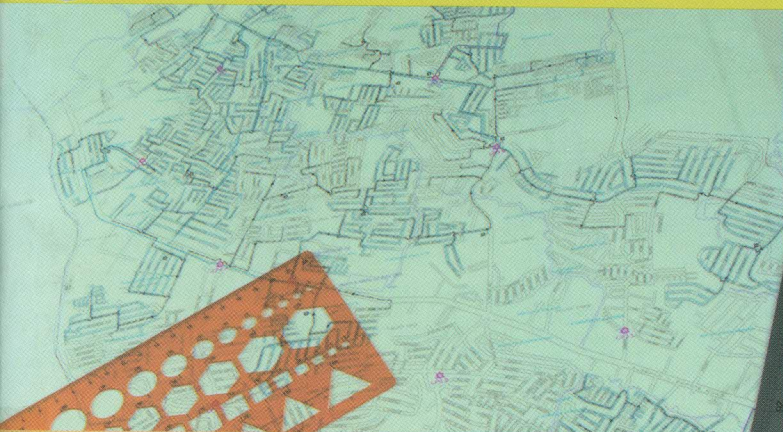


Investing In The Future

Annual Report

2004



SOLID GROUP INC.

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SOLID GROUP ANNUAL REPORT 2004

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DEAR FELLOW SHAREHOLDERS

SGL is transforming itself to meet that challenge of rapidly changing economic conditions and an uncertain business climate in the Philippines, particularly in the Broadband and Information Services sector. Our management discipline and fiscal prudence has steadied our course and preserved our resources in these difficult times. But now we are focused on growth and are ready to exploit the emerging opportunities the changing economy is bringing. And we are pursuing this with the full commitment to grow businesses that will create increasing value for our stockholders.

We are embracing new technologies in products and software that will enhance the data, communication and entertainment experience of our customers. We are combining our strength in the local market with the expertise of foreign technology partners to accomplish this efficiently and quickly. We have developed a number of cooperative business arrangements to enable quick and efficient entry into vertical markets such as high rise buildings with cutting edge internet technology. Furthermore, we are currently studying similar business models on a larger scale in the field of outsourced information management software.

We are making affordable high-speed Internet available to more Filipinos. Working with world-class equipment and systems, we have implemented a network development program that will further enhance our Internet service capabilities. Our focus on cable broadband network expansion and service improvement will also benefit our cable television service delivery systems as well with clearer signals and more entertainment channels. There is no shortcut in building and maintaining a robust metro wide data network and we are committed to it for the long term.

SGL's growth goals will be achieved in these critical business opportunity areas:

1. Growth in Cable Television Business Segment

Our major client, Global Destiny, has expanded its program channel offerings that appeal to specialized and focused markets. Growth has been fueled by the development of such niche market areas and it aims to reach even more cable viewers that want a choice in their cable television provider. This growth will increase revenues from network carriage fees paid by Global Destiny as well as expand the potential market of High Speed Internet services to cable television customers.

2. Enhanced Data Network Services & Competitive Cost Structures

Our primary competitive edge in broadband services is that our metro manila wide Hybrid Fiber Coaxial (HFC) network is capable of simultaneous transmission of video, data and voice. It is the single biggest contiguous network of its kind covering Metro Manila. We continue to work hard to maintain the robustness, scalability and high bandwidth capacity of the network.

We have finished most of the massive capital investments required to roll out our network so we can now focus more of our attention to streamlining and standardizing processes to further lower costs while maintaining the best recreational service level for its price in the market. Our goal is to combine both values to meet the needs of more Internet users. In line with this, we have launched our Fiber-to-Building Project in selected areas of Makati and Ortigas Business Districts to further enhance our customers' experience of our service and support the introduction of higher value Internet Protocol services including VOIP.



3. Rationalization of Sony Brand Business

We are in the process of negotiating with Sony Japan Inc. the terms and conditions that will govern the conclusion of our eight year joint venture participation in Sony Philippines Inc. The objective of this negotiation process is to ensure the proper valuation and future potential revenue for SGI as we conclude more than 30 years of investment, manufacturing and marketing that made Sony a major brand in the country. Let me emphasize that we are pursuing this negotiation first and foremost in behalf of you, our stockholders, and protecting the value of our company's investment. We will report to you as soon as the results of our negotiations are finalized.

4. Maximizing Selected Real Estate Asset Values

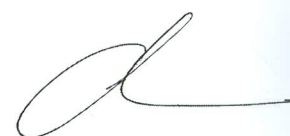
SGI asset portfolio includes high value urban real estate holdings whose value can be unlocked by development into high-rise properties for both residential and commercial use. The first development is the tri-tower project known as the Zen Towers ideally located in front of SM Manila along Concepcion Street, Manila. The strong differentiation value of this and our future developments will be its Intelligent Building status with a complete array of Broadband cable entertainment, Internet, data and IP communication services. While we are confident of the market potential and revenue for this project, it must be emphasized that the rational for SGI's real estate development activities is conservative and prudently focused on value enhancement of existing properties rather than speculative large-scale developments. We are confident that this project will serve as the model for similar developments in SGI's other high-value Manila properties.

We have taken stock of SGI's resources and talents and we are confident that our growth opportunities far outweigh possible threats and challenges. Our Metro wide cable infrastructure provides the platform to deliver entertainment, data, voice and network backbone for a wide array of wireless services. In particular, the National Telecommunications Commission's (NTC) recent issuance of the Memorandum for VOIP draft rules has created the industry opportunity for our broadband company to immediately become a major VOIP provider in its network coverage area in Metro Manila.

Our partnerships are developing everyday to bring in cutting edge technology and specialized information systems. Our Overnet and Samsung technology partners are providing digital line equipment that enable a quick and efficient service rollout to high value accounts in vertical markets such as high rise buildings. This technology will accelerate the utilization of our fiber capacity in the building dense business districts.

Our move to develop an investment direction in information technology-based businesses was refined over several years of international industry research and investigation. We have had preliminary discussions with information technology and application providers to acquire and service large government and corporate accounts. These businesses will be built in synergy with our broadband and satellite services to further enhance its competitive value to the customers. Our direction is clear and we hope to announce more details later this year.

We are maximizing value for our existing resources and investing to unlock greater values in our infrastructure and real estate holdings. Your SGI management team will be providing leadership and innovation to bring about such exciting changes and growing value in the days to come. Together we will work to make tomorrow better for all of us.



David S. Lim
Director, President and
Chief Executive Officer

REVIEW OF OPERATIONS

Management Discussion

I. Broadband Services

The broadband cable priority of 2004 was an extensive network plant maintenance and expansion program aimed at raising customer data speed, maintaining service consistency and instituting proactive maintenance activities. As part of our technology partnership with Samsung, we retained the services of their network-consulting group, which laid the groundwork for this program. To support these efforts, we also installed newly developed monitoring software that will enable our Hub & Node Maintenance teams to identify trends that signal possible service degradation even before it becomes apparent to the customer.

Significant expansion activities were accomplished in the commercial business districts of Salcedo and Legaspi Villages in Makati City and the Ortigas business district. We are the only broadband cable company participating in the telecommunications company consortium laying underground fiber cables to the buildings throughout those areas. Our services in our fiber to the building test sites are also being received very well and we look forward to a quick market acceptance.

Our broadband business has begun a steady but controlled trend with a 16% increase in revenues to 191 million pesos for our broadband and Internet services. Our efficiency and streamlining activities contributed greatly to reducing our operating expense to total revenue ratio from 29% (prior to reorganization in 2003) to 25% the following year. As a result, we have reduced our EBITDA loss by more than 47% from previous year to only 35,917,031 pesos. We are looking forward to a positive EBITDA report by the following year.

II. Real Estate

Our Real Estate business group revenue registered growth primarily due to strong sales revenues by Starworld Corporation, which enjoyed a surge in sales of industrial estate properties, which contributed 225,548,883 pesos. Solid Manila Corporation (SMC) and other subsidiaries reported revenues of 112 million pesos.

Preliminary site development has begun in the Concepcion street property right across the SM Mall in Manila for the tri-tower development called the Zen Towers. Pre-selling is expected to begin by the second semester or of 2005. Other prime commercial Manila properties in Ermita and T.M. Kalaw are also being studied for future developments.

III. Manufacturing Services and Support Services

The Plastic Injection operations (SLC –Plastics Division & Clark Plastics) contributed 312,115,797 pesos which provided 52% of this segment's total revenue of 600,554,873 pesos.

Omni Logistics Corporation (OLC) posted a slight reduction in business volume (-5%) with revenue of 91,981,836 pesos as it continued to service the warehousing and logistics requirements of brands such as TCL and Sony.

After sales service operations of Solid Electronics Corporation (SEC) and its subsidiaries grew slightly at 3% with a revenue of 196,457,240 pesos as more higher value items such as digital video cameras and digital still cameras are introduced into the market. SEC is the only after-sales service provider authorized by Sony Japan.

There was a general decline in manufacturing revenue as foreign consumer electronics brand generally opted for importation of CBU (completely built up units) as lower government tariffs removed the advantage of local assembly operations. As a result, revenues of the manufacturing and support services reached 554 million pesos, which is a 39% reduction versus 2003.

IV. Trading and Distribution

Solid Video Corporation (SVC) posted a slowdown in sales of broadcast and professional equipment from the previous year reporting 99,383,177 pesos in revenue. The lack of growth was due to a number of broadcast and production companies that delayed upgrade and expansion plans for implementation the following year.

AA Plastics, the former AA Commercial Inc., contributed 149 million pesos in revenues.

V. Investments

Revenues from financing and investment activities grew by 11% for a total of 193.6 million pesos. The improvement in earnings was mainly attributed to higher interest rate yield for bond investments with an average interest rate of 8% per annum.



BOARD OF DIRECTORS



Elena S. Lim
Chairman
Emeritus

Gabriel V. Manalac
Director

Vincent S. Lim
Director
Senior Vice President
and Chief Financial Officer

David S. Lim
Director
President
and Chief Executive Officer

Joseph Lim
Director

Susan L. Tan
Director
Chairman of
the Board

Quintin Chua
Director

Jason S. Lim
Director
Senior Vice President
and Chief Operating Officer

CORPORATE OFFICERS

James H. Uy
Senior Vice President and
Chief Operating Officer,
Destiny Inc.

Lita L. Joaquin
Treasurer

Irineo D. Tubio, Jr.
Senior Vice-President and
Chief Accounting Officer

Enrique L. Ligerálde
Senior Vice President for
Administration and Control

(Not in picture)
Roberto V. San Jose
Corporate Secretary



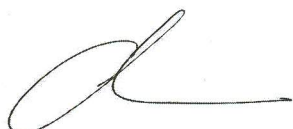
STATEMENT OF MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS

The management of Solid Group, Inc. is responsible for all information and representation contained in the financial statements for years ended December 31, 2004, 2003 and 2002. The financial statements have been prepared in conformity with generally accepted accounting principles in the Philippines and reflect amounts that are based on the best estimates and informed judgment of management with an appropriate consideration of materiality.

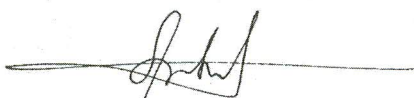
In this regard, management maintains a system of accounting and reporting which provides for the necessary internal controls to ensure that transactions are properly authorized and recorded, assets are safeguarded against unauthorized use or disposition and liabilities are recognized. The management likewise discloses to the Company's audit committee and to its external auditor: (i) all significant deficiencies in the design or operation of internal controls that could adversely affect its liability to record, process, and report financial data; (ii) material weaknesses in the internal controls; and (iii) any fraud that involves management or other employees who exercise significant roles in internal controls.

The Board of Directors reviews the financial statements before such statements are approved and submitted to the stockholders of the Company.

Punongbayan & Araullo, the independent auditors appointed by the stockholders, has examined the financial statements of the Company in accordance with the generally accepted auditing standards in the Philippines and has expressed its opinion on the fairness of the presentation upon completion of such examination, in its report to the Board of Directors and stockholders.



David S. Lim
President and Chief Executive Officer



Susan L. Tan
Chairman of the Board



Vincent S. Lim
Chief Financial Officer

SOLID GROUP INC. AND SUBSIDIARIES

REPORT OF INDEPENDENT AUDITORS

The Board of Directors

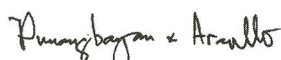
Solid Group Inc. and Subsidiaries
2285 Don Chino Roces Avenue Extension
Makati City

Punongbayan & Araullo 

We have audited the accompanying consolidated balance sheet of Solid Group Inc. and subsidiaries as of December 31, 2004, and the related consolidated statements of income, changes in equity and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit. The consolidated financial statements of Solid Group Inc. and subsidiaries for the years ended December 31, 2003 and 2002 were audited by other auditors whose reports, dated May 5, 2004, and March 21, 2003, respectively, expressed an unqualified opinion on those statements.

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

In our opinion, the 2004 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Solid Group Inc. and subsidiaries as of December 31, 2004, and the results of their operations and their cash flows for the year then ended in accordance with generally accepted accounting principles in the Philippines.



April 13, 2005

CONSOLIDATED BALANCE SHEET

For the year ended December 31, 2004 (With Comparative Figures for 2003 and 2002)

	2004	2003
ASSETS		
Current Assets		
Cash and cash equivalents (Note 5)	P 1,619,213,573	P 1,548,376,544
Short-term investments (Note 6 and 14)	704,264,491	618,129,555
Trade and other Receivables - net (Notes 7, 12, 13, 21, 25 and 27)	355,840,857	564,743,383
Inventories - net (Notes 8 and 21)	120,438,048	47,622,629
Land and development costs (Note 9)	318,462,630	488,642,619
Other current assets - net (Note 10)	82,616,060	91,882,119
Total Current Assets	3,200,835,659	3,359,396,849
Non-Current Assets		
Investments and advances (Notes 1, 11 and 21)	78,384,763	226,063,238
Property, plant and equipment - net (Notes 1, 7, 12 and 27)	3,459,426,664	3,437,215,396
Deferred tax assets (Notes 3 and 20)	4,399,438	4,264,851
Other non-current assets (Notes 1, 7, 13 and 21)	571,073,028	474,348,448
Total Non-current Assets	4,113,283,893	4,141,891,933
TOTAL ASSETS	P 7,314,119,552	P 7,501,288,782
LIABILITIES AND EQUITY		
Current Liabilities		
Interest-bearing loans (Notes 6 and 14)	P 262,412,605	P 291,634,490
Trade and other payable (Notes 1, 15, 19, 25 and 26)	407,611,206	401,663,438
Estimated liability for land and development costs	19,816,448	28,185,593
Income tax payable	7,357,197	9,194,795
Total Current Liabilities	697,197,456	730,678,316
Non-Current Liabilities		
Advances from related parties (Note 21)	96,697,485	95,461,929
Deferred tax liabilities (Notes 3 and 20)	15,036,414	9,922,769
Minority Interest	263,433,124	264,045,089
Total Non-Current Liabilities	375,167,023	369,429,787
TOTAL LIABILITIES	1,072,364,479	1,100,108,103
EQUITY		
Capital stock (Notes 1 and 16)	2,030,975,000	2,255,436,752
Additional paid-in-capital (Notes 1 and 16)	4,641,701,922	4,664,902,932
Treasury shares (Note 16)	(115,614,380)	(115,614,380)
Deficit (Notes 1, 3 and 16)	(315,307,469)	(403,544,625)
Total Equity	6,241,755,073	6,401,180,679
TOTAL LIABILITIES AND EQUITY	P 7,314,119,552	P 7,501,288,782

See Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF INCOME

For the year ended December 31, 2004 (With Comparative Figures for 2003 and 2002)

	2004	2003	2002
REVENUES			
Sales of goods (Note 21)	P 721,750,822	P 839,010,456	P 1,300,618,121
Rendering of Services (Notes 21 and 25)	441,830,145	444,095,809	491,742,888
Interest (Note 21)	182,523,364	156,332,055	83,816,550
Rent (Notes 3 and 27)	110,354,171	108,066,361	93,702,143
Foreign currency gains-net	9,112,222	28,173,499	16,235,044
Others (Notes 1 and 13)	132,865,799	71,684,588	42,423,837
	<u>1,598,436,523</u>	<u>1,647,362,768</u>	<u>2,028,538,583</u>
COSTS AND EXPENSES			
Cost of goods sold (Notes 12, 17, 19 and 21)	595,218,802	774,137,671	1,217,886,288
Cost of services (Notes 3, 12, 17 and 19)	524,813,016	508,987,699	460,742,485
Operating expenses (Notes 1, 13, 18, 19 and 27)	292,583,880	297,505,236	461,871,047
Impairment loss (Notes 12 and 13)	22,481,001	350,000,000	35,000,000
	<u>1,435,096,699</u>	<u>1,930,630,606</u>	<u>2,175,499,820</u>
INCOME (LOSS) FROM OPERATIONS	163,339,824	(283,267,838)	(146,961,237)
OTHER CHARGES	8,833,348	4,391,785	728,842
Finance costs (Note 14)			
INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE TAXES AND MINORITY INTEREST	154,506,476	(287,659,623)	(147,690,079)
TAX EXPENSE (Notes 3, 20, 23 and 24)	46,156,718	32,502,475	61,185,867
INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE MINORITY INTEREST	108,349,758	(320,162,098)	(208,875,946)
MINORITY INTEREST	(15,092,528)	3,345,367	4,463,839
INCOME (LOSS) FROM CONTINUING OPERATION	93,257,230	(316,816,731)	(204,412,107)
INCOME (LOSS) FROM DISCONTINUING OPERATIONS Net of income taxes of			
P295,167 in 2003 (Notes 1 and 13)	(5,020,074)	18,272,968	(42,990,045)
NET INCOME (LOSS)	P 88,237,156	(P 298,543,763)	(247,402,152)
Basic Earnings (Loss) per Share (Note 22)			
Continuing operations	P 0.04	(P 0.15)	(P 0.11)
Discontinuing operation	(0.00)	0.01	(0.02)
	<u>P 0.04</u>	<u>(P 0.14)</u>	<u>(P 0.13)</u>

See Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended December 31, 2004 (With Comparative Figures for 2003 and 2002)

	2004	2003	2002
CAPITAL STOCK			
Balance at beginning of year	P 2,255,436,752	P 2,030,975,000	P 2,030,975,000
Uniting of interest adjustment (Notes I and I6)	—	—	100,000,000
Issuances for the acquisition of			
Destiny, Inc. (Notes I and I6)	—	224,461,752	—
Effects of re-valuation of net assets of			
Destiny, Inc. (Notes I and I6)	(224,461,752)	—	—
Balance at end of year	2,030,975,000	2,255,436,752	2,130,975,000
ADDITIONAL PAID-IN CAPITAL			
Balance at beginning of year	4,664,902,932	4,589,076,596	4,589,076,596
Uniting of interest adjustment (Notes I and I6)	—	75,826,336	932,064,077
Effects of re-valuation of net assets			
of Destiny, Inc. (Notes I and I6)	(23,201,010)	—	—
Balance at end of year	4,641,701,922	4,664,902,932	5,521,140,673
TREASURY SHARES			
Balance at beginning of year	(115,614,380)	(115,614,380)	(114,830,162)
Treasury shares acquired during the year	—	—	(784,218)
Balance at end of year	(115,614,380)	(115,614,380)	(115,614,380)
RETAINED EARNINGS (DEFICIT)			
Balance at beginning of year			
As previously stated	(403,544,625)	(42,616,817)	123,423,235
Effect of change in accounting for pre-operating			
expenses - net of tax (Note 3)	—	(19,949,150)	(16,290,038)
Uniting of interest adjustment (Notes I and I6)	—	(42,434,895)	35,268,093
As restated	(403,544,625)	(105,000,862)	142,401,290
Net income (loss)	88,237,156	(298,543,763)	(247,402,152)
Balance at end of year	(315,307,469)	(403,544,625)	(105,000,862)
TOTAL EQUITY	P 6,241,755,073	P 6,401,180,679	P 7,431,500,431

See Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended December 31, 2004 (With Comparative Figures for 2003 and 2002)

	2004	2003	2002
CASH FLOWS FROM OPERATING ACTIVITIES			
Income (loss) from continuing operations before income tax and minority interest	P 154,506,476	(P 287,659,623)	(P 147,690,079)
Adjustment for:			
Depreciation and amortization	151,410,835	160,458,692	299,870,755
Impairment loss	22,481,001	350,000,000	35,000,000
Interest expense	8,833,348	4,391,785	728,842
Provision for warranty expense	3,536,176	793,002	668,198
Gain on sale of other current assets	(2,373,546)	—	—
Unrealized foreign currency gains - net	(4,372,750)	(11,534,577)	(19,666,868)
Loss (gain) on sale of investments	(5,235,432)	1,399,218	—
Gain on sale of property and equipment	(8,647,523)	(5,572,863)	(1,155,223)
Reversal of allowances for various assets	(15,876,909)	—	—
Reversal of impairment losses on property, plant and equipment	(16,807,098)	—	—
Interest income	(182,523,364)	(156,332,055)	(83,694,759)
Operating income before working capital changes	104,931,214	55,943,579	84,060,866
Decrease in trade and other receivables	279,765,143	87,081,585	50,787,816
Decrease (increase) in inventories	(2,665,815)	29,121,980	309,708,605
Decrease in land and development costs	170,179,989	6,240,630	—
Decrease (increase) in other current assets	30,504,472	(24,240,795)	37,105,386
Increase (decrease) in trade and other payables	(49,226,709)	37,289,581	(57,737,563)
Decrease in estimated liability for land and development cost	(8,369,145)	(12,571,405)	(2,412,921)
Increase (decrease) in advances from related parties	(137,454,437)	71,193,409	33,288,112
Cash generated from continuing operations	387,664,712	250,058,564	454,800,301
Cash paid for income taxes	(43,091,909)	(60,850,886)	(39,088,760)
Net Cash from Continuing Operating Activities	344,572,803	189,207,678	415,711,541
CASH FLOWS FROM INVESTING ACTIVITIES			
Interest received	161,345,804	129,561,350	83,694,759
Proceeds from sale of short-term investments	84,543,972	74,993,165	—
Cash from return of shares of stock in an associate	26,730,000	—	—
Net cash from acquired division	21,342,086	—	—
Proceeds from sale of property and equipment	13,519,001	79,109,912	26,592,861
Proceeds from sale of other current assets	4,851,000	—	—
Placement in short-term investments	(86,134,936)	(689,797,779)	—
Decrease (increase) in other non-current assets	(111,612,459)	(335,783,176)	56,458,140
Acquisitions of property and equipment	(131,506,662)	(80,632,255)	(123,166,955)
Decrease (increase) in investments and advances	(203,344,533)	(51,275,128)	151,193,740
Net Cash From (Used in) Investing Activities	(220,266,727)	(873,823,911)	194,772,545

forward

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended December 31, 2004 (With Comparative Figures for 2003 and 2002)

	2004	2003	2002
CASH FLOWS FROM FINANCING ACTIVITIES			
Interest paid	(8,833,348)	(2,030,056)	(728,842)
Minority interest	(17,272,493)	(55,085,753)	(32,506,873)
Payments of long-term debt and loans payable	(29,221,885)	(79,843,123)	(98,715,794)
Proceeds from loans payable	—	291,634,490	—
Acquisition of treasury shares	—	—	(784,218)
Net Cash From (Used in) Financing Activities	(55,327,726)	154,675,558	(132,735,727)
Effect of Exchange Rate Changes on Cash and Cash Equivalents	3,829,201	1,978,000	—
Net Cash Flows From (used in) Continuing Operations	72,807,551	(527,962,675)	477,748,359
CASH FLOWS FROM DISCONTINUED OPERATIONS			
Net cash from (used in) operating activities	(1,970,522)	17,306,962	(647,720)
Net cash from investing activities	—	1,286,148	45,152,858
Net cash used in financing activities	—	(15,381,848)	—
Net Cash Flows From (Used in) Discontinued Operations	(1,970,522)	3,211,262	44,505,138
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	70,837,029	(524,751,413)	522,253,497
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	1,548,376,544	2,073,127,957	1,550,874,460
CASH AND CASH EQUIVALENTS AT END OF YEAR	P 1,619,213,573	P 1,548,376,544	P 2,073,127,957

Supplemental Information on Noncash Investing and Financing Activities

In 2004, the Destiny, Inc. "DI" acquired certain assets and assumed certain liabilities of the Data Division of a related party. Total non-cash assets and liabilities transferred as a result of the acquisition amounted to P171,347,210 and P192,689,296, respectively (see Notes 1 and 12).

In 2003, the Company acquired the entire issued and outstanding shares of DI. As part of the transfer of ownership of DI, the Company recognized the constructive issuance of 224,461,752 shares of stock, and recorded additional paid-in capital of P75,826,336 for the excess of the total paid-in capital acquired over the total par value of the shares issued. In addition, receivables from Destiny Cable, Inc. ("DCI") amounting to P731,775,989 was written off against additional paid-in capital. In 2004, SGI and DCI agreed that certain receivables from and payables to related parties with a total net amount of P247,662,762 were to be excluded from the valuation of DI's net assets. The re-valuation of the net assets of DI were effected in 2004 as a reduction in advances to related parties and reversal of the previously recognized capital stock issuance and the related additional paid-in capital (see Notes 1 and 16).

See Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2004 (With Comparative Figures for 2003 and 2002)

I. Corporate Information and Status of Operations

Corporate Information

Solid Group Inc. ("SGI" or the "Company") and its subsidiaries (collectively referred to herein as the "Group"), are incorporated in the Philippines, except for Brilliant Reach Limited ("BRL"), which is incorporated in the British Virgin Islands ("BVI").

The Company holds interests in the following companies:

Investee Company	Percentage of Ownership		
	2004	2003	2002
Subsidiaries:			
Brilliant Reach Limited ("BRL")	100%	100%	-
Destiny, Inc. ("DI") and Subsidiaries	100	100	-
Kita Corporation ("Kita")	100	100	100%
Omni Logistics Corporation ("OLC")	100	100	100
Solid Broadband Corporation ("SBC")	100	100	100
Solid Corporation ("SC") and Subsidiaries	100	100	100
Solid Electronics Corporation ("SEC")	100	100	100
Solid Laguna Corporation ("SLC")	100	100	100
Solid Manila Corporation ("SMC") and Subsidiaries	100	100	100
Solid Manila Finance, Inc. ("SMFI")	100	100	100
Solid Video Corporation ("SVC")	100	100	100
AA Electronics Corporation ("AAEC")	-	100	100
Associate:			
Sony Philippines, Inc. (SPH")	33	33	33

The Subsidiaries of DI are as follows:

Investee Company	Percentage of Ownership		
	2004	2003	2002
Destiny Communication Corporation ("DCC")	100%	100%	100%
Destiny Multimedia Corporation ("DMC")	100	100	100
Destiny On-line Corporation ("DOC")	100	100	100
Omni Distribution Services, Inc. ("ODSI")	100	100	100

The Subsidiaries of SC are as follows:

Investee Company	Percentage of Ownership		
	2004	2003	2002
SSEC, Inc. ("SSEC")	100%	67%	67%
Precos, Inc. ("Precos")	100	60*	60*
Interstar Holdings Company, Inc. ("IHC")	60	60	60
Laguna International Industrial Park, Inc. ("LIIP")	45	45	45
Clark Plastics Manufacturing Corporation ("CPM")	-	100	100
Solid Electronics Services, Inc. ("SESI")	-	100	100

* In 2003 and 2002, Precos was not consolidated with the Company due to SC's lack of significant control over the operating and financial policies of the investee, and in 2004, SC acquired the remaining 40% ownership interest which was accounted for using the purchase method.

The Subsidiaries of SMC are as follows:

Investee Company	Percentage of Ownership		
	2004	2003	2002
Skyworld Corporation ("Skyworld")	75%	75%	75%
Starworld Corporation ("Starworld")	50	50	50

The Group's main business activities are broadband cable and satellite services, manufacturing of injected plastics and assembly by colored television, repair services for audio and video products, real estate, trading of plastic resins and professional audio/video equipment and peripherals, and financing.

SBC's application with the National Telecommunications Commission for a provisional authority to use its legislative franchise under Republic Act ("RA") No. 9116 entitled "An Act Granting Solid Broadband Corporation a Franchise to Construct, Install, Establish, Operate and Maintain Telecommunications Systems throughout the Philippines", which took effect on April 14, 2001, was approved on April 23, 2002. SBC plans to utilize DI's broadband infrastructure in operating its franchise.

Acquisition of Subsidiaries and a Subsidiary's Division

a. In May 2003, the Company acquired from Destiny Cable, Inc. ("DCI") the entire issued

and outstanding shares of DI, a company engaged in broadband cable and satellite services, in exchange for the proposed issuance of 224,461,752 shares of the Company's common stock. The acquisition was in accordance with the stockholders' approval in November 2002. The acquisition was approved by the BIR on May 15, 2003. A notice of exemption for the issuance of shares under the Revised Securities Act was filed with the Securities and Exchange Commission (the "Commission") on November 6, 2003.

The acquisition of DI was accounted for similar to the pooling of interest accounting. Under this method, similar accounts of the entities starting 2003 were consolidated on a line-by-line basis except for the equity accounts of DI which was recorded as additional paid-in capital in the consolidated financial statements. For comparative purposes, the separate accounts of the entities for 2002 were combined on a line-by-line basis.

In 2004, upon further review of the assets and liabilities of DI, certain receivables from and payables to related parties were removed from the valuation of DI's net assets. The re-valuation resulted in a change in its financial position from a net asset to a net liability of P23,201,010. The Company and DCI agreed that the Company would no longer issue shares of stock to DCI as payment for its acquisition of DI but instead assume DI's net liability representing the excess of the estimated fair value of DI's broadband cable infrastructure and its existing cable internet subscriber base over their aggregate book value which, in accordance with the pooling of interest accounting applied to this transaction, was charged to additional paid-in capital (see Note 16).

b. In 2004, DI acquired the Data Division of DCI with total assets and amounting to P192,689,297 and total liabilities of the same amount. The acquisition was accounted for as a purchase. Consequently, the assets and liabilities of the Data Division are initially measured in the books of DI at fair value.

c. In 2003 and prior years, SC holds 60% interest in Precos, a company in preoperating stage. The investment was accounted for using the cost method because SC has no significant control over the operating and financial policies of Precos. In 2004, SC increased its interest in Precos to 100% by acquiring the remaining 40% interest for a consideration of P6.5 Million thereby making Precos a wholly-owned subsidiary of SC. The acquisition is accounted for using the purchase method and the excess of the fair value of the net assets acquired over total purchase price amounting to P19.3 million is recognized as negative goodwill and is directly recognized as income and included as part of Other income account in the 2004 consolidated statement of income since most of the assets held by Precos are non-depreciable as prescribed under SFAS 22, *Business Combinations*. The investment, which initially formed part of the Other Non-current Assets account, was reclassified to the Investments in Shares of Stocks account and is now accounted for using the equity method in SC's financial statements. Moreover, Precos is consolidated in the Company's financial statements starting in 2004, when the Company obtained control over the subsidiary.

d. SC also increased its interest in SSEC to 100% in 2004, from 67.50% in 2003, by acquiring the 32.50% minority interest for a consideration of P33.5M. As of December 31, 2004, the amount remains unpaid and forms part of the Trade and Other Payables account in the 2004 consolidated balance sheet (see Note 15).

e. On July 31, 2003, the Company acquired 100% ownership of BRL, a BVI offshore company. At the time of BRL acquisition, the offshore company had no assets and liabilities. BRL handles and manages the investment of the Company's funds in foreign currency fixed income financial assets, principally bonds, not exceeding 20% of such amount of funds. The net exchange differences that were taken to the Company's consolidated statement of income as a result of translating the financial statements of BRL, a foreign operation that is integral to the operations of the Company, amounted to P3.4 million in 2004 and P4.0 million in 2003 and are shown as part of Foreign Currency Gains account in the consolidated statements of income.

Changes in Corporate Structure

The Company has initiated a structural reorganization of its various units to sustain operational efficiency through mergers. The results of the said mergers are discussed below:

a. SEC, SESI and AAEC

On December 2, 2003, the stockholders of SEC, SESI and AAEC approved the merger of the three companies. The merger dissolved SESI and AAEC and transferred all their operations, assets and liabilities to SEC, the surviving company. The commission approved the merger on April 12, 2004. Prior to the merger, SESI and AAEC were wholly owned subsidiaries of SC and SGI, respectively. The merger was accounted for at historical cost in a manner similar to that of a pooling of interest method. The

combined net assets of the SEC, SESI and AAEC after the merger amounted to P72,083,706 and P61,430,015 as of December 31, 2004 and 2003, respectively. In 2004 and 2003, the combined net income of SEC, SESI and AAEC amounted to P10,653,691 and P7,225,786, respectively.

b. KITA and CPM

On December 2, 2003, the stockholders of Kita and CPM approved the merger of these two companies. The merger dissolved CPM, a company engaged in the business of manufacturing, importing, exporting, buying, selling or otherwise dealing in, at wholesale, plastic injection molding parts, and transferred all its operations, assets and liabilities to Kita, the surviving company. The Commission approved the merger on April 12, 2004. Prior to the merger, CPM was a wholly owned subsidiary of SGI. The merger was accounted for at historical cost in a manner similar to that of a pooling of interest method. The combined net liabilities of Kita and CPM after the merger amounted to P522,816,768 and P542,764,126 as of December 31, 2004 and 2003, respectively. The combined net income of Kita and CPM in 2004 and 2003 amounted to P19,947,360 and P12,320,777 respectively.

c. SBC and DI

The stockholders of both SBC and DI approved the merger of the two companies on November 5, 2003. The merger will dissolve DI and transfer all its operations, assets and liabilities to SBC, the surviving company. The merger will be effected once the approval from the Commission has been secured. As of December 31, 2004, the Commission has not yet approved the merger of DI and SBC.

d. SMC and Solid Distributors, Inc. ("SDI")

On October 15, 2003, the stockholders of SMC and SDI approved the merger of these two companies. The merger dissolved SDI and transferred all its operations, assets and liabilities to SMC, the surviving company. The Commission approved the merger on December 23, 2003. Prior to the merger, SDI was a wholly owned subsidiary of SGI. The merger was accounted for at historical cost in a manner similar to that of a pooling of interest method. The combined net assets of SMC and SDI after the merger amounted to P117,055,515 as of December 31, 2003. The combined net income of SMC and DI in 2003 amounted to P38,936,515.

e. DI and Destiny Satellite Corporation ("DSC")

On August 20, 2002, the stockholders of DI and DSC approved the merger of these two companies. The merger dissolved DSC and transferred all its operations, assets and liabilities to DI, the surviving company. The Commission approved the merger on January 7, 2003. Prior to the merger, DSC was a wholly owned subsidiary of DI. The merger was accounted for at historical cost in a manner similar to that of a pooling of interest method. The combined assets of DI and DSC after the merger amounted to P989,629,182 as of December 31, 2002. The combined net loss of DSC and DI in 2002 amounted to P77,701,887.

Quasi-Reorganization

- a. In May 2003, SGI acquired DCI's 100% interest in DI. As part of the restructuring and, as a requirement prior to the acquisition by SGI, DI offset its claim from DCI amounting to P731.78 million against its additional paid-in capital.

On August 20, 2004, the Commission approved the conversion of P440 million advances from SGI to additional paid-in capital and the application of the resulting balance against DI's deficit as of December 31, 2003. The quasi-reorganization eliminated the entire deficit of DI as of December 31, 2003 amounting to P577 million. The remaining amount of Additional Paid-in Capital in the books of DI after quasi-reorganization is not allowed to be used to wipe out losses that may be incurred in the future without prior approval of the Commission.

- b. On August 2, 2004, DI's Board of Directors approved the conversion of a portion of DI's advances to DOC amounting to P3 million to equity in relation to DOC's quasi-reorganization. This transaction was approved by the Commission on August 20, 2004.

Return of Investment in an Associate

In August 2004, the common shareholders of SPH, including the Company, received a partial return of their investment in SPH. The Company's investment in SPH has zero net book value and the Company has stopped recognizing equity share in net loss after the accumulated share in net losses already recognized equalled the acquisition cost of the investment. The amount received of P26,730,000 was taken up as a gain and included as part of Equity in Net Earnings (Losses) of Subsidiaries and an Associate under the Other Revenues account in the 2004 consolidated statement of income (see Note 11). The Joint Venture Agreement ("JVA") executed in 1997 with Sony Corporation of Japan

covering the Company's investment in SPH will expire on May 8, 2005. On April 11, 2005, the Company received a formal notice from Sony Holding (Asia) B.V. of the expiry of the JVA. The Company and Sony Corporation have agreed to pursue negotiations for an equitable settlement of all matters relating to the JVA and its expiration.

Status of Operations of the Group

Up to mid-2003, the Group's core business had been the manufacture, marketing and wholesale distribution of consumer electronic products ("SONY" and "AIWA" brands). However, this business had been severely affected by intense competition as import liberalization made it more cost efficient to import complete sets than to manufacture locally. Moreover, the manufacturing agreements with SPH and Aiwa Singapore, Ltd. ("Aiwa Singapore") expired and were not renewed. Thus, the Group closed the consumer electronics operations of its major subsidiaries, namely, SC, SSEC and Kita prior to 2002 and SLC in 2002. It also closed the wholesale distribution and marketing operations of Solid Distributors, Inc. ("SDI") in 2000 for SONY brand and in July 2003 for the AIWA brand.

In 1977, SGI and Sony Corporation ("Sony") of Japan entered into an agreement granting SLC exclusive rights to manufacture certain Sony products and related parts and components in the Philippines. The agreement, which further binds Sony to purchase certain products exclusively from SLC, was terminated on September 30, 2002. As a result, SLC's manufacturing operations of Sony products was discontinued in December 2002. (See Note 13)

Other Corporate Information

The registered office of the Company and its subsidiaries, except those listed below, is located at Solid House, 2285 Don Chino Roces Avenue Extension, Makati City. The registered offices of the other subsidiaries are as follows:

BRL	- 2 nd Floor, Abbott Building, P.O. Box 933, Road Town, Tortola, British Virgin Islands
Kita	- 7170 Clark Special Economic Zone, Clark Field, Pampanga
SC	- 17 A. Fernando St., Marulas, Valenzuela, Metro Manila
SMC	- 1000 J. Bocobo St., Ermita, Manila
SSEC / SEC	- 1172 E. delos Santos Avenue, Balintawak, Quezon City
Starworld	- Bo. Prinza, Calamba City.

The Group operates within the Philippines, except BRL which operates in BVI, and had 837, 802 and 1,110 employees as of December 31, 2004, 2003 and 2002, respectively.

The consolidated financial statements of the Group for the year ended December 31, 2004 were authorized for issue by the Company's Board of Directors on April 13, 2005.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Preparation of Consolidated Financial Statements

The consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the Philippines.

The consolidated financial statements have been prepared on a historical cost basis, except for the measurement at the lower of aggregate cost or market value of short term investments.

The accounting policies have been consistently applied by the Group and are consistent with those used in the previous year, except for the adoption of new accounting standards as discussed below.

Adoption of New Accounting Standards

The Group adopted the following Statements of Financial Accounting Standards ("SFAS")/International Accounting Standards ("IAS") issued by the Accounting Standards Council ("ASC") that are relevant to the Group, in the respective year the accounting standards became effective:

2004		
SFAS 12/IAS 12	:	Income Taxes
SFAS 17/IAS 17	:	Leases
2003		
SFAS 8A	:	Deferral of Foreign Exchange Differences
SFAS 10/IAS 10	:	Events After the Balance Sheet Date
SFAS 22/IAS 22	:	Business Combinations
SFAS 37/IAS 37	:	Provisions, Contingent Liabilities and Contingent Assets
SFAS 38/IAS 38	:	Intangible Assets

2002		
SFAS 16/IAS 16	:	Property, Plant and Equipment
SFAS 24/IAS 24	:	Related Party Disclosures
SFAS 27/IAS 27	:	Consolidated Financial Statements and Accounting for Investments in Subsidiaries
SFAS 28/IAS 28	:	Accounting for Investments in Associates
SFAS 36/IAS 36	:	Impairment of Assets

The effects of the Group's adoption of SFAS 12/IAS 12 and SFAS 17/IAS 17 in 2004, SFAS 38/IAS 38 in 2003 are discussed in Note 3. The Group's adoption of the other new accounting standards did not result in material adjustments to the financial statements of the current and prior years.

Certain accounts in the 2003 and 2002 consolidated financial statements have been reclassified to conform to the 2004 presentation and classification.

Impact of New and Revised Accounting Standards Effective Subsequent to 2004

In 2004, the ASC issued a series of new accounting standards that are adopted from existing IAS, revised IAS and new International Financial Reporting Standards ("IFRSs") issued by the International Accounting Standards Board ("IASB"). The new ASC accounting standards are effective in the Philippines for financial statements covering periods beginning on or after January 1, 2005. Also, the ASC re-named its accounting standards to correspond better with the IASB pronouncements. Philippine Accounting Standards ("PASs") correspond to the adopted IASs, while Philippine Financial Reporting Standards ("PFRSs") correspond to the adopted IFRSs. Existing SFASs and SFASs/IASs not yet superseded will be reissued by the ASC as PASs.

The new ASC pronouncements that are effective in 2005 are the following:

PAS 1	:	Presentation of Financial Statements
PAS 2	:	Inventories
PAS 8	:	Accounting Policies, Changes in Accounting Estimates and Errors
PAS 10	:	Events After the Balance Sheet Date
PAS 16	:	Property, Plant and Equipment
PAS 17	:	Leases
PAS 19	:	Employee Benefits
PAS 21	:	The Effects of Changes in Foreign Exchange Rates
PAS 24	:	Related Party Disclosures
PAS 27	:	Consolidated and Separate Financial Statements
PAS 28	:	Investments in Associates
PAS 29	:	Financial Reporting in Hyperinflationary Economies
PAS 30	:	Disclosures in the Financial Statements of Banks and Similar Institutions
PAS 31	:	Interests in Joint Ventures
PAS 32	:	Financial Instruments: Disclosures and Presentation
PAS 33	:	Earnings per Share
PAS 36	:	Impairment of Assets
PAS 38	:	Intangible Assets
PAS 39	:	Financial Instruments: Recognition and Measurement
PAS 40	:	Investment Property
PAS 41	:	Agriculture
PFRS 1	:	First-time Adoption of PFRS
PFRS 2	:	Share-based Payment
PFRS 3	:	Business Combinations
PFRS 4	:	Insurance Contracts
PFRS 5	:	Non-current Assets Held for Sale and Discontinued Operations

The Group will apply the relevant new accounting standards in 2005 in accordance with their transitional provisions. It is currently evaluating the impact of those standards on its consolidated financial statements and has initially determined that the following new standards may have significant effects on the consolidated financial statements for 2005, as well as for prior and future periods:

- **PAS 19, Employee Benefits.** This new accounting standard prescribes the accounting and disclosure by employers for employee benefits. Employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees. These benefits include short-term benefits (such as short-term compensated absences and profit sharing and bonus plans), post-employment benefits (such as pension plans), other long-term benefits (such as long-service leave or sabbatical leave), termination benefits and equity compensation benefits. Presently, the Group provides short-term benefits to its employees and recognizes employee benefits on its defined benefits pension plan. The Group initially assessed that the application of PAS 19 will not have a material effect on its consolidated financial statements.

- **PAS 21, The Effects of Changes in Foreign Exchange Rates.** PAS 21 requires the recognition of foreign exchange differences as income or expense in the period in which they arise. This standard removes the distinction between integral foreign operations and foreign entities and no longer allows capitalization of foreign currency differences even under severe currency devaluation. The standard also replaced the notion of 'reporting currency' with the notions of 'functional currency' and 'presentation currency.' Functional currency is the currency of the primary economic environment in which the entity operates; presentation currency is the currency in which the financial statements are presented. The standard allows the financial statements of a company to be presented in any currency (or currencies). For financial reporting purposes, BRL will present its financial statements in Philippine peso.

Under the new standard, all assets and liabilities are translated at the closing rate while income and expense accounts are translated at the actual rate prevailing on the date of the transactions, or an average rate as an approximation. As of December 31, 2004, Prepaid Expenses related to insurance policies recorded in the books of BRL amounted to US\$216,088 which is translated to Philippine peso at the actual rate prevailing on the date of the purchase of the asset, or P11,813,554. If translated at current rate, the peso amount would be P12,158,623. In addition, net foreign exchange differences arising from translation of the financial statements of BRL charged as part of current operations amounted to P3.4 million in 2004 and P4.0 million in 2003.

- **PAS 27, Consolidated and Separate Financial Statements.** This new accounting standard requires consolidated financial statements to be prepared based on control of subsidiaries, control being defined as the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. It also requires the reporting date of the parent and its subsidiaries to be not more than three months apart. Further, when separate financial statements are prepared, investments in subsidiaries, jointly controlled entities and associates in those separate financial statements should be accounted for either at cost or in accordance with PAS 39, *Financial Instruments: Recognition and Measurement*.
- **PAS 28, Investment in Associates.** PAS 28 requires investment in associate to be accounted for using the equity method, except when the investment is classified as non-current asset held for sale and when the investor itself is a subsidiary. Further, the standard requires an investment in an associate to be accounted for in the investor's separate financial statement at cost or in accordance with PAS 39.
- **PAS 32, Financial Instruments: Disclosures and Presentation.** PAS 32 prescribes the requirements for the presentation of financial instruments and identifies information that should be disclosed about them. The presentation requirements apply to the classification of financial instruments, from the perspective of the issuer, into financial assets, financial liabilities and equity instruments, as well as the classification of the related income and expense items. The required disclosures include information that affect the amount, timing and certainty of future cash flows relating to the financial instruments, the accounting policies applied to those instruments and the risks associated with them and management's policies for controlling those risks. The standard also requires and provides guidance on the separation of the liability and equity components of a compound financial instrument.
- **PAS 36, Impairment of Assets.** This new accounting standard requires that at each reporting date, an entity should assess whether there is any indication that an asset may be impaired. If any such indication exists, an entity should estimate the recoverable amount of the asset, which is the higher of (a) the asset's fair value less costs to sell, and (b) its value in use, which is the present value of the future cash flows expected to be derived from an asset or cash-generating unit. An impairment loss is recognized immediately in profit or loss. An impairment loss recognized in prior periods is reversed if there is a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized except for impairment loss on goodwill which is no longer allowed to be reversed. The adoption of PAS 36 may have an impact on the future restructuring to be initiated by the Company considering that goodwill arising from the merger, if any, is subject to test for impairment.
- **PAS 39, Financial Instruments: Recognition and Measurement.** This new standard prescribes the principles for recognizing, measuring and disclosing information about financial instruments in the financial statements of companies. It requires initial recognition of a financial asset or liability at fair value, which is normally the transaction price (i.e., the fair value of the consideration given or received). Subsequent measurement is at fair value, amortized cost using the effective interest method, or cost depending on the classification of the financial asset or liability. Recognition of gains or losses mainly from changes in the fair values, amortization, impairment and derecognition also depends on the classification

of the financial instruments. The initial adoption by the Company of PAS 39 in 2005 may give rise to recognition of previously unrecognized assets and liabilities, the derecognition of previously recognized assets and liabilities and recognition of gains or losses from fair value changes that may have material impact on its consolidated financial statements.

- **PAS 40, Investment Property.** This new standard prescribes the accounting treatment for investment property and related disclosure requirements. Investment property is property (generally land or a building or part of a building) held to earn rentals or for capital appreciation, rather than for use in production or supply of goods or services or for administrative purposes, or sale in the ordinary course of business. Investment property is initially recognized at cost. For measurement after initial recognition, an entity shall choose as its accounting policy either the fair value model or the cost model in valuing investment property. Under the fair value model, the investment property is measured at fair value which changes in fair value recognized in profit or loss. Under the cost model, the investment property is measured at depreciated cost (less any accumulated losses). While the Group expects to make reclassification of certain assets as investment property in 2005, the model to be adopted for measuring those assets still has to be decided.
- **PFRS 3, Business Combinations.** This new accounting standard requires that all combinations within the scope of this standard be accounted for by applying the purchase method (pooling of interests method is no longer allowed). All identifiable assets, liabilities and contingent liabilities acquired are measured at fair values. Identifiable intangible assets are recognized separately from goodwill, goodwill being the excess of the cost of the business combination over the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities. If instead there is negative goodwill, the entity should reassess the identification and measurement process relating to the business combination. Any negative goodwill still remaining after such reassessment must be recognized by the acquirer immediately in profit or loss.
- **PFRS 5, Non-current Assets Held for Sale and Discontinued Operations.** This new standard provides that a non-current asset or disposal group (assets to be disposed as a group in a single transaction, and liabilities directly associated with those assets that will be transferred in the transaction) should be classified as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. Subsequently, non-current assets or disposal groups classified as held for sale should be measured at the lower of their (a) carrying amount and (b) fair value less costs to sell. While classified as held for sale, the assets should not be depreciated but subjected to impairment assessment and any impairment loss must be recognized in profit or loss. Any subsequent increases in fair value less costs to sell shall be recognized as gain, but not in excess of the cumulative impairment losses already recognized on the asset.

As for the other new accounting standards, the Group has initially assessed that they will not result in significant changes to the amounts or disclosures in its consolidated financial statements.

Principles of Consolidation

The consolidated financial statements comprise the accounts of the Company and its subsidiaries listed in Note 1, after elimination of material intercompany transactions.

Subsidiaries are consolidated from the date the Company obtains control until such time that such control ceases.

In 2004, the Group acquired full ownership and control of Precos, an investee company previously carried in the books at cost. The financial statement items of Precos are included in the consolidated financial statements from the time the Group acquired control over the subsidiary.

DI and its subsidiaries were acquired by the Group from a company controlled by its major shareholder group. The acquisition, being a transaction between entities under common control, was accounted for under historical cost accounting similar to a pooling of interest. The financial statement items of DI are included in the consolidated financial statements as if these have been part of the Group from the earliest date presented.

In 2003, the Group acquired full ownership of BRL, a foreign company organized in the BVI. The subsidiary's assets, liabilities, as well as the results of its operations and cash flows, are included in the consolidated financial statements beginning 2003.

The Company's and its subsidiaries' financial statements are prepared using uniform accounting policies for like transactions and other events in similar circumstances. The financial statements of the Company and its subsidiaries are prepared for the same reporting period, except for the financial statements of Skyworld, Starworld, and LIIP

which are prepared as of and for fiscal years ended October 31. Adjustments were made for the effects of significant transactions or events that occur between those dates and the date of the Company's financial statements.

Cash and Cash Equivalents

Cash and cash equivalents are defined as cash on hand, demand deposits and short-term, highly liquid investments readily convertible to known amounts of cash and which are subject to insignificant risk of changes in value.

Investments

Investments are initially recorded at cost at the time of acquisition, which is generally measured by the purchase price of the security, or the fair value of the asset given up or the security received in the exchange and other costs directly related to the acquisition. Subsequent to acquisition, the carrying values of the investments are determined as follows:

- Short term investments are carried at the lower of its aggregate cost or market value at the balance sheet date. The excess of aggregate cost over market value is accounted for as valuation allowance. Realized gains and losses and changes in the valuation allowance are recognized in income of the period in which they occur. In computing realized gains or losses, cost is determined on the average cost basis.
- Investments in associates are initially recorded at cost at the time of acquisition, which is generally measured by the purchase price of the security, or the fair value of the asset given up or the security received in the exchange and other costs directly related to the acquisition. Subsequent to acquisition, the carrying values of the investments are determined using the equity method of accounting for investments in shares of stock. Under the equity method, the cost of investments is adjusted for the Company's equity in net earnings or losses of the investee since the date of acquisition, less any impairment in value. However, if recording its share of further losses of an associate is discontinued when such losses equal or exceed the carrying amount of an investment maintained under the equity method, the investment is reported at nil value. Additional losses are provided for to the extent that the Company has incurred obligations or made payments on behalf of the associate to satisfy obligations of the associate that the Company has guaranteed or otherwise committed.
- Other investments, consisting mainly of shares of stock and club membership, are carried at cost.

Trade and Other Receivables

Trade receivables are recognized and carried at original invoice amounts less allowance for any uncollectible amounts. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off when identified.

Inventories

Inventories are valued at the lower of cost and net realizable value.

Cost incurred in bringing each product to its present location and condition is accounted for as follows:

- Raw materials and supplies – purchase cost on a first-in, first-out basis in the case of Kita and OLC, moving average method for DI, SEC, SLG and SVC; and,
- Finished goods and work-in-process – determined on a moving average method; cost includes direct materials and labor and a proportion of manufacturing overheads based on normal operating capacity. For Kita, cost is based on standard cost, which approximates actual cost, of direct materials and labor and a proportion of manufacturing overheads based on normal operating capacity.

Net realizable value for finished goods and work-in-process is the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs necessary to make the sale. Net realizable value for raw materials and supplies is the current replacement cost.

Land and Development Costs

Acquisition costs of raw land intended for future development, including other costs and expenses incurred to effect the transfer of property title to Starworld, are included in the Land and Development Costs account. Related property development costs are also accumulated in this account.

Revenue from sale of land is accounted for using the full accrual method. Under this method, income is recognized when it is probable that the economic benefits from the sale will flow to Starworld and collectibility of the sales price is reasonably assured. Cost of real estate property sold before completion of the development is determined on the basis of the acquisition cost of the land plus its full development costs, which include estimated costs for future development, as determined by Starworld's technical staff. The estimated future expenditures for the development of the real estate property for sale are shown under the Estimated Liability for Land Development Costs account in the consolidated balance sheet.

Land and development costs are carried at the lower of cost and net realizable value. Net realizable value is the selling price in the ordinary course of business, less costs to complete development work and cost to sell. Starworld recognizes the effect of revisions in the total project cost estimate in the year in which these changes become known. Any impairment loss from a real estate project is charged to operations in the period in which the loss is determined.

Property, Plant and Equipment

Property, plant and equipment are stated at cost less accumulated depreciation and amortization and any impairment in value. The cost of an asset comprises its purchase price and directly attributable costs of bringing the asset to working condition for its intended use. Expenditures for additions, major improvements and renewals are capitalized; expenditures for repairs and maintenance are charged to expense as incurred. When assets are sold, retired or otherwise disposed of, their cost and related accumulated depreciation and amortization and impairment losses are removed from the accounts and any resulting gain or loss is reflected in income for the period.

Construction in progress is stated at cost. This includes cost of construction, plant and equipment and other direct costs. Construction in progress is not depreciated until such time as the relevant assets are completed and put into operational use.

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

Buildings and improvements	10-25 years
Cable system equipment	5-20 years
Machinery and equipment	5-10 years
Furniture, fixtures and office equipment	2-5 years
Transportation equipment	5 years
Test, communication and other equipment	5 years
Computer system	5 years
Tools and equipment	2 years

Leasehold improvements are amortized from 2-15 years or over the term of the lease, whichever is shorter.

The useful life and depreciation and amortization method are reviewed periodically to ensure that the period and method of depreciation are consistent with the expected pattern of economic benefits from items of property, plant and equipment.

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

Leasehold Rights

Leasehold rights, included as part of Other Non-current Assets, are recorded at cost less accumulated amortization and any impairment in value. The cost of the asset is the amount of cash or cash equivalents paid or the fair value of the other considerations given to acquire an asset.

Revenue Recognition

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognized:

- Sale of goods – Revenue is recognized when the risks and rewards of ownership of the goods have passed to the buyer and the amount of revenue can be measured reliably.
- Rendering of services – Revenue is recognized when services are rendered.
- Rental – Revenue is recognized on a straight-line basis over the duration of the lease term.
- Sale of investments – Revenue is recognized when the risks and rewards of ownership of the investments have passed to the buyer and the amount of revenue can be measured reliably.

- Interest income on loans receivables – Revenue is recognized when earned. In accordance with RA No. 8556, interest income is not recognized on loans receivable that remain outstanding beyond their maturity dates.
- Other interest – Revenue is recognized as the interest accrues (taking into account the effective yield on the asset).

Leases

- Group as lessee – Leases, which transfer to the Group substantially all risks and benefits incidental to ownership of the leased item, are classified as finance leases and are recognized as assets and liabilities in the consolidated balance sheets at amounts equal at the inception of the lease to the fair value of the leased property or, if lower, at the present value of minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are directly charged against income. Capitalized leased assets are depreciated over the shorter of the estimated useful life of the asset or the lease term.

Leases, which do not transfer to the Group substantially all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognized as expense in the consolidated statements of income on a straight-line basis over the lease term.

- Group as lessor – Leases, whereby the Group substantially transfers to the lessee all risks and benefits incidental to ownership of the leased item, are classified as finance leases and are presented as receivable at an amount equal to the Group's net investment in the lease. Finance income is recognized based on the pattern reflecting a constant periodic rate of return on the Group's net investment outstanding in respect of the finance lease.

Leases, whereby the Group does not substantially transfer all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognized as revenue in the consolidated statement of income on a straight-line basis over the lease term.

Foreign Currency Transactions

The accounting records of the Group, except BRL, are maintained in Philippine pesos. Foreign currency transactions during the year are translated into Philippine pesos at exchange rates which approximate those prevailing on transaction dates. Foreign currency monetary assets and liabilities at the consolidated balance sheet date are translated into Philippine pesos at exchange rates which approximate those prevailing on that date. Exchange gains and losses are recognized in income for the period.

The financial statements of the BRL, expressed in U.S. dollars, have been translated into Philippine peso amounts for consolidation with the Group's financial statements. The following procedures are applied in translating the financial statements into Philippine pesos:

- Monetary assets and liabilities are translated into Philippine peso using the exchange rate prevailing as of the balance sheet date.
- Prepaid Expenses, a non-monetary asset, is translated at the exchange rate prevailing at the time the amount was paid.
- Revenue and expense items are translated using monthly average exchange rates. Any exchange differences arising from the translation are recognized as income or expense for the year.

The translation of the financial statements into Philippine peso should not be construed as a representation that the U.S. dollar amounts could be converted into Philippine peso amounts at the translation rates or at any other rates of exchange.

Provisions

Provisions are recognized when the Group has a present obligation (whether legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Provisions are reviewed at each balance sheet date and adjusted to reflect the current best estimate.

Impairment of Assets

The carrying values of property, plant and equipment; investment in an associate, other long-term investments; leasehold rights and other intangible assets are reviewed for

impairment when events or changes in circumstances indicate that their carrying values may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets or cash generating units are written down to their recoverable amount. The recoverable amount of the assets is the greater of net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognized in the consolidated statement of income.

If there is any indication at the balance sheet date that an impairment loss recognized for an asset in prior years may no longer exist or may have decreased, the Group estimates the recoverable amount of that asset and the carrying amount of the asset is adjusted to the recoverable amount resulting in the reversal of the impairment loss.

Reserve for Warranty

A reserve amounting to 1% of sales of equipment (net of consumable items) is maintained for expected warranty claims on products sold during the year. Sales of equipment are covered by one year warranty on services. The sufficiency of reserve is assessed annually based on the Group's past experience of the level of repairs and returns. Any excess provision over the actual claims are reversed on the year following the recognition of provision for warranty.

Employee Benefits

The Company has a defined benefit multi-employer pension plan covering all regular full-time employees. The pension plan is tax-qualified, noncontributory and administered by a trustee. The cost of providing benefits under the plan is determined using the projected unit credit actuarial valuation method, which utilizes the normal cost, actuarial accrued liability and unfunded actuarial liability concepts. Past service cost is amortized and actuarial gains and losses are recognized over the expected remaining working lives of the employees covered by the plan.

Income Taxes

Deferred income tax is provided, using the balance sheet liability method effective 2004 (see Note 3), on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Under the balance sheet liability method, deferred tax liabilities are recognized for all taxable temporary differences:

- except where the deferred tax liability arises from goodwill amortization or the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and,
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, except where the timing of the reversal of temporary differences can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax assets are recognized for all deductible temporary differences and the carryforward of unused tax losses and unused tax credits to the extent that it is probable that taxable profit will be available against which the deferred tax assets can be utilized:

- except where the deferred tax asset deductible to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and,
- in respect of deductible temporary difference associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are only recognized to the extent that it is probable that the temporary difference will reverse in the foreseeable future and taxable profit will be available against which the temporary difference can be utilized.

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

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

3. CHANGES IN ACCOUNTING POLICIES

Income Taxes

On January 1, 2004, the Group adopted the balance sheet liability method of accounting for income taxes under SFAS 12/IAS 12, *Income Taxes*, which became effective on that date. Prior to 2004, the Group used the method of accounting for income taxes wherein deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences mainly between the taxable income and accounting income and tax consequences of net operating loss carryover ("NOLCO").

The Group adopted the new accounting standard retroactively and resulted in the following adjustments to the consolidated financial statements of the current and prior year:

- Reclassification of deferred tax assets and liabilities – Current deferred tax assets (P4,264,211), non-current deferred tax assets (P10,104,969) and deferred tax liability (P20,027,098), as of December 31, 2003 were netted and reclassified to non-current assets (P4,264,851) and non-current liabilities (P9,922,769). The deferred tax assets and liabilities were previously shown among Other Current Assets, Other Non-current Assets and Deferred Tax Liabilities accounts, respectively, in the consolidated balance sheets (see Note 20).
- Reclassification of minimum corporate income tax ("MCIT") to deferred tax assets – The Group reclassified unutilized MCIT to deferred tax assets. MCIT was previously shown among Other Current Assets in the consolidated balance sheets.
- Recognition of final taxes – Final taxes on interest income from bank deposits are recognized as current tax expense in the years the interest income are received. The recognition of final taxes resulted in the amount of interest income being presented at its gross amount and it increased both the interest income and current tax expense by P19,881,593, P21,508,364 and P13,524,744 for the years ended December 31, 2004, 2003 and 2002, respectively (see Note 20).
- Derecognition of deferred tax assets and liabilities – The Group derecognized the balance of the deferred tax assets on various deductible temporary differences outstanding as of January 1, 2004 against their respective allowances and did not recognize deferred tax assets on the certain current year's deductible temporary differences since management believes that the related deferred tax assets may not be recovered.

Leases

On January 1, 2004, the Group adopted the provisions of SFAS 17/IAS 17, *Leases*. Under SFAS 17/IAS 17, lease payments/collections under an operating lease should be recognized as expense/income in the consolidated statement of income on a straight-line basis over the lease term unless another systematic basis is representative of the time pattern of the user's benefits. Retrospective application of SFAS 17/IAS 17 is encouraged but not required. The Group adopted SFAS 17/IAS 17 prospectively and, accordingly, recognized as expense/income the average rent computed on the remaining lease terms. In previous year, the Group recognized rent expense and income equivalent to the annual rental as stipulated in the lease contract. The effects of the Group's adoption of SFAS 17/IAS 17 are discussed in the succeeding paragraphs.

Kita is a lessee to non-cancellable lease covering land and certain leasehold improvements for 25 years, expiring on August 31, 2019. Rent payments on the land are fixed for the first five years of the lease term and are then subject to 100% escalation rate every five years thereafter. Rent payments on the leasehold improvements, on the other hand, are fixed for the first five years and are then subject to 10% escalation rate every year thereafter.

A portion of the land and leasehold improvements leased by Kita were subleased to third parties for two to three years. Some of these sublease agreements provide a 5% escalation rate to the rent payments. Kita's prospective adoption of SFAS 17/IAS 17 resulted in an increase in the rent expense and income by P1,517,691 and P202,608, respectively, in 2004.

For tax purposes, a deferred tax asset or liability is recognized for the difference between the amount of expense or income per lease agreement against the rent expense or income recognized in the financial statements as a result of the adoption of SFAS 17/IAS 17.

Preoperating Expenses

Prior to 2003, SBC capitalized expenses incurred prior to the start of its operations. On January 1, 2003, SBC adopted SFAS 38/IAS 38. Under this new accounting standard,

expenditures on start-up activities or start-up costs, including preopening and preoperating costs, are required to be recognized as expenses when incurred instead of being capitalized and amortized over a specified period.

SBC adopted the benchmark treatment under SFAS 38/IAS 38 and eliminated the balance of preoperating expenses as of December 31, 2002 of P19.9 million as an adjustment to the balance of retained earnings as of January 1, 2003. This change increased net loss and deficit for 2003 by P433,803 and P19,949,150, respectively.

For income tax purposes, preoperating expenses will continue to be amortized over a period of five years from the start of SBC's commercial operations.

4. SEGMENT INFORMATION

The Group's operating businesses are organized and managed separately according to the nature of products and services provided, with each segment representing a strategic business unit that offers different products and serves different markets. Broadband services segment is presently engaged in providing data, transport services, including audio and video, and connectivity through its broadband cable infrastructure. The Manufacturing and Manufacturing Support Services segment is engaged in the business of manufacturing plastic injection molding parts and rendering of after sales service operations as the recognized authorized Service Network for Sony products. Real Estate segment activities include leasing and development and sale of industrial estate. The trading segment is involved in the sale of plastic resins and professional audio/video equipment and peripherals. Lastly,

"Financing and Others" segment is presently engaged in the business of automotive and consumer financing, and credit extension. It is subject to the rules and regulations provided under RA No. 8556. Segment accounting policies are the same as the policies described in Note 2. The Group generally accounts for intersegment sales and transfers as if the sales or transfers were to third parties at current market prices.

The following tables present certain assets and liability information regarding industry segments as of December 31, 2004, 2003 and 2002 and revenue and profit information regarding industry segments for the years then ended (in millions).

	Broadband			Manufacturing and Manufacturing Support Services			Real Estate			Trading			Financing and Others			Eliminations			Consolidated		
	2004	2003	2002	2004	2003	2002	2004	2003	2002	2004	2003	2002	2004	2003	2002	2004	2003	2002	2004	2003	2002
TOTAL REVENUES																					
Sales to external customers	P 181	P164	P271	P 549	P878	P999	P 318	P 93	P109	P 228	P201	P565	P 21	P 4	P 4	P --	P --	P --	P1,297	P1,340	P1,948
Intersegment sales	10	--	--	5	35	28	19	20	17	--	--	--	6	21	22	(40)	(76)	(67)	--	--	--
Total revenues	P 191	P164	P271	P 554	P913	P1,027	P 337	P113	P126	P 228	P201	P565	P 27	P 25	P 26	(P 40)	(P 76)	(P 67)	P1,297	P1,340	P1,948
RESULTS																					
Segment results	(P133)	(P522)	(P 77)	P 48	P 29	(P 40)	P 70	(P 72)	P 11	P 26	P 63	(P 51)	P 154	P 99	P 26	(P 2)	P120	(P 16)	P 163	(P 284)	(P 147)
Finance cost	--	(3)	(6)	--	--	--	--	--	--	--	--	--	(9)	(2)	--	--	1	5	(9)	(4)	(1)
Equity in net income of subsidiaries	--	--	--	--	--	--	--	--	--	--	--	--	10	(372)	(269)	(10)	372	269	--	--	--
Income (loss) from continuing operations before tax and minority interest	(133)	(525)	(83)	48	29	(40)	70	(72)	11	26	63	(51)	155	(275)	(243)	--	--	--	154	(288)	(148)
Tax expense	--	--	--	(12)	(8)	(5)	(12)	(6)	(4)	(1)	(1)	(49)	(21)	(17)	(3)	--	--	--	(46)	(32)	(61)
Income (loss) from continuing operations before minority interest	(133)	(525)	(83)	36	21	(45)	58	(78)	7	25	62	(100)	134	(292)	(246)	--	--	--	108	(320)	(209)
Minority interest	--	--	--	--	--	--	(15)	3	5	--	--	--	--	--	--	--	--	--	(15)	3	5
Income (loss) from continuing operations	(133)	(525)	(83)	36	21	(45)	43	(75)	12	25	62	(100)	134	(292)	(246)	--	--	--	93	(317)	(204)
Income (loss) from discontinuing operations	--	--	--	(5)	18	(43)	--	--	--	--	--	--	--	--	--	--	--	--	(5)	18	(43)
Net income (loss)	(P133)	(P525)	(P 83)	P 31	P 39	(P 88)	P 43	(P 75)	P 12	P 25	P 62	(P100)	P 134	(P 292)	(P 246)	--	--	--	P 88	(P 299)	(P 247)
ASSETS AND LIABILITIES																					
Segment assets	P 826	P 784	P1,232	P 573	P 547	P 613	P3,351	P3,538	P4,309	P 110	P 89	P 283	P2,376	P2,317	P1,677	--	--	--	P7,236	P7,275	P8,114
Investment in subsidiaries	--	--	--	--	--	--	--	117	122	--	--	--	2,413	2,278	3,477	(2,413)	(2,395)	(3,599)	--	--	--
Advances to related parties	109	58	808	--	2	10	573	721	491	5	9	34	1,700	1,575	1,625	(2,309)	(2,139)	(2,753)	78	226	215
Total assets	P 935	P 842	P2,040	P 573	P 549	P 623	P3,924	P4,376	P4,922	P 115	P 98	P 317	P6,489	P6,170	P6,779	--	--	--	P7,314	P7,501	P8,329
Segment liabilities	P 114	P 62	P 139	P 103	P 114	P 103	P 268	P 228	P 254	P 10	P 18	P 56	P 288	P 323	P 54	--	--	--	P 783	P 745	P 606
Advances from related parties	792	1,048	912	698	663	713	813	244	673	32	279	520	71	--	--	(2,309)	(2,139)	(2,753)	97	95	65
Unallocated liabilities	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--	192	260	225
Total liabilities	P 906	P1,110	P1,051	P 801	P 777	P 816	P1,081	P 472	P 927	P 42	P 297	P 576	P 359	P 323	P 54	--	--	--	P1,072	P1,100	P 896
OTHER SEGMENT INFORMATION																					
Capital expenditures	P 98	P 20	P 71	P 19	P 34	P 26	P 13	P 24	P 25	P 1	P 2	P 1	P --	P --	P --	--	--	--	P 131	P 80	P 123
Depreciation and amortization	90	108	113	20	32	28	19	17	21	1	2	2	1	1	2	20	--	134	P 151	P 160	P 300
Impairment losses	10	350	--	--	--	35	12	--	--	--	--	--	--	--	--	--	--	--	22	350	35
Other non-cash expenses	--	--	3	3	--	44	--	--	7	1	11	--	2	1	--	--	--	--	6	12	54

5. CASH AND CASH EQUIVALENTS

Cash and cash equivalents were as follows as of December 31:

	2004	2003
Cash on hand and in banks	P 174,357,648	P 151,208,847
Short-term placements	1,444,855,925	1,397,167,697
	P 1,619,213,573	P 1,548,376,544

Cash accounts with the banks generally earn interest at rates based on daily bank deposit rates. Short-term placements are made for varying periods of between 30 to 60 days and earn interest at the respective short-term placement rates ranging from 1.84% to 10% per annum in 2004 and 4.2% to 8.5% per annum in 2003.

6. SHORT-TERM INVESTMENTS

Short-term investments pertain to investments in fixed income dollar and euro bonds. These bonds earn interest at the respective coupon rates ranging from 6.875% to 14.5% per annum in 2004. A portion of the short-term investments are used as collateral against bank loans (see Note 14).

7. TRADE AND OTHER RECEIVABLES

This account included the following:

	2004	2003
Trade (see Notes 21 and 25)	P 373,917,620	P 533,654,034
Finance receivables – current (see Notes 13 and 21)	9,487,976	57,289,222
Others	88,918,230	68,983,770
	472,323,826	659,927,026
Allowance for doubtful accounts (see Note 27)	(116,482,969)	(95,183,643)
	P 355,840,857	P 564,743,383

As of December 31, 2004, other receivables include receivables from an insurance company representing SLC's claims for the value of inventories and property and equipment that were destroyed during a fire in December 2004 (See Note 12).

Interest rates on finance receivables range from 9% to 29% per annum in 2004 and 9% to 44% per annum in 2003. Certain business loans of SMFI are secured by shares of stock of companies which availed of such loans. Such shares of stock are owned by a related party.

8. INVENTORIES

The details of inventories are shown below:

	2004	2003
At net realizable value:		
Finished goods	P 20,609,657	P 4,400,050
Work in process	1,777,253	1,741,391
Raw materials	23,141,696	5,193,964
Supplies and others (see Note 21)	248,685	7,502,456
	45,777,291	18,837,861
At cost:		
Finished goods	4,754,279	6,118,247
Work in process	321,492	2,315,784
Raw materials	-	13,025,501
Supplies and others (see Note 21)	69,584,986	7,325,236
	74,660,757	28,784,768
	P 120,438,048	P 47,622,629

9. LAND AND DEVELOPMENT COSTS

Under its registration with the Board of Investments ("BOI"), Starworld shall develop 118 hectares of land. As of October 31, 2004, lot areas totaling 65 hectares were already acquired and developed while 18 hectares of land already acquired are still under development.

10. OTHER CURRENT ASSETS

The composition of this account as of December 31 is shown below:

	2004	2003
Creditable withholding taxes	P 42,141,317	P 42,757,621
Input value-added tax	22,574,363	28,784,573
Prepaid expenses	13,670,667	15,175,438
Others	4,229,713	5,164,487
	P 82,616,060	P 91,882,119

11. INVESTMENTS AND ADVANCES

The details of this account are shown below:

	2004	2003
Investment in SPH, a 33% owned associate – at equity (See Note 1)		
Acquisition cost		
Beginning balance	P 35,000,000	P 35,000,000
Return of investment	(26,730,000)	-
Reclassification to other non-current assets	(8,270,000)	-
	-	35,000,000
Accumulated equity in net losses		
Beginning balance	(35,000,000)	(35,000,000)
Return of investment	26,730,000	-
Reclassification to other non-current assets	8,270,000	-
	-	(35,000,000)
Advances to related parties (see Note 21)	78,384,763	226,063,238
	P 78,384,763	P 226,063,238

12. PROPERTY, PLANT AND EQUIPMENT

A reconciliation of the carrying amounts at the beginning and end of 2004 and the gross carrying amounts and the accumulated depreciation, amortization and impairment losses of property, plant and equipment are shown below:

	Land	Buildings and Improvements	Machinery and Equipment	Furniture, Fixtures and Office Equipment	Transportation Equipment	Cable System Equipment
Balance at January 1, 2004 net of accumulated depreciation, amortization and impairment losses	P 2,341,862,549	P 476,224,432	P 107,803,560	P 23,099,599	P 15,516,031	P 398,702,396
Property and equipment from Data Division of DCI (see Note 1)	-	-	-	402,977	1,360,735	29,898,373
Additions	54,475,718	899,538	3,108,472	5,317,208	6,965,519	40,351,335
Reclassifications	-	58,709,250	(58,709,250)	(1,345,960)	2,523,678	(424,608)
Reversal of impairment loss	-	16,807,098	-	-	-	-
Depreciation and amortization charges for the year	-	(38,881,261)	(9,741,383)	(6,089,737)	(6,996,005)	(71,560,369)
Balance at December 31, 2004 net of accumulated depreciation, amortization and impairment losses	P 2,396,338,267	P 513,759,057	P 30,770,746	P 20,988,699	P 19,002,913	P 396,967,127
January 1, 2004 Cost	P 2,341,862,549	P 895,761,077	P 323,430,892	P 169,170,320	P 88,758,960	P 987,675,573
Accumulated depreciation and amortization	-	(387,988,930)	(202,151,248)	(145,299,399)	(73,242,929)	(238,973,177)
Accumulated impairment loss	-	(31,547,715)	13,476,084	771,322	-	(350,000,000)
Net carrying amount	P 2,341,862,549	P 476,224,432	P 107,803,560	P 23,099,599	P 15,516,031	P 398,702,396
December 31, 2004 Cost	P 2,396,338,267	P 927,255,335	P 123,681,952	P 131,643,154	P 88,956,675	P 1,054,010,326
Accumulated depreciation and amortization	-	(413,276,913)	(92,911,206)	(110,654,455)	(69,953,762)	(307,043,199)
Accumulated impairment loss	-	(219,365)	-	-	-	(350,000,000)
Net carrying amount	P 2,396,338,267	P 513,759,057	P 30,770,746	P 20,988,699	P 19,002,913	P 396,967,127

(cont.)

	Test, Communication and Other Equipment	Computer System	Leasehold Improvements	Tools and Equipment	Construction in progress	Total
Balance at January 1, 2004 net of accumulated depreciation, amortization and impairment losses	P 55,491,678	P 9,768,916	P 7,836,842	P 328,095	P 581,298	P 3,437,215,396
Property and equipment from Data Division of DCI (see Note 1)	2,693,927	1,085,775	2,394,437	-	-	37,836,224
Additions	2,807,337	1,540,432	1,852,986	957,028	13,231,089	131,506,662
Reclassifications	(20,615)	-	(732,495)	-	-	-
Reversal of impairment loss	-	-	-	-	-	16,807,098
Depreciation and amortization charges for the year	(9,480,736)	(5,859,053)	(1,979,355)	(822,936)	-	(151,410,835)
Balance at December 31, 2004 net of accumulated depreciation, amortization and impairment losses	P 51,491,591	P 6,536,070	P 9,372,415	P 387,392	P 13,812,387	P 3,459,426,664
January 1, 2004 Cost	P 94,274,177	P 61,950,683	P 72,787,311	P 14,842,983	P 581,298	P 5,051,095,823
Accumulated depreciation and amortization	(38,782,499)	(52,181,767)	(64,950,469)	(13,867,550)	-	(1,217,437,968)
Accumulated impairment loss	-	-	-	(647,338)	-	(396,442,459)
Net carrying amount	P 55,491,678	P 9,768,916	P 7,836,842	P 328,095	P 581,298	P 3,437,215,396
December 31, 2004 Cost	P 99,079,928	P 64,576,890	P 36,638,604	P 12,561,693	P 13,812,387	P 4,948,555,211
Accumulated depreciation and amortization	(47,588,337)	(58,040,820)	(27,266,189)	(12,174,301)	-	(1,138,909,182)
Accumulated impairment loss	-	-	-	-	-	(350,219,365)
Net carrying amount	P 51,491,591	P 6,536,070	P 9,372,415	P 387,392	P 13,812,387	P 3,459,426,664

The balance of Property, Plant and Equipment as of January 1, 2004 has been restated from the amount previously reported due to reclassification of impairment loss amounting to P35 million. The impairment loss was recognized in 2002 for the property, plant and equipment of the discontinued operations of SLC which was presented under Other Non-current Assets.

As a result of the closure of Kita's consumer electronics manufacturing division in 2001, Kita wrote down the carrying amounts of related property, plant and equipment and inventories to net realizable values. The write-down for property, plant and equipment and inventories was charged to impairment loss for the year. However, in 2004, Kita partially reversed the impairment loss on buildings amounting to P16,807,098 due to increase in its recoverable amount resulting from the income generated by the asset through various lease agreements entered into with third parties. The recoverable amount in 2004 was based on value in use and was determined by discounting the net cash flows attributable to the lease agreements at a nominal rate of 12% on a pre-tax basis. Impairment losses previously recognized, which were written off against the cost of the related property, plant and equipment, amounted to P24,892,244 (consisting of P9,997,500 against the cost of building and improvements, P13,476,084 against machinery and equipment, P771,322 against furniture, fixture and office equipment and P647,338 against tools and equipment).

In 2004, DI acquired the Data Division of DCI. The property and equipment of the acquired division amounted to P37,836,224. In 2003, DI recognized impairment losses of P350 million representing the write-down of its cable system equipment to recoverable amount which was based on value in use and was determined at the cash-generating unit level. The cash-generating unit consists of the assets of the Group relating to the broadband segment. In determining value in use for the cash-generating unit, the cash flows were discounted at a nominal rate of 10.7% on a pre-tax basis.

Certain parcels of land of SC are being subject to expropriation coverage under agrarian reform and claims by third parties. Also, certain land properties of SMC are the subject of litigation and claim by third parties (see Note 27).

In December 2004, portion of SLC's office and warehouse located in Bicutan, Parañaque was destroyed by fire. The cost and corresponding accumulated depreciation of those assets amounted to P 13,627,503 and P 11,265,345, respectively. The net book value of the affected assets is included in the claims made from the insurance company (See Note 7).

Depreciation expense charged to cost of goods sold and cost of services amounted to P120,425,146 in 2004, P142,368,317 in 2003 and P234,573,354 in 2002 (see Note 17).

13. OTHER NON-CURRENT ASSETS

The composition of this account as of December 31 is shown below:

	2004	2003
Investment in cash surrender value of life insurance	P 230,750,766	P 224,975,892
Finance receivables – net of current portion (see Notes 7 and 21)	194,521,262	138,241,429
Receivables from sale of land-net cost of current portion	75,224,938	-
Investment in shares of stock – at cost (net of impairment losses of P22,481,001 in 2004)	25,987,882	53,735,682
Miscellaneous deposits	14,136,918	-
Prepaid insurance (See note below)	11,813,554	13,203,381
Others - net	18,637,708	44,192,064
	P 571,073,028	P 474,348,448

In July 2003, BRL purchased life insurance policies for its directors. The beneficiary of the insurance policies is SGI and the investment is accounted for under the Cash Surrender Value method. Total insurance premiums paid amounted to P231,638,266 (US\$4,237,027). The initial cash surrender value, amounting to US\$3,982,806 with a peso equivalent of P214,734,226, was determined and recognized immediately at the time of payment. The difference of P13,898,297 (US\$254,222) between the total premiums paid and the initial cash surrender value represented insurance service fees which was taken up as Prepaid Insurance to be amortized over 10 years. Service fees for the period ended December 31, 2004 amounted to P1,429,599 (US\$25,422) and is presented as part of Other Operating Expenses account in the 2004 consolidated statement of income. Increases in the cash surrender value of the insurance policies amounting to P3,075,972 (US\$54,668) in 2004 and P3,399,385 (US\$63,524) in 2003 are shown as part of Other Income account in the consolidated statements of income.

In December 2002, SLC's manufacturing operations of Sony products was discontinued. As a result, property, plant, and equipment relating to discontinued operation, amounting to P13,042,541 as of December 31, 2004 and P16,015,442 as of December 31, 2003, are presented as part of the Other Non-Current Assets account (See Note 1).

In 2004, DI, Starworld and SMC recognized impairment losses of P9,679,375, P5,220,000, and P7,581,637, respectively, on the value of their investment in shares of stock and club shares which are carried at cost to reduce them to their recoverable amount. The recoverable amounts are based on net selling price as indicated by prevailing market prices as of the balance sheet date.

In 2004, Kita recognized an impairment loss of P1,984,445 on the value of leasehold rights related to its assumption of the lease contract as an affiliate with Clark development Corporation which reduced the value of the leasehold right to its recoverable amount. The recoverable amount is based on value in use determined by discontinuing the cash flow projections at a nominal rate of 12% on a pre-tax basis.

14. INTEREST-BEARING LOANS

This account pertains to loans obtained by BRL from ING Private Bank which are secured by a portion of the BRL's short term investments (see Note 6). In 2004 and 2003, the loans bear interest at prevailing market rates ranging from 2.83% to 3.71% per annum. These loans will mature in 2005.

15. TRADE AND OTHER PAYABLES

This account consists of:

	2004	2003
Trade	P 152,056,231	P 195,474,939
Accrued expenses (see Note 19)	71,074,145	18,221,255
Refundable deposits	20,631,674	29,376,553
Provisions for warranty (see Notes 25 and 26)	2,149,723	1,259,475
Output value-added tax	1,846,517	5,470,142
Others (see Note 1)	159,852,916	151,861,074
	P 407,611,206	P 401,663,438

A provision is recognized for expected warranty claims on products sold during the year, based on the Group's past experience of the level of repairs and returns. SVC and OLC accrue warranty costs for products they sell to customers. In addition, OLC is engaged by another company to conduct repairs of consumer electronics sold by the said company. In 2004 and 2003, based on current sales level and current information on warranty claims experience, SVC reversed to income about P372 thousand and P8.1 million of the provision for product warranty, respectively. The amount reversed is shown as part of Other Revenues in the consolidated statements of income. Meanwhile, OLC expects that a significant portion of its provision will be incurred in 2005.

16. EQUITY

Capital Stock and Additional Paid-in Capital

The movement in the Company's stockholders' equity is as follows:

	2004	2003	2002
Capital stock – P1 par value per share			
Authorized – 5,000,000,000 shares			
Issued and outstanding 2,030,975,000 shares	P 2,255,436,752	P 2,030,975,000	P 2,030,975,000
Pooling of interest adjustment	-	-	100,000,000
Issuances for the acquisition of DI	-	224,461,752	-
Effects of revaluation of DI's net assets (see Note 1)	(224,461,752)	-	-
Balance at end of year	P 2,030,975,000	P 2,255,436,752	P 2,130,975,000
Additional paid-in capital			
Balance at beginning of year	P 4,664,902,932	P 4,589,076,596	P 4,589,076,596

Pro-forma adjustment for the pooling of interest accounting of the acquisition of DI	-	75,826,336	932,064,077
Effects of re-valuation of net assets of DI (see Note 1)	(23,201,010)	-	-
Balance at end of year	P 4,641,701,922	P 4,664,902,932	P 5,521,140,673

In 2003, the Company recognized the constructive issuance of 224,461,752 of the Company's shares of stocks to DCI for the acquisition of DI pending the approval of the Philippine Stock Exchange ("PSE") and the Commission. In 2004, the Company and DCI agreed to exclude receivable and payable accounts of certain related parties from the net asset valuation for the acquisition of DI. The re-valuation changed DI's financial position from net assets to net liability. Consequently, the Company and DCI agreed that the 224,461,752 shares of stock would no longer be issued to DCI. Instead, the Company would assume the net liability of DI representing the excess of the estimated fair value of DI's broadband cable infrastructure and its existing cable internet subscriber base over their aggregate book value. The change on the acquisition value for DI resulted in the reversal of the capital stock issuance recognized in the previous year and the decrease in additional paid-in capital recorded for the acquisition of DI (see Note 1).

Retained Earnings (Deficit)

Retained earnings corresponding to the cost of treasury shares amounting to P115.6 million as of December 31, 2004, 2003 and 2002 are not available for dividend declaration.

Undistributed earnings of subsidiaries amounting to P751 million in 2004 and P764.8 million in 2003 and P679.9 million in 2002 are not currently available for dividend declaration.

17. COST OF GOODS SOLD AND COST OF SERVICES

The details of these accounts are shown below:

	2004	2003	2002
Cost of goods sold:			
Finished goods at beginning of year	P 10,518,297	P 51,106,835	P 357,875,784
Cost of goods manufactured:			
Raw materials at beginning of year	18,219,465	4,159,203	685,883,668
Work-in-process at beginning of year	4,057,175	5,349,900	22,732,075
Net purchases during the year (see Note 21)	493,686,091	673,677,705	90,127,099
Direct labor (see Note 19)	24,036,399	23,832,178	55,894,363
Manufacturing overhead (see Note 12)	95,305,752	48,806,787	65,989,237
Raw materials at end of year	(23,141,696)	(18,219,465)	(4,159,203)
Work-in-process at end of year	(2,098,745)	(4,057,175)	(5,349,900)
	610,064,441	733,549,133	911,117,339
Finished goods at end of year	(25,363,936)	(10,518,297)	(51,106,835)
	P 595,218,802	P 774,137,671	P1,217,886,288
Cost of services:			
Direct costs			
Rental (see Note 3)	P 109,377,807	P 71,566,331	P 75,078,734
Depreciation and amortization (see Note 12)	108,467,221	130,408,177	133,624,358
Salaries and employees' benefits (see Note 19)	107,840,286	128,009,645	103,258,946
Materials, supplies and facilities	102,050,378	76,962,416	64,620,983
Outside services	46,075,533	26,108,533	24,117,373
Repairs and maintenance	15,652,048	20,450,582	6,294,513
Transportation and travel	9,777,753	8,552,875	8,253,921
Others	25,571,990	46,929,140	45,493,657
	P 524,813,016	P 508,987,699	P 460,742,485

18. OPERATING EXPENSES

This account consists of the following:

	2004	2003	2002
Salaries and employees' benefits (see Note 19)	P 108,208,078	P 108,326,833	P 123,366,841
Depreciation and amortization	30,985,689	18,090,375	65,297,401
Property, maintenance, utilities and insurance	29,118,350	40,646,060	36,004,181
Taxes and licenses	27,478,666	24,372,976	32,578,480
Transportation and travel	13,720,057	9,210,555	10,953,303
Doubtful accounts (see Note 27)	6,936,005	11,292,231	11,478,793
Outside services	4,594,348	20,685,658	19,866,846
Advertising and promotions	1,884,043	1,267,594	52,326,995
Inventory losses	-	-	16,379,564
Others (see Notes 1, 13 and 27)	69,658,644	63,612,954	93,618,643
	P 292,583,880	P 297,505,236	P 461,871,047

19. EMPLOYEE BENEFITS

The Group maintains a tax-qualified, non-contributory multi-employer retirement plan that is being administered by a trustee covering all regular full time employees. The benefits are based on years of service and the latest compensation of employees. Total retirement benefit expense shown as part of the appropriate accounts in the consolidated statements of income amounted to P11,642,551 in 2004 and P10,069,958 in 2003 and P18,611,223 in 2002 (see Notes 17 and 18). Accrued retirement costs as of December 31, 2004 and 2003 amounted to P11,642,551 and P10,069,358, respectively, and are shown as part of Trade and Other Payables account in the consolidated balance sheets (see Note 15).

Based on the latest actuarial valuation report as of December 31, 2004, the consolidated actuarial present value of pension benefits and fund assets amounted to P92,546,087 and P99,598,243, respectively. The principal actuarial assumptions used to determine retirement benefits were discount rate and return on plan assets of 8%, and salary increase of 10%. Actuarial valuations are made every two years to update the retirement benefit costs and the amount of contributions.

The annual contribution to the retirement plan covers the current service cost and the amortization of the past service cost.

20. INCOME TAXES

Kita is duly registered with Clark Development Corporation while SMC and Starworld are PEZA registered which entitle them to tax and duty free importation of goods, and exemption from national and local taxes (see Notes 23 and 24).

The major components of tax expense for the years ended December 31 are as follows:

	2004	2003	2002
Consolidated statements of income:			
Current tax expense:			
Final tax at 20% (see Note 3)	P 19,028,226	P 21,133,824	P 12,452,513
Regular corporate tax at 32%	16,646,663	18,846,014	36,304,324
Preferential taxes at 5% (see Notes 23 and 24)	3,891,616	789,192	148,881
Final tax at 7.5% (see Note 3)	853,367	374,540	1,072,231
MCIT at 2%	834,439	1,876,633	2,978,251
	41,254,311	43,020,203	52,956,200
Deferred tax expense relating to origination and reversal of temporary differences	6,653,954	13,247,890	8,229,667
Benefit from previously unrecognized deferred tax assets	(1,751,547)	(23,765,618)	-
	4,902,407	(10,517,728)	8,229,667
Tax expense reported in consolidated statements of income	P 46,156,718	P 32,502,475	P 61,185,867

The reconciliation of tax on pretax income computed at the applicable statutory rate to tax expense attributable to continuing operations is as follows:

	2004	2003	2002
Tax on pre-tax income (loss) at 32%	P 49,442,072	(P 92,051,079)	(P 47,260,825)
Adjustment for income subject to lower tax rates			
At 20%	(11,416,936)	(12,680,294)	(7,471,508)
At 7.5%	(2,787,665)	(1,223,497)	(3,502,621)
At 5%	(21,014,726)	(4,261,633)	(803,957)
Tax effects of:			
Derecognized deductible temporary differences	45,879,944	4,184,447	33,521,406
Non-deductible expenses	24,073,604	4,676,318	13,437,103
Amortization of goodwill attributable to property, plant and equipment	6,496,321	-	43,198,442
Unrecognized deferred tax asset	6,213,520	185,420,116	64,631,463
Dividend income	(5,967)	(3,551)	(17,433)
Reversal of allowance for doubtful accounts	(181,572)	(16,564,445)	-
Non-taxable income	(201,419)	-	-
Intercompany income and expenses eliminated during consolidation	(2,395,290)	(28,925,542)	(37,693,778)
Negative goodwill	(6,175,491)	-	-
Interest income exempted from tax	(6,543,154)	(1,639,348)	-
Gain from return of investment	(8,553,600)	-	-
Income of foreign subsidiary not subject to taxes	(11,487,234)	(4,311,233)	-
Benefit from previously unrecognized deferred tax assets	(13,203,341)	(1,330,042)	-
Write-off of inventory	-	204,894	-
Net income of a subsidiary under income tax holiday	-	-	7,427,572
Others	(1,982,348)	1,027,364	(4,279,997)
Tax expense reported in consolidated statements of income	46,156,718	32,502,475	61,185,867

The net deferred tax assets of subsidiaries which have a net deferred tax asset position as of December 31 related to the following:

	Consolidated Balance Sheets		Consolidated Statements of Income	
	2004	2003	2004	2003
Deferred tax assets:				
Accrued retirement benefits	P 1,712,296	P 1,905,060	P 192,764	(P 777,462)
Allowance for doubtful accounts	1,568,726	1,600,355	31,629	(767,414)
Advance rental costs	420,826	-	(420,826)	-
Unamortized past service costs	377,590	439,436	61,846	34,897
Allowance for inventory losses	320,000	320,000	-	(320,000)
Benefit from previously unrecognized MCIT	-	-	(21,789)	-
Deferred Tax Income	P 4,399,438	P 4,264,851	(P 156,376)	(P 1,829,979)
Net Deferred Tax Assets	P 4,399,438	P 4,264,851	(P 156,376)	(P 1,829,979)

The net deferred tax liabilities of subsidiaries which have a net deferred tax liability position as of December 31 related to the following:

	Consolidated Balance Sheets		Consolidated Statements of Income	
	2004	2003	2004	2003
Deferred tax assets:				
NOLCO	P 5,275,176	P 7,403,418	P 2,128,242	(P 6,159,320)
Unamortized past service costs	2,006,589	1,107,096	(899,493)	(58,803)
MCIT	145,329	145,329	-	(145,329)
Advance rental	-	1,507,825	1,507,825	1,308,144
Accrued retirement benefits	-	693,484	693,484	(125,534)
Allowance for doubtful accounts	-	509,794	509,794	(20,778)
Others	-	-	-	(1,315,618)
Deferred tax liabilities:				
Unrealized foreign exchange gain	(21,269,694)	(20,045,617)	1,224,077	230,000
Rent receivable	(1,193,814)	-	1,193,814	-
Others	-	(1,244,098)	(1,244,098)	-
Benefit from previously unrecognized MCIT	-	-	(54,862)	(4,474,662)
Deferred Tax Expense (Income)	(P 15,036,414)	(P 9,922,769)	P 5,058,783	(P 8,687,749)
Net Deferred Tax Liabilities	(P 15,036,414)	(P 9,922,769)	P 5,058,783	(P 8,687,749)

The movements in the Group's recognized and unrecognized NOLCO and MCIT are as follows:

Year	Original Amount	Applied in Previous Year	Applied in Current Year	Expired Balance	Remaining Balance	Valid Until
NOLCO:						
2004	P 141,433,982	P -	P -	P -	P 141,433,982	2007
2003	327,646,393	-	8,027,351	-	319,619,042	2006
2002	171,858,443	257,598	289,062	-	171,311,783	2005
2001	180,547,759	1,532,090	375,019	178,640,650	-	2004
2000	102,726,616	5,460,560	-	97,266,056	-	2003
1999	83,509,353	-	-	83,509,353	-	2002
	P 1,007,722,546	P 7,250,248	P 8,691,432	P 359,416,059	P 632,364,807	
MCIT:						
2004	P 834,439	P -	P -	P -	P 834,439	2007
2003	1,876,633	-	-	-	1,876,633	2006
2002	2,978,251	233,088	495,279	-	2,249,884	2005
2001	5,458,448	1,284,953	16,384	4,157,111	-	2004
2000	2,351,010	1,455,272	-	895,738	-	2003
1999	7,342,396	-	-	7,342,396	-	2002
	P 20,841,177	P 2,973,313	P 511,663	P 12,395,245	P 4,960,956	

The NOLCO, MCIT and other deductible temporary differences as of the end of 2004 for which the related deferred tax assets have not been recognized are shown below:

	<u>Amount</u>	<u>Tax Effect</u>
NOLCO	P 615,879,882	P 197,081,562
Impairment loss	428,475,363	137,112,116
Allowance for doubtful accounts	78,972,859	25,271,315
Preoperating expenses	36,071,704	11,542,945
Accrued retirement benefits	11,191,378	3,581,241
MCIT	4,815,627	4,815,627
Advance rental	2,750,138	880,044
Provisions for inventory losses	1,378,347	441,071
Provisions for warranty	1,004,016	321,285
Unamortized past service cost	983,238	314,636
Allowance for prepaid advertising	660,163	211,252
Others	399,475	127,832
	<u>P 1,182,582,190</u>	<u>P 381,700,926</u>

21. RELATED PARTY TRANSACTIONS

The significant transactions of the Group in the normal course of business with related parties are described below:

- SEC purchases parts and supplies from a company owned by the ultimate majority stockholders (see Note 8). Total purchases amounted to P69.7 million in 2004, P69.0 million in 2003, and P57.8 million in 2002, and are presented as part of Cost of Goods Sold in the consolidated statements of income (see Note 17). There are no outstanding liabilities arising from these transactions.
- SMFI grants interest-bearing business and other loans to its related parties. Interest rates for these loans range from 9% to 12%. In 2004 and 2003, total loans granted to related parties amounted to P54,294,650 and P53,196,000, respectively. Outstanding receivables arising from these loans, which are presented as part of Trade and Other Receivables and Other Non-current Assets accounts in the consolidated balance sheets (see Notes 7 and 13) amounted to P23,891,526 and P11,319,521 as of December 31, 2004 and 2003, respectively. Outstanding receivables are further broken down as follows:

	<u>2004</u>	<u>2003</u>
Business loans:		
Avid Sales Corporation	P 20,254,000	P 10,561,498
Car loans:		
TCL Sun, Inc.	3,637,526	758,023
	<u>P 23,891,526</u>	<u>P 11,319,521</u>

Certain business loans are secured by shares of stocks of companies which availed of such loans. Such shares of stock are owned by a related party.

- SVC earns commission from sales of a company owned by the ultimate majority stockholders, to customers in the Philippines. Commission revenue amounted to P1.4 million in 2004, P14.3 million in 2003 and P12.3 million in 2002, and are presented as part of Revenues from Rendering of Services in the consolidated statements of income. Outstanding receivables arising from these transactions as of December 31, 2004 and 2003 amounted to P55.2 million and P58.4 million, respectively, and are presented under Trade and Other Receivables account in the consolidated balance sheets (see Note 7).
- SVC sells professional equipment, accessories and tapes to Avid Sales Corporation, a related party. Total sales amounted to P18.3 million in 2004, P17.4 million in 2003 and P13.2 million in 2002, and are presented as part of Revenue from Sale of Goods account in the consolidated statements of income. Outstanding receivables arising from this transaction amounted to P953,623 and P3,634,200 as of December 31, 2004 and 2003, respectively, and are included in Trade and Other Receivables account in the consolidated balance sheets (see Note 7).

- The group obtains advances for working capital requirements from the ultimate majority stockholders and other companies owned by the ultimate majority stockholders. Outstanding liabilities arising from these transactions are presented as Advances from Related Parties account in the consolidated balance sheets.

22. EARNINGS PER SHARE

Basic earnings per share were computed as follows:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Net income (loss) (a):			
Continuing operations	P 93,257,230	(P 316,816,731)	(P 204,412,107)
Discontinuing operations	(5,020,074)	18,272,968	(42,990,045)
	<u>P 88,237,156</u>	<u>(P 298,543,763)</u>	<u>(P 247,402,152)</u>
Weighted average shares outstanding (b)	<u>2,030,975,000</u>	<u>2,046,003,752</u>	<u>1,923,642,000</u>
Earnings (loss) per share (a/b):			
Continuing operations	P 0.04	(P 0.15)	(P 0.11)
Discontinuing operations	(0.00)	0.01	(0.02)
	<u>P 0.04</u>	<u>(P 0.14)</u>	<u>(P 0.13)</u>

23. REGISTRATION WITH CLARK DEVELOPMENT CORPORATION ("CDC")

Kita is registered with the CDC under the Bases Conversion and Development Act of 1992 as a Clark Special Economic Zone ("CSEZ") enterprise primarily engaged in the business of manufacturing consumer electronic products. As a registered CSEZ enterprise, Kita is entitled to tax and duty free importation of raw materials, equipment, household and personal items, and is exempted from national and local taxes. In lieu of all these taxes, Kita is subject to 5% preferential tax rate. In addition, the 32% regular corporate income tax rate is applied to those income which come from sources other than the Kita's registered activities.

24. REGISTRATION WITH PHILIPPINE ECONOMIC DEVELOPMENT AUTHORITY ("PEZA")

SMC is registered with the PEZA as an Ecozone Facilities Enterprise at the Laguna International Industrial Park – Special Economic Zone ("LIIP – SEZ"). As an Ecozone Facilities Enterprise, SMC shall lease its building in LIIP – SEZ to PEZA-registered export enterprises located therein. SMC is subject to 5% tax on gross income earned on such facilities in lieu of all national and local taxes.

On July 1, 1998, the PEZA approved Starworld's registration as an Ecozone developer/operator of the CPIP – Special Economic Zone located at Bo. Parian, Calamba City. Under the terms of the registration and subject to certain requirements, Starworld shall be exempt from all national and local taxes and instead will be subject to the 5% preferential tax rate on gross income after allowable deductions.

25. MEMORANDUM OF UNDERSTANDING WITH SONY PHILIPPINES, INC.

In July 1, 2003, SEC entered into a Memorandum of Understanding ("MOU") with SPH for Network Support for AIWA products. Under the MOU, SPH authorized the Company to perform in-warranty and out-of-warranty services to customers in the Philippines for a fee calculated as a percentage of SPH's annual sales.

In-warranty services shall be rendered free of charge to customers. The actual cost of replacement parts related to in-warranty services shall be shouldered by SPH. Also, SPH agrees to pay SEC network support fee equal to 1% of net sales of P150,000 per month whichever is higher. This MOU covered the period from July 1, 2003 to September 30, 2004. In October 1, 2004, the Company and SPH renewed the MOU with a new term from October 1, 2004 to May 1, 2005.

Network support fees earned amounted to P1,550,000 in 2004 and P750,000 in 2003 and are presented as part of Revenues from Rendering of Services in the consolidated statements of income. As of December 31, 2004 and 2003, outstanding receivables arising from this transaction amounted to P193,402 and P460,656, respectively, and are included in the Trade and Other Receivables account in the consolidated balance sheets (see Note 7).

26. DISTRIBUTORSHIP AGREEMENT WITH SONY CORPORATION

SVC has a non-exclusive Distributorship Agreement (the "Agreement") with Sony Corporation of Hong Kong Limited ("Sony HK"), a corporation organized and existing under and by virtue of the laws of Hong Kong. Under the Agreement, SVC was designated by Sony HK as its non-exclusive distributor of Sony products in the Philippines. In addition, SVC shall provide the customers in the Philippines with repair and parts replacement services, including but not limited to repair and parts replacement services rendered by SVC which are under the 12 month warranty period at its own costs and expenses. The Agreement is good for one year and renewable for another year upon mutual agreement between SVC and Sony HK.

27. COMMITMENTS AND CONTINGENCIES

The following are the significant commitments and contingencies involving the Group:

Operating Lease Commitments – Company as Lessor

Certain subsidiaries leases various properties for a period of 1 to 10 years. Some of these lease transactions are subject to 5% to 10% escalation rate. The future minimum rentals receivable under these non-cancellable operating leases as of December 31 are as follows:

	2004	2003
Within one year	P 65,823,711	P 64,833,561
After one year but not more than five years	185,689,511	191,573,985
More than five years	36,113,907	65,507,976
	P 287,627,129	P 321,915,522

Rental income from these transactions amount to P110,354,171, P108,066,361 and P93,702,143 in 2004, 2003 and 2002, respectively, and forms part of the Rent account in the consolidated statements of income.

Operating Lease Commitments – Company as Lessee

Kita is a lessee to non-cancellable operating leases covering its land and certain leasehold improvements. As of December 31, 2004, these leases have a remaining term of 14 years, expiring in 2019. Lease payments are fixed for the first five years. Thereafter, the lease on land is subject to 100% escalation rate every five years while the lease on land improvements is subject to an annual escalation rate of 10%. The future minimum rentals payable under these non-cancellable operating leases as of December 31 are as follows:

	2004	2003
Within one year	P 3,880,509	P 3,163,190
After one year but not more than five years	18,025,984	16,701,803
More than five years	76,738,689	81,943,379
	P 98,645,182	P 101,808,372

Total rent expense from these operating leases amounted to P5,072,655 and P1,035,791 and P964,035 in 2004, 2003 and 2002, respectively, and are shown as part of Others under Operating Expenses account in the consolidated statements of income (see Note 18)

Legal Claims

Certain subsidiaries are involved in litigations, which arose in the normal course of business. These include, among others, the following:

- SC is involved in a litigation with a local bank concerning letters of credit issued in connection with shipments of electronic parts to SC and parcels of land that are being subject to expropriation coverage under agrarian reform and claims by third parties. Management believes that the ultimate liability or loss, if any, with respect to such litigation will not materially affect the financial position and results of operations of SC.
- As of December 31, 2004, there are claims by a third party against SLC for alleged infringement of copyrights and sound recording. Management believes that the outcome of such lawsuit will not materially affect SLC's financial position and results of operations.

c. SMC is involved in a number of litigations and is subject to certain claims such as:

- Portion of land in Pililla, Rizal, with a carrying value of P3.5 million, subject to expropriation coverage under agrarian reform.
- Land, with a carrying value of P59 million, subject to claims by third parties who filed court cases against the Company.

Management believes that the ultimate liability or loss from the above contingencies, if any, with respect to such litigations will not materially affect the financial position and results of operation of the Group.

Others

The Philippine continues to experience economic difficulties relating to currency fluctuations, volatile stock markets and slowdown in growth. Management is of the opinion that losses, if any, from these events and conditions will not have material effects on the Group's financial statements.

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