

Directors' Report

The Directors are pleased to submit their report together with the audited financial statements of SCMP Group Limited (the "Company") and its subsidiaries (collectively the "Group") for the year ended 31 December 2006.

PRINCIPAL ACTIVITIES AND SEGMENT INFORMATION

The Company is an investment holding company. The principal activities of the Group during the year comprised the publishing, printing and distribution of the *South China Morning Post*, *Sunday Morning Post* and other print and digital publications. The Group was also involved in video and film post-production, property investment and music publishing through its subsidiaries.

An analysis of the Group's performance for the year by business segment is set out in note 5 to the financial statements.

MAJOR SUPPLIERS AND CUSTOMERS

During the year, whilst the Group purchased more than 30% of its goods from its five largest suppliers, sales to the five largest customers accounted for less than 30% of the total sales for the year.

The percentages of purchases and sales for the year attributable to the Group's major suppliers and customers are as follows:

Purchase	
– the largest supplier	18.9%
– five largest suppliers combined	58.0%
Sales	
– the largest customer	3.5%
– five largest customers combined	15.4%

Brandes Investment Partners, L.P., a substantial shareholder of the Company, informed the Company that as at 31 December 2006, it held 1.6% of the issued capital of the holding company of the above-mentioned largest supplier.

Save from the above and as far as the Directors are aware, neither the Directors, their associates, nor shareholders who own more than 5% of the Company's share capital had any interest in the five largest suppliers and customers.

FINANCIAL RESULTS

The profit of the Group for the year and the state of affairs of the Company and the Group as at 31 December 2006 are set out in the financial statements on pages 75 to 79.

DIVIDEND

During the year, an interim dividend of HK6 cents per share was paid. The Directors recommend the payment of a final dividend of HK13 cents per share in respect of the year ended 31 December 2006 to the shareholders whose names appear on the register of members of the Company on Friday, 25 May 2007.

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FIVE YEAR FINANCIAL SUMMARY

The summary of the results and of the assets and liabilities of the Group for the last five financial years is set out on page 120.

PROPERTY, PLANT AND EQUIPMENT AND INVESTMENT PROPERTIES

Movements in the property, plant and equipment and details of investment properties of the Group are disclosed in note 6 and note 7 to the financial statements, respectively.

SUBSIDIARIES

Particulars of the Company's principal subsidiaries as at 31 December 2006 are set out in note 31 to the financial statements.

ASSOCIATES

Particulars of the Group's principal associates as at 31 December 2006 are set out in note 31 to the financial statements.

BANK LOANS

Particulars of bank loans of the Group as at the balance sheet date are set out in note 17 to the financial statements.

SHARE CAPITAL

Details of the authorised and issued share capital of the Company are set out in note 15 to the financial statements.

DISTRIBUTABLE RESERVES

Details of the reserves of the Company available for distribution to shareholders as at 31 December 2006 are set out in note 16 to the financial statements.

PRE-EMPTIVE RIGHTS

There is no provision for pre-emptive rights under the Company's Bye-Laws or the laws in Bermuda which would oblige the Company to offer new shares on a pro rata basis to existing shareholders.

RESERVES

Movements in the reserves of the Company are disclosed in note 16 to the financial statements. Movements in the reserves of the Group are disclosed in the consolidated statement of changes in equity on page 77.

CHARITABLE DONATIONS

During the year, the Group made charitable donations totaling HK\$888,560.

Directors' Report

DIRECTORS

The Directors who held office during the year and up to the date of this report were:

Executive Directors

Mr. Kuok Khoon Ean Chairman
Ms. Kuok Hui Kwong

Non-executive Directors

Mr. Roberto V. Ongpin Deputy Chairman
Tan Sri Dr. Khoo Kay Peng
Mr. Robert Ng Chee Siong

Independent Non-executive Directors

The Hon. Ronald J. Arculli
Mr. Peter Lee Ting Chang
Dr. The Hon. Sir David Li Kwok Po

In accordance with Bye-Law 99 of the Company's Bye-Laws, Tan Sri Dr. Khoo Kay Peng, Mr. Peter Lee Ting Chang and Mr. Robert Ng Chee Siong shall retire by rotation and are eligible for re-election at the forthcoming Annual General Meeting of the Company.

Subsequent to the date of this report, the Board approved the appointment of Mr. Wong Kai Man as an Independent Non-executive Director to take effect from 2 April 2007. In accordance with Bye-Law 102(B) of the Company's Bye-Laws, Mr. Wong shall hold office until the conclusion of the forthcoming Annual General Meeting of the Company and is eligible for re-election at the meeting.

DIRECTORS' INTERESTS IN SHARES, UNDERLYING SHARES AND DEBENTURES

As at 31 December 2006, the Directors of the Company had the following interests or short positions in shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) as recorded in the register required to be kept under Section 352 of the SFO or as notified to the Company and the Hong Kong Stock Exchange (the "Stock Exchange") pursuant to the Model Code for Securities Transactions by Directors of Listed Companies (the "Model Code") or as otherwise notified to the Company:

Name of Director	Ordinary shares of the Company		
	Capacity/ Nature of interests	Number of shares held	Approximate % of issued share capital *
Mr. Kuok Khoon Ean (Note 1)	Corporate	340,000	0.022%
Tan Sri Dr. Khoo Kay Peng (Note 2)	Corporate	27,243,145	1.745%
Dr. The Hon. Sir David Li Kwok Po	Personal	4,778,000	0.306%

Notes:

- The interests in the 340,000 shares are in respect of deemed corporate interests held by Mr. Kuok Khoon Ean through Allerlon Limited, which is wholly owned by Mr. Kuok and his spouse.
- In the notification filed by Tan Sri Dr. Khoo Kay Peng with the Company and the Stock Exchange on 27 December 2006, Dr. Khoo held 28,831,145 shares (representing approximately 1.847% of the Company's issued share capital). In the notification filed by Dr. Khoo with the Company and the Stock Exchange on 3 January 2007, Dr. Khoo held 27,233,145 shares (representing approximately 1.745% of the Company's issued share capital). The Company has been notified informally that as at 31 December 2006, Dr. Khoo held 27,243,145 shares (representing approximately 1.745% of the Company's issued share capital), which change was included in Dr. Khoo's notification filed on 3 January 2007. The interests in the 27,243,145 shares are in respect of deemed corporate interests held by Dr. Khoo through (i) MUI Media Ltd. as to 11,093,145 shares and (ii) Bonham Industries Limited as to 16,150,000 shares. As at 31 December 2006, Dr. Khoo was deemed to have an interest in approximately 32.35% of the issued capital of Pan Malaysian Industries Berhad which in turn holds approximately 46.56% of the issued capital of Malayan United Industries Berhad ("MUI Berhad"). MUI Media Ltd. is wholly owned by MUI Berhad. As at 31 December 2006, Dr. Khoo held 99.9% of the entire issued capital of Bonham Industries Limited.

* Approximate percentage calculated based on the 1,560,945,596 ordinary shares of the Company in issue as at 31 December 2006.

Directors' Report

All the interests stated above represent long positions in the shares of the Company.

Save as stated above, none of the Directors (including their spouses and children under 18 years of age) had been granted by the Company or had exercised any rights to subscribe for shares or debentures of the Company or any of its associated corporations during the year.

Apart from the aforesaid, as at 31 December 2006, none of the Directors of the Company had any interest or short position in any shares, underlying shares and debentures of the Company or any associated corporations (within the meaning of the SFO) as recorded in the register required to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code.

SUBSTANTIAL INTERESTS IN SHARE CAPITAL

As at 31 December 2006, the following persons (other than Directors of the Company) had interests or short positions in the shares and underlying shares of the Company representing 5% or more of the voting power at any general meeting of the Company as recorded in the register required to be kept under Section 336 of the SFO:

Name	Capacity/ Nature of interests	Number of ordinary shares held	Approximate % of issued share capital *
Kerry Media Limited (Note 1)	Beneficial owner	524,730,000	33.62%
Kerry 1989 (C.I.) Limited (Note 2)	Interest of controlled corporations	525,036,000	33.64%
Kerry Holdings Limited (Notes 3 & 4)	Interest of controlled corporations	594,576,000	38.09%
Kerry Group Limited (Note 4)	Interest of controlled corporations	594,576,000	38.09%
Silchester International Investors Limited (Notes 5 & 7)	Investment manager	203,005,000	13.01%
Brandes Investment Partners, L.P. (Note 5)	Investment manager	177,865,278	11.39%
The Northern Trust Company (Note 6)	Approved lending agent	109,705,447	7.03%
Harris Associates L.P. (Notes 5 & 8)	Investment manager	101,304,000	6.49%
Sprucegrove Investment Management Ltd. (Notes 5 & 9)	Investment manager	88,163,000	5.65%

Notes:

1. The interests in the 524,730,000 shares held by Kerry Media Limited are duplicated in the respective interests reported above for Kerry 1989 (C.I.) Limited, Kerry Holdings Limited and Kerry Group Limited.
2. The interests in the 525,036,000 shares held by Kerry 1989 (C.I.) Limited are duplicated in the respective interests reported above for Kerry Holdings Limited and Kerry Group Limited.
3. The interests in the 594,576,000 shares held by Kerry Holdings Limited are duplicated in the interests reported above for Kerry Group Limited.
4. The Company has been notified informally that as at 31 December 2006, Kerry Group Limited and Kerry Holdings Limited were interested in 606,372,000 shares (representing approximately 38.85% of the Company's issued share capital) and this increase in shareholding was not required to be disclosed under Part XV of the SFO.
5. Investment manager acting on behalf of clients and not connected with the Company.
6. Approved lending agent and not connected with the Company.

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7. Silchester International Investors Limited has informally notified the Company that as at 31 December 2006, it held 215,251,000 shares (representing approximately 13.79% of the Company's issued share capital) and this increase in shareholding was not required to be disclosed under Part XV of the SFO.
8. Harris Associates L.P. has informally notified the Company that as at 31 December 2006, it held 103,676,000 shares (representing approximately 6.64% of the Company's issued share capital) and this increase in shareholding was not required to be disclosed under Part XV of the SFO.
9. Sprucegrove Investment Management Ltd. has informally notified the Company that as at 31 December 2006, it held 84,456,000 shares (representing approximately 5.41% of the Company's issued share capital) and this decrease in shareholding was not required to be disclosed under Part XV of the SFO.

* *Approximate percentage calculated based on the 1,560,945,596 ordinary shares of the Company in issue as at 31 December 2006.*

All the interests stated above represent long positions in the shares of the Company.

Save as stated above, as at 31 December 2006, the Company had not been notified of any interests and short positions in the shares and underlying shares of the Company which had been recorded in the register required to be kept under Section 336 of the SFO.

SHARE OPTION SCHEMES

(1) Summary of terms

It is a part of the Group's policy to reward employees for their past contributions to the Group and motivate them to optimize their future contributions and enable the Group to attract and retain individuals with experience and ability.

The Company has two share option schemes. A share option scheme (the "Current Scheme") was approved by shareholders on 27 October 1997 (the "Effective Date") and was amended with shareholders' approval on 6 November 2000 and further amended at the annual general meeting held on 29 May 2002 in conformity with the amended Chapter 17 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"). The Current Scheme will expire on 27 October 2007. Another share option scheme (the "New Scheme") was approved at the annual general meeting of the Company held on 25 May 2006 (the "Adoption Date").

Under the Current Scheme and the New Scheme (together as "the Schemes"), the Board of Directors of the Company (the "Board") may grant options to subscribe for shares of the Company to any full-time employee or Executive Director of the Company or any of its subsidiaries (the "Executive").

The subscription price of the options pursuant to the Schemes shall not be less than whichever is the highest of: (i) the nominal value of a share of the Company; (ii) the closing price of a share of the Company as stated in the daily quotation sheet of the Stock Exchange on the date of the Board's approval of grant of the option (the "Offer Date"); and (iii) the average of the closing prices of a share of the Company in the Stock Exchange's daily quotation sheets for the five business days immediately preceding the Offer Date. An offer of the grant of an option shall remain open for acceptance by the Executive concerned at no consideration for a period of 28 days from the date on which an option is offered to the Executive.

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Under the Current Scheme, no option may be exercised earlier than one year after it has been granted or later than ten years after the Effective Date, i.e. 27 October 2007. The remaining life of the Current Scheme is up to 27 October 2007. Hence, no option can be granted under the Current Scheme on or after 27 October 2006. The maximum number of shares of the Company which may be issued upon exercise of all options to be granted under the Current Scheme may not exceed 10% of the shares of the Company in issue as at 29 May 2002. As at the date of this report, the Directors have granted options pursuant to the Current Scheme to subscribe for a total of 22,867,500 shares, of which options to subscribe for a total of 1,435,000 shares and a total of 14,769,500 shares have so far exercised and lapsed, respectively. No options have been cancelled under the Current Scheme since its adoption by shareholders. Consequently, as at the date of this report, options to subscribe for an aggregate of 6,663,000 shares remain outstanding under the Current Scheme, representing approximately 0.43% of the issued share capital of the Company as at the date of this report.

Under the New Scheme, no option may be exercised earlier than one year after it has been granted or later than ten years after the Adoption Date, i.e. 25 May 2016. The remaining life of the New Scheme is up to 25 May 2016. The maximum number of shares of the Company which may be issued upon exercise of all options to be granted under the New Scheme (when aggregated with shares to be issued upon exercise of options granted under any other share option scheme of the Company) may not exceed 10% of the shares of the Company in issue as at 25 May 2006. As at the date of this report, the total number of shares available for issue under the New Scheme was 147,996,559, representing approximately 9.48% of the issued share capital of the Company as at the date of this report.

The maximum number of shares of the Company issued and to be issued upon exercise of the options granted to any one Executive (including exercised and outstanding options) under the Schemes or any one of them in any 12-month period shall not exceed 1% of the shares of the Company in issue from time to time.

None of the substantial shareholders of the Company has been granted any share option under the Schemes. None of the suppliers of goods or services to the Group has been granted any share option under the Schemes. No participant of the Current Scheme or the New Scheme has been granted share options in excess of the maximum entitlement of each participant.

(2) Movements of options granted

The outstanding shares in respect of options granted under the Current Scheme as at 31 December 2006 are summarised below:

	Number of shares in respect of options granted
Outstanding at 1 January 2006	7,353,000
Granted during the year	–
Exercised during the year	–
Cancelled during the year	–
Lapsed during the year	(560,000)
Outstanding at 31 December 2006	6,793,000

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Details of the movements during the year in the share options granted under the Current Scheme are as follows:

(i) Options granted to Directors

None of the Directors of the Company has been granted any share option under the Current Scheme.

(ii) Options granted to employees

Date of grant	Exercise period	Exercise price/share HK\$	Number of shares involved in the options				
			Outstanding at 01/01/2006	Granted during the year	Exercised during the year	Lapsed during the year	Outstanding at 31/12/2006
02/08/1999	02/08/2000 – 27/10/2007	5.00	1,092,500	–	–	–	1,092,500
11/01/2000	11/01/2001 – 27/10/2007	5.51	880,500	–	–	(140,000)	740,500
20/04/2000	20/04/2001 – 27/10/2007	6.05	3,260,000	–	–	(270,000)	2,990,000
28/06/2001	28/06/2002 – 27/10/2007	4.95	420,000	–	–	–	420,000
23/09/2003	23/09/2004 – 27/10/2007	3.90	1,700,000	–	–	(150,000)	1,550,000
Total			7,353,000	–	–	(560,000)	6,793,000

During the year, no share option was granted, exercised, cancelled or lapsed under the New Scheme. No share option was outstanding under the New Scheme as at 31 December 2006.

DIRECTORS' INTEREST IN COMPETING BUSINESS

Mr. Robert Ng Chee Siong, a Non-executive Director of the Company, informed the Board that as at 31 December 2006, he held interests and/or directorships in companies engaged in businesses of property investment, development and management and operation of hotels in Hong Kong.

The Board is satisfied that property investment, development and management and operation of hotels do not form part of the Company's core business. Publishing remains the core business and focus of the Company.

Save as stated above, none of the Directors of the Company has any interest in a business which competes or is likely to compete with the business of the Group during the year.

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DIRECTORS' INTERESTS IN CONTRACTS

No contract of significance in relation to the Group's business to which the Company or any of its subsidiaries was a party and in which a Director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

DIRECTORS' SERVICE CONTRACTS

No Director proposed to be re-elected at the forthcoming Annual General Meeting has an unexpired service contract with the Group, which is not determinable by the Group within one year without payment of compensation (other than statutory compensation).

MANAGEMENT CONTRACTS

No contract concerning the management and administration of the whole or any substantial part of the business of the Company was entered into or existed during the year.

DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBENTURES AS AT 31 DECEMBER 2006

Save as disclosed herein, at no time during the year was the Company or any of its subsidiaries a party to any arrangement to enable the Directors to acquire benefits by means of acquisition of shares in, or debentures of, the Company or any other body corporate.

CONNECTED TRANSACTIONS

During the year, the Company and its subsidiaries had certain transactions which constituted connected transactions under Chapter 14A of the Listing Rules.

South China Morning Post Publishers Limited ("SCMPP"), a subsidiary of the Company, had the following connected transaction and continuing connected transactions with subsidiaries of Kerry Group Limited, a substantial shareholder of the Company as defined in the Listing Rules. Details of the transactions are set out below:

A Transactions in respect of the financial year ended 31 December 2006

(1) Connected Transaction

An agreement dated 12 April 2006 made between SCMPP and Kerry Properties Limited ("Kerry Properties") which is a subsidiary of Kerry Group Limited, whereby SCMPP was engaged to publish three issues of "The Dress Circle" magazine for Kerry Properties.

Under the above agreement A(1), the service fee was determined based on the editorial cost, project management cost, printing and other production costs involved. A maximum total service fee of HK\$1,821,000 (HK\$607,000 for each of the three issues) was payable by Kerry Properties to SCMPP.

The above agreement A(1) has been fully performed with three issues of the magazine published in May 2006, September 2006 and February 2007. The aggregate amount received or receivable pursuant to the agreement amounted to HK\$1,794,384.

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(2) Continuing Connected Transactions

(i) Advertising Services

- (a) An agreement dated 23 December 2005 made between SCMPP and Kerry Holdings Limited ("Kerry Holdings"), a subsidiary of Kerry Group Limited, whereby SCMPP agreed to provide classified advertising and corporate notices services to Kerry Holdings and Kerry Group Limited and its subsidiaries ("Kerry Group") for a term of one year from 1 January 2006 to 31 December 2006.
- (b) An agreement dated 23 December 2005 made between SCMPP and Kerry Holdings whereby SCMPP agreed to provide display advertising services to Kerry Holdings and other companies in the Kerry Group for a term of one year from 1 January 2006 to 31 December 2006.

The service fees payable pursuant to the above agreements A(2)(i)(a) and A(2)(i)(b) were payable in cash or by cheque by the end of the month following the month in which SCMPP issued invoices.

The aggregate amount of service fees received or receivable pursuant to the above agreements A(2)(i)(a) and A(2)(i)(b) for the financial year ended 31 December 2006 amounted to HK\$4,330,456.

(ii) Publication Services

An agreement dated 14 October 2004 made between SCMPP and Kerry Properties, whereby SCMPP was engaged to publish four issues of "The Dress Circle" magazine for Kerry Properties. The agreement has been fully performed with four issues of the magazine published in December 2004, April 2005, August 2005 and January 2006.

The fee payable pursuant to the above agreement A(2)(ii) was payable by the end of the month following the month in which SCMPP issued invoices.

The total amount received pursuant to the above agreement A(2)(ii) was HK\$1,999,405, of which HK\$498,305, HK\$989,100 and HK\$512,000 were received for the financial years ended 31 December 2004, 2005 and 2006, respectively.

In accordance with Rule 14A.37, Chapter 14A of the Listing Rules, the Directors (including Independent Non-executive Directors) of the Company have reviewed the above continuing connected transactions (the "Transactions") and confirm that the Transactions were entered into:

- (a) in the ordinary and usual course of business of the Group;
- (b) on normal commercial terms; and
- (c) in accordance with the relevant agreements on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

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The Auditors of the Company have also reviewed the Transactions and confirmed to the Directors in writing that:

- (a) the Transactions have been approved by the Board of Directors of the Company;
- (b) the Transactions are in accordance with the pricing policy of the Group;
- (c) the Transactions have been entered into in accordance with the relevant agreements governing the Transactions; and
- (d) the aggregate amount received under the above agreements A(2)(i)(a) and A(2)(i)(b) for the financial year ended 31 December 2006 does not exceed the annual cap of HK\$7 million as stated in the Company's announcement dated 23 December 2005.

B Transactions in respect of the financial year ending 31 December 2007

(1) Connected Transaction

An agreement dated 12 January 2007 made between SCMPP and Kerry Properties, whereby SCMPP will publish three issues of "The Dress Circle" magazine for Kerry Properties.

Under the above agreement B(1), the service fees were determined based on the editorial cost, project management cost, printing and other production costs involved. A maximum total service fee of HK\$1,821,000 (HK\$607,000 for each of the three issues) will be payable by Kerry Properties to SCMPP.

(2) Continuing Connected Transactions

- (a) An agreement dated 13 December 2006 made between SCMPP and Kerry Holdings whereby SCMPP agreed to provide classified advertising and corporate notices services to Kerry Holdings and other companies in the Kerry Group for the period from 1 January 2007 to 31 December 2007.
- (b) An agreement dated 13 December 2006 made between SCMPP and Kerry Holdings whereby SCMPP agreed to provide display advertising services to Kerry Holdings and other companies in the Kerry Group for the period from 1 January 2007 to 31 December 2007.
- (c) An agreement dated 13 December 2006 made between SCMPP and the advertising agent of Shangri-La International Hotel Management Limited, an indirect wholly-owned subsidiary of Shangri-La Asia Limited which is an associate (as defined in the Listing Rules) of Kerry Group Limited, whereby SCMPP agreed to provide advertising services to Shangri-La hotels and resorts for the period from 1 January 2007 to 31 December 2007.

The service fees payable pursuant to the above agreements B(2)(a) to B(2)(c) are payable in cash or by cheque by the end of the month following the month in which SCMPP issued invoices.

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The Company expects that the maximum aggregate amount of service fees receivable under the above agreements B(2)(a) to B(2)(c) for the financial year ending 31 December 2007 to be HK\$7 million as stated in the Company's announcement dated 13 December 2006.

All the above connected transactions and continuing connected transactions have been disclosed in accordance with Rules 14A.32 and 14A.35, Chapter 14A of the Listing Rules, respectively.

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S SHARES

Neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's shares during the year.

VALUATION OF PUBLISHING TITLES

The Company has appointed American Appraisal China Limited (the "Valuer"), an independent valuer, to value two of the Group's publishing titles, *South China Morning Post* and *Sunday Morning Post* (the "Publishing Titles") on an open market basis. The Valuer had valued the Publishing Titles at HK\$4.369 billion as at 31 December 2004. The Directors have adopted the Valuer's valuation in their annual valuation of the Publishing Titles as at 31 December 2006.

The valuation is not reflected in the financial statements as the accounting principles generally accepted in Hong Kong and the accounting policies of the Company require publishing titles with indefinite useful lives to be stated at cost less impairment losses.

CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Board of Directors of the Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as set out in Appendix 10 of the Listing Rules as the code for securities transactions by Directors of the Company. All Directors of the Company have confirmed their compliance with the required standard set out in the Model Code during the year.

CORPORATE GOVERNANCE

The Company is committed to maintaining a high standard of corporate governance. Details of the Company's corporate governance practices are set out in the "Corporate Governance" section of this Annual Report on pages 48 to 55.

AUDITORS

The financial statements have been audited by PricewaterhouseCoopers who retire and, being eligible, offer themselves for re-appointment.

On behalf of the Board
Kuok Khoon Ean
Chairman

Hong Kong, 26 March 2007