

Interim Report > 2003



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





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Financial Highlights

(Financial figures are expressed in Hong Kong dollars)

	Unaudited Six months ended 30 Jun 2003 \$ million	Unaudited and restated Six months ended 30 Jun 2002 \$ million	Change
RESULTS			
Income	907	892	2%
Operating expenses	661	577	14%
Operating profit	246	315	(22%)
Share of profits less losses of associated companies	3	1	329%
Profit before taxation	249	316	(21%)
Taxation	(35)	(27)	29%
Profit attributable to shareholders	214	289	(26%)
Shareholders' funds	5,278	5,490#	(4%)
Total assets*	13,384	14,035 ϕ	(5%)
Earnings per share	\$0.205	\$0.277	(26%)
Interim dividend declared per share	\$0.18	\$0.08	125%
Dividend payout ratio	88%	29%	

* The Group's total assets include the margin funds received from Participants on futures and options contracts.

Audited and restated (down by \$6 million) as at 31 December 2002 due to the implementation of the new SSAP 12: Income Taxes

ϕ Audited as at 31 December 2002

Financial Highlights

	Unaudited Six months ended 30 Jun 2003	Unaudited Six months ended 30 Jun 2002	Change
KEY MARKET STATISTICS			
Average daily turnover value on the Stock Exchange	\$7.1 billion	\$7.6 billion	(7%)
Average daily number of derivatives contracts traded on the Futures Exchange	39,099	27,825	41%
Average daily number of stock options contracts traded on the Stock Exchange	14,614	14,618	0%



Corporate Information

BOARD OF DIRECTORS

Non-executive Chairman

LEE Yeh Kwong, Charles GBS, JP*

Executive Director, Chief Executive

CHOW Man Yiu, Paul JP (joined on 1 May 2003)

KWONG Ki Chi GBS, JP (retired on 15 April 2003)

Non-executive Directors

CHAN Cho Chak, John GBS, JP* (retired on 15 April 2003)

FAN Chor Ho, Paul JP (retired on 15 April 2003)

FONG Hup* (appointment effective on 16 April 2003)

FRESHWATER, Timothy George*

KWOK Chi Piu, Bill

LEE Jor Hung, Dannis BBS

LEE Kwan Ho, Vincent Marshall

LEONG Ka Chai JP*

LIU Jinbao* (resigned on 28 May 2003)

LO Ka Shui GBS, JP*

SETO Gin Chung, John (retired on 15 April 2003)

STRICKLAND, John Estmond GBS, JP (retired on 15 April 2003 as a Public Interest Director and appointed by the Board on 16 April 2003)

WARD, Rodney Gordon* (retired on 15 April 2003)

WEBB, David Michael (elected on 15 April 2003)

WONG Sai Hung, Oscar (elected on 15 April 2003)

YUE Wai Keung (retired on 15 April 2003)

* Public Interest Directors

Corporate Information

EXECUTIVE COMMITTEE

LEE Yeh Kwong, Charles (Chairman)
CHOW Man Yiu, Paul
LEE Jor Hung, Dannis
LEONG Ka Chai

AUDIT COMMITTEE

STRICKLAND, John Estmond (Chairman)
FONG Hup (Deputy Chairman)
LEE Kwan Ho, Vincent Marshall
WEBB, David Michael

INVESTMENT ADVISORY COMMITTEE

FRESHWATER, Timothy George (Chairman)
WONG Sai Hung, Oscar (Deputy Chairman)
WEBB, David Michael

RISK MANAGEMENT COMMITTEE

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

LEE Yeh Kwong, Charles (Chairman)
DICKENS, Mark**
KWOK Chi Piu, Bill
LAM Kin**
LAU James H. Jr**
LEONG Ka Chai**
WONG Tung-shun, Peter**

** Appointed by the Financial Secretary under
Section 65 of the Securities and Futures
Ordinance

REMUNERATION COMMITTEE

LO Ka Shui (Chairman)
LEE Jor Hung, Dannis
LEE Kwan Ho, Vincent Marshall

NOMINATION COMMITTEE

LEE Yeh Kwong, Charles (Chairman)
LO Ka Shui
WONG Sai Hung, Oscar

COMPANY SECRETARY

MAU Kam Shing, Joseph

AUTHORISED REPRESENTATIVES

CHOW Man Yiu, Paul
MAU Kam Shing, Joseph

AUDITORS

PricewaterhouseCoopers

LEGAL ADVISORS

Allen & Overy

REGISTERED OFFICE

12th Floor
One International Finance Centre
1 Harbour View Street
Central
Hong Kong

Shareholder Information

WEBSITE

<http://www.hkex.com.hk>

E-MAIL ADDRESS

info@hkex.com.hk

REGISTRAR AND TRANSFER OFFICE

Hong Kong Registrars Limited

1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East

Wanchai, Hong Kong

FINANCIAL CALENDAR

Information on results announcement 2003

Announcement of first quarter results	14 May 2003
Announcement of interim results	13 August 2003
Ex-dividend date for interim dividend	5 September 2003
Book closing dates for interim dividend	9-11 September 2003
Record date for interim dividend	11 September 2003
Payment date for interim dividend	on or about 15 September 2003
Announcement of third quarter results	November 2003
Announcement of final results for the year ending 31 December 2003	March 2004

SHARE INFORMATION

Stock Code

Stock Exchange, Hong Kong	388
Access to Reuters	0388.HK
Access to Bloomberg	388 HK Equity

Board lot	2,000 shares
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Price and Turnover History

2003	Price per Share		Turnover (in millions)	
	High (HK\$)	Low (HK\$)	Shares	HK\$
January	10.50	9.15	62.2	620.5
February	9.50	8.60	85.6	770.0
March	9.60	8.30	117.4	1,060.7
April	9.25	7.60	98.4	840.6
May	10.45	8.95	107.8	1,036.4
June	11.80	10.30	111.4	1,235.8

Shareholder Information

Analysis of Shareholdings

(Shareholdings as at 30 June 2003)

Size of holding	Number of shareholders	% of shareholders	Number of shares ('000)	% of total issued capital
1 – 1,000	16	1.0%	6	0.0%
1,001 – 5,000	759	49.5%	2,143	0.2%
5,001 – 10,000	364	23.8%	3,026	0.3%
10,001 – 100,000	238	15.5%	7,511	0.7%
100,001 and above	156	10.2%	1,034,269	98.8%
Total	1,533	100.0%	1,046,955	100.0%

Category	Number of shares ('000)	% of total issued capital
Individual ¹	105,649	10.1%
<i>Local</i>	<i>102,681</i>	<i>9.8%</i>
<i>Overseas</i>	<i>2,968</i>	<i>0.3%</i>
Corporate ²	16,084	1.5%
Institutions ³	532,977	50.9%
<i>Local</i>	<i>31,176</i>	<i>3.0%</i>
<i>Overseas</i>	<i>501,801</i>	<i>47.9%</i>
Exchange Participants ⁴	275,410	26.3%
Other nominees/banks ⁵	116,835	11.2%
Total	1,046,955	100.0%

Composition of shareholders according to a survey conducted as at 30 June 2003

¹ Shares registered in individual names other than those who are Exchange Participants

² Shares registered in company names other than those who are Exchange Participants and nominees/banks

³ Institutional investors identified by the six major custodians and HKSCC Nominees Limited

⁴ Exchange Participants include Stock Exchange Participants and Futures Exchange Participants

⁵ Other nominees/banks excluding HKSCC Nominees Limited and the six major custodians

Review of Operations

(Financial figures are expressed in Hong Kong dollars)

Hong Kong Exchanges and Clearing Limited (HKEx) reported unaudited net profits for the six months ended 30 June 2003 of \$214 million (2002: \$289 million). The directors have resolved to pay an interim dividend of \$0.18 per share (2002: \$0.08). The share register will be closed on Tuesday, 9 September 2003 to Thursday, 11 September 2003 inclusive and dividend warrants will be despatched to shareholders on or about Monday, 15 September 2003.

Market sentiment in the first six months of 2003 was adversely affected by poor economic conditions in Hong Kong stemming from the onset of the Severe Acute Respiratory Syndrome (SARS), rising unemployment, continuing property market weakness and slow growth overseas. Average daily turnover on The Stock Exchange of Hong Kong Limited (Stock Exchange) decreased by 7 per cent compared with that of the same period last year. Average daily volume of futures and options contracts traded on the Stock Exchange and the Hong Kong Futures Exchange Limited (Futures Exchange) increased by 27 per cent compared with that of the same period last year. Both averages have an effect on HKEx's results.

In the six months to 30 June 2003, HKEx continued to focus on improving the quality of its markets, increasing the efficiency of its operations, and providing products and services that meet the needs of market participants.

Markets

Securities Market

Average daily turnover value on the Stock Exchange during the period under review was \$7.1 billion, compared with \$7.6 billion during the same period in 2002. A total of 16 new equity issues were listed on the Main Board, including three by companies formerly listed on the Growth Enterprise Market (GEM), and 12 were listed on GEM. In the first half of 2002, there were 34 new equity listings on the Main Board, including two by companies formerly listed on GEM, and 28 on GEM. Capital formation through initial public offering and post issue fund raising totalled \$134.9 billion on the Main Board and \$972 million on GEM, compared with a total of \$25.7 billion on the Main Board and \$3.8 billion on GEM in the first half of 2002.

Derivatives Market

The average daily number of futures and options contracts traded on the Stock Exchange and the Futures Exchange during the first six months of 2003 was 53,713 contracts, up from 42,443 in the first six months of 2002. Total open interest at the end of June 2003 was 537,185 contracts, compared with 671,967 at the end of June 2002.

Review of Operations

Developments since the Report for the Quarter to 31 March 2003

HKEx has started reporting its results on a quarterly basis. As a result, the following section highlights developments since the completion of the Report for the Quarter to 31 March 2003.

Listing Matters

On 30 May 2003, the Stock Exchange and the Securities and Futures Commission (SFC) jointly published their Consultation Paper on Regulation of Sponsors and Independent Financial Advisers (IFAs) to seek the views of market participants on proposals to reinforce the regulatory regime for sponsors, underwriters and IFAs, and to seek comments on issues involving other financial intermediaries. Seminars held by HKEx and the SFC for issuers and market practitioners to discuss the proposals were well attended. The consultation period ended at the close of business on 31 July 2003. The results are being compiled and analysed to help determine the way forward on the proposals.

The Stock Exchange distributed revised guidance on new listing applications to sponsors in early June. It applies to new applications submitted on or after 16 June 2003. The guidance provides a non-exhaustive list of potential issues which should be raised with the Listing Unit and sets out the checklists, information and documentary requirements applicable at each stage of the vetting process. The guidance is aimed at assisting sponsors in orderly submission of the information required so that listing applications can be assessed on a timely basis.

Market Development and Operations

The Stock Exchange will seek market participants' views on proposals to narrow its trading spreads by publishing a consultation paper later this year.

The Stock Exchange narrowed the strike intervals for options on HSBC Holdings and on Hang Seng Bank for the spot and next calendar months by 50 per cent with effect from 30 April 2003. In light of the positive market response, the narrowing of the strike intervals for other stock option classes is being considered.

The Futures Exchange suspended trading in International Stock Futures and Options (ISFO) after the market closed on 29 May 2003. The suspension followed a review of HKEx's product portfolio. Reviews are conducted from time to time to ensure that products meet the needs and demands of the market in a cost efficient manner.

The Futures Exchange and the Shanghai Futures Exchange have formed a working group comprising representatives from both organisations to look into the possibility of developing an Asian energy derivatives market. A study on a market and clearing model is now in progress.

Review of Operations

The Stock Exchange has been discussing the possible introduction of Capital Protected Instruments (CPI) under Chapter 15A of its Listing Rules with potential issuers. CPI offer investors a degree of capital protection along with potential gains based on the performance of designated assets. The Stock Exchange and the Futures Exchange are also studying the possible introduction of other products, including cash-settled Three-Year Exchange Fund Note Futures and Interest Rate Swap Futures.

Clearing

The final phase of CCASS/3, the upgraded Central Clearing and Settlement System (CCASS), was introduced on 26 May 2003 with the rollout of the Participant Gateway. The Participant Gateway serves as an additional communication channel to the CCASS/3 Terminal and provides a direct electronic interface between CCASS/3 and CCASS Participants' back office systems to facilitate straight-through processing. CCASS Participants may subscribe for the use of the Participant Gateway according to their requirements.

Market views will be sought in the coming months on a proposed model for an upgraded version of the Investor Participant account in CCASS and the technical details of the scripless model to be implemented. HKEx will continue to discuss with market participants the possible introduction of Third Party Clearing in the securities market, which was first discussed in a July 2002 consultation paper.

Corporate Treasury

The Corporate Treasury manages funds amounting to about \$9.24 billion, comprising mainly accumulated operating profits, Clearing House Funds, and margin funds received. Investment income represents approximately 20 per cent of HKEx's total income.

Investments are kept sufficiently liquid to meet operating and possible requirements of the Clearing House Funds and margin funds. As at 30 June 2003, 49 per cent of funds were invested in highly liquid investment-grade bonds, 50 per cent in cash or bank deposits and 1 per cent in global equities. The maturity profile of the investments as at 30 June 2003 was as follows:

Overnight	>Overnight to 1 month	>1 month to 1 year	>1 year to 3 years	>3 years
38%	8%	12%	32%	10%

Review of Operations

Credit exposure was well diversified. All bonds held were of investment grade and had a weighted average credit rating of Aa2 and a weighted average maturity of 2.3 years. Deposits were placed with the note-issuing banks in Hong Kong or financial institutions with a minimum credit rating of A3 which are approved by the Board from time to time.

Investment and fund management is governed by guidelines approved by the Board, aimed at optimising return, safeguarding assets and satisfying liquidity requirements. A professional Treasury team in Corporate Treasury is dedicated to the day-to-day management and investment of the funds. External fund managers have also been appointed to manage part of the Corporate Funds.

An Investment Advisory Committee, comprising non-Executive Directors of the Board and external members from the financial community, advises HKEx on portfolio management and monitors the risk and performance of its investments.

Risk management techniques, such as Value-at-Risk (VaR) and portfolio stress testing, are used to identify, measure, monitor and control market risks. For the first half year of 2003, the overall portfolio risk, as measured by the VaR methodology, recorded an average, maximum and minimum VaR of \$21 million, \$26 million and \$18 million respectively.

China Development and Listing Promotion

HKEx has been granted approval to establish a representative office in Beijing under the Mainland and Hong Kong Closer Economic Partnership Arrangement (CEPA) signed on 29 June 2003. The representative office will be opened upon completion of the application process, anticipated to be in the fourth quarter of this year.

As part of ongoing efforts to provide potential listing candidates with a greater understanding of the requirements for listing in Hong Kong, HKEx arranged two August 2003 conferences on the Mainland, one in Guangzhou, the capital of Guangdong province, and one in Fuzhou, the capital of Fujian province.

SARS

There were no SARS-related interruptions to the trading, clearing, or business operations of HKEx and its subsidiaries (the Group).

Review of Operations

Board of Directors

Dr Liu Jinbao tendered his resignation as a Non-executive Director with effect from 28 May 2003 due to personal reasons. He was one of the six Non-executive Directors appointed by the Government to represent public and market interests to the Board.

Reorganisation

As part of continuing efforts to rationalise HKEx's operations and further strengthen its competitiveness, a new organisation structure has been put in place. The main changes involved the Exchange Business Unit and the Listing, Regulation and Risk Management Unit.

Outlook for the Remainder of the Financial Year

The outlook for the remainder of the year depends on the performance of the markets operated by HKEx. Market sentiment and the factors that influence it will continue to affect the results of the Group. Investor confidence remains fragile due to weak economic conditions in Hong Kong and overseas despite recent increases in trading activities in the cash and derivatives markets.

HKEx will continue to review its operations to ensure that they are efficient. Stringent cost controls remain in place and effects of the measures will be reflected in future results. The Group will seek to further improve the quality of its markets to attract more investors. The Group will also encourage more fund-raising activities on the Stock Exchange, strengthen its position among the world's equity markets and maintain its role as the prime international capital formation centre for enterprises from Mainland China.

I was very fortunate to succeed Mr Kwong Ki-chi as the Chief Executive of HKEx. I must express my deepest appreciation to Mr Kwong for having made HKEx into an internationally respected organisation despite its short history. He has also left me with a team of dedicated, professional and quality staff. I am confident that by working together under the leadership of the Board of Directors we can successfully build on the foundation in place and continue to flourish.

Paul Chow

Chief Executive

Hong Kong, 13 August 2003

Management Discussion and Analysis

(Financial figures are expressed in Hong Kong dollars)

OVERALL PERFORMANCE

The Group recorded a profit attributable to shareholders of \$214 million for the interim period (2003 first quarter: \$89 million; 2003 second quarter: \$125 million), compared with \$289 million for the same period in 2002 (2002 first quarter: \$118 million; 2002 second quarter: \$171 million). The \$75 million or 26 per cent decrease in profit was mainly attributable to one-off items not expected to recur in the near future, which included a write-down of strategic investments (\$33 million), retirement of redundant IT systems (\$10 million), and severance costs (\$9 million) following the recent review of the Group's business strategy and operations. Taxation rose despite a lower profit before taxation as a result of the increase in Hong Kong Profits Tax rate announced in the March 2003 Hong Kong Budget and a one-off increase in deferred tax charge (\$6 million) following the implementation of a new accounting standard which became effective on 1 January 2003. In addition, IT and computer maintenance expenses and depreciation increased further by \$20 million mainly due to the roll-out of the upgraded Central Clearing and Settlement System (CCASS/3) in mid-2002.

Had the above-mentioned one-off costs (\$52 million less tax deduction of \$1 million) and deferred tax charge not been incurred, profit attributable to shareholders for the interim period would have been \$271 million, which would be 6 per cent (\$18 million) lower than the corresponding period last year.

Income

Total income (including share of profits less losses of associated companies) for the period increased by 2 per cent to \$910 million (2002: \$893 million).

Hong Kong's economy during the period was adversely affected by the slow growth in the global economy, onset of the Severe Acute Respiratory Syndrome (SARS), rising unemployment and weakening property market. Although trading volume has picked up in the second quarter, the decline in the earlier part of this year has led to a 7 per cent drop in the average daily turnover on The Stock Exchange of Hong Kong Limited (Stock Exchange) to \$7.1 billion compared with the corresponding period last year. In spite of this, trading fees and trading tariff rose by \$18 million or 11 per cent to \$185 million (2002: \$167 million). This was due to a 41 per cent increase in the average daily number of derivatives contracts traded on Hong Kong Futures Exchange Limited (Futures Exchange), mainly on account of an increase in the trading of Hang Seng Index (HSI) Futures contracts, which has more than offset the reduction in trading fees from cash market activities.

Management Discussion and Analysis

Listing fee income fell by 3 per cent to \$160 million (2002: \$165 million), primarily because of a drop in the number of new listings of derivative warrants from 385 to 216. New listings of derivative warrants in the first half of 2002 were exceptionally high, as investment banks were competing to issue new derivative warrants to meet pent-up demand since there were virtually no new issues for six months before the Listing Rules for derivative warrants were amended to streamline the listing procedures towards the end of 2001. The reduction in income was partly offset by initial listing fees forfeited for increased numbers of lapsed and withdrawn initial public offering (IPO) applications and approved IPOs not listed within six months of application. New listings on the Main Board and the Growth Enterprise Market (GEM) declined by 53 per cent and 57 per cent respectively as IPOs, especially for Mainland enterprises, had been put on hold due to poor market sentiment. As at 30 June 2003, 12 Main Board and 9 GEM (31 December 2002: 13 Main Board and 7 GEM) IPO applications had obtained approval in principle from the Listing Committee for listing, and 31 Main Board and 45 GEM applications were under processing (31 December 2002: 35 Main Board and 72 GEM). As at 30 June 2003, there were 824 companies listed on the Main Board and 175 on GEM (31 December 2002: 812 and 166 respectively).

In line with the decline in cash market activities, clearing and settlement fee income dropped by 4 per cent to \$92 million (2002: \$96 million).

Income from sale of information decreased by 20 per cent to \$126 million (2002: \$159 million), due to the consolidation of broking firms and lower demand for stock information.

Depository, custody and nominee services fee income increased by 8 per cent to \$95 million (2002: \$87 million), mostly due to higher scrip fee income for the period.

Total investment income increased by 32 per cent to \$178 million (2002: \$135 million), predominantly due to a net realised gain of \$29 million (2002: loss of \$5 million) and net unrealised mark-to-market gain of \$27 million (2002: loss of \$7 million) on the investment portfolio.

For the six months ended 30 June 2003, the average amount of funds available for investment achieved a positive return of 3.79 per cent (2002: 2.96 per cent). The portfolio recorded a spread of 266 basis points above the 6-month Hong Kong Exchange Fund Bill benchmark, which was higher than the 110 basis points spread achieved in 2002.

Management Discussion and Analysis

The average amount of funds available for investment increased by 3 per cent to \$9.2 billion, primarily attributable to a rise in additional contributions to the Clearing House Funds and margin funds received from Clearing Participants on account of increased trading in futures and options contracts. As at 30 June 2003, 49 per cent of funds were invested in highly liquid investment-grade bonds, 50 per cent in cash or bank deposits and 1 per cent in global equities. As the valuation of our investments in bonds and equities is highly influenced by movements in their market prices, unrealised gains or losses may fluctuate or reverse unless the investments are sold.

Investments are kept sufficiently liquid to meet operating and possible requirements of the Clearing House Funds and margin funds. The maturity profile of the investments as at 30 June 2003 was as follows:

	> Overnight to 1 month	> 1 month to 1 year	> 1 year to 3 years	> 3 years
Overnight	8%	12%	32%	10%

Operating Expenses

Total operating expenses increased by 14 per cent to \$661 million (2002: \$577 million).

Staff costs and related expenses increased by 2 per cent to \$267 million (2002: \$262 million), largely due to one-off severance costs (\$9 million) incurred following the recent reorganisation and streamlining of the Group's operations and such costs are not expected to recur in the near future. The Group will continue to streamline its operations to further raise its efficiency.

Due to HKEx's commitment to constantly enhance the capability and resilience of its trading and settlement systems, information technology and computer maintenance expenses rose by 4 per cent from \$132 million to \$137 million, mainly attributable to expenditures relating to the maintenance of CCASS/3.

Premises expenses fell by 14 per cent to \$43 million (2002: \$50 million) as lower rental was negotiated upon the renewal of certain leases.

Legal and professional fees for the period increased by \$15 million to \$21 million (2002: \$6 million), primarily as a result of professional fees incurred for several one-off consulting projects during the period and for projects brought forward from last year.

Management Discussion and Analysis

Depreciation and amortisation costs increased by 19 per cent to \$93 million (2002: \$78 million), mostly due to the additional depreciation charge arising from the roll-out of CCASS/3 in mid-2002.

Other operating expenses rose by \$50 million to \$91 million (2002: \$41 million), mainly attributable to one-off items not expected to recur in the near future, which included a 100 per cent (\$32 million) write-down of the Group's investment in BondsInAsia Limited and the retirement of redundant IT systems (\$10 million) following the review of its business strategy and operations in May 2003. As the economy continued to deteriorate, significant provision for doubtful debts (\$4 million) was required as listed companies and Participants experienced difficulties in settling their fees. Further, due to the sharp decline in property prices this year, the devaluation of one of the Group's properties has resulted in a charge (\$4 million) to the profit and loss account for the first time.

Taxation

The Group's taxation charge rose by \$8 million to \$35 million (2002: \$27 million), principally by reason of a \$3 million increase arising from the hike in Hong Kong Profits Tax rate from 16 per cent to 17.5 per cent announced in the March 2003 Hong Kong Budget, and the reversal in 2002 of \$5 million of overprovision. The \$3 million increase was primarily due to a one-off increase in deferred tax charge (\$6 million) as, under the new Hong Kong Statement of Standard Accounting Practice (SSAP) 12: Income Taxes, effective from 1 January 2003, outstanding deferred tax liabilities carried forward from 2002 (calculated at the 16 per cent tax rate in 2002) have to be recomputed in 2003 by using the higher rate of 17.5 per cent.

Liquidity, Financial Resources and Capital Commitments

Working capital decreased by 2 per cent to \$4,109 million as at 30 June 2003 (31 December 2002: \$4,207 million), primarily due to a decrease of listing fees receivable in accounts receivable, prepayments and deposits. Bank balances and time deposits of corporate funds increased by \$284 million to \$1,269 million (31 December 2002: \$985 million). Although the Group has consistently been in a very liquid position, credit facilities have nevertheless been put in place for contingency purposes. As at 30 June 2003, the Group's total available credit facilities amounted to \$2,762 million (31 December 2002: \$2,763 million), of which \$1,500 million were repurchase facilities to augment the liquidity of the margin funds and \$1,100 million were for meeting the Group's Continuous Net Settlement money obligations of Hong Kong Securities Clearing Company Limited (HKSCC) in the Central Clearing and Settlement System (CCASS) in circumstances where Broker Participants in CCASS default on their payment obligations. Borrowings of the Group have been very rare and, if required, are mostly

Management Discussion and Analysis

event driven, with little seasonality. As at 30 June 2003, the only facility drawn down was a fixed rate bank loan of SGD11 million (equivalent to HK\$49 million) with a maturity of less than one year which was used for the purpose of hedging the currency exposure of the Group's investment in Singapore (2002: SGD11 million, equivalent to HK\$49 million). The loan will be renewed annually.

As at 30 June 2003, the Group's gearing ratio, measured on the basis of total borrowings as a percentage of total shareholders' equity, was less than one per cent (31 December 2002: less than one per cent).

As at 30 June 2003, the Group's capital expenditure commitments, mainly in respect of its ongoing investments in facilities and technology amounted to \$91 million (31 December 2002: \$94 million). The Group has adequate financial resources to fund its commitments on capital expenditures from its existing cash resources and cash flows generated from its operations.

As at 30 June 2003, 97 per cent of the Group's cash and cash equivalents (comprise cash in hand, bank balances and time deposits within three months of maturity when acquired) were denominated in Hong Kong dollars (HKD) and United States dollars (USD).

Charges on Assets

The Group did not have any charges on assets as at 30 June 2003 and 31 December 2002.

Significant Investments Held and Material Acquisitions and Disposals of Subsidiaries

The Group has been holding 1 per cent (10 million shares) of the issued ordinary share capital of Singapore Exchange Limited since November 2000, 5,854 Class A ordinary shares of BondsInAsia Limited since April 2002, and 24 per cent of Computershare Hong Kong Investor Services Limited and 30 per cent of ADP Wilco Processing Services Limited (formerly known as Wilco International Processing Services Limited) since May 2002.

During the period, the Group has written down 100 per cent (\$32 million) of the value of its investment in BondsInAsia Limited, and 21 per cent (\$0.4 million) of investment in ADP Wilco Processing Services Limited to the Group's share of the net assets of this associated company due to impairment.

There were no material acquisitions or disposals of investments and subsidiaries during the period.

Management Discussion and Analysis

Exposure to Fluctuations in Exchange Rates and Related Hedges

When seeking to optimise returns on its funds available for investment, the Group may invest in non-HKD securities from time to time. Forward foreign exchange contracts or foreign currency credit facilities may be used to hedge the currency exposure of the Group's non-HKD investments to mitigate risks arising from fluctuations in exchange rates. As at 30 June 2003, aggregate net open foreign currency positions amounted to \$1,578 million, of which HK\$257 million were non-USD exposures (31 December 2002: HK\$1,924 million, of which HK\$200 million were non-USD exposures). The Group's foreign currency liabilities, in the form of margin deposits or collateral received, are hedged by investments in the same currencies.

Contingent Liabilities

The Unified Exchange Compensation Fund (Compensation Fund) is a fund set up under the repealed Securities Ordinance (SO) for the purpose of compensating any person dealing with a Stock Exchange Participant (other than another Stock Exchange Participant) for any pecuniary losses suffered as a result of a default of 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, with the approval of the Securities and Futures Commission (SFC), allow an additional payment to the successful claimants before apportionment. Under section 107(1) of the SO, the Stock Exchange has contingent liabilities to the Compensation Fund as it shall replenish the Compensation Fund upon the SFC's request to do so. 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. Under the Securities and Futures Ordinance (SFO) which came into effect on 1 April 2003, all these provisions shall continue to apply to any default occurring before that date despite the repeal of the SO. As at 30 June 2003, there were outstanding claims received in respect of 13 defaulted Stock Exchange Participants (31 December 2002: 14).

Pursuant to the SFO, the Stock Exchange issued a notice on 3 April 2003 inviting for claims against the Compensation Fund in relation to any default of a Stock Exchange Participant occurring before 1 April 2003. The claims period will expire on 3 October 2003. As at 30 June 2003, no claims have been received in response to that notice.

Management Discussion and Analysis

Under the new compensation arrangements implemented under the SFO, a new Investor Compensation Fund has replaced the existing Compensation Fund, the Commodity Exchange Compensation Fund and the Dealers' Deposit Schemes for non-exchange participant dealers. The new arrangements would not require Exchange Participants to make deposits to the Investor Compensation Fund. Existing deposits would be returned to the Stock Exchange and the Futures Exchange in accordance with the provisions of the SFO. The arrangements would remove the requirement for the Stock Exchange to replenish the Investor Compensation Fund.

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 default of any one Participant. In the unlikely event that all of its 447 trading Participants as at 30 June 2003 (31 December 2002: 471) default, the maximum contingent liability of the Stock Exchange under the indemnity will amount to \$89 million (31 December 2002: \$94 million).

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.

Employees

HKEx has developed its human resources policies and procedures based on performance and merit. The Group ensures that the pay levels of its employees are competitive and employees are rewarded on a performance-related basis within the general framework of the Group's salary and bonus system.

Share options may be granted to Executive Directors and employees of the Group to subscribe for shares in HKEx in accordance with the terms and conditions of the Post-Listing Share Option Scheme approved by the shareholders of HKEx at an extraordinary general meeting held on 31 May 2000.

Management Discussion and Analysis

Following the merger of the businesses of the Stock Exchange Group, the Futures Exchange Group and the HKSCC Group in 2000, HKEx has succeeded in streamlining its workforce and the number of employees fell from 1,052 (including 88 full-time and part-time contract staff) prior to the merger to 819 (including 51 full-time contract staff) as at 30 June 2003. For the two semi-annual periods under review, total employees' cost increased by 2 per cent to \$267 million (2002: \$262 million), mainly due to one-off severance costs incurred following the recent reorganisation and streamlining of the Group's operations.

PROSPECTS

As a substantial part of HKEx's income is derived from trading fees, clearing and settlement fees, listing fees and interest income, the performance of the Group is heavily influenced by external factors including, in particular, market sentiment, the level of activity on the Stock Exchange and Futures Exchange, and movements in interest rates.

The slow economic growth in the US and the sluggish economies in Europe and Japan are still deterring investors from actively participating in the securities and derivatives markets. Although activity in the cash and derivatives markets in Hong Kong has increased recently, investor confidence is still fragile owing to the lingering fiscal deficit, continuing deflation, the depressed property market and record unemployment.

The Expert Group appointed by the Government to review the operation of the securities and futures market regulatory structure recommended on 21 March 2003 various market reform measures, including the transfer of the listing function on a bottom-line neutral basis from the Group to the SFC. A public consultation will be conducted on the recommendations and the Government expects this exercise to be started in the third or fourth quarter of 2003 and concluded in early 2004. HKEx will work closely with the Government and the SFC in this process.

HKEx strongly supports the introduction of appropriate reform measures to improve market quality. Improved market quality will lead to a stronger market to the benefit of HKEx as well as the Hong Kong public. HKEx has urged that more powers be granted to statutory regulators, and that heavier penalties be imposed on rule-breakers. Such measures would improve the quality of corporate information disclosure and offer better protection to investors, including minority shareholders. To reduce market irregularities and the violation of shareholder and investor interests, Hong Kong needs to turn the parts of the Listing Rules dealing with post-listing ongoing disclosure obligations, price-sensitive information disclosure and connected transaction disclosure into law, backed by effective statutory sanctions enforced by a statutory regulator such

Management Discussion and Analysis

as the SFC. However, market rules dealing with products, operations and development should continue to be administered by HKEx as the market operator. HKEx will work closely with the Government and the SFC to develop the best model for the Hong Kong stock market.

HKEx will focus its resources on projects that will create value for shareholders and market users. It will continue to raise the quality and efficiency of its markets to increase their competitiveness. The capability and reliability of HKEx's trading and clearing systems will be further enhanced. It will pursue initiatives to attract more investors and capital raising companies to Hong Kong. New financial products and services will be introduced to meet investor needs and diversify the Group's revenue base. It will maintain stringent controls on costs and continue to review and streamline its operations to further enhance efficiency, and it will strive to ensure that the effects of such measures will be reflected in future results.

Following China's accession to the World Trade Organisation, an increasing number of private enterprises from the Mainland are planning to raise capital by listing in Hong Kong. The Closer Economic Partnership Arrangement (CEPA) signed in June 2003 is expected to eliminate substantial trade and investment barriers between Hong Kong and the Mainland. HKEx will focus its efforts on making Hong Kong the premier international capital market for Mainland enterprises and facilitating promotion of such enterprises to international investors. Approval has been granted to HKEx to establish a representative office in Beijing under CEPA. This will enable HKEx to provide quicker and better services to potential issuers on the Mainland in order to attract more new listings to Hong Kong. Large-scale road shows are being planned to promote our services to prospective listing candidates from the Mainland.

The Group has recently reorganised its corporate structure to better position itself to seize future opportunities. With Hong Kong's proximity to and close relationship with China, HKEx is best placed to be the key international capital market for Mainland and Hong Kong enterprises. Given Hong Kong's advantages of location and time zone, the extensive use of the English language, and the practice of the common law, HKEx is an ideal bridge between the Asia-Pacific region and financial markets in Europe and North America. HKEx will continue to develop its markets as the Asian time-zone pillar in the global securities and derivatives markets, as well as the preferred Asian partner for major equities and derivatives exchanges seeking to build global alliances.

Condensed Consolidated Profit and Loss Account

(Financial figures are expressed in Hong Kong dollars)

	Note	Unaudited Six months ended 30 Jun 2003 \$'000	Unaudited and restated Six months ended 30 Jun 2002 \$'000
INCOME			
Trading fees and trading tariff	4	184,509	166,932
Stock Exchange listing fees		160,059	165,007
Clearing and settlement fees		92,312	96,402
Depository, custody and nominee services fees		94,593	87,216
Income from sale of information		126,253	158,538
Investment income	5	178,290	135,008
Other income	6	71,032	83,486
	3	907,048	892,589
OPERATING EXPENSES			
Staff costs and related expenses		266,861	262,336
Information technology and computer maintenance expenses		137,453	131,612
Premises expenses		42,833	49,881
Product marketing and promotion expenses		3,342	7,803
Legal and professional fees		20,991	6,031
Depreciation and amortisation		93,025	78,382
Payment to SFC under dual filing regime		5,000	-
Other operating expenses	7	91,186	41,109
		660,691	577,154
OPERATING PROFIT	3	246,357	315,435
SHARE OF PROFITS LESS LOSSES OF ASSOCIATED COMPANIES	3	3,263	760
PROFIT BEFORE TAXATION	3	249,620	316,195
TAXATION	3/8	(35,234)	(27,403)
PROFIT ATTRIBUTABLE TO SHAREHOLDERS	3	214,386	288,792
DIVIDEND			
Earnings per share	9	\$0.205	\$0.277
Interim dividend declared per share		\$0.18	\$0.08
Dividend payout ratio		88%	29%

Condensed Consolidated Statement of Changes in Equity

(Financial figures are expressed in Hong Kong dollars)

	Note	Unaudited Six months ended 30 Jun 2003 \$'000	Unaudited and restated Six months ended 30 Jun 2002 \$'000
Total equity at 1 Jan, as previously reported		5,496,392	5,235,407
Effect of adopting SSAP 12	1	(6,028)	(2,853)
Total equity at 1 Jan, as restated		5,490,364	5,232,554
Change in valuation of investment property		(200)	(1,500)
Change in valuation of other properties		(8,271)	(8,245)
Change in fair value of non-trading securities		6,636	5,672
Deferred tax arising from change in valuation of other properties	1	763	1,318
Deferred tax arising from change in fair value of non-trading securities	1	199	(517)
Net deficits not recognised in the condensed consolidated profit and loss account		(873)	(3,272)
Profit attributable to shareholders		214,386	288,792
Realisation of change in fair value of non-trading securities on maturity and disposal		(2,357)	(540)
2002/2001 final dividend		(448,740)	(260,166)
Dividend on shares issued for employee share options exercised after declaration of 2001 final dividend		–	(448)
Dividend on shares issued for employee share options exercised after declaration of 2002 final dividend		(647)	–
Proceeds from issue of shares under employee share option schemes	18	25,373	18,514
Total equity at 30 Jun		5,277,506	5,275,434

Condensed Consolidated Balance Sheet

(Financial figures are expressed in Hong Kong dollars)

	Note	Unaudited at 30 Jun 2003 \$'000	Audited and restated at 31 Dec 2002 \$'000
NON-CURRENT ASSETS			
Fixed assets	10	649,965	748,108
Investments in associated companies	11	32,931	35,536
Clearing House Funds	12	1,403,371	980,748
Compensation Fund Reserve Account	13	36,511	35,827
Cash and Derivatives Market Development Fund	14	923	914
Non-trading securities maturing over one year		60,667	87,604
Deferred tax assets	1	1,117	–
		2,185,485	1,888,737
CURRENT ASSETS			
Margin funds on derivatives contracts	15	4,932,473	4,551,601
Accounts receivable, prepayments and deposits	16	1,756,545	3,118,199
Taxation recoverable		222	1,774
Trading securities		3,240,670	3,490,046
Bank balances and time deposits		1,269,010	985,114
		11,198,920	12,146,734
CURRENT LIABILITIES			
Bank loans		48,711	49,456
Margin deposits and securities received from			
Clearing Participants on derivatives contracts	15	4,932,473	4,551,601
Accounts payable, accruals and other liabilities	16	1,882,983	3,007,392
Participants' admission fees received		2,450	3,350
Deferred revenue		151,402	269,774
Taxation payable		46,516	29,051
Provisions	17	25,108	28,863
		7,089,643	7,939,487
NET CURRENT ASSETS		4,109,277	4,207,247
TOTAL ASSETS LESS CURRENT LIABILITIES		6,294,762	6,095,984

Condensed Consolidated Balance Sheet

	Note	Unaudited at 30 Jun 2003 \$'000	Audited and restated at 31 Dec 2002 \$'000
NON-CURRENT LIABILITIES			
Participants' admission fees received		86,050	86,800
Participants' contributions to Clearing House Funds	12	840,602	425,440
Deferred tax liabilities	1	70,565	73,281
Provisions	17	20,039	20,099
		1,017,256	605,620
NET ASSETS			
		5,277,506	5,490,364
CAPITAL AND RESERVES			
Share capital	18	1,046,955	1,043,581
Share premium	18	41,011	19,012
Revaluation reserves	19	26,669	29,899
Designated reserves	20	694,454	727,811
Retained earnings	21	3,279,965	3,221,321
Proposed and declared dividend	21	188,452	448,740
SHAREHOLDERS' FUNDS			
		5,277,506	5,490,364

Condensed Consolidated Cash Flow Statement

(Financial figures are expressed in Hong Kong dollars)

	Note	Unaudited Six months ended 30 Jun 2003 \$'000	Unaudited and restated Six months ended 30 Jun 2002 \$'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Net cash inflow/(outflow) from operating activities	22(a)	707,092	(3,864)
CASH FLOWS FROM INVESTING ACTIVITIES			
Payments for purchases of fixed assets		(29,355)	(81,591)
Proceeds from sales of fixed assets		76	78
Payments for purchases of non-trading securities		–	(24,191)
Decrease/(increase) in time deposits with original maturity more than three months		59,768	(224,399)
Net cash outflow from investments in associated companies and disposal of a subsidiary		–	(42,446)
Dividends received from an associated company		2,400	–
Dividends received from non-trading securities		1,049	964
Interest received from non-trading securities		19,712	20,624
Realised gain on sale of non-trading securities of specific funds	22(c)	6,586	1,901
Repayment of loan receivable from an associated company		2,000	–
Net cash inflow/(outflow) from investing activities		62,236	(349,060)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from issue of shares under employee share option scheme		25,373	18,514
Admission fees received less refunds to Participants		(1,650)	(11,750)
Dividend paid		(449,387)	(260,614)
Net cash outflow from financing activities		(425,664)	(253,850)
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS			
Cash and cash equivalents at 1 Jan		679,956	1,351,964
Cash and cash equivalents at 30 Jun	22(b)	1,023,620	745,190

Notes to the Condensed Consolidated Accounts

(Financial figures are expressed in Hong Kong dollars)

1. Basis of Preparation and Accounting Policies

These unaudited condensed consolidated interim accounts are prepared in accordance with Hong Kong Statement of Standard Accounting Practice (SSAP) 25: Interim Financial Reporting, issued by the Hong Kong Society of Accountants (HKSA).

These condensed consolidated interim accounts should be read in conjunction with the 2002 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 2002 except that the Group has adopted the new SSAP 12: Income Taxes, issued by the HKSA, which is effective for accounting periods commencing on or after 1 January 2003. The effects of the change to the Group's accounting policies are set out below.

Under the new SSAP 12, deferred taxation is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the accounts. Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised. Tax rates enacted or substantively enacted by the balance sheet date are used to determine deferred tax assets and liabilities. As a result, deferred tax assets and liabilities in 2002 are computed using a tax rate of 16 per cent and deferred tax assets and liabilities in 2003 using the higher tax rate of 17.5 per cent announced in the March 2003 Hong Kong Budget. As outstanding deferred tax liabilities carried forward from 2002 have to be recomputed at the higher tax rate in 2003, the change in tax rate has resulted in an increase in deferred tax liabilities of which \$6,040,000 was absorbed as an additional deferred tax charge in the first half of 2003.

The new SSAP 12 has been applied retrospectively and comparatives presented have been restated to conform to the changed policy. As a result, total deferred tax liabilities as at 31 December 2001 and 2002 increased by \$2,853,000 (with a corresponding reduction of \$5,369,000 in revaluation reserves and an increase of \$2,516,000 in retained earnings) and \$6,028,000 (with a corresponding reduction of \$4,081,000 in revaluation reserves and reduction of \$1,947,000 in retained earnings) respectively. Therefore, as detailed in note 21 to the accounts, opening retained earnings at 1 January 2002 and 2003 have increased by \$2,516,000 and decreased by \$1,947,000 respectively. The change has reduced the profit for the year ended 31 December 2002 by \$4,463,000 (from \$592,968,000 to \$588,505,000).

Notes to the Condensed Consolidated Accounts

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:

	Six months ended 30 Jun 2003 (unaudited)				Group
	Cash Market	Derivatives Market	Clearing Business	Others	
Income	437,615	138,660	206,341	124,432	907,048
Costs	213,091	72,615	149,182	–	434,888
Segment results	224,524	66,045	57,159	124,432	472,160
Unallocated costs					225,803
Operating profit					246,357
Share of profits less losses of associated companies	35	–	3,228	–	3,263
Profit before taxation					249,620
Taxation					(35,234)
Profit attributable to shareholders					214,386

Notes to the Condensed Consolidated Accounts

3. Segment Information (continued)

Six months ended 30 Jun 2002 (unaudited and restated)					
\$'000					
	Cash Market	Derivatives Market	Clearing Business	Others	Group
Income	476,784	118,519	215,187	82,099	892,589
Costs	195,596	60,300	118,607	-	374,503
Segment results	281,188	58,219	96,580	82,099	518,086
Unallocated costs					202,651
Operating profit					315,435
Share of profits less losses of associated companies	-	-	760	-	760
Profit before taxation					316,195
Taxation					(27,403)
Profit attributable to shareholders					288,792

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. The major sources of income of the business are trading fees, trading tariff, listing fees and income from sale of information.

Notes to the Condensed Consolidated Accounts

3. Segment Information (continued)

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

The **Clearing Business** refers mainly 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 interests earned on the Clearing House Funds and the fees charged on providing clearing, settlement, depository and nominee services.

Income under the **Others Segment** represents mainly investment income derived from corporate funds, which is not directly attributable to any of the three business segments and is therefore not allocated to the business segments. Unallocated costs represent overheads which are not directly attributable to the above-mentioned business segments.

4. Trading Fees and Trading Tariff

	Unaudited Six months ended 30 Jun 2003 \$'000	Unaudited Six months ended 30 Jun 2002 \$'000
Trading fees and trading tariff are derived from:		
Securities and options traded on the Stock Exchange	106,914	116,350
Derivatives contracts traded on the Futures Exchange	77,595	50,582
	184,509	166,932

Notes to the Condensed Consolidated Accounts

5. Investment Income

	Unaudited Six months ended 30 Jun 2003 \$'000	Unaudited Six months ended 30 Jun 2002 \$'000
Interest income	120,284	147,285
Interest expense	(969)	(2,466)
Net interest income	119,315	144,819
Non-interest investment income		
Dividends and net realised gain/(loss) on trading and non-trading securities	32,464	(2,366)
Net unrealised gain/(loss) on trading securities	26,511	(7,445)
Total investment income	178,290	135,008

6. Other Income

	Unaudited Six months ended 30 Jun 2003 \$'000	Unaudited Six months ended 30 Jun 2002 \$'000
Stock Exchange network and terminal user fees	42,116	33,084
Participants' subscription and application fees	18,543	20,586
Share registration services fees	727	13,394
Miscellaneous income	9,646	16,422
	71,032	83,486

Notes to the Condensed Consolidated Accounts

7. Other Operating Expenses

	Unaudited Six months ended 30 Jun 2003 \$'000	Unaudited Six months ended 30 Jun 2002 \$'000
Write-down of strategic investments (note a)	32,667	–
Retirement of redundant IT systems	9,846	2
Impairment of other property–revaluation deficit	4,411	–
Provision for/(reversal of provision for) doubtful debts	3,574	(137)
Insurance	5,984	4,525
Financial data subscription fees	4,504	4,319
Custodian and fund management fees	4,238	4,322
Other miscellaneous expenses	25,962	28,078
	91,186	41,109

(a) Includes a 100 per cent write-down (\$32,303,000) of the Group's investment in BondsInAsia Limited under non-trading securities following a recent review of the group's business strategy and operations.

8. Taxation

Taxation in the condensed consolidated profit and loss account represents:

	Unaudited Six months ended 30 Jun 2003 \$'000	Unaudited and restated Six months ended 30 Jun 2002 \$'000
Provision for Hong Kong Profits Tax (note a)	37,352	32,932
Overprovision in respect of prior years	–	(5,229)
	37,352	27,703
Deferred taxation (note b)	(2,871)	(459)
	34,481	27,244
Share of taxation of associated companies	753	159
	35,234	27,403

Notes to the Condensed Consolidated Accounts

8. Taxation (continued)

- (a) Hong Kong Profits Tax has been provided for at 17.5 per cent (2002: 16 per cent) on the estimated assessable profit for the period.
- (b) As explained in note 1, under the new SSAP 12, deferred tax assets and liabilities in 2002 are computed using a tax rate of 16 per cent and deferred tax assets and liabilities in 2003 using the higher tax rate of 17.5 per cent announced in the March 2003 Hong Kong Budget. Deferred taxation for 2003 includes a one-off deferred tax charge of \$6,040,000, which arose from recomputing outstanding deferred tax liabilities carried forward from 2002 using the higher tax rate of 17.5 per cent.

9. Earnings Per Share

The calculation of basic earnings per share is based on the profit attributable to shareholders of \$214,386,000 (2002: \$288,792,000) and the weighted average of 1,044,626,393 shares (2002: 1,041,861,730) in issue during the six-month period.

The employee share options outstanding as set out in note 18 did not have a material dilutive effect on the basic earnings per share.

10. 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. The total cost of additions to fixed assets of the Group during the six months to 30 June 2003 was \$17,811,000 (2002: \$81,591,000) of which \$15,858,000 (2002: \$66,494,000) or 89 per cent (2002: 81 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 six months to 30 June 2003 were \$164,823,000 and \$10,048,000 respectively (2002: \$2,177,000 and \$47,000).

Notes to the Condensed Consolidated Accounts

11. Investments in Associated Companies

	Unaudited at 30 Jun 2003 \$'000	Audited at 31 Dec 2002 \$'000
Share of net assets of associated companies	9,313	8,215
Goodwill on acquisition of shares in associated companies less amortisation (note a)	23,618	25,321
	32,931	33,536
Loan receivable from an associated company (note b)	–	2,000
	32,931	35,536

(a) Goodwill

	\$'000
Cost	
At 1 Jan 2003 and 30 Jun 2003	26,889
Accumulated amortisation and impairment	
At 1 Jan 2003	1,568
Charge for the period	1,339
Impairment loss	364
At 30 Jun 2003	3,271
Net book value	
At 30 Jun 2003	23,618
At 31 Dec 2002	25,321

Goodwill is amortised on a straight-line basis over 10 years.

Notes to the Condensed Consolidated Accounts

11. Investments in Associated Companies (continued)

(b) The loan was unsecured with interest payable semi-annually at prime rate per annum and was repaid before its maturity date of 31 May 2004.

(c) Details of the unlisted associated companies as at 30 June 2003 are as follows:

Name	Place of incorporation	Principal activities	Particulars of shares held	Interest held
Computershare Hong Kong Investor Services Limited	Hong Kong	Provision of share registration services	5,854 Class A ordinary shares	24%
ADP Wilco Processing Services Limited (formerly known as Wilco International Processing Services Limited)	Hong Kong	Provision of transaction processing services to Stock Exchange Participants	6 Class B ordinary shares	30%

ADP Wilco Processing Services Limited has an accounting year end of 30 June, which is not coterminous with the Group's accounting year end.

Notes to the Condensed Consolidated Accounts

12. Clearing House Funds

	Unaudited at 30 Jun 2003 \$'000	Audited at 31 Dec 2002 \$'000
Net asset values of the Clearing House Funds are as follows:		
HKSCC Guarantee Fund	371,377	372,352
SEOCH Reserve Fund	132,420	134,185
HKCC Reserve Fund	899,574	474,211
	1,403,371	980,748
Net assets of the Clearing House Funds are composed of:		
Unlisted non-trading securities, at fair value		
– debt securities	216,139	155,688
Contributions receivable from Participants	50,160	31,490
Bank balances and time deposits	1,152,593	806,401
	1,418,892	993,579
Less: Other liabilities	(15,521)	(12,831)
	1,403,371	980,748
The Clearing House Funds are funded by:		
Clearing Participants' contributions	840,602	425,440
Clearing houses' contributions	320,200	320,200
Accumulated investment income net of expenses included in designated reserves attributable to:		
– Clearing Participants' contributions	180,935	176,643
– Clearing houses' contributions	59,789	58,465
Revaluation reserve (note 19)	1,845	–
	1,403,371	980,748

Notes to the Condensed Consolidated Accounts

12. Clearing House Funds (continued)

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.

In prior years, temporary fluctuations in fair value of investments were reflected in the assets and investment revaluation reserve of the Group. As at 31 December 2002, the aggregate cost and market value of the funds were \$980,748,000 and \$983,526,000 respectively.

13. Compensation Fund Reserve Account

The Securities and Futures Commission (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:

- (a) 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;
- (b) Amounts received or paid out in relation to each of the Stock Exchange Trading Rights granted or revoked by the Stock Exchange respectively; and
- (c) Amounts reserved for the replenishment of the Compensation Fund.

The Compensation Fund is further explained in note 25(a).

Notes to the Condensed Consolidated Accounts

14. Cash and Derivatives Market Development Fund (CDMD Fund)

The CDMD Fund was established by the cash received from The Hong Kong Futures Guarantee Corporation Limited (the former clearing house of the Futures Exchange) for the purpose of providing funding for the development and betterment of the cash and derivatives markets in Hong Kong.

15. Margin Funds on Derivatives Contracts

	Unaudited at 30 Jun 2003 \$'000	Audited at 31 Dec 2002 \$'000
The margin funds comprise:		
SEOCH Clearing Participants' margin funds	792,434	757,333
HKCC Clearing Participants' margin funds	4,140,039	3,794,268
	4,932,473	4,551,601
The assets of the margin funds comprise:		
Bank balances and time deposits	2,430,041	2,148,753
Listed securities deposited as alternatives to cash deposits, at market value	1,046,474	1,119,682
Margin receivable from Clearing Participants	–	3,198
Listed non-trading securities, at fair value		
– debt securities	102,602	173,907
Unlisted non-trading securities, at fair value		
– money market fund	86,710	162,484
– debt securities	1,266,646	943,577
	4,932,473	4,551,601
The Group's liabilities in respect of the margin funds are as follows:		
Margin deposits and securities received from SEOCH and HKCC Participants on derivatives contracts	4,932,473	4,551,601

Notes to the Condensed Consolidated Accounts

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

The Group's accounts receivable, prepayments and deposits and accounts payable, accruals and other liabilities amounted to \$1,756,545,000 (31 December 2002: \$3,118,199,000) and \$1,882,983,000 (31 December 2002: \$3,007,392,000) respectively. These mainly represent the Group's CNS money obligations under the T+2 settlement cycle. The Group's CNS money obligations receivable represent 85 per cent (31 December 2002: 85 per cent) of the total accounts receivable, prepayments and deposits. CNS money obligations payable represent 76 per cent (31 December 2002: 88 per cent) of the total accounts payable, accruals and other liabilities. CNS money obligations mature within two days as they are due for settlement two days after the trade date. The majority of the remaining accounts receivable, prepayments, deposits, accounts payable, accruals and other liabilities will mature within three months.

17. Provisions

	Reinstatement costs \$'000	Employee benefit costs \$'000	Total \$'000
At 1 Jan 2003	25,136	23,826	48,962
Provision for the period	-	13,083	13,083
Amount used during the period	-	(12,335)	(12,335)
Amount paid during the period	(301)	(4,262)	(4,563)
At 30 Jun 2003	24,835	20,312	45,147

	Unaudited at 30 Jun 2003 \$'000	Audited at 31 Dec 2002 \$'000
Analysis of provisions:		
Current	25,108	28,863
Non-current	20,039	20,099
	45,147	48,962

Notes to the Condensed Consolidated Accounts

18. Share Capital and Share Premium

	Unaudited at 30 Jun 2003 \$'000	Audited at 31 Dec 2002 \$'000
Authorised: 2,000,000,000 shares of \$1 each	2,000,000	2,000,000

Issued and fully paid:

	No. of shares of \$1 each	Share capital \$'000	Share premium \$'000	Total \$'000
At 1 Jan 2002	1,040,664,846	1,040,665	–	1,040,665
Shares issued under employee share option schemes	2,916,000	2,916	19,012	21,928
At 31 Dec 2002	1,043,580,846	1,043,581	19,012	1,062,593
Shares issued under employee share option schemes	3,374,000	3,374	21,999	25,373
At 30 Jun 2003	1,046,954,846	1,046,955	41,011	1,087,966

Under the Pre-Listing Share Option Scheme of HKEx, share options were granted to employees on 20 June 2000 which are exercisable between 6 March 2002 and 30 May 2010 at an exercise price of \$7.52 per share.

Under the Post-Listing Share Option Scheme of HKEx, share options were granted to an executive director on 2 May 2003 which are exercisable between 2 May 2005 and 1 May 2013 at an exercise price of \$9.05 per share.

During the period, Pre-Listing employee share options were exercised to subscribe for 3,374,000 shares (year ended 31 December 2002: 2,916,000) in HKEx at a consideration of \$7.52 per share, of which \$1.00 per share was credited to share capital and the balance of \$6.52 per share was credited to the share premium account.

Notes to the Condensed Consolidated Accounts

18. Share Capital and Share Premium (continued)

Movements of the employee share options during the period were as follows:

	Number of shares issuable under the employee share options outstanding as at 1 Jan 2003	Number of employee share options lapsed	Number of employee share options granted	Number of employee share options exercised	Number of shares issuable under the employee share options outstanding as at 30 Jun 2003
Pre-Listing Share Option Scheme	23,253,020	(2,007,513)	-	(3,374,000)	17,871,507
Post-Listing Share Option Scheme	-	-	3,000,000	-	3,000,000
	23,253,020	(2,007,513)	3,000,000	(3,374,000)	20,871,507

No specific accounting guidance has been issued by the HKSA on the accounting for employee share options. In November 2002, the International Accounting Standards Board (IASB) published an exposure draft, ED2: Share-based Payment, which covers the accounting treatment for employee share options. The exposure draft is expected to be finalised as an International Financial Reporting Standard (IFRS) in the fourth quarter of 2003.

In line with other countries/regions (e.g., USA, European Union, etc), Hong Kong is working towards harmonising its accounting standards with those issued by the IASB. The HKSA has announced that, following IASB's issuance of an IFRS on share-based payment, it intends to recommend the adoption of a new SSAP so that the SSAPs maintain conformity with the IASB standards.

When the employee share options are exercised and new shares are issued, the share capital is increased by the nominal value of the new shares issued and the share premium account is increased by the remainder of the proceeds. HKEx has not expensed the employee share options to the profit and loss account. Had all the outstanding employee share options been fully exercised on 30 June 2003, the Group would have received \$161,543,733 in proceeds. The market value of the shares issued based on the closing price of \$11.20 per share on that date was \$233,760,878. The employees concerned under the Pre-Listing Share Option Scheme would have made a gain of \$3.68 per share, or, in aggregate, \$65,767,146. The executive director concerned under the Post-Listing Share Option Scheme would have made a gain of \$2.15 per share, or, in aggregate, \$6,450,000.

Notes to the Condensed Consolidated Accounts

19. Revaluation Reserves

	Unaudited at 30 Jun 2003 \$'000	Audited and restated at 31 Dec 2002 \$'000
Investment properties revaluation reserve	1,571	1,771
Other properties revaluation reserve	6,734	14,242
Investment revaluation reserve (note b)	18,364	13,886
	26,669	29,899

(a) The revaluation reserves are segregated for their respective specific purposes.

(b) Includes \$1,845,000 (31 December 2002: \$Nil) which is attributable to investments of the Clearing House Funds.

20. Designated Reserves

	Unaudited at 30 Jun 2003 \$'000	Audited at 31 Dec 2002 \$'000
Clearing House Funds reserves		
– HKSCC Guarantee Fund reserve	255,912	255,912
– SEOCH Reserve Fund reserve	48,182	47,185
– HKCC Reserve Fund reserve	256,830	252,211
	560,924	555,308
Compensation Fund Reserve Account reserve	36,218	35,827
CDMD Fund reserve	914	914
Development reserve	96,398	135,762
	694,454	727,811

These reserves are segregated for their respective purposes.

Notes to the Condensed Consolidated Accounts

21. Retained Earnings

	Note	Unaudited at 30 Jun 2003 \$'000	Audited and restated at 31 Dec 2002 \$'000
At 1 Jan			
Retained earnings, as previously reported		3,223,268	3,198,763
Effect of adopting SSAP 12	1	(1,947)	2,516
Retained earnings, as restated		3,221,321	3,201,279
Proposed and declared dividend		448,740	260,166
Profit for the period/year		214,386	588,505
Investment income net of expenses of Clearing House Funds for the period/year transferred to Clearing House Funds reserves		(5,616)	(35,114)
Investment income net of expenses of Compensation Fund Reserve Account for the period/year transferred to Compensation Fund Reserve Account reserve		(391)	(681)
Transfer from Development reserve		39,364	-
Dividends paid:			
2001 final dividend		-	(260,166)
2002 final/interim dividend		(448,740)	(83,450)
Dividend on shares issued for employee share options exercised after declaration of 2001 final dividend		-	(448)
Dividend on shares issued for employee share options exercised after declaration of 2002 interim dividend		-	(30)
Dividend on shares issued for employee share options exercised after declaration of 2002 final dividend		(647)	-
At 30 Jun/31 Dec		3,468,417	3,670,061
Representing:			
Retained earnings		3,279,965	3,221,321
Proposed and declared dividend		188,452	448,740
At 30 Jun/31 Dec		3,468,417	3,670,061

Notes to the Condensed Consolidated Accounts

22. Notes to the Condensed Consolidated Cash Flow Statement

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

	Unaudited Six months ended 30 Jun 2003 \$'000	Unaudited and restated Six months ended 30 Jun 2002 \$'000
Profit before taxation	249,620	316,195
Adjustments for:		
Net interest income	(119,315)	(144,819)
Dividends received from non-trading securities	(1,049)	(964)
(Gain)/loss on trading securities and exchange differences on investments	(33,530)	12,009
Gain on non-trading securities	(6,586)	(1,901)
Depreciation and amortisation	93,025	78,382
Impairment of non-trading securities	32,303	-
Impairment of investments in associated companies	364	-
Impairment of other property	4,411	-
Changes in provisions	(3,815)	(155)
Share of profits less losses of associated companies	(3,263)	(760)
Loss on retirement of redundant IT systems	9,846	2
Loss on disposal of other fixed assets	126	15
Operating profit before working capital changes	222,137	258,004
Net decrease/(increase) in trading securities	300,709	(106,270)
Settlement of amount transferred from retained earnings to Clearing House Funds and Compensation Fund Reserve Account	(6,007)	(4,892)
Decrease in accounts receivable, prepayments and deposits	1,366,924	108,345
Decrease in other current liabilities	(1,266,083)	(360,146)
Net cash inflow/(outflow) from operations	617,680	(104,959)
Interest received from banks and trading securities	109,286	117,455
Interest paid	(1,539)	(3,330)
Hong Kong Profits Tax paid	(18,335)	(20,117)
Refund of Hong Kong Profits Tax	-	7,087
Net cash inflow/(outflow) from operating activities	707,092	(3,864)

Notes to the Condensed Consolidated Accounts

22. Notes to the Condensed Consolidated Cash Flow Statement (continued)

(b) Analysis of cash and cash equivalents

	Unaudited Six months ended 30 Jun 2003 \$'000	Unaudited Six months ended 30 Jun 2002 \$'000
Time deposits with original maturity within three months	975,468	668,221
Cash at bank and in hand	48,152	76,969
Cash and cash equivalents at 30 Jun	1,023,620	745,190

- (c) The net assets in Clearing House Funds, Compensation Fund Reserve Account, CDMD Fund 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 do not constitute any cash or cash equivalent transactions to the Group except for the investment income net of expenses of these funds which has been accounted for as the Group's assets and profit.

23. Commitments

	Unaudited at 30 Jun 2003 \$'000	Audited at 31 Dec 2002 \$'000
Commitments in respect of capital expenditures:		
Contracted but not provided for	17,234	36,454
Authorised but not contracted for	73,512	57,170
	90,746	93,624

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

Notes to the Condensed Consolidated Accounts

24. Financial Risk Management

When seeking to optimise returns on its funds available for investment, the Group may invest in non-HKD securities from time to time. Forward foreign exchange contracts are used to hedge the currency exposures of the Group's non-HKD investments to mitigate risks arising from fluctuations in exchange rates. As at 30 June 2003, the total nominal value of outstanding forward foreign exchange contracts amounted to HK\$259 million (31 December 2002: HK\$197 million). All contracts will mature within three months.

25. Contingent Liabilities

- (a) The Compensation Fund is a fund set up under the repealed SO for the purpose of compensating any person dealing with a Stock Exchange Participant (other than another Stock Exchange Participant) for any pecuniary losses suffered as a result of a default of 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, with the approval of the SFC, allow an additional payment to the successful claimants before apportionment. Under section 107(1) of the SO, the Stock Exchange has contingent liabilities to the Compensation Fund as it shall replenish the Compensation Fund upon the SFC's request to do so. 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. Under the SFO which came into effect on 1 April 2003, all these provisions shall continue to apply to any default occurring before that date despite the repeal of the SO. As at 30 June 2003, there were outstanding claims received in respect of 13 defaulted Stock Exchange Participants (31 December 2002: 14).

Pursuant to the SFO, the Stock Exchange issued a notice on 3 April 2003 inviting for claims against the Compensation Fund in relation to any default of a Stock Exchange Participant occurring before 1 April 2003. The claims period will expire on 3 October 2003. As at 30 June 2003, no claims have been received in response to that notice.

Notes to the Condensed Consolidated Accounts

25. Contingent Liabilities (continued)

- (a) Under the new compensation arrangements implemented under the SFO, a new Investor Compensation Fund has replaced the existing Compensation Fund, the Commodity Exchange Compensation Fund and the Dealers' Deposit Schemes for non-exchange participant dealers. The new arrangements would not require Exchange Participants to make deposits to the Investor Compensation Fund. Existing deposits would be returned to the Stock Exchange and the Futures Exchange in accordance with the provisions of the SFO. The arrangements would remove the requirement for the Stock Exchange to replenish the Investor Compensation Fund.
- (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 default of any one Participant. In the unlikely event that all of its 447 trading Participants as at 30 June 2003 (31 December 2002: 471) default, the maximum contingent liability of the Stock Exchange under the indemnity will amount to \$89 million (31 December 2002: \$94 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.

26. Material Related Party Transactions

Certain Directors of HKEx are directors and/or shareholders of (i) Stock Exchange Participants and Futures Exchange Participants (Exchange Participants) and Clearing Participants; (ii) companies listed on the Stock Exchange; and (iii) buy-in brokers. Securities and derivatives contracts traded by, and fees levied on, these Exchange Participants and Clearing Participants, fees levied on these listed companies and fees paid to these buy-in brokers are all undertaken in the ordinary course of business of the Group on the standard terms and conditions applicable to all other Exchange Participants and Clearing Participants, listed companies and buy-in brokers.

Notes to the Condensed Consolidated Accounts

26. Material Related Party Transactions (continued)

In addition to the transactions mentioned above, \$862,285 (2002: \$2,521,807) of consultancy fee was paid during the period to Goldman Sachs (Asia) LLC where Mr Tim Freshwater, an independent non-executive director of HKEx is a director. The transaction was carried out in the ordinary course of business on normal commercial terms.

During the period, one of the subsidiaries, the Futures Exchange, has entered into a lease agreement with Shine Hill Development Limited, a subsidiary of Great Eagle Holdings Limited whose group managing director, Dr K S Lo is an independent non-executive director of HKEx, to lease office space for a period of two years commencing 1 January 2003. The rental payment for the period amounted to \$1,614,000 (2002: \$3,825,000) and the lease was entered into on normal commercial terms.

27. Off Balance Sheet Risks

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 condensed consolidated interim accounts.

The Group mitigates its exposure to the 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.

Other Information

(Financial figures are expressed in Hong Kong dollars)

The Chairman, Board of Directors, and the Chief Executive

At the annual general meeting (AGM) held on 15 April 2003, five Directors were elected by shareholders to fill six available vacancies. The five elected Directors are Dr Kwok Chi Piu, Bill, Mr Lee Jor Hung, Dennis, Mr Lee Kwan Ho, Vincent Marshall, Mr David Michael Webb, and Mr Wong Sai Hung, Oscar. The Financial Secretary had also on the same day appointed six Public Interest Directors, namely Mr Fong Hup, Mr Tim Freshwater, Mr Lee Yeh Kwong, Charles, Mr Leong Ka Chai, Dr Liu Jinbao, and Dr Lo Ka Shui with effect from 16 April 2003.

As there was a casual vacancy on the Board arising from only five out of the six vacancies having been filled at the AGM, the Directors had, at the board meeting held on 16 April 2003, appointed Mr John Estmond Strickland to fill the casual vacancy in accordance with the Articles of Association. At the same meeting, the Board also re-appointed Mr Lee Yeh Kwong, Charles as the Chairman, and whose appointment was subsequently approved by the Chief Executive of the Hong Kong Special Administrative Region.

Dr Liu Jinbao tendered his resignation as a Director with effect from 28 May 2003.

Mr Chow Man Yiu, Paul joined HKEx on 1 May 2003 as the Chief Executive. Mr Chow is an ex-officio member of the Board.

Interim Dividend and Close of Register

The Board of Directors has resolved to declare an interim dividend of \$0.18 per share (2002: \$0.08 per share) for the year ending 31 December 2003, amounting to a total of about \$188 million (2002: \$83 million).

The share register will be closed from Tuesday, 9 September 2003 to Thursday, 11 September 2003, both dates inclusive, during which period no transfer of shares will be registered. Dividend warrants will be despatched to shareholders on or about Monday, 15 September 2003. In order to qualify for the interim dividend, all properly completed transfer forms accompanied by the relevant share certificates must be lodged with HKEx's registrar, Hong Kong Registrars Limited, at Rooms 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong not later than 4:00 p.m. on Monday, 8 September 2003.

Other Information

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 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 (Listing Rules) effected on 1 September 2001.

Options to subscribe for 34,890,262 shares had been granted and accepted by employees on 20 June 2000. 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.

Pursuant to the Post-Listing Scheme, a share option to subscribe for 3,000,000 shares in HKEx was granted on 2 May 2003 to Mr Chow Man Yiu, Paul, a Director and the Chief Executive of HKEx.

As at 30 June 2003, the total number of shares available for issue was 76,904,977 which represented about 7.4 per cent of the issued share capital of HKEx. Since the first grant of options in 2000, options for the issue of 10,728,755 shares had lapsed up to and including 30 June 2003.

Other Information

Details of the share options outstanding as at 30 June 2003 under the Pre-Listing Scheme and the Post-Listing Scheme were as follows:

(A) Pre-Listing Scheme

	Date of Grant	Exercise price	No. of shares issuable under the options granted as at 1 January 2003	No. of shares issued during the six months ended 30 June 2003	No. of shares lapsed during the six months ended 30 June 2003	No. of shares issuable under the options granted as at 30 June 2003	Exercise period
Kwong Ki Chi (note 1)	20 June 2000	\$7.52	1,092,126	364,000	728,126	-	6 March 2002 – 30 May 2010 (note 5)
Aggregate total for employees (note 2)	20 June 2000	\$7.52	22,160,894	3,010,000	1,279,387	17,871,507	6 March 2002 – 30 May 2010 (note 5)
Total			23,253,020	3,374,000 (note 3)	2,007,513 (note 4)	17,871,507	

(B) Post-Listing Scheme

	Date of grant	Exercise Price	No. of shares issuable under the option granted	Option Value	No. of shares issuable under the option granted as at 30 June 2003	Exercise period
Chow Man Yiu, Paul	2 May 2003	\$9.05 (note 6)	3,000,000	\$8,010,000 (note 7)	-	2 May 2005 – 1 May 2013 (note 8)

Notes:

1. Mr Kwong Ki Chi retired as a Director and the Chief Executive of HKEx on 15 April 2003.
2. Employees working under employment contracts that were regarded as “continuous contracts” for the purpose of the Employment Ordinance of Hong Kong.
3. The weighted average closing price immediately before the dates on which the options were exercised was \$9.85.

Other Information

4. Options lapsed in accordance with the terms of the Pre-Listing Scheme due to resignation of employees.
5. 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.
6. The closing price immediately before the date on which the option was granted was \$9.10.
7. According to the Binomial Option Pricing Model, the value of the option was estimated at \$8,010,000 as at 2 May 2003, the date of grant, with the following variables and assumptions:
 - Risk Free Rate 4.3%, being the yield of 10-year Exchange Fund Note as at 30 April 2003.
 - Expected Volatility 36%, being the annualised volatility of the closing price of the shares in HKEx from 3 May 2002 to 2 May 2003.
 - Expiration date of the option 10 years from the date of grant.
 - Expected Dividend 5.6%, being the 2003 prospective dividend yield of the shares.
 - Assumption No material difference between the expected volatility over the whole life of the options and the historical volatility of the shares in HKEx over the period from 3 May 2002 to 2 May 2003 is assumed.

The Binomial Option Pricing Model is 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.

No option granted during the period under review has lapsed.

8. Option granted is exercisable between 2 May 2005 to 1 May 2013, in tranches of 25 per cent each reaching 100 per cent as from 2 May 2008.

Other Information

Directors' and Chief Executive's Interests and Short Positions

As at 30 June 2003, the Directors, the Chief Executive and their respective associates had 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) as follows:

(i) Shares

Name of Director	Number of shares held			Total
	Personal Interests	Family Interests	Corporate Interests	
Lee Jor Hung, Dannis	–	–	1,610,000 (note 1)	1,610,000
David Michael Webb	2 (note 2)	2 (note 3)	6 (note 4)	10
John Estmond Strickland	18,000 (note 5)	–	–	18,000

Notes:

1. 1,610,000 shares were owned by DL Brokerage Limited, a private company beneficially wholly owned by Mr Lee Jor Hung, Dannis, representing approximately 0.15 per cent of the issued share capital of HKEx.
2. The shares held by Mr David Michael Webb as beneficial owner represent approximately 0.00 per cent of the issued share capital of HKEx.
3. The shares were owned by the spouse of Mr David Michael Webb, representing approximately 0.00 per cent of the issued share capital of HKEx.
4. The shares were owned by Fundamental Consultants Limited, Member One Limited and Member Two Limited which are under the control of Mr David Michael Webb, representing approximately 0.00 per cent of the issued share capital of HKEx.
5. The shares held by Mr John Estmond Strickland as beneficial owner represent approximately 0.00 per cent of the issued share capital of HKEx.

(ii) Underlying Shares

As at 30 June 2003, the outstanding number of shares issuable under a share option granted pursuant to the Post-Listing Scheme to Mr Chow Man Yiu, Paul, a Director and the Chief Executive of HKEx, was 3,000,000 (2002: Nil), which represents approximately 0.29 per cent of the issued share capital of HKEx. The said option was granted on 2 May 2003, and is exercisable between 2 May 2005 and 1 May 2013 at an exercise price of \$9.05 per share.

Other Information

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 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 Companies 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 June 2003, 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 June 2003, J.P. Morgan Chase & Co and its associates were holding 63,432,521 shares of HKEx, representing approximately 6.07 per cent of the issued share capital of HKEx as recorded in the register required to be kept by HKEx under Section 336 of the SFO, of which 1,134,000 shares were held by J.P. Morgan Chase & Co and its associates as beneficial owner, 2,759,591 shares as investment manager, and 59,538,930 shares as an approved lending agent pursuant to the Securities and Futures (Disclosure of Interests - Securities Borrowing and Lending) Rules.

Apart from the aforesaid, no other party has an interest or a short position in the issued share capital of HKEx, as recorded in the register required to be kept by HKEx under Section 336 of the SFO.

Minority Controller

Under 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 5 per cent or more of the voting power at any general meeting of the recognized exchange controller, except with the approval in writing of the Securities and Futures Commission (SFC) after consultation with the Financial Secretary of the HKSAR.

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 June 2003, the Minority Controllers were in aggregate holding 48.0 per cent of the issued capital of HKEx (30 June 2002 : 43.7 per cent).

Corporate Governance

The Audit Committee has reviewed the unaudited interim financial statements for the six months ended 30 June 2003 in conjunction with HKEx's external auditors. The independent review report of the external auditors is set out on page 54.

None of the Directors of HKEx is aware of information that would reasonably indicate that HKEx is not, or was not at any time during the six months ended 30 June 2003, in compliance with Appendix 14 of the Listing Rules.

Purchase, Sale or Redemption of HKEx's Listed Securities

During the six months ended 30 June 2003, HKEx had not redeemed, and neither HKEx nor any of its subsidiaries had purchased or sold any of HKEx's listed securities.

Independent Review Report to the Board of Directors of Hong Kong Exchanges and Clearing Limited

Introduction

We have been instructed by HKEx to review the interim financial report set out on pages 21 to 47.

Respective responsibilities of directors and auditors

The Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited require the preparation of an interim financial report to be in compliance with SSAP 25: Interim Financial Reporting, issued by the Hong Kong Society of Accountants. The interim financial report is the responsibility of, and has been approved by, the Directors.

It is our responsibility to form an independent conclusion, based on our review, on the interim financial report and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

Review work performed

We conducted our review in accordance with Statement of Auditing Standard 700: Engagements to review interim financial reports, issued by the Hong Kong Society of Accountants. A review consists principally of making enquiries of the Group's management and applying analytical procedures to the interim financial report and based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit and therefore provides a lower level of assurance than an audit. Accordingly we do not express an audit opinion on the interim financial report.

Review conclusion

On the basis of our review which does not constitute an audit, we are not aware of any material modifications that should be made to the interim financial report for the six months ended 30 June 2003.

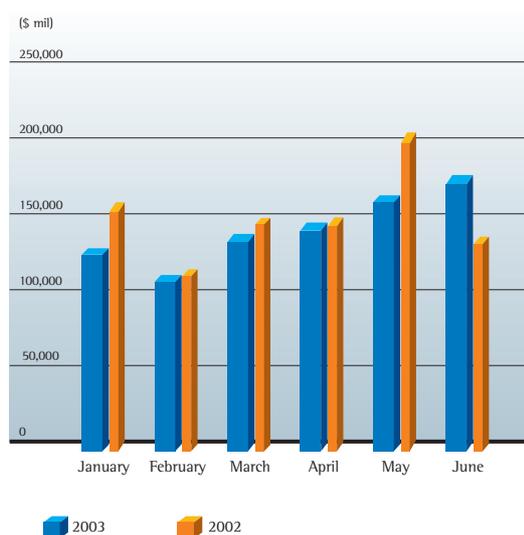
PricewaterhouseCoopers
Certified Public Accountants

Hong Kong, 13 August 2003

Market Statistics

(Financial figures are expressed in Hong Kong dollars)

Monthly Turnover, Main Board & GEM (in Dollars)



	2003 (\$ mil)	2002 (\$ mil)	% Change
January	124,842.68	159,372.81	- 21.67
February	109,006.34	113,259.98	- 3.76
March	135,937.04	146,986.57	- 7.52
April	145,418.88	149,295.13	- 2.60
May	162,648.30	204,870.78	- 20.61
June	176,202.38	135,343.25	+ 30.19
Total	854,055.62	909,128.52	- 6.06

Note: Market turnover values have been adjusted for late reported and rejected sales.

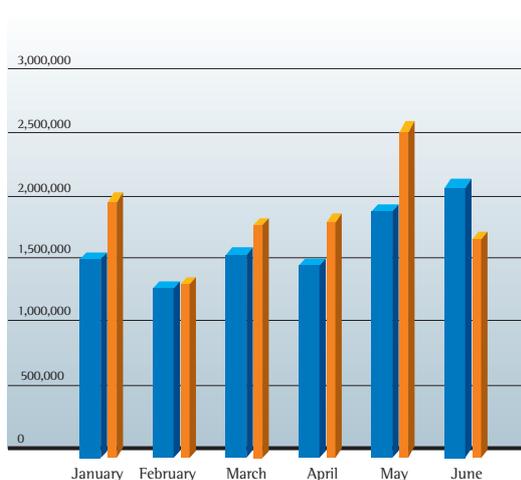
Monthly Turnover, Main Board & GEM (in Shares)



	2003 (mil shares)	2002 (mil shares)	% Change
January	122,025.27	129,717.86	- 5.93
February	110,816.44	86,612.14	+ 27.95
March	130,454.71	127,924.22	+ 1.98
April	125,044.76	157,416.31	- 20.56
May	164,760.38	270,203.06	- 39.02
June	189,950.59	153,311.43	+ 23.90
Total	843,052.15	925,185.02	- 8.88

Market Statistics

Monthly Number of Transactions, Main Board & GEM



■ 2003 ■ 2002

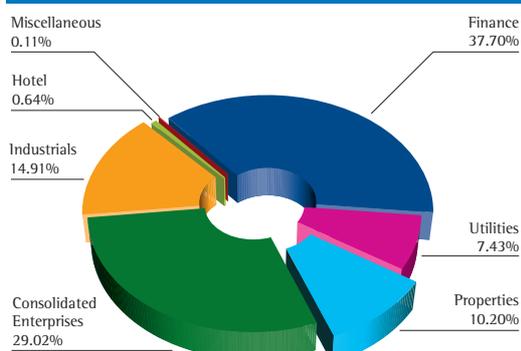
	2003	2002	% Change
January	1,527,125	2,000,674	- 23.67
February	1,305,267	1,329,753	- 1.84
March	1,555,696	1,798,115	- 13.48
April	1,488,813	1,833,662	- 18.81
May	1,912,933	2,559,812	- 25.27
June	2,106,085	1,684,689	+ 25.01
Total	9,895,919	11,206,705	- 11.70

Market Value of All Listed Companies

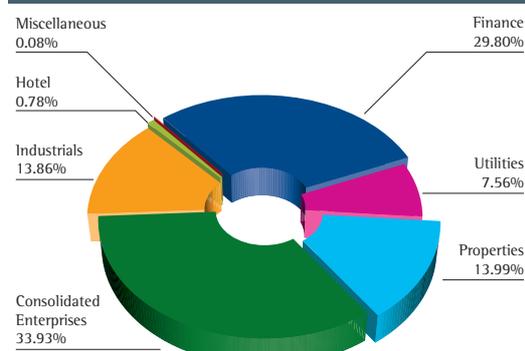
As at the end of June

	2003 (\$ mil)	2002 (\$ mil)	% Change
Finance	1,472,856.01	1,129,998.22	+ 30.34
Utilities	290,137.32	286,468.46	+ 1.28
Properties	398,362.31	530,633.99	- 24.93
Consolidated Enterprises	1,133,881.09	1,286,345.60	- 11.85
Industrials	582,567.01	525,529.81	+ 10.85
Hotels	25,089.58	29,740.94	- 15.64
Miscellaneous	4,393.34	2,980.45	+ 47.41
Sub-total	3,907,286.66	3,791,697.47	+ 3.05
GEM	60,965.10	60,520.52	+ 0.73
Total	3,968,251.76	3,852,217.99	+ 3.01

Market value as at the end of June 2003 (Main Board)



Market value as at the end of June 2002 (Main Board)



Market Statistics

Number of Listed Companies

As at the end of June

	2003	2002	% Change
Main Board			
Finance	71	66	+ 7.58
Utilities	13	12	+ 8.33
Properties	99	97	+ 2.06
Consolidated Enterprises	263	249	+ 5.62
Industrials	361	344	+ 4.94
Hotels	13	14	- 7.14
Miscellaneous	4	5	- 20.00
Sub-total	824	787	+ 4.70
GEM	175	137	+ 27.74
Total	999	924	+ 8.12

Number of Listed Securities, Main Board & GEM

As at the end of June

	2003	2002	% Change
Ordinary shares	999	925	+ 8.00
Preference shares	4	4	0
Warrants	351	462	- 24.03
Equity Linked Instruments	10	N/A	-
Unit trusts	9	11	- 18.18
Debt securities	160	179	- 10.61
Total	1,533	1,581	- 3.04

Market Value By Type of Securities, Main Board & Gem

As at the end of June

	2003 (\$ mil)	2002 (\$ mil)	% Change
Equities	3,968,251.76	3,852,217.99	+ 3.01
Warrants	20,055.17	26,102.66	- 23.17
Equity Linked Instruments	387.86	N/A	-
Debt securities	494,971.10*	544,960.94*	- 9.17
Unit trusts	N/A	N/A	N/A
Total	4,483,665.89	4,423,281.59	+ 1.37

* Nominal value

Market Statistics

Participations and Trading Right Holders Status

As at the end of June

	Stock Exchange	Futures Exchange
Exchange Participants*	506	130
Trading	447	N/A
Non-Trading	59	N/A
Trading Right Holders	33	65
Corporate	2	56
Individual	31	9

* An Exchange Participant must hold at least one Trading Right.

S&P/HKEx LargeCap Index and Hang Seng Index

January 2002 – June 2003



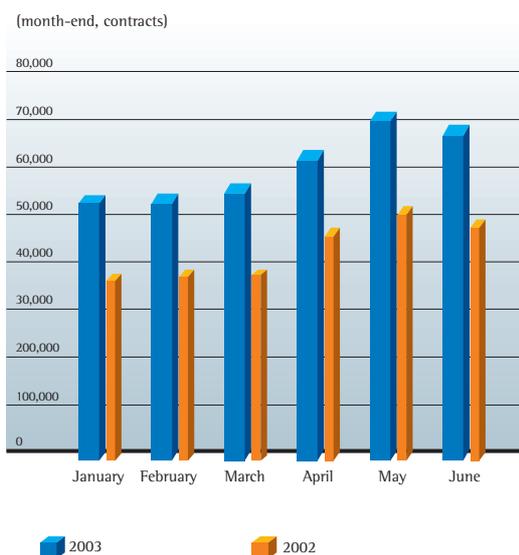
Market Statistics

Hang Seng Index Futures – Volume



	2003 Volume (contracts)	2002 Volume (contracts)
January	430,860	397,804
February	407,789	306,556
March	528,266	346,089
April	575,935	344,096
May	533,295	439,086
June	519,912	359,883

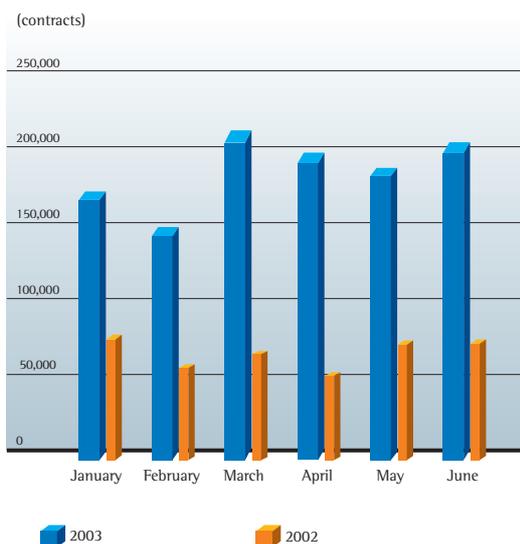
Hang Seng Index Futures – Open Interest



	2003 Open Interest (month-end, contracts)	2002 Open Interest (month-end, contracts)
January	53,757	37,215
February	54,158	37,986
March	56,346	38,552
April	63,517	47,164
May	71,770	51,536
June	68,828	48,691

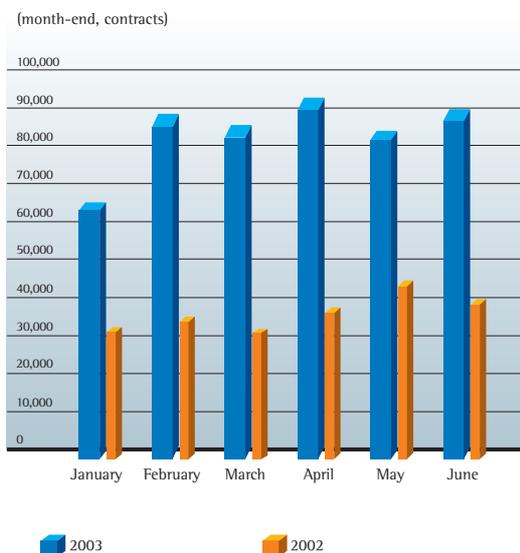
Market Statistics

Hang Seng Index Options – Volume



	2003 Volume (contracts)	2002 Volume (contracts)
January	169,890	75,196
February	146,423	55,286
March	210,314	64,783
April	195,957	50,505
May	186,196	72,128
June	202,617	71,682

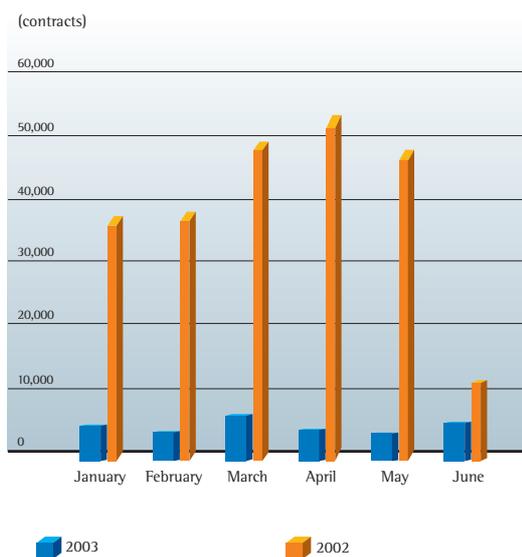
Hang Seng Index Options – Open Interest



	2003 Open Interest (month-end, contracts)	2002 Open Interest (month-end, contracts)
January	65,090	32,275
February	88,342	35,018
March	85,571	31,765
April	92,808	37,462
May	83,959	44,614
June	89,670	39,637

Market Statistics

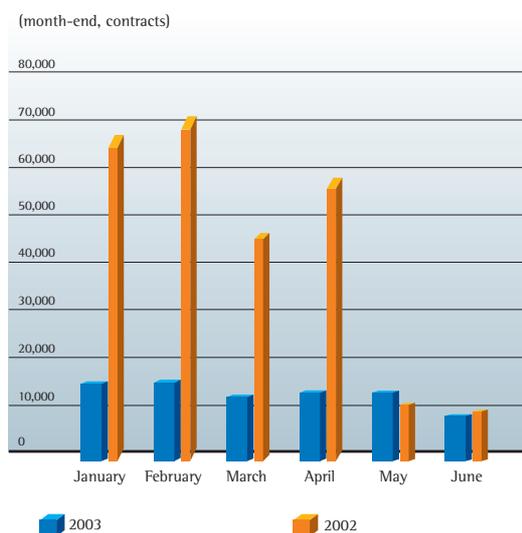
3-Month HIBOR Futures – Volume



	2003 Volume (contracts)	2002 Volume (contracts)
January	4,398	37,241
February	3,202	37,846
March	6,015	48,981
April	3,523	53,109
May	2,898	47,594
June	4,693	11,355

Note: The size of HIBOR futures contracts was increased to 5 times the original size on 27 May 2002.

3-Month HIBOR Futures – Open Interest



	2003 Open Interest (month-end, contracts)	2002 Open Interest (month-end, contracts)
January	14,833	66,731
February	14,960	70,692
March	11,851	46,013
April	12,774	57,672
May	12,776	10,287
June	7,686	8,929

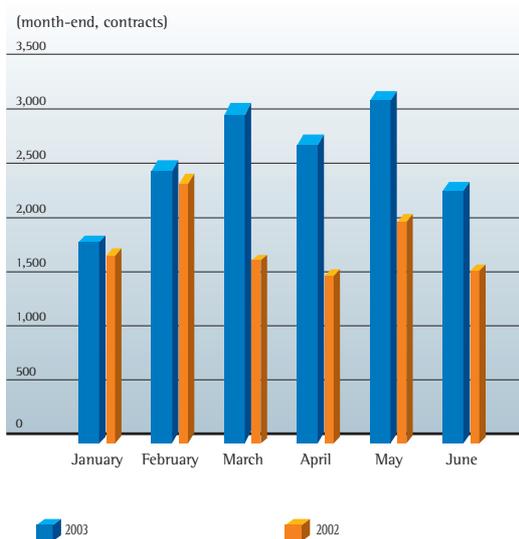
Market Statistics

Mini-Hang Seng Index Futures – Volume



	2003 Volume (contracts)	2002 Volume (contracts)
January	94,158	91,008
February	74,709	69,756
March	97,051	84,590
April	111,723	69,363
May	94,652	92,170
June	91,723	74,199

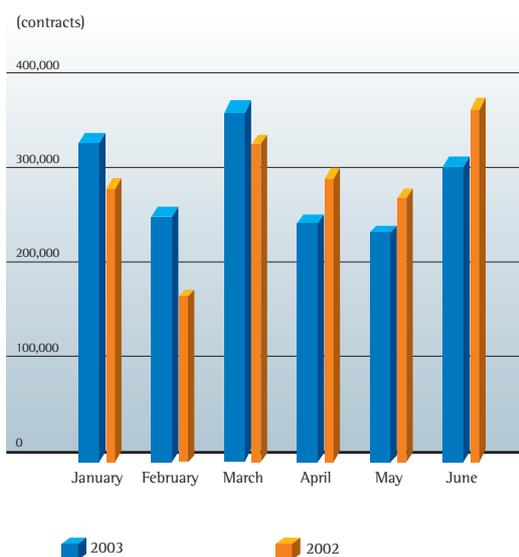
Mini-Hang Seng Index Futures – Open Interest



	2003 Open Interest (month-end, contracts)	2002 Open Interest (month-end, contracts)
January	1,840	1,718
February	2,528	2,394
March	3,056	1,655
April	2,758	1,479
May	3,163	2,022
June	2,310	1,541

Market Statistics

Stock Options – Volume



	2003 Volume (contracts)	2002 Volume (contracts)
January	336,124	288,883
February	258,752	171,460
March	371,773	334,555
April	250,610	298,936
May	239,556	278,683
June	311,464	374,308

Stock Options – Open Interest

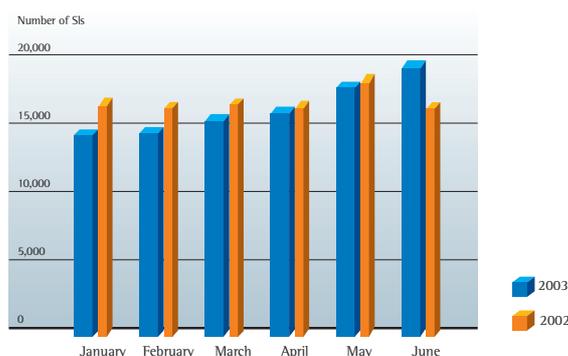


	2003 Open Interest (month-end, contracts)	2002 Open Interest (month-end, contracts)
January	452,740	306,940
February	482,252	301,790
March	374,622	338,142
April	389,769	425,892
May	402,437	501,803
June	367,713	572,118

Market Statistics

Average Daily Settlement Instruction (SIs) Settled in CCASS

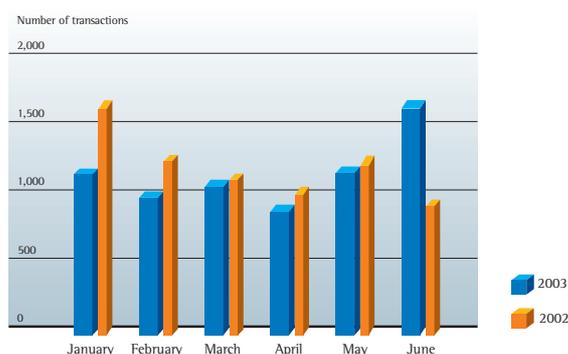
(both delivering and receiving SIs are counted)



	2003 Number of SIs	2002 Number of SIs	2003 HKD Securities SIs by share (bil)	2002 HKD Securities SIs by share (bil)	2003 SIs by value (\$ bil)	2002 SIs by value (\$ bil)
January	14,518	16,619	5.9	6.6	16.1	19.0
February	14,662	16,545	5.7	7.0	16.8	19.5
March	15,494	16,864	6.9	6.4	17.9	21.2
April	16,093	16,531	7.3	9.1	19.9	20.3
May	17,977	18,284	8.9	10.3	21.4	22.3
June	19,420	16,471	9.1	8.0	22.7	19.4

Average Daily Transactions Handled by CCASS Depository

(both deposit and withdrawal transactions are counted)

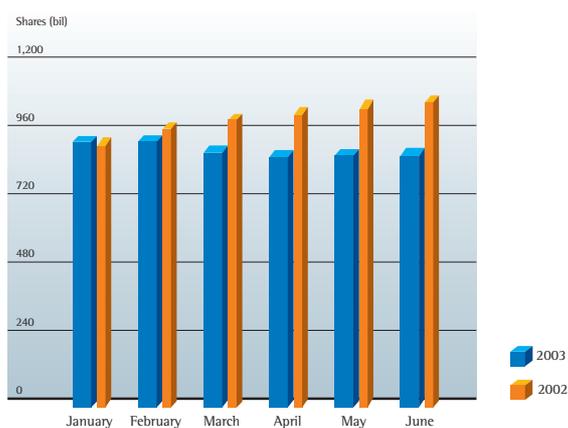


	2003 Number of transactions	2002 Number of transactions	2003 HKD Securities Number of share (bil)	2002 HKD Securities Number of share (bil)	2003 Value of transactions (\$ bil)	2002 Value of transactions (\$ bil)
January	1,178	1,642	0.8	0.9	0.5	0.8
February	1,013	1,277	0.3	0.8	0.5	0.5
March	1,092	1,142	0.3	0.8	0.5	0.6
April	907	1,032	0.4	1.2	0.4	1.2
May	1,189	1,238	0.6	1.3	0.7	1.0
June	1,661	946	0.8	1.0	0.6	0.5

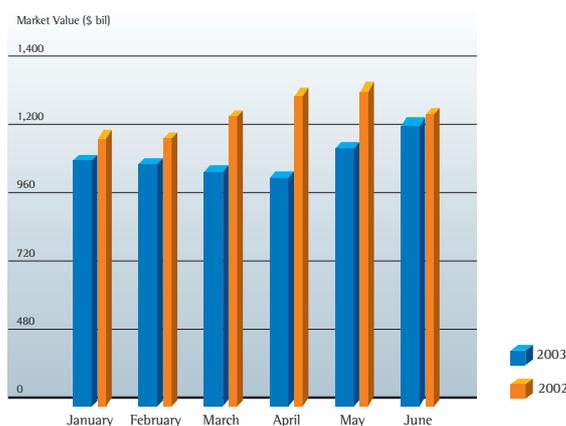
Market Statistics

Securities under CCASS Custody

(balances at the end of each month)



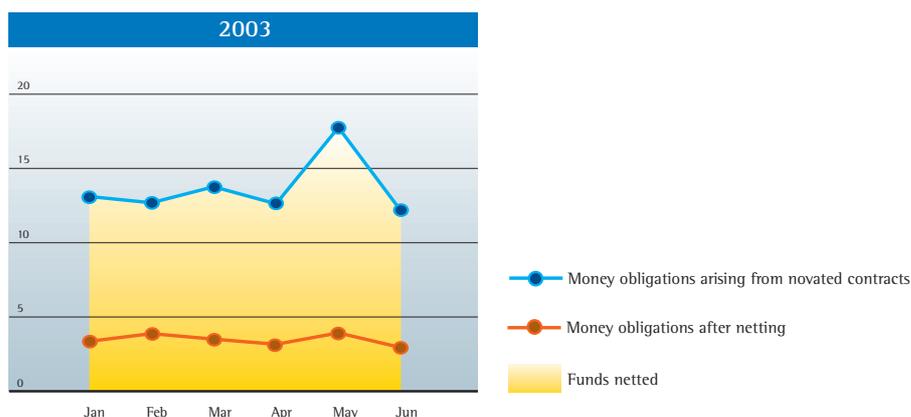
	2003 Number of shares (bil)	2002 Number of shares (bil)	2003 % of issued shares of admitted securities	2002 % of issued shares of admitted securities
January	924.4	923.2	54.6	56.4
February	925.9	971.9	54.2	56.9
March	889.7	1,001.8	52.0	57.5
April	872.8	1,025.5	53.0	58.3
May	876.7	1,050.9	53.8	58.8
June	880.4	1,067.1	53.6	58.2



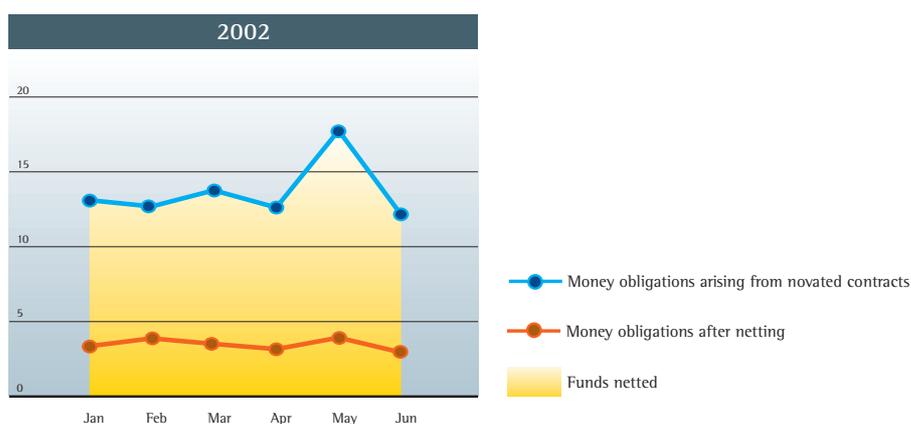
	2003 Market Value (\$ bil)	2002 Market Value (\$ bil)	2003 % of market capitalisation of admitted securities	2002 % of market capitalisation of admitted securities
January	1,142	1,194	29.9	29.0
February	1,136	1,192	30.0	29.2
March	1,084	1,257	30.0	29.4
April	1,072	1,319	29.7	29.7
May	1,177	1,335	29.0	30.0
June	1,218	1,266	29.3	30.2

Market Statistics

Average Daily Funds Netting Efficiency of CNS Trades



2003	Money obligations arising from novated contracts (\$ billion)	Money obligations after netting (\$ billion)	Funds netting efficiency (%)
January	10.8	2.1	76.2
February	10.5	2.4	77.4
March	11.8	3.0	74.5
April	13.3	3.4	75.1
May	14.8	3.4	77.5
June	16.4	3.3	79.9



2002	Money obligations arising from novated contracts (\$ billion)	Money obligations after netting (\$ billion)	Funds netting efficiency (%)
January	13.3	3.0	77.4
February	12.2	3.1	70.2
March	13.5	3.1	76.8
April	13.7	3.1	77.5
May	17.8	3.5	80.6
June	12.4	3.2	75.1

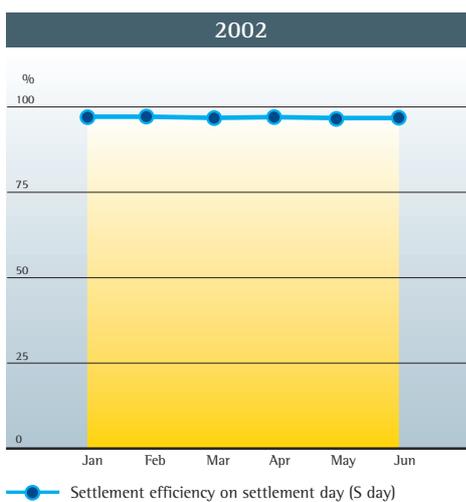
Market Statistics

Average Daily Settlement Efficiency of CNS Stock Positions



Settlement efficiency (%) HKD Securities

2003	S Day	S+1 Day
January	99.73	99.97
February	99.71	99.97
March	99.71	99.97
April	99.63	99.97
May	99.71	99.97
June	99.65	99.97



Settlement efficiency (%) HKD Securities

2002	S Day	S+1 Day
January	99.60	99.97
February	99.62	99.96
March	99.64	99.96
April	99.65	99.96
May	99.60	99.95
June	99.71	99.97

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