A. MEMORANDUM OF UNDERSTANDING

Further to the Company’s announcements dated 24th February, 2004, 20th August, 2004, 16th September, 2004 and 9th April, 2006, the Company is pleased to confirm that the Company and Government have entered into a Confidential Memorandum of Understanding in relation to the Rail Merger with the Government of the People’s Republic of China (the “Government”). The Company and Government have confirmed that the Memorandum of Understanding (the “Confidential Memorandum of Understanding”) was signed on 24th February, 2006.

1. BACKGROUND

The Company confirms that, following the signing of the Confidential Memorandum of Understanding, discussions between the Company and Government have continued and have been broadened to include matters relating to the future operations and management of the MTR System. The Company and the Government have confirmed that the Confidential Memorandum of Understanding will be replaced by a more comprehensive document that will contain more detailed provisions relating to the future operations and management of the MTR System.

2. THE RAIL MERGER

The Company and Government have agreed that the Rail Merger would be unconditional and terms of the Rail Merger are set out below. However, if the Rail Merger is implemented, there will be an amendment to be implemented in accordance with the terms and conditions set out below.

3. PAYMENTS TO THE COMPANY

In accordance with the terms of the Confidential Memorandum of Understanding, the Company shall make the following payments to the Company:

4. ASSET TRANSFERS

The Company and Government have agreed that the Rail Merger would be unconditional and terms of the Rail Merger are set out below. However, if the Rail Merger is implemented, there will be an amendment to be implemented in accordance with the terms and conditions set out below.

5. CORPORATE GOVERNANCE

The Company and Government have agreed that the Rail Merger would be unconditional and terms of the Rail Merger are set out below. However, if the Rail Merger is implemented, there will be an amendment to be implemented in accordance with the terms and conditions set out below.

6. WORKING CAPITAL

The Company and Government have agreed that the Rail Merger would be unconditional and terms of the Rail Merger are set out below. However, if the Rail Merger is implemented, there will be an amendment to be implemented in accordance with the terms and conditions set out below.

7. CONCLUSION

The Company and Government have agreed that the Rail Merger would be unconditional and terms of the Rail Merger are set out below. However, if the Rail Merger is implemented, there will be an amendment to be implemented in accordance with the terms and conditions set out below.
If the discussions between the Company, Government and KCRC are successful, it is expected that the following steps will be taken:

1. Liaison committees will be established, consisting of members from Government, the Company and KCRC, which shall discuss material decisions to be taken by KCRC and the Company.

2. A Service Concession Agreement to document the terms of the Service Concession.

3. The Sale and Purchase Agreement to document the terms and conditions of the sale to MergeCo of the Purchased Rail Assets (or any part thereof).

4. The Merging Agreement to document the terms of the merger of the operations of the Company and KCRC, to be more particularly defined in the definitive transaction documents.

In accordance with the Listing Rules, the independent board committee established by the Company (consisting only of independent non-executive directors) will consider, in accordance with the Code on Takeovers and Mergers, the terms of the Sale and Purchase Agreement and the Merging Agreement, and will provide advice to the Board of Directors on the Company's position in relation to the material terms of the proposed transaction.

This announcement is made in English and Chinese. In the case of any inconsistency, the English version shall prevail.