



## Quality Education Fund

Financial statements for the year ended 31 August 2017

# Report of the Director of Audit



**Audit Commission**  
The Government of the Hong Kong Special Administrative Region

## **Independent Auditor's Report To the Permanent Secretary for Education Incorporated**

### *Opinion*

I certify that I have audited the financial statements of the Quality Education Fund set out on pages 4 to 22, which comprise the statement of financial position as at 31 August 2017, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In my opinion, the financial statements give a true and fair view of the financial position of the Quality Education Fund as at 31 August 2017, and of its financial performance and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA") and have been properly prepared in accordance with section 8(3) of the Permanent Secretary for Education Incorporation Ordinance (Cap. 1098).

### *Basis for opinion*

I conducted my audit in accordance with section 8(5) of the Permanent Secretary for Education Incorporation Ordinance and the Audit Commission auditing standards. My responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of my report. I am independent of the Quality Education Fund in accordance with those standards, and I have fulfilled my other ethical responsibilities in accordance with those standards. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

### *Responsibilities of the Permanent Secretary for Education Incorporated for the financial statements*

The Permanent Secretary for Education Incorporated is responsible for the preparation of the financial statements that give a true and fair view in accordance with HKFRSs issued by the HKICPA and section 8(3) of the Permanent Secretary for Education Incorporation Ordinance, and for such internal control as the Permanent Secretary for Education Incorporated determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Permanent Secretary for Education Incorporated is responsible for assessing the Quality Education Fund's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting.

### *Auditor's responsibilities for the audit of the financial statements*

My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Audit Commission auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with the Audit Commission auditing standards, I exercise professional judgment and maintain professional skepticism throughout the audit. I also:

- identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;
- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose

of expressing an opinion on the effectiveness of the Quality Education Fund's internal control;

- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Permanent Secretary for Education Incorporated;
- conclude on the appropriateness of the Permanent Secretary for Education Incorporated's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Quality Education Fund's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause the Quality Education Fund to cease to continue as a going concern; and
- evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.



Kenneth Ho  
Assistant Director of Audit  
for Director of Audit

14 February 2018

Audit Commission  
26th Floor  
Immigration Tower  
7 Gloucester Road  
Wanchai, Hong Kong



**QUALITY EDUCATION FUND**  
**STATEMENT OF COMPREHENSIVE INCOME**  
**FOR THE YEAR ENDED 31 AUGUST 2017**  
*(Expressed in thousands of Hong Kong dollars)*

|                                                        | Note | 2017      | 2016      |
|--------------------------------------------------------|------|-----------|-----------|
| <b>INCOME</b>                                          |      |           |           |
| Interest income                                        | 3    | 87,788    | 85,419    |
| Dividend income                                        | 4    | 95,926    | 82,820    |
| Net realised and revaluation gains/(losses) on:        |      |           |           |
| — securities                                           |      | 702,874   | 295,263   |
| — trading financial instruments                        |      | (7,543)   | 8,102     |
| — deposits with banks and other financial institutions |      | 8,401     | (15,985)  |
|                                                        |      | 703,732   | 287,380   |
| Other income                                           | 5    | 4,089     | 259       |
|                                                        |      | 891,535   | 455,878   |
| <b>EXPENDITURE</b>                                     |      |           |           |
| Grants and awards                                      | 6    | (71,843)  | (86,937)  |
| Operating expenses                                     | 7    | (49,475)  | (53,046)  |
|                                                        |      | (121,318) | (139,983) |
| <b>SURPLUS FOR THE YEAR</b>                            |      | 770,217   | 315,895   |
| <b>OTHER COMPREHENSIVE INCOME</b>                      |      | —         | —         |
| <b>TOTAL COMPREHENSIVE INCOME FOR THE YEAR</b>         |      | 770,217   | 315,895   |

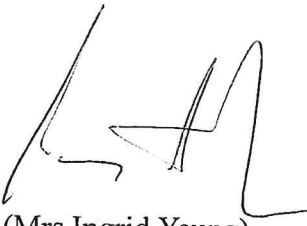
The accompanying notes 1 to 17 form part of these financial statements.

**QUALITY EDUCATION FUND**  
**STATEMENT OF FINANCIAL POSITION**  
**AS AT 31 AUGUST 2017**  
*(Expressed in thousands of Hong Kong dollars)*

|                                                      | Note | 2017             | 2016             |
|------------------------------------------------------|------|------------------|------------------|
| <b>ASSETS</b>                                        |      |                  |                  |
| Cash at bank                                         |      | 48,146           | 63,898           |
| Deposits with banks and other financial institutions |      |                  |                  |
| with original maturity within three months           | 8    | 157,381          | 157,068          |
| Deposits with banks and other financial institutions |      |                  |                  |
| with original maturity over three months             | 8    | 855,431          | 1,007,011        |
| Securities                                           | 9    | 6,971,927        | 6,910,553        |
| Trading financial instruments                        | 10   | 4,600            | 8,140            |
| Receivables and other assets                         | 11   | 98,725           | 118,708          |
| Placement with the Exchange Fund                     | 12   | 1,116,878        | 230,700          |
|                                                      |      | <b>9,253,088</b> | <b>8,496,078</b> |
| <b>LIABILITIES</b>                                   |      |                  |                  |
| Trading financial instruments                        | 10   | (17,533)         | (7,723)          |
| Payables and other liabilities                       | 13   | (62,416)         | (85,433)         |
|                                                      |      | <b>(79,949)</b>  | <b>(93,156)</b>  |
| <b>NET ASSETS</b>                                    |      | <b>9,173,139</b> | <b>8,402,922</b> |
| Representing:                                        |      |                  |                  |
| <b>FUND BALANCE</b>                                  |      |                  |                  |
| Accumulated surplus                                  |      | <b>9,173,139</b> | <b>8,402,922</b> |

The accompanying notes 1 to 17 form part of these financial statements.

Permanent Secretary for Education Incorporated  
Trustee of the Quality Education Fund

  
(Mrs Ingrid Yeung)

Permanent Secretary for Education  
14 February 2018

**QUALITY EDUCATION FUND**  
**STATEMENT OF CHANGES IN EQUITY**  
**FOR THE YEAR ENDED 31 AUGUST 2017**  
*(Expressed in thousands of Hong Kong dollars)*

|                                         | 2017                    | 2016                    |
|-----------------------------------------|-------------------------|-------------------------|
| <b>ACCUMULATED SURPLUS</b>              |                         |                         |
| Balance at beginning of year            | 8,402,922               | 8,087,027               |
| Total comprehensive income for the year | <u>770,217</u>          | <u>315,895</u>          |
| Balance at end of year                  | <u><b>9,173,139</b></u> | <u><b>8,402,922</b></u> |

The accompanying notes 1 to 17 form part of these financial statements.

**QUALITY EDUCATION FUND**  
**STATEMENT OF CASH FLOWS**  
**FOR THE YEAR ENDED 31 AUGUST 2017**  
*(Expressed in thousands of Hong Kong dollars)*

|                                                                                                           | 2017      | 2016      |
|-----------------------------------------------------------------------------------------------------------|-----------|-----------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                                                               |           |           |
| Surplus for the year                                                                                      | 770,217   | 315,895   |
| Adjustments for:                                                                                          |           |           |
| Interest income                                                                                           | (87,788)  | (85,419)  |
| Dividend income                                                                                           | (95,926)  | (82,820)  |
| Decrease in deposits with banks and other financial institutions with original maturity over three months | 151,580   | 73,964    |
| Increase in investments in securities                                                                     | (61,374)  | (444,826) |
| Increase in placement with the Exchange Fund                                                              | (886,178) | (230,700) |
| Change in trading financial instruments                                                                   | 13,350    | (1,724)   |
| Decrease/(Increase) in receivables and other assets                                                       | 37,486    | (70,051)  |
| (Decrease)/Increase in payables and other liabilities                                                     | (23,017)  | 49,611    |
| Elimination of foreign exchange differences in revaluation of cash and cash equivalents                   | (1,587)   | (77)      |
| Interest received                                                                                         | 74,417    | 89,560    |
| Dividends received                                                                                        | 91,794    | 82,830    |
|                                                                                                           | (17,026)  | (303,757) |
| <b>NET CASH USED IN OPERATING ACTIVITIES</b>                                                              |           |           |
| <b>CASH AND CASH EQUIVALENTS</b>                                                                          |           |           |
| <b>AT BEGINNING OF YEAR</b>                                                                               | 220,966   | 524,646   |
| <b>EFFECT OF EXCHANGE RATE CHANGES</b>                                                                    | 1,587     | 77        |
| <b>CASH AND CASH EQUIVALENTS</b>                                                                          | 205,527   | 220,966   |
| <b>AT END OF YEAR</b>                                                                                     | 205,527   | 220,966   |
| <b>ANALYSIS OF CASH AND CASH EQUIVALENTS</b>                                                              |           |           |
| Deposits with banks and other financial institutions with original maturity within three months           | 157,381   | 157,068   |
| Cash at bank                                                                                              | 48,146    | 63,898    |
|                                                                                                           | 205,527   | 220,966   |

The accompanying notes 1 to 17 form part of these financial statements.

# QUALITY EDUCATION FUND

## Notes to the financial statements

*(Amounts expressed in thousands of Hong Kong dollars, unless otherwise stated.)*

### 1. General

The Quality Education Fund (the Fund) was established by a declaration of trust made on 2 January 1998 by the Permanent Secretary for Education Incorporated (the Trustee). The Fund provides grants to fund projects that aim to raise the quality of school education, and to promote quality school education in Hong Kong.

### 2. Significant accounting policies

#### (a) Statement of compliance

The financial statements have been prepared in accordance with section 8(3) of the Permanent Secretary for Education Incorporation Ordinance (Cap. 1098), accounting principles generally accepted in Hong Kong, and all applicable Hong Kong Financial Reporting Standards (HKFRSs), which is a collective term that includes all applicable individual HKFRSs, Hong Kong Accounting Standards (HKASs) and Interpretations issued by the Hong Kong Institute of Certified Public Accountants (HKICPA). A summary of the significant accounting policies adopted by the Fund is set out below.

#### (b) Basis of preparation of the financial statements

The measurement basis used in the preparation of the financial statements is historical cost except that financial assets designated at fair value and trading financial instruments are stated at their fair value as explained in the accounting policies set out below.

The preparation of financial statements in conformity with HKFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and the reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making judgements about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

There are no critical accounting judgements involved in the application of the Fund's accounting policies. There are also no key assumptions concerning the future, and other key sources of estimation uncertainty at the end of the reporting



period, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities in the next year.

(c) Financial assets and financial liabilities

(i) Initial recognition

The Fund classifies its financial assets and financial liabilities into different categories at inception, depending on the purpose for which the assets were acquired or the liabilities were incurred. The categories are: trading financial instruments, financial assets designated at fair value, loans and receivables, held-to-maturity securities and other financial liabilities.

Financial assets and financial liabilities are measured initially at fair value plus, for loans and receivables, held-to-maturity securities and other financial liabilities, transaction costs that are directly attributable to the acquisition of the financial assets or the issue of the financial liabilities. Transaction costs on trading financial instruments and financial assets designated at fair value are expensed immediately.

The Fund recognises financial assets and financial liabilities on the date it becomes a party to the contractual provisions of the instrument. Regular way purchases and sales of financial assets are accounted for at trade date.

(ii) Categorisation and subsequent measurement

*Trading financial instruments*

These comprise forward currency contracts used by the Fund to manage its risks associated with foreign currency fluctuations. Such derivative financial instruments do not qualify for hedge accounting and are categorised as “trading” under HKAS 39, Financial Instruments: Recognition and Measurement.

Trading financial instruments are carried at fair value, and presented as assets when the fair value is positive and as liabilities when the fair value is negative. Changes in the fair value are included in surplus or deficit in the period in which they arise.

*Financial assets designated at fair value*

Financial assets designated at fair value consist of equity and debt securities that are managed and evaluated on a fair value basis in accordance with a documented risk management and investment strategy.

Financial assets designated at fair value are carried at fair value. Changes in the fair value are included in surplus or deficit in the period in which they arise.

### *Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and which the Fund has no intention of trading, other than those that the Fund, upon initial recognition, designates at fair value. This category includes cash at bank, deposits with banks and other financial institutions, placement with the Exchange Fund, receivables and other assets.

Loans and receivables are carried at amortised cost using the effective interest method less impairment losses, if any (note 2(c)(vi)).

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Fund estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees received or paid between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

### *Held-to-maturity securities*

Held-to-maturity securities are non-derivative financial assets with fixed or determinable payments and fixed maturity which the Fund has the positive intention and ability to hold to maturity, other than (a) those that the Fund, upon initial recognition, designates as at fair value; and (b) those that meet the definition of loans and receivables.

Held-to-maturity securities are carried at amortised cost using the effective interest method less impairment losses, if any (note 2(c)(vi)).

### *Other financial liabilities*

These are financial liabilities other than trading financial instruments. This category includes payables and other liabilities. They are carried at amortised cost using the effective interest method.

### (iii) Fair value measurement principles

The Fund measures its investments in certain securities and trading financial instruments at fair value at the end of each reporting period. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either (a) in the principal market for the asset or liability, or (b) in the absence of a

principal market, in the most advantageous market for the asset or liability; and the Fund has access to these markets at the measurement date.

The fair value of an asset or a liability is measured with those assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their best economic interest.

The Fund uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs. The Fund measures fair values using the following fair value hierarchy that reflects the significance of inputs used in making the measurements:

Level 1 – fair values are quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2 – fair values are determined with inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and

Level 3 – fair values of financial instruments are determined with inputs that are not based on observable market data (unobservable inputs).

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Fund determines whether transfers between levels in the hierarchy should be reflected in the financial statements by re-assessing categorisation (based on the level of input that is most significant and relevant to the fair value measurement as a whole) at the end of the reporting period.

(iv) Derecognition

A financial asset is derecognised when the contractual rights to receive the cash flows from the financial asset expire, or where the financial asset together with substantially all the risks and rewards of ownership have been transferred.

The Fund uses the weighted average method to determine realised gains and losses to be recognised in surplus or deficit on derecognition.

A financial liability is derecognised when the obligation specified in the contract is discharged, cancelled or when it expires.

(v) Offsetting

Financial assets and financial liabilities are offset and the net amount is reported in the statement of financial position where there is a legally enforceable right to offset the recognised amounts and there is an intention

to settle on a net basis, or realise the assets and settle the liabilities simultaneously.

(vi) Impairment of financial assets

The carrying amounts of loans and receivables and held-to-maturity securities are reviewed at the end of each reporting period to determine whether there is objective evidence of impairment. If any such evidence exists, an impairment loss is recognised in surplus or deficit as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate. If in a subsequent period the amount of such impairment loss decreases and the decrease can be linked objectively to an event occurring after the impairment loss was recognised, the impairment loss is reversed through surplus or deficit. A reversal of impairment losses is limited to the asset's carrying amount that would have been determined had no impairment loss been recognised in prior years.

(d) Revenue recognition

(i) Interest income

Interest income is recognised in surplus or deficit on an accrual basis, using the effective interest method.

(ii) Dividend income

Dividend income from equity securities is recognised in surplus or deficit when the share price is quoted ex-dividend.

(iii) Net realised and revaluation gains/losses

Realised gains or losses on financial instruments are recognised in surplus or deficit when the financial instruments are derecognised. Changes in fair value of trading financial instruments and financial assets designated at fair value are recognised as revaluation gains or losses in surplus or deficit in the period in which they arise.

(iv) Other income

Other income is recognised in surplus or deficit on an accrual basis.

(e) Grants recognition

Grants are payable to schools, educational bodies, institutions or individuals who are permanent residents in Hong Kong. Grants are recognised as expenditure when they are approved by the Trustee except in those cases where the release of grant is subject to certain conditions, such grants are only recognised as expenditure when the conditions are met.

(f) Foreign currency translation

Foreign currency transactions during the year are translated into Hong Kong dollars at the spot exchange rates at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated into Hong Kong dollars at the closing exchange rates at the end of the reporting period. All foreign currency translation differences are recognised in surplus or deficit.

(g) Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents include cash at bank and deposits with banks and other financial institutions with original maturity within three months.

(h) Impact of new and revised HKFRSs

The HKICPA has issued certain new and revised HKFRSs that are first effective or available for early adoption for the current accounting period. There have been no changes to the accounting policies applied in the financial statements for the years presented as a result of these developments. The Fund has not applied any new HKFRSs that are not yet effective for the current accounting period (note 17).

**3. Interest income**

|                                                               | 2017   | 2016   |
|---------------------------------------------------------------|--------|--------|
| This represents interest income from:                         |        |        |
| — placement with the Exchange Fund                            | 18,295 | 3,640  |
| — held-to-maturity debt securities                            | 730    | 1,900  |
| — debt securities designated at fair value<br>denominated in: |        |        |
| — Hong Kong dollar                                            | 14,122 | 14,902 |
| — other currencies                                            | 39,204 | 40,302 |
|                                                               | 53,326 | 55,204 |
| — deposits denominated in:                                    |        |        |
| — Hong Kong dollar                                            | 5,537  | 3,319  |
| — other currencies                                            | 9,900  | 21,356 |
|                                                               | 15,437 | 24,675 |
|                                                               | 87,788 | 85,419 |



**4. Dividend income**

|                                                                | 2017          | 2016          |
|----------------------------------------------------------------|---------------|---------------|
| This represents dividend income from equity securities listed: |               |               |
| — in Hong Kong                                                 | 44,157        | 37,660        |
| — outside Hong Kong                                            | 51,769        | 45,160        |
|                                                                | <u>95,926</u> | <u>82,820</u> |

**5. Other income**

|                                           | 2017         | 2016       |
|-------------------------------------------|--------------|------------|
| Sale of materials developed from projects | 117          | 214        |
| Commission recapture income               | 57           | 45         |
| Tax refund                                | 3,915        | —          |
|                                           | <u>4,089</u> | <u>259</u> |

**6. Grants and awards**

|                                             | 2017          | 2016          |
|---------------------------------------------|---------------|---------------|
| Grants paid/due for payment                 | 70,121        | 85,374        |
| Refund of unused grants                     | (5,046)       | (6,172)       |
|                                             | 65,075        | 79,202        |
| Awards under the teaching excellence scheme | 6,768         | 7,735         |
|                                             | <u>71,843</u> | <u>86,937</u> |

**7. Operating expenses**

|                                   | 2017          | 2016          |
|-----------------------------------|---------------|---------------|
| Dissemination and promotion costs | 23,592        | 28,793        |
| Fees for investment managers      | 17,933        | 16,885        |
| Investment transaction costs      | 4,945         | 4,490         |
| Fees for custodians               | 2,852         | 2,671         |
| Others                            | 153           | 207           |
|                                   | <u>49,475</u> | <u>53,046</u> |

**8. Deposits with banks and other financial institutions**

|                                                                                                           | 2017                  | 2016               |
|-----------------------------------------------------------------------------------------------------------|-----------------------|--------------------|
| Fixed deposits denominated in:                                                                            |                       |                    |
| — Hong Kong dollar                                                                                        | 55,960                | 800,630            |
| — other currencies                                                                                        | 822,950               | 270,501            |
| Call deposits and balances with custodians<br>denominated in currencies other than<br>Hong Kong dollar    | <u>133,902</u>        | <u>92,948</u>      |
|                                                                                                           | <b>1,012,812</b>      | 1,164,079          |
| Less: Deposits with banks and other financial<br>institutions with original maturity<br>over three months | <u>(855,431)</u>      | <u>(1,007,011)</u> |
| Deposits with banks and other financial<br>institutions with original maturity<br>within three months     | <u><b>157,381</b></u> | <u>157,068</u>     |

**9. Securities**

|                                                                                                      | 2017                    | 2016             |
|------------------------------------------------------------------------------------------------------|-------------------------|------------------|
| <i>Held-to-maturity securities at amortised cost</i>                                                 |                         |                  |
| Debt securities denominated in currencies<br>other than Hong Kong dollar<br>maturing within one year | —                       | 57,922           |
| <i>Financial assets designated at fair value</i>                                                     |                         |                  |
| Equity securities listed:                                                                            |                         |                  |
| — in Hong Kong                                                                                       | 1,573,087               | 1,246,255        |
| — outside Hong Kong                                                                                  | 2,901,689               | 2,755,087        |
| Debt securities denominated in:                                                                      |                         |                  |
| — Hong Kong dollar                                                                                   | 510,428                 | 600,019          |
| — other currencies                                                                                   | 1,986,723               | 2,251,270        |
|                                                                                                      | <u><b>6,971,927</b></u> | <u>6,910,553</u> |

## 10. Trading financial instruments

|                                              | 2017         |               | 2016         |              |
|----------------------------------------------|--------------|---------------|--------------|--------------|
|                                              | Assets       | Liabilities   | Assets       | Liabilities  |
| Forward currency contracts,<br>at fair value | <u>4,600</u> | <u>17,533</u> | <u>8,140</u> | <u>7,723</u> |

All these forward currency contracts would mature within one year and had a total notional amount of HK\$1,539.7 million as at 31 August 2017 (2016: HK\$1,759.0 million). The notional amounts of these contracts indicate the volume of outstanding transactions and do not represent the amounts at risk.

## 11. Receivables and other assets

|                                                           | 2017          | 2016           |
|-----------------------------------------------------------|---------------|----------------|
| Proceeds receivable from investments sold                 | 37,162        | 78,137         |
| Accrued interest from placement with<br>the Exchange Fund | 15,757        | 3,640          |
| Other interest and dividends receivable                   | 35,264        | 29,878         |
| Other receivables                                         | <u>10,542</u> | <u>7,053</u>   |
|                                                           | <u>98,725</u> | <u>118,708</u> |

## 12. Placement with the Exchange Fund

The balance of the placement with the Exchange Fund amounted to HK\$1,116.9 million (2016: HK\$230.7 million), being the principal sums of HK\$1,110.7 million (2016: HK\$230.7 million) plus interest paid but not yet withdrawn at the end of the reporting period of HK\$6.2 million (2016: nil). The term of the placement is six years from the date of placement, during which the amount of principal sums cannot be withdrawn.

Interest on the placement is payable at a fixed rate determined every January. The rate is the average annual investment return of the Exchange Fund's Investment Portfolio for the past six years or the average annual yield of three-year government bond for the previous year subject to a minimum of zero percent, whichever is the higher. The interest rate has been fixed at 2.8% for the calendar year 2017 and at 3.3% for the calendar year 2016.

### 13. Payables and other liabilities

|                                    | 2017          | 2016          |
|------------------------------------|---------------|---------------|
| Unsettled purchases of investments | 54,866        | 74,677        |
| Other payables and accruals        | <u>7,550</u>  | <u>10,756</u> |
|                                    | <u>62,416</u> | <u>85,433</u> |

### 14. Commitments

As at 31 August 2017, grants approved but not yet due for payment (note 2(e)) amounted to HK\$167.8 million (2016: HK\$81.2 million).

### 15. Financial risk management

#### (a) Investment management and control

The Trustee may invest moneys of the Fund in accordance with section 5 of the Permanent Secretary for Education Incorporation Ordinance. She has appointed the Director of Accounting Services to manage the investments of the Fund.

The Steering Committee, established under the declaration of trust, may advise the Trustee on policies and procedures governing the operation of the Fund and on the assessment of applications for the funding from the Fund. Members of the Steering Committee are appointed by the Secretary for Education.

The Fund's investment objective is to generate a reasonable growth in the value of the funds whilst producing recurrent income to meet regular funding requests in order to support the development of quality education in Hong Kong and to fund activities that aim to raise the quality of school education, and to promote quality school education in Hong Kong.

The investment performance of the Fund is monitored through the Investment Committee which meets regularly to review investment reports prepared by the Director of Accounting Services and to interview the Fund's external investment managers. The Investment Committee also formulates guidelines on asset allocation in order to meet the investment objective. Members of the Investment Committee are appointed by the Secretary for Education.

The investment management and control of the Fund are set out in a documented risk management and investment strategy and are reviewed on a regular basis by the Investment Committee.

#### (b) Market risk

Market risk is the risk that changes in market variables such as equity prices, interest rates and currency exchange rates may affect the fair value or cash flows of a financial instrument.

(i) Equity price risk

Equity price risk is the risk of loss arising from changes in equity prices. The Fund's equities are subject to the equity price risk inherent in all equity securities, i.e. the value of holdings may fall as well as rise. As at 31 August 2017, the equities were included in securities as shown in note 9. The risk is primarily addressed through diversification of investment portfolio in accordance with a documented risk management and investment strategy, and the Fund monitors the risk on a continuous basis.

It was estimated that, as at 31 August 2017, a 10% increase/decrease in the market bid prices of the equities, with all other variables held constant, would increase/decrease the surplus for the year by HK\$447.5 million (2016: HK\$400.1 million).

(ii) Interest rate risk

Interest rate risk refers to the risk of loss arising from changes in market interest rates. This can be further classified into fair value interest rate risk and cash flow interest rate risk.

Fair value interest rate risk is the risk that the fair value of a financial instrument will fluctuate because of changes in market interest rates. Since a substantial portion of the Fund's debt securities and all of its deposits with banks and other financial institutions bear interest at fixed rates, their fair values will fall when market interest rates increase. Investments in debt securities are made in accordance with a documented risk management and investment strategy, and the Fund monitors the fair value interest rate risk on a continuous basis.

It was estimated that, as at 31 August 2017, a 100 basis points increase/decrease in interest rates, with all other variables held constant, would decrease/increase the surplus for the year by HK\$152.6 million (2016: HK\$160.7 million). As regards deposits with banks and other financial institutions and held-to-maturity securities, since they are all stated at amortised cost, their carrying amounts will not be affected by changes in market interest rates.

Cash flow interest rate risk is the risk that future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Fund does not have a significant exposure to cash flow interest rate risk because only a small portion of its debt securities bear interest at rates determined by reference to market interest rates.

(iii) Currency risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in currency exchange rates. The Fund's foreign currency investments are exposed to currency risk. The Fund only makes investments denominated in Hong Kong dollar, US dollar, Renminbi and currencies of countries whose foreign currency long-term debt



has a high credit rating. The Fund's exposure to currency risk is handled in accordance with a documented risk management and investment strategy, and the Fund monitors the risk on a continuous basis.

The net exposure to each currency at the end of the reporting period arising from recognised assets and liabilities after taking into account the effect of forward currency contracts is shown below:

|                  | 2017                    | 2016                    |
|------------------|-------------------------|-------------------------|
| Hong Kong dollar | 4,103,149               | 3,826,563               |
| US dollar        | 3,577,358               | 3,135,023               |
| Renminbi         | —                       | 58,149                  |
| Euro             | 728,249                 | 697,979                 |
| Japanese yen     | 325,438                 | 339,034                 |
| Pound sterling   | 184,366                 | 181,159                 |
| Others           | <u>254,579</u>          | <u>165,015</u>          |
|                  | <u><u>9,173,139</u></u> | <u><u>8,402,922</u></u> |

It was estimated that, as at 31 August 2017, with all other variables held constant:

- a 0.5% increase/decrease in the exchange rate of US dollar against Hong Kong dollar would increase/decrease the surplus for the year by HK\$17.9 million (2016: HK\$15.7 million); and
- a 5% increase/decrease in the exchange rates of other currencies against Hong Kong dollar would increase/decrease the surplus for the year by HK\$74.6 million (2016: HK\$72.1 million).

(c) Credit risk

Credit risk is the risk that an issuer or a counterparty will cause a financial loss to the Fund by failing to discharge an obligation. Investments in debt securities, trading financial instruments and loans and receivables are potentially subject to credit risk. The Fund selects issuer or counterparty with good credit standing, strong financial strength and sizeable capital. The Fund also limits the individual exposure, in accordance with a documented risk management and investment strategy, and monitors credit risk on a continuous basis.

The credit quality of cash at bank, deposits with banks and other financial institutions and debt securities at the end of the reporting period, analysed by the ratings designated by Moody's or their equivalents, is shown below:

|                                                                                                | 2017                    | 2016                    |
|------------------------------------------------------------------------------------------------|-------------------------|-------------------------|
| Cash at bank and deposits with<br>banks and other financial institutions, by<br>credit rating: |                         |                         |
| Aa3 to Aa1                                                                                     | 174,901                 | 578,106                 |
| A3 to A1                                                                                       | <u>886,057</u>          | <u>649,871</u>          |
|                                                                                                | <u><u>1,060,958</u></u> | <u><u>1,227,977</u></u> |

|                                    | 2017                    | 2016                    |
|------------------------------------|-------------------------|-------------------------|
| Debt securities, by credit rating: |                         |                         |
| Aaa                                | 722,453                 | 809,670                 |
| Aa3 to Aa1                         | 553,556                 | 846,444                 |
| A3 to A1                           | 970,578                 | 976,466                 |
| Baa3 to Baa1                       | 250,564                 | 274,428                 |
| Below Baa3                         | <u>—</u>                | <u>2,203</u>            |
|                                    | <u><u>2,497,151</u></u> | <u><u>2,909,211</u></u> |

For the placement with the Exchange Fund, the credit risk is considered to be low.

The maximum exposure to credit risk of the financial assets of the Fund is equal to their carrying amounts at the end of the reporting period.

(d) Liquidity risk

Liquidity risk is the risk that the Fund will encounter difficulty in meeting obligations associated with financial liabilities. The Fund monitors the liquidity requirements on a continuous basis and maintains a level of short-term deposits and cash to pay grants and operating expenses as necessary. Hence the Fund does not have significant exposure to liquidity risk.

As at 31 August 2017, the remaining contractual maturities of all financial liabilities, based on contractual undiscounted cash flows and the earliest date on which the Fund can be required to pay, were one year or less (2016: one year or less).

(e) Other financial risk

The Fund is exposed to financial risk arising from change in the interest rate on the placement with the Exchange Fund which is determined every January (note 12). It was estimated that, as at 31 August 2017, a 50 basis points increase/decrease in the interest rate, with all other variables held constant, would increase/decrease the surplus for the year by HK\$3.2 million (2016: HK\$0.6 million).

## 16. Fair values of financial instruments

The fair value of financial instruments classified under Level 1 is based on the quoted market prices of these financial instruments at the end of the reporting period, without any deduction for estimated future selling costs.

In the absence of such quoted prices, the fair value of financial instruments classified under Level 2 is estimated using present value or other valuation techniques which maximise the use of observable data, using inputs based on market conditions existing at the end of the reporting period.

### (a) Financial instruments measured at fair value on a recurring basis

The carrying value of financial instruments measured at fair value at the end of the reporting period according to the fair value hierarchy is shown below:

| 2017                                      | Level 1          | Level 2          | Total            |
|-------------------------------------------|------------------|------------------|------------------|
| Assets                                    |                  |                  |                  |
| Financial assets designated at fair value | 4,474,776        | 2,497,151        | 6,971,927        |
| Trading financial instruments             | —                | 4,600            | 4,600            |
|                                           | <u>4,474,776</u> | <u>2,501,751</u> | <u>6,976,527</u> |
| Liabilities                               |                  |                  |                  |
| Trading financial instruments             | —                | 17,533           | 17,533           |
|                                           | <u>—</u>         | <u>17,533</u>    | <u>17,533</u>    |
| 2016                                      |                  |                  |                  |
|                                           | Level 1          | Level 2          | Total            |
| Assets                                    |                  |                  |                  |
| Financial assets designated at fair value | 4,301,792        | 2,550,839        | 6,852,631        |
| Trading financial instruments             | —                | 8,140            | 8,140            |
|                                           | <u>4,301,792</u> | <u>2,558,979</u> | <u>6,860,771</u> |
| Liabilities                               |                  |                  |                  |
| Trading financial instruments             | —                | 7,723            | 7,723            |
|                                           | <u>—</u>         | <u>7,723</u>     | <u>7,723</u>     |

No financial assets or liabilities were classified under Level 3.

### (b) Financial instruments not measured at fair value on a recurring basis

All other financial instruments are stated in the statement of financial position at amounts equal to or not materially different from their fair values.

**17. Possible impact of amendments, new standards and interpretations issued but not yet effective for the year ended 31 August 2017**

Up to the date of issue of the financial statements, the HKICPA has issued a number of amendments, new standards and interpretations which are not yet effective for the year ended 31 August 2017 and which have not been early adopted in the financial statements.

The Fund is in the process of making an assessment of what the impact of these amendments, new standards and interpretations is expected to be in the period of initial adoption. So far, it has concluded that the adoption of them is unlikely to have a significant impact on the Fund's results of operations and financial position.

The following development may result in new or amended disclosures in future financial statements:

**Effective for accounting  
periods beginning on or after**

HKFRS 9, *Financial Instruments*

1 January 2018