

**BILLS COMMITTEE ON MASS TRANSIT RAILWAY BILL**

**FARE AUTONOMY FROM A CREDIT RATING PERSPECTIVE**

**PURPOSE**

At the Bills Committee on 10 December 1999, Members requested the Administration to arrange for more financial experts to appear before the Committee to give testimony in relation to the proposed partial privatisation of the Mass Transit Railway Corporation (MTRC). In response to this request, the Administration has arranged for the following persons to attend the meeting of the Bills Committee on 16 December 1999: -

Mr. Fan JIANG  
Executive Director  
Goldman Sachs (Asia)

Mr. Paul COUGHLIN  
Managing Director  
Standard & Poor's International Ratings

Mr. Leonard WEI  
Managing Director  
The Chase Manhattan Bank

2. Set out in the following paragraphs are the opinions of Mr. Coughlin on MTRC's privatisation from a credit rating agency perspective. Messrs. Jiang and Wei will present their views to the Bills Committee from an institutional bond investor angle and a lending bank perspective respectively.

## **BACKGROUND ON STANDARD & POOR'S (S&P)**

3. S&P is a global organisation which assigns credit ratings to companies, governments, and other organisations, and to debt securities which these organisations issue. It is well respected internationally for its financial analysis and for its independent, unbiased and expert opinions. S&P has been assigning ratings to MTRC for well over a decade. Currently, S&P assigns an “A+” local currency credit rating to MTRC, which is at the same level as the sovereign rating of HKSAR Government. This reflects not only MTRC’s solid operational record and adequate financial profile, but also its ownership by and strong support from the HKSAR Government.

## **S&P'S VIEWS**

4. S&P considers that, as the backbone of Hong Kong’s public transport network, MTRC has historically enjoyed strong Government support since its inception. This is illustrated by the Government’s substantial direct equity contributions and the supportive policy environment it provides. S&P’s current rating assumes that MTRC’s basic commercial framework and its current fare setting mechanism (i.e. autonomy subject to market competition) will be preserved over the long term.

5. MTRC has substantial capital programmes, including the Tseung Kwan O extension and improvements to the existing system. S&P expects MTRC to maintain an adequate financial profile despite continued substantial capital expenditures. Railway earnings are expected to be supplemented substantially in the years ahead by contributions from property development

along the Airport Railway and the proposed Tseung Kwan O Extension, as well as the increased patronage these developments will generate.

6. S&P considers that the partial privatisation of MTRC may be positive as it will likely endorse and reinforce the company's commercial principles. As MTRC is wholly owned by the Government, S&P's rating reflects not only the Corporation's solid operating record and adequate financial performance, but also the strong support from the Government. This support has been evidenced by the Government's equity injections and the property development rights it has granted. The MTRC management has the autonomy to manage MTRC according to commercial principles, including the autonomy to set fares. S&P considers that changes in credit status could occur, depending on the regulatory structure which is developed, as the Government reassesses its relationship with an enterprise that also has private shareholders. The Government, MTRC, and the Legislative Council will need to agree on a suitable regulatory framework that will reflect the interest of the public and of private shareholders.

7. S&P will be monitoring the privatisation process closely to assess the rating implications. Specifically, it will monitor developments with fare setting arrangements, support for MTRC's commercial viability, and the continuance of generally supportive arrangements for a company engaged in a capital intensive business in which commercial outcomes are often difficult to predict.

**ADVICE SOUGHT**

8. Members are requested to note the contents of this paper.

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**Transport Bureau**  
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