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DIVESTITURE STRATEGIES FOR
THE PRIVATIZATION PROGRAM
DEPARTMENT OF AGRICULTURE

FILE COPY

PHILIPPINES

REPORT BY

Ronald J. Ivey

In Cooperation With a Team of Consultants of
ARTHUR YOUNG & CO.

CENTER FOR PRIVATIZATION
10 Pennsylvania Avenue, N.W. - Washington, D.C.

FILE COPY

Project No. 14

January 1988

Prepared for the
BUREAU FOR PRIVATE ENTERPRISE
U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT



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ACRONYMS

ADB	Asian Development Bank
ADU	Asset Disposal Unit, Department of Agriculture
AFP	Armed Forces of the Philippines
APMP	Agro-Processing and Marketing Project, NFA
APT	Asset Privatization Trust
BAI	Bureau of Animal Industry
CARP	Comprehensive Agrarian Reform Program
CFP	Center for Privatization
COA	Commission on Audit
COP	Committee on Privatization
DCF	Discounted cash flow
DA	Department of Agriculture
DBP	Development Bank of the Philippines
DF	Department of Finance
DTRI	Dairy Training and Research Institute
FTI	Food Terminal, Incorporated
GOCC	Government-owned or controlled corporation
GOP	Government of the Philippines
IFAD	Institute of Food and Agricultural Development
KKK	Kilusang Kabukayan at Kaunlaran
MCDC	Mindanao Cotton Development Corporation
NCC	Northern Cotton Corporation
NFA	National Food Authority
NEGC	Northern Philippines Grains Complex
PCC	Philippine Cotton Corporation
PDC	Philippine Dairy Corporation

PECO	Panay Electric Company
PNB	Philippine National Bank
SLDP	Smallholder Livestock Development Project
SOCO	Special Operations Coordinating Office, NFA
SMP	Seed Multiplication Program
SPGC	Southern Philippines Grains Complex
STDC	Southern Tagalog Dairy Cooperative
UPLB	University of the Philippines, Los Banos
USAID	United States Agency for International Development
WACC	Weighted-average cost of capital

I. INTRODUCTION AND EXECUTIVE SUMMARY

This chapter discusses the purposes of the Project, and delineates the scope of work as set forth in a cable from USAID/Manila to the AID Private Enterprise Bureau and the Center for Privatization. It also provides an executive summary containing the major findings and recommendations of this report.

1. THE PURPOSES OF THE PROJECT WERE TO DEVELOP PRIVATIZATION OPTIONS FOR PHILIPPINE COTTON CORPORATION AND PHILIPPINE DAIRY CORPORATION, AND TO DESIGN A MORE DETAILED STRATEGY AND ORGANIZATION FOR DIVESTITURE OF THE DEPARTMENT OF AGRICULTURE'S ATTACHED ORGANIZATIONS

The primary purpose of this Project was to respond to a request by the Department of Agriculture to review the operations of two government-owned corporations, the Philippine Cotton Corporation (PCC) and the Philippine Dairy Corporation (PDC) to develop their privatization plans. This assignment was an extension of a previous study, performed and financed by the Center for Privatization (CFP) of Washington, D.C., that developed privatization strategies for the peripheral operations of the National Food Authority (NFA), a government agency also included in the portfolio of the Department of Agriculture.

However, this Project also included a review of the progress of implementation of the recommendations of the previous study of the NFA to make appropriate recommendations for accelerating the divestiture of the NFA peripheral activities.

The final purpose of the Project was to review a recommendation in the NFA study concerning the establishment within the Department of Agriculture of an Asset Disposal Unit (ADU), a small, temporary office that was to be responsible for the divestiture of the NFA peripheral operations. The purpose of this review was to:

- Determine whether such an office is necessary

- If necessary, develop more detailed guidelines for the ADU: in terms of its relationship to the GOP's national privatization program; the transfer of assets to the ADU; and the unit's proposed activities.

2. THE SCOPE OF WORK CALLED FOR DETAILED ANALYSES AND FORMULATION OF GUIDELINES FOR THE PRIVATIZATION PROGRAM OF THE DA

To meet the objectives of this Project, USAID/Manila provided a detailed scope of work for developing the divestiture strategies of the PCC and PDC, calling specifically for analyses of the following:

- Status of current management and staffing
- Determination of the validity of the business plan
- Relevance of the marketing strategy
- Review of the financial situation, including the contribution of each corporation's profit centers
- Determination of commercial viability
- Valuation of the operation taking into consideration the elimination of government subsidies after its sale
- Determination of a range of "fair market values" that might be received from each of these operations, given recommendations made about packaging the operations for sale, prospective buyers, etc.
- Calculation of a liquidation value, in cases where commercial viability does not exist.

Based upon the above review, the Project Team was to develop action plans for the divestiture of the PCC and PDC.

In connection with the foregoing analysis of the PCC, the Project that was to carry out an analysis of the Philippine cotton industry, assessing the impact of current trade, regulatory and subsidy policies upon that industry. The Study Team also was to determine components of the cotton industry which may have an international comparative advantage. The section on the PDC, however, was to cover privatization issues only.

The Project Team was to review the progress of the divestiture program for the NFA subsidiary operations to make recommendations for alternative courses of action to effect the transfer and divestiture of those operations.

Based upon the DA's future divestiture requirements, the Project Team was to develop recommendations for establishment of an Asset Disposal Unit (ADU) within the DA. The guidelines were to be formulated regarding the following:

- Relationship of the ADU to the Asset Privatization Trust (APT), the Committee on Privatization (COP), and the Department of Finance (DF)
- Transfer of assets to the ADU and subsequently to the APT
- Establishment of priorities for divestiture
- Procedures for conservation of assets
- Desirability of rehabilitation of assets prior to sale
- Consideration of organizational restructuring, mergers and other forms of reorganization
- Appropriate activities of the ADU
- Development of an action plan for disposal of the DA's "attached" organizations.

3. BECAUSE OF PROGRESS MADE IN PRIVATIZATION AT THE NATIONAL LEVEL AND THE INTENTION OF THE SECRETARY OF AGRICULTURE TO TRANSFER PDC AND PCC TO THE ASSET PRIVATIZATION TRUST, DIVESTITURE STRATEGIES WERE ALIGNED WITH THE DIVESTMENT PLANNING GUIDELINES OF THE COP AND THE REQUIREMENTS OF THE APT

In the year since the completion of the NFA study, concrete progress has taken place at the national level in the area of privatization. The Asset Privatization Trust (APT) was created under Presidential Proclamation 50, signed December 9, 1986. The APT is the government unit responsible for selling of government-owned or -controlled corporations (GOCCs) that have been selected for privatization.

A Committee on Privatization (COP), a cabinet-level committee headed by the Secretary of Finance, was formed to decide which assets the APT should divest. Approval by the COP is required for all asset sales by the APT. Government agencies which administer GOCCs may undertake their own privatization actions, unless the COP assigns a particular GOCC to the APT for sale.

On October 20, 1987, President Aquino made a landmark speech on a wide variety of issues concerning the nation. Among those issues was a direct reference to privatization:

"I want government to get out of business. I want it to cash in on all the investment it should never have made. Non-performing assets listed to be sold, will be sold in open bid to the highest bidder... The preferred procedure is open bidding."

The policy thrust is that the opportunity to privatize GOCCs must be taken in the near-term to demonstrate to all factions the substantial benefits from the process. The Project Team views the acceleration of the process of privatization at the Department of Agriculture as being "in line" with this national objective.

Because in the initial meeting with the Secretary of Agriculture it became apparent that the DA did not wish to undertake the privatization activities itself, it was jointly decided with USAID/Manila that the Project output should match the requirements of the APT as closely as possible. To accomplish that, the Project Team met with the APT and the COP to define these requirements. The study effort has been guided to a considerable extent by those requirements in order to make the final report as useful as possible.

According to the APT, its informational requirements include:

- An asset valuation, based on data and analysis of markets, production and operations
- Asset list and condition
- Review of legal impediments

- Recommended packaging for divestiture
- Identification of interested buyers.

To this list we have added other information important to privatization:

- Liabilities to be absorbed by the government
- Personnel retention and retrenchment, along with attendant costs to the government.

The COP privatization planning guidelines include the following:

- Date of establishment
- Legal basis of establishment
- Sector/industry
- Shareholders
- Department attachment
- Parent company
- Financial highlights
- Factors to consider
- Extent of privatization envisioned
- Mode of privatization
- Method of privatization
- Potential investor groups
- Valuation
- Valuation entity
- Timing of privatization
- Program of activities.

In line with the study requirements, Chapter II of this report presents a divestiture strategy for the PCC; Chapter III presents the counterpart strategy for the PDC. Chapter II also presents, in broad terms, a discussion of the international competitiveness of the Philippine cotton industry and its components. Chapter IV presents recommendations regarding the NFA/FTI divestiture program. In Chapter V, recommendations concerning the setting up an ADU are discussed.

Appendix A lists the persons interviewed. Appendix B provides privatization plans for PCC and PDC to be submitted to the COP. Appendix C provides privatization plans to be submitted to the COP for the NFA peripheral operations that are considered to be privatizable in the near-term. Appendix D provides draft documents prepared according to COA guidelines for bidding out PDC equipment. Appendix E provides a list of PCC and PDC equipment to be privatized. In Appendix F, we have included the "Guidelines for Privatization of Government Corporations" as developed by the COP.

EXECUTIVE SUMMARY

1. PHILIPPINE COTTON CORPORATION PRESENTS AN EXCELLENT PRIVATIZATION OPPORTUNITY

- Domestically grown cotton has an assured market in the Philippines, although at present it accounts for only 15-20% of total use.
 - Millers prefer local cotton because it is hand-picked and therefore cleaner than imported cotton as well as meeting other quality requirements; they have not, however, been willing to pay a premium for the domestic product.
 - Millers will buy all they can get, at prices equal to imported product prices. (Local lint cotton prices are based on landed cost of imported cotton).
- Cotton can be profitably grown in the Philippines; yields are high by world standards (twice the U.S. average) and production costs are internationally competitive.
- PCC has played an important role in transfer of cotton production technology to farmers and in proving that cotton can be grown and processed in the Philippines.
- PCC's ability to promote cotton production in the Philippines has progressively deteriorated due to internal organizational difficulties, financial constraints and adverse external developments, resulting in a steady decline in hectareage grown for sale to that organization.
- Private sector interests have begun moving aggressively into the gap left by diminishing PCC efforts, taking advantage of technology in place.

- Most Philippine cotton is grown in Southern Mindanao and Northern Luzon, with a lesser amount on Panay.
 - The greatest potential for expansion lies in Southern Mindanao.
 - Northern Luzon hectarage can also be expanded significantly.
 - Panay production can also be increased, given greater industry promotion there.
 - Negros also may represent a potentially viable cotton production base.
- The future viability of the cotton industry and of privatized PCC depends on expanding planted area by at least two to three times the present estimated total of 10,000 ha.
- This increase can be attained, provided growers are assured:
 - Farmgate prices that make cotton production profitable (cotton farmers appear to be very price responsive)
 - Necessary production technology
 - Availability of production credit.
- These elements can be profitably provided by efficient ganners at anticipated world price levels for lint, utilizing Land Bank and other available funds as sources for production credits.

- The profit potential of the ginning industry is demonstrated by the level of interest and activity of the private sector. There are presently four private ginners (and possibly some minor ones) competing with PCC.
- Equipment supplied by Lummus at all three PCC plants is in excellent condition with the following capacities per hour:

San Juan, Ilocos Sur	4 bales
San Fabian, Pangasinan	12 bales
Polomolok, South Cotabato	16 bales.
- PCC also owns a 9-hectare parcel in Tarlac and land and buildings in Cagayan.

The privatization strategy for PCC is as follows:

- Transfer PCC to the APT by seeking approval for privatization from the COP (this was accomplished on November 4, 1987).
- Offer San Juan, San Fabian and Polomolok gins for sale through sealed biddings, with San Fabian and Polomolok to be sold as operating entities and the San Juan equipment to be moved to another location. The San Juan ginning equipment might be utilized by a buyer at Iloilo, which at present has no gin to support the developing cotton industry on Panay Island.

Benchmark values:

San Juan	P2.2 million (sold off-site)
San Fabian	11.2 million
Polomolok	29.7 million
Polomolok (not recommended)	6.5 million (sold off-site)

- Benchmark values assuming San Juan and San Fabian are both sold in-place:

San Juan	P3.6 million
San Fabian	5.4 million

- Sell San Fabian and Polomolok during the March-June ginning season for maximum return
- World sales channels will probably have to be tapped to sell the San Juan equipment since there is little market demand for used ginners equipment
- Another option considered was that of selling the Polomolok gin offshore and moving one of the Northern Luzon gins to South Cotabato; because of the great difference in value between the Polomolok gin sold on-site and sold offshore, this option was not considered desirable.
- Sell miscellaneous assets by bid, except for the airplane, which should be transferred to DA.
 - The real property at San Juan should be reappraised and offered as tobacco or rice storage facilities.
 - Unless CRDI can make a valid case for keeping them, the demonstration farms at San Juan and Polomolok should be sold or used for other purposes by the DA.
 - The baled cotton inventories remaining at the gins could be sold by PCC to textile millers or listed as additional assets in the bid documents.

- Provisions should be made to avoid losing PCC's reservoir of technical cotton knowhow:
 - Buyers of San Fabian and Polomolok should be required to retain key employees for a specific period, probably one ginning season.
 - Other employees should be absorbed by DA, thus reducing retrenchment costs and adverse employment effects.
- The land lease at Nueva Ecija and the seed production joint venture at Zambales will have to be wound up through negotiation or legal proceedings.
- CRDI, which will be retained as an attached agency to the Department of Education, can be of great value in fostering continued improvements in technology; this agency however, should be transferred to the purview of the DA to be most effective.
- Take appropriate financial measures as soon as possible; since the PCC has already been moved to the APT, this will be a responsibility of that organization:
 - Freeze all bank accounts as soon as the privatization decision is final
 - Age receivables and devise collection strategy; in conjunction with COA, determine bad debts to be written off.
- Close down PCC Manila headquarter and sublease the space until the original lease runs out in four years.
- Introduce legislation to wind up PCC.

2. THE WINDING UP OF PHILIPPINE DAIRY CORPORATION WILL BE A RELATIVELY SIMPLE PROCESS THAT CAN BE HANDLED BY THE DA FOLLOWING COA GUIDELINES

- Although about 98% of the dairy products consumed in the Philippines are imported, mainly in the form of dry milk solids, there is a small but growing market for locally produced fresh milk, which can be produced there at a profit.
 - Magnolia has proven that temperate climate Holstein dairy cows can be profitably managed for milk production in the Philippines.
 - At an average supermarket price of about P18-19 per liter, production and marketing of fresh pasteurized-homogenized milk appears to be very profitable.
 - While the market for fresh milk is still limited to upper-class Filipinos and expatriates, growth of consumption appears to be faster than for any other dairy product category.
 - The U.S. military bases, which are presently purchasing some fresh milk from Magnolia, have indicated their interest in developing additional local sources of supply.
- PDC was not, however, designed to exploit this special market niche for fresh fluid milk.
 - PDC was initiated in 1981 for the purpose of providing an alternative income source for small-

holders, increasing Filipino nutritional standards and achieving some measure of import substitution.

- It was originally planned for PDC to sell milk to established milk processors, such as San Miguel; this did not prove feasible; this did not prove feasible so the target markets became the dairy farm families and local communities.
- Due to various shortcomings in quality control, i.e., unsanitary on-farm milking and handling, delays in getting milk chilled down to a proper holding temperature and similar problems, smallholder milk produced generally does not meet the quality specifications of the commercial dairy processors.
- PDC obtained most of its program funding through an ADB-IFAD US\$16 million loan to the GOP for the Philippine Smallholder Livestock Development Program, of which less than US\$5 million was disbursed. The funds were used for the following:
 - Almost 200 staff were hired
 - A milk processing plant and two milk chilling centers were installed in Southern Tagalog
 - Plans were made to establish a breeding center in Bukidnon but these were scrapped after a milking parlor and chilling equipment (still in crates in Bukidnon) were purchased
 - 2,400 cows were imported, and 4,000 animals including offspring of the original imported cattle were dispersed to individual smallholders.

- The Smallholder Livestock Dairy Development Program was a failure, as evidenced by the following:
 - PDC was only able to achieve on average daily throughput of 700 liters a day for its Alabang milk processing plant
 - The two milk chilling centers in Lipa and Trece Martires could not obtain enough milk to justify their operation
 - All useful activities with the exception of some extension services essentially stopped in mid-1986; the chilling centers were closed down in February 1986, after two months operation while the Alabang processing plant was shut down in June 1986, after six months operation.
 - In the seven years of its existence, PDC functioned as an operating entity for a total of only six months, in the first half of 1986.
 - It is estimated that less than half of the original 4,000 cattle dispersed are still in farmers' hands and of these, probably less than 25% are producing milk.
- Three options were considered for privatizing PDC, given the following factors:
 - The cattle are already being sold by DA to the farmers who hold them
 - Only one of the milk chilling center sites is actually owned by the DA; the other chilling center site is the property of the local government, while

the processing plant site is the subject of a controversy between DA and another department as to which actually holds ownership

- The milk chilling centers are located in areas where there is no milk supply; thus, even if there were buyers for an operating dairy processing entity, which is doubtful, no sale could be made on this basis
- Since the value of the assets is so small, the Team recommends that the DA handle the bidding process directly, following COA guidelines, rather than transferring the assets to APT. DA must still submit this step for approval to the COP.
- The three privatizations options were:
 - The milk processing and chilling facilities might be leased to a commercial dairy producer
 - Dairy cooperatives would be allowed to utilize the processing and chilling facilities in return for paying maintenance and operating costs
 - All equipment is sold for removal from site, through sealed bidding, with the sale conducted by DA

All of the above options include closing down the company and retrenching the employees
- Due to a number of constraints, the third option, that of selling the equipment, is considered the most viable and is the recommended approach.

- Liquid assets of PDC, amounting to P75.8 million held in short-term government securities, are sufficient to cover all liabilities that appear on the books which total approximately P74 million as of March 31, 1987; this does not include the costs of retrenching personnel. The DA should seek permission to use these funds to pay off the liabilities.
- It will be necessary to retrench the 90 employees of PDC; it is unlikely that the DA can absorb these people, although some of the 44 dairy technicians on the staff may find employment in the private sector dairy industry.

3. THE NATIONAL FOOD AUTHORITY HAS DONE LITTLE TO PRIVATIZE ITS PERIPHERAL ASSETS -- AND THE DA SHOULD TAKE STEPS TO PUT THAT PROCESS IN MOTION

- NFA did privatize the Kadiwas, which are under its administration.
- Beyond that, NFA is not capable or willing to privatize its other peripheral assets.
- NFA could clean up its balance sheet and improve its annual cash flow by perhaps P250 million through privatization of its peripheral assets. In the case of FTI, it is reluctant to do so because it feels that it should recover its advances amounting to P500 million and that retrenchment costs, which could total P100 million, should be paid out of privatization proceeds. Incidentally, FTI's 1986 balance sheet does not reflect this level of advances -- it shows loans from NFA of only P195 million.
- NFA has in reserve P90 million for retrenchment costs out of P100 million provided to it by the national government

for those purposes. NFA estimates total retrenchment costs of around P100 million for FTI.

- APT currently is successor-in-interest to the DBP and PNB loans, which it means that it probably has the legal right to replace the board and management of FTI or it could foreclose on these non-performing assets, as a means to effect a board and management change there.
- FTI management has in October 1987 produced a business plan, which it submitted to the Department of Management and Budget, that lacks solid business sense and calls for subsidies to FTI of P239.8 million in CY 1988. It also called for the eventual privatization of FTI by selling a portion of the shares to 2.2 million farmers at P637 a share and the remainder to lessees, clients and displaced employees. The government would retain, however, the majority share. FTI shows no sign of becoming profitable -- it lost P134 million in 1985 and P159 million in 1986.
- The claim by FTI that if the complex is not used as a "food terminal" it will revert to the Ayala Corporation (a claim repeated in the October 1987 business plan) is a hoax. There are some conflicting claims regarding the land by the former owners of the Maricaban estate as FTI is located on land expropriated by the American forces after the end of the Spanish-American war. However, the legal basis for the establishment of FTI for a period of 50 years -- and the legal basis for its privatization -- is most likely Presidential Decree No. 347, signed May 3, 1968.
- Unless Presidential Decree No. 347 is overridden by the President or Congress, which is advisable, for the purpose of increasing proceeds from FTI's privatization to finance

CARP, it appears that the privatization of the complex can only be done through a long-term sub-lease.

- A review of the NFA/FTI peripheral operations has led us to the conclusion that some are immediately privatizable by APT, some are immediately privatizable by DA using COA guidelines and some cannot be privatized now:

- Immediately Privatizable By APT

FTI

Tabangao Unloading Facility

Southern Philippines Grains Complex (lease)

Digos Agro-Processing Complex

Bicol Seed

Iloilo Thermal Generating Facility

(Also: Philippine Cotton Corporation which has been approved by COP for privatization)

- Immediately Privatizable By DA

Digos and SPDC demonstration farms

(Also: PDC milking, chilling and processing equipment and San Juan and Polomolok demonstration farms)

- Not Immediately Privatizable

Northern Philippines Grains Complex

The privatization strategy for the NFA peripheral assets should proceed as follows:

FTI

- DA should submit privatization plants to COP for approval, with subsequent transfer to the APT for divestiture.
- APT and DA should act jointly to remove FTI management and board, and install caretaker manager and interim board.
- Secretary of Agriculture should propose to President that ownership of FTI land be transferred to FTI or DA for privatization in order to benefit CARP, and at the same time resolve the problem of MERALCO rates by instructing NPC to connect directly to the FTI sub-station. If this is accomplished the cash proceeds from the FTI privatization will increase dramatically.
- Even if the ownership is not transferred, the privatization can still be accomplished by sub-leasing the facility to a single operator for a period of up to six years, renewable for an additional 25 years. It could be that the transfer of the property can be transferred to FTI, and subsequently sold; it perhaps could be sold with an option to purchase upon transfer of the land. The operator would be required to manage and maintain all property, and be entitled to receive rents for such leases, construct additional structures as appropriate for leasing, and use structures and facilities for the operator's own business activities as required.
- APT should perform a valuation to determine the annual lease amount based on lease and rental income at the complex. Total rental and service income in 1986 was P57.7 million. If ownership of the land is transferred, an appraisal must be made of the remaining 10 hectares of developable land.

- APT should prepare bidding documents that include:
 - Physical improvements
 - Present lessees, lease amounts and space utilization
 - Vacant building space
 - Developable land
 - Kadiwa sites and buildings.

- The private operator should be required to retain for a 12-month period 410 persons presently employed by the Facilities Management Group.

- There should be a 90-day period during which prospective operators can prepare their bids.

- Privatization of FTI need not be held up by the retrenchment of the remainder of its personnel. Retrenchment should be the responsibility of the FTI caretaker management. Retrenchment costs above the P90 million that NFA holds in reserve should be paid from sub-lease proceeds.

- Outstanding loan liabilities should be transferred by the APT to the DF for settlement.

Tabangao Unloading Facility

- APT should seek permission to assign the Pacific Flour Mills agreement.

- APT should prepare bid documents covering:
 - Retention of five employees manning the facility

- Requirement to unload soybeans for the Phil-Asia plant and to bid fees to be charged that plant per ton of soybeans unloaded
- Ample time (at least 60 days) to examine facility and prepare bids.
- NFA should remove rice or palay stored in the facility's warehouses or contract for its continued storage on a fee basis.

SPGC

- DA submits plan for privatization to the COP. Once approved the facility would be transferred to the APT.
- APT should have the DBP staff review the assumptions of the discounted cash flow analysis made in the 1986 CFP report, determine likely level of utilization, and thereby set benchmark value.
- Appraisers should identify and value any excess equipment.
- APT should prepare bid documents specifying:
 - Physical facilities and plant
 - Requirement of the bidder to review the personnel complement for the purpose of specifying employees to be retained for a 12-month period
 - Financial records to be turned over to the buyer.
- Outstanding loan to the DBP should be transferred to the DF for payment.

- DA should sell the 7.3 hectare demonstration farm using COA guidelines. A survey will be required to define boundaries and develop the legal description of the land.

Digos Agro-Industrial Complex

Approximately the same as recommendations above for SPGC.

4. THERE ARE REQUIREMENTS FOR A SMALL ADU AT THE DA FOR A LIMITED TERM TO SUPPORT AND IN SOME CASES, IMPLEMENT THE PRIVATIZATION OF OPERATIONS IN THE DA'S PORTFOLIO

- The ADU recommendation in the CFP report was based on the fact that the APT had not been formed, and that NFA peripheral assets would receive a low priority in the national privatization process.
- While the APT is now active and has the resources required to privatize the larger units within the DA, it will be more expeditious for the Department to handle the privatization of the smaller entities.
- To perform the tasks associated with this function, and to prepare the larger units for disposal by the APT, the DA should establish a small (two to three-person) ADU. This unit is necessary because the Department does not have personnel available to carry out the necessary duties. This unit should be set up within the office of the Undersecretary for Attached Agencies. Some of the activities might be contracted out to local consulting firms. The unit should have a limited tenure -- we recommend one year.

The responsibility of the ADU should include the following activities:

- Have surveys carried out to determine exact boundaries, land area and legal description of the various demonstration farms; contract for appraisals of the SPGC and Digos demonstration farms; contract bidding documents and sell the demonstration farms; formulate bidding documents and sell the demonstration farms on an "as is" basis.
- Formulate bidding documents for the sale of the Iloilo Thermal Generating Plant and the Bicol Seed Company.
- Conduct and/or assist in legal and financial negotiations related to asset disposals, assignment of financial liabilities, retrenchment of personnel, legislation where required and documentation for APT disposal purposes. This activity will cover entities transferred to the APT as well as those to be divested by the DA itself.

II. DIVESTITURE STRATEGY FOR THE PHILIPPINE COTTON CORPORATION

This chapter provides the following information:

- Organizational history of PCC
- Overview of its management and organization
- Assessment of products, markets, pricing and industry structure
- Discussion of special issues, including trade and subsidy policies
- Assets and their condition
- Financial performance indicators
- Privatization options for PCC facilities
- Valuation of facilities given the privatization options
- Recommended privatization strategy.

1. THE PCC WAS CREATED TO SPEARHEAD COTTON SELF-SUFFICIENCY IN THE PHILIPPINES

This section discusses the organizational history of PCC, including the following:

- Rationale for the National Cotton Development Program (NCDP)

- Presidential Decrees 350 and 1063, which created and expanded PCC
- Other programs supporting cotton development
- Historical production performance.

(1) The National Cotton Development Program (NCDP) Was Launched Because of Good Crop Yields And Potential Economic Benefits

In the late 1950s, the National Development Company, a government entity, and later the General Agricultural Corporation, a private company, attempted to establish cotton production and ginning projects in South Cotabato. Both these efforts failed, primarily because of weather and pest problems.

The NCDP was launched in 1974 due to the perceived viability of cotton as a potentially major second crop for farmers in Luzon. A series of field trials, known as Operation Bulak, yielded an average of 1.2 metric tons of seedcotton per hectare. The field trials were conducted at 19 sites in Isabel, Nueva Ecija, Pangasinan, La Union, Ilocos Norte and Cavite. Pangasinan registered a high of 1.4 metric tons per hectare. It was concluded that the agronomic conditions in Luzon were ideal for cotton production and the "package of technology" developed by scientists at the Central Luzon State University could protect the cotton crop from pest infestation and assure good yields.

The Philippines had annually imported about 120,000 bales of cotton worth approximately US\$20 million. The prospect of foreign exchange savings through import substitution and of rural employment creation motivated the government to take steps toward developing a local cotton industry.

(2) PCC Was Established By The GOP To Produce Cotton On A Commercial Scale

In December 1973, then President Marcos issued PD 350 creating PCC as the central authority to undertake cotton production on a commercial scale, with the stated objective of achieving self-sufficiency. PCC was envisioned as a joint venture between the government and the private sector on a 60-40 ownership basis, with an initial paid-up capital of P1 million. Government invested P600,000 and the local textile millers put up the remainder.

PCC's activities were to:

- Encourage the participation of qualified farmers in the prime cotton growing areas
- Arrange production credit with participating commercial and rural banks for the production input and labor requirements of participating farmers
- Extend technical assistance to the farmers
- Purchase seedcotton from farmers at guaranteed prices
- Gin seedcotton
- Sell lint to domestic textile mills and export cotton-seeds.

In December 1976, PD 350 was amended by PD 1063 which increased PCC total authorized capital to P100 million and raised the government subscription to P70 million, which was fully paid. The remaining P30 million was to have been invested by government-owned or controlled corporations and/or private investors. The local textile mills chose not to invest, and the government put up P30 million more.

There are at present no other prospective producers of certified cotton seed. If the hectareage increases envisioned in this report are realized, however, there will be a need for greatly increased quantities of cotton seed. At the point at which the demand for certified seed grows to a volume that might justify entry of a commercial operation for certified seed production, consideration should be given to privatizing this function of CRDI. Provision of adequate supplies of good quality seed will be an important element in maintaining the viability of an expanded cotton production base.

The Philippine-German Cotton Project was initiated in 1982 in cooperation with the Federal Republic of Germany's aid agency GTZ, with the objective of developing a cotton pest management system. At the end of the project in March 1987, a pest management system and the related technology was in place and was being taught to cotton technicians and cotton farmers. .

In 1982, PCC secured a US\$26.7 million loan from the Asian Development Bank (ADB) at an interest rate of 11% per annum, payable over 25 years with a 5-year grace period. Unlike the programs described above, this one is considered a failure by the ADB because few components were implemented. Total draw-down on this loan was only US \$4.3 million and the balance was de-obligated in 1986.

Most of the de-obligated portion of the loan was to have been used for installation of a cotton seed processing plant at Polomolok, with a portion earmarked for additional laboratory and scientific equipment. Volume of seed produced as well as prospects for volume increases appeared too limited in 1986 to justify a seed processing plant.

The principal reason for PCC's failure to effectively utilize the ADB loan was the drop in seedcotton throughput occasioned by the industry and PCC problems discussed elsewhere in this report.

(4) PCC Initially Purchased Cotton Planted On 17,000 Hectares,
A Figure That Later Fell Sharply Because Of Competition
And A Widespread Shortage Of Farm Credit

The majority of seedcotton is grown on small farms ranging from one to three hectares in size. Farm size varies by area, with farms in Ilocos Sur as small as one-fourth of a hectare, while those in Southern Mindanao average two to three hectares. Purchasing large volumes of cotton, therefore, requires dealing with a large number of small farmers.

The figures below compare cotton hectarage of farmers who had marketing agreements with PCC with the estimated total hectarage. A sharp drop in PCC hectarage and purchases can be noted after the 1983-84 crop season.

Purchases And Hectarage
Of Farms Operating Under PCC
Marketing Agreements Compared To
Estimated Total Hectarage

<u>CROP YEAR</u>	<u>PCC PURCHASES IN METRIC TONS</u>	<u>PCC HECTARAGE</u>	<u>ESTIMATED TOTAL HECTARAGE</u>
1980-81	12,760	17,014	17,014
1981-82	14,360	14,500	4,500
1982-83	12,148	10,115	10,115
1983-84	12,789	11,953	12,100
1984-85	5,891	7,398	11,300
1985-86	6,015	4,396	12,500
1986-87	4,437	6,160	12,500

A primary reason for the decline in PCC hectarage after 1983-84 was the critical shortage of production credit. Rural banks, as well as the Philippine National Bank (PNB) and the Development Bank

of the Philippines (DBP), experienced severe liquidity problems and either stopped extending credit or cut back drastically.

In 1985-86, PCC began extending credit directly to farmers through the Modified Cotton Growing Scheme to help fill the gap left by the reduced bank lending. By the 1986-87 growing season, almost all farm production credit came from PCC or from banks whose exposure was guaranteed by PCC. The total amount of credit available was limited, however, by PCC access to funds, and therefore, fewer farmers overall received cotton production credit.

PCC's sharp drop in purchases after 1983-84 also reflects the lack of competitiveness of PCC's seedcotton buying prices vis-a-vis those of private cotton traders. Beginning in 1984, a number of private cotton traders were attracted into the business by PCC's success. In 1986-87, however, PCC's price of P7.30 per kg. was lower than those of private traders; as a result, many farmers delivered only enough cotton to PCC to repay their loans, selling the remainder to the private traders.

2. PCC IS TOP-HEAVY, OVERSTAFFED AND HAS NOT BEEN ABLE TO ORGANIZE ITSELF FOR PROFITABLE OPERATIONS

This section presents a profile of the management and organization of PCC, including the following:

- Board of directors and management
- Organizational growth
- Personnel complement, classification and benefits
- Retrenchment costs.

(1) Government Appointees Have Dominated The PCC Board

The PCC has a nine-person board, seven of whom are appointed by the government, which owns 99.6% of PCC equity. One director represents the textile millers and one represents no particular group. The Secretary of Agriculture acts as ex-officio chairman of the board.

A five-man executive committee composed of government-appointed board members meets monthly to review the operations and policy proposals, approve or disapprove major corporate expenditures and deliberate other matters raised by the PCC management.

The PCC organization has been decentralized to some extent. The current management structure consists of a central headquarters, with an executive vice president reporting to the president, and two operating divisions, one for Luzon and the Visayas, and one for Mindanao. The Officer-in-Charge of each operating division reports directly to the PCC executive vice president.

Each operating division is further sub-divided into three departments. These include:

- Finance and Administration
- Production and Extension
- Processing.

There is also a quality control group attached to each division.

(2) Too Rapid Expansion By PCC Had Adverse Organizational And Financial Results

PCC's initial success was based on slowly increasing production from working with carefully chosen growers in areas particularly well suited to cotton cultivation. In the late 1970s, field staff were pressured by PCC headquarters to rapidly expand the number of hectares under production; by 1980-81 there were 17,000 contracted hectares in 25 provinces.

This strategy overloaded existing administrative, personnel and financial capabilities. The number of employees rose from 890 in 1980 to 1800 in 1981. From P4.7 million in operating expenses in 1980, PCC's operating expenses increased 149%, to P11.7 million in 1981. Interest and other financing charges increased 51-fold from P1.3 million in 1980 to P67 million in 1984. This was due both to a substantial increase in PCC borrowing due to the need to support additional program activities, and the sharp rise in Philippine interest rates.

After 1982-83 PCC returned to careful area and farmer selection as a basis for its operations, but it never recovered from the organizational strains created by the rapid expansion and the concomitant financial charges accumulated. The Corporation's poor financial position, brought about by shortfalls in budgetary support and rapidly increasing expenditures, worsened in 1983-84 after interest rates increased to more than 40% as a result of the Aquino assassination.

A major reorganization effort designed to revitalize PCC was attempted in late 1986, but due to the mounting financial and operational difficulties experienced by the Corporation, it was never fully realized.

(3) The Manpower Complement, Though Greatly Reduced, Is Still Sizeable Considering Present Limited PCC Operations

PCC's manpower complement as of August 31, 1987, shows the following distribution of personnel by function and location:

<u>Major Departments</u>	<u>Head Office</u>	<u>Luzon</u>	<u>Visayas</u>	<u>Mindanao</u>	<u>Total</u>
Production/Extension	11	90	26	100	227
Finance & Administration	57	38	10	42	47
Processing	5	11	1	19	36
Management Services	21	-	-	-	21
Office of the President	7	-	-	-	7
Others (Marketing)	<u>3</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>3</u>
TOTAL	104	139	37	161	441

The personnel engaged in extension and processing in the regional offices comprise about 51% of total employees; finance and administrative personnel make up about 33%. The Manila headquarters is manned mostly by staff support personnel.

The on-going retrenchment program at PCC, using hectarage planted in each operating area as the basis for retaining or laying off personnel, has somewhat reduced excess manpower. Retrenchment is continuing during the 1987-88 crop season.

Monthly compensation and benefits of PCC personnel as of September 1987 were:

	<u>Head Office</u>	<u>Luzon</u>	<u>Visayas</u>	<u>Mindanao</u>	<u>Sub-Total</u>
Basic Salaries	P129,091	146,372	38,039	131,999	445,502
Cost of Living Allowance (COLA)	49,800	52,875	14,718	54,516	171,910
Representation/Transportation Allowance	4,106	34,832	8,684	42,847	90,471
Food Subsidy	<u>21,143</u>	<u>37,231</u>	<u>8,856</u>	<u>41,000</u>	<u>108,231</u>
Grand Total	204,141	271,311	70,2992	70,363	816,115

Retrenched personnel are paid a separation allowance equivalent to one-half of one month's gross salary for every year of service, plus the monetary equivalent of their accumulated leave credits. The average length of service is 5.5 years. Accumulated leave credits must be computed individually; however, an average of 75 days of leave credits per employee seems a reasonable assumption. Present PCC employees' cumulative length of service and leave credits are broken down as follows:

Manila Head Office	572	years
Luzon Operations	979	"
Visayas Operations	244	"
Leave credits	8	"
Mindanao Operations	608	"
TOTAL	2,411	years

Assuming that government has to separate all employees from the service and compensate them according to PCC's present policy (one-half of monthly gross salary for every year of service) and assuming further an average monthly gross pay per employee of P1,850, the total expense would be approximately P4.5 million.

The Department of Agriculture (DA) might absorb some of PCC's extension workers, perhaps 10 in Luzon, five in Visayas and 20 in Mindanao, to complement the DA's existing extension workers in those areas where rice-cotton and corn-cotton cropping patterns are well-established. However, this would reduce the total retrenching costs by only about P300,000.

There are a few employees whose length of service is near 20 years and who will soon retire. It might be advisable to provide full retirement benefits for those within three years of retirement age as these may be among the appropriate personnel to be retained by the private sector buyer, since they are the most experienced.

3. PHILIPPINE GINNERS PRODUCE HIGH-QUALITY LINT PRICED AT WORLD MARKET PRICES AND THERE IS GOOD POTENTIAL FOR EXPANSION OF COTTON PRODUCTION

This section discusses the following aspects of the Philippine cotton industry:

- Present industry outputs
- Market and industry structure
- Marketing channels
- Domestic prices, subsidies, and trade regulation and policies

EXHIBIT II-1

Supply and Source of Philippine Cotton, by Crop Year

YEAR	AREA	YIELD	PRODUCTION	IMPORTS	CONSUMPTION
	-- ha. --	kg.lint/ha	- - - - 1,000 bales	1/	- - - -
1977-78	3,200	200	3	120	124
1978-79	3,200	268	4	147	142
1979-80	6,900	377	12	120	134
1980-81	17,000	243	19	120	129
1981-82	14,600	358	24	67	101
1982-83	10,100	451	21	69	106
1983-84	12,100	427	24	82	105
1984-85	11,300	288	15	86	101
1985-86	12,500	364	21	106	108
1986-87	12,500	382	22	115	120

Source: International Cotton Advisory Committee

1/ 480 lb. net weight bales

- International price trends
- Competitiveness of Philippine cotton in the domestic market
- Domestic production structure.

(1) Philippine Ginners Are Producing About 20,000 Bales Of Lint Per Year, With A Capacity Of Perhaps Three Times That Volume

Production consists generally of clean (strict middling), medium staple, 1 1/16" cotton, which is considered desirable by domestic textile mills. Until 1984-85, all cotton production was contracted, ginned, and marketed by PCC; however, in 1984-85 private traders entered the market and by 1986-87 the private sector handled about one-half of the total crop volume.

Cotton hectarage peaked in 1980-81 at about 17,000 hectares while production reached its highest point in 1983-84 (See Exhibit II-1). Philippine production represents only 15-20% of domestic consumption and just .025% of total world cotton production.

It has been estimated that as much as 500,000 hectares in the Philippines is agronomically suitable for cotton production. Practical considerations, including traditional cropping patterns and irrigation availability, will set the upper limits at a considerably lesser hectarage, however. Expansion to any area more than 50,000 hectoros is a remote possibility at best.

The potential for increased cotton production lies primarily in Southern Mindanao, where abundant land is available for expanded hectarage. Depending on the level of farmgate prices, there is also room for some expansion in Northern Luzon. The other main producing area is around Iloilo on Panay Island, with perhaps some scope for

additional cotton introduction on the neighboring island of Negros, as part of the general shift away from sugar planting.

Several factors make it difficult to accurately estimate total national cotton production or the share of cotton handled by private traders. These factors include the operational secrecy maintained by the traders, the fact that they only entered the market in 1984-85, and the changing production credit situation. The picture will be further clouded during the 1987-88 season by the withdrawal of PCC from extending production credit and their anticipated very limited purchases of cotton from farmers.

Philippine lint is cleaner than imported cotton because it is hand harvested. Milling waste averages about 5%, compared to 8% with U.S. cotton and 13% with Pakistan cotton. Hand harvesting also contributes to its homogeneity. More of the crop is apparently picked when the bolls are fully mature, which improves dyeing properties in the mills and saves on finishing costs in textile processing.

(2) The Market Structure Is Characterized By Many Small Producers And Numerous Textile Mills, While The Ginning Industry Is Confined To PCC And Five Private Ginners

Cotton production is concentrated in Northern Luzon, in the provinces of Pangasinan, Ilocos Sur, Ilocos Norte, La Union and Cagayan; in South Cotabato, Mindanao; and to a lesser extent at Iloilo, Panay.

PCC facilities include gins at San Juan, Ilocos Sur and San Fabian, Pangasinan, in Northern Luzon; and at Polomolok, South Cotabato, Mindanao. In addition, there are several private ginning operations, with the largest private ginneries owned by Northern Cotton Corporation in Northern Luzon and Mindanao Cotton Development Corporation in Southern Mindanao. There are also two smaller

trader/ginners in Mindanao and a number of private cotton traders in both areas who do not have their own ginning facilities.

Assuming a 3-month ginning season, six days per week, 12 hours per day operation, PCC's Northern Luzon gins alone have an annual capacity of about 15,000 bales, and the South Cotabato gin 18,400 bales. Double shifts and an extended season could easily double and triple these annual capacities. There is therefore substantial overcapacity for the current level of cotton production. Even with double the current volume of cotton production, the PCC gins alone could handle the entire throughput. The private ginning capacity, which has been increasing annually, exacerbates the excess capacity situation.

The textile sector consists of 300 companies. These include 89 spinning/weaving firms, 79 finishing and texturizing operations, 148 knitting, and four non-woven products firms. These firms and plants are located in Metro Manila or the immediate vicinity. Most plants use some combination of cotton, polyester, and/or rayon fibers. The textile industry consumes all of the domestic cotton produced, but imports 80-85% of its total cotton needs.

(3) Farmers Market Their Cotton Directly To PCC, Private Ginners Or To Traders

Cotton is harvested by hand, bagged in jute bags, and transported to the gins for processing. Private ginners or PCC gin the cotton, then merchandise lint to domestic mills and export the seed for further processing. The Philippines does not produce enough cotton for seed processing, which is a capital-intensive, high-volume extraction process.

PCC, due to its inherent limitations and recent problems, has found it increasingly difficult to compete with private operators although there tends to be a high degree of loyalty held by cotton

farmers toward individual PCC extension technicians. Private sector purchasers of PCC ginning operations can maintain some of this loyalty by retaining the better qualified PCC extension workers and paying competitive farmgate prices for cotton.

A modification of the PCC marketing program will be in effect for the 1987-88 crop. PCC will provide contract ginning services to traders and/or farmer cooperatives or associations for a fee of P1.50 per kg. of seedcotton, with PCC retaining the seed. Farmers will deliver seedcotton to their cooperative or to traders, who will in turn have it ginned and market it to the textile mills.

The domestic textile industry typically consumes 100,000-120,000 bales of lint per year in addition to substantial quantities of polyester and rayon. Approximately 85% of the lint used is imported, 72% from the United States. The remainder is primarily from Pakistan and Latin America, and more recently, from Australia.

Mill consumption of cotton in the Philippines constitutes 0.15% of the world total. Philippine textile firms prefer domestic lint and will purchase all that is produced at competitive world prices. The mills have, however, given no indication that they would be willing to pay a premium for domestic cotton, possibly because it accounts for only a relatively minor portion of total use -- or perhaps because PCC has never pushed for premiums. The textile industry in general prefers to invest in improved milling equipment rather than integrating backward into production or otherwise attempting to stimulate the cultivation of Philippine cotton, apparently because production is perceived as a high risk activity and the mills can obtain abundant, reliable supplies of cotton lint on the world market. There are indications, however, of growing interest by a few of the millers in ginning or other activities to encourage greater domestic production, provided conditions are right. Lucky Textiles, for example, has recently started a production credit program for growers.

(4) Domestic Lint Prices Are Tied To World Market Prices Through A Formula That Equates The Local Lint Prices With The Landed Cost Of Imported Lint

PCC grower prices for seedcotton are determined at the start of each planting season, based on an analysis of production cost with provisions for a reasonable margin of grower profit.

Purchase prices for lint are derived through a price formula determined by Cotton Marketing Advisory Committee. The domestic lint price is based on New York cotton futures adjusted to reflect actual landed cost of imported cotton. Prices are adjusted from a lint to a seedcotton basis (about 38-40% of seedcotton is lint) with ginning costs considered. Discounts are imposed for lower quality cotton, but the quality gradients are not as discriminating as, for example, in the U.S., where cotton quality varies more.

While cotton growers might obtain higher prices by retaining ownership through ginning, they are accustomed to selling seedcotton rather than lint. In addition, individual farmers generally market too little cotton to exercise any market power. Grower associations are beginning to fill this gap by contracting for members' seedcotton, custom ginning it and marketing the lint directly to the textile mills.

When import prices for cotton lint fell to very low levels during a 3-month period in early 1987, Philippine farmers and cotton traders pressed the government to raise tariffs on imported cotton from 10% to 20-30%. The domestic textile industry opposed the tariff increase but agreed to pay 10% more than the formula price for domestic cotton when the lint formula price falls below P30 per kg. This provides producers with some additional price protection while potentially subjecting the mills to higher prices on only the 15% of domestic cotton consumed, rather than on the 85% of imported cotton.

The domestic textile industry has been fostered by the GOP as an import-substitution industry with consequent imposition of protective trade barriers. In addition to an import tariff on textile fabrics, non-tariff barriers, primarily the requirement of government approval for imports, are effectively used to prevent most textile fabrics from actually entering the country, with the exception of special Muslim barter provisions. The high tariffs and barriers have led to smuggling of textiles and polyester fibers. They have also permitted production inefficiencies to persist. Recently, textile fiber and yarn import provisions were liberalized somewhat.

The textile industry has traditionally produced primarily for the domestic market. The industry in recent years has consistently lost money due to the domestic economic recession. During 1987, however, most textile millers have reportedly been operating profitably. Although the Philippine textile millers have been through some lean years, they are presently engaged in rehabilitation, improvements, and for the first time, are attempting large-scale entry into the world market.

The textile industry is operating with a high percentage of older but apparently functional equipment and a substantial amount of excess capacity. There has been a loss of mid-management and technical production personnel to other countries, resulting in a serious lack of trained people locally. The industry is now investing in training of new technical personnel as well as repair and upgrading of existing equipment, in addition to making some major investments in new plant and equipment.

Government policy has begun to focus on textile exports and several incentive programs have been initiated toward that end. The textile industry now receives immediate credits for rebates on import duties for raw materials when textile goods are exported. These credits can be used to pay any national taxes, but are most

commonly used to defray tariffs on subsequent imports of raw materials.

Bonus points are also provided for value added locally. These bonus points can be used by textile manufacturers in bidding on export quotas, which are awarded by the government. Value-added is derived from use of local labor and raw materials. The Board of Investments also provides marketing advice to textile mills and garment manufacturers to assist in export market development.

(5) Philippine Cotton Prices Are Entirely Dependent On International Cotton Prices Which Are Inherently Unstable

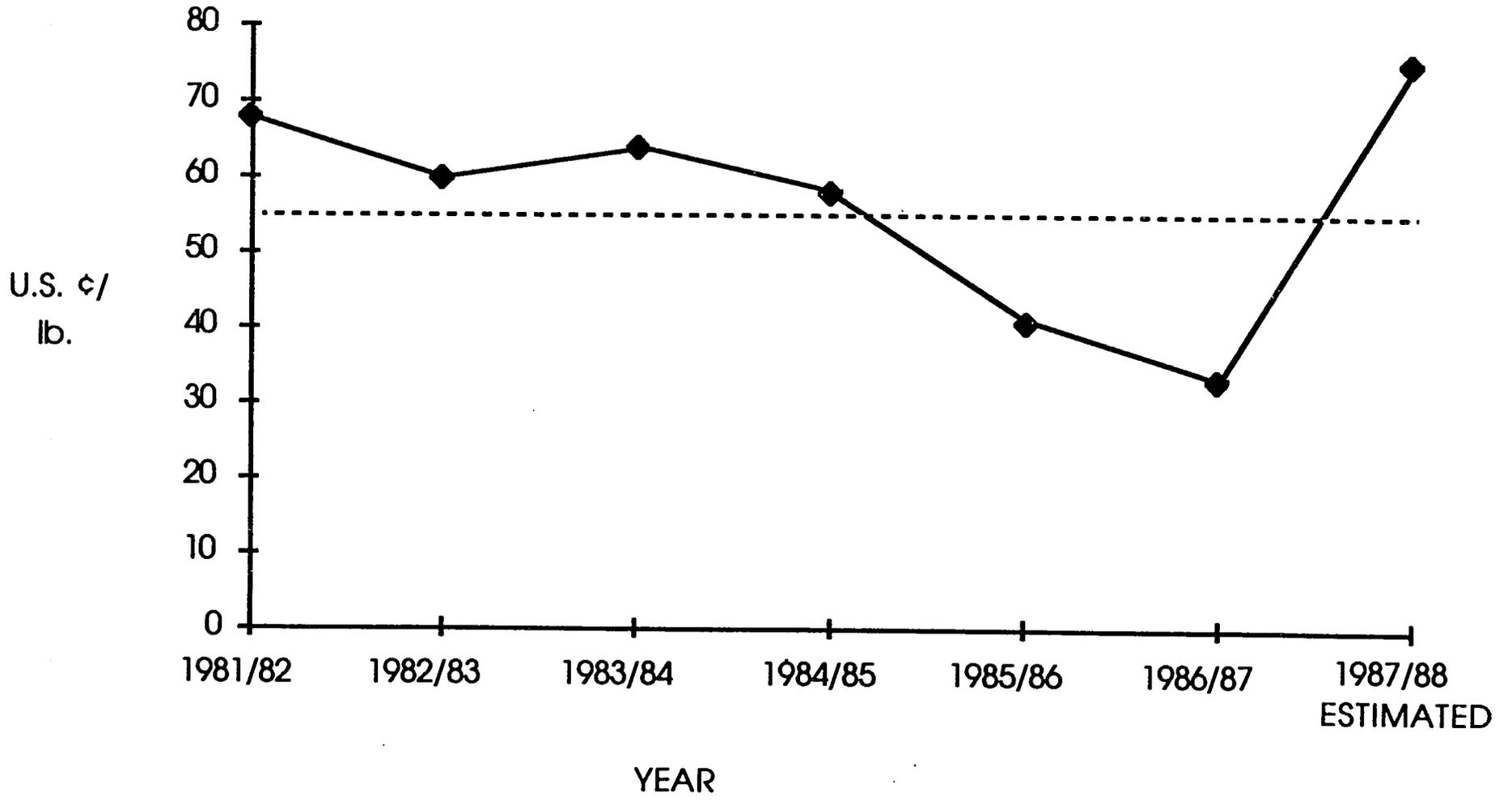
World cotton prices are subject to many supply and demand forces on a global scale. Weather patterns, land area adjustments, domestic policies in producing countries, business cycles, etc., all operate to destabilize cotton prices.

Unlike many food-source agricultural goods, cotton is an industrial input subject to greater demand variation from macroeconomic factors. Internal policies in several cotton exporting countries have accentuated the price swings, especially in more recent years. Since Philippine prices are dictated by international prices, domestic prices are and will be variable.

No one can forecast international cotton prices with a high degree of confidence, but a reasonable estimate for medium-term average price levels is US\$0.55 per pound (P24/kg.) with variations up to US\$0.20/lb. (See Exhibit II-2).

For long-term planning, the expected price is critical but understanding of the price risk is also important. Producers and producing countries must sell at the expected price and be prepared to manage the price risk. For the Philippines, it is noteworthy that price variation is dictated entirely by external forces -- the

EXHIBIT II-2
WEIGHTED AVERAGE COTTON IMPORT PRICES (FOB), BY YEAR



country does not produce enough cotton to have any identifiable effect on world prices.

(6) The Competitive Situation For Cotton As A Crop Varies With The Production Area

Of the two more concentrated areas of cotton production, Northern Luzon and Southern Mindanao, scope for expansion of cotton hectarage is greater in the latter. The reasons include:

- Mindanao has a greater area of unutilized or under-utilized land that is adaptable to cotton production
- There are fewer competing crops, and less profitable crop alternatives in Midanao.

In Northern Luzon, where more cash crops are grown than in Mindanao, cotton competes with tobacco, sugarcane, vegetables and other high-value crops for the available land. Cotton is grown as a second crop after palay and is often in a poor competitive position relative to other crops.

In Mindanao, corn-cotton rotations compete primarily with corn-corn rotation as a cash crop. Cotton, however, can produce much more net revenue per ha. than corn, as long as the farmgate price is above the breakeven cost to the farmer.

Cotton farmers in both areas tend to be very price-responsive. If the present price of seedcotton to the farmer were in the P10-12 per kg. range, it appears that maximum hectarage could be obtained in the preferred cotton-growing areas in Northern Luzon. Available hectarage in Southern Mindanao is almost unlimited, depending on farm gate prices, although an upper limit of 20-30,000 ha. is predicted for purposes of this report. Hectarage can be expected to increase progressively as the price moves up from the P7.30 per kg. paid by PCC in 1986-87, provided adequate

production credit and technical manpower are available. Although the price set by PCC for the 1987-88 season is P8 per kg., some private traders in South Cotabato were already offering P9.50 per kg. of seedcotton in October 1987.

Given an estimated world price of \$0.55 per pound of cotton lint, an efficient ginning operation should be able to generate adequate margins at a P10 per kg. farmgate price level for seedcotton. (See Exhibit II-6 and II-7 for demonstration of profitability given a farmgate price of P10 per kg.)

(7) Cotton Production And Thus The Value Of PCC Gins Depend Heavily On The Availability Of Production Credit

A major consideration for cotton production is the availability of production credit. Cotton requires a relatively high level of production inputs necessitating large cash expenses, which necessitates availability of production credit. When bank production credit became difficult to obtain starting in 1984, PCC began extending credit directly to its farmers. While most farmers repaid their loans, a problem that arose with bank loans and continued with PCC financing was the practice of "polevaulting." Some farmers instead of honoring their marketing contracts, which called for delivery of the total crop to PCC, sold their seedcotton to private traders and failed to repay their loans. The banks subsequently cut off credit to offending farmers. Other farmers repaid their PCC loans with a portion of their crop then sold the remainder at a higher price to a private trader, which had the unfortunate effect of further reducing PCC throughput. Overall loan repayments by farmers have historically averaged 90%-95%, not bad in a developing economy.

PCC stopped providing credit in 1987-88; its activities now consist of technical services, contract ginning and serving as a seed-cotton buyer of last resort. Cotton farmers, however, must

have credit to produce cotton. This credit has traditionally been obtained from the buyer of the cotton.

Credit for the 1987 crop is being extended by several private ginners and by the DA, which is using special program funds. The Land Bank is the source of much of the credit, with private ginners or farmer associations acting as conduits. The Land Bank intends to greatly expand its credit facilities in the future. The Private Sector Division or Development Bank Division of the Asian Development Bank should also be approached to develop a credit program through rural banks for cotton growers. Credit may be a long-term production constraint unless some attention is given to assure its adequacy.

(8) Private Sector Firms Have Posed Increasing Competition For PCC During The Past Three Years

The first private sector competition for PCC surfaced during the 1984-85 crop season. At present, four private ginnery operators compete with PCC for the available seedcotton supply--one in Northern Luzon and three in Mindanao:

- Northern Cotton Corporation (Northern Luzon)
- Mindanao Cotton Development Corp. (South Cotabato)
- TTK Marketing (Southern Mindanao)
- Streamline Cotton Development Corp. (Sultan Kudarat).

There are also a number of traders in both areas who purchase cotton from growers and sell it to small ginnery operators in the Manila area. In some cases, traders act as commission agents for these ginneries.

Typically, the private sector entry into ginning has been through a progression from trading seedcotton to installing a few roller gins, to converting the roller gins to saw-gins, and purchasing other pieces of modern equipment. In the case of the Mindanao Cotton Development Corporation, this entire progression has taken place over a 3-year period. The other three private ginners are at varying stages of development.

Northern Cotton Corporation (NCC) is owned by the Go family. This group is also engaged in tobacco trading, drying and merchandising, and processing of tobacco by-products, in addition to several other small-scale chemical processing activities. NCC operates primarily in Pangasinan and La Union provinces.

NCC started purchasing cotton from growers in 1984. Shortly thereafter they imported several small, simple roller gins from Thailand, which they are presently operating.

Although there is no information available on the volume of cotton processed by NCC during the 1986-87 crop year, the corporation reportedly sold some 80 tons of cottonseed. At an estimated yield of 64% seeds, this would equate to approximately 133 metric tons of seed-cotton milled, or the output of about 110 hectares with an estimated yield of 1.2 metric tons per hectare. Other sources estimate that NCC actually processed a considerably larger volume during 1986-87.

By contrast, throughput of the Pangasinan PCC mill during the 1986-87 crop season was 1,269 metric tons, including seedcotton grown for seed multiplication. Total area under contract for 1986-87 was 877 ha.

Northern Cotton also entered the Mindanao cotton growing region at the start of the 1987-88 crop season. Their approach included negotiating an agreement with PCC to contract gin an anticipated 2,000 metric tons during the 1987-88 ginning season.

Mindanao Cotton Development Corporation (MCDC) is owned by Patricio Amadeo, a South Cotabato businessman. Amadeo started buying cotton and went into the ginning business in 1984 with a few small roller gins. From this small beginning, MCDC has expanded rapidly during the past three years.

Entering the 1987-88 ginning season, MCDC was operating 12 small saw gins with an 8-hour shift per day capacity of two tons each, for a total daily capacity of 24 tons. At the peak of the season, the ginners go to a three-shift per day operation.

MCDC recently purchased a Lummus bale press. This will halve their cost of shipping lint to Manila, from P2 to P1 per kg. MCDC processed between 3,500 and 4,000 bales of seedcotton in 1986-87. Management anticipated a considerable volume increase for the 1987-88 season.

Mindanao Cotton employs field technicians to advise the farmers on production techniques and to ensure the contracted cotton is delivered to the corporation by the farmer. Each technician is assisted by a number of village leaders who are paid a small stipend during the season. As a result, each technician can supervise about 200 ha. of cotton. The technicians are paid an incentive bonus based on cotton deliveries and percent of loan repayment. These bonuses range from P0.05 to P0.12 per kg.

MCDC contracts at the start of the season for delivery of the farmer's cotton at a guaranteed floor price. This price is adjusted upward at harvest time to reflect competitive market conditions. The corporation also advances a crop production loan to the farmer with an upper limit of P3,500 per ha., at 18% per annum interest. Upon delivery of his seedcotton, the farmer receives immediate cash payment, based on delivery receipts.

Another means of increasing total volume of cotton produced is to increase yields per hectare. The history of cotton in the Philippines has generally been one of steadily decreasing yields due to extended use of one variety for planting.

This happened with the Delta Pine variety in the late 1970s and early 1980s. Reba, a Central American variety, was introduced to replace Delta Pine, but its yields are now dwindling. There is an urgent need to foster variety replacement on a regular, relatively short-term basis to maintain satisfactory cotton yields. This could perhaps be done best by a private sector firm specializing in seed sales (as San Miguel and Ayala have done with hybrid corn seed), provided enough volume could be developed to make this an attractive business proposition.

Another contributing cause to continuing declines in yields, particularly during the past three years, is the practice by the private ginners of supplying free seed to growers. Because of the expense involved, the free seed is generally not certified, and consists mostly of gin-run industrial seeds, which are often of low quality.

Wider availability of irrigation for lands planted to cotton would also provide a significant boost to overall yield and production potentials. Irrigation at present in the Philippines is reserved primarily for intensive rice production.

It appears obvious that cotton production will increase in the Philippines if the private sector moves more vigorously into the ginning industry, making appropriate investments to increase hectarage and yields. Domestic cotton is a preferred product with an assured market. World price fluctuations will affect year-to-year profit potential for the ginning industry, but given competitive farmgate pricing, and the availability of production credit and the necessary technology, farmers will continue to increase their plantings and production.

4. GROWERS CAN CULTIVATE COTTON COMPETITIVELY BUT VOLUME MUST BE INCREASED AT THE GINNERIES TO ACHIEVE AN ACCEPTABLE PER UNIT COST

This section presents two special issues which are relevant to the Philippine cotton industry:

- International competitiveness of the industry
- Viability of the industry.

(1) The Domestic Cotton Industry Can Remain Competitive As An Import Replacement Industry, But Continued Cotton Imports Will Be Required

The Philippine cotton industry appears capable of competing with imports on a cost-of-production basis. Best estimates of cotton production costs for the three countries providing most of the cotton to the Philippines, expressed in pesos are:

<u>Country</u>	<u>Fixed Cost</u>	<u>Variable Cost</u>	<u>Total Cost</u>
	- - - - -	- - - - -P/kg.lint-	- - - - -
United States	14.98	17.20	32.18
Pakistan	7.50	21.16	29.10
Australia	5.29	25.57	30.86

Source: P.A. Andrew and D.E. Ethridge, "Comparative Costs of Producing Cotton in Major Exporting Countries," Texas Tech Univ. College of Ag. Sciences Pub. No. T-1-253, July, 1987.

Note: Fixed costs represent land values; key determinant of international competitiveness is variable cost.

Variable production costs in the Philippines, by contrast, are estimated to range from P8.83 to P18.74 per kg. lint, from high production cost areas to low. Thus, Philippine costs (Exhibit II-3) compared to these suggest that domestic cotton growers can generally produce at least as efficiently as their international competitors. There are some substantial differences among different areas in the Philippines, but the same holds for competing countries. One important caveat on the above comparisons should be noted: costs are compared at an exchange rate of P20/US\$1, and the above implications hold if exchange rates are reasonably stable. Large adjustments in exchange rates can modify cost comparisons and trade patterns substantially. The Philippine peso will likely move in only one direction, however -- downward -- and further increase competitive advantage for Philippine cotton.

Because potential for expansion of cotton production is limited, imports of cotton will remain essential to supply an expanding Philippine textile industry. This fact does not, however, diminish the need for the domestic cotton industry to compete effectively for its share of the local market; otherwise its market will decrease.

(2) The Philippine Cotton Industry Is Viable If Adequate Ginning Facilities Can Be Operated At An Acceptable Unit Cost

Cotton can be produced in the Philippines at a competitive cost and its quality is generally preferred by domestic mills. But cotton production must have the infrastructure, most especially ginning facilities, to deliver lint of usable quality.

The geographic dispersal of production dictates multiple ginning sites and the limited production potential in the various areas makes small ginning plants most desirable.

EXHIBIT II-3

Cotton Production Costs by Region

	AREA		
	ILOCOS SUR	PANGASINAN	SO. COTABATO
Variable Costs (P/ha.)	7120	8611	4360
Family Labor	2015	2527	830
Hired labor	2497	1444	1414
Seed	90	90	120
Fertilizer	711	1460	610
Interest 1/	266	317	210
Chemicals	1541	2773	1176
Fixed Costs (P/ha.)			
Land	2000	2000	800
Yield (kg.lint/ha.)	380	494	494
Cost (P/kg.lint)			
Variable	18.74	17.43	8.83
Fixed	5.26	4.05	1.62
TOTAL COST	24.00	21.48	10.45

1/Assumed 11 interest on 1/2 the above expenses

SOURCE: Estimates derived in part from internal data of Philippine Cotton Corporation in 1986; and report for Philippine Cotton Corporation by the Asia Development Bank, 1985

Ginning is a high fixed-cost process, making unit cost very sensitive to volume. The smallest size of plant which can process the available volume will result in the least cost per bale.

In addition, smaller plants which are operated more hours per day and per season are more energy efficient on a unit basis than larger plants operated fewer hours. Energy is a very expensive input in the Philippines. Consequently, the excess ginning capacity in the industry implies a lower value for the PCC gins based on their residual productive value than if the plants conformed more closely to local ginning requirements.

5. PCC ASSETS INCLUDE LAND, BUILDINGS AND THREE GINNING PLANTS WHICH HAVE BEEN WELL MAINTAINED AND ARE IN EXCELLENT CONDITION

This section identifies and cites the condition of the various physical assets presently held by PCC. These assets consist of land, land improvements, buildings, three cotton ginning plants, vehicles, an airplane and various miscellaneous pieces of equipment.

(1) Cotton Ginning Equipment At The Two Ginneries In Northern Luzon Has Been Well Maintained And Is In Good Condition

The major physical assets consist of:

- Approximately 69 hectares of land owned by PCC in the provinces of Tarlac, Ilocos Sur, Cagayan, and Pangasinan
- Two cotton ginneries located at Barrio Alacan, San Fabian, Pangasinan; and at Barrio Labnig, San Juan, Ilocos Sur.
- Warehouses and miscellaneous structures at San Juan, Ilocos Sur; Solana, Cagayan; and San Fabian, Pangasinan.

- Vehicles and other miscellaneous equipment, with the majority of such equipment at San Fabian.
- An airplane.

Title to the land in the above four locations is held by PCC. The property at Victoria, Tarlac, consisting of 15 hectares, is presently undeveloped, but is suitable for cropping with either sugarcane or rice, the crops most widely grown in the area. Since the property is situated adjacent to a main provincial road, it might also be suitable for commercial purposes.

The property at San Juan covers approximately 16.6 ha., including a demonstration farm of 16 ha. utilized by the Cotton Research and Development Institute (CRDI). The demonstration farm is suitable for growing cotton, vegetables, rice or other crops. Structures on the property include an administration building, the ginney, a warehouse, experiment station and miscellaneous buildings. It is bordered by a national highway.

The cotton ginning equipment consists of:

- Two 90-saw gin stands
- Lint cleaner and drier
- Bale press system
- Related equipment.

This equipment was originally owned by a private cotton ginning enterprise in south Cotabato, which failed. Capacity is four bales per hour.

The equipment is reportedly about 40 years old and was donated to PCC for installation at San Juan. The gin was operated by PCC

for a total of only two months in 1985, and according to knowledgeable sources, was used for a relatively short period by the original owners. Thus, the equipment, although antiquated, is in very good condition. It has been well maintained by PCC.

The PCC-owned property at Solana, Cagayan, consists of nine hectares, with a small administration building and miscellaneous structures. The land is well-suited to rice cultivation as well as other crops.

The San Fabian, Pangasinan property includes 4.66 ha. It is the location of the PCC regional headquarters for Northern Luzon and the only site on Luzon where PCC field activities are still being carried on. Buildings include an administrative office, ginnery building, two single and one twin warehouses and miscellaneous structures. There are 17 motor vehicles currently assigned to the operation.

The ginning plant consists of:

- Two 128-saw Lummus gin stands
- Two lint cleaners
- Seedcotton drier
- One standard density bale press
- One low density bale press
- Related equipment.

Lummus supplied all of the ginning equipment, which was installed in 1976. Capacity is 12 bales per hour. The plant has been well maintained and is in very good condition. The drier and lint cleaners have been used very little because the cotton

delivered contains almost no waste. It is possible that one of the bale presses could be sold off separately, since one press will handle the projected output of this plant. There is a lien on the equipment held by DBP as collateral for a P725,000 loan to PCC.

The San Fabian property is located adjacent to a national road, and other roadways in the vicinity are generally very good. The majority of the land is utilized for the existing buildings and improvements.

(2) The South Cotabato Ginnery Includes Late Model, Large Volume Ginning And Related Equipment Which Is In Excellent Condition

The site at Polomolok, South Cotabato, consists of 23.86 ha. Buildings include an administration building, ginnery building, two warehouses and miscellaneous structures.

Most of the ginning equipment was supplied by Lummus.

- Two 158-saw gin stands
- Three lint cleaners
- Standard density bale press
- Three wire tie baler
- Related equipment
- Two cotton module builders, supplied by HYFAB of Australia
- Unassembled double roller gin (Indian origin).

The two 158-saw stands and other ginning equipment was installed in 1983 and 1985. Plant capacity is 16 bales per hour.

The Indian rolling mill and various other pieces of equipment from a defunct private cotton ginning operation in South Cotabato are stored under tarpaulins in one of the warehouses.

All of the operating equipment has been well maintained and is in excellent condition. In addition to cotton handling and ginning equipment, there are seven Komatsu fork lift trucks and two International Harvester 64-hp. diesel tractors; as well as 16 road vehicles.

There is also a 10-hectare experimental farm at the site, which is operated by CRDI.

(4) PCC's Airplane Is In Excellent Condition And Can Be Used In Government Operations, Or Sold

The aircraft owned by PCC is a Beechcraft Kingaire 100. This nine-passenger, fixed wing aircraft was purchased new in 1974. It is in excellent condition. An appraisal made in late 1985 valued it at US \$750,000.

6. OPERATING COSTS OF PCC ARE TOO HIGH FOR PROFITABLE OPERATION, AND THE CORPORATION HAS INCURRED A HEAVY DEBT BURDEN, DESPITE SUBSTANTIAL GOVERNMENT SUBSIDIES

The financial performance of PCC is shown in the historical income statements and balance sheets in Exhibits II-4 and II-5 respectively. In comparing historical annual financial data, it is important to note the high inflation experienced in 1983 and 1984. Thus, growth in income and expense accounts over that period does not necessarily indicate a real growth in economic activity.

Exhibit II-4

PHILIPPINE COTTON CORPORATION
 STATEMENT OF INCOME AND RETAINED EARNINGS (IN PESOS)
 Calendar Years 1975-1980

	1975	1976	1977	1978	1979	1980
	----	----	----	----	----	----
Sales	486,173	3,693,297	7,753,997	10,302,547	15,053,833	52,725,428
Cost of Goods Manufactured & Sold	324,883	2,486,615	5,546,744	7,482,980	9,894,655	32,832,655
Gross Profit from Sales	161,290	1,206,682	2,207,253	2,819,567	5,159,179	19,892,773
Operating Expenses	121,228	1,231,639	2,268,296	4,065,421	3,248,154	4,720,480
Net Income (Loss) from Operations	40,063	(24,956)	(61,043)	(1,245,854)	1,911,024	15,172,293
Other Income (Charges)						
Interest Income (Charges)-Net	144,497	(96,473)	341,068	650,228	(358,046)	(1,329,358)
Production & Extension Expenses		(608,691)	(706,422)	(1,532,213)	(2,269,798)	(4,668,415)
Research & Development Expenses	(310,357)		(433,851)	(442,602)		(15,000)
Corporate Farm Proj. Exp.						
Other Expenses		(136,492)			(12,073)	(233,821)
Total Other Income (Charges)	(165,860)	(841,656)	(799,205)	(1,324,587)	(2,639,918)	(6,246,594)
Net Income (Loss) for the Period	(125,797)	(866,612)	(860,248)	(2,570,441)	(728,893)	8,925,698
Provision for Income & Development Taxes	(17,020)					(1,472,388)
Net Income (Loss) after Income & Development Taxes	(142,817)	(866,612)	(860,248)	(2,570,441)	(728,893)	7,453,310
Add: Interest Income Subject to Final Tax (net)						
Net Income before Subsidy Extension Subsidy from the National Government	(142,817)	(866,612)	(860,248)	(2,570,441)	(728,893)	7,453,310
Net Income after Subsidy	(142,817)	(866,612)	(860,248)	(2,570,441)	(728,893)	7,453,310
Retained Earnings at the Beginning of the Period		(142,817)	(1,009,429)	(1,869,677)	(4,440,119)	(5,169,012)
Correction of Prior Years' Profit						
Retained Earnings at the End of the Period	(142,817)	(1,009,429)	(1,869,677)	(4,440,119)	(5,169,012)	2,284,298

Exhibit II-4 (Continued)

PHILIPPINE COTTON CORPORATION
STATEMENT OF INCOME AND RETAINED EARNINGS (IN PESOS)
Calendar Years 1981-1986

	1981	1982	1983	1984	1985	1986
	----	----	----	----	----	----
Sales	86,785,708	110,745,946	104,506,968	207,569,625	71,766,229	68,994,109
Cost of Goods Manufactured & Sold	65,578,164	96,457,216	69,265,480	87,930,076	47,144,345	72,535,242
Gross Profit from Sales	21,207,544	14,288,730	35,241,489	119,639,550	24,621,884	(3,541,133)
Operating Expenses	11,694,444	13,089,517	10,952,055	17,430,835	18,795,185	12,757,865
Net Income (Loss) from Operations	9,513,100	1,199,213	24,289,434	102,208,715	5,826,699	(16,298,999)
Other Income (Charges)						
Interest Income (Charges)-Net	(8,104,869)	(21,856,239)	(21,345,781)	(67,034,186)	(41,372,351)	(49,126,123)
Production & Extension Expenses	(806,697)	(4,016,810)	(2,371,175)	(32,005,040)	(19,589,887)	(17,755,065)
Research & Development Expenses		(66,273)	(362,359)	(792,842)	(1,944,944)	(2,978,555)
Corporate Farm Proj. Exp.						(1,145,938)
Other Expenses	(105,276)	(12,073)	(12,073)	(12,073)	(6,037)	
Total Other Income (Charges)	(9,016,842)	(25,951,396)	(24,091,387)	(99,844,141)	(62,913,219)	(71,005,682)
Net Income (Loss) for the Period	496,258	(24,752,182)	198,047	2,364,574	(57,086,520)	(87,304,681)
Provision for Income & Development Taxes	(22,192)		(59,316)	(817,601)		
Net Income (Loss) after Income & Development Taxes	474,065	(24,752,182)	138,730	1,546,973	(57,086,520)	(87,304,681)
Add: Interest Income Subject to Final Tax (net)				20,577,963	18,525,566	6,590,288
Net Income before Subsidy	474,065	(24,752,182)	138,730	22,124,936	(38,560,954)	(80,714,393)
Extension Subsidy from the National Government				12,128,824	9,354,000	
Net Income after Subsidy	474,065	(24,752,182)	138,730	34,253,760	(29,206,954)	(80,714,393)
Retained Earnings at the Beginning of the Period	2,284,298	2,737,017	(29,608,317)	(26,898,026)	2,584,940	(19,851,098)
Correction of Prior Years' Profit	(21,346)	(7,593,151)	2,571,561	(4,770,794)	6,770,916	(5,223,307)
Retained Earnings at the End of the Period	2,737,017	(29,608,317)	(26,898,026)	2,584,940	(19,851,098)	(105,788,797)

Exhibit II-5

Philippine Cotton Corporation Balance Sheets
 Calendar Years 1975 - 1980
 (1,000's of Pesos)

Assets	1975	1976	1977	1978	1979	1980
.....
Current assets						
Cash on hand and in banks	40	290	8,110	9,630	7,270	7,660
Investments	320	1,650	2,000	6,940		
Trade accounts and notes receivable	320	1,070	1,810	2,180	7,970	25,160
Other receivables	40	70	20	30		
Other inventories - finished goods		340	50	150	70	340
raw materials			20	110	70	70
supplies		50	70	90	340	1,230
Other current assets	610	210	1,110	220	260	940
	-----	-----	-----	-----	-----	-----
Total current assets	1,330	3,680	13,190	19,350	15,980	35,400
Property, plant and equipment - gross	10	2,690	3,960	8,700	12,520	14,200
Less: accumulated depreciation		90	360	840	1,600	2,520
	-----	-----	-----	-----	-----	-----
Property, plant and equipment - net	10	2,600	3,600	7,860	10,920	11,680
Other assets	120	960	2,180	8,170	13,190	18,330
	-----	-----	-----	-----	-----	-----
TOTAL ASSETS	1,460	7,240	18,970	35,380	40,090	65,410
	=====	=====	=====	=====	=====	=====
Liabilities						
Current liabilities						
Accounts payable and accrued expenses	80	2,950	80	190	790	2,200
Notes payable						5,000
	-----	-----	-----	-----	-----	-----
Total current liabilities	80	2,950	80	190	790	7,200
Long term debts		2,300	2,300	2,300	2,180	2,050
Other liabilities	520	190	9,280	17,650	17,610	13,200
	-----	-----	-----	-----	-----	-----
Total liabilities	600	5,440	11,660	20,140	20,580	22,450
Stockholders' equity						
Paid in capital	1,000	1,810	7,930	18,430	23,430	39,430
Donated capital		1,000	1,250	1,250	1,250	1,250
Retained earnings	(140)	(1,010)	(1,870)	(4,440)	(5,170)	2,280
	-----	-----	-----	-----	-----	-----
Total stockholders' equity	860	1,800	7,310	15,240	19,510	42,960
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	1,460	7,240	18,970	35,380	40,090	65,410
	=====	=====	=====	=====	=====	=====

Exhibit II-5
(Cont.)
Philippine Cotton Corporation Balance Sheets
Calendar Years 1981 - 1986
(1,000's of Pesos)

Assets	1981	1982	1983	1984	1985	1986
.....	----	----	----	----	----	----
Current assets						
Cash on hand and in banks	1,720	11,200	36,710	39,960	36,810	21,800
Investments		12,000	65,050	108,990	58,140	13,040
Trade accounts and notes receivable	88,190	142,680	98,440	64,760	83,580	56,930
Other receivables	3,500	2,680	2,830	5,930	6,520	7,720
Other inventories - finished goods	2,220	370	490	1,310	11,580	670
raw materials	80		20	620	1,810	9,050
supplies	5,590	7,440	6,710	5,350	6,360	6,910
Other current assets	14,650	4,530	880	490	33,390	60
	-----	-----	-----	-----	-----	-----
Total current assets	115,950	180,900	211,130	227,410	238,190	116,180
Property, plant and equipment - gross	36,490	52,450	62,240	66,520	82,210	85,680
Less: accumulated depreciation	5,410	9,820	14,850	20,200	27,230	33,770
	-----	-----	-----	-----	-----	-----
Property, plant and equipment - net	31,080	42,630	47,390	46,320	54,980	51,910
Other assets	31,490	48,260	49,920	50,370	54,700	39,470
	-----	-----	-----	-----	-----	-----
TOTAL ASSETS	178,520	271,790	308,440	324,100	347,870	207,560
	*****	*****	*****	*****	*****	*****
Liabilities						
Current liabilities						
Accounts payable and accrued expenses	740	7,420	14,210	25,840	23,690	29,690
Notes payable	110,000	219,100	239,420	204,420	177,020	120,020
	-----	-----	-----	-----	-----	-----
Total current liabilities	110,740	226,520	253,630	230,260	200,710	149,710
Long term debts	1,890	1,710	4,280	10,600	75,400	77,030
Other liabilities	13,240	13,260	13,470	18,780	24,740	18,880
	-----	-----	-----	-----	-----	-----
Total liabilities	125,870	241,490	271,380	259,640	300,850	245,620
Stockholders' equity						
Paid in capital	48,660	58,660	62,960	62,970	62,970	62,970
Donated capital	1,250	1,250	1,000	1,140	3,780	4,580
Retained earnings	2,740	(29,610)	(26,900)	350	(19,730)	(105,610)
	-----	-----	-----	-----	-----	-----
Total stockholders' equity	52,650	30,300	37,060	64,460	47,020	(38,060)
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	178,520	271,790	308,440	324,100	347,870	207,560
	*****	*****	*****	*****	*****	*****

As indicated by the level of sales revenue, the years 1975 through 1979 represented a start-up and experimental period. During that period, both assets and liabilities, as shown on the balance sheets, remained at low levels. Sales increased markedly in the period from the 1979 level of P15.1 million to P110.7 million in 1982. This represents an average compound annual growth rate of nearly 95%. Over the same period total assets grew at a comparable rate.

The large volume of sales in the years after 1981 indicates the growth of operations of PCC. However, sales revenue declined in 1985 and 1986 when lack of credit availability caused a substantial decrease in the hectareage of cotton planted and an even greater decrease in volume of cotton delivered to PCC.

Because of the volatility of cotton prices on the world market, the gross margin percentages of the PCC varied substantially from year to year. Gross margins have typically been in the range of 25% to 35% of sales revenue. However, this percentage was as high as 57% in 1984 and as low as a negative 5% in 1986. Operating expenses varied somewhat with total expenses, but as a percentage of sales revenue, they decreased with increasing volume.

Due to the extraordinarily high price of seedcotton compared to the price of lint, PCC experienced an enormous operating loss in 1986. In all other years since 1978, income from operations was positive. However, expenses listed in the "other income" portion of the income statement have been so large as to put PCC in the position of breaking even at best, and incurring large losses typically. The heading for "other income" is somewhat misleading since nearly all items in this category are negative amounts; thus, they are mostly expense items. The largest element in the "other income" category is interest. This became a significant item when the capital expansion began. The net interest expense was substantially increased when PCC was providing subsidized financing to farmers in 1985 and 1986. The worst condition occurred when PCC

was borrowing funds at 36% per annum, and lending to the farmer at 12% per annum.

The other significant item under "other income" is "production and extension" expense. The figures shown on the income statements are not consistent, as some years show this amount net of government subsidy. The exclusion of extension and production expenses from operating expenses could be misleading as to the importance of this activity. Since extension services are critical to assure a reliable supply of seedcotton, the cost of operating the service should be regarded as an operating expense.

Over the years that PCC has operated, the pre-tax income has generally been negative. In four of the twelve years of reported financial statements, the pre-tax income was positive, but in two of those years the amount was so small as to represent a virtual break-even situation. In 1985 and 1986 the losses became enormous, both in absolute terms and as a percentage of sales. While much of the loss in 1986 was attributable to the effect of cotton prices in the world market, it is nevertheless apparent that a cost structure was in place that would preclude PCC from operating profitably over the long term.

The balance sheets of PCC reflect a dismal financial performance over the past ten years. Retained earnings have rarely been positive, and in 1986 retained earnings were so largely negative that the corporation showed negative equity. Because of the discrepancy between the ginning season and the financial reporting year (calendar year), short-term balance sheet accounts could fluctuate substantially at the closing period. However, it is interesting to note that in half of the past six years, current liabilities have exceeded current assets, indicating a liquidity problem.

Total assets have increased with the increased level of sales revenue. As of 1986, the net fixed assets constituted 25% of total

assets. Because of underutilization, the net book value of the fixed assets is believed to overstate their market value. If a true market value were substituted for the net book value, the asset and equity values would probably be lower.

As of 1986, total liabilities stood at P245.6 million, with notes payable representing almost 58% of this total. These were mostly lines of bank credit. Based upon the relatively low level of long-term debt and the low current ratios (current assets/current liabilities), it appears that PCC relied predominantly on short-term loans for the debt portion of the corporation's capital.

PCC has never paid a dividend on its equity. Instead, it has received substantial new equity inputs throughout its history. The table below shows the cumulative paid-in capital from the PCC balance sheets, the GOP share of that amount, and the annual contribution by the GOP. Also shown are the subsidies provided by the government for operation costs and the seedcotton fund.

Government Investment and Subsidy
 Philippine Cotton Corporation
 (000's of Pesos)

Year	Total Paid In Capital	GOP Share Paid In Capital	GOP Equity Yearly Contrib.	Prod. & Extension Subsidy	Seedcotton Fund Subsidy
----	-----	-----	-----	-----	-----
1975	1,000	600	600		
1976	1,810	1,266	666		
1977	7,930	7,266	6,000		15,000
1978	18,430	17,666	10,400		2,600
1979	23,430	22,766	5,100		
1980	39,430	38,766	16,000		(5,000)
1981	48,660	43,766	5,000	10,000	
1982	58,660	53,766	10,000		
1983	62,960	53,766		12,953	
1984	62,970	58,066	4,300	12,129	
1985	62,970	58,066		9,354	
1986	62,970	-----	Data Unavailable -----		
Total			58,066	44,436	12,600

The source of all data on this table except total paid in capital was an internal report by PCC. There appear to be an

inconsistency, inasmuch as the PCC figures indicate an equity contribution of P4.3 million in 1984, but the total paid-in capital on the balance sheet did not change from 1983 to 1984.

Because of the high level of inflation that the Philippines has experienced, direct comparison of the historical subsidies is not appropriate. Nevertheless, it is obvious from the totals through 1985 that the government input into PCC has been substantial. Further, these figures do not reflect the effects of the financially disastrous year of 1986.

The direct subsidies from the government are not reflected in the balance sheets, so they are not included as capital contribution. They appear on the income statements as a direct revenue, or as an offset to expenses. As such, the cost to the government is somewhat hidden in the financial statements, and serves to make the income statement more favorable than the actual business enterprise warrants.

PCC has a significant amount of outstanding debt obligations that will require resolution upon its privatization. These obligations appear on the balance sheets as notes payable and long-term debt. The debt, as of September 1987, is summarized below.

Summary of PCC Debt

Philippine National Bank	P55	million
Land Bank of the Philippines	30	million
Union Bank	25	million
Development Bank of the Philippines	21.26	million
Asian Development Bank	76.3	million

Accrued interest	19.5 million

Total	P222.4 million

The amount of the obligation to the Development Bank of the Philippines (DBP) is in dispute. The DBP claims an additional obligation of P27 million is owed as a result of defaults by textile millers.

7. THERE ARE SEVERAL PRIVATIZATION OPTIONS FOR PCC FACILITIES INVOLVING EITHER PUTTING THEM UP FOR BID AS OPERATING CONCERNS OR FOR REMOVAL

Based on its field visits, the Project Team has concluded the following:

- All privatization plans should include closing of the headquarters of the PCC, which is leased for four more years
- The sale of the two northern facilities in San Juan, Ilocos Sur, and San Fabian, Pangasinan, must be considered jointly because their locations imply that they will compete for the same raw material supplies
- The facility in South Cotabato should be considered as a separate entity, but it is too large for the production potential of the area
- The Department of Agriculture and the APT should require that PCC going-concern purchasers retain a number of key local personnel, at least for a time, because they embody the cotton cultivation, pest control and ginning technology as well as farmer contacts

- All outstanding liabilities should be transferred to the Department of Finance for settlement. According to PCC management, no legal impediments bar the sale of PCC facilities; however, it was learned that title to the land of the Polomolok facility has not yet been granted to PCC by the Bureau of Lands, although the title granting process is reportedly underway.

(1) There Are Three Privatization Options For The San Juan and San Fabian Facilities

Although the San Juan facility is currently shut down, its location within the raw material sourcing area of the San Fabian operation means privatization strategies for both facilities must be inter-related. The land area of farmers growing cotton in the San Juan area for PCC's San Fabian ginnery is presently 300 hectares.

The privatization options and valuation implications are as follows:

<u>Option 1</u>	<u>Valuation Implications</u>
Liquidate and relocate San Juan ginning equipment	Lower than replacement value -- even though the equipment was originally donated
Bid out San Fabian facility	Price would be based on current and potential operations

Option 2

Bid out San Juan facility

May not have value due to limited potential operations

Bid out San Fabian facility

Price would be lower than "going concern value" under Option 1

Option 3

Liquidate San Juan facility

Lower than replacement value

Liquidate San Fabian facility

Lower than acquisition value, and certainly lower than the "going concern" value.

Liquidating either of these facilities by selling off key items of equipment will leave the gin buildings, warehouses and office facilities for sale or lease for tobacco or rice warehousing operation. The gin buildings will require modification by the buyer because the ginning equipment installations extend below the floor level. Liquidating either of the operations would not result in the facility left in operation becoming a monopoly. Northern Cotton Corporation is an active competitor; however, a monopoly situation could be created if NCC buys the facility.

(2) There Are Two Options For The General Santos Ginnery:
Selling Its Assets Or Selling It To An Off-Shore Buyer

The two options for this facility include:

- Liquidate it and sell it to an off-shore buyer, such as the People's Republic of China
- Put the assets of the facility up for bids.

The valuations presented below in Section 8 consider both options.

(3) The APT Should Require The Buyers Of These Facilities To Retain Several Key Groups Of Employees

We recommend that the following key groups of employees be retained by private sector buyers of going concerns:

- Extension specialists, based on approximately one per every 50 hectares of cotton
- Permanent ginnery personnel
- A reduced number of accounting personnel
- Guards.

These personnel should be retained by the private sector buyer for at least 12 months, adequate time to determine their productivity. After that period the buyer would be free to release them from employment.

The Department of Agriculture has expressed a willingness to absorb the maximum number of employees not employed by the private sector buyers. This would reduce employment impacts altogether, if the DA can obtain budgetary support for such a move.

(4) All Outstanding Notes And Loans Payable Should Be Transferred To The Department Of Finance For Write-Off Or Payment

There are notes and loans payable by PCC amounting to P207.9 million plus P19.5 million accrued interest payable. The APT presently holds the PNB and DBP loans. As soon as PCC is sold by the APT, the Land Bank, Union Bank and ADB liabilities should be transferred to the DF.

(5) Only One Legal Impediment Exists To Bar Privatization Of The Ginning Facilities

There are, according to PCC management, no outstanding lawsuits, liens, or other legal complications that would prevent the sale of PCC assets. It was learned, however, that the land under the Polomolok ginnery was originally homestead land, which was legally not saleable to a corporation. The law was changed recently, however, to allow this. PCC has a clean bill of sale for the land and expects the Bureau of Lands to award title to them in the near future.

Once a decision has been made concerning the establishment of an authority to promote cultivation of cotton including its size and location as well as clarification of the future status and scope of CRDI, it may be possible to vacate the presently leased headquarters building. It is highly unlikely that a private sector buyer of the ginning facilities would want to assume this lease. Several floors of the PCC headquarters buildings are now sub-leased. Conceivably the entire space can be sub-leased for the next four years, until the PCC lease runs out.

(6) Careful Timing Of The Divestitures Will Maximize Their Sales Prices

Because it is currently shut down, the San Juan facility can be put up for bids immediately. However, as the assets of the other two ginning facilities are to be sold as "going concerns," they should be put out for bids once the harvest season is well underway. The potential buyers should be given ample time to visit the plant while ginning operations are going on and -- most importantly -- have an opportunity to discuss cultivation questions with the farmers and operating questions with the personnel employed at these ginneries, so that they can better assess the viability of the operations.

8. VALUATIONS FOR THE GINS WERE DEVELOPED USING DISCOUNTED CASH FLOW ANALYSES AND WORLD EQUIPMENT MARKET ANALYSES

The valuation of PCC assets is based, in part, upon the value of ongoing business concerns. The valuation of business enterprises of PCC has been conducted using the discounted flow analysis technique. This method requires that certain assumptions be made to project future earnings and cash flow. This section details assumptions that were made for the analyses. The world equipment market analyses are included in Appendix G of this report.

(1) Expected Average Commodity Prices And Costs Are Estimated To Grow At A Long-Term Inflation Rate Of Seven Percent

An important assumption is that expected long-term inflation in the Philippines will be 7.0% per annum. This inflation rate is generally used to project the growth of all revenue and expense rates. The rationale for projecting expense rates to grow at the long-term inflation rate is straightforward. Since the inflation rate is composed of such elements as cost of labor, supplies, power,

and transportation, it is reasonable to expect that cost of these items will reflect the Philippines inflation rate.

It is also assumed that revenues will grow at the long-term Philippines inflation rate. However, world cotton prices are affected by many factors other than world inflation (which is likely to be different from inflation in the Philippines). Cotton prices do not directly reflect inflation, but show wide variations from year-to-year. World lint prices between 1986 and 1987 went from less than \$0.20 per lb. to more than \$0.70 per lb., for example. It is not possible to predict cotton prices over the long-term with any reasonable degree of precision. Thus, since the price is expected to show considerable fluctuation, and it is necessary to project some increase in price to match anticipated increases in costs, an inflation-related price increase is deemed to be as appropriate as any other measure that might be arrived at.

The landed cost of imported cotton lint is calculated by using a formula established by the Board of Investment (BOI). This is the price that is paid by the textile millers for delivered lint. The table below shows the calculation of the landed cost of imported lint assuming a world market price of US\$ 0.55 per pound (as derived in Exhibit II-2). Using indicated conversion rates, this is equivalent to P25.10 per kilogram. A ten percent import duty is added.

An advance sales tax is calculated based upon the import price. It is assumed that a 25% markup will be imposed by the importer. Thus the projected sales price is calculated by adding the commodity import price and the import duty, and multiplying that sum by 1.25. This total is multiplied by 10% to calculate the advance sales tax.

An additional allowance is made for incidental expenses such as brokerage fees, licenses, and commissions. For the purposes of this analysis, these incidental fees and commissions are assumed to be

10% of the total import price including import duty and advance sales tax. The calculation results in an assumed lint price of P34.17 per kilo.

Estimate of Unit Revenue
for Cotton Lint

Price per pound (\$)	0.55
Peso/US\$1	20.70

Price per pound (Pesos)	11.39
Kilos/pound	2.2046

Commodity price per kilo	25.10
Add 10% duty	2.51

Price plus duty	27.61
 Advance sales tax calculated as 10% of price plus duty and 25% markup	 3.45

	31.06
Add 10% misc. fees and commissions	 3.11

Landed cost estimate pesos per kilo	 34.17

Cotton seeds are sold as a by-product of the ginning operation. While also subject to world market conditions, the assumed price of seeds is not as critical to the valuation analysis as the price of lint, because seed sales represent a much smaller portion of the total revenue generated. The selling price of seeds

is estimated at P1.70 per kilo, increased annually on the basis of projected inflation rate.

An estimate of yields of both lint and seeds from the ginning process is necessary to project revenue from sales of the two products. Based upon historical performance, and the existing ginning technology at the ginneries, it is estimated that yield of lint will be 39% of input seedcotton weight, with seed yield projected at 60%. This implies a 1% waste rate.

(2) A Weighted-Average Cost Of Capital Is Projected Based On Estimated Rates Of Return On Equity And Debt

Several financial assumptions are necessary for the discounted cash flow analysis. Included are assumptions regarding investment rates, capital structure, and the value of the enterprise at the end of the ten-year projection period.

Since the discounted cash flow analysis determines an amount that can be paid by a buyer expecting a fair return on investment, it is necessary to establish a required return on capital (real discount rate). A weighted-average cost of capital (WACC) is used as the rate of return required on the business enterprise. The formula for the WACC is:

$$WACC = S \times (1-L) + B \times L \times (1-T)$$

where

S = Equity rate of return

B = Debt rate of return

L = Percentage of capital financed by debt

T = Income tax rate

For the business opportunities of PCC, a rate of return on equity of 27% per annum is considered appropriate. This is a relatively high rate, reflecting the inherent riskiness of the business due to the commodity price risk involved. The long-term debt rate is projected as 20%. Based upon discussions with commercial bankers, it is assumed that 60% of the purchase price of PCC assets could be financed as debt. The corporate income tax rate in the Philippines is 35%. These assumptions yield a calculated WACC of 18.6%. It is assumed that the value of the business enterprise at the end of the ten-year projection period will be four times the annual cash flow in the tenth year.

(3) Depreciable Assets Are Assumed To Be 65% Of Total Assets
And To Have 20-Year Lives

In calculating income taxes in the DCF analysis, it is necessary to project depreciation expenses for existing assets. This creates a problem, since some assets, such as buildings and machinery, are depreciable, while other assets, such as land, are not. Since the purchase price of the privatized business is expected to be well below the book value, it is not entirely clear how the allocation would be made between depreciable and non-depreciable assets. Discussions with officers of the Bureau of Internal Revenue indicated that such a situation would be negotiated with the new buyer on an individual case basis. A reasonable allocation for this analysis is that 65% of the assets are depreciable, and 35% are non-depreciable.

With appropriate maintenance, major ginnery equipment has a relatively long life. Both buildings and the machinery are assumed to be depreciated for 20 years on a straight-line basis, with no residual value assumed.

Depreciation of new assets is based on the capital expenditures projected in the DCF analysis. New assets are assumed to have useful lives of five years and are depreciated over a 5-year period using the straight-line method. Capital expenditures are assumed to be two percent of sales revenue. Because of currently sufficient stock of capital equipment, however, it is assumed that no capital expenditure will be required for the first two years of the projection.

It is assumed that average net working capital will be two percent of annual purchases. It is also assumed that the business will be sold with no working capital in place. Thus, the buyer will be required to supply an infusion of working capital in the first year. In subsequent years, smaller infusions of cash will be required to meet the additional needs for working capital caused by the increase in sales revenue.

(4) San Fabian Ginnery Valuation Assumptions Are Based On Historic Operating Costs And Projections Based On Changes Resulting From Privatization

Two key assumptions for the valuation are the the price paid for seedcotton and the amount of seedcotton purchased. These assumptions are closely interrelated, due to the apparent sensitivity of the farmer to cotton prices. In the analysis, it is assumed that the farmgate price for cotton will be P10 per kg. in the first year, and the amount will grow at the projected rate of inflation. At this price, it is conservatively assumed that a total of 4,000 hectares of cotton will be planted in the area, and that 50% of the production will be purchased by the privatized operations of PCC. While this amount of planting has been exceeded in the past, it represents an increase over current planting levels. As such, it is assumed that higher farmgate prices will gradually induce more planting until the full hectarage is achieved in the third year of the projection. The hectarages for the first and

second years are projected as 60% and 80% of the long-term hectarage, respectively.

An analysis of historic operating costs along with projections of probable changes upon privatization were conducted to establish projections for operating costs. Some of these costs were assumed to be fixed, some variable, and some semi-variable. In all cases, both the fixed portion and the variable rate were assumed to grow at the long-term inflation rate. The operating expense assumptions for the first projected year are detailed below.

San Fabian Ginnery
1988 Cost Assumptions
(Pesos)

	Fixed Costs	Variable Costs
Ginning Costs	451,000	0.88 x kilos of lint
Handling and Warehousing	340,000	0.54 x kilos of lint
Freight	-	0.25 x kilos of seedcotton 0.30 x kilos of lint 0.20 x kilos of seeds
Extension Services	905,000	0.168 x hectares supplied 0.015 x seedcotton purch.
General & Administrative	961,000	-

Ginning costs are projected to include costs of labor, supplies, power and their utilities, and insurance, all based upon historical data and projected future cost estimates. Depreciation expense and capital cost of equipment is excluded from the ginning

cost because the historical depreciable basis is considered irrelevant to the financial operations of the privatized firm. Instead, depreciation is calculated separately as a non-cash expense, based upon the expected sale price of the business, as described earlier in this section.

Exhibit II-6 shows the discounted cash flow analysis for the San Fabian ginnery, based upon the foregoing assumptions. The concluded value is P11,232,000.

(5) Polomolok Ginnery Valuation Assumptions Are Derived In The Same Fashion As Those For The San Fabian Ginnery

The analysis of the Polomolok ginnery is very similar to that of the San Fabian ginnery. The major differences are in the projected revenue totals and some operating costs. The revenues differ because of the greater hectarage of cotton estimated available for purchase in Southern Mindanao, as opposed to Northern Luzon. Ginning and handling costs differ between the two plants as a result of the equipment differences. Specifically, the Polomolok ginnery is a more sophisticated plant with a higher degree of automation than the San Fabian ginnery. In the analysis, it is assumed that the farmgate price for cotton will be P10 per kg. in the first year, and the amount will grow at the projected rate of inflation. At this price, it is assumed that a total of 8,000 hectares of cotton will be planted in the area, and that 50% of the production will be purchased by the privatized operations of PCC.

Hectarage is actually projected to attain or exceed 8,000 ha. for the 1987-88 season. Operating expenses were projected in the same fashion as in the San Fabian DCF analysis, with expenses generally growing at the long-term rate of inflation. The operating expense assumptions for the first projected year are detailed below.

Exhibit II-6

DISCOUNTED CASH FLOW ANALYSIS
SAN FABIAN GINNERY
(1,000'S OF PESOS)

	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997
REVENUE	----	----	----	----	----	----	----	----	----	----
SEED COTTON (M.T.)	1,200	1,600	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000
LINT (M.T.)	468	624	780	780	780	780	780	780	780	780
PRICE PER KILO (PESOS)	34.17	36.56	39.12	41.86	44.79	47.93	51.28	54.87	58.71	62.82
SALES REVENUE - LINT	15,992	22,815	30,515	32,651	34,936	37,382	39,998	42,798	45,794	49,000
SEEDS (M.T.)	720	960	1,200	1,200	1,200	1,200	1,200	1,200	1,200	1,200
PRICE PER KILO (PESOS)	1.70	1.82	1.95	2.08	2.23	2.38	2.55	2.73	2.92	3.13
SALES REVENUE - SEEDS	1,224	1,746	2,336	2,499	2,674	2,861	3,061	3,276	3,505	3,750
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TOTAL REVENUE	17,216	24,561	32,850	35,150	37,610	40,243	43,060	46,074	49,299	52,750
CASH EXPENSE ITEMS										
SEED COTTON PURCHASES	12,000	17,120	22,898	24,501	26,216	28,051	30,015	32,116	34,364	36,769
GINNING COSTS	863	1,070	1,302	1,393	1,491	1,595	1,707	1,826	1,954	2,091
HANDLING & WAREHOUSING	593	724	871	933	998	1,068	1,142	1,222	1,308	1,399
FREIGHT	584	834	1,115	1,193	1,277	1,366	1,462	1,564	1,674	1,791
EXTENSION SERVICES	1,421	1,585	1,764	1,888	2,020	2,161	2,313	2,475	2,648	2,833
GENERAL & ADMINISTRATIVE	961	1,028	1,100	1,177	1,260	1,348	1,442	1,543	1,651	1,767
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TOTAL CASH EXPENSES	16,422	22,361	29,051	31,085	33,261	35,589	38,080	40,746	43,598	46,650
NON-CASH EXPENSE ITEMS										
DEPRECIATION	365	365	496	637	787	948	1,121	1,174	1,230	1,291
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TOTAL NON-CASH EXPENSES	365	365	496	637	787	948	1,121	1,174	1,230	1,291
TOTAL EXPENSES	16,787	22,726	29,548	31,722	34,048	36,538	39,201	41,920	44,828	47,941
NET INCOME										
NET INCOME BEFORE TAX	429	1,835	3,302	3,428	3,562	3,705	3,859	4,114	4,471	4,809
INCOME TAX	150	642	1,156	1,200	1,247	1,297	1,351	1,454	1,565	1,683
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AFTER TAX INCOME	279	1,193	2,147	2,228	2,315	2,408	2,508	2,700	2,906	3,126
NON-TAXABLE CASH SOURCES (USES)										
CHANGES IN WRKNG CAPITAL	(344)	(147)	(166)	(46)	(49)	(53)	(56)	(60)	(65)	(69)
CAPITAL EXPENDITURES	0	0	(657)	(703)	(752)	(805)	(861)	(921)	(986)	(1,055)
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TOTAL NON-TAXABLE CASH	(344)	(147)	(823)	(749)	(801)	(858)	(918)	(982)	(1,050)	(1,124)
CASH FLOW										
AFTER TAX INCOME	279	1,193	2,147	2,228	2,315	2,408	2,508	2,700	2,906	3,126
NON-CASH EXPENSE ADDBACK	365	365	496	637	787	948	1,121	1,174	1,230	1,291
TOTAL NON-TAXABLE CASH	(344)	(147)	(823)	(749)	(801)	(858)	(918)	(982)	(1,050)	(1,124)
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NET CASH FLOW	299	1,411	1,820	2,116	2,301	2,499	2,711	2,892	3,086	3,293
PRESENT VALUE FACTOR	0.918	0.774	0.653	0.550	0.464	0.391	0.330	0.278	0.235	0.198
P.V. OF CASH FLOW	275	1,092	1,188	1,165	1,068	978	895	805	724	651

Exhibit 11-6
(Continued)

DISCOUNTED CASH FLOW ANALYSIS
SAN FABIAN GINNERY
(1,000'S OF PESOS)

VALUE CONCLUSIONS	
P.V. OF 10 YR. CASH FLOW	8,840
P.V. OF RESIDUAL	2,392

CONCLUDED VALUE	11,232

ASSUMPTIONS

FARM GATE PRICE (P/KILO)	10.00
HECTARES PLANTED	4,000
% OF CROP PURCHASED	50%
PHILCOTTON HECTARES	2,000
SEED COTTON YIELD (KILO/HA)	1,000
LINT PRICE (P/KILO)	34.17
LINT YIELD RATE	39.00%
SEED PRICE (P/KILO)	1.70
SEED YIELD RATE	60.00%
LONG TERM INFLATION RATE	7.0%
RESIDUAL MULTIPLE	4
INITIAL BASIS (OLD ASSETS)	7,301
AVG. REM. LIFE - OLD ASSETS	20
AVERAGE LIFE - NEW ASSETS	5
INCOME TAX RATE	35.0%
% OF CAPITAL AS DEBT	60.0%
COST OF DEBT	20.0%
COST OF EQUITY	27.0%
WGHT. AVG. COST OF CAPITAL	18.6%
INITIAL NET WORKING CAPITAL	0
NET WRKG CAP AS % OF REV	2.0%

Polomolok Ginnery
1988 Cost Assumptions
(Pesos)

	Fixed Costs	Variable Costs
Ginning Costs	353,000	0.55 x kilos of lint
Handling & Warehousing	136,000	0.68 x kilos of lint
Freight	-	0.25 x kilos of seedcotton 1.05 x kilos of lint 0.70 x kilos of seeds
Extension Services	1,060,000	0.168 x hectares supplied 0.015 x seedcotton purch.
General & Administrative	961,000	-

Exhibit II-7 shows the discounted cash flow analysis for the Polomolok ginnery, based upon the foregoing assumptions. The concluded value is P29,739,000.

(6) Liquidation Of Ginneries Will Yield Low Prices Due To High Cost Of Relocation And Small Worldwide Demand For Used Ginning Equipment

An investigation was conducted to determine the value of the San Juan and Polomolok ginneries assuming they would be sold for disassembly and relocation. The valuation sought in this analysis is an indication of the world market price for ginning equipment. However, this does not preclude the sale of subject assets for relocation within the Philippines. The concluded values of the assets for relocation are expressed as "value in exchange."

Exhibit II-7

DISCOUNTED CASH FLOW ANALYSIS
 TOLOMOLOK GINNERY
 (1,000'S OF PESOS)

	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997
REVENUE	----	----	----	----	----	----	----	----	----	----
SEED COTTON (M.T.)	4,000	4,000	4,000	4,000	4,000	4,000	4,000	4,000	4,000	4,000
LINT (M.T.)	1,560	1,560	1,560	1,560	1,560	1,560	1,560	1,560	1,560	1,560
PRICE PER KILO (PESOS)	34.17	36.56	39.12	41.86	44.79	47.93	51.28	54.87	58.71	62.82
SALES REVENUE - LINT	53,305	57,037	61,029	65,301	69,872	74,763	79,997	85,597	91,588	97,999
SEEDS (M.T.)	2,400	2,400	2,400	2,400	2,400	2,400	2,400	2,400	2,400	2,400
PRICE PER KILO (PESOS)	1.70	1.82	1.95	2.08	2.23	2.38	2.55	2.73	2.92	3.13
SALES REVENUE - SEEDS	4,080	4,366	4,671	4,998	5,348	5,722	6,123	6,552	7,010	7,501
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
TOTAL REVENUE	57,385	61,402	65,700	70,299	75,220	80,486	86,120	92,148	98,598	105,500
CASH EXPENSE ITEMS										
SEED COTTON PURCHASES	40,000	42,800	45,796	49,002	52,432	56,102	60,029	64,231	68,727	73,538
GINNING COSTS	1,211	1,296	1,386	1,484	1,587	1,698	1,817	1,945	2,081	2,226
HANDLING & WAREHOUSING	1,197	1,281	1,370	1,466	1,569	1,679	1,796	1,922	2,056	2,200
FREIGHT	4,518	4,834	5,173	5,535	5,922	6,337	6,780	7,255	7,763	8,306
EXTENSION SERVICES	2,332	2,495	2,670	2,857	3,057	3,271	3,500	3,745	4,007	4,287
GENERAL & ADMINISTRATIVE	961	1,028	1,100	1,177	1,260	1,348	1,442	1,543	1,651	1,767
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TOTAL CASH EXPENSES	50,219	53,734	57,496	61,520	65,827	70,434	75,365	80,640	86,285	92,325
NON-CASH EXPENSE ITEMS										
DEPRECIATION	967	967	1,229	1,511	1,811	2,133	2,478	2,584	2,697	2,818
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
TOTAL NON-CASH EXPENSES	967	967	1,229	1,511	1,811	2,133	2,478	2,584	2,697	2,818
TOTAL EXPENSES	51,185	54,701	58,725	63,031	67,638	72,568	77,843	83,224	88,982	95,143
NET INCOME										
NET INCOME BEFORE TAX	6,200	6,702	6,975	7,269	7,582	7,918	8,277	8,924	9,616	10,357
INCOME TAX	2,170	2,346	2,441	2,544	2,654	2,771	2,897	3,123	3,366	3,625
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AFTER TAX INCOME	4,030	4,356	4,534	4,725	4,928	5,147	5,380	5,801	6,251	6,732
NON-TAXABLE CASH SOURCES (USES)										
CHANGES IN WRKNG CAPITAL	(1,148)	(80)	(86)	(92)	(98)	(105)	(113)	(121)	(129)	(138)
CAPITAL EXPENDITURES	0	0	(1,314)	(1,406)	(1,504)	(1,610)	(1,722)	(1,843)	(1,972)	(2,110)
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
TOTAL NON-TAXABLE CASH	(1,148)	(80)	(1,400)	(1,498)	(1,603)	(1,715)	(1,835)	(1,964)	(2,101)	(2,248)
CASH FLOW										
AFTER TAX INCOME	4,030	4,356	4,534	4,725	4,928	5,147	5,380	5,801	6,251	6,732
NON-CASH EXPENSE ADDBACK	967	967	1,229	1,511	1,811	2,133	2,478	2,584	2,697	2,818
TOTAL NON-TAXABLE CASH	(1,148)	(80)	(1,400)	(1,498)	(1,603)	(1,715)	(1,835)	(1,964)	(2,101)	(2,248)
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
NET CASH FLOW	3,849	5,242	4,363	4,737	5,137	5,565	6,023	6,421	6,846	7,302
PRESENT VALUE FACTOR	0.918	0.774	0.653	0.550	0.464	0.391	0.330	0.278	0.235	0.198
P.V. OF CASH FLOW	3,534	4,059	2,848	2,607	2,384	2,178	1,997	1,786	1,606	1,444

Exhibit 11-7
(Continued)

DISCOUNTED CASH FLOW ANALYSIS
POLOMOLOK GINNERY
(1,000'S OF PESOS)

VALUE CONCLUSIONS

.....	
P.V. OF 10 YR. CASH FLOW	24,434
P.V. OF RESIDUAL	5,305
.....	
CONCLUDED VALUE	29,739

ASSUMPTIONS

.....	
FARM GATE PRICE (P/KILO)	10.00
HECTARES PLANTED	8,000
% OF CROP PURCHASED	50%
PHILCOTTON HECTARES	4,000
SEED COTTON YIELD (KILO/HA)	1,000
LINT PRICE (P/KILO)	34.17
LINT YIELD RATE	39.00%
SEED PRICE (P/KILO)	1.70
SEED YIELD RATE	60.00%
LONG TERM INFLATION RATE	7.0%
RESIDUAL MULTIPLE	4
INITIAL BASIS (OLD ASSETS)	19,330
AVG. REM. LIFE - OLD ASSETS	20
AVERAGE LIFE - NEW ASSETS	5
INCOME TAX RATE	35.0%
% OF CAPITAL AS DEBT	60.0%
COST OF DEBT	20.0%
COST OF EQUITY	27.0%
WGHT. AVG. COST OF CAPITAL	18.6%
INITIAL NET WORKING CAPITAL	0
NET WRKG CAP AS % OF REV	2.0%

The ginneries include a substantial amount of permanent installation features, such as ducting, wiring, and machinery foundations. At such, removal and crating of a ginning plant is a costly endeavor that can take one to two months to complete. Also, much of the peripheral fixtures and equipment is not economically feasible to relocate. The study of prices of used gins considered these costs as a deduction to value of machinery and equipment.

The approach taken to the asset valuation is a direct sales comparison analysis. There is a world market for ginning equipment, but the number of sales that occur is relatively small. Individuals and firms that are knowledgeable of the world market were contacted to determine selling prices and market activity. Based upon information gathered, value conclusions were established.

The San Juan ginnery is an old facility, and is considered obsolete by current industry standards. This type of equipment can generally be sold only in underdeveloped nations at a small fraction of the replacement cost for equivalent ginning capacity. The estimated value of the San Juan ginnery equipment for relocation is US\$110,000.

The Polomolok ginnery is a modern facility which would be operationally satisfactory in any cotton producing country. It provides a large ginning capacity. The limitation to the desirability of such a facility is in the ginning capacity requirements of the buyer. If the capacity requirements are low, a buyer might meet his ginning needs more economically with a smaller gin. The equipment would be expected to sell for substantially less than the replacement cost for equivalent ginning capacity. The estimated value of the Polomolok ginnery equipment for relocation is US\$320,000.

In both cases, it should be noted that the estimated value of the ginning equipment does not include the value of the real property. Thus, the total proceeds from privatization by the

liquidation of assets would be the price received for the equipment, plus the price received for the real property, which would be sold in separate transactions. Since the sale of assets represents a liquidation of the business, there would be no intangible value realized from the sale.

(7) Sale Of Both San Fabian And San Juan Gineries May Yield A Lower Total Price Than Selling The San Fabian Gin In Place And The San Juan Gin For Relocation

It is possible that APT privatization procedures will dictate that both the San Fabian and San Juan gineries be sold as operating units in place. A DCF valuation was conducted to estimate value of each ginery based upon the assumption that both gins would operate in place. Generally, the cost assumptions for the two gins were the same as for the San Fabian ginery operating alone. However, some adjustments were made due to differences in transportation distances and size of staff required to operate a smaller-volume ginning business. The most significant differences are based upon the change in assumed volume of seedcotton purchased by the gins.

It is assumed that the two privatized gins would compete with each other and with other private sector ginners to purchase seed cotton from generally the same areas. While the price paid to the farmer is assumed to have a substantial effect upon the amount of cotton planted, it is assumed that for a specified farmgate price, the available volume of seedcotton would be constant, regardless of the number of operating gins. In the valuation of the San Fabian ginery operating in the absence of the San Juan ginery, it was assumed that 50% of harvested seedcotton in northern Luzon would be purchased by the San Fabian ginery. In valuing the gineries, assuming that both are operating, it is assumed that 60% percent of the seedcotton available in the area would be purchased by the two gins, since two separate owners of the gins would provide for more aggressive competition for raw material supplies. It is further

assumed that the amount of seedcotton purchased by the two gins would be allocated: 60% to the San Fabian ginnery, and 40% to the San Juan ginnery. This allocation is based on the approximate proportion of hectarage in the provinces nearest the gins. Cotton grown in Ilocos Norte and Ilocos Sur is assumed to be ginned at the San Juan plant, while cotton grown in Pangasinan and La Union is assumed to be ginned at San Fabian. Thus, San Fabian is assumed to receive 36% of total production in northern Luzon, and San Juan is assumed to receive 24%.

Most of the fixed operating costs for both ginneries are expected to be the same as in the DCF analysis for the San Fabian gin operating in the absence of the San Juan gin. However, because of the relatively smaller geographic area of seedcotton production each ginnery would supervise, it is assumed that the fixed portion of extension service costs would be reduced by P52,000, which represents about half of the total fixed cost, including expense allowances, of the extension workers.

Transportation costs, which are purely variable, were adjusted to reflect the geographical differences in the facilities and the sources of seedcotton. Relative to the cost estimate for the San Fabian gin operation only, transportation costs for each gin were lowered because it is assumed that, on average, the seedcotton will not travel as far from the farm to the gin. Freight costs are the same for the San Fabian gin regardless of whether the San Juan gin is operated. The San Juan freight costs are higher due to the greater distance the lint must be shipped (to Metro Manila), and the greater distance seeds must be shipped to an ocean port in La Union for export.

The expense assumptions for 1988 used for the models, assuming both ginneries are operating, are shown below. Costs are expressed in pesos. For expense items not shown, assumptions are identical to the analysis for the San Fabian ginnery alone.

San Fabian Ginnery

	<u>Fixed Costs</u>	<u>Variable Costs</u>
Freight		0.12 x kilos of seedcotton 0.30 x kilos of lint 0.20 x kilos of seeds
Extension Services	853,000	0.168 x hectares supplied 0.015 x seedcotton purch.

San Juan Ginnery

	<u>Fixed Costs</u>	<u>Variable Costs</u>
Freight		0.20 x kilos of seedcotton 0.48 x kilos of lint 0.40 x kilos of seeds
Extension Services	853,000	0.168 x hectares supplied 0.015 x seedcotton purch.

The DCF analyses assuming operation of both the San Juan and San Fabian ginneries are shown on Exhibits II-8 and II-9. The results indicate values of P5,428,000 for the San Fabian ginnery and P3,574,000 for the San Juan ginnery.

It is noted that the combined value of the two gins as valued under this scenario is less than the calculated value of the San Fabian ginnery alone assuming that the San Juan ginnery will be relocated. Thus optimal sales proceeds would most likely be realized by relocating the San Juan facility and selling the San Fabian ginnery as an operating unit in place.

Exhibit 11-8

DISCOUNTED CASH FLOW ANALYSIS
SAN JUAN GINNERY
(1,000'S OF PESOS)

	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997
REVENUE	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....
SEED COTTON (M.T.)	864	1,152	1,440	1,440	1,440	1,440	1,440	1,440	1,440	1,440
LINT (M.T.)	337	449	562	562	562	562	562	562	562	562
PRICE PER KILO (PESOS)	34.17	36.56	39.12	41.86	44.79	47.93	51.28	54.87	58.71	62.82
SALES REVENUE - LINT	11,514	16,427	21,970	23,508	25,154	26,915	28,799	30,815	32,972	35,280
SEEDS (M.T.)	518	691	864	864	864	864	864	864	864	864
PRICE PER KILO (PESOS)	1.70	1.82	1.95	2.08	2.23	2.38	2.55	2.73	2.92	3.13
SALES REVENUE - SEEDS	881	1,257	1,682	1,799	1,925	2,060	2,204	2,359	2,524	2,700

TOTAL REVENUE	12,395	17,684	23,652	25,308	27,079	28,975	31,003	33,173	35,495	37,980
CASH EXPENSE ITEMS										
SEED COTTON PURCHASES	8,640	12,326	16,487	17,641	18,875	20,197	21,611	23,123	24,742	26,474
GINNING COSTS	748	906	1,082	1,158	1,239	1,326	1,419	1,518	1,624	1,738
HANDLING & WAREHOUSING	522	623	736	788	843	902	965	1,033	1,105	1,183
FREIGHT	542	773	1,034	1,106	1,184	1,267	1,355	1,450	1,552	1,660
EXTENSION SERVICES	1,225	1,356	1,501	1,606	1,718	1,839	1,967	2,105	2,252	2,410
GENERAL & ADMINISTRATIVE	961	1,028	1,100	1,177	1,260	1,348	1,442	1,543	1,651	1,767

TOTAL CASH EXPENSES	12,637	17,013	21,940	23,476	25,120	26,878	28,759	30,772	32,927	35,231
NON-CASH EXPENSE ITEMS										
DEPRECIATION	116	116	211	312	420	536	660	698	739	783

TOTAL NON-CASH EXPENSES	116	116	211	312	420	536	660	698	739	783
TOTAL EXPENSES	12,753	17,129	22,151	23,788	25,540	27,414	29,420	31,471	33,666	36,014
NET INCOME										
NET INCOME BEFORE TAX	(358)	554	1,501	1,520	1,539	1,561	1,584	1,703	1,830	1,966
INCOME TAX	0	69	525	532	539	546	554	596	640	688

AFTER TAX INCOME	(358)	486	976	988	1,001	1,014	1,029	1,107	1,189	1,278
NON-TAXABLE CASH SOURCES (USES)										
CHANGES IN WRKNG CAPITAL	(248)	(106)	(119)	(33)	(35)	(38)	(41)	(43)	(46)	(50)
CAPITAL EXPENDITURES	0	0	(473)	(506)	(542)	(579)	(620)	(663)	(710)	(760)

TOTAL NON-TAXABLE CASH	(248)	(106)	(592)	(539)	(577)	(617)	(661)	(707)	(756)	(809)
CASH FLOW										
AFTER TAX INCOME	(358)	486	976	988	1,001	1,014	1,029	1,107	1,189	1,278
NON-CASH EXPENSE ADDBACK	116	116	211	312	420	536	660	698	739	783
TOTAL NON-TAXABLE CASH	(248)	(106)	(592)	(539)	(577)	(617)	(661)	(707)	(756)	(809)

NET CASH FLOW	(490)	496	594	760	844	933	1,029	1,098	1,172	1,251
PRESENT VALUE FACTOR	0.918	0.774	0.653	0.550	0.464	0.391	0.330	0.278	0.235	0.198
P.V. OF CASH FLOW	(450)	384	388	419	392	365	339	305	275	247

Exhibit 11-8
(Continued)

DISCOUNTED CASH FLOW ANALYSIS
SAN JUAN GINNERY
(1,000'S OF PESOS)

VALUE CONCLUSIONS	
P.V. OF 10 YR. CASH FLOW	2,665
P.V. OF RESIDUAL	909

CONCLUDED VALUE	3,574

ASSUMPTIONS

FARM GATE PRICE (P/KILO)	10.00
HECTARES PLANTED	4,000
% OF CROP PURCHASED	36%
PHILCOTTON HECTARES	1,440
SEED COTTON YIELD (KILO/HA)	1,000
LINT PRICE (P/KILO)	34.17
LINT YIELD RATE	39.00%
SEED PRICE (P/KILO)	1.70
SEED YIELD RATE	60.00%
LONG TERM INFLATION RATE	7.0%
RESIDUAL MULTIPLE	4
INITIAL BASIS (OLD ASSETS)	2,323
AVG. REM. LIFE - OLD ASSETS	20
AVERAGE LIFE - NEW ASSETS	5
INCOME TAX RATE	35.0%
% OF CAPITAL AS DEBT	60.0%
COST OF DEBT	20.0%
COST OF EQUITY	27.0%
WGHT. AVG. COST OF CAPITAL	18.6%
INITIAL NET WORKING CAPITAL	0
NET WRKG CAP AS % OF REV	2.0%

Exhibit II-9

DISCOUNTED CASH FLOW ANALYSIS
SAN FABIAN GINNERY
(1,000'S OF PESOS)

	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997
REVENUE	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
SEED COTTON (M.T.)	864	1,152	1,440	1,440	1,440	1,440	1,440	1,440	1,440	1,440
LINT (M.T.)	337	449	562	562	562	562	562	562	562	562
PRICE PER KILO (PESOS)	34.17	36.56	39.12	41.86	44.79	47.93	51.28	54.87	58.71	62.82
SALES REVENUE - LINT	11,514	16,427	21,970	23,508	25,154	26,915	28,799	30,815	32,972	35,280
SEEDS (M.T.)	518	691	864	864	864	864	864	864	864	864
PRICE PER KILO (PESOS)	1.70	1.82	1.95	2.08	2.23	2.38	2.55	2.73	2.92	3.13
SALES REVENUE - SEEDS	881	1,257	1,682	1,799	1,925	2,060	2,204	2,359	2,524	2,700
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
TOTAL REVENUE	12,395	17,684	23,652	25,308	27,079	28,975	31,003	33,173	35,495	37,980
CASH EXPENSE ITEMS										
SEED COTTON PURCHASES	8,640	12,326	16,487	17,641	18,875	20,197	21,611	23,123	24,742	26,474
GINNING COSTS	748	906	1,082	1,158	1,239	1,326	1,419	1,518	1,624	1,738
HANDLING & WAREHOUSING	522	623	736	788	843	902	965	1,033	1,105	1,183
FREIGHT	308	440	589	630	674	721	771	826	883	945
EXTENSION SERVICES	1,225	1,356	1,501	1,606	1,718	1,839	1,967	2,105	2,252	2,410
GENERAL & ADMINISTRATIVE	961	1,028	1,100	1,177	1,260	1,348	1,442	1,543	1,651	1,767
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
TOTAL CASH EXPENSES	12,403	16,680	21,495	23,000	24,610	26,332	28,175	30,148	32,258	34,516
NON-CASH EXPENSE ITEMS										
DEPRECIATION	176	176	271	372	481	596	720	759	799	843
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
TOTAL NON-CASH EXPENSES	176	176	271	372	481	596	720	759	799	843
TOTAL EXPENSES	12,580	16,857	21,766	23,372	25,090	26,929	28,896	30,906	33,057	35,359
NET INCOME										
NET INCOME BEFORE TAX	(185)	827	1,886	1,936	1,989	2,046	2,107	2,267	2,438	2,621
INCOME TAX	0	225	660	678	696	716	738	793	853	917
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
AFTER TAX INCOME	(185)	602	1,226	1,258	1,293	1,330	1,370	1,474	1,585	1,704
NON-TAXABLE CASH SOURCES (USES)										
CHANGES IN WRKNG CAPITAL	(248)	(106)	(119)	(33)	(35)	(38)	(41)	(43)	(46)	(50)
CAPITAL EXPENDITURES	0	0	(473)	(506)	(542)	(579)	(620)	(663)	(710)	(760)
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
TOTAL NON-TAXABLE CASH	(248)	(106)	(592)	(539)	(577)	(617)	(661)	(707)	(756)	(809)
CASH FLOW										
AFTER TAX INCOME	(185)	602	1,226	1,258	1,293	1,330	1,370	1,474	1,585	1,704
NON-CASH EXPENSE ADDBACK	176	176	271	372	481	596	720	759	799	843
TOTAL NON-TAXABLE CASH	(248)	(106)	(592)	(539)	(577)	(617)	(661)	(707)	(756)	(809)
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
NET CASH FLOW	(256)	673	905	1,091	1,197	1,309	1,430	1,525	1,628	1,737
PRESENT VALUE FACTOR	0.918	0.774	0.653	0.550	0.464	0.391	0.330	0.278	0.235	0.198
P.V. OF CASH FLOW	(235)	521	591	601	555	512	472	424	382	344

Exhibit II-9
(Continued)

DISCOUNTED CASH FLOW ANALYSIS
SAN FABIAN GINNERY
(1,000'S OF PESOS)

VALUE CONCLUSIONS	
P.V. OF 10 YR. CASH FLOW	4,166
P.V. OF RESIDUAL	1,262

CONCLUDED VALUE	5,428

ASSUMPTIONS

.....

FARM GATE PRICE (P/KILO)	10.00
HECTARES PLANTED	4,000
% OF CROP PURCHASED	36%
PHILCOTTON HECTARES	1,440
SEED COTTON YIELD (KILO/HA)	1,000
LINT PRICE (P/KILO)	34.17
LINT YIELD RATE	39.00%
SEED PRICE (P/KILO)	1.70
SEED YIELD RATE	60.00%
LONG TERM INFLATION RATE	7.0%
RESIDUAL MULTIPLE	4
INITIAL BASIS (OLD ASSETS)	3,528
AVG. REM. LIFE - OLD ASSETS	20
AVERAGE LIFE - NEW ASSETS	5
INCOME TAX RATE	35.0%
% OF CAPITAL AS DEBT	60.0%
COST OF DEBT	20.0%
COST OF EQUITY	27.0%
WGHT. AVG. COST OF CAPITAL	18.6%
INITIAL NET WORKING CAPITAL	0
NET WRKG CAP AS % OF REV	2.0%

Another important issue in the valuation of the two northern Luzon gins is the sensitivity of the assumptions regarding volume of seedcotton purchased. The seedcotton supply is a critical assumption in the valuation. In particular, the assumption that the San Juan ginnery will purchase 24% of all seedcotton produced in northern Luzon may be questionable. As previously discussed, there are certain locational disadvantages to the San Juan plant. Thus it might not compete as effectively as assumed for the purchase of seedcotton grown in Ilocos Sur and Ilocos Norte. The calculated value of the San Juan ginnery is low given the assumed volume of seedcotton. Any significant decrease in volume would result in a negative value for the plant. Thus, it appears possible that no bids would be offered for the San Juan ginnery.

This leads to the worst outcome scenario regarding the amount of revenues raised by the privatization of the northern Luzon ginneries. If both the San Fabian and San Juan ginneries are offered for bid as operating plants, there may be no bidders for the San Juan plant.

8. IMMEDIATE PRIVATIZATION OF ALL OF PCC IS RECOMMENDED

The PCC operation has been extensively analyzed and options and requirements in privatization have been determined above. The recommended privatization strategy for PCC is as follows:

- As soon as the final determination on privatization has been made, all bank accounts should be frozen
- Offer San Juan and San Fabian ginneries for sale simultaneously through a sealed bidding process. Sale of the San Juan ginnery should be conditioned on its disassembly and removal to another location in the Philippines or off-shore. The San Fabian ginnery should be sold in-place, as is. The benchmark values of these

ginneries under these conditions are:

- San Juan ginney P2,200,000
- San Fabian ginney 11,232,000.

- Pursue the sale of the San Juan ginney equipment through worldwide channels as well as locally as the market for such equipment is thin. There may be interest by a buyer to set up this equipment on Panay
- Offer the Polomolok ginney for sale by sealed bids on an in-place basis. The value in-place is estimated at P29.7 million. If sold for disassembly and removal it is estimated to be only worth P6.5 million
- Re-appraise the real property at the San Juan site to establish a benchmark value. Sell to buyers interested in acquiring rice or tobacco storage capacity along with office facilities
- The sales proceeds from the two gins to be sold in-place will be increased if their sale coincides with the ginning season, i.e. March to June
- Unsold baled cotton inventories should be sold to textile millers by PCC or included in bid documents as assets to be purchased by the buyer at cost
- The APT should require the buyers of the Polomolok and San Fabian ginneries to retain key workers, including some extension agents, ginney engineers, mechanics and operators, some accounting personnel and guards. This will maintain a high-level of knowledge and technology of cotton cultivation and ginning as well as enable the buyers to maintain operating momentum at the gins

- The DA should absorb the remaining personnel to maintain a public sector cotton extension capability and reduce the adverse economic impacts of privatization
- Unless a compelling reason exists for CRDI to continue operating the demonstration farms at San Juan and Polomolok, these should be put up for bids by the DA using COA guidelines. If they are not to be put up for bids, title should be transferred to the Department of Education
- PCC's aircraft should be transferred to the Department of Agriculture where there is a need for it.
- The termination of the land lease at Nueva Ecija as well as that of the seed co-production joint venture should be negotiated
- PCC receivables should be aged and collection strategies should be formulated. In conjunction with COA, determine debts to be written off
- Transfer the loan liabilities to the DF for settlement
- DA should close down PCC headquarters, and sub-lease the vacated space of the headquarters building for the next four years
- DA should introduce legislation to wind up the Philippine Cotton Corporation.

III. DIVESTITURE STRATEGY FOR THE PHILIPPINE DAIRY CORPORATION

This chapter examines the Philippine Dairy Corporation (PDC) and recommends a strategy for privatizing PDC. It covers of the following topics:

- History
- Management and Organization
- Industry Structure, Markets and Prices
- Assets and Their Condition
- Special Issues
- Summary of Financial Performance
- Privatization Options
- Valuation
- Recommended Privatization Strategy.

1. THE PURPOSE OF THE PHILIPPINE DAIRY CORPORATION WAS TO HELP IMPROVE SMALLHOLDER INCOMES AND TO FOSTER A MEASURE OF IMPORT SUBSTITUTION

The PDC was established pursuant to the authority contained in the Dairy Development Act of 1979. The PDC business plan and objectives were drawn from a National Dairy Development plan (1981-1990) designed to provide an alternative income source for smallholders while substituting domestic production for a portion of dairy product imports.

The majority of corporate assets were acquired with funds provided through a US\$16 million loan from the ADB and IFAD for the Philippine Smallholder Livestock Development Project (SLDP). Only US\$5 million of the loan was actually disbursed. The assets acquired with these funds include:

- Milking equipment
- Milk collection, chilling and processing equipment
- Cattle
- Miscellaneous equipment.

The PDC imported a total of 2,400 dairy heifers and distributed approximately 4,000 imported and local dairy animals to small farmers. Milk collection and chilling facilities were established at Trece Martires, Cavite and at Lipa, Batangas, in Southern Luzon. A milk processing plant was set-up at Alabang, a suburb of Metro Manila. A breeding center was planned at Bukidnon but was never set up. In mid-1986 the new administration within the Department of Agriculture decided to curtail operations of the PDC in order to re-evaluate the status of the organization in light of the current GOP goals of withdrawing from those activities that can be better handled by the private sector. Subsequently the Department decided to privatize the PDC.

Expressions of interest in acquiring the corporation as a going concern were solicited from the obvious prospects, including Magnolia, Monterey and Selecta, companies currently engaged in the dairy business, but at that time there were no concrete expressions of interest in either the corporation or its assets.

PDC stopped buying milk from farmers in about June 1986, at which time the milk processing plant at Alabang was closed down. The two chilling plants had already been shut down in February 1986 after operating for only a couple of months, due to an insufficient volume of milk.

Due to uncertainties within the PDC organization resulting from the Departmental action, almost all PDC activities had stopped by July 1986. Regional technical extension supervisors were withdrawn from the provinces and given desks in the central PDC headquarters in Manila. The extension fieldmen in the provinces continued to work with dairy farmers to the extent allowed by their limited resources.

In early 1987, PDC started to redevote more time and resources to field extension activities. The main thrust of these activities has been to attempt to develop local cooperatives to handle the production, processing and marketing functions previously carried out by PDC. This has been accomplished only to a very limited degree.

The Southern Tagalog Dairy Cooperative (STDC), which was formed by PDC, is collecting milk and processing it at the University of the Philippines, Los Banos (UPLB) Dairy Training and Research Institute (DTRI) mainly because the volume of milk from farmer members is insufficient to justify using the PDC plant.

The PDC is in the process of selling dispersed dairy cattle to the farmers now holding them.

2. PDC IS A WHOLLY GOVERNMENT-OWNED CORPORATION, WHICH HAS ALREADY SUSPENDED MOST OPERATIONS

PDC's board of directors is composed of the secretaries of Agriculture, Natural Resources, Finance, and Trade and Industry. Three board positions reserved for the private sector have never been filled.

The president of the PDC serves as chief executive officer and is a member of the board. An undersecretary of Agriculture serves as PDC president. Divisions are controlled by vice-presidents and field operations by regional managers.

When PDC was collecting and processing milk, during the first half of 1986, the organization had a total staff of around 186 persons. By October 1987, the staff had shrunk to 90 plus the president. Most of the staff are presently based in Manila.

The staff, with the possible exception of some fieldmen still in the provinces, is underutilized due to cessation of most activities. staff morale is very low, as might be expected, due to the uncertainty surrounding their future.

3. MOST DAIRY PRODUCTS CONSUMED IN THE PHILIPPINES ARE IMPORTED, WITH LOCALLY PRODUCED FRESH MILK ACCOUNTING FOR ABOUT TWO PERCENT OF THE MARKET

The dairy industry in the Philippines is mostly based on imported, reconstituted dry milk solids. Only about two percent of the total dairy product consumption is supplied from locally produced fresh milk.

Average annual per capita consumption of dairy products in the Philippines (liquid milk equivalent) is estimated to be approximately 16 kg. Consumption varies sharply among income groups, with the lowest income category, persons with per capita incomes of less than P400, consuming an average 11 liters annually. Those persons with over P1,500 per capita income consume about 53 liters.

On a geographic basis, consumption varies from a low of seven liters per capita in Mindanao to a high of 31 liters per capita in Metro Manila. Consumption levels are thus influenced by both the level of consumer income and the availability of dairy products.

There are actually four milk processors in the Philippines, all of which are located in the Metro Manila urban area. The four are:

- Holland
- Nestle (a joint venture with Magnolia)
- Magnolia
- Selecta.

Nestle and Holland process only imported milk powder, which is reconstituted into various dairy products including fluid milk. Magnolia and Selecta process both milk powder and fresh, locally produced milk.

There were in November 1987 only two large commercial dairy herds in the Philippines. These are owned by Magnolia and by Monterey Farms, both majority owned by the San Miguel Corporation. There were several small (under 100 head) private herds, and several thousand milking animals in the hands of small farmers. A number of other smaller dairy operations have been started by private entrepreneurs during the past two decades, but all have failed for one reason or another. There have also been three separate dairy development campaigns by the GOP during the past 20 years, but these have also failed.

Magnolia presently has some 1600 dairy cattle and is milking approximately 650. These are all Holstein-Friesians, offspring of stock imported from New Zealand and the United States. Average production levels are reportedly 14-16 liters per cow per day. Milk from both the above operations is processed by Magnolia.

Monterey Farms is milking about 600 head. These animals are predominantly crossbred Brahmin-Holstein, which produce about 8-10 liters of milk daily per head. Monterey also has a few Holstein cows culled from the Magnolia herd.

A new joint dairy venture, Nashville, was approved by the BOI in August 1987. The company plans to utilize a foundation herd of Holstein-Friesians imported from the United States and to begin milk production and processing in early 1988.

There are two primary reasons why the market for dairy products in the Philippines is dominated by imported milk solids. First, due to continuing milk surpluses among the European Economic Community, the EEC heavily subsidizes its exports of milk powder, making the

landed cost less than the production cost of most locally produced milk. New Zealand, due to its low production costs, is able to match EEC milk powder price internationally.

The fluid milk equivalent cost of dry non-fat milk solids landed in the Philippines is approximately P3.75 per liter. To this must be added the cost of butter fat or vegetable fats and of reconstituting the powder. Magnolia fresh pasteurized/homogenized whole milk is sold at P17.50-P18.50 per liter in Manila supermarkets, compared with P9.40 per liter of fresh milk equivalent.

At least one dairyman with long experience in the Philippine dairy industry, Santiago Freixas of Monterey Farms, is convinced that under appropriate management conditions and with optimum scale of operations, domestically produced milk can compete on a cost basis with imported dry milk solids. The common view in the Philippines, however, has been that the domestic dairy industry cannot compete on a cost basis with imported dry milk solids.

The second factor retarding local dairy production has been the lack of the systematic application of modern dairy technology. Several smaller local dairy operations have achieved regular daily production levels of 18-20 liters per cow using good quality imported Holstein-Friesian cows, for example. However, such production is not widespread -- although at these levels commercial dairying can be quite profitable.

Despite the dominance of imported dry milk solids, there is a market in the Philippines for locally produced fresh milk. The major fresh milk processors, which are Magnolia and a smaller processor, Selecta, have expressed their interest in purchasing a substantial volume of fresh milk if a suitable quality supply were available.

Also attractive is the market represented by the US bases, Clark and Subic. Clark has a powdered milk reconstituting plant that supplies both bases. The plant uses about 11 tons of milk powder

weekly. Clark is also buying some local fresh milk from Magnolia, but this constitutes only a small portion of total use.

Emphasis is currently being placed by the US base commands on procuring as many needed supplies as possible from domestic Philippine sources. The procurement officer at Clark has indicated his interest in substituting more of the reconstituted milk, in addition to the Magnolia purchases, with locally produced milk. However, the sourcing herd and processing plant must be inspected and approved by the US Department of Agriculture.

The Philippine Dairy Corporation, during the approximately six months that it operated the Alabang processing plant, purchased milk directly from farmers, processed it into pasteurized, homogenized fluid milk and sold it to dealers in Metro Manila. The plant also produced some Filipino-style white cheese utilizing sub-standard milk. The plant had a peak throughput of 1500 liters a day, but averaged only 700 liters a day overall.

The milk was purchased from farmers at a cost of P5.75 per liter delivered to PDC. The farmer realized P5.00. The remainder went to the milk collectors and the milk collection center.

PDC sold pasteurized/homogenized milk to dealers who retailed the milk in Metro Manila. The price from PDC to the dealers was P10.75 per liter. The dealer sold the milk at about P15 per liter.

After PDC stopped purchasing milk and closed down the Alabang processing plant in June 1986, marketing of PDC cooperator-farmer milk shifted to alternative channels, including several private traders. PDC field staff attempted to form cooperatives in each area where the PDC cattle dispersal program had operated with the aim of helping these cooperatives take over the PDC collection and marketing role. The only group successfully organized, under PDC auspices, to actually market its own milk, however, is the Southern Tagalog Dairy Coopera-

tive (STDC), which operates primarily in San Pablo and Cavite. Many of the other cattle recipients have stopped milking their cows.

STDC farmers aggregately have about 400 dairy cattle, of which only about 100 are being milked. This is primarily due to the inability of the farmers to spot heat symptoms in the cows. When they are able to in-semenate their cows on a timely basis, conception often fails because of the low motility of much of the semen, most of which has been on hand since 1984.

STDC purchases milk from farmers at P5.00 per liter. An additional P0.70 goes to collectors and collection centers. STDC takes P0.15 per liter for operations.

The milk is custom-processed for P0.95 per liter at the Los Banos milk processing plant operated by the Dairy Training and Research Institute (DTRI), which is attached to the University of the Philippines.

The milk is packaged in 400 gram and one liter plastic pouches. The pouches cost P0.30 for the 400 gram size and P0.45 for the liter size.

The milk is sold to dealers at P11 per liter. The dealers in turn sell it to consumers on a door-to-door basis at P15 per liter. STDC markets about 500 liters per day, including 300 from member producers and 200 purchased from DTRI.

Farmers in Batangas and Cavite are largely unorganized and many have quit milking their cows. A private trader is buying about 200 liters a day from local farmers in the Batangas area. He has his milk processed at DTRI and at the Kilusang Kabuhayan at Kaunlaran (KKK) processing plant at Taguig, Rizal.

A dairy farmer near Batangas with 70 cows of his own, also buys some milk from small local dairymen. His milk is processed at KKK. Some milk is also purchased directly by KKK.

There is a serious quality problem with much of the milk sourced from smallholders. Milking is done by hand, often under less than sanitary conditions. Milk may not be chilled immediately due to lack of chilling facilities. The STDC farmers and a few of the semi-commercial farmers (10 cows or more) in the Batangas and Cavite area are doing a somewhat better job with milk quality control.

If farmers were assured of a market for their milk, and provided with the required technical back-up, more would undoubtedly enter or re-enter dairying. But the difficulties involved in milk collection and quality control militate against any tie-up between small farmers and commercial milk processors.

4. PDC ASSETS INCLUDE CATTLE ALREADY DISPERSED TO FARMERS; AND MILK PRODUCTION, PROCESSING AND CHILLING EQUIPMENT

- (1) The PDC Holds In Trust For The SLDP Physical Assets For Collection, Chilling And Processing Of Milk And For Associated Activities Of Artificial Insemination Services, Advisory Services And Administration

The following is a brief description of PDC's major assets. Appendix E contains a more detailed asset schedule.

- Milk collection equipment, including:
 - Motorcycles with sidecars, 43 units
 - Pickups, 7 units (not all used for milk collection)
 - Milk collection equipment including milk cans and milk testing equipment

- Milk collection equipment on loan to farmers cooperative groups.
- Two milk chilling centers at Lipa and Cavite, each containing:
 - Milk weighing scales
 - Milk pump
 - Plate cooler chilling tanks (2 X 2000 ltr. + 1000 ltr. = 5,000 ltr.)
 - Compressors
 - Icebank
 - Standby generator
 - Water pumps
 - Laboratory equipment
 - 2,000 liter insulated stainless steel tank for bulk milk transportation plus sundries and spare parts.

NOTE: Both milk chilling centers have identical equipment. Chilling center throughput depends on how long the chilled milk stays in the 5,000 liter storage tanks located at each plant. The plate cooler capacity is 3000 liters/hr.

- Milk processing plant at Alabang, which contains:
 - Milk reception scales
 - Milk pump
 - Plate cooler
 - Pasteurizer
 - Homogenizer
 - Refrigerated milk tanks
 - Compressor
 - 2 cold-stores
 - Laboratory equipment
 - Sundry items and spare parts.

NOTE: Alabang milk processing capacity is limited by the packaging equipment which has a capacity of around 100 liters per hour. Capacity of the pasteurizing/homogenizing equipment is 700 liters per hour. There is very little storage capacity for bulk pasteurized/homogenized milk.

- Insemination equipment, including two cryogenerators plus liquid nitrogen tanks and various semen collection and processing equipment
- Double-12 herringbone milking parlor and milk chilling unit, still in crates at Bukidnon, Northern Mindanao
- PDC management and administration assets, including motor vehicles, office equipment and furniture, air conditioners, refrigerators, SSB & VHF radio sets
- Dairy cattle, of which 2400 head were imported and dispersed to farmers.
- PDC owns no land. Its facilities are located on land owned by various national and local government units.

(2) The Equipment Is In Near New Condition, And Has Been Well Maintained; The Milking Parlour Is Still Crated

The milk chilling and processing equipment, most of which is stainless steel, was manufactured by internationally recognized companies, and is in excellent condition, as are the cryogenerators and liquid nitrogen tanks.

The majority of milk collection equipment is also in good condition, with the exception of some motorbikes that have been used extensively either by the PDC field staff or the farmer cooperatives.

Progeny Test Center equipment at Bukidnon is all in good condition according to PDC extension personnel. The milking parlor and chilling equipment, which is still in shipping crates, is new and the other assets have received little use. The crated equipment was purchased on the basis that the supplier, Danish Turnkey, would install and commission it prior to acceptance by the government. Danish Turnkey has confirmed that it will satisfy this obligation in the case of a new buyer.

PDC vehicles, office equipment and furniture are in good to fair condition.

5. THERE ARE TWO KEY SPECIAL ISSUES AND ONE ADMINISTRATIVE ISSUE WHICH COMPLICATE PRIVATIZATION OF PDC

(1) PDC Is Not A Viable Business Entity And The Only Assets Available For Sale Are The Various Sets Of Equipment, Which Are Held In Trust Rather Than Owned By PDC

PDC does not in fact hold title to the majority of assets, which are held under a trust agreement with the Philippine government in connection with PDC administration of the ADB-IFAD funded Small Holder Dairy Development Scheme. As noted above, PDC does not own any of the land on which its equipment is held. The buildings are also owned by other government units.

Ownership of the milk processing plant site at Alabang is under dispute among various government agencies and it is almost certain that the processing plant will not be retained there.

The dispersed cattle are already being sold separately to farmers. Thus PDC's saleable assets consist of various pieces of equipment as listed above.

(2) There Will Be Few Potential Buyers Of PDC Facilities And Equipment

Potential new entrants into the industry are discouraged by the actual and perceived barriers to successful operation of a milking and fresh milk processing venture. These perceptions have been reinforced by the failures of several operations over the past decade. Thus it is highly unlikely that anyone would purchase PDC as a going business, even if it were available. A few companies have, however, indicated interest in purchasing individual pieces of equipment.

(3) Provision Must Be Made For The Transfer Or Retrenchment Of PDC Staff

There are 90 staff members still employed by PDC, down from a total of more than 180. Some 44 of these are dairy production and/or processing specialists. Both BAI and DTRI have expressed interest in the possibility of having some of these technical personnel transferred to their respective agencies.

The greatest interest has been expressed by the administration of DTRI in hiring PDC technical personnel and picking up the PDC farmer support activities. This would, however, require a significant addition by the GOP to the DTRI budget.

The BAI feels that, in any case, the support capability for the PDC farmers is already in place within the BAI structure. Furthermore, BAI is currently being reorganized and no plans can be made to acquire PDC personnel until these plans are complete.

6. PDC CANNOT OPERATE AS A GOING CONCERN AND THE EQUITY VALUE IS OVERSTATED; PDC HAS HOWEVER, ENOUGH LIQUID ASSETS TO COVER ALL OUTSTANDING LIABILITIES

PDC, established in 1981, did not begin business operations until 1985. In the 1981-84 period, pre-production and start-up cost, were incurred; however, the details of those costs were unavailable to the Study Team because the financial records of PDC had been taken by the COA for audit. For this reason, it is also not known how much these costs were. However, the December 31, 1985, balance sheet shows only P72,790 as an asset balance of start-up costs, so it is reasonable to assume that most of the costs incurred during that period were expensed for accounting purposes. Because of the extended start-up period, the total start-up cost was probably extraordinarily high for an operation of the scale of PDC.

The PDC income statements and balance sheets for 1985 through 1987 are shown in tables III-1 and III-2 respectively. The 1986 income statement reflects only the period from April 1 through December 31, as the books were closed March 31, after the February revolution.

The income statements reveal a dismal financial condition, indicating that PDC cannot operate as a going concern. The cost of sales figures from the income statement certainly distort the real financial situation, e.g. the figures indicate that 1985 cost of sales were 182% of actual sales, while in 1986 they accounted for only 9%. Such inconsistency in the cost of sales must be attributable to inappropriate accounting in the matching of revenues and costs. Because the first three months of 1986 are not included in the data, a combined 1985 and 1986 total cannot be calculated. However, it is noted that for the data available, the total cost of sales exceeds the total sales revenue. This indicates that PDC did not establish viable procurement and marketing systems on which to build a business.

In 1985 operating costs were in excess of 1000% of sales revenue, and in 1986 they were nearly 500% of sales. By far the largest opera-

ting expense category is personal services, at 751% of sales and 391% of sales for the two years. In addition, the other operating expenses combined also exceed sales revenue in both of the years shown. Clearly, the levels of sales experienced by PDC could not possibly generate enough revenue to cover operating expenses. As a result, PDC showed losses from operations of 1100% of sales revenue in 1985, and 400% of sales revenue in 1986.

The total income (loss) figure is tempered by the income categorized as other income. Of the other income, the largest portion is interest, which is earned on the large amount of cash deposits and short-term securities held by PDC. This represents non-operating income, as it is not necessary to have an ongoing business to hold securities and cash deposits for interest. In both 1985 and 1986, however, interest income was larger than all other reported revenues combined.

The balance sheet indicates a substantial amount of liquidity due to the large cash deposits held. In fact, as of the March 31, 1987, balance sheet, total cash amounts to more than P82 million. This is sufficient to cover total liabilities at that date of about P74 million. The largest liability is shown as a trust liability to the national government in the amount of P72 million. This indicates that much of the financial impact of the closing of PDC will be a shifting

Exhibit III-1

PHILIPPINE DAIRY CORPORATION
 Profit and Loss Statement in Pesos
 Years Ended December 31, 1985 and 1986
 and Quarter Ending March 31, 1987

	1985	1986	1st Qtr. 1987
	----	----	----
Sales	631,002	543,267	0
Less: Cost of Sales	1,148,182	48,845	0
	-----	-----	-----
Gross Profit (Loss) from Sales	(517,180)	494,422	0
Less: Operating Expenses			
Personal Services	4,740,277	2,124,007	455,644
Rent Expenses	238,677	133,267	
Supplies and Materials	140,732	73,849	1,281
Communication Services	42,993	17,057	
Other Services	178,815	8,555	8,604
Amortization of Pre-Operating Organization Cost	57,607	43,212	
Water, Illum., and Power Serv.	60,000	30,000	
Taxes, Duties, and Licenses	1,224	16,237	9,968
Maintenance of Motor Vehicles	80,102	17,078	3,059
Transportation Services	328	150	
Auditing Services	116,816	9,377	
Travelling Expenses	44,906	3,003	2,010
Representation Expenses	10,000		
Depreciation Expenses	240,207	172,110	
Discretionary Expenses	475,333	20,098	
Insurance		1,016	
Bank Charges		1,916	1,520
Meeting Expenses		346	
Repairs and Maint. Facilities	12,047		
	-----	-----	-----
Total	6,440,064	2,671,279	482,086
Income (Loss) from Operations	(6,957,244)	(2,176,857)	(482,086)
Add: Other Income			
Income from Business Operations (25% PDC Share on Milk Collect.)	272,275	149,745	136,948
Interest Income	4,638,900	1,217,284	285,461
Miscellaneous Income	164,071	43,722	201,025
	-----	-----	-----
Total	5,075,246	1,410,752	623,434
Net Income (Loss)	(1,881,998)	(766,105)	141,348
	=====	=====	=====

Exhibit III-2

PHILIPPINE DAIRY CORPORATION
Balance Sheets Stated in Pesos

	Dec. 31 1985	Dec. 31 1986	March 31 1987
Current Asset	....	....	....
Cash on Hand	1,202,656	1,233,599	1,105,074
Cash in Bank	3,669,664	53,563,252	80,947,969
Cash Treasury/Agency Account			
Current Deposits		880,000	
Receivables	1,243,226	1,866,195	1,848,914
Inventories	420,556	231,252	243,298

Total	6,536,102	57,774,297	84,145,255
Other Assets			
Prepayments		1,518	15,968
Short-Term Investments	26,291,701		
Deposits	66,603	14,450	
Pre-Operating Organization Cost	72,790	15,176	15,176

Total	26,431,094	31,144	31,144
Investments			
Pilot Upgrading & Milk			
Production Project (PUMMP)	1,954,545	1,967,417	1,968,360
Contract Breeding	2,338,905	2,338,332	2,338,332
Smallholder Livestock Dev. Proj.	10,864,534	11,746,343	11,972,963
Smallholder Livestock Dev. Proj.			
-Economic Support Fund (ESF)	1,020,615	1,495,466	1,485,891

Total	16,178,599	17,547,559	17,765,547
Fixed Assets			
Land & Land Improvements-Held			
in Trust		239,598	239,598
Building & Structures-PSLDP		2,111,140	2,111,140
Building & Structures-Held			
in Trust		9,484,738	9,484,738
Building & Structures-Held			
in Trust (RPSP)		215,218	215,218
Leasehold Improvements	156,902		
Land Transportation Equipment	586,442	586,442	586,442
Furniture & Fixtures	335,253	336,866	336,866
Office Equipment	507,928	508,878	508,878
Field Equipment	1,125	1,125	1,125
Assets Held in Trust	46,995,380	52,597,130	52,597,130

Total	48,583,030	66,081,135	66,081,135
Less: Accumulated Depreciation	(805,675)	(3,646,936)	(3,646,936)

Net Fixed Assets	47,777,355	62,434,199	62,434,199
Contingent Assets			
Claims for Disallowed Payments	3,592,939	4,515,242	4,515,242
Total Assets	100,516,089	142,302,440	168,891,386
	=====	=====	=====

Exhibit III-2
(Continued)

PHILIPPINE DAIRY CORPORATION
Balance Sheets Stated in Pesos

	Dec. 31 1985	Dec. 31 1986	March 31 1987
Current Liabilities	----	----	----
Vouchers Payable	2,549,563	1,239,643	604,708
Payables - Others	40,000	20,038	20,038

Total	2,589,563	1,259,681	624,745
Trust Liabilities			
National Government	63,237,009	72,150,615	72,145,390
Government Corporations	9,899	(13,902)	44,582
Others	87,287	58,642	349,464

Total	63,334,196	72,195,355	72,539,436
Loans Payable-Foreign	19,500	19,500	19,500
Deferred Credits-Animals Dispersed	1,140,064	1,142,651	1,142,651

Total Liabilities	67,083,322	74,617,187	74,326,332
Capital and Surplus			
Capital Stock	100,000,000	100,000,000	100,000,000
Less Subscriptions Receivable	(63,355,607)	(41,843,842)	(16,990,842)

Paid-Up Capital	36,644,393	58,156,158	83,009,158
Invested Surplus Held in Trust		13,382,210	13,382,210
Capital Donated Surplus	86,000	86,000	86,000
Retained Earnings (Deficit)	(6,890,566)	(8,454,357)	(6,427,556)
Contingent Surplus	3,592,939	4,515,242	4,515,242

Total Capital and Surplus	33,432,767	67,685,253	94,565,054
Total Liabilities and Capital	100,516,089	142,302,440	168,891,386
	=====	=====	=====

of assets between government entities. The cash holdings are, however, currently allocated for the specific purpose as counterpart funds, thus these funds will have to be officially dedicated before they can be used to pay for liabilities.

The balance sheet data for many of the assets, including virtually all of the fixed assets, can be misleading, because this information is based upon the assumption that the business is a viable going concern that will continue to operate for the foreseeable future. Since this is not the case, many of the tangible assets are worth only their salvage value, regardless of the book value. Thus the equity in the firm, as stated on the balance sheet, overstates the value of PDC in the case of liquidation.

The fact that the financial statements of PDC are undergoing an audit and restatement by COA is of relatively minor significance for this study. The business is clearly not viable, and there can be no foreseeable results of the audit that would alter this conclusion.

7. PRIVATIZATION OPTIONS FOR THE PDC ARE VERY LIMITED DUE TO THE SPECIAL ISSUES INDICATED IN SECTION 5 AND BELOW

(1) The Surviving Cattle From The PDC Dispersal Program Are Being Sold To Farmers

There are an estimated 1,600 cattle still in the hands of farmer-recipients, from a total of almost 4,000 animals originally dispersed. The DA is in the process of negotiating the sale of these cattle to the farmers who hold them, at a price of P12,500 each, with payments made on an extended term basis and the farmer cooperative co-signing the purchase agreements as guarantors. Thus, these cattle are already in the process of being sold cannot be considered in the list of saleable items.

(2) PDC Does Not Own The Sites Where Its Facilities Are Located

The Trece Martires site is owned by the Bureau of Animal Industry, Department of Agriculture, and the Lipa site is owned by the local government. The ownership of the Alabang site is under dispute between the Department of Agriculture and the Department of the Environment and Natural Resources. PDC has been occupying the sites under the provision of letters of agreement. The proposed sire progeny test station at Bukidnon is the property of the BAI.

(3) The Milk Chilling Plants At Cavite And Lipa Are Located In Areas Where There Is Very Little Milk Supply

There is not an adequate supply of milk in either area to justify operating the centers, nor does it appear that there will be an adequate supply in the foreseeable future. In addition, the site at Trece Martires, Cavite, lacks enough water to operate the plant.

(4) The Remaining Physical Assets Are Still In Crates

The only other physical assets possessed by the PDC consist of a double-12 herringbone milking parlar and accompanying milk chilling equipment. There are in storage at Bukidnon, in Mindanao, still packed in their original crates.

(5) While Farmer Groups Have Been Offered The Equipment, At The Present Time It Appears That None Of These Are Financially Able to Set-Up And Operate Their Own Plants

The Southern Tagalog Dairy Cooperative is the only group organized sufficiently to utilize the PDC equipment. STDC is,

however, operating on a very low margin. It has a P100,000 credit cooperative loan falling due which cannot at present be repaid due to its inadequate cash flow.

(6) It Will Be Impossible To Sell PDC To The Private Sector As A Going Business; A Sale of The Assets Through Bids By The DAT or Using COA Guidelines Is Probably The Best Option

Approval for the sale must be obtained from the Committee on Privatization (COP). While transferring the assets to APT is one possible option, the assets are probably not of sufficient value to make APT divestiture procedures worthwhile. The most workable option would be a direct sale through a bid offering handled by the DA, since this would probably speed up the process considerably.

8. THE VALUATION OF PDC ASSETS IS CONFINED TO VALUE OF EQUIPMENT SOLD FOR LIQUIDATION

The value of the fixed assets of PDC were estimated as value in exchange of the equipment. Since no viable business entry has been identified, there is no value ascribed to any intangible assets. There are no real estate holdings of PDC, and all of the milk production and processing equipment is expected to be sold for relocation. It is expected that the equipment will be relocated within the Philippines.

Since there is not a broad domestic market for milk production and processing equipment in the Philippines, it is not practical to value the assets based upon sales of similar used assets. The best alternative for valuation is to use the depreciated replacement cost method.

All of the processing and milking equipment was purchased from Danish Turnkey Dairies. Invoices were inspected to determine prices paid. Consultation with personnel of Danish Turnkey Dairies indicated that prices of dairy equipment would have increased by at least 20% since the dates of purchase of the subject assets (December 1984 and May 1985). This information was used to adjust the historic cost of subject assets to a current replacement cost of comparable new assets.

The market for used equipment generally discounts the replacement cost very heavily, even if the assets are new and in good condition. Also, relocation costs tend to reduce the amount a buyer is willing to pay for such equipment. Generally this type of equipment would sell in a range of prices from 25% to 40% of replacement cost. For this analysis, the value in exchange of the assets is estimated as 35% of replacement cost.

A review of the invoices from Danish Turnkey Dairies was made to determine which items and cost elements would be included in the valuation. Specifically, the fixed assets of the milk processing plant in Alabang, the chilling centers at Trece Martires and Lipa, and the crated equipment in Bukidnon were considered as having value for sale. Items that were purchased for use by dairy cooperatives and miscellaneous supplies were assumed to have no value for sale.

Since this type of equipment would have to be imported by any buyer in the Philippines, freight and insurance costs are included in calculating replacement cost. Costs related to installation, start-up, and training were not included in the replacement cost for the milk processing plant and the chilling centers, because these services would not provide any benefit to the buyer who relocates the facilities. Installation, start-up, and training services are included as elements of value for the equipment in Bukidnon, because Danish Turnkey is still committed to provide such services to the ultimate buyer of the equipment.

Tables in Appendix E show the detail of the items of value, along with invoice prices shown. These prices are shown in Danish and Singapore currency for the December 1984 and May 1985 purchases respectively. For start-up services that are not ascribed any value, the invoice prices were replaced with zeros. For consistency with the invoices, each set of equipment (e.g. the milk processing plant) shows several asset listings with sub-totals.

The sub-totals are added to yield a grand total for each set of equipment. This amount is then multiplied by 1.2 to allow for a 20% increase in replacement cost. A currency conversion restates the replacement cost in Philippine Pesos. Finally, the replacement cost is multiplied by 0.35, to allow for the market discount of used assets. The result of this calculation is the estimated value in exchange.

The calculated values in exchange are shown below, rounded to the nearest thousand pesos.

	<u>Replacement Cost</u>	<u>Value in Exchanges</u>
Milk Processing Plant	P 8,533,000	P2,986,000
Two Chilling Centers	7,275,000	2,546,000
Crated Equipment in Bukidnon	<u>5,125,000</u>	<u>1,794,000</u>
Total	P20,933,000	P7,326,000

The two chilling centers are virtually identical, so the value in exchange of each center is 1,273,000, which is one half of the total calculated value in exchange for the chilling centers.

9. THE RECOMMENDED PRIVATIZATION OPTION FOR PDC IS TO LIQUIDATE THE ASSETS THROUGH A BIDDING PROCESS CONDUCTED BY DA

DA should as soon as possible complete the tendering requirements and bid out the available equipment, i.e., the administration equipment, chilling plants, processing plant, and crated milking parlor/chilling equipment.

BAI and/or DTRI should be encouraged to employ as many of the 44 PDC dairy production and processing technical staff as are interested in transferring to these organizations. Other staff should be absorbed by the Department of Agriculture, or retrenched with all appropriate benefits paid upon dismissal.

PDC should be closed down as an entity at the earliest possible date.

IV. REVIEW AND RECOMMENDATIONS FOR NFA/FTI DIVESTITURE

In late 1986, the Center for Privatization (CFP) completed a divestiture plan for operations considered by NFA to be peripheral to its grain stabilization activities. Those operations included:

- Food Terminal, Inc. (FTI)
- NFA Kadiwas
- Tabangao Bulk Unloading and Storage Facility
- Iloilo Thermal Generation Plant
- Southern Philippines Grains Complex (SPGC)
- Digos Agro-Industrial Complex
- Agro-Processing and Marketing Project (APMP), which includes the Northern Philippines Grains Complex (NPGC)
- Bicol Seed Company.

The purpose of this chapter is to review progress made on the privatization of these operations by the NFA and the DA. Based on this review, recommendations are made to expedite the privatization of these operations.

In response to the recommendations made in the CFP report, divestment activities were assigned by NFA management to the Special Operations Coordinating Office (SOCO), a department newly established within the NFA as a result of its 1986 reorganization. In addition, an Asset Divestment Committee for Peripheral Projects was formed June 11, 1987, headed by NFA's assistant administrator for Finance and Administration. Within SOCO, a Special Project Evaluation Team was formed with its main function being to review and evaluate all NFA Special Projects, conducting in-depth viability studies to determine the feasibility of privatizing peripheral projects.

1. A DIVESTITURE PLAN FOR FTI HAS BEEN PREPARED AND APPROVED BY THE NFA ADMINISTRATOR BUT IT IS NOT FEASIBLE TO IMPLEMENT

In June 1986, a joint NFA-FTI committee on privatization was created to develop a plan for divestiture for FTI. In December 1986, the Committee finished the plan which was approved by the NFA administrator in April 1987. An information paper on the FTI divestiture was submitted by the NFA Asset Divestment Committee to the DA in September 1987. The divestiture plan laid out three major steps:

- A recovery program
- Pre-divestment work, to be carried out between January 1987 and July 1988
- Sale of assets following various strategies.

The "recovery program" included:

- Revision of FTI's charter to become a for-profit corporation
- Transfer of land ownership
- Re-appraisal of equipment, facilities and building
- Restructuring the PNB/LBP loan
- Conduct of a Privatization Awareness Program
- Revision of COA and OCPC systems and rules
- Conduct of an effective promotional campaign.

The pre-divestment work was to consist of:

- Creation of an FTI-NFA Divestment Committee
- Study of the FTI Investment Package
- Hiring investment advisors
- Sale of non-performing assets.

The sale of assets was to have followed one of the following schemes:

- Plan A -- partial divestment of the joint venture with NFA, gradually disposing of the shares through the stock exchange or private placement
- Plan B -- full divestment through a 100% "lot sale"
- Plan C -- if plans A and B fail, sell the complex by segments.

In addition, the plan called for the creation of an NFA-FTI Asset Divestment Unit under supervision or in coordination with the SOCO. An independent company was to be hired to make a final re-evaluation of FTI's market value.

The divestment plan, as put together by the NFA-FTI Divestment Committee, however, is misguided. First, FTI can never be profitable as presently structured, and there is no conceivable way that it could become profitable operating under its present management, overstaffing, policies and goals. Therefore, even if it is set up as a for-profit corporation, its stock will have no value; its shares will not be saleable on the local stock exchange.

The FTI management, through press releases, has been strongly recommending that FTI continue as a GOCC, with funds for its rehabilitation provided by the government. Privatization goes against the personal and professional interests of FTI management, and there is no will on their part to privatize. Moreover, the sales price for the complex quoted by FTI and NFA, primarily to cover all outstanding liabilities is P2 billion (US\$100 million). This is based on faulty reasoning concerning the value of the complex. The CFP report included two valuations based on present and reduced electricity costs for the complex, not including the underdeveloped land, of P82 million and P239 million (or at most US\$12 million).

It appears that NFA does not understand the concept of valuation as explained in the CFP report as it wants to recover all of FTI's outstanding liabilities owed to the banks and to the NFA itself. These liabilities currently amount to:

Loans from banks and NFA	P 945.4 million
Advances from DBP	<u>495.0 million</u>
	P1,440.0 million
FTI real property "value"	<u>560.0 million</u>
	P2000.0 million

It was reported by various sources that FTI had already been transferred to the APT. Only the DBP and PNB loans, however, have been transferred to the APT. Thus, the full transfer of FTI to the APT needs to be effected.

On 23 October 1987, FTI management submitted a plan of operations, including a new "plan" for privatizing the complex, to the Department of Management and Budget. The plan notes that FTI has incurred losses of P134 million in 1985 and P159 million in 1986 -- then follows that up with a request for additional subsidies in the amount of P88 million plus P151.5 million to pay off its revolving credit line with PNB and Land Bank. FTI, with these subsidies, plans to fully lease out all industrial sites (10 hectares still remain), develop a comprehensive commercial complex, and enter joint ventures to develop housing and a hospital on the complex. The plan suggests that FTI be privatized by selling it to 2.2 million farmers who would pay P637 each as a "triggering factor to shape farmer groups as active and dynamic participants in the market and total economy." FTI would also be divested to lessees, clients and displaced employees, with current FTI ownership maintaining the majority share. This plan is totally unworkable and verges on folly.

FTI has taken several steps that may hasten the privatization of the complex:

- An improved waterline is nearly completed, which when connected will measurably improve the supply of water to the complex
- Conversations have been held with MERALCO and the NPC, which although not yet finalized, could result in a direct connection between the NPC grid and FTI's sub-station. As noted above, such a hook-up can make an enormous difference in the value of this complex
- A lease agreement has recently been signed with a Japanese electronics manufacturer for 28,000 square meters leased at P55 per square meter per year. The lease stipulates a 10% annual escalation and runs for 25 years, renewable for an additional six years. The rate per square meter is below that of other leases of comparable industrial sites -- market rates are about P70 per square meter
- FTI has closed 16 kadiwas (two were closed this year) and there are rental agreements that can be transferred to the private operator on many of the sites and buildings
- FTI has made some limited repairs to the lines in the refrigerated warehouse, and has considerably raised utilization there.

A memorandum of understanding has been signed with Laigo Company, an Italian firm that has proposed to upgrade the refrigerated warehouse. However, the NFA administrator expects nothing to come from the proposed deal.

One group of investors, First Pacific, has expressed its interest in purchasing the complex to NFA and FTI. The APT is aware of First Pacific's interest, and that of nine other parties.

Another constraint to privatization has arisen: FTI management has claimed that the original deed of donation of the land to the Military stated that if the land were not used for its original purposes, it must be reverted to the Ayala Corporation. However, conversations by the Project Team with the legal department of the Ayala Corporation revealed that neither the Corporation nor the Ayala family ever owned the land on which FTI is situated. According to Ayala's legal department, FTI's land was originally "friar land" owned by a religious order under the Spaniards. After the Spanish-American War, these lands were expropriated for distribution to tenants. Several areas were retained for strategic purposes, including Fort Bonifacio (formerly McKinley) and the site which eventually became Villamor (formerly Nicholl) Air Base. At independence the land was transferred by the U.S. Army to the Philippine Army.

However, the strategy to privatize the complex need not hinge on being able to transfer the land on a fee simple basis, although a transfer of land ownership to the private sector would certainly be preferable, both in the short- and long-term. The land tenure problems can probably be resolved by something tantamount to a presidential decree. If that could be accomplished, the short-term proceeds could be greatly increased, thus increasing revenues for the land reform program.

Perhaps the best strategy, given the present ownership arrangement, would be to sub-lease the facility to a user who can utilize components of the complex for its own business, manage and maintain the facility for present commercial and industrial lessees and further sub-lease other components, such as the slaughterhouse and chicken processing operation. Approximately 31 years remain in the long-term lease from the Military, ample time for a user to

occupy and recover carefully made investments. Once again, we would stress that the value of the complex will be greatly increased if title to the property can be transferred, but privatization need not be delayed until the transfer can be arranged. If it appears that an ownership transfer can eventually be effected, this might be structured as a "sub-lease with purchase option".

Conversations with the NFA administrator indicated that he was in favor of the privatization of FTI. He has two main requirements: adequate coverage of the retrenchment costs and some repayment on the approximately P676 million exposure NFA currently has in FTI. Regarding retrenchment costs, at one point in 1986 the NFA received a P100 million budget allocation, which was put in a reserve fund, especially for this purpose. Approximately P10 million of this fund has been used to pay interest on the PNB loan. Current retrenching costs are estimated by NFA and FTI to be approximately P100 million, as there were 1,482 employees as in June 1987. This figure should be re-calculated to assure that all accrued benefits can be paid to employees. NFA is making an effort to have UNIDEM, the Japanese electronics manufacturer, absorb some FTI staff. However, the Project Team has the impression that nothing was formalized in the lease agreement with UNIDEM and therefore there is no requirement for transfer of FTI staff to that company.

According to the 1986 FTI balance sheets, NFA has actually loaned FTI P195.4 million, the remainder owed NFA is P481 million, a debt of FTI to DBP that was assumed by the NFA. It is unlikely that NFA will recover much of this -- especially not in the short-term if the facility is sub-leased to a private operator.

Despite all of this reported activity, no concrete privatization action has been taken and actual sale of the asset is projected by SOCO for 1990. At least ten groups have offered to purchase the entire complex, but response to these offers has been

delayed until guidelines for its divestiture are prepared by the APT and approval is given for privatization.

The Project Team recommends the following privatization strategy:

- First, the DA should submit an application to the COP to privatize FTI; if approved, responsibility for its privatization would be assumed by the APT
- The second step should be to remove the board and management. This might be accomplished by pursuing several strategies, but each must be fully researched before proceeding:
 - As successor-in-interest to DBP, the APT can take advantage of various provisions under the standard loan agreement to effect a management and board takeover. Among such provisions is the assignment of 67% of the voting shares and the right to nominate board members.
 - As successor-in-interest to PNB, the APT may foreclose on PNB's P100 million loan exposure in FTI. Such a move would be unprecedented in Philippine public corporate history and would cause considerable political fallout, however.
- If neither of the above approaches prove workable, the only alternative to privatize FTI will be for the Secretary of Agriculture to exert his authority over the NFA administrator to effect the replacement of the board and management of FTI.
- The Secretary of Agriculture should propose to the President that ownership of the FTI land be transferred to

FTI from the AFP for ultimate privatization to benefit CARP, and that the problem of MERALCO rates by instructing NPC to connect directly to the FTI sub-station. If these two steps can be accomplished, cash proceeds from the FTI privatization will decrease dramatically.

- If land cannot be transferred from the AFP to the APT, then the complex should be sub-leased for 6 years, renewable for an additional period up to 25 years, to a private sector operator who would be entitled to manage and maintain all leased property, receive rents from such leases, construct additional structures as appropriate for leasing, and use structures and facilities for the operator's own business activities as required. Kadiwa operations should be shut down when the leasing arrangement is consummated.
- If the sub-leasing alternative is utilized, APT should perform a valuation based on lease and rental income at the complex, and should determine an appropriate escalator clause, since only the government's leasehold interest would be transferred. Total rental and service income in 1986 was P57.7 million. FTI's liabilities would most likely not be covered by the proceeds to the government from a sub-lease arrangement.
- APT should prepare bidding documents including:
 - Physical improvements
 - Present lessees, lease amounts and space utilization
 - Vacant space
 - Developable land
 - Kadiwa sites and buildings.
- Presently about 410 persons work in the Facilities Management Group. Conceivably these persons could be

absorbed by the private sector operator. Therefore, APT should document persons, titles, and salaries to be specified in the sub-lease agreement. It is recommended that these persons be retained by the private sector operator for a 6-month period, after which time the operator would be free to dismiss unproductive individuals.

- There should be at least 90 days between the announcement of the bidding to the opening of sealed bids to give prospective buyers ample time to inspect the premises and analyze financial data.
- The privatization of FTI need not be held up by the retrenchment of its personnel. Retrenchment should be the responsibility of the FTI caretaker management and board. NFA should turn over the P90 million it holds in reserve for retrenching costs. Retrenchment costs above the P90 million that NFA holds in reserve should be paid with sub-lease proceeds.
- Outstanding loan liabilities should be transferred to the DF for settlement.
- The FTI corporation should be continued, if the ownership of the complex cannot be transferred, to maintain the lease arrangement with the AFP.

2. THE CLOSURE OF ALL NFA KADIWAS REPRESENTS ONE SOLID STEP IN THE PRIVATIZATION PROCESS

At the time of the CFP study, the divestiture of the Kadiwa Centers was well underway with 64 non-viable outlets scheduled to be sold by November 1987, and 23 provincial centers that could be closed by year-end 1987.

The NFA continued these planned closures, finishing the task in June 1987. Three viable Kadiwas were divested to private sector operators, while four were taken over by the NFA employees association. All of the 242 Kadiwas and 47 satellite centers (minimarts) were closed or divested. As of August 1987 the remaining inventory had been reduced to P2.6 million.

These closures and divestitures demonstrate that privatization of government-operated commercial operations where there is already considerable private sector activity can be closed in the Philippines without social disruption.

3. THERE HAS BEEN SOME BUYER INTEREST IN PURCHASING THE TABANGAO BULK UNLOADING AND STORAGE FACILITY BUT NO CONCRETE ACTION HAS BEEN TAKEN

The CFP study recognized that the Tabangao facility was functionally connected to the Phil-Asia soybean processing plant and therefore should be sold with the plant. Some discussions were held by that study team with DBP officials -- DBP having the major outstanding exposure in Phil-Asia -- and subsequently the DBP and NFA senior officials held discussions on splitting the proceeds based on the respective exposures of DBP and NFA. The CFP recommendation for dividing the sales proceeds in that manner was made prior to the establishment of the APT and COP, and was based on the need for NFA to be responsible for its liabilities. At the time of that study the Tabangao-related liabilities included:

DBP	P32.5 million
Swiss Transfer Credit Facility	<u>17.2 million</u>
Total	P49.7 million

In a September 1, 1987, letter from the NFA administrator to the DA Undersecretary for Attached Agencies it was stated that the divestiture of Tabangao facility should be conditioned as follows:

- The amount of P126.5 million, representing the sound value of the property less outstanding DBP and Swiss Government loan balances, must be paid back to NFA
- Buyer must assume related liabilities:

DBP	P27.6 million
Swiss Transfer Credit Facility	<u>28.5 million</u>
Total	P56.1 million

- APT arranges recovery of P225.0 million from DBP for losses connected with Phil-Asia's bankruptcy (these losses resulted in soybeans provided to Phil-Asia by NFA)
- Tabangao personnel must be employed by the buyer at same or higher salary levels.

Letters have been received by NFA from four prospective buyers; however, other than replies to these buyers stating that NFA is undertaking a valuation of the complex and intends to sell the facility outright, no action has been taken. At the time of the Project Team interview, SOCO was seeking advice concerning how to undertake a valuation of the facility. It was learned later that APT had already completed a facility valuation.

The posture of the NFA vis-a-vis the Tabangao facility is unrealistic. It attempts to recover all expenses and liabilities incurred in connection with its construction and subsequent maintenance. Consonant with recommendations made elsewhere in this report, the Tabangao complex should be passed to APT and all related liabilities should be transferred to the Department of Finance. The first part of this recommendation has occurred de facto, as the APT is now promoting the sale of Tabangao. The assets corresponding to the non-performing DBP loan have already been transferred to the APT. Upon the transfer of the facility to the APT, the Swiss

Transfer Credit Loan should be transferred to the DF for eventual settlement.

Tabangao can be sold immediately, but some recognition must be made in its sales agreement of the integral connection of the unloading facility to the Phil-Asia plant. Bidders for Tabangao should be asked to examine the projected soybean delivery requirements for Phil-Asia, and to bid a per ton fee for unloading and/or storing shipments of soybeans.

There is an additional but probably not limiting complication: In 1983 NFA signed a 20-year agreement with the Pacific Flour Mills, Inc., that "allowed" the NFA to build its facility and permitted either party to use the other's pier in case either party had two ships to unload at the same time. It appears that this agreement could be assigned to the buyer of the Tabangao facility, or that Pacific Flour Mills might allow a release from this agreement. This agreement should receive careful consideration, but it should not pose an obstacle to the privatization of the facility.

The privatization of this facility can proceed immediately in the following manner:

- APT should attempt to assign the Pacific Flour Mills agreement
- APT should prepare bid documents stipulating:
 - Retention of the five employees manning the facility
 - Requirement to unload soybeans for the Phil-Asia plant and to bid fees to be charged that plant per ton of soybeans unloaded

- Ample time (at least 60 days) to examine the facility and prepare bids.
- NFA should remove rice or palay stored in the facility's warehouses or make arrangements with the private sector buyer for its continued storage on a fee basis
- Sale by bidding and transfer is concluded.

4. THE ILOILO POWER GENERATING PLANT IS IN LIMBO--NEITHER ABLE TO BE DIVESTED NOR OPERATED FEASIBLY

The previous CFP study of NFA peripheral operations found this facility in an economically precarious position:

- The power plant had experienced a series of technical problems (however, these have now been resolved)
- The amortization of the P48.5 million loan was to begin after the plant had functioned for a full year, with an amortization period of only 7 years
- The extension of a 75 mw submarine power line from the Negros Oriental geothermal plant planned for completion in 1989 would reduce the useful life of the facility and make the NFA facility superfluous
- The NFA milling facilities do not yield enough husk materials, and costs must be incurred to gather sufficient husks from millers operating within a 10-mile radius.

The CFP study recommended that the NFA negotiate with the British Government to convert the loan to a grant, but not to commission the facility until that arrangement had been established. The study also recommended that the facility be sold to the Panay Electric Company or the National Power Corporation

the only two buyers identified at that time who could buy the plant in its present location.

The NFA acted on the loan-to-grant conversion recommendation immediately in August 1986. However, it found out that no grant could be arranged because NEI, the engineering firm that designed and erected the facility, had provided the financing. The British Government had only guaranteed the loan, and the guarantee would not come into effect until the NFA defaulted on the loan. Furthermore, NFA could not default until the facility had operated for a full year.

NEI has, as of November 1987, completed operating, testing and debugging the facility for a full year, interrupted only because of a shortage of rice husks. Even though the facility is now fully functional, it is not certain when the facility will be accepted by the NFA. The plant has generated 1176 mw hours (only 800 hours of operation) between April and October 1987. The output was purchased by PECO for P800,000 (US\$40,000).

There is little reason for NFA to continue its ownership of this facility. The facility has little economic utility in its present location and NFA should not be in the power generation business. However, to escape this "catch-22" situation, the NFA, which is reportedly satisfied that the facility is operating properly, should now accept the facility from NEI and transfer it to the DA for divestiture. In addition to PECO, a potential private buyer might be some party interested in dismantling the facility and moving it to a remote location requiring electricity. PECO, in fact, probably will not bid on the plant because of the power supply that will become available within that region, especially after the Negros line is extended, which is expected within two to three years. The National Electrification Administration, a public body which promotes the installation of generating units under 5 mw, could be a buyer, but is reported to be in organizational disarray. The Project Team was also approached by an individual

interested in moving the facility to Palawan, and there may be numerous other prospective buyers who require electric power in remote locations. This may be the best ultimate use for the facility.

The outstanding NEI/British government and DBP liabilities should be transferred to the Department of Finance to be liquidated to the extent possible by the proceeds from the sale of the facility.

The Study team recommends that the privatization of this facility become the responsibility of the Undersecretary for Attached Agencies, who can put it out for sealed bids using COA guidelines.

5. NO CONCRETE ACTION HAS BEEN TAKEN ON SPGC; THE LARGE RICE-MILLING AND STORAGE FACILITY ON CENTRAL MINDANAO

The CFP report recommended that NAF sell SPGC to a single private sector operator. Once sold, the study recommended the following steps:

- SPGC be used as NFA's procurement agent for market interventions in Central Mindanao, with NAF paying SPGC the market price for storage of palay and milling of rice
- If feasible, shut down nearby NFA facilities to increase the volume handled by SPGC and other private millers.

SOCO has gathered data and made an on-site inspection to determine whether these recommendations are corrected. SOCO is currently drafting a re-evaluation of the CFP privatization plan.

One of the major issues that arises in connection with the privatization of rice milling and storage facilities, the Project Team believes, is that NFA perceives such steps as threatening to

its market stabilization functions. However, it is quite possible that its entire stabilization function could be carried out without owning either rice mills or storage facilities.

Milling could be done on a contract basis with private millers, as is presently done in Iloilo. Carrying this concept one step farther, NFA conceivably would not even have to own the storage facilities, but could contract the storage of palay on a bonded warehouse basis with private millers. These concepts should be the subject of further study, possibly under the forthcoming AAP project.

NFA appears reluctant to even experiment with any approaches that would diminish its "empire". For example, a demonstration farm forms part of SPGC, but serves no demonstration purpose and could have been sold during the past year if NFA were at all serious about privatization. Such a sale could have been accomplished by performing a single land survey to formulate a legal description followed by putting it up for bids following COA instructions on the disposal of GOCC property.

The privatization strategy for SPGC is as follows:

- DA submits plan for privatization to the COP. There appears to be interest in a lease with option to buy and that may be the best privatization strategy. Once approved, the facility is transferred to the APT
- APT should have the DBP staff review the assumptions of the discounted cash flow analysis valuation made by the CFP team in 1986. It should project a likely level of utilization by a private sector buyer, and thereby establish a benchmark value for the facility
- Appraisers should identify and value any excess equipment

- ADP should prepare bid documents specifying:
 - Physical facilities and plant
 - Requirement of bidder to review the personnel complement for the purpose of specifying employees to be retained for a 6-month period
 - Financial records will be turned over to the buyer
- Ample time, perhaps 90 days, should be allowed for examination of the facilities by prospective buyers
- The outstanding loan to the DBP should be transferred to the DF for settlement
- The DA should sell the 7.3 hectare demonstration farm, using COA guidelines, once the farm has been valued by local appraisers. A survey will be required to develop the legal description of the land.

6. NAFA HAS NEGATED THE CFP RECOMMENDATIONS FOR THE PRIVATIZATION OF THE DIGOS AGRO-INDUSTRIAL COMPLEX, CONCLUDING THAT THE COMPLEX SHOULD BE RETAINED BY THE AGENCY

SOCO compiled additional information on the Digos Complex and made a physical inventory of the facility. Its recommendations, now approved by the NFA Administrator, were:

- Retention of the complex by NFA in line with its procurement and distribution program in the region
- Divestment of the 8.1 hectare demonstration farm in concurrence with a recommendation made in the CFP report

- Further evaluation by NFA to determine what to do with the defective components of the complex.

Again, no concrete action has been taken as NFA appears incapable of disposing of any asset. The Digos privatization should proceed similarly to the SPGC process described above.

7. IT IS LIKELY THAT NPGC WILL BE SCALED DOWN TO PREPARE FOR ITS PRIVATIZATION

At the time of the CFP report, NPGC was less than 50% complete. That report supported the careful review of certain project components being performed at that time by the NFA. The review covered the parboiling plant, bran oil extraction and refining plants, feedmill, and power plant. The CFP report also recommended reduction in the Private Sector Modernization component and the Fruit and Vegetables Marketing Scheme.

The CFP report noted that the ricemilling facility was operational and could be privatized along with the storage facilities and satellite centers.

The SOCO reports that NFA is cutting back the scale of the project, with concurrence from the ADB, to make the facility more privatizable. However, no agreement has been reached with the ADB concerning whether certain components will be included in the project. However, the ADB will go along with any concrete plans to privatize the facility. NFA considers that it may be premature to privatize the complex and no concrete action has been taken by NFA.

The Study team recommends that DA monitor the situation closely and, if possible, help speed up the termination of the ADB-financed project. Once completed, it should transfer the ricemilling and storage facilities to the APT for privatization, in the same manner as the SPDC and Digos complex. The Study Team

believes, it should be emphasized, that no privatization action should be taken as follows.

The privatization process should proceed, when appropriate, as follows:

- DA submits privatization plan to COP for approval
- DA puts complex up for bids, using COA guidelines
- Sale should be on an "as is, where is" basis
- Proceeds from the sale should be turned over to the DA.

8. NO ACTION HAS BEEN TAKEN ON BICOL SEEDS PRIVATIZATION

Because of the location, poor condition, and insurgency activities in the Bicol region, the CFP report recommended putting the facility up for bid "as is". If there are no buyers, the report recommended liquidating the complex for parts or scrap.

SOCO officials have inspected the facility and reviewed documents on its acquisition; however, concrete action is being held in abeyance pending a final evaluation.

This facility should be transferred to ADT for sales "as is, where is."

9. THE OVERALL CONCLUSION REACHED FROM THIS REVIEW IS THAT NFA WILL NOT VOLUNTARILY PRIVATIZE ITS PERIPHERAL ACTIVITIES AND THUS THAT FUNCTION SHOULD NOT BE LEFT IN NFA'S HANDS

Nearly one year has passed since the submission of the CFP report.

The following conclusions must be reached:

- The is lack of understanding concerning the use of valuations as developed in that reported -- NFA continues

to believe that it should recover the "sound" value of the assets plus all interest, maintenance and other expense

- There is a lack of understanding concerning handling of liabilities -- NFA believes it will be required to pay off the outstanding liabilities after disposing of the assets connected with them
- NFA would prefer to study the possibilities and infinitum, rather than take any action
- Most importantly, NFA obviously does not want to have its "empire" tampered with.

Regarding valuation, there is no conceivable way that the sale of these assets will yield anywhere near "sound" value, not to mention cost sunk in financial advances, interest, maintenance, etc. NFA's unrealistic point of view is suggested in their valuation of FTI at P2 billion. "Sound" value of FTI was calculated by a local appraisal firm using original acquisition costs plus periodic asset value markups to reflect rising inflation. In contrast, the CFP report used a valuation concept based on projected, after-tax cash flow discounted by a rate reflective of required returns on equity and borrowing. While the APT reportedly has not used this latter methodology (along the COP approves its use) the APT has been selling assets for prices averaging 22% of book value. The CFP valuation used for going concerns in the Philippines has been yielding a similar figure.

There is no way that all of the costs resulting from mismanagement, political deals, out-of-scale development and graft and corruption can be recovered in a single privatization transaction. There is also some residual resistance to privatization in that write-off of a loss in book value when disposing of assets at the agency level must be approved by the

President of the country. This provision does not apply, however, when such assets are transferred to APT.

A part of the resistance to privatization by NFA is a belief that it will be required to pay off liabilities, especially in light of the likelihood that the operations will yield a relatively low amount, as noted above. With the transfer of the assets to the APT, the liabilities need to be transferred to the Department of Finance to handle repayment of loans to ADB and the Swiss Transfer Credit Facility and to repay Government-owned financial institutions to the extent possible, writing off the remaining outstanding balance. This was discussed with the NFA administrator who will go along with cleaning up his balance sheet, as long as NFA advances can be compensated in some way, probably on a pro-rata basis along with other liabilities.

A letter from the NFA administrator to the Department of Agriculture dated 1 September 1987 perhaps best summarizes NFA's intransigence regarding privatization:

"The privatization of other NFA properties be held in abeyance pending the re-evaluation of NFA management considering new policies and operations and the eventual sale, if done, shall be solely facilitated by NFA to give us a free hand on divestment options most advantageous to our Agency."

This point of view plus NFA's current attempt to re-establish a four import monopoly further demonstrates that the NFA has little intention in moving forward with privatization. It is not a good policy to allow operational managers to be involved with privatization decisions -- they have a vested interest in doing nothing.

On a broader basis, the Project Team recognizes the dilemma of the NFA:

- NFA does not receive, in its opinion, adequate national budgetary support to carry out its stabilization mission and, therefore, must resort to provide sector borrowing to finance its market interventions
- The flour and wheat import monopoly that it once held give it excess profits with which to cover its stabilization short-falls without borrowing
- It has some "white elephants" on its hands that must be amortized with scarce revenues.

The result is in NFA's view, an untenable financial position. However, it is important for the NFA to recognize what could be accomplished through privatization. It is possible that NFA could clean up its balance sheet and improve its cash flow by perhaps as much as P250 million through privatization of its peripheral assets. This figure is based on estimates made in the previous CFP study.

NFA did continue privatizing the Kadiwas, as it had already planned. However, nothing else has been accomplished, despite the fact that some buyers have expressed interest in certain facilities. At a minimum, NFA could have sold off the demonstration farm at Digos and SPGC.

The SOCO now projects the actual sale of assets as follows:

Operations

Planned Date of Sale

FTI	1st quarter 1990
Tabangao Complex	June-September 1988
Digos Complex	3rd quarter 1988
SPGC	4th quarter 1988
Bicol	1st quarter 1989
Iloilo Power Plant	To be determined
NPGC	To be determined

10. TO INITIATE THE ACTION THE SECRETARY OF AGRICULTURE SHOULD TAKE
DECISIVE ACTION TO PRIVATIZE NAF ASSETS

The major question raised by this review is whether there is a willingness to privatize this group of operations. If privatization is felt to be desirable for NFA, the Secretary of Agriculture must exert his authority over the NFA and FTI. FTI if it continues undeterred could end up employing "scorched earth" tactics, taking actions that would make its purchase undesirable to private investors. We recommend that the Secretary of Agriculture act immediately to have the FTI management and board replaced, so that privatization may proceed. The real lever that can be employed are the DBP and PNB loans that have been transferred to the APT.

To the extent possible, NFA assets should be transferred to the APT -- provided APT will accept them. To initiate that process, the DA should submit privatization plans to the COP when it submits the plans PCC and PDC. Once approved by COP and APT, the privatization process is initiated and will be more difficult to stop by NFA. Small assets, such as the demonstration farms at Digos and Tacurong, can be sold by the Undersecretary of Agriculture for Attached Assets using the guidelines for disposal of such assets prepared by the

COA. The liabilities incurred when the assets were acquired should be transferred to the Department of Finance.

USAID could facilitate this process by providing funds for technical assistance to the Department of Agriculture, purpose of which would be to assist the Undersecretary for Attached Assets to transfer these assets in an orderly fashion to the APT.

The Study Team believes that NFA will continue to delay the sale of these operations as long as their sale is left up that Agency.

V. RECOMMENDATIONS CONCERNING AN ASSET DISPOSAL
UNIT IN THE DEPARTMENT OF AGRICULTURE

The 1986 CFP report recommended that the Department of Agriculture (then Ministry of Agriculture and Food) set up an Asset Disposal Unit (ADU) to be responsible for the sale of the peripheral operations of the NFA. That recommendation was made because the Asset Privatization Trust had not been formed and "because of the possible, substantial delays in setting up an entity of such overriding importance to the privatization effort". In addition, it was felt that the NFA assets would have to compete for priority with a large number of other government holdings, many of which would command more attention by virtue of their size and importance to the country's economy.

The present assignment was to develop guidelines for the transfer of assets to the ADU and for disposition of liabilities associated with corporate assets to be privatized to the national government. However, the Asset Privatization Trust is now well established and staffed, and has been divesting government-owned assets at the rate of about one company per week as of October 1987. Coupled with that, The Secretary of Agriculture, as noted above, recognized the progress of the APT and felt that a more rapid divestiture could take place if NFA and DA assets were transferred directly to the APT.

The Project Team concurs with the Secretary's strategy; however, an ADV will still be required in the Department of Agriculture to take responsibility for the privatization tasks. These tasks include not only liaison with the APT, but also actual divestment of smaller assets and operations not transferred to the APT. The final recommendations concerning the ADU were formulated, and are included in detail below, after considerable discussion with Department of Agriculture officials following the completion of fieldwork in November 1987.

This chapter reviews the present privatization framework of the government to define further the role and activities of the proposed ADU. The framework for privatization is discussed in the following sections below:

- The role of the Committee on Privatization and information required to initiate the privatization process
- The role of the APT
- The Commission on Audit guidelines that would be employed by the Department of Agriculture to divest smaller assets
- The activities that should be undertaken by the DA.

1. THE COMMITTEE ON PRIVATIZATION WILL HAVE TO APPROVE THE DIVESTITURE OF DA ASSETS

On 12 August 1987 the Committee on Privatization mandated the procedures for approval of privatization plans.

The COP subsequently wrote to the DA, designating it as a disposition entity and asking it to develop and execute a plan for each corporation to be privatized. Being a disposition entity does not require that the DA itself divest the operation. If in the opinion of the COP, there is a separate organization that would be in a better position to implement the privatization of a particular corporation, another entity, usually the APT, may be designated.

Government departments may privatize GOCCs without going through this approval process, but the price, buyer and terms of disposition are still subject to approval by the COP.

The plan for divestiture of each government-owned corporation is to include the following:

- Extent of privatization
- Timing
- Modes of privatization
- Employment impacts
- Valuation
- Identification of potential investor types
- Rehabilitation prior to sale
- Financial restructuring
- Legal impediments.

Once the plan has been submitted by the DA, the COP has 30 days to act on it. Failure of the COP to act on the plan means that the plan is automatically approved. Appendix B of this report includes a draft of the privatization plans for the Philippine Cotton Corporation. Appendix C contains privatization plans for the NFA peripheral operations judged to be immediately privatizable.

2. THE ASSET PRIVATIZATION TRUST CAN SUBSEQUENTLY OFFER NFA AND DA ASSETS FOR BIDDING

The Asset Privatization Trust has set up a procedure for divestiture of state-owned corporations and non-performing assets. The Project Team believes that it is appropriate to immediately transfer the larger NFA and DA assets to the APT, including:

- Philippine Cotton Corporation
- Food Terminal, Incorporated
- Southern Philippines Grains Complex
- Digos Agro-Industrial Complex
- Tabangao Unloading Facility.

There are potential buyers for all of these facilities.

The Northern Pacific Grains Complex probably cannot be privatized now, for the reasons stated in Chapter IV.

Information provided in Chapter II on the Philippine Cotton Corporation can be provided to the APT by the DA for inclusion in the APT's General and Specific Catalogs, which are provided to potential buyers. (A draft of that chapter was given to the APT, which was especially interested in the valuations developed by the Study Team for PCC's various facilities.) The background and technical information in that chapter, if provided to potential buyers, may increase the proceeds from the sale of PCC assets.

A directive should be given by the Secretary of Agriculture to maintain the assets during the period until they are privatized. Upon sale, the rice and corn inventories of the NFA, specifically, should be transferred to other NFA facilities.

3. SMALLER ASSETS CAN BE DIRECTLY PRIVATIZED BY THE DA UNDER-SECRETARY OR ATTACHED AGENCIES USING COA GUIDELINES

The Commission on Audit Circular No. 86.264 issued October 16, 1986, presents the vehicle through which smaller easier-to-privatize assets can be sold. Such assets and operations include:

- Digos, SPDC, San Juan and Polomolok demonstration farms
- Other PCC farm land
- PDC milking, chilling and processing equipment
- Bicol seed company
- Iloilo Thermal Generating Facility.

Under the guidelines, public auction or bidding is to be the primary mode of disposal of the assets. The bidding procedures are to include:

- Adequate publicity and notification
- Sufficient time between publication of the bidding and date of submitting bids
- Opportunity to inspect the assets to be disposed
- Bonding and other prequalification requirements to guarantee performance
- Fair evaluation of the tenders and proper notification of the award.

In each case a Disposal Committee shall be formed by the "proper authority in the corporation". The Project Team believes that the proper DA authority is the Undersecretary for Attached Agencies, and that the Secretary of Agriculture should inform the affected GOCCs, the board of the PDC for example, of his intention, and then proceed.

This Committee is to provide the COA Auditor at least 20 days before the advertisement of the bidding with the following information:

- Program for disposal of assets, with time schedules
- Inventory list and description of the assets
- Appraisal reports
- Disposal procedures to be followed.

The advertisement of the bids is to be placed in a newspaper of general circulation for three consecutive days and a notice

must be placed in three locations near the assets to be privatized.

A draft of the bidding documents for the PDC assets are included in Appendix D.

4. PRIVATIZATION OF DA AND NFA ASSETS SHOULD BE COORDINATED BY THE UNDERSECRETARY FOR ATTACHED AGENCIES BUT NO SPECIAL ADU SHOULD BE ESTABLISHED

In addition to guidelines for the ADU, the scope of work for this assignment also required the identification of alternative modes for the ADU (Undersecretary of Attached Agencies) to access and utilize technical and administrative support services in carrying out its (his) functions, including:

- Performing sectoral/industry analyses, as necessary
- Reviewing existing business operations to determine overall commercial viability of concern and its components
- Performing project-specific studies as necessary (e.g., rehabilitation vs. liquidation)
- Estimating net worth of concern and its components, based on realistic assessment of market factors
- Conducting asset valuation of each component of the concern to determine break-up value
- Establishing a fair price for the concern and its components
- Assisting with turnover of accounting information, files, documents to ADU, including information on

physical assets, employment data and third-party creditor information

- Recommending appropriate information and data management systems, including both hardware and software
- Preparing sales materials, including prospectus, photos, maps, surveys, financial information, to be made available to prospective buyers; develop advertising and brochures
- Aggressive marketing of the concern, including preparation of a potential buyers list
- Preparation of sales memoranda
- Bid development
- Legal services
- Business statements in reference to offers received
- Investment banking services when necessary in case of world-wide sale of concern.

Given the information and strategies contained in this report, there is little left to do in the way of developing strategies for divestiture of these assets. There are other operations such as Planter's Products, Inc. or GRAINSCOR, within the portfolio that may require divestiture strategies, probably formulated using outside technical assistance. The APT, as described above, will handle the marketing of the larger corporations.

The responsibilities of the ADU should include the following activities:

- Surveys of the various demonstration farms so that the exact boundaries, land area and legal descriptions are determined
- Appraisals of the Digos and SPGC demonstration farms
- Formulation of bidding documents for the sale of the demonstration farms on an "as is" basis
- Formulate bidding documents for Bicol Seed Company on an "as is, where is" basis
- Formulate bidding documents for sale on lease of the Iloilo Thermal Generating Plant on an "as is, where is" basis, or for sale for removal to another site
- Conduct legal and financial negotiations related to asset disposals, assignment of financial responsibilities, retrenchment of and documentation for APT disposal purposes. This activity will support the privatization of operations by the APT, as well as those privatized by the DA itself
- Monitor operations until they are privatized.

In order to perform the various tasks associated with this function, and to prepare the larger units for transfer to the APT, the DA will need to establish an ADU, since personnel are not now available within The Department. However, only a very limited number of new staff (perhaps two or three) are required. In addition to these two or three staff members, it may be useful to contract outside consulting services to be provided in the same manner as those provided by Project Team.

Such a unit should only be set up on the basis that its tenure is limited. The ADU should be set up within the office of the Undersecretary of Attached Agencies for a maximum term of one-year.

These are easily within the capabilities of the Undersecretary's Office. The major requirement is follow-through.

APPENDIX A

PERSONS INTERVIEWED

Asian Development Bank

Mrigendramani Dixit, Financial Analyst
Peter Carroll
K. Kulavaratharajah, Project Engineer

Asset Privatization Trust

David Sycip, Executive Trustee
Leopoldo P. de Guzman, Associate Executive Trustee

Board of Investment

Ramona Miguel, Director, Agro-based Industries
Ofelia Bulaong, Director, Non-organic Fibers,
Textile Industry Group

British Cotton Growing Association, Ltd.

Iain M.R.S. Black, Director (Consultant to the ADB)

Bureau of Animal Industry

Dr. Manuel D. Rocha, Assistant Director
Jesus de Guzman, Director, Dairy Development

Bureau of Internal Revenue

Jaime Maya, Assistant Commissioner
Gregorio Sabayle, Assistant Chief Revenue Officer
Jesus Sandoval, Senior Revenue Legal Officer
Milardo Mansaguido

Central Bank of the Philippines

Edgardo del Fonso, Undersecretary of Finance

Cotton Research and Development Institute

Dr. Isagani G. Catedral, Officer-in-Charge

Department of Agriculture

Carlos G. Dominguez, Secretary
Conrado C. Gozun, Undersecretary for Attached Agencies
Emmeline Huang, Head Executive Assistant
Vicente Lim, AAP Program Coordinator

Dairy Research Training Institute

Dr. Teofilo A. Dulay, Plant Manager
Tonnette H. Pamplane
Gregorio L. Javier, Administrative Officer

Danish Turnkey Dairies
 Wilfredo L. Valencia, Area Representative

Imperial Textile Mills, Inc.
 Cesar Marcelo, Vice President, Finance
 Frank P. Karn

Land Bank
 Jesus F. Diaz, Executive Vice-President

Lucky Textile Mills
 Carlos G. Chung, President

Magnolia
 Mario R. Nery, Senior Vice President

Mindanao Cotton Development Corporation
 Benjamin Cruz, Personnel Officer

Monterey Farms
 Amadeo Veloso, President
 Santiago J. Freixas, Jr., Vice President, Livestock Operations

National Food Authority
 Emil Ong, Administrator
 Gregorio Y. Tan, Jr., Assistant Administrator
 for Marketing Development
 Teofilo T. Vergara, Special Assistant,
 Special Operations Coordinating Office
 Maristela S. Soriano, Staff Assistant, SOCO

New Zealand Trade Commission
 John Waugh, Trade Commissioner

Northern Engineering, Inc.
 Victor Newman, Senior Commissioning Engineer

Philippine Cotton Corporation
 Josemari F. Lim, Executive Vice President
 Jesse Gomex, Manager, San Fabian, Pangasinan
 Raffy Mendoza, Financial Officer
 Enrico Lucas, Extension Supervisor (Northern Luzon)
 Daniel Biosbas, Extension Supervisor (Northern Luzon)
 Rudolfo Anchata, Extension Supervisor (Northern Luzon)
 Roberto Ma. R. Arquiza, Vice President
 Mindanao Operations, Mindanao
 Isaac G. Larot, Regional Manager,
 Production Division, Mindanao
 Kudos A. Gayo, Assistant Vice President for
 Production, Mindanao

Philippine Dairy Corporation

Buddy Natividad, Manager, Finance & Administration
Baltazar Montiel, Dairy Development Officer
Marissa S. Montiel, Supervisor, Planning Officer
Lito Baarde, Dairy Development Farm Supervisor
Buenaventura A. Malabayabes, Dairy Development Coordinator
Dr. Jaime Lopez, Provincial Manager

Prime Index Philippines, Inc. (representative of NEI)
Andres L. Pizarro, President

Southern Tagalog Dairy Cooperative

Adolfo Gabfurio, President (Pagsanjan, Laguna)
Simon Santos, farmer member (Santa Cruz, Laguna)

Textile Mills Association of the Philippines

Benedicto V. Dakanay, Executive Vice-President

United Cotton Growers of Mindanao, Inc.

Henry P. Callao, President

Universal Textile Mills, Inc.

Walter Euyang, Vice-President

PERSONS INTERVIEWED

Mr. Orville Curry, Marketing, Lummus Industries, Inc. Textile Machinery Division, 712 Tenth Avenue, Columbus, Georgia

Mr. Larry Jay, Marketing, Lummus Industries, Inc., Textile Machinery Division, 712 Tenth Avenue, Columbus, Georgia

Mr. Mike Davis, The British Cotton Growers Association Ltd., 3 Shortlands, London W6 8RT

Mr. Hank Bush, Textile Machinery Export Association, Box 6968, Station B, Greenville, South Carolina

Mr. Ken Rowan, Manager, Broadview Cooperative Gin, Firebaugh, California

Mr. Aaron Smith, Manager, Rosedale Cooperative Gin, Inc., Bakersfield, California

Philippine National Bank, 700 South Flower Street, Los Angeles, California

Philippine Consulate General, 3460 Wilshire Boulevard, Los Angeles, California

APPENDIX B

PRIVATIZATION PLAN FOR THE
PHILIPPINE COTTON CORPORATION (PCC)
TO BE SUBMITTED TO THE
COMMITTEE ON PRIVATIZATION (COP)

I. BACKGROUND INFORMATION

- | | | | |
|----|-------------------------------|---|--|
| 1. | DATE ESTABLISHED/INCORPORATED | - | 22 December 1973 |
| 2. | BASIS OF ESTABLISHMENT | - | PD 350, as amended by PD 1063 |
| 3. | SECTOR/INDUSTRY | - | Agricultural Sector
Production, Processing
and Marketing of Cotton |
| 4. | SHAREHOLDERS: | | |
| | GOVERNMENT | - | National Government
94.6% |
| | | - | Philippine National Bank
5.0% |
| | PRIVATE | - | Textile Mills Association
of the Philippines
0.4% |
| 5. | DEPARTMENT ATTACHMENT | - | Department of Agriculture
and Food |
| 6. | PARENT COMPANY | - | None |
| 7. | FINANCIAL HIGHLIGHTS: | | |

	<u>31 December 1986</u>	<u>30 June 1987</u>
TOTAL ASSETS	P207,568,425.28	209,962,132.22
FIXED ASSETS	51,905,532.33	81,503,732.11
TOTAL LIABILITIES	245,630,800.96	247,777,971.62
NET WORTH	(38,234,129.09)	(37,815,839.40)
GROSS REVENUES	68,994,108.89	(33,566,058.89)
NET INCOME (LOSS)	(80,714,392.93)	(4,472,592.73)

BASIS:

AUDIT OF COMMISSION ON AUDIT

II. FACTORS TO CONSIDER

1. The company has an outstanding long-term loan of US\$4.3 million from the Asian Development Bank. Consent of the Bank for the privatization of the fixed assets may have to be obtained beforehand.
2. The company has an outstanding industrial loan with DBP to establish the San Fabian Complex. The assets of the San Fabian ginnery complex are pledged to DBP.

III. PRIVATIZATION PLAN

1. **EXTENT OF PRIVATIZATION** A 100% divestiture to the private sector is envisioned.
2. **MODE OF PRIVATIZATION** The assets of PCC will be sold, with liabilities being transferred to the DF.
3. **METHOD OF PRIVATIZATION** Assets should be sold through sealed bidding based on well-prepared bid documents.
4. **POTENTIAL INVESTOR GROUPS** Bidders for the San Fabian,

Pangasinan and Polomolok gins are likely to be companies presently engaged in cotton ginning or textile millers. A rice miller or tobacco trader may be interested in the ginning building warehouse, etc. of the San Juan, Ilocos Sur facility, after the gins have been removed. The gin at San Juan can be sold to ginners interested in setting up a gin in other locations such as Panay, Cebu, etc.

Local farmers will purchase the demonstration farms and undeveloped parcels.

5. VALUATIONS

Values have been estimated in two ways: discounted cash flows for those ginning assets to be employed within a going concern; liquidation values for those assets to be sold for removal to another location.

Demonstration farms can be bid off separately. Our valuation

estimates are as follows:

- . San Fabian (operating concern)
P11.2 million
- . San Juan, Ilocos Sur
(liquidation) P2.2 million
- . Polomolok, So. Cotabato
(operating concern)
P29.7 million

These evaluations were carried out by Arthur Young, an international accounting firm.

6. TIMING OF PRIVATIZATION

- . San Fabian assets should be put out for bids on March-April 1988, allowing PCC time to complete its current crop/harvest/ginning cycle.
- . San Juan assets could be put out for bids immediately, as the plant is presently mothballed, but because its sale as an operating gin will decrease the overall sales proceeds from its sale and the San Fabian ginnery, it should

be sold at the same time as San Fabian, with the provision that its ginning equipment will be removed.

- . Polomolok assets can be put for bids in March-April 1988, allowing it time to complete its current crop/harvest/ginning cycle.

7. PROGRAM OF ACTIVITIES

1. Department of Agriculture submits application for privatization to COP
2. COP amends/approves application
3. APT develops bid documents for three facilities:
 - San Juan and San Fabian facilities should be put out for bids simultaneously, with the provision that San Juan is for removal of ginning and ancillary equipment only
 - San Fabian and Polomolok facilities should be sold during March-June

ginning season to generate maximum buyer interest and sales proceeds

- World sales channels will have to be tapped to sell the San Juan equipment since there is little market demand for used ginnery equipment

4. Department of Agriculture develops retrenchment program recommending the retention of key local employees, absorption of a certain number of employees into the Department, and dismissal of the remainder, with full payment of benefits to those dismissed.
5. After sale of the San Juan ginning equipment, the remaining real property there should be re-appraised and offered as tobacco and

rice storage facilities

6. The demonstration farms at San Juan and Polomolok should be transferred to CRDI or should be sold
7. The land lease at Nueva Ecija and the seed production joint venture at Zambales will have to be wound up through negotiation or legal proceedings
8. Unsold baled cotton inventories should be sold to textile millers by PCC or included in bid documents as assets.
9. The DA will take appropriate financial measures:
 - Freeze all PCC bank accounts as soon as privatization decision is final
 - Receivables are aged and collection strategies are formulated. In conjunc-

tion with COA, determine
bad debts to be written
off.

- Transfer loan liabilities
to APT for settlement

10. Department of Agriculture
closes down PCC headquart-
ers and sub-leases space or
relinquishes space in head-
quarters building.

APPENDIX B

CUERVO APPRAISERS EQUIPMENT INVENTORY

SAN JUAN, ILOCOS SUR

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
<u>Ginnery</u>		
2 - Suction Telescopes - Lummus Cotton Gin Co., USA, GI tubings, size 370 mm dia., with 360° ball joint, complete with balancers, counterweights and suction pen with 1-rock catcher, GI sheet housing, single suction, 406 mm dia., complete with dis- charge pipe, overflow pipe control valve, GI tubings and supports	P 254,500	P 127,200
Unloading Separator - Lummus, Model HM-22 1/2, 572 mm dia. cylinder x 1829 mm face width, mild steel housing with built-in blower and vacuum wheel, 572 mm dia. cylinder x 1829 mm face width, mild steel plate housing, mainly driven by 11.2-kw electric motor, 1760 rpm, complete with dust flue discharge line, ductings, structural steel supports, catwalk, railings and controls	532,000	319,300
Conveyor Distributor - Lummus, screw type, approx. 254 mm dia., U-bottom, 10.06 m L, mild steel plate construction, driven by 7.5-kw electric motor, 1770 rpm, complete with feeder hopper, supports and controls	400,000	240,000

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
<p>2 - Gin Stands - Lumms, Model Thermex "double moming", 90 saw blades, air blast type, 310 mm dia. saw blades, 1830 mm face width, driven by 18.7 7-kw motor, complete with air blast feeder, pipe lines and automatic seed weighing scale</p>	<p>P 3,776,000</p>	<p>P 1,699,200</p>
<p>Seed and Hull Conveyor - Screw type 230 mm dia. x 10.06 m L, U-trough, mild steel plate cons- truction, driven by 5.6-kw electric motor, 1740 rpm with spiral eleva- tor, driven by 2.2-kw electric motor, 865 rpm, complete with piping and standard parts and accessories</p>	<p>487,100</p>	<p>243,500</p>
<p>Inclined Lint Cleaner - Lumms, 2440 mm face width x 2134 mm long, with 6-spiked cylinder, 305 mm dia., with vacuum wheel, 584 mm dia. x 1830 mm face width, mild steel plate housing with discharge chute, commonly driven by 15-kw electric motor, 1755 rpm, complete with controls and supports</p>	<p>1,754,600</p>	<p>1,052,700</p>
<p>Outfil Battery Condenser - Lumms, 1016 mm dia. x 1372 mm width drum assembly, mild steel plate housing, 1930 mm dia. x 1372 mm face width driven thru gear reducer by 2.24-kw electric motor, 1730 rpm.</p>		

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
with vane axial tube blower, 1070 mm dia. driven by 11.2-kw motor, 1740 rpm, with lint fly catcher and lint slide, complete with pipings, controls and standard parts and accessories	P 1,065,500	P 532,700
Seed Cotton Drier - Consisting of: Oil fired burner, Model 77, Ser. NO. 7717, 640 mm dia. x 660 mm L combustion chamber, 3 million Btu capacity, with vane axial fan driven by 2.25-kw electric motor, complete with igniter, gauges, regulator and standard parts and accessories;		
Hot Air Push Fan - Axial vane type, Lummus, Model HF176, Hot Air Pull Fan - Lummus, Model HF196, complete with hot air ductings, cyclone collectors and standard parts and accessories;		
Tower Drier - 23-shelf, 4 stage, mild steel plate construction, 1828 mm L x 1828 W x 6.44 m H, complete with hot air ductings and standard parts and accessories (Note: Push/Pull Fan without drive units)	1,690,000	845,000
Thrash & Ling Fly Exhaust System - consisting of: Elevator Double Fan - Axial vane type, 914 mm dia. blade,		

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
mild steel plate housing, driven by 30-kw electric motor, 1770 rpm, complete with cyclone collectors, ductings, controls, steel supports and standard accessories;		
Gin Thrash Fan - Axial vane type, driven by 15-kw electric motor, complete with ducting and accessories;		
Lint Cleaner Exhaust Fan - Axial vane type, driven by 11.2-kw electric motor, 1770 rpm, complete with lint waste cyclone collectors, ductings, supports and standard accessories	P 946,100	P 473,000
Air Blast Fan - Lummus, Model HF176, 1000 mm dia. blade, mild steel plate housing, vane axial type, driven by 30-kw electric motor, 1770 rpm, complete with pipings, controls, supports and standard parts and accessories	558,000	362,700
Press System - consisting of: Lint Feeder - Lummus, belt-type, 1372 mm W x 1220 mm centers, mild steel housing, driven by 3.75-kw Reuland brake motor;		
Tramper - Lummus, chain type, driven by 11.2-kw brake electric motor;		
Bale Press - Lummus, 686 mm x 1372 mm double box, low density, all metal pressing unit		

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
with steel deck turntable, power turning, 3.5 m dia. driven by 0.37-kw geared motor, 356 mm hydraulic cylinder, single acting, 2.13 m ram travel with hydraulic pump unit, driven by 30-kw electric motor, 1780 rpm, complete with controls and standard parts and accessories	P 9,200,000	P 7,360,000
 <u>Miscellaneous</u>		
13 - Platform weighing Scales - Century Scale, beam type, 500 kg. capacity, 50 cm W x 74 cm platform	74,100	32,500
Impulse Sealer - Tew, Model T1SF-450, 450 mm sealing width, 400 watts, 230 volts	4,000	1,600
Engine Pump Set - Honda, Model F200, centrifugal type, 51 mm x 51 mm suction and discharge, driven by 5 HP air-cooled gasoline engine	11,800	7,600
Fire Pump - Koeler, Model K-341, centrifugal type, 38 mm x 38 mm suction and discharge, driven by 16 Hp. single cylinder engine	23,000	15,000

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
Agricultural Tractor - Masey Ferguson, Model MF165, power by 60 Hp., 4-cylinder diesel engine, with MF-34 disc harrow, 20 mm - 558 dia. disc (Note: Unite in Guimba, Nueva Ecija - not inspected, appraisal based on reasonable averages)	P 519,000	P 155,700
Electric Forklift - Toyota, Model 4FB15, 1,400 kgs. capacity, clamp type, 5000 mm max. lift height, battery operated, 48 volts, DC motor, Ser. No. 4FS15- C24	248,000	173,600
Electric Forklift - Toyota, Model 3FB10, 900 kg. capacity, fork type, 4000 mm max. lift height, batter operated, 48 volts DC motor, Sev. No. 3FB10- 10951	248,000	99,200
Air Compressor - Vespa, 2 cylinder, reciprocating type, driven by 0.375-kw electric motor, 1720 rpm, complete with air receiver and standard parts and accessories	14,000	7,000
Electric Grinder - Bench type, double arbor, 177 mm dia. grinding wheel, 381 mm distance between arbor, driven by 0.37-kw elec- tric motor	4,500	1,800

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
Machinist Vise - Stationary type, 229 mm jaw	P 3,600	P 1,200
Engine Pump Set - Yanmar, centrifugal type, 102 mm x 102 mm suction and discharge, driven by 10,5 hp., single cylinder, air-cooled diesel engine	42,000	21,000
3 - Engine Pump Sets - Briggs & Stratton, centrifugal type, 51 mm x 51 mm suction and discharge, driven by 5 hp., single cylinder, air-cooled gasoline engine. (Note: Units out of order)	35,400	10,600
2 - Battery Chargers - Toyota, Type SG3-69-75, 48 VDC, 6.4 kva	17,600	7,000
Room Air-conditioner - Carrier, split packaged type, 5 tons capacity, Ser. No. 056NP2377	65,000	39,000
Radio Transceiver - ADTECH, FH/SSB, Model AF-150SB, 150 watts, Ser. No. 81-101B, com- plete with antenna and microphone	40,000	26,000

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
Portable Generator Set - Robins, Model LG102, 1200 watts, driven by Robins EY-150, single cylinder, air-cooled gasoline engine (Note: brand new)	P 12,400	P 12,400
2 - Roller Gins - No nameplate 60 kgs.hr. cap., 14 cm dia. x 100 cm L roller, belt driven by 2.2-kw electric motor, 1780 rpm (Note: 1-unit in CROI Batac)	158,000	94,800
2 - Power Transformers - Powercome, 250 kva, 13200/240 colts, oil-immersed self-cooled, Ser. Nos. 32185-C and 32185-A	330,000	198,000
Elevated Water Storage Tank - Welded mild steel plate cons- truction, 10,000 gallons cap., 340 cm dia. x 500 cm H on 10 meter steel towers, with piping distribution system, complete with valves and fittings	276,000	165,600
Sumbersible Pump - Granfos, 1.5 kw, 38 mm x 38 mm suction and discharge, 51 mm well casing, 54,8 meters well depth, complete with standard parts and accessories	51,000	30,000
3 - Distribution Transformers - Super, 15 kva, 1380/240 volts, oil-immersed self-cooled	78,000	46,800

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
Truck Scale -		
Toledo, Model 4351, 50 tons cap., 3.04 meters x. 15.24 meters, rein- forced concrete platform, Ser. No. 81168, complete with electronic digital printer and standard parts and accessories (Note: brand new)	P 1,150,000	P 1,150,000
 <u>Laboratory Equipment</u>		
5 - Moisture Testers -		
Delmhorst, Model CM-1, 0-20 moisture range, battery operated, 9 VDC	50,000	42,500
2 - Soil Testers -		
OSK, EM System	7,400	4,400
2 - Thermohydrographs -		
Sunshine Recorder - Siap, Bologna	9,800	5,800
Sunshine Recorder - Siap, Bologna	9,300	7,500
Light Trap Housing -	6,500	3,900
Rain Gauge -	6,500	3,900
Anemometer -		
Weathertronic, Model 2511, Ser. No. 349	<u>19,400</u>	<u>13,600</u>
	P 24,173,300	P15,630,300

APPENDIX C

PRIVATIZATION PLANS
FOR NFA PERIPHERAL OPERATIONS
CONSIDERED IMMEDIATELY PRIVATIZABLE

COMPANY: FOOD TERMINAL, INC.

Date Prepared: November 1987

I. BACKGROUND INFORMATION

1. DATE ESTABLISHED/INCORPORATED - May 3, 1968
2. BASIS OF ESTABLISHMENT - PD 347
3. SECTOR/INDUSTRY - Commercial Sector-
Grocery Wholesaler

Real Estate Sector-
Lessor of industrial
wholesale and retail
lands and buildings

Industrial Sector-
processor of meats and
poultry
4. SHAREHOLDERS - National Government
100%
5. DEPARTMENT ATTACHMENT - National Food Authority,
Department of Agriculture
6. PARENT COMPANY - National Food Authority
7. FINANCIAL HIGHLIGHTS:

II. FACTORS TO CONSIDER

1. The 120-acre site was transferred in 1969 from the Fort Bonifacio Military Reservation to the Greater Manila Terminal Food Market by Presidential Decree that set up a 25-year lease, renewable for an additional 25 years. The lease has 6 years to run

before the renewal date. If the ownership of this land can be transferred to FTI the proceeds from the privatization will be dramatically increased. If this transfer cannot be arranged, it can be privatized using a sublease. There should be an "option to purchase" clause in the agreement if it appears that the ownership of the land can be transferred at some point.

2. FTI employs a large number of employees, currently 1,482 who have few options to be retained by the government. Retrenchment costs are estimated by the NFA administrator to be P100 million. Some 400 employees of FTI's Property Management Group could be retained by a private sector operator of the complex after privatization. NFA has P90 million in reserve that should be used for retrenchment costs.
3. The company has an outstanding loan of P93 million payable to the Land Bank. NFA considers that it has P500 million plus in loans made to FTI, and that will have to be sorted out.

4. A recent agreement has been signed with UNIDEM, a Japanese electronics manufacturer to construct an industrial facility on 3 hectares.
5. Another agreement was signed recently with Laigo, an Italian company, which wants to undertake a project to rehabilitate the refrigerated warehouse. This agreement, unless it includes concessionary funding, should be terminated.
6. Electricity costs charged by MERALCO in the past have seriously reduced FTI profitability. FTI has been trying to negotiate an arrangement whereby it purchases electricity directly from NPC. If such an agreement can be reached, it will reduce power costs and raise the value of the complex.
7. FTI continues to operate a series of Kadiwa food outlets in Metro Manila. These should be closed down and sub-leased.
8. FTI has the following short-term investments:

Trustfund investment	
PNB	P3.145 million
DBP	.220 million

Treasury bills	
PISO Bank	8.0 million
Union Bank	6.103 million

III. PRIVATIZATION PLAN

1. EXTENT OF PRIVATIZATION

If AFP retains title to the land, the complex can be subleased to a private sector operator who will be entitled to receive all sub-lease payments, to sub-lease structures, land and agribusiness components, to construct buildings for leases, and arrange for appropriate lease payments; all improvements revert to the AFP at the end of the lease period. Such a sub-lease might include an option to purchase if land might ultimately be transferred.

3. METHOD OF PRIVATIZATION

Complex will be sub-leased out to operator based on competitive annual lease payments plus escalations.

4. POTENTIAL INVESTOR GROUPS

Local and foreign companies experienced in property management operations.

5. VALUATION METHOD

Target annual sub-lease value should be determined by discounted cash flow method,

using current and projected income of the Estate Management Operation of FTI.

6. TIMING OF PRIVATIZATION

Sub-leasing to private operator can be done immediately.

7. PROGRAM OF ACTIVITIES

1. APT and DA jointly remove FTI management and board; caretaker manager and interim board are installed
2. Valuation based on discounted lease and rental income should be completed
3. Preparation of bidding documents including list of all present lessees, lease amounts and terms, physical improvements, vacant building space, developable land, and Kadiwa sites and buildings.
4. Putting operation out for sealed bids with at least 90 days for prospective bidders to inspect premises and analyze data
5. FTI property management personnel transfers to FTI headquarters building -- to make room for successful bidder to occupy the premises
6. NFA should transfer retrenchment funds to FTI. FTI caretaker management and board retrenches personnel. Retrenchment costs exceeding

reserve should be paid out of
privatization proceeds.

TABANGAO UNLOADING FACILITY

I. BACKGROUND INFORMATION

1. DATE ESTABLISHED - 1981
2. BASIS OF ESTABLISHMENT - NFA project
3. SECTOR/INDUSTRY - Underloading dock (infrastructure) and warehousing
4. SHAREHOLDERS - National government 100%
5. DEPARTMENT ATTACHMENT - National Food Authority, Department of Agriculture
6. PARENT COMPANY - None
7. FINANCIAL HIGHLIGHTS:
(REQUESTED BY THE UNDERSECRETARY)

II. FACTORS TO CONSIDER

1. There is an outstanding loan repayable to the Swiss Transfer Credit Facility amounting to approximately P28.5 million
2. There is a 20-year agreement signed by the NFA in 1983 with the Pacific Flour Mills, Inc., which allows either party to use the other's pier in case one party had two ships docking during the same period. Agreement can probably be derogated or assigned.
3. NFA rice and palay inventories stored in the warehouses will have to be removed upon sale of the facility.

4. Conveyor is limited in type of grains it can handle. It was designed to handle soybeans or other smooth grains. Handling other grains will seriously erode conveyor equipment.
5. This facility was originally constructed to serve the Phil-Asia soybean processing plant. Phil-Asia will eventually be divested by APT and APT should reserve right of future buyer of Phil-Asia to use Tabangao unloading facility to unload soybeans on a fee basis.
6. NFA presently employs 5 persons at facility who are familiar with its operation and who should be employed by private sector buyer.

II. PRIVATIZATION PLAN

- | | | |
|----|---------------------------|---|
| 1. | EXTENT OF PRIVATIZATION | 100% immediately |
| 2. | MODE OF PRIVATIZATION | Sale of Assets |
| 3. | METHOD OF PRIVATIZATION | APT should sell through sealed bidding |
| 4. | POTENTIAL INVESTOR GROUPS | <ol style="list-style-type: none"> 1. Grain dealers or millers who require uncongested docking facilities 2. Purchaser of Phil-Asia 3. Docking/warehousing company that will adapt dock to unload from ship-to-barge |

5. VALUATION METHOD
6. TIMING OF PRIVATIZATION
7. PROGRAM OF ACTIVITIES

for movement of grains to Manila Bay/Pasig River.

APT has prepared valuation of Tabangao dock and warehouses

As soon as possible

1. Facility is listed for bids providing ample time (at least 60 days) for buyers to examine and prepare offers
2. Bidding documents are opened and award is made
3. NFA removes any rice and palay inventory
4. Sales transaction is concluded.

OPERATION: SOUTHERN PHILIPPINE GRAINS COMPLEX

Date Prepared: November 1987

I. BACKGROUND INFORMATION

- | | |
|----------------------------|---|
| 1. Date Established | Early 1970s |
| 2. Basis for Establishment | Private investment project of the Mindanao Progress Corporation (MINPROCOR) foreclosed on by the DBP and sold to the National Grains Authority, the predecessor of the NFA. |
| 3. Sector/Industry | Industrial Sector Ricemill and oil extraction and refinery |
| 4. Shareholders | 100% government-owned |
| 5. Department Attachment | National Food Authority
Department of Agriculture |
| 6. Parent Company | Not Applicable |
| 7. Financial Highlights | Have been requested |

II. FACTORS TO CONSIDER

- SPGC is a very large ricemilling operation, with a 25 ton/hour Buhler Miag ricemill installed in a seven-story concrete building. This operation faces considerable competition from 21 private sector millers located within a 100-kilometer radius of Tacurong.
- The buyer must be capable of operating in Mindanao, despite the instability caused by the MNLF and other forces.

III. PRIVATIZATION PLAN

- | | |
|-----------------------------|--|
| 1. Extent of Privatization | 100% |
| 2. Mode of Privatization | Sale of assets to be used as going concern |
| 3. Mode of Privatization | Sealed bidding executed by the APT |
| 4. Potential Investor Group | Rice millers and traders |
| 5. Valuation | Discounted cash flow method yields a range of values, given varying utilization rates:
40% utilization P33.6 million
50% utilization 50.9 million
60% utilization 68.2 million
Utilization under aggressive management could probably exceed 50%. Utilization of |

6. Timing of Privatization

7. Program of Activities

the plant during 1978-84 averaged 49%.

Valuation was done by Arthur Young, an international accounting firm.

Divestiture can proceed immediately; arrangements must be made with NFA to remove rice inventories before closing.

1. APT should have the DBP staff review assumptions for discounted cash flow analysis valuation made in 1986, which is attached.

2. Appraisers should be used to identify and value any excess equipment.

3. APT should advertise for sealed bids, providing ample time for potential buyers to visit the plant and prepare projections. The bidding documents should ask that the buyer review the personnel complement, and offer to specify workers to be retained for a 12-month period after the sale.

4. The outstanding loan of the DBP, currently P _____, should be transferred to the DF for settlement.

5. The DA should sell the 7.3 hectare demonstration farm, using COA guidelines,

once the farm has been valued
by local appraisers.

COMPANY: ILOILO THERMAL ELECTRIC
GENERATING PLANT

Date Prepared: 1987

I. BACKGROUND INFORMATION

1. DATE ESTABLISHED/INCORPORATED - 1986
2. BASIS OF ESTABLISHMENT NFA Project
3. SECTOR/INDUSTRY Energy Sector
Power Plant based on
rice husks as fuel
4. SHAREHOLDERS Wholly owned by NFA
5. DEPARTMENT ATTACHMENT Department of
Agriculture
6. PARENT COMPANY National Food Authority
7. FINANCIAL HIGHLIGHTS: NA

II. FACTORS TO BE CONSIDERED

NFA financed the project in part with a longterm loan of P48.5 million from Northern Engineering, guaranteed by the Government of the U.K. NFA attempted in August 1986 to have the loan converted to a grant, but this cannot be done until NFA officially defaults on the loan and the UK government exercises its guarantee.

Extension of a 75 kw submarine power line from the Negros oriental geothermal plant, scheduled for completion in 1989 will make the facility superfluous.

The plant has been operated, tested and debugged for one year as provided in the purchase contract.

The plant has been able to operate only 800 hours total between April and October, 1987, because NFA rice mills in the area have been unable to supply adequate rice husks.

III. PRIVATIZATION PLAN

1. EXTENT OF PRIVATIZATION 100%
2. MODE OR PRIVATIZATION Sell assets, with liabilities to be transferred to DF
3. METHOD OF PRIVATIZATION Sale to be handled by DY Undersecretary for Attached Agencies in compliance with COA guidelines, through sealed bids.
4. POTENTIAL INVESTOR GROUPS

The logical bidders for the facility in place are the Panay Electric Company or the National Power Corporation: however, with the power line from the Negros geothermal plant to be brought in during the next two or three years, neither may bid.

Alternatively, a private investor may be interested in purchasing the plant for removal to another site. At least one such investor has already made inquiries.
5. VALUATION

Facility valuation was established by Arthur Young, an international accounting firm and based on discounted cash flow analysis. Since the plant has not yet been put into operation as an income producing entity, the operating expenses and revenue projections are based on

NFA estimates revised to reflect what is felt to be a more realistic level of capacity utilization. The value of the plant, based on a projected capacity utilization of 75% with a five year useful life is P10,397,000; with a 10-year useful life it is 6,144,000. Cost of dismantling and relocating the plant would reduce the estimated value; however, this should be offset by the longer useful life at a new location.

6. TIMING OF PRIVATIZATION

Should be bid out as soon as possible.

7. PROGRAM OF ACTIVITIES

NFA should immediately accept the facility and transfer it to DA for privatization, concurrently notifying the U.K. government that is defaulting on the loan and requesting that the loan be converted to a grant.

DA submits application for privatization to COP.

COP amends/approves application.

DA develops bid documents and proceeds to sell the facility through sealed bids.

COMPANY: DIGOS AGRO-INDUSTRIAL COMPLEX

I. BACKGROUND INFORMATION

- | | |
|---------------------------|--|
| 1. DATE ESTABLISHED | 1973 |
| 2. BASIS OF ESTABLISHMENT | Acquired from RCA |
| 3. SECTOR/INDUSTRY | Industrial, rice and corn milling, warehouse |
| 4. SHAREHOLDERS | Wholly owned by NFA |
| 5. DEPARTMENT ATTACHMENT | Department of Agriculture |
| 6. PARENT COMPANY | National Food Authority |
| 7. FINANCIAL HIGHLIGHTS | To be developed |

II. FACTORS TO CONSIDER

Digos has extensive but underutilized facilities which should make it easier to privatize, including:

Three warehouses/21,000 mt. Nine bulk storage silos
10 T./hr Satake rice mill
Corn mill (inoperable)
Mechanical drier
Assorted vehicles/farm equip.
13.5 ha land/improvements
Office building
Training center

The warehouse and training center are presently leased to Coca-Cola

III. PRIVATIZATION PLAN

1. EXTENT OF PRIVATIZATION 100%
2. MODE OF PRIVATIZATION Divestiture of assets to the private sector in their entirety or as separate components with financial liabilities transferred to DF.
3. METHOD OF PRIVATIZATION Transfer to APT for sale by sealed bids.
4. POTENTIAL INVESTOR GROUPS Investors looking for a modern rice mill and warehouse.
5. VALUATION The facility was valued on a discounted cash flow basis.

Fair market value was adjusted to take into account projections of utilization levels.

Utilization (%)	Value (P000)
0	(23,744)
10	(15,367)
20	(6,990)
30	830
40	7,065
50	13,232
60	19,400

70	25,568
80	31,736
90	37,904
100	44,071

6. TIMING OF PRIVATIZATION

As soon as possible

7. PROGRAM OF ACTIVITIES

Inspect and appraise demonstration farm site to determine physical facilities and conditions and to assess market value.

DA sell farm by sealed bidding according to COA guidelines

Transfer remainder of assets to APT for bidding out

Transfer liabilities to DF

COMPANY; BICOL SEEDS, INC.

I. BACKGROUND INFORMATION

1. DATE ESTABLISHED/INCORPORATED

1974

Acquired by NFA in 1980

2. BASIS OF ESTABLISHMENT

Purchased from PDGP for P9.3 million

3. SECTOR/INDUSTRY

Industrial processing sector-- rice mill and associated facilities.

- | | | |
|----|--------------------------|---------------------------|
| 4. | SHAREHOLDERS | Wholly owned by NFA |
| 5. | DEPARTMENT OF ATTACHMENT | Department of Agriculture |
| 6. | PARENT COMPANY | National Food Authority |
| 7. | FINANCIAL HIGHLIGHTS | NA |

II. FACTORS TO CONSIDER

The complex is badly deteriorated, capable of achieving only half its rated capacity and is very little utilized.

The complex would require at least P-1 million to make it operational.

The electric generator (525 Kva) is too big and thus too costly to operate.

The facility is poorly located since it is not near a major highway.

There are a large number of private, competing rice mills in the area.

III. PRIVATIZATION PLAN

1. EXTENT OF PRIVATIZATION

2. MODE OF PRIVATIZATION

Sell "as is, where is"; or, if bids are forthcoming, offer equipment for liquidation sale; sell land and buildings separately.

3. METHOD OF PRIVATIZATION

Transfer to APT

4. POTENTIAL INVESTOR GROUPS

Rice millers needing additional capacity and/or equipment; local business firms seeking warehouse space.

5. VALUATION

NA

6. TIMING OF PRIVATIZATION

As soon as possible

7. PROGRAM OF ACTIVITIES

Transfer assets to APT

If APT not willing to assume sales responsibility, AD should sell in compliance with COA guidelines.

APPENDIX C

CUERVO APPRAISERS EQUIPMENT INVENTORY

POLOMOLOK, SOUTH COTABATO

1970

POLOMOLIK, SOUTH COTABATO

197B

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
<p>Suction System - consisting of: Power Telescope - Lummus cotton gin Co., USA, Size 381 mm, 360° ball joint swing, with inner and outer GI tubings, with balancer and counterweights; Rock Catcher - GI sheet housing, single suction, 406 mm dia., 230 mm dia. discharge, manual shut-off valve, complete with GI tubing (Note: Dismantled, for future expansion)</p>	P 133,300	P 80,000
<p>Suction System - consisting of: 2 - Travelling Power Telescopes - Lummus Cotton gin Co., USA, Size 381 mm, 360° ball joint swing, 90° arm travel with flexible boot, with trolly on I-beam track, 9.14 m long, driven by 0.25-kw motor, with automatic balancer; Rock Catcher - GI sheet housing, double suction, 406 dia., with manual shut-off valve, complete with GI sheet pipings</p>	1,343,000	1,303,000
<p>2 - Vacuum Wheels - Lummus, Cotton gin Co., USA, No. 5-315, 560 mm dia. x 1830 mm face width, steel plate housing (Note: Uninstalled)</p>	328,600	197,200

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
<p>Unloading Separator -- Lummus Cotton Gin Co., USA, Product ID No. 4-211, 1120 mm dia. cylinder, 2440 mm face W with flushing, mild steel plate housing, equipped with built-in blower and bottom vacuum wheel, Lummus, ID No. 5-361, 864 mm dia. x 2440 mm face W, mild steel plate housing, mainly driven by 19-kw electric motor, 1750 rpm, complete with structural steel supports, cat- walks, railings and ladder, and controls.</p>	<p>P 963,000</p>	<p>P 934,100</p>
<p>Unloading Separator - Lummus Cotton Gon Co., USA, ID No. 4-221, 1020 mm dia. cylinder, 1830 mm face W with flushings, mild steel plate housing, equipped with vacuum wheel, I.D., No. 5-373, 560 mm dia. x 1830 mm face W, mild steel plate housing, mainly driven by 15-kw electric motor, complete with struc- tural steel supports, catwalks and railings and controls</p>	<p>576,700</p>	<p>461,400</p>
<p>Inclined Lint Cleaner - Lummus Cotton Gon Co., USA, ID. No. 8-284, 2440 mm face W x 2134 mm long, with 6-spiked cylinder, 305 mm dia., with vacuum wheel, ID No. 5-298, 584 mm dia. x 2440 face W, mild steel plate housing, with discharge chute, commonly driven by 15-kw Columbus Electric motor, 1755 rpm, complete with controls.</p>	<p>1,754,600</p>	<p>1,702,000</p>

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Reproduction, New</u>	<u>Sound Value</u>
<p>Conveyor Distributor - Lummus Cotton Gin Co., USA, ID No. 3-223, screw type, 406 mm dia., U-bottom, 610 mm W x 711 mm H x 10.06 m L, mild steel plate housing, 3-sheave belt driven by 15-kw electric motor, with hopper for feeders, complete with supports and controls</p>	<p>P 717,200</p>	<p>P 502,000</p>
<p>Ginning System - consisting of: Feeder/Extractor - Lummus Cotton Gin Co., USA, Model 700, ID No. 2-298, mild steel plate housing, with spiked extractor cylinder, 2440 mm long, with trash conveyor and stainless steel cotton slide;</p> <p>Gin Stand - Lummus Cotton Gin co., USA, Model Imperial 158, ID No. 1-274, 158 saw blades, 305 mm dia. on shaft, 2440 mm long, with brush doffer, 508 mm dia. x 2440 mm W, spiked extractor cylinder, mainly driven by 93.25 kw Columbus Electric motor, 1775 rpm, with lint flue pipe, 152 mm t x 2440 mm face W, mild steel plate construction, complete with controls and other standard accessories</p>	<p>3,808,000</p>	<p>3,173,300</p>

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Reproduction, New</u>	<u>Sound Value</u>
Ginning System - consisting of: Feeder/Extractor - Lummus Cotton Gin Co., USA, Model 700, ID No. 2-235, mild steel plate housing, with spiked extractor cylinder, 2440 mm long, with trash conveyor and stainless steel cotton slide; Gin Stand - Lummus Cotton Gin Co., USA, Model Imperial 158, ID No. 1-218, 158 saw blades, 305 mm dia. on shaft, 2440 mm long, with brush doffer, 508 mm dia. x. 2440 mm W. spiked extractor cylinder, mainly driven by 90-kw Asea motor, 1764 rpm, with lint flue pipe, 152 mm t x 2440 mm face W, mild steel plate construction, complete with controls and other standard accessories	P 3,808,000	P 3,173,300
Seed & Hull Conveyor - Screw type, 2-row, 230 mm dia. x 230 mm plight, U-trough, mild steel plate construction, 254 mm W x 305 mm D x 10.67 m L, 76 mm dia. shaft, 2-sheave belt driven by 3.7-kw elec- tric motor, 1730 rpm, complete with elevators and other standard accessories	540,100	486,100

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
Seed Blower - Roots Connersville, Type AF, Size 717, Ser. No. 5528-145, rotary lobe type, positive displacement, 3-sheave belt driven by 15-kw electric motor, 1760 rpm	P 213,000	P 117,200
Overflow System (Automatic Suction Control) - Lummus Cotton Gin Co., USA, ID No. 6-302, 2440 mm W with feed rollers, mild steel plate housing, with air cut-off valve, equipped with vacuum wheel, 572 mm dia. x 2440 mm face W, mainly driven by 11.2-kw Relance motor, complete with GI piping and electrical controls	1,164,300	1,129,400
2 - Lint Cleaners - Lummus Cotton Gin Co. USA, Model 108, ID No. 11-261 and 11246, 406 mm dia. saw type brush doffing cylinder, 762 mm dia. screen drum cylinder, mild steel plate housing, each mainly driven by 30-kw motor, 1720 rpm, with lint fly catcher, each equipped with vane axial fan, Lummus, ID No. 14-331 VAF24 and 1- none, 6-blade, 610 mm dia. driven by 11.2-kw motor, with discharge flue pipe, 203 mm t x 2440 mm face W, complete with 914 mm dia. GI pipings, 1070 mm dia. x 1830 mm H lint fly catcher, supports and controls	4,312,000	3,816,000

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Reproduction, New</u>	<u>Sound Value</u>
<p>Elevator Fan (For Unloading Separator #2) - Lummus Cotton Gin Co., USA, ID. No. 19-1060, Model HF-176, centrifugal type, 914 mm dia. blade, steel plate housing, 1016 mm dia. x 305 mm w, 3-sheave belt driven by 30-kw Columbus Electric motor, 1765 rpm, with 4 cyclone collector, 838 mm dia. x 1524 mm H, conical botton, 1830 mm H, complete with ductings and other standard accessories, with GI pipings, supports and controls</p>	<p>P 310,600</p>	<p>P 233,000</p>
<p>Lint Cleaner Trash Fan - Lummus Cotton GinCo., USA, MOdel HF136, ID No. 19-1065, centrifugal type, 610 mm dia. blade, 762 mm dia. x 241 mm W steel housing, 3-sheave belt driven by 11.2-kw Reliance motor, 1765 rpm, with 2-cyclone collectors, mild steel plate welded construction, 838 mm dia. x. 1524 mm H, conical bottom, 1830 mm H, complete with ductings and other standard accessories</p>	<p>223,900</p>	<p>167,900</p>
<p>Gin Trash Fan - LUmmus Cotton Gin Co., Model FH136, ID. No. 19-1065, centrifugal type, 610 mm dia. blade, 762 mm dia. x 241 mm W steel housing, 3 sheave belt driven by 15-kw Columbus electric motor, 1760 rpm, with 2-cyclone collectors, mild steel plate welded construction, 914 mm dia. x</p>		

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
1830 mm H, conical bottom, 1830 mm H, complete with ductings and other standard accessories	P 229,200	P 171,900
Welding Machine - Daihen, Model KR-300, 300 amps. rating, transformer type	8,800	5,700
Bench Grinder - Double arbor, 356 mm center distance, 203 mm dia. wheel, fractional kw drive	3,300	1,700
Welding Outfit - Harris oxy-acetylene with welding and cutting torches	5,500	3,600
Wire Cutting & Straightening Machine - Ebis, Type No. 402, 3.7 kw motor, 3 mm dia. min. capacity, 305 m L, steel construction with standard motor drive	189,400	142,100
Spare Motor - Reliance, 7.5 kw rating, 1160 rpm, 3-phase 230/460 volts, foot mounted	19,700	14,800
Outfit Battery Condenser - Lumms, ID NO. 13-203, 1016 mm dia. x 1372 mm W drum assembly with flushing, mild steel plate housing, 1930 mm dia. x 1372 mm face W, driven thru gear reducer by 2.24-kw Reliance motor, 1750 rpm, with vane axial tube blower, 1070 mm dia., 11.2-kw GE motor, 1740 rpm,		

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Reproduction, New</u>	<u>Sound Value</u>
with lint fly catcher, 1220 mm. dia. x 4.88 mm L, GI sheet welded construction with lint slide, 1372 mm W, mild steel plate construction, complete with controls, pipings and other standard accessories	P 1,065,500	P 799,000

Press System -
consisting of:

Lint Feeder -

Lummus Cotton Gin Co. USA, ID. No. 15-283, 1372 mm W belt x 1220 mm centers, mild steel plate housing, driven by 3.7 kw Reuland brake motor, with magnetic brake;

Tramper -

Lummus, ID No. 18-4434, heavy duty, chain type with sills, belt driven by 15-kw brakemotor;

Bale press -

Lummus, ID. No. 17-486, 1372 x 508 mm double box standard density up packing, all metal pressing unit, with steel deck turntable, power turning, 3.5 m dia. driven by 0.37-kw gearmotor, 356 mm dia. hydraulic cylinder, single acting, 2.13 m ram travel with follow blocks, 508 mm x 1372 mm;

Hydraulic Control Unit -

Lummus, ID. No. 18-772, Model H-188, 2-hydraulic oil pumps, Size 51 mm x 38 mm, 6-sheave belt driven thru common shaft by 56 kw Smith Gray Electric motor, 1780 rpm, mounted on oil tank, mild steel plate welded

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
construction, 1981 mm L x 914 mm W x 1070 mm H, system complete with controls and other standard accessories for normal installation	P 9,343,000	P 8,008,000
 Hydraulic Control Unit - Lummus Cotton Gin Co., USA, ID. No. 18-678, Model H-188, 2-hydraulic oil pumps, Size 51 mm x 38 mm, mounted on oil tank, 1981 mm L x 914 mm W x 1070 mm H, mild steel plate welded construction (Note: Not in use, no drive motor)	1,201,000	720,600
 Dehumidifier - Samuel Jackson Mfg. Co., Cat. No. CT2200, 115 volts, 60-cycle, single phase, with rotary pump, 6.35 mm size, coupled to 0.37-kw motor	11,000	6,600
 Automatic Weighing Scale - Fairbanks Morse, Code Spec 11485 NAWB7AK, Ser. No. G376584, 910 kgs. capacity; beam type, with Budgit electric hoist, 500 kgs. capacity, manual trolley on I-beam, 9.14 m L	30,000*	30,000
 Electrical Control System - consisting of: MCC #1 - Fuji Haya Electric, 600 amps. ACB, with magnetic contactor, metal clad		

* Reproduction Cost New Less Depreciation

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Reproduction, New</u>	<u>Sound Value</u>
housing, 4-vertical section, self-standing;		
MCC #2 -		
Fuji Haya Electric, 1000 amps total		
ACB, 2 main control switches, with voltmeter and ammeters, 7 vertical sections, metal clad housing, self-standing;		
MCC #3 -		
Cutler Hammer, 400 amps. ACB, metal clad housing, complete with wirings and other standard accessories	P 353,000	P 282,400
2 - Cotton Module Builders -		
"Hyfab", Hydraulics & Fabricators Pty. Ltd., roller bed type, 9.57 m L x 2.3 m W bottom x 2.3 m H, steel plate housing, 2-wheel mounted, hydraulic retract, approx. 508 mm lift, hydraulic rear door, overhead travelling compactor, 2.9 m stroke hydraulic cylinder, each with 2-side mounted elevating and tipping baskets, mild steel plate welded construction, each with 3-stage hydraulic pump with oil reservoir, driven thru Twin Disc power transmission, Model No. SP111P3 by 4-cylinder Perkins diesel engine, Engine Nos. LD90121U916171K, and LD90121U916179K, battery starting, skid mounted complete with draw bar, operator's platform and other standard accessories		
(Note: brand new)	2,935,000	2,935,000

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Reproduction, New</u>		<u>Sound Value</u>	
Battery Charger - Locally fabricated, 12 & n 24 volts, approx. 10 amps. capacity	P	2,500	P	800
3 - Wire Tire Balers - Maren Eng'g Corp., Illinois, USA, Model 30, Ser. No. 9801, portable type, 3 ties, 15 Ga. single loop bale ties, 2.9 m long, horizontal with hydraulic pump, Sperry Vickers, driven by 3.73-kw electric motor, 1735 rpm (Note: Units in crates, used in Area VII)		570,000		342,000
Cotton Ginning Machines - Lummus Cotton Gin Co., USA, consisting of: Suction Telescope - Size 305 mm dia., 360° rotation, with balancer; Rock Catcher - GI sheet welded construction; Unloading Separator - Type C, Model Cs6, Ser. No. CS6- C-35, 914 mm dia x. 1830 mm face W drum, mild steel plate housing, with vacuum wheel, 406 mm dia. x 1830 mm face W; Conveyor/Distributor - Screw type, 406 mm dia., 406 mm plight, 89 mm shaft, 9.14 m long, U-trough, msp construction; 2 - Gin Stands - 90 saws, 1830 mm face width, with airblast, feeder and automatic seed weighing scale;				

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
<p>Cotton Seed & Hull Conveyor - 2-row, screw type, 254 mm dia. x 254 mm plight, approx 12.2 m long, U-trough, msp construction;</p> <p>Battery Condenser - Mild steel plate housing, 1372 mm dia. x 1070 mm face W;</p> <p>Tower Drier - Mild steel plate welded construction, 19-shelf, 4-stage, 1372 mm x 1220 mm x 5.5 m Hf, with oil-fired burner;</p> <p>Inclined Cleaner - Model 11, Type C, Ser. No. 11-C-24, steel plate housing, 1830 mm W, with vacuum wheel, Model 19, Type C, Serv. No. 19-C-129, mild steel plate housing;</p> <p>Hot Air Push Fan - Hi-Efficiency, No. 176, centrifugal type, 914 mm dia. blade, 1016 mm dia. housing, steel plate welded construction;</p> <p>Baling Machine - 1016 mm x 456 mm double box density up packing, 2-hydraulic rams, 254 mm dia., hydraulic cylinder, 991 mm x 445 mm follow block, with tramper, hydraulic control unit, complete with flat belts and pulleys and other standard accessories (Note: Not operational, dismantled, some parts cannibalized)</p>	<p>P 9,140,000</p>	<p>P 900,000</p>
<p>Double Roller Gin - N. C. Panchal Industries, Made in India, 1070 mm working width, with</p>		

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
fixed knives, CI frames, complete with standard motor drive, counter-weight and other standard accessories	P 79,100	P 55,300
Diesel Generator Set - Caterpillar diesel engine, Model D348, V12, 665 kw, 1800 rpm, turbo-charged, Engine Ser. No. 36V03337, directly coupled to Caterpillar AC generator, Model SR4, 620 kw, 240/480 volts, 3-phase, Ser. No. 589, complete with automatic transfer switch, control panel, circuit breakers, radiator and standard parts and accessories	2,636,000	2,320,000
Electrical Distribution System - Consisting of various sizes and types of wires, complete with conduits, supports, insulation and other standard accessories for normal installation.	838,000	735,700
3 - Power Transformers - Powercom, 250 kva, 7620/13200Y, oil-immersed self-cooled, Class OA, Ser. Nos. 5811017 and 5811018 (Note: One unit without Ser. No.)	495,000	432,000
Distribution Transformer - Super Manufacturing, Inc., 225 kva, 13800/240 V, oil immersed, self-cooled, Type OA, Ser. No. 84-10A06	135,000	118,000

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
Fuel Tank (Day Tank) - Welded steel construction, 121 cm L x 154 cm W x 121 cm H, 2,250 liters cap. equipped with 20 mm flow meter and standard parts and accessories	P 21,000	P 17,600
Fuel Storage Tank - Welded steel construction, 3.05 m dia. x 5.18 m L, 37,000 liters cap., complete with manhold and inspection ladder, on steel pedestal, in concrete foundation	110,000	92,000
Elevated Water Storage Tank - Welded steel construction, 558 cm dia. x 600 cm H, 113,500 liters cap. on 2439 cm steel tower, complete with inspection ladder and catwalk, deep- well, submersible pump, 3.75 kw drive motor and standard parts and acces- sories	623,000	548,200
Water Distribution System - Consisting of various types and sizes of pipes, complete with valves and fittings	228,000	201,000
Truck Scale - Toledo, Model 4351, 50,000 kgs. capacity, 3.0 m W x 15 m L, platform dimension, complete with digital printer unit and standard parts and accessories	1,150,000	978,000
3 - Module Cotton Trailers - Bush Hog Loadcraft, 8-wheeler, double axle, steel construction,		

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
1082 cm L x 242 cm W, roller conveyor type trailer bed, 14,500 kgs. gross vehicular weight, complete with hydraulic tilting unit, hydraulic winch, and tow bar, Ser. Nos. FB855130, FB855131 and FB-855132	P 1,320,000	P 1,290,000
80 - Seed Cotton Steel Pallets - Welded steel framework, 222 cm W x 950 cm L with corrugated GI sheet top	704,000	688,000
Pallet Trailer - Locally fabricated, welded steel construction, 219 cm W x 600 cm L, 4-wheeler, 2-axle, 750 x 20 tires with steel mesh wire sidings	15,000	9,700
Weighing Scale - Toledo, Model 2881FC, dial type, 1300 kgs. capacity, 76 cm x 76 cm platform, Ser. NO. 288105067	81,800	72,000
48 - Platform Balancers - Century Scale, Model DB5H, beam type 500 kg. capacity, 50 cm W x 74 cm platform	273,600	191,500
3 - Platform Balancers - Fairbanks, Model 41-13132, beam type, 500 kgs. capacity, 47 cm W x 70 cm platform (Note: Units not in use - out of order)	19,500	6,600

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>		<u>Sound Value</u>	
3 - Portable Weighing Scales - Nutex, dial type, 10 kgs. capacity	P	1,050	P	630
2 - Portable Weighing Scales - THIC, dial type, 10 kgs. capacity		700		420
Bench Grinder - Keng Feng, double arbor, 127 mm grinding wheels, driven by 190 watt electric motor, 3600 rpm, 220 volts		3,500		1,200
Portable Drill - Makita, 100 watts motor, 3600 rpm		800		480
Portable Drill - Black & Decker, 100 watts motor, 2000 rpm,		800		480
Air Compressor - Meiji Master, driven by 375 watt electric motor, 1720 rpm, 230 volts, complete with air receiver and stan- dard parts and accessories		9,000		5,400
Oxygen-Acetylene Welding Outfit - Anaka, complete with oxy-acetylene hoses, pressure gauges, regulators and welding torch nozzles		5,700		2,900
Air Compressor - Sui Yuan, driven by 190 watt electric motor, 1720 rpm, single phase, 220 volts, complete with air receiver and standard parts and accessories		7,000		3,500
Machinist Vise - Stationary type, 108 mm jaw		1,250		600

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
3 - Battery Chargers - Komatsu, Type K43, 48 VDC, 80 amperes charging rate	P 26,400	P 17,100
2 - Battery Chargers - Toyota, Type SG3, 48 VDC, 80 amperes charging rate, 6.4 kva	17,600	14,900
2 - Farm Tractors - International Harvester, Model 585, powered by 64 Hp, 4 cylinder IH diesel engine, Ser. Nos. B011505, B011506	804,000	788,000
2 - Forklifts - Komatsu, Model Fb15, 1400 kgs. capacity, fork type, 5000 mm max. fork height, 2-speed battery operated, 48 VDC motor, Ser. Nos. 11419 and 11420	478,000	334,000
2 - Electric Forklifts - Komatsu, Model FB15, 1400 kgs. capacity, clamp type, 5000 mm max. fork height, 2-speed, battery operated, 48 VDC motor, Ser. Nos. 11422 and 11421	496,000	330,000
2 - Electric Forklifts - Toyota, Model 4FB15, 1350 kgs. capacity, fork type, 5000 mm max. fork height, 2-speed, battery operated, 48 VDC motor, Ser. Nos. 10840 and 10830	478,000	318,000

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro-</u> <u>duction, New</u>	<u>Sound Value</u>
Electric Forklift - Toyota, Model 4FB15, 1350 kgs. capacity, 5000 mm max. lift height, clamp type, 2-speed, battery operated, 48 VDC motor, Ser. No. 10882	P 248,000	P 165,000
Hand Digital Tachometer - Simpo Model EE-1, battery operated, Ser. No. 10258301	3,500	2,100
Growler Tester - Crown Industrial Products, Co., USA, Catalog No. 2533, 230 volts, 50/60 cycles, Ser. No. 83023	2,400	1,400
Multi-Tester - Sanwa, Model JP-80, Ser. No. GF-1W10664	1,600	1,000
Megger Tester - Sanwa, Model DM501, 500 volts, 0-1000, mega-hertz, Ser. No. 3050084	2,400	1,800
Clamp Meter - Kyoritsu, Model 2103 AC 1159, 50/60 cycles, volt-ohm-ammeter	2,500	1,500
Megger Tester - Simpson, Model 260, volt-ohm- ammeter, Ser. No. 3-712397	2,400	1,400
Clamp Meter - Sanwa, Model CEM270D, No. 4F	2,500	1,500

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
3 - Air-Conditioners - Fedders, split packaged-type, 5 tons capacity, complete with standard parts and accessories (Note: One unit installed at PCG field office in Marbel)	P 195,000	P 129,000
2 - Air-Conditioners - Carrier, Model 38GF006-36, split packaged-type, 7.5 tons capacity, complete with standard parts and accessories, Ser. No. 056NP2-375 and 056NP2-376	170,000	136,000
3 - SSB HF Transceiver Radio - P.A. Electronics, 150 watts, single channel, 230 volts, single phase, complete with microphone and antenna (Note: 1-unit each at Marbel and Kidapawan field offices)	120,000	84,000
2 - Chain Hoists - Mechanical manual type, 3 tons capacity	12,400	7,400
Flowmeter - Steel construction, 40 mm diameter (Note: Spare Unit, brand new)	7,000	7,000
Pipe Vise - Size 78 mm	900	360
26 - Seed Cotton Moisture Testers - Delmshorst, Model CM-1, 0-20% moisture capacity, 9 VDC (Note: 21 units in Makati PCC		

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Repro- duction, New</u>	<u>Sound Value</u>
Office for calibration)	260,000	208,000
Sling Psychrometer -		
Bacharach - consisting of two thermometer 5°C-50°C and chart unit	P 2,300	P 1,700
4 - Irrigation Pumps -		
Kelly, Size 51 mm x 51 mm, driven by 4.5 hp Briggs & Stratton gasoline engine	43,600	26,200
2 - Irrigation Pumps -		
Planters, size 102 mm x 102 mm, driven by Yanmar diesel engine, Model TS105, 10.5 Hp	84,200	50,000
Irrigation Pump -		
Jaguar Pump, Size 51 mm x 51 mm, driven by 10.3 Hp Clinton gasoline engine	18,400	11,000
Irrigation Pump -		
Jackson Pump, Size 76 mm x 76 mm, driven by Briggs & Stratton gasoline engine	19,800	11,900
Sirene -		
Super Celerest, 115 AC decible, 220 volts, 203 phase, 500 mm audible radius, with standard motor drive	3,500	3,300
50 - Chemical Sprayers -		
Gloria, 10 liters tank capacity with centrifugal pump, driven by 2.2 kw air-cooled gasoline engine, complete with spray nozzle and back strap		

MACHINERY AND EQUIPMENT

<u>Description</u>	<u>Cost of Reproduction, New</u>	<u>Sound Value</u>
(Note: 44 units distributed to farmers, 6 units at PCC raw material warehouse)	P 540,000	P 485,000
4 - Impulse Sealers - Tew, Model T1SF-450, 71mm sealing width, 600 watts, 230 volts, single phase	16,000	9,600
3 - Fischbein Bag Closers - Model A, driven by 90 watt electric motor, 7500 rpm, Ser. Nos. 11346, 11320 and 11331	30,000	18,000
Siruba Bag Closer - Model Aa, driven by 90 watt electric motor, 7500 rpm, 200/240 volts, Ser. No. 7505363	<u>10,000</u>	<u>6,000</u>
	P 60,523,800	P 44,558,670

APPENDIX D

DRAFT BIDDING DOCUMENTS FOR PDC EQUIPMENT

The Committee on Privatization, Government of the Philippines, has approved the privatization of the Philippine Dairy Corporation (PDC). The physical assets of PDC will be offered at public auction by the Department of Agriculture. The disposal of the equipment will be carried out according to Commission on Audit Circular 86-264.

A list of PDC physical assets available for sale is contained in the attached Tender Document. The Tender Document is available from the Department of Agriculture, Office of the Secretary, Diliman, Quezon City.

The DA will appoint a Disposal Committee, which will:

- Receive from PDC
 - A program for disposal, with time schedule
 - Inventory report showing itemized list and complete description of all assets
 - Appraisal documents (refer to PDC Privatization Team Report)
- Inspect the assets to be disposed of and verify justification for disposal (refer to PDC Privatization Team Report)
- Establish the floor price for each asset item, considering the valuation contained in PDC Privatization Team Report, which has taken into account relevant factors including:
 - Market demand
 - Economic viability

- Physical condition, estimated economic value and depreciated value.
- Furnish the COA auditor at least 20 days prior to the advertisement for public bid with copies of:
 - The disposal program and schedule
 - Inventory report
 - Appraisal report
 - Disposal procedures

The tender will be advertised for not less than 3 consecutive days in a newspaper or newspapers of general circulation (Bulletin and Business Star?). (See attached advertisement form). Notice shall also be posted on Department of Agriculture bulletin boards.

The Disposal Committee will also constitute the Bids and Awards Committee, and shall:

- Invite all qualified bidders to be present at the bid opening.
- Open the bids in the presence of the bidders and of a COA representative at the designated time and place.
- If the first bidding fails, conduct a second bidding, following the procedures outlined above.
- Approve and issue the award to the winning bidder.

In order to accomplish these measures, the DA Disposal Committee has prepared the attached tender document to provide interested parties with all known and relevant information on the physical assets of PDC, to enable them to prepare offers for these physical assets.

All offers must be submitted in sealed envelopes to the Disposal Committee, Department of Agriculture and Food, before 4:00 p.m. on the date designated, which must be within four weeks of the date of this tender document.

Bidders must at time of tendering their bid post a bidder's bond in the amount of 10% of the bid amount. This bond will be returned in the case of all unsuccessful bids.

In this tender document, you will find the following:

- A list of equipment included in the offer, with appropriate specifications
- Statement of present location and current condition of equipment.

The equipment at Alabang, consisting of a milk processing plant; at Trece Martires, Cavite, consisting of a milk chilling plant; and at Lipa, Batangas, consisting of a milk chilling plant, are to be dismantled and moved from the present site at buyer's expense.

The milking parlor and chilling equipment located at Malaybalay Stock Farm, Bukidnon, is still in crates and is to be moved from the site at buyer's expense. The purchase of the milking parlor and chilling equipment will include installation and commissioning by the supplier, Danish Turnkey Dairy. There will be some additional cost to the buyer for installation, representing the increase in costs over the past three years since the original equipment purchase, involved in bringing a Danish expert to the Philippines to install the equipment.

Office and administration equipment will be sold as one lot.

Bidders may arrange to inspect the equipment by scheduling an appointment through the DA Disposal Committee, at the Office of Undersecretary of Agriculture Conrado C. Gozun.

The Disposal Committee reserves the right to refuse all offers and to re-advertise this tender.

Your bid should include the following:

- Price offer for each item of equipment for which an offer is being made.
- Complete identification of bidder including corporate affiliation, address and nature of business
- Bank reference
- Certified check in the amount of 10% of the offered price.

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DISPOSAL COMMITTEE
DEPARTMENT OF AGRICULTURE

PUBLIC TENDER
PHILIPPINE DAIRY CORPORATION EQUIPMENT

The Committee on Privatization, Government of the Philippines, has approved the privatization of the Philippine Dairy Corporation. A tender document has been prepared which can be obtained from the office of Undersecretary Conrado Gozun, Department of Agriculture, Diliman Avenue, Quezon City, Metro Manila. A charge of P _____ will be made for each copy of the tender document. All tender shall be addressed to the Disposal Committee, Department of Agriculture and should be received by the Disposal Committee on or before 4:00 p.m.

DRAFT NEWSPAPER ADVERTISEMENT

PUBLIC TENDER
DAIRY PRODUCTION AND PROCESSING EQUIPMENT

The Committee on Privatization, Government of the Philippines, has approved the privatization of the Philippine Dairy Corporation (PDC).

A tender document has been prepared which prescribes the conditions of tender for various items of PDC dairy production and processing equipment. The tender document can be obtained from the Office of Secretary, Department of Agriculture, Diliman Avenue, Quezon City. A charge of P_____ will be made for each copy of the tender document.

All tender should be addressed to the Disposal Committee, Department of Agriculture, Diliman Avenue, Quezon City and should be received by the Disposal Committee on or before 4:00 p.m. _____.

(List of equipment to be attached to tender document)

APPENDIX E

LIST OF PCC AND PDC PHYSICAL ASSETS
TO BE PRIVATIZED

<u>Summary</u>	<u>Replacement Value (P)*</u>
<u>Victoria, Tarlac</u>	
Land	525,648
<u>San Juan, Ilocos Sur</u>	
Land	579,954
Buildings	5,456,000
Land Improvements	626,000
Machinery and Equipment	24,173,300

TOTAL	30,835,254
<u>Solana, Cagayan</u>	
Land	302,900
Buildings	836,000
Land Improvements	516,000

TOTAL	1,898,318
<u>San Fabian, Pangasinan</u>	
Land	302,900
Buildings	11,771,000
Land Improvements	1,509,000
Machinery and Equipments	41,865,900
Vehicles	2,956,300

TOTAL	58,405,100
<u>Polomolok, South Cotabato</u>	
Land	2,862,576
Buildings	11,812,300
Land Improvements	1,276,900
Machinery and Equipment	60,523,800
Vehicles	3,079,000

TOTAL	79,554,576

* Estimated in appraisal report dated June 7, 1986.
Adjusted to reflect situation as of October, 1987.

NORTHERN LUZON

<u>LAND</u>			
LOCATION	NO. OF LOTS	AREA SQ. METER	APPRAISAL (VALUE P)
Victoria, Tarlac	4	150,185	525,648
		(15.0185 ha.)	
(Four contiguous lots-owned)			
B. Labnig, San Juan Ilocos Sur	2c	165,701 (16.5701 ha.)	579,954
Solana, Cagayan	2c	91,053 (9.10 ha.)	546,318
Bo. Alacan, San Fabian Pangasinan	4c	46,600 (4.66 ha.)	302,900
Polomolok, So. Cotabato	3c	238,548 (238.548 ha.)	2,862,576

IMPROVEMENTS

LOCATION	REPLACEMENT COST (P)
Bo. Labnig, San Juan Ilocos Sur	626,000
Solana, Cagayan	516,000
San Fabian, Pangasinan	1,509,000
Polomok, So. Cotabato	1,276,900

BUILDINGS

LOCATION	TYPE	SQ.M.	REPLACEMENT COST (P)
San Juan, Ilocos Sur	Admin. Bldg.	388	658,000
	Ginnery	574	1,027,000
	Warehouse	3,144	3,408,000
	Exp. Station	148	183,000
	Car Shed	77	38,000
	Guardhouse	29	86,000
	Scale House	13	56,000
Solana, Cagayan	Admin. Bldg.	384	727,000
	Car Shed	75	59,000
	Guardhouse	22	50,000
San Fabian, Pangasinan	Admin. Bldg.	1,029	1,745,000
	Ginnery	715	1,279,000
	Warehouse (3)	5,572	6,190,000
	Canteen	92	135,000
	Greenhouse	77	95,000
	Generator Rm.	8	7,000
	Stockroom	59	66,000
	Scalehouse	14	56,000
	Guardhouse	15	55,000
	Garage	26	27,000
	Satellite Warehouse* (7)	263	2,116,000
Polomolok, South Cotabato	Admin. Bldg.	545	1,550,800
	Ginnery	577	1,023,000
	Warehouse	2,880	8,777,200
	Powerhouse	43	115,700
	Maintenance Shed	126	47,700
	Scale House	14	37,300
	Greenhouse (2)	19.5	55,000
	Shed	6	2,500
	Cue Sheds (3)	90	15,700
	Farmer's Cottage	40	7,400

MAJOR EQUIPMENT

LOCATION	ITEM	REPLACEMENT COST (P)
San Juan, Ilocos Sur	Suction System (2)	254,500
	Unloading Separator	532,200
	Conveyor Distributor	400,000
	Ginstand (2)	3,776,000
	Seed and Hull Conveyor	487,100
	Inclined Lint Cleaner	1,754,600
	Outfit Battery Condenser	1,065,500
	Seed Cotton Drier	1,690,000
	Thrash & Lint Fly Exhaust System	946,100
	Air Blast Fan	558,000
	Press System	9,200,000
	Misc.	3,405,400
	Laboratory Equip.	84,500
	San Fabian, Pinan Pangasinan	Suction System	254,500
Unloading Separator		532,200
Conveyor Distributor		566,600
Seed Cotton Feeders (2)		2,023,600
Gin Stand		2,360,000
Seed and Hull Conveyor		487,100
Waste Conveyor		335,000
Inclined Lint Cleaner		1,754,600
Lint Cleaner System		2,090,800
Outfit Battery Condenser		896,000
Seed Cotton Drier		1,767,000
Thrash and Lint Fly Exhaust System		967,100
Press System		9,200,000
Misc.		4,927,900
Lab. Equip., Chemical Sprayer		41,865,900
Vehicles		2,956,300
Toyota Tamaraw (10)		1,230,000
Toyota Hi-Lux (1)		165,000
Mercedes Jeep (1)		581,300
Suzuki Jeep (4)		5,760,000
Ford Fierra (1)	140,000	

Polomolok, So. Cotabato

Suction System (2)	1,476,300
Vacuum Wheels (2)	328,600
Unloading Separator	1,539,000
Inclined Lint Cleaner	1,754,600
Conveyor Distributor	717,200
Ginning System (2)	7,616,000
Seed Hull Conveyor	540,100
Seed Blower	213,000
Overflow System	1,164,300
Lint Cleaner (2)	4,312,000
Elevator Trash Fans (3)	763,700
Misc.	3,809,100
Press System	9,343,000
Hydraulic Cotton System	1,202,000
Cotton Module Builder (2)	2,935,000
Cotton ginning system (not operable, cannabalized)	9,140,000
Double Roller Gin	79,100
Diesel Generator Set	2,636,000
Electrical Dist. System	1,466,000
Fuel & Water tanks	2,220,000
Water distribution System	228,000
Truck Scale	1,150,000
Module Cotton Trailers (3)	1,320,000
Seedcotton Pallets, Trailer	719,000
Weighing Scales, Etc.	376,650
Machine Shop Items	448,700
Vehicles	
Farm Tractors (2)	804,000
Fork lifts (7)	2,148,700
Suzuki Van (1)	210,000
Suzuki Jeep (4)	840,000
Toyota Landcruiser (1)	230,000
Toyota Tamaraw (7)	1,220,000
Toyota Minicruiser (1)	210,000
Colt Galant (1)	275,000
Toyota Hi-Lux (1)	70,000

PDC ASSETS

Milk Processing Plant (Purch. Dec. 7, 1984)

<u>Qty.</u>	<u>Description</u>	<u>DKK Price</u>	<u>Totals</u>
1	Milk Weighing Scales	37,550	
1	Dump Tank	15,830	
1	In-Line Strainer	1,190	
1	Milk Pump	7,160	
1	Plate Heat Exchanger	24,490	
1	Refrigerated Vat	47,538	
1	Milk Pump	7,160	
1	Cream Separator	17,375	

1 Balance Tank	7,086
1 Milk Pump	7,160
1 Hand Regulating Valve	2,315
1 Plate Pasteurizer and Control Equipment	76,568
1 Air Compressor	12,490
1 Hot Water Set	38,630
1 Hot Water Pump	2,340
1 Chilled Water Unit	170,772
1 Insulated Milk Storage	49,848
1 Sachet Filler	32,175
4 Cheese Vats with Agitators	220,690
1 Hot Water System	18,042
1 Cheese Making Utensils	6,945
1 Starter Preparation Equipment	22,400
1 Platform Scale	12,224
1 Al Milk Can	3,253
1 Boiling Vessel	9,125
1 Insulated Water Bath	16,125
1 Chilled Water Pump	1,770
1 Butter Churn	7,400
1 Buttermilk Drain with Hose	500
1 Buttermaking Utensil	18,490
1 Flat Topped Trolley	5,180
2 Cold Store	156,450
1 Shelving	12,940
1 Cabinet Freezer	2,550
1 Washing Tub	4,875
1 Set Stainless Steel Pipes, Valves, Etc.	54,300
1 Set Service Pipe, etc.	21,450
Electrical Installation	390,000
1 Set Laboratory Equipment	144,024
Installation, Running-In and Training	0

Sub-Total	1,686,410
Freight & Ins.	216,590

Total	1,903,000
	=====

PDC ASSETS

Milk Processing Plant (Purch. Dec. 7, 1984)

<u>Qty.</u>	<u>Description</u>	DKK <u>Price</u>	<u>Totals</u>
	Milk Weighing Scale	4,038	
	Milk Pumps	3,210	
	Plate Cooler	2,680	
	Refrigerated Vat	3,299	
	Cream Separator	1,246	
	Plate Pasteurizer and Panel	1,800	
	Spare Parts	4,170	
	Air Compressor	949	
	Hot Water Set and Pumps	7,280	
	Chilled Water Unit	6,931	

Sachet Filler	2,860
Platform Scale	3,233
Chilled Water Pump	630
Cold Stores	7,934
Electrical Installation	0

Sub-Total	50,259
Freight (Est.)	5,627

Total	55,886
Homogenizer, Capacity 700 Litres	167,010

Sub-Total	167,010
Freight & Ins.	62,000

Total	229,010
Grand Total, Milk Processing Plant	2,187,896
Trended Up by 20%	2,625,475
Peso conversion Factor	3.25
Replacement Cost in Pesos	8,532,795
	0.35

Estimated Value in Exchange	2,986,478
	=====

PDC ASSETS

Two Milk Chilling Centers (Purch. Dec. 7, 1984)

<u>Qty.</u>	<u>Description</u>	<u>DKK</u> <u>Price</u>	<u>Totals</u>
2	Milk Weighing Scale	75,100	
2	Pump Tank	31,660	
2	In-Line Trap Strainer	2,380	
2	Milk Pump	14,320	
2	Plate Heat Exchanger	58,700	
2	Ice Bank Unit	623,180	
6	Refrigerated Vats	239,450	
2	Milk Pumps	19,880	
2	Hot Water Storage Cylinder	5,100	
2	Washing Tub	9,750	
2	Stainles Steel Pipes, Valves, etc.	28,580	
2	Service Piping	57,160	
2	Diesel Generator	131,120	
2	Electrical Installation	225,000	
2	Laboratory Equipment	97,640	
2	Transport Milk Tank	145,240	
	Installation, Start-Up and Tech. Advice	0	

	Sub-Total		1,764,260
	Freight (Est.)		30,000

	Total		1,794,260
	Milk Weighing Scale	8,076	
	Milk Pumps	3,360	
	Plate Cooler	5,230	
	Ice Bank Plant	15,342	
	Refrigerated Vats	19,794	
	Diesel Generator	11,940	
	Electrical Installation	0	

	Sub-Total		63,742
	Freight (Est.)		7,361

	Total		71,103
	Grand Total, Two Milk Chilling Centers		1,865,363
	Trended Up by 20%		2,238,436
	Peso conversion Factor		3.25
	Replacement Cost in Pesos		7,274,916
			0.35

	Estimated Value in Exchange		2,546,220
	Value for Each Center		1,273,110
			=====

PDC ASSETS

Bukidnon Milking Equipment (Purch. May 21, 1985)

<u>Qty.</u>	<u>Description</u>	\$ Sing. <u>Price</u>	<u>Totals</u>
2	Vacuum Pump and Electric Motor	1,606	
1	Vacuum Tank and Vacuum Line	2,605	
2	Vacuum Regulator	105	
2	Vacuum Gauge	35	
30	Pulsator	2,235	
2	Pulsator Controller	1,350	
24	Milk Claws	1,895	
120	Rubber Milk Claws Inflation	1,840	
1	Set Misc. Equipment	9,747	
24	Milking Claw Holder	1,326	
6	Water Nozzle and Water Line	257	
2	Glass Tank Receiver	1,158	
2	Milk Transform Pump	1,005	
1	2 x 12 Herringbone Galv. System	5,389	
1	2 x 12 Feed Managers	12,395	
1	Equipment System for Cleaning Installation, Startup, and Training	1,700 23,350	
1	SAC Maintenance Tools	3,720	
	F.O.B. Cost	532	

	Sub-Total		72,250
	Freight & Ins.		8,289

	Total		80,539
1	Milk Receiving Vat	2,937	
1	Plate Heat Exchanger	24,646	
2	Self-Refrigerated Milk Tank	43,111	
2	Milk Delivery Pump	3,847	
1	Hot Water System	3,800	
1	Washing Vat	1,129	
1	Milk Can Steamer	2,262	
1	Trolley for Pipe Fittings and Pipe	1,200	
2	Pipe Spanner	47	
24	Assorted Hand Brushes, Nylon	176	
24	Pipe Brushes	183	
2	Detergent for In-Place-Cleaning	158	
1	Laboratory Equipment Installation, Start-Up, and Training	10,130 12,200	
24	Cleaning Brushes	48	

	Sub-Total		105,874
	F.O.B. Cost		1,514
	Freight & Ins.		19,910

	Total		127,298

PDC ASSETS

Bukidnon Milk Processing Equipment (Purch. May 21, 1985)

<u>Qty.</u>	<u>Description</u>	\$ Sing. <u>Price</u>	<u>Totals</u>
I	Supply and Installation of Herringbone Milking Parlor	80,539	
II	Supply and Installation of Milk Chilling and Holding Equipment	127,298	
III	Spare Parts for Item II	5,076	

	Sub-Total		212,913
	Grand Total in Singapore Dollars		420,750
	Trended Up by 20%		504,900
	Peso conversion Factor		10.15
	Replacement Cost in Pesos		5,124,735
			0.35

	Estimated Value in Exchange		1,793,657
			=====

NICHOLAS C. ARMSTRONG, ARICS, ASVA

Mr. Armstrong is a specialist in the valuation of tangible assets. In the course of his work he has valued a diversified range of process plants, machinery, equipment, and fixtures. He has extensive experience in the use of computer models to value large groups of assets. He has prepared studies for use in acquisitions, divestitures, financing, insurance, leasing, receiverships, and condemnation purposes.

His real estate appraisal assignments have included studies to determine market value, leasehold interest value, and highest and best use. He has also conducted feasibility studies and reuse appraisals for property development. Real property appraised includes large manufacturing plants, distribution warehouses, shopping centers, small retail properties, office buildings, and undeveloped land. Special purpose appraisals have included valuation of churches and determination of market value of easements.

PREVIOUS EXPERIENCE

Before co-founding Armstrong & Ryan, Mr. Armstrong was a manager at Arthur D. Little Valuation, Inc. He has also held positions as project manager and appraiser at two large British valuation firms, Edward Rushton Son and Kenyon and Weatherall, Green & Smith.

EDUCATION

B.S., Valuation and Estate Management, Bristol Polytechnic

PROFESSIONAL AFFILIATIONS

The Royal Institution of Chartered Surveyors

The Incorporated Society of Valuers and Auctioneers

REPRESENTATIVE CLIENTS

Allergan Medical Optics
Amalgamated Dental
AT&T
ARCO Metals
Arthur Cox
Associated Newspapers
Australis & New Zealand
Bank
Beacon Oil Company
Beatrice Foods
Boosey & Hawkes
Borden Chemicals
City of Buena Park
CALTRANS
Cape Asbestos
Chartered Medical
The Chemical Society

Chloride Industries
Coca Cola Bottling
Company
The Commonwealth
Secretariat
Denny's Inc.
First Interstate Bank
Florida National Banks
General Motors
Corporation
Greyhound, Inc.
Ernest W. Hahn, Inc.
Hanson & Olson
High Duty Alloys
City of Inglewood
IBM Corporation
IRECO

The Irvine Company
Kellog & Company
Lotus Cars
Lunday Thagard
Marshall Friedman
Midland Oil & Chemical
City of Montebello
NTRON Inc.
Oasis Petroleum
Pacific Airmotive Corp.
Pearson Longman
Management
Group
Prosser Pump
Purex Industries
Rank Industries
Royal Doulton Group
Royal Worcester
Schnitzer Steel Company
Security Pacific Bank
Shasta Beverages
Solo Cup Corp.
Solatron
Sunrise Medical
Swan Hunter/British
Shipbuilders
Taco Bell Restaurants
Tenneco
Transamerica Corporation
Tube Investments
Santa Anita Park Race
Track
United Glass
Waste Management Corp.

COMMITTEE ON PRIVATIZATION

GUIDELINES FOR PRIVATIZATION OF GOVERNMENT CORPORATIONS

I. INTRODUCTION

1. It is the declared policy of the government, pursuant to Proclamation No. 50, to give primacy to the private sector in undertaking economic activities under a climate of fair competition. Accordingly, the government shall undertake a systematic, orderly and time-bound program that seeks to transfer to private ownership assets and activities which have been identified as no longer necessary or appropriate under government ownership or control.

2. These guidelines shall apply to government corporations, whether created under special charter or organized under the Corporation Code, in which the government has majority ownership or management control. Government assets assigned to the Asset Privatization Trust (APT) for disposition shall be covered by a separate set of guidelines.

II. IDENTIFICATION OF CORPORATIONS FOR PRIVATIZATION

3. The Committee on Privatization (COP), pursuant to the authority vested in it by Proclamation No. 50, shall identify to the President government corporations for privatization. The recommendations of the Presidential Commission on Government Reorganization with respect to the disposition of government corporations shall be reviewed by the COP and shall constitute the initial basis for the identification of government corporations for privatization. Corporations which in the judgement of the COP should be transferred to private ownership shall then be endorsed to the President for privatization.

4. The approval by the President of a recommendation to privatize a corporation shall constitute the COP's sanction to monitor, oversee and implement its privatization. In the exercise of this authority, the COP shall designate a disposition entity which shall assume the primary responsibility for developing and executing, subject to these guidelines, the plan of privatization for each corporation so identified. The designation of disposition entities shall be contained in an appropriate document from the COP.

assets. Outright sale of assets shall be preferred to leases, especially those extending beyond one year. Leases shall be subject to prior approval by the COP.

8. In formulating privatization plans the disposition entity shall give due consideration to the potential impact of privatization on employment and job security of the affected employees.

9. The disposition entity shall submit its privatization plan for approval by the COP. If the COP fails to act on the plan within 30 days from submission of all relevant information, the same shall be deemed approved. The format attached as Annex A is intended as a guide in the preparation and submission of individual privatization plans.

10. The disposition entity shall submit periodic reports on the progress of the privatization program. If in the judgement of the COP the disposition entity has not achieved satisfactory progress, and if the outlook indicates that privatization plan would not be accomplished in the manner and within the time frame agreed upon, the COP may after written notice assign the privatization of the corporation concerned to another disposition entity.

11. Where the COP has designated a disposition entity other than the APT, the COP may nevertheless delegate to the APT the task of monitoring and coordinating the disposition activities of those other entities.

12. The COP shall assist disposition entities in accessing technical assistance as appropriate to aid in the formulation and implementation of privatization programs, including the preparation of valuation studies and detailed information memoranda, identification of potential investors, possible restructuring arrangements, etc.

IV. VALUATION

13. Generally accepted valuation approaches shall be used in order to establish a range of values for a particular asset or corporation, including appraised value, replacement cost, discounted cash flows, market valuation and other such methods. The valuation methodology should be suited to the characteristics of the enterprise being sold.

5. The COP may designate parent corporations or supervising departments as disposition entities if in the judgement of the COP these organizations manifest the requisite commitment and capability to undertake in an effective and expeditious manner the privatization of government corporations assigned to them. If, on the other hand, the COP believes a separate organization would be in a better position to formulate and implement the privatization of a particular corporation, a separate disposition entity such as the APT may be so designated.

6. Government corporations may on their own initiative carry out their privatization without the need for prior identification and approval as indicated above. However, matters pertaining to price, buyer and terms of disposition shall be subject to approval by the COP.

III. PREPARATION OF PRIVATIZATION PLANS

7. Disposition entities shall within 60 days from the date of their designation prepare detailed privatization plans in behalf of corporations assigned to them in accordance with the modalities of privatization as may be determined by the COP, indicating specific timetables for the accomplishment of key tasks. Such modalities may include the following elements:

a. Extent of privatization. Divestiture may be partial or total. As a rule the government shall aim for total privatization of the corporations concerned, except in cases where strategic reasons or other special circumstances warrant partial i.e. minority, government ownership on a transitory or indefinite basis. In such instances, partial privatization may be allowed.

b. Timing. The COP shall advise the disposition entity concerned the time frame within which privatization should be accomplished. Corporations belonging to the "first stage" group, i.e., those which can be privatized immediately, shall be required to prepare plans which would provide for actual sale within the next twelve months. Corporations belonging to the "second stage" group are generally those which cannot be privatized immediately due to some legal, financial or organizational impediment. Their sale may be deferred until these issues are resolved.

c. Modes of privatization. The COP shall specify if the privatization of a particular corporation will involve the sale of shares of stock or the sale of assets. Corporations to be privatized as going concerns shall be sold in the form of shares. Privatization may also be in the form of asset sale in cases where a government corporation sells all or substantially all of its tangible

14. Disposition entities may engage the services of financial advisors, appraisal companies, valuation specialists and other generally recognized specialized entities in carrying out valuation studies. In some cases involving corporations to be sold as going concerns, disposition entities may undertake the valuation if they can demonstrate that the valuation basis employed provides a reasonable and fair estimate of the value of the enterprise.

V. IDENTIFICATION OF POTENTIAL INVESTORS

15. All things being equal, and in accordance with existing laws, preference shall be given to Filipino investors.

16. To the extent possible, privatization plans should consider the feasibility of public sale of shares and employee stock ownership plans in order to widen the ownership base of enterprises.

17. Sale to investors which would result in undue concentration of economic power in the hands of a few groups or individuals shall be discouraged.

18. Where deemed appropriate to protect the continuing operations and financial well-being of the corporations to be sold, the COP may require disposition entities to provide reasonable and sufficient information concerning the financial, managerial, technical and other qualifications of prospective buyers.

VI. DISPOSITION METHODS

19. In the privatization of government corporations, first preference should be for public offering and listing of the shares. If this is not feasible, sale of corporations should be done through sealed bids. Negotiated sale may be allowed as a third option only if bidding should prove to be unsatisfactory, impractical or inappropriate under the individual circumstances. If disposition is to be done through negotiations, the matter should be given as much publicity as possible in order to give all qualified potential investors the opportunity to participate in the proposed sale. In these cases the disposition entity should conduct simultaneous negotiations with all interested parties so that all serious offers may be considered before a final recommendation is made.

20. Cash offers shall be given preference. If sale is to be made on installment basis, the unconditional guarantee of an acceptable financial institution must be secured. For this purpose, the guarantee of government financial institutions shall not be acceptable, since the financial exposure remains with the government.

VII. REHABILITATION, RESTRUCTURING AND OTHER ACTIONS PRIOR TO SALE

21. The government discourages expenditure of funds for the rehabilitation of corporations to be privatized. In exceptional cases, however, rehabilitation may be considered if an asset or company is adjudged to be marketable but rehabilitation is required for (a) physical conservation of assets where shutdown or mothball costs may approximate costs of actual operations; or (b) preservation of factor inputs such as technical skills or maintenance of necessary contractual relations such as franchises, supply contracts, and other commitments.

22. Financial restructuring may be allowed if it can be demonstrated that balance sheet restructuring, conversion of some debt into equity, refunding of existing debt or similar action would enhance the value and the marketability of the firm.

23. Disposition entities shall report to the COP legal and other impediments to privatization of selected corporations, and shall describe measures being taken to resolve the same.

VIII. ROLE OF THE COMMITTEE ON PRIVATIZATION

24. As specified under Proclamation No. 50, the COP shall be the principal entity authorized to monitor the privatization of government assets. As such, it has the authority to supervise privatization activities approved by the President. The COP shall review and pass upon privatization plans, designate disposition entities for each corporation to be privatized, require disposition entities to make periodic reports on the progress of their privatization efforts, and approve all individual dispositions. The COP shall report to the President and to Congress the progress of the overall privatization program.

25. The price, buyer, terms of disposition, such as sale or lease, rehabilitation or restructuring of corporations are subject to the prior approval of the COP, which shall be the final approving authority on such matters without need for further action by any other government authority.

final approving authority on such matters without need for further action by any other government authority.

26. The COP shall act expeditiously on all matters submitted to it for decision. Disposition recommendations not acted upon after 30 days from submission of all required information and documents shall be considered approved.

APPROVED BY THE COMMITTEE ON PRIVATIZATION (COP) AT ITS
MEETING OF 12 AUGUST 1987

ANNEX A

PRIVATIZATION PLAN

To be accomplished by disposition entities for each corporation assigned to them. Indicate full name of the corporation and date accomplished.

I. BACKGROUND INFORMATION

1. Date Established/Incorporated - Use date of registration with the SEC or date of Special Law creating the corporation.
2. Basis of Establishment - If created under general corporation law indicate SEC registration number; if chartered by special law, indicate number of Presidential Decree, Letter of Instruction, Executive Order, Commonwealth Act and/or Republic Act, whichever is applicable. Indicate amendments to original acts.
3. Sector/Industry - Indicate whether in Agriculture, Industry or Services sector; indicate also the particular industry the corporation is in. In cases where the corporation is engaged in various activities and therefore can be classified under more than one sector or industry, consider its main activity in determining sector / industry classification.
4. Shareholders - Identify which government agency and/or GOCC own shares of stocks of the corporation and extent of holdings. In cases where there is private sector participation in the company, identify individual or institutional partners

and extent of holdings of each.

5. Department Attachment

- Indicate which Department / Office supervises the corporation.

6. Parent Company

- This refers to another GOCC which owns the majority of the corporation's shares of stock; in cases where more than one GOCC own shares in the corporation, and each has less than 50%, the parent company is the one that holds the largest share and thus owns controlling interests in the corporation.

7. Financial Highlights

- As much as possible use only audited financial statements; for the interim period of 1987, in-house financial statements may be used. Indicate the source of financial data, identifying the auditor involved where audited statements have been utilized.

II. FACTORS TO CONSIDER

- Special situations or factors that may affect the privatization of the corporation in any way should be enumerated in this section.

In general, these factors would call for special steps that would need to be taken and which would be identified in Section III.7 below.

III. PRIVATIZATION PLAN

1. Extent of Privatization

- Indicate whether government divestiture is total or partial; if partial, indicate extent or percentage of divestiture.

HYPOTHETICAL MODEL

PRIVATIZATION PLAN

COMPANY: XYZ Inc.

Date Prepared: 31 August 1987

I. BACKGROUND INFORMATION

1. DATE ESTABLISHED/INCORPORATED - 3 March 1984
2. BASIS OF ESTABLISHMENT - PD 12345 as amended by PD 67890
3. SECTOR/INDUSTRY - Agriculture Sector
Trading of Agricultural
Commodities
4. SHAREHOLDERS:
 - GOVERNMENT - National Government-100%
 - PRIVATE - None
5. DEPARTMENT ATTACHMENT - Department of Trade and Industry
6. PARENT COMPANY - None
7. FINANCIAL HIGHLIGHTS:

	31 DEC. 1986	30 JUNE 1987
TOTAL ASSETS	P230,000,000	P245,000,000
FIXED ASSETS	180,000,000	180,000,000
TOTAL LIABILITIES	150,000,000	160,000,000
NET WORTH	80,000,000	85,000,000
GROSS REVENUES	135,000,000	86,800,000
NET INCOME	70,600,000	40,300,000
BASIS:	AUDIT OF COMMISSION ON AUDIT	IN-HOUSE STATEMENTS

II. FACTORS TO CONSIDER

1. The company is a non-stock corporation. It has to be converted to a stock corporation

2. Mode of Privatization - Indicate whether privatization will involve the sale of the corporation as a going concern or the sale of its assets.
3. Method of Privatization - Privatization may take the form of either public offering of shares of stock of the corporation, sealed bidding (of shares or assets) or negotiated sale (of shares or assets). Privatization may also involve a combination of any of the three mentioned possibilities.
4. Potential Investor Group - Identify the potential investor groups - i.e. the general public, employees of the corporation, local companies (indicate qualification desired / required); foreign companies (indicate qualification desired/required); do not name specific investor or company.
5. Valuation - Indicate the method to be used in appraising the company and/or its assets - i.e. replacement cost, discounted cash flows, sound value, earnings potential, etc. Identify the type of entity that will carry out the valuation - i.e. appraisal company, accounting firm, investment bank, etc. ; do not give name of specific valuation entity.
6. Timing of Privatization - Indicate the month and year when divestiture is expected to be carried out.
7. Program of Activities - List down all the steps to be undertaken by the disposition entity and/or corporation before the eventual privatization is

effected. Due to the possible existence of situations peculiar to individual corporations, steps identified in the hypothetical model may not apply to the subject corporation.

Identify all critical activities that may need to be undertaken. Where, for example, litigation exists due to questions on ownership of shares in the company or assets, a critical step may be the prior resolution of this issue. Or where the transfer of ownership over land where company facilities stand may enhance the value of the company, such a step should be indicated.

- 2. The company has an outstanding long-term loan of \$2 million from the Asian Development Bank. Consent of the Bank for the privatization of the company has to be obtained beforehand.

III. PRIVATIZATION PLAN

- 1. EXTENT OF PRIVATIZATION - 100% (70% by March 1988; 100% by June 1988)
- 2. MODE OF PRIVATIZATION - Sale of the company as a going concern/sale of shares of stock of the company
- 3. METHOD OF PRIVATIZATION -
 - 1. Public Offering of 70% of shares of stock
 - 2. Bidding through sealed bids for 30% of shares of stock
- 4. POTENTIAL INVESTOR GROUPS -
 - 1. General public - 70% of shares of stock
 - 2. Local companies (must have experience in trading of agricultural commodities) - minimum of 20% of shares of stock
 - 3. Foreign companies (must have experience in trading of agricultural commodities) - maximum of 10% of shares of stock
- 5. VALUATION:
 - VALUATION METHOD -
 - 1. Shares for Offering to the General Public (70%) - Estimated Price/Earnings Ratio
 - 2. Shares for Sealed Bidding (30%) - Discounted Earnings Approach

VALUATION ENTITY

1. Shares for offering to the General Public
Investment Bank/ Financial Advisors
2. Shares for Sealed Bidding-
Accounting Firm

6. TIMING OF PRIVATIZATION

1. Public offering
March 1988
2. Sealed Bids
June 1988

7. PROGRAM OF ACTIVITIES
(COMPLETION DATES)

1. Notice to ADB re plan to privatize the company
September 1987
2. Registration with the Securities and Exchange Commission - October 1987
3. Appraisal of company and assets - October 1987
4. Hiring of Investment Counsellor - October 1987
5. Preparation of Prospectus
December 1987
6. Application with the Makati Stock Exchange
January 1988

CERTIFIED BY :

Authorized Signature

Designation

Date

RECEIVED BY:

COP Authorized Signature

Date

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INTRODUCTION

Armstrong & Ryan has been engaged to estimate the fair market value of certain fixed assets of Philippine Cotton Corporation, located at San Juan, Ilocos Sur in Northern Luzon and at Polomolok, South Cotabato in Southern Mindanao. These fixed assets form the production plant of two independent cotton ginning facilities. The cost of dismantling the equipment has also been estimated for each plant. The purpose of the appraisal is to help establish a suitable privatization policy.

NATURE OF THE BUSINESS

Essentially, the cotton gin removes seeds from harvested cotton to procure lint cotton. The cotton gin contains rows of saw-toothed bands which separate the cotton fiber from the seed. The seed falls into a conveyor and the lint, on the saw-tooth, is blasted by air and blown or brushed into a lint cotton conveyor. Cotton fiber is then pressed into rectangular bales and tied with wire.

Important considerations when assessing a ginning operation are the age of the plant, production capacity in terms of bales per hour, and hand picked or mechanically picked raw material supply.

VALUE TERMINOLOGY

Fair market value is defined as follows:

The fair market value is the amount expressed in terms of money that may reasonably be expected to exchange between a willing buyer and a willing seller with equity to both, neither under

any compulsion to buy or sell, and both fully aware of all relevant facts, as of a certain date.¹

VALUE AND COST ANALYSIS

The San Juan facility is largely equipped with Lummus cotton ginning machinery and appears to be a two stand ginning operation with an estimated capacity of 5 - 6 bales per hour. Lummus Industries, Inc. of Columbus, Georgia, is one of the most prominent manufacturers of textile machinery. It is estimated that the plant was in fact relocated to its present site in 1983 and was probably modified during this period. Cotton appears to be harvested by hand.

A copy of an appraisal of the San Juan facility by Cuervo Appraiser's, Inc. is shown in appendix B. Major items of equipment are now summarized in the order they appear on the Cuervo appraisal. Important facts and dismantling considerations are outlined for each item.

Suction Telescopes: Suction telescopes remove the harvested cotton from the delivery trailers and discharge it directly into the process system. These are bulky items and difficult to dismantle. There is a significant amount of structural steel and component parts fabricated on site. Ducting and component sizes are often peculiar to the building and to the process design and layout. In essence, it would be easier to build new suction scopes at the new location but, in the event of a sale, a typical buyer would no doubt prefer to salvage as much as was physically possible.

Unloading Separator: A substantial amount of site fabrication is involved in installation. If sold and dismantled, much of this

ASA Standard definition, American Society of Appraisers
Board of Governors, 1984.

fabrication work would have to be repeated at the new location. Once again there is some debate as to the feasibility of dismantling but since labor is available and reasonably priced, the unloading separator would be salvaged.

Conveyor Distributor, 2 Gin Stands, Seed and Hull Conveyor: The two gins are manufactured by Lummus and are a model Thermex, 90 saw blade air blast type. Lummus informs me that this particular model has not been manufactured for fifteen years. Changes in design and size have rendered this model obsolete.

For instance, the air blast has been replaced with a brush system and capacities increased. As part of the process system, the conveyor distributor and the seed and hull conveyor are designed specifically for this type of gin and do not have sufficient capacity to serve other models. Again, there is a built-in obsolescence because opening widths and center dimensions have generally increased in size. Lummus indicates that the gins can not be upgraded and that replacement parts may be unavailable. Finally, it is important to realize that these machines form a unit. If the gins were sold separately, it might prove difficult to dispose of the remainder. No major problems are anticipated in disassembly of the major component parts.

Inclined Lint Cleaner: Separates trash from the cotton lint. An important item of equipment, easily removable.

Battery Condenser: A 40" model, highly suitable for a two stand ginning operation. Forms cotton into a blanket and simple to remove.

Seed Cotton Drier: The burner appears old but has the correct 3 million B.T.U. rating. The push and pull fans are current models and were probably updated at the time of relocation. All the main components would be removed, including the Tower Drier, but some ducting would be lost in the dismantling process.

Trash and Lint Exhaust: A similar situation to the seed cotton drier.

Air Blast Fan: A current model, manufactured by Lummus which would be removed:

Press System: This is probably a flat bale press. The flat bale press has been superseded by a high density model. In the U.S., it can still be seen in textile mills and is often used as a waste press. However, its continued use as the cotton gin's primary baler limits the potential of the end product. With the flat bale press, the density of the cotton bale depends upon the experience of the machine operator, making the weight of one bale different from the next. This lack of standardization will suppress the price the cotton may bring on the world market. A lower price represents the necessary cost of reprocessing the cotton bale at a later date, by high density press, which automatically sets the density and thus the weight. A buyer of the ginning equipment has the option of purchasing a high density "dorles" press for the new location and retaining the flat bale press for impure cotton. Obsolescence will depress the price that can be expected from a serious use for this type of flat bale press.

Miscellaneous Items: The elevated water storage tank would appear unworthy of dismantling for relocation as part of the process plant. Fabrication of a new tank might be a cheaper alternative to relocation. If the ginning plant was sold as a complete package, the purchaser might sell the tank to a local user. There is always a local need for this type of service plant.

Cost of Dismantling and Container Packing

In accordance with instructions, I have endeavoured to estimate a likely cost for disassembly and container packing. Conversations

with various people in the industry suggest that equipment dismantling might take two months and require an engineer plus a local crew. If a Lummus engineer is employed, a charge of \$6,500 per month will be incurred plus all expenses and living accommodation. In addition to the cost of the crew, special tooling including cranes, forklifts and hoists must be supplied and this cost has been estimated at \$8,000 - \$12,000.

The cost of packing freight containers for shipping, excluding any overseas freight charge, is estimated by Lummus at 1% of equipment cost new. This would equate to approximately \$15,000 but may be lower in the Philippines.

The total cost of dismantling a similar U.S. located cotton ginning plant, and packing the freight containers for shipping, would be approximately \$75,000 - \$115,000, excluding land freight. The cost for dismantling and packaging a Philippine ginning facility will be lower. However, if a professional engineer from Lummus is employed for an assumed two month disassembly period, the engineer's costs plus certain specialist equipment costs will together equate to approximately 25% of the total cost in U.S. terms.

Cost of Relocation and Installation

The cost of relocation and installation is a relevant consideration in determining value in exchange. Although this expenditure is borne by the buyer, it forms a large part of his total costs of purchase. It is partly instrumental in dictating the amount that can be paid for a plant. For information, relocation is a costly exercise. Shipping costs are difficult to ascertain, but Lummus indicated that the freight charge from U.S. to Africa could be in the region of \$100,000. Depending upon the destination, costs might be less for a plant shipped from the Philippines.

Installation of the relocated production plant would likely require an engineer and a local crew for a period of six months. If a Lummus engineer is employed, a charge of \$6,500 per month will be incurred plus all expenses and living accommodation. In addition to the cost of the crew, special tooling including cranes, forklifts and hoists must be supplied.

There are a series of considerations in reinstalling the equipment, including:

- Inland freight to the site
- Site preparation
- Concrete equipment foundations
- Erection of structural supports and fabricated components, including ducting
- Rewiring and possible acquisition of new motors because of differences in local power supplies
- Production building
- Building services

If a comparable ginning operation was installed in the United States, the estimated total cost would be in the range of \$200,000 to \$300,000. The installation cost in the Philippines will again be lower.

Fair Market Value

The San Juan plant is a small ginning operation. Production capacity is estimated at only 5 - 6 bales per hour and the age of the plant is approximately thirty years. These two factors may be of low significance to some perspective buyers but they are of sufficient importance to establish the market. The Textile Machinery Export Association reports that the typical market would be composed of groups of private investors from Third World countries whose aim is simply to establish a cotton ginning plant

with a minimum investment. Technological factors and input from farmer users are of lower priority. The equipment does not have to be new, and cotton farmers will adapt the plant to their suit use.

Comparable transactions proved difficult to confirm. However, the Textile Machinery Export Association currently has three independent ginning mills available for sale. They are all located in South Carolina, in close proximity to the coast, and are complete production facilities. Although maintained, they have not operated for three to ten years. Most importantly, they are twenty to thirty year old plants and their production capacities are 7 - 9 bales per hour, similar to San Juan. They have been exposed to the market for eight to twelve months and are offered for sale at \$75,000 to \$150,000 the higher price being for the newest and cleanliest plant. Equipment includes Lummus ginning machinery. Dismantling costs and freight would be at the buyer's expense. I am informed that there have been responses but no offers. The Textile Machinery Export Association believes that a sale of this nature takes a substantial time to materialize.

Discussion with Lummus, the gin manufacturer, supports this price range. Lummus suggests that the San Juan facility might realize 10% of cost new if offered for sale, \$100,000 - \$200,000. Information from other sources estimates a price range of \$75,000 to \$100,000.

It is, therefore, my opinion that, should the San Juan ginning equipment be offered for sale on the market, a likely realization would be in the range of \$75,000 to \$150,000. It is my further opinion that the estimated fair market value in exchange is \$110,000.

Polomolok, South Cotabato

Polomolok is a two stand ginning operation with a production capacity of up to 20 bales per hour. Study of the appraisal inventory, prepared by Cuervo Appraisers Inc., shows that this facility is simi arly equipped with modern, current production machinery by Lummus of Georgia. The inventory also shows that there are examples of older ginning equipment, stored in a dismantled condition.

A copy of an appraisal of the Polomolok facility by Cuervo Appraiser's, Inc. is shown in appendix C. Major items of equipment are now summarized in the order they appear on the Cuervo appraisal. Important facts and dismantling considerations are outlined for each item.

Suction System, Power Telescope: According to the Cuervo Appraisers appraisal inventory, this item is dismantled and stored. Dismantled machinery will usually command less attention from perspective buyers because of the uncertainties in condition, design and operating capabilities.

Suction System, 2 Traveling Power Telescopes: These machines are situated in place. Each telescope appears to be mounted on a motorized, traveling bridge or trolley which runs along a 35 foot, steel I-beam track. An installation of this nature requires substantial structural supports and component fabrication and, normally, if dismantled, only selected parts would be salvaged for re-erection. In the case of sale, the track and other parts may be sold to a local buyer in order to avoid the expense of dismantling and shipping such a bulky item.

Vacuum Wheels, 2: Uninstalled, but would be shipped to the new location as valuable Lummus parts.

Unloading Separator, 2: A more complex and large system than San Juan. Structural steel supports and fabricated housing, catwalk and other components will make dismantling a costly procedure. Not all items will be salvagable.

Inclined Lint Cleaner: An important item of equipment which would be removed in a sale.

Conveyor Distributor, 2 Gin Stands each with Federal Extractor, Seed and Hull Conveyor: A group of items which form the nucleus of the ginning operation. Manufactured by Lummus, the gins and supporting equipment are capable of processing 20 bales of cotton per hour. Importantly, the Imperial 158 model gin is current Lummus technology with no difficulty in obtaining replacement parts. This two stand ginning operation is able to offer three times the capacity of the San Juan facility.

Seed Blower: The blower is manufactured by Roots Connerville and has a processing capacity of 25 bales per hour. It is highly suitable for this type of ginning operation.

Overflow System: Substantial amount of site fabrication. Certain component parts, including piping, would be lost in disassembly.

Lint Cleaners, 2: Current model equipment from Lummus. Only ancilliary fittings would be lost in disassembly and relocation.

Elevator Fan, Lint Cleaner Trash Fan, Gin Trash Fan: Current model centrifugal fans. The cyclone dust collectors are bulky and costly to relocate.

Outfit Battery Condenser: A 40" model suitable for a two stand ginning facility. Although bulky, the battery condenser will breakdown into component parts for shipping.

Press System: 54" standard density press with feeder, tramper and hydraulics. This is good, current and modern equipment which would be of high interest if exposed to the market in the United States.

Hydraulic Control Unit: Not in use, but self contained and ready to crate.

Electrical Control: Voltage differences at the new location might necessitate replacement of parts and rewiring.

Cotton Module Builders: Purchased new in 1965. Self contained and ready to crate.

Wire Tire Balers, 3: Units were crated at the date of inspection by Cuervo Appraisers.

Cotton Ginning Machinery: According to Cuervo Appraisers, these machines are not operational. They have been dismantled and cannibalized. It should be noted that the equipment is old and obsolete and in its present condition would be of minimum value to a prospective purchaser of the facility.

Diesel Generator Set: Self contained and essential for the operation.

Electrical Distribution System: Consists of electrical distribution wiring throughout the facility with conduit and local switchgear. Small components and specialist parts can be salvaged for relocation but it is simpler and more cost effective to rip out the wiring and sell to local dealers for recycling. The act of removing the wiring might be accomplished more efficiently if offered to the local dealer. Rewiring would be necessary at the new site.

Transformers: Currently removable but may be suitable at new site.

Fuel and Water Tanks: Bulky and costly to ship. These items are simple to replicate at the new site and therefore these existing tanks may just be sold to local dealers or users.

Water Distribution: Consists of distribution piping and valves. It is more cost effective to rip out the piping and sell to local dealers for recycling.

Truck Scale: Installation and foundations are important. Foundations will remain but the platform should be removed together with the tare mechanism.

Miscellaneous Items: All items appear removable and some could be sold independently to local sources in order to obtain a higher realization.

Cost of Dismantling and Container Packing

The same considerations outlined for the San Juan facility apply to Polomolok, except that the cost incurred in dismantling a twenty bale operation will be slightly greater. This plant is large and more complex and will take more time to disassemble and crate. A cost of \$100,000 - \$140,000 is estimated if the plant was located in the United States. Once again, these costs will be lower in the Philippines. However, if the advice of a professional engineer from Lummus is sought for an assumed two month disassembly period, the engineer's costs together with ancillary equipment costs will equate to approximately 25% of the estimated cost in U.S. terms.

Cost of Relocation and Installation

These factors are explained for the San Juan facility and do not need to be reiterated. However, Polomolok is a larger and more complex operation than San Juan. The cost of installing a similar ginning operation in the United States is estimated in the range of

\$250,000 - \$300,000. The cost in the Philippines will be considerably lower.

Fair Market Value

Production capacity of 20 bales per hour and current Lummus machinery make this plant a more attractive proposition than San Juan. Capacity is three times greater than San Juan. Lummus believes that if a plant of this capacity and age was exposed to the market, it may realize an amount in the region of 25% of the cost new, or between \$300,000 - \$400,000. Another source, manager of a large ginning cooperative in California with similar production machinery, suggests \$400,000. It is my opinion, therefore, that should the Polomolok ginning equipment be offered for sale on the market, a likely realization would be in the range of \$300,000 - \$400,00. It is my further opinion that the estimated fair market value in exchange is \$325,000.

PROPERTY DISPOSAL CONSIDERATIONS

It is important to point out that if a cotton gin is offered for sale on the world market, one offer should be sought for the purchase of all the production equipment. The equipment is often more desirable if it forms a production process which can be demonstrated as an operating facility. Equipment that is installed and capable of running will be of more interest to a prospective purchaser than one that has been partly dismantled or dismantled and moved to a temporary location awaiting sale. Disassembly, crating and shipping should be at the buyer's expense. A sale of the complete production facility also ensures disposal of the less marketable items, which effectively minimizes the costs of sale.

The aforementioned investigation and analysis concluded that there is a world market for used cotton ginning plant and equipment.

However, disposal of an entire production facility is usually a lengthy procedure. The market is fragmented. Interested parties are scattered around the world and must be contacted and informed that the property is available for sale. Indeed, certain specialist organizations and individuals may be effective in the dissemination of sale particulars to draw the first responses. This will be followed by inspection of facilities, negotiations, financing arrangements and organization for removal. It is understood that it took many months to locate a buyer for a cotton ginning plant in Ecuador. In fact, three ginning facilities in South Carolina have been listed for sale for twelve months and as of this date there have been no offers to purchase. Information suggests that a one to two year time period must be anticipated for the disposal of a cotton ginning facility.

VALUE CONCLUSION

San Juan, Ilocos Sur

It is estimated that if the San Juan ginning equipment is offered for sale, a figure in the range of \$75,000 - \$150,000 would be expected. Based upon the aforementioned investigation and analysis, it is my opinion that the fair market value is \$110,000.

Polomolok, South Cotabato

It is estimated that if the Polomolok ginning equipment is offered for sale, a figure in the range of \$300,000 - \$400,000 would be expected. Based upon the aforementioned investigation and analysis, it is my opinion that the fair market value is \$325,000.

STATEMENT OF LIMITING CONDITIONS

1. This appraisal report was prepared only for the stated purpose, and opinions of value are effective only as of the stated valuation date.
2. All statements of value are presented as considered opinions based upon the facts and data available, as discussed within this report. Armstrong & Ryan takes no responsibility for changes in market conditions, or for the inability of the owner to locate a purchaser at the appraised value.
3. The analysis included herein did not include a physical inspection of the property nor investigation of legal fee or title to the property. The owner's claim to the property is assumed to be valid. No consideration has been given to possible liens or encumbrances against the property.
4. All facts and dimensions have been obtained from information provided to us by others.
5. We have verified factual matters contained in this report to the extent we have deemed feasible. Armstrong & Ryan certify that, to the best of their knowledge and belief, such factual matters are true and correct, and that no important factors affecting the value of this property were knowingly overlooked or withheld. We have taken market data from sources deemed reliable, but which we could not verify in all cases. The appraised value is predicated on the financial structure prevailing as of the date of value.