Chairman's letter

Dear Stakeholders,

I have the pleasure of presenting to you the 2003 results of MTR Corporation Limited (MTR).

Firstly, I would like to welcome Mr. C K Chow as the Company's Chief Executive Officer. C K brings with him extensive management experience in publicly-listed, multinational companies and with his roots in Hong Kong is the ideal person to lead MTR forward, as the Company enters a new era of development both locally and abroad. I would also like to thank again Mr. Jack So for his leadership and contribution over his eight years as MTR's Chairman and Chief Executive, during which time MTR had gone from strength to strength. Thanks are also due to Mr. Philip Gaffney for his excellent work as Acting CEO following Jack's departure and prior to C K's appointment, which ensured a smooth management transition.

Despite the challenges and difficulties in 2003, MTR achieved good results mainly due to very significant property development profits. Net profit for the year was HK$4,450 million, an increase of 24.3% over 2002 (as adjusted for the revised accounting standard on deferred income tax). Correspondingly, earnings per share increased by 21.4% to HK$0.85 per share. The Board proposed a final dividend of HK$0.28 per share which when combined with the interim dividend of HK$0.14 per share will result in total dividends for 2003 of HK$0.42.

The outbreak of Severe Acute Respiratory Syndrome (SARS) was the single most difficult challenge MTR faced in 2003. It put a lot of strain on our system but at the end, through the hard work and dedication of our staff, especially those at the front line, we ensured the health and safety of our passengers, customers and tenants. I must therefore commend our staff for the courage and professionalism that they exhibited during this crisis.

During the year, the issue of fare discounts and fare setting mechanism continued to attract much public discussion. From its inception, fare autonomy has been the cornerstone of MTR's business model and success. In assessing fares we must take into consideration all our stakeholders, including shareholders and debt holders who require reasonable risk adjusted returns from their investments. However, we are also sensitive to the needs of the travelling public and recognise that the Company's ultimate success depends on its ability to deliver quality service in a competitive market. We are mindful of the economic conditions and deflationary environment in Hong Kong and have introduced a number of initiatives to offer relief to our passengers. These initiatives include the "Ride 10 Get 1 Free" scheme which on average benefits 450,000 passengers every week.

It is important to point out that having completed the Airport Railway and the Tseung Kwan O Line in the past few years, the Company has seen certain costs such as interest and depreciation charges increase significantly by about 220% between 1997 and 2003. With the two additional lines, in this same six years period, the number of car kilometres run has increased by 52.0% to 128 million kilometres but patronage has reduced by 4.3% due to the economic slowdown in Hong Kong. As a result, fare box revenues are insufficient to meet operating expenses of the rail network. It has to be augmented by non-fare revenues, property rental and property development profits.

During the year, there have also been debates about our property development business. Our business model of "rail plus property development" has served the Company and Hong Kong well for over the past 25 years, and has given Hong Kong a world class urban railway system without costing Government or taxpayers anything. This is a record envied around the world.

In 2002, amid excess supply of flats in the market, we decided in line with Government policy to refrain from tendering out any property development packages in 2003. With the recent recovery in the property market, we are in the process of planning tenders for the packages along the Tseung Kwan O Line in the fourth quarter of 2004. However, it is unlikely that any new flats will be available from these yet to be tendered packages until 2007.

A very exciting development for MTR is the opportunity to invest outside of Hong Kong in areas where the Company has significant knowledge and competence. I am very pleased that our first potential overseas investment is the Shenzhen Line 4 project, which when completed will provide a critical north-south corridor for one of Asia's most dynamic municipalities and set new standards for comprehensive community development in the Mainland. There are other projects which we are discussing in the Mainland as well as in Europe.

We were pleased to note Government's decision to invite MTR and Kowloon-Canton Railway Corporation (KCRC) to commence discussions on the possible merger between MTR and KCRC. We will work with all parties concerned to structure and negotiate this complex transaction, such that the outcome will yield sustainable benefits to Hong Kong's travelling public, rail industry employees and, importantly, our shareholders.

Finally, I would like to thank my fellow directors, management and all staff for their hard work and dedication during 2003. 2004 marks the 25th anniversary of the commencement of MTR's rail services in Hong Kong and also the beginning of an exciting new era of overseas expansion and investments, as well as a possible merger with KCRC. I know that I can count on my colleagues' continued support in this exciting new era.

Raymond K.F. Chien

Dr. Raymond Ch'ien Kuo-fung, *Chairman*
Hong Kong, 2 March 2004