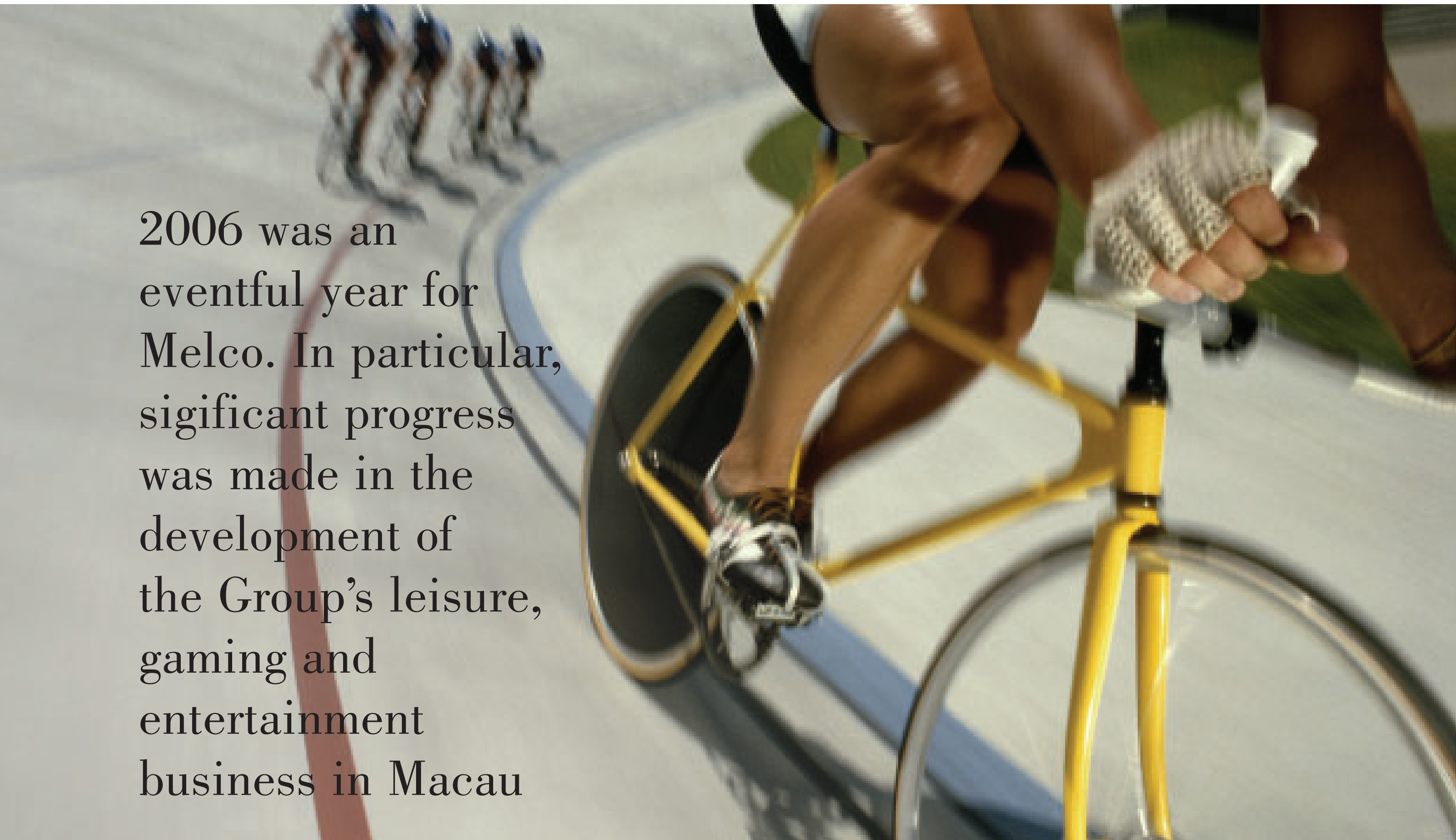
Management Discussion and Analysis



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SIGNIFICANT EVENTS AND DEVELOPMENTS

2006 was an eventful year for Melco. In particular, significant progress was made in the development of the Group's leisure, gaming and entertainment business in Macau.

In March 2006, Melco PBL (our joint venture with PBL) entered into a series of transactions to acquire the last remaining gaming subconcession in Macau from Wynn Resorts (Macau) SA. In October, the acquisition was approved by the Macau Government and Melco PBL Gaming (Macau) Limited formally became one of the six license holders to operate gaming business in Macau.

In November, following a corporate restructuring, all the Melco PBL gaming operations were grouped under Melco PBL Entertainment. In December, Melco PBL Entertainment was listed on NASDAQ by way of an offering of 17.2% of its enlarged share capital (after exercise of greenshoe) in the form of new shares to US investors. Gross proceeds, before deduction of issuance costs, amounted to approximately US$1.32 billion, making it the largest IPO ever launched by an Asian company on NASDAQ and the fourth largest IPO in the United States in year 2006.

The construction of Melco PBL Entertainment's projects in Macau remains on track. Crown Macau, which primarily caters for high rollers, is scheduled to have its trial opening on 28 April 2007. City of Dreams, a premium integrated urban entertainment resort targeting the mass market, broke ground in 2006 and phase one of the project is expected to complete towards the end of 2008. During the year, various partnerships have been formed with world-renowned companies to operate the facilities at the City of Dreams. These included hotel operators Hyatt International and Hard Rock International and world-class performing company Dragone Entertainment GmbH.

Management Discussion and Analysis

Melco PBL Entertainment entered into a transaction in May 2006 to acquire a site on the waterfront of the Macau Peninsula for the development of its third casino hotel complex targeting the day-trippers. This acquisition is expected to be completed in the third quarter of 2007.

In an initiative to further develop Melco's leisure and entertainment business and to tap the rapid growth of the lottery markets in Asia, particularly China, PAL Development Limited ("PAL") was established as a joint venture company between an indirect wholly-owned subsidiary of Melco and Singapore listed LottVision in September 2006. PAL was initially owned as to 60% by the Group and 40% by LottVision.

Subsequent to the balance sheet date, on 28 March 2007, it was announced that Melco would swap approximately 29.47% of its shareholding in PAL for approximately 28.5% of the enlarged share capital of LottVision after issue of the consideration shares. By virtue of this transaction:

(i) Melco would become the largest single shareholder of LottVision;

(ii) LottVision would own approximately 69.47% of PAL;

(iii) Melco's effective interest in PAL would become approximately 50.33%.

Melco also has a call option to subscribe up to a maximum of 88 million LottVision new shares at S$0.1034 per share and its shareholding in LottVision will increase to approximately 37.4% of the enlarged issued share capital of LottVision following the issue of the consideration shares and upon exercise of the call option in full. Its effective interest in PAL would increase to approximately 56.5% if the call option is exercised in full.

PAL is currently engaged in three main business streams in the lottery space:

(1) Distribution of Lottery Vending Terminals in China;

(2) Provision of Venue Management Consultancy Services to lottery sales outlets in China; and

(3) Provision of technological solutions for interactive lottery games on mobile phones.

FINANCIAL REVIEW

The Group engages in four main business streams, namely (i) Leisure, Gaming and Entertainment, (ii) Technology, (iii) Investment Banking and Financial Services and (iv) Property and Other Investments.

To facilitate the review, the segment information shown in Note 8 to the consolidated financial statements is reproduced below with some minor re-arrangements:

Management Discussion and Analysis

	Year ended 31 Dec 2006 *HK$'000*	Year ended 31 Dec 2005 *HK$'000*
Segment Result: Leisure, Gaming and Entertainment	**(182,072)**	25,224
Segment Result: Technology	**26,336**	33,766
Segment Result: Investment Banking and Financial Services	**49,343**	21,849
Segment Result: Property and Other Investments	**105,588**	47,494
Intra-group eliminations	**(7,945)**	(11,871)
Group operating result	**(8,750)**	116,462
Loss on disposal of subsidiaries	**(12,140)**	–
(Loss) gain on deemed disposal of partial interests in subsidiaries	**(33)**	514,407
Gain on deemed disposal of interests in jointly controlled entities	**3,102,253**	–
Gain on formation of a jointly controlled entity	**20,000**	–
Share of (loss) profit of jointly controlled entities	**(191,835)**	2,234
Unallocated corporate expenses	**(68,257)**	(38,886)
Finance costs	**(85,879)**	(31,747)
Profit before tax	**2,755,359**	562,470
Income tax credit (expense)	**4,622**	(6,010)
Profit for the year	**2,759,981**	556,460
Minority interests	**76,774**	(7,742)
Profit for the year attributable to shareholders	**2,836,755**	548,718

Consolidated operating EBITDA for the Group (excluding the Macau gaming business conducted through Melco PBL Entertainment and its predecessors) amounted to HK$108.8 million for the year ended 31 December 2006 (2005 – HK$64.7 million). According to the financial statements of Melco PBL Entertainment, operating EBITDA of Melco PBL Entertainment amounted to US$13.2 million for the year ended 31 December 2006 (2005 – US$7.4 million).

Management Discussion and Analysis

LEISURE, GAMING AND ENTERTAINMENT

For the year ended 31 December 2006, losses from this segment amounted to HK$182.1 million (2005 – Profit of HK$25.2 million) and are made up of the following:

	Year ended 31 Dec 2006 ***HK$'000***	Year ended 31 Dec 2005 *HK$'000*
Melco PBL – Macau Gaming (prior to October 2006)	**(164,601)**	25,574
Jumbo Kingdom	**1,849**	(350)
Gaming License Bidding Costs	**(19,320)**	–
	(182,072)	25,224

Melco PBL – Macau Gaming (prior to October 2006)

Prior to October 2006, the Macau gaming operations (operated through a joint venture with PBL) was effectively owned as to 60% by the Group and 40% by PBL. Consequently, the results of Melco PBL's Macau operations for the first nine months ended 30 September 2006 were fully consolidated into the Group's financial statements. Effective from 1 October 2006, following a restructuring of the Group and the formal grant of the gaming subconcession by the Macau Government, Melco's effective interest in the joint venture decreased to 50%, resulting in Melco PBL being re-classified as jointly controlled entities. As a result, the attributable results of Melco PBL Entertainment and its subsidiaries for the three months ended 31 December 2006 was shown under "share of losses of jointly controlled entities".

For the first nine months of 2006, Melco PBL's Macau operations recorded a negative contribution of approximately HK$164.6 million, versus a positive contribution of HK$25.6 million for the whole year in 2005. The drastic change was primarily due to the following:

(1) Substantial pre-opening expenses were incurred in respect of Crown Macau and City of Dreams. According to the financial statements of Melco PBL Entertainment, the total pre-opening expenses amounted to approximately US$11.7 million for the full year ended 31 December 2006.

(2) An intangible asset write-off of approximately HK$90.4 million resulting from the termination of Mocha Slots' service agreements with Sociedade de Jogos de Macau, S.A.. These agreements were terminated as a result of Melco PBL acquiring its own gaming subconcession in October 2006.

Management Discussion and Analysis

According to the financial statements of Melco PBL Entertainment, Mocha generated an operating EBITDA of approximately US$13.2 million for the year ended 31 December 2006 (2005 – US$7.4 million). Average number of gaming machines at Mocha (on a time-weighted basis) increased from 634 in 2005 to 937 in 2006 and the gross daily gaming revenue per machine (on a time-weighted basis) decreased from US$229 in 2005 to US$210 in 2006. For the fourth quarter of 2006, this figure reached a record of US$248.

Jumbo Kingdom
Jumbo Kingdom staged a turnaround in 2006 with a positive contribution of HK$1.8 million against a loss of HK$0.4 million in 2005.

Jumbo Kingdom includes the Jumbo and Tai-Pak floating restaurants located in Aberdeen, Hong Kong, and Jumbo's Chua Lam Gourmet Kitchen in Macau. A premier tourist destination and fine-dining establishment, Jumbo Kingdom has continually upgraded its facilities over the past 30 years. In 2003, Jumbo Kingdom carried out a multi-million dollar renovation that transformed it into a modern floating complex for fine dining, sightseeing and cultural attractions, and represents a must-see destination for any visitor to Hong Kong.

Following its renovation in 2003 and an extensive marketing campaign launched to rebuild the brand, Jumbo Kingdom recently won Hong Kong's prestigious "Superbrand 2006/2007" award.

Gaming License Bidding Costs
Together with our joint venture partner PBL, Melco is continually looking to explore gaming opportunities outside Macau. In 2006, Melco, PBL and Eighth Wonders formed a partnership to bid for a gaming license in Singapore. Unfortunately, the bid turned out to be unsuccessful. As a result, our share of the costs involved in the bidding, amounting to approximately HK$19.3 million (2005 – Nil), was written off in 2006.

TECHNOLOGY
Profit from the segment amounted to HK$26.3 million (2005 – HK$33.8 million) and is made up of the following:

	Year ended 31 Dec 2006 ***HK$'000***	Year ended 31 Dec 2005 *HK$'000*
Elixir Technology	**23,707**	32,844
iAsia Technology	**2,669**	963
Others	**(40)**	(41)
	26,336	33,766

Management Discussion and Analysis

Elixir is the major technology arm of the Melco Group based in Macau. As a premier gaming technology solutions provider in Asia, it is principally engaged in the distribution of electronic gaming machines and other gaming products to casino operators. It also supplies integrated systems to hotels and casino operators such as installation of casino surveillance systems and LED display.

Contribution from Elixir dropped by 28% to HK$23.7 million in 2006 from HK$32.8 million in 2005. This was primarily because Elixir was going through a transformational change in 2006, repositioning itself from an equipment distributorship to becoming Asia's only gaming machine supplier with R&D and manufacturing capabilities which would, in due course, include developing Elixir's own games.

Benefiting from the growth in gaming in the region, Elixir has successfully established Elixir Gaming Technology Philippines, Inc in Philippines for the servicing and distribution of gaming machines in the region, including Indo China. In early 2006 Elixir began setting up a gaming research & development centre in Macau to focus on the development of gaming machine content and gaming technologies for Asian markets.

In order to allow Elixir to have greater flexibility to develop its business in Asia, Elixir terminated its Asia gaming technology alliance with Stargames Corporation Pty Ltd., the Australian subsidiary of Shuffle Master, Inc. (NASDAQ national Market: SHFL) in February 2007.

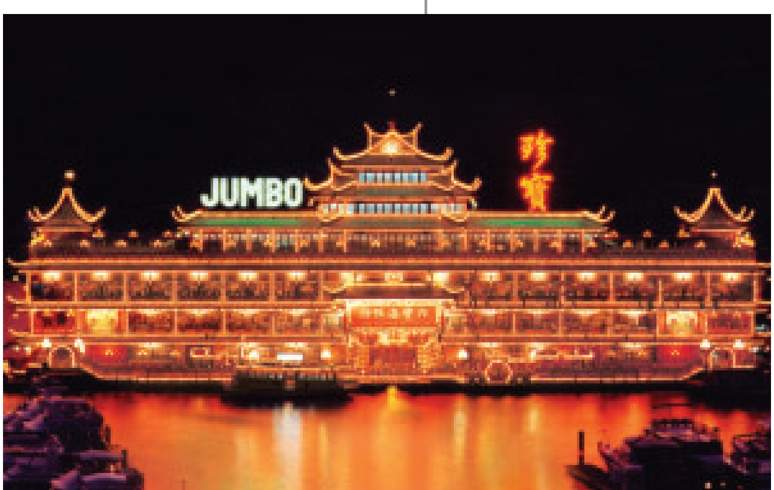
iAsia Technology made a positive contribution to the Group amounting to HK$2.7 million for the year (2005 – HK$1 million), representing a spectacular increase of over 170%. Based in Hong Kong, iAsia is engaged in the provision of comprehensive online trading and related systems and services to financial institutions and intermediaries, principally in Asia. During the year, iAsia developed a new and well-received Bullion Order Matching System. It has continued to improve and integrate its existing online trading modules and related systems, and the new Bullion Order Matching System has enhanced the comprehensiveness of its systems.

The Group's IT systems for investment banking and financial services are all supported by iAsia, and iAsia has contributed significantly to improving the technological sophistication of the Group's financial services unit.

INVESTMENT BANKING AND FINANCIAL SERVICES

Contribution from investment banking and financial services (before finance costs) increased significantly from HK$21.8 million in 2005 to HK$49.3 million, representing a spectacular increase of 126%.

The Group's investment banking and financial service business is conducted through Value Convergence Holdings Limited ("Value Convergence", Stock Code: 8101), a company listed on the GEM Board of the Stock Exchange of Hong Kong Limited. Value



Management Discussion and Analysis

Convergence recorded a consolidated turnover of approximately HK$182.0 million in 2006, representing an increase of around 58% as compared to 2005.

The improved operating results for the year were mainly attributable to enhanced operating performance from the brokerage business as well as increased contribution from the Group's investment trading portfolio.

Going forward, Value Convergence will actively pursue fresh initiatives such as the provision of fund management services and new investment products, as well as embarking on business acquisitions beneficial to the overall growth of the Group's business.

PROPERTY AND OTHER INVESTMENTS

Contribution from property and other investments increased from HK$47.5 million to HK$105.6 million, representing an increase of 122%. The increase is mainly attributable to the increase in income from the Group's treasury functions.

LOSS ON DISPOSAL OF SUBSIDIARIES

Effective from October 2006, the Macau gaming business conducted through Melco PBL ceased to be accounted for as subsidiaries of the Group and began to be accounted for as jointly-controlled entities. Pursuant to an agreement with PBL, the Group's effective interest in the Macau joint venture decreased from 60% to 50%. As a result, an accounting loss amounting to HK$12.1 million (2005 – Nil) was created. Full details and explanations are given in Note 13 to the consolidated financial statements.

(LOSS) GAIN ON DEEMED DISPOSAL OF PARTIAL INTERESTS IN SUBSIDIARIES

In 2006, a small loss of HK$33,000 was recognized as a result of the exercise of certain share options by minority shareholders of a subsidiary (2005 – HK$24,000). In 2005, a gain of HK$514.4 million was recognized as a result of the formation of the Melco PBL Joint Venture. Full details and explanations are given in Note 12 to the consolidated financial statements.

GAIN ON DEEMED DISPOSAL OF INTERESTS IN JOINTLY CONTROLLED ENTITIES

In December 2006, Melco PBL Entertainment was listed on NASDAQ in the US and approximately 15.3% of the enlarged share capital (prior to the exercise of the greenshoe which took place after the year end) was offered to public shareholders in the form of an IPO. According to prevailing Accounting Standards, this constituted a deemed disposal of interests in jointly controlled entities (Group's effective interest reduced from 50% to 42.3%) and Melco PBL Entertainment would henceforth be accounted for as an associate. The deemed disposal resulted in a gain of approximately HK$3.1 billion (2005 – Nil) to the Group. Full details and explanations are given in Note 32 to the consolidated financial statements.

Management Discussion and Analysis

GAIN ON FORMATION OF A JOINTLY CONTROLLED ENTITY

In September 2006, PAL, in which the Group has an interest of 60%, was formed to pursue lottery business in Asia. Upon the formation of this jointly controlled entity, the Group realized a gain of HK$20 million (2005 – Nil) which arose as a difference between the contributed value of certain intangible assets and the fair value of such assets as estimated by a professional valuer. Full details and explanations are given in Note 31 to the consolidated financial statements.

SHARE OF (LOSS) PROFIT OF JOINTLY CONTROLLED ENTITIES

Share of (loss) profit of jointly controlled entities is made up of the following:

	Year ended 31 Dec 2006 ***HK$'000***	Year ended 31 Dec 2005 *HK$'000*
Share of (loss) profit of Melco PBL Entertainment and its subsidaries	**(189,736)**	2,234
Share of (loss) of PAL	**(2,099)**	–
	(191,835)	2,234

(i) **Share of (Loss) Profit of Melco PBL Entertainment and its Subsidiaries**

As explained above, subsequent to a restructuring which took place in October 2006, the Group's interest in the Macau gaming operations of Melco PBL was grouped under Melco PBL Entertainment and the Group's effective interest decreased from 60% to 50%. As a result, the Group's attributable loss of Melco PBL Entertainment and its subsidiaries were shown in the consolidated financial statements for the three months ended 31 December 2006 under the category of share of loss of jointly controlled entities.

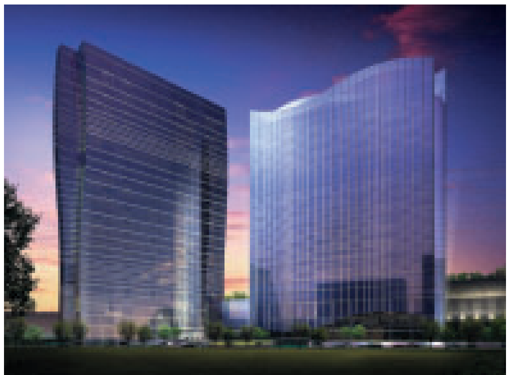
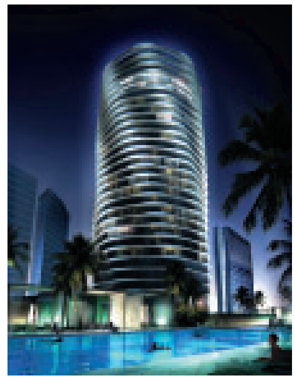
During this period, the Group's attributable loss arising from its 50% ownership of Melco PBL Entertainment amounted to approximately HK$189.7 million. The substantial losses were primarily due to the following:

(1) Substantial pre-opening expenses were incurred in respect of Crown Macau and City of Dreams. According to the financial statements of Melco PBL Entertainment, the total pre-opening expenses amounted to approximately US$11.7 million for the full year ended 31 December 2006.

(2) Effective from September 2006, Melco PBL Entertainment started to provide for the amortization of the gaming license and its relevant costs. According to the financial statements of Melco PBL Entertainment, for the three months ended 31 December 2006, approximately US$14.3 million, US$11.2 million and US$10.2 million for the amortization, the written-off of deferred financing costs for the subconcession facility and the relevant interest charges thereon, respectively, were charged to income statement in relation to the gaming license.

For the year ended 31 December 2005, the Group's share from Melco PBL Entertainment recorded a profit of approximately

Management Discussion and Analysis

HK$2.2 million. This was primarily due to the interest income earned on time deposits prior to the cash being deployed for the development projects.

(ii) Share of Loss of PAL
As explained above, in an effort to tap the growing lottery markets in Asia, especially China, PAL was formed as a jointly controlled entity in September 2006. For the four months ended 31 December 2006, the operational losses attributable to the Group amounted to HK$2.1 million (2005 – Nil). The losses were primarily due to pre-opening expenses incurred prior to the operation of the lottery sales outlets in China.

UNALLOCATED CORPORATE EXPENSES
Unallocated corporate expenses increased by 75% from approximately HK$38.9 million in 2005 to HK$68.2 million in 2006. The increase was primarily due to the increased staff costs and office rental and utility expenses at head office level as a result of the Group's rapid expansion in 2006.

FINANCE COSTS
Finance costs increased by 171% from approximately HK$31.7 million in 2005 to HK$85.9 million in 2006. The increase was primarily due to (i) increase in bank interest payable as a result of the increased funding needs of Value Convergence and (ii) increase in "deemed" interest payable (ie no cash flow implications) in relation to the convertible loan notes. Full details and explanations are given in Note 14 to the consolidated financial statements.

INCOME TAX CREDIT/ (EXPENSE)
Income tax credit amounted to approximately HK$4.6 million versus an income tax expense of HK$6.0 million in 2005. This was primarily due to a deferred tax credit of HK$13.5 million in 2006 (2005 – HK$1.9 million) and the full details of which are shown in Notes 17 and 48 to the consolidated financial statements.

OUTLOOK
The listing of Melco PBL Entertainement in the US marked an important chapter in the development of the Group. Not only does it substantially relieve the funding burden on Melco, but it also releases a lot of Melco's human resources previously dedicated to Melco PBL to the development of other business initiatives. Going forward, in addition to the continual improvement of the operating performance of our existing business units, we will leverage off our strength in Macau as well as our strong connections in Greater China to tap the various business opportunities that are available to us.

LIQUIDITY AND FINANCIAL RESOURCES/CAPITAL STRUCTURE/CHARGE ON GROUP ASSETS
The Group finances its business operations and investments with internal resources, cash revenues generated from operating activities and short-term bank borrowing.

As at 31 December 2006, total assets of the Group amounted to HK$9,344.6 million (2005 – HK$5,652.9 million) which were financed by shareholders' equity of HK$7,567.1 million (2005 – HK$3,558.2 million), minority interests of HK$94.1 million (2005

– HK$686.3 million), current liabilities of HK$419.2 million (2005 – HK$306.5 million), and non-current liabilities of HK$1,264.0 million (2005 – HK$1,101.9 million). The Group's current ratio, expressed as current assets over current liabilities, was maintained at a satisfactory level of 6.3 (2005: 9.4).

For the year under review, the Group recorded a net cash outflow of HK$1,140.5 million (2005 – inflow of HK$1,955.3 million). As at 31 December 2006, cash and cash equivalents of the Group amounted to HK$1,209.8 million (2005 – HK$2,350.3 million). The gearing ratio, expressed as a percentage of total borrowings (including bank borrowing, obligation under finance leases, convertible loan notes, long term payable and shareholder's loan) over shareholders' equity, was at a satisfactory level of 0.17 time as at 31 December 2006 (2005 – 0.31 time). The Group adopts a prudent treasury policy. Cash and bank balances consisted of about 11% of cash and bank balances and 89% of short term fixed deposits. All borrowings and cash and bank balances are denominated in Hong Kong dollars and U.S. dollars to maintain stable exposure to foreign exchange risks.

As at 31 December 2006, the Group's total convertible loan notes amounted to HK$1,093.5 million, which were due in 2009 and 2010. The Group's long term payable amounted to HK$170.5 million, which was unsecured, non-interest bearing and due in 2008.

As at 31 December 2006, the Group's total available banking facilities from various banks amounted to HK$220.7 million (2005 – HK$229.8 million), of which HK$60 million (2005 – HK$80 million) was secured by margin clients listed securities, HK$49.8 million (2005 – HK$49.8 million) was secured by pledging HK$85 million of the Group's investment properties, and HK$0.9 million (2005 – HK$0.3 million) was secured by pledging the same amount of the Group's time deposit. As at 31 December 2006, the Group had used HK$49 million and HK$0.9 million of unsecured and secured banking facilities respectively (2005 – unsecured HK$23 million; secured HK$5 million). The said amount of HK$49 million had matured and was repaid by 4 January 2007.

MATERIAL ACQUISITIONS

In 2006, the Group had entered into/completed the following acquisitions:

On 1 March 2006, the land for the development of Crown Macau was officially granted to the Melco PBL. Subsequent to that, the Company issued 22,222,222 new shares to Sociedade de Turismo e Diversôes de Macau, S.A. in accordance with previously signed agreements between the two companies.

Pursuant to a Memorandum of Agreement dated 5 March 2006 and a Supplemental Agreement dated 26 May 2006 entered into between the Company and PBL, the Company contributed an amount of approximately HK$1,244,800,000 (US$160,000,000) to Melco PBL Gaming (Macau) Limited through Melco PBL Entertainment for the acquisition of the Macau gaming subconcession from Wynn Resorts (Macau) SA.

On 9 May 2006, Melco PBL International Limited ("Melco PBL International"), a jointly controlled entity of the Group, entered into an agreement ("Sale and Purchase Agreement") with Dr. Stanley Ho in relation to the sale of 20% of the issued share capital of Mocha Slots Group Limited ("Sale Shares") and related loan ("Sale Loan") from Dr. Ho to Melco PBL International for an aggregate consideration of approximately HK$295.7 million, with approximately HK$250 million being the consideration for the Sale Shares and approximately HK$45.7 million being the consideration for the Sale Loan. The sale and purchase of the Sale Shares and the assignment of the Sale Loan under the Sale and Purchase Agreement were completed on the same day the Sale and Purchase Agreement was signed.

On 17 May 2006, Melco PBL Entertainment's direct wholly-owned subsidiary Melco PBL (Macau Peninsula) Limited, a jointly controlled entity of the Group, entered into an agreement to purchase the entire issued share capital of a company holding the rights to a land lease grant in respect of a plot of land with an area of 6,480 square meters located at Zona dos Novos Aterros do Porto Exterior (NAPE), the Macau Peninsula, at an aggregate

Management Discussion and Analysis

consideration amounting to approximately HK$1.5 billion. The acquisition is subject to the fulfillment of a number of conditions and is expected to be completed in the third quarter of 2007. An amount of HK$100 million was paid as stakeholder money on signing of the sale and purchase agreement. The balance of the consideration is payable in cash on completion of the acquisition. Melco PBL Entertainment intends to develop its third hotel and casino project in Macau on the site.

HEADCOUNT/EMPLOYEES' INFORMATION

To support its business expansion, the Group's workforce has grown. As at 31 December 2006, it had 485 employees (excluding Melco PBL Entertainment's employees) against 431 as at 31 December 2005 (note). The over 12.5% increase included the addition of 54 new positions in the Group. Of all the employees, 419 were based in Hong Kong and the rest worked in Macau and the PRC. The majority of the newly created positions were for the Macau business and Melco Corporate Office. Staff costs for the year of 2006, including emoluments for Directors and share options expenses, amounted to HK$269.3 million (2005 – HK$169.7 million).

1. **Recruitment**
   Melco is an equal opportunity employer and we recruit talents with outstanding abilities and commitment to professional excellence. We identify and validate talents through different recruitment sources and regularly review our recruitment structure and assessment criteria. We also employ suitable tools to assess candidates' potential.

2. **Performance and Rewards**
   Melco demands and appreciates high performance. Our reward principle is primarily performance based and we reward our people competitively based on their job responsibilities, performance and contribution to business results as well as professional and managerial competencies.

3. **Learning & Development**
   Melco provides training to develop the necessary and other skills needed to satisfy business needs, which, on the one hand, would improve performance and deliver value and, on the other hand, would enhance personal growth.

   We adopt a systematic approach in structuring our training programs, which are focused to individual and corporate needs. Training objective would first be established with the desired outcomes clearly defined and results are continually reviewed.

Note: Originally it was 842 employees reported as at 31 December 2005. However, 411 employees under Mocha and Design & Construction project team were transferred to Melco PBL Entertainment at the end of year 2006.

FOREIGN EXCHANGE EXPOSURE

It is the Group's policy for its operating entities to operate in their corresponding local currencies to minimize currency risks. The Group's principal businesses are conducted and recorded in Hong Kong dollars and Macau Pataca. As the impact from foreign exchange exposure is minimal, no hedging against foreign currency exposure is necessary.

FUTURE PLANS FOR MATERIAL INVESTMENTS OR CAPITAL ASSETS

Material capital expenditure will be incurred when the Company begins to pursue different projects in the coming years. The Company expects the respective project companies to secure required funding themselves using different financing options available. The Company will also provide the required equity capital to the new projects coming ahead, should it be deemed appropriate. Details are given in Notes 56 and 57 to the consolidated financial statements.

CONTINGENT LIABILITIES

On 31 December 2006, the Company provided a total guarantee of approximately HK$12,603,000 (2005 – HK$4,680,000) to a supplier and an insurance company in respect of goods purchased and service provided by its subsidiaries and the amount utilized is approximately HK$1,247,000 (2005 – HK$1,082,000).

Management Discussion and Analysis

CORPORATE GOVERNANCE PRACTICES

In 2005, the Group adopted its Code on Corporate Governance ("Company Code"), which sets out the corporate standards and practices used by the Group in directing and managing its business affairs. The Company Code was prepared with reference to the principles, Code Provisions and Recommended Best Practices stipulated in the Code on Corporate Governance Practices issued by the Stock Exchange, which came into effect on 1 January 2005. The Company Code not only formalizes the Group's existing corporate governance principles and practices, but also serves to assimilate practices with benchmarks prescribed by the Stock Exchange, ultimately ensuring that the Group runs a highly transparent operation and is accountable to its shareholders.

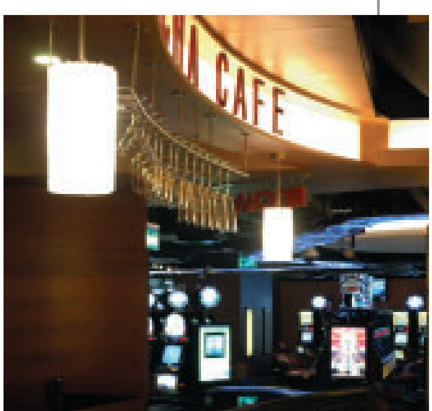
CORPORATE RECOGNITION

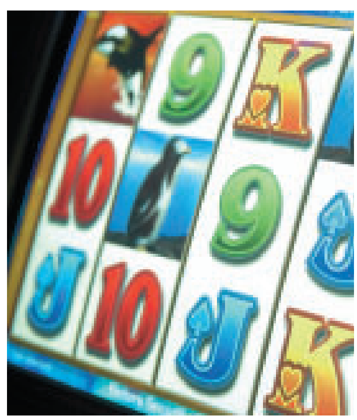
During the year, the Group received a number of accolades for its outstanding business performance as well as high corporate governance standard.

In recognition of the Group's excellent corporate governance practices, its Chairman, Mr. Lawrence Ho was awarded 'Directors of the Year Award 2005' by the Hong Kong Institute of Directors. In the survey conducted by *Institutional Investor*, a leading global investment and capital market research and publishing organization, Mr. Ho was named the "Best CEO" in the 'Conglomerates' category. The award reviews and ranks Asian companies annually for "best practices" in investor and shareholder relations.

With a caring spirit, Melco was recognized, for the second consecutive year, as a Caring Company by The Hong Kong Council of Social Service, an umbrella organization of over 300 non-governmental organizations (NGOs) providing over 90% of the social welfare services in Hong Kong. Melco was also recognized as one of the 'Business Superbrands' by Superbrands Hong Kong. The "Superbrand" award selection process adheres to a set of strict criteria rating attributes such as consumers' awareness of the brand, company reputation, market share and brand quality.

As a socially responsible young entrepreneur in Hong Kong, Mr Ho was elected as one of the 'Ten Outstanding Young Persons' in 2006. Presented annually by the Junior Chamber of Commerce International Hong Kong, the award recognizes young people demonstrating professional excellence and commitment to the community. Mr Ho also received the 5th China Enterprise Award for Creative Businessmen in Beijing and was named "Leader of Tomorrow 2005" by Hong Kong Tatler for his leadership wisdom and traits.



Management Discussion and Analysis

INVESTOR RELATIONS

Melco believes maintaining communication and operational transparency is vital to building good investors relations. During the year, the Group actively participated in investor conferences organized by well-known securities houses and regularly met with analysts and institutional investors. Various site visits to our development sites in Macau were also organized for investors.

The Group will continue to actively enhance communication with investors to foster investor relations. The Group would like to thank all investors for their continuous support over the years.

SOCIAL RESPONSIBILITY

Apart from growing its business, the Group is also committed to supporting charitable events and activities that can help improve the society. The Melco Volunteer Team was set up in 2004 to encourage staff to actively involve in worthwhile charitable causes and activities such as goodwill visits, raffle sales and fundraising campaigns in both Macau and Hong Kong. Through taking part in community and social service activities, the Group hopes to nurture a sense of social responsibility among its staff.

In the past year, Melco employees of all levels took part in the following charitable and environmental protection activities and events in Hong Kong and Macau:

- (Jan) Elderly Visit & Chinese New Year Loving Gift Packs organized by Hong Kong Physically Handicapped and Able-bodied Association (HK PHAB)
- (Feb) The Macau Melco Fives 2006
- (Apr) The Community Chest's Treasure Hunt at Fisherman's Wharf, Macau
- (May) City Junior Chamber's Fundraising Football Match for Supporting China Student
- (Jun) Society for Abandoned Animals Charity Gala Premiere 'A Bite of Love'
- (Jul) World Wide Fund for Nature Diamond Membership
- (Jul) The Community Chest's Melco's Planting Day 2006
- (Sept) Playday at Jumbo Kingdom jointly organized with Playright Children's Play Association
- (Sept) Mid-Autumn Visit organized by HKPHAB
- (Oct) Orbis Pinday
- (Oct) The Community Chest's Dress Special Day
- (Nov) The Community Chest's New Territories Walk for Million
- (Dec) The Community Chest's Run-up IFC Two 2007
- (Dec) UNICEF 15km Run

The "Greening in Melco" environmental protection initiative promotes a "green" culture in the Group. It encourages employees to recycle papers, cans and plastic bottles. Melco Green Team also participated in fundraising walk and nature appreciation visits organized by World Wide Fund for Nature. Employees were able to enjoy the natural beauty of Mai Po while learning more about work of World Wide Fund for Nature in environmental protection and

Management Discussion and Analysis

conservations. To further promote green awareness among the Group, Melco Green Team launched a "Lunar Year End Recycling Campaign" to collect reusable or recyclable materials (including waste papers, books, aluminum cans and plastic bottles) at designated spots. This campaign was well received and very successful.