Hang Seng made solid progress in the first half of 2006, supported by a buoyant local economy.

Steps to expand and diversify our customer base led to increases in total deposits and loan balances. Together with the effects of rising interest rates, these increases underpinned growth in net interest income.

We expanded our wealth management and commercial banking businesses, with good growth in investment services and insurance, trading profit and trade finance.

Operating profit excluding loan impairment charges and other credit risk provisions was HK$6,387 million, an increase of HK$453 million, or 7.6 per cent, compared with the first half of 2005.

Attributable profit after taxation and minority interests was HK$6,190 million, an increase of 2.4 per cent compared with the same period last year which benefited from a large property revaluation surplus.

In June we undertook our first-ever US dollar subordinated notes offering. The US$450 million issue has further strengthened our capital base for future business expansion. Along with the HK$2,575 million growth in retained profits, this helped our total capital ratio as at 30 June 2006 reach 14.2 per cent, compared with 12.8 per cent at the end of 2005. Our tier 1 ratio also improved, rising 0.6 percentage points to 11 per cent.

The increase in retained profits was also reflected in shareholders' funds, which, excluding proposed dividends, rose by 6.9 per cent to reach HK$41,615 million. Return on average shareholders' funds was 29 per cent, compared with 29.7 per cent a year earlier.

Earnings per share were up 2.5 per cent at HK$3.24.

The Directors have declared a second interim dividend of HK$1.10 per share. Along with the first interim dividend of HK$1.10 per share, the total distribution for the first half of 2006 is HK$2.20 per share, the same as that in the first half of last year.

Personal Financial Services' operating profit excluding loan impairment charges rose by 7 per cent to HK$3,960 million. This rise reflects a 23.9 per cent increase in wealth management income to HK$2,211 million, driven by strong growth in our securities, life insurance and private banking businesses.

Further efforts to deepen relationships with customers saw Commercial Banking's operating profit excluding loan impairment charges increase by 21.8 per cent to HK$933 million. Total loans were up 9.9 per cent compared with the end of 2005, supported by good growth in commercial loans and trade finance.

Corporate Banking's operating profit excluding loan impairment charges fell by 8.2 per cent to HK$257 million as high levels of liquidity and market competition among lenders continued to exert downward pressure on pricing.

Rising interest rates further compressed spreads on treasury balance sheet management portfolios. This outweighed the encouraging 201.6 per cent growth in net trading income with Treasury recording a 39 per cent decline in operating profit excluding loan impairment charges to HK$444 million.

We increased our service capabilities in mainland China by hiring about 100 new staff and opening a fourth sub-branch in Shanghai. We also recently became the first foreign bank to receive approval to open a branch in Dongguan.

Investments in human resources and increasing rental expenses saw operating costs rise by 8.4 per cent to HK$2,338 million.

Success relies heavily on having a dedicated and talented team. I would like to thank all staff for their commitment to service excellence and strong contributions to business growth.

The outlook for the rest of the year remains broadly positive with interest rate trends likely to have the greatest influence on economic performance. Sustained strong growth on the Mainland should continue to benefit Hong Kong's exports and re-exports, although a small decline in trade activity is likely. Higher interest rates may restrain domestic demand slightly, particularly in the property sector, but consumption will be supported by improvement in the labour market.

Competition in the banking sector will remain keen. We will further build our capabilities in areas such as wealth management, small and medium-sized enterprise services and consumer lending that offer good growth prospects. We will continue to expand our Mainland business and invest in our staff, brand and delivery channels. We will enhance our product and service offerings. This will enable us to build on the progress made in the first half and deliver increasing value for shareholders.

Michael Smith
Chairman
Hong Kong, 31 July 2006