



香港交易所

HKEx 2003 INTERIM RESULTS

CONSOLIDATED FINANCIAL STATEMENTS

CONDENSED CONSOLIDATED PROFIT AND LOSS ACCOUNT

(Financial figures are expressed in Hong Kong dollars)

		Unaudited Six months ended 30 Jun 2003 \$'000	Unaudited and restated Six months ended 30 Jun 2002 \$'000
INCOME			
Trading fees and trading tariff	4	184,509	166,932
Stock Exchange listing fees		160,059	165,007
Clearing and settlement fees		92,312	96,402
Depository, custody and nominee services fees		94,593	87,216
Income from sale of information		126,253	158,538
Investment income	5	178,290	135,008
Other income	6	71,032	83,486
	3	907,048	892,589
OPERATING EXPENSES			
Staff costs and related expenses		266,861	262,336
Information technology and computer maintenance expenses		137,453	131,612
Premises expenses		42,833	49,881
Product marketing and promotion expenses		3,342	7,803
Legal and professional fees		20,991	6,031
Depreciation and amortisation		93,025	78,382
Payment to SFC under dual filing regime		5,000	-
Other operating expenses	7	91,186	41,109
		660,691	577,154
OPERATING PROFIT	3	246,357	315,435
SHARE OF PROFITS LESS LOSSES OF ASSOCIATED COMPANIES	3	3,263	760
PROFIT BEFORE TAXATION	3	249,620	316,195
TAXATION	3/8	(35,234)	(27,403)
PROFIT ATTRIBUTABLE TO SHAREHOLDERS	3	214,386	288,792
DIVIDEND		188,452	83,450
Earnings per share	9	\$0.205	\$0.277
Interim dividend declared per share		\$0.18	\$0.08
Dividend payout ratio		88%	29%

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

(Financial figures are expressed in Hong Kong dollars)

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

CONDENSED CONSOLIDATED BALANCE SHEET

(Financial figures are expressed in Hong Kong dollars)

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

CONDENSED CONSOLIDATED BALANCE SHEET (continued)

(Financial figures are expressed in Hong Kong dollars)

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

CONDENSED CONSOLIDATED CASH FLOW STATEMENT

(Financial figures are expressed in Hong Kong dollars)

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

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

(Financial figures are expressed in Hong Kong dollars)

1. BASIS OF PREPARATION AND ACCOUNTING POLICIES

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

These condensed consolidated interim accounts should be read in conjunction with the 2002 annual accounts.

The accounting policies and methods of computation used in the preparation of these accounts are consistent with those used in the annual accounts for the year ended 31 December 2002 except that the Group has adopted the new SSAP 12: Income Taxes, issued by the HKSA, which is effective for accounting periods commencing on or after 1 January 2003. The effects of the change to the Group's accounting policies are set out below.

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

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

2. TURNOVER

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

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

3. SEGMENT INFORMATION

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

	Six months ended 30 Jun 2003 (unaudited)				
	\$'000				
	Cash Market	Derivatives Market	Clearing Business	Others	Group
Income	437,615	138,660	206,341	124,432	907,048
Costs	<u>213,091</u>	<u>72,615</u>	<u>149,182</u>	<u>-</u>	<u>434,888</u>
Segment results	<u>224,524</u>	<u>66,045</u>	<u>57,159</u>	<u>124,432</u>	472,160
Unallocated costs					<u>225,803</u>
Operating profit					246,357
Share of profits less losses of associated companies	35	-	3,228	-	<u>3,263</u>
Profit before taxation					249,620
Taxation					<u>(35,234)</u>
Profit attributable to shareholders					<u>214,386</u>

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

3. SEGMENT INFORMATION (continued)

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

The **Cash Market** business mainly refers to the operations of the Stock Exchange, which covers all products traded on the cash market platforms, such as equities, debt securities, unit trusts, warrants and rights. Currently, the Group operates two cash market platforms, the Main Board and the Growth Enterprise Market. The major sources of income of the business are trading fees, trading tariff, listing fees and income from sale of information.

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

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

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

3. SEGMENT INFORMATION (continued)

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

4. TRADING FEES AND TRADING TARIFF

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

5. INVESTMENT INCOME

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

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

6. OTHER INCOME

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

7. OTHER OPERATING EXPENSES

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

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

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

8. TAXATION

Taxation in the condensed consolidated profit and loss account represents:

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

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

9. EARNINGS PER SHARE

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

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

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

10. FIXED ASSETS

The Group is heavily reliant on the capability and reliability of its computer systems for its business operations, including those required for its electronic trading platforms and for post-trading clearing and settlement services. The total cost of additions to fixed assets of the Group during the six months to 30 June 2003 was \$17,811,000 (2002: \$81,591,000) of which \$15,858,000 (2002: \$66,494,000) or 89 per cent (2002: 81 per cent) was on computer systems, hardware and software. The total cost and net book value of disposals and write-offs of fixed assets during the six months to 30 June 2003 were \$164,823,000 and \$10,048,000 respectively (2002: \$2,177,000 and \$47,000).

11. INVESTMENTS IN ASSOCIATED COMPANIES

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

(a) Goodwill

Cost

At 1 Jan 2003 and 30 Jun 2003

\$'000

26,889

Accumulated amortisation and impairment

At 1 Jan 2003

Charge for the period

Impairment loss

1,568

1,339

364

At 30 Jun 2003

3,271

Net book value

At 30 Jun 2003

23,618

At 31 Dec 2002

25,321

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

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

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

11. INVESTMENTS IN ASSOCIATED COMPANIES (continued)

(c) Details of the unlisted associated companies as at 30 June 2003 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%
Wilco International Processing Services Limited	Hong Kong	Provision of transaction processing services to Stock Exchange Participants	6 Class B ordinary shares	30%

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

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

12. CLEARING HOUSE FUNDS

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

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.

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

12. CLEARING HOUSE FUNDS (continued)

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

13. COMPENSATION FUND RESERVE ACCOUNT

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

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

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

14. CASH AND DERIVATIVES MARKET DEVELOPMENT FUND (CDMD FUND)

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

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

15. MARGIN FUNDS ON DERIVATIVES CONTRACTS

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

16. ACCOUNTS RECEIVABLE, PREPAYMENTS AND DEPOSITS/ACCOUNTS PAYABLE, ACCRUALS AND OTHER LIABILITIES

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

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

17. PROVISIONS

	Reinstatement costs \$'000	Employee benefit costs \$'000	Total \$'000
At 1 Jan 2003	25,136	23,826	48,962
Provision for the period	-	13,083	13,083
Amount used during the period	-	(12,335)	(12,335)
Amount paid during the period	(301)	(4,262)	(4,563)
At 30 Jun 2003	<u>24,835</u>	<u>20,312</u>	<u>45,147</u>
		Unaudited at 30 Jun 2003 \$'000	Audited at 31 Dec 2002 \$'000
Analysis of provisions:			
Current		25,108	28,863
Non-current		20,039	20,099
		<u>45,147</u>	<u>48,962</u>

18. SHARE CAPITAL AND SHARE PREMIUM

		Unaudited at 30 Jun 2003 \$'000	Audited at 31 Dec 2002 \$'000	
Authorised:				
2,000,000,000 shares of \$1 each		<u>2,000,000</u>	<u>2,000,000</u>	
Issued and fully paid:				
	No. of shares of \$1 each	Share capital \$'000	Share premium \$'000	Total \$'000
At 1 Jan 2002	1,040,664,846	1,040,665	-	1,040,665
Shares issued under employee share option schemes	<u>2,916,000</u>	<u>2,916</u>	<u>19,012</u>	<u>21,928</u>
At 31 Dec 2002	1,043,580,846	1,043,581	19,012	1,062,593
Shares issued under employee share option schemes	<u>3,374,000</u>	<u>3,374</u>	<u>21,999</u>	<u>25,373</u>
At 30 Jun 2003	<u>1,046,954,846</u>	<u>1,046,955</u>	<u>41,011</u>	<u>1,087,966</u>

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

18. SHARE CAPITAL AND SHARE PREMIUM (continued)

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

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

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

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

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

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

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

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

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

19. REVALUATION RESERVES

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

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

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

20. DESIGNATED RESERVES

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

These reserves are segregated for their respective purposes.

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

21. RETAINED EARNINGS

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

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

22. NOTES TO THE CONDENSED CONSOLIDATED CASH FLOW STATEMENT

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

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

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

22. NOTES TO THE CONDENSED CONSOLIDATED CASH FLOW STATEMENT (continued)

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

(c) The net assets in Clearing House Funds, Compensation Fund Reserve Account, CDMD Fund and margin funds are held in segregated accounts for specific purposes. Movements in individual items of the net assets of the funds during the period therefore do not constitute any cash or cash equivalent transactions to the Group except for the investment income net of expenses of these funds which has been accounted for as the Group's assets and profit.

23. COMMITMENTS

	Unaudited at 30 Jun 2003 \$'000	Audited at 31 Dec 2002 \$'000
Commitments in respect of capital expenditures:		
Contracted but not provided for	17,234	36,454
Authorised but not contracted for	73,512	57,170
	<u>90,746</u>	<u>93,624</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 to mitigate risks arising from fluctuations in exchange rates. As at 30 June 2003, the total nominal value of outstanding forward foreign exchange contracts amounted to HK\$259 million (31 December 2002: HK\$197 million). All contracts will mature within three months.

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

25. CONTINGENT LIABILITIES

- (a) The Compensation Fund is a fund set up under the repealed SO for the purpose of compensating any person dealing with a Stock Exchange Participant (other than another Stock Exchange Participant) for any pecuniary losses suffered as a result of a default of the Stock Exchange Participant. According to section 109(3) of the SO, the maximum compensation amount is \$8 million for each Stock Exchange Participant's default. Under section 113(5A) of the SO, the Stock Exchange may, upon satisfying certain conditions, with the approval of the SFC, allow an additional payment to the successful claimants before apportionment. Under section 107(1) of the SO, the Stock Exchange has contingent liabilities to the Compensation Fund as it shall replenish the Compensation Fund upon the SFC's request to do so. The amounts to be replenished should be equal to the amount paid in connection with the satisfaction of the claims, including any legal and other expenses paid or incurred in relation to the claims but capped at \$8 million per default. Under the SFO which came into effect on 1 April 2003, all these provisions shall continue to apply to any default occurring before that date despite the repeal of the SO. As at 30 June 2003, there were outstanding claims received in respect of 13 defaulted Stock Exchange Participants (31 December 2002: 14).

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

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

- (b) The Stock Exchange has undertaken to indemnify the Collector of Stamp Revenue against any loss of revenue resulting from any underpayment or default or delay in payment of stamp duty by its Participants, up to \$200,000 in respect of default of any one Participant. In the unlikely event that all of its 447 trading Participants as at 30 June 2003 (31 December 2002: 471) default, the maximum contingent liability of the Stock Exchange under the indemnity will amount to \$89 million (31 December 2002: \$94 million).

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

25. CONTINGENT LIABILITIES (continued)

- (c) HKEx gave an undertaking on 6 March 2000 in favour of HKSCC to contribute an amount not exceeding \$50 million in the event of HKSCC being wound up while it is a wholly-owned subsidiary of HKEx or within one year after HKSCC ceases to be a wholly-owned subsidiary of HKEx, for payment of the debts and liabilities of HKSCC contracted before HKSCC ceases to be a wholly-owned subsidiary of HKEx, and for the costs, charges and expenses of winding up.

26. MATERIAL RELATED PARTY TRANSACTIONS

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

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

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

27. OFF BALANCE SHEET RISKS

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

NOTES TO THE CONDENSED CONSOLIDATED ACCOUNTS

27. OFF BALANCE SHEET RISKS (continued)

The Group mitigates its exposure to the risks described above by requiring the Participants to meet the Group's established financial requirements and criteria for admission as Participants, monitoring compliance with risk management measures such as position limits established by the Group and requiring Clearing Participants to contribute to the Clearing House Funds set up by HKSCC, SECH 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.