



**MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS
For the Three Months Ended March 31, 2006**

In the following discussion and analysis of our financial condition and results of operations, unless the context indicates or otherwise requires, references to "we," "us," "our" or "PLDT Group" mean the Philippine Long Distance Telephone Company and its consolidated subsidiaries, and references to "PLDT" mean the Philippine Long Distance Telephone Company, not including its consolidated subsidiaries (see Note 2 – Summary of Significant Accounting Policies and Practices to the accompanying unaudited consolidated financial statements for a list of these subsidiaries, including a description of their respective principal business activities).

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the accompanying unaudited consolidated financial statements and the related notes. Our financial statements, and the financial information discussed below, have been prepared in accordance with Philippine generally accepted accounting principles, or Philippine GAAP, which differ in certain significant respects from generally accepted accounting principles in the United States.

The financial information appearing in this report and in the accompanying unaudited consolidated financial statements is stated in Philippine pesos. All references to "pesos," "Philippine pesos" or "Php" are to the lawful currency of the Philippines; all references to "U.S. dollars," "US\$" or "dollars" 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. Translations of Philippine peso amounts into U.S. dollars in this report and in the accompanying unaudited consolidated financial statements were made based on the exchange rate of Php51.158 to US\$1.00, the volume weighted average exchange rate at March 31, 2006 quoted through the Philippine Dealing System.

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 forward-looking statements and assumed facts or bases almost always vary from actual results, and the differences between the results implied by the forward-looking statements and 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 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 at 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 forward-looking statements in this report after the date hereof. In light of these risks and uncertainties, any forward-looking statement made in this report or elsewhere might not occur.

Financial Highlights and Key Performance Indicators

	<u>March 31,</u>	<u>December 31,</u>	<u>Increase (Decrease)</u>	
	<u>2006</u>	<u>2005</u>	<u>Amount</u>	<u>%</u>
(in millions, except for operational data, exchange rates and earnings per common share)				
Consolidated Balance Sheets				
Total assets	Php251,110	Php249,713	Php1,397	1
Property, plant and equipment	173,571	176,974	(3,403)	(2)
Cash and cash equivalents and short-term investments	37,945	32,810	5,135	16
Total equity	76,752	74,369	2,383	3
Interest-bearing financial liabilities	111,109	116,616	(5,507)	(5)
Notes payable and long-term debt	98,987	103,544	(4,557)	(4)
Net debt to equity ratio ⁽¹⁾	0.80x	0.95x	-	-
Three Months Ended March 31,				
	<u>2006</u>	<u>2005</u>	<u>Increase (Decrease)</u>	
		(Unaudited)	<u>Amount</u>	<u>%</u>
Consolidated Statements of Income				
Revenues and other income	Php30,879	Php30,144	Php735	2
Expenses	19,602	17,430	2,172	12
Income before income tax	11,277	12,714	(1,437)	(11)
Net income attributable to equity holders	8,581	9,217	(636)	(7)
Net income	8,765	9,239	(474)	(5)
Net income margin	28%	31%	-	-
Earnings per common share – basic	46.74	51.93	(5.19)	(10)
Consolidated Statements of Cash Flows				
Net cash provided by operating activities	15,429	15,464	(35)	-
Net cash used in investing activities	5,825	2,191	3,634	166
Capital expenditures	4,869	4,263	606	14
Net cash used in financing activities	3,997	10,459	(6,462)	(62)
Operational Data				
Number of cellular subscribers	20,899,631	20,252,513	647,118	3
Number of fixed lines in service	2,085,904	2,149,489	(63,585)	(3)
Number of broadband subscribers	140,110	57,843	82,267	142
Fixed Line	101,195	56,960	44,235	78
Wireless	38,915	883	38,032	4,307
Number of employees	20,134	18,581	1,553	8
Fixed Line	9,160	9,620	(460)	(5)
Wireless	5,076	5,294	(218)	(4)
ICT	5,898	3,667	2,231	61
Exchange Rates				
	<u>Php per US\$</u>	<u>Php per JP¥</u>		
March 31, 2006	Php51.158	Php0.4347		
December 31, 2005	53.062	0.4504		
March 31, 2005	54.747	0.5111		
December 31, 2004	56.341	0.5495		

(1) Net debt is derived by deducting cash and cash equivalents and short-term investments from long-term debt.

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 Smart Communications, Inc., or Smart, and Pilipino Telephone Corporation, or Piltel, our

cellular service providers; Meridian Telekoms, Inc., or Meridian, our wireless broadband provider; Wolfpac Mobile, Inc., or Wolfpac, our wireless content operator, Mabuhay Satellite Corporation, or Mabuhay Satellite, ACeS Philippines Cellular Satellite Corporation, or ACeS Philippines, and Telesat, Inc., or Telesat, our satellite and very small aperture terminal, or VSAT, operators;

- *Fixed Line* — fixed line telecommunications services are primarily provided through PLDT. We also provide fixed line services through PLDT's subsidiaries PLDT Clark Telecom, Inc., Subic Telecommunications Company, Inc., PLDT-Maratel, Inc., Piltel and Bonifacio Communications Corporation, which together account for approximately 3% of our consolidated fixed lines in service, and PLDT Global Corporation, or 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, Inc., or ePLDT; call center services provided under one umbrella brand name *ePLDT Ventus*, including Parlance Systems, Inc., or Parlance and Vocativ Systems, Inc., or Vocativ; Internet access and gaming services provided by ePLDT's subsidiaries, Infocom Technologies, Inc. or Infocom, Digital Paradise, Inc., or Digital Paradise, Digital Paradise Thailand, Ltd., or Digital Paradise Thailand, netGames, Inc., or netGames, Airborne Access Corporation, or Airborne Access and Level Up!, Inc., or Level Up!; and e-commerce, and IT-related services provided by other investees of ePLDT, as discussed in *Note 9 – Investments in Associates* to the accompanying unaudited consolidated financial statements.

We registered total revenues and other income of Php30,879 million in the first quarter of 2006, an increase of Php735 million, or 2%, as compared to Php30,144 million in the same period in 2005, primarily due to an increase in our service revenues and other income of Php700 million and Php141 million, respectively, partially offset by a decline in our non-service revenues of Php106 million.

Expenses increased by Php2,172 million, or 12%, to Php19,602 million in the first quarter of 2006 from Php17,430 million in the same period in 2005, largely resulting from increases in depreciation and amortization, and financing costs partly offset by lower cost of sales.

As a result of the foregoing, our net income decreased by Php474 million, or 5%, to Php8,765 million in the first quarter of 2006 from Php9,239 million in the same period in 2005. Consequently, basic earnings per common share decreased by 10% to Php46.74 in the first quarter of 2006 from Php51.93 in the same period in 2005.



Results of Operations

The table below shows the contribution by each of our business segments to our revenues and other income, expenses and net income for the three months ended March 31, 2006 and 2005. Most of our revenues are derived from our operations within the Philippines.

(in millions)	Wireless	Fixed Line	ICT	Inter-segment Transactions	Total				
For the three months ended									
March 31, 2006 (Unaudited)									
Revenues and other income	Php19,697	Php12,269	Php872	(Php1,959)	Php30,879				
Service	18,944	12,149	813	(1,931)	29,975				
Non-service	646	13	53	(3)	709				
Equity share in net income of associates	-	-	2	-	2				
Other income	107	107	4	(25)	193				
Expenses	9,567	11,136	858	(1,959)	19,602				
Income before income tax	10,130	1,133	14	-	11,277				
Net income for the period	7,894	842	29	-	8,765				
Net income attributable to equity shareholders	7,693	842	46	-	8,581				
For the three months ended									
March 31, 2005 (Unaudited)									
Revenues and other income	18,620	11,857	751	(1,084)	30,144				
Service	17,841	11,826	652	(1,044)	29,275				
Non-service	759	-	66	(10)	815				
Equity share in net income of associates	-	-	2	-	2				
Other income	20	31	31	(30)	52				
Expenses	9,038	8,755	721	(1,084)	17,430				
Income before income tax	9,582	3,102	30	-	12,714				
Net income for the period	6,937	2,272	30	-	9,239				
Net income attributable to equity shareholders	6,907	2,271	39	-	9,217				
Increase (Decrease)									
Revenues and other income	Php1,077	6	Php412	3	Php121	16	(Php875)	Php735	2
Service	1,103	6	323	3	161	25	(887)	700	2
Non-service	(113)	(15)	13	100	(13)	(20)	7	(106)	(13)
Other income	87	435	76	245	(27)	(87)	5	141	271
Expenses	529	6	2,381	27	137	19	(875)	2,172	12
Income before income tax	548	6	(1,969)	(63)	(16)	(53)	-	(1,437)	(11)
Net income for the period	957	14	(1,430)	(63)	(1)	(3)	-	(474)	(5)
Net income attributable to equity shareholders	786	11	(1,429)	(63)	7	18	-	(636)	(7)

Wireless

Revenues and Other Income

Our wireless business segment offers cellular services as well as satellite, VSAT, wireless broadband, and other services.



The following table summarizes our service and non-service revenues and other income from our wireless business for the three months ended March 31, 2006 and 2005 by service segment:

(in millions)	Three Months Ended March 31,					
	2006		2005		Increase (Decrease)	
	Amount	%	Amount	%	Amount	%
Wireless services:	(Unaudited)					
Service Revenues						
Cellular	Php18,205	92	Php17,188	92	Php1,017	6
Satellite, VSAT, wireless broadband and others	739	4	653	4	86	13
	<u>18,944</u>	<u>96</u>	<u>17,841</u>	<u>96</u>	<u>1,103</u>	<u>6</u>
Non-service Revenues						
Sale of cellular handsets and SIM-packs	646	3	759	4	(113)	(15)
Other Income	<u>107</u>	<u>1</u>	<u>20</u>	<u>-</u>	<u>87</u>	<u>435</u>
Total Wireless Revenues and Other Income	<u>Php19,697</u>	<u>100</u>	<u>Php18,620</u>	<u>100</u>	<u>Php1,077</u>	<u>6</u>

Service Revenues

Our wireless service revenues increased by Php1,103 million, or 6%, to Php18,944 million in the first quarter of 2006 compared to Php17,841 million in the same period in 2005, mainly as a result of the growth of Smart's and Piltel's subscriber base. As a percentage of our total wireless revenues and other income, service revenues remained relatively flat at 96% in the first quarter of 2006 and 2005.

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 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 service; and
- other charges, including those for reconnection and migration.

Our cellular service revenues in the first quarter of 2006 amounted to Php18,205 million, an increase of Php1,017 million, or 6%, from Php17,188 million in the same period in 2005. Cellular service revenues accounted for 96% of our wireless service revenues in the first quarter of 2006 and 2005.

As at March 31, 2006, Smart and Piltel cellular subscribers reached 20,899,631, an increase of 647,118, or 3%, over their combined cellular subscriber base of 20,252,513 as at March 31,

2005. Prepaid subscribers accounted for 99% of our total subscriber base as at March 31, 2006 and 2005. Prepaid and postpaid subscribers totaled 20,614,552 and 285,079 as at March 31, 2006, reflecting net subscriber activations of 486,009 and 5,001, respectively, in the first quarter of 2006.

Smart markets nationwide cellular communications services under the brand names *Smart Buddy*, *Smart Gold*, *addict mobile*, *addict mobile prepaid*, or *amp*, *Smart Infinity* and *Smart Kid prepaid*. *Smart Buddy*, *amp* and *Smart Kid prepaid* are prepaid services while *Smart Gold*, *Smart Infinity* and *addict mobile* are postpaid services, which are all provided through Smart's digital network.

Piltel markets its cellular prepaid service under the brand name *Talk 'N Text* which is provided through Smart's network. On December 22, 2004, the Board of Directors of Smart and Piltel approved the amendment of Piltel's and Smart's revenue sharing arrangement of 50-50 for the *Talk 'N Text* service to 80-20 in favor of Piltel.

Beginning March 11, 2005, Smart launched a series of promotions to test the market demand for fixed rate or "bucket" plans for voice and text services. Under a service branded as *Smart 258*, Smart and *Talk 'N Text* subscribers had the option to register for unlimited on-network (Smart-to-Smart) voice calls or unlimited on-network (Smart-to-Smart) text messaging service. Since launch, the promotion has taken on several variations involving changes in load denominations, the periods of network availability (peak/off-peak) as well as a "double text" variation.

The current *Smart 258* promotion, which has been extended until June 2, 2006, has the following features:

- Unlimited Text – Php15, Php30 and Php60 denominations with expiry periods of one, two and four days, respectively, with unlimited on-network text all day service; and
- Text and Call Combo – Php20 load denomination with unlimited text on-network for one day and a call with a maximum duration of five minutes and valid within 24 hours.

On August 23, 2005, Smart also operated a flat rate promotion which allows Smart and *Talk 'N Text* prepaid subscribers to make a call to another Smart or *Talk 'N Text* subscriber of up to three minutes for Php10, or extend up to five minutes for a flat rate of Php15. The flat rate promotion was relaunched on February 11, 2006 and is valid until May 13, 2006.

On February 12, 2006, Smart introduced a new variety of top-ups – *Smart Load* "All Text," which allows 10 and 20 messages without expiration for a suggested retail price of Php12 and Php23, respectively. On May 1, 2006, the number of messages allocated for the 10-message load was increased to 15. This promotion offering the additional five messages is effective until May 31, 2006.

On April 1, 2006, Smart rolled-out *Smart Click*, a chain of mobile Internet cafés. *Smart Click* Internet cafés are currently housed in air-conditioned 40-foot container vans and designed to provide remote communities with high-speed, wireless Internet access nationwide. *Smart Click* has established 12 mobile Internet cafés to-date and plans to open at least 20 branches within the first half of 2006.

On February 14, 2006, Smart launched its third generation or 3G service on a free-trial basis. Subscribers using Smart's network with 3G handsets in selected key areas could avail of



services such as video calling, video streaming, high-speed internet browsing and special 3G content downloading under Smart's 3G network.

On May 1, 2006, Smart unveiled new and expanded 3G services and announced as well the commercial rates of its 3G services. Under the introductory pricing scheme that took effect on May 1, Smart 3G rates are aligned with existing 2G rates while some services remain free of charge.

- Smart-to-Smart video calls remain free of charge while international video calls, initially available in three countries, are priced similarly to a regular IDD call at US\$0.40 per minute;
- all 3G video and audio streaming are charged a Php15 access fee for every 30 minutes plus a separate fee for content;
- 3G Internet and WAP browsing are priced at Php10 for every 30 minutes;
- downloads of 3G content such as video clip, ringtones, visual ringers and games range from Php20 to Php50 per download; and
- MMS among all Smart subscribers has been set at Php1 per MMS and Php2 for Smart-to-other networks.

The following table summarizes key measures of our cellular business as at and for the three months ended March 31, 2006 and 2005:

(in millions)	Three Months Ended March 31,			
	2006	2005	Increase (Decrease)	
			Amount	%
				(Unaudited)
Cellular service revenues	Php18,205	Php17,188	Php1,017	6
<i>By component</i>	<i>17,647</i>	<i>16,714</i>	<i>933</i>	<i>6</i>
Voice	8,246	8,326	(80)	(1)
Data	9,401	8,388	1,013	12
<i>By service type</i>	<i>17,647</i>	<i>16,714</i>	<i>933</i>	<i>6</i>
Prepaid	16,486	15,695	791	5
Postpaid	1,161	1,019	142	14
<i>Others⁽¹⁾</i>	<i>558</i>	<i>474</i>	<i>84</i>	<i>18</i>

(1) Refers to other non-subscriber-related revenues consisting primarily of inbound international roaming fees, revenues from Smart's public calling offices and payphone businesses, revenues from Wolfpac and Smart Money Holdings Corporation and a small number of leased line contracts.

	March 31,			
	2006	2005	Increase	
			Amount	%
				(Unaudited)
Cellular subscriber base	20,899,631	20,252,513	647,118	3
Prepaid	20,614,552	19,984,376	630,176	3
Smart	15,256,105	15,242,173	13,932	-
Piltel	5,358,447	4,742,203	616,244	13
Postpaid	285,079	268,137	16,942	6

	Three Months Ended March 31,			
	2006	2005⁽¹⁾	Increase (Decrease)	
			Amount	%
			(Unaudited)	
Systemwide traffic volumes (in millions)				
Calls (in minutes)				
Domestic	1,385	1,307	78	6
International	868	945	(77)	(8)
Inbound	517	362	155	43
Outbound	476	319	157	49
Outbound	41	43	(2)	(5)
Text messages				
Standard	49,721	11,565	38,156	330
25 ⁸ Unlimited	9,186	10,561	(1,375)	(13)
	40,535	1,004	39,531	3,937

(1) *Smart 25⁸ Unlimited Call and Text promotion was launched on March 11, 2005.*

Voice Services

Cellular revenues from voice services, which include all voice traffic and voice value-added services such as voice mail and international roaming, decreased by Php80 million, or 1%, to Php8,246 million in the first quarter of 2006 from Php8,326 million in the same period in 2005, primarily due to a 12% drop in the average outbound voice usage per subscriber from 17 minutes per month in the first quarter of 2005 to 15 minutes per month in the same period in 2006.

Air time rates for postpaid subscribers vary depending on the type of postpaid plan selected by subscribers.

Data Services

Cellular revenues from data services, which include all text messaging-related services as well as value-added services, increased by Php1,013 million, or 12%, to Php9,401 million in the first quarter of 2006 from Php8,388 million in the same period in 2005. Cellular data services accounted for 52% of cellular service revenues in the first quarter of 2006, compared to 49% in the same period in 2005.



The following table shows the breakdown of cellular data revenues for the three months ended March 31, 2006 and 2005:

	Three Months Ended March 31,			
	2006	2005	Increase (Decrease)	
		(Unaudited)	Amount	%
(in millions)				
Text messaging				
Domestic	Php8,052	Php6,689	Php1,363	20
Standard	6,001	6,551	(550)	(8)
25 ⁸ Unlimited	2,051	138	1,913	1,386
International	434	452	(18)	(4)
	<u>8,486</u>	<u>7,141</u>	<u>1,345</u>	<u>19</u>
Value-added services				
Non-Zed ⁽¹⁾	613	680	(67)	(10)
<i>Smart Zed</i> TM	100	172	(72)	(42)
<i>Smart Money</i>	23	21	2	10
Mobile Banking	1	1	-	-
Roaming SMS and WAP	178	373	(195)	(52)
	<u>915</u>	<u>1,247</u>	<u>(332)</u>	<u>(27)</u>
Total	<u>Php9,401</u>	<u>Php8,388</u>	<u>Php1,013</u>	<u>12</u>

(1) Value-added services developed by Smart on its own platform.

Text messaging-related services contributed revenues of Php8,486 million in the first quarter of 2006, an increase of Php1,345 million, or 19%, compared to Php7,141 million in the same period in 2005, and accounted for 90% and 85% of the total cellular data revenues in the first quarter of 2006 and 2005. The increase in revenues from text messaging-related services resulted mainly from the ongoing *Smart 25⁸ Unlimited Text* promotion and an increase in *Pasa Load* transactions. Text messaging revenues from the *Smart 25⁸* promotions totaled Php2,051 million. Value-added services, which contributed revenues of Php915 million in the first quarter of 2006, decreased by Php332 million, or 27%, from Php1,247 million in the same period in 2005 primarily due to lower usage of roaming SMS and WAP, *Smart Zed*TM and non-Zed services in the first quarter of 2006 as compared to the same period in 2005.

Text messages, excluding *Smart 25⁸* messages, totaled 9,186 million in the first quarter of 2006, a decrease of 1,375 million, or 13%, from 10,561 million in the same period in 2005 due to a shift to unlimited texting service. *Smart 25⁸* messages in the first quarter of 2006 totaled 40,535 million, an increase of 39,531 million as compared to 1,004 million in the same period in 2005.

Subscriber Base, ARPU and Churn Rates

Prepaid subscribers accounted for approximately 99% of our 20,899,631 subscribers as at March 31, 2006, while postpaid subscribers accounted for the remaining 1%. The cellular prepaid subscriber base grew by 3% to 20,614,552 as at March 31, 2006 from 19,984,376 as at March 31, 2005, whereas the postpaid subscriber base increased by 6% to 285,079 as at March 31, 2006 from 268,137 as at March 31, 2005.



Our net subscriber activations (reductions) for the three months ended March 31, 2006 and 2005 were as follows:

	Three Months Ended March 31,			
	2006	2005	Increase (Decrease)	
			Amount	%
		(Unaudited)		
Prepaid				
Smart ⁽¹⁾	111,987	920,885	(808,898)	(88)
Piltel	374,022	129,753	244,269	188
Postpaid	5,001	(6,357)	11,358	179
Total	491,010	1,044,281	(553,271)	(53)

(1) Subscriber activations were higher in 2005 due to the SIM-swapping promotion which was terminated only in May 2005.

Revenues attributable to our cellular prepaid service amounted to Php16,486 million in the first quarter of 2006, a 5% increase over the Php15,695 million earned in the same period in 2005. Prepaid service revenues in the first quarter of 2006 and 2005 accounted for 93% and 94%, respectively, of voice and data revenues. Revenues attributable to Smart's postpaid service amounted to Php1,161 million in the first quarter of 2006, a 14% increase over the Php1,019 million earned in the same period in 2005 and accounted for 7% and 6% of voice and data revenues in the first quarter of 2006 and 2005, respectively.

The following table summarizes our cellular ARPUs for the three months ended March 31, 2006 and 2005:

	Three Months Ended March 31,								
	Gross		Increase (Decrease)		Net		Increase (Decrease)		
	2006	2005	Amount	%	2006	2005	Amount	%	
			(Unaudited)						
Prepaid									
Smart	Php356	Php356	Php-	-	Php294	Php289	Php5	2	
Piltel	245	269	(24)	(9)	207	220	(13)	(6)	
Prepaid – Blended	328	335	(7)	(2)	272	273	(1)	-	
Postpaid – Smart	1,867	1,767	100	6	1,386	1,257	129	10	
Prepaid and Postpaid Blended	349	355	(6)	(2)	287	286	1	-	

ARPU is computed for each month by dividing the revenues for the relevant services for the month by the average of the number of subscribers at the beginning and at the end of the month. Gross monthly ARPU is computed by dividing the revenues for the relevant services, gross of dealer discounts and allocated content-provider costs, including interconnection income but excluding inbound roaming revenues, by the average number of subscribers. Net monthly ARPU, on the other hand, is calculated based on revenues net of dealer discounts and allocated content-provider costs and interconnection income net of interconnection expense. ARPU for any period of more than one month is calculated as the simple average of the monthly ARPUs in that period.

Prepaid service revenues consist mainly of charges for subscribers' actual usage of their loads. Gross monthly ARPU for Smart prepaid subscribers in first quarter of 2006 and 2005 was Php356. The average outbound local and international voice revenue per subscriber declined in the first quarter of 2006 compared to the same period in 2005, but was offset by an increase in the average text messaging revenue and inbound international revenue per subscriber. On a net basis,

ARPU in the first quarter of 2006 increased by 2% to Php294 from Php289 in the same period in 2005. Gross monthly ARPU for *Talk 'N Text* subscribers in the first quarter of 2006 was Php245, a decrease of 9% compared to Php269 in the same period in 2005. The decline was attributable to the decrease in the average outbound local voice revenue per subscriber as well as the average inbound revenue per subscriber partly offset by an increase in the average text messaging revenue per subscriber. On a net basis, ARPU in the first quarter of 2006 decreased by 6% to Php207 from Php220 in the same period in 2005.

Monthly ARPU for Smart's postpaid services is calculated in a manner similar to that of prepaid service, except that the revenues consist mainly of monthly service fees and charges on usage in excess of the monthly service fees.

Gross monthly ARPU for postpaid subscribers increased by 6% to Php1,867 while net monthly ARPU increased by 10% to Php1,386 in the first quarter of 2006 as compared to Php1,767 and Php1,257 in the same period in 2005, respectively. Prepaid and postpaid monthly gross blended ARPU was Php349 in the first quarter of 2006, a decrease of 2% compared to Php355 in the same period in 2005. Monthly net blended ARPU increased to Php287 in the first quarter of 2006 from Php286 in the same period in 2005.

Our quarterly prepaid and postpaid ARPUs for the three months ended March 31, 2006 and 2005 were as follows:

	Prepaid				Postpaid	
	Smart		Piltel		Smart	
	Gross	Net	Gross	Net	Gross	Net
	(Unaudited)					
2006						
First Quarter	Php356	Php294	Php245	Php207	Php1,867	Php1,386
2005						
First Quarter	Php356	Php289	Php269	Php220	Php1,767	Php1,257
Second Quarter	357	294	262	212	1,896	1,360
Third Quarter	343	285	234	194	1,889	1,389
Fourth Quarter	370	308	261	220	1,923	1,467

Churn, or the rate at which existing subscribers have their service 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 at the end of a month, all divided by the number of months in the same period.

Prior to June 2004, a prepaid cellular subscriber was recognized as an active subscriber when that subscriber activated and used the SIM card in the handset, which contained pre-stored air time. The pre-stored air time, which can be used for both voice and text, was reduced from Php100 to Php50 in April 2004. In May 2005, this was changed to Php1 plus 50 free SMS which could only be used upon purchase or reload of air time of any value. Subscribers can reload their air time by purchasing prepaid "call and text" cards; by purchasing additional air time "over the air" via *Smart Load* or *Smart Load "All Text"*; and by receiving loads of Php2, Php5, Php10 and Php15 via *Pasa Load*, 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 cellular subscriber is disconnected if the subscriber does not reload within four months after the full usage or expiry of the last reload. Our current policy is to recognize a prepaid subscriber as "active" only when the subscriber activates and uses the SIM card and reloads at least once during the month of initial activation or in the immediate succeeding month. For example, if a customer activated a SIM card

in April but had not reloaded by May 31, this customer would not be counted as a subscriber. The rationale for this change stems from our observance of “SIM-swapping” activities in the market. “SIM-swapping” refers to the promotional activity wherein subscribers can exchange their current prepaid SIM card for another operator’s SIM card at no cost to the subscriber. We believe that these activities have given rise to a situation where certain subscribers swap their SIM cards between mobile operators upon full usage of the pre-stored air time, which may result in our subscriber base reflecting a certain number of transient subscribers at any one point in time. In May 2005, we terminated our “SIM swapping” promotions; as a result, our churn rates increased beginning in the third quarter of 2005 and continuing on to the first quarter of 2006.

For Smart prepaid, the average monthly churn rate for the first quarter of 2006 was 3.4%, compared to 2.7% in the same period in 2005, while the average monthly churn rate for *Talk ‘N Text* subscribers was 3.7% in the first quarter of 2006 compared to 4.6% in the same period in 2005. The increased churn in our prepaid service can be attributed primarily to the residual effect of the termination of the “SIM-swapping” activities described above.

The average monthly churn rate for Smart's postpaid subscribers for the first quarter of 2006 was 1.3%, compared to 2.5% in the same period in 2005. Smart's policy is to redirect outgoing calls to an interactive voice response system if the postpaid subscriber's account is either 45 days overdue or the subscriber has exceeded the prescribed credit limit. If the subscriber does not make a payment within 44 days of redirection, the account is disconnected. Within this 44-day period, a series of collection activities are implemented, involving the sending of a collection letter, call-out reminders and collection messages via text messaging.

Satellite, VSAT, Wireless Broadband and Other Services

Our revenues from satellite, VSAT, wireless broadband and other services consist mainly of rentals received for the lease of Mabuhay Satellite's transponders and Telesat's VSAT facilities to other companies, wireless broadband service revenues for Meridian, charges for ACeS Philippines' satellite phone service and service revenues generated from a PLDT Global subsidiary's mobile virtual network operations. Meridian offers a number of wireless broadband services with 38,915 subscribers as of March 31, 2006, including 35,105 *Smart WiFi* subscribers. *Smart WiFi*, the fixed wireless broadband service of Smart linked to Smart wireless broadband-enabled base stations, allows people to connect to the Internet using an outdoor aerial antenna installed in a subscriber's home. In April 2006, this service was relaunched as *Smart Bro*.

Gross revenues from these services for the first quarter of 2006 amounted to Php739 million, an increase of Php86 million, or 13%, from Php653 million in the same period in 2005 principally due to the growth in our wireless broadband business.

Non-service Revenues

Our wireless non-service revenues consist of:

- proceeds from sales of cellular handsets; and
- proceeds from sales of cellular SIM-packs.

Our wireless non-service revenues decreased by Php113 million, or 15%, to Php646 million in the first quarter of 2006 as compared to Php759 million in the same period in 2005, primarily due to lower handset sales. In the first quarter of 2006, activations were driven more by

SIM-pack sales.

Other Income

All other income/gains such as rental income and gain on disposal of property, which do not fall under service and non-service revenues, are included under this classification. Our wireless business segment generated other income of Php107 million in the first quarter of 2006, an increase of Php87 million, or 435%, as compared to Php20 million in the same period in 2005.

Expenses

Expenses associated with our wireless business in the first quarter of 2006 amounted to Php9,567 million, an increase of Php529 million, or 6%, from Php9,038 million in the same period in 2005. A significant portion of this increase was attributable to higher rent, provisions and compensation and benefits, partially offset by lower cost of sales and selling and promotions. As a percentage of our total wireless revenues and other income, expenses associated with our wireless business remained flat at 49% in the first quarter of 2006 and 2005.

Cellular business expenses accounted for 95% of our wireless business expenses, while satellite, VSAT, wireless broadband and other business expenses accounted for the remaining 5% of our wireless business expenses in the first quarter of 2006 as compared to 96% and 4%, respectively, in the same period in 2005.

The following table summarizes the breakdown of our wireless-related expenses for the three months ended March 31, 2006 and 2005 and the percentage of each expense item to the total:

	Three Months Ended March 31,					
	2006		2005		Increase (Decrease)	
	%	%	Amount		%	
			(Unaudited)			
(in millions)						
Wireless services						
Depreciation and amortization	Php2,576	27	Php2,460	27	Php116	5
Rent	1,702	18	967	11	735	76
Cost of sales	1,202	12	2,004	22	(802)	(40)
Compensation and benefits ⁽¹⁾	1,042	11	844	9	198	23
Maintenance	923	10	782	9	141	18
Selling and promotions	793	8	1,034	12	(241)	(23)
Professional and other contracted services	422	4	358	4	64	18
Taxes and licenses	347	4	376	4	(29)	(8)
Communication, training and travel	253	3	242	3	11	5
Insurance and security services	215	2	246	3	(31)	(13)
Provisions	158	2	(54)	(1)	212	393
Amortization of intangible assets	63	1	71	1	(8)	(11)
Financing costs	(360)	(4)	(507)	(6)	147	29
Other expenses	231	2	215	2	16	7
Total	Php9,567	100	Php9,038	100	Php529	6

(1) Includes salaries and benefits, incentive plan, pension and manpower rightsizing program, or MRP, costs.

Depreciation and amortization charges increased by Php116 million, or 5%, to Php2,576 million in the first quarter of 2006, principally due to additional depreciation provided for certain equipment amounting to Php176 million and Php120 million for the first quarter of 2006 and 2005, respectively; the useful lives of these certain equipment have been shortened due to network and

equipment upgrade. For further details, see *Note 8 – Property, Plant and Equipment* to the accompanying unaudited consolidated financial statements.

Rent expenses increased by Php735 million, or 76%, to Php1,702 million on account of an increase in domestic fiber optic network, or DFON, facilities leased by Smart from PLDT and site rental expense. As at March 31, 2006, we had 4,329 GSM cell sites and 6,043 base stations, compared with 4,071 GSM cell sites and 5,480 base stations as at March 31, 2005.

Cost of sales decreased by Php802 million, or 40%, to Php1,202 million due to a decrease in volume of phone kits sold and the termination of SIM-swapping activities in May 2005. The breakdown of cost of sales for our wireless business for the three months ended March 31, 2006 and 2005 is as follows:

	Three Months Ended March 31,			
	2006	2005	Increase (Decrease)	
			Amount	%
		(Unaudited)		
(in millions)				
Cost of cellular handsets and SIM-packs sold	Php1,155	Php1,959	(Php804)	(41)
Cost of satellite air time and terminal units	47	45	2	4
	<u>Php1,202</u>	<u>Php2,004</u>	<u>(Php802)</u>	<u>(40)</u>

Compensation and benefits expenses increased by Php198 million, or 23%, to Php1,042 million, primarily due to salary increases and higher long-term incentive costs of Smart. On the other hand, Smart's employee headcount decreased by 220, or 4%, to 5,024 in the first quarter of 2006 compared to 5,244 in the same period in 2005.

Maintenance expenses increased by Php141 million, or 18%, to Php923 million, mainly on account of higher expenses for electricity and power generation for cell sites and higher repairs and maintenance costs for network facilities and information technology equipment.

Selling and promotion expenses decreased by Php241 million, or 23%, to Php793 million due to efficient media spending and termination of certain media contracts.

Professional and other contracted services increased by Php64 million, or 18%, to Php422 million, primarily due to increased legal, technical service, call center and contracted service fees.

Taxes and licenses decreased by Php29 million, or 8%, to Php347 million primarily due to a decrease in Smart's business-related taxes.

Communication, training and travel expenses increased by Php11 million, or 5%, to Php253 million, due to higher foreign-related expenses incurred in the first quarter of 2006.

Insurance and security services decreased by Php31 million, or 13%, to Php215 million, primarily due to the decrease in site security expenses and lower amortization charges on prepaid insurance contracts.

Provisions increased by Php212 million, or 393%, to Php158 million, primarily due to an increase in write-down of slow-moving handsets to net realizable values. The breakdown of provisions for the three months ended March 31, 2006 and 2005 is as follows:

	Three Months Ended March 31,			
	2006	2005	Increase	
			Amount	%
		(Unaudited)		
(in millions)				
Doubtful accounts	Php49	Php35	Php14	40
Write-down (reversal of write-down) of inventories to net realizable value	109	(89)	198	222
	<u>Php158</u>	<u>(Php54)</u>	<u>Php212</u>	<u>393</u>

Amortization of intangible assets decreased by Php8 million, or 11%, to Php63 million mainly due to a reduction in the amount of intangible assets booked by Smart from the purchase of Meridian following the finalization by an independent appraiser of the valuation work on the intangible assets in September 2005.

Financing costs in the first quarter of 2006 amounted to a negative Php360 million compared to a negative Php507 million in the same period in 2005, due to the combined results of: (1) lower foreign exchange gains recognized in the first quarter of 2006 compared to the same period in 2005; (2) lower accretion on financial liabilities with the conversion of holders of convertible preferred shares to common shares; and (3) lower loss on derivatives recorded in the first quarter of 2006 as compared to the same period in 2005. The breakdown of our financing costs for our wireless business for the three months ended March 31, 2006 and 2005 is as follows:

	Three Months Ended March 31,			
	2006	2005	Change	
			Amount	%
		(Unaudited)		
(in millions)				
Accretion on financial liabilities – net	Php545	Php707	(Php162)	(23)
Interest on loans and related items	405	456	(51)	(11)
Dividends on preferred stock subject to mandatory redemption	49	67	(18)	(27)
Financing charges	25	47	(22)	(47)
Loss on derivative transactions – net	1	127	(126)	(99)
Capitalized interest	(61)	(3)	(58)	1,933
Interest income	(309)	(293)	(16)	5
Foreign exchange gains – net	(1,015)	(1,615)	600	(37)
	<u>(Php360)</u>	<u>(Php507)</u>	<u>Php147</u>	<u>29</u>

Other expenses increased by Php16 million, or 7%, to Php231 million due to higher various business and operational-related expenses such as office supplies expense.

Provision for Income Tax

Provision for income tax decreased by Php409 million, or 15%, to Php2,236 million in the first quarter of 2006 from Php2,645 million in the same period in 2005. In the first quarter of 2006, the effective tax rate for our wireless business was 22% compared to 28% in the same period in 2005 due to differences in the net movement of deferred tax assets.

Net Income

Our wireless business segment recorded a net income of Php7,894 million in the first quarter of 2006, an increase of Php957 million, or 14%, over Php6,937 million registered in the same period in 2005, primarily due to the growth in our cellular service revenues and lower provision for income tax, which partly offset an increase in operating expenses.

Fixed Line

Revenues and Other Income

Our fixed line business provides local exchange service, international and national long distance services, data and other network services, and miscellaneous services. Total fixed line revenues generated from our fixed line business in the first quarter of 2006 totaled Php12,269 million, an increase of Php412 million, or 3%, from Php11,857 million in the same period in 2005.

The following table summarizes revenues from our fixed line business for the three months ended March 31, 2006 and 2005 by service segment:

	Three Months Ended March 31,					
	2006		2005		Increase (Decrease)	
	Amount	%	Amount	%	Amount	%
	(Unaudited)					
(in millions)						
Fixed line services:						
Service Revenues						
Local exchange	Php4,348	35	Php4,664	39	(Php316)	(7)
International long distance	2,559	21	3,010	26	(451)	(15)
National long distance	1,810	15	1,788	15	22	1
Data and other network	3,068	25	2,058	17	1,010	49
Miscellaneous	364	3	306	3	58	19
	12,149	99	11,826	100	323	3
Non-Service Revenues	13	—	—	—	13	100
Other Income	107	1	31	—	76	245
Total Fixed Line Revenues and Other Income	Php12,269	100	Php11,857	100	Php412	3

Service Revenues

Local Exchange Service

Our local exchange service revenues consist of:

- flat monthly fees for our postpaid service;
- installation charges and other one-time fees associated with the establishment of customer service;
- revenues from usage of prepaid cards for calls within the local area and any unused peso value of expired prepaid cards; and
- charges for special features, including bundled value-added services such as call waiting, call forwarding, multi-party conference calling, speed calling and caller ID.



The following table summarizes key measures of our local exchange service business as at and for the three months ended March 31, 2006 and 2005:

	Three Months Ended March 31,			
	2006	2005	Increase (Decrease)	
			Amount	%
	(Unaudited)			
Total local exchange service revenues (in millions)	Php4,348	Php4,664	(Php316)	(7)
Number of fixed lines in service	2,085,904	2,149,489	(63,585)	(3)
Number of fixed line employees	9,160	9,620	(460)	(5)
Number of fixed lines in service per employee	228	223	5	2

Revenues from our local exchange service decreased by Php316 million, or 7%, to Php4,348 million in the first quarter of 2006 from Php4,664 million in the same period in 2005. The decrease was primarily due to a 3% decline in the number of fixed lines in service and the appreciation of the peso which required us to make downward adjustments in our monthly local service rates. The percentage contribution of local exchange revenues to our fixed line service revenues decreased to 36% in the first quarter of 2006 compared to 39% in the same period in 2005.

Fixed line net reduction in the first quarter of 2006 was 27,895 compared to a net reduction of 2,538 in the same period in 2005. In the first quarter of 2006, prepaid and postpaid fixed lines in service declined by 20,980 and 6,915, respectively. As at March 31, 2006, postpaid and prepaid fixed line subscribers totaled 1,783,982 and 301,922, which accounted for approximately 86% and 14%, respectively, of our total fixed lines in service.

Initially intended as an affordable alternative telephone service for consumers under difficult economic conditions, our prepaid fixed line services now form an important part of our overall churn and credit risk exposure management and subscriber retention strategy. Prepaid subscribers are charged based on usage at a rate of Php1.00 per minute for local calls, but the rates for prepaid and postpaid fixed line subscribers for national and international long distance calls are the same. 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. All sales of prepaid cards, whether through dealers or through PLDT's business offices, are non-refundable.

Pursuant to a currency exchange rate adjustment mechanism authorized by the Philippine National Telecommunications Commission, or the NTC, we adjust our monthly local service rates upward or downward by 1% for every Php0.10 change in the peso-to-dollar exchange rate relative to a base rate of Php11.00 to US\$1.00. During the first quarter of 2006 and 2005, we implemented three downward adjustments in our monthly local service rates. The average Philippine peso to U.S. dollar rate factored in our monthly local service rates in the first quarter of 2006 was Php51.847 to US\$1.00, compared to an average of Php54.982 to US\$1.00 in the same period in 2005. This change in the average peso-to-dollar rate translated to a peso appreciation of 5%, which resulted in an average net decrease of approximately 5% in our monthly local service rates in the first quarter of 2006.

International Long Distance Service

Our international long distance service revenues, which we generate through our international gateway facilities, consist of:

- inbound call revenues representing settlements from foreign telecommunications carriers for inbound international calls, virtual transit and hubbing service and reverse charged calls such as received collect and home country direct service;
- access charges paid to us by other Philippine telecommunications carriers for terminating inbound international calls to our local exchange network; and
- outbound call revenues representing amounts billed to our customers (other than our cellular customers) for outbound international calls, net of amounts payable to foreign telecommunications carriers for terminating calls in their territories.

The following table shows information about our international fixed line long distance business for the three months ended March 31, 2006 and 2005:

	Three Months Ended March 31,			
	2006	2005	Increase (Decrease)	
		(Unaudited)	Amount	%
Total international long distance service revenues (in millions)	Php2,559	Php3,010	(Php451)	(15)
Inbound	2,147	2,543	(396)	(16)
Outbound	412	467	(55)	(12)
International call volumes (in million minutes, except call ratio)	514	585	(71)	(12)
Inbound	468	549	(81)	(15)
Outbound	46	36	10	28
Inbound-outbound call ratio	10.2:1	15.3:1	-	-

Our total international long distance service revenues decreased by Php451 million, or 15%, to Php2,559 million in the first quarter of 2006 from Php3,010 million in the same period in 2005 due to the peso appreciation coupled with the decrease in call volumes largely as a result of alternative means of communications such as e-mailing, texting and Internet telephony. The percentage contribution of international long distance service revenues to our fixed line service revenues decreased to 21% in the first quarter of 2006 from 26% in the same period in 2005.

Our revenues from inbound international long distance service decreased by Php396 million, or 16%, due to a decrease in inbound traffic volume by 81 million minutes to 468 million minutes in the first quarter of 2006. In addition, the appreciation of the peso to the U.S. dollar with average rates of Php51.847 during the first quarter of 2006 and Php54.982 during the same period in 2005 contributed to the decrease in our inbound international long distance revenues in peso terms since settlement charges for inbound calls are billed in U.S. dollars or in special drawing rights, an established method of settlement among international telecommunications carriers using values based on a basket of foreign currencies that are translated into pesos at the time of billing.

Our revenues from outbound international long distance service decreased by Php55 million, or 12%, in the first quarter of 2006, primarily due to a decline in average revenue per minute as a result of lower average collection rate with the introduction of low-rate services such as *PLDT ID-DSL* and the modified *Budget Card*, and the peso appreciation in the first quarter of 2006.

On September 15, 2005, we introduced *PLDT ID-DSL*, a service that allows overseas calls for registered *myDSL* plan subscribers using a regular PLDT fixed line or a voice pad dialer for as low as US\$0.10 per minute or US\$0.08 per minute, respectively, depending on the subscribers' DSL plan/package.

To address the market's demand for low-priced international calls, PLDT modified the *Budget Card*, a prepaid call card, offering a reduced IDD rate of Php5 per minute, as a promotional offer starting September 24, 2005, for calls to 89 overseas destinations including the United States, Canada, Japan and China. Beginning March 4, 2006, *Budget Card* has been further modified to Php3, Php5 and Php8 per minute calls depending on the destination and now has 100 overseas destinations, including Saudi Arabia and other Middle East countries. *Budget Cards* are sold in denominations of Php200 and Php100, which must be consumed within 30 days from first use.

National Long Distance Service

Our national long distance service revenues consist of:

- per minute charges for calls made by our fixed line customers outside of the local service areas but within the Philippines, net of interconnection charges payable for calls carried through the backbone network of, and/or terminating to the customer of, another telecommunications carrier;
- access charges received from other telecommunications carriers for calls carried through our backbone network and/or terminating to our customers; and
- fixed charges paid by other telephone companies, charges retained by PLDT for calls terminating to cellular subscribers within the local area, and local access charges paid by cellular operators for calls by cellular subscribers that terminate to our local exchange network.

The following table shows our national long distance service revenues and call volumes for the three months ended March 31, 2006 and 2005:

	Three Months Ended March 31,			
	2006	2005	Increase	
			Amount	%
	(Unaudited)			
Total national long distance service revenues (in millions)	Php1,810	Php1,788	Php22	1
National long distance call volumes (in million minutes)	545	449	96	21

Our national long distance service revenues increased by Php22 million, or 1%, to Php1,810 million in the first quarter of 2006 from Php1,788 million in the same period in 2005 due to an increase in call volumes partially offset by a lower average revenue per minute due to our Php10 per call promotion. Accordingly, the percentage contribution of national long distance revenues to our fixed line service revenues was 15% in the first quarter of 2006 and 2005.

On February 14, 2005, we launched a Php10 per call promotion to PLDT landline subscribers nationwide and for calls to PLDT, to Smart and *Talk 'N Text* subscribers. This promotion was launched with the objective of determining a more effective tariff structure that would stimulate landline usage. Under the promotion, NDD calls between any PLDT landline



subscriber nationwide or to all Smart and *Talk 'N Text* subscribers were charged Php10 per call instead of being charged on a per minute basis.

On May 12, 2005, PLDT began offering the Php10 per call promotion with an additional Php5 per call for the same unlimited talktime to Smart and *Talk 'N Text* subscribers. PLDT to PLDT NDD calls below the equivalent Php10 toll usage were charged based on the regular rate per minute. On August 12, 2005, PLDT ceased offering the Php10 per call promotion to calls terminating to Smart and *Talk 'N Text* subscribers.

Beginning September 12, 2005, PLDT charged an optional Php20 add-on monthly service fee for PLDT landline subscribers who may want to continue to avail themselves of the Php10 per call promotion for calls within our network.

In January 2006, PLDT launched the *10-10-10* promotion. This promotion offers a flat rate of Php10 for unlimited calls terminating PLDT to PLDT and Smart and *Talk 'N Text* subscribers for a Php50 monthly service fee.

PLDT capped the Php10 per call service to Smart and *Talk 'N Text* subscribers to those who registered on or before February 24, 2006. PLDT fixed line subscribers, however, can still register and avail of the unlimited Php10 per call service for national long distance calls within the PLDT network.

Data and Other Network Services

Our data and other network service revenues include charges for leased lines, IP-based, packet-based and switched-based services. These services are used for domestic and international communications such as private networking, broadband and narrowband internet-based data communications, and packet-based communication.

The following table shows salient information about our data and other network service revenues for the three months ended March 31, 2006 and 2005:

	Three Months Ended March 31,			
	2006	2005	Increase	
(in millions)		(Unaudited)	Amount	%
Data and Other Network Service Revenues	Php3,068	Php2,058	Php1,010	49
Number of PLDT DSL broadband subscribers	101,195	56,960	44,235	78
Number of PLDT Vibe narrowband subscribers	420,154	330,486	89,668	27

Our data and other network services in the first quarter of 2006 posted revenues of Php3,068 million, an increase of Php1,010 million, or 49%, from Php2,058 million in the same period in 2005, primarily due to increases in leased lines, IP-based and switched-based data services, particularly Diginet, *PLDT DSL* and *PLDT Vibe* services, respectively. The revenue contribution of this service segment to our fixed line service revenues increased to 25% in the first quarter of 2006 from 17% in the same period in 2005.

Internet-based products are bannered by *PLDT DSL (myDSL and BizDSL)*, *PLDT Vibe* and I-Gate. *PLDT DSL* broadband Internet service is targeted for heavy individual internet users as well as for small and medium enterprises; while *PLDT Vibe*, or PLDT's dial-up/narrowband Internet service, is targeted for light to medium residential or individual internet users. I-Gate, our



dedicated leased line Internet access service, on the other hand, is targeted to enterprises and value-added service providers.

PLDT DSL, which contributed revenues of Php733 million during the first quarter of 2006 increased by Php239 million, or 48%, from Php494 million in the same period in 2005. *PLDT DSL* has reached 101,195 subscribers as at March 31, 2006 compared with 56,960 subscribers in the same period in 2005. PLDT offers a number of *DSL* packages with speeds and monthly fees varying from 256 kbps at Php999 per month to up to 1 Mbps at Php3,000 per month.

PLDT Vibe revenues increased by Php35 million, or 58%, to Php95 million in the first quarter of 2006 from Php60 million in the same period in 2005. As at March 31, 2006, the number of PLDT's fixed line subscribers for *PLDT Vibe* stood at 420,154, of which 154,934 were exclusive postpaid users, 234,315 were exclusive prepaid users, and 30,905 were both postpaid and prepaid users. As at March 31, 2005, *PLDT Vibe* subscribers totaled 330,486, of which 134,389 were exclusive postpaid users, 174,817 were exclusive prepaid users, and 21,280 were both postpaid and prepaid users.

The continued growth in data services revenues can be attributed to several product offerings. The steady demand for dedicated connectivity or private networking from the corporate market using PLDT's traditional bandwidth offerings – Fibernet, Arcstar, Acacia, I-Gate, Diginet, BRAINS, among others – continues to provide us with a stable revenue source. Through Diginet, we provide Smart's increasing fiber optic and leased line data requirements, which are included under our national data services. Diginet contributed Php1,406 million in our data revenues in the first quarter of 2006, increasing by Php720 million, or 105%, from Php686 million in the same period in 2005.

We introduced *PLDT WeRoam*, a wireless broadband service offering running on Smart's nationwide wireless network (using GPRS, EDGE and WiFi technologies) and PLDT's extensive IP infrastructure. *PLDT WeRoam* provides workers and remote offices, of large, medium and small businesses, with continuous wireless data connectivity, wherever the users may be, to their corporate headquarters' Intranet and/or the global Internet. Some of the recent enhancements to the service are the inclusion of international roaming in key roaming countries all over the globe and national WiFi roaming access. Principally targeted to the corporate market, the service has experienced a take-up rate of more than 7,500 contracted customers as at March 31, 2006.

In June 2005, the *PLDT Innolab* in Manila, was further expanded in partnership with the leading technology companies in the country. The PLDT Innolab is a first-of-its-kind innovation & testing center for the Philippine telecommunications industry. With the expanded Innovation Laboratory, more clients as well as people from the academe and government can now be accommodated and can experience more live industry solutions.

Also in June 2005, *F.A.S.Track*, an application-based solution that tracks the whereabouts of a company's field assets through GPS and GSM technology was introduced. *F.A.S.Track* allows near real-time and simultaneous monitoring of fleet vehicles and field personnel virtually connecting mobile company assets in the field to the main office through the use of digital maps and statistical data.

Miscellaneous

Miscellaneous service revenues are derived mostly from directory advertising and facilities rental. In the first quarter of 2006, these revenues increased by Php58 million, or 19%, to Php364

million from Php306 million in the same period in 2005. The improvement was mainly due to an increase in co-location charges from more co-location sites coupled with an increase in rent income on duct utilization and cable restoration. The percentage contribution of miscellaneous service revenues to our fixed line service revenues was 3% in the first quarter of 2006 and 2005.

Non-service Revenues

Non-service revenues of Php13 million recognized under our fixed line business represent proceeds of computer sales in the first quarter of 2006 in relation to our DSL promo.

Other Income

All other income/gains such as rental income, gain on disposal of property, which do not fall under service and non-service revenues are included under this classification. In the first quarter of 2006, our fixed line business segment registered an increase in other income of Php76 million, or 245%, to Php107 million in the first quarter of 2006 from Php31 million in the same period in 2005, primarily due to higher service and facility fees.

Expenses

Expenses related to our fixed line business in the first quarter of 2006 totaled Php11,136 million, an increase of Php2,381 million, or 27%, compared to Php8,755 million in the same period in 2005. The increase was primarily due to higher depreciation and amortization, financing costs, and compensation and benefits expenses partially offset by lower provisions and insurance and security services.

The following table shows the breakdown of our total fixed line-related expenses for the three months ended March 31, 2006 and 2005 and the percentage of each expense item to the total:

	Three Months ended March 31,					
	2006		2005		Increase (Decrease)	
	%	%	Amount	%		
	(Unaudited)					
(in millions)						
Fixed line services:						
Depreciation and amortization	Php4,971	45	Php3,001	34	Php1,970	66
Compensation and benefits ⁽¹⁾	2,216	20	1,934	22	282	15
Financing costs	1,408	13	773	9	635	82
Maintenance	808	7	810	9	(2)	-
Rent	427	4	391	5	36	9
Selling and promotions	386	3	355	4	31	9
Professional and other contracted services	214	2	213	2	1	-
Taxes and licenses	205	2	188	2	17	9
Insurance and security services	133	1	163	2	(30)	(18)
Communication, training and travel	124	1	94	1	30	32
Provisions	70	1	653	8	(583)	(89)
Cost of sales	32	-	-	-	32	100
Other expenses	142	1	180	2	(38)	(21)
Total	Php11,136	100	Php8,755	100	Php2,381	27

(1) Includes salaries and benefits, incentive plan, pension and MRP costs.

Depreciation and amortization charges increased by Php1,970 million, or 66%, to Php4,971 million mainly due to the effect of our change in estimated useful lives of certain property and equipment in line with our upgrade to the next-generation network which resulted in increased

depreciation charges of Php1,941 million for 2006, and higher depreciation of our regular asset base from additional completed projects. Please see *Note 8 – Property, Plant and Equipment* to the accompanying unaudited consolidated financial statements for further discussion.

Compensation and benefits expenses increased by Php282 million, or 15%, to Php2,216 million primarily due to the effect of the collective bargaining agreement-related increases in salaries and benefits and an increase in incentive plan-related accruals, partially offset by a reduction in headcount due to PLDT's MRP.

Financing costs increased by Php635 million, or 82%, to Php1,408 million due to: (1) lower foreign exchange gains recorded in the first quarter of 2006 compared to the same period in 2005; (2) loss on derivatives recorded in the first quarter of 2006 compared to a gain in the same period in 2005; and (3) lower interest on loans and related items owing to lower debt balances in the first quarter of 2006 compared to the same period in 2005. The breakdown of financing costs for our fixed line business for the three months ended March 31, 2006 and 2005 is as follows:

	Three Months ended March 31,			
	2006	2005	Change	
			Amount	%
		(Unaudited)		
(in millions)				
Interest on loans and related items	Php1,718	Php2,470	(Php752)	(30)
Hedge costs	341	241	100	41
Accretion on financial liabilities – net	69	89	(20)	(22)
Loss (gain) on derivative transactions – net	21	(217)	238	110
Financing charges	11	(19)	30	158
Capitalized interest	(68)	(94)	26	(28)
Interest income	(108)	(73)	(35)	48
Foreign exchange gains – net	(576)	(1,624)	1,048	(65)
	<u>Php1,408</u>	<u>Php773</u>	<u>Php635</u>	<u>82</u>

Maintenance expenses decreased by Php2 million to Php808 million primarily due to lower maintenance costs for foreign cable and wire facilities as more operating and maintenance-related restorations were incurred in the first quarter of 2006 as compared to the same period in 2005.

Rent expenses increased by Php36 million, or 9%, to Php427 million due to an increase in international leased circuits and rental charges occupied by various equipments, partially offset by lower rentals for bundled sales/value added service units.

Selling and promotion expenses increased by Php31 million, or 9%, to Php386 million, primarily as a result of an increase in PLDT's promotional activities in relation to various products and services, partially offset by lower commissions paid in the first quarter of 2006.

Professional and other contracted services increased by Php1 million to Php214 million primarily due to an increase in facility management fees and collection agency fees, partially offset by lower advisory and legal fees in the first quarter of 2006 for various services.

Taxes and licenses increased by Php17 million, or 9%, to Php205 million mainly on account of higher NTC supervision and license fees, fringe benefit taxes in respect of our stock option plan and other business-related taxes paid in the first quarter of 2006 as compared to the same period in 2005.

Insurance and security services decreased by Php30 million, or 18%, to Php133 million, primarily due to lower premiums on property all-risk, industrial all-risk and industrial fire insurance, partially offset by higher security services due to a rate increase for contracted security guards.

Communication, training and travel expenses increased by Php30 million, or 32%, to Php124 million due to an increase in mailing, courier and delivery services, as well as an increase in local travel and training in the first quarter of 2006 as compared to the same period in 2005.

Provisions decreased by Php583 million, or 89%, to Php70 million, primarily on account of a lower provision by PLDT for anticipated uncollectible accounts from various specifically identified domestic telecommunications carriers which were provided for in 2004 complemented by a decrease in our write-down of inventories to net realizable value. The breakdown of provisions for our fixed line business for the three months ended March 31, 2006 and 2005 is as follows:

	Three Months Ended March 31,			
	2006	2005	Change	
(in millions)			Amount	%
			(Unaudited)	
Doubtful accounts	Php155	Php703	(Php548)	(78)
Onerous contracts and assessments	(85)	(50)	(35)	70
	<u>Php70</u>	<u>Php653</u>	<u>(Php583)</u>	<u>(89)</u>

Cost of sales of computers amounting to Php32 million were recognized in the first quarter of 2006 in relation to our DSL promo. No similar charges were incurred in the same period in 2005.

Other expenses decreased by Php38 million, or 21%, to Php142 million due to lower office supplies consumption and printing costs resulting from PLDT's continuing cost-containing activities.

Provision for Income Tax

Provision for income tax amounted to Php291 million in the first quarter of 2006 compared to Php830 million in the same period in 2005, a decrease of Php539 million, or 65%, primarily due to lower income subject to tax.

Net Income

In the first quarter of 2006, our fixed line business segment contributed a net income of Php842 million, a decrease of Php1,430 million, or 63%, as compared to Php2,272 million in the same period in 2005 mainly as a result of a 27% increase in fixed line-related expenses, particularly depreciation and amortization which more than offset the 3% increase in fixed line-related revenues.

Information and Communications Technology

Revenues and Other Income

Our information and communications technology business is conducted by ePLDT and its subsidiaries.

In the first quarter of 2006, our information and communications technology business generated revenues of Php872 million, an increase of Php121 million, or 16%, from Php751 million in the same period in 2005. Going forward, we expect revenues from our call center business to continue to contribute significantly to our information and communications technology revenues with the growing demand for our call center services.

The following table summarizes revenues from our information and communications technology business for the three months ended March 31, 2006 and 2005 by service segment:

	Three Months Ended March 31,					
	2006		2005		Increase (Decrease)	
	Amount	%	Amount	%	Amount	%
	(Unaudited)					
(in millions)						
Service Revenues						
Call center	Php563	65	Php408	54	Php155	38
Internet and gaming	142	16	146	20	(4)	(3)
Vitro™ data center	83	10	81	11	2	2
Others	25	3	17	2	8	47
	<u>813</u>	<u>94</u>	<u>652</u>	<u>87</u>	<u>161</u>	<u>25</u>
Non-service Revenues						
Point-of-Product Sales	53	6	66	9	(13)	(20)
Other Income	4	–	31	4	(27)	(87)
Equity share in net income of associates	<u>2</u>	<u>–</u>	<u>2</u>	<u>–</u>	<u>–</u>	<u>–</u>
Total ICT Revenues and Other Income	<u>Php872</u>	<u>100</u>	<u>Php751</u>	<u>100</u>	<u>Php121</u>	<u>16</u>

Service Revenues

Service revenues generated by our information and communications technology segment amounted to Php813 million in the first quarter of 2006, an increase of Php161 million, or 25%, as compared to Php652 million in the same period in 2005 primarily as a result of the continued growth of our call center business.

Call Center

We are focused on developing our call center business which capitalizes on the availability of English-speaking college graduates in the Philippines with a strong customer service orientation. ePLDT now uses one umbrella brand name, *ePLDT Ventus*, for all of its call center businesses, including Vocativ and Parlance. Vocativ provides customer and technical support to its clients in the Philippines, U.S. and U.K. while Parlance provides the exclusive customer support and billing requirements to one of the largest direct-to-home satellite television providers in the U.S. In aggregate, we own and operate 3,690 seats with 3,842 customer service representatives, or CSRs, as of March 31, 2006 compared to 2,174 seats with 2,378 CSRs as of March 31, 2005. In 2005, ePLDT had four call centers in Metro Manila and one in Iloilo; two more will open in 2006.

Call center revenues consist of:

- inbound calls for customer care, product inquiries, sales and technical support based on active minutes, billable hours and full-time equivalents;

- outbound calls for sales and collections based on active minutes, billable hours and full-time equivalents; and
- service income for e-mail handling, web chat, web co-browsing, data entry and business process outsourcing based on transaction volume.

Revenues related to our call center business in the first quarter of 2006 increased by Php155 million, or 38%, to Php563 million from Php408 million in the same period in 2005, primarily due to the combined effects of the following:

- Vocativ's upward price adjustment for calls and an increase in programs being handled;
- an upward price adjustment by Parlance for its inbound and outbound projects, coupled with an increase in the number of registered minutes for inbound projects and hours for outbound projects;
- expansion of existing Parlance and Vocativ facilities by 906 and 211 seats, respectively, from 1,234 and 999 in the first quarter of 2005 to 1,400 and 1,210 in the same period in 2006;
- commencement of Ventus operations in Iloilo in March 2005; and
- continuous ramp up of CSRs by 1,464, or 62%, from a total of 2,378 in the first quarter of 2005 to 3,842 in the same period in 2006.

Call center revenues accounted for 69% and 63% of total information and communications technology service revenues in the first quarter of 2006 and 2005, respectively.

Internet and gaming

ePLDT has also invested in a number of other e-commerce and internet-related businesses, which include:

- a 99.6% interest in Infocom, one of the country's leading internet service providers. Infocom offers consumer prepaid and postpaid internet access, corporate leased lines, dedicated dial-up, multi-user dial-up, broadband internet access through DSL, web consulting and development, hosting and other value-added services;
- a 75% interest in Digital Paradise, an internet café business which assumed the assets of Netopia Computer Technologies, Inc., and the brand *Netopia*. *Netopia* is now one of the largest and fastest growing internet café chains in the country with 186 branches and over 8,500 work stations. Digital Paradise offers high-speed internet services, including internet advertising, gaming and printing;
- a 60% interest in netGames, a publisher for Massively Multi-player Online Game in the Philippines. netGames is the Philippine licensee of Khan Online, Pangya and Flyff, and the owner of Juanworld, a community gaming portal. netGames commenced full commercial operations in February 2005;
- a 60% interest in Level Up!, a leading publisher of online games in the Philippines with about 80% of the online gaming market;

- 51% interest in Airborne Access, the country's leading operator of WiFi hotspots, which provides wireless internet access in hotspots equipped with Airborne Access WiFi access points; and
- a 51% interest in Digital Paradise Thailand, an affiliate of Digital Paradise, offering similar products and services. Digital Paradise Thailand currently has four branches in addition to its head office all situated in Bangkok, Thailand.

Internet Service revenues consist of:

- revenues derived from actual usage of the internet access network by prepaid subscribers and any unused peso value of expired prepaid cards or electronic internet time loads, net of discounts given to dealers;
- monthly service fees from postpaid corporate and consumer subscribers, including (1) charges for internet usage in excess of allocated free plan internet hours; (2) one-time installation and activation fees; and (3) fees for value added services such as additional mailbox accounts;
- monthly service fees on value added services, including e-mail and web hosting services;
- one-time fees generated from resellership of internet-related solutions such as security solutions and domain registration;
- sales revenues from retailing of prepaid cards for cellular, landline and internet access;
- franchise fees for *Netopia* Internet cafés, including a one-time subscription fee and monthly recurring franchise fees based on certain conditions on the franchise agreement; and
- share in revenues of text, voice and internet messages for cellular, landline and internet-based content and applications.

Revenues from our internet business in the first quarter of 2006 decreased by Php4 million, or 3%, to Php142 million from Php146 million in the same period in 2005, primarily due to a decrease in Infocom's revenues in 2005, which was partially offset by the consolidation of Digital Paradise in June 2004. Our internet business revenues accounted for 17% and 22% of service revenues from information and communications technology business in the first quarter of 2006 and 2005, respectively.

*Vitro*TM data center

ePLDT operates an internet data center under the brand name *Vitro*TM. Granted pioneer status as an internet data center by the Board of Investments, *Vitro*TM provides co-location services, 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 security services such as firewall and managed firewall.

*Vitro*TM revenues consist of:

- monthly service fees derived from co-location services, server hosting, hardware and software maintenance services, website development and maintenance services, web hosting, data recovery security services and other value added services;
- installation charges and other one-time fees associated with the set-up of services; and
- monthly service fees or one-time fees generated from professional services of *Vitro*'s certified professionals.

In the first quarter of 2006, *Vitro*TM contributed revenues of Php83 million, an increase of Php2 million, or 2%, from Php81 million in the same period in 2005, primarily due to an increase in co-location revenues, server hosting and other services. *Vitro*TM revenues accounted for 10% and 12% of service revenues from our information and communications technology business in the first quarter of 2006 and 2005, respectively.

Others

Other revenues consist of:

- fees generated for issuance of digital certificates; and
- revenues derived from IT helpdesk/contact center solutions and terminals for credit, debit and credit card transactions.

Revenues from other businesses related to our information and communications technology segment in the first quarter of 2006 increased to Php25 million from Php17 million in the same period in 2005 largely due to IT helpdesk/contact center services rendered coupled with an increase in the number of digital certificates sold.

Please refer to *Note 9 – Investments in Associates* to the accompanying unaudited consolidated financial statements for further discussion on ePLDT's other information and communications technology services.

Non-service Revenues

Non-service revenues consist of sales generated from reselling certain Microsoft licenses, server solutions, networking products, storage products and data security products. In the first quarter of 2006, non-service revenues generated by our information and communications technology business decreased by Php13 million, or 20%, to Php53 million compared to Php66 million in the same period in 2005, primarily due to lower revenues from sales of networking equipment and Microsoft licenses.

Other Income

All other income/gains which do not fall under service and non-service revenues are included under this classification. Other income generated from our information and communications technology business segment decreased to Php4 million in the first quarter of 2006 from Php31 million in the same period in 2005 primarily due to Infocom's sale of its *NOW* cable internet business the first quarter of 2005; no similar transaction was incurred in the same period in 2006.

Equity Share in Net Income of Associates

Equity share in net income of associates amounted to Php2 million in the first quarter of 2006 and 2005, due to share in the earnings of ePDS, an unconsolidated subsidiary.

Expenses

Expenses associated with our information and communications technology business totaled Php858 million in the first quarter of 2006, an increase of Php137 million, or 19%, from Php721 million in the same period in 2005, primarily due to an increase in compensation and benefits, depreciation and amortization and selling and promotions. As a percentage of our information and communications technology revenues, expenses related to our information and communications technology business were at 98% and 96% for the first quarter of 2006 and 2005, respectively.

The following table shows the breakdown of our total information and communications technology-related expenses for the three months ended March 31, 2006 and 2005 and the percentage of each expense item to the total:

	Three Months Ended March 31,					
	2006		2005		Increase (Decrease)	
	Amount	%	Amount	%	Amount	%
	(Unaudited)					
(in millions)						
Information and communications technology services:						
Compensation and benefits ⁽¹⁾	Php386	45	Php308	43	Php78	25
Depreciation and amortization	120	14	95	13	25	26
Rent	99	12	99	14	—	—
Selling and promotions	81	9	64	9	17	27
Maintenance	58	7	70	10	(12)	(17)
Communication, training and travel	30	3	16	2	14	88
Professional and other contracted services	23	3	20	3	3	15
Financing costs	13	1	13	2	—	—
Taxes and licenses	8	1	10	1	(2)	(20)
Insurance and security services	5	1	3	—	2	67
Provisions	1	—	—	—	1	100
Other expenses	34	4	23	3	11	48
Total	Php858	100	Php721	100	Php137	19

(1) Includes salaries and benefits, incentive plan, pension and MRP costs.

Compensation and benefits increased by Php78 million, or 25%, to Php386 million, mainly due to the expansion of our call center and Internet and gaming businesses, which resulted in an increase in headcount coupled with an increase in salaries, bonuses and various incentives of employees.

Depreciation and amortization charges increased by Php25 million, or 26%, to Php120 million, primarily due to an increase in the depreciable asset base in relation to the expansion of our call center and internet and gaming businesses.

Selling and promotion expenses increased by Php17 million, or 27%, to Php81 million mainly due to an increase in advertising and marketing spending by our Internet and gaming businesses in the first quarter of 2006 as compared to the same period in 2005.

Maintenance expenses decreased by Php12 million, or 17%, to Php58 million primarily due to Vitro's lower hardware maintenance costs related to its IBM and CISCO equipments partially offset by higher hosting-related costs incurred in the first quarter of 2006 as compared to the same period in 2005.

Communication, training and travel expenses increased by Php14 million, or 88%, to Php30 million due to the increased cost of bandwidth and information system charges, coupled by the increase in telecommunications costs incurred by our call center business for its outbound calls.

Professional and other contracted services increased by Php3 million, or 15%, to Php23 million, primarily due to an increase in consultancy, legal and audit fees in the first quarter of 2006 as compared to the same period in 2005.

Financing costs amounted to Php13 million in the first quarter of 2006 and 2005, primarily due to higher foreign exchange losses from dollar-denominated receivables, partially offset by lower interest on loans as debt balances decreased in the first quarter of 2006 as compared to the same period in 2005.

Taxes and licenses decreased by Php2 million, or 20%, to Php8 million due to lower business-related taxes paid in the first quarter of 2006 as compared to the same period in 2005.

Insurance and security services increased by Php2 million, or 67%, to Php5 million primarily due to higher premium costs and an increase in the assets insured in the first quarter of 2006 as compared to the same period in 2005.

Provisions increased by Php1 million in the first quarter of 2006 due to the non-collectibility status of certain accounts; no similar provisions were recorded in 2005.

Other expenses increased by Php11 million, or 48%, to Php34 million mainly due to higher royalty fees on licenses by our Internet and gaming businesses, and increase in other business-related costs.

Provision for (Benefit from) Income Tax

Benefit from income tax amounted to Php15 million in the first quarter of 2006 primarily due to the recognition of deferred tax assets pertaining to accrued pension costs, net operating loss carry-over and allowance for doubtful accounts as compared to the same period in 2005.

Net Income (Loss)

In the first quarter of 2006, our information and communications technology business segment registered a net income of Php29 million, a decrease of Php1 million compared to Php30 million in the same period in 2005 mainly as a result of a 19% increase in ICT-related expenses, particularly compensation and benefits partially offset by a 16% increase in ICT-related revenues.

Liquidity and Capital Resources

The following table shows our consolidated cash flows for the three months ended March 31, 2006 and 2005 as well as consolidated capitalization and other selected financial data as at March 31, 2006 and December 31, 2005:

	Three Months Ended March 31,	
	2006	2005
	(Unaudited)	
(in millions)		
Cash Flows		
Net cash provided by operating activities	Php15,429	Php15,464
Net cash used in investing activities	5,825	2,191
Capital expenditures	4,869	4,263
Net cash used in financing activities	3,997	10,459
Net increase in cash and cash equivalents	5,138	2,456
	March 31,	December 31,
	2006	2005
	(Unaudited)	(Audited)
(in millions)		
Capitalization		
Long-term portion of interest-bearing financial liabilities – net of current portion:		
Long-term debt	Php75,281	Php84,860
Obligations under capital lease	330	381
Preferred stock subject to mandatory redemption	11,030	11,974
	<u>86,641</u>	<u>97,215</u>
Current portion of interest-bearing financial liabilities:		
Long-term debt maturing within one year	23,706	18,684
Obligations under capital lease maturing within one year	762	717
	<u>24,468</u>	<u>19,401</u>
Total interest-bearing financial liabilities	111,109	116,616
Total equity	<u>76,752</u>	<u>74,369</u>
	<u>187,861</u>	<u>Php190,985</u>
Other Financial Data		
Total assets	Php251,110	Php249,713
Property, plant and equipment – net	173,571	176,974
Cash and cash equivalents	35,202	30,064

As at March 31, 2006, our consolidated cash and cash equivalents totaled Php35,202 million. Principal sources of consolidated cash and cash equivalents in the first quarter of 2006 were cash flows from operating activities amounting to Php15,429 million and drawings from Smart's debt facilities aggregating Php3,446 million. These funds were used principally for capital outlays of Php4,869 million, total debt principal payments of Php4,804 million and interest payments of Php1,422 million.

Operating Activities

Our consolidated net cash flows from operating activities in the first quarter of 2006 decreased by Php35 million to Php15,429 million, from Php15,464 million in the same period in 2005.

A significant portion of our cash flow is generated by our wireless business, which accounted for 59% of our service revenues in the first quarter of 2006 and 2005. Revenues from our fixed line and information and communications technology services accounted for 38% and 3%, respectively, of our service revenues in the first quarter of 2006 compared to 39% and 2%, respectively, in the same period in 2005.

Cash flows from operating activities of our wireless business amounted to Php7,730 million in the first quarter of 2006, a decrease of Php2,288 million, or 23%, compared to Php10,018 million in the same period in 2005. Our fixed line business contributed Php7,383 million in the first quarter of 2006, a decrease of Php2,236 million, or 43%, compared to Php5,147 million in the same period in 2005. The overall decrease in our cash flows from operating activities was due to an increase in working capital requirements with the settlement of various current liabilities. Our wireless business segment accounted for 50% of our cash flows from operating activities while our fixed line segment accounted for 48% in the first quarter of 2006. We currently believe that our continuing strong cash flows from operating activities on a consolidated basis will allow us to defray our current liabilities despite our current ratio being less than 1:1 as at March 31, 2006.

While Smart is subject to loan covenants that restrict its ability to pay dividends, redeem preferred shares, make distributions to PLDT or otherwise provide funds to PLDT or any associate without the consent of its lenders, Smart has been able to obtain waivers from Finnvera and certain of its lenders for each of the dividend payments made by Smart to PLDT in 2005, 2004, 2003 and 2002 aggregating Php19,717 million, Php16,100 million, Php6,166 million and Php1,540 million, respectively. In September and December 2005, Smart redeemed 200 million and 180.8 million preferred shares, respectively, previously issued to PLDT at a redemption price of Php13.875 per share, or a total redemption price aggregating to Php5,283 million.

Investing Activities

Net cash used in investing activities in the first quarter of 2006 amounted to Php5,825 million, an increase of Php3,634 million, or 166%, compared to Php2,191 million in the same period in 2005. This was a result of an increase in payments for purchase of investments by Php963 million primarily due to the final settlement in relation to Meridian's acquisition, increase in capital expenditures by Php606 million and an increase in short-term investments in the first quarter of 2005 compared to a decrease in the same period in 2006.

Our consolidated capital expenditures in the first quarter of 2006 totaled Php4,869 million, an increase of Php606 million, or 14%, from Php4,263 million in the same period in 2005, primarily due to Smart's and ePLDT's higher capital spending. Smart's capital spending of Php2,530 million in the first quarter of 2006 was used to roll-out its 3G network and further expand and upgrade its transmission network facilities to increase capacity and coverage in respect of basic and advanced cellular services. PLDT's capital spending of Php1,955 million was principally used to finance the expansion of its fixed line data and IP-based network services. ePLDT and its subsidiaries' capital spending of Php331 million was primarily used to fund its *Vitro*TM, Digital Paradise and call center business operations. The balance represented other subsidiaries' capital spending. Consolidated capital expenditures in the same period in 2005 amounted to Php4,263 million, of which Php1,753 million, Php2,344 million and Php158 million were attributable to Smart, PLDT and ePLDT, respectively. The balance represented other subsidiaries' capital spending.

Financing Activities

On a consolidated basis, we used net cash of Php3,997 million for financing activities, net of loan drawings by Smart, in the first quarter of 2006, compared to Php10,459 million in the same period in 2005. The net cash used in financing activities in the first quarter of 2006 was mainly attributable to debt repayments and interest payments by PLDT in line with its ongoing debt reduction program and dividend payments distributed to preferred stockholders.

Debt Financing

Additions to our consolidated long-term debt in the first quarter of 2006 totaled Php3,446 million mainly from Smart's drawings related to the financing of its Phase 8 loan facilities. Payments in respect of principal and interest of our total debt amounted to Php4,804 million and Php1,422 million, respectively, in the first quarter of 2006, of which Php3,446 million and Php1,224 million were attributable to PLDT, respectively.

The following table shows our long-term debt, including current portion as at March 31, 2006 and December 31, 2005:

	March 31,	December 31,	Increase (Decrease)	
	2006	2005	Amount	%
	(Unaudited)	(Audited)		
(in millions)				
U.S. Dollar Debt:				
Export Credit Agencies-Supported Loans	Php20,649	Php23,126	(Php2,477)	(11)
Fixed Rate Notes	48,952	52,354	(3,402)	(6)
Term Loans	16,934	14,288	2,646	19
Restructured Loans	4,654	4,767	(113)	(2)
Satellite Acquisition Loans	2,665	3,040	(375)	(12)
	<u>93,854</u>	<u>97,575</u>	<u>(3,721)</u>	<u>(4)</u>
Japanese Yen Debt:				
JBIC's Overseas Investment Loan	2,424	3,139	(715)	(23)
Export Credit Agency-Supported Loan	684	709	(25)	(4)
	<u>3,108</u>	<u>3,848</u>	<u>(740)</u>	<u>(19)</u>
Philippine Peso Debt:				
Peso Fixed Rate Corporate Notes	1,577	1,576	1	-
Term Loans	65	166	(101)	(61)
Restructured Loans	383	379	4	1
	<u>2,025</u>	<u>2,121</u>	<u>(96)</u>	<u>(5)</u>
	<u>Php98,987</u>	<u>Php103,544</u>	<u>(Php4,557)</u>	<u>(4)</u>

For a complete discussion of long-term debt, see *Note 17 – Interest-bearing Financial Liabilities* to the accompanying unaudited consolidated financial statements.

Our long-term debt decreased by Php4,557 million, or 4%, to Php98,987 million as at March 31, 2006 largely due to debt amortizations and prepayments in line with PLDT's efforts to reduce its overall debt level and also due to the appreciation of the peso. PLDT's debt was reduced by 8% to Php67,470 million by March 31, 2006. In addition, the debt levels of Mabuhay and ePLDT as at March 31, 2006 decreased by 12% and 61%, to Php2,665 million and Php65 million, respectively, due to the peso appreciation and debt amortizations during 2005. Conversely, the debt level of Smart increased by 7%, to Php28,788 million as at March 31, 2006 due to additional drawings.

As at March 31, 2006, PLDT had no undrawn committed long-term credit facilities. On August 8, 2005, Smart signed a US\$30 million commercial facility with Nordic Investment Bank to partly finance the related Phase 8 GSM equipment and services contracts. The facility is expected to be drawn in the third quarter of 2006. On August 10, 2005, Smart signed a US\$70 million loan facility with Finnish Export Credit Ltd. for its GSM Phase 8 financing. Smart opted to utilize only a total of US\$66.79 million which was drawn in February 15, 2006 and March 13, 2006 for US\$10.02 million and US\$56.77 million, respectively. The balance of US\$3.2 million was canceled. The first repayment of the facility was made in March 1, 2006. Smart also had available facilities under its €50 million Framework Agreement with Bayerische Hypo-und Vereinsbank Aktiengesellschaft up to a maximum aggregate amount of €44 million. Please see *Note 17 – Interest-bearing Financial Liabilities* to the accompanying unaudited consolidated financial statements for a detailed discussion of our long-term debt.

The scheduled maturities of our outstanding unaudited consolidated long-term debt at nominal values as at March 31, 2006 are as follows:

Year	US\$ Loans ⁽¹⁾		JP¥ Loans ⁽²⁾ (in millions)		Peso Loans	Total
2006 ⁽³⁾	US\$268	Php13,695	JP¥2,024	Php880	Php829	Php15,404
2007	334	17,113	3,418	1,486	36	18,635
2008	124	6,378	1,709	743	24	7,145
2009	281	14,374	–	–	24	14,398
2010	63	3,208	–	–	834	4,042
2011 and onwards	924	47,253	–	–	380	47,633
	<u>US\$1,994</u>	<u>Php102,021</u>	<u>JP¥7,151</u>	<u>Php3,109</u>	<u>Php2,127</u>	<u>Php107,257</u>

(1) The exchange rate used was Php51.158 to US\$1.00.

(2) The exchange rate used was Php0.4347 to JP¥1.00.

(3) April 1, 2006 to December 31, 2006.

Approximately Php59,624 million principal amount of our consolidated outstanding long-term debt as at March 31, 2006 is scheduled to mature over the period from 2006 to 2010. Of this amount, Php39,969 million was attributable to PLDT, Php16,925 million to Smart, and the remainder to Mabuhay Satellite, Maratel and ePLDT.

Debt Covenants

Our debt instruments contain restrictive covenants, including covenants that could prohibit us from paying common dividends under certain circumstances, and require us to comply with specified financial ratios and other financial tests, calculated in conformity with accounting principles generally accepted in the Philippines, at relevant measurement dates, principally at the end of each quarterly period. We have complied with all of our maintenance financial ratios as required under our loan covenants and other debt instruments.

Please see *Note 17 – Interest-bearing Financial Liabilities* to the accompanying unaudited consolidated financial statements for a detailed discussion of our covenants.

Financing Requirements

We believe that our available cash, including cash flow from operations, will provide sufficient liquidity to fund our projected operating, investment, capital expenditures and debt service requirements for the next 12 months.

Since 2002, we have been utilizing internally generated cash, particularly from our cellular business, to reduce our overall level of indebtedness. In line with this objective, we have managed our capital expenditures, reduced our investments and suspended dividend payments to common shareholders from April 2001. As a result of our improving cash flows and reduced debt levels, we restored the payment of dividends in May 2005 and currently intend to gradually increase our dividend payout ratio in succeeding years as we improve our leverage ratios.

Credit Ratings

None of our existing indebtedness contains provisions under which credit rating downgrades would trigger a default, changes in applicable interest rates or other similar terms and conditions.

PLDT's current credit ratings are as follows:

<u>Rating Agency</u>	<u>Credit Rating</u>	<u>Outlook</u>
Standard and Poor's	Foreign Currency Senior Unsecured Debt Rating	BB+ Stable
Moody's Investor Service	Foreign Currency Senior Unsecured Debt Rating	Ba2 Negative
	Local Currency Corporate Family Rating	Ba1 Positive
Fitch	Long-term Foreign Currency Rating	BB Stable
	Long-term Local Currency Rating	BB+ Stable

On March 29, 2006, Moody's Investor Service, or Moody's, placed the Ba1 local currency corporate family rating of PLDT on review for possible upgrade. At the same time, Moody's affirmed PLDT's Ba2 foreign currency senior unsecured ratings, with a negative outlook.

On February 20, 2006, Fitch Ratings has revised its outlook on PLDT's long-term foreign currency from negative to stable. PLDT's long-term foreign currency, global bonds and senior notes has been affirmed at "BB" and convertible preferred stock at "B+." The revision in outlook reflects that of the outlook of the Republic of the Philippines as foreign currency and senior debt instrument ratings are constrained by the sovereign foreign currency rating. At the same time, PLDT's long-term local currency rating has been affirmed at "BB+" with a stable outlook.

Equity Financing

PLDT raised Php21 million and Php83 million from the exercise by certain officers and executives of stock options in the first quarter of 2006 and 2005, respectively. In addition, through our subscriber investment plan, or SIP, which provides postpaid fixed line subscribers the opportunity to buy shares of our 10% cumulative convertible preferred stock as part of the upfront payments collected from subscribers, PLDT was able to raise Php81 million in 2006.

Cash dividend payments to preferred shareholders in the first quarter of 2006 amounted to Php222 million compared to Php320 million in the same period in 2005. On March 1, 2005, PLDT declared cash dividends of Php14 per common share to holders of record as at March 31, 2005 paid on May 12, 2005. This was the first cash dividend declaration to common shareholders in four years since April 2001. In addition, on each of May 5, 2005 and November 8, 2005, PLDT declared cash dividends of Php21 per common share to holders of record as at June 3, 2005 and November 28, 2005 paid on July 14, 2005 and December 28, 2005, respectively. On February 27,



2006, PLDT declared cash dividends of Php28 per common share to holders of record as at March 20, 2006 paid on April 20, 2006.

As at March 31, 2006, there were 181,431,099 PLDT common shares outstanding.

Contractual Obligations and Commercial Commitments

Contractual Obligations

The following table discloses our consolidated contractual obligations outstanding as at March 31, 2006:

	Payments Due by Period				
	Total	Within 1 year	2-3 years	4-5 years	After 5 years
	(Unaudited)				
(in millions)					
Long-term debt ⁽¹⁾	Php107,257	Php23,816	Php18,370	Php17,438	Php47,633
Long-term lease obligations:					
Operating lease	3,560	614	1,082	855	1,009
Capital lease	1,677	938	288	15	436
Unconditional purchase obligations ⁽²⁾	10,682	4,799	2,046	2,046	1,791
Other long-term obligations	14,231	-	7,431	6,800	-
Total contractual obligations	Php137,407	Php30,167	Php29,217	Php27,154	Php50,869

(1) Before deducting unamortized debt discount and debt issuance costs.

(2) Based on the original Air Time Purchase Agreement with ALL.

Long-term Debt

For a discussion of our long-term debt, see *Note 17 – Interest-bearing Financial Liabilities* to the accompanying unaudited consolidated financial statements.

Long-term Operating Lease Obligations

Digital Passage Service Contracts. PLDT has existing Digital Passage Service Contracts with foreign telecommunication administrations for several dedicated circuits to various destinations for ten to 25 years expiring at various dates. As at March 31, 2006, PLDT's aggregate remaining obligation under these contracts amounted to approximately Php14 million.

License Agreement with Mobius Management Systems (Australia) Pty Ltd., or Mobius. PLDT entered into a license agreement with Mobius pursuant to which Mobius has granted PLDT a non-exclusive, non-assignable and non-transferable license for the use of computer software components. Under this agreement, Mobius is also required to provide maintenance services for a period of one year at no additional maintenance charge. PLDT may purchase maintenance services upon expiration of the first year for a fee of 15% of the current published license fee. As at March 31, 2006, PLDT's aggregate remaining obligation under this agreement was approximately Php25 million.

Other Long-term Operating Lease Obligations. The PLDT Group has various long-term lease contracts for periods ranging from two to ten years covering certain offices, warehouses, cell sites, telecommunication equipment locations and various office equipment. In particular, Smart has lease obligations aggregating Php3,242 million as at March 31, 2006 in respect of office and cell site rentals with over 3,000 lessors nationwide, PLDT has lease obligations aggregating Php105 million as at March 31, 2006, and ePLDT has lease obligations aggregating Php174 million as at

March 31, 2006 in respect of certain office space rentals.

Long-term Capital Lease Obligations

For a discussion of our long-term capital lease obligations, see *Note 17 – Interest-bearing Financial Liabilities* to the accompanying unaudited consolidated financial statements.

Unconditional Purchase Obligations

Air Time Purchase Agreement with AIL. PLDT is a party to a Founder NSP, or National Service Provider, Air Time Purchase Agreement entered into with ACeS International Limited, or AIL, in March 1997, which was amended in December 1998, under which PLDT was granted the exclusive right to sell AIL services in the Philippines. In exchange, the Air Time Purchase Agreement required PLDT to purchase from AIL a minimum of US\$5 million worth of air time annually over ten years commencing on January 1, 2002, the purported date of the start of commercial operations of the Garuda I Satellite.

In the event that AIL's aggregate billing revenue is less than US\$45 million in any given year, the Air Time Purchase Agreement also states that PLDT has to make supplemental air time purchase payments not to exceed US\$15 million per year during the ten-year term.

PLDT and the other founder NSPs are endeavoring to amend the Air Time Purchase Agreement due to the occurrence of partial satellite loss, changes in the primary business of ACeS and other events affecting the business.

In March 2003, PLDT, together with the other founder NSPs, entered into a Standstill Agreement with AIL suspending the application and enforcement of the minimum and supplemental air time payments under the original Air Time Purchase Agreement. The parties agreed that AIL shall provide PLDT and the other founder shareholders, with unlimited use of air time for the year 2003 in exchange for a fixed fee in the amount of US\$3.8 million for PLDT. Moreover, PLDT was also obliged to purchase from AIL 13,750 satellite phone units in 2003 at US\$395 F.O.B. per unit, subject to quarterly price adjustments. The parties to the Standstill Agreement also agreed to negotiate in good faith and use their best efforts to reach an agreement on a revised Air Time Purchase Agreement before November 15, 2003 that would cover, among other things, the amended minimum and supplemental air time payment provisions subject to the approval of AIL's creditors.

On February 10, 2004, notwithstanding the ongoing negotiations, AIL advised PLDT of the termination of the Standstill Agreement and the reinstatement of the terms under the original Air Time Purchase Agreement effective January 1, 2002 following the lapse of the November 15, 2003 deadline set in the Standstill Agreement for the negotiation of a revised Air Time Purchase Agreement. Negotiations are continuing with the relevant parties towards an amicable settlement of this matter. See *Note 20 – Related Party Transactions* and *Note 23 – Provisions and Contingencies* to the accompanying unaudited consolidated financial statements for further details relating to the Air Time Purchase Agreement with AIL.

As at March 31, 2006, PLDT's aggregate remaining minimum obligation under the original Air Time Purchase Agreement was approximately Php10,682 million.

Other Long-term Obligations

Mandatory Conversion and Purchase of Shares. As discussed in *Note 17 – Interest-bearing Financial Liabilities* to the accompanying unaudited consolidated financial statements, as at March 31, 2006, PLDT had issued a total of 3 million shares of Series V Convertible Preferred Stock, 5 million shares of Series VI Convertible Preferred Stock and 4 million shares of Series VII Convertible Preferred Stock in exchange for a total of 58 million shares of Series K Class I Convertible Preferred Stock of Piltel, pursuant to the debt restructuring plan of Piltel adopted in June 2001.

Each share of Series V, VI and VII Convertible Preferred Stock is convertible at any time at the option of the holder into one PLDT common share. On the date immediately following the seventh anniversary of the issue date of the Series V and Series VI Convertible Preferred Stocks and on the eighth anniversary of the issue date of the Series VII Convertible Preferred Stock, the remaining outstanding shares under these series will be mandatorily converted to PLDT common shares. Under a put option exercisable for 30 days, holders of common shares received on mandatory conversion of the Series V, VI and VII Convertible Preferred Stocks will be able to require PLDT to purchase such PLDT common shares for Php1,700 per share, US\$36.132 per share, and JP¥4,071.89 per share, respectively.

As at March 31, 2006, 2,638,014 shares of Series V Convertible Preferred Stock and 1,351,823 shares of Series VI Convertible Preferred Stock had been converted to PLDT common shares. As at March 31, 2006, 83,426 shares of Series V, 3,943,281 shares of Series VI and 3,842,000 shares of Series VII Convertible Preferred Stocks remained outstanding. The aggregate value of the put option based on outstanding shares as at March 31, 2006 was Php14,231 million, of which Php7,431 million is puttable on June 4, 2008 and Php6,800 million on June 4, 2009, if all of the outstanding shares of Series V, VI and VII Convertible Preferred Stocks were mandatorily converted and all the underlying shares of common stock were put to PLDT. The market value of the underlying shares of common stock was Php15,147 million, based on the market price of PLDT common shares of Php1,925 per share as at March 31, 2006.

Please refer to *Note 17 – Interest-bearing Financial Liabilities* to the accompanying unaudited consolidated financial statements for further discussion.

Commercial Commitments

As at March 31, 2006, our outstanding commercial commitments, in the form of letters of credit, amounted to Php3,013 million. These commitments will expire within one year.

Quantitative and Qualitative Disclosures about Market Risks

Our operations are exposed to various risks, including liquidity risk, foreign exchange risk and interest rate risk. The importance of managing these risks has significantly increased in light of considerable change and continuing volatility in both the Philippine and international financial markets. With a view to managing these risks, we have incorporated financial risk management functions in our organization, particularly in our treasury operations and equity issues and sales of certain assets.

Liquidity Risk Management

We seek to manage our liquidity profile to be able to finance our capital expenditures and service our maturing debts. To cover our financing requirements, we intend to use internally generated funds and proceeds from debt.

As part of our liquidity risk management program, we regularly evaluate our projected and actual cash flow information and continuously assess conditions in the financial markets for opportunities to pursue fund-raising initiatives. These initiatives may include bank loans, export credit agency-guaranteed facilities, and debt capital and equity market issues.

Foreign Exchange Risk Management

As at March 31, 2006, the Philippine peso had appreciated by Php1.904, or 4%, against the U.S. dollar to Php51.158 to US\$1.00 from Php53.062 to US\$1.00 as at December 31, 2005. As at March 31, 2005, on the other hand, the peso appreciated by Php1.594, or 3%, to Php54.747 to US\$1.00 from Php56.341 to US\$1.00 as at December 31, 2004. As at March 31, 2006, the Philippine peso had appreciated by 3% against the Japanese yen to Php0.4347 to JP¥1 from Php0.4504 to JP¥1 as at December 31, 2005. On the other hand, as at March 31, 2005, the peso appreciated by 7% to Php0.5111 to JP¥1 from Php0.5495 to JP¥1 as at December 31, 2004. The revaluation of our foreign-currency denominated assets and liabilities is recognized as foreign exchange gains or losses as at balance sheet date. Since substantially all of our indebtedness is denominated in U.S. dollars and Japanese yen, the appreciation of the peso has resulted to the recognition of net foreign exchange gains. The extent of foreign exchange gains or losses is largely dependent on the amount of foreign currency debt we carry. As at March 31, 2006, consolidated foreign currency debt-denominated amounted to Php96,962 million, a reduction from Php133,214 million last March 31, 2005. As such, we recognized lower net foreign exchange gains of Php1,578 million in the first quarter of 2006 as compared to Php3,232 million recorded in the same period in 2005.

While a certain percentage of our revenues is either linked to or denominated in U.S. dollars, 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 foreign currencies, mostly in U.S. dollars.

As at March 31, 2006, approximately 98% of our total consolidated debts were denominated in foreign currencies, principally in U.S. dollars. Of our foreign currency-denominated debts, 3% are in Japanese yen on a consolidated basis and the balance in U.S. dollars. Thus, a weakening of the Philippine peso against the U.S. dollar or Japanese yen will increase both the principal amount of our unhedged foreign currency-denominated debts (representing 55% of our consolidated debts, or 40% net of our U.S. dollar cash balances as at March 31, 2006), and interest expense on our debt in peso terms. In addition, many of our financial ratios and other financial tests will be negatively affected. If, among other things, the value of the Philippine peso against the U.S. dollar substantially drops from its current level, we may be unable to maintain compliance with these ratios, which could result in acceleration of some or all of our indebtedness. For further information on our loan covenants, see “Liquidity and Capital Resources – Financing Activities – Covenants” above and *Note 17 – Interest-bearing Financial Liabilities* to the accompanying unaudited consolidated financial statements.

To manage our foreign exchange risks, stabilize cash flows, and improve investment and cash flow planning, we enter into forward foreign exchange contracts, foreign currency swap

contracts, currency option contracts and other hedging products aimed at reducing and/or managing the adverse impact of changes in foreign exchange rates on our operating results and cash flows. However, these hedges do not cover all of our exposure to foreign currency risks.

Specifically, we use forward foreign exchange contracts, foreign currency swap contracts and currency option contracts to manage the foreign currency risk associated with our foreign currency-denominated loans. In order to manage hedge costs of these contracts, we utilize structures that include credit-linkage with PLDT as the reference entity, a combination of currency option contracts, and fixed to floating coupon only swap agreements. Accounted as either cash flow hedges or transactions not designated as hedges, changes in the fair value of these instruments are recognized as cumulative translation adjustments in equity until the hedged item is recognized in earnings or directly to income for the period. As at March 31, 2006, PLDT's outstanding forward foreign exchange contracts, principal-only long-term cross-currency swap contracts and currency option contracts amounted to US\$179 million and JP¥445 million; US\$550 million; and US\$175 million, respectively. Smart has no outstanding forward foreign exchange contracts as at March 31, 2006.

For further discussions of these contracts, see *Note 24 – Financial Assets and Liabilities – Derivative Financial Instruments* to the accompanying unaudited consolidated financial statements.

Interest Rate Risk Management

On a limited basis, we enter into interest rate swap agreements in order to manage our exposure to interest rate fluctuations. As at March 31, 2006, PLDT's outstanding interest rate swap contracts amounted to US\$63 million. For further discussions of these contracts, see *Note 24 – Financial Assets and Liabilities – Derivative Financial Instruments* to the accompanying unaudited consolidated financial statements.

We make use of hedging instruments and structures solely for reducing or managing financial risks associated with our liabilities and not for trading or speculative purposes.

Impact of Inflation and Changing Prices

Inflation can be a significant factor in the Philippine economy, and we are continually seeking ways to minimize its impact. In recent periods, we do not believe inflation has had a material impact on our operations. The average inflation rate in the Philippines in the first quarter of 2006 was 7.3%, compared to 8.4% in the same period in 2005.

OTHER INFORMATION

ePLDT's Investment in Philweb

On May 5, 2006, ePLDT and Philweb Corporation, or Philweb, signed an investment agreement and subscription agreement for ePLDT to invest in and subscribe to newly issued common shares equivalent to 20% of Philweb's outstanding common stock for an aggregate amount of Php502.4 million. Philweb is primarily engaged in Internet-based gaming and will enable the PLDT Group to gain a firm hold on legitimate gaming content for the PLDT Group's cellular, fixed line and wireless broadband businesses thereby increasing the PLDT Group's usage of its various network resources.

Launch of Pwede! Card

On May 5, 2006, PLDT and Smart launched the *Pwede! Card*, a convergent product made possible by our NGN capability. *Pwede! Card* is the first reloadable PIN-based prepaid card that provides access to a range of voice and Internet services at affordable rates. *Pwede! Card* is applicable to a host of fixed line and wireless services including local, domestic and international long distance calls, text messaging, payphones and prepaid Internet.

Smart's 20% Acquisition of WolfPac

On May 8, 2006, Smart signed a share purchase agreement to acquire the remaining 20% equity interest in Wolfpac, a company engaged in the business of consumer mobile applications software development and content development. Smart acquired 80% equity interest in Wolfpac in October 2003.

Related Party Transactions

In the ordinary course of business, a number of companies related to but outside of the consolidated PLDT Group are engaged in arm's-length intercompany transactions. We believe that the terms of these transactions are comparable with those available from unrelated parties.

Transactions to which PLDT or any of its subsidiaries are a party, in which a director or key officer or owner of more than 10% of the outstanding common stock of PLDT, or any member of the immediate family of a director or key officer or owner of more than 10% of the outstanding common stock of PLDT had a direct or indirect material interest, as at March 31, 2006 and December 31, 2005 and for the three months ended March 31, 2006 and 2005 are as follows:

Agreements with NTT Communications and/or its Affiliates — agreements under which (1) NTT Communications provides advisory services for various business areas of PLDT; (2) NTT World Engineering Marine Corporation provides maintenance services to PLDT's DFON; (3) PLDT is licensed to market managed data and other services using NTT Communications' Arcstar brand; and (4) PLDT and NTT Communications agreed to cooperative arrangements for conventional international telecommunication services. Total fees under these agreements totaled Php51 million and Php81 million for the three months ended March 31, 2006 and 2005, respectively. PLDT's outstanding obligations under these agreements amounted to Php46 million and Php23 million as at March 31, 2006 and December 31, 2005, respectively.

Agreements between Smart and Asia Link B.V. — agreements under which Asia Link undertakes to provide technical support services and assistance in the operations and maintenance of Smart's cellular business. Total fees under these agreements totaled Php142 million and Php123 million for the three months ended March 31, 2006 and 2005, respectively. Outstanding obligations of Smart under the Technical Service Agreement amounted to Php62 million and Php194 million as at March 31, 2006 and December 31, 2005, respectively. Asia Link is a subsidiary of the First Pacific Group.

Agreements relating to insurance companies — Gotuaco del Rosario and Associates, or Gotuaco, acts as the broker for certain insurance companies to cover certain insurable properties of the PLDT Group. Insurance premiums are remitted to Gotuaco and the broker's fees are settled between Gotuaco and the insurance companies. In addition, PLDT has an insurance policy with Malayan Insurance Co., Inc., or Malayan, wherein premiums are directly paid to Malayan. Total insurance



expenses paid under these agreements amounted to Php105 million and Php155 for the three months ended March 31, 2006 and 2005, respectively. Two directors of PLDT have direct/indirect interests in or serve as a director/officer of Gotuaco and Malayan.

For a more detailed discussion of the related party transactions enumerated above, see *Note 20 – Related Party Transactions* to the accompanying unaudited consolidated financial statements.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PHILIPPINE LONG DISTANCE TELEPHONE COMPANY

By: /s/ Ma. Lourdes C. Rausa-Chan
MA. LOURDES C. RAUSA-CHAN
Senior Vice President, Corporate Affairs and
Legal Services Head and Corporate Secretary

Date: May 9, 2006