

**Letterhead of Baring Asset Management**

*Syd Bone*  
*Managing Director*

3 December, 1999

By fax # 2121 0420 & by post

The Clerk to the Bills Committee On Mass Transit Railway Bill  
3/F Citibank Tower  
3 Garden Road  
Hong Kong

Dear Sirs,

I refer to your letter of 16 November concerning the Mass Transit Railway Bill. You have asked for a written submission.

**GENERAL**

Baring Asset Management (Asia) Limited is a professional investment management organisation investing primarily into shares listed on stock markets in Asia Pacific including Hong Kong. We do this on behalf of a large number of clients either in segregated accounts or through mutual funds we offer. Total assets invested are in excess of US\$2.0 billion. Our investment approach is to create portfolios of shares which are actively managed against benchmark indices on a risk controlled basis. As such we would look to have holdings in major sectors of the key markets in the region. In Hong Kong's case this would include utilities. At present the choice in this sector is limited and excludes railways. The latter would be an important diversification option for regional and global equity portfolios. The listing of MTRCL would thus be welcomed by us and very likely by our industry generally.

**SPECIFICS**

The government would retain a majority stake. This would be necessary in order that the credit rating would be maintained in the medium term. As MTRC will require debt financing e.g. the new projects such as Junk Bay line will need huge amount of long-term financing, it is crucial that cost of capital be kept as low as possible. Currently MTRC enjoys the same credit rating as Hong Kong government. A minority stake by the government of less than 50% could potentially lead to downgrade by credit agencies.

Letter to The Clerk to the Bills Committee

On Mass Transit Railway Bill

Page 2

It is very important that MTRCL has full fare autonomy. There is a risk that this may not be the case in practice due to political pressure. The latter is most likely to be applied at difficult times —economically for the economy as a whole and financially for MTRCL itself. If the market perceives a risk in this area, the stock P/E will be rated down accordingly.

There is no problem in the Government continuing to promote healthy competition with KCRC and others, provided that this is indeed the case in practice. The government should clearly demonstrate arms length decision making in relation to new project opportunities.

Where new projects are offered, MTRCL should be free to decide for itself on the viability of the projects from a pure business perspective. Incentives in the area of property development rights are entirely reasonable and in fact would probably be a central plank of the business proposition in any case.

It is in MTRCL's own business interests to maintain a proper and efficient service. By all accounts it is already a global leader in this area. Any deterioration would have business implications in many ways without the government needing to get involved - passenger usage rates, preference for competitor product, and declining reputation to name a few. We suggest the main risk of this happening would be unreasonable constraint on fares which reinforces the need for autonomy in this area.

The length of the franchise (50 years) may become a problem for MTRCL in the future. It is understood that the period of time needed to amortise up front expenditure on new rail projects is very long. It may well be that the franchise length may end up impeding MTRCL's ability to participate in new projects unless clear compensation is available for assets and associated unamortised expenditure outstanding at the end the franchise period.

**SUMMARY**

In summary, we applaud the proposal to form the MTRCL. We trust that it will be allowed to operate on a fully arm's length basis in relation to focus on profitability, shareholder financial returns, management control, fares autonomy, new project assessment, and operational efficiency.

Yours sincerely,

Syd Bone  
Managing Director