CEO's review of operations and outlook

Dear Stakeholders,

The first six months of 2007 saw continued progress for MTR Corporation. Firstly, and importantly, all legislation required to implement the proposed merger with the Kowloon-Canton Railway Corporation (KCRC), except the Commencement Notice to establish a date to commence the Rail Merger Bill, has now been approved by the Legislative Council of Hong Kong (LegCo). The next stage of the proposed merger is independent shareholders' approval by way of an Extraordinary General Meeting (EGM) of the Company, which is likely to be held in October. Secondly, in our growth outside of Hong Kong, we together with our partner, Laing Rail, were awarded the London Overground concession in June. This is our first "asset light" train operating franchise in Europe.

The Company's financial results for the first half of 2007 remained strong, with good growth in revenue and operating profit before depreciation and property development profit. However, property development profit was lower in the first half of 2007 compared with the same period in 2006, as we had accounted for property development profit from a number of Tseung Kwan O projects, such as The Grandiose and Metro Town, in the first half of last year, the magnitude of which was not repeated in the first six months of 2007. The recognition of property development profit is dependent on completion of development projects which vary from year to year. As highlighted in our 2006 Annual Report, we will account for property development profits from Le Point at Tiu Keng Leng Station upon receipt of the Occupation Permit, which is expected in the fourth quarter of 2007. The development costs relating to Le Point had already been accounted for in 2006.

The Company's revenue for the period rose 6.3% to HK$4,852 million as compared with the first six months of 2006. Operating profit from railway and related businesses before depreciation increased by 6.0% to HK$2,797 million. Property development profit realised in the period was HK$1,664 million, compared with HK$4,072 million in the same period of 2006. As a result, profit attributable to equity shareholders, excluding gain from revaluation of investment properties net of tax, was HK$2,050 million. Gain from investment properties revaluation before tax was HK$2,450 million (HK$2,021 million post-tax), resulting in reported net profit of HK$4,071 million, a decline of 21.2 % over the first six months of 2006. Reported earnings per share were HK$0.73, and the Board has declared an interim dividend of HK$0.14 per share.

Railway Operations

Total fare revenue for the first half of 2007 increased by 3.5% to HK$3,247 million when compared with the same period last year. Revenue growth was driven by rising patronage and a slight increase in average fare.

For the first six months, total patronage on the MTR Lines reached another record of 429.3 million, a 2.6% increase over the same period in 2006. Average weekday patronage increased by 3.0% to 2.5 million. Despite strong competition, the Company's share of the total franchised public transport market increased to 25.0% from 24.7%, with the share of cross-harbour traffic rising from 60.4% to 61.2%. Average fare on the MTR Lines increased by 0.6% to HK$6.84 when compared with the first six months of 2006 due to changes in promotion program, longer journey distance travelled by passengers and higher growth in cross-harbour movements. As a result, fare revenue on the MTR Lines rose 3.1% to HK$2,935 million.

Passenger volume on Airport Express rose 7.2% from 4.5 million to 4.8 million, as the number of air travellers using Hong Kong International Airport continued to rise, and the number of exhibitions and other events at the AsiaWorld-Expo increased. Fare revenue on Airport Express increased by 6.8% to HK$312 million.

We once again exceeded both the minimum performance levels required by the Government under the Operating Agreement, and our own more stringent Customer Service Pledges.

Service promotions on the MTR Lines continued to support patronage growth, with events such as "red packet" promotions and the first ever wedding in an MTR station. There was also a successful trial initiative to encourage people to travel earlier so as to relieve morning peak congestion.

Airport Express launched a "Children travel free" promotion from the end of 2006 to February 2007, and beginning in April, discounts on Airport Express tickets were offered to MTR shareholders, accompanied by dining offers at SkyPlaza restaurants. The "Ride to Rewards" programme was enhanced with new rewards for registered enrollees having accumulated four journeys on Airport Express.

To encourage use of MTR by travellers further away from MTR stations, the number of fare saver machines offering discounts to Octopus card holders increased by two to 21 in total. The number of feeder bus routes offering intermodal fare discount was maintained at 32, helping to promote patronage through enhancing the connection between the MTR system and other modes of transport.

Technology improvements included completion of the programme to replace motor alternators with static inverters on 78 trains on the MTR Lines, which improved reliability and energy efficiency.

Access to stations was enhanced through a third platform at the Airport Station to serve passengers using the new Airport Passenger Terminal 2, while the Three Pacific Place pedestrian link to Admiralty Station was opened in February.

Investments in facilities for the disabled continued across the network. Installation of a new internal passenger lift at Admiralty Station began in June and self operated stair lifts came into operation in three stations.

Train door and escalator safety were a focus of passenger education. To minimise train door incidents, we extended the door-closing chimes and deployed train door safety ambassadors. Desirable passenger behaviour was further promoted through in-station games and sponsored school tours organised by Metro Broadcast Radio's metro show biz. Escalator safety ambassadors were also deployed at selected stations.

We were honoured to have received a number of awards for our services, including the Sing Tao Excellent Services Brand Award 2006 – Public Transportation presented by *Sing Tao Daily*, Hong Kong Service Awards – Public Transportation Category presented by *East Week* Magazine, Q-Mark Service Scheme Award, HKGCC Environmental Performance Award, *Next Magazine*'s Top Service Awards 2007 – Public Transportation Category, and Eco-Service Enterprise Award. Furthermore, international recognition for our asset management came with the Gold Asset Management Excellence Award, and the Steve Maxwell Leadership Award for our Operations Director, awarded jointly by the Asset Management Council and the Maintenance Engineering Society of Australia.

Operations performance in first half 2007

Service performance item	Performance Requirement	Customer Service Pledge target	**Actual performance**
Train service delivery	98.5%	99.5%	**99.9%**
Passenger journeys on time			
– MTR Lines	98.5%	99.5%	**99.9%**
– Airport Express	98.0%	99.0%	**99.9%**
Train punctuality			
– MTR Lines	98.0%	99.0%	**99.8%**
– Airport Express	98.0%	99.0%	**99.9%**
Train reliability: train car-km per train failure causing delays ≥ 5 minutes	N/A	500,000	**1,776,730**
Ticket reliability: magnetic ticket transactions per ticket failure	N/A	8,000	**15,607**
Add value machine reliability	98.0%	98.5%	**99.5%**
Ticket issuing machine reliability	97.0%	98.0%	**99.5%**
Ticket gate reliability	97.0%	99.0%	**99.8%**
Escalator reliability	98.0%	99.0%	**99.9%**
Passenger lift reliability	98.5%	99.0%	**99.9%**
Temperature and ventilation			
– Trains: to maintain a cool, pleasant and comfortable train environment generally at a temperature at or below 26˚C	N/A	97.0%	**99.9%**
– Stations: to maintain a cool, pleasant and comfortable environment generally at or below 27˚C for platforms and 29˚C for station concourses, except on very hot days	N/A	90.0%	**99.9%**
Cleanliness			
– Train compartment: cleaned daily	N/A	98.5%	**100%**
– Train body: washed every 2 days	N/A	98.0%	**100%**
Passenger enquiry response time within 7 working days	N/A	99.0%	**99.9%**

Station Commercial and Rail Related Businesses

An expanding economy and rising patronage supported our advertising and station commercial businesses but decreases in telecommunication and consultancy income led to revenue for the six months being unchanged from the same period in 2006 at HK$735 million.

Advertising revenue rose by 3.8% to HK$248 million, sustained by higher passenger volumes and more innovative advertising formats. The advertising business also benefited from the replacement of seatback TV with the new multimedia system in Airport Express carriages, which was completed in May.

Station retail revenue increased 9.5% to HK$208 million as both rental rates and retail sales volumes trended higher. New layouts and refurbishments were completed at five stations during the six months, bringing an additional 10.4% or 1,760 square metres of retail floor space into operation, resulting in a total retail footage in our stations of 18,627 square metres. In all, 39 new shops and 12 new trades were added, resulting in a total of 582 shops.

Revenue from telecommunications services declined by 20.3% to HK$110 million, partly due to a one-off recognition of income from a mobile operator network upgrade in 2006 which was not repeated in 2007. Revenue shared with 2G mobile operators was affected by further cuts in tariffs and cannibalisation of call minutes to 3G mobile services. Our fixed network services provider TraxComm Limited recorded higher revenue, and by the end of June had provided over 180Gbps of bandwidth services to carrier customers.

Revenue from consultancy was HK$82 million during the six months, a decrease of 16.3% compared to the same period in 2006 mainly due to the deferred installation work for Phase 2 of the Automated People Mover project at the Hong Kong International Airport. In the Mainland of China, we secured a design review consultancy for Chengdu Metro and a study funded by the Asian Development Bank, while new contracts were also secured in Europe and India.

Overseas Expansion

Our expansion overseas saw a step forward with the award of the London Overground concession to our joint venture MTR Laing Metro Limited (now renamed as London Overground Railway Operations Limited (LORO)), whilst work progressed on the Beijing Metro Line 4 (BJL4) project as well as on the approval for the Shenzhen Metro Line 4 (SZL4) project.

Mainland of China

In the Mainland of China, the Public-Private Partnership (PPP) company comprising MTR Corporation, Beijing Infrastructure Investment Co. Ltd. and Beijing Capital Group made good progress on the BJL4 project.

By the end of June, tendering for the Electrical & Mechanical (E&M) Works Contracts was nearly complete. Design work for E&M equipment including rolling stock, power supply, communications, platform screen doors and automatic fare collection was making substantial progress. A mock-up of the rail cars to be used on the new line has been completed and the quality management system of the PPP company was successfully granted ISO9001 certification in April. The senior operations team is now in place and around 250 train drivers and station controllers have been recruited to join the one-and-a-half year training programme that will start in September. About 70% of the tunnelling works have been completed. The first batch of eight stations is to be handed over to the PPP company for E&M installation in September. We anticipate that this line will begin operations in 2009.

In Shenzhen, the Company is still liaising with Shenzhen Municipal Government and the National Development and Reform Commission on the final approval of the SZL4 project. Preparatory work continues, whilst expanded trial section work has begun.

We continue to pursue other projects in the Mainland of China, such as the BJL4 Extension, or Daxing Line, and the development of new lines in Wuhan, Hangzhou and Suzhou.

Europe

In Europe, where we are committed to an "asset light" strategy of bidding for rail operating service contracts, our 50:50 joint venture with the UK's Laing Rail was awarded the London Overground concession on 19 June. LORO was selected out of four companies short-listed to bid for the franchise.

Under this concession, LORO will operate five existing lines in Greater London for seven years from 11 November 2007, with an option for a two-year extension at the discretion of Transport for London (TfL). The cost based operating concession, which will be overseen by TfL, will receive an amount of around £700 million over the lifetime of the contract, which includes an expected profit margin for LORO.

London Overground is an important franchise in the UK capital. It is a semi-orbital route serving West, North and East London and will be a crucial link for the 2012 Olympic Games. The total route network measures 107.2 kilometres and under the franchise, LORO will eventually manage 55 of the 78 stations on the network. Among the five lines, the East London Line is currently undergoing an extensive extension and upgrade programme and is scheduled to re-open in 2010.

Some of the service improvements already planned for London Overground include the introduction of a more comprehensive ticketing system, a phased programme of station upgrades to improve comfort and security for passengers, as well as the introduction of a fleet of new trains from 2009.

Our earlier bid with our joint venture partner Swedish railway company SJ for the Öresundståg concessions in Sweden and Denmark was unsuccessful.

Property and Other Businesses

The property market saw broad based strength in the first half of 2007. The Grade A office market saw strong demand, as capital markets activity led to expansion by financial services firms. The retail market was supported by local spending and inbound tourism. Prices in the luxury residential market enjoyed strong upward momentum, while demand in the mass residential market remained strong.

Property Development

For the six months, profit on property developments was HK$1,664 million, mainly derived from developments along the Airport Railway.

The contributors to property development profit from Airport Railway projects were deferred income recognition in line with construction and / or sales progress at Elements in Kowloon Station, and at Coastal Skyline and Caribbean Coast in Tung Chung, as well as surplus proceeds from Harbour Green at Olympic Station and from Caribbean Coast.

Pre-sales were launched at Crystal Cove in Tung Chung and sales were relaunched at Harbour Green with good response, whilst occupation permits were obtained for the two towers of The Cullinan and The HarbourView Place at Kowloon Station.

Following approval by the Town Planning Board, the land application procedure has begun for the conversion of part of the lorry park and transport interchange adjacent to Tsing Yi Station to commercial use.

On the Tseung Kwan O Line, sales were relaunched for Le Point at Tiu Keng Leng Station, with positive response from the market. Construction of the superstructure for Area 86 Package One continued on schedule and the foundation works for Package Two are substantially complete.

The tender for Area 56 in Tseung Kwan O was awarded in February to Lansmart Ltd, a subsidiary of Sun Hung Kai Properties Ltd, with the plan to develop a hotel, residential, office and retail complex in Tseung Kwan O Town Centre.

In Shenzhen, the master development plan for SZL4 property projects has been completed. We are now awaiting approval for the overall SZL4 project.

Property Rental, Management and Other Businesses

Total revenue from property rental, property management and other businesses increased by 25.5% to HK$870 million during the six months compared to the same period of 2006.

Demand for both office and retail space was robust and rental income increased by 13.8% over the comparable period in 2006 to HK$710 million. The increase was driven by favourable rental renewals and new lettings, as well as contribution from The Edge, which opened in November 2006 and Ginza Mall in Beijing.

The strong demand from retailers enabled us to maintain 100% occupancy at all of our shopping centres, except for areas under renovation at Telford Plaza and Luk Yeung Galleria. Our office premises at Two IFC also maintained full occupancy. Elements, our new shopping centre at Kowloon Station, is now 100% pre-let and hand over to tenants had begun. The tenant mix of our retail portfolio was enhanced further by the addition of new trades at Telford Plaza and Maritime Square.

Our property management business saw revenue increase 19.4% to HK$80 million. During the six months, 2,338 residential units were added to the portfolio, bringing the total number of residential units managed by the Company to 61,214 at the end of June, together with 583,372 square metres of commercial space.

In the Mainland of China, following refurbishment and rebranding, Ginza Mall, the shopping centre in Beijing, opened in January and by the end of June had been 99% let. Memoranda of Understanding were signed for property management contracts for two more office and commercial developments in the capital, with SOHO China Ltd for a project at Guanghua Lu and with Nan Fung China Holdings Ltd for one at Xidan.

The Ngong Ping 360 cable car and associated theme village on Lantau Island which opened in September 2006 contributed revenue of HK$80 million during the first six months of 2007. Since opening, the tourist attraction has carried some 1.5 million passengers, which exceeded our projections for the first 12 months of operations. In June, during the annual testing outside of operation hours, one of the gondolas detached from the cable. There were no injuries and operations immediately ceased, followed by detailed investigations. We will only resume passenger operations of the cable car system once we are completely satisfied with all safety aspects of the system.

Octopus continued to extend its operations to new areas within and beyond the transport sector, helped by the launch of the "Portable Octopus Processor" that enables smaller retailers to join the system. Cards in circulation rose to 15.4 million and average daily transaction volume and value rose to 9.9 million and HK$78.4 million respectively. The number of service providers increased by 20% to 456. MTR Corporation's share of earnings from Octopus Holdings Limited rose by 50% to HK$42 million for the six-month period.

Tseung Kwan O Line property developments (packages awarded)

Location	Developers	Type	Gross floor area (sq. m.)	No. of parking spaces	Status	Actual or expected completion date
Tseung Kwan O Station						
Area 57a	Sun Hung Kai Properties Ltd.	Residential	26,005		Awarded	Completed
(Central Heights)	Nan Fung Development Ltd.	Retail	3,637		in July	in 2005
	Henderson Land Development Co. Ltd.	Car park		74	2000	
	Chime Corporation Ltd.					
Area 55b	New World Development Co. Ltd.	Residential	84,920		Awarded	Completed
(The Grandiose	Chow Tai Fook Enterprises Ltd.	Retail	11,877		in January	in 2006
and The Edge)	Wee Investments Pte. Ltd.	Car park		249	2002	
Area 56	Sun Hung Kai Properties Ltd.	Residential	80,000		Awarded	2011
		Hotel	58,130		in February	
		Retail	20,000		2007	
		Office	5,000			
		Car park		363		
Hang Hau Station						
(Residence Oasis	Sino Land Co. Ltd.	Residential	138,652		Awarded	Completed
and The Lane)	Kerry Properties Ltd.	Retail	3,500		in June	in 2004
		Car park		369	2002	
Tiu Keng Leng Station						
(Metro Town)	Cheung Kong (Holdings) Ltd.	Residential	236,965		Awarded in	By phases
		Retail	16,800		October	from
		Car park		609	2002	2006–2007
Tseung Kwan O South Station						
Area 86 Package One	Cheung Kong (Holdings) Ltd.	Residential	136,240		Awarded	2008
		Retail	500		in January	
		Car park		325	2005	
		Residential Care				
		Home for the Elderly	3,100			
Area 86 Package Two	Cheung Kong (Holdings) Ltd.	Residential	309,696		Awarded	By phases
		Kindergarten	800		in January	from
		Car park		905	2006	2009–2010

Tseung Kwan O Line property developments (packages to be awarded)

Location	No. of packages envisaged	Type	Gross floor area (sq. m.)	Expected No. of parking spaces	Period of package tenders	Expected completion date
Tseung Kwan O South Station	6–11	Residential	1,153,764 –			
Area 86*			1,163,764		2007–2011	2015
		Retail	39,500 – 49,500			
		Car park		3,653 (max.)		

* Subject to review in accordance with planning approval, land grant conditions and completion of statutory processes.

Choi Hung Park and Ride development

Location	Developers	Type	Gross floor area (sq. m.)	No. of parking spaces	Status	Actual completion date
Choi Hung Station	Chun Wo Holdings Ltd.	Residential	19,138		Awarded	Completed
(No. 8 Clear Water Bay Road)		Retail	2,400		in July 2001	in 2005
		Car park		54		
		Park & Ride		450		

Hong Kong Network Expansion Projects

MTR Corporation's projects to expand and enhance the network in Hong Kong continued throughout the first half of 2007.

The construction of Tseung Kwan O South Station is on track, with all civil, building services and system-wide contracts progressing satisfactorily. By the end of June, some 90% of the station concrete had been placed and track laying had begun. Construction of the Government entrusted works for one of the access roads is also progressing on programme. This station is expected to open in April 2009.

Following the Government's announcement of proposals for the rejuvenation of Aberdeen and Ap Lei Chau, centred on a new Fisherman's Wharf, we submitted a revised proposal for the South Island Line (East) in June.

Negotiations with the Government on the proposed West Island Line continued. Drafting of the gazette documents has proceeded and preparatory work for the next design stage is underway.

Work has begun on a new pedestrian subway for Lai Chi Kok Station and design of a new subway at Prince Edward Station is under review.

The Government accepted the proposal for construction of entrances linking Tsim Sha Tsui Station with the redevelopment of No. 63 Nathan Road, while our proposal for an underground link at Causeway Bay Station remains under review. The design of a further subway at the north end of Tsim Sha Tsui Station to link with adjoining developments has begun.

Merger with KCRC

The Rail Merger Bill was passed in LegCo on 8 June and By-Laws and Regulations on 11 July. Hence all legislation except the final Commencement Notice is now approved. We are now in the final stages of agreeing legal documents with the Government and KCRC, after which the proposed merger will be submitted to independent shareholders for approval at an EGM, which is likely to be held in October.

A circular containing details of the transaction, as well as recommendations from the Independent Board Committee, which is advised by the Independent Financial Adviser, Merrill Lynch, will be dispatched to shareholders after the signing of the legal agreements. Shareholders should make their own decisions on the merger and are advised to read the EGM Circular carefully. If independent shareholders approve the merger, the Government would then need to introduce the Commencement Notice in LegCo for approval by LegCo for the Rail Merger Bill to come into effect. We would then proceed to Day One of the merger, which could take place by the end of the year.

The Joint Integration Group and Merger Integration Office have continued to lead the work to prepare for the proposed merger and all of the integration issues have now been substantially resolved to facilitate a smooth start from Day One of the merger.

Financial Review

The Group's financial performance in the first half of 2007 continued to benefit from the economic growth of Hong Kong with total revenue increasing by 6.3% to HK$4,852 million as compared with the same period last year. Fare revenue grew by 3.5% to HK$3,247 million, mainly attributable to patronage increases of 2.6% for the MTR Lines and 7.2% for Airport Express. Average fare for the MTR Lines also increased from HK$6.80 to HK$6.84, whilst average fare for Airport Express declined slightly from HK$64.80 to HK$64.40 due to the larger proportion of passengers traveling to and from the AsiaWorld-Expo Station paying lower fares. Non-fare revenues rose by 12.4% to HK$1,605 million as the strong retail market helped increase revenue from advertising and station commercial facilities as well as rentals from our properties, while additional income streams were generated from the new Ngong Ping 360 and the expanded property rental and management portfolios in Hong Kong and Beijing.

Operating costs before depreciation for the first half of 2007 increased by 6.6% to HK$2,055 million as compared with the same period last year. The increase was mainly attributable to business expansion in property rental, management and other businesses, increased business development in Europe and China, as well as a non-recurring refund of operational rent and rates in 2006. As a result, operating profit from railway and related businesses before depreciation was HK$2,797 million, a 6.0% increase from the same period last year, with the operating profit margin at 57.6% in the first half of 2007.

Property development profit for the first half of 2007 amounted to HK$1,664 million, mainly comprising surplus proceeds from Harbour Green and Caribbean Coast along the Airport Railway as well as deferred income recognition from Coastal Skyline, Caribbean Coast and Elements, also along the Airport Railway. Operating profit before depreciation amounted to HK$4,461 million, a decrease of 33.5% from the same period last year due to a decrease in property development profits where in the first half of 2006 substantial surplus proceeds were recognised from The Grandiose and Metro Town along the Tseung Kwan O Line .

Depreciation charge for the first half of 2007 increased by 2.5% to HK$1,348 million mainly due to the addition of depreciation charge for Ngong Ping 360. With strong cash flow and reduction in total borrowings, net interest expense decreased by 11.5% to HK$654 million as compared with the same period last year. The increase in fair value of investment properties since the end of 2006 amounted to HK$2,450 million pre-tax and HK$2,021 million post-tax.

Including the share of profit from Octopus of HK$42 million, profit before taxation decreased by 19.5% to HK$4,951 million when compared with the same period last year. Income tax correspondingly decreased by 10.7% to HK$879 million, which was wholly non-cash deferred income tax. Net profit attributable to shareholders of the Company for the first half of 2007 therefore amounted to HK$4,071 million, with reported earnings per share of HK$0.73. Excluding investment property revaluation gain and related deferred tax, underlying net profit was HK$2,050 million, while earnings per share were HK$0.37.

The Directors have declared an interim dividend of HK$0.14 per share, which is the same as last year. As with previous dividend payments, a scrip dividend option will be offered to all shareholders except those with registered addresses in the United States of America or any of its territories or possessions. The Company's majority shareholder, the Financial Secretary Incorporated (FSI), has agreed to receive its entitlement to dividends in the form of shares to the extent necessary to ensure that a maximum of 50% of the Company's total dividend will be paid in cash.

The Group's balance sheet remains strong. During the first half of 2007, shareholders' equity increased by 4.6% to HK$80,277 million as of 30 June, from retained profit as well as the re-investment of scrip dividends by the Government and other shareholders.

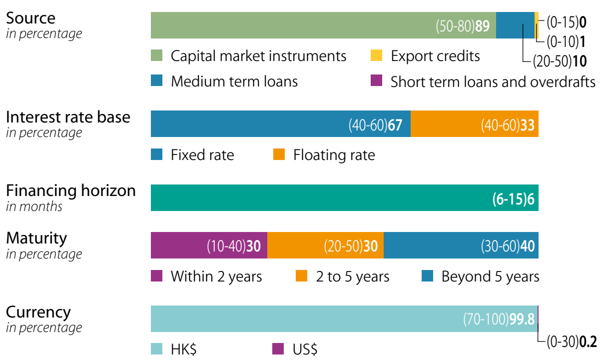
Total assets increased by 2.2% to HK$123,034 million largely due to property revaluation gains of HK$2,595 million mainly from the office space at Two IFC and from retail space at Telford Plaza, Maritime Square and Luk Yeung Galleria. There were also increases in fitting out project works of HK$213 million at Elements and property held for sale of HK$146 million from unsold units mainly at Harbour Green. Other increases in assets include capital expenditure incurred on the SkyPlaza Platform project and other capital improvement projects.

During the period, the Group's total borrowings decreased from HK$28,152 million to HK$25,170 million due mainly to loan repayments. As a result, the debt-to-equity ratio decreased from 36.7% at 31 December 2006 to 31.4% at period-end.

The Group's net cash inflow from railway and related activities increased to HK$2,981 million in the first half of 2007 compared to HK$2,728 million for the same period in 2006, while cash receipts from property development projects increased to HK$3,136 million from HK$584 million in the first half of 2006, mainly due to receipt of forward sale deposits from Le Point at Tiu Keng Leng Station development. Total cash outflow before dividend and loan repayment decreased to HK$2,057 million as compared to HK$6,293 million in 2006 when an interest-free loan of HK$4,000 million was provided to the property developer of Tseung Kwan O Area 86 Package Two. Major outflows included capital project payments of HK$1,062 million, interest expenses of HK$791 million, investment in our associate Beijing MTR Corporation Limited, of HK$103 million and other minor items. After dividend payments of HK$777 million and net loan repayment of HK$3,176 million, there was a net cash inflow of HK$107 million.

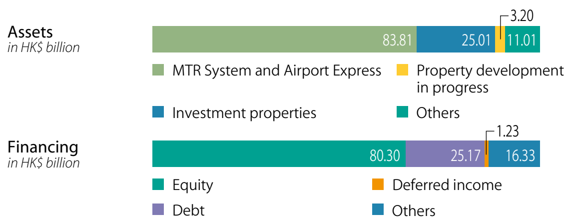
Preferred financing model and debt profile

(Preferred Financing Model) vs. **Actual debt profile**
As at 30 June 2007



Simplified balance sheet

As at 30 June 2007



Financing Activities

With our strong positive cash flows and the availability of a sizeable pool of undrawn committed banking facilities, we did not raise any new debt financings during the period. As at the end of June 2007, the Group had total undrawn committed facilities of HK$6.3 billion. Apart from additional funding that may be required for the proposed merger with KCRC, these undrawn committed facilities, together with cash on hand and projected positive operating cash flow, are expected to cover all of our estimated funding needs until the end of 2007.

During the period, we continued to manage our debt portfolio in a prudent manner in accordance with our Preferred Financing Model to achieve adequate risk diversification. As at the end of June 2007, the Company's debt maturity profile was well balanced, with 30% of total outstanding repayable within 2 years, 30% between 2 and 5 years, and 40% beyond 5 years. In terms of exposure to foreign currency risk, only 0.2% of the debt portfolio was denominated in US dollars with the remainder either hedged into or denominated in HK dollars. In terms of interest rate risk, about 33% of our debt carried interest based on floating interest rates with the balance either based on or hedged into fixed interest rates. This prudent level of fixed rate debt enabled us to maintain our average borrowing cost at 5.7%, roughly the same level as the 5.5% experienced during the same period last year, despite generally higher interest rates in 2007.

Human Resources

Maintaining harmonious staff relations and attracting and retaining high calibre people remain key elements in supporting rapid business growth.

During the merger integration discussions, extensive communication and consultation with staff and staff bodies of both companies ensured acceptance of the salary protection principles, as well as major terms and conditions of employment post merger. A series of cultural integration workshops were arranged together with KCRC, for managers and senior supervisors from both companies.

These workshops helped keep staff up to date on the latest developments in the merger integration process, to prepare them for the coming challenges and to receive their feedback. The workshops were attended by some 1,200 managers and supervisors and a total of 107 Integration Ambassadors were identified as change agents to champion merger-related changes.

MTR Corporation's numerous training and development programmes, designed to enhance skills and maintain motivation, continued throughout the first half of 2007, with courses covering topics ranging from railway safety rules to empowerment and empathetic listening.

Resourcing and developing our staff for our overseas business continue to be a focus and we also implemented programmes designed to build an MTR culture at operations outside Hong Kong.

Outlook

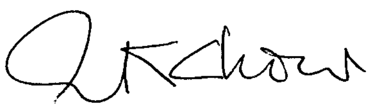
Barring any external shocks, we continue to hold a cautiously positive view for the economy in Hong Kong.

Our rail businesses, as well as most of our non-fare and rail related businesses, will continue to benefit from Hong Kong's economic growth. However, our telecommunications business will face continuing headwinds from the further cannibalisation of 2G users by 3G.

In our property rental business, we plan to open Phase 1 of Elements, our majority owned shopping centre in Kowloon Station in the fourth quarter of 2007. We continue to see positive rental reversions across our portfolio which will also benefit from the full year effect of the opening of The Edge and Ginza Mall.

In our property development business we expect to receive Occupation Permit for Le Point at Tiu Keng Leng Station in the fourth quarter of 2007. As I have noted in the past, in accordance with the Development Agreement and our accounting policy, costs relating to Le Point were already accounted for when we accounted for profits for Metro Town in the first half of 2006. Given current market conditions, pre-sales and the issuance of the Occupation Permit for Area 86 Package One may allow for profit recognition for that development in 2008.

Finally, I take this opportunity to thank all of my colleagues for their continued commitment to making our business a success.



C K Chow, *Chief Executive Officer*
Hong Kong, 7 August 2007