

This Summary Financial Report 2004 only gives a summary of the information and particulars of MTR's 2004 Annual Report from which this Summary Financial Report is derived. Both documents are available (in both English and Chinese versions) in electronic form on the Company's website at www.mtr.com.hk

You may obtain a printed copy of the 2004 Annual Report free of charge by writing to the Company's share registrar, Computershare Hong Kong Investor Services Limited, or our Corporate Relations Department. Their details are set out on page 32 of this Summary Financial Report.

Summary financial report 2004



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Vision

To be a world class enterprise, growing in Hong Kong and beyond, focusing on rail, property and related businesses

Mission

- > Provide excellent value to our Customers, enhancing their quality of life, and contributing to development of the communities in which we operate
- > Provide opportunities for employees to grow and prosper with the Company and reward our investors
- > Develop the rail network as the backbone of public transport in Hong Kong
- > Grow in Mainland China and capture opportunities in Europe by building on our core competencies

Onwards, Upwards and Outwards

MTR is always on the move

- > to new ways of thinking and delivering our services
- > to higher levels of operational and financial performance
- > to a world of business opportunities at home and abroad

You may at any time choose to receive summary financial reports or annual reports in printed form or to rely on their versions posted on the Company's website. You may also at any time choose to receive (a) summary financial reports or annual reports in place of the other and (b) the English version only, the Chinese version only or both the English and the Chinese versions of the Company's summary financial reports or annual reports. You may make the above choices notwithstanding any wish to the contrary has previously been conveyed to the Company. You may change your choice on these matters by writing to the Company's share registrar, Computershare Hong Kong Investor Services Limited, whose details are set out on page 32.

If you have already chosen to rely on the versions of the summary financial reports and annual reports posted on the Company's website or have difficulty in having access to those documents, you will, promptly upon written request, be sent those documents in printed form free of charge. Please send your request to the Company's share registrar, Computershare Hong Kong Investor Services Limited.

Key figures

Financial highlights <i>in HK\$ million</i>	2004	2003	% Increase/(Decrease)
Revenue			
– Fare	5,932	5,489	8.1
– Non-fare	2,419	2,105	14.9
Operating profit from railway and related operations before depreciation	4,546	3,747	21.3
Profit on property developments	4,568	5,369	(14.9)
Operating profit before depreciation	9,114	9,116	(0.0)
Profit attributable to shareholders	4,496	4,450	1.0
Total assets	106,674	102,366	4.2
Loans, obligations under finance leases and bank overdrafts	30,378	32,025	(5.1)
Shareholders' funds	63,499	57,292	10.8
Financial ratios <i>in %</i>			
Operating margin	54.4	49.3	5.1% pt.
Gross debt-to-equity ratio	47.8	55.9	(8.1)% pt.
Return on average shareholders' funds	7.4	8.0	(0.6)% pt.
Interest cover <i>in times</i>	6.1	5.6	8.9
Share information			
Basic earnings per share <i>in HK\$</i>	0.84	0.85	(1.2)
Dividend per share <i>in HK\$</i>	0.42	0.42	–
Share price as at 31 December <i>in HK\$</i>	12.45	10.25	21.5
Market capitalisation as at 31 December <i>in HK\$ million</i>	67,105	54,209	23.8
Operations highlights			
Total passenger boardings			
– MTR Lines <i>in millions</i>	833.6	770.4	8.2
– Airport Express Line <i>in thousands</i>	8,015	6,849	17.0
Average number of passengers <i>in thousands</i>			
– MTR Lines <i>weekday</i>	2,403	2,240	7.3
– Airport Express Line <i>daily</i>	21.8	18.7	16.6
Fare revenue per passenger <i>in HK\$</i>			
– MTR Lines	6.50	6.57	(1.1)
– Airport Express Line	64.25	62.07	3.5
Proportion of franchised public transport boardings <i>in %</i>			
– All movements	24.8	24.3	0.5% pt.
– Cross-harbour movement	59.6	58.7	0.9% pt.
Proportion of transport boardings travelling to/from the airport <i>in %</i>			
– Airport Express Line	21	23	(2)% pt.

Chairman's letter

Dear Stakeholders,

I am pleased to present to you the results of MTR Corporation Limited (MTR) for 2004, the 25th Anniversary of commencement of MTR's rail services in Hong Kong.

The 2004 results reflect a heartening turnaround from the SARS buffeted 2003. Our satisfactory performance was underpinned by a broad based economic recovery, driven by tourism, positive consumer sentiment, waning deflationary pressure and steadily improving property prices. During the year, the Company recorded total turnover of HK\$8,351 million, an increase of 10.0% over the previous year, with net profit rising by 1.0% to HK\$4,496 million. Net profit in 2003 included a large book profit recorded on receipt of 18 floors in Two IFC.

In February, the Government requested the Company and the Kowloon-Canton Railway Corporation (KCRC) to begin merger discussions. As I indicated in my letter to you in the 2004 Interim Report, we worked hand in hand with KCRC to move matters forward. Thanks to the cooperative and mutually supportive manner in which discussions took place, we jointly submitted to the Government in September a merger proposal. The proposal addresses positively the five parameters laid down by the Government whilst providing a blueprint for integrating the two railway operations to create a single, world-class railway network for Hong Kong.

Those five parameters are: an objective and transparent fare adjustment mechanism; abolition of transfer charges; fare reduction; job security for frontline staff; and provision of seamless interchange.

Upon submission of the joint proposal, the Company began negotiations with the Government on the terms of the possible merger, which has continued into the New Year. MTR believes that deal terms can be reached that would benefit all stakeholders, including customers, the Government, shareholders and staff of both MTR and KCRC. A well executed merger would create a world leading mass transit cum property development enterprise, providing greater convenience, better connectivity, higher operational and financial efficiency and compelling international competitiveness.

In 2004, we took significant steps forward in implementing the Company's expansion strategy outside Hong Kong. In January, MTR signed an Agreement in Principle with the Shenzhen Municipal People's Government to construct Phase 2 of Line 4 in the Shenzhen Metro System and to operate the whole line for a period of 30 years following completion of Phase 2. The project will also include property development rights of an aggregate gross floor area of 2.9 million square metres at stations and the depot along Line 4. Negotiations on the Concession Agreement and related agreements with the Shenzhen authorities are progressing, albeit at a slower pace than originally anticipated, due to the measures implemented by the Central Government to dampen overheating aggregate demand.

In December, the Company signed an Agreement in Principle with Beijing Infrastructure Investment Co. Ltd. and Beijing Capital Group, both subsidiaries of the Beijing Municipal People's Government, to form a Public-Private-Partnership (PPP) for the



investment, construction and operation of the Beijing Metro Line 4 project for a period of 30 years. MTR will own 49% of the PPP company which will be responsible for providing the electrical and mechanical systems including trains, and for running the line upon completion of the project. Based on this PPP model, land acquisition and civil construction of the project will be financed by the Beijing Municipal People's Government. In February 2005, together with our partners, we initialled the Concession Agreement for the franchise with the Beijing Municipal People's Government and the related agreements, and now await approval from the National Development and Reform Commission.

We are encouraged by business opportunities in Europe, particularly the UK, where we are pursuing operating franchise contracts. In November, we signed a joint-venture agreement with the Great North Eastern Railway Holdings Limited to bid for the Integrated Kent Franchise in southeast England. We are eyeing a similar opportunity in Thameslink / Great Northern Franchise, which serves London north and south of the River Thames.

Our offshore expansion strategy complements the Company's continuing interest in extending the MTR network in Hong Kong. The Disneyland Resort Line and the Tung Chung Cable Car projects are on track whilst we are engaged in earnest discussion with the Government on proposed projects such as the West Island Line (WIL) and South Island Line (SIL).

The wider responsibilities of MTR to our stakeholders and society were high on our agenda in 2004. Full details of the Company's achievements in this area are given in our Sustainability Report, which adheres to Global Reporting Initiative (GRI) guidelines. The Report was included in the GRI's top 100 reports and named Best Sustainability Report

by the Association of Chartered Certified Accountants (ACCA). In addition, in late 2004 we began the development of a new Enterprise-Wide Risk Management System to help better monitor and track risks and best practices across our businesses. We also enhanced and strengthened our processes to engage community stakeholders through extensive consultations on the proposed WIL and SIL, and by establishing a Sustainability Advisory Board for the Tung Chung Cable Car project. The Company continued to apply our tried and true rail plus socially responsible property development business model, codes of conduct, training and best governance practices to our projects abroad and actively supported international initiatives to enhance enterprise sustainability.

MTR persistently maintains a high standard of corporate governance and financial disclosure. We were once again recognised by the Hong Kong Management Association (HKMA), which gave us the Silver Award in the General Category in the 2004 Best Annual Report Awards Competition. This marks the sixteenth consecutive year of award winning for MTR.

Community service is part of MTR's fabric. Two ongoing programmes are noteworthy, namely, "Art in Station" which sponsors local artists and students to display and perform art in our stations, and promotion of healthy living. The latter, which, among other things, encourages walking as a form of daily exercise, will be highlighted by an Annual Race Walking event beginning in 2005.

Although Hong Kong was not directly affected, we were all touched by the human sufferings and tragedies that followed in the wake of the Indian Ocean Tsunami. MTR, by working with our employees, passengers, commercial tenants and affiliates, accounted for over HK\$2 million of relief funds raised to date. We are deeply grateful to all those who have cooperated with us in this humanitarian endeavour.

Finally, I would like to thank my Board colleagues, management and all staff for their smart conscientious work, dedication and focus on excellence, which contributed to the successes of our 25th Anniversary Year. As MTR drives into the future, I am confident we can build on our strong quarter century legacy and continue being caring, innovative, visionary and profitable.



Dr. Raymond Ch'ien Kuo-fung, *Chairman*
Hong Kong, 1 March 2005

CEO's review of operations and outlook

Dear Stakeholders,

I am pleased to report that MTR's operational results for the year 2004 experienced a dramatic rebound over 2003, a year when our operations were severely impacted by the weak economy, soft property prices and, most significantly, the outbreak of SARS.

The strong operational results achieved in 2004 were brought about by a broad based economic recovery in Hong Kong which also led to a significant increase in property prices. The Company has managed this recovery well. Growth in patronage led to significant fare revenue increases. Growth in non-fare revenues was even stronger propelled by buoyant station businesses and improved rental rates for our investment properties. Property development profit also exceeded our earlier expectation, albeit lower than the very high property development profit recognised in 2003 on receipt of our 18 floors in Two IFC.

The Company's favourable performance produced good financial results in 2004. MTR recorded total revenues of HK\$8,351 million, an increase of 10.0% over the previous year while operating profit before property development,

interest and depreciation improved by 21.3% to HK\$4,546 million. With property development profit of HK\$4,568 million recognised for the year, a reduction of HK\$801 million from 2003, net profit improved marginally by 1.0% to HK\$4,496 million. However, earnings per share decreased slightly by 1.2% to HK\$0.84 as more shares were issued during the year. The Board recommended a final dividend of HK\$0.28 which together with the interim dividend of HK\$0.14 brought the full year dividend to HK\$0.42, same as last year.

Review of operations

After a sharp rebound in patronage from SARS in the second half of 2003 passenger growth continued through 2004 assisted by the economic recovery in Hong Kong, increase in tourist arrivals from the Mainland, and the opening of our West Rail interchanges in December 2003. In all, total patronage for the MTR Lines increased significantly by 8.2% to 834 million. Airport Express (AEL) also saw a strong recovery, with total patronage rising 17% to reach 8.0 million, following an increase in air passenger traffic at the Hong Kong International Airport.

Our market share also improved with our overall share of total franchised public transport rising to 24.8% from 24.3% in 2003, while our cross-harbour market share increased to 59.6% from 58.7%. The Company's estimated market share of passengers travelling to and from the airport decreased from 23% to 21%, partly due to a change in the mix of visitors arriving and departing from Hong Kong airport.

The increases in patronage and market share were supported by the continuing high quality of service. In 2004, our customer service performance continued to surpass both the Government's requirement under the Operating Agreement and our own more stringent Customer Service Pledges. In fact, during the year, statistics measuring MTR performance were among the best on record at MTR. The number of journeys experiencing a delay of five minutes or more showed a 25% improvement over 2003. MTR passenger journeys on time were 99.9%, supported by 99.9% reliability for train service delivery, which were amongst the best in the world. In January, MTR employees won extensive praise



for their rapid and effective response to an arson attack on an Urban Line train, by resolving the incident quickly, thus preventing injury to our passengers and employees, and allowing us to resume normal service swiftly.

Regrettably, a number of noticeable incidents in the latter part of the year had given rise to public concerns over the reliability of our system. Based on the principle of continuous improvement and to address passenger concerns, the Company set up a high-level internal task force to seek operational improvements and commissioned an independent study by Lloyd's Register Rail, a leading international rail expert and validation agency, to conduct a comprehensive review on our asset conditions and asset management practices.

Following the conclusion of the internal task force investigation in November, we have begun implementation of a series of improvement initiatives to augment our maintenance regime and incident handling procedures. The Lloyd's Register Rail report was received in early February 2005. The report's recommendations are constructive and useful. We will study the report in detail and will set up the necessary organisations and processes to implement the recommendations expeditiously whilst at the same time taking immediate actions to address some of its recommendations. We are encouraged to note that the report did not find any evidence to suggest MTR assets are declining as the system enters its 25th year of operation and our asset management system is recognised to be in line with international best practice. Nevertheless, both the Board and management are committed to ensuring that the Lloyd's Register Rail recommendations are effectively implemented to ensure that the people of Hong Kong continue to enjoy a safe, reliable and efficient mass transit service that they can be proud of.

MTR continued to seek improvements in efficiency and productivity through various initiatives. As a result, our railway operating costs per car km during the year fell by 1.8% to HK\$22.1.

Our station commercial and other revenues benefited significantly from the economic recovery and strong rebound in consumer spending, growing by 17.4% to HK\$1,311 million. The substantial increases in advertising and telecommunication income were particularly noteworthy. Our strategy to

upgrade advertising facilities and introduce new formats, such as the trackside plasma TV network introduced during the year, has proved most effective and continued to boost advertising revenues by 21%. The station renovation programme to add more space, vibrancy and a better trade mix to MTR stations also helped improve station commercial revenues.

In telecommunications, MTR became one of the first rail networks in the world to be 3G enabled as we successfully upgraded our existing integrated radio system on the Island Line to support UMTS based 3G service. Our fixed-line subsidiary TraxComm began operation and management of a 50 Gigabit bandwidth network, serving a number of telecom service operators in Hong Kong.

With the economic recovery, further increases in the number of service providers and a rise in average daily usage of the Octopus card, pre-tax profit contribution from Octopus Cards Limited increased significantly by 91.3% over 2003 to HK\$44 million.

MTR has for some time been active overseas in external consultancy and this work currently extends to contracts in 22 cities in 11 countries. During 2004 we made the strategic decision to reorient this business to refocus on service contracts which are larger and of longer duration, and which are likely to lead to investment opportunities. This refocus has already led to an improvement of consultancy profit.

On future Hong Kong projects, we made significant progress on the construction of Disneyland Resort Line (DRL), formerly known as the Penny's Bay Rail Link, which will connect Hong Kong Disneyland with the Tung Chung Line, and are confident of meeting the target completion date of 1 July 2005. The Tung Chung Cable Car project, our major new tourist attraction project for Hong Kong, is also on track for completion by early 2006, following the start of construction work in February 2004.

In February, we put forward our proposal to the Government to extend the Kwun Tong Line from Yau Ma Tei Station to the popular residential area of Whampoa Garden. In March, following extensive consultations and much hard work, the Company submitted revised proposals on WIL and SIL to the Government. All of these proposals are currently under review by the Government.

With a buoyant property market in 2004, MTR achieved highly satisfactory results in our property businesses, as more developments were completed and sold. Together with our property developers, we launched and achieved very strong sales in developments at The Harbourside, Carmel Cove of Caribbean Coast and 8 Clearwater Bay Road as well as achieving good results from developments previously launched for sale such as Coastal Skyline, Monterey Cove and Albany Cove of Caribbean Coast, and Residence Oasis. We and our property developers sold or pre-sold 3,554 units in 2004. As a result, profit from property development was HK\$4,568 million. The main contributions to property development profit came from sharing in kind in respect of the Union Square retail shell structure at Kowloon Station, recognition of deferred income relating to the Caribbean Coast and Coastal Skyline developments at Tung Chung Station and The Harbourside at Kowloon Station, and share of surplus proceeds from Residence Oasis at Hang Hau Station in Tseung Kwan O and The Harbourside at Kowloon Station. However, this high level of property development profit was, as forecasted, lower than that achieved in 2003 which was favourably impacted by the receipt of 18 floors in Two IFC.

In Tseung Kwan O, following approval in August 2004 for a substantial improvement to the Master Layout Plan for the "Dream City" at Area 86, developers were invited to tender for Package One of Area 86 in December which was ultimately awarded to City Investments Limited, a subsidiary of Cheung Kong (Holdings) Limited in January 2005. This was our first development tender since October 2002. The tender invitation differed from our previous format as we offered to pay half of the land premium in return for a higher profit sharing ratio. This method allows us to increase our profit participation in the development, albeit at slightly increased risk, whilst attracting a number of large and medium sized developers to the tender. Elsewhere in Tseung Kwan O, Occupation Permit was issued for the 2,130-unit Residence Oasis at Hang Hau Station in December allowing us to record profit from this development earlier than we had originally anticipated.

Property rental and management income increased by 12.1% to HK\$1,108 million. This was mainly the result of higher rental income from Two IFC arising from a faster than expected commitment by tenants at higher

rents, together with strong performance in all four shopping centres and an expanded portfolio of managed properties.

Another notable achievement by the Company during the year was the launch of our revised Vision, Mission and Core Values. These are built on the statements of strategic intent and values that will now guide us into the future as the Company continues to grow our business in Hong Kong and beyond.

Financial performance

The financial results for 2004 reflected an all round improvement in every aspect of our businesses. Total fare revenue for the MTR Lines amounted to HK\$5,417 million, a 7.0% increase over 2003, while that from AEL increased by 21.2% to HK\$515 million. Taking into account non-fare revenue including property rental and management income which in total rose 14.9% to HK\$2,419 million, total revenue grew by 10.0% to HK\$8,351 million.

Despite a general increase in business activities during 2004, operating expenses were well contained with gains in productivity. This, together with the write-back of prior year revaluation deficit for our self-occupied office property, has led to operating expenses before depreciation reducing by 1.1% to HK\$3,805 million. Consequently, operating margin for the year improved significantly to 54.4% compared with 49.3% in 2003. Profit from property development was HK\$4,568 million, a reduction of HK\$801 million from the very significant property development profit recorded in 2003 when MTR received our 18 floors in Two IFC. Depreciation charges increased by 4.6% to HK\$2,512 million from HK\$2,402 million in 2003, mainly due to a full year's depreciation on the West Rail Interchange and on new railway assets. Net interest expenses decreased by 5.8% to HK\$1,450 million mainly as a result of lower borrowing costs. The Company's share of Octopus Cards Limited's pre-tax earnings was HK\$44 million for the year. After deducting income tax expenses of HK\$700 million, the Group's profit attributable to shareholders for the year was HK\$4,496 million, a slight increase of 1.0% over 2003.

In January, the Group took advantage of the favourable market and successfully launched a 10-year US\$600 million fixed rate bond. The transaction not only enabled us to obtain

cost-effective fixed-rate long-term funds and to further extend our debt maturity profile, but also established a new 10-year US dollar benchmark for Hong Kong's quasi-sovereign credits. As a result of the attractive terms of our new financings and low interest rates prevailing during the year, we were able to further reduce our average borrowing cost to 4.7% from 5.1% in 2003.

Growth beyond Hong Kong

In the annual report last year, I discussed our strategy of seeking growth outside Hong Kong. While Hong Kong will firmly remain our home market, we shall use our core capability as a world class rail operator and property developer to capture business opportunities outside of Hong Kong with the objective to create value for our shareholders as well as development opportunities for our staff.

Whilst we see tremendous growth opportunities overseas, particularly in the Mainland of China and Europe, we are mindful of the associated business and financial risks as well as our responsibility to create value for our shareholders. As such, when evaluating and deciding on these investment opportunities we will be guided by prudent commercial principles that aim to deliver an appropriate risk-adjusted return.

In the Mainland of China, our investment strategy is focused on the major cities where the demand for mass rapid transit systems and hence potential for profit is the greatest due to expanding populations, heightened environmental concerns and increasing traffic congestions. We shall also adopt various business models to meet the different market needs. In some cases, we can repeat the very successful "rail and property model" as used in Hong Kong, whilst in other cities we may choose a PPP model where Government funds most of the capital expenditure.

As reported last year, in January 2004 we signed an Agreement in Principle with the Shenzhen Municipal People's Government to build, operate and transfer Phase 2 of Line 4 of the Shenzhen Metro System, and to operate the entire line for 30 years when Phase 2 is completed. The total investment in this project is approximately RMB 6 billion (HK\$5.7 billion). The project will be implemented based on the "rail and property model", with associated property developments of 2.9 million square metres of commercial and residential space along the railway.

Since signing the Agreement in Principle, we have begun preliminary project design and construction works as well as negotiations with the Shenzhen Municipal People's Government on a Concession Agreement and other related agreements which would give MTR, through our project company, the right to construct Phase 2 and to operate the entire Line 4. However, given the current economic climate in China, it is possible that the necessary government approvals, including that from the Central Government, may take longer than originally anticipated.

In December we signed a separate Agreement in Principle to form a PPP with Beijing Infrastructure Investment Co. Ltd. (BIIC) and Beijing Capital Group (BCG), both subsidiaries of the Beijing Municipal People's Government, for the investment, construction and operation of the Beijing Metro Line 4 for a period of 30 years. The total investment for this project is estimated at RMB 15.3 billion (HK\$14.4 billion). Based on the PPP framework, the Beijing Municipal People's Government will fund 70% of total project cost comprising mainly land acquisition and civil construction with the remaining 30% funded by the PPP company. This 30% will mainly consist of provision of trains and related electrical and mechanical systems, costing approximately RMB 5 billion (HK\$4.7 billion) over 60% of which would be financed by non-recourse RMB debt. The balance will be funded by equity contribution from the PPP partners of which MTR will own 49% with BIIC and BCG owning respectively 2% and 49%. Hence our equity contribution to this project is estimated to be RMB 735 million (HK\$693 million). In February 2005, this project took another step forward when MTR and its partners together with the Beijing Municipal People's Government initialled the 30-year Concession Agreement, which will become effective when approval from the National Development and Reform Commission is obtained.

In addition to these two major investment opportunities, the Company is in active discussions with parties concerning other projects in Beijing, Shenzhen and Shanghai.

In contrast to Mainland China, our expansion strategy in Europe can be characterised as "asset light". We will seek to enter into joint-venture partnership with experienced local firms to bid for operation and maintenance franchises and contracts, as deregulation of

railway industries in Europe continues to unfold. Our initial focus will be on the highly deregulated UK market.

In November, the Company signed a joint-venture agreement with the UK's Great North Eastern Railway Holdings Limited to jointly bid for the Integrated Kent Franchise in southeast England and since December we have been working to pursue a similar opportunity in Thameslink / Great Northern Franchise, which serves London north and south of the River Thames. Although we believe that our two consortia have competitive advantages in their respective bids, as with all tenders there is no certainty that either consortium will be successful.

Possible merger between MTR and KCRC

During the year, we worked hard in close co-operation with KCRC on the merger discussions. As a result, we were able to complete and present our joint merger proposal to the Government in September. This joint proposal, which we believe properly addresses the five parameters set out by the Government when it invited the two corporations to begin merger discussions, is currently under review by the Government. At the same time, the Company has started discussion with the Government on terms of the possible merger. Our stance on the merger has always been that if properly structured and on acceptable terms, the merger benefits all our stakeholders.

People

MTR's performance is the achievement of our people. It is their dedication and professionalism that took us through the difficult year of 2003 and the challenges in the eventful but rewarding 2004.

During the year, we continued to work hand in hand with our people, creating opportunities for their development and growth including tailor-made training programmes. Open and clear communications with employees was of paramount importance in 2004, as we seek to align the new Vision, Mission and Core Values with all of our people in a series of workshops and continued to keep them abreast of developments surrounding the possible merger.

MTR again received considerable recognition for our achievement in our people development process. The Operations Training Department gained Integrated Management System – ISO9001, ISO14001 and OHSAS18001 accreditation. The Company also secured a "Most Innovative Award" from the HKMA's Excellence in Training programme and a "BEST" Award from the American Society for Training and Development. Most significantly, for the third consecutive time, we were recognised by the Hong Kong Labour Department with a Good People Management Award, making us the only company to have done so in Hong Kong.

Outlook

Although the ongoing macroeconomic adjustments in the Mainland, the recent sharp increases in oil prices and the U.S. Federal Reserve's decisions to tighten monetary policy have all aroused concerns, on balance we are cautiously optimistic about Hong Kong's business outlook in 2005. We expect economic conditions in Hong Kong to continue to improve albeit at a slower rate of growth than in 2004.

Our rail business should be positively impacted by the opening of the new lines such as the Disneyland Resort Line and KCRC's Ma On Shan Rail but partially offset by the opening of KCRC's Tsim Sha Tsui Extension in October 2004. Our station commercial and related businesses should continue to benefit from improved economic activities in Hong Kong.

Our property rental and management business will benefit from Two IFC being fully leased. In our property development business we expect that over the next two years, the bulk of such profit will come from the remaining Airport Railway developments as they are completed. Beyond that, we would expect our Tseung Kwan O property developments to be the significant contributor to property development profit. In our Airport Railway developments we expect to receive our share of the remaining 25,245 square metres (gross) of retail shell structure at Union Square mainly over the next two years, and the fit out works will take three years prior to an anticipated opening date of end 2007.

In January 2005 we received the remaining up-front payment of HK\$936 million relating to Olympic Package Three which will be booked to our profit and loss account in accordance with the progress of construction and pre-sale

activities, expected to be over the next two years. At Tseung Kwan O, profit from the successful Residence Oasis at Hang Hau Station was already recognised in 2004. In 2005, we will receive the 3,500 square metres (gross) shopping arcade, "The Lane" in Hang Hau Station. Booking of profit for the other three Tseung Kwan O residential developments currently being built, namely at Tiu Keng Leng, and Tseung Kwan O Town Centre Area 57a and Area 55b will depend on the timing and progress of pre-sales as well as the timing of receipt of Occupation Permit. Currently we expect only the development of 390 units at Tseung Kwan O Town Centre Area 57a to receive Occupation Permit in 2005. Package One of Area 86, which was awarded in January 2005 is not expected to contribute to our financial results before 2008. Given current property market conditions and planned development and pre-sale activities, the relatively fewer projects from which we anticipate to record profit in 2005 could lead to lower property development profit recognition than those recorded in 2004.

The Company's financial statements and results may be affected by a number of accounting changes in 2005, notably those relating to valuation of investment properties and financial instruments, which came into effect on 1 January 2005. I will refer you to the more detailed discussion of these in the Financial Review section.

Finally, I would like to extend my gratitude to my fellow Directors, management and all employees, as well as customers, suppliers and shareholders, for their contributions to MTR's continuing success during the year.



C K Chow, *Chief Executive Officer*
Hong Kong, 1 March 2005

Executive management's report

> railway operations

The recovery from SARS saw our railway operations resume steady growth. Passenger numbers rose strongly by 8.3% as economic activity returned to normal and the number of tourists from the Mainland sharply increased. The opening of West Rail in December 2003 and the MTR interchange stations also generated an increase in patronage, more than compensating for a slight loss from the opening of KCRC's East Tsim Sha Tsui Station in October.

Patronage

For the year, the MTR Lines recorded total passenger volume of 834 million, against 770 million in 2003. The year also saw the highest patronage recorded on a single, regular 19-hour service day of 2.72 million on 17 December and a record Christmas Eve patronage of 3.38 million passengers. MTR had a 24.8% share of the total franchised public transport market, higher than in 2003, and increased our share of cross-harbour traffic to 59.6%. Fare revenues from operations rose 7.0% to HK\$5,417 million.

On AEL, passenger volume rose by 17% to 8.0 million. Average fare rose from HK\$62.07 in 2003 to HK\$64.25. Fare revenues rose by 21.2% to HK\$515 million. However, AEL's estimated market share was 21%, 2% points lower than 2003, reflecting a change in the mix of visitors arriving at and departing from Hong Kong Airport.

Service promotion

The Company launched a series of 25th Anniversary celebration campaigns during 2004, including a special anniversary theme train on the Tsuen Wan Line, TV commercials, one-minute TV segments and participation in TVB Jade's "Hong Kong Superbrands" programme. Hong Kong Station was decorated with a birthday theme, and a lucky draw was conducted. Anniversary ticket sets and supplements were produced. We also continued with fare campaigns emphasising the value for money of MTR services, including "Ride 10 Get 1 Free" and "\$2 Holiday Ride" promotions for children and elderly citizens on Sundays and major public holidays, as well as other initiatives. Five fare saver machines were added and five intermodal discount

promotions were launched. An online shopping service on the MTR website added a distribution channel for MTR souvenirs and AEL tickets, and the MTR Club's "WOW Fun Scheme" was extended.

For AEL, increased service frequency was extensively advertised and festive promotional campaigns boosted revenue, notably the group ticket plus free child ride during the summer months. Overseas awareness was enhanced through TV programmes in the Mainland and the launch of online advertising in key markets. AEL launched a "Customer Service Ambassadors" programme to establish a continuous presence in the airport arrival area, as well as online ticketing to secure pre-arrival sales of AEL tickets. MTR also partnered with Cathay Pacific Airways to pre-sell tickets in-flight. Marketing partnerships continued with Asia Miles and the Hong Kong Tourism Board.

Service performance

During the year, we maintained our very high standards of reliability, safety, comfort, and customer satisfaction. Regrettably, a number of noticeable, but not safety critical, incidents in the final months gave rise to public concerns over the reliability of our system. The Company established a high-level internal task force to seek operational improvements and commissioned an independent review of processes and assets by international rail expert and validation agency Lloyd's Register Rail. Following the conclusion of the internal task force in November, the Company began initiatives to augment our maintenance regime and incident handling procedures.

The Lloyd's Register Rail report was received in February 2005, which concluded that MTR service performance has seen significant improvement since 2001 and that best practice asset management system is in place across the Company. We have begun taking immediate action to address some of the report's recommendations, and will study the report in detail and set up the necessary organisations and processes to implement its other recommendations.

Our Asset Management Policy stipulates that MTR is committed to the efficient and effective management of our railway assets to ensure

that the Operating Agreement and all relevant statutory requirements are complied with. This is achieved through continuous improvement of the asset management processes under the principles of minimising the life cycle costs of assets, maximising their worth to the business and managing the associated risks.

Despite the attention given to these incidents of delay and concern to passengers, for 2004 as a whole the Company continued to exceed the minimum performance levels required by the Government under the Operating Agreement, and the more stringent Customer Service Pledges established by MTR. MTR passenger journeys on time were 99.9%, supported by 99.9% reliability for train service delivery. Escalator reliability was 99.9%. Performance was also excellent in key areas affecting passenger comfort such as temperature, ventilation and cleanliness.

Levels of customer satisfaction recorded by our regular survey remained high. The Service Quality Index for the MTR and AEL stood at 71 and 82 respectively on a 100-point scale. MTR also again performed well according to the 11-member Community of Metros (CoMET) benchmarking report, in the areas of safety, service quality and passenger cost. In addition, MTR won the Top Service Award 2004 – Public Transport from Hong Kong's *Next* magazine for the sixth year running.

The effectiveness of our crisis response was demonstrated in January, when the first ever arson attack took place on an MTR train. The incident was resolved quickly and caused no injury to either passengers or personnel thanks to the rapid and effective response of MTR staff and the calm reaction of passengers. The staff involved were presented with commendation letters by the Secretary for Environment, Transport and Works to recognise their exemplary performance in handling the incident.

MTR maintained a high level of safety throughout 2004 and achieved all safety targets set out in the Corporate Safety Plan. We promoted safe behaviour through educational activities and campaigns including a Safety Web Game, a Safety Carnival and a one-month safety campaign.

Service improvements

The year saw further improvements to MTR's infrastructure and services.

During the year, we opened a new entrance at Kowloon Tong Station connecting the station with the new concourse of KCRC's Kowloon Tong Station, and a new subway system connecting Tsim Sha Tsui Station with the KCRC's East Tsim Sha Tsui Station. Inter-modal fare discounts were extended to 14 feeder routes for travellers transferring to MTR from feeder buses on three New Lantao Bus routes, ten Green Minibus routes and one cross-border bus route. The number of fare saver machines offering discounts to Octopus card holders was increased to 15.

Projects to improve barrier free movement in stations continued, with new passenger lifts installed at Central, Tin Hau and Sai Wan Ho stations. At Tsim Sha Tsui Station, three new escalators were installed.

The project to retrofit platform screen doors at all 30 underground stations remained on schedule. At the end of 2004, these doors were in operation on 56 of the 74 platforms involved in 22 stations, with the project now completed on Tsuen Wan Line, and for stations on the Kwun Tong Line between Yau Ma Tei and Wong Tai Sin. The project was also completed between Sheung Wan and Causeway Bay stations, and at North Point Station, on the Island Line.

Productivity increases

The continuing hiring freeze and increased outsourcing helped MTR to raise productivity during the year, as did other initiatives such as Airport Railway stations assuming responsibility for AEL car park management at Hong Kong, Kowloon and Tsing Yi stations, and installing a new computer system to improve non-traffic hours utilisation. Operating costs per car km decreased 1.8% in 2004 to HK\$22.1. Since 1998, operating costs per car km have decreased by 24.3%.

> station commercial and other businesses

The MTR's station commercial and other businesses benefited from the broad economic recovery.

Advertising

Advertising revenue rose 21.0% to HK\$467 million, also helped by upgraded advertising venues and more attractive formats.

Spectacular tunnel advertising was introduced between Wan Chai and Causeway Bay stations. A billboard was installed on the external wall at Quarry Bay Station and a Bloomberg display showing real-time financial information was introduced at Hong Kong Station. In December, a plasma ring was launched at Causeway Bay Station, adding a new format to our plasma network. Almost 700 12-sheet advertising panels were installed network-wide.

We commissioned Nielsen Media Research to conduct "Reach & Frequency Research of MTR Advertising", the first survey of its type in Hong Kong's out-of-home advertising market, and the results helped strengthen our media pricing strategy and advertising media planning.

Telecommunications

Revenue from telecommunications, including TraxComm, rose by 20.2% to HK\$238 million, thanks to increased mobile phone call volumes. The existing integrated radio system was upgraded to support UMTS standard 3G service provision on the Island Line, making it one of the world's first rail networks to be 3G enabled. TraxComm began operating and managing a 50 Gigabit bandwidth network, serving telecom service operators and extending the fibre-optic network to 26 locations.

Station commercial

Revenue from station commercial facilities increased by 8.4% to HK\$298 million. Renovations delivering an additional 1,192 square metres of retail floor area and an enhanced retail environment were completed at Choi Hung, Central, Shau Kei Wan, Tai Koo, Tsuen Wan, Po Lam, Mei Foo, Admiralty and Hong Kong stations. However, with retail space reduced at Kowloon Station for station integration works, the net increase was 268 square metres to reach 18,717 square metres. Renovation works began at Kwai Fong, Sham Shui Po, Yau Ma Tei, Causeway Bay, Wong Tai Sin, Diamond Hill, Lok Fu, Olympic and Tsing Yi stations, and are targeted to complete in the first quarter of 2005.

The Company continued to improve the retail mix, introducing 69 new shops and 28 new trades, including H₂O, Yume, Lo Hang Ka, Q Q Rice, Pie & Tart and TCBY. Sales counters were also introduced in Tseung Kwan O Station for short-term leases to retailers.

External consultancy

The Company currently has consultancy contracts in 22 cities in 11 countries and revenues increased by 27.3% to HK\$182 million. During the year, we decided to reorient this business by focusing on smartcard projects and projects likely to lead to investment opportunities.

Together with Octopus and our other partners, we made good progress on the implementation of a national system for the Netherlands. The Design, Build and Test phase is on track for completion in April 2005, when the Company will provide operation support services. We and our partners are focusing on upcoming projects in Melbourne, Toronto and Los Angeles.

MTR's joint-venture subsidiary in Shanghai, Shanghai Hong Kong Metro Construction Management, currently acting as Owner's Representative for Phase 1 of Line 9 of the Shanghai Rail Transit, has helped ensure that this RMB 11 billion (HK\$10.4 billion) project made substantial progress towards completion by the end of 2007.

Rail Sourcing Solutions (International) Limited

In August, we established Rail Sourcing Solutions (International) Limited as a wholly-owned subsidiary, to expand into global railway supply and sourcing services.

Octopus Cards Limited (Octopus)

Octopus Cards Limited achieved progress in both the transportation and retail sectors. Its pre-tax profit contribution to the Company increased by 91.3% to HK\$44 million. Average daily Octopus card usage rose from HK\$50.7 million to HK\$57.5 million. Cards in circulation rose from 10.4 million to 11.8 million, while the number of service providers increased from 253 to 299.

Growth in retail usage was driven by the addition of new service providers and full roll out to existing providers. The number of financial institutions participating in the Automatic Add Value Service increased to 19 in 2004 and now includes HSBC, Bank of China, Standard Chartered Bank and Citibank. Overall usage was supported by year-round promotions, including "Rewards on the Go", a monthly lucky draw for frequent card users at retail outlets and car parks.

> international expansion

Mainland of China

Our Mainland investment strategy focuses on major cities of Beijing, Shanghai and Shenzhen where demand for mass transit systems and profit potential is greatest. The Company has adopted a gradual approach, leveraging the experience gained from one project to others.

In January, the Company entered into an Agreement in Principle for a Build-Operate-Transfer project with the Shenzhen Municipal People's Government for the construction of Phase 2 of Line 4 of the proposed Shenzhen Metro System and the operation of the entire line for 30 years. The project will also include property development rights of an aggregate gross floor area of 2.9 million square metres at stations and depot along Line 4.

Line 4 is a 21-kilometre double-track urban railway running from Huanggang, at the boundary between Hong Kong and Shenzhen, to Longhua New Town in Shenzhen, with a total of 14 stations. Total investment in Phase 2 is estimated at approximately RMB 6 billion (HK\$5.7 billion). This will be financed by equity capital of RMB 2.4 billion (HK\$2.3 billion) with the balance by non-recourse bank loans in RMB. Phase 1 of Line 4 is targeted for full completion before end of 2008. Upon completion of Phase 2 by MTR's project company in late 2008, both Phases 1 and 2 will be operated by MTR.

Since signing the Agreement in Principle, MTR has set up a project office in Shenzhen to undertake preliminary design of the railway and property works and entered into

negotiations with the Shenzhen Municipal People's Government on a Concession Agreement and other related agreements which would give the MTR's project company the right to construct Phase 2 and to operate the entire line, together with the right to use the Phase 1 facilities. These agreements are subject to the approval of the Central Government. Planning for property developments associated with the Shenzhen Line 4 project progressed despite a delay in the approval process, and the target completion of the development sites is from 2008 onwards.

After signing a Memorandum of Understanding in April, we entered into an Agreement in Principle with Beijing Infrastructure Investment Co. Ltd (BIIIC) and Beijing Capital Group (BCG) in December, to form a Public-Private-Partnership company for the investment, construction and operation of the Beijing Metro Line 4. In February 2005, together with our partners, we initialled the Concession Agreement with the Beijing Municipal People's Government and now await approval from the National Development and Reform Commission. Total investment is approximately RMB 15.3 billion (HK\$14.4 billion) of which 70%, land acquisition and civil construction, will be financed by the Beijing Municipal People's Government. The partnership project company will invest approximately RMB 5 billion (HK\$4.7 billion) to finance the remaining 30%, comprising provision of trains and related electrical and mechanical systems, and will be responsible

for the operation and management of the new line for 30 years.

MTR and BCG will each own 49% of the joint venture company, with BIIIC owning the remaining 2%. The joint venture company will seek non-recourse bank loans to finance over 60% of the project with the remainder to be funded by equity capital. This new 29-kilometre underground line will run from Majialou Station on the South Fourth Ring Road to the north western Haidian District and terminate at Longbeicun Station, forming a main north-south traffic artery of Beijing.

Europe

Our growth strategy in Europe focuses on train operation franchises, which do not require significant capital expenditure. MTR will seek joint-venture partnerships with experienced local firms to bid for operation and maintenance franchises and contracts.

In November, we signed a joint-venture agreement with the UK's Great North Eastern Railway Holdings Limited to bid for a service contract to operate and maintain trains for the Integrated Kent Franchise (IKF). MTR owns 29% of the joint-venture company. IKF is a suburban commuter network in Kent, operating through 179 stations, 1,600 rail cars and with annual revenue of about £300 million. It includes the high-speed railway service from the Kent Coast to London operating over the Channel Tunnel Rail Link.

Since December, MTR has been working to pursue a similar opportunity for the Thameslink / Great Northern Franchise, which serves London north and south of the River Thames.

> property business

In 2004, MTR's property businesses benefited from a sustained recovery and growth in the Hong Kong property market, inbound tourism and an improved economy.

Property development

Property development profit was HK\$4,568 million, a decrease from 2003, when we recognised as income the receipt of our share of floors in Two IFC.

Airport Railway

Along the Airport Railway, profit contributions came from the receipt of part of the Union Square retail shell structure at Kowloon

Station. Other contributors included our share of surplus proceeds from The Harbourside, and recognition of deferred income from Tung Chung Packages Two and Three (Coastal Skyline and Caribbean Coast), and The Harbourside.

Sales and pre-sales of properties benefited from the strong property market. Sales of luxury apartments at The Harbourside achieved very satisfactory results. The pre-sale of Caribbean Coast Towers 9 and 11 met with a very good response. The sale was launched of the 392 units at Coastal Skyline Tower 2 of Tung Chung Package Two.

The Company and our developers continued to work with the Government and the Town Planning Board to refine future development plans, to take advantage of market developments. A revised Master Layout Plan for Tung Chung Package Two, Coastal Skyline, was approved by the Town Planning Board, providing more open space by reducing the number of low-rise developments. At Tsing Yi, the Town Planning Board took forward our proposed part-conversion scheme to change the lorry park to retail use through a land use rezoning.

At Kowloon Station, a review of the construction programme and design for Union Square Packages Five, Six and Seven was undertaken by the developer, which may delay completion of the Landmark Tower development to 2010.

Tseung Kwan O Line

Along the Tseung Kwan O Line, development profit was derived from Residence Oasis at Hang Hau Station. Sales of residential units of Residence Oasis were very satisfactory and pre-leasing progressed well for the associated 3,500-square metre shopping centre, "The Lane."

Pre-sale consent for Area 57a was obtained and the developer is expected to launch sales in early 2005. Pre-sale consent for Area 55b is planned and should be granted in early 2005.

At Area 86, location of the Tseung Kwan O Line depot and future Tseung Kwan O South Station, approval was granted for a substantial revision to the Master Layout Plan for the "Dream City", which greatly enhanced the garden city and pollution-free concept. The tender for Package One of Area 86 was awarded in January 2005.

The Company also submitted a planning application for Area 56 to the Town Planning

Board in January 2005, to convert the site to a more commercially viable mixed-use development.

Investment properties

The continuing economic recovery increased revenue from investment properties by 11.9% to HK\$994 million. The primary drivers were higher renewal rents, favourable turnover rental, better promotional counter income and higher rental income from Two IFC.

We again achieved 100% occupancy at our shopping centres, Telford Plaza, Maritime Square, Luk Yeung Galleria and Paradise Mall. Several large new tenants signed during 2004. IKEA opened its largest 7,800 square metres store in Kowloon at Telford Plaza. Demand for space at Two IFC continued to grow. By year end, 100% of MTR's 18 floors were leased. At year end, MTR's investment property portfolio totalled 176,020 square metres

Property management and others

The year saw steady growth in the MTR's property management portfolio, leading to a 14.9% rise in revenues from property

management to HK\$108 million. During the year, 2,368 units were added to the portfolio: 854 from Sorrento, 1,122 from The Harbourside, and 392 from Coastal Skyline. As a result, by year end MTR had 49,283 residential units and 558,796 square metres of commercial and office space under management.

Revenue from property agency was stable at HK\$6 million. The MTR's Octopus Access Control business continued to expand, with annual turnover increasing by 19% to HK\$10 million. In the Mainland, Octopus Access Control was adopted by Shanghai Hong Kong Metropolis, a high-end serviced apartment and commercial complex located in Shanghai's Central Business District and to be completed in 2008.

Business in the Mainland

MTR's expertise continued to translate into Mainland contracts for pre-management advisory and property management. Currently, MTR has more than 800,000 square metres of residential and commercial space under pre-management contracts and some 422,000 square metres of residential and commercial space under property management contracts.

> future Hong Kong projects

MTR made further progress on projects to expand and enhance our rail-property infrastructure in Hong Kong, while ensuring project plans are sensitive to the environment and economically sound.

We are working to ensure completion by 1 July 2005 of the Disneyland Resort Line, which will connect the theme park with the MTR network. Construction of the Tai Yam Teng Tunnel was completed. Architectural and builders works, and installation of electrical and mechanical equipment were substantially completed for both Disneyland Resort Station and Sunny Bay Station. Automatic platform gates have been installed and conversion of rolling stock completed.

Construction work began on the Tung Chung Cable Car project. Mules were imported to transport materials in the Country Park. Construction of the Tung Chung and Ngong Ping terminals progressed well and work

started on the Theme Village. Completion of the project by early 2006 remains on track.

In February, we submitted to the Government proposals for an extension of the Kwun Tong Line from Yau Ma Tei Station to Whampoa Gardens. Consultants were asked to prepare detailed design proposals for Tseung Kwan O South Station located within the future "Dream City", which will be completed in 2009.

In January 2003, the Government requested MTR to proceed with planning for the West Island Line and the South Island Line. In March 2004, MTR submitted revised proposals to the Government. The proposals contain three elements: an extension of the high capacity Island Line to serve Western District; and two medium capacity lines to serve the south side of Hong Kong Island. One of the medium capacity lines would interchange with the Island Line at Admiralty Station and serve Ocean Park, Wong Chuk Hang and Ap Lei Chau. The other would interchange with the Island

Line extension in Western District and serve locations such as Cyberport, Wah Fu and Aberdeen, terminating at the Wong Chuk Hang interchange station. Discussions continue with the Government on the scope and programme for these new lines.

Work proceeded on schedule for the new AsiaWorld-Expo Station at the end of AEL at Hong Kong International Airport that will serve the AsiaWorld-Expo. It is scheduled for completion by end 2005.

The Company continues discussions with the Airport Authority over plans to expand the facilities at Airport Station to connect to the Authority's new Skyplaza development.

In January, developer funded construction began on the new Queensway subway that will connect Three Pacific Place with Admiralty Station, with completion scheduled by the end of 2005.

> human resources

We continued to work closely with our skilled, talented and committed employees to ensure their continuing support. A hiring freeze in line with our productivity drive remained in force and this has resulted in our total staff number declining to 6,555 from 6,629 in 2003. Turnover per operating railway employee increased from HK\$1.27 million in 2003 to HK\$1.40 million.

The Company's new Vision, Mission and Core Values were actively communicated to all staff. 134 workshops designed to help align the Company's culture and values with our Hong Kong and overseas business strategies were held. We also worked to ensure open and transparent communication with employees about the possible merger with KCRC and its potential implications.

A number of initiatives were developed in response to employee concerns raised in the 2003 Staff Attitude Survey. "Meet the CEO" and "Meet Senior Management" programmes were initiated to improve staff and senior management communication.

Specific programmes were also developed to help managers and supervisors improve their leadership skills. In addition, over 1,300 supervisory staff participated in a "New Horizon for Supervisors" training programme.

To support the Company's overseas business development, MTR's Human Resource Management Department provided professional advice and personnel support to line managers and staff on overseas assignments. In meeting the challenges posed

by overseas expansion, MTR has also implemented a just-in-time manpower resourcing strategy. This includes building a dedicated resource pool to grow the business, backed by customised remuneration and employment terms, comprehensive human resources policies and systems, as well as training and development initiatives.

For the third consecutive time, MTR received the Hong Kong Labour Department's Good People Management Award. The Operations Training Department gained ISO9001, ISO14001 and OHSAS18001 accreditations for its Integrated Management System. The Company also received the HKMA's "Most Innovative Award" and a "BEST Award" from the American Society for Training and Development.

> financial review

Review of 2004 financial results

Profit and loss

Total patronage for the MTR Lines increased significantly from 770 million to 834 million. Average weekday patronage improved to 2.40 million from 2.24 million. MTR's overall share of total franchised public transport rose to 24.8% from 24.3%, while the cross-harbour market share increased from 58.7% to 59.6%.

Total fare revenue for the MTR Lines increased 7.0% to HK\$5,417 million. With a higher proportion of passengers using concessionary tickets and an increase in free-ride tickets issued through the "Ride 10 Get 1 Free" promotion campaign, the average fare dropped slightly to HK\$6.50.

Average daily patronage on AEL rose by 16.6% to 21,800, while our estimated market share of airport passengers reduced from 23% to 21%. Total revenue from AEL increased by 21.2% to HK\$515 million, with the average fare improving from HK\$62.07 to HK\$64.25 in 2004.

Non-fare revenue grew strongly to HK\$2,419 million, comprising HK\$1,311 million from station commercial and other revenue and HK\$1,108 million from property rental and management. Station commercial and other revenue grew 17.4% mainly due to advertising and telecommunication income. Property rental and management income increased by 12.1%, mainly attributable to a full year of operation of Two IFC, an expanded portfolio of managed properties, higher rental renewal rates, and the removal of SARS rental concessions.

Despite a general increase in business activities, operating expenses before depreciation decreased 1.1% to HK\$3,805 million and staff costs were reduced from HK\$1,643 million to HK\$1,542 million, mainly due to lower pension expenses. There was also a HK\$69 million write-back of property revaluation deficit on our head office building made in 2003. These were partly offset by higher Government rent and rates, higher maintenance costs of HK\$517 million, and higher project study and business development costs.

Operating profit from railway and related operations before depreciation and interest amounted to HK\$4,546 million, an increase of 21.3%. Operating margin was 54.4% compared with 49.3% in 2003.

Profit on property development was HK\$4,568 million compared with HK\$5,369 million, comprising mainly sharing in kind for part of Kowloon Station's Union Square retail shell structure, recognition of deferred income relating to Caribbean Coast and Coastal Skyline at Tung Chung Station and The Harbourside at Kowloon Station, and surplus proceeds from the Harbourside at Kowloon Station and Residence Oasis at Hang Hau Station in Tseung Kwan O.

Operating profit before depreciation was HK\$9,114 million, almost the same as in 2003. Depreciation charges increased by 4.6% to HK\$2,512 million from HK\$2,402 million, mainly due to a full year's depreciation in respect of the West Rail Interchange facilities following its commissioning in December 2003, and depreciation on new railway assets.

Net interest expenses decreased to HK\$1,450 million due to lower interest rate environment and reduced borrowings. The average interest rate reduced to 4.7% while the interest cover increased to 6.1 times.

The Company's share of Octopus Cards Limited's pre-tax earnings was HK\$44 million. Income tax expenses decreased by 6.4% to HK\$700 million, mainly due to a HK\$300 million deferred tax adjustment on an increase in the Profits Tax rate in 2003, which was partly offset by higher deferred tax expense on the 2004 property development profit. As a result, the Group's profit attributable to shareholders for the year was HK\$4,496 million, an increase of 1.0%. Earnings per share decreased slightly from HK\$0.85 to HK\$0.84 owing to new shares issued.

The Board recommended a final dividend of HK\$0.28 per share, amounting in total to HK\$1,509 million. The Government has agreed to receive its entitlement to dividends in the form of shares to the extent necessary to ensure a maximum of 50% of MTR's total dividend will be paid in cash.

Balance sheet

The Group's balance sheet remained strong, with the bulk of assets invested in the railway system. Total fixed assets increased from HK\$96,921 million to HK\$100,313 million as at 31 December 2004, mainly attributable to receipt of the shell structure of a retail centre and surpluses in investment property revaluation.

Railway construction in progress increased to HK\$962 million as at 31 December 2004, due to additional capital expenditures on the Disneyland Resort Line, Tung Chung Cable Car and AsiaWorld-Expo Station projects. Property development in progress at the year end decreased by 9.6% to HK\$2,088 million, mainly due to the transfer of development costs of Hang Hau property development project upon its completion out of the account.

Cash and cash equivalents decreased to HK\$269 million as at 31 December 2004 from HK\$376 million as at 2003 year end.

Total loans outstanding at year end were HK\$30,378 million, a decrease of HK\$1,647 million due to loan repayments. Loans drawn down amounted to HK\$7,194 million which were primarily for refinancing purposes.

Deferred income decreased to HK\$4,638 million following profit recognition at Tung Chung and Kowloon station developments based on progress of property construction and pre-sales programmes. This was partly offset by an increase in the transfer-in of deferred income in respect of the retail shell structure at Kowloon Station.

Our share capital, share premium and capital reserve of HK\$36,269 million at year-end was HK\$1,183 million higher than in 2003, as a result of shares issued for scrip dividend and share options exercised. Together with increases in property revaluation reserves of HK\$2,759 million and retained earnings net of dividend of HK\$2,265 million, total shareholders' funds increased to HK\$63,499 million from HK\$57,292 million. As a result, the Group's gross debt-to-equity ratio improved from 55.9% to 47.8% at 2004 year-end and net debt-to-equity ratio from 55.2% to 47.4%.

Cash flow

Net cash inflow generated from railway and related activities increased to HK\$4,486 million, while cash receipts from developers for property development projects increased from HK\$855 million to HK\$2,576 million. Outflows for capital project payments and interest expenses amounted to HK\$2,889 million and HK\$1,301 million respectively, compared to HK\$2,670 million and HK\$1,643 million. Together with other minor movements, net cash flow before dividends and loan repayments were HK\$2,566 million, HK\$2,109 million higher. After dividend payments of HK\$1,079 million and net loan repayment of HK\$1,593 million, there were net cash outflows of HK\$106 million compared to HK\$1,320 million.

Revised accounting standards in 2005

Following the convergence of the Hong Kong Accounting Standards with the International Accounting Standards from 1 January 2005, the accounting standards in Hong Kong have been substantially revised and the Company's future financial statements and results will be affected

by these changes, notably those relating to valuation of investment properties and financial instruments. Previously, changes in the fair value of investment properties arising from revaluation had been generally recognised through the reserve account on a portfolio basis without impacting the Profit and Loss Account (P&L). However, after 1 January 2005, these revaluation gains or losses are required to be brought through the P&L. With the volatility of property prices being a characteristic of the Hong Kong market, this new accounting standard could have a significant impact on the level and consistency of our reported profit.

The new accounting standard relating to financial instruments requires that after 1 January 2005 all financial instruments which the Company is using to hedge the interest rate and currency risks of our borrowings must be marked to market, with any change in their fair values recognised in the P&L directly. However, the standard allows the application of hedge accounting, that is, to use the change in fair value of the underlying hedged items to offset this impact so that only inefficiency in the hedging relationship resulting in net residual impact will be reported in the P&L. Given that hedge efficiency is affected by a number of factors including the nature of the hedging relationship, direction of interest rates and changes in foreign exchange rates, it is difficult to forecast and control this residual impact.

It should be stressed, however, that both these items are non-cash items and hence do not affect cash flow. The revised standards also introduced a number of other minor changes, mainly on alignment of disclosure with the international standards, which will be reflected in the 2005 accounts.

Financing activities

New financings

In January, the Group took advantage of favourable market conditions and successfully launched a US\$600 million 10-year fixed rate bond. The offering attracted total subscriptions of almost US\$1.9 billion from over 130 accounts. Carrying a coupon rate of 4.75%, the bond was priced at an attractive re-offer spread of 83 basis points over 10-year treasuries. The transaction not only extended our debt maturity profile but also established a new benchmark for Hong Kong's quasi-sovereign credits. This was later in the year supplemented by a HK\$200 million 12-year and HK\$300 million 15-year bond. At the end of 2004, the Company had total undrawn committed facilities amounting to HK\$5.8 billion, sufficient to cover all of our expected funding needs into the second quarter of 2006.

Cost of borrowing

The attractive terms of the new financings together with prevailing low interest rates enabled the Group to further lower overall borrowing cost to 4.7% from 5.1%, and to reduce gross interest expense by HK\$149 million.

Risk management

The Company continued to undertake fund raising activities and manage our debt portfolio in accordance with the Preferred Financing Model. As a result, the Company maintained a balanced debt profile with adequate risk diversification and sufficient coverage of anticipated future funding needs. The Company uses derivatives solely for hedging purposes.

Credit ratings

Moody's re-affirmed the Company's short-term foreign currency rating and long-term domestic/foreign currency ratings at respectively P-1 and Aa3/A1 with a stable outlook. Standard & Poor's also affirmed our ratings at A-1+/A-1 and AA-/A+ for short-term local/foreign currency and long-term local/foreign currency borrowings respectively with a negative/stable outlook respectively on the local and foreign currency ratings, with the negative outlook on local currency subsequently revised to stable. R&I also re-affirmed the Company's short-term local currency and long-term domestic/foreign currency ratings at respectively a-1+ and AA/AA-.

Financing capacity

Our current committed capital expenditure programme comprises mainly the maintenance and upgrade of the existing lines, 50% land premium of Tseung Kwan O Area 86 Package One, and the construction of the Disneyland Resort Line and Tung Chung Cable Car. Capital expenditure programme for the next three years is therefore expected to be modest, with a budget of around HK\$6.8 billion. MTR thus has financing capacity to take advantage of any new investment opportunities.

The estimated total investment of RMB 6 billion (HK\$5.7 billion) for Shenzhen Line 4 will be funded 40% by equity and 60% by non-recourse bank loans in Renminbi. MTR's investment in Beijing Line 4 will be represented by our 49% shareholding in the PPP company which is responsible for the trains and related electrical and mechanical systems which are estimated at RMB 5.0 billion (HK\$4.7 billion). It is planned that more than 60% of the investment by the PPP company will be funded by non-recourse bank loans in Renminbi with the balance financed by equity capital. MTR's equity investment in the PPP company therefore is estimated at around RMB 735 million (HK\$693 million). We anticipate that MTR's total equity investment of slightly above RMB 3 billion (HK\$2.8 billion) in these two projects will be financed by a combination of internally generated funds and external borrowing by the Company.

The capital structure and funding alternatives for the SIL and WIL as well as the Kwun Tong Line extension, in respect of which MTR submitted proposals to the Government, will be examined at a later stage if and when Government approvals are obtained.

Ten-year statistics

	2004*	2003*	2002*	2001*	2000*	1999	1998	1997	1996	1995
Financial										
Profit and loss account										
<i>in HK\$ million</i>										
Turnover	8,351	7,594	7,686	7,592	7,577	7,252	6,981	6,574	6,253	5,737
Operating profit before depreciation	9,114	9,116	7,769	7,301	7,290	5,523	4,720	3,805	3,342	3,143
Depreciation	2,512	2,402	2,470	2,178	2,091	2,039	1,426	927	850	658
Interest and finance charges	1,450	1,539	1,125	874	1,143	1,104	475	95	957	1,289
Profit	4,496	4,450	3,579	4,278	4,069	2,116	2,819	2,783	1,535	1,196
Dividend proposed and declared	2,259	2,215	2,161	2,118	500	–	–	1,252	647	–
Earnings per share <i>in HK\$</i>	0.84	0.85	0.70	0.85	0.81	0.42	–	–	–	–
Balance sheet										
<i>in HK\$ million</i>										
Total assets	106,674	102,366	101,119	98,126	92,565	87,250	82,104	75,428	64,644	45,356
Loans, obligations under finance leases and bank overdrafts	30,378	32,025	33,508	31,385	27,203	23,177	16,897	10,875	12,696	14,736
Deferred income	4,638	5,061	6,226	8,411	10,403	13,776	15,970	16,705	9,094	1,056
Shareholders' funds	63,499	57,292	53,574	53,893	50,355	45,115	42,601	41,815	35,473	25,261
Financial ratios										
<i>in percentage</i>										
Operating margin	54.4	49.3	52.2	53.4	51.7	48.2	47.3	53.7	53.4	54.8
Non-fare revenue as a percentage of turnover	29.0	27.7	25.6	24.6	24.6	22.2	22.1	21.0	18.8	17.8
Gross debt-to-equity ratio	47.8	55.9	62.5	58.2	54.0	51.4	39.7	26.0	35.8	58.3
Gross debt-to-equity ratio (excluding revaluation reserves)	56.2	63.3	71.1	66.4	62.2	58.5	45.0	31.3	43.8	73.4
Interest cover <i>in times</i>	6.1	5.6	4.5	3.8	3.8	3.7	5.1	15.7	4.0	2.9
Employees										
Corporate management and service departments	860	855	886	930	966	1,031	1,317	1,104	1,069	1,075
Operations	4,669	4,730	4,836	4,756	4,943	5,132	5,890	4,575	4,499	4,490
Engineering and project	366	402	551	978	904	918	1,111	2,380	1,871	1,444
Property development and management	660	642	618	567	519	456	468	427	405	388
Total	6,555	6,629	6,891	7,231	7,332	7,537	8,786	8,486	7,844	7,397

	2004*	2003*	2002*	2001*	2000*	1999	1998	1997	1996	1995
Railway operations										
Revenue car km operated										
<i>in thousands</i>										
MTR Lines	114,364	112,823	103,318	96,751	92,199	94,704	94,260	84,258	83,769	82,472
Airport Express Line	16,081	15,227	19,467	19,458	19,557	19,394	9,011	–	–	–
Total number of passengers										
<i>in thousands</i>										
MTR Lines	833,550	770,419	777,210	758,421	767,416	779,309	793,602	811,897	816,572	812,519
Airport Express Line	8,015	6,849	8,457	9,022	10,349	10,396	3,928	–	–	–
Average number of passengers										
<i>in thousands</i>										
MTR Lines – weekday average	2,403	2,240	2,261	2,231	2,240	2,284	2,326	2,382	2,379	2,377
Airport Express Line – daily average	22	19	23	25	28	29	22	–	–	–
Average passenger km travelled										
MTR Lines	7.7	7.7	7.6	7.4	7.3	7.4	7.4	7.4	7.5	7.5
Airport Express Line	30.2	29.7	29.9	29.8	29.7	29.9	31.2	–	–	–
Average car occupancy										
MTR Lines	56	53	57	58	61	61	62	71	73	74
Airport Express Line	15	13	13	14	16	16	14	–	–	–
Proportion of franchised public transport boardings										
<i>in percentage</i>										
All movements	24.8	24.3	23.5	23.5	24.1	25.2	25.7	25.9	26.7	27.4
Cross-harbour movements	59.6	58.7	58.2	57.4	57.9	60.3	61.9	64.2	66.5	67.6
Proportion of transport boardings										
<i>in percentage</i>										
To/from the airport	21	23	25	27	28	32	25	–	–	–
HK\$ per car km operated (all services)										
Fare revenue	45.5	42.9	46.6	49.3	51.1	49.4	52.7	61.6	60.6	57.2
Railway operating costs	22.1	22.5	22.8	24.6	26.8	27.3	29.2	29.5	29.1	26.0
Railway operating profit	23.4	20.4	23.8	24.7	24.3	22.1	23.5	32.1	31.5	31.2
HK\$ per passenger carried (all services)										
Fare revenue	7.05	7.06	7.28	7.46	7.35	7.14	6.82	6.39	6.22	5.80
Railway operating costs	3.43	3.70	3.57	3.72	3.85	3.94	3.78	3.06	2.99	2.64
Railway operating profit	3.62	3.36	3.71	3.74	3.50	3.20	3.04	3.33	3.23	3.16
Safety performance										
Number of incidents	701	641	690	686	748	859	842	814	869	716
Incidents per million passengers carried	0.83	0.82	0.88	0.89	0.96	1.09	1.05	1.00	1.06	0.88
Number of staff and contractors' staff accidents	25	33	24	39	36	49	65	54	40	42

* Consolidated results

Board and Executive Directorate

Members of the Board

Dr. Raymond Ch'ien Kuo-fung 53, was appointed Non-Executive Chairman in July 2003. He has been a member of the Board since 1998. Dr. Ch'ien is executive chairman of chinadotcom corporation and non-executive chairman of HSBC Private Equity (Asia) Limited. He serves on the boards of HSBC Holdings plc, The Hongkong and Shanghai Banking Corporation Limited and Inchcape plc. Dr. Ch'ien is chairman of the Advisory Committee on Corruption of the Independent Commission Against Corruption; chairman of the Hong Kong/European Union Business Cooperation Committee (with effect from 1 February 2005) and a Hong Kong member of the APEC Business Advisory Council. Dr. Ch'ien received a doctoral degree in economics from the University of Pennsylvania in 1978.

Chow Chung-kong 54, was appointed Chief Executive Officer on 1 December 2003. He was formerly chief executive officer of Brambles Industries PLC. From 1997 to 2001, Mr. Chow was chief executive of GKN PLC and before that, he spent 20 years with the BOC Group PLC and was appointed a director of its board and chief executive of its Gases Division in 1993. He is a chartered engineer with B.S. and M.S. degrees in Chemical Engineering from The University of Wisconsin and The University of California respectively. He holds a master of business administration degree from The Chinese University of Hong Kong and was a graduate of the Advanced Management

Program of Harvard Business School. He was awarded an Honorary Doctor of Engineering degree by The University of Bath. Mr. Chow was knighted in the United Kingdom in 2000 for his contribution to industry. He is currently member of the Council of the Hong Kong Institute of Certified Public Accountants, the Hong Kong Tourism Board and the Council of The Chinese University of Hong Kong. Mr. Chow is also a non-executive director of Standard Chartered PLC and the non-executive chairman of Standard Chartered Bank (Hong Kong) Limited.

Professor Cheung Yau-kai 70, is an independent non-executive Director and has been a member of the Board since 1999. Professor Cheung is Honorary Professor of Engineering and Special Adviser to the Vice-Chancellor of The University of Hong Kong. He has been awarded several honorary degrees including, an honorary Doctor of Science by The University of Hong Kong and an honorary Doctor of Laws by the University of Wales.

David Gordon Eldon 59, is an independent non-executive Director and has been a member of the Board since 1999. He is the chairman of The Hongkong and Shanghai Banking Corporation Limited and a director of HSBC Holdings plc, the non-executive chairman of Hang Seng Bank Limited, a director of HSBC Bank Australia Limited and a director of Swire Pacific Limited. In addition, Mr. Eldon is also a Steward of the Hong Kong Jockey Club.

Christine Fang Meng-sang 46, was appointed independent non-executive Director on 1 January 2004. Ms. Fang has been the chief executive of the Hong Kong Council of Social Service since 2001. She sits on various government advisory committees, including the Social Welfare Advisory Committee, the Rehabilitation Advisory Committee, the Community Investment & Inclusion Fund Committee, the Hong Kong Housing Authority, the Sustainable Development Council, and the Advisory Council on AIDS.

Edward Ho Sing-tin 66, is an independent non-executive Director and has been a member of the Board since 1991. He is an architect and is deputy chairman and managing director of Wong Tung & Partners Limited. Mr. Ho is also a board member of the Hospital Authority.

Lo Chung-hing 53, is an independent non-executive Director and has been a member of the Board since 1995. Mr. Lo is currently general manager of Bank of China (Hong Kong) Ltd, after the restructuring of the Bank of China Group in October 2001. He is also a board member of the Hospital Authority and a director of the Urban Renewal Authority.

T. Brian Stevenson 60, is an independent non-executive Director and has been a member of the Board since October 2002. He is a non-executive director of The Hongkong and Shanghai Banking Corporation Limited and is a member of the Public Service Commission and a Steward of the Hong Kong Jockey Club. He is a chartered accountant and holds law degrees from Glasgow and Hong Kong Universities.

Commissioner for Transport (Robert Charles Law Footman 52, joined the Board as a non-executive Director appointed as an “additional director” under section 8 of the Mass Transit Railway Ordinance in June 2000. He is the Commissioner for Transport of the Government of the Hong Kong Special Administrative Region of the People’s Republic of China (“SAR”). Mr. Footman had previously served as Postmaster General, Head of the Efficiency Unit and Deputy Director-General of Trade of the Hong Kong Government. As Commissioner for Transport, Mr. Footman is also a director of several transport-related companies, including The Kowloon Motor Bus Holdings Ltd., Long Win Bus Co. Ltd., New World First Bus Services Limited, New Lantao Bus Company Limited, Citybus Limited, The Star Ferry Company Limited, The New Hong Kong Tunnel Company Limited, Western Harbour Tunnel

Company Limited, Tate’s Cairn Tunnel Company Limited and Route 3 (CPS) Company Limited.)

Secretary for the Environment, Transport and Works (Dr. Sarah Liao Sau-tung 53, joined the Board as a non-executive Director appointed as an “additional director” under section 8 of the Mass Transit Railway Ordinance in August 2002 after her appointment as the Secretary for the Environment, Transport and Works of the Government of the Hong Kong SAR on 1 July 2002. As Secretary for the Environment, Transport and Works, she is also a director of a number of companies including Kowloon-Canton Railway Corporation, and Route 3 (CPS) Company Limited. Dr. Liao obtained a Doctorate Degree (Environmental/Occupational Health) from The University of Hong Kong. She has also been a fellow of the Royal

Society of Chemistry since 1995 and of the Hong Kong Institution of Engineers since 1996.)

Frederick Ma Si-hang 53, joined the Board as a non-executive Director on 1 July 2002 upon his appointment as Secretary for Financial Services and the Treasury of the Government of the Hong Kong SAR. Besides serving as board member of Kowloon-Canton Railway Corporation and Airport Authority, Mr. Ma is also a director of Hong Kong International Theme Parks Limited, Hong Kong Mortgage Corporation Limited, Mandatory Provident Fund Schemes Authority and Hong Kong Institute for Monetary Research. Graduated from The University of Hong Kong in 1973, Mr. Ma holds a Bachelor of Arts degree, majoring in economics and history.

Members of the Executive Directorate

Chow Chung-kong Brief biographical details are set out on page 16.

Russell John Black 58, has been appointed the Project Director of the Company since 1992. He initially worked for the Company from 1976 to 1984 and, prior to rejoining the Company in 1992, he was project director on the London Underground Jubilee Line Extension. Mr. Black holds an honours degree in civil engineering from the University of Canterbury in New Zealand. He is a Fellow of the Hong Kong Academy of Engineering Sciences, the Hong Kong Institution of Engineers and the Institution of Professional Engineers New Zealand.

William Chan Fu-keung 56, has been the Human Resources Director since August 1998. Mr. Chan joined the Company as Human Resources Manager in 1989. He graduated from The University of Hong Kong in 1971, majoring in economics.

Philip Gaffney 57, was appointed Managing Director of Operations and Business Development in March 2004. He joined the Company in 1977 and was previously Operations Director. Mr. Gaffney is a railway signalling engineer.

Thomas Ho Hang-kwong 54, has served as Property Director since joining the Company in 1991. Between 1971 and 1990, he worked for the Hong Kong Government specialising in land administration. Mr. Ho is a chartered surveyor.

Lincoln Leong Kwok-kuen 44, has served as the Finance Director since February 2002. Mr. Leong graduated from Cambridge University and is a chartered accountant. Prior to joining the Company as Finance Director, he worked in both the accountancy and investment banking industries.

Mr. Leong is also a non-executive director of both Hong Kong Aircraft Engineering Company Limited (HAECO) and Tai Ping Carpets International Limited.

Leonard Bryan Turk 55, is a solicitor admitted to practice both in England and Wales and in Hong Kong. He joined the Company in 1981 and has been Legal Director and Secretary to the Board since 1988.

Report of the Members of the Board

The members of the Board have pleasure in submitting their Report and the summary financial statements for the financial year ended 31 December 2004.

Principal Activities of the Group

The principal activities of the Company and its subsidiaries are:

- A** the operation of a mass transit railway system with lines from Central to Tsuen Wan (Tsuen Wan Line), from Yau Ma Tei to Tiu Keng Leng (Kwun Tong Line), from Po Lam to North Point (Tseung Kwan O Line), from Chai Wan to Sheung Wan (Island Line), from Hong Kong to Tung Chung (Tung Chung Line) and from Hong Kong to the Hong Kong International Airport at Chek Lap Kok (Airport Express Line);
- B** property development at locations relating to the railway system including the Tseung Kwan O Extension;
- C** related commercial activities, including the letting of advertising and retail space, bandwidth services on the railway telecommunication system, property management and leasing management of investment properties (including shopping centres and offices), property agency and Octopus Card Building Access System services;
- D** the construction of Disneyland Resort Line (formerly known as Penny's Bay Rail Link);
- E** the design, construction and operation of the Tung Chung Cable Car Project and related tourist development;
- F** the planning and construction of future extensions to the railway system and other related infrastructure projects;
- G** consultancy services covering all areas of expertise required in the project management, planning, construction, operation, maintenance and up-grading of railways plus fare collection, property integration/development advice including other property related services and advice on generation of non-fare revenues;
- H** the operation of a smart card system by Octopus Cards Limited, a subsidiary of the Company, for the collection of payments for both transport and non-transport applications; and
- I** equity investments and long term operation and maintenance contracts outside of Hong Kong.

Dividend

The Directors have recommended a final dividend of HK\$0.28 per Ordinary Share to be payable to shareholders whose names appear on the Register of Members of the Company on 1 April 2005. Subject to the passing of the necessary resolution at the forthcoming Annual General Meeting, such dividend will be payable on or about 21 June 2005, in cash in Hong Kong dollars, with a scrip dividend alternative. The Company's majority shareholder, The Financial Secretary Incorporated, has agreed to elect to receive all or part of its entitlement to dividends in the form of scrip to the extent necessary to ensure that a maximum of 50% of the total dividend paid by the Company will be in the form of cash.

Members of the Board

Members of the Board who served during the year were Raymond Ch'ien Kuo-fung (non-executive Chairman), Chow Chung-kong (Chief Executive Officer), Cheung Yau-kai, David Gordon Eldon, Christine Fang Meng-sang (appointed

on 1 January 2004), Edward Ho Sing-tin, Lo Chung-hing, T. Brian Stevenson, Frederick Ma Si-hang, the Secretary for the Environment, Transport and Works (Sarah Liao Sau-tung) and the Commissioner for Transport (Robert Charles Law Footman).

At the Annual General Meeting on 3 June 2004 and pursuant to the articles of association of the Company ("the Articles of Association"), Raymond Ch'ien Kuo-fung, Chow Chung-kong, David Gordon Eldon and Christine Fang Meng-sang retired under the Articles of Association and were re-elected as members of the Board.

At the forthcoming Annual General Meeting and in accordance with the Articles of Association, Cheung Yau-kai, Edward Ho Sing-tin and Lo Chung-hing will retire by rotation. All these three Board members will offer themselves for re-election at the forthcoming Annual General Meeting.

Brief biographical details for Board members are set out on pages 16 and 17.

Alternate Directors

The Alternate Directors in office during the year were (i) Martin McKenzie Glass and Alan Lai Nin (both for Frederick Ma Si-hang), (ii) both the Permanent Secretary for the Environment, Transport & Works (Rita Lau Ng Wai-lan [who ceased to be the Permanent Secretary for the Environment, Transport & Works with effect from 2 January 2004], Margaret Fong Shun-man [with effect from 1 July 2004 and ceased to be the Permanent Secretary for the Environment, Transport & Works with effect from 15 August 2004] and Joshua Law Chi-kong [with effect from 23 August 2004]) and the Deputy Secretary for the Environment, Transport & Works (Arthur Ho Kin-wah [who ceased to be a Deputy Secretary for the Environment, Transport & Works with effect from 15 November 2004], Margaret Fong Shun-man [who ceased to be a Deputy Secretary for the Environment, Transport & Works with effect from 1 July 2004], Patrick Ho Chung-kei [with effect from 1 July 2004], Thomas Chow Tat-ming [with effect from 1 July 2004], Cathy Chu Man-ling [with effect from 15 November 2004] and Annie Choi Suk-han) (for the Secretary for the Environment, Transport & Works), and (iii) the Deputy Commissioner for Transport/Transport Services and Management (Judy Li Wu Wai-lok) (for the Commissioner for Transport).

Executive Directorate

The members of the Executive Directorate who served during the year were Chow Chung-kong (Chief Executive Officer and a member of the Board), Russell John Black, William Chan Fu-keung, Philip Gaffney, Thomas Ho Hang-kwong, Lincoln Leong Kwok-kuen and Leonard Bryan Turk.

Brief biographical details for members of the Executive Directorate during the year are set out on page 17.

Corporate Governance

The Company is committed to ensuring high standards of corporate governance in the interests of shareholders and devotes considerable effort to identifying and formalising best practices.

The Board of Directors

The overall management of the Company's business is vested in the Board of Directors (the "Board"). Pursuant to the Articles of Association and the Protocol adopted by the Board, the Board has delegated the day-to-day management of the Company's business to the Executive Directorate, and focuses its attention on matters affecting the Company's overall strategic policies,

finances and shareholders. These include financial statements, dividend policy, significant changes in accounting policy, the annual operating budget, certain material contracts, strategies for future growth, major financing arrangements and major investments, risk management strategies, treasury policies and fare structures.

The Board comprises eleven members, consisting of one executive Director (the Chief Executive Officer) and ten non-executive Directors, of which six are independent non-executive Directors. Following the Board's decision to split the roles of Chairman and Chief Executive Officer, Dr. Raymond Ch'ien Kuo-fung, already a member of the Board, was appointed non-executive Chairman for three years with effect from 21 July 2003, and Mr. Chow Chung-kong was appointed Chief Executive Officer and a member of the Board on 1 December 2003. Two of the other non-executive Directors (being the Secretary for the Environment, Transport and Works and the Commissioner for Transport) are appointed by the Chief Executive of The Hong Kong Special Administrative Region of the People's Republic of China ("HKSAR"). Another non-executive Director, Mr. Frederick Ma Si-hang, is the Secretary for Financial Services and the Treasury of the Government of the HKSAR. The Government of the HKSAR through The Financial Secretary Incorporated, holds approximately 76% of the issued share capital of the Company. Coming from diverse business and professional backgrounds, the non-executive Directors actively bring their valuable experience to the Board for promoting the best interests of the Company and its shareholders. On the other hand, independent non-executive Directors contribute to ensuring that interests of all shareholders of the Company are taken into account by the Board and that relevant issues are subjected to objective and dispassionate consideration by the Board. The Company has received confirmation from each independent non-executive Director about his/her independence under The Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"), and continues to consider each of them to be independent. None of the Directors or members of the Executive Directorate is related to each other.

The posts of Chairman and Chief Executive Officer are distinct and separate. The non-executive Chairman is responsible for chairing and managing the operations of the Board, as well as monitoring the performance of the Chief Executive Officer and members of the Executive Directorate. Apart from ensuring adequate information about the Company's business is provided to the Board on a timely basis, the Chairman also facilitates effective contribution of non-executive Directors at Board meetings. As head of the Executive Directorate, the Chief Executive Officer is responsible to the Board for managing the business of the Company.

The Board meets in person regularly, and all members of the Board have full and timely access to relevant information and may take independent professional advice, if necessary. In year 2004, the Board held eight meetings, of which the possible merger between the Company and Kowloon-Canton Railway Corporation ("KCRC") was discussed at seven meetings by members of the Board who did not have conflicts of interest. In addition, two meetings solely on the possible merger were held during the year by those members who did not have conflicts of interest.

A person may be appointed as a member of the Board at any time either by the shareholders in general meeting or by the Board upon recommendation of the Nominations Committee. Directors who are appointed by the Board must retire at the first annual general meeting after their appointment. In either case, the Directors so elected and appointed are eligible for re-election and re-appointment. At each annual general meeting of the Company, one third of the Directors (or such number as is nearest to and less than one third) are required to retire from office by rotation.

The Chief Executive of the HKSAR may, pursuant to Section 8 of the Mass Transit Railway Ordinance ("MTR Ordinance"), appoint up to three persons as "additional directors". Unless the Chief Executive of the HKSAR otherwise directs, the Directors appointed in this way may not be removed from office and they are not subject to any requirement to retire by rotation stated in the preceding paragraph. In all other respects, "additional directors" are treated for all purposes in the same way as other Directors. The Chief Executive has appointed the Office for the Secretary for Environment, Transport and Works and the Office for Commissioner for Transport as "additional directors".

Each of the Directors, on appointment to the Board, is given a comprehensive induction program on key areas of business operations and practices of the Company, as well as a Directors' Manual. Amongst other things, the Manual not only sets out general and specific duties of Directors under general law (common law and legislation) and the Listing Rules, but also the Terms of Reference of Board Committees. The Directors' Manuals are updated from time to time to reflect developments in those areas.

Board Committees

As an integral part of good corporate governance, the Board have established the following Board Committees to oversee particular aspects of the Company's affairs. Each of these Committees comprise entirely non-executive Directors who have been invited to serve as members. The Committees are governed by their respective Terms of Reference.

Audit Committee

The Audit Committee consists of three non-executive Directors, two of whom are independent non-executive Directors. The members of the Committee are T. Brian Stevenson (chairman), Professor Cheung Yau-kai and the Commissioner for Transport (Robert Charles Law Footman). The Finance Director, the Head of Internal Audit Department and representatives of the external auditors of the Company are expected to attend meetings of the Committee. At the discretion of the Committee, others may also be invited to attend meetings. The Committee normally meets four times a year, and the external auditors or the Finance Director may request a meeting if they consider it necessary.

The duties of the Audit Committee include financial and efficiency aspects. Amongst other things, the Committee reviews the truth and fairness of the Group's annual and interim financial statements, and discusses with the external auditors the nature and scope of audit before the audit commences. It also reviews and approves non-audit services. The Audit Committee conducts an assessment, at least annually, of the effectiveness of the Company's systems of internal control. These systems allow the Board to monitor the Company's overall financial position and to protect its assets. In addition, the Committee reviews the internal audit function. The Audit Committee selects, in consultation with the Chairman and Members of Executive Directorate (or otherwise to approve) any topic to be the subject of an audit into the efficiency, effectiveness or value for money of any of the activities or operations of the Company. It then reviews reports of such audit and puts forward recommendations to the Board. The chairman of the Committee summarizes activities of the Committee for the year and highlights issues arising therefrom in a report to the Board.

In year 2004, the Audit Committee held four meetings. Representatives of the external auditors, the Finance Director and the Head of Internal Audit Department attended all those meetings for reporting and answering questions about their work. Further to that and by invitation, Managing Director – Operations and Business Development and Property Director had respectively provided an overview of the Company's railway operations and property business to the members at a meeting.

Remuneration Committee

The Remuneration Committee consists of three non-executive Directors, two of whom are independent non-executive Directors. The members of the Remuneration Committee are Edward Ho Sing-tin (chairman), T. Brian Stevenson and Frederick Ma Si-hang. The Remuneration Committee makes recommendation to the Board on executive Directors' remuneration packages and terms of employment. The Committee also determines relevant remuneration policy for executive Directors and their participation in incentive schemes operated by the Company. In 2004, the Remuneration Committee held two meetings.

Nominations Committee

The Nominations Committee consists of three non-executive Directors, two of whom are independent non-executive Directors. The members of the Nominations Committee are David Gordon Eldon (chairman), Lo Chung-hing and the Secretary for the Environment, Transport and Works (Dr. Sarah Liao Sau-tung). The Nominations Committee nominates and recommends to the Board candidates for filling vacancies on the Board. The Committee held no meeting in year 2004.

Independent Committee

The Board is committed to looking after the interests of independent shareholders of the Company, and for this purpose, an independent committee of the Board (the "Independent Committee"), chaired by Edward Ho Sing-tin, together with Professor Cheung Yau-kai, Christine Fang Meng-sang, Lo Chung-hing and T. Brian Stevenson, has been established to consider and review terms of any possible merger between the Company and KCRC, and advise independent shareholders whether they are fair and reasonable. All members of the Independent Committee are independent non-executive Directors of the Company.

Code of Best Practice

The Company has complied throughout the year with the Code of Best Practice set out in Appendix 14 to the Listing Rules except that non-executive Directors of the Company are not appointed for a specific term but are subject (save for those appointed pursuant to Section 8 of the MTR Ordinance) to retirement by rotation and re-election at the Company's annual general meetings in accordance with Articles 87 and 88 of the Articles of Association. Dr. Raymond Ch'ien Kuo-fung, a member of the Board, was appointed as the non-executive Chairman of the Company with effect from 21 July 2003 for a term of three years.

Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code")

The Company, having made specific enquiry, confirms that members of the Board and the Executive Directorate complied throughout the year with the Model Code set out in Appendix 10 to the Listing Rules. Senior managers who, because of their office in the Company, are likely to be in possession of unpublished price sensitive information, have been requested to comply with the provisions of the Model Code.

U.S. Sarbanes-Oxley Act 2002

This legislation, which seeks to enhance the transparency and accountability of companies in the areas of corporate governance and financial reporting, was signed into law by the President of the United States on 30 July 2002.

As the Company is a U.S. Securities and Exchange Commission reporting company, it is generally bound by this legislation.

The Company has been, and will continue its process of, reviewing its internal systems and practices and implementing new requirements under this legislation in line with applicable compliance dates.

Internal Audit

The Company's Internal Audit Department provides independent, objective assurance and consulting services designed to add value and improve the Company's operations. Key responsibilities of the Department include:

- > Assessments on the adequacy and effectiveness of the Company's system of internal control for controlling its activities and managing its risks.
- > Identification of opportunities for improving management control, resources utilisation and profitability.
- > Special reviews and/or investigations as commissioned by Company management.

The Company's Internal Auditor reports directly to the Chief Executive Officer and has direct access to the Audit Committee.

Business Ethics

The Company is committed to a high standard of business ethics and integrity.

The 2002 Code of Conduct on the ethical and behavioral framework for all staff was reviewed and reissued to all staff in June 2004 to align it with the latest developments in corporate governance standards, including corporate governance standards under the Sarbanes-Oxley Act of 2002. A new "Corporate Guidebook for All Staff on Code of Conduct" was issued to all staff at the same time. The Guidebook provides specific guidelines for employees in respect of behaviour within and outside the workplace. Communication sessions were held to brief employees on the changes in the Code of Conduct and the contents of the new Corporate Guidebook.

Policies

The Board has adopted risk management strategies on the following matters:

- A Construction and insurance;
- B Finance;
- C Treasury risk management;
- D Safety risk management;
- E Security management.

No changes to such policies may be made without the approval of the Board.

Summary Financial Statements

The state of affairs of the Group as at 31 December 2004 and of its results for the year are set out in the summary financial statements on pages 24 to 30.

Ten-Year Statistics

A summary of the results and of the assets and liabilities of the Group together with some major operational statistics for the last ten years are set out on pages 14 and 15.

Fixed Assets and Railway Construction in Progress

Movements in fixed assets and railway construction in progress during the year are set out in notes 4A and 4B to the summary financial statements respectively.

Movements in Reserves

Movements in reserves during the year are set out in note 6 to the summary financial statements.

Share Capital

As at 31 December 2003, the authorised share capital of the Company was HK\$6.5 billion, divided into 6.5 billion Ordinary Shares, 5,288,695,393 of which were issued and credited as fully paid. During the year, the Company issued a total of 101,304,581 Ordinary Shares. Of this number:

A 8,023,500 Ordinary Shares were issued by the Company pursuant to the exercise of share options which had been granted under the Company's Pre-Global Offering Share Option Scheme. In respect of each Ordinary Share issued, the relevant exercising share option holder paid HK\$8.44 to the Company;

B 62,069,342 Ordinary Shares were issued by the Company in order to satisfy shareholders' scrip dividend elections in respect of the final dividend of the Company for the year ended 31 December 2003 (for which the cash dividend was HK\$0.28 per Ordinary Share); and

C 31,211,739 Ordinary Shares were issued by the Company in order to satisfy shareholders' scrip dividend elections in respect of the interim dividend of the Company for the six months ended 30 June 2004 (for which the cash dividend was HK\$0.14 per Ordinary Share).

As at 31 December 2004, the authorised share capital of the Company was HK\$6.5 billion, divided into 6.5 billion Ordinary Shares, 5,389,999,974 of which were issued and credited as fully paid.

Redemption of Listed Securities

Neither the Company nor any of its subsidiaries purchased, sold or redeemed any of its listed securities during the financial year 2004.

Donations

During the year, the Company donated a total of HK\$581,724 to charitable organisations, out of which HK\$381,724 went to the Community Chest of Hong Kong for the Community Chest Green Day. The remaining HK\$200,000 raised from the launching ceremony of the Doraemon MTR Souvenir Ticket went to the Kelly Chen Children Education Fund Limited.

Internal Control

The Board is responsible for ensuring that there is in place a satisfactory system of internal control. The main objectives are to ensure adherence to management policies, the safeguarding of assets, the efficiency and effectiveness of operation, the prevention and detection of fraud and error, the accuracy and completeness of the accounting records, and the timely preparation of reliable financial information.

A function of the Audit Committee is to review the effectiveness of the system of internal control from information provided by the Executive Directorate and management of the Company and by the auditors.

Reporting and Monitoring

There is a comprehensive budgeting system for all operational and business activities, with an annual budget approved by the Board. Monthly results of the Company's operations, businesses and projects are reported against the budget to the Board and updated forecasts for the year are prepared regularly.

Treasury Management

The Company's Treasury Department operates within approved guidelines from the Board. It manages the Company's debt profile with reference to the Preferred Financing Model which defines the preferred mix of financing instruments, fixed and floating rate debts, maturities, interest rate risks, currency exposure and financing horizon. The model is reviewed and refined periodically to reflect changes in the Company's financing requirements and market environment. Derivative financial instruments such as interest rate swaps and cross currency swaps are used only as hedging tools to manage the Group's interest rate and currency risks. Prudent guidelines and procedures are in place to control the Company's derivatives activities, including a comprehensive credit risk management system for monitoring counterparty credit exposure using the Value-at-Risk approach. There is also appropriate segregation of duties within the Company's Treasury Department.

Major financing transactions and guidelines for derivatives transactions including credit risk management framework are approved at the Board level.

Capital and Revenue Expenditure

There are defined procedures for the appraisal, review and approval of major capital and revenue expenditures. All project expenditure over 0.2% of the net assets of the Company and the employment of consultancy services over 0.1% of the net assets of the Company require the approval of the Board.

Bonds and Notes Issued

The Group issued bonds and notes during the year ended 31 December 2004, details of which are set out in note 5 to the summary financial statements. Such bonds and notes were issued in order to meet the Group's general corporate funding requirements, including the financing of new capital expenditure and the refinancing of maturing debts.

Computer Processing

There are defined procedures and regular quality reviews on the operation of computer systems to ensure the accuracy and completeness of financial records and efficiency of data processing. The Company's computer centre operation and support has been certified under ISO 9001:2000. Disaster recovery rehearsal on critical applications is conducted annually.

Interests in Contracts of Members of the Board and the Executive Directorate

There was no contract of significance, to which the Company or any of its subsidiaries was a party and in which a member of the Board or a member of the Executive Directorate had a material interest (whether direct or indirect), which subsisted at the end of the year or at any time during the year.

Board Members' and Executive Directorate's Interests in Shares

As at 31 December 2004, the interests or short positions of the members of the Board and the Executive Directorate in the shares, underlying shares and debentures of the Company (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) as recorded in the register required to be kept under section 352 of the SFO or as otherwise notified to the Company and The Stock Exchange of Hong Kong Limited (the "HKSE") pursuant to the Model Code were as follows:

Long Positions in Shares and Underlying Shares of the Company

Member of the Board or Executive Directorate	Number of Ordinary Shares held			Derivatives		Total interests	Percentage of aggregate interests to total issued share capital
	Personal* interests	Family† interests	Corporate interests	Share Options	Other		
Chow Chung-kong	–	–	–	–	700,000 (Note 1)	700,000	0.01299
T. Brian Stevenson	4,443	–	–	–	–	4,443	0.00008
Christine Fang Meng-sang	1,675	–	–	–	–	1,675	0.00003
Philip Gaffney	46,553	614	–	416,000 (Note 2)	–	463,167	0.00859
Russell John Black	51,132	–	–	–	–	51,132	0.00095
William Chan Fu-keung	46,233	–	–	317,500 (Note 2)	–	363,733	0.00675
Thomas Ho Hang-kwong	51,075	2,524	–	321,000 (Note 2)	–	374,599	0.00695
Lincoln Leong Kwok-kuen	–	–	23,000 (Note 3)	1,066,000 (Note 4)	–	1,089,000	0.02020

Notes

- Chow Chung-kong has a derivative interest in respect of 700,000 shares in the Company within the meaning of Part XV of the SFO. That derivative interest represents Mr. Chow's entitlement to receive 700,000 shares in the Company (or their equivalent value in cash) on completion of his three-year contract (on 30 November 2006).
- Further details of the above share options are set out in the table below showing details of the options to subscribe for ordinary shares granted under the Pre-Global Offering Share Option Scheme.
- The 23,000 shares are held by Linsan Investment Ltd., a private limited company beneficially wholly owned by Lincoln Leong Kwok-kuen.
- Further details of the above share options are set out in the table below showing details of the options to subscribe for ordinary shares granted under the New Joiners Share Option Scheme.

Notes of MTR Corporation (C.I.) Limited

Member of the Executive Directorate	Personal interests*
William Chan Fu-keung	HK\$50,000 MTR 301 4.50% Notes due 2005

* Interests as beneficial owner

† Interests of spouse or child under 18 as beneficial owner

Options to subscribe for Ordinary Shares granted under the Pre-Global Offering Share Option Scheme, as referred to in Note 2B (i) to the summary financial statements

Executive Directorate and eligible employees	Date granted	No. of options granted	Period during which rights exercisable (day/month/year)	Options outstanding as at 1 January 2004	Options vested during the year	Options lapsed during the year	Options exercised during the year	Price per share paid on exercise of options (HK\$)	Options outstanding as at 31 December 2004	Weighted average closing price of shares immediately before the date(s) on which options were exercised (HK\$)
Philip Gaffney	20/9/2000	1,066,000	5/4/2001 – 11/9/2010	1,022,000	–	–	606,000	8.44	416,000	11.80
William Chan Fu-keung	20/9/2000	1,066,000	5/4/2001 – 11/9/2010	822,000	–	–	504,500	8.44	317,500	12.14
Thomas Ho Hang-kwong	20/9/2000	1,066,000	5/4/2001 – 11/9/2010	621,000	–	–	300,000	8.44	321,000	12.25
Other eligible employees	20/9/2000	40,343,000	5/4/2001 – 11/9/2010	22,764,500	–	–	6,613,000	8.44	16,151,500	12.00

Notes

- The Pre-Global Offering Share Option Scheme ("Pre-IPO Option Scheme") shall be valid and effective for a period of ten years after the adoption of the Pre-IPO Option Scheme on 12 September 2000. No option may be offered to be granted on or after the commencement of dealings in shares of the Company on HKSE on 5 October 2000.
- The number of shares to which the option granted to each participant under the Pre-IPO Option Scheme does not exceed 25% of the number of the shares issued and issuable under the Pre-IPO Option Scheme.

Options to subscribe for Ordinary Shares granted under the New Joiners Share Option Scheme, as referred to in Note 2B (ii) to the summary financial statements

Executive Directorate and eligible employees	Date granted	No. of options granted	Period during which rights exercisable (day/month/year)	Options outstanding as at 1 January 2004	Options vested during the year	Options lapsed during the year	Options exercised during the year	Price per share paid on exercise of options (HK\$)	Options outstanding as at 31 December 2004	Weighted average closing price of shares immediately before the date(s) on which options were exercised (HK\$)
Lincoln Leong Kwok-kuen	1/8/2003	1,066,000	14/7/2004 – 14/7/2013	1,066,000	355,500	–	–	–	1,066,000	–
Other eligible employees	1/8/2003	495,200	14/7/2004 – 14/7/2013	495,200	165,500	–	–	–	495,200	–

Notes

1. No option may be exercised later than ten years after its date of offer and no option may be offered to be granted more than five years after the adoption of the New Joiners Share Option Scheme ("New Option Scheme") on 16 May 2002.

2. Unless approved by shareholders in the manner as required by the Listing Rules, the total number of shares issued and issuable upon exercise of the options granted to any eligible employee under the New Option Scheme together with the total number of shares issued and issuable upon the exercise of any option granted to such eligible employee under any other share option scheme of the Company (including, in each case, both exercised and outstanding options) in any 12-month period must not exceed 1% of the shares of the Company in issue at the date of offer in respect of such option under the New Option Scheme.

Save as disclosed above:

A none of the members of the Board or Executive Directorate of the Company had any interest or short position in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO); and

B during the year ended 31 December 2004, no member of the Board or Executive Directorate nor any of their spouses or children under 18 years of age held any rights to subscribe for equity or debt securities of the Company nor had there been any exercises of any such rights by any of them,

as recorded in the register kept by the Company under section 352 of the SFO or otherwise notified to the Company and the HKSE pursuant to the Model Code.

Substantial Shareholders' Interests

Set out below is the name of the party which was interested in 5% or more of the nominal value of the share capital of the Company and the respective relevant numbers of shares in which it was interested as at 31 December 2004 as recorded in the register kept by the Company under section 336 of the SFO:

Name	No. of Ordinary Shares	Percentage of Ordinary Shares to total issued share capital
The Financial Secretary Incorporated (in trust on behalf of the Government)	4,121,262,921	76.46

The Company has been informed by the Government that, as at 31 December 2004, approximately 1.37% of the shares of the Company were held for the account of the Exchange Fund. The Exchange Fund is a fund established under the Exchange Fund Ordinance (Cap. 66 of the laws of Hong Kong) under the control of the Financial Secretary.

Major Suppliers and Customers

Less than 30% in value of supplies (which were not of a capital nature) purchased during the year ended 31 December 2004 was attributable to the Company's five largest suppliers. Less than 30% in value of the Company's turnover during the year ended 31 December 2004 was attributable to the Company's five largest customers combined by value.

Going Concern

The summary financial statements on pages 24 to 30 have been prepared on a going concern basis. The Board has reviewed the Company's budget for 2005, together with the longer-term forecast for the following five years and is satisfied that the Company has sufficient resources to continue as a going concern for the foreseeable future.

By order of the Board

Leonard Bryan Turk
Secretary to the Board
Hong Kong, 1 March 2005

Consolidated profit and loss account

for the year ended 31 December in HK\$ million	2004	2003
Fare revenue	5,932	5,489
Station commercial and other revenue	1,311	1,117
Rental and management income	1,108	988
Turnover	8,351	7,594
Staff costs and related expenses	(1,542)	(1,643)
Energy and utilities	(544)	(546)
Operational rent and rates	(70)	(21)
Stores and spares consumed	(128)	(128)
Repairs and maintenance	(517)	(477)
Railway support services	(72)	(80)
Expenses relating to station commercial and other businesses	(315)	(351)
Property ownership and management expenses	(207)	(198)
Project study and business development expenses	(167)	(49)
General and administration expenses	(167)	(167)
Other expenses	(76)	(187)
Operating expenses before depreciation	(3,805)	(3,847)
Operating profit from railway and related operations before depreciation	4,546	3,747
Profit on property developments	4,568	5,369
Operating profit before depreciation	9,114	9,116
Depreciation	(2,512)	(2,402)
Operating profit before interest and finance charges	6,602	6,714
Interest and finance charges	(1,450)	(1,539)
Share of profit of non-controlled subsidiary	44	23
Profit before taxation	5,196	5,198
Income tax	(700)	(748)
Profit attributable to shareholders	4,496	4,450
Dividends		
Interim dividend declared and paid during the year	750	734
Final dividend proposed after the balance sheet date	1,509	1,481
	2,259	2,215
Earnings per share:		
– Basic	HK\$0.84	HK\$0.85
– Diluted	HK\$0.84	HK\$0.85

Consolidated balance sheet

at 31 December in HK\$ million

	2004	2003
Assets		
Fixed assets		
– Investment properties	16,687	14,169
– Other property, plant and equipment	83,626	82,752
	100,313	96,921
Railway construction in progress	962	181
Property development in progress	2,088	2,309
Deferred expenditure	243	104
Interest in non-controlled subsidiary	63	110
Deferred tax assets	15	–
Investments in held-to-maturity securities	202	–
Staff housing loans	47	67
Properties held for sale	815	812
Stores and spares	248	249
Debtors, deposits and payments in advance	1,276	1,153
Amounts due from the Government and other related parties	133	84
Cash and cash equivalents	269	376
	106,674	102,366
Liabilities		
Bank overdrafts	11	12
Short-term loans	–	353
Creditors, accrued charges and provisions	3,034	3,420
Current taxation	3	2
Contract retentions	240	311
Amounts due to the Government and other related parties	1	161
Loans and obligations under finance leases	30,367	31,660
Deferred liabilities	109	86
Deferred income	4,638	5,061
Deferred tax liabilities	4,764	4,000
	43,167	45,066
Minority interests	8	8
Net assets	63,499	57,292
Shareholders' funds		
Share capital, share premium and capital reserve	36,269	35,086
Other reserves	27,230	22,206
	63,499	57,292

Approved and authorised for issue by the Members of the Board on 1 March 2005

Raymond K F Ch'ien

C K Chow

Lincoln K K Leong

Notes to the summary financial statements

1 Significant accounting policies

This summary financial statements have been prepared from the audited financial statements of the Company and all its subsidiaries (the "Group") for the year ended 31 December 2004.

The same accounting policies adopted in the 2003 annual accounts have been consistently applied.

2 Remuneration of Members of the Board and the Executive Directorate

A Remuneration of Members of the Board and the Executive Directorate

(i) The aggregate emoluments of the Members of the Board and the Executive Directorate of the Company disclosed pursuant to section 161 of the Hong Kong Companies Ordinance were as follows:

<i>in HK\$ million</i>	2004	2003
Fees	3	2
Salaries, housing allowances and other benefits-in-kind	28	28
Variable remuneration related to performance	8	3
Retirement scheme contributions	3	4
	42	37

The above emoluments do not include realised gains on exercise of share options amounting to HK\$5.1 million (2003: HK\$8.7 million) in respect of certain Members of the Executive Directorate, which are disclosed under the paragraph "Board Members and Executive Directorate's Interest in Shares" of the Report of the Members of the Board.

Non-executive directors of the Company are not appointed for a specific term but are subject (save as those appointed pursuant to Section 8 of the Mass Transit Railway Ordinance (Chapter 556 of the Laws of Hong Kong)) to retirement by rotation and re-election at the Company's annual general meetings in accordance with Articles 87 and 88 of the Company's Articles of Association.

(ii) The gross emoluments (excluding share option benefit) of the Members of the Board and the Members of the Executive Directorate were within the following bands:

Emoluments	2004 Number	2003 Number
HK\$0 – HK\$500,000	9	8
HK\$500,001 – HK\$1,000,000	1	2
HK\$4,000,001 – HK\$4,500,000	–	3
HK\$4,500,001 – HK\$5,000,000	4	2
HK\$5,000,001 – HK\$5,500,000	2	1
HK\$6,000,001 – HK\$6,500,000	–	1
HK\$9,000,001 – HK\$9,500,000	1	–
	17	17

The information shown in the above table includes the five highest paid employees. The independent non-executive directors' emoluments are included in the first remuneration band except the non-executive Chairman, whose emolument is included in the second remuneration band. Emolument of the ex-Chairman, Jack C K So who resigned on 20 July 2003, is included under the highest remuneration band in 2003.

2 Remuneration of Members of the Board and the Executive Directorate (continued)

(iii) The remuneration details (excluding share option benefit) of the current members of the Executive Directorate are shown below:

<i>in HK\$ million</i>	2004		2003	
	Base pay, allowance, retirement scheme contribution and other benefits	Variable remuneration related to performance	Total	Total
Chief Executive Officer ("CEO")*	5.61	3.44	9.05	0.68
Finance Director	3.89	0.75	4.64	4.30
Human Resources Director	4.11	0.75	4.86	4.45
Legal Director and Secretary	4.26	0.75	5.01	4.67
Managing Director – Operations & Business Development	4.50	0.81	5.31	5.11
Project Director	4.10	0.77	4.87	4.65
Property Director	4.10	0.75	4.85	4.46
	30.57	8.02	38.59	28.32

* Appointed in December 2003

(iv) The CEO will be entitled to receive 700,000 shares in the Company (or their equivalent value in cash) on completion of his three-year contract (i.e. 30 November 2006). The final number of shares (or cash amount) delivered may be adjusted to reflect relevant changes (if any) in the Company's share capital after his appointment in order that the CEO's compensation is closely tied to the Company's longer-term performance and aligns his interests with those of shareholders. In certain limited circumstances, the CEO may be entitled to receive some or all of the shares (or the cash amount) prior to completion of his contract.

The restricted shares were offered in order to provide a competitive level of compensation and to enable the CEO's total pay to be closely tied to the performance of the Company.

B Share options

Options exercised and outstanding in respect of each Member of the Executive Directorate as at 31 December 2004 are set out under the paragraph "Board Members and Executive Directorate's Interest in Shares" of the Report of the Members of the Board. Details of the options granted to Members of the Executive Directorate are as follows:

(i) Pre-Global Offering Share Option Scheme

Under the Company's Pre-Global Offering Share Option Scheme ("Pre-IPO Option Scheme"), Jack C K So (ex-Chairman) and each of the other Members of the Executive Directorate, except C K Chow and Lincoln K K Leong, were granted options on 20 September 2000 to acquire 1,599,000 and 1,066,000 shares respectively. C K Chow and Lincoln K K Leong joined the Company on 1 December 2003 and 1 February 2002 respectively and are not beneficiaries of the Pre-IPO Option Scheme.

Under the vesting terms of the Pre-IPO Option Scheme, each eligible Member of the Executive Directorate must continue to beneficially own (i) at all times after 26 October 2001, at least 40,000 shares in the case of the ex-Chairman and at least 23,000 shares in the case of other Members of the Executive Directorate; and (ii) at all times after 26 October 2002, at least 80,000 shares in the case of the ex-Chairman and at least 46,000 shares in the case of other Members of the Executive Directorate, in each case, up to and including the date on which he has exercised his option in full or the date on which his option lapses (whichever is earlier).

(ii) New Joiners Share Option Scheme

Under the New Joiners Share Option Scheme ("New Option Scheme"), Lincoln K K Leong, a Member of the Executive Directorate, was granted options to acquire 1,066,000 shares on 1 August 2003.

Under the vesting terms of the New Option Scheme, the grantee must continue to beneficially own (i) at all times on and after 4 August 2004, at least 23,000 shares; and (ii) at all times on and after 4 August 2005, at least 46,000 shares, up to and including the date on which he has exercised his option in full or the date on which his option lapses (whichever is earlier).

3 Segmental information

The results of major business activities are summarised below:

in HK\$ million	Turnover		Contribution to profit	
	2004	2003	2004	2003
Railway operations	5,932	5,489	674	345
Station commercial and other businesses	1,311	1,117	879	657
	7,243	6,606	1,553	1,002
Property ownership and management	1,108	988	897	786
	8,351	7,594	2,450	1,788
Property developments			4,568	5,369
			7,018	7,157
Unallocated corporate expenses			(1,866)	(1,982)
Share of profit of non-controlled subsidiary			44	23
Income tax			(700)	(748)
Profit for the year			4,496	4,450

No geographical analysis is shown as substantially all the principal activities of the Company and its subsidiaries are carried out in Hong Kong throughout the reporting periods.

4 Fixed assets and railway construction in progress

A Fixed assets

in HK\$ million	Investment properties	Leasehold land and buildings	Civil works	Plant and equipment	Assets under construction	Total
Cost or Valuation						
At 1 January 2004	14,169	1,598	45,740	54,319	940	116,766
Additions	32	–	–	49	3,245	3,326
Capitalisation adjustments*	–	–	(124)	(156)	–	(280)
Disposals / Write-offs	–	–	(1)	(172)	(4)	(177)
Surplus on revaluation (Note 6)	2,486	311	–	–	–	2,797
Write back of revaluation deficit	–	69	–	–	–	69
Reclassification	–	–	82	(82)	–	–
Other assets commissioned	–	–	7	1,123	(1,130)	–
At 31 December 2004	16,687	1,978	45,704	55,081	3,051	122,501
At Cost	–	732	45,704	55,081	3,051	104,568
At 31 December 2004 Valuation	16,687	1,246	–	–	–	17,933
Aggregate depreciation						
At 1 January 2004	–	98	2,705	17,042	–	19,845
Charge for the year	–	33	392	2,107	–	2,532
Capitalisation adjustments*	–	–	(3)	(17)	–	(20)
Written back on disposal	–	–	(1)	(148)	–	(149)
Written back on revaluation (Note 6)	–	(20)	–	–	–	(20)
At 31 December 2004	–	111	3,093	18,984	–	22,188
Net book value at 31 December 2004	16,687	1,867	42,611	36,097	3,051	100,313
Net book value at 31 December 2003	14,169	1,500	43,035	37,277	940	96,921

* Capitalisation adjustments relate to certain railway assets capitalised at time of commissioning based on contractors' claimed values. Such assets' final values have been adjusted downward following finalisation of contract claims with contractors at lower final contract values during the year.

Depreciation charge for the year was HK\$2,512 million, comprising depreciation for the year of HK\$2,532 million less adjustments for the capitalisation of HK\$20 million.

4 Fixed assets and railway construction in progress (continued)

B Railway construction in progress

<i>in HK\$ million</i>	Balance at 1 Jan 2004	Transferred from deferred expenditure	Expenditure/ (Government grant)	Costs written off to profit and loss account	Balance at 31 Dec 2004
Tseung Kwan O Extension Further Capital Works Project	44	–	12	(49)	7
Disneyland Resort Line Project	883	–	526	–	1,409
Government grant	(883)	–	(48)	–	(931)
	–	–	478	–	478
Tung Chung Cable Car Project	137	–	307	–	444
AsiaWorld-Expo Station Project	–	3	30	–	33
Total	181	3	827	(49)	962

Costs written off to profit and loss account relates to certain station design costs in respect of the future Tseung Kwan O South Station, which became abortive following the submission of a revised station design plan and its approval by the Town Planning Board during the year.

During the year, HK\$37 million (2003: HK\$675 million) cash dividends were waived by the Government. Such amount (2003: HK\$664 million), together with HK\$11 million (2003: Nil) brought forward from previous year, have been offset against the construction costs of Disneyland Resort Line Project (previously known as Penny's Bay Rail Link Project).

5 Bonds and notes issued and redeemed

Bonds and notes issued during the year ended 31 December 2003 and 2004 comprise:

<i>in HK\$ million</i>	2004		2003	
	Principal amount	Net consideration received	Principal amount	Net consideration received
Debt issuance programme notes	5,158	5,109	3,099	3,091

The net proceeds from the above issues were used for general working capital, refinancing or other corporate purposes.

During the year, the Group redeemed HK\$4,415 million (2003: HK\$500 million) unlisted Hong Kong dollar notes upon maturity.

None of the Group's listed debt securities was redeemed during the year ended 31 December 2004.

6 Reserves

<i>in HK\$ million</i>	Share premium	Capital reserve	Investment property revaluation reserve	Fixed asset revaluation reserve	Retained profits	Total
2004						
Balance as at 1 January 2004	2,609	27,188	6,682	18	15,506	52,003
Employee share options exercised	60	–	–	–	–	60
Shares issued under Scrip Dividend Schemes	1,022	–	–	–	–	1,022
Dividends paid	–	–	–	–	(2,231)	(2,231)
Surplus on revaluation (Note 4A), net of deferred tax	–	–	2,486	273	–	2,759
Profit for the year	–	–	–	–	4,496	4,496
Balance as at 31 December 2004	3,691	27,188	9,168	291	17,771	58,109
2003						
Balance as at 1 January 2003	1,563	27,188	6,406	24	13,234	48,415
Employee share options exercised	78	–	–	–	–	78
Shares issued under Scrip Dividend Schemes	968	–	–	–	–	968
Dividends paid	–	–	–	–	(2,178)	(2,178)
Surplus/(Deficits) on revaluation, net of deferred tax	–	–	276	(6)	–	270
Profit for the year	–	–	–	–	4,450	4,450
Balance as at 31 December 2003	2,609	27,188	6,682	18	15,506	52,003

7 Other information

This summary financial statements is only a summary of information in the Group's 2004 Annual Accounts. It is not the Group's statutory financial statements and it does not contain sufficient information to allow as full an understanding of the results and state of affairs of the Group as would be provided by the full Annual Report and Accounts. The full 2004 Annual Report is available in electronic form on the Company's website at www.mtr.com.hk. A printed copy of the 2004 Annual Report can be obtained free of charge by writing to the Company's share registrar or the Company's Corporate Relations Department. Their details are listed on page 32 of this Summary Report.

Auditors' statement on the summary financial report

To the shareholders of MTR Corporation Limited

(Incorporated in Hong Kong with limited liability)

We have examined the summary financial report of MTR Corporation Limited for the year ended 31 December 2004 on pages 1 to 30 and the front and back cover pages.

Respective responsibilities of directors and auditors

Under the Hong Kong Companies Ordinance, the directors are responsible for preparing the summary financial report which complies with section 141CF(1) of the Hong Kong Companies Ordinance. In preparing the summary financial report, section 141CF(1) of the Hong Kong Companies Ordinance requires that the summary financial report be derived from the annual accounts and the auditors' report thereon and the report of the Members of the Board for the year ended 31 December 2004, be in such form and contain such information and particulars as specified in section 5 of the Hong Kong Companies (Summary Financial Reports of Listed Companies) Regulation, and be approved by the board of directors.

It is our responsibility to form an independent opinion on the summary financial report, based on our examination, and to report our opinion solely to you, as a body, and we are also required to state whether the auditors' report on the annual accounts for the year ended 31 December 2004 is qualified or otherwise modified, in accordance with section 5 of the Hong Kong Companies (Summary Financial Reports of Listed Companies) Regulation, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this statement.

Basis of opinion

We conducted our engagement in accordance with Standards on Assurance Engagements and with reference to Practice Note 710 "The auditors' statement on the summary financial report" issued by the Hong Kong Institute of Certified Public Accountants. Our examination includes examining evidence supporting the consistency of the summary financial report with the annual accounts and the auditors' report thereon and the report of the Members of the Board for the year ended 31 December 2004, and the compliance of the summary financial report with the requirements of section 5 of the Hong Kong Companies (Summary Financial Reports of Listed Companies) Regulation, and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

Opinion

Based on the foregoing, in our opinion the summary financial report on pages 1 to 30 and the front and back cover pages:

- (a) is consistent with the annual accounts and the auditors' report thereon and the report of the Members of the Board of MTR Corporation Limited for the year ended 31 December 2004 from which it is derived; and
- (b) complies with the requirements of section 5 of the Hong Kong Companies (Summary Financial Reports of Listed Companies) Regulation.

We have audited the annual accounts of MTR Corporation Limited for the year ended 31 December 2004 and have issued an auditors' report thereon dated 1 March 2005 which is unqualified or otherwise unmodified.

KPMG

Certified Public Accountants

Hong Kong, 1 March 2005

Key shareholder information

Financial calendar 2005

Announcement of 2004 results	1 March
Last day to register for 2004 final dividend	22 March
Book closure period	23 March to 1 April
Annual General Meeting	2 June
2004 final dividend payment date	on or about 21 June
Announcement of 2005 interim results	August
2005 interim dividend payment date	October
Financial year end	31 December

Registered office

MTR Corporation Limited
MTR Tower, Telford Plaza, Kowloon Bay, Hong Kong
Telephone: (852) 2993 2111 Facsimile: (852) 2798 8822

Website

www.mtr.com.hk

Share information

Listing

MTR Corporation Limited's shares are listed on The Stock Exchange of Hong Kong. In addition, shares are traded in the United States through an American Depositary Receipt (ADR) Level 1 Programme sponsored by JP Morgan Chase Bank. The shares are also quoted on the London SEAQ International System.

Ordinary shares (as at 31 December 2004):

Shares outstanding: 5,389,999,974 shares
Hong Kong SAR Government shareholding: 4,121,262,921 shares (76.46%)
Free float: 1,268,737,053 shares (23.54%)

Nominal value HK\$1 per share
Market Capitalisation (as at 31 December 2004): HK\$67,105 million

Share price performance



Dividend Policy

Subject to the financial performance of the Company, we expect to pay two dividends each financial year with interim and final dividends payable around October and June respectively, with the interim dividend representing approximately one third of the total dividends to be paid for the entire year.

Dividend per share (in HK\$)

2003 Final Dividend	0.28
2004 Interim Dividend	0.14
2004 Final Dividend	0.28

ADR Level 1 Programme

Ordinary share to ADR ratio	10:1
Depository Bank	JP Morgan Chase Bank 40th Floor, One Chase Manhattan Plaza New York, NY 10081 USA

Index Constituent

MTR Corporation Limited is a constituent of the following indices:
Hang Seng Index Series
MSCI Index Series
FTSE All-World Hong Kong Index
FTSE4Good Global Index
Dow Jones Sustainability World Index

Stock codes

Ordinary Shares

The Stock Exchange of Hong Kong	66
Reuters	0066.HK
Bloomberg	66 HK
CUSIP Reference Number	Y5896Y104
Sedol Reference Number	6290054

ADR Level 1 Programme MTRJY

Annual report 2004

Our annual report is available in both English and Chinese. Shareholders can obtain copies by writing to:

Computershare Hong Kong Investor Services Limited
46th Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong

If you are not a shareholder, please write to:

Corporate Relations Department, MTR Corporation Limited
MTR Tower, Telford Plaza, Kowloon Bay, Hong Kong

Our annual/interim reports and accounts are also available online at our corporate website at www.mtr.com.hk

Shareholder services

Any matters relating to your shareholding, such as transfer of shares, change of name or address, and loss of share certificates should be addressed in writing to the Registrar:

Computershare Hong Kong Investor Services Limited, Shops 1712 -1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong
Telephone: (852) 2862 8628 Facsimile: (852) 2529 6087

Shareholder enquiries

Our enquiry hotline is operational during normal office hours:
Telephone: (852) 2881 8888

Investor relations

For enquiries from institutional investors and securities analysts, please contact:

Investor Relations Department, MTR Corporation Limited
MTR Tower, Telford Plaza, Kowloon Bay, Hong Kong
Email: investor@mtr.com.hk



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