Economic recovery continued

Hong Kong's economic recovery gained momentum in 2000, posting an impressive GDP growth of 10.5% against 3.1% in 1999. Driven by continued increases in exports and re-exports, as well as further improvement in tourism, this strong growth was also supported by rising fixed investment on the back of infrastructure projects and e-commerce development. Meanwhile, revival in domestic consumption continued as employment conditions and the deflationary environment further improved. As at the year-end, the unemployment rate stood at 4.5%, down from 6% in the beginning of the year and the CPI was down 1.8% versus -4.0% for the previous year.

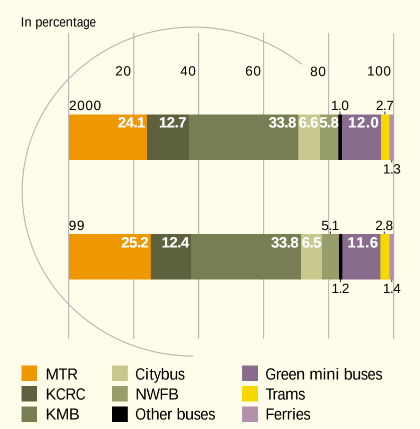
Hong Kong's foreign exchange reserves rose to the third highest in the world with US$107.5 billion by the year-end. During the year, the Hong Kong dollar was very stable and traded mostly on the strong side of the peg rate of 7.80 underpinned by the strong economic recovery and continued capital inflows. Hong Kong interest rates moved largely in tandem with those in the United States and high liquidity among banks further improved credit conditions with credit spreads for top-tier borrowers, such as MTR, returning to favourable pre-financial crisis levels.

Equity markets have been volatile with the new economy and technology stocks being hardest hit. The Hang Seng Index closed the year down 11% at 15,095 whilst the Growth Enterprise Market Index ended the year at 309, or approximately 70% off its peak recorded in March 2000. Despite the disappointing performance, the stock exchanges helped to raise a record HK$460 billion in equity during the year including the Company's highly successful HK$9.4 billion initial public offering by the SAR Government in October.

Government continued to implement its planned initiatives and reforms to develop Hong Kong as a knowledge-based economy and improve the environment to support its long-term goals for sustainable development. Projects such as the "Cyberport", Science Park and Disney Theme Park are in progress. To prevent further environmental deterioration, measures to improve air and water quality were introduced. To help consolidate Hong Kong's position as an international financial centre, the securities and futures exchanges were de-mutualised, merged and listed, and a link with the NASDAQ was established. Measures to reinforce the linked exchange rate system were implemented and a US dollar clearing system was put in place. The launching of the Mandatory Provident Fund scheme will also help to promote further development of the domestic capital market.

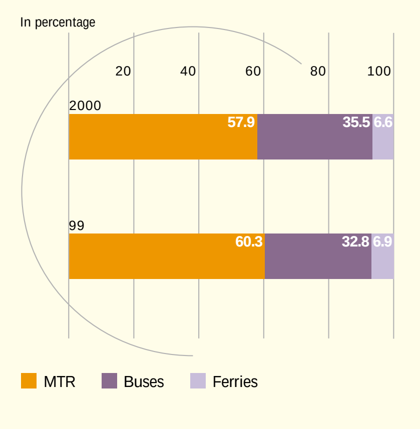
Looking ahead, Hong Kong's economic growth is expected to continue in 2001 albeit at a slower pace than in 2000. With China's imminent accession to the World Trade Organisation and its attendant economic and financial reforms, trade flows and capital investments will be boosted which will present unprecedented opportunities to Hong Kong as a gateway and service centre for China, providing the platform for Hong Kong's sustained growth and development in the coming years.

MARKET SHARES OF MAJOR TRANSPORT OPERATORS IN HONG KONG



Total public transport utilisation for 2000 was 3,971 million passengers of which 3,229 million were carried by the franchised transport operators.

MARKET SHARES OF TRANSPORT OPERATORS CROSSING THE HARBOUR



Reliability and value for money have helped the MTR retain a strong market share amongst the franchised operators for cross-harbour transport.

Transport strategy prioritises railway development

During the year, Government released the Railway Development Strategy 2000 (RDS-2000) which confirms priority for rail development over the next 15 years. RDS-2000 outlines Government's continued infrastructure initiatives to make Hong Kong a world-class city and regional business hub. It carries forward the proposals set out in the Third Comprehensive Transport Study (CTS-3) issued in late 1999, in which the broad strategy for long-term transport infrastructure was outlined. CTS-3 concluded that substantial new investment in infrastructure would be required to meet future population growth and travel demand. Rail transport, because of its high passenger capacity and low impact on the environment, was identified as the backbone for future Territory transport needs. Locating future population and employment growth centres in the vicinity of railway stations, with other modes of transport being used as feeder services to facilitate convenient access to rail stations, would be Government's objectives in its urban planning strategy. Other highlights from RDS-2000 include:

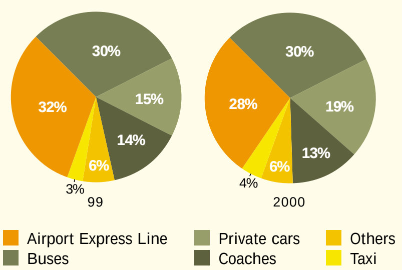
- Identification of six new rail corridors for new railway projects. The timing, award and sequence of these projects will be subject to feasibility studies. New lines forming natural extensions to existing lines will be granted to the relevant rail operators and independent lines will be publicly tendered and awarded on a level playing field basis.
- Enlargement of the rail network so that upon completion of the new rail corridors, about 70% of the population and about 80% of employment will be located within one kilometre of a railway station.
- Increase in the overall rail share of the public transport market to approximately 43% by 2016 from 31% currently. This is expected to reduce the reliance on road-based transport and translate into environmental benefits.

Amongst the new rail corridors identified under RDS-2000, the North Island Line and the West Island Line are considered natural extensions of the MTR system and will be undertaken by the Company, whilst the Shatin to Central Link (SCL) and the Regional Express Line (REL) will be opened to public tender by Government, with the SCL tender invitation announced in January 2001.

Transport market remains competitive

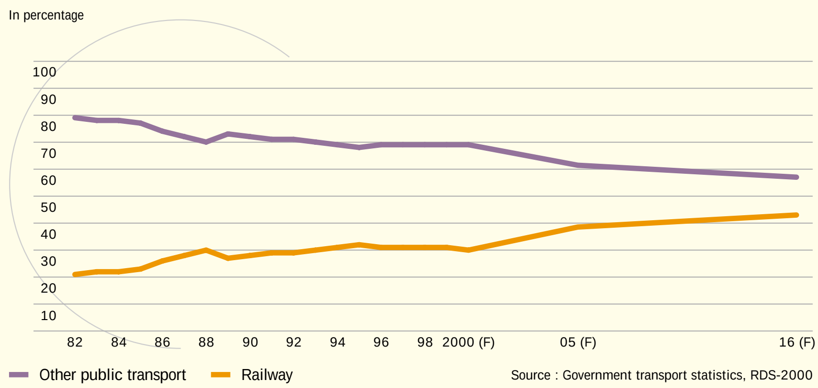
In line with the economic recovery the franchised public transport industry experienced a moderate growth of 2.6%. Total public transport demand for the year stood at 3,971 million passengers, up from 3,929 million in 1999 of which franchised operators carried 3,229 million. The franchised operators include the MTR, KCRC, buses, green mini-buses,

MARKET SHARES OF TRANSPORT OPERATORS TRAVELLING TO/FROM THE AIRPORT



Since opening in 1998 the Airport Express has remained a market leader amongst the franchised airport transport operators.

FORECAST OF FUTURE RAILWAY MARKET SHARE (1982 – 2016)



Under the RDS-2000 the overall railway market share of public transport is expected to increase to approximately 43%, an increase of some 12% over the next 15 years.

trams and ferries, with market shares of 24.1%, 12.7%, 47.2%, 12.0%, 2.7% and 1.3% respectively for 2000. Increases were captured mainly by the bus operators, with a cumulative 0.6% growth for the year while the MTR's market share dropped a marginal 1.1%.

Overseas tourist arrivals grew some 15.3% in 2000 with air passenger traffic increasing to 23.0 million from 21.3 million in 1999. Market share for the Airport Express Line (AEL) dropped from 32% to 28% mainly due to the effect of the reduction in AEL fare discounts in July 2000. A total of 10.3 million passengers used the AEL during the year.

The decline in the MTR's urban rail passenger boardings over the last four years is mainly a result of the economic recession and deflation, increased routes and enhanced services from franchised bus operators, the opening of the Western Harbour Tunnel and a general trend of less road congestion. These factors are increasingly being negated as the local economy improves and road congestion increases.

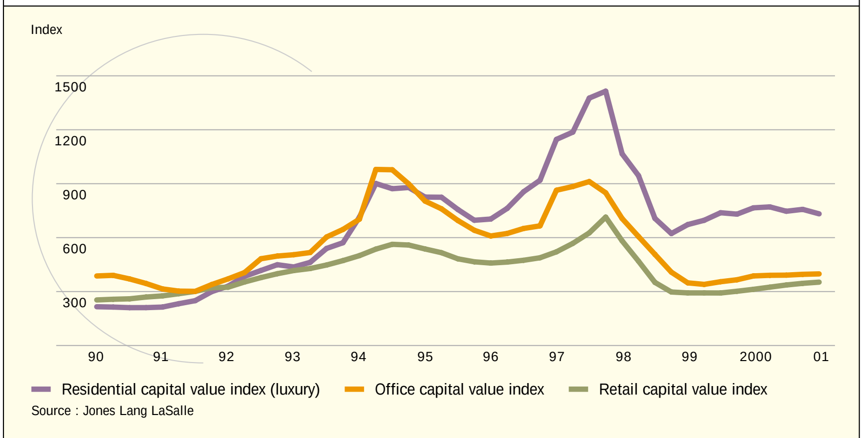
Sector improvements in the property market

The domestic property market remained fundamentally weak throughout the year with buyer confidence not having recovered despite tangible improvement in the general economy. In the mass-market sector, selected demand related to particular circumstances was noted, which however was not strong enough to lift the sector in general. Mortgage rates and lending remained highly competitive amongst banks, with some developers further assisting purchasers' financing. In spite of ample financing, the number of transactions remained at a 10-year low of 85,744 units. There were forecast to be about 27,000 new units completed in 2000 resulting in a significant supply overhang especially in less favoured areas. Despite the current over-supply situation in this sector, it is expected that the commensurate slowdown in new building starts will give rise to a more balanced situation in the next few years.

The luxury residential market sector for developments in favoured urban locations strengthened, notably towards the year-end, as limited supply coincided with an improvement in economic activity and increased foreign investment.

Prime location office property values and rentals rose sharply throughout the year due to strong demand for premium space from the expanding services sector and by the limited Grade A office supply anticipated over the next few years. Demand has been fuelled by multi-national companies expanding their presence in the region and using Hong Kong as their Asian headquarters and by China's anticipated accession to the World Trade Organisation in 2001.

TREND OF HONG KONG PROPERTY PRICES (1990 – 2000)



Prices in the various property sectors have recovered since bottoming in 1998.

state-of-the-art technology controls a network of 96 trains, moving through 44 stations and arriving at frequencies of 120 seconds during morning rush hour