



Hong Kong Exchanges and Clearing Limited  
香港交易及結算所有限公司

# Quarterly Report 2005

For the nine months ended 30 September

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# CORPORATE INFORMATION

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## BOARD OF DIRECTORS

### Independent Non-executive Chairman

LEE Yeh Kwong, Charles\* GBS, JP

### Independent Non-executive Directors

CHEUNG Kin Tung, Marvin\* SBS, OBE, JP  
*(appointment effective 12 April 2005)*

FAN Hung Ling, Henry\* SBS, JP  
*(re-appointment effective 12 April 2005)*

FONG Hup\*  
*(re-appointment effective 12 April 2005)*

FRESHWATER, Timothy George\*

KWOK Chi Piu, Bill  
*(re-elected on 12 April 2005)*

LEE Jor Hung, Dannis BBS

### Executive Director, Chief Executive

CHOW Man Yiu, Paul SBS, JP

LEE Kwan Ho, Vincent Marshall  
*(re-elected on 12 April 2005)*

LEONG Ka Chai\* SBS, JP  
*(retired on 12 April 2005)*

LO Ka Shui\* GBS, JP

STRICKLAND, John Estmond GBS, JP

WEBB, David Michael

WONG Sai Hung, Oscar

\* Government Appointed Directors

## COMMITTEES

### Audit Committee

STRICKLAND, John Estmond *(Chairman)*

FONG Hup *(Deputy Chairman)*

CHEUNG Kin Tung, Marvin  
*(appointment effective 13 April 2005)*

FAN Hung Ling, Henry

LEE Kwan Ho, Vincent Marshall

WEBB, David Michael  
*(resigned on 13 April 2005)*

### Executive Committee

LEE Yeh Kwong, Charles *(Chairman)*

CHOW Man Yiu, Paul

CONROY, Patrick Kevin

KWOK Chi Piu, Bill  
*(appointment effective 13 April 2005)*

LEE Jor Hung, Dannis

LEONG Ka Chai  
*(retired on 12 April 2005)*

### Investment Advisory Committee

FRESHWATER, Timothy George *(Chairman)*

WONG Sai Hung, Oscar *(Deputy Chairman)*

SUN, David

WEBB, David Michael

### Nomination Committee

LEE Yeh Kwong, Charles *(Chairman)*

FONG Hup  
*(appointment effective 20 April 2005)*

KWOK Chi Piu, Bill  
*(retired on 12 April 2005)*

LEE Kwan Ho, Vincent Marshall  
*(appointment effective 13 April 2005)*

WEBB, David Michael  
*(appointment effective 20 April 2005)*

WONG Sai Hung, Oscar

**Remuneration Committee**

LO Ka Shui (*Chairman*)

CHEUNG Kin Tung, Marvin  
(*appointment effective 13 April 2005*)

LEE Jor Hung, Dannis

LEE Kwan Ho, Vincent Marshall  
(*retired on 12 April 2005*)

**Risk Management Committee**

(*established under Section 65 of the Securities and Futures Ordinance*)

LEE Yeh Kwong, Charles (*Chairman*)

CHAN Ka-lok\*\*  
(*appointment effective 1 July 2005*)

DICKENS, Mark\*\*  
(*retired on 31 March 2005*)

FAN Hung Ling, Henry  
(*re-appointment effective 13 April 2005*)

FONG Hup\*\*  
(*appointment effective 1 July 2005*)

KWOK Chi Piu, Bill  
(*re-appointment effective 13 April 2005*)

LAM Kin\*\*  
(*retired on 30 June 2005*)

LEONG Ka Chai\*\*  
(*retired on 30 June 2005*)

OR Ching Fai, Raymond\*\*  
(*retired on 31 March 2005*)

WHEATLEY, Martin\*\*  
(*appointment effective 1 July 2005*)

WONG Tung-shun, Peter\*\*  
(*appointment effective 1 April 2005*)

YUE Wai Man, Eddie\*\*  
(*re-appointment effective 1 July 2005*)

\*\* *Appointed by the Financial Secretary*

**COMPANY SECRETARY**

MAU Kam Shing, Joseph

**AUTHORISED REPRESENTATIVES**

CHOW Man Yiu, Paul

MAU Kam Shing, Joseph

**AUDITORS**

PricewaterhouseCoopers

**LEGAL ADVISERS**

Allen & Overy

# FINANCIAL HIGHLIGHTS

(Financial figures are expressed in Hong Kong Dollar)

	Nine months ended 30 Sept 2005	Nine months ended 30 Sept 2004	Change
<b>KEY MARKET STATISTICS</b>			
Average daily turnover value on the Stock Exchange	<b>\$18.2 billion</b>	\$15.3 billion	19%
Average daily number of derivatives contracts traded on the Futures Exchange	<b>66,393</b>	57,078	16%
Average daily number of stock options contracts traded on the Stock Exchange	<b>33,732</b>	22,569	49%

	Unaudited Nine months ended 30 Sept 2005 \$'000	As restated Unaudited Nine months ended 30 Sept 2004 \$'000	
<b>RESULTS</b>			
Income	<b>1,971,300</b>	1,734,545	14%
Operating expenses	<b>852,912</b>	857,037	(0%)
Operating profit	<b>1,118,388</b>	877,508	27%
Share of profits less losses of associates	<b>12,992</b>	8,968	45%
Profit before taxation	<b>1,131,380</b>	886,476	28%
Taxation	<b>(171,464)</b>	(140,441)	22%
Profit attributable to shareholders	<b>959,916</b>	746,035	29%
Earnings per share	<b>\$0.91</b>	\$0.71	28%

	Unaudited at 30 Sept 2005 \$'000	Audited at 31 Dec 2004 \$'000	
<b>KEY BALANCE SHEET ITEMS</b>			
Shareholders' funds	<b>3,982,217</b>	4,052,143	(2%)
Total assets *	<b>26,433,123</b>	21,443,404	23%
Net assets per share #	<b>\$3.75</b>	\$3.83	(2%)

\* The Group's total assets include the Margin Funds received from Participants on futures and options contracts.

# Based on 1,062,396,846 shares issued and fully paid as at 30 September 2005 (31 December 2004: 1,056,638,846 shares)

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# MANAGEMENT DISCUSSION AND ANALYSIS

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(Financial figures are expressed in Hong Kong Dollar)

## BUSINESS REVIEW

### LISTING

#### Consultations on Enhancing Listing Regulation

As the exchange controller, Hong Kong Exchanges and Clearing Limited (“HKEx”) is committed to operating quality markets with high regulatory standards. To determine the most effective level of regulation for protecting interests of the investing public, HKEx is working closely with the Financial Services and the Treasury Bureau (“FSTB”) and the Securities and Futures Commission (“SFC”) on further developing the Government’s proposals for giving statutory backing to major listing requirements to achieve the objective of giving “teeth” to major listing requirements but without causing much disruption to the market.

#### Proposed New Structure for Listing Decision-Making

HKEx is finalising the Consultation Conclusions on the Proposed New Structure for Listing Decision-Making (“Conclusions”) and the proposed amendments to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited and the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (collectively the “Listing Rules”) for implementing the Conclusions with the SFC, HKEx Board and Listing Committees. The Conclusions and the recommended amendments to the Listing Rules will be published in late 2005 or early 2006. HKEx believes that the implementation of the new structure could further bolster investors’ confidence in the markets as being fair, efficient and transparent.

#### Revision of the Mechanisms for Disseminating Regulatory Information by Main Board Issuers

As the market evolves, HKEx has continually revisited the principles and rules underlying a disclosure-based regime to ensure their effectiveness in meeting changing market needs. In this regard, the Listing Committee has approved a proposal to require Main Board issuers to publish a notification announcement in newspapers instead of the full version of the announcement and the latter will be required to be posted only on the HKEx website and the issuer’s website or released through other electronic communication channels. HKEx will publish a policy statement in November 2005 inviting the market to comment on certain aspects of the proposed transitional arrangements, including the form and content of the proposed notification announcement. The requirement of publishing notification announcements will be implemented subject to HKEx’s system and operational readiness and the SFC’s approval of the relevant rule amendments.

#### Review of the Growth Enterprise Market (“GEM”)

HKEx has established an internal working group to co-ordinate studies and develop proposals for the comprehensive review of the GEM which has been in operation for six years. The working group has held a number of informal meetings with various stakeholders, including shareholders, issuers, investors, market practitioners and participants, the SFC and the Government, to solicit views on the GEM and possible solutions and operation models. Individual Board members and members of the GEM Listing Committee have also contributed their views. A consultation paper setting out the diversity of views expressed and the recommendations will be published in late 2005 or early 2006.

## CASH MARKET

### Market Performance

In the first three quarters of 2005, there were a total of 33 (corresponding period in 2004: 52) newly listed companies on The Stock Exchange of Hong Kong Limited (“Stock Exchange”), of which 28 (corresponding period in 2004: 32) were listed on the Main Board and five (corresponding period in 2004: 20) on the GEM. The total capital raised, including post-listing funds, reached \$189.5 billion (corresponding period in 2004: \$226.7 billion).

As at 30 September 2005, there were 907 (as at 30 September 2004: 877) companies listed on the Main Board, including China Shenhua Energy Co Ltd and Bank of Communications Co Ltd, the two largest initial public offerings (“IPOs”) during the first nine months of 2005, and 202 (as at 30 September 2004: 203) companies listed on the GEM. The market capitalisation of the Main Board and the GEM was \$7,544 billion (as at September 2004: \$5,898 billion) and \$72 billion (as at September 2004: \$62 billion) respectively. The average daily turnover in the first three quarters of 2005 was \$18.1 billion (corresponding period in 2004: \$15.2 billion) on the Main Board and \$91.5 million (corresponding period in 2004: \$114.1 million) on the GEM.

In addition, there were 1,192 derivative warrants, eight Exchange Traded Funds (“ETFs”) (excluding two ETFs for trading only) and 165 debt securities listed on the Stock Exchange as at the end of September 2005.

Strong growth was registered in the ETF segment during the reporting period with an average daily turnover of \$129 million recorded in the third quarter of 2005 (in the third quarter of 2004: \$67 million). On 7 July 2005, the ABF Pan Asia Bond Index Fund was first listed, which tracks the performance of the iBoxx Pan-Asia Bond Index, and is traded and settled on the Stock Exchange in US Dollar.

### Renovation of the Trading Hall

The renovation of the Trading Hall has commenced and is progressing smoothly. It is expected that new trading facilities will be ready for use in January 2006. The construction and installation of other ancillary facilities will begin thereafter and are scheduled to complete by the end of April 2006.

### Review of the Derivative Warrant Market

Responding to the increasing interest in its derivative warrant market in the past few months, HKEx on 10 October 2005 published an article on derivative warrants, which included, inter alia, the related rules and a summary of the issues relating to the recent development, to invite public comments with an aim at enhancing transparency and public awareness of the derivative warrant market.

HKEx is committed to promoting investor education and will continue to allocate resources to help further increase investors’ understanding of the products traded on its markets.

### Other Product and Market Development Initiatives

The Phase 1 reduction of minimum trading spreads for shares priced above \$30 was successfully launched on 4 July 2005. Market data was collected and is being analysed to study the impact and experience.

HKEx is in the final stage discussion with the SFC on the regulatory approval for the introduction of Callable Bull/Bear Contracts (“CBBCs”), and the launch of the product will be subject to the readiness of the market infrastructure. Investor education and product promotion will be conducted prior to the launch of CBBCs.

The proposal to exempt placing or fund raising activities by Exchange Participants (“EPs”) from the current prohibition of dealings in suspended securities under the Rules of the Exchange was implemented on 8 September 2005.

## DERIVATIVES MARKET

### Market Performance

During the third quarter of 2005, the products that achieved record high are highlighted as follows:

Products	Record High Daily Volume		Record High Open Interest	
	Date	Number of Contracts	Date	Number of Contracts
Hang Seng Index Options	–	–	28 Sept	298,505
Mini-Hang Seng Index Futures	–	–	25 Jul	5,636
FTSE/Xinhua China 25 Index Options	–	–	29 Aug	1,607
H-shares Index Options	22 Jul	4,280	29 Aug	65,249
Stock Options	–	–	28 Sept	1,655,274

### Product and Market Development

Responding to market demand, HKEx further introduced futures and options contracts on Bank of Communications Co Ltd, China Netcom Group Corporation (Hong Kong) Ltd and Ping An Insurance (Group) Co of China Ltd on 7 November 2005. This brings to a total of 8 option classes on H-shares and 12 option classes on Red Chips for trading on the Stock Exchange. To further facilitate the trading of stock options, HKEx has obtained the SFC’s approval on the proposal to revise the position limit and reporting level for stock options. The implementation of the new levels will be subject to the relevant changes in sub-legislation.

The number of OMnet Application Programming Interface connections increased 23 per cent from 258 as at the end of 2004 to 318 as at 30 September 2005, representing greater system flexibility for the market as a whole in establishing trading connections to the Hong Kong Futures Automated Trading System (“HKATS”). Upon completion of the Phase I rollout of the consolidation of the existing market networks into the new Optical Ethernet network (“SDNet”) on 31 October 2005, the line rentals of HKATS, Derivatives Clearing and Settlement System (“DCASS”) and Price Reporting System (“PRS”) for Participants have been reduced by about 20 per cent.



### **Education and Marketing**

Continuous professional training courses and briefings for EPs and market professionals have also been organised to update them on HKEx's products, services and requirements. In August, HKEx participated in the FIA Asia Derivatives Conference in Beijing to introduce its market infrastructure and products to overseas market professionals.

## **CLEARING**

### **Scripless Market**

Hong Kong Securities Clearing Company Limited ("HKSCC") has finalised the operational arrangements and system changes required for the implementation of the initial phase of scripless market, i.e. dematerialisation of physical scrip in the Central Clearing and Settlement System ("CCASS") Depository. Meanwhile, the SFC and the FSTB are still in the process of finalising the relevant legislative changes for the implementation of the scripless market in Hong Kong. Subject to the enactment of the enabling legislation, initial phase of the scripless market might start in late 2006.

### **Clearing Services Enhancements**

To better serve the specific interests of CCASS Participants, HKSCC has extended the CCASS deadline for its Participants to submit their corporate action instructions to a time much closer to the issuer's deadline with effect from 8 August. Furthermore, CCASS Participants are able to make payments, including intra-day marks, through the Real Time Gross Settlement payment mechanism operated by the Hong Kong Interbank Clearing Limited and hence, exempted from the existing fee of \$100 per settlement transaction. Further improvements to the CCASS nominee services are planned for implementation in early 2006.

### **Risk Management Policies Harmonisation**

Harmonisation of the three clearing houses' collateral policies took effect on 22 August 2005. Further policy changes to broaden the eligible collateral types for the two derivatives clearing houses are also under consideration.

In addition, the review of the capital requirements of each category of Clearing Participants has been completed. Relevant rule amendments to simplify the structure of participation and harmonise the capital requirements for Clearing Participants of the two derivatives clearing houses will be implemented by the end of this year.

## **BUSINESS DEVELOPMENT**

In the past years, HKEx has been pro-actively promoting Hong Kong as a preferred listing venue for the Mainland prospective issuers. Following the completion of the organisational restructuring in August, the Business Development Division remains focused on attracting quality Mainland enterprises to list in Hong Kong.

### **Attracting Prospective Issuers**

In July, a large scale listing promotion event was held in collaboration with the Pan Pearl River Delta Region's governments and the Shanghai and Shenzhen stock exchanges. During the event, a one-day conference was held in Chengdu with the participation of more than 300 enterprise representatives and government officials from various provinces. In September, another well-received listing forum was held in Fuzhou during the financial services delegation visit to Fujian led by the FSTB.

HKEx has expanded its marketing effort beyond the Mainland to attract quality potential issuers from different sectors in other regional markets such as Japan and Taiwan. In July, our Chief Executive addressed two conferences organised for the Japanese business enterprises in Tokyo and Osaka. In August, a presentation was made to the Taiwanese prospective issuers in Shanghai. All these concerted efforts raised the interest of potential issuers to list on the Stock Exchange.

### **Training Programmes for Issuers**

To ensure a quality market, HKEx is committed to educating the issuers about their continuing listing obligations. Corporate governance seminars were organised for issuers to help them better understand the relevant rules and regulations. In July, HKEx co-organised a one-week training programme for the senior management of the Mainland issuers with the Hong Kong Polytechnic University and the State Council's Office of Hong Kong & Macao Affairs. HKEx also participated in a Corporate Governance seminar organised by an accountancy firm for the senior officials of the State-owned Assets Supervision and Administration Commission and senior management of state-owned enterprises in August. Going forward, HKEx will continue to promote good corporate governance practices amongst the companies already listed or to be listed on the Stock Exchange to ensure that their governance practices are in line with international standards.

## **INFORMATION SERVICES**

In recognition of the need to provide real-time and historical market data of the Cash and Derivatives Markets to market practitioners and investors for enhancing market transparency, HKEx has introduced a new service for the redistribution of historical data products and successfully entered into the first Historical Data Product Vendor Agreement in September. To further enhance our information services, the throttle rate of the real-time derivatives information feed will be increased in late 2005 or early 2006 after successful completion of system upgrade and market rehearsals.

A seminar was held in August to update the derivatives vendors on the data volume projection, system and line upgrade plan as well as the approach for the migration of the HKATS, DCASS and PRS circuits to the SDNet (Phase I rollout). Separately, to safeguard the interests of both HKEx and its vendors and ensure healthy development of the information business on Hong Kong market data, HKEx has continued taking prompt action against unauthorised dissemination of its market data.

## **INFORMATION TECHNOLOGY**

### **Production Systems Stability and Reliability**

HKEx is committed to upholding a high standard of system stability and reliability through the continuing improvement of market infrastructure to achieve delivery excellence. Up to the end of September 2005, all major trading, clearing and settlement, and market data dissemination systems for the Cash and Derivatives Markets have maintained 100 per cent operational system uptime for the prior 30 months.

On 19 October 2005, the Hong Kong Computer Society conferred the Gold Award (the highest) of the Application Category of 7th IT Excellence Awards to HKEx in respect of its CCASS/3. The assessment criteria included functionality and design, productivity, competitiveness, cost performance, social impact and innovative use of information technology.

### **Capacity Planning and Upgrade**

During the third quarter of 2005, HKEx has upgraded the capacity of and substantially enhanced the disaster recovery arrangement for the HKEx website ([www.hkex.com.hk](http://www.hkex.com.hk)) to ensure that it can maintain the highest performance and availability during potential disastrous situation.

Moreover, the capacity upgrade exercise in respect of the Automatic Order Matching and Execution System/Third Generation ("AMS/3"), HKATS, DCASS and PRS is in progress and will be completed by the end of this year.

### **Obsolescent Technology Replacement and System Migration**

The replacement of the AMS/3 off-floor terminals with an upgraded AMS/3 security solution has been commenced and is expected to be completed by the end of this year. In line with the refurbishment of the Trading Hall, additional off-floor terminals will also be installed in the latter part of the year upon completion of the relinquishment of the existing AMS/3 on-floor terminals. The migration of the existing AMS/3 Order Routing System to HP/Nonstop platform to reduce technology complexity and achieve operational cost savings is in progress and is planned to be completed by the end of 2005.

### **System Consolidation and Operational Efficiency**

The consolidation of the existing four market system networks into the SDNet, which has been started early this year, proceeded smoothly as scheduled. The phased migration of Participants' circuits of HKATS, DCASS and PRS onto the SDNet (Phase I rollout) has been carried out in four batches in October. After the migration, Participants will be able to enjoy reduced line rentals and significant technological improvements, including higher participant line bandwidth, better network reliability, greater operational efficiency and advanced network management.

The consolidation of the AMS/3 satellite system has been largely completed. The redevelopment of derivatives market surveillance and risk management systems to further improve operational efficiency and effectiveness is on schedule.

## TREASURY

HKEx's investment funds comprise Corporate Funds, Margin Funds and Clearing House Funds, totalling \$16.8 billion on average for the nine months ended 30 September 2005 (30 September 2004 average: \$13.9 billion).

As compared with 30 June 2005, the overall fund size as at 30 September 2005 increased by 24 per cent or \$3.9 billion to \$20.4 billion (30 June 2005: \$16.5 billion). Details of the asset allocation of the investments as at 30 September 2005 against those as at 30 June 2005 are set out below.

	Fund size \$ billion		Bonds		Cash or Bank deposits		Global equities	
	Sept	Jun	Sept	Jun	Sept	Jun	Sept	Jun
Corporate Funds	<b>4.0</b>	3.9	<b>59%</b>	60%	<b>33%</b>	34%	<b>8%</b>	6%
Margin Funds	<b>14.6</b>	11.2	<b>31%</b>	36%	<b>69%</b>	64%	<b>0%</b>	0%
Clearing House Funds	<b>1.8</b>	1.4	<b>13%</b>	17%	<b>87%</b>	83%	<b>0%</b>	0%
<b>Total</b>	<b>20.4</b>	16.5	<b>35%</b>	40%	<b>63%</b>	58%	<b>2%</b>	2%

Investments are kept sufficiently liquid to meet HKEx's operating needs and possible liquidity requirements of the Clearing House Funds and Margin Funds. Excluding equities held under the Corporate Funds (\$0.3 billion as at 30 September 2005 and 30 June 2005), which have no maturity date, the maturity profiles of the remaining investments as at 30 September 2005 (\$20.1 billion) and 30 June 2005 (\$16.2 billion) were as follows:

	Fund size \$ billion		Overnight		>Overnight to 1 month		>1 month to 1 year		>1 year to 3 years		> 3 years	
	Sept	Jun	Sept	Jun	Sept	Jun	Sept	Jun	Sept	Jun	Sept	Jun
Corporate Funds	<b>3.7</b>	3.6	<b>13%</b>	18%	<b>19%</b>	12%	<b>24%</b>	25%	<b>28%</b>	29%	<b>16%</b>	16%
Margin Funds	<b>14.6</b>	11.2	<b>45%</b>	38%	<b>26%</b>	26%	<b>20%</b>	23%	<b>9%</b>	13%	<b>0%</b>	0%
Clearing House Funds	<b>1.8</b>	1.4	<b>83%</b>	78%	<b>3%</b>	4%	<b>9%</b>	11%	<b>5%</b>	7%	<b>0%</b>	0%
<b>Total</b>	<b>20.1</b>	16.2	<b>43%</b>	36%	<b>22%</b>	21%	<b>20%</b>	23%	<b>12%</b>	16%	<b>3%</b>	4%

Credit exposure is well diversified. As at 30 September 2005, the bond portfolio held was of investment grade and had a weighted average credit rating of Aa2 (30 June 2005: Aa2) and a weighted average maturity of 1.2 years (30 June 2005: 1.5 years). Deposits are placed only with the note-issuing banks in Hong Kong, investment grade licensed banks and restricted licence banks approved by the Board from time to time.

Risk management techniques, such as Value-at-Risk (“VaR”) and portfolio stress testing, are used to identify, measure, monitor and control market risks. VaR measures the expected maximum loss over a given time interval (a holding period of 10 trading days is used by HKEx) at a given confidence level (95 per cent confidence interval is adopted by HKEx) based on historical data (one year is used by HKEx). The overall risk, as measured by the VaR methodology, during the third quarter and second quarter of 2005 was as follows:

	Average VaR \$ million		Maximum VaR \$ million		Minimum VaR \$ million	
	Jul-Sept	Apr-Jun	Jul-Sept	Apr-Jun	Jul-Sept	Apr-Jun
Corporate Funds	<b>12.7</b>	12.1	<b>13.5</b>	14.7	<b>11.2</b>	11.3
Margin Funds	<b>13.5</b>	15.4	<b>14.5</b>	16.2	<b>12.0</b>	14.3
Clearing House Funds	<b>1.0</b>	1.4	<b>1.2</b>	1.5	<b>0.9</b>	1.2

For details of HKEx’s investment income, please refer to the Income section under the Financial Review and note 6 to the condensed consolidated accounts of this quarterly report.

## INVESTMENTS IN ASSOCIATES

### Computershare Hong Kong Investor Services Limited (“CHIS”)

In May 2005, the Group acquired a further six per cent interest in CHIS for \$25 million and raised its interest to 30 per cent. As at 30 September 2005, the cost of the investment in CHIS was \$52 million and the book value of the investment was \$58 million.

### ADP Wilco Processing Services Limited (“AWPS”)

The Group acquired a 30 per cent interest in AWPS in May 2002 (cost: \$1.8 million; and book value: \$1.3 million). AWPS is in the process of a voluntary dissolution. The liquidation proceeds of AWPS are expected to approximate its book value.

## FINANCIAL REVIEW

### OVERALL PERFORMANCE

	<b>Unaudited Nine months ended 30 Sept 2005 \$'000</b>	As restated Unaudited Nine months ended 30 Sept 2004 \$'000
<b>RESULTS</b>		
Income:		
Income directly affected by market turnover	1,054,499	934,935
Stock Exchange listing fees	303,561	271,314
Income from sale of information	243,860	230,250
Investment income	224,999	163,896
Other income	144,381	134,150
	<b>1,971,300</b>	1,734,545
Operating expenses	<b>852,912</b>	857,037
Operating profit	<b>1,118,388</b>	877,508
Share of profits less losses of associates	<b>12,992</b>	8,968
Profit before taxation	<b>1,131,380</b>	886,476
Taxation	<b>(171,464)</b>	(140,441)
Profit attributable to shareholders	<b>959,916</b>	746,035
Earnings per share	<b>\$0.91</b>	\$0.71
	<b>Unaudited at 30 Sept 2005 \$'000</b>	Audited at 31 Dec 2004 \$'000
<b>KEY BALANCE SHEET ITEMS</b>		
Shareholders' funds	<b>3,982,217</b>	4,052,143
Total assets*	<b>26,433,123</b>	21,443,404
Net assets per share <sup>#</sup>	<b>\$3.75</b>	\$3.83

\* The Group's total assets include the Margin Funds received from Participants on futures and options contracts.

<sup>#</sup> Based on 1,062,396,846 shares issued and fully paid as at 30 September 2005 (31 December 2004: 1,056,638,846 shares)

The Group recorded a profit attributable to shareholders of \$960 million for the first nine months of 2005 (first quarter: \$245 million, second quarter: \$326 million, third quarter: \$389 million), compared with \$746 million, as restated, for the same period in 2004 (first quarter: \$313 million, second quarter: \$185 million, third quarter: \$248 million).

As compared with that for the same period last year, the increase in profit for the nine months ended 30 September 2005 was primarily attributable to the higher turnover-related income resulting from the increase in level of activities in the Cash and Derivatives Markets, rise in Stock Exchange listing fees due to the higher number of listed securities and newly listed derivative warrants during the period, and higher investment income from increased fund size and rising interest rates in 2005.

Despite an increase in staff costs, the Group has managed to keep its total operating expenses for the nine-month period at a level similar to that of the same period last year.

## Income

### (A) Income directly affected by market turnover

	Unaudited Nine months ended 30 Sept 2005 \$'000	Unaudited Nine months ended 30 Sept 2004 \$'000	Change
Trading fees and trading tariff	<b>580,453</b>	494,610	17%
Clearing and settlement fees	<b>282,242</b>	258,438	9%
Depository, custody and nominee services fees	<b>191,804</b>	181,887	5%
<b>Total</b>	<b>1,054,499</b>	934,935	13%

The increase in trading fees and trading tariff was mainly due to the higher market turnover of the Cash and Derivatives Markets in the first nine months of 2005 against that of the corresponding period last year.

Clearing and settlement fees are derived predominantly from Cash Market transactions. Despite being mostly ad valorem fees, clearing and settlement fees are subject to a minimum and a maximum fee per transaction. Clearing and settlement fees did not increase linearly with the Cash Market turnover in 2005 as there was a higher proportion of transactions with value subject to the maximum fee and a lower proportion of transactions with value subject to the minimum fee.

Depository, custody and nominee services fees increased due to the higher scrip fee income, corporate action fees and dividend collection fees but partly offset by lower stock withdrawal fees in 2005.

### Key market indicators

	Nine months ended 30 Sept 2005	Nine months ended 30 Sept 2004	Change
Average daily turnover value on the Stock Exchange	<b>\$18.2 billion</b>	\$15.3 billion	19%
Average daily number of derivatives contracts traded on the Futures Exchange	<b>66,393</b>	57,078	16%
Average daily number of stock options contracts traded on the Stock Exchange	<b>33,732</b>	22,569	49%

**(B) Stock Exchange listing fees**

	Unaudited Nine months ended 30 Sept 2005 \$'000	Unaudited Nine months ended 30 Sept 2004 \$'000	Change
Annual listing fees	197,613	187,283	6%
Initial and subsequent issue listing fees	100,881	79,599	27%
Others	5,067	4,432	14%
<b>Total</b>	<b>303,561</b>	<b>271,314</b>	<b>12%</b>

The increase in annual listing fees was attributable to the higher number of listed securities. Although the number of newly listed companies dropped as compared with that for the same period in 2004, the decrease in initial listing fees from newly listed companies was more than offset by the higher income from newly listed derivative warrants and the initial listing fees forfeited due to increased numbers of lapsed and withdrawn IPO applications and approved IPOs not listed within six months of application.

**Key drivers for annual listing fees**

	As at 30 Sept 2005	As at 30 Sept 2004	Change
Number of companies listed on the Main Board	907	877	3%
Number of companies listed on the GEM	202	203	(0%)
<b>Total</b>	<b>1,109</b>	<b>1,080</b>	<b>3%</b>

**Key drivers for initial and subsequent issue listing fees**

	Nine months ended 30 Sept 2005	Nine months ended 30 Sept 2004	Change
Number of newly listed derivative warrants	1,238	869	42%
Number of new listings on the Main Board	28	32	(13%)
Number of new listings on the GEM	5	20	(75%)
Total equity funds raised on the Main Board	\$187.3 billion	\$221.7 billion	(16%)
Total equity funds raised on the GEM	\$2.2 billion	\$5.0 billion	(56%)



**(C) Income from sale of information**

	<b>Unaudited Nine months ended 30 Sept 2005 \$'000</b>	Unaudited Nine months ended 30 Sept 2004 \$'000	Change
Income from sale of information	<b>243,860</b>	230,250	6%

Income from sale of information rose as demand for information increased in tandem with the activities of the Cash and Derivatives Markets.

**(D) Investment income**

	<b>Unaudited Nine months ended 30 Sept 2005 \$'000</b>	As restated Unaudited Nine months ended 30 Sept 2004 \$'000	Change
<b>Income from:</b>			
Funds available for investment	<b>224,999</b>	138,264	63%
Investment in Singapore Exchange Limited	–	25,632	(100%)
<b>Total</b>	<b>224,999</b>	163,896	37%

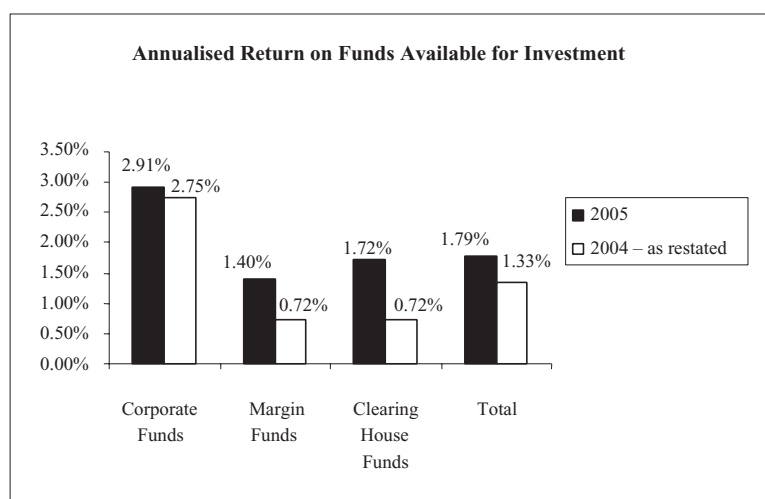
The average amount of funds available for investment was as follows:

	<b>Nine months ended 30 Sept 2005 \$ billion</b>	Nine months ended 30 Sept 2004 \$ billion	Change
Corporate Funds	<b>4.0</b>	4.2	(5%)
Margin Funds	<b>11.3</b>	8.3	36%
Clearing House Funds	<b>1.5</b>	1.4	7%
<b>Total</b>	<b>16.8</b>	13.9	21%

The increase in average amount of Margin Funds available for investment during the period was primarily due to the increased open interest in futures and options contracts. The decrease in Corporate Funds was mainly due to the \$2.2 billion payment of 2003 special and final dividends in April 2004.

The increase in income generated from funds available for investment was primarily due to the higher interest income arising from increases in fund size and interest rates during the first nine months of 2005.

The performance of funds available for investment during the first nine months was as follows:



For details of the investment portfolio, please refer to the Treasury section under the Business Review.

**(E) Other income**

	Unaudited Nine months ended 30 Sept 2005 \$'000	As restated Unaudited Nine months ended 30 Sept 2004 \$'000	Change
Network, terminal user, dataline and software sub-license fees	94,726	86,731	9%
Participants' subscription and application fees	25,837	25,778	0%
Brokerage on direct IPO applications	10,149	11,288	(10%)
Fair value gain of an investment property	3,200	–	N/A
Accommodation income	1,898	4,361	(56%)
Miscellaneous income	8,571	5,992	43%
<b>Total</b>	<b>144,381</b>	<b>134,150</b>	<b>8%</b>

Despite the 20 per cent reduction in AMS/3 user fees that took effect on 1 January 2005, network, terminal user, dataline and software sub-license fees rose due to the increase in sales of additional throttle.

Accommodation income (i.e. retention interest charged on cash margin deposits in non-contract settlement currencies and securities deposited by Participants as alternatives to cash deposits of the Margin Funds) decreased mainly due to less cash margin deposits denominated in non-contract settlement currencies received in the first half of 2005. In addition, from 1 June 2005 onwards, accommodation charges on cash margin deposits were abolished and accommodation fee on utilised non-cash collateral charged by HKFE Clearing Corporation Limited (“HKCC”) and The SEHK Options Clearing House Limited (“SEOCH”) were reduced from 1.2 per cent and 2 per cent respectively to 0.5 per cent.

## Operating Expenses

	Unaudited Nine months ended 30 Sept 2005 \$'000	As restated Unaudited Nine months ended 30 Sept 2004 \$'000	Change
Staff costs and related expenses	424,764	398,630	7%
Information technology and computer maintenance expenses	148,472	166,643	(11%)
Premises expenses	60,175	59,301	1%
Product marketing and promotion expenses	7,681	7,853	(2%)
Legal and professional fees	10,367	7,968	30%
Depreciation	125,548	137,926	(9%)
Payment to SFC under dual filing regime	15,000	15,000	0%
Other operating expenses	60,905	63,716	(4%)
<b>Total</b>	<b>852,912</b>	<b>857,037</b>	<b>(0%)</b>

Staff costs and related expenses increased by \$26 million, primarily due to the increase in salary costs and contribution to provident funds of \$19 million as a result of the increase in headcount and salary adjustment in 2005. Employee share option costs also rose by \$7 million due to the amortisation of the option costs arising from grants of new share options in March 2004, May 2004 and January 2005.

Information technology and computer maintenance expenses of the Group, after excluding goods and services directly consumed by the Participants of \$39 million (2004: \$44 million), were \$109 million (2004: \$123 million). The decrease was mainly due to lower system maintenance costs and reduced network line rental charges. During the period under review, capital expenditures on computer systems, hardware and software amounted to \$36 million (2004: \$16 million).

Depreciation decreased as certain fixed assets became fully depreciated.

Other operating expenses decreased mainly as a result of the reduction in bank charges following the expiry of certain banking facilities that were no longer necessary.

## Share of Profits Less Losses of Associates

	Unaudited Nine months ended 30 Sept 2005 \$'000	As restated Unaudited Nine months ended 30 Sept 2004 \$'000	Change
Share of profits less losses of associates	12,992	8,968	45%

Share of profits less losses of associates increased due to the higher profitability of one of the associates, CHIS, and the acquisition of a further six per cent interest in CHIS in May 2005.

## Taxation

	<b>Unaudited Nine months ended 30 Sept 2005 \$'000</b>	As restated Unaudited Nine months ended 30 Sept 2004 \$'000	Change
Taxation	<b>171,464</b>	140,441	22%

Taxation increased mainly attributable to an increase in operating profit, but partly offset by an increase in non-taxable investment income.

## Comparison of 2005 Third Quarter Performance with 2005 Second Quarter Performance

	<b>Unaudited Three months ended 30 Sept 2005 \$'000</b>	Unaudited Three months ended 30 Jun 2005 \$'000
Income:		
Income directly affected by market turnover:		
Trading fees and trading tariff	<b>227,838</b>	169,935
Clearing and settlement fees	<b>109,815</b>	80,786
Depository, custody and nominee services fees	<b>58,122</b>	100,069
	<b>395,775</b>	350,790
Stock Exchange listing fees	<b>107,989</b>	98,869
Income from sale of information	<b>81,615</b>	83,255
Investment income	<b>102,926</b>	79,193
Other income	<b>44,530</b>	52,106
	<b>732,835</b>	664,213
Operating expenses	<b>282,394</b>	287,843
Operating profit	<b>450,441</b>	376,370
Share of profits less losses of associates	<b>4,357</b>	6,018
Profit before taxation	<b>454,798</b>	382,388
Taxation	<b>(65,678)</b>	(57,013)
Profit attributable to shareholders	<b>389,120</b>	325,375

Profit attributable to shareholders increased by \$64 million mainly due to a \$69 million increase in income while total operating expenses fell by \$5 million during the third quarter.

**Key market indicators**

	Three months ended 30 Sept 2005	Three months ended 30 Jun 2005	Change
Average daily turnover value on the Stock Exchange	<b>\$20.6 billion</b>	\$15.4 billion	34%
Average daily number of derivatives contracts traded on the Futures Exchange	<b>73,382</b>	61,545	19%
Average daily number of stock options contracts traded on the Stock Exchange	<b>49,784</b>	23,907	108%

The increase in the level of activities in the Cash and Derivatives Markets has led to an increase in trading fees of \$58 million and clearing and settlement fees of \$29 million. However, depository, custody and nominee services fees fell by \$42 million as dividend collection and scrip fee income declined due to seasonal factors.

Investment income increased by \$24 million, principally due to a higher interest income attributable to increased fund size and rising interest rates in 2005.

Taxation increased, mainly as a result of the increase in operating profit, but partly offset by an increase in non-taxable investment income.

**Working Capital**

Working capital fell by \$36 million or one per cent to \$3,029 million as at 30 September 2005 (31 December 2004: \$3,065 million). The decline was primarily due to the payment of the 2004 final dividend of \$498 million and the 2005 interim dividend of \$521 million, which was offset by the profit generated during the period of \$960 million, and the increase in other net current assets of \$23 million.

**Exposure to Fluctuations in Exchange Rates and Related Hedges**

Details of the Group's exposure to fluctuations in exchange rates and related hedges are included in note 32(a)(i) – Foreign exchange risk to the condensed consolidated accounts of this quarterly report.

### **Contingent Liabilities**

In May 2005, the Court of Appeal issued its judgement in the New World Development Company Limited and others (“New World”) judicial review appeal case. The Court allowed the appeal and quashed the direction of the Chairman of the Listing (Disciplinary) Committee in the New World disciplinary proceedings that legal advisers not be permitted to address the Listing (Disciplinary) Committee. New World was awarded costs which are estimated to be in the region of \$4 million. The Stock Exchange has been granted leave to appeal to the Court of Final Appeal. A formal submission will be made to the Court of Final Appeal shortly. In the opinion of external legal counsel, the Stock Exchange has valid grounds for an appeal, a reasonable prospect of success and consequently it is not probable that the Stock Exchange will be required to bear the costs incurred by New World in the legal proceedings. Accordingly, no provision for such costs has been made in the accounts.

For details of the other contingent liabilities, please refer to notes 29(a), (b) and (c) to the condensed consolidated accounts of this quarterly report.

### **Changes since 31 December 2004**

There were no other significant changes in the financial position or from the information disclosed under Management Discussion and Analysis in the annual report for the year ended 31 December 2004.

It is the Group’s plan to declare dividend only at the half-year and year-end. Therefore, no dividend will be proposed for the third quarter ended 30 September 2005 (third quarter of 2004: \$Nil).

Due to fluctuations in market conditions and changes in operating environment, certain categories of income and operating expenses may vary from quarter to quarter. Therefore, quarterly results should not be extrapolated to project the Group’s full-year performance.

## PROSPECTS

The Mainland's sustained economic growth and increasing capital needs have resulted in the debut of some of the largest global IPOs by Mainland enterprises in Hong Kong. The total capitalisation of the equity market as at the end of September this year increased by about 28 per cent compared with the same period last year. Trading of Stock Options and Hang Seng Index Options gained even greater appeal and recorded significant rises of about 49 per cent and 44 per cent respectively in terms of volume traded against last year's corresponding period. With the successful listing of China Construction Bank Corporation in October 2005, capital raised through IPOs this year up to the end of October stood at \$137 billion, a historical high.

However, as an international financial centre, Hong Kong is inevitably affected by global economic changes. The potential inflationary pressure resulting from high energy prices and escalating interest rates would impede the pace of global economic growth and might dampen the performance of major international capital markets.

Amid the changing environment, HKEx will continue to implement its three-year Strategic Plan. In line with its commitment to maintain a high quality marketplace, HKEx will focus on improving the robustness of its markets to keep pace with the international standards of quality in regulation, infrastructure and operations. HKEx will also reinforce its pivotal position as the pre-eminent marketplace for capital raising for Mainland and Hong Kong issuers.

## CONDENSED CONSOLIDATED PROFIT AND LOSS ACCOUNT

(Financial figures are expressed in Hong Kong Dollar)

	Note	Unaudited Nine months ended 30 Sept 2005 \$'000	As restated Unaudited Nine months ended 30 Sept 2004 \$'000	Unaudited Three months ended 30 Sept 2005 \$'000	As restated Unaudited Three months ended 30 Sept 2004 \$'000
<b>INCOME</b>	2				
Trading fees and trading tariff	4	580,453	494,610	227,838	147,438
Stock Exchange listing fees	5	303,561	271,314	107,989	88,344
Clearing and settlement fees		282,242	258,438	109,815	72,488
Depository, custody and nominee services fees		191,804	181,887	58,122	56,730
Income from sale of information		243,860	230,250	81,615	71,910
Investment income	6	224,999	163,896	102,926	90,408
Other income	7	144,381	134,150	44,530	43,459
	3	1,971,300	1,734,545	732,835	570,777
<b>OPERATING EXPENSES</b>					
Staff costs and related expenses	8	424,764	398,630	142,002	133,477
Information technology and computer maintenance expenses	9	148,472	166,643	49,409	56,626
Premises expenses		60,175	59,301	20,229	20,056
Product marketing and promotion expenses		7,681	7,853	2,148	2,157
Legal and professional fees		10,367	7,968	3,775	2,484
Depreciation		125,548	137,926	39,868	46,348
Payment to SFC under dual filing regime		15,000	15,000	5,000	5,000
Other operating expenses	10	60,905	63,716	19,963	19,594
	3	852,912	857,037	282,394	285,742
<b>OPERATING PROFIT</b>	3	1,118,388	877,508	450,441	285,035
<b>SHARE OF PROFITS LESS LOSSES OF ASSOCIATES</b>	3/15(c)	12,992	8,968	4,357	2,824
<b>PROFIT BEFORE TAXATION</b>	3	1,131,380	886,476	454,798	287,859
<b>TAXATION</b>	3/11	(171,464)	(140,441)	(65,678)	(39,249)
<b>PROFIT ATTRIBUTABLE TO SHAREHOLDERS</b>	3/26	959,916	746,035	389,120	248,610
<b>Earnings per share</b>	12	\$0.91	\$0.71	\$0.37	\$0.24



# CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

(Financial figures are expressed in Hong Kong Dollar)

	Unaudited						
	Share capital and share premium (note 22)	Employee share-based compensation reserve (note 23)	Revaluation reserves (note 24)	Hedging reserve	Designated reserves (note 25)	Retained earnings (note 26)	Total equity
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
At 1 Jan 2005	1,160,673	17,061	18,829	–	680,996	2,174,584	4,052,143
Change in valuation of leasehold buildings	–	–	(548)	–	–	–	(548)
Change in fair value of available-for-sale financial assets	–	–	(71,924)	–	–	–	(71,924)
Realisation of change in fair value of available-for-sale financial assets on maturity and disposal	–	–	(2,680)	–	–	–	(2,680)
Cash flow hedges:							
– fair value gain	–	–	–	47	–	–	47
– transfer to profit and loss account	–	–	–	(39)	–	–	(39)
Deferred tax arising from change in valuation of leasehold buildings	–	–	96	–	–	–	96
Deferred tax arising from change in fair value of available-for-sale financial assets	–	–	3,170	–	–	–	3,170
Net (loss)/profit recognised directly in equity	–	–	(71,886)	8	–	–	(71,878)
Profit attributable to shareholders	–	–	–	–	–	959,916	959,916
Total recognised (loss)/profit	–	–	(71,886)	8	–	959,916	888,038
2004 final dividend	–	–	–	–	–	(498,217)	(498,217)
2005 interim dividend	–	–	–	–	–	(520,567)	(520,567)
Shares issued under employee share option schemes	43,523	–	–	–	–	–	43,523
Employee share option benefits	–	17,254	–	–	–	–	17,254
Share of reserve of an associate	–	43	–	–	–	–	43
Transfer of reserves	4,065	(4,065)	–	–	5,663	(5,663)	–
At 30 Sept 2005	1,208,261	30,293	(53,057)	8	686,659	2,110,053	3,982,217

**CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (CONT'D)**

	As restated Unaudited					
	Share capital and share premium \$'000	Employee share-based compensation reserve \$'000	Revaluation reserves \$'000	Designated reserves \$'000	Retained earnings \$'000	Total equity \$'000
At 31 Dec 2003, as previously reported	1,103,337	–	46,431	689,657	3,763,838	5,603,263
Effect of changes in accounting policies	–	2,771	(9,932)	–	18,023	10,862
At 31 Dec 2003, as restated	1,103,337	2,771	36,499	689,657	3,781,861	5,614,125
Effect of initial adoption of HKAS 39	–	–	–	–	28	28
At 1 Jan 2004, as restated	1,103,337	2,771	36,499	689,657	3,781,889	5,614,153
Change in valuation of leasehold buildings	–	–	565	–	–	565
Change in fair value of available-for-sale financial assets	–	–	(24,693)	–	–	(24,693)
Realisation of change in fair value of financial assets on maturity and disposal	–	–	(25,190)	–	–	(25,190)
Deferred tax arising from change in valuation of leasehold buildings	–	–	(99)	–	–	(99)
Deferred tax arising from change in fair value of available-for-sale financial assets	–	–	3,462	–	–	3,462
Net loss recognised directly in equity	–	–	(45,955)	–	–	(45,955)
Profit attributable to shareholders	–	–	–	–	746,035	746,035
Total recognised (loss)/profit	–	–	(45,955)	–	746,035	700,080
2003 special and final dividends	–	–	–	–	(2,218,559)	(2,218,559)
2004 interim dividend	–	–	–	–	(454,291)	(454,291)
Shares issued under employee share option schemes	57,019	–	–	–	–	57,019
Employee share option benefits	–	10,096	–	–	–	10,096
Transfer of reserves	–	–	–	(1,264)	1,264	–
At 30 Sept 2004, as restated	1,160,356	12,867	(9,456)	688,393	1,856,338	3,708,498

# CONDENSED CONSOLIDATED BALANCE SHEET

(Financial figures are expressed in Hong Kong Dollar)

	Note	Unaudited at 30 Sept 2005 \$'000	Audited at 31 Dec 2004 \$'000
<b>NON-CURRENT ASSETS</b>			
Fixed assets	13	239,460	324,300
Investment property	14	16,500	13,300
Lease premium for land		94,260	94,670
Investments in associates	15	59,090	38,731
Clearing House Funds	16	1,760,776	1,861,487
Compensation Fund Reserve Account	17	37,963	37,451
Time deposit with maturity over one year		38,849	38,941
Deferred tax assets		3,687	1,227
Other assets		12,987	13,142
		<b>2,263,572</b>	<b>2,423,249</b>
<b>CURRENT ASSETS</b>			
Accounts receivable, prepayments and deposits	18	5,621,805	4,691,846
Lease premium for land		548	548
Taxation recoverable		17	91
Margin Funds on derivatives contracts	19	14,593,240	10,529,692
Financial assets at fair value through profit or loss	20	2,686,185	2,761,593
Time deposits with original maturity over three months		48,603	1,340
Cash and cash equivalents		1,219,153	1,035,045
		<b>24,169,551</b>	<b>19,020,155</b>
<b>CURRENT LIABILITIES</b>			
Margin deposits from Clearing Participants on derivatives contracts	19	14,593,240	10,529,692
Accounts payable, accruals and other liabilities	18	6,121,919	4,902,350
Financial liabilities at fair value through profit or loss	20	2,058	10,749
Participants' admission fees received		4,100	4,850
Deferred revenue		116,046	284,148
Taxation payable		275,134	199,678
Provisions	21	27,895	23,212
		<b>21,140,392</b>	<b>15,954,679</b>
<b>NET CURRENT ASSETS</b>		<b>3,029,159</b>	<b>3,065,476</b>
<b>TOTAL ASSETS LESS CURRENT LIABILITIES</b>		<b>5,292,731</b>	<b>5,488,725</b>

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**CONDENSED CONSOLIDATED BALANCE SHEET (CONT'D)**

	Note	Unaudited at 30 Sept 2005 \$'000	Audited at 31 Dec 2004 \$'000
<b>NON-CURRENT LIABILITIES</b>			
Participants' admission fees received		<b>81,050</b>	82,850
Participants' contributions to Clearing House Funds	16	<b>1,189,683</b>	1,298,752
Deferred tax liabilities		<b>18,658</b>	30,876
Provisions	21	<b>21,123</b>	24,104
		<b>1,310,514</b>	1,436,582
<b>NET ASSETS</b>			
		<b>3,982,217</b>	4,052,143
<b>CAPITAL AND RESERVES</b>			
Share capital	22	<b>1,062,397</b>	1,056,639
Share premium	22	<b>145,864</b>	104,034
Employee share-based compensation reserve	23	<b>30,293</b>	17,061
Revaluation reserves	24	<b>(53,057)</b>	18,829
Hedging reserve		<b>8</b>	–
Designated reserves	25	<b>686,659</b>	680,996
Retained earnings	26	<b>2,110,053</b>	1,677,964
Proposed/declared dividends	26	–	496,620
<b>SHAREHOLDERS' FUNDS</b>			
		<b>3,982,217</b>	4,052,143

## CONDENSED CONSOLIDATED CASH FLOW STATEMENT

(Financial figures are expressed in Hong Kong Dollar)

	Note	Unaudited Nine months ended 30 Sept 2005 \$'000	As restated Unaudited Nine months ended 30 Sept 2004 \$'000
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net cash inflow from operating activities	27(a)	1,189,874	1,452,801
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Payments for purchases of fixed assets		(23,439)	(18,828)
Proceeds from sales of fixed assets		53	156
Proceeds from sales of other assets		–	1,175
Proceeds from sales of available-for-sale financial assets		–	75,773
Payments for acquisition of interest in an associate		(24,876)	–
(Increase)/decrease in time deposits with original maturity more than three months		(47,171)	372,951
Dividends received from an associate		4,800	8,401
Dividends received from available-for-sale financial assets		–	1,070
Interest received from available-for-sale financial assets		62,678	41,310
Interest paid on bank loan		–	(827)
Net cash (outflow)/inflow from investing activities		(27,955)	481,181
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Proceeds from issue of shares under employee share option schemes		43,523	57,019
Admission fees refunded to less receipts from Participants		(2,550)	(1,750)
Repayment of bank loan		–	(50,286)
Dividends paid		(1,018,784)	(2,672,850)
Net cash outflow from financing activities		(977,811)	(2,667,867)
<b>Net increase/(decrease) in cash and cash equivalents</b>		<b>184,108</b>	<b>(733,885)</b>
Cash and cash equivalents at 31 Dec 2004/2003		1,035,045	1,355,390
Effect of initial adoption of HKAS 39		–	25,886
<b>Cash and cash equivalents at 30 Sept 2005/2004</b>		<b>1,219,153</b>	<b>647,391</b>
<b>Analysis of cash and cash equivalents</b>			
Time deposits with original maturity within three months		965,955	560,801
Cash at bank and in hand		253,198	86,590
		<b>1,219,153</b>	<b>647,391</b>

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# NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS (UNAUDITED)

(Financial figures are expressed in Hong Kong Dollar)

## 1. Basis of Preparation and Accounting Policies

These unaudited condensed consolidated accounts are prepared in accordance with Hong Kong Accounting Standard (“HKAS”) 34: Interim Financial Reporting, issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”).

These unaudited condensed consolidated accounts should be read in conjunction with the 2004 annual accounts.

The accounting policies and methods of computation used in the preparation of these accounts are consistent with those used in the annual accounts for the year ended 31 December 2004.

In the third quarter of 2005, the Group designated certain foreign currency bank deposits as the hedging instruments for hedging the foreign exchange risk of:

- the fair value of recognised liabilities (fair value hedges); and
- highly probable forecast transactions (cash flow hedges).

The accounting policies for hedging transactions are as follows:

The Group documents at the inception of the transactions the relationship between the hedging instruments and the hedged items, as well as the risk management objectives and strategies for undertaking various hedge transactions. The Group also documents its assessment, both at the inception of the hedges and on an ongoing basis, of whether the hedging instruments are highly effective in offsetting changes in fair values or cash flows of the hedged items.

### (a) Fair value hedges

Changes in the fair value of hedging instruments that are designated and qualify as fair value hedges are recognised in the profit and loss account, together with any changes in the fair value of the hedged assets or liabilities or firm commitments that are attributable to the hedged risk.

### (b) Cash flow hedges

For hedging instruments that are designated as cash flow hedges, the changes in the fair value relating to the effective portion of the hedges are recognised in equity. The gains or losses relating to the ineffective portion of the hedges are recognised immediately in the profit and loss account.

Amounts accumulated in equity are recycled to the profit and loss account in the periods when the hedged items affect profit or loss. However, when the forecast transactions that are hedged result in the recognition of a non-financial asset or a non-financial liability, the gains and losses previously deferred in equity are transferred from equity and included in the initial measurement of the cost of the non-financial asset or non-financial liability.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss retained in equity at that time remains in equity and is recognised in accordance with the above policy when the forecast transaction occurs. When a forecast transaction is no longer expected to occur, the cumulative gain or loss retained in equity is immediately transferred to the profit and loss account.

**1. Basis of Preparation and Accounting Policies (continued)**

In May 2005, the HKICPA issued an interpretation HK-INT 4 “Leases – Determination of the Length of Lease Term in respect of Hong Kong Land Leases”, which is applicable to the Group’s operation and became effective on 24 May 2005. The adoption of the interpretation has no financial impact to the Group as the Group’s accounting policies already comply with the interpretation.

As disclosed in the 2004 annual accounts, the Group adopted various new Hong Kong Financial Reporting Standards (“HKFRSs”) issued by the HKICPA in the fourth quarter of 2004. The results for the nine months ended 30 September 2004 have been restated in accordance with the new HKFRSs.

The effect of changes in accounting policies on the unaudited condensed consolidated profit and loss account for the nine months ended 30 September 2004 was as follows:

	Effect of adopting						Total \$'000
	HKAS 1 \$'000	HKAS 17 \$'000	HKFRS 2 \$'000	HKFRS 3, HKAS 36 & HKAS 38 \$'000	HKAS 32 & HKAS 39 \$'000	Other reclassification \$'000	
Decrease in investment income	-	-	-	-	(2,035)	(4,361)	(6,396)
Increase in other income	-	-	-	-	-	4,361	4,361
Increase in staff costs and related expenses	-	-	(10,096)	-	-	-	(10,096)
Increase in premises expenses	-	(411)	-	-	-	-	(411)
Decrease in depreciation	-	1,562	-	-	-	-	1,562
Increase in other operating expenses	-	-	-	-	(513)	-	(513)
(Decrease)/increase in share of profits less losses of associates	(1,890)	-	-	1,987	-	-	97
Decrease/(increase) in taxation	1,890	(75)	-	-	(52)	-	1,763
<b>Total increase/(decrease) in profit</b>	<b>-</b>	<b>1,076</b>	<b>(10,096)</b>	<b>1,987</b>	<b>(2,600)</b>	<b>-</b>	<b>(9,633)</b>
Increase/(decrease) in basic earnings per share	-	0.10 cents	(0.96 cents)	0.19 cents	(0.24 cents)	-	(0.91cents)

The effect of changes in accounting policies on equity as at 30 September 2004 was as follows:

	Effect of adopting						Total \$'000
	HKAS 17 \$'000	HKFRS 2 \$'000	HKFRS 3, HKAS 36 & HKAS 38 \$'000	HKAS 32 & HKAS 39 \$'000	HKAS 40 \$'000	HK(SIC)- INT 21 \$'000	
<b>Increase/(decrease) in equity</b>							
Employee share-based compensation reserve	-	12,867	-	-	-	-	12,867
Revaluation reserves	(25,932)	-	-	-	(1,771)	-	(27,703)
Retained earnings	17,763	(12,867)	4,633	(2,572)	1,771	(310)	8,418

**1. Basis of Preparation and Accounting Policies (continued)**

The Group manages a significant portfolio of investments. Securities and derivative financial instruments (i.e. forward foreign exchange contracts) held for trading purposes (such as those of the Corporate Funds), and securities or bank deposits with embedded derivatives of the Margin Funds and the Corporate Funds whose economic characteristics and risks are not closely related to the host investments (“structured securities” or “structured deposits”) are classified as financial assets/liabilities at fair value through profit or loss with changes in fair value recognised in the profit and loss account. Securities not held for trading (such as those held for the Clearing House Funds, Compensation Fund Reserve Account and Margin Funds (other than structured securities or structured deposits)) are classified as available-for-sale financial assets with changes in fair value recognised in the investment revaluation reserve.

**2. Turnover**

Turnover comprises trading fees and trading tariff from securities and options traded on The Stock Exchange of Hong Kong Limited (“Stock Exchange”) and derivatives contracts traded on Hong Kong Futures Exchange Limited (“Futures Exchange”), Stock Exchange listing fees, clearing and settlement fees, depository, custody and nominee services fees, income from sale of information, investment income (including investment income net of interest expenses of Clearing House Funds) and other income, which are **disclosed as Income** in the condensed consolidated profit and loss account.

**3. Segment Information**

The Group’s income is derived solely from business activities in Hong Kong. An analysis of the Group’s income and results for the period by business segments is as follows:

	Nine months ended 30 Sept 2005				
	Cash Market \$'000	Derivatives Market \$'000	Clearing Business \$'000	Information Services \$'000	Group \$'000
<b>Income</b>	845,696	328,856	551,482	245,266	1,971,300
<b>Costs</b>	407,302	110,712	283,721	51,177	852,912
<b>Segment results</b>	438,394	218,144	267,761	194,089	1,118,388
Share of profits less losses of associates	(21)	–	13,013	–	12,992
Segment profits before taxation	438,373	218,144	280,774	194,089	1,131,380
Taxation					(171,464)
Profit attributable to shareholders					<b>959,916</b>



3. Segment Information (continued)

	As restated				Group \$'000
	Nine months ended 30 Sept 2004				
	Cash Market \$'000	Derivatives Market \$'000	Clearing Business \$'000	Information Services \$'000	
<b>Income</b>	757,498	238,154	506,956	231,937	1,734,545
<b>Costs</b>	399,643	108,199	291,064	58,131	857,037
<b>Segment results</b>	357,855	129,955	215,892	173,806	877,508
Share of profits less losses of associates	(1)	–	8,969	–	8,968
Segment profits before taxation	357,854	129,955	224,861	173,806	886,476
Taxation					(140,441)
Profit attributable to shareholders					746,035

The **Cash Market** business mainly refers to the operations of the Stock Exchange, which covers all products traded on the Cash Market platforms, such as equities, debt securities, unit trusts, warrants and rights. Currently, the Group operates two Cash Market platforms, the Main Board and the Growth Enterprise Market (“GEM”). The major sources of income of the business are trading fees, trading tariff and listing fees. Direct costs of the Listing Function are treated as segment costs under the Cash Market. Costs of the Listing Function are further explained in note 5.

The **Derivatives Market** business refers to the derivatives products traded on the Futures Exchange and stock options traded on the Stock Exchange, which includes the provision and maintenance of trading platforms for a range of derivatives products, such as equity and interest rate futures and options. Its income mainly comprises trading fees and net interest income on the Margin Funds received.

The **Clearing Business** refers to the operations of the three Clearing Houses, namely Hong Kong Securities Clearing Company Limited (“HKSCC”), The SEHK Options Clearing House Limited (“SEOCH”) and HKFE Clearing Corporation Limited (“HKCC”), which are responsible for clearing, settlement and custodian activities and the related risk management of the Cash and Derivatives Markets operated by the Group. Its income is derived primarily from interest earned on the Clearing House Funds and fees from providing clearing, settlement, depository and nominee services.

The **Information Services** business is responsible for developing, promoting, compiling and sales of real-time, historical as well as statistical market data and issuer information. Its income comprises primarily income from sale of Cash Market and Derivatives Market data.

In addition to the above, central income (mainly investment income of Corporate Funds) and central costs (mainly costs of the support functions that centrally provide services to all of the business segments) are allocated to the business segments and included in the segment income and costs.

#### 4. Trading Fees and Trading Tariff

	Nine months ended 30 Sept 2005 \$'000	Nine months ended 30 Sept 2004 \$'000	Three months ended 30 Sept 2005 \$'000	Three months ended 30 Sept 2004 \$'000
Trading fees and trading tariff were derived from:				
Securities traded on the Cash Market	386,952	328,087	152,192	91,280
Derivatives contracts traded on the Derivatives Market	193,501	166,523	75,646	56,158
	<b>580,453</b>	494,610	<b>227,838</b>	147,438

#### 5. Stock Exchange Listing Fees

Stock Exchange listing fees and costs of Listing Function comprised the following:

	Nine months ended 30 Sept 2005				As restated Nine months ended 30 Sept 2004			
	Equity		Debt & Derivatives	Total	Equity		Debt & Derivatives	Total
	Main Board	GEM			Main Board	GEM		
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
<b>Income</b>								
Annual listing fees	176,836	19,379	1,398	197,613	167,053	18,697	1,533	187,283
Initial and subsequent issue listing fees	35,124	3,470	62,287	100,881	26,104	9,540	43,955	79,599
Prospectus vetting fees	1,620	285	130	2,035	1,930	225	85	2,240
Other listing fees	2,272	760	–	3,032	1,530	662	–	2,192
Total income	<b>215,852</b>	<b>23,894</b>	<b>63,815</b>	<b>303,561</b>	196,617	29,124	45,573	271,314
<b>Costs of Listing Function</b>								
Staff costs and related expenses	71,506	20,523	3,915	95,944	55,030	22,930	3,853	81,813
Information technology and computer maintenance expenses	1,167	311	–	1,478	1,685	451	1	2,137
Premises expenses	4,749	1,354	296	6,399	4,104	1,688	285	6,077
Legal and professional fees	2,705	1,041	1	3,747	1,417	1,372	–	2,789
Depreciation	4,890	1,476	183	6,549	8,076	3,187	440	11,703
Payment to SFC under dual filing regime	12,238	2,762	–	15,000	12,251	2,749	–	15,000
Other operating expenses	3,477	1,327	137	4,941	4,374	1,363	148	5,885
Total costs	<b>100,732</b>	<b>28,794</b>	<b>4,532</b>	<b>134,058</b>	86,937	33,740	4,727	125,404
<b>Contribution</b>	<b>115,120</b>	<b>(4,900)</b>	<b>59,283</b>	<b>169,503</b>	109,680	(4,616)	40,846	145,910

5. Stock Exchange Listing Fees (continued)

	Three months ended 30 Sept 2005				As restated Three months ended 30 Sept 2004			
	Equity		Debt & Derivatives	Total	Equity		Debt & Derivatives	Total
	Main Board	GEM			Main Board	GEM		
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
<b>Income</b>								
Annual listing fees	59,335	6,450	472	66,257	56,967	6,187	465	63,619
Initial and subsequent issue listing fees	12,342	950	27,195	40,487	8,455	2,420	12,727	23,602
Prospectus vetting fees	435	120	20	575	370	15	–	385
Other listing fees	456	214	–	670	516	222	–	738
<b>Total income</b>	<b>72,568</b>	<b>7,734</b>	<b>27,687</b>	<b>107,989</b>	<b>66,308</b>	<b>8,844</b>	<b>13,192</b>	<b>88,344</b>
<b>Costs of Listing Function</b>								
Staff costs and related expenses	23,381	7,615	1,306	32,302	19,910	8,465	1,167	29,542
Information technology and computer maintenance expenses	395	95	–	490	519	146	(2)	663
Premises expenses	1,539	495	111	2,145	1,483	622	88	2,193
Legal and professional fees	1,070	284	–	1,354	335	477	–	812
Depreciation	1,172	413	41	1,626	2,334	947	109	3,390
Payment to SFC under dual filing regime	4,088	912	–	5,000	4,075	925	–	5,000
Other operating expenses	786	347	41	1,174	1,243	309	43	1,595
<b>Total costs</b>	<b>32,431</b>	<b>10,161</b>	<b>1,499</b>	<b>44,091</b>	<b>29,899</b>	<b>11,891</b>	<b>1,405</b>	<b>43,195</b>
<b>Contribution</b>	<b>40,137</b>	<b>(2,427)</b>	<b>26,188</b>	<b>63,898</b>	<b>36,409</b>	<b>(3,047)</b>	<b>11,787</b>	<b>45,149</b>

Listing fee income is fees paid by issuers to enable them to gain access to the Stock Exchange and enjoy the privileges and facilities by being admitted, listed and traded on the Stock Exchange.

The costs listed above are regulatory in nature, which comprise direct costs of the Listing Function on vetting Initial Public Offerings (“IPOs”) and enforcing the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited and the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited, disseminating information relating to listed companies, and payments to the Securities and Futures Commission (“SFC”) under the dual filing regime. Other indirect costs, comprising costs incurred by other divisions on building the reputation of the Stock Exchange (e.g. marketing and promotion, brand-building, and providing an efficient market infrastructure and market access facilities) to attract issuers to list on the Stock Exchange, which contribute to the Stock Exchange listing fee income above, are not included as they are part and parcel of the activities of the Group and cannot be separately quantified. Moreover, the costs do not cover costs of support services and other central overheads attributable to the Listing Function.

6. Investment Income

	Nine months ended 30 Sept 2005 \$'000	As restated Nine months ended 30 Sept 2004 \$'000	Three months ended 30 Sept 2005 \$'000	As restated Three months ended 30 Sept 2004 \$'000
Interest income				
– bank deposits	159,733	14,977	91,162	7,149
– listed available-for-sale financial assets	8,191	3,097	3,293	1,183
– unlisted available-for-sale financial assets	54,487	38,213	20,000	13,679
	<b>222,411</b>	56,287	<b>114,455</b>	22,011
Interest expenses	<b>(65,375)</b>	(314)	<b>(46,141)</b>	(195)
Net interest income	<b>157,036</b>	55,973	<b>68,314</b>	21,816
Net realised and unrealised gains/(losses) and interest income on financial assets at fair value through profit or loss				
– bank deposits with embedded derivatives	266	505	–	2,834
– listed securities	70,561	53,319	34,111	25,684
– unlisted securities	5,119	25,560	1,258	10,980
– exchange differences	<b>(13,389)</b>	(3,086)	<b>(3,691)</b>	2,257
	<b>62,557</b>	76,298	<b>31,678</b>	41,755
Gains/(losses) on disposal and maturity of available-for-sale financial assets				
– listed securities	–	24,841	–	24,841
– unlisted securities	–	101	–	–
– exchange differences	–	(192)	–	(41)
	–	24,750	–	24,800
Dividend income				
– listed available-for-sale financial assets	–	1,070	–	–
– listed financial assets at fair value through profit or loss	5,707	5,251	2,296	1,899
	<b>5,707</b>	6,321	<b>2,296</b>	1,899
Other exchange differences	<b>(301)</b>	554	<b>638</b>	138
<b>Total investment income</b>	<b>224,999</b>	163,896	<b>102,926</b>	90,408
Total investment income was derived from:				
Corporate Funds (note a)	86,838	111,577	44,495	66,812
Margin Funds	118,374	44,864	49,221	20,870
Clearing House Funds	19,787	7,455	9,210	2,726
	<b>224,999</b>	163,896	<b>102,926</b>	90,408

- (a) Investment income derived from Corporate Funds included investment income of Compensation Fund Reserve Account of \$869,000 (2004: \$412,000) and Cash and Derivatives Market Development Fund (“CDMD Fund”) of \$Nil (2004: \$17,000) for the nine months ended 30 September 2005, and investment income of Compensation Fund Reserve Account of \$371,000 (2004: \$149,000) and CDMD Fund of \$Nil (2004: \$5,000) for the three months ended 30 September 2005. The CDMD Fund was fully utilised in 2004.

**7. Other Income**

	Nine months ended 30 Sept 2005 \$'000	As restated Nine months ended 30 Sept 2004 \$'000	Three months ended 30 Sept 2005 \$'000	As restated Three months ended 30 Sept 2004 \$'000
Network, terminal user, dataline and software sub-license fees	94,726	86,731	28,592	29,924
Participants' subscription and application fees	25,837	25,778	8,555	8,548
Brokerage on direct IPO applications	10,149	11,288	3,961	2,906
Fair value gain of an investment property	3,200	–	600	–
Accommodation income on cash margin deposits in non-contract settlement currencies and securities deposited by Participants as alternatives to cash deposits of the Margin Funds	1,898	4,361	404	572
Miscellaneous income	8,571	5,992	2,418	1,509
	<b>144,381</b>	134,150	<b>44,530</b>	43,459

**8. Staff Costs and Related Expenses**

Staff costs and related expenses comprised the following:

	Nine months ended 30 Sept 2005 \$'000	As restated Nine months ended 30 Sept 2004 \$'000	Three months ended 30 Sept 2005 \$'000	As restated Three months ended 30 Sept 2004 \$'000
Salaries and other short-term employee benefits	369,382	349,162	123,242	116,952
Employee share option benefits (note 23(a))	17,254	10,096	5,909	4,194
Termination benefits	236	3,918	236	322
Retirement benefit costs (note a):				
– ORSO Plan	37,683	35,195	12,539	11,939
– MPF Scheme	209	259	76	70
	<b>424,764</b>	398,630	<b>142,002</b>	133,477

- (a) The Group has sponsored two defined contribution post-retirement benefit plans – the Hong Kong Exchanges and Clearing Provident Fund Scheme (“ORSO Plan”) and the AIA-JF Premium MPF Scheme (“MPF Scheme”). The retirement benefit costs charged to the condensed consolidated profit and loss account represent contributions paid and payable by the Group to the ORSO Plan and the MPF Scheme. No contribution payable was outstanding as at 30 September 2004 and 2005.

**9. Information Technology and Computer Maintenance Expenses**

	Nine months ended 30 Sept 2005 \$'000	Nine months ended 30 Sept 2004 \$'000	Three months ended 30 Sept 2005 \$'000	Three months ended 30 Sept 2004 \$'000
Costs of services and goods:				
– consumed by the Group	109,054	122,863	36,227	41,740
– directly consumed by Participants	39,418	43,780	13,182	14,886
	<b>148,472</b>	166,643	<b>49,409</b>	56,626

**10. Other Operating Expenses**

	Nine months ended 30 Sept 2005 \$'000	As restated Nine months ended 30 Sept 2004 \$'000	Three months ended 30 Sept 2005 \$'000	As restated Three months ended 30 Sept 2004 \$'000
Reversal of provision for impairment losses of trade receivables	(425)	(614)	(53)	(744)
Insurance	12,023	12,389	3,821	4,144
Financial data subscription fees	3,898	5,822	1,141	1,889
Custodian and fund management fees	5,885	5,858	1,994	1,895
Bank charges	2,824	5,603	1,036	1,644
Repair and maintenance expenses	5,767	5,103	1,993	1,714
Other miscellaneous expenses	30,933	29,555	10,031	9,052
	<b>60,905</b>	63,716	<b>19,963</b>	19,594

**11. Taxation**

Taxation charge/(credit) in the condensed consolidated profit and loss account represents:

	Nine months ended 30 Sept 2005 \$'000	As restated Nine months ended 30 Sept 2004 \$'000	Three months ended 30 Sept 2005 \$'000	As restated Three months ended 30 Sept 2004 \$'000
Provision for Hong Kong Profits Tax (note a)	182,910	156,499	68,061	46,880
Overprovision in respect of prior years	(34)	–	(34)	–
	<b>182,876</b>	156,499	<b>68,027</b>	46,880
Deferred taxation	(11,412)	(16,058)	(2,349)	(7,631)
	<b>171,464</b>	140,441	<b>65,678</b>	39,249

- (a) Hong Kong Profits Tax has been provided for at 17.5 per cent (2004: 17.5 per cent) on the estimated assessable profit for the period.

## 12. Earnings Per Share

The calculation of basic earnings per share for the nine months ended 30 September 2005 is based on the profit attributable to shareholders of \$959,916,000 (2004: \$746,035,000) and the weighted average of 1,059,628,097 shares (2004: 1,054,436,372 shares) in issue during the period.

The calculation of basic earnings per share for the three months ended 30 September 2005 is based on the profit attributable to shareholders of \$389,120,000 (2004: \$248,610,000) and the weighted average of 1,061,660,552 shares (2004: 1,056,502,998 shares) in issue during the period.

The employee share options outstanding did not have a material dilutive effect on the basic earnings per share for the nine-month and three-month periods ended 30 September 2005 and 30 September 2004.

## 13. Fixed Assets

The Group is heavily reliant on the capability and reliability of its computer systems for its business operations, including those required for its electronic trading platforms and for post-trading clearing and settlement services. Fixed assets decreased mainly attributable to depreciation during the period. The total cost of additions to fixed assets of the Group during the nine months to 30 September 2005 was \$41,257,000 (2004: \$17,274,000) of which \$36,173,000 (2004: \$16,424,000) or 88 per cent (2004: 95 per cent) was on computer systems, hardware and software. The total cost and net book value of disposals and write-offs of fixed assets during the nine months to 30 September 2005 were \$8,062,000 and \$1,000 respectively (2004: \$140,507,000 and \$172,000 respectively).

## 14. Investment Property

The Group's investment property was revalued as at 30 September 2005 on the basis of its open market value by Jones Lang LaSalle, an independent firm of qualified property valuers. The fair value gain during the nine months ended 30 September 2005 of \$3,200,000 (2004: \$Nil) was credited to the condensed consolidated profit and loss account under other income (note 7).

**15. Investments in Associates**

	At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000
Share of net assets of associates	8,883	13,790
Goodwill (note a)	50,207	24,941
	<b>59,090</b>	<b>38,731</b>

(a) Goodwill

	At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000
At 1 Jan	24,941	24,941
Further acquisition of 6% interest in Computershare Hong Kong Investor Services Limited on 3 May 2005	25,266	–
At 30 Sept 2005/31 Dec 2004	<b>50,207</b>	<b>24,941</b>
Represented by:		
Opening value upon adoption of HKFRS 3	25,321	25,321
Addition at cost	25,266	–
Accumulated impairment	(380)	(380)
	<b>50,207</b>	<b>24,941</b>

(b) Details of the unlisted associates as at 30 September 2005 were as follows:

Name	Place of incorporation	Principal activities	Particulars of shares held	Interest held
Computershare Hong Kong Investor Services Limited ("CHIS")	Hong Kong	Provision of share registration services	7,317 Class A ordinary shares	30%
ADP Wilco Processing Services Limited ("AWPS")	Hong Kong	Provision of transaction processing services to Stock Exchange Participants	6 Class B ordinary shares	30%

AWPS has an accounting year end of 30 June, which is not coterminous with the Group's accounting year end. Voluntary liquidation of AWPS commenced in April 2005.

(c) Share of profits less losses of associates

	Nine months ended 30 Sept 2005 \$'000	As restated Nine months ended 30 Sept 2004 \$'000	Three months ended 30 Sept 2005 \$'000	As restated Three months ended 30 Sept 2004 \$'000
Share of profits less losses of associates	14,992	10,858	5,174	3,369
Share of taxation of associates	(2,000)	(1,890)	(817)	(545)
	<b>12,992</b>	<b>8,968</b>	<b>4,357</b>	<b>2,824</b>



**16. Clearing House Funds**

	At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000
Net assets of the Clearing House Funds were as follows:		
HKSCC Guarantee Fund	335,604	339,598
SEOCH Reserve Fund	427,034	160,119
HKCC Reserve Fund	998,138	1,361,770
	<b>1,760,776</b>	<b>1,861,487</b>
Net assets of the Clearing House Funds were composed of:		
Available-for-sale financial assets, at fair value		
– listed debt securities	99,715	–
– unlisted debt securities	124,679	127,569
Time deposits with original maturity over three months	30,155	144,610
Cash and cash equivalents	1,520,538	1,604,089
	<b>1,775,087</b>	<b>1,876,268</b>
Less: Other liabilities	(14,311)	(14,781)
	<b>1,760,776</b>	<b>1,861,487</b>
The Clearing House Funds were funded by:		
Clearing Participants' cash contributions (note a)	1,189,683	1,298,752
Designated reserves (note 25):		
– Clearing houses' contributions	320,200	320,200
– Forfeiture of a defaulted Clearing Participant's contributions	1,928	1,928
– Accumulated investment income net of expenses attributable to:		
– Clearing Participants' contributions	191,912	182,839
– Clearing houses' contributions	58,896	55,659
	<b>572,936</b>	<b>560,626</b>
Revaluation reserve (note 24(c))	(1,843)	2,109
	<b>1,760,776</b>	<b>1,861,487</b>
The maturity profile of the net assets of the Clearing House Funds was as follows:		
Amounts maturing after more than twelve months	99,715	157,858
Amounts maturing within twelve months	1,661,061	1,703,629
	<b>1,760,776</b>	<b>1,861,487</b>

- (a) Amount included Participants' additional deposits of \$837,733,000 (31 December 2004: \$961,502,000).
- (b) The HKSCC Guarantee Fund provides resources to enable HKSCC to discharge the liabilities and obligations of defaulting Broker Participants in Central Clearing and Settlement System ("CCASS") arising from their Stock Exchange trades accepted for settlement on the Continuous Net Settlement ("CNS") basis and defective securities deposited into CCASS. The SEOCH Reserve Fund and the HKCC Reserve Fund were established for the exclusive purpose of supporting SEOCH and HKCC to fulfil their counterparty obligations in the event that one or more of their Clearing Participants fail to meet their obligations to SEOCH and HKCC respectively.

**17. Compensation Fund Reserve Account**

	At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000
Net assets of the Compensation Fund Reserve Account were composed of:		
Available-for-sale financial assets, at fair value		
– unlisted debt securities	18,326	18,831
Cash and cash equivalents	29,943	29,137
Other receivable	–	100
	<b>48,269</b>	48,068
Less: Other liabilities	<b>(10,306)</b>	(10,617)
	<b>37,963</b>	37,451
The Fund represented:		
Accumulated investment income net of expenses included in designated reserves (note 25)	38,003	37,117
Revaluation reserve (note 24(c))	(40)	334
	<b>37,963</b>	37,451
The maturity profile of the net assets of the Compensation Fund Reserve Account was as follows:		
Amounts maturing after more than twelve months	–	18,831
Amounts maturing within twelve months	37,963	18,620
	<b>37,963</b>	37,451

The SFC is responsible for maintaining the Unified Exchange Compensation Fund (“Compensation Fund”). By virtue of Schedule 10 of the Securities and Futures Ordinance (“SFO”), the Stock Exchange’s obligation under the repealed Securities Ordinance (“SO”) to deposit with the SFC and keep deposited \$50,000 in respect of each Stock Exchange Trading Right in the Compensation Fund remains. The Stock Exchange maintains an account known as the Compensation Fund Reserve Account for all receipts and payments in relation to the Compensation Fund under the Rules of the Exchange, in particular the following:

- (i) The interest received from the SFC on the statutory deposits paid in respect of each Stock Exchange Trading Right into the Compensation Fund maintained by the SFC;
- (ii) Amounts received or paid out in relation to each of the Stock Exchange Trading Rights granted or revoked by the Stock Exchange respectively; and
- (iii) Amounts reserved for the replenishment to the Compensation Fund.

The Compensation Fund is further explained in note 29(a).

**18. Accounts Receivable, Prepayments and Deposits/Accounts Payable, Accruals and Other Liabilities**

The Group's accounts receivable, prepayments and deposits amounted to \$5,621,805,000 (31 December 2004: \$4,691,846,000). These mainly represented the Group's CNS money obligations receivable under the T+2 settlement cycle, which accounted for 94 per cent (31 December 2004: 91 per cent) of the total accounts receivable, prepayments and deposits. CNS money obligations receivable mature within two days as they are due for settlement two days after the trade date. Fees receivable are due immediately or up to 30 days depending on the type of services rendered. The majority of the remaining accounts receivable, prepayments and deposits would mature within three months.

The Group's accounts payable, accruals and other liabilities amounted to \$6,121,919,000 (31 December 2004: \$4,902,350,000). These mainly represented the Group's CNS money obligations payable under the T+2 settlement cycle, which accounted for 86 per cent (31 December 2004: 87 per cent) of the total accounts payable, accruals and other liabilities. CNS money obligations payable mature within two days as they are due for settlement two days after the trade date. The majority of the remaining accounts payable, accruals and other liabilities would mature within three months.

**19. Margin Funds on Derivatives Contracts**

	At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000
The Margin Funds comprised:		
SEOCH Clearing Participants' Margin Funds	1,857,958	915,250
HKCC Clearing Participants' Margin Funds	12,735,282	9,614,442
	<b>14,593,240</b>	<b>10,529,692</b>
The assets of the Margin Funds comprised:		
Financial assets at fair value through profit or loss, on designation		
– bank deposits with embedded derivatives, at fair value	–	130,871
Available-for-sale financial assets, at fair value		
– listed debt securities	436,552	339,158
– unlisted debt securities	4,088,339	3,280,786
Time deposits with original maturity over three months	150,778	300,784
Cash and cash equivalents	9,904,211	6,443,406
Margin receivable from Clearing Participants	13,360	34,687
	<b>14,593,240</b>	<b>10,529,692</b>
The Group's liabilities in respect of the Margin Funds were as follows:		
Margin deposits from SEOCH and HKCC Participants on derivatives contracts	14,593,240	10,529,692
The maturity profile of the assets of Margin Funds was as follows:		
Amounts maturing after more than twelve months	1,264,541	2,138,362
Amounts maturing within twelve months	13,328,699	8,391,330
	<b>14,593,240</b>	<b>10,529,692</b>

## 20. Financial Assets/Liabilities at Fair Value through Profit or Loss

	At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000
<b>Analysis of financial assets at fair value through profit or loss:</b>		
<i>Held for trading</i>		
Equity securities, at fair value		
– listed in Hong Kong	153,560	93,154
– listed outside Hong Kong	174,324	151,954
	<b>327,884</b>	245,108
<i>Held for trading</i>		
Debt securities, at fair value		
– listed in Hong Kong	40,919	–
– listed outside Hong Kong	1,089,114	1,278,858
– unlisted	1,227,097	1,200,195
	<b>2,357,130</b>	2,479,053
<i>Held for trading</i>		
Derivative financial instruments, at fair value		
– forward foreign exchange contracts	1,171	247
<i>Designated as financial assets at fair value through profit or loss</i>		
Bank deposits with embedded derivatives, at fair value	–	37,185
	<b>2,686,185</b>	2,761,593
<b>Analysis of financial liabilities at fair value through profit or loss:</b>		
<i>Held for trading</i>		
Derivative financial instruments, at fair value		
– forward foreign exchange contracts	2,058	10,749

## 21. Provisions

	Reinstatement costs \$'000	Employee benefit costs \$'000	Total \$'000
At 1 Jan 2005	24,104	23,212	47,316
Provision for the period	20	25,994	26,014
Amount used during the period	(441)	(22,162)	(22,603)
Amount paid during the period	–	(1,709)	(1,709)
At 30 Sept 2005	<b>23,683</b>	<b>25,335</b>	<b>49,018</b>
		At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000
<b>Analysis of provisions:</b>			
Current		27,895	23,212
Non-current		21,123	24,104
		<b>49,018</b>	<b>47,316</b>

## 22. Share Capital and Share Premium

	At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000
Authorised:		
2,000,000,000 shares of \$1 each	<b>2,000,000</b>	2,000,000

Issued and fully paid:

	Number of shares of \$1 each	Share capital \$'000	Share premium \$'000	Total \$'000
At 1 Jan 2004	1,048,998,846	1,048,999	54,338	1,103,337
Shares issued under employee share option schemes	7,640,000	7,640	49,696	57,336
At 31 Dec 2004	1,056,638,846	1,056,639	104,034	1,160,673
Shares issued under employee share option schemes	<b>5,758,000</b>	<b>5,758</b>	<b>37,765</b>	<b>43,523</b>
Transfer from employee share-based compensation reserve	–	–	<b>4,065</b>	<b>4,065</b>
At 30 Sept 2005	<b>1,062,396,846</b>	<b>1,062,397</b>	<b>145,864</b>	<b>1,208,261</b>

During the period, employee share options granted under the Pre-Listing Share Option Scheme (“Pre-Listing Scheme”) and Post-Listing Share Option Scheme (“Post-Listing Scheme”) were exercised to subscribe for 5,758,000 shares (year ended 31 December 2004: 7,640,000 shares) in HKEx at an average consideration of \$7.56 per share (year ended 31 December 2004: \$7.50 per share), of which \$1.00 per share was credited to share capital and the balance was credited to the share premium account.

## 23. Employee Share-based Compensation Reserve

	At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000
At 1 Jan	<b>17,061</b>	2,771
Employee share option benefits (note a)	<b>17,254</b>	14,290
Transfer to share premium upon exercise of employee share options	<b>(4,065)</b>	–
Share of reserve of an associate	<b>43</b>	–
At 30 Sept 2005/31 Dec 2004	<b>30,293</b>	17,061

- (a) Employee share option benefits represent the fair value of employee services estimated to be received in exchange for the grant of the relevant options over the vesting period, the total of which is based on the fair value of the options at grant date. The amount for each period is determined by spreading the fair value of the options over the vesting period and is recognised as staff costs and related expenses (note 8) with a corresponding increase in the employee share-based compensation reserve.

**23. Employee Share-based Compensation Reserve (continued)**

- (b) Share options have been granted to an Executive Director and employees of the Group to subscribe for shares in HKEx in accordance with the terms and conditions of the Share Option Schemes approved by the shareholders of HKEx at an extraordinary general meeting held on 31 May 2000.

During the period, options for the subscription of 5,884,000 shares were granted under the Post-Listing Scheme to a number of employees on 26 January 2005 which are exercisable between 26 January 2007 and 25 January 2015 at an exercise price of \$19.25 per share.

- (c) Movements in the number of shares issuable under options granted and their related weighted average exercise prices were as follows:

	Nine months ended 30 Sept 2005		Year ended 31 Dec 2004	
	Average exercise price per share \$	Number of shares issuable under options granted	Average exercise price per share \$	Number of shares issuable under options granted
<b>Pre-Listing Scheme</b>				
Outstanding at 1 Jan	6.88	6,680,000	7.52	14,171,626
Exercised	6.88	(4,446,000)	7.50	(7,640,000)
Forfeited	–	–	7.00	(524,829)
Adjusted *	–	–	N/A	673,203
Outstanding at 30 Sept 2005/31 Dec 2004	6.88	2,234,000	6.88	6,680,000
<b>Post-Listing Scheme</b>				
Outstanding at 1 Jan	13.78	13,218,000	11.26	5,800,000
Granted	19.25	5,884,000	17.21	6,888,000
Exercised	9.86	(1,312,000)	–	–
Forfeited	17.95	(620,000)	16.96	(106,000)
Adjusted *	–	–	N/A	636,000
Outstanding at 30 Sept 2005/31 Dec 2004	15.80	17,170,000	13.78	13,218,000
<b>Total</b>	<b>14.78</b>	<b>19,404,000</b>	<b>11.46</b>	<b>19,898,000</b>

\* Adjustments approved by shareholders at the 2004 annual general meeting held on 31 March 2004

**23. Employee Share-based Compensation Reserve (continued)**

- (d) According to the Binomial Option Pricing Model, the details of the options granted during the period under the Post-Listing Scheme were as follows:

Date of grant	Number of shares issuable under options granted	Option value	Closing share price at date of grant	Risk free rate (being the yield of 10-year Exchange Fund Notes)	Expected volatility (note i)	Expiration of the options	Expected ordinary dividend (note iii)
26 Jan 2005	5,884,000	\$26,183,800	\$19.25	3.67%	26%	10 years from 26 Jan 2005	4.42%

- (i) The volatility measured at the standard deviation of expected share price returns is based on statistical analysis of daily share prices over the one year immediately preceding the grant date.
- (ii) The above calculation is based on the assumption that there is no material difference between the expected volatility over the whole life of the options and the historical volatility of the shares in HKEx set out above.
- (iii) Expected ordinary dividend is based on 2005 prospective dividend yield of the shares as at 26 January 2005.
- (e) Had all the outstanding employee share options been fully exercised on 30 September 2005, the Group would have received \$286,711,260 in proceeds. The market value of the shares issued based on the closing price of \$26.55 per share on that date would have been \$515,176,200. The theoretical gains made by the employees or Executive Director concerned would have been as follows:

	Number of shares issuable under options granted as at 30 Sept 2005	Exercise price \$	Gain per share \$	Aggregate gain \$'000
<b>Pre-Listing Scheme</b>				
– granted to employees on 20 Jun 2000	2,234,000	6.88	19.67	43,943
<b>Post-Listing Scheme</b>				
– granted to an Executive Director on 2 May 2003	2,460,000	8.28	18.27	44,944
– granted to an employee on 14 Aug 2003	1,094,000	12.45	14.10	15,425
– granted to an employee on 18 Aug 2003	1,476,000	12.49	14.06	20,753
– granted to an employee on 15 Jan 2004	1,094,000	17.30	9.25	10,119
– granted to employees on 31 Mar 2004	5,230,000	16.96	9.59	50,156
– granted to an employee on 17 May 2004	200,000	15.91	10.64	2,128
– granted to employees on 26 Jan 2005	5,616,000	19.25	7.30	40,997
<b>Total</b>	<b>19,404,000</b>			<b>228,465</b>

## 24. Revaluation Reserves

	At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000
Leasehold buildings revaluation reserve	2,085	2,537
Investment revaluation reserve (note c)	(55,142)	16,292
	<b>(53,057)</b>	<b>18,829</b>

- (a) The revaluation reserves are segregated for their respective specific purposes and are stated net of applicable deferred taxes.
- (b) Leasehold buildings are revalued on a six-monthly basis at the end of June and December each year.
- (c) Included gross investment revaluation deficits of \$1,843,000 and \$40,000 (31 December 2004: gross surpluses of \$2,109,000 and \$334,000 respectively) which were attributable to investments of the Clearing House Funds and the Compensation Fund Reserve Account respectively. The significant decrease in investment revaluation reserve was primarily due to the decrease in fair value of available-for-sale financial assets of the Margin Funds arising mainly from increases in interest rates during the period. The revaluation deficit is not expected to have any impact to the Group's profit and loss account as the available-for-sale financial assets are expected to be held till maturity and the deficit will gradually reduce to zero.

## 25. Designated Reserves

	At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000
Clearing House Funds reserves		
– HKSCC Guarantee Fund reserve	249,265	247,853
– SEOCH Reserve Fund reserve	52,853	48,774
– HKCC Reserve Fund reserve	270,818	263,999
	<b>572,936</b>	<b>560,626</b>
Compensation Fund Reserve Account reserve	38,003	37,117
Development reserve (note b)	75,720	83,253
	<b>686,659</b>	<b>680,996</b>

- (a) These reserves are segregated for their respective purposes.
- (b) The Development reserve was set aside for systems development for the Stock Exchange. During the nine months ended 30 September 2005, \$7,533,000 (2004: \$3,159,000) of the reserve was utilised and transferred to the Group's retained earnings (note 26) for funding systems development projects relating to the securities market.



**26. Retained Earnings (Including Proposed/Declared Dividends)**

	At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000
At 1 Jan		
Retained earnings	1,677,964	1,578,991
Proposed/declared dividends	496,620	2,202,898
Profit for the period/year (note a)	959,916	1,056,884
(Surplus)/deficit of investment income net of expenses of Clearing House Funds for the period/year transferred to Clearing House Funds reserves	(12,310)	5,040
Investment income net of expenses of Compensation Fund Reserve Account for the period/year transferred to Compensation Fund Reserve Account reserve	(886)	(576)
Transfer from CDMD Fund reserve (note b)	–	914
Transfer from Development reserve	7,533	3,283
Dividends paid:		
2004 final dividend/2003 special and final dividends	(496,620)	(2,202,898)
Dividend on shares issued for employee share options exercised after 31 Dec 2004/2003	(1,597)	(15,661)
	(498,217)	(2,218,559)
2005/2004 interim dividend	(519,988)	(454,283)
Dividend on shares issued for employee share options exercised after 30 Jun 2005/2004	(579)	(8)
	(520,567)	(454,291)
At 30 Sept/31 Dec	<b>2,110,053</b>	2,174,584
Representing:		
Retained earnings	2,110,053	1,677,964
Proposed/declared dividends	–	496,620
At 30 Sept/31 Dec	<b>2,110,053</b>	2,174,584

- (a) The Group's profit for the period/year included a net profit attributable to investment income net of expenses of the Clearing House Funds, Compensation Fund Reserve Account and CDMD Fund for an aggregate amount of \$13,196,000 (year ended 31 December 2004: deficit of \$2,182,000).
- (b) The CDMD Fund reserve was fully utilised in 2004 for funding initiatives that were for the development and betterment of the Cash and Derivatives Markets in Hong Kong.

**27. Notes to the Condensed Consolidated Cash Flow Statement**

(a) Reconciliation of profit before taxation to net cash inflow from operating activities:

	Nine months ended 30 Sept 2005 \$'000	As restated Nine months ended 30 Sept 2004 \$'000
Profit before taxation	1,131,380	886,476
Adjustments for:		
Net interest income	(157,036)	(55,973)
Dividends from available-for-sale financial assets	–	(1,070)
Net realised and unrealised gains and interest income on financial assets at fair value through profit or loss	(62,557)	(76,298)
Gain on disposal of available-for-sale financial assets	–	(24,841)
Amortisation of lease premium for land	410	411
Fair value gain of an investment property	(3,200)	–
Depreciation	125,548	137,926
Employee share option benefits	17,254	10,096
Reversal of provision for impairment losses of trade receivables	(425)	(614)
Changes in provisions	1,682	(66)
Share of profits less losses of associates	(12,992)	(8,968)
(Gain)/loss on disposal of fixed assets	(52)	16
Operating profit before working capital changes	1,040,012	867,095
Net decrease in financial assets and financial liabilities at fair value through profit or loss	25,928	609,839
Fair value gain of hedging instruments retained in hedging reserve	8	–
Settlement of amount transferred from retained earnings to Clearing House Funds and Compensation Fund Reserve Account	(13,196)	(2,400)
Settlement of amount transferred from CDMD Fund reserve to retained earnings	–	505
(Increase)/decrease in accounts receivable, prepayments and deposits	(940,068)	1,651,681
Increase/(decrease) in other current liabilities	1,029,871	(1,753,353)
Net cash inflow from operations	1,142,555	1,373,367
Interest received	159,733	14,977
Cash received on financial assets at fair value through profit or loss	60,190	64,697
Interest paid	(65,258)	(204)
Hong Kong Profits Tax paid	(107,346)	(36)
Net cash inflow from operating activities	1,189,874	1,452,801

(b) The net assets of the Clearing House Funds, Compensation Fund Reserve Account and Margin Funds are held in segregated accounts for specific purposes. Movements in individual items of the net assets of the funds during the period therefore did not constitute any cash or cash equivalent transactions to the Group.

## 28. Commitments

Commitments in respect of capital expenditures:

	At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000
Contracted but not provided for	18,048	4,484
Authorised but not contracted for	83,514	73,554
	<b>101,562</b>	<b>78,038</b>

The commitments in respect of capital expenditures were mainly for the refurbishment of the Trading Hall and the development and purchases of computer systems.

## 29. Contingent Liabilities

- (a) The Compensation Fund is a fund set up under the repealed SO for the purpose of compensating any person (other than a Stock Exchange Participant) dealing with a Stock Exchange Participant for any pecuniary losses suffered as a result of a default by the Stock Exchange Participant. According to section 109(3) of the SO, the maximum compensation amount is \$8 million for each Stock Exchange Participant's default. Under section 113(5A) of the SO, the Stock Exchange may, upon satisfying certain conditions, and with the approval of the SFC, allow an additional payment to successful claimants before apportionment. Under section 107(1) of the SO, the Stock Exchange has contingent liabilities to the Compensation Fund as it is obligated to replenish the Compensation Fund upon the SFC's request. The amounts to be replenished should be equal to the amount paid in connection with the satisfaction of the claims, including any legal and other expenses paid or incurred in relation to the claims but capped at \$8 million per default. As at 30 September 2005, there were outstanding claims received in respect of 8 Stock Exchange Participants (31 December 2004: 10).

Pursuant to the SFO, the Stock Exchange issued a notice on 3 April 2003 inviting claims against the Compensation Fund in relation to any default of a Stock Exchange Participant occurring before 1 April 2003. The claims period expired on 3 October 2003 and no claims were received in response to that notice. Claims made after the claims period are, unless the Stock Exchange otherwise determines, barred. As at 30 September 2005, no such claims had been received in response to the said notice.

Following the implementation of the new compensation arrangements under the SFO, an Investor Compensation Fund has been established to replace the existing Compensation Fund, the Commodity Exchange Compensation Fund and the Dealers' Deposit Schemes for non-exchange participant dealers. Pursuant to the SFO, Exchange Participants are no longer required to make deposits to the Investor Compensation Fund and the Stock Exchange is not required to replenish the Investor Compensation Fund. Hence, deposits to the Commodity Exchange Compensation Fund were returned to the Futures Exchange by the SFC in January 2004. The Futures Exchange had in turn reimbursed holders of Futures Exchange Trading Rights their contributions to the Commodity Exchange Compensation Fund. Similarly, deposits to the Compensation Fund would be returned to the Stock Exchange in accordance with the SFO pending completion of any determination of outstanding claims and replenishment to the Compensation Fund.

**29. Contingent Liabilities (continued)**

- (b) The Stock Exchange has undertaken to indemnify the Collector of Stamp Revenue against any loss of revenue resulting from any underpayment or default or delay in payment of stamp duty by its Participants, up to \$200,000 in respect of the default of any one Participant. In the unlikely event that all of its 426 trading Participants as at 30 September 2005 (31 December 2004: 434) defaulted, the maximum contingent liability of the Stock Exchange under the indemnity would amount to \$85 million (31 December 2004: \$87 million).
- (c) HKEx gave an undertaking on 6 March 2000 in favour of HKSCC to contribute an amount not exceeding \$50 million in the event of HKSCC being wound up while it is a wholly-owned subsidiary of HKEx or within one year after HKSCC ceases to be a wholly-owned subsidiary of HKEx, for payment of the debts and liabilities of HKSCC contracted before HKSCC ceases to be a wholly-owned subsidiary of HKEx, and for the costs, charges and expenses of winding up.
- (d) In May 2005, the Court of Appeal issued its judgement in the New World Development Company Limited and others (“New World”) judicial review appeal case. The Court allowed the appeal and quashed the direction of the Chairman of the Listing (Disciplinary) Committee in the New World disciplinary proceedings that legal advisers not be permitted to address the Listing (Disciplinary) Committee. New World was awarded costs which are estimated to be in the region of \$4 million. The Stock Exchange has been granted leave to appeal to the Court of Final Appeal. A formal submission will be made to the Court of Final Appeal shortly. In the opinion of external legal counsel, the Stock Exchange has valid grounds for an appeal, a reasonable prospect of success and consequently it is not probable that the Stock Exchange will be required to bear the costs incurred by New World in the legal proceedings. Accordingly, no provision for such costs has been made in the accounts.

**30. Non-cash Collateral Received from Participants**

As at 30 September 2005, the following non-cash collateral had been received from Clearing Participants for covering part of their Clearing House Fund contributions and Margin Fund obligations:

	At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000
<b>Clearing House Funds</b>		
Bank guarantees	151,408	322,724
<b>Margin Funds</b>		
Equity securities, listed in Hong Kong	640,369	610,318
US Treasury Bills	271,401	504,287
	911,770	1,114,605
<b>Total</b>	<b>1,063,178</b>	<b>1,437,329</b>

### 31. Material Related Party Transactions

Certain Directors of HKEx are investor participants of HKSCC (“Investor Participants”) or directors and/or shareholders of (i) Stock Exchange Participants and Futures Exchange Participants (“Exchange Participants”), Clearing Participants and Investor Participants; (ii) companies listed on the Stock Exchange; and (iii) Exchange Participants for buying shares on behalf of HKSCC. Securities and derivatives contracts traded by, and fees levied on, these Exchange Participants, Clearing Participants and Investor Participants, fees levied on these listed companies and fees paid to these Exchange Participants for buying shares on behalf of HKSCC are all undertaken in the ordinary course of business of the Group on the standard terms and conditions applicable to all other Exchange Participants, Clearing Participants and Investor Participants, listed companies and Exchange Participants for buying shares on behalf of HKSCC.

In addition to the above, the Group has entered into the following transactions with related parties:

(a) An associate

	<b>Nine months ended 30 Sept 2005 \$'000</b>	Nine months ended 30 Sept 2004 \$'000	<b>Three months ended 30 Sept 2005 \$'000</b>	Three months ended 30 Sept 2004 \$'000
Income received and receivable from/(expenses paid and payable to) an associate, CHIS:				
– Dividend income	<b>17,952</b>	8,401	<b>5,284</b>	2,401
– Share registration service fees	<b>(364)</b>	(284)	<b>(95)</b>	(112)

(b) Related companies with common directors

	<b>Nine months ended 30 Sept 2005 \$'000</b>	Nine months ended 30 Sept 2004 \$'000	<b>Three months ended 30 Sept 2005 \$'000</b>	Three months ended 30 Sept 2004 \$'000
Rental payments (including air conditioning and cleaning service charges) to Shine Hill Development Limited (“Shine Hill”) (note i)	<b>3,970</b>	3,325	<b>1,302</b>	1,345

- (i) On 5 February 2003, the Futures Exchange as the tenant entered into a tenancy agreement (“Lease”) with Shine Hill as the landlord. The Lease expired on 31 December 2004 and was subsequently renewed for a further term of two years commencing 1 January 2005 (“New Lease”). The Futures Exchange is a wholly-owned subsidiary of HKEx. Shine Hill is a subsidiary of Great Eagle Holdings Limited (“Great Eagle”). Dr LO Ka Shui is an Independent Non-executive Director of HKEx and the deputy chairman, managing director and substantial shareholder of Great Eagle. The Lease and the New Lease were arm’s length transactions entered into on normal commercial terms.

**31. Material Related Party Transactions (continued)**

(c) Key management personnel compensation

	Nine months ended 30 Sept 2005 \$'000	Nine months ended 30 Sept 2004 \$'000	Three months ended 30 Sept 2005 \$'000	Three months ended 30 Sept 2004 \$'000
Salaries and other short-term employee benefits	39,142	36,851	13,174	12,364
Employee share option benefits	7,256	6,202	2,392	2,236
Termination benefits	–	1,569	–	819
Retirement benefit costs	4,116	4,096	1,362	1,431
	<b>50,514</b>	48,718	<b>16,928</b>	16,850

(d) Amounts due from/(to) related parties

	At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000
Amounts due from:		
– An associate	13,152	–
– Related companies with common directors	867	867
Amounts due to:		
– An associate	(72)	(55)
– Related companies with common directors	(101)	(144)
– Key management personnel	(5,646)	(5,894)

(e) Post-retirement benefit plans

For details of transactions with the Group's post-retirement benefit plans, please refer to note 8.

(f) Save as aforesaid, the Group has entered into other transactions in the ordinary course of business with companies where there are common directors but the amounts were immaterial.

## 32. Financial Risk Management

The Group's investment policy is to prudently invest all funds managed by the Group in a manner which will satisfy liquidity requirements, safeguard financial assets, manage risks while optimising return on investments.

The Group's activities expose it to a variety of financial risks: market risk (including foreign exchange risk and equity price risk), credit risk, liquidity risk, fair value interest rate risk and cash flow interest rate risk. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's performance.

The investment of the funds comprises three main categories: Corporate Funds (mainly share capital and retained earnings of the Group), Clearing House Funds and Margin Funds received (which exclude non-cash collateral and contributions receivable from Participants).

(a) Market risk

(i) Foreign exchange risk

Foreign exchange risk is the risk of loss due to adverse movements in foreign exchange rates relating to investments and transactions denominated in foreign currencies. When seeking to optimise the returns on its funds available for investment, the Group may invest in non-HKD securities from time to time. Forward foreign exchange contracts and foreign currency deposits have been used to hedge the currency exposure of the Group's non-HKD investments, highly probable forecast transactions and liabilities to mitigate risks arising from fluctuations in exchange rates. As at 30 September 2005, the aggregate net open foreign currency positions amounted to HK\$1,953 million, of which HK\$179 million were non-USD exposures (31 December 2004: HK\$1,996 million, of which HK\$170 million were non-USD exposures), and the total nominal value of outstanding forward foreign exchange contracts amounted to HK\$664 million (31 December 2004: HK\$358 million). All forward foreign exchange contracts would mature within two months (31 December 2004: one month).

The Group's foreign currency margin deposits received are hedged by investments in the same currencies.

During the period, the Group has designated a bank deposit of 8,500,000 Swedish Krona ("SEK") as a cash flow hedge for hedging the foreign exchange risk of forecast expenses of SEK8,500,000 from August to December 2005. The fair value of the deposit as at 30 September 2005 was \$8,531,000 (31 December 2004: \$Nil). Gains on the bank deposit remained in hedging reserve as of 30 September 2005 will be released to the profit and loss account between October to December 2005.

During the period, the Group has designated another bank deposit of SEK11,000,000 as a fair value hedge to hedge against the foreign exchange risk of a financial liability of the Group of SEK11,000,000. The fair value of the deposit as at 30 September 2005 was \$11,040,000 (31 December 2004: \$Nil).



## 32. Financial Risk Management (continued)

### (a) Market risk (continued)

#### (ii) Equity and commodity price risks

The Group is exposed to equity price risk as equities are held as part of the Corporate Fund's investments. Equity price risk is capped by an asset allocation limit. The Group is not exposed to commodity price risk as investment in commodities is not permitted under the Group's Investment Policy.

Risk management techniques, such as Value-at-Risk ("VaR") and portfolio stress testing, are used to identify, measure and control market risks. VaR measures the expected maximum loss over a given time interval (a holding period of 10 trading days is used by HKEx) at a given confidence level (95 per cent confidence interval is adopted by HKEx) based on historical data (one year is used by HKEx).

### (b) Credit risk

#### (i) Investment and accounts receivable-related risk

The Group is exposed to credit risk, which is the risk that a counterparty will be unable to pay amounts in full when due. Impairment provisions are made for losses that have been incurred at the balance sheet date. The Group limits its exposure to credit risk by rigorously selecting the counterparties (i.e. deposit-takers and issuers) and by diversification. As at 30 September 2005, all bonds held were of investment grade. Deposits are placed only with the note-issuing banks in Hong Kong, investment grade licensed banks and restricted licence banks approved by the Board from time to time. All investments are subject to a maximum concentration limit predetermined by the Board. The Group mitigates its exposure to risks relating to accounts receivables from its Participants by requiring the Participants to meet the Group's established financial requirements and criteria for admission as Participants.

#### (ii) Clearing and settlement-related off balance sheet risk

In the normal course of business, the clearing houses of the Group, HKSCC, SEOCH and HKCC, act as the counterparties to eligible trades concluded on the Stock Exchange and the Futures Exchange through the novation of the obligations of the buyers and sellers. HKSCC is also responsible for the good title to the securities deposited and accepted in the CCASS depository. As a result, the Group has considerable market risk and credit risk since the Participants' ability to honour their obligations in respect of their trades and securities deposited may be adversely impacted by economic conditions affecting the Cash and Derivatives Markets. If the Participants default on their obligations on settlement or there are defects in the title of securities deposited and accepted in the CCASS depository, the Group could be exposed to potential risks not otherwise accounted for in these accounts.



### 32. Financial Risk Management (continued)

(b) Credit risk (continued)

(ii) Clearing and settlement-related off balance sheet risk (continued)

The Group mitigates its exposure to risks described above by requiring the Participants to meet the Group's established financial requirements and criteria for admission as Participants, monitoring compliance with risk management measures such as position limits established by the Group and requiring Clearing Participants to contribute to the Clearing House Funds set up by HKSCC, SEOCH and HKCC. HKSCC also retains recourse against those Participants whose securities are deposited and accepted in the CCASS depository. Moreover, insurance has been taken out by the Group to cover the risks.

Position limits are imposed by HKCC to regulate or limit the maximum number or value of gross and net positions which can be held or controlled by the Participants based on their liquid capital. Bank guarantees may also be accepted to extend Participants' position limits. As of 30 September 2005, bank guarantees of \$1,035,400,000 were accepted (31 December 2004: \$902,500,000) for such purpose.

In addition to the above, the Group has set aside \$1,500 million of retained earnings for the purpose of strengthening the risk management regime of the clearing houses and supporting their roles as central counterparties.

(c) Liquidity risk

Due to the dynamic nature of the Group's underlying businesses, investments are kept sufficiently liquid to meet operating needs and possible liquidity requirements of the Clearing House Funds and Margin Funds. In addition, banking facilities have been put in place for contingency purposes. As at 30 September 2005, the Group's total available banking facilities amounted to \$1,608 million (31 December 2004: \$1,608 million), of which \$1,500 million were repurchase facilities to augment the liquidity of Margin Funds.

(d) Fair value and cash flow interest rate risks

Fair value interest rate risk is the risk that the value of a financial instrument will fluctuate because of changes in market interest rates. Cash flow interest rate risk is the risk that future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Group is exposed to both fair value and cash flow interest rate risks.

The table below summarises the Group's exposure to fair value interest rate risk. Included in the table were the Group's financial assets and financial liabilities whose interest rate will be reset within the buckets as shown below (categorised by the earlier of contractual repricing or maturity dates) and their related effective interest rates.

**32. Financial Risk Management (continued)**

## (d) Fair value and cash flow interest rate risks (continued)

	At 30 Sept 2005							
	Overnight \$'000	> Overnight to 1 month \$'000	> 1 month to 1 year \$'000	> 1 year to 3 years \$'000	> 3 years \$'000	Non- interest bearing \$'000	Total \$'000	Effective interest rate of interest bearing items
<b>Non-current assets</b>								
Clearing House Funds	1,468,328	49,810	154,834	99,715	–	(11,911)	1,760,776	3.75%
Compensation Fund Reserve Account	300	29,642	18,327	–	–	(10,306)	37,963	3.35%
Time deposit with maturity over one year	38,849	–	–	–	–	–	38,849	N/A *
Other non-interest bearing non-current assets	–	–	–	–	–	425,984	425,984	N/A
	<b>1,507,477</b>	<b>79,452</b>	<b>173,161</b>	<b>99,715</b>	<b>–</b>	<b>403,767</b>	<b>2,263,572</b>	
<b>Current assets</b>								
Accounts receivable, prepayments and deposits	–	–	–	–	–	5,621,805	5,621,805	N/A
Margin Funds on derivatives contracts	6,699,620	3,739,534	2,876,184	1,264,542	–	13,360	14,593,240	2.79% #
Financial assets at fair value through profit or loss	22,604	110,799	834,255	933,300	456,172	329,055	2,686,185	3.27% #
Time deposits with original maturity over three months	–	10,094	38,509	–	–	–	48,603	2.37%
Cash and cash equivalents	555,371	585,906	77,876	–	–	–	1,219,153	2.86%
Other non-interest bearing current assets	–	–	–	–	–	565	565	N/A
	<b>7,277,595</b>	<b>4,446,333</b>	<b>3,826,824</b>	<b>2,197,842</b>	<b>456,172</b>	<b>5,964,785</b>	<b>24,169,551</b>	
<b>Current liabilities</b>								
Margin deposits from Clearing Participants on derivatives contracts	14,593,240	–	–	–	–	–	14,593,240	1.47%
Accounts payable, accruals and other liabilities	263,509	–	–	–	–	5,858,410	6,121,919	1.65%
Other non-interest bearing current liabilities	–	–	–	–	–	425,233	425,233	N/A
	<b>14,856,749</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>6,283,643</b>	<b>21,140,392</b>	
<b>Non-current liabilities</b>								
Participants' contributions to Clearing House Funds	548,803	–	–	–	–	640,880	1,189,683	3.71%
Other non-interest bearing non-current liabilities	–	–	–	–	–	120,831	120,831	N/A
	<b>548,803</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>761,711</b>	<b>1,310,514</b>	
<b>Net (liabilities)/assets</b>	<b>(6,620,480)</b>	<b>4,525,785</b>	<b>3,999,985</b>	<b>2,297,557</b>	<b>456,172</b>	<b>(676,802)</b>	<b>3,982,217</b>	

\* The time deposit was a structured range accrual deposit. The effective interest rate of such deposit is not readily determinable as interest is paid only for those days where the agreed floating interest rate benchmark falls within a predetermined range.

# Excluded structured range accrual deposits and securities the effective interest rates of which were not readily determinable (Margin Funds on derivatives contracts: \$50,173,000; Financial assets at fair value through profit or loss: \$14,762,000).

32. Financial Risk Management (continued)

(d) Fair value and cash flow interest rate risks (continued)

At 31 Dec 2004

	Overnight \$'000	> Overnight to 1 month \$'000	> 1 month to 1 year \$'000	> 1 year to 3 years \$'000	> 3 years \$'000	Non- interest bearing \$'000	Total \$'000	Effective interest rate of interest bearing items
<b>Non-current assets</b>								
Clearing House Funds	1,550,359	51,060	114,321	157,858	–	(12,111)	1,861,487	0.60%
Compensation Fund Reserve Account	400	28,737	–	18,831	–	(10,517)	37,451	1.21%
Time deposit with maturity over one year	38,941	–	–	–	–	–	38,941	N/A *
Other non-interest bearing non-current assets	–	–	–	–	–	485,370	485,370	N/A
	1,589,700	79,797	114,321	176,689	–	462,742	2,423,249	
<b>Current assets</b>								
Accounts receivable, prepayments and deposits	–	–	–	–	–	4,691,846	4,691,846	N/A
Margin Funds on derivatives contracts	4,220,879	2,761,283	1,524,730	1,988,113	–	34,687	10,529,692	0.65% #
Financial assets at fair value through profit or loss	10,031	154,413	912,981	1,002,374	436,440	245,354	2,761,593	2.80%
Time deposits with original maturity over three months	–	402	938	–	–	–	1,340	0.94%
Cash and cash equivalents	541,776	465,397	27,872	–	–	–	1,035,045	0.27%
Other non-interest bearing current assets	–	–	–	–	–	639	639	N/A
	4,772,686	3,381,495	2,466,521	2,990,487	436,440	4,972,526	19,020,155	
<b>Current liabilities</b>								
Margin deposits from Clearing Participants on derivatives contracts	10,529,692	–	–	–	–	–	10,529,692	0.00%
Accounts payable, accruals and other liabilities	148,946	–	–	–	–	4,753,404	4,902,350	0.04%
Other non-interest bearing current liabilities	–	–	–	–	–	522,637	522,637	N/A
	10,678,638	–	–	–	–	5,276,041	15,954,679	
<b>Non-current liabilities</b>								
Participants' contributions to Clearing House Funds	931,427	–	–	–	–	367,325	1,298,752	0.07%
Other non-interest bearing non-current liabilities	–	–	–	–	–	137,830	137,830	N/A
	931,427	–	–	–	–	505,155	1,436,582	
<b>Net (liabilities)/assets</b>	<b>(5,247,679)</b>	<b>3,461,292</b>	<b>2,580,842</b>	<b>3,167,176</b>	<b>436,440</b>	<b>(345,928)</b>	<b>4,052,143</b>	

\* The time deposit was a structured range accrual deposit. The effective interest rate of such deposit is not readily determinable as interest is paid only for those days where the agreed floating interest rate benchmark falls within a predetermined range.

# Excluded \$50,000,000 of structured range accrual deposits the effective interest rates of which were not readily determinable.

**32. Financial Risk Management (continued)**

(d) Fair value and cash flow interest rate risks (continued)

The Group's exposure to cash flow interest rate risk is summarised below. Included in the table were the Group's floating rate interest bearing financial assets and financial liabilities whose cash flows will vary with changes in interest rates (e.g. interest income and interest expenses) and their interest rate reset dates (categorised by the earlier of contractual repricing or maturity dates).

	At 30 Sept 2005					Total \$'000
	Overnight \$'000	> Overnight to 1 month \$'000	> 1 month to 1 year \$'000	> 1 year to 3 years \$'000	> 3 years \$'000	
<b>Non-current assets</b>						
Clearing House Funds	1,468,328	–	–	–	–	1,468,328
Compensation Fund Reserve Account	300	–	–	–	–	300
Time deposit with maturity over one year	38,849	–	–	–	–	38,849
	1,507,477	–	–	–	–	1,507,477
<b>Current assets</b>						
Margin Funds on derivatives contracts	6,699,620	–	100,142	–	–	6,799,762
Financial assets at fair value through profit or loss	22,604	66,412	215,477	22,968	41,420	368,881
Cash and cash equivalents	555,371	–	–	–	–	555,371
	7,277,595	66,412	315,619	22,968	41,420	7,724,014
<b>Current liabilities</b>						
Margin deposits from Clearing Participants on derivatives contracts	14,593,240	–	–	–	–	14,593,240
Accounts payable, accruals and other liabilities	263,509	–	–	–	–	263,509
	14,856,749	–	–	–	–	14,856,749
<b>Non-current liabilities</b>						
Participants' contributions to Clearing House Funds	548,803	–	–	–	–	548,803
	548,803	–	–	–	–	548,803

**32. Financial Risk Management (continued)**

(d) Fair value and cash flow interest rate risks (continued)

	At 31 Dec 2004				
	Overnight \$'000	> Overnight to 1 month \$'000	> 1 month to 1 year \$'000	> 1 year to 3 years \$'000	Total \$'000
<b>Non-current assets</b>					
Clearing House Funds	1,550,359	–	–	–	1,550,359
Compensation Fund Reserve Account	400	–	–	–	400
Time deposit with maturity over one year	38,941	–	–	–	38,941
	1,589,700	–	–	–	1,589,700
<b>Current assets</b>					
Margin Funds on derivatives contracts	4,220,879	180,965	100,249	–	4,502,093
Financial assets at fair value through profit or loss	10,031	103,520	173,208	28,610	315,369
Cash and cash equivalents	541,776	–	–	–	541,776
	4,772,686	284,485	273,457	28,610	5,359,238
<b>Current liabilities</b>					
Margin deposits from Clearing Participants on derivatives contracts	10,529,692	–	–	–	10,529,692
Accounts payable, accruals and other liabilities	148,946	–	–	–	148,946
	10,678,638	–	–	–	10,678,638
<b>Non-current liabilities</b>					
Participants' contributions to Clearing House Funds	931,427	–	–	–	931,427
	931,427	–	–	–	931,427

### 32. Financial Risk Management (continued)

- (e) Fair values of financial assets and financial liabilities not reported at fair value

The following table summarises the carrying amounts and fair values of financial assets and financial liabilities not presented on the Group's balance sheet at their fair value. The carrying amounts of short-term receivables (i.e. accounts receivable, deposits and cash and cash equivalents) and short-term payables (i.e. accounts payable and other liabilities) approximate their fair values, and accordingly no disclosure of the fair values of these items is presented.

	Carrying amount in balance sheet		Fair value	
	At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000	At 30 Sept 2005 \$'000	At 31 Dec 2004 \$'000
<b>Financial assets</b>				
Time deposit with maturity over one year	38,849	38,941	36,640	37,808
Other financial assets included in other non-current assets (note i)	9,780	9,935	9,664	9,833
<b>Financial liabilities</b>				
Participants' admission fees received included in non-current liabilities (note i)	81,050	82,850	77,847	82,306
Participants' contributions to Clearing House Funds:				
– Minimum contributions (note i)	351,950	337,250	338,040	335,035
– Participants' additional deposits	837,733	961,502	837,733	961,502

- (i) The fair values are based on cash flows discounted using Hong Kong Government bond rates of a tenor similar to the contractual maturity of the respective assets/liabilities, adjusted by an estimated credit spread. Assets/liabilities without a contractual maturity are assumed to mature exactly one year after the balance sheet date. The discount rates used ranged from 4.12 per cent to 4.33 per cent as at 30 September 2005 (31 December 2004: 0.66 per cent to 1.30 per cent).

### 33. Comparative Figures

Other than the restatements necessitated by the changes in accounting policies adopted in the fourth quarter of 2004 as mentioned in note 1, the comparative figure of accommodation income on cash margin deposits in non-contract settlement currencies and securities deposited by Participants as alternatives to cash deposits of the Margin Funds has been reclassified from investment income to other income in order to conform with current period's presentation.

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# OTHER INFORMATION

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(Financial figures are expressed in Hong Kong Dollar)

## Share Option Schemes

On 31 May 2000, the Pre-Listing Share Option Scheme (“Pre-Listing Scheme”) and the Post-Listing Share Option Scheme (“Post-Listing Scheme”) were approved by shareholders under which the Directors of Hong Kong Exchanges and Clearing Limited (“HKEx”) may, at their discretion, offer any employee (including any executive director) of HKEx or of any of its subsidiaries, options to subscribe for shares in HKEx subject to the terms and conditions stipulated in the two schemes.

The Post-Listing Scheme was subsequently amended by shareholders on 17 April 2002 to comply with the new requirements of Chapter 17 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (“Main Board Listing Rules”) effective 1 September 2001.

As at 30 September 2005, the total number of shares available for issue, save for those granted but yet to be exercised, under the Pre-Listing Scheme and the Post-Listing Scheme, was 62,930,484 which represented about 5.92 per cent of the issued share capital of HKEx.

Details of the share options outstanding as at 30 September 2005 under the Pre-Listing Scheme and the Post-Listing Scheme were as follows:

### Pre-Listing Scheme

Date of Grant	Exercise Price	Number of shares issuable under the options granted					Exercise Period
		As at 1 January 2005	Issued upon subscription during the nine months ended 30 September 2005	Lapsed during the nine months ended 30 September 2005	As at 30 September 2005		
<b>Employees (note 1)</b>							
20 June 2000	\$6.88	6,680,000	4,446,000 (note 2)	–	2,234,000	6 March 2002 – 30 May 2010 (note 3)	

No further options can be, or have been, issued under the Pre-Listing Scheme from 27 June 2000, the date of listing of HKEx on The Stock Exchange of Hong Kong Limited (“Stock Exchange”).

## Post-Listing Scheme

Date of Grant	Exercise Price	Number of shares issuable under the options granted					Exercise Period (note 6)
		As at 1 January 2005	Granted during the nine months ended 30 September 2005	Issued upon subscription during the nine months ended 30 September 2005 (note 5)	Lapsed during the nine months ended 30 September 2005	As at 30 September 2005	
<b>Director (note 4)</b>							
2 May 2003	\$8.28	3,280,000	–	820,000	–	2,460,000	2 May 2005 – 1 May 2013
<b>Employees (note 1)</b>							
14 August 2003	\$12.45	1,094,000	–	–	–	1,094,000	14 August 2005 – 13 August 2013
18 August 2003	\$12.49	1,968,000	–	492,000	–	1,476,000	18 August 2005 – 17 August 2013
15 January 2004	\$17.30	1,094,000	–	–	–	1,094,000	15 January 2006 – 14 January 2014
31 March 2004	\$16.96	5,582,000	–	–	352,000	5,230,000	31 March 2006 – 30 March 2014
17 May 2004	\$15.91	200,000	–	–	–	200,000	17 May 2006 – 16 May 2014
26 January 2005	\$19.25 (note 7)	–	5,884,000	–	268,000	5,616,000	26 January 2007 – 25 January 2015

No option granted under these two share option schemes was cancelled during the nine months ended 30 September 2005.

## Notes:

- Employees working under employment contracts that were regarded as “continuous contracts” for the purpose of the Employment Ordinance of Hong Kong.
- The weighted average closing price immediately before the dates on which the options were exercised was \$20.57.
- Options granted are exercisable between 6 March 2002 and 30 May 2010, in tranches of 25 per cent each reaching 100 per cent as from 6 March 2005.
- The option was granted to Mr Chow Man Yiu, Paul, a Director and the Chief Executive of HKEx.
- The weighted average closing price immediately before the dates on which the options were exercised was \$20.88.
- Options granted are subject to a vesting scale in tranches of 25 per cent each per annum starting from the second anniversary and fully vested in the fifth anniversary of the date of grant.
- The closing price immediately before the date of grant was \$19.05.
- HKEx has used the Binomial Option Pricing Model for estimating the fair value of options issued under the Post-Listing Scheme. The assumptions used in the calculation are:
  - Risk-free rate of return – the yield of 10-year Exchange Fund Notes
  - Expected volatility of share price – annualised volatility for 1 year immediately preceding the grant date
  - Expected dividend yield – annual dividend (excluding special dividend) of the most recent financial year and the closing price on grant date



*The amount written off to the profit and loss account for the nine months ended 30 September 2005 was \$17,254,000 (30 September 2004: \$10,096,000).*

*According to the Binomial Option Pricing Model, the value of the option granted on 26 January 2005 was \$26,183,800. For details, please refer to note 23 to the condensed consolidated accounts.*

*The Binomial Option Pricing Model was developed to estimate the fair value of American style options. It is one of the commonly used models to estimate the fair value of an option which can be exercised before the expiry of the option period. The value of an option varies with different variables of certain subjective assumptions. Any change in variables so adopted may materially affect the estimation of the fair value of an option.*

## **Employees' Share Award Scheme**

On 14 September 2005 ("Adoption Date"), the Board of HKEx adopted an Employees' Share Award Scheme ("the Scheme") in which all employees (including without limitation any executive directors) of HKEx and its subsidiaries ("Group") will be entitled to participate. The purposes and objectives are to recognise the contributions by certain employees of the Group and to give incentive to them in order to retain them for the continual operation and development of the Group, and to attract suitable personnel for further development of the Group. Unless early terminated by the Board of HKEx, the Scheme shall be valid and effective for a term of 15 years commencing on the Adoption Date provided that no contribution to the trust fund will be made by HKEx on or after the 10th anniversary date of the Adoption Date. Details of the Scheme were announced by HKEx on the Adoption Date.

Pursuant to the rules relating to the Scheme, the Board of HKEx or the trustee of the Scheme (as the case may be) shall select the employees of the Group for participation in the Scheme, and determine the number of shares of HKEx to be awarded. Relevant number of shares awarded will be acquired by the trustee from the market at the cost of HKEx and be held in trust for those selected employees until the end of each vesting period. Awarded shares and the related income derived therefrom are subject to a vesting scale in tranches of 25 per cent each on every anniversary date starting from the second anniversary date of the date of award until the fifth. Vested shares will be transferred at no cost to the relevant selected employees of HKEx.

Throughout the duration of the Scheme, the aggregate number of shares which may be awarded is limited to three per cent of the shares of HKEx in issue as at the Adoption Date, i.e. a total of 31,871,575 shares. The maximum number of shares which may be awarded to a selected employee under the Scheme shall not exceed one per cent of the shares of HKEx in issue as at the Adoption Date, i.e. 10,623,858 shares. No shares have ever been awarded under the Scheme since its adoption.

The Board has decided that, after adoption of the Scheme, no further options will be granted under the existing Post-Listing Scheme.

The rules and the trust deed relating to the Scheme are posted on HKEx's corporate website.

## Directors' and Chief Executive's Interests and Short Positions

As at 30 September 2005, the Directors, the Chief Executive and their respective associates had the following interests in the shares and underlying shares of HKEx, as recorded in the register maintained by HKEx pursuant to Section 352 of the Securities and Futures Ordinance ("SFO"):

Name of Director	Number of Shares / Underlying Shares Held				Total	% of Issued Share Capital
	Personal Interests	Family Interests	Corporate Interests	Other Interests		
Chow Man Yiu, Paul	3,280,000 (note 1)	–	–	–	3,280,000	0.31
Lee Jor Hung, Dannis	–	–	1,610,000 (note 2)	–	1,610,000	0.15
John Estmond Strickland	18,000 (note 3)	–	–	–	18,000	0.00
David Michael Webb	2 (note 4)	2 (note 5)	6 (note 6)	–	10	0.00

Notes:

1. Mr Chow, a Director and the Chief Executive of HKEx, has beneficial interests in 820,000 shares, and 2,460,000 underlying shares in respect of the share option granted to him pursuant to the Post-Listing Scheme on 2 May 2003. The said option is exercisable between 2 May 2005 and 1 May 2013 at an exercise price of \$8.28 per share. The number of shares issuable under the option granted and the exercise price had been adjusted in accordance with the resolution passed by shareholders at the annual general meeting held in 2004.
2. 1,610,000 shares were owned by DL Brokerage Limited, a private company beneficially wholly-owned by Mr Lee.
3. The shares were held by Mr Strickland as beneficial owner.
4. The shares were held by Mr Webb as beneficial owner.
5. The shares were owned by the spouse of Mr Webb.
6. The shares were owned by Fundamental Consultants Limited, Member One Limited and Member Two Limited which are under the control of Mr Webb.

Other than the holdings disclosed above, no interests and short positions were held or deemed or taken to be held under Part XV of the SFO by any Director or the Chief Executive of HKEx or their respective associates in the shares, underlying shares and debentures of HKEx or any of its associated corporations (within the meaning of Part XV of the SFO) which were required to be notified to HKEx and the Stock Exchange pursuant to Part XV of the SFO or pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers ("Model Code") or which are required pursuant to Section 352 of the SFO to be entered in the register referred to therein. Nor any of the Directors and the Chief Executive (including their spouses and children under the age of 18) had, as at 30 September 2005, any interest in, or had been granted any right to subscribe for the securities and options of HKEx and its associated corporations within the meaning of the SFO, or had exercised any such rights.

## **Disclosable Interests and Short Positions of Shareholders under the SFO**

As at 30 September 2005, the Directors are not aware of any party who was directly or indirectly interested in five per cent or more of the issued share capital of HKEx, as recorded in the register required to be kept by HKEx under Section 336 of the SFO.

## **Minority Controllers**

Under Section 61 of the SFO, no person shall be or become a Minority Controller, i.e. a person who either alone or with any associate or associates, is entitled to exercise, or control the exercise of five per cent or more of the voting power at any general meeting of the recognised exchange controller, except with the approval in writing of the Securities and Futures Commission (“SFC”) after consultation with the Financial Secretary.

The SFC has so far granted approval to five entities to be Minority Controllers of HKEx, on the basis that the shares are held by them in custody for their clients.

As at 30 September 2005, the Minority Controllers were in aggregate holding 64.81 per cent of the issued share capital of HKEx (30 September 2004: 52.51 per cent).

## **Corporate Governance**

HKEx applied the principles and complied with all requirements set out in the Code on Corporate Governance Practices (“CG Code”) contained in Appendix 14 of the Main Board Listing Rules, with certain deviations from code provisions A.4.1 and A.4.2 in respect of the service term and rotation of Directors, throughout the review period.

The code provisions A.4.1 and A.4.2 provide that (a) non-executive directors should be appointed for specific terms, subject to re-election, and (b) all directors appointed to fill casual vacancy should be subject to election by shareholders at the first general meeting after their appointment, and every director, including those appointed for a specific term, should be subject to retirement by rotation at least once every three years. Details of the deviations were set out in the Corporate Governance Report of HKEx’s 2004 Annual Report issued in March 2005.

To ensure stricter compliance with the CG Code, relevant amendments to the Articles of Association were proposed and approved by shareholders at the annual general meeting held in 2005 (“2005 AGM”) and subsequently approved by the SFC on 18 April 2005 pursuant to Section 67 of the SFO.

Following the effectiveness of the amendments to the Articles of Association, and shareholders’ resolutions passed at the 2005 AGM, HKEx fully complies with the CG Code.

On 7 November 2005, HKEx was awarded the 2005 HKMA Best Annual Reports Awards – Bronze Award in “General” Category organised by the Hong Kong Management Association. HKEx, as the regulator and a public company, will continue its commitment to articulate and maintain high standards of corporate governance.

In addition, the FTSE4Good Policy Committee has confirmed that HKEx has met the FTSE4Good selection criteria and become a member of the FTSE4Good Index Series effective from September 2005.

The FTSE4Good Index Series is produced by FTSE Group, and has been designed to identify companies that are working towards environmental sustainability, developing positive relationships with stakeholders and upholding and supporting universal human rights. Being selected a member of the FTSE4Good Index Series shows investors and other stakeholders HKEx's commitment to responsible business practice, and delivers a strong message to investors that HKEx meets globally recognised corporate social responsibility standards.

### **Compliance with the Model Code**

HKEx has adopted the Model Code as set out in Appendix 10 to the Main Board Listing Rules. All Directors have confirmed, following specific enquiry by HKEx, that they fully complied with the Model Code throughout the review period.

### **Review of Accounts**

The Audit Committee has reviewed the Group's unaudited condensed consolidated financial statements for the nine months ended 30 September 2005 in conjunction with HKEx's external auditors.

Management has appointed the external auditors to carry out certain agreed-upon procedures in accordance with Hong Kong Standards on Related Services 4400 "Engagements to perform agreed-upon procedures regarding financial information" issued by the Hong Kong Institute of Certified Public Accountants on the unaudited condensed consolidated financial statements for the nine months ended 30 September 2005.

### **Purchase, Sale or Redemption of HKEx's Listed Securities**

During the nine months ended 30 September 2005, HKEx had not redeemed, and neither HKEx nor any of its subsidiaries had purchased or sold any of HKEx's listed securities.

By Order of the Board  
**Hong Kong Exchanges and Clearing Limited**  
**Lee Yeh Kwong, Charles**  
*Chairman*

Hong Kong, 9 November 2005

## **Hong Kong Exchanges and Clearing Limited**

12/F, One International Finance Centre, 1 Harbour View Street, Central, Hong Kong

Tel: +852 2522 1122

Fax: +852 2295 3106

Website: [www.hkex.com.hk](http://www.hkex.com.hk)

Email: [info@hkex.com.hk](mailto:info@hkex.com.hk)