



# 中航興業有限公司

CHINA NATIONAL AVIATION COMPANY LIMITED

(incorporated in Hong Kong with limited liability)

## INTERIM RESULTS 2003

The Board of Directors (the “Directors”) of the China National Aviation Company Limited (the “Company”) hereby presents the unaudited condensed consolidated interim results of the Company and its subsidiaries (collectively the “Group”) for the six months ended 30th June 2003 as set out below:

### CONDENSED CONSOLIDATED PROFIT AND LOSS ACCOUNT

For the six months ended 30th June 2003

		Unaudited	
		Six months ended 30th June	
		2003	2002
	Note	HK\$'000	HK\$'000
Turnover		513,526	486,186
Other revenues		8,209	7,446
Total revenues		521,735	493,632
Staff costs		117,017	69,992
Passenger catering and service costs		31,392	31,386
Fuel costs		82,261	46,566
Route operating costs		131,862	98,948
Aircraft maintenance costs		76,049	35,048
Aircraft leases and equipment costs		170,844	94,483
Depreciation and amortisation costs		45,772	21,368
Sales and promotion costs		24,906	27,968
Other operating costs		32,192	14,831
Total operating expenses		712,295	440,590
Operating (loss)/profit	2	(190,560)	53,042
Finance costs		–	(8,426)
Share of losses less profits of associated companies		(98,606)	153,535

(Loss)/profit before taxation		<b>(289,166)</b>	198,151
Taxation	3	<b>39,083</b>	(36,733)
(Loss)/profit after taxation		<b>(250,083)</b>	161,418
Minority interests		<b>68,796</b>	(24,189)
(Loss)/profit attributable to shareholders		<b>(181,287)</b>	137,229
Proposed interim dividends	4	<b>9,938</b>	19,916
Basic (loss)/earnings per share	5	<b>(HK5.47 cents)</b>	HK4.21 cents
Diluted earnings per share	5	<b>N/A</b>	HK4.14 cents

Notes:

### 1. Segment information

The Group is principally engaged in the provision of aviation related services.

An analysis of the Group's revenues and results for the period by business segments is as follows:

	<b>Unaudited</b>				<b>Group</b>
	<b>Six months ended 30th June 2003</b>				
	<b>Property holding</b>	<b>Airline operation</b>	<b>Airport ground handling</b>	<b>Logistics and other businesses</b>	<b>HK\$'000</b>
	<b>(note)</b>	<b>HK\$'000</b>	<b>HK\$'000</b>	<b>HK\$'000</b>	<b>HK\$'000</b>
Segment revenues	—	<b>516,044</b>	—	—	<b>516,044</b>
Segment results	—	<b>(176,428)</b>	—	—	<b>(176,428)</b>
Interest income					<b>5,691</b>
Unallocated costs					<b>(19,823)</b>
Operating loss					<b>(190,560)</b>
Finance costs					—
Share of losses less profits of associated companies	—	<b>(128,961)</b>	<b>34,909</b>	<b>(4,554)</b>	<b>(98,606)</b>
Loss before taxation					<b>(289,166)</b>
Taxation					<b>39,083</b>
Loss after taxation					<b>(250,083)</b>
Minority interests					<b>68,796</b>
Loss attributable to shareholders					<b>(181,287)</b>

	Unaudited				Group HK\$'000
	Property holding (note) HK\$'000	Airline operation HK\$'000	Airport ground handling HK\$'000	Logistics and other businesses HK\$'000	
Segment revenues	<u>5,644</u>	<u>481,315</u>	<u>–</u>	<u>–</u>	<u>486,959</u>
Segment results	<u>4,719</u>	<u>56,193</u>	<u>–</u>	<u>–</u>	60,912
Interest income					6,673
Unallocated costs					<u>(14,543)</u>
Operating profit					53,042
Finance costs					(8,426)
Share of profits less losses of associated companies	–	109,908	45,311	(1,684)	<u>153,535</u>
Profit before taxation					198,151
Taxation					<u>(36,733)</u>
Profit after taxation					161,418
Minority interests					<u>(24,189)</u>
Profit attributable to shareholders					<u>137,229</u>

*Note:* The Group's airline operation and certain of airport ground handling businesses were acquired from China National Aviation Corporation (Group) Limited ("CNACG"), the immediate holding company, on 25th March 2002 and on the same date, the Group's property holding business was vested in CNACG.

## 2. Operating (loss)/profit

Operating (loss)/profit is stated after charging the following:

	Unaudited	
	Six months ended 30th June 2003 HK\$'000	2002 HK\$'000
Amortisation of intangible assets		
– Goodwill	<b>9,419</b>	4,709
– Trademarks	–	11
– Deferred expenditure	<b>76</b>	114
Cost of inventories expensed	<b>20,867</b>	7,987
Depreciation of fixed assets	<b>36,277</b>	16,534
Outgoings in respect of investment properties	<u>–</u>	<u>925</u>

### 3. Taxation

Hong Kong profits tax has been provided at the rate of 17.5% (six months ended 30th June 2002: 16%) on the estimated assessable profit for the period. Macau Complementary Tax has been provided at the rate of 15.75% (six months ended 30th June 2002: 15.75%) on the estimated assessable profit for the period. Taxation on overseas profits has been calculated on the estimated assessable profit for the period at the rates of taxation prevailing in the countries in which the Group operates.

The amount of taxation (credited)/charged to the condensed consolidated profit and loss account represents:

	<b>Unaudited</b>	
	<b>Six months ended 30th June</b>	
	<b>2003</b>	<b>2002</b>
	<b>HK\$'000</b>	<b>HK\$'000</b>
Company and subsidiaries:		
Hong Kong profits tax	–	379
Macau Complementary Tax	–	6,203
Overseas taxation	<b>386</b>	209
Deferred taxation	<b>(27,702)</b>	2,757
	<hr/>	<hr/>
	<b>(27,316)</b>	9,548
Share of taxation attributable to associated companies	<b>(11,767)</b>	27,185
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	<b>(39,083)</b>	36,733
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### 4. Proposed interim dividends

	<b>Unaudited</b>	
	<b>Six months ended 30th June</b>	
	<b>2003</b>	<b>2002</b>
	<b>HK\$'000</b>	<b>HK\$'000</b>
Interim, proposed, of HK0.3 cent (six months ended 30th June 2002: HK0.6 cent) per ordinary share ( <i>note</i> )	<b>9,938</b>	19,916
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*Note:* At a meeting held on 5th September 2003, the Directors declared an interim dividend of HK0.3 cent per share for the year ending 31st December 2003. This proposed dividend is not reflected as a dividend payable in these condensed accounts, but will be reflected as an appropriation of retained earnings for the year ending 31st December 2003.

### 5. (Loss)/earnings per share

The calculations of basic and diluted (loss)/earnings per share are based on the Group's loss attributable to shareholders of HK\$181,287,000 (six months ended 30th June 2002: profit attributable to shareholders of HK\$137,229,000).

The basic (loss)/earnings per share is based on the weighted average of 3,316,939,359 (six months ended 30th June 2002: 3,261,674,714) ordinary shares in issue during the period. No diluted loss per share for the six months ended 30th June 2003 is presented as the exercise of options is anti-dilutive. The diluted earnings per share for the six months ended 30th June 2002 was based on 3,318,075,642 ordinary shares which was the number of ordinary shares in issue during that period plus the weighted average 56,400,928 ordinary shares which would be issued at no consideration on the exercise of all dilutive options.

## **MANAGEMENT DISCUSSION AND ANALYSIS**

### **Review of Operations and Prospects**

For the first six months of 2003, the Group recorded a loss of HK\$181.3 million, compared to a profit of HK\$137.2 million recorded in the first half of 2002.

The Group started off apparently well in the beginning of 2003 even though its airline operations had been slightly impacted by the higher fuel cost due to the Iraqi war. However, the outbreak of atypical pneumonia or Severe Acute Respiratory Syndrome (“SARS”) in China mainland, Hong Kong and Taiwan region quickly brought substantial drop in passenger traffic from mid March onwards. The Group recognized the imminent severe impact of SARS on the revenues of its airline operations and aviation related businesses, and issued a profit warning on 15th April, 2003. Since the containment of the SARS outbreak and the lifting of the World Health Organisation’s (“WHO”) travel advisories on the Greater China region towards the end of the second quarter, passenger traffic has been recovering gradually.

The turnover and operating results of the Group for the period under review were HK\$513.5 million and a loss of HK\$190.6 million respectively, compared to HK\$486.2 million and a profit of HK\$53.0 million respectively for the corresponding period in 2002. The increase in turnover for the period under review was due to the full period effect of the Group’s acquisition in March 2002 of China National Aviation Corporation (Macau) Company Limited (“CNAC Macau”), which includes Air Macau Company Limited (“Air Macau”).

#### **Air Macau Company Limited**

Although there was no outbreak of SARS in Macau, Air Macau suffered negative impact with sharp fall in passenger traffic since some major cities of China mainland and Taiwan region imposed preventive measures such as travel restrictions and passengers quarantine on arrival. During the first half of 2003, the number of passenger flights operated decreased by 30.3 per cent over the same period of 2002. As at 30th June 2003, Air Macau operated to 7 destinations in Asia, 3 of which were in China mainland. Before the SARS outbreak, Air Macau had been operating passenger services to 16 destinations in Asia, of which 9 were in China mainland. Air Macau currently has sales offices and agents in 25 cities, employing a workforce of approximately 800 staff.

For the first six months ended 30th June 2003, Air Macau recorded substantial declines of 33.9 per cent and 45.6 per cent in revenue and total number of passengers carried respectively over the same period of 2002. The available seat kilometre and revenue passenger kilometre decreased by 28.9 per cent and 41.5 per cent respectively as compared to the same period of last year. Despite substantial cuts in flight service operation, the average passenger load factor still dropped by 12.7 percentage points to 58.5 per cent as compared to the same period of last year. Yield per passenger for the first six months of 2003 increased slightly by 3.4 per cent.

The impact on cargo flight operation by SARS was much less, despite the fact that the cancellation of passenger flights during the SARS period had once created a critical space problem. Cargo revenue and tonnage carried increased by 66.9 per cent and 122.4 per cent respectively over the same period of last year. Likewise cargo load factor also increased by 15.4 percentage points to 76.6 per cent, whereas the average cargo yield per cargo tonne kilometre increased by 8.3 per cent as compared to the same period of 2002.

Air Macau took delivery of two A319s, rejuvenated one A321 and returned two A320s and the wet leased B757 during the first six months of 2003. As at the end of June 2003, Air Macau's operating fleet consisted of four A319s, one A320, five A321s and one B727 freighter. All aircraft are under operating leases except for one owned A321 and one wet leased B727 freighter.

### **Hong Kong Dragon Airlines Limited (“Dragonair”)**

During the SARS period, Dragonair has suspended 9 passenger routes and reduced around 40 per cent of passenger capacity in the second quarter of 2003 due to a substantial drop of passenger traffic demand. As at 30th June 2003, Dragonair was operating passenger services to 19 destinations in Asia, of which 11 were in China mainland. Before the SARS outbreak, Dragonair had been operating passenger services to 28 destinations in Asia, of which 18 were in China mainland. Dragonair also offers freighter services to 7 destinations in Europe, the Middle East, Japan, Taiwan region and China mainland.

The outbreak of SARS brought a steep decline in passenger traffic from end of March to early June. Dragonair reported a loss for the first six months of 2003. Passenger revenue fell significantly by 34.5 per cent over the same period in 2002 with passenger number falling to 1.1 million, representing a 32.1 per cent decrease. Passenger load factor dropped significantly by 14.1 percentage points to 50.4 per cent despite a substantial reduction in capacity. The weak passenger traffic demand further deteriorated due to the quarantine requirements introduced by some major cities in China mainland and Taiwan region in May 2003.

Cargo services were less affected with 121,000 tonnes of cargo carried in the first half of 2003, representing a growth of 49.6 per cent as compared with the same period in 2002. With the introduction of the third purchased freighter late last year, cargo revenue increased by 65.5 per cent. Strong market demand also led cargo load factor to increase by 6.6 percentage points to 82.7 per cent. During the period, cargo yield for passenger aircraft increased by 2.7 per cent; whereas cargo yield for freighter increased by 26.7 per cent, attributed mainly to the higher yield from more short-haul freighter services operated, which included the Osaka and the Taipei routes, as well as from the Shanghai/Xiamen co-terminal services.

There was no change in Dragonair's servicing fleet during the period under review. As at the end of June 2003, Dragonair's fleet in service consisted of eight A320s, four A321s, nine A330s and three B747-300 freighter. Dragonair has agreed with the manufacturer Airbus to postpone the delivery of two purchased A321s to September and October 2003 respectively.

Dragonair has been managing the effects on its operations resulting from the outbreak of SARS by adopting stringent measures to control costs and preserve cash reserves. These included the long-term parking of passenger aircraft surplus in accordance with its operation requirement, the implementation of a revised aircraft maintenance program and a revised catering menu, the suspension of all capital expenditures and staff recruitment, the request for all staff to take annual and special no-pay leaves, the reduction of advertising and marketing expenses, and other measures. With WHO removing China mainland cities, Hong Kong and Taiwan region from the SARS-infected areas list in June and July 2003, and with the promising results of a series of sales promotional activities, Dragonair's passenger traffic has been recovering much faster than expected. Dragonair expects its passenger capacity to restore back to 80 per cent and 100 per cent of the planned level in the third and fourth quarter of 2003 respectively. Dragonair remains optimistic of the performance of its air cargo services and would dedicate more resources to this area in the future. As a result

of the rapid recovery since July, the management of Dragonair is optimistic about a significant improvement in the second half of 2003.

### **Jardine Airport Services Limited (“JASL”)**

For the six month period under review, the consolidated turnover of JASL decreased by 31.7 per cent. The decrease was mainly due to the negative impact of the SARS outbreak and the disposal of Jardine Airport Services Australia Pty. Ltd in September 2002. JASL handled 19,204 aircraft movements, representing a decrease of 21.4 per cent over the same period of 2002, and maintained approximately 40 per cent of the third party market at the Hong Kong International Airport (“HK Airport”). Jardine Air Terminal Services Limited (“JATS”) handled 27,684 aircraft movements, representing a decrease of 20.5 per cent and an approximately 60 per cent share of the third party market at the HK Airport. JATS is a 70 per cent owned subsidiary of JASL.

In May 2003, JATS sold its entire shareholding in Jardine Skyporters Limited.

Given the strong support and business connections of its shareholders, JASL will continue to explore new business opportunities in China mainland and is confident of successfully securing these opportunities.

### **Menzies Macau Airport Services Limited (“Menzies Macau”)**

Menzies Macau handled 4,389 aircraft movements in the first quarter of 2003, representing an increase of 13 per cent as compared to the same period in 2002; whereas the turnover and operating profit for the first quarter of 2003 went up by 4 per cent and 2 per cent respectively as compared to the same period of last year. During the Lunar New Year holiday period, Menzies Macau provided ground handling services to 27 “Direct Charter Flights” between China mainland and Taiwan region.

In April 2003, the SARS outbreak began to take a toll on the aviation business; since then, Menzies Macau had experienced a drastic downturn in the operations. Menzies Macau had to face the situation that an average of 60 per cent of scheduled flights were cancelled in the second quarter of 2003. The SARS outbreak costed Menzies Macau deep cuts in revenue and a 69 per cent decrease in operating profit as compared to the same period of 2002.

Since the end of June, flight activities have been slowly getting back to normal. Menzies Macau anticipates returning to its normal level of operations by August 2003.

### **Tradeport Hong Kong Limited (“Tradeport”)**

Tradeport commenced operations in the second quarter of this year during the SARS period, and is beginning to see positive results of the management team’s hard work. Three contracts have been signed with major multinational companies.

## **OUTLOOK**

Despite all the uncertainties, the outlook for the aviation industry in the second half of 2003 should be in a much better shape as compared to the period under review as we see the demand for passenger travel picking up gradually. Given the herald of world economic recovery, the

conclusion of the Closer Economic Partnership Arrangement, and the relaxation of individual travel rules for residents from Shanghai, Beijing and Guangdong province and cities visiting Hong Kong from September 2003 onwards, we expect a promising post SARS rebound and stronger travel demand in the industry in the months ahead. Overall, the Group anticipates a better result for the second half of 2003.

## **LIQUIDITY AND FINANCIAL RESOURCES**

As at 30th June 2003, the Group's shareholders' funds amounts to HK\$2,490 million, compared to HK\$2,704 million as at 31st December 2002.

The Group generally financed its operations with cash flows generated internally. As at 30th June 2003, the Group had cash and bank balances of a total amount of approximately HK\$939 million and net current assets of approximately HK\$804 million, as compared to HK\$1,171 million and HK\$974 million respectively as at 31st December 2002, whereas the current liabilities of the Group dropped from HK\$434 million (as at 31st December 2002) to approximately HK\$299 million as at 30th June 2003. The Group had no outstanding borrowings and consistently maintained a strong working capital base that provides a good foundation for the Group's future business development.

## **SHARE CAPITAL**

During the period under review, the Company repurchased a total of 6,628,000 ordinary shares of the Company of HK\$0.1 each at an aggregate consideration of HK\$5,325,000 on The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). The highest and lowest prices per share paid were HK\$0.83 and HK\$0.77 respectively. All of the shares repurchased were subsequently cancelled.

No options were granted or exercised during the six months ended 30th June 2003 and 147,059,800 options remained outstanding as at 30th June 2003.

As at 30th June 2003, 3,312,680,000 ordinary shares were in issue (31st December 2002: 3,319,308,000 shares).

## **CONTINGENT LIABILITIES**

As at 30th June 2003, the Group had given a guarantee of HK\$75 million to a bank for the banking facilities provided to an associated company, and in February 2001, the Group together with the logistics centre consortium partners jointly gave a guarantee to the Hong Kong Airport Authority in respect of their obligations to provide sufficient funding for the development of the logistics centre. The Directors are of the opinion that, had the Group been required to perform its obligation under the guarantee in the event of default of all of the consortium partners, the maximum amount of the contingent liabilities assumed, including the Group's estimated share of capital commitments of approximately HK\$131 million, would have been approximately HK\$780 million.



## **FOREIGN EXCHANGE AND CURRENCY RISKS**

The Group generates a portion of its revenue from ticket sales in certain foreign jurisdictions giving rise to exposures to fluctuation in foreign exchange rates. The Group continuously monitors its foreign currency positions and does not consider that it has a significant exposure to foreign exchange risk from any currency.

## **HUMAN RESOURCES**

The bulk of human resources of the Company and their remuneration, amongst others, are covered by a management services agreement concluded with the Company's immediate holding company, CNACG. Likewise CNAC Macau also concluded a management services agreement with CNAC (Macau) Aviation Limited. Both agreements were negotiated under normal commercial terms and conditions.

Air Macau, a 51 per cent held subsidiary, employs about 800 staff (six months ended 30th June 2002: about 700), of which about 144 (six months ended 30th June 2002: about 84) are based outside Macau. Employees remuneration packages are designed and structured based on the foregoing market conditions, relevant laws and regulations, industry practices and standards, work performance, education or professional training background and past working experience.

## **CORPORATE GOVERNANCE**

None of the Directors of the Company is aware of any information that would reasonably indicate that the Company is or was not for any part of the six months under review in compliance with the Code of Best Practice (the "Code") as set out in Appendix 14 to the Listing Rules, except that the independent Non-Executive Directors were not appointed for specific terms but appointed to their offices for such terms and subject to retirement by rotation in accordance with Article 98 of the Articles of Association of the Company.

In compliance of the Code, the Company has established an audit committee and has adopted the terms of reference governing the authority and duties of the audit committee. The audit committee has reviewed with management the accounting principles and practices adopted by the Company and discussed internal controls and financial reporting matters including a review of the unaudited condensed interim results for the six months ended 30th June 2003.

## **INTERIM DIVIDEND**

The Directors have declared an interim dividend of HK0.3 cent per share for the six months ended 30th June 2003 (six months ended 30th June 2002: HK0.6 cent per share) payable to the shareholders ("Eligible Shareholders") whose names appear on the Register of Members of the Company on Friday, 3rd October 2003. Dividend warrants will be despatched to the Eligible Shareholders on or about Wednesday, 15th October 2003.

## **CLOSURE OF REGISTER OF MEMBERS**

The Register of Members will be closed from Monday, 29th September 2003 to Friday, 3rd October 2003 both days inclusive, during which period no transfers of shares will be registered. In order to qualify for the interim dividend, all transfer documents together with the relevant share certificates must be lodged with the Company's Share Registrars, Computershare Hong Kong Investor Services Limited, 19th Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong not later than 4:00 p.m. on Friday, 26th September 2003.

## **PUBLICATION OF DETAILED RESULTS ANNOUNCEMENT ON THE STOCK EXCHANGE'S WEBSITE**

A detailed Interim Results Announcement containing all the information in respect of the Company required by paragraphs 46(1) to (6) of Appendix 16 of the Listing Rules will be published on the Stock Exchange's website in due course.

On behalf of the Board  
**KONG DONG**  
*Chairman*

Hong Kong, 5th September 2003

"Please also refer to the published version of this announcement in The Standard".