



PUBLIC FINANCIAL HOLDINGS LIMITED

stock code: 626



Annual Report 2006

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Corporate Information

Board of Directors

Non-executive Chairman

Tan Sri Dato' Sri Dr. Teh Hong Piow (Chairman),
also Chairman and Founder of
Public Bank Berhad

Executive Directors

Tan Yoke Kong
Lee Huat Oon

Non-executive Directors

Dato' Sri Tay Ah Lek
Dato' Chang Kat Kiam
Wong Kong Ming

Independent Non-executive Directors

Tan Sri Dato' Thong Yaw Hong (Co-Chairman)
Dato' Yeoh Chin Kee
Lee Chin Guan

Joint Secretaries

Tan Yoke Kong
Chan Sau Kuen

Registered Office

Clarendon House
Church Street
Hamilton HM 11
Bermuda

Head Office and Principal Place of Business

1105-7 Wing On House
71 Des Voeux Road Central
Hong Kong
Telephone : (852) 2525 9351
Facsimile : (852) 2845 0681
Websites : www.publicbank.com.hk
www.publicfinance.com.hk

Share Listing

Main Board of The Stock Exchange
of Hong Kong Limited
Stock Code : 626

Principal Registrar

Butterfield Fund Services (Bermuda) Limited
Rosebank Centre
11 Bermudiana Road
Pembroke
Bermuda

Hong Kong Branch Registrar

Tengis Limited
26th Floor, Tesbury Centre
28 Queen's Road East
Wanchai
Hong Kong
Telephone : (852) 2980 1333
Facsimile : (852) 2810 8185

Auditors

Ernst & Young
Certified Public Accountants

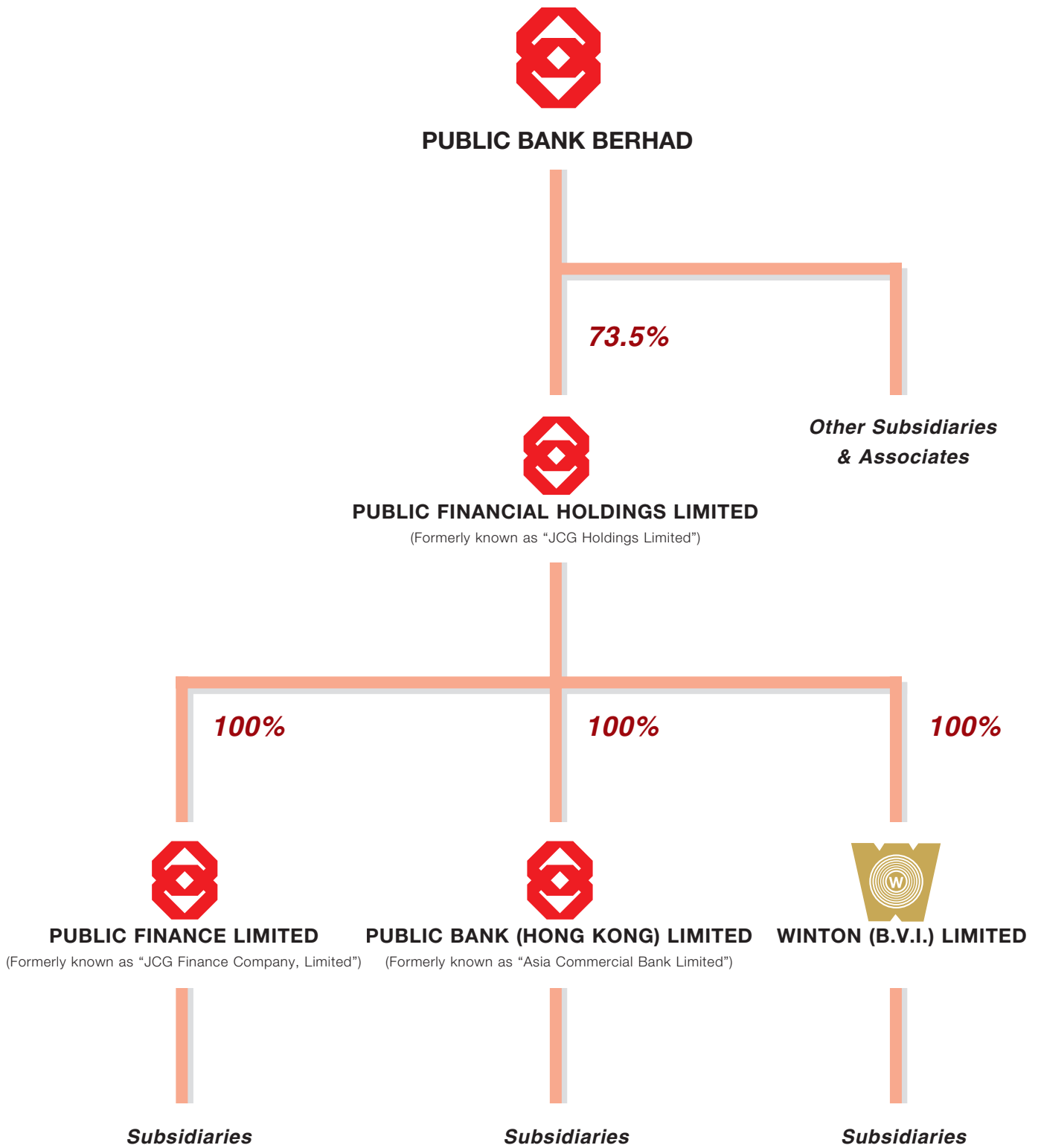
Legal Advisers

Charles Yeung Clement Lam Liu & Yip
Deacons
Gallant Y.T. Ho & Co.
Philip K H Wong, Kennedy Y H Wong & Co.
Siao, Wen and Leung

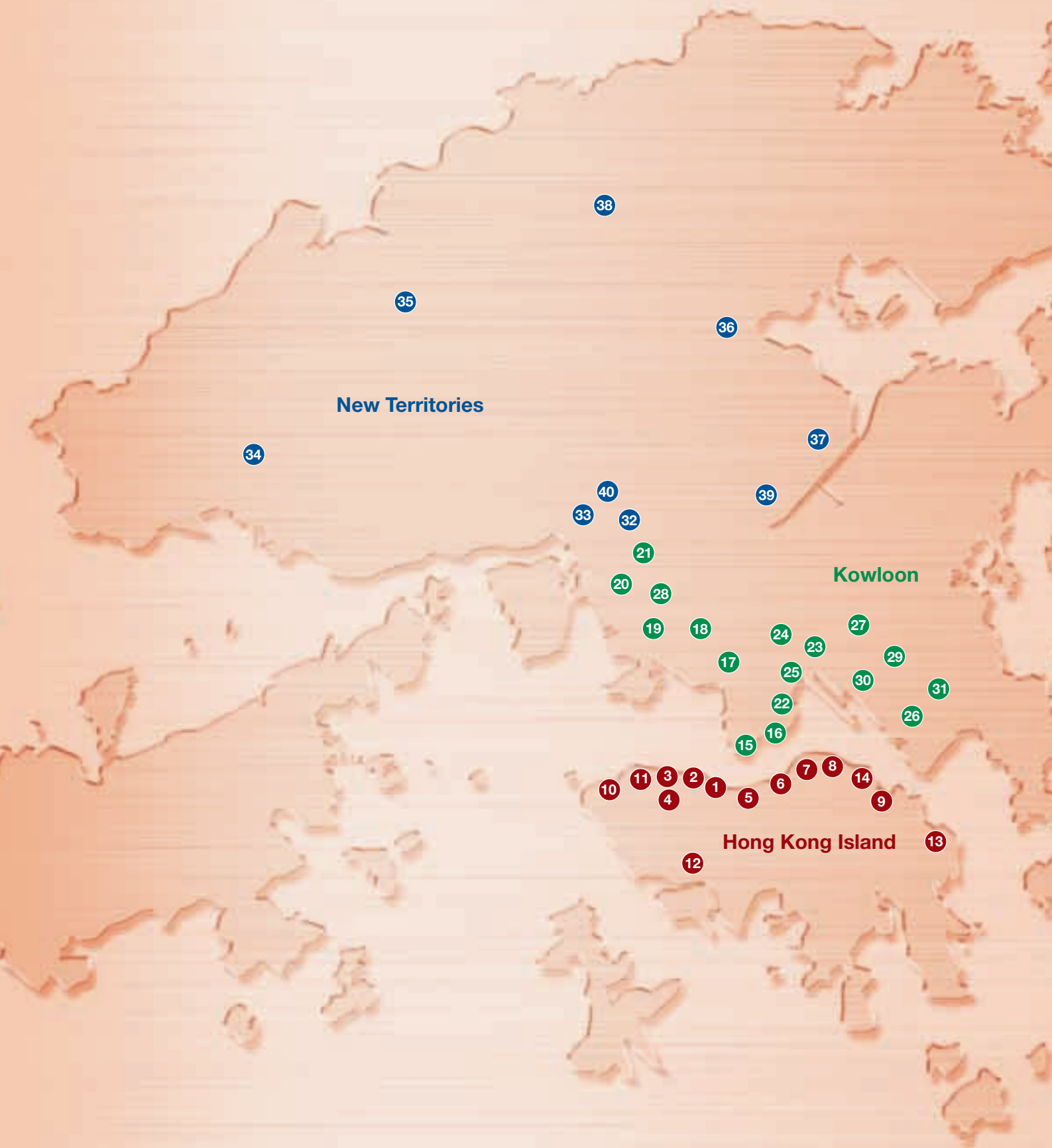
Principal Bankers

Bangkok Bank Public Company Ltd
Bank of China (Hong Kong) Limited
Barclays Bank PLC
China Merchants Bank Co Ltd
China Minsheng Banking Corp. Ltd
CIMB Bank Berhad
Industrial and Commercial Bank of China (Asia) Limited
Oversea-Chinese Banking Corporation Limited
Public Bank Berhad
Scotiabank (Hong Kong) Limited
Standard Chartered Bank
The Bank of Tokyo – Mitsubishi UFJ Ltd
The Hongkong and Shanghai Banking Corporation Limited

Group Structure



Public Finance Limited – Branch Network



Public Finance Limited – Branch Network

Hong Kong Island

- 1 **Landmark Branch**
Room 1905, Gloucester Tower
The Landmark, Central
Tel: 25224067 Fax: 25373623
Manager: Rodriguez Lolita H
- 2 **Queen's Road Central Branch**
1/F, Parker House
72 Queen's Road Central
Tel: 25266415 Fax: 28779088
Manager: Wong Kai Ip Jimmy
- 3 **Central Branch**
M/F, Chung Nam House
59 Des Voeux Road Central
Tel: 25248676 Fax: 28779084
Manager: Leung Kwok Fai Eric
- 4 **Wing On House Branch**
Room 1109-10, Wing On House
71 Des Voeux Road Central
Tel: 25245603 Fax: 25372909
Manager: Villareal Ma Aurora B
- 5 **Wanchai Branch**
G/F, 170 Hennessy Road
Tel: 25746245 Fax: 28936653
Manager: Tong Woon Shing
- 6 **Tin Lok Lane Branch**
G/F, Foo Tak Building
365 Hennessy Road
Tel: 28917028 Fax: 28933769
Manager: Ho Sau Yan
- 7 **Causeway Bay Branch**
1/F, Coasia Building
496-498 Lockhart Road
Tel: 28936575 Fax: 28932770
Manager: Lau Kan So Ivan
- 8 **North Point Branch**
Shop No.1, G/F, Wah Hing Building
449-455 King's Road
Tel: 25610160 Fax: 28563647
Manager: Louie Kin Cheong Daniel
- 9 **Shaukeiwan Branch**
G/F, 134 Shaukeiwan Road
Tel: 25670461 Fax: 28858501
Manager: Chan Siu Sung Jeffery
- 10 **Shek Tong Tsui Branch**
Shop G.1, Hong Kong Plaza
188 Connaught Road West
Tel: 28176125 Fax: 28177618
Manager: Li Wai Yin
- 11 **Western District Branch**
G/F, 161 Des Voeux Road West
Tel: 25479148 Fax: 25461142
Manager: Wu Kin Sang Wilson
- 12 **Aberdeen Branch**
Shop A, G/F, Kong Kai Building
184-188 Aberdeen Main Road
Tel: 25538231 Fax: 25543897
Manager: Ng Siu Kwan Arthur
- 13 **Chai Wan Branch**
G/F, Flat B, 77 Walton Estate
341-343 Chai Wan Road
Tel: 25578003 Fax: 25574088
Manager: Miu Ka Lok Patrick
- 14 **Quarry Bay Branch**
G/F, 14 Hoi Kwong Street
Tel: 25166368 Fax: 25790084
Manager: Wong Wai Keung Thomas

Kowloon

- 15 **Star House Branch**
Basement, Shop B9-B10
Star House Plaza, TST
Tel: 27308395 Fax: 27302346
Manager: Ho Mei Yu Denise
- 16 **Tsimshatsui Branch**
Shop No. 51-53
1/F, Harbour Crystal Centre
100 Granville Road, TST East
Tel: 23693236 Fax: 23110433
Manager: Lai Chung Wai Danny
- 17 **Jordan Road Branch**
Shop B, G/F, Dao Hing Building
34 Jordan Road
Tel: 27364711 Fax: 23148432
Manager: Ho Kwok Sin Tom
- 18 **Nathan Road Branch**
G/F, 480 Nathan Road
Tel: 27715285 Fax: 27704127
Manager: Leung Kwok Chung Solomon
- 19 **Mongkok Branch**
Flat B, 1/F, JCG Building
16 Mongkok Road
Tel: 23940253 Fax: 27875630
Manager: Cheng Ho Fat Ricky
- 20 **Shamshuipo Branch**
G/F,
27 Castle Peak Road
Tel: 27282347 Fax: 27299685
Manager: Kwan Wai Choi Samuel
- 21 **Cheung Sha Wan Branch**
Unit C1, G/F
746 Cheung Sha Wan Road
Tel: 27445416 Fax: 27853634
Manager: Yuen Chuk Kwan Raymond
- 22 **Hunghom Branch**
G/F, 130 Ma Tau Wai Road
Tel: 23344307 Fax: 27644876
Manager: Cheung Chu Ming Albert
- 23 **Sanpokong Branch**
G/F, 92 Shung Ling Street
Tel: 23283175 Fax: 23254504
Manager: Wong Chun Pui Paul
- 24 **Kowloon City Branch**
G/F, 31 Lion Rock Road
Tel: 23824893 Fax: 27164819
Manager: Li Kit Shing Joe
- 25 **Tokwawan Branch**
Shop 9-10, G/F
Chong Chien Court
355 Tokwawan Road
Tel: 23657061 Fax: 27642832
Manager: Man Wing Sun Ethan
- 26 **Kwun Tong Branch**
G/F, 367 Ngau Tau Kok Road
Tel: 23440264 Fax: 27635427
Manager: Cheng Man Kwong Ringo
- 27 **Wong Tai Sin Branch**
G/F, 89 Fung Tak Road
Tel: 23205112 Fax: 27260106
Manager: Ng Chung Tak
- 28 **Prince Edward Branch**
G/F, 751 Nathan Road
Tel: 23803260 Fax: 23804100
Manager: Leung Sze Wan Irene
- 29 **Ngau Tau Kok Branch**
Shop 29, G/F
Wang Kwong House
33 Ngau Tau Kok Road
Tel: 27578299 Fax: 27578737
Manager: Lam Kwan Chee Evans
- 30 **Kowloon Bay Branch**
Unit 2B, G/F
Fook Hong Industrial Building
19 Sheung Yuet Road
Tel: 27567320 Fax: 27585706
Manager: Tong Ka Ling Tony
- 31 **Tseung Kwan O Branch**
Shop G29, G/F
Metro City Plaza, Phase II
Tel: 31944312 Fax: 31944377
Manager: Ho Wai Ming Ian

New Territories

- 32 **Kwai Chung Branch**
Shop 301, 3/F
Kwai Chung Plaza
7-11 Kwai Foo Road
Tel: 24200121 Fax: 24850590
Manager: Ho Kam Ming
- 33 **Tsuen Wan Branch**
G/F, 281 Sha Tsui Road
Tel: 24934187 Fax: 24174497
Manager: Law Shue Sum Dennis
- 34 **Tuen Mun Branch**
Shop 7, G/F, Mei Hang Building
Kai Man Path
Tel: 24572901 Fax: 24402503
Manager: Chan Chiu Ming Peter
- 35 **Yuen Long Branch**
G/F, 182 Main Road
Tel: 24762146 Fax: 24759903
Manager: Yuen Chak Sang Michael
- 36 **Tai Po Branch**
G/F, 86 Kwong Fuk Road
Tel: 26565207 Fax: 26577019
Manager: Kan Yuk Lun Taylor
- 37 **Shatin Branch**
Shop 10A, 11A & B
Lucky Plaza Commercial Centre
Tel: 26995633 Fax: 26914588
Manager: Lee Man Fai Eric
- 38 **Sheung Shui Branch**
G/F, 99 San Fung Avenue
Tel: 26732729 Fax: 26739278
Manager: Kam Ying Wah
- 39 **Tai Wai Branch**
Shop 2C, G/F
11-13 Chik Fai Street
Tel: 26092611 Fax: 26094088
Manager: Cheung Wa Wai Victor
- 40 **Nan Fung Centre Branch**
Rm 1523, Nan Fung Centre
264-298 Castle Peak Road
Tsuen Wan
Tel: 24141198 Fax: 24131624
Manager: Chow Koon Ping Danny

Public Bank (Hong Kong) Limited – Branch Network



Public Bank (Hong Kong) Limited – Branch Network

Head Office and Branches

Head Office

Public Bank Centre
120 Des Voeux Road Central
Tel : 2541 9222
Post Box : G.P.O. Box 824
Telex : 73085 HKACB HX
Fax : 2541 0009
Website : www.publicbank.com.hk

Hong Kong Island

- 1 Main Branch**
G/F, Public Bank Centre
120 Des Voeux Road
Central
Tel : 2541 9222
Fax : 2545 2866
Manager : Wong Lam Fai, Philip
- 2 Western Branch**
Shop 2-3
G/F, Kam Kwan Building
163-173 Des Voeux Road West
Tel : 2858 2220
Fax : 2858 2638
Manager : Lau Yiu Fai, Lawrence
- 3 Wanchai Commercial Centre**
Unit A
9/F, China Overseas Building
139 Hennessy Road
Wanchai
Tel : 2891 4171
Fax : 2834 1012
Manager : Chin Yoke Fong, Marina
- 4 North Point Branch**
Shop A
G/F, Yue Yick Building
363-365 King's Road
North Point
Tel : 2568 5141
Fax : 2567 0655
Manager : Yam Oi Yin, Pauline
- 5 Shek Tong Tsui Branch**
Shop B1
G/F, Hong Kong Plaza
369-375 Des Voeux Road West
Tel : 2546 2055
Fax : 2559 7962
Manager : Fong Fung Mei, Marisa
- 6 Causeway Bay Branch**
G/F and M/F
447 Hennessy Road
Causeway Bay
Tel : 2572 2363
Fax : 2572 3033
Manager : So Wai Ming, Aubrey

Kowloon

- 7 Yaumatei Branch**
Shop No. 1
G/F, Ginza Square
565-567 Nathan Road
Tel : 2381 1678
Fax : 2395 6398
Manager : Siu Kit Ching, Christina
- 8 Kowloon City Branch**
G/F, 15 Nga Tsin Wai Road
Kowloon City
Tel : 2382 0147
Fax : 2718 4281
Manager : Cheung Wing Kwong
- 9 Hung Hom Branch**
G/F, Hunghom Commercial Centre
37 Ma Tau Wai Road
Hung Hom
Tel : 2363 9213
Fax : 2363 3195
Manager : So Tak Fai, Peter
- 10 Kwun Tong Branch**
Unit 2310
Tower 1, Millennium City 1
388 Kwun Tong Road
Kwun Tong
Tel : 2389 9119
Fax : 2389 9969
Manager : Kwok Ka Leung, Joe
- 11 Mongkok Branch**
G/F, JCG Building
16 Mongkok Road
Tel : 2391 8393
Fax : 2391 6909
Manager : Ngai Mo Ngan, Andy
- 12 San Po Kong Branch**
G/F, 92 Shung Ling Street
San Po Kong
Tel : 2326 8318
Fax : 2326 9180
Manager : Kwong Hon Wun, Peter
- 13 Yuen Long Branch**
Shop No. 5
Fu Ho Building
3-7 Kau Yuk Road
Yuen Long
Tel : 2479 4265
Fax : 2473 3934
Manager : Lam Wong Kan, Kent
- 14 Tsuen Wan Branch**
G/F, Victory Court
185-187 Castle Peak Road
Tsuen Wan
Tel : 2490 4191
Fax : 2490 4811
Manager : Choi Kam Yee, Catalina
- 15 Kwai Fong Branch**
Room 809-811
Metroplaza Tower 2
223 Hing Fong Road
Kwai Fong
Tel : 2480 8822
Fax : 2401 2367
Manager : Law Chan Shang, Peter

China

- 16 Shenzhen Branch**
Shop No.1
G/F, Carrianna Friendship Square
Renminnan Road
Shenzhen
People's Republic of China
Tel : (86-755) 2518 2822
Fax : (86-755) 2518 2327
Manager : Cheung Po Tung, David
- Shenyang Representative Office**
Unit A, 18/F, Xinji Huoju Building
No. 262 Shifu Road
Shenhe District
Shenyang
Liaoning
People's Republic of China
Tel : (86-24) 2279 1368
Fax : (86-24) 2279 1369
Representative: Li Yu Jie

Shanghai Representative Office

Room 302, 3/F
7 Zhongshan Road (E1)
Shanghai
People's Republic of China
Tel : (86-21) 6323 6181
Fax : (86-21) 6323 6802
Representative: Cheung Ding Keung, Sammy

Taiwan

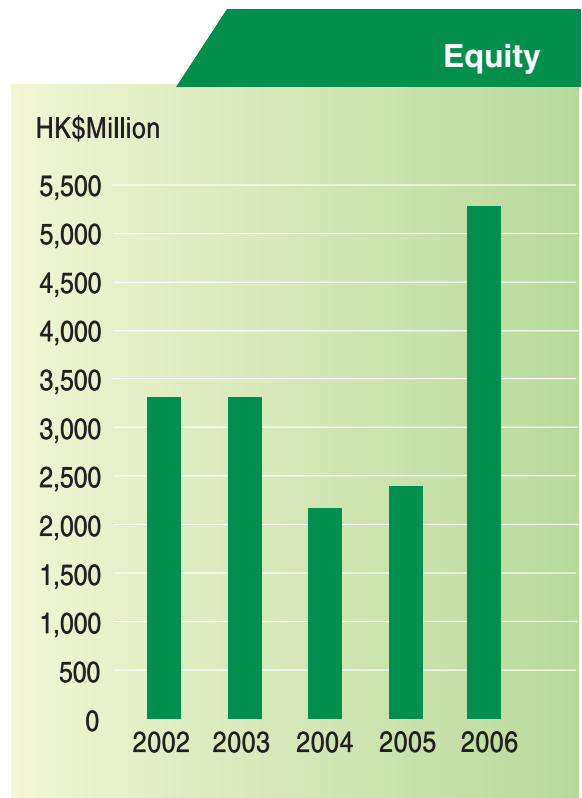
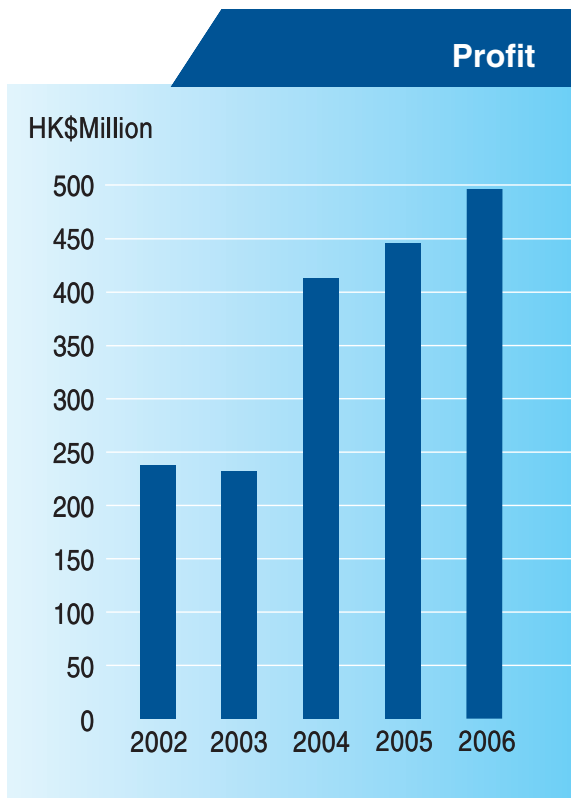
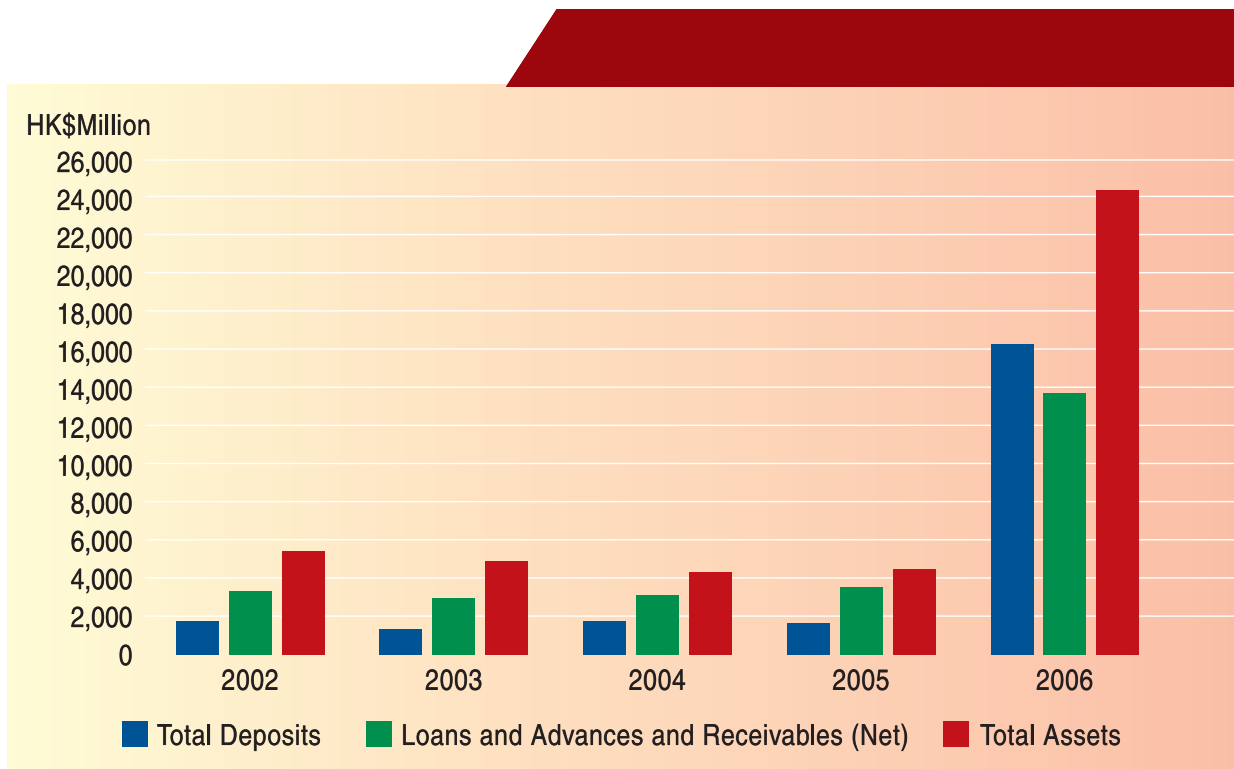
Taipei Representative Office

Room 905
No. 18 Chan-An E. Road
Section 1
Taipei
Taiwan
Tel : (88-62) 2568 3080
Fax : (88-62) 2564 2047
Representative: Huang Si Lung, David

New Territories

- 13 Yuen Long Branch**
Shop No. 5
Fu Ho Building
3-7 Kau Yuk Road
Yuen Long
Tel : 2479 4265
Fax : 2473 3934
Manager : Lam Wong Kan, Kent
- 14 Tsuen Wan Branch**
G/F, Victory Court
185-187 Castle Peak Road
Tsuen Wan
Tel : 2490 4191
Fax : 2490 4811
Manager : Choi Kam Yee, Catalina
- 15 Kwai Fong Branch**
Room 809-811
Metroplaza Tower 2
223 Hing Fong Road
Kwai Fong
Tel : 2480 8822
Fax : 2401 2367
Manager : Law Chan Shang, Peter

Five-year Financial Summary



Five-year Financial Summary

2006 Financial Highlights

Profit for the year:	HK\$496.6 million
Loans and advances and receivables (net):	HK\$13,694.6 million
Total deposits:	HK\$16,139.4 million
Equity:	HK\$5,320.0 million
Earnings per share:	
Basic	HK\$0.500
Diluted	HK\$0.500
Total dividends per share:	HK\$0.250

A summary of the results and of the assets and liabilities of Public Financial Holdings Limited and its subsidiaries for the last five financial years, as extracted from the published audited financial statements, is set out below:

	For the year ended 31 December				
	2006 HK\$'000	2005 HK\$'000	2004 HK\$'000	2003 HK\$'000	2002 HK\$'000
Cash, placements with banks and financial institutions	2,861,992	458,009	795,924	1,430,122	1,572,980
Loans and advances and receivables (net)	13,694,636	3,512,255	3,103,027	2,961,573	3,312,525
Held-to-maturity securities	3,679,604	–	–	–	–
Other assets	4,008,165	493,158	394,728	467,165	505,199
Total assets	24,244,397	4,463,422	4,293,679	4,858,860	5,390,704
Deposits and balances of banks and other financial institutions	516,097	–	–	–	–
Customer deposits	14,853,655	1,641,978	1,720,381	1,309,344	1,774,336
Certificate of deposits issued	769,674	–	–	–	–
Total deposits	16,139,426	1,641,978	1,720,381	1,309,344	1,774,336
Declared dividend	218,779	291,706	283,104	141,552	–
Bank loans	2,000,000	–	–	–	–
Other liabilities	566,144	136,304	123,657	100,426	96,245
Total liabilities	18,924,349	2,069,988	2,127,142	1,551,322	1,870,581
Net assets	5,320,048	2,393,434	2,166,537	3,307,538	3,520,123
Equity	5,320,048	2,393,434	2,166,537	3,307,538	3,304,600
Minority interests	–	–	–	–	215,523
Total equity	5,320,048	2,393,434	2,166,537	3,307,538	3,520,123
Profit for the year	496,637	446,297	412,889	232,133	237,338
Basic earnings per share (HK\$)	0.500	0.623	0.583	0.328	0.335
Diluted earnings per share (HK\$)	0.500	0.622	–	–	–



Tan Sri Dato' Sri Dr. Teh Hong Piow, Chairman

I am pleased to present a review of the results of the Group for the financial year ended 31 December 2006.

Corporate Development Corporate Rebranding

In January 2006, the Group's principal operating subsidiary, JCG Finance Company, Limited was renamed Public Finance Limited ("Public Finance") to reflect the corporate identity of the Group as a member of the Public Bank Group of Malaysia. Subsequently in March 2006, the Company was also renamed Public Financial Holdings Limited.

Acquisition of Asia Commercial Bank

In February 2006, the Company entered into an agreement to acquire a 100% equity interest in Asia Commercial Bank Limited ("ACB"), a full service commercial bank incorporated in Hong Kong with a branch network of 12 branches in Hong Kong, one branch in Shenzhen in the People's Republic of China ("PRC"), and a representative office each in the cities of Shanghai and Shenyang in the PRC, and in Taipei, Taiwan. The acquisition was successfully completed on 30 May 2006. ACB was later renamed Public Bank (Hong Kong) Limited ("Public Bank (Hong Kong)").

The acquisition of Public Bank (Hong Kong) is expected to bring to the Group synergies of lower operating and funding costs, greater economies of scale and more extensive customer reach with a broader customer base, and provide the Group with a platform to offer a full range of banking and financing services in Hong Kong and in the PRC through its Shenzhen branch. The branch network of Public Bank (Hong Kong) in Hong Kong was expanded to 15 branches with the opening of 3 new branches in December 2006, and in Shenzhen to 2 branches with the opening of a new sub-branch in the Futian District of Shenzhen expected to commence business in February 2007, bringing the total number of branches of Public Bank (Hong Kong) to 17.

Business Performance of Public Bank (Hong Kong)

For the year ended 31 December 2006, Public Bank (Hong Kong) recorded a significant improvement in its profit after tax of 68.0% to HK\$145.50 million from HK\$86.59 million for the previous year ended 31 December 2005.

Chairman's Statement

Business Performance of Public Bank (Hong Kong) (Continued)

In the second half of 2006, after its acquisition by the Company, total loans and advances (including trade bills) of Public Bank (Hong Kong) grew by 12.9% or HK\$1.16 billion to HK\$10.16 billion as at 31 December 2006 from HK\$9.0 billion as at 30 June 2006. Customer deposits also grew by 9.9% or HK\$1.21 billion to HK\$13.43 billion from HK\$12.22 billion as at 30 June 2006.

Group Performance Financial Review

For the year ended 31 December 2006, the Group recorded a profit after tax of HK\$496.6 million, representing an increase of 11.3% or HK\$50.3 million when compared to HK\$446.3 million in the previous financial year. The increase in profit after tax was mainly attributed to the consolidation of the financial results of Public Bank (Hong Kong) for the period from May 2006 to December 2006.

The Group's basic earnings per share for the year ended 31 December 2006 was HK\$0.50 per share after accounting for the enlarged issued and paid-up share capital arising from the rights issue of the Company which was completed in April 2006. The directors have declared a first interim dividend of HK\$0.05 per share in June 2006 and a second interim dividend of HK\$0.20 per share in December 2006. The Directors do not recommend the payment of a final dividend, making a total dividend of HK\$0.25 per share for the year.

After consolidation of the account of Public Bank (Hong Kong), the Group's net interest income for the year ended 31 December 2006 increased by 18.8% or HK\$144.4 million to HK\$910.4 million when compared to the previous year. Interest income increased by 80.0% or HK\$642.1 million to HK\$1,444.8 million, and interest expense increased by HK\$497.8 million to HK\$534.4 million. The interest expense of the Group included interest paid of approximately HK\$65.3 million on the 3-year bank term loan of HK\$2.0 billion to partly finance the acquisition of Public Bank (Hong Kong). Non-interest income increased by 54.3% or HK\$72.8 million to HK\$207.0 million, whilst the Group's operating expenses increased by 46.9% or HK\$99.1 million to HK\$310.7 million. The Group's tight control over its operating costs together with operating synergies derived from the initial integration of some operations between Public Bank (Hong Kong) and Public Finance contributed to a low cost to operating income ratio of 27.8% for the year ended 31 December 2006.

However, the Group's impairment allowance for impaired assets rose by 32.8% or HK\$52.1 million to HK\$210.8 million mainly due to the increase in bad debts relating to the personal loans portfolio of Public Finance as a result of an increase in bankruptcy petitions and individual voluntary arrangement of Public Finance's consumer loan customers in 2006.

As at 31 December 2006, the Group's total loans and advance (including trade bills) stood at HK\$13,775.0 million while total deposits from customers, financial institutions and issuance of certificates of deposits were HK\$16,139.4 million, after the consolidation of the assets and liabilities of Public Bank (Hong Kong). Following the acquisition of Public Bank (Hong Kong), the Group's overdue and impaired loan ratio has improved significantly from 5.8% at the end of December 2005 to 2.4% at the end of June 2006, and further improved to 2.2% as at 31 December 2006.

Business Development

The Group will continue to expand the branch network of Public Bank (Hong Kong) and Public Finance as well as to relocate branches to more prominent locations for higher visibility and easy access by customers. The Group will continue to target selected market segments with aggressive marketing promotions and cross-selling business strategies to grow its retail and commercial banking and consumer financing businesses through the expanded branch network; enhance customer satisfaction and loyalty by the provision of better customer service; and training of staff to enhance their technical knowledge and skills through internal and external training courses. The Group will also look for further synergies to reduce operating costs and improve operational efficiency, and seek greater economies of scale through the integration of the support functions of Public Bank (Hong Kong) and Public Finance where appropriate.

Acknowledgement

On behalf of the Board of Directors, I wish to take this opportunity to express our appreciation to the management and staff of the Group for their commitment, dedication and perseverance. On behalf of the management and staff of the Group, I also wish to express our sincere gratitude to our customers for their invaluable patronage, to our shareholders for their continued confidence in and support of the Group, and to the Hong Kong Monetary Authority, Securities and Futures Commission, Hong Kong Stock Exchange, and other relevant authorities for their invaluable advice, guidance and support.

Tan Sri Dato' Sri Dr. Teh Hong Piow
Chairman

Management Discussion and Analysis

Corporate Development in the Year 2006

(a) Rebranding of corporate identity

To align the corporate identity of the Group as a subsidiary of Public Bank Berhad (“Public Bank”) of Malaysia and as a member of the Public Bank Group, the Group’s principal operating subsidiary, JCG Finance Company, Limited changed its name to Public Finance Limited in January 2006 and the signage of its 40 branches was replaced with the new signage name reflecting the new name at the same time. Subsequently, at the Company’s annual general meeting on 8 March 2006, the shareholders of the Company approved the change of the Company’s name from JCG Holdings Limited to Public Financial Holdings Limited. The rebranding has had a positive impact to the image and financial standing of the Group as a member of Malaysia’s Public Bank Group.

(b) Acquisition of Asia Commercial Bank

The Company successfully completed the acquisition of a 100% equity interest in Asia Commercial Bank Limited (“ACB”), a commercial bank incorporated in Hong Kong with a branch network of 12 branches in Hong Kong, one branch in Shenzhen, the PRC, and a representative office each in the cities of Shanghai and Shenyang in the PRC and in Taipei, Taiwan, on 30 May 2006.

The purchase consideration of ACB was partly financed by a rights issue of HK\$2.6 billion, and a 3-year term loan of HK\$2.0 billion. Upon completion of the acquisition of ACB, ACB changed its name to Public Bank (Hong Kong) Limited on 30 June 2006. The acquisition of Public Bank (Hong Kong) is expected to bring to the Group synergies of lower operating and funding costs, greater economies of scale and greater customer reach with a broader customer base and provide the Group with a platform to offer full banking services in Hong Kong as well as in the PRC through its Shenzhen branch.

(c) Business development of Public Bank (Hong Kong) after the acquisition by the Company

Total loans and advances (including trade bills) of Public Bank (Hong Kong) grew during the second half year of 2006 by 12.9% or HK\$1.16 billion to HK\$10.16 billion from HK\$9.0 billion as at the end of June 2006. Customer deposits also grew 9.9% or HK\$1.21 billion to HK\$13.43 billion from HK\$12.22 billion as at end of June 2006.

In December 2006, Public Bank (Hong Kong) opened 3 new branches in Hong Kong. A new sub-branch in Shenzhen is expected to open for business in February 2007, thereby bringing Public Bank (Hong Kong)’s branch network to a total of 17 branches.

For the year ended 31 December 2006, Public Bank (Hong Kong) recorded a significant improvement in profit after tax of 68.0% to HK\$145.50 million from HK\$86.59 million for the year ended 31 December 2005.

Financial Review Group

For the year ended 31 December 2006, the Group recorded a profit after tax of HK\$496.6 million, representing an increase of 11.3% or HK\$50.3 million when compared to HK\$446.3 million in the previous financial year. The increase in profit after tax was mainly attributed to the consolidation of the financial performance of Public Bank (Hong Kong) for the period from May 2006 to December 2006.

The Group’s basic earnings per share for the year ended 31 December 2006 was HK\$0.50 per share with the enlarged issued share capital after the rights issue of 1 rights share for every 2 shares held in April 2006. The directors have declared a first interim dividend of HK\$0.05 per share in June 2006 and a second interim dividend of HK\$0.20 per share in December 2006. The Directors do not recommend the payment of a final dividend, making a total dividend paid for the year of HK\$0.25 per share.

Management Discussion and Analysis

Financial Review (Continued) Group (Continued)

The Group's net interest income for the year ended 31 December 2006 increased by 18.8% or HK\$144.4 million to HK\$910.4 million when compared to the previous year. Interest income increased by 80.0% or HK\$642.1 million to HK\$1,444.8 million after consolidation of the interest income of Public Bank (Hong Kong). Correspondingly, interest expense increased by HK\$497.8 million to HK\$534.4 million, again mainly due to the consolidation of Public Bank (Hong Kong), and interest expense of approximately HK\$65.30 million on the 3-year term loan to partly finance the acquisition of Public Bank (Hong Kong).

The Group's non-interest income increased by 54.3% or HK\$72.8 million to HK\$207.0 million after consolidation of Public Bank (Hong Kong).

During the year under review, the Group's operating expenses increased by 46.9% or HK\$99.1 million to HK\$310.7 million with the consolidation of Public Bank (Hong Kong). The Group's tight control over its operating costs together with operating synergies derived from the initial integration of some operations between Public Bank (Hong Kong) and Public Finance contributed to a low cost to operating income ratio of 27.8% for the year ended 31 December 2006.

However, the Group's impairment allowance for impaired assets rose by 32.8% or HK\$52.1 million to HK\$210.8 million mainly due to the increase in bad debts of personal loans of Public Finance arising from an increase in bankruptcy petitions and individual voluntary arrangement of its customers in 2006.

As at 31 December 2006, the Group's total loans and advance (including trade bills) was HK\$13,775.0 million while total deposits from customers, financial institutions and issuance of certificates of deposits were HK\$16,139.4 million.

Segmental information

The Group's business comprised mainly of two segments: retail and commercial banking and other businesses. Over 90% of the Group's operating income and profit before tax was contributed by retail and commercial banking. When compared to the previous year, the Group's operating income from retail and commercial banking increased by 22.5% or HK\$198.8 million to HK\$1,083.7 million after the consolidation of Public Bank (Hong Kong). Consequently, profit before tax from retail and commercial banking increased by 16.7% or HK\$82.4 million to HK\$574.2 million when compared to the previous year.

Contingent liabilities and commitments

The Group had no material contingent liabilities (other than those related to treasury, trade finance and loan commitments disclosed in the notes to the financial statements) at the end of the year under review. The Group also did not incur any material capital expenditure or entered into any material commitments in respect of capital expenditure during the year under review. The charge over a subsidiary's deposit placement with a bank as disclosed in the 2005 annual report was uplifted in the second half of 2006.

Operational Review Funding and capital management

The main objective of the Group's funding activities and capital management is to ensure the availability of funds at reasonable cost to meet all contractual financial commitments, to fund loan growth and to generate reasonable returns from available funds. The Group also encourages its subsidiaries to be self-reliant in funding their business growth.

Management Discussion and Analysis

Operational Review (Continued) Funding and capital management (Continued)

The Group relied principally on its internally generated capital, customer deposits, deposits from financial institutions, issuance of certificate of deposits and bank loans to fund its retail consumer financing business and commercial banking business. The Group's bank borrowing of HK\$2.0 billion in the form of a 3-year term loan denominated in Hong Kong dollars at floating interest rates are to partly finance the acquisition cost of Public Bank (Hong Kong). This bank borrowing has increased the Group's gearing ratio from nil at the end of the previous year to 37.6% at the end of December 2006. The Group has entered into foreign exchange and interest rate contracts to reduce foreign exchange risk and interest rate risk exposures in its normal banking business.

Asset quality

Following the acquisition of Public Bank (Hong Kong), the Group's overdue and impaired loan ratio has improved significantly from 5.8% at the end of December 2005 to 2.4% at the end of June 2006, and further improved to 2.2% as at 31 December 2006. The asset quality of Public Bank (Hong Kong) had also improved with its overdue and impaired loan ratio reduced from 1.2% at the end of June 2006 to 0.8% as at the end of December 2006 as a result of more prudent credit risk management.

Human resources management and development

The objective of the Group's human resources management activities is to reward and recognise performing staff by providing a competitive remuneration package and implementing a sound performance appraisal system with appropriate incentives, and to promote career development and progression within the Group. Staff were enrolled for external training courses, seminars, professional and technical courses with appropriate sponsorship from the Group in order to upgrade their technical knowledge and skills, to increase their awareness of the market and technological changes, and to improve their business acumen. The Group also encourage staff to participate in social activities organised to promote

team spirit and building a cohesive workforce as well as to serve the community at large as part of corporate responsibility.

To further retain, motivate and enhance staff morale, options to subscribe for 66,526,000 shares in the Company were granted to employees of the Group in May 2005 pursuant to the Group's share option scheme approved by shareholders on 28 February 2002. As at the end of December 2006, options to subscribe for 43,068,000 shares in the Company remained unexercised.

As at the end of December 2006, the Group's staff force increased to over 800 employees with the inclusion of the staff from Public Bank (Hong Kong). For the year ended 31 December 2006, the Group's staff cost amounted to HK\$169.3 million.

Prospects

The economic outlook of Hong Kong is expected to remain positive in 2007. However, there remains uncertainties in the trend of interest rate movements which may have an impact on the economic growth. With the improved employment market and expected positive wage growth, the Hong Kong economy is expected to sustain its growth momentum and consumer spending is expected to increase leading to higher demand for consumer financing.

With the acquisition of Public Bank (Hong Kong), the Group will focus on expanding its retail and commercial banking business through Public Bank (Hong Kong) and its consumer financing business through Public Finance. The Group will continue to seek further synergies in lowering operating costs and greater economies of scale through integration of the support functions of Public Bank (Hong Kong) and Public Finance where appropriate and cross-selling through the combined branch network of Public Finance and Public Bank (Hong Kong) to a wider customer base. Public Bank (Hong Kong) will continue its branch expansion programme and the Group will continue to target selected market segments with aggressive marketing promotions and business strategies to grow its retail and commercial banking and consumer financing businesses.

Corporate Governance Report

Corporate Governance Practices

The board of directors of the Company believes that corporate governance is essential to the success of the Company and has adopted various measures to ensure that a high standard of corporate governance is maintained. With effect from 1 January 2005, the Company has applied the principles and complied with the requirements of the Code on Corporate Governance Practices (the “Code on CGP”) of the Rules Governing the Listing of Securities (the “Listing Rules”) on The Stock Exchange of Hong Kong Limited (the “Stock Exchange”), except for the deviation in respect of the service term under code provision A.4.1 of the Listing Rules. The current practices will be reviewed and updated regularly to follow the latest practices in corporate governance.

Public Finance and Public Bank (Hong Kong), both being major subsidiaries of the Company, are a deposit taking company and a licensed bank respectively, and are incorporated in Hong Kong and are under the supervision of the Hong Kong Monetary Authority (“HKMA”). The respective boards of directors are fully committed to adopting and implementing the principles and best practices in corporate governance as set out in the guidelines on “Corporate Governance of Locally Incorporated Authorised Institutions” issued by the HKMA. Specialised committees with clear terms of references and specific authorities delegated by the boards of directors have been set up by the Company, Public Finance and Public Bank (Hong Kong).

Directors’ Securities Transactions

The Company has adopted the code of conduct regarding directors’ securities transactions as set out in the Model Code for Securities Transactions by Directors of Listed Issuers (the “Model Code”) of the Listing Rules. All the directors have confirmed that they have complied with the required standards as set out in the Model Code throughout the year.

Board of Directors

The board of directors of the Company comprises:

Executive Directors	: Tan Yoke Kong Lee Huat Oon
Non-executive Directors	: Tan Sri Dato’ Sri Dr. Teh Hong Piow, <i>Chairman</i> Dato’ Sri Tay Ah Lek Dato’ Chang Kat Kiam Wong Kong Ming
Independent Non-executive Directors	: Tan Sri Dato’ Thong Yaw Hong, <i>Co-Chairman</i> (appointed on 1 July 2006) Dato’ Yeoh Chin Kee Lee Chin Guan Geh Cheng Hooi, Paul (resigned on 1 July 2006)

The non-executive directors provide the Group with a wide range of expertise and knowledge in the banking and finance sector. The independent non-executive directors are persons of high calibre; with academic and professional qualifications in the fields of accounting, law, banking and business management. With their experience gained from senior positions held in other companies, they provide strong support towards the effective discharge of the duties and responsibilities of the board. Each independent non-executive director has given an annual confirmation of his independence to the Company, and the Company considers these directors to be independent under Rule 3.13 of the Listing Rules.

Corporate Governance Report

Corporate Governance Practices (Continued)

Board of Directors (Continued)

During the year, eight full board meetings were held and the attendance of each director is set out as follows:

Name of director	Number of board meetings attended in 2006	Attendance rate
Tan Sri Dato' Sri Dr. Teh Hong Piow, <i>Chairman</i>	5/8	62.5%
Tan Sri Dato' Thong Yaw Hong, <i>Co-Chairman</i> (appointed on 1 July 2006)	3/4	75%
Tan Yoke Kong	7/8	87.5%
Lee Huat Oon	8/8	100%
Dato' Sri Tay Ah Lek	5/8	62.5%
Dato' Chang Kat Kiam	5/8	62.5%
Wong Kong Ming	8/8	100%
Dato' Yeoh Chin Kee	5/8	62.5%
Lee Chin Guan	6/8	75%
Geh Cheng Hooi, Paul (resigned on 1 July 2006)	3/4	75%

The board formulates overall strategy of the Group, monitors its financial performance and maintains effective oversight over the management. The board members are fully committed to their roles and have acted in good faith to maximize the shareholders' value in the long run, and have aligned the Group's goals and directions with the prevailing economic and market conditions. Daily operations and administration are delegated to the management.

The schedule of board meetings for a year is planned in the preceding year. At least 14 days notice of all board meetings is given to all directors and they can include matters for discussion in the agenda if the need arises. The Company Secretary assists the Chairman in preparing the agenda for meetings and ensures that all relevant rules and regulations are followed. The agenda and the accompanying board papers are sent to all directors at least 3 days before the date of every board meeting so that the directors have the time to review the documents. Minutes of every board meeting are circulated to all directors for their perusal prior to confirmation of the minutes at the following board meeting.

Every board member is entitled to have access to board papers and related materials and has unrestricted access to the advice and services of the Company Secretary, and has the liberty to seek external professional advice if so required. The Company Secretary continuously updates all directors on the latest development of the Listing Rules and other applicable regulatory requirements to ensure compliance and upkeep of good corporate governance practice.

Chairman, Co-Chairman and Chief Executive

The Chairman and the Chief Executive of the Company are Tan Sri Dato' Sri Dr. Teh Hong Piow and Mr. Tan Yoke Kong respectively. Tan Sri Dato' Thong Yaw Hong, an independent non-executive director, was appointed as the Co-Chairman of the Company on 14 July 2006 to share the workload of the Chairman.

Corporate Governance Report

Corporate Governance Practices (Continued)

Chairman, Co-Chairman and Chief Executive (Continued)

The roles of the Chairman and the Chief Executive are segregated and assumed by two separate individuals who have no relationship with each other. It is aimed at striking a balance of power and authority so that the job responsibilities are not concentrated on any one individual. The Chairman of the board is responsible for the leadership and effective running of the board, while the Chief Executive is delegated with the authorities to manage the business of the Group in all aspects effectively. The division of responsibilities between the Chairman and the Chief Executive have been clearly established and set out in writing.

Appointment and Re-election of Directors

The Company has not fixed the terms of appointment for non-executive directors. However, they are appointed subject to retirement by rotation and re-election at the annual general meeting of the Company in accordance with the provision of the Bye-laws. This deviates from the provision of A.4.1 of the Code on CGP which requires that non-executive directors be appointed for a specific term. The board has discussed and concluded that the current practice of appointing non-executive directors without specific terms but otherwise subject to rotation and re-election by shareholders is fair and reasonable, and does not intend to change the current practice at the moment.

In compliance with provision A.4.2 of the Code on CGP, the Company has amended its Bye-laws in March 2006 to the effect that any director appointed to fill casual vacancy be subject to election by shareholders at the first general meeting after his/her appointment, and every director, including those appointed for a specific term, be subject to retirement by rotation at least once every three years.

Remuneration Committee

The Remuneration Committee of the Company comprises two non-executive directors and three independent non-executive directors.

The Remuneration Committee was formed in January 2005 and meetings shall be held at least once a year. Two meetings were held in 2006. The attendance of each member is set out as follows:

Name of member	Number of meetings attended in 2006	Attendance rate
Tan Sri Dato' Sri Dr. Teh Hong Piow, <i>Chairman</i>	2/2	100%
Tan Sri Dato' Thong Yaw Hong (appointed on 1 July 2006)	1/1	100%
Dato' Sri Tay Ah Lek	2/2	100%
Dato' Yeoh Chin Kee	2/2	100%
Lee Chin Guan	2/2	100%
Geh Cheng Hooi, Paul (resigned on 1 July 2006)	1/1	100%

At the meetings held during the year, the directors' fees and meeting allowances of the Group for the year 2005 and the promotion, secondment and terms of employment of the management staff within the Group in 2006 were reviewed and noted.

The Company has adopted a share option scheme on 28 February 2002, which serves as an incentive to attract, retain and motivate talented eligible staff, including the directors. Details of the share option scheme are set out in note 36 to the financial statements. The emolument payable to directors will depend on their respective contractual terms under employment contracts, if any, and as recommended by the Remuneration Committee. Details of the directors' emoluments are set out in note 8 to the financial statements.

Corporate Governance Report

Corporate Governance Practices (Continued)

Remuneration Committee (Continued)

The major role and function of the Group's Remuneration Committee are as follows:

1. To review annually and recommend to the board the overall remuneration policy for the directors, the Chief Executive and key senior management officers.
2. To review annually the performance of the executive directors, the Chief Executive and key senior management officers and recommend to the board specific adjustments in remuneration and/or reward payments.
3. To ensure that the level of remuneration for non-executive directors and independent non-executive directors are linked to their level of responsibilities undertaken and contribution to the effective functioning of the boards of the respective companies in the Group.
4. To review and approve the compensation payable to executive directors, the Chief Executive and key senior management officers in connection with any loss or termination of their office or appointment.
5. To review and approve compensation arrangements relating to dismissal or removal of directors for misconduct.
6. To ensure that no director is involved in deciding his own remuneration.

The terms of reference of the Remuneration Committee are posted on the Company's website.

Nomination Committee

The Nomination Committee of the Company comprises two non-executive directors and three independent non-executive directors.

The Nomination Committee was formed in January 2005 and meetings shall be held at least once a year. Two meetings were held in 2006. The attendance of each member is set out as follows:

Name of member	Number of meetings attended in 2006	Attendance rate
Tan Sri Dato' Sri Dr. Teh Hong Piow, <i>Chairman</i>	2/2	100%
Tan Sri Dato' Thong Yaw Hong (appointed on 1 July 2006)	1/1	100%
Dato' Sri Tay Ah Lek	2/2	100%
Dato' Yeoh Chin Kee	2/2	100%
Lee Chin Guan	2/2	100%
Geh Cheng Hooi, Paul (resigned on 1 July 2006)	1/1	100%

At the meetings held during the year, the independence of Mr. Geh Cheng Hooi, Paul was assessed and the proposed re-election of Tan Sri Dato' Sri Dr. Teh Hong Piow and Dato' Sri Tay Ah Lek as non-executive directors at the 2006 annual general meeting was recommended. In addition, the changes of management staff in Public Finance and Public Bank (Hong Kong) were noted and the mechanisms for annual assessment of the board and each individual directors were adopted.

Corporate Governance Report

Corporate Governance Practices (Continued)

Nomination Committee (Continued)

The major role and function of the Group's Nomination Committee are as follows:

1. To assess and recommend the appointment and re-appointment of directors and Chief Executive to the board.
2. To oversee the overall composition of the board, in terms of the appropriate size and skills, and the balance between executive directors, non-executive directors and independent non-executive directors through annual review.
3. To assess the independence of independent non-executive directors.
4. To establish a mechanism for the formal assessment on the effectiveness of the board as a whole and the performances of each director, the Chief Executive and other key senior management officers.
5. To oversee the appointment, management succession planning and performance evaluation of key senior management officers.

The terms of reference of the Nomination Committee are posted on the Company's website.

Accountability and Audit

The directors are responsible for overseeing the preparation of accounts of each financial period, which give a true and fair view of the state of affairs of the Group and of the results and cash flow for that period. In preparing the accounts for the year ended 31 December 2006, the directors have selected suitable accounting policies and have applied them consistently, adopted appropriate Hong Kong Financial Reporting Standards and Hong Kong Accounting Standards which are pertinent to its operations and relevant to the financial statements, made judgements and estimates that are prudent and reasonable, and have prepared the accounts on the going concern basis.

Audit Committee

The Audit Committee of the Company comprises one non-executive director and three independent non-executive directors.

The Audit Committee shall meet at least twice a year. Five meetings were held during the year. The minutes of the Audit Committee meetings were tabled to the board for noting and for action by the board where appropriate. The attendance of each member is set out as follows:

Name of member	Number of meetings attended in 2006	Attendance rate
Tan Sri Dato' Thong Yaw Hong, <i>Chairman</i> (appointed on 1 July 2006)	3/3	100%
Dato' Yeoh Chin Kee	4/5	80%
Dato' Sri Tay Ah Lek	5/5	100%
Lee Chin Guan	5/5	100%
Geh Cheng Hooi, Paul (resigned on 1 July 2006)	2/2	100%

Corporate Governance Report

Accountability and Audit (Continued)

Audit Committee (Continued)

During the meetings held in 2006, the Audit Committee had performed the following work:

- (i) reviewed the financial reports for the year ended 31 December 2005 and for the six months ended 30 June 2006;
- (ii) reviewed the findings and recommendations of the Internal Audit Departments on the operations and performance of the branches and departments of Public Finance, Public Bank (Hong Kong) and other subsidiaries of the Group;
- (iii) reviewed the effectiveness of internal control system;
- (iv) reviewed the examination reports on Public Finance issued by the regulatory authorities, and the audit report on the examination of the computer centre and network operations of Public Finance issued by the Internal Auditors of Public Bank Berhad;
- (v) reviewed the external auditors' statutory audit plan and engagement letter;
- (vi) reviewed the management letter from the external auditors in relation to the audit of the Group for the year ended 31 December 2005;
- (vii) reviewed and recommended for approval by the board the 2006 audit scope and fees; and
- (viii) reviewed the connected transactions entered into by the Group during the year.

The major role and function of the Group's Audit Committee are as follows:

- 1. To consider the appointment of the external auditors, the audit fees, and any questions of resignation or dismissal of the external auditors of the Group.
- 2. To discuss with the external auditors the nature and scope of the audit.
- 3. To review the interim and annual financial statements before submission to the board of directors.
- 4. To discuss problems and reservations arising from the interim audit review and final audits, and any matters the auditors may wish to discuss.
- 5. To review the external auditors' management letters and management's response.
- 6. To review the Group companies' statements on internal control systems (where one is included in the annual report) prior to endorsement by the respective boards of directors.
- 7. To review the internal audit programme, ensure co-ordination between the internal and external auditors, and ensure that the internal audit function is adequately resourced and has appropriate standing within the Group.
- 8. To consider the major findings of internal investigations and management's response.

The terms of reference of the Audit Committee are posted on the Company's website.

Corporate Governance Report

Accountability and Audit (Continued)

Auditors' Remuneration

During the year under review, the remuneration paid/payable to the Company's auditors, Messrs Ernst & Young, is set out as follows:

Services rendered	Fees paid/payable HK\$'000
Audit services	2,950
Non-audit services	1,513
Total:	<u>4,463</u>

Internal Control

The board is responsible for the Group's system of internal controls and its effectiveness. However, such a system is designed to manage the Group's risks within an acceptable risk profile, rather than to eliminate the risk of failure to achieve the policies and business objectives of the Group. Accordingly, it can only provide reasonable assurance but not absolute assurance against material misstatement of management and financial information and records or against financial losses or fraud.

The board has established an on-going process for identifying, evaluating and managing the significant risks faced by the Group and this process includes updating the system of internal controls when there are changes to business environment or regulatory guidelines.

The board is of the view that the system of internal controls in place for the year under review and up to the date of issuance of the annual report and financial statements is sound and is sufficient to safeguard the interests of shareholders, customers and employees, and the Group's assets.

The management assists the board in the implementation of the board's policies and procedures on risk and control by identifying and assessing the risks faced, and involving in the design, operation and monitoring of suitable internal controls to mitigate and control these risks.

The key processes that have been established in reviewing the adequacy and integrity of the system of internal controls include the following:

- The Board Executive Committees under Public Finance and Public Bank (Hong Kong) consist of executive directors and non-executive directors and are responsible for the management of the businesses of Public Finance and Public Bank (Hong Kong) in all aspects and the implementation of strategic business plans and policies approved and formulated by the respective boards of directors.
- The Management Committees are established by the respective boards of Public Finance and Public Bank (Hong Kong) to ensure the effectiveness of the Group's daily operations and that the Group's operations are in accordance with the corporate objectives, strategies and the annual budget as well as the policies and business directions that have been approved.
- The Audit Committees are established at the Group level as well as at the bank level to review internal control issues identified by the Internal Audit Departments, external auditors, regulatory authorities and management, and evaluate the adequacy and effectiveness of the Group's risk management and internal control systems. They also conduct review of the internal audit functions with particular emphasis on the scope of audits, quality of internal audits and independence of the Internal Audit Departments. The minutes of the Audit Committee meetings are tabled to the board for noting and further action, where appropriate.

Corporate Governance Report

Accountability and Audit (Continued)

Internal Control (Continued)

- The Internal Audit Departments monitor compliance with policies and procedures and the effectiveness of the internal control systems, and highlight significant findings in respect of any non-compliance. Audits are carried out on all branches, the frequency of which is determined by the level of risk assessed, to provide an independent and objective report on the operational and management activities of these branches. The annual audit plan of the Group is reviewed and approved by the Audit Committee and the findings of the audits are submitted to the Audit Committee for review.
 - The Credit Committees under Public Finance and Public Bank (Hong Kong) are responsible for making decision on loan applications for all types of loan facilities within its discretionary powers, assisting the respective boards of directors in formulating policy guidelines for Public Finance's and Public Bank (Hong Kong)'s lending business, and recommending applications for loan facilities exceeding the discretionary powers of the Credit Committees to the respective boards for approval.
 - The Assets and Liabilities Committee under Public Finance and the Asset and Liability Management Committee under Public Bank (Hong Kong) review and assess the risk profile and capital structure of Public Finance and Public Bank (Hong Kong), set the objectives for the asset and liability management function and implement the risk management policies approved by the respective boards of Public Finance and Public Bank (Hong Kong).
 - Operational committees have also been established under Public Finance and Public Bank (Hong Kong) with appropriate authorities to ensure effective management and supervision of the Group's core areas of business operations. These committees include the Human Resources Committees and the Information Technology Committees.
- The Human Resources Committees assist the respective boards of directors in formulating and implementing human resources policies including staff recruitment, promotion, career development, performance appraisal and remuneration of all staff.
- The Information Technology Committee under Public Finance and Information Technology (I.T.) Steering Committee under Public Bank (Hong Kong) are responsible for establishing objectives, policies and strategies for the computerisation of the Group, recommending to the respective boards on major acquisitions of computer hardware and software, and monitoring the progress of implementation of all information technology related projects.
 - The Finance Committees under Public Finance and Public Bank (Hong Kong) assist the respective boards of directors in the financial planning and budgeting process of the business of Public Finance and Public Bank (Hong Kong) and the review of the business performance, statutory and half year accounts.
 - Compliance Working Group of Public Finance and Compliance Department of Public Bank (Hong Kong) are established to review the relevant policies and guidelines issued from time to time by the HKMA and other regulatory authorities, to assess the impact of the relevant regulatory requirements on Public Finance and Public Bank (Hong Kong) and to ensure that the relevant business units and/or departments comply with the relevant regulatory requirements and internal policy guidelines of business units and departments.

Corporate Governance Report

Management of Risks

The respective boards of directors of the subsidiaries are responsible for the oversight of risks and approval of risk management policies. The Internal Audit Departments perform regular audits to ensure compliance with the policies and reports directly to the respective Audit Committees. In addition, various committees were formed to mitigate and monitor various kinds of risks within the Group. In 2006, the Risk Management Committee of the Company was established to oversee the overall management of all risks covering market risk management, liquidity risk management, credit risk management and operational risk management of the Group.

Credit Risk

Credit risk is the risk associated with a customer or counterparty being unable to meet a commitment when it falls due, and arises from the lending, trade finance, treasury and other activities undertaken by the Group.

The Group has established policies and systems for the monitoring and control of credit risk. These policies define the credit extension and measurement criteria, the credit review, approval and monitoring processes, and the loan classification and the level of impairment allowances for impaired loans. It has a hierarchy of credit authorities which approve credits in compliance with the respective subsidiaries' credit policies; exposures are monitored against credit limits and other control limits (such as large exposures and concentration limits); segregation of duties in key credit functions is in place to ensure separate credit control and monitoring; management and recovery of problem credits are handled by an independent workout team.

The Group manages its credit risk within a conservative framework. The credit policies are regularly reviewed, taking into account factors such as prevailing business and economic conditions, regulatory requirements and capital resources.

Credit and compliance audits are periodically held to evaluate the effectiveness of the credit review, approval and monitoring processes and to test the compliance of established credit policies and procedures.

The Credit Risk Management Committee of Public Bank (Hong Kong) is responsible for establishing the framework for identifying, measuring, monitoring and controlling credit risk of existing and new products, and approving credit risk management policies and credit risk tolerable limits as and when necessary. It reports to the Risk Management Committee of the Company.

Market Risk

Market risk is the risk to the Group's earnings and capital due to changes in the market level of interest rates, securities, foreign exchange and equities as well as the volatilities of those prices.

The Group monitors market risk principally by limits established for transactions and open positions. These limits are reviewed and approved by the directors of the respective subsidiaries, and are monitored on a daily basis.

The Assets and Liabilities Committee of Public Finance and the Asset and Liability Management Committee of Public Bank (Hong Kong) meet regularly to review the balance sheet structure, interest rate risk management, liquidity management, and capital structure, allocation and planning. They evaluate the impact of alternative asset and liability management strategies, identify the types of risks inherent in Public Finance and Public Bank (Hong Kong) and assess the vulnerability of the net interest income to these risks. The latest development in interest rates and foreign exchange rate movements, fiscal and monetary policies will be brought to the attention of the respective boards of directors. All foreign exchange positions are managed by the Treasury Department of Public Bank (Hong Kong) within limits approved by its board of directors.

Corporate Governance Report

Management of Risks (Continued) Liquidity Risk

The main objectives of the Group's liquidity risk management are to ensure the availability of funds at reasonable costs to meet all contractual financial commitments, to fund loan growth and to generate reasonable returns from available funds.

The Assets and Liabilities Committee of Public Finance and the Asset and Liability Management Committee of Public Bank (Hong Kong) monitor the liquidity position as part of the ongoing assets and liabilities management, and set up trigger limits to monitor liquidity risk. They also closely monitor the liquidity of the respective subsidiaries on a periodic basis to ensure that the liquidity structure of the respective subsidiaries' assets, liabilities and commitments can meet the funding needs, and that the statutory liquidity ratio is always complied with. Standby facilities are maintained to provide liquidity to meet unexpected, material cash outflows in the ordinary course of business.

Operational Risk

Operational risk relates to the risk of loss resulting from inadequate or failed internal processes, people or systems, or from external events. Operational Risk Management Committees have been established under Public Finance and Public Bank (Hong Kong) to implement the operational risk management framework approved by the respective boards of directors and to develop specific policies, processes and procedures for managing operational risk in the material products, activities, processes and systems. They report to the Risk Management Committee of the Company.

Communications with Shareholders and Investors

The board recognises the importance of good communications with all shareholders. The Company's annual general meeting ("AGM") is a valuable forum for the board to communicate directly with the shareholders. The Chairman of the board as well as Chairmen of the Audit, Nomination and Remuneration Committees together with the external auditors are present to answer shareholders' questions. An AGM circular is distributed to all shareholders at least 21 days before the AGM. It sets out the procedures for demanding and conducting a poll and other relevant information of the proposed resolutions. The Chairman explains the procedures for demanding and conducting a poll again at the beginning of the AGM and (except where a poll is demanded) reveals how many proxies for and against have been filed in respect of each resolution. The results of the poll, if any, will be published in the newspapers and on the Company's website.

A key element of effective communication with shareholders and investors is the prompt and timely dissemination of information in relation to the Group. The Company has announced its annual and interim results in a timely manner within 20 days after the end of the relevant periods in 2006, which were well before the time limits as laid down in the Listing Rules.

The management personnel responsible for investor relations held regular meetings with equity research analysts, fund managers and institutional shareholders and investors.

The amendments to the Bye-laws of the Company were approved in the 2006 AGM to reflect the changes brought by the new Listing Rules effective on 1 January 2005.

The market capitalisation of the Company as at 29 December 2006 was HK\$6,727,464,201 (issued share capital: 1,093,896,618 shares at closing market price: HK\$6.15 per share). The public float is around 26.5%.

The 2007 AGM will be held at Shek O Room, Lower Level I, Kowloon Shangri-La Hotel, 64 Mody Road, Kowloon, Hong Kong on Tuesday, 13 March 2007 at 10:00 a.m.

Brief Biography of Directors and Senior Management

Directors

Tan Sri Dato' Sri Dr. Teh Hong Piow

Tan Sri Dato' Sri Dr. Teh Hong Piow, aged 76, is the founder and the Chairman and is a substantial shareholder of Public Bank, a commercial bank listed on Bursa Malaysia Securities Berhad and the holding company of the Company. He has 57 years of experience in the banking and finance industry. He was appointed a Non-executive Director and the Chairman of the Company in September 1991. He is currently the Chairman of the Remuneration Committee and the Nomination Committee of the Company. He is also the Executive Chairman of Public Bank (Hong Kong) and the Non-executive Chairman of Public Finance. He also holds directorships in several other companies in the Public Bank Group.

He had served in various capacities in public service bodies in Malaysia; he was a member of the Malaysian Business Council from 1991 to 1993; a member of the National Trust Fund from 1988 to 2001; a founder member of the Advisory Business Council since 2003; and is a member of the IPRM Accreditation Privy Council of Malaysia. He is a Fellow of several institutes which include the Institute of Bankers Malaysia; the Chartered Institute of Bankers, United Kingdom; the Institute of Administrative Management, United Kingdom; the Institute of Chartered Secretaries and Administrators, Australia; and the Malaysian Institute of Management.

Tan Sri Dato' Thong Yaw Hong

Tan Sri Dato' Thong Yaw Hong, aged 76, was appointed an Independent Non-executive Co-Chairman of the Company in July 2006 and is the Chairman of the Audit Committee and Risk Management Committee, and a member of the Remuneration Committee and Nomination Committee. He is the Independent Non-executive Co-Chairman of Public Bank and Public Bank (Hong Kong). He also holds directorships in several other companies in the Public Bank Group.

He graduated with a Bachelor of Arts (Hons) degree in Economics from University of Malaya and a Master's degree in Public Administration from Harvard University. He attended the Advanced Management Program at Harvard Business School. In September 2006, he was conferred the Doctor of Economics (Honorary) from University Putra Malaysia.

He has had a distinguished career with the Government of Malaysia, primarily in the fields of socio-economic development planning and finance. He had served in the Economic Planning Unit in the Prime Minister's Department since 1957 and became its Director-General from 1971 to 1978 and served as Secretary-General, Ministry of Finance from 1979 until his retirement in 1986.

Mr. Tan Yoke Kong

Mr. Tan Yoke Kong, aged 54, has more than 25 years of experience in the banking and finance industry. He was appointed an Executive Director of the Company in February 1992 and is the Chief Executive/Executive Director of Public Bank (Hong Kong) and an Executive Director of Public Finance. He is a member of the Risk Management Committee of the Company. Mr. Tan is a Fellow of the Association of Chartered Certified Accountants, United Kingdom and an Associate of the Institute of Chartered Secretaries and Administrators, United Kingdom. He is currently the Vice-chairman of The DTC Association in Hong Kong.

Brief Biography of Directors and Senior Management

Directors (Continued)

Mr. Lee Huat Oon

Mr. Lee Huat Oon, aged 44, has more than 19 years of experience in the banking and finance industry. He was appointed an Executive Director of the Company in June 1996 and is currently the General Manager/Chief Executive and an Executive Director of Public Finance. He holds a degree in Accounting from the University of Malaya and is a Registered Accountant with the Malaysian Institute of Accountants.

Dato' Sri Tay Ah Lek

Dato' Sri Tay Ah Lek, aged 64, has 46 years of experience in the banking and finance industry. He was appointed a Non-executive Director of the Company in January 1995 and is a member of the Audit Committee, Remuneration Committee, Nomination Committee and Risk Management Committee. He is the Managing Director of Public Bank and a Non-executive Director of Public Bank (Hong Kong). He also holds directorships in several other companies in the Public Bank Group.

He holds a Master's degree in Business Administration from Henley, United Kingdom and attended the Advanced Management Program at Harvard Business School. He is a Fellow of the Financial Services Institute of Australasia, the Institute of Bankers Malaysia and the Malaysian Institute of Management.

He is presently the Chairman of the Association of Finance Companies of Malaysia and Honorary Advisor to the Association of Hire Purchase Companies Malaysia. He is a Council Member of the National Economic Action Council and the National Payments Advisory Board in Malaysia.

Dato' Chang Kat Kiam

Dato' Chang Kat Kiam, aged 52, has 32 years of experience in the banking and finance industry. He was appointed a Non-executive Director of the Company in March 2004. He is also a Non-executive Director of Public Bank (Hong Kong) and Public Finance and a member of the Risk Management Committee of the Company. He is currently the Chief Operating Officer of Public Bank. He also holds directorships in several other companies in the Public Bank Group. He is a holder of Masters in Business Administration degree.

Mr. Wong Kong Ming

Mr. Wong Kong Ming, aged 53, has over 31 years of experience in the banking and finance industry. He was appointed a Non-executive Director of the Company in June 1996. He is also the General Manager of Public Bank, Hong Kong Branch and a Non-executive Director of Public Finance. He is an Associate of the Chartered Institute of Bankers, United Kingdom; the Institute of Bankers Malaysia and the Malaysian Institute of Management. He is a holder of Master of Business Administration degree.

Dato' Yeoh Chin Kee

Dato' Yeoh Chin Kee, aged 64, has 46 years of experience in the banking and finance industry. He was appointed an Independent Non-executive Director of the Company in September 2002 and is a member of the Audit Committee, Remuneration Committee, Nomination Committee and Risk Management Committee. He is also an Independent Non-executive Director of Public Bank and Public Bank (Hong Kong). He also holds directorships in several other companies in the Public Bank Group. He is a Fellow of the Australian Society of Certified Practising Accountants and the Financial Services Institute of Australasia.

Brief Biography of Directors and Senior Management

Directors (Continued)

Mr. Lee Chin Guan

Mr. Lee Chin Guan, aged 48, has 14 years of experience in the legal practice, principally in commercial and corporate matters. He was appointed an Independent Non-executive Director of the Company in September 2004 and is a member of the Audit Committee, Remuneration Committee, Nomination Committee and Risk Management Committee. He is also an Independent Non-executive Director of Public Bank and Public Bank (Hong Kong). He also holds directorships in several other companies in the Public Bank Group. He qualified as a Barrister-at-Law from the Middle Temple, United Kingdom in 1982. He also holds a Bachelor Degree in Science (Hons) from the University of Manchester Institute of Science and Technology, England and Degrees in Law from Cambridge University, Oxford University and University of Chicago Kent College of Law.

Senior Management

Mr. Chong Yam Kiang

Mr. Chong Yam Kiang, aged 56, has more than 37 years of experience in the banking and finance industry. He was appointed an Executive Director of Public Bank (Hong Kong) in May 2006 and is currently the Alternate Chief Executive of Public Bank (Hong Kong). He holds a diploma in Management from Malaysian Institute of Management.

Our Corporate Family



The Group Chairman, Tan Sri Dato' Sri Dr. Teh Hong Piow, delivered his opening address at the Group's Annual Dinner 2006.



Staff performing at the Group's Annual Dinner 2006 took a photo with members of the Board of Directors.



The Board of Directors at the Company's 2006 Annual General Meeting and Special General Meeting held at JW Marriott Hotel Hong Kong on 8 March 2006.



Mr. Tan Yoke Kong, Chief Executive, and Mr. Chong Yam Kiang, Alternate Chief Executive, of Public Bank (Hong Kong) at the press conference to announce the change of name of Asia Commercial Bank Limited to Public Bank (Hong Kong) Limited.



Senior management of Public Bank (Hong Kong) at the staff briefing on the new corporate name and identity.

Our Corporate Family



Mr. Tan Yoke Kong presented a birthday gift to our Group Chairman in celebration of his grand 76th birthday at JW Marriott Hotel Hong Kong.



Tan Sri Dato' Sri Dr. Teh Hong Piow, the Group Chairman, accompanied by members of the board, cut the birthday cake after making his birthday wish.



Staff paying attention to the instructor at the Management Seminar 2006 held at the Aberdeen Marine Club in November 2006.



Group photo of our staff and family members taken during the Group Annual Outing to Shenzhen, Dongguan and Panyu, China in November 2006.



Our staff members participating at the Corporate Games 2006 Sports Day.



Participants of the Corporate Games 2006 Distance Run event.



Group photo taken at the Inter-house Basketball Competition 2006 organised by the Sports Club.

Report of the Directors

The directors present their report and the audited financial statements of the Company and of the Group for the year ended 31 December 2006.

Change of name

Pursuant to a special resolution passed at the annual general meeting of the Company held on 8 March 2006 and as approved by the Registrar of Companies of the Bermuda, the name of the Company has been changed from JCG Holdings Limited to Public Financial Holdings Limited with effect from 20 March 2006.

Principal activities

The Company is an investment holding company. The principal activities of its subsidiaries during the year were deposit taking, personal and commercial lending, mortgage financing, stockbroking, the letting of investment properties, the provision of finance to purchasers of taxis and public light buses, the trading of taxi cabs and taxi licences, and the leasing of taxis. After the completion of the acquisition of the entire issued and paid-up share capital of Public Bank (Hong Kong) Limited (formerly known as "Asia Commercial Bank Limited") during the year, the Group's principal activities also included the provision of a comprehensive range of banking, financial and related services.

Details of the principal activities of the Company's subsidiaries are set out in note 22 to the financial statements.

Results and dividends

The Group's profit for the year ended 31 December 2006 and the state of affairs of the Company and of the Group at that date are set out in the financial statements on pages 42 to 109.

The first interim dividend of HK\$0.05 (2005: HK\$0.06 and a special dividend of HK\$0.29) per ordinary share was paid on 24 August 2006. The second interim dividend of HK\$0.20 (2005: HK\$0.40) per ordinary share was declared on 22 December 2006 and will be payable on 14 February 2007 to shareholders of the Company whose names appear on the register of members on 8 February 2007. The directors do not recommend the payment of a final dividend for the year (2005: Nil).

A summary of the results and of the assets and liabilities of the Group for the last five financial years is set out on pages 8 to 9.

Investment properties, property, plant and equipment and land lease prepayments

Details of movements in the investment properties, property, plant and equipment and land lease prepayments of the Company and of the Group are set out in notes 19, 20, and 21 to the financial statements, respectively.

Rights issue

On 17 February 2006, the Company passed a board resolution to make a rights issue of not less than 364,632,206 rights shares and not more than 386,571,206 rights shares to shareholders at HK\$7.30 per share on the basis of one rights share for every two shares held on 17 March 2006 (the "Rights Issue"). Pursuant to the Rights Issue, 364,632,206 ordinary shares of HK\$0.10 each were issued at HK\$7.30 per share. None of the directors had subscribed for the rights shares under the Rights Issue except for Tan Sri Dato' Sri Dr. Teh Hong Piow who, by virtue of his direct and indirect interests in Public Bank, is also deemed to be interested in the shares in the Company to the extent that Public Bank has interests. Public Bank had accepted its entitlement of 233,384,055 rights shares and subscribed for all the 131,021,755 rights shares that had not been taken up pursuant to its obligations under the underwriting agreement dated 17 February 2006. The net proceeds from the Rights Issue, after deduction of related expenses, of approximately HK\$2,660,504,000, were used to pay the consideration of acquiring Public Bank (Hong Kong) Limited.

Report of the Directors

Share capital and share options

Details of movements of the Company's share capital and share options are set out in notes 35 and 36 to the financial statements, respectively.

Pre-emptive rights

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

Purchase, sale or redemption of listed shares of the Company

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

Reserves

Details of movements in the reserves of the Company and of the Group during the year are set out in note 38 to the financial statements and the consolidated summary statement of changes in equity.

Distributable reserves

The Company's contributed surplus is distributable to shareholders in accordance with the Companies Act 1981 of Bermuda. At 31 December 2006, the Company's reserves available for cash distribution and/or distribution in specie amounted to approximately HK\$226,351,000 (inclusive of the Company's contributed surplus) as computed in accordance with generally accepted accounting principles of Hong Kong, SAR. In addition, the Company's share premium account in the amount of approximately HK\$3,988,219,000 may be distributed in the form of fully paid bonus shares.

Major customers and suppliers

In the year under review, income attributable to the Group's five largest customers accounted for less than 30% of the total income for the year. Purchases from the Group's five largest suppliers accounted for less than 30% of the total purchases for the year.

Directors

The directors of the Company during the year were as follows:

Non-executive Directors:

Tan Sri Dato' Sri Dr. Teh Hong Piow, *Chairman*
Dato' Sri Tay Ah Lek
Dato' Chang Kat Kiam
Wong Kong Ming

Executive Directors:

Tan Yoke Kong
Lee Huat Oon

Independent Non-executive Directors:

Tan Sri Dato' Thong Yaw Hong, *Co-Chairman*
(Appointed on 1 July 2006)
Dato' Yeoh Chin Kee
Lee Chin Guan
Geh Cheng Hooi, Paul (Resigned on 1 July 2006)

In accordance with the Bye-laws, Tan Sri Dato' Thong Yaw Hong, Dato' Yeoh Chin Kee and Mr. Wong Kong Ming shall retire by rotation and, being eligible, will offer themselves for re-election at the forthcoming annual general meeting.

Report of the Directors

Directors' remuneration and the five highest paid individuals

Details of directors' remuneration and those of the five highest paid individuals in the Group are set out in notes 8 and 9 to the financial statements, respectively.

Directors' service contracts

No director proposed for re-election at the forthcoming annual general meeting has a service contract with the Company or any of its subsidiaries which is not determinable by the Group within one year without payment of compensation other than statutory compensation.

Directors' interests in contracts

Except as detailed in note 43 to the financial statements and in the section headed "Connected transactions" below, no director had a beneficial interest, either directly or indirectly, in any contract of significance to the business of the Group to which the Company, its holding company or any of its subsidiaries and fellow subsidiaries was a party at the balance sheet date or at any time during the year.

Loan agreement with covenants relating to specific performance of the controlling shareholder

On 21 July 2006, the Company entered into a facility agreement (the "Facility Agreement") with Barclays Capital and others as mandated lead arrangers and Barclays Bank PLC as agent and financial institutions as stipulated in the Company's announcement dated 21 July 2006 as the original lenders for a 3-year term loan facility in an aggregate amount of HK\$2,000,000,000 (the "Facility").

The Facility Agreement provides, among other things, that it is an event of default if Public Bank Berhad, the controlling shareholder (currently holding approximately 73.5% interest) of the Company, does not or ceases to beneficially own, directly or indirectly, at least 51% of the issued share capital of, and ownership interests in, the Company free from any charge or other security interest, or does not or ceases to exercise management control over the Company.

If an event of default occurs, Barclays Bank PLC as agent may, among other things, demand immediate repayment of all or any of the loans made to the Company together with accrued interest.

As at 31 December 2006, the Facility was fully utilised and the circumstances giving rise to the obligation under Rule 13.18 of the Rules Governing the Listing of Securities (the "Listing Rules") on The Stock Exchange of Hong Kong Limited (the "Stock Exchange") continue to exist.

Report of the Directors

Directors' interests and short positions in shares and underlying shares

At the balance sheet date, the directors' interests and short positions in the shares and underlying shares of the Company or any of 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 otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") were as follows:

(a) Long positions in ordinary shares of the Company and associated corporations

Interests in	Name of director	Number of ordinary shares			Total	Percentage of interest in issued share capital
		Directly beneficially owned	Through spouse or minor children	Through controlled corporation		
1. The Company	Tan Sri Dato' Sri Dr. Teh Hong Piow	-	-	804,017,920	804,017,920	73.5004
	Tan Sri Dato' Thong Yaw Hong	498,000	-	-	498,000	0.0455
	Dato' Yeoh Chin Kee	80,000	-	-	80,000	0.0073
	Tan Yoke Kong	80,000	-	-	80,000	0.0073
	Lee Huat Oon	20,000	-	-	20,000	0.0018
2. Public Bank Berhad ("Public Bank"), the ultimate holding company	Tan Sri Dato' Sri Dr. Teh Hong Piow	21,524,250	-	786,468,596	807,992,846	23.3333
	Tan Sri Dato' Thong Yaw Hong	5,518,750	300,000	312,500	6,131,250	0.1771
	Dato' Sri Tay Ah Lek	7,810,109	-	139,482	7,949,591	0.2296
	Dato' Yeoh Chin Kee	200,000	400,000	-	600,000	0.0173
	Lee Chin Guan	1,200,000	-	-	1,200,000	0.0347
	Dato' Chang Kat Kiam	56,435	-	-	56,435	0.0016
	Tan Yoke Kong	15,000	-	-	15,000	0.0004
	Lee Huat Oon	5,000	-	-	5,000	0.0001
3. Winsure Company, Limited, a subsidiary	Wong Kong Ming	176,386	-	-	176,386	0.0051
	Tan Sri Dato' Sri Dr. Teh Hong Piow	-	-	15,500	15,500	96.8750

Tan Sri Dato' Sri Dr. Teh Hong Piow, by virtue of his total direct and indirect interests of 807,992,846 shares in Public Bank, is deemed to be interested in the shares in the Company and its associated corporations as disclosed above, to the extent that Public Bank has interests.

Report of the Directors

Directors' interests and short positions in shares and underlying shares
(Continued)

(b) Long positions in underlying shares of the Company and an associated corporation

Interests in	Name of director	Number of ordinary shares attached to the share options				Exercise price	Exercise period
		At the beginning of the year	Granted during the year	Exercised during the year	At the end of the year		
1. The Company	Dato' Sri Tay Ah Lek	1,680,000	–	–	1,680,000	HK\$6.35	10.6.2005 to 9.6.2015
	Dato' Yeoh Chin Kee	700,000	–	–	700,000	HK\$6.35	10.6.2005 to 9.6.2015
	Lee Chin Guan	350,000	–	–	350,000	HK\$6.35	10.6.2005 to 9.6.2015
	Dato' Chang Kat Kiam	1,680,000	–	–	1,680,000	HK\$6.35	10.6.2005 to 9.6.2015
	Tan Yoke Kong	1,928,000	–	–	1,928,000	HK\$6.35	10.6.2005 to 9.6.2015
	Lee Huat Oon	3,170,000	–	–	3,170,000	HK\$6.35	10.6.2005 to 9.6.2015
	Wong Kong Ming	4,000,000	–	–	4,000,000	HK\$6.35	10.6.2005 to 9.6.2015
2. Public Bank	Tan Sri Dato' Thong Yaw Hong	2,000,000*	–	–	2,000,000	RM6.37	24.2.2005 to 24.2.2008
		500,000*	–	500,000	–	RM5.67	5.12.2005 to 24.2.2008
		2,500,000*	–	500,000	2,000,000		
	Dato' Sri Tay Ah Lek	4,500,000	–	–	4,500,000	RM6.37	24.2.2005 to 24.2.2008
		4,000,000	–	4,000,000	–	RM5.67	5.12.2005 to 24.2.2008
		8,500,000	–	4,000,000	4,500,000		
	Dato' Yeoh Chin Kee	2,025,000	–	–	2,025,000	RM6.37	24.2.2005 to 24.2.2008
		2,250,000	–	250,000	2,000,000	RM5.67	5.12.2005 to 24.2.2008
		4,275,000	–	250,000	4,025,000		
	Lee Chin Guan	1,125,000	–	–	1,125,000	RM6.37	24.2.2005 to 24.2.2008
		1,250,000	–	600,000	650,000	RM5.67	5.12.2005 to 24.2.2008
		2,375,000	–	600,000	1,775,000		

Report of the Directors

Directors' interests and short positions in shares and underlying shares (Continued)

(b) Long positions in underlying shares of the Company and an associated corporation (Continued)

Interests in	Name of director	Number of ordinary shares attached to the share options				Exercise price	Exercise period
		At the beginning of the year	Granted during the year	Exercised during the year	At the end of the year		
2. Public Bank (continued)	Dato' Chang Kat Kiam	123,000	-	-	123,000	RM6.37	24.2.2005 to 24.2.2008
		130,000	-	-	130,000	RM5.67	5.12.2005 to 24.2.2008
		253,000	-	-	253,000		
	Tan Yoke Kong	30,000	-	-	30,000	RM6.37	15.2.2005 to 24.2.2008
		40,000	-	-	40,000	RM5.67	5.12.2005 to 24.2.2008
		70,000	-	-	70,000		
	Lee Huat Oon	20,000	-	-	20,000	RM6.37	15.2.2005 to 24.2.2008
		30,000	-	-	30,000	RM5.67	5.12.2005 to 24.2.2008
		50,000	-	-	50,000		
	Wong Kong Ming	8,000	-	-	8,000	RM4.92	17.6.2004 to 24.2.2008
		10,000	-	-	10,000	RM6.37	16.2.2005 to 24.2.2008
		25,000	-	-	25,000	RM5.67	5.12.2005 to 24.2.2008
43,000		-	-	43,000			

* At the date of appointment

Notes:

- The options to subscribe for ordinary shares of HK\$0.10 each in the Company under the Share Option Scheme of the Company (the "Scheme") are only exercisable during certain periods as notified by the board or the Share Option Committee to each grantee which it may in its absolute discretion determine from time to time before the expiry of the share options on 9 June 2015.
- The exercise price of the share options under the Scheme has been adjusted to HK\$6.35 per share following the completion of the Rights Issue.
- The options to subscribe for ordinary shares of RM1.00 each in Public Bank were first granted on 10 April 1998 under the Public Bank Berhad Employees' Share Option Scheme (the "PBB ESOS"). Following approvals from the relevant authorities and the shareholders of Public Bank at the extraordinary general meetings held on 20 May 2002, 20 April 2004 and 30 March 2005, the PBB ESOS has been extended for a total of five years to 25 February 2008. Hence, the exercise period of the options has also been extended up to and including 24 February 2008. The options are exercisable subject to the terms of the PBB ESOS.

Report of the Directors

Directors' interests and short positions in shares and underlying shares (Continued)

(b) Long positions in underlying shares of the Company and an associated corporation (Continued)

Save as disclosed above, none of the directors had registered an interest or short position in the shares, or underlying shares of the Company or any of its associated corporations that was required to be recorded under Section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code as at the balance sheet date.

Directors' rights to acquire shares or debentures

Apart from the share option schemes and the Rights Issue disclosed above and set out in note 36 to the financial statements, at no time during the year was the Company, its holding company or any of its subsidiaries and fellow subsidiaries a party to any arrangement to enable the Company's directors, their respective spouse or minor children to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or in any other body corporate.

Directors' interests in competing businesses

Tan Sri Dato' Sri Dr. Teh Hong Piow and Dato' Sri Tay Ah Lek are also directors of Public Bank, which is also engaged in the provision of financing for licensed public vehicles, mortgage loans and the taking of deposits from customers in Hong Kong through its fully licensed branch in Hong Kong.

Tan Sri Dato' Sri Dr. Teh Hong Piow is deemed to be a substantial shareholder of Public Bank by virtue of his interest in Public Bank.

The provision of financing for licensed public vehicles undertaken by Public Bank, Public Finance Limited ("Public Finance") and Public Bank (Hong Kong) Limited ("Public Bank (Hong Kong)") during the year was referred by a wholly-owned subsidiary, Winton Motors, Limited ("Winton Motors") and other taxi dealers. The terms and conditions of the taxi financing loans are market driven and agreed at arm's length between the hirers and the financiers. The terms and conditions of other businesses of Public Finance, Public Bank (Hong Kong) and Public Bank, Hong Kong Branch are also market driven.

Report of the Directors

Substantial shareholders' and other persons' interests and short positions in shares and underlying shares

At the balance sheet date, the register of interests and short positions in the shares and underlying shares of the Company kept under Section 336 of the SFO showed that, other than the interests of Tan Sri Dato' Sri Dr. Teh Hong Piow as disclosed above, the following shareholders had an interest of 5% or more in the issued share capital of the Company:

Name	Capacity	Number of ordinary shares	Percentage of interest in issued share capital
Substantial shareholder			
1. Public Bank	Beneficial owner	804,017,920	73.5004
Other person			
2. JP Morgan Chase & Co	Custodian corporation/ approved lending agent	65,704,945	6.0065

All the interests stated above represent long positions. Save as disclosed above and under the heading "Directors' interests and short positions in shares and underlying shares", no person had registered an interest or short position in the shares or underlying shares of the Company that was required to be recorded under Section 336 of the SFO at the balance sheet date.

Connected transactions

(1) A tenancy arrangement was first made on 23 July 1997 and was renewed subsequently by tenancy agreements between Public Finance, a wholly-owned subsidiary, as the landlord and Public Bank, the ultimate holding company, as the tenant whereby Public Finance agreed to lease an apartment located in Taikoo Shing, Hong Kong to Public Bank as its staff quarters. The existing tenancy agreement was entered into on 29 August 2006 for a term of two years commencing from 1 August 2006 to 31 July 2008 at a monthly rental of HK\$20,600.

A lease arrangement was first made on 1 September 1993 and was renewed subsequently by tenancy agreements between Public Finance as the landlord and Public Bank as the tenant whereby Public Finance agreed to lease a portion of the office premises located at 11th Floor, Wing On House, 71 Des Voeux Road Central, Hong Kong to Public Bank as its office. The existing tenancy agreement was entered into on 31 July 2006 for a term of two years commencing from 1 August 2006 to 31 July 2008 at a monthly rental of HK\$43,800.

A tenancy agreement was first made on 11 November 2003 and was renewed subsequently by tenancy agreement between the Company as the landlord and Public Bank as the tenant whereby the Company agreed to lease the premises located at Shop A, Ground Floor, Wing On House, 71 Des Voeux Road Central, Hong Kong to Public Bank as its branch office. The existing tenancy agreement was entered into on 15 November 2006 for a term of three years commencing from 1 November 2006 to 31 October 2009 at a monthly rental of HK\$250,000.

Report of the Directors

Connected transactions (Continued)

- (2) Pursuant to the master dealer agreement entered into between Winton Motors, a wholly-owned subsidiary, and Public Bank on 29 December 1994, WML may from time to time refer hirers to Public Bank for obtaining taxi financing loans, and in return, Winton Motors will receive dealer's commission from Public Bank (the "Transaction"). Dealer's commission received/receivable by Winton Motors for the year from Public Bank was HK\$133,000 (2005: HK\$196,000).

The Transaction is only subject to the reporting requirements set out in Rules 14A.45 and 14A.46 of the Listing Rules. Tan Sri Dato' Thong Yaw Hong, Dato' Yeoh Chin Kee and Mr. Lee Chin Guan, the Independent Non-executive Directors of the Company, have reviewed the Transaction. They have confirmed that the Transaction was entered into (i) in the ordinary and usual course of business of the Company; (ii) on normal commercial terms; and (iii) in accordance with the relevant master dealer agreement on terms that were fair and reasonable and in the interests of the shareholders of the Company as a whole. The auditors have also confirmed that (i) the Transaction received the approval of the Company's board of directors; (ii) the terms were in accordance with the pricing policy of Winton Motors; (iii) the Transaction was entered into in accordance with the relevant master dealer agreement; and (iv) the dealer's commission received/receivable by Winton Motors did not exceed the percentage ratios as allowed under Rule 14A.34 of the Listing Rules.

Some of the related party transactions disclosed in note 43 to the financial statements also fell under the definition of "connected transaction" or "continuing connected transaction" in Chapter 14A of the Listing Rules. The Company has complied with the disclosure requirements, where applicable, in accordance with Chapter 14A of the Listing Rules.

Donations

During the year, the Group made charitable donations totalling HK\$1,000 (2005: HK\$15,000).

Compliance with Supervisory Policy Manual

The Group has followed the guidelines on "Financial Disclosure by Locally Incorporated Authorised Institutions" and "Corporate Governance of Locally Incorporated Authorised Institutions" under the Supervisory Policy Manuals issued by the HKMA.

Corporate governance

The Group is committed to maintaining a high level of corporate governance practices. A detailed Corporate Governance Report is set out on pages 15 to 24 in the annual report.

Report of the Directors

Sufficiency of public float

Based on information that is publicly available to the Company and within the knowledge of its directors, the directors confirmed that the Company has maintained the amount of public float as required under the Listing Rules as at the latest practicable date prior to the issue of the annual report.

Auditors

Ernst & Young retire and a resolution for their reappointment as auditors of the Company will be proposed at the forthcoming annual general meeting.

ON BEHALF OF THE BOARD

Tan Yoke Kong

Director

Hong Kong

10 January 2007

Independent Auditors' Report



To the shareholders of

Public Financial Holdings Limited

(Incorporated in Bermuda with limited liability)

We have audited the financial statements of Public Financial Holdings Limited set out on pages 42 to 109, which comprise the consolidated and company balance sheets as at 31 December 2006, and the consolidated income statement, the consolidated summary statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' responsibility for the financial statements

The directors of the Company are responsible for the preparation and the true and fair presentation of these financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the disclosure requirements of the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. Our report is made solely to you, as a body, in accordance with Section 90 of the Bermuda Companies Act 1981, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and true and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Independent Auditors' Report

Opinion

In our opinion, the financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2006 and of the Group's profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Ernst & Young

Certified Public Accountants

18/F, Two International Finance Centre

8 Finance Street

Hong Kong

10 January 2007

Consolidated Income Statement

For the year ended 31 December 2006

	Notes	2006 HK\$'000	2005 HK\$'000
Interest income		1,444,809	802,660
Interest expense		(534,372)	(36,613)
NET INTEREST INCOME		910,437	766,047
Other operating income	5	207,029	134,180
OPERATING INCOME		1,117,466	900,227
Operating expenses	6	(310,722)	(211,587)
OPERATING PROFIT BEFORE IMPAIRMENT LOSS AND ALLOWANCES		806,744	688,640
Impairment loss and allowances for loans and advances and receivables	7	(210,825)	(158,751)
OPERATING PROFIT		595,919	529,889
SHARE OF PROFITS AND LOSSES OF A JOINTLY-CONTROLLED ENTITY		176	–
PROFIT BEFORE TAX		596,095	529,889
Tax	10	(99,458)	(83,592)
PROFIT FOR THE YEAR	11	496,637	446,297
Attributable to:			
Equity holders of the holding company		496,637	446,297
DIVIDENDS	12		
Interim		273,474	335,461
Special		–	211,487
		273,474	546,948
EARNINGS PER SHARE (HK\$)	13		
Basic		0.500	0.623
Diluted		0.500	0.622

Balance Sheets

31 December 2006

	Notes	Group		Company	
		2006 HK\$'000	2005 HK\$'000	2006 HK\$'000	2005 HK\$'000
ASSETS					
Cash and short term placements	14	2,295,219	453,009	919,734	369,968
Placements with banks and financial institutions maturing between one and twelve months	15	566,773	5,000	-	445,845
Securities measured at fair value through profit or loss	16	10,213	-	-	-
Loans and advances and receivables	7	13,694,636	3,512,255	-	-
Available-for-sale security investments	17	75,632	25,881	-	-
Held-to-maturity securities	18	3,679,604	-	-	-
Inventories of taxi licences		24,105	26,988	-	-
Investment properties	19	196,666	147,987	53,000	45,000
Property, plant and equipment	20	71,003	21,336	-	-
Land lease prepayments	21	562,030	233,568	-	-
Interests in subsidiaries	22	-	-	5,612,733	1,057,572
Interest in a jointly-controlled entity	23	1,676	-	-	-
Deferred tax assets	32	17,849	2,854	-	-
Other assets	24	273,863	34,418	8,837	4,645
Goodwill	25	2,774,403	-	-	-
Intangible assets	26	725	126	-	-
TOTAL ASSETS		24,244,397	4,463,422	6,594,304	1,923,030
EQUITY AND LIABILITIES					
LIABILITIES					
Deposits and balances of banks and other financial institutions	28	516,097	-	-	-
Customer deposits	29	14,853,655	1,641,978	-	-
Certificates of deposits issued	30	769,674	-	-	-
Declared dividend	12	218,779	291,706	218,779	291,706
Bank loans	31	2,000,000	-	2,000,000	-
Current tax payable		32,810	31,555	-	-
Deferred tax liabilities	32	64,332	13,410	3,700	2,200
Other liabilities	33	469,002	91,339	2,100	1,313
TOTAL LIABILITIES		18,924,349	2,069,988	2,224,579	295,219
EQUITY					
Issued capital	35	109,390	72,926	109,390	72,926
Reserves	38	5,210,658	2,320,508	4,260,335	1,554,885
TOTAL EQUITY		5,320,048	2,393,434	4,369,725	1,627,811
TOTAL EQUITY AND LIABILITIES		24,244,397	4,463,422	6,594,304	1,923,030

Tan Yoke Kong
Director

Lee Huat Oon
Director

Consolidated Summary Statement of Changes in Equity

For the year ended 31 December 2006

	2006 HK\$'000	2005 HK\$'000
TOTAL EQUITY		
Balance at beginning of year	2,393,434	2,282,447
Rights issue, net of expenses	2,660,504	–
Shares issued on exercise of share options, net of expenses	–	156,736
Employee share-based compensation reserve	–	45,765
Surplus on revaluation of available-for-sale security investments and total income and expense recognised directly in equity	42,947	9,137
Profit for the year	496,637	446,297
Dividends paid/declared on shares	(273,474)	(546,948)
	223,163	(100,651)
Balance at end of year	5,320,048	2,393,434

Consolidated Cash Flow Statement

For the year ended 31 December 2006

	Notes	2006 HK\$'000	2005 HK\$'000
NET CASH (OUTFLOW)/INFLOW FROM OPERATING ACTIVITIES	39	(157,638)	44,710
CASH FLOWS FROM INVESTING ACTIVITIES			
Acquisition of a subsidiary	44	(1,551,980)	–
Purchases of property, plant and equipment		(6,044)	(1,793)
Proceeds from sale of property, plant and equipment and an investment property		4,920	5
Dividends from listed investments		1,306	773
Dividends from unlisted investments		780	–
Net cash outflow from investing activities		(1,551,018)	(1,015)
CASH FLOWS FROM FINANCING ACTIVITIES			
Rights issue, net of expenses		2,660,504	–
New bank loans		4,500,000	–
Repayment of bank loans		(2,500,000)	–
Shares issued on exercise of share options, net of expenses		–	156,736
Dividends paid on shares		(346,401)	(538,346)
Net cash inflow/(outflow) from financing activities		4,314,103	(381,610)
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS		2,605,447	(337,915)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR		458,009	795,924
CASH AND CASH EQUIVALENTS AT END OF YEAR		3,063,456	458,009
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS			
Cash and short term placements		289,424	453,009
Money at call and short notice with original maturity within three months		2,003,455	–
Placements with banks and financial institutions with original maturity within three months		331,521	5,000
Held-to-maturity securities with original maturity within three months		439,056	–
		3,063,456	458,009

Notes to Financial Statements

1. CORPORATE INFORMATION

The registered office of the Company is located at Clarendon House, Church Street, Hamilton HM 11, Bermuda.

During the year, the Group's principal activities were deposit taking, personal and commercial lending, mortgage financing, stockbroking, the letting of investment properties, the provision of finance to purchasers of taxis and public light buses, the trading of taxi cabs and taxi licences, and the leasing of taxis. After the completion of the acquisition of the entire issued and paid-up share capital of Public Bank (Hong Kong), the Group's principal activities also included the provision of a comprehensive range of banking, financial and related services.

In the opinion of the directors, the ultimate holding company is Public Bank, which is incorporated in Malaysia.

2.1 BASIS OF PREPARATION

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") (which also include Hong Kong Accounting Standards ("HKASs") and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA"), accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for investment properties, securities measured at fair value through profit or loss, derivative financial instruments and available-for-sale security investments, which have been measured at fair value. These financial statements are presented in Hong Kong dollars and all values are rounded to the nearest thousand except when otherwise indicated.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries for the year ended 31 December 2006. The results of subsidiaries are consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases. All significant intercompany transactions and balances within the Group are eliminated on consolidation.

The acquisition of subsidiaries during the year has been accounted for using the purchase method of accounting. This method involves allocating the cost of the business combinations to the fair value of the identifiable assets acquired, and liabilities and contingent liabilities assumed at the date of acquisition. The cost of the acquisition is measured at the aggregate of the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition.

Notes to Financial Statements

2.2 IMPACT OF NEW AND REVISED HKFRSs

The Group has adopted the following new and revised HKFRSs for the first time for the current year's financial statements. The adoption of these new and revised standards and interpretation has had no material effect on these financial statements.

- | | |
|--------------------------------|--|
| • HKAS 21 Amendment | Net Investment in a Foreign Operation |
| • HKAS 39 & HKFRS 4 Amendments | Financial Guarantee Contracts |
| • HKAS 39 Amendment | The Fair Value Option |
| • HKAS 39 Amendment | Cash Flow Hedge Accounting of Forecast Intragroup Transactions |
| • HK(IFRIC) – Int 4 | Determining whether an Arrangement contains a Lease |

The principal changes in accounting policies are as follows:

(a) HKAS 21 “The Effects of Changes in Foreign Exchange Rates”

Upon the adoption of the HKAS 21 Amendment regarding a net investment in a foreign operation, all exchange differences arising from a monetary item that forms part of the Group's net investment in a foreign operation are recognised in a separate component of equity in the consolidated financial statements irrespective of the currency in which the monetary item is denominated. This change has had no material impact on these financial statements as at 31 December 2006 or 31 December 2005.

(b) HKAS 39 “Financial Instruments: Recognition and Measurement”

(i) Amendment for financial guarantee contracts

This amendment has revised the scope of HKAS 39 to require financial guarantee contracts issued that are not considered as insurance contracts, to be recognised initially at fair value and to be remeasured at the higher of the amount determined in accordance with HKAS 37 “Provisions, Contingent Liabilities and Contingent Assets” and the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with HKAS 18 “Revenue”. The adoption of this amendment has had no material impact on these financial statements.

(ii) Amendment for the fair value option

This amendment has changed the definition of a financial instrument classified as fair value through profit or loss and has restricted the use of the option to designate any financial asset to be measured at fair value through the income statement. The Group had not previously used this option, and hence the amendment has had no effect on the financial statements.

(iii) Amendment for cash flow hedge accounting of forecast intragroup transactions

This amendment has revised HKAS 39 to permit the foreign currency risk of a highly probable intragroup forecast transaction to qualify as a hedged item in a cash flow hedge, provided that the transaction is denominated in a currency other than the functional currency of the entity entering into that transaction and that the foreign currency risk will affect the consolidated income statement. As the Group currently has no such transaction, the amendment has had no effect on these financial statements.

Notes to Financial Statements

2.2 IMPACT OF NEW AND REVISED HKFRSs (Continued)

(c) HK(IFRIC) – Int 4 “Determining whether an Arrangement contains a Lease”

The Group has adopted this interpretation as of 1 January 2006, which provides guidance in determining whether arrangements contain a lease to which lease accounting must be applied. This interpretation has had no material impact on these financial statements.

2.3 IMPACT OF ISSUED BUT NOT YET EFFECTIVE HKFRSs

The Group has not applied the following new and revised HKFRSs, which have been issued but are not yet effective, in these financial statements:

- | | |
|---------------------|--------------------------------------|
| • HKAS 1 Amendment | Capital Disclosures |
| • HKFRS 7 | Financial Instruments: Disclosures |
| • HK(IFRIC) – Int 8 | Scope of HKFRS 2 |
| • HK(IFRIC) – Int 9 | Reassessment of Embedded Derivatives |

HKAS 1 Amendment shall be applied for annual periods beginning on or after 1 January 2007. This revised standard will affect the disclosures of qualitative information about the Group’s objective, policies and processes for managing capital; quantitative data about what the Company regards as capital; and compliance with any capital requirements and the consequences of any non-compliance.

HKFRS 7 shall be applied for annual periods beginning on or after 1 January 2007. This standard requires disclosures that enable users of the financial statements to evaluate the significance of the Group’s financial instruments and the nature and extent of risks arising from those financial instruments and also incorporates many of the disclosure requirements of HKAS 32.

HK(IFRIC) – Int 8 and HK(IFRIC) – Int 9 shall be applied for annual periods beginning on or after 1 May 2006 and 1 June 2006, respectively.

The Group is in the process of making an assessment of the impact of these new and revised HKFRSs upon initial application. In the opinion of the directors, while the adoption of HKAS 1 Amendment and HKFRS 7 will result in new or amended disclosures, these new and revised HKFRSs should not have any significant impact on the Group’s results of operations and financial position.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Goodwill

Goodwill arising on the acquisition of subsidiaries represents the excess of the cost of the business combination over the Group’s interest in the net fair value of the acquirees’ identifiable assets acquired, and liabilities and contingent liabilities as at the date of acquisition.

Goodwill arising on acquisition is recognised in the consolidated balance sheet as an asset, initially measured at cost and subsequently at cost less any accumulated impairment losses.

The carrying amount of goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that carrying value may be impaired.

Notes to Financial Statements

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Goodwill (Continued)

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the combination's synergies, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units.

Impairment is determined by assessing the recoverable amount of the cash-generating unit, to which the goodwill relates. Where the recoverable amount of the cash-generating unit is less than the carrying amount, an impairment loss is recognised.

Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained. An impairment loss recognised for goodwill is not reversed in a subsequent period.

Goodwill arising on acquisitions before 1 January 2001 was eliminated against the consolidated capital reserve in the year of acquisition. The Group applied the transitional provisions of HKFRS 3 that permitted such goodwill to remain eliminated against the consolidated capital reserve and that required such goodwill not to be recognised in the consolidated income statement when the Group disposes of all or part of the business to which that goodwill relates or when a cash-generating unit to which the goodwill relates become impaired.

Excess over the cost of business combination

On acquisition of subsidiaries, jointly-controlled entities and associates, if the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of an entity being acquired recognised as at the date of acquisition exceeds the cost of the business combination, the Group shall reassess the identification and measurement of the identifiable assets, liabilities and contingent liabilities of that entity and the measurement of the cost of the business combination; and recognise immediately in the consolidated income statement any excess remaining after that reassessment.

Subsidiaries

A subsidiary is a company whose financial and operating policies the Company controls, directly or indirectly, so as to obtain benefits from its activities.

The results of subsidiaries are included in the Company's income statement to the extent of dividends received and receivable. The Company's interests in subsidiaries are stated at cost less any impairment losses.

Notes to Financial Statements

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Joint venture companies

A joint venture is an entity set up by contractual arrangement, whereby the Group and other parties undertake an economic activity. The joint venture operates as a separate entity in which the Group and the other parties have an interest.

The joint venture agreement between the venturers stipulates the capital contributions of the joint venture parties, the duration of the joint venture entities and the basis on which the assets are to be realised upon its dissolution. The profits and losses from the joint venture's operations and any distributions of surplus assets are shared by the venturers, either in proportion to their respective capital contributions, or in accordance with the terms of the joint venture agreement.

A joint venture is treated as:

- (a) a subsidiary, if the Group has unilateral control, directly or indirectly, over the joint venture;
- (b) a jointly-controlled entity, if the Group does not have unilateral control, but has joint control, directly or indirectly, over the joint venture;
- (c) an associate, if the Group does not have unilateral or joint control, but holds, directly or indirectly, generally not less than 20% of the joint venture's registered capital and is in a position to exercise significant influence over the joint venture; or
- (d) an equity investment accounted for in accordance with HKAS 39, if the Group holds, directly or indirectly, less than 20% of the joint venture's registered capital and has neither joint control of, nor is in a position to exercise significant influence over, the joint venture.

Jointly-controlled entities

A jointly-controlled entity is a joint venture that is subject to joint control, resulting in none of the participating parties having unilateral control over the economic activity of the jointly-controlled entity.

The Group's share of the post-acquisition results and reserves of jointly-controlled entities is included in the consolidated income statement and consolidated reserves, respectively. The Group's interests in jointly-controlled entities are stated in the consolidated balance sheet at the Group's share of net assets under the equity method of accounting, less any impairment losses. Adjustments are made to bring into line any dissimilar accounting policies that may exist.

The results of jointly-controlled entities are included in the Group's income statement to the extent of dividends received and receivable. The Group's interests in jointly-controlled entities are treated as non-current assets and are stated at cost less any impairment losses.

Notes to Financial Statements

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Impairment of non-financial assets other than goodwill

Where an indication of impairment exists, or when annual impairment testing for an asset is required (other than deferred tax assets, financial assets, goodwill and inventories of taxi licences), the asset's recoverable amount is estimated. An asset's recoverable amount is calculated as the higher of the asset's or cash-generating unit's value in use and its fair value less costs to sell, and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is recognised only if the carrying amount of an asset exceeds the present value of its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. An impairment loss is charged to the income statement in the period in which it arises in those expense categories consistent with the function of the impaired asset, unless the asset is carried at a revalued amount, in which case the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognised impairment loss of an asset other than goodwill and certain financial assets is reversed only if there has been a change in the estimates used to determine the recoverable amount of that asset, however not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation), had no impairment loss been recognised for the asset in prior years. A reversal of such impairment loss is credited to the income statement in the period in which it arises, unless the asset is carried at a revalued amount, in which case the reversal of the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

Related parties

A party is considered to be related to the Group if:

- (a) the party, directly or indirectly through one or more intermediaries, (i) controls, is controlled by, or is under common control with, the Group; (ii) has an interest in the Group that gives it significant influence over the Group; or (iii) has joint control over the Group;
- (b) the party is an associate;
- (c) the party is a jointly-controlled entity;
- (d) the party is a member of the key management personnel of the Group or its ultimate holding company;
- (e) the party is a close member of the family of any individual referred to in (a) or (d);
- (f) the party is an entity that is controlled, jointly-controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e); or
- (g) the party is a post-employment benefit plan for the benefit of the employees of the Group, or of any entity that is a related party of the Group.

Notes to Financial Statements

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Property, plant and equipment and depreciation

The building component of owner-occupied leasehold properties and other property, plant and equipment, other than investment properties, is stated at cost, except for certain leasehold buildings transferred from investment properties, which are stated at deemed cost at the date of transfer, less accumulated depreciation and impairment. The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after items of property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to the income statement in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of an item of property, plant and equipment, and where the cost of the item can be measured reliably, the expenditure is capitalised as an additional cost of that asset or as a replacement.

Depreciation is calculated on the straight-line basis to write off the cost of each item of property, plant and equipment to its residual value over its estimated useful life. The principal annual rates used for this purpose are as follows:

Leasehold buildings	2%-4%
Leasehold improvements:	
Own leasehold buildings	20%-33 $\frac{1}{3}$ %
Others	Over the shorter of the remaining lease terms or seven years
Furniture, fixtures and equipment	10%-33 $\frac{1}{3}$ %
Motor vehicles	20%-25%

Where parts of an item of property, plant and equipment have different useful lives, the cost or valuation of that item is allocated on a reasonable basis among the parts and each part is depreciated separately.

Residual values, useful lives and the depreciation method are reviewed, and adjusted if appropriate, at each balance sheet date.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss on disposal or retirement recognised in the income statement in the year the asset is derecognised is the difference between the net sale proceeds and the carrying amount of the relevant asset.

Investment properties

Investment properties are interests in land and buildings held to earn rental income and/or for capital appreciation, rather than for use in the production or supply of goods or services or for administrative purposes; or for sale in the ordinary course of business. Such properties are measured initially at cost, including transaction costs. Subsequent to initial recognition, investment properties are stated at fair value, which reflects market conditions at the balance sheet date. Gains or losses arising from changes in the fair values of investment properties are included in the income statement in the year in which they arise. Any gains or losses on the retirement or disposal of an investment property are recognised in the income statement in the year of the retirement or disposal.

Notes to Financial Statements

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Investment properties (Continued)

For a transfer from investment properties to owner-occupied properties, the deemed cost of property for subsequent accounting is its fair value at the date of change in use. If the property occupied by the Group as an owner-occupied property becomes an investment property, the Group accounts for such property in accordance with the policy stated under "Property, plant and equipment and depreciation" up to the date of change in use, and any difference at that date between the carrying amount and the fair value of the property is accounted for.

Intangible assets

Intangible assets (other than goodwill), representing eligibility rights to trade on or through the Stock Exchange are stated at net book value as at 1 January 2005. The Group ceased amortisation of its remaining intangible asset from 1 January 2005. The carrying amount of intangible assets is subject to an impairment test, and impairment, if any, is charged to the income statement.

Leases

Leases that transfer substantially all the rewards and risks of ownership of assets to the Group, other than legal title, are accounted for as finance leases. At the inception of a finance lease, the cost of the leased asset is capitalised at the present value of the minimum lease payments and recorded together with the obligation, excluding the interest element, to reflect the purchase and financing. Assets held under capitalised finance leases are included in property, plant and equipment, and depreciated over the shorter of the lease terms and the estimated useful lives of the assets. The finance costs of such leases are charged to the income statement so as to provide a constant periodic rate of charge over the lease terms.

The amounts due from the lessees under finance leases are recorded in the balance sheet as advances to customers. The amount comprises the gross investment in the finance leases less gross earnings allocated to future accounting periods.

The total gross earnings under finance leases are allocated to the accounting periods over the duration of the underlying agreements so as to produce an approximately constant periodic rate of return on the net cash investment for each accounting period.

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Where the Group is the lessor, assets leased by the Group under operating leases are included in investment properties and rentals receivable under the operating leases are credited to the income statement on the straight-line basis over the lease terms. Where the Group is the lessee, rentals payable under the operating leases are charged to the income statement on the straight-line basis over the lease terms.

Land lease prepayments are stated at cost less accumulated amortisation and any impairment, and are amortised over the remaining lease terms on the straight-line basis to the income statement.

Notes to Financial Statements

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Inventories

Inventories are stated at the lower of cost and fair value. Cost is determined as the actual cost for taxi cabs and taxi licences. Fair value is based on estimated selling prices less any estimated costs to be incurred on disposal.

Investments and other financial assets

Financial assets in the scope of HKAS 39 are classified as either securities measured at fair value through profit or loss, loans and advances and receivables, available-for-sale securities, and held-to-maturity securities, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not measured at fair value through profit or loss, directly attributable transaction costs. The Group considers whether a contract contains an embedded derivative when the Group first becomes a party to it. The embedded derivatives are separated from the host contract which is not measured at fair value through profit or loss when the analysis shows that the economic characteristics and risks of embedded derivatives are not closely related to those of the host contract.

The Group determines the classification of its financial assets after initial recognition and, where allowed and appropriate, re-evaluates this designation at the balance sheet date.

All regular way purchases and sales of financial assets are recognised on the trade date, that is, the date that the Group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

Securities measured at fair value through profit or loss

Financial assets held for trading are included in the category "Securities measured at fair value through profit or loss". Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. Derivatives are also classified as held for trading unless they are designated as effective hedging instruments. Gains or losses on investments held for trading are recognised in the income statement.

Held-to-maturity securities

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity securities when the Group has the positive intention and ability to hold to maturity. Investments intended to be held for an undefined period are not included in this classification. Held to maturity investments are subsequently measured at amortised cost. Amortised cost is computed as the amount initially recognised minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initially recognised amount and the maturity amount. This calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums and discounts. For investments carried at amortised cost, gains and losses are recognised in the income statement when the investments are derecognised or impaired, as well as through the amortisation process.

Notes to Financial Statements

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Investments and other financial assets (Continued)

Loans and advances and receivables

Loans and advances and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are subsequently carried at amortised cost using the effective interest method. Amortised cost is calculated taking into account any discount or premium on acquisition and includes fees that are an integral part of the effective interest rate and transaction costs. Gains and losses are recognised in the income statement when the loans and advances and receivables are derecognised or impaired, as well as through the amortisation process.

Available-for-sale securities

Available-for-sale securities are those non-derivative financial assets in listed and unlisted securities that are designated as available-for-sale or are not classified in any of the other three categories. After initial recognition, available-for-sale securities are measured at fair value with gains or losses being recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in equity is included in the income statement.

When the fair value of unlisted equity securities cannot be reliably measured because (a) the variability in the range of reasonable fair value estimates is significant for that investment or (b) the probabilities of the various estimates within the range cannot be reasonably assessed and used in estimating fair value, such securities are stated at cost less any impairment losses.

Fair value

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument, which is substantially the same; a discounted cash flow analysis and option pricing models.

Impairment of financial assets

The Group assesses at each balance sheet date whether there is any objective evidence that a financial asset or group of financial assets is impaired.

Assets carried at amortised cost

If there is objective evidence that an impairment loss on loans and advances and receivables or held-to-maturity securities carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced either directly or through the use of an allowance account. The amount of the impairment loss is recognised in the income statement.

Notes to Financial Statements

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Impairment of financial assets (Continued)

Assets carried at amortised cost (Continued)

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group is also collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed. Any subsequent reversal of an impairment loss is recognised in the income statement, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date.

Assets carried at cost

If there is objective evidence that an impairment loss on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, or on a derivative asset that is linked to and must be settled by delivery of such an unquoted equity instrument has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Impairment losses on these assets are not reversed.

Available-for-sale securities

If an available-for-sale security is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in the income statement, is transferred from equity to the income statement. Impairment losses on equity instruments classified as available-for-sale are not reversed through the income statement.

Impairment losses on debt instruments are reversed through profit or loss, if the increase in fair value of the instrument can be objectively related to an event, occurring after the impairment loss was recognised in the income statement.

Derecognition of financial assets

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- the rights to receive cash flows from the asset have expired;
- the Group retains the rights to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; or
- the Group has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Notes to Financial Statements

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Derecognition of financial assets (Continued)

Where the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Group's continuing involvement is the amount of the transferred asset that the Group may repurchase, except that in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, where the extent of the Group's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

Reposessed assets

Collateral assets for loans and advances and receivables are reposessed by the Group when the borrowers are unable to service their repayments, and would be realised in satisfaction of outstanding debts. Advances with reposessed collateral assets will continue to be accounted for as customer advances, except for those where the Group has taken the legal title of the reposessed collateral assets, in which cases, the reposessed assets are shown under other accounts at the predetermined value with a corresponding reduction in the related advances. Individual impairment allowance is made on the shortfall between the expected net realisable value of reposessed assets and the outstanding advances.

Reposessed assets are recognised at the lower of their carrying amount of the related loans and advances and receivables and fair value less costs to sell.

Interest-bearing loans and borrowings

All loans and borrowings are initially recognised at the fair value of the consideration received less directly attributable transaction costs.

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method.

Gains and losses are recognised in net profit or loss when the liabilities are derecognised as well as through the amortisation process.

Derecognition of financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and a recognition of a new liability, and the difference between the respective carrying amounts is recognised in the income statement.

Notes to Financial Statements

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Derivative financial instruments

The Group uses derivative financial instruments such as forward currency contracts and interest rate swaps to hedge its risks associated with interest rate and foreign currency fluctuations. Such derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

Any gains or losses arising from changes in fair value on derivatives that do not qualify for hedge accounting are taken directly to the income statement for the year.

The fair value of forward currency contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles. The fair value of interest rate swap contracts is determined by reference to market values for similar instruments.

Cash and cash equivalents

For the purpose of the consolidated cash flow statement, cash and cash equivalents consist of cash at banks and on hand, net of outstanding bank overdrafts, and short term highly liquid investments which are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months of maturity when acquired.

For the purpose of the balance sheets, cash and cash equivalents comprise cash on hand and at banks, including term deposits, and assets similar in nature to cash, which are not restricted as to use.

Provisions

A provision is recognised when a present obligation (legal or constructive) has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

When the effect of discounting is material, the amount recognised for a provision is the present value at the balance sheet date of the future expenditures expected to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in finance costs in the income statement.

Income tax

Income tax comprises current and deferred tax. Income tax is recognised in the income statement or in equity if it relates to items that are recognised in the same or a different period, directly in equity.

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities.

Deferred tax is provided, using the liability method, on all material temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Notes to Financial Statements

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income tax (Continued)

Deferred tax liabilities are recognised for all material taxable temporary differences, except:

- where the deferred tax liability arises from goodwill or the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all material deductible temporary differences, carryforward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward of unused tax credits and unused tax losses can be utilised except:

- where the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries and interests in joint ventures, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Conversely, previously unrecognised deferred tax assets are reassessed at each balance sheet date and are recognised to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted at the balance sheet date.

Deferred tax assets and deferred tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

Notes to Financial Statements

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Foreign currencies

These financial statements are presented in Hong Kong dollars, which is the Group's functional and presentation currency. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Foreign currency transactions are initially recorded using the functional currency rates ruling at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rates of exchange ruling at the balance sheet date. All differences are taken to the income statement. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

Employee benefits

(a) Retirement benefit schemes

The Group operates two defined contribution retirement benefit schemes for those employees who are eligible to participate. The assets of the schemes are held separately from those of the Group in independently administered funds. Contributions are made based on a percentage of the participating employees' relevant monthly income from the Group, and are charged to the income statement as they become payable in accordance with the rules of the respective schemes. When an employee leaves the Occupational Retirement Scheme Ordinance Scheme prior to his/her interest in the Group's employer non-mandatory contributions vesting with the employee, the ongoing contributions payable by the Group may be reduced by the relevant amount of forfeited contributions. When an employee leaves the Mandatory Provident Fund, the Group's mandatory contributions vest fully with the employee.

(b) Share option scheme

The Company operates a share option scheme (the "Scheme") for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. Employees (including directors) of the Group receive remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity-settled transactions.

For share options granted under the Scheme, the fair value of the employee's services rendered in exchange for the grant of the options is recognised as an expense and credited to an employee share-based compensation reserve under equity. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted at the grant date. At each balance sheet date, the Group revises its estimates of the number of options that are expected to become exercisable. It recognises the impact of the revision of the original estimates, if any, in the income statement, and a corresponding adjustment to the employee share-based compensation reserve over the remaining vesting period.

Where the terms of an equity-settled award are modified, as a minimum an expense is recognised as if the terms had not been modified. In addition, an expense is recognised for any modification, which increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee as measured at the date of modification.

Notes to Financial Statements

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Employee benefits (Continued)

(b) Share option scheme (Continued)

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. However, if a new award is substituted for the cancelled award, and is designated as a replacement award on the date that is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph.

The dilutive effect of outstanding options is reflected as additional share dilution in the computation of earnings per share.

(c) Employment Ordinance long service payments

Certain of the Group's employees have completed the required number of years of service to the Group in order to be eligible for long service payments under the Hong Kong Employment Ordinance (the "Employment Ordinance") in the event of the termination of their employment. The Group is liable to make such payments in the event that such a termination of employment meets the circumstances specified in the Employment Ordinance.

A provision is recognised in respect of probable future long service payments based on the best estimate of the probable future outflow of resources which has been earned by the employees from their service to the Group to the balance sheet date, if applicable.

(d) Employee leave entitlements

The cost of accumulating compensated absences is recognised as an expense and measured based on the additional amount that the Group expects to pay as a result of the unused entitlement that has accumulated at the balance sheet date.

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

- (a) interest income, on an accrual basis using the effective interest method by applying the rate that discounts the estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial assets;
- (b) commission, brokerage, handling fees and fee income, when services are rendered;
- (c) from the sale of goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold;
- (d) interest income on finance leases is recognised on the basis as set out above under the heading of "Leases";
- (e) rental income, on the straight-line basis over the lease terms; and
- (f) dividend income, when the shareholders' right to receive payment has been established.

Notes to Financial Statements

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Dividends

Final dividends proposed by the directors are classified as a separate allocation of retained profits within reserves in the balance sheet, until they have been approved by the shareholders in a general meeting. When these dividends are approved by the shareholders and declared, they are recognised as a liability.

Interim dividends are simultaneously proposed and declared because the Bye-laws grant the directors the authority to declare interim dividends. Consequently, interim dividends are recognised directly as a liability when they are proposed and declared.

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

Judgements

In the process of applying the Group's accounting policies, management has made the following judgements, apart from those involving estimations, which have the most significant effect on the amounts recognised in the financial statements:

Held-to-maturity securities

The Group follows the guidance of HKAS 39 on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. This classification requires significant judgement. In making this judgement, the Group evaluates its intention and ability to hold such investments to maturity. If the Group fails to keep these investments to maturity other than for the specific circumstances, it is required to reclassify the entire class of held-to-maturity securities to other appropriate classes of financial assets. The investments would then be measured at fair value and not at amortised cost.

Estimation uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

Impairment allowances on loans and advances and receivables

The Group reviews its loan portfolios to assess impairment on a regular basis. In determining whether an impairment loss should be recorded in the income statement, the Group makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the Group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Impairment of goodwill

The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the value in use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of goodwill at 31 December 2006 was HK\$2,774,403,000. Further details are set out in note 25 to the financial statements.

Notes to Financial Statements

4. SEGMENT INFORMATION

In accordance with the Group's internal financial reporting, the Group has determined that business segments are its primary reporting format and geographical segments are its secondary reporting format.

(a) By business segments

The Group's operating businesses are organised and managed separately, according to the nature of products and services provided, with each segment representing a strategic business unit that offers products and services which are subject to risks and returns that are different from those of the other business segments:

- the retail and commercial banking and lending segment mainly comprises the provision of deposit account services, wealth management services, the extension of mortgages and consumer lending, hire purchase and leasing, provision of finance to purchasers of licensed public vehicles such as taxis and public light buses, provision of services and financing activities for customers in trading, manufacturing and various business sectors, foreign exchange activities, centralised cash management for deposit taking and lending, interest rate risk management, management of investments in securities and the overall funding management of the Group;
- other business segment comprises securities trading and stockbroking, taxi trading and the leasing of taxis and letting of investment properties.

The Group's inter-segment transactions during the year were mainly related to dealers' commission from referrals of taxi financing loans, and these transactions were entered into on similar terms and conditions as those contracted with third parties at the dates of the transactions.

Notes to Financial Statements

4. SEGMENT INFORMATION

(a) By business segments (Continued)

The following tables represent revenue and profit information for these segments for the years ended 31 December 2006 and 2005, and certain asset and liability information regarding business segments as at 31 December 2006 and 2005.

Group	Retail and commercial banking and lending	Retail and commercial lending	Other businesses		Eliminated on consolidation		Total	
	2006 HK\$'000	2005 HK\$'000	2006 HK\$'000	2005 HK\$'000	2006 HK\$'000	2005 HK\$'000	2006 HK\$'000	2005 HK\$'000
Segment revenue								
Net interest income	910,399	766,136	38	(89)	-	-	910,437	766,047
Other operating income:								
Fees and commission income	158,900	118,674	17,449	3,056	-	-	176,349	121,730
Others	14,357	-	16,323	12,450	-	-	30,680	12,450
Elimination of inter-segment transactions	-	-	373	737	(373)	(737)	-	-
	1,083,656	884,810	34,183	16,154	(373)	(737)	1,117,466	900,227
Segment results	574,190	491,834	21,729	38,055	-	-	595,919	529,889
Share of profits and losses of a jointly-controlled entity							176	-
Profit before tax							596,095	529,889
Tax							(99,458)	(83,592)
Profit for the year							496,637	446,297
Segment assets	20,934,798	4,201,485	516,622	258,957	-	-	21,451,420	4,460,442
Unallocated assets:								
Goodwill							2,774,403	-
Intangible assets							725	126
Deferred tax assets							17,849	2,854
Total assets							24,244,397	4,463,422
Segment liabilities	18,471,397	1,662,637	137,031	70,680	-	-	18,608,428	1,733,317
Unallocated liabilities:								
Declared dividend							218,779	291,706
Deferred tax liabilities and tax payable							97,142	44,965
Total liabilities							18,924,349	2,069,988
Other segment information								
Capital expenditure	6,044	1,793	-	-	-	-	6,044	1,793
Amortisation and write-off of commission expenses	288	133	-	-	-	-	288	133
Depreciation and amortisation of land lease prepayments	13,179	5,100	-	-	-	-	13,179	5,100
Reversal of an impairment loss on land lease prepayments	(4,694)	(3,514)	-	-	-	-	(4,694)	(3,514)
Changes in fair value of investment properties	-	-	(30,719)	(30,160)	-	-	(30,719)	(30,160)
Impairment loss and allowances for loans and advances and receivables	210,825	158,751	-	-	-	-	210,825	158,751
(Gain)/loss on disposal of property, plant and equipment	(204)	30	-	-	-	-	(204)	30

Notes to Financial Statements

4. SEGMENT INFORMATION (Continued)

(b) By geographical segments

Over 90% of the Group's operating income, results, assets, liabilities, off-balance sheet commitments and exposures are derived from operations carried out in Hong Kong. Accordingly, no geographical segment information is presented in the financial statements.

5. OTHER OPERATING INCOME

	Group	
	2006	2005
	HK\$'000	HK\$'000
Fees and commission income:		
Retail and commercial banking	162,405	118,092
Securities	15,006	3,638
	177,411	121,730
Less: Fees and commission expenses	(1,062)	–
Net fees and commission income	176,349	121,730
Gross rental income	11,739	7,198
Less: Direct operating expenses	(212)	(265)
Net rental income	11,527	6,933
Gains less losses arising from dealing in foreign currencies	10,646	–
Gain on disposal of securities measured at fair value through profit or loss	438	–
Gain on securities measured at fair value through profit or loss	933	–
Gain/(loss) on disposal of property, plant and equipment	204	(30)
Dividends from listed investments	1,306	773
Dividends from unlisted investments	780	–
Others	4,846	4,774
	207,029	134,180

The direct operating expenses included repair and maintenance expenses arising from investment properties.

Notes to Financial Statements

6. OPERATING EXPENSES

	Group	
	2006	2005
	HK\$'000	HK\$'000
Staff costs:		
Salaries and other staff costs	160,383	86,731
Pension contributions	9,086	6,393
Less: Forfeited contributions	(129)	(524)
Net pension contributions	8,957	5,869
	169,340	92,600
Employee share option benefits	–	45,765
	169,340	138,365
Other operating expenses:		
Operating lease rentals on leasehold buildings	24,981	20,221
Depreciation and amortisation of land lease prepayments	13,179	5,100
Auditors' remuneration	2,950	1,473
Amortisation and write-off of commission expenses	288	133
Administrative and general expenses	32,382	15,528
Others	103,015	64,441
Operating expenses before reversal of an impairment loss on land lease prepayments and changes in fair value of investment properties	346,135	245,261
Reversal of an impairment loss on land lease prepayments	(4,694)	(3,514)
Changes in fair value of investment properties	(30,719)	(30,160)
	(35,413)	(33,674)
	310,722	211,587

As at 31 December 2006, the Group had no material forfeited contributions available to reduce its contributions to the pension schemes in future years (2005: Nil). The current year credits arose in respect of staff who left the scheme during the year.

Notes to Financial Statements

7. LOANS AND ADVANCES AND RECEIVABLES

(a) Advances to customers and receivables

	Group	
	2006 HK\$'000	2005 HK\$'000
Loans and advances to customers	13,676,597	3,583,800
Trade bills	98,381	–
	13,774,978	3,583,800
Interest receivable	113,916	45,232
	13,888,894	3,629,032
Other receivables	68,473	73,902
	13,957,367	3,702,934
Impairment allowances for advances to customers and receivables:		
Individual impairment allowances	(104,785)	(78,276)
Collective impairment allowances	(157,946)	(112,403)
	(262,731)	(190,679)
	13,694,636	3,512,255

Certain loans and advances and receivables were secured by properties, taxi licences, taxi cabs, shares, cash and other collateral.

Included in loans and advances and receivables are receivables in respect of assets leased under finance leases as set out below:

	Group		Group	
	2006 Present value of minimum lease payments HK\$'000		2005 Present value of minimum lease payments HK\$'000	
Amounts receivable under finance leases:				
Within one year	408,197	293,704	75,506	46,921
In the second to fifth years, inclusive	826,497	482,119	198,016	109,490
Over five years	2,466,746	1,468,776	483,765	344,856
	3,701,440	2,244,599	757,287	501,267
Less: Unearned finance income	(1,456,841)		(256,020)	
Present value of minimum lease payments receivable	2,244,599		501,267	

The Group has entered into finance lease arrangements with customers in respect of motor vehicles and equipment. The terms of the finance leases entered into range from 1 to 25 years.

Notes to Financial Statements

7. LOANS AND ADVANCES AND RECEIVABLES (Continued)**(a) Advances to customers and receivables (Continued)**

The maturity profile of loans and advances to customers and receivables at the balance sheet date is analysed by the remaining periods to their contractual maturity dates as follows:

	Group	
	2006	2005
	HK\$'000	HK\$'000
Repayable:		
On demand	481,847	19,999
Within three months or less	2,141,654	546,405
Within one year or less but over three months	2,009,319	1,196,343
Within five years or less but over one year	4,228,162	1,217,724
After five years	4,772,898	490,573
Undated	323,487	231,890
	13,957,367	3,702,934

(b) Gross amount of overdue and impaired loans and advances

	Group			
	2006		2005	
	Gross amount HK\$'000	Percentage of total loans and advances	Gross amount HK\$'000	Percentage of total loans and advances
Gross overdue and impaired loans and advances				
Overdue for:				
Six months or less but over three months	80,142	0.6	62,450	1.7
One year or less but over six months	49,930	0.4	29,385	0.8
Over one year and loss accounts	166,901	1.2	116,786	3.3
	296,973	2.2	208,621	5.8
Rescheduled loans	907	-	-	-
Total overdue and impaired loans and advances	297,880	2.2	208,621	5.8
Impairment allowances for overdue and impaired loans and advances:				
Individual impairment allowances	(104,785)		(78,276)	
Collective impairment allowances	(128,608)		(105,834)	
	(233,393)		(184,110)	
	64,487	0.5	24,511	0.7

Notes to Financial Statements

7. LOANS AND ADVANCES AND RECEIVABLES (Continued)**(b) Gross amount of overdue and impaired loans and advances (Continued)**

Interest accrual of overdue and impaired loans and advances amounted to less than 1% of total gross loans and advances and is considered immaterial to the Group. Accordingly, the aforesaid interest accrual is not disclosed in the financial statements.

(c) Impairment allowances for loans and advances and receivables

	Group	
	2006 HK\$'000	2005 HK\$'000
Balance at beginning of year	190,679	193,750
Recoveries	67,538	59,648
Charge for the year	278,363	218,399
Amounts released	(67,538)	(59,648)
Net charge to the consolidated income statement	210,825	158,751
Amounts written off	(282,661)	(221,470)
Acquisition of subsidiaries	76,350	–
Balance at end of year	262,731	190,679

(d) Repossessed assets

Collateral assets for loans and advances are repossessed by the Group when the borrowers are unable to service their repayments, and would be realised for the settlement of the outstanding debts. Advances with repossessed collateral assets will continue to be accounted for as customer advances and impairment allowance is measured as the difference between the carrying value of the outstanding advance and the net present value of estimated future cash flows including the sales proceeds from the realisation of the repossessed asset.

The total value of the repossessed assets of the Group amounted to HK\$21,679,000 (2005: HK\$1,251,000).

Notes to Financial Statements

8. DIRECTORS' REMUNERATION

The remuneration of each director for the years ended 31 December 2006 and 2005 are set out below:

Group

Name of Director	2006				Total HK\$'000
	Fees HK\$'000	Salaries and other benefits HK\$'000	Bonuses HK\$'000	Pension scheme contributions HK\$'000	
	(Note 1)				
Tan Sri Dato' Sri Dr. Teh Hong Piow	265	-	-	-	265
Tan Sri Dato' Thong Yaw Hong (Note 2)	120	-	-	-	120
Tan Yoke Kong (Note 3)	75	1,242	412	136	1,865
Lee Huat Oon	50	912	305	101	1,368
Dato' Sri Tay Ah Lek	150	-	-	-	150
Dato' Chang Kat Kiam	125	-	-	-	125
Wong Kong Ming	50	-	-	-	50
Dato' Yeoh Chin Kee	150	-	-	-	150
Lee Chin Guan	150	-	-	-	150
Geh Cheng Hooi, Paul (Note 4)	50	-	-	-	50
	1,185	2,154	717	237	4,293

Notes to Financial Statements

8. DIRECTORS' REMUNERATION (Continued)

Group

Name of Director	2005				Total HK\$'000
	Fees HK\$'000	Salaries and other benefits HK\$'000	Bonuses HK\$'000	Pension scheme contributions HK\$'000	
		(Note 1)			
Tan Sri Dato' Sri Dr. Teh Hong Piow	205	486	–	–	691
Tan Yoke Kong (Note 3)	50	4,300	372	125	4,847
Lee Huat Oon	50	3,924	275	90	4,339
Dato' Sri Tay Ah Lek	100	2,775	–	–	2,875
Dato' Chang Kat Kiam	100	2,775	–	–	2,875
Wong Kong Ming	50	2,775	–	–	2,825
Dato' Yeoh Chin Kee	100	486	–	–	586
Lee Chin Guan	100	486	–	–	586
Geh Cheng Hooi, Paul (Note 4)	100	486	–	–	586
	855	18,493	647	215	20,210

Notes:

- Salaries and other benefits included basic salaries, housing, other allowances, benefits in kind and employee share option benefits. In last year, the employee share option benefits represent fair value at the date of share options granted and accepted under the Scheme included in the income statement disregarding whether the options have been exercised or not.
- Appointed on 1 July 2006.
- The director occupies a property of the Group rent free. The estimated monetary value of the accommodation so provided to him and not charged to the income statement is HK\$636,000 (2005: HK\$576,000).
- Resigned on 1 July 2006.

Notes to Financial Statements

9. FIVE HIGHEST PAID INDIVIDUALS

The five highest paid individuals during the year included two (2005: five) directors, details of whose remuneration are set out in note 8 above.

Details of the remaining three highest paid individuals' remuneration in 2006 are as follows:

	Group 2006 HK\$'000
Basic salaries, housing, other allowances and benefits in kind	2,642
Bonuses paid and payable	392
Pension scheme contributions	157
	3,191

The number of highest paid individuals in 2006 whose remuneration fell within the bands set out below is as follows:

	2006 Number of individuals
Nil-HK\$1,000,000	1
HK\$1,000,001-HK\$1,500,000	2
	3

10. TAX

	Group 2006 HK\$'000	2005 HK\$'000
Current tax charge:		
Hong Kong	93,260	80,851
Elsewhere	2,627	–
Over-provisions in prior years	(1,700)	–
Deferred tax charge (Note 32)	5,271	2,741
	99,458	83,592

Hong Kong profits tax has been provided at the rate of 17.5% (2005: 17.5%) on the estimated assessable profits arising in Hong Kong during the year. Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the countries in which the Group operates, based on existing legislation, interpretations and practices in respect thereof.

Notes to Financial Statements

10. TAX (Continued)

A reconciliation of the tax expense applicable to profit before tax using the statutory rates for the locations in which the Company and its subsidiaries and a jointly-controlled entity are domiciled to the tax expense at the effective tax rates, and a reconciliation of the applicable rates to the effective tax rates, are as follows:

	2006					
	Hong Kong		Mainland China		Total	
	HK\$'000	%	HK\$'000	%	HK\$'000	%
Profit before tax	578,583		17,512		596,095	
Tax at the applicable tax rate	101,252	17.5	2,627	15.0	103,879	17.5
Share of profits and losses of a jointly-controlled entity	(37)	-	-	-	(37)	-
Estimated tax effect of net income that is not taxable	(1,294)	(0.2)	-	-	(1,294)	(0.3)
Estimated tax losses from previous periods utilised	(1,463)	(0.3)	-	-	(1,463)	(0.2)
Estimated tax losses not recognised	73	-	-	-	73	-
Adjustments in respect of current tax of previous periods	-	-	(1,700)	(9.7)	(1,700)	(0.3)
Tax charge at the Group's effective rate	98,531	17.0	927	5.3	99,458	16.7
	2005					
	Hong Kong		Mainland China		Total	
	HK\$'000	%	HK\$'000	%	HK\$'000	%
Profit before tax	529,889		-		529,889	
Tax at the applicable tax rate	92,731	17.5	-	-	92,731	17.5
Estimated tax effect of net income that is not taxable	(8,883)	(1.7)	-	-	(8,883)	(1.7)
Estimated tax losses from previous periods utilised	(571)	(0.1)	-	-	(571)	(0.1)
Estimated tax losses not recognised	315	0.1	-	-	315	0.1
Tax charge at the Group's effective rate	83,592	15.8	-	-	83,592	15.8

11. PROFIT ATTRIBUTABLE TO EQUITY HOLDERS OF THE HOLDING COMPANY

The consolidated profit attributable to equity holders of the holding company for the year ended 31 December 2006 included a profit of HK\$354,884,000 (2005: HK\$597,696,000) which has been dealt with in the financial statements of the Company (note 38).

Notes to Financial Statements

12. DIVIDENDS

	2006 HK\$ per ordinary share	2005 HK\$ per ordinary share	2006 HK\$'000	2005 HK\$'000
Interim:				
First	0.05	0.06	54,695	43,755
Second	0.20	0.40	218,779	291,706
Special	–	0.29	–	211,487
	0.25	0.75	273,474	546,948

13. EARNINGS PER SHARE

(a) Basic earnings per share

The calculation of basic earnings per share is based on the profit for the year of HK\$496,637,000 (2005: HK\$446,297,000) and the weighted average number of 992,998,391 (2005: 715,880,181) ordinary shares in issue during the year.

(b) Diluted earnings per share

The calculation of diluted earnings per share is based on the profit for the year of HK\$496,637,000 (2005: HK\$446,297,000) and on the weighted average number of 994,185,625 (2005: 717,699,181) ordinary shares, being the weighted average number of 992,998,391 (2005: 715,880,181) ordinary shares in issue during the year as used in the basic earnings per share calculation and the weighted average number of 1,187,234 (2005: 1,819,000) ordinary shares assumed to have been issued at no consideration on the deemed exercise of all share options outstanding during the year.

	2006 HK\$'000	2005 HK\$'000
Profit for the year, used in the basic and diluted earnings per share calculation	496,637	446,297
Weighted average number of ordinary shares in issue during the year used in the basic earnings per share calculation	992,998,391	715,880,181
Weighted average number of ordinary shares assumed issued at no consideration on deemed exercise of all share options outstanding during the year	1,187,234	1,819,000
Weighted average number of ordinary shares used in diluted earnings per share calculation	994,185,625	717,699,181
Diluted earnings per share (HK\$)	0.500	0.622

Notes to Financial Statements

14. CASH AND SHORT TERM PLACEMENTS

	Group		Company	
	2006	2005	2006	2005
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Cash and balances with banks and other financial institutions	289,424	80,756	2,844	377
Money at call and short notice	2,005,795	372,253	916,890	369,591
	2,295,219	453,009	919,734	369,968

Cash and balances with banks and other financial institutions earn interest at floating rates based on daily bank deposit rates. Money at call and short notice are made for various periods of between one day and one month depending on the immediate cash requirement of the Group and the Company, and earn interest at the respective short term time deposit rates.

15. PLACEMENTS WITH BANKS AND FINANCIAL INSTITUTIONS MATURING BETWEEN ONE AND TWELVE MONTHS

The Group's maturity profile of the placements with banks and financial institutions maturing between one and twelve months at the balance sheet date is analysed by the remaining periods to their contractual maturity dates as follows:

	Group	
	2006	2005
	HK\$'000	HK\$'000
Repayable:		
Within three months or less	481,966	5,000
Within one year or less but over three months	84,807	–
	566,773	5,000

In the prior year, the Group's placements with banks amounting to HK\$5,000,000 were pledged to a bank for credit facilities of HK\$5,000,000 granted to the Group. The credit facilities were cancelled in current year and the pledged bank balance was released accordingly. The credit facilities were not utilised in the prior year.

16. SECURITIES MEASURED AT FAIR VALUE THROUGH PROFIT OR LOSS

	Group	
	2006	2005
	HK\$'000	HK\$'000
Unlisted investment funds, at quoted market price	10,213	–

Notes to Financial Statements

17. AVAILABLE-FOR-SALE SECURITY INVESTMENTS

	Group	
	2006 HK\$'000	2005 HK\$'000
Listed security investment in Hong Kong, at market value:		
At beginning of year	25,881	16,744
Change in fair value (Note 38)	42,947	9,137
Sub-total	68,828	25,881
Unlisted security investment, at cost:		
At beginning of year	–	–
Acquisition of subsidiaries	6,804	–
Sub-total	6,804	–
Total at end of year	75,632	25,881

The Group's listed available-for-sale security investment is non-current in nature and represents 805,000 ordinary shares of HK\$1.00 each in Hong Kong Exchanges and Clearing Limited.

18. HELD-TO-MATURITY SECURITIES

	Group	
	2006 HK\$'000	2005 HK\$'000
Debt securities and exchange fund bills, at amortised cost:		
– listed in Hong Kong	19,980	–
– listed outside Hong Kong	46,661	–
– unlisted*	3,612,963	–
	3,679,604	–
Market value of listed held-to-maturity securities	66,158	–

* Included certificates of deposits held of HK\$564,186,000 (2005: Nil) and treasury bills of HK\$99,224,000 (2005: Nil). Treasury bills of HK\$19,900,000 (2005: Nil) were with original maturity within three months.

Notes to Financial Statements

18. HELD-TO-MATURITY SECURITIES (Continued)

The maturity profile of treasury bills as at the balance sheet date was as follows:

	Group	
	2006 HK\$'000	2005 HK\$'000
With a residual maturity of:		
Three months or less	49,893	–
One year or less but over three months	49,331	–
	99,224	–

The held-to-maturity securities analysed by issuers as at the balance sheet date were as follows:

	Group	
	2006 HK\$'000	2005 HK\$'000
Central government and central banks	99,224	–
Public sector entities	23,329	–
Banks and other financial institutions	3,214,200	–
Corporate entities	342,851	–
	3,679,604	–

The maturity profile of held-to-maturity securities as at the balance sheet date was as follows:

	Group	
	2006 HK\$'000	2005 HK\$'000
Repayable:		
Within three months or less	1,133,079	–
Within one year or less but over three months	506,222	–
Within five years or less but over one year	1,902,156	–
Over five years	138,147	–
	3,679,604	–

Notes to Financial Statements

19. INVESTMENT PROPERTIES

	Group HK\$'000	Company HK\$'000
At valuation:		
At 1 January 2005	106,255	32,412
Transfer from owner-occupied property	11,572	–
Carrying amount before change in fair value	117,827	32,412
Change in fair value	30,160	12,588
At 31 December 2005 and 1 January 2006	147,987	45,000
Acquisition of subsidiaries	21,660	–
Disposals	(3,700)	–
Carrying amount before change in fair value	165,947	45,000
Change in fair value	30,719	8,000
At 31 December 2006	196,666	53,000

The Group's investment properties are all situated in Hong Kong and are held under the following lease terms:

	Group 2006 HK\$'000	Company 2006 HK\$'000
At valuation:		
Medium term leases	61,472	–
Long term leases	135,194	53,000
	196,666	53,000

In the prior year, the carrying amounts of the investment properties transferred from owner-occupied properties approximated the fair values at the date of transfer.

Investment properties with a carrying amount of HK\$165,947,000 were revalued at HK\$196,666,000 based on the revaluation report issued by Chung Sen Surveyors Limited, a firm of independent professionally qualified valuers, on an open market value based on their existing use. The increase in fair value of HK\$30,719,000 resulting from the above valuation has been credited to the income statement.

The investment properties held by the Group are let under operating leases from which the Group earns rental income. Details of future annual rental receivables under operating leases are included in note 40(a) to the financial statements.

Notes to Financial Statements

20. PROPERTY, PLANT AND EQUIPMENT

	Group			Total HK\$'000	Company
	Leasehold buildings HK\$'000	Leasehold improvements, fixtures and equipment HK\$'000	Motor vehicles HK\$'000		Leasehold buildings HK\$'000
Cost:					
At 1 January 2005	26,593	76,247	2,746	105,586	-
Additions	-	1,793	-	1,793	-
Transfer to investment properties	(2,416)	-	-	(2,416)	-
Disposals/write-off	-	(4,820)	-	(4,820)	-
At 31 December 2005 and 1 January 2006	24,177	73,220	2,746	100,143	-
Acquisition of subsidiaries	41,751	10,640	696	53,087	-
Additions	-	6,044	-	6,044	-
Disposals/write-off	(9)	(4,315)	(658)	(4,982)	-
At 31 December 2006	65,919	85,589	2,784	154,292	-
Accumulated depreciation:					
At 1 January 2005	7,007	72,713	2,746	82,466	-
Provided during the year	677	1,560	-	2,237	-
Transfer to investment properties	(1,111)	-	-	(1,111)	-
Disposals/write-off	-	(4,785)	-	(4,785)	-
At 31 December 2005 and 1 January 2006	6,573	69,488	2,746	78,807	-
Provided during the year	1,194	7,274	41	8,509	-
Disposals/write-off	(5)	(3,847)	(175)	(4,027)	-
At 31 December 2006	7,762	72,915	2,612	83,289	-
Net book value:					
At 31 December 2006	58,157	12,674	172	71,003	-
At 31 December 2005	17,604	3,732	-	21,336	-

Notes to Financial Statements

21. LAND LEASE PREPAYMENTS

	Group HK\$'000
Cost:	
At 1 January 2005	293,441
Transfer to investment properties	(24,311)
	269,130
At 31 December 2005 and 1 January 2006	328,499
Acquisition of subsidiaries	(82)
Disposals	(82)
	597,547
At 31 December 2006	597,547
Accumulated amortisation and impairment:	
At 1 January 2005	50,257
Provided during the year	2,863
Transfer to investment properties	(14,044)
Reversal of an impairment loss	(3,514)
	35,562
At 31 December 2005 and 1 January 2006	4,670
Provided during the year	(21)
Disposals	(4,694)
Reversal of an impairment loss	(4,694)
	35,517
At 31 December 2006	35,517
Net book value:	
At 31 December 2006	562,030
At 31 December 2005	233,568

The leasehold land lease prepayments of the Group are situated in Hong Kong and held under the following lease terms:

	Group 2006 HK\$'000
Net book value:	
Medium term leases	181,009
Long term leases	381,021
	562,030

The land leases are stated at recoverable amount subject to an impairment test pursuant to HKAS 36 which is based on the higher of fair value less costs to sell and value in use. The recoverable amount of one land lease was stated at fair value, which was higher than its value in use. A reversal of impairment of HK\$4,694,000 (2005: HK\$3,514,000) was credited to the income statement due to increase in fair value as at 31 December 2006. The fair value less costs of the land lease was determined with reference to a qualified external valuer's valuation.

The current and non-current portions of the land lease prepayments were HK\$4,670,000 and HK\$557,360,000 (2005: HK\$2,863,000 and HK\$230,705,000) respectively.

Notes to Financial Statements

22. INTERESTS IN SUBSIDIARIES

	Company	
	2006	2005
	HK\$'000	HK\$'000
Unlisted shares, at cost	5,362,792	769,444
Amount due from subsidiaries	249,941	288,128
	5,612,733	1,057,572

The amounts due from subsidiaries were unsecured, and had no fixed terms of repayments. The amounts due from subsidiaries of HK\$16,000,000 (2005: Nil) were interest-bearing and current in nature while HK\$233,941,000 (2005: HK\$288,128,000) were non-interest-bearing and non-current in nature. Their carrying amounts approximate their fair values.

Particulars of the Company's subsidiaries are as follows:

Name	Nominal value of issued ordinary share capital HK\$	Percentage of equity attributable to the Company		Principal activities
		Direct	Indirect	
Public Bank (Hong Kong) Limited (formerly known as "Asia Commercial Bank Limited") #	810,000,000	100	–	Provision of banking, financial and related services
Public Bank (Nominees) Limited (formerly known as "Asia Commercial Bank (Nominees) Limited") #	100,000	–	100	Provision of nominee services
PB Finance Limited (formerly known as "ACB Finance Limited") #	25,000,000	–	100	Dormant
Public Investments Limited (formerly known as "Hocomban Investments Limited") #	5,000,000	–	100	Property investment
Public Realty Limited (formerly known as "Hocomban Realty Limited") #	100,000	–	100	Dormant
Public Credit Limited (formerly known as "AFH Credit Limited") #	5,000,000	–	100	Dormant
Public Futures Limited (formerly known as "Asia Financial (Futures) Limited") #	20,000,000	–	100	Dormant

Notes to Financial Statements

22. INTERESTS IN SUBSIDIARIES (Continued)

Name	Nominal value of issued ordinary share capital HK\$	Percentage of equity attributable to the Company		Principal activities
		Direct	Indirect	
Public Pacific Securities Limited (formerly known as "Asia Financial Pacific (Securities) Limited") #	12,000,000	–	100	Dormant
Public Financial Securities Limited (formerly known as "Asia Financial (Securities) Limited") #	15,000,000	–	100	Securities brokerage
Public Finance Limited (formerly known as "JCG Finance Company, Limited")	258,800,000	100	–	Deposit-taking and finance
Public Financial Limited	10,100,000	–	100	Investment holding
Public Securities Limited (formerly known as "JCG Securities Limited")	10,000,000	–	100	Securities brokerage
Public Securities (Nominees) Limited (formerly known as "JCG Nominees Limited")	10,000	–	100	Provision of nominee services
Winton (B.V.I.) Limited	61,773	100	–	Investment and property holding
Winton Holdings (Hong Kong) Limited	20	–	100	Property holding
Winton Financial Limited	4,000,010	–	100	Provision of financing for licensed public vehicles and provision of personal and short term loans
Winton Motors, Limited	78,000	–	100	Trading of taxi licences and taxi cabs, and leasing of taxis
Winsure Company, Limited	1,600,000	–	96.9	Dormant

Acquired during the year

Note: Except for Winton (B.V.I.) Limited, which was incorporated in the British Virgin Islands, all other subsidiaries were incorporated in Hong Kong. Except for Public Bank (Hong Kong) Limited which operates in Hong Kong, Mainland China and Taiwan, all other subsidiaries operate in Hong Kong.

Notes to Financial Statements

23. INTEREST IN A JOINTLY-CONTROLLED ENTITY

	Group 2006 HK\$'000	2005 HK\$'000
Share of net assets other than goodwill	1,676	–

Particulars of the Group's jointly-controlled entity are as follows:

Name	Business structure	Place of incorporation and operations	Percentage of ownership interest and profit sharing	Voting power	Principal activity
Net Alliance Co. Limited #	Corporate	Hong Kong	17.6	2 out of 8 *	Provision of electronic banking support services

Acquired during the year

* Representing the number of votes on the board of directors attributable to the Group

24. OTHER ASSETS

	Note	Group		Company	
		2006 HK\$'000	2005 HK\$'000	2006 HK\$'000	2005 HK\$'000
Interest receivable from authorised institutions		51,439	258	1,695	4,489
Other debtors, deposits and prepayments		209,644	34,160	7,142	156
Positive fair values of derivatives	41(b)	12,780	–	–	–
		273,863	34,418	8,837	4,645

The Group's interest receivable from authorised institutions was current in nature at 31 December 2006 and 2005. The current and non-current portion of the Group's other debtors, deposits and prepayments were HK\$201,032,000 and HK\$8,612,000 (2005: HK\$27,992,000 and HK\$6,168,000) respectively.

The Company's interest receivable from authorised institutions was current in nature while the Company's other debtors, deposits and prepayments were non-current in nature at 31 December 2006 and 2005.

The carrying amounts of the other debtors, deposits and prepayments approximate their fair values.

Notes to Financial Statements

25. GOODWILL

	Group	
	2006	2005
	HK\$'000	HK\$'000
Cost:		
At beginning of year	–	–
Additions	2,774,403	–
At end of year	2,774,403	–

On 14 February 2006, the Company and Asia Financial Holdings Limited (“AFH”) entered into a share purchase agreement (“SPA”) pursuant to which AFH agreed to sell and the Company agreed to purchase, the entire issued and paid-up share capital of Public Bank (Hong Kong) for a consideration of HK\$4,499,550,000 (the “Consideration”). The Consideration was subsequently adjusted to HK\$4,584,999,000. The total cost of acquisition of Public Bank (Hong Kong) amounted to HK\$4,593,348,000, including legal and professional fees and stamp duty of HK\$8,349,000, which were directly attributable to the acquisition of Public Bank (Hong Kong). The fair value of net assets and the carrying amount of goodwill amounted to HK\$1,818,945,000 and HK\$2,774,403,000, respectively (note 44).

On 17 February 2006, the Company passed a board resolution to make a rights issue of not less than 364,632,206 rights shares and not more than 386,571,206 rights shares to shareholders at HK\$7.30 per share on the basis of one rights share for every two shares held on 17 March 2006 (the “Rights Issue”). Pursuant to the Rights Issue, 364,632,206 shares of HK\$0.1 each were issued at HK\$7.3 per share. The net proceeds from the Rights Issue, after deduction of related expenses, amounted to approximately HK\$2,660,504,000.

Impairment test of goodwill

Goodwill acquired through business combinations was allocated to the cash-generating unit (the “CGU”) representing an operating entity within the business segment identified by the Group. The acquired subsidiaries involved in retail and commercial banking and treasury and other businesses. The recoverable amounts of the CGU are determined based on a value in use for calculation. The calculation uses cash flow projections based on financial budgets approved by management covering a five-year period and assumed growth rates are used to extrapolate the cash flows in the following 45 years. All cash flows are discounted at a discount rate of 7%. Management’s financial model assumes an overall growth rate of 10% per annum during the first 5 years, and 5% from the sixth to fiftieth year per annum. The discount rates used is based on the rate which reflect specific risks relating to the CGU.

No impairment loss has been recognised in respect of goodwill for the year ended 31 December 2006 as its value in use exceeded the carrying amount.

Notes to Financial Statements

26. INTANGIBLE ASSETS

	Group	
	2006	2005
	HK\$'000	HK\$'000
Cost:		
At beginning of year	126	126
Acquisition of subsidiaries	599	–
At end of year	725	126

The intangible assets represent four units of Stock Exchange Trading Right and one unit of Futures Exchange Trading Right in Hong Kong Exchanges and Clearing Limited.

27. LOANS TO DIRECTORS AND OFFICERS

Loans granted by the Group to directors and officers disclosed pursuant to Section 161B(10) of the Hong Kong Companies Ordinance are as follows:

	Group	
	2006	2005
	HK\$'000	HK\$'000
Aggregate amount of principal and interest outstanding at end of year	1,067	1,135
Maximum aggregate amount of principal and interest outstanding during the year	1,165	1,227

28. DEPOSITS AND BALANCES OF BANKS AND OTHER FINANCIAL INSTITUTIONS

The Group's maturity profile of deposits and balances of banks and other financial institutions at the balance sheet date is analysed by the remaining periods to their contractual maturity dates as follows:

	Group	
	2006	2005
	HK\$'000	HK\$'000
Repayable:		
On demand	12,811	–
Within three months or less	493,324	–
Within one year or less but over three months	9,962	–
	516,097	–

Notes to Financial Statements

29. CUSTOMER DEPOSITS

	Group	
	2006	2005
	HK\$'000	HK\$'000
Demand deposits and current accounts	640,534	–
Savings deposits	2,016,059	–
Time, call and notice deposits	12,197,062	1,641,978
	14,853,655	1,641,978

The Group's maturity profile of customer deposits at the balance sheet date is analysed by the remaining periods to their contractual maturity dates as follows:

	Group	
	2006	2005
	HK\$'000	HK\$'000
Repayable:		
On demand	2,662,221	3,648
Within three months or less	10,582,550	1,051,642
Within one year or less but over three months	1,083,649	108,692
Within five years or less but over one year	40,414	1,268
	14,368,834	1,165,250
Connected deposits	484,821	476,728
	14,853,655	1,641,978

The connected deposits were repayable and subject to renewal by a fellow subsidiary within one year.

Notes to Financial Statements

30. CERTIFICATES OF DEPOSITS ISSUED

All the certificates of deposits issued are measured at amortised cost. The Group's maturity profile of certificates of deposits issued at the balance sheet date is analysed by the remaining periods to their contractual maturity dates as follows:

	Group	
	2006	2005
	HK\$'000	HK\$'000
Repayable:		
Within three months or less	249,979	–
Within one year or less but over three months	419,751	–
Within five years or less but over one year	99,944	–
	769,674	–

31. BANK LOANS

	Group and Company	
	2006	2005
	HK\$'000	HK\$'000
Unsecured bank loans	2,000,000	–
Repayable:		
In the second to fifth years, inclusive	2,000,000	–

On 21 July 2006, the Company entered into a facility agreement (the "Facility Agreement") with Barclays Capital and others as mandated lead arrangers and Barclays Bank PLC as an agent and certain original lenders, including Public Bank (L) Ltd ("PB(L)L"), a fellow subsidiary of the Company, for a Hong Kong dollar 3-year term loan facility in an aggregate amount of HK\$2,000,000,000 (the "Facility").

The bank loans are denominated in Hong Kong dollars. The carrying amounts of the bank loans approximate their fair values and bear interests at floating interest rates and the effective interest rate at 4.74% per annum.

Notes to Financial Statements

32. DEFERRED TAX

The movements in deferred tax assets and liabilities during the year are as follows:

Group

Deferred tax assets:

	At 1 January 2005 HK\$'000	Deferred tax (charged)/ credited to the income statement HK\$'000	At 31 December 2005 and 1 January 2006 HK\$'000	Acquisition of subsidiaries HK\$'000	Deferred tax charged to the income statement HK\$'000	At 31 December 2006 HK\$'000
Collective impairment allowances for loans and advances and receivables	2,684	(1,077)	1,607	3,766	(111)	5,262
Losses available for offset against future taxable profit	1,048	(571)	477	–	(477)	–
Unrealised profit in inventories	–	483	483	–	(128)	355
Accelerated allowances depreciation	–	287	287	–	(287)	–
Fair value adjustment on held-to-maturity securities	–	–	–	13,020	(788)	12,232
	3,732	(878)	2,854	16,786	(1,791)	17,849

Deferred tax liabilities:

	At 1 January 2005 HK\$'000	Deferred tax charged/ (credited) to the income statement HK\$'000	At 31 December 2005 and 1 January 2006 HK\$'000	Acquisition of subsidiaries HK\$'000	Deferred tax charged to the income statement HK\$'000	At 31 December 2006 HK\$'000
Interest receivable that will be taxable only when received	2,034	(2,034)	–	–	–	–
Accelerated tax depreciation and revaluation surplus of investment properties	9,513	3,897	13,410	47,442	3,480	64,332
	11,547	1,863	13,410	47,442	3,480	64,332

The Group has tax losses arising in Hong Kong of HK\$42,549,000 (2005: HK\$11,374,000) that are available indefinitely for offsetting against future taxable profits of the companies in which the losses arose. Deferred tax assets have not been recognised in respect of these losses as they have arisen in subsidiaries that have incurred losses for some time.

The deferred tax liabilities of the Company of HK\$3,700,000 (2005: HK\$2,200,000) represented accelerated tax depreciation and revaluation surplus of investment properties.

There are no significant income tax consequences attaching to the payment of dividends by the Company to its shareholders.

Notes to Financial Statements

33. OTHER LIABILITIES

	Notes	Group		Company	
		2006 HK\$'000	2005 HK\$'000	2006 HK\$'000	2005 HK\$'000
Creditors, accruals and interest payable		454,834	86,995	1,600	1,013
Amount due to the ultimate holding company		541	338	500	300
Provision for long service payments	34	3,892	4,006	–	–
Negative fair values of derivatives	41(b)	9,735	–	–	–
		469,002	91,339	2,100	1,313

As the trade payables were immaterial to the Group, the maturity profile thereof has not been disclosed. The other liabilities, other than the provision for long service payments, were current in nature.

The carrying amounts of the creditors, accruals and interest payable approximate their fair values.

34. PROVISION FOR LONG SERVICE PAYMENTS

	Group	
	2006 HK\$'000	2005 HK\$'000
Balance at beginning of year	4,006	4,268
Movement during the year	(114)	(262)
Balance at end of year	3,892	4,006

The Group provides for the probable future long service payments expected to be made to employees under the Employment Ordinance, as explained under the heading "Employment Ordinance long service payments" in note 2.4 to the financial statements.

Notes to Financial Statements

35. SHARE CAPITAL

	2006 HK\$'000	2005 HK\$'000
Ordinary shares		
Authorised:		
2,000,000,000 (2005: 1,000,000,000) ordinary shares of HK\$0.10 each (Note (a))	200,000	100,000
	Number of ordinary shares of HK\$0.10 each	Share capital HK\$'000
Issued and fully paid:		
At 1 January 2005	707,758,412	70,776
Shares issued on exercise of share options (Note (b))	21,506,000	2,150
At 31 December 2005 and 1 January 2006	729,264,412	72,926
Rights Issue (Note 25)	364,632,206	36,464
At 31 December 2006	1,093,896,618	109,390

Notes:

- (a) Pursuant to an ordinary resolution passed on 8 March 2006, the authorised share capital of the Company was increased from HK\$100,000,000 to HK\$200,000,000 by the creation of 1,000,000,000 additional shares of HK\$0.10 each ranking pari passu in all respects with the existing shares of the Company.
- (b) The increase in issued share capital represented the shares issued on exercise of share options pursuant to the share option scheme for the year ended 31 December 2005.

Notes to Financial Statements

36. SHARE OPTION SCHEME

Under the Scheme approved on 28 February 2002, the board of directors passed a board resolution on 18 May 2005 to grant share options to subscribe for a total of 66,526,000 shares in the Company to eligible participants, including directors and employees of the Company and its subsidiaries. Each share option gives the holder the right to subscribe for one ordinary share. 65,976,000 share options were accepted by the directors and employees of the Group. The Group is not legally bound or obliged to repurchase or settle the options in cash.

Pursuant to the terms of the Scheme, an adjustment is required to be made to the exercise price and/or the number of shares falling to be issued upon exercise of the outstanding share options as a result of the Rights Issue. After the completion of the Rights Issue, the exercise price of the outstanding share options was adjusted from HK\$7.29 per share to HK\$6.35 per share and there was no adjustment to the number of shares falling to be issued.

Particulars in relation to the Scheme that are required to be disclosed under Rules 17.07 to 17.09 of Chapter 17 of the Listing Rules and HKAS 19 “Employee benefits” are as follows:

(a) Summary of the Scheme

Purpose	:	To attract, retain and motivate talented eligible participants.
Participants	:	Eligible participants include: <ul style="list-style-type: none"> (i) any employee and director of the Company or any subsidiary or any associate or controlling shareholder; (ii) any discretionary trust whose discretionary objects include person(s) belonging to the aforesaid participants; (iii) a company beneficially owned by person(s) belonging to the aforesaid participants; and (iv) any business partner, agent, consultant, representative, customer or supplier of any member of the Group or controlling shareholder determined by the board of directors as having contributed or may contribute to the development and growth of the Group.
Total number of ordinary shares available for issue and the percentage of the issued share capital that it represents as at the date of this annual report	:	72,926,441 ordinary shares which represent 6.7% of the issued share capital.

Notes to Financial Statements

36. SHARE OPTION SCHEME (Continued)

(a) Summary of the Scheme (Continued)

Maximum entitlement of each participant	:	Shall not exceed 1% of the ordinary shares of the Company in issue in the 12-month period up to and including the date of grant.
Period within which the ordinary shares must be taken up under an option	:	Exercisable within open exercise periods determined by the board of directors within 10 years from the commencement date on which the option is granted and accepted.
Amount payable on acceptance	:	HK\$1.00
Basis of determining the exercise price	:	Determined by the directors at their discretion based on the higher of: <ul style="list-style-type: none"> (i) the closing price of the ordinary shares on the Stock Exchange at the offer date; (ii) the average closing price of the ordinary shares on the Stock Exchange for 5 business days immediately preceding the offer date; and (iii) the nominal value of an ordinary share.
Vesting condition	:	Nil, subject to open exercise periods to be determined by the board of directors or the Share Option Committee. The first open exercise period was from 28 July 2005 to 10 September 2005.
The remaining life of the Scheme	:	The Scheme remains in force until 27 February 2012.

Notes to Financial Statements

36. SHARE OPTION SCHEME (Continued)

(b) Movement of share options

Name	Number of share options				Outstanding at the end of the year
	Outstanding at the beginning of the year	Granted and accepted during the year	Lapsed during the year	Exercised during the year	
<i>Directors</i>					
Tan Yoke Kong	1,928,000	–	–	–	1,928,000
Lee Huat Oon	3,170,000	–	–	–	3,170,000
Dato' Sri Tay Ah Lek	1,680,000	–	–	–	1,680,000
Dato' Chang Kat Kiam	1,680,000	–	–	–	1,680,000
Wong Kong Ming	4,000,000	–	–	–	4,000,000
Dato' Yeoh Chin Kee	700,000	–	–	–	700,000
Lee Chin Guan	350,000	–	–	–	350,000
Geh Cheng Hooi, Paul (resigned on 1 July 2006)	700,000	–	–	–	700,000
<i>Employees working under "continuous contracts" for the purposes of the Employment Ordinance other than the directors as disclosed above</i>					
	29,670,000	–	810,000	–	28,860,000
	43,878,000	–	810,000	–	43,068,000

Notes:

- (i) The share options are only exercisable at the exercise price of HK\$6.35 per share during certain periods as notified by the board or the Share Option Committee to each grantee which it may in its absolute discretion determine from 10 June 2005 to 9 June 2015.
- (ii) There was no open exercise period during the year.
- (iii) The remaining contractual life of the 43,068,000 outstanding options was 8.44 years as at 31 December 2006.
- (iv) The share option outstanding at end of 2006 can only be exercised in future open exercise periods.

- (c) Had all the outstanding share options been fully exercised on 29 December 2006, the last trading date of 2006, the Group would have received proceeds of HK\$273,481,800 (2005: HK\$319,870,620). The market value of the shares issued based on the closing price of HK\$6.15 (2005: HK\$8.15) per share on that date would have been HK\$264,868,200 (2005: HK\$357,605,700). The directors and employees concerned under the Scheme would have made no gain from the exercise of share options (2005: HK\$0.86 per share or, in aggregate, HK\$37,735,080).

Notes to Financial Statements

37. EMPLOYEE SHARE-BASED COMPENSATION RESERVE

	Group	
	2006 HK\$'000	2005 HK\$'000
At beginning of year	45,765	–
Employee share option benefits	–	45,765
At end of year	45,765	45,765

38. RESERVES

Group	Share	Capital	Contributed	Available-	Employee	Regulatory	Retained	Total
	premium	redemption	surplus	for-sale	share-	reserve	profits	
	account	reserve	surplus	investment	based	reserve	profits	
	HK\$'000	HK\$'000	HK\$'000	reserve	reserve	HK\$'000	HK\$'000	HK\$'000
At 1 January 2005	1,209,593	829	96,116	16,481	–	75,686	812,966	2,211,671
Change in fair value and total income and expense recognised directly in equity (Note 17)	–	–	–	9,137	–	–	–	9,137
Employee share option benefits	–	–	–	–	45,765	–	–	45,765
Profit for the year	–	–	–	–	–	–	446,297	446,297
Premium, net of expense, arising on share options exercised	154,586	–	–	–	–	–	–	154,586
Transfer from retained profits	–	–	–	–	–	9,714	(9,714)	–
Dividends for 2005 (Note 12)	–	–	–	–	–	–	(546,948)	(546,948)
At 31 December 2005 and 1 January 2006	1,364,179	829	96,116	25,618	45,765	85,400	702,601	2,320,508
Change in fair value and total income and expense recognised directly in equity (Note 17)	–	–	–	42,947	–	–	–	42,947
Profit for the year	–	–	–	–	–	–	496,637	496,637
Premium, net of expense, arising on Rights Issue	2,624,040	–	–	–	–	–	–	2,624,040
Transfer from retained profits	–	–	–	–	–	10,481	(10,481)	–
Dividends for 2006 (Note 12)	–	–	–	–	–	–	(273,474)	(273,474)
At 31 December 2006	3,988,219	829	96,116	68,565	45,765	95,881	915,283	5,210,658

Notes to Financial Statements

38. RESERVES (Continued)

Company	Share premium account HK\$'000	Capital redemption reserve HK\$'000	Contributed surplus HK\$'000	Available- for-sale investment revaluation reserve HK\$'000	Employee share- based compensation reserve HK\$'000	Regulatory reserve HK\$'000	Retained profits HK\$'000	Total HK\$'000
At 1 January 2005	1,209,593	829	194,176	-	-	-	(100,812)	1,303,786
Employee share option benefits	-	-	-	-	45,765	-	-	45,765
Premium, net of expense, arising on share options exercised	154,586	-	-	-	-	-	-	154,586
Dividends for 2005 (Note 12)	-	-	-	-	-	-	(546,948)	(546,948)
Profit for the year	-	-	-	-	-	-	597,696	597,696
At 31 December 2005 and 1 January 2006	1,364,179	829	194,176	-	45,765	-	(50,064)	1,554,885
Premium, net of expense, arising on Rights Issue	2,624,040	-	-	-	-	-	-	2,624,040
Dividends for 2006 (Note 12)	-	-	-	-	-	-	(273,474)	(273,474)
Profit for the year	-	-	-	-	-	-	354,884	354,884
At 31 December 2006	3,988,219	829	194,176	-	45,765	-	31,346	4,260,335

The contributed surplus of the Group represents the excess of the nominal value of the shares of the subsidiaries acquired pursuant to the Group's reorganisation in September 1991 over the nominal value of the Company's shares issued in exchange therefor.

The contributed surplus of the Company represents the excess of the fair value of the shares of the subsidiaries acquired pursuant to the Group's reorganisation in September 1991 over the nominal value of the Company's shares issued in exchange therefor. Under the Companies Act 1981 of Bermuda, a company may make distributions to its shareholders out of the contributed surplus under certain circumstances.

Deducted from the contributed surplus of the Group as at 31 December 2006 were positive goodwill of HK\$98,406,000 (2005: HK\$98,406,000), which arose from the acquisition of certain subsidiaries in prior years.

Notes to Financial Statements

39. NOTE TO THE CONSOLIDATED CASH FLOW STATEMENT

A reconciliation of profit before tax to the net cash flows from operating activities is set out below:

	Group	
	2006	2005
	HK\$'000	HK\$'000
Profit before tax	596,095	529,889
Employee share option benefits	–	45,765
Depreciation and amortisation of land lease prepayments	13,179	5,100
(Gain)/loss on disposal of property, plant and equipment	(204)	30
Decrease in impairment loss and allowances for advances to customers and receivables	(4,298)	(3,071)
Dividends from listed investments	(1,306)	(773)
Dividends from unlisted investments	(780)	–
Amortisation and write-off of commission expenses	288	133
Reversal of an impairment loss on land lease prepayments	(4,694)	(3,514)
Increase in fair value of investment properties	(30,719)	(30,160)
Share of profits and losses of a jointly-controlled entity	(176)	–
Decrease in provision for long service payments	(114)	(262)
Increase/(decrease) in an amount due to the ultimate holding company	203	(56)
Hong Kong profits tax paid	(99,434)	(88,855)
Operating profit before changes in operating assets and liabilities	468,040	454,226
Increase in operating assets:		
Decrease in cash and short term placements	35,767	–
Increase in placements with banks and financial institutions	(55,543)	–
Decrease in securities measured at fair value through profit or loss	15,526	–
Increase in loans and advances and receivables	(1,078,323)	(328,911)
Decrease in held-to-maturity securities	132,402	–
Decrease/(increase) in other debtors, deposits, prepayments and interest receivable from authorised institutions	113,842	(23,969)
Decrease in inventories of taxi licences	2,883	2,661
	(833,446)	(350,219)
Increase/(decrease) in operating liabilities:		
Decrease in deposits and balances of banks and other financial institutions	(255,165)	–
Increase/(decrease) in customer deposits	1,171,208	(78,403)
Decrease in certificates of deposits issued	(654,017)	–
(Decrease)/increase in creditors, accruals and interest payable	(54,258)	19,106
	207,768	(59,297)
Net cash (outflow)/inflow from operating activities	(157,638)	44,710

Notes to Financial Statements

40. OPERATING LEASE ARRANGEMENTS

- (a) The Group leases its investment properties under operating lease arrangements, and the terms of the leases range from one to five years.

As at 31 December 2006, the Group had total future minimum lease rental receivables under non-cancellable operating leases falling due as follows:

	Group	
	2006	2005
	HK\$'000	HK\$'000
Within one year	10,026	7,312
In the second to fifth years, inclusive	8,496	3,418
	18,522	10,730

- (b) The Group entered into non-cancellable operating lease arrangements with landlords, and the terms of the leases range from one to five years.

As at 31 December 2006, the Group had total future minimum lease rental payables under non-cancellable operating leases falling due as follows:

	Group	
	2006	2005
	HK\$'000	HK\$'000
Within one year	25,804	16,172
In the second to fifth years, inclusive	18,225	11,461
	44,029	27,633

Notes to Financial Statements

41. OFF BALANCE SHEET EXPOSURE

(a) Commitments and contingent liabilities

The following is a summary of the contractual amount of each significant class of contingent liabilities and commitments of the Group outstanding:

	Group					
	2006			2005		
	Contractual	Replacement	Risk	Contractual	Replacement	Risk
	amount	cost	weighted	amount	cost	weighted
HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	
Direct credit substitutes	90,111	-	66,060	-	-	-
Transaction-related contingencies	6,842	-	2,955	-	-	-
Trade related contingencies	169,626	-	28,499	-	-	-
Forward deposits placed	3,988	-	798	-	-	-
Forward asset purchases	19,504	-	3,901	-	-	-
Foreign exchange rate contracts	5,286,409	2,295	10,575	-	-	-
Interest rate swap and future contracts	227,780	-	-	-	-	-
Other commitments with an original maturity of:						
Under one year or which are unconditionally cancellable	3,297,666	-	-	773	-	-
One year and over	279,594	-	139,797	-	-	-
Capital commitment contracted for, but not provided in the financial statements	6,308	-	6,308	1,603	-	1,603
	9,387,828	2,295	258,893	2,376	-	1,603

The Group has not entered into any bilateral netting arrangements and accordingly the above amounts are shown on a gross basis. The credit risk weighted amounts are calculated in accordance with the Third Schedule of the Banking Ordinance and guidelines issued by the HKMA. The amounts calculated are dependent upon the status of the counterparty and the maturity characteristics. The risk weights used range from 0% to 100% for contingent liabilities and commitments and from 0% to 50% for exchange rate contracts. Replacement cost represents the cost of replacing all contracts which have a positive value when marked to market.

As at 31 December 2006 and 2005, the Company had no other material outstanding contingent liabilities and commitments.

Notes to Financial Statements

41. OFF BALANCE SHEET EXPOSURE (Continued)**(b) Derivatives**

The following tables set out the summary of the notional amounts, fair values and credit risk weighted amounts of each significant type of derivatives.

	2006	Group	2006
	Contract/ notional amount	Fair values	Fair values
	HK\$'000	of assets	of liabilities
		HK\$'000	HK\$'000
Derivatives held for trading:			
Foreign exchange rate contracts	5,286,409	11,434	8,129
Interest rate swaps and future contracts	227,780	1,346	1,606
	5,514,189	12,780	9,735

The Group and the Company did not have any derivatives held solely for trading at 31 December 2005.

	2006	2005
	Credit risk	Credit risk
	weighted amount	weighted amount
	HK\$'000	HK\$'000
Derivatives held for trading:		
Foreign exchange rate contracts	10,575	–
Interest rate swaps and future contracts	–	–
	10,575	–

Notes to Financial Statements

42. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's principal financial instruments, other than derivatives, comprise bank loans and overdrafts, other interest-bearing loans, certificates of deposits issued, finance leases, and cash and short-term deposits. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial assets such as trade bills, held-to-maturity securities, loans and advances and receivables, available-for-sale securities and securities measured at fair value through profit or loss, which arise directly from its operations.

The Group also enters into derivative transactions, including principally interest rate swaps and forward currency contracts. The purpose is to manage the interest rate and currency risks arising from the Group's operations and its sources of finance.

It is, and has been, throughout the year under review, the Group's policy that no trading in financial instruments shall be undertaken.

The main risks arising from the Group's financial instruments are interest rate risk, credit risk, liquidity risk, foreign currency risk and market risk. The board reviews and agrees policies for managing each of these risks and they are summarised below. The Group's accounting policies in relation to derivatives are set out in note 2.4 to the financial statements.

Risk management

The Group has established policies and procedures for the control and monitoring of credit, liquidity, capital, foreign currency, interest rate and market risks, which are reviewed regularly by the Group's management, Credit Committees, the Assets and Liabilities Committee and Asset and Liability Management Committee. The internal auditors of the Group also perform regular audits to ensure compliance with the policies and procedures.

Interest rate risk management

Interest rate risk is the risk that the Group's position may be adversely affected by a change of market interest rates. The Group's interest rate risk arises primarily from the timing difference in the maturity and the repricing of the Group's interest bearing assets, liabilities and off-balance sheet commitments. The primary objective of interest rate risk management is to limit the potential adverse effects of interest rate movements in net interest income by closely monitoring the net repricing gap of the Group's assets and liabilities. The interest rate risk is managed by the Group's Treasury Department and monitored by management under limits approved by the directors.

Notes to Financial Statements

42. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

Interest rate risk management (Continued)

The carrying amounts of financial instruments exposed to interest rate risk based on maturity or repricing as at 31 December 2006 and 2005 are detailed as follows:

Group	2006						Non-interest bearing HK\$'000	Total HK\$'000
	One year or less HK\$'000	Over 1 year but not more than 2 years HK\$'000	Over 2 years but not more than 3 years HK\$'000	Over 3 years but not more than 4 years HK\$'000	Over 4 years but not more than 5 years HK\$'000	Over 5 years HK\$'000		
	Assets:							
Fixed rate financial assets								
Cash and short term placements	1,954,683	-	-	-	-	-	289,424	2,244,107
Placements with banks and other financial institutions maturing between one and twelve months	452,080	-	-	-	-	-	-	452,080
Loans and advances and receivables	2,235,054	916,689	416,978	107,825	26,671	51,733	157,150	3,912,100
Securities measured at fair value through profit or loss	-	-	-	-	-	-	10,213	10,213
Available-for-sale securities	-	-	-	-	-	-	75,632	75,632
Held-to-maturity securities	1,892,887	137,414	163,545	57,242	38,127	-	-	2,289,215
	6,534,704	1,054,103	580,523	165,067	64,798	51,733	532,419	8,983,347
Floating rate financial assets								
Cash and short-term placements	51,112	-	-	-	-	-	-	51,112
Placements with banks and other financial institutions maturing between one and twelve months	114,693	-	-	-	-	-	-	114,693
Loans and advances and receivables	9,982,891	-	-	-	-	-	62,376	10,045,267
Held-to-maturity securities	1,390,389	-	-	-	-	-	-	1,390,389
Other assets	150,000	-	-	-	-	-	-	150,000
	11,689,085	-	-	-	-	-	62,376	11,751,461
Less:								
Liabilities:								
Fixed rate financial liabilities								
Deposits and balances of banks and other financial institutions	503,286	-	-	-	-	-	12,811	516,097
Customer deposits	11,983,203	39,799	615	-	-	-	-	12,023,617
	12,486,489	39,799	615	-	-	-	12,811	12,539,714
Floating rate liabilities								
Customer deposits	2,232,459	-	-	-	-	-	597,579	2,830,038
Certificates of deposits issued	769,674	-	-	-	-	-	-	769,674
Bank loans	2,000,000	-	-	-	-	-	-	2,000,000
Other liabilities	150,000	-	-	-	-	-	-	150,000
	5,152,133	-	-	-	-	-	597,579	5,749,712
Total interest sensitivity gap	585,167	1,014,304	579,908	165,067	64,798	51,733	(15,595)	2,445,382

Notes to Financial Statements

42. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES
(Continued)

Interest rate risk management (Continued)

Group	2005						Non-interest bearing HK\$'000	Total HK\$'000
	One year or less HK\$'000	Over 1 year but not more than 2 years HK\$'000	Over 2 years but not more than 3 years HK\$'000	Over 3 years but not more than 4 years HK\$'000	Over 4 years but not more than 5 years HK\$'000	Over 5 years HK\$'000		
Assets:								
Fixed rate financial assets								
Cash and short term placements	372,253	-	-	-	-	-	80,756	453,009
Placements with banks and other financial institutions maturing between one and twelve months	5,000	-	-	-	-	-	-	5,000
Loans and advances and receivables	1,721,291	759,399	278,034	51,942	-	69,101	148,664	3,028,431
Available-for-sale securities	-	-	-	-	-	-	25,881	25,881
	2,098,544	759,399	278,034	51,942	-	69,101	255,301	3,512,321
Floating rate financial assets								
Loans and advances and receivables	594,502	-	-	-	-	-	80,001	674,503
Less:								
Liabilities:								
Fixed rate financial liabilities								
Customer deposits	1,640,710	1,268	-	-	-	-	-	1,641,978
Total interest sensitivity gap	1,052,336	758,131	278,034	51,942	-	69,101	335,302	2,544,846

Notes to Financial Statements

42. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

Interest rate risk management (Continued)

The table below summarises the effective average interest rates at 31 December for monetary financial instruments:

	Group	
	2006 HK dollar Rate (%)	2005 HK dollar Rate (%)
Assets		
Cash and short term placements	4.86	3.95
Placements with banks and other financial institutions	5.00	3.10
Loans and advances and receivables (including trade bills)	10.32	23.14
Held-to-maturity securities	4.27	–
Liabilities		
Deposits and balances of banks and other financial institutions	4.59	–
Deposits from customers	4.11	4.00
Certificates of deposits issued	4.78	–
Bank loans	4.74	–

There were no financial assets and liabilities denoted in currency other than the Hong Kong dollar as at 31 December 2006 and 2005.

Credit risk management

Credit risk is the risk that a customer or counterparty in a transaction may default. It arises from the lending, trade finance, treasury and other activities undertaken by the Group.

The Group has a credit risk management process to measure, monitor and control credit risk. Its Credit Policy Manual defines the credit extension and measurement criteria, the credit review, approval and monitoring processes, and the loan classification and provisioning systems. It has a hierarchy of credit authority which approves credit in compliance with the Group's credit policy; exposures are monitored against credit limits and other control limits (such as large exposures and concentration limits); segregation of duties in key credit functions is in place to ensure separate credit control and monitoring; management and recovery of problem credits is handled by an independent work-out team.

The Group manages its credit risk within a conservative framework. Its credit policy is regularly revised, taking into account factors such as prevailing business and economic conditions, regulatory requirements and its capital resources.

Credit and compliance audits are periodically held to evaluate the effectiveness of the credit review, approval and monitoring processes and to test the compliance of the established credit policies and procedures.

Notes to Financial Statements

42. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

Liquidity risk management

Liquidity risk is the risk that the Group cannot meet its current obligation. To manage liquidity risk, the Group has established the liquidity management policy which is reviewed by management and approved by the directors. The Group measures the liquidity of the Group using the statutory liquidity ratio, loan-to-deposit ratio and maturity mismatch portfolio.

The Assets and Liabilities Committee of Public Finance and the Asset and Liability Management Committee of Public Bank (Hong Kong) monitor the liquidity position as part of the ongoing assets and liabilities management, and set up trigger limits to monitor liquidity risk. They also closely monitor the liquidity of the respective subsidiaries on a periodic basis to ensure that the liquidity structure of the respective subsidiaries' assets, liabilities and commitments can meet the funding needs, and that the statutory liquidity ratio is always complied with. Standby facilities are maintained to provide liquidity to meet unexpected, material cash outflows in the ordinary course of business.

Capital management

The Group's policy is to maintain a strong capital base to support the development of the Group's businesses and to meet the statutory capital adequacy ratio and other regulatory capital requirements. Capital is allocated to the various activities of the Group depending on the risk taken by each business division and in accordance with the requirements of relevant regulatory bodies.

Market risk management

Market risk is the risk to the Group's earnings and capital due to changes in the market level of interest rates, securities, foreign exchange and equities as well as the volatilities of those prices.

The Group monitors market risk principally by limits established for transactions and open positions. These limits are reviewed and approved by the directors and are monitored on a daily basis.

The Group does not actively trade in financial instruments and in the opinion of the directors, the market risk related to trading activities to which the Group is exposed is not material. Accordingly, no quantitative market risk disclosures have been prepared.

All foreign exchange positions are managed by the Group's Treasury Department within limits approved by the directors.

Notes to Financial Statements

42. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

Fair value measurement principles

The fair value of financial instruments is based on their quoted market prices at the balance sheet date, or a date close to the balance sheet date, without any deduction for estimated future selling costs. Financial assets are priced at current bid prices, while financial liabilities are priced at current asking prices unless the position is immaterial. In such case, a mid rate will be applied for both long and short positions.

If a quoted market price is not available on a recognised stock exchange or from a broker/dealer for non-exchange-traded financial instruments, the fair value of the instrument is estimated using valuation techniques, including the use of recent arm's-length market transactions, reference to the current fair value of another instrument that is substantially the same, discounted cash flow techniques or any other valuation technique that provides a reliable estimate of prices obtained in actual market transactions.

Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates, and the discount rate used is a market rate at the balance sheet date applicable for an instrument with similar terms and conditions. Where other pricing models are used, inputs are based on market data at the balance sheet date.

Use of derivatives

Being a financial institution, the Group employs derivatives during the course of running its ordinary banking businesses. These derivatives can be either exchange-traded or over-the-counter including interest rate futures, interest rate swaps and options. Before engaging in any such products and instruments, the Group will conduct thorough study and evaluation on both its risk and necessity affecting the Group's operation. In this respect, the Group will consider those over-the-counter derivatives, e.g., options and interest rate swaps, as solely for hedging purposes. While for the exchange-traded instruments, the Group will impose appropriate trading limits together with a daily mark-to-market revaluation process. The Group monitors closely these derivative positions in order to achieve a stable and commensurable contribution to the Group's revenue.

Notes to Financial Statements

43. RELATED PARTY TRANSACTIONS

The Group also had the following major transactions with related parties during the year which were carried out on essentially the same terms and/or at prevailing market rates with other customers or suppliers.

		Group	
	Notes	2006 HK\$'000	2005 HK\$'000
Related party transactions included in the income statement:			
Commission income from the ultimate holding company for referrals of taxi financing loans	(a)	133	196
Interest income from the ultimate holding company	(b)	15,211	198
Rental income from the ultimate holding company	(c)	2,686	2,424
Management fees from the ultimate holding company	(d)	920	863
Services charge paid to the ultimate holding company	(d)	31	6
Interest paid and payable to a fellow subsidiary	(e)	19,762	10,995
Key management personnel compensation:	(f)		
– short-term employee benefits		4,056	3,480
– share-based payment		–	16,515
– post employment benefits		237	215
		4,293	20,210
Interest income received from key management personnel	(g)	42	29
Interest expense paid to key management personnel	(h)	138	3
Commission fee income from key management personnel	(i)	7	28
Post employment benefits for employees other than key management personnel	(j)	8,720	5,654
Related party transactions included in the assets and liabilities:			
Cash and short term funds with the ultimate holding company	(b)	8,446	21,207
Deposits from a fellow subsidiary	(e)	484,821	476,728
Interest payable to fellow subsidiaries	(e)	2,792	1,721
Rental deposits from the ultimate holding company	(c)	541	338
A mortgage loan to key management personnel	(g)	1,037	1,135
Deposits from key management personnel	(h)	10,254	300

Notes to Financial Statements

43. RELATED PARTY TRANSACTIONS (Continued)

Notes:

- (a) The commission income received from referrals of floating rate taxi financing loans to Public Bank was determined based on market practice.
- (b) The Group placed deposits with Public Bank at prevailing market rates. Interest income was received/receivable by the Group for the year from Public Bank in respect of placements with Public Bank, which was included in cash and short term placements in the balance sheet.
- (c) The rental income and deposits were derived from properties rented to:
- (i) Public Bank as its staff quarters for a term of two years commencing on 1 August 2006 at a monthly rental of HK\$20,600;
 - (ii) Public Bank as its office for a term of two years commencing on 1 August 2006 at a monthly rental of HK\$43,800; and
 - (iii) Public Bank as its branch office for a term of three years commencing on 1 November 2006 at a monthly rental of HK\$250,000.
- (d) The management fees arose from administrative services provided by the Group to the ultimate holding company. They were charged based on the cost incurred by the Group during the year.

The services charge arose from the commission paid to the ultimate holding company.

- (e) During the year, fixed deposits were accepted from PB Trust (L) Ltd. ("PB Trust"), a fellow subsidiary of the Company, in the ordinary course of business by Public Finance. The interest was paid/payable to PB Trust for the year by Public Finance in respect of the placements. The balances of the said fixed deposits and interest payable were included in customer deposits and other liabilities, respectively, in the balance sheet.
- (f) Further details of post-employment benefits and directors' remuneration are included in notes 6 and 8 to the financial statements respectively.
- (g) A mortgage loan was granted to one of the directors by Public Finance. Interest income was received from the director.
- (h) During the year, deposits were accepted from directors by Public Bank (Hong Kong) and Public Finance. Interest expenses were paid to the directors.
- (i) The commission income was received from the key management personnel of the Group for securities dealing.
- (j) The Group's post-employment benefit plan for the benefits of employees was detailed in note 6 to the financial statements.

During the year, a syndicated loan of HK\$2,000,000,000 (2005: Nil) was granted to the Company by Barclays Capital and others as mandated lead arrangers and Barclays Bank PLC as an agent and certain original lenders, including PB(L)L. As at 31 December 2006, the bank loan from the fellow subsidiary amounted to HK\$500,000,000 (2005: Nil).

In addition, certain banking facilities of the Group are supported by letters of comfort issued by the ultimate holding company.

Notes to Financial Statements

44. ACQUISITION OF A SUBSIDIARY

During the year, the Company acquired the entire issued and paid-up share capital of Public Bank (Hong Kong). Further details of the acquisition are included in note 25 to the financial statements. The purchase consideration for the acquisition was in the form of cash, with total cost of HK\$4,593,348,000, including legal and professional fees and stamp duty of HK\$8,349,000.

The fair values of the identifiable assets and liabilities of Public Bank (Hong Kong) as at the date of acquisition and the corresponding carrying amounts immediately before the acquisition were as follows:

	Note	Fair value recognised on acquisition HK\$'000	Carrying amount HK\$'000
Net assets acquired:			
Assets:			
Cash and short term placements		2,522,586	2,522,586
Placements with banks and financial institutions maturing between one and twelve months		360,472	360,472
Securities measured at fair value through profit or loss		25,739	25,739
Loans and advances and receivables		9,099,760	9,103,820
Available-for-sale security investment		6,804	6,804
Held-to-maturity securities		3,749,076	3,823,473
Interest in a jointly-controlled entity		1,500	1,500
Investment properties		21,660	21,660
Property, plant and equipment		53,087	53,087
Land lease prepayments		328,499	328,499
Intangible assets		599	599
Deferred tax assets		13,020	–
Other assets		353,575	353,575
		16,536,377	16,601,814
Less			
Liabilities:			
Deposits and balances of banks and other financial institutions		771,262	771,262
Customer deposits		12,040,469	12,040,469
Certificates of deposits issued		1,423,691	1,423,691
Deferred tax liabilities		43,676	43,676
Other liabilities		438,334	434,334
		14,717,432	14,713,432
		1,818,945	1,888,382
Goodwill on acquisition	25	2,774,403	
Satisfied by cash		4,593,348	

Notes to Financial Statements

44. ACQUISITION OF A SUBSIDIARY (Continued)

Included in the balances of cash and short term placements, placements with banks and financial institutions maturing between one and twelve months and held-to-maturity securities were HK\$2,484,479,000, HK\$180,763,000 and HK\$376,126,000 with original maturity within three months, respectively.

Included in other liabilities were tax payables of HK\$6,502,000.

An analysis of the net outflow of cash and cash equivalents in respect of the acquisition of a subsidiary is as follows:

	Note	HK\$'000
Cash paid, including legal and professional fees	25	(4,593,348)
Cash and cash equivalents acquired		3,041,368
Net outflow of cash and cash equivalents in respect of the acquisition of subsidiaries		(1,551,980)

Since acquisition, Public Bank (Hong Kong) contributed HK\$227,953,000 to the Group's revenue and HK\$105,873,000 to the net profit for the year ended 31 December 2006.

Had the combination taken place at the beginning of the year, the revenue from continuing operations and the net profit from Public Bank (Hong Kong) to the Group for the year would have been HK\$341,984,000 and HK\$145,500,000 respectively.

45. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 10 January 2007.

Supplementary Information (Unaudited)

Advances to customers by industry sectors

	Group	
	Gross advances to customers	
	2006	2005
	HK\$'000	HK\$'000
Loans for use in Hong Kong		
Industrial, commercial and financial:		
Property development	291,630	–
Property investment	1,770,464	56,674
Financial concerns	74,066	–
Stockbrokers	66,018	–
Telecommunication	51,578	–
Wholesale and retail trade	16,355	–
Manufacturing	484,588	1,602
Transport and transport equipment	2,139,575	516,024
Others	1,190,590	–
Individuals:		
Loans for the purchase of flats in the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	257,769	–
Loans for the purchase of other residential properties	2,676,947	19,927
Credit card advances	12,467	–
Others	3,255,512	2,911,121
Trade finance	727,657	–
Loans for use outside Hong Kong	661,381	78,452
	13,676,597	3,583,800

The advances to customers are classified by industry sectors based on the industry in which the loans granted were used. In those cases where loans cannot be classified with reasonable certainty, they are classified according to the known principal activity of the borrowers or by reference to the assets financed according to the loan documentation.

Supplementary Information (Unaudited)

Cross-border claims

The following table illustrates the geographical disclosure of the Group's cross-border claims by type of counterparties on which the ultimate risk lies, and is shown according to the location of the counterparties after taking into account the transfer of risk. An individual country or geographical area is reported if it constitutes 10% or more of the aggregate cross-border claims.

	Banks and other financial institutions	Public sector entities	Others	Total
	HK\$'million	HK\$'million	HK\$'million	HK\$'million
As at 31 December 2006 (2005: Nil)				
1. Asia Pacific excluding Hong Kong	2,087	7	154	2,248
of which:				
Australia	899	–	23	922
2. Western Europe	2,953	–	308	3,261

Currency risk

Foreign currency exposures with a net position (regardless of sign) which constitutes 10% or more of the total net position in all foreign currencies of the Group are as follow:

	US Dollars	Others	Total
	In HK\$'million	In HK\$'million	In HK\$'million
As at 31 December 2006 (2005: Nil)			
Spot assets	3,762	1,332	5,094
Spot liabilities	(4,320)	(1,819)	(6,139)
Forward purchases	2,944	902	3,846
Forward sales	(2,319)	(205)	(2,524)
Net long position	67	210	277
		Renminbi	
		In HK\$'million	
Net structural long position			199

Supplementary Information (Unaudited)

Capital adequacy and liquidity ratios

	2006	2005
Capital adequacy ratio as at 31 December:		
Public Bank (Hong Kong)		
Unadjusted ratio	17.54%	–
Adjusted ratio	17.17%	–
Public Finance		
Unadjusted ratio:		
Before final dividend	38.79%	38.52%
After final dividend	34.44%	34.06%
Average liquidity ratio for the year:		
Public Bank (Hong Kong)	51.96%	–
Public Finance	64.95%	72.45%

The above unadjusted and adjusted capital adequacy ratio and average liquidity ratio for the year are computed in accordance with the Third Schedule and the Fourth Schedule of the Banking Ordinance respectively.

The unadjusted capital adequacy ratio of Public Bank (Hong Kong) is computed on a consolidated basis (including Public Investments Limited, Public Credit Limited and Public Bank (Nominees) Limited). The adjusted capital adequacy ratio which takes into account market risk is computed in accordance with the guidelines on “Maintenance of Adequate Capital Against Market Risks” under the Supervisory Policy Manuals issued by the HKMA and the subsidiaries included in the consolidated basis are the same as those included in the unadjusted capital adequacy ratio.

The unadjusted capital adequacy ratio of Public Finance is computed on a consolidated basis (including Public Securities Limited and Public Financial Limited). The adjusted capital adequacy ratio is not disclosed herein as the market risk arising from Public Finance’s trading book is regarded as immaterial. Public Finance meets all of the de minimis exemption criteria for reporting market risk as set out in “Maintenance of Adequate Capital Against Market Risks” under the Supervisory Policy Manuals issued by the HKMA and has relied on such criteria in considering the materiality of market risk arising from its trading book.