

Notes to the Unaudited Interim Financial Report

1 Basis of Preparation

This interim financial report is unaudited, but has been reviewed by KPMG in accordance with Hong Kong Standard on Review Engagements 2410 “Review of Interim Financial Information Performed by the Independent Auditor of the Entity”, issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”). KPMG’s review report to the Board of Directors is set out on page 48. In addition, this interim financial report has been reviewed by the Company’s Audit Committee.

This interim financial report has been prepared in accordance with the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, including compliance with Hong Kong Accounting Standard (“HKAS”) 34 “Interim financial reporting” issued by the HKICPA.

The preparation of an interim financial report in conformity with HKAS 34 requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses on a year to date basis. Actual results may differ from these estimates.

This interim financial report contains the condensed consolidated accounts and selected explanatory notes, which include an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the Company and its subsidiaries (collectively referred to as the “Group”) and the Group’s interest in non-controlled subsidiaries and associates since the issuance of the 2007 annual accounts. The condensed consolidated interim accounts and notes thereon do not include all of the information required for full set of accounts prepared in accordance with Hong Kong Financial Reporting Standards (“HKFRSs”).

The financial information relating to the financial year ended 31 December 2007 included in the interim financial report does not constitute the Company’s statutory accounts for that financial year but is derived from those accounts. Statutory accounts for the year ended 31 December 2007, on which the auditors have expressed an unqualified opinion on those accounts in their report dated 11 March 2008, are available from the Company’s registered office.

The same accounting policies adopted in the 2007 annual accounts have been applied to the interim accounts.

In the current interim period, the Group has applied, for the first time, a number of new standards, amendments and interpretations (“new HKFRSs”) issued by the HKICPA, which are effective for the Group’s financial period beginning on or after 1 January 2008:

HK(IFRIC) Interpretation 11, HKFRS 2 – Group and treasury share transactions

HK(IFRIC) Interpretation 14, HKAS 19 – The limit on a defined benefit asset, minimum funding requirements and their interaction

The adoption of these new HKFRSs had no material effect on the results and financial position of the Group for the current or prior accounting periods. Accordingly, no prior period adjustment has been recognized.

In 2007, the HKICPA issued HK(IFRIC) Interpretation 12 “Service concession arrangements” to provide guidance on the accounting by operators in service concession arrangements to be effective for reporting periods commencing on or after 1 January 2008. As the merger of the Company’s operations with Kowloon–Canton Railway Corporation (“KCRC”) on 2 December 2007 is considered to include a service concession arrangement under HK(IFRIC) Interpretation 12, the Company has early adopted the Interpretation in the 2007 accounts.

2 Rail Merger with Kowloon-Canton Railway Corporation

On 2 December 2007 (the “Appointed Day”), the Company’s operations merged with those of KCRC (“Rail Merger”). The structure and key terms of the Rail Merger were set out in a series of transaction agreements entered into between, inter alia, the Government of the Hong Kong Special Administrative Region, KCRC and the Company including the Service Concession Agreement, Property Package Agreements and Merger Framework Agreement. Key elements of the Rail Merger include the following:

- The expansion of the Company’s existing franchise under the Mass Transit Railway Ordinance (“MTR Ordinance”) to cover the construction, operation and regulation of railways in addition to the MTRC railway for an initial period of 50 years from the Appointed Day (“Franchise Period”), which may be extended pursuant to the provisions of the MTR Ordinance;
- The Service Concession Agreement (“SCA”) pursuant to which KCRC granted the Company the right to access, use and operate the KCRC system for an initial term of 50 years (the “Concession Period”), which will be extended if the Franchise Period (as it relates to the KCRC railway) is extended. The SCA also sets out the basis on which the KCRC system will be returned at the end of the Concession Period. In accordance with the terms of the SCA, the Company paid an upfront lump sum to KCRC on the Appointed Day and is obliged to pay an annual fixed payment to KCRC for the duration of the Concession Period. Additionally, commencing after three years from the Appointed Day, the Company is obliged to pay an annual variable fee to KCRC based on the revenue generated from the KCRC system above certain thresholds;
- Under the SCA, the Company is responsible for the expenditure incurred in relation to the maintenance, repair, replacement and upgrade of the KCRC system (with any new assets acquired being classified as “additional concession property”). To the extent that such expenditure exceeds an agreed threshold (“Capex Threshold”), the Company will be reimbursed for any above threshold expenditure at the end of the Concession Period with such reimbursement to be on the basis of depreciated book value;

2 Rail Merger with Kowloon-Canton Railway Corporation *(continued)*

- In the event that the Concession Period is extended, the fixed annual payment and the variable annual payment will continue to be payable by the Company. On such extension, the Capex Threshold may also be adjusted;
- With effect from the Appointed Day, staff of the Company and KCRC have been employed by the Company on their prevailing terms and conditions of employment. In connection with the Rail Merger, a Staff Voluntary Separation Scheme has been offered to eligible staff;
- Property Package Agreements whereby property assets comprising certain investment and own-used properties, property management rights and property development rights were acquired by the Company;
- Merger Framework Agreement setting out the framework for the Rail Merger including the implementation of the Fare Adjustment Mechanism whereby the extent to which fares may be adjusted is linked to certain public indices, the provision of a fare reduction starting from the Appointed Day and the guarantee of job security for front line staff employed at the time of the Rail Merger;
- Pursuant to the above and the vesting and novation of certain contracts, the Company assumed certain assets and liabilities of KCRC on the Appointed Day. The assumption of the liabilities of deposits refundable to third parties was subject to compensation by KCRC on the Appointed Day; and
- Other post-Appointed Day arrangements between the Company and KCRC such as the arrangements documented by the Kowloon Southern Link ("KSL") Project Management Agreement, the West Rail Agency Agreement and the Outsourcing Agreement.

The principle terms of the Rail Merger and their financial impact were described in the Company's audited accounts for the year ended 31 December 2007. Income and expenditure and assets and liabilities in relation to the operation of the service concession are accounted for in the respective line items of the Group's profit and loss account and balance sheet.

3 Profit on Property Developments

Profit on property developments comprises:

<i>in HK\$ million</i>	Half year ended 30 June 2008	Half year ended 30 June 2007
Transfer from deferred income on		
– up-front payments	95	510
– sharing in kind	37	42
Share of surplus from development	224	1,100
Income recognised from sharing in kind	–	21
Other overhead costs	(8)	(9)
	348	1,664

4 Share of Profits of Non-controlled Subsidiaries and Associates

Share of profits of non-controlled subsidiaries and associates comprises:

<i>in HK\$ million</i>	Half year ended 30 June 2008	Half year ended 30 June 2007
Share of profit before taxation of non-controlled subsidiaries	86	50
Share of profit before taxation of associates	19	–
	105	50
Share of income tax of non-controlled subsidiaries	(8)	(8)
Share of income tax of associates	(6)	–
	91	42

5 Income Tax

Income tax in the consolidated profit and loss account represents:

<i>in HK\$ million</i>	Half year ended 30 June 2008	Half year ended 30 June 2007
Current tax for the period	6	–
Deferred tax		
– Origination and reversal of temporary differences on:		
– change in fair value of investment properties	343	429
– utilisation of tax losses	406	423
– others	(43)	27
	706	879
– Effect of decrease in the Hong Kong Profits Tax rate from 17.5% to 16.5%	(704)	–
	2	879
	8	879

No provision for current Hong Kong Profits Tax has been made in the consolidated profit and loss account in respect of the Company and most of its subsidiaries, as the Company and these subsidiaries either have substantial accumulated tax losses brought forward which are available for set off against current period's assessable profits or have sustained tax losses for the half year ended 30 June 2008. Current Hong Kong Profits Tax totalling HK\$5 million (2007: nil) was provided for certain of the Company's subsidiaries acquired in the Rail Merger, calculated at the prevailing Hong Kong Profits Tax rate at 16.5%. Current taxation for overseas subsidiaries of HK\$1 million (2007: nil) is charged at the appropriate current rates of taxation ruling in the relevant countries.

Provision for deferred tax on temporary differences arising in Hong Kong is calculated at the Hong Kong Profits Tax rate at 16.5% (2007: 17.5%).

6 Dividends

During the period, dividends paid and proposed to equity shareholders of the Company comprised:

<i>in HK\$ million</i>	Half year ended 30 June 2008	Half year ended 30 June 2007
Dividends payable in respect of 2008		
– Interim dividend declared after the balance sheet date of 14 cents (2007: 14 cents) per share	790	782
Dividend in respect of 2007		
– 2007 final dividend of 31 cents (2006: 28 cents) per share approved and paid in 2008	1,740	1,554

7 Earnings Per Share

A Basic Earnings Per Share

The calculation of basic earnings per share is based on the profit for the half year ended 30 June 2008 attributable to equity shareholders of HK\$4,689 million (2007: HK\$4,071 million) and the weighted average number of ordinary shares of 5,613,941,337 in issue during the period (2007: 5,550,144,410), calculated as follows:

	Half year ended 30 June 2008	Half year ended 30 June 2007
Issued ordinary shares at 1 January	5,611,057,035	5,548,613,951
Effect of scrip dividends issued	2,290,854	1,082,419
Effect of share options exercised	593,448	448,040
Weighted average number of ordinary shares at 30 June	5,613,941,337	5,550,144,410

B Diluted Earnings Per Share

The calculation of diluted earnings per share is based on the profit for the half year ended 30 June 2008 attributable to equity shareholders of HK\$4,689 million (2007: HK\$4,071 million) and the weighted average number of ordinary shares of 5,619,005,310 in issue during the period (2007: 5,555,165,343) after adjusting for the number of dilutive potential ordinary shares under the employee share option schemes, calculated as follows:

	Half year ended 30 June 2008	Half year ended 30 June 2007
Weighted average number of ordinary shares at 30 June	5,613,941,337	5,550,144,410
Number of ordinary shares deemed to be issued for no consideration	5,063,973	5,020,933
Weighted average number of ordinary shares (diluted) at 30 June	5,619,005,310	5,555,165,343

C Both basic and diluted earnings per share would have been HK\$0.49 (2007: HK\$0.37) if the calculation is based on profit from underlying businesses attributable to equity shareholders, i.e. excluding increase in fair value of investment properties net of related deferred tax, adjusted as follows:

<i>in HK\$ million</i>	Half year ended 30 June 2008	Half year ended 30 June 2007
Profit attributable to equity shareholders	4,689	4,071
Increase in fair value of investment properties	(2,080)	(2,450)
Deferred tax on change in fair value of investment properties		
– Effect of the change during the period (note 5)	343	429
– Effect of decrease in the Hong Kong Profits Tax rate from 17.5% to 16.5%	(221)	-
Profit from underlying businesses attributable to equity shareholders	2,731	2,050

8 Segmental Information

Segmental information is presented in accordance with the Group's business segments, which comprise the following:

Railway operations: The operation of an urban mass transit railway system within Hong Kong and an Airport Express serving both the Hong Kong International Airport and the AsiaWorld-Expo at Chek Lap Kok and, after the Rail Merger, the KCR System consisting of the East Rail Line (excluding Cross-boundary Service), West Rail Line, Ma On Shan Line, Cross-boundary Service, Light Rail, Bus and Intercity passenger services.

Station commercial and rail related businesses: Commercial activities including letting of advertising and retail space, bandwidth services on the railway telecommunication system, railway consultancy services, freight and rail related subsidiaries' businesses.

Property ownership, management and other businesses: Property rental, property management and operations relating to Ngong Ping 360.

Property developments: Property development at locations relating to the railway system.

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8 Segmental Information (continued)

The Group's results of major business activities for the half year ended 30 June 2008, with comparative figures for the half year ended 30 June 2007, are summarised below:

<i>in HK\$ million</i>	Railway operations	Station commercial and rail related businesses	Property ownership, management and other businesses	Total railway operations and related activities	Property developments	Total
Half year ended 30 June 2008						
Revenue	5,592	1,645	1,290	8,527	–	8,527
Operating expenses before depreciation and amortisation	(2,662)	(388)	(340)	(3,390)	–	(3,390)
	2,930	1,257	950	5,137	–	5,137
Profit on property developments	–	–	–	–	348	348
Operating profit before depreciation and amortisation	2,930	1,257	950	5,137	348	5,485
Depreciation and amortisation	(1,413)	(38)	(37)	(1,488)	–	(1,488)
	1,517	1,219	913	3,649	348	3,997
Unallocated corporate expenses						(370)
Merger related expenses						(24)
Operating profit before interest and finance charges						3,603
Interest and finance charges						(1,078)
Change in fair value of investment properties			2,080			2,080
Share of profits of non-controlled subsidiaries and associates						91
Income tax						(8)
Profit for the period ended 30 June 2008						4,688
Half year ended 30 June 2007						
Revenue	3,247	735	870	4,852	–	4,852
Operating expenses before depreciation and amortisation	(1,413)	(165)	(223)	(1,801)	–	(1,801)
	1,834	570	647	3,051	–	3,051
Profit on property developments	–	–	–	–	1,664	1,664
Operating profit before depreciation and amortisation	1,834	570	647	3,051	1,664	4,715
Depreciation and amortisation	(1,258)	(32)	(32)	(1,322)	–	(1,322)
	576	538	615	1,729	1,664	3,393
Unallocated corporate expenses						(280)
Operating profit before interest and finance charges						3,113
Interest and finance charges						(654)
Change in fair value of investment properties			2,450			2,450
Share of profits of non-controlled subsidiaries and associates						42
Income tax						(879)
Profit for the period ended 30 June 2007						4,072

As substantially all the principal operating activities of the Group were carried out in Hong Kong throughout the reporting periods, no geographical analysis is provided.

9 Investment Properties

Investment properties carried at fair value were revalued at 30 June 2008 on an open market basis by an independent firm of surveyors, Jones Lang LaSalle Limited (30 June 2007: DTZ Debenham Tie Leung), who have among their staff Members of the Hong Kong Institute of Surveyors. As a result, a gain of HK\$2,080 million (2007: HK\$2,450 million), and deferred tax thereon of HK\$343 million (2007: HK\$429 million) in respect of the investment properties, have been included in the consolidated profit and loss account.

10 Other Property, Plant and Equipment

A Acquisitions and Disposals

During the half year ended 30 June 2008, the Group acquired or commissioned assets at a total cost of HK\$576 million (2007: HK\$684 million). Items of self-occupied office land and buildings, civil works and plant and equipment with a net book value of HK\$54 million (2007: HK\$14 million) were disposed of during the same period, resulting in a net loss on disposal of HK\$8 million (2007: HK\$14 million).

B Valuation

Self-occupied office land and buildings carried at fair value were revalued at 30 June 2008 on an open market value basis by an independent firm of surveyors, Jones Lang LaSalle Limited (30 June 2007: DTZ Debenham Tie Leung), who have among their staff Members of the Hong Kong Institute of Surveyors. As a result, revaluation surpluses of HK\$86 million (2007: HK\$120 million), net of deferred tax, have been transferred to the fixed asset revaluation reserve (note 25).

11 Service Concession Assets

Service concession assets comprise the Company's right to access, use and operate the KCRC system ("Initial Concession Property") and the expenditures incurred in relation to the maintenance, repair, replacement and upgrade of the KCRC system. During the half year ended 30 June 2008, the Company had additions of HK\$178 million (2007: nil) and charged HK\$154 million (2007: nil) to the profit and loss account as amortisation.

12 Property Development in Progress

Property development in progress comprises foundation, site enabling works and land costs incurred by the Company for property development projects, net of payments received from developers. Movements of property development in progress during the half year ended 30 June 2008 and the year ended 31 December 2007 were as follows:

<i>in HK\$ million</i>	Balance at 1 January	Expenditure	Offset against payments received from developers	Balance at 30 June/ 31 December
30 June 2008 (Unaudited)				
Airport Railway Property Projects	–	15	(15)	–
Tseung Kwan O Extension Property Projects	3,307	100	(6)	3,401
East Rail Line/Light Rail/Kowloon Southern Link Property Projects	5,759	1,855	(42)	7,572
	9,066	1,970	(63)	10,973
31 December 2007 (Audited)				
Airport Railway Property Projects	–	139	(139)	–
Tseung Kwan O Extension Property Projects	3,297	288	(278)	3,307
East Rail Line/Light Rail/Kowloon Southern Link Property Projects	–	5,812	(53)	5,759
	3,297	6,239	(470)	9,066

13 Deferred Expenditure

Deferred expenditure comprises capital expenditures on the preliminary studies and designs of new railway extensions including the Shenzhen Metro Line 4, West Island Line, Kwun Tong Line Extension, South Island Line East, Shatin to Central Link and Express Rail Link.

During the half year ended 30 June 2008, the Company received the first part of the Government's capital grant for the West Island Line Project of HK\$400 million, which has been used to offset the detailed design cost incurred up to 30 June 2008.

14 Interests in Associates

During the half year ended 30 June 2008, the Group has made a further equity contribution of HK\$515 million to Beijing MTR Corporation Limited, a public-private partnership company in which the Group holds a 49% interest, making the cumulative equity contribution HK\$718 million as at 30 June 2008. More details are set out in note 26C.

15 Properties Held for Sale

<i>in HK\$ million</i>	At 30 June 2008 (Unaudited)	At 31 December 2007 (Audited)
Properties held for sale		
– at cost	404	649
– at net realisable value	107	107
	511	756

Properties held for sale at net realisable value are stated net of provision of HK\$12 million (2007: HK\$12 million) made in order to state these properties at the lower of their cost and estimated net realisable value.

16 Derivative Financial Assets and Liabilities

Derivative financial assets and liabilities comprise:

<i>in HK\$ million</i>	At 30 June 2008 (Unaudited)		At 31 December 2007 (Audited)	
	Notional amount	Fair value	Notional amount	Fair value
Derivative Financial Assets				
Foreign exchange forwards				
– fair value hedges	7	–	7	–
– cash flow hedges	1,580	16	777	15
– not qualified for hedge accounting	206	16	265	3
Cross currency swaps				
– fair value hedges	5,224	82	2,012	70
Interest rate swaps				
– fair value hedges	4,448	139	4,698	184
– cash flow hedges	300	13	300	1
Others	300	1	–	–
	12,065	267	8,059	273
Derivative Financial Liabilities				
Foreign exchange forwards				
– cash flow hedges	18	–	593	1
– not qualified for hedge accounting	1	–	–	–
Cross currency swaps				
– fair value hedges	11,258	34	14,480	142
Interest rate swaps				
– fair value hedges	1,000	18	–	–
– cash flow hedges	2,542	24	2,242	49
– not qualified for hedge accounting	100	1	100	–
Others	300	2	–	–
	15,219	79	17,415	192
Total	27,284		25,474	

17 Debtors, Deposits and Payments in Advance

The Group's credit policy in respect of receivables arising from its principal activities are as follows:

- (i) Rentals, advertising and telecommunication service fees are billed monthly with due dates ranging from 7 to 50 days. Tenants of the Group's investment properties and station kiosks are required to pay three months' rental deposit upon the signing of lease agreements.
- (ii) Amounts receivable under interest rate and currency swap agreements with financial institutions are due in accordance with the respective terms of the agreements.
- (iii) Consultancy service incomes are billed monthly and are due within 30 days.
- (iv) Debtors in relation to contracts and capital works entrusted to the Group, subject to any agreed retentions, are due within 21 days upon the certification of work in progress.
- (v) Amounts receivable from property purchasers are due in accordance with terms of respective sale and purchase agreements.

The ageing of debtors is analysed as follows:

<i>in HK\$ million</i>	At 30 June 2008 (Unaudited)	At 31 December 2007 (Audited)
Amounts not yet due	1,507	4,201
Overdue by 30 days	158	172
Overdue by 60 days	9	19
Overdue by 90 days	8	14
Overdue by more than 90 days	71	55
Total debtors	1,753	4,461
Deposits and payments in advance	532	552
Prepaid pension costs	186	154
	2,471	5,167

18 Loan to a Property Developer

Nominal and carrying amounts of the loan to a property developer are stated below:

<i>in HK\$ million</i>	At 30 June 2008 (Unaudited)		At 31 December 2007 (Audited)	
	Nominal amount	Carrying amount	Nominal amount	Carrying amount
Interest-free loan to a property developer	4,000	3,624	4,000	3,532

The loan was provided to the developer of Package 2, Tseung Kwan O Area 86 property development project under the terms of the development agreement. The loan is interest-free and guaranteed by the developer's ultimate holding company and is repayable on completion of the respective phases of the project.

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19 Material Related Party Transactions

The Financial Secretary Incorporated, which holds approximately 76.7% of the Company's issued share capital on trust for the Government of the Hong Kong Special Administrative Region ("Government"), is the majority shareholder of the Company. Transactions between the Group and Government departments, agencies or Government controlled entities, other than those transactions arising in the normal dealings between the Government and the Group, are considered to be related party transactions pursuant to HKAS 24 "Related party disclosures" and are identified separately in this interim financial report.

During the half year ended 30 June 2008, amounts due from/to the Government and other related parties in respect of material related party transactions with the Group are stated below:

<i>in HK\$ million</i>	At 30 June 2008 (Unaudited)	At 31 December 2007 (Audited)
Amounts due from:		
– the Government	49	34
– Housing Authority	22	22
– Airport Authority	1	–
– KCRC	151	261
– non-controlled subsidiaries	9	96
– associates	77	131
	309	544
Amounts due to:		
– the Government	10	–
– KCRC	1,245	975
	1,255	975

The amount due from the Government is related to outstanding receivables and retention, as well as provision for contract claims recoverable from the Government, in connection with infrastructure works entrusted to the Company and West Rail property development. The amount due to the Government is related to civil works on the extended overrun tunnel at Hong Kong Station entrusted to the Government.

The amounts due from the Housing Authority and Airport Authority are related to infrastructure works entrusted to the Company in respect of the Tseung Kwan O Extension Project and SkyPlaza Project respectively.

The amount due from KCRC is related to KCRC's cost sharing of the Rail Merger integration works, payments to the Company in respect of the Outsourcing Agreement and KSL Project Management Agreement as well as reimbursable expenditures of KCRC settled by the Company on KCRC's behalf. The amount due to KCRC is related to mandatory payments and related interest in respect of the East Rail Line/Light Rail/Kowloon Southern Link property development sites as well as the accrued portion of the first fixed annual payment for the service concession assets.

During the period, the following dividends were paid to the Government:

<i>in HK\$ million</i>	Half year ended 30 June 2008	Half year ended 30 June 2007
Cash dividend paid	555	482
Shares allotted in respect of scrip dividends	779	708
	1,334	1,190

19 Material Related Party Transactions (continued)

The detail of major related party transactions entered into by the Group with the Government in prior years which are still relevant for the current year and with KCRC in respect of the Rail Merger were described in the Company's audited accounts for the year ended 31 December 2007.

During the half year ended 30 June 2008, the Group had the following transactions with its non-controlled subsidiary, Octopus Holdings Limited ("OHL"), and associate, London Overground Rail Operations Ltd ("LOROL"):

<i>in HK\$ million</i>	Half year ended 30 June 2008	Half year ended 30 June 2007
OHL		
– Payment to OHL in respect of central clearing services	48	29
– Fees received from OHL in respect of load agency services, card issuance and refund services and management services	12	8
– Full repayment received from OHL on shareholder subordinated loan	86	–
– Dividend distribution by OHL for profits during the years from 2005 to 2007	23	–
LOROL		
– Full repayment received from LOROL on senior debt	23	–
– Receipt from LOROL for recovery of bidding costs on the London Rail Concession	32	–

20 Loans and Other Obligations

A Bonds and Notes Issued and Redeemed

Bonds and notes issued by the Group during the half years ended 30 June 2008 and 2007 comprise:

<i>in HK\$ million</i>	Half year ended 30 June 2008		Half year ended 30 June 2007	
	Principal amount	Net consideration received	Principal amount	Net consideration received
Debt issuance programme notes	1,250	1,250	–	–

The above notes were issued by a subsidiary, MTR Corporation (C.I.) Limited. The notes issued are unconditionally and irrevocably guaranteed by the Company, and are direct, unsecured, unconditional and unsubordinated to other unsecured and unsubordinated obligations of MTR Corporation (C.I.) Limited. The obligations of the Company under the guarantee are direct, unsecured, unconditional and unsubordinated to other unsecured and unsubordinated obligations of the Company. The net proceeds received from the issues were on lent to the Company for general working capital, refinancing or other corporate purposes.

During the half year ended 30 June 2008, the Group redeemed HK\$1,000 million (2007: nil) of its unlisted debt securities and none (2007: nil) of its listed debt securities.

B Short-term Loans

During the half year ended 30 June 2008, the Group drew down a short-term Renminbi loan, amounting to RMB700 million (HK\$796 million), to finance the Shenzhen Metro Line 4 Project.

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20 Loans and Other Obligations (continued)

C Lease Out/Lease Back Transaction

In the Group's lease out/lease back transaction entered into in March 2003, certain debt securities ("Defeasance Securities") are used to defease the future obligations under the lease. As the Group is not able to control these Defeasance Securities and its obligations to pay the lease payments are fully funded by the proceeds of the Defeasance Securities, these lease obligations and Defeasance Securities are not recognised as obligations and assets of the Group. A small portion of these Defeasance Securities are subject to replacement on credit rating downgrades, and as a result of the downgrade of some of these securities, HK\$93.5 million has been charged to the profit and loss account for the half year ended 30 June 2008 in respect of the estimated net cost to the Group of its obligation to replace such securities. There are other Defeasance Securities, currently rated double A and single A by S&P's and Moody's respectively, issued by the same issuer as the above-noted Defeasance Securities, with accreted value of US\$54.0 million as of 30 June 2008, which are not subject to replacement obligation on ratings downgrade.

21 Creditors, Accrued Charges and Provisions

Creditors, accrued charges and provisions are mainly related to capital projects which are settled upon certification of work in progress, swap interest payable and forward sale deposits received in respect of properties for which occupation permits have not been issued. The Group has no significant balances of trade creditors resulting from its provision of transportation services.

Under the development agreement in respect of the Che Kung Temple property development, the Company is obliged to pay 50% of the land premium, amounting to HK\$1.8 billion. This payable has been settled in July 2008.

The analysis of creditors as at 30 June 2008 by due dates is as follows:

<i>in HK\$ million</i>	At 30 June 2008 (Unaudited)	At 31 December 2007 (Audited)
Due within 30 days or on demand	3,026	1,354
Due after 30 days but within 60 days	893	652
Due after 60 days but within 90 days	138	218
Due after 90 days	1,542	1,563
	5,599	3,787
Rental and other refundable deposits	1,395	1,462
Accrued employee benefits	215	163
Total	7,209	5,412

22 Obligations under Service Concession

Obligations under service concession represent the outstanding balance of the discounted total fixed annual payments for the service concession acquired in the Rail Merger.

23 Deferred Tax Assets and Liabilities

A Movements of deferred tax assets and liabilities during the half year ended 30 June 2008 and the year ended 31 December 2007 were as follows:

<i>in HK\$ million</i>	Deferred tax arising from					
	Depreciation allowances in excess of related depreciation	Revaluation of properties	Provision and other temporary differences	Cash flow hedges	Tax losses	Total
30 June 2008 (Unaudited)						
At 1 January 2008	8,809	4,126	215	(5)	(575)	12,570
Effect of decrease in the Hong Kong Profits Tax rate from 17.5% to 16.5%	(503)	(235)	(12)	–	32	(718)
Charged/(credited) to profit and loss account	(47)	343	4	–	406	706
Charged to reserves (note 25)	–	9	–	7	–	16
At 30 June 2008	8,259	4,243	207	2	(137)	12,574
31 December 2007 (Audited)						
At 1 January 2007	8,749	2,681	205	(2)	(2,181)	9,452
Addition through subsidiary acquisition	–	–	–	–	(2)	(2)
Charged to profit and loss account	60	1,402	10	–	1,608	3,080
Charged/(credited) to reserves (note 25)	–	43	–	(3)	–	40
At 31 December 2007	8,809	4,126	215	(5)	(575)	12,570

B Deferred tax assets and liabilities recognised amount to:

<i>in HK\$ million</i>	At 30 June 2008 (Unaudited)	At 31 December 2007 (Audited)
Net deferred tax assets recognised in the balance sheet	(4)	(4)
Net deferred tax liabilities recognised in the balance sheet	12,578	12,574
	12,574	12,570

24 Share Capital, Share Premium and Capital Reserve

<i>in HK\$ million</i>	At 30 June 2008 (Unaudited)	At 31 December 2007 (Audited)
Authorised:		
6,500,000,000 shares of HK\$1.00 each	6,500	6,500
Issued and fully paid:		
5,644,905,489 shares (2007: 5,611,057,035 shares) of HK\$1.00 each	5,645	5,611
Share premium	7,886	7,029
Capital reserve	27,188	27,188
	40,719	39,828

Notes to the Unaudited Interim Financial Report

24 Share Capital, Share Premium and Capital Reserve (continued)

A Pursuant to the Articles of Association of the Company, the capital reserve can only be applied in paying up in full unissued shares to be allotted and distributed as fully paid bonus shares to the shareholders of the Company.

Share premium represents the amount by which the issue price of shares exceeds the par value of those shares. The application of the share premium account is governed by section 48B of the Hong Kong Companies Ordinance.

B New shares issued and fully paid up during the period comprise:

	Number of shares	Option/ scrip price HK\$	Proceeds credited to		
			Share capital account HK\$ million	Share premium account HK\$ million	Total HK\$ million
Employee share options exercised					
– Pre-Global Offering Share Option Scheme	1,283,000	8.440	1	10	11
– New Joiners Share Option Scheme	31,500	15.450	–	–	–
	45,000	15.970	–	1	1
	31,500	18.300	–	1	1
	355,500	19.404	1	6	7
	30,000	20.660	–	1	1
Issued as 2007 final scrip dividends	32,071,954	27.070	32	836	868
	33,848,454		34	855	889

C Key details of the Company's share option schemes are summarised as follows:

	Half year ended 30 June 2008			Half year ended 30 June 2007		
	Pre-Global Offering Share Option Scheme	New Joiners Share Option Scheme	2007 Share Option Scheme	Pre-Global Offering Share Option Scheme	New Joiners Share Option Scheme	2007 Share Option Scheme
No. of previously vested share options exercised during the period	1,283,000	493,500	–	711,000	31,000	–
No. of share options granted during the period	–	–	3,054,000	–	1,066,000	–
No. of share options lapsed during the period	17,000	93,500	65,000	–	–	–
No. of share options vested during the period	–	649,500	–	–	325,500	–
No. of share options outstanding as at 30 June	3,967,000	3,130,700	10,957,000	7,118,500	3,815,700	–

Details of the movements in respect of these share option schemes are set out under the Corporate Governance and Other Information section on page 19.

24 Share Capital, Share Premium and Capital Reserve (continued)

D During the half year ended 30 June 2008, the following share options were granted under the 2007 Share Option Scheme:

Date of grant	Number of share options	Exercise price HK\$	Exercisable period
02 January 2008	75,000	27.60	on or prior to 10 December 2014
03 January 2008	40,000	27.60	on or prior to 10 December 2014
04 January 2008	65,000	27.60	on or prior to 10 December 2014
07 January 2008	125,000	27.60	on or prior to 10 December 2014
28 March 2008	255,000	26.52	on or prior to 26 March 2015
31 March 2008	379,000	26.52	on or prior to 26 March 2015
01 April 2008	261,000	26.52	on or prior to 26 March 2015
02 April 2008	296,000	26.52	on or prior to 26 March 2015
03 April 2008	171,000	26.52	on or prior to 26 March 2015
04 April 2008	23,000	26.52	on or prior to 26 March 2015
05 April 2008	17,000	26.52	on or prior to 26 March 2015
07 April 2008	390,000	26.52	on or prior to 26 March 2015
08 April 2008	174,000	26.52	on or prior to 26 March 2015
09 April 2008	85,000	26.52	on or prior to 26 March 2015
10 April 2008	58,000	26.52	on or prior to 26 March 2015
11 April 2008	134,000	26.52	on or prior to 26 March 2015
12 April 2008	48,000	26.52	on or prior to 26 March 2015
14 April 2008	40,000	26.52	on or prior to 26 March 2015
15 April 2008	34,000	26.52	on or prior to 26 March 2015
16 April 2008	57,000	26.52	on or prior to 26 March 2015
17 April 2008	147,000	26.52	on or prior to 26 March 2015
18 April 2008	32,000	26.52	on or prior to 26 March 2015
19 April 2008	25,000	26.52	on or prior to 26 March 2015
20 April 2008	23,000	26.52	on or prior to 26 March 2015
21 April 2008	66,000	26.52	on or prior to 26 March 2015
23 April 2008	34,000	26.52	on or prior to 26 March 2015

25 Other Reserves

in HK\$ million	Attributable to equity shareholders of the Company					
	Fixed asset revaluation reserve	Hedging reserve	Employee share-based capital reserve	Exchange reserve	Retained profits	Total
30 June 2008 (Unaudited)						
Balance as at 1 January 2008	1,170	(25)	7	42	49,992	51,186
Cash flow hedges:						
Effective portion of changes in fair value, net of deferred tax	-	28	-	-	-	28
Transfer from equity						
– to profit and loss account	-	19	-	-	-	19
– to initial carrying amount of non-financial hedged items	-	(12)	-	-	-	(12)
– to deferred tax	-	(1)	-	-	-	(1)
2007 final dividend	-	-	-	-	(1,740)	(1,740)
Surplus on revaluation, net of deferred tax (note 23)	86	-	-	-	-	86
Release of revaluation reserve on disposal, net of deferred tax (note 23)	(35)	-	-	-	42	7
Effect of decrease in the Hong Kong Profits Tax rate from 17.5% to 16.5%	14	-	-	-	-	14
Employee share-based payments	-	-	9	-	-	9
Release to share premium upon share options exercised	-	-	(2)	-	-	(2)
Exchange difference on translation of accounts of overseas subsidiaries	-	-	-	27	-	27
Profit for the period	-	-	-	-	4,689	4,689
Balance as at 30 June 2008	1,235	9	14	69	52,983	54,310
31 December 2007 (Audited)						
Balance as at 1 January 2007	968	(10)	5	17	37,148	38,128
Cash flow hedges:						
Effective portion of changes in fair value, net of deferred tax	-	(13)	-	-	-	(13)
Transfer from equity						
– to profit and loss account	-	-	-	-	-	-
– to initial carrying amount of non-financial hedged items	-	(2)	-	-	-	(2)
– to deferred tax	-	-	-	-	-	-
2006 final dividend	-	-	-	-	(1,554)	(1,554)
2007 interim dividend	-	-	-	-	(782)	(782)
Surplus on revaluation, net of deferred tax (note 23)	202	-	-	-	-	202
Employee share-based payments	-	-	2	-	-	2
Exchange difference on translation of accounts of overseas subsidiaries	-	-	-	25	-	25
Profit for the year	-	-	-	-	15,180	15,180
Balance as at 31 December 2007	1,170	(25)	7	42	49,992	51,186

Apart from retained profits, the other reserves are not available for distribution to shareholders because they do not constitute realised profits. In addition, the Company considers the cumulative surpluses on revaluation of investment properties, net of tax of HK\$20,216 million (31 December 2007: HK\$18,280 million) included in retained profits are non-distributable as they also do not constitute realised profits. As at 30 June 2008, the Company considered that the total amount of reserves available for distribution to equity shareholders amounted to HK\$31,993 million (31 December 2007: HK\$31,069 million).

26 Capital Commitments

A Outstanding capital commitments as at 30 June 2008 not provided for in the accounts are as follows:

<i>in HK\$ million</i>	Railway operations	Railway extension projects	Property projects and management	Overseas project	Total
At 30 June 2008 (Unaudited)					
Authorised but not yet contracted for	1,195	–	76	–	1,271
Authorised and contracted for	842	226	302	1,155	2,525
	2,037	226	378	1,155	3,796
At 31 December 2007 (Audited)					
Authorised but not yet contracted for	916	–	72	–	988
Authorised and contracted for	547	152	377	633	1,709
	1,463	152	449	633	2,697

Included in the amounts authorised but not yet contracted for are costs that will not be subject to capital contracts such as staff costs, overhead expenses and capitalised interest.

B The commitments under railway operations comprise the following:

<i>in HK\$ million</i>	Improvement and enhancement works	Acquisition of property, plant and equipment	Additional concession property	Total
At 30 June 2008 (Unaudited)				
Authorised but not yet contracted for	943	6	246	1,195
Authorised and contracted for	543	1	298	842
	1,486	7	544	2,037
At 31 December 2007 (Audited)				
Authorised but not yet contracted for	854	11	51	916
Authorised and contracted for	342	9	196	547
	1,196	20	247	1,463

C Investments in Mainland of China

Beijing MTR Corporation Limited, the public-private partnership company (“PPP”) between the Group, Beijing Infrastructure Investment Co., Ltd and Beijing Capital Group for the Beijing Metro Line 4 Project has obtained its business license in January 2006 and the Concession agreement with the Beijing Municipal People’s Government was signed in April 2006. Electrical and mechanical equipment manufacturing, including rolling stock and site installation, are in progress as scheduled. The PPP has a registered capital of RMB1,380 million of which 49% (about RMB676 million) would be contributed by the Group. In May 2008, the Group injected its last tranche of equity of RMB471 million (HK\$515 million). The total equity contribution made by the Group was RMB676 million (HK\$718 million), representing 100% of the Group’s committed share. As at 30 June 2008, the PPP had outstanding contract commitments totalling approximately RMB2.2 billion (HK\$2.5 billion) related to the project (2007: HK\$2.5 billion).

In 2005, the Group and the Shenzhen Municipal People’s Government initialed the project Concession Agreement to build Phase 2 of Shenzhen Metro Line 4 and to operate both Phase 1 and 2 of Shenzhen Metro Line 4 for a period of 30 years. The project is awaiting the approval from the Central Government. Preparatory work including design and tendering and expanded trial section is in progress. Under the Agreement in Principle and the approval document issued by the Shenzhen Development and Reform Bureau, there are certain buy-back arrangements with Shenzhen Government in the project related costs incurred by the Group should the project not be approved by the Central Government. Total investment of the project is estimated at RMB6.0 billion (HK\$6.8 billion) which will be financed by equity capital contributed by the Group of RMB2.4 billion (HK\$2.7 billion) and the balance by non-recourse bank loans in Renminbi.

27 Approval of Interim Financial Report

The interim financial report was approved by the Board on 5 August 2008.