



**BPI** Capital  
Corporation

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# 2018 ANNUAL REPORT

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## I. Corporate Policy

### a. Vision and Mission Statement

- i. Our vision is to be the Philippines' investment banking champion and to remain unsurpassed as the most trusted financial partner to the most respected names in business and major stakeholders in the Philippines.
- ii. We commit ourselves to creating value for our stakeholders by providing superior, efficient, innovative, and client-focused financial solutions with utmost integrity.

### b. Brand

- i. On February 5, 1976, BPI Capital was incorporated in the Philippines as a wholly-owned subsidiary of the Bank of the Philippine Islands (BPI), the first bank in the Philippines. For over 40 years, BPI Capital has maintained a leadership position in the banking and finance industry, making it the most trusted financial partner to the most respected names and major stakeholders in Philippine business.

### c. Business Model

- i. BPI Capital provides financial services to its clients. We provide an exceptional and comprehensive suite of capabilities in corporate finance and capital markets advisory, debt and equity underwriting, loan syndication, project finance, corporate restructuring, pre-IPO restructuring, mergers and acquisitions, merchant banking, securities distribution and trading, and other investment banking solutions. We are one of the leading investment banking firms in the country and one of the most trusted advisers in the Philippine capital markets.

## II. Financial Summary/Highlights and Review of Operations

|                                  | Consolidated  |               | Parent (Solo) |               |
|----------------------------------|---------------|---------------|---------------|---------------|
|                                  | Current Year  | Previous Year | Current Year  | Previous Year |
| <b>Profitability</b>             |               |               |               |               |
| Total Income, net of GRT         | 1,017,960,404 | 1,377,088,474 | 907,263,162   | 1,103,500,060 |
| Total Expenses                   | 473,515,458   | 553,360,298   | 274,189,430   | 296,763,818   |
| Income before Tax                | 544,444,946   | 823,728,176   | 633,073,732   | 806,736,242   |
| Net Income                       | 388,030,130   | 610,947,583   | 481,466,771   | 598,223,489   |
| <b>Select Balance Sheet Data</b> |               |               |               |               |
| Assets                           | 4,672,596,159 | 4,586,882,313 | 3,933,374,360 | 3,459,333,812 |
| Liabilities                      | 478,664,658   | 760,024,555   | 109,304,730   | 101,008,725   |
| Equity                           | 4,193,931,501 | 3,826,857,758 | 3,824,069,630 | 3,358,325,087 |
| <b>Select Ratios</b>             |               |               |               |               |
| Return on Average Equity         | 9.68%         | 12.96%        | 13.76%        | 14.02%        |
| Return on Average Assets         | 8.38%         | 8.99%         | 11.94%        | 13.16%        |

### III. Financial Condition and Results of Operations

#### a. Review of Operations

In 2018, BPI Capital Corporation and its subsidiary (the “Group”) generated PHP 388.03 million in consolidated Net Income, down 36% from the previous year. Major contributors to our results are as follows:

1. The Group posted a total revenue of PHP 1.02 billion (net of Gross Receipts Taxes of PHP 60.96 million), with approximately 88% coming from fees and commissions. Our revenues were primarily derived from over 37 landmark deals and transactions.
2. Fees and commissions, accounting for approximately 88% of the total revenues, decreased by 21% (PHP 259.91 million). This year’s net interest income of PHP 85.40 million, derived from lending and borrowing activities, also decreased by 26% (PHP 30.79 million). Dividend income from BPI Capital's investments in equity securities decreased by 13% (PHP 3.70 million).
3. Total expenses decreased by approximately 14% or PHP 79.8 million due to the decrease in overall compensation, fringe benefits, management and professional fees, brokerage and underwriting fees, and other operating expenses.
4. The Group’s cost to income ratio and return on average equity is at 46.52% and 9.68%, respectively.

The Group closed the year with PHP 4.67 billion in total assets, 2% higher than 2017’s PHP 4.59 billion. Key accounts noted below:

1. Deposits maintained with the Bangko Sentral ng Pilipinas (BSP) amounted to PHP 1.10 billion, 103% higher than PHP 541.03 million in 2017. This includes BPI Capital's placements in special deposit accounts with the BSP, short-term lending to BSP under a reverse repurchase agreement, and mandatory reserve deposits.
2. With the full implementation of PFRS 9, financial assets at fair value through profit or loss totaled PHP 773.43 million, lower than last year’s PHP 1.53 billion with a PHP 1.09 billion decrease in investment in various debt securities and a PHP 92.8 million decrease in investments in listed equity securities. However, this was offset by the transition adjustment on mutual funds Php 424.79 million.
3. Financial assets at fair value through other comprehensive income and investment securities at amortized cost were recorded at PHP 771.41 million and PHP 655.55 million, respectively.
4. The parent company’s Investment in Equity, amounting to PHP 202 million, pertains to the carrying cost of BPI Securities, BPI Capital’s wholly-owned subsidiary.
5. Net trade and other receivables substantially decreased from 2017’s PHP 537.36 million down to 2018’s PHP 219.67 million due to the collection of the previous year’s accrued fees.
6. Total liabilities decreased to PHP 478.66 million due to settlement of the retail treasury bond transaction and customers arising from brokerage transactions.

b. Highlights of Major Activities

|   |     | Deal Size         | BPI Capital Role   | Date of Issue/Close |
|---|-----|-------------------|--|---------------------|
| <b>Debt Capital Markets</b>   |     |                   |  |                     |
| Bounty Fresh's Acquisition of Tegal Group Holdings  | PHP | 16,500,000,000.00 | Joint Arranger and Bookrunner  | 10/31/2018          |
| Bank of the Philippine Islands Issued Its First US Dollar Bonds                             | USD | 600,000,000.00    | Sole Global Coordinator, Joint Bookrunner                                      | 9/30/2018           |
| International Finance Corporation's Maiden USD 90 million Green Bonds                       | PHP | 4,800,000,000.00  | Joint Lead Manager and Bookrunner  | 7/31/2018           |
| <b>Equity Capital Markets</b>   |     |                   |  |                     |
| Bank of the Philippine Islands, Inc. PHP 50.0 Billion Stock Rights Offering                 | PHP | 50,000,000,000.00 | Sole Global Coordinator and Lead Manager, Sole Domestic Manager                | 5/31/2018           |
| D.M. Wenceslao and Associates, Inc. PHP 8.15 Billion Initial Public Offering                | PHP | 8,150,000,000.00  | Joint Global Coordinator and Bookrunner, Domestic Lead Manager and Underwriter | 6/30/2018           |
| San Miguel Food & Beverage, Inc. PHP 39.2 Billion Follow-On Public Offering                 | PHP | 35,722,045,600.00 | Local lead Underwriter   | 12/31/2018          |
| Integrated Micro-Electronics, Inc. PHP 5.0 Billion Stock Rights Offering                    | PHP | 5,100,000,000.00  | Issue Manager, Bookrunner and Underwriter                                      | 3/31/2018           |
| Robinsons Land Corporation PHP 20.0 Billion Stock Rights Offering                           | PHP | 20,000,000,000.00 | Issue Manager, Bookrunner and Underwriter                                      | 2/28/2018           |
| <b>Project Finance</b>  |     |                   |  |                     |
| Apo Agua Infraestructura, Inc. Up to PHP 9.0 Billion Financing                              | PHP | 9,000,000.00      | Sole Mandated Lead Arranger, Bookrunner and Issue Coordinator                  | 12/31/2018          |
| MPCALA Holdings, Inc. Enters into a PHP 24.2 Billion Financing Agreement                    | PHP | 23,600,000,000.00 | Joint Mandated Lead Arranger   | 12/31/2018          |
| Cebu Cordova Link Expressway Corporation Up to PHP 19.0 Billion Financing                   | PHP | 19,000,000,000.00 | Participating Arranger   | 2/28/2019           |
| <b>Advisory</b>   |     |                   |  |                     |
| Advisory Services to AC Energy for the divestment of AC Energy's Thermal Power Company      |     |                   | Financial Advisor  | 10/31/2018          |
| Advisory Services to Ayala Education, Inc. for the acquisition of National Teachers College |     |                   | Financial Advisor  | 04/31/2018          |
| Advisory Services for the Merger of iPeople, Inc. and AC Education, Inc.                    |     |                   | Financial Advisor  | 5/31/2019           |

### c. Outlook and Major Strategic Initiatives

We have invested in and built an investment bank that is strong and relevant in the core and key disciplines of investment banking: Project Finance, Structured Finance, Debt and Equity Products, and Advisory.

We are prepared for what the future brings as we are built for scale, change, and flexibility. We expect the Philippines to continue to grow; our clients want to be part of that growth as well. We believe the path to growth has become more complex and uncertain but our unwavering commitment to serve our country and our clients is stronger than ever. Our focus on providing our clients with the best financial advice and execution enables us to take on any market condition and to leverage on the challenges and opportunities that may come our way.

We expect continued significant activity in the energy and infrastructure space as it is apparent that our growing country desperately needs these investments. However, these deals are very complex and generally take a few years to complete so the timing to close these projects remains uncertain.

We expect the fixed income market to accelerate as clients try to adapt their financing needs to a rapidly changing market environment. Best advice and execution will test and differentiate companies and investment houses in this challenging environment.

BPI Capital's strategic initiative is to intensify its marketing efforts to source new clients. For the capital markets space, this involves introducing new companies to the capital markets; for the project finance space, this involves strengthening focus on renewable projects.

### d. Challenges, Opportunities, and Responses

The investment banking business is generally a reflection of the projects undertaken by our clients and our government. BPI Capital's activities in 2018 were no exception to that. It was a challenging year characterized by spiking inflation, a slowdown in large-scale power projects, a tapering gross domestic product, and prevailing net foreign outflows.

We continue to remain positive on Philippine economic outlook and aim to contribute to Philippine capital market development by developing new investment products and innovative ways of doing things.

While domestic bank liquidity remains high and serves as the primary source of funding for many corporates, especially with banks raising or planning to raise capital through investments and stock rights offerings, banks have begun to realize the need to increase their discipline and focus on profitability. The capital markets continue to grow, but the fixed income market in particular has mainly served the larger and more familiar corporate names. We have done significant work to introduce new names and medium-sized companies to the capital markets. We work with clients of any size to advise them on their funding options to achieve their financial objectives.

We also continue to grow our advisory business, the genesis and interconnection for many of our deals and ideas. Our team has been active in the education, healthcare, consumer, utilities, infrastructure, and financials space.

## IV. Financial Results of Business Segments

### a. Segment Performance and Contribution

Corporate Finance generated PHP 718.1 million, accounting for 67% of 2018's total revenues. The biggest revenue contributor in Corporate Finance is the Equity Products, amounting to PHP 295 million. See below for a further breakdown of our revenue:

### **Contribution to Revenue**

| Financial Summary (Gross of GRT) | PHP           | %    |
|----------------------------------|---------------|------|
| Corporate Finance                | 718,100,198   | 67%  |
| Distribution Sales               | 28,064,753    | 3%   |
| Treasury Capital Market          | 112,062,543   | 10%  |
| Commission and Other Income      | 220,697,242   | 20%  |
| Total                            | 1,078,924,736 | 100% |

### **Breakdown of Corporate Finance revenue**

| Corporate Finance and Distribution Sales | PHP         | %    |
|--|-------------|------|
| Underwriting and Loan Syndication        | 676,324,105 | 91%  |
| Financial Advisory                       | 41,776,093  | 6%   |
| Broker's Fee                             | 18,190,337  | 2%   |
| Service Fee                              | 9,874,416   | 1%   |
| Total                                    | 746,164,951 | 100% |

### **Breakdown of Treasury Capital Markets revenue**

| Treasury Capital Markets  | PHP         | %    |
|---------------------------|-------------|------|
| Interest Income           | 78,138,568  | 70%  |
| Dividend Income           | 23,506,820  | 21%  |
| Trading (loss) gain, net  | 1,836,573   | 2%   |
| Net Foreign Exchange Gain | 6,646,398   | 6%   |
| Miscellaneous Income      | 1,934,184   | 2%   |
| Total                     | 112,062,543 | 100% |

#### **b. Significant Developments, Major Activities, and Future Plans/Objectives**

See III. *Financial Results and Results of Operations*

## **V. Risk Management Framework Adopted**

### **a. Overall risk management culture and risk management process**

As a wholly-owned subsidiary of the Bank of the Philippine Islands, BPI Capital's risk management and corporate governance frameworks follow that of our parent company. A detailed discussion of the risk culture and corporate governance structure can be found on the BPI website.

BPI Capital Corporation has a comprehensive and integrated Risk and Capital Management Framework guiding the management of all risk exposures and ensuring that the Company has adequate capital to cover and mitigate risks. This framework follows BSP regulations to implement an active and effective Internal Capital Adequacy Assessment Process ("ICAAP") and risk management processes that are consistent and form part of the BPI Group's ICAAP.

Following BPI's Risk Management top-down approach, our Board carries out its risk management function through its Risk Management Committee ("RMC"), which is tasked with nurturing a culture of risk management across the enterprise, proposing guidelines and regularly reviewing risk management structures, metrics, limits, and issues across the Company, in order to meet and comply with regulatory and international standards on risk measurement and management.

The RMC reviews the reports from the Company's various business units that are necessary to identify, monitor and assess the risk exposures and capital adequacy and its implications to the Company. It also reviews and recommends to the Board the approval of the Company's risk and capital management policies, and the appropriate capital structure for the bank in support of long-term strategic objectives, current business plans, and risk appetite.

At BPI Capital Corporation, we aim to achieve 99.5% availability of critical customer-facing services. We have low risk appetites and low tolerance for business process execution failures, improper business practices, damage to physical and intangible assets, vendor failures and damages, and trade counterparty failures. We aim to maintain compliance with regulatory requirements.

We apply industry standards in securing sensitive data and we strive to mitigate emerging risks with zero tolerance for data confidentiality and integrity breaches. We have zero appetite for events that compromise the health and safety of employees. We have zero appetite for any fraudulent activity.

We use established industry practices to deliver projects with minimal time, budget and quality variances. We innovate by adopting and customizing new, market-tested technologies with the key objective of providing our customers with the best experience and minimum risks.

#### b. Risk appetite and Strategy

We identify risks according to three major classifications – credit, market, and operational and IT risks. Credit risk is the risk to earnings arising from obligor's, customer's, or counterparty's failure to perform or to meet the contractual obligation in accordance with agreed terms. Market risk to earnings or capital arises from adverse movements in factors that affect market value of the financial assets (interest rate risk and liquidity risk). On the other hand, operational and IT risk is the loss resulting from inadequate or failed internal processes, people, and systems or from external events. This includes people and process risks, information security, technology and physical security risks, compliance and regulatory risks, legal and tax risks, and reputation risks amongst others.

With the parent bank establishing robust and effective risk management processes and controls, BPI Capital is able to manage risks closer to the source, either preventing them from happening or mitigating their impact. The Company uses various methodologies, tools, and systems to measure its risk exposure.

We continuously promote and observe a culture of proactive risk management and client-centricity, with the CRO and the Risk Management Office continuously engaging the RMC, management and business units, communicating the risk awareness culture to the rest through various internal channels, facilitating learning programs on risk management, and promoting best practices enterprise-wide.

#### *Credit Risk*

Under the organizational structure of BPI Capital, the management of credit risk is handled by the following:

1. Treasury and Capital Management Department ("TCMD") manages credit risk which may arise from its proprietary investment in non-marketable or unlisted securities, debt and equity linked instruments, and other strategic investments; a credit and counterparty risk from its trading portfolio of fixed income and equity securities, as well as pooled funds;
2. Fixed Income Sales manages credit risk which may arise from its brokerage services;
3. BPI Capital Investment Committee reviews all recommendations for trading lines and proprietary investment as proposed by the TCMD Officer; and

4. BPI Capital Board of Directors approves all investment recommendations and credit proposals endorsed by the Investment Committee.

We conduct prior due diligence whenever a strategic investment proposal is prepared to determine financial suitability, risk exposure, viability and profitability.

We measure our credit risk exposures in terms of regulatory capital requirement using the standardized approach in compliance with Basel and BSP Standards on minimum capital requirements. Using this method, our credit exposures to sovereigns, corporates and banks are risk-weighted to reflect credit assessment from eligible rating agencies.

We continuously enhance our credit policies and guidelines and align regulatory changes to enable robust analysis of the loan portfolio while delivering timely and accurate reporting of the Company's loan structures, credit concentrations, and other risk data analytics.

#### *Market, Interest Rate in the Baking Book, and Liquidity Risk*

Under the Market Risk Management unit, the Risk Officer employs various risk metrics commensurate to the size and sophistication of business operations, which guide the Company to effectively manage the risks arising from position-taking strategies balanced by the Board's overall risk appetite. Risk limits are continuously reviewed and updated to align with BPI Capital's goals, objectives, strategies, and enterprise-wide risk appetite.

We closely monitor the risk exposures of both trading and non-trading portfolios. Assets in both on- and off-balance sheet trading portfolios are marked-to-market and the resulting gains and losses are recognized through profit or loss. Market risk exposures from these portfolios are measured by using the historical simulation value at-at-risk model complemented by several risk metrics such as Stop Loss and DV01.

#### *Operational and IT Risk*

Concurrent with BPI's Operational and Information Technology Risk Management unit, BPI Capital monitors risks arising from inadequate or failed internal processes, people, and systems or from external fortuitous events that disrupt the business. Operational risk is inherent in all banking products and services, and may include risks that give rise to adverse legal, tax, regulatory or reputational consequences. Information technology is a significant risk factor assumed in conjunction with operational risk, given the highly automated nature of BPI Capital's processes and services. IT risk is any potential adverse outcome arising from the use of or reliance on IT (i.e hardware, software, devices, systems, applications and networks).

Our Business Risk Officer ("BRO") is responsible to the Risk Management Office (RMO) for promoting a sound risk management culture, implementing risk management best practices as determined by the RMO, and ensuring timely submission of operational, IT and other risk reports.

We monitor key risk indicators ("KRI"), and oversee the thoroughness of the Company' risk and control self-assessments, loss event management processes, and operational risk management awareness and appreciation programs. We manage our operational and IT risks by ensuring such risks are identified, assessed, monitored, reported and mitigated. We have defined responsibilities related to the performance of the risk management function, accountabilities, methods and tools employed to identify and mitigate operational and IT risks in our operating units. We require operating units to undertake regular self-assessments to identify risks, assess inherent and residual risks, identify controls, and assess the design and performance effectiveness of controls. KRIs are used to monitor risk profiles, trigger early warning alerts, and instigate mitigating action. Operational loss events, and the corresponding data collection and analysis provide meaningful information in effectively managing risks.

Our exposure to operational risks are identified, assessed, and monitored as an integral part of the risk assessment processes. We currently use the Basel regulatory basic indicator approach to quantify operational risk-weighted assets by using the historical total annual gross income as the main measure of risk.

c. Entity-wide risk governance structure and risk management process

We manage risks through clearly-defined functions, using the three lines of defense model to ensure effective risk management governance and control processes across the Company. The first line of defense is performed by functions that own and manage risks (i.e. business line management and personnel). They are primarily responsible for managing the risks in their respective areas. The second line of defense shall be performed by functions that oversee risks. The third line of defense is performed by the BPI Internal Audit, who provides independent assurance to the Board on the quality and effectiveness of the Company's risk management framework, including the implementation of the risk management policies and processes.

In order to thrive with our commitment and mission in creating value for our stakeholders by providing superior, efficient and client-focused financial solutions with utmost integrity, we exercise proactive and prudent risk management. BPI's Risk Management Office, headed by the Chief Risk Officer ("CRO"), leads the formulation of risk management policies and methodologies aligned with our strategy. The CRO, who is primarily responsible for the overall management of the BPI Group's total risk, ensures that risks are rationally undertaken, within the risk appetite, and commensurate to returns on capital. The CRO also supports the RMC by recommending risk management policies and methodologies. With this process, the CRO promotes an enterprise-wide risk management awareness, learning and appreciation.

We are exposed to interest rate risk on unfavorable changes in the interest rate curves, which would have adverse effects on the BPI Capital's earnings and its economic value of equity. Interest rate risk exposure arising from the core banking activities is measured by (a) earnings-at-risk ("EaR"), or the potential deterioration in net interest income over the next 12 months, and (b) balance sheet value-at-risk ("BSVaR"), or the impact on the economic value of the future cash flows in the banking book due to changes in interest rates. The interest rate gap model is measured based on the re-pricing schedule of the balance sheet accounts. For instance, the held-to-collect and available-for-sale securities in the banking book of BPI Capital are the subject to interest rate risk movement.

We ensure adequate liquidity levels at all times and contingency plans are in place in the event of liquidity stress. A Liquidity Contingency Funding Plan Testing ("LCFP Testing") is done periodically at least once a year, or as deemed necessary by the BPI Capital Treasurer in coordination with the Risk Officer, to establish awareness and preparedness among personnel. LCFP Testing aims to test effectivity of the company's liquidity sources and alternatives in order to refine assumptions, policies and procedures to make the funding plan implementable and relevant.

We continuously improve our liquidity and re-pricing gap models through improvements in model assumptions. Under assumed severe market stress scenarios, our CAR and CET1 are well above the minimum regulatory requirements.

d. AML governance and culture, and description of the overall Money Laundering (ML) / Terrorist Financing (TF) risk management framework

Prevention of financial crimes is a top priority of BPI, not only because they pose a significant threat to our reputation, but because they weaken the integrity of the global financial system. Our Compliance Office extends its ambit beyond the Bank, its policies, and its employees to ensure that our clients also act within the law and do not use the Bank for illegal activities.

BPI Capital adopts a comprehensive and risk-based Money Laundering and Terrorist Financing Prevention Program (MLPP) that ensures consistent and effective compliance with the BSP Circular

950, the AMLA, as amended, and its Revised Implementing Rules and Regulations (RIRRs), and with all internal policies related to anti-money laundering. These are geared toward the promotion of high ethical and professional standards and the prevention of the Company, and its employees from being used for money laundering and terrorist financing. It consists of conscientious customer due diligence and know-your-customer (KYC) processes; technology and tools to identify and detect financial transactions of a suspicious nature; and monitoring, periodic review, and timely reporting of anti-money laundering-combating the financing of terrorism (AML-CFT) events to management.

We constantly review our program to ensure compliance with the latest legislative and regulatory developments. To promote awareness, knowledge and understanding of AML concepts, principles and requirements, all employees attend in-house or external training programs.

| Description   | BPI Capital Response  |
|---|---|
| <b>Credit Risk</b>  |   |
| <p>It is the risk to earnings arising from the obligor's, customer's, or counterparty's failure to perform or to meet the contractual obligation in accordance with agreed terms.</p> | <p>Under the organizational structure of BPI Capital, the management of credit risk is handled by the business line management and personnel.</p> <p>We conduct prior due diligence whenever a strategic investment proposal is prepared to determine financial suitability, risk exposure, viability and profitability.</p> <p>We measure our credit risk exposures in terms of regulatory capital requirement using the standardized approach in compliance with Basel and BSP Standards on minimum capital requirements. Using this method, our credit exposures to sovereigns, corporates and banks are risk-weighted to reflect credit assessment from eligible rating agencies.</p> <p>We continuously enhance our credit policies and guidelines and align regulatory changes to enable robust analysis of the loan portfolio while delivering timely and accurate reporting of the Company's loan structures, credit concentrations, and other risk data analytics.</p> |
| <b>Market Risk</b>  |   |
| <p>This risk to earnings or capital arises from adverse movements in factors that affect market value of the financial assets.</p>  | <p>Under the Market Risk Management unit, the Risk Officer employs various risk metrics commensurate to the size and sophistication of business operations, which guide the Company to effectively manage the risks arising from position-taking strategies balanced by the Board's overall risk appetite.</p> <p>We closely monitor the risk exposures of both trading and non-trading portfolios. Assets in both on- and off-balance sheet trading portfolios are marked-to-market and the resulting gains and losses are recognized through profit or loss. Market risk exposures from these portfolios are measured by using the historical simulation value at-at-risk model complemented by several risk metrics such as Stop Loss and DV01.</p>  |
| <b>Interest Rate Risk in the Banking Book</b>   |   |
| <p>This risk type is inherent to our business operations, as movements in interest rates expose us to adverse shifts in the level of net interest income and could impair the</p>     | <p>We are exposed to interest rate risk on unfavorable changes in the interest rate curves, which would have adverse effects on the BPI Capital's earnings and its economic value of equity. Interest rate risk exposure arising from the core banking activities is measured by (a) earnings-at-risk (EaR), or the potential deterioration in net interest income over the next 12</p>   |

|  |  |
|--|--|
| underlying values of its assets and liabilities.   | months, and (b) balance sheet value-at-risk (BSVaR), or the impact on the economic value of the future cash flows in the banking book due to changes in interest rates. The interest rate gap model is measured based on the re-pricing schedule of the balance sheet accounts. For instance, the held-to-collect and available-for-sale securities in the banking book of BPI Capital are the subject to interest rate risk movement.   |
| <b>Liquidity Risk</b>  |  |
| <p>This is a potential risk arising from inability to meet the financial obligation to a client or counterparty on a timely payment or only being able to meet these obligations at excessive costs or losses.</p> <p>The inability to manage unplanned decreases or changes in funding sources.</p> <p>Arises from failure to recognize or address changes in market conditions that affect the ability to liquidate assets quickly and with minimal loss in value.</p> | <p>We ensure adequate liquidity levels at all times and contingency plans are in place in the event of liquidity stress. A Liquidity Contingency Funding Plan Testing (LCFP Testing) is done periodically at least once year, or as deemed necessary by the BPI Capital Treasurer in coordination with the Risk Officer, to establish awareness and preparedness among personnel.</p> <p>We continuously improve our liquidity and repricing gap models through improvements in model assumptions. Under assumed severe market stress scenarios, our CAR and CET1 are well above the minimum regulatory requirements.</p>  |
| <b>Operational and IT Risk</b>   |  |
| <p>This is the loss resulting from inadequate or failed internal processes, people, and systems or from external events. This includes people and process risks, information security, technology and physical security risks, compliance and regulatory risks, legal and tax risks, and reputation risks amongst others.</p>  | <p>Concurrent with BPI's Operational and Information Technology Risk Management unit, BPI Capital monitors risks arising from inadequate or failed internal processes, people, and systems or from external fortuitous events that disrupt the business.</p> <p>Our Business Risk Officer (BRO) is responsible to the Risk Management Office (RMO) for promoting a sound risk management culture, implementing risk management best practices as determined by the RMO, and ensuring timely submission of operational, IT and other risk reports.</p> <p>We monitor key risk indicators (KRI), and oversee the thoroughness of the Company' risk and control self-assessments, loss event management processes, and operational risk management awareness and appreciation programs.</p> <p>Our exposure to operational risks are identified, assessed, and monitored as an integral part of the risk assessment processes. We currently use the Basel regulatory basic indicator approach to quantify operational risk-weighted assets by using the historical total annual gross income as the main measure of risk.</p> |

## VI. Corporate Governance

### a. Overall corporate governance structure and practices

The Board of Directors and stockholders, Management, and employees of BPI Capital Corporation believe that sound and effective corporate governance is the cornerstone of BPI Capital's strength and

long-term existence. It subscribes to a philosophy of adhering to honesty, integrity and professionalism in the conduct of its business, exercising prudence in arriving at decisions, enforcing internal discipline and a system of checks and balances in its operating processes, and providing transparency to its various publics regarding basic management policies and practices, major business strategies and decisions, and its operating results.

The Board of Directors is ultimately responsible in ensuring that consumer protection practices are embedded in BPI Capital's various business operations. The Board and Senior Management are responsible for the development of BPI Capital's consumer protection strategy and establishment of an effective oversight over BPI Capital's consumer protection programs. In their respective capacities, they shall have further responsibilities as follows:

#### *Board of Directors*

1. Approving BPI Capital's consumer protection policies as well as the mechanism to ensure compliance with said policies, including policies and mechanisms related to the consumer assistance management process;
2. Overseeing the implementation of, and compliance with, BPI Capital's consumer protection policies by monitoring the performance of Senior Management in managing the day-to-day consumer protection activities of BPI Capital; and
3. Developing and maintaining a sound Consumer Protection Risk Management System (CPRMS) that is integrated into the overall framework for the entire product/service life cycle.

The Board may delegate other duties and responsibilities to a board-level Committee or to a Senior Management but not the function of overseeing compliance with the prescribed consumer protection framework/policies.

#### *Senior Management*

1. Implementing the consumer protection policies approved by the Board;
2. Managing BPI Capital's day-to-day consumer protection activities; and
3. Other duties and responsibilities delegated by the Board or its designated committee.

#### b. Selection process for the Board and Senior Management

As disclosed in the Manual of Corporate Governance, candidates for board membership may be recommended by shareholders to the Nominations Committee through the Office of the Corporate Secretary. Among other qualifications, candidates must be fit and proper for the position of director, taking into consideration integrity, physical/mental fitness, relevant education/financial literacy/training, possession of competencies relevant to the job such as knowledge and experience, skills, diligence and independence of mind and sufficiency of time to carry out responsibilities. Candidates recommended by shareholders are evaluated in the same manner as director candidates identified by any other means. The Committee itself may identify and recommend qualified individuals for nomination and election to the Board.

Board members are elected by BPI stockholder who are entitled to one vote per share at the company's Annual Stockholder's Meeting, where votes may be cumulated as provided for in the Corporation Code. The nominees receiving the highest number of votes are declared elected and hold office for one year until their successors, qualified in accordance with the by-laws, are elected at the next Annual Stockholders Meeting.

c. Board's overall responsibility

The Board of Directors (the Board) bears the primary responsibility for creating and enhancing the long-term value of BPI Capital and ensuring that this objective is achieved in all its business activities. It must ensure the Company's ability to satisfy the needs of its customers, sustain its leadership and competitiveness, and uphold its reputation in order to maintain BPI Capital's long-term success and viability as a business entity. Its mandate consists of setting the strategic business directions of BPI Capital, appointing its senior executive officers, confirming its organizational structure, approving all major strategies and policies, overseeing all major risk-taking activities, monitoring the financial results, measuring and rewarding the performance of management, and generating a reasonable investment return to stockholders. It shall also provide an independent check on management.

The charter of the Board of Directors articulates with specificity the governance and oversight responsibilities exercised by the directors and their roles and functions in the Company. The Board Charter is incorporated in our Manual of Corporate Governance. The Company's updated and revised Manual of Corporate Governance was approved and adopted by our Board of Directors on June 21, 2017.

d. Description of the role and contribution of executive, non-executive and independent directors, and of the chairman of the Board

The Board of Directors is ultimately responsible in ensuring that consumer protection practices are embedded in BPI Capital's various business operations. The Board and Senior Management are responsible for the development of BPI Capital's consumer protection strategy and establishment of an effective oversight over BPI Capital's consumer protection programs. In their respective capacities, they shall have further responsibilities as follows:

*Chairman*

The Chairman of the Board, shall, when present, preside at all meetings of the Board and shall render advice and counsel to the President. He shall:

1. Ensure that the meetings of the Board are held in accordance with the By-Laws of BPI Capital or as the Chairman may deem necessary;
2. Supervise the preparation of the agenda of the meeting in coordination with the Corporate Secretary, taking into consideration the suggestions of the CEO, Management, and the directors;
3. To provide leadership in the board of directors. The chairperson of the board shall ensure effective functioning of the board, including maintaining a relationship of trust with board members;
4. Maintain qualitative and timely lines of communication and information between the Board and the Management;
5. Exercise control over quality, quantity, and timeliness of the flow of information between the Management and the Board;
6. Assist in ensuring compliance with the Corporation's guidelines on corporate governance; and
7. To ensure that the board takes an informed decision. The chairperson of the board shall ensure a sound decision-making process and he should encourage and promote critical discussions and ensure that dissenting views can be expressed and discussed within the decision-making process.

The Chairman shall have such other responsibilities as the Board of Directors may impose upon him.

e. Board composition and qualification as of December 31, 2018

| # | Member                         | Board* | Officer   | Shares | % of Shares | Nat. | Years Served  | Age |
|---|--------------------------------|--------|-----------|--------|-------------|------|---------------|-----|
| 1 | Cezar P. Consing               | C      | Chairman  | 1      | 0           | Fil. | 6 yrs.        | 59  |
| 2 | Reginaldo Anthony B. Cariaso** | M      | President | 1      | 0           | Fil. | 1 yrs, 11 mos | 51  |
| 3 | Gerardo C. Ablaza, Jr.         | M      | N/A       | 1      | 0           | Fil. | 1 yrs, 11 mos | 65  |
| 4 | Jesse O. Ang                   | I      | N/A       | 1      | 0           | Fil. | 10 mos        | 59  |
| 5 | Romeo L. Bernardo***           | I      | N/A       | 1      | 0           | Fil. | 16 yrs, 7 mos | 64  |
| 6 | Rebecca G. Fernando            | M      | N/A       | 1      | 0           | Fil. | 10 yrs, 1 mos | 70  |
| 7 | Aurelio R. Montinola III       | M      | N/A       | 1      | 0           | Fil. | 12 yrs        | 67  |
| 8 | Mercedita S. Nollado           | M      | N/A       | 1      | 0           | Fil. | 16 yrs        | 77  |
| 9 | Antonio Jose U. Periquet       | I      | N/A       | 1      | 0           | Fil. | 9 yrs         | 57  |

\* C = Chairman; M = Member; I = Independent Director

\*\* Replaced by Rhoda A. Huang on May 1, 2019

\*\*\* Replaced by Ignacio R. Bunye on June 19, 2019

The Board of Directors has nine (9) members who are elected by the stockholders entitled to vote at the annual meeting. Board membership is effective for one (1) year and until their successors are elected and qualified in accordance with the By-Laws of the corporation.

To the extent practicable, the members of the board of directors shall be selected from a broad pool of qualified candidates. The position of Director of BPI Capital is a position of trust. A sufficient number of qualified non-executive members shall be elected to promote the independence of the board from the views of senior management. For this purpose, non-executive members of the board of directors shall refer to those who are not part of the day-to-day management of banking operations and shall include the independent directors.

In accordance with Securities and Exchange Commission (SEC) Memo Circular No. 6, Series 2009 on the Revised Code of Corporate Governance and BSP Circulars 749, 969, 970, 971, 972, BPI Capital shall conform to the legal requirement to have at least 1/3, but not less than two (2) members of the Board of Directors, who shall be independent directors.

Our Board of Directors enjoys the trust and respect of the local and international business community. They are established professionals who provide perspective, objectivity, practical wisdom, and sound judgment in their oversight, recommendations and evaluation of bank operations and management. Imbued with public interest, qualifications for membership in our Board of Directors are dictated by our Amended By-laws, Manual of Corporate Governance, the Corporation Code, and relevant regulations of the Bangko Sentral ng Pilipinas and the Securities and Exchange Commission.

*Cezar P. Consing*

Filipino, 59 years old, Executive Director, has, since 2013, been President and Chief Executive Officer of Bank of the Philippine Islands (BPI), and a Senior Managing Director of Ayala Corporation, BPI's controlling shareholder. He has been in the BPI Capital board since May 2013.

He has served on BPI's Board of Directors for 16 years (1995 - 2000, 2004 - 2007, 2010 - present), including 5 years representing J.P. Morgan & Co., then BPI's second largest shareholder, and 3 years as an Independent Director. Mr. Consing serves as Chairman of BPI's thrift bank, investment bank, UK bank, property and casualty insurance, leasing, and rental subsidiaries, and Vice Chairman of the

BPI Foundation. He is also a board director of BPI's life insurance, asset management, and microfinance subsidiaries. Mr. Consing is a member of BPI's Executive Committee, and is Chairman of its Credit and Management Committees.

Mr. Consing serves as Chairman of publicly listed National Reinsurance Corporation, President and board director of Bancnet, Inc., and LGU Guarantee Corporation, three industry consortium institutions where BPI is a minority shareholder.

Outside his association with BPI, Mr. Consing serves as an Independent Director of publicly listed Jollibee Foods Corporation (2010 – Present). He presently also serves on the boards of four private companies: The Rohatyn Group, Sqreem Technologies, FILGIFTS.com and Endeavor Philippines. Previously, he also served as an Independent Director of Malaysia-based CIMB Group Holdings (2006 - 2013) and First Gen Corporation (2005 - 2013), which is listed on the PSE. He is also a board director of the US-Philippines Society and a trustee of the Manila Golf Club Foundation. Mr. Consing has been a member of the Trilateral Commission since 2014.

Mr. Consing first worked for BPI in Corporate Planning and Corporate Banking, from 1980 - 1985. He worked for J.P. Morgan & Co., based in Hong Kong and Singapore, from 1985 - 2004, rising to co-head and head the firm's investment banking business in Asia Pacific from 1997 - 2004, and head J.P. Morgan Securities (Asia Pacific) Ltd. in the last five years as President of J.P. Morgan Securities (Asia Pacific) Ltd. As a senior Managing Director of J.P. Morgan, Mr. Consing was a member of the firm's global investment banking management committee and its Asia Pacific management committee. Mr. Consing was a partner at The Rohatyn Group from 2004 - 2013, headed its Hong Kong office and its private investing business in Asia, and was a board director of its real estate, and energy and infrastructure private equity investing subsidiaries.

*Reginaldo Anthony B. Cariaso*

Filipino, 51, Non-Executive Director, became a member of the BPI Capital Board in June 2017.

Mr. Cariaso joined BPI Capital in 2013 and is currently the Co-Head of Investment Banking and Chief Operating Officer. He is also the Chairman of BPI Securities, the brokerage arm of the Bank of the Philippine Islands. Mr. Cariaso serves on the board of several corporations and is a member of the board of directors of the Investment House Association of the Philippines (IHAP) and a member of the Capital Markets Development Committee of the Bankers Association of the Philippines (BAP).

Prior to joining BPI Capital, Mr. Cariaso worked in investment banking for Nomura International and JP Morgan based in Hong Kong covering Asia ex-Japan.

He has extensive experience originating and executing corporate advisory and capital markets transactions, in a variety of industries, including financial institutions, across Asia and the Philippines. Since joining BPI Capital, the firm has executed a number of landmark transactions in the Philippines including some of the largest debt capital markets deals, innovative project and structured financings and brought some of the most familiar names to the public equity markets, most recent of which is the Initial Public Offering of Pilipinas Shell Petroleum Corporation last 3 November 2016.

Mr. Cariaso was a Lieutenant in the United States Navy and received a B.A. degree from the University of Pennsylvania.

*Gerardo C. Ablaza, Jr.*

Filipino, 65 years old, Non-Executive Director, was elected as Director of BPI Capital in June 2017.

He is currently a Management Consultant at the Ayala Corporation and a member of the Board of Directors in publicly listed Manila Water Company, Inc., as well as other Ayala subsidiaries including AC Energy, AC Health, AC Infrastructures and Ayala Foundation.

From 2010 to 2017, Mr. Ablaza was the President and CEO of Manila Water Company. He was responsible for overseeing the financial and operational growth within Manila Water's service areas in

the Metro Manila East Zone and in its expansion areas. From 1998 to April 2009, he was President and CEO of Globe Telecom, Inc. During this period, he took the company from being the fourth-ranked mobile services provider to the second-largest full-service telecom operator with a subscriber base of 25 million in 2008.

In 2004, Mr. Ablaza was recognized by CNBC as the Asia Business Leader of the Year, making him the first Filipino CEO to win the award. He was also awarded by Telecom Asia as the Best Asian Telecom CEO. In 2013, he was recognized for his consistent leadership and innovation across the banking, investment, telecommunications and utility service industries through the Citi Distinguished Alumni Award for Leadership and Ingenuity. He was the first Filipino to be awarded with such an honor.

In June 2015, he became a member of the International Advisory Panel of the Institute for Water Policy under the Lee Kuan Yew School of Public Policy in Singapore. In 2017, he became a member of the Board of Directors and Executive Committee of Advance Info Services, PLC based in Thailand.

Mr. Ablaza graduated summa cum laude from the De La Salle University in 1974 with a degree in Liberal Arts, major in Mathematics (Honors Program). As one of the most accomplished graduates of his alma mater, he sits as a member of the Board of Trustees in various De La Salle schools in the country.

*Jesse O. Ang*

Filipino, 59 years old, Non-executive Director, has served as a member of the Board of Directors of BPI Capital since July 18, 2018.

Mr. Ang is also an Independent Director at BPI Asset Management Corporation having assumed such position on June 29, 2018.

Prior to joining BPI Capital, he was the Principal Investment Officer of the International Finance Corporation with over 18 years of experience at the IFC.

He graduated with a B.S. Industrial Engineering degree from the University of the Philippines in 1981 and an MBA from Wharton Business School in 1985.

*Romeo L. Bernardo*

Filipino, 64 years old, Independent Director, has served as a member of the Board of Directors of BPI Capital since October 2002.

He is the Chairman of the Bank's Nomination Committee and a member of the Personnel & Compensation, Related Party Transaction, and Risk Management Committees. He also serves as Independent Director of BPI Capital Corporation, BPI/MS Insurance Corporation, BPI-Philam Life Assurance Corporation and BPI Asset Management and Trust Corporation. Mr. Bernardo also serves as an Independent Director of the following listed companies: Aboitiz Power Corporation, National Reinsurance Corporation of the Philippines, and RFM Corporation. He is also a Non-Executive Director in publicly listed Globe Telecom, Inc. He is also Chairman of the Board of Directors (Independent) of Ayala Life Fixed-Income Fund; the Peso, Dollar, Euro, Growth, Money Market Bond Funds. He also serves as a Board Director of Management Association of the Philippines and Finex Foundation.

Mr. Bernardo is a former undersecretary of the Department of Finance and founded his consultancy practice, Lazaro Bernardo Tiu & Associates in 1997. He has been advisor to various multilateral institutions such as the World Bank, International Finance Corporation, Asian Development Bank, and Japan International Cooperation Agency. He has also worked with government institutions and the National Economic Development Authority (NEDA) in policy matters involving pension reform, capital markets reform, and fiscal and debt management.

He is, likewise, a public advocate of good corporate and national governance and frequently writes on the subject in his capacity as Vice Chair and Co-Founder of the Foundation for Economic Freedom and

the Philippine Partner of GlobalSource Partners, Inc., a worldwide association of country-based experts providing insights on global emerging markets.

Mr. Bernardo graduated with a B.S. Business Economics degree, magna cum laude, from the University of the Philippines in 1974. He obtained his M.A. Development Economics at Williams College, Williamstown, Massachusetts, graduating as valedictorian in 1977.

*Rebecca G. Fernando*

Filipino, 70 years old, Non-Executive Director, has served on the BPI Capital board since April 2009.

Ms. Fernando is a member of the following Committees in BPI: Executive Committee, Related Party Transaction Committee and Retirement/Pension Committee. She is also a member of the Board of Directors of BPI Capital Corporation, BPI Family Savings Bank, Inc., and BPI Asset Management and Trust Corporation.

Ms. Fernando is the Financial Consultant and Member of the Finance Boards of The Roman Catholic Archbishop of Manila and of The Roman Catholic Archbishop of Antipolo.

She graduated with a BSBA degree major in accounting from the University of the Philippines in 1970. She took further studies for an MBA at the University of the Philippines and attended an Executive Program on Transnational Business at the Pacific Asian Management Institute at the University of Hawaii. She is a Certified Public Accountant.

*Aurelio R. Montinola III*

Filipino, 67 years old, Non-Executive Director, has been a member of the Board of Directors of BPI Capital since April 2007.

Mr. Montinola also served as President and Chief Executive Officer of BPI for eight years from 2005 to 2013, and BPI Family Savings Bank, Inc. for twelve years from 1992 to 2004. He is a member of the Bank's Executive, Risk Management, Personnel & Compensation and Nomination Committees.

Among the several BPI subsidiaries and affiliates, Mr. Montinola serves as member of the Board of Directors of the following: BPI Capital Corporation; BPI Direct BankKo, Inc.; BPI Family Savings Bank, Inc.; BPI/MS Insurance Corporation; and BPI-Philam Life Assurance Corporation.

Mr. Montinola is the Chairman of the Board and Non-Executive Director of Far Eastern University and an Independent Director of Roxas and Company, both listed companies. Since May 2017, he is also an Independent Director of Xeleb Technologies, Inc., a subsidiary of publicly listed Xurpas, Inc. He is also Chairman of the Nicanor Reyes Educational Foundation Inc., Roosevelt Colleges, Inc., East Asia Computer Center Inc., Amon Trading Corporation, and the Kabang Kalikasan ng Pilipinas Foundation, Inc. He is also a member of the Board of Trustees of BPI Foundation Inc. and Philippine Business for Education Inc. where he sits as Vice-Chairman.

Significant awards received by Mr. Montinola include Management Man of the Year 2012 (Management Association of the Philippines), Asian Banker Leadership Award (twice), and Legion d'Honneur (Chevalier) from the French Government. He obtained his Bachelor of Science in Management Engineering Degree at the Ateneo de Manila University in 1973 and his MBA from the Harvard Business School in 1977.

*Mercedita S. Nolleto*

Filipino, 77 years old, Non-Executive Director, has been a member of the Board of Directors of BPI Capital since April 2003.

She is the Chairman of the Bank's Retirement & Pension Committees and a member of the Executive Committee and Corporate Governance Committee. Ms. Nolleto is also a Director in the following BPI

subsidiaries and affiliates: BPI Investment Management, Inc., where she sits as Chairman; BPI Family Savings Bank, Inc.; BPI Capital Corporation, and BPI Asset Management and Trust Corporation.

Ms. Nolloedo serves as a Non-Executive Director of publicly listed Xurpas, Inc.; and, since 2016, is an Independent Director of listed company D&L Industries, Inc. She is also a Director of the following companies: Ayala Land Commercial REIT, Inc., Michigan Holdings, Inc., and Anvaya Cove Beach and Nature Club, Inc. She is also a member of the Board of Trustees of the Ayala Foundation, Inc. and BPI Foundation, Inc. as well as Vice-President of Sonoma Properties, Inc. She was previously also a member of the Board of Directors of Ayala Corporation from 2004 until September 2010.

Ms. Nolloedo graduated with the degree of Bachelor of Science in Business Administration major in Accounting (magna cum laude) from the University of the Philippines in 1960 and placed second at the Certified Public Accountant Licensure Board Examination administered in the same year. In 1965, she obtained her Bachelor of Laws degree (cum laude) also from the University of the Philippines where she also placed second at the Bar Examination held in the same year.

*Antonio Jose U. Periquet*

Filipino, 57 years old, Independent Director, has been an independent member of the BPI Capital Board since May 2010.

He is a member of the Bank's Executive Committee. He is the Chairman/ Independent Director of BPI Asset Management and Trust Corporation and serves as an Independent Director of BPI Capital Corporation and BPI Family Savings Bank, Inc. Mr. Periquet is an Independent Director of the following publicly listed companies: ABS-CBN Corporation; ABS-CBN Holdings; Ayala Corporation; DMCI Holdings, Inc.; Max's Group of Companies; and Philippine Seven Corporation. He is the Chairman of the Campden Hill Group, Inc. and Pacific Main Holdings and an Independent Director of Albizia ASEAN Tenggara Fund. He is a member of the Board of Trustees of Lyceum University of the Philippines and a member of the Dean's Global Advisory Council at the University of Virginia's Darden School of Business.

Mr. Periquet graduated from the Ateneo de Manila University with an AB Economics degree in 1982. He also holds a Master of Science degree in Economics from Oxford University and an MBA from the University of Virginia.

f. List of board-level committees

*Audit Committee*

The Audit Committee monitors and evaluates the adequacy and effectiveness of the Company's internal control system, including financial reporting control and information technology security. This committee provides oversight on the overall management of operating risks, financial reporting and control, internal audit department and external auditors, quality of compliance with the Corporate Governance Manual and reviews conducted by the Bangko Sentral ng Pilipinas.

Chairman: Romeo L. Bernardo

Members: Rebecca G. Fernando, Jesse O. Ang

*Risk Management Committee*

The Risk Management Committee oversees and manages the Company's exposures to financial and non-financial risks and monitors the regulatory and internal capital adequacy vis-a-vis these exposures to risks. The committee nurtures a culture of risk management across the entity and implements and oversees the company's risk management program to assist the Board in fulfilling its responsibilities relating to the management of risks.

Chairman: Antonio Jose U. Periquet

Members: Romeo L. Bernardo , Mercedita S. Nolleo

*Nomination Committee*

The Nominations Committee ensures that the Board of Directors is made up of individuals of proven integrity and competence, and that each possesses the ability to resolve to effectively oversee the Company in his capacity as board member and member in their respective board committee. This Committee also reviews and evaluates the qualifications of all persons nominated to the Board.

Chairman: Cezar P. Consing

Members: Romeo L. Bernardo, Aurelio R. Montinolla, III

*Personnel and Compensation Committee*

The Personnel and Compensation Committee directs and ensures the development and implementation of long-term strategies and plans for the Company's human resources, in alignment with the Board's vision for the organization.

Chairman: Cezar P. Consing

Members: Romeo L. Bernardo, Aurelio R. Montinolla, III

g. Directors' attendance at Board and committee meetings as of December 31, 2018

| #  | Director                     | Board of Directors | Audit Committee | Risk Management Committee | Personnel and Compensation Committee | Nominations Committee |
|----|------------------------------|--------------------|-----------------|---------------------------|--------------------------------------|-----------------------|
| 1  | Gerardo C. Ablaza, Jr.       | 85%                | N/A             | N/A                       | N/A                                  | N/A                   |
| 2  | Jesse O. Ang*                | 83%                | 100%            | N/A                       | N/A                                  | N/A                   |
| 3  | Romeo L. Bernardo            | 100%               | 100%            | 100%                      | 100%                                 | 100%                  |
| 4  | Reginaldo Anthony B. Cariaso | 100%               | N/A             | N/A                       | N/A                                  | N/A                   |
| 5  | Cezar P. Consing             | 100%               | N/A             | N/A                       | 100%                                 | 100%                  |
| 6  | Rebecca G. Fernando          | 100%               | 100%            | N/A                       | N/A                                  | N/A                   |
| 7  | Aurelio R. Montinola III     | 92%                | N/A             | N/A                       | 100%                                 | 100%                  |
| 8  | Mercedita S. Nolleo          | 100%               | N/A             | 100%                      | N/A                                  | N/A                   |
| 9  | Simon R. Paterno**           | 100%               | N/A             | N/A                       | N/A                                  | N/A                   |
| 10 | Antonio Jose U. Periquet***  | 100%               | 100%            | 100%                      | N/A                                  | N/A                   |

\* Effective July 18, 2018

\*\* Board member until July 17, 2018

\*\*\* Audit committee member until July 17, 2018

h. List of Executive Officers/Senior Management as of December 31, 2018

| List of Executive Officers / Senior Management |   |
|--|---|
| Reginaldo Anthony B. Cariaso*                  | President   |
| Rhoda A. Huang                                 | Head of Advisory and Equity Capital Markets       |
| Franciso Javier P. Bonoan                      | Head of Structured Finance & Debt Capital Markets |
| Marie Natalie J. Collado                       | Head of Execution                                 |
| Jenny C. Guevara                               | Head of Sales                                     |
| Francis L. Jardeleza                           | Execution Team Head                               |
| George S. Uy-Tioco Jr.                         | Head of Mergers and Acquisitions                  |

\* Replaced by Rhoda A. Huang on May 1, 2019

i. Orientation and Education Program

The Bank has in place a formal board and director development program. For new directors, there is a deliberate, systematic and rapid familiarization with the organization and the operations of the board, Articles of Incorporation and Amended By-Laws, Manual of Corporate Governance, Board Charter, as well as the Code of Conduct, standards of Conflict of Interest and policies on Insider Trading, Whistleblowing, Data Privacy, and Related Party Transactions. The Bank, through its various units, also provides continuing director education in relation to current developments; these include regulatory initiatives like Data Privacy, the Anti-Money Laundering and Terrorist Financing Prevention Program, Foreign Account Tax Compliance Act, Securities Regulations Code, SEC memorandum circulars, and BSP regulations, among others. In 2018, all of the Bank's directors underwent the requisite corporate governance seminar provided by an SEC- or Bangko Sentral-accredited institution.

j. Retirement and Succession Policy

The Board, through its Personnel and Compensation Committee, manages the talent pipeline and assembles the required personnel capable of navigating changes. In consultation with the President, the Committee reviews the Company's talent development process for proper management. Senior management provides a report to the committee on the results of its talent and performance review process for key management positions and other high-potential individuals. The review process identifies opportunities, performance gaps and proactive measures in the Company's succession planning aside from ensuring that there is sufficient pool of qualified internal candidates to fill senior leadership positions.

The retirement policy is anchored with the BPI/Bank Retirement Policy. The Bank set a retirement age for directors at 80 years old. In specific cases, the Board, in mutual agreement with the director, may opt to postpone said director's retirement in accordance with the conditions set in the bank's policy. The term limit for independent directors is maximum of nine (9) years. After serving as ID for nine (9) years, the ID shall be perpetually barred from being elected as such in BPI Capital, but may continue to serve as a regular director, without prejudice to being elected as ID in other companies outside the business conglomerate, where applicable, under same conditions as provided for in the Circular. Reckoning of the cumulative nine-year term is from 2012.

Retirement of senior management is done with the requisite succession planning and in accordance with the Bank's policies and implementing guidelines of its retirements plan for all employees, the Bank's Amended by-Laws, Labor Code and the Corporation Code of the Philippines. Currently, the retirement age for employees of the Bank is set at 60 years of age.

#### k. Remuneration Policy

Our remuneration decisions for the Board and senior management are aligned with the risk incentives and support sustainable, long-term value creation. Anchored with BPI's Personnel and Compensation Committee, it recommends to the Board the fees and other compensation for directors, ensuring that compensation fairly remunerates directors for work required in the Company. As provided by our Amended By-laws, each director is entitled to receive fees and other compensation for his services as director. The Board has the sole authority to determine the amount, form and structure of the fees and other compensation of the directors. Board members receive per diems for each occasion of attendance at meetings of the Board or of a board committee. Board members with executive responsibilities within the BPI Group are compensated as full-time officers of the company, not as Executive Directors or Non-Executive Directors.

In 2018, BPI Capital's Board of Directors received a total of Php 2,412,352 as remuneration for the services rendered by them to the Company.

The Personnel and Compensation Committee annually reviews and approves base salary, incentive compensation for senior management, board of directors, and key officers and recommend appropriate remuneration package to the Board for approval that enables the institution to attract and keep superior human talent in its fold.

#### l. Self-Assessment Function and Performance Assessment Program

The Board annually conducts a self-assessment to ascertain the alignment of leadership fundamentals and issues, and to validate and affirm the Board's appreciation of its roles and responsibilities. The self-assessment also aims to measure the performance of the board by what it delivers, how it meets its responsibilities to the Company's stakeholders, and how it addresses issues that impact the Board's ability to effectively fulfill its fiduciary duties.

Using a standard evaluation method of self-assessment and feedback review, performance is assessed across four levels: the Board as a body, Board Committees, individual directors, and President and CEO.

The Personnel and Compensation Committee (PerCom) oversees the performance evaluation process within the company, which includes the annual review and approval of the corporate goals, strategic objectives and standards relevant to CEO, senior management, and other key officers.

The compliance System of BPI Capital is basically a two-tiered system. The primary level is achieved through self-regulation within each division by consciously abiding by provisions of Corporate Governance Manual, adhering to company policies and BPI Capital Corp's code of conduct.

The secondary level is conducted through the audit function which is performed by the Internal Audit Division and the Compliance Office as well as the external auditors appointed by the Board. The compliance review in turn, are reviewed and evaluated by the Audit Committee of the Board of Directors. The compliance office oversees the implementation of BPI Capital's compliance programs which take into account the applicable rules and regulations and business risks that may arise due to non-compliance. Through regulatory and self-assessment compliance matrices, compliance measures are formulated in order to help mitigate identified business risks and tested to ensure effectiveness.

Internal audit is an integral part of the Bank's internal control system. Internal audit helps ensure that key risk areas are properly identified and proactively managed through appropriate internal control policies that are fully disseminated and through appropriate and effective risk measurement, monitoring and control systems.

#### m. Related Party Transactions Policy

This policy guards against internal conflicts of interest between the company and/or its group and their directors, officers and significant shareholders and ensures that transactions such as loans and advances, deposit arrangement, trading of government securities and commercial papers, sale of assets, lease of bank premises, investment advisory/management, service arrangements and advances for operating expenses are made in the normal course of banking activities with terms and conditions that are generally comparable to those offered to non-related parties or to similar transactions in the market.

Vetting transactions is done by the board-level Related Party Transaction Committee (RPTC). The management of BPI Capital submit for vetting all its related party transactions to BPI's RPT Committee instead of setting a threshold amount of significant transactions. The management has taken the more conservative and prudent approach and has decided to do such considering the sensitive nature of the transactions and limited number thereof.

#### n. Dividend Policy

BPI Capital's dividend policy is to declare cash dividends to its common stockholders on a regular basis as may be determined by its Board of Directors.

#### o. Corporate Social Responsibility Initiatives

The brilliance of our future greatly depends on the vigor at which we invest in our world now. BPI Capital has a proven track record in delivering the best financial solutions to support those who promote economic growth and development. In the same light, we commit ourselves to extend the same level of care and diligence in supporting our communities.

2017 saw the beginning of our partnership with Dynamic Teen Company (DTC), a youth-oriented non-profit organization that is geared towards guiding the out-of-school and disadvantaged youth of the country and bringing them out of the streets and into the classrooms. DTC is headed by 2009 CNN Hero of the Year Efrén Peñaflorida, whose passion is driven by his mission to renew the Filipino youth's love for learning.

In continued support of the goal to make education accessible for the underprivileged Filipino youth, BPI Capital joined DTC's Learners' Educational Aid Program (LEAP) in Cavite City last September 22, 2018. Volunteers from various BPI Capital groups spent the day with 40 DTC students between grades 1 to 10. Their enthusiasm and eagerness to learn were very evident during the LEAP sessions, wherein topics in English, Math, and Science were covered. During the day, the volunteers came to teach, sing, play, and interact with the DTC students and teachers. As a parting gift, BPI Capital gave each student a bag of school supplies to further encourage them on their on-going pursuit for education.

It is not difficult to be moved after having had the chance to spend a day with these children. The children exhibited ingenuity and intellect during the sessions that the volunteers had with them. While these children have looked to their teachers for knowledge, we cannot help but look to them for inspiration. They showed us that they will not let their circumstances hinder their journey towards a better life. The fire of our country's future continues to burn bright because of the dedication that the youth is giving for their future.

Our role in the investment banking space is critical in furthering our nation's economic advancement. And with this experience, we at BPI Capital also recognize that our duty to touch the lives of Filipinos is just as important.

p. Consumer Protection Practices

Financial consumers play an essential role in creating a strong and stable financial system. It is therefore necessary for BPI Capital to establish an environment that empowers financial consumers to make informed financial decisions, protects their rights in all stages of their transactions with BPI Capital, and provides them an avenue to express their grievances regarding BPI Capital's products and services.

BPI Capital shall establish and keep updated a financial consumer protection governance structure that aims to establish a business environment that protects the interests of financial consumers and to create an institutional culture of fair and responsible treatment of customers through good governance exercised by the Board and governing bodies, and reinforced by the various functions that own, manage, oversee, or provide independent assurance over consumer protection activities.

*Consumer Protection Risk Management System*

BPI Capital has a formal and written Consumer Protection Compliance Program that is part of the overall compliance system and in accordance with the Revised Compliance Framework for Banks under the guidelines of the BSP.

Under the Board of Directors and Senior Management Oversight, the Board and the Senior Management are responsible for the following:

1. Periodically review of the effectiveness of the CPRMS;
2. Ensure sufficient resources are allocated to the program; and
3. Ensure that the weaknesses of the CPRMS are addressed and corrective actions are taken in a timely manner.

BPI Capital has established Board-approved consumer protection policies and procedures in place to ensure consumer protection practices are embedded in BPI Capital's business operations. These policies and procedures are prepared, reviewed, approved, published, disseminated, and updated in accordance with BPI Capital's policy on Approval of Required Manuals.

The consumer protection practices, adherence to internal policies and procedures, and compliance with existing laws, rules, and regulations are subject to periodic internal review by the BPI Internal Audit Group in accordance with an approved Consumer Protection Audit Guide. Results of the review and recommendations are reported to the Board's Audit Committee.

BPI Capital exercises full disclosure and utmost transparency by ensuring that consumers have a reasonable holistic understanding of BPI Capital's financial products and services, providing customers with ready access to key information (i.e. information regarding a product's or service's nature and structure, terms and conditions, and fundamental benefits and risks), and disclosing any conflict of interest throughout the product/service life cycle.

BPI Capital has a customer assistance/feedback facility in its various channels where financial consumers may express their complaints, requests, or inquiries. This includes the designated BPI Capital Customer Assistance Officers ("CAO"s). BPI Capital also ensures that financial customers are aware of the available channels, how to lodge concerns (e.g. centralized web portal, walk-in or personal visit, letter, e-mail, telephone, and facsimile), and where to lodge them (e.g. BPI Capital premises and websites).

To further ensure that we are more than able to address our customers' needs and concerns, the BPI Human Resources Department has established a Customer Protection Training Program to provide continuing education about Consumer Protection laws, rules, and regulations, as well as related policies and procedures to all relevant personnel, especially those whose roles and responsibilities involve customer interface.

Complaints, requests, and inquiries from financial consumers are received, acknowledged, investigated, and resolved in accordance with BPI Capital’s process on handling customer complaints, requests, and inquiries.

## VII. Corporate Information

### a. Organizational structure

The following is an overview of the Company’s principal activities and its functional organization (as of December 31, 2018):



### b. List of majority stockholders

BPI Capital is 100% owned by Bank of the Philippine Islands

### c. List and description of products and services offered

See *I.c – Business Model*

### d. Website

<https://www.bpiexpressonline.com/p/0/132/about-bpi-capital-corporation>

### e. List of branches/units

None.

## VIII. Audited Financial Statements

See attached Annex A – Audited Financial Statements

## IX. Compliance with Appendix Q-46 of the MORBNBFI

### a. Capital Structure and Adequacy

The Company's qualifying capital for the year's ended 2018 and 2017 were P3,418 million and P3,115 million, respectively. The Company's total qualifying capital for and 2017 were largely composed of CET1 capital and Tier 1 at 99% and comprised 100% for 2018.

The table below shows the composition of the Company's capital structure and total qualifying capital.

| Capital Structure<br>(Php Mn)   | 31-Dec-18        |              |                 | 31-Dec-17        |              |                 |
|---|------------------|--------------|-----------------|------------------|--------------|-----------------|
|   | CET1 /<br>Tier 1 | Tier 2       | Total           | CET1 /<br>Tier 1 | Tier 2       | Total           |
| <b>Core Capital</b>   | <b>4,078.53</b>  | -            | <b>4,078.53</b> | <b>3,839.71</b>  | <b>0.58</b>  | <b>3,840.29</b> |
| Paid-up common stock  | 506.44           | -            | 506.44          | 506.43           | -            | 506.43          |
| Additional paid-in capital  | 260.36           | -            | 260.36          | 260.36           | -            | 260.36          |
| Retained earnings   | 2,939.80         | -            | 2,939.80        | 2,320.45         | -            | 2,320.45        |
| Undivided profits   | 438.10           | -            | 438.10          | 619.96           | -            | 619.96          |
| Net unrealized gains or losses on AFS securities  | (75.62)          | -            | (75.62)         | 126.47           | -            | 126.47          |
| Remeasurements of Net Defined Benefit Liability   | 9.45             | -            | 9.45            | 6.04             | -            | 6.04            |
| General loan loss provision   | -                | -            | -               | -                | 0.58         | 0.58            |
| <b>Regulatory Adjustments</b>   | <b>660.88</b>    | -            | <b>660.88</b>   | <b>724.63</b>    | -            | <b>724.63</b>   |
| Deferred tax assets   | 56.61            | -            | 56.61           | 27.39            | -            | 27.39           |
| Defined benefit pension fund  | 30.30            | -            | 30.30           | 20.95            | -            | 20.95           |
| Investment in equity of unconsolidated subsidiary securities dealer/brokers and insurance companies | 573.98           | -            | 573.98          | 676.29           | -            | 676.29          |
| <b>TOTAL QUALIFYING CAPITAL</b>   | <b>3,417.65</b>  | -            | <b>3,417.65</b> | <b>3,115.08</b>  | <b>0.58</b>  | <b>3,115.66</b> |
| <b>% to Total</b>   | <b>100.00%</b>   | <b>0.00%</b> | <b>100%</b>     | <b>99.98%</b>    | <b>0.02%</b> | <b>100%</b>     |

b. Risk Exposure and Assessments

*Credit Risk Weighted Assets*

Using the Basel regulatory standardized approach, our total credit risk-weighted assets as of end-2018 amounted to P1,120 million. The table below presents the Company's credit risk-weighted assets for the year 2018 and 2017:

| Credit RWAs<br>(Php Mn)                                   | Amount          |               |
|---|-----------------|---------------|
|   | 2018            | 2017          |
| Total RWA (On-balance sheet)                              | 1,117.79        | 730.55        |
| Total RWA (Off-balance sheet)                             | -               | -             |
| Total counterparty RWA (banking book)                     | -               | -             |
| Total counterparty RWA (trading book)                     | 2.98            | -             |
| Total risk-weighted amount of credit linked notes         | -               | -             |
| Total risk-weighted securitization exposures              | -               | -             |
| <b>Total Gross Risk Weighted Assets</b>                   | <b>1,120.77</b> | <b>730.55</b> |
| General Loan Loss Provisions                              | -               | -             |
| Unbooked valuation reserves and other capital adjustments | -               | -             |
| <b>Total Deductions</b>                                   | <b>-</b>        | <b>-</b>      |
| <b>TOTAL CREDIT RWA</b>                                   | <b>1,120.77</b> | <b>730.55</b> |

*Market Risk Weighted Assets*

In terms of capital usage using the Basel standardized approach, total market risk-weighted assets stood at P682 million as of end-2018, of which equity exposures accounted for more than half, followed by foreign exposures and interest rate exposures, respectively. The significant decrease of the interest rate exposure was due on the reclassification of debt instruments from held-to-maturity and now measured at amortized cost.

The table below presents the Company's market risk-weighted assets for the year 2018 and 2017:

| Market RWAs (Php Mn)       | Amount        |                 |
|----------------------------|---------------|-----------------|
|                            | 2018          | 2017            |
| Interest rate exposures    | 8.37          | 319.96          |
| Equity exposures           | 485.47        | 672.01          |
| Foreign exchange exposures | 188.32        | 102.80          |
| <b>TOTAL MARKET RWA</b>    | <b>682.17</b> | <b>1,094.77</b> |

### Operational Risk Weighted Assets

We currently use the Basel regulatory basic indicator approach to quantify operational risk-weighted assets, by using the historical total annual gross income as the main measure of risk. In 2018, the Company's total operational risk-weighted assets stood at P2,028 million.

The table below presents the Company's operational risk-weighted assets for the year 2018 and 2017:

| Operational RWAs (Php Mn)    | Amount          |                 |
|------------------------------|-----------------|-----------------|
|                              | 2018            | 2017            |
| Gross income                 | 1,115.57        | 1,213.69        |
| Capital requirement          | 167.34          | 182.05          |
| Average capital requirement  | 162.28          | 176.55          |
| Adjusted capital charge      | 202.85          | 220.69          |
| <b>TOTAL OPERATIONAL RWA</b> | <b>2,028.52</b> | <b>2,206.91</b> |

### c. Summary of Financial Performance

| (in P Millions)                        | Consolidated    |                 | Solo            |                 |
|--|-----------------|-----------------|-----------------|-----------------|
|  | 2018            | 2017            | 2018            | 2017            |
| CET1 Capital                           | 3,980.88        | 3,783.34        | 3,417.65        | 3,115.08        |
| Tier 2 Capital                         | -               | 0.58            | -               | 0.58            |
| <b>Total Qualifying Capital</b>        | <b>3,980.88</b> | <b>3,783.92</b> | <b>3,417.65</b> | <b>3,115.66</b> |
| Total Credit Risk Weighted Assets      | 2,171.98        | 2,308.30        | 1,120.77        | 730.56          |
| Total Market Risk Weighted Assets      | 682.95          | 1,094.95        | 682.17          | 1,094.77        |
| Total Operational Risk Weighted Assets | 2,501.83        | 2,650.57        | 2,028.52        | 2,206.91        |
| <b>Total Risk Weighted Assets</b>      | <b>5,356.76</b> | <b>6,053.82</b> | <b>3,831.45</b> | <b>4,032.24</b> |
| CET1 Ratio                             | 74.32%          | 62.50%          | 89.20%          | 77.25%          |
| Capital Conservation Buffer            | 68.32%          | 56.50%          | 83.20%          | 71.25%          |
| Tier 1 Capital Ratio                   | 74.32%          | 62.50%          | 89.20%          | 77.25%          |
| Total Capital Adequacy Ratio           | 74.32%          | 62.50%          | 89.20%          | 77.27%          |

The Company ensures compliance with regulatory and internal minimum capital adequacy requirements, referred to as the Company's internal minimum CAR, or IMCAR, and the CAR management action trigger, or CARMAT, which incorporate the company's internal capital buffers and limit triggers, and captures risks beyond Pillar 1 (credit, market, and operational).

Total qualifying capital increased by P262 million or 8% from 2017's P3,156 million. Capital adequacy ratio, using Basel III measures, ended at 89.20%, with CET 1 at 89.20%. The CAR and CET 1 remained above the regulatory requirement.

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# **AUDITED FINANCIAL STATEMENTS**

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## Independent Auditor's Report

To the Board of Directors and Shareholders of  
**BPI Capital Corporation**  
8th Floor, BPI Building  
Ayala Avenue corner Paseo de Roxas  
Makati City

## Report on the Audits of the Consolidated Financial Statements

### *Our Opinion*

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of BPI Capital Corporation and Subsidiary (the "Group") as at December 31, 2018 and 2017, and its financial performance and its cash flows for the years then ended in accordance with Philippine Financial Reporting Standards (PFRS).

### *What we have audited*

The consolidated financial statements of the Group comprise:

- the consolidated statements of financial position as at December 31, 2018 and 2017;
- the consolidated statements of income for the years ended December 31, 2018 and 2017;
- the consolidated statements of comprehensive income for the years ended December 31, 2018 and 2017;
- the consolidated statements of changes in equity for the years ended December 31, 2018 and 2017;
- the consolidated statements of cash flows for the years ended December 31, 2018 and 2017; and
- the notes to consolidated financial statements, which include a summary of significant accounting policies.

### *Basis for Opinion*

We conducted our audits in accordance with Philippine Standards on Auditing (PSA). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements section of our report.

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

### *Independence*

We are independent of the Group in accordance with the Code of Ethics for Professional Accountants in the Philippines (Code of Ethics), together with the ethical requirements that are relevant to our audit of consolidated financial statements in the Philippines, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the Code of Ethics.

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T: +63 (2) 845 2728, F: +63 (2) 845 2806, [www.pwc.com/ph](http://www.pwc.com/ph)

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Independent Auditor's Report  
To the Board of Directors and Shareholders of  
BPI Capital Corporation  
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***Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements***

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with PFRS, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the ability of each entity within the Group to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

***Auditor's Responsibilities for the Audit of the Consolidated Financial Statements***

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with PSA will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with PSA, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

Independent Auditor's Report  
To the Board of Directors and Shareholders of  
BPI Capital Corporation  
Page 3

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the ability of each entity within the Group to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the entities within the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

*Other Matter - Restriction on Use*

This report is intended solely for the information and use of the Group and for filing with the Bangko Sentral ng Pilipinas and is not intended for any other purpose.

**Isla Lipana & Co.**



Zaldy D. Aguirre

Partner

CPA Cert No. 105660

P.T.R. No. 0024447, issued on January 8, 2019, Makati City

SEC A.N. (individual) as general auditors 1176-AR-2, Category A; effective until June 20, 2021

SEC A.N. (firm) as general auditors 0009-FR-5, Category A; effective until June 20, 2021

TIN 221-755-698

BIR A.N. 08-000745-077-2018, issued on January 29, 2018; effective until January 28, 2021

BOA/PRC Reg. No. 0142, effective until September 30, 2020

Makati City  
March 25, 2019

## BPI Capital Corporation and Subsidiary

### Statements of Financial Position As at December 31, 2018 and 2017 (All amounts in Philippine Peso)

|  | Notes | Consolidated         |                      | Parent               |                      |
|--|-------|----------------------|----------------------|----------------------|----------------------|
|  |       | 2018                 | 2017                 | 2018                 | 2017                 |
| <b>ASSETS</b>  |       |                      |                      |                      |                      |
| Cash and other cash items  | 2     | 762,809,446          | 855,680,373          | 281,623,204          | 462,859,040          |
| Due from Bangko Sentral ng Pilipinas   | 2     | 1,100,401,541        | 541,029,448          | 1,100,401,541        | 541,029,448          |
| Interbank loans receivable and securities purchased under agreements to resell | 2     | 291,153,583          | 192,523,005          | 291,153,583          | 192,523,005          |
| Financial assets at fair value through profit or loss                          | 3     | 773,433,306          | 1,528,782,980        | 624,172,544          | 1,528,782,980        |
| Financial assets at fair value through other comprehensive income              | 4     | 771,413,999          | -                    | 771,316,448          | -                    |
| Available-for-sale securities, net   | 4     | -                    | 616,884,911          | -                    | 412,661,130          |
| Investment securities at amortized cost, net                                   | 5     | 655,551,035          | -                    | 558,355,206          | -                    |
| Held-to-maturity securities  | 5     | -                    | 223,945,103          | -                    | -                    |
| Equity investments   | 6     | -                    | -                    | 202,361,610          | 202,361,610          |
| Trade and other receivables, net   | 7     | 219,673,471          | 537,355,932          | 29,933,905           | 44,912,154           |
| Property and equipment, net  | 8     | 18,877,902           | 21,725,889           | 17,709,520           | 19,726,064           |
| Deferred income tax assets, net  | 9     | 9,758,375            | 15,288,601           | 7,377,307            | 27,392,713           |
| Other assets, net  | 10    | 69,523,501           | 53,666,071           | 48,969,492           | 27,085,668           |
| <b>Total assets</b>  |       | <b>4,672,596,159</b> | <b>4,586,882,313</b> | <b>3,933,374,360</b> | <b>3,459,333,812</b> |
| <b>LIABILITIES AND EQUITY</b>  |       |                      |                      |                      |                      |
| <b>Liabilities</b>   |       |                      |                      |                      |                      |
| Accounts payable and other liabilities   | 11    | 478,664,658          | 760,024,555          | 109,304,730          | 101,008,725          |
| <b>Equity</b>  |       |                      |                      |                      |                      |
| Share capital  | 12    | 506,435,080          | 506,435,080          | 506,435,080          | 506,435,080          |
| Share premium  |       | 260,364,020          | 260,364,020          | 260,364,020          | 260,364,020          |
| Accumulated reserves   | 12    | (11,410,178)         | 136,730,012          | (11,330,938)         | 36,697,083           |
| Retained earnings  | 12    | 3,438,542,579        | 2,923,328,646        | 3,068,601,468        | 2,554,828,904        |
| <b>Total equity</b>  |       | <b>4,193,931,501</b> | <b>3,826,857,758</b> | <b>3,824,069,630</b> | <b>3,358,325,087</b> |
| <b>Total liabilities and equity</b>  |       | <b>4,672,596,159</b> | <b>4,586,882,313</b> | <b>3,933,374,360</b> | <b>3,459,333,812</b> |

(The notes on pages 1 to 60 are integral part of these consolidated financial statements)

**BPI Capital Corporation and Subsidiary**

Statements of Changes in Equity  
For the years ended December 31, 2018 and 2017  
(All amounts in Philippine Peso)

|                                     | Consolidated               |               |                                   |                                |                 |
|-------------------------------------|----------------------------|---------------|-----------------------------------|--------------------------------|-----------------|
|                                     | Share capital<br>(Note 12) | Share premium | Accumulated reserves<br>(Note 12) | Retained earnings<br>(Note 12) | Total equity    |
| Balances at January 1, 2017         | 506,435,080                | 260,364,020   | 5,031,277                         | 4,812,381,063                  | 5,584,211,440   |
| Comprehensive income                |                            |               |                                   |                                |                 |
| Net income for the year             | -                          | -             | -                                 | 610,947,583                    | 610,947,583     |
| Other comprehensive income          | -                          | -             | 131,290,408                       | -                              | 131,290,408     |
| Total comprehensive income          | -                          | -             | 131,290,408                       | 610,947,583                    | 742,237,991     |
| Transaction with owners             |                            |               |                                   |                                |                 |
| Exercise of stock options           | -                          | -             | 408,327                           | -                              | 408,327         |
| Dividends declared and paid         | -                          | -             | -                                 | (2,500,000,000)                | (2,500,000,000) |
| Total transaction with owners       | -                          | -             | 408,327                           | (2,500,000,000)                | (2,499,591,673) |
| Balances at December 31, 2017       | 506,435,080                | 260,364,020   | 136,730,012                       | 2,923,328,646                  | 3,826,857,758   |
| Impact of PFRS 9 adoption (Note 21) | -                          | -             | 507,723                           | 92,548,669                     | 93,056,392      |
| Restated balance at January 1, 2018 | 506,435,080                | 260,364,020   | 137,237,735                       | 3,015,877,315                  | 3,919,914,150   |
| Comprehensive income                |                            |               |                                   |                                |                 |
| Net income for the year             | -                          | -             | -                                 | 388,030,130                    | 388,030,130     |
| Other comprehensive loss            | -                          | -             | (149,986,279)                     | 34,635,134                     | (115,351,145)   |
| Total comprehensive income          | -                          | -             | (149,986,279)                     | 422,665,264                    | 272,678,985     |
| Transaction with owners             |                            |               |                                   |                                |                 |
| Exercise of stock options           | -                          | -             | 1,338,366                         | -                              | 1,338,366       |
| Balances at December 31, 2018       | 506,435,080                | 260,364,020   | (11,410,178)                      | 3,438,542,579                  | 4,193,931,501   |

(The notes on pages 1 to 60 are integral part of these consolidated financial statements)

## BPI Capital Corporation and Subsidiary

### Statements of Income For the years ended December 31, 2018 and 2017 (All amounts in Philippine Peso)

|   | Notes  | Consolidated  |               | Parent      |               |
|---|--------|---------------|---------------|-------------|---------------|
|   |        | 2018          | 2017          | 2018        | 2017          |
| <b>Income</b>                                 |        |               |               |             |               |
| Fees and commissions                          | 13     | 953,001,536   | 1,212,909,556 | 746,164,951 | 950,382,284   |
| Interest income                               | 14     | 85,400,192    | 116,188,071   | 78,138,568  | 78,094,097    |
| Dividend income                               | 3,4,6  | 25,669,196    | 29,371,649    | 133,506,820 | 27,689,567    |
| Net foreign exchange gain                     | 19     | 5,949,984     | 4,585,794     | 6,646,398   | 4,585,794     |
| Trading gain (loss), net                      | 3      | 1,836,573     | (5,469,256)   | 1,836,573   | 23,609,411    |
| Gain on sale of available-for-sale securities | 4      | -             | 94,739,938    | -           | 94,961,098    |
| Miscellaneous income                          |        | 7,067,255     | 1,708,225     | 1,934,184   | 1,123,312     |
|   |        | 1,078,924,736 | 1,454,033,977 | 968,227,494 | 1,180,445,563 |
| <b>Expenses</b>                               |        |               |               |             |               |
| Compensation and fringe benefits              | 17     | 227,657,894   | 270,881,795   | 167,452,434 | 186,248,122   |
| Gross receipts tax                            |        | 60,964,332    | 76,945,503    | 60,964,332  | 76,945,503    |
| Brokerage and underwriting fees               |        | 18,456,392    | 26,699,689    | 7,223,981   | 2,185,035     |
| Occupancy and equipment-related expenses      | 8      | 17,105,901    | 17,302,070    | 15,851,091  | 15,971,059    |
| Management and other professional fees        |        | 8,266,792     | 31,097,231    | 7,205,085   | 9,828,957     |
| Taxes and licenses                            |        | 3,325,622     | 2,794,025     | 2,425,116   | 2,071,046     |
| (Reversal) provision for impairment           | 4,7,10 | (1,071,307)   | (307,774)     | (1,071,307) | (113,815)     |
| Other operating expenses                      | 15     | 199,774,164   | 204,893,262   | 75,103,030  | 80,573,414    |
|   |        | 534,479,790   | 630,305,801   | 335,153,762 | 373,709,321   |
| Income before income tax                      |        | 544,444,946   | 823,728,176   | 633,073,732 | 806,736,242   |
| <b>Income tax expense</b>                     |        |               |               |             |               |
| Current                                       | 16     | 150,909,345   | 214,168,391   | 147,225,931 | 209,075,191   |
| Deferred                                      | 9,16   | 5,505,471     | (1,387,798)   | 4,381,030   | (562,438)     |
|   |        | 156,414,816   | 212,780,593   | 151,606,961 | 208,512,753   |
| Net income for the year                       |        | 388,030,130   | 610,947,583   | 481,466,771 | 598,223,489   |

(The notes on pages 1 to 60 are integral part of these consolidated financial statements)

## BPI Capital Corporation and Subsidiary

### Statements of Comprehensive Income For the years ended December 31, 2018 and 2017 (All amounts in Philippine Peso)

|  | Note | Consolidated  |             | Parent        |             |
|--|------|---------------|-------------|---------------|-------------|
|  |      | 2018          | 2017        | 2018          | 2017        |
| Net income for the year  |      | 388,030,130   | 610,947,583 | 481,466,771   | 598,223,489 |
| Other comprehensive (loss) income  | 12   |               |             |               |             |
| Item that may be subsequently reclassified to profit or loss                               |      |               |             |               |             |
| Net change in fair value reserve on financial assets at fair value through OCI, net of tax |      | (118,974,276) | 125,178,606 | (113,669,925) | 121,732,255 |
| Item that will not be subsequently reclassified to profit or loss                          |      |               |             |               |             |
| Realized gain on sale of FVOCI, net of tax, reclassified to retained earnings              |      | (34,635,134)  | -           | -             | -           |
| Remeasurement gain on Retirement benefits, net of tax                                      |      | 3,623,131     | 6,111,802   | 3,552,938     | 6,025,747   |
| Total other comprehensive (loss) income, net of tax  |      | (149,986,279) | 131,290,408 | (110,116,987) | 127,758,002 |
| Total comprehensive income for the year  |      | 238,043,851   | 742,237,991 | 371,349,784   | 725,981,491 |

(The notes on pages 1 to 60 are integral part of these consolidated financial statements)

## BPI Capital Corporation and Subsidiary

### Statements of Changes in Equity For the years ended December 31, 2018 and 2017 (All amounts in Philippine Peso)

|                                     | Parent                     |               |                                   |                                |                 |
|-------------------------------------|----------------------------|---------------|-----------------------------------|--------------------------------|-----------------|
|                                     | Share capital<br>(Note 12) | Share premium | Accumulated reserves<br>(Note 12) | Retained earnings<br>(Note 12) | Total equity    |
| Balances at January 1, 2017         | 506,435,080                | 260,364,020   | (92,406,427)                      | 4,456,605,415                  | 5,130,998,088   |
| Comprehensive income                |                            |               |                                   |                                |                 |
| Net income for the year             | -                          | -             | -                                 | 598,223,489                    | 598,223,489     |
| Other comprehensive income          | -                          | -             | 127,758,002                       | -                              | 127,758,002     |
| Total comprehensive income          | -                          | -             | 127,758,002                       | 598,223,489                    | 725,981,491     |
| Transaction with owners             |                            |               |                                   |                                |                 |
| Exercise of stock options           | -                          | -             | 1,345,508                         | -                              | 1,345,508       |
| Dividends declared and paid         | -                          | -             | -                                 | (2,500,000,000)                | (2,500,000,000) |
| Total transaction with owners       | -                          | -             | 1,345,508                         | (2,500,000,000)                | (2,498,654,492) |
| Balances at December 31, 2017       | 506,435,080                | 260,364,020   | 36,697,083                        | 2,554,828,904                  | 3,358,325,087   |
| Impact of PFRS 9 adoption (Note 21) | -                          | -             | 60,750,600                        | 32,305,793                     | 93,056,393      |
| Restated balance at January 1, 2018 | 506,435,080                | 260,364,020   | 97,447,683                        | 2,587,134,697                  | 3,451,381,480   |
| Comprehensive income                |                            |               |                                   |                                |                 |
| Net income for the year             | -                          | -             | -                                 | 481,466,771                    | 481,466,771     |
| Other comprehensive loss            | -                          | -             | (110,116,987)                     | -                              | (110,116,987)   |
| Total comprehensive income          | -                          | -             | (110,116,987)                     | 481,466,771                    | 371,349,784     |
| Transaction with owners             |                            |               |                                   |                                |                 |
| Exercise of stock options           | -                          | -             | 1,338,366                         | -                              | 1,338,366       |
| Balances at December 31, 2018       | 506,435,080                | 260,364,020   | (11,330,938)                      | 3,068,601,468                  | 3,824,069,630   |

(The notes on pages 1 to 60 are integral part of these consolidated financial statements)

## BPI Capital Corporation and Subsidiary

### Statement of Cash Flows For the years ended December 31, 2018 and 2017 (All amounts in Philippine Peso)

|   | Notes  | Consolidated  |                 | Parent        |                 |
|---|--------|---------------|-----------------|---------------|-----------------|
|   |        | 2018          | 2017            | 2018          | 2017            |
| <b>Cash flows from operating activities</b>   |        |               |                 |               |                 |
| Profit before income tax  |        | 544,444,946   | 823,728,176     | 633,073,732   | 806,736,242     |
| Adjustments for:  |        |               |                 |               |                 |
| Unrealized fair value loss on trading securities  | 3      | 27,407,069    | 3,248,030       | 27,407,069    | 3,248,030       |
| Depreciation  | 8      | 7,091,720     | 7,222,437       | 5,836,910     | 5,891,426       |
| Reversal for impairment   | 4,7,10 | (1,071,307)   | (307,774)       | (1,071,307)   | (113,815)       |
| Stock option plan amortization  |        | 1,338,365     | 408,327         | 1,338,365     | 1,345,508       |
| Loss on sale of property and equipment  | 8      | -             | 79,934          | -             | -               |
| Gain on sale of available-for-sale securities   | 4      | -             | (94,739,938)    | -             | (94,961,098)    |
| Interest income   | 14     | (85,400,191)  | (116,188,071)   | (78,138,568)  | (107,172,764)   |
| Dividend income   | 3,4,6  | (25,669,196)  | (29,371,649)    | (133,506,820) | (27,689,567)    |
| Operating income before changes in operating assets and liabilities                         |        | 468,141,406   | 594,079,472     | 454,939,381   | 587,283,962     |
| Changes in operating assets and liabilities   |        |               |                 |               |                 |
| Decrease (Increase) in:   |        |               |                 |               |                 |
| Trading securities  |        | 522,004,222   | (928,317,962)   | 522,004,222   | (928,317,962)   |
| Trade and other receivables   |        | 318,810,205   | 114,233,917     | 16,105,993    | 294,049,510     |
| Other assets  |        | (19,498,562)  | 27,632,019      | (16,808,197)  | 1,343,422       |
| (Decrease) increase in accounts payable and other liabilities                               |        | (217,437,251) | 189,674,690     | (44,782,775)  | (9,951,051)     |
| Cash generated from operations  |        | 1,072,020,020 | (2,697,864)     | 931,458,624   | (55,592,119)    |
| Interest received   |        | 51,714,305    | 93,230,389      | 50,174,460    | 92,034,636      |
| Contributions to retirement fund  | 17     | (756,657)     | (10,604,396)    | -             | -               |
| Income taxes paid   |        | (102,783,600) | (341,675,721)   | (96,196,700)  | (331,230,485)   |
| Net cash (used in) from operating activities  |        | 1,020,194,068 | (261,747,592)   | 885,436,384   | (294,787,968)   |
| <b>Cash flows from investing activities</b>   |        |               |                 |               |                 |
| Acquisition of available for sales securities   | 4      | (539,855,454) | (113,559,994)   | (539,855,454) | (113,328,749)   |
| Acquisition of held-to-maturity (HTM) securities  | 5      | -             | (98,332,772)    | -             | -               |
| Proceeds from disposal of available-for-sale securities                                     | 4      | -             | 685,759,160     | -             | 680,701,136     |
| Proceeds from disposal of financial assets at fair value through other comprehensive income |        | 57,475,665    | -               | 1,499,451     | -               |
| Dividend received   | 3,4,6  | 25,669,196    | 29,371,649      | 133,506,820   | 27,689,567      |
| Interest received on investment securities  |        | 5,892,002     | 14,351,727      | -             | -               |
| Acquisitions of property and equipment  | 8      | (5,412,066)   | (13,250,263)    | (4,988,699)   | (12,881,623)    |
| Proceeds from maturities of HTM securities  | 5      | -             | 104,623,494     | -             | -               |
| Proceeds from disposals of property and equipment   | 8      | 1,168,333     | 1,000           | 1,168,333     | 2,865,317       |
| Net cash (used in) from investing activities  |        | (455,062,324) | 608,964,001     | (408,669,549) | 585,045,648     |
| <b>Cash flows from financing activities</b>   |        |               |                 |               |                 |
| Dividend declared and paid  | 12     | -             | (2,500,000,000) | -             | (2,500,000,000) |
| Net increase (decrease) in cash and cash equivalents  |        | 565,131,744   | (2,152,783,591) | 476,766,835   | (2,209,742,320) |
| Cash and cash equivalents at January 1  |        | 1,589,232,826 | 3,737,430,622   | 1,196,411,493 | 3,406,153,813   |
| Effect of exchange rate differences   |        | -             | 4,585,795       | -             | -               |
| Cash and cash equivalents at December 31  | 2      | 2,154,364,570 | 1,589,232,826   | 1,673,178,328 | 1,196,411,493   |

(The notes on pages 1 to 60 are integral part of these consolidated financial statements)

## **BPI Capital Corporation and Subsidiary**

Notes to Consolidated Financial Statements

For the years ended December 31, 2018 and 2017

(Amounts are shown in Philippine Peso unless otherwise stated)

### **Note 1 - General information**

BPI Capital Corporation (the “Parent Company”) was incorporated in the Philippines and registered with the Securities and Exchange Commission (SEC) on February 5, 1977, primarily to act as an institutional vehicle by and through which the business of financial intermediation may be provided by carrying out and exercising the powers, rights, privileges, and attributes of an investment house as may be allowed under applicable laws.

The Parent Company owns 100% of BPI Securities Corporation, (collectively the “Group”) a domestic commercial bank with an expanded banking license. The Group is registered and domiciled in the Philippines.

As at December 31, 2018, the Parent Company’s registered office address, which was also its principal place of business, was located at the 8th Floor, BPI Building, Ayala Avenue corner Paseo de Roxas, Makati City. In 2019, the Parent Company’s office, which is also its principal place of business, was transferred to Ayala North Exchange, Ayala Avenue corner Salcedo Street, Legaspi Village, Makati City. The Parent Company is a wholly-owned subsidiary of Bank of the Philippine Islands (“Parent Bank” or “BPI”), a commercial bank with an expanded banking license registered in the Philippines.

The Group has 116 employees as at December 31, 2018 (2017 - 110 employees).

These financial statements have been approved and authorized for issuance by the Group’s Board of Directors of the Parent Company on March 20, 2019. There are no material events that occurred subsequent to March 20, 2019 until March 25, 2019.

### **Note 2 - Cash and cash equivalents**

The account at December 31 consists of:

|                                      | Consolidated  |               | Parent        |               |
|--------------------------------------|---------------|---------------|---------------|---------------|
|                                      | 2018          | 2017          | 2018          | 2017          |
| Cash and other cash items            | 762,809,446   | 855,680,373   | 281,623,204   | 462,859,040   |
| Due from Bangko Sentral ng Pilipinas | 1,100,401,541 | 541,029,448   | 1,100,401,541 | 541,029,448   |
| Interbank loans receivable and SPAR  | 291,153,583   | 192,523,005   | 291,153,583   | 192,523,005   |
|                                      | 2,154,364,570 | 1,589,232,826 | 1,673,178,328 | 1,196,411,493 |

#### *Due from Bangko Sentral ng Pilipinas (BSP)*

The account pertains to the Group's placements in special deposit accounts with BSP with an average maturity of 7 to 28 days (2017 - 5 to 7 days) and average effective rate of 5.20% in 2018 (2017 - 3.01%). The account includes mandatory reserve deposits in compliance with regulatory requirement amounting to P401,541 as at December 31, 2018 (2017 - P1,029,448).

#### *Interbank Loans Receivable and Securities Purchased Under Agreements to Resell (SPAR)*

The account represents short-term lending to BSP under reverse repurchase agreement which bears an effective interest rate of 3.65% in 2018 (2017 - 3%) with an average maturity of 1.5 days as at December 31, 2018 (2017 - 5 days).

Interest income earned from cash and cash equivalents is disclosed in Note 14.

#### *Significant judgment - Expected credit losses*

Due from BSP and interbank loans receivable and SPAR are deemed by the Group to have low credit risk. Debt instruments are considered to be low credit risk when they have a low risk of default and the issuer has a strong capacity to meet its contractual cash flow obligations in the near term. The Group uses external ratings in assessing the credit risk arising from these exposures. Under PFRS 9, the low credit risk assets are at the minimum subject to 12-month expected credit loss (ECL). Based on its assessment, management has ascertained that the corresponding 12-month ECL is not material.

The detailed accounting policy for credit losses is disclosed in Note 21. Likewise, information on the credit quality of cash and cash equivalents is presented in Note 21.

### **Note 3 - Financial assets at fair value through profit or loss (FVTPL)**

The account at December 31 consists of:

|                                  | Consolidated |               | Parent      |               |
|----------------------------------|--------------|---------------|-------------|---------------|
|                                  | 2018         | 2017          | 2018        | 2017          |
| Debt securities                  |              |               |             |               |
| Philippine government securities | 94,036,064   | 1,166,864,792 | 94,036,064  | 1,166,864,792 |
| Philippine corporate bonds       | 7,365,645    | 28,627,319    | 7,365,645   | 28,627,319    |
| Listed equity securities         | 237,907,843  | 330,735,709   | 237,907,843 | 330,735,709   |
| Mutual funds                     | 424,768,469  | -             | 275,507,707 | -             |
| Derivatives                      | 9,355,285    | 2,555,160     | 9,355,285   | 2,555,160     |
|                                  | 773,433,306  | 1,528,782,980 | 624,172,544 | 1,528,782,980 |

Listed equity securities were issued by Philippine corporations and are traded in Philippine Stock Exchange (PSE). Dividend income earned from investments in equity securities for the year ended December 31, 2018 amounted to P16,351,675 (2017 - P12,880,229).

Details of net trading gain (loss) for the years ended December 31 on financial assets at FVTPL are summarized as follows:

|                            | Consolidated |             | Parent       |             |
|----------------------------|--------------|-------------|--------------|-------------|
|                            | 2018         | 2017        | 2018         | 2017        |
| Realized (loss) gain       | 29,243,642   | (2,221,226) | 29,243,642   | (2,221,226) |
| Unrealized fair value loss | (27,407,069) | (3,248,030) | (27,407,069) | (3,248,030) |
|                            | 1,836,573    | (5,469,256) | 1,836,573    | (5,469,256) |

(2)

**Note 4 - Financial Assets at fair value through other comprehensive income (FVOCI)/Available-for-sale securities**

Details of financial assets at FVOCI, net as of December 31, 2018 consists of:

| PFRS 9            | Consolidated | Parent      |
|-------------------|--------------|-------------|
| Equity securities |              |             |
| Listed            | 323,575,200  | 323,575,200 |
| Unlisted          | 447,838,799  | 447,741,248 |
|                   | 771,413,999  | 771,316,448 |

Listed equity securities were issued by Philippine corporations and are traded in PSE.

Unlisted equity securities mainly pertain to investments in close-ended foreign private equity funds.

The above investments in equities are held for strategic purposes rather than with a view to profit on a subsequent sale. Management has no plans of selling these investments in the short or medium term. Accordingly, the Group has designated these investments at FVOCI under PFRS 9. Please see Note 21 for the impact of adoption PFRS 9.

The Group's investments previously classified as available-for-sale (AFS) as at December 31, 2017 under PAS 39 are as follows:

|                          | Consolidated | Parent      |
|--------------------------|--------------|-------------|
| Equity securities        |              |             |
| Listed                   | 57,599,520   | -           |
| Unlisted                 | 245,580,902  | 245,474,566 |
| Mutual funds             | 315,354,489  | 168,836,564 |
| Total                    | 618,534,911  | 414,311,130 |
| Allowance for impairment | (1,650,000)  | (1,650,000) |
|                          | 616,884,911  | 412,661,130 |

In 2018, certain PSE shares classified as financial assets at fair value through OCI were sold. Net gain on sale amounting to P34,635,134 was directly recognized in retained earnings.

For the year ended December 31, 2017, proceeds from disposal of investments in financial assets at FVOCI amounted to P685,759,160 resulting in a gain of P94,739,938.

For the year ended December 31, 2018, dividend income earned from investments in equity securities amounted to P9,317,521 (2017 - P16,491,420).

**Critical accounting estimate - Fair value of other financial instruments**

The fair values of financial instruments that are not quoted in active markets are determined by using generally accepted valuation techniques. Where valuation techniques (for example, discounted cash flow models) are used to determine fair values, they are validated and periodically reviewed by qualified personnel independent of the area that created them. Inputs used in these models are from observable data and quoted market prices in respect of similar financial instruments.

(3)

All models are approved by the BOD before they are used, and models are calibrated to ensure that outputs reflect actual data and comparative market prices. Changes in assumptions about these factors could affect reported fair value of financial instruments. The Group considers that it is impracticable to disclose with sufficient reliability the possible effects of sensitivities surrounding the fair value of financial instruments that are not quoted in active markets.

#### **Note 5 - Investment securities at amortized cost**

Details of investment securities at amortized cost as at December 31, 2018 are as follows:

|                             | Consolidated | Parent      |
|-----------------------------|--------------|-------------|
| Government debt securities  |              |             |
| Face amount                 | 649,044,142  | 554,355,000 |
| Unamortized discount        | (3,410,470)  | (4,799,449) |
|                             | 645,633,672  | 549,555,551 |
| Accrued interest receivable | 9,917,363    | 8,799,655   |
|                             | 655,551,035  | 558,355,206 |

Investment securities previously classified as held-to-maturity as at December 31, 2017 are as follows:

|                             | Consolidated | Parent |
|-----------------------------|--------------|--------|
| Government debt securities  |              |        |
| Face amount                 | 228,893,995  | -      |
| Unamortized discount        | (6,236,823)  | -      |
|                             | 222,657,172  | -      |
| Accrued interest receivable | 1,287,931    | -      |
|                             | 223,945,103  | -      |

#### *Significant judgment - Impairment of investment securities at amortized cost*

Government securities at amortized cost are deemed by the Group to have low credit risk. Debt instruments are considered to be low credit risk when they have a low risk of default and the issuer has a strong capacity to meet its contractual cash flow obligations in the near term. The Group uses external ratings in assessing the credit risk arising from these exposures. Under PFRS 9, the low credit risk assets are at the minimum subject to 12-month expected credit loss (ECL). Based on its assessment, management has ascertained that the corresponding 12-month ECL is not material.

The detailed accounting policy for credit losses is disclosed in Note 21. Likewise, information on the credit quality of investment securities at amortized cost is presented in Note 21.

#### **Note 6 - Equity investments**

The account pertains to the Parent Company's wholly-owned subsidiary, BPI Securities Corporation (BSC), amounting to P202,361,610 which is carried at cost as at December 31, 2018 and 2017.

BSC is primarily engaged in the brokerage business of purchase and sale of any and all kinds of shares, bonds, debentures, securities and any and all kinds of properties, either in the Philippines or in any foreign country; to underwrite and distribute securities issued by another person, firm, corporation or association, whether domestic or foreign; and to sell the aforesaid securities to customers and/or to act as broker and/or dealer of securities.

(4)

Financial information of BSC as at and for the years ended December 31 follow:

|                                   | 2018         | 2017          |
|-----------------------------------|--------------|---------------|
| Total current assets              | 821,767,312  | 1,014,003,517 |
| Total non-current assets          | 119,816,100  | 328,010,706   |
| Total assets                      | 941,583,412  | 1,342,014,223 |
| Total current liabilities         | 369,359,929  | 659,015,830   |
| Total non-current liabilities     | -            | 12,104,112    |
| Total liabilities                 | 366,359,929  | 671,119,942   |
| Net assets                        | 572,223,483  | 670,894,281   |
|                                   | 2018         | 2017          |
| Revenues                          | 220,697,242  | 276,291,099   |
| Expenses                          | 199,326,027  | 259,299,165   |
| Income before income tax          | 21,371,215   | 16,991,934    |
| Income tax expense                | 4,807,855    | 4,267,840     |
| Net income                        | 16,563,360   | 12,724,094    |
| Other comprehensive (loss) gain   | (39,869,292) | 3,532,406     |
| Total comprehensive (loss) income | (23,305,932) | 16,256,500    |

Dividend income earned from BSC recognized in the statement of comprehensive income for the year ended December 31, 2018 amounts to P110,000,000.

*Significant judgment - Impairment of equity investments*

Impairment assessment on investments in subsidiaries is performed whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Impairment loss is recognized whenever the carrying amount of the asset exceeds its recoverable amount. The recoverable amount is computed based on the higher of the asset's fair value less cost to sell or value-in-use. Management has not identified any indicators of impairment as at December 31, 2018 and 2017.

**Note 7 - Trade and other receivables, net**

The account at December 31 consists of:

|   | Consolidated |              | Parent       |              |
|---|--------------|--------------|--------------|--------------|
|   | 2018         | 2017         | 2018         | 2017         |
| Trade   | 293,649,149  | 604,358,739  | 103,334,310  | 111,741,051  |
| Notes   | -            | 5,385,618    | -            | 5,385,618    |
| Loans   | -            | 1,883,012    | -            | 1,883,012    |
|   | 293,649,149  | 611,627,369  | 103,334,310  | 119,009,681  |
| Allowance for impairment on trade receivables | (73,975,678) | (74,271,437) | (73,400,405) | (74,097,527) |
|   | 219,673,471  | 537,355,932  | 29,933,905   | 44,912,154   |

(5)

Trade and other receivables are expected to be realized as follows:

|                             | Consolidated |             | Parent     |            |
|-----------------------------|--------------|-------------|------------|------------|
|                             | 2018         | 2017        | 2018       | 2017       |
| Within one year (current)   | 219,547,569  | 530,087,302 | 29,808,003 | 37,643,524 |
| Over one year (non-current) | 125,902      | 7,268,630   | 125,902    | 7,268,630  |
|                             | 219,673,471  | 537,355,932 | 29,933,905 | 44,912,154 |

Loans receivable mainly pertain to unsecured loans granted to Group officers with interest at rates ranging from 7% to 9% with a term of five years.

The movement in allowance for impairment of trade receivables for the years ended December 31 are as follows:

|                        | Consolidated |            | Parent     |            |
|------------------------|--------------|------------|------------|------------|
|                        | 2018         | 2017       | 2018       | 2017       |
| Beginning of year      | 74,271,437   | 74,465,395 | 74,097,527 | 74,097,527 |
| Reversal of impairment | (295,759)    | (193,958)  | (697,122)  | -          |
| End of year            | 73,975,678   | 74,271,437 | 73,400,405 | 74,097,527 |

In 2015, management provided full impairment on the receivable from a third party customer amounting to P72,893,710 from an executed and completed financial advisory services rendered by the Parent Company to the latter. Management's judgment to fully impair the said receivable stemmed from the significant disagreement between the Parent Company and the third party customer as to the fees on the services rendered. The Parent Company has already filed a legal case against the customer in the appropriate court and no decision has been issued as at December 31, 2018.

*Critical accounting judgment - Trade and other receivables*

From January 1, 2018, the Group has applied Philippine Financial Reporting Standard (PFRS) 9 simplified approach in determining the recoverable amount of trade and other receivables based on the expected credit losses of the portfolio of receivables, as a whole. In arriving at the expected credit loss for a particular period, management considers both historical loss experience and certain macroeconomic factors of the countries of the related parties to which it renders services.

In these cases, management uses judgments based on the best available facts and circumstances, including but not limited to the length of relationship with the related parties and whether there had been payment defaults in the past. An evaluation of receivables designed to identify potential charges to the provision is performed on a continuous basis throughout the year. The carrying value of receivables at the end of each reporting period and the amount and timing of recorded provision for any period could differ based on actual experience and changes in judgments made.

Prior to January 1, 2018, the Group determines the recoverable amount of trade and other receivables, based on the historical experience of incurred losses established for these receivables considering the ageing structure of receivables that are past due and evaluation of specific accounts that are unable to meet their financial obligations, irrespective of ageing.

The detailed accounting policy for credit losses is disclosed in Note 21. Likewise, information on the credit quality of trade and other receivables is presented in Note 21.

(6)

### **Note 8 - Property and equipment, net**

Details and movements of the account follow:

#### **Consolidated**

|   | Furniture, fixtures and<br>equipment | Computer equipment | Total       |
|---|--------------------------------------|--------------------|-------------|
| <b>Cost</b>                             |                                      |                    |             |
| January 1, 2018                         | 40,820,257                           | 10,408,409         | 51,228,666  |
| Additions                               | 5,057,809                            | 354,257            | 5,412,066   |
| Disposals                               | (1,510,000)                          | -                  | (1,510,000) |
| December 31, 2018                       | 44,368,066                           | 10,762,666         | 55,130,732  |
| <b>Accumulated depreciation</b>         |                                      |                    |             |
| January 1, 2018                         | 19,880,141                           | 9,622,636          | 29,502,777  |
| Depreciation                            | 6,402,389                            | 689,331            | 7,091,720   |
| Disposals                               | (341,667)                            | -                  | (341,667)   |
| December 31, 2018                       | 25,940,863                           | 10,311,967         | 36,252,830  |
| Net carrying value at December 31, 2018 | 18,427,203                           | 450,699            | 18,877,902  |

|   | Furniture, fixtures and<br>equipment | Computer equipment | Total       |
|---|--------------------------------------|--------------------|-------------|
| <b>Cost</b>                             |                                      |                    |             |
| January 1, 2017                         | 33,498,228                           | 9,500,175          | 42,998,403  |
| Additions                               | 12,342,029                           | 908,234            | 13,250,263  |
| Disposals                               | (1,200,000)                          | -                  | (1,200,000) |
| Transfers to Parent Bank                | (3,820,000)                          | -                  | (3,820,000) |
| December 31, 2017                       | 40,820,257                           | 10,408,409         | 51,228,666  |
| <b>Accumulated depreciation</b>         |                                      |                    |             |
| January 1, 2017                         | 15,759,078                           | 8,755,278          | 24,514,356  |
| Depreciation                            | 6,355,079                            | 867,358            | 7,222,437   |
| Disposals                               | (1,119,066)                          | -                  | (1,119,066) |
| Transfers to Parent Bank                | (1,114,950)                          | -                  | (1,114,950) |
| December 31, 2017                       | 19,880,141                           | 9,622,636          | 29,502,777  |
| Net carrying value at December 31, 2017 | 20,940,116                           | 785,773            | 21,725,889  |

#### **Parent**

|   | Furniture, fixtures and<br>equipment | Computer equipment | Total       |
|---|--------------------------------------|--------------------|-------------|
| <b>Cost</b>                             |                                      |                    |             |
| January 1, 2018                         | 35,205,605                           | 3,405,327          | 38,610,932  |
| Additions                               | 4,988,699                            | -                  | 4,988,699   |
| Disposals                               | (1,510,000)                          | -                  | (1,510,000) |
| December 31, 2018                       | 38,684,304                           | 3,405,327          | 42,089,631  |
| <b>Accumulated depreciation</b>         |                                      |                    |             |
| January 1, 2018                         | 16,013,370                           | 2,871,497          | 18,884,867  |
| Depreciation                            | 5,613,557                            | 223,353            | 5,836,910   |
| Disposals                               | (341,666)                            | -                  | (341,666)   |
| December 31, 2018                       | 21,285,261                           | 3,094,850          | 24,380,111  |
| Net carrying value at December 31, 2018 | 17,399,043                           | 310,477            | 17,709,520  |

(7)

|  | Furniture, fixtures and<br>equipment | Computer equipment | Total             |
|--|--------------------------------------|--------------------|-------------------|
| <b>Cost</b>                                    |                                      |                    |                   |
| January 1, 2017                                | 27,981,010                           | 2,768,298          | 30,749,308        |
| Additions                                      | 12,244,594                           | 637,029            | 12,881,623        |
| Disposals                                      | (1,200,000)                          | -                  | (1,200,000)       |
| Transfers to Parent Bank                       | (3,820,000)                          | -                  | (3,820,000)       |
| <b>December 31, 2017</b>                       | <b>35,205,604</b>                    | <b>3,405,327</b>   | <b>38,610,931</b> |
| <b>Accumulated depreciation</b>                |                                      |                    |                   |
| January 1, 2017                                | 12,726,861                           | 2,500,596          | 15,227,457        |
| Depreciation                                   | 5,520,525                            | 370,901            | 5,891,426         |
| Disposals                                      | (1,119,066)                          | -                  | (1,119,066)       |
| Transfers to Parent Bank                       | (1,114,950)                          | -                  | (1,114,950)       |
| <b>December 31, 2017</b>                       | <b>16,013,370</b>                    | <b>2,871,497</b>   | <b>18,884,867</b> |
| <b>Net carrying value at December 31, 2017</b> | <b>19,192,234</b>                    | <b>533,830</b>     | <b>19,726,064</b> |

Details of sale of property and equipment follow:

|  | Consolidated |          | Parent      |          |
|--|--------------|----------|-------------|----------|
|  | 2018         | 2017     | 2018        | 2017     |
| Proceeds on the sale of property and equipment | 1,168,333    | 1,000    | 1,168,333   | 1,000    |
| Net book value of the asset sold               | (1,168,333)  | 80,934   | (1,168,333) | (80,934) |
| Loss on sale                                   | -            | (79,934) | -           | (79,934) |

Depreciation is included in occupancy and equipment-related expenses in the statement of income.

#### **Note 9 - Deferred income taxes, net**

Deferred income tax (DIT) assets, net as at December 31 represent the tax effects of the following temporary differences, including the period in which the temporary differences are expected to be recovered or settled:

|  | Consolidated        |                     | Parent              |                    |
|--|---------------------|---------------------|---------------------|--------------------|
|  | 2018                | 2017                | 2018                | 2017               |
| <b>DIT assets</b>  |                     |                     |                     |                    |
| Allowance for impairment   | 24,909,303          | 25,073,897          | 24,736,721          | 24,993,414         |
| Provision for short-term employee benefit  | 4,784,507           | 10,617,154          | 1,707,553           | 6,302,594          |
| Past service cost  | 4,298,292           | 1,491,378           | 2,967,907           | 1,100,803          |
| Stock options plan   | 1,338,366           | 1,279,735           | 1,338,366           | 1,279,735          |
| Others   | -                   | 1,478,871           | -                   | 1,653              |
| <b>Total DIT assets</b>  | <b>35,330,468</b>   | <b>39,941,035</b>   | <b>30,750,547</b>   | <b>33,678,199</b>  |
| <b>DIT liabilities</b>   |                     |                     |                     |                    |
| Retirement benefit asset   | (10,559,047)        | (7,540,025)         | (9,178,532)         | (6,285,486)        |
| Unrealized fair value gains on financial assets at fair value through other comprehensive income | (15,013,046)        | (17,112,409)        | (14,194,708)        | -                  |
| <b>Total DIT liabilities</b>   | <b>(25,572,093)</b> | <b>(24,652,434)</b> | <b>(23,373,240)</b> | <b>(6,285,486)</b> |
| <b>DIT assets, net</b>   | <b>9,758,375</b>    | <b>15,288,601</b>   | <b>7,377,307</b>    | <b>27,392,713</b>  |

(8)

The movements in DIT assets, net for the years ended December 31 are as follows:

|  | Consolidated |             | Parent       |             |
|--|--------------|-------------|--------------|-------------|
|  | 2018         | 2017        | 2018         | 2017        |
| Beginning of year  | 15,288,601   | 15,158,640  | 27,392,713   | 29,412,697  |
| (Credited to) charged against statement of income        | (6,982,690)  | 1,387,798   | (4,381,030)  | 562,438     |
| (Credited to) charged against other comprehensive income | (13,391,166) | (1,257,837) | (15,634,376) | (2,582,422) |
| Credited directly to retained earnings                   | 14,843,630   | -           | -            | -           |
| End of year  | 9,758,375    | 15,288,601  | 7,377,307    | 27,392,713  |

*Significant judgment: Realization of DIT assets*

The recognition of DIT assets depend on management's assessment of adequate future taxable income against which the temporary differences can be applied. The Group reviews the carrying amounts of DIT assets at the end of each reporting period and reduces the amounts to the extent that it is no longer probable that sufficient taxable profit will allow all or part of its DIT assets to be utilized. The Group's management believes that the DIT assets at the end of each reporting period will be fully realized.

**Note 10 - Other assets, net**

The account at December 31 consists of:

|  | Note | Consolidated |             | Parent      |             |
|--|------|--------------|-------------|-------------|-------------|
|  |      | 2018         | 2017        | 2018        | 2017        |
| Retirement benefit asset                                   | 17   | 39,039,879   | 28,307,335  | 30,595,108  | 20,282,483  |
| Creditable withholding taxes                               |      | 14,161,062   | 17,530,029  | 5,813,529   | 2,981,555   |
| Software and other investments                             |      | 8,804,997    | 8,804,997   | 8,804,997   | 8,804,997   |
| Prepaid expenses   |      | 1,580,738    | 1,493,821   | -           | -           |
| Prepaid taxes  |      | 590,792      | 899,783     | -           | -           |
| Trading right  |      | 440,000      | 440,000     | -           | -           |
| Others   |      | 12,095,699   | 3,753,957   | 10,945,524  | 2,580,484   |
|  |      | 76,713,167   | 61,229,922  | 56,159,158  | 34,649,519  |
| Allowance for impairment of software and other investments |      | (7,189,666)  | (7,563,851) | (7,189,666) | (7,563,851) |
|  |      | 69,523,501   | 53,666,071  | 48,969,492  | 27,085,668  |

The current and non-current portion of other assets, net follow:

|             | Consolidated |            | Parent     |            |
|-------------|--------------|------------|------------|------------|
|             | 2018         | 2017       | 2018       | 2017       |
| Current     | 17,940,405   | 4,892,904  | 16,359,667 | 4,892,904  |
| Non-current | 51,583,096   | 48,773,167 | 32,609,825 | 22,192,764 |
|             | 69,523,501   | 53,666,071 | 48,969,492 | 27,085,668 |

(9)

The movements in allowance for impairment for the years ended December 31 are as follows:

|                                      | Consolidated |           | Parent    |           |
|--------------------------------------|--------------|-----------|-----------|-----------|
|                                      | 2018         | 2017      | 2018      | 2017      |
| Beginning of year                    | 7,563,851    | 7,189,667 | 7,563,851 | 7,189,667 |
| (Reversal of) provision for the year | (374,185)    | 374,184   | (374,185) | 374,184   |
| End of year                          | 7,189,666    | 7,563,851 | 7,189,666 | 7,563,851 |

**Note 11 - Accounts payable and other liabilities**

The account at December 31 consists of:

|                            | Note | Consolidated |             | Parent      |             |
|----------------------------|------|--------------|-------------|-------------|-------------|
|                            |      | 2018         | 2017        | 2018        | 2017        |
| Trade payable              |      | 315,252,083  | 644,727,335 | 3,970,073   | 26,173,213  |
| Income tax payable         |      | 63,591,508   | 29,477,753  | 63,591,508  | 26,753,254  |
| Due to related parties     | 18   | 35,599,629   | 5,881,269   | -           | 69,808      |
| Taxes and licenses payable |      | 32,218,084   | 26,152,225  | 29,093,844  | 18,907,865  |
| Accrued salaries and wages |      | 16,147,540   | 35,588,730  | 5,891,026   | 21,206,862  |
| Accrued expenses           |      | 6,362,548    | 9,129,680   | 367,604     | 337,750     |
| Withholding taxes payable  |      | 2,228,039    | 648,964     | -           | -           |
| Others                     |      | 7,265,227    | 8,418,599   | 6,390,675   | 7,559,973   |
|                            |      | 478,664,658  | 760,024,555 | 109,304,730 | 101,008,725 |

Trade payable mainly pertains to accounts payable to customers.

Other liabilities mainly pertain to final tax on premium on debt securities and other fees.

Trade payable and other liabilities are expected to be settled within the next financial year.

**Note 12 - Share capital; accumulated reserves**

*Share capital*

Details of share capital at December 31, 2018 and 2017 follow:

|  | Consolidated |               | Parent      |               |
|--|--------------|---------------|-------------|---------------|
|  | Shares       | Amount        | Shares      | Amount        |
| Authorized, at P10 par value per share |              |               |             |               |
| Common shares                          | 100,000,000  | 1,000,000,000 | 100,000,000 | 1,000,000,000 |
| Issued and outstanding shares          |              |               |             |               |
| Common shares                          | 50,643,508   | 506,435,080   | 50,643,508  | 506,435,080   |

On June 9, 2017, the Board of Directors of the Parent Company declared cash dividends amounting to P2.5 billion on its total outstanding common shares as at April 30, 2017 record date, which was subsequently paid on July 21, 2017. The dividend rate per share is P49.36.

No dividends were declared by the Board of Directors of the Parent Company during 2018.

### Retained earnings

As at December 31, 2018, the Parent Company has retained earnings in excess of its additional paid-in capital amounting to P2.3B. Management intends to retain the excess to cover the growth in its merchant banking activities, in preparation for any potential equity investment if the market proves favorable. Likewise, the excess will be used by the Parent Company for its regular and future capital market underwriting activities for both debt and equity securities.

### Accumulated reserves

The details and movements of the account for the years ended December 31 are summarized as follow:

|   | Notes | Consolidated  |              | Parent        |              |
|---|-------|---------------|--------------|---------------|--------------|
|   |       | 2018          | 2017         | 2018          | 2017         |
| Fair value reserve on financial assets at fair value through other comprehensive income, net of tax |       |               |              |               |              |
| Beginning of year   |       | 126,467,292   | 1,288,686    | 26,295,462    | (95,436,793) |
| Impact of PFRS 9 adoption   | 21    | 507,723       | -            | 60,750,600    | -            |
| Restated balance at January 1, 2018   |       | 126,975,015   | 1,288,686    | 87,046,062    | (95,436,793) |
| Deferred tax effect   |       | 2,273,293     | (115,751)    | -             | -            |
| Realized gain on sale of FVOCI securities credited directly to retained earnings                    |       | (34,635,134)  | -            | -             | -            |
| Unrealized fair value (loss) gain   |       | (121,247,569) | 220,034,295  | (113,669,925) | 216,693,353  |
| Realized gain recycled to profit or loss  | 3     | -             | (94,739,938) | -             | (94,961,098) |
| End of year   |       | (26,634,395)  | 126,467,292  | (26,623,863)  | 26,295,462   |
| Remeasurement of defined benefit plan, net of tax   |       |               |              |               |              |
| Beginning of year   |       | 6,035,018     | (76,784)     | 6,173,919     | 148,172      |
| Remeasurement gain  |       | 3,653,214     | 6,148,683    | 3,552,938     | 6,025,747    |
| Deferred tax effect   |       | (30,083)      | (36,881)     | -             | -            |
| End of year   | 17    | 9,658,149     | 6,035,018    | 9,726,857     | 6,173,919    |
| Stock option reserve  |       |               |              |               |              |
| Beginning of year   |       | 4,227,702     | 3,819,375    | 4,227,702     | 2,882,194    |
| Employee stock option plan amortization   |       | 1,338,366     | 408,327      | 1,338,366     | 1,345,508    |
| End of year   |       | 5,566,068     | 4,227,702    | 5,566,068     | 4,227,702    |
|   |       | (11,410,178)  | 136,730,012  | (11,330,938)  | 36,697,083   |

### Note 13 - Fees and commissions

The account for the years ended December 31 consists of income from the following activities:

|                                   | Consolidated |               | Parent      |             |
|-----------------------------------|--------------|---------------|-------------|-------------|
|                                   | 2018         | 2017          | 2018        | 2017        |
| Underwriting and loan syndication | 676,324,105  | 898,551,350   | 676,324,105 | 898,551,350 |
| Commissions                       | 206,836,585  | 262,527,272   | -           | -           |
| Financial advisory                | 41,776,093   | 32,957,248    | 41,776,093  | 32,957,248  |
| Broker's fees                     | 18,190,337   | 9,457,773     | 18,190,337  | 9,457,773   |
| Service fees                      | 9,874,416    | 9,415,913     | 9,874,416   | 9,415,913   |
|                                   | 953,001,536  | 1,212,909,556 | 746,164,951 | 950,382,284 |

(11)

#### **Note 14 - Interest income**

Interest income for the years ended December 31 are as follows:

|                                     | Consolidated |             | Parent     |             |
|-------------------------------------|--------------|-------------|------------|-------------|
|                                     | 2018         | 2017        | 2018       | 2017        |
| Interbank loans receivable and SPAR | 33,602,971   | 57,397,332  | 33,602,971 | 57,397,332  |
| Investment securities               | 33,629,451   | 29,078,667  | 27,907,672 | 29,078,667  |
| Due from BSP                        | 16,160,217   | 20,250,716  | 16,160,217 | 20,250,716  |
| Cash in bank                        | 1,951,116    | 1,477,682   | 411,271    | 281,929     |
| Loans and receivables               | 56,437       | 164,120     | 56,437     | 164,120     |
| Held-to-maturity securities         | -            | 7,819,554   | -          | -           |
|                                     | 85,400,192   | 116,188,071 | 78,138,568 | 107,172,764 |

#### **Note 15 - Other operating expenses**

Other operating expenses for the years ended December 31 consists of:

|   | Note | Consolidated |             | Parent     |            |
|---|------|--------------|-------------|------------|------------|
|   |      | 2018         | 2017        | 2018       | 2017       |
| Outsourced services                         |      | 105,705,457  | 112,679,647 | 39,220,440 | 49,913,155 |
| Trading system charges                      |      | 45,986,465   | 46,445,168  | -          | -          |
| Periodicals and magazines                   |      | 15,254,940   | 14,155,523  | 15,254,940 | 14,155,523 |
| Advertising expense                         |      | 4,674,811    | 4,487,428   | 2,901,970  | 3,039,038  |
| Directors' remuneration                     | 18   | 3,152,352    | 2,640,000   | 2,412,352  | 1,996,000  |
| Representation and entertainment            |      | 3,049,026    | 3,037,013   | 1,711,860  | 1,815,700  |
| Transportation expense                      |      | 2,948,440    | 2,371,157   | 1,946,786  | 1,296,290  |
| Stationery and office supplies              |      | 2,576,605    | 2,981,457   | 1,457,128  | 1,851,454  |
| Postage and telegram                        |      | 2,080,875    | 2,084,333   | 2,080,875  | 2,084,333  |
| BSP supervision and examination fees        |      | 1,097,744    | 1,174,468   | 1,097,744  | 1,174,468  |
| Messengerial and other contractual services |      | 768,666      | 1,086,230   | -          | -          |
| Fees and charges                            |      | 75,281       | 1,187,945   | -          | -          |
| Others                                      |      | 12,403,502   | 10,562,893  | 7,018,935  | 3,247,453  |
|   |      | 199,774,164  | 204,893,262 | 75,103,030 | 80,573,414 |

Other operating expenses comprise mainly of travelling expenses, utilities expenses, membership fees and dues, and repairs and maintenance.

### **Note 16 - Income taxes**

The reconciliation between income tax expense at the statutory rate and the actual income tax expense presented in the statement of income for the years ended December 31 follows:

|  | Consolidated |          |              |          |
|--|--------------|----------|--------------|----------|
|  | 2018         |          | 2017         |          |
|  | Amount       | Rate (%) | Amount       | Rate (%) |
| Statutory income tax                         | 196,333,485  | 30.00    | 247,118,453  | 30.00    |
| Income tax effects of permanent differences: |              |          |              |          |
| Income subjected to lower tax rates, net     | (11,409,177) | (4.46)   | (28,803,209) | (3.50)   |
| Tax-exempt income                            | (33,701,470) | (1.85)   | (6,480,014)  | (0.79)   |
| Others, net                                  | 5,191,978    | 1.80     | 945,363      | 0.11     |
| Effective income tax expense                 | 156,414,816  | 28.73    | 212,780,593  | 38.45    |

  

|  | Parent       |          |              |          |
|--|--------------|----------|--------------|----------|
|  | 2018         |          | 2017         |          |
|  | Amount       | Rate (%) | Amount       | Rate (%) |
| Statutory income tax                         | 189,922,120  | 30.00    | 242,020,873  | 30.00    |
| Income tax effects of permanent differences: |              |          |              |          |
| Income subjected to lower tax rates, net     | (10,653,923) | (1.68)   | (27,872,535) | (3.44)   |
| Tax-exempt income                            | (32,014,729) | (5.06)   | (5,976,372)  | (0.74)   |
| Others, net                                  | 4,353,493    | 0.69     | 340,787      | 0.04     |
| Effective income tax expense                 | 151,606,961  | 23.95    | 208,512,753  | 25.86    |

### **Note 17 - Retirement benefits**

The BPI Group maintains both defined benefit and defined contribution retirement plans. Assets of both retirement plans are held in trust and governed by local regulations and practices in the Philippines. The key terms of these pension plans are discussed below.

#### **(a) Defined benefit retirement plan**

BPI has a unified plan which covers all subsidiaries except insurance entities. Under this plan, the normal retirement age is 60 years. Normal retirement benefit consists of a lump sum benefit equivalent to 200% of the basic monthly salary of the employee at the time of his retirement for each year of service, if he has rendered at least 10 years of service, or to 150% of his basic monthly salary, if he has rendered less than 10 years of service. For voluntary retirement, the benefit is equivalent to 112.50% of the employee's basic monthly salary for a minimum of 10 years of service with the rate factor progressing to a maximum of 200% of basic monthly salary for service years of 25 or more. Death or disability benefit, on the other hand, shall be determined on the same basis as in voluntary retirement.

The net defined benefit cost and contributions to be paid by the entities within the BPI Group are determined by an independent actuary.

The amount recognized in the statement of financial position as at December 31 follows:

|   | Consolidated |              | Parent       |              |
|---|--------------|--------------|--------------|--------------|
|   | 2018         | 2017         | 2018         | 2017         |
| Fair value of plan assets                             | 104,443,459  | 105,100,733  | 84,515,333   | 85,228,502   |
| Present value of defined benefit obligation           | (43,455,348) | (67,075,740) | (40,258,961) | (62,128,396) |
| Excess of plan assets over defined benefit obligation | 60,988,111   | 38,024,993   | 44,256,372   | 23,100,106   |
| Asset ceiling limit                                   | (21,911,469) | (9,717,658)  | (13,661,264) | 2,817,623    |
| Retirement benefit asset                              | 39,076,642   | 28,307,335   | 30,595,108   | 20,282,483   |

The retirement benefit asset is recorded as part of the other assets shown in the statement of financial position.

The movements in the present value of defined benefit obligation for the years ended December 31 follow:

|  | Consolidated |              | Parent       |              |
|--|--------------|--------------|--------------|--------------|
|  | 2018         | 2017         | 2018         | 2017         |
| Beginning of year                                | 67,075,740   | 87,914,498   | 62,128,396   | 78,728,840   |
| Current service cost                             | 7,659,776    | 7,196,304    | 6,207,271    | 5,837,601    |
| Interest cost                                    | 3,820,201    | 4,228,940    | 3,510,003    | 3,710,869    |
| Benefit payments                                 | (3,430,543)  | (17,160,173) | (3,430,543)  | (17,160,173) |
| Remeasurement - changes in financial assumptions | (31,669,826) | (15,103,829) | (28,156,166) | (8,988,741)  |
| End of year                                      | 43,455,348   | 67,075,740   | 40,258,961   | 62,128,396   |

The movements in fair value of plan asset for the years ended December 31 are as follows:

|                                       | Consolidated |              | Parent      |              |
|---------------------------------------|--------------|--------------|-------------|--------------|
|                                       | 2018         | 2017         | 2018        | 2017         |
| Beginning of year                     | 105,100,733  | 102,336,367  | 85,228,502  | 86,747,428   |
| Interest income                       | 6,287,589    | 5,299,438    | 5,017,879   | 4,344,766    |
| Contributions                         | 6,462,698    | 10,604,396   | 5,706,041   | 7,928,671    |
| Benefit payments                      | (3,430,543)  | (17,160,173) | (3,430,543) | (17,160,173) |
| Remeasurement - return on plan assets | (9,977,018)  | 4,020,705    | (8,006,546) | 3,367,810    |
| End of year                           | 104,443,459  | 105,100,733  | 84,515,333  | 85,228,502   |

The composition of the plan assets at fair value as at December 31 are as follows:

|                   | Consolidated |     |             |     |
|-------------------|--------------|-----|-------------|-----|
|                   | 2018         |     | 2017        |     |
|                   | Amount       | %   | Amount      | %   |
| Debt securities   | 34,871,284   | 31  | 39,567,369  | 38  |
| Equity securities | 43,769,193   | 53  | 38,573,758  | 37  |
| Others            | 25,802,982   | 16  | 26,959,606  | 26  |
|                   | 104,443,459  | 100 | 105,100,733 | 100 |

|                   | Parent     |     |            |     |
|-------------------|------------|-----|------------|-----|
|                   | 2018       |     | 2017       |     |
|                   | Amount     | %   | Amount     | %   |
| Debt securities   | 29,580,367 | 35  | 29,829,976 | 35  |
| Equity securities | 29,580,367 | 35  | 29,829,976 | 35  |
| Others            | 25,354,599 | 30  | 25,568,550 | 30  |
|                   | 84,515,333 | 100 | 85,228,502 | 100 |

The plan asset of the BPI unified plan include investments in BPI's common shares. The actual return on plan assets attributable to the Group for the year ended December 31, 2018 amounted to P4,959,139 (2017 - P7,059,681).

The Group has no other transactions with the fund other than the contributions presented above.

The principal actuarial assumptions used as at December 31 are as follows:

|                         | Consolidated   |                | Parent |       |
|-------------------------|----------------|----------------|--------|-------|
|                         | 2018           | 2017           | 2018   | 2017  |
| Discount rate           | 8.62% to 9.11% | 5.81% to 6.27% | 8.62%  | 5.81% |
| Future salary increases | 5.00%          | 5.00%          | 5.00%  | 5.00% |

Expected maturity analysis of undiscounted retirement benefits as at December 31:

|                   | Consolidated     |                   |                    |                     |                    |
|-------------------|------------------|-------------------|--------------------|---------------------|--------------------|
|                   | Less than a year | Between 1-5 years | Between 5-10 years | Between 10-15 years | More than 15 years |
| December 31, 2018 | 531,977          | 3,117,420         | 70,004,299         | 58,644,053          | 83,833,924         |
| December 31, 2017 | 1,246,590        | 21,284,648        | 35,467,003         | 105,313,957         | 324,070,615        |

  

|                   | Parent           |                   |                    |                     |                    |
|-------------------|------------------|-------------------|--------------------|---------------------|--------------------|
|                   | Less than a year | Between 1-5 years | Between 5-10 years | Between 10-15 years | More than 15 years |
| December 31, 2018 | 531,977          | 3,117,420         | 65,697,611         | 58,644,053          | 81,414,292         |
| December 31, 2017 | 1,246,590        | 21,284,648        | 26,951,733         | 88,837,000          | 197,442,781        |

Assumptions regarding future mortality and disability experience are based on published statistics generally used for local actuarial valuation purposes.

The defined benefit plan typically exposes the Group to a number of risks such as investment risk, interest rate risk and salary risk. The most significant of which relate to investment and interest rate risk. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of government bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating the terms of the related pension liability. A decrease in government bond yields will increase the defined benefit obligation although this will also be partially offset by an increase in the value of the plan's fixed income holdings. Hence, the present value of defined benefit obligation is directly affected by the discount rate to be applied by the Group. However, the Group believes that due to the long-term nature of the pension liability and the strength of the Group itself, the mix of debt and equity securities holdings of the plan is an appropriate element of the Group's long term strategy to manage the plan efficiently.

The Group ensures that the investment positions are managed within an asset-liability matching framework that has been developed to achieve long-term investments that are in line with the obligations under the plan. The Group's main objective is to match assets to the defined benefit obligation by investing primarily in long-term debt securities with maturities that match the benefit payments as they fall due. The asset-liability matching is being monitored on a regular basis and potential change in investment mix is being discussed with the trustor, as necessary to better ensure the appropriate asset-liability matching.

For the year ended December 31, 2018, the weighted average duration of the defined benefit obligation is 10.25 years (2017 - 9.2 years).

*Critical accounting estimate and assumption: Principal assumptions and estimation of retirement obligation*

The present value of the retirement benefit obligation depends on a number of factors that are determined on an actuarial basis using a number of assumptions. The assumptions used in determining the net cost for pensions include the discount rate and future salary increases. Any changes in these assumptions will impact the carrying amount of the retirement benefit obligation.

The Group determines the appropriate discount rate at the end of each period. This is the interest rate that should be used to determine the present value of estimated future cash outflows expected to be required to settle the retirement benefit obligation. In determining the appropriate discount rate, the Group considers the interest rates of high-quality government bonds that are denominated in the currency in which the benefits will be paid and that have terms to maturity approximating the terms of the related retirement obligation.

Other key assumptions for retirement benefit obligation are based in part on current market conditions.

The sensitivity of the defined benefit plan to changes in the weighted principal assumptions is presented as follows:

|                      | Consolidated                         |                        |                        |
|----------------------|--------------------------------------|------------------------|------------------------|
|                      | Impact on defined benefit obligation |                        |                        |
|                      | Change in assumption                 | Increase in assumption | Decrease in assumption |
| December 31, 2018    |                                      |                        |                        |
| Discount rate        | 0.5%                                 | (2,486,630)            | 2,695,427              |
| Salary increase rate | 1.0%                                 | 5,775,169              | (4,981,212)            |
| December 31, 2017    |                                      |                        |                        |
| Discount rate        | 0.5%                                 | (3,061,473)            | 3,302,100              |
| Salary increase rate | 1.0%                                 | 6,174,475              | (5,427,164)            |
|                      | Parent                               |                        |                        |
|                      | Impact on defined benefit obligation |                        |                        |
|                      | Change in assumption                 | Increase in assumption | Decrease in assumption |
| December 31, 2018    |                                      |                        |                        |
| Discount rate        | 0.5%                                 | (2,297,101)            | 2,484,623              |
| Salary increase rate | 1.0%                                 | 5,314,742              | (4,605,041)            |
| December 31, 2017    |                                      |                        |                        |
| Discount rate        | 0.5%                                 | (2,757,051)            | 2,966,939              |
| Salary increase rate | 1.0%                                 | 5,520,678              | (4,875,849)            |

(16)

The sensitivity analyses are based on a change in an assumption while holding all other assumptions constant. In practice, this is unlikely to occur, and changes in some of the assumptions may be correlated. When calculating the sensitivity of the defined benefit obligation to significant actuarial assumptions the same method (present value of the defined benefit obligation calculated with the projected unit credit method at the end of the reporting period) has been applied as when calculating the retirement benefit obligation recognized in the statement of financial position.

The methods and types of assumptions used in preparing the sensitivity analysis did not change compared to the previous period.

(b) Defined contribution retirement plan

All non-unionized employees hired on or after the January 1, 2016 are automatically under the new defined contribution plan. Employees hired prior to the effective date shall have the option to elect to become members of the new defined contribution plan.

The defined contribution retirement plan has a defined benefit minimum guarantee equivalent to a certain percentage of the monthly salary payable to an employee at normal retirement age with the required credited years of service based on the provisions of Republic Act (“RA”) No. 7641.

Under the normal or late retirement, employees are entitled to a benefit equal to the total of the following amounts:

- The higher between (a) cumulative fund balance equivalent to 8% of the basic monthly salary and (b) the minimum legal retirement benefit under the Retirement Law.
- Employee contributions fund.

Accordingly, the liability for the defined benefit minimum guarantee is actuarially calculated similar to the defined benefit plan.

Following are the details of the Group’s DC plan as at December 31 that has a DB minimum guarantee:

|   | Consolidated |             | Parent       |             |
|---|--------------|-------------|--------------|-------------|
|   | 2018         | 2017        | 2018         | 2017        |
| Fair value of plan assets                             | 22,965,680   | 12,106,196  | 17,459,554   | 9,210,159   |
| Present value of defined benefit obligation           | (7,372,485)  | (5,994,248) | (4,282,026)  | (4,147,980) |
| Excess of plan assets over defined benefit obligation | 15,593,195   | 6,111,948   | 13,177,528   | 5,062,179   |
| Asset ceiling limit                                   | (15,593,195) | (6,111,948) | (13,177,528) | (5,062,179) |
| Retirement benefit asset                              | -            | -           | -            | -           |

The movements in the present value of DB obligation for the year ended December 31 are as follows:

|  | Consolidated |             | Parent      |           |
|--|--------------|-------------|-------------|-----------|
|  | 2018         | 2017        | 2018        | 2017      |
| Beginning of year                                | 5,994,248    | 4,774,819   | 4,147,980   | 3,372,775 |
| Current service cost                             | 2,558,676    | 2,349,818   | 1,578,247   | 1,483,008 |
| Interest expense                                 | 362,427      | 258,409     | 247,220     | 185,503   |
| Benefit payments                                 | (111,622)    | -           | -           | -         |
| Remeasurement - changes in financial assumptions | (1,431,244)  | (1,388,798) | (1,691,421) | (893,306) |
| End of year                                      | 7,372,485    | 5,994,248   | 4,282,026   | 4,147,980 |

The movements in the fair value of plan asset for the year ended December 31 are as follows:

|                                       | Consolidated |            | Parent     |           |
|---------------------------------------|--------------|------------|------------|-----------|
|                                       | 2018         | 2017       | 2018       | 2017      |
| Beginning of year                     | 12,106,196   | 6,024,814  | 9,210,159  | 4,639,666 |
| Interest income                       | 971,337      | 1,488,039  | 730,413    | 350,415   |
| Contributions                         | 8,131,653    | 3,564,630  | 6,090,189  | 3,463,024 |
| Benefit payments                      | (111,622)    | -          | -          | -         |
| Remeasurement - return on plan assets | 1,868,116    | 1,028,713  | 1,428,793  | 757,054   |
| End of year                           | 22,965,680   | 12,106,196 | 17,459,554 | 9,210,159 |

The components of pension expense recognized in the statement of income for the years ended December 31 consist of:

|                      | Consolidated |             | Parent      |           |
|----------------------|--------------|-------------|-------------|-----------|
|                      | 2018         | 2017        | 2018        | 2017      |
| Current service cost | 10,218,452   | 7,196,304   | 7,785,518   | 7,320,609 |
| Net interest cost    | (2,305,439)  | (1,017,009) | (1,525,659) | (705,245) |
| Pension expense      | 7,913,013    | 6,179,295   | 6,259,859   | 6,615,364 |

Pension expense is presented as part of compensation and fringe benefits account for the years ended December 31, 2018 and 2017.

The movements in reserve for remeasurement of retirement obligation as at December 31 are as follows:

|  | Note | Consolidated |              | Parent       |             |
|--|------|--------------|--------------|--------------|-------------|
|  |      | 2018         | 2017         | 2018         | 2017        |
| Beginning of year                        |      | (6,035,018)  | 76,784       | (6,173,919)  | (211,676)   |
| Remeasurement (gain) loss on DBO         |      | (33,101,070) | (11,124,423) | (29,847,587) | (7,606,513) |
| Remeasurement (gain) loss on plan assets |      | 8,108,902    | (4,020,705)  | 6,577,753    | (3,367,810) |
| Changes in the effect of asset ceiling   |      | 20,115,639   | 5,638,461    | 18,493,580   | 2,366,115   |
| Adjustments                              |      | (209,561)    | 808,429      | (209,561)    | -           |
|  |      | (5,086,090)  | (8,698,238)  | (4,985,815)  | (8,608,208) |
|  |      | (11,121,108) | (8,621,454)  | (11,159,734) | (8,819,884) |
| Deferred tax effect                      |      | 1,462,959    | 2,586,436    | 1,432,876    | 2,645,965   |
| End of year                              | 12   | (9,658,149)  | (6,035,018)  | (9,726,858)  | (6,173,919) |

Remeasurements on retirement benefits recognized in OCI are presented in the statement of total comprehensive income net of 30% deferred tax.

### **Note 18 - Related party transactions**

In the normal course of business, the Group transacts with its Parent Bank and other related entities and with its directors, officers, shareholders and related interest (DOSRI).

These transactions such as loans and advances, deposit arrangements, underwriting/advisory services and advances for operating expenses are made in the normal operating activities and have terms and conditions that are generally comparable to those offered to non-related parties and to similar transactions in the market.

(18)

Transactions with the Parent Bank include outsourcing of services related to the following activities: (a) anti-money laundering; (b) accounting and securities administration services; (c) deposit arrangements; and (d) loan operations, treasury operations, human resource-related functions and information systems.

BPI Family Savings Bank, Inc. (BPI FSB), and BPI Card Finance Corporation (BCFC) are fellow entities under common control. Transactions with these fellow subsidiaries consist primarily of outsourcing of services related to information systems.

Significant related party transactions as at and for the years ended December 31 are summarized below:

Consolidated

|                                  | Transactions<br>for the year | Outstanding<br>Balances | Terms and conditions   |
|----------------------------------|------------------------------|-------------------------|--|
| December 31, 2018                |                              |                         |  |
| Loans and other receivables, net |                              |                         |  |
| Parent Bank                      | 532,298                      | 738,780                 | - Unsecured<br>- Non-interest bearing<br>- Non-guaranteed<br>- Collectible in cash on demand<br>- Unsecured<br>- Interest of 2.65%           |
|                                  | 532,298                      | 738,780                 |  |
| Cash deposits to:                |                              |                         |  |
| Parent Bank                      | (70,263,435)                 | 719,800,191             | - These are demand and savings deposits bearing the following average interest rates:<br>Demand - 0.22% to 0.50%<br>Savings - 0.76% to 1.14% |
| BPI FSB                          | 6,277                        | 1,551,317               |  |
|                                  | (70,257,158)                 | 721,351,508             |  |
| Other liabilities                |                              |                         |  |
| Parent Bank                      | 28,179,523                   | 34,060,332              | - Unsecured<br>- Non-interest bearing<br>- Payable in cash on demand   |
|                                  | 28,179,523                   | 34,060,332              |  |

|                                  | Transactions<br>for the year | Outstanding<br>Balances | Terms and conditions   |
|----------------------------------|------------------------------|-------------------------|--|
| December 31, 2017                |                              |                         |  |
| Loans and other receivables, net |                              |                         |  |
| Parent Bank                      | (204,846)                    | 206,482                 | - Unsecured<br>- Non-interest bearing<br>- Non-guaranteed<br>- Collectible in cash on demand<br>- Unsecured<br>- Interest of 2.65%           |
|                                  | (204,846)                    | 206,482                 |  |
| Cash deposits to:                |                              |                         |  |
| Parent Bank                      | 337,320,561                  | 790,063,625             | - These are demand and savings deposits bearing the following average interest rates:<br>Demand - 0.22% to 0.41%<br>Savings - 0.76% to 1.14% |
| BPI FSB                          | 6,522                        | 1,545,041               |  |
|                                  | 337,327,083                  | 791,608,666             |  |
| Other liabilities                |                              |                         |  |
| Parent Bank                      | (4,437,798)                  | 5,881,269               | - Unsecured<br>- Non-interest bearing<br>- Payable in cash on demand   |
|                                  | (4,437,798)                  | 5,881,269               |  |

Parent

|                                  | Transactions<br>for the year | Outstanding<br>Balances | Terms and conditions   |
|----------------------------------|------------------------------|-------------------------|--|
| December 31, 2018                |                              |                         |  |
| Loans and other receivables, net |                              |                         |  |
| Parent Bank                      | 532,298                      | 738,780                 | - Unsecured<br>- Non-interest bearing<br>- Non-guaranteed<br>- Collectible in cash on demand   |
|                                  | 532,298                      | 738,780                 |  |
| Cash deposits to:                |                              |                         |  |
| Parent Bank                      | (181,242,112)                | 280,071,888             | - These are demand and savings deposits bearing the following average interest rates:<br>Demand - 0.22% to 0.41%<br>Savings - 0.76% to 1.14% |
| BPI FSB                          | 6,277                        | 1,551,317               |  |
|                                  | (181,235,835)                | 281,623,205             |  |
| Other liabilities                |                              |                         |  |
| Parent Bank                      | (1,609,106)                  | (1,539,297)             | - Unsecured<br>- Non-interest bearing<br>- Payable in cash on demand   |
|                                  | (1,609,106)                  | (1,539,297)             |  |

|                                  | Transactions<br>for the year | Outstanding<br>Balances | Terms and conditions   |
|----------------------------------|------------------------------|-------------------------|--|
| December 31, 2017                |                              |                         |  |
| Loans and other receivables, net |                              |                         |  |
| Parent Bank                      | (204,846)                    | (206,482)               | - Unsecured<br>- Non-interest bearing<br>- Non-guaranteed<br>- Collectible in cash on demand |
|                                  | (204,846)                    | (206,482)               |  |
| Cash deposits to:                |                              |                         |  |
| Parent Bank                      | 313,319,273                  | 461,313,999             | - These are demand and savings<br>deposits bearing the following average<br>interest rates:  |
| BPI FSB                          | 6,522                        | 1,545,041               | Demand - 0.22% to 0.41%<br>Savings - 0.76% to 1.14%  |
|                                  | 313,325,795                  | 462,859,040             |  |
| Other liabilities                |                              |                         |  |
| Parent Bank                      | 69,808                       | 69,808                  | - Unsecured  |
| BPI Securities                   | (9,107,143)                  | -                       | - Non-interest bearing<br>- Payable in cash on demand  |
|                                  | (9,037,335)                  | 69,808                  |  |

The aggregate amounts included in the determination of income before income tax that resulted from transactions with each class of related parties are as follows:

|  | Consolidated |             | Parent      |            |
|--|--------------|-------------|-------------|------------|
|  | 2018         | 2017        | 2018        | 2017       |
| Interest income                                    |              |             |             |            |
| Parent Bank  | 1,752,774    | 1,381,145   | 212,929     | 219,524    |
| BPI FSB  | 5,272        | 9,403       | 5,272       | 9,403      |
|  | 1,758,046    | 1,390,548   | 218,201     | 228,927    |
| Outsourcing services                               |              |             |             |            |
| Parent Bank  | 98,054,159   | 101,745,602 | 39,225,482  | 49,913,155 |
| Rent   |              |             |             |            |
| Parent Bank  | 4,629,108    | 4,500,938   | 4,629,108   | 4,500,938  |
| Fees and commission                                |              |             |             |            |
| Parent Bank  | 112,003,586  | 5,107,344   | 112,003,586 | 5,107,344  |
| Retirement benefits                                |              |             |             |            |
| Key management personnel                           | 6,017,669    | 6,999,247   | 3,767,169   | 4,722,399  |
| Salaries, allowances and other short-term benefits |              |             |             |            |
| Key management personnel                           | 97,109,264   | 107,514,700 | 65,459,264  | 75,891,200 |
| Directors' remuneration                            | 3,152,352    | 2,640,000   | 2,412,352   | 1,996,000  |

There were no provisions recognized against receivables from related parties. Also, no additional provision was recognized during the year.

Details of DOSRI loans and interest income earned are as follows:

|   | Consolidated |           | Parent |           |
|---|--------------|-----------|--------|-----------|
|   | 2018         | 2017      | 2018   | 2017      |
| Outstanding DOSRI loans                     | -            | 1,740,690 | -      | 1,740,690 |
| Interest income earned                      | -            | 164,120   | -      | 164,120   |
| % to total outstanding loans and receivable | 0.00%        | 23.96%    | 0.00%  | 23.96%    |
| % to total outstanding DOSRI loans          |              |           |        |           |
| Unsecured DOSRI loans                       | 0.00%        | Nil       | 0.00%  | Nil       |
| Past due DOSRI loans                        | 0.00%        | 0.00%     | 0.00%  | 0.00%     |
| Non-performing DOSRI loans                  | 0.00%        | Nil       | 0.00%  | Nil       |

At December 31, 2018 and 2017, the Group is in full compliance with the General Banking Act and the Bangko Sentral ng Pilipinas regulations on DOSRI loans.

### **Note 19 - Financial risk and capital management**

The Board of Directors carries out its risk management function through the Risk Management Committee (RMC) of the BOD. The RMC is tasked with nurturing a culture of risk management across the enterprise. The RMC sets the risk appetite; proposes and approves risk management policies, frameworks, and guidelines; and regularly reviews risk management structures, metrics, limits, and issues across the Group, in order to meet and comply with regulatory and international standards on risk measurement and management.

At the management level, the Risk Management Office (RMO) is headed by the Chief Risk Officer (CRO). The CRO is ultimately responsible in leading the formulation of risk management policies and methodologies in alignment with the overall business strategy of the Group, ensuring that risks are prudently and rationally undertaken and within its risk appetite, as well as commensurate and disciplined to maximize returns on shareholders' capital. Risk management is carried out by a dedicated team of skilled risk managers and senior officers who have extensive prior operational experience. The Group's risk managers regularly monitor key risk indicators and report exposures against carefully established financial and business risk metrics and limits approved by the RMC. Finally, independent reviews are regularly conducted by the Internal Audit group and regulatory examiners to ensure that risk controls and mitigants are in place and functioning effectively as intended.

The possibility of incurring losses is, however, compensated by the possibility of earning more than expected income. Risk-taking is, therefore, not entirely negative to be avoided. Risk-taking actions present opportunities if risks are fully identified and accounted, deliberately taken, and are kept within prudent and rationalized limits.

The most important financial risks that the Group manages are credit risk, liquidity risk and market risk.

#### **19.1 Credit risk**

The Group takes on exposure to credit risk, which is the risk that counterparty will cause a financial loss for the Group by failing to discharge an obligation. Significant changes in the economy, or in the health of a particular industry segment that may represent a concentration in the Group's portfolio, could result in losses that are different from those provided for at the reporting date. Management therefore carefully manages its exposure to credit risk. Credit exposures arise principally in loans and receivables and debt securities.

(22)

### 19.1.1 Credit risk management

#### (a) Trade and other receivables

The Company applies the PFRS 9 simplified approach to measuring expected credit losses which uses a lifetime expected loss allowance for all trade and other receivables. The detailed impairment policy of the Company is disclosed in Note 21.

#### (b) Debt securities carried at amortized cost

Investments in high grade securities and bills are viewed as a way to gain better credit quality mix and at the same time, maintain a readily available source to meet funding requirements. The level of credit risk for treasury and other investment debt securities and their associated probability of default (PD) are determined using reputable external ratings and/or available and reliable qualitative and quantitative information. In the absence of credit ratings, a comparable issuer or guarantor rating is used. Should there be a change in the credit rating of the chosen comparable, evaluation is made to ascertain whether the rating change is applicable to the security being assessed for impairment.

| Classifications     | Credit Risk Grade following S&P or its equivalent |
|---------------------|---|
| Standard monitoring | IG (AAA to BBB-)                                  |
| Special monitoring  | Non-IG (BB+ to C)                                 |
| Default             | Default (D)                                       |

### 19.1.2 Risk limit control and mitigation policies

The Group manages limits and controls concentrations of credit risk wherever they are identified, in particular, to individual counterparties and groups, to industries and sovereigns.

The Group structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored on a regular basis and subject to an annual or more frequent review, when considered necessary.

The exposure to any one borrower is further restricted by sub-limits covering on- and off- balance sheet exposures. Actual exposures against limits are monitored regularly.

Exposure to credit risk is also managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate.

The Group employs a range of policies and practices to mitigate credit risk such as collateral. Collateral is one of the most traditional and common practice in mitigating credit risk which serves as security particularly for loans and receivables. The Group implements guidelines on the acceptability of specific classes of collateral for credit risk mitigation. The principal collateral type for loans and receivable used by the Group is mortgages over real estate properties and chattels. In order to minimize credit loss, the Group seeks additional collateral from the counterparty when impairment indicators are observed for the relevant individual loans and receivables.

### 19.1.3 Maximum exposure to credit risk

Credit risk exposures relating to on-balance sheet assets are as follows:

|  | Consolidated  |               | Parent        |               |
|--|---------------|---------------|---------------|---------------|
|  | 2018          | 2017          | 2018          | 2017          |
| Cash and other cash items                    | 762,809,446   | 855,680,373   | 281,623,204   | 462,859,040   |
| Due from BSP                                 | 1,100,401,541 | 541,029,448   | 1,100,401,541 | 541,029,448   |
| Interbank loans receivable and SPAR          | 291,153,583   | 192,523,005   | 291,153,583   | 192,523,005   |
| Financial assets at FVTPL                    | 101,401,709   | 1,195,492,111 | 101,401,709   | 1,195,492,111 |
| Investment securities at amortized cost, net | 655,551,035   | 223,945,103   | 558,355,206   | -             |
| Trade and other receivables, net             | 293,073,876   | 537,355,932   | 103,334,310   | 44,912,154    |
|  | 3,204,391,190 | 3,546,025,972 | 2,436,269,553 | 2,436,815,758 |

The carrying amount of financial assets above also represents the Group's maximum exposure to credit risk.

The following table contain an analysis of the credit risk exposure of each financial instrument.

### 19.1.4 Credit quality of financial assets other than trade and other receivables

Credit risk exposures relating to on-balance sheet assets are as follows:

#### Consolidated

|  | 2018                       |                         |                            | Total         | 2017          |
|--|----------------------------|-------------------------|----------------------------|---------------|---------------|
|  | ECL Staging                |                         |                            |               |               |
|  | Stage 1<br>12-month<br>ECL | Stage 2<br>Lifetime ECL | Stage 3<br>Lifetime<br>ECL |               |               |
| Cash and other cash items                    | 281,623,204                | 481,186,242             | -                          | 762,809,446   | 855,680,373   |
| Due from BSP                                 | 1,100,401,541              | -                       | -                          | 1,100,401,541 | 541,029,448   |
| Interbank loans receivable and SPAR          | 291,153,583                | -                       | -                          | 291,153,583   | 192,523,005   |
| Financial assets at FVTPL                    | 101,401,709                | -                       | -                          | 101,401,709   | 1,195,736,176 |
| Held-to-maturity securities                  | -                          | -                       | -                          | -             | 223,945,103   |
| Investment securities at amortized cost, net | 558,355,206                | 97,195,829              | -                          | 655,551,035   | -             |
| Gross carrying amount                        | 2,332,935,243              | 578,382,071             | -                          | 2,911,317,314 | 3,008,914,105 |
| Loss allowance                               | -                          | -                       | -                          | -             | -             |
| Carrying amount                              | 2,332,935,243              | 578,382,071             | -                          | 2,911,317,314 | 3,008,914,105 |

Parent

|  | 2018                    |                            |                         |               | 2017          |
|--|-------------------------|----------------------------|-------------------------|---------------|---------------|
|  | ECL Staging             |                            |                         |               | Total         |
|  | Stage 1<br>12-month ECL | Stage 2<br>Lifetime<br>ECL | Stage 3<br>Lifetime ECL | Total         |               |
| Cash and other cash items                    | 281,623,204             | -                          | -                       | 281,623,204   | 462,859,040   |
| Due from BSP                                 | 1,100,401,541           | -                          | -                       | 1,100,401,541 | 541,029,448   |
| Interbank loans receivable and SPAR          | 291,153,583             | -                          | -                       | 291,153,583   | 192,523,005   |
| Financial assets at FVTPL                    | 101,401,709             | -                          | -                       | 101,401,709   | 1,195,736,176 |
| Investment securities at amortized cost, net | 558,355,206             | -                          | -                       | 558,355,206   | -             |
| Gross carrying amount                        | 2,332,935,243           | -                          | -                       | 2,332,935,243 | 2,392,147,669 |
| Loss allowance                               | -                       | -                          | -                       | -             | -             |
| Carrying amount                              | 2,332,935,243           | -                          | -                       | 2,332,935,243 | 2,392,147,669 |

(a) Cash and other cash items

Cash and other cash items substantially consist of deposit placements with the Parent Bank and its subsidiary.

(b) Due from BSP, interbank loans receivable and SPAR

Due from BSP, interbank loans receivable and SPAR are made with a sovereign counterparty and are considered fully performing.

The table below presents the ratings of debt securities, treasury bills and other government securities based on Standard & Poor's rating:

Consolidated

| December 31, 2018 | Financial assets at fair value through profit or loss | Financial assets at amortized cost | Total       |
|-------------------|---|------------------------------------|-------------|
| A- to A+          | 7,365,645   | -                                  | 7,365,645   |
| Lower than A-     | 94,036,064  | 655,551,035                        | 749,587,099 |
|                   | 101,401,709   | 655,551,035                        | 756,952,744 |

| December 31, 2017 | Financial assets at fair value through profit or loss | Financial assets at amortized cost | Total         |
|-------------------|---|------------------------------------|---------------|
| A- to A+          | 28,627,319  | -                                  | 28,627,319    |
| Lower than A-     | 1,166,864,792   | 223,945,103                        | 1,390,809,895 |
|                   | 1,195,492,111   | 223,945,103                        | 1,419,437,214 |

Parent

| December 31, 2018 | Financial assets at fair value through profit or loss | Financial assets at amortized cost | Total       |
|-------------------|---|------------------------------------|-------------|
| A- to A+          | 7,365,645   | -                                  | 7,365,645   |
| Lower than A-     | 94,036,064  | 558,355,206                        | 652,391,270 |
|                   | 101,401,709   | 558,355,206                        | 659,756,915 |

  

| December 31, 2017 | Financial assets at fair value through profit or loss | Financial assets at amortized cost | Total         |
|-------------------|---|------------------------------------|---------------|
| A- to A+          | 28,627,319  | -                                  | 28,627,319    |
| Lower than A-     | 1,166,864,792   | -                                  | 1,166,864,792 |
|                   | 1,195,492,111   | -                                  | 1,195,492,111 |

The above financial assets are deemed to have low credit risk. Accordingly, the applicable 12-month expected credit loss is deemed not material for financial reporting purposes.

**19.1.5 Credit quality of trade and other receivables, net**

The carrying amount of the Group's trade and other receivables as at December 31, 2018 amounts to P219,098,198 (2017 - P537,182,022).

The Group's trade and other receivables generally arise from transactions with various unrated counterparties with good credit standing. The BPI Group applies the PFRS 9 simplified approach to measuring expected credit losses which uses a lifetime expected loss methodology for trade and other receivables.

Credit risk exposures relating to trade and other receivable follows:

Consolidated

|                             | 2018                    |                         |                         |              | 2017         |
|-----------------------------|-------------------------|-------------------------|-------------------------|--------------|--------------|
|                             | ECL Staging             |                         |                         |              | Total        |
|                             | Stage 1<br>12-month ECL | Stage 2<br>Lifetime ECL | Stage 3<br>Lifetime ECL | Total        |              |
| Trade and other receivables | -                       | 219,098,198             | 73,975,678              | 293,073,876  | 611,453,459  |
| Loss allowance              | -                       | -                       | (73,975,678)            | (73,975,678) | (74,271,437) |
| Carrying amount             | -                       | 219,098,198             | -                       | 219,098,198  | 537,182,022  |

Parent

|                             | 2018                    |                         |                         |              | 2017         |
|-----------------------------|-------------------------|-------------------------|-------------------------|--------------|--------------|
|                             | ECL Staging             |                         |                         |              | Total        |
|                             | Stage 1<br>12-month ECL | Stage 2<br>Lifetime ECL | Stage 3<br>Lifetime ECL | Total        |              |
| Trade and other receivables | -                       | 29,933,905              | 73,400,405              | 103,334,310  | 119,009,681  |
| Loss allowance              | -                       | -                       | (73,400,405)            | (73,400,405) | (74,097,527) |
| Carrying amount             | -                       | 29,933,905              | -                       | 29,933,905   | 44,912,154   |

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## 19.2 Concentration of risk on financial assets with credit risk exposure

The Group's main credit exposure at their carrying amounts, as categorized by industry sectors are as follows:

### Consolidated

At December 31, 2018

|   | Financial institutions | Manufacturing | Real estate | Others | Total |
|---|------------------------|---------------|-------------|--------|-------|
| <i>(In million pesos)</i>                   |                        |               |             |        |       |
| Cash and other cash items                   | 763                    | -             | -           | -      | 763   |
| Due from BSP                                | 1,100                  | -             | -           | -      | 1,100 |
| Interbank loans receivable and SPAR         | 291                    | -             | -           | -      | 291   |
| Financial assets at FVTPL – debt securities | 94                     | 5             | 2           | -      | 101   |
| Financial assets at amortized cost          | 656                    | -             | -           | -      | 656   |
| Trade and other receivables                 | 11                     | 8             | -           | 201    | 220   |
|   | 2,915                  | 13            | 2           | 201    | 3,131 |

At December 31, 2017

|                                      | Financial institutions | Manufacturing | Real estate | Others | Total |
|--------------------------------------|------------------------|---------------|-------------|--------|-------|
| <i>(In million pesos)</i>            |                        |               |             |        |       |
| Cash and other cash items            | 856                    | -             | -           | -      | 856   |
| Due from BSP                         | 541                    | -             | -           | -      | 541   |
| Interbank loans receivable and SPAR  | 193                    | -             | -           | -      | 193   |
| Trading securities - debt securities | 1,167                  | 1             | 28          | -      | 1,196 |
| Trade and other receivables          | -                      | -             | -           | 537    | 537   |
|                                      | 2,757                  | 1             | 28          | 537    | 3,323 |

### Parent

At December 31, 2018

|   | Financial institutions | Manufacturing | Real estate | Others | Total |
|---|------------------------|---------------|-------------|--------|-------|
| <i>(In million pesos)</i>                   |                        |               |             |        |       |
| Cash and other cash items                   | 282                    | -             | -           | -      | 282   |
| Due from BSP                                | 1,100                  | -             | -           | -      | 1,100 |
| Interbank loans receivable and SPAR         | 291                    | -             | -           | -      | 291   |
| Financial assets at FVTPL - debt securities | 94                     | 5             | 2           | -      | 101   |
| Financial assets at amortized cost          | 558                    | -             | -           | -      | 558   |
| Trade and other receivables                 | 11                     | 8             | -           | 11     | 30    |
|   | 2,336                  | 13            | 2           | 11     | 2,362 |

At December 31, 2017

|                                      | Financial institutions | Manufacturing | Real estate | Others | Total |
|--------------------------------------|------------------------|---------------|-------------|--------|-------|
| <i>(In million pesos)</i>            |                        |               |             |        |       |
| Cash and other cash items            | 463                    | -             | -           | -      | 463   |
| Due from BSP                         | 541                    | -             | -           | -      | 541   |
| Interbank loans receivable and SPAR  | 193                    | -             | -           | -      | 193   |
| Trading securities - debt securities | 1,167                  | 1             | 28          | -      | 1,196 |
| Trade and other receivables          | -                      | -             | -           | 45     | 45    |
|                                      | 2,364                  | 1             | 28          | 45     | 2,438 |

### 19.3 Market risk management

The Group is exposed to market risk - the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk management is guided by policies and procedures reviewed by the Group's RMC and approved by the Executive Committee/Board of Directors.

The Group reviews and controls market risk exposures in its trading operations. Trading portfolios include those positions arising from the Group's market-making transactions.

To estimate its exposure to market risk, the Group computes the statistical "value at risk" (VaR) of its trading position on a daily basis. The VaR measurement estimates, at 99% degree of confidence, the maximum loss, due to adverse market movements, that could be incurred by portfolios over assumed holding periods. As such, there remains 1% statistical probability that portfolios' actual loss could be greater than the VaR estimate.

VaR of the Group as at December 31 follows:

|                   | Consolidated   |        | Parent |        |
|-------------------|----------------|--------|--------|--------|
|                   | 2018           | 2017   | 2018   | 2017   |
|                   | (In thousands) |        |        |        |
| Balance Sheet VaR | 23,962         | 22,016 | 20,372 | 27,036 |

VaR is an integral part of the Group's market risk control system. VaR limits for all trading portfolios are set by the Group's Board of Directors. Actual market risk exposures vis-à-vis market risk limits are reported daily to the Group's management as well as the Parent Bank's FRMC.

### 19.4 Foreign exchange risk

The Group takes on exposure to the effects of fluctuations in the prevailing exchange rates on its foreign currency financial position and cash flows.

The Group's exposure to foreign currency exchange rate risk at December 31, 2018 arises from its cash and other cash items denominated in United States Dollar (US Dollar) amounting to P188,322,680 (2017 - P109,188,148). The Group has no foreign-currency denominated liabilities as at December 31, 2018 and 2017.

Net realized foreign exchange gain from foreign currency denominated transactions for the year ended December 31, 2018 amounted to P5,949,948 (2017 - 4,585,794).

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At December 31, 2018 and 2017, if the Philippine Peso had weakened/strengthened by 1% against the US Dollar based on rate 60 days after reporting period with all other variables held constant, pre-tax income as at and for the year ended December 31, 2018 would have been P2 million (2017 - P3 million) higher/lower, mainly as a result of foreign exchange gains/losses on translation of US Dollar-denominated assets.

### 19.5 Interest rate risk

Cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Fair value interest rate risk is the risk that the value of a financial instrument will fluctuate because of changes in market interest rates. The Group takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on both its fair value and cash flow risks. Interest margins may increase as a result of such changes but may also result in losses in the event that unexpected movements arise. The Board of Directors sets limits on the level of mismatch of interest rate repricing that may be undertaken, which is monitored daily by the Parent Bank's RMC.

The table below summarizes the Group's exposure to interest rates to its financial assets with no repricing. The Group has no financial liabilities with exposure to interest rate risk as at December 31, 2018 and 2017.

#### Consolidated

|   | 2018          | 2017          |
|---|---------------|---------------|
| Financial assets  |               |               |
| Cash and other cash items   | 762,809,446   | 855,680,373   |
| Due from BSP  | 1,100,401,541 | 541,029,448   |
| Interbank loans receivable and securities purchased under agreements to resell (SPAR) | 291,153,583   | 192,523,005   |
| Financial assets at FVTPL - debt securities   | 101,401,709   | -             |
| Financial assets at amortized cost  | 655,551,035   | -             |
| Trading securities - debt securities  | -             | 1,195,492,111 |
| Held-to maturity securities   | -             | 223,945,103   |
| Trade and other receivables, net  | 219,673,471   | 537,355,932   |
|   | 3,130,990,785 | 3,546,025,972 |

#### Parent

|   | 2018          | 2017          |
|---|---------------|---------------|
| Financial assets  |               |               |
| Cash and other cash items   | 281,623,204   | 462,859,040   |
| Due from BSP  | 1,100,401,541 | 541,029,448   |
| Interbank loans receivable and securities purchased under agreements to resell (SPAR) | 291,153,583   | 192,523,005   |
| Financial assets at FVTPL - debt securities   | 101,401,709   | -             |
| Financial assets at amortized cost  | 558,355,206   | -             |
| Trading securities - debt securities  | -             | 1,195,492,111 |
| Trade and other receivables, net  | 29,933,905    | 44,912,154    |
|   | 2,362,869,148 | 2,436,815,758 |

## **19.6 Price risk**

The Group is exposed to price risk to the extent of equity securities held under trading securities and available-for-sale securities. The Group's sensitivity and exposure to price risk on its equity securities are measured and monitored through the Group's VaR (Note 19.3).

## **19.7 Liquidity risk**

Liquidity risk is the risk that the Group is unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. The consequence may be the failure to meet current obligations and/or immediate sale of securities.

The Group's liquidity management process, as carried out within the Group and monitored by the Group's RMC and the Parent Bank's FRMC includes:

- Day-to-day funding, managed by monitoring future cash flows to ensure that requirements can be met. This includes replenishment of funds as they mature or are borrowed by customers;
- Maintaining a portfolio of highly marketable assets that can easily be liquidated as protection against any unforeseen interruption to cash flow;
- Monitoring balance sheet liquidity ratios against internal and regulatory requirements; and
- Managing the concentration and profile of debt maturities.

Monitoring and reporting take the form of cash flow measurement and projections for the next day, week and month respectively, as these are key periods for liquidity management. The starting point for these projections is an analysis of the contractual maturity of the financial liabilities and the expected collection date of the financial assets.

The table below presents the maturity profile of non-derivative financial instruments based on undiscounted cash flows, which the Group uses to manage the inherent liquidity risk. The analysis into maturity grouping is based on the remaining period from the end of the reporting period to the contractual maturity date or, if earlier, the expected date the financial asset will be realized or the financial liability will be settled.

Consolidated

| As at December 31, 2018  | Up to 1 year         | Over 1 up to<br>3 years | Over 3 years       | Total                |
|--|----------------------|-------------------------|--------------------|----------------------|
| <b>Financial assets</b>  |                      |                         |                    |                      |
| Cash and other cash items  | 762,809,446          | -                       | -                  | 762,809,446          |
| Due from BSP   | 1,100,401,541        | -                       | -                  | 1,100,401,541        |
| Interbank loans receivable and SPAR  | 291,153,583          | -                       | -                  | 291,153,583          |
| Financial assets at FVTPL - debt securities  | 101,926,905          | 1,380,155               | 552,083            | 103,859,143          |
| Financial assets at amortized cost   | 31,313,574           | 45,027,838              | 558,131,802        | 634,473,214          |
| Trade and other receivables, net   | 219,547,569          | 125,902                 | -                  | 219,673,471          |
| <b>Total financial assets</b>  | <b>2,507,152,618</b> | <b>46,533,895</b>       | <b>558,683,885</b> | <b>3,112,370,398</b> |
| <b>Financial liabilities</b>   |                      |                         |                    |                      |
| Trade payables to customers, net   | 304,946,612          | -                       | -                  | 304,946,612          |
| Accounts payable   | 10,305,471           | -                       | -                  | 10,305,471           |
| Accrued expenses, excluding accrued taxes and licenses and other non-financial liabilities | 22,521,517           | -                       | -                  | 22,521,517           |
| Due to related parties   | 37,138,926           | -                       | -                  | 37,138,926           |
| Miscellaneous, excluding non-financial liabilities   | 7,154,586            | -                       | -                  | 7,154,586            |
| <b>Total financial liabilities</b>   | <b>382,067,112</b>   | <b>-</b>                | <b>-</b>           | <b>382,067,112</b>   |
| <b>Total maturity gap</b>  | <b>2,125,085,506</b> | <b>46,533,895</b>       | <b>558,683,885</b> | <b>2,730,303,286</b> |
| <hr/>  |                      |                         |                    |                      |
| As at December 31, 2017  | Up to 1 year         | Over 1 up to<br>3 years | Over 3 years       | Total                |
| <b>Financial assets</b>  |                      |                         |                    |                      |
| Cash and other cash items  | 855,680,373          | -                       | -                  | 855,680,373          |
| Due from BSP   | 541,029,448          | -                       | -                  | 541,029,448          |
| Interbank loans receivable and SPAR  | 192,523,005          | -                       | -                  | 192,523,005          |
| Trading securities   | 205,137,127          | 336,828,254             | 653,526,730        | 1,195,492,111        |
| Trade and other receivables, net   | 530,439,964          | 6,117,970               | 797,998            | 537,355,932          |
| <b>Total financial assets</b>  | <b>2,324,809,917</b> | <b>342,946,224</b>      | <b>654,324,728</b> | <b>3,322,080,869</b> |
| <b>Financial liabilities</b>   |                      |                         |                    |                      |
| Trade payables to customers, net   | 610,590,594          | -                       | -                  | 610,590,594          |
| Accounts payable   | 33,906,841           | -                       | -                  | 33,906,841           |
| Accrued expenses, excluding accrued taxes and licenses and other non-financial liabilities | 44,205,931           | -                       | -                  | 44,205,931           |
| Due to related parties   | 5,881,269            | -                       | -                  | 5,881,269            |
| Miscellaneous, excluding non-financial liabilities   | 8,278,148            | -                       | -                  | 8,278,148            |
| <b>Total financial liabilities</b>   | <b>702,862,783</b>   | <b>-</b>                | <b>-</b>           | <b>702,862,783</b>   |
| <b>Total maturity gap</b>  | <b>1,621,947,134</b> | <b>342,946,224</b>      | <b>654,324,728</b> | <b>2,619,218,086</b> |

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Parent

| As at December 31, 2018   | Up to 1 year         | Over 1 up to<br>3 years | Over 3 years       | Total                |
|---|----------------------|-------------------------|--------------------|----------------------|
| <b>Financial assets</b>   |                      |                         |                    |                      |
| Cash and other cash items   | 281,623,204          | -                       | -                  | 281,623,204          |
| Due from BSP  | 1,100,401,541        | -                       | -                  | 1,100,401,541        |
| Interbank loans receivable and SPAR   | 291,153,583          | -                       | -                  | 291,153,583          |
| <b>Financial assets at FVTPL - debt securities</b>  |                      |                         |                    |                      |
|   | 101,926,905          | 1,380,155               | 552,083            | 103,859,143          |
| Financial assets at amortized cost  | 31,313,574           | 45,027,838              | 558,131,802        | 634,473,214          |
| Trade and other receivables, net  | 29,808,003           | 125,902                 | -                  | 29,933,905           |
| <b>Total financial assets</b>   | <b>1,836,226,810</b> | <b>46,533,895</b>       | <b>558,683,885</b> | <b>2,441,444,590</b> |
| <b>Financial Liabilities</b>  |                      |                         |                    |                      |
| Accounts payable  | 3,970,073            | -                       | -                  | 3,970,073            |
| <b>Accrued expenses, excluding accrued taxes and licenses and other non-financial liabilities</b> |                      |                         |                    |                      |
|   | 6,258,630            | -                       | -                  | 6,258,630            |
| Due to related parties  | 1,539,297            | -                       | -                  | 1,539,297            |
| <b>Miscellaneous, excluding non-financial liabilities</b>   |                      |                         |                    |                      |
|   | 6,390,675            | -                       | -                  | 6,390,675            |
| <b>Total financial liabilities</b>  | <b>18,158,675</b>    | <b>-</b>                | <b>-</b>           | <b>18,158,675</b>    |
| <b>Total maturity gap</b>   | <b>1,818,068,135</b> | <b>46,533,895</b>       | <b>558,683,885</b> | <b>2,423,285,915</b> |

| As at December 31, 2017   | Up to 1 year         | Over 1 up to<br>3 years | Over 3 years       | Total                |
|---|----------------------|-------------------------|--------------------|----------------------|
| <b>Financial assets</b>   |                      |                         |                    |                      |
| Cash and other cash items   | 462,859,040          | -                       | -                  | 462,859,040          |
| Due from BSP  | 541,029,448          | -                       | -                  | 541,029,448          |
| Interbank loans receivable and SPAR   | 192,523,005          | -                       | -                  | 192,523,005          |
| Trading account securities  | 205,137,127          | 336,828,254             | 653,526,730        | 1,195,492,111        |
| Trade and other receivables, net  | 37,996,186           | 6,117,970               | 797,998            | 44,912,154           |
| <b>Total financial assets</b>   | <b>1,439,544,806</b> | <b>342,946,224</b>      | <b>654,324,728</b> | <b>2,436,815,758</b> |
| <b>Financial Liabilities</b>  |                      |                         |                    |                      |
| Accounts payable  | 25,943,313           | -                       | -                  | 25,943,313           |
| <b>Accrued expenses, excluding accrued taxes and licenses and other non-financial liabilities</b> |                      |                         |                    |                      |
|   | 21,020,704           | -                       | -                  | 21,020,704           |
| Due to related parties  | 69,808               | -                       | -                  | 69,808               |
| <b>Miscellaneous, excluding non-financial liabilities</b>   |                      |                         |                    |                      |
|   | 7,559,973            | -                       | -                  | 7,559,973            |
| <b>Total financial liabilities</b>  | <b>54,593,798</b>    | <b>-</b>                | <b>-</b>           | <b>54,593,798</b>    |
| <b>Total maturity gap</b>   | <b>1,384,951,008</b> | <b>342,946,224</b>      | <b>654,324,728</b> | <b>2,382,221,960</b> |

## 19.8 Fair value hierarchy

The following table presents the fair value hierarchy of the Group's significant assets and liabilities at December 31:

### Consolidated

| 2018                                | Fair value  |               |             | Total         |
|-------------------------------------|-------------|---------------|-------------|---------------|
|                                     | Level 1     | Level 2       | Level 3     |               |
| Recurring measurements              |             |               |             |               |
| Financial assets                    |             |               |             |               |
| Financial assets at FVTPL           | 243,296,826 | 530,136,480   | -           | 773,433,306   |
| Financial assets at FVOCI           | 323,575,200 | 97,551        | 447,741,248 | 771,413,999   |
| Fair values disclosed               |             |               |             |               |
| Financial assets                    |             |               |             |               |
| Cash and other cash items           | -           | 762,809,446   | -           | 762,809,446   |
| Due from BSP                        | -           | 1,100,401,541 | -           | 1,100,401,541 |
| Interbank loans receivable and SPAR | -           | 291,153,583   | -           | 291,153,583   |
| Financial assets at amortized cost  | 97,195,829  | 509,731,347   | -           | 606,927,176   |
| Trade and other receivables, net    | -           | 219,673,471   | -           | 219,673,471   |
| Financial liabilities               |             |               |             |               |
| Other liabilities                   | -           | 16,619,378    | -           | 16,619,378    |
| 2017                                |             |               |             |               |
| Recurring measurements              |             |               |             |               |
| Financial assets                    |             |               |             |               |
| Trading securities                  | 359,118,963 | 1,169,664,017 | -           | 1,528,782,980 |
| Available-for-sale securities       | 204,117,445 | 168,942,900   | 243,824,566 | 616,884,911   |
| Fair values disclosed               |             |               |             |               |
| Financial assets                    |             |               |             |               |
| Cash and other cash items           | -           | 855,680,373   | -           | 855,680,373   |
| Due from BSP                        | -           | 541,029,448   | -           | 541,029,448   |
| Interbank loans receivable and SPAR | -           | 192,523,005   | -           | 192,523,005   |
| Held-to-maturity securities         | 231,180,438 | -             | -           | 231,180,438   |
| Trade and other receivables, net    | -           | 537,355,932   | -           | 537,355,932   |
| Financial liabilities               |             |               |             |               |
| Other liabilities                   | -           | 54,823,698    | -           | 54,823,698    |

Parent

| 2018                                | Fair value  |               |             | Total         |
|-------------------------------------|-------------|---------------|-------------|---------------|
|                                     | Level 1     | Level 2       | Level 3     |               |
| Recurring measurements              |             |               |             |               |
| Financial assets                    |             |               |             |               |
| Financial assets at FVTPL           | 94,036,064  | 530,136,480   | -           | 624,172,544   |
| Financial assets at FVOCI           | 323,575,200 | -             | 447,741,248 | 771,316,448   |
| Fair values disclosed               |             |               |             |               |
| Financial assets                    |             |               |             |               |
| Cash and other cash items           | -           | 281,623,204   | -           | 281,623,204   |
| Due from BSP                        | -           | 1,100,401,541 | -           | 1,100,401,541 |
| Interbank loans receivable and SPAR | -           | 291,153,583   | -           | 291,153,583   |
| Financial assets at amortized cost  | -           | 509,731,347   | -           | 509,731,347   |
| Trade and other receivables, net    | -           | 29,933,905    | -           | 29,933,905    |
| Financial liabilities               |             |               |             |               |
| Other liabilities                   | -           | 16,619,378    | -           | 16,619,378    |

| 2017                                | Fair value  |               |             | Total         |
|-------------------------------------|-------------|---------------|-------------|---------------|
|                                     | Level 1     | Level 2       | Level 3     |               |
| Recurring measurements              |             |               |             |               |
| Financial assets                    |             |               |             |               |
| Trading securities                  | 359,118,963 | 1,169,664,017 | -           | 1,528,782,980 |
| Available-for-sale securities       | -           | 168,836,564   | 243,824,566 | 412,661,130   |
| Fair values disclosed               |             |               |             |               |
| Financial assets                    |             |               |             |               |
| Cash and other cash items           | -           | 462,859,040   | -           | 462,859,040   |
| Due from BSP                        | -           | 541,029,448   | -           | 541,029,448   |
| Interbank loans receivable and SPAR | -           | 192,523,005   | -           | 192,523,005   |
| Trade and other receivables, net    | -           | 44,912,154    | -           | 44,912,154    |
| Financial liabilities               |             |               |             |               |
| Other liabilities                   | -           | 54,593,798    | -           | 54,593,798    |

The Group's RMC is responsible for performing the valuation of fair value measurements included in the financial statements, including Level 3 fair values. The valuation processes and results for recurring measurements are reviewed and approved by the Chief Risk Officer (CRO) at least once every quarter, in line with the Group's quarterly reporting dates. The valuation processes and results for non-recurring measurements are reviewed and approved by the CRO in the quarter in which the measurement occurs. All Level 3 valuation results are discussed with the Audit Committee as part of its quarterly review of the Group's financial statements.

The Group's Level 2 financial instruments include government debt securities. The fair values of Level 2 financial instruments are estimated using values obtained from government board summary.

The table below shows the valuation techniques and applicable unobservable inputs used to measure the Group's Level 3 financial instruments as at December 31:

| Description                | 2018        | 2017        | Valuation technique                     | Unobservable inputs                     |
|----------------------------|-------------|-------------|---|---|
| Unlisted equity securities | 447,741,248 | 243,824,566 | Net asset value;<br>investment multiple | Net asset value;<br>investment multiple |

There is no gain included in profit or loss for assets held under Level 3 for the reporting periods.

The investment valuation sensitivity of the underlying portfolio investee company is mainly impacted by the movement in net asset value and investment multiple. At December 31, 2018 and 2017, if the net asset value and investment had increased/ decreased by 1% with all other variables held constant, net income and equity as at and for the year ended December 31, 2018 would have been P4,448,627 (2017 - P2,454,746) higher/lower.

### 19.9 Offsetting of financial assets and liabilities

The following financial assets and liabilities are subject to offsetting, enforceable master netting arrangements and similar agreements:

|                              | 2018   |  | Net amount presented in the statement of financial position |
|------------------------------|--|--|---|
|                              | Gross amounts of recognized financial assets (liabilities) | Gross amounts of recognized financial assets (liabilities) |   |
| <b>Financial assets</b>      |  |  |   |
| Trade receivables from       |  |  |   |
| Customers                    | 310,837,296  | (129,465,368)  | 181,371,928   |
| Clearing house               | 316,348,055  | (309,833,463)  | 6,514,592   |
| <b>Financial liabilities</b> |  |  |   |
| Trade payables to            |  |  |   |
| Customers                    | (434,411,980)  | 129,465,368  | (304,946,612)   |
| Clearing house               | (309,833,463)  | 309,833,463  | -   |
| <hr/>                        |  |  |   |
|                              | 2017   |  | Net amount presented in the statement of financial position |
|                              | Gross amounts of recognized financial assets (liabilities) | Gross amounts of recognized financial assets (liabilities) |   |
| <b>Financial assets</b>      |  |  |   |
| Trade receivables from       |  |  |   |
| Customers                    | 393,062,134  | (238,271,749)  | 154,790,385   |
| Clearing house               | 728,983,263  | (391,574,849)  | 337,408,414   |
| <b>Financial liabilities</b> |  |  |   |
| Trade payables to            |  |  |   |
| Customers                    | (848,862,343)  | 238,271,749  | (610,590,594)   |
| Clearing house               | (391,574,849)  | 391,574,849  | -   |

Trade receivable from customers in the statements of financial position are reported net of allowance for impairment as at December 31, 2018 amounting to P575,273 (2017 - P173,910) (Note 3).

For financial assets and liabilities subject to enforceable master netting arrangements or similar arrangements above, each agreement between the Company and the counterparty allows for net settlement of the relevant financial assets and liabilities when both elect to settle on a net basis. In the absence of such an election, financial assets and liabilities will be settled on a gross basis, however, each party to the master netting agreement or similar agreement will have the option to settle all such amounts on a net basis in the event of default of the other party.

### 19.10 Capital management

Capital management is understood to be a facet of risk management. The primary objective of the Group is the generation of recurring acceptable returns to shareholders' capital. To this end, the Group's policies, business strategies and activities are directed towards the generation of cash flows that are in excess of its fiduciary and contractual obligations to its depositors, and to its various funders and stakeholders.

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Cognizant of its exposure to risks, the Group understands that it must maintain sufficient capital to absorb unexpected losses, to stay in business for the long haul, and to satisfy regulatory requirements. The Group further understands that its performance, as well as the performance of its various units, should be measured in terms of returns generated vis-à-vis allocated capital and the amount of risk borne in the conduct of business.

Effective January 1, 2014, the BSP, through its Circular 781, requires each bank and its financial affiliated subsidiaries to adopt new capital requirements in accordance with the provisions of Basel III. The new guidelines are meant to strengthen the composition of the Bank's capital by increasing the level of core capital and regulatory capital. The Circular sets out minimum Common Equity Tier 1 (CET1) ratio and Tier 1 Capital ratios of 6.0% and 7.5%, respectively. A capital conservation buffer of 2.5%, comprised of CET1 capital, was likewise imposed. The minimum required capital adequacy ratio remains at 10% which includes the capital conservation buffer.

Qualifying capital and risk-weighted assets are computed based on BSP regulations. The qualifying capital of the Group consists of core tier 1 capital and tier 2 capital. Tier 1 capital comprises paid-up capital stock, paid-in surplus, surplus including net income for the year, surplus reserves less deductions such as deferred income tax, unsecured credit accommodations to DOSRI and unrealized fair value losses on financial assets at fair value through other comprehensive income. Tier 2 capital includes net unrealized fair value gains on financial assets at fair value through other comprehensive income, and general loan loss provisions for BSP reporting purposes. The Group has fully complied with the CAR requirement. The Group's capital-to-risk assets ratio is 74.32% (2017 - 62.50 %).

Under the provisions of Section 8 of Republic Act (RA) No. 8366, an Act amending Presidential Decree No. 29, otherwise known as the Investment Houses Law, the Group is required to maintain a minimum paid-up capital of P300,000,000.

At December 31, 2018 and 2017, the Group has complied with the CAR required by the BSP and the minimum capital requirement prescribed by the Investment Houses Law.

**Note 20 - Basic quantitative indicators of financial performance**

The key financial performance indicators of the Group follow:

|                          | Consolidated |        | Parent |        |
|--------------------------|--------------|--------|--------|--------|
|                          | 2018         | 2017   | 2018   | 2017   |
| Return on average equity | 9.68%        | 12.96% | 13.76% | 14.02% |
| Return on average assets | 8.38%        | 8.99%  | 11.94% | 13.16% |
| Net interest margin      | 1.84%        | 2.22%  | 2.01%  | 2.41%  |

**Note 21 - Summary of significant accounting policies**

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to both years presented, unless otherwise stated.

## 21.1 Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with Philippine Financial Reporting Standards (PFRS). The term PFRS in general includes all applicable PFRS, Philippine Accounting Standards (PAS), and interpretations of the Philippine Interpretations Committee (PIC), Standing Interpretations Committee (SIC) and International Financial Reporting Interpretations Committee (IFRIC) which have been approved by the Financial Reporting Standards Council (FRSC) and adopted by the SEC.

The Parent Company is a wholly-owned subsidiary of BPI. BPI, as an ultimate parent company, publishes consolidated financial statements which are available for public use and prepared in accordance with Philippine Financial Reporting Standards. In accordance with IAS 27, Consolidated Financial Statements, the Parent Company is not required to prepare consolidated financial statements as it is a parent that is in itself a controlled subsidiary. These consolidated financial statements are prepared by management for BSP reporting purposes only.

These consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of financial assets at fair value through profit or loss and financial assets at fair value through other comprehensive income (available-for-sale in 2017) which measured at fair value.

The preparation of consolidated financial statements in conformity with PFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 19.

### Changes in accounting policy and disclosures

#### (a) New standards adopted by the Group

The Group has adopted the following standards effective January 1, 2018:

- *PFRS 15, 'Revenue from contracts with customers'* replaces PAS 18, 'Revenue' which covers contracts for goods and services and PAS 11, 'Construction contracts' which covers construction contracts. The new standard is based on the principle that revenue is recognized when control of a good or service transfers to a customer - so the notion of control replaces the existing notion of risks and rewards.

A new five-step process must be applied before revenue can be recognized: (1) identify contracts with customers, (2) identify the separate performance obligation, (3) determine the transaction price of the contract, (4) allocate the transaction price to each of the separate performance obligations, and (5) recognize the revenue as each performance obligation is satisfied.

The adoption of PFRS 15 did not have a material impact on the financial statements of the Group.

- *PFRS 9, 'Financial instruments'* replaces the provisions of PAS 39 that relate to the recognition, classification and measurement of financial assets and financial liabilities, derecognition of financial instruments, impairment of financial assets and hedge accounting.

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### PFRS 9 adoption

The adoption of PFRS 9 resulted in changes in accounting policies and adjustments to the amounts previously recognized in the financial statements. The Group did not early adopt any provisions of PFRS 9 in previous periods.

As permitted by the transitional provisions of PFRS 9, the Group elected not to restate comparative figures. Resulting adjustments to the carrying amounts of financial assets at the date of transition were recognized in the opening balance of “Retained earnings” and “Accumulated Reserves” as of January 1, 2018.

The adoption of PFRS 9 has resulted in changes mainly in the Group’s accounting policies for recognition, classification and measurement and impairment of financial assets. There were no changes in the classification of financial liabilities. PFRS 9 also significantly amends other standards dealing with financial instruments such as PFRS 7, Financial Instruments: Disclosures.

The Group shifted from incurred loss model under PAS 39 to expected credit loss model in the determination of impairment provisions for financial assets not carried at fair value through profit or loss upon adoption of PFRS 9. The adoption did not result to significant adjustments on the level of allowance for credit losses recognized as at December 31, 2017.

Set out below are disclosures relating to the impact of the adoption of PFRS 9 on the Company:

#### *Classification and measurement of financial assets*

The measurement category and the carrying amount of financial assets in accordance with PFRS 9 (from PAS 39) at January 1, 2018 are as follows:

#### Consolidated

|  | PAS 39               |                   | PFRS 9               |                 |
|--|----------------------|-------------------|----------------------|-----------------|
|  | Measurement category | December 31, 2017 | Measurement category | January 1, 2018 |
| Financial assets   |                      | Carrying amount   |                      | Carrying amount |
| Cash and other cash items  | Amortized cost       | 855,680,373       | Amortized cost       | 855,680,373     |
| Due from Bangko Sentral ng Pilipinas   | Amortized cost       | 541,029,448       | Amortized cost       | 541,029,448     |
| Interbank loans receivable and securities purchased under agreements to resell | Amortized cost       | 192,523,005       | Amortized cost       | 192,523,005     |
| Financial assets at fair value through profit or loss (FVTPL)                  |                      |                   |                      |                 |
| Debt   | FVTPL                | 1,195,736,176     | FVTPL                | 651,970,664     |
| Equity   | FVTPL                | 333,046,804       | Amortized cost       | 548,127,557     |
| Financial assets at fair value through other comprehensive income (FVOCI)      |                      |                   | FVOCI                | 333,046,804     |
| Held-to-maturity securities (HTM)  | FVOCI (AFS)          | 616,884,911       | FVTPL                | 428,236,633     |
| Trade and other receivables  | Amortized cost       | 223,945,103       | Amortized cost       | 315,354,489     |
|  | Amortized cost       | 537,355,932       | Amortized cost       | 223,945,103     |
|  |                      |                   |                      | 537,355,932     |

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Parent

|  | PAS 39               |                 | PFRS 9               |                 |
|--|----------------------|-----------------|----------------------|-----------------|
|  | December 31, 2017    |                 | January 1, 2018      |                 |
| Financial assets   | Measurement category | Carrying amount | Measurement category | Carrying amount |
| Cash and other cash items  | Amortized cost       | 462,859,040     | Amortized cost       | 462,859,040     |
| Due from Bangko Sentral ng Pilipinas   | Amortized cost       | 541,029,448     | Amortized cost       | 541,029,448     |
| Interbank loans receivable and securities purchased under agreements to resell | Amortized cost       | 192,523,005     | Amortized cost       | 192,523,005     |
| Financial assets at fair value through profit or loss (FVTPL)                  |                      |                 |                      |                 |
| Debt   | FVTPL                | 1,195,736,176   | FVTPL                | 651,970,664     |
| Equity   | FVTPL                | 333,046,804     | Amortized cost       | 548,127,557     |
| Financial assets at fair value through other comprehensive income (FVOCI)      | FVOCI (AFS)          | 412,661,130     | FVOCI                | 333,046,804     |
| Trade and other receivables  | Amortized cost       | 44,912,154      | FVTPL                | 370,530,777     |
|  |                      |                 | Amortized cost       | 168,836,564     |
|  |                      |                 |                      | 44,912,154      |

*Reconciliation of balances from PAS 39 to PFRS 9*

On January 1, 2018, the Group performed a detailed analysis of its business models for managing financial assets including their cash flow characteristics.

The financial assets affected by the adoption of the new standard are shown below. The reconciliation of the carrying amounts of these financial assets from their previous measurement category in accordance with PAS 39 to their new measurement categories upon transition to PFRS 9 on January 1, 2018 follow:

Consolidated

|  | FVTPL - Trading securities | Investment securities at FVOCI (Available-for-sale in 2017) | Investment securities at amortized cost |
|--|----------------------------|---|---|
| Closing balance, December 31, 2017 - PAS 39      | 1,528,782,980              | 616,884,911   | 223,945,103                             |
| Reclassifications from:                          |                            |   |   |
| FVTPL to Investment securities at amortized cost | (543,765,512)              | -   | 548,127,556                             |
| AFS to FVTPL                                     | 315,354,489                | (315,354,489)   | -                                       |
| Remeasurement of AFS equity securities to FVOCI  | -                          | 126,706,211   | -                                       |
| Opening balance, January 1, 2018 - PFRS 9        | 1,300,371,957              | 428,236,633   | 772,072,659                             |

## Parent

|   | FVTPL -<br>Trading<br>securities | Investment securities at<br>FVOCI (Available-for-<br>sale in 2017) | Investment<br>securities at<br>amortized cost |
|---|----------------------------------|--|---|
| Closing balance,<br>December 31, 2017 - PAS 39      | 1,528,782,980                    | 412,661,130  | -   |
| Reclassifications from:                             |                                  |  |   |
| FVTPL to Investment securities at<br>amortized cost | (543,765,512)                    | -  | 548,127,556                                   |
| AFS to FVTPL  | 168,836,564                      | (168,836,564)  | -   |
| Remeasurement of AFS equity<br>securities to FVOCI  | -                                | 126,706,211  | -   |
| Opening balance,<br>January 1, 2018 - PFRS 9        | 1,153,854,032                    | 370,530,777  | 548,127,556                                   |

The impact on the relevant equity items as at January 1, 2018 is as follows:

## Consolidated

|  | Retained<br>earnings | Accumulated<br>reserves |
|--|----------------------|-------------------------|
| Closing balances, December 31, 2017 - PAS 39     | 2,923,328,646        | 136,730,012             |
| Reclassifications from:                          |                      |                         |
| FVTPL to Investment securities at amortized cost | 4,362,045            | -                       |
| AFS to FVTPL                                     | 86,536,624           | (86,536,624)            |
| Remeasurement of AFS securities to FVOCI         | 1,650,000            | 87,044,347              |
| Opening balances, January 1, 2018 - PFRS 9       | 3,015,877,315        | 137,237,735             |

## Parent

|  | Retained<br>earnings | Accumulated<br>reserves |
|--|----------------------|-------------------------|
| Closing balances, December 31, 2017 - PAS 39     | 2,554,828,904        | 36,697,083              |
| Reclassifications from:                          |                      |                         |
| FVTPL to Investment securities at amortized cost | 4,362,045            | -                       |
| AFS to FVTPL                                     | 26,293,748           | (26,293,747)            |
| Remeasurement of AFS securities to FVOCI         | 1,650,000            | 87,044,347              |
| Opening balances, January 1, 2018 - PFRS 9       | 2,587,134,697        | 97,447,683              |

In addition to the above, the following debt instruments have been reclassified to new categories under PFRS 9, as their previous categories under PAS 39 were 'retired', with no changes to their measurement basis:

- (i) Those previously classified as available-for-sale and now classified as measured at FVOCI; and
- (ii) Those previously classified as held-to-maturity and now classified as measured at amortized cost.

For financial assets that have been reclassified to the amortized cost category, the table below shows their fair values as at December 31, 2018 and the fair value gain or loss that would have been recognized if these financial assets had not been reclassified as part of the transition to PFRS 9:

|  |              |
|--|--------------|
| Fair value as at December 31, 2018   | 509,731,347  |
| Fair value loss that would have been recognized during the year if the financial asset had not been reclassified | (34,034,165) |

In addition to PFRS 9 and 15, the following amendments have also been adopted by the Group effective January 1, 2018:

- Amendments to PFRS 2 - Share-based payments
- IFRIC 22, Foreign currency transactions and advance consideration

The adoption of the above amendments did not have a material impact on the financial statements of the Group.

*(b) New standards, amendments and interpretations not yet adopted*

The following new accounting standards and interpretations are mandatory for annual periods after December 31, 2018 and have not been early adopted by the Group:

PFRS 16, Leases (effective for annual periods beginning on or after January 1, 2019)

PFRS 16 will replace the current guidance in *PAS 17, Leases*. PFRS 16 which will become effective on January 1, 2019 will affect primarily the accounting by lessees and will result in the recognition of almost all leases on balance sheet. PFRS 16 removes the current distinction between operating and financing leases and requires recognition of an asset (the right to use the leased item) and a financial liability to pay rentals for virtually all lease contracts. Under PFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. An optional exemption exists for short-term and low-value leases.

The adoption of PFRS 16 will likely affect the accounting of certain assets currently held by the Group under operating lease arrangements.

Philippine Interpretation IFRIC-23, Uncertainty over Income Tax Treatments (effective for annual periods beginning on or after January 1, 2019)

It has been clarified previously that PAS 12, not PAS 37, *Provisions, Contingent Liabilities and Contingent Assets*, applies to accounting for uncertain income tax treatments. IFRIC 23 explains how to recognize and measure deferred and current income tax assets and liabilities where there is uncertainty over a tax treatment.

An uncertain tax treatment is any tax treatment applied by an entity where there is uncertainty over whether that treatment will be accepted by the tax authority. For example, a decision to claim a deduction for a specific expense or not to include a specific item of income in a tax return is an uncertain tax treatment if its acceptability is uncertain under tax law. IFRIC 23 applies to all aspects of income tax accounting where there is an uncertainty regarding the treatment of an item, including taxable profit or loss, the tax bases of assets and liabilities, tax losses and credits and tax rates.

The adoption of the above interpretation will not have a material impact on the consolidated financial statements of the Group.

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Likewise, the following relevant accounting pronouncements effective for annual periods after December 31, 2018 have not been early adopted by the Company:

- Amendments to PAS 28, Long-term Interests in Associates and Joint Ventures (effective on or after January 1, 2019)
- Amendments to PFRS 9, Prepayment Features with Negative Compensation (effective on or after January 1, 2019)

The adoption of the above amendments are not expected to have a material impact on the financial statements of the Group.

### **21.2 Consolidation**

Subsidiaries are all entities over which the Parent Company has the power to govern the financial and operating policies generally accompanying a shareholding of more than one-half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Parent Company controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Parent Company. They are deconsolidated from the date which control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Parent Company. The cost of an acquisition is measured at the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Parent Company's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the Parent Company's share of the net assets of the subsidiary acquired, the difference is recognized directly in profit or loss.

Intercompany transactions, balances and unrealized gains on transactions among the entities within the Group are eliminated. Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Subsidiaries' accounting policies have been changed where necessary to ensure consistency with the policies adopted by the Parent Company. The consolidated financial statements include the accounts of the Parent Company and its wholly-owned subsidiary, BPI Securities Corporation.

BSC was registered with the Securities and Exchange Commission (SEC) on August 26, 1980 and is a registered trading participant of the Philippine Stock Exchange, Inc. (PSE). In July 2000, the Parent Company launched "bpitrade.com", an on-line stock trading facility via internet or through wireless access protocol which enables clients to view live stock market information, do online buying and selling of stocks and access its research reports.

### **21.3 Cash and cash equivalents**

Cash and cash equivalents consist of cash and other cash items and interbank loans receivable and securities purchased under agreements to resell with maturities of less than three months from the date of acquisition and that are subject to insignificant risk of changes in value.

## **21.4 Financial instruments**

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity. The Company recognizes a financial instrument in the statements of condition when, and only when, the Company becomes a party to the contractual provisions of the instrument.

### **21.4.1 Measurement methods**

#### *Amortized cost and effective interest rate*

The amortized cost is the amount at which the financial asset or financial liability is measured at initial recognition minus the principal repayments, plus or minus the cumulative amortization using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any loss allowance.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset (i.e. its amortized cost before any impairment allowance) or to the amortized cost of a financial liability. The calculation does not consider expected credit losses and includes transaction costs, premiums or discounts and fees and points paid or received that are integral to the effective interest rate, such as origination fees.

When the Group revises the estimates of future cash flows, the carrying amount of the respective financial assets or financial liability is adjusted to reflect the new estimate discounted using the original effective interest rate. Any changes are recognised in profit or loss.

#### *Initial recognition and measurement*

Financial assets and financial liabilities are recognised when the entity becomes a party to the contractual provisions of the instrument. Regular way purchases and sales of financial assets are recognised on trade-date, the date on which the Group commits to purchase or sell the asset.

At initial recognition, the Group measures a financial asset or financial liability at its fair value plus or minus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are incremental and directly attributable to the acquisition or issue of the financial asset or financial liability, such as fees and commissions. Transaction costs of financial assets and financial liabilities carried at fair value through profit or loss are expensed in profit or loss.

When the fair value of financial assets and liabilities differs from the transaction price on initial recognition, the entity recognises the difference as follows:

- When the fair value is evidenced by a quoted price in an active market for an identical asset or liability (i.e. a Level 1 input) or based on a valuation technique that uses only data from observable markets, the difference is recognised as a gain or loss.
- In all other cases, the difference is deferred and the timing of recognition of deferred day one profit or loss is determined individually. It is either amortised over the life of the instrument, deferred until the instrument's fair value can be determined using market observable inputs, or realised through settlement.

## 21.4.2 Financial assets

### 21.4.2.1 Classification

#### Policy from January 1, 2018 (PFRS 9)

The Group has applied PFRS 9 and classifies its financial assets in the following measurement categories:

- Amortized cost;
- Fair value through other comprehensive income (FVOCI); or
- Fair value through profit or loss (FVTPL).

The classification requirements for debt and equity instruments are described below:

#### *Debt instruments*

Debt instruments are those instruments that meet the definition of a financial liability from the issuer's perspective, such as loans, government and corporate bonds and trade receivables purchased from clients in factoring arrangements without recourse.

Classification and subsequent measurement of debt instruments depend on the Group's business model for managing the asset and the cash flow characteristics of the asset.

Based on these factors, the Group classifies its debt instruments into one of the following three measurement categories:

- *Amortized cost*  
Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest ('SPPI'), and that are not designated at FVTPL, are measured at amortized cost. The carrying amount of these assets is adjusted by any expected credit loss allowance recognized and measured. Interest income from these financial assets is included in "Interest income" using the effective interest rate method. Amortized cost financial assets include due from BSP, interbank loans receivable and securities purchased under agreements to resell, investment debt securities, trade receivables and other financial receivables.
- *Fair value through other comprehensive income (FVOCI)*  
Financial assets that are held for collection of contractual cash flows and for selling the assets, where the assets' cash flows represent solely payments of principal and interest, and that are not designated at FVTPL, are measured at fair value through other comprehensive income (FVOCI). Movements in the carrying amount are taken through other comprehensive income, except for the recognition of impairment gains or losses, interest revenue and foreign exchange gains and losses on the instrument's amortized cost which are recognized in the statements of comprehensive income. When the financial asset is derecognized, the cumulative gain or loss previously recognized in other comprehensive income is reclassified from equity to profit or loss. Interest income from these financial assets is included in "Interest income" using the effective interest rate method.

- *Fair value through profit or loss (FVTPL)*  
Assets that do not meet the criteria for amortized cost or FVOCI are measured at FVTPL. A gain or loss on a debt investment that is subsequently measured at FVTPL and is not part of a hedging relationship is recognized in profit or loss and presented in the statements of comprehensive income within “Trading gain on securities” in the period in which it arises, unless it arises from debt instruments that were designated at fair value or which are not held for trading, in which case they are presented separately.

*Business model:* The business model reflects how the Group manages the assets in order to generate cash flows. That is, whether the Group’s objective is solely to collect the contractual cash flows from the assets or is to collect both the contractual cash flows and cash flows arising from the sale of assets. If neither of these is applicable, then the financial assets are classified as part of ‘other’ business model and measured at FVTPL. Factors considered by the Group in determining the business model for a group of assets include past experience on how the cash flows for these assets were collected, how the asset’s performance is evaluated and reported to key management personnel, how risks are assessed and managed and how managers are compensated.

*SPPI:* Where the business model is to hold assets to collect contractual cash flows or to collect contractual cash flows and sell, the Group assesses whether the financial instruments’ cash flows represent solely payments of principal and interest (the ‘SPPI test’). In making this assessment, the Bank considers whether the contractual cash flows are consistent with a basic lending arrangement i.e. interest includes only consideration for the time value of money, credit risk, other basic lending risks and a profit margin that is consistent with a basic lending arrangement. Where the contractual terms introduce exposure to risk or volatility that are inconsistent with a basic lending arrangement, the related financial asset is classified and measured at FVTPL.

The Group reclassifies debt investments when and only when its business model for managing those assets changes. The reclassification takes place from the start of the first reporting period following the change. Such changes are expected to be very infrequent and none occurred during the period.

#### *Equity instruments*

Equity instruments are instruments that meet the definition of equity from the issuer’s perspective; that is, instruments that do not contain a contractual obligation to pay and that evidence a residual interest in the issuer’s net assets.

The Group subsequently measures all equity investments at FVTPL, except where the Group’s management has elected, at initial recognition, to irrevocably designate an equity investment at FVOCI. The Group’s policy is to designate equity investments as FVOCI when those investments are held for purposes other than to generate investment returns. When this election is used, fair value gains and losses are recognized in other comprehensive income and are not subsequently reclassified to profit or loss, even on disposal. Impairment losses (and reversal of impairment losses) are not reported separately from other changes in fair value. Dividends, when representing a return on such investments, continue to be recognized in profit or loss as other income when the Group’s right to receive payments is established. Gains and losses on equity investments at FVTPL are included in the “Trading gain on securities” in the statements of comprehensive income.

*Policy prior to January 1, 2018 (PAS 39)*

The Group used to classify its financial assets in the following categories: (i) financial assets at fair value through profit or loss, (ii) loans and receivables, (iii) held-to-maturity securities, and (iv) available-for-sale securities. The classification depended on the purpose for which the assets are acquired. Management determines the classification of its investments at initial recognition.

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

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception.

A financial asset is classified as held for trading if it is acquired or incurred principally for the purpose of selling or repurchasing in the near term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. Financial assets held for trading are shown as “trading securities” in the statement of financial position.

Financial assets designated at fair value through profit or losses at inception are those that are managed and their performance is evaluated on a fair value basis, in accordance with a documented investment strategy.

(b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and with no intention of trading.

Significant accounts falling under this category are cash and other cash items, trade and other receivables, Due from Bangko Sentral ng Pilipinas (BSP) and Interbank loans receivable and SPAR.

(c) Held-to-maturity securities

Held-to-maturity financial assets are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group’s management has the positive intention and ability to hold to maturity.

(d) Available-for-sale securities

Available-for-sale securities are non-derivatives that are either designated in this category or not classified in any of the other categories.

*Subsequent measurement of financial assets (PAS 39)*

AFS and financial assets at fair value through profit or loss are subsequently carried at fair value.

Loans and receivables are subsequently carried at amortized cost using the effective interest method.

Gains and losses arising from changes in the fair value of the financial assets at fair value through profit or loss are included in the statement of income in the year in which they arise.

Gains and losses arising from changes in the fair value of available-for-sale debt securities were recognized directly in the statement of income, until the financial asset is derecognized or impaired at which time the cumulative gain or loss previously recognized in other comprehensive income in equity are recognized in the statement of income. However, interest calculated on these debt securities using the effective interest method and foreign currency gains and losses on monetary assets classified as available-for-sale are recognized in the statement of income. Dividends on AFS equity instruments were recognized in the statement of income when the Company's right to receive payment is established.

Changes in the fair value of monetary securities denominated in a foreign currency and classified as available-for-sale are analyzed between translation differences resulting from changes in amortized cost of the security and other changes in the carrying amount of the security. The translation differences are recognized in the statement of income, and other changes in carrying amount are recognized in equity. Changes in the fair value of non-monetary securities classified as available-for-sale are recognized in other comprehensive income.

#### **21.4.2.2 Impairment of financial assets**

##### *Policy starting January 1, 2018 (PFRS 9)*

The Group applies the PFRS 9 simplified approach to measuring expected credit losses which uses a lifetime expected loss allowance for all trade receivables

##### (a) Trade and other receivables

The Group applies the PFRS 9 simplified approach to measuring expected credit losses which uses a lifetime expected loss allowance for all trade and other financial receivables.

To measure the expected credit losses, trade and other receivables have been grouped based on shared credit risk characteristics and the days past due.

The expected loss rates are based on the payment profiles of customers over a period of 36 month and the corresponding historical credit losses experienced within this period. The historical loss rates are adjusted to reflect current and forward-looking information on macroeconomic factors affecting the ability of the customers to settle the receivables. The Group has identified the domestic GDP and the inflation rate to be the most relevant factors, and accordingly adjusts the historical loss rates based on expected changes in these factors.

##### (b) Debt investments

All of the Group's debt investments at amortized cost and FVOCI are considered to have low credit risk, and the loss allowance recognized is therefore limited to 12-month expected credit losses. Management considers "low credit risk" for listed bonds to be an investment grade credit rating with at least one major rating agency. Other debt instruments are considered to be low credit risk when they have a low risk of default and the issuer has a strong capacity to meet its contractual cash flow obligations in the near term.

#### Policy prior to January 1, 2018 (PAS 39)

Prior to January 1, 2018, the impairment of financial assets was assessed based on incurred loss model. Receivables were assessed collectively to determine whether there was objective evidence that an impairment has been incurred but not yet identified. For these receivables, the estimated impairment losses were recognized in a separate provision for impairment. Objective evidence of impairment that the Group considered included but not limited to the following:

- Significant financial difficulties of the debtor
- Probability that the debtor will enter bankruptcy or financial reorganization; and
- Default or late payments (more than 90 days overdue).

Receivables for which an impairment provision was recognized were written off against the provision when there was no expectation of cash recovery.

#### **21.5.3 Derecognition of financial assets (PFRS 9 and PAS 39)**

Financial assets are derecognized when the contractual right to receive cash flows from the financial assets has ceased to exist or the Company has transferred substantially all risks and rewards of ownership.

#### **21.6 Financial liabilities**

The Group classifies its financial liabilities as: (i) financial liabilities at fair value through profit or loss (including financial liabilities held for trading and those that are designated at fair value); and (ii) other financial liabilities measured at amortized cost.

##### **21.6.1 Classification**

###### **(a) Financial liabilities at fair value through profit or loss**

This category comprises two sub-categories: financial liabilities classified as held for trading, and financial liabilities designated by the Group as at fair value through profit or loss upon initial recognition.

A financial liability is classified as held for trading if it is acquired or incurred principally for the purpose of selling or repurchasing it in the near term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. Derivatives are also categorized as held for trading unless they are designated and effective as hedging instruments. Financial liabilities held for trading also include obligations to deliver financial assets borrowed by a short seller. The Group has no financial liabilities that are held for trading or designated at fair value through profit loss.

###### **(b) Other liabilities measured at amortized cost**

The Group's other financial liabilities at amortized cost comprise mainly of accounts payable and other liabilities (except for payables to the Bureau of Internal Revenue and other government agencies for taxes and remittances and advances from a customer), which are carried at amortized cost using the effective interest rate method. These are included in current liabilities, except for maturities greater than 12 months after the reporting date or when the Group has an unconditional right to defer settlement for at least 12 months after the reporting date which are classified as non-current liabilities.

### **21.6.2 Recognition and measurement**

#### *(a) Recognition*

Financial liabilities are recognized in the statement of financial position when, and only when, the Group becomes a party to the contractual provisions of the instrument.

#### *(b) Measurement*

Financial liabilities carried at fair value through profit or loss are initially recognized at fair value, and transaction costs are expensed in profit or loss. Other financial liabilities carried at amortized cost are initially recognized at fair value plus transaction cost.

Financial liabilities carried at fair value through profit or loss are subsequently carried at fair value. Other financial liabilities at amortized cost are subsequently measured at amortized cost using the effective interest rate method.

Gains or losses arising from changes in the fair value of financial assets and liabilities at fair value through profit or loss, including interest and dividend income and interest expense, are presented in profit or loss within other income (expenses) in the period in which they arise. Dividend income from financial assets at fair value through profit and loss is recognized in profit or loss as part of other income when the Group's right to receive payment is established.

#### *(c) Derecognition*

Financial liabilities are derecognized when it is extinguished, that is, when the obligation specified in a contract is discharged or cancelled, or when the obligation expires. When an existing financial liability is replaced by another financial liability from the same creditor with substantially different terms, or the terms of an existing liability are substantially modified, such modification is treated as a derecognition of the original financial liability and a recognition of a new financial liability, and the difference in the respective carrying amounts is recognized in profit or loss within finance costs.

### **21.7 Offsetting of financial instruments**

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis or realize the asset and settle the liability simultaneously. The legally enforceable right must not be contingent on future events and must be enforceable in the normal course of business and in the event of default, insolvency or bankruptcy of the Group or the counterparty.

There are no offsetting of financial assets and liabilities as at December 31, 2018 and 2017.

### **21.8 Determination of fair value of financial instruments**

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The fair value of a non-financial asset is measured based on its highest and best use. The asset's current use is presumed to be its highest and best use.

The fair value of financial and non-financial liabilities takes into account non-performance risk, which is the risk that the entity will not fulfill an obligation.

The Group classifies its fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

- Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities. This level includes listed equity securities and debt instruments on exchanges (for example, Philippine Stock Exchange, Inc., Philippine Dealing and Exchange Corp., etc.).
- Level 2 - Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices). This level includes the majority of the over-the-counter (“OTC”) derivative contracts. The primary source of input parameters like LIBOR yield curve or counterparty credit risk is Bloomberg.
- Level 3 - Inputs for the asset or liability that are not based on observable market data (unobservable inputs). This level includes equity investments and debt instruments with significant unobservable components. This hierarchy requires the use of observable market data when available.

The appropriate level is determined on the basis of the lowest level input that is significant to the fair value measurement.

The fair value of financial instruments traded in active markets is based on quoted market prices at the reporting date. 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. The quoted market price used for financial assets held by the Group is the most representative price within the bid-ask spread. These instruments are included in Level 1.

The fair value of assets and liabilities that are not traded in an active market (for example, over-the-counter derivatives) is determined by using valuation techniques. These valuation techniques maximize the use of observable market data where it is available and rely as little as possible on entity specific estimates. If all significant inputs required to fair value an instrument are observable, the asset or liability is included in Level 2. If one or more of the significant inputs is not based on observable market data, the asset or liability is included in Level 3.

Specific valuation techniques used to value financial instruments include:

- Quoted market prices or dealer quotes for similar instruments.
- The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows based on observable yield curves.
- The fair value of forward foreign exchange contracts is determined using forward exchange rates at the reporting date, with the resulting value discounted back to present value.
- Other techniques, such as discounted cash flow analysis, are used to determine fair value for the remaining financial instruments.

## **21.9 Investments in subsidiary and associates**

### *(a) Subsidiary*

As disclosed in Note 6, the Parent Company has a subsidiary.

Subsidiaries are all entities over which the Parent Company has control. The Parent Company controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The Parent Company also assesses existence of control where it does not have more than 50% of the voting power but is able to govern the financial and operating policies by virtue of de-facto control. De-facto control may arise in circumstances where the size of the Parent Company's voting rights relative to the size and dispersion of holdings of other shareholders give the Parent Company the power to govern the financial and operating policies.

Subsidiaries are fully consolidated from the date on which control is transferred to the Parent Company. They are deconsolidated from the date that control ceases.

The Company applies the acquisition method of accounting to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred to the former owners of the acquiree and the equity interests issued by the Company. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition-related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. On an acquisition-by-acquisition basis, the Company recognizes any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's identifiable net assets.

Acquisition-related costs are expensed as incurred.

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

Any contingent consideration to be transferred by the Parent Company 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 39 either in profit or loss or as a change to other comprehensive income. Contingent consideration that is classified as equity is not re-measured, and its subsequent settlement is not accounted for within equity.

The excess of the aggregate of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the Parent Company's share of the identifiable net assets acquired is recorded as goodwill. If the total of consideration transferred, non-controlling interest recognized and previously held interest measured is less than the fair value of the net assets of the subsidiary acquired in the case of a bargain purchase, the difference is recognized directly in profit or loss.

When the Parent Company ceases to have control, any retained interest in the entity is re-measured to its fair value at the date when control is lost, with the change in carrying amount recognized in profit or loss. The fair value is the initial carrying amount for purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognized in other comprehensive income in respect of that entity are accounted for as if the Company had directly disposed of the related assets or liabilities. This may mean that amounts previously recognized in other comprehensive income are reclassified to profit or loss.

As allowed under PFRS 10, *Consolidated Financial Statements*, investment in a wholly-owned subsidiary is accounted for at cost method in the separate financial statements of the Company. Under this method, income from investment is recognized in the statement of income only to the extent that the investor receives distributions from accumulated net income of the investee arising subsequent to the date of acquisition.

*(b) Associate*

Associates are entities over which the Parent Company has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights.

The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition.

Following the provisions of PAS 28, *Investments in Associates*, equity investment in associate is accounted for at cost in the preparation of separate financial statements. Under this method, income from investment is recognized in the statement of income only to the extent that the investor receives distributions from accumulated net income of the investee arising subsequent to the date of acquisition.

**21.10 Other assets**

Other assets are recognized in the event that payment has been made in advance of obtaining right of access to goods or receipt of services and measured at nominal amounts. These are derecognized upon delivery of goods or when services have been rendered, through amortization over a certain period of time, and use or consumption.

Creditable withholding tax is recognized as asset to the extent that it is probable that the benefit will flow to the Group. This are derecognized when applied against the related tax liability or refunded by the tax authorities as prescribed by the relevant tax laws.

Other assets are included in current assets, except when the related goods or services are expected to be received or rendered more than twelve (12) months after the reporting date, which are then classified as non-current assets.

**21.11 Property and equipment**

Property and equipment are stated at historical cost less accumulated depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or are recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the statement of income during the year in which they are incurred.

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Depreciation is calculated using the straight-line method to allocate cost or residual values over the estimated useful lives of the assets as follows:

|                                   |           |
|-----------------------------------|-----------|
| Furniture, fixtures and equipment | 3-5 years |
| Computer equipment                | 3 years   |

Major renovations are depreciated over the remaining useful life of the related asset.

The asset's residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date.

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. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use.

The Group derecognizes the carrying amount of an item of property and equipment on disposal or when no future economic benefits are expected from its use or disposal.

Gains and losses on disposals are determined by comparing proceeds with carrying amount and are included in the statement of income.

#### **21.12 Software costs**

Acquired software licenses are capitalized on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortized over their estimated useful life of three (3) years.

Cost associated with maintaining computer software programs are recognized as an expense when incurred.

The carrying amount of software costs is derecognized on disposal or when no future economic benefits are expected from its use or disposal. The gain or loss arising from derecognition is recognized in profit or loss.

#### **21.13 Accounts payable and other liabilities**

Accounts payable and other liabilities are obligations to pay for goods or services that have been acquired in the ordinary course of business. These are recognized in the period in which the related money, goods or services are received or when a legally enforceable claim against the Group is established or when the corresponding assets and expenses are recognized. Accounts payable and other liabilities are classified as current liabilities if payment is due within one year or less. If not, these are presented as non-current liabilities. These are measured at the original invoice amount (as the effect of discounting is immaterial) and subsequently measured at amortized cost using the effective interest rate method.

Accounts payable and other liabilities are derecognized when it is extinguished, that is, when the obligation specified in a contract is discharged or cancelled, or when the obligation expires.

#### **21.14 Provisions**

Provisions are recognized when the Group has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated. Provisions are not recognized for future operating losses.

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. A provision is recognized even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognized in profit or loss.

Provisions are reviewed at the end of each reporting period and adjusted to reflect the current best estimate. If it is no longer probable that an outflow of resources embodying economic benefits will be required to settle the obligation, the provision is reversed and derecognized in the statement of financial position.

#### **21.15 Income taxes**

The provision for income tax for the period comprises current and deferred income tax. Income tax is recognized in profit or loss, except to the extent that 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.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the reporting date where the Group operates and generates taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is recognized on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statement. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted at reporting date and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

Deferred income tax assets are recognized for all deductible temporary differences, carry-forward of unused tax losses (net operating loss carryover or NOLCO) and unused tax credits (excess minimum corporate income tax or MCIT) to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized. Deferred income tax assets arising from NOLCO and excess MCIT are recognized to the extent that it is probable that the Group will have future taxable profit before any unused tax losses or unused tax credits expire as prescribed by the relevant tax provisions.

Deferred tax liabilities are the amounts of income taxes payable in future periods in respect of taxable temporary differences. Deferred income tax liabilities are recognized in full for all taxable temporary differences.

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Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income tax assets and liabilities relate to income taxes levied by the same taxation authority on the taxable entity and where there is an intention to settle the balances on a net basis.

The Group has substantial income from its investment in government securities subject to final withholding tax. Such income is presented at its gross amount and the tax paid or withheld is included in Current provision for income tax.

The Group re-assesses at each reporting date the need to derecognize a previously recognized deferred income tax asset.

## **21.16 Income and expense recognition**

### **(a) Revenue from fees and commission**

Starting January 1, 2018, the Group has applied PFRS 15 where revenue is recognized when (or as) the Group satisfies a performance obligation by transferring a promised good or service to a customer (i.e. an asset). An asset is transferred when (or as) the customer obtains control of that asset.

The recognition of revenue can be either over time or at a point in time depending on when the performance obligation is satisfied.

When control of a good or service is transferred over time, that is, when the customer simultaneously receives and consumes the benefits, the Group satisfies the performance obligation and recognizes revenue over time. Otherwise, revenue is recognized at the point in time at the point of transfer control of the good or service to the customer.

Variable consideration is measured using either the expected value method or the most likely amount method depending on which method the Group expects to better predict the amount of consideration to which it will be entitled. This is the estimated amount of variable consideration, or the portion, if any, of that amount for which it is highly probable that a significant reversal in the amount of cumulative revenue recognized will not occur. Where there is a single performance obligation, the transaction price is allocated in its entirety to that performance obligation. Where there are multiple performance obligations, the transaction price is allocated to the performance obligation to which it relates based on stand-alone selling prices.

The Group recognizes revenue based on the price specified in the contract, net of the estimated rebates/discounts and include variable consideration, if there is any. Accumulated experience is used to estimate and provide for the discounts and revenue is only recognized to the extent that it is highly probable that a significant reversal will not occur.

The Group does not expect to have any contracts where the period between the transfer of the promised goods or services to the customer and payment by the customer exceeds one year. As a consequence, the Group does not adjust any of the transaction prices for the time value of money.

There are no warranties and other similar obligation and refunds agreed with customers.

Until December 31, 2017, the Group recognizes revenue under PAS 8.

Fees and commission income from underwriting, loan syndication, brokering services, and financial advisory activities are recognized in the period the related services are rendered and completed and the right to receive payment is established.

(b) Interest income

Interest income is recognized in the statement of income for all interest-bearing financial instruments using the effective interest method.

When calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees 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 impairment loss.

(c) Other income

Other income is recognized when earned and the Group's right to receive payment is established..

(d) Cost and expenses

Costs and expenses are recognized in profit or loss when a decrease in future economic benefit related to a decrease in an asset, or an increase in a liability has arisen, that can be measured reliably.

Brokerage fees and underwriting fees pertain to payments made by the Group to broker-dealers for brokering and underwriting services rendered related to certain underwritten deals.

## **21.17 Employee benefits**

(a) Pension benefits

The Group has both defined benefit and defined contribution plans. A defined benefit plan is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and compensation. A defined contribution plan is a pension plan under which the Group pays fixed contributions into a separate fund. Under a defined contribution plan, the Group has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods.

*Defined benefit plan*

The Group's defined benefit plan is funded through payments to a trustee-administered fund as determined by periodic actuarial calculations.

The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of government bonds that are denominated in Philippine Peso, and that have terms to maturity approximating the terms of the related retirement benefit obligation.

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The liability recognized in the statement of financial position in respect of defined benefit plans is the present value of the defined benefit obligation at the end of the reporting period less the fair value of plan assets. In cases when the amount determined results in a surplus (being an excess of the fair value of the plan assets over the present value of the defined benefit obligation), the Group measures the resulting asset at the lower of the surplus in the defined benefit plan and the present value of future benefits in the form of refunds or reductions in future contributions to the plan.

Restricted or non-transferrable assets of the fund are excluded in the determination of the fair value of plan assets.

Remeasurement gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited directly to other comprehensive income under remeasurement loss or gain in the period in which they arise.

All past service costs are recognized immediately in profit or loss.

The net interest cost is calculated by applying the discount rate to the net balance of the defined benefit obligation and the fair value of plan assets. This cost is included as part of retirement benefit expense recognized in profit or loss.

When the benefits of a plan are changed or when a plan is curtailed, the resulting change in benefit that relates to past service or the gain or loss on curtailment is recognized immediately in profit or loss. The Group recognizes gains or losses on the settlement of a defined benefit plan when the settlement occurs.

#### *Defined contribution plan*

The Group also maintains a defined contribution plan that covers certain full-time employees. Under its defined contribution plan, the Group pays fixed contributions based on the employees' monthly salaries to a privately trustee-administered fund. Contribution is determined by periodic actuarial calculations and compensation. The Group, however, is covered under RA No. 7641, otherwise known as The Philippine Retirement Law, which provides for its qualified employees a defined benefit minimum guarantee. The defined benefit minimum guarantee is equivalent to a certain percentage of the monthly salary payable to an employee at normal retirement age with the required credited years of service based on the provisions of RA No. 7641. Accordingly, the Group accounts for its retirement obligation under the higher of the defined benefit obligation relating to the minimum guarantee and the obligation arising from the defined contribution plan.

For the defined benefit minimum guarantee plan, the liability is determined based on the present value of the excess of the projected defined benefit obligation over the projected defined contribution obligation at the end of the reporting period. The defined benefit obligation is calculated annually by a qualified independent actuary using the projected unit credit method.

The liability recognized in the statement of financial position in respect of defined benefit pension plans is the present value of the defined benefit obligation at the reporting date less the fair value of plan assets. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of government bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating the terms of the related pension liability. The fair value of plan asset is the defined contribution assets upon which the defined contribution benefits depend, with an adjustment for margin on asset returns, if any, where this is reflected in the defined contribution benefits.

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The Group has no further payment obligations once the contributions have been paid. The contributions are recognized as employee benefit expense when these are due. Prepaid contributions are recognized as an asset to the extent that a cash refund or a reduction in the future payments is available.

Remeasurement gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity in other comprehensive income in the period in which they arise.

Past-service costs are recognized immediately in profit or loss.

(b) Profit-sharing and bonus plans

The Group recognizes a liability and an expense for bonuses and profit-sharing, based on a formula that takes into consideration the profit attributable to the Group's shareholders after certain adjustments. The Group recognizes a provision where contractually obliged or where there is a past practice that has created a constructive obligation.

(c) Share-based compensation

The Group's management awards high-performing employees bonuses in the form of options to purchase Parent Bank's common shares, from time to time, on a discretionary basis. The options are subject to certain service vesting conditions.

The fair value of the services received is measured by reference to the fair value of the shares or share options granted on the date of the grant. The grant by BPI of the options over its equity instruments to the employees of the Group is recorded in equity. The fair value of employee services received by the Group in respect of the options granted is recognized in profit or loss over the period that the services are received, which is the vesting period. The Group is recharged by BPI for the share-based payment when the award vests. The subsidiary recognizes the recharge over the vesting period as a charge to equity.

The fair value of the options granted is determined using option pricing models which take into account the exercise price of the option, the current share price, the risk-free interest rate, the expected volatility of the share price over the life of the option and other relevant factors.

When the stock options are exercised, the proceeds received, net of any directly attributable transaction costs, are credited to share capital (par value) and share premium for the excess of exercise price over par value.

(d) Termination benefits

Termination benefits are payable when employment is terminated by the Group before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Group recognizes termination benefits at the earlier of the following dates: (a) when the Group can no longer withdraw the offer of those benefits; and (b) when the entity 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.

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### **21.18 Share capital; retained earnings**

Common shares are classified as equity and are measured at par value for all shares issued. The amount of proceeds from the issuance or sale of shares representing the aggregate par or stated value is credited to share capital. Proceeds in excess of the aggregate par or stated value of shares, if any, are credited to share premium. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction from the proceeds, net of tax.

After initial recognition, share capital and share premium are carried at historical cost and are classified as equity in the statement of financial position.

Retained earnings represent the accumulated profit or loss as a result of the operations of the Group less any dividends declared.

### **21.19 Dividends on common shares**

Dividends on common shares are recognized in the period in which they are approved by the Board of Directors.

### **21.20 Leases (the Group is the lessee)**

Leases in which substantially all risks and rewards of ownership are retained by another party, the lessor, are classified as operating leases. Payments, including prepayments, made under operating leases (net of any incentives received from the lessor) are charged to the statement of income on a straight-line basis over the period of the lease.

### **21.21 Related party relationships and transactions**

Related party relationships exist when one party has the ability to control, directly, or indirectly through one or more intermediaries, the other party or exercises significant influence over the other party in making financial and operating decisions. Such relationships also exist between and/or among entities which are under common control with the reporting enterprise, or between, and/or among the reporting enterprise and its key management personnel, directors, or its shareholder. In considering each possible related party relationship, attention is directed to the substance of the relationship and not merely the legal form.

### **21.22 Foreign currency transactions and translation**

#### *Functional and presentation currency*

Items included in the financial statements of the Group are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The financial statements are presented in Philippine Peso, which is the Group's functional and presentation currency.

#### *Transactions and balances*

Foreign currency transactions are translated into Philippine Peso using the exchange rates prevailing at the dates of the transaction. Foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at the year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in profit or loss.

### **21.23 Subsequent events**

Post year-end events that provide additional information about the Group's position at the end of the reporting period (adjusting events) are reflected in the financial statements. Post year-end events that are not adjusting events are disclosed in the notes to the consolidated financial statements when material.