

The Directors have pleasure in submitting their Report and the audited statement of Accounts for the financial year ended 31 December 2000.

Principal activities of the Company

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 Quarry Bay (Kwun Tong 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;

C related commercial activities, including the letting of advertising space and marketing of commercial franchises on the railway system, property management and leasing management of investment properties;

D the design, construction, financing and operation of the Tseung Kwan O Extension and the undertaking of related property developments;

E the planning and construction of future extensions to the railway system, and

F the operation of a smart card system by Creative Star Limited, a subsidiary of the Company, for the collection of payments for both transport and non-transport applications.

The privatisation of the Mass Transit Railway Corporation ("MTRC")

In his budget speech on 3 March 1999, the Financial Secretary announced the Government's intention to partially privatise the Company through the sale of a minority interest of its shares and a listing of the Company's shares on The Stock Exchange of Hong Kong Limited ("HKSE"). A key element in the privatisation process was the enactment in March 2000 of the Mass Transit Railway Ordinance (Cap.556 of the Laws of Hong Kong) (the "new MTR Ordinance") which came into effect on 30 June 2000 (the "Appointed Day"). On the same day, the entire property, rights and liabilities of the Mass Transit Railway Corporation ("MTRC") were vested in the Company, which was incorporated on 26 April 2000, with the effect that the Company became the successor to MTRC and is to be treated as if it were the same entity in law as MTRC. In addition, the new MTR Ordinance provides for the granting of a franchise, for an initial period of 50 years (which commenced on the Appointed Day and which may be extended in accordance with the new MTR Ordinance and the related operating agreement (the "Operating Agreement")), to the Company to operate and develop the Mass Transit Railway, as well as for the regulation and operation of the Mass Transit Railway under the Operating Agreement.

On 5 October 2000, the Financial Secretary Incorporated ("FSI"), on behalf of the Hong Kong Government ("Government"), completed an offer for sale of 1,000,000,000 HK\$1 Ordinary Shares in the Company ("Ordinary Shares"). Dealings in the shares in the Company commenced on the HKSE on 5 October 2000. As a result of the offer, the FSI's 100% shareholding was reduced to 80%. On 1 November 2000, the FSI completed the sale of an additional 150,000,000 Ordinary Shares pursuant to an over-allotment option granted to the underwriters of the share offer. As a result, the FSI's shareholding in the Company was further reduced to 77%.

Dividend

The Directors have recommended a final dividend of HK\$0.10 per Ordinary Share to be payable to shareholders whose names appear on the Register of Members of the Company on 17 May 2001. Subject to the passing of the necessary resolutions at the Annual General Meeting, such dividend will be payable on 26 June 2001, in cash in Hong Kong dollars, with a scrip dividend alternative.

Members of the Board and the Executive Directorate

The Board of Directors who served during the year were Jack So Chak-kwong, Cheung Yau-kai, Raymond Ch'ien Kuo-fung, David Gordon Eldon, David Wylie Gairns, Edward Ho Sing-tin, Kevin Ho Chi-ming, Lo Chung-hing, the Commissioner for Transport (Robert Charles Law Footman), the Secretary for Transport (Nicholas Ng Wing-fui) and Denise Yue Chung-ye.

Robert Charles Law Footman was appointed as a Director in his personal capacity on 12 June 2000 and resigned as a Director on 30 June 2000. The Commissioner for Transport (Robert Charles Law Footman) was subsequently appointed as a Director on 30 June 2000.

Kevin Ho Chi-ming was appointed as a Director on 12 June 2000 and resigned as a Director on 30 June 2000. The Secretary for Transport (Nicholas Ng Wing-fui) was subsequently appointed as a Director on 30 June 2000.

The appointment of each of the Secretary for Transport and the Commissioner for Transport was made by the Chief Executive pursuant to the new MTR Ordinance.

Mr. Jack So Chak-kwong and Ms. Denise Yue Chung-ye will retire by rotation at the forthcoming Annual General Meeting (in accordance with the Company's Articles of Association) and offer themselves for re-election.

Brief biographical details for each Director and each member of the Executive Directorate are set out on pages 59.

Corporate governance

The Company is committed to high standards of corporate governance.

The management of the Company's business is vested in the Board of Directors. Pursuant to the Company's Articles of Association and the protocol adopted by the Board of Directors, the Board of Directors has delegated the day-to-day management of the Company's business to the Executive Directorate but the Board of Directors has reserved to itself certain powers, such as the approval of the Company's financial statements, dividends, significant changes in accounting policy, its annual operating budget, certain material contracts, certain financing arrangements and major investments, risk management strategy, treasury policies and fare structures.

The Board of Directors meets regularly and members of the Board receive information between meetings about developments in the Company's business. All members of the Board have full and timely access to the relevant information and may take independent professional advice if necessary. As an integral part of good corporate governance the following committees have been set up:

Executive Directorate

The members of the Executive Directorate who served during the year are Jack So Chak-kwong (Chairman), a member of the Board of Directors, and Russell John Black, William Chan Fu-keung, Philip Gaffney, Thomas Ho Hang-kwong, Clement Kwok King-man and Leonard Bryan Turk.

Audit Committee

The Audit Committee meets regularly with the Company's senior financial, internal audit and compliance management and the external auditor to consider the Company's financial reporting, the nature and scope of audit review and the effectiveness of the systems of internal control and compliance. The members of the Audit Committee comprised (a) prior to the 13 June 2000, David Wylie Gairns (chairman), Raymond Ch'ien Kuo-fung and Edward Ho Sing-tin and (b) after 13 June 2000, David Wylie Gairns (chairman), Cheung Yau-kai and the Commissioner for Transport (Robert Charles Law Footman), all of whom are non-executive Directors.

Remuneration Committee

The Remuneration Committee meets regularly to consider human resources issues, including the terms and conditions of employment, remuneration, and retirement benefits of the Chairman and Chief Executive and members of the Executive Directorate. The members of the Remuneration Committee comprised (a) prior to 13 June 2000, the whole Board of Directors and (b) after 13 June 2000, Raymond Ch'ien Kuo-fung (chairman), Edward Ho Sing-Tin and Denise Yue Chung-ye, all of whom are non-executive Directors.

Nominations Committee

The Nominations Committee was formed on 13 June 2000 and carries out the process of recommending and nominating candidates to fill vacancies on the Board of Directors. A person may be appointed as a Director at any time either by the shareholders in general meeting or by the Board upon the 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 the 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 (excluding the Directors appointed by the Chief Executive of Hong Kong under the new MTR Ordinance). The members of the Nominations Committee are David Gordon Eldon (chairman), Lo Chung-hing and the Secretary for Transport, all of whom are non-executive Directors.

The Company has complied throughout the year (both before and after the above-mentioned offer for sale of Ordinary Shares on 5 October 2000) with the Code of Best Practice as set out in Appendix 14 of the Rules Governing the Listing of Securities on the HKSE, except that non-executive Directors of the Company are not appointed for a specific term but are subject (save those appointed pursuant to Section 8 of the new 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 Company's Articles of Association.

The Company received the Diamond Award in the public sector category for Best Corporate Governance Disclosure from the Hong Kong Society of Accountants in 2000.

Accounts

The results of the Company and the cash flows for the year ended 31 December 2000 and the state of affairs of the Company at that date are set out in the Accounts on pages 68 to 106.

Ten-year statistics

A summary of the results and of the assets and liabilities of the Company together with some major operational statistics for the last ten years are set out on pages 56 and 57.

Fixed assets

Movements in fixed assets during the year are set out in Note 14 to the accounts.

Movements in reserves

Movements in reserves during the year are set out in Note 31 to the accounts.

Share capital

The Company was incorporated with an authorised share capital of HK\$33 billion divided into 33 billion Ordinary Shares, one of which was issued and credited as fully paid to the FSI and one of which was issued and credited as fully paid to Denise Yue Chung-ye. On 30 June 2000, 2,999,999,998 Ordinary Shares were issued to the FSI and credited as fully paid in accordance with the determination made by the Financial Secretary under Section 42 of the new MTR Ordinance. On 12 September 2000, the authorised share capital of the Company was reduced from HK\$33 billion divided into 33 billion Ordinary Shares to HK\$6.5 billion divided into 6.5 billion Ordinary Shares. On the same day, all of the shareholders of the Company resolved that the Company applies its capital reserve (in accordance with its Articles of Association) in paying up in full 2 billion unissued Ordinary Shares and to issue such shares to the FSI, credited as fully paid bonus shares. As at 31 December 2000, the authorised share capital of the Company was HK\$6.5 billion, divided into 6.5 billion Ordinary Shares, 5 billion of which were issued fully paid. These changes to the Company's share capital were made to facilitate the listing of the Company's Ordinary Shares on the HKSE.

Redemption of listed securities

There was no redemption of the Company's debt securities listed on the stock exchanges during the year.

Properties

Particulars of the principal investment properties of the Company are shown on pages 37.

Donations

During the year, a total of HK\$1.3 million was donated to the Community Chest of Hong Kong and the Sports Federation & Olympic Committee of Hong Kong, China.

Internal controls and internal audit

The Board is responsible for ensuring that there is in place a satisfactory system of internal financial controls. The main objectives are to ensure adherence to the Company's control policies so that the Company's assets are safeguarded and that the financial records are complete and accurate.

The Company has an Internal Audit Department which reviews both manual and computerised systems and procedures in all major financial and operational activities. This department is headed by the Head of Internal Audit and Business Processes who is directly responsible to the Chairman of the Board and submits regular reports to the Audit Committee.

A function of the Audit Committee is to review the effectiveness of the system of internal financial controls 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 according to the Preferred Financing Model which defines the preferred mix of financing instruments, fixed and floating rate debt, 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 currency swaps are used only as hedging tools to manage our 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 authorised 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 Company issued bonds and notes during the year ended 31 December 2000, details of which are set out in Note 24C of the accounts. Such bonds and notes were issued in order to meet the Company's general corporate funding requirements, including the financing of new capital expenditure and the refinancing of maturing debts.

Electronic data and year 2000

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 successfully completed its plan and timetable for Year 2000 rollover and the transition into 2000 went smoothly. No Year 2000-related problems were detected.

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

Save for two loans made by the Company to two Members of the Executive Directorate, details of which are set out in Note 5B of the accounts, and the deed of indemnity, details of which are set out in the section below headed "Transactions in connection with the Privatisation Share Offer of the Company", no contracts 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, subsisted at the end of the year or at any time during the year.

Board Members and Executive Directorate's interests in shares

At 31 December 2000, the interests of the members of the Board of Directors and the Executive Directorate in the equity securities of the Company as recorded in the register required to be kept under section 29 of the Securities (Disclosure of Interests) Ordinance ("SDI") or as otherwise notified to the Company and the HKSE pursuant to the Model Code for Securities Transactions by Directors of Listed Companies were as follows:

Ordinary Shares

Members of the Board of Directors or Executive Directorate	Number of Ordinary Shares
Jack So Chak-kwong	2,000
Russell John Black	2,000
William Chan Fu-keung	2,000
Philip Gaffney	2,500
Thomas Ho Hang-kwong	4,000
Clement Kwok King-man	4,000
Leonard Bryan Turk	4,000

Options to subscribe for ordinary shares granted under the Share Option Scheme, as referred to in Note 5C of the accounts

Members of the Board of Directors or Executive Directorate	Numbers of Ordinary Shares	Date granted	Period during which rights exercisable (day/ month/ year)	Price per share to be paid on exercise of options	Consideration paid for options granted
Jack So Chak-kwong	1,599,000	20/9/00	5/10/2000 to 5/10/2010	\$8.44	None
Russell John Black	1,066,000	20/9/00	5/10/2000 to 5/10/2010	\$8.44	None
William Chan Fu-keung	1,066,000	20/9/00	5/10/2000 to 5/10/2010	\$8.44	None
Philip Gaffney	1,066,000	20/9/00	5/10/2000 to 5/10/2010	\$8.44	None
Thomas Ho Hang-kwong	1,066,000	20/9/00	5/10/2000 to 5/10/2010	\$8.44	None
Clement Kwok King-man	1,066,000	20/9/00	5/10/2000 to 5/10/2010	\$8.44	None
Leonard Bryan Turk	1,066,000	20/9/00	5/10/2000 to 5/10/2010	\$8.44	None

Save as disclosed above:

A there were no interests held as at 31 December 2000 by any members of the Board of Directors or Executive Directorate of the Company in securities of the Company and its associated corporations (within the meaning of the SDI); and

B during the year ended 31 December 2000, no member of the Board of Directors 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 29 of the SDI or otherwise notified to the Company and the HKSE pursuant to the Model Code for Securities Transaction by Directors of Listed Companies.

Substantial shareholders' interests

Set out below is the name of the party which was interested in 10 per cent 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 2000 as recorded in the register kept by the Company under Section 16(1) of the SDI:

Name	No. of Ordinary Shares
Financial Secretary Incorporated (in trust on behalf of the Government)	3,849,999,999

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 2000 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 2000 was attributable to the Company's five largest customers combined by value.

Going concern

The financial statements on pages 68 to 106 have been prepared on a going concern basis. The Board has reviewed the Company's budget for 2001, 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.

Connected transactions

During the year under review the following transactions and arrangements described below have been entered into (or were ongoing) with persons who are "connected persons" for the purposes of the Rules Governing the Listing of Securities on the HKSE:

Entrustment agreements

A The Company has entered into the following entrustment agreements with Government in relation to the Tseung Kwan O Extension / Lantau & Airport Railway under which Government agreed to carry out works on behalf of the Company in return for monthly payments based on the work completed:

1 Agreement dated 15 August 1997, for Government to carry out works relating to a 4-cell box tunnel near junction of Road P2/D4 in Tseung Kwan O, with a total value of HK\$79,000,000.

2 Agreement dated 12 January 1999, for Government to carry out works relating to construction of diaphragm walls crossing underneath Road P1 in Tseung Kwan O Town Centre, with a total value of HK\$19,034,200.

3 Agreement dated 6 March 1995, for Government to carry out construction and part design of railway tunnels and railway formation works within West Kowloon Expressway Corridor, with a total value of HK\$302,992,941.

4 Agreement dated 6 March 1995, for Government to carry out design and construction of 2.5km of twin and single track railway viaduct within the Route 3 Expressway Corridor, with a total value of HK\$430,094,669.

5 Agreement dated 6 March 1995, for Government to carry out design and construction of railway drainage and subballast and all bridges between Tsing Chau Tsai and Chek Lap Kok, with a total value of HK\$684,176,963.

6 Agreement dated 10 February 1997, for Government to carry out works relating to support for railway elements within the Lantau Fixed Crossing, with a total value of HK\$1,144,301,313.

Government is a substantial shareholder in the Company.

B The Company has entered into the following entrustment agreements with Government in relation to the Tseung Kwan O Extension under which the Company agreed to carry out works on behalf of Government in return for monthly payments based on the work completed:

1 Agreement dated 26 May 1999, for the Company to carry out construction works relating to infrastructure adjacent to Areas 45, 55, 56 and 57 in Tseung Kwan O Town Centre, with a total value of HK\$47,750,000.

2 Agreement dated 19 November 1999, for the Company to carry out construction works at Road D4 in Tseung Kwan O Town Centre, with a total value of HK\$19,397,685.

3 Agreement dated 28 February 2000, for the Company to carry out design and construction of landscape bund and footbridge link to Area 24 to Po Lam, with a total value of HK\$20,850,000.

Government is a substantial shareholder in the Company.

C The Company has entered into the following entrustment agreements with the Housing Authority in relation to the Tseung Kwan O Extension, under which the Company agreed to carry out works on behalf of the Housing Authority in return for monthly payments based on the work completed:

1 Agreement dated 10 December 1997, for the Company to carry out site formation works at Tiu Keng Leng (South), with a total value of HK\$124,045,032.

2 Agreement dated 10 April 1999, for the Company to carry out site formation works and part foundations of housing blocks at Eastern Harbour Crossing and shopping spine above Yau Tong Station, with a total value of HK\$397,600,000.

3 Agreement dated 11 December 1998, for the Company to carry out construction work relating to Yau Tong Phase 4 Public Transport Interchange, with a total value of HK\$46,278,514.

The Housing Authority is a Governmental statutory body and Government is a substantial shareholder in the Company.

D The Company has entered into an entrustment agreement with the Airport Authority, dated 15 December 1995, for the Airport Authority to carry out construction work for the Company relating to the Airport Platform at Chek Lap Kok, with a total value of HK\$854,000,000.

The Airport Authority is a Governmental statutory body and Government is a substantial shareholder in the Company.

E The Company has entered into an entrustment agreement with Kowloon-Canton Railway Corporation ("KCRC"), dated 18 January 2000, for KCRC to carry out design and construction work for the Company, at the cost of KCRC, relating to the Airport Railway element of Nam Cheong Station.

KCRC is wholly-owned by Government, which is a substantial shareholder in the Company.

Land agreements

The Company has entered into the following land grants with Government in relation to the Airport Railway, which provides for the Company to develop certain sites adjacent to the Airport Express and Tung Chung Lines. Upon payment of the relevant land premium, the Company may develop the relevant site within the building covenant period. All agreements provide for the sites (once developed) to have a lease term up to 30 June 2047.

1 Grant No. 12459, dated 21 May 1997, for Private Treaty Grant of IL No. 8898 for development at Hong Kong Station (building covenant period expiry date 30 September 2005) with a total consideration or value of HK\$5,834,000,000.

2 Modification of Grant No. 12459, dated 1 February 2000, for development at Hong Kong Station (building covenant period expiry date 1 February 2006) with a total consideration or value of HK\$5,500,000,000.

3 Grant of KIL No. 11080 to the Company, dated 8 July 1996, for development at Kowloon Station (building covenant period expiry date

30 March 2009) with a total consideration or value of: Site A - HK\$3,377,230,000; Sites B,C,D,E, F and G - to be assessed.

4 Modification, dated 15 May 2000, to amend and allow the Company to develop Site C at Kowloon Station under new user and gross floor area restrictions (building covenant period expiry date 14 June 2006) with a total consideration or value of HK\$2,400,000,000.

5 Modification, dated 12 December 2000, to amend and allow the Company to develop Sites E, F and G at Kowloon Station under new user and gross floor area restrictions (building covenant period expiry dates 31 March 2007 for Sites E and F and 31 March 2009 for Site G) with a total consideration or value of HK\$5,562,710,000.

6 Grant No. 12349 for Private Treaty Grant of KIL No. 11068, dated 8 May 1995, for development at Olympic Station (building covenant period expiry date 7 November 1999) with a total consideration or value of HK\$1,530,000,000.

7 Grant No. 12375 for Private Treaty Grant of KIL No. 11074, dated 31 January 1996, for development at Olympic Station (building covenant period expiry date 30 January 2002) with a total consideration or value of HK\$3,777,860,000.

8 Grant No. 12434 for Private Treaty Grant of KIL No. 11090, dated 10 January 1997, for development at Olympic Station (building covenant period expiry date 9 January 2003) with a total consideration or value of HK\$6,118,000,000.

9 Grant No. 12529 for Private Treaty Grant of KIL No. 11104, dated 25 February 1999, for development at Olympic Station (building covenant period expiry date 31 March 2004) with a total consideration or value of HK\$302,480,000.

10 New Grant No. 6993 for Private Treaty Grant of TYTL No. 132, dated 7 March 1996, for development at Tsing Yi Station (building covenant period expiry date 30 September 2001) with a total consideration or value of HK\$4,343,500,000.

11 New Grant No. 7973 for Private Treaty Grant of Tung Chung Town Lot No. 1, dated 16 August 1995, for development at Tung Chung Station (building covenant period expiry date 30 September 2000) with a total consideration or value of HK\$1,730,550,000.

12 New Grant No. 7984 for Private Treaty Grant of Tung Chung Town Lot No. 2, dated 27 September 1995, for development at Tung Chung Station (building covenant period expiry date 30 September 2003) with a total consideration or value of HK\$724,010,000.

13 New Grant No. 8015 for Private Treaty Grant of Tung Chung Town Lot No. 3, dated 1 May 1996, for development at Tung Chung Station (building covenant period expiry date 31 March 2001) with a total consideration or value of HK\$873,030,000.

14 Modification for New Grant No. 8082, dated 3 May 2000, for additional gross floor area and some other amendments at Tung Chung Station (building covenant period expiry date 31 March 2005) with a total consideration or value of HK\$493,570,000.

15 New Grant No. 8102 for Private Treaty Grant, dated 26 June 1997, of Tung Chung Town Lot No. 5 for development at Tung Chung Station (building covenant period expiry date 30 June 2003) with a total consideration or value of HK\$4,150,000,000.

16 Modification for New Grant No. 8102, dated 16 August 1999, for additional gross floor area and some other amendments for development at Tung Chung Station (building covenant period expiry date 30 June 2005) with a total consideration or value of HK\$660,000,000.

17 New Grant No. 8082, dated 26 March 1997, of Tung Chung Town Lot No. 4 for development at Tung Chung Station (building covenant period expiry date 31 March 2002) with a total consideration or value of HK\$2,510,000,000.

Transactions between the Company and Creative Star Limited ("Creative Star")

The Company has entered into the following transactions with its subsidiary, Creative Star, to enable Creative Star to meet the requirements of a deposit-taking company under the Banking Ordinance (Cap.155 of the laws of Hong Kong).

1 Subscription by the Company on 18 April 2000 of 28,475,322 additional shares in Creative Star, for a total consideration of HK\$28,475,322.

2 Subordinated loan agreement, dated 18 April 2000, under which the Company made a loan of HK\$18,984,000 to Creative Star, with interest payable at prime lending rate, which is subordinate to all other claims against Creative Star and will not be repaid by Creative Star without the consent of the Hong Kong Monetary Authority.

During the year ended 31 December 2000, the Company paid Creative Star a total amount of HK\$43 million in respect of central clearing services provided by Creative Star. During the same period, load agent fees amounting to HK\$11 million were received by the Company from Creative Star in respect of services and facilities provided by the Company at various MTR stations to enable customers to add value to Octopus cards.

In connection with the listing of the Company's shares on the HKSE in October 2000, the HKSE granted the Company a waiver from strict compliance with Chapter 14 of the Listing Rules insofar as it relates to connected transactions, subject to compliance with certain requirements. As required by one of these requirements, the Company now confirms that those of the central clearing services provided by Creative Star and load agent fees paid to the Company which occurred following completion of the Global Offering (as defined in the prospectus issued by the Company in relation to the MTR Privatisation Share Offer and dated 25 September 2000) were: (i) transactions entered into by the Company in the ordinary and usual course of its business; (ii) entered into on normal commercial terms (by reference to transactions of a similar nature made by similar entities within Hong Kong); and (iii) entered into on terms no less favourable than terms available to the other shareholders of Creative Star.

Transactions between the Company and KCRC in relation to Creative Star

The Company has entered into the following agreements with KCRC, The Kowloon Motor Bus Company (1933) Limited, Citybus Limited and The Hongkong and Yaumati Ferry Company, Limited and which were ongoing during 2000.

1 Shareholders' agreement, dated 9 June 1994, under which the parties agreed to incorporate a company, Creative Star, in order to undertake the development and operation of a contactless smart card ticketing system (now known as Octopus). The Company held 67.8% of the equity capital in Creative Star but the voting rights at board meetings of the director appointed by the Company to the board of directors of Creative Star were limited to 49% only. The parties paid HK\$1,000 in aggregate (in proportion to their respective shareholdings) for shares in Creative Star and undertook to make available loans to Creative Star (in proportion to their respective

shareholdings) up to a total amount of not more than HK\$195.7 million (which has been fully repaid).

2 Supplemental shareholders' agreement, dated 13 August 1999, which revised the terms of the shareholders' agreement dated 9 June 1994 to address, inter alia, certain issues arising from the application by Creative Star for authorisation under the Banking Ordinance (Cap.155 of the laws of Hong Kong) to carry on business as a deposit-taking company. The parties made a commitment to provide funds to Creative Star and give guarantees and indemnities as required under the Banking Ordinance (Cap.155 of the laws of Hong Kong).

During the year ended 31 December 2000, KCRC paid Creative Star a total amount of HK\$27 million in respect of transaction and interchange fees for the handling of Octopus tickets. During the same period, load agent fees amounting to HK\$5 million were received by KCRC from Creative Star in respect of services and facilities provided by KCRC at various KCR stations to enable customers to add value to Octopus cards.

As at 31 December 2000, The Company held 67.8% of the issued share capital in Creative Star and KCRC held 24.7%. Creative Star is a subsidiary of the Company and KCRC is a substantial shareholder in Creative Star. Furthermore, Government is a substantial shareholder in the Company and KCRC is an associate of Government.

Creative Star - updated information

1 On 17 January 2001, the then shareholders in Creative Star (New World First Bus Services Limited and New World First Ferry Services Limited having replaced The Hongkong and Yaumati Ferry Company, Limited as a shareholder) entered into a replacement shareholders' agreement in respect of Creative Star, under which, inter alia, Creative Star was converted to profit making status. In connection with this agreement, the Company's shareholding in Creative Star was reduced to 57.4% and KCRC's shareholding was reduced to 22.1%. Further details of the replacement shareholders' agreement are set out in Note 39 to the accounts.

2 On 17 January 2001, the Company entered into an Octopus Card Services Agreement (the "MTR Octopus Services Agreement") with its subsidiary, Creative Star, in order to formalise the arrangements that already existed between them as to services provided to each other relating to Octopus cards. The estimated fees payable by the Company to Creative Star in 2001 under the MTR Octopus Services Agreement are HK\$46.4 million and the estimated fees payable by Creative Star to the Company in 2001 are HK\$12.7 million. Under the terms of the MTR Octopus Services Agreement, the Company will accept use of Octopus cards as payment for its fares and will provide add-value services, refund handling and other services to Creative Star for an indefinite period terminable on six months' notice (not to be given before 1 July 2010).

As required by the waiver referred to above granted to the Company by the HKSE in relation to connected transactions, the Company confirms that the MTR Octopus Services Agreement was: (i) a transaction entered into by the Company in the ordinary and usual course of its business; (ii) entered into on normal commercial terms (by reference to transactions of a similar nature made by similar entities within Hong Kong); and (iii) entered into on terms no less favourable than terms available to the other shareholders of Creative Star.

3 On 17 January 2001, KCRC entered into an Octopus Card Services Agreement (the "KCRC Octopus Services Agreement") with Creative Star in order to formalise the arrangements that already existed between them as to services provided to each other relating to Octopus cards. Under the terms of the KCRC Octopus Services Agreement, KCRC will accept use of Octopus cards as payment for its fares and will provide add-value services, refund handling and other services to Creative Star for an indefinite period terminable on six months' notice (not to be given before 1 July 2010).

Project Agreements

The Company and the Secretary for Transport, for and on behalf of Government, entered into an Amendment and Restatement Agreement on 30 June 2000 which, in the light of the partial privatisation of the Company, provides for the amendment and restatement of, inter alia, the TKE Project Agreement and the QBR Project Letter as defined below (both of which were ongoing during 2000). Government is a substantial shareholder in the Company.

The Company and the Secretary for Transport, for and on behalf of Government, had entered into a Project Letter on 29 April 1998 (which was acknowledged, accepted and agreed on 7 May 1998) relating to the Quarry Bay Congestion Relief Works ("QBR Works") (the "QBR Project Letter"). Under the QBR Project Letter, the Company is obliged to carry out the design, construction, completion, commissioning and bringing into operation of the QBR Works. The costs of those works are to be borne by the Company. The QBR Project Letter provides for the grant of land to the Company for the operation of the railway (subject to the payment of nominal land premium only).

The Company and the Secretary for Transport, for and on behalf of Government, had entered into a Project Agreement for the Design, Construction, Financing and Operating of the Tseung Kwan O Extension ("TKE") (the "TKE Project Agreement") on 4 November 1998. Under the TKE Project Agreement, the capital cost of work undertaken by the Company to complete the TKE and other costs are borne by the Company and there are provisions relating to the design, construction and operation of the TKE by the Company, and provisions relating to works to be carried out by the Company on behalf of Government (in respect of which, Government will reimburse the Company). The TKE Project Agreement provides for the grant of land to the Company for the operation of the railway (subject, inter alia, to the payment by the Company to Government of nominal land premium only), land for the construction of a depot and land for property development (subject, in each case, to the payment by the Company to Government of an amount to be assessed). The TKE Project Agreement also provides for the future grant to the Company of the ownership and operating rights in respect of the TKE.

Land comfort letter

The Company has received a letter from Government, dated 14 July 2000, pursuant to which Government agreed to extend the period of certain of the Company's land interests so that they are coterminous with the Company's initial 50-year franchise and, for certain other interests, Government has agreed to render assistance to the Company to facilitate the smooth operation of the railway during the Company's

franchise period. If the Company's initial 50-year franchise is extended, Government has agreed that, subject to certain conditions (including the prevailing land policy at the time of extension of the franchise), Government will amend certain documents, including the Running Lines Leases, to make them coterminous with the extended franchise period. Government is a substantial shareholder in the Company.

Eastern Harbour Crossing Agreement

The Company and the Secretary for the Treasury, for and on behalf of Government, entered into an agreement on 30 June 2000 in respect of the vesting of certain assets comprised in the Eastern Harbour Crossing by Government into the Company in 2008 for nominal consideration (the "EHC Agreement"). Under the EHC Agreement, the Company agreed to indemnify Government for certain amounts which are expected to be nominal. Government is a substantial shareholder in the Company.

Transactions in connection with the Privatisation Share Offer of the Company

1 The Company entered into a deed of indemnity dated 22 September 2000, with the members of the Board and members of the Executive Directorate and the FSI, under which, inter alia, the FSI agreed to indemnify the Company, the members of the Board and members of the Executive Directorate in certain circumstances and in respect of certain liabilities in respect of the global offering of the shares in the Company by the FSI. The FSI is a substantial shareholder in the Company and the members of the Board and members of the Executive Directorate are also connected persons of the Company.

2 The Company, the FSI, Goldman Sachs (Asia) L.L.C., HSBC Investment Bank Asia Limited and UBS AG entered into the following underwriting agreements in relation to the underwriting of the Privatisation Share Offer of the Company, details of which were disclosed in the prospectus issued by the Company in connection with the Privatisation Share Offer of the Company dated 25 September 2000:

- i the Hong Kong Underwriting Agreement, with the Hong Kong Underwriters (as defined therein), dated 22 September 2000; and
- ii the International Underwriting Agreement, with the International Underwriters (as defined therein), dated 1 October 2000.

The FSI is a substantial shareholder in the Company.

Auditors

The retiring auditors, KPMG, have signified their willingness to continue in office. A resolution will be proposed at the Annual General Meeting to reappoint them and to authorise the directors to fix their remuneration.

By order of the Board

Leonard B. Turk
Secretary to the Board
 Hong Kong, 1 March 2001