

Executive Management's Report

Railway Operations

Total fare revenue for the Company in 2007 increased by 9.1% to HK\$7,115 million as a result of increase in patronage from the economic growth in Hong Kong as well as the Rail Merger effect from 2 December to the end of 2007.

Patronage

For the year as a whole, total patronage on the Integrated MTR System increased by 8.2% to 948.3 million, including the Rail Merger effect since 2 December.

Our Domestic Service, which includes the MTR Lines (comprising the Kwun Tong, Tsuen Wan, Island, Tung Chung, Tseung Kwan O and Disneyland Resort lines) and after the Rail Merger, the KCR Lines (comprising the East Rail excluding Cross-boundary Service, West Rail and Ma On Shan lines), recorded total patronage of 915.8 million for 2007. Fare revenue increased by 5.1% to HK\$6,213 million.

Airport Express' passenger volume rose 6.3% to 10.2 million. For the Cross-boundary Service at Lo Wu and Lok Ma Chau, a total patronage of 8.2 million was recorded for the period from 2 December to the year end. Fare revenue from the Airport Express increased by 7.0% to HK\$655 million whilst Cross-boundary, Light Rail, Intercity and Bus services contributed total revenue of HK\$247 million after the Rail Merger.

Our overall share of the franchised public transport market increased from 25.0% in 2006 to 25.3% in the period before the Rail Merger. After the Rail Merger including all rail and bus passenger services, our market share increased further to 41.6%.

Service Promotions

One of the key contributors of our incremental patronage growth is the effectiveness of our service promotions. A number of station events and segment promotions were launched, including MTR Hello Kitty Heroes Redemption Programme and the Ride 5 Get Free Breakfast Promotion.

In a strategic partnership with the Hong Kong Tourism Board, a tailor-made shopping guide entitled "MTR Easy Ride to Hong Kong Shopping Festival" was distributed to tourists who purchased a MTR 1-day Pass or Tourist Octopus during the promotion period. This programme increased sales of these two products by 48% compared to the same period last year.

For Airport Express, the popular "Ride to Rewards" programme was enhanced with new rewards for registered members that accumulated four journeys on Airport Express. For Asia

World-Expo, we joined with trade show organisers to arrange same-day return trips on Airport Express as well as discounted prices for visitors.

The flourishing economy of the Pearl River Delta continued to benefit the Cross-boundary and through train businesses that we took over from KCRC on the Appointed Day. For long-haul Intercity services to Beijing and Shanghai, a fare promotion for both single trip and round trip passengers during non-peak periods continued. For Cross-boundary Service, we launched promotions by offering free rides to Lok Ma Chau Station in the New Year and Lunar New Year holidays.

For East Rail Line, West Rail Line and Ma On Shan Line, most of the promotion activities that were in place before the Appointed Day continued, such as the Monthly Pass for the East Rail Line and West Rail Line and Day Pass for the West Rail Line.

Service Performance

Continuity of good performance is essential in an era of transformation. For the period before the Rail Merger in 2007, we exceeded all the minimum performance levels required by the Government and our own more stringent Customer Service Pledge targets for the MTR System. Passenger journeys on time were 99.9% (Airport Express 99.9%), supported by 99.9% reliability for train service delivery and 99.8% train punctuality (Airport Express 99.9%).

With the Rail Merger, a new Operating Agreement came into effect from 2 December 2007 to include the East Rail Line, West Rail Line, Ma On Shan Line and Light Rail. The performance levels of the integrated network for the post-Merger period from 2 December to the end of 2007 will be incorporated into the next period for reporting purposes.

These results underpinned our "We serve from the heart" campaign, which was launched during the year to further enhance passenger service. This campaign was supplemented by other monthly campaigns promoting train door and escalator safety, as well as general safety.

Customer satisfaction levels remained high. In 2007, the Service Quality Index for the MTR Lines and Airport Express stood at 72 and 81 respectively, while the Fare Index, which indicates the level of satisfaction of customers with our fares, stood at 61 and

62 respectively. This performance also received international recognition. In the benchmarking performed by the 11-member Community of Metros (CoMET) for 2006, we continued to hold a leading position.

The excellence of our service performance was again reflected in the winning of numerous awards. In Hong Kong, we won East Week magazine's "Hong Kong Service Awards" in the Public Transport category for the third consecutive year. We also won Next Magazine's "Top Service Award" – Public Transport Category for the ninth consecutive year. International recognition came in the form of the Gold Asset Management Excellence Award, awarded jointly by the Asset Management Council and Maintenance Engineering Society of Australia at the 2007 International Asset Management Conference.

Service Improvements

We continued to enhance train services and network infrastructure.

The new platform serving SkyPlaza at Hong Kong International Airport Terminal 2 was opened and put into operation on 28 February 2007.

The opening of new pedestrian links at various stations further enhanced accessibility to the MTR System. Three Pacific Place Link was completed in February and provided a linkage between Admiralty Station and Three Pacific Place. Two new entrances at Kowloon Station were opened to link up with the Elements shopping centre. On the West Rail Line, three new footbridges are under construction at Tuen Mun Station, which will link with a nearby passenger transport interchange and new residential development.

The station improvement initiatives continued to upgrade the ambience and design of MTR stations. 46 stations on the merged network underwent renovations and enhancements of various kinds to enrich station environment and provide more shopping outlets.

Two new "Self-Service Point" prototype machines were installed for trial use in Hong Kong Station starting from July and performance monitoring progressed well. The Self-Service Point machine is another new service channel for passengers, providing them with a more convenient and straightforward way of resolving ticketing issues.

To improve passenger comfort on the existing network, five new trains are being procured for use on Tsuen Wan, Kwun Tong, Island and Tseung Kwan O lines.

The noise enclosure project in the Tung Chung area was completed, which brought a reduction in the level of train noise in the area. Improvement work was also in progress in the Tsing Yi area.

Productivity

Improving efficiency and productivity remained a key priority for the Company. In March, we completed the replacement of 469 motor alternator sets on the 78 trains on the MTR Lines with state-of-the-art static inverter units, thereby achieving energy savings of HK\$7.7 million per year whilst also reducing noise levels. The static inverter replacement work also started for trains on the East Rail Line with planned completion in 2010 and estimated energy cost savings of HK\$5.1 million per year. Operating costs per car kilometre decreased by 2.3% to HK\$21.6 for our enlarged network.

Station Commercial and Rail Related Businesses

Revenue from the Company's station commercial and rail related businesses increased by 12.9% in 2007 to HK\$1,741 million. The revenue increase was driven by a strong economy, rising patronage and the Rail Merger effect from 2 December to the end of 2007. Excluding the Rail Merger effect, such revenues would have increased by 4.8% in 2007 to HK\$1,616 million.

Advertising

Advertising revenue grew by 11.0% to HK\$593 million (a 9.6% increase to HK\$585 million excluding the Rail Merger effect), supported by higher passenger volumes and advertising innovations.

The MTR Plasma TV network continued to be enhanced. We successfully replaced 68 units of trackside plasmas and their

back-end system by the end of March 2007 for maintaining the best viewing quality for our passengers.

On Airport Express, the replacement of seatback TV with a new multimedia system was completed in May 2007. At the end of May, we launched rental payment services for Hong Kong Housing Authority tenants at Customer Service Centres in stations on the Kwun Tong, Island, Tsuen Wan, Tung Chung and Tseung Kwan O lines.

With the Rail Merger, advertising coverage now extends to the enlarged network including the cross-boundary market. The scale of our advertising business also increased, with the number of advertising media in stations and trains totalling 20,564 and 27,011 respectively at the year end.