CEO's review of operations and outlook

Dear Stakeholders,

MTR Corporation's results for the first six months of 2004 showed a recovery from the lows experienced in the comparable period of 2003, when the combination of a weak economy, soft property prices and the outbreak of SARS severely affected Hong Kong and impacted the Company's core businesses.

As a result of the improved economic environment, the Company's revenues for the six months ended 30 June 2004 increased 11.8% to HK$3,987 million as compared with the same period of 2003. Net profit increased significantly to HK$1,175 million. Earnings per share were HK$0.22 for the first six months of 2004, as compared with HK$0.02 over the same period of 2003. Your Board of Directors has declared an Interim Dividend of HK$0.14 per share, unchanged from the Interim Dividend paid last year.

Railway operations

For the first six months of 2004, the MTR Lines recorded total patronage of 403.6 million, a 12% increase over the first half of last year.

The Company's overall share of total franchised public transport rose slightly to 24.6% from 23.9% in the comparable period of 2003. Share of cross-harbour trips increased from 58.2% to 59.3%. The performance of the Tseung Kwan O Line was better than forecast and this helped offset the lower than expected increase in patronage interchanging from the KCRC's West Rail.

With the recovery of passenger arrivals and departures at Hong Kong International Airport, the Airport Express Line (AEL) experienced strong recovery, leading to total passenger numbers rising 32.5%, as compared to the first half of 2003 to an average of 21.1 thousand per day. In order to accomodate the increase in passengers, we increased the frequency of services on AEL from every 15 minutes to every 12 minutes in March.

MTR continued to meet or exceed both the Government's requirements under the Operating Agreement and the Company's own more stringent Customer Service Pledges.

The Company's marketing and promotional programmes continued to support recovery in patronage. The popular "Ride 10 get 1 Free" scheme was further extended to 3 October this year, while during Chinese New Year and Easter holidays, as well as over the summer months, senior citizens and children enjoyed the HK$2 promotion programme on Sundays and public holidays. In addition, our MTR Club has continued with a bonus point scheme to encourage and reward our frequent passengers.

To commemorate the Company's 25th year of operations, a number of initiatives were launched, including new TV commercials, Theme Train, a feature in the TVB Hong Kong Superbrand programme, as well as a special section on the Company's website. For AEL, we continued our partnership with the Asia Miles frequent flyer programme, and with the Hong Kong Tourism Board to market the Airport Express service to inbound air travellers. In addition, we began accepting renminbi credit cards at all our AEL stations in May this year to further improve our service to Mainland visitors.

Promotions designed to achieve greater integration between MTR and other transport providers continued, with two more Green Minibus routes offering intermodal discounts, as well as the extension of the taxi interchange programme for AEL.

Overall quality of passenger experience was further enhanced as the various schemes to improve network facilities progressed. The scheme to retrofit all underground stations with platform screen doors saw installations at 17 stations, bringing to 44 the number of platforms completed, out of 74 in total. Under the station improvement programme, renovations were undertaken at Prince Edward, Admiralty, Kowloon Tong, Mong Kok and Central stations. New escalators came into service at Tsim Sha Tsui Station and the number of stations with free internet access sites was increased to six.

Further progress was achieved on projects to improve station access through pedestrian links. A refurbished entrance at Tsim Sha Tsui Station was opened, followed by a new interchange subway at Kowloon Tong Station, providing easier passage to the KCRC concourse. Construction work on improving links began or continued at other stations, including Mong Kok which integrates with the Urban Renewal Authority's development, Admiralty which connects with Three Pacific Place, and Choi Hung which connects to the Park and Ride development.

Operations performance in the first half 2004

Service performance item	Performance requirement	Customer service pledge target	**Actual performance**
Train service delivery	98.5%	99.5%	**99.9%**
Passenger journeys on time			
– MTR Lines	98.5%	99.5%	**99.9%**
– Airport Express Line	98.0%	99.0%	**99.9%**
Train punctuality			
– MTR Lines	98.0%	99.0%	**99.8%**
– Airport Express Line	98.0%	99.0%	**99.9%**
Train reliability: train car-km per train failure causing delays ≥ 5 minutes	N/A	500,000	**1,084,267**
Ticket reliability: magnetic ticket transactions per ticket failure	N/A	8,000*	**10,590**
Add value machine reliability	95.5%	98.0%*	**99.5%**
Ticket issuing machine reliability	93.0%	98.0%*	**99.5%**
Ticket gate reliability	97.0%	99.0%	**99.8%**
Escalator reliability	98.0%	99.0%	**99.9%**
Passenger lift reliability	98.5%	99.0%	**99.9%**
Temperature and ventilation			
– Trains: to maintain a cool, pleasant and comfortable train environment generally at a temperature at or below 26°C	N/A	97.0%	**99.9%**
– Stations: to maintain a cool, pleasant and comfortable environment generally at or below 27°C for platforms and 29°C for stations concourses, except on very hot days	N/A	90.0%	**99.7%**
Cleanliness			
– Train compartment: cleaned daily	N/A	98.5%*	**100%**
– Train body: washed every 2 days	N/A	98.0%	**99.9%**
Passenger enquiry response time within 7 working days†	N/A	99.0%	**99.9%**

* Targets raised for 2004
† New performance criterion for 2004

Property

Our property development business achieved satisfactory results in the first half of 2004 with development profits increasing by 70.1% to HK$1,153 million when compared to the first half of 2003. Profits were derived mainly from Caribbean Coast (Tung Chung Package Three), together with Sorrento and The Harbourside (Kowloon Packages Two and Four respectively).

Along the Airport Railway, sales of residential units at the Company's various joint venture developments benefited from the improvement in market sentiment. Sales at Kowloon Package Four, The Harbourside, proceeded well whilst by 30 June 2004, all remaining units at Seaview Crescent (Tung Chung Package One) and Caribbean Coast Phase 2 (Tung Chung Package Three) had been sold. Construction on the superstructure began at Olympic Package Three, while construction of town houses began at Coastal Skyline Phase 2 at Tung Chung Station.

Developments along the Tseung Kwan O Line made further progress with satisfactory sale results in our joint venture development, Residence Oasis, at Hang Hau Station. At Tiu Keng Leng Station, construction has commenced on the superstructure whilst at Area 55b in Tseung Kwan O Station, work on the superstructure, including the podium, is proceeding on schedule. Also in Tseung Kwan O Station, following acceptance of design changes, an additional premium was paid for the amended Area 57a scheme, while the proposal for a mixed commercial and residential development for Area 56 remained under review. For Area 86, which forms the bulk of MTR's land bank in Tseung Kwan O, we expect to make our first package available for development later this year.

Following rejection by the Town Planning Board of our proposals for Tsing Yi Town Lot No 135 adjacent to Tsing Yi Station, we are considering views of the community to develop a revised proposal.

The Company's commercial investment properties performed well in the first six months of 2004, with rental income rising 10.1% over the same period last year to HK$481 million, as a result of the general economic upturn, supported by recovery in consumer confidence and increase in the number of Mainland visitors. Average rents at the Company's shopping centres rose while overall occupancy remained at over 99%.

The Company's landmark Two International Finance Centre above Hong Kong Station continued its success to secure more tenants and increase its profile as a state-of-the-art office building. As at 30 June 2004, MTR's 18 floors of this building were 85% let, with a number of reputable companies including ABN AMRO Bank, Bank of America and Samsung choosing to relocate there. Our tenants have been attracted by the building's modern design, prime location, advanced building services and information technology facilities.

In April 2004, marketing began for MTR's new retail centre above Hang Hau Station, "The Link", which is scheduled to open in the first half of 2005. The Union Square Shopping Centre at Kowloon Station saw steady construction progress and we are expecting to receive the bare shell of this centre later this year. At Olympic Station, refurbishment began at Olympian City One to create a "sports city", which is targeted for completion in the third quarter of 2004.

The property management business also saw solid growth, with revenue rising 9.8% over the corresponding six months of last year to reach HK$56 million inclusive of agency income, as the managed portfolio continued to expand. In Hong Kong, as at 30 June 2004, the number of residential units managed by MTR had risen to 47,769, while commercial and office space increased to 558,796 square metres. In the Mainland, we continued to develop our property consultancy and management business with four developments now under management or pre-management contracts.

Other businesses

Economic recovery and rising patronage led to a marked recovery in the Company's revenues from rail related and other businesses, which for the first half of this year rose by 13.1% to HK$579 million when compared to the same period of 2003.

Tseung Kwan O Line property developments (packages awarded)

Location	Developers	Type	Gross floor area (sq. m.)	No. of parking spaces	Status	Expected completion date
Tseung Kwan O Station						
Area 57a	Sun Hung Kai Properties Ltd.	Residential	26,005		Awarded in July 2000	2005
	Nan Fung Development Ltd.	Retail	3,637			
	Henderson Land Development Co. Ltd.	Car park		74		
	Chime Corporation Ltd.					
Area 55b	New World Development Co. Ltd.	Residential	84,920		Awarded in January 2002	2006
	Chow Tai Fook Enterprises Ltd.	Retail	11,877			
	Wee Investments Pte. Ltd.	Car park		249		
Hang Hau Station	Sino Land Co. Ltd.	Residential	138,652		Awarded in June 2002	2005
(Residence Oasis, The Link)	Kerry Properties Ltd.	Retail	3,500			
		Car park		369		
Tiu Keng Leng Station	Cheung Kong (Holdings) Ltd.	Residential	236,965		Awarded in October 2002	2007
		Retail	16,800			
		Car park		587		

Tseung Kwan O Line property developments (packages to be awarded)*

Location	No. of packages envisaged	Type	Gross floor area (sq. m.)	No. of parking spaces	Expected package launch date	Expected completion date
Tseung Kwan O Station	2	Retail	60,000		2005–2006	2009
		Office	103,130			
		Car park		1,291		
Area 86 (Tseung Kwan O South Station)	14	Residential	1.6 million		2004–2010	2013
		Retail	40,000			
		Car park		4,131		

* Subject to review in accordance with planning approval, land grant conditions and completion of statutory processes

Choi Hung Park and Ride Development

Location	Developers	Type	Gross floor area (sq. m.)	No. of parking spaces	Status	Expected completion date
Choi Hung Station	Chun Wo Holdings Ltd.	Residential	19,138		Awarded in July 2001	2005
		Retail	2,400			
		Car park		54		
		Park and Ride		450		

Station commercial facilities revenues rose by 8.9% to HK$147 million as usage of the network rebounded and a comprehensive programme to renovate MTR stations and improve tenant mix brought additional revenue growth. During the six months, 26 new shops were built under the renovation programme, including four at the new exit to Kowloon Tong Station that links with the KCRC network.

Advertising revenues rose significantly by 18.8% over the first half of 2003 to HK$190 million. According to findings of the first "Reach & Frequency Research of MTR Advertising" by Nielsen Media Research, advertising at MTR reaches an average of 2.8 million passengers each week, about 45% of Hong Kong's total population.

New advertising formats and services continued to attract clients. In April, the first non-flash tunnel advertising was introduced between Wan Chai and Causeway Bay stations. The concourse and trackside TV plasma network expanded further, with a further 51 units installed during the first half of the year, bringing the total to 119 units by 30 June 2004. The programme to convert 4-sheet panels to higher impact 12-sheet panels in station concourses also progressed and is now 97% complete. To enhance competitiveness, some 12-sheet trackside panels at five key stations were converted to mega panels for sticker advertising.

Revenues from telecommunications services increased by 26.7% to HK$114 million due to increased usage of mobile telephones within our network. We continue to upgrade our network to handle 3G communications with 18 stations now offering this service. We also introduced wireless LAN hot-spot services in most of the concourse and platform areas of all AEL stations. TraxComm Limited recorded higher revenue as it extended the reach of its optical fibre network to data centres and commercial buildings whilst continuing to upgrade its backbone network. A sales team was established to improve the service to wholesale customers, resulting in a number of bandwidth contracts.

Revenue from external consultancy increased slightly to HK$73 million as compared with the same period last year as we took a more focused approach to seek only those contracts which would enhance our overseas growth strategy.

Miscellaneous business revenue during the first six months of 2004 amounted to HK$55 million.

In the Mainland, we signed several new consulting and training contracts during the period, in cities such as Beijing, Nanjing and Tianjin. In Shanghai, the Company's joint venture partnership, SHKM Construction Management, signed the agreement to be the owner's representative on Shen-song Line R4, and work has started on several key contracts. The joint venture also secured two further consultancy contracts, both on Shanghai Line 11 (Shen-jia Line) .

Elsewhere, our contribution to a project to build a nation-wide Automatic Fare Collection system for the Netherlands has made satisfactory progress, with station layouts nearing completion and the bulk initialisation machine delivered.

Octopus Cards continued to expand its operations both within and beyond the transport sector. As at 30 June 2004, cards in circulation rose to 11.0 million and average daily transaction volume and value for the month of June 2004 increased to 8.3 million and HK$56.7 million respectively. MTR's share of earnings from this company rose by 81.8% to HK$20 million for the six months period. By 30 June 2004, almost all Green Minibuses accepted Octopus, as well as 47 Red Minibuses. Car parks accepting the system have increased to 143 and the roll-out to parking meters continued. More large retail chains joined during the first half of the year, including St Honore, while Citibank and Hang Seng Bank became the latest to join the expanding group of banks that offers Automatic Added-Value Service to their credit card clients. To increase usage, Octopus Cards launched a "Rewards on the Go" promotion for users. In April 2004, the Octopus Online Shopping Mall went live, offering for sale a wide range of Octopus products over the internet.

Projects

Work on the Disneyland Resort Line (formerly the Penny's Bay Rail Link) to the Disneyland Theme Park continued to progress well, with the interconnecting tunnel at Tai Yam Teng completed and handed over to the trackwork contractor, and civil works completed at both stations. Conversion of the rolling stock is on target and all electrical and mechanical contracts are either in manufacture or installation.

In the Tung Chung Cable Car project, the critical stream diversion work at Ngong Ping was completed to facilitate follow-on works, and foundation piling at the Tung Chung Terminal was completed slightly ahead of schedule. The foundations for the Airport Island Angle Station were laid and a specialist project management consultant appointed for the Ngong Ping Village Specialist Attractions. Throughout, we have worked closely with local stakeholders and environmental groups to ensure a socially and environmentally appropriate approach.

MTR continued to work with the Government to explore options for extending the urban railway network. A project proposal for an extension of the Kwun Tong Line to Whampoa Gardens was submitted in February 2004. A revised proposal for the West Island Line and South Island Line was submitted in March 2004 and is under review by the Government.

In March, the Company signed a project agreement with Hong Kong IEC Limited to construct the new AsiaWorld-Expo Station at the end of AEL at Hong Kong International Airport. The station will give direct access to the AsiaWorld-Expo (formerly the International Exhibition Centre) via two link bridges and is designed to handle peak passenger flows, using both Tung Chung Line and AEL trains. Construction work began in June 2004 with a target opening date of December 2005.

Expansion outside Hong Kong

As I mentioned in the 2003 Annual Report, MTR is determined to expand our business outside of Hong Kong to enhance value for our shareholders. The first example of this expansion is the Shenzhen Line 4 Project where we signed an Agreement in Principle with the Shenzhen Municipal People's Government in January 2004 to build Phase 2 of Line 4 and to operate both Phase 1 and Phase 2 of Line 4 for a period of 30 years.

Under the agreement, MTR will construct a double-track line between Shaoniangong and Longhua town, including two underground and seven above-ground stations. The Shenzhen project follows our well proven "rail and property model". Initial design of the property development schemes is now underway, and the first development package is expected to be issued for tender at the end of 2005, subject to detailed planning and market conditions. Construction of Phase 2 is scheduled to begin in 2005 after finalising the concession and operating agreements which are subject to Central Government approval and operation is expected in 2008. The total project cost of Phase 2 is estimated at RMB6 billion of which RMB2.4 billion is expected to be capital injection from MTR. With the current investment climate in China, it is possible that the approval process of the Shenzhen project may take longer than originally expected.

In April 2004, the Company signed a Memorandum of Understanding with Beijing Infrastructure Investment Company Limited and Beijing Capital Group. The intention is to form a Public-Private Partnership for the procurement management of electrical and mechanical systems for, and operation of the Beijing Metro Line 4 project, one of the major infrastructure projects to prepare for the 2008 Olympic Games.

As noted in the 2003 Annual Report, we intend to explore growth opportunities outside Hong Kong but we also recognise the associated risk. Hence, investments will be analysed prudently with return requirements commensurate with the risk assumed. We will continue to focus on projects where MTR can add value through the significant experience developed in all our businesses.

Possible merger between MTR and KCRC

As noted in the 2003 Annual Report on 24 February 2004, Government invited MTR and KCRC to commence discussions on a possible merger under five set parameters. Since the announcement, a significant amount of work has been done in close co-operation with KCRC which will allow the two companies to present a joint proposal to Government by the deadline of 31 August 2004.

The Government's parameters will be carefully weighed against the terms of the merger to ensure that any transaction will be value enhancing to MTR, our shareholders and other capital providers. The possible merger will be a connected transaction and therefore will require independent shareholders' approval. Stakeholders should note that there is no assurance at this time that a merger will be implemented.

Financial review

Total revenue for the first half year was HK$3,987 million, a significant increase of 11.8% from the same period last year during which the Hong Kong economy was severely affected by the outbreak of SARS. As a result, total fare revenue increased by 11.8% to HK$2,871 million during the period, with substantial improvement in the patronage of both the MTR Lines and AEL of 12.0% and 32.5% respectively. With continued fare promotions and concessions, average fares on the MTR Lines declined by 2.1% to HK$6.50 in the first half of 2004 compared to HK$6.64 for the same period last year.

Non-fare revenue including property investment revenue grew strongly by 11.6% to HK$1,116 million mainly due to significant increases in advertising, telecommunication and property rental income. With the end of SARS, the growth in advertising and telecommunication income was helped by a recovery in consumer spending during the period. The increase in property rental income was mainly attributable to rent increases upon tenancy renewals in our shopping centres.

Operating costs before depreciation increased by 1.0% to HK$1,769 million as compared with the same period last year, mainly due to higher maintenance cost resulting from the expiry of warranty periods in respect of most of the Tseung Kwan O Line assets, together with higher station commercial and property rental expenses owing to expanded business activities in these areas. However, these increases were partially offset by lower staff and related costs resulting from the effect of continued cost control measures and reduction in pension expenses. In comparing the prior period, there was an operational rate adjustment of HK$46 million in the first half of 2003. Had this adjustment been excluded, there would have been a reduction of HK$28 million or 1.6% in operating cost in the first six-month of 2004 when compared to the same period 2003.

Operating profit from railway and related operations before depreciation was HK$2,218 million, an increase of 22.1% compared to the same period last year, resulting in an operating profit margin of 55.6%, an increase of 4.7 percentage points when compared with the same period last year.

Property development profit of HK$1,153 million was recognised in the first half of 2004 mainly from deferred income relating to Caribbean Coast at Tung Chung Station and The Harbourside at Union Square, Kowloon Station, as well as profit on sale of properties held at Sorrento, Kowloon Station. As a result, operating profit for the Company before depreciation was HK$3,371 million for the first six months of 2004, an increase of 35.2% compared with the same period last year.

Depreciation charges increased by 4.9% to HK$1,251 million mainly due to the commissioning of the West Rail Interchange facilities in December 2003. Net interest expenses decreased by 9.8% to HK$743 million due to lower interest rates and reduced borrowing. Deferred income tax expense was HK$221 million. As in prior years, this deferred income tax is a non-cash item. Together with the Company's share of Octopus Cards Limited's earnings of HK$20 million, the Group's profit attributable to shareholders for the first half year was HK$1,175 million, a significant increase compared to the same period last year. Earnings per share rose to HK$0.22 compared with HK$0.02 in the comparable period last year.

The Directors have declared an interim dividend of HK$0.14 per share, which is the same as last year. As with previous dividend payments, a scrip dividend option will be offered to all shareholders with a Hong Kong address. As reported in the 2003 Annual Report, the Government has agreed to extend scrip dividend arrangements for another three years up to and including dividends declared for the Company's financial year ending 31 December 2006.

The Group's balance sheet remained strong. Shareholders' funds increased to HK$57,778 million with the re-investment of scrip dividends by the Government and other shareholders offset partially by a net reduction in retained profits after payment of the 2003 final dividend. Major capital outlays for the half-year period related to the expenditure on the Disneyland Resort Line, the Tung Chung Cable Car project and other capital improvement projects. During the period, the Group was able to reduce its gross borrowings from HK$32,025 million at year-end 2003 to HK$31,736 million at the end of June 2004, resulting in the gross debt-to-equity ratio reducing from 55.9% to 54.9%. Netting off the cash balances on our balance sheet, the Group's net debt-to-equity ratio as at 30 June 2004 was 54.3% compared with 55.2% as at 31 December 2003.

The Group's cash outflows for the six months ended 30 June 2004 amounted to HK$3.3 billion, which included capital payments for the Disneyland Resort Line and other capital projects for the existing railway system, net loan repayments as well as interest and dividends paid. These payments were financed partly by the net cash inflow from operating activities, and partly by proceeds from properties sold and cash surplus brought forward from 2003.

Financing activities

In January this year, the Group took advantage of favourable issuing conditions in the US dollar market and successfully launched a US$600 million 10-year Eurobond at an attractive re-offer spread of 83 basis points over the comparable yield of 10-year US treasuries. The offering attracted total subscriptions of close to US$1.9 billion from over 130 investors represented by a diverse group of institutional investors including banks, insurance companies, pension funds and money managers. This financing not only enabled the Group to further extend our debt maturity profile, but also set a new 10-year US dollar benchmark for Hong Kong's quasi-sovereign credits.

At the end of June 2004, the Group had undrawn committed facilities totaling HK$5.6 billion, which would be sufficient to cover all of our projected funding needs well into the third quarter of 2005.

In the first half of 2004, the Group continued to manage our debt portfolio in accordance with our Preferred Financing Model to achieve a well-balanced debt profile with adequate risk diversification. As at 30 June 2004, the debt portfolio had a well-balanced spread of maturities, with 25% repayable within 2 years, 31% due between 2 and 5 years, and 44% maturing beyond 5 years. In total, 72% of the borrowings were based on fixed interest rates, and 98% were either denominated in or hedged into Hong Kong dollars, with the remaining 2% held in US dollars.

As a result of the continuing low interest rates and attractive terms of new financings obtained, the Group was able to reduce its borrowing cost further during the period to 4.8% from 5.4% in 2003.

Human resources

During the first half-year of 2004, the Company continued to improve staff productivity, with the number of staff reduced to 6,570 as at 30 June 2004.

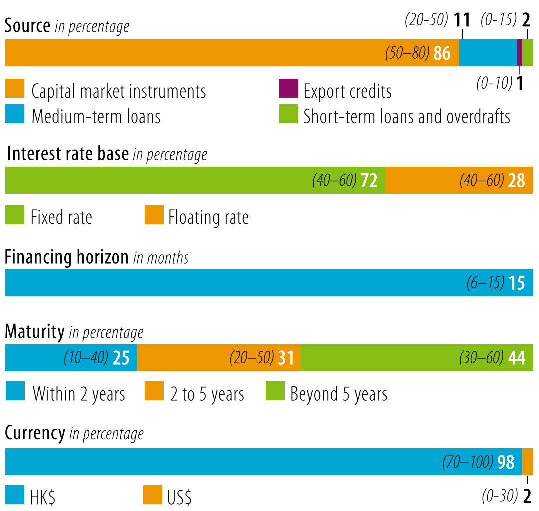
Following announcement by the Government inviting the Company and KCRC to commence discussion on the possible merger, extensive staff communication was immediately initiated. To strengthen corporate governance, the Code of Conduct was updated to reflect the latest regulatory requirements and a guidebook was prepared to provide more specific guidelines on employee behaviour.

Subsequent to the revision of the Vision, Mission and Core Values, a six-month communication programme was launched to promote staff understanding and adoption of the new direction. Results of the Staff Attitude Survey conducted at the end of 2003 showed staff sentiment at MTR continue to stay above the Hong Kong norm in almost all areas, and the Company will

Preferred financing model and debt profile

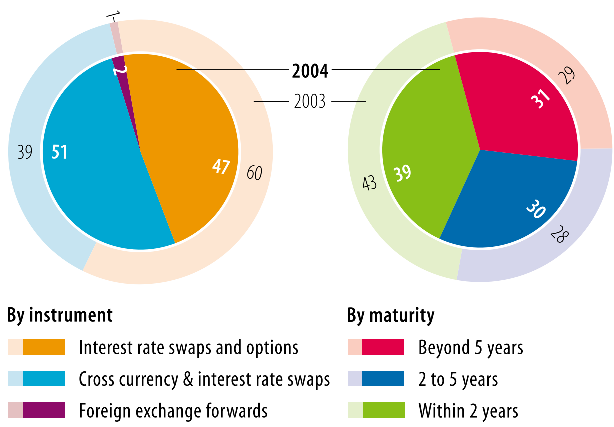
(Preferred Financing Model) vs. **Actual debt profile**

As at 30 June 2004



Use of interest rate and currency risk hedging products

Percentage (As at 30 June 2004)



continue to strive for further improvements. During the first half of 2004, a total of 21,900 man-days of training were completed. Our effort in staff training and development was recognised by the Hong Kong Management Association with the "Most Innovative Award" for Excellence in Training 2004.

Outlook

Looking into the second half of 2004, we see continuous improvement in the Company's recurring revenues, reflecting the growth of the Hong Kong economy.

Further improvement in patronage

Patronage in our rail network should continue to improve, supported by improving economic conditions and increased visitor arrivals, particularly from the Mainland as more cities are added to those permitting individual travels. We are also hopeful that interchanging passenger flow from KCRC's West Rail will increase as the public becomes more aware of the convenience and benefits offered by our interchange. This will be partially offset by some loss of patronage when the KCRC Tsim Sha Tsui Extension opens in the second half of the year.

MTR is committed to improving station environments to enhance passenger comfort and experience. We aim to complete retrofitting of platform screen doors on 10 more platforms at five stations by the end of 2004. We will also work closely with our external pedestrian link partners, the Government and private developers to create further pedestrian links.

Stable environment for property businesses

The property market appears to be entering a period of relative stability and this should be supportive of all our property businesses. At Tseung Kwan O Area 86 we anticipate making available the first package of the "Dream City" for development by year-end, involving some 2,000 flats. As noted in the 2003 Annual Report, in our property development business during the second half, we expect profit contribution from receipt of our share of Phase 1 of the shell of the retail centre in Union Square in Kowloon. This shell will require internal fit out and decoration over the next two years. We also expect to book profits from deferred income relating to Coastal Skyline and Caribbean Coast (Tung Chung Packages Two and Three respectively) as well as some surplus proceeds from The Harbourside at Union Square. The timing of recognition of other property development profits will be dependent on stages of completion and pre-sales for deferred income, and generally the issuance of occupation permits for profit sharing.

Construction of the Olympic Package Three superstructure and the Tiu Keng Leng Station Development, and of town houses at Coastal Skyline Phase 2 at Tung Chung Station will continue. Pre-sales of units at Tiu Keng Leng and Choi Hung stations are planned for the second half of the year. In the second half of 2004, we will open the new "sports city" at Olympic Station.

Our commercial investment properties should benefit from the sustained recovery in retail spending and we will take advantage of this through promotional campaigns, effective management and continuous enhancement of trade mix at our shopping centres. Discussions currently underway with prospective tenants of Two IFC are also expected to lead to further commitments over the coming months.

The stability in the property market and improved end-user sentiment should support our property management and property agency businesses. Our property management portfolio is expected to grow further in the second half of 2004 when an estimated 2,362 units will be added from completion of The Harbourside and Caribbean Coast.

Further inroads are also expected in the Mainland property management market where our management portfolio will increase to 1,800 units after completion of Beijing Palm Springs International Apartment in Beijing, Chongqing Springs International Phase 1 in Chongqing, and The Image of North Europe in Shenzhen.

Steady growth in other businesses

The steady improvement in patronage and rebound in retail activities will help improve our station commercial and advertising businesses.

The ongoing programme to renovate stations and advertising formats will continue to boost the Company's advertising and kiosk rental revenues. During the second half of the year, we plan to complete renovations at nine more stations.

New projects continue on schedule

Our two leisure related projects on Lantau Island are expected to achieve major milestones during the second half of the year. The Disneyland Resort Line will see the commencement of running of engineer's works trains, dynamic testing of trains and track energisation. The project is expected to meet its target completion date of mid-2005 and be well within the budget estimate.

For the Tung Chung Cable Car project, construction of the terminals, angle stations and Theme Village will continue, whilst completion of the public transport interchange entrusted works at Ngong Ping is expected by November.

Investments outside Hong Kong

For the Shenzhen Line 4 project, we shall continue our negotiations with the Shenzhen Municipal People's Government. Given the current investment climate, however, there may be delays in the finalisation of the operating and concession agreements. We will also forge ahead with discussions with Beijing Infrastructure Investment Company Limited and Beijing Capital Group on the Beijing Line 4 project with the aim of progressing our Memorandum of Understanding towards an Agreement in Principle.

C K Chow, *Chief Executive Officer*

Hong Kong, 3 August 2004