



### 1. PRINCIPAL ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these accounts are set out below:

#### (a) Basis of preparation

The accounts have been prepared in accordance with accounting principles generally accepted in Hong Kong and comply with accounting standards issued by the Hong Kong Society of Accountants ("HKSA"). They have been prepared under the historical cost convention.

In the current year, the Group adopted new Statement of Standard Accounting Practice ("SSAP") 12 "Income taxes" issued by the Hong Kong Society of Accountants which is effective for accounting periods commencing on or after 1st January, 2003. The change to the Group's accounting policy on deferred taxation is set out in note 1(h) below.

#### (b) Consolidation

The consolidated accounts include the accounts of the Company and its subsidiaries made up to 31st December. Subsidiaries are those entities in which the Group controls the composition of the board of directors, controls more than half the voting power or holds more than half of the equity share capital.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated profit and loss account from the effective date of acquisition or up to the effective date of disposal, as appropriate.

All significant intercompany transactions and balances within the Group are eliminated on consolidation.

The gain or loss on the disposal of a subsidiary represents the difference between the proceeds of the sale and the Group's share of its net assets together with any unamortised goodwill which was not previously charged or recognised in the consolidated profit and loss account.

Minority interests represent the interests of outside shareholders in the operating results and net assets of subsidiaries.

In the Company's balance sheet the investments in subsidiaries are stated at cost less provision for impairment losses. The results of subsidiaries are accounted for by the Company on the basis of dividend income.



## 1. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

### (c) Associated companies

An associated company is a company, not being a subsidiary, in which an equity interest is held for the long-term and significant influence is exercised in its management.

The consolidated profit and loss account includes the Group's share of the results of associated companies for the year, and the consolidated balance sheet includes the Group's share of the net assets of the associated companies.

In the Company's balance sheet the investments in associated companies are stated at cost less provision for impairment loss. The results of associated companies are accounted for by the Company on the basis of dividend income.

### (d) Jointly controlled operations

A joint venture is a contractual arrangement whereby the Group and other parties undertake an economic activity which is subject to joint control and none of the participating parties has unilateral control over the economic activity.

The assets that the Group controls and liabilities that it incurs in relation to jointly controlled operations joint ventures are recognised in the balance sheet on an accrual basis and classified according to the nature of the item. The expenses that the Group incurs and its share of income that it earns from services rendered by these joint controlled operations are included in the profit and loss account.

### (e) Intangible assets

#### (i) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net assets of the acquired subsidiaries at the date of acquisition.

Goodwill on acquisitions occurring on or after 1st January, 2001 is included in intangible assets and is amortised using the straight-line method over its estimated useful lives of not more than 20 years.

#### (ii) Trademark

Expenditure on trademark is carried at cost less accumulated amortisation and impairment losses. Amortisation is calculated on a straight-line basis at an annual rate of 16.66%.



## 1. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

### (e) Intangible assets (cont'd)

#### (iii) *Deferred expenditure*

Transaction fees and transportation charges in relation to placing the leased aircraft into operation are deferred and amortised over the terms of the related leases.

#### (iv) *Impairment of intangible assets*

The carrying amount of any intangible assets, including goodwill previously taken directly to reserves, is reviewed annually and provision is only made to write down to its recoverable amount where, in the opinion of the Directors, there is a long-term impairment in value.

### (f) Fixed assets

Fixed assets, comprising leasehold improvements, aircraft and engines, flight equipment and rotatable spares and machinery, other equipment, furniture and motor vehicles, are stated at cost less accumulated depreciation and impairment losses.

Fixed assets are depreciated at rates sufficient to write off their cost less accumulated impairment losses over their estimated useful lives on a straight-line basis, after taking into account their estimated residual values. The estimated useful lives are as follows:

Leasehold improvements	6 years
Aircraft and engines	10 to 20 years
Flight equipment and rotatable spares	7 to 20 years
Machinery, other equipment, furniture and motor vehicles	3 to 10 years

Expenditure incurred to replace a component of an item of fixed assets that is accounted for separately, including major inspection and overhaul expenditure, is capitalised (note 1(q)). Other subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the item of fixed assets. All other expenditure is expensed as incurred.

At each balance sheet date, both internal and external sources of information are considered to assess whether there is any indication that the fixed assets are impaired. If any such indication exists, the recoverable amount of the asset is estimated and where relevant, an impairment loss is recognised to reduce the assets to its recoverable amount. Such impairment losses are recognised in the profit and loss account.

The gain or loss on disposal of a fixed asset is the difference between the net sales proceeds and the carrying amount of the relevant asset, and is recognised in the profit and loss account.



## 1. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

### (g) Inventories

Inventories comprise expendable spare parts and supplies, are stated at the lower of cost and net realisable value, and are expensed when used in operations. Cost is calculated on the average cost basis except for aircraft spare parts, cost of which is calculated on the first-in-first-out basis. Net realisable value is determined on the basis of anticipated sales proceeds less estimated selling expenses.

### (h) Deferred taxation

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 base. 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 previous 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 new SSAP 12 represents a change in accounting policy, but such change does not have significant effect on the accounts for the previous years.

### (i) Translation of foreign currencies

Transactions in foreign currencies are translated at exchange rates ruling at the transaction dates. Monetary assets and liabilities expressed in foreign currencies at the balance sheet date are translated at rates of exchange ruling at the balance sheet date. Exchange differences arising in these cases are dealt with in the profit and loss account.

The balance sheets of subsidiaries and associated companies expressed in foreign currencies are translated at the rates of exchange ruling at the balance sheet date whilst the profit and loss accounts of subsidiaries and associated companies are translated at the weighted average rate during the year. Exchange differences are dealt with as a movement in reserves.



### 1. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

#### (j) Accounts receivable

Provision is made against accounts receivable to the extent they are considered to be doubtful. Accounts receivable in the balance sheet are stated net of such provision.

#### (k) Manufacturers' credits

Manufacturers' credits received in connection with leasing of aircraft, which the Group can apply those credits to reduce future costs of acquiring aircraft spares or rental payments, are either deferred and amortised as income or as a reduction of rental expenses for aircraft over relevant leases.

#### (l) Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, deposits held at call with banks, cash investments with a maturity of three months or less from date of investment and bank overdrafts.

#### (m) Provisions

Provisions are recognised when there is a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Where it is expected a provision to be reimbursed, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

#### (n) Employee benefits

##### (i) *Employee leave entitlements*

Employee entitlements to annual leave are recognised when they accrue to employees of the Group. A provision is made for the estimated liability for annual leave as a result of services rendered by employees up to the balance sheet date.

Employee entitlements to sick leave and maternity or paternity leave are not recognised until the time of leave.

##### (ii) *Retirement benefit costs*

Contributions to the defined contribution schemes are charged to the profit and loss account in the year in which the contributions relate.

##### (iii) *Equity compensation benefits*

Share options are granted to Directors and continuous contract employees. No compensation cost is recognised in the profit and loss account in connection with share options granted. When the share options are exercised, the proceeds received net of any transaction costs are credited to share capital (nominal value) and share premium.



## 1. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

### (o) Contingent liabilities and contingent assets

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognised because it is not probable that outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

A contingent liability is not recognised but is disclosed in the notes to the accounts. When a change in the probability of an outflow occurs so that outflow is probable, they will then be recognised as a provision.

A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain events not wholly within the control of the Group.

Contingent assets are not recognised but are disclosed in the notes to the accounts when an inflow of economic benefits is probable. When inflow is virtually certain, an asset is recognised.

### (p) Revenue recognition

#### (i) *Traffic revenue*

Passenger, cargo and mail revenues are recognised when the transportation is provided. Ticket sales for transportation not yet provided are included in current liabilities as sales in advance of carriage.

#### (ii) *Inflight sales commission*

Inflight sales commission is recognised when services are rendered.

#### (iii) *Rental income*

Rental income is recognised on a straight-line basis over the terms of the leases.

#### (iv) *Interest income*

Interest income is recognised on a time proportion basis, taking into account the principal amounts outstanding and the interest rates applicable.

#### (v) *Dividend income*

Dividend income is recognised when the right to receive payment is established.



### 1. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

#### (q) Maintenance and overhaul costs

Costs of major checks and overhauls performed on owned aircraft to replace a component of an item of fixed assets are capitalised and amortised over a period of 3 years. Other maintenance and major overhaul costs incurred for owned aircraft are expensed as and when incurred.

In respect of aircraft under operating leases, a provision is made for the estimated costs of major checks and overhauls required to be conducted to fulfill the requirements under the relevant leases based on the maintenance cycle of each aircraft.

#### (r) Operating leases

Leases where substantially all the risks and rewards of ownership of assets remain with the lessor are accounted for as operating leases. Payments made under operating leases net of any incentives received from the lessor are charged to the profit and loss account on a straight-line basis over the lease periods.

#### (s) Segment reporting

In accordance with the Group's internal financial reporting, the Group has determined that the primary segment reporting is by business segments and the secondary segment reporting is by geographical segments.

Unallocated costs represent corporate expenses and amortisation of unallocated goodwill. Segment assets consist primarily of intangible assets, fixed assets, lease and equipment deposits, inventories, trade and other receivables and operating cash and mainly exclude unallocated goodwill, associated companies, tax recoverable and non-operating bank balances and cash. Segment liabilities comprise operating liabilities and mainly exclude taxation payable. Capital expenditure comprises additions to intangible assets and fixed assets, including additions resulting from acquisitions through purchases of subsidiaries.

In respect of geographical segment reporting, turnover and operating profit by geographical segments is based on the following criteria:

- (i) Traffic revenue from inbound and outbound services between Macau and overseas markets is attributed to the geographical area in which the relevant overseas origin/destination lies.
- (ii) Revenues from gross rental income from investment properties is attributed on the basis of where the properties are located and other aviation related services are attributed on the basis of where the services are performed.

Total assets and capital expenditure are where the assets are located.



## 2. TURNOVER, REVENUES AND SEGMENT INFORMATION

The Group is principally engaged in provision of aviation related services. Revenues recognised during the year are as follows:

	<b>2003</b>	2002
	<b>HK\$'000</b>	HK\$'000
Turnover		
Traffic revenues		
– Passenger services	<b>984,211</b>	1,171,504
– Cargo and mail services	<b>242,820</b>	152,278
Gross rental income from investment properties	–	5,644
	<b>1,227,031</b>	1,329,426
Other revenues		
Inflight sales commission	<b>1,861</b>	1,887
Interest income	<b>9,172</b>	13,546
Rental income from sub-lease of aircraft	<b>14,460</b>	–
	<b>25,493</b>	15,433
Total revenues	<b>1,252,524</b>	1,344,859

The Group is organised into four main business segments including airline operation, airport ground handling, logistics and other businesses and property holding.

On 25th March, 2002, the property holding business of the Group was vested to the China National Aviation Corporation (Group) Limited (“CNACG”).

There are no sales or other transactions between the business segments.





## 2. TURNOVER, REVENUES AND SEGMENT INFORMATION (CONT'D)

### Business segments

	Airline operation HK\$'000	Airport ground handling HK\$'000	Logistics and other businesses HK\$'000	Property holding HK\$'000	Group HK\$'000
<b>Year ended 31st December, 2003</b>					
Segment revenues	<u>1,243,352</u>	<u>–</u>	<u>–</u>	<u>–</u>	<u>1,243,352</u>
Segment results	<u>(193,390)</u>	<u>–</u>	<u>–</u>	<u>–</u>	<u>(193,390)</u>
Interest income					9,172
Unallocated costs					<u>(39,365)</u>
Operating loss					<u>(223,583)</u>
Share of profits less losses of associated companies	29,796	101,280	(9,594)	–	<u>121,482</u>
Loss before taxation					<u>(102,101)</u>
Taxation credit					<u>13,944</u>
Loss after taxation					<u>(88,157)</u>
Minority interests					<u>69,410</u>
Loss attributable to shareholders					<u><u>(18,747)</u></u>
Segment assets	931,323	–	–	–	931,323
Associated companies	1,125,143	132,271	29,628	–	1,287,042
Unallocated assets					1,155,070
Total assets					<u><u>3,373,435</u></u>
Segment liabilities	477,442	–	–	–	477,442
Unallocated liabilities					<u>4,865</u>
Total liabilities					<u><u>482,307</u></u>
Capital expenditure	27,467	–	–	–	27,467
Depreciation	68,519	–	–	–	68,519
Amortisation	138	–	–	–	138
Other non-cash expenses	–	–	–	–	–

Capital expenditure and amortisation charge by business segments did not include goodwill arising from acquisitions of China National Aviation Corporation (Macau) Company Limited ("CNAC Macau") of HK\$339,111,000 for the year ended 31st December, 2002 and related amortisation of HK\$14,130,000 and HK\$18,840,000 for the years ended 31st December, 2002 and 2003 respectively as the Directors consider that there is no meaningful basis for allocation of such goodwill between airline operation and airport ground handling businesses.



## 2. TURNOVER, REVENUES AND SEGMENT INFORMATION (CONT'D)

### Business segments (cont'd)

	Airline operation HK\$'000	Airport ground handling HK\$'000	Logistics and other businesses HK\$'000	Property holding HK\$'000	Group HK\$'000
<b>Year ended 31st December, 2002</b>					
Segment revenues	1,325,669	–	–	5,644	1,331,313
Segment results	77,783	–	–	4,719	82,502
Interest income					13,546
Unallocated costs					(34,212)
Operating profit					61,836
Finance costs					(8,426)
Share of profits less losses of associated companies	291,535	107,490	(4,145)	–	394,880
Profit before taxation					448,290
Taxation charge					(89,343)
Profit after taxation					358,947
Minority interests					(41,530)
Profit attributable to shareholders					317,417
Segment assets	1,102,291	–	–	–	1,102,291
Associated companies	1,096,208	117,472	34,066	–	1,247,746
Unallocated assets					1,160,395
Total assets					3,510,432
Segment liabilities	466,877	–	–	–	466,877
Unallocated liabilities					20,849
Total liabilities					487,726
Capital expenditure	491,905	–	–	–	491,905
Depreciation	49,843	–	–	–	49,843
Amortisation	288	–	–	–	288
Other non-cash expenses	620	–	–	–	620



## 2. TURNOVER, REVENUES AND SEGMENT INFORMATION (CONT'D)

**Geographical segments**

The Group operates in four main geographical areas including China mainland, Taiwan, Hong Kong and other regions (mainly Macau, Thailand and Philippines). Except for Hong Kong where the Group's property holding business operated, all other geographical areas are attributed to the Group's airline operation business. There are no sales between the geographical segments.

	Segment revenues		Segment results	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
China mainland	489,377	539,489	(106,745)	(28,145)
Taiwan	651,251	702,899	(9,838)	133,449
Hong Kong	–	5,644	–	4,719
Other regions	102,724	83,281	(76,807)	(27,521)
Total	<u>1,243,352</u>	<u>1,331,313</u>	<u>(193,390)</u>	82,502
Interest income			9,172	13,546
Unallocated costs			(39,365)	(34,212)
Operating (loss)/profit			<u>(223,583)</u>	<u>61,836</u>

The major revenue-earning assets of the Group are its aircraft fleet, all of which are registered in Macau. Since the Group's aircraft fleet is deployed flexibly across its route network, the Directors consider that there is no meaningful basis to allocating such assets to geographical segments.

The Group's assets, other than its aircraft fleet as mentioned in the above, and capital expenditure are mainly located in Macau.



### 3. STAFF COSTS

	<b>2003</b>	2002
	<b>HK\$'000</b>	HK\$'000
Wages and salaries (including directors' emoluments) (note a)	<b>211,345</b>	184,697
Retirement benefit costs (note b)	<b>4,065</b>	3,717
	<b>215,410</b>	188,414

- (a) The above staff costs did not include the benefits in kind arising from the exercise of share options by employees of the Group (note 10(b)).
- (b) The Company contributes to the mandatory provident fund scheme ("MPF Scheme") established under the Hong Kong Mandatory Provident Fund Scheme Ordinance which is available to eligible employees in Hong Kong.

The subsidiary in Macau operates defined contribution pension plans which are available to eligible employees. The assets of the plans are held separately from the subsidiary in independently administrated funds. Monthly contributions made by the subsidiary are calculated based on certain percentages of the applicable payroll costs or fixed sums as stipulated under the relevant requirements, as appropriate.

The retirement benefit costs represent gross contributions paid and payable to the MPF Scheme in Hong Kong and the defined contribution pension plans in Macau (collectively the "Retirement Schemes"). Contributions totalling HK\$3,394,000 (2002: HK\$2,878,000) payable to the Retirement Schemes as at 31st December, 2003 are included in trade and other payables. Forfeited contributions totalling HK\$927,000 (2002: HK\$334,000) were utilised during the year leaving HK\$51,000 (2002: HK\$10,000) available at the year end to reduce future contributions.



## 4. OPERATING (LOSS)/PROFIT

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

	<b>2003</b>	2002
	<b>HK\$'000</b>	HK\$'000
<b>Crediting</b>		
Amortisation of manufacturers' credits	<b>7,600</b>	7,523
Net exchange gains	<b>349</b>	–
<b>Charging</b>		
Amortisation of intangible assets		
– Goodwill	<b>18,840</b>	14,130
– Trademarks	–	18
– Deferred expenditure	<b>138</b>	270
Auditors' remuneration	<b>1,312</b>	1,302
Cost of inventories expensed	<b>43,560</b>	31,487
Depreciation of fixed assets	<b>68,519</b>	49,843
Loss on disposal of fixed assets	<b>458</b>	444
Net exchange losses	–	2,367
Operating lease rentals		
– Aircraft and related equipments	<b>332,340</b>	248,424
– Land and buildings	<b>20,226</b>	14,995
Outgoings in respect of investment properties	–	925
Provision for overhaul and major checks costs (note 20)	<b>95,658</b>	91,941

## 5. FINANCE COSTS

	<b>2003</b>	2002
	<b>HK\$'000</b>	HK\$'000
Interest expense on bank loan	–	648
Other incidental borrowing costs	–	7,778
	–	8,426



## 6. TAXATION CREDIT/(CHARGE)

	2003 HK\$'000	2002 HK\$'000
Company and subsidiaries:		
Hong Kong profits tax	–	(379)
Macau complementary tax	–	(9,153)
Taxation outside Hong Kong and Macau	<b>(613)</b>	(609)
Over provisions in prior years	<b>468</b>	–
Deferred taxation (note 21)	<b>30,333</b>	–
	<b>30,188</b>	(10,141)
Associated companies:		
Hong Kong profits tax	<b>(10,664)</b>	(52,307)
Macau complementary tax	<b>(10,463)</b>	(11,686)
Taxation outside Hong Kong and Macau	<b>(7,251)</b>	(8,744)
Over/(under) provisions in prior years	<b>15,075</b>	(1,669)
Deferred taxation	<b>(2,941)</b>	(4,796)
	<b>(16,244)</b>	(79,202)
	<b>13,944</b>	(89,343)

Hong Kong profits tax has been provided at the rate of 17.5% (2002: 16%) on the estimated assessable profit for the year. Macau complementary tax has been provided at the rate of 15.75% (2002: 15.75%) on the estimated assessable profit for the year. Taxation outside Hong Kong and Macau has been calculated on the estimated assessable profit for the year at the rates of taxation prevailing in the regions in which the Group operates.



## 6. TAXATION CREDIT/(CHARGE) (CONT'D)

The taxation on the Group's (loss)/profit before taxation differs from the theoretical amount that would arise using the applicable profits tax rate prevailing in the territory in which the Group's principal operating subsidiary operates as follows:

	2003 HK\$'000	2002 HK\$'000
(Loss)/profit before taxation	<b>(102,101)</b>	448,290
Calculated at a tax rate of 15.75% (2002: 15.75%)	<b>(16,081)</b>	70,606
Effect of different taxation rates in other territories	<b>6,487</b>	3,625
Income not subject to taxation	<b>(9,530)</b>	(7,862)
Expenses not deductible for taxation purposes	<b>10,428</b>	18,008
Utilisation of previously unrecognised tax losses	<b>(177)</b>	(230)
Increase in taxation resulting from an increase in tax rate	<b>4,540</b>	–
Withholding tax	–	1,620
Tax losses not recognised	<b>5,770</b>	4,366
(Over)/under provisions for taxation in prior years	<b>(15,543)</b>	1,669
Others	<b>162</b>	(2,459)
Taxation (credit)/charge	<b>(13,944)</b>	89,343

## 7. (LOSS)/PROFIT ATTRIBUTABLE TO SHAREHOLDERS

The (loss)/profit attributable to shareholders includes a profit of the Company to the extent of HK\$36,173,000 (2002: HK\$479,279,000).



## 8. DIVIDENDS

	2003 HK\$'000	2002 HK\$'000
Interim dividend, paid, of HK0.3 cent (2002: HK0.6 cent) per share	9,938	19,916
Final dividend, proposed, of HK0.6 cent (2002: HK0.8 cent) per share	19,876	26,554
Additional 2001 final dividend on shares issued under share options	–	505
Adjustment on 2002 final dividend due to repurchase of shares	(53)	–
	<u>29,761</u>	<u>46,975</u>

The Directors proposed a final dividend of HK0.6 cent per share. This proposed dividend is not reflected as a dividend payable in these accounts, but will be reflected as an appropriation of retained earnings for the year ending 31st December, 2004.

## 9. (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\$18,747,000 (2002: profit of HK\$317,417,000).

The basic (loss)/earnings per share is based on the weighted average of 3,314,824,000 (2002: 3,290,728,000) shares in issue during the year. No diluted loss per share for the year ended 31st December, 2003 is presented as the exercise of options is anti-dilutive. The diluted earnings per share for the year ended 31st December, 2002 was based on 3,346,872,000 shares representing the weighted average of 3,290,728,000 shares in issue during the year plus the weighted average of 56,144,000 shares which would be issued at no consideration on the exercise of all dilutive options.





## 10. DIRECTORS' AND SENIOR MANAGEMENT'S EMOLUMENTS

### (a) Directors' emoluments

The aggregate amounts of emoluments payable to Directors during the year are as follows:

	<b>2003</b> <b>HK\$'000</b>	2002 HK\$'000
Fees	<b>202</b>	80
Salaries and allowances	<b>5,973</b>	6,015
	<b>6,175</b>	6,095

Directors' emoluments include fees of HK\$80,000 (2002: HK\$80,000) to independent non-executive Directors.

During the year, 104,378,000 (2002: Nil) options were granted to the Directors under the share option scheme approved by the shareholders at the Annual General Meeting held on 29th May, 2002. The market value of the share at the date of grant is HK\$1.12 (2002: Nil). Details of options lapsed and exercised during the year are set out in note 18(a) below.

The emoluments of the Directors fell within the following bands:

Emolument bands	<b>Number of Directors</b>	
	<b>2003</b>	2002
HK\$ nil – HK\$1,000,000	<b>6</b>	7
HK\$1,000,001 – HK\$1,500,000	<b>1</b>	1
HK\$1,500,001 – HK\$2,000,000	<b>1</b>	1
HK\$2,000,001 – HK\$2,500,000	<b>1</b>	1
	<b>9</b>	10



## 10. DIRECTORS' AND SENIOR MANAGEMENT'S EMOLUMENTS (CONT'D)

### (b) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group for the year include three Directors (2002: three) whose emoluments are set out above. The emoluments payable to the remaining two (2002: two) individuals during the year are as follows:

	<b>2003</b> <b>HK\$'000</b>	2002 HK\$'000
Wages, salaries and allowances	<b>2,318</b>	–
Benefits in kind	–	43,746
Retirement benefit costs	<b>128</b>	–
	<b><u>2,446</u></b>	<b><u>43,746</u></b>

On 4th April, 2002, Messrs. Wang Guixiang and Xinwei, employees of the Group who were former Directors, in aggregate, exercised options for 84,126,000 shares at an exercise price of HK\$1.04 per share. The difference between the aggregate value of the Company's shares issued upon the exercise of these options at the exercise price of HK\$1.04 per share and the market price of the Company's shares on 4th April, 2002 of HK\$1.56 per share amounted to HK\$43,746,000 was included in the benefits in kind above.

The emoluments of the employees fell within the following bands:

	<b>Number of individuals</b>	
	<b>2003</b>	2002
Emolument bands		
HK\$1,000,001 – HK\$1,500,000	<b>2</b>	–
HK\$19,500,001 – HK\$20,000,000	–	1
HK\$23,500,001 – HK\$24,000,000	–	1
	<b><u>–</u></b>	<b><u>1</u></b>



## 11. FIXED ASSETS

	Group				
	Leasehold improvements	Aircraft and engines	Flight equipment and rotable spares	Machinery, other equipment, furniture and motor vehicles	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Cost or valuation					
As at 1st January, 2003	28,384	418,040	230,065	49,954	726,443
Additions	2,598	–	15,887	8,982	27,467
Disposals	(2,041)	–	(2,155)	(2,610)	(6,806)
<b>As at 31st December, 2003</b>	<b><u>28,941</u></b>	<b><u>418,040</u></b>	<b><u>243,797</u></b>	<b><u>56,326</u></b>	<b><u>747,104</u></b>
Accumulated depreciation					
As at 1st January, 2003	22,924	105,277	125,380	31,728	285,309
Charge for the year	1,350	31,849	29,542	5,778	68,519
Disposals	(2,017)	–	(1,551)	(2,534)	(6,102)
<b>As at 31st December, 2003</b>	<b><u>22,257</u></b>	<b><u>137,126</u></b>	<b><u>153,371</u></b>	<b><u>34,972</u></b>	<b><u>347,726</u></b>
Net book value					
<b>As at 31st December, 2003</b>	<b><u>6,684</u></b>	<b><u>280,914</u></b>	<b><u>90,426</u></b>	<b><u>21,354</u></b>	<b><u>399,378</u></b>
As at 31st December, 2002	5,460	312,763	104,685	18,226	441,134



## 12. INTANGIBLE ASSETS

	Group			Total HK\$'000
	Goodwill HK\$'000	Trademarks HK\$'000	Deferred expenditure HK\$'000	
Cost				
At 1st January, 2003 and at 31st December, 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 year	(18,840)	–	(138)	(18,978)
<b>As at 31st December, 2003</b>	<b>(32,970)</b>	<b>(928)</b>	<b>(2,679)</b>	<b>(36,577)</b>
Net book amount				
<b>As at 31st December, 2003</b>	<b>306,141</b>	<b>–</b>	<b>54</b>	<b>306,195</b>
As at 31st December, 2002	324,981	–	192	325,173

## 13. SUBSIDIARIES

	Company	
	2003 HK\$'000	2002 HK\$'000
Unlisted shares, at cost	803,666	803,666
Amounts due from subsidiaries	714,674	709,293
Amounts due to subsidiaries	(216)	(141)
	<b>1,518,124</b>	<b>1,512,818</b>

The amounts due from/to subsidiaries are unsecured, interest free and have no fixed terms of repayment.



## 13. SUBSIDIARIES (CONT'D)

The subsidiaries at 31st December, 2003 are set out below:

Name	Place of incorporation	Place of operation	Principal activities	Particulars of issued share/capital	Group equity interest	
					2003	2002
<sup>#1</sup> Air Macau Company Limited ("Air Macau")	Macau	Macau	Airline operator	4,000,000 ordinary shares of MOP100 each	51%	51%
<sup>1</sup> China National Aviation Corporation (Macau) Company Limited	Macau	Macau	Investment holding	Quota capital of MOP10,000,000	100%	100%
Skylink Global Limited	British Virgin Islands	Hong Kong	Investment holding	10 ordinary share of US\$1 each	100%	100%
Kingston International Limited	British Virgin Islands	Hong Kong	Investment holding	2 ordinary shares of US\$1 each	100%	100%
Queenston International Limited	British Virgin Islands	Hong Kong	Investment holding	2 ordinary shares of US\$1 each	100%	100%
Serfil Limited	British Virgin Islands	Hong Kong	Investment holding	1 ordinary share of US\$1	100%	100%
Skyrise Limited	British Virgin Islands	Hong Kong	Investment holding	1 ordinary share of US\$1	100%	100%
Wington Limited	British Virgin Islands	Hong Kong	Investment holding	1 ordinary share of US\$1	100%	100%
China National Aviation Logistics Company Limited	Hong Kong	Hong Kong	Investment holding	2 ordinary shares of HK\$10 each	100%	100%
China National Aviation Technology Company Limited	Hong Kong	Hong Kong	Investment holding	2 ordinary shares of HK\$10 each	100%	100%
<sup>1</sup> China National Aviation CyberWorks Limited	Bermuda	Hong Kong	Dormant	1,000,000 ordinary shares of HK\$0.1 each	100%	100%



### 13. SUBSIDIARIES (CONT'D)

All subsidiaries are limited liability companies.

# Subsidiary not audited by PricewaterhouseCoopers. The aggregate net assets and turnover of the subsidiary not audited by PricewaterhouseCoopers amounted to approximately 18% (2002: 23%), 100% (2002: 99%) respectively. The aggregate (loss)/profit before taxation and minority interests of the subsidiary not audited by PricewaterhouseCoopers has not been disclosed as the amount is not meaningful.

<sup>1</sup> Shares held indirectly by the Company.

### 14. ASSOCIATED COMPANIES

	Group		Company	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
Unlisted shares, at cost	–	–	51,789	51,789
Share of net assets	1,204,939	1,170,893	–	–
Loans to associated companies	82,103	76,853	37,560	37,560
	<b>1,287,042</b>	<b>1,247,746</b>	<b>89,349</b>	<b>89,349</b>

The loans to associated companies are unsecured, interest free and have no fixed terms of repayment.

The following is a list of principal associated companies at 31st December, 2003:

Name	Place of incorporation and operation	Principal activities	Particulars of issued share/capital	Group equity interest	
				2003	2002
<sup>1</sup> Hong Kong Dragon Airlines Limited ("Dragonair")	Hong Kong	Airline operator	500,000,000 ordinary shares of HK\$1 each	43.29%	43.29%
Jardine Airport Services Limited	Hong Kong	Airport ground handling services	1,000 ordinary shares of HK\$10 each	50.00%	50.00%
<sup>2</sup> Tradeport Hong Kong Limited	Hong Kong	Development and operation of a logistic center	400 ordinary shares of HK\$1 each	25.00%	25.00%
<sup>#2</sup> Menzies Macau Airport Services Limited	Macau	Airport ground handling services	Quota capital of MOP10,000,000	33.65%	33.65%
<sup>#2</sup> Macau Aircraft Repair and Conversion Company Limited	Macau	Aircraft repair and conversion	Quota capital of MOP100,000	25.05%	25.05%



## 14. ASSOCIATED COMPANIES (CONT'D)

- <sup>1</sup> 1.47% of the Group's equity interest in Dragonair is held directly by the Company, while the remaining 41.82% is held indirectly through subsidiaries.
- <sup>2</sup> Shares held indirectly by the Company.
- # Associated companies not audited by PricewaterhouseCoopers.

A summary of the audited financial information of Dragonair, a significant associated company of the Group is set out as follows:

	2003 HK\$'000	2002 HK\$'000
<b>Results</b>		
Turnover	<b>5,867,790</b>	5,942,475
Operating profit after finance costs	<b>52,617</b>	635,259
Share of profits less losses of associated companies	<b>16,212</b>	38,187
Profit before taxation	<b>68,829</b>	673,446
Taxation	<b>1,972</b>	(132,618)
Profit after taxation	<b>70,801</b>	540,828
<b>Net assets</b>		
Fixed assets	<b>6,831,966</b>	6,211,323
Investments in associated companies	<b>154,896</b>	159,264
Investments in securities	<b>20,234</b>	24,197
Deferred tax assets	<b>2,473</b>	–
Other non-current assets	<b>497,408</b>	611,135
Current assets	<b>3,188,993</b>	2,736,365
Current liabilities	<b>(2,263,513)</b>	(1,822,015)
Deferred income	<b>(475,047)</b>	(424,502)
Deferred liabilities	<b>(78,711)</b>	(98,610)
Provision for overhaul and major checks	<b>(155,966)</b>	(77,200)
Long-term liabilities	<b>(5,123,659)</b>	(4,787,720)
	<b>2,599,074</b>	2,532,237



## 15. TRADE AND OTHER RECEIVABLES

	Group		Company	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
Trade receivables (notes a and c)	111,440	121,000	–	–
Prepayments, deposits and other receivables	42,514	64,313	4,664	2,437
Due from:				
An associated company (notes b and c)	30	–	–	–
Fellow subsidiaries (notes b and c)	28	316	–	–
Related companies (notes b and c)	44	162	–	–
	<b>154,056</b>	<b>185,791</b>	<b>4,664</b>	<b>2,437</b>

- (a) The credit terms granted to sales agents and other trade customers are generally half month.
- (b) The amounts due from an associated company, fellow subsidiaries and related companies are unsecured, interest free and have credit periods ranging from 15 days to 45 days.
- (c) The age analysis of the trade receivable with third parties, an associated company, fellow subsidiaries and related companies is as follows:

	Group		Company	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
Within 31 days	103,643	112,690	–	–
31 – 60 days	7,198	8,499	–	–
61 – 90 days	112	289	–	–
Over 90 days	589	–	–	–
	<b>111,542</b>	<b>121,478</b>	<b>–</b>	<b>–</b>

## 16. BANK BALANCES AND CASH

Bank balances and cash of the Group include a deposit of HK\$25,637,000 (2002: HK\$13,155,000), which has been pledged to banks for banking facilities and guarantees granted to and obtained by the Group.





## 17. TRADE AND OTHER PAYABLES

	Group		Company	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
Trade payables (note a)	117,016	134,607	–	–
Other payables and accruals	166,489	147,441	4,160	8,439
Due to:				
Associated companies (notest a and b)	13,869	18,255	–	42
Fellow subsidiaries (notest a and b)	11,895	15,905	–	32
Immediate holding company (notest a and b)	50	181	50	62
Related companies (notest a and b)	63	1,004	–	–
	<b>309,382</b>	<b>317,393</b>	<b>4,210</b>	<b>8,575</b>

- (a) The age analysis of trade payable with third parties, associated companies, fellow subsidiaries, immediate holding company and related companies is as follows:

	Group		Company	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
Within 31 days	68,208	96,116	–	104
31 – 60 days	36,030	30,121	–	–
61 – 90 days	11,392	25,404	–	–
Over 90 days	27,213	18,311	–	32
	<b>142,843</b>	<b>169,952</b>	<b>–</b>	<b>136</b>

- (b) The amounts due to associated companies, fellow subsidiaries, immediate holding company and related companies are unsecured and interest free. Except for the amount due to immediate holding company which has no fixed terms of repayment, other balances have the credit terms generally ranging from 40 to 45 days.



## 18. SHARE CAPITAL

	<b>Ordinary shares of HK\$0.10 each</b>	
	<b>Number of shares</b>	<b>HK\$'000</b>
Authorised:		
At 1st January, 2002, 2003 and 31st December, 2003	4,000,000,000	400,000
Issued and fully paid:		
At 1st January, 2002	3,235,182,000	323,518
Exercise of share options (note a)	84,126,000	8,413
At 1st January, 2003	3,319,308,000	331,931
Repurchase of own shares (note b)	(6,628,000)	(663)
<b>At 31st December, 2003</b>	<b>3,312,680,000</b>	<b>331,268</b>

### (a) Share options

At an Annual General Meeting of the Company held on 29th May, 2002, a new share option scheme ("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.

Under the terms of the New Share Option Scheme, the Directors may, at their discretion, grant to any director, employee, supplier, customer or other relevant business partners of the Group, share options to subscribe for the Company's shares at the subscription price of the highest of (i) the closing price of the Company's shares as stated in The Stock Exchange of Hong Kong Limited's (the "Stock Exchange") daily quotations sheets on the date of grant; (ii) the average closing price of the Company's shares 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. A nominal consideration at HK\$1 was paid by grantee for the acceptance of the grant of share options.

The maximum number of shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under the New Share Option Scheme and any other share option scheme of the Group shall not exceed 30% of the number of issued shares of the Company from time to time.

The total number of shares to be granted under the New Share Option Scheme and any other share options scheme of the Group shall not exceed 331,930,800, representing 10% of the number of issued shares at the date of adoption of the New Share Option Scheme.

An option may be exercised in accordance with the terms of the New Share Option Scheme at any time during a period, in relation to the relevant option, to be notified by the Directors to the grantee, such period not exceeding six years commencing on the date falling three months after the date of grant and expiring on the last day of the said period.



18. SHARE CAPITAL (CONT'D)

(a) Share options (cont'd)

The New Share Option Scheme will remain in force for a period of ten years commencing on the date on which it was adopted.

Movements in the number of share options outstanding during the year are as follows:

	Number of options	
	2003	2002
At beginning of year	147,059,800	231,185,800
Granted (note i)	104,378,000	–
Exercised (note ii)	–	(84,126,000)
Lapsed (note iii)	(114,708,000)	–
At end of year (note iv)	136,729,800	147,059,800

(i) Shares options were granted on 25th July, 2003 at the exercise price of HK\$1.14 per share and will expire on 25th October, 2009. Consideration received was HK\$4 in respect of the share options granted during the year.

(ii) No options were exercised during the year ended 31st December, 2003. Options exercised on 4th April, 2002 resulted in 84,126,000 shares being issued at HK\$1.04 each, with proceed of HK\$87,491,000.

The market price of shares at the exercise date of 4th April, 2002 was HK\$1.56 and their aggregate market value was HK\$131,237,000.

(iii) During the year, 114,708,000 share options were lapsed in accordance with the terms of the old share option scheme.

(iv) Share options outstanding at the end of the year have the following terms:

Expiry Date	Exercise price	Number of options		Vested percentages	
		2003	2002	2003	2002
<b>Directors</b>					
11th July, 2003	1.04	–	114,708,000	–	100%
24th March, 2004	0.82	32,351,800	32,351,800	100%	100%
25th October, 2009	1.14	104,378,000	–	100%	–
		136,729,800	147,059,800		

No share options were cancelled during the year (2002: Nil).



## 18. SHARE CAPITAL (CONT'D)

### (b) Repurchase of own shares

In April 2003, 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. The highest and lowest prices per share paid for the repurchase were HK\$0.83 and HK\$0.77 respectively. The above shares repurchased were then cancelled.

## 19. RESERVES

### Group

	Share premium HK\$'000	Capital redemption reserve HK\$'000	Legal reserve HK\$'000	Investments revaluation reserve HK\$'000	Retained earnings HK\$'000	Total HK\$'000
At 1st January, 2003	1,434,558	–	3,666	4,180	930,164	2,372,568
Share of exchange differences of associated companies	–	–	–	–	59	59
Share of reserve realised upon disposal of investments in securities of an associated company	–	–	–	(1,716)	–	(1,716)
Repurchase of own shares (note 18(b))	–	663	–	–	(5,325)	(4,662)
Loss for the year	–	–	–	–	(18,747)	(18,747)
Dividends	–	–	–	–	(36,439)	(36,439)
<b>At 31st December, 2003</b>	<b><u>1,434,558</u></b>	<b><u>663</u></b>	<b><u>3,666</u></b>	<b><u>2,464</u></b>	<b><u>869,712</u></b>	<b><u>2,311,063</u></b>
Representing:						
Reserves	1,434,558	663	3,666	2,464	849,836	2,291,187
2003 final dividend proposed	–	–	–	–	19,876	19,876
<b>At 31st December, 2003</b>	<b><u>1,434,558</u></b>	<b><u>663</u></b>	<b><u>3,666</u></b>	<b><u>2,464</u></b>	<b><u>869,712</u></b>	<b><u>2,311,063</u></b>
Retained by:						
Company and subsidiaries	1,434,558	663	3,666	–	129,945	1,568,832
Associated companies	–	–	–	2,464	739,767	742,231
<b>At 31st December, 2003</b>	<b><u>1,434,558</u></b>	<b><u>663</u></b>	<b><u>3,666</u></b>	<b><u>2,464</u></b>	<b><u>869,712</u></b>	<b><u>2,311,063</u></b>



## 19. RESERVES (CONT'D)

### Group

	<b>Share premium</b>	<b>Capital redemption reserve</b>	<b>Legal reserve</b>	<b>Investments revaluation reserve</b>	<b>Retained earnings</b>	<b>Total</b>
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 1st January, 2002	1,355,480	–	–	6,324	653,872	2,015,676
Transfer	–	–	3,666	–	(3,666)	–
Share of exchange differences of an associated company	–	–	–	–	2,373	2,373
Share of deficit on revaluation of investments in securities of an associated company	–	–	–	(2,144)	–	(2,144)
Issue of new shares	79,078	–	–	–	–	79,078
Profit for the year	–	–	–	–	317,417	317,417
Dividends	–	–	–	–	(39,832)	(39,832)
At 31st December, 2002	<u>1,434,558</u>	<u>–</u>	<u>3,666</u>	<u>4,180</u>	<u>930,164</u>	<u>2,372,568</u>
Representing:						
Reserves	1,434,558	–	3,666	4,180	903,610	2,346,014
2002 final dividend proposed	–	–	–	–	26,554	26,554
At 31st December, 2002	<u>1,434,558</u>	<u>–</u>	<u>3,666</u>	<u>4,180</u>	<u>930,164</u>	<u>2,372,568</u>
Retained by:						
Company and subsidiaries	1,434,558	–	3,666	–	226,159	1,664,383
Associated companies	–	–	–	4,180	704,005	708,185
At 31st December, 2002	<u>1,434,558</u>	<u>–</u>	<u>3,666</u>	<u>4,180</u>	<u>930,164</u>	<u>2,372,568</u>

A subsidiary in Macau has transferred 10% of its profit to non-distributable legal reserve which is required to be retained in the accounts of the subsidiary in accordance with Article 432 of the Macau Commercial Code.



## 19. RESERVES (CONT'D)

## Company

	Share premium HK\$'000	Capital redemption reserve HK\$'000	Retained earnings HK\$'000	Total HK\$'000
At 1st January, 2003	1,434,558	–	660,641	2,095,199
Profit for the year	–	–	36,173	36,173
Repurchase of own shares (note 18(b))	–	663	(5,325)	(4,662)
Dividends	–	–	(36,439)	(36,439)
<b>At 31st December, 2003</b>	<b><u>1,434,558</u></b>	<b><u>663</u></b>	<b><u>655,050</u></b>	<b><u>2,090,271</u></b>
Representing:				
Reserves	1,434,558	663	635,174	2,070,395
2003 final dividend proposed	–	–	19,876	19,876
<b>At 31st December, 2003</b>	<b><u>1,434,558</u></b>	<b><u>663</u></b>	<b><u>655,050</u></b>	<b><u>2,090,271</u></b>
At 1st January, 2002	1,355,480	–	221,194	1,576,674
Profit for the year	–	–	479,279	479,279
Issue of new shares	79,078	–	–	79,078
Dividends	–	–	(39,832)	(39,832)
At 31st December, 2002	<u>1,434,558</u>	<u>–</u>	<u>660,641</u>	<u>2,095,199</u>
Representing:				
Reserves	1,434,558	–	634,087	2,068,645
2002 final dividend proposed	–	–	26,554	26,554
At 31st December, 2002	<u>1,434,558</u>	<u>–</u>	<u>660,641</u>	<u>2,095,199</u>



## 20. PROVISION FOR OVERHAUL AND MAJOR CHECKS

	Group	
	2003 HK\$'000	2002 HK\$'000
At beginning of year	53,695	–
Acquisition of subsidiaries	–	61,768
Charged during the year (note 4)	95,658	91,941
Utilised during the year	(84,484)	(100,014)
At end of year	<u>64,869</u>	<u>53,695</u>

## 21. DEFERRED TAXATION

	Group Tax losses	
	2003 HK\$'000	2002 HK\$'000
At beginning of year	–	–
Credited to profit and loss account (note 6)	30,333	–
At end of year	<u>30,333</u>	–
Deferred tax assets to be recovered after more than 12 months	<u>19,494</u>	–

Deferred taxation is calculated in full on temporary differences under the liability method using the statutory profits tax rate prevailing in which the Group's principal operating subsidiary operates of 15.75% (2002: 15.75%).

Deferred income tax assets are recognised for tax loss carry forwards to the extent that realisation of the related tax benefit through the future taxable profits is probable. The Group has unrecognised tax losses of HK\$54,155,000 (2002: HK\$37,679,000) to carry forward against future taxable income; these tax losses have no expiry date.



## 22. DISCONTINUING OPERATION OF PROPERTY HOLDING BUSINESS

The entire property holding business segment of the Group was vested in CNACG on 25th March, 2002. The property holding business segment was sold and is reported in the accounts as a discontinuing operation. The turnover, results, cash flows and net assets of the property holding business segment were as follows:

	<b>From 1st January, 2002 to 25th March, 2002</b>
	HK\$'000
Turnover	5,644
Other revenue	10
Administrative expenses	(1,334)
	<hr/>
Profit before taxation	4,320
Taxation	(379)
	<hr/>
Profit after taxation	3,941
	<hr/> <hr/>
Operating cash inflow	4,667
	<hr/> <hr/>
	<b>25th March, 2002</b>
	HK\$'000
Investment properties	600,000
Current assets	17,264
	<hr/>
Total assets	617,264
Total liabilities	(324,381)
	<hr/>
Net assets	292,883
	<hr/> <hr/>

The loss on discontinuing operation is insignificant to the accounts for the year ended 31st December, 2002 (note 23(c)).





## 23. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

### (a) Reconciliation of operating (loss)/profit to cash (used in)/generated from operations

	2003 HK\$'000	2002 HK\$'000
Operating (loss)/profit	(223,583)	61,836
Depreciation	68,519	49,843
Amortisation of goodwill	18,840	14,130
Amortisation of development costs, patents and trademarks	138	288
Loss on disposal of fixed assets	458	444
Interest income	(9,172)	(13,546)
Operating (loss)/profit before working capital changes	(144,800)	112,995
Decrease/(increase) in inventories	340	(5,697)
Decrease/(increase) in lease and equipment deposits	5,214	(8,981)
Decrease/(increase) in trade and other receivables	30,621	(38,799)
Change in balances with fellow subsidiaries	(3,722)	4,286
Change in balances with related companies	(823)	842
(Increase)/decrease in amount due to immediate holding company	(131)	80
Change in balances with associated companies	(4,416)	7,093
Increase in tenants' deposits	-	161
Increase in trade and other payables	4,688	66,177
Increase/(decrease) in sales in advance of carriage	1,226	(9,858)
Increase/(decrease) in provision for overhaul and major checks	11,174	(8,073)
Cash (used in)/generated from operations	<u>(100,629)</u>	<u>120,226</u>

### (b) Major non-cash transaction

During the year ended 31st December, 2002, the Group acquired the entire equity interest in CNAC Macau for an aggregate consideration of HK\$665,000,000. The purchase consideration was partially offset by the consideration payable of HK\$600,000,000 for the restructuring of the property holding business.



## 23. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (CONT'D)

## (c) Restructuring of the property holding business

	2003 HK\$'000	2002 HK\$'000
Net assets disposed of:		
Investment properties	—	600,000
Trade and other receivables	—	5,970
Tax recoverable	—	346
Bank balances and cash	—	10,140
Trade and other payables	—	(16,456)
Amounts due to holding company	—	(307,117)
	<hr/>	<hr/>
	—	292,883
Add: Amounts due from former subsidiaries assigned to the CNACG	—	307,117
	<hr/>	<hr/>
	—	600,000
	<hr/> <hr/>	<hr/> <hr/>
Satisfied by:		
Consideration payable for the acquisition of CNAC Macau	—	600,000
	<hr/> <hr/>	<hr/> <hr/>
Net cash outflow in respect of restructuring of the property holding business	—	10,140
	<hr/> <hr/>	<hr/> <hr/>



## 23. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (CONT'D)

## (d) Purchase of business

	2003 HK\$'000	2002 HK\$'000
Net assets disposed of:		
Intangible assets	—	480
Fixed assets	—	458,680
Associated companies	—	62,508
Lease and equipment deposits	—	79,274
Inventories	—	45,467
Trade and other receivables	—	145,583
Amount due from a fellow subsidiary	—	237
Pledged deposits	—	7,923
Bank balances and cash	—	466,041
Trade and other payables	—	(337,505)
Amounts due to fellow subsidiaries	—	(11,540)
Amount due to an associated company	—	(11,162)
Amount due to immediate holding company	—	(101)
Sales in advance of carriage	—	(116,101)
Taxation payable	—	(9,726)
Long-term bank loan	—	(241,512)
Provision for overhaul and major checks	—	(61,768)
Minority interests	—	(276,677)
	—	200,101
Add: Shareholder's loan assigned to the Group included in trade and other payables above	—	130,391
	—	330,492
Goodwill	—	339,111
	—	669,603
Satisfied by:		
Consideration for the restructuring of the property holding business	—	600,000
Cash consideration (including direct costs of HK\$4,603,000 relating to the acquisition)	—	69,603
	—	669,603



### 23. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (CONT'D)

#### (d) Purchase of business (cont'd)

The subsidiaries acquired during the year ended 31st December, 2002 contributed HK\$110,631,000 to Group's net operating cash flows, paid HK\$270,992,000 in respect of financing activities and contributed HK\$21,233,000 for investing activities.

	2003 HK\$'000	2002 HK\$'000
Cash consideration	–	(69,603)
Bank balances and cash in hand acquired	–	466,041
	<hr/>	<hr/>
Net cash inflow in respect of the purchase of subsidiaries	–	396,438
	<hr/> <hr/>	<hr/> <hr/>

#### (e) Analysis of changes in financing during the year

	Share capital including premium		Minority interests		Long-term bank loan		Dividend payable	
	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000	2003 HK\$'000	2002 HK\$'000
At beginning of year	1,766,489	1,678,998	318,207	–	–	–	3,252	3,483
Acquisition of subsidiaries	–	–	–	276,677	–	241,512	–	–
Minority interests' share of (loss)/profits	–	–	(69,410)	41,530	–	–	–	–
Dividends	–	–	–	–	–	–	36,439	38,822
Repurchase of own shares out of distributable profits	4,662	–	–	–	–	–	–	–
Cash (outflows)/inflows	(5,325)	87,491	–	–	–	(241,512)	(39,670)	(39,053)
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
At end of year	1,765,826	1,766,489	248,797	318,207	–	–	21	3,252
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### 24. COMMITMENTS

- (a) 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 (2002: HK\$42,900,000). As at 31st December, 2003, no payment has been made by the Group to the JV.



24. COMMITMENTS (CONT'D)

- (b) 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 Hong Kong International Airport (the "Project"). The Group has 25% equity 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 (2002: HK\$130,650,000), of which HK\$44,096,000 (2002: HK\$38,846,000) was advanced to the Project as at 31st December, 2003.

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 Consortium Partners have jointly given a guarantee to the Airport Authority in respect of their obligations to provide sufficient funding for the Project. Had the Group been 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 have been approximately HK\$649,350,000 (2002: HK\$649,350,000).

- (c) Commitments under operating leases

The Group had future aggregate minimum lease payments under non-cancellable operating leases in respect of aircraft and related equipment as follows:

	2003 HK\$'000	Group 2002 HK\$'000
Not later than one year	290,071	388,854
Later than one year and not later than five years	831,081	1,020,708
More than five years	609,249	—
	<u>1,730,401</u>	<u>1,409,562</u>

At 31st December, 2003, the Company did not have any significant commitments (2002: Nil).

25. FINANCIAL INSTRUMENTS

- (a) Foreign currency swap contracts

The Group employed foreign exchange contracts to manage its foreign currency exposure in Taiwan. The Group has no foreign exchange contracts outstanding at 31st December, 2003 (2002: HK\$23,400,000). These instruments are used solely to reduce or eliminate the foreign exchange risk associated with the operation activities and not for trading and speculation purposes.



## 25. FINANCIAL INSTRUMENTS (CONT'D)

### (b) Fuel price forward contact

As at 31st December, 2003, the Group had a forward contract with a third party to lock in future fuel price at a certain range. According to the contract, the Group is entitled to receive the difference between the fuel price and the strike price of US\$28 per barrel for a notional quantity of 5,000 barrels if the fuel price rises above the strike price and pay the difference between the fuel price and the strike price of US\$22.75 per barrel for a notional quantity of 10,000 barrels if the fuel price falls below the strike price.

## 26. CONTINGENT LIABILITIES

	<b>Group and Company</b>	
	<b>2003</b>	2002
	<b>HK\$'000</b>	HK\$'000
Guarantee for banking facilities granted by bank to an associated company	<b>75,000</b>	75,000

## 27. JOINTLY CONTROLLED OPERATION

The Group has entered into a jointly controlled operation to operate air transportation service between Macau and Taiwan.

The aggregate amounts of turnover and results recognised in the accounts relating to the Group's interest in the jointly controlled operation are as follows:

	<b>Group</b>	
	<b>2003</b>	2002
	<b>HK\$'000</b>	HK\$'000
Results for the year		
Turnover	<b>15,120</b>	54,581
Operating expenses	<b>(527)</b>	(1,865)
Group's share of profit for the year	<b>14,593</b>	52,716

There were no assets and liabilities relating to the jointly controlled operation recognised in the accounts as at 31st December, 2003 (2002: Nil).

The jointly controlled operation was terminated during the year.



## 28. RELATED PARTY TRANSACTIONS

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

	2003 HK\$'000	2002 HK\$'000
Management fee paid to:		
– Immediate holding company (note i)	6,000	6,000
– A fellow subsidiary (note ii)	3,600	2,768
Landing, loading, parking and other airport charges paid to a fellow subsidiary (note iii)	51,927	81,045
Ground handling costs paid to an associated company (note iv)	93,858	87,075
Technical and ground handling costs paid to an associated company (note v)	3,201	2,497
Inflight meal services expenses paid to a related company (note vi)	40,637	43,965
Over-riding commission paid to a related company (note vii)	–	10,123
Value of tickets sold to (note viii):		
– An associated company	550	–
– Fellow subsidiaries	4,201	6,553
– Related companies	15,468	40,769
	<b>15,468</b>	<b>40,769</b>

- (i) On 3rd August, 2001, the Company and CNACG entered into a management services agreement pursuant to which CNACG agreed to provide secretarial, personnel, accounting and general office administrative services to the Group for a period of two years from 1st July, 2001 to 30th June, 2003 at a monthly fee of HK\$500,000. The management services agreement was renewed on 27th August, 2003 with same terms for a period of two years commencing 1st July, 2003.
- (ii) The Group entered into a management services agreement with CNAC (Macau) Aviation Limited pursuant to which CNAC (Macau) Aviation Limited provides 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 either at terms pursuant to the tariff published by the Macau Airport or at terms pursuant to agreements entered into by the Group with ADA or the Macau 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 services rendered 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 Taiwan area.
- (viii) Air tickets were sold to the related ticket sales agents in accordance with the pricing policy of the Group.

**28. RELATED PARTY TRANSACTIONS (CONT'D)**

In addition to the above, on 18th October, 1997, the Company entered into a license agreement with China National Aviation Corporation ("CNAC") pursuant to which CNAC has agreed to grant a license to the Company, free of royalty, for the use of certain trademarks in Hong Kong, the Taiwan region and Macau 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 year (2002: Nil).

**29. ULTIMATE HOLDING COMPANY**

The Directors regard China National Aviation Holding Limited, a state-owned enterprise established in the People's Republic of China, as being the ultimate holding company.

**30. APPROVAL OF ACCOUNTS**

The accounts were approved by the Board of Directors on 26th March, 2004.