



vision:
MTR - Hong Kong's
fast track to a
world class city

mission:
to develop and
manage a world
class railway
together with
property and other
related businesses,
to enhance the
quality of life in
Hong Kong

Dear Shareholders

MTR entered into a new era as a publicly listed company on 5 October 2000 when the trading of its shares commenced on The Stock Exchange of Hong Kong. With the successful initial public offering which attracted HK\$164 billion of strong institutional and retail demand from both Hong Kong and overseas for a HK\$9.4 billion offering, our Company went from being wholly-owned by Government to having over 600,000 shareholders at the time of listing. Government's shareholding interest is now 77%. It is pleasing that the market has continued to strongly support our shares since listing, with the share price closing the year at HK\$13.65, a 45% premium to the listing price.

We believe that the success of the listing bears testament to the high quality standards which we have established in all areas of our business. First and foremost, we have a well-trained and committed workforce which takes pride in our achievements. Our beliefs and commitment are reflected in our vision, our mission and our core values. Support from staff for the partial privatisation was important and I am pleased to see that the various share schemes implemented at the time of listing have further aligned their interests with those of our shareholders.

Unlike many newly privatised enterprises, MTR did not need to undergo a major transformation to become a listed company. Since

inception over 20 years ago, MTR has operated as a commercial entity with a dedicated professional management team. Our strict cost controls have enabled us to achieve a high level of operational efficiency and to complete all of our railway projects on time and within budget. Our careful financial management has enabled us to be regarded as one of Asia's premier issuers in the capital markets. These will be maintained as we develop our future business as a listed company. In addition, the listing has provided us with a clearer cost of capital and additional focus on creating shareholder value, thereby establishing the benchmark against which all our investment proposals must be measured. At the same time, we never forget that the root of our business comes from providing the Hong Kong travelling public with a safe, efficient and good value for money transport service.

To enable the partial privatisation to proceed, the new Mass Transit Railway Ordinance became effective on 30 June 2000 and on that day, we entered into the new Operating Agreement with Government for an initial period of 50 years. Under the new Ordinance, all of the property, rights and liabilities of Mass Transit Railway Corporation were vested into MTR Corporation Limited. The new regulatory framework has preserved and reinforced the key principles of operating the railway on a commercial basis, including the Company having the autonomy to set its own fares subject to our well-established consultation procedure and

the need to achieve a commercial rate of return on investments in new railway projects.

A unique business model

Over the years, MTR has created a successful and unique business model, deriving significant benefits from integrating our railway business with the development of substantial properties in conjunction with our railway stations and depots. Providing an efficient transport service has enhanced the attractiveness of properties situated at MTR stations. On the other hand, building communities along MTR lines has enhanced patronage and supplemented the return on our railway investments. Built on the foundations of our successful railway, property and other commercial businesses, we have gained access to a substantial proportion of Hong Kong's population, comprising an average of approximately 2.3 million passenger trips per weekday on the railway, approximately 170,000 residents living and working in properties managed by the MTR, approximately 160,000 visitors per day to our shopping centres and the holders of the 7.1 million Octopus contactless smart cards currently in issue.

We intend to provide further services and expand our commercial activities to enhance the lifestyle of our customers; our model "MTR person" is an individual who lives, works and shops in one of the MTR developments, commutes on the railway and uses the Octopus card. At the same time, we

will continue to expand the railway network by undertaking new extensions on the basis of a commercial rate of return, which Government has recognised would typically be calculated on the basis of our weighted average cost of capital plus a margin of 1-3%. New railway lines will also open up further opportunities for property development and commercial activities.

Progress made in 2000

In 2000, satisfactory progress was made in all areas of our business in pursuance of the strategies described above. Despite continued strong competition from other transport modes which contributed to a 2.6% year-on-year drop in patronage in the first half of the year, the trends improved in the second half, resulting in our total fare revenue increasing by 1.3% to HK\$5,715 million in 2000. With our continuing efforts to control costs and improve efficiency resulting in total operating costs decreasing by 2.6% from the previous year, our operating profit from railway and related operations before depreciation grew by 12% to HK\$3,912 million.

On the property side, all of the development packages along the Airport Railway have now been awarded to property developers. During the year, significant progress was made on the construction and pre-sales of certain Airport Railway developments which resulted in HK\$3,376 million of property development profits being recognised. We expect that earnings from property developments associated

with new railway extensions will continue to help counteract the effects of additional depreciation and interest charges arising from the large capital investment in new railway projects.

Our net profit for the year was HK\$4,055 million, an increase of 92% over the previous year's figure and comfortably above the profit forecast contained in the initial public offering prospectus. The Directors are proposing a final dividend of HK\$0.10 per share in respect of the approximately three months of the year during which the Company was listed.

Shareholders will be given an option to receive dividends in either cash or in scrip. Government has undertaken to elect for scrip for such amount as to ensure that no more than half of the total dividend will be paid in cash. We welcome this as it confirms Government's support for the Company and will increase our capital for future development.

Future opportunities

Looking ahead, we see exciting opportunities for the future growth of our Company. Construction of the Tseung Kwan O Extension is proceeding smoothly on schedule for completion in late 2002. Our partnership approach with contractors continues to achieve cost savings and the budget for this project was further reduced to HK\$21.0 billion from the original figure of HK\$30.5 billion. There will be

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a total of 2.3 million square metres of property development potential along this new line, of which the largest development will be the "Dream City" at the future depot site where our designs for an environmentally friendly city for 58,000 residents have already received widespread support.

Of significant long-term importance to us was Government's confirmation in its Railway Development Strategy 2000 (RDS-2000) published during the year that railways will form the backbone of the future transport system in Hong Kong. Further substantial development of the overall railway network will be required to serve the significant expected increase in Hong Kong's population, particularly as rail will provide substantial passenger capacity in an environmentally friendly manner. As a result, it is expected that the overall market share for rail will increase from the current 31% to 43% by the year 2016.

RDS-2000 has identified a number of new railway lines for priority development. Of these, the North Island Line and the West Island Line are natural extensions of the MTR system and will be built and operated by us. Lines which are not regarded as natural extensions will be offered for tender on a level playing field basis and we expect to make a strong proposal to construct and operate the Shatin to Central Link. The above projects will ensure continued

development opportunities for us up to and beyond 2010.

Recent data has indicated an improvement in patronage trends amidst continuing strong competition from buses and other modes of transport and we will continue to undertake initiatives to improve our ridership, including working with Government on transport planning, improving feeder services to MTR stations, creating a more lively environment in our stations and various promotional activities to attract patronage. We expect that our ridership will benefit from Hong Kong's growing population, increasing road congestion and the continuing build-up of communities along the Tung Chung Line. Discussions with Government on the Penny's Bay Rail Link to serve the future Disneyland Theme Park on Lantau Island are well advanced. This spur line will also increase ridership on the Tung Chung Line.

We are actively seeking to develop further commercial activities to enhance service to our very large customer base. The usage of the Octopus contactless smart card is being expanded to a wide range of non-transport as well as transport applications since Creative Star Limited, which is majority-owned by the Company, became authorised as a deposit-taking company in April 2000. We are always on the look out for new technologies in developing our commercial activities. Some recent examples include the creation of the Cybermall at Kowloon Station, the

provision of an Internet portal for our managed residential apartments and the use of interactive advertising in our stations such as the recently launched "e-instant bonus" product.

We continue to be mindful of overseas expansion opportunities, with many cities in Asia planning to develop urban railway systems. We have established our involvement with many of these projects through our railway consultancy business and expect an increasing trend of income from this source.

Underlying our development is a strong financial position with investment grade credit ratings at the Hong Kong sovereign ceiling and excellent access to the international capital markets. Reflecting the success of the initial public offering and the US\$600 million Global Bond issue this year, we have received numerous financing awards including *IFR Asia's* Borrower of the Year, *Asiamoney's* Issuer of the Year and a number of deal-specific awards.

Positive outlook

There are signs of continuing recovery in the Hong Kong economy, with GDP growth estimated at 10% for 2000 and the recent cut in interest rates expected to provide further impetus. With operating costs tightly under control and having already made substantial infrastructure investment, MTR will benefit from this

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economic growth through its high operating margins. Our property development business is also structured to mitigate downside risk but benefit from an upturn in the property market. The prospects of MTR are therefore regarded as being a good proxy for Hong Kong's economic growth.

Our objectives in the coming year will be focused on:

- improving ridership and market share
- developing the usage of Octopus and other commercial businesses associated with the railway
- delivery of the Tseung Kwan O Extension project on time and within budget
- establishing the foundations of our future project development particularly with respect to the railways identified in RDS-2000, tendering a strong bid for the proposed Shatin to Central Link as well as finalising the terms of the Penny's Bay Link
- commencing the tendering process for the Tseung Kwan O Extension property developments and ensuring

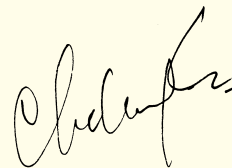
smooth delivery of the awarded Airport Railway developments

- continuing to be a leader in raising environmental awareness and promoting an improved environment in Hong Kong

We will continue to build the MTR as a dynamic, professional and innovative company operating to the

highest standards of ethics and integrity, putting emphasis on technology, professional development and preservation of the environment.

I am deeply grateful to my directors and staff for their commitment to our vision and for their hard work and I would like to thank our shareholders, financiers and business partners for their continued strong support.



Jack So Chak-kwong *Chairman*
Hong Kong, 1 March 2001