

## MANAGEMENT DISCUSSION AND ANALYSIS

### ▶ Significant Events and Developments

The first half of 2006 saw a significant breakthrough in the development of our leisure, gaming and entertainment business in Macau. In March 2006, Melco PBL (a 50:50 joint venture with Publishing and Broadcasting Limited (“PBL”)) entered into a series of transactions to acquire the last remaining gaming subconcession in Macau. The acquisition of a gaming license is a major milestone for the Group as this transforms Melco PBL from a mere industry participant riding on Sociedade de Jogos de Macau, S.A. (“SJM”)’s license into a fully fledged license holder in Macau.

The subconcession to PBL Entertainment (Macau) Limited (“PBL Macau”) (a special purpose company set up to hold the gaming license) was formally approved and granted by the Macau Government on 8 September 2006. Subject to completion of the remaining standard legal procedures, Melco PBL, in which Melco International Development Limited (“Melco”) has a de facto interest of 50%, will be able to instantly enjoy 100% of the economic benefits of its Macau gaming business.

Furthermore, on 29 August 2006, our joint venture partner, PBL received formal approval from the Victorian Commission for Gambling Regulation and the Gaming and Wagering Commission of Western Australia to the joint venture with Melco. This clears the remaining regulatory hurdle in Australia for the joint venture and signifies the endorsement of Melco’s good standing by Australian gaming regulatory bodies.

By virtue of having our own gaming license in Macau, we will be able to tap the abundant opportunities directly. To start with, we will be able to independently operate all our gaming businesses in Macau without having to give up a significant portion of the gaming revenue to SJM for the right to operate under its license – as would have been the case under the previous arrangement. Moreover, we will have the total flexibility to run our own casinos or add new ones without being constrained by SJM. In addition, subject to Macau Government’s approval, we may further enhance our return by entering into revenue-sharing arrangements with other seasoned gaming operators.

As a result of the Group’s increasing importance in the capital markets, Melco has been officially included as a constituent stock in the MSCI Hong Kong Index since May 2006.

## ▶ Outlook

In 2004, Macau overtook Atlantic City in the US to become the world's second-largest gaming market, and it is still growing fast. With another 16 casino projects currently in the pipeline for completion by 2010, Macau is fast transforming into a leisure and entertainment destination in Asia. At the heart of Macau's growth is its gaming and entertainment industry, which has given the city a unique edge in the Greater China region.

Being a license holder, the Group is in a very strong position to capitalize on Macau's growth and transformation. Crown Macau is scheduled to open in April of 2007, and City of Dreams in the second half of 2008, supplemented by the highly successful chain of Mocha Slot Clubs. In addition, the Group has recently unveiled a third casino project, to be sited on the waterfront of the Macau Peninsula on which a mass-market oriented casino will be built to cater for the day-tripper market.

With a stronghold in Hong Kong and Macau, the Group intends to expand its operations to cover the whole of Asia. Together with our exclusive partner PBL, we have an ideal platform on which to capitalize on the lucrative opportunities in Asia and beyond.