



## CHAIRMAN'S STATEMENT

Dear Shareholders,

2003 was a year filled with difficult challenges for us. The outbreak of Severe Acute Respiratory Syndrome ("SARS") during 2003 in China and other parts of Asia caused an unprecedented adverse impact to our business. Nevertheless, the Group and our staff did not succumb to these difficult circumstances. With the recovery of the economy after the SARS epidemic was brought under control, together with the support of the government through implementation of a series of related policies, we once again were given the opportunities for development and achieved satisfactory performance in terms of safety and services quality.



**Yan Zhi Qing**  
*Chairman*

During the first half of 2003, the Group encountered the most severe challenge due to the outbreak of SARS. The Group's air passenger business was severely affected as a result and recorded a significant drop in the number of passengers carried and passenger load factor for the period from April to June 2003, as compared to the corresponding period of the previous year. In terms of revenue tonne kilometres, there was a decrease of 40%, 83.5% and 61.5% respectively in April, May and June comparing to the corresponding period of the previous year. To minimise the negative impact of SARS, the Group took various timely measures to adjust its operating capacity, including reduction in the number of flights and suspension of certain routes to cope with the sharp decrease in demand for air transport caused by SARS. In addition, we also minimised controllable expenses through strictly controlling expenses to offset part of the negative impact.

In order to alleviate the operational pressure on the PRC's civil aviation industry caused by the SARS epidemic, the PRC government waived the levies of China Aviation Administration of China ("CAAC") Infrastructure Development Fund, sales tax and related supplementary charges for passenger transportation business for the period from 1 May to 31 December, 2003. These measures have significantly boosted the recovery of the Group's business.

While the Group was dealing with the challenges brought by the SARS epidemic, we continued to enhance the standards of our safety and services. As a result, we once again received the Golden Roc Cup, the highest award for flight safety in the civil aviation industry, and won the Five-star Diamond Award for flight services. These awards demonstrated the excellent performance of our colleagues in their effort to improve the standards of our safety and services.

In July 2003, the Group successfully issued 1,000,000,000 A Shares in the domestic market for listing and raised an aggregate proceeds of RMB2,700,000,000. Such proceeds have been applied to acquire the new model of Boeing 737 series and related flight equipment. The successful offering of A Shares was crucial to the realisation of our business goal, as it marked the entry of the Company into the PRC capital market. The successful fund raising exercise provides the Group with additional capital resources for future development, improves the Group's assets quality and strengthens its operating capacity, which in turn provides a solid foundation for the Group to compete efficiently in the ever increasingly competitive civil aviation market.



## CHAIRMAN'S STATEMENT (Cont'd)



The injection of the airline transportation businesses of China Northern Airlines Company and Xinjiang Airlines Company into the Group by China Southern Air Holding Company ("CSAHC"), the controlling shareholder of the Company, is progressing as scheduled. Since 1 January, 2003, the three airlines have implemented a code sharing arrangement, whereby the flight code of CZ is used for the flights of the three airlines. The preparatory work for business integration and assets restructuring is making good progress. The proposed restructuring will provide the Group with opportunities for expanding its flight networks and enlarging its market share in the civil aviation industry.

In view of global and domestic economic development, we believe that there will be robust growth in the airlines market in the coming year. The global economy has shown a visible recovery in a new cycle of economic growth, which will stimulate rapid development of the global air transport business. China's macro economic development in 2004 will also help to maintain the growth momentum of China in its economic cycle. The direction and guidelines of the Government in economic development represent the principles of scientific development, pursuant to which China's economy will see integral, harmonious and sustainable growth whilst maintaining a stable



and rapid pace of development. The stably increasing consumption will gradually replace the previously substantial investments as a stimulant to economic growth. China's air transportation industry has regained growth on all fronts after the SARS outbreak and the overall growth trend will gain further momentum in the coming year. The Group, as a major player in the PRC airlines market, will make its contributions to the growth of the domestic economy. Meanwhile, the implementation of the Closer Economic Partnership Arrangement between mainland China, Hong Kong and Macau, and the State policies on the overall development of the Western region and the revitalisation of the old industrial base of Northeast China will provide a perfect opportunity for the business growth of the Group.

With the approval of the State Council, the "Pricing Reform Plan for the Domestic Civil Aviation Industry" was adopted on 20 April, 2004. Pursuant to this Pricing Reform Plan, the pricing guidelines formulated by the government will be applied to the domestic air transport industry. Direct control by governmental pricing authorities over airfares for different flight routes will be changed to indirect control through the setting of basic rates and price ranges for air transport by such governmental pricing authorities. China's airlines will be able to determine their own airfares within the price ranges set by the governmental pricing authorities based on the changes in supply and demand of the market, and will adopt more flexible sales policies with an objective of maximising economic benefits. It is expected that as the reform in China's civil aviation industry continues to intensify, airline operators will gain a greater level of autonomy in managing their own business operations, and the Group will be able to achieve further business growth through fair and positive competition in a gradually regulated and orderly market.



## CHAIRMAN'S STATEMENT (Cont'd)

On the other hand, recent political instability in the Middle East and other uncertainties continue to hamper global economic growth. The continuing high jet fuel price is also a factor unfavorable to the growth of the air transport industry.

Challenges come with opportunities. In this year, the Group will continue to ensure a high standard of safety in our service and expedite its progress in the restructuring of the airline-related businesses with CSAHC. The Group will further strengthen its market competitiveness and strive to maintain and increase its market share. The Group will strive to achieve the above objectives through the following measures:

1. In the middle of the year, the Group will be able to enhance its operating capacity, route coverage and flight networks after the official opening of the Guangzhou New Airport and the commencement of operation of terminal No. 1 in the Beijing Capital International Airport leased by the Group.
2. Consistent with the business policies that emphasise development in the domestic market and expansion into overseas market for further growth, the Group will build domestic transportation hubs, optimise its flight networks in China and at the same time, actively explore overseas and regional markets. We will increase our overseas market share by opening new routes including flights from Guangzhou to Paris and adjusting our international cargo flights during the year.
3. We will further promote the "China Southern" brand name and enhance brand value in terms of "Reliability, Punctuality and Convenience".
4. The Group's cargo operation will be advanced to a higher standard upon the commencement of operation of the Guangzhou New Airport and its new cargo transportation centre.
5. We will continue to strengthen our financial management and tighten cost controls.

Looking back on 2003, we and our counterparts in the air transport industry had been striving for growth and meeting challenges amid difficult market conditions. On behalf of the board, I would like to express our gratitude to our management and staff. If not for their team spirit and dedication, China Southern Airlines would not have managed to overcome these unprecedented difficulties. We are particularly grateful to our front line staff who have shown their professional attitude and devotion by bravely and diligently performing their duties in the dangerous situation during the SARS outbreak. Finally, I would like to express our sincere gratitude to our shareholders for their continuous trust and support.

**Yan Zhi Qing**

*Chairman*

Guangzhou, the PRC

23 April, 2004