

SECURITIES AND EXCHANGE COMMISSION

SEC FORM 17-Q

**QUARTERLY REPORT PURSUANT TO SECTION 17 OF THE SECURITIES
REGULATION CODE AND SRC RULE 17 (2)(b) THEREUNDER**

1. For the quarterly period ended September 30, 2011.
2. SEC Identification Number 31171 3. BIR Tax Identification No. 000-168-801
4. Exact name of registrant as specified in its charter PETRON CORPORATION
5. Philippines
Province, Country or other
jurisdiction of incorporation or
organization
6. (SEC Use Only)
Industry Classification Code:
7. SMC Head Office Complex, 40 San Miguel Avenue, Mandaluyong City, 1550
Address of principal office
Postal Code
8. (0632) 886-3888
Registrant's telephone number, including area code
9. N/A
(Former name, former address, and former fiscal year, if changed since last report.)
10. Securities registered pursuant to Sections 8 and 12 of the SRC or Sections 4 and 8 of the RSA

Title of Each Class	Number of Shares of Common Stock Outstanding and Amount of Debt Outstanding
<u>Common Stock</u>	<u>9,375,104,497 Shares</u>
<u>Preferred Stock</u>	<u>100,000,000 Shares</u>
<u>Total Liabilities</u>	<u>P111,676 million</u>

11. Are any or all of these securities listed on the Philippine Stock Exchange.

Yes No

If yes, state the name of such stock exchange and the classes of securities listed therein:

Philippine Stock Exchange

Common and Preferred Stocks

12. Indicate by check mark whether the Registrant:

(a) has filed all reports required to be filed by Section 17 of the Code and SRC Rule 17 thereunder or Sections 11 of the RSA and RSA Rule 11 (a)-1 thereunder, and Sections 26 and 141 of the Corporation Code of the Philippines, during the preceding 12 months (or for such shorter period the registrant was required to file such reports).

Yes No

(b) has been subject to such filing requirements for the past 90 days.

Yes No

TABLE OF CONTENTS

Page No.

PART I - FINANCIAL INFORMATION		
Item 1	Financial Statements	
	Petron Corporation & Subsidiaries Consolidated Statements of Financial Position	5
	Petron Corporation & Subsidiaries Consolidated Statements of Income	6
	Petron Corporation & Subsidiaries Consolidated Statements of Comprehensive Income	7
	Petron Corporation & Subsidiaries Consolidated Statements of Changes in Equity	8
	Petron Corporation & Subsidiaries Consolidated Statements of Cash Flows	9
	Selected Notes to Consolidated Financial Statements	10-53
	Details of Accounts Receivables	54
Item 2	Management's Discussion and Analysis of Financial Conditions and Results of Operations	55-63
PART II - OTHER INFORMATION		
SIGNATURES		64




PETRON CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
SEPTEMBER 30, 2011 and DECEMBER 31, 2010
(Amounts in Million Pesos)

	<i>Note</i>	September 30, 2011 Unaudited	December 31, 2010 Audited
ASSETS			
Current Assets			
Cash and cash equivalents		20,399	43,984
Financial assets at fair value through profit or loss	11,12	323	227
Available-for-sale financial assets	11,12	-	178
Trade and other receivables - net	11,12	26,003	24,266
Inventories		47,088	28,145
Other current assets		7,085	4,286
		100,898	101,086
Assets held for sale	5	10	823
Total Current Assets		100,908	101,909
Non-Current Assets			
Property, plant and equipment - net	4	42,978	34,957
Investment in associates	9	1,325	804
Investment properties		817	119
Available-for-sale financial assets	11,12	1,034	983
Deferred tax assets	2	170	28
Other noncurrent assets	11,12	23,729	23,016
Total Noncurrent Assets		70,053	59,907
Total Assets	P	170,961	161,816
LIABILITIES AND EQUITY			
Current Liabilities			
Short-term loans	11,12	35,502	32,457
Liabilities for crude oil and petroleum product importation	11,12	21,872	11,194
Trade and other payables	11,12	6,790	6,744
Derivative liabilities	11,12	97	30
Current portion of long-term debt - net	11,12	2,698	11,517
Income tax payable		532	14
Total Current Liabilities		67,491	61,956
Noncurrent Liabilities			
Long-term debt - net of current portion	11,12	40,584	42,885
Retirement benefits liability		249	249
Deferred tax liabilities	2	1,772	1,958
Asset retirement obligation		878	815
Other noncurrent liabilities	12	702	609
Total Noncurrent Liabilities		44,185	46,516
Equity Attributable to Equity Holders of the Parent Company			
Capital stock		9,475	9,475
Additional paid-in capital		9,764	9,764
Retained earnings		39,678	33,748
Other reserves		74	83
Total Equity Attributable to Equity Holders of the Parent Company		58,991	53,070
Non-controlling interest		294	274
Total Equity		59,285	53,344
Total Liabilities & Equity	P	170,961	161,816

Note: See accompanying Management Discussion and Analysis and Selected Notes to Consolidated Financial Statements.

Certified by:


EFREM P. GABRILLO
 Assistant Vice President - Controllers




PETRON CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
FOR THE PERIOD ENDED SEPTEMBER 30, 2011 and 2010
(Amounts in Million Pesos, Except Per Share Amounts)
(UNAUDITED)

	Note	July to September		January to September	
		2011	2010	2011	2010
SALES	2	67,032	54,444	P 201,929	P 169,798
COST OF GOODS SOLD		62,601	50,612	183,638	156,479
GROSS PROFIT		4,431	3,832	18,291	13,319
SELLING AND ADMINISTRATIVE EXPENSES		(2,106)	(1,575)	(5,177)	(4,414)
INTEREST INCOME		309	257	1,007	419
INTEREST EXPENSE		(1,256)	(1,051)	(3,879)	(2,922)
SHARE IN NET LOSS OF AN ASSOCIATE		(66)	-	(169)	-
OTHER INCOME (CHARGES) - net		750	925	40	669
INCOME BEFORE INCOME TAX		2,062	2,388	10,113	7,071
PROVISION FOR INCOME TAX		507	581	2,513	1,724
NET INCOME		P 1,555	P 1,807	P 7,600	P 5,347
Attributable to:					
Equity holders of the parent company	7	1,552	1,798	P 7,581	P 5,320
Non-controlling interest		3	9	19	27
		P 1,555	P 1,807	P 7,600	P 5,347
BASIC DILUTED EARNINGS PER COMMON SHARE ATTRIBUTABLE					
TO EQUITY HOLDERS OF THE PARENT COMPANY	7	P 0.14	0.17	P 0.73	P 0.52

Note: See accompanying Management Discussion and Analysis and Selected Notes to Consolidated Financial Statements.

Certified by:


EFREN P. CABRILLO
 Assistant Vice President - Controllers



PETRON CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
FOR THE PERIOD ENDED SEPTEMBER 30, 2011 AND 2010
(Amounts in Million Pesos)
(UNAUDITED)

	<u>July to September</u>		<u>January to September</u>	
	2011	2010	2011	2010
NET INCOME	P 1,555	P 2,387	P 7,600	P 5,347
NET GAIN (LOSS) ON AVAILABLE-FOR-SALE FINANCIAL ASSETS - NET OF TAX	1	-	(0)	-
EXCHANGE DIFFERENCES ON TRANSLATION OF FOREIGN OPERATIONS	(13)	26	(7)	42
OTHER COMPREHENSIVE INCOME - NET OF TAX	<u>(12)</u>	<u>26</u>	<u>(7)</u>	<u>42</u>
TOTAL COMPREHENSIVE INCOME	<u>P 1,543</u>	<u>P 2,413</u>	<u>P 7,593</u>	<u>P 5,389</u>
Comprehensive Income Attributable to:				
Equity holders of the Parent Company	P 1,538	P 2,404	P 7,573	P 5,362
Non-controlling Interest	<u>5</u>	<u>9</u>	<u>20</u>	<u>27</u>
	<u>P 1,543</u>	<u>P 2,413</u>	<u>P 7,593</u>	<u>P 5,389</u>

Note: See accompanying Management Discussion and Analysis and Selected Notes to Consolidated Financial Statements.

Certified by:


EFREN P. GABRILLO
Assistant Vice President-Controllers




PETRON CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
FOR THE PERIOD ENDED SEPTEMBER 30, 2011 AND 2010
 (Amounts in Million Pesos)

	Equity Attributable to Equity Holders of the Parent Company									
	Retained Earnings									
	Preferred Stock	Common Stock	Additional paid-in capital	Appro- priated	Unappro- priated	Other Reserves	Total	Non- controlling Interest	Total Equity	
Balance at January 1, 2011 (Audited)	P 100	P 9,375	P 9,764	P 15,554	P 18,194	P 83	P 53,070	P 274	P 53,344	
Total comprehensive income					7,582	(9)	7,573	20	7,593	
Appropriation for capital projects				9,627	(9,627)		-		-	
Cash dividends (Note 8)					(1,652)		(1,652)		(1,652)	
Balance at September 30, 2011 (Unaudited)	<u>P 100</u>	<u>P 9,375</u>	<u>P 9,764</u>	<u>P 25,181</u>	<u>P 14,497</u>	<u>P 74</u>	<u>P 58,991</u>	<u>P 294</u>	<u>P 59,285</u>	
Balance at January 1, 2010 (Audited)	-	P 9,375		P 15,492	P 12,522	(P 98)	P 37,291	P 244	P 37,535	
Total comprehensive income					5,320	42	5,362	27	5,389	
Cash dividends (Note 8)					(1,414)		(1,414)		(1,414)	
Issuance of shares	100		9,764				9,864		9,864	
Balance at September 30, 2010 (Unaudited)	<u>P 100</u>	<u>P 9,375</u>	<u>P 9,764</u>	<u>P 15,492</u>	<u>P 16,428</u>	<u>(P 56)</u>	<u>P 51,103</u>	<u>P 271</u>	<u>P 51,374</u>	

Note: See accompanying Management Discussion and Analysis and Selected Notes to Consolidated Financial Statements.

Certified by:


EFREN F. GABRILLO
 Assistant Vice President-Controllers




PETRON CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE PERIOD ENDED SEPTEMBER 30, 2011 and 2010
(Amounts in Million Pesos)
(UNAUDITED)

	2011		2010	
	P	10,113	P	7,070
CASH FLOWS FROM OPERATING ACTIVITIES				
Income before income tax				
Adjustments for:				
Share in net loss of an associate		169		
Depreciation and amortization		2,705		2,485
Interest expense		3,879		2,922
Interest income		(1,007)		(419)
Net unrealized foreign exchange gain		171		(873)
Others		(69)		(3)
Operating income before working capital changes		15,961		11,182
Changes in operating assets and liabilities				
Decrease (increase) in assets:				
Receivables		(3,181)		475
Inventories		(18,943)		(3,849)
Other current assets		(1,903)		(1,460)
Increase (decrease) in liabilities:				
Liabilities for crude oil and petroleum product importation		10,446		16,844
Accounts payable and accrued expenses		360		94
Provisions for doubtful accounts, inventory obsolescence and others		54		(132)
Interest paid		(3,953)		(2,805)
Income taxes paid		(520)		(73)
Interest received		1,038		415
Net cash flows provided by (used in) operating activities		(641)		20,691
CASH FLOWS FROM INVESTING ACTIVITIES				
Additions to:				
Property, plant and equipment		(10,635)		(2,659)
Investment properties		(698)		(760)
Decrease (increase) in:				
Other receivables		(329)		(2,479)
Other noncurrent assets		316		352
Reductions from (additions to):				
Financial assets at fair value through profit or loss		(104)		0
Available-for-sale investments		127		191
Investments		(1,734)		(24,145)
Net cash flows used in investing activities		(13,057)		(29,500)
CASH FLOWS FROM FINANCING ACTIVITIES				
Availment of loans		55,031		145,539
Payments of:				
Loans		(63,445)		(142,179)
Cash dividends		(1,640)		(1,365)
Issuance of Preferred Stock		-		9,864
Others		107		76
Net cash flows provided by (used in) financing activities		(9,947)		11,935
EFFECTS OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS				
		60		(61)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS		(23,585)		3,065
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR		43,984		12,985
CASH AND CASH EQUIVALENTS AT END OF PERIOD	P	20,399	P	16,050

Note: See accompanying Management Discussion and Analysis and Selected Notes to Consolidated Financial Statements.

Certified by:


EFREN S. GABRILLO
Assistant Vice President - Controllers

PETRON CORPORATION AND SUBSIDIARIES
SELECTED NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Amounts in Millions, Except Per Share Data)

1. Summary of Significant Accounting and Financial Reporting Policies

Petron Corporation and Subsidiaries (collectively referred to as the “Group”) prepared its consolidated interim financial statements as of and for the period ended September 30, 2011 and comparative financial statements for the same period in 2010 following the new presentation rules under Philippine Accounting Standard (PAS) No. 34, Interim Financial Reporting. The consolidated financial statements of the Group have been prepared in compliance with Philippine Financial Reporting Standards (PFRS).

The consolidated financial statements are presented in Philippine peso and all values are rounded to the nearest million (₱000,000), except when otherwise indicated.

The principal accounting policies and methods adopted in preparing the interim consolidated financial statements of the Group are the same as those followed in the most recent annual audited financial statements.

Adoption of New Standards, Amendments to Standards and Interpretations

The Financial Reporting Standards Council (FRSC) approved the adoption of a number of new or revised standards, amendments to standards, and interpretations [based on International Financial Reporting Interpretation Committee (IFRIC) Interpretations] as part of PFRS.

Amendments to Standard and Interpretations Adopted in 2011

Starting January 1, 2011, the Group adopted the following PFRS:

- *Prepayments of a Minimum Funding Requirement (Amendments to Philippine Interpretation IFRIC 14: PAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction)*. These amendments remove unintended consequences arising from the treatment of prepayments where there is a minimum funding requirement and result in prepayments of contributions in certain circumstances being recognized as an asset rather than an expense. The amendments are effective for annual period beginning on or after January 1, 2011.
- Revised PAS 24, *Related Party Disclosures (2009)*, amends the definition of a related party and modifies certain related party disclosure requirements for government-related entities. The revised standard is effective for annual periods beginning on or after January 1, 2011.

- *Improvements to PFRSs 2010* contain 11 amendments to 6 standards and 1 interpretation, of which only the following are applicable to the Group:
 - PAS 1, *Presentation of Financial Statements*. The amendments clarify that disaggregation of changes in each component of equity arising from transactions recognized in other comprehensive income also is required to be presented either in the statement of changes in equity or in the notes. The amendments are effective for annual periods beginning on or after January 1, 2011.
 - PAS 27, *Consolidated and Separate Financial Statements*. The amendments clarify that the consequential amendments to PAS 21, *The Effects of Changes in Foreign Exchange Rates*, PAS 28, *Investment in Associates*, and PAS 31, *Interest in Joint Ventures* resulting from PAS 27 (2008) should be applied prospectively, with the exception of amendments resulting from renumbering. The amendments are effective for annual periods beginning on or after July 1, 2010.
 - PAS 34, *Interim Financial Reporting*. The amendments add examples to the list of events or transactions that require disclosure under PAS 34 and remove references to materiality in PAS 34 that describes other minimum disclosures. The amendments are effective for annual periods beginning on or after January 1, 2011.
 - PFRS 1, *First-time Adoption of PFRSs*. The amendments: (i) clarify that PAS 8 is not applicable to changes in accounting policies occurring during the period covered by an entity's first PFRS financial statements; (ii) introduce guidance for entities that publish interim financial information under PAS 34, *Interim Financial Reporting* and change either their accounting policies or use of the PFRS 1 exemptions during the period covered by their first PFRS financial statements; (iii) extend the scope of paragraph D8 of PFRS 1 so that an entity is permitted to use an event-driven fair value measurement as deemed cost for some or all of its assets when such revaluation occurred during the reporting periods covered by its first PFRS financial statements; and (iv) introduce an additional optional deemed cost exemption for entities to use the carrying amounts under previous GAAP as deemed cost at the date of transition to PFRSs for items of property, plant and equipment or intangible assets used in certain rate-regulated activities. The amendments are effective for annual periods beginning on or after January 1, 2011.

- PFRS 3, *Business Combinations*. The amendments: (i) clarify that contingent consideration arising in a business combination previously accounted for in accordance with PFRS 3 (2004) that remains outstanding at the adoption date of PFRS 3 (2008) continues to be accounted for in accordance with PFRS 3 (2004); (ii) limit the accounting policy choice to measure non-controlling interests upon initial recognition at fair value or at the non-controlling interest's proportionate share of the acquiree's identifiable net assets to instruments that give rise to a present ownership interest and that currently entitle the holder to a share of net assets in the event of liquidation; (iii) expand the current guidance on the attribution of the market-based measure of an acquirer's share-based payment awards issued in exchange for acquiree awards between consideration transferred and post-combination compensation cost when an acquirer is obliged to replace the acquiree's existing awards to encompass voluntarily replaced unexpired acquiree awards. These amendments are effective for annual periods beginning on or after July 1, 2010.
- PFRS 7, *Financial Instruments: Disclosures*. The amendments add an explicit statement that qualitative disclosure should be made in the context of the quantitative disclosures to better enable users to evaluate the entity's exposure to risks arising from financial instruments. In addition, the IASB amended and removed existing disclosure requirements. The amendments are effective for annual periods beginning on or after January 1, 2011.
- Philippine Interpretation IFRIC 13, *Customer Loyalty Programmes*. The amendments clarify that the fair value of award credits takes into account the amount of discounts or incentives that otherwise would be offered to customers that have not earned the award credits. The amendments are effective for annual periods beginning on or after January 1, 2011.
- Philippine Interpretation IFRIC 19, *Extinguishing Financial Liabilities with Equity Instruments*, addresses issues in respect of the accounting by the debtor in a debt for equity swap transaction. It clarifies that equity instruments issued to a creditor to extinguish all or part of the financial liability in a debt for equity swap are consideration paid in accordance with PAS 39 paragraph 41. The interpretation is applicable for annual period beginning on or after July 1, 2010.

The adoption of these foregoing new or revised standards, amendments to standards and Philippine Interpretations of IFRIC did not have a material effect on the interim consolidated financial statements.

New or Revised Standards, Amendments to Standards and Interpretations Not Yet Adopted

The Group will adopt the following new or revised standards, amendments to standards and interpretations in the respective effective dates:

- *Disclosures - Transfers of Financial Assets (Amendments to PFRS 7)*, require additional disclosures about transfers of financial assets. The amendments require disclosure of information that enables users of financial statements to understand the relationship between transferred financial assets that are not derecognized in their entirety and the associated liabilities; and to evaluate the nature of, and risks associated with, the entity's continuing involvement in derecognized financial assets. Entities are required to apply the amendments for annual periods beginning on or after July 1, 2011.
- *Philippine Interpretation IFRIC 15, Agreements for the Construction of Real Estate*, applies to the accounting for revenue and associated expenses by entities that undertake the construction of real estate directly or through subcontractors. It provides guidance on the recognition of revenue among real estate developers for sales of units, such as apartments or houses, "off plan"; i.e., before construction is completed. It also provides guidance on how to determine whether an agreement for the construction of real estate is within the scope of PAS 11, *Construction Contracts*, or PAS 18, *Revenue*, and the timing of revenue recognition. The interpretation is effective for annual periods beginning on or after January 1, 2012.

The Group will assess the impact of the new or revised standards, amendments to standards and interpretations on the consolidated financial statements upon adoption on their respective effective dates.

- PFRS 9, *Financial Instruments* (2009) was issued as the first phase of the PAS 39 replacement project. The chapters of the standard released in 2009 only related to classification and measurement of financial assets. PFRS 9 (2009) retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets: amortized cost and fair value. The basis of classification depends on the entity's business model and contractual cash flow characteristics of the financial asset. In October 2010, a new version of PFRS 9, *Financial Instruments* (2010) was issued which now includes all the requirements of PFRS 9 (2009) without amendment. The new version of PFRS 9 also incorporates requirements with respect to the classification and measurement of financial liabilities and the derecognition of financial assets and financial liabilities. The guidance in PAS 39 on impairment of financial assets and hedge accounting continues to apply. The new standard is effective for annual periods beginning on or after January 1, 2013. PFRS 9 (2010) supersedes PFRS 9 (2009). However, for annual periods beginning before January 1, 2013, an entity may elect to apply PFRS 9 (2009) rather than PFRS 9 (2010).

The Group has decided not to early adopt either PFRS 9 (2009) or PFRS 9 (2010) for its 2011 annual financial reporting. The Group shall conduct in early 2012 another impact evaluation using the outstanding balances as of December 31, 2011. The Group's decision whether to early adopt either PFRS 9 (2009) or PFRS 9 (2010) for the 2012 financial reporting shall be disclosed in the Group's interim financial statements as of March 31, 2012.

2. Segment Information

Management identifies segments based on business and geographic locations. These operating segments are monitored and strategic decisions are made on the basis of adjusted segment operating results. The CEO (the chief operating decision maker) reviews management reports on a regular basis.

The Group's major sources of revenues are as follows:

- a. Sales of petroleum and other related products which include gasoline, diesel and kerosene offered to motorists and public transport operators through its service station network around the country.
- b. Insurance premiums from the business and operation of all kinds of insurance and reinsurance, on sea as well as on land, of properties, goods and merchandise, of transportation or conveyance, against fire, earthquake, marine perils, accidents and all others forms and lines of insurance authorized by law, except life insurance.
- c. Lease of acquired real estate properties for petroleum, refining, storage and distribution facilities, gasoline service stations and other related structures.
- d. Sales on wholesale or retail and operation of service stations, retail outlets, restaurants, and the like.
- e. Export sales of various petroleum and non-fuel products to other Asian countries such as South Korea, Taiwan, China, Thailand, Indonesia, Singapore, Cambodia, Japan, India, UAE, Pakistan and Malaysia.

Segment Assets and Liabilities

Segment assets include all operating assets used by a segment and consist principally of operating cash, receivables, inventories, and property, plant and equipment, net of allowances and impairment. Segment liabilities include all operating liabilities and consist principally of accounts payable, wages, taxes currently payable and accrued liabilities. Segment assets and liabilities do not include deferred taxes.

Inter-segment Transactions

Segment revenues, expenses and performance include sales and purchases between operating segments. Transfer prices between operating segments are set on an arm's length basis in a manner similar to transactions with third parties. Such transfers are eliminated in consolidation.

The following tables present revenue and income information and certain asset and liability information regarding the business segments as of September 30, 2011 and December 31, 2010 and for the nine months ended September 30, 2011 and 2010. Segment assets and liabilities exclude deferred tax assets and deferred tax liabilities:

	Petroleum	Insurance	Leasing	Marketing	Elimination	Total
<u>Period Ended Sept. 30, 2011</u>						
Revenue						
External Sales	P200,702	P -	P -	P1,227	P -	P201,929
Inter-segment Sales	159,033	89	265	-	(159,387)	-
Segment results	12,588	70	123	65	268	13,114
Net income	7,581	120	32	75	(208)	7,600
<u>As of Sept. 30, 2011</u>						
Assets and liabilities						
Segment assets	190,536	1,877	3,437	832	(25,891)	170,791
Segment liabilities	131,297	243	2,497	161	(24,294)	109,904
Other segment information						
Property, plant and equipment	39,495	-	-	216	3,267	42,978
Depreciation and amortization	2,676	-	-	29	-	2,705
<u>Period Ended Sept. 30, 2010</u>						
Revenue						
External Sales	P166,434	P -	P -	P3,364	P -	P169,798
Inter-segment Sales	2,354	107	247	-	(2,708)	-
Segment results	8,459	89	128	122	107	8,905
Net income	5,075	132	44	120	(24)	5,347
<u>As of Dec. 31, 2010</u>						
Assets and liabilities						
Segment assets	163,823	2,086	2,935	1,097	(8,153)	161,788
Segment liabilities	108,665	559	2,027	303	(5,040)	106,514
Other segment information						
Property, plant and equipment	31,753	-	1	379	2,824	34,957
Depreciation and amortization	3,419	-	-	65	(1)	3,483

The following tables present additional information on the petroleum business segment as of September 30, 2011 and December 31, 2010 and for the nine months ended September 30, 2011 and 2010:

	Retail	Lube	Gasul	Industrial	Others	Total
<u>Property, plant and equipment</u>						
As of September 30, 2011	P4,990	P293	P211	P73	P33,921	P39,488
As of December 31, 2010	4,524	345	181	43	26,660	31,753
<u>Capital Expenditures</u>						
As of September 30, 2011	P492	P -	P44	P6	P11,880	P12,422
As of December 31, 2010	169	1	8	2	2,615	2,795
<u>Revenue</u>						
Period ended Sept. 30, 2011	P79,885	P1,855	P14,668	P78,187	P26,822	P201,417
Period ended Sept. 30, 2010	67,632	1,594	10,855	69,742	18,964	168,787

Geographical Segments

The following table presents revenue information regarding the geographical segments of the Group for the nine months ended September 30, 2011 and 2010.

	Petroleum	Insurance	Leasing	Marketing	Elimination	Total
<u>Period ended</u>						
<u>September 30, 2011</u>						
Revenue						
Local	P181,085	P56	P265	P1,227	(P1,742)	P180,891
Export/International	178,650	33	-	-	(157,645)	21,038
<u>Period ended</u>						
<u>September 30, 2010</u>						
Revenue						
Local	P154,830	P63	P247	P3,364	(P2,708)	P155,796
Export/International	13,958	44	-	-	-	14,002

3. Related Party Transactions

Lease Agreement

On September 30, 2009, New Ventures Realty Corporation entered into a 25-year lease with the Philippine National Oil Company (PNOC) without rent-free period, covering a property which shall be used for refinery, commencing January 1, 2010 and ending on December 31, 2039. The annual rental shall be P93 payable on the 15th day of January each year without the necessity of demand. This non-cancellable lease is subject to renewal options and annual escalation clauses of 3% per annum up to 2011. The leased premises shall be reappraised starting 2012 and every fifth year thereafter in which the new rental rate shall be determined equivalent to 5% of the reappraised value, and still subject to annual escalation clause of 3% for the four years following the appraisal. Prior to this agreement, Petron has an outstanding lease agreement on the same property from PNOC. Also, as of September 30, 2011, Petron leases other parcels of land from PNOC for its bulk plants and service stations.

Transactions with Current Owners/Related Parties

- a. Sales relate to the Parent Company's supply agreements with various subsidiaries of San Miguel Corporation (SMC). Under these agreements, the Parent Company supplies the bunker, diesel fuel and lube requirements of selected SMC plants and subsidiaries.
- b. Purchases relate to purchase of goods and services such as construction, information technology and shipping.
- c. Petron entered into lease agreement with San Miguel Properties, Inc. (SMPI) for its office space covering 6,759 square meters with a monthly rate of P3.9. The lease, which commenced on June 1, 2011, is for a period of one year and maybe renewed for a period in accordance with the written agreement of the parties.
- d. The Parent Company also pays SMC for its share in common expenses such as utilities and administrative fees.
- e. The Parent Company has advances to Petron Corporation Employee Retirement Plan (PCERP) amounting to P22,668 and P22,435 as of September 30, 2011 and December 31, 2010, respectively, included as part of "Other noncurrent assets" account.
- f. As of September 30, 2011, the Parent Company has current receivables of P172 and noncurrent receivables of P529 from Petrochemical Asia (HK) Limited included as part of "Other current assets" and "Other noncurrent assets" accounts, respectively.

The balances and transactions with related parties as of September 30, 2011 and December 31, 2010 follows:

September 30, 2011 Related Parties	Relationship with Related parties	Revenue from Related Parties	Purchases from Related Parties	Amounts owed by Related Parties	Amounts owed to Related Parties
SMC	Ultimate Parent	P1	P56	P0.07	P3
Distileria Bago, Inc.	Under common control	374	-	131	-
San Miguel Brewery Inc.	Under common control	677	0.18	97	44
San Miguel Yamamura Packaging Corporation	Under common control	532	0.19	108	-
SMC Shipping and Lighterage Corporation	Under common control	302	555	48	43
Ginebra San Miguel, Inc.	Under common control	106	12	19	5
San Miguel Foods, Inc.	Under common control	229	0.02	31	-
San Miguel Energy Corporation	Under common control	87	453	-	56
San Miguel Yamamura Asia Corporation	Under common control	575	-	83	-
Challenger Aero Air Corporation	Under common control	20	-	13	-
Mindanao Corrugated Fibreboard, Inc.	Under common control	31	-	4	-
San Miguel Purefoods Company, Inc.	Under common control	125	2	40	1
Archen Technologies, Inc.	Under common control	12	307	-	93
SMPI	Under common control	-	40	29	-
Others	Under common control	27	55	16	12
		P3,098	P1,480.39	P619.07	P257

December 31, 2010 Related Parties	Relationship with Related parties	Revenue from Related Parties	Purchases from Related Parties	Amounts owed by Related Parties	Amounts owed to Related Parties
SMC	Ultimate Parent	P1	P29	P2	P33
PanAsia Energy Holdings, Inc.	Under common control	8,045	-	1,428	-
Distileria Bago, Inc.	Under common control	720	-	38	-
San Miguel Brewery Inc.	Under common control	573	0.60	100	-
San Miguel Yamamura Packaging Corporation	Under common control	350	-	51	-
SMC Shipping and Lighterage Corporation	Under common control	304	407	46	13
Ginebra San Miguel, Inc.	Under common control	169	0.30	58	-
San Miguel Foods, Inc.	Under common control	150	3	36	-
San Miguel Energy Corporation	Under common control	83	-	25	-
San Miguel Yamamura Asia Corporation	Under common control	40	-	40	-
Challenger Aero Air Corporation	Under common control	22	2	9	-
Mindanao Corrugated Fibreboard, Inc.	Under common control	17	-	4	-
San Miguel Purefoods Company, Inc.	Under common control	14	4	-	7
Archen Technologies, Inc.	Under common control	12	227	2	26
SMPI	Under common control	-	63	-	5
San Miguel Paper Packaging Corporation	Under common control	-	-	49	-
Others	Under common control	12	39	5	6
		P10,512	P774.90	P1,893	P90

4. Property, Plant and Equipment

Property, plant and equipment consists of:

	<u>September 30, 2011</u>			
	January 1, 2011	Additions and Transfers	Disposals and Reclassifications	Sept. 30, 2011
Cost:				
Buildings	P8,055	P42	(P2)	P8,095
Machinery & Equipment Refinery and Plant Equipment	5,816	(198)	-	5,618
Service Stations and Other Equipment	37,292	83	-	37,375
Transportation Equipment	5,353	301	(8)	5,646
Office Equipment, Furniture & Fixtures	519	63	(20)	562
Land Improvements	1,626	187	(62)	1,751
Leasehold Improvements	4,332	430	-	4,762
Capital Projects in Progress	194	12	-	206
	2,796	9,626	-	12,422
	65,983	10,546	(92)	76,437
Accumulated Depreciation:				
Buildings	(3,714)	(248)	-	(3,962)
Machinery & Equipment Refinery and Plant Equipment	(3,907)	(168)	-	(4,075)
Service Stations and Other Equipment	(16,552)	(1,516)	-	(18,068)
Transportation Equipment	(3,756)	(362)	6	(4,112)
Office Equipment, Furniture & Fixtures	(355)	(38)	19	(374)
Land Improvements	(1,373)	(95)	48	(1,420)
Leasehold Improvements	(1,271)	(27)	-	(1,298)
	(98)	(52)	-	(150)
	(31,026)	(2,506)	73	(33,459)
Net Book Value	P34,957	P8,040	(P19)	P42,978

September 30, 2010

	January 1, 2010	Additions and Transfers	Disposals and Reclassifications	Sept. 30, 2010
Cost:				
Buildings	P9,545	P145	(P1,640)	P8,050
Machinery & Equipment Refinery and Plant	5,191	99	(42)	5,248
Equipment	36,802	419	-	37,221
Service Stations and Other Equipment	4,070	631	22	4,723
Transportation Equipment	504	70	(63)	511
Office Equipment, Furniture & Fixtures	1,522	53	(30)	1,545
Land Improvements	4,962	(733)	-	4,229
Leasehold Improvements	82	8	2	92
Capital Projects in Progress	1,450	2,019	-	3,469
	64,128	2,711	(1,751)	65,088
Accumulated Depreciation:				
Buildings	(4,214)	(349)	885	(3,678)
Machinery & Equipment Refinery and Plant	(3,593)	(190)	9	(3,774)
Equipment	(14,439)	(1,595)	5	(16,029)
Service Stations and Other Equipment	(3,383)	(236)	1	(3,618)
Transportation Equipment	(364)	(37)	47	(354)
Office Equipment, Furniture & Fixtures	(1,295)	(83)	28	(1,350)
Land Improvements	(1,231)	(29)	-	(1,260)
Leasehold Improvements	(32)	(6)	-	(38)
	(28,551)	(2,525)	975	(30,101)
Net Book Value	P35,577	P186	(P776)	P34,987

Capital Commitments

As of September 30, 2011, and December 31, 2010 the Group has outstanding commitments to acquire property, plant and equipment amounting to P3,864 and P1,142, respectively.

5. Assets Held for Sale

Petron has an investment property consisting of office units located at Petron Mega Plaza which has a floor area of 21,216 square meters covering the 28th - 44th floors and 206 parking lots. On December 1, 2010, Petron's Board of Directors (BOD) approved the sale of these properties to provide cash flows for various projects. On May 2, 2011, the Parent company sold the 32nd floor (with total floor area of 1,530 square meters) and 10 parking lots to the International Committee of the Red Cross with a total book value of P57. On September 2011, it was reverted back to "Investment Property" account in view of the fact that the remaining floors have already been tenanted. As of September 30, 2011, the carrying amount of assets-held-for-sale dropped to P10 from P823 in December 2010.

6. Fuel Supply Contract

The Parent Company entered into various fuel supply contracts with National Power Corporation (NPC). Under the agreements, the Parent Company supplies the bunker and diesel fuel oil requirements of NPC, its Independent Power Producers (IPP) and Small Power Utility Groups (SPUG) power plants/barges. For the nine months ended September 30, 2011, the following are the fuel supply contracts granted to Petron:

Bid Date	Date of Award	Contract Duration	IFO** (in KL**)	IFO (Amount)	DFO** (in KL)	DFO (Amount)
Jan 12, 2011	Jan 31, 2011	Jan to Dec 2011	44,587	P1,127	15,192	P490
Mar 10, 2011	Mar 23, 2011	Apr to Jun 2011	4,833	140	9,560	373
Jun 17, 2011	Jul 8, 2011	Jul to Dec 2011	87,000	3,074		
Jul 1, 2011	Jul 6, 2011	Jul to Aug 2011	1,326	48	2,791	121
Jul 18, 2011	Jul 25, 2011	Jul to Aug 2011			1,610	71
Aug 26, 2011	Aug 26, 2011	Apr to Jun 2011	1,207	35	569	22
Sep 5, 2011	Sep 20, 2011	Sep to Dec 2011	5,709	197	22,913	980
Sep 15, 2011	Sep 16, 2011	Sep to Dec 2011			900	36

***IFO = Industrial Fuel Oil*

DFO = Diesel Fuel Oil

KL = Kilo Liters

7. Earnings Per Share

Basic and diluted earnings per share amounts for the nine months ended September 30, 2011 and 2010 are as follows:

	2011	2010
Net income attributable to equity holders of the Parent Company	P7,581	P5,320
Dividends on preferred shares for the period	714	476
Net income attributable to common shareholders of Parent Company	P6,867	P4,844
Weighted average number of common shares outstanding (in millions)	9,375	9,375
Basic/diluted earnings per common share	P0.73	P0.52

As of September 30, 2011 and 2010, the Group has no dilutive debt or equity instruments.

8. Dividends

Cash dividends declared by the Parent Company's BOD to common shareholders amounted to P0.10 per share as of September 30, 2011 and 2010.

While cash dividends declared by the Parent Company's BOD to preferred stockholders amounted to P7.146 per share as of September 30, 2011 and P4.764 per share as of September 30, 2010.

9. Investment in an Associate

On January 3, 2011, Petron entered into a Share Sale and Purchase Agreement with Harbour Centre Port Terminal, Inc. for the purchase of 35% of the outstanding and issued capital stock of Manila North Harbour Port Inc.

10. Commitments and Contingencies

Unused Letters of Credit and Outstanding Standby Letters of Credit

Petron has unused letters of credit amounting to approximately P13 as of September 30, 2011 and P532 as of December 31, 2010. On the other hand, outstanding standby letters of credit for crude importations amounted to P18,272 and P8,704 as of September 30, 2011 and December 31, 2010, respectively.

Tax Credit Certificates Related Cases

In 1998, Petron contested before the Court of Tax Appeals (CTA), the collection by the Bureau of Internal Revenue (BIR) of deficiency taxes arising from the company's acceptance and use of Tax Credit Certificates (TCCs) worth P659 million from 1993-1997. The CTA ruled in favor of Petron. The BIR then appealed the case to the Court of Appeals (CA) after which the CA issued a resolution suspending decision on the case until the termination of the Department of Finance (DOF) investigation. Petron filed a motion for reconsideration which remains pending at the moment.

In May 2002, the BIR issued a collection letter for deficiency taxes of P254 million plus interest and charges for the years 1995-1998, as a result of the cancellation of the Tax Debit Memos and TCCs by the DOF Center ExCom. Petron elevated the protest to the CTA. The Second Division CTA denied Petron's Petition for Review for lack of merit. Petron then appealed the case with the CTA En Banc. On December 3, 2008, the CTA En Banc promulgated a decision reversing the unfavorable decision of the CTA 2nd Division. The CIR filed a Petition for Review with the Supreme Court where the case remains submitted for resolution.

Pandacan Terminal Operations

Citing concerns for safety, security and health, the City of Manila passed City Ordinance No. 8027 which reclassified the Pandacan Terminal from industrial to commercial. Petron, together with the other oil companies asked the Supreme Court to change the ruling since the Comprehensive Land Use Plan and Zoning Ordinance (Ordinance No.8119) repealed the Manila Ordinance No. 8027. Ordinance No. 8119 gives Petron a seven-year grace period to continue its operations in the Pandacan Terminal. In February 2008, the Supreme Court denied the oil company's motion for reconsideration and declared Manila Ordinance No. 8027 valid and applicable to all oil terminals. The Court directed the oil companies to submit their relocation plans to the RTC within 90 days to determine the reasonableness of the time frame for relocation. In May 2008, Petron, Shell and Chevron submitted their Comprehensive Relocation Plan in compliance with the February Resolution. The Pandacan Terminal is strategically significant since it serves about 40% of the company's refinery output and 100% of the company's lubricants, greases and oxidized asphalt.

On May 28, 2009, Mayor Alfredo Lim of Manila approved and signed proposed Ordinance 7177 (which became Ordinance No. 8187) repealing Ordinance No. 8027 and 8119 and allowing the continued stay of the oil depots at Pandacan. Mayor Lim was reelected Mayor of Manila in the May 10, 2010 election.

On June 1, 2009, Social Justice Society officers filed a petition for prohibition against Mayor Lim before the Supreme Court, seeking the nullification of Ordinance 8187. On June 5, 2009, former Mayor Lito Atienza filed his own petition with the Supreme Court seeking to stop the implementation of Ordinance 8187. The Court has ordered the City to file its comment but the Court did not issue a temporary restraining order. The City filed its comment on August 13, 2009.

The main storage facility of Petron is located at the Pandacan Terminal. Approximately 40% of Petron's total sales volume is moved through Pandacan. To ensure steady supply and in order to mitigate the risks at the Pandacan Terminal, the company's nearby depots in Navotas, Metro Manila and in Rosario, Cavite can also distribute products to the areas being served by the Pandacan terminal.

Petron believes that, given the prevailing law and existing jurisprudence, the Supreme Court will uphold the validity of Ordinance No. 8187.

As stated in the papers (Philippine Daily Inquirer, June 28, 2010 issue), and as confirmed during the management meeting in 2010, Petron is looking at the Manila North Harbor as a possible location for its depot that will replace its facilities at the Pandacan Terminal. This is just one of the sites that Petron is looking at for the transfer, should it be forced to move out of Pandacan. According to SMC President and COO, Mr. Ramon Ang, moving Petron's depot facilities to the North Harbor would reduce the company's handling costs by as much as 80%, which may, in turn, result in lower pump prices. Mr. Ang explained that bringing oil to Pandacan can only be done with barges as a result of the Pasig River's shallow draught of only 3 meters. North Harbor, on the other hand, has deep-water facilities which tankers can use directly.

Based on SEC FORM 17-A filings of Petron, the company has filed its Manifestation on November 30, 2010 to inform the Supreme Court that it has decided to cease operation of its petroleum product storage facilities in Pandacan, Manila within 5 years or not later than January 2016 due to environmental issues and issues on the location of the terminal.

Petron's operations at the Pandacan Terminal are being scaled down in line with its commitment to have minimal operations there by 2014. The company is already building storage capacities in alternative sites. These storage facilities will support the expected growth in demand for petroleum products outside of Metro Manila and the increased production under RMP-2.

Guimaras Case

Complaints for Violation of Sec. 28, Paragraph 5 in relation to Section 4 of the Philippine Clean Water Act of 2004 (RA 9275) were filed against Messrs. Nicasio I. Alcantara and Khalid D. Al-Faddagh, Petron's former Chairman and President, respectively, and the Captain and owner of M/T Solar 1 on June 17, 2009, as a result of the oil slick from the said vessel which sank on August 11, 2006.

The Respondents denied the allegations imputed against them, as the same accusation was already resolved and dismissed by the Provincial Prosecutor's Office of Guimaras in a Resolution dated March 2, 2007.

On July 14, 2011, the Provincial Prosecutor's Office of Guimaras issued a Joint Resolution finding probable cause to indict the owner and the Captain of M/T Solar 1 and Messrs. Alcantara and Mr. Faddagh for Violation of Section 28, Paragraph 5 in relation to Section 4 of the Clean Water Act of 2004.

Messrs. Alcantara and Faddagh filed their Motion for Reconsideration with the Provincial Prosecutor's Office of Guimaras on August 1, 2011. The Complainants filed their Reply and Supplemental Comment while Messrs. Alcantara and Faddagh countered this with a Reply with Motion for Inhibition. Both Motions for Reconsideration and Inhibition have not been resolved.

Petron did not hire or engaged the services of the Captain of M/T Solar 1 contrary to the finding contained in the Marine Accident Inquiry Report of the Special Marine Inquiry Board relied upon by the Prosecutor's Office. In addition, under Republic Act No. 9483, otherwise known as "The Oil Pollution Compensation Act of 2007", it is the owner of the vessel, not the charterer, that is liable for any oil spill or pollution damage that may result from the operation of the said vessel.

11. Financial Risk Management Objectives and Policies

Objectives and Policies

The Group has significant exposure to the following financial risks primarily from its use of financial instruments:

- Foreign currency risk
- Interest rate risk
- Credit risk
- Liquidity risk
- Commodity price risk
- Other market price risk

This note presents information about the Group's exposure to each of the foregoing risks, the Group's objectives, policies and processes for measuring and managing these risks, and the Group's management of capital.

The Group's principal financial instruments include cash and cash equivalents, debt and equity securities, bank loans and derivative instruments. The main purpose of bank loans is to finance working capital relating to importation of crude and petroleum products, as well as to partly fund capital expenditures. The Group has other financial assets and liabilities such as trade and other receivables and trade and other payables, which are generated directly from its operations.

It is the Group's policy not to enter into derivative transactions for speculative purposes. The Group uses hedging instruments to protect its margin on its products from potential price volatility of crude oil and products. It also enters into short-term forward currency contracts to hedge its currency exposure on crude oil importations.

The main risks arising from the Group's financial instruments are foreign exchange risk, interest rate risk, credit risk, liquidity risk and commodity price risk. The BOD regularly reviews and approves the policies for managing these financial risks. Details of each of these risks are discussed below, together with the related risk management structure.

Risk Management Structure

The Group follows an enterprise-wide risk management framework for identifying, assessing and addressing the risk factors that affect or may affect its businesses.

The Group's risk management process is a bottom-up approach, with each risk owner mandated to conduct regular assessment of its risk profile and formulate action plans for managing identified risks. As the Group's operation is an integrated value chain, risks emanate from every process, while some could cut across groups. The results of these activities flow up to the Management Committee and, eventually, the BOD through the Group's annual business planning process.

Oversight and technical assistance is likewise provided by corporate units and committees with special duties. These groups and their functions are:

1. The Risk and Insurance Management Group, which is mandated with the overall coordination and development of the enterprise-wide risk management process.
2. The Financial Risk Management Unit of the Treasurer's Department, which is in charge of foreign exchange hedging transactions.
3. The Transaction Management Unit of Controllers Department, which provides backroom support for all hedging transactions.
4. The Corporate Technical & Engineering Services Group, which oversees strict adherence to safety and environmental mandates across all facilities.
5. The Internal Audit Department, which has been tasked with the implementation of a risk-based auditing.

The BOD also created separate board-level entities with explicit authority and responsibility in managing and monitoring risks, as follows:

- a. The Audit Committee, which ensures the integrity of internal control activities throughout the Group. It develops, oversees, checks and pre-approves financial management functions and systems in the areas of credit, market, liquidity, operational, legal and other risks of the Group, and crisis management. The Internal Audit Department and the External Auditor directly report to the Audit Committee regarding the direction, scope and coordination of audit and any related activities.
- b. The Compliance Officer, who is a senior officer of Petron reports to the BOD through the Audit Committee. He monitors compliance with the provisions and requirements of the Corporate Governance Manual, determines any possible violations and recommends corresponding penalties, subject to review and approval of the BOD. The Compliance Officer identifies and monitors compliance risk. Lastly, the Compliance Officer represents the Group before the SEC regarding matters involving compliance with the Code of Corporate Governance.

Foreign Currency Risk

The Group's functional currency is the Philippine peso, which is the denomination of the bulk of the Group's revenues. The Group's exposures to foreign exchange risk arise mainly from United States (US) dollar-denominated sales as well as purchases principally of crude oil and petroleum products. As a result of this, the Group maintains a level of US dollar-denominated assets and liabilities during the period. Foreign exchange risk occurs due to differences in the levels of US dollar-denominated assets and liabilities.

The Group pursues a policy of hedging foreign exchange risk by purchasing currency forwards or by substituting US dollar-denominated liabilities with peso-based debt. The natural hedge provided by US dollar-denominated assets is also factored in hedging decisions. As a matter of policy, currency hedging is limited to the extent of 100% of the underlying exposure.

The Group is allowed to engage in active risk management strategies for a portion of its foreign exchange risk exposure. Loss limits are in place, monitored daily and regularly reviewed by management.

Information on the Group's US dollar-denominated financial assets and liabilities and their Philippine peso equivalents as of September 30, 2011 and December 31, 2010 are as follows:

	September 30, 2011		December 31, 2010	
	US Dollar	Peso Equivalent	US Dollar	Peso Equivalent
Assets				
Cash and cash equivalents	US\$318	P13,897	US\$648	P28,395
Trade and other receivables	608	26,573	173	7,606
Non-current receivables	1	63	1	29
	927	40,533	822	36,030
Liabilities				
Drafts and loans payable	30	1,312	59	2,573
Liabilities for crude oil and petroleum product importation	1,067	46,629	288	12,606
Long-term debt (including current maturities)	276	12,072	355	15,563
	1,373	60,013	702	30,742
Net foreign currency-denominated monetary assets	(US\$446)	(P19,480)	US\$120	P5,288

The Group reported net foreign exchange gains (losses) amounting to (P18) and P1,182 for the period ending September 30, 2011 and 2010, respectively, with the translation of its foreign currency-denominated assets and liabilities. These mainly resulted from the movements of the Philippine peso against the US dollar as shown in the following table:

	Peso to US Dollar
December 31, 2009	46.20
September 30, 2010	43.88
December 31, 2010	43.84
September 30, 2011	43.72

The management of foreign currency risk is also supplemented by monitoring the sensitivity of financial instruments to various foreign currency exchange rate scenarios. Foreign exchange movements affect reported equity through the retained earnings arising from increases or decreases in unrealized and realized foreign exchange gains or losses.

The following table demonstrates the sensitivity to a reasonably possible change in the US dollar exchange rate, with all other variables held constant, of profit before tax and equity as of September 30, 2011 and December 31, 2010:

	₱1 decrease in the US\$ exchange rate		₱1 increase in the US\$ exchange rate	
	Effect on Income before Income Tax	Effect on Equity	Effect on Income before Income Tax	Effect on Equity
September 30, 2011				
Cash and cash equivalents	(P299)	(P228)	P299	P228
Trade and other receivables	(95)	(579)	95	579
Noncurrent receivables	-	(2)	-	2
	(394)	(809)	394	809
Drafts and loans payable	30	21	(30)	(21)
Liabilities for crude oil and petroleum product importation	569	896	(569)	(896)
Long-term debt (including current maturities)	276	193	(276)	(193)
	875	1,110	(875)	(1,110)
	P481	P301	(P481)	(P301)

	₱1 decrease in the US\$ exchange rate		₱1 increase in the US\$ exchange rate	
	Effect on Income before Income Tax	Effect on Equity	Effect on Income before Income Tax	Effect on Equity
December 31, 2010				
Cash and cash equivalents	(P642)	(P455)	P642	P455
Trade and other receivables	(97)	(144)	97	144
Noncurrent receivables	-	(1)	-	1
	(739)	(600)	739	600
Drafts and loans payable	-	59	-	(59)
Liabilities for crude oil and petroleum product importation	285	202	(285)	(202)
Long-term debt (including current maturities)	355	249	(355)	(249)
	640	510	(640)	(510)
	(P99)	(P90)	P99	P90

Exposures to foreign exchange rates vary during the period depending on the volume of overseas transactions. Nonetheless, the analysis above is considered to be representative of the Group's currency risk.

Interest Rate Risk

Interest rate risk is the risk that future cash flows from a financial instrument (cash flow interest rate risk) or its fair value (fair value interest rate risk) will fluctuate because of changes in market interest rates. The Group's exposure to changes in interest rates relates mainly to long-term borrowings and investment securities. Investments or borrowings issued at fixed rates expose the Group to fair value interest rate risk. On the other hand, investments or borrowings issued at variable rates expose the Group to cash flow interest rate risk.

The Group manages its interest costs by using a combination of fixed and variable rate debt instruments. Management is responsible for monitoring the prevailing market-based interest rates and ensures that the marked-up rates levied on its borrowings are most favorable and benchmarked against the interest rates charged by other creditor banks.

On the other hand, the Group's investment policy is to maintain an adequate yield to match or reduce the net interest cost from its borrowings prior to deployment of funds to their intended use in operations and working capital management. However, the Group invests only in high-quality money market instruments while maintaining the necessary diversification to avoid concentration risk.

In managing interest rate risk, the Group aims to reduce the impact of short-term volatility on earnings. Over the longer term, however, permanent changes in interest rates would have an impact on profit or loss.

The management of interest rate risk is also supplemented by monitoring the sensitivity of financial instruments to various standard and non-standard interest rate scenarios. Interest rate movements affect reported equity through the retained earnings arising from increases or decreases in interest income or interest expense as well as fair value changes reported in profit or loss, if any.

The sensitivity to a reasonably possible 1% increase in the interest rates, with all other variables held constant, would have decreased the Group's profit before tax (through the impact on floating rate borrowings) by P136 and P180 in the period ending September 30, 2011 and December 31, 2010, respectively. A 1% decrease in the interest rate would have had the equal but opposite effect. There is no impact on the Group's other income.

Interest Rate Risk Table

As at September 30, 2011 and December 31, 2010, the terms and maturity profile of the interest-bearing financial instruments, together with its gross amounts, are shown in the following tables:

September 30, 2011	<1 year	1-<2 years	2-<3 years	3-<4 years	4-<5 years	>5 years	Total
Fixed rate							
Philippine peso denominated	P356	P48	P5,248	P48	P4,512	P20,000	P30,212
Interest rate	6.4% - 9.3%	6.4% - 9.3%	6.4% - 9.3%	6.4% - 9.3%	6.4% - 9.3%	6.4% - 9.3%	
Floating rate							
Philippine peso denominated	767	600	150	-	-	-	1,517
Interest rate	net 1M SDA + margin, 3-mo. Mart1/PDSTF + margin	net 1M SDA + margin	net 1M SDA + margin				
US\$ denominated (expressed in Php)	1,724	3,449	3,449	3,449	-	-	12,071
Interest rate*	3, 6 mos. Libor + margin	3, 6 mos. Libor + margin	3, 6 mos. Libor + margin	3, 6 mos. Libor + margin			
	P2,847	P4,097	P8,847	P3,497	P4,512	P20,000	P43,800

*The group reprices every 3 months but has been given an option to reprice every 6 months.

December 31, 2010	<1 year	1-<2 years	2-<3 years	3-<4 years	4-<5 years	>5 years	Total
Fixed rate							
Philippine peso denominated	P6,963	P202	P48	P5,248	P48	P24,511	P37,020
Interest rate	6.4% - 9.3%	6.4% - 9.3%	6.4% - 9.3%	6.4% - 9.3%	6.4% - 9.3%	6.4% - 9.3%	
Floating rate							
Philippine peso denominated	1,267	600	600	-	-	-	2,467
Interest rate	net 1M SDA + margin, 3-mo. Mart1/PDSTF + margin	net 1M SDA + margin	net 1M SDA + margin				
US\$ denominated (expressed in Php)	3,459	3,459	3,458	3,458	1,729	-	15,563
Interest rate	3, 6 mos. Libor + margin	3, 6 mos. Libor + margin	3, 6 mos. Libor + margin	3, 6 mos. Libor + margin	3, 6 mos. Libor + margin		
	P11,689	P4,261	P4,106	P8,706	P1,777	P24,511	P55,050

Credit Risk

Credit Risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations. In effectively managing credit risk, the Group regulates and extends credit only to qualified and credit-worthy customers and counterparties, consistent with established Group credit policies, guidelines and credit verification procedures. Request for credit facilities from trade customers undergo stages of review by Sales and Finance Divisions. Approvals, which are based on amounts of credit lines requested, are vested among line managers and top management that include the President and the Chairman. Generally, the maximum credit risk exposure of financial assets is the total carrying amount of the financial assets as shown on the face of the consolidated statement of financial position or in the notes to the consolidated financial statements, as summarized below:

	September 30, 2011	December 31, 2010
Cash in bank and cash equivalents	P17,141	P40,358
Derivative assets	138	34
Trade and other receivables-net	26,003	24,266
Due from affiliates	23,378	22,447
Noncurrent receivables	110	122
	P66,770	P87,227

The credit risk for cash in bank and cash equivalents and derivative financial instruments is considered negligible, since the counterparties are reputable entities with gain high quality external credit ratings. The credit quality of these financial assets is considered to be high grade.

In monitoring trade receivables and credit lines, the Group maintains up-to-date records where daily sales and collection transactions of all customers are recorded in real-time and month-end statements of accounts are forwarded to customers as collection medium. Finance Division's Credit Department regularly reports to management trade receivables balances (monthly) and credit utilization efficiency (semi-annually).

Collaterals. To the extent practicable, the Group also requires collateral as security for a credit facility to mitigate risk in trade receivables. Among the collaterals held are letters of credit, bank guarantees, real estate mortgages, and cash bonds valued at P3,138 and P2,736 as of September 30, 2011 and December 31, 2010, respectively. These securities may only be called on or applied upon default of customers.

Credit Risk Concentration. The Group's exposure to credit risk arises from default of counterparty. Generally, the maximum credit risk exposure of trade and other receivables is its carrying amount without considering collaterals or credit enhancements, if any. The Group has no significant concentration of credit risk since the Group deals with a large number of homogenous trade customers. The Group does not execute any guarantee in favor of any counterparty.

Credit Quality. In monitoring and controlling credit extended to counterparty, the Group adopts a comprehensive credit rating system based on financial and non-financial assessments of its customers. Financial factors being considered comprised of the financial standing of the customer while the non-financial aspects include but are not limited to the assessment of the customer's nature of the business, management profile, industry background, payment habit and both present and potential business dealings with the Group.

Class A "High Grade" are accounts with strong financial capacity and business performance and with the lowest default risk.

Class B "Moderate Grade" refer to accounts of satisfactory financial capability and credit standing but with some elements of risks where certain measure of control is necessary in order to mitigate risk of default.

Class C “Low Grade” are accounts with high probability of delinquency and default.

Liquidity Risk

Liquidity risk pertains to the risk that the Group will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash of another financial asset.

The Group’s objectives in managing its liquidity risk are as follows: a) to ensure that adequate funding is available at all times; b) to meet commitments as they arise without incurring unnecessary costs; c) to be able to access funding when needed at the least possible cost; and d) to maintain an adequate time spread of refinancing maturities.

The Group constantly monitors and manages its liquidity position, liquidity gaps or surplus on a daily basis. A committed stand-by credit facility from several local banks is also available to ensure availability of funds when necessary. The Group also uses derivative instruments such as forwards and swaps to manage liquidity.

The table below summarizes the maturity profile of the Group’s financial assets and financial liabilities based on contractual undiscounted payments used for liquidity management as of September 30, 2011 and December 31, 2010.

September 30, 2011	Carrying Amount	Contractual Cash Flow	1year or less	>1 year - 2 years	>2 year - 5 years	Over 5 years
Financial assets						
Cash and cash equivalents	P20,399	P20,399	P20,399	P-	P-	P-
Trade and other receivables	26,003	26,003	26,003	-	-	-
Due from affiliates	23,378	24,141	1,764	21,952	425	-
Derivative assets	138	138	138	-	-	-
Financial assets at FVPL	185	185	185	-	-	-
AFS financial assets	1,034	1,211	71	112	1,028	-
Noncurrent receivables	110	122	7	25	56	34
Financial liabilities						
Short-term loans	35,502	35,760	35,760	-	-	-
Accounts payable and accrued expenses (excluding taxes payable)	28,067	28,067	28,067	-	-	-
Derivative liabilities	97	97	97	-	-	-
Long-term debt (including current maturities)	43,282	59,261	5,819	6,957	24,104	22,381
Cash bonds	305	313	260	12	12	29
Cylinder deposits	346	346	-	-	-	346
Other noncurrent liabilities	51	51	-	1	32	18

December 31, 2010	Carrying Amount	Contractual Cash Flow	1year or less	>1 year - 2 years	>2 year - 5 years	Over 5 years
Financial assets						
Cash and cash equivalents	P43,984	P43,984	P43,984	P-	P-	P-
Trade and other receivables	24,266	24,266	24,266	-	-	-
Due from affiliates	22,447	22,921	907	22,014	-	-
Derivative assets	34	34	34	-	-	-
Financial assets at FVPL	193	193	193	-	-	-
AFS financial assets	1,161	1,372	250	57	1,065	-
Noncurrent receivables	122	122	-	20	65	37
Financial liabilities						
Short-term loans	32,457	32,733	32,733	-	-	-
Accounts payable and accrued expenses (excluding taxes payable)	17,375	17,375	17,375	-	-	-
Derivative liabilities	30	30	30	-	-	-
Long-term debt (including current maturities)	54,402	72,752	15,360	7,198	22,162	28,032
Cash bonds	275	284	219	26	19	20
Cylinder deposits	274	274	-	-	-	274
Other noncurrent liabilities	60	60	-	10	27	23

Commodity Price Risk

Commodity price risk is the risk that future cash flows from a financial instrument will fluctuate because of changes in market prices.

To minimize the Company's risk of potential losses due to volatility of international crude and product prices, the Group implemented commodity hedging for petroleum products. The Group enters into various commodity derivatives to (a) protect margins of MOPS (Mean of Platts of Singapore) based sales and (b) protect product inventories from downward price risk. Hedging policy includes the use of commodity price swaps, buying of put options, and use of collars and 3-way options. Decisions are guided by the conditions set and approved by the Group's management.

Other Market Price Risk

The Group's market price risk arises from its investments carried at fair value (FVPL and AFS financial assets). The Group manages its risk arising from changes in market price by monitoring the changes in the market price of the investments.

Capital Management

The Group's capital management policies and programs aim to provide an optimal capital structure that would ensure the Group's ability to continue as a going concern while at the same time provide adequate returns to the shareholders. As such, it considers the best trade-off between risks associated with debt financing and relatively higher cost of equity funds. Likewise, compliance with the debt to equity ratio covenant of bank loans has to be ensured.

An enterprise resource planning system is used to monitor and forecast the Group's overall financial position. The Group may adjust the amount of dividends paid to shareholders, issue new shares as well as increase or decrease assets and/or liabilities depending on the prevailing internal and external business conditions.

The Group monitors capital via carrying amount of equity as stated in the consolidated statement of financial position. The Group's capital for the covered reporting period is summarized in the table below:

	September 30, 2011	December 31, 2010
Total assets	P170,961	P161,816
Total liabilities	111,676	108,472
Total equity	59,285	53,344
Debt to equity ratio	1.9:1	2.0:1

There were no changes in the Group's approach to capital management during the period.

12. Financial Assets and Financial Liabilities

Date of Recognition. The Group recognizes a financial asset or a financial liability in the consolidated statements of financial position when it becomes a party to the contractual provisions of the instrument. In the case of a regular way purchase or sale of financial assets, recognition is done using settlement date accounting.

Initial Recognition of Financial Instruments. Financial instruments are recognized initially at fair value of the consideration given (in case of an asset) or received (in case of a liability). The initial measurement of financial instruments, except for those designated at fair value through profit or loss (FVPL), includes transaction costs.

The Group classifies its financial assets in the following categories: held-to-maturity (HTM) investments, available for sale (AFS) financial assets, financial assets at FVPL and loans and receivables. The Group classifies its financial liabilities as either FVPL or other financial liabilities. The classification depends on the purpose for which the investments are acquired and whether they are quoted in an active market. Management determines the classification of its financial assets and financial liabilities at initial recognition and, where allowed and appropriate, re-evaluates such designation at every reporting date.

Determination of Fair Value. The fair value for financial instruments traded in active markets at the reporting date is based on their quoted market price or dealer price quotations (bid price for long positions and ask price for short positions), without any deduction for transaction costs. When current bid and ask prices are not available, the price of the most recent transaction provides evidence of the current fair value as long as there is no significant change in economic circumstances since the time of the transaction.

For all other financial instruments not listed in an active market, the fair value is determined by using appropriate valuation techniques. Valuation techniques include the discounted cash flow method, comparison to similar instruments for which market observable prices exist, options pricing models and other relevant valuation models.

'Day 1' Profit. Where the transaction price in a non-active market is different from the fair value of the other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable market, the Group recognizes the difference between the transaction price and fair value (a 'Day 1' profit) in profit or loss unless it qualifies for recognition as some other type of asset. In cases where use is made of data which are not observable, the difference between the transaction price and model value is only recognized in the consolidated statement of income when the inputs become observable or when the instrument is derecognized. For each transaction, the Group determines the appropriate method of recognizing the 'Day 1' profit amount.

Financial Assets

Financial Assets at FVPL. A financial asset is classified at FVPL if it is classified as held for trading or is designated as such upon initial recognition. Financial assets are designated at FVPL if the Group manages such investments and makes purchase and sale decisions based on their fair value in accordance with the Group's documented risk management or investment strategy. Derivative instruments (including embedded derivatives), except those covered by hedge accounting relationships, are classified under this category.

Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term.

Financial assets may be designated by management at initial recognition as at FVPL, when any of the following criteria is met:

- the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or recognizing gains or losses on a different basis;
- the assets are part of a group of financial assets which are managed and their performances are evaluated on a fair value basis, in accordance with a documented risk management or investment strategy; or

- the financial instrument contains an embedded derivative, unless the embedded derivative does not significantly modify the cash flows or it is clear, with little or no analysis, that it would not be separately recognized.

The Group uses commodity price swaps to protect its margin on petroleum products from potential price volatility of international crude and product prices. It also enters into short-term forward currency contracts to hedge its currency exposure on crude oil importations. In addition, the Company has identified and bifurcated embedded foreign currency derivatives from certain non-financial contracts.

Derivatives instruments are initially recognized at fair value on the date in which a derivative transaction is entered into or bifurcated, and are subsequently re-measured at fair value. Derivatives are presented in the separate statement of financial position as assets when the fair value is positive and as liabilities when the fair value is negative. Gains and losses from changes in fair value of these derivatives are recognized under the caption marked-to-market gain (losses) included as part of "Other Income (Expenses)" in the separate statement of comprehensive income.

The fair values of freestanding and bifurcated forward currency transactions are calculated by reference to current exchange rates for contracts with similar maturity profiles. The fair values of commodity swaps are determined based on quotes obtained from counterparty banks.

The Group's financial assets at FVPL and derivative assets are included in this category.

The carrying values of financial assets under this category amounted to P323, P195 and P227 as of September and June 30, 2011 and December 31, 2010, respectively.

Loans and Receivables. Loans and receivables are non-derivative financial assets with fixed or determinable payments and maturities that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not designated as AFS financial assets or financial assets at FVPL.

Subsequent to initial measurement, loans and receivables are carried at amortized cost using the effective interest rate method, less any impairment in value. Any interest earned on loans and receivables shall be recognized as part of "Interest income" in profit and loss on an accrual basis. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees that are integral part of the effective interest rate. The periodic amortization is also included as part of "Interest income" in the consolidated statements of income. Gains or losses are recognized in profit or loss when loans and receivables are derecognized or impaired, as well as through the amortization process.

Cash includes cash on hand and in banks which are stated at face value. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

The Group's cash and cash equivalents, trade and other receivables, due from affiliates and noncurrent receivables are included in this category.

The combined carrying values of financial assets under this category amounted to P69,890, P69,031 and P90,819 as of September and June 30, 2011 and December 31, 2010, respectively.

HTM Investments. HTM investments are quoted non-derivative financial assets with fixed or determinable payments and fixed maturities for which the Group's management has the positive intention and ability to hold to maturity. Where the Group sells other than an insignificant amount of HTM investments, the entire category would be tainted and reclassified as AFS financial assets. After initial measurement, these investments are measured at amortized cost using the effective interest rate method, less impairment in value. Any interest earned on the HTM investments shall be recognized as part of "Interest income" in the consolidated statements of income on an accrual basis. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees that are integral part of the effective interest rate. The periodic amortization is also included as part of "Interest income" in the consolidated statements of income. Gains or losses are recognized in profit or loss when the HTM investments are derecognized or impaired, as well as through the amortization process.

As of September and June 30, 2011 and December 31, 2010, the Group has no investments accounted under this category.

AFS Financial Assets. AFS financial assets are non-derivative financial assets that are either designated in this category or not classified in any of the other financial asset categories. Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses and foreign currency differences on AFS debt instruments, are recognized in other comprehensive income and presented in the "Other reserves" in equity. The effective yield component of AFS debt securities, as well as the impact of restatement on foreign currency-denominated AFS investment securities, is reported as part of "Interest income" in the consolidated statement of income. The unrealized gains and losses arising from the changes in fair value of AFS financial assets, net of tax, are excluded from profit and loss and are recognized as other comprehensive income reported in the consolidated statement of comprehensive income and in the consolidated statement of changes in equity under "Other Reserves" account. Any interest earned on AFS debt securities shall be recognized as part of "Interest income" in the consolidated statement of income on an accrual basis. Dividends earned on holding AFS equity securities are recognized as "Dividend income" when the right of collection has been established. When individual AFS financial assets are either derecognized or impaired, the related accumulated unrealized gains or losses previously reported equity are transferred to and recognized in profit or loss.

Where the Group holds more than one investment in the same security, these are deemed to be disposed on a first-in, first-out basis. Interest and dividends earned on holding AFS financial assets are recognized in "Other Income" account in the consolidated statement of income when the right to receive payment has been established. The losses arising from impairment of such investments are recognized as impairment losses in profit or loss.

AFS financial assets also include unquoted equity instruments with fair values which cannot be reliably determined. These instruments are carried at cost less impairment in value, if any. The Group's investments in debt are classified under this category.

The carrying values of financial assets under this category amounted to P1,034, P1,186 and P1,161 as of September and June 30, 2011 and December 31, 2010, respectively.

Financial Liabilities

Financial Liabilities at FVPL. Financial liabilities are classified under this category through the fair value option. Derivative instruments (including embedded derivatives) with negative fair values are also classified under this category.

The Group carries financial liabilities at FVPL using their fair values and reports fair value changes in the consolidated statement of income.

The carrying values of financial liabilities under this category amounted to P97, P6 and P30 as of September and June 30, 2011 and December 31, 2010, respectively.

Other Financial Liabilities. This category pertains to financial liabilities that are not designated or classified as at FVPL. After initial measurement, other financial liabilities are carried at amortized cost using the effective interest rate method. Amortized cost is calculated by taking into account any premium or discount and any directly attributable transaction costs that are considered an integral part of the effective interest rate of the liability.

Included in this category are the Group's liabilities arising from its short term loans, liabilities for crude oil and petroleum product importation, trade and other payables, long-term debt, cash bond, cylinder deposits and other non-current liabilities.

The combined carrying values of financial liabilities under this category amounted to P107,553, P99,415 and P104,843 as of September and June 30, 2011 and December 31, 2010, respectively.

Debt Issue Costs

Debt issue costs are considered as an adjustment to the effective yield of the related debt and are deferred and amortized using the effective interest rate method. When a loan is paid, the related unamortized debt issue costs at the date of repayment are charged against current operations.

Embedded Derivatives

The Group assesses whether embedded derivatives are required to be separated from host contracts when the Group becomes a party to the contract.

An embedded derivative is separated from the host contract and accounted for as a derivative if all of the following conditions are met: a) the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract; b) a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and c) the hybrid or combined instrument is not recognized at FVPL. Reassessment only occurs if there is a change in the terms of the contract that significantly modifies the cash flows that would otherwise be required.

Derecognition of Financial Assets and Financial Liabilities

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

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

When the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognized to the extent of the Group’s continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Financial Liabilities. A financial liability is derecognized when the obligation under the liability is discharged, cancelled or expired. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability. The difference in the respective carrying amounts is recognized in profit or loss.

Impairment of Financial Assets

The Group assesses at reporting date whether a financial asset or group of financial assets is impaired.

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

Assets Carried at Amortized Cost. For assets carried at amortized cost such as loans and receivables, the Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If no objective evidence of impairment has been identified for a particular financial asset that was individually assessed, the Group includes the asset as part of a group of financial assets pooled according to their credit risk characteristics and collectively assesses the group for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognized are not included in the collective impairment assessment.

Evidence of impairment for specific impairment purposes may include indications that the borrower or a group of borrowers is experiencing financial difficulty, default or delinquency in principal or interest payments, or may enter into bankruptcy or other form of financial reorganization intended to alleviate the financial condition of the borrower. For collective impairment purposes, evidence of impairment may include observable data on existing economic conditions or industry-wide developments indicating that there is a measurable decrease in the estimated future cash flows of the related assets.

If there is objective evidence of impairment, the amount of loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses) discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition). Time value is generally not considered when the effect of discounting the cash flows is not material. If a loan or receivable has a variable rate, the discount rate for measuring any impairment loss is the current effective interest rate, adjusted for the original credit risk premium. For collective impairment purposes, impairment loss is computed based on their respective default and historical loss experience.

The carrying amount of the asset shall be reduced either directly or through use of an allowance account. The impairment loss for the period shall be recognized in profit or loss. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed. Any subsequent reversal of an impairment loss is recognized in profit or loss, to the extent that the carrying amount of the asset does not exceed its amortized cost at the reversal date.

AFS Financial Assets. If an AFS financial asset is impaired, an amount comprising the difference between the cost (net of any principal payment and amortization) and its current fair value, less any impairment loss on that financial asset previously recognized in profit or loss, is transferred from equity to profit or loss. Reversals in respect of equity instruments classified as AFS financial assets are not recognized in profit or loss. Reversals of impairment losses on debt instruments are recognized in profit or loss, if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognized in profit or loss.

In the case of an unquoted equity instrument or of a derivative asset linked to and must be settled by delivery of an unquoted equity instrument, for which its fair value cannot be reliably measured, the amount of impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows from the asset discounted using its historical effective rate of return on the asset.

Classification of Financial Instruments Between Debt and Equity

From the perspective of the issuer, a financial instrument is classified as debt instrument if it provides for a contractual obligation to:

- deliver cash or another financial asset to another entity;
- exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavorable to the Group; or
- satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity shares.

If the Group does not have an unconditional right to avoid delivering cash or another financial asset to settle its contractual obligation, the obligation meets the definition of a financial liability.

Offsetting Financial Instruments

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

The table below presents a comparison by category of carrying amounts and fair values of the Group's financial instruments as of September 30, 2011 December 31, 2010:

	September 30, 2011		December 31, 2010	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial assets (FA):				
Cash and cash equivalents	P20,399	P20,399	P43,984	P43,984
Trade and other receivables	26,003	26,003	24,266	24,266
Due from affiliates	23,378	23,378	22,447	22,447
Long-term receivables	110	110	122	122
Loans and receivables	69,890	69,890	90,819	90,819
AFS financial assets	1,034	1,034	1,161	1,161
Financial assets at FVPL	185	185	193	193
Derivative assets	138	138	34	34
FA at FVPL	323	323	227	227
Total financial assets	P71,247	P71,247	P92,207	P92,207
Financial liabilities (FL):				
Short-term loans	P35,502	P35,502	P32,457	P32,457
Liabilities for crude oil and petroleum product importation	21,872	21,872	11,194	11,194
Trade and other payables (excluding specific taxes and other taxes payable)	6,195	6,195	6,181	6,181
Long-term debt including current portion	43,282	43,282	54,402	54,402
Cash bonds	305	305	275	275
Cylinder deposits	346	346	274	274
Other noncurrent liabilities	51	51	60	60
FL at amortized cost	107,553	107,553	104,843	104,843
Derivative liabilities	97	97	30	30
Total financial liabilities	P107,650	P107,650	P104,873	P104,873

The following methods and assumptions are used to estimate the fair value of each class of financial instruments and when it is practicable to estimate such value:

Cash and Cash Equivalents, Trade and Other Receivables and Noncurrent Receivables. The carrying amount of cash and cash equivalents and receivables approximates fair value primarily due to the relatively short-term maturities of these financial instruments. In the case of long-term receivables, the fair value is based on the present value of expected future cash flows using the applicable discount rates based on current market rates of identical or similar quoted instruments.

Derivatives. The fair values of freestanding and bifurcated forward currency transactions are calculated by reference to current forward exchange rates for contracts with similar maturity profiles. Mark-to-market valuation in 2011 and 2010 of commodity hedges were based on the forecasted crude and product prices by Mitsui & Co. Commodity Risk Management Ltd. (MCRM), an independent trading group.

Financial Assets at FVPL and AFS Financial Assets. The fair values of publicly traded instruments and similar investments are based on quoted market prices in an active market. For debt instruments with no quoted market prices, a reasonable estimate of their fair values is calculated based on the expected cash flows from the instruments discounted using the applicable discount rates of comparable instruments quoted in active markets. Unquoted equity securities are carried at cost less impairment.

Long-term Debt - Floating Rate. Variable rate loans are repriced every three month, the carrying value approximates its fair value because of recent regular repricing based on current market rates.

Cash Bonds. Fair value is estimated as the present value of all future cash flows discounted using the market rates for similar types of instruments.

Derivative Financial Instruments

The Group's derivative financial instruments according to the type of financial risk being managed and the details of freestanding and embedded derivative financial instruments are discussed below.

The Group enters into various commodity derivative contracts to manage its exposure on commodity price risk. The portfolio is a mixture of instruments including forwards, swaps and options covering the Group's requirements on crude oil and finished products. These include freestanding and embedded derivatives found in host contracts, which are not designated as accounting hedges. Changes in fair value of these instruments are recognized directly in profit or loss.

The Group's derivative financial instruments according to the type of financial risk being managed are discussed below.

Freestanding Derivatives

Freestanding derivatives consist of commodity derivatives and currency derivatives entered into by the Group.

Currency Forwards

As of September and June 30, 2011 and December 31, 2010, the Company has outstanding foreign currency forward contracts with aggregate notional amount of US\$182, US\$155 and US\$15, respectively with various maturities up to December 2011. As of September and June 30, 2011 and December 31, 2010, the net positive (negative) fair value of these currency forwards amounted to P138, (P1) and nil, respectively.

Currency Options

The Company has no outstanding currency option agreements as of September and June 30, 2011 and December 31, 2010.

Commodity Swaps

The Company has outstanding swap agreements covering its fuel and crude requirements, with various maturities in 2011. Under the agreement, payment is made either by the Company or its counterparty for the difference between the agreed fixed price of fuels and crude and the price based on the relevant price index. The outstanding equivalent notional quantities covered by the commodity swaps as of September and June 30, 2011 and December 31, 2010 were 3.0 MMB, 5.7 MMB and 1.5 MMB, respectively. As of September and June 30, 2011 and December 31, 2010, the total mark-to-market gain (loss) of these swaps amounted to (P267), (P128) and P32, respectively.

Commodity Options

The Company has outstanding commodity option agreements as of September and June 30, 2011 and December 31, 2010 with notional quantities totaling 2.4 MMB, 0.9 MMB and 2.8 MMB, respectively. The respective mark-to-market gain (loss) of these hedges amounted to P634, P102 and P234 as of September and June 30, 2011 and December 31, 2010, respectively.

Embedded Derivatives

The Group assesses whether embedded derivatives are required to be separated from the host contracts when the Group becomes a party to the contract.

An embedded derivative is separated from the host contract and accounted for as a derivative if all of the following conditions are met: a) the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract; b) a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and c) the hybrid or combined instrument is not recognized at FVPL. Reassessment only occurs if there is a change in the terms of the contract that significantly modifies the cash flows that would otherwise be required.

The Group's embedded derivatives include currency derivatives (forwards and options) embedded in non-financial contracts.

Embedded Currency Forwards

As of September and June 30, 2011 and December 31, 2010, the total outstanding notional amount of currency forwards embedded in non-financial contracts amounted to US\$71, US\$4 and US\$151, respectively. These non-financial contracts consist mainly of foreign currency-denominated service contracts, purchase orders and sales agreements. The embedded forwards are not clearly and closely related to their respective host contracts. As of September and June 30, 2011 and December 31, 2010, the net positive (negative) fair value of these embedded currency forwards amounted to (P97), (P0.7) and (P4), respectively.

For the periods ended September 30, 2011 and 2010 and June 30, 2011 and 2010, the Group recognized marked-to-market gains from embedded derivatives amounting to P229, P189, P68 and P85, respectively.

Fair Value Hierarchy

In accordance with PFRS 7, financial assets and liabilities measured at fair value in the statement of financial position are categorized in accordance with the fair value hierarchy. This hierarchy groups financial assets and liabilities into three levels based on the significance of inputs used in measuring the fair value of the financial assets and liabilities.

The table below analyzes financial instruments carried at fair value, by valuation method as of September 30, 2011 and December 31, 2010. The different levels have been defined as follows:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3: inputs for the asset or liability that are not based on observable market data.

September 30, 2011	Level 1	Level 2	Total
Financial Assets			
Financial assets at FVPL	P185	P-	P185
Derivative assets	-	138	138
AFS financial assets	-	1,034	1,034
Financial Liabilities			
Derivative liabilities		97	97
December 31, 2010			
Financial Assets			
Financial assets at FVPL	P193	P -	P193
Derivative assets	-	34	34
AFS financial assets	-	1,161	1,161
Financial Liabilities			
Derivative liabilities		30	30

As of September 30, 2011 and December 31, 2010, the Group has no financial instruments valued based on Level 3. During the year, there were no transfers between Level 1 and Level 2 fair value measurements, and no transfers into and out of Level 3 fair value measurements.

13. Events after the Reporting Date

On October 7, 2011, we disclosed that the Philippine Rating Services Corporation (PhilRatings) maintained Petron Corporation's corporate credit rating of PRS Aaa (corp.) on the Company's overall capacity to service its maturing obligations within a period of one year. A PRS Aaa credit rating is the highest score on PhilRatings' issuer/corporate credit rating scale, which is given to companies exhibiting a strong capacity to meet its financial commitments relative to that of other Philippine corporate.

On October 21, 2011, the BOD declared a cash dividend of P2.382/share to all preferred stockholders for the last quarter of 2011 and the first quarter of 2012 with the following record and payment dates:

Period	Record Date	Payment Date
4 th Quarter 2011	November 16, 2011	December 5, 2011
1 st Quarter 2012	February 21, 2012	March 5, 2012

On October 28, 2011, the Parent Company raised P3,600 from the sale of fixed-rate corporate notes with ING Bank N.V.'s Manila Branch as arranger and bookrunner.

14. Other Matters

- a. There were no unusual items as to nature and amount affecting assets, liabilities, equity, net income or cash flows, except those stated in Management's Discussion and Analysis of Financial Position and Performance.
- b. There were no seasonal aspects that had a material effect on the financial position or financial performance of the Group.
- c. There were no material off-statements of financial position transactions, arrangements, obligations (including contingent obligations), and other relationship of the Group with unconsolidated entities or other persons created during the reporting period, except for the outstanding derivative transactions entered by the Group as of and for the period ended September 30, 2011.

- d. Known trends, demands, commitments, events or uncertainties that will have a material impact on the Group's liquidity.

Gross Domestic Product (GDP)

After growing robustly in 2010 due to high election spending, the domestic economy slowed down in 2011. GDP in the 2Q11 expanded merely by 3.4% after the strong 8.9% growth in the same quarter last year. The slowdown was due to the rising commodity prices, particularly of fuels, lower growth of remittances due to the turmoil in the Middle East and North Africa and the tragedy in Japan, lower foreign direct investments and exports, and large decline in government spending. Government underspending was observed as the current administration has become more stringent in releasing funds for infrastructure and other social projects to avoid corruption and reduce budget deficit.

91-Day Treasury-Bill Rate

91-day T-bills averaged 1.6% in the first three quarters of 2011, substantially lower than the same period last year of 3.9% and FY 2010 average of 3.7%. Interest rates in 2011 have been low due to the sufficient liquidity in the domestic financial markets.

Peso-Dollar Exchange Rate

The local currency sustained its strength and averaged P43.3/\$ in the first three quarters of 2011 from 2010 FY average of P45.1/\$ and 3-quarter average of P45.6/\$ in 2010. The continuously growing OFW remittances, and strong portfolio investments contributed to the peso's appreciation. The Dollar's general weakness due to the US' fragile economy also benefitted other currencies like the peso.

Inflation

Inflation averaged 4.3% in the first nine months of 2011 (based on 2000 prices), slightly higher from 4.1% average in the same period last year and from FY 2010's 3.8% average. Prices of fuel, light, water, and services have been higher this year compared to 2010. YTD September average inflation remains within the government's target inflation of 3-5% for FY 2011.

Dubai price

Dubai crude averaged \$106.2/bbl as of YTD September 2011, a large leap from the \$76.0/bbl average in the same period last year and \$77.1/bbl FY average in 2010. The surge of crude prices was triggered by the heightened turmoil in the oil-exporting regions Middle East and North Africa especially during the 1H, disrupting some supply of crude. Crude prices were also boosted by high investment in the crude futures market due to the weakness of the dollar, and the strength of the equities market.

Industry Oil Demand

Data from DOE shows that as of August 2011, total oil industry demand dropped by 5.9% from 308.6 MBD in the same period last year to only 290.4 MBD this year. The rising prices of fuels in 2011 affected industry demand. Motorists, industries, and households tend to conserve fuel consumption during times of high prices.

Tight Industry Competition

Competition remains stiff with the new players implementing different marketing strategies and aggressively expanding. As of YTD August 2011, the new players (excluding direct imports) have collectively cornered around 24.6% of the total oil market. Collectively, the new players are leading the LPG market segment with 45.0% market share.

Updates on 2011 Capital Program

The 2011 capital program endorsed last December 2010 is P88.6 billion. Of this amount P23.7 billion has already been approved and includes partial funding for the refinery expansion project, service station network expansion, consumer facilities, asphalt facilities, maintenance and other efficiency projects.

- e. Known trends, events or uncertainties that have had or that are reasonably expected to have a favorable or unfavorable impact on net sales or revenues or income from continuing operation.

Illegal Trading Practices

Cases of smuggling and illegal trading (e.g. “bote-bote” retailing, illegal refilling) continue to be a concern. These illegal practices have resulted in unfair competition among players.

Existing or Probable Government Regulation

EO 890: Removing Import Duties on All Crude and Refined Petroleum Products. After the ASEAN Trade in Goods Agreement (ATIGA) was implemented starting 2010, tariff rate structure in the oil industry was distorted with crude and product imports from ASEAN countries enjoying zero tariff while crude and product imports from outside the ASEAN are levied 3%. To level the playing field, Petron filed a petition with the Tariff Commission to apply the same tariff duty on crude and petroleum product imports, regardless of source. In June 2010, the government approved Petron’s petition and issued Executive Order 890 which eliminates import duties on all crude and petroleum products regardless of source. The reduction of duties took effect on July 4, 2010.

Biofuels Act of 2006. The Biofuels Act of 2006 mandates that ethanol comprise 5% of total gasoline volumes, and diesels contain 2% CME (cocomethyl ester). By 2011, all gasoline grades should contain 10% ethanol.

The Department of Energy circular (DC 2011-02-0001) signed February 6, 2011 further elaborates that the 10% ethanol blend shall be mandatory beginning August 26, 2011, subject to exempt gasoline grades. These exempt gasoline grades are regular gasoline with RON 81 for use of off-road engines, farm equipment and small motorized bancas; regular gasoline with RON 87 for use of motorcycles and premium plus gasoline with minimum RON of 97. By February 6, 2012 or upon full implementation, all gasoline grades, no exemptions, shall be required to contain 10% ethanol. Full implementation will be subject to review 30 days before February 6, 2012 to determine its economic viability given availability of supply and ethanol prices.

To produce compliant fuels, the Company invested in CME (coco methyl ester) injection systems at the refinery and depots. Prior to the mandatory blending of ethanol into gasoline by 2009, the Company already started selling ethanol blended gasoline in selected service stations in Metro Manila in May 2008.

Renewable Energy Act of 2008. The Renewable Energy Act signed in December 2008 aims to promote development and commercialization of renewable and environment-friendly energy resources (e.g. biomass, solar, wind) through various tax incentives. Renewable energy developers will be given 7-year income tax holiday, power generated from these sources will be VAT-exempt, and facilities to be used or imported will also have tax incentives.

Laws on Oil Pollution. To address issues on marine pollution and oil spillage, the MARINA mandated the use of double-hull vessels for transporting black products beginning end-2008 and by January 2012 for white products.

Petron has been using double-hull vessels in transporting all black products and some white products already.

Clean Air Act. Petron invested in a Gasoil Hydrotreater Plant and in an Isomerization Plant to enable it to produce diesel and gasoline compliant with the standards set by law.

Liquefied Petroleum Gas (LPG) Bill. The LPG Act of 2009 aims to ensure safe practices and quality standards and mitigate unfair competition in the LPG sector. LPG cylinder seal suppliers must obtain a license and certification of quality, health and safety from the Department of Energy before they are allowed to operate. LPG cylinder requalifiers, repairers and scrapping centers, will also have to obtain a license from the Department of Trade and Industry. The Bill also imposes penalties on underfilling, underdelivering, illegal refilling and storage, sale or distribution of LPG-filled cylinders without seals, illegal possession of LPG cylinder seal, hoarding, and importation of used or second-hand LPG cylinders, refusal of inspection, and non-compliance to standards.

- f. Events that will trigger direct or contingent financial obligation that is material to the company, including any default or acceleration of an obligation.

Tax Credit Certificates Related Cases

In 1998, Petron contested before the Court of Tax Appeals (CTA), the collection by the Bureau of Internal Revenue (BIR) of deficiency taxes arising from the company's acceptance and use of Tax Credit Certificates (TCCs) worth P659 million from 1993-1997. The CTA ruled in favor of Petron. The BIR then appealed the case to the Court of Appeals (CA) after which the CA issued a resolution suspending decision on the case until the termination of the Department of Finance (DOF) investigation. Petron filed a motion for reconsideration which remains pending at the moment.

In May 2002, the BIR issued a collection letter for deficiency taxes of P254 million plus interest and charges for the years 1995-1998, as a result of the cancellation of the Tax Debit Memos and TCCs by the DOF Center ExCom. Petron elevated the protest to the CTA. The Second Division CTA denied Petron's Petition for Review for lack of merit. Petron then appealed the case with the CTA En Banc. On December 3, 2008, the CTA En Banc promulgated a decision reversing the unfavorable decision of the CTA 2nd Division. The CIR filed a Petition for Review with the Supreme Court where the case remains submitted for resolution.

Pandacan Terminal Operations

Citing concerns for safety, security and health, the City of Manila passed City Ordinance No. 8027 which reclassified the Pandacan Terminal from industrial to commercial. Petron, together with the other oil companies asked the Supreme Court to change the ruling since the Comprehensive Land Use Plan and Zoning Ordinance (Ordinance No.8119) repealed the Manila Ordinance No. 8027. Ordinance No. 8119 gives Petron a seven-year grace period to continue its operations in the Pandacan Terminal. In February 2008, the Supreme Court denied the oil company's motion for reconsideration and declared Manila Ordinance No. 8027 valid and applicable to all oil terminals. The Court directed the oil companies to submit their relocation plans to the RTC within 90 days to determine the reasonableness of the time frame for relocation. In May 2008, Petron, Shell and Chevron submitted their Comprehensive Relocation Plan in compliance with the February Resolution. The Pandacan Terminal is strategically significant since it serves about 40% of the company's refinery output and 100% of the company's lubricants, greases and oxidized asphalt.

On May 28, 2009, Mayor Alfredo Lim of Manila approved and signed proposed Ordinance 7177 (which became Ordinance No. 8187) repealing Ordinance No. 8027 and 8119 and allowing the continued stay of the oil depots at Pandacan. Mayor Lim was reelected Mayor of Manila in the May 10, 2010 election.

On June 1, 2009, Social Justice Society officers filed a petition for prohibition against Mayor Lim before the Supreme Court, seeking the nullification of Ordinance 8187. On June 5, 2009, former Mayor Lito Atienza filed his own petition with the Supreme Court seeking to stop the implementation of Ordinance 8187. The Court has ordered the City to file its comment but the Court did not issue a temporary restraining order. The City filed its comment on August 13, 2009.

The main storage facility of Petron is located at the Pandacan Terminal. Approximately 40% of Petron's total sales volume is moved through Pandacan. To ensure steady supply and in order to mitigate the risks at the Pandacan Terminal, the company's nearby depots in Navotas, Metro Manila and in Rosario, Cavite can also distribute products to the areas being served by the Pandacan terminal.

Petron believes that, given the prevailing law and existing jurisprudence, the Supreme Court will uphold the validity of Ordinance No. 8187.

As stated in the papers (Philippine Daily Inquirer, June 28, 2010 issue), and as confirmed during the management meeting in 2010, Petron is looking at the Manila North Harbor as a possible location for its depot that will replace its facilities at the Pandacan Terminal. This is just one of the sites that Petron is looking at for the transfer, should it be forced to move out of Pandacan. According to SMC President and COO, Mr. Ramon Ang, moving Petron's depot facilities to the North Harbor would reduce the company's handling costs by as much as 80%, which may, in turn, result in lower pump prices. Mr. Ang explained that bringing oil to Pandacan can only be done with barges as a result of the Pasig River's shallow draught of only 3 meters. North Harbor, on the other hand, has deep-water facilities which tankers can use directly.

Based on SEC FORM 17-A filings of Petron, the company has filed its Manifestation on November 30, 2010 to inform the Supreme Court that it has decided to cease operation of its petroleum product storage facilities in Pandacan, Manila within 5 years or not later than January 2016 due to environmental issues and issues on the location of the terminal.

Petron's operations at the Pandacan Terminal are being scaled down in line with its commitment to have minimal operations there by 2014. The company is already building storage capacities in alternative sites. These storage facilities will support the expected growth in demand for petroleum products outside of Metro Manila and the increased production under RMP-2.

Guimaras Case

Complaints for Violation of Sec. 28, Paragraph 5 in relation to Section 4 of the Philippine Clean Water Act of 2004 (RA 9275) were filed against Messrs. Nicasio I. Alcantara and Khalid D. Al-Faddagh, Petron's former Chairman and President, respectively, and the Captain and owner of M/T Solar 1 on June 17, 2009, as a result of the oil slick from the said vessel which sank on August 11, 2006.

The Respondents denied the allegations imputed against them, as the same accusation was already resolved and dismissed by the Provincial Prosecutor's Office of Guimaras in a Resolution dated March 2, 2007.

On July 14, 2011, the Provincial Prosecutor's Office of Guimaras issued a Joint Resolution finding probable cause to indict the owner and the Captain of M/T Solar 1 and Messrs. Alcantara and Mr. Faddagh for Violation of Section 28, Paragraph 5 in relation to Section 4 of the Clean Water Act of 2004.

Messrs. Alcantara and Faddagh filed their Motion for Reconsideration with the Provincial Prosecutor's Office of Guimaras on August 1, 2011. The Complainants filed their Reply and Supplemental Comment while Messrs. Alcantara and Faddagh countered this with a Reply with Motion for Inhibition. Both Motions for Reconsideration and Inhibition have not been resolved.

Petron did not hire or engaged the services of the Captain of M/T Solar 1 contrary to the finding contained in the Marine Accident Inquiry Report of the Special Marine Inquiry Board relied upon by the Prosecutor's Office. In addition, under Republic Act No. 9483, otherwise known as "The Oil Pollution Compensation Act of 2007", it is the owner of the vessel, not the charterer, that is liable for any oil spill or pollution damage that may result from the operation of the said vessel.



Petron Corporation and Subsidiaries
Trade and Other Receivables
September 30, 2011
(Amounts in Millions of Pesos)

Breakdown:

Accounts Receivable - Trade	P 17,091
Accounts Receivable - Non-Trade	8,912
Total Accounts Receivable	<u>26,003</u>

AGING OF TRADE ACCOUNTS RECEIVABLES

Receivables	1-30 days	P 14,465
	31-60 days	2,339
	61-90 days	617
	Over 90 days	<u>721</u>
Total		18,142
Allowance for doubtful accounts		<u>1,051</u>
Accounts Receivable - Trade		<u>P 17,091</u>

Interim Financial Report as of September 30, 2011

Management's Discussion and Analysis of Financial Position and Performance

Financial Performance

2011 vs 2010

For the third quarter of 2011, Petron reported a net income of **₱ 1.56 billion**. Gross revenues increased to **₱ 67.03 billion** as a result of high fuel prices. Compared to the same period in 2010, both sales volume and net income were lower by 7% and 14%, respectively.

The company noted a significant drop in earnings during the third quarter when compared to the previous two quarters. The decline was caused by weak demand brought about by higher fuel prices and more aggressive competition particularly in the retail and industrial sectors.

(In Million Pesos)	2011	2010	Variance- Fav (Unfav)	
			Amt	%
Sales	201,929	169,798	32,131	19
Cost of Goods Sold	183,638	156,479	(27,159)	(17)
Gross Margin	18,291	13,319	4,972	37
Selling and Administrative Expenses	5,177	4,414	(763)	(17)
Non-operating Charges	3,001	1,834	(1,167)	(63)
Net Income	7,600	5,347	2,253	42
EBITDA	15,727	11,234	4,493	40
Sales Volume (MB)	34,284	35,838	(1,554)	(4)
Earnings per Share	0.73	0.52	0.21	40
Return on Sales (%)	3.8	3.1	0.7	23

Overall, for the first nine months of 2011, revenues surged to **₱ 201.93 billion** while net earnings amounted to **₱ 7.60 billion**. Higher income can be attributed to the growth of petrochemical sales which contributed about **₱ 2.5 billion** earnings.

With the improved bottom line, **earnings before interest, taxes, depreciation and amortization (EBITDA)** of **₱ 15.73 billion** also topped the **₱ 11.23 billion** level a year earlier.

Earnings per share increased by 40% to **₱ 0.73** from **₱ 0.52** of the previous year while **return on sales** grew from 3.1% to **3.8%**.

Major contributory factors are the following:

Gross margin (GM) rose to **₱ 18.29 billion** from previous year's **₱ 13.32 billion**. The following account for the variance in gross margin:

- ◆ **Sales volume as of September 2011** ended lower at **34.3MMB** compared to last year's 35.8MMB as current level of prices resulted in a 7% (2.16MMB) contraction in the domestic market. Meanwhile, exports improved by 17% (0.62MMB). The slowdown in local sales came from Diesel (1,233MB) and Fuel Oil (1,774MB) mitigated by the growth in LPG and Jet (880MB).
- ◆ **Net sales revenue** grew by 19% to **₱ 201.93 billion** from ₱ 169.80 billion the year before essentially due to the hike in average selling price per liter (2011: ₱ 36.13 vs. 2010: ₱ 29.08) prompted by the 36% spike in regional MOPS prices (2011 Ave - US\$122.64/bbl vs. 2010 Ave - US\$90.48/bbl), tempered by the ₱ 2.33 average appreciation of the peso versus the US dollar.
- ◆ **Cost of Goods Sold (CGS)** went up to **₱ 183.64 billion** from last year's ₱ 156.48 billion as the average cost per liter increased by 22% (2011: ₱ 32.88 vs 2010: ₱ 26.94). Higher cost per liter was principally due to the 31% escalation in landed cost of crude that formed part of the total cost of goods sold (2011: US\$ 104.08/bbl vs 2010: US\$ 79.37).
- ◆ **Refinery Operating Expenses** which formed part of CGS rose to **₱ 4.12 billion** from ₱ 3.71 billion during the same period last year. This was attributed to increased power consumption due to higher cost per kilowatt-hour (2011: ₱ 6.31 vs 2010: ₱ 4.65) and higher maintenance and repairs on several facilities. Employee costs also moved up due largely to additional manpower complement and payment of signing bonus to rank-and-file employees.
- ◆ **Selling and Administrative Expenses** of **₱ 5.18 billion** exceeded last year's ₱ 4.41 billion expenditures as newly built service stations resulted in increased rent and depreciation. Materials and supplies also went up due to acquisition of LPG cylinders while aggressive promotional activities accounted for higher advertising expenses. With the surge in operating expenses despite the drop in volume, **opex per liter** of volume sold grew from ₱ 0.77 last year to **₱ 0.95** this year.
- ◆ **Net Financing Costs and Other Charges** rose to **₱ 3.00 billion** from the ₱ 1.84 billion level as of September 2010. The increase in average borrowing level and rate (2011: ₱ 77.00 billion @ 5.8% vs. 2010: ₱ 59.00 billion @ 5.3%) resulted to higher interest expense. Losses from US-dollar denominated transactions also contributed to the increment. The increase was partly offset by the interest earned from advances to Petron Corporation Employee Retirement Plan, marked-to-market gains on Embedded Derivatives, and commodity hedging gains.

2010 vs 2009

(In Million Pesos)	2010	2009	Variance- Fav (Unfav)	
			Amt	%
Sales	169,798	123,635	46,163	37
Cost of Goods Sold	156,479	111,620	(44,859)	(40)
Gross Margin	13,319	12,015	1,304	10
Selling and Administrative Expenses	4,414	4,116	(298)	(7)
Non-operating Charges	1,835	3,261	1,426	46
Net Income	5,347	3,366	1,981	58
EBITDA	11,234	10,394	840	8
Sales Volume (MB)	35,838	32,324	3,514	10
Earnings per Share	0.57	0.36	0.21	58
Return on Sales (%)	3.1	2.7	0.40	14

Petron's consolidated **net income** for the first nine months of 2010 reached **₱ 5.35 billion**, up by **₱ 1.98 billion** from the **₱3.37 billion** earnings posted during the same period in 2009. The 59% improvement in the company's bottom line was primarily attributed to the combined effect of higher sales volume, better margins of petrochemical products, lower interest expense and unrealized foreign exchange gains on outstanding US\$ loan with the continued appreciation of the Philippine peso versus the U.S. dollar.

In the third quarter of 2010, Petron posted a net profit of **₱ 1.81 billion**, 16% better than the **₱ 1.56 billion** income reported in 2009 despite the **₱ 0.91 billion** drop in margin. The deterioration in margin was more than offset by higher interest income and translation gains versus translation losses in 2009.

On a year to date basis, **earnings before interest, taxes, depreciation and amortization (EBITDA)** of **₱ 12.1 billion** surpassed 2009 level by 16% or P1.7 billion.

Earnings per share improved to **₱ 0.57** from **₱ 0.36** in 2009 while **return on sales** increased from 2.7% to **3.1%**.

Major contributory factors are the following:

Gross margin (GM) grew by 11% to **₱ 13.32 billion** from prior year's **₱ 12.02 billion**. The following accounted for the variance in gross margin:

- ◆ **Sales volume** reached **35.8MMB**, up by 11% from 32.3MMB in 2009 prompted by higher diesel, fuel oil and petrochemical sales. Diesel sales rose due to volume requirements of new builds while increase in fuel oil was triggered by heightened operations of independent power producers. Also, the commercial operations of BTX units which produce new petrochemical products benzene and toluene started only in April 2009.

- ◆ **Net sales revenue of ₱ 169.8 billion** for the first three quarters of 2010 exceeded 2009 level of ₱ 123.6 billion by 37%, due to the combined effect of higher average selling price (2010: ₱ 29.13 vs. 2009: ₱ 23.48) and volume. Regional MOPS prices increased from an average US\$60.64/bbl in 2009 to US\$80.45/bbl in 2010.

- ◆ **Cost of Goods Sold (CGS) soared to ₱ 156.48 billion** from ₱ 111.62 in 2009 billion as crude cost went up (2010: US\$77.46 vs. 2009: US\$57.97). In 2010, 85% of CGS was sourced from crude compared to 67% of the same period in 2009. Lower crude consumption in 2009 was primarily due to the total plant shutdown in the first few months of 2010.

- ◆ **Refinery Operating Expenses**, which formed part of CGS, totaled **₱ 3.71 billion** or 5% lower than 2009. The decline in expenses was brought about mainly by the decrease in maintenance and repairs (M&R) and lower depreciation expense. M&R was higher in 2009 due to repairs of properties damaged by the fire incident and turnaround activities of some units. The reduction, however, was partly offset by the increases in purchase utilities and materials and supplies on account of higher crude run.

- ◆ **Selling & Administrative Expenses** amounted to **₱ 4.41 billion**, 7% higher than 2009. Aggressive retail expansion, rental on SMC offices and higher purchase of LPG cylinders contributed to the rise in expenses. However, on a **peso per liter basis**, actual operating expense was lower at **₱ 0.65** versus ₱ 0.76 in 2009 primarily on account of the 11% rise in sales volume.

- ◆ **Net Financing Costs & Other Charges** dropped significantly from 2009 total of ₱ 3.26 billion to **₱ 1.84 billion** in 2010. Interest expense declined by ₱ 362 million attributed to favorable average borrowing rate (2010: 5.2% vs. 2009: 6.4%) despite the increase in average borrowing level (2010: ₱ 59.4 billion vs. 2009: ₱ 56.3 billion). In addition, higher interest income coupled with favorable foreign exchange translation on dollar-denominated loans largely contributed to the positive variance.

Financial Position

September 2011 vs. December 2010

As of September 30, 2011, **consolidated resources** stood at **₱ 170.96 billion**, 6% (₱ 9.14 billion) higher compared to end-December 2010 level of ₱ 161.82 billion due to the combined effects of the following:

Cash and cash equivalents were reduced by 54% to **₱ 20.40 billion** primarily to fund working capital requirement (Inventories and Receivables), capital expenditures and other investments.

Financial assets at fair value through profit or loss was up by 42% from ₱ 0.23 billion to **₱ 0.32 billion** brought about by the strengthened fair value of free standing derivatives partly offset by the decline in market value of investments in marketable securities and club membership shares.

Trade and other receivables-net rose by 7% (₱ 1.74 billion) to **₱ 26.00 billion** from the ₱ 24.27 billion level in December 2010 attributed to increased sales to industrial customers.

Inventories grew significantly from ₱ 28.15 billion to **₱ 47.09 billion** largely due to higher crude price and volume.

Other current assets of **₱ 7.09 billion** surpassed the ₱ 4.29 billion level as at year-end of 2010 owing to higher Input VAT as a result of higher purchase price of crude and finished products.

The drop in **Assets-held-for-sale** from ₱ 0.82 billion to **₱ 0.01 billion** pertained to the transfer of Petron Mega Plaza to **Investment Properties** which surged to **₱ 0.82 billion** from ₱ 0.12 billion.

Property, plant and equipment-net increased by 23% from ₱ 34.96 billion to **₱ 42.98 billion** due to various capital projects in the refinery such as the Refinery Solid Fuel Fired Power Plant and Refinery Master Plan 2, and additional service stations.

Investment in associates also increased from ₱ 0.80 billion to **₱ 1.32 billion** with the purchase of 35% interest in Manila North Harbour Port, Inc.

Available-for-sale financial assets (current and non-current) fell to **₱ 1.03 billion** from ₱ 1.16 billion in December 2010 resulting from lesser investments in government securities and corporate bonds during the period.

Deferred tax assets-net went up to **₱ 170 million** from ₱ 28 million in 2010 due essentially to the effect of unrealized profit from subsidiaries.

Short-term loans and liabilities for crude oil and petroleum product importations of ₱ 57.37 billion surged by 31% (₱ 13.72 billion), an offshoot of higher crude and finished product prices this year.

Derivative Liabilities of **₱ 97 million** more than tripled the ₱ 30 million level as at end of December 2010 due to higher notional amounts heightened by deteriorating fair value of embedded derivative transactions.

Income tax payable ballooned from ₱ 14 million to **₱ 532 million** prompted by higher taxable income during the nine-month period. The December 2010 taxable income considered the net operating loss carry-over (NOLCO) of prior years. In addition, last year's tax due was reduced by the utilization of past years' MCIT as against zero this year.

Long-term debt inclusive of current portion went lower by 20% from ₱ 54.40 billion to **₱ 43.28 billion** with the settlement of maturing loans.

Deferred tax liabilities-net of **₱ 1.77 billion**, showed a 9% reduction from the ₱ 1.96 billion balance as at December 31, 2010 after considering the impact of temporary differences in income tax computation.

Asset retirement obligation escalated by 8% (₱ 63 million) to **₱ 878 million** on account of higher accretion rate.

Other non-current liabilities perked up by 15% (₱ 93 million) to **₱ 702 million** with the increase in cylinder deposit and cash bonds.

Total equity amounted to **₱ 59.29 billion**, 11% higher than the ₱ 53.34 billion level in December 2010, traceable to the **₱ 7.58 billion** income realized during the first nine months of the year partly offset by cash dividends paid to preferred and common shareholders totaling **₱ 1.65 billion**.

September 2010 vs. December 2009

Petron closed the third quarter of 2010 with **total assets** of **₱ 138.34 billion**, 22% or ₱ 25.15 billion higher than end-December 2009 level of ₱ 113.19 billion.

Cash and cash equivalents increased by 24% or ₱ 3.07 billion to **₱ 16.05 billion** principally due to the proceeds from loan availments and issuance of preferred shares.

Available for-sale investments (current and non-current) of **₱ 1.20 billion** declined by 11% or ₱ 151 million on account of the maturity of investment in government securities of the local insurance subsidiary.

Trade and other receivables-net amounted to **₱ 25.25 billion**, 15% or ₱ 4.45 billion lower than the ₱ 29.70 billion level as of December 31, 2009 mainly due to the drop in government receivables as a result of significant utilization of tax credit certificates.

Inventories-net went up to **₱ 32.12 billion** from ₱ 28.17 billion as at end of 2009. The ₱ 3.95 billion increase was primarily attributed to higher volume of both crude and finished products. There were minimal purchases in December 2009 in anticipation of the implementation of the ASEAN Trade in Goods Agreement (ATIGA) starting January 2010.

Other current assets posted a 29% or ₱ 1.31 billion reduction from ₱ 4.47 billion to **₱ 3.16 billion**, essentially due to the filing of input VAT claims on zero-rated sales.

Investment Properties of **₱ 0.96 billion** was four times higher than the ₱ 0.23 billion figure reported in December 2009 chiefly due to the transfer of the book value of Petron Megaplaza Offices from Property, Plant and Equipment account.

Deferred tax assets of **₱ 15 million** was twice as much from end-December 2009 balance of ₱ 7 million due mainly to the effect of translation adjustment of the foreign insurance subsidiary.

Other non-current assets were considerably higher at **₱ 24.43 billion in 2010** from ₱ 1.33 billion in year-end 2009 primarily traced to advances to the retirement fund.

Short-term loans and liabilities for crude oil and petroleum product importations went down by 9% (₱ 4.54 billion) to **₱ 45.74 billion** principally due to settlements made countered by higher crude/finished products importations.

Long-term debt inclusive of current portion showed a significant movement from ₱ 18.89 billion to **₱ 33.12 billion** chiefly due to the newly-availed NORD loan amounting to US\$355 million partly reduced by amortizations of outstanding loans.

Income tax payable increased to **₱ 14 million** from ₱ 10 million as at December 31, 2009 owing to higher tax liabilities reported by the subsidiaries.

Deferred income tax liabilities-net at **₱ 1.89 billion** grew almost three-fold from ₱ 514 million largely due to the impact of NOLCO as well as temporary differences reflected under parent and subsidiaries' accounts.

Other non-current liabilities rose by 10% or ₱ 109 million to **₱ 1.16 billion** mainly due to the increases in provision for Asset Retirement Obligation and cylinder/cash bond deposits.

Total equity attributable to equity holders of the parent aggregated **₱ 51.10 billion** at the end of third quarter 2010, showing a 37% or ₱ 13.81 billion improvement over the end-December 2009 level due to the combined effect of the following:

- ◆ **₱ 9.86 billion** issuance of preferred shares, net of issue cost
- ◆ **₱ 5.35 billion** year-to-date net income partly reduced by the **₱ 1.44 billion** dividends on common and preferred shares.

Cash Flow

Cash generated from operating activities was more than offset by the substantial increase in inventories, thus, resulted in a net cash outflow of **₱ 0.64 billion**.

Cash outflows from investing activities were used primarily in capital projects in the refinery, construction of additional service stations, and investment in Manila North Harbour Port, Inc.

Available cash was also used to pay-off maturing obligations and dividends.

In Million Pesos	Sept 30, 2011	Sept 30, 2010	Change
Operating (outflows)/inflows	(641)	20,691	(21,332)
Investing Outflows	(13,057)	(29,500)	16,443
Financing (outflows)/inflows	(9,947)	11,935	(21,882)

Discussion of the company's key performance indicators:

Ratio	Sept 30, 2011	Dec 31, 2010
Current Ratio	1.5	1.6
Debt to Equity Ratio	1.9	2.0
Return on Equity (%)	18.0	17.4
Debt Service Coverage	4.1	4.2
Tangible Net worth	59.3B	53.3B

Current Ratio: Total current assets divided by total current liabilities. This ratio is a rough indication of a company's ability to service its current obligations. Generally, the higher the current ratio, the greater the "cushion" between current obligations and a company's ability to pay them.

Debt to Equity Ratio: Total liabilities divided by tangible net worth. This ratio expresses the relationship between capital contributed by creditors and that contributed by owners. It expresses the degree of protection provided by the owners for the creditors. The higher the ratio, the greater the risk being assumed by creditors. A lower ratio generally indicates greater long-term financial safety.

Return on Equity: Net income divided by average total stockholders' equity. This ratio reveals how much profit a company earned in comparison to the total amount of shareholder equity found on the statements of financial position. A business that has a high return on equity is more likely to be one that is capable of generating cash internally. For the most part, the higher a company's return on equity compared to its industry, the better.


Debt Service Coverage: Free cash flows add available closing cash balance divided by projected debt service. This ratio shows the cash flow available to pay for debt to the total amount of debt payments to be made. It also measures the company's ability to settle dividends, interests and other financing charges.

Tangible Net Worth: Net worth minus intangible assets. This figure gives a more immediately realizable value of the company.

SIGNATURES

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

Registrant PETRON CORPORATION

Signature and Title 

JOEL ANGELO C. CRUZ
Corporate Secretary

Date: November 14, 2011

Principal Financial/Accounting Officer/Controller

Signature and Title 

EFREN P. GABRILLO
Assistant Vice President - Controllers

Date: November 14, 2011

