PHILEQUITY PSE INDEX FUND, INC.
(An Open-End Mutual Fund Company)

Financial Statements
December 31, 2006 and 2005 and
Years Ended December 31, 2006, 2005 and 2004

and

Independent Auditors' Report

COVER SHEET

A1998-16221
SEC Registration Number

PHILEQUITY PSE INDEX FUND, INC. (An Open-End Mutual Fund Company)
(Company's Full Name)

2703-A, East Tower, Philippine Stock Exchange Centre, Exchange Road, Ortigas Center, Pasig City
(Business Address: No. Street City/Town/Province)

Mr. Edmundo Bunyi, Jr.	635-6963
(Contact Person)	(Company Telephone Number)

12 31	AAFS	06
Month *Day* (Fiscal Year)	(Form Type)	*Month* *Day* (Annual Meeting)

NA
(Secondary License Type, If Applicable)

Dept. Requiring this Doc.

Amended Articles Number/Section

Total Amount of Borrowings

12	₱	₱
Total No. of Stockholders	Domestic	Foreign

To be accomplished by SEC Personnel concerned

File Number

LCU

Document ID

Cashier

STAMPS

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SGV & Co

SyCip Gorres Velayo & Co.
6760 Ayala Avenue
1226 Makati City
Philippines

Phone: (632) 891-0307
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www.sgv.com.ph

BOA/PRC Reg. No. 0001
SEC Accreditation No. 0012-FR-1

INDEPENDENT AUDITORS' REPORT
TO ACCOMPANY INCOME TAX RETURN

The Stockholders and the Board of Directors
Philequity PSE Index Fund, Inc.
2703-A, East Tower
Philippine Stock Exchange Centre
Exchange Road, Ortigas Center
Pasig City

We have audited the financial statements of Philequity PSE Index Fund, Inc. (an open-end mutual fund company) for the year ended December 31, 2006, on which we have rendered the attached report dated March 21, 2007.

In compliance with Revenue Regulations V-20, we are stating the following:

1. The taxes paid or accrued by the above Company for the year ended December 31, 2006 are shown in the Schedule of Taxes and Licenses attached to the Annual Income Tax Return.

2. No partner of our Firm is related by consanguinity or affinity to the president, manager or principal stockholders of the Company.

SYCIP GORRES VELAYO & CO.

Juanito A. Fullecido
Partner
CPA Certificate No. 25543
SEC Accreditation No. 0080-AR-1
Tax Identification No. 102-086-897
PTR No. 0267355, January 2, 2007, Makati City

March 21, 2007

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In compliance with SRC Rule 68, we are stating that the above Company has a total number of five (5) stockholders owning one hundred (100) or more shares each.

SYCIP GORRES VELAYO & CO.

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INDEPENDENT AUDITORS' REPORT

The Stockholders and the Board of Directors
Philequity PSE Index Fund, Inc.
2703-A, East Tower
Philippine Stock Exchange Centre
Exchange Road, Ortigas Center
Pasig City

We have audited the accompanying financial statements of Philequity PSE Index Fund, Inc. (an open-end mutual fund company), which comprise the statements of assets and liabilities as at December 31, 2006 and 2005, and the statements of operations, statements of changes in net assets attributable to unitholders and statements of cash flows for each of the three years in the period ended December 31, 2006, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Philippine Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with Philippine Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Philequity PSE Index Fund, Inc. as of December 31, 2006 and 2005, and its financial performance and its cash flows for each of the three years in the period ended December 31, 2006 in accordance with Philippine Financial Reporting Standards.

SYCIP GORRES VELAYO & CO.

Juanito A. Fullecido
Partner
CPA Certificate No. 25543
SEC Accreditation No. 0080-AR-1
Tax Identification No. 102-086-897
PTR No. 0267355, January 2, 2007, Makati City

March 21, 2007

INDEPENDENT AUDITORS' REPORT

The Stockholders and the Board of Directors
Philequity PSE Index Fund, Inc.

We have audited the accompanying financial statements of Philequity PSE Index Fund, Inc. (an open-end mutual fund company), which comprise the statements of assets and liabilities as at December 31, 2006 and 2005, and the statements of operations, statements of changes in net assets attributable to unitholders and statements of cash flows for each of the three years in the period ended December 31, 2006, and a summary of significant accounting policies and other explanatory notes.

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Tax Identification No. 102-086-897
PTR No. 0267355, January 2, 2007, Makati City

March 21, 2007

PHILEQUITY PSE INDEX FUND, INC.
(An Open-End Mutual Fund Company)

STATEMENTS OF ASSETS AND LIABILITIES

	December 31	
	2006	2005
ASSETS		
Financial Assets at Fair Value through Profit or Loss (FVPL) (Notes 6 and 12)	**₱37,518,667**	₱27,938,713
Cash and Cash Equivalents (Notes 7 and 12)	**5,390,186**	2,908,719
Receivables (Note 12)	**1,177,160**	86,465
	44,086,013	30,933,897
LIABILITY		
Accrued Expenses (Note 12)	**46,090**	40,228
NET ASSETS ATTRIBUTABLE TO UNITHOLDERS (Note 8)	**₱44,039,923**	₱30,893,669
Net Asset Value Per Share (Note 8)	**₱1.711**	₱1.236

See accompanying Notes to Financial Statements.

PHILEQUITY PSE INDEX FUND, INC.
(An Open-End Mutual Fund Company)

STATEMENTS OF OPERATIONS

	Years Ended December 31		
	2006	2005	2004
INVESTMENT INCOME			
Gain on market valuation of fair value through profit or loss (FVPL) financial assets (Note 6)	**₱10,169,350**	₱3,293,487	₱–
Net realized gain on sale of:			
Financial assets at FVPL	**1,111,029**	419,566	–
Investments in listed securities	**–**	–	67,065
Dividends	**853,280**	727,868	561,701
Interest	**219,355**	183,769	155,614
	12,353,014	4,624,690	784,380
EXPENSES			
Professional fees	**194,994**	104,500	59,000
Taxes and licenses	**31,419**	27,652	12,653
Commission expense (Note 10)	**14,415**	–	–
Printing and reproduction	**–**	20,828	27,250
Advertising and promotions	**–**	5,148	24,750
Others	**15,932**	784	10,062
	256,760	158,912	133,715
INCREASE IN NET ASSET ATTRIBUTABLE TO UNITHOLDERS FROM OPERATIONS (Note 8)	**₱12,096,254**	₱4,465,778	₱650,665

See accompanying Notes to Financial Statements.

PHILEQUITY PSE INDEX FUND, INC.
(An Open-End Mutual Fund Company)

STATEMENTS OF CHANGES IN NET ASSETS ATTRIBUTABLE TO UNITHOLDERS

	Years Ended December 31		
	2006	2005	2004
NET ASSETS ATTRIBUTABLE TO UNITHOLDERS AT BEGINNING OF YEAR	**₱30,893,669**	₱26,427,891	₱21,083,217
INCREASE IN NET ASSET ATTRIBUTABLE TO UNITHOLDERS FROM OPERATIONS (Note 8)	**12,096,254**	4,465,778	650,665
FROM TRANSACTIONS WITH UNITHOLDERS			
Proceeds from subscriptions of capital stock - 736,368 shares in 2006	**1,050,000**	–	–
NET CHANGE IN UNREALIZED APPRECIATION OF INVESTMENTS IN LISTED SECURITIES (Note 8)	–	–	4,694,009
NET ASSETS ATTRIBUTABLE TO UNITHOLDERS AT END OF YEAR (Note 8)	**₱44,039,923**	₱30,893,669	₱26,427,891

See accompanying Notes to Financial Statements.

PHILEQUITY PSE INDEX FUND, INC.
(An Open-End Mutual Fund Company)

STATEMENTS OF CASH FLOWS

	Years Ended December 31		
	2006	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES			
Increase in net assets attributable to unitholders	**₱12,096,254**	₱4,465,778	₱650,665
Adjustments for:			
Gain on market valuation of FVPL securities	**(10,169,350)**	(3,293,487)	–
Net realized gain on sale of:			
FVPL securities	**(1,111,029)**	(419,566)	–
Investments in listed securities	**–**	–	(67,065)
Operating income before working capital changes	**815,875**	752,725	583,600
Decrease (increase) in:			
Financial assets at FVPL	**(1,093,838)**	(4,122,583)	–
Investments in listed securities	**–**	–	(680,937)
Receivables	**(1,090,695)**	43,241	23,317
Proceeds from sale of:			
Financial assets at FVPL	**2,794,263**	3,682,270	–
Investments in listed securities	**–**	–	666,724
Increase (decrease) in accrued expenses	**5,862**	(437)	665
	1,431,467	355,216	593,369
CASH FLOWS FROM FINANCIAL ACTIVITY			
Proceeds from issuance of capital stock	**1,050,000**	–	–
NET INCREASE IN CASH AND CASH EQUIVALENTS	**2,481,467**	355,216	593,369
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	**2,908,719**	2,553,503	1,960,134
CASH AND CASH EQUIVALENTS AT END OF YEAR	**₱5,390,186**	₱2,908,719	₱2,553,503

See accompanying Notes to Financial Statements.

PHILEQUITY PSE INDEX FUND, INC.
(An Open-End Mutual Fund Company)

NOTES TO FINANCIAL STATEMENTS

1. **Corporate Information**

Philequity PSE Index Fund, Inc. (the Fund) is incorporated in the Philippines. It was registered with the Philippine Securities and Exchange Commission (SEC) on February 22, 1999 as an open-end mutual fund company, the purpose of which is to, among others, engage in the sale of its capital stock and investing such proceeds in shares of stock that comprise the Philippine Stock Exchange (PSE) Composite Index.

Effective February 7, 2007, the registered address of the Fund is 2703-A (previously 2103-B), East Tower, Philippine Stock Exchange Centre, Exchange Road, Ortigas Center, Pasig City.

The accompanying financial statements of the Fund were approved and authorized for issuance by the Board of Directors (BOD) on March 21, 2007.

2. **Basis of Preparation**

The financial statements of the Fund have been prepared on the historical cost basis, except for financial assets at fair value through profit or loss (FVPL), which are measured at fair value. The financial statements are presented in Philippine peso, which is the Fund's functional and presentation currency, and all values are rounded to the nearest peso unit, unless otherwise stated.

Statement of Compliance
The financial statements of the Fund have been prepared in compliance with Philippine Financial Reporting Standards (PFRS) which include Philippine Accounting Standards (PAS) and Philippine Interpretations issued by the Financial Reporting Standards Council.

3. **Changes in Accounting Policies**

The accounting policies adopted are consistent with those of the previous financial year except for the adoption of the following new and amended PFRS and International Financial Reporting Interpretations Committee (IFRIC) interpretations during the year.

- Amendment to PAS 21, "The Effects of Changes in Foreign Exchange Rates"
- Amendment to PAS 39, "Financial Instruments: Recognition and Measurement"

The effects of these changes are described below:

- Amendment to PAS 21, "The Effects of Changes in Foreign Exchange Rates," requires all exchange differences arising from a monetary item that forms part of the Fund's net investment in a foreign operation to be recognized in a separate component of equity in the financial statements regardless of the currency in which monetary item is denominated. This change has no significant impact on the Fund's financial statements.

- Amendments to PAS 39, "Financial Instruments: Recognition and Measurement"

  Amendment for Financial Guarantee Contract (August 2005) — amended the scope of PAS 39 to require financial guarantee contracts that are considered to be insurance contracts to be recognized initially at fair value and to be measured at the higher of the amount determined in accordance with PAS 37, "Provisions, Contingent Liabilities and Contingent Assets" and the amount initially recognized less, when appropriate, cumulative amortization recognized in accordance with PAS 18, "Revenue". This amendment did not have an effect on the Fund's financial statements.

  Amendment for Hedges of Forecast Intragroup Transactions (April 2005) — amended PAS 39 to permit the foreign currency risk of a highly probable intragroup forecast transaction to qualify as the hedged item in a cash flow hedge, provided that the transaction is denominated in a currency other than the functional currency of the entity entering into that transaction and that the foreign currency risk will affect the statement of operations. As the Fund currently has no such transactions, the amendment did not have an effect on the Fund's financial statements.

  Amendment for the Fair Value Option (June 2005) — amended PAS 39 to restrict the use of the option to designate any financial asset or any financial liability to be measured at fair value through the statement of operations. The Fund had not previously used this option; hence, the amendment did not have an effect on the Fund's financial statements.

The following Philippine Interpretations are also effective for annual periods beginning on or after January 1, 2006 but are not relevant to the Fund:

- Philippine Interpretation IFRIC 5, "Rights to Interest Arising from Decommissioning, Restoration and Environmental Rehabilitation Funds"

- Philippine Interpretation IFRIC 6, "Liabilities Arising from Participating in a Specific Market - Waste Electrical and Electronic Equipment"

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

- PAS 1, "Amendment - Presentation of Financial Statements: Capital Disclosure." This amendment requires the Fund to make new disclosures that enable users to evaluate the significance of the Fund's objectives, policies and processes for managing capital. The new and revised disclosures provided by this standard will be included in the 2007 financial statements of the Fund.

- PFRS 7, "Financial Instruments - Disclosures." This standard requires disclosures that enable users to evaluate the significance of the Fund's financial instruments and the nature and extent of risks arising from those financial instruments. The new and revised disclosures on financial instruments provided by this standard will be included in the 2007 financial statements of the Fund.

- PFRS 8, “Operating Segments (effective for annual periods beginning on or after January 1, 2009).” This PFRS adopts a management approach to reporting segment information. PFRS 8 will replace PAS 14, “Segment Reporting,” and is required to be adopted only by entities whose debt or equity instruments are publicly traded, or are in the process of filing with the Securities and Exchange Commission for purposes of issuing any class of instruments in a public market. The Fund is not required to and will not adopt PFRS 8.

- Philippine Interpretation IFRIC 7, “Applying the Restatement Approach under PAS 29, Financial Reporting in Hyperinflationary Economies (effective for annual periods beginning on or after March 1, 2006).” This Interpretation provides guidance on how to apply PAS 29 when an economy first becomes hyperinflationary, in particular, the accounting for deferred income tax. The Interpretation has no impact on the Fund’s financial statements.

- Philippine Interpretation IFRIC 8, “Scope of PFRS 2.” This Interpretation requires PFRS 2 to be applied to any arrangements where equity instruments are issued for consideration which appears to be less than fair value. As there are no equity instruments issued within the scope of PFRS 2, the Interpretation had no impact on the financial statements of the Fund.

- Philippine Interpretation IFRIC 9, “Reassessment of Embedded Derivatives, (effective for financial years beginning June 1, 2006).” This Interpretation establishes that the date to assess the existence of an embedded derivative is the date the Fund first becomes a party to the contract, with reassessment only if there is a change to the contract that significantly modifies the cash flows. The Fund believes that adoption of the Interpretation will have no impact on the Fund’s financial statements when implemented in 2007.

- Philippine Interpretation IFRIC 10, “Interim Financial Reporting and Impairment (effective for annual periods beginning on or after November 1, 2006).” This Interpretation prohibits the reversal of impairment losses on goodwill and available-for-sale equity investments recognized in the Interim financial reports even if impairment is no longer present at the annual balance sheet date. This Interpretation has no significant impact on the Fund’s financial statements.

- Philippine Interpretation IFRIC 11, “PFRS 2 - Group and Treasury Share Transactions.” This Interpretation indicates how to account for circumstances where goods and services are received in return for a company’s own equity instruments and how to account circumstances when a parent company grants its own equity instruments to employee of a subsidiary. The Fund currently does not have any stock option plan and, therefore, does not expect this Interpretation to have a significant impact to its financial statements.

- Philippine Interpretation IFRIC 12, “Service Concession Arrangements (effective for annual periods beginning on or after January 1, 2008).” This Interpretation covers contractual arrangements arising from private entities providing public services and is not relevant to the Fund’s current operations.

4. **Summary of Significant Accounting Policies**

Cash and Cash Equivalents
Cash includes cash in banks. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash with original maturities of three months or less and that are subject to an insignificant risk of change in value.

Financial Instruments - Initial Recognition and Subsequent Measurement
Date of Recognition. Purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace are recognized on the settlement date.

Initial Recognition of Financial Instruments. All financial assets are initially measured at fair value. Except for securities valued at fair value through profit or loss, the initial measurement of financial assets includes transaction costs. The Fund classifies its financial assets in the following categories: financial assets at fair value through profit or loss, held-to-maturity financial assets, available-for-sale financial assets, and loans and receivables. The classification depends on the purpose for which the investments were acquired and whether they are quoted in the active market. Management determines the classification of its investments at initial recognition and, where allowed and appropriate, re-evaluates such designation at every reporting date.

a. Financial assets at fair value through profit or loss (FVPL)

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

   Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. Derivatives are also classified as held for trading unless they are designated as effective hedging instruments.

   Financial assets may be designated at initial recognition as at FVPL if the following criteria are met:

   (i) the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the financial assets or recognizing gains or losses on them on a different basis;

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

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

Financial assets at FVPL are recorded in the statement of assets and liabilities at fair value. Changes in fair value are recognized directly in earnings. Interest earned or incurred is recorded as interest income or expense, respectively, while dividend income is recorded in other operating income according to the terms of the contract, or when the right of the payment has been established.

The Fund's financial assets at FVPL include investments in listed and unlisted shares.

b. Loans and receivables

Loans and receivables are nonderivative financial assets with fixed or determinable payments that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not classified as "fair value through profit or loss," designated as "available-for-sale financial assets" or "held-to-maturity investments."

After initial measurement, loans and receivables are subsequently measured at amortized cost using the effective interest rate method, less allowance for impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are integral part of the effective interest rate. The amortization is included in the interest income in the statement of operations. The losses arising from impairment are recognized in provision for impairment losses in the statement of operations.

Included under this classification are the Fund's receivables.

c. Held-to-maturity investments

Held-to-maturity investments are quoted nonderivative financial assets with fixed or determinable payments and fixed maturities for which the Fund's management has the positive intention and ability to hold to maturity. Where the Fund sells other than an insignificant amount of held to maturity investments, the entire category would be tainted and reclassified as available-for-sale financial assets. After initial measurement, these investments are subsequently measured at amortized cost using the effective interest rate method, less impairment in value. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the effective interest rate. The amortization is included in interest income in the statement of operations. Gains and losses are recognized in income when the held-to-maturity investments are derecognized and impaired, as well as through the amortization process. The losses arising from impairment of such investments are recognized in the statement of operations. The effects of restatement on foreign currency denominated held-to-maturity investments are recognized in the statement of operations.

The Fund has no held-to-maturity investments.

d. Available-for-sale financial assets

Available-for-sale financial assets are those which are designated as such or do not qualify to be classified and designated as "fair value through profit or loss," "held-to-maturity" or "loans and receivables." They are purchased and held indefinitely and may be sold in response to liquidity requirements or changes in market conditions.

After initial measurement, available-for-sale financial assets are subsequently measured at fair value. The effective yield component of available-for-sale financial assets, as well as the impact of restatement on foreign currency-denominated available-for-sale financial assets, is reported in the statement of operations. The unrealized gains and losses arising from the fair valuation of available-for-sale financial assets are excluded, net of tax, from the statement of operations and are reported as net unrealized gain on available-for-sale financial assets in the equity section of the statement of assets and liabilities and in the statement of changes in net assets attributable to unitholders.

When the financial asset is disposed of, the cumulative gain or loss previously recognized in equity is recognized in the statement of operations. Where the Fund holds more than one investment in the same security, these are deemed to be disposed of on a first-in first-out basis. Interest earned on holding available-for-sale financial assets are reported as interest income using the effective interest rate. Dividends earned on holding available-for-sale financial assets are recognized in the statement of operations when the right of the payment has been established. The losses arising from impairment of such financial assets are recognized in the statement of operations.

The Fund has no available-for-sale financial assets.

Determination of Fair Value

The fair value of financial instruments traded in active markets at the balance sheet date is based on their quoted market price or dealer price quotations (bid price for long positions and ask price for short positions), without any deduction for transaction costs. When current bid and asking prices are not available, the price of the most recent transaction is used since it provides evidence of the current fair value as long as there has not been a significant change in economic circumstances since the time of the transaction. For all other financial instruments not listed in an active market, the fair value is determined by using appropriate valuation techniques. Valuation techniques include net present value techniques, comparison to similar instruments for which market observable prices exist, options pricing models, and other relevant valuation models.

Derecognition of Financial Assets and Liabilities

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

- the rights to receive cash flows from the asset have expired;
- the Fund retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a “pass-through” arrangement; or
- the Fund has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Fund has transferred its rights to receive cash flows from an asset or has entered into a "pass-through arrangement," and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognized to the extent of the Fund's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Fund could be required to repay.

On the other hand, a financial liability is derecognized when the obligation under the liability is discharged, cancelled or has expired.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability and the difference in the respective carrying amounts is recognized in the statement of operations.

Impairment of Financial Assets

The Fund assesses at each balance sheet date whether a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred "loss event") and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated.

For loans and receivables, the Fund assesses whether objective evidence of impairment exists. If there is objective evidence that an impairment loss on loans and receivables has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset shall be reduced through use of an allowance account and the amount of loss is charged to the statement of operations. Receivables, together with the associated allowance, are written off when there is no prospect of future recovery. The amount of the loss shall be recognized in the statement of operations. If, in a subsequent year, the amount of the estimated impairment loss decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is reduced by adjusting the allowance account. If write off is later recovered, any amounts formerly charged are credited account in the statement of operations.

Offsetting of Financial Instruments

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

Revenue
Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Fund and the revenue can be reliably measured. Revenues are recognized on the following bases:

a. Gain on sale of financial assets at FVPL, determined at the time of sale transaction calculated as the difference between the net sales proceeds and the net book value;

b. Interest, on a time proportion basis taking into account the effective yield on the asset; and,

c. Dividend, when the Fund's right to receive payment is established.

Net Asset Value (NAV) Per Share
NAV per share is computed by dividing net assets (total assets less total liabilities) by the number of shares issued and outstanding.

Transactions with Unitholders
Sales of units are recorded by crediting net assets attributable to unitholders for the amount received; redemptions are recorded by debiting this account.

Provisions
Provisions, if any, are recognized when the Fund has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. Where the Fund expects some or all of a provision to be reimbursed, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain the expense relating to any provision is presented in the statement of operations, net of any reimbursement. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and where appropriate, the risks specific to the liability.

Foreign Currency Transactions and Translations
Transactions in foreign currencies are recorded in Philippine peso using the exchange rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are restated using the exchange rate at the balance sheet date. Foreign exchange gains and losses are taken to the statement of operations.

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

Deferred Tax. Deferred income tax is provided using the liability method on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognized for all taxable temporary differences. Deferred tax assets are recognized for all deductible temporary differences, carryforward benefits of unused tax losses [such as net operating loss carryover (NOLCO)], to the extent that it is probable that future taxable income will be available against which the deductible temporary differences, and the carryforward benefits of unused NOLCO can be utilized.

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

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

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

Contingencies

Contingent liabilities are not recognized in the financial statements. They are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote. Contingent assets are not recognized in the financial statements but disclosed when an inflow of economic benefits is probable.

Subsequent Events

Post balance sheet events that provide additional information about the Fund's financial position at the balance sheet date (adjusting events) are reflected in the financial statements. Post balance sheet events that are not adjusting events are disclosed in the notes to financial statements when material.

5. Significant Accounting Judgments, Estimates and Assumptions

Judgments

In the process of applying the Fund's accounting policies, management has made judgments, apart from those involving estimations, which have significant effect on the amounts recognized in the financial statements and accompanying notes. The judgments are based upon management's evaluation of relevant facts and circumstances as of the date of the financial statements.

Functional Currency. The functional currency of the Fund has been determined to be the Philippine peso based on the economic substance of the underlying circumstances relevant to the Fund. The Philippine peso is the currency of the primary economic environment in which the Fund operates. It is the currency that mainly influences the Fund's revenue and expenses.

Estimates and Assumptions
The key assumptions concerning the future and other key sources of estimation uncertainty as of balance sheet date that have the most significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are as follows:

Fair Value of Financial Assets. Fair value determinations for the financial assets at FVPL are based generally on quoted prices.

While significant components of fair value measurement were determined using verifiable objective evidence, the amount of changes in the fair value of these financial assets would affect net assets.

Impairment of Financial Assets. In determining the fair values, management evaluates the financial health of the issuer and the industry and sector performance like changes in operational and financial cash flows. Any indication of deterioration in the above factors can have a negative impact on the fair value. The carrying value of the Company's financial assets at FVPL amounted to ₱37.5 million and ₱27.9 million as of December 31, 2006 and 2005, respectively.

6. Financial Assets at Fair Value Though Profit or Loss

This account consists of investments in the following:

	2006			2005		
	Number of Shares	**Cost**	**Market Value**	Number of Shares	Cost	Market Value
Philippine Long Distance Telephone Company	**2,930**	**₱2,666,901**	**₱7,471,500**	2,930	₱2,666,901	₱5,376,550
Ayala Corporation	**5,590**	**2,099,488**	**3,298,100**	5,590	2,099,488	1,760,850
Bank of the Philippine Islands	**46,397**	**1,727,403**	**2,946,210**	38,664	1,727,403	2,107,188
Ayala Land, Inc.	**183,800**	**1,487,462**	**2,802,950**	183,800	1,487,462	1,819,620
Globe Telecom, Inc.	**2,255**	**1,510,599**	**2,784,925**	2,255	1,510,599	1,657,425
SM Investment Corporation	**8,500**	**2,039,065**	**2,762,500**	8,500	2,039,065	2,040,000
San Miguel Corporation "A"	**32,559**	**1,636,970**	**2,197,732**	32,559	1,636,970	2,116,335
SM Prime Holdings, Inc.	**170,000**	**1,179,877**	**1,827,500**	170,000	1,179,877	1,343,000
San Miguel Corporation "B"	**20,847**	**1,178,506**	**1,615,643**	20,847	1,178,506	1,844,960
Metropolitan Bank & Trust Company	**27,900**	**1,317,723**	**1,436,850**	27,900	1,317,723	892,800
Equitable PCI Bank, Inc.	**12,400**	**932,821**	**1,029,200**	12,400	372,335	731,600
International Container Terminal Services, Inc.	**40,000**	**138,840**	**830,000**	40,000	138,840	372,000
Jollibee Foods Corporation	**16,900**	**259,675**	**709,800**	16,900	259,675	684,450
Banco De Oro	**15,000**	**478,925**	**690,000**	15,000	478,925	510,000
Petron Corporation	**160,000**	**317,645**	**656,000**	160,000	317,645	720,000
First Philippine Holdings Corporation	**9,580**	**220,203**	**603,540**	9,580	220,203	469,420
Aboitiz Equity Ventures, Inc.	**85,000**	**189,874**	**595,000**	85,000	189,874	408,000
Manila Electric Company "A"	**10,600**	**825,781**	**572,400**	10,600	825,781	151,050
Megaworld Corporation	**201,000**	**162,108**	**486,420**	201,000	162,108	241,200
Manila Electric Company "B"	**7,120**	**698,455**	**391,600**	7,120	698,455	154,860
Filinvest Land, Inc.	**173,437**	**296,310**	**371,155**	138,750	296,310	191,475
Manila Water Corporation	**32,000**	**211,830**	**300,800**	32,000	211,830	198,400
ABS-CBN Broadcasting Corporation	**14,400**	**468,629**	**291,600**	14,400	468,629	183,600
DMCI Holdings, Inc.	**42,000**	**136,752**	**256,200**	42,000	136,752	132,300
Philex Mining Corporation "A"	**50,000**	**57,343**	**202,500**	30,000	31,972	39,000
Benpres Holdings Corporation	**70,000**	**58,791**	**151,200**	70,000	58,791	75,600
Lepanto Consolidated Mining Company "B"	**438,750**	**118,907**	**118,462**	390,000	109,157	97,500
Belle Corporation	**84,000**	**157,394**	**94,080**	84,000	157,394	85,680
Manila Mining A	**600,000**	**12,658**	**14,400**	–	–	–
Manila Mining B	**400,000**	**9,258**	**10,400**	–	–	–

(Forward)

	2006			2005		
	Number of Shares	**Cost**	**Market Value**	Number of Shares	Cost	Market Value
Pilipino Telephone Corporation	–	₱–	₱–	197,000	₱582,884	₱679,650
Holcim Philippines, Incorporated	–	–	–	130,000	103,811	572,000
Metro Pacific Corporation	–	–	–	330,000	225,033	112,200
Digital Telecommunications Phils., Inc.	–	–	–	110,000	79,148	102,300
Philex Mining Corporation "B"	–	–	–	20,000	25,371	35,200
Philippine National Bank	–	–	–	700	47,303	22,050
Ionics, Inc.	–	–	–	9,500	141,346	10,450
		₱22,596,193	**₱37,518,667**		₱23,183,566	₱27,938,713

Upon adoption of PAS 39, investments in listed securities were designated as "Financial assets at FVPL" and changes in market values are included as "Gain on market valuation of FVPL securities" in the statements of operations.

As of March 21, 2007, the market value of financial assets at FVPL held as of December 31, 2006 amounted to ₱38.9 million.

Details of sale of financial assets at FVPL/investments in listed securities are as follows:

	2006	2005	2004
Proceeds from sale of:			
Financial assets at FVPL	**₱2,794,263**	₱3,682,270	₱–
Investments in listed securities	–	–	666,724
Less cost of investments sold	**1,683,234**	3,262,704	599,659
	₱1,111,029	₱419,566	₱67,065
Net realized gain on sale of:			
Financial assets at FVPL	**₱1,111,029**	₱419,566	₱–
Investments in listed securities	–	–	67,065
	₱1,111,029	₱419,566	₱67,065

7. **Cash and Cash Equivalents**

This account consists of:

	2006	2005
Cash in bank	**₱1,064,212**	₱300,995
Short-term deposits	**4,325,974**	2,607,724
	₱5,390,186	₱2,908,719

Cash in bank earns interest at the prevailing bank deposit rates. Short-term deposits are made for varying periods of up to three months depending on the immediate cash requirements of the Fund, and earn interest at the prevailing short-term deposit rates.

8. Net Assets Attributable to Unitholders

Under PAS 32, the units issued to shareholders are liabilities in substance. Accordingly, the accounting treatment and presentation of the units issued to shareholders are in accordance with PAS 32 for purposes of PFRS financial statements. However, under Republic Act No. 2629, Rules and Regulations Governing Investment Companies, investment companies including mutual funds shall be organized in the form of a stock corporation. Therefore, units issued to shareholders are legally considered as equity instruments.

This account consists of:

	2006		2005		2004	
	Number of Shares	**Amount**	Number of Shares	Amount	Number of Shares	Amount
Capital stock - ₱1 par value						
Authorized	**100,000,000**	**₱100,000,000**	100,000,000	₱100,000,000	100,000,000	₱100,000,000
Issued:						
Balance at beginning of year	**25,000,000**	**25,000,000**	25,000,000	25,000,000	25,000,000	25,000,000
Issuance	**736,368**	**736,368**	–	–	–	–
Balance at end of year	**25,736,368**	**25,736,368**	25,000,000	25,000,000	25,000,000	25,000,000
Additional paid-in capital:						
Balance at beginning of year		**–**		–		–
Issuance in excess of par value		**313,632**		–		–
Balance at end of year		**313,632**		–		–
Retained earnings (deficit):						
Balance at beginning of year		**5,893,669**		(33,769)		(684,434)
Effect of adoption of PAS 39		**–**		1,461,660		–
Net income		**12,096,254**		4,465,778		650,665
Balance at end of year		**17,989,923**		5,893,669		(33,769)
Unrealized appreciation (depreciation) of investments in listed securities:						
Balance at beginning of year		**–**		1,461,660		(3,232,349)
Effect of adoption of PAS 39		**–**		(1,461,660)		–
Net change in unrealized appreciation of investments in listed securities		**–**		–		4,694,009
Balance at end of year		**–**		–		1,461,660
		₱44,039,923		₱30,893,669		₱26,427,891
NAV per share		**₱1.711**		₱1.236		₱1.057

NAV per share is computed as follows:

	2006	2005	2004
Net assets	**₱44,039,923**	₱30,893,669	₱26,427,891
Number of shares outstanding	**25,736,368**	25,000,000	25,000,000
NAV per share	**₱1.711**	₱1.236	₱1.057

9. Income Tax

As of December 31, 2006, the Fund has temporary deductible expense amounting to ₱709,446, which pertains to the carryforward benefit of NOLCO, for which related deferred tax asset of ₱248,306 is not recognized in the statement of assets and liabilities as management believes that future taxable income will not be sufficient against which they can be utilized.

As of December 31, 2006, the NOLCO that can be claimed as deduction from normal taxable income follows:

Year Incurred	Expiry Year	Amount
2004	2007	₱253,924
2005	2008	198,762
2006	2009	256,760
		₱709,446

NOLCO amounting to ₱246,657 incurred in 2003 expired and was written-off in 2006.

Due to the enactment of Republic Act (RA) No. 9337, effective November 1, 2005, RCIT is at 35%. As of December 31, 2006 and 2005, the effective statutory income tax is at 35% and 32.5%, respectively. The deferred tax assets and liabilities were measured using the appropriate corporate income tax rate on the year it is expected to be reversed or settled.

A reconciliation between the Fund's provision for income tax computed at the statutory income tax rate to the provision for income tax as shown in the statements of operations is summarized as follows:

	2006	2005	2004
Income tax at statutory tax rate of 35% in 2006, 32.5% in 2005 and 32% in 2004	**₱4,233,689**	₱1,451,378	₱208,213
Tax effects of:			
Gain on market valuation of fair value through profit and loss securities	**(3,559,273)**	(1,070,383)	–
Net realized loss (gain) on sale of:			
Financial assets at FVPL	**(388,860)**	(136,359)	–
Investments in listed securities	**–**	–	(21,461)
Dividend income exempt from tax	**(298,648)**	(236,557)	(179,744)
NOLCO expired and written-off	**86,330**	75,111	76,682
Interest income subjected to final tax	**(76,774)**	(59,725)	(49,797)
Effect of change in tax rate	**–**	(20,186)	–
Change in unrecognized deferred tax assets	**3,536**	(3,279)	(33,893)
	₱–	₱–	₱–

10. **Management and Distribution Agreement (Agreement)**

The Fund has an existing Agreement with Philippine Management, Inc. (PMI). Pursuant to the terms of the Agreement, the Fund shall pay the following for services rendered by PMI:

a. Annual management fee of a maximum of 1.5% of the monthly average net asset value of the Fund's assets. The NAV shall be determined in accordance with the procedures agreed upon by both parties. As of December 31, 2006, the payment of management fee has not been made effective by the Fund and PMI.

b. Sales commission of a maximum of 3.5% of the cost of investment for every sale of the Fund's shares of stock. Sales commission amounted to ₱14,415 in 2006.

11. **Financial Risk Management Objectives and Policies**

Governance Framework
The Fund has established a risk management function with clear terms of reference and with the responsibility for developing policies on market, credit, liquidity and operational risk. It also supports the effective implementation of policies.

The policies define the Fund's identification of risk and its interpretation, limit structure to ensure the appropriate quality and diversification of assets to the corporate goals and specify reporting requirements.

Regulatory Framework
The operations of the Fund are also subject to the regulatory requirements of the SEC. Such regulations not only prescribe approval and monitoring of activities but also impose certain restrictive provisions (e.g., investment portfolios, capital requirements, etc.).

Financial Risk
The Fund is exposed to financial risk through its financial assets and financial liabilities. The most important components of this financial risk are credit risk, liquidity risk and market risk. The BOD reviews and approves policies for managing these risks and they are summarized below:

Credit Risk. Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss.

In respect of investment securities, the Fund secures satisfactory credit quality by setting maximum limits of portfolio securities with a single or group of issuers. The Fund also transacts only with institutions with high credit worthiness.

The Fund sets the maximum amounts and limits that may be advanced to or placed with individual corporate counterparties which are set by reference to their long term ratings.

The Fund credit risk exposure as of December 31, 2006 and 2005 represents the carrying value of cash and cash equivalents and financial assets at FVPL.

The Fund did not have any significant concentration of credit risk with a single counterparty or group of counterparties, geographical and industry segments as of December 31, 2006.

Liquidity Risk. Liquidity or funding risk is the risk that an entity will encounter difficulty in raising funds to meet commitments associated with financial instruments. Liquidity risk may result from either the inability to sell financial assets quickly at their fair values, counterparty failing on repayment of a contractual obligation, or inability to generate cash inflows as anticipated.

The Fund is exposed to daily cash redemptions of redeemable participating shares. It therefore invests the majority of its assets in investments that are traded in an active market and can be readily disposed of and only a limited proportion of its assets in investments not actively traded on a stock exchange.

The Fund manages liquidity through a liquidity risk policy which determines what constitutes liquidity risk for the Fund; specifies minimum proportion of funds to meet emergency calls; setting up of contingency funding plans; specify the sources of funding and the events that would trigger the plan; concentration of funding sources; reporting of liquidity risk exposures and breaches to the monitoring authority; monitoring compliance with liquidity risk policy and review of liquidity risk policy for pertinence and changing environment.

The table below analyzes financial assets of the Fund into their relevant maturity groups based on the remaining period at the balance sheet date to their contractual maturities or expected repayment dates as of December 31, 2006 and 2005:

		2006		
	Up to a Year	**2-5 Years**	**Over 5 Years**	**Total**
Financial assets at FVPL	**₱37,518,667**	**₱–**	**₱–**	**₱37,518,667**
Cash and cash equivalents	**5,390,186**	**–**	**–**	**5,390,186**
Receivables	**1,177,160**	**–**	**–**	**1,178,147**
	₱44,086,013	**₱–**	**₱–**	**₱44,087,000**

		2005		
	Up to a Year	2-5 Years	Over 5 Years	Total
Financial assets at FVPL	₱27,938,713	₱–	₱–	₱27,938,713
Cash and cash equivalents	2,908,719	–	–	2,908,719
Receivables	86,465	–	–	86,465
	₱30,933,897	₱–	₱–	₱30,933,897

Market Risk. Market risk is the risk of change in fair value of financial instruments from fluctuation in foreign exchange rates (currency risk), market interest rates (interest rate risk) and market prices (price risk), whether such change in price is caused by factors specific to the individual instrument or its issuer or factors affecting all instruments traded in the market.

The Fund structures levels of market risk it accepts through a market risk policy that determines what constitutes market risk for the Fund; basis used to fair value financial assets and liabilities; asset allocation and duration limit based on the Fund's chosen benchmark; diversification benchmarks by type of instrument and geographical area; sets out the net exposure limits by each counterparty or group of counterparties, geographical and industry segments; reporting of market risk exposures and breaches to the monitoring authority; monitoring compliance with market risk policy and review of market risk policy for pertinence and changing environment.

Price Risk. The Fund's price risk exposure at year-end relates to financial assets and liabilities whose values will fluctuate as a result of changes in market prices, principally FVPL equity securities.

Such investment securities are subject to price risk due to changes in market values of instruments arising either from factors specific to individual instruments or their issuers or factors affecting all instruments traded in the market.

The Fund's market risk policy requires it to manage such risks by setting and monitoring objectives and constraints on investment, diversification plan and limits on investments.

12. Fair Value of Financial Instruments

Fair value is defined as the amount at which the financial instrument could be exchanged in a current transaction between knowledgeable willing parties in an arm's-length transaction, other than in a forced liquidation or sale. Fair values are obtained from quoted market prices, discounted cash flow models and option pricing models, as appropriate. The following table sets forth the carrying values and estimated fair values of financial assets recognized as of December 31, 2006 and 2005.

	2006		2005	
	Carrying Value	**Fair Value**	Carrying Value	Fair Value
Financial assets:				
Financial assets at FVPL	**₱37,518,667**	**₱37,518,667**	₱27,938,713	₱27,938,713
Cash and cash equivalents	**5,390,186**	**5,390,186**	2,908,719	2,908,719
Receivables	**1,177,160**	**1,177,160**	86,465	86,465
	₱44,086,013	**₱44,086,013**	₱30,933,897	₱30,933,897
Financial liability -				
Accrued expenses	**₱46,090**	**₱46,090**	₱40,228	₱40,228

Fair values of financial assets are estimated as follows:

	Methods and Assumptions
Financial assets at FVPL	Fair values are based on quoted prices.
Cash and cash equivalents, receivables and accrued expenses	Due to the short term nature of the instrument, the fair value approximates the carrying amount.

13. **Related Party Disclosures**

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

Shares held by directors totaled 7 and 25.0 million as of December 31, 2006 and 2005, respectively.

The Fund has no key management personnel. The key management functions are being handled by Philequity Management, Inc.