CEO's review of operations and outlook

Dear Stakeholders,

The first six months of 2006 saw a number of significant developments for MTR Corporation. On the possible merger of the rail systems of MTR Corporation and KCRC, a Memorandum of Understanding was signed between Government and the Company on 11 April. In our overseas development, all government approvals were obtained for our 49% owned joint venture company for the Beijing Metro Line 4 project. This was followed by the signing of the Concession Agreement with the Beijing Municipal Government and the commencement of project work.

The Company's financial results for the first half of 2006 benefited from strong property development income and continued growth in our recurring businesses. As a result, revenue increased by 4.1% to HK$4,566 million while operating profit from railway and related operations before depreciation rose by 3.9% to HK$2,639 million. Property development profit realised in the period was HK$4,072 million mainly from the booking of profit from The Grandiose at Tseung Kwan O Station and from Metro Town, Tiu Keng Leng Station Phase One Development. Profit attributable to equity shareholders, excluding gain from revaluation of investment properties net of tax, increased by 123.2% to HK$3,948 million. Gain from investment properties revaluation was HK$1,478 million pre-tax (HK$1,219 million post-tax) resulting in reported net profit of HK$5,167 million, an increase of 98.3% over the corresponding period in 2005. Reported earnings per share increased by 95.8% to HK$0.94. The Board has declared an interim dividend of HK$0.14 per share.

Railway operations

For the first six months of 2006, total fare revenue for the MTR Lines and the Airport Express increased by 5.0% to HK$3,138 million. The MTR Lines recorded total patronage of 418.4 million, a 1.2% increase over the same period last year. The increase reflected the state of Hong Kong's economic activities and opening of the Disneyland Resort Line ("DRL") last August.

Operations performance in first half 2006

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	98.0%	99.0%	**99.9%**
Train punctuality			
– MTR Lines	98.0%	99.0%	**99.7%**
– Airport Express	98.0%	99.0%	**99.9%**
Train reliability: train car-km per train failure causing delays ≥ 5 minutes	N/A	500,000	**1,745,541**
Ticket reliability: magnetic ticket transactions per ticket failure	N/A	8,000	**16,131**
Add value machine reliability	95.5%	98.0%	**99.4%**
Ticket issuing machine reliability	93.0%	98.0%	**99.6%**
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%	**99.9%**
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%	**99.8%**

The Company's overall share of total franchised public transport was 24.7%, comparable to the same period last year. Share of the cross-harbour market was unchanged at 60.4%.

The Airport Express recorded total patronage of 4.5 million during the first half of 2006, an 11.4% increase over the same period last year, but market share dropped slightly from 24% to 23% reflecting intense competition in this sector.

As in prior periods, MTR Corporation continued to meet or exceed the requirements under our Operating Agreement and our own more stringent Customer Service Pledges.

Service improvements during the first six months included installation of new passenger lifts in Cheung Sha Wan and Sham Shui Po stations, completion of new pedestrian links at Choi Hung and Kwai Fong stations, and completion of retrofitting platform screen doors for all 74 platforms in our 30 underground stations on the Island Line, Tsuen Wan Line and Kwun Tong Line.

Continuing efforts were made to further improve the connectivity of the MTR network with other modes of transport, which enhances MTR's attraction to the travelling public. During the period, three new green minibus routes were added to the intermodal fare discount scheme, taking the scheme total to 28, while one new fare saver machine was installed in Tai Kok Tsui, bringing the total to 19 machines.

Station commercial and other businesses

The continued growth of the Hong Kong economy and rising MTR patronage supported further increase in revenue from the Company's station commercial and other businesses. Although reported revenue at HK$735 million showed a 2.5% reduction from the same period last year, this was due to a one-off income received in 2005 from settlement of an early termination of a telecommunication contract which did not repeat in 2006. Revenue for the first half of 2006 also included a small one-off income relating to mobile network upgrade. Excluding these two one-off items, revenue from station commercial and other businesses would have increased by 7.1%.

Advertising revenue increased by 8.6% to HK$239 million, boosted by higher passenger volume. A number of new formats and services were introduced. In May, Real-time Projection Zones went live at eight MTR stations in conjunction with promotion of the Hollywood blockbuster movie *The Da Vinci Code*. A new advertising train, the "Spectacular Mobile Showcase", made its debut in June. These innovative formats demonstrate the Company's commitment to enhancing our leadership position in the out-of-home advertising market in Hong Kong.

Station commercial revenue rose by 15.9% to HK$190 million due to improvements in rental rates and station commercial retail space layout from our station renovation programme, as well as the continued buoyant economy. During the period, retail floor area in stations increased by 134 square metres as new layouts and refurbishments were completed at Po Lam, Ngau Tau Kok and Admiralty stations. However, due to the repossession of 367 square metres of retail space at other stations to facilitate station improvement works, the net retail floor space in the first half was slightly reduced to 18,837 square metres in total. These station improvements, when completed, will benefit future revenue. Also during the period, 12 new shops were added to the MTR station portfolio.

Reported revenue from telecommunications services decreased by 31.3% to HK$138 million, mainly due to the one-off payment received in 2005 for early termination of an agreement which did not repeat in 2006. Excluding this and the one-off income from mobile network upgrade in 2006, revenue would have increased by 3.0%. Our fixed network services provider TraxComm Limited recorded higher revenue and is operating an over 100 Gbps bandwidth network with coverage extended to all major data centres in Hong Kong. However, revenue from mobile services has dropped due to fierce competition amongst operators resulting in lower tariffs, while usage volume remained unchanged.

Octopus Holdings Limited ("Octopus") continued to expand its operations both within and outside the transport sector. Cards in circulation rose to 13.8 million and average daily transaction volume and value rose to 9.3 million and HK$70 million respectively. MTR Corporation's share of Octopus' post-tax earnings increased by 9.1% to HK$28 million for the six-month period.

Revenue from external consultancy was HK$98 million during the six months. The project to construct an Automated People Mover System to connect the Hong Kong International Airport to SkyPlaza and the SkyPier is underway. In Taiwan, two new contracts started in early 2006, one with the Kaohsiung Rapid Transit Company to provide operations and maintenance support for three years to 2009, and the second, with the Taiwan High Speed Rail Company to cover station, train service, and operations control centre management as well as signalling system maintenance for two years to 2008. In the Mainland of China, the Company secured a consultancy contract to provide consultancy for the Integrated Supervision Control System for Beijing Line 5.

Property businesses

While Hong Kong's economy continued to grow in the first half of 2006, sentiment in the residential property market has become more cautious as interest rates continued to trend higher and financial markets around the world became more volatile. As a result, residential property transaction volume declined throughout the period, and prices softened. The office and retail rental sectors however continued to be active in the first half although the rate of growth may slow in the second half.

The Company's profit from property developments in the first half of 2006 was HK$4,072 million. Along the Airport Railway, we recognised profit from deferred income relating to Coastal Skyline and Caribbean Coast in Tung Chung, Harbour Green at Olympic Station and fitting out works for Elements at Kowloon Station, from sharing in kind relating to receipt of a small area of the retail shell of Elements as well as surplus proceeds from The Harbourside at Kowloon Station. Along the Tseung Kwan O Line, as I noted at the time of the 2005 annual results, we booked surplus proceeds from Metro Town, Tiu Keng Leng Station Phase One Development and The Grandiose at Tseung Kwan O Station.

The tender for Package Two of Tseung Kwan O Area 86 was awarded in January to Rich Asia Investments Limited ("Rich Asia"), a subsidiary of Cheung Kong (Holdings) Limited ("Cheung Kong"), and the development agreement was signed in February. This was followed in June by our consent to Cheung Kong's transfer of 15% of its interest in Rich Asia to Nan Fung Development Limited, a wholly owned subsidiary of Chen's Holdings Limited. As part of our strategy to attract better profit sharing from this tender and in line with the tender conditions, the Company has provided an interest-free loan of HK$4,000 million (equal to about half of the land premium) to Rich Asia. This loan is supported by a guarantee from Cheung Kong for the full amount.

Along the Airport Railway, to meet the increased desire for town houses, we have obtained Town Planning Board approval in June to convert the original low-rise residential development to town houses at Caribbean Coast.

Rental income from investment properties increased by 7.8% to HK$624 million supported by higher rents. A vibrant retail sector, further refinements to the trade mix and strong promotional efforts at our shopping centres continued to increase shopper traffic. During the first half of 2006, favourable growth in rental rates was achieved for renewal of leases at our shopping centres.

The continuing demand for high quality retail space enabled us to maintain 100% occupancy levels at all of our shopping centres except for Luk Yeung Galleria, where a total of 427 square metres was repossessed in April in preparation for renovation work. The Company's 18 floors at Two IFC continued to be fully let during the period. A total of 504 parking spaces at No.8 Clear Water Bay Road (including 450 Park & Ride Carpark spaces) were added to the portfolio upon commencement of operation of the carpark.

To enhance the retail environment of Telford Plaza I, a major renovation programme was launched in April to refurbish its entrances, atria, shopfronts, ceilings and floors, with target completion by year-end 2006.

Pre-letting of Elements, the forthcoming 82,750 square metres gross MTR flagship mall at Union Square in Kowloon Station, progressed well, with good response from both overseas and local retailers, as well as food and beverage operators. Pre-letting of The Edge, the new shopping centre of 11,877 square metres gross at Area 55b of Tseung Kwan O Station, also saw good progress.

Our property management business experienced steady growth, with revenue rising 7.8% to HK$69 million. During the period, a total of 2,842 residential units was added to the management portfolio, bringing the total number of residential units under management to 57,200.

Our property management business in the Mainland of China continued to expand with the award in April of a service contract by SOHO Shangdu, a major commercial-cum-shopping mall development in Beijing. The Company will take over management responsibility of this property by the end of 2006.

Renovation of the 31,000 square metres gross shopping centre under a long-term head lease in Beijing's Dong Cheng district is now underway. This shopping centre has been renamed Ginza Mall, and is scheduled to open by early 2007 after major upgrading and refurbishment.

Tseung Kwan O Line property developments (packages awarded)

Location	Developers	Type	Gross floor area (sq. m.)	No. of parking spaces	Status	Actual or expected completion date
Tseung Kwan O Station						
Area 57a	Sun Hung Kai Properties Ltd.	Residential	26,005		Awarded in	Completed in
(Central Heights)	Nan Fung Development Ltd.	Retail	3,637		July 2000	2005
	Henderson Land Development Co. Ltd.	Carpark		74		
	Chime Corporation Ltd.					
Area 55b	New World Development Co. Ltd.	Residential	84,920		Awarded in	Completed in
(The Grandiose	Chow Tai Fook Enterprises Ltd.	Retail	11,877		January 2002	January 2006
and The Edge)	Wee Investments Pte. Ltd.	Carpark		249		
Hang Hau Station	Sino Land Co. Ltd.	Residential	138,652		Awarded in	Completed
(Residence Oasis	Kerry Properties Ltd.	Retail	3,500		June 2002	in 2004
and The Lane)		Carpark		369		
Tiu Keng Leng Station						
(Metro Town	Cheung Kong (Holdings) Ltd.	Residential	236,965		Awarded in	By phases
and Le Point)		Retail	16,800		October 2002	from
		Carpark		609		2006-2007
Tseung Kwan O South Station						
Area 86 Package One	Cheung Kong (Holdings) Ltd.	Residential	136,240		Awarded in	2008
		Retail	500		January 2005	
		Carpark		325		
		Residential Care Home for the Elderly	3,100			
Area 86 Package Two	Cheung Kong (Holdings) Ltd.	Residential	309,696		Awarded in	2009-2010
		Kindergarten	800		January 2006	
		Carpark		905		

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

Location	No. of packages envisaged	Type	Gross floor area (sq. m.)	Expected parking spaces	Period of package tenders	Expected completion date
Tseung Kwan O Station	1-2	Residential	80,000		2006–2007	2011
Area 56		Hotel	58,130			
		Retail	20,000			
		Office	5,000			
		Carpark		390		
Tseung Kwan O South Station	6-11	Residential	1,153,764 – 1,163,764		2007–2011	2014
Area 86		Retail	39,500 – 49,500			
		Carpark		3,533		

* 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	Actual completion date
Choi Hung Station	Chun Wo Holdings Ltd.	Residential	19,135		Awarded in	Completed in
(No. 8 Clear Water Bay Road)		Retail	2,400		July 2001	2005
		Carpark		54		
		Park & Ride		450		

Hong Kong projects

MTR Corporation continued the development and planning of new rail and non-rail projects during the first half of 2006.

"Ngong Ping 360", comprising the Ngong Ping Skyrail and the Ngong Ping Village on Lantau Island, is undergoing pre-opening trials and is expected to open for business later in the year.

Following approval of the revised proposal for the West Island Line by Government and Executive Council last year, discussion with Government is continuing over detailed scope, cost and funding requirements. The decision on the South Island Line (East) proposal is still awaiting completion of Government's review of the Southern District's planning of tourism and commercial development.

In the "Dream City" development at Area 86 in Tseung Kwan O, the construction contract for Tseung Kwan O South Station was awarded in late June. This latest extension to the MTR network is designed to serve the "Dream City" property development and is scheduled to open in 2009.

New pedestrian links in Admiralty and Sheung Wan stations are targeted for opening by the end of this year, and another at Lai Chi Kok Station is planned for completion in 2008. Further license agreements have been signed and are under negotiation with adjacent developers respectively for Tsim Sha Tsui and Choi Hung stations.

At the Hong Kong International Airport, the project to construct a second platform at the departure level of the Airport Station continued with the connection to the Skyplaza retail development and the project is expected to be completed by the end of 2006.

Merger with KCRC

On 11 April, the Company signed a Memorandum of Understanding with Government setting out the terms for the proposed rail merger between the Company and KCRC, together with the acquisition of a property package.

The proposed transaction is subject to approval by both LegCo and independent shareholders of the Company. A Rail Merger Bill was submitted to LegCo by Government on 5 July which was followed by the first meeting of the Bills Committee to examine the Bill on 27 July. We expect the approval processes by LegCo and independent shareholders to take about a year or more from the 11 April announcement day.

An IBC comprising six independent non-executive Directors of the Company has been established to examine the proposed transaction and advise independent shareholders. The IBC will appoint and be advised by an Independent Financial Adviser.

Overseas growth

Mainland of China

In Beijing, the public-private partnership ("PPP") company formed with the Beijing Infrastructure Investment Co. Ltd. and Beijing Capital Group for the Beijing Line 4 project obtained its business license in January, and the related concession, lease and financing agreements were signed in April. With management in place, and the rolling stock and signalling contracts having been awarded, construction of the project has commenced with target completion in 2009.

In Shenzhen, we are still awaiting approval from the National Development and Reform Commission for Shenzhen Metro Line 4. We have put in place a management team which has progressed detailed design of the system, and the master plan for property developments along the line.

In line with our strategy, we have furthered negotiations regarding plans for the investment, construction and operation of Shenzhen Metro Line 3 following the signing of a Memorandum of Understanding ("MoU") last year with the municipal government on this potential 32.8-kilometre line in the eastern part of the municipality. In Beijing, feasibility studies are also progressing on two possible metro lines, one for Beijing Line 4 Extension and the other for Beijing Metro Line 9, following signing of the respective MoU's and Letter of Interest this year.

Elsewhere in the Mainland, the Company submitted an investment proposal to the Wuhan Municipal Government in April following the signing of an MoU with the government in 2005 to explore co-operation opportunities for the construction and operation of metro lines in Wuhan. In May, we signed an MoU with the Hangzhou Municipal Government for a joint study on a metro development plan for that city. However, we must point out that MoU's do not always result in investments.

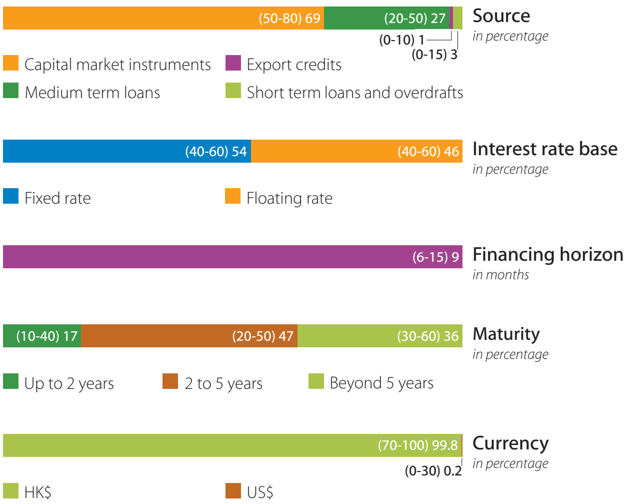
Europe

In Europe, we continued to pursue "asset light" rail operating service contracts during the first half of 2006.

In the UK, a tender for the South Western Train Franchise was submitted in conjunction with our partner National Express in June and the result is expected to be announced by October. A joint venture between MTR Corporation and Laing Rail has been pre-qualified to bid for the London Rail Concession, formerly called the North London Railway Franchise, and is currently working on the tender submission for October. Both of these are competitive tenders where the Company will compete with other bidders.

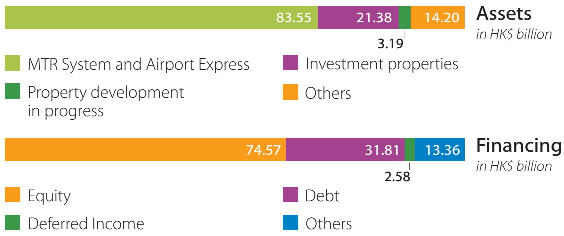
Preferred financing model and debt profile

(Preferred Financing Model) vs. **Actual debt profile** *As at 30 June 2006*



Simplified balance sheet

As at 30 June 2006



Financial review of operations

Revenue for the first half of 2006 was HK$4,566 million, an increase of 4.1% over the same period last year. Revenue from the MTR Lines and the Airport Express reported increases of 4.7% and 7.7% respectively as a result of patronage growth, particularly in the early months of 2006, and an increase in average fare for the MTR Lines. Patronage on the MTR Lines increased 1.2% and on the Airport Express 11.4%, whilst the average fare for the MTR Lines increased 3.5% to HK$6.8 but on the Airport Express decreased 3.2% to HK$64.8 mainly due to the lower fares paid by passengers travelling to the AsiaWorld-Expo Station which opened in December 2005.

Revenue from station commercial and other businesses amounted to HK$735 million, a 2.5% drop from the same period last year due to the one-off income received from settlement of an early termination of a telecommunication contract in 2005 which did not repeat this year. Revenue for the first half of 2006 also included a small one-off income relating to mobile network upgrade. Excluding these two one-off items, revenue from station commercial and other businesses would have increased by 7.1% when compared to the same period last year. Property rental and management income increased 7.8% to HK$693 million.

Operating cost before depreciation for the first half year increased by 4.5% to HK$1,927 million as compared to the same period last year. The increase was mainly due to the opening of DRL and AsiaWorld-Expo Station, increases in expenditures in the development of our overseas growth business in the Mainland and Europe, as well as expenses relating to "Ngong Ping 360". Operating profit from railway and related businesses before depreciation amounted to HK$2,639 million, a 3.9% increase from the same period last year, with an operating profit margin of 57.8%, similar to last year. Excluding the one-off impacts from telecommunication contract termination and mobile network upgrade, operating profit would have increased by 6.7% whilst operating profit margin would have increased by 0.5% point.

Property development profit during the first half year amounted to HK$4,072 million, mainly comprising surplus proceeds from The Grandiose and Metro Town along the Tseung Kwan O Line, deferred income recognition from Coastal Skyline, Caribbean Coast, Harbour Green and Elements along the Airport Railway as well as sharing in kind from the receipt of an additional 572 square metres at Elements. Operating profit before depreciation amounted to HK$6,711 million, an increase of 65.3% as compared to the same period last year.

Depreciation charge for the first half year dropped by 3.5% to HK$1,315 million mainly due to adjustments made for depreciation charges on some systems in the Tseung Kwan O Line and Nam Cheong Station in 2005. Net interest expense increased by 16.6% to HK$739 million mainly due to higher interest rates and increased borrowings as compared to the same period last year. The increase in fair value of investment properties since the end of 2005 amounted to HK$1,478 million pre-tax or HK$1,219 million post-tax.

Including the share of profit from Octopus and the share of cost incurred by the joint venture company for the bidding of the South Western Train Franchise in the UK, profit before taxation for the first half year amounted to HK$6,151 million, a 98.7% increase from the same period last year. Correspondingly, income tax increased by 101.2% to HK$984 million, which was mainly non-cash deferred income tax. The resulting net profit attributable to shareholders for the first half year amounted to HK$5,167 million, an increase of 98.3% compared to the same period last year. Reported earnings per share therefore increased from HK$0.48 for the first half of 2005 to HK$0.94 for 2006. Excluding investment property revaluation gain and related deferred tax, underlying net profit was HK$3,948 million, an increase of 123.2% compared to same period last year.

The Directors have declared an interim dividend of HK$0.14 per share. A scrip dividend option will be offered to all shareholders except those with registered addresses in the United States of America or any of its territories or possessions. As in previous years, Government has agreed to receive its entitlement to dividends in the form of shares to the extent necessary to ensure that a maximum of 50% of the Company's total dividend will be paid in cash.

The Group's balance sheet remains strong. During the first half of 2006, shareholders' equity increased by 6.7% to HK$74,548 million as of 30 June, from retained profit as well as the re-investment of scrip dividends by Government and other shareholders.

Total assets increased by 7.6% to HK$122,318 million mainly due to an interest-free loan of HK$4,000 million (recognised on balance sheet at fair value of HK$3,232 million at inception) provided to the property developer of Tseung Kwan O Area 86 Package Two as part of the tender terms, an increase of HK$2,053 million on properties held for sale from unsold units at Metro Town and The Grandiose along the Tseung Kwan O Line, gross revaluation gain on properties of HK$1,770 million, and increases in amount receivable in respect of property developments of HK$957 million. Other increases in assets include capital expenditures incurred on the "Ngong Ping 360" project and other capital improvement projects.

The Group's net cash inflow generated from railway and related activities increased to HK$2,737 million in the first half of 2006 compared to HK$2,562 million for the same period in 2005, whilst cash receipts from developers for property development project decreased to HK$584 million from HK$2,332 million in 2005. Total cash outflow rose from HK$3,095 million to HK$6,366 million which included the HK$4,000 million interest-free loan for Package Two of Tseung Kwan O Area 86, capital project payments of HK$1,339 million, interest expenses of HK$830 million and other minor items. The Group had a net cash outflow of HK$3,045 million before dividend as compared to a net cash inflow of HK$1,799 million in the same period last year. After the dividend payment of HK$767 million and net loan drawdowns of HK$3,824 million, there was a net cash inflow of HK$12 million.

During the period, total borrowings of the Group increased from HK$28,264 million to HK$31,809 million due mainly to amounts drawn to finance the interest-free loan to the developer. As a result, the debt-to-equity ratio increased from 40.4% at 31 December 2005 to 42.7% at period-end.

Financing activities

The credit markets continued to see high levels of liquidity, leading to tight credit spreads. Given this favourable environment, we successfully arranged total financings of HK$3.1 billion during the first half of 2006, including a HK$500 million 4.3% 2-year fixed rate note, and a number of 5-year and 7-year bilateral facilities totalling HK$2.6 billion. As at the end of June 2006, the Group had total undrawn committed facilities of HK$2.9 billion, which together with cash on hand and projected significant positive cash flows from our property development business, are expected to cover all of the Company's estimated funding needs until the first quarter of 2007.

As at the end of June, the Company's debt portfolio was well balanced with 17% of total outstanding repayable within 2 years, 47% between 2 and 5 years, and 36% beyond 5 years. As a measure of exposure to foreign currency risk, only 0.2% of the debt portfolio was denominated in US dollars with the remainder either hedged into or denominated in HK dollars.

At the end of June, 54% of the debt portfolio was based on fixed interest rates with the balance based on floating rates. This prudent level of fixed rate debt, together with the attractive terms of the Group's financings, has enabled the Company to contain our financing cost in a rising interest rate environment. As a result, despite the significant increase in short-term interest rates during the first half of 2006 as compared with the same period last year, the Company's average borrowing cost rose to 5.5% from 5.0%.

In the Mainland of China, agreements for two project loans of RMB1.6 billion each provided separately by China Development Bank and Industrial and Commercial Bank of China for the development and construction of Beijing Metro Line 4 were signed by the associated PPP company in April.

Human resources

Immediately following signing of the Memorandum of Understanding on the proposed merger, the Company held a total of 60 briefing sessions to provide staff with the latest information and opportunities to raise their concerns. Going forward, we will regularly update our staff on the merger using a variety of means such as staff communication sessions, merger newsletters, *MTR Express*, Corporate Notices and additional briefing sessions.

We are committed to looking after the interests of all staff, and will consult them on matters affecting them during the merger process before any final decisions are made. To ensure that best practices are adopted for the merged company, the Company in conjunction with KCRC has commenced a series of in-depth studies on different aspects of human resources integration such as grading and reward structure, and employment terms and conditions.

Outlook

Although business conditions remain generally positive in Hong Kong, successive interest rate increases coupled with high oil and commodity prices have slowed the rate of economic growth. While there was patronage growth in the early months of 2006, MTR Lines patronage in May and June was lower than last year due to the combination of the impact of Football World Cup and slower growth of economic activities. Although MTR Lines patronage growth has resumed in the last two weeks of July, it would be prudent to adopt a cautious outlook for the rail and related businesses in the second half. On the other hand, although competition continues to increase, we see positive rental reversions in our property investment business. Given this environment we continue to pay close attention to cost and enhance efficiency whilst at the same time continuing our efforts in the overseas growth business.

In our property development business we recognised profit from both The Grandiose at Tseung Kwan O Station and Metro Town, Tiu Keng Leng Station Phase One Development in the first half of 2006. For the balance of the year, in line with our accounting treatment, property development profit recognition is expected to come mainly from developments along the Airport Railway, particularly from deferred income and the expected receipt as sharing in kind of a small area of some 7,100 square metres gross at Elements in Kowloon Station. In Tseung Kwan O, property development profit recognition in the second half would depend on sales progress of the 390-unit development at Central Heights Tseung Kwan O Town Centre Area 57a. Given that most of the property development profit for 2006 has been recognised in the first half, the amount of development profit to be recognised in the second half is expected to be significantly less.

Finally, I would like to take this opportunity to thank all my colleagues for their hard work and support.

C K Chow, *Chief Executive Officer*
Hong Kong, 10 August 2006