

**QUARTERLY REPORT**  
**FOR THE FIRST QUARTER ENDED 31 MARCH 2004**



**Hong Kong Exchanges and Clearing Limited**

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## FINANCIAL HIGHLIGHTS

(Financial figures are expressed in Hong Kong dollars)			
	Unaudited for the three months ended 31 Mar		
	2004	2003	Change
<b>KEY MARKET STATISTICS</b>			
Average daily turnover value on the Stock Exchange	<b>\$19.7 billion</b>	\$6.1 billion	223%
Average daily number of derivatives contracts traded on the Futures Exchange	<b>53,087</b>	35,952	48%
Average daily number of stock options contracts traded on the Stock Exchange	<b>25,723</b>	15,847	62%
	<b>\$'000</b>	\$'000	
<b>RESULTS</b>			
Income	<b>648,249</b>	403,271	61%
Operating expenses	<b>283,139</b>	300,489	(6%)
Operating profit	<b>365,110</b>	102,782	255%
Share of profits of associated companies	<b>2,928</b>	1,695	73%
Profit before taxation	<b>368,038</b>	104,477	252%
Taxation	<b>(54,519)</b>	(15,801)	245%
Profit attributable to shareholders	<b>313,519</b>	88,676	254%
Shareholders' funds	<b>3,756,343</b>	5,603,263	Φ (33%)
Total assets *	<b>20,575,969</b>	19,802,264	Φ 4%
Net assets per share #	<b>\$3.56</b>	\$5.34	Φ (33%)
Earnings per share	<b>\$0.30</b>	\$0.08	275%

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

Φ Audited as at 31 December 2003

# Based on 1,056,456,846 shares issued and fully paid as at 31 March 2004 (31 December 2003: 1,048,998,846 shares)

# **BUSINESS REVIEW AND PROSPECTS**

## **Business and Market Developments**

### **Market Activity**

Average daily turnover value on The Stock Exchange of Hong Kong Limited (the Stock Exchange) during the period under review was \$19.7 billion, compared with \$6.1 billion during the same period in 2003. There were eight new equity listings on the Main Board, including one by a company formerly listed on the Growth Enterprise Market (GEM), and eight new equity listings on GEM. In the first quarter of 2003, there were nine new equity listings on the Main Board, including three by companies formerly listed on GEM, and five on GEM. Equity capital formation through initial public offering (IPO) and post-IPO fund-raising totalled \$36.0 billion on the Main Board and \$2.8 billion on GEM, compared with a total of \$125.2 billion on the Main Board and \$522.7 million on GEM in the first quarter of 2003. The Main Board total figure for 2003 includes \$107.4 billion raised by HSBC Holdings in connection with its acquisition of Household International. Excluding this HSBC Holdings transaction, fund raising on the Main Board for the first quarter of 2003 was \$17.8 billion.

The average daily number of derivatives contracts traded on Hong Kong Futures Exchange Limited (the Futures Exchange) and stock options traded on the Stock Exchange during the first three months of 2004 was 78,810, up from 51,799 in the first three months of 2003. Total open interest at the end of March 2004 was 857,062 contracts, compared with 533,290 contracts at the end of March 2003.

### **Chairman and Board of Directors**

On 31 March 2004, Hong Kong Exchanges and Clearing Limited (HKEx) held its Annual General Meeting (AGM) and shareholders elected Mr John Strickland and re-elected Mr Oscar Wong to the Board of Directors. Mr Strickland, a former Public Interest Director, was appointed by the Board last year to fill a casual vacancy on the Board, while Mr Wong was elected to the Board at last year's AGM. Both terms expired at the end of this year's AGM in accordance with HKEx's Articles of Association. On the same day, the Financial Secretary reappointed Mr Charles Lee, Mr Tim Freshwater and Dr Lo Ka Shui as Public Interest Directors for a term of two years until the conclusion of the AGM in 2006.

Mr Lee was reappointed the Chairman of the Board at the Board Meeting held on 1 April 2004 for a term to be co-terminous with his term of directorship, and his appointment was subsequently approved by the Chief Executive of the Hong Kong Special Administrative Region (HKSAR) in accordance with the Securities and Futures Ordinance (SFO).

### **Listing Function**

On 26 March 2004, the Government published its Consultation Conclusions on Proposals to Enhance the Regulation of Listing. The Government's recommendations include giving statutory backing to certain more important listing requirements, such as those covering financial reporting and other periodic disclosure, disclosure of price-sensitive information and shareholders' approval for notifiable transactions, and expanding the dual filing system. As for the regulatory structure, the Stock Exchange will continue to receive initial public offer applications and no securities will be listed on the Stock Exchange unless they are approved by the Listing Committee/GEM Listing Committee. The Stock Exchange will remain responsible

for administering the listing process, and will continue to be the primary point of contact for listing applicants and their advisers. As for ongoing compliance of listed companies, the Stock Exchange will continue to enforce the non-statutory requirements in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (Listing Rules).

HKEx will work closely with the Government and the Securities and Futures Commission (SFC) on implementing the recommendations, which are aimed at raising the quality of Hong Kong's financial markets.

### **Enhancement of Corporate Governance and Market Quality**

Amendments to the Listing Rules designed to enhance corporate governance and market quality came into effect on 31 March 2004. They include new chapters of the Main Board Rules on notifiable transactions and connected transactions, revised classifications of notifiable transactions and connected transactions, revised definitions of the terms *reverse takeover*, *connected person* and *associate of a connected person*, revised requirements for refreshment of general mandate and revised requirements on the disclosure of directors' remuneration in annual reports. In addition, there have been changes in the initial listing eligibility criteria, listed issuers' continuing obligations and the disclosure requirements at the time of listing.

The rule amendments, along with the Code on Corporate Governance Practices and the disclosure requirements relating to the Report on Corporate Governance Practices that will be published later this year, represent the most comprehensive overhaul of the rules in over a decade. The new Code provisions and the related disclosure obligations will be effective for accounting periods commencing on or after 1 January 2005, except those on internal controls, which will be effective for accounting periods commencing on or after 1 July 2005.

### **Regulation of Sponsors and Independent Financial Advisers**

On 4 May 2004, the Stock Exchange invited Hong Kong sponsor and financial advisory firms to comment on draft amendments to the Listing Rules on the regulation of sponsors and independent financial advisers (IFAs). The draft amendments reflect policy developed by the Stock Exchange and the SFC after extensive public consultation in conjunction with the release in May 2003 of the joint Consultation Paper on the Regulation of Sponsors and Independent Financial Advisers.

The Stock Exchange and the SFC have agreed to proceed with reforms to the regulation of sponsors and IFAs in two stages. The first stage involves amendments to the Listing Rules and the introduction of a revised statement on conduct to clarify the Stock Exchange's expectations with regard to due diligence. The second stage involves modification of the SFC licensing regime to create specific licensing requirements for sponsors. The Stock Exchange expects its rule amendments to become effective around 1 October 2004.

### **Products and Services**

HKEx began disseminating real-time odd lot market information to information vendors on 8 March 2004 to increase market transparency. Six vendors have been offering the information to the public since the end of March and more are expected to offer the service in the coming months.

Trading in MSCI China Free Index Futures was discontinued after the market closed on 26 March 2004, due to low market demand. The decision was based on reviews conducted from

time to time to ensure that products meet the needs and demands of the market in a cost efficient manner.

A revamped version of the HKEx website was rolled out on 29 March 2004. It has a new look and streamlined navigation path along with additional content and functionality. The new features include a news alert service, information for potential issuers interested in listing in Hong Kong and a simplified Chinese character version of the website. As a result, users now have three choices of language: simplified Chinese characters, traditional Chinese characters or English.

The implementation of the Derivatives Clearing and Settlement System (DCASS) was completed on 6 April 2004. It replaced two separate clearing systems that were introduced by HKFE Clearing Corporation Limited (HKCC) and The SEHK Options Clearing House Limited (SEOCH) before they became part of HKEx in 2000. DCASS provides a common platform for the clearing and settlement of all futures and options contracts traded on the HKEx markets. The integration of the new system with the derivatives trading system helps reduce Participants' operating costs as hardware, equipment and network facilities can be shared between trading and clearing and settlement operations. PRiME (Portfolio Risk Margining System of HKEx), the new margining sub-system rolled out with DCASS for use with all futures and options contracts, provides a prudent and equitable assessment of the risks and margin requirements of derivatives market participants, supporting better risk management for the derivatives market. The stabilisation period for DCASS ended on schedule on 21 April 2004.

The H-shares Index Futures introduced on 8 December 2003 were among the derivatives market's five most actively traded products in the three months to 31 March 2004. In addition, they set a one-day volume record of 23,670 contracts on 27 April 2004 and a one-day open interest record of 27,092 contracts on 28 April 2004.

HKEx reached a milestone at the end of March 2004 when each of its major market systems had a 100 per cent uptime record for at least 12 consecutive months. The major systems comprise the trading platforms for the securities and derivatives markets, the corresponding clearing and settlement systems, the securities market's Market Data Feed System and the derivatives market's Price Reporting System.

A trial run of SIMart, HKEx's simulated investment market, began on 21 April 2004. The online educational platform's investment games allow investors to learn about HKEx's investment products through buying and selling them with notional capital in a trading environment based on delayed market data.

## **Treasury**

The Treasury Division supervises the investment of funds which can be divided into three main categories: Corporate Funds (accumulated operating profits), Clearing House Funds and margin funds received (excludes contributions receivable from Participants and securities deposited by Participants as alternatives to cash deposits of margin funds). During the period under review, the average amount of funds available for investment increased by 63 per cent or \$5.87 billion to \$15.17 billion (2003: \$9.30 billion), mainly due to a rise in margin funds received from Participants as a result of increased open interest in futures and options contracts.

As at 31 March 2004, details of the asset allocation were as follows:

	<b>Fund size</b> \$ billion	<b>Bonds</b>	<b>Cash or bank deposits</b>	<b>Global equities</b>
Corporate Funds	5.61	39%	55%	6%
Margin funds	8.17	39%	61%	0%
Clearing House Funds	1.59	8%	92%	0%
<b>Total</b>	<b>15.37</b>	<b>36%</b>	<b>62%</b>	<b>2%</b>

Investments of the three funds are kept sufficiently liquid to meet HKEx's operating needs and possible liquidity requirements of the Clearing House Funds and margin funds. Excluding equities held under the Corporate Funds (\$0.32 billion), which do not have a maturity date, the maturity profile of the remaining \$15.05 billion of investments as at 31 March 2004 was as follows:

	<b>Fund size</b> \$ billion	<b>Overnight</b>	<b>&gt;Overnight to 1 month</b>	<b>&gt;1 month to 1 year</b>	<b>&gt;1 year to 3 years</b>	<b>&gt; 3 years</b>
Corporate Funds	5.29	27%	30%	13%	22%	8%
Margin funds	8.17	54%	4%	7%	35%	0%
Clearing House Funds	1.59	72%	11%	7%	10%	0%
<b>Total</b>	<b>15.05</b>	<b>46%</b>	<b>14%</b>	<b>9%</b>	<b>28%</b>	<b>3%</b>

Following the payment of the 2003 special and final dividends of \$2,219 million on 14 April 2004, the amount of Corporate Funds available for investment has been reduced by this amount.

Risk management techniques, such as Value-at-Risk (VaR) and portfolio stress testing, are used to identify, measure, monitor and control market risks. VaR measures the expected maximum loss over a given time interval (a holding period of 10 trading days is used by HKEx) at a given confidence level (95 per cent confidence level is adopted by HKEx) based on historical data (one year is used by HKEx). The overall risk, as measured by the VaR methodology, during the first quarter of 2004 was as follows:

	<b>Average VaR</b> \$ million	<b>Maximum VaR</b> \$ million	<b>Minimum VaR</b> \$ million
Corporate Funds	16.65	18.33	15.47
Margin funds	14.00	16.93	10.27
Clearing House Funds	1.15	1.22	1.03

Credit exposure was well diversified. As at 31 March 2004, all bonds held were of investment grade and had a weighted average credit rating of Aa2 and a weighted average maturity of 1.7 years. Deposits were placed only with the note-issuing banks in Hong Kong and licensed banks and restricted licence banks with a minimum credit rating of A3 by Moody's or equivalent approved by the Board from time to time.

For details of HKEx's investment income, please refer to the Overall Performance section and note 6 to the accounts of this quarterly report.

### **China Development**

Staff from HKEx's Beijing Representative Office and the Hong Kong office will be stationed in the Mainland cities of Guangzhou and Shanghai later this year to conduct market research and introduce the services and markets of HKEx to listed and potential issuers on the Mainland.

### **Overall Performance**

The Group recorded a profit attributable to shareholders of \$314 million in the first quarter of 2004, compared with \$89 million for the same period in 2003. The \$225 million or 254 per cent increase in profit was mainly attributable to the increase in cash and derivatives market activities in 2004, which has resulted in an increase in trading fees and trading tariff, and clearing and settlement fees.

Total operating expenses for the first quarter decreased by \$17 million or 6 per cent to \$283 million (2003: \$300 million), mainly due to a decrease in information technology and computer maintenance expenses.

### **Income**

Total income (including share of profits of associated companies) for the first quarter increased by \$246 million or 61 per cent to \$651 million (2003: \$405 million).

Improved investment sentiment since the second half of 2003 continued, and the increase in cash and derivatives market activities gathered more momentum in the first quarter of 2004. Average daily turnover on the Stock Exchange for the period increased by 223 per cent to \$19.7 billion, compared with \$6.1 billion in the first quarter of 2003. Average daily number of stock options contracts traded on the Stock Exchange increased by 62 per cent in 2004 compared with that in 2003. Average daily number of derivatives contracts traded on the Futures Exchange increased by 48 per cent, mainly on account of an increase in the trading of Hang Seng Index (HSI) Futures contracts. Consequently, trading fees and trading tariff rose by \$109 million or 131 per cent to \$193 million (2003: \$84 million).

Listing fee income for the first quarter rose by \$12 million or 15 per cent to \$91 million (2003: \$79 million), largely because of an increase in initial listing fees mainly arising from an increase in the number of newly listed warrants to 314 in 2004 (2003: 112), and a rise in annual listing fees due to a higher number of listed securities. 8 (2003: 9) new companies joined the Main Board and 8 (2003: 5) joined the GEM during the first quarter. As at 31 March 2004, 7 Main Board and 4 GEM (31 December 2003: 3 Main Board and 5 GEM) IPO applications had obtained approval in principle from the Listing Committee for listing, and 24 Main Board and 23 GEM applications were under processing (31 December 2003: 19 Main Board and 32 GEM). As at 31 March 2004, there were 856 companies listed on the Main Board and 192 on GEM (31 December 2003: 852 and 185 respectively).



In line with the increase in cash market activities, clearing and settlement fee income increased by \$66 million or 161 per cent to \$107 million in the first quarter (2003: \$41 million) and depository, custody and nominee services fee income increased by \$10 million or 37 per cent to \$38 million in the first quarter (2003: \$28 million).

Income from sale of information for the first quarter increased by \$16 million or 25 per cent to \$80 million (2003: \$64 million), as demand for information increased, in line with the increase in the activities of cash and derivatives markets.

Investment income comprises income from investments supervised by the Treasury Division, investment in Singapore Exchange Limited and accommodation income from Participants. Total investment income for the Group for the first quarter increased by \$25 million or 36 per cent to \$93 million (2003: \$68 million).

For investments supervised by the Treasury Division, income for the first quarter amounted to \$90 million, 42 per cent or \$27 million higher than the \$63 million reported for the same period in 2003. The increase was due to higher net realised gain at \$24 million (2003: \$15 million), net unrealised mark-to-market gain at \$25 million (2003: loss of \$7 million) on the investment portfolio, and dividends at \$1 million (2003: \$1 million), but partly offset by lower net interest income at \$40 million (2003: \$54 million) due to lower interest rates. As the valuation of the 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.

During the quarter under review, the average 6-month Hong Kong Exchange Fund Bill rate dropped from 1.20 per cent in the first quarter of 2003 to 0.08 per cent in the same period in 2004, and the average 90-day US Treasury Bill rate declined from 1.16 per cent to 0.92 per cent.

For the quarter ended 31 March 2004, the Treasury Division achieved a positive return on investments of 2.37 per cent (2003: 2.72 per cent). The Corporate Funds returned 5.66 per cent (2003: 3.32 per cent), the margin funds 0.64 per cent (2003: 2.01 per cent), and the Clearing House Funds 0.60 per cent (2003: 2.40 per cent). Therefore, the overall portfolio recorded a spread of 229 basis points (2003: 152 basis points) with the Corporate Funds registering a spread of 558 basis points (2003: 212 basis points), the margin funds 56 basis points (2003: 81 basis points), and the Clearing House Funds 52 basis points (2003: 120 basis points) above the 6-month Hong Kong Exchange Fund Bill yield.

The average amount of funds available for investment in the first quarter increased by \$5.9 billion or 63 per cent to \$15.2 billion (2003: \$9.3 billion), mainly due to a rise in margin funds received from Clearing Participants as a result of increased open interest in futures and options contracts. As at 31 March 2004, 62 per cent (31 December 2003: 59 per cent) of the funds were invested in cash or bank deposits, 36 per cent (31 December 2003: 39 per cent) in high-grade bonds with an average credit rating of Aa2, and 2 per cent (31 December 2003: 2 per cent) in global equities.

Income from the Group's investment in Singapore Exchange Limited for the first quarter remained at the same level as 2003 at \$0.8 million (2004: dividend of \$1 million less foreign exchange loss and interest expense of \$0.2 million for funding the investment; 2003: dividend of \$1 million less interest expense of \$0.2 million). Accommodation income (i.e. retention interest charged on cash margin deposits and securities deposited by Participants as alternatives to cash deposits of the margin funds) decreased by 48 per cent or \$2.2 million to \$2.3 million (2003: \$4.5 million).

Following the payment of the 2003 special and final dividends of \$2,219 million on 14 April 2004, the amount of Corporate Funds available for investment has been reduced by this amount. As a result, the Group's investment income is unlikely to be sustainable at the level achieved in the first quarter of 2004.

Other income for the first quarter increased by \$7 million or 19 per cent to \$46 million (2003: \$39 million), mainly due to a \$6 million increase in brokerage on direct IPO applications.

### **Operating Expenses**

Total operating expenses for the first quarter decreased by \$17 million or 6 per cent to \$283 million (2003: \$300 million).

Staff costs and related expenses for the first quarter rose by \$2 million or 1 per cent to \$131 million (2003: \$129 million), mainly due to an accrual for performance bonus on account of the Group's improved performance in 2004 which was partly offset by savings in salaries as a result of reduced headcount following the streamlining of the Group's operations in May 2003.

Information technology and computer maintenance expenses for the first quarter fell by \$18 million or 25 per cent to \$55 million in 2004 (2003: \$73 million), mainly attributable to lower hardware and software rental. During the period under review, capital expenditures on computer systems, hardware and software amounted to \$6 million (2003: \$9 million).

Premises expenses for the first quarter fell by \$3 million or 13 per cent to \$19 million (2003: \$22 million) on account of lower rental negotiated upon the renewal of certain leases and savings from reduced floor area leased during the first quarter of 2004.

Legal and professional fees for the first quarter decreased by \$4 million or 50 per cent to \$4 million (2003: \$8 million), primarily as a result of professional fees incurred for several one-off consulting projects in 2003.

Depreciation and amortisation costs for the first quarter decreased by \$2 million or 3 per cent to \$45 million (2003: \$47 million) as a result of revising the estimated useful life of the hardware of trading and clearing systems from 3 years to 5 years to better reflect the useful life of the equipment.

Payment to the SFC was \$5 million for the first quarter 2004 (2003: \$Nil) under the dual filing regime, which started from 1 April 2003.

Other operating expenses for the first quarter rose by \$1 million or 8 per cent to \$21 million (2003: \$20 million), mainly attributable to higher insurance cost.

The Group's taxation charge rose by \$39 million or 245 per cent to \$55 million for the first quarter (2003: \$16 million), mainly on account of a \$45 million rise in tax charge arising from an increase in net profit in 2004, but partly offset by a one-off deferred tax charge of \$6 million recognised in 2003 due to an increase in tax rate from 16 per cent in 2002 to 17.5 per cent in 2003 and the first time adoption of Hong Kong Statement of Standard Accounting Practice (SSAP)12: Income Taxes, effective from 1 January 2003.

## **Working Capital**

Working capital fell by \$1,815 million or 41 per cent to \$2,648 million (31 December 2003: \$4,463 million) mainly due to the 2003 special and final dividends of \$2,219 million that were payable in April 2004. In preparation for the dividend payment, certain trading securities were liquidated, which has in turn pushed the bank balances and time deposits up by \$1,264 million or 71 per cent to \$3,042 million (31 December 2003: \$1,778 million).

## **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. During the period, the Singapore dollar credit facility (31 December 2003: S\$11 million or HK\$50 million) used to hedge the currency exposure of the Group's investment in shares of Singapore Exchange Limited was fully repaid. Thereafter, only forward foreign exchange contracts are used to hedge the currency exposure of the Group's non-HKD investments to mitigate risks arising from fluctuations in exchange rates. As at 31 March 2004, aggregate net open foreign currency positions amounted to HK\$1,625 million, of which HK\$289 million were non-USD exposures (31 December 2003: HK\$1,663 million, of which HK\$204 million were non-USD exposures). The Group's foreign currency liabilities, mainly in the form of margin deposits or collateral received, are hedged by investments in the same currencies.

There were no other significant changes in the financial position or from the information disclosed under Management Discussion and Analysis in the annual report for the year ended 31 December 2003.

It is the Group's plan to declare dividends only at the half-year and year-end. Therefore, no dividend will be proposed for the quarter ended 31 March 2004 (first quarter of 2003: \$Nil).

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

## **Prospects**

A substantial part of HKEx's income is tied to the activity on its exchanges, which is driven by a variety of domestic and external factors. While the Hong Kong economy appears poised for solid growth this year, market sentiment appears likely to remain mixed. Investors are concerned about the macro economic measures implemented for adjusting the Mainland economy, and the likelihood of interest rate rises in the United States. In addition, further volatility in the currency and commodity markets could affect sentiment.

HKEx will continue its efforts to improve the quality of its markets and services to attract more issuers and investors to Hong Kong. Further development of the China dimension of HKEx's business is also a top priority, and stringent cost controls remain in place.

**CONDENSED CONSOLIDATED PROFIT AND LOSS ACCOUNT**

(Financial figures are expressed in Hong Kong dollars)

	Note	Unaudited Three months ended 31 Mar 2004 \$'000	Unaudited Three months ended 31 Mar 2003 \$'000
<b>INCOME</b>	2		
Trading fees and trading tariff	4	192,784	83,569
Stock Exchange listing fees	5	90,691	79,083
Clearing and settlement fees		106,634	40,823
Depository, custody and nominee services fees		37,826	27,645
Income from sale of information		80,555	64,218
Investment income	6	92,966	68,467
Other income	7	46,793	39,466
	3	<u>648,249</u>	<u>403,271</u>
<b>OPERATING EXPENSES</b>			
Staff costs and related expenses		130,585	129,043
Information technology and computer maintenance expenses		54,614	72,859
Premises expenses		19,393	22,175
Product marketing and promotion expenses		3,168	2,131
Legal and professional fees		3,881	7,758
Depreciation and amortisation		45,352	46,929
Payment to SFC under dual filing regime		5,000	-
Other operating expenses	8	21,146	19,594
	3	<u>283,139</u>	<u>300,489</u>
<b>OPERATING PROFIT</b>	3	365,110	102,782
<b>SHARE OF PROFITS OF ASSOCIATED COMPANIES</b>	3	<u>2,928</u>	<u>1,695</u>
<b>PROFIT BEFORE TAXATION</b>	3	368,038	104,477
<b>TAXATION</b>	3/9	<u>(54,519)</u>	<u>(15,801)</u>
<b>PROFIT ATTRIBUTABLE TO SHAREHOLDERS</b>	3/22	<u>313,519</u>	<u>88,676</u>
<b>Earnings per share</b>	10	<u>\$0.30</u>	<u>\$0.08</u>

## CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

(Financial figures are expressed in Hong Kong dollars)

	Note	Unaudited Three months ended 31 Mar 2004 \$'000	Unaudited Three months ended 31 Mar 2003 \$'000
<b>Total equity at 1 Jan</b>		<b>5,603,263</b>	5,490,364
Change in fair value of non-trading securities		<b>2,665</b>	397
Deferred tax arising from change in valuation of other properties		-	(612)
Deferred tax arising from change in fair value of non-trading securities		<u>(777)</u>	<u>429</u>
Net surplus not recognised in the condensed consolidated profit and loss account		<b>1,888</b>	214
Profit attributable to shareholders		<b>313,519</b>	88,676
Realisation of change in fair value of non-trading securities on maturity and disposal		<b>148</b>	(2,665)
2003 special and final dividends		<b>(2,218,559)</b>	-
Proceeds from issue of shares under employee share option schemes	19	<u><b>56,084</b></u>	<u>5,911</u>
<b>Total equity at 31 Mar</b>		<u><b>3,756,343</b></u>	<u>5,582,500</u>

## CONDENSED CONSOLIDATED BALANCE SHEET

(Financial figures are expressed in Hong Kong dollars)

		<b>Unaudited at 31 Mar 2004 \$'000</b>	Audited at 31 Dec 2003 \$'000
<b>NON-CURRENT ASSETS</b>			
Fixed assets	11	546,373	585,627
Investments in associated companies	12	33,920	34,002
Clearing House Funds	13	1,687,226	1,551,330
Compensation Fund Reserve Account	14	37,081	36,859
Cash and Derivatives Market Development Fund	15	930	925
Non-trading securities		77,156	77,258
Other assets		3,639	4,814
		<u>2,386,325</u>	<u>2,290,815</u>
<b>CURRENT ASSETS</b>			
Margin funds on derivatives contracts	16	8,877,056	7,874,510
Accounts receivable, prepayments and deposits	17	3,746,824	4,644,680
Taxation recoverable		1,257	1,558
Trading securities		2,522,231	3,212,998
Bank balances and time deposits		3,042,276	1,777,703
		<u>18,189,644</u>	<u>17,511,449</u>
<b>CURRENT LIABILITIES</b>			
Bank loans		-	50,286
Margin deposits and securities received from Clearing			
Participants on derivatives contracts	16	8,877,056	7,874,510
Accounts payable, accruals and other liabilities	17	4,081,286	4,779,904
Dividends payable		2,218,559	-
Participants' admission fees received		1,500	4,100
Deferred revenue		219,057	257,068
Taxation payable		118,299	57,370
Provisions	18	25,745	25,011
		<u>15,541,502</u>	<u>13,048,249</u>
<b>NET CURRENT ASSETS</b>		<u>2,648,142</u>	<u>4,463,200</u>
<b>TOTAL ASSETS LESS CURRENT LIABILITIES</b>		<u>5,034,467</u>	<u>6,754,015</u>

**CONDENSED CONSOLIDATED BALANCE SHEET (continued)**

(Financial figures are expressed in Hong Kong dollars)

		<b>Unaudited at 31 Mar 2004 \$'000</b>	<b>Audited at 31 Dec 2003 \$'000</b>
<b>NON-CURRENT LIABILITIES</b>			
Participants' admission fees received		<b>84,850</b>	84,950
Participants' contributions to Clearing House Funds		<b>1,118,591</b>	984,045
Deferred tax liabilities		<b>52,085</b>	58,665
Provisions	18	<b>22,598</b>	23,092
		<b>1,278,124</b>	1,150,752
<b>NET ASSETS</b>			
		<b>3,756,343</b>	5,603,263
<b>CAPITAL AND RESERVES</b>			
Share capital	19	<b>1,056,457</b>	1,048,999
Share premium	19	<b>102,964</b>	54,338
Revaluation reserves	20	<b>48,467</b>	46,431
Designated reserves	21	<b>690,360</b>	689,657
Retained earnings	22	<b>1,858,095</b>	1,560,940
Proposed and declared dividends	22	<b>-</b>	2,202,898
<b>SHAREHOLDERS' FUNDS</b>			
		<b>3,756,343</b>	5,603,263

## 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 accounts should be read in conjunction with the 2003 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 2003.

### 2. Turnover

Turnover comprises trading fees and trading tariff from securities and options traded on the Stock Exchange and derivatives contracts traded on the 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:

	Unaudited Three months ended 31 Mar 2004				
	Cash Market \$'000	Derivatives Market \$'000	Clearing Business \$'000	Information Services \$'000	Group \$'000
Income	302,666	82,238	181,745	81,600	648,249
Costs	<u>134,921</u>	<u>36,232</u>	<u>93,009</u>	<u>18,977</u>	<u>283,139</u>
Segment results	167,745	46,006	88,736	62,623	365,110
Share of profits of associated companies	<u>-</u>	<u>-</u>	<u>2,928</u>	<u>-</u>	<u>2,928</u>
Segment profits before taxation	167,745	46,006	91,664	62,623	368,038
Taxation					<u>(54,519)</u>
Profit attributable to shareholders					<u><u>313,519</u></u>



## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 3. Segment Information (continued)

	Unaudited				Group \$'000
	Three months ended 31 Mar 2003				
	Cash Market \$'000	Derivatives Market \$'000	Clearing Business \$'000	Information Services \$'000	
<b>Income</b>	169,637	73,938	94,567	65,129	403,271
<b>Costs</b>	<u>143,860</u>	<u>41,510</u>	<u>87,797</u>	<u>27,322</u>	<u>300,489</u>
<b>Segment results</b>	25,777	32,428	6,770	37,807	102,782
Share of profits of associated companies	<u>38</u>	<u>-</u>	<u>1,657</u>	<u>-</u>	<u>1,695</u>
Segment profits before taxation	25,815	32,428	8,427	37,807	104,477
Taxation					<u>(15,801)</u>
Profit attributable to shareholders					<u><u>88,676</u></u>

- (a) The **Cash Market** business 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 GEM. The major sources of income of the business are trading fees, trading tariff and listing fees. Direct costs of the Listing Function are included under the Cash Market Segment. Costs of the Listing Function are further explained in note 5.

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

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

The **Information Services Segment** is responsible for developing and promoting e-commerce products, compiling and developing index and statistical data, and sales and business development of market data. Its income comprises primarily income from sale of Cash Market and Derivatives Market information.

## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 3. Segment Information (continued)

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

### 4. Trading Fees and Trading Tariff

	<b>Unaudited Three months ended 31 Mar 2004 \$'000</b>	Unaudited Three months ended 31 Mar 2003 \$'000
Trading fees and trading tariff are derived from:		
Securities traded on the Cash Market	<b>140,353</b>	43,126
Derivatives contracts traded on the Derivatives Market	<b>52,431</b>	40,443
	<b>192,784</b>	83,569

### 5. Stock Exchange Listing Fees

Stock exchange listing fees comprise the following:

Income	<b>Unaudited Three months ended 31 Mar 2004</b>			Unaudited Three months ended 31 Mar 2003		
	<b>Equity \$'000</b>	<b>Debt &amp; derivatives \$'000</b>	<b>Total \$'000</b>	Equity \$'000	derivatives \$'000	Total \$'000
Annual listing fees	<b>60,444</b>	<b>581</b>	<b>61,025</b>	57,847	906	58,753
Initial listing fees	<b>9,800</b>	<b>14,978</b>	<b>24,778</b>	12,200	5,945	18,145
Prospectus vetting fees	<b>725</b>	<b>-</b>	<b>725</b>	480	-	480
Other listing fees	<b>2,323</b>	<b>1,840</b>	<b>4,163</b>	1,705	-	1,705
	<b>73,292</b>	<b>17,399</b>	<b>90,691</b>	72,232	6,851	79,083

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

## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 5. Stock Exchange Listing Fees (continued)

<b>Costs of Listing Function</b>	<b>Unaudited Three months ended 31 Mar 2004 \$'000</b>	<b>Unaudited Three months ended 31 Mar 2003 \$'000</b>
Staff costs and related expenses	25,218	24,602
Information technology and computer maintenance expenses	752	658
Premises expenses	1,812	1,939
Legal and professional fees	2,064	2,693
Depreciation and amortisation	4,220	3,332
Payment to SFC under the dual filing regime	5,000	-
Other expenses	2,411	1,733
	<u>41,477</u>	<u>34,957</u>

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

## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 6. Investment Income

	Unaudited Three months ended 31 Mar 2004 \$'000	Unaudited Three months ended 31 Mar 2003 \$'000
Interest income		
- bank deposits	5,721	14,763
- listed securities	9,578	11,656
- unlisted securities	24,473	28,803
	<u>39,772</u>	<u>55,222</u>
Interest expenses	<u>(104)</u>	<u>(340)</u>
Net interest income	<u>39,668</u>	<u>54,882</u>
Accommodation income on cash margin deposits and securities deposited by Participants as alternatives to cash deposits of the margin funds	<u>2,323</u>	<u>4,481</u>
Non-interest investment income		
Net realised gain/(loss) on investments including realisation of change in fair value of non-trading securities on maturity or disposal		
- listed trading and non-trading securities	14,463	587
- unlisted trading and non-trading securities	12,632	6,669
- exchange difference	(2,952)	7,485
	<u>24,143</u>	<u>14,741</u>
Net unrealised gain/(loss) on investments		
- listed trading securities	20,968	(8,692)
- unlisted trading securities	(3,584)	984
- exchange difference	7,241	275
	<u>24,625</u>	<u>(7,433)</u>
Dividend income		
- non-trading securities	1,070	1,049
- trading securities	1,137	747
	<u>2,207</u>	<u>1,796</u>
Total non-interest investment income	<u>50,975</u>	<u>9,104</u>
Total investment income	<u>92,966</u>	<u>68,467</u>
Total investment income is derived from:		
Corporate Funds (note a)	74,973	40,365
Margin funds	15,635	22,322
Clearing House Funds	2,358	5,780
	<u>92,966</u>	<u>68,467</u>

- (a) Corporate Funds include investment income of Compensation Fund Reserve Account of \$131,000 (2003: \$186,000) and Cash and Derivatives Market Development Fund (CDMD Fund) of \$6,000 (2003: \$38,000).

## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 7. Other Income

	<b>Unaudited Three months ended 31 Mar 2004 \$'000</b>	<b>Unaudited Three months ended 31 Mar 2003 \$'000</b>
Exchange network, terminal user, dataline and software sub-license fees	29,089	27,384
Participants' subscription and application fees	8,676	9,732
Share registration services fees	606	593
Brokerage on direct IPO applications	6,365	44
Miscellaneous income	2,057	1,713
	<u>46,793</u>	<u>39,466</u>

### 8. Other Operating Expenses

	<b>Unaudited Three months ended 31 Mar 2004 \$'000</b>	<b>Unaudited Three months ended 31 Mar 2003 \$'000</b>
(Reversal of provision for)/provision for doubtful debts	(503)	61
Insurance	4,290	2,991
Financial data subscription fees	2,032	2,203
Custodian and fund management fees	2,097	2,137
Bank charges	2,118	1,556
Repair and maintenance	1,573	1,296
Other miscellaneous expenses	9,539	9,350
	<u>21,146</u>	<u>19,594</u>

## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 9. Taxation

Taxation in the condensed consolidated profit and loss account represents:

	<b>Unaudited Three months ended 31 Mar 2004 \$'000</b>	<b>Unaudited Three months ended 31 Mar 2003 \$'000</b>
Provision for Hong Kong Profits Tax (note a)	<b>61,266</b>	11,986
Deferred taxation (note b)	<b>(7,357)</b>	3,430
	<b>53,909</b>	15,416
Share of taxation of associated companies	<b>610</b>	385
	<b>54,519</b>	15,801

- (a) Hong Kong Profits Tax has been provided for at 17.5 per cent (2003: 17.5 per cent) on the estimated assessable profit for the period.
- (b) Deferred taxation for 2003 includes an one-off deferred tax charge of \$6,218,000, which arose from recomputing outstanding deferred tax liabilities carried forward from 2002 using the higher tax rate of 17.5 per cent and the adoption of SSAP 12: Income Taxes in 2003.

### 10. Earnings Per Share

The calculation of basic earnings per share is based on the profit attributable to shareholders of \$313,519,000 (2003: \$88,676,000) and the weighted average of 1,050,318,758 shares (2003: 1,043,676,335) in issue during the three-month period.

The employee share options outstanding did not have a material dilutive effect on the basic earnings per share.

## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 11. 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 three months to 31 March 2004 was \$6,248,000 (2003: \$11,959,000) of which \$6,050,000 (2003: \$9,015,000) or 97 per cent (2003: 75 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 three months to 31 March 2004 were \$3,472,000 and \$149,000 respectively (2003: \$95,106,000 and \$97,000 respectively). During the period, the estimated useful life of the hardware of trading and clearing systems was revised from 3 years to 5 years to better reflect the useful life of the equipment.

### 12. Investments in Associated Companies

	<b>Unaudited at 31 Mar 2004 \$'000</b>	Audited at 31 Dec 2003 \$'000
Share of net assets of associated companies	12,287	11,707
Goodwill on acquisition of shares in associated companies less amortisation and impairment (note a)	<u>21,633</u>	<u>22,295</u>
	<u><b>33,920</b></u>	<u><b>34,002</b></u>

(a) Goodwill

#### Cost

At 1 Jan 2004 and 31 Mar 2004

\$'000

26,889

#### Accumulated amortisation and impairment

At 1 Jan 2004

4,594

Charge for the period

662

At 31 Mar 2004

5,256

#### Net book value

At 31 Mar 2004

21,633

At 31 Dec 2003

22,295

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

## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 12. Investments in Associated Companies (continued)

(c) Details of the unlisted associated companies as at 31 March 2004 are as follows:

<u>Name</u>	<u>Place of incorporation</u>	<u>Principal activities</u>	<u>Particulars of shares held</u>	<u>Interest held</u>
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	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

### 13. Clearing House Funds

	Unaudited at 31 Mar 2004 \$'000	Audited at 31 Dec 2003 \$'000
Net asset values of the Clearing House Funds are as follows:		
HKSCC Guarantee Fund	370,822	371,289
SEOCH Reserve Fund	128,377	131,274
HKCC Reserve Fund	<u>1,188,027</u>	<u>1,048,767</u>
	<u><b>1,687,226</b></u>	<u><b>1,551,330</b></u>
Net assets of the Clearing House Funds are composed of:		
Unlisted non-trading securities, at fair value		
- debt securities	126,428	125,643
Contributions receivable from Clearing Participants fully secured by bank guarantees	116,585	92,234
Bank balances and time deposits	<u>1,460,004</u>	<u>1,349,644</u>
	1,703,017	1,567,521
Less: Other liabilities	<u>(15,791)</u>	<u>(16,191)</u>
	<u><b>1,687,226</b></u>	<u><b>1,551,330</b></u>
The Clearing House Funds are funded by:		
Clearing Participants' contributions:		
- cash	1,002,006	891,811
- bank guarantees	116,585	92,234
Clearing houses' contributions	320,200	320,200
Forfeiture of defaulted Clearing Participants' contributions	1,928	1,928
Accumulated investment income net of expenses included in designated reserves attributable to:		
- Clearing Participants' contributions	183,803	183,305
- Clearing houses' contributions	60,307	60,233
Revaluation reserve (note 20(c))	<u>2,397</u>	<u>1,619</u>
	<u><b>1,687,226</b></u>	<u><b>1,551,330</b></u>

## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 13. 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.

For the HKSCC Guarantee Fund, investment income was insufficient to cover the fund's expenses during the three months ended 31 March 2004 and a loss of \$1,530,000 (2003: \$184,000) arose. Accumulated losses of \$3,792,000 were included in the Group's retained earnings as at 31 March 2004 (31 December 2003: \$2,262,000). Future surplus investment income net of expenses of the fund will be offset against such accumulated losses before appropriation from the Group's retained earnings to the fund.

### 14. Compensation Fund Reserve Account

SFC is responsible for maintaining the Unified Exchange Compensation Fund (Compensation Fund). By virtue of Schedule 10 of the 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 to the Compensation Fund.

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

### 15. Cash and Derivatives Market Development 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.

## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 16. Margin Funds on Derivatives Contracts

	Unaudited at 31 Mar 2004 \$'000	Audited at 31 Dec 2003 \$'000
The margin funds comprise:		
SEOCH Clearing Participants' margin funds	1,098,412	1,083,679
HKCC Clearing Participants' margin funds	<u>7,778,644</u>	<u>6,790,831</u>
	<u>8,877,056</u>	<u>7,874,510</u>
The assets of the margin funds comprise:		
Bank balances and time deposits	4,981,637	4,900,011
Listed securities deposited as alternatives to cash deposits, at market value	706,626	805,430
Listed non-trading securities, at fair value		
- debt securities	264,512	102,780
Unlisted non-trading securities, at fair value		
- debt securities	<u>2,924,281</u>	<u>2,066,289</u>
	<u>8,877,056</u>	<u>7,874,510</u>
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	<u>8,877,056</u>	<u>7,874,510</u>

### 17. 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 \$3,746,824,000 (31 December 2003: \$4,644,680,000) and \$4,081,286,000 (31 December 2003: \$4,779,904,000) respectively. These mainly represent the Group's CNS money obligations under the T+2 settlement cycle. The Group's CNS money obligations receivable represent 90 per cent (31 December 2003: 87 per cent) of the total accounts receivable, prepayments and deposits. CNS money obligations payable represent 82 per cent (31 December 2003: 84 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.

## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 18. Provisions

	<b>Reinstatement costs \$'000</b>	<b>Employee benefit costs \$'000</b>	<b>Total \$'000</b>
At 1 Jan 2004	24,578	23,525	48,103
Provision for the period	-	9,277	9,277
Amount used during the period	-	(8,317)	(8,317)
Amount paid during the period	(190)	(530)	(720)
At 31 Mar 2004	<u>24,388</u>	<u>23,955</u>	<u>48,343</u>
		<b>Unaudited at 31 Mar 2004 \$'000</b>	<b>Audited at 31 Dec 2003 \$'000</b>
Analysis of provisions:			
Current		<b>25,745</b>	25,011
Non-current		<b>22,598</b>	23,092
		<u><b>48,343</b></u>	<u>48,103</u>

### 19. Share Capital and Share Premium

		<b>Unaudited at 31 Mar 2004 \$'000</b>	<b>Audited at 31 Dec 2003 \$'000</b>	
Authorised:				
2,000,000,000 shares of \$1 each		<u><b>2,000,000</b></u>	<u>2,000,000</u>	
Issued and fully paid:				
	<b>No. of shares of \$1 each</b>	<b>Share capital \$'000</b>	<b>Share premium \$'000</b>	<b>Total \$'000</b>
At 1 Jan 2003	1,043,580,846	1,043,581	19,012	1,062,593
Shares issued under employee share option schemes	<u>5,418,000</u>	<u>5,418</u>	<u>35,326</u>	<u>40,744</u>
At 31 Dec 2003	1,048,998,846	1,048,999	54,338	1,103,337
Shares issued under employee share option schemes	<u>7,458,000</u>	<u>7,458</u>	<u>48,626</u>	<u>56,084</u>
At 31 Mar 2004	<u>1,056,456,846</u>	<u>1,056,457</u>	<u>102,964</u>	<u>1,159,421</u>

## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 19. Share Capital and Share Premium (continued)

Under the Pre-Listing Share Option Scheme (Pre-Listing 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. Following the declaration of a special dividend and final dividend for 2003, at the AGM held on 31 March 2004, shareholders of HKEx approved the adjustments to the subscription price and the contract size of the outstanding options granted under the Pre-Listing Scheme. The subscription price of the shares issuable under the options granted was adjusted from \$7.52 per share to \$6.88 per share and the aggregate contract size of the options granted but not yet exercised as at 31 March 2004 was adjusted from 6,615,465 shares to 7,078,000 shares.

Under the Post-Listing Share Option Scheme (Post-Listing Scheme) of HKEx, share options were granted to:

- (a) 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;
- (b) an employee on 14 August 2003 which are exercisable between 14 August 2005 and 13 August 2013 at an exercise price of \$13.60 per share;
- (c) an employee on 18 August 2003 which are exercisable between 18 August 2005 and 17 August 2013 at an exercise price of \$13.65 per share;
- (d) an employee on 15 January 2004 which are exercisable between 15 January 2006 and 14 January 2014 at an exercise price of \$18.90 per share; and
- (e) a number of employees on 31 March 2004 which are exercisable between 31 March 2006 and 30 March 2014 at an exercise price of \$16.96 per share.

At the AGM held on 31 March 2004, shareholders of HKEx approved the adjustments to the subscription price and the contract size of the options granted under the Post-Listing Scheme in (a) to (d) above that were not yet exercised prior to the AGM. The adjustments made to the first four option grants under the Post-Listing Scheme are as follows:

<b>Date of grant</b>	<b>Exercise price after adjustment</b>	<b>No. of shares issuable under the options granted before adjustment</b>	<b>No. of shares issuable under the options granted after adjustment</b>
2 May 2003	\$8.28	3,000,000	3,280,000
14 August 2003	\$12.45	1,000,000	1,094,000
18 August 2003	\$12.49	1,800,000	1,968,000
15 January 2004	\$17.30	1,000,000	1,094,000

During the period, Pre-Listing employee share options were exercised to subscribe for 7,458,000 shares (year ended 31 December 2003: 5,418,000) 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

### 19. Share Capital and Share Premium (continued)

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

	No. of shares issuable under the employee share options outstanding as at 1 Jan 2004	No. of shares issuable under the new employee share options granted during the period	No. of shares issuable under the employee share options granted pursuant to the adjustment approved at the AGM	No. of shares issuable under the employee share options lapsed during the period	No. of shares issued under the employee share options exercised during the period	No. of shares issuable under the employee share options outstanding as at 31 Mar 2004
Pre-Listing Scheme	14,171,626	-	462,535	(98,161)	(7,458,000)	7,078,000
Post-Listing Scheme	<u>5,800,000</u>	<u>6,688,000</u>	<u>636,000</u>	<u>-</u>	<u>-</u>	<u>13,124,000</u>
	<u>19,971,626</u>	<u>6,688,000</u>	<u>1,098,535</u>	<u>(98,161)</u>	<u>(7,458,000)</u>	<u>20,202,000</u>

Currently, 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 31 March 2004, the Group would have received \$229,450,340 in proceeds. The market value of the shares issued based on the closing price of \$16.70 per share on that date would have been \$337,373,400. The employees concerned under the Pre-Listing Scheme would have made a gain of \$9.82 per share, or, in aggregate, \$69,505,960. The executive director concerned under the Post-Listing Scheme would have made a gain of \$8.42 per share, or, in aggregate, \$27,617,600. The two employees concerned under the Post-Listing Scheme granted on 14 August 2003 and 18 August 2003 would have made a gain of \$4.25 per share, or, in aggregate, \$4,649,500 and \$4.21 per share, or, in aggregate, \$8,285,280 respectively.

In April 2004, the Hong Kong Society of Accountants issued a Hong Kong Financial Reporting Standard, HKFRS2: Share-based Payment, which covers the accounting treatment for employee share options. The new HKFRS2 is effective for accounting periods beginning on or after 1 January 2005.

## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 20. Revaluation Reserves

	Unaudited at 31 Mar 2004 \$'000	Audited at 31 Dec 2003 \$'000
Investment properties revaluation reserve (note b)	1,771	1,771
Other properties revaluation reserve (note b)	10,668	10,668
Investment revaluation reserve (note c)	<u>36,028</u>	<u>33,992</u>
	<u><u>48,467</u></u>	<u><u>46,431</u></u>

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

(b) Properties are revalued on a six-monthly basis at the end of June and December each year.

(c) Includes \$2,397,000, \$16,000 and \$409,000 (31 December 2003: \$1,619,000, \$11,000 and \$318,000 respectively) which are attributable to investments of the Clearing House Funds, the CDMD Fund and the Compensation Fund Reserve Account respectively.

### 21. Designated Reserves

	Unaudited at 31 Mar 2004 \$'000	Audited at 31 Dec 2003 \$'000
Clearing House Funds reserves		
- HKSCC Guarantee Fund reserve	255,912	255,912
- SEOCH Reserve Fund reserve	48,574	48,571
- HKCC Reserve Fund reserve	<u>261,752</u>	<u>261,183</u>
	566,238	565,666
Compensation Fund Reserve Account reserve	36,672	36,541
CDMD Fund reserve	914	914
Development reserve	<u>86,536</u>	<u>86,536</u>
	<u><u>690,360</u></u>	<u><u>689,657</u></u>

These reserves are segregated for their respective purposes.

## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 22. Retained Earnings

	Unaudited at 31 Mar 2004 \$'000	Audited at 31 Dec 2003 \$'000
At 1 Jan		
Retained earnings	1,560,940	3,221,321
Proposed and declared dividends	2,202,898	448,740
Profit for the period/year (note a)	313,519	691,765
Investment income net of expenses of Clearing House Funds for the period/year transferred to Clearing House Funds reserves	(572)	(8,430)
Investment income net of expenses of Compensation Fund Reserve Account for the period/year transferred to Compensation Fund Reserve Account reserve	(131)	(714)
Transfer from Development reserve	-	49,226
Dividends:		
2003 interim dividend paid	-	(188,452)
2003/2002 special and final dividends declared/paid	(2,202,898)	(448,740)
Dividends on shares issued for employee share options exercised after declaration of 2003/2002 special and final dividends	(15,661)	(647)
Dividend on shares issued for employee share options exercised after declaration of 2003 interim dividend	-	(231)
At 31 Mar/31 Dec	<u>1,858,095</u>	<u>3,763,838</u>
Representing:		
Retained earnings	1,858,095	1,560,940
Proposed and declared dividends	-	2,202,898
At 31 Mar/31 Dec	<u>1,858,095</u>	<u>3,763,838</u>

- (a) The Group's profit for the period/year includes a net deficit attributable to investment income net of expenses of the Clearing House Funds, Compensation Fund Reserve Account and CDMD Fund for an aggregate amount of \$820,000 (year ended 31 December 2003: surplus of \$6,938,000).



## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 23. Commitments

Commitments in respect of capital expenditures

	<b>Unaudited at 31 Mar 2004 \$'000</b>	Audited at 31 Dec 2003 \$'000
Contracted but not provided for	<b>18,182</b>	18,359
Authorised but not contracted for	<b>65,343</b>	72,275
	<b><u>83,525</u></b>	<u>90,634</u>

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

### 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 and liabilities to mitigate risks arising from fluctuations in exchange rates. As at 31 March 2004, the total nominal value of outstanding forward foreign exchange contracts amounted to HK\$342 million (31 December 2003: HK\$322 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. As at 31 March 2004, there were outstanding claims received in respect of 12 defaulted Stock Exchange Participants (31 December 2003: 13).

## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 25. Contingent Liabilities (continued)

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 expired on 3 October 2003 and no claims had been received in response to that notice. Claims made after the claims period shall, unless the Stock Exchange otherwise determines, be barred. As at 31 March 2004, no such claims had been received.

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. In accordance with the provisions of the SFO, deposits to the Commodity Exchange Compensation Fund had been returned to the Futures Exchange by the SFC in January 2004. The Futures Exchange had in turn reimbursed holders of Futures Exchange Trading Rights their contributions to the Commodity Exchange Compensation Fund. Existing deposits to the Unified Exchange Compensation Fund would be returned to the Stock Exchange in accordance with the provisions of the SFO. There is no 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 438 trading Participants as at 31 March 2004 (31 December 2003: 437) default, the maximum contingent liability of the Stock Exchange under the indemnity will amount to \$88 million (31 December 2003: \$87 million).
- (c) HKEx gave an undertaking on 6 March 2000 in favour of HKSCC to contribute an amount not exceeding \$50 million in the event of HKSCC being wound up while it is a wholly-owned subsidiary of HKEx or within one year after HKSCC ceases to be a wholly-owned subsidiary of HKEx, for payment of the debts and liabilities of HKSCC contracted before HKSCC ceases to be a wholly-owned subsidiary of HKEx, and for the costs, charges and expenses of winding up.

## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 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) Exchange Participants for buying shares on behalf of HKSCC. 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 Exchange Participants for buying shares on behalf of HKSCC are all undertaken in the ordinary course of business of the Group on the standard terms and conditions applicable to all other Exchange Participants and Clearing Participants, listed companies and Exchange Participants for buying shares on behalf of HKSCC.

In addition to the above, one of the subsidiaries, the Futures Exchange, 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 three-month period amounted to \$508,008 (2003: \$521,554) and the lease was entered into on normal commercial terms. In addition, \$159,207 (2003: \$173,780) was paid during the three-month period for air conditioning services and \$13,158 (2003: \$13,425) for premises cleaning services to The Great Eagle Properties Management Company Limited and Sun Fook Kong Housing Services Limited respectively of which Dr K S Lo was a director.

During the period, share registration service fees amounted to \$106,728 (2003: \$36,550) were paid to and dividends and loan interest amounted to \$2,400,140 and \$Nil respectively (2003: \$Nil and \$20,652 respectively) were received from an associated company, Computershare Hong Kong Investor Services Limited.

During the three months ended 31 March 2004, bank charges of \$1,471,120 (2003: \$666,952) were paid to The Hongkong & Shanghai Banking Corporation Limited where Dr K S Lo was a non-executive director.

During the corresponding period in 2003, consultancy fee of \$862,285 was paid 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.

Save as aforesaid, HKEx had entered into other transactions with companies where there are common directors but the amount was immaterial.

## NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

### 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 accounts.

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

### 28. Events after Balance Sheet Date

The 2003 special and final dividends of \$2,219 million were paid on 14 April 2004. As the amount of Corporate Funds available for investment thereafter has been reduced by this amount, the Group's investment income in future is unlikely to be sustainable at the level achieved in the first quarter of 2004.

## OTHER INFORMATION

(Financial figures are expressed in Hong Kong dollars)

### Outstanding Share Options

Details of the share options outstanding as at 31 March 2004 under the Pre-Listing Scheme and Post-Listing Scheme were as follows:

#### (a) Pre-Listing Scheme

	Date of grant	Exercise price	No. of shares				Exercise period
			issuable as at 1 January 2004	issued during the three months ended 31 March 2004	lapsed during the three months ended 31 March 2004	issuable as at 31 March 2004	
Aggregate total for employees (note 1)	20 June 2000	\$6.88 (note 2)	14,171,626	7,458,000 (note 3)	98,161 (note 4)	7,078,000 (note 2)	6 March 2002 – 30 May 2010 (note 5)

#### (b) Post-Listing Scheme

Date of grant	Exercise price	No. of shares issuable under the options granted	Option value	No. of shares issuable under the options granted as at 31 March 2004	Exercise period
<b>Director</b> (note 6)					
2 May 2003	\$8.28 (note 7)	3,280,000 (note 7)	\$8,036,000 (note 8)	-	2 May 2005 – 1 May 2013 (note 9)
<b>Employees</b> (note 1)					
14 August 2003	\$12.45 (note 7)	1,094,000 (note 7)	\$4,561,980 (note 8)	-	14 August 2005 – 13 August 2013 (note 10)
18 August 2003	\$12.49 (note 7)	1,968,000 (note 7)	\$8,226,240 (note 8)	-	18 August 2005 – 17 August 2013 (note 11)
15 January 2004	\$17.30 (note 7)	1,094,000 (note 7)	\$6,564,000 (note 8)	-	15 January 2006 – 14 January 2014 (note 12)
31 March 2004 (note 13)	\$16.96 (note 14)	5,688,000	\$32,250,960 (note 8)	-	31 March 2006 – 30 March 2014 (note 15)

Notes:

1. Employees working under employment contracts that were regarded as “continuous contracts” for the purpose of the Employment Ordinance of Hong Kong.
2. At the annual general meeting of HKEx held on 31 March 2004 (AGM), shareholders of HKEx approved the adjustments to the subscription price and the contract size of the unexercised options granted under the Pre-Listing Scheme and those granted under the Post-Listing Scheme prior to the AGM. The subscription price of the shares issuable under the unexercised options granted under the Pre-Listing Scheme is adjusted from \$7.52 per share to \$6.88 per share and the aggregate contract size of the unexercised options granted is adjusted from 6,615,465 shares to 7,078,000 shares.
3. The weighted average closing price immediately before the dates on which the options were exercised was \$20.11.
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 option was granted to Mr Chow Man Yiu, Paul, a Director and the Chief Executive of HKEx.
7. At the AGM, shareholders of HKEx approved the adjustments to the subscription price and the contract size of the unexercised options granted under the Post-Listing Scheme prior to the AGM. Adjustments made to the four unexercised options granted under the Post-Listing Scheme prior to the AGM are as follows:

Date of grant	Exercise price before adjustment	Exercise price after adjustment	No. of shares issuable under the options granted before adjustment	No. of shares issuable under the options granted after adjustment	Closing price immediately before the date on which the option was granted	Closing price immediately before the date on which the option was adjusted
2 May 2003	\$9.05	\$8.28	3,000,000	3,280,000	\$9.10	\$16.85
14 August 2003	\$13.60	\$12.45	1,000,000	1,094,000	\$13.95	\$16.85
18 August 2003	\$13.65	\$12.49	1,800,000	1,968,000	\$13.35	\$16.85
15 January 2004	\$18.90	\$17.30	1,000,000	1,094,000	\$19.00	\$16.85

8. According to the Binomial Option Pricing Model, the value of the options granted during the period under review and the revaluation of the options granted in 2003 were as follows:

	Date of grant				
	<u>2 May 2003</u>	<u>14 August 2003</u>	<u>18 August 2003</u>	<u>15 January 2004</u>	<u>31 March 2004</u>
<u>Option value</u>					
Before adjustment	\$8,010,000	\$4,560,000	\$8,226,000	\$6,550,000	\$32,250,960
After adjustment	\$8,036,000	\$4,561,980	\$8,226,240	\$6,564,000	(note 13)
<u>Variables</u>					
Risk Free Rate (being the yield of 10-year Exchange Fund Notes)	4.3% as at 30 April 2003	4.84% as at 14 August 2003	4.76% as at 18 August 2003	3.96% as at 15 January 2004	3.78% as at 31 March 2004
Expected Volatility (annualized volatility for 1 year immediately preceding the grant date)	36%	36%	36%	34%	35%
Expiration of the option	10 years from 2 May 2003	10 years from 14 August 2003	10 years from 18 August 2003	10 years from 15 January 2004	10 years from 31 March 2004
Expected ordinary dividend	5.6% (2003 prospective dividend yield of the shares as at 2 May 2003)	4.49% (2003 prospective dividend yield of the shares as at 14 August 2003)	4.47% (2003 prospective dividend yield of the shares as at 18 August 2003)	3.23% (2004 prospective dividend yield of the shares as at 15 January 2004)	3.59% (2004 prospective dividend yield of the shares as at 31 March 2004)

The above calculation is based on the assumption that 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 respective periods.

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.

9. 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.
10. Option granted is exercisable between 14 August 2005 to 13 August 2013, in tranches of 25 per cent each reaching 100 per cent as from 14 August 2008.
11. Option granted is exercisable between 18 August 2005 to 17 August 2013, in tranches of 25 per cent each reaching 100 per cent as from 18 August 2008.
12. Option granted is exercisable between 15 January 2006 to 14 January 2014, in tranches of 25 per cent each reaching 100 per cent as from 15 January 2009.
13. Options granted on 31 March 2004 under the Post-Listing Scheme, and are not subject to the adjustments as referred to in note 7.
14. The closing price immediately before the date on which the options were granted was \$16.85.
15. Options granted are exercisable between 31 March 2006 to 30 March 2014, in tranches of 25 per cent each reaching 100 per cent as from 31 March 2009.

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

As at 31 March 2004, the Directors, the Chief Executive and their respective associates had the following interests in the shares and underlying shares of HKEx, as recorded in the register maintained by HKEx pursuant to Section 352 of the SFO:

### (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 31 March 2004, 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 3,280,000, which represents approximately 0.31 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 \$8.28 per share. The number of shares issuable under the option granted and the exercise price have been adjusted in accordance with the resolution passed by shareholders of HKEx at the AGM. Please refer to note 7 under "Outstanding Share Options" for more 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 31 March 2004, 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 31 March 2004, the Directors are not aware of any party who was directly or indirectly interested in 5 per cent or more of the issued share capital of HKEx, as recorded in the register required to be kept by HKEx under Section 336 of the SFO.

### **Minority Controllers**

Under 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 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 31 March 2004, the Minority Controllers were in aggregate holding 53.7 per cent of the issued share capital of HKEx (31 March 2003 : 42.1 per cent).

### **Corporate Governance**

The Audit Committee has reviewed the unaudited condensed consolidated accounts for the three months ended 31 March 2004.

Management has appointed the external auditors to carry out certain agreed upon procedures in accordance with Statement of Auditing Standards 710 "Engagements to perform agreed upon procedures regarding financial information" issued by the Hong Kong Society of Accountants on the unaudited condensed consolidated accounts for the three months ended 31 March 2004.

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 three months ended 31 March 2004, in compliance with Appendix 14 of the Listing Rules.

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

During the three months ended 31 March 2004, HKEx had not redeemed, and neither HKEx nor any of its subsidiaries had purchased or sold any of HKEx's listed securities.

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

Hong Kong, 12 May 2004