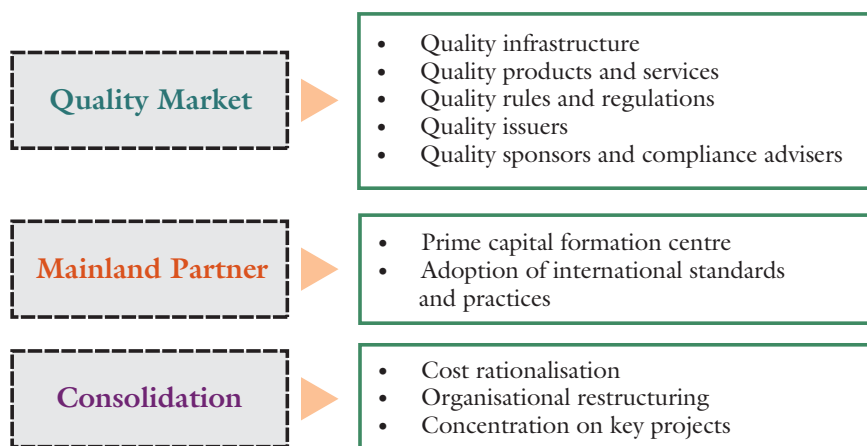


Chief Executive's Review

*Under its Strategic Plan 2004-06, HKEx has successfully built up a world-class marketplace for Hong Kong and Mainland China securities and derivatives products. HKEx has implemented the plan – structured around the overarching themes of **QUALITY MARKET**, **MAINLAND PARTNER**, and **CONSOLIDATION** – and upheld the interest of the investing public, while recording strong financial results. To attain a higher level of performance while continuing to improve market quality, HKEx has refined its mission and adopted a new Strategic Plan for 2007-09 based on the foundation laid down in the past few years.*

STRATEGIC PLAN 2004-06



Guided by the Strategic Plan 2004-06, in its final year of implementation, HKEx made considerable progress during 2006.

Building a Quality Market

We believe that mounting global competition is best countered with a quality market. To sustain continued market growth, HKEx has been monitoring and reviewing prevailing market conditions and promoting appropriate initiatives to improve the businesses and operations of not only HKEx, but the securities market in Hong Kong as a whole.

Quality Infrastructure

Efficient and Reliable Market Systems

An efficient and reliable market infrastructure is indispensable to a quality market. As the operator of the only securities and derivatives marketplace in Hong Kong, HKEx has made ongoing efforts to ensure that its market systems operate at the highest levels. All major trading, clearing, settlement, and market data dissemination systems achieved 100 per cent operational system uptime in 2006. AMS/3 and CCASS/3 have been highly recognised in the IT industry and have earned a number of awards. HKEx will continue reviewing and improving the system performance to ensure that market demand is being satisfied in an efficient and cost-effective manner at all times.





Technology Upgrade

Given the growing market demand, HKEx upgraded the capacities of HKATS, DCASS and PRS and the AMS/3 OG and MWS hardware in 2006. Further upgrade of these systems and the market surveillance system will be carried out in 2007. In addition, the Non-TCP (Transmission Control Protocol) AMS interfaces will be migrated to the TCP/IP (Internet Protocol) for harmonisation of network protocol this year.

Systems Consolidation

The final phase of implementation of SDNet (a new Optical Ethernet network for the securities and derivatives markets) progressed smoothly, and is to be completed in mid-2007. The roll out of the SDNet infrastructure delivers significant technological improvements as well as financial benefits to our EPs and HKEx. More details are provided in the Information Technology section under the Business Review of this Annual Report.

Grand Opening of the Exchange Trading and Exhibition Hall Complex

The Trading Hall underwent renovation between July 2005 and April 2006 to provide more efficient trading facilities for our EPs. There are 294 dealing desks in the new Trading Hall. In addition, an Exchange Exhibition Hall has been constructed to provide local and overseas visitors with more information on the Hong Kong securities and derivatives markets, and the products and services offered by HKEx. Three newly constructed media booths have been reserved for designated television organisations to broadcast market news, and one other is retained as a common media area. The Exchange Auditorium is also open for use by listed issuers, Exchange and Clearing House Participants, Trading Right Holders and related professional bodies at a cost to hold events such as shareholder meetings, news conferences and seminars. During the period between May and December 2006, about 20,000 people visited the Exchange Exhibition Hall and over 7,000 people attended more than a hundred events held at the Exchange Auditorium.

Enhancements to HKEx's Website

In September 2006, HKEx introduced new features on its website to improve investors' access to the latest listed company documents and the related archives. To ensure that the HKEx website is robust and reliable so that it can discharge its important role as the sole primary information provider of Hong Kong issuers' news, especially under the new regime of no paid announcements, we have strengthened the HKEx Website Disaster Recovery Site, increased the system capacity, and improved the recovery speed and the security arrangements for the HKEx EPS.

Establishment of the Public Viewing Room

In support of the new information dissemination regime, HKEx opened a Public Viewing Room to the public on 8 February 2007. The Public Viewing Room is equipped with four workstations which investors can use to search and view issuers' announcements, notices and other documents on the HKEx website, and to access the SFC website.

Improvements to Trading Environment

HKEx has reduced the minimum securities trading spreads for stocks priced above \$2 and enhanced the selection criteria of designated securities for short selling for the Cash Market. In respect of the Derivatives Market, it has streamlined the approval process for the introduction or discontinuation of stock options and futures and amended the relevant rules to cater for the increased position limits for Stock Options.

Quality Products and Services

Introduction of New Products

HKEx successfully introduced CBBCs in June 2006. HKEx will continue organising educational programmes to familiarise EPs and investors with the new products and the associated risks.

Strengthening of Derivative Warrant Market

To enhance the investing public's understanding of derivative warrants, HKEx introduced a new web-based DWRC in May 2006 to offer investors easy access to derivative warrant information for educational and reference purposes, and later amended its Main Board Listing Rules in response to the SFC's proposed "Six-Point Plan" for enhancing and strengthening our derivative warrants market. Delayed intra-day trading information on the entire range of securities and derivative products has also been made available on the HKEx website.

Expansion of CCASS Services

Effective January 2006, a series of improvements to nominee services have been implemented with a view towards improving service levels. More details are provided in the Clearing section under the Business Review of this Annual Report. To accommodate the active IPO market, HKEx will continue to promote eIPOs to improve market efficiency.

Review of Fee Structure

Since 2004, HKEx has implemented a series of fee reductions/abolitions enabling investors and market participants to enjoy substantial saving in transaction costs. In 2006, the scrip fee on deemed book close dates was eliminated effective 1 January, waiver of Short Message Service fees for IP Account Holders who opt for the service was further extended until June 2007, and the discounted monthly fee of \$80 per device for Mainland users of HKEx's real-time securities trading information (including a waiver of the regular monthly subscription fee for the futures data package of \$25 per device) was extended to June 2008.

Risk Management Measures

In November 2006, HKEx successfully completed the FSTB-led Sector-wide Market Contingency Rehearsal Exercise which provided an opportunity to test the market's response to high impact issues with cross-market implications which might undermine the financial stability of Hong Kong. As part of its corporate mission, HKEx will continue monitoring the existing risk management regime to ensure that risks across HKEx are always under appropriate control.

Quality Rules and Regulations

Higher Efficiency and Effectiveness

In 2006, measures continued to improve the effectiveness and efficiency of the work of the Listing Division. These measures included the reorganisation of the Listing Division, recruitment of senior executives to strengthen the management team, the introduction of new workflow procedures and implementation of a comprehensive electronic management information system.

Introduction of New Listing Decision-making Structure

In the first phase of improvement, HKEx introduced a new structure for listing decision-making in mid-2006 to improve the administrative framework for listing decision-making while also preserving checks and balances necessary to minimise and manage regulatory risk.

Review of GEM

GEM has been in operation for more than seven years since its establishment in 1999. HKEx released a Discussion Paper on GEM to invite suggestions on its future development in January 2006 and received 16 responses from various parties including listed companies and market practitioners. Of the 16 submissions, 14 agreed to have a growth company market and seven of which preferred a new alternative market. HKEx continued to work with the SFC on options for GEM's development to take into account respondents' views as well as the interests of the existing GEM-listed companies.

Support of Statutory Backing Initiative

In Hong Kong, the main regulatory requirements for issuers incorporated outside of Hong Kong rest in the Listing Rules which are contractual rather than statutory. In light of this, HKEx strongly supports the Government's proposal to give statutory backing to the more important listing requirements to be administered by the SFC, on three core areas of periodic financial reporting, disclosure of price-sensitive information and notifiable transactions and connected transactions which require shareholders' approval, to enhance our regulatory framework. Upon conclusion of the legislative procedures, HKEx will support the SFC to prepare for the embodiment of certain key Listing Rules into statute by the Government.

Abolition of Paid Advertisements

Efficient and accurate disclosure of corporate information not only helps cultivate confidence among shareholders and investors, but also contributes to a company's good public image and reputation. To achieve this, Main Board issuers will follow the GEM practice of disseminating their corporate information via the HKEx website, instead of publishing paid announcements in newspapers. This decision should result in the lowering of costs for Main Board issuers to maintain their listing on the Exchange.

Quality Issuers

Setting a Good Example

As a listed company, HKEx is committed to achieving the best corporate governance practices, and setting and articulating high standards for listed companies in Hong Kong. In setting our governance standards we have made reference to such sources as "Internal Control and Risk Management – A Basic Framework" published by the HKICPA and "Guidance Notes – A practical guide to good governance" published by the Hong Kong Institute of Chartered Secretaries. We endeavour to deliver a clear account of how we have performed in fulfilling our statutory objectives. In this regard, we have designed a Corporate Governance Section on our corporate website to give our stakeholders a more thorough understanding of our corporate governance framework. We are pleased to have had our efforts recognised in successive years by various local and overseas organisations. More information in this respect is set out in the Corporate Governance Report of this Annual Report.

On-going Review of Corporate Governance Standards

As a regulator, HKEx continues to play a pivotal role in promoting and improving corporate governance standards in Hong Kong. Good corporate governance strengthens investor confidence. To this end, on an ongoing basis HKEx has been reviewing the Listing Rules to ensure that they are aligned with the prevailing best practices and international standards. In 2006, HKEx reviewed listed issuers' progress in implementing the CG Code which took effect on 1 January 2005 and marked a big step forward in bringing governance disclosure in Hong Kong on a par with international standards.

Promoting Good Governance Practices

Recognising the special needs of Mainland issuers, HKEx has organised a series of training programmes on the Hong Kong regulatory framework and requirements to increase issuers' knowledge of corporate governance. In 2006, HKEx co-organised three training programmes and organised a total of eight training sessions in Hong Kong and the Mainland and conducted regular training sessions in the Mainland.

Quality Sponsors and Compliance Advisers

Stringent Regulatory Regime

Timely and accurate financial disclosures are fundamental to investors' confidence. A major responsibility in this respect rests with market professionals, especially sponsors who are key facilitators in bringing new listings to the market. With the aim of raising the overall standard of professionalism in the market, in October 2006 HKEx released the relevant amendments to the Listing Rules to coincide with the SFC's revised licensing regime for sponsors and compliance advisers.

Support Participant Regulation

In 2006, HKEx implemented the Participant Information System ("PIS") which supports the centralised admission of Participants and registration of registered persons and provides search functions to track the record of related Participants and registered persons. Further enhancements are planned to improve efficiency. Moreover, a Participant Financial Resources Surveillance System to be integrated with the PIS will be developed to facilitate the capturing of Participants' finance resources data, monitoring of Participants' financial positions for potential breaches of HKEx rules and regulations, and detecting risky Participants across markets and across products under various market conditions.

Becoming a Mainland Partner

The Mainland has helped propel global growth and provided significant opportunities for the development of Hong Kong's financial market. In its Strategic Plan 2004-06, HKEx proactively aimed to be a Mainland partner by providing Mainland enterprises not only with an effective and well-regarded platform to raise funds and improve their international visibility, but also with know-how on capital formation, good corporate governance practices as well as a regulatory framework compatible with global standards.

Mainland Outreach

Following the establishment of the Beijing Representative Office in late 2003, HKEx staff were deployed to Guangzhou and Shanghai in 2004 to bolster HKEx's presence in the Mainland and to strengthen relationships with the Mainland government authorities and regulatory bodies as well as potential Mainland issuers. In Hong Kong, the Business Development Division was set up in May 2004 to take full responsibility for coordinating with the representative offices in the Mainland on the organisation of conferences and seminars for Mainland business executives and government officials.

Closer Cooperation with Mainland Exchanges and Authorities

In line with the growing number of Mainland enterprises listed or seeking to list in Hong Kong, HKEx has been in close cooperation with the SFC, the CSRC, the Shanghai Stock Exchange and the Shenzhen Stock Exchange on the regulation of these enterprises. The Mainland China Affairs Team was established within the Listing Division to lead HKEx's liaison efforts with the CSRC and other Mainland authorities and to coordinate training programmes on best corporate governance practices for Mainland listed and potential issuers. Recently, an A+H Working Team was formed respectively with the Shanghai Stock Exchange and the Shenzhen Stock Exchange to pursue issues of mutual interests including information disclosures by A+H issuers, sharing of regulatory information between exchanges and provision of training to A+H companies' management teams.

Expansion of Marketing Activities

The listings of Mainland enterprises have helped drive the development of Hong Kong's financial markets in recent years. HKEx had proactively promoted Hong Kong as a listing venue of choice to Mainland enterprises. Mainland marketing activities were not only confined to well-developed cities in the Mainland but also included the fast-growing ones such as Changsha and Xi'an. Recently, HKEx's business development approach was extended to other parts of Asia such as Japan, South Korea, Malaysia, Taiwan, Vietnam and Russia, to as far as the Republic of Kazakhstan, as well as Europe to encourage potential companies to list in Hong Kong. In 2006, HKEx co-organised and conducted a total of 10 conferences and over 180 presentations respectively in the Mainland, overseas and in Hong Kong to promote listing in Hong Kong. HKEx will continue our marketing activities to promote Hong Kong as a premier capital formation centre and an international financial centre.

Consolidation

Since the merger of the exchanges and clearing houses in 2000, HKEx has rationalised costs, streamlined its organisational structure and prioritised projects, with the aim of improving efficiency and maximising Shareholder value. The successful consolidation has strengthened us and helped us better allocate resources to meet challenges ahead.

Streamlining of Organisational Structure and Strengthening of Accountability Regime

In May 2004, HKEx extensively revised its organisational structure, based on its core businesses, namely, listed issuers, intermediaries, investors, infrastructure, and information services, thereby improving overall operational efficiency and reducing operating costs. A succession plan has been formulated to ensure the smooth transition of senior executives, crucial to the stability and reliability of HKEx's operation. The organisational structure has been further refined since to provide senior executives with opportunities to further expand their exposure and enhance their management experience.

Prioritisation of Projects

HKEx focuses its resources as far as possible on initiatives with strategic importance. The list of initiatives is updated and reviewed annually when management prepares the annual operating plan and the budget, and kept under review by the Senior Management Committee throughout the year.

Prudent Cost Control

Prudent cost controls were incorporated in the past three years and operating expenses were maintained at a similar level.

Establishment of MIS

The development of the finance MIS ("FMIS") was completed to strengthen the quality of management information to support HKEx's businesses and operations, formulation of policies and development of business strategies. Further enhancements to the FMIS will continue in 2007.

Strong Corporate Culture and Staff Career Development

The successful implementation of the many business strategies under the Strategic Plan 2004-06 depended very much on teamwork, which is widely promoted within the organisation as one of the key core values. A well-developed human resources development framework is in place to help HKEx retain and attract a high-quality customer-oriented workforce with good market exposure. To demonstrate its commitment to the highest standards of integrity, and to develop a culture of openness, probity and accountability, HKEx has introduced a whistle-blowing policy to encourage employees to raise matters of concern relating to HKEx in a responsible and effective manner. Details are set out in the Corporate Social Responsibility Report of this Annual Report.

Remuneration Review

To achieve its mission and strategic plan, HKEx must retain its team of talented and business-oriented staff. To this end, HKEx commissioned an independent consultant in February 2006 to conduct an overall review of HKEx's remuneration policy and structure with the objective of introducing refinements to the existing remuneration structure to facilitate the fulfillment of the Group's strategic objectives. The review mainly focused on establishing a structured and systematic approach to HKEx's variable compensation, including the annual performance bonus and share award. Results of the review are explained in more detail in the Remuneration Committee Report of this Annual Report.

STRATEGIC PLAN 2007-09

On completion of the Strategic Plan 2004-06, considerable progress has been made on market quality through upgrades to corporate governance and market infrastructure and systems; Hong Kong hosted a number of listings of major state banks and insurance companies, becoming the major capital formation centre in the Asian region; and the organisational structure of HKEx has been streamlined to enhance efficiency and contain costs.

Following the demutualisation of the exchanges in 2000, HKEx is approaching its eighth year as a listed company. We remain committed to acting in the broader interests of the central marketplace by providing quality markets along with products and services that meet the needs of our market participants and investors, and to serving as the premier fund-raising centre for Hong Kong and the Mainland.

While continuous economic growth in the Mainland is envisaged, serving as the primary source of new business to HKEx, there are growing challenges such as the resumption of the Mainland IPO market, the gradual opening up of the Mainland financial and securities markets, the gradual liberalisation of Renminbi, and the consolidation and formation of alliances among overseas exchanges.

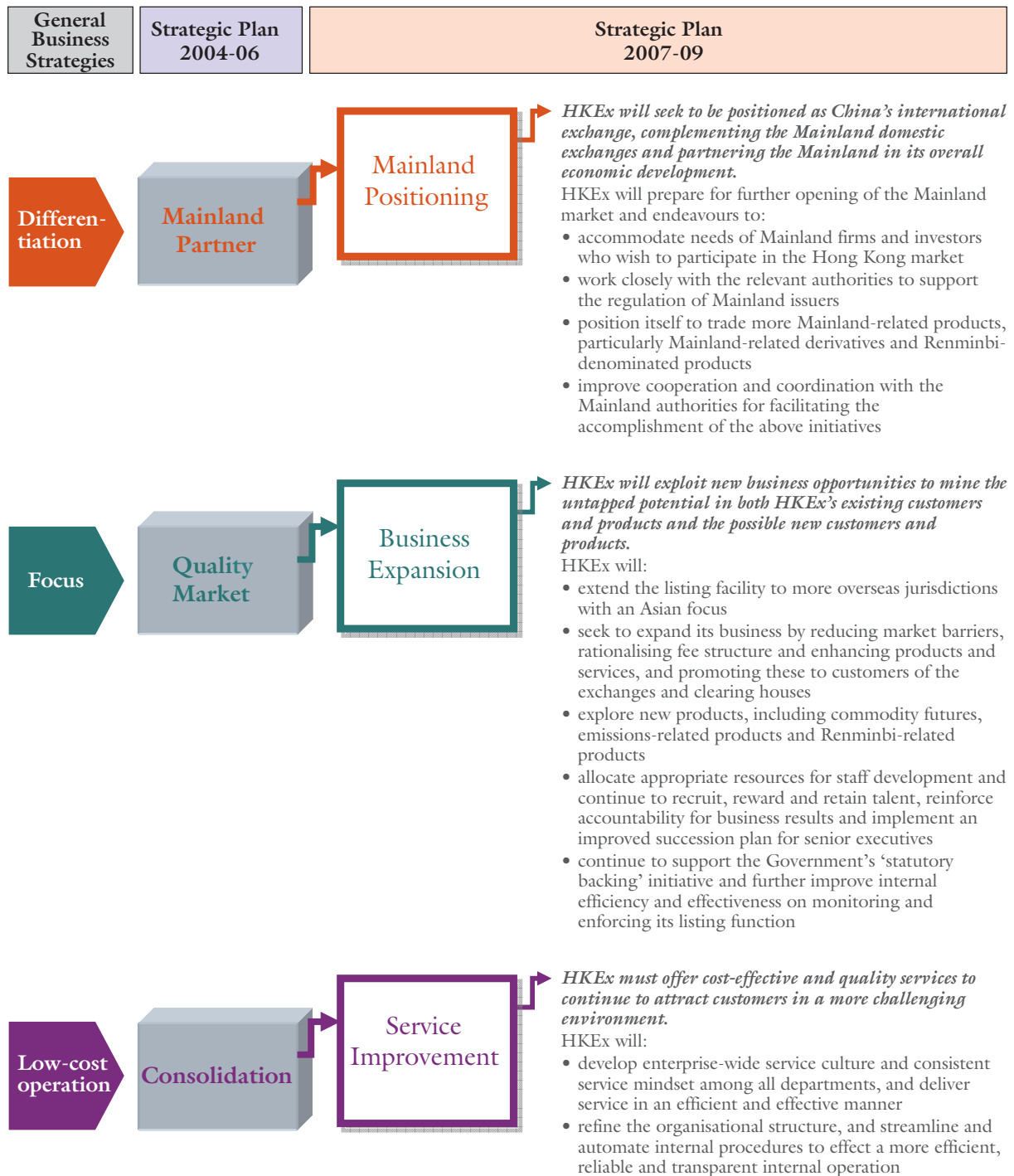
We believe that the present scale of the Hong Kong market provides a platform for a new stage of growth. Accordingly, HKEx has adopted a new mission statement which lays down the direction for the Group's future development.

In line with its new mission and growth strategy, HKEx has mapped out a Strategic Plan 2007-09 which is built on the foundation of the previous plan, but which takes a broader view on business development to cover not only the Mainland but also other areas in Asia. HKEx adopted the three major themes, **MAINLAND POSITIONING**, **BUSINESS EXPANSION** and **SERVICE IMPROVEMENT** for the Strategic Plan 2007-09 with the following key objectives:

- to further strengthen HKEx's Mainland positioning, including capturing more Mainland-related listings, trading more Mainland-related products and engaging more Mainland-related participants and investors;
- to expand HKEx's business into new areas, including developing an Asian focus and diversifying into new product types;



- to become a more business-orientated organisation with accountability for business results more directly assigned to senior management, and market mechanisms and procedures that better facilitate business flow; and
- to improve HKEx's service offering, and to reinforce our internal infrastructure to support improved service delivery.



Support from the Government, the SFC and other professional and industrial associations will be crucial to the success of these business strategies. We will continue to closely communicate and work hard with our stakeholders in the implementation of the new strategic plan.

HKEx has already begun implementation of its new strategic plan.

Widening Issuer Base

To facilitate overseas issuers' access to the Hong Kong market, the Exchange has already accepted Australia and British Columbia, Canada as approved jurisdictions of incorporation for the purposes of primary and secondary listing. Guidance applicable to issuers from other overseas jurisdictions has been issued. Details are set out in the Listing section under the Business Review of this Annual Report.

Broadening Product Base

To meet the varying needs of different types of investors, HKEx is seeking qualified consultants to study the feasibility of trading of commodities derivatives and emissions-related products in Hong Kong. HKEx will continue to explore other new products such as Mainland-related products, including Renminbi futures products.

Expanding Business

HKEx is working on improvement of the trading rights regime. Details are set out in the Cash Market section under the Business Review of this Annual Report. HKEx will continue its effort to address the barriers to securities and derivatives market trading. In this regard, we are supportive of the proposal to reduce/abolish the stamp duty. We will also continue reviewing our fee structure to seek further refinements in a bid to counter increasing competition from other exchanges, to attract over-the-counter trades, and to bring benefits to our EPs and ultimately to investors.

Development of Third Party Clearing

Third Party Clearing ("TPC") is a relatively new concept in the Hong Kong securities market but it is already well-established in major securities markets in the US, the UK and Europe. HKEx plans to introduce TPC to the securities market this year to help ensure that the securities clearing infrastructure in Hong Kong conforms to international standards and is in line with developments in other major financial markets.

Improving Service

In early 2007, HKEx introduced new features to its SSA to provide a more user-friendly customer interface and timely information to account users. Further enhancements such as relaxation of the restriction on the number of SSAs will be introduced in the middle of this year. Details of the enhancements are set out in the Clearing section under the Business Review of this Annual Report.

HKEx will continue reviewing its process for monitoring listed companies and conduct a feasibility study on further improving the MIS and automating internal processes for the Listing Division.

In February 2007, following the appointment of Mr Gerald Greiner to succeed Mr Patrick Conroy as the Chief Operating Officer, the organisational structure was further streamlined. Apart from classifying HKEx's business and operational functions under the Primary Market, Secondary Market and Support Services, the Administration and the Finance support services have been consolidated to improve synergies between the purchase and payment cycles and the provision of administrative services within HKEx. The organisation structure up to 9 February 2007 and the current one are depicted on page 40 of this Annual Report.

One of the key initiatives in our new three-year strategic plan is to consolidate HKEx's various offices and data centres.

APPRECIATION

I am greatly indebted to my colleagues, for it is very much the result of their commitment, diligence, professionalism and excellent teamwork that made 2006 a successful year for HKEx. I want to thank them for the important part they play in HKEx's continued success. I would like to take this opportunity to thank Mr Patrick Conroy, who retired as HKEx's Chief Operating Officer in February this year, for his contributions to HKEx over the past three and a half years, and also to welcome his successor, Mr Gerald Greiner, who joined HKEx as the Deputy Chief Operating Officer and the Head of the Exchange Division on 17 May 2004. He is also the Chief Executive of SEHK and HKFE, and a director of various subsidiaries of HKEx. Prior to joining HKEx, Mr Greiner was the senior director of the Supervision of Markets Division in the SFC.

Additionally, I would like to extend a warm welcome to Mr Ronald Arculli, who took the chair of the Board in April 2006, and our other new Directors, either appointed or elected to the Board during the year. Our Board members contribute significantly to HKEx's achievements, offering guidance, advice and support that are of great value to the Group and the capital markets of Hong Kong. I acknowledge with a deep sense of gratitude their contributions and invaluable advice.

It has been my honour to have been the Chief Executive of HKEx since 2003, and to have witnessed progress in our evolution as a world-class marketplace for Hong Kong and Mainland China securities and derivatives products. I am delighted and privileged to be given the opportunity to continue serving HKEx for another two years. I would particularly like to pay special tribute to our ex-Chairman, Mr Charles Lee, for his insightful guidance and unwavering support in the past few years. I have also immensely enjoyed working with my fellow Board members and colleagues. In the days ahead, my team and I will use our best endeavour to work together for the further growth of HKEx and the betterment of Hong Kong's financial market.

CHOW Man Yiu, Paul
Director and Chief Executive
Hong Kong, 8 March 2007