PHILIPPINE LONG DISTANCE TELEPHONE CO
Form 20-F
June 24, 2004

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 20-F

[ ] REGISTRATION STATEMENT PURSUANT TO SECTION 12(B) OF THE SECURITIES EXCHANGE ACT OF 1934

OR

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 For the fiscal year ended December 31, 2003

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 For the transition period from _________ to _________

Commission file number 1-03006

Philippine Long Distance Telephone Company

(Exact name of Registrant as specified in its charter)

Republic of the Philippines

(Jurisdiction of incorporation or organization)

Ramon Cojuangco Building

Makati Avenue

Makati City, Philippines

(Address of principal executive or organization)

Securities registered or to be registered pursuant to Section 12(b) of the Act.

Title of each class	Name of each exchange on which registered
Common Capital Stock, Par Value Five Philippine Pesos Per Share	New York Stock Exchange*
American Depositary Shares, evidenced by American Depositary Receipts, each representing one share of Common Capital Stock	New York Stock Exchange Pacific Exchange
Series III Convertible Preferred Stock, Par Value Ten Philippine Pesos Per Share	New York Stock Exchange*
Global Depositary Shares, evidenced by Global Depositary Receipts, each representing one share of Series III Convertible Preferred Stock	New York Stock Exchange

** Registered on the New York Stock Exchange not for trading but only in connection with the registration of American Depositary Shares or Global Depositary Shares, as the case may be, pursuant to the requirements of such stock exchange.*

Securities registered or to be registered pursuant to Section 12(g) of the Act.

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act.

10.625% Notes due 2004	10.625% Notes due 2007
9.875% Notes due 2005	10.500% Notes due 2009
9.250% Notes due 2006	11.375% Notes due 2012
7.850% Notes due 2007	8.350% Notes due 2017

Indicate the number of outstanding shares of each of the issuer s classes of capital or common stock as of the close of the period covered by the annual report.

As of December 31, 2003:
169,476,120 shares of Common Capital Stock, Par Value Five Philippine Pesos Per Share
458,434,729 shares of Serial Preferred Stock, Par Value Ten Philippine Pesos Per Share

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days: Yes [X] No

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Indicate by check mark which financial statement item the registrant has elected to follow: Item 17 Item 18 [X]

TABLE OF CONTENTS

CERTAIN CONVENTIONS AND TERMS USED IN THIS REPORT

Unless the context indicates or otherwise requires, references to we, us, our or PLDT Group mean Philippine Long Distance Telephone Company and its consolidated subsidiaries, and references to PLDT mean Philippine Long Distance Telephone Company, not including its consolidated subsidiaries (see *Note 2 Basis of Consolidated Financial Statement Preparation* to the accompanying consolidated financial statements in Item 18 for a list of these subsidiaries, including a description of their respective principal business activities).

Any discrepancies in any table between totals and the sums of the amounts listed are due to rounding.

All references to the Philippines contained in this report mean the Republic of the Philippines and all references to the U.S. or the United States are to the United States of America.

In this report, unless otherwise specified or the context otherwise requires, all references to pesos, Philippine pesos or Php are to the lawful currency of the Philippines, all references to dollars, U.S. dollars or US$ are to the lawful currency of the United States, all references to Japanese yen, JP¥ or ¥ are to the lawful currency of Japan, and all references to Euro or are to the lawful currency of the European Union. Unless otherwise indicated, translations of peso amounts into U.S. dollars in this report were made based on the volume weighted average exchange rate quoted through the Philippine Dealing System, which was Php55.586 to US$1.00 on December 31, 2003. On June 23, 2004, the volume weighted average exchange rate quoted was Php56.261 to US$1.00.

In this report, each reference to:

- ACeS Philippines means ACeS Philippines Cellular Satellite Corporation, a 93.7%-owned subsidiary of PLDT;
- AIL means ACeS International Limited;
- AMPS means advanced mobile phone system;
- BCC or Bonifacio Communications Corporation, our 75%-owned subsidiary;

- BSP means Bangko Sentral ng Pilipinas;
- CDMA means code division multiple access;
- Clark Telecom means PLDT Clark Telecom, Inc., our wholly-owned subsidiary;
- ePLDT means ePLDT, Inc., our wholly-owned subsidiary;
- ETACS means enhanced total access communications system;
- First Pacific means First Pacific Company Limited;
- GAAP means generally accepted accounting principles;
- GSM means global system for mobile communications;
- ISP means internet service provider;
- Infocom means Infocom Technologies, Inc., a 99.6%-owned subsidiary of ePLDT;
- Mabuhay Satellite means Mabuhay Satellite Corporation (formerly Mabuhay Philippines Satellite Corporation), our 67%-owned subsidiary;
- Maratel means PLDT-Maratel (formerly Maranao Telephone Company, Inc.), our 97.5%-owned subsidiary;
- NTC means the National Telecommunications Commission of the Philippines;

- NTT Communications means NTT Communications Corporation, a wholly-owned subsidiary of Nippon Telegraph and Telephone Corporation of Japan;

- NTTC-UK means NTT Communications Capital (UK) Ltd., a wholly-owned subsidiary of NTT Communications;

- PAPTELCO means Philippine Association of Private Telephone Companies;

- Parlance means Parlance Systems, Inc., a wholly-owned subsidiary of ePLDT;

- Piltel means Pilipino Telephone Corporation, an associate in which we have a 45.3% ownership interest and which is treated as a consolidated subsidiary under U.S. GAAP;

- PLDT Beneficial Trust Fund means the beneficial trust fund created by PLDT to pay the benefits under the PLDT Employees Benefit Plan;

- PLDT Global means PLDT Global Corporation, our wholly-owned subsidiary;

- SEC means the Philippine Securities and Exchange Commission;

- SMS means short message service;

- Smart means Smart Communications, Inc., our wholly-owned subsidiary;

- Subic Telecom means Subic Telecommunications Company, Inc., our wholly-owned subsidiary;

- Telesat means Telesat, Inc., our 94.4%-owned subsidiary;

- Vocativ means Vocativ Systems, Inc., a wholly-owned subsidiary of ePLDT; and

- VSAT means very small aperture terminal.

FORWARD-LOOKING STATEMENTS

Some information in this report may contain forward-looking statements within the meaning of Section 27A of the U.S. Securities Act of 1933 and Section 21E of the U.S. Securities Exchange Act of 1934. We have based these forward-looking statements on our current beliefs, expectations and intentions as to facts, actions and events that will or may occur in the future. Such statements generally are identified by forward-looking words such as believe, plan, anticipate, continue, estimate, expect, may, will or other similar words.

A forward-looking statement may include a statement of the assumptions or bases underlying the forward-looking statement. We have chosen these assumptions or bases in good faith, and we believe that they are reasonable in all material respects. However, we caution you that assumed facts or bases almost always vary from actual results, and the differences between results implied by the forward-looking statements, assumed facts or bases and actual results can be material, depending on the circumstances. When considering forward-looking statements, you should keep in mind the description of risks and other cautionary statements in this report. You should also keep in mind that any forward-looking statement made by us in this report or elsewhere speaks only as of the date on which we made it. New risks and uncertainties come up from time to time, and it is impossible for us to predict these events or how they may affect us. We have no duty to, and do not intend to, update or revise the statements in this report after the date hereof. In light of these risks and uncertainties, you should keep in mind that actual results may differ materially from any forward-looking statement made in this report or elsewhere.

PART I

Item 1. Identity of Directors, Senior Management and Advisors

Not applicable.

Item 2. Offer Statistics and Expected Timetable

Not applicable.

Item 3. Key Information

Selected Financial Data

The selected consolidated financial information below should be read in conjunction with, and is qualified in its entirety by reference to, our audited consolidated financial statements, including the notes, included elsewhere in this report. The consolidated financial statements have been prepared and presented in conformity with U.S. GAAP. Due to our decision to commence using U.S. GAAP for our Annual Report on Form 20-F in respect of the year ended December 31, 2002, we are unable to provide without unreasonable effort and expense U.S. GAAP consolidated financial information with respect to the fiscal year ended December 31, 1999. As a result, we have omitted such information in the table below. In our Annual Reports on Form 20-F for years prior to 2002, we disclosed consolidated financial statements, including the financial information with respect to the year ended December 31, 1999, prepared in conformity with Philippine GAAP, along with a reconciliation to U.S. GAAP.

Prior to the filing of our Annual Report on Form 20-F in respect of the year ended December 31, 2002, the consolidated financial statements included in our Annual Reports on Form 20-F filed with the U.S. Securities and Exchange Commission, or U.S. SEC, were prepared in conformity with Philippine GAAP. Philippine GAAP varies in certain significant respects from U.S. GAAP. A description of the significant differences between U.S. GAAP and Philippine GAAP and a quantitative reconciliation of such differences in the net loss and stockholders equity to U.S. GAAP was disclosed in a note to our previously filed consolidated financial statements.

	Consolidated Financial Data Years Ended December 31,				
	2003	**2003**(1)	**2002**	**2001**	**2000**
	(in millions, except net operating income (loss) per share, earnings per common share, ratio of earnings to fixed charges and dividends declared per common share)				
Amounts in conformity with U.S. GAAP:					
Statements of Operating Data:					
Operating revenues	Php112,036	US$2,016	Php92,800	Php80,294	Php60,348
Operating expenses	78,563	1,413	80,771	86,236	49,824
Net operating income (loss)	33,473	602	12,029	(5,942)	10,524
Net operating income (loss) per share					
Basic	179.59	3.23	55.47	(47.36)	58.82
Diluted	165.85	2.98	52.23	(47.36)	58.82
Net income (loss)	11,045	199	(6,158)	(27,782)	(29,258)
Earnings per common share(2)					
Basic	47.20	0.85	(52.08)	(176.85)	(193.48)
Diluted	45.72	0.82	(52.08)	(176.85)	(193.48)
Balance Sheets Data:					

Cash and cash equivalents	19,372	349	10,974	4,276	
Total assets	276,628	4,977	269,387	284,877	
Total long-term debt - net of current portion	160,459	2,887	171,283	169,870	
Long-term debt	184,275	3,315	190,908	190,099	
Total debt(3)	186,408	3,353	191,668	196,561	
Total liabilities(4)	236,897	4,262	240,622	249,563	
Total stockholders equity	24,745	445	16,413	24,472	
Other Data:					
EBITDA(5)	44,055	793	26,281	6,475	(4,972)
Depreciation	21,882	393	17,566	16,218	12,756
Ratio of earnings to fixed charges(6)	1.8x	1.8x			
Net cash provided by operating activities	Php40,920	US$736	Php39,722	Php20,113	Php20,727
Net cash used in investing activities	18,359	330	17,167	29,376	25,183
Net cash provided by (used in) financing activities	(14,135)	(254)	(15,954)	3,841	5,511
Dividends declared to common shareholders				202	752
Dividends declared per common share(7)				1.20	4.80

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(1) We maintain our accounts in Philippine pesos. For convenience, the peso financial information as of and for the year ended December 31, 2003, has been translated into U.S. dollars at the exchange rate of Php55.586 to US$1.00, the rate quoted through the Philippine Dealing System as of December 31, 2003. This translation should not be construed as a representation that the Philippine peso amounts represent, or have been or could be converted into, U.S. dollars at that rate or any other rate.

(2) Prior to 2003, our convertible preferred shares were deemed anti-dilutive based on a calculation of the required dividends on preferred shares for each series of convertible preferred shares divided by the number of equivalent common shares assuming such preferred shares were converted into common shares and compared against the basic earnings per share. Since the amount of dividends on preferred shares over the equivalent number of common shares were greater than the basic earnings per share, the amounts for basic and diluted earnings per share are the same.

(3) Total debt represents current portion of long-term debt, long-term debt net of current portion and notes payable.

(4) Total liabilities on a consolidated basis represent the difference between total assets and minority interest in consolidated subsidiaries, preferred stock subject to mandatory redemption and stockholders equity.

(5) On a consolidated basis, EBITDA is defined as income (loss) before minority interest in net income of consolidated subsidiaries and adding back interest expense and related items (net of capitalized interest), taxes, depreciation, and amortization and deducting interest income and is presented because it is generally accepted as providing useful information regarding a company s ability to service and/or incur debt. In light of our substantial indebtedness, we believe that the presentation of EBITDA measures is useful information regarding our ability to

service our debt and to incur any additional debt. In addition, many of our loan agreements incorporate various covenants or limitations based on EBITDA (calculated on the basis of Philippine GAAP). EBITDA should not be considered in isolation or as a substitute for operating income, net income, cash flows from operating activities and other income or cash flow statement data prepared in accordance with applicable generally accepted accounting principles, or as a measure of PLDT s profitability or liquidity. A quantitative reconciliation of EBITDA from income (loss) before minority interest in net income of consolidated subsidiaries is provided in the following table:

	Consolidated Financial Data Years Ended December 31,				
	2003	**2003**(1)	**2002**	**2001**	**2000**
	(in millions)				
Amounts in conformity with U.S. GAAP:					
Income (loss) before minority interest in net income of consolidated subsidiaries	Php11,159	US$201	(Php6,032)	(Php27,674)	(Php29,117)
Add/(deduct):					
Interest expenses and related items, net of capitalized interest	12,161	219	12,780	14,697	13,541
Interest income	(513)	(9)	(237)	(373)	(1,016)
Provision for (benefit from) income tax	(1,400)	(25)	1,438	(2,570)	(5,613)
Depreciation	21,882	393	17,566	16,218	12,756
Amortization of goodwill and other intangible assets	766	14	766	6,177	4,477
EBITDA	Php44,055	US$793	Php26,281	Php6,475	(Php4,972)

(6) For purposes of this ratio, Earnings consist of income before provision for income tax (excluding PLDT s share in undistributed income of less than 50% owned affiliates) and fixed charges (excluding capitalized interest). Fixed charges consist of interest (including capitalized interest, discounts and other financing costs) on all indebtedness, amortization of deferred financing costs and the estimated financing component of rent expense (i.e., one-third of rent expense).

Due to PLDT s net losses in 2002, 2001 and 2000, the coverage ratio on a consolidated basis was less than 1.0x in these three years. In order to achieve a coverage ratio of 1.0x, we would have had to generate additional consolidated earnings of Php2,464 million, Php30,126 million and Php35,509 million for each of the three years ended December 31, 2002, 2001 and 2000, respectively.

(7) The most recent cash dividend declaration made by PLDT on its common stock was in March 2001, which was paid in April 2001.

Capital Stock

The following table summarizes PLDT s capital stock outstanding as of December 31, 2003, 2002 and 2001.

	December 31,		
	2003	**2002**	**2001**
	(in millions)		
Serial Preferred Stock			
Cumulative Convertible			
10% Convertible			
A to DD	Php4,099	Php4,068	Php3,723
Series III	46	46	46
Series V(1)	26	25	26
Series VI(1)	47	49	49
Series VII(1)	38	36	38
Cumulative Nonconvertible			
Series IV	360	360	360
	Php4,616	Php4,584	Php4,242
Common Stock	Php847	Php847	Php845

Dividends Declared

	Years Ended December 31,		
	2003	**2002**	**2001**
Cash dividends declared per share of PLDT s common stock, in pesos (2)	Php	Php	Php1.20

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(1) Preferred stock subject to mandatory redemption (see Note 16 Preferred Stock Subject to Mandatory Redemption to the accompanying consolidated financial statements in Item 18 for further discussion) in 2008 and 2009.

(2) The most recent cash dividend declaration made by PLDT on its shares of common stock was in March 2001, which was paid in April 2001. PLDT does not expect to declare cash dividends on these shares in 2004.

Dividends Paid

A summary of dividends paid per share of PLDT's common stock stated in both Philippine pesos and U.S. dollars follows:

	In Philippine Pesos	**In U.S. Dollars**

1999		
January 15	1.20	0.031
April 15	1.20	0.031
July 15	1.20	0.031
October 15	1.20	0.030
2000		
January 14	1.20	0.030
April 14	1.20	0.029
July 15	1.20	0.027
October 15	1.20	0.025
2001		
January 15	1.20	0.023
April 16	1.20	0.024

(*Note*: *Dividends on PLDT's common stock were declared and paid in Philippine pesos. For the convenience of the reader, the peso dividends are translated into U.S. dollars based on exchange rates on the respective dates of dividend payments. Dividends paid in January of each of the calendar years 1999-2001 were declared in the preceding December. Accordingly, total amounts shown for cash dividends declared under Dividends Declared above may differ from the amounts shown for cash dividends paid under Dividends Paid.*)

Exchange Rates

The Philippine government does not administratively fix the exchange rate between the Philippine peso and the U.S. dollar. Since August 1, 1992, a market average rate has been determined daily in inter-bank trading using the Philippine Dealing System, known as the Philippine Dealing System Reference Rate. The Philippine Dealing System is a specialized off-floor direct dealing service for the trading of Philippine pesos-U.S. dollars by member banks of the Bankers Association of the Philippines and BSP, the central bank of the Philippines. All members of the Bankers Association of the Philippines are required to make their Philippine peso-U.S. dollar trades through this system, which was established by Telerate Financial Information Network of Hong Kong.

The following shows the exchange rates between the Philippine peso and the U.S. dollar, expressed in pesos per U.S. dollar, for the periods indicated, based on the volume-weighted average exchange rate for each business day in each of the periods presented:

	Year Ended December 31,			
	Period End	**Average(1)**	**Low(2)**	**High(3)**
1999	Php40.298	Php39.090	Php37.566	Php41.112
2000	49.986	44.179	39.830	51.680
2001	51.690	51.009	47.550	55.013

2002	53.254	51.583	49.336	53.841
2003	55.586	54.215	52.021	55.767
2004 (through June 23, 2004)	56.261	55.945	55.142	56.429

Source: Philippine Dealing System Reference Rate

(1) Simple average of exchange rates for the period.

(2) Lowest exchange rate for the period.

(3) Highest exchange rate for the period.

		Month		
	Period End	**Average(1)**	**Low(2)**	**High(3)**
2003				
December	Php55.586	Php55.438	Php55.288	Php55.586
2004				
January	55.964	55.545	55.142	56.085
February	56.332	56.089	55.872	56.332
March	56.216	56.298	56.151	56.429
April	56.034	55.894	55.577	56.346
May	55.807	55.835	55.490	55.973
June (through June 23, 2004)	56.261	55.965	55.669	56.393

Source: Philippine Dealing System Reference Rate

(1) Simple average of exchange rates for the month.

(2) Lowest exchange rate for the month.

(3) Highest exchange rate for the month.

This report contains conversions of peso amounts into U.S. dollars for your convenience. Unless otherwise specified, these conversions were made at the exchange rate as of December 31, 2003 of Php55.586 to US$1.00. You should not assume that such peso amounts represent such U.S. dollar amounts or could have been or could be converted into U.S. dollars at the rate indicated, or at any particular rate. As of June 23, 2004, the exchange rate quoted through the Philippine Dealing System was Php56.261 to US$1.00.

Risk Factors

Risks Relating to Us

Our substantial indebtedness could impair our ability to fulfill our financial obligations, service our other debt and carry out new financings

We have substantial indebtedness. As of December 31, 2003, we had consolidated total indebtedness of approximately Php186,408 million (US$3,353 million), including short-term debt of approximately Php2,133 million (US$38 million) and a consolidated ratio of debt to equity (total debt on a consolidated basis divided by stockholders' equity) of 7.53x. Our consolidated ratio of earnings to fixed charges was less than the minimum required ratio of 1.0x for the years ended December 31, 2002 and 2001. For an explanation on how we calculate our consolidated ratio of earnings to fixed charges, see footnote 6 to our consolidated financial data table under Selected Financial Data and Exhibit 7 in Item 19. Our existing debt contains covenants, which, among other things, require PLDT to maintain certain financial ratios calculated on the basis of Philippine GAAP on a consolidated and non-consolidated basis, limit our ability to incur indebtedness, make investments, incur expenditures and pay dividends. Financial statements prepared in conformity with Philippine GAAP differ in some material respects from financial statements prepared in conformity with U.S. GAAP. For a description of some of these covenants, see Item 5. Operating and Financial Review and Prospects Liquidity and Capital Resources Financing Activities Debt Financing Covenants.

Our substantial indebtedness and the requirements and limitations imposed by our debt covenants could have important consequences. For example, they could:

- make it more difficult for us to satisfy our debt obligations;

- require us to dedicate a substantial portion of our cash flow to payments on our indebtedness, thereby reducing the availability of our cash flow to fund working capital, capital expenditures and other general corporate requirements;

- limit our ability to refinance our debt obligations or incur new debt needed to finance our working capital, capital expenditure or other requirements;

- limit our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate; and

- place us at a competitive disadvantage compared to our competitors.

If we are unable to meet our debt service obligations or comply with our debt covenants, we could be forced to restructure or refinance our indebtedness, seek additional equity capital or sell assets. An inability to effect these measures successfully could result in a declaration of default and an acceleration of some or all of our indebtedness.

Under the indenture for our 10.625% Notes due 2007 and 11.375% Notes due 2012, we may only incur additional debt, subject to certain exceptions, if, after incurrence of such debt, our consolidated leverage ratio under Philippine GAAP, (the ratio of debt to EBITDA calculated on a non-consolidated basis based on definitions provided in the same indenture and except under certain circumstances) would be less than 5.5:1 on or prior to December 31, 2003, 5.0:1 from January 1, 2004 to December 31, 2004 and 4.5:1 thereafter. Because our consolidated leverage ratio at December 31, 2003 is in excess of 5.0:1, we are currently restricted from incurring any additional debt, subject to certain exceptions, including exceptions for refinancing transactions. In addition, we expect that we will have difficulty meeting our debt payment obligations if we do not continue to receive cash dividends from Smart.

We may not be able to maintain compliance with restrictive covenants and ratios imposed by our indebtedness

Our debt instruments contain restrictive covenants and require us to comply with specified financial ratios and other financial tests calculated on the basis of Philippine GAAP at relevant measurement dates, principally at the end of each quarterly period. Financial statements prepared in conformity with Philippine GAAP differ in some material respects from financial statements prepared in conformity with U.S. GAAP.

The principal factors that can negatively affect our ability to comply with these financial ratios and other financial tests are depreciation of the peso relative to the U.S. dollar, poor operating performance of PLDT and its consolidated subsidiaries, impairment or similar charges in respect of investments or other long-lived assets that may be recognized by PLDT and its consolidated subsidiaries, and increases in our interest expenses. Since approximately 96% of PLDT's total debt is denominated in foreign currencies, principally in U.S. dollars, many of these financial ratios and other tests are negatively affected by any weakening of the peso, which declined by approximately 5% against the U.S. dollar to an average of Php54.215 to US$1.00 in 2003 from an average of Php51.583 to US$1.00 in 2002. As of December 31, 2003, the exchange rate was Php55.586 to US$1.00, equivalent to a 4% depreciation of the peso relative to the rate at the end of 2002. In addition, certain of our financial ratios are adversely affected by increases in interest expense, which may result from factors including issuance of new debt, the refinancing of lower cost indebtedness by higher cost indebtedness, depreciation of the peso, the lowering of PLDT's credit ratings or the credit ratings of the Philippines, an increase in reference interest rates, and general market conditions.

PLDT s ability to maintain compliance with financial covenant requirements measured on a non-consolidated basis is principally affected by the performance of our fixed line business, which is predominantly conducted by PLDT. PLDT cannot be assured of the benefit of results generated by Smart and PLDT s other investees in assisting in complying with non-consolidated covenants or covenants that are calculated without giving effect to the results of PLDT s investees.

We have maintained compliance with all of our financial ratios and covenants as measured under Philippine GAAP under our loan agreements and other debt instruments. However, if negative factors adversely affect our financial ratios, we may be unable to maintain compliance with these ratios and covenants or be unable to incur new debt. Under some of our loan agreements, certain of our financial ratios have become more restrictive at the end of the second and fourth quarters of 2003 and the first quarter of 2004, and will continue to become more restrictive in increments thereafter, which will make it more difficult for PLDT to maintain compliance with this ratio in the future. Inability to comply with our financial ratios and covenants or raise new financing could result in a declaration of default and acceleration of some or all of our indebtedness. The terms of some of our debt instruments have no minimum amount for cross-default.

For more information on the requirements of our loan agreements and other debt instruments and our compliance with them, see Item 5. Operating and Financial Review and Prospects Liquidity and Capital Resources Financing Activities Debt Financing Covenants.

Creditors of our subsidiaries will have superior claims to our subsidiaries cash flow and assets

A growing portion of our consolidated revenues and cash flow from operations is derived from our subsidiaries, particularly Smart. Smart and some of our other subsidiaries have significant internal cash requirements for debt service, capital expenditures and operating expenses and so may be financially unable to pay any dividends to PLDT. In addition, some of our subsidiaries are subject to covenants that restrict them from distributing cash to PLDT except under certain circumstances. In particular, Smart is subject to loan covenants that restrict its ability to distribute cash to PLDT. Although Smart received consents under its relevant loans that permitted it to make dividend payments to PLDT in December 2002, June 2003, November 2003 and May 2004, we cannot assure you that PLDT will continue to receive dividends or other distributions, or otherwise be able to derive liquidity from Smart or any other subsidiary or investee in the future.

Creditors of our subsidiaries will have prior claims to our subsidiaries assets and cash flows. We and our creditors will effectively be subordinated to the existing and future indebtedness and other liabilities, including trade payables, of our subsidiaries, except that we may be recognized as a creditor on loans we have made to subsidiaries. If we are recognized as a creditor of a subsidiary, our claim will still be subordinated to any indebtedness secured by assets of the subsidiary and any indebtedness of the subsidiary otherwise deemed senior to indebtedness we hold.

Our businesses require substantial capital investment, which we may not be able to finance

Our projects under development and the continued maintenance and improvement of our networks and services, including Smart s projects, networks and services, require substantial ongoing capital investment. Our consolidated capital expenditures in 2003 and 2002 totaled Php17,943 million and Php17,239 million, respectively. Our 2004 budget for consolidated capital expenditures is approximately Php22,000 million, of which approximately Php7,000 million is budgeted to be spent by PLDT and approximately Php15,000 million is budgeted to be spent by Smart. PLDT s capital spending is intended principally to finance the continued build-out of its data and internet protocol infrastructures and for its data services and the maintenance of its network. Smart s capital spending is focused on expanding and upgrading its GSM network to meet increased demand for cellular services.

Future strategic initiatives could require us to incur significant additional capital expenditures. We may be required to finance a portion of our future capital expenditures from external financing sources, which have not yet been fully arranged. We cannot assure you that financing for new projects will be available on terms acceptable to us or at all. If we cannot complete our development programs and other capital projects, our growth, results of operations and financial condition could be materially and adversely affected.

Our ability to refinance our debt and raise new financing to fund our working capital, capital expenditures and other needs depends on many factors beyond our control

In addition to our existing available credit facilities, we may require new external financing in order to fund all of our operating, investment, capital expenditures and debt service requirements and to refinance and extend the maturities of our short and medium-term indebtedness. Our ability to arrange for this and other financing and the cost of such financing will be dependent on numerous factors outside of our control, including:

- general economic and capital market conditions, including the peso-to-U.S. dollar exchange rate;
- the availability of credit from banks or other lenders;
- investor confidence in us;
- investor views about the Philippines;
- the continued success of our business;

- our credit ratings and the sovereign credit ratings of the Philippines; and

- provisions of tax and securities laws that may be applicable to our efforts to raise capital.

Any credit rating downgrades may significantly affect the availability and the terms of our prospective financing, including financing costs. In addition, restrictions under our current indebtedness subject us to various financial tests, which could prevent us from incurring additional debt. Inability to arrange such debt could materially and adversely affect our ability to fund our anticipated operating, investment and capital expenditures as well as our anticipated debt service requirements, and could result in defaults and cross-defaults under our existing debt, thereby adversely affecting our results of operations and financial condition.

If the peso depreciates against the U.S. dollar, our financial position could be materially and adversely affected

Substantially all of our indebtedness and related interest expense, a substantial portion of our capital expenditures and a portion of our operating expenses are denominated in U.S. dollars and other foreign currencies, but a significant portion of our revenues is denominated in pesos. As of December 31, 2003, approximately 94% of our consolidated indebtedness was denominated in U.S. dollars and other foreign currencies. A depreciation of the peso against the U.S. dollar increases the amount of our debt obligations and operating and interest expenses in peso terms. In the event that the peso depreciates against the U.S. dollar, we may be unable to generate enough funds through operations (such as by raising our service rates, including through adjustments to rates for local exchange service based on movements in the peso-to-dollar exchange rate) and other means to offset the resulting increase in our obligations in peso terms. Further, these changes could cause us not to be in compliance with the financial covenants imposed by our lenders under certain loan agreements and other indebtedness.

During the last decade, the peso has generally depreciated against most foreign currencies. In addition, during this period, the Philippine economy has also, from time to time, experienced periods of concentrated peso devaluation and limited availability of foreign currency. Since June 30, 1997, when the BSP announced that it would let market forces determine the value of the peso, the peso has experienced a significant decline against the U.S. dollar. It depreciated from Php26.376 to US$1.00 on June 30, 1997, to Php55.586 to US$1.00 as of December 31, 2003 and further decreased to Php56.216 to US$1.00 as of March 31, 2004. The peso declined by approximately 4% against the U.S. dollar to Php55.586 to US$1.00 as of December 31, 2003 from Php53.254 to US$1.00 as of December 31, 2002 and by approximately 1% against the U.S. dollar to Php56.216 to US$1.00 as of March 31, 2004 from Php55.586 to US$1.00 as of December 31, 2003. The peso has also been subject to significant fluctuations. For example, during the first nine months of 2003, the peso depreciated to a low of Php55.532 to US$1.00 on August 26, 2003, recovered to a high of Php52.021 to US$1.00 on May 8, 2003 and again depreciated to a low of Php55.767 to US$1.00 on November 27, 2003. The peso may again be subject to significant fluctuations and may depreciate due to a range of factors, including:

- political and economic developments affecting the Philippines;

- the volatility of regional currencies, particularly the Japanese yen;

- any interest rate increases by Federal Reserve Bank of the United States;

- higher demand for U.S. dollars by both banks and domestic businesses to service their maturing U.S. dollar obligations; and

- some banks covering their short U.S. dollar positions.

Our results of operations have been, and may continue to be, adversely affected by competition in international long distance service

The international long distance business was historically one of our major sources of revenue. However, due to competition and the steep decline in international settlement rates that are paid to us by foreign telecommunications carriers for termination of international calls on our network, revenues generated from our international long distance business have overall declined in recent years.

Although revenue generated from our international long distance business increased primarily due to increased termination rates in 2003, we anticipate that revenues from international communications and information services, including our services, will continue to decline in the future, primarily due to:

- installed and expanding fiber networks and satellite capacities that provide substantially more transmission capacity than may be needed in the short or medium term;

- substantial increases in the transmission capacity of new and existing networks, including those operated by our competitors, due to recent technological advances;

- increased competition from other domestic and international telecommunications providers;

- alternative providers offering internet telephony and broadband capacity; and

- advances in technology.

We cannot assure you that these declines will not materially and adversely affect our financial performance.

Net settlement payments between PLDT and other foreign telecommunications carriers for origination and termination of international call traffic between the Philippines and other countries have been our predominant source of foreign currency revenues. However, in U.S. dollar terms, these payments have been declining in recent years. Continued decline in our foreign currency revenues could increase our exposure to risks from declines in the value of the Philippine peso against the U.S. dollar. We cannot assure you that we will be able to achieve adequate increases in our other revenues to make up for any adverse impact of a further decline in our net settlement payments.

We face strong competition and may need to increase our marketing expenditures or reduce our rates in order to compete effectively

We cannot assure you that the number of providers of cellular telecommunication services will not increase or that competition for telecommunications customers will not lead our cellular and fixed line subscribers to switch to other operators or lead us to increase our marketing expenditures or reduce our rates, resulting in a reduction in our profitability.

The Philippine government has liberalized the Philippine telecommunications industry and opened up the Philippine telecommunications market to new entrants. Including us, there are nine major local exchange carriers, 11 international gateway facility providers and six cellular mobile telephone system providers in the Philippines, including one which has not yet commenced operations. Many new entrants into the Philippine telecommunications market have entered into strategic alliances with foreign telecommunications companies, which provide them access to technological and funding support as well as service innovations and marketing strategies. Consequently, we are facing increasing competition in major segments of the telecommunications industry, particularly cellular, fixed line and data and other network services segments.

The cellular telecommunications industry in the Philippines has been particularly competitive, as operators have sought to develop and maintain market shares and to attract new subscribers. Our principal cellular competitor, Globe Telecom, Inc., or Globe, acquired another telecommunications provider, Isla Communications Company, Inc., or Islacom, on June 27, 2001, thereby strengthening Globe as a competitor. Further consolidation in the industry could result in more vigorous competition. Digital Telecommunications Philippines, Inc., or Digitel, which was awarded a license to operate cellular telecommunications services in 2000, launched its cellular service, *Sun Cellular*, on March 29, 2003. In addition, the NTC has awarded a license to Bayan Telecommunications Philippines, Inc., or BayanTel, to operate cellular telecommunications services, but as of the filing of this annual report has not yet commenced cellular operations. The recent entry of Digitel and the grant of a license to Bayantel are expected to create additional competition in the industry. In the future, the government may allocate further frequencies and award additional cellular telecommunications licenses, which would further increase competition.

Competitive pressures on our cellular rates may affect our cellular revenues and revenue growth. For example, we have not increased our cellular rates to reflect fluctuations in the peso-to-U.S. dollar exchange rate since November 1998 as a result of such competitive pressures. In addition, our prepaid GSM subscribers can, using their existing handsets, switch to one of our competitors by having their handsets unlocked from our service for a fee and purchasing a new SIM card from the desired operator. We cannot assure you that these marketing expense and rate pressures and loss of customers will not have a material adverse effect on our financial performance.

If we are unable to install and maintain telecommunications facilities and equipment in a timely manner, we may not be able to keep up with our principal competitors, which may have negative implications for our revenue and profitability

Our business requires the regular installation of new, and the maintenance of existing, telecommunications transmission and other facilities and equipment. The installation and maintenance of these facilities and equipment are subject to risks and uncertainties relating to:

- shortages of equipment, materials and labor;
- work stoppages and labor disputes;
- interruptions resulting from inclement weather and other natural disasters;
- unforeseen engineering, environmental and geological problems; and
- unanticipated cost increases.

Any of these factors could give rise to delays or cost overruns in the installation of new facilities or equipment or could prevent us from properly maintaining the equipment used in our networks, and could have a material adverse effect on our results of operations and financial condition.

Rapid changes in telecommunications technology may adversely affect the economics of our existing businesses and the value of our assets, increase our required capital expenditures and create new competition

The telecommunications sector has been characterized recently by rapid technological changes. We cannot assure you that these developments will not result in competition from providers of new services or the need to make substantial capital expenditures to upgrade our facilities. For example, if third-generation, or 3G, cellular services were introduced in the Philippines, we would likely incur significant expenses if we were to roll out those services.

Our future success will depend, in part, on our ability to anticipate or adapt to such changes and to offer services that meet customer demands on a competitive and timely basis. We cannot assure you that we will be able to obtain new technologies on a timely basis or on satisfactory terms or implement them in an appropriate or effective manner. The development and introduction of new technologies by us or our competitors may cause significant portions of our existing assets to become obsolete and suffer an impairment in value earlier than their anticipated useful lives and require us to accelerate their depreciation. In 2001, we recognized impairment charges in respect of Smart s analog assets and Smart s unamortized intangible asset relating to analog customer lists. Piltel recognized impairment losses in respect of its AMPS/CDMA and Executive Order No. 109, or E.O. 109 assets in 2001 and 2002, respectively.

The cellular telecommunications industry may not continue to grow or may grow at a slower rate

The majority of our consolidated revenues is currently derived from our cellular services. As a result, we depend on the continued development and growth of the cellular telecommunications industry. Growth of the cellular communications market depends on many factors beyond our control, including the continued introduction of new and enhanced cellular devices and consumer preferences. Any economic, technological or other developments resulting in a reduction in demand for cellular services may harm our business.

Our businesses depend on the reliability of our network infrastructure, which is subject to physical, technological and other risks

The development and operation of telecommunications networks are subject to physical, technological and other risks, which may cause interruptions in service or reduced capacity for customers. These risks include:

- physical damage;

- power loss;
- capacity limitation;
- software defects; and
- breaches of security by computer viruses, break-ins or otherwise.

The occurrence of any of these risks could have a material adverse effect on our ability to provide services to customers, and could have a material adverse effect on our business.

Piltel has experienced financial difficulties and we cannot assure you that it will be able to discharge any of its debts or other obligations, including its debts or other obligations owed to us and our affiliates

Piltel has experienced significant financial difficulties in recent years. It has restructured substantially all of its debts in accordance with its debt restructuring plan, which was signed on June 4, 2001. Under the terms of such debt restructuring plan, PLDT issued a Letter of Support for the benefit of Piltel and its creditors under which PLDT has agreed to cover any funding shortfalls of Piltel up to a maximum amount of US$150 million, of which approximately US$50 million remained undrawn as of December 31, 2003. In June and October 2002, more creditors of Piltel agreed to participate in its restructuring plan on the same terms. As of December 31, 2003, total restructured long-term debt of Piltel amounted to Php23,382 million, with maturities of up to June 14, 2016. Piltel is currently in the process of restructuring certain other debts. However, we cannot assure you that Piltel will be able to restructure or otherwise pay the claims relating to its unrestructured debt or that Piltel will have sufficient cash flow to meet its debt service and other payment obligations, including its payment obligations to us. As of December 31, 2003, Piltel owed PLDT Php985 million, while Smart owed Piltel Php2,199 million in respect of their respective facilities sharing and other agreements with Piltel. Until all amounts owed to creditors participating in the debt restructuring plan have been paid or discharged, PLDT will not be permitted to demand or receive any payment, redemption, or distribution in respect of any present and future liability owed by Piltel to PLDT or any affiliate of PLDT, subject to specified exceptions. These liabilities include amounts owed on Piltel preferred shares owned by PLDT and other financial indebtedness owed by Piltel to PLDT or any affiliate of PLDT, but exclude payments due in respect of transactions having arm s-length terms or in which the pricing is based on market terms. These severe long-term restrictions significantly impair Piltel s ability to transfer funds to PLDT.

Moreover, Piltel may not be able to restructure or otherwise pay the claims relating to its unrestructured debt. As of December 31, 2003, Piltel had an aggregate principal amount of Php51 million of unrestructured debt. Piltel does not intend to make any payments in respect of this debt unless and until it reaches a restructuring agreement with the creditors holding the obligations. If Piltel s non-participating creditors take forceful measures to enforce their claims, it is possible that Piltel would be required to submit itself to a court-supervised rehabilitation proceeding or an involuntary insolvency proceeding seeking liquidation. All of Piltel s creditors that participated in the debt restructuring agreed in connection with the debt restructuring that they would submit Piltel to a rehabilitation proceeding in those circumstances and petition for the adoption of a plan of rehabilitation that includes the financial terms of the debt restructuring plan. However, the laws and procedures governing a rehabilitation proceeding in the Philippine courts remain untested in significant respects. We cannot assure you that a rehabilitation plan, which incorporates the financial terms of the debt restructuring, would be adopted promptly or at all. Even if such a rehabilitation plan was adopted, we cannot assure you that Piltel will prove to be viable thereafter and that it will be able to meet its obligations, including its obligations owed to us or our affiliates. On March 23, 2004, Smart sent out invitations to the creditors of Piltel to offer to sell their indebtedness to Smart, see Item 5. Operating and Financial Review and Prospects Other Information Smart s Proposed Exchange Offer to Piltel Creditors and *Note 28 Other Matters(g)* to the accompanying consolidated financial statements in Item 18 for further discussion.

The franchise of Smart may be revoked if it cannot make a public offering of its shares in August 2004

Smart believes that it has ten years from the commencement of its operations, or until August 2004, to conduct a public offering of its shares required under the Public Telecommunications Policy Act (Republic Act No. 7925, or R.A. 7925). If Smart will not conduct a public offering of its shares by August 2004, the Philippine Congress may revoke the franchise of Smart if it fails to comply with the requirement under R.A. 7925 on the public offering of its shares. A *quo warranto* case may also be filed against Smart by the Office of the Solicitor General of the Philippines for the revocation of the franchise of Smart on the ground of violation of R.A. 7925 if Smart will fail to conduct the public offering of its shares by August 2004.

A significant number of PLDT s shares are held by two separate shareholders, which may not act in the interests of other shareholders or stakeholders in PLDT

Affiliates of First Pacific directly or indirectly own approximately 31.4% of PLDT s common stock as of December 31, 2003. This is the largest block of PLDT s common stock that is directly or indirectly under common ownership. NTT Communications owns 14.9% of PLDT s common stock as of December 31, 2003 and has contractual veto rights over a number of major decisions and transactions that PLDT could make or enter into, including:

- capital expenditures in excess of US$50 million;

- any investments, if the aggregate amount of new investments for the previous 12 months is greater than US$100 million, determined on a rolling monthly basis;

- any investments in a specific investee, if the cumulative value of all investments made by PLDT in that investee is greater than US$10 million in the case of an existing investee and US$50 million in the case of a new investee;

- issuance of common stock or stock that is convertible into common stock;

- new business activities other than those we currently engage in;

- merger or consolidation; and

- the provision of financial support to Piltel in excess of that remaining available under the PLDT Letter of Support.

First Pacific and NTT Communications have also entered into a shareholders agreement relating to PLDT. As a result of this agreement and their respective stockholdings, First Pacific and its affiliates and/or NTT Communications are able to influence our actions and corporate governance, including:

- elections of PLDT s directors; and

- approval of major corporate actions, which require the vote of common stockholders.

First Pacific and its affiliates and/or NTT Communications may exercise control over these decisions and transactions in a manner that could be contrary to your interests.

If a major shareholder sells its interest in PLDT, the transaction may result in an event of default

If First Pacific or NTT Communications sells all or a portion of its equity interest in PLDT, in certain circumstances, such sale may give rise to an obligation for us to make an offer to purchase or prepay our outstanding debt under our 10.625% Notes due 2007 and our 11.375% Notes due 2012, our US$145 million multicurrency term loan facility agreement, our JP¥9,760 million loan agreement with Japan Bank for International Cooperation, or JBIC, (formerly known as the Export-Import Bank of Japan) and our JP¥5,615 million syndicated term loan facility, and may result in a default under all of Smart s loan agreements. As of December 31, 2003, Php33,152 million in principal amount of PLDT s indebtedness is directly subject to a change in control offer to purchase or prepay requirement and Php19,733 million in principal amount of Smart s indebtedness is subject to an event of default in the event of a change in control of PLDT. If we fail to complete a required change in control offer to purchase or prepay the affected debts, all of our debt could become immediately due and payable as a result of various cross-default provisions. See Item 5. Operating and Financial Review and Prospects Liquidity and Capital Resources Financing Activities Debt Financing Covenants.

The outcome of a pending investigation by the U.S. Department of Justice is uncertain

In January 2004, PLDT, a PLDT employee and an employee of Smart received grand jury subpoenas seeking documents and testimony in connection with a criminal investigation being conducted by the U.S. Department of Justice with respect to alleged antitrust violations relating to the provision of international termination services in the Philippines. The U.S. Department of Justice has also requested testimony and documents from Smart in connection with this investigation. Moreover, in March 2004, PLDT (U.S.) Ltd., a subsidiary of PLDT Global, also received a grand jury subpoena seeking documents in connection with this investigation. At this time, PLDT cannot predict the outcome of this investigation.

PLDT s franchise may be revoked if we are unsuccessful in legal proceedings, which are pending

The Constitution of the Philippines requires that at least 60% of the capital of a corporation operating a public utility in the Philippines be owned by Philippine citizens. In 1990, the then-Solicitor General of the Philippines instituted legal proceedings seeking to revoke PLDT s franchise on various grounds, including violation of this requirement. We believe that these proceedings are without merit. In 1991, the Philippine Congress extended the term of PLDT s franchise until 2028 and broadened PLDT s franchise authority. The Congress granted this amended franchise to PLDT despite these pending legal proceedings and despite the opposition of the Solicitor General. The Solicitor General has not taken any further action to pursue or continue the proceedings on this case. The parties filed their last pleadings in 1992 and since then the case has remained inactive. Consequently, under a court order dated January 20, 1999, the case has been archived, though the case can potentially be revived by action of either PLDT or the Solicitor General s office. It is a normal practice for Philippine courts to archive cases that remain inactive for a long period of time. We are not aware of any court notice for the resumption of the proceedings in this case.

Our business is significantly affected by governmental laws and regulations, including regulations in respect of our franchises and rates

We operate our business under franchises, each of which is subject to amendment, termination or repeal by the Philippine Congress. Additionally, PLDT operates pursuant to various provisional authorities and certificates of public convenience and necessity, or CPCNs, which are granted by the NTC and expire between now and 2028. Some of PLDT s CPCNs and provisional authorities have already expired. However, PLDT filed applications for extension of these CPCNs and provisional authorities prior to their respective expiration dates and is therefore entitled to continue to conduct its business under its existing CPCNs and provisional authorities pending the NTC s decisions on these extensions. Smart also operates its cellular, international long distance, national long distance and global mobile personal communications via satellite services pursuant to CPCNs, which will expire upon the expiration of its franchise. Smart s franchise is due to expire on March 27, 2017, 25 years after the date on which its current franchise was granted. Smart operates international private leased circuits under a provisional authority, which expired on May 6, 2003. Smart applied for an extension of this provisional authority prior to its expiration. Because PLDT and Smart filed the applications for extension on a timely basis, we expect that these extensions will be granted. However, we cannot assure you that the NTC will grant these extensions. If a CPCN has not been issued, the NTC may permit an operator to provide services pursuant to a provisional authority. Provisional authorities are typically granted for a period of 18 months. The Philippine Revised Administrative Code of 1987 provides that if the grantee of a license or permit, such as a CPCN or provisional authority, has made timely and sufficient application for the extension thereof, the existing CPCN or provisional authority will not expire until the application is finally decided upon by the administrative agency concerned. However, we cannot assure you that our franchises, CPCNs and provisional authorities will be renewed. For a description of our licenses, see Item 4. Information on the Company Licenses and Regulation.

The NTC also regulates the rates we are permitted to charge for services that have not yet been deregulated, such as local exchange services. We cannot assure you that the NTC will not impose additional obligations on us that could lead to the revocation of our licenses if not adhered to and/or reduction in our operating revenues or profitability. In addition, the NTC could adopt changes to the regulations governing our interconnection with other telecommunications companies or the rates and terms upon which we provide services to our customers that could have a material and adverse effect on our results of operations.

The NTC may implement proposed changes in billing requirements for cellular operators, which may have negative implications for our revenues and profitability

On June 16, 2000, the NTC issued Memorandum Circular No. 13-6-2000 proposing that Philippine cellular operators, including Smart and Piltel, be required, among other things:

- to bill their subscribers for cellular calls on a six-second pulse basis instead of the current per minute basis;

- not to bill calls directed to recorded voice messages; and

- to extend the expiration date of prepaid cards from the current two months to two years.

Along with the other Philippine cellular operators, Smart sought and obtained from a Quezon City trial court a preliminary injunction restraining the implementation of the memorandum circular. The NTC appealed the issuance of the injunction to the Court of Appeals which, on October 9, 2001, annulled the preliminary injunction, ruling that the

NTC had jurisdiction over the matter. On January 10, 2002, the Court of Appeals denied the cellular operators motion to annul and reverse the decision of the Court of Appeals. On February 22, 2002, Smart filed an appeal with the Supreme Court arguing that the appellate court had erred in ruling that the NTC, and not the trial court, had jurisdiction over its case. On September 2, 2003, the Supreme Court upheld Smart s appeal, reversing and setting aside the decision of the Court of Appeals and affirming that the Quezon City trial court could hear and decide the case. The case was remanded to the Quezon City trial court for continuation of the proceedings. The NTC filed a motion for reconsideration on September 29, 2003 which was denied with finality by the Supreme Court on November 13, 2003. The Supreme Court stated that considering that the basic issues have already been passed upon and there is no substantial argument to warrant a modification of this court s decision, the court resolves to deny consideration with finality.

The Philippine Congress is considering five bills, each of which, if passed by Congress and enacted into law, would impose a 7% or 10% tax on the gross receipts of cellular operators. The proposed taxes would apply to both cellular calls and cellular data revenues and prohibit cellular operators from imposing additional charges or fees to compensate for the imposition of the proposed taxes.

We may be subject to significant local business and franchise taxes if we are unsuccessful in legal proceedings, which are pending

We are currently facing various lawsuits for local business and franchise taxes assessed by different local government units, or LGUs as described under Item 8. Financial Information Legal Proceedings Taxation Local Business and Franchise Taxes. Generally, each province may impose local franchise tax at a rate of up to 0.5% of the gross annual receipts received or realized within that province. Cities within each province may also impose annual franchise taxes on gross annual receipts received or realized in those cities, at a rate that may not exceed the provincial franchise tax rate by more than 50%. In one case, involving the City of Davao, the Supreme Court has ruled that we are not exempt from payment of local business and franchise taxes. On March 25, 2003, the Supreme Court denied our motion for reconsideration and affirmed the local franchise tax assessment of Davao City in the amount of approximately Php4 million. Subsequently, PLDT paid the Davao City government franchise taxes covering the period 1999 to 2003, including the Php4 million, but we are seeking reconsideration of the surcharges and interests of about Php10 million imposed by the Davao City government. Although the Supreme Court decision would constitute a precedent, this will not automatically result in the termination of the other pending local franchise tax cases, with the courts rendering decisions adverse to us. While the courts in these cases are expected to adhere to this Supreme Court decision, each court would have to make its own determination based on the evidence introduced by the parties and the factual circumstances of each case. We cannot assure you that other LGUs will not file lawsuits against us or otherwise claim amounts owed in respect of business and franchise taxes. If the courts rule against us, we would be liable for these taxes, including interest and penalties, for past periods to the extent these taxes are assessed within five years from the date they were due and for future periods.

As of December 31, 2003, the aggregate amount claimed by the plaintiffs in these lawsuits was Php5,142 million with respect to PLDT, Php313 million with respect to Smart and Php45 million with respect to Piltel. We believe that in the event these lawsuits and protests were decided against us, in many cases, we would not be liable for the full amounts claimed by the local governments because these amounts (1) were computed based on the gross annual receipts received or realized not only from within the related province or city for the related period but also from gross annual receipts received or realized from other provinces or cities and (2) include assessments for periods occurring more than five years before the respective lawsuits were filed. Accordingly, in the event these lawsuits are decided against us, we believe that our potential liability is likely to be significantly lower than the amounts claimed by the plaintiffs.

Risks Relating to the Philippines

Our business may be affected by political or social instability in the Philippines

In the past three years, an increasing number of kidnapping, criminal and terrorist activities have occurred in Mindanao, principally led by the extremist "Abu Sayyaf" group, which reportedly has ties to the Al-Qaeda terrorist network. There have been a series of bombing incidents in key cities in Mindanao, including Davao City. The armed conflict between the Philippine military and the communist Moro Islamic Liberation Front also continues in Mindanao. This social unrest negatively impacted the operations of Piltel s fixed line business in Mindanao.

In November 2001, members of the rebel groups damaged three of our cell sites located in Central Luzon and one of our relay stations, including some radio facilities, in Southern Mindanao in response to our failure to pay revolutionary taxes demanded by these groups. On July 27, 2003, approximately 300 Philippine soldiers took control of a shopping center and apartment complex in Makati City in an effort to express their dissatisfaction with the Philippine government. The mutineers surrendered within 20 hours. The government has reported that the actions taken by the approximately 300 Philippine soldiers were part of a coup attempt. In October 2003, a group of unidentified armed men inflicted minor damage to Smart s cell site in Bicol.

On May 10, 2004, the Philippines held a presidential elections, as well as elections for members of the Senate and the Congress. The canvassing of votes has just been concluded and resulted in a victory by the incumber President Gloria Macapagal-Arroyo who successfully retained her post. The opposition has alleged irregularities in the presidential elections, such as stolen ballots and vote buying, and has threatened street protests. We cannot assure you that political events or terrorists activities will not result in major public protest or the involvement of the military in politics. Any political instability in the future may have a negative effect on our results of operations and financial condition. We cannot assure you that the political environment in the Philippines will be stable or that the current or any future government will adopt economic policies conducive to sustained economic growth or which do not impact adversely on the current regulatory environment for telecommunications or other companies.

Our results of operations may be negatively affected by slow growth rates and economic instability in the Philippines and in Asia

In the past, the Philippines has experienced periods of slow growth, high inflation, significant devaluation of the peso, imposition of exchange controls, debt restructuring and electricity shortages and blackouts, and has been significantly affected by economic volatilities in the Asian Region.

In 2003, the Philippine government incurred a fiscal deficit of Php199,900 million which was lower by approximately 6% from the Php212,000 million incurred in 2002. The fiscal deficit incurred for 2003 represents 4.7% of the nominal gross domestic product, or GDP.

On January 27, 2004, Moody s downgraded the Philippine Government s long-term foreign currency bond rating to Ba2 with a negative outlook citing concerns over the government s fiscal deficit and unsettled political dynamics. While Moody s upgraded PLDT s foreign currency senior unsecured debt rating to Ba2 on the same day, PLDT outlook was constrained to negative by Moody s reflecting the outlook on the Philippine Government s rating. In case the Philippine sovereign rating is downgraded by Moody s, it is highly likely that PLDT s credit rating would be downgraded as well.

The growing government fiscal deficit and a global increase in oil prices, have resulted in increased concerns about the political and economic stability in the Philippines. This, in turn, has resulted in the depreciation of the peso against the U.S. dollar and the volatility of the prices of shares traded on the domestic stock market. We cannot assure you that these factors will not affect our results of operations in a materially adverse manner.

If foreign exchange controls were to be imposed, our ability to meet our foreign currency payment obligations could be adversely affected

Approval from or registration with the BSP for the issuance and guarantee of foreign currency denominated borrowings is not required in order to make our foreign currency payment obligations legally valid and binding. However, receiving this approval and registration will enable a borrower to access the banking system to obtain foreign currency to service its debt obligations rather than using other sources of foreign currency, for example, foreign currency revenue streams.

The Philippine government has, in the past, instituted restrictions on the conversion of the peso into foreign currency and the use of foreign exchange received by Philippine companies to pay foreign currency-denominated obligations. The Monetary Board of the BSP has statutory authority, with the approval of the President of the Philippines, during a foreign exchange crisis or in times of national emergency, to:

- suspend temporarily or restrict sales of foreign exchange;

- require licensing of foreign exchange transactions; or

- require the delivery of foreign exchange to the BSP or its designee banks.

We cannot assure you that foreign exchange controls will not be imposed in the future. If imposed, these restrictions could materially adversely affect our ability to obtain foreign currency to service our foreign currency obligations.

The occurrence of natural catastrophes may materially disrupt our operations

The Philippines has experienced a number of major natural catastrophes over the years including typhoons, volcanic eruptions and earthquakes that may materially disrupt and adversely affect our business operations. We cannot assure you that the insurance coverage we maintain for these risks will adequately compensate us for all damage and economic losses resulting from natural catastrophes.

Item 4. Information on the Company

Overview

We are the leading national telecommunications service provider in the Philippines. Through our three principal business groups wireless, fixed line, and information and communications technology we offer a wide range of telecommunications services to over 15 million wireless and fixed line subscribers in the Philippines across the nation's most extensive fiber optic backbone and fixed line, cellular and satellite networks.

We are the leading fixed line provider in the Philippines with approximately 65% of the total reported fixed lines in service nationwide as of December 31, 2003. Smart, our wholly-owned subsidiary, is the leading cellular service provider in the country, with approximately 46% of total reported cellular subscribers as of December 31, 2003. Piltel, our 45.3%-owned subsidiary, had approximately 13% of total reported cellular subscribers as of December 31, 2003. We have interests in the information and communications technology sectors, including Infocom, one of the leading ISPs in the Philippines.

Our common shares are listed on the Philippine Stock Exchange, or PSE, and our American Depositary Shares are listed on the New York Stock Exchange and the Pacific Exchange. We had a market capitalization of approximately Php181,178 million (US$3,259 million) as of May 31, 2004, representing one of the largest market capitalizations among Philippine-listed companies. For the year ended December 31, 2003, we had consolidated revenues and EBITDA of Php112,036 million (US$2,016 million) and Php44,055 million (US$793 million), respectively. See footnote 5 to the selected financial data table in Item 3. Key Information Selected Financial Data for a quantitative reconciliation of EBITDA on a consolidated basis to income (loss) before minority interest in net income of consolidated subsidiaries.

Our principal executive offices are located at the Ramon Cojuangco Building, Makati Avenue, Makati City, Philippines and our telephone number is (632) 816-8024. Our website address is *www.pldt.com.ph*. The contents of our website are not a part of this annual report.

Historical Background and Development

PLDT was incorporated under the old Corporation Law of the Philippines (Act 1459, as amended) on November 28, 1928, following the merger of four telephone companies under common U.S. ownership. Under its amended Articles of Incorporation, PLDT s corporate term is limited through 2028. In 1967, effective control of PLDT was sold by General Telephone and Electronics Corporation (a major shareholder since PLDT s incorporation) to a group of Filipino businessmen. In 1981, in furtherance of the then existing policy of the Philippine government to integrate the Philippine telecommunications industry, PLDT purchased substantially all of the assets and liabilities of the Republic Telephone Company which at that time was the second largest telephone company in the Philippines. During 1998, First Pacific, through its Philippine and other affiliates, acquired a significant interest in PLDT. On March 24, 2000, NTT Communications, through NTTC-UK, became PLDT s strategic partner with approximately 15% economic and voting interest in the issued common capital stock of PLDT. Simultaneous with NTT Communications investment in PLDT, we acquired 100% of Smart.

PLDT s original franchise, which was granted in 1928, was last amended in 1991 to be extended until 2028. The amended franchise (R.A. 7082), which became effective on August 24, 1991, also broadened PLDT s franchise to permit PLDT to provide virtually every type of telecommunications service. PLDT s franchise covers the business of providing basic and enhanced telecommunications services in and between the provinces, cities and municipalities in the Philippines and between the Philippines and other countries and territories including mobile, cellular, wired or wireless telecommunications system, fiber optics, multi-channel transmission distribution systems and their value-added services such as but not limited to transmission of voice, data, facsimile, control signals, audio and video, information services bureau and all other telecommunications systems technologies, as are at present available or can be made available through technical advances or innovations in the future. See Item 8. Financial Information Legal Proceedings Quo Warranto Action for information regarding legal proceedings initiated by the Solicitor General with respect to PLDT s franchise.

Since the implementation of its Subscriber Investment Plan, or SIP, in 1973 pursuant to Presidential Decree No. 217, which, until April 21, 2003, required telephone subscribers to purchase shares of PLDT's preferred stock, PLDT has developed a broad base of public ownership with approximately 2,207,008 common and preferred shareholders of record as of December 31, 2003. Approximately 2,190,318 of these shareholders are Philippine persons representing approximately 88% of PLDT's outstanding common and preferred shares. For purposes of the percentages described in this paragraph, all the ADSs evidenced by American Depositary Receipts, or ADRs, are considered to be held of record in the United States. As approved by the NTC, the purchase of PLDT preferred shares by PLDT subscribers pursuant to the SIP became optional starting April 22, 2003.

On a consolidated basis, capital expenditures amounted to Php17,943 million, Php17,239 million and Php28,201 million in 2003, 2002 and 2001, respectively. Of these amounts, Php6,100 million, Php8,194 million and Php9,252 million were attributable to PLDT for 2003, 2002 and 2001, respectively, while Php11,305 million, Php7,564 million and Php17,961 million were spent by Smart for 2003, 2002 and 2001, respectively. The remaining balances were spent by our other subsidiaries, principally ePLDT and its subsidiaries.

Organization

Our two largest shareholders are First Pacific, a Hong Kong-based investment and management company engaged in consumer, telecommunications and property businesses, which, through its Philippine and other affiliates, beneficially owns 31.4% of our common shares, and NTT Communications, a wholly-owned subsidiary of Nippon Telegraph and Telephone Corporation of Japan, which beneficially owns 14.9% of our common shares.

PLDT and the following subsidiaries were all incorporated in the Philippines, except for PLDT Global, which was incorporated in the British Virgin Islands:

		Percentage of Ownership		
Name of Subsidiary/Investee	**Principal Activity**	**2003**	**2002**	2001
Wireless				
Smart and subsidiaries	Cellular mobile services	100.0	100.0	100.0
Telesat	Satellite communications services	94.4	94.4	94.4
ACeS Philippines	Satellite phone services	93.7	93.7	93.7
Mabuhay Satellite	Satellite communications services	67.0	67.0	67.0
Piltel and subsidiaries	Cellular mobile and telecommunications services	45.3	45.3	45.3
Fixed Line				
Clark Telecom	Telecommunications services	100.0	100.0	100.0
Subic Telecom	Telecommunications services	100.0	100.0	100.0
Smart-NTT Multimedia, Inc.	Data and network services	100.0	100.0	100.0
PLDT Global and subsidiaries	Telecommunications services	100.0	100.0	100.0
PLDT-Maratel	Telecommunications services	97.5	97.5	92.3
BCC	Telecommunications, infrastructure and related value-added services	75.0	37.5	
Information and Communications Technology				
ePLDT and subsidiaries		100.0	100.0	100.0

Information and communications infrastructure for internet-based services, e-commerce, call centers and IT-related services

Wireless

We provide cellular, satellite, VSAT and other services through our wireless business segment. Revenues from our wireless services accounted for 58% of our consolidated operating revenues for the year ended December 31, 2003.

Our cellular service (including handset sales), which accounted for about 99% of our wireless business revenues for the year ended December 31, 2003, is provided through Smart and Piltel. Smart is the leading cellular service provider in the Philippines, with approximately 10.1 million subscribers as of December 31, 2003, representing an estimated market share of approximately 46%. Piltel, a reseller of Smart's digital GSM capacity under its own branding and pricing strategy for voice and text messaging services, had approximately 2.9 million subscribers as of December 31, 2003, representing an estimated market share of 13%. In 2003, the combined number of Smart's and Piltel's subscribers (being served using Smart s GSM network) increased by 51%, representing the largest increase in the number of cellular subscribers in absolute terms in that period among Philippine cellular providers. As of December 31, 2003, cellular penetration in the Philippines was approximately 27%, which was nearly seven times the country's fixed line penetration.

Smart's and Piltel's cellular subscriber gains were predominantly attributable to their respective prepaid GSM services, which were introduced in September 1999 and April 2000, respectively. Approximately 98% of Smart's cellular GSM subscribers were prepaid as of December 31, 2003. The predominance of prepaid service reflects one of the distinguishing characteristics of the Philippine cellular market. The growth in our prepaid service has enabled us to increase and broaden our subscriber base rapidly while controlling credit risk and reducing billing and administrative costs on a per-subscriber basis.

Our cellular subscriber growth has also been driven by text messaging service. Text messaging service is extremely popular in the Philippines, particularly on the prepaid platform, as it provides a convenient and inexpensive alternative to voice and e-mail based communications. During 2003, our text messaging service system handled 28,825 million outbound messages, an increase of 47% compared to 19,558 million outbound messages handled during 2002.

As of December 31, 2003, Smart's digital GSM network included 32 switching centers with a capacity of 14.3 million subscribers and 3,904 base stations covering 1,039 cities and municipalities. Piltel s prepaid GSM service, *Talk N Text*, is also supported on this network. In addition, Piltel had six active cell sites as of December 31, 2003.

Fixed Line

We are the leading fixed line operator in the Philippines and the only company providing fixed line telecommunications service throughout the country. Our fixed line business group offers local exchange, international long distance, national long distance, data and other network and miscellaneous services. As of December 31, 2003, we had approximately 2.1 million fixed lines in service. Revenues from our fixed line services accounted for 41% of our consolidated operating revenues for the year ended December 31, 2003.

We have a 5,400-kilometer long digital fiber optic backbone, which is supported by an extensive digital microwave backbone. Our fixed line network reaches all of the major cities and municipalities in the Philippines, with a concentration in the Metropolitan Manila area. Our network offers the country s most extensive connections to international networks through three international gateway switching exchanges, satellite systems and various regional submarine cable systems in which we have interests.

Information and Communications Technology

Through our wholly-owned subsidiary, ePLDT, we provide broad-based integrated information and communications, or ICT, services focusing on infrastructure and solutions for internet applications, internet protocol-based solutions and multimedia content delivery. Incorporated in August 2000, ePLDT started commercial operations in February 2001. ePLDT's principal activities are the operation of an internet data center under the brand name *Vitro* , call center businesses and Infocom, an ISP.

ePLDT has also invested in a number of other e-commerce and internet-related businesses, as described in Business Information and Communications Technology Infrastructure and Services Other Investments below.

As a new business, revenues from our information and communications technology services accounted for 1% of our consolidated operating revenues in 2003.

Strengths

We believe our business is characterized by the following competitive strengths:

• *Recognized Brands*. PLDT and Smart are strong and widely recognized brand names in the Philippines. We have built the PLDT brand name for 75 years as the leading telecommunications provider in the Philippines. Smart is recognized in the Philippines as an innovative provider of high-quality cellular services. Piltel s *Talk 'N Text* brand, which is provided using Smart s GSM network, has also gained significant recognition.

• *Leading Market Shares*. With over 15 million wireless and fixed line subscribers as of December 31, 2003, we have the leading market position in both the fixed line and cellular markets in the Philippines. ePLDT s subsidiary, Infocom, is one of the leading ISPs in the Philippines.

• *Diversified Revenue Sources*. As a result of the continued growth of wireless service in the country, approximately 58% of our consolidated operating revenues in 2003 are now derived from our wireless business segment. Fixed line revenues, which represent 41% of our consolidated revenues in 2003 compared to 49% in 2002, have remained stable over the past three years despite pressures on traditional fixed line voice revenues, resulting from increases in our international long distance, fixed line data and other network services. We continue to identify and develop new revenue sources from our wireless, fixed line and ICT businesses.

• *Advanced Integrated Network*. With one of the most advanced and extensive telecommunications networks in the Philippines, we are able to offer a wide array of communications services. We are enhancing the capabilities of our fixed line and wireless networks to allow us to better exploit this competitive strength and achieve higher levels of network efficiency in providing voice and data services.

• *Innovative Products and Services*. We have successfully introduced a number of innovative and award-winning cellular products and services, including *Smart Load, Talk N Text Load* and *Pasa Load. Smart* and *Talk N Text Loads* are over-the-air electronic loading facilities designed to make reloading of air time credits more convenient for, and accessible to consumers. *Pasa Load* (literally means transfer load), a derivative service of *Smart and Talk N Text Loads,* allows load transfers to other *Smart Buddy* and *Talk N Text* subscribers.

• *Strong Strategic Relationship*. We have an important strategic relationship with NTT Communications and First Pacific. The technological support, international experience and management expertise made available to us through these strategic relationships enhance our market leadership and ability to provide and cross-sell a more complete range of products and services.

Strategy

The key elements of our business strategy are:

• *Build on our leading positions in the wireless and fixed line businesses*. We plan to build on our position as the leading wireless service provider in the Philippines by continuing to introduce new products and services to increase our subscribers use of our network for both voice and data, as well as their reliance on our services. We also plan to further increase the capacity and expand the geographic reach of our cellular network, as well as to improve our service quality and indoor coverage. Our operating target is to continue growth in profitability by increasing our revenues while controlling costs. We plan to build on our position as the leading provider of fixed line service in the Philippines by continuing to launch new products and services to increase subscriber value and utilization of our existing facilities and equipment at reduced cost.

- *Capitalize on our strength as an integrated provider of telecommunications services*. We offer the broadest range of telecommunications services among all operators in the Philippines. We plan to capitalize on this position to maximize revenue opportunities by bundling and cross-selling our products and services between voice and data and fixed line and cellular. We are also lowering our costs by integrating the operations of our different businesses.

- *Strengthen our leading position in the data market*. Recognizing the significant growth potential of data and other network services, including internet-based services, and their increasing importance to PLDT's overall business strategy, we are emphasizing the development of our data and network business segment to address the needs of large corporations, small and medium-sized enterprises and retail customers. We have launched a variety of products and services, including data network services like digital leased lines, frame relay, asynchronous transfer mode, or ATM, internet Protocol Virtual Private Network, or IP-VPN. We are progressively introducing internet-based services such as digital subscriber line, or DSL to our corporate and residential clients, International internet Gateway or I-Gate for ISPs and large corporations.

- *Strengthen our financial position*. We are engaged in a number of initiatives to strengthen our financial position. We are working to increase our cash flow available for debt reduction by containing our operating costs, reducing capital expenditures and generating cash returns from our investments in subsidiaries. In December 2002, Smart made its first dividend payment of Php1,540 million (not to exceed 40% of its net income in 2001) to PLDT to supplement PLDT s cash flows available for debt reduction, followed by Php4,300 million in June 2003 and Php1,866 million in November 2003 (representing dividends equivalent to 70% and 30%, respectively, of its 2002 net income) and Php11,280 million in May 2004 (representing 70% of Smart s 2003 net income under Philippine GAAP.)

Business

Wireless

We provide cellular and satellite, VSAT and other services through our wireless business segment.

Cellular Service

Overview

Our cellular business, which we provide through Smart and Piltel to approximately 13 million GSM subscribers, more than 98% of whom are prepaid subscribers, is focused on providing wireless voice communications, wireless data communications (primarily through text messaging) and a variety of other value-added services, which include (a) *Mobile Banking* (banking services delivered over the mobile phone); (b) *Smart zedTM*; (c) *Smart Money*; and (d) international roaming, as well as other value-added services developed on Smart s and Piltel s own platform. Smart services the almost three million subscribers of Piltel on its GSM network through a facilities service agreement with Piltel, under the brand name *Talk N Text*.

The following table summarizes key measures of our cellular business as of and for the years ended December 31, 2003, 2002 and 2001:

	Years Ended December 31,		
	2003	**2002**	**2001**
Systemwide cellular subscriber base	12,947,197	8,599,306	6,368,850
Smart	10,080,112	6,825,686	4,893,844
GSM	10,080,112	6,825,686	4,641,666
Prepaid	9,831,135	6,649,038	4,569,616
Postpaid	248,977	176,648	72,050
Analog/ETACS (1)			252,178
Prepaid			87,429
Postpaid			164,749
Piltel	2,867,085	1,773,620	1,475,006
GSM Prepaid(2)	2,867,085	1,773,620	1,329,326
Analog/CDMA(1)			145,680
Prepaid			76,473
Postpaid			69,207
Growth rate of cellular subscribers	51%	35%	81%
Smart	48%	39%	71%
GSM	48%	47%	99%
Analog/ETACS		(100%)	(52%)
Piltel	62%	20%	125%
GSM Prepaid(2)	62%	33%	261%
Analog/CDMA		(100%)	(49%)
Cellular revenues (in millions)	Php63,434	Php45,565	Php32,835
Service (3)	51,001	30,583	19,820
Handset sales	12,433	14,982	13,015
Percentage of cellular revenues to total operating revenues	57%	49%	41%

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(1) In December 2002, Smart closed down its analog/ETACS network. In 2001, Piltel recognized impairment losses in respect of its AMPS/CDMA network.

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(2) Represents Talk N Text, a prepaid GSM service provided by Piltel using Smart s GSM network. Piltel s GSM revenue is net of service fees payable to Smart for using Smart s GSM network. Piltel does not offer postpaid GSM service.

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(3) Refers to GSM and analog voice and data revenues.

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Service Plans. Smart markets nationwide cellular communications services under the brand names *Smart Buddy, Smart Gold, addict mobile* and *Smart Infinity. Smart Buddy* is a prepaid service while *Smart Gold, addict mobile* and *Smart Infinity* are postpaid services, all of which are provided through Smart's digital GSM network.

Of Smart s total cellular subscribers as of December 31, 2003, 98% were *Smart Buddy* prepaid subscribers and 2% were *Smart Gold, addict mobile* and *Smart Infinity* postpaid subscribers. Introduced in April 2003, *addict mobile* offers exclusive multimedia content to subscribers and features personalized means for internet surfing and allows subscribers to apply their allocated free credits towards their choice of data and value-added services. *Smart Infinity* is a premium postpaid plan launched in January 2004 for the affluent and highly mobile market, offering first class quality services, including a round-the-clock dedicated personal concierge service, international assistance services, premium handset packages and exclusive lifestyle content. Before Smart decommissioned its analog/ETACS network in December 2002, it had also offered analog prepaid and postpaid services under the brand names *BillCrusher* and *PriceBuster*, respectively.

Piltel markets its cellular services under the brand name *Talk 'N Text*, a prepaid service provided using Smart s GSM network pursuant to a facilities service agreement between Smart and Piltel. As of December 31, 2003, Piltel s *Talk 'N Text* subscribers reached 2,867,085.

Text Messaging Service and Other Value-added Services. Our cellular subscriber growth has been driven by text messaging service on GSM networks. Text messaging is extremely popular in the Philippines, particularly on the prepaid platform, as it provides a convenient and cost-efficient alternative to voice and e-mail based communications. Text messaging also utilizes less network capacity than voice, thereby increasing network efficiency. Strong volume growth in text messaging contributed significantly to our cellular revenue growth in 2003. The total volume of messages handled by our text messaging service system during 2003 increased by 47% to 28,825 million outbound messages from 19,558 million outbound messages handled during 2002.

Our value-added services are primarily based on text messaging service technology. Since 2000, Smart launched the following value-added cellular services:

- *Smart zed* , a partnership with international cellular operator Sonera zed Ltd., or Sonera zed, of Finland, enables subscribers to personalize their information requirements not only as to the types of information required but also when the information is required. Sonera zed has introduced a single platform that provides access to local and global information through text messaging or wireless application protocol;

- *Mobile Banking*, launched in collaboration with various banks, allows subscribers to execute banking transactions, such as balance inquiries and transfers, over their mobile telephones; and

- *Smart Money*, launched in conjunction with MasterCard, enables subscribers to pay for their purchases by transferring money from their bank accounts to their Smart Money cards as well as reload their prepaid cards electronically.

We also offer value-added services such as voice mail, information-on-demand, which is a service that allows subscribers to order information from our content providers whenever desired, mobile banking and *TextMail*, which is a service that allows subscribers to send and receive text messages through their personal computers and location-based services. In addition, we have a number of interactive activities, such as text games and chat services, developed on our own platforms.

Smart Money was cited as the "Best Product Innovation" by MasterCard International and the "Most Innovative GSM Wireless Service for Customers" at the 3rd GSM World Congress held in Cannes, France, in March 2001. In February 2004, at the sixth GSM World Congress, *Smart Load,* an over-the-air electronic loading facility designed to make reloading of air time credits more convenient for and accessible to subscribers was cited as the Best Mobile Application or Service for the Consumer Market.

Due to the high level of text messaging service usage, we believe that the Philippine market is well suited for text-based informational and e-commerce services. Our current approach is to continue maximizing our GSM, or 2G, services and also offer General Packet Radio Service, or GPRS or 2.5G, to service increased demand for bandwidth-intensive applications. GPRS allows data transfer at an average speed of up to 115 kilobits per second. In addition, we continue to upgrade our network to Enhanced Data for GSM Evolution, or EDGE. EDGE is a technology that would further increase the speed and data capability of our GSM network.

Rates and Discounts

A prepaid cellular subscriber is recognized as an active subscriber when that subscriber activates and uses the SIM card in the handset, which already contains Php100 worth of pre-stored air time. Subscribers can then reload by purchasing prepaid call-and-text cards that are sold in denominations of Php300, Php500 and Php1,000 or, by purchasing additional air time over the air via *Smart Load* and *Talk N Text Load* in smaller denominations of Php30, Php60, Php115 and Php200, by receiving loads of Php2, Php5, Php10 and Php15 via *Pasa Load* (for prepaid subscribers only) or through their handsets using *Smart Money*. Reloads have validity periods ranging from one day to two months, depending on the amount reloaded. A prepaid GSM account is disconnected if the subscriber does not reload within four months after the full usage or expiry of the last reload. As a result, a subscriber would not be included in our churn rate calculation for up to 121 days to six months after the subscriber may have stopped using the service to make calls or send messages (although the subscriber may continue to receive calls and messages). These effects may cause our calculated churn rate for a period to be lower than the actual rate at which subscribers are ceasing to use Smart's and Piltel s services, and may contribute to more rapid growth in calculated churn following periods of rapid subscriber growth.

Smart Buddy and Piltel s *Talk N Text* prepaid cards are sold in denominations of Php300, Php500 and Php1,000, which include 33, 83 and 250 free text messages, respectively. The stored value of a prepaid card remains valid for a period of two months from the time a subscriber activates the card. On May 11, 2003, we introduced *Smart Load* and *Talk N Text Load*, an over-the-air electronic loading facility designed to make reloading of air time credits more convenient for, and accessible to consumers. These over-the-air reloads come in the following denominations and corresponding expiration periods:

Denomination	**Load Expiry**	**Equivalent Values**
Php30	3 days	30 text messages or 4 local call minutes
Php60	6 days	60 text messages or 8 to 9 local call minutes
Php115	12 days	115 text messages or 15 to 17 local call minutes
Php200	30 days	200 text messages or 26 to 30 local call minutes

Smart and *Talk N Text Loads* were followed in January 2004 with *Pasa Load*, a derivative service allowing prepaid subscribers to transfer even smaller denominations to other prepaid subscribers for a charge of Php1.00 per transfer. *Pasa Load* comes in denominations of Php2, Php5, Php10 and Php15, all carrying a one-day load expiry.

Beginning January 2004, *Smart Buddy* subscribers pay the following air time rates per minute: (a) Php6.50 for Smart-to-Smart and Smart-to-*Talk N Text* subscribers; and (b) Php7.50 for Smart-to-other mobile operators, fixed lines and national long distance calls.

Prior to January 2004, *Smart Buddy* subscribers paid a rate of Php8.00 per minute for calls made during peak hours and Php4.00 per minute for calls made during off-peak hours, regardless of whether the calls were made within the Smart network or to other mobile operators networks. From October 25 to December 31, 2003, national long distance calls were charged at Php11.00 per minute for peak hours and Php7.00 per minute for off-peak hours. Previous to that date, *Smart Buddy* subscribers paid varying national long distance rates depending on the destination of the call.

Beginning January 25, 2004, *Smart Gold* launched its flat rate and consumable plans as follows:

• Flat Rate (regular plans) Plans are available with monthly service fees ranging from Php500 to Php8,000 with varying amounts of free air time and text messages and different rates beyond the free minutes and text messages, depending on the monthly service fee. Monthly service fees for these plans are applicable only to local calls and text messages. All other services are billed on top of the monthly service fee; and

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• Consumable plans are available with monthly service fees ranging from Php800 to Php8,000 with different amounts of free air time and text messages and different rates beyond the free minutes and text messages. Subscribers to these plans may apply their monthly service fees to all voice calls, text messages (both local and international) and value-added services.

Under both types of plans, the rates for calls to other mobile operators, landlines and NDD calls are Php1.00 higher than calls within the Smart network.

From January 1, 2002 to January 24, 2004, *Smart Gold* subscribers could choose from seven different subscription plans with monthly services fees ranging from Php500 to Php3,500 with different amounts of free air time and text messages and different rates beyond the free minutes and text messages. Under each of these plans, calls during peak hours and to other mobile operators, landlines and NDD calls were charged at higher rates per minute than calls within the Smart network.

Prior to January 1, 2002, *Smart Gold* offered the following monthly air time plans: Php600, Php1,200, Php1,800, Php3,000 and Php4,000. Subscribers who enrolled in these plans prior to January 1, 2002 remained on these plans following introduction of the plans described above.

From April 12, 2003 to January 24, 2004, *addict mobile* offered seven different subscription plans with monthly services fees ranging from Php500 to Php3,500 with different amounts of free air time and text messages and different rates beyond the free minutes and text messages. Under each of these plans, calls during peak hours to other mobile operators, landlines and NDD calls were charged at higher rates per minute than calls within the Smart network.

On January 25, 2004, *addict mobile* began offering flat rate plans similar to the ones launched for *Smart Gold* on the same day with monthly service fees ranging from Php500 to Php3,500 with different amounts of free air time and text messages and different rates beyond the free minutes and text messages. Under each of these plans, calls to other mobile operators and landlines are charged at higher rates per minute than calls within the Smart network.

Smart is permitted to adjust its cellular air time and national direct dial rates according to changes in the peso-to-U.S. dollar exchange rate. Under the authorization granted to Smart by the NTC, Smart is permitted to increase and is required to decrease its air time and national direct dial rates by 1% for every Php0.25 change in the exchange rate relative to a base rate of Php24.726 to US$1.00. However, Smart has not implemented any foreign currency adjustments to its rates since November 4, 1998 because of the concern that increased rates may result in decreased usage by its subscribers.

All Smart subscribers pay an international direct dialing rate of US$0.40 per minute. This rate applies to 200 destinations, including the United States, Hong Kong, Japan, Singapore, the United Kingdom and the United Arab Emirates. Smart charges US$0.98 per minute for 27 other destinations such as Afghanistan and Cuba and US$2.18 per minute for another ten destinations such as East Timor and the Falkland Islands.

Charges for point-to-point text messages beyond the allotted free text messages are as follows:

• for *Smart Buddy* and *addict mobile* subscribers, Php1.00 per message; and

• for *Smart Gold* and *Smart Infinity* subscribers, Php0.50 or Php1.00 per message, depending on air time plan.

Smart Buddy, Smart Gold and *addict mobile* subscribers pay the same charges for SMS-based value-added services, as follows:

• Php15.00 per message for international text for *Smart Buddy* subscribers and Php10.00 per message for international text under the new *Smart Gold* plans and for *addict mobile* and *Smart Infinity* subscribers;

• Php2.50 per message for e-text and information-on-demand services, such as news, stock and entertainment updates;

• Php15.00 per download of ring tones and logos;

- Php2.50 per Mobile Banking and *Smart Money* transaction, such as balance inquiry and fund transfer; and

- Php10.00 per subscription download.

For multimedia messaging service, or MMS, and wireless application protocol, or WAP, services, the charges are as follows:

- Php5.00 per person-to-person MMS still and animated images;

- Php15.00 per download of pictures, greeting cards, polyphonic ring tones and traffic shots;

- Php2.50 per MMS for e-text and information-on-demand services (such as news, stock and entertainment updates);

- Php2.00 per transaction when surfing on the Smart WAP portal; and

- Php0.25 per kilobyte when surfing outside the Smart WAP portal.

For voice mail retrieval, all Smart subscribers are charged Php6.50 per minute.

In addition to enjoying the same tariffs as *Smart Gold* subscribers, *addict mobile* subscribers are allowed to apply their allocated free credits on their choice of data and value-added services.

We sell our cellular services primarily through a network of independent dealers that generally have their own retail networks, direct sales forces and sub-dealers. These dealers include major distributors of cellular handsets. We currently have six dealers that carry out distribution throughout the Philippines. On December 1, 2002, Smart purchased the assets of Telecommunications Specialists, Inc., or TSI, a major dealer that used to account for more than half of our sales of prepaid air time cards, and integrated TSI s employees following the acquisition. Account managers from our dealer sales force manage our dealer network and regularly update these dealers on our upcoming marketing strategies, promotional campaigns and product development. With the introduction of *Smart Load* and *Talk N Text Load* in May 2003, Smart and Piltel moved into a new mode of distribution. These over-the-air reloads, which were based on the sachet marketing concept of consumer goods such as shampoo and ketchup, required a distribution network more comparable to those of soft drink and beer distributors. Starting with just 50,000 outlets when it was launched, *Smart Load* s distribution network now encompasses over 400,000 retail agents, 80% of which are micro businesses (e.g. neighborhood stores, individuals acting as roving agents).

For prepaid services, we provided discounts to dealers for prepaid phone kits, air time cards and over-the-air reloads sold. Beginning August 1, 2002, Smart and Piltel reduced the maximum discount to dealers for prepaid phone kit sales from a range of Php1,000 to Php1,300 per unit sold in the form of prepaid call and text cards (depending on the volume purchased) to Php800 in cash per prepaid phone kit sold. An additional 1% rebate was given on cash purchases. Air time cards and over-the-air reloads are sold to dealers at volume discounts determined by the value of the cards purchased by the dealers. Discounts for air time cards sold range from 8% to 10% while discounts on over-the-air reloads range from 4% to 5%. Air time cards cannot be returned or refunded and normally expire within six to 12 months after release from the Smart warehouse. For postpaid services, we pay dealer discounts based on the air time plan sold.

Piltel's *Talk 'N Text* prepaid cards are sold in the same denominations and offer the same international direct dialing rates as *Smart Buddy* prepaid cards at US$0.40 per minute to all destinations. In October 2003, Piltel implemented an all-day/all-night flat rate of Php9.50 per minute for local calls, calls to other network and national long distance calls replacing the Php12.00 per minute during peak hours and Php8.00 per minute during off-peak hours. In January 2004, this rate was further reduced to Php6.50 per minute while the rate for *Talk N Text* to *Talk N Text* calls was reduced to a flat rate of Php5.50 per minute from Php6.50 per minute. The same rate of Php5.50 per minute is charged for voice mail retrieval. *Talk N Text* subscribers are charged Php1.00 for a regular text message in excess of free text allocations while for value added services, such as text games, logo and ring tone downloads are charged within a range of Php2.50 to Php15.00 per message.

Satellite and VSAT

Overview

We currently provide satellite and VSAT services through Mabuhay Satellite and Telesat. ACeS Philippines, our satellite phone service provider, started to roll out fixed satellite terminals in the last quarter of 2001.

Mabuhay Satellite

We currently own 67% of Mabuhay Satellite, which is engaged in the control and operation of the Agila II satellite. Commencing commercial operations in January 1998, Agila II is the Philippines' first communications satellite. Mabuhay Satellite leases satellite space segments in both the C and Ku bands on the Agila II. Through Agila II, Mabuhay Satellite also offers internet backbone access, video and data broadcasting, and bandwidth-on-demand, facilitating communication links between telecommunications, broadcast and other public utility companies operating in the Asia-Pacific region. See Item 5. Operating and Financial Review and Prospects Critical Accounting Policies Investments and *Note 8 Investments* to the accompanying consolidated financial statements in Item 18 for a discussion of our investment account in Mabuhay Satellite.

Telesat

We currently own 94.4% of Telesat which operates a nationwide communications satellite network using VSAT technology. Telesat offers voice, facsimile and data transmission services throughout the Philippines, including areas that are underserved or unserved by local fixed line operators.

Using VSAT technology, we also provide the following services:

- point-to-multipoint data transmission services, usually for intercompany communication for corporate customers;

- private point-to-point service; and

- connectivity for the cell sites of our wireless network in outlying locations.

We lease transponder capacity on the Agila II to provide VSAT services.

ACeS Philippines

We currently own 93.7% of ACeS Philippines, which owns approximately 20.23% of AIL, and the remaining 6.3% of ACeS Philippines is owned by other shareholders of Piltel. AIL aims to develop and implement a satellite-based communications system to provide services to users in the Asia-Pacific region through the Garuda I satellite, or ACeS System and ACeS Service. AIL has entered into interconnection agreements and roaming service agreements with PLDT and other major telecommunications operators that will allow ACeS subscribers to access GSM terrestrial cellular systems in addition to the ACeS system. Further, AIL has an Air Time Purchase Agreement, or ATPA, with National Service Providers, or NSPs, in Asia, including PLDT. For further discussion of this ATPA, please see *Note 18 Related Party Transactions* and *Note 23 Contractual Obligations and Commercial Commitments* to the accompanying consolidated financial statements in Item 18.

Revenues

Our satellite and VSAT service revenues consist of:

- lease payments from the rental of Mabuhay Satellite s C-band and Ku-band transponders;
- revenues generated from Telesat s nationwide satellite network; and
- revenues generated from ACeS Philippines satellite phone service.

Rates

Mabuhay Satellite leases its transponders to third parties at annual rates of approximately US$1.5 million and US$1.0 million for its C-band and Ku-band transponders, respectively. Telesat provides its VSAT services on a cost plus mark-up basis. ACeS Service mobile subscribers are charged Php13.84 per minute for local and cell-to-cell calls and for national direct dial services while residential subscribers are charged a peak-hour rate of Php13.00 per minute and an off-peak hour rate of Php8.00 per minute for domestic calls regardless of destination. For ACeS System public calling offices, callers are charged Php4.50 and Php7.00 per minute for calls terminating to fixed line and cellular networks, respectively. Rates for international long distance calls, depending on the country of termination, ranging from US$0.35 per minute for frequently called countries to US$0.85 per minute for less frequently called countries.

Fixed Line

We provide local exchange, international long distance, national long distance, data and other network and miscellaneous services under our fixed line business segment.

Local Exchange Service

Overview

Our local exchange service, which consists of our basic voice telephony business, is provided primarily through PLDT.

The following table summarizes key measures of our local exchange service segment as of and for the years ended December 31, 2003, 2002 and 2001:

	Years Ended December 31,		
	2003	**2002**	**2001**
Number of PLDT local exchange lines in service (at period-end)	2,115,671	2,092,539	2,075,109
Net additions	23,132	17,430	159,124
Growth rate	1%	1%	8%
Number of PLDT employees (at period-end)	10,230	12,131	12,915
Number of local exchange lines in service per employee	207	172	161
Consolidated local exchange revenues (in millions)	Php20,728	Php21,345	Php21,356
Growth rate	(3%)		14%
Local exchange revenues as a percentage of total operating revenues	19%	23%	27%

We also provide local exchange services through our subsidiaries Clark Telecom, Subic Telecom, Maratel and Piltel. Together, these subsidiaries account for approximately 1% of our total fixed lines in service.

We regularly adjust our rates and introduce new products and services in an effort to increase our number of subscribers, improve our churn management efforts and minimize our credit risk exposure. Since 1999, we have launched a prepaid fixed line service, introduced additional value-added services, introduced initiatives aimed at increasing subscription in areas where we have excess capacity and reduced our installation fees, as described below under " Rates."

Initially intended as an alternative affordable telephone service for consumers under difficult economic conditions, our prepaid fixed line services now form an important part of PLDT s overall churn and credit risk exposure management and subscriber retention strategy. For more information on prepaid fixed line services, see Rates below.

To attract new fixed line subscribers and retain existing ones, PLDT has introduced various value-added services such as *Hype* in April 2003. *Hype* is a full two-way fixed line text messaging service, which allows subscribers to send and receive text messages to and from landline and mobile phones, and is capable of international text messaging. *Hype* also allows subscribers to join TV network-based and new PLDT-initiated texting services.

Rates

As of December 31, 2003, basic monthly charges for our local exchange service in the Metropolitan Manila area were Php653.88 for a single-party residential line and Php1,362.66 for a single business line. Monthly charges vary according to the type of customer (business or residential) and location, with charges for urban customers generally being higher than those for rural/provincial customers. In July 2003, we launched the Telegusto promotion waiving installation charges up to December 31, 2003 to encourage subscriber growth. Installation charges amount to Php1,200 for residential customers and Php1,500 for business customers. Other than basic monthly charges, we do not charge our postpaid subscribers for local calls.

Pursuant to a currency exchange rate adjustment mechanism authorized by the NTC, we adjust our monthly local exchange service rates according to changes in the peso-to-U.S. dollar exchange rate. Under the authorization granted to us by the NTC, we are permitted to increase and are required to decrease these rates by 1% for every Php0.10 change in the exchange rate relative to a base exchange rate of Php11 to US$1.00. During 2003, we implemented 11 upward and three downward adjustments in our monthly local exchange service rates.

Effective January 1, 2003, local access charges for cellular subscribers calls that terminate to our fixed line subscribers increased from Php2.00 per minute to Php2.50 per minute, and was further increased to Php3.00 per minute effective January 1, 2004.

A prepaid fixed line subscriber is recognized as an active subscriber when that subscriber activates and uses a prepaid call card. Prepaid fixed line subscribers can reload their accounts by purchasing call cards that are sold in denominations of Php500, Php300 and Php150. Reloads are valid for two months for the Php500 and Php300 card. The lower denomination of Php150 card, launched in September 2003, has an account life of 15 days. A prepaid fixed line subscriber is disconnected if that subscriber does not reload within one month for the Php500 card, four months for the Php300 card, and 15 days for the Php150 card after the expiry of the last reload. All sales of prepaid cards, whether through dealers or through PLDT's business offices, are non-refundable. Our prepaid fixed line customers do not pay a basic monthly charge and are charged based on usage. For local calls, prepaid fixed line customers are charged based on usage at a rate of Php1.00 per minute. The international and national long distance rates we charge to our prepaid fixed line customers are similar to the rates we charge our postpaid customers. For a description of these rates, see " International Long Distance Service Rates" and " National Long Distance Service Rates." Prepaid phone kits, each containing Php500 worth of pre-stored call credits, are sold for Php1,900 per unit.

International Long Distance Service

Overview

Our international long distance service consists of voice and packet-based voice services that go through our international gateway facilities. We also generate international long distance revenues through access charges paid to us by other Philippine telecommunications carriers for incoming international voice calls that terminate to our local exchange network. Our packet-based voice services are transmitted over our existing traditional circuits: voice over internet protocol, or VOIP; network of a consortium of dominant carriers in Asia; ATM; and internet protocol global backbone of PLDT Global.

The following table shows certain information about our international long distance business as of and for the years ended December 31, 2003, 2002 and 2001:

	Years Ended December 31,		
	2003	**2002**	**2001**
Total PLDT call volumes (million minutes)	2,183	2,576	2,814
Growth rate	(15%)	(8%)	18%
Inbound call volumes (million minutes)	2,028	2,409	2,648
Growth rate	(16%)	(9%)	18%
Outbound call volumes (million minutes)	155	167	166
Growth rate	(7%)	1%	18%
Inbound-outbound call ratio	13.1:1	14.4:1	16:1
Consolidated international long distance revenues (in millions)	Php12,634	Php10,636	Php11,701
Growth rate	19%	(9%)	(12%)
International long distance revenues as a percentage of total operating revenues	11%	11%	15%

International long distance service historically has been a major source of revenue. However, due to the steep decline in inbound termination and collection rates and intense competition, revenues derived from our international long distance service had been declining through the end of 2002. We adopted a two-pronged initiative in early 2000 with respect to inbound international service to try to address this issue. First, we lowered our inbound termination rates at that time.

By reducing our rates, we reduced the incentive for unauthorized traffic termination and bypass routings by international simple resale operators, and therefore were able to recover some lost traffic. Secondly, we intensified our efforts to identify and contain unauthorized traffic termination and bypass through more effective monitoring of our international trunks, leased lines or local network. International simple resale operation occurs when a company rents an international leased line from a Philippine international gateway operator, aggregates traffic outside the Philippines and carries and terminates this traffic at the public switch telephone network in the Philippines. International simple resale can be used to bypass the local access charge system, which is illegal in the Philippines.

Since 2001, we have become more selective in accepting incoming traffic from some carriers, particularly second and third tier international carriers. In addition, we adopted a policy requiring prepayment from certain second and third tier international carriers as a prerequisite for accepting their incoming traffic.

We are also pursuing a number of other initiatives to further strengthen our inbound business. Through PLDT Global, we aggregate inbound call traffic to the Philippines at our points of presence and, using our capacity in submarine cable systems connected to each point of presence, transmit calls to our network. PLDT Global is also enhancing the presence of PLDT in other international markets by offering new products and services such as international prepaid cards, SMS transit and other global bandwidth services. We believe this strategy will help us maximize the use of our existing international facilities, and develop alternative sources of revenue.

To stimulate call volume growth and prevent further erosion in our share of outbound international call traffic, we have introduced a number of marketing initiatives, including substantial cuts in international direct dialing rates, innovative pricing packages for large accounts and loyalty programs for some customers.

The table below sets forth the net settlement amounts for international calls handled by PLDT, by country, for the years ended December 31, 2003, 2002 and 2001:

	Net Settlement Years Ended December 31, (in millions)		
	2003	**2002**	**2001**
United States	US$52	US$68	US$82
Saudi Arabia	15	5	7
Canada	15	7	10
Italy	14	5	6
Japan	12	16	23
Australia	11	5	18
United Arab Emirates	10	8	3
Hong Kong	9	3	7
Taiwan	4	6	3
Others	77	63	41
Total	US$219	US$186	US$200

Rates

We adopted the U.S. FCC accounting rate benchmark of US$0.38 per minute for inbound international calls on January 1, 2000, which represented a settlement rate of US$0.19 per minute, for international long distance traffic between the Philippines and the United States. Adopting the U.S. FCC benchmark accounting rate one year ahead of the target date of January 1, 2001 allowed us pricing flexibility for inbound call traffic. Termination rates for inbound calls from the United States continued to decline through the end of 2002 to levels below the U.S. FCC benchmark accounting rate under pressure from unauthorized terminations and bypass operations. Termination rates for inbound calls from other countries have also been declining generally. As of December 31, 2002, a substantial portion of PLDT s international inbound traffic terminating on its fixed line network was charged an average termination rate of approximately US$0.08 per minute. PLDT increased termination rates with carriers accounting for a substantial portion of its international inbound traffic terminating on its fixed line network to an average of approximately US$0.12 per minute effective February 1, 2003. See Item 8. Financial Information Legal Proceedings U.S. Federal Communications Commission, or FCC, Ruling versus Philippine Telecommunications Companies , Investigation by U.S. Department of Justice and *Note 28 Other Matters* to the accompanying consolidated financial statements in Item 18 for further discussion.

Rates for outbound international long distance calls are based on the length of the call, country of destination, and type of service such as operator-assisted and direct-dialed calls. Our rates are quoted in U.S. dollars and billed in pesos. The peso amounts are determined at the time of billing.

Effective February 1, 2001, PLDT reduced its international direct dialing, or IDD, rates for retail customers from US$0.49 per minute for off-peak hours and US$0.69 per minute for peak hours to a flat rate for retail customers of US$0.40 per minute, applicable to all call destinations at any time on any day of the week. Additionally, in November 2001, PLDT introduced *Budget Card*, a prepaid call card offering a reduced IDD rate of US$0.24 per minute for calls to 20 overseas destinations including the United States, Canada, Japan and China. *Budget Cards* are sold in a denomination of Php200, which must be consumed within 30 days from first use.

National Long Distance Service

Overview

Our national long distance services are provided primarily through PLDT. This service consists of voice services for calls made by our fixed line customers outside of their local service areas within the Philippines and access charges paid to us by other telecommunications carriers for calls carried through our backbone network and/or terminating to our fixed line customers.

The following table shows our national long distance call volumes and revenues as of and for the years ended December 31, 2003, 2002 and 2001:

	Years Ended December 31,		
	2003	**2002**	**2001**
Total PLDT call volumes (million minutes)	2,017	2,145	2,756
Growth rate	(6%)	(22%)	(15%)
Consolidated national long distance revenues (in millions)	Php6,694	Php7,818	Php8,500
Growth rate	(14%)	(8%)	(19%)
National long distance revenue as a percentage of total operating revenues	6%	8%	11%

Cellular substitution and the widespread availability and growing popularity of alternative, more economical, non-voice means of communications, particularly e-mailing and cellular text messaging, have negatively affected our national long distance call volumes. The integration of some of our local exchanges into a single local calling area effective August 2000, as approved by the NTC, has also negatively affected our national long distance call volumes, and consequently, our revenues. Because of this integration, calls between two exchanges located within the same province are no longer considered national long distance calls but are treated as local calls.

A substantial portion of our national long distance calls were direct-dialed calls. Operator-assisted calls are charged based on a minimum of three minutes plus operator charges, while direct-dialed calls are charged on a less costly per minute basis.

We offer various *PLDT Premium Phone Services*, which allows customers to choose from a range of service applications, such as appointment-booking services for select embassies in the Philippines (including, among others, the U.S. and Australian embassies), spiritual and love counseling, joining television-based game shows, celebrity chatting, downloading and sending of ring tones and logos, televoting, job postings, and *myMusic*, a music entertainment line to various popular artists. PLDT charges a minimum of Php10.00 per minute for these premium phone services.

Rates

Rates for national long distance calls are based on type of service, such as whether the call is operator-assisted or direct-dialed. In the latter part of 2001, PLDT simplified its rates for calls to fixed line subscribers and for those terminating to cellular subscribers resulting in an overall rate increase. For calls terminating to fixed line subscribers, the applicable rates from January to November 1, 2001 ranged from Php3.00 per minute to Php5.00 per minute, depending on distance and time of call. In line with its move towards rate simplification, PLDT simplified these rates to a flat rate of Php4.50 per minute effective November 2, 2001. At the same time, PLDT simplified its rates for calls terminating to cellular subscribers from a range of Php10.00 per minute to Php16.00 per minute to a uniform rate of Php13.75 per minute. Effective March 1, 2003, PLDT increased the rate for calls terminating to other local exchange carriers from a flat rate of Php4.50 per minute to Php5.00 per minute. In addition, NDD calls originating from and terminating to PLDT was also adjusted to Php5.00 per minute from a flat rate of Php4.50 per minute effective June 8, 2003. Through rate simplification, we aim to simplify our tariff structure in order to enhance the competitiveness of our products and services and increase our operating efficiencies. We adopted these simplified pricing plans with a view to maximizing our national long distance revenues going forward.

PLDT entered into new interconnection agreements with local exchange carriers and cellular operators. In particular, in May 2001, PLDT entered into an interconnection arrangement with the majority of other local exchange carriers, pursuant to which the originating carrier pays (1) a hauling charge of Php0.50 per minute for short-haul traffic or Php1.25 per minute for long-haul traffic to the carrier owning the backbone network and (2) an access charge of Php1.00 per minute to the terminating carrier. In addition, effective January 2002, access charges being paid by PLDT to cellular operators were reduced to Php4.50 per minute from Php6.50 per minute it paid for the period from July to December 2001. Prior to July 2001, PLDT was paying access charges ranging from a low of Php7.69 to a high of Php10.94 per minute for calls terminating to cellular subscribers, depending on whether the calls were local or long distance. PLDT still maintains revenue-sharing arrangements with a few other local exchange carriers, whereby charges are generally apportioned 30% for the originating entity, 40% for the backbone owner and the remaining 30% for the terminating entity.

Data and Other Network Services

Recognizing the growth potential of data and other network services, including internet-based services, and in light of their importance to our business strategy, we have been putting considerable emphasis on this service segment. In 2002, this segment registered the highest percentage growth in revenues among our fixed line services and it continued to grow in 2003.

The upgrading of our network in recent years through the completion of our domestic fiber optic backbone has enabled us to offer a growing range of value-added and broadband services. With this and other technological upgrades, our infrastructure is being developed from a traditional voice facility to a new packet-switched and internet-based network that allows faster transmission of voice, video and data. Data services we currently provide include:

- traditional bandwidth service   high-speed point-to-point domestic and international digital leased line services;

- broadband/packet-based/internet protocol-based services   frame relay, ATM, internet protocol virtual private network, or IP-VPN, DSL, internet gateway and wholesale digital signal level 3, or DS3; and

- other packet-based switching services   Datapac and integrated services digital network, or ISDN.

The foregoing services are used for the following:

- domestic and international communications;

- broadband data transmission services that transmit data over a range of frequencies and/or bandwidth into several narrower bands;

- internet exchange services that provide ISPs with a primary connection to the global internet to exchange local traffic generated within the Philippines;

- private networking services that use the public internet as a backbone for private interconnection between different locations;

- switch-based services, provided through a fixed bandwidth transmission facility, that allow establishment of a dedicated connection for the duration of the call; and

- international packet-based services, provided through bilateral arrangements and global alliances that integrate voice, video and data.

In 2003 and 2002, we continued to broaden our service offerings with the launch of new services and expansion or enhancement of some of the existing ones.

In May 2002, PLDT launched a pay-per-use dial-up internet service under the brand name *PLDT Vibe*, which is available on a postpaid or prepaid basis to PLDT s fixed line subscribers. Charges for this service are Php0.25 per minute for off-peak hours, which are from 10:01 p.m. to 6:00 a.m., and Php0.50 per minute for peak hours, which are from 6:01 a.m. to 10:00 p.m. With the launch of *PLDT Vibe*, PLDT now offers two residential internet service packages targeting separate markets: *PLDT Vibe* for light to medium internet users and *DSL* broadband for heavy internet users. As of December 31, 2003, the number of PLDT s fixed line subscribers that signed up for *PLDT Vibe* was 206,979, of which 129,447 were postpaid and 77,532 were prepaid subscribers, compared to 76,014 as of December 31, 2002, of which 60,878 were postpaid and 15,136 were prepaid subscribers, while the number of *DSL* subscribers reached 23,884 and 10,896 as of December 31, 2003 and 2002, respectively.

In March 2003, PLDT launched a number of data services, namely: *Continuum, iView* and *Encompass*, all under the *Brains* umbrella. *Brains Continuum* provides customers the ability to recover from service interruptions and offers network diversity, facility and hosting services in partnership with ePLDT. *Brains iView* enables customers to monitor the performance of their network, track bandwidth utilization patterns and identify the source of network problems. *Brains Encompass* provides a broad range of services for the customers managed networking needs, be it a wide area network or local area network.

In April 2003, PLDT introduced *Resort Solutions,* a network service that provides communication links between the head office and the remote offices of vacation resorts. It enables resort offices to access the information vital to the business and to do transactions such as real-time updating of room bookings, real-time checking of room inventory or even real-time audit of resort profitability via IP-VPN or internet access.

In May 2003, *Shops.work* was fully launched*,* a network service that allows the electronic linking of retail stores providing, among other features, sales and inventory reports, up-to-date and real-time monitoring of sales and inventory, and on-line access to head offices.

In June 2003, *Embed* was introduced to the market through a soft launch. The service is a wholesale banking solution that enables a bank partner to build a community among its clients in a business to business or business to consumer arrangement through the use of IP-VPN network solution.

In September 2003, *High Bandwidth Optical Service*, or *HBOS* was launched, a dedicated high-speed point-to-point optical access solution that enables data mirroring, storage area network, or SAN, and local area network, or LAN, interconnectivity within Metro Manila. *HBOS* offers an option for a virtually ready alternative data center.

Information and Communications Technology

We conduct our information and communications technology businesses through our wholly-owned subsidiary ePLDT, which was incorporated in August 2000 and started commercial operations in February 2001. ePLDT is a broad-based integrated information and communications technology company, focusing on infrastructure and solutions for internet applications, internet protocol-based solutions and multimedia content delivery. ePLDT's principal businesses are the operation of: (a) an internet data center under the brand name *Vitro* ; (b) call centers through Vocativ and Parlance, which commenced commercial operations in April 2002 and June 2002, respectively, and (c) an ISP through Infocom.

Infrastructures and Services

Data Center

ePLDT operates *VitroTM*, one of the Philippines' first internet data centers. The Philippine Board of Investments granted *Vitro* pioneer status, which entitles it to tax and other governmental incentives. *Vitro* is a CISCO-certified co-location service provider. *Vitro* provides co-location, web and server hosting, hardware and software maintenance services, website development and maintenance services, webcasting and webhosting, shared applications, data disaster recovery and business continuity services, intrusion detection and internet protocol security services, as well as firewall and managed firewall services.

Call Centers

ePLDT is focusing on developing its call center services business, which capitalizes on the availability of English-speaking labor in the Philippines. The call center service business is being undertaken through the following wholly-owned subsidiaries of ePLDT:

- Vocativ which owns and operates a 722-seat call center facility with 883 customer service representatives, or CSRs, exclusively for clients of a global provider of customer relationship management services. Vocativ commenced commercial operations in April 2002; and

- Parlance which owns and operates a 522-seat call center facility with 619 CSRs, exclusively for one of the largest direct-to-home satellite service providers in the United States for customer support and billing requirements. Parlance commenced commercial operations in June 2002.

ePLDT sold its entire 51% interest in Contact World, Inc., another call center facility, on June 30, 2003 and assigned its receivables from the same to Service Zone Inc., a U.S.-based call center operator, for a total consideration of US$700,000.

Internet Service

ePLDT owns 99.6% interest in Infocom, one of the country's leading ISPs. Infocom offers consumer prepaid internet access under the name *Warpspeed* and postpaid internet access; dedicated dial-up and multi-user business dial-up access; broadband internet access through corporate leased lines and *NOW* cable internet; and consulting, web development and hosting.

Other Investments

ePLDT also has investments in several other internet-related businesses, including:

- 100% interest in mySecureSign, Inc., which issues VeriSign digital certificates in the Philippines for e-commerce transactions;

- 100%-owned subsidiary, iPlus Intelligent Network, Inc., which provides IT helpdesk/contact center solutions;

- 20.5% interest in BayanTrade Dotcom, Inc., a business-to-business exchange established together with six of the Philippines leading conglomerates;

- debt securities convertible into a 40% interest in Netopia, a leading branded chain of internet cafes in the Philippines; and

- 22.5% interest in convertible securities of Stradcom International Holdings, the parent company of Stradcom Corporation, which has an existing concession agreement with the Philippine government for the modernization of the Philippine Land Transportation Office, including the computerization of driver s license issuance, vehicle registration and traffic adjudication systems.

In addition, we held convertible notes issued by Unilink Communications Corporation, or Unilink, which owns 100% of the shares of the Philippine Home Cable Holdings, Inc., or Home Cable, the Philippines second largest cable television operator by subscriber numbers. PLDT s total investments in convertible notes of Unilink amounted to Php2,052 million as of December 31, 2002. Mediaquest Holdings, Inc., a company wholly-owned by the PLDT Beneficial Trust Fund, or BTF, owns all of the shares of Unilink. In June 2003, PLDT assigned and ceded unto the PLDT BTF all of its rights, interest and participation in respect of its investment in convertible notes of Unilink with a fair value of zero and effectively for zero consideration under U.S. GAAP.

These notes are convertible into shares of common stock of Unilink or exchangeable into common stock of Home Cable at the option of the holder, if and when the law limiting the ownership of cable television systems to Philippine citizens or corporations, which are 100% owned by Philippine citizens, is eventually changed. Unilink is a Philippine corporation owning all the outstanding common shares of Home Cable, which is also a Philippine corporation licensed to own, maintain and operate a cable television system in the Philippines.

All of Unilink s shares in Home Cable have been pledged to a group of lenders as security for a loan of Home Cable. On December 6, 2001, Home Cable defaulted on the principal and interest payments in respect of certain of its loan obligations. On April 10, 2002, the loan agent, at the request of the lenders, delivered a notice to Home Cable declaring an event of default and accelerating the loan repayment. Consequently, the lenders are entitled to foreclose on or sell the collateral granted as security for the loan, including Unilink s share in Home Cable. In the event that Home Cable s lenders were to foreclose on Unilink s Home Cable shares, the lenders would be entitled to the proceeds from the sale thereof or, if such shares were not sold, to the shares, and Unilink would be subrogated to the lenders claims against Home Cable. On October 17, 2003, Home Cable signed a Memorandum of Agreement with its key creditors providing the framework and indicative terms and conditions for the restructuring of its debt obligations.

On July 18, 2001, we entered into a master consolidation agreement pursuant to which a newly incorporated company, Beyond Cable, Inc., would hold all interests in Sky Cable and Home Cable. Completion of the trasaction is subject to certain conditions, including obtaining consents of lenders of Sky Cable and Home Cable. Upon completion of the transaction, the Benpress Group, which currently holds the interests in Sky Cable, would hold a 66.5% interest in Beyond Cable and Mediaquest would hold remainder.

Wireless Network Infrastructure

Cellular

Through Smart, we operate a digital GSM network. To meet the growing demand for cellular services, Smart has implemented an extensive deployment program for its GSM network covering substantially all of Metro Manila and most of the other population centers in the Philippines. In 2003, Smart added 1,127 base stations to its nationwide cellular network, bringing to 3,904 Smart's total GSM base stations in operation. Smart has 32 mobile switching centers and 37 text messaging service centers, which have raised significantly Smart's GSM network capacity to cover approximately 14.3 million subscribers as of December 31, 2003. As of December 31, 2003, Piltel had six active cell sites.

Smart has an operating spectrum of 7.5 MHz in the 900 MHz band supporting both its GSM and previously its ETACS network and 17.5 MHz in the1800 MHz band for GSM. Its dual-band GSM network allows it to efficiently deploy high capacity 1800 MHz base transceiver stations in dense urban areas while its 900 MHz base transceiver stations can be much more economically deployed in potentially high growth, but less densely populated provincial areas. Spectrum constraints will not affect the Smart s expansion plans for GSM in the foreseeable future. Piltel, on the other hand, has an operating spectrum of 11.5MHz out of the 12.5MHz allocated in the 800 MHz band.

Due to its access to PLDT s network assets, Smart has been able to achieve significant capital expenditure savings, which are understood to be significantly less, on a per net addition basis, than its current competitors. This translates into an improved ability to price competitively and target the mass market subscriber base in the Philippines, while retaining profitability. Based on existing equipment purchase contracts, Smart expects incremental capital expenditure per net additional subscriber to amount to less than US$50.

The coming years will see continued increases in coverage (particularly indoor), as well as new types of BTS for outdoor, street level and commercial office coverage. Smart has recently started to introduce the Nokia *ConnectSite* GSM system for wider coverage and increased efficiencies in underserved areas of the Philippines. The new base station equipment called *ConnectSite* can be up to 25% more efficient than traditional outdoor cell sites. Smart is one of the very first operators in the world to adopt this system.

Smart and Piltel have been co-locating their cell sites where their base stations are installed. As of December 31, 2003, 20 of Smart's mobile switching centers and 75 of Smart's cell sites are housed in PLDT s fixed line complexes while 233 of Smart s cell sites are co-located with Piltel. These operational synergies have allowed Smart to reduce switch installation time from three months to five weeks.

Satellite and VSAT

Mabuhay Satellite controls and operates the Agila II satellite, which has 30 C-band transponders and 24 Ku-band transponders covering the Asia-Pacific region, the Indian subcontinent and Hawaii. Of the 54 transponders, six have restricted usage due to satellite interference. Through Agila II, Mabuhay Satellite offers internet service, video and data broadcasting, and bandwidth-on-demand, facilitating communication links between telecommunications, broadcast and other public utility companies operating in the Asia-Pacific region. In December 2000, Agila II joined the U.S. FCC's "Permitted Space Station" list, which permits U.S. owned and operated earth stations in Hawaii to access Agila II for transpacific telecommunications, data, video and internet-over-satellite traffic and vice versa.

Telesat operates a national communications satellite network using VSAT technology to provide voice, facsimile, video and data transmission services to areas in the country that are still underserved or unserved by local telephone operators. Telesat leases transponder capacity from Agila II to provide VSAT services such as multipoint-to-multipoint and point-to-multipoint data transmission services, private point-to-point service, and connectivity for the cell sites of our cellular network in outlying locations.

ACeS Philippines manages, controls and operates its own satellite gateway and other ground infrastructure, including a 13-meter feeder-link C-band earth station, beam congruency antenna and equipment that serve as the primary interface between the ACeS system and other telecommunications networks. It uses the Garuda I satellite to provide digital voice services to ACeS Philippines mobile and fixed terminal users within the Asian service area.

Fixed Line Network Infrastructure

Domestic

Our domestic telephone network includes installed telephones and other equipment on customers premises, local access lines connecting customers to exchanges, referred to as outside plant, inter-office lines connecting exchanges, and long distance transmission equipment.

The following table gives some basic measures of the development of our domestic telephone network as of December 31, 2003, 2002 and 2001:

	As of December 31,		
	2003	**2002**	**2001**
Number of central office exchanges	183	183	187
PLDT fixed lines in service	2,115,671	2,092,539	2,075,109
PLDT employees per 10,000 local exchanges in service	48	58	62

We have our own 5,400 kilometer domestic fiber optic backbone, the country's first telecommunications network using fiber optics in delivering voice, video, data, and other broadband and multimedia services nationwide. Constructed at a total cost of US$188 million, our fiber optic network employs synchronous digital hierarchy technology to improve network performance and reduce operating costs. Our network is composed of in-land and submarine cable installations and is configured in six self-healing rings and an extension link, allowing route delivery even in the event of link failures. It has an initial transmission speed of 2.5 gigabits per second and is connected directly to five existing international submarine cable systems. We use *CS PLDT*, a cable ship which we lease from NTT World Engineering Marine Corporation pursuant to a five year Chartered Arrangement Maintenance Contract to maintain the 2,400 kilometers of submarine cable comprising the submerged portion of our domestic fiber optic network, or DFON.

In 2001, we activated a second fiber pair on our existing fiber cable and installed dense wavelength division multiplexing technology in certain portions of the network. The new system serves the areas of Luzon, Visayas and Mindanao and also serves the international node connecting the Philippines to the Asia-Pacific Cable Network 2. The second pair provides an extra 10 gigabits per second of capacity, or the equivalent of 120,000 voice circuits. Nortel Networks supplied us with a suite of optical internet solutions, including a 10-gigabit per second dense wavelength division multiplexing solution based on Nortel Networks OPTera Long Haul 1600 Optical Line System.

In 2002, we increased our transmission and data network capacities and sold to Smart certain assets comprising a portion of our digital fiber optic cable loops from Luzon to Mindanao and certain related equipment.

International

We provide international network services using our three international gateway switching exchanges. As of December 31, 2003, our international long distance facilities allow direct correspondence with 50 countries/territories (representing 76 correspondents) and can reach 229 foreign destinations worldwide. We also own interests in submarine and satellite systems, through which we route most of our international traffic.

The table below shows the submarine cable systems in which we have interests and the countries or territories they link:

Cable System	**Countries Being Linked**
B-M-P	Brunei, Malaysia and Philippines
G-P	Guam and the Philippines
Asia-Pacific Cable Network	Korea, Japan, Hong Kong, Taiwan, Australia, Philippines, Singapore, Malaysia, Indonesia and Thailand
Asia-Pacific Cable Network 2	Philippines, Hong Kong, Japan, Korea, Malaysia, Singapore, Mainland China and Taiwan
Transpacific Cable No. 4	Japan, Canada and the U.S. Mainland
Transpacific Cable No. 5	Guam, Japan, Hawaii and the U.S. Mainland
KN-KK	Kuantan and Kota Kinabalu in Malaysia
SEA-ME-WE-3	Japan, Korea, China, Taiwan, Hong Kong, Macau, Philippines, Vietnam, Cambodia, Brunei, Malaysia, Singapore, Indonesia, Australia, Thailand, Myanmar, Sri Lanka, India, Pakistan, United Arab Emirates, Oman, Djibouti, Saudi Arabia, Egypt, Cyprus, Turkey, Greece, Italy, Morocco, Portugal, France, UK, Belgium and Germany
SEA-ME-WE-2	13 countries in South East Asia, the Middle East and Western Europe, including Singapore, Indonesia, India, Saudi Arabia, Egypt, Italy, Turkey and France
Asia Pacific	Hong Kong, Japan, Singapore, Malaysia and Taiwan
PacRim West	Guam and Australia
PacRim East	Hawaii and New Zealand
M-T	Malaysia and Thailand
Hawaii-5	Hawaii and the U.S. Mainland
C-J	Mainland China and Japan
North Pacific	Japan, Alaska and the U.S. Mainland
H-J-K	Hong Kong, Japan and Korea
Americas Cable 1	U.S. Mainland, U.S. Virgin Islands, Brazil, Trinidad and Venezuela
China-U.S. Cable	Japan, China, Taiwan, Korea, Guam and U.S. Mainland
Columbus II Cable	U.S. Mainland, Italy, U.S. Virgin Islands, Mexico, Portugal and Spain
FLAG Cable	Japan, Korea, Mainland China, Hong Kong, Malaysia, Thailand, India, United Arab Emirates, Saudi Arabia, Egypt, Italy, Spain and UK
MAT 2 Cable	Italy and Spain
RIOJA Cable	Spain, UK, Belgium and Netherlands
RJK Cable	Russia, Japan and Korea

Southern Cross Cable	U.S. Mainland, Hawaii, Fiji, Australia and New Zealand
TASMAN2 Cable	Australia and New Zealand
TAT 10 Cable	Germany and the Netherlands
TAT 12/13 Cable	U.S. Mainland, UK and France
TVH Cable	Thailand, Vietnam and Hong Kong
EAC Cable	Japan, Hong Kong, Korea, Taiwan, Singapore and the Philippines
PC-1 and Japan-U.S. Cable	Japan and the U.S.

Interconnection Agreements

Since the issuance of Executive Order No. 59 in 1993, which requires non-discriminatory interconnection of Philippine carriers' networks, we have entered into bilateral interconnection arrangements with other Philippine fixed line and cellular carriers.

Prior to July 1, 2001, PLDT retained an origination charge of Php2.00 per minute on every call terminating to the network of Smart or Globe. From July 1, 2001 to December 31, 2001, Smart and Globe charged PLDT Php6.50 per minute pursuant to an amended interconnection agreement. The new arrangement also applied to national long distance calls originating from PLDT and terminating on the cellular network of either Smart or Globe removing any distinction between access charges for local calls and national long distance calls. For local calls originating from PLDT and terminating to the cellular networks of Smart and Globe, Smart and Globe charged PLDT a rate of Php4.50 per minute effective January 1, 2002. Effective January 1, 2004, calls terminating to cellular subscribers originating from fixed line subscribers will be charged a termination rate of Php4.00 per minute, a decrease from the previous Php4.50 per minute.

Effective January 1, 2003, local access for cellular operators, including Smart and Piltel, which terminate calls on PLDT s fixed line network increased from Php2.00 per minute to Php2.50 per minute, which further increased to Php3.00 per minute effective January 1, 2004.

Under a separate agreement between PLDT and PAPTELCO, PLDT is the transit facility provider between Smart, Globe and PAPTELCO. Transit traffic is an accommodation by PLDT to Smart, Globe and PAPTELCO members where PAPTELCO members have no direct interconnection with either Smart or Globe.

Effective February 1, 2003, international calls terminating on PLDT s fixed line network were charged a termination rate of an average of approximately US$0.12 per minute from the previous rate of an average of approximately US$0.08 per minute. Also, international calls terminating on Smart s and Piltel s cellular network were charged a termination rate of an average of approximately US$0.16 per minute, an increase from the previous termination rate of an average of approximately US$0.12 per minute.

Effective January 1, 2002, Smart charged a termination rate of Php4.00 per minute for calls originating from/terminating on another cellular operator s network. For SMS originating from Smart and Piltel and terminating on other operators cellular network and for SMS originating from other operators and terminating on Smart s and Piltel s cellular network, the charge is Php0.35 per message.

Licenses and Regulation

PLDT, Smart and Piltel provide telecommunications services pursuant to legislative franchises, which expire, in the case of PLDT, November 28, 2028, in the case of Smart, March 27, 2017 and, in the case of Piltel, May 14, 2019. A franchise holder is required to obtain operating authority from the NTC to provide specific telecommunications services. These approvals may take the form of a CPCN or, while an application for a CPCN is pending, a provisional authority to operate.

PLDT operates its business pursuant to a number of provisional authorities and CPCNs, the terms of which expire at various times between now and 2028. PLDT's CPCNs to provide services to most of the Metropolitan Manila area, Davao and other Philippine cities expired in 2003. Although some of PLDT's CPCNs and provisional authorities have already expired, PLDT filed timely applications for extension of these CPCNs and provisional authorities prior to their respective expiration dates and is therefore entitled to continue to conduct its business under its existing CPCNs and provisional authorities pending the NTC s decision on these extensions. PLDT expects that the NTC will grant these extensions; however, there is no assurance that this will occur. The period of validity of some of PLDT s CPCNs expired on November 28, 2003, coterminous with the term of its previous franchise under R.A. 6146, which has been extended further by the NTC to November 28, 2028, coterminous with PLDT s current franchise under R.A. 7082. Motions to extend the period of validity of the other CPCNs to November 28, 2028 are now pending with the NTC. See Item 3. Key Information Risks Factors Risks Relating to Us Our business is significantly affected by governmental laws and regulations, including regulations in respect of our franchises and rates." Piltel holds a CPCN to provide a nationwide cellular telephone service which expires in August 2019.

Smart operates its cellular, international long distance and national long distance services pursuant to CPCNs, the terms of which will expire upon the expiration of its franchise. On August 26, 2002, Smart was granted a CPCN to install, operate and maintain nationwide global mobile personal communications via satellite which shall also expire upon expiration of its franchise. Smart s provisional authority to establish, install, maintain, lease and operate an international private leased circuit expired on May 6, 2003. Prior to its expiration, Smart filed for an extension of this provisional authority. On July 22, 2002, Smart was granted separate CPCNs to operate a cellular mobile telephone system and an international gateway facility.

Piltel is authorized to provide virtually every type of telecommunications service, including the transmission of voice, data facsimile, audio and video and information services, in and between provinces, cities and municipalities throughout the Philippines. The franchise, which was last amended on May 14, 1992, expires on May 14, 2019 and may be extended by a legislative act of the Philippine Congress.

The following table sets forth the spectrum system, licensed frequency and bandwidth allocated to Smart and Piltel:

Carrier	**Spectrum System**	**Frequency Assignment**	**Bandwidth**
Smart	ETACS/GSM 900	897.5-905/942.5-950 Mhz	7.5 Mhz
	GSM 1800	1725-1730/1820-1825 Mhz	5.0 Mhz
		1730-1732.5/1825-1827.5 Mhz	2.5 Mhz
		1735-1740/1830-1835 Mhz	5.0 Mhz
		1745-1750/1840-1845 Mhz	5.0 Mhz
Piltel	AMPS/CDMA	824-835/869-880 Mhz	11.0 Mhz
		845-846.5/890-891.5 Mhz	1.5 Mhz

Operators of international gateway facilities and cellular telephone operators, pursuant to E. O. 109, are required to install a minimum number of local exchange lines. Of these new lines, operators are required to install one rural exchange line for every ten urban exchange lines installed. Smart and Piltel were required to install 700,000 and 400,000 lines, respectively, and each has received a certificate of compliance from the NTC.

We are required to pay various permit, regulation and supervision fees to the NTC and are currently engaged in disputes with the NTC over some of the assessed fees. For more information on these disputes, see Item 8. Financial Information Legal Proceedings NTC Fees.

On May 27, 1998, Smart filed an Urgent Ex Parte Motion and Manifestation regarding the permit fee in the amount of approximately Php113 million assessed by the NTC for CPCN 93-482, pertaining to Smart s Integrated Local Exchange Telephone Service, Domestic Toll Service and Private Line Service. Smart contended that the fee should have been calculated on the basis of the actual local exchange carrier project cost, and that therefore the fee should be Php70 million. Although the NTC has not yet resolved this issue, Smart has already paid Php50 million in respect of this assessment as of the date of filing of this annual report.

In a letter dated January 17, 2002, the NTC requested that Smart pay the following fees in respect of its CPCNs and provisional authorities:

Case No.	**Fee**
92-303	Php3,750,000
93-482	62,510,950
94-220	878,830
96-248	6,815,500

Total	Php73,955,280

Piltel has also been assessed by the NTC for deficiency supervision and regulation fees. Based on the latest computation of deficiency supervision and regulation fees received from the NTC, which is dated as of September 30, 2002, the total amount assessed on Piltel stands at Php640 million, including penalty fees amounting to Php275 million. Piltel has protested the assessments in good faith. Piltel continues to make payments for which it believes are properly due to the NTC. On September 30, 2002, Piltel made a payment to the NTC under protest in the amount of Php9.1 million.

In order to diversify the ownership base of public utilities, the Public Telecommunications Policy Act (R.A. 7925) requires a telecommunications entity with regulated types of services, such as Smart and Piltel, to make a public offering through the stock exchanges representing at least 30% of its aggregate common shares by the later of the following:

- the fifth anniversary of the date the law became effective; and

- the fifth anniversary of the date of the entity s commencement of commercial operations.

PLDT and Piltel have complied with this requirement. Smart believes that it has ten years from the commencement of its operations, or until August 2004, to conduct a public offering because the Philippine government has granted franchises to other telecommunications companies requiring a public offering within ten years from the later of their commencement of operations or the date on which the franchise was granted. Because R.A. 7925 provides that any advantage granted under existing franchises automatically becomes part of previously granted telecommunications franchises, Smart believes that it is also entitled to this ten-year period. PLDT currently contemplates to cause Smart to conduct a public offering based on market conditions and in accordance with applicable rules and regulations of the PSE. The Philippine Congress may revoke the franchise of Smart if it fails to comply with the requirement under R.A. 7925 on the public offering of its shares by August 2004. A *quo warranto* case may also be filed against Smart by the Office of the Solicitor General of the Philippines on the ground of violation of R.A. 7925 if Smart will fail to conduct public offering of its shares by August 2004.

In addition, the Philippine Congress is considering five bills, each of which, if passed by Congress and enacted into law, would impose a 7% or 10% tax on the gross receipts of cellular operators. The proposed taxes would apply to both cellular calls and cellular data revenues and prohibit cellular operators from imposing additional charges or fees to compensate for the imposition of the proposed taxes.

Competition

The enactment of the Public Telecommunications Policy Act (R.A. 7925) of the Philippines in March 1995 consolidated the government's various policy issuances governing the telecommunications industry and reaffirmed, among other things, the policy of liberalizing the industry and opening up the telecommunications market to new entrants. Including us, there are nine major local exchange carriers, 11 international gateway facility providers, and six cellular service providers in the country, including one which has not yet commenced operations. Many new entrants into the Philippine telecommunications market have entered into strategic alliances with foreign telecommunications companies, which provide them access to technological and funding support as well as service innovations and marketing strategies. Consequently, we are facing increasing competition in major segments of the telecommunications industry, particularly cellular, fixed line and data and other network services segments.

Cellular Service

Competition in the cellular business has intensified with the introduction by competitors of affordably priced handsets offering a range of new functions and features, new and improved plans for postpaid subscribers, reduced rates per minute and aggressive marketing and promotional strategies. Our principal competitor in the cellular business is Globe, which acquired Islacom in 2001. The principal bases of competition are price, including handset cost, quality of service, network reliability, geographic coverage and attractiveness of packaged services.

Cellular operators are also competing actively against each other in launching innovative products and value-added services. The growing range of cellular products and services now include text messaging, multimedia messaging, voice mail, text mail, international roaming, information-on-demand, mobile banking, e-commerce, mobile data and cellular internet access.

Consistent with industry practice and Smart s churn management efforts, Smart "locks" the handsets it sells to its subscribers, rendering them incompatible with SIM cards issued by competitors. However, subscribers may have their handsets unlocked by unauthorized parties, for a nominal fee, and purchase new SIM cards from competing operators. Unlocking does not involve significant cost. In addition, switching to another cellular operator would result in a change of the subscriber s cellular telephone number.

There are six operating cellular service providers, namely Smart, Piltel, Globe, Islacom, Digitel and Express Telecom. Globe acquired Islacom (now known as *Innove*) to form into one operating group while Smart and Piltel, both being part of the PLDT Group, form another operating group. There are therefore effectively only two key competitors in the Philipppine cellular market. Digitel commenced its cellular service, *Sun Cellular*, on March 29, 2003 and is estimated to have less than 1% of the market. Extelcom operates on an analog platform and is estimated to have less than 50,000 subscribers.

Local Exchange Service

The concerted nationwide local exchange line build-out by various players, as mandated by the Philippine government, significantly increased the number of fixed lines in service in the country and resulted in wider access to basic telephone service. The growth of the fixed line market has considerably weakened due to the surge in demand for cellular services and the general sluggishness of the national economy. Nevertheless, we have sustained our leading position in the fixed line market on account of PLDT's extensive network in key cities nationwide. In most areas, we face one or two competitors. Our principal competitors in the local exchange market are Digitel, BayanTel and Globe.

Over the past couple of years, however, competition among local exchange operators has reduced as certain operators have faced financial difficulties or have shifted strategic focus away from the fixed line business to cellular services. On the other hand, we are facing increasing competition from cellular operators mainly due to substitution of cellular services for fixed line services.

International Long Distance Service

Including us, there are 11 international gateway facility operators in the country. While we have so far been able to maintain a leadership position in this highly competitive segment of the industry, in recent years, our market share has reduced largely as a result of (1) competition from other international gateway facility operators and international simple resale operators, (2) an increase in inbound and outbound international long distance calls terminating to and originating from the growing number of cellular subscribers, and (3) the popularity of alternative and cheaper means of long distance communications, such as text messaging, e-mailing and internet telephony, further heightening the competition.

With respect to inbound calls into the Philippines, we adopted the U.S. FCC benchmark accounting rate of US$0.38 per minute for inbound international calls which represented a settlement rate of US$0.19 per minute, one year ahead of the target date of January 1, 2001. This provided us with increased flexibility to terminate more U.S. traffic into the Philippines, minimize unauthorized traffic termination through international simple resale operations and recover traffic lost due to bypass routings. We have also established presence in key cities overseas to identify traffic at its source, maximize the use of our international facilities and develop alternative sources of revenue. Effective February 1, 2003, after lengthy negotiations with approximately 100 telecommunications operators around the world, we increased the termination rate with carriers accounting for a substantial portion of our international inbound traffic terminating on our fixed line network to an average of approximately US$0.12 per minute. Prior to the increase in termination rates, a substantial portion of PLDT s international inbound traffic terminating on its fixed line network was charged an average termination rate of approximately US$0.08 per minute. See Item 8. Financial Information Legal Proceedings U.S. Federal Communications Commission, or FCC, Ruling versus Philippine Telecommunications Companies , Item 5. Operating and Financial Review and Prospects Results of Operations 2003 Compared to 2002 Consolidated Operating Revenue Fixed Line International Long Distance , Item 3. Key Information Risks Factors Risks Relating to Us Our results of operations have been, and may continue to be, adversely affected by competition in international long distance service and *Note 28 Other Matters* to the accompanying consolidated financial statements in Item 18 for further discussion.

With respect to outbound calls from the Philippines, we compete for market share through our local exchange and cellular businesses, which are the origination points of outbound international calls. We have also introduced a number of marketing initiatives to stimulate growth of outbound call volumes, including tariff reductions and volume discounts for large corporate subscribers.

National Long Distance Service

Since 2000, our national long distance service business has been negatively impacted by the growing number of cellular subscribers in the Philippines and the widespread availability and growing popularity of alternative economical non-voice methods of communication, particularly text messaging and e-mailing.

While national long distance call volumes have been declining, we have remained a leading provider of national long distance service in the Philippines due to our significant subscriber base and ownership of the Philippines most extensive DFON. In order to mitigate the decline of our national long distance revenues, we have renegotiated the interconnection agreements with the cellular operators to provide the fixed line business a more equitable access charge arrangement for calls between fixed line and cellular subscribers.

Data and Other Network Services

Another rapidly growing segment of the industry is the market for data and other network services. The growth is spurred by the significant growth in consumer/retail narrowband and broadband internet access, enterprise resource planning applications, call centers, business process outsourcing, on-line gaming and other e-services that drive the need for broadband and internet-protocol based solutions both here and abroad. Our principal competitors in this area are Globe/Innove, BayanTel, Eastern Telecommunications and Digitel. The principal bases of competition in the data services market are price, customer service and quality of service.

Environmental Matters

We have not been subject to any material fines or legal or regulatory action involving non-compliance with environmental regulations of the Philippines. We are not aware that we are not in compliance in any material respect with relevant environmental protection regulations.

Intellectual Property Rights

We do not own any material intellectual property rights apart from our brand names and logos. We are not dependent on patents, licenses or other intellectual property which are material to our business or results of operations, other than licenses to use the software that accompany most of our equipment purchases.

Properties

PLDT owns four office buildings located in Makati City and owns and operates 183 exchanges nationwide, of which 61 are located in the Metropolitan Manila area. The remaining 122 exchanges are located in small cities and municipalities outside Metropolitan Manila area. We also own radio transmitting and receiving equipment used for international and domestic communications.

Smart s digital GSM network includes 32 switching centers with a capacity of over 14 million subscribers and 3,904 base stations covering 1,039 cities and municipalities nationwide. Piltel also has six active cell sites at the end of 2003.

As of December 31, 2003, our principal properties, excluding property under construction, consisted of the following, based on book value:

- 53% consisted of cable and cellular facilities, including our DFON, subscriber cable facilities, inter-office trunking and toll cable facilities and cellular facilities;

- 30% consisted of central office equipment, including three international gateway facilities, six pure national toll exchanges and 15 combined local and toll exchanges, and communications satellite;

- 8% consisted of land and improvements and buildings, which we acquired to house our telecommunications equipment;

- 1% consisted of information origination and termination equipment, including, pay telephones and radio equipment installed for customers use, as well as cables and wires installed within customers' premises; and

- 8% consisted of other work equipment.

For more information on these properties, see *Note 7 Property, Plant and Equipment* to the accompanying consolidated financial statements in Item 18. These properties are located in areas being served by our exchanges. In our opinion, these properties are in good condition, except for ordinary wear and tear, and are adequately insured.

The majority of our connecting lines are above or under public streets and properties owned by others.

PLDT's and Smart s properties are free from any mortgage, charge, pledge, lien or encumbrance. However, substantial properties of Piltel and Mabuhay Satellite are subject to liens.

PLDT Group has various long-term lease contracts for periods ranging from two to ten years covering certain offices, warehouses, telecommunications equipment locations and various office equipment.

Item 5. Operating and Financial Review and Prospects

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our audited consolidated financial statements (and the related notes) as of December 31, 2003 and 2002 and for the years ended December 31, 2003, 2002 and 2001 included elsewhere in this report. This discussion contains forward-looking statements that reflect our current views with respect to future events and our future financial performance. These statements involve risks and uncertainties, and our actual results may differ materially from those anticipated in these forward-looking statements as a result of particular factors such as those set forth under "Forward-Looking Statements" and Item 3. Key Information Risk Factors" and elsewhere in this report. Our audited consolidated financial statements, and the financial information discussed below, have been prepared in accordance with U.S. GAAP. For convenience, certain peso financial information in the following discussions has been translated to U.S. dollars at the exchange rate at December 31, 2003 of Php55.586 to US$1.00, as quoted through the Philippine Dealing System.

Overview

We are the largest and most diversified telecommunications company in the Philippines. We have organized our business into three main segments:

- *Wireless* wireless telecommunications services provided by PLDT s subsidiaries, Smart and Piltel, our cellular service providers, and Mabuhay Satellite, ACeS Philippines, and Telesat, our satellite and VSAT operators;

- *Fixed Line* fixed line telecommunications services primarily provided through PLDT. We also provide fixed line services through PLDT s subsidiaries Clark Telecom, Subic Telecom, SNMI and Maratel, which together account for approximately 1% of our consolidated fixed lines in service, BCC (in 2003) and PLDT Global; and

- *Information and Communications Technology* information and communications infrastructure and services for internet applications, internet protocol-based solutions and multimedia content delivery provided by PLDT s subsidiary, ePLDT, internet access services provided by ePLDT s subsidiary Infocom, and e-commerce, call centers and IT-related services provided by ePLDT s other subsidiaries and associates.

Key performance indicators and drivers that our management uses for the management of our business include, among others, the general economic conditions in the Philippines, our subscriber base, traffic volumes, and interconnection arrangements.

Wireless

Our wireless business provides cellular and satellite, VSAT and other services, contributing about 99% and 1% of our wireless revenues, respectively, as of December 31, 2003. Rapid growth in the cellular market has resulted in a change in our revenue composition and sources of our revenue growth. For 2003, cellular service was our major revenue source surpassing fixed line revenues by four percentage points. As of December 31, 2003, Smart and Piltel, which offers GSM service using Smart s GSM network, had the largest and third largest cellular subscriber bases, respectively, in the Philippines. In addition, Smart s and Piltel s subscribers increased by 51% in 2003, resulting in our aggregate system-wide cellular subscribers outnumbering our fixed line in service by more than 6 to 1 at the end of 2003. Cellular data services, which include all text messaging and text-related services ranging from ordinary text to value-added services, contributed significantly to our revenue increase. Wireless business revenues accounted for 58%, 50% and 42% of our consolidated revenues for 2003, 2002 and 2001, respectively.

Fixed Line

Our fixed line business provides local exchange service, international and national long distance services, data and other network services and miscellaneous services. Until 2003, fixed line services have been our major revenue source contributing 49% and 58% of total operating revenues in 2002 and 2001, respectively. Although relatively stable in absolute terms, our fixed line revenues contribution to consolidated operating revenues have declined to 41% in 2003, largely due to the substantial growth in our wireless business. Local exchange revenues have declined slightly owing to shift in subscriber preference from postpaid to prepaid service. National long distance revenues have also been declining largely due a drop in call volumes, and an increase in the proportion of calls subject to revenue sharing with other carriers. Mitigating these declines was the steady growth of our data and other network services over the recent years. Recognizing the growth potential of the data and other network services segment, we have put considerable emphasis on the development of new packet-switched, data-capable and internet-based networks. International long distance revenues have declined until 2002 due to lower inbound call volumes, lower termination rates and increased competition and substitution, but has increased its contribution to the overall fixed line revenues in 2003 on account of an increase in our average termination rates.

Information and Communications Technology

Our information and communications technology business is conducted through our wholly- owned subsidiary, ePLDT, which was incorporated in August 2000 and started commercial operations in February 2001. ePLDT s principal businesses are the operation of an internet data center under the brand name *Vitro*TM; two wholly-owned call centers, Vocativ and Parlance; and Infocom, an ISP. The revenue contribution of our information and communications technology segment accounted for 1% of our total consolidated operating revenues for the years 2003 and 2002, and less than 1% in 2001.

Critical Accounting Policies

Our consolidated financial statements are prepared in accordance with U.S. GAAP, which requires management to make estimates and assumptions that affect amounts reported in our consolidated financial statements and related notes. In preparing these consolidated financial statements, we have made our best estimates and judgments of certain amounts, giving due consideration to materiality.

We believe the following represent our critical accounting policies under U.S. GAAP. The impact and any associated risks relating to these policies in our business operations are discussed elsewhere in this section.

Revenue Recognition

Revenue for services is stated at amounts invoiced to customers and excludes value-added tax. We provide wireless communication services, fixed line communication services, and information and communications technology services. We provide such services to business, residential, payphone and mobile customers. Revenue represents the value of fixed consideration that has been received or is receivable. Revenue is recognized when there is evidence of an arrangement, collectibility is reasonably assured, and the delivery of the product or service has occurred. In certain circumstances, revenue is split into separately identifiable components and recognized when the related components are delivered in order to reflect the substance of the transaction. The value of components is determined using verifiable objective evidence. We do not provide our customers with the right to a refund.

Products and services

Subscriptions. We provide telephone and data communication services under postpaid and prepaid payment arrangements. Revenue includes fees for installation and activation. Installation and activation-related fees and the corresponding costs, not exceeding the activation revenue, are deferred and recognized over the expected average period of the customer relationship of seven years and three years for fixed line and cellular service, respectively. Postpaid service arrangements include subscription fees, typically fixed monthly fees, which are recognized over the subscription period on a pro rata basis.

Air time, traffic and value-added services. Prepaid service revenue collected in advance is deferred and recognized based on the earlier of actual usage or upon expiration of the usage period. Payphone service revenue is recognized when the service is provided. Interconnection revenue for call termination, call transit, and network usage are recognized in the period the traffic occurs. Revenues related to local, long distance, network-to-network, roaming and international call connection services are recognized when the call is placed or the connection is provided, net of amounts payable to other telecommunication carriers for terminating calls in their territories. Revenue related to products and value-added services is recognized upon delivery of the product or service.

Equipment sales. Sales of communication equipment are recognized upon delivery to the customer.

Directory services. Revenue related to published directory services is recognized on a pro rata basis over the period in which the publication expires, which is generally 12 months. Telephone-based directory service revenue is recognized when the service is provided.

Incentives. We record commission expense based on the number of new subscriber connections initiated by certain dealers. All other cash incentives provided to dealers and customers are recorded as a reduction from revenue. Product-based incentives provided to dealers and customers as part of a transaction are accounted for as multiple element arrangements and recognized when earned.

Others. Interest income from cash deposits is recognized on a time proportion basis taking into account the principal amount outstanding and the effective interest rate.

Impairment of Long-Lived Assets

U.S. GAAP requires that an impairment review be performed when certain impairment indicators are present. The impairment review first compares the future undiscounted cash flows expected to be generated from the continued use and ultimate disposition of the assets with the book value of the assets. If these cash flows are not sufficient to recover the book value of the assets, an impairment charge is recognized based on the comparison between the discounted value of these cash flows and the book value of the assets. In addition, our projections for future cash flows are generally less during periods of reduced cash flow. As a result, an impairment charge is more likely to occur during a period when our operating results are already otherwise depressed.

Purchase accounting requires extensive use of accounting estimates and judgments to allocate the purchase price to the fair market values of the assets and liabilities purchased. Our business acquisitions typically result in goodwill, which affected our results of operations for the amount of future period amortization expense. However, we no longer amortize goodwill under U.S. GAAP effective January 1, 2002. Instead, goodwill is subject to a periodic impairment test. Determining the value of goodwill and future undiscounted cash flows expected to be generated from the continued use and ultimate disposition of such assets require us to make estimates and assumptions that can materially affect our consolidated financial statements. Future events could cause us to conclude that goodwill associated with an acquired business is impaired. Any resulting impairment loss could have a material adverse impact on our financial condition and results of operations.

Piltel recognized an asset impairment charge of Php12,938 million in 2001 and Php13,204 million in 2002 relating to its AMPS/CDMA and E.O. 109 assets, respectively. The revenues generated from these services could no longer support the cost of operating the network.

Also, Smart carried out an impairment review of its analog assets in 2001 as a result of declining subscriber numbers, decreasing average revenue per user and the general migration of analog subscribers to Smart s GSM services. This resulted in an asset impairment charge of Php3,783 million in 2001 based on the estimated discounted future cash flows from continued use and eventual disposition of these assets. In 2001, Smart wrote-off the unamortized intangible assets (customer lists) amounting to Php2,077 million relating to analog customers.

As of December 31, 2003, ACeS Philippines has a 20% investment in AIL, a company incorporated under the laws of the island of Bermuda. AIL owns the Garuda I satellite and the related system control equipment in Batam, Indonesia. In December 1998, AIL and its 95% owned subsidiary, PT Asia Cellular Satellite, entered into an Amended and Restated Credit Agreement, or Amended Agreement, to amend the original Credit Agreement entered into by PT Asia Cellular Satellite and its bank creditors in 1997. Under the Amended Agreement, AIL has, among others, assigned to the banks as collateral all of its intangible properties, including the Garuda Satellite, the system control facilities and system control equipment. On September 30, 2002, PT Asia Cellular Satellite, AIL, as guarantor, P.T. Bank International Indonesia, as security agent, and various banks signed the Rescheduling Agreement, which amended the terms of the Amended and Restated Credit Agreement dated December 29, 1998, moving the principal repayment dates to agreed periods with the final maturity date on January 31, 2012. As of December 2001, AIL has incurred recurring significant losses, negative operating cash flows, and significant levels of debt. The financial condition of AIL was partly due to the NSP s inability to generate the amount of revenues originally expected as the growth in subscriber numbers have been significantly lower than budgeted. These factors raised substantial doubt about AIL s ability to continue as a going concern. On this basis, we recognized an impairment provision in respect of our investment in AIL of Php3,314 million and ground station equipment of ACeS Philippines in relation to the business of AIL in 2001 of Php673 million.

PLDT s total investments in convertible notes of Unilink amounted to Php2,052 million. These notes are convertible into shares of common stock of Unilink or exchangeable into common stock of Home Cable at the option of the holder, if and when the law limiting the ownership of cable television systems to Philippine citizens or corporations, which are 100% owned by Philippine citizens, is eventually changed. Unilink is a Philippine corporation owning all the outstanding common stocks of Home Cable, which is also a Philippine corporation licensed to own, maintain and operate a cable television system in the Philippines. All of Unilink s shares in Home Cable have been pledged to a group of lenders as security for a loan to Home Cable. On December 6, 2001, Home Cable defaulted on the principal and interest payments in respect of certain of its loan obligations. On April 10, 2002, the loan agent, at the request of the lenders, delivered a notice to Home Cable declaring an event of default and accelerating the loan repayment. Consequently, the lenders are entitled to foreclose on or sell the collateral granted as security for the loan, including Unilink s share in Home Cable. In the event that Home Cable s lenders were to foreclose on Unilink s Home Cable shares, the lenders would be entitled to the proceeds from the sale thereof or, if such shares were not sold, to the shares, and Unilink would be subrogated to the lenders claims against Home Cable. Home Cable is currently engaged in negotiations with the lenders to restructure its debt. On the basis of Home Cable s default on certain of its obligations, the uncertainty surrounding the negotiations with its creditors and equity holders, and its financial condition, we provided for a full permanent decline in value of our investment totaling Php2,052 million in 2001. In June 2003, PLDT assigned and ceded unto the PLDT Beneficial Trust Fund, or BTF, all of its rights, interest and participation in respect of its investment in convertible notes of Unilink with a fair value of zero and effectively for zero consideration under U.S. GAAP. In addition, PLDT also ceded its rights, interest and participation to certain other assets unrelated to Unilink for and in consideration of partial payment of the contributions which PLDT is required to make to the BTF under PLDT s employee benefit plan.

The preparation of the estimated future cash flows involves significant judgment and estimations. While we believe that our assumptions are appropriate and reasonable, significant changes in our assumptions may materially affect our assessment of recoverable values and may lead to future additional impairment changes under U.S. GAAP.

Estimating Allowances for Doubtful Accounts

We estimate the allowance for doubtful accounts related to our trade receivables based on two methods. The amounts calculated using each of these methods are combined to determine the total amount we reserve. First, we evaluate specific accounts, mostly of foreign administrators and fixed line subscribers, or, where we have information that certain customers may be unable to meet their financial obligations. In these cases, we use judgment, based on the best available facts and circumstances, including but not limited to, the length of our relationship with the customer and the customer s current credit status based on third party credit reports and known market factors, to record specific reserves for customers against amounts due to reduce our receivables to amounts that we expect to collect. These specific reserves are re-evaluated and adjusted as additional information received impacts the amounts estimated. Second, a general provision is established as a certain percentage of operating revenues. This percentage is based on historical collection, write-off experience, current economic trends and changes in our customer payment terms. The amount and timing of recorded expenses for any period would differ if we made different judgments or utilized different estimates.

Full allowance is provided for receivables from permanently disconnected subscribers. Permanent disconnections are made after a series of collection steps following non-payment by subscribers. Such permanent disconnections generally occur within 105 days from due date. Partial allowance is provided for active subscribers based on the age status of the receivable.

Full allowance is provided for carrier accounts which have been past due for over 360 days from transaction date and after a review of the status of settlement with other carriers.

An increase in our allowance for doubtful accounts would increase our recorded operating expenses and decrease our current assets. Provision for doubtful accounts amounted to Php4,092 million in 2003, Php4,160 million in 2002 and Php3,221 million in 2001. The provision for doubtful accounts represented approximately 4% of our consolidated operating revenues for each of the years ended December 31, 2003, 2002 and 2001.

Acquisitions and Intangible Assets

Acquisitions have generally been accounted for as purchases. Accordingly, the acquisition of Smart was accounted for using the purchase method of accounting. The excess of the total acquisition cost over the fair value of the net assets acquired was Php23,096 million. Based on management's review and estimate, Php5,900 million was recorded as the value of customers acquired. Prior to 2002, the excess of the total acquisition cost over the fair value of the net assets acquired was amortized on a straight-line basis over five years. Starting 2002, the unamortized balance is reviewed annually for impairment using the fair value approach. On the other hand, prior to 2001, customers list for both GSM and analog subscribers were amortized over five years which at that time was the expected average period of the customer relationship. Beginning 2001, we revised our estimated useful life of the acquired GSM customer lists based on our analysis of customer churn rates over three years. The unamortized balance of the analog customer lists was fully impaired in 2001. Purchase accounting requires extensive use of accounting estimates and judgments to allocate the purchase price to the fair market values of the assets and liabilities purchased.

Foreign Exchange Revaluation Losses

When we incur unhedged foreign currency-denominated liabilities arising directly from the acquisition of property, plant and equipment invoiced in a foreign currency, such as U.S. dollar-denominated loans to finance equipment purchases, foreign exchange losses on those liabilities are charged or credited to operations in the current period. In recent years, the Philippine peso has depreciated significantly against the U.S. dollar, resulting in substantial foreign exchange losses, and has resulted in our incurring net losses for certain periods.

Investments

The various interests that we hold in companies are accounted for under three methods: consolidation, the equity method and the cost method. The applicable accounting method is generally determined based on our voting interest in a company. Majority-owned companies are consolidated, 20% to 50% owned companies are accounted for using the equity method and our investments in companies over which no significant influence is exercised or in cases where our investments are temporary, the investments are stated at cost.

Pension Cost

The determination of our obligation and cost for pension and other retirement benefits is dependent on our selection of certain assumptions used by actuaries in calculating such amounts. Those assumptions are described in *Note 19 Employee s Benefit Plan* to the accompanying consolidated financial statements in Item 18, and include among others, discount rates, expected returns on plan assets and rates of compensation increase. In accordance with U.S. GAAP, actual results that differ from our assumptions are accumulated and amortized over future periods and therefore, generally affect our recognized expense and recorded obligation in such future periods. While we believe that our assumptions are reasonable and appropriate, significant differences in our actual experience or significant changes in our assumptions may materially affect our pension and other retirement obligations.

Legal Contingencies

We are currently involved in various legal proceedings. Our estimate of the probable costs for the resolution of these claims has been developed in consultation with outside counsel handling our defense in these matters and is based upon an analysis of potential results. We currently do not believe these proceedings will have a material adverse effect on our consolidated financial position. It is possible, however, that future results of operations could be materially affected by changes in our estimates or in the effectiveness of our strategies relating to these proceedings. See Item 8. Financial Information Legal Proceedings.

Impact of Recently Issued Accounting Pronouncements

In June 2002, the Financial Accounting Standard Board, or FASB, issued SFAS 146, Accounting for Costs Associated with Exit or Disposal Activities. SFAS 146 provides guidance related to accounting for costs associated with disposal activities covered by SFAS 144 or with exit or restructuring activities previously covered by Emerging Issues Task Force, or EITF, Issue No. 94-3, Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring). SFAS 146 supersedes EITF Issue No. 94-3 in its entirety. SFAS 146 requires that costs related to exiting an activity or to a restructuring should not be recognized until the liability is incurred. SFAS 146 will be applied prospectively to exit or disposal activities that are initiated after December 31, 2002.

In January 2003, the FASB issued FASB Interpretation No., or FIN, 46, Consolidation of Variable Interest Entities. The primary objective of FIN 46 is to provide guidance on the identification of, and financial reporting for, entities over which control is achieved through means other than voting rights; such entities are known as variable interest entities. FIN 46 requires variable interest entities to be consolidated by the primary beneficiary of the variable interest entities and expands disclosure requirements for variable interest entities that are consolidated as well as those within which an enterprise holds a significant variable interest. For variable interests in entities commonly referred to as special purpose entities , implementation of this statement is required by January 1, 2004. And for all other variable interest entities, implementation is required by December 31, 2004.

In April 2003, the FASB issued SFAS 149, Amendment of SFAS 133 on Derivative Instruments and Hedging Activities. This Statement amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts (collectively referred to as derivatives) and for hedging activities under SFAS 133. This Statement is effective for contracts entered into or modified after June 30, 2003 and for hedging relationships designated after June 30, 2003.

In May 2003, the FASB issued SFAS 150 Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity . SFAS 150 establishes standards on how companies classify and measure certain financial instruments with characteristics of both liabilities and equity. The Statement requires that the Company classify as liabilities the fair value of all mandatorily redeemable financial instruments that had previously been recorded as equity or elsewhere in the consolidated financial statements. This Statement is effective for financial instruments entered into or modified after May 31, 2003, and otherwise effective for all existing financial instruments, except for minority interests in limited-life entities, beginning of the first interim period beginning after June 15, 2003. Certain provisions of this Statement relating to noncontrolling interests in limited-life subsidiaries were deferred indefinitely. We continue to monitor the deferral status of SFAS 150.

The adoption of FIN 46, SFAS 146, SFAS 149 and SFAS 150 did not have a material impact on PLDT Group s consolidated financial statements.

In May 2003, EITF Issue No. 00-21, Accounting for Revenue Arrangements with Multiple Deliverables, was finalized. EITF No. 00-21 provides guidance on how to account for arrangements that involve the delivery or performance of multiple products, services and/or rights to use assets. The provisions of EITF No. 00-21 apply to revenue arrangements entered into in fiscal periods beginning after June 15, 2003. In December 2003, the U.S. SEC issued Staff Accounting Bulletin, or SAB, No. 104, Revenue Recognition, which codifies and rescinds certain sections of SAB No. 101, Revenue Recognition , in order to make this interpretive guidance consistent with EITF No. 00-21. We are currently in the process of evaluating any effect the adoption of EITF No. 00-21 will have on our consolidated financial statements.

In December 2003, the FASB revised SFAS 132, Employers Disclosures about Pensions and Other Postretirement Benefits. It requires additional disclosures to those in the original SFAS 132 about the plan assets, benefit obligations, cash flows and net periodic benefit cost of defined benefit plans and other postretirement benefit plans. The new disclosures are generally effective for 2003 calendar yearend financial statements of public companies, with a delayed effective date for certain disclosures and for foreign plans. The requirements of this Statement are included in *Note 19 Employees Benefit Plans* to the accompanying consolidated financial statements in Item 18.

Results of Operations

The following table shows the contribution by each of our business segments to our consolidated operating revenues, operating expenses and net operating income (loss) for each of the years ended December 31, 2003, 2002 and 2001. Most of our revenues are derived from our operations within the Philippines. Our revenues derived from outside the Philippines consist primarily of revenues from incoming international calls to the Philippines.

	Years Ended December 31,					
	2003	**%(1)**	**2002**	**%(1)**	**2001**	**%(1)**
			(in millions)			
Operating Revenues						
Wireless	Php64,332	58	Php46,298	50	Php33,597	42
Fixed line	46,195	41	45,851	49	46,323	58
Information and communications technology	1,509	1	651	1	374	
	112,036	100	92,800	100	80,294	100
Operating Expenses						
Wireless	45,649	41	37,282	40	57,537	72
Fixed line	30,878	27	42,032	45	27,495	34
Information and communications technology	2,036	2	1,457	2	1,204	1
	78,563	70	80,771	87	86,236	107
Net Operating Income (Loss)						
Wireless	18,683	17	9,016	10	(23,940)	(30)
Fixed line	15,317	14	3,819	4	18,828	24
Information and communications technology	(527)	(1)	(806)	(1)	(830)	(1)
	Php33,473	30	Php12,029	13	(Php5,942)	(7)

(1) Operating expenses and net operating income (loss) as a percentage of operating revenues.

2003 Compared to 2002

Consolidated Operating Revenues

Largely driven by the continued strong growth of our wireless business, particularly Smart s cellular business, our consolidated operating revenues for 2003 increased by Php19,236 million, or 21%, to Php112,036 million from Php92,800 million in 2002. The revenue contribution of our wireless business accounted for 58% of our consolidated operating revenues for 2003, compared to 50% in 2002. Smart contributed Php58,740 million in revenues in 2003, an increase of 33% over its revenue contribution of Php44,316 million in 2002.

The following table shows the breakdown of our total consolidated operating revenues for the years ended December 31, 2003 and 2002 by business segment:

	Years Ended December 31,					
					Increase	
	2003	**%**	**2002**	**%**	**Amount**	**%**
			(in millions)			
Wireless	Php64,332	58	Php46,298	50	Php18,034	39
Fixed line	46,195	41	45,851	49	344	1
Information and communications technology	1,509	1	651	1	858	132
Total	Php112,036	100	Php92,800	100	Php19,236	21

Wireless

The following table summarizes our consolidated operating revenues from our wireless business for the years ended December 31, 2003 and 2002 by service segment:

	Years Ended December 31,					
					Increase (Decrease)	
	2003	**%**	**2002**	**%**	**Amount**	**%**
(in millions)						

Wireless services:						
Cellular services	Php51,001	79	Php30,583	66	Php20,418	67
Cellular handset sales	12,433	20	14,982	32	(2,549)	(17)
Satellite, VSAT and others	898	1	733	2	165	23
Total	Php64,332	100	Php46,298	100	Php18,034	39

Our wireless service revenues increased significantly by Php18,034 million, or 39%, to Php64,332 million in 2003 from Php46,298 million in 2002 mainly as a result of the continued strong growth in revenues generated from Smart s and Piltel s cellular services. Accordingly, as a percentage of our consolidated operating revenues, wireless service revenues increased to 58% in 2003 from 50% in 2002.

Cellular Service

Our cellular service revenues consist of:

- revenues derived from actual usage of the network by prepaid subscribers and any unused peso value of expired prepaid cards or electronic air time loads, net of discounts given to dealers;

- monthly service fees from postpaid subscribers, including (1) charges for calls in excess of allocated free local calls, (2) toll charges for national and international long distance calls, (3) charges for text messages of our GSM service customers in excess of allotted free text messages and (4) charges for value-added services, net of related content provider costs;

- revenues generated from incoming calls and messages to our subscribers, net of interconnection expenses; fees from reciprocal traffic from international correspondents; and revenues from inbound international roaming calls for the GSM service; and

- other charges, including those for reconnection and migration.

Our cellular service revenues in 2003 amounted to Php51,001 million, an increase of Php20,418 million, or 67%, from Php30,583 million in 2002. Cellular service revenues accounted for 46% of our consolidated operating revenues in 2003, compared to 33% in 2002. This increase was primarily due to increased traffic volumes and the 51% growth in our wireless subscriber base, which increased by 4,347,891 from 8,599,306 as of December 31, 2002 to 12,947,197 as of December 31, 2003.

The following table shows our cellular subscriber base as of December 31, 2003 and 2002:

	Years Ended December 31,			
			Increase	
	2003	**2002**	**Amount**	**%**
GSM Cellular Subscribers	12,947,197	8,599,306	4,347,891	51
Smart	10,080,112	6,825,686	3,254,426	48
Prepaid	9,831,135	6,649,038	3,182,097	48
Postpaid	248,977	176,648	72,329	41
Piltel Prepaid	2,867,085	1,773,620	1,093,465	62

Of our 12,947,197 GSM subscribers as of December 31, 2003, prepaid subscribers accounted for approximately 98% while postpaid subscribers accounted for the remaining 2%. Smart's prepaid GSM subscriber base grew by 48% to 9,831,135 as of December 31, 2003 from 6,649,038 as of December 31, 2002, whereas Smart's postpaid GSM subscriber base increased by 41% to 248,977 as of December 31, 2003 from 176,648 as of December 31, 2002. Smart s prepaid and postpaid net subscriber activations totaled 3,182,097 and 72,329, respectively, in 2003, or a monthly average addition of 265,175 prepaid and 6,027 postpaid subscribers. On the other hand, Piltel s prepaid subscribers increased by 62% to 2,867,085 as of December 31, 2003 from 1,773,620 as of December 31, 2002 or a monthly average addition of 91,122 subscribers.

Churn, or the rate at which existing subscribers have their services cancelled in a given period, is computed based on total disconnections in the period, net of reconnections in the case of postpaid subscribers, divided by the average of the number of subscribers at the beginning and the end of a month, all divided by the number of months in the same period.

Cellular Handset Sales

Our cellular revenues include revenues from the sale of handsets amounting to Php12,433 million, a decrease of Php2,549 million, or 17%, over the Php14,982 million in 2002. The decrease was attributable to lower sale of handsets in 2003 as compared to 2002.

Satellite, VSAT and Other Services

Our revenues from satellite, VSAT and other services consist mainly of rentals received for the lease of Mabuhay Satellite's transponders and Telesat's VSAT facilities to other companies and charges for ACeS Philippines satellite phone service. Total revenues from these services for 2003 amounted to Php898 million, an increase of Php165 million, or 23%, from Php733 million for 2002.

Fixed Line

Revenues generated from our fixed line business in 2003 totaled Php46,195 million, an increase of Php344 million, or 1%, from Php45,851 million in 2002. This increase was due to higher revenues generated from international long distance service and data and other network services, partially offset by decreased revenues from local exchange service, national long distance service, and miscellaneous services. As a percentage of our consolidated operating revenues, however, fixed line revenues decreased to 41% in 2003 from 49% in 2002 principally due to the continued strong growth of our wireless business.

The following table summarizes our consolidated operating revenues from our fixed line business for the years ended December 31, 2003 and 2002 by service segment:

	Years Ended December 31,					
					Increase (Decrease)	
	2003	**%**	**2002**	**%**	**Amount**	**%**
(in millions)						
Fixed line services:						
Local exchange	Php20,728	45	Php21,345	47	(Php617)	(3)
International long distance	12,634	27	10,636	23	1,998	19
National long distance	6,694	14	7,818	17	(1,124)	(14)
Data and other network	5,802	13	5,561	12	241	