGUs), shipowners and other stakeholders, especially those involved in port development.

Our other projects under Infrastructure and Logistics in 2005 might not have the same integrative impact as the SLDP but they also responded to clear development needs. Among these were the National Transmission Commission's (NTC) Leyte-Cebu Interconnection Uprating Project, the P5 billion syndicated loan for additional cell sites to spur regional development, and various smaller projects handled by the branches.

Environment

By our fourth year as an ISO 14001 certified institution, we already had a good handle of key environmental projects. Addressing environmental concerns of DBP-funded projects had become second-nature to our employees. Projects in 2005 under the environment priority areas also demonstrated our having equated sustainability to environmental responsibility.

A major initiative launched by the Bank in April 2005 was the DBP Forest Program. With a P50 million seed fund from Kreditanstalt fur Weideraufbau


The DBP Family Credo

(KfW) of Germany, the program has undertaken 17 reforestation projects covering 3,906 hectares distributed across the archipelago. These were designed to reforest denuded areas, restore the coastal ecology and provide alternative livelihood to various people's organizations. By integrating funding support to this program to our lending activity, we ensured its continuity as long as the Bank lends money.

Loans released to pollution control projects under JBIC's Environmental Infrastructure Support Credit Program and KfW's Industrial Pollution Control Program benefited 17 projects for P2.8 billion. The Bank also approved five projects amounting to P167 million under KfW's Credit Line for Solid Waste Management; another 29 projects amounting to P1.4 billion were in the pipeline. Approvals for major water projects in the Visayas and Mindanao, through water districts and LGU water projects, approximated P2.5 billion, responding to the need for potable and sustainable water supply. The first of four Adaptable Program Loans under the Rural Power Program of World Bank, APL I of P530 million, was fully committed to seven accounts. DBP also concluded negotiations with the National Transmission Company for the financing of the purchase of the latter's sub-transmission assets by electric cooperatives.

In 2005, we put in place the Greenhouse Gas Emission Reduction Program of the Bank. The program serves to harness carbon credits from DBP's borrowing clients for trading in the evolving carbon market. Through the Bank's promotional efforts, a growing interest in this clean development mechanism resulted, both at the carbon credit sources and among their investors in developed countries. We foresee greater activity in this program in coming years.

MSMEs

The MSMEs priority development area posed one of greatest challenges to the Bank. Despite an outstanding MSME portfolio of P18.6 billion as of 2005, DBP needed to search for more effective ways of delivering financial resources to this sector that constitutes 99.6% of Philippine enterprises.

In 2005, a separate department for microfinance under wholesale banking operations was created. This entailed the inclusion of smaller banking institutions in DBP accreditation system and the dedication of personnel to the task of delivering financial services to micro enterprises. Towards the close of the year, we began the initiatives for a vertically integrated delivery unit for microfinance. Most of our branches also catered to SMEs in their locality under SULONG. For the year, releases to SMEs reached P10.5 billion, not counting a total of P465 million credit lines granted to an SME and a Microfinance wholesaler institution, respectively.

Three MSME oriented projects were at various stages of implementation. The DBP Factoring Facility, directed at SMEs doing business with "Big Brother" corporations, increased its volume by more than 60% over that of 2004. A project on alternative trading system started in 2004, the Marketplace for SME Receivables Purchase (M4SME-RP), hurdled the required clearances from government agencies and will likely do its first transaction in 2006. Finally, we also established the first seven of a nationwide network of Business Assistance Centers (BACs). BACs are one-stop-shops designed to help out MSMEs under our Sustainable Partnership for Energizing Entrepreneurship Development (SPEED) Program.

The seven BACs in 2005 were set up in the campuses of Mariano Marcos State University in Laoag, Ilocos Norte; Benguet State University in La Trinidad, Benguet; Pampanga Agricultural College in Magalang, Pampanga; Camarines Sur State Agricultural College in Pili, Camarines Sur; Aklan State University in Kalibo, Aklan; Central Philippine University in Iloilo; and Foundation University in Dumaguete City. SPEED fosters a partnership with DTI, DOST, NGOs and private/state universities and colleges for the benefit of MSMEs.

Social Services

This priority program supports investments in social capital, particularly in the areas of education, healthcare and community development. With public services devolved to the LGUs, many of our projects in social services are pursued in partnership with them. Together with projects in the Environment priority area, it is in Social Services where we closely interact with LGUs and other government agencies.

With 2005 exemplifying the strategic role of our overseas Filipino workers (OFW) to the economy, we decided to strengthen our support to this sector. We partnered with the Overseas Workers Welfare Administration (OWWA) in designing an OWWA Credit Program with an initial funding of P62.5 million. The program responds to the OFW's twin needs: for his pre-departure financing and the subsistence needs of his family. DBP offered the OWWA Credit Program in six branches (Commonwealth Avenue – NCR, San Fernando – Pampanga, San Fernando – La Union, Iloilo City, Cebu City and Davao City), registering a total of 932 OFW borrowers for P31.4 million in 2005.

Most of the projects in education and healthcare were originated by the branches. Several cities and municipalities as well as private institutions tapped our branches for the funding of school houses and related facilities. Many of these were incremental and answered the need for additional classrooms. A few big projects, however, stood out like the City of Manila's loan for the transfer of the City College of Manila to a new campus at the Mehan Garden, and De la Salle College of St. Benilde's funding requirement for its 14-storey School of Design and Arts.

Investment Banking

DBP also brought to the fore its investment banking expertise to mobilize funds for various government agencies and private corporations. Illustrative projects included our participation in the P8 billion long term notes of the National Food Authority (NFA) to ensure food security and price stability of rice, underwriting the Home Development Mutual Fund's (HDMF) P5 billion Pag-IBIG Housing Bond Floatation, and serving as one of the selling agents for the 7th Retail Treasury Bond. We also figured prominently in funding arrangements for big private sector projects like Globe Telecommunication's P5 billion syndicated loan, Nutri-Asia Pacific's US$215 million syndicated bridge facility, and a P3 billion loan for the North Triangle Depot. These projects in 2005 attested to our Bank's reliable placement power and effectiveness in domestic and foreign fund mobilization.

Fund Sourcing

DBP made breakthroughs in its fund sourcing activities. The bank has been directing these funds to socially-responsive programs and to all its development initiatives. In 2005, negotiations for three facilities, in the total amount of P2.4 billion, were concluded. These are the EURO 25 million facility from the European Investment Bank (EIB), US$10 million facility from the Swedish International Development Agency (SIDA), and US$5.287 million Credit Line for Micro, Small and Medium Enterprises (CMSME).

The European facility can be accessed by both private companies and government agencies to finance commercial infrastructure, agro-industry, tourism, and related services including leasing, microfinance, health, and urban development. The SIDA facility is dedicated to the funding of environmental projects. The CMSME, on the other hand, has been enhanced with the inclusion of local government units and microfinance institutions as eligible borrowers.

Branch Operations

Five Area Management Offices (AMOs) continue to supervise DBP's 77 branches nationwide. AMO-Southern Luzon has jurisdiction over 12 branches, AMO-NCR has 6 branches while AMO-Northern Luzon handles 16 branches. AMO-Visayas has jurisdiction over 19 branches, while AMO-Mindanao supervises 24 branches.

In 2005, the branches released a total of P7.31 billion for various developmental and high-impact projects in support of DBP's role as an effective arm in financing development in the countryside. Branch loan portfolio aggregated to P17.1 billion or 19.7% of bankwide portfolio. The branch network also generated P30.1 billion in deposits representing 59.2% of total bankwide deposits.

Highlights of developmental and community building initiatives by the branch network include the P1.98 billion assistance to four water districts including P62 million for the Nasugbu Water District. Branch assistance to education and health care projects amounted to P1.92 billion as of year-end 2005.

Trust Operations

Trust portfolio as of year-end 2005 amounted to P17.39 billion, an increase of P1.95 billion or 12.63% compared to the end 2004 level of P15.44 billion. The 2005 portfolio comprised of Investment Management Accounts representing 58.83% of total portfolio, Traditional and Other Fiduciary Accounts at 39.95%, and Common Trust Fund accounts at 1.22%.

Gross trust income for the year of P85.74 million, less administrative expenses of P54.41 million, resulted in a net income of P31.33 million.

Human Resource Management & Career Development

To promote enterprise-wide risk management, the Bank's Human Resource Management collaborated with various institutions in updating and strengthening the skills of its personnel through training on legal and credit aspects, internal controls, and International Financial Reporting Standards. It also reinforced its young and high-potential officer workforce through rigorous training under the Management Associates Program. The program started its first year of operations in 2005 and will continue to be implemented in the coming years in line with the Bank's quest for excellence and competitiveness.

As an effective business partner in organizational strengthening and business capital management, the Bank promoted a culture of excellence by encouraging strong corporate values among management and staff, proactive talent acquisition and retention strategies, relevant training programs, and an effective performance management system aligned with the Bank's thrusts. The Bank also maintained a compensation structure and employee benefits program that were both competitive industry-wide and performance-based.

To adopt a leaner organization and improve its operations through the realignment or streamlining of work processes, DBP implemented an early retirement program for officers and employees, aged 50 and above, with at least 15 years of creditable government service.

Organizational Strengthening

The Bank continued organizational refinements to enable it to be more responsive to its target markets and to fully achieve its development mandate. These refinements were envisioned to improve DBP's core line of business and profitability, thus lessening its reliance on Official Development Assistance funds while strengthening its financial viability.

The first phase of organizational refinement provided for the realignment of certain responsibilities to specific functions, changes in lines of control, authority and responsibility, and the creation of new departments. Thereafter, the right people were tapped for the right jobs. The position of Chief Finance Officer was created to strengthen the Bank's treasury, institutional relationships, and remittance center operations. Two units were created, namely Financial Institutions and Remittance Center, with the latter as a proactive move to capture the growing OFW market. The refinement also embodied a modified matrix system, an internal structure that forces people to answer to more than one leader.

The second phase of refinement involved streamlining the organizational structure of various sectors in the Bank to further promote efficiency and operational effectiveness and ensure the alignment of organization goals with individual goals.

Computerization

To enhance its competitiveness in a highly technology driven market, the Bank continues to upgrade and improve its information technology capability. It focused on maximizing the use of technology through the purchase and installation of various systems such as the New Integrated Deposit Servicing System, the Integrated Messaging and Collaboration System, and data warehousing to shorten the time required for the preparation of reports requested by top management. Its service delivery system was improved with the adoption of streamlined guidelines for the setting-up of Automated Tellering Machines, the conduct of studies on adopting contactless time capture machines for employee attendance and leave credit availment, and the deployment of electronic workflow applications at the Credit and Appraisal Management for the review, approval, and transmittal of documents to and from the branches and Head Office.

Internal Credit Risk Rating System (ICRRS)

The Bank has also put in place the critical components of its risk management system in accordance with good governance principles and practices. Along this line, the Bank has adopted the ICRRS in time for the implemention of the Basel II in 2007. With BSP Circular No. 439, s. 2004, banks are also required to rate all borrowers with assets of more than P15 million in accordance with a system approved by the BSP. DBP's Credit Review & Policy Supervision office adapted the system and calibrated it to suit DBP's thrust and management.

The ICRRS is progressive in terms of helping the Bank's account officers to uniformly assess new and existing accommodations based on factors and standards consistently applied, thus serving as an effective tool for marketing and credit decisions, evaluating the credit risk of existing and potential borrowers, and for pricing purposes.

FINANCIAL PERFORMANCE

Our financial performance in 2005 showed the effectiveness of our scale and scope strategies. We built up business volumes where we have been traditionally strong at, and put resources in new areas that have emerging excellent prospects. To capitalize on the strengths of the Bank's balance sheet, we brought in the expertise needed to exploit the shifts in the domestic and global financial markets. We refined our organization to match business prospects with manpower and financial resources.

Breaking Records

As of 2005, DBP climbed two rungs, from No. 9 to No. 7 in the country's top 10 banks in terms of assets. While the private banks did it through acquisitions and consolidation, DBP did it through internally generated growth. Its net income performance was even more impressive, occupying the 4th rank, after only BPI, Metrobank and Citibank. Our loan portfolio of P79.3 billion (net of unearned discount and including accrued interest receivable) is a record breaking performance. New all-time highs were also attained for deposits (P50.8 billion), capital funds (P25.6 billion), gross income (P16.2 billion) and net income (P3.2 billion).

DBP more than matched the benchmarks it set for itself in 2005. Return on Average Equity (non-consolidated) improved from 12.76% in 2004 to 14.80% for a very significant rise of 204 basis points. Return on Average Assets (non-consolidated) likewise rose from 1.55% to 1.76%. Aside from the build-up of assets, there was also significant improvement in asset quality. Past due rate on loans scaled down by 237 basis points from 11.92% to 9.55%. Net interest margin (non-consolidated) narrowed from 4.00% to 3.80% in 2005 to suggest the increase in the cost of funds. This conclusion is quite true, but only because in 2005, the Bank's treasury operations had the capacity to turn around the higher cost funds and make a spread. Manpower cost increased in 2005 but this was more because of the need for provisions as the Bank pushed its early retirement program.

Financial Markets Sector

Financial Markets Sector was the creation of our organizational refinements in 2005. It housed the Office of the Chief Finance Officer who had an overarching supervisory role on Treasury, Financial Institutions and Remittance Center. Strong capability build-up by tapping available expertise from private unibanks complemented the refined organization. These management moves proved to be correct and timely in the context of global market developments and changes in the BSP policy posture.

Treasury Operations explored alternative investment outlets and other avenues for income optimization while maintaining its attention on the traditional domestic markets. FCDU resources went up by 107% to US$589 million while bills payable also rose by 157% to US$392.5 million. Foreign currency based businesses scaled new heights boosted by adept investment selection that resulted in trading gains and interest income. Towards the close of 2005, Treasury also set into motion the capital build-up program of the Bank through Tier 2 and Tier 1 capital notes issuances to anticipate the regulatory adjustments.

Financial Institutions (what used to be the wholesale banking) continued to cater to the needs of its participating financial institutions (PFIs). However, the onset of consolidation among banks reduced the volume from PFIs in 2005. Financial Institutions created a new unit, the Correspondent Banking and Trade Development, for a renewed emphasis on trade finance and LC business. Volume in this business line jumped 470% to reach US$889 million. But more importantly, DBP learned how to leverage its correspondent banking relationship to harness reciprocity.

The decision to strengthen support for OFWs required the setting up of the Remittance Center to serve as its backbone. In 2005, our Remittance Center began to establish foreign offices and alliances in key OFW destinations. While it takes some time to complete the network of remittance offices, we look forward to making a difference in this endeavor.

CONTINUING COMMITMENT

With the Financial Markets Sector now in place, the Development Bank of the Philippines has transformed into a more complete development finance institution. It is now in a better position to maximize its stockholder value to the Philippine Government, while at the same time possessing the resources to be an effective development agent. I believe, Madame President, that the full realization of DBP's institutional strength is in the healthy balance of its development orientation and its earning capacity. Any slackening of either one slows the other down.

Our 2005 performance allowed us to have a grasp on how well the Bank can perform financially without abdicating its developmental role. Last year was a confirmation that our twin goals of development impact and profitability can run side by side. Occasionally, one of these goals can be made to outstrip the other to create the urgency for catching up. Madame President, DBP's sterling financial performance in 2005 only serves to build up its resources for a continuing commitment in development finance.

REYNALDO G. DAVID
President and CEO

Development Bank of the Philippines

VISION STATEMENT

We are the pre-eminent Philippine Bank for financing development.

DBP is dynamic, environmentally responsible and globally recognized.

MISSION STATEMENT

To influence and accelerate sustainable economic growth of the country. DBP works with and through others to attain its objectives, and ensures its viability by the prudent management of risks and returns.

DBP and the Economic Environment

Despite the incessant political noise, frequent oil spikes, dry spell, and the EVAT, the year 2005 managed to post a 5% growth in the domestic economy, thanks to the exceptional recovery in Finance, the resurgence in Mining, and the resumed Government Expenditure sub-sectors. This was further bolstered by the strong overseas Filipino workers' (OFW) remittances to post a 5.6% growth in the national economy. It could have been more had the multi-billion peso revenue generated by the business process outsourcing (BPO) sector been reflected.

The slowdown, when compared to 2004, was expected as everyone anticipated risk factors like budget deficit and debt burden, oil price spikes, and the slowing down of the export market.

SUPPLY-DRIVEN GROWTH

Services, while easing somewhat to a 6.4% growth from a high of 7.6% in 2004, still provided the drive in the economy. It is Finance's 13.6% rise that took the cudgels this time for the Service Sector as all its other sub-sectors slowed down including Transportation, Communication, & Storage (TCS) from 11.2% to 7.2%. Agriculture eked out a 1.8% growth as it took its toll from the prolonged mild dry spell in the first half of 2005. Industry's 4.9% mirrors the 5.6% momentum in Manufacturing and a 9.3% resurgence in Mining.

The growth driver on the expenditure accounts, Private Consumption, also slowed down to 4.9% from 5.8% in 2004. This was compensated by the 4% increase in Government Consumption, an improvement from its stagnant performance a year ago. Investment remained weak, as it contracted by 6%. The drop was on account of the significant depletion of stocks by 54% and the weak demand for durable equipment by 7%. Exports were up 4.2% while imports grew by 2.4%, both driven by the increase in trade of non-factor services such as tourism.

THE BANKING ENVIRONMENT

Despite the various reforms the banks had to contend with in 2005, coupled with an economic backdrop of high oil prices, rising global interest rates, lower farm output, and to some extent, political concerns, the Philippine commercial banking system ended the year on an upbeat note, showing signs of improvement in asset quality, lending and deposit base. This creditable performance by the banks was supported mainly by the continued economic expansion manifested by the easing inflation environment, improving fiscal performance, and surging peso, which resulted to an average GDP growth rate of 5% for the whole of 2005.

Resources of commercial banks grew by more than 7% to P4.141 trillion fueled by increases in bank borrowings of more than 14% to P471.4 billion, as well as deposit liabilities of more than 8% to P2.783 trillion. Growth in deposits, the system's main source of funding, carried consistent growth marks for the past three years, averaging at 8.4%. Although NPL ratio registered a single-digit level of 8.51% from 12.72% in end 2004, growth in net bank lending, meanwhile, continued to be modest at almost 3% to P1.518 trillion total loans in end 2005.

Asset quality of banks improved as indicated by the single digit NPL ratio of 8.51% and reflected in the marked decline in NPLs which decreased by 32.36%.

Banks' ROPAs and NPAs likewise showed decreases of 2.49% and 18.31%, respectively, reflecting Banks' ability to dispose not only of NPLs but foreclosed assets as well. Banks may find their non-performing assets significantly reduced further after the BSP approved lately a new regulation allowing joint ventures with real estate firms using real and other properties acquired (ROPAs).

Under the Special Purpose Vehicle, banks unloaded a total of P96.7 billion worth of NPAs through SPVs as of end-2005, or just a fifth of what banks promised lawmakers when the law offering perks to such deals was being formulated. Banks were estimated to have P520 billion worth of bad assets and have unloaded P103 billion during the SPV Law's first two years of implementation starting 2003. The law has been extended to give way to the financial community's projection of reaching the P200-billion target bad asset disposal, given another two years.

Initial figures reported by banks listed in the Philippine Stock Exchange indicate they were among the better performers in the equities markets in 2005, with bottom lines reporting earnings performance of over 20%. However, on an industry level, banks' average return on equity (ROE) reflected a lower 12% but still considered as creditable showing in 2005.

Last year, the BSP issued policy guidelines to signal the start of two of the most important banking reforms: (1) the adoption of banking standards under Basel II accord and (2) the aligning of local accounting with international standards.

The Basel II accord hopes to prevent bank failures by making sure that banks put up adequate capital. This requires banks to compute their capital adequacy ratio (CAR) in a way that would reflect all the risks that they are taking.

On the other hand, in shifting to the International Financial Reporting Standards or IFRS, the BSP approved the provisions of the Philippine Financial Reporting Standards and the Philippine Accounting Standards effective 2005. Among others, the rules require amendments to the booking of investments in debt equities and securities and recognition of sale of non-performing assets to SPVs.

Obviously, the poorly capitalized banks are the ones which will have problems complying with the new set of accounting standards and the Basel II accord as both are expected to erode the capital base. Already, 5 of the top ten KBs reported declines in total capital as of end 2005 as they begin to adjust to these standards.

With the new regulation calling for high capitalization, this might spawn a new wave of consolidation in the banking industry, similar to the ones that happened in previous years.

As of January 2006, BSP came out with its amendments to its regulations on the "fit and proper rule" centering on (1) persons disqualified to become directors; and (2) effects of non-possession of qualifications or possession of disqualifications. This is to ensure that officials tasked to manage banks and other financial institutions possess the required integrity and competence. To further ensure continued growth and promote healthy competition, BSP has liberalized certain aspects of banking. Among them is the lifting of the moratorium on bank branching except in 7 cities and one municipality in Metro Manila as well as allowing banks to outsource some of its operations to make them more cost efficient.

In early 2006, credit rating agency FitchRatings recognized the banks' performance in 2005 by revising its outlook particularly on four Philippine banks from negative to stable and at the same time affirmed all its ratings on the banks ranging from BB to D/E on their long and short term foreign currency, long-term local currency, individual and support ratings.

For DBP, Fitch gave the following credit ratings update published in May 2006: Individual, C/D and Support, 3. DBP's individual rating reflects its sound balance sheet strength and good profitability.

On July 13, 2005, Moody's Investors Service changed the outlooks for DBP's foreign currency B1 long-term deposit rating and local currency Ba2 long-term deposit rating to negative from stable together with other Moody's-rated Philippine banks.

This rating action followed the change in outlook to negative from stable for the Philippines' sovereign rating on foreign currency debt/deposit ceilings as well as foreign and local government bond ratings. The weaker outlook for the sovereign ratings reflects Moody's concern that the political turmoil which has beset the Arroyo administration may negatively affect the budget and external payments position.

DBP's constrained B1 rating essentially reflects its standalone financial fundamentals. In view of its 100% state ownership and status as the policy bank financing the country's long-term infrastructure projects, regulatory support can also be expected, if needed. But we are mindful that the government's pressured fiscal position and the political instability could constrain future assistance.

The recent change in outlook does not relate to bank-specific issues. Therefore, DBP's Bank Financial Strength Rating remains stable at D. At D, it is rated at the same level as the Philippines' stronger banks – Metropolitan Bank & Trust Co., Banco de Oro Universal Bank and Unionbank of the Philippines. Only the Bank of the Philippine Islands is rated higher.

GUARDED 2006 OUTLOOK

Philippine prospect for higher growth in 2006 is hinged on a rebound in the agriculture and export sectors. However, a Democles' sword hangs before most economies, i.e., the rising world oil prices – an external and uncontrollable factor. Once again, government economic managers cut their growth targets while local and international businesses remained either conservative or cautiously optimistic.

On top of the declaration of a week-long state of national emergency in late February to counter coup attempts and which hurt temporarily the tourism industry, there is still the attendant political uncertainty being faced by the country on the impending charter change. Nevertheless, government remains confident the economy will grow at a faster pace in 2006 than in 2005.

Consumption is seen as the main driver from the demand side with support from remittances. It is feared that the EVAT and the volatile oil prices could dampen personal consumption. However, the low interest rate environment, conducive to greater consumer credit and mortgage loans resulting to vibrant private consumption, coupled with the on-going government pump-priming activities, may boost the expenditure sector. Increasing globalization can reverse trade directions for countries with restricted markets such as the continued dependence of RP exports on the US market. While prospects are bleak from exports, capital inflows, particularly Foreign Direct Investments (FDIs), remain positive. The Philippines is getting new attention, thanks to a budgetary makeover that has put the country in a position to benefit from an anticipated surge of foreign funds into the region this year. Also, while the electronics exports may be anemic, the country's biggest export – labor – is booming. OFW remittances account for 10% of GDP. The backlash, of course, is that with this labor exodus of select professionals, rosy government projects have been negated.

From the supply side, Services will remain as the major contributor to GDP with key growth drivers seen in BPO, information technology and IT-enabled services, telecommunication, and tourism. A rejuvenated agricultural sector is expected on a mild La Niña scenario, otherwise, a slowdown may occur on increased rainfall that could hurt farm production and have spill-over effects on the food and beverage sector. In Industry, not much growth is expected from the manufacturing sector, particularly the export-oriented ones, while mining growth is hopefully not stymied by environmental concerns. On a global basis, the mining sector will be robust with RP catering to the mineral needs of China, India, Japan and Korea.

The year 2006 is a tough year ahead. Political developments could sideline economic reforms and put a break on growth momentum. The peso's continued strength could pull down growth way below government targets. On the other hand, it has reduced foreign debts with its falling borrowing costs and spreads.

I M A G E S

DBP in 2005: THE YEAR IN REVIEW

The state of affairs in 2005 was obviously anything but perfect in general. Good thing, DBP's optimism prevailed over challenging developments on the world and local stage.

Against a backdrop of economic, political and social uncertainties, the Bank never lost sight of its mission. Imbued with resiliency, it turned challenges into opportunities to persevere in what it has set out to achieve for the nation and to continue with its task of making life better for every Filipino.

A look at the past year, in fact, reveals that DBP continued to cover a lot of ground in its mandate of influencing and accelerating sustainable economic growth for the continued well-being of the Filipino people. This, certainly, augurs well for 2006.

- The Bank ventured into an unsecured lower Tier 2 subordinated notes offering of up to P10 billion to strengthen its capital base in view of an improving investor appetite, marking the first time a government financial institution (GFI) is issuing capital notes.

- A P137-million term loan was extended to Calapan Waterworks Corporation to finance the rehabilitation and expansion of its existing water distribution system in Calapan City. The project marks DBP's first partnership initiative with a private firm in the area of local water utilities. It is expected to provide better access to safe and clean water for the residents of Calapan City and complements efforts to improve its basic utilities in line with its development as a prime destination in Southern Luzon.

- DBP tapped a US$10 million-fund from the AB Svensk Exportkredit (SEK) through the Swedish International Development Cooperation Agency, which will be made available to finance environmental investments under the Credit Facility for Environmental Management Project.

- The government's energy audit team gave the Bank a five-star rating with a corresponding grade of 90% for complying with the national government's energy conservation directive.

- The Japan Bank for International Cooperation conferred on DBP an overall rating of 'A' for its successful implementation of the Yen 5.158 Billion Environmental Infrastructure Support Credit Program (EISCP) 1. The rating was based on the relevance, efficiency, effectiveness, impact, and sustainability of environmental projects and investments financed under the EISCP I.

- The Social Security System once again named DBP the 2005 Best Participating Financial Institution for Social Development Loans in recognition of its support to the SSS Financing Program for Educational Institutions. This achievement marks the Bank's eighth citation under the Balikat ng Bayan Awards, making it the most awarded partner of the SSS.

IMAGES

- DBP, together with the Philippine National Bank and Allied Banking Corporation, participated in the P1.5 billion syndicated committed credit line/ term loan to the Bases Conversion Development Authority to partially finance its counterpart fund for the Subic-Clark-Tarlac Expressway Project (SCTEP). The SCTEP is among the infrastructure projects identified in President Arroyo's ten-point agenda, as well as in the Medium-Term Philippine Development Plan that is expected to develop Clark and Subic as centers of excellence in international service and logistics in the entire Southeast Asian Region.

- DBP was one of the joint issue managers and lead underwriters for the five-year Pag-IBIG Housing Bonds which exceeded the original P5-billion issuance. Owing to high market demand, the bond offering was 2.2 times oversubscribed as total volume awarded by the Home Development Mutual Fund reached P7 billion. Proceeds of the bond offering are intended to finance the various housing programs of the Pag-IBIG Fund.

- The P62.5-million DBP-OWWA Credit Program for Overseas Filipino Workers (OFWs) was established to provide non-collateral credit assistance to ready to leave members of the Overseas Workers Welfare Administration and their eligible dependents to tide them over during emergency situations.

- The Bank and the Rizal Commercial Banking Corporation (RCBC) signed a P3-billion loan agreement to assist North Triangle Depot Commercial Corporation in the development of an integrated retail center located at North Triangle along EDSA, Quezon City. The project reflects DBP's continuing efforts to build the infrastructure to further encourage community development.

- In furtherance of its sustainable development advocacy, DBP launched in April the DBP Forest Program to support and encourage the reforestation of open and denuded areas through the planting of relatively high value fruit trees and other useful plant species. With an initial seed fund of P50 million from the KfW of Germany, the Program is envisioned to contribute to the protection of coastal areas and the conservation of soil and water in the uplands, while improving spawning grounds for terrestrial and marine aquatic life. In the long run, it also aims to help in the development of downstream industries in the countryside. As of December 2005, 17 forest projects have already been launched in identified areas in Bataan,

DBP in 2005: THE YEAR IN REVIEW

Sarangani, Davao City, Bukidnon, Palawan, Cagayan, Quezon, Guimaras and Iloilo.

- DBP with Banco de Oro participated in the P600-million syndicated term loan to finance the Leyte-Cebu Interconnection Uprating Project, a major power project aimed at sustaining the reliability and stability of electricity supply in the Visayas. The project, which marks another partnership initiative to fast track the country's geothermal power industry, is one of several initiatives under the Visayas Transmission Augmentation Program that is envisioned to provide medium- and long-term solutions to the looming power crisis in the area.

- A P110-million credit support was extended to the local government of Mandaue for its solid waste management system. The project envisions a modern, durable and multi-sized container system to enable the City to achieve a more efficient waste collection system that would complement the national government's efforts to address problems related to solid waste management and disposal.

- The Sustainable Partnership for Energizing Entrepreneurship Development (SPEED) Program was launched to encourage the growth and development of micro, small and medium enterprises. Beyond financing, the SPEED Program represents DBP's consistent thrust to extend assistance to mSMEs in a more integrated and complete way. Business Assistance Centers (BACs) were established under the Program to provide Filipino entrepreneurs with convenient and efficient access to market information, technology research and development, and credit and technical assistance. Seven BACs are now fully operational in Benguet State University, Mariano Marcos State University, Pampanga Agricultural College, Camarines Sur State Agricultural College, Aklan State University, Central Philippine University, and Foundation University. Funding support was also extended to jumpstart the operations of BAC hosted by the Palawan State University.

- DBP retained its ISO 14001 certification for its continuing commitment and efforts to sustain the implementation of its environmental management system (EMS) in all areas of its banking, lending and investment operations. In December, an upgrade audit was conducted by AJA Registrars Limited to assess the conformance of the Bank's EMS to the new requirements of the 2004 version of this international standard. A new certificate will soon be issued to DBP by AJA attesting to its compliance under ISO14001:2004.

Review

DBP classifies its financing initiatives into four priority development programs. These are: environment, social services, infrastructure and logistics, and MSMEs (Micro, Small and Medium Enterprises).

# of Operations

A review of the Bank's annual operations always underscores the fact that financing development is a unique mandate. Each year provides new insights on how management has addressed its twin goals of profitability as a bank and relevance as a development institution. The thread of continuity over the years has been how the DBP has attained a delicate balance between these two opposing pursuits, moreover, how one complemented the other, in the achievement of the Bank's development mission.

Since the last quarter of 2004, the Bank has been utilizing the built-in strengths of its balance sheets more effectively. As a result, the Treasury under Financial Markets Sector, a new sector under the refined organization, significantly increased its revenue generation in 2005. Treasury introduced new products intended to maximize income possibilities from financial market developments here and abroad. It was clearly in management's mind that these income windfalls could fund the new scope products, particularly those in the remittance business and microfinance.

PROGRAM DEVELOPMENT

At the core of DBP's role in financing development is program lending. It starts with an appreciation of the national government's thrusts and private sector initiatives. Such appreciation primes the program development activity that entails the design of the appropriate financing packages. What follows is the fund sourcing efforts that require touching base with multilateral and bilateral fund sources. Then it is the task of the Bank's delivery system to ensure that the program facilities reach their intended beneficiaries.

DBP classifies its financing initiatives into four priority development programs. These are: environment, social services, infrastructure and logistics, and MSMEs (Micro, Small and Medium Enterprises). Credit facilities and technical grants sourced from official development assistance (ODA) funds support these priority development programs. Program Development (PD) Sector formulates the funding programs through its three departments. PD I handles environment and social services programs, and PD II carries infrastructure and logistics and MSMEs. These departments are the program champions that provide technical assistance to the marketing units. The third department, Fund Sourcing mobilizes funding facilities in support of the programs to be moved by the Bank's delivery system.

Environmental Development Programs

DBP's environmental programs do not merely form part of its business mandate. They are integral to the Bank's way of doing business as an ISO 14001-certified institution. Integrating environmental considerations in its lending programs is one of the basic principles of the Bank's Environmental Management System that has been in place since 2002 and re-certified in 2005.

1. **DBP Forest Program**. This program aims to expand the efforts in conserving and protecting the environment while stimulating rural productivity. It was initially funded with P50 million seed money from KfW, and continuously built up from front-end fees on big-ticket loans. DBP's direct contribution to the Program, on the other hand, reached almost P68.5 million as of year-end 2005 covering a total of 17 re-greening projects nationwide with a total area

of more than 3,900 hectares. These projects were implemented with local government units (LGUs), state universities and colleges (SUCs) and people's organizations (POs) as partners. Department of Environment and Natural Resources, Department of Agriculture, and Department of Science and Technology also provided the needed support.

2. **Clean Development Mechanism (CDM)**. The Bank put in place the Greenhouse Gas Emission Reduction Program to identify greenhouse gases emitted from the Bank's lending activities, calculate the emissions and target their reduction. DBP established carbon market links with investors/ buyers from Japan, Singapore, United Kingdom, as well as with various CDM consultants. The Climate Change Program and Financing Option for CDM projects were presented in Hongkong, Bangkok, Malaysia and Jakarta as well as in local seminars and briefings, thus generating interest in CDM.

3. **Rural Power Project (RPP)**. This World Bank-funded program, with total of US$150 million over a 14-year period, aims to raise electrification in the countryside from the estimated present level of 80% to 90%. The first of four RPP-Adaptable Program Loans (APLs), APL I of P530 million, has been fully committed to seven accounts. Negotiations with National Transmission Company for DBP to finance the purchase of Transco's sub-transmission assets by electric cooperatives have been concluded. In anticipation of subsequent APLs, PD I conducted training seminars on renewable energy projects for officers and staff of the DBP marketing units.

4. **Solid and Hazardous Waste Management**. Five projects amounting to P167 million were approved under the KfW – Credit Line for Solid Waste Management. The facility financed the construction of material recovery facility, purchase of collection and transport equipment, and acquisition of heavy equipment for the construction and operation of sanitary landfill. Another 29 projects amounting to about P1.4 billion were in the pipeline. PD I also briefed 43 provinces, cities and municipalities on solid waste management, and initiated research studies on ethanol and coco methyl ester.

5. **Pollution Prevention & Control**. Loans released to 17 projects reached P2.8 billion, funded under the JBIC Environmental Infrastructure Support Credit Program (EISCP) and the KfW Industrial Pollution Control Loan Program (IPCLP). PD I and the Area Management Offices also provided assistance and inputs to the JBIC Pre-Appraisal Mission for the crafting of the Environment Development Program.

6. **Water Resources**. World Bank-funded LGU Urban Water and Sanitation Program aims to provide potable and sustainable water supply throughout the country in line with the Administration's Ten-Point Legacy Agenda. Loan approvals reached an estimated P2.5 billion, with releases totaling P113 million as of year-end with bulk of the loans approved projected to be released during the first quarter of 2006. PD I, in partnership with the Department of Interior and Local Government (DILG) and the Municipal Development Fund Office (MDFO) of the Department of Finance also conducted capacity-building workshops in Baguio City for Luzon LGUs, and in Cagayan de Oro City for Visayas and Mindanao LGUs.

Social Services Development Programs

This priority area covers education, healthcare and community development among others. Because this priority area includes the public services devolved to LGUs by the Local Government Code, DBP finds itself working very closely with them, and with other stakeholders in local development. Most of the social services programs concern the development of human capital. Oftentimes, this priority area intersects with environmental development programs since a number of projects under the latter are also necessary services to community development.

1. **OWWA Credit Program**. In 2005, DBP strengthened its funding support for the overseas Filipino workers (OFWs) through its Overseas Workers Welfare Administration (OWWA) Credit Program. An initial funding of P62.5 million was set up for the program that caters to the financing

needs of OFWs. The program addresses two categories of financing requirements of the OFW. One is his pre-departure needs such as placement/processing fees, and the other is for subsistence allowance or assistance to his family members during emergency situations.

2. **Housing Program**. The Bank initiated a review of the ADB-funded Development of Poor Urban Community Sector Project (DPUCSP). The review addressed the need to streamline the requirements and transaction flows of DPUCSP. With the streamlining, the banks were able to give a fresh push in marketing the housing program cum livelihood to the urban poor communities in coordination with LGUs.

3. **Health and Education Programs**. In 2005, PD I undertook three initiatives in these areas to enhance these programs. One is the coordinative role it assumed in the study for the creation of a nationwide health program. It also developed qualification standards for state universities and colleges, and surveyed the investment requirements of educational institutions, hospitals and LGUs. The marketing units endorsed to PD I for technical evaluation 21 schools availing a total of P232 million loans, and four healthcare projects for P171 million.

Infrastructure & Logistics

DBP has been carving out a name in its initiatives at supplementing the national government's efforts in addressing the country's infrastructure requirements. It came at a time when ballooning debt service significantly curtailed the national budget for infrastructure outlays. More than just supporting infrastructure projects, DBP formulated a development rationale through its Sustainable Logistics Development Program (SLDP). Railroads, airports and expressways are lodged under this priority program, so too are utilities, transportation and communications.

A major component of the SLDP is the Road-RORO Terminal System (RRTS). RRTS links up the islands comprising the Philippine archipelago, by roll-on, roll-off (RORO) ships. DBP created this project from studies made proving that significant losses and costs are incurred from handling and transfers along transport routes. RRTS reduced these losses and, in addition, required LGUs to provide the terminal facilities. The strategic importance of RRTS led to its adoption as the Strong Republic Nautical Highway.

In 2005, the Central Nautical Highway took shape, a third alternative in addition to the Eastern and Western nautical highways. This route traverses the provinces of Quezon, Sorsogon, Masbate and Cebu. DBP is also encouraging shorter island link-ups that crisscross these three parallel main highways. DBP approved P210 million RRTS projects in 2005.

The other two components of SLDP are the Grains Highway and the Cold Chain. The Grains Highway includes the network of post-harvest facilities mainly for rice and corn, bulk storage and loading facilities. The Cold Chain, on the other hand, provides specialized facilities to maintain the freshness, and therefore, the quality and value of perishable goods like fruits, vegetables and meat products. In 2005, DBP approved P297 million for the Grains Highway and another P310 million for the Cold Chain.

Micro, Small & Medium Enterprises (MSMEs)

With MSMEs playing a vital role in the Ten-Point Legacy Agenda of the Administration, DBP has continuously been searching for ways to be involved in very meaningful ways. The MSME as a priority development program poses the greatest challenge to DBP. Both the Bank's infrastructure and business economics are no longer well-suited for MSME financing. In 2005, it gained some headway in responding to this challenge.

DBP created a Microfinance Department under its wholesale operations. This entailed dedicated resources and personnel and more relevant accreditation process and criteria for the participation of smaller financial institutions. Prior to this, DBP's wholesale banking technology catered only to the biggest banks in the country. At the close of the year, DBP began to undertake initiatives towards a vertical organization for microfinance in the Bank.

As signatory to the memorandum of understanding that gave rise to the SME Unified Lending Opportunity for National Growth (SULONG), DBP pursued SME loans through the branches and its Factoring Department. For the year, it released a total of P10.5 billion to SMEs, not counting the credit lines approved for SB Corporation and for People's Credit and Finance Corporation in the total amount of P465 million.

To benefit the SMEs, DBP launched the Sustainable Partnership for Energizing Entrepreneurship Development (SPEED) Program in 2005. Under SPEED, DBP set up an initial seven Business Assistance Centers (BACs) in Luzon and the Visayas. Four more are under process to cover Mindanao, Cebu and Palawan.

As with its other programs, DBP collaborated with other stakeholders in setting up the BACs. Among its partners are the state/private universities and colleges who, through their e-business centers, provide the BAC with an office and officer-in-charge. DTI and DOST provide business counselors and technology assistance. In certain areas, the BACs count on outreach programs of MASICAP Foundation to touch base with entrepreneurs, and on participating financial and microfinance institutions to serve as financing conduits. To put the players of the BAC together, DBP provides the initial seed operating capital, promotes SPEED, and brings into the equation the assemblers and consolidators of the supply chains made up of small businessmen and farmers.

DBP's Factoring Facility gained substantial scale in 2005. This facility for SMEs doing supply business with "Big Brother" corporations topped its 2004 performance by over 60% in all benchmarks, including accounts receivable purchased, releases, collections and income. Factoring Department also conducted roadshows to invite more participants to the program, and held a Factoring Forum to disseminate the lessons and improvements among the Bank's officers and support units. It organized a Factoring Summit attended by about 70 clients to get their views on how to further improve the Bank's factoring service.

Fund Sourcing

DBP, through Fund Sourcing, developed new and strengthened existing partnerships with European agencies. These efforts resulted in the conclusion of Euro 25 million from the European Investment Bank (EIB), and US$10 million from the Swedish International Development Authority (SIDA). The EIB facility covers a wide scope of qualified projects to include power, commercial and social infrastructure, agro-industry, transportation, environment and tourism. The SIDA facility, on the other hand, is dedicated to environmental projects. The third tranche of the Credit Line for Micro, Small & Medium Enterprises (CMSME) of US$5.3 million from KfW became available in 2005 to support local government units (LGUs) and microfinance institutions (MFIs). Altogether, the fresh funds from these three facilities for developmental loans of private and public sector projects amounted to P2.4 billion.

DELIVERY SYSTEM

The search for a more responsive delivery system of the Bank's products and services is the primary reason for continuing organizational refinements. There really is no long-lasting equilibrium in the Bank's organization because the balance between profitability and relevance objectives of DBP is constantly changing. Significant organizational adjustments were made in 2005 to make the Bank more responsive to market opportunities and the developmental thrusts of the national government.

Organizational Strengthening

Starting April 2005, the Bank pushed a continuing organizational refinement. It was prompted in part by the on-going early retirement programs, ERIP IV and the new ERIP V availed of by a number of senior officers and staff. But the larger consideration

was the need to be responsive to the Bank's target markets and the pursuit of its development mandate.

The Board approved the first phase of a function-based organizational refinement that aligned DBP to the marketplace on April 20, 2005. One of the key changes was the creation of the position of the Chief Finance Officer to head the Financial Markets Sector and spearhead the strengthening of treasury, institutional relationships and remittance center operations. This led to the creation of two major units. One is the Financial Institutions to enhance wholesale banking to cover as well the wider area of correspondent banking. The other is the Remittance Center, a proactive move to bid for greater involvement in the welfare of OFWs.

Program Development Sector gained more focus from the organizational adjustments; its marketing functions were transferred to either Marketing Head Office Sector or Marketing Branches Sector. The refinements also embodied the matrix system, an internal structure that emphasizes collaboration, and places operating personnel under more than one leader in appreciation of specialized capabilities in the Bank, e.g., banking relationships of branches and technical expertise of program development.

The second phase of organizational strengthening took place in December 2005, after the completion of the 2006 budget hearings. This made sure that all the key result areas of the Bank are addressed in terms of logistics and personnel. The various sectors of the Bank streamlined further to promote efficiency and responsiveness.

Corporate and Investment Banking

Marketing Head Office Sector (MHS) posted strong performance records in 2005. Its loan portfolio rose to P23.8 billion for a 76% growth over the previous year. Intensified marketing efforts, particularly in the priority areas, resulted in a significant build-up of pipeline projects. Loan approvals hit P37.8 billion and loan releases P46.6 billion, both registering impressive growth marks of 125% and 206%, respectively, over comparable 2004 figures. MHS continued its lending activities to existing clients belonging to the country's top 1000 corporations and pursued projects with development impact. It also focused on activities that maintained the soundness of its existing portfolio, and exerted extra efforts in assisting clients affected by the slowdown of the economy. Among its 2005 highlights are the following:

1. Participated in the P8 billion Long Term Notes for National Food Authority in the pursuit of food security, price stabilization, and access to affordable rice by the poorest of the poor.

2. Participated in National Transmission Corporation's Leyte-Cebu Interconnection Uprating Project designed to avert a looming power crisis in the Visayas area caused mainly by transmission congestion. The project promotes the use of "clean electricity" generated by the geothermal plants in Leyte, dispensing the over-reliance on fossil-fueled power generators of Cebu-based plants that have been run to capacity.

3. Along with other banks, participated in the P5.0 billion Syndicated Term Loan arranged for Globe Telecom, Inc. to finance its "Phase 10" Expansion Projects. These projects installed additional cell sites in both rural and urban areas either previously unserved or where capacity was already inadequate, thereby providing a vital factor in spurring regional development.

4. Partially funded the construction of the 14-storey School of Design & Arts (SDA) of the De La Salle College of St. Benilde. The SDA building features specialized rooms and laboratories, a 500-seat theater, a museum, and other amenities and facilities in design and arts.

5. Investment Banking (InB) acted as coordinating arranger and underwriter to Nutri-Asia Pacific Limited for US$215 million Syndicated Bridge Facility for the acquisition of Del Monte Pacific Ltd.

6. Acted as one of the issue managers and one of 18 accredited selling agents in the Republic's 7th Retail Treasury Bond (RTB) offering in August 2005. DBP contributed close to 7% of the P3.1 billion mobilized, with an estimated 45% tapping the targeted retail market.

7. Took the role of joint issue manager and lead underwriter for the Pag-IBIG Housing Bond Flotation. Tenders at the auction reached P11 billion enabling HDMF to exercise a P2 billion greenshoe option on top of the P5.0 billion original issue size.

8. Acted as underwriter in the P140 million Balanghay Bond Float of the City Government of Butuan. Proceeds will be used for the construction of two middle buildings within the proposed D.O. Plaza Regional Center, a one-stop government service hub.

9. With HSBC, acted as arranger in the P3.0 billion loan and note issuance for the North Triangle Depot Commercial Corporation.

10. Through the Factoring Department, purchased P2.9 billion worth of accounts receivable from 61 SME suppliers of 23 big corporate buyers. As a continuing response to the needs of SME suppliers, Factoring presented its facility and invited other big prospects, such as Petron Haulers Association, Ford Philippines, and Manila Water Company, to participate in the program.

11. Asset Management (AM) under MHS carried on the efforts to reduce non-performing assets of the Bank and to maximize capital recovery. AM implemented the work-out solutions for 20 non-performing loans with outstanding balance of P1.6 billion for a 23% reduction of its P7.0 billion NPL portfolio. It also realized 76 sale transactions and four write-offs of acquired asset accounts. AM also began the spadework for the sale of a significant portion of the Bank's NPAs through the SPV mode.

Area Management Offices (AMOs)

Marketing Branches Sector (MBS) has five AMOs that have jurisdiction over 77 branches nationwide. These five AMOs in 15 regional areas where 77 branches are based provide the presence of DBP in the countryside. They accounted for a combined loan portfolio of P17.1 billion or 19.7% of the Bank's total loan portfolio as of 2005. They also generated P30.1 billion in deposits accounting for 59.2% of total. Since they are the relationship managers in their respective areas, they provide the entry point of DBP's products and services. The branch officers and staff are the ones who rub shoulders with other development partners such as the LGU officials, local entrepreneurs and businessmen. It should be no surprise then that illustrative development projects abound in the AMOs.

1. **LGU Loans**. In responding to the financing needs of LGUs, the AMOs dealt with the biggest LGUs such as the City of Manila as well as with the smaller municipalities in Mindanao and Bicol Provinces. Sample LGU projects in 2005 include school facilities like the new campus and buildings of City College of Manila at Mehan Garden and the 15 new school houses for various barangays in the City of Lucena. Two municipalities in Sorsogon accessed DBP's funding facilities for water supply and sanitation. Major and fast growing cities like Mandaue City in Cebu and Iligan City in Lanao del Norte funded their solid waste management systems from DBP. DBP also prodded LGUs, especially those in missionary routes of the Road-RORO Terminal System, to invest in port and terminal facilities. These sample LGU projects have something in common: they all cater to a public need.

2. **Water Districts & Electric Cooperatives**. Local water districts and electric cooperatives are among the clients of the AMO. Both sets of utility providers aimed at improving their service deliveries and efficiencies. Financing to water districts ensured both adequate potable supply as well as sanitation. In 2005, a total of P1.98 billion to four water districts were at various stages of loan release. In the case of electric cooperatives, financing addressed renewable power sources, reduction of systems losses and acquisition of transmission lines from Transco. Bohol Electric Cooperative I harnessed a 2.68 MW mini-hydro power plant, while Antique Electric Cooperative improved the link-up among its three substations.

3. **Private Schools and Hospitals**. Both LGUs and private businesses tapped the branches for funds to support the financing of schools and hospitals. Aside from smaller private technical and vocational centers, the Bank also supported the Davao Medical School Foundation for the completion of a 100-bed tertiary hospital. This facility augments the hospital facilities in Davao City which also caters to its neighboring provinces. The foundation, a consortium of five educational institutions with healthcare related

courses, has its own medical school which will also access the hospital as training facility.

4. **Small Borrowers**. The branches under the AMOs also served as outlets for new services of the Bank. In 2005, six branches were chosen to extend OWWA Credit Program in their locality. Branches in Commonwealth Avenue (NCR), Iloilo City, Cebu City, San Fernando - Pampanga, and San Fernando - La Union, being major areas of origin of OFWs, were tapped to offer the OWWA Credit Program. The combined availments in these branches totaled P31.4 million from 932 OFW borrowers. Another role that the AMOs fulfill is to identify partners in the delivery of service. AMO-Mindanao, for example, facilitated the firming-up of a rediscounting facility for One Network Rural Bank. Some 8,400 public school teachers will benefit from this facility to fund their livelihood projects for supplemental family income. Branches under the five AMOs also catered to the bulk of the Bank's P11.8 billion retail loan portfolio to MSMEs.

Treasury and Financial Institutions

The Bank's organizational refinement in early 2005 formed the Financial Markets Sector to house Treasury, Financial Institutions and Remittance Center. This move was accompanied by strong capability build-up efforts, tapping the available expertise from the private sector. By the 2005 financial results, these management decisions did not only prove correct but also timely given the global market developments and the BSP policy stance. Treasury took the cudgels in building up the Bank's resources and shoring up its income to effectively supplement loans as source of revenues.

Foreign currency-based businesses of the Bank fared exceptionally well in 2005. FCDU resources scaled to a new level of US$589 million, up by 107%, brought about by significant increases in cash assets, interbank loans and investments. FCDU deposits rose 40% to hit $176.7 million from intensive marketing, especially to government entities. Bills payable also registered a 157% rise to $392.5 million. While costs, mainly financial charges and interest expenses also rose, adept investment decisions and bond asset selection boosted trading gain and interest income. FCDU operations produced net income improvements, hitting $8.26 million for 2005.

On the other hand, the newly-created unit under Financial Institutions, Correspondent Banking and Trade Development (CBTD), renewed emphasis on trade business. This resulted in a 470% jump in trade volume to reach $889 million in 2005. The move generated a fee income of P7.5 million, but more importantly, DBP learned how to leverage its correspondent banking business relationships and to harness reciprocity.

Wholesale lending, also handled by Financial Institutions, continued to do its role as a catalyst for sustainable development through its partnership with various financial institutions. Wholesale portfolio inched higher by 3.1% in 2005 to reach a level of P38.9 billion to account for 45% of the Bank's loan portfolio. Our main beneficiary industries were transport, storage and communication for P9.8 billion, followed by construction with P8.3 billion and MSME with P6.7 billion. However, the continuing consolidation among banks and their liquid positions connived to threaten the growth of the wholesale portfolio. For 2005, approvals and releases amounted to P5 billion and P9.4 billion, respectively, 60% and 14.6% lower than the 2004 comparable figures.

Domestic operations of Treasury in 2005 also recorded very credible results. From the P40 billion average investment portfolio in government securities, Treasury earned accrual interest income of P3.3 billion, and further realized gains on trading and sale of securities of P857 million, higher by 47.25% than year ago. Throughout 2005, the Bank complied with regulatory reserves and met the funding needs for operations and investments. Treasury increased placements in BSP's reverse repo averaging P8.4 billion and earning P608 million, both significantly higher than the year ago figures. It also worked on the issuance of the Bank's Tier 2 Capital Notes whose offering period began in December 2005.

FINANCIAL HIGHLIGHTS

As of 2005, DBP climbed two rungs in the country's Top 10 ranking among banks, from No. 9 to No. 7 in asset size. Its net income performance in 2005 was even more impressive, ranking No. 4, after BPI, Metrobank, and Citibank. DBP also set a record high in loan portfolio (net) at P79.3 billion, and in deposits (P50.8 billion), capital (P25.6 billion), gross income (P16.2 billion) and net income (P3.2 billion). All these support the sustainability of DBP.

Record Net Income

The consolidated net income recorded in 2005 is unprecedented. The adoption of the Philippine Financial Reporting Standards (PFRS) did not adversely affect the Bank's profitability. Compared to the preceding year, the net income of P3.2 billion for a 31.6% improvement was quite a feat considering a restrained economic growth in 2005. The Bank maximized marginal income from high cost deposits, indicating Treasury's keen market sense. Aside from raising the deposit level to P50.8 billion, an all-time high, this capability facilitated access to prime clients, thereby opening up more banking opportunities with them.

Other income at P2.8 billion was 14% better than last year. Providing the momentum were the profits from investments and securities trading that posted a 114% increase to P1.9 billion. The gross income of P16.2 billion, or the combined contributions of interest income and other income, was likewise an all-time high, enabling the Bank to absorb higher interest expenses, and to brace for the impact of its early retirement program that runs up to 2008. The efficiency ratio (operating expense over gross income margin) slightly rose to 56% from 55%. That income delivery in 2005 which was also incentive-driven may be argued by the increase in variable pay given out in 2005. Provisions for the early retirement program were also built-up. Operating expenses rose 14% mainly from manpower-related expenses in 2005.

Resource Build-up

A much tamer year-on-year balance sheet growth resulted from the adherence to the Philippine Financial Reporting Standards. Consolidated resource level hit P213 billion for a 3.3% growth in 2005 over comparable, PFRS-adjusted 2004 figures. The fair value measurement of financial assets on trading and available for sale securities, certain derivative instruments and real and other properties owned modified the 2004 financial statements.

These valuation adjustments, however, did not affect the loan portfolio. At P79.3 billion (net of unearned discount and including accrued interest receivable) in 2005 loans rose by 12.6%. This is the biggest annual increase attained since the turn of the millennium. Interbank loans, on the other hand, trebled to P24.7 billion to suggest DBP's much-enhanced correspondent banking and overall relationships with domestic and foreign banks.

Both the heightened activity in Treasury and the nuances of PFRS translated to significant changes in the values of financial assets. The reduction in marketable securities reflected Treasury's strategy, given the interest rate environment, to sell down these investments to realize profits. The money market transactions executed by Treasury translated to an increase in the level of deposits with other banks and interbank loans. Also underpinning the Treasury activities was the growth in deposit liabilities which rose by P14.3 billion or unprecedented growth of 39.3% with growth momentum coming from FCDU deposits.

Measures of Performance

Close to 60% of the Bank's outstanding loan portfolio in 2005 were in developmental projects, with the remaining 40% in commercial loans. The four priority development programs guided marketing work and funding, particularly the ODA funds, to specific priority areas. Infrastructure and logistics had P21.7 billion or 25% of the Bank's loan portfolio, followed by MSME at P18.5 billion or 21.3%, environment had P6 billion for a 6.9% share and social services at P5.2 billion accounted for 6%.

Various financial measures vouch for the strong performance of DBP in 2005. Profitability ratios (non-consolidated) carried the impact of the Bank's scale and scope strategies. Return on equity improved to 14.80% from 12.76% in 2004 or a very material rise of 204 basis points. Return on assets likewise increased but at less impressive rate, improving from 1.55% in 2004 to 1.76%. A salient factor to higher profitability in 2005 was the improvement in asset quality. Past due rate, excluding interbank, improved by 237 basis points, from 11.92% to 9.55%. A greater portion of the loan portfolio yielded interest income and reduced the need to set up additional provisions.

Improved profitability was attained despite hikes in costs. Net interest margin narrowed from 4% to 3.80% in 2005. While this suggests higher cost of funds, what the Bank succeeded to do was turn around a bigger volume even on lower spreads for bigger absolute income results. Manpower related costs also rose, but this was more from higher performance incentives and retirement contributions as the early retirement program of the Bank has been into full swing.

While DBP focused on developmental projects, it never lost sight of the conditions for its sustainability. It pushed both scale and scope strategies to maximize its profitability in support of developmental objectives. Scale factors included the continued volume increases in loans and investments that provided a steady stream of income to the Bank. Scope factors, on the other hand, could be grouped into two types. One catered to new products, mostly Treasury instruments, which resulted in short-term or "windfall" income. Another set of new initiatives addressed the long-term thrusts of DBP as a development bank. The latter scope products entailed investments of longer gestation periods with income streams in the future yet. Among the scope products in 2005 are remittance business, microfinance, and capital notes.

Corporate Governance and Risk Management

The spate of bank closures in the global scene during recent years had changed the behavior of bankers, as well as of their regulators, here and abroad. In the domestic scene, Bangko Sentral ng Pilipinas (BSP) issued a series of circulars to compel greater involvement on the part of the Board of Directors in bank affairs, and to shift capital adequacy determination to the risk-based framework. BSP defined the duties and responsibilities of the Board and required each bank director to attend the special seminar on corporate governance. In line with the capital adequacy measurement, risk management became a focal point for bank transactions and resource build-up.

GOVERNANCE

Adherence to the principles and best practices in corporate governance is a declared commitment of the Development Bank of the Philippines. The Bank acknowledges that the observance of the fundamental principles of fairness, transparency and accountability starts with the Board and serves as guide in the attainment of Bank's goals. For these principles to flourish in the Bank, the Board ensures that a culture of ethics, compliance and social responsibility pervades at all levels of DBP's operations. In this sense, good governance underpins proper risk management.

The Board of Directors

The Board of Directors consists of nine members, all of whom are appointed by the President of the Republic of the Philippines. Their selection factored in the perspective that they give to the Board, so that as a body, the Board is very much multi-faceted.

The Board members of 2005 are proud to possess sterling records in business, finance and banking. They showed genuine concern and expertise in SMEs, NGOs, labor and human resource, political economy, business management, legal and audit. Aside from their unassailable characters, they spoke for all the regions in the country. Mostly hailing from Luzon and Metro Manila, the Visayas and Mindanao, too found voice in the Board.

Board Committees

Bangko Sentral ng Pilipinas ascertained that the Board of Directors of a bank is fully aware that one of its responsibilities is to ensure good governance. DBP strictly conformed to the BSP stipulations on Board concerns, including the creation of several Board committees.

Executive Committee (ExCom). The ExCom is a scale down of the Board. It is composed of only five members including the Chairman and the President/CEO, with the Chief Operating Officer and Chief Legal Counsel as Ex-officio members. In 2005, it addressed the Board agenda of matters that are within its delegated authority in 15 meetings on top of the Board's 32 meetings.

Governance Committee. This committee is comprised of at least five members of the Board who elect a chairman among themselves. The President/CEO and the Chief Operating Officer serve as Ex-officio members. During the year, the committee ensured adherence to the Bank's Manual on Good Governance approved under Board Resolution No. 0445 on December 19, 2003 and the Code of Ethics formalized by Board Resolution No. 0246 on July 07, 2004. It reviewed certain major transactions to aid the Board in the formulation of policies to safeguard the Bank's credit and investment activities. As one of its basic functions, it oversaw the periodic performance evaluation of the Board and its committees.

Audit and Compliance Committee (AuditCom). This committee, made up of three members of the Board, is the overseer of the activities of the Bank's Internal Audit (IA) and Compliance Monitoring Office (CoM). Sitting as Ex-officio members are the President/CEO, the Chief Operating Officer and a representative of the Office of the Legal Counsel. In 2005, the committee reviewed 65 regular and special reports of Internal Audit, a majority of which were credit and operations review of the branches that served to improve risk awareness and proper control procedures. It also delineated the functions of CoM vis-à-vis Internal Audit, Risk Management, Credit Review and Policy Supervision and Office of the Legal Counsel. The Board approved the Updated Manual on the Protection Against Money Laundering on May 25, 2005 and the Revised Compliance Program of the Bank on September 28, 2005.

Committee on Risk Management (CRM). The CRM includes three members of the Board with the President/CEO, the Chief Operating Officer, the Chairman of the Audit and Compliance Committee, the Chairman of the Executive Credit Committee (ExCreCom), and the heads of Internal Audit, Risk Management, Treasury and the Chief Legal Counsel as Ex-officio members. The CRM, through the Risk Management, is principally responsible for the development and oversight of the Bank's Risk Management Program. The membership of CRM resulted from its reconstitution in 2005 to ensure adequate representation and independence. Among the matters it tackled were the Operating Principles of the Bank's Risk Management and Risk Assessment System, the Risk Roadmap towards Basel II Compliance, and the revised charter of the CRM.

Human Resource Committee (HRC). The HRC has at least three members of the Board, with the President/CEO as Ex-Officio member, and is back-staffed by Human Resource Management. In 2005, it met 12 times and formulated over 30 major policy decisions that addressed organizational concerns and employee welfare. Among these were the early retirement programs (ERIP IV – 2nd tranche and ERIP V) and the series of refinements of the Bank's organizational structure. Various improvements on employee benefits and compensation structure were also deliberated upon and decided by the HRC.

RISK MANAGEMENT

The Bank sees risk management as a personal responsibility that is ingrained in the policies, procedures and controls in the discharge of one's functions. Officers of line units have well-defined approving authorities and credit limits.

The Management Committee (ManCom) has an overarching coverage on the more specialized concerns of the other top management committees. Each critical risk area has its own specialized management committee, such as the Executive Credit Committee (ExCreCom) for credit matters and the Assets and Liabilities Committee (ALCO) for investments. They also have support units to provide assistance in transactions review, policy formulation, capability build-up and management information.

For a more structured approach to managing risk, however, the Bank created the Risk Management (RM). RM provides direct assistance to Management and to the Board of Directors. It undertakes risk identification, measurement, monitoring and control to serve as inputs in the oversight function of the Board Committee on Risk Management (CRM) that is also overseeing the development of the Risk Management Program of the Bank.

Management of Credit Risk

Credit risk management is built-in to the operating systems and policies of the Bank. Credit Review and Policy Supervision (CRPS), a specialized support unit, reviews credit transactions, formulates responsive credit policies, promotes a strong credit culture and strengthens the Bank's Credit Risk Management System. All credit proposals go through the ExCreCom where deliberations are enriched by the various disciplines of its members. Approving authorities and credit limits are clearly defined, so that accounts exceeding certain limits go to the Board for approval. Since credit risk is part of the overall risk management concern of the Bank, it is also monitored by RM and forms part of its report to the CRM of the Board.

The Bank has implemented an Internal Credit Risk Rating System (ICRRS) for corporate borrowers with asset size of more than P15 million. It has likewise put in place a pre-approval rating review of accounts. Internal Audit also evaluates all credit transactions as well as the operating procedures and controls of lending.

As a corollary activity, RM strictly monitors the prudential limits set by the BSP. One of these is the Single Borrower's Limit (SBL) applied on the Bank's retail lending operations (25% SBL), as well as on its wholesale lending operations (35% SBL on participating financial institutions). However, the Bank has set more conservative internal limits on retail borrowers as well as on counterparties. RM monitors these limits against exposures and reports to Management and the Board. It is also finalizing more risk-sensitive credit concentration limits than those set by BSP guidelines. There is also a continuing build-up of information towards compliance with the Basel II framework. These include default data gathering and warehousing.

Management of Market and Liquidity Risks

Developments in the financial markets affect the trading and investment positions of the Bank. They pose the market risks faced by the Bank's Treasury operations, in the form of interest rate and price risks, foreign currency risks, and liquidity risks. To address these market risks, the treasury officials make use of technical/analytical tools, provide hedges through swaps and derivatives, and adhere to internal prudential limits set by the Board and those stipulated by the regulatory authority.

Positions in debt instruments, both peso and foreign currency-denominated, and derivatives have set limits based on the Value-at-Risk (VaR) methodology. VaR, using historical simulations, measures maximum potential loss on these positions. Conservative limits are thus guided by the VaR analyses. Other methods serving to ensure investment positions from risks include mark-to-market valuation, sensitivity analysis and stress testing. Aside from keeping positions and transactions within prudential limits, interest rate and foreign currency exchange rate risks, when necessary and feasible, are further hedged through interest rate and currency swaps.

Liquidity risk, or the ability of the Bank to honor maturing obligations and funding commitments, is minimized through the proper matching of fund uses and sources. Basic liquidity provision is addressed by the compliance with BSP's statutory reserve requirement. The Bank also sets maximum limits for pre-determined tenor buckets. To facilitate the setting of these limits separately for FCDU and regular banking units, it makes use of the Liquidity Gap and Maximum Cumulative Outflow (MCO) analysis. RM also monitors adherence to the MCO limits. Off balance sheet risk items are duly accounted for in the preparation of MCO and Capital Adequacy Ratio computations (CAR).

The Bank's positions in derivative instruments are strictly in accordance with BSP Circular Nos. 466, 468 and 469 (series of 2005), respectively. While DBP does not have an expanded derivative authority to invest, it observes the above BSP guidelines in terms of specific approvals, qualified parties and transactions, and risk weights.

Management of Operational Risk

The primary means to control operational risk is to have an effective system of internal control. Under this guiding principle, clear lines of management responsibility, accountability and reporting have been duly considered in the approving authorities. Conflicts of interest are avoided by separation of responsibilities and reporting lines between risk control functions (middle office), business lines (front office) and support functions (back office). Operating and product manuals include control processes and procedures. Dual control is observed over all transactions and items of value. Compliance checks, verification and reconciliation of transactions are regularly conducted. The Bank has a Business Disaster Recovery Plan in place, including an automated retrieval system for actual operational loss data requirement.

In 2005, RM started tracking the requirements of Basel II and best practices in the area of operational risks. It undertook three initiatives to address operational risks, namely: product manuals, documentation of operational losses, and the red flag reporting system to ensure the effectiveness of internal control systems. The re-issuance of DBP Circular No. 24, dated July 15, 2005, institutionalized the preparation of product manuals. It covered existing and new products and services to ensure that inherent risks in all products, services, transactions, processes and systems are identified and assessed for purposes of mitigating or controlling such risks. The manuals also serve as reference for process improvements and documentation of risk systems.

The build-up of bankwide historical data on operational losses is a preliminary stage to more sophisticated risk assessment methods. Its preparation and consolidation shall subsequently be automated. This monitoring tool for assessing risk exposures aims to modify internal policies and procedures, and design controls and contingency plans for risk mitigation. Once the Bank can develop a more advanced internal model for operational risk assessment, it can free more capital for enhancing its business.

Assessment of the Bank's current financial condition is facilitated through the set up of a red flag reporting system. This integrates in the assessment of the Bank's performance an early warning or alert system to pinpoint possible risk compromises. Some of the indicators used in the red flag reporting system are the budget variance analysis and marked deviations from industry benchmarks.

Culture of Risk Awareness

Management has been inculcating a risk awareness culture in the Bank. This is the best mode for actualizing the risk management roadmap along the framework charted in Basel II and pursued by the BSP. In view of this objective, the various support units were likewise geared at enhancing an enterprise-wide risk awareness program, aside from just the primary risk-takers.

Support units promoted the risk management objectives in their respective support roles. Human Resource Management facilitated the training programs designed to strengthen the skills and capabilities of employees in various critical areas of bank operations, such as loan documentation, signature verification and counterfeit detection, credit appraisal and review, among others. The Office of the Legal Counsel provided the technical resource in many of these seminars and facilitated access to the Legal Library through the intranet portal. More direct interventions characterized the activities of Risk Management, Credit Review and Policy Supervision, Compliance Office and Internal Audit. Accounting, Systems and Methods, and Corplan, Budget and Special Projects also made adjustments in the support activities.

The Global Compact

and DBP's CORPORATE SOCIAL RESPONSIBILITY

As a signatory to the United Nations Global Compact since 2002, DBP sustained the implementation of its corporate citizenship program in active advocacy of the ten universal principles spanning Human Rights, Labor, Environment and Anti-Corruption. This section presents the significant advances made by the Bank in this global campaign for corporate social responsibility. This Communication on Progress highlights DBP's own contributions to enabling the Global Compact mission and principles gain a foothold among businesses amid the challenges of globalization.

Human Rights

DBP's human rights initiatives encompass equality, life and security, and economic, social and cultural freedoms as basic premises. The Bank's program of assistance in this area involves activities that address the identified needs of specific target beneficiaries which include victims of calamities, abandoned elderly, orphaned children, the sick, indigenous peoples, and other marginalized groups.

Complementing efforts to enable identified beneficiaries gain adequate access to basic needs and services such as health and medical care, food, and education, while at the same time safeguarding their basic rights, the Bank's program of assistance in 2005 was carried out in partnership with concerned government and non-government organizations and other relevant agencies and institutions.

In response to the calamity caused by typhoons "Yoyong" and "Winnie" that hit the country towards the end of 2004, DBP launched an integrated relief and rehabilitation program for affected areas in the provinces of Nueva Ecija and Quezon. Led by the Bank's key officials, on-site relief assistance was immediately extended to affected families through the then regional management offices in Southern Tagalog and Central Luzon. Rehabilitation efforts, on the other hand, involved support for identified livelihood activities and projects. Volunteer groups were also involved in post-calamity missions designed to rebuild and restore normal activities in affected communities.

In October 2005, DBP participated in relief efforts for victims of typhoon "Labuyo" in Libon and Oas in Albay. The Bank turned over relief assistance to the local government of these towns that included sacks of rice, medicines, canned goods, and other basic necessities for distribution to affected families.

The Bank's Share-a-Gift outreach mission in December, on the other hand, benefited 100 Alangan-Mangyan families in Sitio Banilad, Oriental Mindoro. DBP conducted a medical mission, feeding project, and gift-giving activity. Cash donations were likewise turned over to the local chieftain to support the community livelihood project.

The Bank was also among the first government agencies to respond to the call for relief assistance when mudslides severely hit Guinsaugon, Southern Leyte and neighboring towns in February 2006. The disaster claimed hundreds of lives and caused millions of losses in damaged properties and livelihood. The Bank is also currently mapping out its support strategy for rehabilitation efforts, particularly in the area of educational assistance.

Integrating thrusts cognizant of the economic, social and cultural right indispensable to human dignity, DBP organized in the second half of 2005 a roundtable discussion on the proposed Free and Prior Informed Consent Guidelines of the Indigenous Peoples Rights Act. It provided a venue to assess the guidelines in response to new operational policies issued by the World Bank, which underscore the need for poverty reduction and sustainable development efforts that fully respect the dignity, human rights, economies, and cultures of indigenous peoples.

Labor

DBP's corporate philosophy is anchored on the basic principle of respect for each person. All human resource policies and decisions, therefore, promote concern for the employee and his welfare, his family, and life outside of DBP.

As a government institution, DBP's human resource policies are strictly guided by civil service rules and regulations being enforced by the Civil Service Commission (CSC), the central personnel agency of the Philippine government.

To motivate its employees towards continually improving performance, DBP continued to provide adequate compensation and other benefits that enable employees to meet the basic economic needs of their families. A system of rewards and accountabilities was sustained to encourage service excellence and high standards of work performance.

Several mechanisms were also put in place to ensure that the institution was able to keep up with prevailing industry practices and acceptable benchmarks governing human resource management and relations.

In 2004, the Bank, represented by a Management panel composed of selected key officers, and the DBP Employees Union (DBPEU) entered into a three-year collective negotiation agreement (CNA). This landmark agreement – the first in DBP's 59-year history – was founded on Management and the employees' shared goal of achieving and maintaining industrial peace in the Bank. The CNA is set to expire in January 2007.

In addition to the DBPEU, two other employee organizations – the Association of DBP Career Officers (ADCO) and the Association of DBP Junior Officers (ADJO) – exist in the Bank. The presence of these groups attests to the Bank's continued adherence to an institutionalized system of employee communication that helps maintain a healthy dialogue between management and the staff, promote direct resolution of employee-related concerns in an atmosphere of mutual trust, sustain a culture of trust, and keep employees abreast of developments on the Bank's operations and work environment.

Reflective of its continued emphasis on the provision of training to develop the appropriate skills and technical competencies, the Bank has allocated a bigger training budget for 2006. Fifty-two percent of the budget has been earmarked for technical and skills-oriented training activities to be disbursed by the respective operating units. The remaining 48% of the budget, which is lodged with Human Resource Management, has been set aside for focused officer training program and management development program for senior officers.

In addition to these institution-directed efforts, DBP also continued to encourage compliance to acceptable labor practices among businesses. The Bank has incorporated safeguards in its qualification standards to ensure that prospective borrowers and projects also comply with applicable labor laws and regulations.

Environment

DBP holds the distinction of being the first Philippine bank to be ISO 14001-certified since 2002 for its successful establishment and implementation of an Environmental Management System (EMS). Its sustained compliance to this international environmental standard in all aspects of its business operations and decisions was re-affirmed by AJA Registrars following a full EMS audit in December 2005.

Taking its environmental advocacy a step further, the Bank launched in April 2005 the DBP Forest Program to support and encourage the reforestation of open and denuded areas through the planting of relatively high value fruit trees and other useful plant species. The Program was launched in response to the government's call to preserve the environment and to step up reforestation efforts in light of the calamities that struck Nueva Ecija and Quezon Province in 2004.

With an initial seed fund of P50 million from KfW of Germany, the Program was initiated to contribute to the protection of coastal areas and the conservation of soil and water in the uplands,

while improving spawning grounds for terrestrial and marine aquatic life. In the long run, it is also envisioned to help in the development of downstream industries in the countryside. These projects are expected to benefit a total of 2,500 poor families from partner-peoples' organizations (POs) through increased livelihood opportunities.

The Bank's environmental lending programs, meanwhile, provided assistance to various sectors amounting to P3 Billion in 2005. This supported projects in pollution control, cleaner production, solid waste management, water supply, renewable energy and alternative clean fuel.

Preliminary studies were undertaken with respect to the full commercialization of bio-ethanol and Coco Methyl Ester projects. There are two projects which are under evaluation.

To further influence industries to observe environmental responsibility in their operations, DBP also undertook the publication of sectoral guidebooks and manuals for target industries like hospitals, furniture, textile, transport, plastics, hotels and resorts, and SMEs. An Environmental Performance Monitoring (EPM) was also institutionalized as a tool for managing environmental risks to evaluate borrowers' compliance with environmental requirements.

As a signatory to the global Carbon Disclosure Project, DBP sustained efforts towards the continued improvement of its Climate Change Program.

Another project-in-progress being developed with several partners is the Environmental Portal, a web-based system that provides easily accessible information on the environment. The Portal, better known as "one-environment.ph" started as a partnership venture between the DENR and the DBP. The Portal seeks to provide relevant information that will help guide the business and industry comply with regulatory requirements and conform to standards.

Anti-Corruption

An institutionalized corporate culture of excellence that emphasizes a firm adherence to positive values, commitment to high standards of productivity and competence, and a deep spirit of service to the Bank as an institution, its clientele, and to the economy forms DBP's first line of defense against corruption. It promoted a culture of excellence through strong corporate values, proactive talent acquisition and retention strategies, relevant training and leadership program, and an effective performance management system aligned with the Bank's thrusts.

As a sustaining activity under its corporate culture program, officers and employees regularly gather during the Monday forum to share their reflections on weekly themes that espouse the four pillars of the DBP corporate culture. These are: Integrity, Competence, Teamwork and Professionalism.

To promote enterprise-wide risk management, the Bank's human resource management collaborated with various institutions in updating and strengthening personnel skills on Loan Documentation, Examination of Questioned Documents, Signature Verification and Counterfeit Money Detection, Credit Review, International Financial Reporting Standards and Credit Appraisal.

DBP also continued to enforce strict compliance with relevant laws and regulations such as the procurement of contracts for goods and services as stipulated under RA No. 9184.

The Manual on Code of Ethics guides the office behavior of employees. It has been disseminated to all Bank units in pamphlet form, and is integrated in the Personnel Manual which is accessible to all employees through the Intranet. The Code underscores the duties and obligations of DBP to its various stakeholders. It also stipulates the duties and obligations of officers and employees to DBP, and sets the standards of behavior and performance, particularly on confidentiality and conflict of interest.

Complementing the Code as basis for discipline in the Bank are the Uniform Rules on Administrative Cases and the Grievance Machinery. The former defines the process whereby erring officers and staff are complained against, charged, investigated, heard and disciplined. The latter addresses employee dissatisfaction, by providing the mechanism for expeditious resolution of employee complaint at all times and at the lowest level possible in the organization. These avenues to complain and be complained against strengthen the fight against anomalies, including corruption.

Republic of the Philippines
COMMISSION ON AUDIT
Corporate Government Sector
Cluster I - Financial A

The Board of Directors
Development Bank of the Philippines
Sen. Gil J. Puyat Avenue cor. Makati Avenue
Makati City

We have audited the accompanying consolidated statement of condition of Development Bank of the Philippines and its subsidiaries referred to as "the Group" as of December 31, 2005 and the related consolidated statements of income, changes in capital funds and cash flows for the year then ended. These financial statements are the responsibility of Management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted state auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. 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 audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Group as of December 31, 2005 and the results of its operations and its cash flows for the year then ended, in conformity with generally accepted state accounting principles in the Philippines.

COMMISSION ON AUDIT

DIVINIA M. ALAGON
Director III
Officer-in-Charge

August 31, 2006

Statements of Condition

As of December 31, 2005
(With comparative figures for 2004, as restated)
(In thousands of pesos)

		Group		Parent	
	Notes	2005	2004	2005	2004
Resources					
Cash and other cash items	2,4,5,6,7	P 694,137	P 740,878	P 694,106	P 740,848
Due from Bangko Sentral ng Pilipinas	2,4,5,6,7,8	3,266,702	1,684,088	3,266,702	1,684,088
Due from other banks	2,4,5,6,7	7,900,222	1,024,259	7,895,153	1,002,174
Interbank loans receivable	2,4,5,6,7,9	24,739,800	7,771,557	24,739,800	7,771,557
Financial assets at fair value through profit or loss	2,3,4,5,6,10	3,686,242	1,116,330	3,686,242	1,116,330
Financial assets available for sale - net	2,3,4,5,6,11,14	34,025,898	38,837,918	34,000,681	38,834,901
Financial assets held to maturity - net	2,3,4,5,6,12,14	22,640,526	23,556,771	22,640,526	23,547,489
Loans and receivables - net	2,3,4,5,6,13,14,27	79,309,556	70,459,283	79,309,556	70,459,283
Bank premises, furniture, fixtures and equipment - net	2,3,5,6,14,15	962,865	976,778	940,114	971,888
Equity investment in subsidiaries - net	2,4,5,6,16	0	0	38,750	3,750
Equity investment in associates - net	2,4,5,6,14,17	121,399	151,740	121,399	151,740
Equity investment in joint venture	2,4,5,18	16,000	16,000	0	0
Non-current assets held for sale - net	2,3,5,6,14	3,951,589	4,430,343	3,951,589	4,430,343
Accounts receivable-NG foreign exchange differential	2,5,6	21,278,309	46,567,078	21,278,309	46,567,078
Other assets - net	2,3,4,5,6,14,19	10,363,723	8,822,291	10,325,886	8,796,093
		P 212,956,968	**P 206,155,314**	**P 212,888,813**	**P 206,077,562**
Liabilities and capital funds					
Liabilities					
Current maturities of long-term borrowings	2,5,6,20	P 38,898,052	P 23,938,733	P 38,896,341	P 23,938,733
Deposits liabilities:	5,6,21				
Demand		15,112,385	13,217,235	15,113,490	13,217,851
Savings		25,846,746	15,641,761	25,867,372	15,641,981
Time		9,793,744	7,578,801	9,793,744	7,578,801
		50,752,875	36,437,797	50,774,606	36,438,633
Bills payable	2,5,6,20	91,072,136	117,591,065	91,069,538	117,591,065
Due to Bangko Sentral ng Pilipinas	5,6	70,000	60,000	70,000	60,000
Due to other banks	5,6	33,681	28,441	33,681	28,441
Manager's checks and demand drafts outstanding	5,6	624,280	488,778	624,280	488,778
Accrued taxes, interests and expenses	2,3,5,6	3,405,296	2,824,174	3,400,753	2,824,005
Deferred credits and other liabilities	5,6,22	2,550,638	2,305,225	2,535,646	2,288,769
		187,406,958	**183,674,213**	**187,404,845**	**183,658,424**
Capital funds					
Common stock, P100 par value (Authorized - 350 million shares, issued and outstanding - 125 million shares)	6	12,500,000	12,500,000	12,500,000	12,500,000
Surplus	6	9,152,536	7,709,213	9,110,689	7,670,941
Surplus reserves	6,23	267,021	263,888	247,021	243,888
Net unrealized gains/(losses) on securities	2,6	413,908	(619,903)	414,232	(619,563)
Appraisal increment on property	2,6	0	182,836	0	182,836
Undivided profits	6	3,216,545	2,445,067	3,212,026	2,441,036
		25,550,010	**22,481,101**	**25,483,968**	**22,419,138**
		P 212,956,968	**P 206,155,314**	**P 212,888,813**	**P 206,077,562**

See accompanying Notes to Financial Statements.

Statements of Income

For the year ended December 31, 2005
(With comparative figures for 2004, as restated)
(In thousands of pesos, except per share amounts)

	Notes	Group 2005	Group 2004	Parent 2005	Parent 2004
Interest income on:	2,6				
Loans and receivables		P 6,713,017	P 6,154,939	P 6,713,017	P 6,154,939
Financial assets - debt and equity securities		5,279,781	4,881,911	5,279,781	4,881,911
Interbank loans receivable		1,292,492	451,227	1,292,492	451,227
Deposits with banks		102,793	55,026	101,849	53,043
		13,388,083	11,543,103	13,387,139	11,541,120
Interest expense on:	2,6				
Bills payable and other borrowings		5,734,771	5,002,968	5,734,734	5,002,968
Deposits		1,537,860	1,069,957	1,538,132	1,070,551
		7,272,631	6,072,925	7,272,866	6,073,519
Net interest income before provision for impairment		6,115,452	5,470,178	6,114,273	5,467,601
Provision for impairment	2,3,6,14	910,880	1,203,391	910,880	1,203,391
Net interest income after provision for impairment		5,204,572	4,266,787	5,203,393	4,264,210
Other income					
Profits from investment and securities trading	2,6	1,850,332	865,111	1,850,332	865,111
Foreign exchange profit/(loss)	2,6	(111,925)	462,475	(111,925)	462,475
Service charges, fees and commissions	6	272,907	227,294	269,892	224,498
Dividends - equity investments	6	9,138	30,481	9,138	38,117
Miscellaneous	2,6,24	811,902	901,394	765,791	848,644
		2,832,354	2,486,755	2,783,228	2,438,845
Other expenses					
Compensation and fringe benefits	2,3,6,27	3,000,067	2,515,775	2,915,973	2,434,437
Taxes and licenses	2,6	483,895	473,199	482,814	473,177
Occupancy expenses	2,6	48,390	43,067	42,963	40,758
Other operating expenses	2,6,25	1,495,704	1,382,664	1,542,321	1,424,154
		5,028,056	4,414,705	4,984,071	4,372,526
Net income before income tax		3,008,870	2,338,837	3,002,550	2,330,529
Provision for income tax	2,6,26	(207,675)	(106,230)	(209,476)	(110,507)
Net income for the year		P 3,216,545	P 2,445,067	P 3,212,026	P 2,441,036
Earnings per share		P 25.73	P 19.56	P 25.70	P 19.53

See accompanying Notes to Financial Statements.

Statements of Changes in Capital Funds

For the year ended December 31, 2005
(With comparative figures for 2004, as restated)
(In thousands of pesos, except per share amounts)

GROUP

	Notes	Common Stock Shares	Common Stock Amount	Surplus	Surplus Reserves/ Others	Undivided Profits	Total
Balance, December 31, 2003	6	125,000,000	P 12,500,000	P 6,443,945	P 767,055	P 1,978,846	P 21,689,846
Net income for the year	6					2,445,067	2,445,067
Cash dividends - 2003							
P6.00 per share				(750,000)			(750,000)
Prior years' adjustments				40,125			40,125
Net unrealized losses on							
securities	2,6				(940,452)		(940,452)
Surplus reserve set up	6,23			(3,703)	3,703		0
Appraisal increment reserves	2,6				(3,485)		(3,485)
Transfers to surplus				1,978,846		(1,978,846)	0
Balance, December 31, 2004	6	125,000,000	12,500,000	7,709,213	(173,179)	2,445,067	22,481,101
Net income for the year						3,216,545	3,216,545
Cash dividends - 2004							
P9.08 per share				(1,135,110)			(1,135,110)
Prior years' adjustments				(46,337)			(46,337)
Net unrealized gains on							
securities	2,6				1,033,811		1,033,811
Surplus reserve set up	6,23			(3,133)	3,133		0
Appraisal increment reserves	2,6			182,836	(182,836)		0
Transfers to surplus				2,445,067		(2,445,067)	0
Balance, December 31, 2005		125,000,000	P 12,500,000	P 9,152,536	P 680,929	P 3,216,545	P 25,550,010

PARENT

	Notes	Common Stock Shares	Common Stock Amount	Surplus	Surplus Reserves/ Others	Undivided Profits	Total
Balance, December 31, 2003	6	125,000,000	P 12,500,000	P 6,411,752	P 757,315	P 1,972,767	P 21,641,834
Net income for the year	6					2,441,036	2,441,036
Cash dividends - 2003							
P6.00 per share				(750,000)			(750,000)
Prior years' adjustments				40,125			40,125
Net unrealized losses on							
securities					(950,372)		(950,372)
Surplus reserve set up	6,23			(3,703)	3,703		0
Appraisal increment reserves	2,6				(3,485)		(3,485)
Transfers to surplus				1,972,767		(1,972,767)	0
Balance, December 31, 2004	6	125,000,000	12,500,000	7,670,941	(192,839)	2,441,036	22,419,138
Net income for the year						3,212,026	3,212,026
Cash dividends - 2004							
P9.08 per share				(1,135,110)			(1,135,110)
Prior years' adjustments				(45,881)			(45,881)
Net unrealized gains on							
securities	2,6				1,033,795		1,033,795
Surplus reserve set up	6,23			(3,133)	3,133		0
Appraisal increment reserves	2,6			182,836	(182,836)		0
Transfers to surplus				2,441,036		(2,441,036)	0
Balance, December 31, 2005		125,000,000	P 12,500,000	P 9,110,689	P 661,253	P 3,212,026	P 25,483,968

See accompanying Notes to Financial Statements.

Statements of Cash Flows

For the year ended December 31, 2005
(With comparative figures for 2004, as restated)
(In thousands of pesos)

	Notes	Group 2005	Group 2004	Parent 2005	Parent 2004
Cash flows from operating activities	6				
Interest income and dividends received		P 13,271,074	P 11,474,460	P 13,270,131	P 11,480,114
Interest expense paid		(7,402,574)	(5,873,721)	(7,402,809)	(5,874,314)
Bank commission, service charges and fees received		291,659	230,548	288,644	227,752
Profit from sale or redemption of investments		819,240	482,198	819,240	482,198
Trading gain		1,031,092	382,913	1,031,092	382,913
Other income received		463,409	1,101,721	417,299	1,048,971
General and administrative expenses paid		(3,979,829)	(4,553,342)	(3,941,076)	(4,512,958)
Changes in operating assets and liabilities:					
(Increase) Decrease in operating assets:					
Interbank loans receivable		3,078,879	(3,153,010)	3,078,879	(3,153,010)
Financial assets at fair value thru profit or loss		(2,550,443)	702,850	(2,550,443)	702,850
Financial assets available for sale		5,914,889	(6,606,795)	5,937,570	(6,614,613)
Loans and receivables		(9,950,413)	(2,328,835)	(9,950,413)	(2,328,835)
Accounts receivable-NG foreign exchange differential		25,288,769	(2,777,917)	25,288,769	(2,777,917)
Other assets		(602,949)	462,585	(593,453)	458,877
Increase (Decrease) in operating liabilities:					
Deposit liabilities		14,315,077	(964,172)	14,335,973	(964,980)
Due to Bangko Sentral ng Pilipinas		10,000	(258)	10,000	(258)
Due to other banks		5,241	(5,981)	5,240	(5,981)
Manager's checks and demand drafts outstanding		120,752	19,553	120,752	19,553
Deferred credits and other liabilities		247,366	(934,700)	248,831	(925,661)
Net cash generated from/(used in) operations	6	40,371,239	(12,341,903)	40,414,226	(12,355,299)
Income taxes paid		(1,054,231)	(1,194,108)	(1,052,431)	(1,189,830)
Net cash provided by/(used in) operating activities	6	39,317,008	(13,536,011)	39,361,795	(13,545,129)
Cash flows from investing activities	6				
Acquisition of bank premises, furniture, fixtures and equipment	15	(126,070)	(196,634)	(105,252)	(192,049)
Disposal/other transactions of bank premises, furniture, fixtures and equipment		35,245	55,357	35,246	55,357
(Increase) Decrease in:					
Financial assets held to maturity		1,270,027	(889,249)	1,260,745	(897,352)
Equity investment in subsidiaries		-	-	(35,000)	-
Equity investment in associates/joint venture			(21,198)	-	(10,937)
Non-current assets held for sale		657,468	(415,739)	657,468	(415,739)
Net cash provided by/(used in) investing activities	6	1,836,670	(1,467,463)	1,813,207	(1,460,720)
Cash flows from financing activities	6				
Increase (Decrease) in borrowings		(11,559,610)	12,338,003	(11,563,919)	12,338,003
Cash dividends paid		(1,135,110)	(750,000)	(1,135,110)	(750,000)
Net cash provided by/(used in) financing activities	6	(12,694,720)	11,588,003	(12,699,029)	11,588,003
Net increase (decrease) in cash and cash equivalents	6	28,458,958	(3,415,471)	28,475,973	(3,417,846)
Cash and cash equivalents at beginning of year		7,817,635	11,233,106	7,795,520	11,213,366
Cash and cash equivalents at end of year	2,6,7	P 36,276,593	P 7,817,635	P 36,271,493	P 7,795,520

See accompanying Notes to Financial Statements.

Notes to Financial Statements

Note 1 – General Information

The Development Bank of the Philippines (hereafter referred to as "Parent Company") was created by Republic Act No. 85 for the primary purpose of providing principally medium and long-term credit facilities for the rehabilitation, development and expansion of agriculture, industry, export development and government sector for the broadening and diversification of the national economy and to promote the establishment of private development banks in provinces and cities. On December 3, 1986, the Parent Company's Charter was revised under Executive Order No. 81 enabling them to achieve a more efficient and effective use of its resources. Under the new Charter, the Parent Company shall primarily provide banking services principally to cater to the medium and long-term financing needs of agricultural and industrial enterprises particularly in the countryside with emphasis on small and medium-scale industries. The Parent Company's orientation is that of a predominantly wholesale bank with a significant retail presence. As such, the Parent Company provides financial assistance to participating financial institutions for on-lending to investment enterprises and also direct to borrowers as may be required by its catalytic role in the economy. The Parent Company is also indulged in other activities including investments in government and private financial instruments.

The Bangko Sentral ng Pilipinas (BSP), in its letter dated December 20, 1995, granted the Parent Company the permit to operate as an expanded commercial bank (EKB). The Parent Company commenced operation as an EKB on February 7, 1996.

Republic Act No. 8523, otherwise known as an "Act Strengthening the Development Bank of the Philippines," amending EO No. 81 was signed into law by President Fidel V. Ramos on February 4, 1998. R.A. No. 8523 increased the authorized capital stock of the Parent Company from P5 billion to P35 billion, created the position of President or Vice Chairman of the Board of Directors who shall act as the Chief Executive Officer of the Bank and exempted the DBP from the coverage of the Salary Standardization Law.

The Parent Company and its subsidiaries (the Group) are engaged in development banking, financing, management services and computer services.

Its principal place of business is at Sen. Gil J. Puyat Avenue corner Makati Avenue, Makati City.

As of December 31, 2005, the Group had 3,879 employees (2004 – 3,648) and operated a total of 77 branches nationwide.

Note 2 - Summary of Significant Accounting Policies

a. Basis of Financial Statement Preparation

The Group's consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the Philippines as set forth in the Philippine Financial Reporting Standards/Philippine Accounting Standards (PFRS/PAS). These financial statements are prepared on the historical cost basis modified by the fair value measurement of financial assets on trading and available for sale securities, certain derivative instruments and real and other properties owned. The accompanying financial statements of the Parent Company reflect the accounts maintained in the Regular Banking Unit (RBU) and Foreign Currency Deposit Unit (FCDU). PFRS 1, First-time Adoption of the Philippine Financial Reporting Standards, has been applied in preparing these financial statements. These consolidated financial statements of the Group are their first financial statements prepared in accordance with PFRS.

The policies set out below have been consistently applied to all the years presented. The policies applied to financial instruments for 2004 and 2005 are discussed separately below.

Reconciliations and descriptions of the effect of the transition from the previous GAAP to PFRS on the Parent Company's balance sheet, net income and cash flows are provided in Note 6.

The preparation of financial statements in conformity with PFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the bank's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 3.

New accounting standards effective in 2005

The Financial Reporting Standards Council (FRSC) approved the issuance of new and revised accounting standards which are based on revised International Accounting Standards (IASs) and new International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB). These new standards have been renamed PASs to correspond to adopted IASs while the PFRSs correspond to adopted IFRSs.

The Group adopted the following PFRS/PAS, which are relevant to its operations.

PFRS 1	First-time Adoption of Philippine Financial Reporting Standards
PFRS 5	Non-current Assets Held for Sale and Discontinued Operations
PAS 1	Presentation of Financial Statements
PAS 7	Cash Flow Statements
PAS 8	Accounting Policies, Changes in Accounting Estimates and Errors
PAS 10	Events after the Balance Sheet Date
PAS 12	Income Taxes
PAS 16	Property, Plant and Equipment
PAS 17	Leases
PAS 18	Revenue
PAS 19	Employee Benefits
PAS 20	Accounting for Government Grants and Disclosure of Government Assistance
PAS 21	The Effects of Changes in Foreign Exchange Rates
PAS 23	Borrowing Costs
PAS 24	Related Party Disclosures
PAS 27	Consolidated and Separate Financial Statements
PAS 28	Investments in Associates
PAS 30	Disclosures in the Financial Statements of Banks and Similar Financial Institutions
PAS 31	Interests in Joint Ventures
PAS 32	Financial Instruments: Disclosures and Presentation
PAS 36	Impairment of Assets
PAS 37	Provisions, Contingent Liabilities and Contingent Assets
PAS 38	Intangible Assets
PAS 39	Financial Instruments: Recognition and Measurement

Except for PAS 21, 32, 36, and 39, the adoption of the above revised PASs did not result in substantial changes to the Group's accounting policies.

The 2004 accounts have been restated in accordance with the relevant requirements, except for those which specifically require prospective application. All changes in the accounting policies have been made in accordance with the transition provisions in the respective standards.

Changes in Accounting Policies

On January 1, 2005, the following new and revised accounting standards became effective and were adopted by the Group:

- PFRS 1, *First-time Adoption of Philippine Financial Reporting Standards,* requires compliance with each PFRS effective at the reporting date for its first PFRS financial statements. The standard allows limited exceptions from these requirements in specified areas where the cost of complying would be likely to exceed the benefits to users of financial statements. The standard also prohibits retrospective application of PFRSs in some areas, particularly where retrospective application would require judgements by management about past conditions after the outcome of a particular transaction is already known.

- PFRS 5, *Non-current Assets Held for Sale and Discontinued Operations,* specifies the accounting for assets held for sale and sets out requirements for the classification, measurement, presentation and disclosure of non-current assets held for sale. It requires assets that meet the criteria to be classified as held-for-sale to be measured at the lower of carrying amount and fair value less costs to sell, and once classified as such, the assets cease to be depreciated. Furthermore, assets that meet the criteria to be classified as held-for-sale should be presented separately on the face of the statements of condition.

- PAS 1, *Presentation of Financial Statements*, prescribes the basis for presentation of general purpose financial statements to ensure comparability both with the entity's financial statements of previous periods and with the financial statements of other entities; provides a framework within which the Group assesses how to present fairly the effects of transactions and other events; allows presentation of assets and liabilities in order of liquidity for as long as the liquidity presentation provides information that is reliable and is more relevant than a current/non-current presentation; prohibits the presentation of income and expense as extraordinary items and shown as separate line items in the statements of income; and specifies the disclosures about key sources of estimation uncertainty and judgements that management has made in the process of applying the Bank's accounting policies.

- PAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*, prescribes the criteria for selecting and changing accounting policies, changes in accounting estimates and corrections of errors. It removes the concept of fundamental error and the allowed alternative to retrospective application of voluntary changes in accounting policies and retrospective restatement to correct prior period errors. It defines material omissions or misstatements, and describes how to apply the concept of materiality when applying accounting policies and correcting errors.

- PAS 10, *Events After the Balance Sheet Date*, specifies when an entity should adjust its financial statements for events after the balance sheet date and the disclosures that an entity should give about the date when the financial statements were authorized for issue and about events after the balance sheet date; provides a limited clarification of the accounting for dividends declared after the statement of condition date. The standard defines events after balance sheet date as "those events, whether favorable or unfavorable, that occur between the balance sheet date and the date on which the financial statements are authorized for issue". These are simply known as subsequent events. Such events may either require adjustment or disclosure.

- PAS 12, *Income Taxes*, prescribes the accounting treatment for income tax specifically the principal issue of accounting for the current and future tax consequences; requires that a deferred tax asset be recognized only to the extent that it is probable that a tax benefit will be realized in the future. If it is probable that a tax benefit will be realized, a deferred tax asset is recognized on unused tax losses and unused tax credits. On the other hand, a deferred tax liability shall be recognized for all taxable temporary differences arising from revaluation of assets.

- PAS 16, *Property, Plant and Equipment (PPE)*, addresses the principal issues in accounting for PPE which are the recognition of the assets, the determination of their carrying amounts and the depreciation charges and impairment losses to be recognized in relation to them. It also provides that each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item shall be depreciated separately.

- PAS 17, *Leases*, provides a limited revision to clarify the classification of a lease of land and buildings and eliminates accounting alternative for initial direct costs in the financial statements of lessors.

- PAS 19, *Employee Benefits*, provides the accounting treatment for long-term and other employee benefits. The standard requires the use of projected unit credit method in determining the retirement benefits of the employees and a change in the manner of computing benefit expense relating to past service cost and actuarial gains and losses. It requires the Group to determine the present value of defined benefit obligations and the fair value of any plan assets with sufficient regularity that the amounts recognized in the financial statements do not differ materially from the amounts that would be determined at the statement of condition date.

- PAS 20, *Accounting for Government Grants and Disclosure of Government Assistance*, applies the accounting for and disclosure of, government grants and the other forms of government assistance. This standard requires that a government grant will not be recognized until there is reasonable assurance that the entity will comply with the conditions attached to it and that the grant will be received. It also requires that a government grant be recognized as income on a systematic basis over the periods necessary to match the grant income with the related costs that it is intended to compensate. If the related costs have already been incurred, the grant is recognized as income in the period in which it becomes receivable. A government grant is not credited directly to equity. Government grants related to assets are presented in the balance sheet either as deferred credits or as a deduction in determining the carrying amount of the asset. A government grant that becomes repayable is accounted for as a revision to an accounting estimate (PAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*).

- PAS 21, *Effects of Changes in Foreign Exchange Rates*, addresses the accounting for transactions and balances in foreign currency and the principal issues of which exchange rates to use and how to report the effects of changes in exchange rates in the financial statements.

- PAS 24, *Related Party Disclosures*, requires the disclosure of key management personnel (including non-executive directors) as a single total amount broken down into employee benefit types. This standard also considers retirement plans as related parties and requires disclosure of amounts of transactions and outstanding balances with respect to related parties, including the terms and conditions and any guarantee given or received. Any allowance for doubtful accounts and bad debts expense on related-party balances should be disclosed as well.

- PAS 27, *Consolidated and Separate Financial Statements*, applies in the preparation and presentation of consolidated financial statements for a group of entities under the control of a parent; reduces alternatives in accounting for subsidiaries in consolidated financial statements and in accounting for investments in the separate financial statements of a parent, venturer or investor. Investments in subsidiaries will be accounted for at cost. Equity method of accounting will no longer be allowed in the separate financial statements. This standard also requires strict compliance with adoption of uniform accounting policies and requires the parent to make appropriate adjustments to the subsidiary's financial statements to conform them to the Parent Company's accounting policies for reporting like transactions and other events in similar circumstances.

- PAS 28, *Investments in Associates*, reduces alternatives in accounting for associates in consolidated financial statements and in accounting for investments in the separate financial statements of an investor. Investments in associates will be accounted for at cost. Equity method of accounting will no longer be allowed in the separate financial statements. This standard also requires strict compliance with adoption of uniform accounting policies and requires the investor to make appropriate adjustments to the associate's financial statements to conform them to the investor's accounting policies for reporting like transactions and other events in similar circumstances.

- PAS 30, D*isclosures in the Financial Statements of Banks and Similar Financial Institutions*, sets out the required disclosures and presentation in respect of the accounts of banks and similar financial institutions.

- PAS 31, *Interests in Joint Ventures*, requires uniform application of accounting policies in accounting for interests in joint ventures. For separate financial statements of the parent company, PAS provides for the use of either the cost method or PAS 39 treatment in accounting for investments in joint ventures. The use of the equity method of accounting is no longer allowed.

- PAS 32, *Financial Instruments: Disclosure and Presentation*, covers the disclosures and presentation of all financial instruments. The standard requires more comprehensive disclosures about the Group's financial instruments, whether recognized or unrecognized in the financial statements. New disclosure requirements include terms and conditions of financial instruments used by the Group, types of risks associated with both recognized and unrecognized financial instruments (market risk, price risk, credit risk, liquidity risk, and cash flow risk), fair value information of both recognized and unrecognized financial assets and financial liabilities, and the Group's financial risk management policies and objectives. The standard also requires financial instruments to be classified as liabilities or equity in accordance with its substance and not its legal form.

- PAS 36, *Impairment of Assets*, establishes the procedures that an entity applies to ensure that assets are carried at not more than their recoverable amount. An asset is carried at more than its recoverable amount, if its carrying amount exceeds the amount to be recovered through use or sale of the asset. If this is the case, the asset is described as impaired and the standard requires the recognition of an impairment loss. The standard also specifies when to reverse an impairment loss and the required disclosures.

- PAS 38, *Intangible Assets,* requires discontinuance of amortization of intangible asset with an indefinite useful life. The effect of adopting this standard will not result in retroactive adjustment of prior year's financial statements but will effect prospective financial statements as a result of non-amortization.

- PAS 39, *Financial Instruments: Recognition and Measurement,* establishes the accounting and reporting standards for the recognition and measurement of the Bank's financial assets and financial liabilities. The standard requires a financial asset or financial liability to be recognized initially at fair value. Subsequent to initial recognition, the Group should continue to measure financial assets at their fair values, except for loans and receivables and held-to-maturity investments, which are measured at cost or amortized cost using the effective interest rate method. Financial liabilities are subsequently measured at cost or amortized cost, except for derivatives, which are subsequently measured at fair value.

  PAS 39 also covers the accounting for derivative instruments. The standard has expanded the definition of a derivative instrument to include derivatives (derivative-like provision) embedded in non-derivative contracts. Under the standard, every derivative instrument is recorded in the statements of condition as either an asset or liability measured at its fair value. Derivatives that are not hedges are adjusted to fair value through income. If the derivative is designated and qualifies as a hedge, depending on the nature of the hedge, changes in the fair value of the derivative are either offset against the change in fair value of the hedged assets, liabilities, or firm commitments through earnings, or recognized in capital funds until the hedged item is recognized in income. The Group must formally document, designate, and assess the effectiveness of derivative transactions that receive hedge accounting treatment.

b. Consolidation

Subsidiaries are consolidated when control is transferred to the Group and cease to be consolidated from the date on which the control is transferred out of the Group.

Under PAS 27, *Consolidated Financial Statements and Accounting for Investments in Subsidiaries,* the financial statements of the investee company have to be consolidated to the financial statements of the investor even if the shareholding of an enterprise is below 50% but the investor has evidence of control.

The Group financial statements reflect the consolidated accounts of the Parent Company and the following wholly-owned subsidiaries incorporated in the Philippines:

Subsidiary	Effective Percentage of Ownership
DBP Data Center, Incorporated	100%
DBP Management Corporation	100%

All significant inter-company balances and transactions have been eliminated in consolidation. The consolidated financial statements of the Group are prepared using uniform accounting policies for like transactions and other events in similar circumstances.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the bank. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition.

Investments in subsidiaries reflected in the Parent Company's financial statements are accounted for using the cost method.

c. Foreign currency translation

1) Functional and presentation currency

Items included in the financial statements of the bank's investee company are measured using the currency of the primary economic environment in which the subsidiary operates (the functional currency). The consolidated financial statements are presented in Philippine pesos, which is the bank's functional and presentation currency.

2) Transactions and balances

Foreign currency monetary items are accounted for in accordance with the provisions of PAS 21 "Effects of Changes in Foreign Exchange Rates" and are revalued monthly using the Philippine Dealing System (PDS) Peso/US dollar closing rate and the New York US dollar/third currencies closing rates as prescribed under BSP Circular 494 dated September 20, 2005. Actual foreign currency transactions are booked based on prevailing PDS as of transaction date. Foreign exchange differences arising from the above are charged to operations.

New provisions of PAS 21 do not apply to Bills Payable with foreign exchange risk cover. Bills Payable after initial recognition are restated to an amount corresponding to the loans granted which is the basis of computation of the foreign exchange risk claim from the National Government. Thereafter, as approved by the BSP in its letter dated December 27, 2005, revaluation of these foreign borrowings is charged to Accounts Receivable – NG Foreign Exchange Differential instead of profit or loss since the foreign exchange risk of these accounts is shouldered by the National Government.

Past due loans are now being revalued using the above rates and the foreign exchange difference booked under profit or loss.

d. Cash and cash equivalents

For purposes of reporting cash flows, cash and cash equivalents consist of cash and other cash items on hand, bank deposits, short-term interbank loans receivable, highly liquid investments that are readily convertible to cash and which are subject to insignificant risk of changes in value.

e. Due from other banks

Due from other banks include balances of funds on deposit with other foreign and local banks to meet not only reserve requirements but also to cover operational requirements especially in areas not covered by BSP clearing offices. This includes requirements for encashment of checks issued by the Department of Education, Culture and Sports (DECS) against their DBP accounts for the payroll of its public school teachers and other disbursements of the Department of Budget and Management (DBM) under the Modified Disbursement Scheme (MDS) of the Bureau of Treasury.

f. Financial assets

Consistent with PAS 39, Financial instruments - recognition and measurement, the Group's financial assets or financial liabilities are recognized initially at fair value. Subsequent to initial recognition, we continue to measure at fair value except for loans and receivables and held-to-maturity investments, which are measured at cost or amortized cost using the effective interest rate method. The effective interest rate shall refer to the rate that exactly discounts the estimated future cash receipts through the expected life of the security or when appropriate, a shorter period to the net carrying amount of the security. However, interest calculated using the effective interest rate method is recognized in the income statement when the entity's right to receive payment is established. Financial liabilities are measured at cost or amortized cost, except for derivatives, which are measured at fair value.

Available-for-sale financial assets and financial assets at fair value through profit or loss are carried at fair values. Gains and losses arising from changes in the fair value of the "financial assets at fair value through profit or loss" category are included in the income statement in the period in which they arise. Gains and losses arising from changes in the fair value of available-for-sale financial assets are recognized directly in equity, until the financial asset is derecognized or impaired at which time the cumulative gain or loss previously recognized in equity should be recognized in profit or loss.

This standard also covers the accounting for derivative instruments. This also expanded the definition of derivative instruments to include derivatives (derivative-like-provisions) embedded in non-derivative contracts. Every derivative instrument is recorded in the statement of condition as either an asset or liability measured at its fair value. Derivatives that are not hedges are adjusted to fair value through income. If the derivative is designated and qualifies as a hedge, depending on the nature of the hedge, changes in the fair value of the derivative are either offset against the change in fair value of the hedged assets, liabilities or firm commitments through earnings, or recognized in capital funds until the hedged item is recognized in income. The embedded derivative is being separated from the host contract and accounted for as a derivative considering the economic and risks of the host contract and booked as Available for Sale (AFS) Securities and Held for Trading (HFT) Securities/Derivatives at Fair Value Through Profit or Loss (DFVPL) for the host instrument and the embedded derivative, respectively.

The Group classifies its financial assets under the following categories:

Financial assets at fair value through profit or loss (FVTPL)

A financial asset is classified under this category where acquired principally for the purpose of selling in the near term or generating a profit from short-term fluctuations in price or dealer's margin. In other words, these are trading debt and equity securities that are purchased with the intent of selling them in the near term. These are normally classified as current assets. Derivatives are also categorized as held for trading unless they are designated as hedges. FVTPL are carried at fair or market value. Gains or losses arising from change in fair value or market revaluation are credited or charged to operations.

Financial assets available-for-sale (AFS)

Available for sale investments are those purchased and held indefinitely, which may be sold in response to liquidity needs or changes in interest rates, exchange rates or equity prices. These securities may be classified as current or non-current depending on whether they are intended to be held within one (1) year or for more than one (1) year. AFS are carried at fair or market value. Unrealized gains or losses on market valuation or change in fair value are reported as a separate component of stockholder's equity.

Sale and repurchase agreements

Securities sold subject to repurchase agreements (repos) are reclassified in the financial statement as pledged/repurchased assets when the transferee has the right by contract or custom to sell or repledge the collateral.

Financial assets held-to-maturity (HTM)

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the management has the positive intention and ability to hold to maturity. If the Group decides to sell or reclass more than an insignificant amount of held-to-maturity assets before maturity, the entire category would be tainted and reclassified as available-for-sale. Securities falling under this category are normally classified as non-current investments. HTM are carried at amortized cost. Gains or losses on amortization or on sales are credited or charged to operations.

g. Loans and receivables

Loans and receivables are non-derivative financial assets that are created by providing money directly to a debtor with fixed and determinable payment that are not quoted in an active market, other than:

1. those that the entity intends to sell immediately or in the near term, which shall be classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss;

2. those that the entity upon initial recognition designates as available for sale; or

3. those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration, which shall be classified as available for sale.

They are carried in the books at its amortised cost or the amount at which the financial asset or financial liability is measured at initial recognition minus principal repayments, plus or minus the cumulative amortization using the effective interest method of any difference between that initial amount and the maturity amount, and minus any reduction (directly or through the use of an allowance account) for impairment or uncollectibility.

In determining the effective interest rate, the estimated future cash flows considers all contractual terms of the financial instrument but shall not consider future credit losses. The Group collects front-end fees and other charges (i.e. commitment fees and service charges) that are not considered transaction costs in calculating the effective rate. These fees and other charges are recognized immediately as income of the Group upon collection except for front-end fees which are being amortized for a period of one year. Only forest funds collected as front-end fees are being booked directly as income.

Past due accounts are automatically carried on non-accrual basis. Interest income on such accounts is recognized only upon collection.

h. Unquoted debt securities classified as loans (UDSCL)

These are unquoted debt securities with fixed or determinable payments and fixed maturity. Unquoted debt securities classified as loans shall be measured upon initial recognition at their fair value plus transaction costs that are directly attributable to the acquisition of these securities. After initial recognition, a bank shall measure these securities at their amortized cost using the effective interest method.

i. Impairment of assets

A financial asset or a group of financial assets is impaired and impairment losses (the amounts by which the carrying amounts of loan, i.e., Outstanding Principal Balance (OPB) less Allowance for Probable Losses and Impairment Losses exceed their recoverable values) are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset and that loss event has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably measured/estimated.

If there is objective evidence that an impairment loss on loans and receivables has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and its recoverable value. Recoverable amount is the higher of its fair value less costs to sell and its value in use. Value in use is the present value of the future cash flows expected to be derived from an asset. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognized in the income statement.

When a loan is uncollectible, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of the provision for loan impairment in the income statement.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognized in the income statement.

In the case of real and other properties acquired (ROPA), bank premises, furniture, fixtures and equipment, and other assets, impairment loss is the difference between the carrying amount and the fair value less costs to sell in case carrying amount is higher. The loss is recognized in the income statement and an allowance account is set up to reduce the carrying amount of the asset.

j. Bank premises, furniture, fixtures and equipment

Bank premises, furniture, fixtures and equipment (including leasehold improvements) are stated at cost, less accumulated depreciation and amortization, and any impairment in value. Depreciation is computed based on a straight-line method over the estimated useful lives of the related assets as follows:

Building	15 - 50 years
Furniture and equipment	3 - 10 years

Impairment is recognized when there is a substantial evidence of decline in the value of the bank premises, furniture, fixtures and equipment.

The cost of leasehold improvements is amortized over the term of the lease or the estimated useful life of the improvements, whichever is shorter. Minor expenditures for replacement, maintenance and repairs are expensed as incurred. Major renovations and betterments that will extend the life of the asset are capitalized.

Properties that are no longer needed or uneconomical to maintain are disposed of in accordance with existing guidelines on disposal. Property Disposal Committees were created for this purpose. The cost and the related accumulated depreciation and amortization of the disposed asset are removed from the accounts and any resulting gain or loss is credited or charged to current operations.

In September 1992, the Parent Company's Norham property in Baguio was stated at appraised value as determined by an independent appraiser. The net increase in appraised value was credited to Appraisal Increment on Property shown under Stockholder's Equity. In compliance with the new PAS requirements, said appraisal increment was recognized as part of the deemed cost of the property and reversed to Surplus. Subsequent additions are stated at cost.

k. Investment in subsidiaries

Investment in subsidiary represents investment in equity securities for which the Parent Company owns 50% or more voting stocks and has control over the investee. These investments are carried at cost.

l. Investment in associates

Investment in associates represents investment in equity securities for which the Parent Company owns 20% to 50% of voting stock and has significant influence over the investee. These investments are carried at cost.

m. Non-current assets held for sale (NCAHFS)

Non-current assets held for sale are real and other properties acquired by the Parent Company in settlement of loans through foreclosure or dation in payment which are principally held for sale rather than through continuing use. They are available for immediate sale in its present condition subject only to terms that are usual and customary for sale of such assets and its sale are highly probable.

In compliance with PFRS 5, NCAHFS are carried in the books at the lower of its carrying amount and fair value less costs to sell. They are not subject to depreciation.

n. Leases

The leases entered into by the Parent Company are primarily operating leases. The total payments made under operating leases are recognized as an expense on a straight-line basis over the period of the lease.

When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognized as an expense in the period in which termination takes place.

o. Intangible assets

Intangible assets represent cost of software licenses and system development and maintenance. Intangible assets are measured at cost and amortized based on a straight line method with an expected useful life as follows:

Computer software licenses	2 - 5 years
System development and maintenance	3 - 10 years

Costs associated with developing or maintaining computer software programs are recognized as an expense as incurred. Costs that are directly associated with the production of identifiable and unique software products controlled by the bank, and that will probably generate economic benefits exceeding costs beyond one year, are recognized as intangible assets. Direct costs include software development employee costs and an appropriate portion of relevant overheads.

p. Employee benefits

Retirement benefits of the Parent Company's staff are covered by laws applicable to all government employees. Gratuities are paid by DBP for staff employed prior to June 1, 1977. Those employed thereafter shall be paid directly by the Government Service Insurance System. The Parent Company pays through a funded non-contributory gratuity plan consisting of actuarially determined normal annual service costs plus amortization of past service liability over a ten-year period which are charged to operations.

In compliance with applicable laws, the Parent Company established a provident fund for the benefit of its employees. Contributions made to the fund based on a predetermined rate are charged to operations.

q. Deferred Income Tax

Deferred income tax liabilities are the amounts of income taxes payable in future periods in respect of taxable temporary differences, including asset revaluations. Deferred income tax assets are the amounts of income taxes recoverable in future periods which are recognized for all deductible temporary differences, the carryforward of unused net operating loss carryover (NOLCO), to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and carry forward of and unused NOLCO can be utilized and unused tax credits.

Taxable temporary differences are temporary differences that will result in taxable amounts in determining taxable profit (tax loss) of future periods when the carrying amount of the asset or liability is recovered or settled. Deductible temporary differences are temporary differences that will result in amounts that are deductible in determining taxable profit (tax loss) of future periods when the carrying amount of the asset or liability is recovered or settled.

Deferred tax liabilities are not provided for non-taxable temporary differences associated with investments in domestic subsidiaries, associates and interest in joint ventures.

The carrying amount of deferred income tax asset is reviewed at each statement of condition date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilized.

Deferred income tax assets and liabilities are measured at the tax rates that are applicable to the period when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the statement of condition date.

r. Borrowing costs

Borrowing costs represent interests and other pertinent financial charges and costs incurred in connection with the availments of domestic and foreign borrowings. In compliance with PAS 23, that prescribes the accounting treatment for borrowing costs, such costs are generally recognized and accrued as an expense in the period in which they are incurred.

s. Government grants (WB-RPP Grant)

Global Environmental Facility Grant Trust Fund Agreement dated December 8, 2003 under Grant No. TF052188-PH amounting to US$9 M was signed between the International Bank for Reconstruction and Development (World Bank) and the Republic of the Philippines (ROP). The grant is intended to support activities for the efficient implementation of the World Bank – Rural Power Project (WB – RPP) with Development Bank of the Philippines and Department of Energy as executing agencies.

Out of the US$9 M grant, US$900,000 has been allocated to DBP through a Memorandum of Agreement (MOA) between Department of Finance (DOF), Department of Energy (DOE) and DBP to implement activities to reduce market barriers to the commercialization of renewable energy technologies. The agreement became effective on May 16, 2004 and shall be closed on December 31, 2009.

In compliance with PAS 20, Accounting for Government Grants and Disclosure of Government Assistance, the grant was recorded as deferred credits and recognized as income on the period the related costs were booked for proper matching of income and expense. As of December 31, 2005, total receipt of funds from the grant aggregated US$87 thousand with peso equivalent of P4.88 M.

t. Interest and other income and expense

Interest and other income and expenses are recognized on accrual basis, except for those loan accounts which are adversely classified consistent with the guidelines of the Bangko Sentral ng Pilipinas (BSP).

Note 3 – Significant Accounting Judgements and Estimates

The following are the critical judgements and key assumptions that have a significant risk of material adjustment to the carrying amounts of assets and liabilities within the next financial year:

a. Impairment losses of loans and receivables
The Group reviews its loan portfolios to assess impairment at

least annually or as the need arises. In determining whether an impairment loss should be recorded in the statement of income, the Group makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows which includes observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group.

b. *Fair value of derivatives*
The fair values of financial instruments that are not quoted in active markets are determined by using valuation methods. Where valuation methods are used to determine fair values, they are validated and periodically reviewed by qualified personnel independent of the area that created them. To the extent practical, valuation methods use only observable data. Changes in assumptions about these factors could affect reported fair values of financial instruments.

c. *Impairment of AFS investments*
The Group determines that AFS equity investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgement. In making this judgement, the Group evaluates among other factors, the normal volatility in share price. In addition, impairment may be appropriate when there is evidence of a deterioration in the financial health of the investee, industry and sector performance, changes in technology, and operational and financing cash flows.

d. *HTM Investments*
The Group follows the guidelines of PAS 39 on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as HTM. This classification requires significant judgement. In making this judgement, the Group evaluates its intention and ability to hold such investments to maturity. If the Group fails to keep these investments to maturity other than in certain specific circumstances – for example, selling of more than an insignificant amount close to maturity – it will be required to reclassify the entire portfolio as AFS. The investments would therefore be measured at fair value and not amortized cost.

e. *Recognition of deferred tax asset*
There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognizes liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

f. *Impairment of non-current assets held for sale / bank premises, furniture, fixtures and equipment / other assets*
Assets are reviewed and tested whenever there is indication of impairment at least annually. For the purpose of impairment test, assets may be grouped at the lowest levels or a cash generating unit defined as the smallest identifiable group of assets that generates cash inflows from other assets or groups of assets.

g. *Present value of retirement obligation*
The present value of incentives accruing to officers and employees who responded to the Parent Company's offer for early retirement up to the year 2008 amounted to P1.10 billion. PAS 19 provides that benefits which fall due for more than twelve months after the balance sheet date be rediscounted using average market yields on Philippine government bonds with terms consistent with the expected employee benefit payout as of statement of condition dates.

Accrued retirement incentives of the Parent Company for 2005 amounted to P835 million (2004 – P225 million).

Note 4 – Fair Values of Financial Assets and Liabilities

The methods and assumptions used by the Group in estimating the fair value of the financial instruments are:

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

Equity securities – Fair values are based on quoted prices published in markets.

Loans – Fair values are estimated using the discounted cash flow methodology, using the Group's current incremental lending rates for similar types of loans. Loans and advances are net of provisions for impairment.

Short-term investments – Carrying amounts approximate fair values.

Other – Quoted market prices are not readily available for these assets. They are not reported at fair value and are not significant in relation to the Group's total portfolio of securities.

Cash and cash equivalents – Carrying amounts approximate fair values.

Derivative instruments – Fair values are estimated based on quoted market prices provided by independent parties or accepted valuation models.

Note 5 – Financial Instruments Risk Position

The Parent Company's activities include investments in financial instruments including derivatives (subject to BSP regulations). The Bank accepts deposits from clients at both fixed and floating rates on various tenors, and seeks to earn considerable returns by investing these funds on high-quality assets.

The Parent Company also takes positions in traded instruments, including instruments with embedded derivatives, to take advantage of the volatilities on bonds and interest rates. The Board of Directors sets the trading parameters based on approved risk tolerance in relation to market positions. With the exception of specific hedging arrangements, foreign exchange and interest rate exposures associated with these derivatives are normally offset by entering into counter-balancing positions, thereby controlling the variability in the cash amounts required to liquidate market positions.

Credit/Counterparty Risk

Credit/counterparty risk, in its most basic form, is the risk that a client or counterparty will be unable or unwilling to pay obligations on time or in full as previously contracted, thus subjecting the Parent Company to a financial loss. The Parent Company manages its credit risk through the following:

- During the year, the Parent Company put in place an internal credit risk rating system for its Retail Lending Operation to standardize the measurement of credit risk for every exposure and use the result for business and financial decision making. The system, which covers companies having asset size of above P15 million, adopted primarily the Banker's Association of the Philippines model approved by the BSP as a minimum standard under BSP Circular 439. It has two (2) components: the Borrower Risk Rating System which provides credit assessment without security arrangements; and the Facility Risk Rating which takes into account credit risk mitigants. It has ten (10) rating levels, six (6) of which are mapped into unclassified accounts (Current and Watchlisted) and four (4) into classified accounts (Especially Mentioned, Substandard, Doubtful and Loss) requiring regulatory provisioning.

  Toward the end of the year, the Parent Company likewise approved the implementation of a pre-approval internal credit risk rating review of accounts by an independent internal control unit other than the marketing unit which initially rated the account to further strengthen the system's credibility as a good measurement of credit risk.

- Under the Parent Company's Wholesale Lending Operation, an accreditation guideline is in place to assess a financial institution's credit worthiness for participating local banks. This includes the following pre-qualifying factors: 3-year profitable track record, PDO of not more than 20%, capital to risk assets ratio of not less than 8% (for EKBs) and 10% (for non-EKBs), positive balance sheet and yield cost gap and compliance with BSP's minimum capital requirement. On the other hand, accreditation of foreign banks follows a Bank set minimum credit rating requirement from any of the following international credit rating agencies: Fitch IBCA, Standard and Poor's and Moody's.

- A system of limit is likewise in place to control credit risk. This is in the form of the BSP-prescribed Single Borrower's Limit (SBL) of 25% for retail, 35% for wholesale operation and counterparty limits for money market lines. As a manifest of a more prudent management, the Parent Company has also prescribed an internal retail SBL of 20% which is 5% lower than the external one. Independent monitoring and reporting of these limits are being done periodically.

The composition of the loans and receivable portfolio is detailed under Note 13.

Credit-related Commitments

The primary purpose of credit related commitments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit – which represent irrevocable assurances that the Parent Company will make payments in the event that a customer cannot meet its obligations to third parties – carry the same credit risk as loans. Documentary and commercial letters of credit – which are written undertakings by the Bank on behalf of a customer authorizing a third party to draw drafts on the Parent Company up to a stipulated amount under specific terms and conditions – are collateralized by the underlying shipments of goods to which they relate and therefore carry less risk than a direct borrowing.

Commitments to extend credit represent unused portions of authorizations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Parent Company is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards.

Market Risk

Market risk is the risk of loss of earnings on the Parent Company's portfolio, immediate or over time, resulting from changes in the price or interest rates, foreign currency exchange rates, equity prices and other market changes. The Parent Company's market risk comes from its positions in debt securities, equities, foreign exchange instruments and derivatives. The Parent Company uses the Value at Risk (VaR) methodology to measure its maximum potential loss from existing market sensitive positions using Historical Simulation Approach with the following assumptions: 99% confidence level, one-day holding period and a 500-day observation period. The VaR taken in conjunction with the VaR limit, which is set at a level higher than VaR, is the Parent Company's mechanism to control potential market risk. This is based on the principle that VaR should not exceed the set limit as the latter defines the management and the Board's risk appetite. However, the use of this approach does not prevent losses outside of this limit in the event of a more significant market movement.

The Parent Company has initially established the VaR for interest rate and foreign currency exchange rate which is being computed, monitored vis-a-vis their limits and reported to management on a daily basis. Table below shows the Parent Company's VaR for the year 2005: (In thousands)

Risk Factor	Average	High	Low
Interest rate risk	P 165,880	P 260,680	P 70,730
Foreign exchange risk	3,770	2,030	20
Total VaR	P 169,650	P 262,710	P 70,750

Interest Rate Risk

The Parent Company follows a prudent policy on managing its assets and liabilities so as to ensure that exposure to fluctuations in interest rates is kept within acceptable limits.

Treasury hedges part of its existing interest rate risk resulting from any potential decrease in the fair value of fixed assets or increase in fair value of the liabilities denominated both in local and foreign currencies using the interest rate swaps.

Liquidity Risk

The Parent Company is exposed daily on the following funding requirements: overnight deposits, current accounts, maturing deposits, loan draw-downs and guarantees, trading activities settlement and from margins and other calls on cash-settled derivatives. Management of the Parent Company's liquidity requirement is both on a day to day and long term basis. The Parent Company adheres to the required BSP's statutory reserve requirement. In addition, Liquidity Gap and Maximum Cumulative Outflow are being prepared to ensure that cumulative outflow for each pre-determined tenor bucket are within the maximum limits defined by the Board of Directors.

The following table sets forth the asset-liability gap position of the Group and the Parent Company as of December 31, 2005 and 2004: (In thousands)

Group
2005

	Up to 3 months	Over 3 - 6 months	Over 6 months - 1 year	Over 1 - 5 years	Over 5 years	Total
Assets						
Cash and other cash items	694,137	0	0	0	0	694,137
Due from BSP	3,266,702	0	0	0	0	3,266,702
Due from other banks	7,800,222	0	0	100,000	0	7,900,222
Loans - net	34,256,176	2,185,846	1,892,180	44,159,455	21,555,699	104,049,356
Investment securities	10,356,712	1,837,853	3,153,471	39,792,920	5,349,109	60,490,065
Other assets	30,080,667	666,042	1,943,901	3,193,675	672,201	36,556,486
Total Assets	86,454,616	4,689,741	6,989,552	87,246,050	27,577,009	212,956,968
Liabilities						
Due to BSP	0	0	0	70,000	0	70,000
Due to other banks	33,681	0	0	0	0	33,681
Deposits	46,495,720	1,404,445	2,123,882	595,929	132,899	50,752,875
Borrowings	13,048,216	7,519,829	5,265,837	20,269,501	83,866,805	129,970,188
Other liabilities	5,678,382	473,533	199,606	131,705	96,988	6,580,214
Total Liabilities	65,255,999	9,397,807	7,589,325	21,067,135	84,096,692	187,406,958
Asset-liability gap	21,198,617	(4,708,066)	(599,773)	66,178,915	(56,519,683)	25,550,010

Group
2004

	Up to 3 months	Over 3 - 6 months	Over 6 months - 1 year	Over 1 - 5 years	Over 5 years	Total
Assets						
Cash and other cash items	740,878	0	0	0	0	740,878
Due from BSP	1,684,088	0	0	0	0	1,684,088
Due from other banks	1,024,259	0	0	0	0	1,024,259
Loans - net	8,167,394	2,245,596	10,990,195	32,074,926	24,752,729	78,230,840
Investment securities	6,201,160	5,348,670	7,867,026	39,725,072	4,536,831	63,678,759
Other assets	56,254,445	697,075	366,379	2,903,300	575,291	60,796,490
Total Assets	74,072,224	8,291,341	19,223,600	74,703,298	29,864,851	206,155,314
Liabilities						
Due to BSP	0	0	0	60,000	0	60,000
Due to other banks	28,441	0	0	0	0	28,441
Deposits	31,680,198	2,801,404	889,045	925,868	141,282	36,437,797
Borrowings	4,673,991	15,066	3,946,830	1,990,523	130,903,388	141,529,798
Other liabilities	4,143,389	586,349	144,115	404,545	339,779	5,618,177
Total Liabilities	40,526,019	3,402,819	4,979,990	3,380,936	131,384,449	183,674,213
Asset-liability gap	33,546,205	4,888,522	14,243,610	71,322,362	(101,519,598)	22,481,101

Parent
2005

	Up to 3 months	Over 3 - 6 months	Over 6 months - 1 year	Over 1 - 5 years	Over 5 years	Total
Assets						
Cash and other cash items	694,106	0	0	0	0	694,106
Due from BSP	3,266,702	0	0	0	0	3,266,702
Due from other banks	7,795,153	0	0	100,000	0	7,895,153
Loans - net	34,256,176	2,185,846	1,892,180	44,159,455	21,555,699	104,049,356
Investment securities	10,354,245	1,837,853	3,153,471	39,792,920	5,349,109	60,487,598
Other assets	30,020,079	666,042	1,943,901	3,193,675	672,201	36,495,898
Total Assets	86,386,461	4,689,741	6,989,552	87,246,050	27,577,009	212,888,813
Liabilities						
Due to BSP	0	0	0	70,000	0	70,000
Due to other banks	33,681	0	0	0	0	33,681
Deposits	46,517,451	1,404,445	2,123,882	595,929	132,899	50,774,606
Borrowings	13,043,907	7,519,829	5,265,837	20,269,501	83,866,805	129,965,879
Other liabilities	5,658,847	473,533	199,606	131,705	96,988	6,560,679
Total Liabilities	65,253,886	9,397,807	7,589,325	21,067,135	84,096,692	187,404,845
Asset-liability gap	21,132,575	(4,708,066)	(599,773)	66,178,915	(56,519,683)	25,483,968

Parent
2004

	Up to 3 months	Over 3 - 6 months	Over 6 months - 1 year	Over 1 - 5 years	Over 5 years	Total
Assets						
Cash and other cash items	740,848	0	0	0	0	740,848
Due from BSP	1,684,088	0	0	0	0	1,684,088
Due from other banks	1,002,174	0	0	0	0	1,002,174
Loans - net	8,167,394	2,245,596	10,990,195	32,074,926	24,752,729	78,230,840
Investment securities	6,185,893	5,339,388	7,867,026	39,725,072	4,536,831	63,654,210
Other assets	56,223,357	697,075	366,379	2,903,300	575,291	60,765,402
Total Assets	74,003,754	8,282,059	19,223,600	74,703,298	29,864,851	206,077,562
Liabilities						
Due to BSP	0	0	0	60,000	0	60,000
Due to other banks	28,441	0	0	0	0	28,441
Deposits	31,681,034	2,801,404	889,045	925,868	141,282	36,438,633
Borrowings	4,673,991	15,066	3,946,830	1,990,523	130,903,388	141,529,798
Other liabilities	4,126,764	586,349	144,115	404,545	339,779	5,601,552
Total Liabilities	40,510,230	3,402,819	4,979,990	3,380,936	131,384,449	183,658,424
Asset-liability gap	33,493,524	4,879,240	14,243,610	71,322,362	(101,519,598)	22,419,138

Foreign Currency Risk

Control of foreign currency risks of the Parent Company is governed by the following policies:

- Position follows BSP regulation which is capped at US$ 5 million (long) or 2.5% of unimpaired capital, whichever is lower and the same amount for its short position.

- Stop loss limit.

The table summarizes the Parent Company's exposure to foreign exchange risk as of December 31, 2005. Included in the table are the Parent Company's assets and liabilities at carrying amounts, categorized by currency: (In thousand pesos)

	USD	Others	Total
Resources			
Due from other banks	7,138,223	518,372	7,656,595
Interbank loans receivables	12,040,102		12,040,102
Financial assets at fair value through profit and loss	1,134,207		1,134,207
Financial assets available for sale	12,460,086		12,460,086
Financial assets held to maturity	14,426,865		14,426,865
Loans and receivables	1,985,371	2,739	1,988,110
Non-current assets held for sale	4,435		4,435
Other resources	3,116,020		3,116,020
Total resources	52,305,309	521,111	52,826,420
Liabilities			
Deposit liabilities	9,370,841	7,202	9,378,043
Bills payable	27,990,806	161,439	28,152,245
Accrued taxes, interests and expenses	640,814	323,295	964,109
Deferred credits and other liabilities	431,140	22,309	453,449
Total liabilities	38,433,601	514,245	38,947,846
Net exposure	13,871,708	6,866	13,878,574
Total contingent accounts	12,768,299	68,432	12,836,731

Note 6 – Transition to PFRS

a. Basis of transition to PFRS

The Group's financial statements for the year ended December 31, 2005 will be the first annual financial statements that comply with PFRS. The Group's financial statements have been prepared as described in Note 2 and have applied PFRS 1 in preparing these financial statements.

The Group's transition date is January 1, 2004. The Group prepared its opening PFRS statement of condition at that date. The reporting date of these financial statements is December 31, 2005. The Group's PFRS adoption date is January 1, 2005.

b. Exceptions from full retrospective application followed by the Group

Pursuant to the mandatory exceptions with respect to PFRS 5, the Group recognized all assets held for sale only from January 1, 2005.

c. Reconciliations between PFRS and GAAP

The following table presents the reconciliation of the statement of condition of the Parent Company as previously reported to its restated figures in 2004 due to adoption of PFRS: (In thousands)

		December 31, 2004			January 1, 2004		
	Notes	Previous GAAP	Effect of transition to PFRS	PFRS	Previous GAAP	Effect of transition to PRFS	PFRS
Resources							
Cash and other cash items		P 740,848		P 740,848	P 1,028,541		P 1,028,541
Due from Bangko Sentral ng Pilipinas		1,684,088		1,684,088	1,988,273		1,988,273
Due from other banks	a	997,647	P 4,527	1,002,174	1,098,542	P 3,656	1,102,198
Interbank loans receivable	b	7,776,928	(5,371)	7,771,557	7,344,491		7,344,491
Financial asset at fair value through profit or loss	c	1,096,771	19,559	1,116,330	1,799,621	42,337	1,841,958
Financial asset available for sale - net	d	36,118,871	2,716,030	38,834,901	32,451,883	1,302,842	33,754,725
Financial asset held to maturity - net	e	24,726,958	(1,179,469)	23,547,489	21,753,675	415,410	22,169,085
Loans and receivables - net	f	69,998,674	460,609	70,459,283	68,194,024	475,431	68,669,455
Bank premises, furniture, fixtures and equipment - net		971,888		971,888	932,858		932,858
Equity investment in subsidiaries/ associates - net	g	528,039	(372,549)	155,490	731,451	(586,898)	144,553
Non-current assets held for sale - net	h	4,604,574	(174,231)	4,430,343	4,187,467	(205,638)	3,981,829
Accounts receivable- NG FX differential	i	0	46,567,078	46,567,078	0	43,789,161	43,789,161
Other assets – net	j	7,876,545	919,548	8,796,093	7,243,699	834,435	8,078,134
Total resources		P157,121,831	P48,955,731	P206,077,562	P148,754,525	P46,070,736	P 194,825,261
Liabilities							
Current maturities of long-term borrowings	k	P 9,924,138	P14,014,595	P23,938,733	P 7,629,038	P 4,024,961	P 11,653,999
Deposit liabilities		36,438,633		36,438,633	37,403,613		37,403,613
Bills payable	k	85,261,224	32,329,841	117,591,065	77,985,960	39,551,836	117,537,796
Due to Bangko Sentral ng Pilipinas		60,000		60,000	60,258		60,258
Due to other banks		28,441		28,441	34,422		34,422
Manager's checks and demand drafts outstanding		488,778		488,778	469,225		469,225
Accrued taxes, interests and expenses	l	2,591,465	232,540	2,824,005	2,596,410	216,020	2,812,430
Deferred credits and other liabilities	m	2,473,824	(185,055)	2,288,769	3,334,702	(123,018)	3,211,684
Total liabilities		137,266,503	46,391,921	183,658,424	129,513,628	43,669,799	173,183,427
Capital Funds							
Common Stock		12,500,000		12,500,000	12,500,000		12,500,000
Surplus	n	5,270,004	2,400,937	7,670,941	4,034,750	2,377,002	6,411,752
Surplus Reserves		243,888		243,888	240,185		240,185
Net unrealized gain/ (loss) on securities	o	(611,620)	(7,943)	(619,563)	330,809		330,809
Appraisal increment on property		182,836		182,836	186,321		186,321
Undivided profits		2,270,220	170,816	2,441,036	1,948,832	23,935	1,972,767
Total capital funds		19,855,328	2,563,810	22,419,138	19,240,897	2,400,937	21,641,834
Total liabilities and capital funds		P157,121,831	P 48,955,731	P206,077,562	P148,754,525	P 46,070,736	P 194,825,261

The following table presents the reconciliation of the statement of income of the Parent Company as previously reported to net income, as restated in 2004: (In thousands)

		For the year ended December 31, 2004		
	Notes	Previous GAAP	Effect of transition to PRFS	PFRS
Interest income				
Loans and receivables		P 6,154,939		P 6,154,939
Financial assets - debt and equity securities	p	4,915,326	P (33,415)	4,881,911
Interbank loans receivable		451,227		451,227
Deposits with banks		53,043		53,043
		11,574,535	(33,415)	11,541,120
Interest expense				
Bills payable and other borrowings		5,002,968		5,002,968
Deposits		1,070,551		1,070,551
		6,073,519		6,073,519
Net interest income before provision for impairment		5,501,016	(33,415)	5,467,601
Provision for impairment		1,203,391		1,203,391
Net interest income after provision for impairment		4,297,625	(33,415)	4,264,210
Other income				
Profits from investment and securities trading		870,482	(5,371)	865,111
Foreign exchange profit/(loss)		466,550	(4,075)	462,475
Service charges, fees and commissions		224,498		224,498
Dividends – equity investments		30,481	7,636	38,117
Miscellaneous		863,352	(14,708)	848,644
	q	2,455,363	(16,518)	2,438,845
Other expenses				
Compensation and fringe benefits		2,434,437		2,434,437
Taxes and licenses		473,177		473,177
Occupancy expenses		33,835	6,923	40,758
Other operating expenses		1,437,229	(13,075)	1,424,154
	r	4,378,678	(6,152)	4,372,526
Net income before income tax		2,374,310	(43,781)	2,330,529
Provision for income tax	s	104,090	(214,597)	(110,507)
Net income for the year		P 2,270,220	P 170,816	P 2,441,036

The following table presents the reconciliation of the statement of cash flow of the Parent Company as previously reported to its restated figures in 2004 due to adoption of PFRS: (In thousands)

		For the year ended December 31, 2004		
	Notes	Previous GAAP	Effect of transition to PRFS	PFRS
Cash flows from operating activities				
Interest income and dividends received	t	P 11,466,029	P 14,085	P 11,480,114
Interest expense paid	u	(5,882,074)	7,760	(5,874,314)
Bank commission, service charges and fees received	v	226,527	1,225	227,752
Profit from sale or redemption of investments		482,198		482,198
Trading gain	w	388,284	(5,371)	382,913
Other income received	x	1,039,695	9,276	1,048,971
General and administrative expenses paid	y	(4,401,236)	(111,722)	(4,512,958)
Changes in operating assets and liabilities:				
(Increase) Decrease in operating assets:				
Interbank loans receivable	z	(3,158,381)	5,371	(3,153,010)
Financial assets at fair value thru profit or loss		702,850		702,850
Financial assets available for sale	aa	(4,648,782)	(1,965,831)	(6,614,613)
Loans and receivables	bb	(2,360,065)	31,230	(2,328,835)
Accts. Receivable-NG FX Diff'l	cc		(2,777,917)	(2,777,917)
Other assets	dd	341,553	117,324	458,877
(Increase) Decrease in operating liabilities:				
Deposit liabilities		(964,980)		(964,980)
Due to Bangko Sentral ng Pilipinas		(258)		(258)
Due to other banks		(5,981)		(5,981)
Manager's checks and demand drafts outstanding		19,553		19,553
Deferred credits and other liabilities	ee	(849,048)	(76,613)	(925,661)
Net cash generated from/(used in) operations		(7,604,116)	(4,751,183)	(12,355,299)
Income taxes paid		(1,189,830)		(1,189,830)
Net cash provided by/(used in) operating activities		(8,793,946)	(4,751,183)	(13,545,129)
Cash flows from investing activities				
Acquisition of bank premises, furniture, fixtures and equipment		(192,049)		(192,049)
Disposal/other transactions of bank premises, furniture, fixtures and equipment		55,357		55,357
(Increase) Decrease in:				
Financial assets held to maturity	ff	(2,528,883)	1,631,531	(897,352)
Equity investment in subsidiaries/associates	gg	(391,583)	380,646	(10,937)
Non-current assets held for sale	hh	(387,977)	(27,762)	(415,739)
Net cash provided by/(used in) investing activities		(3,445,135)	1,984,415	(1,460,720)
Cash flows from financing activities				
(Increase) Decrease in borrowings	ii	9,570,364	2,767,639	12,338,003
Cash dividends paid		(750,000)		(750,000)
Net cash provided by/(used in) financing activities		8,820,364	2,767,639	11,588,003
Net increase (decrease) in cash and cash equivalents		(3,418,717)	871	(3,417,846)
Cash and cash equivalents at beginning of year	jj	11,209,710	3,656	11,213,366
Cash and cash equivalents at end of year	jj	P 7,790,993	P 4,527	P 7,795,520

Notes to the reconciliation of statement of condition as of December 31 and January 1, 2004: (amounts in thousand pesos)

(a) The adjustments to Due from other banks consist of:

Description	Dec. 31, 2004	Jan. 1, 2004
Foreign exchange revaluation of Due from foreign banks special account	P 4,527	P 3,656

(b) The (P5,371) adjustment in 2004 represents marking to market of credit linked notes/credit linked deposits (CLN/CLD) placements after considering bifurcation.

(c) The adjustments to Financial asset at fair value through profit or loss (FVTPL) consist of:

Description	Dec. 31, 2004	Jan. 1, 2004
Reclassification from other assets of accrued interest receivable pertaining to FVTPL	P 19,559	P 42,337

(d) The net adjustments to Financial asset available for sale (AFS) account as a result of adoption of certain standards consist of:

Description	Dec. 31, 2004	Jan. 1, 2004
Reclassification from equity investments investments and held to maturity of investment securities	P 2,514,303	P 556,416
Reclassification from other assets of accrued interest receivable pertaining to AFS	824,175	768,601
Reclassification from equity investments of allowance for probable losses	(622,448)	(22,175)
	P 2,716,030	P 1,302,842

(e) The net adjustments to Financial asset held to maturity (HTM) account as a result of adoption of certain standards consist of:

Description	Dec. 31, 2004	Jan. 1, 2004
Reclassification to Financial asset available for sale of investment securities	P (1,610,962)	
Reclassification from other assets of accrued interest receivable pertaining to HTM	431,493	P 415,410
	P (1,179,469)	P 415,410

(f) The adjustments to Loans and receivable account as a result of adoption of certain standards consist of:

Description	Dec. 31, 2004	Jan. 1, 2004
Reclassification from other assets of accrued interest receivable pertaining to Loans and receivables	P 644,060	P 567,219
Reclassification from deferred credits of unearned interest and discounts	(183,451)	(123,018)
Foreign exchange revaluation of past due loans		62,460
Additional provision as a result of recording impairment losses under PAS 39		(31,230)
	P 460,609	P 475,431

(g) The adjustments to Equity investment in subsidiaries/associates consist of:

Description	Dec. 31, 2004	Jan.1, 2004
Change from equity to cost method of accounting for investments in subsidiaries and associates	P (50,299)	
Reclassification to available for sale securities	(944,698)	P (609,073)
Reclassification to available for sale of related allowance for probable losses	622,448	22,175
	P (372,549)	P (586,898)

(h) The net adjustments of Non-current assets held for sale are as follows:

Description	Dec. 31, 2004	Jan. 1, 2004
Reclassification to other assets of sales contract receivable and other real estate owned	P (176,956)	P (208,315)
Reclassification to other assets of related allowance for probable losses	2,725	2,677
	P (174,231)	P (205,638)

(i) The net adjustments to Accounts Receivable – NG FX differential consist of:

Description	Dec. 31, 2004	Jan. 1, 2004
Revaluation of Bills payable with FX risk cover through AR-NG FX differential	P 46,567,078	P 43,789,161

(j) The net adjustments to Other assets consist of:

Description	Dec. 31, 2004	Jan. 1, 2004
Reclassification of accrued interest receivable to the following accounts:		
- Fair value through profit or loss	P (19,559)	P (42,337)
- Available for sale securities	(824,175)	(768,601)
- Held to maturity	(431,493)	(415,410)
- Loans and receivables	(644,060)	(567,219)
Marking to market of foreign exchange swap	27,642	
Set up of Deferred Income Tax on Allowance for Probable Losses and other temporary differences	2,636,962	2,422,364
Reclassification from ROPA of sales contract receivable and other real estate owned and its related allowance for probable losses	174,231	205,638
	P 919,548	P 834,435

(k) The adjustments represent foreign exchange revaluation of Bills payable with foreign exchange risk cover, as follows:

Description	Dec. 31, 2004	Jan. 1, 2004
Current maturities of long-term borrowings	P 14,014,595	P 4,024,961
Bills payable	32,329,841	39,551,836
	P 46,344,436	P 43,576,797

(l) The adjustments to accrued taxes, interests and expenses consist of:

Description	Dec. 31, 2004	Jan. 1, 2004
Foreign exchange revaluation of accrued interest payable of borrowings with FX risk cover	P 225,617	P 216,020
Additional accrual of leases for the Branch network due to adoption of straight line method of computation	6,923	
	P 232,540	P 216,020

(m) The net adjustments to Deferred credits and other liabilities consist of:

Description	Dec. 31, 2004	Jan. 1, 2004
Reclassification to loans and receivable of related unearned interest and discounts	P (183,451)	P (123,018)
Reclassification to profit/(loss) on sale of asset of unrealized profit on asset sold/ exchange	(3,645)	
Proceeds of Grant which will be recognized as income in the same period as the relevant expense	2,041	
	P (185,055)	P (123,018)

(n) The net adjustments to Surplus represent:

Description	Dec. 31, 2004	Jan. 1, 2004
Change in the method of accounting for investments in subsidiaries and associates from equity to cost	P (21,427)	P (45,362)
Set up of Deferred Income Tax on Allowance for Probable Losses and other temporary differences	2,422,364	2,422,364
	P 2,400,937	P 2,377,002

(o) The (P7,943) adjustment in 2004 of Net Unrealized gain/(loss) on securities represents marking to market of CLN/CLD placements after considering bifurcation.

Notes to the reconciliation of statement of income for the year ended December 31, 2004: (amounts in thousand pesos)

(p) The (P33,415) adjustment represents amortization of premium and discount as a result of adoption of effective interest rate.

(q) The adjustments on Other Income consist of :

Marking-to-market of CLN/CLD placements after considering bifurcation	P (5,371)
Foreign exchange (FX) revaluation of past due loans and special bank accounts for bills payable with FX risk cover and marking-to-market of FX Swap	(4,075)
Dividend income received from DBP MC	7,636
Reclassification of loss on acquisition of acquired asset (AA) account from operating expenses to miscellaneous income	(13,075)
Derecognition of share in net income from equity investment as a result of change in accounting method from equity to cost	(5,278)
Reclassification to income from sale of AA from unrealized profit from sale of AA	3,645
	P (16,518)

(r) The adjustments on Other Expenses consist of :

Additional accrual of leases for the Branch network due to the adoption of straight line method of computation	P 6,923
Reclassification of loss on acquisition of acquired asset (AA) account from operating expenses to miscellaneous income	(13,075)
	P (6,152)

(s) The (P214,597) adjustment on Provision for Income Tax represents set-up of Deferred Income Tax on provision for probable losses and other temporary differences.

Notes to the reconciliation of statement of cash flow for the year ended December 31, 2004: (amounts in thousand pesos)

(t) The adjustments on interest income and dividends received are due to the following:

Amortization of premium and discount as a result of adoption of effective interest rate	P (33,415)
Dividend income received from DBP MC	7,636
Inclusion of the net transactions of the following:	
Unearned interest and discount	60,433
Accumulated bond discount	(89,656)
Accumulated bond premium	69,087
	P 14,085

(u) The adjustments on interest expense paid consist of the following:

FX differential due to revaluation of Accrued interest payable	P 9,597
Inclusion of the net transactions of Prepaid expenses-guarantee fees	(1,837)
	P 7,760

(v) The difference is due to the inclusion of the net transactions of Other deferred credits (ODC) – Front-end-fees amounting to P1,225.

(w) The (P5,371) adjustment represents marking to market of CLN/CLD placements after considering bifurcation.

(x) The adjustments in other income consist of the following:

Foreign exchange (FX) revaluation of past due loans and special bank accounts for bills payable with FX risk cover and marking-to-market of FX Swap	P (4,075)
Inclusion of the net transactions of ODC other than front-end-fees and interest differential fund	13,351
	P 9,276

(y) The difference in general and administrative expenses is due to the following:

Inclusion of the net transactions of the following:	
Deferred charges	P (87,560)
Prepaid expenses other than guarantee fees	(24,162)
	P (111,722)

(z) The P5,371 adjustment represents marking to market of CLN/CLD placements after considering bifurcation.

(aa) The net adjustments to Financial assets available for sale represent the following adjustments:

Reclassification from equity investments and held to maturity of Investment securities	P (1,957,887)
Net effect of accumulated market gain/loss	(7,944)
	P (1,965,831)

(bb) The P31,230 adjustment represents additional provision as a result of recording impairment losses under PAS 39.

(cc) The net adjustments to Accounts Receivable – NG FX Differential are due to the foreign exchange revaluation of the following accounts:

Bills payable	P (2,767,639)
Accrued interest payable	(9,597)
Due from banks	(681)
	P (2,777,917)

(dd) The net adjustments to Other assets consist of:

Marking to market of foreign exchange swap	P (27,642)
Reclassification from ROPA of sales contract receivable and other real estate owned and its related allowance for probable losses	31,407
Exclusion of the net transactions of the following:	
- Prepaid expenses	25,999
- Deferred charges	87,560
	P 117,324

(ee) The net adjustments to Deferred credits and other liabilities consist of:

Reclassification to profit/(loss) on sale of asset of unrealized profit on asset sold/exchange	P (3,645)
Proceeds of Grant which will be recognized as income in the same period as the relevant expense	2,041
Exclusion of the net transactions of the following:	
- Unearned interest and discounts	(60,433)
- Other deferred credits	(14,576)
	P (76,613)

(ff) The net adjustments to Financial asset held to maturity (HTM) are detailed as follows:

Reclassification to Financial assets available for sale of investment securities	P 1,610,962
Inclusion of the net transactions of the following:	
Accumulated bond discount	89,656
Accumulated bond premium	(69,087)
	P 1,631,531

(gg) The adjustments to Equity investment in subsidiaries/associates are due to the adoption of certain standards, as follows:

Change from equity to cost method of accounting for investments in subsidiaries and associates	P 50,299
Reclassification to available for sale securities	335,625
Derecognition of share in net income from equity investment as a result of change in accounting method from equity to cost	(5,278)
	P 380,646

(hh) The net adjustments to Non-currrent assets held for sale are detailed as follows:

Reclassification to other assets of sales contract receivable and other real estate owned	P	(31,359)
Reclassification to other assets of related allowance for probable losses		(48)
Reclassification to income from sale of acquired assets from unrealized profit from sale of AA		3,645
	P	(27,762)

(ii) The P2,767,639 adjustment to borrowings represents foreign exchange revaluation of Bills payable with foreign exchange risk cover.

(jj) The adjustments to cash and cash equivalents consist of:

Description	Dec. 31, 2004	Jan. 1, 2004	Diff.
Foreign exchange revaluation of Due from foreign banks special account	P 4,527	P 3,656	P 871

Note 7 – Cash and cash equivalents

This account at December 31 consists of: (In thousands)

	Group		Parent	
	2005	2004	2005	2004
Cash and other cash items	P 694,137	P 740,878	P 694,106	P 740,848
Due from Bangko Sentral ng Pilipinas	3,266,702	1,684,088	3,266,702	1,684,088
Due from other banks	7,900,222	1,024,259	7,895,153	1,002,174
Interbank loans receivable	24,415,532	4,368,410	24,415,532	4,368,410
	P36,276,593	P 7,817,635	P36,271,493	P 7,795,520

The undrawn borrowing facilities of the Parent Company that may be available for future operating activities and to settle capital commitments as of December 31, 2005 amounted to P17.56 billion.

Note 8 - Due from Bangko Sentral ng Pilipinas

This account represents the Group's demand and time deposits in local and foreign currencies maintained with BSP to meet reserve requirements and to serve as clearing account for interbank claims consistent with BSP guidelines. DBP, as a government financial institution (GFI), maintains BSP as its major depository.

Note 9 – Interbank loans receivable

This account consists of loans and placements granted to the following banks: (In thousands)

	Group		Parent	
	2005	2004	2005	2004
Domestic	P14,870,268	P 4,174,346	P14,870,268	P 4,174,346
Foreign	9,869,532	3,597,211	9,869,532	3,597,211
	P24,739,800	P 7,771,557	P24,739,800	P 7,771,557

Interbank loans receivable of the Group carry interest rates at December 31 as follows:

	2005	2004
Peso denominated	7.50% - 8.375%	6.75% - 8.25%
Foreign currency denominated	4.22% - 7.21625%	2.34% - 10.35%

Note 10 – Financial assets at fair value through profit or loss

This account consists of: (In thousands)

	Group		Parent	
	2005	2004	2005	2004
Government securities purchased	P 3,637,733	P 1,087,394	P 3,637,733	P 1,087,394
Equity securities	9,481	9,377	9,481	9,377
	3,647,214	1,096,771	3,647,214	1,096,771
Accrued interest receivable	39,028	19,559	39,028	19,559
Total Trading account securities	P 3,686,242	P 1,116,330	P 3,686,242	P 1,116,330

The movement in FVTPL is summarized as follows: (In thousands)

	Group	Parent
At December 31, 2004	P 1,116,330	P 1,116,330
Additions	34,297,824	34,297,824
Disposals	(32,136,589)	(32,136,589)
Fair value adjustments	556,962	556,962
Exchange differences	(167,754)	(167,754)
	3,666,773	3,666,773
Interest accrual	19,469	19,469
At December 31, 2005	P 3,686,242	P 3,686,242

The FVTPL of the Group carry interest rates at December 31 as follows:

	2005	2004
Peso denominated	5.320% - 10.953%	7.929% - 12.741%
Foreign currency denominated	5.397% - 10.378%	4.952% - 8.344%

Note 11 – Financial assets available for sale

This account consists of: (In thousands)

	Group		Parent	
	2005	2004	2005	2004
Debt securities:				
Government				
Treasury notes	P16,061,051	P22,819,677	P16,061,051	P22,819,677
Retail treasury bonds	2,065,169	5,445,567	2,065,169	5,445,567
Treasury bills	94,541	3,397,601	94,541	3,397,601
Treasury bonds - ROP	1,102,670	4,215,788	1,102,670	4,215,788
NFA bonds	1,400,000	0	1,400,000	0
Pag-ibig bonds	722,044	0	722,044	0
	21,445,475	35,878,633	21,445,475	35,878,633
Private				
PLDT	218,138	240,238	218,138	240,238
	21,663,613	36,118,871	21,663,613	36,118,871
Investments/Notes with embedded derivatives	11,139,278	1,569,605	11,139,278	1,569,605
Equity securities:				
Government	205,000	205,000	205,000	205,000
Private	746,563	742,512	721,508	739,698
	951,563	947,512	926,508	944,698
	33,754,454	38,635,988	33,729,399	38,633,174
Accrued interest receivable	893,892	824,378	893,730	824,175
	34,648,346	39,460,366	34,623,129	39,457,349
Allowance for impairment	(622,448)	(622,448)	(622,448)	(622,448)
	P34,025,898	P38,837,918	P34,000,681	P38,834,901

The Parent Company's AFS is carried at inclusive/net of accumulated unrealized gain/(loss) of P414 million and (P620) million as of December 31, 2005 and 2004, respectively.

The movement in AFS is summarized as follows: (In thousands)

	Group	Parent
At December 31, 2004	P 38,837,918	P 38,834,901
Additions	120,532,337	120,510,096
Disposals	(125,713,842)	(125,713,842)
Fair value adjustments	1,246,918	1,246,918
Exchange differences	(946,947)	(946,947)
	33,956,384	33,931,126
Interest accrual	69,514	69,555
At December 31, 2005	P 34,025,898	P 34,000,681

The AFS of the Group carry interest rates at December 31 as follows:

	2005	2004
Peso denominated	5.200% - 11.814%	7.855% - 16.015%
Foreign currency denominated	4.743% - 10.270%	3.598% - 9.110%

Note 12 – Financial assets held to maturity

This account consists of debt securities at amortized cost: (In thousands)

	Group		Parent	
	2005	2004	2005	2004
Marketable securities	P 7,131,032	P16,136,912	P 7,131,032	P16,127,630
Long-term bonds/ securities	15,054,893	7,412,336	15,054,893	7,412,336
	22,185,925	23,549,248	22,185,925	23,539,966
Accrued interest receivable	454,601	431,493	454,601	431,493
	22,640,526	23,980,741	22,640,526	23,971,459
Allowance for impairment	0	(423,970)	0	(423,970)
	P22,640,526	P23,556,771	P22,640,526	P23,547,489

Government securities amounting to P231 million has been deposited with BSP since December 31, 2003 as security for trust duties.

The movement in HTM is summarized as follows: (In thousands)

	Group	Parent
At December 31, 2004	P 23,556,771	P 23,547,489
Additions	78,594,130	78,594,130
Maturities	(79,802,615)	(79,793,333)
(Amortization)/accretion of premium/discount	71,619	71,619
Exchange differences	(226,457)	(226,457)
	22,193,448	22,193,448
Interest accrual	23,108	23,108
Reclass of allowance for impairment	423,970	423,970
At December 31, 2005	P 22,640,526	P 22,640,526

The HTM of the Group carry interest rates at December 31 as follows:

	2005	2004
Peso denominated	3.702% - 15.625%	7.050% - 17.784%
Foreign currency denominated	4.770% - 10.751%	3.049% - 10.981%

Note 13 – Loans and receivables

a. This account consists of: (In thousands)

	Group		Parent	
	2005	2004	2005	2004
Loans and discounts	P83,992,027	P74,994,605	P83,992,027	P74,994,605
Underwritten debt securities purchased	2,800,000	2,257,950	2,800,000	2,257,950
Bills purchased	2,355	8,481	2,355	8,481
	86,794,382	77,261,036	86,794,382	77,261,036
Accrued interest receivable	780,274	644,060	780,274	644,060
Unearned discount/ income	(170,026)	(183,451)	(170,026)	(183,451)
	87,404,630	77,721,645	87,404,630	77,721,645
Allowance for impairment	(8,095,074)	(7,262,362)	(8,095,074)	(7,262,362)
	P79,309,556	P70,459,283	P79,309,556	P70,459,283

	2005	2004
Current Portion	P 17,462,027	P 12,638,001
Past Due Loans:		
Amount	P 8,289,476	P 9,212,677
Rate	7.43%	10.83%
Non-Performing Loans:		
Amount	P 8,895,049	P 9,118,730
Rate	7.44%	10.01%

Above past due rates are way below industry average of 9.00% for CY 2005 and 13.75% for CY 2004, based on BSP figures.

Wholesale lending portfolio represents 45% as of December 31, 2005 and 49% as of 2004 of the Parent Company's total loan portfolio.

The highest exposure is to the financial intermediation amounting to P36 billion or 41% of the total loan portfolio. The next highest exposure is the P15 billion for manufacturing sector representing 17% of the total loan portfolio. This is followed by financial assistance to real estate, renting and business administration sector amounting to P9 billion or 11% of the total loan portfolio for the year. Other exposures are distributed widely among BSP classified industries.

b. Classification of loans as to security exclusive of AIR is as follows: (In thousands)

	2005			2004		
Secured:						
Retail	P 29,006,143		83%	P 30,293,691		86%
Wholesale *	5,871,508		17%	5,000,000		14%
	P 34,877,651	40%	100%	P 35,293,691	46%	100%
Unsecured:						
Retail	18,863,782		36%	9,221,917		22%
Wholesale *	33,052,949		64%	32,745,428		78%
	P 51,916,731	60%	100%	P 41,967,345	54%	100%
	P 86,794,382	100%		P 77,261,036	100%	

These loans pertain to the conduit lending granted to 41 accredited financial institutions for various developmental projects with longer gestation periods payable at determinable amounts and fixed maturity dates. The risks associated to the loans are secured by a Deed of Assignment of the mortgaged collaterals executed by all the participating financial institutions.

- Participating financial institutions (PFIs) of the Wholesale Banking Sector (WBS) pass through rigid accreditation criteria. Once accredited, said PFIs can avail themselves of credit facilities generally on a clean line basis. However, the investment enterprises (IEs), beneficiaries of the loan facilities from the PFIs, are required to assign their collaterals to DBP.

Note 14 - Allowance for impairment

The changes in the Allowance for Impairment are as follows: (In thousands)

	Group		Parent	
	2005	2004	2005	2004
Balance, January 1	P 9,204,587	P 8,191,475	P 9,204,161	P 8,191,109
Effect of transition to PFRS	0	70,954	0	70,954
Provision for impairment	910,880	1,203,391	910,880	1,203,391
Reserve charges due to				
Write-offs/writedowns	(5,817)	(3,404)	(5,817)	(3,404)
Foreclosure	(77,618)	(271,765)	(77,618)	(271,765)
Sale of acquired assets	(293,094)	0	(293,094)	0
Other adjustments	(61,398)	13,936	(61,398)	13,876
Balance, December 31	P 9,677,540	P 9,204,587	P 9,677,114	P 9,204,161

The Parent Company's General Reserves is P1.43 billion, of which P0.50 billion is intended for additional provision for impairment that may be required by the marketing units for specific loans, NCAHFS, investments and other related accounts and those that maybe suggested by BSP and/or COA.

Note 15 - Bank premises (including leasehold improvements), furniture, fixtures and equipment

This account represents the book value of the following assets: (In thousands)

	Group		Parent	
	2005	2004	2005	2004
Land	P 321,050	P 321,050	P 321,050	P 321,050
Building	565,990	561,403	561,045	560,453
Office equipment, furniture and fixtures	1,104,953	1,137,345	1,077,598	1,125,656
Transportation equipment	350,364	334,119	349,694	333,450
	2,342,357	2,353,917	2,309,387	2,340,609
Accumulated depreciation	(1,379,152)	(1,377,139)	(1,368,933)	(1,368,721)
Allowance for impairment	(340)	0	(340)	0
	(1,379,492)	(1,377,139)	(1,369,273)	(1,368,721)
Total	P 962,865	P 976,778	P 940,114	P 971,888

Broken down as follows:

Group	Land	Building	Leasehold Improvement	Computer Equipment	Office Machine, Furniture and Fixtures	Transportation Equipment	Total
At December 31, 2004							
Cost	321,050	540,423	20,980	544,211	593,134	334,119	2,353,917
Accumulated depreciation	0	(231,808)	0	(345,981)	(496,358)	(302,992)	(1,377,139)
Net book amount	**321,050**	**308,615**	**20,980**	**198,230**	**96,776**	**31,127**	**976,778**
Year ended December 2005							
Opening net book amount	321,050	308,615	20,980	198,230	96,776	31,127	976,778
Additions	0	9,314	7,266	40,708	34,359	34,423	126,070
Disposals	0	(4,884)	0	(79,294)	(32,689)	(5,201)	(122,068)
Impairment loss	0	(340)	0	0	0	0	(340)
Depreciation	0	(18,525)	0	9,724	11,404	(4,616)	(2,013)
Amortization	0	0	(5,102)	0	0	0	(5,102)
Adjustments	0	(2,007)	0	6,107	(1,583)	(12,977)	(10,460)
Closing net book amount	**321,050**	**292,173**	**23,144**	**175,475**	**108,267**	**42,756**	**962,865**
At December 31, 2005							
Cost	321,050	542,846	23,144	511,732	593,221	350,364	2,342,357
Accumulated depreciation	0	(250,333)	0	(336,257)	(484,954)	(307,608)	(1,379,152)
Allowance for impairment	0	(340)	0	0	0	0	(340)
Net book amount	**321,050**	**292,173**	**23,144**	**175,475**	**108,267**	**42,756**	**962,865**

Parent	Land	Building	Leasehold Improvement	Computer Equipment	Office Machine, Furniture and Fixtures	Transportation Equipment	Total
At December 31, 2004							
Cost	321,050	540,423	20,030	534,699	590,957	333,450	2,340,609
Accumulated depreciation	0	(231,808)	0	(338,786)	(495,585)	(302,542)	(1,368,721)
Net book amount	321,050	308,615	20,030	195,913	95,372	30,908	971,888
Year ended December 2005							
Opening net book amount	321,050	308,615	20,030	195,913	95,372	30,908	971,888
Additions	0	9,314	2,210	28,119	31,186	34,423	105,252
Disposals	0	(4,884)	0	(79,294)	(32,689)	(5,201)	(122,068)
Impairment loss	0	(340)	0	0	0	0	(340)
Depreciation	0	(18,525)	0	11,100	11,709	(4,496)	(212)
Amortization	0	0	(4,041)	0	0	0	(4,041)
Adjustments	0	(2,007)	0	6,110	(1,490)	(12,978)	(10,365)
Closing net book amount	321,050	292,173	18,199	161,948	104,088	42,656	940,114
At December 31, 2005							
Cost	321,050	542,846	18,199	489,634	587,964	349,694	2,309,387
Accumulated depreciation	0	(250,333)	0	(327,686)	(483,876)	(307,038)	(1,368,933)
Allowance for impairment	0	(340)	0	0	0	0	(340)
Net book amount	321,050	292,173	18,199	161,948	104,088	42,656	940,114

The P340 million allowance for impairment pertains to DBP's Norham property in Baguio.

Note 16 – Equity investment in subsidiaries

This account consists of: (In thousands)

	Group 2005	Group 2004	Parent 2005	Parent 2004
Investments in subsidiaries (wholly owned)				
Acquisition cost:				
DBP Data Center, Incorporated	P 0	P 0	P 1,250	P 1,250
DBP Management Corporation	0	0	37,500	2,500
	P 0	P 0	P 38,750	P 3,750

Note 17 – Equity investment in associates

This account consists of: (In thousands)

	Group 2005	Group 2004	Parent 2005	Parent 2004
DBP Service Corporation	P 856	P 856	P 856	P 856
LGU Guarantee Corporation	105,690	105,690	105,690	105,690
Odyssey Capital Ventures	10,938	10,938	10,938	10,938
DBP Daiwa Securities	45,675	45,675	45,675	45,675
	P 163,159	P 163,159	P 163,159	P 163,159
Allowance for impairment	(41,760)	(11,419)	(41,760)	(11,419)
	P 121,399	P 151,740	P 121,399	P 151,740

Note 18 – Equity investment in joint venture

At a special meeting held on December 20, 1995, the Board of Directors of DBP Management Corporation (MC) approved the following:

· The designation of the DBP MC as nominee/assignee of the Parent Company with respect to the latter's performance of part or all of its obligations and exercise of part or all of its rights in the Shareholder's Agreement to be entered into by and among the DBP, Daiwa Securities Co. Ltd. (DAIWA) and Pan Malayan Management and Investment Corporation (PMMIC);

· The appropriation of the sum of P16 M representing DBP-MC's investment as nominee/assignee in the Company to be organized by DBP, Daiwa and PMMIC pursuant to the Shareholder's Agreement.

This account consists of: (In thousands)

	Group 2005	Group 2004	Parent 2005	Parent 2004
Daiwa Securities Co., Ltd.	P 16,000	P 16,000	P 0	P 0

Note 19 - Other assets

This account consists of: (In thousands)

	Group 2005	Group 2004	Parent 2005	Parent 2004
Accounts receivable	P 3,872,284	P 2,762,291	P 3,840,955	P 2,742,062
Deferred income tax	2,979,417	2,636,962	2,979,417	2,636,962
Amortization fund - TSD	1,254,482	1,446,544	1,254,482	1,446,544
Inter-office float items	497,529	192,997	497,529	192,997
Prepaid expenses	479,190	423,587	478,470	423,168
Other assets - Heritage Park	421,921	431,135	417,747	426,962
Sales contract receivable	201,503	174,768	201,503	174,768
Other deferred charges	126,165	326,521	126,165	326,521
Miscellaneous assets - Intangibles *	98,780	80,504	98,780	80,504
Dividends and interest receivable	55,689	71,709	55,689	71,709
Real estate owned	1,034	2,187	1,034	2,187
Miscellaneous	551,603	444,625	549,563	442,822
	10,539,597	8,993,830	10,501,334	8,967,206
Allowance for impairment	(175,874)	(171,539)	(175,448)	(171,113)
	P10,363,723	P 8,822,291	P10,325,886	P 8,796,093

* Net of accumulated amortization amounting to P59.99 million for 2005.

Note 20 – Bills payable

The Group and Parent Company's bills payable consists of the following: (In thousands)

	Group 2005	Group 2004	Parent 2005	Parent 2004
Domestic	P 4,098,976	P 3,819,260	P 4,094,667	P 3,819,260
Foreign:				
- with FX risk cover	97,718,967	125,837,668	97,718,967	125,837,668
- without FX risk cover	28,152,245	11,872,870	28,152,245	11,872,870
	125,871,212	137,710,538	125,871,212	137,710,538
	P129,970,188	P141,529,798	P129,965,879	P141,529,798
Maturities:				
Within one year	P 38,898,052	P 23,938,733	P 38,896,341	P 23,938,733
Beyond one year	91,072,136	117,591,065	91,069,538	117,591,065
	P129,970,188	P141,529,798	P129,965,879	P141,529,798

Borrowings in foreign currency without foreign exchange risk cover (FXRC) by the National Government (NG) are lent in the same currency. Accordingly, foreign exchange risk is assumed by the borrower.

The 2005 year-end balances of all foreign borrowings were revalued using the month-end PDS rate in accordance with PAS 21 and BSP Circular 494 dated September 20, 2005. Likewise, to make it comparable, the 2004 outstanding bills payable balances were also restated at revalued amounts.

The foreign exchange gain/(loss) arising from revaluation of outstanding foreign borrowings wherein the foreign exchange risk is assumed by the NG were booked under Accounts Receivable – NG Foreign Exchange Differential. The revaluation of Bills Payable were P21,050,723 and P46,344,436 in 2005 and 2004, respectively.

Other information for bills payable as of December 31, 2005, were as follows: (In thousand pesos)

	Bills Payable	
	Wholesale	Retail
a. Maturities		
Maximum		
Domestic	12 years	25 years
Foreign	40 years	40 years
Average		
Domestic	5 years	14 years
Foreign	21 years	20 years
b. Average rate (interest rate to funders)		
Domestic	4.83%	7.74%
Foreign	3.18%	2.51%
c. Balance		
Maximum month-end balance	72,980,377	31,387,927
Average monthly balance	57,542,660	29,576,375

Note 21 - Deposit liabilities

Deposits maturing within the year amounted to P49,655,059 thousand and P49,676,790 thousand for the Group and Parent Company, respectively.

Note 22 - Deferred credits and other liabilities

This account consists of: (In thousands)

	Group		Parent	
	2005	2004	2005	2004
Accounts payable	P1,194,924	P1,151,402	P1,194,879	P1,151,377
Unearned income/ deferred credits	485,302	762,844	485,302	762,844
Due to Treasury of the Philippines	224,236	63,627	224,236	63,627
Withholding taxes payable	170,319	125,883	170,319	125,883
Cash letters of credit	97,806	75,606	97,806	75,606
Outstanding acceptances	33,291	6,206	33,291	6,206
Other miscellaneous liabilities	344,760	119,657	329,813	103,226
	P2,550,638	P2,305,225	P2,535,646	P2,288,769

Miscellaneous liabilities include mainly derivative financial liabilities, special funds and domestic bills for clearing.

Note 23 – Surplus reserves

This account consists of: (In thousands)

	Group		Parent	
	2005	2004	2005	2004
Reserve for trust business	P 90,812	P 87,679	P 90,812	P 87,679
Reserve for contingencies	85,199	85,199	85,199	85,199
Other surplus reserves				
Loans – Japan Exim Special Facility	4,937	4,937	4,937	4,937
Fund – Japan Training & Technical Assistance	66,027	66,027	66,027	66,027
Expense – Japan Exim Special Facility	46	46	46	46
Appropriated General Reserves Fund for the proposed increase in capitalization - DBP MC	20,000	20,000	0	0
	91,010	91,010	71,010	71,010
	P 267,021	P 263,888	P 247,021	P 243,888

In accordance with BSP regulations, reserves for trust business represents accumulated appropriation of surplus computed based on 10% of the yearly net income realized by the Parent Company from its trust operations as follows: (In thousand pesos)

	Annual Trust Net Income	10% Share in Net Income	Balance
Beginning CY 2003			80,573
Add: 10% Net Income			
CY 2003	34,018	3,402	83,975
CY 2004	37,035	3,704	87,679
CY 2005	31,332	3,133	90,812

Reserves for contingencies include P50.0 million set aside per Board Resolution No. 0578 dated October 12, 2001 to cover possible losses the Parent Company may incur for any unfavorable court decision on all lawsuits where the Parent Company is involved. It also includes P35.2 million set aside for possible losses on defalcation by and other unlawful acts of the Parent Company's personnel or third parties.

Note 24 – Miscellaneous income

The Group's miscellaneous income substantially represents profit/(loss) from assets sold, additional interest and penalty charges and recovery from charged-off assets.

Note 25 – Other operating expenses

The Group's other operating expenses comprise significantly of management and other professional fees, security, clerical, messengerial and janitorial expenses, depreciation and amortization expenses, insurance expense, litigation/assets acquired expense and power, light and water expenses.

Note 26 - Provision for income tax

Under Philippine tax laws, the Group is 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 or GRT and documentary stamp taxes.

Income taxes include the corporate income tax, as discussed below, and final taxes paid at the rate of 20% which is a final withholding tax on gross interest income from government securities and other deposit substitutes.

The regular corporate income tax rate increased from 32% to 35% effective November 1, 2005. This is in pursuant to BIR Revenue Regulations No. 16-2005 dated September 1, 2005, implementing RA 9337 dated May 24, 2005, otherwise known as the New Expanded VAT. Statutory income tax reflected below is pro-rated to 32% for 10 months and 35% for 2 months.

Interest allowed as a deductible expense is reduced by an amount equivalent to 38% and 42% of interest income subjected to final tax pro-rated for ten (10) months and two (2) months, respectively. The regulations also provide for minimum corporate income tax (MCIT) of 2% on modified gross income and allow a NOLCO. The MCIT and NOLCO may be applied against the Group's income tax liability and taxable income respectively, over a three-year period from the year of inception.

Provision for income tax consists of: (In thousands)

	Group		Parent	
	2005	2004	2005	2004
Current				
Final taxes	P 103,463	P 104,090	P 103,463	P 104,090
RCIT	1,801	4,277		
MCIT	29,516	0	29,516	0
	134,780	108,367	132,979	104,090
Deferred	(342,455)	(214,597)	(342,455)	(214,597)
	P (207,675)	P(106,230)	P(209,476)	P (110,507)

Components of the deferred income tax are as follows: (In thousands)

	Group		Parent	
	2005	2004	2005	2004
Allowance for probable losses	P2,642,894	P2,448,399	P2,642,894	P2,448,399
Gratuity pay	213,522	0	213,522	0
Foreign exchange profit/ (loss) revaluation	58,756	0	58,756	0
Others	210,616	188,563	210,616	188,563
Trading gain revaluation	(146,371)	0	(146,371)	0
	P2,979,417	P2,636,962	P2,979,417	P2,636,962

A reconciliation between the provision for corporate income tax at statutory tax rate and the actual provision for corporate income tax as of December 31 of the Parent Company is as follows: (In thousands except for rates)

	2005		2004	
	Amount	Rate (%)	Amount	Rate (%)
Statutory income tax	P 975,829	32.50	P 759,779	32.00
Effect on items not subject to statutory tax rate:				
Income subjected to lower tax rates	(824,750)	(27.47)	(901,272)	(37.96)
Tax-exempt income	(855,715)	(28.50)	(440,251)	(18.54)
Non-deductible expenses	987,465	32.89	583,451	24.57
Others	(492,305)	(16.40)	(112,214)	(4.72)
Tax benefits	P (209,476)	(6.98)	P (110,507)	(4.65)

The Parent Company did not recognize deferred tax assets on NOLCO since it believes that it is not reasonably probable that it will be realized in the future.

The details of the Parent Company's NOLCO and MCIT are as follows: (In thousands)

Inception Year	Amount	Used/Expired	Balance	Expiry Year
NOLCO				
2003	P 791,582	P 534,947 *	P 256,635	2006
2004	24,286	0	24,286	2007
	815,868	534,947	280,921	
MCIT				
2005	29,516	0	29,516	2008
	29,516	0	29,516	

* NOLCO claimed as deduction in CY 2005.

Note 27 – Related party transactions

In the ordinary course of business, the Parent Company enters into loan transactions with certain directors, officers and related interests (DOSRI). Under the existing policies of the Parent Company, these loans are made substantially on the same terms as with other individuals and businesses of comparable risks. The amount of individual loans to DOSRI, 70% of which must be secured, should not exceed the amount of their unencumbered deposits and book value of their investments in the Parent Company. In the aggregate, DOSRI loans should not exceed the total capital funds or 15% of the total loan portfolio of the Parent Company, whichever is lower. BSP Circular No. 423 dated March 15, 2004 amended the definition of DOSRI accounts to include a corporation, association or firm in which the DBP and/or the National Government holds or owns at least twenty percent (20%) of the subscribed capital of such corporation or in the equity of such association or firm.

The following table shows Parent Company's information relating to loans, other credit accommodations and guarantees classified as DOSRI accounts under said circular: (In thousands)

	2005	2004
Total outstanding DOSRI loans	P 4,272,514	P 4,649,527
% to total outstanding loans and advances	4.92%	6.03%
% to total outstanding DOSRI loans		
Unsecured DOSRI loans	22.76%	17.53%
Past due DOSRI loans	0.43%	0.00%
Non-performing DOSRI loans	0.43%	0.00%

The remuneration of directors and members of key management are estimated as follows: (In millions)

	Group		Parent	
	2005	2004	2005	2004
a.) Short-term employee benefits	P 52.22	P 54.80	P 46.62	P 53.17
b.) Post employment benefits	54.59	123.91	54.28	123.91
	P 106.81	P 178.71	P 100.90	P 177.08

Note 28 - Commitments and contingent liabilities

In the normal course of the Group's operations, there are various lawsuits filed against the Group, pending tax assessments, outstanding commitments and contingent liabilities, such as guarantees, commitments to extend credit, forward exchange contracts, interest rate swaps and similar arrangements which are not reflected in the accompanying financial statements. No material losses are anticipated as a result of these transactions.

The Parent Company has also received assessments on two industry issues, which are presently being resolved in an industry basis. Accordingly, no provision has yet been recognized.

The Parent Company's contingent liabilities aggregated as follows: (In thousands)

	2005	2004
Transferred to national government (NG)	P 33,054,373	P 40,356,619
Letters of credits and other contingent liabilities	25,459,639	15,729,510
	P 58,514,012	P 56,086,129

Contingent liabilities transferred to NG is in accordance with Proclamation No. 50 dated December 8, 1986. Since then, NG provides funding for maturing amortizations thereon.

Note 29 - Trust funds

The Parent Company is authorized under its charter to perform trust and fiduciary activities thru the Trust Services Department. Trust Funds are managed, accounted and reported individually in accordance with regulatory policies and investment agreements with trustors. Trust resources as of December 31, 2005 amounted to P17.39 billion from 2004 year-end balance of P15.44 billion. Consistent with the General Banking Act, government securities with total principal amount of P24.77 million are deposited with BSP as security for the Parent Company's faithful performance of its fiduciary obligation. These are off-books transactions and therefore not included in the Parent Company's financial statements.

Income realized from trust operations amounted to P31.33 million, net of operating expenses of P49.96 million and Gross Receipts Tax of P4.45 million, which was remitted to the Parent Company and included in its financial statements.

Note 30 - Foreign currency deposit unit

The Parent Company has been authorized by BSP to operate an Expanded Foreign Currency Deposit Unit (EFCDU) since August 1995.

Income derived under the expanded foreign currency deposit system from foreign currency transactions with non-residents, offshore banking units in the Philippines, local commercial banks including branches of foreign banks that may be authorized by the BSP to transact business with foreign currency deposit units and other depository banks under the expanded foreign currency deposit system shall be exempt from all taxes. However, interest income from foreign currency loans granted to residents shall be subject to a final tax of ten percent (10%), pursuant to Republic Act No. 9294 (approved by President Gloria M. Arroyo on April 28, 2004).

Following BSP Circular letter dated November 7, 2003, FCDU transferred to Bank Proper on February 13, 2006 a total amount of US$ 8.3 million in the form of cash (due from foreign banks) covering CY 2005 income.

Note 31 - Other information

	2005	2004
Key financial indicators of the Parent Company		
Return on average equity	14.80%	12.76%
Return on average assets	1.76%	1.55%
Net interest margin	3.80%	4.00%
Capital to risk assets ratio	19.73%	22.72%
Efficiency ratio	56.01%	55.31%
Salaries & personnel expenses/ operating expenses	58.51%	55.66%

Note 32 – Events after the balance sheet date

To strengthen its capital base, the Parent Company offered in January 2006 unsecured lower tier 2 subordinated notes to the public. The notes have a maturity of 10 years and are subject to an optional redemption by the issuer after 5 years. Interest rate was pegged at 9.5% net for individual and tax-exempt institutions. The initial offering generated P 2.35 billion.

Note 33 – Approval of financial statements

The financial statements of the DBP Group have been approved for issuance by the Board of Directors on August 30, 2006.