

Financial Review

HKEx Group – Overview of 2006 Results and Financial Position

Key Market Statistics and Business Drivers – Cash Market

Average daily turnover value on the Stock Exchange	\$33.9 billion*
Number of newly listed derivative warrants	2,823*
Number of newly listed companies on Main Board	56
Number of newly listed companies on GEM	6
Number of Main Board companies at 31 December 2006	975
Number of GEM companies at 31 December 2006	198
Total equity funds raised on Main Board	\$516.0 billion*
Total equity funds raised on GEM	\$8.5 billion
Total equity funds raised	\$524.5 billion*

* New record high in 2006

2005 Consolidated Balance Sheet

		As restated \$'000
Assets		
Fixed assets, land and properties	6	370,246
Investments in associates		64,581
Funds	7	15,027,401
Investments and time deposits		2,799,178
Cash and cash equivalents		1,359,133
Other assets	8	3,310,377
		<u>22,930,916</u>
Liabilities		
Participants' contributions to Funds	9	14,400,332
Participants' admission fees received		82,700
Other liabilities	10	4,110,413
		<u>18,593,445</u>
Net assets		
		<u>4,337,471</u>
Capital and reserves		
Share capital, share premium and reserves		1,911,695
Shares held for Share Award Scheme	11	(30,028)
Retained earnings		1,776,254
Proposed/declared dividend		679,550
		<u>2,455,804</u>
		<u>4,337,471</u>

Segment Profit for the Year

	Cash Market \$'000	Derivatives Market \$'000	Clearing Business \$'000	Information Services \$'000	Total \$'000
Income	1,822,011	661,305	1,269,840	393,760	4,146,916
Operating expenses	570,324	158,201	420,779	61,269	1,210,573
Segment results	1	2	3	4	2,936,343
Share of profits less losses of associates	1	-	27,123	-	5
Segment profits before taxation	1,251,688	503,104	876,184	332,491	2,963,467
Taxation					(444,898)
Profit attributable to shareholders					<u>2,518,569</u>

Cash Flows for the Year

		\$'000
Net cash inflow from operating activities	12	2,865,468
Purchases of shares held for Share Award Scheme	11	(21,269)
Capital expenditures		(60,269)
Dividends paid		(1,671,151)
Purchases of available-for-sale financial assets of the Corporate Funds		(535,585)
Other net cash inflows		278,930
Net increase in cash and cash equivalents		856,124
Cash and cash equivalents at 1 January 2006		1,359,133
Cash and cash equivalents at 31 December 2006		<u>2,215,257</u>

Key Market Statistics and Business Drivers – Derivatives Market

Average daily number of derivatives contracts traded on the Futures Exchange	100,318*
Average daily number of stock options contracts traded on the Stock Exchange	73,390*

* New record high in 2006

2006 Consolidated Balance Sheet

		\$'000
Assets		
Fixed assets, land and properties	6	323,584
Investments in associates		68,377
Funds	7	23,977,540
Investments and time deposits		3,641,853
Cash and cash equivalents		2,215,257
Other assets	8	10,226,687
		<u>40,453,298</u>
Liabilities		
Participants' contributions to Funds	9	23,308,969
Participants' admission fees received		81,450
Other liabilities	10	11,805,293
		<u>35,195,712</u>
Net assets		
		<u>5,257,586</u>
Capital and reserves		
Share capital, share premium and reserves		1,982,340
Shares held for Share Award Scheme	11	(51,297)
Retained earnings		2,060,156
Proposed/declared dividend		1,266,387
		<u>5,257,586</u>

Movements in Share Capital, Share Premium and Reserves for the Year

	Share capital and share premium \$'000	Employee share-based compensation reserves \$'000	Revaluation reserves \$'000	Designated reserves \$'000	Total \$'000
At 1 January 2006	1,213,160	34,980	(37,086)	700,641	1,911,695
Issue of shares	30,895	-	-	-	30,895
Employee share-based compensation benefits	-	24,033	-	-	24,033
Fair value change net of deferred tax:					
- financial assets	-	-	47,203	-	47,203
- leasehold buildings	-	-	415	-	415
Share of reserves of an associate	-	441	37	-	478
Transfer to retained earnings	-	-	-	(32,379)	(32,379)
Transfer	7,335	(7,335)	-	-	-
At 31 December 2006	1,251,390	52,119	10,569	668,262	1,982,340

Notes

Due to the positive market sentiment stimulated by the large IPOs and the sustained economic growth in the Mainland, activity on the Stock Exchange and the Futures Exchange increased substantially. As a result, the Group achieved record profit for the third consecutive year in 2006. The performance of the Group by business segment during 2006 was as follows:

- 1 Profit of the Cash Market increased by \$624m mainly due to the higher turnover of the Cash Market and the rise in Stock Exchange listing fees attributable to the higher number of newly listed derivative warrants during the year.
- 2 Profit of the Derivatives Market increased by \$209m mainly as a result of the increase in investment income from the Margin Funds and the increase in the level of activity on the Derivatives Market.
- 3 Profit of the Clearing Business rose by \$480m mainly attributable to the increase in clearing and settlement fees generated from Cash Market transactions and depository, custody and nominee services fees.
- 4 Profit of the Information Services Business increased by \$74m as demand for information increased in tandem with the activities of the Cash and Derivatives Markets.
- 5 Share of profits less losses of associates increased due to the higher profitability of one of the associates and the acquisition of a further six per cent interest in that associate during 2005.
- 6 Fixed assets, land and properties decreased by \$47m mainly attributable to depreciation during the year.
- 7 Funds comprised Margin Funds of \$21,666m (2005: \$13,649m), Clearing House Funds of \$2,271m (2005: \$1,340m) and Compensation Fund Reserve Account of \$41m (2005: \$38m). The rise in Margin Funds was as a result of increased open interest in futures and options contracts. The increase in Clearing House Funds reflected the increase in additional contributions from Participants in response to market fluctuations and changes in risk exposure.
- 8 Other assets mainly consisted of money obligations receivable under the CNS system of \$9,586m (2005:\$2,890m) and other receivables.
- 9 Participants' contributions to funds represented Margin deposits from Participants of \$21,666m (2005:\$13,649m) and Participants' contributions to Clearing House Funds of \$1,643m (2005:\$752m). The reasons for the movements in the contributions were similar to those for the movements in the funds as explained in note 7.
- 10 Other liabilities mainly represented money obligations payable under the CNS system of \$9,588m (2005:\$2,890m) and other payables.
- 11 Shares were held by The HKEx Employees' Share Award Scheme ("HKEx Employee Share Trust") on behalf of eligible employees before the share awards became vested. During the year, additional shares purchased by the HKEx Employee Share Trust amounted to \$21m.
- 12 Net cash inflow from operating activities increased by \$1,436m mainly due to higher profit generated during the year.

Movements in Retained Earnings for the Year

	\$'000
Profit attributable to shareholders	2,518,569
Dividends	(1,680,895)
Dividends forfeited	686
Transfer from reserves	32,379
Net increase in retained earnings	870,739
Retained earnings at 1 January 2006	2,455,804
Retained earnings at 31 December 2006	3,326,543
Representing:	
Retained earnings	2,060,156
Proposed/declared dividend	1,266,387
	3,326,543

Overall Performance

	2006 \$'000	As restated 2005 \$'000
RESULTS		
Income:		
Income affected by market turnover	2,390,846	1,437,218
Stock Exchange listing fees	465,445	413,000
Income from sale of information	391,213	322,713
Investment income	601,080	300,120
Other income	298,332	221,017
	4,146,916	2,694,068
Operating expenses	1,210,573	1,145,483
	2,936,343	1,548,585
Operating profit	27,124	18,433
Share of profits less losses of associates		
	2,963,467	1,567,018
Profit before taxation	(444,898)	(227,460)
Taxation		
	2,518,569	1,339,558
Profit attributable to shareholders		
	\$2.37	\$1.26
Basic earnings per share	\$2.34	\$1.26
Diluted earnings per share		
	\$0.94	\$0.49
Interim dividend per share	\$1.19	\$0.64
Final dividend per share		
	\$2.13	\$1.13
Dividend payout ratio	90%	90%
	2006 \$'000	As restated 2005 \$'000
KEY BALANCE SHEET ITEMS		
Shareholders' funds	5,257,586	4,337,471 ^o
Total assets *	40,453,298	22,930,916 ^o
Net assets per share #	\$4.94	\$4.09 ^o

^o Audited and restated (shareholders' funds down by \$30 million, total assets down by \$30 million and net assets per share down by \$0.02) due to the adoption of a revised HKFRS

* The Group's total assets include the Margin Funds received from Participants on futures and options contracts.

Based on 1,064,190,346 shares as at 31 December 2006, being 1,065,448,346 shares issued and fully paid less 1,258,000 shares held for the Share Award Scheme (2005: 1,061,796,846 shares, being 1,062,754,846 shares issued and fully paid less 958,000 shares held for the Share Award Scheme)

The Group achieved record high profit for the third consecutive year in 2006. Profit attributable to shareholders increased by 88 per cent to \$2,519 million for the year ended 31 December 2006, compared with \$1,340 million for 2005 mainly due to higher turnover-related income and investment income.

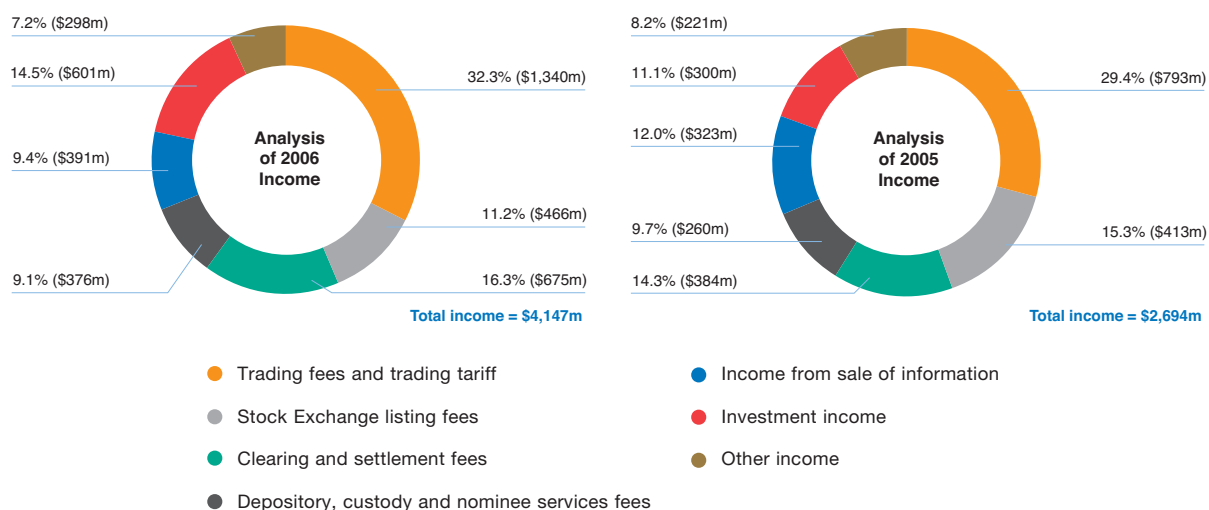
Due to the positive market sentiment stimulated by the large IPOs and the sustained economic growth in the Mainland, activity on the Stock Exchange and the Futures Exchange increased substantially. Several new records were achieved in the Cash and the Derivatives Markets in 2006, including the highest total equity capital raised and highest IPO equity capital raised, record annual turnover of the Cash Market and the highest number of contracts traded on the Derivatives Market. As a result, total turnover-related income of the Group increased significantly.

Investment income doubled due to the increase in net interest income and fair value gains of Corporate Fund investments.

Total operating expenses increased by six per cent during the year mainly due to higher staff costs and premises expenses driven by the buoyant job and property markets but were partly offset by the decrease in depreciation.

The accounts have been prepared in accordance with HKFRSs issued by the HKICPA, which have been aligned with the requirements of International Financial Reporting Standards in all material respects as at 31 December 2006.

Income



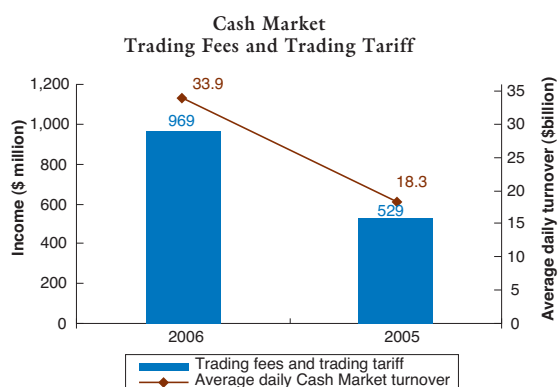
(A) Income affected by market turnover

	2006 \$'000	2005 \$'000	Change
Trading fees and trading tariff	1,340,355	793,247	69%
Clearing and settlement fees	674,373	384,019	76%
Depository, custody and nominee services fees	376,118	259,952	45%
Total	2,390,846	1,437,218	66%

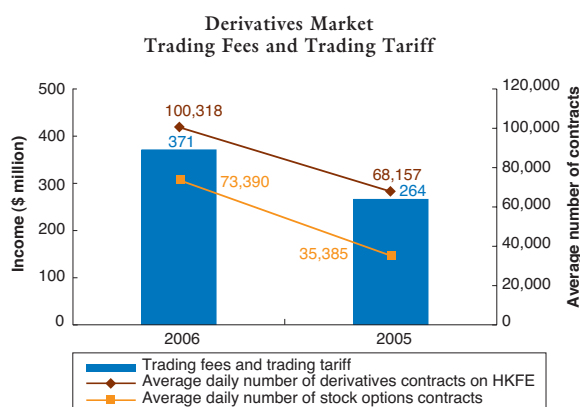
Key market indicators

	2006	2005	Change
Average daily turnover value on the Stock Exchange	\$33.9 billion	\$18.3 billion	85%
Average daily number of derivatives contracts traded on the Futures Exchange	100,318	68,157	47%
Average daily number of stock options contracts traded on the Stock Exchange	73,390	35,385	107%

Trading fees and trading tariff



The increase in trading fees and trading tariff from the Cash Market was mainly due to the significant increase in turnover of the Cash Market, in particular, H shares. Several new records were achieved in the Cash Market in 2006, including the highest total market turnover, and the highest trading turnover of H shares and derivative warrants.



The increase in trading fees and trading tariff from the Derivatives Market was mainly driven by the increase in the number of contracts traded on the Derivatives Market. Total number of futures, options, HSI Futures and stock options traded was at record high in 2006.

Clearing and settlement fees

Clearing and settlement fees are derived predominantly from Cash Market transactions. Despite being mostly ad valorem fees, clearing and settlement fees are subject to a minimum and a maximum fee per transaction. Clearing and settlement fees did not increase linearly with the Cash Market turnover as a higher proportion of the value of transactions was subject to the maximum fee and a lower proportion of the value of transactions was subject to the minimum fee in 2006.

Depository, custody and nominee services fees

Depository, custody and nominee services fees mainly comprised scrip fees, stock custody fees, eIPO handling charges, dividend collection fees, stock withdrawal fees and corporate action fees. Despite the abolition of scrip fees on deemed book close effective 1 January 2006 (2005 deemed book close scrip fees: \$41 million), depository, custody and nominee services fees increased due to higher scrip fees, stock withdrawal fees, corporate action fees, dividend collection fees and eIPO handling charges resulting from increased activity of the Cash Market. The fees were influenced by the level of Cash Market activities but did not move proportionately with changes in the Cash Market turnover as they varied mostly with the board lots rather than the value of the securities concerned and many were subject to a maximum fee. Moreover, scrip fee was only chargeable on the net increase in individual Participants' aggregate holdings of the securities on book closing dates.

(B) Stock Exchange listing fees

	2006 \$'000	2005 \$'000	Change
Annual listing fees	274,586	263,945	4%
Initial and subsequent issue listing fees	184,601	142,075	30%
Others	6,258	6,980	(10%)
Total	465,445	413,000	13%

The increase in annual listing fees was attributable to the higher number of listed securities. The increase in initial and subsequent issue listing fees was primarily due to the increase in the number of newly listed derivative warrants.

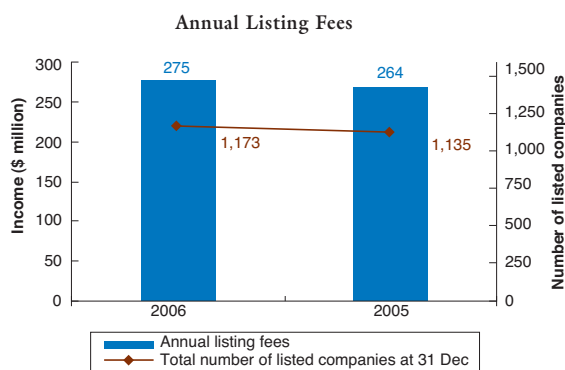
Key drivers for annual listing fees

	As at 31 Dec 2006	As at 31 Dec 2005	Change
Number of companies listed on Main Board	975	934	4%
Number of companies listed on GEM	198	201	(1%)
Total	1,173	1,135	3%

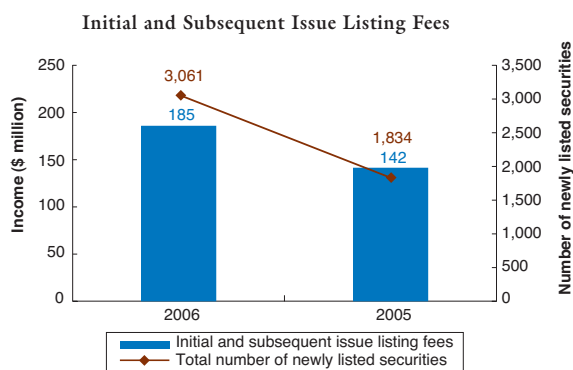
Key drivers for initial and subsequent issue listing fees

	2006	2005	Change
Number of newly listed derivative warrants	2,823	1,682	68%
Number of newly listed CBBCs	83	–	N/A
Number of newly listed companies on Main Board	56	57	(2%)
Number of newly listed companies on GEM	6	10	(40%)
Number of other newly listed securities on Main Board and GEM	93	85	9%
Total number of newly listed securities	3,061	1,834	67%

	2006 \$ billion	2005 \$ billion	Change
Total equity funds raised on Main Board	516.0	298.7	73%
Total equity funds raised on GEM	8.5	3.0	183%
Total equity funds raised	524.5	301.7	74%



Annual listing fees increased in line with the total number of listed companies.



Initial and subsequent issue listing fees increased with the total number of newly listed securities.

(C) Income from sale of information

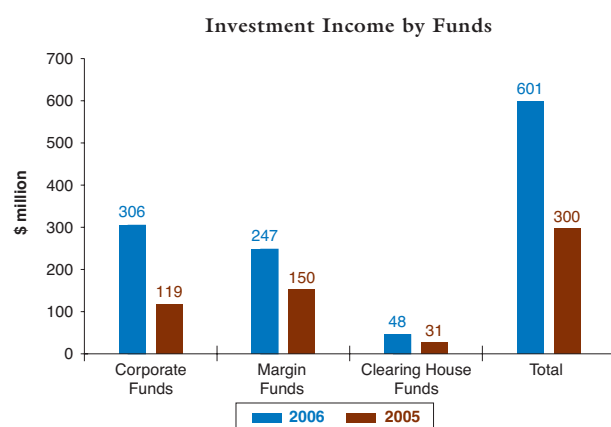
	2006 \$'000	2005 \$'000	Change
Income from sale of information	391,213	322,713	21%

Income from sale of information rose as demand for information increased in tandem with the activity on the Cash and Derivatives Markets.

(D) Investment income

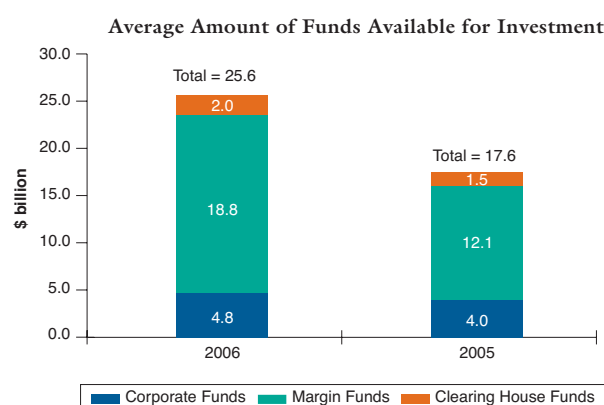
	2006 \$'000	As restated 2005 \$'000	Change
Gross investment income	1,043,750	426,380	145%
Interest expenses	(442,670)	(126,260)	251%
Investment income	601,080	300,120	100%

The movements in total investment income by Funds were as follows:



Investment income from Margin Funds and Clearing House Funds rose due to increased fund size and rising interest rates in 2006. The increase in investment income from Corporate Funds was due to rising interest rates and a significant increase in fair value gains of Corporate Fund investments in 2006.

The average amount of funds available for investment was as follows:

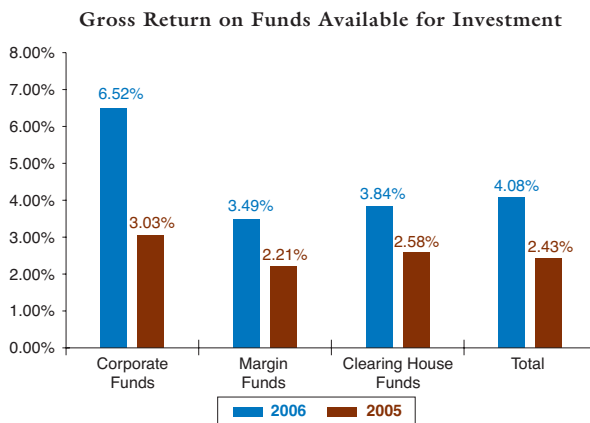


The increase in average amount of Corporate Funds was mainly due to the profit net of dividends paid.

Average amount of Margin Funds increased primarily on account of the increased open interest in futures and options contracts.

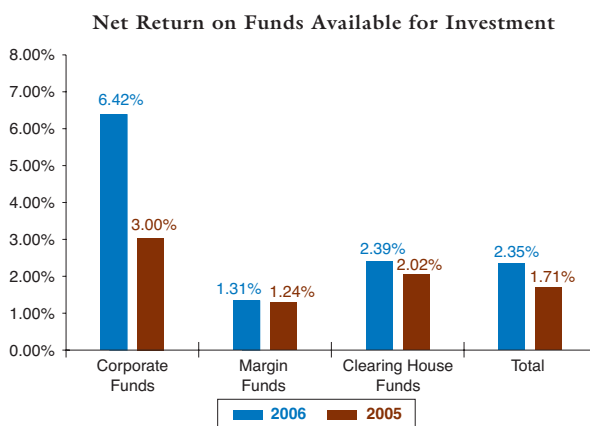
The increase in average amount of Clearing House Funds was mainly due to the increase in additional contributions from Participants in response to market fluctuations and changes in risk exposure.

The gross return on funds available for investment is set out below:



The return on Corporate Funds increased due to the rise in fair value gains of Corporate Fund investments, reflecting market movements, and the increase in interest rates. The return on Margin Funds and Clearing House Funds increased mainly as a result of rising interest rates in 2006. The return on Margin Funds was lower than that of the Clearing House Funds as part of the margin deposits was denominated in Japanese Yen, which generated very low interest income.

The net return on funds available for investment after the deduction of interest expenses was as follows:



Interest was payable on all margin deposits, certain part of Clearing House Fund contributions and a small portion of Corporate Funds. The net return on Margin Funds in 2006 was only marginally higher than that of 2005 as the increase in gross return in 2006 was mostly offset by a substantial increase in interest payable to the Participants due to higher interest rates and a change in the benchmarked interest rate payable on cash margin deposits from 1 June 2005 onwards. In 2006, interest was paid on cash margin deposits based on the savings rate. Prior to 1 June 2005, interest was not always paid to Participants as the interest rates payable on the cash margin deposits were often lower than the retention rates charged by HKCC and SEOCH on such cash margin deposits. The increase in net return on Clearing House Funds in 2006 was lower than the increase in gross return as a higher proportion of the Clearing House Fund contributions was entitled to interest in 2006.

Details of the investment portfolio are set out in the Treasury section under the Business Review.

(E) Other income

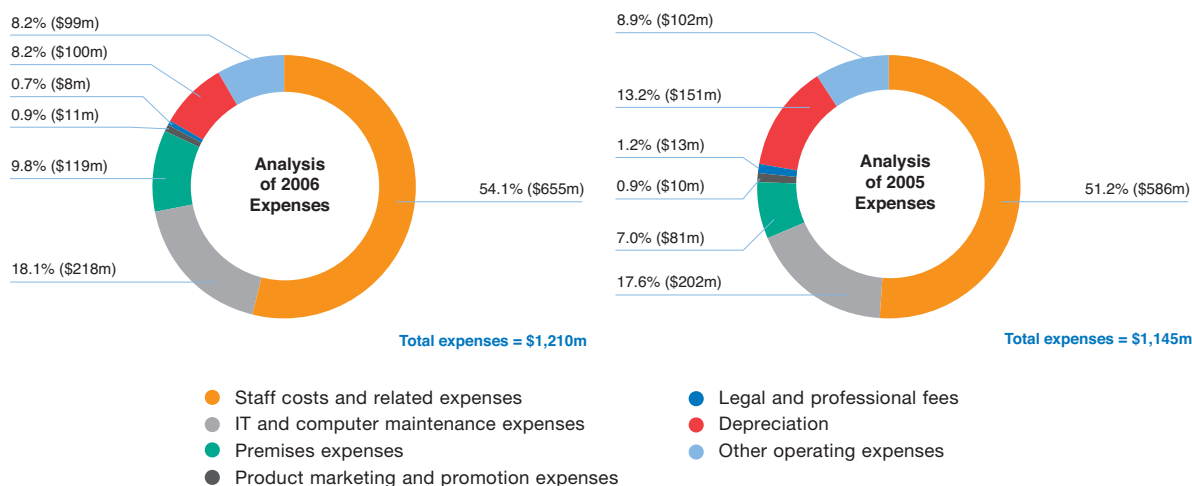
	2006 \$'000	2005 \$'000	Change
Network, terminal user, dataline and software sub-license fees	180,372	129,733	39%
Participants' subscription and application fees	33,927	34,351	(1%)
Brokerage on direct IPO applications	57,066	34,123	67%
Trading booth user fees	9,162	–	N/A
Fair value gain of an investment property	1,600	4,400	(64%)
Accommodation income on cash margin deposits in non-contract settlement currencies and securities deposited by Participants as alternatives to cash deposits of Margin Funds	3,164	2,154	47%
Miscellaneous income	13,041	16,256	(20%)
Total	298,332	221,017	35%

Network, terminal user, dataline and software sub-license fees rose due to the increase in sales of OG and AMS/3 terminals (as most Participants replaced their outdated network equipment) and related user fees.

Brokerage on direct IPO applications increased in line with funds raised by IPOs, in particular ICBC, the largest IPO in the world in 2006, and BOC.

Despite the abolition of accommodation charges on cash margin deposits and the reduction in accommodation fees charged on utilised non-cash collateral by HKCC and SEOCH from 1 June 2005 onwards, accommodation income increased mainly due to the increase in utilisation of non-cash collateral by Participants to meet their margin obligations.

Miscellaneous income decreased due to an exchange gain on accounts payable denominated in foreign currencies caused by the strengthening HKD and interest on late payment levied on information vendors in 2005 which were not repeated in 2006.

Operating Expenses

	2006 \$'000	As restated 2005 \$'000	Change
Staff costs and related expenses	654,806	586,034	12%
Information technology and computer maintenance expenses	218,608	201,725	8%
Premises expenses	119,167	80,679	48%
Product marketing and promotion expenses	11,270	10,065	12%
Legal and professional fees	7,996	13,641	(41%)
Depreciation	99,888	150,995	(34%)
Other operating expenses	98,838	102,344	(3%)
Total	1,210,573	1,145,483	6%

Staff costs and related expenses increased by \$69 million, primarily due to the increase in salary costs and contribution to provident funds as a result of the increase in headcount and salary adjustment, and an increase in performance bonus on account of the improved performance of the Group in 2006.

Information technology and computer maintenance expenses of the Group, after excluding goods and services directly consumed by the Participants of \$85 million (2005: \$55 million), were \$133 million (2005: \$147 million). The reduction was mainly due to lower license fees and network costs. The increase in costs directly consumed by Participants was primarily due to purchases of OG and AMS/3 terminals by the Participants to replace their outdated network equipment. Costs consumed by Participants were mostly recovered from the Participants and the income was included as part of network, terminal user, dataline and software sub-license fees under Other income. During the year, capital expenditures on computer systems, hardware and software amounted to \$27 million (2005: \$58 million).

Premises expenses rose due to increases in rental upon the renewal of certain leases.

Product marketing and promotion expenses increased due to promotional activities relating to the opening of the new Exchange Trading and Exhibition Hall Complex.

Legal and professional fees decreased mainly due to legal costs incurred in 2005 on the New World judicial review case.

Depreciation decreased as certain fixed assets largely IT-related became fully depreciated.

Share of Profits less Losses of Associates

	2006 \$'000	2005 \$'000	Change
Share of profits less losses of associates	27,124	18,433	47%

Share of profits less losses of associates increased due to the higher profitability of one of the associates, CHIS, and the acquisition of a further six per cent interest in CHIS in May 2005.

Taxation

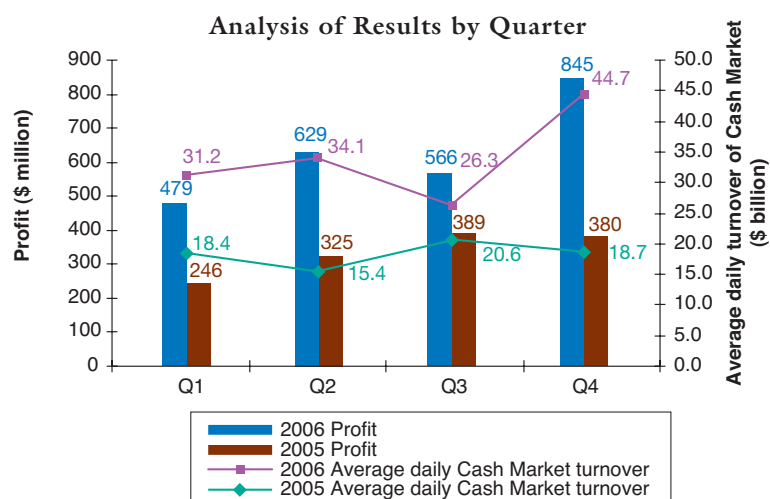
	2006 \$'000	2005 \$'000	Change
Taxation	444,898	227,460	96%

Taxation increased mainly attributable to an increase in operating profit, but partly offset by an increase in non-taxable investment income.

Analysis of Results by Quarter

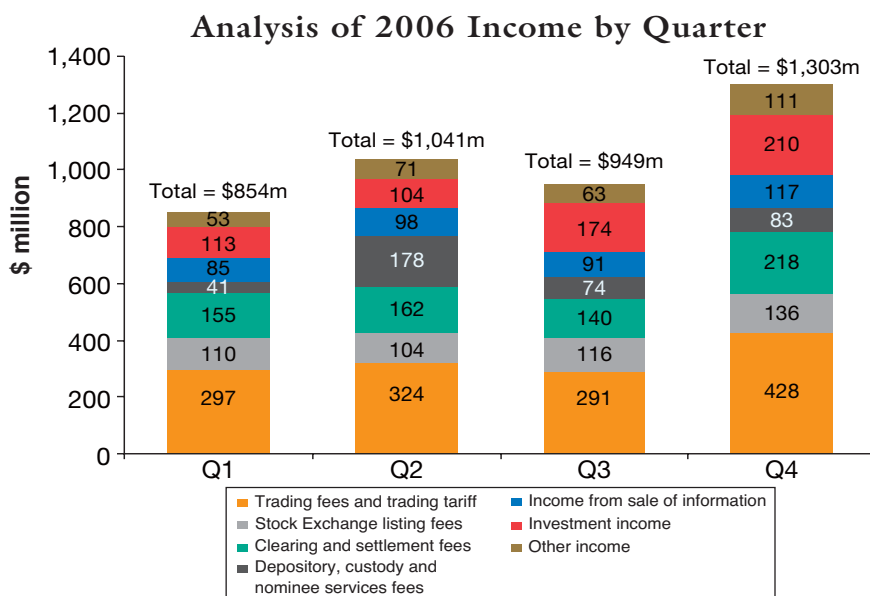
Analysis of results by quarter

	Q1 2006 \$'000	Q2 2006 \$'000	Q3 2006 \$'000	Q4 2006 \$'000	Total 2006 \$'000
Income	854,127	1,041,121	948,435	1,303,233	4,146,916
Operating expenses	292,527	303,961	297,163	316,922	1,210,573
Operating profit	561,600	737,160	651,272	986,311	2,936,343
Share of profits less losses of associates	3,220	6,032	6,734	11,138	27,124
Profit before taxation	564,820	743,192	658,006	997,449	2,963,467
Taxation	(85,981)	(113,720)	(92,288)	(152,909)	(444,898)
Profit attributable to shareholders	478,839	629,472	565,718	844,540	2,518,569
	Q1 2005 \$'000	Q2 2005 \$'000	Q3 2005 \$'000	As restated Q4 2005 \$'000	As restated Total 2005 \$'000
Profit attributable to shareholders	245,421	325,375	389,120	379,642	1,339,558



Profit attributable to shareholders for all quarters of 2006 has shown a significant growth over 2005. The highest profit was recorded in the fourth quarter of 2006 when the average daily turnover value on the Stock Exchange, average daily number of derivatives contracts traded on the Futures Exchange and stock options contracts traded reached the peak during the quarter.

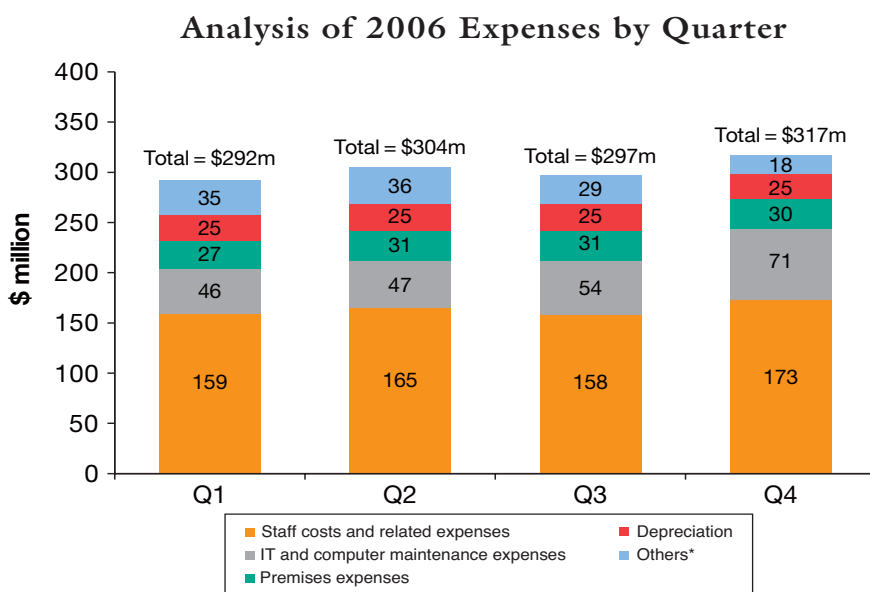
Analysis of income by quarter



The key market indicators affecting the income of the Group by quarters are set out below:

	Q1 2006	Q2 2006	Q3 2006	Q4 2006	Year 2006
Average daily turnover value on the Stock Exchange (\$ billion)	31.2	34.1	26.3	44.7	33.9
Average daily number of derivatives contracts traded on the Futures Exchange	87,755	107,681	95,911	110,661	100,318
Average daily number of stock options contracts traded on the Stock Exchange	61,863	65,038	66,836	100,169	73,390
Number of newly listed derivative warrants	546	566	716	995	2,823
Number of newly listed companies on Main Board	12	10	10	24	56
Number of newly listed companies on GEM	3	1	1	1	6

Analysis of operating expenses by quarter



* Others include product marketing and promotion expenses, legal and professional fees and other operating expenses.

Key Changes to Financial Position

Key changes in the Group's financial position during the year were as follows:

(A) Fixed assets and capital commitments

The Group's fixed assets consisted of leasehold buildings, computer trading and clearing systems, other computer hardware and software and miscellaneous assets such as leasehold improvements.

As at 31 December 2006, the net book value of fixed assets dropped by \$48 million compared with 31 December 2005 mainly due to a \$62 million decrease in computer trading and clearing systems and other computer hardware and software to \$150 million (2005: \$212 million), attributable to depreciation of \$89 million, but partly offset by additions of \$27 million during the year. In 2006, the net book value of leasehold improvements increased by \$11 million to \$38 million (2005: \$27 million) due to the refurbishment of the Exchange Trading Hall and Exhibition Hall Complex.

The Group's capital expenditure commitments as at 31 December 2006, mainly related to the development and purchases of computer systems, amounted to \$92 million (2005: \$137 million, mainly related to the refurbishment of the Trading Hall and development and purchases of computer systems). The Group has adequate internal resources to fund its commitments on capital expenditures.

(B) Funds

	2006 \$'000	As restated 2005 \$'000	Change
Clearing House Funds	2,270,531	1,340,410	69%
Margin Funds	21,666,474	13,648,581	59%
Corporate Funds	5,897,645	4,196,721	41%
Total	29,834,650	19,185,712	56%

The increase in Clearing House Funds during the year reflected the increase in additional contributions from Participants in response to market fluctuations and changes in risk exposure.

The increase in Margin Funds was due to higher open interest in futures and options contracts.

The increase in Corporate Funds in 2006 was mainly due to the profit net of dividends paid during the year and increase in marks and stamp duty collected on behalf of the Government in line with the higher volume of Cash Market activities at the year-end.

(C) Significant investments held and material acquisitions and disposals of investments and subsidiaries

There were no material acquisitions or disposals of investments and subsidiaries during the year.

Details of the investments in associates are set out in the Investments in Associates section under the Business Review.

(D) Accounts receivable, prepayments and deposits and accounts payable, accruals and other liabilities

	2006 \$'000	As restated 2005 \$'000	Change
CNS money obligations receivable	9,586,161	2,889,804	232%
Other receivables from Participants	408,321	203,933	100%
Other accounts receivable, prepayments and deposits	211,759	197,427	7%
Less: provision for impairment losses of trade receivables	(4,679)	(4,329)	8%
Total accounts receivable, prepayments and deposits	10,201,562	3,286,835	210%
CNS money obligations payable	9,588,374	2,889,524	232%
Other payables to Participants	802,261	190,594	321%
Stamp duty payable	268,236	75,899	253%
Other accounts payable, accruals and other liabilities	448,329	485,054	(8%)
Total accounts payable, accruals and other liabilities	11,107,200	3,641,071	205%

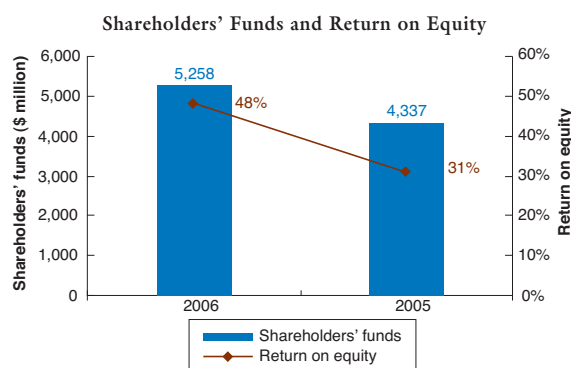
The Group's accounts receivable, prepayments and deposits and accounts payable, accruals and other liabilities mainly comprised CNS money obligations receivable and payable and other receivables from and payables to Exchange and Clearing Participants.

The significant increase in CNS money obligations receivable and payable in 2006 was mainly due to the increase in the level of Cash Market activities at the end of 2006 compared with the end of 2005. Similarly, other receivables from Participants (mainly transaction levy, stamp duty and fees receivable), other payables to Participants (mainly cash marks received from Participants) and stamp duty payable to the Government all recorded a considerable increase.

(E) Shareholders' funds and return on equity

Shareholders' funds as at 31 December 2006 increased by \$921 million to \$5,258 million (2005: \$4,337 million, as restated). The increase was mainly attributable to a \$839 million increase in retained profit before transfers to/from designated reserves and a \$48 million increase in revaluation reserves. Share capital, share premium and employee share-based compensation reserve in aggregate rose by \$34 million mainly due to share options exercised and employee share-based compensation benefits recognised during 2006 of \$55 million, but partly offset by the purchase of shares held for the Share Award Scheme during the year of \$21 million.

Return on equity rose from 31 per cent in 2005 to 48 per cent in 2006 as profit attributable to shareholders increased.



Return on equity achieved record high due to the record high profit in 2006.

Liquidity, Financial Resources and Gearing

Working capital rose by \$914 million or 27 per cent to \$4,271 million as at 31 December 2006 (2005: \$3,357 million). The increase was primarily due to the profit generated during the year of \$2,519 million and the proceeds from issuing shares upon the exercise of employee share options less shares purchased for the Share Award Scheme of \$10 million, which was partly offset by payment of the 2005 final dividend of \$681 million and 2006 interim dividend of \$1,000 million, and the increase in other net current assets of \$66 million.

Although the Group has consistently maintained a very liquid position, banking facilities have nevertheless been put in place for contingency purposes. As at 31 December 2006, the Group's total available banking facilities amounted to \$1,558 million (2005: \$1,608 million), of which \$1,500 million (2005: \$1,500 million) represented repurchase facilities to augment the liquidity of the Margin Funds.

Borrowings of the Group have been rare and are mostly event driven, with little seasonality. As at 31 December 2006 and 31 December 2005, the Group had no bank borrowings, and therefore had zero gearing.

As at 31 December 2006, 97 per cent (2005: 99 per cent) of the Group's cash and cash equivalents (comprising cash on hand, bank balances and time deposits within three months of maturity when acquired) were denominated in HKD or USD.

Charges on Assets

None of the Group's assets was pledged as at 31 December 2006 and 31 December 2005.

Exposure to Fluctuations in Exchange Rates and Related Hedges

Details of the Group's exposure to fluctuations in exchange rates and related hedges are included in note 48(a)(i) – Foreign exchange risk to the consolidated accounts of this Annual Report.

Contingent Liabilities

Details of contingent liabilities are included in note 42 to the consolidated accounts of this Annual Report.