

SECURITIES AND EXCHANGE COMMISSION

SEC FORM 17-Q

QUARTERLY REPORT PURSUANT TO SECTION 17 OF THE SECURITIES
REGULATION CODE AND SRC RULE 17(2) (b) THEREUNDER

1. For the quarterly period ended SEPTEMBER 30, 2016
2. SEC Identification Number A199701584 3. BIR Tax Identification No. 000-005-469-606
4. Exact name of issuer as specified in its charter PHILIPPINE BUSINESS BANK, INC.
5. CALOOCAN Province, Country or other jurisdiction of incorporation or organization
6. (SEC Use Only) Industry Classification Code:
7. 350 Rizal Avenue corner 8th Avenue Grace Park, Caloocan City 1400
Address of principal office Postal Code
8. (02) 363-33-33
Issuer's telephone number, including area code
9. NOT APPLICABLE
Former name, former address, and former fiscal year, if changed since last report.

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

Title of Each Class	Number of Shares of Common Stock Outstanding and Amount of Debt Outstanding
<u>Common</u>	536,458,438

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

Yes [x] No []

The Bank was listed in Philippine Stock Exchange last February 19, 2013

If yes, state the name of such Stock Exchange and the class/es of securities listed therein:

PHILIPPINE STOCK EXCHANGE

COMMON SHARES OF STOCK

12. Indicate by check mark whether the registrant:

- (a) has filed all reports required to be filed by Section 17 of the Code and SRC Rule 17 thereunder or Sections 11 of the RSA and RSA Rule 11(a)-1 thereunder, and Sections 26 and 141 of the Corporation Code of the Philippines, during the preceding twelve (12) months (or for such shorter period the registrant was

required to file such reports)

Yes [] No []

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

Yes [] No []

PART I – FINANCIAL INFORMATION

Item I:

Management's Discussion & Analysis of Financial Position and Results of Operations

Item II:

Financial Statements (Attachment 1 - Unaudited Interim Financial Statements)

PART II – OTHER INFORMATION

Please refer to the following:

Attachment 2 – Aging of Past Due Loans and Other Receivables

Attachment 3 – Consolidated Financial Ratios

There are no material disclosures that have not been reported under SEC Form 17-C during the period covered by this report.

SIGNATURES

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

PHILIPPINE BUSINESS BANK, INC.

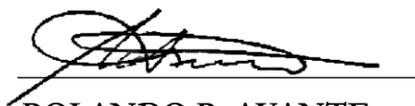
Issuer

By:

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FRANCIS T. LEE

Chairman

A handwritten signature in black ink, featuring a large, stylized initial 'R' followed by several horizontal and vertical strokes, positioned above a horizontal line.

ROLANDO R. AVANTE

President & CEO

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements.

The accompanying financial reporting package (FRP) of Philippine Business Bank (“PBB” or the “Bank”) which comprise the Bank’s financial position as of September 30, 2016 and December 31, 2015 and the statements of income, statements of comprehensive income, statements of changes in equity and statements of cash flows for the nine-month periods ending September 30, 2016 and September 30, 2015 have been prepared in compliance with Philippine Financial Reporting Standards (PFRS).

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

A. Management’s Discussion and Analysis

	For the nine-months ended			
	9/30/2016	9/30/2015	Variance	%
Interest Income				
Loans and other receivables	₱ 1,957,817,676	₱ 1,915,773,881	₱ 42,043,795	2.2
Investment and trading securities	319,383,414	384,741,615	(65,358,201)	(17.0)
Securities purchased under reverse repurchase agreement	16,985,269	-	16,985,269	-
Due from BSP and other banks	75,762,590	47,574,463	28,188,127	59.3
	2,369,948,949	2,348,089,959	21,858,990	0.9
Interest Expense	(556,937,265)	(553,318,520)	(3,618,745)	0.7
Net Interest Income	1,813,011,684	1,794,771,439	18,240,245	1.0

Interest income for the nine months ended 2016 reached ₱2.4 billion, 0.9% higher than the ₱2.3 billion generated as of September 30, 2015. Interest income on loans and other receivables grew by 2.2% from ₱1.92 billion in September 30, 2015 to ₱1.96 billion as of September 2016.

Interest expense grew by 0.7% or ₱3.6 million to ₱556.9 million for the nine-month period ending September 30, 2016. The increase was a result of the expansion of interest expense on deposit liabilities from ₱550.0 million in 2015 to ₱556.9 million this year.

As a result, net interest income expanded to ₱1.8 billion, up 1.0% from last year.

	For the nine-months ended			
	9/30/2016	9/30/2015	Variance	%
Core income				
Net interest income	₱ 1,813,011,684	₱ 1,794,771,439	₱ 18,240,245	1.0
Service charges, fees and commissions	67,865,171	65,176,256	2,688,915	4.1
Miscellaneous	72,349,741	79,822,178	(7,472,437)	(9.4)
	1,953,226,596	1,939,769,873	13,456,723	0.7
Non-interest expenses	(1,505,916,452)	(1,307,394,784)	(198,521,668)	15.2
Core income	447,310,144	632,375,089	(185,064,945)	(29.3)

Service charges, fees and commissions increased by ₱2.7 million, or 4.1% YoY and miscellaneous fees decreased by ₱7.5 million or 9.4%, which bolstered core revenue to ₱2.0 billion, up 0.7%.

At the same time, non-interest expenses grew by 15.2% YoY primarily as a result of the increase in the support function requirements from the Bank's continuing expansion of its branch network and increase in personnel. As of September 30, 2016 the bank has a total of 139 branches, an addition of one (1) branch over the second quarter, plus 12 branches via acquisitions.

As a result, core income net of operating expenses declined by 29.3% or ₱185.1 million YoY, as the Bank continued to enlarge its coverage area, causing a drag on earnings due to expansion-related expenses.

	For the nine-months ended				
	9/30/2016	9/30/2015	Variance	%	
Core income	₱ 447,310,144	₱ 632,375,089	(₱ 185,064,945)	(29.3)	
Trading gains (losses)	383,917,676	74,316,795	309,600,881	416.6	
Pre-tax pre-provision profit	831,227,820	706,691,884	124,535,936	17.6	
Loan loss provision	(60,000,000)	(90,925,000)	30,925,000	(34.0)	
Profit before tax	771,227,820	615,766,884	155,460,936	25.2	
Taxes	(101,267,100)	(143,995,792)	42,728,692	(29.7)	
Net income	669,960,720	471,771,092	198,189,628	42.0	

The Bank's trading gains amounted to ₱383.9 million this year, a 416.6% increase from ₱74.3 million over the same period last year. Pre-tax pre-provision profit reached ₱831.2 million from last year's ₱706.7 million, a 17.6% increase YoY. Net income stood at ₱670.0 million, 42.0% higher YoY from last year's ₱471.8 million.

Annualized Return on Equity (ROE) and Return on Assets (ROA) were at 9.6% and 1.4%, respectively.

For the quarters ended September 30, 2016 and June 30, 2016:

	For the quarter ended				
	9/30/2016	6/30/2016	Variance	%	
Core income					
Net interest income	₱ 594,438,950	₱ 629,124,430	(₱ 34,685,480)	(5.5)	
Service charges, fees and commissions	22,120,128	21,890,626	229,502	1.0	
Miscellaneous	30,702,328	22,809,433	7,892,895	34.6	
	647,261,406	673,824,489	(26,563,083)	(3.9)	
Non-interest expenses	(555,009,532)	(477,199,958)	(77,809,574)	16.3	
Core income	92,251,874	196,624,531	(104,372,657)	(53.1)	

Net interest income generated ₱594.4 million or a ₱34.7 million decrease from last quarter's ₱629.1 million. The decrease was mainly due to the decline of the interest income earned on investment and trading securities of 45.0% totaling ₱68.9 million in 2016 from ₱125.3 million in the last linked quarter due to the disposal of securities to capitalize on movements in the treasury market.

Service charges, fees and commissions rose by 1.0% to ₱22.1 million while miscellaneous fees grew to ₱30.7 million, a 34.6% increase.

Non-interest expenses grew by ₱77.8 million or 16.3%, primarily as a result of the Bank's continuing branch expansion plan.

	For the quarter ended			
	9/30/2016	6/30/2016	Variance	%
Core income	₱ 92,251,874	₱ 196,624,531	(₱ 104,372,657)	(53.1)
Trading gains (losses)	291,055,334	42,140,536	248,914,798	590.7
Pre-tax pre-provision profit	383,307,208	238,765,067	144,542,141	60.5
Loan loss provision	(40,000,000)	(15,000,000)	(25,000,000)	166.7
Profit before tax	343,307,208	223,765,067	119,542,141	53.4
Taxes	(13,350,959)	(45,793,227)	32,442,268	(70.8)
Net income	329,956,249	177,971,840	151,984,409	85.4

Trading gains for the third quarter reached ₱291.1 million, a 590.7% increase versus ₱42.1 million last quarter. Thus, pre-tax pre-provision profit increased by 60.5% or ₱144.5 million to ₱383.3 million.

The Bank provided an additional ₱25.0 million in provisions for the quarter. Net income was up by ₱152.0 million, or 85.4% from ₱178.0 to ₱330.0 million.

For the quarters ended September 30, 2016 and 2015:

	For the quarter ended			
	9/30/2016	9/30/2015	Variance	%
Core income				
Net interest income	₱ 594,438,950	₱ 587,213,250	₱ 7,225,700	1.2
Service charges, fees and commissions	22,120,128	22,305,866	(185,738)	(0.8)
Miscellaneous	30,702,328	51,202,553	(20,500,225)	(40.0)
	647,261,406	660,721,669	(13,460,263)	(2.0)
Non-interest expenses	(555,009,532)	(457,549,916)	(97,459,616)	21.3
Core income	92,251,874	203,171,753	(110,919,879)	(54.6)

Net interest income increased by ₱7.2 million or 1.2% compared with the same quarter last year as interest income on due from BSP and other banks expanded by ₱21.5 million, a 105.6% growth YoY to ₱41.8 million while interest expense declined by 3.3% to ₱191.3 million.

Service charges, fees and commissions decreased by ₱0.2 million or 0.8%. Miscellaneous fees reduced by 40.0% from ₱51.2 million to ₱30.7 million.

Non-interest expenses grew by ₱97.5 million, a 21.3% increase versus the same period last year. As of September 30 2016, the Bank had a total of 139 branches nationwide from 134 branches as of Year-End 2015, with additional 12 branches via acquisitions.

	For the quarter ended			
	9/30/2016	9/30/2015	Variance	%
Core income	₱ 92,251,874	₱ 203,171,753	(₱ 110,919,879)	(54.6)
Trading gains (losses)	291,055,334	26,094,347	264,960,987	1,015.4
Pre-tax pre-provision profit	383,307,208	229,266,100	154,041,108	67.2
Loan loss provision	(40,000,000)	(5,000,000)	(35,000,000)	700.0
Profit before tax	343,307,208	224,266,100	119,041,108	53.1
Taxes	(13,350,959)	(52,737,327)	39,386,368	(74.7)
Net income	329,956,249	171,528,773	158,427,476	92.4

Pre-tax pre-provision profit showed a 67.2% growth over the same quarter last year for a total of ₱383.3 million. This was due to a ₱265.0 million increase in trading gains which amounted to ₱291.1 million for the quarter versus ₱26.1 million last year.

The Bank provided an additional ₱35.0 million in provisions for the quarter. Net income was up ₱158.4 million, or 92.4% from ₱171.5 million to ₱330.0 million.

Financial condition as of September 30, 2016 versus December 31, 2015:

Amounts in Thousand Pesos	9/30/2016	12/31/2015	Variance	%
Loans and Receivables	₱ 47,347,742	₱ 41,737,830	₱ 5,609,911	13.4
Non Performing Loans (NPL)	1,704,823	1,191,600	513,223	43.1
Deposits	54,153,542	55,016,220	(862,677)	(1.6)
Assets	65,681,073	65,582,162	98,911	0.2
Equity	9,783,295	8,469,553	1,313,742	15.5

Loans and receivables increased by 13.4% from ₱41.7 billion to ₱47.3 billion as of September 30, 2016.

The bank's non-performing loans increased by ₱513.2 million bringing the Bank's non-performing loans to ₱1.7 billion as of September 30, 2016. As a result, PBB's NPL ratio increased 100 basis points from 2.8% in the same period last year to 3.8% as of September 30, 2016. The NPL ratio as of year-end 2015 was at 2.9%.

Non-performing loans increased 43.1% mainly due to the consolidation of an acquired rural bank. The valuation of the acquired rural bank factored in the ₱105.8 million in NPLs, a portion of which PBB expects to recover via restricted licenses.

Trading and investment securities decreased by 80.2% or ₱7.3 billion as the Bank capitalized on favorable trading opportunities. Investment properties decreased 13.9% from ₱675.8 million to ₱582.0 million as of 2016. Total resources grew by ₱99.0 million from ₱65.6 billion to ₱65.7 billion, up 0.2%.

On the liabilities side, deposit liabilities contracted by ₱862.7 million from ₱55.0 billion to ₱54.2 billion, down 1.6%. This was a result of the decrease in demand deposits of 60.0% from ₱2.3 billion to ₱0.9 billion as well as a decline in time deposits from ₱33.4 billion to ₱32.3 billion. However, savings deposits grew by ₱1.5 billion reaching ₱20.9 billion for the third quarter of 2016, an increase of 8.0%.

Total equity grew by ₱1.3 billion to ₱9.8 billion, up 15.5% as of September 30, 2016.

B. Key Performance Indicators

Capital Adequacy Ratio, CAR, which is a measure of a bank's financial strength, stood at 19.3% by the end of the second quarter which is 111bps higher than the previous quarter.

Asset Quality: The Bank's non-performing loans (NPL) ratio increased to 3.8% as of September 30, 2016 from 2.9% in December 31, 2015.

Profitability: Return on equity (ROE) increased from 6.1% in December 31, 2015 to 9.6% in September 30, 2015. Net interest margin remained at 4.0%.

Liquidity: The Bank's loans-to-deposit ratio as of September 30, 2016 was at 87.4% from 75.9% in December 31, 2015.

Cost efficiency: Cost-to-income ratio decreased to 64.4% as of the end of September from 67.0% in December 31, 2015.

C. Discussions on Key Variable and Other Qualitative and Quantitative Factors

Vertical and Horizontal Analysis

Financial Condition (September 30, 2016 vs. December 31, 2015)

- PBB's assets reached ₱65.7 billion as of September 30, 2016. This is slightly higher by 0.2% compared to ₱65.6 billion in December 31, 2015. Significant changes in assets were registered in the following accounts:
 - a. Cash and other cash items decreased by ₱558.5 million or 43.7%
 - b. Due from BSP increased by ₱2.4 billion or 31.6%.
 - c. Trading and Investment Securities decreased by 80.2% or ₱7.3 billion.
 - d. Loans and Other Receivables increased by 13.4% or ₱5.6 billion.
- PBB's liabilities amounted to ₱55.9 billion as of September 30, 2016. This is ₱1.2 billion or 2.1% lower as compared to the December 31, 2015 level of ₱57.1 billion, largely due from the 60.0% decrease or ₱1.4 billion in Demand Deposits.

Results of Operations for the Third quarter ended September 30, 2016 and September 30, 2015

- The Bank's core income, composed of net interest income and fee-based income, exclusive of trading gains, declined from ₱203.2 million to ₱92.3 million or a 54.6% decrease. PBB posted a ₱330.0 million net income for the third quarter ending September 30, 2016. This is a 92.4% or ₱158.4 million increase compared to the same quarter last year. The increase was due to the 1,015.4% growth in trading gains resulting in ₱291.1 million from ₱26.1 million over the quarter last year.
- Interest income on investment and trading securities weakened by 61.8% to ₱68.9 million for the third quarter of 2016 from ₱180.6 million for the third quarter of 2015. Total interest income grew by 0.1% or ₱0.7 million compared to the same period last year.
- Service charges, fees and commissions decreased by 0.8% from ₱22.3 million in the third quarter of 2015 to ₱22.1 million for the same period this year resulting from a decrease in the volume of transaction of consumer lending.
- Miscellaneous income declined in the third quarter of 2016 from ₱51.2 million in 2015 to ₱30.7 million in the same period of 2016.
- Manpower costs continued to rise from ₱134.0 million for the third quarter of 2015 to ₱154.9 million in the same quarter this year on account of business expansion and a larger branch network.

Significant Elements of Income or Loss

Significant elements of the net income of the Bank for the period ended September 30, 2016 came from its operations. A significant portion came from the core business of interest income on loans and trading gains/losses from the sale of Peso securities.

Known trends, demands, commitments, events or uncertainties

There are no known demands, commitments, events or uncertainties that will have a material impact on the Bank's liquidity within the next twelve (12) months.

Events that will trigger direct or contingent financial obligation

There are no events that will trigger direct or contingent financial obligation that is material to the Bank, including any default or acceleration of an obligation.

Material off-balance sheet transactions, arrangements or obligations

There are no material off-balance sheet transactions, arrangements, obligations (including contingent obligations), and other relationships of the Bank with unsolicited entities or other persons created during the reporting period other than those disclosed in the financial statements.

Significant Elements of Income or Loss

Significant elements of the consolidated net income for the nine months period ended September 30, 2016 and 2015 came from its continuing operations.

Seasonal Aspects

There are no seasonal aspects that had a material effect on the Bank's financial position and results of operations.

Attachment 1

PHILIPPINE BUSINESS BANK, INC.

As of September 30, 2016 (Unaudited) and December 31, 2015 (Audited)

And for the Nine Months Ended September 30, 2016 and 2015 (Unaudited)

PHILIPPINE BUSINESS BANK, INC. A SAVINGS BANK
UNAUDITED STATEMENTS OF FINANCIAL POSITION
SEPTEMBER 30, 2016 AND DECEMBER 31, 2015
(Amounts in Philippine Pesos)

	<u>Unaudited</u> <u>September 30, 2016</u>	<u>Audited</u> <u>December 31, 2015</u>
<u>RESOURCES</u>		
CASH AND OTHER CASH ITEMS	P 720,752,350	P 1,279,302,155
DUE FROM BANGKO SENTRAL NG PILIPINAS	10,096,216,628	7,672,637,783
DUE FROM OTHER BANKS	2,881,963,420	2,825,982,401
TRADING AND INVESTMENT SECURITIES		
At Fair Value Through Profit or Loss	246,969,885	75,942,639
Available-For-Sale	1,558,027,874	3,094,538,311
Held-To-Maturity	-	5,948,727,495
LOANS AND OTHER RECEIVABLES - Net	47,347,741,645	41,737,830,222
BANK PREMISES, FURNITURE, FIXTURES AND EQUIPMENT - Net	548,852,674	562,634,722
INVESTMENT PROPERTIES - Net	582,036,710	675,770,624
OTHER RESOURCES - Net	<u>1,698,511,719</u>	<u>1,708,795,604</u>
TOTAL RESOURCES	<u>P 65,681,072,905</u>	<u>P 65,582,161,956</u>
<u>LIABILITIES AND EQUITY</u>		
DEPOSIT LIABILITIES		
Demand	P 927,384,452	P 2,318,743,667
Savings	20,893,375,910	19,346,525,011
Time	<u>32,332,781,722</u>	<u>33,350,950,832</u>
Total Deposit Liabilities	54,153,542,084	55,016,219,510
BILLS PAYABLE	-	956,250
ACCRUED EXPENSES AND OTHER LIABILITIES	<u>1,744,236,102</u>	<u>2,095,433,359</u>
Total Liabilities	55,897,778,186	57,112,609,119
EQUITY	<u>9,783,294,719</u>	<u>8,469,552,837</u>
TOTAL LIABILITIES AND EQUITY	<u>P 65,681,072,905</u>	<u>P 65,582,161,956</u>

PHILIPPINE BUSINESS BANK, INC. A SAVINGS BANK
UNAUDITED STATEMENTS OF INCOME
FOR NINE MONTHS PERIOD ENDED SEPTEMBER 30, 2016 AND SEPTEMBER 30, 2015
(Amounts in Philippine Pesos)

	<u>For the quarter</u> <u>ended Sept. 30, 2016</u>	<u>For the quarter</u> <u>ended Sept. 30, 2015</u>	<u>Unaudited</u> <u>For nine months</u> <u>ended Sept. 30, 2016</u>	<u>Unaudited</u> <u>For nine months</u> <u>ended Sept. 30, 2015</u>
INTEREST INCOME				
Loans and other receivables	P 659,627,721	P 584,087,964	P 1,957,817,676	P 1,915,773,881
Investment and trading securities	68,896,376	180,585,951	319,383,414	384,741,615
Securities purchased under reverse repurchase agreements	15,336,740	-	16,985,269	-
Due from Bangko Sentral ng Pilipinas and other banks	<u>41,845,005</u>	<u>20,353,197</u>	<u>75,762,590</u>	<u>47,574,463</u>
	<u>785,705,842</u>	<u>785,027,112</u>	<u>2,369,948,949</u>	<u>2,348,089,959</u>
INTEREST EXPENSE				
Deposit liabilities	191,266,892	197,753,502	556,924,479	550,020,827
Bills payable	<u>-</u>	<u>60,360</u>	<u>12,786</u>	<u>3,297,693</u>
	<u>191,266,892</u>	<u>197,813,862</u>	<u>556,937,265</u>	<u>553,318,520</u>
NET INTEREST INCOME	594,438,950	587,213,250	1,813,011,684	1,794,771,439
IMPAIRMENT LOSSES	<u>40,000,000</u>	<u>5,000,000</u>	<u>60,000,000</u>	<u>90,925,000</u>
NET INTEREST INCOME AFTER IMPAIRMENT LOSSES	<u>554,438,950</u>	<u>582,213,250</u>	<u>1,753,011,684</u>	<u>1,703,846,439</u>
OTHER INCOME				
Trading gains - net	291,055,334	26,094,347	383,917,676	74,316,795
Service charges, fees and commissions	22,120,128	22,305,866	67,865,171	65,176,256
Miscellaneous	<u>30,702,328</u>	<u>51,202,553</u>	<u>72,349,741</u>	<u>79,822,178</u>
	<u>343,877,790</u>	<u>99,602,766</u>	<u>524,132,588</u>	<u>219,315,229</u>
OTHER EXPENSES				
Salaries and other employee benefits	154,877,712	134,027,670	454,721,935	393,984,692
Taxes and licenses	116,526,517	77,402,067	292,481,121	241,938,172
Management and other professional fees	51,065,202	25,333,672	98,206,261	73,035,355
Depreciation and amortization	46,556,030	39,832,831	130,720,384	113,720,085
Insurance	36,427,929	35,068,438	103,232,245	94,434,179
Representation and entertainment	7,909,881	7,484,013	22,717,311	22,229,674
Miscellaneous	<u>141,646,261</u>	<u>138,401,225</u>	<u>403,837,195</u>	<u>368,052,627</u>
	<u>555,009,532</u>	<u>457,549,916</u>	<u>1,505,916,452</u>	<u>1,307,394,784</u>
PROFIT BEFORE TAX	343,307,208	224,266,100	771,227,820	615,766,884
TAX EXPENSE	<u>13,350,959</u>	<u>52,737,327</u>	<u>101,267,100</u>	<u>143,995,792</u>
NET PROFIT	<u>P 329,956,249</u>	<u>P 171,528,773</u>	<u>P 669,960,720</u>	<u>P 471,771,092</u>
Earnings Per Share				
Basic			<u>P 1.25</u>	<u>P 0.88</u>
Diluted			<u>P 1.25</u>	<u>P 0.88</u>

PHILIPPINE BUSINESS BANK, INC. A SAVINGS BANK
 UNAUDITED STATEMENTS OF COMPREHENSIVE INCOME
 FOR NINE MONTHS PERIOD ENDED SEPTEMBER 30, 2016, AND SEPTEMBER 30, 2015
 (Amounts in Philippine Pesos)

	<u>For the quarter</u> <u>ended Sept. 30, 2016</u>	<u>For the quarter</u> <u>ended Sept. 30, 2015</u>	<u>Unaudited</u> <u>For the six months</u> <u>ended Sept. 30, 2016</u>	<u>Unaudited</u> <u>For the six months</u> <u>ended Sept. 30, 2015</u>
NET PROFIT	<u>P 329,956,249</u>	<u>P 171,528,773</u>	<u>P 669,960,720</u>	<u>P 471,771,092</u>
OTHER COMPREHENSIVE INCOME				
Fair value gains (losses) on available-for-sale securities during the year - net	38,816,451	(410,524)	573,590,523	(188,780)
Fair value gains (losses) reclassified to profit or loss	24,337,847	(88,254,345)	64,714,941	(31,009,613)
Amortization of fair value loss on reclassified securities	(<u>2,924,747</u>)	(<u>8,731,995</u>)	<u>-</u>	(<u>6,043,316</u>)
	<u>60,229,551</u>	(<u>97,396,864</u>)	<u>638,305,464</u>	(<u>37,241,709</u>)
TOTAL COMPREHENSIVE INCOME	<u>P 390,185,800</u>	<u>P 74,131,909</u>	<u>P 1,308,266,184</u>	<u>P 434,529,383</u>

PHILIPPINE BUSINESS BANK, INC. A SAVINGS BANK
 UNAUDITED STATEMENTS OF CHANGES IN EQUITY
 FOR NINE MONTHS PERIOD ENDED SEPTEMBER 30, 2016, AND SEPTEMBER 30, 2015
 (Amounts in Philippine Pesos)

	Capital Stock		Additional Paid-in Capital	Surplus		Unrealized Fair Value Gains (Losses) on Available-for-sale Securities	Accumulated Actuarial Gains (Losses)	Total Equity
	Preferred Stock	Common Stock		Appropriated	Unappropriated			
BALANCE AS OF JANUARY 1, 2016	P 620,000,000	P 5,364,584,370	P 1,998,396,816	P 4,799,387	P 1,087,656,779	(P 577,298,405)	(P 28,586,105)	P 8,469,552,842
Prior period adjustment	-	-	-	-	5,475,687	-	-	P 5,475,687
Proceeds from capital stock issuance	-	-	-	-	-	-	-	-
Stock dividends	-	-	-	-	-	-	-	-
Cash dividends	-	-	-	-	-	-	-	-
Total comprehensive income (loss)	-	-	-	-	669,960,720	638,305,464	-	1,308,266,184
BALANCE AS OF SEPTEMBER 30, 2016	P 620,000,000	P 5,364,584,370	P 1,998,396,816	P 4,799,387	P 1,763,093,186	P 61,007,059	(P 28,586,105)	P 9,783,294,713
BALANCE AS OF JANUARY 1, 2015	P 620,000,000	P 4,291,667,500	P 1,998,396,816	P 3,411,900	P 1,659,819,127	(P 519,742,021)	(P 31,186,830)	P 8,022,366,492
Prior period adjustment	-	-	-	-	(11,937,800)	-	-	(P 11,937,800)
Proceeds from capital stock issuance	-	-	-	-	-	-	-	-
Stock dividends	-	-	-	-	-	-	-	-
Cash dividends	-	-	-	-	-	-	-	-
Total comprehensive income (loss)	-	-	-	-	471,771,092	(66,792,316)	-	404,978,776
BALANCE AS OF SEPTEMBER 30, 2015	P 620,000,000	P 4,291,667,500	P 1,998,396,816	P 3,411,900	P 2,119,652,419	(P 586,534,337)	(P 31,186,830)	P 8,415,407,468

PHILIPPINE BUSINESS BANK, INC. A SAVINGS BANK
UNAUDITED STATEMENTS OF CASH FLOWS
FOR NINE MONTHS PERIOD ENDED SEPTEMBER 30, 2016, AND SEPTEMBER 30, 2015
(Amounts in Philippine Pesos)

	<u>2016</u>	<u>2015</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Profit before tax	P 771,227,820	P 615,766,884
Adjustments for:		
Depreciation and amortization	130,720,384	113,720,085
Impairment losses	60,000,000	90,925,000
	<u>-</u>	<u>-</u>
Operating profit before working capital changes	961,948,204	820,411,969
Increase in financial assets at fair value through profit or loss	(171,027,246)	(853,107,871)
Decrease (increase) in hold-to-maturity	5,948,727,495	(164,000,224)
Increase in loans and other receivables	(5,669,911,423)	77,249,903
Decrease (increase) in other resources	28,283,885	(928,860,121)
Increase in deposit liabilities	(862,677,426)	5,032,079,524
Increase in accrued expenses and other liabilities	(312,392,409)	(384,983,103)
Increase in capital accounts	<u>-</u>	<u>-</u>
Cash generated from (used in) operations	(77,048,920)	3,598,790,077
Cash paid for income taxes	(<u>158,071,948</u>)	(<u>190,296,913</u>)
Net Cash From (Used in) Operating Activities	(<u>235,120,868</u>)	<u>3,408,493,164</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Acquisition of available-for-sale (AFS) securities	113,555,858	2,106,373,672
Proceeds from sale of AFS securities	2,061,260,044	(3,371,599,345)
Proceeds from sale of investment and other properties	99,209,611	41,389,071
Net acquisitions of bank premises, furniture, fixtures and equipment	(116,938,336)	(147,139,576)
	<u>-</u>	<u>-</u>
Net Cash From (Used In) Investing Activities	<u>2,157,087,177</u>	(<u>1,370,976,178</u>)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net borrowings (payments) of bills payable	(956,250)	(306,666,697)
	<u>-</u>	<u>-</u>
Net Cash From (Used in) Financing Activities	(<u>956,250</u>)	(<u>306,666,697</u>)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS		
	<u>1,921,010,059</u>	<u>1,730,850,289</u>
CASH AND CASH EQUIVALENTS AT BEGINNING OF THE YEAR		
Cash and other cash items	1,279,302,155	1,174,011,464
Due from Bangko Sentral ng Pilipinas	7,672,637,783	4,554,441,827
Due from other banks	2,825,982,401	2,031,581,088
Securities purchased under reverse repurchase agreements	<u>-</u>	<u>-</u>
	<u>11,777,922,339</u>	<u>7,760,034,379</u>
CASH AND CASH EQUIVALENTS AT END OF THE YEAR		
Cash and other cash items	720,752,350	903,931,241
Due from Bangko Sentral ng Pilipinas	10,096,216,628	5,583,004,326
Due from other banks	2,881,963,420	3,003,949,101
Securities purchased under reverse repurchase agreements	<u>-</u>	<u>-</u>
SEC Form 17-Q		
Philippine Business Bank	<u>P 13,698,932,398</u>	<u>P 9,490,884,668</u>

PHILIPPINE BUSINESS BANK, INC., A SAVINGS BANK
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND DECEMBER 31, 2015
(Amounts in Philippine Pesos or As Otherwise Indicated)

1. CORPORATE MATTERS

1.1 Incorporation and Operations

Philippine Business Bank, Inc., A Savings Bank (the Bank or PBB) was incorporated in the Philippines on January 28, 1997 to engage in the business of thrift banking. It was authorized to engage in foreign currency deposit operations on August 27, 1997 and in trust operations on November 13, 2003. As a banking institution, the Bank's operations are regulated and supervised by the Bangko Sentral ng Pilipinas (BSP). In this regard, the Bank is required to comply with rules and regulations of the BSP such as those relating to maintenance of reserve requirements on deposit liabilities and those relating to adoption and use of safe and sound banking practices, among others, as promulgated by the BSP. The Bank's activities are subject to the provisions of the General Banking Law of 2000 (Republic Act No. 8791) and other relevant laws. On April 1, 2010, PBB is the first savings bank in the Philippines that obtained the BSP approval to issue foreign letters of credit and pay/accept/negotiate import/export drafts/bills of exchange under Republic Act Nos. 8791 and 7906 and the Manual of Regulations for Banks.

On January 9, 2013, the Philippine Stock Exchange (PSE) approved the Bank's application for the listing of its common shares. The approval covered the initial public offering (IPO) of 101,333,400 unissued common shares of the Bank at P31.50 per share and the listing of those shares in the PSE's main board on February 19, 2013 (see Note 16.1).

As of September 30, 2016 and December 31, 2015, the Bank operates within the Philippines with 151 and 134 branches, respectively, located nationwide.

The Bank's registered address, which is also its principal place of business, is at 350 Rizal Avenue Extension corner 8th Avenue, Grace Park, Caloocan City.

1.2 Approval of the Financial Statements

The financial statements of the Bank as of and for the quarter ended September 30, 2016 (including the comparative financial statements as of December 31, 2015 and for the years ended September 30, 2016 and September 30, 2015) were authorized for issue by the Bank's Board of Directors (BOD) on April 13, 2016.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies that have been used in the preparation of these financial statements are summarized below and in the succeeding pages. These policies have been consistently applied to all the years presented, unless otherwise stated.

2.1 Basis of Preparation of Financial Statements

a. Statement of Compliance with Philippine Financial Reporting Standards

The financial statements of the Bank have been prepared in accordance with Philippine Financial Reporting Standards (PFRS). PFRS are adopted by the Financial Reporting Standards Council (FRSC), from the pronouncements issued by the International Accounting Standards Board, and approved by the Philippine Board of Accountancy.

The financial statements have been prepared using the measurement bases specified by PFRS for each type of asset, liability, income and expense. The measurement bases are more fully described in the accounting policies that follow.

b. Presentation of Financial Statements

The financial statements are presented in accordance with Philippine Accounting Standard (PAS) 1, *Presentation of Financial Statements*. The Bank presents a statement of comprehensive income separate from the statement of profit or loss.

The Bank presents a third statement of financial position as at the beginning of the preceding period when it applies an accounting policy retrospectively, or makes a retrospective restatement or reclassification of items that has a material effect on the information in the statement of financial position at the beginning of the preceding period. The related notes to the third statement of financial position are not required to be disclosed.

c. Functional and Presentation Currency

These financial statements are presented in Philippine pesos, the Bank's functional and presentation currency, and all values represent absolute amounts except when otherwise indicated.

Items included in the financial statements of the Bank are measured using its functional currency. Functional currency is the currency of the primary economic environment in which the Bank operates. The financial statements of the Bank's foreign currency deposit unit (FCDU) which is reported in its functional currency, the United States (US) dollar, are translated to Philippine peso based on Philippine Dealing System closing rates (PDSCR) at the end of reporting period (for the statement of financial position accounts) and at the average PDSCR for the period (for profit and loss accounts).

2.2 Adoption of New and Amended PFRS

a. Effective in 2015 that are Relevant to the Bank

In 2015, the Bank adopted for the first time the following amendment and annual improvements to PFRS which are mandatorily effective for annual periods on or after July 1, 2014 for the Bank's annual reporting period beginning January 1, 2015:

PAS 19 (Amendment)	:	Employee Benefits – Defined Benefit Plans – Employee Contributions
Annual Improvements	:	Annual Improvements to PFRS (2010-2012 Cycle) and PFRS (2011-2013 Cycle)

Discussed below are the relevant information about these amended standard and improvements.

- i. PAS 19 (Amendment), Employee Benefits – Defined Benefit Plans – Employee Contributions. The amendment clarifies that if the amount of the contributions to defined benefit plans from employees or third parties is dependent on the number of years of service, an entity shall attribute the contributions to periods of service using the same attribution method (i.e., either using the plan's contribution formula or on a straight-line basis) for the gross benefit. The amendment did not have a significant impact on the Bank's financial statements since the Bank's defined benefit plan does not require employees or third parties to contribute to the benefit plan.
- ii. Annual Improvements to PFRS. Annual improvements to PFRS (2010-2012 Cycle) and PFRS (2011-2013 Cycle) made minor amendments to a number of PFRS. Among those improvements, the following amendments are relevant to the Bank but had no material impact on the Bank's financial statements as these amendments merely clarify the existing requirements:

Annual Improvements to PFRS (2010-2012 Cycle)

- PFRS 3 (Amendment), Business Combinations. The amendment clarifies that an obligation to pay contingent consideration which meets the definition of a financial instrument is classified as a financial liability or as equity in accordance with PAS 32, Financial Instruments – Presentation. It also clarifies that all non-equity contingent consideration should be measured at fair value at the end of each reporting period, with changes in fair value recognized in profit or loss.
- PFRS 8 (Amendment), Operating Segments. The amendment requires disclosure of the judgments made by management in applying the aggregation criteria to operating segments. This includes

a description of the segments which have been aggregated and the economic indicators which have been assessed in determining that the aggregated segments share similar economic characteristics. It further clarifies the requirement to disclose for the reconciliations of segment assets to the entity's assets if that amount is regularly provided to the chief operating decision maker.

- PAS 16 (Amendment), Property, Plant and Equipment and PAS 38 (Amendment), Intangible Assets. The amendments clarify that when an item of property, plant and equipment and intangible assets is revalued, the gross carrying amount is adjusted in a manner that is consistent with a revaluation of the carrying amount of the asset.
- PAS 24 (Amendment), Related Party Disclosures. The amendment clarifies that an entity providing key management services to a reporting entity is deemed to be a related party of the latter. It also clarifies that the information required to be disclosed in the financial statements are the amounts incurred by the reporting entity for key management personnel services that are provided by a separate management entity and not the amounts of compensation paid or payable by the management entity to its employees or directors.

Annual Improvements to PFRS (2011-2013 Cycle)

- PFRS 3 (Amendment), Business Combinations. It clarifies that PFRS 3 does not apply to the accounting for the formation of any joint arrangement under PFRS 11, Joint Arrangement, in the financial statements of the joint arrangement itself.
- PFRS 13 (Amendment), Fair Value Measurement. The amendment clarifies that the scope of the exception for measuring the fair value of a group of financial assets and financial liabilities on a net basis (the portfolio exception) applies to all contracts within the scope of and accounted for in accordance with PAS 39, Financial Instruments: Recognition and Measurement, or PFRS 9, Financial Instruments, regardless of whether they meet the definition of financial assets or financial liabilities as defined in PAS 32.
- PAS 40 (Amendment), Investment Property. The amendment clarifies the interrelationship of PFRS 3 and PAS 40 in determining the classification of property as an investment property or owner-occupied property, and explicitly requires an entity to use judgment in determining whether the acquisition of an investment property is an acquisition of an asset or a group of asset in accordance with PAS 40 or a business combination in accordance with PFRS 3.

b. Effective in 2015 that are not Relevant to the Bank

Among the annual improvements to PFRS, which are mandatory for accounting

periods beginning on or after July 1, 2014, only PFRS 2 (Amendment), Shared-based Payment – Definition of Vesting Condition is not relevant to the Bank's financial statements.

c. Effective Subsequent to 2015 but not Adopted Early

There are new PFRS, amendments and annual improvements to existing standards effective for annual periods subsequent to 2015, which are adopted by the FRSC, Management will adopt the following relevant pronouncements in accordance with their transitional provisions and; unless otherwise stated, none of these are expected to have significant impact on the Bank's financial statements:

- i. PAS 1 (Amendment), *Presentation of Financial Statements – Disclosure Initiative* (effective from January 1, 2016). The amendment encourages entities to apply professional judgment in presenting and disclosing information in the financial statements. Accordingly, it clarifies that materiality applies to the whole financial statements and an entity shall not reduce the understandability of the financial statements by obscuring material information with immaterial information or by aggregating material items that have different natures or functions. It further clarifies that in determining the order of presenting the notes and disclosures, an entity shall consider the understandability and comparability of the financial statements.
- ii. PAS 16 (Amendment), Property, Plant and Equipment and PAS 38 (Amendment), *Intangible Assets – Clarification of Acceptable Methods of Depreciation and Amortization* (effective from January 1, 2016). The amendment in PAS 16 clarifies that a depreciation method that is based on revenue that is generated by an activity that includes the use of an asset is not appropriate for property, plant and equipment. In addition, amendment to PAS 38 introduces a rebuttable presumption that an amortization method that is based on the revenue generated by an activity that includes the use of an intangible asset is not appropriate, which can only be overcome in limited circumstances where the intangible asset is expressed as a measure of revenue, or when it can be demonstrated that revenue and the consumption of the economic benefits of an intangible asset are highly correlated.
- iii. PFRS 11 (Amendment), *Joint Arrangements – Accounting for Acquisitions of Interests in Joint Operations* (effective from January 1, 2016). This amendment requires the acquirer of an interest in a joint operation in which the activity constitutes a business as defined in PFRS 3 to apply all accounting principles and disclosure requirements on business combinations under PFRS 3 and other PFRSs, except for those principles that conflict with the guidance in PFRS 11.

- iv. PFRS 9 (2014), *Financial Instruments* (effective from January 1, 2018). This new standard on financial instruments will eventually replace PAS 39 and PFRS 9 (2009, 2010 and 2013 versions). This standard contains, among others, the following:
- three principal classification categories for financial assets based on the business model on how an entity is managing its financial instruments;
 - an expected loss model in determining impairment of all financial assets that are not measured at fair value through profit or loss (FVTPL), which generally depends on whether there has been a significant increase in credit risk since initial recognition of a financial asset; and,
 - a new model on hedge accounting that provides significant improvements principally by aligning hedge accounting more closely with the risk management activities undertaken by entities when hedging their financial and non-financial risk exposures.

In accordance with the financial asset classification principle of PFRS 9 (2014), a financial asset is classified and measured at amortized cost if the asset is held within a business model whose objective is to hold financial assets in order to collect the contractual cash flows that represent solely payments of principal and interest (SPPI) on the principal outstanding. Moreover, a financial asset is classified and subsequently measured at fair value through other comprehensive income if it meets the SPPI criterion and is held in a business model whose objective is achieved by both collecting contractual cash flows and selling the financial assets. All other financial assets are measured at FVTPL.

In addition, PFRS 9 (2014) allows entities to make an irrevocable election to present subsequent changes in the fair value of an equity instrument that is not held for trading in other comprehensive income.

The accounting for embedded derivatives in host contracts that are financial assets is simplified by removing the requirement to consider whether or not they are closely related, and, in most arrangements, does not require separation from the host contract.

For liabilities, the standard retains most of the PAS 39 requirements, which include amortized cost accounting for most financial liabilities, with bifurcation of embedded derivatives. The amendment also requires changes in the fair value of an entity's own debt instruments caused by changes in its own credit quality to be recognized in other comprehensive income rather than in profit or loss.

The Bank is currently assessing the impact of PFRS 9 (2014) on the financial statements of the Bank to determine whether the effect of PFRS 9 (2014) is significant or not to the financial statements and it is conducting a comprehensive study of the potential impact of this standard to the financial statements and operations of the Bank prior to its mandatory adoption date.

- v. Annual Improvements to PFRS (2012-2014 Cycle) effective for annual periods beginning on or after January 1, 2016. Among those improvements, the following amendments are relevant to the Bank but management does not expect those to have material impact on the Bank's financial statements:
- PFRS 5 (Amendment), *Non-current Assets Held for Sale and Discontinued Operations*. The amendment clarifies that when an entity reclassifies an asset (or disposal group) directly from being held for sale to being held for distribution (or vice-versa), the accounting guidance in paragraphs 27-29 of PFRS 5 does not apply. It also states that when an entity determines that the asset (or disposal group) is no longer available for immediate distribution or that the distribution is no longer highly probable, it should cease held-for-distribution accounting and apply the guidance in paragraphs 27-29 of PFRS 5.
 - PFRS 7 (Amendment), *Financial Instruments – Disclosures*. The amendment provides additional guidance to help entities identify the circumstances under which a contract to “service” financial assets is considered to be a continuing involvement in those assets for the purposes of applying the disclosure requirements of PFRS 7. Such circumstances commonly arise when, for example, the servicing is dependent on the amount or timing of cash flows collected from the transferred asset or when a fixed fee is not paid in full due to non-performance of that asset.
 - PAS 19 (Amendment), *Employee Benefits*. The amendment clarifies that the currency and term of the high quality corporate bonds which were used to determine the discount rate for post-employment benefit obligations shall be made consistent with the currency and estimated term of the post-employment benefit obligations

2.3 Business Combinations

Business acquisitions are accounted for using the acquisition method of accounting.

Goodwill acquired in a business combination is initially measured at cost being the excess of the cost of a business combination over the Bank's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the acquired entity or net assets.

Subsequent to initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed (see Note 2.19).

Negative goodwill which is the excess of the Bank's interest in the net fair value of net identifiable assets acquired over acquisition cost is charged directly to profit or loss.

For the purpose of impairment testing, goodwill is allocated to cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose. The cash-generating units or groups of cash-generating units are identified according to operating segment.

If the business combination is achieved in stages, the acquirer is required to remeasure its previously held equity interest in the acquiree at its acquisition-date fair value and recognize the resulting gain or loss, if any, in profit or loss or other comprehensive income, as appropriate.

Any contingent consideration to be transferred by the Bank is recognized at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration that is deemed to be an asset or liability is recognized in accordance with PAS 37, Provision, Contingent Liabilities and Contingent Assets, either in profit or loss or as a change to other comprehensive income. Contingent consideration that is classified as equity is not remeasured, and its subsequent settlement is accounted for within equity.

2.4 Segment Reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the Bank's chief operating decision-maker. The chief operating decision maker is responsible for allocating resources and assessing performance of the operating segments.

In identifying its operating segments, management generally follows the Bank's products and services as disclosed in Note 7.

Each of these operating segments is managed separately as each of these services requires different technologies and resources as well as marketing approaches. All inter-segment transfers are carried out at arm's length prices.

The measurement policies of the Bank used for segment reporting under PFRS 8 is the same as those used in its financial statements. In addition, corporate resources which are not directly attributable to the business activities of any operating segment are not allocated to a segment.

There have been no changes from prior periods in the measurement methods used to determine reported segment profit or loss.

The Bank's operations are organized according to the nature of the products and services provided. Financial performance on operating segments is presented in Note

2.5 Financial Assets

Financial assets are recognized when the Bank becomes a party to the contractual terms of the financial instrument. For purposes of classifying financial assets, an instrument is considered as an equity instrument if it is non-derivative and meets the definition of an equity for the issuer in accordance with the criteria under PAS 32. All other non-derivative financial instruments are treated as debt instruments.

a. Classification, Measurement and Reclassification of Financial Assets

Financial assets, other than those designated and effective as hedging instruments, are classified into the following categories: financial assets at FVTPL, loans and receivables, held-to-maturity (HTM) investments and available-for-sale (AFS) securities. Financial assets are assigned to the different categories by management on initial recognition, depending on the purpose for which the investments were acquired. Except for derivative financial instruments and financial assets designated at FVTPL, the designation of financial assets is re-evaluated at the end of each reporting period and at which date, a choice of classification or accounting treatment is available which is subject to compliance with specific provisions of applicable accounting standards.

Regular purchases and sales of financial assets are recognized on their settlement date. All financial assets that are not classified as at FVTPL are initially recognized at fair value, plus any directly attributable transaction costs. Financial assets carried at FVTPL are initially recorded at fair value and the related transaction costs are recognized in profit or loss.

A more detailed description of the four categories of financial assets is as follows

i. Financial Assets at FVTPL

This category includes financial assets that are either classified as held for trading or that meets certain conditions and are designated by the Bank to be carried at FVTPL upon initial recognition. All derivatives fall into this category, except for those designated and effective as hedging instruments.

Financial assets at FVTPL are measured at fair value, and changes therein are recognized in profit or loss. Financial assets (except derivatives and financial instruments originally designated as financial assets at FVTPL) may be reclassified out of fair value through profit or loss category if they are no longer held for the purpose of being sold or repurchased in the near term.

ii. Loans and Receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Bank provides money or services directly to a debtor with no intention of trading the receivables. Included in this category are financial assets arising from direct loans to customers, securities purchased under

reverse repurchase agreements (SPURRA), unquoted debt securities, sales contract receivables and all receivables from customers and other banks.

The Bank's financial assets categorized as loans and receivables are presented as Cash and Other Cash Items, Due from BSP, Due from Other Banks, Loans and Other Receivables, and Other Resources (specifically Security deposits, Petty cash fund and Foreign currency notes and coins on hand) in the statement of financial position. For purposes of reporting cash flows, cash and cash equivalents include cash and other cash items, due from BSP and other banks and SPURRA.

Loans and receivables are subsequently measured at amortized cost using the effective interest method, less impairment losses, if any.

iii. HTM Investments

This includes non-derivative financial assets with fixed or determinable payments and a fixed date of maturity. Investments are classified as HTM if the Bank has the positive intention and ability to hold them until maturity. Investments intended to be held for an undefined period are not included in this classification.

If the Bank were to sell other than an insignificant amount of HTM investments, the whole category would be tainted and reclassified to AFS securities under PFRS, and the Bank will be prohibited from holding investments under the HTM investments category for the next two financial reporting years after the year the tainting occurred. The tainting provision under PFRS will not apply if the sales or reclassifications of HTM investments are so close to maturity or the financial asset's call date that changes in the market rate of interest would not have a significant effect on the financial asset's fair value; occur after the Bank has collected substantially all of the financial asset's original principal through scheduled payments or prepayments; or are attributable to an isolated event that is beyond the control of the Bank, is nonrecurring and could not have been reasonably anticipated by the Bank. The Bank currently holds listed sovereign bonds and corporate bonds designated into this category.

Subsequent to initial recognition, the HTM investments are measured at amortized cost using the effective interest method, less impairment losses, if any.

iv. AFS Securities

This category includes non-derivative financial assets that are either designated to this category or do not qualify for inclusion in any of the other categories of financial assets. The Bank's AFS securities include government securities, corporate bonds and equity securities.

All financial assets within this category are subsequently measured at fair value. Gains and losses from changes in fair value are recognized in other

comprehensive income and are reported as part of the Revaluation Reserves account in equity, except for interest and dividend income, impairment losses and foreign exchange differences on monetary assets, which are recognized in profit or loss.

When the financial asset is disposed of or is determined to be impaired, the cumulative fair value gains or losses recognized in other comprehensive income is reclassified from equity to profit or loss and is presented as reclassification adjustment within other comprehensive income even though the financial assets has not been derecognized.

b. Impairment of Financial Assets

The Bank assesses at each reporting date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses 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 (a loss event) and that loss event (events) has (have) an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Objective evidence that a financial asset or group of assets is impaired includes observable data that comes to the attention of the Bank about certain loss events, including, among others: (i) significant financial difficulty of the issuer or debtor; (ii) a breach of contract, such as a default or delinquency in interest or principal payments; (iii) it is probable that the borrower will enter bankruptcy or other financial reorganization; (iv) the disappearance of an active market for that financial asset because of financial difficulties; or, (v) observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group.

i. Carried at Amortized Cost – Loans and Receivables and HTM Investments

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

If there is objective evidence that an impairment loss on loans and other receivables or HTM investments carried at amortized cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit loss that have not been incurred) discounted at the

financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognized in profit or loss. If loans and other receivables or HTM investments have a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the Bank may measure impairment on the basis of an instrument's fair value using an observable market price. The calculation of the present value of the estimated future cash flows of a collateralized financial asset reflects the cash flows that may result from foreclosures less costs for obtaining and selling the collateral, whether or not the foreclosure is probable.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (i.e., on the basis of the Bank's grading process that considers asset type, industry, geographical location, collateral type, past due status and other relevant factors). Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the Bank and historical loss experience for assets with credit risk characteristics similar to those in the Bank. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently.

Estimates of changes in future cash flows for groups of assets should reflect and be directionally consistent with changes in related observable data from period to period (for example, changes in unemployment rates, property prices, payment status, or other factors indicative of changes in the probability of losses in the group and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Bank to reduce any differences between loss estimates and actual loss experience.

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, including approval from the management and the BOD, 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 profit or loss.

If in a subsequent period, the amount of the impairment loss decreases and the decrease can be objectively related to an event occurring after the impairment was recognized (such as an improvement in the debtor's credit rating), the previously recognized impairment loss is reversed by adjusting

the allowance account. The reversal shall not result in a carrying amount of the financial asset that exceeds what the amortized cost would have been had the impairment not been recognized at the date of the impairment is reversed. The amount of the reversal is recognized in profit or loss.

When possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due. Management continuously reviews restructured loans to ensure that all criteria are met and that future payments are likely to occur.

ii. Carried at Fair Value – AFS Financial Assets

The Bank assesses at the end of each reporting period whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity investments classified as AFS securities, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exists for AFS securities, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognized in profit or loss – is removed from equity and recognized in profit or loss.

Impairment losses recognized in the statement of profit or loss on equity instruments are not reversed through profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as AFS securities increases and the increase can be objectively related to an event occurring after the impairment loss was recognized the impairment loss is reversed through profit or loss.

Reversal of impairment losses is recognized in other comprehensive income, except for financial assets that are debt securities which are recognized in profit or loss only if the reversal can be objectively related to an event occurring after the impairment loss was recognized.

iii. Carried at Cost – AFS Financial Assets

The Bank assesses at the end of each reporting period whether there is objective evidence that any of the unquoted equity securities which are carried at cost, may be impaired. The amount of impairment loss is the difference between the carrying amount of the equity security and the present value of the estimated future cash flows discounted at the current market rate of return of a similar asset. Impairment losses on assets carried at cost cannot be reversed.

c. Items of Income and Expense Related to Financial Assets

All income and expenses, including impairment losses relating to financial assets are recognized in the statement of profit or loss.

Non-compounding interest and other cash flows resulting from holding financial assets are recognized in profit or loss when earned, regardless of how the related carrying amount of financial assets is measured.

d. **Derecognition of Financial Assets**

The financial assets are derecognized when the contractual rights to receive cash flows from the financial instruments expire, or when the financial assets and all substantial risks and rewards of ownership have been transferred to another party. If the Bank neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Bank recognizes its retained interest in the asset and an associated liability for amounts it may have to pay. If the Bank retains substantially all the risks and rewards of ownership of a transferred financial asset, the Bank continues to recognize the financial asset and also recognizes a collateralized borrowing for the proceeds received.

2.6 Derivative Financial Instruments

The Bank uses derivative financial instruments to manage its risks associated with fluctuations in foreign currency. Such derivative financial instruments are initially recognized at fair value on the date on which the derivative contract is entered into and are subsequently remeasured at fair value. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

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

2.7 Offsetting Financial Instruments

Financial assets and financial liabilities are offset and the resulting net amount is reported in the statement of financial position when there is a legally enforceable right to set-off the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously. The right of set-off must be available at the end of the reporting period, that is, it is not contingent on future event. It must also be enforceable in the normal course of business, in the event of default, and in the event of insolvency or bankruptcy; and must be legally enforceable for both entity and all counterparties to the financial instruments.

2.8 Financial Liabilities

Financial liabilities include Deposit Liabilities, Bills Payable and Accrued Expenses and Other Liabilities (excluding tax-related payables and post-employment benefit obligation) and are recognized when the Bank becomes a party to the contractual terms of the instrument. All interest-related charges are recognized as Interest Expense in the statement of profit or loss.

Deposit liabilities and bills payable are recognized initially at their fair value, which is the issuance proceeds (fair value of consideration received) net of direct issue costs, and are subsequently measured at amortized cost using effective interest method for maturities beyond one year, less settlement payments. Any difference between proceeds net of transaction costs and the redemption value is recognized in the profit or loss over the period of the borrowings.

Accrued expenses and other liabilities are recognized initially at their fair value and subsequently measured at amortized cost, using effective interest method for maturities beyond one year, less settlement payments.

In 2014 and 2013, dividend distributions to shareholders are recognized as financial liabilities upon declaration by the Group and subsequent approval of the BSP. In 2015, BSP approval is no longer necessary on dividend recognition in accordance with the liberalized rules for banks and quasi-banks on dividend declaration.

Financial liabilities are derecognized from the statement of financial position only when the obligations are extinguished either through discharge, cancellation or expiration. The difference between the carrying amount of the financial liability derecognized and the consideration paid or payable is recognized in profit or loss.

2.9 Other Resources

Other resources pertain to other assets controlled by the Bank as a result of past events. These are recognized in the financial statements when it is probable that the future economic benefits will flow to the Bank and the asset has a cost or value that can be measured reliably.

2.10 Bank Premises, Furniture, Fixtures and Equipment

Land is stated at cost. Bank premises, furniture, fixtures and equipment are carried at acquisition cost less accumulated depreciation and amortization and any impairment losses.

The cost of an asset comprises its purchase price and directly attributable cost of bringing the asset to working condition for its intended use. Expenditures for additions, major improvements and renewals are capitalized; expenditures for repairs and maintenance are charged to expense as incurred.

Depreciation is computed on a straight-line basis over the estimated useful lives of the assets as follows:

Building	50 years
Furniture, fixtures and equipment	5-7 years
Transportation equipment	5 years

Leasehold improvements are amortized over the term of the lease or the estimated useful life of the improvements of 5 to 20 years, whichever is shorter.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (see Note 2.19).

Fully depreciated and fully amortized assets are retained in the accounts until they are no longer in use and no further charge for depreciation and amortization is made in respect of those assets.

The residual values, estimated useful lives and method of depreciation and amortization of Bank premises, furniture, fixtures and equipment (except land) are reviewed and adjusted if appropriate, at the end of each reporting period.

An item of bank premises, furniture, fixtures and equipment, including the related accumulated depreciation, amortization and impairment loss, is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in profit or loss in the year the item is derecognized.

2.11 Investment Properties

Investment properties pertain to land and buildings or condominium units acquired by the Bank, in settlement of loans from defaulting borrowers through foreclosure or dacion in payment. These properties are held by Bank either to earn rental income or for capital appreciation or for both, but not for sale in the ordinary course of business, use in the supply of services or for administrative purposes.

Investment properties are stated at cost, less accumulated depreciation and any impairment losses (see Note 2.19). The cost of an investment property comprises its purchases price and directly attributable costs incurred such as legal fees, transfer taxes and other transaction costs.

Investment properties except land are depreciated over a period of five to ten years. Depreciation and impairment loss are recognized in the same manner as in bank premises, furniture, fixtures and equipment.

Investment properties, including the related accumulated depreciation and any impairment losses, are derecognized upon disposal or when permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gain or loss on the retirement or disposal of investment properties is recognized in profit or loss under the Gain or loss on sale of properties under Miscellaneous Income or Expenses in the statement of profit or loss, in the year of retirement or disposal.

2.12 Intangible Assets

Intangible assets include goodwill, acquired branch licenses and computer software included as part of other resources which is accounted for under the cost model. The cost of the asset is the amount of cash or cash equivalents paid or the fair value of the other considerations given to acquire an asset at the time of its acquisition.

Acquired computer software licenses are capitalized on the basis of the costs incurred to acquire and install the specific software. Capitalized costs are amortized on a straight-line basis over the estimated useful life lives of these intangible assets are considered finite. In addition, intangible assets are subject to impairment testing as described in Note 2.19. Costs associated with maintaining computer software and those costs associated with research activities are recognized as expense in profit or loss as incurred.

Goodwill represents the excess of the cost of acquisition over the fair value of the net assets acquired and branch licenses at the date of acquisition. Goodwill and branch licenses are classified as intangible assets with indefinite useful life, and thus, not subject to amortization but to an annual test for impairment (see Note 2.19). For purposes of impairment testing, goodwill and branch licenses are allocated to cash-generating units and are subsequently carried at cost less any allowance for impairment losses.

When an intangible asset is disposed of, the gain or loss on disposal is determined as the difference between the proceeds and the carrying amount of the asset and is recognized in profit or loss.

2.13 Provisions and Contingencies

Provisions are recognized when present obligations will probably lead to an outflow of economic resources and they can be estimated reliably even if the timing or amount of the outflow may still be uncertain. A present obligation arises from the presence of a legal or constructive commitment that has resulted from past events, for example, legal disputes or onerous contracts.

Provisions are measured at the estimated expenditure required to settle the present obligation, based on the most reliable evidence available at the end of the reporting period, including the risks and uncertainties associated with the present obligation. Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. When time value of money is material, long-term provisions are discounted to their present values using a pre-tax rate that reflects market assessments and the risks specific to the obligation. The increase in the provision due to passage of time is recognized as interest expense. Provisions are reviewed at the end of each reporting period and adjusted to reflect the current best estimate.

In those cases where the possible outflow of economic resource as a result of present obligations is considered improbable or remote, or the amount to be provided for cannot be measured reliably, no liability is recognized in the financial statements. Similarly, possible inflows of economic benefits to the Bank that do not yet meet the recognition criteria of an asset are considered contingent assets, hence, are not recognized in the financial statements. On the other hand, any reimbursement that the Bank is virtually certain to collect from a third party with respect to the obligation is recognized as a separate asset not exceeding the amount of the related provision.

2.14 Equity

Capital stock represents the nominal value of the common and preferred shares that have been issued.

Additional paid-in capital includes any premium received on the issuance of capital stock. Any transaction costs associated with the issuance of shares are deducted from additional paid-in capital.

Appropriated surplus pertains to appropriations made by the Bank for a portion of the Bank's income from trust operations in compliance with BSP regulations.

Unappropriated surplus includes all current and prior period results of operations as disclosed in the statement of profit or loss, less appropriated surplus and dividends declared.

Revaluation reserves comprise remeasurements of post-employment defined benefit plan and unrealized fair value gains (losses) on mark-to-market valuation of AFS securities, net of amortization of fair value gains or losses on reclassified financial assets.

2.15 Related Party Transactions and Relationships

Related party transactions are transfers of resources, services or obligations between the Bank and its related parties, regardless whether a price is charged.

Parties are considered to be related if one party has the ability to control the other party or exercises significant influence over the other party in making financial and operating decisions. These parties include: (a) individuals owning, directly or indirectly through one or more intermediaries, control or are controlled by, or under common control with the Bank; (b) associates; (c) individuals owning, directly or indirectly, an interest in the voting power of the Bank that gives them significant influence over the Bank and close members of the family of any such individual; and (d) the Bank's funded retirement plan.

In considering each possible related party relationship, attention is directed to the substance of the relationship and not merely on the legal form.

2.16 Revenue and Expense Recognition

Revenue is recognized to the extent that it is probable that the revenue can be reliably measured; it is probable that future economic benefits will flow to the Bank; and the costs and expenses incurred and to be incurred can be measured reliably. Cost and expenses are recognized in profit or loss upon utilization of the assets or services or at the date these are incurred. In addition, the following specific recognition criteria must also be met before revenue is recognized:

a. Interest Income and Expense

Interest income and expense are recognized in the statement of profit or loss for all financial instruments using the effective interest method.

The effective interest method is a method of calculating the amortized cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument (for example, prepayment options) but does not consider future credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognized using the rate of interest used to discount future cash flows for the purpose of measuring the impairment loss.

b. Trading Gains or Losses

Trading gains or losses are recognized when the ownership of the security is transferred to the buyer and is computed as the difference between the selling price and the carrying amount of the security. Trading gains or losses also include result from the mark-to-market valuation of the securities classified as FVTPL at the valuation date and gain or loss from foreign exchange trading.

c. Service Charges, Fees and Commissions

Service charges, fees and commissions are generally recognized on an accrual basis when the service has been provided. Other service fees are recognized based on the applicable service contracts, usually on a time-appropriate basis.

2.17 Leases

The Bank accounts for its leases as follows:

- Bank as Lessee

Leases, which do not transfer to the Bank substantially all the risks and benefits of ownership of the assets are classified as operating leases. Operating lease payments (net of any incentive received from a lessor) are

recognized as expense in profit or loss on a straight-line basis over the lease term. Associated costs, such as insurance and repairs and maintenance, are expensed as incurred.

- Bank as Lessor

Leases, which do not transfer to the lessee substantially all the risks and benefits of ownership of the asset, are classified as operating leases. Lease income from operating leases is recognized in profit or loss on a straight-line basis over the lease term.

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

2.18 Foreign Currency Transactions and Translation

The accounting records of the Bank's regular banking unit are maintained in Philippine pesos while the FCDU are maintained in US dollars. Foreign currency transactions during the period are translated into the functional currency at exchange rates, which approximate those prevailing on transaction dates.

Foreign exchange gains and losses resulting from the settlement of foreign currency denominated transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in profit or loss.

Changes in the fair value of monetary financial assets denominated in foreign currency classified as AFS securities are analyzed between translation differences resulting from changes in the amortized cost of the security and other changes in the carrying amount of the security. Translation differences related to changes in amortized cost are recognized in profit or loss, and other changes in the carrying amount are recognized in other comprehensive income.

2.19 Impairment of Non-financial Assets

The Bank's premises, furniture, fixtures and equipment, investment properties, goodwill, branch licenses, computer software, other properties held for sale (classified as part of Miscellaneous under Other Resources) and other non-financial assets are subject to impairment testing. Intangible assets with an indefinite useful life or those not yet available for use are tested for impairment at least annually. All other individual assets or cash-generating units are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

For purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). As a result, assets are tested for impairment either individually or at the cash-generating unit level.

An impairment loss is recognized for the amount by which the asset or cash-generating unit's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of fair value, reflecting market conditions less costs to sell and value in use, based on an internal discounted cash flow evaluation. In determining value in use, management estimates the expected future cash flows from each cash-generating unit and determines the suitable interest rate in order to calculate the present value of those cash flows. Discount factors are determined individually for each cash-generating unit and reflect management's assessment of respective risk profiles, such as market and asset-specific risk factors. Impairment loss is charged pro rata to the other assets in the cash generating unit.

All assets are subsequently reassessed for indications that an impairment loss previously recognized may no longer exist. An impairment loss is reversed if the cash generating units' recoverable amount exceeds its carrying amount.

2.20 Employee Benefits

The Bank provides post-employment benefits to employees through a defined benefit plan and defined contribution plan, and other employee benefits which are recognized as follows:

a. Post-employment Defined Benefit Plan

A defined benefit plan is a post-employment plan that defines an amount of post-employment benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and salary. The legal obligation for any benefits from this kind of post-employment plan remains with the Bank, even if plan assets for funding the defined benefit plan have been acquired. Plan assets may include assets specifically designated to a long-term benefit fund, as well as qualifying insurance policies. The Bank's defined benefit post-employment plan covers all regular full time employees. The post-employment plan is tax-qualified, non-contributory and administered by a trustee bank.

The liability recognized in the statement of financial position for defined benefit post-employment plans is the present value of the defined benefit obligation (DBO) at the end of the reporting period less the fair value of plan assets. The DBO is calculated annually by independent actuaries using the projected unit credit method. The present value of the DBO is determined by discounting the estimated future cash outflows using interest rates based on zero coupon government bonds as published by Philippine Dealing & Exchange Corp. (PDEX) that are denominated in the currency in which the benefits will be paid and that have terms to maturity approximating to the terms of the related post-employment liability.

Remeasurements, comprising of actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions and the return on plan assets (excluding amount included in net

interest) are reflected immediately in the statement of financial position with a charge or credit recognized in other comprehensive income in the period in which they arise. Net interest is calculated by applying the discount rate at the beginning of the period, taking account of any changes in the net defined benefit liability or asset during the period as a result of contributions and benefit payments. Net interest is reported as part of Interest Expense account in the statement of profit or loss.

Past-service costs are recognized immediately in profit or loss in the period of a plan amendment or curtailment.

b. Post-employment Defined Contribution Plan

A defined contribution plan is a post-employment plan under which the Bank pays fixed contributions into an independent entity (e.g. Social Security System and Philhealth). The Bank has no legal or constructive obligations to pay further contributions after payment of the fixed contribution. The contributions recognized in respect of defined contribution plans are expensed as they fall due. Liabilities and assets may be recognized if underpayment or prepayment has occurred and are normally of a short-term nature.

c. Termination Benefits

Termination benefits are payable when employment is terminated by the Bank before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Bank recognizes termination benefits at the earlier of when it can no longer withdraw the offer of such benefits and when it recognizes costs for a restructuring that is within the scope of PAS 37 and involves the payment of termination benefits. In the case of an offer made to encourage voluntary redundancy, the termination benefits are measured based on the number of employees expected to accept the offer. Benefits falling due more than 12 months after the end of the reporting period are discounted to their present value.

d. Bonus Plan

The Bank recognizes a liability and an expense for employee bonuses, based on a formula that is fixed regardless of the Bank's income after certain adjustments and does not take into consideration the profit attributable to the Bank's shareholders. The Bank recognizes a provision where it is contractually obliged to pay the benefits, or where there is a past practice that has created a constructive obligation.

e. Compensated Absences

Compensated absences are recognized for the number of paid leave days (including holiday entitlement) remaining at the end of the

reporting period. They are included in the Accrued Expenses and Other Liabilities account in the statement of financial position at the undiscounted amount that the Bank expects to pay as a result of the unused entitlement.

2.21 Income Taxes

Tax expense recognized in profit or loss comprises the sum of deferred tax and current tax not recognized in other comprehensive income or directly in equity, if any.

Current tax assets or liabilities comprise those claims from, or obligations to, fiscal authorities relating to the current or prior reporting period, that are uncollected or unpaid at the reporting period. They are calculated according to the tax rates and tax laws applicable to the fiscal periods to which they relate, based on the taxable profit for the year. All changes to current tax assets or liabilities are recognized as a component of tax expense in profit or loss.

Deferred tax is accounted for using the liability method, on temporary differences at the end of each reporting period between the tax base of assets and liabilities and their carrying amounts for financial reporting purposes. Under the liability method, with certain exceptions, deferred tax liabilities are recognized for all taxable temporary differences and deferred tax assets are recognized for all deductible temporary differences and the carry forward of unused tax losses and unused tax credits to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilized. Unrecognized deferred tax assets are reassessed at the end of each reporting period and are recognized to the extent that it has become probable that future taxable profit will be available to allow such deferred tax assets to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period when the asset is realized or the liability is settled provided such tax rates have been enacted or substantively enacted at the end of the reporting period.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized.

The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Bank expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Most changes in deferred tax assets or liabilities are recognized as a component of tax expense in profit or loss, except to the extent that it relates to items recognized in other comprehensive income or directly in equity. In this case, the tax is also recognized in other comprehensive income or directly in equity, respectively.

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

2.22 Earnings per Share

Basic earnings per share (EPS) is determined by dividing net profit by the weighted average number of common shares subscribed and issued during the period, after retroactive adjustment for any stock dividend declared in the current period.

The diluted EPS is also computed by dividing net profit by the weighted average number of common shares subscribed and issued during the period. However, net profit attributable to common shares and the weighted average number of common shares outstanding are adjusted to reflect the effects of potentially dilutive convertible preferred shares as approved by the Securities and Exchange Commission. Convertible preferred shares are deemed to have been converted to common shares at the issuance of preferred shares. As of December 31, 2015 and 2014, the Bank has no convertible preferred shares.

2.23 Trust and Fiduciary Operations

The Bank acts as trustee and in other fiduciary capacity that result in the holding or placing of assets on behalf of individuals, trusts, retirement benefit plans and other institutions. These assets and their income arising thereon are excluded from these financial statements, as these are neither resources nor income of the Bank.

2.24 Events After the End of the Reporting Period

Any post-year-end event that provides additional information about the Bank's financial position at the end of the reporting period (adjusting event) is reflected in the financial statements. Post-year-end events that are not adjusting events, if any, are disclosed when material to the financial statements.

3. SIGNIFICANT ACCOUNTING JUDGMENTS AND ESTIMATES

The preparation of the Bank's financial statements in accordance with PFRS requires management to make judgments and estimates that affect the amounts reported in the financial statements and related notes. Judgments and estimates are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Actual results may ultimately differ from these estimates.

3.1 Critical Management Judgments in Applying Accounting Policies

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

a. Classifying Financial Assets at HTM Investments

In classifying non-derivative financial assets with fixed or determinable payments and fixed maturity, such as bonds, as HTM investments, the Bank evaluates its intention and ability to hold such investments up to maturity. Management has confirmed its intention and determined its

ability to hold the investments up to maturity.

If the Bank fails to keep these investments at maturity other than for the allowed specific circumstances as discussed in the succeeding paragraph, it will be required to reclassify the entire class to AFS securities. The investments would therefore be measured at fair value and not at amortized cost. However, the tainting provision will not apply if the sales or reclassifications of HTM investments are so close to maturity or the financial asset's call date that changes in the market rate of interest would not have a significant effect on the financial asset's fair value; occur after the Bank has collected substantially all of the financial asset's original principal through scheduled payments or prepayments; or are attributable to an isolated event that is beyond the control of the Bank, is nonrecurring and could not have been reasonably anticipated by the Bank.

b. Impairment of AFS Securities

The determination when an investment is other-than-temporarily impaired requires significant judgment. In making this judgment, the Bank evaluates, among other factors, the duration and extent to which the fair value of an investment is less than its cost, and the financial health of and near-term business outlook for the investee, including factors such as industry and sector performance, changes in technology and operational and financing cash flows.

Based on the recent evaluation of information and circumstances affecting the Bank's AFS securities, management concluded that no assets are impaired as of September 30, 2106 and December 31, 2015. Future changes in those information and circumstance might significantly affect the carrying amount of the assets.

c. Distinguishing Investment Properties and Owner-occupied Properties

The Bank determines whether a property qualifies as investment property. In making this judgment, the Bank considers whether the property generates cash flows largely independent of the other assets held by an entity. Owner-occupied properties generate cash flows that are attributable not only to properties but also to other assets used in the production or supply process.

Some properties may comprise a portion that is held to earn rental or for capital appreciation and another portion that is held for use in providing services or for administrative purposes. If these portions can be sold separately (or leased out separately under finance lease), the Bank accounts for the portions separately. If the portions cannot be sold separately, the property is accounted for as investment property only if an insignificant portion is held for use in providing services or for administrative purposes.

Judgment is applied in determining whether ancillary services are so significant that a property does not qualify as investment property. The Bank considers each property separately in making its judgment.

d. Classifying of Acquired Properties and Determining Fair Value of Investment Properties and Other Properties Held-for-Sale

The Bank classifies its acquired properties (foreclosed properties) as Bank Premises, Furniture, Fixtures and Equipment if used in operations, as other properties held for sale presented as part of Miscellaneous under Other Resources if the Bank expects that the properties (properties other than land and building) will be recovered through sale rather than use, as Investment Properties if the Bank intends to hold the properties for capital appreciation or as financial assets in accordance with PAS 39. At initial recognition, the Bank determines the fair value of the acquired properties based on valuations performed by both internal and external appraisers. The appraised value is determined based on the current economic and market conditions as well as the physical condition of the property.

e. Distinguishing Operating and Finance Leases

The Bank has entered into various lease agreements. Critical judgment was exercised by management to distinguish each lease agreement as either an operating or finance lease by looking at the transfer or retention of significant risk and rewards of ownership of the properties covered by the agreements. Failure to make the right judgment will result in either overstatement or understatement of assets and liabilities.

As of September 30, 2016 and December 31, 2015, the Bank has determined that all its leases are operating leases.

f. Recognition of Provisions and Contingencies

Judgment is exercised by management to distinguish the difference between provisions and contingencies. Policies on recognition and disclosure of provisions and contingencies are discussed in Note 2.13.

In dealing with the Bank's various legal proceedings, its estimate of the probable costs that may arise from claims and contingencies has been developed in consultation and coordination with the Bank's internal and outside counsels acting in defense for the Bank's legal cases and are based upon the analysis of probable results.

Although the Bank does not believe that its dealing on these proceedings will have material adverse effect on the Bank's financial position, it is possible that future results of operations could be materially affected by changes in the estimates or in the effectiveness of the strategies conducted relating to those proceedings.

3.2 Key Sources of Estimation Uncertainty

The following are the key assumptions concerning the future, and other key sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing a material adjustment to the carrying amounts of resources and liabilities within the next reporting period:

- a. Evaluating Impairment of Financial Assets (HTM Investments and Loans and Other Receivables)

The Bank reviews its HTM investments and loans and other receivable to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in profit or loss, the Bank makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from the portfolio before the decrease can be identified with an individual item in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers or issuers in a group, or national or local economic conditions that correlate with defaults on assets in the group, including, but not limited to, the length of the Bank's relationship with the customers, the customers' current credit status, average age of accounts, collection experience and historical loss experience.

Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

The carrying value of loans and other receivables and the analysis of the related allowance for impairment on such financial assets are shown in Notes 14. There are no impairment losses recognized on HTM investments in September 30, 2016, December 31, 2015 and 2014.

- b. Fair Value of Financial Instruments

Management applies valuation techniques to determine the fair value of financial instruments where active market quotes are not available. This requires management to develop estimates and assumptions based on market inputs, using observable data that market participants would use in pricing the instrument. Where such data is not observable, management uses its best estimate. Estimated fair values of financial instruments may vary from the actual prices that would be achieved in an arm's length transaction at the end of the reporting period.

- c. Estimating Useful Lives of Bank Premises, Furniture, Fixtures and Equipment, Investment Properties Except Land, Branch Licenses and Computer Software

The Bank estimates the useful lives of bank premises, furniture, fixtures and equipment, investment properties except land, branch licenses and computer software based on the period over which the assets are expected to be available for use. The estimated useful lives of bank premises, furniture, fixtures and equipment, investment properties and computer software are reviewed periodically and are updated if expectations differ from previous estimates due to physical wear and tear, technical or commercial obsolescence and legal or other limits on the use of the assets.

The Bank's branch licenses were regarded as having an indefinite useful lives considering there is no foreseeable limit to the period over which such assets are expected to generate net cash inflows for the Bank. The assessment of having indefinite useful lives is reviewed periodically and is updated whether events and circumstances such as the period of control over these assets and legal or similar limits on the use of these assets continue to support such assessment.

The carrying amounts of bank premises, furniture, fixtures and equipment and investment properties are analyzed in Notes 15 and 16, respectively. Based on management assessment, there is no change in the estimated useful lives of these assets during the year. Actual results, however, may vary due to changes in estimates brought about by changes in factors mentioned above.

d. Determining Realizable Amount of Deferred Tax Assets

The Bank reviews its deferred tax assets at the end of each reporting period and reduces the carrying amount to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized.

e. Determination of Fair Value of Investment Properties

The Bank's investment properties are composed of parcels of land and buildings and improvements, which are held for capital appreciation or held-for-lease, and are measured using cost model. The estimated fair value of investment properties disclosed is determined on the basis of the appraisals conducted by professional appraiser applying the relevant valuation methodologies as discussed therein.

For investment properties with appraisal conducted prior to the end of the current reporting period, management determines whether there are significant circumstances during the intervening period that may require adjustments or changes in the disclosure of fair value of those properties.

A significant change in key inputs and sources of information used in the determination of the fair value disclosed for those assets may result in adjustment in the carrying amount of the assets reported in the financial statements if their fair value will indicate evidence of impairment.

f. Estimating Impairment Losses of Non-financial Assets

Except for intangible assets with indefinite useful lives (i.e. goodwill and acquired branch licenses), PFRS requires that an impairment review be performed when certain impairment indications are present. The Bank's policy on estimating the impairment of non-financial assets is discussed in detail in Note 2.19. Though management believes that the assumptions used in the estimation of fair values reflected in the financial statements are appropriate and reasonable, significant changes in these assumptions may materially affect the assessment of recoverable values and any resulting impairment loss could have a material adverse effect on the results of operations.

There are no impairment losses recognized in goodwill, acquired branch licenses, bank premises, furniture, fixtures and equipment.

g. Valuation of Post-employment Benefits

The determination of the Bank's obligation and cost of post-employment benefit plan is dependent on the selection of certain assumptions used by actuaries in calculating such amounts. Those assumptions include, among others, discount rates, expected rate of salary increases and employee turnover. A significant change in any of these actuarial assumptions may generally affect the recognized expense and the carrying amount of the post-employment benefit obligation in the next reporting period.

4. RISK MANAGEMENT OBJECTIVES AND POLICIES

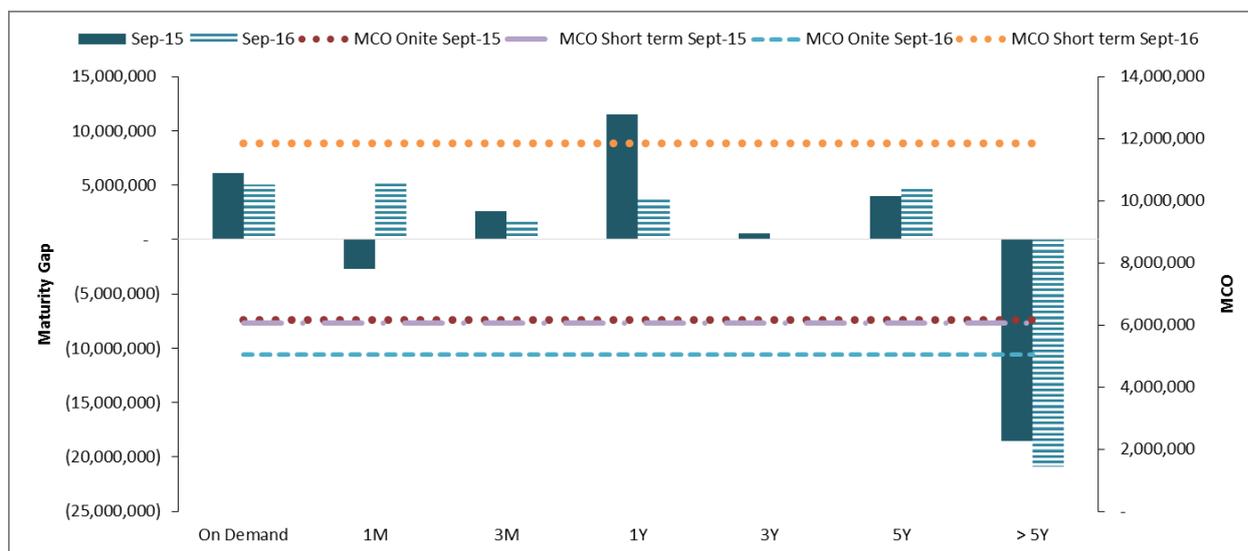
The Bank's financial risks sums up the credit and market risk exposures as a result of its dealings and inventory of financial instruments inherent in its banking functions. The Bank's BOD formulates the corporate risk policy, sets risk tolerances and appetite and provide risk oversight function through the Risk Management Committee (RiskCom), which in turn supervises the Chief Risk Officer and Head of the Risk Management Center in the development and implementation of risk policies, processes and guidelines. The Bank's policy in managing its financial risks is embodied in the BOD-approved Risk Management Manuals.

4.1 Liquidity Risks

Liquidity risk is the risk to income and capital as a result of the Bank failing its commitment for funds as they fall due. The Bank manages its liquidity risk through the management's monitoring of various liquidity ratios, Treasury's weekly and regular assessment of liquidity gaps, and the maturity ladder. To control liquidity gap risks, a quantitative ceiling to the net outflow of funds of the bank called Maximum Cumulative Outflow (MCO) limit is observed per currency based on the recommendation of management, which model and assumptions are reviewed by the Asset and Liability Committee (ALCO) and the RiskCom prior to the confirmation by the BOD.

Additional measures to mitigate liquidity risks include reporting of funding concentration, available funding sources, and liquid assets analysis. More frequent analysis of projected funding source and requirements as well as pricing strategies is discussed thoroughly during the weekly Asset and Liability Committee meetings.

The analysis of the cash flow gap analysis of resources, liabilities, capital funds and off-statement financial position items as of September 30, 2016 and September 30, 2015 is presented below (amounts in thousands).



4.2 Credit Risks

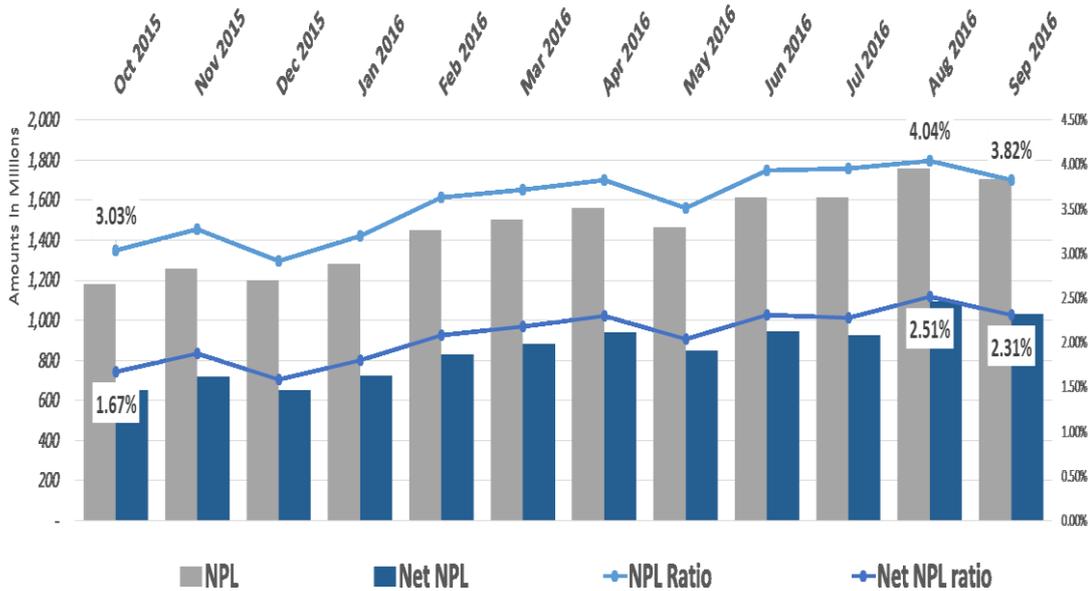
Credit risk pertains to the risk to income or capital due to non-payment by borrowers or counterparties of their obligations, either in full or partially as they fall due, deterioration in the credit quality of a borrower, issuer or counterparty, and the reduced recovery from a credit facility in the event of default. This is inherent in the Bank's lending, investing, and trading and is managed in accordance with the Bank's credit risk framework of risk identification, measurement, control and monitoring.

Credit risk is managed through a continuing review of credit policies, systems, and procedures. It starts with the definition of business goals and setting of risk policies by the Board of Directors (BOD). Account officers and credit officers directly handle credit risk as guided by BOD-approved policies and limits. The Risk Management Center, as guided by the RiskCom, performs an independent portfolio oversight of credit risks and reports regularly to the BOD and the RiskCom.

The Bank sets aside loan loss provisions pursuant to the requirement of the BSP and performs regular impairment analysis consistent with the Philippine Accounting Standards (PAS).

Pursuant to regulatory requirements and best practices, the Bank also conducts sensitivity analysis and stress testing of the credit portfolio to assess sensitivity of the Bank's capital to BOD-approved credit risk scenarios. As of September 30, 2016, the ratio of the Bank's loan loss provisions to its non-performing loans is at 42%.

The table below shows the NPL and Net NPL trend of the Bank for the 12-month period ending September 30, 2016:



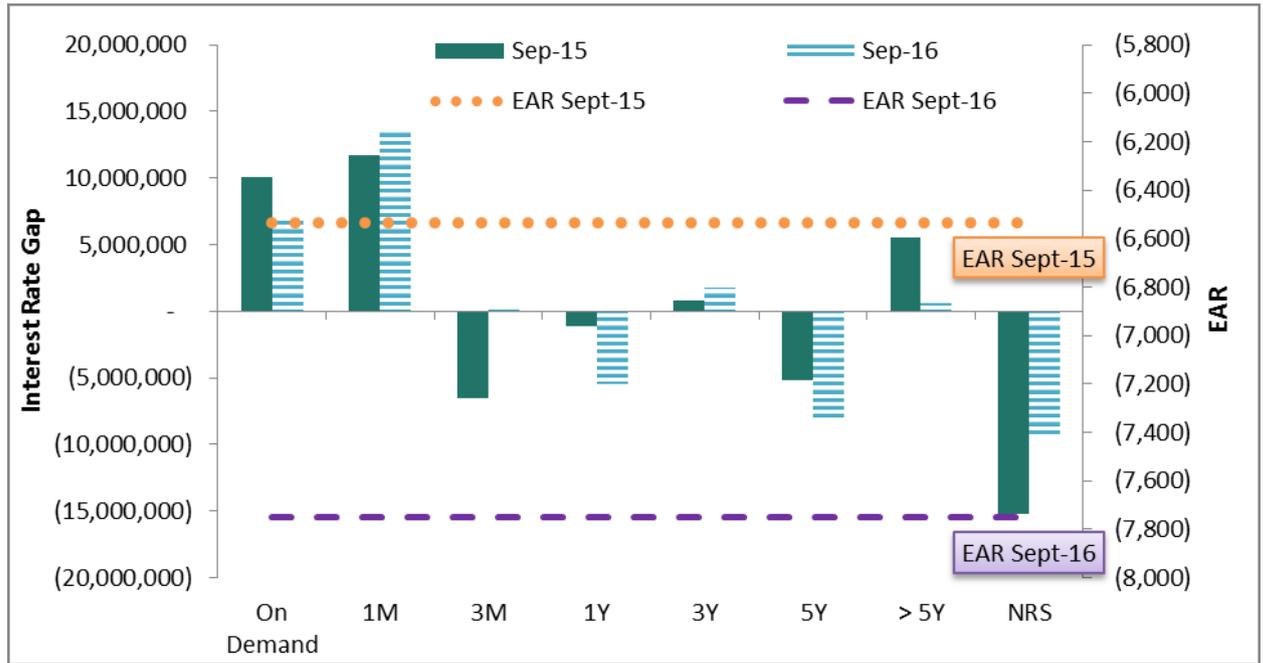
$NPL\ Ratio = (PD + ITL) / Gross\ Loans$
 $Net\ NPL = NPL - Specific\ Loan\ Provision$
 $Net\ NPL\ Ratio = Net\ NPL / Gross\ Loans$

4.3 Interest Rate Risks

Interest rate risk is the probability of decline in net interest earnings as a result of an adverse movement of interest rates.

In measuring interest rate exposure from an earnings perspective, the Bank calculates the Earnings at Risk (EAR) to determine the impact of interest rate changes on the Bank's accrual portfolio. The EAR is the potential decline in net interest income due to the adverse movement in interest rates. A negative interest rate sensitivity gap position implies that EAR increases with a rise in interest rates, while a positive interest rate sensitivity gap results in a potential decline in net interest rate income as interest rates fall. To supplement the EAR, the Bank regularly employs sensitivity analysis on the Bank's interest rate exposure.

To mitigate interest rate risk, the Bank follows a prudent policy on managing assets and liabilities so as to ensure that exposure to interest rate risk are kept within acceptable levels. The BOD has also approved the EAR Limit which is reviewed regularly. Interest rate gap & EAR are presented below (in thousands).



4.4 Price Risks

In measuring the magnitude of exposures related to the Bank's trading portfolio arising from holding of government and other debt securities, the Bank employs Value-at-Risk (VaR) methodology. VaR is an estimate of the amount of loss that a given risk exposure is unlikely to exceed during a given time period, at a given level of statistical confidence. Analytically, VaR is the product of: (a) the sensitivity of the market value of the position to movement of the relevant market risk factors, and (b) the volatility of the market risk factor for the given time horizon at a specified level of statistical confidence. Typically, the Bank uses a 99% confidence level for this measurement (i.e. losses could exceed the VaR in one out of 100 trading days). As the VaR methodology requires a minimum historical period of reckoning with market movements from a transparent discovery platform, the Bank uses yield and price data from the Philippine Dealing Exchange Corporation and Bloomberg in the calculation of the volatility of rates of return and security prices, consistent with BSP valuation guidelines.

In assessing market risk, the Bank scales the calculated VaR based on assumed defeasance or holding periods that range from one day and 10 days consistent with best practices and BSP standards.

As a prudent market risk control and compliance practice, the BOD has approved a market risk limit system which includes: (1) VaR limit on a per instrument and portfolio; (2) loss limit on per investment portfolio (3) off-market rate limits on per instrument type; and (4) holding period for investment securities.

In recognition of the limitations of VaR related to the assumptions on which the model is based, the Bank supplements the VaR with a wide range of stress tests to model the financial impact of a variety of exceptional market scenarios on individual trading portfolios and the Bank's overall position.

Table below shows AFS, HFT and FX VaR statistics from July-September 2016:

Value-at-Risk			
in Thou			
	AFS	HFT	FX
Average	100,813	153,433	2,583
High	137,874	411,378	6,696
Low	47,057	9,185	228

4.5 FX Risks

The Bank manages its exposure to effects of fluctuations in the foreign currency exchange rates by maintaining foreign currency exposure within the existing regulatory guidelines and at a level that it believes to be relatively conservative for a financial institution engaged in that type of business.

The Bank's foreign currency exposure is primarily limited to the foreign currency deposits, which are sourced within the Philippines or generated from remittances by Filipino expatriates and overseas Filipino workers. Also, foreign currency trading with corporate accounts and other financial institutions is a source of foreign currency exposure for the Bank. At the end of each month, the Bank reports to the BSP on its acquisition and disposition of foreign currency resulting from its daily transactions.

The Bank always maintains the BSP required asset cover for its foreign-currency liabilities.

5. ANTI-MONEY LAUNDERING CONTROLS

The Anti-Money Laundering Act (AMLA) or RA No. 9160 was passed in September 2001 and was amended by RA No. 9194, RA No. 10167, and RA No. 10365 in March 2003, June 2012 and February 2013, respectively. Under the AMLA, as amended, the Bank is required to submit "Covered Transaction Reports" to the Anti-Money Laundering Council (AMLC) involving single transactions in cash or other equivalent monetary instruments in excess of P0.5 million within one banking day. The Bank is also required to submit "Suspicious Transaction Reports" to the AMLC in the event that circumstances exist and there are reasonable grounds to believe that the transaction is suspicious. Furthermore, terrorist financing was criminalized in RA No. 10168.

In addition, the AMLA requires that the Bank safe keeps, as long as the account exists, all the Know Your Customer (KYC) documents involving its clients, including documents that establish and record the true and full identity of its clients. Likewise, transactional documents must be maintained and stored for five years from the date of the transaction. In cases involving closed accounts, the KYC documents must be kept for five years after their closure. Meanwhile, all records of accounts with court cases must be safe kept until there is a final resolution.

On January 27, 2011, BSP Circular No. 706 was implemented superseding all policies on AMLA. The Circular requires the Bank to adopt a comprehensive and risk-based Money Laundering and Terrorist Financing Prevention Program (MLPP) designed according to

the covered institution's corporate structure and risk profile.

In an effort to further prevent money laundering activities, the Bank revised its KYC policies and guidelines in order to comply with the aforementioned Circular. Under the guidelines, each business unit is required to validate the true identity of a customer based on official or other reliable identifying documents or records before an account may be opened. Likewise, the Bank is required to risk profile its clients to Low, Normal or High with its corresponding due diligence of Reduced, Average or Enhanced, in compliance with the risk-based approach mandated by the Circular. Decisions to enter into a business relationship with a high risk customer requires senior management approval, and in some cases such as a politically exposed person or a private individual holding a prominent position, Group Head approval is necessary.

The Bank's procedures for compliance with the AMLA are set out in its MLPP. The Bank's Compliance Officer, through the Anti-Money Laundering Department (AMLDD), monitors AMLA compliance and conducts regular compliance testing of business units.

The AMLDD requires all banking units to submit to the Compliance Office certificates of compliance with the Anti-Money Laundering Rules and Regulations on a quarterly basis.

The Compliance Officer regularly reports to the Audit Committee and to the BOD results of their monitoring of AMLA compliance.

6. CAPITAL MANAGEMENT AND REGULATORY CAPITAL

The Bank's lead regulator, the BSP, sets and monitors capital requirements for the Bank. In implementing current capital requirements, the BSP requires the Bank to maintain a prescribed ratio of qualifying capital to risk-weighted assets. PBB, being a stand-alone thrift bank, is required under BSP regulations to comply with Basel 1.5. Under this regulation, the qualifying capital account of PBB should not be less than an amount equal to 10% of its risk weighted assets.

The qualifying capital of the Bank for purposes of determining the capital-to-risk assets ratio consists of Tier 1 capital plus Tier 2 capital elements net of the required deductions from capital such as:

- unbooked valuation reserves and other capital adjustments as may be required by the BSP;
- total outstanding unsecured credit accommodations to directors, officers, stockholders and related interests (DOSRI);
- deferred tax asset net of deferred tax liability;
- goodwill;
- sinking fund for redemption of redeemable preferred shares; and
- other regulatory deductions.

Risk weighted assets is the sum of the Bank's credit risk weighted assets, operational risk weighted assets, and market risk weighted assets. The latter was due to the Bank's authority to engage in derivatives as end-user under a Type 3 Limited End-User Authority. Risk weighted assets are computed using the standardized approach for credit and market risks while basic

indicator approach with modification was used for operational risks.

The following are the risk-based capital adequacy of the Bank as of September 30, 2016, December 31, 2015 and 2014 (amounts in millions):

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Tier 1 Capital	P 9,379	P 8,709	P 8,275
Tier 2 Capital	<u>436</u>	<u>376</u>	<u>407</u>
Total Regulatory Capital	9,815	9,085	8,682
Deductions	<u>-</u>	<u>-</u>	()
Total Qualifying Capital	<u>P 9,815</u>	<u>P 9,085</u>	<u>P 8,682</u>
Tier 1 Capital	P 9,379	P 8,709	P 8,275
Tier 1 Capital Deductions	<u>-</u>	<u>-</u>	()
Net Tier 1 Capital	<u>P 9,379</u>	<u>P 8,709</u>	<u>P 8,275</u>
Risk Weighted Assets			
Credit Risk Weighted Assets	P 45,795	P 43,382	P 38,348
Operational Risk Weighted Assets	3,594	3,580	3,233
Market Risk Weighted Assets	<u>1,515</u>	<u>4,378</u>	<u>139</u>
Total Risk-Weighted Assets	<u>P 50,904</u>	<u>P 51,340</u>	<u>P 41,720</u>
	<u>2016</u>	<u>2015</u>	<u>2014</u>

Capital ratios:

Total qualifying capital expressed as percentage of total risk-weighted assets	19.28%	20.8%	26.0%
Net Tier 1 capital expressed as percentage of total risk-weighted assets	18.43%	19.8%	22.9%

The amount of surplus funds available for dividend declaration is determined also on the basis of regulatory net worth after considering certain adjustments.

The Bank's policy is to maintain a strong capital base in order to maintain investor, creditor and market confidence and to sustain future development of the business. The impact of the level of capital on shareholder's return is also recognized and the Bank recognizes the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

A Bank's regulatory capital is analyzed into two tiers, which are Tier 1 Capital plus Tier 2 Capital less deductions from the total of Tier 1 and Tier 2 capital equivalent to

50% of the following:

1. Investments in equity of unconsolidated subsidiary banks and other financial allied undertakings, but excluding insurance companies;
2. Investments in debt capital instruments of unconsolidated subsidiary banks;
3. Investments in equity of subsidiary insurance companies and non-financial allied undertakings;
4. Reciprocal investments in equity of other banks/enterprises; and,
5. Reciprocal investments in unsecured subordinated term debt instruments of other banks/quasi-banks qualifying as Hybrid Tier 1, Upper Tier 2 and Lower Tier 2, in excess of the lower of (i) an aggregate ceiling of 5% of total Tier 1 capital of the bank excluding Hybrid Tier 1; or (ii) 10% of the total outstanding unsecured subordinated term debt issuance of the other bank/quasi-banks.

Provided, that any asset deducted from the qualifying capital in computing the numerator of the risk-based capital ratio shall not be included in the risk-weighted assets in computing the denominator of the ratio.

As of September 30, 2016 and December 31, 2015, the Bank has no exposure in item (a) to item (e) above. There were no material changes in the Bank's management of capital during the current year.

As of September 30, 2016 and December 31, 2015, the Bank has satisfactorily complied with the capital-to-risk assets ratio.

Under existing BSP regulations, the determination of the Bank's compliance with regulatory requirements and ratios is based on the amount of the Bank's "unimpaired capital" (regular net worth) reported to the BSP, determined on the basis of regulatory accounting policies, which differ from PFRS in some aspects (mainly in the recognition of deferred tax assets). Thrift banks with head office within Metro Manila are required to comply with the minimum capital requirement of P1.0 billion. The Bank has complied with the minimum capital requirement at the end of each reporting period.

7. FAIR VALUE MEASUREMENT AND DISCLOSURES

Fair Value Hierarchy

In accordance with PFRS 13, the fair value of financial assets and financial liabilities and non-financial assets which are measured at fair value on a recurring or non-recurring basis and those assets and liabilities not measured at fair value but for which fair value is disclosed in accordance with other relevant PFRS, are categorized into three levels based on the significance of inputs used to measure the fair value. The fair value hierarchy has the following levels:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities that an entity can access at the measurement date;
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices); and,
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The level within which the financial asset or liability is classified is determined based on the lowest level of significant input to the fair value measurement.

For purposes of determining the market value at Level 1, a market is regarded as active if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service, or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis.

For investments which do not have quoted market price, the fair value is determined by using generally acceptable pricing models and valuation techniques or by reference to the current market of another instrument which is substantially the same after taking into account the related credit risk of counterparties, or is calculated based on the expected cash flows of the underlying net asset base of the instrument.

When the Bank uses valuation technique, it maximizes the use of observable market data where it is available and relies as little as possible on entity specific estimates. If all significant inputs required to determine the fair value of an instrument are observable, the instrument is included in Level 2. Otherwise, it is included in Level 3.

8. SEGMENT REPORTING

The Bank's main operating businesses are organized and managed separately according to the nature of services and products provided and the different markets served, with each segment representing a strategic business unit. These are also the basis of the Bank in reporting to its chief operating decision-maker for its strategic decision-making activities.

Management currently identifies the Bank's three service lines as primary operating segments.

1. *Consumer Banking* – includes auto financing, home financing, and salary or personal loans;
2. *Corporate Banking* – includes term loans, working capital credit lines, bills purchase and discounting lines; and,
3. *Treasury Operations* – manages liquidity of the Bank and is a key component in revenue and income generation through its trading and investment activities.

These segments are the basis on which the Bank reports its segment information.

Transactions between the segments are on normal commercial terms and conditions.

Segment revenues and expenses that are directly attributable to primary operating segment and the relevant portions of the Bank's revenues and expenses that can be allocated to that operating segment are accordingly reflected as revenues and expenses of that operating segment. Revenue sharing agreements are used to allocate external customer revenues to a segment on a reasonable basis.

The contribution of these various business activities to the Bank's revenues and income for the years 2016, 2015 and 2014 follow (amounts in millions):

	<u>Corporate Banking</u>	<u>Consumer Banking</u>	<u>Treasury Operations</u>	<u>Total</u>
<u>September 30, 2016</u>				
Statement of Profit or Loss				
Net interest income	P 1,407	P 153	P 253	P 1,813
Non-interest income	<u>140</u>	<u>-</u>	<u>384</u>	<u>524</u>
Total income (after interest expense)	1,547	153	637	2,337
Operating expenses	<u>1,109</u>	<u>74</u>	<u>383</u>	<u>1,566</u>
Pre-tax profit (loss)	<u>438</u>	<u>79</u>	<u>254</u>	<u>771</u>
Net profit (loss)	<u><u>P 380</u></u>	<u><u>P 69</u></u>	<u><u>P 221</u></u>	<u><u>P 670</u></u>

	Corporate Banking	Consumer Banking	Treasury Operations	Total
Statement of Financial Position				
Total Resources				
Segment assets	P 45,917	P 3,276	P 16,075	P 65,268
Intangible assets	51	-	-	51
Deferred tax assets	<u>362</u>	<u>-</u>	<u>-</u>	<u>362</u>
	<u>P 46,330</u>	<u>P 3,276</u>	<u>P 16,075</u>	<u>P 65,681</u>
Total Liabilities	<u>P 38,920</u>	<u>P 2,763</u>	<u>P 14,215</u>	<u>P 55,898</u>
Other segment information				
Depreciation and amortization	<u>P 91</u>	<u>P 7</u>	<u>P 33</u>	<u>P 131</u>
Capital expenditures	<u>P 71</u>	<u>P 5</u>	<u>P 26</u>	<u>P 102</u>

September 30, 2015

Statement of Profit or Loss

Net interest income	P 1,385	P 127	P 283	P 1,795
Non-interest income	<u>145</u>	<u>-</u>	<u>74</u>	<u>219</u>
Total income (after interest expense)	1,530	127	357	2,014
Operating expenses	<u>993</u>	<u>53</u>	<u>352</u>	<u>1,398</u>
Pre-tax profit	<u>537</u>	<u>74</u>	<u>5</u>	<u>616</u>
Net profit	<u>P 411</u>	<u>P 57</u>	<u>P 4</u>	<u>P 472</u>

Statement of Financial Position

Total Resources				
Segment assets	P 39,379	P 2,625	P 20,208	P 62,212
Intangible assets	55	-	-	55
Deferred tax assets	<u>313</u>	<u>-</u>	<u>-</u>	<u>313</u>
	<u>P 39,747</u>	<u>P 2,625</u>	<u>P 20,208</u>	<u>P 62,580</u>
Total Liabilities	<u>P 37,394</u>	<u>P 2,186</u>	<u>P 14,585</u>	<u>P 54,165</u>
Other segment information				
Depreciation and amortization	<u>P 79</u>	<u>P 5</u>	<u>P 30</u>	<u>P 114</u>
Capital expenditures	<u>P 23</u>	<u>P 1</u>	<u>P 9</u>	<u>P 33</u>

9. CASH AND DUE FROM BSP

This account is composed of the following:

	<u>2016</u>	<u>2015</u>
Cash and other cash items	P 837,690,644	P 1,279,302,155
Due from BSP		
Mandatory reserves	3,842,143,980	3,802,637,783
Other than mandatory reserves	3,480,000,000	3,870,000,000
	<u>7,322,143,980</u>	<u>7,672,637,783</u>
	<u>P 8,159,834,624</u>	<u>P 8,951,939,938</u>

Cash consists primarily of funds in the form of Philippine currency notes and coins in the Bank's vault and those in the possession of tellers, including automated teller machines. Other cash items include cash items (other than currency and coins on hand) such as checks drawn on the other banks or other branches that were received after the Bank's clearing cut-off time until the close of the regular banking hours.

Mandatory reserves represent the balance of the deposit account maintained with the BSP to meet reserve requirements and to serve as clearing account for interbank claims.

10. DUE FROM OTHER BANKS

The balance of this account represents deposits with the following:

	<u>2016</u>	<u>2015</u>
Local banks	P 2,512,085,011	P 1,493,241,853
Foreign banks	369,878,409	538,339,235
	<u>P 2,881,963,420</u>	<u>P 2,031,581,088</u>

The breakdown of due from other banks by currency follows:

	<u>2016</u>	<u>2015</u>
US dollars	P 2,477,626,225	P 463,361,884
Philippine peso	404,337,195	1,568,219,204
	<u>P 2,881,963,420</u>	<u>P 2,031,581,088</u>

11. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

This account is composed of held-for-trading government securities with fair value amounting to P246 million as of September 30, 2016 and P75.9 million as of December 31, 2015. Interest rates on these investments range from 3.50% in September 30, 2016, 4.6% to 6.1% in December 31, 2015. The total interest income earned amounted to P5.15 million and P21.92 million for the three quarter ending September 30, 2016 and 2015 respectively, and are included as part of Interest Income on Trading and Investment Securities in the statements of profit or loss.

The related net unrealized fair value gains or losses, presented as part of Trading Gains - net in the statements of profit or loss, amounted to a loss of P320 thousand and a loss of P153 thousand for the three quarter ending September 30, 2016 and 2015. Realized trading gains, net of losses, amounted to P65.00 million and P17.03 million in 2016 and 2015 respectively.

12. AVAILABLE-FOR-SALE SECURITIES

This account is composed of the following:

	<u>2016</u>	<u>2015</u>
Corporate bonds	P 1,293,690,290	P 1,931,193,769
Government securities	264,337,584	1,161,644,542
Equity securities		1,700,000
	<u>P 1,558,027,874</u>	<u>P 3,094,538,311</u>

As to currency, this account consists of the following:

	<u>2016</u>	<u>2015</u>
Foreign currencies	P 1,459,200,905	P 2,990,980,345
Philippine pesos	98,826,969	103,557,966
	<u>P 1,558,027,874</u>	<u>P 3,094,538,311</u>

Changes in the AFS securities are summarized below.

	<u>2016</u>	<u>2015</u>
Balance at beginning of year	P 3,093,224,480	P 1,715,736,721
Additions	63,843,358	615,246,804
Amortization of discount	37,921,613	(2,416,721)
Disposals	(829,711,980)	(40,000,000)
Foreign currency revaluation		(990,158)
Fair value gains (losses)	189,169,927	57,244,732
Reclassification	-	-
	<u>P 2,554,447,398</u>	<u>P 2,344,821,378</u>

13. HELD-TO-MATURITY INVESTMENTS

As of December 31, 2015, this account is composed of local and foreign government debt securities which have remaining maturities of beyond one year, nil as of September 30, 2016.

As to currency, this account consists of the following:

	<u>2015</u>
Foreign currencies	P 5,487,613,698
Philippine pesos	<u>461,113,797</u>
	<u>P 5,948,727,495</u>

14. LOANS AND OTHER RECEIVABLES

	<u>2016</u>	<u>2015</u>
Receivables from customers:		
Loans and discounts	P 40,388,816,981	P 36,954,001,403
Bills purchased	934,517,376	1,259,177,626
Customers' liabilities on acceptances, letters of credit and trust receipts	3,288,185,357	3,066,453,404
	<u>44,611,519,714</u>	<u>41,279,632,433</u>
Unearned discount	(115,364,903)	(96,231,198)
	<u>44,496,154,811</u>	<u>41,183,401,235</u>
Other receivables:		
Unquoted debt securities	1,214,138,072	1,216,105,404
Accrued interest receivable	134,778,151	178,793,670
Sales contracts receivable	103,872,376	91,856,163
Accounts receivable	91,454,927	87,727,360
Deficiency claims receivable	52,456,968	56,571,522
SPURRA	2,452,378,297	
	<u>4,049,078,791</u>	<u>1,631,054,119</u>
	48,545,233,602	42,814,455,354
Allowance for impairment	<u>(1,197,491,957)</u>	<u>(1,076,625,132)</u>
	<u>P 47,347,741,645</u>	<u>P 41,737,830,222</u>

On various dates in 2002, the Bank purchased P259.0 million face value of the 10-year Poverty Eradication and Alleviation Certificates (PEACe) bonds, in the belief that these were tax-exempt. Said bonds were issued by the Bureau of Treasury (BTr) in 2001 which matured on October 18, 2011. As of September 30, 2016 and December 31, 2015, the Accounts receivable includes P36.7 million set up by the Bank for the final tax withheld by

the BTr upon maturity of the bonds subject to the resolution of a case filed with the Supreme Court on the matter. On January 13, 2015, the Supreme Court nullified the 2011 Bureau of Internal Revenue (BIR) Rulings classifying all bonds as deposit substitutes and ordered the Bureau of Treasury to return to the petitioning banks the 20% final withholding taxes it withheld on the PEACe Bonds on October 18, 2011; hence, management believes that recoverability of the final tax on PEACe bonds continues to be probable.

As of September 30, 2016 and December 31, 2015, non-performing loans of the Bank amount to P1,533.54 million and P1,191.6 million, respectively, while restructured loans amount to P54.62 million and P80.96 million, respectively.

The maturity profile of the Bank's loans and discounts follows (amounts in thousands):

	<u>2016</u>	<u>2015</u>
Within one year	P 29,924,808	P 29,422,915
Beyond one year	<u>14,686,712</u>	<u>11,856,720</u>
	<u>P 44,611,520</u>	<u>P 41,279,632</u>

The Bank's concentration of credit as to industry for its loans and discounts portfolio follows (amounts in thousands):

	<u>2016</u>	<u>2015</u>
Wholesale and retail trade	P 15,011,919	P 17,390,757
Construction	8,425,816	8,744,390
Manufacturing	6,157,393	5,011,775
Administrative and support services	6,995,672	4,984,934
Transportation and storage	4,063,243	3,218,626
Activities of private household as employers and undifferentiated goods and services and producing activities of households for own use	15,074	681,598
Electricity, gas, steam and air-conditioning supply	3,407,418	675,625
Agriculture, fishery and forestry	382,254	461,296
Mining and quarrying	<u>152,731</u>	<u>110,631</u>
	<u>P 44,611,520</u>	<u>P 41,279,632</u>

As to security, loans and discounts are classified into the following (amounts in thousands):

	<u>2016</u>	<u>2015</u>
Secured:		
Real estate mortgage	P 17,494,058	P 14,247,890
Deposit hold-out	2,454,293	2,693,318
Chattel mortgage	3,225,975	2,335,847
Others	1,118,312	1,259,177
Unsecured	<u>18,779,541</u>	<u>20,743,400</u>
	<u>P 41,071,031</u>	<u>P 41,279,632</u>

15. DEPOSIT LIABILITIES

The maturity profile of the Bank's deposit liabilities follows:

	<u>2016</u>	<u>2015</u>
Within one year	P 51,643,907,035	P 54,225,906,880
Beyond one year	<u>2,509,635,049</u>	<u>790,312,630</u>
	<u>P 54,153,542,084</u>	<u>P 55,016,219,510</u>

The classification of the Bank's deposit liabilities as to currency follows:

	<u>2016</u>	<u>2015</u>
Philippine peso	P 49,336,087,467	P 48,557,474,402
Foreign currencies	<u>4,817,454,617</u>	<u>6,458,745,108</u>
	<u>P 54,153,542,084</u>	<u>P 55,016,219,510</u>

Under existing BSP regulations, non-FCDU deposit liabilities are subject to required reserves for deposits of 8.00%. The Bank is in compliance with these regulations.

On April 6, 2012, the BSP issued an amendment to the existing provisions as to the eligibility of cash and deposit accounts with BSP as forms of reserve requirements. As indicated in the recent amendment, cash and other cash items are no longer considered as eligible reserves. Available reserves as of September 30, 2016 and December 31, 2015 amount to P3,996.2 million and P3,802.6 million, respectively.

16. EQUITY

16.1 Capital Stock

Capital stock as of September 30, 2016 consists of:

	Number of Shares		Amount	
	2016	2015	2016	2015
Preferred shares – P10 par value				
Authorized -130,000,000 shares				
Issued, fully paid and outstanding	62,000,000	62,000,000	P 620,000,000	P 620,000,000
Common shares – P10 par value				
Authorized – 870,000,000 shares in 2013				
Issued, fully paid and outstanding				
Balance at beginning of year	536,458,437	429,166,750	P5,364,584,370	P4,291,667,500
Stock dividends		107,291,687		1,072,916,870
	536,458,437	536,458,437	P5,364,584,370	P5,364,584,370

The Bank's preferred shares are nonvoting, nonconvertible, and are redeemable at the option of the Bank. These shares are entitled to non-cumulative dividend of 8.0% per annum.

On February 18, 2013, the Bank offered its 101,333,400 unissued common shares by way of IPO at P31.50 per share resulting in the recognition of additional paid-in capital of P1,998.4 million, net of transactions costs.

As of September 30, 2016, the Bank has 64 holders of its equity securities listed in the PSE and its share price closed at P14.40. The Bank has 536,458,438 million common shares traded in the PSE as of September 30, 2016.

16.2 Dividends

On August 19, 2015, the BOD approved the declaration stock dividends totaling 107.3 million common shares amounting to P1.1 billion for all issued and outstanding common shares to stockholders on record for the year ended December 31, 2014. The dividend distribution was approved by the stockholders representing at least two-thirds of the issued and outstanding capital stock and the BSP on May 29, 2015 and August 4, 2015, respectively.

On May 5, 2014, the BOD approved the declaration of cash dividends amounting to P62.3 million for all issued and outstanding preferred shares and stock dividends totaling 85.8 million common shares amounting to P858.3 million for all issued and outstanding common shares to stockholders on record for the year ended December 31, 2013. The dividend distribution was approved by the stockholders representing at least two-thirds of the issued and outstanding capital stock and the BSP on May 30, 2014 and June 26, 2014, respectively.

16.3 Appropriated Surplus

In 2015, 2014 and 2013, additional appropriations of surplus amounting to P1.4 million, P1.6 million and P0.9 million, respectively, pertain to the portion of the

**SCHEDULE OF AGING OF LOANS
RECEIVABLES
(PSE Requirement per Circular No. 2164-99)
As of September 30, 2016**

Current Accounts (by maturity)	
Up to 12 months	30,485,842,276
Over 1 year to 3 years	4,327,332,203
Over 3 years to 5 years	3,972,773,932
Over 5 years	8,169,827,295
Past due and items in litigations	1,704,822,829
Loans Receivables (gross)	48,660,598,535
Less:	
Unearned and other deferred income	115,364,903
Allowance for credit losses	1,197,491,957
Loans Receivables (Net)	47,347,741,675

FINANCIAL SOUNDNESS INDICATORS
(As Required by SRC Rule)

	September 30, 2016	December 31, 2015
Current Ratio ⁽¹⁾	71.05%	96.45%
Solvency Ratio ⁽²⁾	1.18%	1.15%
Debt-to-equity ⁽³⁾	5.71%	6.74%
Asset-to-equity ⁽⁴⁾	6.71%	7.74%
Interest rate coverage ratio ⁽⁵⁾	238.48%	193.03%
Return on Equity ⁽⁶⁾	9.60%	6.10%
Return on Assets ⁽⁷⁾	1.40%	0.81%
Net Interest Margin ^{(8) (9)}	3.95%	4.03%
Cost-to-Income Ratio ⁽¹⁰⁾	64.43%	66.98%

Notes:

- 1) Current assets divided by current liabilities
- 2) Total assets divided by total liabilities
- 3) Total liabilities divided by total equity
- 4) Total assets divided by total equity
- 5) Income before interest and taxes divided by interest expense
- 6) Net income divided by average total equity for the periods indicated (annualized)
- 7) Net income divided by average total assets for the periods indicated (annualized)
- 8) Net interest income divided by average interest-earning assets (incl. interbank loans, trading and investment securities and loans)
- 9) Starting April 2012, the BSP stopped paying interest on reserves on customer deposits of banks. The Q1 2013 computation considered the Bank's deposit with BSP as non-earning. In Q1 2012 and previous to that, it is considered part of earning assets. NIM in Q1 2012 would have been 7.3% if this was to be calculated on same basis as that of Q1 2013
- 10) Other expenses (excl. provision for impairment and credit losses) divided by the sum of interest and other income for the periods indicated