



中航興業有限公司

CHINA NATIONAL AVIATION COMPANY LIMITED

(於香港註冊成立之有限公司)

*(incorporated in Hong Kong with limited liability)*

2003

中期報告

**INTERIM REPORT**



## CORPORATE INFORMATION

### Directors

Kong Dong (*Chairman*)  
Chuang Shih Ping  
Zhang Xianlin  
Tsang Hing Kwong, Thomas  
Gu Tiefei  
Lok Kung Nam\*  
Hu Hung Lick, Henry\*  
Ho Tsu Kwok, Charles\*  
Li Kwok Heem, John\*

\* *Independent Non-Executive Directors*

### Company Secretary

Li Man Kit

### Registered Office

5th Floor, CNAC House  
12 Tung Fai Road  
Hong Kong International Airport  
Lantau  
Hong Kong

### Principal Bankers

Bank of China (Hong Kong) Limited  
Nanyang Commercial Bank, Ltd.  
Bank of Communications, Hong Kong Branch

### Solicitors

Baker & McKenzie

### Auditors

PricewaterhouseCoopers

### Public Relations

Ketchum Newscan Public Relations Limited

### Share Registrars

Computershare Hong Kong Investor Services Limited  
19th Floor, Hopewell Centre  
183 Queen's Road East  
Wanchai  
Hong Kong

### Financial Calendar

Six months ended 30th June 2003  
Book Close from 29th September 2003  
to 3rd October 2003  
2003 interim dividend payable 15th October 2003



The Board of Directors (the “Directors”) of China National Aviation Company Limited (the “Company”) hereby presents the Interim Report and condensed accounts of the Company and its subsidiaries (collectively the “Group”) for the six months ended 30th June 2003. The consolidated results, consolidated cash flow statement and consolidated statement of changes in equity for the Group for the six months ended 30th June 2003, and the consolidated balance sheet as at 30th June 2003 of the Group, all of which are unaudited and condensed, along with selected explanatory notes, are set out on pages 8 to 22 of this report.

## 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 in the region, 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 leave, 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 has experienced a drastic downturn in the operations. Menzies Macau had to face the situation that an average 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.

### CONTINGENT LIABILITIES AND COMMITMENTS

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, China National Aviation Corporation (Group) Limited ("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: 700 staff), of which about 144 (six months ended 30th June 2002: 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.

## DIRECTORS' INTERESTS IN EQUITY OR DEBT SECURITIES

As at 30th June 2003, none of the Directors nor the chief executive had any interest in shares in the Company according to the register maintained under the Securities and Future Ordinance ("SFO").

The interests of the Directors in the share options of the Company are separately disclosed in the heading "Share Options" below.

Apart from the disclosed under the heading "Share Options" below, at no time during the period was the Company, its fellow subsidiaries, its subsidiaries or its holding company a party to any arrangement to enable any director or chief executive of the Company or his spouse or children under 18 years of age to acquire benefits by means of acquisition of shares in, or debentures of, the Company or any other body corporate.

## SHARE OPTIONS

At an Annual General Meeting of the Company held on 29th May 2002, a new share option scheme (the "Scheme") was approved and adopted to replace the old share option scheme adopted on 22nd October 1997. The major terms of the Scheme are as follows:

1. The purpose of the Scheme is to provide incentives to participants to contribute to the prosperity, business development or growth of the Group and/or to enable the Group to recruit and/or retain high calibre employees and attract resources that are valuable to the Group.
2. The participants of the Scheme are any Director, employee, supplier, customer or other relevant business partners of the Group as invited by the Board.
3. The subscription price determined by the Board will be the higher of (i) the closing price of the Company's share as stated in The Stock Exchange of Hong Kong Limited's (the "Stock Exchange") daily quotations sheet on the date of grant; (ii) the average closing price of the Company's share as stated in the Stock Exchange's daily quotations sheets for the five business days immediately preceding the date of grant; and (iii) the nominal value of the Company's shares.
4. The acceptance of grant of share options must be made within 28 days from the date of grant with a non-refundable payment of HK\$1.00 from the grantee.



5. The maximum number of shares over which options may be granted under the Scheme shall not exceed 30% of the issued share capital of the Company from time to time. As at the date of this report, the maximum number of shares available for issue under the Scheme is 331,268,000, being 10% of the number of issued share capital of the Company.
6. The exercise period of any option granted under the Scheme must not exceed six years commencing on the date falling three months after the date of grant and expiring on the last day of the said period.
7. The Scheme shall be valid and effective till 28th May 2012.

No options were granted or exercised under the Scheme during the six months ended 30th June 2003.

Details of the share options held by Directors as at 30th June 2003 under the old share option scheme are as follows:

	Options held at 1st January 2003	Options granted during the period	Options exercised during the period	Options held at 30th June 2003	Exercise price HK\$	Grant Date	Exercisable from until	
<b>Directors:</b>								
Kong Dong	32,351,800	-	-	32,351,800	0.82	24/09/2001	25/03/2002	24/03/2004
Chuang Shih Ping	38,236,000	-	-	38,236,000	1.04	04/01/2001	12/07/2001	11/07/2003
Zhang Xianlin	38,236,000	-	-	38,236,000	1.04	04/01/2001	12/07/2001	11/07/2003
Tsang Hing Kwong, Thomas	38,236,000	-	-	38,236,000	1.04	04/01/2001	12/07/2001	11/07/2003
<b>Total:</b>	147,059,800	-	-	147,059,800				

Other than stated above, as at 30th June 2003, no Director or chief executive of the Company had any interest or short position in the shares or underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO).

## SUBSTANTIAL SHAREHOLDERS

As at 30th June 2003, the register of substantial shareholders maintained under Part XV of the SFO shows that the following shareholders' with interests representing 5% or more of the Company's issued share capital:

Name	Percentage of issued capital	Number of ordinary shares	Note
China National Aviation Holding Company	69.0	2,286,988,000	1
China National Aviation Corporation	69.0	2,286,988,000	1
China National Aviation Corporation (Group) Limited	69.0	2,286,988,000	1
Best Strikes Limited	5.6	187,656,000	
On Ling Investments Limited	9.7	322,856,000	2
Novel Investments Holdings Limited	9.7	322,856,000	2
Novel Enterprises (BVI) Limited	9.7	322,856,000	2
Novel Credit Limited	9.7	322,856,000	2
Novel Holdings (BVI) Limited	9.7	322,856,000	2
Westleigh Limited	9.7	322,856,000	2





## INTERIM REPORT 2003

*Note 1:* The entire issued share capital of China National Aviation Corporation (Group) Limited is beneficially owned by China National Aviation Corporation. China National Aviation Corporation is in turn wholly-owned by China National Aviation Holding Company, a state-owned enterprise established in the People's Republic of China. Accordingly, the interests of China National Aviation Corporation (Group) Limited, China National Aviation Corporation and China National Aviation Holding Company in the Company duplicate to each other.

*Note 2:* Duplication of Best Strikes Limited's holding.

Save as disclosed above, as at 30th June 2003, the Directors are not aware of any other persons who have interests or short positions in the shares, underlying shares of equity derivatives or debentures of the Company or any associated corporations (within the meaning of Part XV of SFO) which would be required to be disclosed to the Company pursuant to Part XV of the SFO.

### REPURCHASE, SALE OR REDEMPTION OF SHARES

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. 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.

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

### 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.

### 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.



**CONDENSED CONSOLIDATED PROFIT AND LOSS ACCOUNT**  
**FOR THE SIX MONTHS ENDED 30TH JUNE 2003**

	Note	Unaudited Six months ended 30th June	
		2003 HK\$'000	2002 HK\$'000
Turnover		513,526	486,186
Other revenues		8,209	7,446
Total revenues		<u>521,735</u>	<u>493,632</u>
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		<u>712,295</u>	<u>440,590</u>
Operating (loss)/profit	3	(190,560)	53,042
Finance costs		–	(8,426)
Share of losses less profits of associated companies		(98,606)	153,535
(Loss)/profit before taxation		(289,166)	198,151
Taxation	4	39,083	(36,733)
(Loss)/profit after taxation		(250,083)	161,418
Minority interests		68,796	(24,189)
(Loss)/profit attributable to shareholders		<u>(181,287)</u>	<u>137,229</u>
Proposed interim dividends	5	9,938	19,916
Basic (loss)/earnings per share	6	<u>(HK5.47 cents)</u>	<u>HK4.21 cents</u>
Diluted earnings per share	6	<u>N/A</u>	<u>HK4.14 cents</u>

**CONDENSED CONSOLIDATED BALANCE SHEET**

AS AT 30TH JUNE 2003

	Note	Unaudited 30th June 2003 HK\$'000	31st December 2002 HK\$'000
Non-current assets			
Fixed assets	7	425,816	441,134
Intangible assets	8	315,678	325,173
Investments in associated companies	9	1,139,458	1,247,746
Lease and equipment deposits		82,983	88,255
Deferred tax assets		27,702	–
		<u>1,991,637</u>	<u>2,102,308</u>
Total non-current assets			
Current assets			
Inventories, at cost		53,319	51,164
Trade and other receivables	10	110,627	185,791
Bank balances and cash			
– Pledged		17,859	13,155
– Unpledged		921,040	1,158,014
		<u>1,102,845</u>	<u>1,408,124</u>
Current liabilities			
Trade and other payables	11	207,619	317,393
Sales in advance of carriage		81,377	106,243
Taxation payable		10,143	10,395
		<u>299,139</u>	<u>434,031</u>
Net current assets			
		<u>803,706</u>	<u>974,093</u>
Total assets less current liabilities			
		<u>2,795,343</u>	<u>3,076,401</u>
Financed by:			
Share capital	12	331,268	331,931
Reserves		2,148,461	2,346,014
Proposed dividend		9,938	26,554
		<u>2,489,667</u>	<u>2,704,499</u>
Shareholders' funds		2,489,667	2,704,499
Minority interests		249,411	318,207
Non-current liabilities			
Provision for overhaul and major checks		56,265	53,695
		<u>2,795,343</u>	<u>3,076,401</u>

On behalf of the Board

**Zhang Xianlin**  
Director

**Tsang Hing Kwong, Thomas**  
Director

**CONDENSED CONSOLIDATED CASH FLOW STATEMENT**  
*FOR THE SIX MONTHS ENDED 30TH JUNE 2003*

	Unaudited	
	Six months ended 30th June	
	2003 <i>HK\$'000</i>	2002 <i>HK\$'000</i>
Net cash (outflow)/inflow from operating activities	<b>(204,929)</b>	86,984
Net cash from investing activities	<b>147</b>	381,632
Net cash used in financing activities	<b>(32,192)</b>	(154,021)
Net (decrease)/increase in cash and cash equivalents	<b>(236,974)</b>	314,595
Cash and cash equivalents at 1st January	<b>1,158,014</b>	677,922
Cash and cash equivalents at 30th June	<b>921,040</b>	992,517
Analysis of balances of cash and cash equivalents:		
Bank balances and cash	<b>921,040</b>	992,517



**CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**  
**FOR THE SIX MONTHS ENDED 30TH JUNE 2003**

	Unaudited						
	Six months ended 30th June 2003						
	Share capital	Share premium	Capital redemption reserve	Legal reserve	Investments revaluation reserve	Retained earnings	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 1st January 2003	331,931	1,434,558	-	3,666	4,180	930,164	2,704,499
Share of exchange differences of an associated company	-	-	-	-	-	(4)	(4)
Share of deficit on revaluation of investments in securities of an associated company	-	-	-	-	(1,715)	-	(1,715)
Net gains or losses not recognised in the consolidated profit and loss account	-	-	-	-	(1,715)	(4)	(1,719)
Repurchase of own shares	(663)	(4,662)	663	-	-	(663)	(5,325)
Loss for the period	-	-	-	-	-	(181,287)	(181,287)
Dividends	-	-	-	-	-	(26,501)	(26,501)
At 30th June 2003	<b>331,268</b>	<b>1,429,896</b>	<b>663</b>	<b>3,666</b>	<b>2,465</b>	<b>721,709</b>	<b>2,489,667</b>

	Unaudited						
	Six months ended 30th June 2002						
	Share capital	Share premium	Capital redemption reserve	Legal reserve	Investments revaluation reserve	Retained earnings	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 1st January 2002	323,518	1,355,480	-	-	6,324	653,872	2,339,194
Share of exchange differences of an associated company	-	-	-	-	-	1,336	1,336
Share of deficit on revaluation of investments in securities of an associated company	-	-	-	-	(2,954)	-	(2,954)
Net gains or losses not recognised in the consolidated profit and loss account	-	-	-	-	(2,954)	1,336	(1,618)
Issue of shares	8,413	79,078	-	-	-	-	87,491
Profit for the period	-	-	-	-	-	137,229	137,229
Dividends	-	-	-	-	-	(19,916)	(19,916)
At 30th June 2002	<b>331,931</b>	<b>1,434,558</b>	<b>-</b>	<b>-</b>	<b>3,370</b>	<b>772,521</b>	<b>2,542,380</b>



## NOTES TO THE CONDENSED ACCOUNTS

### 1. Basis of preparation and accounting policies

These unaudited consolidated condensed accounts are prepared in accordance with Hong Kong Statement of Standard Accounting Practice ("SSAP") 25 "Interim Financial Reporting" issued by the Hong Kong Society of Accountants ("HKSA").

These condensed accounts should be read in conjunction with the 2002 annual financial statements.

The accounting policies and methods of computation used in the preparation of these condensed accounts are consistent with those used in the annual accounts for the year ended 31st December 2002 except that the Group has changed its accounting policy following its adoption of the revised SSAP 12 "Income taxes" issued by the HKSA which is effective for accounting periods commencing on or after 1st January 2003.

The change to the Group's accounting policy and the effect of adoption of the revised SSAP 12 is set out below.

In accordance with the revised SSAP 12, deferred taxation is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the accounts. The principal temporary differences arise from depreciation on fixed assets and tax losses carried forward; and, in relation to acquisitions, on the difference between the fair values of the net assets acquired and their tax bases. Tax rates enacted or substantively enacted by the balance sheet date are used to determine deferred taxation.

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred taxation is provided on temporary differences arising on investments in subsidiaries and associated companies, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

In prior years, deferred taxation was accounted for at the current tax rate in respect of timing differences between profit as computed for taxation purposes and profit as stated in the accounts to the extent that a liability or an asset was expected to be payable or recoverable in the foreseeable future. The adoption of the revised SSAP 12 represents a change in accounting policy, but it does not have significant effect on the accounts for the prior period.



## 2. 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:

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



	Unaudited				Group HK\$'000
	Six months ended 30th June 2002				
	Property holding (note) HK\$'000	Airline operation HK\$'000	Airport ground handling HK\$'000	Logistics and other businesses HK\$'000	
Segment revenues	5,644	481,315	-	-	486,959
Segment results	4,719	56,193	-	-	60,912
Interest income					6,673
Unallocated costs					(14,543)
Operating profit					53,042
Finance costs					(8,426)
Share of profits less losses of associated companies	-	109,908	45,311	(1,684)	153,535
Profit before taxation					198,151
Taxation					(36,733)
Profit after taxation					161,418
Minority interests					(24,189)
Profit attributable to shareholders					137,229

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

### 3. 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	9,419	4,709
- Trademarks	-	11
- Deferred expenditure	76	114
Cost of inventories expensed	20,867	7,987
Depreciation of fixed assets	36,277	16,534
Outgoings in respect of investment properties	-	925





#### 4. 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</b>	
	<b>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
	<b>(27,316)</b>	9,548
Share of taxation attributable to associated companies	<b>(11,767)</b>	27,185
	<b>(39,083)</b>	36,733

#### 5. Proposed interim dividends

	<b>Unaudited</b>	
	<b>Six months ended</b>	
	<b>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

*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.



## 6. (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.

## 7. Fixed assets

	Unaudited				
	Leasehold improve- ments HK\$'000	Aircraft and engines HK\$'000	Flight equipment and rotable spares HK\$'000	Machinery, other equipment, furniture, and motor vehicles HK\$'000	Total HK\$'000
Cost or valuation					
As at 1st January 2003	28,384	418,040	230,065	49,954	726,443
Additions	2,601	–	15,076	3,370	21,047
Disposals	(2,030)	–	(201)	(1,921)	(4,152)
	<u>28,955</u>	<u>418,040</u>	<u>244,940</u>	<u>51,403</u>	<u>743,338</u>
As at 30th June 2003	28,955	418,040	244,940	51,403	743,338
Accumulated depreciation					
As at 1st January 2003	22,924	105,277	125,380	31,728	285,309
Charge for the period	629	15,924	16,907	2,817	36,277
Disposals	(2,006)	–	(186)	(1,872)	(4,064)
	<u>21,547</u>	<u>121,201</u>	<u>142,101</u>	<u>32,673</u>	<u>317,522</u>
As at 30th June 2003	21,547	121,201	142,101	32,673	317,522
Net book value					
As at 30th June 2003	<u>7,408</u>	<u>296,839</u>	<u>102,839</u>	<u>18,730</u>	<u>425,816</u>
As at 31st December 2002	<u>5,460</u>	<u>312,763</u>	<u>104,685</u>	<u>18,226</u>	<u>441,134</u>



## 8. Intangible assets

	<b>Goodwill</b> <i>HK\$'000</i>	<b>Trademarks</b> <i>HK\$'000</i>	<b>Unaudited Deferred expenditures</b> <i>HK\$'000</i>	<b>Total</b> <i>HK\$'000</i>
Cost				
As at 1st January 2003 and 30th June 2003	339,111	928	2,733	342,772
Accumulated amortisation				
As at 1st January 2003	14,130	928	2,541	17,599
Charge for the period	9,419	–	76	9,495
As at 30th June 2003	23,549	928	2,617	27,094
Net book amount				
As at 30th June 2003	315,562	–	116	315,678
As at 31st December 2002	324,981	–	192	325,173

## 9. Investments in associated companies

	<b>Unaudited 30th June 2003 HK\$'000</b>	<b>31st December 2002 HK\$'000</b>
Hong Kong Dragon Airlines Limited	984,072	1,096,205
Jardine Airport Services Limited	56,969	50,826
Menzies Macau Airport Services Limited	64,699	66,646
Tradeport Hong Kong Limited	33,487	33,760
Macau Aircraft Repair and Conversion Company Limited ("MARCCO")	231	309
	<b>1,139,458</b>	<b>1,247,746</b>

The investments in associated companies above also include loans to JASL, Tradeport and MARCCO of HK\$37,560,000 (31st December 2002: HK\$37,560,000), HK\$43,096,000 (31st December 2002: HK\$38,846,000) and HK\$446,000 (31st December 2002: HK\$446,000) respectively.

**10. Trade and other receivables**

Included in trade and other receivables are trade receivables with third parties and related companies of HK\$47,324,000 (31st December 2002: HK\$121,478,000).

The amounts due from related companies have normal commercial terms of settlement. The credit terms granted to sales agents and other trade customers are generally half month.

At 30th June 2003, the age analysis of the trade receivable balances with third parties and related companies is as follows:

	<b>Unaudited 30th June 2003 HK\$'000</b>	31st December 2002 HK\$'000
Within 31 days	<b>44,314</b>	112,690
31 – 60 days	<b>158</b>	8,499
61 – 90 days	<b>207</b>	289
Over 90 days	<b>2,645</b>	–
	<b><u>47,324</u></b>	<b><u>121,478</u></b>

**11. Trade and other payables**

Included in trade and other payables are trade payable balances with third parties, associated companies, fellow subsidiaries and related companies of HK\$88,737,000 (31st December 2002: HK\$169,952,000).

At 30th June 2003, the age analysis of the trade payable balances with third parties, associated companies, fellow subsidiaries and related companies is as follows:

	<b>Unaudited 30th June 2003 HK\$'000</b>	31st December 2002 HK\$'000
Within 31 days	<b>26,628</b>	96,116
31 – 60 days	<b>11,833</b>	30,121
61 – 90 days	<b>15,886</b>	25,404
Over 90 days	<b>34,390</b>	18,311
	<b><u>88,737</u></b>	<b><u>169,952</u></b>



## 12. Share capital

	<b>Unaudited Ordinary shares of HK\$0.10 each</b>	
	<b>Number of shares</b>	<b>HK\$'000</b>
Authorised:		
At 1st January 2002, 2003 and 30th June 2003	<u>4,000,000,000</u>	<u>400,000</u>
Issued and fully paid:		
At 1st January 2002	3,235,182,000	323,518
Exercise of share options	<u>84,126,000</u>	<u>8,413</u>
At 1st January 2003	3,319,308,000	331,931
Repurchase of shares	<u>(6,628,000)</u>	<u>(663)</u>
At 30th June 2003	<u>3,312,680,000</u>	<u>331,268</u>

At an Annual General Meeting of the Company held on 29th May 2002, a new share option scheme was approved and adopted to replace the old share option scheme which was approved by the shareholders of the Company on 22nd October 1997.

During the six months ended 30th June 2002, 84,126,000 options were exercised and 84,126,000 ordinary shares were issued at a subscription price of HK\$1.04. No options were granted or exercised during the six months ended 30th June 2003 and 147,059,800 options remained outstanding at 30th June 2003. 114,708,000 options lapsed on 11th July 2003 and the remaining 32,351,800 options will be expired on 24th March 2004. On 25th July 2003, 104,378,000 options were granted to Directors to subscribe for shares of the Company at exercise price of HK\$1.14 per share, with the expiry date on 25th October 2009.

In April 2003, the Company repurchased a total of 6,628,000 ordinary shares in the Company of HK\$0.1 each at an aggregate consideration of HK\$5,325,000. The highest and lowest prices per share paid were HK\$0.83 and HK\$0.77 respectively. The above shares repurchased were then cancelled and accordingly the issued capital of the Company was reduced by the nominal value of those shares. The premium paid on repurchase of shares was charged against the share premium account. An amount equivalent to the nominal value of shares cancelled was transferred from retained earnings to capital redemption reserve account.

**13. Commitments**

- (i) On 15th May 2000, the Group entered into a memorandum of understanding with a third party for the establishment of a joint venture company (the "JV"), of which the Group will own 55% equity interest, to provide aviation related internet based services. The initial investment of the Group in the JV amounts to approximately HK\$42,900,000 (31st December 2002: HK\$42,900,000). As at 30th June 2003, no payment has been made by the Group to the JV (31st December 2002: Nil).
- (ii) On 16th February 2001, the Group entered into an agreement with third parties (the "Consortium Partners") for the joint development and operation of the logistics centre at the South Commercial District of the HK Airport (the "Project"). The Group has 25% interest in the Project. The Directors estimate that the Group's attributable share of capital commitments in respect of the Project is approximately HK\$130,650,000 (31st December 2002: HK\$130,650,000), of which HK\$43,096,000 was advanced to project as at 30th June 2003 (31st December 2002: HK\$38,846,000).

In the event of default of any of the Consortium Partners, the Group will be required to provide additional funds for the Project. The Group and the Consortium Partners have jointly given a guarantee to the Hong Kong Airport Authority in respect of their obligations to provide sufficient funding for the Project. Should the Group be required to perform its obligations under the guarantee in the event of default of all of the Consortium Partners, the maximum amount of the additional liabilities assumed, in addition to the Group's estimated share of capital commitments as disclosed above, would be approximately HK\$649,350,000 (31st December 2002: HK\$649,350,000).

**14. Contingent liabilities**

	<b>Unaudited 30th June 2003 HK\$'000</b>	31st December 2002 HK\$'000
Guarantee for banking facilities granted by bank to an associated company	<b><u>75,000</u></b>	<u>75,000</u>



## 15. Related party transactions

In addition to those disclosed elsewhere in the condensed accounts, significant related party transactions, which were carried out in the normal course of the Group's business, are as follows:

	Unaudited	
	Six months ended 30th June	
	2003	2002
	HK\$'000	HK\$'000
Management fee paid to:		
– Immediate holding company ( <i>note i</i> )	3,000	3,000
– A fellow subsidiary ( <i>note ii</i> )	1,800	968
Landing, loading, parking and other airport charges paid to a fellow subsidiary ( <i>note iii</i> )	23,052	29,046
Ground handling costs paid to an associated company ( <i>note iv</i> )	39,305	31,007
Technical and ground handling costs paid to an associated company ( <i>note v</i> )	1,071	687
Inflight meal supplies expenses paid to a related company ( <i>note vi</i> )	15,944	14,124
Over-riding commission paid to a related company ( <i>note vii</i> )	–	10,123
Value of tickets sold to ( <i>note viii</i> ):		
– Fellow subsidiaries	2,484	2,997
– Related companies	6,533	24,424
	<b>6,533</b>	<b>24,424</b>

### Notes:

- (i) On 3rd August 2001, the Company and CNACG entered into a management services agreement pursuant to which CNACG has agreed to provide secretarial, personnel, accounting and general office administrative services to the Group at a monthly fee of HK\$500,000.
- (ii) The Group entered into a management services agreement with CNAC (Macau) Aviation Limited pursuant to which CNAC (Macau) Aviation Limited will provide general management services including but not limited to secretarial, personnel, accounting and general office administrative services to CNAC Macau at a monthly fee of HK\$300,000.
- (iii) The airport related charges paid to ADA-Administrative Airport Limited ("ADA") were mainly charged at terms pursuant to the tariff published by the Macau International Airport. Other airport charges were charged at terms pursuant to agreements entered into by the Group with ADA or the Macau International Airport.
- (iv) The ground handling services rendered were charged at terms pursuant to agreements entered into by the Group with Menzies Macau.
- (v) The technical and ground handling services rendered were charged at terms pursuant to agreements entered into by the Group with Dragonair.
- (vi) The inflight meal supplies were charged at terms pursuant to agreements entered into by the Group with Macau Catering Services Company Limited, a 34.5% owned associated company held by a minority shareholder of Air Macau.



(vii) Over-riding commission was charged at a fixed rate of 3% on the passenger flown revenue generated in the Taiwan region.

(viii) Air tickets were sold to the related ticket sales agents in accordance with the pricing policy of the Group.

In addition to the above, on 18th October 1997, the Company entered into a licence agreement with China National Aviation Corporation ("CNAC") pursuant to which CNAC agreed to grant a licence to the Company, free of royalty, for the use of certain trademarks in Hong Kong, Macau and the Taiwan region so long as the Company is a subsidiary of CNACG. No royalty charge was levied in respect of the use of these trademarks during the period (six months ended 30th June 2002: Nil).

## 16. Comparative figures

Comparative figures of other revenues, passenger catering and service costs, route operating costs, aircraft maintenance costs, depreciation and amortisation costs, other operating costs and finance costs have been reclassified or extended to conform with the current period's presentation.

## 17. Approval of the condensed accounts

The condensed accounts were approved by the Directors on 5th September 2003.

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

Hong Kong, 5th September 2003





中航興業有限公司

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