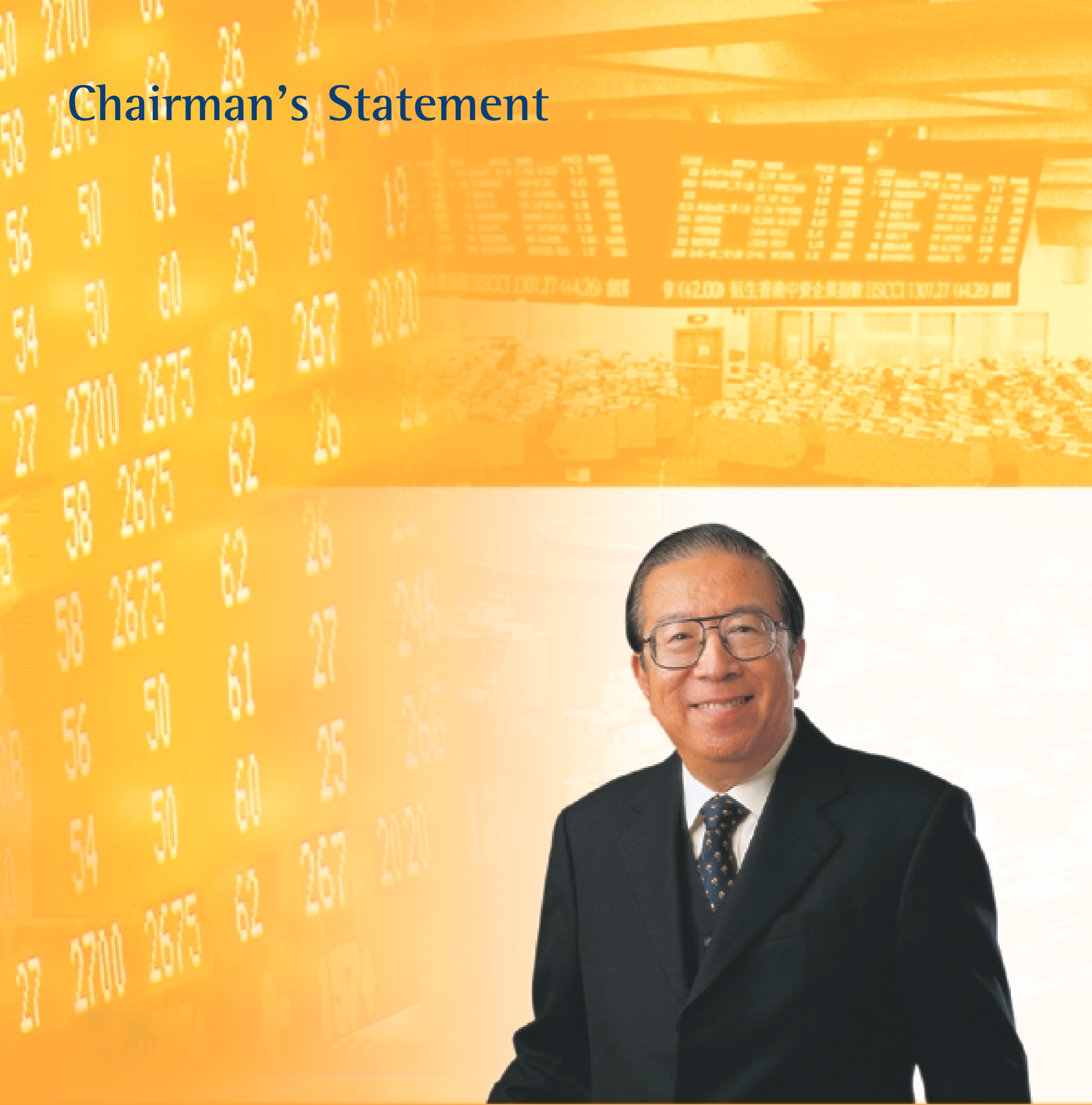
Chairman's Statement



LEE Yeh Kwong, Charles
Chairman

(Financial figures are expressed in Hong Kong dollars)

I am pleased to present this annual report of Hong Kong Exchanges and Clearing Limited (HKEx) for the year 1 January to 31 December 2003. It should be read in conjunction with the Review of Operations by the Chief Executive, which reports on the Group's operations and development.

Financial Results

The period under review was a year marked by different economic circumstances. The first half of the year was adversely affected by poor domestic economic conditions, emanating from the onset of SARS (Severe Acute Respiratory Syndrome), rising unemployment, continuing weakness in the property market and slow growth overseas. The second half saw the end of SARS in Hong Kong, enthusiasm about the signing of the Mainland and Hong Kong Closer Economic Partnership Arrangement, or CEPA, and the first signs of returning confidence and economic health — although there is still some way to go before full recovery.

HKEx recorded a profit before taxation of $805 million during the year, an increase of 24 per cent over 2002. Profit attributable to shareholders was $692 million, 18 per cent higher than in the previous year. The rise in profit is principally due to strong activity in the securities and derivatives markets in the second half of the year, resulting in increased revenue from trading fees, trading tariff and clearing and settlement fees. However, the low level of interest rates continued to affect our interest income.

The Board of Directors has recommended payment of a final dividend of $0.42 per share, which, together with the interim dividend of $0.18 per share, will bring the total dividend distribution for the year to $0.60 per share.

The Board has carried out a review of the Group's policy regarding its cash funds, which are made up largely of liquid funds required in connection with our clearing businesses but also include substantial retained earnings. The review has taken into account the changed economic environment, the Group's strategy and our medium-term capital and risk management requirements. Following this review, the Board has recommended, in addition to the dividend referred to above, a special dividend of $1.68 per share.

Operating expenses increased by 5 per cent to $1,222 million, largely due to one-off expenses of $52 million incurred in the second quarter that are not expected to recur. The Group continued to maintain rigorous control of costs in order to minimise operating expenses. Shareholders' funds amounted to $5,603 million at the end of the year, compared with $5,490 million a year earlier.

Quarterly Reporting

HKEx introduced quarterly reporting during 2003 to promote high standards of corporate governance and provide shareholders with timely information about the Group's performance. The quarterly, interim and final financial reports were reviewed by the Audit Committee before they were presented to the Board. The voluntary publication of our results on a quarterly basis demonstrates our commitment to transparency and good corporate governance.

Strategic Plan

Since the merger of the exchanges and clearing houses, HKEx has established an integrated corporate structure, strengthened the market infrastructure and streamlined management and operations. One of the most important tasks in 2003 was to formulate a strategic plan for 2004-2006, to guide the path of the Group's future development.

Our mission is to operate a world-class market for capital formation and the trading of securities and derivatives products. We are committed to fulfilling our obligations to ensure a fair and orderly market, to ensure that risks of the markets are managed prudently and to safeguard the interests of the public, in particular the interests of the investing public. Our strategic focus is to further strengthen the status of Hong Kong as an international financial centre and China's leading capital market, where Mainland issuers can gain access to international investors through listings on our market.

Development during the period 2004 to 2006 will incorporate three aspects: Consolidation; Building a higher quality market; and Expanding relationship with the Mainland.

Consolidation

The efficiency and cost effectiveness of the Group's internal operations will be raised by cost rationalisation, constant review of project portfolios and strengthening of project management. Development of a business culture that emphasises quality service will continue to be promoted. Through consolidation, the Group seeks to become a more efficient organisation with a dedicated workforce focussed on stakeholders and performance.

Building a Higher Quality Market

It is vital for HKEx and the markets it operates to maintain international quality standards and practices in today's competitive global environment. This will require further strengthening of market regulation and risk management. Issuer supervision will be augmented at all levels, encompassing structure, policy and day-to-day operations, to further affirm our commitment to raise market quality.

We have also submitted our views on "Proposals to Enhance the Regulation of Listing", a consultation paper published by the Government in October 2003, and we will continue to work closely with the Government to identify and establish the most suitable model for the enhancement of the regulation of listing in Hong Kong.

Expanding Relationship with the Mainland

The further development of Mainland China-related business is a major component in the strategy of HKEx. Our goal is to further expand our relationship with the Mainland, building upon the solid foundation we have laid. For over a decade, through sustained and persistent efforts, we have successfully promoted and attracted the listing of Mainland state enterprises in Hong Kong through H shares, as well as the listing of red-chip companies and private enterprises. Our close partnership with Mainland businesses will continue to grow through the opening of the Beijing office in November 2003.

Last year marked the 10th anniversary of the listing of the first Mainland state enterprise in Hong Kong, and the beginning of a new era of large-scale capital formation by Mainland companies in the Hong Kong market. Development of this activity and the impact on the growth of our markets have been phenomenal. The China dimension of our business has become the most dynamic driving force in our operations.

In 2003, a total of 73 companies were listed, including 38 Mainland enterprises, which comprise H-share issuers, red-chip companies and private enterprises. The total funds raised by the newly listed Mainland enterprises amounted to $52 billion, representing 88 per cent of the total funds raised by initial public offering (IPO) in 2003. At the end of 2003, a total of 258 Mainland enterprises were listed in Hong Kong, with a market capitalisation of $1,695.1 billion, representing 31 per cent of our total market capitalisation. Trading of Mainland-related shares in our equity market accounted for 46 per cent of our total turnover of $2,304.8 billion last year. The size of our market has quadrupled in the space of about 10 years from a market capitalisation of $1,332.2 billion at the end of 1992 to $5,547.8 billion last year. Average daily turnover increased from $2.8 billion in 1992 to $10.4 billion in 2003. Since the first H-share listing, funds totalling $780 billion have been raised by Mainland enterprises, including $458 billion or 58 per cent by way of further issues after listing.

The Group's efforts to develop our market into the premier international capital formation centre for Mainland enterprises have helped strengthen Hong Kong's role as an international financial centre. Issuers and investors are attracted by the quality of our regulation and accounting standards, the absence of foreign exchange controls, reliable and cost effective banking and securities services, the rule of law and the free flow of information. We will seek to ensure that our markets remain attractive to investors and issuers from Hong Kong, the Mainland and overseas in the face of today's intense competition in the world's financial markets.

Staff Changes

Successful implementation of our strategic plan and HKEx's future development require us to maintain a highly professional management team. We were pleased that Paul Chow joined the Group to succeed Kwong Ki-chi as the chief executive in May last year. Mr Chow is a former chief executive of The Stock Exchange of Hong Kong Limited who was involved in the establishment of the framework for the initial listing of H shares and the development of the Exchange's Automatic Order Matching and Execution System.

Patrick Conroy, a former director for financial sector development and global partnerships at the International Bank for Reconstruction and Development (the World Bank) and a former senior director of the supervision of markets division of the Securities and Futures Commission, also joined the Group as chief operating officer last year. Other senior management changes in 2003 included the appointment of Stewart Shing as the head of the Clearing Business Unit. Mr Shing, who has more than 30 years of securities operations and business management experience, was the chief executive of Hong Kong Securities Clearing Company Limited from 1996 to 2000.

Outlook

The external environment is likely to be influenced by low interest rate levels, Mainland China's rapid economic growth, and movements in the currency markets. In this climate, investment funds will likely continue to be drawn to equities. The inflow of international funds will continue to bring about a favourable environment for the listing of major enterprises, in particular those from the Mainland. I am optimistic that these factors augur well for the prospects of our markets.

I acknowledge with deep gratitude the work and support of my fellow directors, and the executives and staff of HKEx, which have been crucial to our success. I am confident that their endeavours will continue to help the Group achieve greater accomplishments in the years ahead.

LEE Yeh Kwong, Charles
Chairman

26 February 2004