

Management Discussion and Analysis

(Financial figures are expressed in Hong Kong Dollar)

BUSINESS REVIEW

LISTING

Consultations on Enhancing Listing Regulation

Since the submission of a combined response to the Consultation Paper on Proposed Amendments to the Securities and Futures Ordinance to give Statutory Backing to Major Listing Requirements published by the Financial Services and the Treasury Bureau (“FSTB”) and the Consultation Paper on Proposed Amendments to the Securities and Futures (Stock Market Listing) Rules issued by the Securities and Futures Commission (“SFC”), Hong Kong Exchanges and Clearing Limited (“HKEx”) has been working with the FSTB and the SFC on further developing the proposals in a manner which would minimise disruption to the market and achieve the objective of giving “teeth” to major listing requirements.

Proposed New Structure for Listing Decision-Making

The consultation on the New Structure for Listing Decision-Making issued on 18 February 2005 for soliciting public views on the overall listing decision-making structure together with the proposed amendments to Chapters 2A and 2B of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (“Listing Rules”) for implementing such a structure closed on 22 April 2005. The objective of the proposed new structure is to put in place a simpler administrative framework for listing decision-making whilst retaining the checks and balances for minimising and managing regulatory risk including potential conflicts of interest within HKEx and its subsidiaries (“Group”).

A total of 18 submissions were received from 17 respondents, which have been published on the HKEx website. Comments are being analysed, and the consultation conclusions and recommended amendments to the Listing Rules and the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited for implementing the conclusions will be published in the second half of 2005.

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

The Main Board Listing Committee has approved a proposal to require Main Board issuers to publish a notification announcement in newspapers instead of the full version of the announcement. The full version will be posted on the HKEx website, the issuer’s website and/or other communication channels. HKEx is finalising an implementation plan with the view to assisting the issuers, the professional advisers, the market participants and the investors at large to familiarise themselves with this mode of dissemination of regulatory information by Main Board issuers. A policy statement will be made in the near future which will provide an opportunity for the market to comment, among other things, on certain aspects of the proposed transitional arrangements including the form and content of the proposed notification announcement. The requirement of publishing notification announcements will be implemented subject to the system and operational readiness and approval of the relevant rule amendments by the SFC.

Review of the Growth Enterprise Market (“GEM”)

HKEx has recently established an internal working group to co-ordinate studies and develop proposals for the comprehensive review of the GEM. Informal views will also be sought from stakeholders including shareholders, issuers, investors, market practitioners and participants, and the Government.

Publication of Listing Committee Annual Report

The annual report of the Main Board and GEM Listing Committees (collectively the “Listing Committees”) was published on 7 July 2005 and posted on the HKEx website. The report provides an account of the work of the Listing Committees during the service term of their members from 1 May 2004 to 13 May 2005 with the aim at enhancing the transparency of the regulatory functions discharged by the Listing Committees and The Stock Exchange of Hong Kong Limited (“Stock Exchange”).

CASH MARKET

Market Performance

In the first half of 2005, 19 companies were listed on the Main Board and two on the GEM. Total capital raised, including post-listing funds, reached \$124.7 billion. As at 30 June 2005, 901 companies were listed on the Main Board with a total market capitalisation of \$6,893 billion, and 203 companies were listed on the GEM with a total market capitalisation of \$65 billion. The market capitalisation of the Main Board and the GEM exceeded \$7,000 billion for the first time on 13 July 2005. Total funds raised through initial public offerings (“IPOs”) (both the Main Board and the GEM) in one month also reached a new high of exceeding \$53.3 billion. In addition, there were 927 derivative warrants, seven Exchange Traded Funds (“ETFs”) (excluding two ETFs for trading only) and 164 debt securities listed on the Stock Exchange as at the end of June 2005. Average daily turnover in the first half of 2005 was \$16.8 billion on the Main Board and \$78 million on the GEM.

Renovation of the Trading Hall

The renovation of the Trading Hall commenced on 18 July 2005. Part of the hall is now a temporary trading area including back-up trading facilities for Exchange Participants (“EPs”).

New trading booths will be provided in the renovated Trading Hall at a monthly user fee of \$2,800 per trading booth for a binding three-year period. The renovation of the trading area will be ready by the end of this year whilst the exhibition and conference facilities of the Trading Hall will be in operation by the second quarter of 2006.

Reduction of Minimum Trading Spreads

Following the publication of the consultation conclusions on 4 February 2005, the phase one reduction of trading spreads involving shares priced above \$30 was implemented on 4 July 2005 affecting a total of 29 shares. Various trading parameters of the trading system have been enhanced to support the change, and so far, no irregularities were noted. Trading spreads for shares priced at or below \$30 remain unchanged. Data is being collected for analysing the market impact.

Callable Bull/Bear Contracts

HKEx is proposing the introduction of Callable Bull/Bear Contracts (“CBBC”) to give the Hong Kong market an additional choice of investment product. HKEx has held extensive discussions with issuers and overseas exchanges on the development of CBBC and consulted market practitioners, including issuers, brokers and industry associations, on the infrastructure and the market model to be adopted for the launch and trading of CBBC. Issuers have expressed interest in issuing CBBC with different kinds of underlying assets and market practitioners have also indicated favourable response to trading the product. HKEx is discussing with the SFC on the approval of CBBC for listing and trading in Hong Kong.

Development of the ETFs Market

As at the end of June 2005, there were nine ETFs trading on the Stock Exchange, including two ETFs listed in June 2005. Average daily turnover in the first half of 2005 was \$64 million.

The Hang Seng FTSE/Xinhua China 25 Index ETF commenced trading on 8 June 2005 and has closely tracked the performance of the FTSE/Xinhua China 25 Index (“FXI China 25”) which consists of the 25 largest and most liquid Mainland enterprises (H-shares and Red Chips) listed on the Stock Exchange.

On 21 June 2005, the first bond ETF, ABF Hong Kong Bond Index Fund, made its debut in Asia. It is designed to provide investment results that correspond to the total return of the iBoxx ABF Hong Kong Index, an index that comprises 70 Hong Kong Dollar bond issues with an average maturity of slightly more than three years.

The ABF Pan Asia Bond Index Fund was also listed on 7 July 2005. It tracks the performance of the iBoxx Pan-Asia Bond Index, a US Dollar-denominated index of Asian currency bonds. The fund is traded and settled on the Stock Exchange in US Dollar.

The two ABF funds are key components of an initiative of 11 Asian central banks and monetary authorities to support the further development of the region’s bond markets.

With a view to enhancing the market making arrangements for ETF, trading rules that generally tighten the market making obligations of Securities Market Makers for each group of ETF were proposed by HKEx and approved by the SFC, and are expected to take effect in the latter part of this year.

Exemptions on Dealings in Suspended Securities

HKEx has proposed that exemptions be given to placing and fund raising activities by the EPs from the current prohibition of dealings in suspended securities under Rule 539 of the Rules of the Exchange. The relevant rule amendments have been submitted to the SFC for approval.

Market Value of All Listed Companies – Main Board & GEM

As at the end of June

	2005 (\$ mil)	2004 (\$ mil)	% Change
Main Board			
Finance	2,290,924.52	2,027,248.19	13.01
Utilities	434,193.55	379,578.60	14.39
Properties	811,456.63	605,261.01	34.07
Consolidated Enterprises	2,088,019.81	1,532,319.44	36.27
Industrials	1,176,998.78	887,541.33	32.61
Hotels	70,547.99	41,088.50	71.70
Miscellaneous	21,185.85	9,537.16	122.14
Sub-total	6,893,327.13	5,482,574.23	25.73
GEM	65,376.11	72,670.33	(10.04)
Total	6,958,703.24	5,555,244.56	25.26

Number of Listed Companies – Main Board & GEM

As at the end of June

	2005	2004	% Change
Main Board			
Finance	80	79	1.27
Utilities	15	14	7.14
Properties	100	99	1.01
Consolidated Enterprises	289	279	3.58
Industrials	399	380	5.00
Hotels	12	13	(7.69)
Miscellaneous	6	5	20.00
Sub-total	901	869	3.68
GEM	203	199	2.01
Total	1,104	1,068	3.37

Number of Listed Securities – Main Board & GEM*As at the end of June*

	2005	2004	% Change
Ordinary shares	1,104	1,068	3.37
Preference shares	4	4	0
Warrants	953	840	13.45
– Equity warrants	26	37	(29.73)
– Derivative warrants	927	803	15.44
Equity Linked Instruments	0	33	(100.00)
Debt securities	164	151	8.61
Unit trusts	10	8	25.00
Total	2,235	2,104	6.23

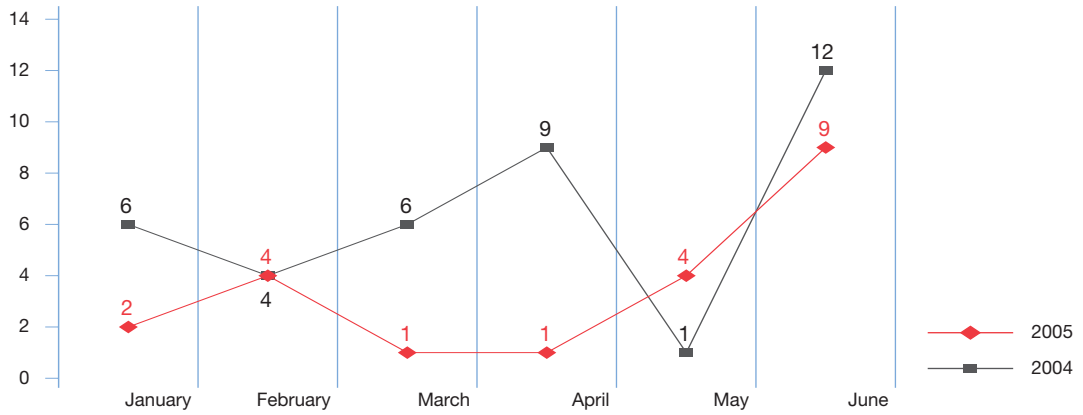
Market Value by Type of Securities – Main Board & GEM*As at the end of June*

	2005 (\$ mil)	2004 (\$ mil)	% Change
Equities	6,958,703.24	5,555,244.56	25.26
Warrants	69,622.77	56,348.30	23.56
– Equity warrants	2,499.05	1,222.24	104.46
– Derivative warrants	67,123.72	55,126.06	21.76
Equity Linked Instruments	0.00	1,049.46	(100.00)
Debt securities	431,586.37*	407,182.40*	5.99
Unit trusts	N/A	N/A	N/A
Total	7,459,912.38	6,019,824.72	23.92

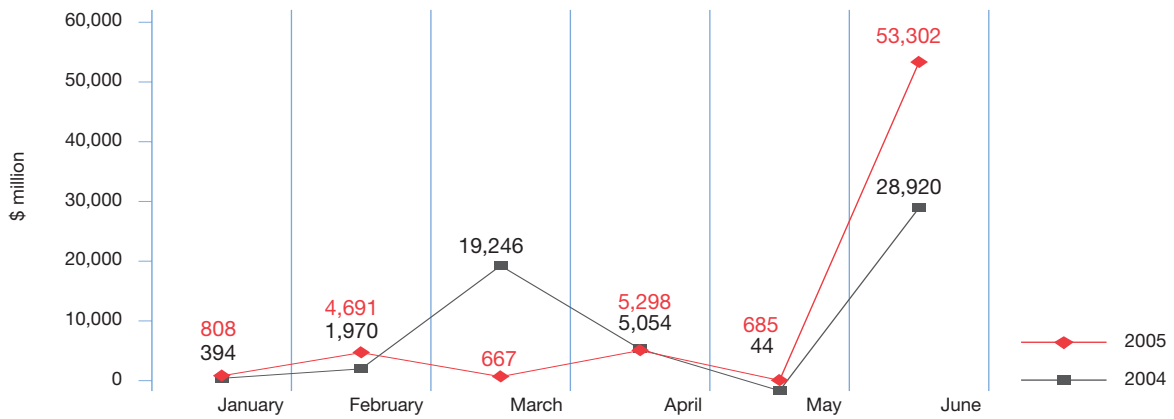
* *Nominal value***Turnover Value by Type of Securities – Main Board & GEM***For the six months ended 30 June*

	2005 (\$ mil)	2004 (\$ mil)	% Change
Equities	1,700,243.24	1,793,286.58	(5.19)
Warrants	331,105.83	246,955.45	34.08
– Equity warrants	1,644.03	1,152.43	42.66
– Derivative warrants	329,461.80	245,803.02	34.03
Equity Linked Instruments	1.02	168.67	(99.40)
Debt securities	7.72	23.59	(67.29)
Unit trusts	7,728.43	13,655.14	(43.40)
iShares	6.05	6.85	(11.61)
Total	2,039,092.29	2,054,096.28	(0.73)

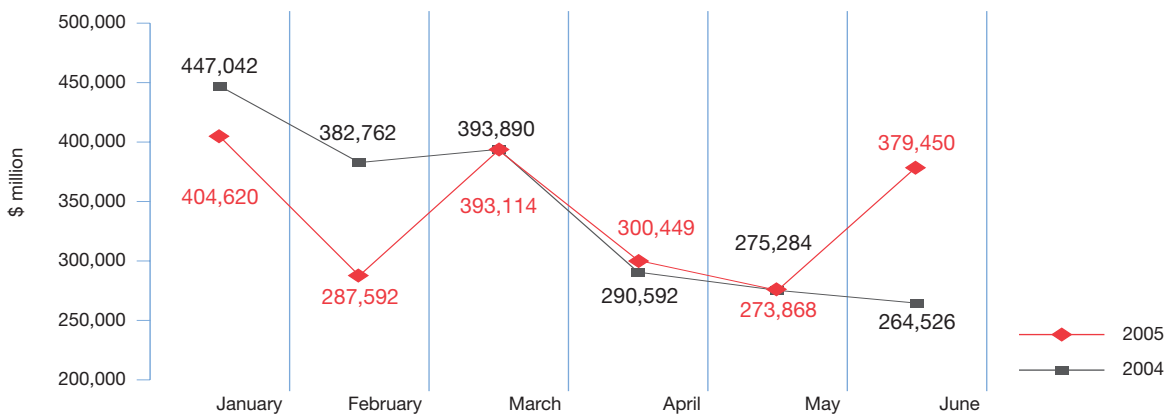
Number of Newly Listed Companies – Main Board & GEM



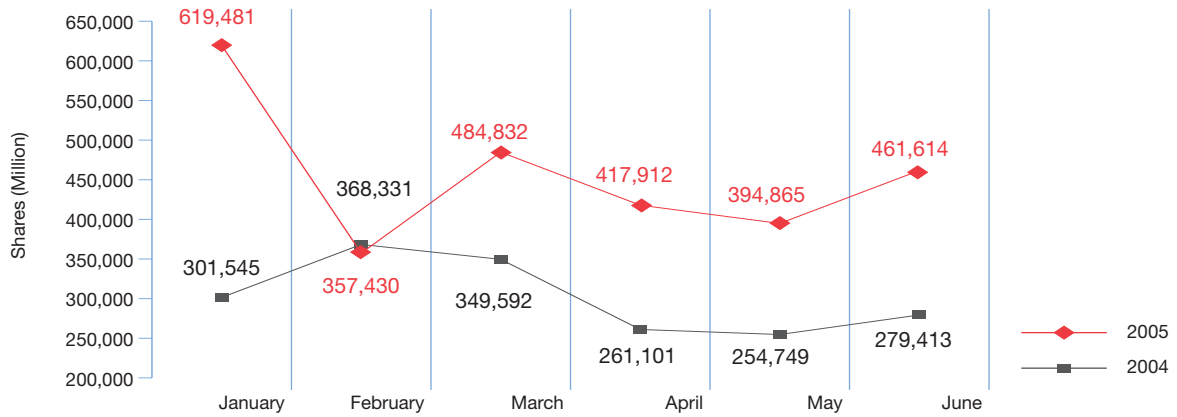
Funds Raised by Newly Listed Companies – Main Board & GEM



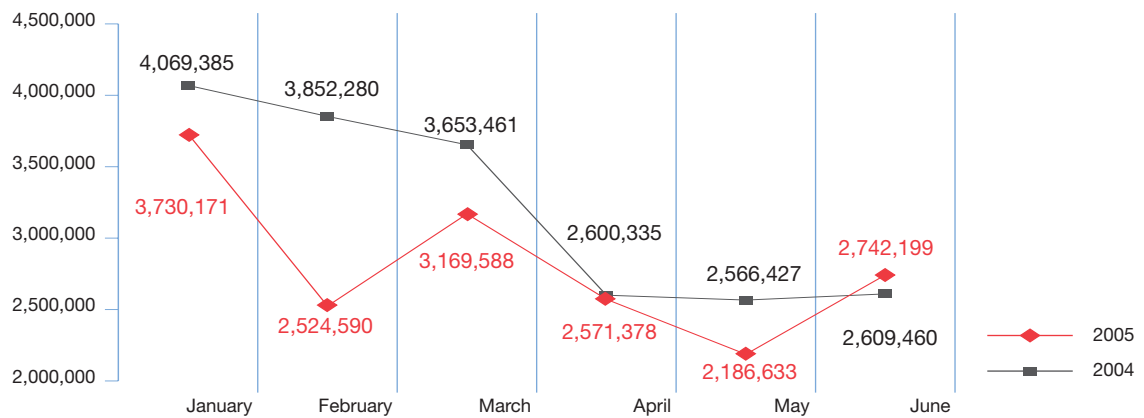
Monthly Turnover (Value) – Main Board & GEM



Monthly Turnover (Volume) – Main Board & GEM

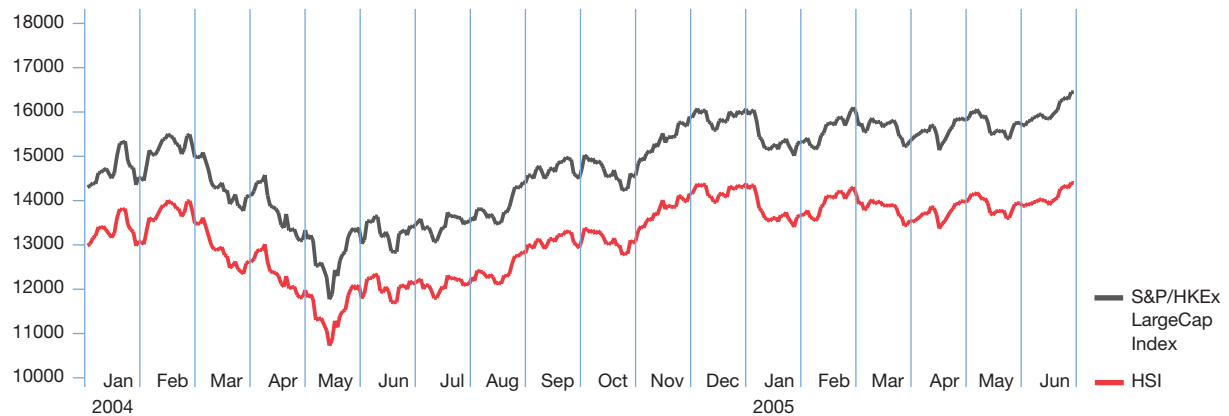


Number of Transactions – Main Board & GEM



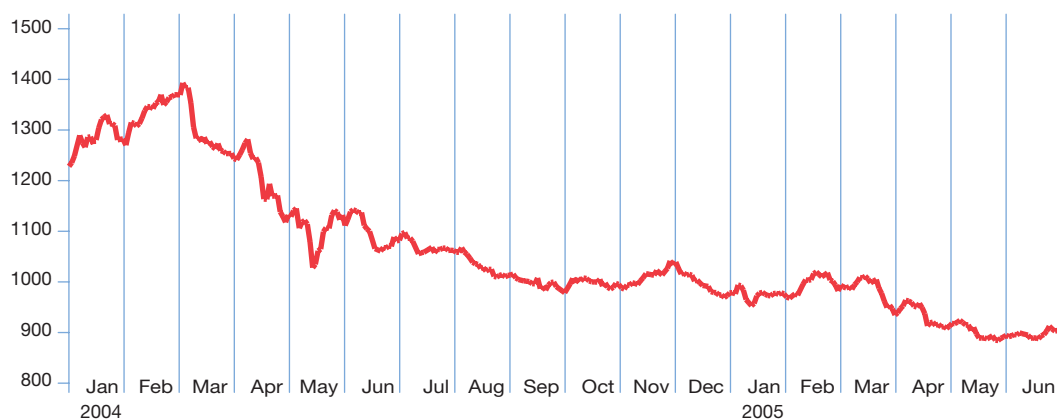
Hang Seng Index (“HSI”) and S&P/HKEx LargeCap Index

January 2004 – June 2005



S&P/HKEx GEM Index

January 2004 – June 2005



DERIVATIVES MARKET

Market Performance

Products	Products Achieved Record High in 2005 (up to 30 June)			
	Daily Volume		Open Interest	
	Date	Number of Contracts	Date	Number of Contracts
Hang Seng Index Options	22 Jun 2005	26,412	28 Jun 2005	228,842
Mini-Hang Seng Index Futures	–	–	29 Jun 2005	5,610
H-shares Index Futures	23 Feb 2005	31,770	29 Mar 2005	45,212
H-shares Index Options	29 Apr 2005	3,098	27 Jun 2005	48,987
Stock Options	–	–	28 Jun 2005	1,106,093

Product and Market Development

FXI China 25 Futures and Options contracts commenced trading on 23 May 2005. The new contracts were introduced to provide products on a broad-based stock index covering most of the large Mainland enterprises, and serve as trading and hedging tools for investors in Mainland enterprises and for those who invest in other products linked to FXI China 25, such as ETFs, warrants, and over-the-counter products. To support the trading of FXI China 25 Futures and H-shares Index Futures, HKEx has made an application to the US Commodity Futures Trading Commission for no-action relief concerning the offering of these futures contracts in the US.

A series of enhancement measures for the stock options market have been implemented in stages with effect from 1 February 2005. Market makers were recruited and equipped with upgraded communication lines to provide continuous quotes in eight designated stock option classes to increase market liquidity. More choices in strike prices were offered to investors by narrowing the strike intervals in all expiry months of seven option classes. The trading tariff of Tier 1 option classes was reduced from \$5 to \$3 per contract. Two new stock option classes were launched on 11 July 2005 to meet market demand. Since 1 February 2005, stock options have shown significant increases in average daily turnover, and open interest has set successive new records.

In view of the demand from market makers for more Options Hedging Participants to perform hedging transactions for their stock option trades, the restriction on the number of Options Hedging Participants to be appointed by a market maker was lifted from 21 April 2005.

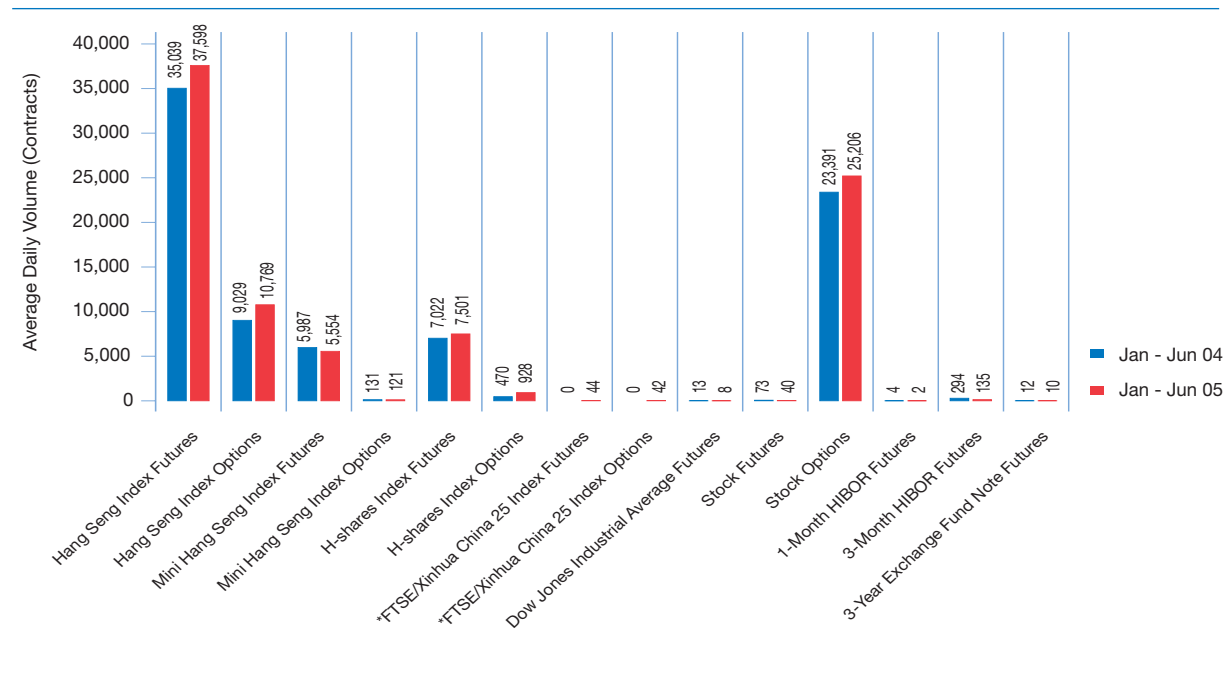
HKEx introduced preventive measures to regulate excessive order-book activity being entered into Hong Kong Futures Automated Trading System (“HKATS”) to ensure smooth trading functioning for all market participants. HKEx also enhanced the audit trail function in HKATS to further strengthen market monitoring and supervision capabilities. In view of the continuous growth in business for the past few years, HKEx is reviewing HKATS system capacity and is planning for a system upgrade in the fourth quarter.

Education and Marketing

To promote the stock options market, HKEx introduced a joint education programme under which nine participating Option Trading EPs were sponsored by HKEx to conduct public investor seminars on stock options, which were well attended. In addition, HKEx co-organised two seminars and nine workshops on 21 May 2005 to promote FXI China 25 Futures and Options.

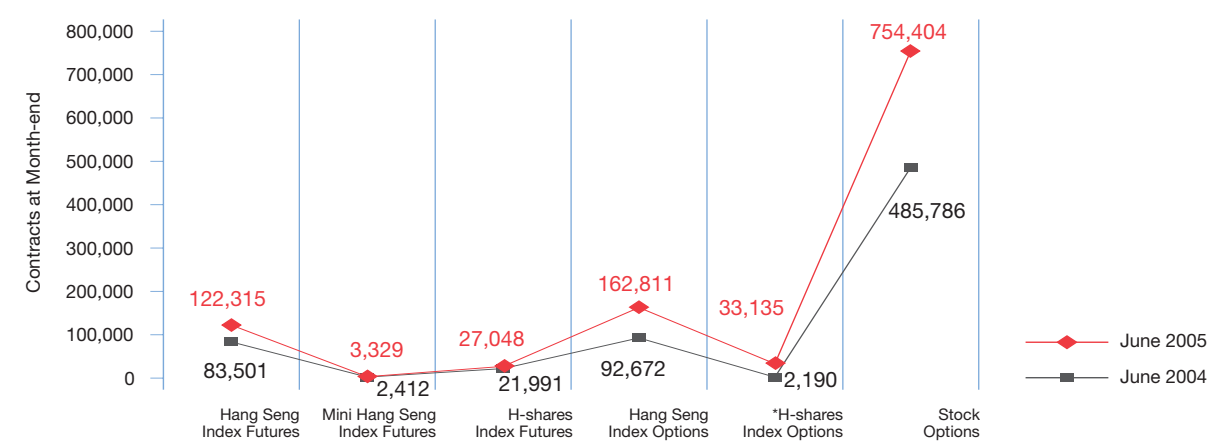
To promote HKEx as a quality marketplace to trade China equity derivatives, HKEx made overseas marketing trips to New York, Chicago and Tokyo, and arranged meetings with management of the affiliates and clients of EPs, as well as potential investors.

Volume of Derivatives Products (Contracts)



* Commenced trading on 23 May 2005

Open Interest of Derivatives Products (Month-end, Contracts)



* Commenced trading on 14 June 2004

Exchange Participants and Trading Right Holders Status

As at 30 June 2005

	Stock Exchange	Futures Exchange
Exchange Participants	464	129
<i>Trading</i>	425	129
<i>Non-trading</i>	39	0
Trading Right Holders	56	62
<i>Corporate</i>	2	53
<i>Individual</i>	54	9

CLEARING

Scripless Project

Hong Kong Securities Clearing Company Limited (“HKSCC”) is working with the Federation of Share Registrars to finalise the operational arrangements and system changes for the implementation of the initial phase of scripless, i.e. dematerialisation of physical scrip in the Central Clearing and Settlement System (“CCASS”) Depository. The SFC and the FSTB are in the process of finalising the relevant legislative changes for the implementation of scripless in Hong Kong. Subject to the enactment of the enabling legislation, initial phase of dematerialisation will start in 2006.

Clearing Fees Reductions

Effective 1 February 2005, HKSCC has waived its stock custody fee of \$0.012 per board lot charged on a monthly basis for delisted securities and securities in prolonged suspension. HKSCC has also extended the fee waiver on Short Message Service for the Investor Participant (“IP”) accounts up to the end of June 2006 and abolished the requirement of \$1,000 initial deposit upon the opening of an IP account with effect from 1 July 2005.

HKFE Clearing Corporation Limited (“HKCC”) and The SEHK Options Clearing House Limited (“SEOCH”) have both abolished the Derivatives Clearing and Settlement System (“DCASS”) standard instruction input/processing fees of \$1.5 per transaction per side with effect from 1 March 2005, and implemented several other fees changes with effect from 1 June 2005. Interest retention at the rate of 1.2 per cent per annum for HKCC and that of 2 per cent per annum for SEOCH on margin deposits were abolished, and interest is now paid to Participants at the prevailing bank savings deposit rate on their cash margin deposits (however, a negative interest will be charged if the bank savings deposit rate is negative). In addition, the accommodation charges on utilised non-cash collateral levied by HKCC and SEOCH have been reduced respectively from 1.2 per cent per annum and 2 per cent per annum to 0.5 per cent per annum.

Clearing Services Enhancements

HKSCC upgraded its Clearing Service Call Centre and Interactive Voice Recording System (“IVRS”) on 31 January 2005. The hotline for CCASS IPs has been revamped to streamline the call flow and make it more user-friendly. The input and enquiry functions of the IVRS are now available 24 hours a day, seven days a week.

The CCASS deadline for its Participants to submit their voting instructions has been extended to the business day before the relevant meeting date with effect from 4 April 2005. The CCASS deadline for its Participants to submit their corporate action instructions has been extended to a time much closer to the issuer’s deadline effective 8 August 2005.

The automation of the cash prepayment service, through which CCASS Participants are able to make payments through the Real Time Gross Settlement payment mechanism operated by Hong Kong Interbank Clearing Limited, has been launched on 8 August 2005. Such automated payment transactions will be exempted from the existing cash prepayment service fee of \$100 per transaction. Further improvements to the CCASS nominee services are planned for implementation in early 2006.

Risk Management Policies Harmonisation

A comprehensive review of the clearing houses’ collateral policy was completed in the first quarter of 2005. The new policy, which will broaden the eligible collateral types for the Derivatives Market and largely harmonise various collateral management measures of the three clearing houses, is expected to be implemented in the second half of 2005.

In addition, the capital requirements of each category of clearing participants have been reviewed. Relevant rule amendments will be made to simplify the structure of the participants and harmonise the capital requirements for clearing participants of the two derivatives clearing houses.

The three clearing houses, namely HKSCC, HKCC and SEOCH, act as the central counterparties for clearing trades concluded on the Stock Exchange and Hong Kong Futures Exchange Limited (“Futures Exchange”). Insurance cover is one of the risk management measures adopted to cover counterparty risk, which has been renewed for another year while an additional cover of \$78 million has been secured for HKCC to further strengthen its financial backing and reduce the financial burden on its Participants.

CCASS Statistics (Up to six months ended 30 June)

	2005	2004
Average Daily Exchange Trades Handled by CCASS		
– Number of trades	139,870	158,616
– Value of trades	\$16.9 billion	\$16.8 billion
– Share quantity involved	22.6 billion	14.9 billion
Average Daily Settlement Instructions (“SIs”) Settled by CCASS		
– Number of SIs	24,201	25,641
– Value of SIs	\$40.9 billion	\$42.0 billion
– Share quantity involved	13.9 billion	12.1 billion
Average Daily Investor SIs (“ISIs”) Settled by CCASS		
– Number of ISIs	342	460
– Value of ISIs	\$93.5 million	\$116.7 million
– Share quantity involved	75.0 million	80.0 million
Average Daily Settlement Efficiency of Continuous Net Settlement (“CNS”) Stock Positions on Due Day (T+2)	99.81%	99.69%
Average Daily Settlement Efficiency of CNS Stock Positions on the Day following the Due Day (T+3)	99.98%	99.98%
Average Daily Buy-ins Executed on T+3		
– Number of brokers involved	7	10
– Number of buy-ins	7	11
– Value of buy-ins	\$1.7 million	\$4.1 million
Shares Deposited in the CCASS Depository		
– Number of shares	1,234.6 billion	1,163.7 billion
– Percentage of total issued share capital of the admitted securities	60.55%	58.61%
– Value of shares	\$2,621.7 billion	\$1,984.8 billion
– Percentage of the total market capitalisation of the admitted securities	35.47%	33.39%

BUSINESS DEVELOPMENT AND INVESTOR SERVICES

Conferences and Seminars for Prospective Issuers

To promote Hong Kong as the largest fund-raising market in Asia and the Stock Exchange as a premier capital market for the Mainland and international companies, HKEx has co-organised a conference for the Japanese business community and participated in a conference during the Hebei-Hong Kong week organised by the Hebei Provincial Government jointly with the Government of the Hong Kong Special Administrative Region in June.

HKEx Investor Conference and Investor Education

HKEx organised its first half-day investor conference for individual investors at the Hong Kong Convention and Exhibition Centre on 2 April 2005. The conference provided a forum for senior HKEx officials to have a direct dialogue with the investing public on the present and future roles and functions of HKEx. The presentation materials of the various speakers and answers to questions raised by the participants at the conference have been posted on the HKEx website.

Seminars for introducing HKEx's new products have been held from time to time jointly with professional organisations. HKEx has also provided mentorship to university students and received delegations from different countries to facilitate their better understanding of the various aspects of the Hong Kong capital market.

Training Programmes for Listed Mainland Enterprises

It is our belief that continual training for listed companies' management is pivotal to upkeeping the best corporate governance practices among our issuers. HKEx has therefore organised three intensive training programmes in Hong Kong for the senior management of Mainland enterprises early this year. The training curriculum focused on the new requirements under the International Financial Reporting Standards ("IFRSs") and the amendments to the Listing Rules relating to the Code on Corporate Governance Practices and the Corporate Governance Report. Another training programme was held at HKEx's Beijing Representative Office for the management of H-shares companies to update them with the latest development of the IFRSs.

Communications with Fund Managers and Analysts

Open dialogue is maintained with fund managers and analysts locally and overseas to improve their understanding of HKEx's business development and update them with the latest corporate information of HKEx. Besides, HKEx has also conducted meetings with various investment firms in the UK and the US in March this year to raise the awareness of overseas investors of the Cash and Derivatives Markets in Hong Kong.

INFORMATION SERVICES

At the end of June 2005, there were 67 real-time information vendors for the Cash Market and 33 data vendors for the Derivatives Market. A total of 20 information vendors have participated in our China Promotion Programme (2004: 18) which allows the Mainland investors to subscribe to HKEx data at a discounted rate for a promotional period till the end of 2005.

Three international vendors have completed integration of their services with HKEx's Issuer Information Feed service to provide instantaneous access to disclosure documents filed by listed issuers. Packaged in Extensible Markup Language (XML) format, electronic copies of listed issuers' disclosures and announcements are transmitted to vendors once the information is posted on the HKEx website.

In the first half of 2005, HKEx has released 40,236 issuer disclosure documents on the HKEx website, an increase of 11.5 per cent from the corresponding period last year. Hit rate in the access of issuer information has increased 18.7 per cent with an average of around 15 million hits per month. For the six months ended June 2005, a total of 15,760 notices of Disclosure of Interests were filed with an average of around 900,000 hits for such information per month.

INFORMATION TECHNOLOGY

Production Systems Stability and Reliability

As of the end of June 2005, all major trading, clearing, settlement, and market data dissemination systems for the Cash and Derivatives Markets have maintained 100 per cent operational system uptime for the prior 27 months. To uphold this high standard of system stability and reliability, HKEx has upgraded the operating system of the HKATS, DCASS and the CCASS/3 to its updated version to secure continued and quality system vendor support.

Capacity Planning and Upgrade

In view of the overwhelming usage and popularity, the HKEx website (www.hkex.com.hk) is now undergoing a capacity upgrade and an enhancement to the disaster recovery arrangement to ensure its highest performance and availability during site disastrous situation.

The number of OMnet Application Programming Interface connections increased 19.8 per cent from 258 as at end of 2004 to 309 as at 30 June 2005, representing greater system flexibility for the market as a whole in establishing trading connections to the HKATS.

To meet the continuous growth of market activities and development, the Third Generation Automatic Order Matching and Execution System ("AMS/3") capacity upgrade exercise has been commenced and is planned to be completed in the fourth quarter of 2005. The capacity planning for HKATS, DCASS and Price Reporting System ("PRS") has also been formulated and it is planned to be implemented by the end of this year.

Obsolescent Technology Replacement and System Migration

Due to hardware obsolescence, the AMS/3 off-floor terminals will be replaced and its associated AMS/3 security will be upgraded. Initial phase of the replacement will be commenced in the latter part of August 2005. In line with the Trading Hall renovation programme, installation of additional off-floor terminals is anticipated in the latter part of the year as a result of the relinquishment of the existing AMS/3 on-floor terminals. Moreover, the existing AMS/3 Order Routing System will be migrated to HP/Nonstop platform to reduce technology complexity and achieve operational cost savings by the end of 2005.

System Consolidation and Operational Efficiency

The consolidation of the existing four market system networks into a new Optical Ethernet network (“SDNet”) to ensure a cost effective network infrastructure for the Hong Kong Cash and Derivatives Markets has started early this year. Fiber circuit installation for HKATS and DCASS participants and PRS information vendors has been substantially completed. The migration of the HKATS, DCASS and PRS circuits to the SDNet is planned in October 2005 following the successful completion of various market rehearsals.

AMS/3 satellite systems consolidation and Derivatives Market surveillance and risk management systems redevelopment are in progress to further improve operational efficiency and effectiveness.

TREASURY

HKEx’s investment funds comprise Corporate Funds, Margin Funds and Clearing House Funds, totalling \$15.6 billion on average for the six months ended 30 June 2005 (first half of 2004 average: \$14.3 billion).

As compared with 31 March 2005, the overall fund size as at 30 June 2005 increased by 13 per cent or \$1.9 billion to \$16.5 billion (31 March 2005: \$14.6 billion). Details of the asset allocation of the investments as at 30 June 2005 against those as at 31 March 2005 are set out below.

	Fund size \$ billion		Bonds		Cash or bank deposits		Global equities	
	Jun	Mar	Jun	Mar	Jun	Mar	Jun	Mar
Corporate Funds	3.9	4.1	60%	59%	34%	35%	6%	6%
Margin Funds	11.2	9.0	36%	47%	64%	53%	0%	0%
Clearing House Funds	1.4	1.5	17%	15%	83%	85%	0%	0%
Total	16.5	14.6	40%	47%	58%	51%	2%	2%

Investments are kept sufficiently liquid to meet HKEx's operating needs and possible liquidity requirements of the Clearing House Funds and Margin Funds. Excluding equities held under the Corporate Funds (\$0.3 billion as at 30 June 2005 and 31 March 2005), which have no maturity date, the maturity profiles of the remaining investments as at 30 June 2005 (\$16.2 billion) and 31 March 2005 (\$14.3 billion) were as follows:

	Fund size \$ billion		Overnight		>Overnight to 1 month		>1 month to 1 year		>1 year to 3 years		> 3 years	
	Jun	Mar	Jun	Mar	Jun	Mar	Jun	Mar	Jun	Mar	Jun	Mar
Corporate Funds	3.6	3.8	18%	10%	12%	28%	25%	23%	29%	23%	16%	16%
Margin Funds	11.2	9.0	38%	42%	26%	11%	23%	28%	13%	19%	0%	0%
Clearing House Funds	1.4	1.5	78%	81%	4%	2%	11%	8%	7%	9%	0%	0%
Total	16.2	14.3	36%	37%	21%	15%	23%	25%	16%	19%	4%	4%

Credit exposure is well diversified. As at 30 June 2005, the bond portfolio held was of investment grade and had a weighted average credit rating of Aa2 (31 March 2005: Aa2) and a weighted average maturity of 1.5 years (31 March 2005: 1.4 years). Deposits are placed only with the note-issuing banks in Hong Kong and investment grade licensed banks and restricted licence banks approved by the Board from time to time.

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

	Average VaR \$ million		Maximum VaR \$ million		Minimum VaR \$ million	
	Apr-Jun	Jan-Mar	Apr-Jun	Jan-Mar	Apr-Jun	Jan-Mar
Corporate Funds	12.1	15.3	14.7	16.1	11.3	14.1
Margin Funds	15.4	16.3	16.2	17.9	14.3	14.3
Clearing House Funds	1.4	0.7	1.5	1.5	1.2	0.6

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

INVESTMENTS IN ASSOCIATES

Computershare Hong Kong Investor Services Limited ("CHIS")

In May 2005, the Group acquired a further six per cent interest in CHIS for \$25 million and raised its interest to 30 per cent. As at 30 June 2005, the cost of the investment in CHIS was \$52 million and the book value of the investment was \$59 million.

ADP Wilco Processing Services Limited ("AWPS")

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

FINANCIAL REVIEW

OVERALL PERFORMANCE

	Unaudited Six months ended 30 Jun 2005 \$ million	As restated Unaudited Six months ended 30 Jun 2004 \$ million
Income:		
Income directly affected by market turnover	659	658
Stock Exchange listing fees	195	183
Investment income	122	74
Income from sale of information	162	158
Other income	100	91
	1,238	1,164
Operating expenses	570	571
Operating profit	668	593
Share of profits less losses of associates	9	6
Profit before taxation	677	599
Taxation	(106)	(101)
Profit attributable to shareholders	571	498
Earnings per share	\$0.54	\$0.47
Interim dividend declared per share	\$0.49	\$0.43
Dividend payout ratio	91%	91%
Shareholders' funds	4,103	4,052 ^o
Total assets *	21,238	21,443 ^o
Net assets per share #	\$3.87	\$3.83 ^o

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

^o Audited as at 31 December 2004

Based on 1,061,200,846 shares issued and fully paid as at 30 June 2005 (31 December 2004: 1,056,638,846 shares)

The Group recorded a profit attributable to shareholders of \$571 million for the first six months of 2005 (first quarter: \$245 million, second quarter: \$326 million), compared with \$498 million, as restated, for the same period in 2004 (first quarter: \$313 million, second quarter: \$185 million).

The increase in profit for the six months ended 30 June 2005 was primarily attributable to the significant increase in investment income compared with the same period last year, mainly due to higher interest income resulting from the rising interest rates in 2005 and increased fund size, and the increase in Stock Exchange listing fees due to the higher number of listed securities and newly listed derivative warrants during the period.

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

INCOME

(A) Income directly affected by market turnover

	Unaudited Six months ended 30 Jun 2005 \$'000	Unaudited Six months ended 30 Jun 2004 \$'000	Change
Trading fees and trading tariff	352,615	347,172	2%
Clearing and settlement fees	172,427	185,950	(7%)
Depository, custody and nominee services fees	133,682	125,157	7%
Total	658,724	658,279	0%

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

Clearing and settlement fees are derived predominantly from Cash Market transactions. Despite being mostly ad valorem fees, clearing and settlement fees are subject to a minimum and a maximum fee per transaction. Clearing and settlement fees decreased mainly due to lower exchange trade settlement income as there was a higher proportion of transactions with value subject to the maximum fee and a lower proportion of transactions with value subject to the minimum fee in 2005. Income from SIs also decreased as average daily market value of SIs dropped.

Depository, custody and nominee services fees increased due to the increase in scrip fee income and dividend collection fees in 2005.

Key market indicators

	Six months ended 30 Jun 2005	Six months ended 30 Jun 2004	Change
Average daily turnover value on the Stock Exchange	\$16.9 billion	\$16.8 billion	1%
Average daily number of derivatives contracts traded on the Futures Exchange	62,681	57,651	9%
Average daily number of stock options contracts traded on the Stock Exchange	25,206	23,391	8%

(B) Stock Exchange listing fees

	Unaudited Six months ended 30 Jun 2005 \$'000	Unaudited Six months ended 30 Jun 2004 \$'000	Change
Annual listing fees	131,356	123,664	6%
Initial and subsequent issue listing fees	60,394	55,997	8%
Others	3,822	3,309	16%
Total	195,572	182,970	7%

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

Key drivers for annual listing fees

	As at 30 Jun 2005	As at 30 Jun 2004	Change
Number of companies listed on the Main Board	901	869	4%
Number of companies listed on the GEM	203	199	2%
Total	1,104	1,068	3%

Key drivers for initial and subsequent issue listing fees

	Six months ended 30 Jun 2005	Six months ended 30 Jun 2004	Change
Number of newly listed derivative warrants	679	595	14%
Number of new listings on the Main Board	19	23	(17%)
Number of new listings on the GEM	2	15	(87%)
Total equity funds raised on the Main Board	\$123.2 billion	\$210.9 billion	(42%)
Total equity funds raised on the GEM	\$1.5 billion	\$4.0 billion	(63%)

(C) Investment income

	Unaudited Six months ended 30 Jun 2005 \$'000	As restated Unaudited Six months ended 30 Jun 2004 \$'000	Change
Income from:			
Funds available for investment	122,073	72,656	68%
Investment in Singapore Exchange Limited	–	832	(100%)
Total	122,073	73,488	66%

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

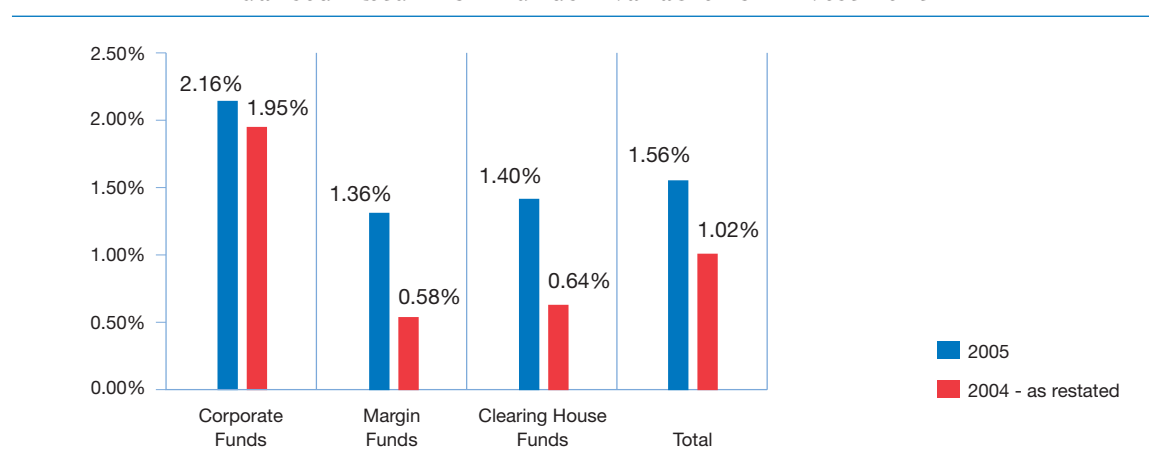
	Six months ended 30 Jun 2005 \$ billion	Six months ended 30 Jun 2004 \$ billion	Change
Corporate Funds	3.9	4.5	(13%)
Margin Funds	10.2	8.3	23%
Clearing House Funds	1.5	1.5	0%
Total	15.6	14.3	9%

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

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

The performance of funds available for investment was as follows:

Annualised Return on Funds Available for Investment



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

(D) Income from sale of information

	Unaudited Six months ended 30 Jun 2005 \$'000	Unaudited Six months ended 30 Jun 2004 \$'000	Change
Income from sale of information	162,245	158,340	2%

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

(E) Other income

	Unaudited Six months ended 30 Jun 2005 \$'000	As restated Unaudited Six months ended 30 Jun 2004 \$'000	Change
Other income			
Network, terminal user, dataline and software sub-license fees	66,134	56,807	16%
Participants' subscription and application fees	17,282	17,230	0%
Brokerage on direct IPO applications	6,188	8,382	(26%)
Fair value gain of an investment property	2,600	–	N/A
Accommodation income	1,494	3,789	(61%)
Miscellaneous income	6,153	4,483	37%
Total	99,851	90,691	10%

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

Accommodation income (i.e. retention interest charged on cash margin deposits in non-contract settlement currencies and securities deposited by Participants as alternatives to cash deposits of the Margin Funds) decreased as there were less cash margin deposits denominated in non-contract settlement currencies during the period. Furthermore, from 1 June 2005, accommodation charges on cash margin deposits were abolished and accommodation fee on utilised non-cash collateral charged by HKCC and SEOCH were reduced from 1.2 per cent and 2 per cent respectively to 0.5 per cent.

OPERATING EXPENSES

	Unaudited Six months ended 30 Jun 2005 \$'000	As restated Unaudited Six months ended 30 Jun 2004 \$'000	Change
Staff costs and related expenses	282,762	265,153	7%
Information technology and computer maintenance expenses	99,063	110,017	(10%)
Premises expenses	39,946	39,245	2%
Product marketing and promotion expenses	5,533	5,696	(3%)
Legal and professional fees	6,592	5,484	20%
Depreciation	85,680	91,578	(6%)
Payment to SFC under dual filing regime	10,000	10,000	0%
Other operating expenses	40,942	44,122	(7%)
Total	570,518	571,295	(0%)

Staff costs and related expenses rose by \$18 million, primarily due to the increase in salary costs of \$13 million as a result of the increase in headcount and salary adjustment in 2005. Employee share option costs also rose by \$5 million due to the amortisation of the option costs arising from grants of new share options in March 2004, May 2004 and January 2005.

Information technology and computer maintenance expenses of the Group, after excluding goods and services directly consumed by the Participants of \$26 million (2004: \$29 million), were \$73 million (2004: \$81 million). The reduction was mainly due to lower system maintenance costs and reduced network line rental charges. During the period under review, capital expenditures on computer systems, hardware and software amounted to \$11 million (2004: \$11 million).

Depreciation fell as certain fixed assets became fully depreciated.

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

SHARE OF PROFITS LESS LOSSES OF ASSOCIATES

	Unaudited Six months ended 30 Jun 2005 \$'000	As restated Unaudited Six months ended 30 Jun 2004 \$'000	Change
Share of profits less losses of associates	8,635	6,144	41%

Share of profits less losses of associates increased due to the higher profitability of one of the associates, CHIS. In May 2005, the Group acquired a further six per cent of the share capital of CHIS.

TAXATION

	Unaudited Six months ended 30 Jun 2005 \$'000	As restated Unaudited Six months ended 30 Jun 2004 \$'000	Change
Taxation	105,786	101,192	5%

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

COMPARISON OF 2005 SECOND QUARTER PERFORMANCE WITH 2005 FIRST QUARTER PERFORMANCE

	Unaudited Three months ended 30 Jun 2005 \$ million	Unaudited Three months ended 31 Mar 2005 \$ million
Income:		
Income directly affected by market turnover:		
Trading fees and trading tariff	170	183
Clearing and settlement fees	81	92
Depository, custody and nominee services fees	100	33
	351	308
Stock Exchange listing fees	99	96
Investment income	79	43
Income from sale of information	83	79
Other income	52	48
	664	574
Operating expenses	287	283
Operating profit	377	291
Share of profits less losses of associates	6	3
Profit before taxation	383	294
Taxation	(57)	(49)
Profit attributable to shareholders	326	245

Profit attributable to shareholders increased by \$81 million to \$326 million for the second quarter of 2005, compared with \$245 million recorded in the first quarter of 2005. The improvement in profit was mainly due to an increase in depository, custody and nominee services fees due to seasonal factors and higher investment income, while operating expenses remained fairly stable during the two quarters.

Key market indicators

	Three months ended 30 Jun 2005	Three months ended 31 Mar 2005	Change
Average daily turnover value on the Stock Exchange	\$15.4 billion	\$18.4 billion	(16%)
Average daily number of derivatives contracts traded on the Futures Exchange	61,545	63,885	(4%)
Average daily number of stock options contracts traded on the Stock Exchange	23,907	26,583	(10%)

Despite a decrease in trading fees and trading tariff of \$13 million and clearing and settlement fees of \$11 million due to the decline in activities in the Cash and Derivatives Markets in the second quarter of 2005, income directly affected by market turnover increased by \$43 million in the second quarter as compared to the first quarter as depository, custody and nominee services fees rose by \$67 million on account of an increase in dividend collection and scrip fee income due to seasonal fluctuations.

Investment income increased by \$36 million, principally due to higher interest income attributable to rising interest rates in 2005 and increased fair value gains on the investments held, reflecting the market movements in the bond and equity prices during the two quarters.

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

WORKING CAPITAL

Working capital rose by \$82 million or three per cent to \$3,147 million as at 30 June 2005 (31 December 2004: \$3,065 million). The increase was primarily due to the profit generated during the period of \$571 million, which was partly offset by payment of the 2004 final dividend of \$498 million in April 2005, and the increase in other net current assets of \$9 million.

Although the Group has consistently maintained a very liquid position, banking facilities have nevertheless been put in place for contingency purposes. As at 30 June 2005, the Group's total available banking facilities amounted to \$1,608 million (31 December 2004: \$1,608 million), of which \$1,500 million (31 December 2004: \$1,500 million) represented repurchase facilities to augment the liquidity of the Margin Funds.

Borrowings of the Group have been rare and are mostly event driven, with little seasonality. As at 30 June 2005 and 31 December 2004, the Group had no bank borrowings, and therefore had zero gearing.

The Group's capital expenditure commitments as at 30 June 2005 were related to the refurbishment of the Trading Hall and the ongoing investments in facilities and technology, and amounted to \$144 million (31 December 2004: \$78 million). The Group has adequate internal resources to fund its commitments on capital expenditures.

As at 30 June 2005, 97 per cent (31 December 2004: 99 per cent) of the Group's cash and cash equivalents (comprise cash on hand, bank balances and time deposits within three months of maturity when acquired) were denominated in HKD or USD.

CHARGES ON ASSETS

None of the Group's assets was pledged as at 30 June 2005 and 31 December 2004.

SIGNIFICANT INVESTMENTS HELD AND MATERIAL ACQUISITIONS AND DISPOSALS OF INVESTMENTS AND SUBSIDIARIES

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

EXPOSURE TO FLUCTUATIONS IN EXCHANGE RATES AND RELATED HEDGES

Details of the Group's exposure to fluctuations in exchange rates and related hedges are included in note 31(a)(i) – Foreign exchange risk to the condensed consolidated accounts of this interim report.

CONTINGENT LIABILITIES

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

For details of the other contingent liabilities, please refer to note 28(a), (b) and (c) to the condensed consolidated accounts of this interim report.

EMPLOYEES

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

For the purpose of motivating and retaining employees for the continual operation and development of the Group, share options were granted to some of the employees (including the executive Director) of HKEx to subscribe for shares in HKEx in accordance with the terms and conditions of the Pre-Listing Share Option Scheme and Post-Listing Share Option Scheme approved by the shareholders of HKEx at an extraordinary general meeting held on 31 May 2000 and the latter being subsequently amended by the shareholders of HKEx on 17 April 2002 so as to comply with the new Listing Rules which came into effect on 1 September 2001. No further options can be, or have been, issued under the Pre-Listing Share Option Scheme after the date of listing of HKEx on the Stock Exchange.

The staff team as at the end of June 2005 comprised 823 employees, including 40 temporary staff (31 December 2004: 791 employees, including 16 temporary staff).

There are no significant changes to the policies relating to remuneration, bonus, share option schemes and training schemes from the information disclosed in the 2004 annual report.

PROSPECTS

As the controller of the stock and futures exchanges, HKEx's revenue is closely correlated with the activities in the Cash and Derivatives Markets. Apart from the local economic development which is one of the contributing factors, the Group's performance is also subject to the economic growth of the Mainland and other major international financial markets. The rising interest rate and oil prices, the impact of the revaluation of Renminbi on international trade and capital inflow to Hong Kong will remain major concerns of both local and international investors.

In the first half of the year, Mainland enterprises raised a total of \$58.5 billion through IPOs on the Main Board and GEM, accounting for about 90 per cent of the total IPO funds raised during the period. HKEx has benefited from the steady economic growth on the Mainland in recent years and has successfully attracted the listings of major Mainland enterprises including some of the world's largest IPOs. These listings have further strengthened HKEx's role as a Mainland partner in capital raising and as the most liquid market for the trading of Mainland-related securities and derivatives. HKEx will continue building on its strength to reaffirm its position as the pre-eminent exchange where Mainland and Hong Kong enterprises can tap the global capital market, and reinforce Hong Kong's role as an international financial centre.