PROFIT AND LOSS

CASH FLOW

STATEMENT OF FINANCIAL POSITION

FINANCING CAPACITY

FINANCING ACTIVITIES

Financial Review

Profit and Loss

The Group's businesses consist of (i) recurrent businesses (comprising Hong Kong Transport Operations, Hong Kong Station Commercial Businesses, Hong Kong Property Rental & Management Businesses, Mainland of China and International Railway, Property Rental and Management Businesses and Other Businesses) and (ii) property development businesses (together with recurrent businesses referred to as underlying businesses).

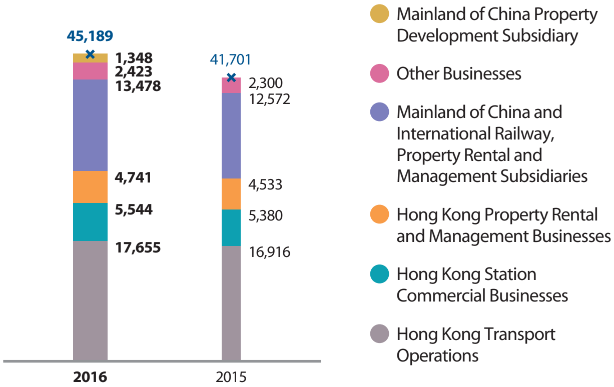
In 2016, the Group recorded reasonable profits from our recurrent businesses and modest profits from our property development businesses.

Net profit attributable to shareholders of the Company is arrived at after adjusting for the underlying business profit with any gain or deficit arising from investment property revaluation, which is a non-cash accounting item.

The financial review of the Group's total revenue, underlying business profit and net profit attributable to shareholders of the Company is provided in the following sections.

Total Revenue

Total Revenue by Business
(HK$ million)



In 2016, the Group recorded revenue growth in all business segments. Total revenue increased by 8.4% to HK$45,189 million, reflecting mainly the contributions from Tiara, railway subsidiaries outside of Hong Kong, as well as the adjustment in fares under the FAM, net of fare concessions.

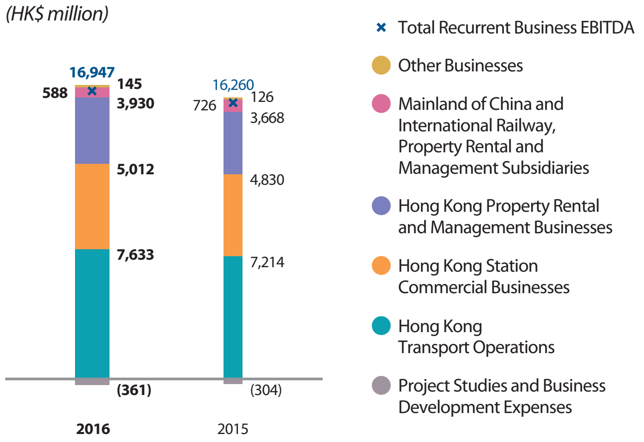
Underlying Business Profit and Net Profit Attributable to Shareholders of the Company

HK$ million		2016		2015	2016 vs 2015 Increase/(Decrease)	
Recurrent Businesses						
EBITDA		**16,947**		16,260	687	4.2%
Depreciation and Amortisation		**(4,127)**		(3,849)	278	7.2%
Variable Annual Payment		**(1,787)**		(1,649)	138	8.4%
EBIT		**11,033**		10,762	271	2.5%
Interest and Finance Charges		**(702)**		(616)	86	14.0%
Share of Profit or Loss of Associates		**537**		361	176	48.8%
Income Tax		**(1,858)**		(1,798)	60	3.3%
Non-controlling Interests		**(94)**		(144)	(50)	(34.7%)
Recurrent Business Profit		**8,916**		8,565	351	4.1%
Property Development Businesses						
Post-tax Property Development Profit						
– Hong Kong Property Development	**267**		2,416		(2,149)	(88.9%)
– Mainland of China Property Development	**263**		(87)		350	N/A
Post-tax Property Development Profit		**530**		2,329	(1,799)	(77.2%)
Underlying Business Profit		**9,446**		10,894	(1,448)	(13.3%)
Investment Property Revaluation		**808**		2,100	(1,292)	(61.5%)
Net Profit Attributable to Shareholders of the Company		**10,254**		12,994	(2,740)	(21.1%)
Earnings per Share (in HK$)		**HK$1.74**		HK$2.22	(HK$0.48)	(21.6%)
Earnings per Share on Underlying Business Profit (in HK$)		**HK$1.61**		HK$1.87	(HK$0.26)	(13.9%)
Total EBITDA Margin(in %)		**38.3%**		38.7%	(0.4%)	pt.
Total EBITDA Margin (excluding Mainland of China and International Subsidiaries) (in %)		**53.9%**		53.3%	0.6%	pt.
Total EBIT Margin^ (in %)		**25.2%**		25.5%	(0.3%)	pt.
Total EBIT Margin (excluding Mainland of China and International Subsidiaries)^ (in %)		**34.8%**		34.8%	–	pt.
Return on Average Equity Attributable to Shareholders of the Company Arising from Underlying Businesses (in %)		**5.9%**		6.5%	(0.6%)	pt.

^ *Excluding Profit on Hong Kong Property Development and Share of Profit or Loss of Associates*

Recurrent Business EBITDA

Recurrent Business EBITDA by Business
(HK$ million)



Recurrent Business Profit

Recurrent business profit grew by 4.1% to HK$8,916 million, mainly due to increase in share of profit from associates of Mainland of China and international railway, higher EBIT of Hong Kong Property Rental and Management Businesses and Hong Kong Station Commercial Businesses, partly offset by decrease in EBIT of subsidiaries of Mainland of China and International Railway, Property Rental and Management Businesses. Further details of the divisional performance are set out in the ensuing paragraphs.

Post-tax Property Development Profit

Post-tax property development profit in 2016 was HK$530 million, mainly derived from Tiara in Shenzhen and sundry income sources in Hong Kong. This was HK$1,799 million lower than 2015 when substantial profit was recognised from Hemera.

Dividend

In line with the Company's progressive ordinary dividend policy, the Board has proposed a final ordinary dividend of HK$0.82 per share (with a scrip dividend option offered), giving a full year ordinary dividend of HK$1.07 per share, higher than the HK$1.06 per share in 2015.

Recurrent Businesses

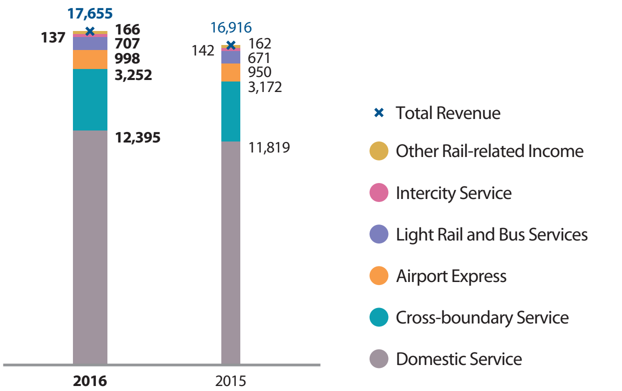
Hong Kong Transport Operations

HK$ million	2016	2015	2016 vs 2015 Increase/(Decrease)	
Total Revenue	**17,655**	16,916	739	4.4%
Total Expenses	**(10,022)**	(9,702)	320	3.3%
EBITDA	**7,633**	7,214	419	5.8%
EBIT*	**2,572**	2,493	79	3.2%
EBITDA Margin (in %)	***43.2%***	*42.6%*	*0.6%*	*pt.*
EBIT Margin (in %)*	***14.6%***	*14.7%*	*(0.1%)*	*pt.*

* *EBIT represents EBITDA net of depreciation, amortisation and variable annual payment*

Total Revenue

(HK$ million)



Total revenue increased mainly due to the adjustment in fares under the FAM, net of concessions. Average fares for the Domestic Service increased by 4.3%, Cross-boundary Service by 3.4%, Light Rail by 4.3% and Bus Service by 3.7%. Average fares for Airport Express and Intercity services, which are not subject to FAM, increased by 2.4% and 5.3% respectively. Total patronage of all our rail and bus passenger services increased by 0.5% to 1,948.8 million, partially explained by the opening of two new lines in the second half. Total expenses increased mainly owing to increased train trips and staff salaries. Depreciation and amortisation charges increased by 7.0% to HK$3,780 million, mainly due to new asset additions in the Hong Kong railway network. Variable annual payment to KCRC increased by 7.9% to HK$1,281 million as the incremental fare revenue was charged at the top progressive rate of 35%. As a result, EBIT increased by 3.2% to HK$2,572 million and EBIT margin decreased by 0.1 percentage point to 14.6%.

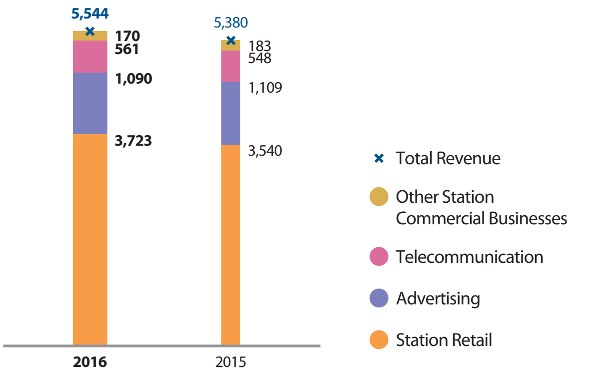
Hong Kong Station Commercial Businesses

HK$ million	2016	2015	2016 vs 2015 Increase/(Decrease)	
Total Revenue	**5,544**	5,380	164	3.0%
Total Expenses	**(532)**	(550)	(18)	(3.3%)
EBITDA	**5,012**	4,830	182	3.8%
EBIT*	**4,362**	4,230	132	3.1%
EBITDA Margin (in %)	***90.4%***	*89.8%*	*0.6%*	*pt.*
EBIT Margin (in %)*	***78.7%***	*78.6%*	*0.1%*	*pt.*

* *EBIT represents EBITDA net of depreciation, amortisation and variable annual payment*

Total Revenue

(HK$ million)



Total revenue increased by 3.0% mainly due to higher station retail revenue, as rents increased resulting from trade mix refinements, positive rental reversions in station shops and increases in base rents in accordance with lease contracts of Duty Free Shops at Lo Wu and Hung Hom stations. In addition, telecommunication revenue increased due to incremental revenue from mobile data capacity enhancement. The increases were partly offset by mild decreases in revenue from advertising and other station commercial businesses. Total expenses decreased due to lower agency fees relating to advertising business. Variable annual payment to KCRC increased by 9.6% to HK$502 million owing to a higher level of revenue subject to variable annual payment. As a result, EBIT increased by 3.1% to HK$4,362 million and EBIT margin increased by 0.1 percentage point to 78.7%.

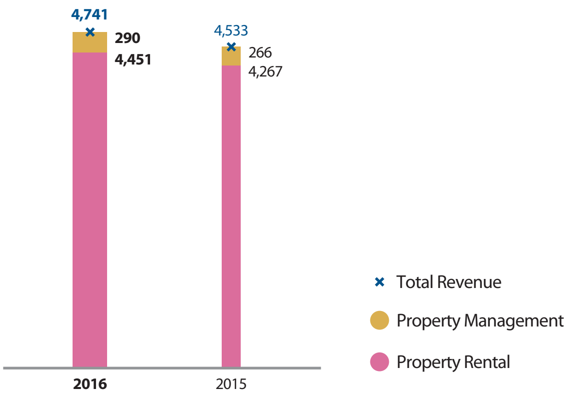
Hong Kong Property Rental and Management Businesses

HK$ million	2016	2015	2016 vs 2015 Increase/(Decrease)	
Total Revenue	**4,741**	4,533	208	4.6%
Total Expenses	**(811)**	(865)	(54)	(6.2%)
EBITDA	**3,930**	3,668	262	7.1%
EBIT*	**3,912**	3,650	262	7.2%
EBITDA Margin (in %)	***82.9%***	*80.9%*	*2.0%*	*pts.*
EBIT Margin (in %)*	***82.5%***	*80.5%*	*2.0%*	*pts.*

* *EBIT represents EBITDA net of depreciation, amortisation and variable annual payment*

Total Revenue

(HK$ million)



Property rental income increased due to the favourable rental reversion at an average of 3.4% in 2016 in our shopping malls. Our shopping malls and the Company's 18 floors in Two International Finance Centre remained close to 100% let as at 31 December 2016. Property management income increased due to higher expenditure in managed properties and the full 12-month impact of new residential units taken up in 2015. Total expenses decreased from 2015 when a one-off provision was made. As a result, EBIT increased by 7.2% to HK$3,912 million and EBIT margin increased by 2.0 percentage points to 82.5%.

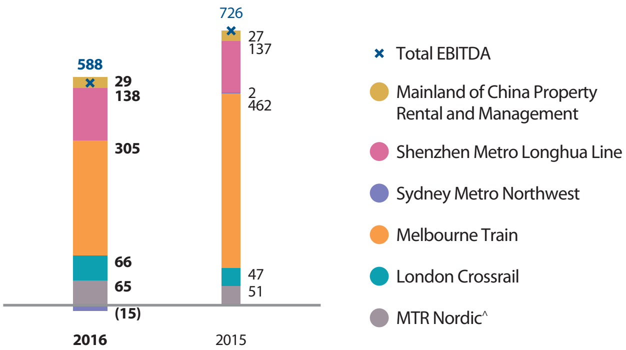
Mainland of China and International Railway, Property Rental and Management Subsidiaries

HK$ million	2016	2015	2016 vs 2015 Increase/(Decrease)	
Total Revenue	**13,478**	12,572	906	7.2%
Total Expenses	**(12,890)**	(11,846)	1,044	8.8%
EBITDA	**588**	726	(138)	(19.0%)
EBIT#	**468**	633	(165)	(26.1%)
EBITDA Margin (in %)	***4.4%***	*5.8%*	*(1.4%)*	*pts.*
EBIT# Margin (in %)	***3.5%***	*5.0%*	*(1.5%)*	*pts.*

\# *EBIT represents EBITDA net of depreciation and amortisation*

EBITDA

(HK$ million)



^ *Representing businesses in Sweden which include MTR Nordic AB, MTR Tunnelbanan AB, MTR Tech AB, MTR Express (Sweden) AB & MTR Pendeltågen AB*

Total revenue increased by 7.2%, total expenses by 8.8%, and total EBITDA decreased by 19.0%, mainly due to refranchising costs, lower contribution from maintenance and overhaul activities and lower profit from project activities of Melbourne Train of MTM in Australia. In Sweden, the higher EBITDA of Nordic Group was mainly due to acquisition of the remaining 50% shares of Tunnelbannan Teknik Stockholm in February 2016, which became our subsidiary and renamed as MTR Tech AB, partly offset by mobilisation and operating costs incurred by MTR Pendeltågen AB. In the United Kingdom, the higher EBITDA of London Crossrail of MTRXR was due to its full 12-month contributions in 2016 since the franchise commencement in May 2015. In Mainland of China, EBITDA of Shenzhen Metro Longhua Line maintained at a level similar to 2015. Total depreciation and amortisation charges increased by 29.0% to HK$120 million mainly due to the full 12-month operations of MTR Express and MTRXR. As a result, EBIT decreased by 26.1% to HK$468 million and EBIT margin decreased by 1.5 percentage points to 3.5%.

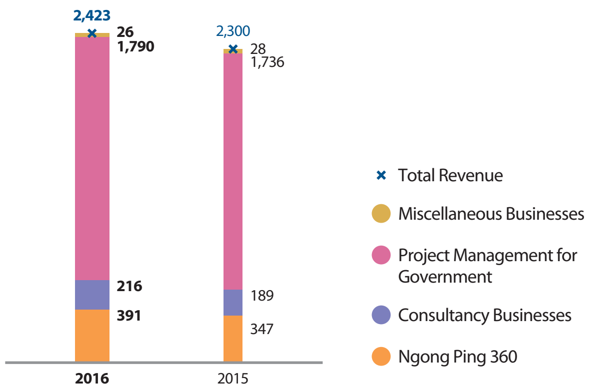
Other Businesses

HK$ million	2016	2015	2016 vs 2015 Increase/(Decrease)	
Total Revenue	**2,423**	2,300	123	5.3%
Total Expenses	**(2,278)**	(2,174)	104	4.8%
EBITDA	**145**	126	19	15.1%
EBIT*	**80**	60	20	33.3%
EBITDA Margin (in%)	***6.0%***	*5.5%*	*0.5%*	*pt.*
EBIT Margin (in%)*	***3.3%***	*2.6%*	*0.7%*	*pt.*

* *EBIT represents EBITDA net of depreciation and amortisation*

Total Revenue

(HK$ million)



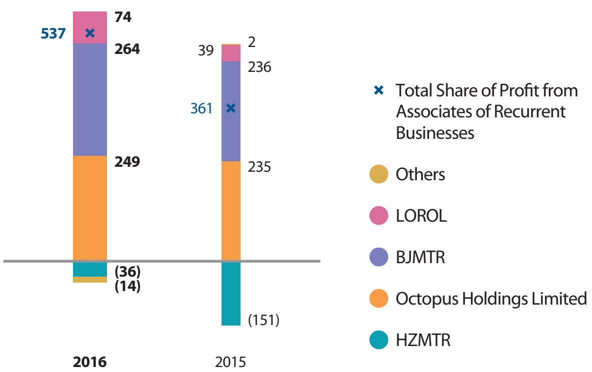
Income from project management services to Government is predominately from entrustment works on the Express Rail Link and Shatin to Central Link. Such income increased by 3.1% to HK$1,790 million. Income from the entrustment works is booked on a cost recovery basis. Revenue from Ngong Ping 360 increased due to the fare rise effective from 1 January 2016 and increase in visitor numbers brought about by 7.5 more operating days in 2016. Total expenses increased in line with the revenue growth. EBIT increased by 33.3% to HK$80 million and EBIT margin increased by 0.7 percentage point to 3.3%.

Depreciation and Amortisation

Depreciation and amortisation increased mainly due to new asset additions in our Hong Kong railway network.

Share of Profit from Associates of Recurrent Businesses

(HK$ million)



Share of profit from associates of recurrent businesses increased primarily due to improvement in the result of HZMTR, which benefited from HZL1 patronage growth, as well as higher share of profits from BJMTR, mainly resulting from a full 12-month profit contribution from BJL14 concession.

Property Development Businesses

Post-tax Profit from Hong Kong Property Development

Post-tax profit from Hong Kong Property Development in 2016 was mainly derived from sundry income sources such as the sharing in kind of the kindergarten at Hemera and sales of inventory units. This was HK$2,149 million lower than 2015 when substantial property development profit was recognised from Hemera.

Post-tax Profit from Mainland of China Property Development

Post-tax profit from Mainland of China Property Development in 2016 was derived from profit recognition of the first batch of units handed over at Tiara. In 2015, Tiara recorded operating loss of HK$140 million, being mainly sales and marketing expenses.

Statement of Financial Position

HK$ million	At 31 December 2016	At 31 December 2015	2016 vs 2015 Increase/(Decrease)	
Fixed Assets	**201,942**	175,719	26,223	14.9%
Railway Construction in Progress	**–**	19,064	(19,064)	(100.0%)
Property Development in Progress	**17,484**	17,983	(499)	(2.8%)
Interests in Associates	**7,015**	5,912	1,103	18.7%
Debtors, Deposits and Payment in Advance	**4,073**	5,135	(1,062)	(20.7%)
Cash, Bank Balances and Deposits	**20,290**	12,318	7,972	64.7%
Other Assets	**6,536**	4,972	1,564	31.5%
Total Assets	**257,340**	241,103	16,237	6.7%
Total Loans and Other Obligations	**(39,939)**	(20,811)	19,128	91.9%
Creditors and Accrued Charges	**(30,896)**	(22,860)	8,036	35.2%
Amounts Due to Related Parties	**(11,783)**	(1,858)	9,925	534.2%
Obligations Under Service Concession	**(10,507)**	(10,564)	(57)	(0.5%)
Deferred Tax Liabilities	**(12,125)**	(11,209)	916	8.2%
Other Liabilities	**(2,534)**	(3,630)	(1,096)	(30.2%)
Total Liabilities	**(107,784)**	(70,932)	36,852	52.0%
Net Assets	**149,556**	170,171	(20,615)	(12.1%)
Represented by:				
Total Equity Attributable to Shareholders of the Company	**149,461**	170,055	(20,594)	(12.1%)
Non-controlling Interests	**95**	116	(21)	(18.1%)
Total Equity	**149,556**	170,171	(20,615)	(12.1%)

Fixed Assets and Railway Construction in Progress

Net increase in fixed assets and railway construction in progress was due to capitalisation of further construction costs of the South Island Line and Kwun Tong Line Extension, as well as renewal and upgrade works for our existing Hong Kong railway network. Upon the opening of the South Island Line and Kwun Tong Line Extension, the construction costs under railway construction in progress were transferred to fixed assets.

Debtors, Deposits and Payment in Advance

Debtors, deposits and payment in advance decreased mainly due to receipts of surplus proceeds from Hemera in Hong Kong.

Cash, Bank Balances and Deposits

Cash, bank balances and deposits increased mainly due to cash inflow from operating activities, proceeds of drawdown of part of the HK$25 billion syndicated loan and from the US$600 million Green Bond issuance, cash receipts in respect of Hong Kong and Mainland of China property developments, partly offset by dividend payments and capital expenditure.

Total Loans and Other Obligations

Total loans and other obligations increased mainly due to the drawdown of part of the HK$25 billion syndicated loan and the issuance of US$600 million Green Bond.

Creditors and Accrued Charges

Creditors and accrued charges increased mainly due to the accrual for the second tranche of special dividend under the XRL Agreement for independent shareholders, sales proceeds received in advance from Tiara and deposit received from the property developer in relation to Ho Man Tin Station Package One.

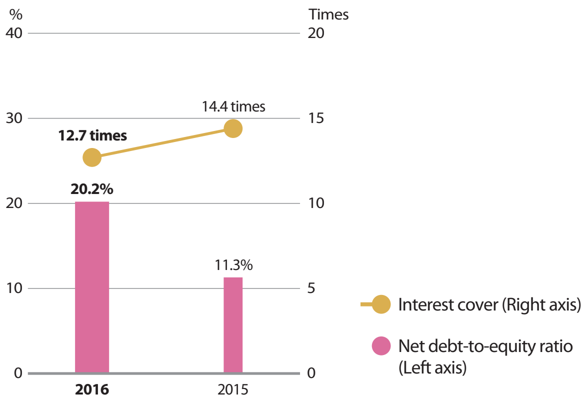
Amounts Due to Related Parties

Amounts due to related parties increased mainly due to the accrual for the second tranche of special dividend under the XRL Agreement to the Government.

Total Equity

The decrease in total equity of HK$20,615 million was mainly due to the accounting for the HK$25,902 million special dividend paid and payable under the XRL Agreement.

Debt Servicing Capability

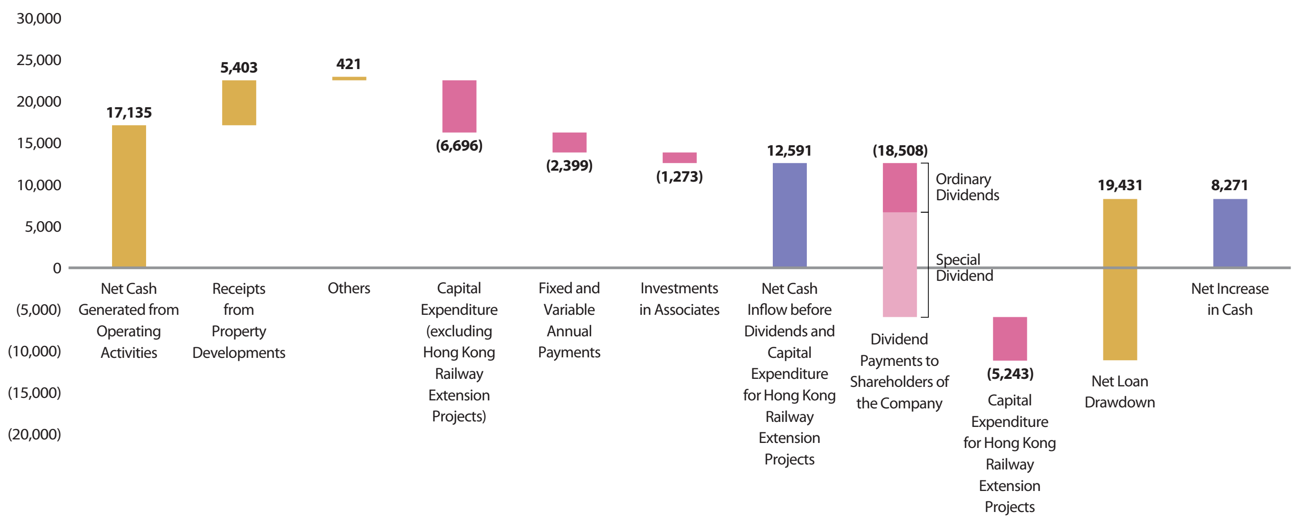


Cash Flow

HK$ million	2016	2015
Net Cash Generated From Operating Activities	**17,135**	14,941
Receipt from Hong Kong Property Development	**2,177**	2,707
Receipt from Shenzhen Longhua Depot Property Development	**3,226**	5,527
Other Receipts	**1,160**	940
Net Cash Receipts	**23,698**	24,115
Capital Expenditure	**(11,939)**	(21,670)
Fixed Annual Payment	**(750)**	(750)
Variable Annual Payment	**(1,649)**	(1,472)
Net Interest Payment	**(519)**	(577)
Investments in Associates	**(1,273)**	(61)
Other Payments	**(112)**	(241)
Dividends Paid to Shareholders of the Company	**(18,508)**	(5,748)
Dividends Paid to Holders of Non-controlling Interests	**(108)**	(157)
Total Cash Outflow	**(34,858)**	(30,676)
Net Cash Outflow before Financing	**(11,160)**	(6,561)
Net Loan Drawdown	**19,431**	154
Increase/(Decrease) in Cash	**8,271**	(6,407)
Cash, Bank Balances and Deposits as at 1 January	**12,318**	18,893
Increase/(Decrease) in Cash	**8,271**	(6,407)
Effect of Exchange Rate Changes	**(299)**	(168)
Cash, Bank Balances and Deposits as at 31 December	**20,290**	12,318

Cash Flow for the Year Ended 31 December 2016

(HK$ million)



Investments in Associates

Investments in associates in 2016 mainly related to equity contribution made to BJMTR to support our investment in BJL14.

Dividend Payments to Shareholders of the Company

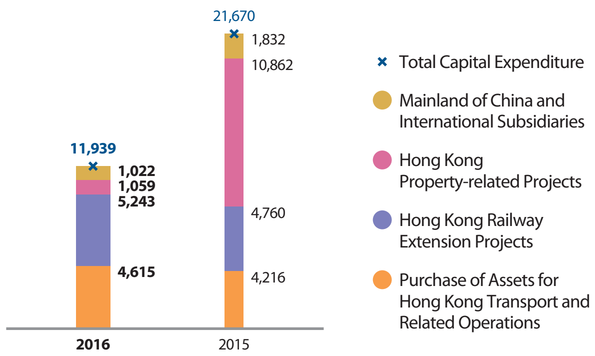
Dividend payments to shareholders of the Company in 2016 included an amount of HK$12.9 billion being the first tranche of special dividend paid under the XRL Agreement.

Net Loan Drawdown

Net loan drawdown in 2016 mainly related to the drawdown of part of the HK$25 billion syndicated loan, as well as the US$600 million Green Bond issuance.

Capital Expenditure

(HK$ million)



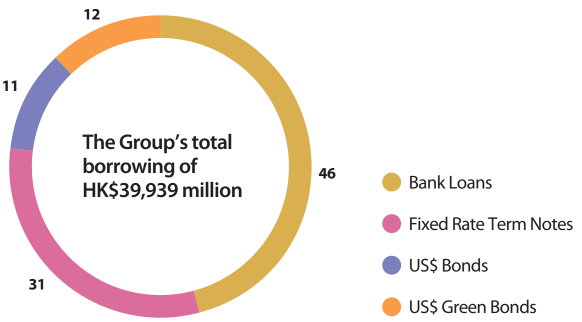
Financing Activities

Sources of Borrowing

Our strategy is to continually diversify funding sources and to maintain ready access to both loan and debt capital markets

(As at 31 December 2016)

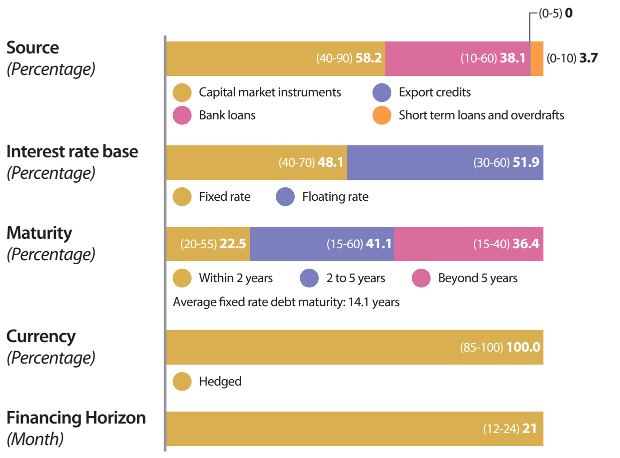
(Percentage)



Preferred Financing Model and Debt Profile

The Preferred Financing Model exemplifies the Company's prudent approach to debt management and helps ensure a prudent and well-balanced debt portfolio

(Preferred Financing Model) vs. **Actual debt profile** *As at 31 December 2016*



Despite continuing strengthening of the U.S. economy and warning from the U.S. Federal Reserve on additional rate hikes, long-term interest rates declined for much of 2016, accentuated by global economic and political uncertainties, including the shock decision by the U.K. to exit the E.U.. In the circumstances, the 10-year US Treasury yield declined to an all-time low of 1.36% p.a. in July.

Against the backdrop of an expected Fed rate hike that materialised in December, Treasuries tumbled after the U.S. presidential election on fear that the tax cut and infrastructure investment plans proposed by the then President-elect would significantly increase federal government debt and inflation. This sent treasury yields surging with the 10-year US Treasury yield ending the year much higher at 2.44% p.a..

The Company took advantage of the attractive market window before the significant rise in long-term interest rates after the U.S. election to expand its fixed rate debt portfolio and extend duration, resulting in the amount of net fixed rate debt increasing from HK$9,477 million at the end of 2015 to HK$17,692 million at the end of 2016 with average maturity extended from 12.0 years to 14.1 years.

Amongst its various fixed rate debt issues was the Group's debut US$600 million 10-year Green Bond issued in November. Launched at US$500 million in October based on the Group's newly established Green Bond Framework, which is aligned with the Green Bond Principles of International Capital Market Association, the issue met with strong interest from institutional investors from across Asia and Europe, many of whom dedicated green bond investors. This resulted in an order book in excess of US$1.4 billion, allowing the deal to be upsized to US$600 million and priced at 80 basis points, at the tight end of the indicated price range, over the benchmark 10-year US Treasury yield of 1.737% p.a. for an overall yield of 2.537% p.a..

The Green Bond has allowed the Company to tap into a new and fast expanding base of green bond investors as an additional funding source and to use the funds to finance its various environmentally friendly service and projects as envisaged in Rail Gen 2.0 whilst at the same time playing a role in helping Hong Kong to develop as a regional green finance hub.

The Bond was awarded "Best Green Bond" deal in the "FinanaceAsia Achievement Awards 2016" and is currently included in a number of green bond indices, including Barclays MSCI Green Bond Index, BofA Merrill Lynch Green Bond Index, Solactive Green Bond Index and S&P Green Bond Index.

In addition to the Green Bond, the Company's other fixed rate debt issuances include a number of HK and US dollar long-term fixed rate notes. Totalling about HK$3 billion, these notes were issued through private placement with maturities ranging from 15 to 35 years at attractive fixed interest rates, which helped further extend and diversify debt maturity profile.

Another major funding exercise completed during the year was a HK$25 billion syndicated loan facility signed in June with 21 major banks from across Asia, Australia, the Middle East, Europe and North America. Launched at HK$15 billion but increased to HK$25 billion on the back of substantial over-subscription, the facility comprises a HK$12.5 billion 3-year term loan and a HK$12.5 billion 5-year revolving credit facility. All-in pricing of the 3-year term loan was the lowest in the HK dollar loan market since the 2008 Global Financial Crisis and that of the 5-year revolving facility was also the lowest amongst the outstanding 5-year facilities then. Usage of proceeds of the facility is for general corporate purposes.

Cost of Borrowing

The Group's consolidated gross debt position increased from HK$20,811 million at year-end 2015 to HK$39,939 million at year-end 2016. The weighted average borrowing cost of the Group decreased to 2.9% p.a. from 3.5% p.a. due to a combination of a higher proportion of floating rate debt in the portfolio as well as lower floating interest rates and average fixed rate borrowing cost.

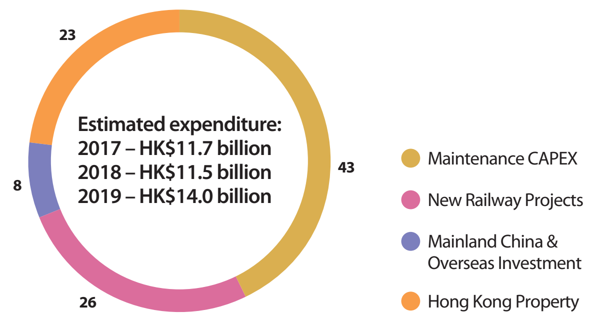
Financing Capacity

The Group's capital expenditure programme consists of three parts – Hong Kong railway projects (including maintenance), Hong Kong property investment and development, and Mainland of China and overseas investments.

Capital expenditure for Hong Kong railway projects comprises investment in and expenditure relating to the new ownership projects of the South Island Line (East) and the Kwun Tong Line Extension, as well as outlays for maintaining and upgrading existing rail lines. Capital expenditure for concession projects of the Express Rail Link (for project cost of up to HK$84.42 billion) and the Shatin to Central Link ("SCL") are generally funded by the Government and therefore not included in the Group's capital expenditure programme, although for SCL the Company will share certain costs for the rolling stock and signalling systems attributable to the East Rail and Ma On Shan lines.

Capital Expenditure and Investment (2017 – 2019)

Total spending for the next three years from 2017 to 2019 is estimated at HK$37.2 billion
(Percentage)



Capital expenditure for Hong Kong property investment and development is comprised mainly of costs associated with work for property development, fitting-out and the renovation of shopping centres, and payments of development costs for certain property development projects. Expenditure for Mainland of China and overseas investment consists primarily of equity contribution to Beijing Metro Line 16 project and the Sydney Metro Northwest project.

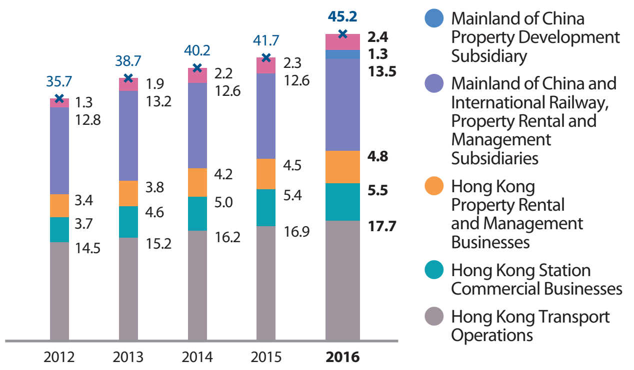
The Group believes that based on its available cash balance and unused committed banking facilities, as well as its ready access to both the loan and debt capital markets, it will have sufficient financing capacity to fund the above capital expenditure projects and the special dividend of approximately HK$13 billion to be paid in 2017.

Credit ratings	Short-term*	Long-term*
Standard & Poor's	A-1+/A-1+	AAA/AAA
Moody's	-/P-1	Aa1/Aa1
Rating & Investment Information, Inc. (R&I)	a-1+	AA+

* *Ratings for Hong Kong dollar/foreign currency denominated debts respectively*

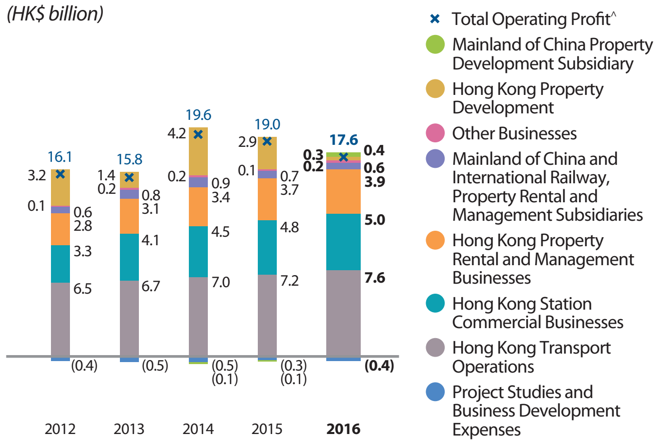
Total Revenue

(HK$ billion)



Operating Profit^ Contributions

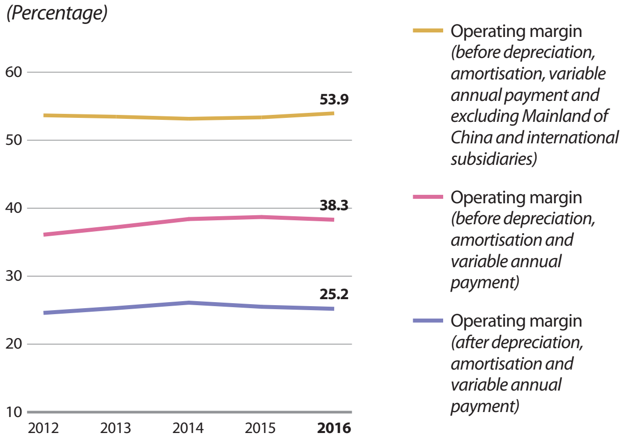
(HK$ billion)



^ *Representing operating profit before depreciation, amortisation and variable annual payment*

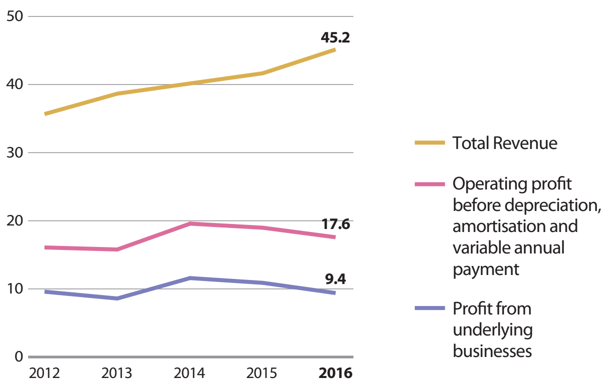
Operating Margin

(Percentage)



Net Results from Underlying Businesses

(HK$ billion)



Fixed Assets Growth

(HK$ billion)