IMPORTANT

If you are in any doubt about this prospectus, you should consult your stockbroker, bank manager, solicitor, professional accountant or other professional advisers.

海南美蘭機場股份有限公司
Hainan Meilan Airport Company Limited*

(A joint stock company incorporated in the People's Republic of China with limited liability)

PUBLIC OFFER AND INTERNATIONAL PLACING

Number of H Shares	:	**201,700,000 H Shares comprising 198,000,000 New H Shares and 3,700,000 Sale H Shares (subject to the Over-allotment Option)**
Number of Public Offer Shares	:	**20,170,000 H Shares (subject to reallocation)**
Number of International Placing Shares	:	**181,530,000 H Shares (subject to reallocation and the Over-allotment Option)**
Offer Price	:	**Not more than HK$3.79 per H Share and expected to be not less than HK$3.15 per H Share (payable in full by applicants in the Public Offer subject to refund)**
Nominal Value per H Share	:	**RMB1.00**
Stock Code	:	**357**

Global Coordinator and Bookrunner

The Hongkong and Shanghai Banking Corporation Limited

Joint Sponsors and Joint Lead Managers

The Hongkong and Shanghai Banking Corporation Limited

Oriental Patron Asia Limited

Co-Lead Managers

CITIC Capital Markets Limited | **ICEA Capital Limited** | **ING Bank N.V.** | **Nomura International (Hong Kong) Limited**

The Stock Exchange of Hong Kong Limited and Hong Kong Securities Clearing Company Limited take no responsibility for the contents of this prospectus, make no representation as to its accuracy or completeness and expressly disclaim any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of the contents of this prospectus.

A copy of this prospectus, having attached thereto the documents specified in the paragraph headed "Documents Delivered to the Registrar of Companies" in Appendix XI, has been registered by the Registrar of Companies in Hong Kong as required by section 342C of the Companies Ordinance. The Securities and Futures Commission of Hong Kong and the Registrar of Companies in Hong Kong take no responsibility for the contents of this prospectus or the documents referred to above.

The Offer Price is expected to be fixed by agreement between HSBC and Oriental Patron, on behalf of the Underwriters, and the Company on or before 5:00 p.m. (Hong Kong time) on the Price Determination Date. The Price Determination Date is expected to be on or about 12th November, 2002 and in any event not later than 14th November, 2002. The Offer Price will not be more than HK$3.79 per H Share and is expected to be not less than HK$3.15 per H Share, although HSBC and Oriental Patron, on behalf of the Underwriters, may with the prior written consent of the Company, reduce such indicative Offer Price range at any time prior to the morning of the last day for lodging applications under the Public Offer. Applicants should note that in no circumstances can applications be withdrawn once submitted. If, for any reason, the Offer Price is not agreed between the Company, HSBC and Oriental Patron, on behalf of the Underwriters, the Offering will not proceed and will lapse.

The Company is incorporated, and its businesses are located, in the PRC. Potential investors in the Company should be aware of the differences in the legal, economic, and financial systems between the PRC and Hong Kong and that there are different risk factors relating to investment in PRC-incorporated companies. Potential investors should also be aware that the regulatory framework in the PRC is different from the regulatory framework in Hong Kong and should take into consideration the different market nature of the Shares of the Company. Certain of such differences and risk factors are set out in the sections headed "Risk Factors" and "Appendix IX — Summary of Principal Legal and Regulatory Provisions and Articles of Association". Investors should also be aware that the companies and securities regulatory framework in the PRC to which the Company is subject has only recently been introduced.

6th November, 2002

* *For identification purpose only*

	2002 [1]
Latest time to lodge **white** and **yellow** application forms	12:00 noon on Monday, 11th November
Application lists open[2]	11:45 a.m. on Monday, 11th November
Application lists close[2]	12:00 noon on Monday, 11th November
Price Determination Date (expected)[3]	on Tuesday, 12th November
Announcement of the level of indication of interest in the International Placing, the results of applications and the basis of allocation of the Public Offer Shares to be published in the South China Morning Post (in English) and the Hong Kong Economic Times (in Chinese) on	Friday, 15th November
Despatch of H Share certificates and refund cheques[4][5][6]	Friday, 15th November
Dealings in the H Shares expected to commence on	Monday, 18th November

(1) All times refer to Hong Kong local time. Details of the structure of the Offering, including its conditions, are set out in the section headed "Structure of the Offering".

(2) If there is a "black" rainstorm warning or tropical cyclone warning signal number 8 or above in force at any time between 9:00 a.m. and 12:00 noon on 11th November, 2002, the application lists will not open on that day. Further information is set out under "Effect of Bad Weather on the Opening of the Application Lists" in the section headed "How to Apply for Public Offer Shares".

(3) The Price Determination Date is expected to be on or around Tuesday, 12th November, 2002, and in any event will be on or before Thursday, 14th November, 2002. If, for any reason, the Offer Price is not agreed on or before Thursday, 14th November, 2002, the Offering will not proceed and will lapse.

(4) Refund cheques will be issued in respect of wholly or partially unsuccessful applications and in respect of successful applications if the Offer Price is determined at less than the price payable on applications.

(5) Any applicant for 1,000,000 H Shares or more and who has indicated in his/her application forms that he or she wishes to collect refund cheque (where applicable) and H Share certificates (where applicable) personally may collect refund cheque (where applicable) and H Share certificate (where applicable) personally from the Company's H Share registrar, Computershare Hong Kong Investor Services Limited, at Shops 1712–1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong from 9:00 a.m. to 1:00 p.m. on 15th November, 2002 or any other date notified by the Company in the newspapers as the date of despatch of H Share certificates/refund cheques. Applicants being individuals who opt for personal collection must not authorise any other person to make collection on their behalf. Applicants being corporations who opt for personal collection must attend by their authorised representatives bearing letters of authorisation from their corporations stamped with the corporation chop. Both individuals and authorised representatives must produce at the time of collection evidence of identity acceptable to Computershare Hong Kong Investor Services Limited.

(6) Uncollected H Share certificates and refund cheques will be despatched by ordinary post at the applicants' own risk to the addresses specified in the relevant application forms. For any applicant who has applied for less than 1,000,000 H Shares or who has applied for 1,000,000 H Shares or more but has not indicated in the application form that he or she wishes to collect the H Share certificates and/or refund cheques, his/her H Share certificates (if applying by using a white application form) and/or refund cheque will be sent to the address on the applicant's application form on 15th November, 2002, by ordinary post and at the applicant's own risk. Further information is set out in the section headed "How to Apply for Public Offer Shares". For further details of the Offering, see the section headed "Information about this Prospectus and the Offering" in this prospectus.

CONTENTS

You should rely only on the information contained in this prospectus and the application forms to make your investment decision. None of the Company and the Vendors has authorised anyone to provide you with information that is different from what is contained in this prospectus. Any information or representation not made in this prospectus must not be relied on by you as having been authorised by the Company, the Vendors, the Joint Sponsors, the Underwriters, any of their respective directors, or any other person or party involved in the Offering.

CONTENTS

This summary aims to give you an overview of the information contained in this prospectus. Because this is a summary, it does not contain all the information that may be important to you. You should read the whole document before you decide to invest in the H Shares. There are risks associated with any investment. Some of the particular risks in investing in the H Shares are set out in the section headed "Risk Factors". You should read that section carefully before you decide to invest in the H Shares.

THE COMPANY

The Company, a joint stock company incorporated in the PRC with limited liability, was established on 28th December, 2000 to operate the Meilan Airport.

Occupying approximately 560 hectares of land, the Meilan Airport is located in the southeast of Haikou, the capital city of Hainan Province, PRC and approximately 25 kilometres away from the city centre of Haikou. The Meilan Airport commenced commercial operation on 25th May, 1999 and was ranked the eighth largest airport in China in terms of passenger throughput, the ninth largest in terms of aircraft movements and the thirteenth largest in terms of cargo throughput in 2001, according to CAAC Journal 2002. During 2001, passenger departures and arrivals at the Meilan Airport reached approximately 5.08 million and aircraft takeoffs and landings reached approximately 53,800.

The Meilan Airport has one runway, one Terminal and one cargo centre. The runway has been constructed in accordance with ICAO category 4E standards and is capable of accommodating landing and takeoff of Boeing 747-400 aircraft, the largest commercial airliner. The Terminal has an annual handling capacity of approximately six million passenger arrivals and departures. The cargo centre has an annual capacity of approximately 54,000 tonnes of cargo.

The Group is engaged in both aeronautical and non-aeronautical businesses at the Meilan Airport. The Group's aeronautical business consists of the provision of airfield services, through a revenue sharing arrangement with Parent Company, and the provision of terminal facilities, ground handling services, passenger and cargo handling services. Its non-aeronautical business includes leasing of commercial and retail spaces at the Meilan Airport, airport-related business franchising, advertising, car parking, tourism services and sales of duty-free and consumable goods.

For each of the three years ended 31st December 2001, the total operating revenues of the Group were approximately RMB80.5 million, RMB161.6 million and RMB185.0 million, respectively. For the five months ended 31st May, 2002, the total operating revenues were approximately RMB118.5 million. Please refer to the sections headed "Business" and "Financial Information" for further information.

HISTORY AND DEVELOPMENT

The construction of the Meilan Airport commenced in November 1996 initially by Meilan International, a company established and wholly-owned by HAC, and was completed in February 1999.

Parent Company was established on 25th August, 1998 by its promoters, namely Central South Bureau, Hainan Airlines, Hainan International Trust and Investment Company Limited and Aviation Oil, with a registered capital of RMB600 million and took over the development and construction of the Meilan Airport from Meilan International. Each of Central South Bureau, Hainan

Airlines, Hainan International Trust and Investment Company Limited and Aviation Oil held 50.0%, 33.4%, 8.3% and 8.3% equity interest in Parent Company, respectively. On 8th August, 2000, the registered capital of Parent Company was increased to RMB1,350 million through further capital injection. Immediately following such further capital injection, the shareholders of Parent Company were Hainan Airlines, HNA Group, Central South Bureau, Hainan Asset Bureau, China Southern Airlines and Aviation Oil and their shareholdings in Parent Company were approximately 30.0%, 28.1%, 22.2%, 8.6%, 7.4% and 3.7% respectively. In December 2000, the 8.6% stake held by Hainan Asset Bureau was allocated to Golden City pursuant to a directive issued by Hainan Asset Bureau (Qiong Guo Zi Wei [2000] No. 6).

In preparation for the Offering and the listing of H Shares on the Stock Exchange, the Company was established on 28th December, 2000 by Parent Company, HNA Group, Hainan Airlines, China Southern Airlines and Central South Aviation Development. Parent Company owns 95% of the Company, and has satisfied its capital contribution by injecting into the Company the Terminal, aprons, aircraft connection bridges, ground traffic control centre, fire fighting centre, emergency centre and certain other assets, while Hainan Airlines, HNA Group, China Southern Airlines and Central South Aviation Development respectively injected capital of approximately RMB6.9 million, RMB4.6 million, RMB1.2 million and RMB3.6 million into the Company in cash and own approximately 2.1%, 1.4%, 0.4% and 1.1% of the share capital of the Company, respectively. The value of the net assets injected by Parent Company amounted to RMB310.2 million, according to the valuation performed by Hainan Asset Valuation Company as described in its valuation report dated 8th November, 2000.

To enhance efficiency and integration of its business operations, Parent Company and the Company entered into an Asset Swap Agreement pursuant to which the Company purchased four assets which were valued by an independent PRC valuation at approximately RMB78.1 million from Parent Company and sold three assets at a book value of approximately RMB28.4 million to Parent Company. Among the four assets purchased, 60.0% of the registered capital in Meilan Travelling and 95.0% of the registered capital of DFG were sold to the Company for cash consideration only, while the consideration for the remaining assets were settled by a combination of cash and assets sold to Parent Company. The Company has agreed to settle the aggregate purchase price difference in the amount of approximately RMB49.7 million by three cash instalment payments within 12 months from the date of the Asset Swap Agreement.

The businesses that are retained by Parent Company include the ownership and maintenance of the runway. Pursuant to the Agreement on Runway, Parent Company has agreed to, among others, maintain the runway in accordance with the applicable regulatory and industrial standards and continually hold the airport permit and maintain the validity thereof for a term of 20 years. Parent Company has also granted to the Company an option to acquire the runway from Parent Company in future. Please refer to the sections “Business — Restructuring of the Group” and “Business — Connected Transactions — Agreement on Runway” of this prospectus for more details on the arrangements regarding the runway.

Further details of the Restructuring are set out in the section headed “Restructuring of the Group” in the “Business” section of this prospectus.

RELATIONSHIP WITH THE STRATEGIC INVESTOR

Overview

Copenhagen Airports A/S, the Strategic Investor, is one of Europe's listed airport companies, with a market capitalisation of approximately DKK4,659 million (US$621.0 million) as at the Latest Practicable Date. The Strategic Investor has interests in 13 airports, with a total passenger throughput of over 33 million passengers per annum, in Denmark, Norway, Mexico and the United Kingdom. The largest of these airports is Copenhagen Airport in Denmark, which has a passenger throughput of over 18 million passengers per annum. Copenhagen Airport is the intercontinental hub for SAS (Scandinavian Airlines), one of the European hubs for the Star Alliance airline group and the North-European hub for DHL. Copenhagen Airport won the IATA "Best Airport in the World Award" in both 2000 and 2002 and has also previously been rated as Europe's best airport. It has been ranked highest in such areas as airport-related infrastructure, customer service and shopping and dining facilities.

The Strategic Investor has conditionally agreed to subscribe for the Strategic Placing Shares through the Strategic Placing Underwriter pursuant to the Strategic Investment Agreement. Further details of the Strategic Placing are set out in the sections headed "Business — Relationship with the Strategic Investor" and "Structure of the Offering — The Strategic Placing" of this prospectus.

Shareholders' Agreement

Under the Shareholders' Agreement, the Strategic Investor, Parent Company and HNA Group have agreed on, amongst other things, certain issues relating to the following:

(a) Board representation;

(b) Board reserved matters;

(c) Restrictions on further acquisition of Shares;

(d) Restrictions on disposal of Shares;

(e) Non-competition undertakings; and

(f) Co-investment rights.

Further details of the Shareholders' Agreement are set out under the section headed "Business — Relationship with the Strategic Investor" of this prospectus.

Technical Services Agreement

The Company and CADI have entered into the Technical Services Agreement for the provision by CADI to the Group of certain technical and advisory services in respect of the long-term management and development of the Meilan Airport. Details of the Technical Services Agreement are set out under the section headed "Business — Relationship with the Strategic Investor" of this prospectus.

BUSINESS STRATEGY AND STRENGTHS

Business Strategy

The Group's strategy is to focus on Haikou's unique position as the provincial capital and the main gateway to Hainan, the "Hawaii of China", and includes the following specific elements:

Prepare for anticipated increase in air traffic demand. According to Booz Allen Hamilton, the independent air traffic consultant, air traffic in terms of passenger throughput at the Meilan Airport is expected to increase by approximately 10.2% and 9.2% annually from 2001 to 2006 and from 2001 to 2011, respectively (please see Appendix V to this prospectus). To take advantage of the expected increase in air traffic, the Group plans to expand its current operating facilities. The current plan includes expanding the Terminal by approximately 30,000 m^2 and the apron area by approximately 280,000 m^2, adding 20 aircraft parking stands and eight air bridges.

Capitalise on its management expertise to create an airport management brand name and manage other airports. The management of the Group has considerable experience in operating airports and believes such experience can be utilised to the Group's benefit. The Group intends to build up its reputation as a premier airport management group in the PRC. The Sanya Management Contract in relation to the management of the Sanya Airport was signed with SPIA on 23rd August, 2002. Pursuant to this contract, the Group is responsible for the day-to-day management of the Sanya Airport, including its operations, finance, accounting, administration and investment activities, for five years commencing from 1st August, 2002. Please refer to the section headed "Business — Sanya Management Contract" of this prospectus.

Increase operation efficiency. The Group plans to improve its overall operating and financial performance and to carefully control its operating costs. By benchmarking its operating and financial performance metrics against those of leading international airport operators, the Group intends to identify and eliminate inefficiencies in its airport operations.

Increase non-aeronautical revenues. For each of the three years ended 31st December, 2001 and the five months ended 31st May, 2002, revenues from non-aeronautical businesses of the Group represented approximately 28.6%, 26.1%, 28.1% and 19.1% of the Group's total revenue. The Group plans to expand its non-aeronautical business in the areas of tourist services, franchising, sales of goods at the Terminal and other non-aeronautical activities. The Directors believe that the anticipated international airport status and expected higher number of international flights utilising the Meilan Airport will contribute to the continued growth of the Group's non-aeronautical operations.

Increase cargo throughput. The cargo throughput in 2001 increased by 3.6% over 2000. The growth of cargo throughput in the first five months of 2002 was 9.3% over the corresponding period of 2001. The Directors believe that cargo throughput at the Meilan Airport will grow significantly in the next several years. The Group plans to build a new cargo centre with a floor area of approximately 30,000 m^2, and a cargo apron with a total area of approximately 50,000 m^2.

Benefit from the Company's relationship with Hainan Airlines. Hainan Airlines, one of the Promoters of the Company, has its home base in the Meilan Airport. It is the fourth largest airline group in China in terms of total traffic tonne kilometers assuming completion of the airlines consolidation announced by CAAC in October 2002. Benefiting from this special relationship, the two companies can create synergies through resources sharing in the operations of the Meilan Airport and concerted marketing efforts in promoting Hainan Province as a popular tourist destination.

Obtain international airport status. The Group is seeking to obtain international airport status for the Meilan Airport from CAAC. To obtain such status, the Group must fulfil certain requirements relating to infrastructure and custom and inspection capacities. The Directors believe that, once the international airport status is obtained, international flights at the Meilan Airport and related revenues of the Group will increase, as the status of international airport will simplify the approval and operational process for airlines to set up international routes to and from the Meilan Airport. In anticipation of obtaining such status, a custom and inspection joint operation building located adjacent to the Terminal is under construction and expected to be completed by the end of 2002. The Directors believe that international airport status will, subject to further inspection before approval, be approved before the end of 2002.

The Group's Strengths

The Directors believe that the Group's operations benefit from the following factors:

Rapid growth of China's economy and air traffic. The demand for airport services is driven primarily by the volume of air traffic. Air traffic volume has been growing rapidly in China due to its strong economic and real income growth, increased mobility and rising popularity of tourism in the past 20 years. The Directors expect that more disposable income of the domestic population will be spent on travelling.

Strong growth of the tourism industry in Hainan. Hainan is the only tropical province in China. The well-known beaches and other tourist attractions have made Hainan Island one of the top tourist destinations in China attracting both domestic and international visitors. Currently the majority of visitors to Hainan are from domestic locations in China. In 2001, there were 11.3 million person-visits to Hainan Island, 10.8 million of which were generated by domestic travellers. Revenue from domestic tourism in 2001 amounted to RMB7,910 million, a 13.8% increase compared to that of 2000, while revenue from foreign tourism amounted to US$106 million, a decrease of 2.6% over the previous year. The top five sources of regional and international visitors are Hong Kong,Taiwan, Macau, Korea and Japan. Due to the relative ease of travel to Hainan for PRC residents, compared to foreign destinations where visa and other requirements pertain, Booz Allen Hamilton recently forecasted a substantial increase in domestic air passenger arrivals in Hainan in the near future. See Appendix V to this prospectus.

Aviation — a sensible transport solution for Hainan Island. Hainan Island is the largest tropical island of China with a population of approximately 7.7 million and a GDP of approximately RMB56.7 billion in 2001. Demands for air travel are increasing along with Hainan's popularity as a resort destination. Currently, the only other mode of transportation linking Hainan Island with the mainland is sea transportation. Aviation is a sensible transport solution for connecting the island with the rest of China.

Haikou — the main gateway to Hainan. As the capital city, Haikou is the centre of economic, cultural and political activities of Hainan Province. The Meilan Airport, situated approximately 25 kilometres from the city centre of Haikou, is well positioned to capture the economic benefits of Haikou's status. It is a gateway airport for people travelling to and from Hainan Province.

Market oriented management team. The management team has been involved in the management of Parent Company and the Group since the inception of the Meilan Airport. The Group has adopted a flexible management structure focusing on performance rather than seniority. The management comprises a number of young professionals who are familiar with modern corporate management style. This is complemented by the senior management team of the Group which has considerable experience in the civil aviation industry in China, including China's leading airlines, airports and the aviation regulators.

In 2001, out of all the airports in China, the Meilan Airport, along with Nanjing Lukou International Airport, Xiamen International Airport, Wuhan Tianhe Airport and Zhenzhou Xinchen International Airport, won the national-level "Consumer Satisfaction Award" organised by CAAC.

Good location, well-maintained runway and advanced facilities. The terrain where the Meilan Airport is located is flat and wide, making it a suitable site for an airport. There is adequate land supply for future expansion. The runway of the Meilan Airport was designed according to ICAO category 4E standards. It is 3,600-metre long, 44% longer than the ICAO specification of 2,500 metres as the required length for accommodating the maximum gross weight takeoff requirements of Boeing 747-400 aircraft. The runway's precision instrument markings, lighting and taxiways are all constructed according to ICAO category 4E standards. The category II precision instrument landing system at the west approach (the primary approach used by the majority of flights) provides for aircraft operations with 30-metre decision height and visibility distance of 400-metre while the category I precision instrument landing system at the east approach provides for 60-metre decision height and 800-metre visibility distance.

The Meilan Airport is also equipped with a flight information system and an automatic baggage handling system. An evaluation of these facilities is contained in the engineering consultants' report, a summary of which is set out in Appendix VI to this prospectus. Apart from these facilities, the Meilan Airport also has radar systems for air traffic control and weather monitoring, an aircraft repair and maintenance hangar and aviation fuel supply facilities.

Limited direct competition. The Meilan Airport is the primary airport serving Hainan Island. As such, the Group's core operations, namely the provision of airport services, face limited direct competition. The only other civil airport on Hainan is the Sanya Airport, which had a passenger throughput of nearly 1 million in 2001, representing approximately 20% of that of the Meilan Airport in the same period. The Company entered into the Sanya Management Contract on 23rd August, 2002 with SPIA under which the Company manages the Sanya Airport and receives management fees set at 1.5% of the annual operating revenue of the Sanya Airport and other compensations based on the improvement to the profitability of the Sanya Airport. Most of the Group's non-aeronautical operations, such as operating the duty-free shop and the car park, advertising and commercial leasing, do not face any direct competition.

Stable customer base. The revenues of the Group depend on the air traffic to and from Haikou, Hainan. Various airlines have established flights to and from Haikou. The Directors do not believe that the Group's prospects depend on the presence of any particular airline customer other than the Hainan Airlines and China Southern Airlines. With the projected growth in air traffic in and out of Hainan Province, the existing airline customers, including Hainan Airlines, China Southern Airlines and other major airlines in China, are expected to continue their presence at the Meilan Airport.

Good safety record. The Meilan Airport has not had any accidents involving aircraft, nor any accident resulting in loss of life or any significant personal injury or property damage since its inception. The Directors believe that the emphasis by CAAC, SCATC and the Group on proper safety training and the staff's continued efforts in focusing on safety matters have contributed to the Meilan Airport's safety record.

High growth potential in international flights. Based on the traffic forecast by Booz Allen Hamilton (see Appendix V to this prospectus), international aircraft movement at the Meilan Airport will have on average a compound annual growth rate of 20.6% for the next 10 years. The Directors believe that the Meilan Airport will be better positioned to respond to the increasing demand when the current expansion plan of the Terminal is implemented and the new cargo centre is built.

RISK FACTORS

The Directors consider that there are certain risks involved in the operation of the Group. They can be categorised into (i) risk factors relating to the Group; (ii) risk factors relating to the PRC; and (iii) risk factors relating to the Offering. These risk factors are set out in the section headed "Risk Factors" in this prospectus as follows:

Risk relating to the Group

- The Group has a limited operating history on which prospective investors may base an investment decision
- Results of operations is dependent on factors beyond the Group's control
- Dependence on Hainan as a tourist destination
- Competition with other modes of transport to and from Hainan
- Competition with other airports
- Dependence on domestic and regional economic growth
- Customer concentration
- Operation and business interruption
- Reliance on and integration with other authorities and service providers
- Control of the Runway
- Revenue sharing with Parent Company

- Material changes to the Agreement on Runway
- Technical Services Agreement
- Natural disasters
- Construction risk
- Implementation of the Group's business strategy
- Potential conflicts of interests
- Regulation by CAAC
- Impact of consolidation and reorganisation in the PRC aviation industry
- 11th September 2001 terrorist attacks on the US
- Environmental protection
- Forecasts prepared by Booz Allen Hamilton and Parsons Brinckerhoff (Asia) Limited
- Future operating results may vary significantly from profit forecast
- Loss of tax preferences could affect net profit attributable to shareholders
- Dividends

Risk relating to the PRC

- Political and economic factors
- Foreign exchange considerations
- Legal and other regulatory considerations

Risk relating to the Offering

- Marketability and possible price volatility of shares
- Forward-looking statements
- Certain statistics from third party publications

THE OFFERING

The Offering will be fully underwritten and comprises (i) the Public Offer (initially representing approximately 10% of the total number of H Shares initially being offered under the Offering), and (ii) the International Placing (initially representing approximately 90% of the total number of H Shares initially being offered under the Offering). H Shares under the Public Offer and the International Placing will be issued at the Offer Price (excluding the brokerage, the Stock Exchange trading fee and the SFC transaction levy). The Offer Price is expected to be fixed by agreement between HSBC and Oriental Patron on behalf of the Underwriters and the Company at or before 5:00 p.m. (Hong Kong time) on the Price Determination Date. If, for any reason, the Offer Price is not agreed between the Company and HSBC and Oriental Patron on behalf of the Underwriters at or before 5:00 p.m. (Hong Kong time) on 14th November, 2002, the Offering will not proceed. Investors may apply for H Shares under the Public Offer or indicate an interest for H Shares under the International Placing, but may not do both.

The Public Offer is a fully underwritten public offer (subject to agreement as to pricing and the conditions described in the section headed "Structure of the Offering — Conditions of the Offering" of this prospectus) for the subscription and purchase in Hong Kong of, initially, 20,170,000 H Shares divided equally into two pools, pool A and pool B. H Shares in pool A are for allocation to applicants who have applied for H Shares with an aggregate price (excluding the brokerage, the Stock Exchange trading fee and the SFC transaction levy payable) of HK$5 million or less and H Shares in pool B are for allocation to applicants who have applied for H Shares with an aggregate price (excluding the brokerage, the Stock Exchange trading fee and the SFC transaction levy payable) of more than HK$5 million. Applicants can only receive an allocation of H Shares from either pool A or pool B but not from both pools.

The allocation of H Shares between the Public Offer and the International Placing (excluding the Strategic Placing) is subject to adjustment. If the number of H Shares validly applied for under the Public Offer is or exceeds (i) 15 times but less than 50 times, (ii) 50 times but less than 100 times, or (iii) 100 times or more of the number of H Shares initially available under the Public Offer, then H Shares will be reallocated to the Public Offer from the International Placing (excluding the Strategic Placing), so that the total number of H Shares available under the Public Offer will be 60,510,000 H Shares (in the case of (i)), 80,680,000 H Shares (in the case of (ii)) and 100,850,000 H Shares (in the case of (iii)), representing approximately 30%, 40% and 50% respectively of the Offer Shares initially available under the Offering, respectively. In such circumstances, the additional H Shares reallocated to the Public Offer will be allocated equally between pool A and pool B and the allocations to placees under the International Placing (excluding the Strategic Placing) will be reduced accordingly. In addition, under the International Placing Agreement, the Company intends to grant to the International Placing Underwriters the Over-allotment Option, to require the Company to allot and issue up to an aggregate 25,213,000 additional H Shares at the Offer Price solely to cover over-allocations (if any) in the International Placing, within 30 days after the date of this prospectus. Further details of the structure of the Offering are set out in the section headed "Structure of the Offering" in this prospectus.

The allocation of H Shares between the Public Offer and the International Placing (excluding the Strategic Placing) as described above will not affect the Strategic Investor's aggregate shareholding in the Company immediately following completion of the Offering.

The Strategic Placing

As part of the International Placing, the Company is offering the Strategic Placing Shares through the Strategic Placing Underwriter to the Strategic Investor pursuant to the Strategic Investment Agreement. The Strategic Placing will be underwritten by the Strategic Placing Underwriter only.

Under the Strategic Investment Agreement, the Strategic Investor will subscribe for the Strategic Placing Shares through the Strategic Placing Underwriter at a price equivalent to the Offer Price plus brokerage, SFC transaction levy and Stock Exchange trading fee, otherwise subject to and (except as set forth in this prospectus) on the same terms and conditions as are generally applicable to the International Placing. The Strategic Investor will hold approximately 20% of the enlarged issued share capital of the Company immediately after the completion of the Offering (including any exercise of the Over-allotment Option).

The Strategic Investor has undertaken to the Company, Parent Company and HNA Group that it will not dispose of any of the Strategic Placing Shares for a period of 12 months following the commencement of dealings in the H Shares on the Stock Exchange. It has also undertaken to the Company, Parent Company and HNA Group that: (a) it will not dispose of any of the Strategic Placing Shares for a period of six months following the expiry of the 12-month period after the commencement of dealings in the H Shares on the Stock Exchange without the prior written consent of the Company; (b) in the event of any disposal of any interest in the Strategic Placing Shares: (i) it will take all reasonable steps to ensure that such disposal shall be in accordance with the terms of the Strategic Investment Agreement and will not create a disorderly or false market for any class of shares of the Company; and (ii) it shall not, for so long as Parent Company shall remain as the single largest shareholder of the Company, knowingly dispose of or otherwise transfer any of such interest to any party which carries on or is engaged in carrying on airport services or any party which holds an equity interest in any airports (except where the disposal is made to professional investment funds or financial institutions whose ordinary course of business is investment in securities).

The Strategic Investor has also undertaken not to purchase or subscribe for any additional H Shares so as to increase its shareholding in the Company to more than 25% of the issued share capital of the Company without the prior written consent of the Company.

The Strategic Placing is subject to a number of conditions including:

(a) those conditions set out in the section headed "Structure of the offering — Conditions of the Offering" of this prospectus;

(b) the Strategic Investor having completed its due diligence review on the business, financial position and prospects of the Group to its satisfaction; and

(c) the total subscription price for the Strategic Placing Shares payable by the Strategic Investor not exceeding DKK500 million (equivalent to approximately RMB550 million).

HISTORICAL TRADING RECORD

The table below sets out a summary of the consolidated results of the Group for each of the three years ended 31st December, 2001 and the five months ended 31st May, 2002, based on the information included in the Accountants' Report as set out in Appendix I to this prospectus, which presents the results of the Group as if the Group had been in existence throughout the Track Record Period. The construction of the Meilan Airport was completed and the assets of Meilan Airport were ready for operation on 28th March, 1999. Prior to that time, costs and expenses of construction were capitalised. Commencing from the beginning of trial operations on 29th March, 1999, cost and expense items were recorded in the income statement; and commencing from the beginning of commercial operations on 25th May, 1999, all items of revenue, cost and expense were recorded in the income statement. The consolidated financial information has been prepared and presented in accordance with International Accounting Standards.

	Year ended 31st December,			Five months ended 31st May,
	1999[(1)]	**2000**	**2001**	**2002**
		(RMB'000)		
Revenues				
Aeronautical[(2)]				
Passenger charges	41,766	90,371	102,283	50,584
Airport fee	—	—	—	29,442
Ground handling services fee	10,091	18,371	20,556	10,644
Aircraft movement fees and related charges	5,642	10,661	10,198	5,138
Total aeronautical revenues	57,499	119,403	133,037	95,808
Non-aeronautical				
Leasing of commercial areas, counters and office in the Terminal	10,424	22,921	26,261	10,899
Franchise fee[(3)]	6,592	11,809	15,490	6,597
Advertising	3,530	5,087	4,018	2,021
Other revenues	2,437	2,423	6,195	3,162
Total non-aeronautical revenues	22,983	42,240	51,964	22,679
Total revenues	80,482	161,643	185,001	118,487

	Year ended 31st December,			Five months ended 31st May,
	1999[1]	2000	2001	2002
	(RMB'000)			
Business taxes and levies	(2,931)	(5,952)	(6,819)	(4,364)
Net revenues	77,551	155,691	178,182	114,123
Operating costs				
Cost of goods and services	(6,568)	(13,384)	(13,395)	(4,751)
Depreciation and amortisation	(21,282)	(28,143)	(28,404)	(12,005)
Staff costs	(5,793)	(9,008)	(8,111)	(3,442)
Utilities and power	(4,804)	(7,183)	(7,225)	(2,688)
Repairs and maintenance	(459)	(994)	(2,006)	(355)
Other costs	(359)	(663)	(1,085)	(913)
Total operating costs	(39,265)	(59,375)	(60,226)	(24,154)
Gross profit	38,286	96,316	117,956	89,969
Administrative expenses	(8,388)	(15,157)	(12,892)	(7,451)
Profit from operating activities	29,898	81,159	105,064	82,518
Other income	—	—	—	2,528
Finance expenses, net	(22,067)	(22,966)	(17,659)	(7,666)
Profit before tax	7,831	58,193	87,405	77,380
Tax[4]	—	—	—	—
Profit after tax	7,831	58,193	87,405	77,380
Minority interests	(94)	(4)	6	(9)
Net profit attributable to shareholders	7,737	58,189	87,411	77,371
Distribution to Parent Company[5]	—	29,081	—	—
Final dividends[6]	—	—	45,000	—
EPS[7]	0.03	0.23	0.35	0.31
EBITDA[8]	51,180	109,302	133,468	97,051

(1) Construction commenced in November 1996 and commercial operations of the Meilan Airport commenced on 25th May, 1999. Accordingly, the relevant data for 1999 reflects only seven months of commercial operations and therefore is not directly comparable with those of the subsequent years.

(2) The presentation of the historical figures throughout the Track Record Period for the following aeronautical revenues reflect the revenue sharing arrangement between the Company and Parent Company on the basis of 75% to the Company and 25% to Parent Company:

- Aircraft movement fees;
- Passenger charges; and
- Basic ground handling services fees charged to Hong Kong, Macau and foreign airlines.

(3) The franchise fees for the Track Record Period consist of the following items:

- Annual fees from Hainan Food with respect to the air catering rights at the Meilan Airport;
- Annual fees from Hainan Airlines in 1999 and 2000 and from Parent Company in 2001 and the first five months of 2002 with respect to the right to operate the cargo centre at the Meilan Airport;
- Annual fees from THIA with respect to the right to sell accident insurance policies at the Meilan Airport; and
- Fees from HLAS with respect to air ticketing operation at the Meilan Airport.

(4) The Company is entitled to an exemption from corporate income tax from 2000 to 2004, and a reduced income tax rate of 7.5% from 2005 to 2009. Please refer to subsection "Financial Information — Taxation" for details.

(5) Pursuant to a resolution of shareholders dated 29th June, 2001, the Company made a distribution to Parent Company which represented the profit after tax of the Company for the period from 1st August, 2000 to 31st December, 2000. Such profit after tax was determined in accordance with relevant PRC accounting regulations.

(6) On 19th July, 2002, the shareholders of the Company approved the distribution of a final dividend of RMB45 million for the year ended 31st December, 2001 to the then existing shareholders.

(7) The calculation of earnings per share is based on the Group's profit attributable to shareholders for each of the three years ended 31st December, 2001 and for the five months ended 31st May, 2002 and on the 250 million shares deemed to have been in issue and issuable during the Track Record Period.

(8) EBITDA (earnings before interest, tax, depreciation and amortisation) should not be construed as an alternative to operating income or any other measure of performance or as an indicator of the Group's operating performance, liquidity or cash flows generated by operating, investing and financing activities. The items of net income excluded EBITDA are significant components in understanding and assessing the Group's financial performance, and the Group's computation of EBITDA may not be comparable in other similarly titled measures of other companies. The Group has included the information concerning EBITDA because the Directors believe that it is an useful supplement to cash flow data as a measure of the Group's performance.

The Directors have confirmed that they have performed sufficient due diligence on the Group to ensure that, save as disclosed herein, up to the date of this prospectus, there has been no material adverse change in the financial position or prospect of the Group since 31st May, 2002 and there is no event which would materially affect the information shown in the Accountants' Report of the Group as set out in Appendix I. The following data should be read in conjunction with the financial statements, including the notes thereto, contained elsewhere in this prospectus. Results for the five months ended 31st May, 2002 are not necessarily indicative of the Group's results for the full year.

SELECTED OPERATING DATA

The table below sets out certain operating data relating to the Group's business for the three years ended 31st December, 2001, the five months ended 31st May, 2001 and 2002 and the nine months ended 30th September, 2001 and 2002, respectively.

	Year ended 31st December,			Five months ended 31st May,		Nine months ended 30th September,	
	1999(1)	2000	2001	2001	2002	2001	2002
Passenger throughput (in thousands)							
Domestic flights	2,068.0	4,178.8	4,900.0	2,170.0	2,497.6	3,709.3	4,097.3
International flights	3.8	11.8	13.0	7.3	7.5	10.1	10.6
Hong Kong/Macau flights	130.0	172.6	166.1	67.3	58.1	125.9	106.2
Total	2,201.8	4,363.2	5,079.1	2,244.6	2,563.2	3,845.3	4,214.1
Aircraft movements							
Domestic flights	29,524	54,927	52,091	23,758	26,504	39,662	43,931
International flights	58	169	173	93	89	133	140
Hong Kong/Macau flights	1,152	1,669	1,522	657	607	1,150	1,103
Total	30,734	56,765	53,786	24,508	27,200	40,945	45,174

(1) Commercial operations of the Meilan Airport commenced on 25th May, 1999. Accordingly, the relevant data for 1999 reflects only seven months of commercial operations and therefore are not directly comparable with those of the subsequent years.

DIVIDEND POLICY

On 19th July, 2002, the shareholders of the Company approved the distribution of a final dividend of RMB45 million for the year ended 31st December, 2001 to the then existing shareholders. The dividend was financed by internal sources.

The Articles of Association permit the Company to distribute dividends or make other distributions according to an ordinary resolution of the shareholders, and prevent the Company from distributing dividends or bonuses without first making up for losses and making all tax and other payments required by law. Under the Articles of Association, the Company may, in addition to final dividend, distribute interim or special dividends in the form of cash or shares. In accordance with the Articles of Association, the distributable profits available to the Company for the purpose of profit distribution will be deemed to be the lesser of:

1. the net income determined in accordance with PRC accounting standards and regulations; and

2. the net income determined in accordance with IAS.

However, prior to payment of dividends, profits of the Company are subject to deductions such as allocations to the statutory common reserve and the statutory public welfare fund. The Company's outstanding credit facilities do not impose any restrictions on its ability to pay dividends. See the section headed "Financial Information — Liquidity and Capital Resources — Capital Resources".

Subject to the foregoing, the Company intends to make interim dividend payments in or around October of each year and final dividend payments in or around June of each year. It is the present intention of the Directors that, for each year, the interim dividend will represent approximately 25% of the total estimated dividends to be paid for the entire year (except for the financial year of 2002 for which no interim dividend will be declared) and that the sum of interim and final dividend will represent approximately 60% (for each of the financial years of 2002 and 2003) or 50% (for each subsequent financial year) of the Company's net profit attributable to shareholders before deduction of statutory reserves for the relevant financial year determined in accordance with IAS, and limited to the distributable profits available. The distribution of dividend payment will be dependent upon the Company's earnings, financial conditions, cash requirements and availability, the provisions of the PRC Company Law and other factors. There is no assurance as to whether the dividend distribution will occur as intended, the amount of dividend payment or the timing of such payment.

The Articles of Association require that cash dividends of H Shares will be declared in Renminbi and paid in Hong Kong dollars to H Shareholders. Conversion of Renminbi into Hong Kong dollars will be subject to the relevant PRC foreign exchange regulations and will be calculated at an exchange rate which will be the average of the PBOC Exchange Rate one calendar week preceding the date of declaration of dividends. If the Company does not have sufficient foreign exchange reserves to pay its Hong Kong dollars dividends, it intends to exchange its RMB funds into the required Hong Kong dollars from authorised banks or through other approved means. There is no assurance that the Company will be able to obtain Hong Kong dollar funds as needed.

FUTURE PLANS AND PROSPECTS

The Group's strategy is to maintain and capitalise on the position of Meilan Airport as the main gateway to Hainan and to seek sustainable long-term growth in its aeronautical and non-aeronautical related businesses.

For aeronautical businesses, the Group plans to expand and improve the existing facilities at the Meilan Airport, including the Terminal and apron, and to build new facilities, including a new cargo centre and cargo aircraft parking apron, a new customs and inspection joint operation building, in anticipation of future air traffic increase and the attainment of international airport status.

The Group will seek to increase its non-aeronautical business, which contributed approximately 28.6%, 26.1%, 28.1% and 19.1% of the total revenue in each of the three years ended 31st December, 2001 and the first five months of 2002. The Group will explore opportunities to further increase the advertising spaces and commercial areas for leasing at the Meilan Airport. Further, the Group will seek to increase the utilisation rate of the available advertising spaces and of commercial area in conjunction with the expected growth of passenger traffic.

In addition, the Group is committed to improving quality of service by developing more training programmes for its management and staff. The Group also plans to strengthen communications and cooperation with other governmental and business entities that operate at the Meilan Airport.

The Directors believe that the Group can capitalise on its experience in managing airport business. The Company signed a contract with SPIA on 23rd August, 2002 to manage the Sanya Airport. The Group intends to establish its reputation as a premier airport operator in the PRC.

Parent Company has granted the Company an option to acquire from Parent Company aeronautical or non-aeronautical businesses and assets owned by it from time to time. The Group plans to take advantage of such opportunities to achieve revenue and earnings growth, as well as economies in planning, procurement and services. The Group intends to fund the cost of possible acquisitions and capital expenditures with its internal resources, loan financing and possible future issues of shares.

Based on the report prepared by Booz Allen Hamilton, the air traffic by passenger throughput at the Meilan Airport is expected to increase by approximately 10.2% and 9.2% annually from 2001 to 2006 and from 2001 to 2011, respectively. See Appendix V to this prospectus. With the expansion and improvement of the Terminal and aprons, the Group expects to be able to capture the business opportunities associated with the expected air traffic increase.

REASONS FOR THE OFFERING AND THE USE OF PROCEEDS

The Directors intend to use the net proceeds of the Offering of the New H Shares to finance the Group's capital expenditure, strengthen its capital base and improve its financial position.

The net proceeds of the Offering of the New H Shares (after deduction of underwriting fees and estimated expenses payable by the Group in relation to the Offering, assuming the Over-allotment Option is not exercised and assuming an Offer Price of HK$3.47 per H Share, being the mid-point of the Offer Price range of HK$3.15 to HK$3.79 per H Share) are estimated to be approximately HK$642.0 million (HK$727.4 million, if the Over-allotment Option is fully exercised). The Group currently intends to use the net proceeds from the Offering in the following approximate proportion:

- approximately RMB392.0 million (HK$369.4 million) for the airport expansion project. The project includes construction of approximately 30,000 m^2 of expanded Terminal area, an aircraft parking apron of approximately 280,000 m^2, 20 aircraft parking positions and eight aircraft parking positions with air bridges;

- approximately RMB198.0 million (HK$186.6 million) for the construction of a new cargo centre with a floor area of approximately 30,000 m^2 and aprons with an area of approximately 50,000 m^2 with four aircraft parking positions;

- approximately RMB70.0 million (HK$66.0 million) for the renovation of the Terminal and construction of a customs and inspection joint operation building for international passengers and cargoes; and

- the balance of RMB21.2 million (HK$20 million) is expected to be used as general working capital of the Group and for other general corporate purposes. It may be used to acquire or invest in complementary businesses or to establish joint ventures that the Group believes will complement its current or future business. However, the Group has no specific agreements or commitments at this stage relating to any material acquisition.

Pending the use of the net proceeds of the Offering of the New H Shares for the purposes described above, the Group intends to place the net proceeds, to the extent permitted by relevant PRC laws and regulations, in short-term bank deposits or in money market instruments in accounts maintained with banks in the PRC. Upon approval by SAFE, the Group will be entitled to retain the net proceeds of the Offering of the New H Shares in Hong Kong dollars and convert them into United States dollars or other foreign currencies. The Group will be entitled to use such proceeds for any legitimate purpose, such as purchase of equipment from overseas (if required) in accordance with the exchange control regulations.

In the event that any part of the business plan of the Group does not materialise or proceed as planned, the Directors will carefully evaluate the situation and may reallocate the intended funding to other business plans and/or new projects and/or hold such funds in short-term deposit for so long as the Directors deem to be in the best interests of the Company and its shareholders taken as a whole.

In the event that there is any material modification to the use of proceeds as described above, the Company will issue an announcement of the change.

FORECASTS FOR THE YEAR ENDING 31ST DECEMBER, 2002

Forecast consolidated profit after tax and minority interests but before extraordinary items(1) . . . . not less than RMB156 million (HK$147 million)

Forecast earnings per Share

— pro forma fully diluted(2) . . . . RMB0.36 (HK$0.34)

— weighted average(3) . . . . RMB0.57 (HK$0.54)

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(1) The bases on which the above profit forecast has been prepared are set out in Appendix III to this prospectus.

(2) The calculation of the forecast earnings per Share on a fully diluted basis is based on the forecast consolidated profit after tax and minority interest but before extraordinary items for the year ending 31st December, 2002, assuming that the Company had been listed on the Stock Exchange since 1st January, 2002 and a total of 448,000,000 Shares were in issue during the entire year. The estimated earnings per Share has been adjusted to take into account the interest income that would have been earned if the estimated net proceeds from the Offering were received on 1st January, 2002 on the basis of an interest rate of 0.98% per annum. It should be noted, however, that the net proceeds of the Offering will not in fact be invested to earn interest income, except as described in the section headed "Future Plans and Use of Proceeds", please refer to the descriptions therein for the details on how the proceeds are intended to be used. These calculations assume that the Over-allotment Option will not be exercised, and the H Shares issued pursuant to the Offering were issued on 1st January, 2002 at an Offer Price of HK$3.47 per H Share (being the mid-point of the proposed Offer Price range of HK$3.15 to HK$3.79 per H Share) (excluding brokerage, the Stock Exchange trading fee and the SFC transaction levy, which are payable by applicants in the Offering).

(3) The calculation of the forecast earnings per Share on a weighted average basis is based on the forecast consolidated profit after tax and minority interest but before extraordinary items and a weighted average number of 273,868,493 Shares assumed to be in issue during the year. The calculation assumes that the Over-allotment Option will not be exercised and the H Shares will be issued on 18th November, 2002.

ISSUE STATISTICS

Except where otherwise indicated, the issue statistics have been prepared on the assumption that the Over-allotment Option will not be exercised. Issue statistics shown in Hong Kong dollars and the prospective earnings of the Company projected in the prospective price/earnings multiple have been translated from Renminbi into Hong Kong dollars at the rate of HK$1.00 = RMB1.0611 being the PBOC Rate prevailing on 31st May, 2002. The per share Offer Price of HK$3.15 and of HK$3.79 for H Shares issued in the Offering does not include brokerage, Stock Exchange trading fee and the SFC transaction levy, which are payable by applicants in the Offering.

	Based on an Offer Price of HK$3.15 per H Share	**Based on an Offer Price of HK$3.79 per H Share**
Market capitalisation of H Shares	HK$635.4 million	HK$764.4 million
Price/earnings multiple based on 2002 profit forecast		
— pro forma fully diluted[(1)]	9.17 times	11.03 times
— weighted average[(2)]	5.83 times	7.02 times
Adjusted net tangible asset value per Share[(3)]	RMB2.67 (HK$2.52)	

(1) The price/earnings multiple based on 2002 profit forecast on a pro forma fully diluted basis is based on the assumed Offer Price and the forecast earnings per Share on a pro forma fully diluted basis for the year ending 31st December, 2002 calculated based on the "Bases of Preparation" set out in Appendix III to this prospectus. The calculation of the earnings per Share on a pro forma fully diluted basis is based on the forecast consolidated profit after tax and minority interests but before extraordinary items for the year ending 31st December, 2002 and assuming that the Company had been listed on the Stock Exchange since 1st January, 2002 and that a total of 448,000,000 Shares were in issue during the entire year. These calculations assume that the Over-allotment Option was not exercised.

(2) The calculation of the prospective price/earnings multiple on a weighted average basis is based on the forecast earnings per Share on a weighted average basis at the respective Offer Price of HK$3.15 and HK$3.79 per Share assuming that the Over-allotment Option is not exercised.

(3) The adjusted net tangible asset value per Share has been arrived at after the adjustments referred to in "Financial Information — Adjusted Net Tangible Assets" in this prospectus and assumes that the Over-allotment Option will not be exercised, and the H Shares issued pursuant to the Offering were issued on 1st January, 2002 at an Offer Price of HK$3.47 per H Share (being the mid-point of the proposed Offer Price range of HK$3.15 to HK$3.79 per H Share) (excluding brokerage, the Stock Exchange trading fee and the SFC transaction levy, which are payable by applicants in the Offering).

If the Over-allotment Option is exercised in full, the adjusted net tangible assets of the Company will be increased to approximately RMB1,287.8 million based on the assumed Offer Price of HK$3.47 per H Share (being the mid-point of the proposed Offer Price range of HK$3.15 to HK$3.79 per H Share) and the adjusted net tangible asset value per Share will be RMB2.72. The estimated earnings per Share on a fully diluted basis for the year ending 31st December, 2002 will be reduced to RMB0.35 per Share.

In this prospectus, unless the context otherwise requires, the following expressions have the meanings set out below. Certain other terms are explained in the section headed "Glossary".

"Affiliates"	any subsidiary or holding company of a party, any subsidiary of any such holding company, and any company in which a party or any such holding company or subsidiary directly or indirectly has 30% or more equity interest, where holding company and subsidiary shall have the meanings as set out in the Companies Ordinance
"Agreement on Runway"	the agreement on runway entered into between the Company and Parent Company on 25th October, 2002 in relation to, amongst others, the operation and maintenance of the Runway
"Air China"	中國國際航空公司 (Air China), a PRC enterprise wholly-owned by the PRC Government
"Airport Fee"	civil airport management and construction fee payable to a civil airport by passengers departing from such airport in China
"Articles of Association" or "Articles"	the articles of association of the Company, adopted on 4th September, 2002 by the shareholders in general meeting and approved on 18th September, 2002 by SETC
"Asset Swap Agreement"	an asset swap agreement dated 30th May, 2002 and entered into between the Company and Parent Company, and supplemented by a supplemental agreement dated 25th October, 2002 entered into between the same parties in relation to swap of certain assets
"Aviation Oil"	中國航空油料總公司 (China Aviation Oil Company), a company established in the PRC
"Board"	the board of Directors
"Booz Allen Hamilton"	Booz Allen Hamilton (Australia) Limited, the independent air traffic consultants appointed by the Company to prepare the air traffic consultants' report, a summary of which is set out in Appendix V
"business day"	any day (other than a Saturday) on which banks in Hong Kong are generally open for business
"CAAC"	中國民用航空總局 (General Administration of Civil Aviation of China), also known as Civil Aviation Administration of China
"CADI"	Copenhagen Airport Development International A/S, a wholly-owned subsidiary of the Strategic Investor
"CCASS"	the Central Clearing and Settlement System established and operated by HKSCC
"Central South Aviation Development"	中南民航經濟發展公司 (Central South Civil Aviation Economy Development Corporation), a company established in the PRC and one of the Promoters of the Company

"Central South Bureau"	民航中南管理局 (Central South Management Bureau of CAAC)
"CFETC"	中國外滙交易中心 (China Foreign Exchange Trading Centre)
"China Eastern Airlines"	中國東方航空股份有限公司 (China Eastern Airlines Company Limited), a joint stock limited company incorporated in the PRC and listed on the Stock Exchange, and its affiliates
"China Northern Airlines"	中國北方航空公司 (China Northern Airlines Company), a PRC enterprise wholly owned by the PRC Government
"China Northwest Airlines"	中國西北航空公司 (China Northwest Airlines Company), a PRC enterprise wholly owned by the PRC Government
"China Southern Airlines"	中國南方航空股份有限公司 (China Southern Airlines Company), a joint stock limited company incorporated in the PRC and listed on the Stock Exchange and one of the Promoters of the Company
"China Southwest Airlines"	中國西南航空公司 (China Southwest Airlines Company), a PRC enterprise wholly owned by the PRC Government
"China Xinhua Airlines"	中國新華航空有限責任公司 (China Xinhua Airlines Company Limited), a limited liability company incorporated in the PRC and owned as to 51% by Hainan Airlines, 9% by HNA Group and 40% by 神華集團有限公司 (Shenhua Group Company Limited)
"Companies Ordinance"	the Companies Ordinance (Chapter 32 of the Laws of Hong Kong, as amended)
"Company"	海南美蘭機場股份有限公司 (Hainan Meilan Airport Company Limited), a joint stock limited company incorporated in the PRC on 28th December, 2000
"Company Law"	中華人民共和國公司法 (the Company Law of the PRC), as enacted by the Standing Committee of the Eighth NPC on 29th December, 1993 and become effective on 1st July, 1994, as amended, supplemented or otherwise modified from time to time
"CSRC"	中國證券監督管理委員會 (China Securities Regulatory Commission), a regulatory body responsible for the supervision and regulation of the PRC national securities markets
"DFG"	海南海口美蘭機場免税品有限公司 (Haikou Meilan Airport Duty-Free Shop Company Limited), a limited liability company incorporated in the PRC and a 95%-owned subsidiary of the Company
"Director(s)"	the director(s) of the Company
"DKK"	Danske Kroner, the lawful currency of Denmark
"Domestic Shares"	domestic shares issued by the Company, the par value of which is denominated in Renminbi, and which are subscribed for in Renminbi

"EBITDA"	earnings before interest, tax, depreciation and amortisation
"Foreign Shares"	shares issued by the Company, the par value of which is denominated in Renminbi, and which are subscribed for in a currency other than Renminbi
"GDP"	gross domestic product
"Global Coordinator"	HSBC
"Golden City"	海南金城國有資產經營管理有限責任公司 (Hainan Golden City State-owned Assets Management Company Limited), a company established in the PRC
"Group"	the Company and its subsidiaries or, where the context so requires, in respect of the period prior to the Company becoming the holding company of its present subsidiaries, the present subsidiaries of the Company, or in respect of the period prior to the incorporation of the Company, the business of the Company and its subsidiaries conducted by Parent Company (as the case may be)
"H Shares"	overseas listed Foreign Shares of nominal value RMB1.00 each in the share capital of the Company, which are to be listed on the Stock Exchange and subscribed for in HK dollars
"HAC"	海南機場股份有限公司 (Hainan Airport Company Limited), a limited liability company established in the PRC
"Hainan Airlines"	海南航空股份有限公司 (Hainan Airlines Company Limited), a joint stock limited company incorporated in the PRC and one of the Promoters of the Company
"Hainan Asset Bureau"	海南省國有資產管理委員會 (Hainan State Asset Management Bureau)
"Hainan Food"	海南航空食品有限公司 (Hainan Airlines Food Company Limited), a company established in the PRC and 51% owned by Hainan Airlines
"Hainan Zhong Li Xin"	海南中力信資產評估有限公司 (Hainan Zhong Li Xin Asset Valuation Company Limited), an independent property valuer in the PRC
"HK$" or "HK dollars" and "cents"	Hong Kong dollars and cents respectively, the lawful currency of Hong Kong
"HKSCC"	Hong Kong Securities Clearing Company Limited
"HLAS"	海南蘭宇航空服務有限公司 (Hainan Lanyu Air Services Company), a company established in the PRC and 95% owned by Parent Company
"HNA Group"	海航集團有限公司 (HNA Group Company Limited), a company established in the PRC and one of the Promoters of the Company, which was previously named as 海航控股(集團)有限公司 (HNA Holdings (Group) Company Limited) or 海南海航控股有限公司 (Hainan HNA Holdings Company Limited)
"Hong Kong"	the Hong Kong Special Administrative Region of the PRC

"HSBC"	The Hongkong and Shanghai Banking Corporation Limited, an exempt dealer under the Securities Ordinance (Chapter 333 of the Laws of Hong Kong) and a licensed bank under the Banking Ordinance (Chapter 155 of the Laws of Hong Kong)
"IAS"	International Accounting Standards
"IATA"	International Air Transport Association, an international association of airlines
"ICAO"	International Civil Aviation Organisation
"ICCT"	Industrial and Commercial Consolidated Tax
"International Placing"	the conditional placing of the International Placing Shares by the International Placing Underwriters, including the Strategic Placing, as described in the section headed "Structure of the Offering" in this prospectus
"International Placing Agreement"	the international placing agreement expected to be dated on or about 12th November, 2002 relating to the International Placing and expected to be entered into between the Company, Parent Company and the International Placing Underwriters
"International Placing Shares"	the H Shares being offered by the Company under the International Placing
"International Placing Underwriters"	HSBC, Oriental Patron, CITIC Capital Markets Limited, ICEA Capital Limited, ING Bank N.V., Nomura International (Hong Kong) Limited
"Joint Sponsors"	HSBC and Oriental Patron
"Latest Practicable Date"	31st October, 2002
"Listing Rules"	the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited
"Mandatory Provisions"	到境外上市公司章程必備條款 (the Mandatory Provisions for Articles of Association of Companies to be Listed Overseas), for inclusion in the articles of association of companies incorporated in the PRC to be listed overseas, which were promulgated by the CSRC and the former State Restructuring Commission on 27th August, 1994, as amended and supplemented from time to time
"Meilan Advertising"	海南海口美蘭機場廣告有限公司 (Hainan Haikou Meilan Airport Advertising Company Limited), a 95%-owned subsidiary of the Company
"Meilan Airport"	the civil airport known as 海口美蘭機場 (Haikou Meilan Airport) located in Qiongshan City, Hainan Province, PRC
"Meilan International"	海口美蘭國際機場總公司 (Haikou Meilan International Airport Company Limited), a company established in the PRC and a wholly-owned subsidiary of HAC

"Meilan Travelling"	海南美蘭機場旅行社有限責任公司 (Hainan Meilan Airport Travelling Company Limited), a company established in the PRC and a 60%-owned subsidiary of the Company
"MOF"	中國財政部 (the Ministry of Finance of the PRC)
"MOFTEC"	中國對外貿易經濟合作部 (the Ministry of Foreign Trade and Economic Cooperation of the PRC)
"New H Shares"	the 198,000,000 new H Shares to be issued as part of the Offer Shares by the Company for subscription at the Offer Price under the Offering
"Noise Pollution Prevention Law"	The Law of the PRC on the Prevention and Treatment of Noise Pollution (中華人民共和國噪聲污染防治法) adopted at the 22nd Session of the Standing Committee of the Eighth National People's Congress on 29th October, 1996, as amended, supplemented or otherwise modified from time to time
"Notice Relating to Foreign Exchange Control Matters for Enterprises Listed Overseas"	關於境外上市企業外滙管理有關問題的通知 (the Notice Relating to Foreign Exchange Control Matters for Enterprises Listed Overseas), issued by the CSRC and MOFTEC in January 1994
"NPC" or "National People's Congress"	全國人民代表大會 (the National People's Congress)
"Offer Price"	the final offer price per H Share (exclusive of brokerage, SFC transaction levy and Stock Exchange trading fee) at not more than HK$3.79 and expected to be not less than HK$3.15, such price to be agreed upon by the Company on the one part and the Joint Sponsors (on behalf of the Underwriters) on the other part at or before 5:00 p.m. on the Price Determination Date
"Offer Shares"	the Public Offer Shares and the International Placing Shares, together, where relevant, with any additional New H Shares issued pursuant to the exercise of the Over-allotment Option; the Offer Shares comprise the New H Shares and the Sale H Shares
"Offering" or "Global Offering"	the Public Offer and the International Placing
"Oriental Patron"	Oriental Patron Asia Limited, an investment adviser and a dealer registered under the Securities Ordinance (Chapter 333 of the Laws of Hong Kong)
"Over-allotment Option"	the option which is intended to be granted by the Company to the International Placing Underwriters pursuant to the International Placing Agreement to require the Company to issue and allot up to an aggregate of 25,213,000 additional H Shares at the Offer Price solely to cover over-allocations in the International Placing, if any

"Parent Company"	海口美蘭機場有限責任公司 (Haikou Meilan Airport Company Limited), a company established in the PRC and the controlling shareholder of the Company
"Parent Group"	Parent Company and its subsidiaries, excluding the Group
"PBOC"	中國人民銀行 (the People's Bank of China), the central bank of the PRC
"PBOC Notice"	關於進一步改革外滙管理體制的公告 (the Notice of the People's Bank of China Concerning Further Reform of the Foreign Currency Control System) issued in December 1993
"PBOC Rate"	the exchange rate for foreign exchange transactions set daily by the People's Bank of China based on the previous day's PRC interbank foreign exchange rates
"PRC" or "China"	the People's Republic of China. Except where the context requires, references in this prospectus to the PRC or China do not include Hong Kong, the Macau Special Administrative Region of the PRC or Taiwan
"PRC GAAP"	Accounting Standards for Business Enterprises and Accounting Regulations for Enterprises in the PRC
"PRC Government"	the central government of the PRC including all governmental subdivisions (including provincial, municipal and other regional or local government entities) and instrumentalities thereof
"Price Determination Agreement"	the agreement to be entered into between the Company and the Joint Sponsors, on behalf of the Underwriters, on the Price Determination Date to record the final Offer Price
"Price Determination Date"	the date, expected to be on or around 12th November, 2002 but no later than 14th November, 2002 (Hong Kong time), on which the Offer Price is fixed for the purpose of the Offering
"Promoters"	the parties to a promoters agreement dated 20th December, 2000 in relation to the promotion and incorporation of the Company, namely, Parent Company, Hainan Airlines, HNA Group, China Southern Airlines and Central South Aviation Development
"Public Offer"	the offer for subscription or purchase, as the case may be, of the Public Offer Shares in Hong Kong for cash, on and subject to the terms and conditions stated in this prospectus and in the application forms relating thereto
"Public Offer Shares"	the H Shares being offered for subscription or purchase under the Public Offer
"Public Offer Underwriters"	HSBC, Oriental Patron, CITIC Capital Markets Limited, ICEA Capital Limited, ING Bank N.V., Nomura International (Hong Kong) Limited
"Public Offer Underwriting Agreement"	the underwriting agreement dated 5th November, 2002 relating to the Public Offer entered into among, inter alia, the Company, Parent Company and the Public Offer Underwriters

"Purchase Option Agreement"	the purchase option agreement dated 30th May, 2002 and amended on 25th October, 2002 between the Company and Parent Company in relation to options granted to the Company for purchase of assets from Parent Company
"Regulation S"	Regulation S under the US Securities Act
"Restructuring"	the incorporation of the Company on 28th December, 2000 as a joint stock limited company and the swap of certain assets and liabilities between Parent Company and the Company
"RMB" or "Renminbi"	Renminbi yuan, the lawful currency of the PRC
"Rule 144A"	Rule 144A under the US Securities Act
"SAFE"	中國國家外滙管理局 (the State Administration for Foreign Exchange of the PRC)
"Sale H Shares"	a total of 3,700,000 H Shares to be converted from an equal number of Domestic Shares of RMB1.00 each held by the Vendors, to be offered for sale by the Vendors as part of the Public Offer Shares at the Offer Price under the Public Offer
"Sanya Airport"	the civil airport known as 三亞鳳凰機場 (Sanya Phoenix Airport) located in Sanya City, Hainan Province, the PRC
"Sanya Management Contract"	the management contract entered into between the Company and SPIA on 23rd August, 2002
"SCATC"	中國民航中南管理局空中交通管理局 (South Central Air Traffic Control Bureau)
"SETC"	中國國家經濟貿易委員會 (the State Economic and Trade Commission of the PRC)
"SFC"	the Securities and Futures Commission
"Shan Xi Airlines"	山西航空有限責任公司 (Shan Xi Airlines Company Limited), a PRC limited liability company which is held as to 89% by Hainan Airlines
"Shareholders' Agreement"	the conditional shareholders' agreement entered into between the Strategic Investor, Parent Company and HNA Group on 16th September, 2002 in relation to the Company
"Shares"	Domestic Shares and H Shares
"Special Regulations"	國務院關於股份有限公司境外募集股份及上市的特別規定 (the PRC Special Regulations on the Overseas Offering and Listing of Shares by Joint Stock Limited Companies), issued by the State Council on 4th August, 1994, as amended, supplemented or otherwise modified from time to time
"SPIA"	三亞鳳凰國際機場有限責任公司 (Sanya Phoenix International Airport Company Limited)

"State"	the Central Government of the PRC
"State Council"	中國國務院 (the State Council of the PRC)
"State Development Planning Commission" or "SDPC"	中國國家發展計劃委員會 (the State Development Planning Commission of the PRC)
"State Plans"	plans devised or approved and implemented by various authorities of the State relating to the economic and social development of the PRC
"State Restructuring Commission"	中國國家經濟體制改革委員會 (the State Commission for Restructuring the Economic Systems of the PRC)
"Stock Exchange"	The Stock Exchange of Hong Kong Limited
"Strategic Investment Agreement"	the conditional agreement dated 16th September, 2002 and amended on 30th October, 2002 relating to the Strategic Placing entered into between the Company, the Strategic Investor and the Strategic Placing Underwriter
"Strategic Investor"	Copenhagen Airports A/S, a company duly incorporated under the laws of the Kingdom of Denmark and whose shares are listed on the Copenhagen Stock Exchange
"Strategic Placing"	the placing of the Strategic Placing Shares with the Strategic Investor as part of the International Placing
"Strategic Placing Shares"	such number of H Shares to be placed with the Strategic Investor as is equal to approximately 20% of the enlarged issued share capital of the Company immediately following completion of the Offering (including any exercise of the Over-allotment Option)
"Strategic Placing Underwriter"	HSBC
"Supervisors"	the members of the supervisory committee of the Company
"Technical Services Agreement"	the conditional technical services agreement entered into between CADI and the Company on 16th September, 2002 and amended on 30th October, 2002 in relation to the provision by CADI to the Company of certain technical and advisory services
"Terminal"	the terminal forming part of the Meilan Airport which commenced commercial operations on 25th May, 1999
"THIA"	海南通滙保險代理有限公司 (Hainan Tong Hui Insurance Agent Company Limited), a company established in the PRC
"Track Record Period"	the period comprising the three financial years ended 31st December, 2001 and the five months ended 31st May, 2002
"Underwriters"	the Public Offer Underwriters and the International Placing Underwriters

"Underwriting Agreements"	the Public Offer Underwriting Agreement and the International Placing Agreement
"US Exchange Act"	the United States Securities Exchange Act of 1934, as amended
"US GAAP"	generally accepted accounting principles in the United States
"US Securities Act"	the US Securities Act of 1933, as amended
"US$" or "U.S. dollars"	United States dollars, the lawful currency of the United States
"US" or "United States"	the United States of America
"Vendors"	China Southern Airlines and Central South Aviation Development
"WTO"	the World Trade Organisation
"Yangzi Express"	揚子江航空快運有限公司 (Yangzijiang Air Express Company Limited), a limited liability company established in the PRC which is held as to 85% by HNA Group, 10% by Shanghai Airport (Group) Company Limited and 5% by Hainan Airlines
"Yunnan Airlines"	雲南航空公司 (Yunnan Airlines Company), a PRC enterprise wholly owned by the PRC Government

"aircraft movements"	landings and take-offs of aircraft
"apron"	a defined area, on a land aerodrome, intended to accommodate aircraft for purposes of loading or unloadng passengers, mail or cargo, fuelling or parking
"available seat kilometres" or "ASKs"	the number of seats made available for sale multiplied by the kilometres flown
"available tonne kilometres" or "ATKs"	the number of tonnes of capacity available for the transportation of revenue load (passengers and cargo) multiplied by the kilometres flown
"CAGR"	compound annual growth rate
"cargo tonne kilometres" or "freight tonne kilometres" or "FTK"	the cargo load in tonnes multiplied by the kilometres flown
"Category I runway" or "Category II runway"	a runway intended for the operation of aircraft using instrument approach procedures served by instrument landing system and visual aids intended for operations (i) down to 60 metres and 30 metres, respectively, decision height and (ii) down to a runway visual range of the order of 800 metres and 400 metres, respectively
"CDDS"	Cargo Departure Documentation System
"DCS"	Departure Control System
"DDS"	Data Display System
"ETV"	elevating transfer vehicles
"hectare(s)"	representing 10,000 m^2
"m" & "m^2"	metres and square metres, respectively
"MTOW"	maximum take-off weight
"overall load factor"	RTKs expressed as a percentage of ATKs
"passenger load factor"	RPKs expressed as a percentage of ASKs
"passenger throughput"	total number of departing and arriving passengers
"payload" or "commercial weight"	total weight of passengers and cargo carried by an aircraft
"revenue passenger kilometres" or "RPKs"	the number of paying passengers carried multiplied by the kilometres flown
"revenue tonne kilometres" or "RTKs"	the load (passenger and cargo) in tonnes multiplied by the kilometres flown

"taxiway"	a defined path on a land aerodrome established for the taxiing of aircraft and intended to provide a link between one part of the aerodrome to another
"tonne"	a metric tonne, equivalent to 1,000 kilogrammes or 2,204.6 pounds

Investors should consider carefully all of the information set out in this prospectus and, in particular, should evaluate the following risks in connection with an investment in the Company, certain of which are not typically associated with investing in equity securities of companies from Hong Kong or other economically advanced jurisdictions. For more information concerning the PRC and certain related matters discussed below, see "Appendix IX — Summary of Principal Legal and Regulatory Provisions and Articles of Association" in this prospectus.

RISKS RELATING TO THE GROUP

The Group has a limited operating history on which prospective investors may base an investment decision

The construction of the Meilan Airport was commenced in November 1996 initially by Meilan International. Parent Company was established on 25th August, 1998 and took over the assets and operations of the Meilan Airport. Construction was completed at the end of March 1999, and the Meilan Airport formally commenced commercial operations on 25th May, 1999. On 28th December, 2000, the Company was incorporated by Parent Company and other Promoters. Certain assets of Parent Company including the Terminal were transferred to the Company as part of the Restructuring.

The results of operations presented in this prospectus reflect the management of the business by the Group's management team for the period from 1st January, 1999 through 31st May, 2002. Accordingly, the Group has a limited operating history under current management on which prospective investors can base an investment decision in relation to the H Shares.

Results of operations is dependent on factors beyond the Group's control

The principal factors affecting the Group's operating results and business prospects are:

- the number and types of aircraft using the Meilan Airport;
- the number of passengers arriving at and departing from the Meilan Airport;
- the respective numbers of flights operated by regional carriers on the one hand, and domestic carriers on the other hand, using the Meilan Airport; and
- the volume of air cargo shipped to and from the Meilan Airport.

These factors are influenced by a number of variables, many of which are beyond the Group's control. These variables include:

- levels of trade, tourism and business travel between the Haikou area and the rest of the PRC;
- levels of trade, tourism and business travel between the Haikou area and those countries and regions that have established international flight connections to Haikou;
- levels of economic activity and per capita income in the PRC;
- competition from alternative airports, tourist destinations and means of transportation;

- relative values of various relevant currencies;
- air ticket prices; and
- actual or perceived security threats to air travel.

Any significant reduction in the numbers of passenger arrivals and departures, aircraft movements or cargo throughput could have a material adverse effect on the Company's results of operations. Currently, the Group's insurance policies follows common practice in PRC which do not provide for compensation for loss of profits or consequential damages in the case of business interruption.

Dependence on Hainan as a tourist destination

Substantially all of the air traffic using the Meilan Airport is destination traffic, rather than transit traffic. According to a survey of departing passengers conducted by Booz Allen Hamilton in July 2002, approximately 69.6% of all departing non-Hainan Island resident passengers were tourists. Hainan competes with other Southeast Asian destinations such as Hong Kong, Macau, Thailand, Philippines and Singapore for tourist arrivals and departures. Any factors that could increase the attractiveness, convenience or affordability of these destinations relative to Hainan, or a change in PRC tourist arrival patterns, could have an adverse effect on the Company's results of operations.

Competition with other modes of transport to and from Hainan

The airport business is dependent on passenger and air cargo traffic of airlines, which compete with each other and with alternative modes of transportation, particularly transport by highways, rail and water. Although air travel is generally significantly more convenient and comfortable for passenger traffic, the cost of air travel is usually much higher than the cost of travel by highways, rail and water. Cargo transport by highways, rail and water are the principal sources of competition to air cargo traffic, particularly in the case of large or heavy loads or goods for which speed is not a priority. In recent years, large amounts of investment have been made in the improvement of the rail network and the construction of highways. This may further intensify the competition for passenger and freight traffic between air transport and transport by highways, rail or water. The Guangdong-Hainan Railway, currently under development by the Ministry of Railways and the Guangdong and Hainan provincial governments and scheduled to open for traffic in 2003, will reduce travel time from Guangzhou to Haikou to approximately 10 hours. The Directors expect that the opening of this railway link will create competition for certain categories of non-priority cargo that is currently carried by air, and among economy travellers. This competition could affect the number of tourist arrivals and cargo throughput at the Meilan Airport.

Competition with other airports

The Meilan Airport faces competition from the Sanya Airport, which is capable of handling all major types of aircraft, including Boeing 747 aircraft. Based on available statistics, aircraft movements at Sanya Airport for the years ended 31st December, 1999, 2000 and 2001 were 15,784, 9,987 and 13,964, respectively, and passenger throughput figures were 500,268, 654,473 and 987,508, respectively. Cumulative annual growth rate for passenger throughput was 40.5%. A large proportion of passenger arrivals at Sanya Airport are tourists who might otherwise fly into and out of the Meilan Airport. If a significant portion of the passengers currently using the Meilan Airport were to choose to fly to Sanya Airport instead, the Company's results of operations could be materially adversely affected.

On 23rd August, 2002, the Company entered into the Sanya Management Contract with SPIA, which owns and operates Sanya Airport. Under this contract, the Company is responsible for the day-to-day management of the Sanya Airport, including human resources, operations, finance, accounting, administration and investment activities. The Company has the right to appoint management of SPIA including the chief executive officer, deputy chief executive officer and chief financial officer. In return, the Company receives a management fee based on the Sanya Airport's annual revenues, plus a percentage of profits (or reduction of net losses).

The Meilan Airport also faces competition from other airports in the region such as Guangzhou, Shenzhen, Zhuhai, Hong Kong and Macau.

Dependence on domestic and regional economic growth

The Chinese civil aviation industry, like that of other countries, is dependent on the level of domestic, regional and global economic growth, international trade and consumer spending. During periods of robust economic growth, passenger movements may grow at a rate as great as, or even greater than, that of the GDP. On the other hand, during periods of slow GDP growth, passenger throughput may exhibit slow or even negative growth. The civil aviation sectors of most Asian countries, including China, were negatively affected by the slow down in economic growth during the Asia financial crisis in late 1990's, leading to reduced load factors among airlines and decreases in passenger throughput and aircraft movements at airports. There can be no assurance that future fluctuations of the economic or business cycle, or other events that could influence GDP growth, will not have an adverse effect on the Group's operating results.

Customer concentration

Revenues from Hainan Airlines and China Southern Airlines, the Group's top two airline customers and two of the shareholders of the Company, accounted for approximately 32.8% and 24.4% of total revenues of the Group for the year ended 31st December, 2001 and 21.9% and 16.3% for the five months ended 31st May, 2002. The Directors expect that revenues from Hainan Airlines and China Southern Airlines will continue to account for a substantial portion of the Group's revenues. None of the Company's airline customers, including Hainan Airlines and China Southern Airlines, have long-term contracts with the Company. Any circumstance that could adversely affect the volume of traffic contributed by Hainan Airlines or China Southern Airlines, or their respective operating and financial conditions, could have an adverse effect on the Group's results of operations.

Operation and business interruption

The operation of the Meilan Airport and the business of the Group could be interrupted or otherwise affected by serious air traffic accidents or natural disasters such as earthquakes that could cause material damage to the airfield or terminal facilities, or disrupt the ability of aircraft to land at the Meilan Airport. The Group's insurance policies which follows common practice in PRC do not provide for compensation for loss of profits or consequential damages in the case of business interruption. Any such event or condition affecting the Meilan Airport or the areas that it serves could have a material adverse effect on the Company's business, results of operations, prospects and financial condition.

As is the case with many other domestic and international airports around the world, the Meilan Airport has only one commercial runway. There is no assurance that the operation of the runway may not be disrupted due to required maintenance or repairs. In addition, the runway could require unscheduled repair or maintenance due to natural disasters, aircraft accidents and other factors that are beyond the Group's control. The closure of the runway for a significant period of time could have a material adverse effect on the Group's business, results of operations, prospects and financial condition.

Reliance on and integration with other authorities and service providers

As is the case with most airports, the safe and efficient operation of the Meilan Airport is in large measure dependent on the services provided by third parties. Air and ramp traffic control for all aircraft landing at and taking off from the Meilan Airport is exercised by SCATC. Energy and water supply are provided by Parent Company which has sourced the energy and water from local public utility operators. The PRC Border Control Authority and Chinese Customs are responsible for immigration and customs procedures, respectively. Air catering services are provided by Hainan Food, a joint venture between Hainan Airlines and Maxim's of Hong Kong, pursuant to a franchise arrangement. The Cargo Centre is operated by a 85%-owned subsidiary of HNA Group, pursuant to a franchise arrangement. Aviation fuel is supplied by Hainan Meiya Industrial Company Limited, a joint venture between Parent Company and Sinopec Hainan Economic Development Company Limited, in which Parent Company owns a 67% majority interest. The operations of these third parties are not generally within the Group's control. There is no assurance that any disruption or failure of the operation of these third parties will not have an adverse effect on the operation of the Meilan Airport and on the Group's financial condition and operating results.

Control of the Runway

Parent Company has retained the ownership and operation of the runway. The airport permit issued by CAAC is also being held under the name of Parent Company. The Company has entered into the Agreement on Runway with Parent Company on 25th October, 2002, which provides, inter alia, that Parent Company is obliged (i) to operate and maintain the runway in accordance with the applicable regulatory and industrial standards and keep the runway in good working condition; (ii) not to change the current usage of the runway unless approved by the relevant governmental departments and agreed in writing by the Company; (iii) not to dispose of any assets of or interests in the runway without agreement of the Company; and (iv) to hold the airport permit and maintain the validity thereof. Neither the operation of the runway nor the maintenance of the airport permit is under the direct control of the Group. There is no assurance that the runway will always be operated and maintained up to the regulatory and industrial standards applicable to the Meilan Airport or that no disruption of operation will occur due to improper or negligent handling of the runway by the staff of Parent Company. Any such disruption or a suspension of the airport permit could have a material adverse effect on the Group's results of operations and financial condition.

Revenue sharing with Parent Company

In view of Parent Company's operation and maintenance of the runway and provision of the related services to airline customers pursuant to the Agreement on Runway, the Company and Parent Company share the aircraft movement fees (for domestic, Hong Kong, Macau and foreign airlines), the passenger charges (for domestic airlines) and the basic ground handling services fees (for Hong Kong, Macau and foreign airlines) on such ratio as CAAC or other regulatory authorities may prescribe from time to time. The current prescribed ratio is on basis of 75% to the Company and 25% to Parent Company. There is no assurance that the current prescribed ratio will not be changed during the term of the agreement to be less favourable to the Company.

Material changes to the Agreement on Runway

The transaction under the Agreement on Runway, which has a term of 20 years, is regarded as a connected transaction as defined under the Listing Rules. The Agreement on Runway provides that any material changes to the terms and conditions of the agreement are subject to approval by the independent shareholders and the requirements under the Listing Rules, so long as the Company maintains its listing status with the Stock Exchange and Parent Company is regarded as a connected person of the Company under the Listing Rules.

If any material changes to the terms of the Agreement on Runway are proposed in the future in order to comply with any regulatory requirements, such material changes must be approved by the shareholders of the Company. If shareholders' approval is not duly obtained, the implementation of the proposed changes in the terms and conditions provided under the Agreement on Runway will not be possible and the business of the Group could be interrupted.

Technical Services Agreement

The Company and CADI, a wholly-owned subsidiary of the Strategic Investor, have entered into the Technical Services Agreement for a term of approximately 10 years for the provision by CADI to the Group of certain technical and advisory services in respect of the long-term management and development of the Meilan Airport. The Technical Services Agreement will terminate upon, amongst other things, the Strategic Investor and its wholly-owned subsidiaries collectively holding less than 75% of the Strategic Placing Shares (which will represent approximately 15% of the enlarged issued share capital of the Company immediately upon completion of the Offering, including any exercise of the Over-allotment Option). Accordingly, there is no assurance that the Company will be able to enjoy the benefits of the Technical Services Agreement for the full term.

Natural disasters

From time to time, Hainan Island, like other South China Sea destinations, experiences typhoons, particularly during the third quarter of each year. Natural disasters could impede operations, damage infrastructure necessary to the Group's operations or adversely affect the destinations served by the Meilan Airport. Any of these events could reduce the passenger traffic volume. The occurrence of natural disasters in the destinations served by the Meilan Airport could adversely affect the Group's business, results of operations, prospects and financial condition. The Group has insured the physical facilities at the Meilan Airport against damage caused by natural disasters, accidents or other similar events, but does not have insurance covering losses due to resulting business interruption. Moreover, should losses occur, there can be no assurance that losses caused by damages to the physical facilities will not exceed the pre-established limits on the policies.

Construction risk

A number of airport expansion and renovation projects to be undertaken by the Group require substantial capital expenditure during their construction and it may take many months, or possibly years, from the time when construction commences for the projects to be completed. The time taken and the costs incurred in completing an expansion or renovation project can be adversely affected by many factors including, but not limited to, shortages of materials, equipment, technical skills and labor; adverse weather conditions; natural disasters; labor disputes; disputes with contractors and sub-contractors; accidents; changes in government priorities and policies; delays in receiving the requisite licenses, permits and approvals from the relevant authorities and unforeseen problems and circumstances. Any of these factors could give rise to delays in the completion of a project and result in costs exceeding those originally budgeted. The failure to complete the construction of a project to its planned specifications or schedule may result in the liabilities being assumed, reduced efficiency or loss of revenue or less attractive returns.

Implementation of the Group's business strategy

The Company's ability to increase the revenues and profitability will depend in part on whether it can successfully implement its business strategy of increasing the revenues from commercial activities and increasing passenger and cargo traffic at the Meilan Airport. See "Business — Business Strategy and Strengths — Business Strategy".

This in turn will depend on several factors, including but not limited to:

- the Group's success in building its airport management business;
- whether and when Meilan Airport can obtain the international airport status;
- the Group's ability to capitalise on opportunities to increase commercial revenues;
- the Group's ability to continue to find means of controlling costs and increasing operating efficiency; and
- the Group's ability to obtain relevant finance as and when required.

Each of these factors is subject to various risks and uncertainties. Further, the ability to increase the commercial revenue is partially dependent upon increasing passenger traffic at the Meilan Airport. There is no assurance that the Group will be successful in implementing its strategy. The passenger traffic volume in the Meilan Airport also depends on other factors beyond the Group's control, such as the appeal of Hainan as a tourist destination. Accordingly, there can be no assurance that the passenger traffic volume in the Meilan Airport will increase.

Potential conflicts of interests

Immediately following the completion of the Offering, Parent Company will directly control over 50% of the Company's issued Shares. Accordingly, Parent Company may be able to exercise significant influence over the Company's business and will be able to control matters requiring shareholders' approval, including:

- the election of directors;
- merger or consolidation of the Company with other entities;
- the timing and amount of dividend payments; and
- other actions that require the approval of the majority of the Company's shareholders.

The interests of Parent Company as the Company's controlling shareholder could conflict with the interests of other shareholders of the Company. There is no assurance that Parent Company, as controlling shareholder, will always vote its Shares in a way that benefits the other shareholders of the Company. In such circumstances, the interests of the other shareholders may be adversely affected.

Subject to compliance with the applicable laws, regulations and rules, there are a number of matters which, pursuant to the Shareholders' Agreement, must be decided by the Board and there are certain matters which can only be approved by the Board if none of the Directors nominated by Parent Company or the executive Director nominated by the Strategic Investor has voted against such matter at the relevant Board meeting. Although Parent Company and the Strategic Investor have agreed to procure that all Directors would vote in the best interests of the Company as a whole, there is no assurance that any resolution in respect of such matters would not be voted against. To such extent, the interests of the other shareholders may also be adversely affected.

Regulation by CAAC

Civil airports in China are subject to extensive direct regulation by CAAC, which also incorporates relevant international treaties in relation to many aspects of their operations including technical standards of airfield facilities and equipment, aeronautical fees, renovation, construction and expansion of airport facilities, air traffic and ground safety. CAAC's regulation relating to airlines such as approval of new international routes, new domestic airlines, route allocation, airfares and the purchase or lease of aircraft may also affect the operation of civil airports in China. While the Group generally benefits from CAAC policies that are beneficial to the civil aviation industry in China as a whole, it is possible that there may be conflicts between these policies and the implementation of certain CAAC policies could from time to time adversely affect the Group's operation. In particular, there can be no assurance that CAAC will not make any changes in the regulations or policies affecting the levels of the aeronautical fees, which may have an adverse effect on the Group's revenues. Also, there can be no assurance of aeronautical fee increases when such increases are applied for, if at all. Nor can there be assurance that CAAC will, in all circumstances, apply its regulations and policies in a manner that results in equal treatment of all airports.

The Group's business is subject to extensive and evolving PRC laws and regulations. Many of the laws, regulations and instruments that regulate the Group's business were only recently adopted or became effective, and there is only a limited history that it would be difficult to predict the impact of these legal requirements on the Company's future operations. These laws and regulations may limit the flexibility in operating the business, which could have a material adverse effect on the Company's business, results of operations, prospects and financial condition. Moreover, there can be no assurance that the laws and regulations governing the Group's business will not change.

Impact of consolidation and reorganisation in the PRC aviation industry

In early 2002, the State Council approved an airline consolidation plan to establish three large airline groups led by the three major carriers — Air China, China Southern Airlines and China Eastern Airlines. In October 2002, the holding companies of the three groups were incorporated. Yunnan Airlines, China Northwest Airlines and China Eastern Airlines formed the China Eastern Airlines group, China Northern Airlines, China Xinjiang Airlines and China Southern Airlines formed the China Southern Airlines group, and China Southwest Airlines, China National Aviation Corporation and Air China formed the Air China group. The three airline groups are proceeding to carry out the asset restructurings necessary to give effect to the consolidation plan.

The Directors believe that the Group's long term growth will depend on the demand for air traffic to Haikou and that the possible mergers and reorganisations of domestic airlines, if consummated, will improve the overall health of the Chinese airline industry and will benefit the Group in the long run. However, there is no assurance that such consolidation will not in the short run result in a reduction of aircraft movements.

11th September 2001 terrorist attacks on the US

On 11th September, 2001, terrorist attacks on the United States using the aircraft of major US airlines caused massive loss of life and property damage and disruption to the United States and global markets, and to the aviation industry in particular.

The adverse impacts of the 11th September attacks on the aviation industry have included:

- decrease of international air traffic and related revenues
- decrease of international tourism
- loss of revenue from decreased international air cargo
- increase of aviation insurance cost
- increase of operational costs, especially those relating to airline and airport security

Although nothing suggests that the aircraft movements of PRC domestic routes or domestic demand have changed significantly since the 11th September attacks, aviation safety and airport security procedures have been made more strict, and such changes could increase operational costs for both the airlines and the airports, including the Meilan Airport.

Environmental Protection

Environmental protection standards applicable to airports in China are set out in certain laws and regulations including the Environmental Protection Law, Noise Pollution Law, Air Pollution Prevention Law and Solid Waste Pollution Prevention Law.

In relation to noise, the aircraft engine noise created by approaching and departing aircraft using the Meilan Airport may exceed the prescribed level applicable to areas around airports. There is no assurance that the Group may not face claims for noise pollution in the future. Under PRC law, questions of airport liability for aircraft noise pollution are unclear. If the Group were required to pay fines or compensation for violations of noise pollution standards, or if airlines were forced to curtail or limit flight operations to meet noise pollution standards, the Group's financial position and results of operations could be adversely affected.

Forecasts prepared by Booz Allen Hamilton and Parsons Brinckerhoff (Asia) Limited

The airport traffic forecasts and the future cost projections set out in Appendices V and VI were prepared by Booz Allen Hamilton and Parsons Brinckerhoff (Asia) Limited respectively using various analytical methodologies and assumptions. These assumptions may not be realised, and unanticipated events and circumstances that are beyond the Group's control may occur, which may cause the actual figures to differ from the forecasts.

Future operating results may vary significantly from profit forecast

The profit forecast for the year ending 31st December, 2002 contained in this prospectus has been prepared in accordance with customary practice, on the basis and assumptions set out in Appendix III to this prospectus. These projections reflect the Directors' current judgment of expected operating conditions and results. Actual results for the year may vary from the forecast results, and any such variance could be material. The Group does not intend to update or otherwise revise the forecast prior to announcement of the actual results of operations for the year.

Loss of tax preferences could affect net profit attributable to shareholders

The Company enjoys, and expects to continue to enjoy, significant tax preferences pursuant to which corporate income tax rates are waived for a period, and reduced for a subsequent period to rates substantially below the prevailing rate of 15%. If, pursuant to its accession to the World Trade Organisation, China were to adopt a system of national treatment, or if the tax preferences were otherwise eliminated or phased out as a result of which the enterprises in Hainan Province may no longer enjoy a 15% income tax rate, or an infrastructure project such as an airport may no longer be entitled to a 5-year income tax exemption followed by another 5-year 50% reduction, the Group's net profit attributable to shareholders would be adversely affected. The Group's corporate income tax may increase and this could result in a corresponding decrease to the Group's net profit after tax.

Dividends

On 19th July, 2002, the shareholders of the Company approved the distribution of a final dividend of RMB45 million for the year ended 31st December, 2001 to the then existing shareholders.

Whilst the Company intends to make dividend payments in the future, the amount of dividends to be declared will be subject to, among others, the discretion of the Directors, the Group's earnings, financial position, cash requirements and availability, the provisions of the relevant PRC laws, and other relevant factors. The past dividend distribution record should not be used as a reference or basis to determine the amount of dividends which may be payable in the future. There is no assurance that dividend distribution will continue in the future.

RISKS RELATING TO THE PRC

Political and economic factors

The economy of the PRC differs from the economies of most countries belonging to the Organisation for Economic Cooperation and Development ("**OECD**") in such respects as structure, government involvement, level of development, growth rate, capital reinvestment, allocation of resources, rate of inflation and balance of payments position. Prior to 1978, the economy of the PRC was a planned economy. Since that time, increasing emphasis has been placed on the utilisation of market forces in the development of the PRC economy. Annual and five year State Plans are adopted by the PRC government in connection with the development of the economy. Although state-owned enterprises still account for a substantial portion of the PRC's industrial output, in general, the State is reducing the level of direct control that it exercises over the economy through State Plans and other measures, and there is an increasing degree of liberalisation and autonomy in areas such as allocation of resources, production, pricing and management and a gradual shift in emphasis to a "socialist market economy" and enterprise reform.

The Group's operations and financial results could be adversely affected by political, economic and social conditions or changes in the policies of the PRC government, such as changes in laws and regulations (or the interpretation thereof), measures which may be introduced to regulate or stimulate the rate of economic growth, changes in the rate or method of taxation, imposition of additional restrictions on currency conversion and the imposition of additional import restrictions. Furthermore, a significant portion of the economic activity in the PRC and Hainan depends on the level of export and tourism, respectively, and therefore, is affected by developments in the economies of the PRC's principal trading partners and other economies.

Foreign exchange considerations

As part of its currency reforms, China abolished its two-tiered exchange rate system effective 1st January, 1994 and replaced it with a unified controlled exchange rate system based on market conditions. Under this system, the PBOC quotes a daily exchange rate for Renminbi to the US dollar based on the market rate for foreign exchange transactions conducted by the designated banks in the PRC foreign exchange market during the preceding day. The PBOC also quotes the exchange rates of Renminbi to other foreign currencies based on the international market rate. When the new system came into operation on 1st January, 1994, the exchange rate was set at approximately RMB8.7 to US$1.00, representing a devaluation of the Renminbi of approximately 50% from the previous official rate set at RMB5.8. However, since 1994, the exchange rate for Renminbi against the U.S. dollar has been relatively stable. As the exchange rate is based primarily on market forces, the exchange rates for the Renminbi against other currencies, including the U.S. dollar, HK dollar and yen, are susceptible to movements based on external factors. There can be no assurance that the Renminbi may not be subject to devaluation. Any devaluation could adversely affect the value of an investment in the H Shares and of any cash dividends on the H Shares since the Group's revenues will be received, and its profits and dividends will be expressed, in Renminbi.

Legal and other regulatory considerations

Developing legal system

The PRC legal system is a system based on written statutes and their interpretation by the Supreme People's Court. Prior court decisions may be cited for reference but have limited precedential value. Since 1979, the PRC government has been developing a comprehensive system of commercial laws, and considerable progress has been made in introducing laws and regulations dealing with economic matters such as foreign investment, corporate organisation and governance, commerce, taxation and trade. Two examples are the promulgation of the Contract Law of the PRC to unify the various contract laws into a single code, which went into effect on 1st October, 1999, and the Securities Law of the PRC, which went into effect on 1st July, 1999. However, because these laws and regulations are relatively new, and because of the limited volume of published cases and their non-binding nature, interpretation and enforcement of these laws and regulations involve uncertainties. In addition, as the PRC legal system develops, changes in such laws and regulations, their interpretation or their enforcement may have a material adverse effect on the Group's business operations.

Because the Company is offering and listing its H Shares outside the PRC, it is subject to PRC regulations governing PRC companies that are listed overseas. These regulations contain provisions that are required to be included in the articles of association of these PRC companies and are intended to regulate the internal affairs of these companies. The PRC Company Law and these regulations, in general, and the provisions for the protection of shareholders' rights and access to information, in particular, are less developed than those applicable to companies incorporated in Hong Kong, the United States and other developed countries or regions. Such limited investor protections are off-set, to some extent, by the Mandatory Provisions and additional requirements that are imposed by the Listing Rules, with a view to reducing the differences between Hong Kong company law and PRC Company Law. The articles of association of all PRC companies listed in Hong Kong must incorporate these Mandatory Provisions. Although the Articles of Association have incorporated these provisions and requirements, the Company's shareholders may still not be able to enjoy protections that they may be entitled to in other jurisdictions.

Shareholders' rights

The Company is organised under PRC law and is governed by its Articles of Association. In addition to the Articles of Association, the primary sources of the Company's shareholders' rights are the PRC Company Law and, upon listing on the Hong Kong Stock Exchange, the Listing Rules, which, among other things, impose certain standards of conduct, fairness and disclosure on the Company, its Directors and its controlling shareholder. To the Company's knowledge, there has not been any published report of judicial enforcement in the PRC by holders of H shares of their rights under charter documents of joint stock limited companies or the PRC Company Law or in the application or interpretation of the PRC or Hong Kong regulatory provisions applicable to PRC joint stock limited companies.

The legal framework to which the Company is subject may be materially different from Hong Kong company law or corporate laws in the United States with respect to, for example, the protection of minority shareholders. In addition, the mechanisms for enforcement of rights under the corporate framework to which the Company is subject is also relatively undeveloped and untested. In China, shareholders do not have the right to sue the directors, supervisors, officers or other shareholders on behalf of a corporation to enforce a claim against such party or parties which the corporation has failed to enforce itself.

Dispute resolution mechanism

China does not have treaties providing for the reciprocal recognition and enforcement of judgments of courts with the United States, the United Kingdom, Japan or most other Western countries, and therefore recognition and enforcement in China of judgments of a court in any of these jurisdictions in relation to any matter not subject to a binding arbitration provision may be difficult or impossible. The Articles of Association as well as the Listing Rules provide that most disputes between holders of H Shares and the Company, its Directors, Supervisors, officers or holders of Domestic Shares, arising out of the Articles of Association or the PRC Company Law and related regulations concerning the affairs of the Company or with respect to the transfer of the H Shares are to be resolved through arbitration by arbitration organisations in Hong Kong or China, rather than by a court of law. On 21st June, 1999, an arrangement was made between Hong Kong and the PRC for the reciprocal enforcement of arbitral awards. This new arrangement was approved by the Supreme People's Court of the PRC and the Hong Kong Legislative Council, and became effective on 1st February, 2000. The arrangement was made in accordance with the spirit of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958. Under the arrangement, awards that are made by PRC arbitral authorities recognised under the Arbitration Ordinance of Hong Kong can be enforced in Hong Kong. Hong Kong arbitration awards are also enforceable in China. So far as the Company is aware, no action has been brought in China by any shareholder to enforce an arbitral award, and it is uncertain as to the outcome of any action brought in China to enforce an arbitral award made in favour of shareholders. See "Appendix IX — Summary of Principal Legal and Regulatory Provisions — The Arbitration Law."

Taxation of holders of H Shares

Under current PRC tax laws, regulations and rulings, dividends paid by the Company to holders of H Shares who are foreign individuals not resident in the PRC or which are foreign enterprises with no permanent establishments in the PRC are not currently subject to PRC income tax. In addition, gains realised by individuals or enterprises upon the sale or other disposition of H shares are not currently subject to PRC income tax. There can be no assurance, however, that withholding or capital gains taxes will not become applicable to such dividends or gains in the future. In such event, holders of H Shares could become subject to a withholding tax on dividends, which is currently imposed at the rate of 20% or to a capital gains tax, which may currently be imposed upon individuals at the rate of 20%, unless reduced or eliminated by an applicable double taxation treaty. See Appendix VII to this prospectus.

RISKS RELATING TO THE OFFERING

Marketability and possible price volatility of shares

Prior to the Offering, there has been no trading market for the H Shares, and there can be no assurance that an active trading market for the H Shares will develop or be sustained upon completion of the Offering. Shares of other PRC companies listed on the Stock Exchange have experienced substantial price volatility in the past, and it is possible that the H Shares will be subject to changes in price that may not be directly related to the Company's financial or trading performance.

Forward-looking statements

All statements included in this prospectus that do not represent historical facts, including, without limitation, those relating to the future plans and prospects of the Group's operations, the civil aviation industry and the general economy in Hainan and the PRC, are forward-looking statements.

The forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements of the Group, or industry results, to differ materially from those expressed or implied.

The forward-looking statements are based on numerous assumptions regarding the Company's present and future business strategies and the environment in which the Company will operate in the future. Changes in general economic and business conditions in China and elsewhere, general airline industry trends and government policies or regulations of the PRC are some of the important factors that could cause actual results, performance or achievements to differ materially. There can be no assurance that the Group's actual results, performance or achievements will not vary significantly from the forward-looking statements set forth herein. Under no circumstances should the inclusion of the forward-looking statements be regarded as representation, warranty or prediction with respect to its accuracy or the accuracy of the underlying assumptions, or that the Company has achieved or will achieve or is likely to achieve any particular results.

Certain statistics from third party publications

Certain statistics in this prospectus relating to the civil aviation industry, such as statistics relating to passenger traffic and cargo traffic, are derived from various publications. Such information has not been independently verified by the Company and may be inaccurate, incomplete or out-of-date. The Company makes no representation as to the correctness or accuracy of such statements and, accordingly, such information should not be unduly relied upon.

DIRECTORS' RESPONSIBILITY FOR THE CONTENTS OF THIS PROSPECTUS

This prospectus contains particulars given in compliance with the Companies Ordinance, the Securities (Stock Exchange Listing) Rules 1989 (as amended) and the Listing Rules for the purpose of giving information to the public with regard to the Company. The Directors collectively and individually accept full responsibility for the accuracy of the information contained in this prospectus and confirm, having made all reasonable enquiries, that to the best of their knowledge and belief, there are no other facts the omission of which would make any statement in this prospectus misleading.

CONSENT OF THE CSRC

On 14th October, 2002, the CSRC issued a written consent to the Company with respect to the Offering and the application for the listing of the H Shares on the Stock Exchange. The CSRC accepts no responsibility for the financial soundness of the Company or the accuracy of any of the statements made or opinions expressed in this prospectus or in the application forms by virtue of the issuance of the consent.

UNDERWRITING

This prospectus is published solely in connection with the Offering. For applicants under the Public Offer, this prospectus and the application forms set out the terms and conditions of the Public Offer.

The Offering comprises the Public Offer of initially 20,170,000 H Shares and the International Placing of initially 181,530,000 H Shares (including the H Shares conditionally placed under the Strategic Placing), both at the Offer Price (subject, in each case, to reallocation on the basis described in "Structure of the Offering" and, in the case of International Placing only, the Over-allotment Option). Subject to agreement as to pricing, the Public Offer is fully underwritten by the Public Offer Underwriters, the Strategic Placing is fully underwritten by the Strategic Placing Underwriter and the International Placing (excluding the Strategic Placing) is expected to be fully underwritten by the International Placing Underwriters, under the terms of the Public Offer Underwriting Agreement and the International Placing Agreement.

The listing of the H Shares on the Stock Exchange is jointly sponsored by HSBC and Oriental Patron. The International Placing is managed by the Global Coordinator. The Public Offer Underwriting Agreement relating to the Public Offer was entered into on 5th November, 2002. The International Placing Agreement is expected to be entered into on or about 12th November, 2002. The Strategic Investment Agreement relating to the Strategic Placing was entered into on 16th September, 2002 and amended on 30th October, 2002. For further information about the Underwriters and the underwriting arrangements, please see the section headed "Underwriting".

RESTRICTIONS ON OFFER AND SALE OF THE H SHARES

No action has been taken to permit a public offering of the Offer Shares or the distribution of this prospectus and the application forms in any jurisdiction other than Hong Kong. Accordingly, this prospectus may not be used for the purpose of, and does not constitute, an offer or invitation in any jurisdiction or in any circumstances in which such an offer or invitation is not authorised or to any person to whom it is unlawful to make such an offer or invitation.

The Public Offer Shares are offered solely on the basis of the information contained and representations made in this prospectus and the related application forms. The Company has not authorised anyone to provide any information or to make any representation not contained in this prospectus, and any information or representation not contained herein must not be relied upon as having been authorised by the Company, the Vendors, the Joint Sponsors, the Underwriters, any of their respective directors, or any other person involved in the Offering.

Each person acquiring the Offer Shares will be required to confirm, or will be deemed by his acquisition of Offer Shares to have confirmed, that he is aware of the restrictions on offers of the Offer Shares described in this prospectus.

United States

The Offer Shares have not been and will not be registered under the US Securities Act and, subject to certain exceptions, may not be offered, sold, pledged or transferred within the United States, except to qualified institutional buyers in accordance with Rule 144A or outside the United States in accordance with Rule 903 or Rule 904 of Regulation S. The Offer Shares are being offered and sold outside the United States in reliance on Regulation S and within the United States to qualified institutional buyers in reliance on Rule 144A. In addition, until 40 days after the later of the commencement of the Offering and the completion of the distribution of the Offer Shares, an offer or sale of Offer Shares within the United States by any dealer (whether or not participating in the Offering) may violate the registration requirements of the US Securities Act if such offer or sale is made otherwise than in accordance with Rule 144A or another exemption from the registration requirements of the U.S. Securities Act.

The Offer Shares have not been approved or disapproved by the United States Securities and Exchange Commission, any state securities commission in the United States or any other United States regulatory authority, nor have any of the foregoing authorities passed upon or endorsed the merits of the Offering or the accuracy or adequacy of this prospectus. Any representation to the contrary is a criminal offence in the United States.

United Kingdom

This prospectus has not been approved by an authorised person in the United Kingdom and has not been registered with the Registrar of Companies in the United Kingdom. The Offer Shares are not being offered or sold and may not be offered or sold in the United Kingdom prior to the date six months from the date on which dealings in H Shares commence on the Stock Exchange except to persons whose ordinary activities involve them in acquiring, holding, managing or disposing of investments, as principal or agent, for the purposes of their businesses or otherwise in circumstances which have not resulted in and will not result in an offer to the public in the United Kingdom within the meaning of the Public Offers of Securities Regulation 1995.

In addition, no person may communicate or cause to be communicated any invitation or inducement to engage in investment activity (within the meaning of section 21 of the Financial Services and Markets Act 2000 ("**FSMA**")) received by it in connection with the issue or sale of any Offer Shares except in circumstances in which section 21(1) of the FSMA does not apply to the Company. This communication is directed only at persons who (i) have professional experience in matters relating to investments or (ii) are persons falling within Article 49(2)(a) to (d) (high net worth companies, unincorporated associations, etc.) of The Financial Services and Markets Act 2000 (Financial Promotion) Order 2001 (all such persons together being referred to as "**relevant**

persons"). This communication must not be acted on or relied on by persons who are not relevant persons. Any investment or investment activity to which this communication relates is available only to relevant persons and will be engaged in only by relevant persons.

Singapore

This prospectus has not been and will not be registered as a prospectus with the Monetary Authority of Singapore. The Offer Shares which are the subject of this prospectus are being offered for sale in Singapore pursuant to the exemptions from prospectus requirements under Sections 274 and 275 of the Securities and Futures Act 2001 of Singapore ("**Securities and Futures Act**"). This prospectus is made available to the recipient on the basis that such recipient is a person set out or defined in the aforesaid provisions of the Securities and Futures Act and the recipient's attention is drawn to the restrictions set out in Section 276 of the Securities and Futures Act. Accordingly, the Offer Shares being offered hereby may not be offered or sold nor may this prospectus or any other offering document or material relating to such Offer Shares be circulated or distributed, directly or indirectly, to the public or any member of the public in Singapore other than pursuant to, and in accordance with the conditions of, Sections 274 and 275 of the Securities and Futures Act and to persons to whom such Offer Shares may be offered or sold under those provisions.

PRC

This prospectus does not constitute a public offer of the Offer Shares, whether by way of sale or subscription, in the PRC. The Offer Shares are not being offered and may not be offered or sold directly or indirectly to or for the benefit of legal or natural persons of the PRC.

Italy

The Offer Shares are not being offered, sold or delivered and may not be offered or sold or delivered and this prospectus may not be distributed in Italy except (a) to "Professional Investors" (as defined by Articles 25 and 31, paragraph 2 of Regulation no. 11522 of 1st July, 1998 as amended issued by CONSOB, the local stock market regulator in Italy) in compliance with the terms and procedures provided by Legislative Decree no. 58 of 24th February, 1998, or the Finance Law, or (b) in any other circumstance where an express exemption to comply with the solicitation restrictions provided by the Finance Law or CONSOB Regulation no. 11971 of 14th May, 1999 as amended, or the Issuers Regulation, applies, including those provided for under Art. 100 of the Finance Law and Art. 33 of the Issuers Regulation, and any such offer, sale or delivery of the Offer Shares or distribution of copies of this prospectus or any other document relating to the Offer Shares must be made:

(i) by investment firms, banks or financial intermediaries authorised to carry out such activities in Italy in accordance with the Finance Law, Issuers Regulation, Legislative Decree no. 385 of 1st September, 1993, or the Banking Law, CONSOB Regulation no. 11522 of 1st July, 1998, all as amended, and any other applicable laws and regulations;

(ii) in compliance with Art. 129 of the Banking Law, as supplemented by Bank of Italy's instructions, under which the issue or placement of securities in Italy is subject to a prior notification, unless an exemption, depending, among others on the amount of the issue or placement, applies; and

(iii) in compliance with any other applicable notification requirement or limitation which may, from time to time, be imposed by CONSOB or the Bank of Italy.

Japan

The offering of the Offer Shares has not been and will not be registered under the Securities and Exchange Law of Japan ("**Securities and Exchange Law**") and the Offer Shares may not be offered or sold, directly or indirectly, in Japan or to, or for the benefit of, any resident of Japan (which term as used herein means any person resident in Japan, including any corporation or other entity organised under the law of Japan), or to others for re-offering or resale, directly or indirectly, in Japan or to, or for the benefit of, any resident of Japan, except in circumstances which will result in compliance with the Securities and Exchange Law and all other applicable laws of Japan and regulations promulgated by the relevant Japanese governmental and regulatory authorities in effect at the relevant time.

Denmark

This prospectus has not been filed with or approved by the Danish Securities Council or any other Regulatory Authority in the Kingdom of Denmark. The Offer Shares may not be offered or sold directly or indirectly in Denmark, except to professional investors (being entities which are subject to financial supervision in Denmark or physical and legal persons acting in the course of their business) or otherwise in circumstances which will not result in the offer of the Offer Shares being subject to the Danish prospectus requirements pursuant to Chapter 12 of the Danish Act on Trading in Securities and Executive Order No. 1207 of 15th December, 2000 on the First Public Offer of Certain Securities.

France

Neither this prospectus nor any offering material relating to the Offer Shares has been or will be submitted to the Commission des Operations de Bourse for approval in France, and the Offer Shares may not be offered or sold and this prospectus or any offering material may not be distributed or caused to be distributed, directly or indirectly, in France, except (i) with the prior authorisation of the French Ministry for Economy and Finance in accordance with Articles 9 and 10 of the Décret n° 89-938 of 29th December, 1989 regulating financial relations between France and foreign countries and (ii) in accordance with Articles L. 411-2 of the French Monetary and Financial Code to qualified investors (*"investisseurs qualifies"*) or to a restricted group of investors (*"cercle restreint d'investisseurs"*), qualified investors and members of the restricted group of investors in each case acting for their own account pursuant to the Décret n° 98-880 of 1st October, 1998. The resale in France, directly or indirectly, to the public of the Offer Shares as so purchased may only be made in accordance with the provisions of Articles L. 411-1 *et seq.* of the French Monetary and Financial Code.

Germany

This prospectus has not been filed with or approved by the Federal Financial Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht* — BAFin) in Germany. The Offer Shares may not be offered or sold in Germany except to persons or under circumstances falling within the scope of section 2 numbers 1, 2 or 4 of the German Securities Sales Prospectus Act (*Wertpapier-Verkaufsprospektgesetz* — VerkprospG) in its version of 9th September, 1998 as amended and provided that compliance will be made with all German securities, tax, exchange control and other applicable laws and regulations. Under the above cited exemptions of the VerkprospG, the Offer Shares can only be offered and sold, (i) to persons who, in the course of their professional or commercial activities, purchase or sell securities for their own account or the account of others; or

(ii) to a restricted circle of persons as this term is construed by the courts and BAFin; or (iii) to investors if they acquire in denominations of at least Euro 40,000 or for a purchase price of at least Euro 40,000 per investor.

Sweden

This prospectus has not been filed with or approved by the Swedish Financial Supervisory Authority under the Swedish Financial Instruments Trading Act (1991: 980). The Offer Shares may not be offered or sold directly or indirectly in Sweden except in circumstances which will not trigger the requirement to register and file a prospectus under the Swedish Financial Instruments Trading Act.

APPLICATION FOR LISTING ON THE STOCK EXCHANGE

The Company has applied to the Listing Committee of the Stock Exchange for the listing of, and permission to deal in, the H Shares to be issued or sold pursuant to the Offering (including the additional H Shares which may be issued pursuant to the exercise of the Over-allotment Option). Save as disclosed in this prospectus, no part of the share or loan capital of the Company is listed on or dealt in on any other stock exchange or any other authorised trading facilities and at present, no such listing or permission to list is being or proposed to be sought pursuant to the Offering.

HONG KONG H SHARE REGISTER AND STAMP DUTY

All of the H Shares issued pursuant to the Offering will be registered on the Company's H Share register of members to be maintained in Hong Kong.

Dealings in the H Shares registered in the Hong Kong register of members will be subject to Hong Kong stamp duty. Further information is set out in Appendix VII to this prospectus.

Unless determined otherwise by the Company, dividends payable in respect of the H Shares will be paid to the shareholders on the register of the Company, by ordinary post at the shareholders' risks to the registered address of each shareholder.

PROFESSIONAL TAX ADVICE RECOMMENDED

Potential shareholders are recommended to consult their professional advisers if they are in any doubt as to the taxation implications of subscribing for, purchasing, holding and dealing in the H Shares. None of the Company, the Vendors, the Underwriters, any of their respective directors or any other person or party involved in the Offering accepts responsibility for any tax effects on, or liabilities of, any person resulting from the subscription, purchase, holding or dealing in the H Shares.

REGISTRATION OF SUBSCRIPTION, PURCHASE AND TRANSFER OF H SHARES

The Company has instructed Computershare Hong Kong Investor Services Limited, its Hong Kong share registrar, and Computershare Hong Kong Investor Services Limited has agreed, not to register the subscription, purchase or transfer of any H Shares in the name of any particular holder unless and until the holder delivers a signed form to the share registrar in respect of those H Shares bearing statements to the effect that the holder:

(i) agrees with the Company and each shareholder of the Company, and the Company agrees with each shareholder, to observe and comply with the Company Law, the Special Regulations, and the Articles of Association;

(ii) agrees with the Company, each shareholder of the Company, Director, Supervisor, manager and officer of the Company, and the Company acting for itself and for each Director, Supervisor, manager and officer of the Company agrees with each shareholder of the Company to refer all differences and claims arising from the Articles of Association or any rights or obligations conferred or imposed by the Company Law or other relevant laws and administrative regulations concerning the affairs of the Company to arbitration in accordance with the Articles of Association, and any reference to arbitration shall be deemed to authorise the arbitration tribunal to conduct hearings in open session and to publish its award, which arbitration shall be final and conclusive;

(iii) agrees with the Company and each shareholder of the Company that H Shares in the Company are freely transferable by the holders thereof; and

(iv) authorises the Company to enter into a contract on his behalf with each Director and officer of the Company whereby such Directors and officers undertake to observe and comply with their obligations to shareholders as stipulated in the Articles of Association.

STABILISATION

In connection with the Offering, HSBC, on behalf of the International Placing Underwriters, may over-allocate the H Shares and may cover such over-allocations by exercising the Over-allotment Option no later than 30 days after the date of this prospectus or by making open market purchases in the secondary market or by stock borrowing or by the combination of any of the above. The number of the H Shares over-allocated will not be greater than the maximum number of the H Shares which may be issued upon full exercise of the Over-allotment Option, being 25,213,000 H Shares, which is approximately 12.5% of the H Shares initially available under the Offering. HSBC may also, on behalf of the Underwriters, effect transactions which stabilise or maintain the market price of the H Shares. Such transactions may be effected in all jurisdictions where it is permissible to do so, in each case in compliance with all applicable laws and regulatory requirements. Such transactions, if commenced, may be discontinued at any time. Should stabilising transactions be effected in connection with the distribution of the H Shares, they will be done at the absolute discretion of HSBC.

Stabilisation is a practice used by underwriters in some markets to facilitate the distribution of securities. To stabilise, the underwriters may bid for, or purchase, the newly issued securities in the secondary market, during a specified period of time, to retard and, if possible, prevent a decline in the initial public offer prices of the securities. The stabilisation price will not exceed the initial public offer price.

Stabilisation is not a practice commonly associated with the distribution of securities in Hong Kong. In Hong Kong, such stabilisation activities on the Stock Exchange are restricted to cases where underwriters genuinely purchase shares on the secondary market solely for the purpose of covering over-allocations in an offering. The relevant provisions of the Securities Ordinance (Chapter 333 of the Laws of Hong Kong) prohibit market manipulation in the form of pegging or stabilising the price of securities in certain circumstances.

PROCEDURE FOR APPLICATION FOR PUBLIC OFFER SHARES

The procedure for applying for Public Offer Shares is set out in the section headed "How to Apply for Public Offer Shares" in this prospectus and on the relevant applications forms.

STRUCTURE OF THE OFFERING

Details of the structure of the Offering, including its conditions, are set out in the section headed "Structure of the Offering" in this prospectus.

EXCHANGE RATE CONVERSION

Except as otherwise noted, this prospectus contains translations of Renminbi amounts into Hong Kong dollars at the rate of HK$1.00 = RMB1.0611, the PBOC Rate prevailing on 31st May, 2002, for reference only. No representation is made that the Renminbi amounts set out in this prospectus could have been or could be converted into Hong Kong dollars, as the case may be, at any particular rate on such date or any other date. Risks associated with the restriction on foreign exchange conversion and the fluctuation of Renminbi exchange rate are set out in the section headed "Risk Factors — Risks relating to the PRC — Foreign exchange considerations".

DIRECTORS

Name	Address	Nationality
Executive Directors		
Mr. Chen Wenli (陳文理)	Block 19 Tianhai Court Club Changyu Road Haikou City Hainan Province, PRC	Chinese
Mr. Zhang Han'an (張漢安)	Block 18 Tianhai Court Club Changyu Road Haikou City Hainan Province, PRC	Chinese
Mr. Liu Lu (劉璐)	6412, Taihe Garden Haidian Sidong Road Haikou City Hainan Province, PRC	Chinese
Non-executive Directors		
Mr. Li Xianhua (李先華)	Block 6 Tianhai Court Club Changyu Road Haikou City Hainan Province, PRC	Chinese
Mr. Jing Xingxiang (景興祥)	Room 401 Nanxing Mansion 49 Jichang Road East Haikou City Hainan Province, PRC	Chinese
Independent Non-executive Directors		
Mr. Xu Boling (徐柏齡)	Room 4302 No. 20 Yinzha Alley Beiheyuanda Road Dongcheng District Beijing, PRC	Chinese
Mr. Meng Jianqiang (蒙建強)	Room A, 23rd Floor Block 1, Provident Centre Hong Kong	Chinese

SUPERVISORS

Name	Address	Nationality
Mr. Zhang Cong (張聰)	12E, Block 5 Landmark Garden Mingzhu Road Haikou City Hainan Province, PRC	Chinese
Mr. Zheng Hong (鄭宏)	3A, Block 1 Asia Court Nanhai Road Haikou City Hainan Province, PRC	Chinese
Ms. Zeng Xuemei (曾雪梅)	303, Block 5 Agriculture Science College Liufang Road Haikou City Hainan Province, PRC	Chinese

Global Coordinator and Bookrunner	**The Hongkong and Shanghai Banking Corporation Limited** Level 15 1 Queen's Road Central Hong Kong
Joint Sponsors and Joint Lead Managers	**The Hongkong and Shanghai Banking Corporation Limited** Level 15 1 Queen's Road Central Hong Kong
	Oriental Patron Asia Limited Units 4201–07, COSCO Tower 183 Queen's Road Central Hong Kong
Co-Lead Managers	**CITIC Capital Markets Limited** 26th Floor, CITIC Tower 1 Tim Mei Avenue Central Hong Kong
	ICEA Capital Limited 42nd Floor, Jardine House 1 Connaught Place Central Hong Kong
	ING Bank N.V. 39th Floor, One International Finance Centre 1 Harbour View Street Central Hong Kong
	Nomura International (Hong Kong) Limited 20th–21st Floor, Asia Pacific Finance Tower 3 Garden Road, Central Hong Kong
Public Offer Underwriters	**The Hongkong and Shanghai Banking Corporation Limited** Level 15 1 Queen's Road Central Hong Kong

Oriental Patron Asia Limited
Units 4201–07, COSCO Tower
183 Queen's Road Central
Hong Kong

CITIC Capital Markets Limited
26th Floor, CITIC Tower
1 Tim Mei Avenue
Central
Hong Kong

ICEA Capital Limited
42nd Floor, Jardine House
1 Connaught Place
Central
Hong Kong

ING Bank N.V.
39th Floor, One International Finance Centre
1 Harbour View Street
Central
Hong Kong

Nomura International (Hong Kong) Limited
20th–21st Floor, Asia Pacific Finance Tower
3 Garden Road, Central
Hong Kong

International Placing Underwriters

The Hongkong and Shanghai Banking Corporation Limited
Level 15
1 Queen's Road Central
Hong Kong

Oriental Patron Asia Limited
Units 4201–07, COSCO Tower
183 Queen's Road Central
Hong Kong

CITIC Capital Markets Limited
26th Floor, CITIC Tower
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Central
Hong Kong

Nomura International (Hong Kong) Limited
20th–21st Floor, Asia Pacific Finance Tower
3 Garden Road, Central
Hong Kong

Strategic Placing Underwriter

The Hongkong and Shanghai Banking Corporation Limited
Level 15
1 Queen's Road Central
Hong Kong

Legal Advisers to the Company

as to Hong Kong law:
Deacons
3rd–7th, 18th and 29th Floors
Alexandra House
16–20 Chater Road
Central
Hong Kong

as to PRC law:
Jun He Law Offices
20th Floor, China Resources Building
8 Jianguomenbei Avenue
Beijing 100005
The PRC

Legal Advisers to the Underwriters

as to Hong Kong law and United States laws:
Baker & McKenzie
14th Floor, Hutchison House
10 Harcourt Road
Central
Hong Kong

as to PRC law:
Commerce & Finance Law Offices
No. 714 Huapu International Plaza
19 Chaowai Avenue, Beijing 100020
The PRC

Auditors and Reporting Accountants	**Ernst & Young** *Certified Public Accountants* 15th Floor, Hutchison House 10 Harcourt Road Central Hong Kong
Property Valuers	**Vigers Hong Kong Limited** Room 1607–12, Miramar Tower 132 Nathan Road Tsimshatsui Kowloon Hong Kong
Air Traffic Consultants	**Booz Allen Hamilton (Australia) Limited** Level 7, 123 Eagle Street Brisbane, QLD 4000 Australia
Engineering Consultants	**Parsons Brinckerhoff (Asia) Limited** 23rd Floor, AIA Tower 183 Electric Road North Point Hong Kong
Receiving Banker	**The Hongkong and Shanghai Banking Corporation Limited** 1 Queen's Road Central Hong Kong

Legal address:	Meilan Airport Complex Qiong Shan City Hainan Province PRC
Place of business in Hong Kong:	Unit 3205A Shun Tak Centre (West Tower) 200 Connaught Road Central Sheung Wan Hong Kong
Company secretary:	Mr. Bai Yan (柏彥)
Authorised representatives:	Mr. Chen Wenli (陳文理) Mr. Bai Yan (柏彥)
Hong Kong share registrar and transfer office:	**Computershare Hong Kong Investor Services Limited** Shops 1712–1716, 17th Floor Hopewell Centre 183 Queen's Road East Wanchai Hong Kong
Principal bankers:	**Bank of China Hainan Branch** Meilan Airport Terminal Qiong Shan City Hainan Province PRC

The information provided here and elsewhere in this prospectus relating to industry background is derived in part from various official and unofficial publications and from communications with government officials. This information has not been prepared or independently verified by the Company, the Vendors, the Joint Sponsors or the Underwriters. None of the Company, the Vendors, the Joint Sponsors or the Underwriters make any representation as to the accuracy of this information, which may not be consistent with other information compiled within or outside the PRC, and accordingly the information contained herein may not be accurate and should not be unduly relied upon.

OVERVIEW OF GLOBAL AND REGIONAL AVIATION INDUSTRY

Global aviation industry

The global aviation industry has experienced significant growth in demand for both passenger and cargo services over the past decade. From 1990 to 2001, the global number of passengers carried increased by a compound annual growth rate of 3.0% while growth in global freight, expressed in tonnes, increased by a compound annual growth rate of 3.9%. Total passengers carried grew constantly from 1990 to 2001, interrupted by the Gulf War in 1991 and the 11th September terrorist attacks in 2001.

Development of World Scheduled Revenue Traffic of Scheduled Airlines of ICAO Contracting States from 1990 to 2001

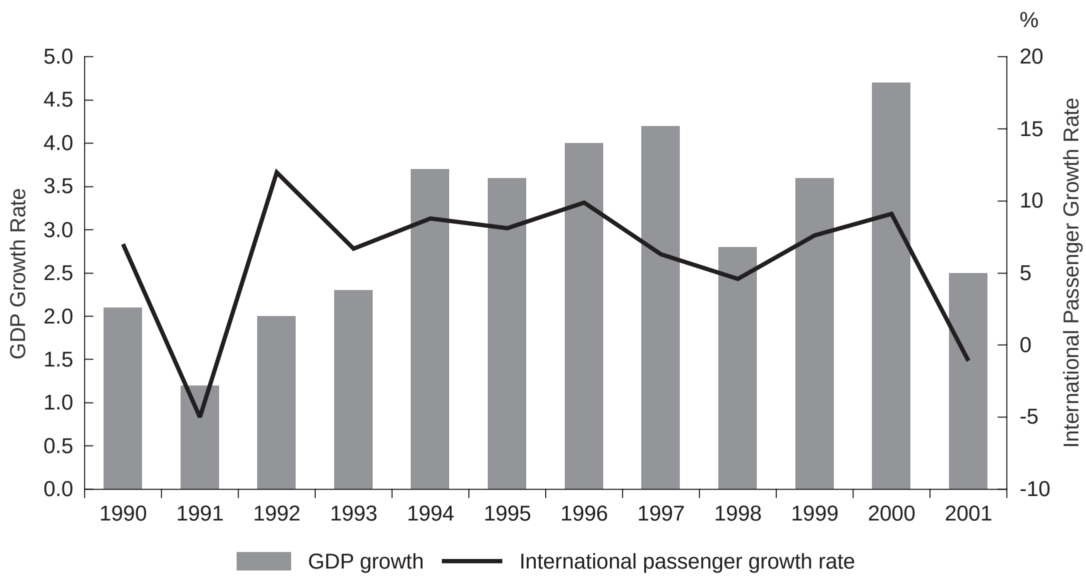
Year	Passengers Carried	Passenger Traffic (passenger kilometres)	Freight tonnes Carried	Cargo and Mail (tonne kilometres)	Total Traffic (tonne kilometres)
			(in millions)		
1990	1,165	1,894,000	18.40	64,130	235,220
1991	1,135	1,845,000	17.50	63,630	230,720
1992	1,146	1,929,000	17.60	67,770	242,140
1993	1,142	1,949,000	18.10	73,680	250,630
1994	1,233	2,100,000	20.50	82,630	273,420
1995	1,304	2,248,000	22.20	88,760	293,930
1996	1,391	2,432,000	23.20	95,000	317,150
1997	1,457	2,573,000	26.40	108,870	344,190
1998	1,471	2,628,000	26.50	107,580	348,600
1999	1,562	2,798,000	28.10	114,380	370,420
2000	1,656	3,017,000	30.10	124,010	401,170
2001[1]	1,621	2,930,000	28.10	115,960	385,370

(1) ICAO provisional estimates issued in May 2002

Source: ICAO (May 2002)

Strong correlation exists between the global economic climate (as measured in annual GDP growth) and the annual growth in international passenger traffic. In 2000, international passengers carried increased by 9.1%, the highest rise since 1996, fuelled by world GDP growth of 4.7%, reaching its highest level since 1990.

Correlation of International Passenger Growth Rate and GDP Growth from 1990 to 2001[1]



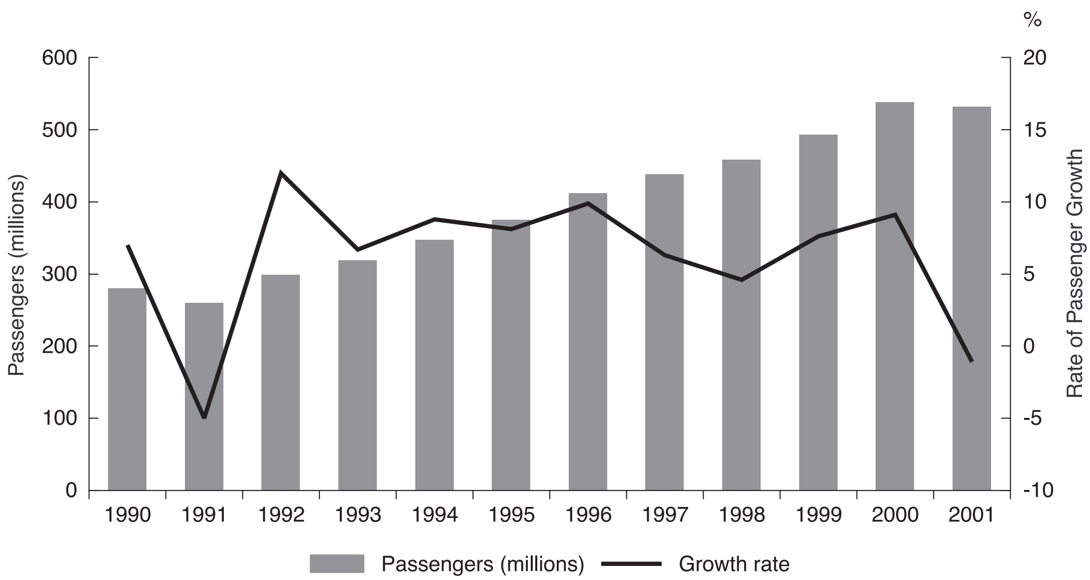
(1) 2001 international passenger growth rate is ICAO provisional estimate issued in May 2002

Sources: IMF World Economic & Financial Surveys (May 2000, April 2002), ICAO (May 2002)

There have been two periods in the past ten years when the airlines of ICAO's contracting states recorded a collective decline in passenger kilometres and cargo tonnage. The 1991 Gulf War was the first period of contraction, when international passenger traffic dropped by 5.0%. The industry soon recovered in 1992 when international passenger kilometres traffic rose to 982 billion passenger kilometres, exceeding the levels recorded in both 1990 and 1991.

The second period of contraction in the past decade started in early 2001 with the beginning of a worldwide economic downturn. The terrorist attacks in the US in September of 2001 accelerated the decline of an already fragile world economy. The number of international air passengers fell by 1.1% while global GDP growth in 2001 was only 2.5%, nearly half of the level in 2000. Each of the major regional airline associations reported significant negative impact of sluggish economy on their member carriers. The Air Transport Association of America reported a combined (domestic and international) passenger traffic decline of American carriers of 35%, 26%, 22% and 14% in September, October, November and December of 2001, respectively, over the same months of 2000.

Evolution of Scheduled International Passengers Traffic from 1990 to 2001[1]



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[1] 2001 international passenger figures are ICAO provisional estimates issued in May 2002

Source: ICAO (May 2002)

Regional aviation industry in Asia

The aviation industry in Asia has experienced considerable growth over the past decade, with increased demand for airport capacity. There have been new airport construction projects or major airport renovation projects in Hong Kong, Kuala Lumpur, Bangkok, Seoul, Shanghai Pudong and Beijing over the past five years. The new airport in Guangzhou is expected to commence operations in 2003. From 1998 to 2000, passenger traffic increased by 12% at major Asian airports in general, with more significant growth at airports in Beijing (25%), Seoul (25%), Pusan (23%), Jakarta (21%) and Singapore (20%).

For the twelve months ended 31st March, 2001, passenger traffic within the Asia-Pacific region amounted to approximately 70 million while cargo transport within the Asia-Pacific region totalled 3,331,983 tonnes. Passenger traffic to and from other regions amounted to 27,687,337 and cargo transport totalled 2,395,989 tonnes in the same period. Major traffic flows to or from Asia take Europe and North America as point of departure or destination. Of the total amount of inter-regional passenger and cargo traffic, 48% and 52%, respectively, were from or to North America; 38% and 35%, respectively, were from or to Europe; 10% and 7%, respectively, were from or to the Indian sub continent; 2% and 5%, respectively, were from or to the Middle East and 2% and 1%, respectively, were from or to Africa. Within Asia, the trade partners with the most passenger traffic for the twelve months ended 31st March, 2001 were Japan-Korea, Taiwan-Hong Kong and Taiwan-Japan with 6,121,350, 5,373,508 and 3,212,091 passengers, respectively.

	Passenger Traffic		Cargo Traffic (tonnes)	
Region of Origin or Destination	**April 1999–March 2000**	**April 2000–March 2001**	**April 1999–March 2000**	**April 2000–March 2001**
Intra-Asia Pacific	**63,836,824**	**70,001,849**	**3,198,916**	**3,331,983**
To/from Asia Pacific	**25,227,359**	**27,687,337**	**2,274,813**	**2,395,989**
North America	12,073,107	13,165,149	1,188,821	1,245,648
Europe	9,481,356	10,584,215	801,471	849,920
Indian Sub. Cont	2,473,145	2,687,535	143,178	164,541
Middle East	673,202	683,944	120,930	116,345
Africa	526,549	566,494	20,413	19,535
Grand Total	**89,064,183**	**97,689,186**	**5,473,729**	**5,727,972**

Sources: Statistical Report 2001, Association of Asia Pacific Airlines, which collects and publishes data for the annual period from 1st April to 31st March of next year

Air traffic in Asia is not immune to the global aviation industry slowdown after the terrorist attacks in the U.S. in September 2001. However, air traffic in Asia has recovered since the attacks. Airline passenger traffic in China experienced an overall increase of 12% in 2001 compared to 2000 and the first eight months of 2002 saw passenger traffic jump 11% over the same period last year.

The following table gives an overview of air traffic at certain airports in the Asia Pacific region in 2001.

Comparison of Certain Airports in the Asia-Pacific region 2001

Airport	Commercial passengers	Cargo (tonnes)	Aircraft movements
	('000)	*('000)*	*('000)*
Tokyo–Haneda	58,693	725	270
Hong Kong	32,553	2,100	208
Bangkok	30,624	843	201
Singapore	28,094	1,530	190
Tokyo–Narita	25,379	1,681	132
Sydney	24,303	517	292
Beijing	24,176	587	222
Osaka–Kansai	19,342	871	123
Taipei	18,461	1,190	124
Melbourne–Tullamarine	17,020	N.A.	178
Kuala Lumpur	14,707	446	114
Seoul–Incheon	14,384	1,197	87
Guangzhou	14,276	532	137
Shanghai–Hongqiao	13,861	452	116
Brisbane	13,098	N.A.	169
Manila	12,619	357	177
Mumbai	11,614	296	112
Jakarta	11,613	289	121
Cheju	9,320	290	61
Pusan	9,248	168	67
New Delhi	8,727	238	84
Auckland	8,354	186	145
Kaohsiung	8,285	89	95

Source: Air Traffic Intelligence, 2002

GROWTH IN AIR TRANSPORTATION IN CHINA

China has experienced unprecedented economic growth during the past decade, with real GDP increasing at a compound annual growth rate of 9.9%. This economic development has been accompanied by growth in China's transportation sector. As illustrated in the table below, air transportation has seen the most dramatic growth compared to more traditional modes of transport such as highways and rail. From 1991 to 2001, air passenger traffic (in terms of passenger kilometres) increased at a compound annual growth rate of 13.7% compared to 9.6% for highway passengers and 5.4% for rail passengers. Similarly, freight traffic (in tonne kilometres) carried by air increased at a compound annual growth rate of 15.8% during the same period, compared to 6.3% for highways and 2.9% for rail.

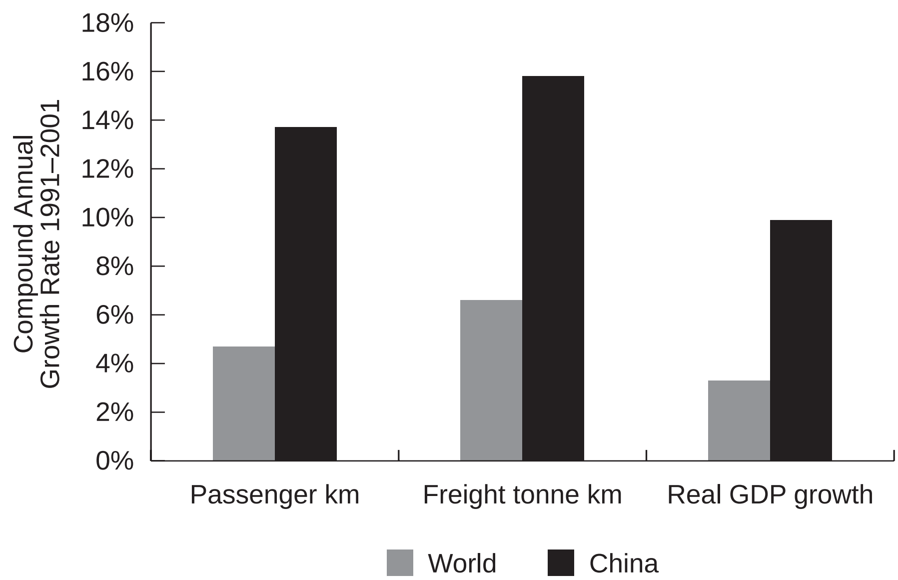
Passenger and Freight Traffic (Rail, Highways and Air) in China from 1990 to 2001 (million)

	Rail		Highways		Air	
Year	Passenger (kilometres)	Cargo (tonne kilometres)	Passenger (kilometres)	Cargo (tonne kilometres)	Passenger (kilometres)	Cargo (tonne kilometres)
			(in millions)			
1990 . .	261,260	1,062,240	262,030	335,810	23,048	818
1991 . .	282,810	1,097,200	287,170	342,800	30,132	1,010
1992 . .	315,220	1,157,560	319,260	375,540	40,612	1,342
1993 . .	348,330	1,195,460	370,070	407,050	47,760	1,661
1994 . .	363,610	1,245,750	422,030	448,630	55,158	1,858
1995 . .	354,570	1,287,030	460,310	469,490	68,130	2,230
1996 . .	334,760	1,304,440	490,880	501,120	74,784	2,493
1997 . .	358,490	1,325,330	554,140	527,150	77,352	2,910
1998 . .	377,340	1,251,710	594,280	548,340	80,024	3,345
1999 . .	413,600	1,283,840	619,920	572,430	85,728	4,234
2000 . .	453,260	1,390,210	665,740	612,940	97,054	5,027
2001 . .	476,700	1,457,500	720,700	633,000	109,101	4,370

Sources: China Statistical Abstract, 2002; China Statistical Year Book, 2001; Statistical Data on Civil Aviation of China, 2001

China's commercial aviation industry has directly benefited from the country's rapid economic growth and the reform and opening policy adopted by the Chinese government. Higher national income has made air travel more affordable. Economic reform has significantly increased the demand for business travel and transportation of goods. The following chart illustrates the growth in GDP and aviation in China, as compared to the world as a whole.

Growth in GDP and Aviation Industry in China



Sources: IMF World Economic & Financial Surveys (May 2000, April 2002), China Statistical Abstract, 2002, Statistical Data on Civil Aviation of China, 2001, China Statistical Year Book, 2001.

As China becomes increasingly modernised and fast-paced and air travel becomes affordable, people attach higher importance to time and increasingly favour air travel over more traditional means of transport. Economic liberalisation, rising consumer income and the opening of China to the rest of the world have also resulted in the rapid growth in domestic and international tourism, international trade and cultural exchanges, all of which have contributed to the growth in China's civil aviation industry. The table below illustrates the growth in air traffic volume for passengers, cargo and mail from 1990 to 2001.

Air Traffic in China from 1990 to 2001

Year	Passengers Carried	Passenger Traffic (passenger kilometres)	Cargo, Baggage and Mail[1] (tonnes)	Cargo, Baggage and Mail (tonne kilometres)	Total Traffic[2] (tonne kilometres)
			(in million)		
1990	16.6	23,048	0.370	818	2,500
1991	21.8	30,132	0.452	1,010	3,207
1992	28.9	40,612	0.575	1,342	4,285
1993	33.8	47,760	0.694	1,661	5,118
1994	40.4	55,158	0.829	1,858	5,841
1995	51.2	68,130	1.011	2,230	7,144
1996	55.6	74,784	1.150	2,493	8,061
1997	56.3	77,352	1.247	2,910	8,668
1998	57.6	80,024	1.400	3,345	9,297
1999	60.9	85,728	1.704	4,234	10,611
2000	67.2	97,054	1.967	5,027	12,250
2001	75.2	109,100	1.710	4,370	14,120[3]

(1) Year 2001 is the first year CAAC applied international standard to calculate cargo volume, which does not include passenger luggage. Should this method have had applied in the years prior to 2001, the total cargo volume for those years would have been lower than the numbers shown in the table.

(2) Total tonnage of passengers, cargo, baggage and mail carried by aircraft multiplied by total distance travelled in kilometres.

(3) CAAC, July 2002.

Sources: Statistical Data on Civil Aviation of China, 2001, China Statistical Abstract 2002

Number of Air Routes within, to and from China

Year	Domestic	International	Hong Kong and Macau[1]
1990	385	44	8
1991	395	49	8
1992	492	58	13
1993	563	71	13
1994	630	84	13
1995	694	85	18
1996	757	98	21
1997	851	109	7
1998	983	131	8
1999	987	128	22
2000	1,032	133	42
2001	1,009	134	42

Source: Statistical Data on Civil Aviation of China, 2001, China Statistical Abstract 2002

(1) Domestic routes have included routes from Mainland China to HK since 1997, and routes from Mainland China to Macau since 1999.

In 2001, Chinese airlines operated a total of 1,185 air routes, including 1,009 domestic air routes, 134 international air routes and 42 routes flying to and from Hong Kong and Macau. Over the past 10-year period, the number of international routes has more than tripled.

The total number of aircrafts operated by domestic commercial airlines in China has increased from 499 as at 31st December, 1990 to 1,031 as at 31st December, 2001.

AIRPORTS IN CHINA

The high level of air traffic growth has created significant demand for airport services in China. As a result, a number of airports have been constructed or expanded during the past 10 years. These include the airports in Beijing, Shanghai Pudong, Guangzhou, Shenzhen, Nanjing, Wuhan, Fuzhou, Xiamen, Kunming and Zhuhai.

The Meilan Airport is one of the busiest airports in southern China by passenger throughput and aircraft movements. Nationally, it ranked eighth according to passenger throughput, thirteenth according to mail and cargo throughput and ninth according to aircraft movements in 2001.

Passenger, Mail and Cargo Throughput and Aircraft Movements in 2001 of Major Civil Airports in China

Airport	Passenger Throughput	Rank	Mail and Cargo Throughput (tonnes)	Rank	Aircraft Movements	Rank[(1)]
	('000)		*('000)*		*('000)*	
Beijing	24,176	1	591	1	221	1
Guangzhou	13,829	2	456	2	137	2
Shanghai Hongqiao	13,761	3	452	3	116	3
Shenzhen	7,775	4	212	5	88	4
Shanghai Pudong	6,899	5	353	4	78	5
Kunming	6,447	6	108	7	71	6
Chengdu	6,245	7	143	6	67	7
Haikou Meilan	**5,079**	**8**	**54**	**13**	**54**	**9**
Xian	4,072	9	55	12	61	8
Xiamen	3,587	10	78	8	44	11
Chongqing	3,193	11	65	10	41	12
Country Total	148,737		3,392		1,941	

(1) Excluding the Luoyang Airport where most aircraft movements are attributable to training of pilots in landings and take-offs of aircraft.

Source: Statistical Data on CAAC Journal, 2002

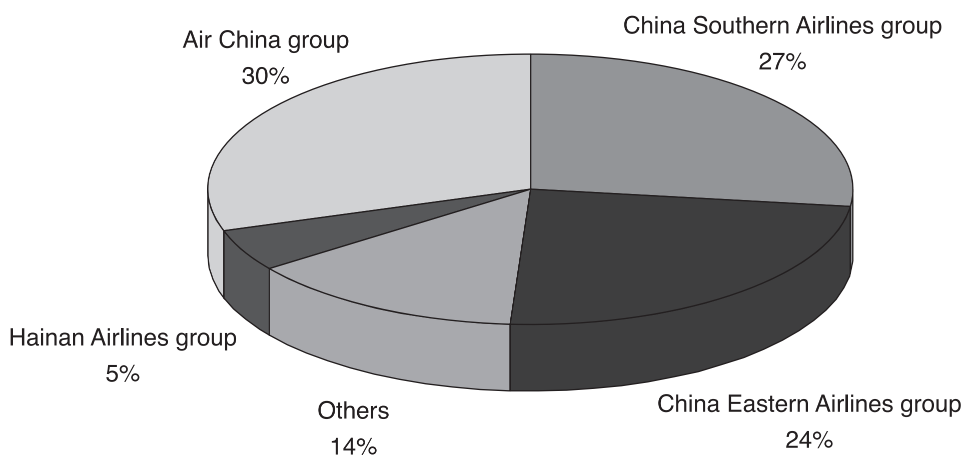
CHINESE AIRLINES

From 1949 until the mid-1980s, the Chinese civil aviation industry, including all passenger, cargo and mail air services within China, was operated by the Chinese government through CAAC. All commercial aircrafts used in China were then owned and leased by CAAC. After the restructuring of the Chinese civil aviation in 1986, CAAC ceased the direct management of the day-to-day operations of the airlines and responsibilities were transferred to six newly-established commercial airlines, namely, Air China, China Southern Airlines, China Eastern Airlines, China Southwest Airlines, China Northwest Airlines and China Northern Airlines. In the subsequent years, more airlines were established, under the supervision of either CAAC or other government entities. Currently there are a total of 22 domestic commercial airlines opened and registered in China.

In early 2002, the State Council approved an airline consolidation plan to establish three large airline groups led by the three major carriers — Air China, China Southern Airlines and China Eastern Airlines. In October 2002, the holding companies of the three groups were incorporated. Yunnan Airlines, China Northwest Airlines and China Eastern Airlines formed the China Eastern Airlines group, China Northern Airlines, China Xinjiang Airlines and China Southern Airlines formed the China Southern Airlines group, and China Southwest Airlines, China National Aviation Corporation and Air China formed the Air China group. The three airline groups are proceeding to carry out the asset restructurings necessary to give effect to the consolidation plan.

As illustrated in the chart below and assuming completion of the airline consolidation as announced by CAAC, the Chinese civil aviation industry would have been dominated by three airlines group in terms of total traffic tonne kilometres, with a total market share of approximately 81% in 2001.

Percentage of Total Traffic Tonne Kilometre by Chinese Airlines in 2001
(Assuming Airline Consolidation)



Source: CAAC, May 2002, market shares taking into account the consolidation of airlines announced by CAAC.

Regulatory Authority and Its Structure

The civil aviation industry in China is under the supervision of CAAC. CAAC was first established in 1949. CAAC was separated from the Air Force of the People's Liberation Army in 1980 and has come under the direct supervision of the State Council. At present, CAAC has 12 administrative departments responsible for managing different aspects of the civil aviation industry in China. CAAC also has seven regional administrations, each of which has its own air traffic control bureau responsible for air traffic control, communications, radar operation, navigation, meteorological information and aeronautical information services in seven different segments of the airspace in China to maintain order, safety and efficiency of air traffic and assist in rescue operations.

As China is a contracting state of the Chicago Convention, the rules and regulations relating to civil airports in China are required to be consistent with the Chicago Convention and to incorporate the international standards established by ICAO.

In China, the Civil Aviation Law promulgated in 1995 is the major national legislation governing air transport in China. This comprehensive legislation provides for the regulatory framework and rules covering a variety of matters, such as air traffic control and safety, airlines, aircraft and airports in China. CAAC derives its regulatory power from the Civil Aviation Law and directives of the State Council.

Regulations by CAAC

Administrative rules and regulations formulated by CAAC (by itself or together with other departments) govern certain aspects of civil airports including technical standards of airfield and terminal facilities, aviation safety, air traffic control and airport management, construction and finance. In addition, CAAC sets standards and guidelines for aeronautical fees and ground handling service fees jointly with MOF and SDPC and oversees airport construction. To ensure airports' compliance with safety, quality and other standards and requirements, each airport in China is required to obtain an airport operating permit from CAAC.

Fees

The scale of aeronautical fees that civil airports in China may charge for the use of their facilities are prescribed or set as guidelines by CAAC jointly with MOF and SDPC. There are currently two sets of fee scales, applicable to flights operated by domestic airlines and foreign airlines, respectively. The charge rates payable by domestic airlines are generally less than those payable by foreign airlines. Further, fees charged to foreign airlines are uniformly applicable to all airports while those charged to domestic airlines vary according to the class of the airports, which is determined based on passenger throughput, aircraft movement and the category of the runway.

CAAC, in conjunction with MOF and SDPC, review and revise aeronautical fee levels from time to time, although such reviews and revisions are not conducted at a fixed time interval. The most recent adjustments of aircraft movement and ground handling fees for domestic airlines took place in 1989, 1992 and 2002. Recent adjustments of charges for aircraft movement and related fees for foreign airlines took place in 1991 and 1995, respectively, each time resulting in an increase in average fee levels of up to 20%. The most recent adjustment of the ground handling fee levels for foreign airlines took place in 1994, which resulted in an increase of approximately 40% of average fee levels.

In addition to aeronautical fees, CAAC also, by way of guidance only, sets the level of fees for leasing of counters at airports. Unlike aeronautical fees, which are prescribed by CAAC and must be adhered to by airports, guidance rates of the fees for leasing allow for up to 20% deviations to be negotiated between an airport and its tenants.

Lease rates for commercial spaces such as retail and restaurants are market driven and not subject to regulation.

Construction, expansion and renovation of airports

CAAC, in conjunction with other relevant State Council departments, formulates comprehensive plans for the development and construction of civil airports in China (the "Master Plans") with a view to optimising air transportation services. Provincial and local governments are empowered to formulate their own plans for the construction of civil airports within their own administrative regions. All these plans for construction must be approved by CAAC. The Civil Aviation Law requires that any new construction or expansion of civil airports conform to the Master Plans and meet the technical, safety, environmental and other standards and requirements for civil airports.

Safety

The State Council, CAAC and other relevant government bodies have issued various regulations which aim at ensuring smooth operation of airports and protecting human life and property in or around the airports. The safety-related aspects of these regulations include:

- designation of clearance areas in the vicinity of an airport prohibiting high-rise buildings or any other facilities or structures which may affect airport communications and navigation;
- safety standards of all-weather operation of civil aircraft;
- prevention of any interference originated from the ground which is harmful to air traffic;
- security check in every airport; and
- safety of airport users, properties and civil aircraft.

Policies on foreign investors

Pursuant to the latest Catalogue for the Guidance of Foreign Investment Industries jointly promulgated by SDPC, SETC and MOFTEC on 11th March, 2002 and the regulations effective on 1st August, 2002 issued jointly by CAAC, MOFTEC and SDPC on the policies concerning foreign investment in the PRC civil aviation industry, foreign investment in the construction and operation of PRC civil airports falls within the encouraged category, provided that the aggregate equity interest held by the Chinese party/parties in the project involving foreign investment is greater than the equity interest held by any foreign party in the project.

Route rights

The right of any Chinese airline to carry passengers or cargo on any domestic route must be obtained from CAAC. Non-Chinese airlines are generally not permitted to provide domestic air service in China. Hong Kong and Macau route rights, are derived from the air service arrangements between the PRC central government and the governments of Hong Kong and Macau Special Administrative Regions, respectively and are allocated by CAAC among designated Chinese airlines. International route rights are derived from air service arrangements/agreements negotiated between the Chinese government, through CAAC, and the government of the relevant foreign country.

Air fares

Air fares of Chinese airlines for domestic routes are set by CAAC and SDPC. Discount policies on air fares are also subject to the control of CAAC.

Air fares of Chinese airlines for Hong Kong and Macau routes must be approved by CAAC and the civil aviation authorities in Hong Kong and Macau. Airlines may at their discretion offer discounts on air fares for flights on their Hong Kong and Macau routes.

Air fares of Chinese airlines for international routes are determined through consultation between the relevant Chinese airlines and foreign airlines in accordance with the civil aviation agreements between the Chinese government and the relevant foreign government, taking into account the international air fare standards established through IATA. All air fares of Chinese airlines for international routes must be approved by CAAC. Discounting of approved international air fares is permitted at the airlines' discretion.

Air traffic control

CAAC is responsible for air traffic control of civil aviation in China. After an aircraft enters into a defined airspace in China, it is subject to the direction of the air traffic control centre of the responsible regional administrative bureau of CAAC and, when approaching an airport for landing, it is subject to the direction of the relevant bureau's control tower at such airport.

The airspace above Hainan Island is within the jurisdiction of SCATC which also owns the control towers at the Meilan Airport and the Sanya Airport.

Other regulations

Environmental protection

Although there is no specific set of airport environmental regulations, airports in China are required to comply with the general environmental requirements under the Environmental Protection Law and other specific requirements in respect of noise, air, water and waste pollution under laws and regulations including the Noise Pollution Prevention Law, Air Pollution Prevention Law, Water Pollution Prevention Law and Solid Waste Pollution Prevention Law, respectively. According to these laws, an enterprise which emits pollutants in excess of the relevant standard is required to pay waste discharge fees. An enterprise which causes serious environmental pollution will be given a limited time to rectify. Penalties for non-compliance include fines, administrative sanctions and suspension or ceasing of production or business.

Duty-free shops

The operation of the duty-free shops at civil airports is subject to supervision and regulation by China Duty-Free Corporation, a state-owned enterprise chartered by the State Council. China Duty-Free Corporation controls such aspects of the duty-free shop's operations as merchandise selection and sourcing. China Duty-Free Corporation also provides suggested prices for duty-free items. The operator of the duty-free shops may offer discounts from the suggested retail prices.

INTRODUCTION

Hainan Province is situated in the southernmost part of China and Hainan Island is the only developed tropical island in China, which is well known for its tourist attractions. Hainan Province is divided into nine municipalities and 10 counties, totalling 34,000 square kilometres of land area and two million square kilometres of sea area.

As at the end of 2001, the population in Hainan was 7.7 million. Hainan is a well-known ancestral home of many ethnic Chinese now residing overseas. Nearly two million Chinese in Hong Kong, Macau and Taiwan and one million ethnic Chinese around the rest of the world have their family roots in Hainan.

Bo'ao, a city located in the eastern part of Hainan Island and 104 kilometres from Haikou, has become a domestic and international convention centre. The Bo'ao Forum for Asia was founded in February 2001 to prompt economic exchanges and cooperation within the region and the city has since hosted an Association of South East Asian Nations ("ASEAN") conference and a meeting of the 21st Century Committee for Sino-Japan Friendship.

Hainan Island is also the home base of Hainan Airlines. Hainan Airlines provides scheduled and chartered flights to more than 60 domestic and overseas destinations, including Hong Kong, Macau, Singapore, Malaysia and Thailand.

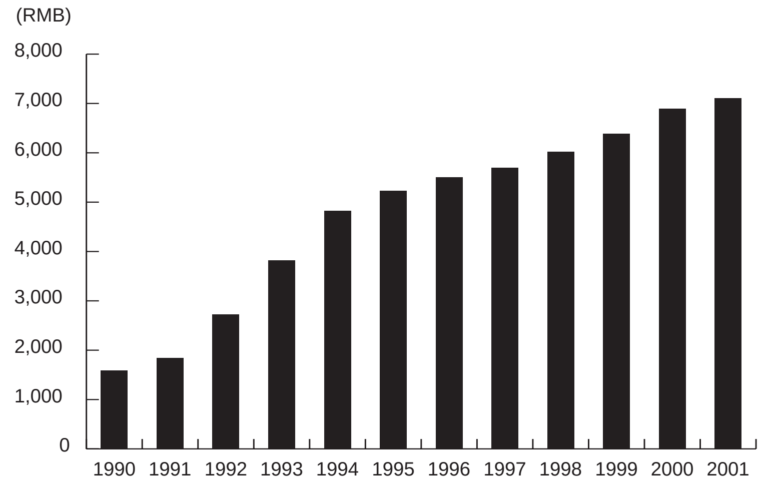
HAIKOU

Haikou, the capital city of Hainan Province, is located at the north end of Hainan Island, with a total area of 244.6 square kilometres and the central business district area of 34 square kilometres. Haikou had a population of approximately 602,012 in 2001. According to Hainan Statistical Yearbook 2002 and the Hainan Yearbook 2001, in 2001, Haikou's GDP amounted to RMB14.6 billion, representing a 9.0% increase over 2000, and its GDP per capita in 2001 was RMB24,782. According to Hainan Statistical Yearbook 2002, the city received 2.9 million tourists staying in designated hotels in Haikou in 2001, a 15.6% increase over the level in the previous year. In 2001, tourism-related revenues reached RMB2.77 billion, 6.73% higher than that of 2000.

ECONOMIC DEVELOPMENT

Hainan Island is the country's largest special economic zone. For four years from 1998 to 2001, Hainan Province recorded a higher economic growth than the national average. According to the Hainan Statistical Yearbook 2002, in 2001, Hainan Province recorded GDP of RMB56.7 billion, an 9.3% increase over the previous year. In the first six months of 2002, Hainan Province registered a 9.4% growth in GDP over the same period of last year. The volume of foreign trade increased by 36.8% to RMB14.6 billion in 2001. Hainan's key exports include agricultural products, seafood, natural gas, jewelry, textiles and natural rubber.

Hainan GDP Per Capita



Source: Hainan Statistical Yearbook 2002

Hainan Island has large amount of natural resources reserves. Its inland and offshore oil and natural gas reserves rank among the highest in China. Hainan has potential oil reserves of 29.1 billion tons and gas reserves of 5.8 trillion cubic metres. It provides 2.9 billion cubic metres of gas annually to Hong Kong through a 770-kilometre-long pipeline. Hainan's titanium reserves represent 70% of the national total. Yinggehai salt field is one of the major salt fields in China.

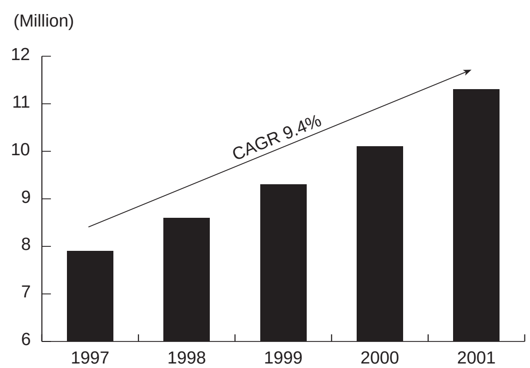
Hainan's tropical climate yields an abundance of tropical crops such as coconuts, pepper, coffee and tea. The island is one of the most important tropical fruit production bases, seeds-breeding bases and rubber production bases in the country. Hainan Province also plays a significant role in the production of herbal medicines in the country.

TOURISM INDUSTRY AND HOLIDAY TRAVEL

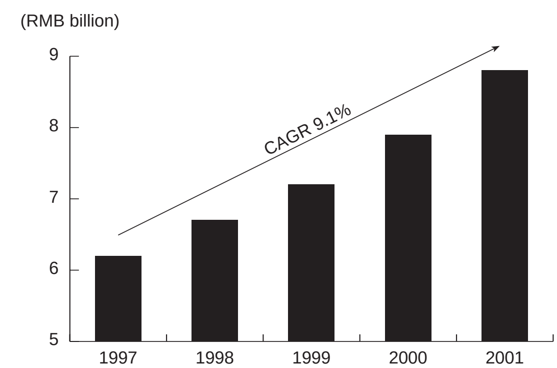
Hainan Island extends 290 kilometres from northeast to southwest and 180 kilometres from northwest to southeast. The coastline is about 1,528 kilometres long with 68 bays along the seashore. Fifty to sixty percent of its seashore comprises sandy beaches, most of which are several hundred to 1,000 metres wide, well suited for holiday resorts and tourism. Eighty-one mountains on the Hainan Island are over 1,000 metres above the sea level, most of which are covered by forests. Wuzhi Mountain, Yingga Mountain and Dongshang Mountain are among the best-known inland tourist attractions.

Hainan Island has a monsoon tropical climate with annual average temperatures ranging from 22°C to 26°C and annual rainfall of 1,500 to 2,000 mm. The island enjoys sunshine more than 300 days a year. Known as the "Hawaii of China", Hainan is a popular destination for holidays and travel. The province has been capitalising on its geographic and climatic advantages to develop tourism into a booming industry.

Tourists



Tourists Revenue



Source: Hainan Statistical Yearbook 2002

In 2001, the number of person-visits to Hainan Island increased by 11.6% to reach 11.2 million. One person-visit is recorded when one tourist checks into a hotel. Revenue from the tourism industry amounted to RMB8.8 billion, representing a 11.8% increase over the previous year, while the nationwide growth rate was 10.5% for the same period.

Short term travels over major holiday seasons and summer/winter camps attract the largest number of tourists in China. The aggregate number of person-visits during the Chinese New Year, Labor Day and National Day holidays reached 1.37 million in 2001, representing a 50.6% growth over the previous year and resulting in an inflow of RMB1.3 billion tourism-related revenues. Major hotels have been building resorts throughout the island, targeting higher-income tourist customers.

In 2000, the Provincial Tourism Bureau launched "Hainan Province Travel Industry Five-Year Plan" and "2020 Long Term Strategic Development Programme", aiming to make Hainan one of the best tropical tourist destinations in Asia. The Provincial Tourism Bureau projected that there would be around 75 million person-visits to Hainan Island in 2020, generating RMB55 billion in total tourism-related revenues, including US$1.8 billion from foreign visitors.

In conjunction with its focus on promoting tourism, the provincial government has also been taking steps in raising the awareness of environmental protection and fostering a legal framework for sustainable development of the island. The provincial government has designated five tropical forest areas as special preservation zones. In addition, Hainan was the first province in China to implement Regulations of Tourist Management for protecting the rights of tourists.

INTRODUCTION

The Group operates the Meilan Airport, the main gateway to the Hainan Island. Trial operations at the Meilan Airport commenced on 28th March, 1999 and commercial operations commenced on 25th May, 1999. For the period starting from the commencement of commercial operations to 30th September, 2002, the Meilan Airport experienced significant growth in terms of aircraft movement, passenger throughput and cargo throughput, as shown by the following table:

Annual Aircraft Movements, Passenger Throughput and Cargo Throughput of the Meilan Airport

	Year ended 31st December,			Five months ended 31st May,		Nine months ended 30th September,	
	1999[(1)]	2000	2001	2001	2002	2001	2002
	('000)	*('000)*	*('000)*	*('000)*	*('000)*	*('000)*	*('000)*
Aircraft movements	30.7	56.8	53.8	24.5	27.2	40.9	45.2
Change as compared to the same period in the previous year *(%)*	—	—	(5.3)	—	11.0	—	10.5
Passenger throughput	2,202	4,363	5,079	2,245	2,563	3,845	4,214
Change as compared to the same period in the previous year *(%)*	—	—	16.4	—	14.2	—	9.6
Cargo throughput *(tonnes)*[(2)]	36.1	71.1	73.6	33.1	36.2	55.8	57.0
Change as compared to the same period in the previous year *(%)*	—	—	3.6	—	9.3	—	2.1

(1) Commercial operations of the Meilan Airport commenced on 25th May, 1999. Accordingly, the relevant data for 1999 reflect only seven months of commercial operations and therefore are not directly comparable with those of the subsequent years.

(2) The figures include cargo, mail and passenger luggage throughput at the Meilan Airport.

The Meilan Airport is located approximately 25 kilometres from downtown Haikou, the provincial capital of Hainan Province. It has one runway, one Terminal and one cargo centre. The runway has been constructed in accordance with ICAO category 4E standards and is capable of accommodating landing and takeoff of Boeing 747-400 aircraft, the largest commercial airliner. The Terminal has an annual handling capacity of approximately six million passenger arrivals and departures. The Meilan Airport's cargo centre has an annual capacity of approximately 54,000 tonnes of cargo.

As at the Latest Practicable Date, the Group's airline customers included 18 domestic airlines and one airline from each of Hong Kong and Macau. As of 31st May, 2002, these airlines operated 197 domestic routes and a total of eight international routes, including Hong Kong and Macau, to and from the Meilan Airport. The Meilan Airport is the home base for Hainan Airlines.

The Group is engaged in both aeronautical and non-aeronautical businesses. Its aeronautical business consists of the provision of airfield services, through a revenue sharing arrangement with Parent Company, and provision of terminal facilities, ground handling services, passenger and cargo handling services. Its non-aeronautical business includes leasing of commercial and retail spaces at the Meilan Airport, airport-related business franchising, advertising, car parking, tourism services, and sales of duty-free and consumable goods. The non-aeronautical revenues, derived from cargo centre franchising, car parking, tourism services and duty-free sales which are the businesses and assets acquired from Parent Company pursuant to the Asset Swap Agreement effective 31st May, 2002, will be reflected in the Group's financial statements for periods subsequent to 31st May, 2002.

The Group's principal operating revenues for the three years ended 31st December, 2001 and the five months ended 31st May, 2002 are shown below:

	Year ended 31st December,			Five months ended 31st May,
	1999[1]	2000	2001	2002
	(RMB'000)			
Revenues				
Aeronautical[2]				
Passenger charges	41,766	90,371	102,283	50,584
Airport Fee	—	—	—	29,442
Ground handling services fee	10,091	18,371	20,556	10,644
Aircraft movement fees and related charges	5,642	10,661	10,198	5,138
Total aeronautical revenues	57,499	119,403	133,037	95,808
Non-aeronautical				
Leasing of commercial areas, counters and office in the Terminal	10,424	22,921	26,261	10,899
Franchise fee[3]	6,592	11,809	15,490	6,597
Advertising	3,530	5,087	4,018	2,021
Other revenues	2,437	2,423	6,195	3,162
Total non-aeronautical revenues	22,983	42,240	51,964	22,679
Total revenues	80,482	161,643	185,001	118,487

(1) Commercial operations of the Meilan Airport commenced on 25th May, 1999. Accordingly, the relevant data for 1999 reflect only seven months of commercial operations and therefore are not directly comparable with those of the subsequent years.

(2) The presentation of the historical figures throughout the Track Record Period for the following aeronautical revenues reflect the revenue sharing arrangement between the Company and Parent Company, on the basis of 75% to the Company and 25% to Parent Company:

- Aircraft movement fees;
- Passenger charges; and

- Basic ground handling services fees charged to Hong Kong, Macau and foreign airlines.

(3) The franchise fees for the Track Record Period consist of the following items:

- Annual fees from Hainan Food with respect to the air catering rights at the Meilan Airport;
- Annual fees from Hainan Airlines in 1999 and 2000 and from Parent Company in 2001 and the first five months of 2002 with respect to the right to operate the cargo centre at the Meilan Airport;
- Annual fees from THIA with respect to the right to sell accident insurance policies at the Meilan Airport; and
- Fees from HLAS with respect to air ticketing operation at the Meilan Airport.

BUSINESS STRATEGY AND STRENGTHS

Business Strategy

The Group's strategy is to focus on Haikou's unique position as the provincial capital and the main gateway to Hainan, the "Hawaii of China", and includes the following specific elements:

Prepare for anticipated increase in air traffic demand. According to Booz Allen Hamilton, the independent air traffic consultant, air traffic in terms of passenger throughput at the Meilan Airport is expected to increase by approximately 10.2% and 9.2% annually from 2001 to 2006 and from 2001 to 2011, respectively (please see Appendix V to this prospectus). To take advantage of the expected increase in air traffic, the Group plans to expand its current operating facilities. The current plan includes expanding the Terminal by approximately 30,000 m^2 and the apron area by approximately 280,000 m^2, adding 20 aircraft parking stands and eight air bridges.

Capitalise on its management expertise to create an airport management brand name and manage other airports. The management of the Group has considerable experience in operating airports and believes such experience can be utilised to the Group's benefit. The Group intends to build up its reputation as a premier airport management group in the PRC. The Sanya Management Contract in relation to the management of the Sanya Airport was signed with SPIA on 23rd August, 2002. Pursuant to this contract, the Group is responsible for the day-to-day management of the Sanya Airport, including its operations, finance, accounting, administration and investment activities, for five years commencing from 1st August, 2002. Please refer to the section headed "Business — Sanya Management Contract" of this prospectus.

Increase operation efficiency. The Group plans to improve its overall operating and financial performance and to carefully control its operating costs. By benchmarking its operating and financial performance metrics against those of leading international airport operators, the Group intends to identify and eliminate inefficiencies in its airport operations.

Increase non-aeronautical revenues. For each of the three years ended 31st December, 2001 and the five months ended 31st May, 2002, revenues from non-aeronautical businesses of the Group represented approximately 28.6%, 26.1%, 28.1% and 19.1% of the Group's total revenue. The Group plans to expand its non-aeronautical business in the areas of tourist services, franchising, sales of goods at the Terminal and other non-aeronautical activities. The Directors believe that the anticipated international airport status and expected higher number of international flights utilising the Meilan Airport will contribute to the continued growth of the Group's non-aeronautical operations.

Increase cargo throughput. The cargo throughput in 2001 increased by 3.6% over 2000. The growth of cargo throughput in the first five months of 2002 was 9.3% over the corresponding period of 2001. The Directors believe that cargo throughput at the Meilan Airport will grow significantly in the next several years. The Group plans to build a new cargo centre with a floor area of approximately 30,000 m^2, and a cargo apron with a total area of approximately 50,000 m^2.

Benefit from the Company's relationship with Hainan Airlines. Hainan Airlines, one of the Promoters of the Company, has its home base in the Meilan Airport. It is the fourth largest airline group in China in terms of total traffic tonne kilometres assuming completion of the airlines consolidation announced by CAAC in October 2002. Benefiting from this special relationship, the two companies can create synergies through resources sharing in the operations of the Meilan Airport and concerted marketing efforts in promoting Hainan Province as a popular tourist destination.

Obtain international airport status. The Group is seeking to obtain international airport status for the Meilan Airport from CAAC. To obtain such status, the Group must fulfil certain requirements relating to infrastructure and custom and inspection capacities. The Directors believe that, once the international airport status is obtained, international flights at the Meilan Airport and related revenues of the Group will increase, as the status of international airport will simplify the approval and operational process for airlines to set up international routes to and from the Meilan Airport. In anticipation of obtaining such status, a custom and inspection joint operation building located adjacent to the Terminal is under construction and expected to be completed by the end of 2002. The Directors believe that international airport status will, subject to further inspection before approval, be approved before the end of 2002.

The Group's Strengths

The Directors believe that the Group's operations benefit from the following factors:

Rapid growth of China's economy and air traffic. The demand for airport services is driven primarily by the volume of air traffic. Air traffic volume has been growing rapidly in China due to its strong economic and real income growth, increased mobility and rising popularity of tourism in the past 20 years. The Directors expect that more disposable income of the domestic population will be spent on travelling.

Strong growth of the tourism industry in Hainan. Hainan is the only tropical province in China. The well-known beaches and other tourist attractions have made Hainan Island one of the top tourist destinations in China attracting both domestic and international visitors. Currently the majority of visitors to Hainan are from domestic locations in China. In 2001, there were 11.3 million person-visits to Hainan Island, 10.8 million of which were generated by domestic travellers. Revenue from domestic tourism in 2001 amounted to RMB7,910 million, a 13.8% increase compared to that of 2000, while revenue from foreign tourism amounted to US$106 million, a decrease of 2.6% over the previous year. The top five sources of regional and international visitors are Hong Kong,Taiwan, Macau, Korea and Japan. Due to the relative ease of travel to Hainan for PRC residents, compared to foreign destinations where visa and other requirements pertain, Booz Allen Hamilton recently forecasted a substantial increase in domestic air passenger arrivals in Hainan in the near future. See Appendix V to this prospectus.

Aviation — a sensible transport solution for Hainan Island. Hainan Island is the largest tropical island of China with a population of approximately 7.7 million and a GDP of approximately RMB56.7 billion in 2001. Demands for air travel are increasing along with Hainan's popularity as a resort destination. Currently, the only other mode of transportation linking Hainan Island with the mainland is sea transportation. Aviation is a sensible transport solution for connecting the island with the rest of China.

Haikou — the main gateway to Hainan. As the capital city, Haikou is the centre of economic, cultural and political activities of Hainan Province. The Meilan Airport, situated approximately 25 kilometres from the city centre of Haikou, is well positioned to capture the economic benefits of Haikou's status. It is a gateway airport for people travelling to and from Hainan Province.

Market oriented management team. The management team has been involved in the management of Parent Company and the Group since the inception of the Meilan Airport. The Group has adopted a flexible management structure focusing on performance rather than seniority. The management comprises a number of young professionals who are familiar with modern corporate management style. This is complemented by the senior management team of the Group which has considerable experience in the civil aviation industry in China, including China's leading airlines, airports and the aviation regulators.

In 2001, out of all the airports in China, the Meilan Airport, along with Nanjing Lukou International Airport, Xiamen International Airport, Wuhan Tianhe Airport and Zhenzhou Xinchen International Airport, won the national-level "Consumer Satisfaction Award" organised by CAAC.

Good location, well-maintained runway and advanced facilities. The terrain where the Meilan Airport is located is flat and wide, making it a suitable site for an airport. There is adequate land supply for future expansion. The runway of the Meilan Airport was designed according to ICAO category 4E standards. It is 3,600-metre long, 44% longer than the ICAO specification of 2,500 metres as the required length for accommodating the maximum gross weight takeoff requirements of Boeing 747-400 aircraft. The runway's precision instrument markings, lighting and taxiways are all constructed according to ICAO category 4E standards. The category II precision instrument landing system at the west approach (the primary approach used by the majority of flights) provides for aircraft operations with 30-metre decision height and visibility distance of 400-metre while the category I precision instrument landing system at the east approach provides for 60-metre decision height and 800-metre visibility distance.

The Meilan Airport is also equipped with a flight information system and an automatic baggage handling system. An evaluation of these facilities is contained in the engineering consultants' report, a summary of which is set out in Appendix VI to this prospectus. Apart from these facilities, the Meilan Airport also has radar systems for air traffic control and weather monitoring, an aircraft repair and maintenance hangar and aviation fuel supply facilities.

Limited direct competition. The Meilan Airport is the primary airport serving Hainan Island. As such, the Group's core operations, namely the provision of airport services, face limited direct competition. The only other civil airport on Hainan is the Sanya Airport, which had a passenger throughput of nearly 1 million in 2001, representing approximately 20% of that of the Meilan Airport in the same period. The Company entered into the Sanya Management Contract on 23rd August, 2002 with SPIA under which the Company manages the Sanya Airport and receives management fees set at 1.5% of the annual operating revenue of the Sanya Airport and other compensations based on the improvement to the profitability of the Sanya Airport. Most of the Group's non-aeronautical operations, such as operating the duty-free shop and the car park, advertising and commercial leasing, do not face any direct competition.

Stable customer base. The revenues of the Group depend on the air traffic to and from Haikou, Hainan. Various airlines have established flights to and from Haikou. The Directors do not believe that the Group's prospects depend on the presence of any particular airline customer other than the Hainan Airlines and China Southern Airlines. With the projected growth in air traffic in and out of Hainan Province, the existing airline customers, including Hainan Airlines, China Southern Airlines and other major airlines in China, are expected to continue their presence at the Meilan Airport.

Good safety record. The Meilan Airport has not had any accidents involving aircraft, nor any accident resulting in loss of life or any significant personal injury or property damage since its inception. The Directors believe that the emphasis by CAAC, SCATC and the Group on proper safety training and the staff's continued efforts in focusing on safety matters have contributed to the Meilan Airport's safety record.

High growth potential in international flights. Based on the traffic forecast by Booz Allen Hamilton (see Appendix V to this prospectus), international aircraft movement at the Meilan Airport will have on average a compound annual growth rate of 20.6% for the next 10 years. The Directors believe that the Meilan Airport will be better positioned to respond to the increasing demand when the current expansion plan of the Terminal is implemented and the new cargo centre is built.

HISTORY AND DEVELOPMENT

The construction of the Meilan Airport commenced in November 1996 initially by Meilan International, a company established and wholly-owned by HAC, and was completed in February 1999. The Meilan Airport commenced commercial operation on 25th May, 1999 and ranked the eighth largest airport in China in terms of passenger throughput, the ninth largest in terms of aircraft movements and the thirteenth largest in terms of cargo throughput in 2001.

Parent Company was established on 25th August, 1998 by its promoters, namely Central South Bureau, Hainan Airlines, Hainan International Trust and Investment Company Limited and Aviation Oil, with a registered capital of RMB600 million and took over the development and construction of the Meilan Airport from Meilan International. The registered address of Parent Company is Meilan Airport, Qiong Shan City, Hainan Province, PRC. Each of Central South Bureau, Hainan Airlines, Hainan International Trust and Investment Company Limited and Aviation Oil held 50.0%, 33.4%, 8.3% and 8.3% equity interest in Parent Company, respectively. On 8th August, 2000, the registered capital of Parent Company increased to RMB1,350 million through further capital injection. Immediately following such further capital injection, the shareholders of Parent Company were Hainan Airlines, HNA Group, Central South Bureau, Hainan Asset Bureau, China

Southern Airlines and Aviation Oil and their shareholdings in Parent Company were approximately 30.0%, 28.1%, 22.2%, 8.6%, 7.4% and 3.7% respectively. In December 2000, the 8.6% stake held by Hainan Asset Bureau was allocated to Golden City pursuant to a directive issued by Hainan Asset Bureau (Qiong Guo Zi Wei [2000] No. 6).

An aggregate amount of approximately RMB283 million was collected by the Meilan Airport as Airport Fees during the period between May 1999 and December 2001. Pursuant to 《民航機場管理建設費管理辦法實施細則民航財發[1997]90號》 (The Implemental Rules of the Civil Aviation Airport Management Construction Fee Measures (Min Heng Cai Fa No. 90 (1997), the "**Implementation Rules**"), the entire Airport Fees collected are required to be remitted to MOF. According to the Implementation Rules and a letter issued by CAAC on 16th September, 2002, a total amount of approximately RMB141.6 million, representing 50% of the Airport Fees collected between 25th May, 1999 up to 31st December, 2001, was designated by CAAC as investment of the State in Parent Company. On 18th September, 2002, shareholders of Parent Company in general meeting passed resolutions to approve the equity investment of the State, and the allocation of the investment on the basis of RMB1.0345 per share to Golden City, Central South Bureau and Aviation Oil (all of which being wholly state-owned shareholders of Parent Company) in proportion to their then existing shareholdings. As a result of such investment, the registered capital of Parent Company will be further increased from RMB1,350 million to approximately RMB1,486.8 million, upon completion of relevant registration procedures. The registered capital will be held by Hainan Airlines, Central South Bureau, HNA Group, Golden City, China Southern Airlines, and Aviation Oil as to approximately 27.2%, 26.1%, 25.5%, 10.1%, 6.7% and 4.4% respectively.

RESTRUCTURING OF THE GROUP

In preparation for the Offering and the listing of H Shares on the Stock Exchange, the Company was established on 28th December, 2000 by Parent Company, HNA Group, Hainan Airlines, China Southern Airlines and Central South Aviation Development. Parent Company owns 95% of the Company, and has satisfied its capital contribution by injecting into the Company the Terminal, aprons, aircraft connection bridges, ground traffic control centre, fire fighting centre, emergency centre and certain other assets, while Hainan Airlines, HNA Group, China Southern Airlines and Central South Aviation Development respectively injected capital of approximately RMB6.9 million, RMB4.6 million, RMB1.2 million and RMB3.6 million into the Company in cash and own approximately 2.1%, 1.4%, 0.4% and 1.1% of the share capital of the Company, respectively. The value of the net assets injected by Parent Company amounted to RMB310.2 million, according to the valuation performed by Hainan Asset Valuation Company as described in its valuation report dated 8th November, 2000.

Asset Swap

To enhance the efficiency and integration of its business operations, Parent Company and the Company have undertaken further restructuring whereby the Company purchased four assets from Parent Company and sold three assets to Parent Company. Parent Company and the Company entered into the Asset Swap Agreement on 30th May, 2002, which was amended by a supplemental agreement on 25th October, 2002 to specify the terms of the asset swap.

The aeronautical business and assets purchased by the Company pursuant to the Asset Swap Agreement include:

— Assets of the cargo centre, valued at RMB42 million as of 31st December, 2001 based on the valuation report prepared by Hainan Zhong Li Xin dated 18th April, 2002. The Group believes that the cargo business in China, particularly in Hainan will grow rapidly in the next two decades. The acquisition of this business also has immediate positive financial impact on the Group. Although cargo-related operations and assets are traditionally categorised as aeronautical operations and assets, the revenues that the Company derived from the cargo centre at the Meilan Airport are in the form of franchise fee which is treated as a type of non-aeronautical revenue in the Company's consolidated financial statements.

The non-aeronautical business and assets purchased by the Company pursuant to the Asset Swap Agreement include:

— Car parking facilities, valued at RMB28.8 million as of 31st December, 2001 based on the valuation report prepared by Hainan Zhong Li Xin dated 18th April, 2002. Carpark business is generally regarded as an integral part of airport business.

— 60% of the registered capital in Meilan Travelling owned by Parent Company. Meilan Travelling is a travel agency which provides bus transportation services between the Meilan Airport and Haikou city and offers Hainan tour packages to visitors. As of 31st December, 2001, Meilan Travelling had total assets of RMB8.5 million and net assets of RMB7.1 million according to the valuation report prepared by Hainan Zhong Li Xin dated 18th April, 2002. Since air travel is an important means of travelling to Hainan, the Directors believe that tourism related services at the Meilan Airport have high growth potential. Parent Company holds the remaining 40% interest in the registered capital of Meilan Travelling.

— 95% of the registered capital in DFG owned by Parent Company. DFG operates the duty-free shop and other retail stores in the Terminal areas of the Meilan Airport. As of 31st December, 2001, DFG had total assets of RMB4.9 million and net assets of RMB263,487 according to the valuation report prepared by Hainan Zhong Li Xin dated 18th April, 2002. DFG operated stores are in both the international flight area and the domestic flight area of the Terminal at the Meilan Airport. The Directors believe that duty-free goods sales and retail business at the Terminal will benefit from projected growth in international and domestic passenger traffic.

The assets sold to Parent Company under the Asset Swap Agreement include:

— An equipment centre with a floor area of 3,974 m^2 and constructed area of 2,004 m^2, providing space for equipment water supply, electricity supply and central air conditioning services. As of 31st December, 2001, the equipment centre recorded a net book value of RMB10.72 million and was valued at RMB10.05 million (which comprised the equipment centre which was valued at RMB9.3 million based on the valuation report prepared by Hainan Zhong Li Xin dated 26th May, 2002 and the underlying land which recorded a net book value of RMB0.75 million).

— Various back up power generation, transformation and transmission equipment housed in the Terminal and equipment centre. As of 31st December, 2001, the equipment recorded a net book value of RMB8.3 million and was valued at RMB8.8 million based on the valuation report prepared by Hainan Zhong Li Xin dated 26th May, 2002.

— Vehicle storage with a floor area of 25,398 m^2, and constructed area of 3,470 m^2 providing storage space for airport vehicles, special vehicles and spare parts. As of 31st December, 2001, the vehicle storage recorded a net book value of RMB9.4 million and was valued at RMB9.4 million (which comprised the vehicle storage which was valued at RMB4.6 million based on the valuation report prepared by Hainan Zhong Li Xin dated 26th May, 2002 and the underlying land which recorded a net book value of RMB4.8 million).

The above three assets sold to Parent Company relate to ancillary operations with supporting functions. Since they are non-revenue generating facilities and necessary to enable Parent Company to provide the airport composite services to the Company under the Airport Composite Services Agreement (please see “Connected Transactions” of this section), the Directors believe it is in the best interest of the Company to sell these facilities to Parent Company.

The assets were purchased by the Company under the Asset Swap Agreement for a total consideration of approximately RMB78.1 million, which was based on the valuation report prepared by Hainan Zhong Li Xin dated 18th April, 2002. The assets sold from the Company to Parent Company under the Asset Swap Agreement were valued based on the valuation report prepared by Hainan Zhong Li Xin dated 26th May, 2002, at approximately RMB28.2 million in total and were sold for a total consideration of approximately RMB28.4 million. 60% of the registered capital in Meilan Travelling and 95% of the registered capital in DFG were sold to the Company for cash consideration only, while the consideration for the remaining assets were settled by a combination of cash and the assets sold to Parent Company. The Company has agreed to settle the aggregate purchase price difference in the amount of approximately RMB49.7 million by three cash instalment payments within 12 months from the date of the Asset Swap Agreement, which will be funded by internal sources.

The assets, liabilities and revenues relating to or derived from four assets purchased by the Company from Parent Company pursuant to the Asset Swap Agreement effective 31st May, 2002 are not reflected in the historical consolidated financial statements of the Group for the three years ended 31st December, 2001 and five months ended 31st May, 2002. Such assets, liabilities and revenues are accounted for as an acquisition and will be reflected in the Group’s financial statements for periods subsequent to 31st May, 2002. The pro forma unaudited combined results of the Group for the three years ended 31st December, 2001 and the five months ended 31st May, 2002, as set forth in Appendix II — Additional Financial Information to the Prospectus, include the Group's operating results as if the four assets had been acquired by the Company on 1st January, 1999 or the acquired companies' respective dates of incorporation, whichever is later.

The businesses that were retained by Parent Company after the Restructuring include the ownership and maintenance of runway, real property development, security inspection operations inside the Terminal, and maintenance services to the Meilan Airport such as cleaning, back up power supply and waste processing.

The Directors believe that, for the following reasons, it is neither necessary nor in the best interest of the Group to acquire the runway from Parent Company at this stage:

(i) taking on substantial financial responsibilities such as liabilities assumed, related interest expenses and depreciation expenses associated with the acquisition of the runway is unnecessary at this stage, particularly where the Group may have a number of potentially more attractive business development opportunities to consider in the near term, for which funds might be required;

(ii) the Group has secured virtually all necessary advantages associated with ownership of the runway, in particular, the right to use the runway in connection with its aeronautical business operations, through the Agreement on Runway with Parent Company for a term of 20 years. Please refer to subsection headed "Business — Connected Transactions — Agreement on Runway" for more details;

(iii) the Company has been granted an option to acquire the runway from Parent Company in the future at any time the Company considers appropriate or strategic. Such options are exercisable at the discretion of the Company, at all times irrespective whether or not Parent Company holds any shares in the Company; and

(iv) the arrangements regarding the runway have been fully discussed with CAAC at the time of the establishment of the Company in 2000 and in preparation of the Offering. After such discussion, the proposed arrangements have been made in compliance with all CAAC existing and prevailing regulations and policy guidelines, and the Company obtained the final approval of CAAC in September 2002. Similar arrangements can also be found in other airport operators in the PRC at the time of their respective initial public offerings, including the Shenzhen Airport, the Shanghai (Pudong) Airport and the Xiamen Airport.

The Directors do not believe that it is appropriate to acquire the security inspection operations from Parent Company for the following reasons:

(i) profitability of this business is limited.

(ii) the security inspection unit is under the leadership of CAAC and the public security ministry. It serves more governmental functions than commercial purposes.

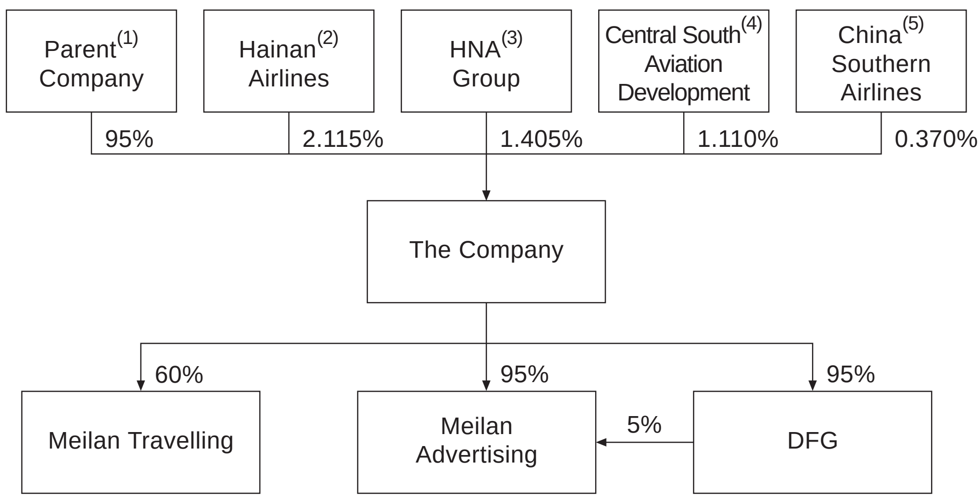
Since the operations such as back up power supply, water supply and waste processing are generally non-revenue generating, the Directors believe that it is in the best interest of the Group to leave these operations with Parent Company.

With respect to the businesses that have been retained by Parent Company after the Restructuring, the Company has entered into a Purchase Option Agreement with Parent Company on 30th May, 2002, which was amended on 25th October, 2002, under which Parent Company has granted to the Company options to purchase from Parent Company any aeronautical or non-aeronautical businesses and assets owned or to be owned by Parent Company from time to time. Please refer to the subsection headed "Connected Transactions" of this section for further details.

Parent Company is the controlling shareholder of the Company, and the registered address of Parent Company is Meilan Airport, Qiong Shan City, Hainan Province, PRC.

Corporate Chart

The following chart sets out the corporate structure of the Group after the Restructuring but before the Offering:



(1) Parent Company is the controlling shareholder of the Company. It was established on 25th August, 1998 and its current registered capital is RMB1,350 million. The shareholders of Parent Company and their respective percentage shareholdings as at the Latest Practicable Date were as follows:

Shareholders	**Percentage shareholdings in Parent Company**
Hainan Airlines *(note (2))*	30.0%
HNA Group *(note (3))*	28.1%
Central South Bureau *(note (6))*	22.2%
Golden City *(note (7))*	8.6%
China Southern Airlines *(note (5))*	7.4%
Aviation Oil *(note (8))*	3.7%

(2) Hainan Airlines is a joint stock limited company incorporated in the PRC on 29th December, 1995 whose shares are listed on the Shanghai Stock Exchange. HNA Group holds approximately 7% interest in Hainan Airlines. The current registered share capital of Hainan Airlines is RMB730,252,801.

(3) HNA Group is a company established in the PRC on 16th April, 1998 whose shares are held as to 70% by 海南交管控股有限公司 (Hainan Transportation Management Holding Company Limited) and 30% by 廣州建運投資有限公司 (Guangzhou Jianyun Investment Company Limited). The current registered capital of HNA Group is RMB100,800,000.

(4) Central South Aviation Development is a company established in the PRC on 16th July, 1993 and wholly owned by the PRC Government. Its current registered capital is RMB9,800,000.

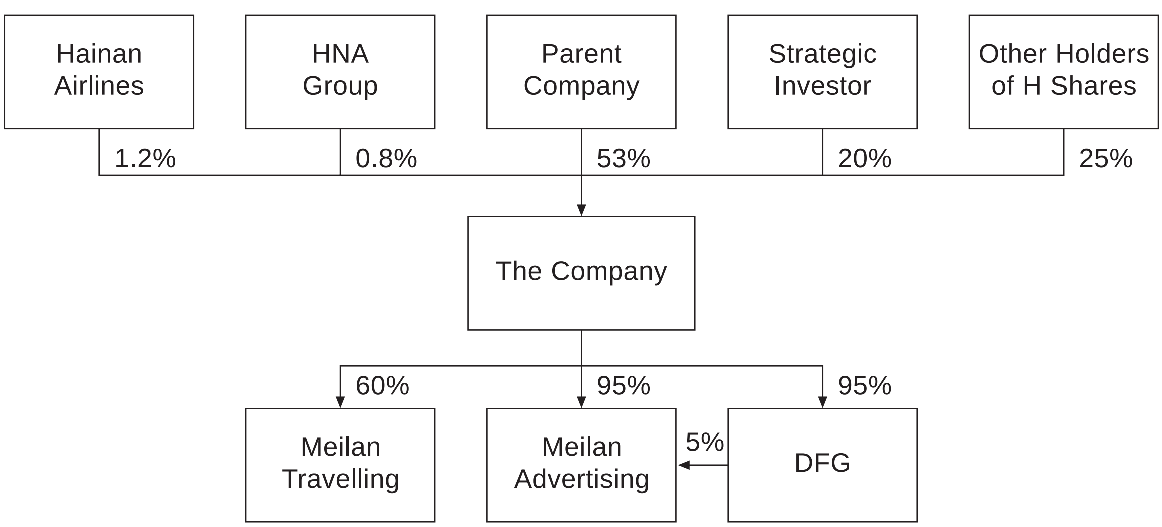
(5) China Southern Airlines is a joint stock limited company incorporated in the PRC on 25th March, 1995 with shares listed on the Stock Exchange. The current registered share capital of China Southern Airlines is RMB3,374,178,000. 中國南方航空(集團)公司 (Southern Airlines (Group)), a wholly state-owned enterprise, is the controlling shareholder of China Southern Airlines.

(6) Central South Bureau is CAAC's regional administrative bureau whose office address is at Baiyun International Airport, Guangzhou City, Guangdong Province, PRC.

(7) Golden City is a company established in the PRC on 28th August, 2001 with a total registered capital of RMB1 billion. Golden City is a wholly state-owned company and its registered address is at 12th Floor, Cai Zheng Building, No. 109, Bin Hai Avenue, Haikou City, Hainan Province, PRC.

(8) Aviation Oil is a company established in the PRC on 16th February, 1990 with a total registered share capital of RMB370 million. Aviation Oil is a wholly state-owned enterprise with the registered address at No. 1 Building, 2nd Block, An Zhen Li, Chaoyang District, Beijing, PRC.

The following chart sets out the corporate structure of the Group immediately after the Offering but before any exercise of the Over-allotment Option:



Note: Both Central South Aviation Development and China Southern Airlines will convert their Domestic Shares into Sale H Shares which will be offered for sale under the Public Offer pursuant to the Temporary Administration Measures on the Reduction of State-Owned Shares for the Raising of Social Security Fund (減持國有股籌集社會保障資金管理暫行辦法) promulgated by the State Council. Immediately after the Offering, they will cease to be shareholders of the Company. For details of the Sale H Shares, please refer to "Structure of the Offering — Sale H Shares" of the prospectus.

AERONAUTICAL OPERATIONS OF THE GROUP

The Group's aeronautical business consists of the provision of airfield services through a revenue-sharing arrangement with Parent Company which owns the runway, and the provision of terminal facilities and ground handling services, passenger and cargo handling services for scheduled and non-scheduled flights at the Meilan Airport. The Group currently provides services to 18 domestic airlines and one airline from each of Hong Kong and Macau for the use of facilities at the Meilan Airport.

Sources of Revenues from Aeronautical Operations

Passenger charges

Domestic airlines are required to pay the Group fees relating to the use of terminal facilities by their passengers. The fee level prior to 1st September, 2002, set by CAAC in conjunction with MOF and SDPC, was approximately RMB50 per passenger, multiplied by 80% of the passenger capacity of the aircraft for each aircraft that lands at the Meilan Airport. Hong Kong and Macau airlines are not required to pay passenger charges. Since 1st September, 2002, the fee level for domestic airlines has been revised to RMB45 per passenger, multiplied by 65% of the passenger capacity of the aircraft for each aircraft that takes off from the Meilan Airport, or, in the case of transit aircraft, RMB45 per passenger who has boarded the aircraft at the Meilan Airport (excluding transit passengers).

For the three years ended 31st December, 2001 and the five months ended 31st May, 2002, passenger charges received by the Group were approximately RMB41.8 million, RMB90.4 million, RMB102.3 million and RMB50.6 million, respectively, representing 51.9%, 55.9%, 55.3% and 42.7% of total revenues respectively.

Airport Fee payable by outbound passengers

According to《民航機場管理建設費管理辦法實施細則民航財發[1997]90號》(the Implementation Rules of the Civil Aviation Airport Management Construction Fee Measures (Min Hang Cai Fa No. 90 [1997])), every passenger departing from an airport in China is required to pay an Airport Fee of RMB50 (for domestic flights) or RMB90 (for international flights, including a fee of RMB20 towards the tourism development fund). All Airport Fees collected from departing passengers by the PRC airports are required to be remitted to MOF, which then re-allocates 50% of such Airport Fees through CAAC or provincial governments to the respective airports for purposes such as renovation or construction of airport facilities or other items designated in CAAC's airport investment scheme as approved by MOF.

Prior to 1st January, 2002, Parent Company was responsible for the collection and remission of the Airport Fees paid by departing passengers at the Meilan Airport to MOF. MOF re-allocated approximately 50% of the collected Airport Fees as equity investment in the registered capital of Parent Company. Please refer to the section headed "History and Development" in this section of the prospectus for further details. Had the 50% of the Airport Fees been treated as revenue of the Company prior to 1st January, 2002, such Airport Fees (less taxes) for each of the three years ended 31st December, 2001 would have been RMB21.9 million, RMB43.9 million and RMB50.3 million, respectively.

From 1st January, 2002 and onwards, pursuant to an application letter by CAAC to MOF on 16th May, 2002 and an approval letter issued by MOF on 25th September, 2002, 50% of the Airport Fees collected shall be payable to MOF and the remaining 50% shall be retained by the Group as ordinary revenue of the Group subject to normal PRC business tax and corporate income tax. For the five months ended 31st May, 2002, the Group's share of the Airport Fees was approximately RMB29.4 million, representing 24.8% of total revenues.

With respect to the Airport Fees for Hong Kong, Macau and foreign flights, the Group receives as revenue 50% of the Airport Fees after the RMB20 contribution towards the tourism development fund.

Ground handling services fee

The Group provides general ground handling services at the Meilan Airport including passenger transport, baggage, cargo and mail handling, aircraft turnaround maintenance, cabin cleaning and waste disposal. The Group currently provides ground handling services to 18 domestic airlines, and one airline from each of Hong Kong and Macau.

The ground handling fees are set by CAAC in conjunction with MOF and SDPC. Two sets of fee scales apply to Hong Kong and Macau airlines and domestic airlines. For Hong Kong and Macau airlines, the basic ground handling fee is US$13 per tonne of MTOW (US$14 for wide body aircraft) for all aircraft with MTOW over 65 tonnes. For small aircraft with MTOW below 30 tonnes, between 30 and 45 tonnes, and between 45 and 65 tonnes, a flat fee of US$390, US$585, and US$845 applies respectively. For example, for a Boeing 737-500 aircraft which has a MTOW of 61 tonnes, the basic ground handling fee is US$845.

Extra ground handling fees for Hong Kong, Macau and foreign airlines are levied for services not covered by the basic charge. These additional ground handling services consist of (i) use of ground equipment such as air bridge and passenger ramp, calculated on a per hour or per use basis; (ii) cabin cleaning services, which are charged at hourly rate; (iii) provision of services including rearrangement of the aircraft cabin, cleaning of aircraft exterior and cabin equipment, calculated at hourly rate.

For each of the three years ended 31st December, 2001 and the five months ended 31st May, 2002, ground handling services fees received by the Company were approximately RMB10.1 million, RMB18.4 million, RMB20.6 million and RMB10.6 million, respectively, representing approximately 12.5%, 11.4%, 11.1% and 9.0% of the total revenues for the relevant period.

Effective 1st September, 2002, the ground handling fee for domestic airlines consists of (i) aircraft cleaning fee, ranging from RMB100 to RMB576 per aircraft, depending on the passenger capacity of the aircraft; (ii) transportation service fee for providing passenger services such as check-in and baggage and mail handling, calculated at RMB61 per payload tonne for all aircraft with a payload over 10 tonnes; and RMB55 per payload tonne for aircraft with a maximum payload of 10 tonnes or less and (iii) special vehicle services fee, which covers the provision of special vehicles including passenger transport vehicles, air bridges, and passenger ramp vehicles, calculated on per hour or per use basis. For example, for a Boeing 737-500 aircraft which has an MTOW of 61 tonnes and a payload of 15 tonnes, the basic aircraft cleaning fee and transportation service fee are RMB120 and RMB915, respectively.

Aircraft movement fees and related charges

Regular aeronautical services at the Meilan Airport include provision of airfield facilities, ramp control and provision of emergency rescue services by the Group and provision of runway and related services such as maintenance of the runway, taxiways and maintenance of lighting system by Parent Company. The Company charges airlines using the Meilan Airport aircraft movement fees and related charges for the provision of these services.

Aircraft movement fees are prescribed by CAAC jointly with MOF and SDPC and vary according to aircraft's MTOW categories and, in respect of those charges against domestic airlines only, the class of the relevant airports. There are two scales of charges, one applicable to domestic airlines and the other applicable to foreign, Hong Kong and Macau airlines.

The following table illustrates the standards of charges for each aircraft movement in effect during the Track Record Period, an aircraft movement is defined for the purpose of fee calculation as one landing and one take-off:

	Charges for foreign, Hong Kong and Macau Airlines	**Charges for Domestic Airlines**
	(US$)	*(RMB)*
MTOW *(tonnes)*		
Less than 25	N.A.	4.40 per tonne
50 or below	558	N.A.
25–99	N.A.	5.50 per tonne
51–100	558 plus 9 per tonne over 50 MTOW	N.A.
100–199	N.A.	7.70 per tonne
101–200	1,008 plus 10 per tonne over 100 MTOW	N.A.
Greater than 200	2,008 plus 12 per tonne over 200 MTOW	N.A.
200 and above	N.A.	8.80 per tonne

For example, the aircraft movement fee for a Boeing 737-500 aircraft, which has an MTOW of 61 tonnes, is RMB335.5 for a domestic airline and US$657 (RMB5,438.7) for a foreign, Hong Kong or Macau airline.

The following table sets out the aircraft movements by relevant weight classes of flights operated by Hong Kong and Macau airlines and domestic airlines at the Meilan Airport for the three years ended 31st December, 2001, and the first five months of 2001 and 2002, respectively:

Flights Operated by Domestic Airlines

	Aircraft movements				
	Year ended 31st December,			**Five months ended 31st May,**	
Aircraft weight class (MTOW by tonnes)	**1999[(1)]**	**2000**	**2001**	**2001**	**2002**
Less than 25	7,589	11,716	9,257	4,663	4,162
25–100	18,676	36,125	35,026	15,736	18,528
101–200	3,277	7,262	8,637	3,747	3,911
Over 200	615	761	107	35	298
Total	30,157	55,864	53,027	24,181	26,899

(1) Commercial operations of the Meilan Airport commenced on 25th May, 1999. Accordingly, the relevant data for 1999 reflects only seven months of commercial operations and therefore are not directly comparable with those of the subsequent years.

Flights Operated by Hong Kong and Macau Airlines

	Aircraft movements				
	Year ended 31st December,			Five months ended 31st May,	
Aircraft weight class (MTOW by tonnes)	**1999(1)**	**2000**	**2001**	**2001**	**2002**
Less than 25	—	—	—	—	1
25–100	577	901	759	327	300
101–200	—	—	—	—	—
Over 200	—	—	—	—	—
Total	577	901	759	327	301

(1) Commercial operations of the Meilan Airport commenced on 25th May, 1999. Accordingly, the relevant data for 1999 reflects only seven months of commercial operations and therefore are not directly comparable with those of the subsequent years.

In addition to aircraft movement fees, airlines are also required to pay related charges such as night, peak hour and lighting surcharges, aircraft parking and air bridge fees and security fees.

For the three years ended 31st December, 2001 and the five months ended 31st May, 2002, aircraft movement fees and related charges received by the Group were approximately RMB5.6 million, RMB10.7 million, RMB10.2 million and RMB5.1 million, respectively, representing 7.0%, 6.6%, 5.5% and 4.3% of total revenues respectively.

The following table illustrates the standards of charges for each aircraft movement for domestic airlines in effect since 1st September, 2002. An aircraft movement is defined for the purpose of fee calculation as one landing and one take-off:

	Charges for Domestic Airlines
	(RMB)
MTOW *(tonnes)*	
Up to 25	16.9 per tonne
26–100	22.0 per tonne
101–200	29.7 per tonne
201 and above	33.8 per tonne

For example, the aircraft movement fee for a Boeing 737-500 aircraft, which has a MTOW of 61 tonnes, is RMB1,342 for a domestic airline.

Revenue sharing arrangement with Parent Company

The Company and Parent Company entered into the Agreement on Runway on 25th October, 2002 in respect of the operation and maintenance of the runway and other integrated services provided to airline customers. The parties have confirmed in the agreement that the aircraft movement fees (for domestic, Hong Kong, Macau and foreign airlines), the passenger charges (for domestic airlines) and the basic ground handling services fees (for Hong Kong, Macau and foreign airlines) will be shared by the Company and Parent Company on such ratio as CAAC or any other regulatory authorities may from time to time prescribe, which as at the date of the agreement was on the basis of 75% to the Company and 25% to Parent Company, pursuant to the document 《海口美蘭機場有限責任公司與海南美蘭機場股份有限公司收入劃分比例的批覆》(總局財函[2002]77號) (Approval Relating to the Ratio of Revenue Sharing between Haikou Meilan Airport Company Limited and Hainan Melian Airport Company Limited (Zhong Ju Zai Han [2002] No. 77)) issued by CAAC on 27th September, 2002.

According to the Purchase Option Agreement entered into on 30th May, 2002 and the supplemental agreement thereto dated 25th October, 2002, the Company has the option to acquire the runway and other assets owned from time to time by Parent Company at a price based on an independent valuation.

Domestic Passenger Traffic

The following table sets out the numbers of aircraft movement and passenger throughput in domestic flights to and from the Meilan Airport for the three years ended 31st December, 2001, the five months ended 31st May, 2001 and 2002 and the nine months ended 30th September, 2001 and 2002, respectively.

	Year ended 31st December,			Five months ended 31st May,		Nine months ended 30th September,	
	1999[1]	2000	2001	2001	2002	2001	2002
Passenger throughput *('000)*	2,068	4,179	4,900	2,170	2,498	3,709	4,097
Change as compared to the same period in the previous year *(%)*	—	—	17.3	—	15.1	—	10.5
Aircraft movements[2]	29,524	54,927	52,091	23,758	26,504	39,662	43,931
Change as compared to the same period in the previous year *(%)*	—	—	(5.2)	—	11.6	—	10.8

(1) Commercial operations of the Meilan Airport commenced on 25th May, 1999. Accordingly, the relevant data for 1999 reflects only seven months of commercial operations and therefore are not directly comparable with those of the subsequent years.

(2) The figures include aircraft movements for training, emergency or agricultural purpose.

Airline customers operating domestic flights

The following table sets out the number of scheduled flights in 2001 operated by the top five domestic airlines in terms of the number of scheduled domestic flights to and from the Meilan Airport.

Airlines	No. of scheduled flights
Hainan Airlines	24,058
China Southern Airlines	13,230
China Northern Airlines	1,614
Wuhan Airlines	1,528
China Eastern Airlines	1,443

Hong Kong and Macau Passenger Traffic

The following table sets out the numbers of aircraft movements and passenger throughput of Hong Kong and Macau flights to and from the Meilan Airport for the three years ended 31st December, 2001, the five months ended 31st May, 2001 and 2002 and the nine months ended 30th September, 2001 and 2002, respectively.

	Year ended 31st December,			Five months ended 31st May,		Nine months ended 30th September,	
	1999[1]	2000	2001	2001	2002	2001	2002
Passenger throughput *('000)*	130.0	172.6	166.1	67.3	58.1	125.9	106.2
Change as compared to the same period in the previous year *(%)*	—	—	(3.8)	—	(13.7)	—	(15.6)
Aircraft movements	1,152	1,669	1,522	657	607	1,150	1,103
Change as compared to the same period in the previous year *(%)*	—	—	(8.8)	—	(7.6)	—	(4.1)
Percentage of aircraft movements operated by							
domestic airlines *(%)*	49.9	46.0	50.1	50.2	50.4	49.9	50.4
Hong Kong and Macau airlines *(%)*	50.1	54.0	49.9	49.8	49.6	50.1	49.6

(1) Commercial operations of the Meilan Airport commenced on 25th May, 1999. Accordingly, the relevant data for 1999 reflects only seven months of commercial operations and therefore are not directly comparable with those of the subsequent years.

Airline customers operating Hong Kong and Macau flights

The following table sets out the airlines operating Hong Kong and Macau flights to and from the Meilan Airport and the number of chartered flights in 2001.

Airlines	No. of chartered flights
China Southern Airlines	760
Hong Kong Dragon Airlines Limited	218
Air Macau Company Limited	541
Hainan Airlines	3

International Passenger Traffic

The following table sets out the numbers of aircraft movements and passenger throughput of international flights for the three years ended 31st December, 2001, the five months ended 31st May, 2001 and 2002 and the nine months ended 30th September, 2001 and 2002, respectively.

	Year ended 31st December,			Five months ended 31st May,		Nine months ended 30th September,	
	1999[(1)]	2000	2001	2001	2002	2001	2002
Passenger throughput *('000)*	3.8	11.8	13.0	7.3	7.5	10.1	10.6
Change as compared to the same period of previous year *(%)*	—	—	10.2	—	2.7	—	5.0
Aircraft movements	58	169	173	93	89	133	140
Change as compared to the same period of previous year *(%)*	—	—	2.4	—	(4.3)	—	5.3
Percentage of aircraft movements operated by							
domestic airlines *(%)*	100.0	100.0	100.0	100.0	100.0	100.0	100.0
foreign airlines *(%)*	—	—	—	—	—	—	—

(1) Commercial operations of the Meilan Airport commenced on 25th May, 1999. Accordingly, the relevant data for 1999 reflects only seven months of commercial operations and therefore are not directly comparable with those of the subsequent years.

Airline customers operating international flights

The following table sets out the number of chartered international flights in 2001 operated by China Southern Airlines to and from the Meilan Airport.

Airline	No. of chartered flights
China Southern Airlines	167

Cargo Traffic[1]

The following table sets out the numbers of cargo throughput at the Meilan Airport for each of the three years ended 31st December, 2001, the five months ended 31st May, 2001 and 2002 and the nine months ended 30th September, 2001 and 2002 respectively.

	Year ended 31st December,			Five months ended 31st May,		Nine months ended 30th September,	
	1999[2]	2000	2001	2001	2002	2001	2002
		(tonnes)					
International cargo throughput *(tonnes)*	63	203	240	123	142	182	203
Hong Kong/Macau cargo throughput *(tonnes)*	893	1,515	1,682	703	687	1,261	1,180
Domestic cargo throughput[3] *(tonnes)*	35,184	69,336	71,691	32,268	35,339	54,387	55,610
Total	36,140	71,054	73,613	33,094	36,168	55,830	56,993
Change as compared to the same period of previous year *(%)*	—	—	3.6	—	9.3	—	2.1

(1) Although cargo-related operations and assets are traditionally categorised as aeronautical operation and asset, the revenues that the Company derived from the cargo centre at the Meilan Airport are in the form of franchise fee which is treated as a type of non-aeronautical revenue in the Company's consolidated financial statements.

(2) Commercial operations of the Meilan Airport commenced on 25th May, 1999. Accordingly, the relevant data for 1999 reflect only seven months of commercial operations and therefore are not directly comparable with those of the subsequent years.

(3) The figures include cargo, mail and passenger luggage throughput at the Meilan Airport.

NON-AERONAUTICAL OPERATIONS OF THE GROUP

The Group also derives income from engaging in certain non-aeronautical businesses which are summarised below.

Non-aeronautical operations

Leasing income

The Group leases out commercial areas of approximately 2,422 m^2 in the Terminal (owned by the Group) for operations of restaurants and shops. The Group leases out commercial spaces for restaurants and retail shops at the Terminal and charges a fixed rent.

The Group also leases out office premises with a total of 1,723 m^2 to Hong Kong and domestic airlines for use as offices, check-in counters and ticketing counters in the Terminal.

The rental rates for offices, counters and lounges are based on guidance rates set by CAAC. Leasing income of the Group was RMB26.3 million and RMB10.9 million for the year ended 31st December, 2001 and five months ended 31st May, 2002, respectively.

Franchise fees

The Group generates franchise fees from a number of sources. Firstly, the Company has granted Hainan Food the right to operate the air catering services business at the Meilan Airport for a term of three years pursuant to an agreement dated 31st December, 2000. In exchange, Hainan Food pays an annual fee of RMB4.38 million to the Company.

The Company outsourced its air ticket sales at the Meilan Airport to HLAS pursuant to a one-year contract for the period from 1st September, 2002 to 31st August, 2003. The annual fee under the current contract is RMB800,000.

In a contract entered into on 1st January, 2002, the Company agreed to appoint THIA to manage the sale of air travel personal accident insurance at the Meilan Airport on an exclusive basis for a period of one year ending 31st December, 2002. The Group receives a fixed annual fee of RMB1.74 million plus a 50% share of the insurance commission in excess of RMB1.74 million per year.

Advertising revenues

The Group earns advertising revenues from leasing out advertising spaces at the Terminal. The Group negotiates individually with advertisers and usually enters into annual contracts with advertisers for a fixed fee. The advertising revenue from such operation was approximately RMB4.0 million and RMB2.0 million for the year ended 31st December, 2001 and the five months ended 31st May, 2002, respectively.

Other revenues

Other revenues mainly consist of fees charged (according to aircraft model, aircraft movements and passenger numbers) by the Company to its airline customers for the use of the Company's electronic boarding confirmation system installed at the boarding gates, as well as fees for the supply of hot water to aircraft.

For the year ended 31st December, 2001, and the five months ended 31st May, 2002, other revenues were approximately RMB6.2 million and RMB3.2 million, respectively.

Non-aeronautical operations acquired on 31st May, 2002

Pursuant to the Asset Swap Agreement dated 30th May, 2002, as amended by a supplemental agreement dated 25th October, 2002, the Company purchased four revenue-generating assets from Parent Company and sold three non-revenue-generating assets to Parent Company. The non-aeronautical business and assets purchased by the Company include car parking facilities at the Meilan Airport, 60% of the registered capital in Meilan Travelling and 95% of the registered capital in DFG. In addition, the Company purchased the cargo centre from Parent Company. Although cargo-related operations and assets are traditionally categorised as aeronautical operations and assets, the revenues that the Company derived from the cargo centre at the Meilan Airport are in the form of franchise fees which are treated as a type of non-aeronautical revenue in the Group's financial statements.

The assets, liabilities and revenues relating to or derived from four assets purchased by the Company from Parent Company pursuant to the Asset Swap Agreement effective 31st May, 2002 are not reflected in the historical consolidated financial statements of the Group for the three years ended 31st December, 2001 and five months ended 31st May, 2002. Such assets, liabilities and revenues are accounted for as an acquisition and will be reflected in the Group's financial statements for periods subsequent to 31st May, 2002. The pro forma unaudited combined results of the Group for the three years ended 31st December, 2001 and the five months ended 31st May, 2002, as set forth in Appendix II — Additional Financial Information to the Prospectus, include the Group's operating results as if the four assets had been acquired by the Company on 1st January, 1999 or the acquired companies' respective dates of incorporation, whichever is later.

The Group's additional sources of non-aeronautical revenues upon the acquisition of the four assets include:

Tourism services

The Group earns tourism revenues from travel services including tourist transportation from the Meilan Airport to Haikou City, hotel reservation, air ticketing and tourist group arrangements, provided through Meilan Travelling, the Company's subsidiary. Meilan Travelling has a registered capital of RMB11 million, 60% of which is owned by the Company and 40% is owned by Parent Company.

Cargo centre franchise fee

The Company acquired the cargo centre from Parent Company pursuant to the Asset Swap Agreement. The Company also entered into an agreement with Yangzi Express effective from 1st June, 2002 to 31st December, 2003. Under the agreement, Yangzi Express obtains from the Company the right to operate the cargo centre and retain all revenues generated therefrom. In return, Yangzi Express pays an annual fee of RMB18 million to the Company.

Sales of duty-free and other retail goods

The Group earns revenue from the sales of duty-free and other retail goods in the duty-free and other shops at the Terminal. The duty-free shops currently occupy approximately 228.5 m^2 in the Terminal. The Group intends to expand its duty-free shop operations.

Established on 11th May, 1999, DFG is engaged in selling duty-free goods including cigarette, alcohol, cosmetics and so forth at the international area of the Terminal and non-duty-free products at the domestic area of the Terminal. DFG is required to procure duty-free merchandise from China Duty-Free Corporation at fixed prices. DFG is owned as to 95% by the Company and 5% by Parent Company.

Car parking charges

The Company receives revenue generated by its car parking facilities. The ground level car park has a site area of 54,183 m^2, which can accommodate 662 vehicles. Additional parking space of 1,440 m^2 and 50 parking lots is available on the upper (departure) level of the Terminal. For ground level car park, parking fees are charged according to the size of the vehicle. The parking fees for large (over five tonnes or 25 seats), medium (between one and five tonnes or 13 to 24 seats) and small-sized (under one tonne or less than 13 seats) vehicles are RMB15, RMB8 and RMB5 per entry, respectively. There is separate charge schedule for overnight parking.

MEILAN AIRPORT'S MAJOR FACILITIES

The Meilan Airport is equipped with facilities for providing both aeronautical and non-aeronautical services to passengers and airlines. These facilities are all located in Qiongshan, Hainan Province and summarised below.

Runway

The runway of Meilan Airport was designed and constructed in accordance with ICAO category 4E standards. It is 3,600-metre long, 44% longer than the ICAO specification of 2,500 metres as the required length for accommodating the maximum gross weight takeoff requirements of Boeing 747-400 aircraft. The runway's concrete surface, precision instrument markings, lighting and taxiways are all constructed according to ICAO category 4E standards. The category II precision instrument landing system at the west approach (the primary approach used by the majority of flights) provides for aircraft operations with 30-metre decision height and 400-metre visibility distance while the category I precision instrument landing system at the east approach provides for 60-metre decision height and 800-metre visibility distance. Both the runway and the underlying land use rights are owned by Parent Company. The term of the lease for the land use rights is 50 years which ends in 2049.

Pursuant to the Agreement on Runway dated 25th October, 2002 between the Company and Parent Company, Parent Company has agreed (i) to operate and maintain the runway in accordance with the applicable regulatory and industrial standards and keep the runway in good working condition; (ii) not to change the current usage of the runway unless approved by the relevant governmental departments and agreed in writing by the Company; (iii) not to dispose of any assets of or interests in the runway without consent of the Company; and (iv) to continually hold the airport permit and maintain the validity thereof. The Company has agreed to manage and operate the Meilan Airport in accordance with the regulatory requirements and share the relevant fees with Parent Company pursuant to the ratio approved by the relevant PRC regulatory authorities.

For details of the runway arrangement, please refer to the sub-section headed "Connected Transactions — Agreement on Runway" of this section.

According to the Purchase Option Agreement entered into on 30th May, 2002 and the supplemental agreement thereto dated 25th October, 2002, the Company has the option to acquire the runway and other related assets owned from time to time by Parent Company at a price based on an independent valuation.

Terminal

Opened in 1999, the Terminal is a three storey building, including one basement level, with a total gross floor area of 60,296 m^2. Facilities included seven air bridges, first/business class and VIP lounges, flight information display system, passenger check-in counters, automatic baggage handling system, DCS airline offices, travel service counters, restaurants and retail shops.

The Terminal and its associated land use rights are owned by the Company.

Apron

The apron provides a total of 15 aircraft parking positions, seven of which are connected to the Terminal by air bridges. The total site area of the apron is 163,237 m^2.

Cargo centre

The cargo centre has a total site area of 16,120 m^2 and a gross floor area of 4,337 m^2. There are 41 transport vehicles and 172 luggage trailers. The cargo centre had an annual cargo throughput of approximately 54,000 tonnes in 2001. The cargo centre was acquired by the Company from Parent Company in May 2002 and is currently managed and operated by Yangzi Express which pays the Company an annual franchise fee of RMB18 million.

Car parking facilities

The ground level car park has a site area of 54,183 m^2, which can accommodate 662 vehicles. The Group installed an automatic system to collect fees for the ground level car parking. There are also car parking spaces on the upper (departure) level with a site area of 1,440 m^2 which can accommodate 50 vehicles.

Fire-fighting facilities

Situated next to the remote aircraft parking aprons is a fire-fighting station with a total gross floor area of 3,908 m^2, 11 fire engines and various fire-fighting equipment.

Medical services and emergency facilities

The Group operates a 24-hour emergency centre with a site area of approximately 3,597 m^2 and a total gross floor area of 1,209 m^2 at the Meilan Airport. The emergency centre is staffed by 13 qualified medical practitioners.

Pledge of land use rights

The Company has pledged the land use rights relating to approximately 26.1 hectares of land underlying the Terminal and other facilities of the Meilan Airport, with a value of RMB50 million, as security for a long-term bank loan from China Development Bank with an outstanding principal amount of RMB270 million as of 31st August, 2002. The final maturity of the loan is 20th December, 2008.

In addition to the land use rights pledged by the Company as security, Parent Company has also pledged land use rights relating to approximately 34.0 hectares, with a value of RMB357 million, as security for the aforesaid China Development Bank loan. The Company obtained the written consent of China Development Bank on 4th November, 2002 to release the guarantee as soon as practicable. The Company has undertaken to the Stock Exchange that it will use its best endeavours to complete the procedures regarding such release within three months from the date on which the H Shares are listed on the Stock Exchange. If the guarantee is not released after three months from the date of commencement of dealing in the H Shares, the Company will release an appropriate announcement. See "Connected Transactions — Connected Transactions between the Company and Parent Group — Provision of Security for Bank Facilities" of this section.

RELATIONSHIP WITH AIRLINE CUSTOMERS

Hainan Airlines has been the largest customer of the Group, accounting for 40.4%, 38.7%, 32.8% and 21.9% of the Group's total revenue for each of the three years ended 31st December, 2001 and the five months ended 31st May, 2002, respectively. Hainan Airlines has its home base at the Meilan Airport and operates the largest number of scheduled flights to and from the Meilan

Airport. Apart from aircraft movement fees, passenger charges and ground handling fees, Hainan Airlines leases offices, ticketing and check-in counters and other facilities in the Terminal. The Group therefore receives a steady stream of revenue from Hainan Airlines.

China Southern Airlines has been the second largest customer of the Group, contributing 26.0%, 22.9%, 24.4% and 16.3% of the Group's total revenue for each of the three years ended 31st December, 2001 and five months ended 31st May, 2002, respectively. All Domestic Shares currently held by China Southern Airlines will be converted into Sale H Shares and offered under the Offering and, immediately upon the completion of the Offering, China Southern Airlines will cease to hold any Shares.

Other significant customers include:

China Northern Airlines, China Southwest Airlines, and China Eastern Airlines contributing respectively 4.1%, 4.1%, and 2.9% of the revenue of the Group for the year ended 31st December, 1999.

China Southwest Airlines, China Northern Airlines, and Shenzhen Airlines contributing respectively 2.4%, 2.1% and 1.6% of the revenue of the Group for the year ended 31st December, 2000.

China Northern Airlines, China Eastern Airlines, and China Southwest Airlines contributing respectively 2.3%, 2.2% and 2.1% of the revenue of the Group for the year ended 31st December, 2001.

China Northern Airlines, Wuhan Airlines, and Air China contributing respectively 2.9%, 1.9% and 1.8% of the revenue of the Group for the five months ended 31st May, 2002.

The Group follows normal commercial practices to ensure collection of receivables within acceptable time limit, usually not more than 90 days. The Group bills its customers one month after the provision of services. Most customers settle their accounts within 60 to 90 days. For any account outstanding for over 90 days, the Group will liaise with the customers more frequently to intensify the collection efforts. Bad debt provisions are reviewed by the management on a case-by-case basis. The outstanding accounts receivables were RMB4.2 million, RMB12.9 million, RMB19.2 million and RMB27.7 million for year 1999, 2000, 2001 and the first five months of 2002, respectively. The provision made for doubtful accounts for each of the three years ended 31st December, 2001 and the five months ended 31st May, 2002 was nil, nil, RMB1,342,000 and RMB522,000, respectively. The average turnover period for receiving payments on the outstanding accounts for each of the three years ended 31st December, 2001 and the five months ended 31st May, 2002 was 67 days, 54 days, 59 days and 80 days, respectively. The longer turnover period for the five months ended 31st May, 2002 was partially due to the unsettled payment of China Southern Airlines as at 31st May, 2002 which was substantially settled subsequently and the extension of grace period to Wuhan Airlines by the Group, normally not more than 60 days, which was also subsequently settled.

In assessing the amount of doubtful debt provision required, management reviews the status of the outstanding debts and applies the policy as follows:

Provisions are not considered necessary by management if all the following criteria are met:

(a) accounts receivable balances are not disputed by customers;

(b) there have been partial settlements by the customers over the financial year; and

(c) the customers have maintained ongoing and stable trade relationships, including settlements, with the Group up to date.

Normally, management will provide full provision for debts overdue for one year.

Mr. Chen Wenli and Mr. Zhang Han'an hold 35,640 and 23,970 staff shares, respectively, in Hainan Airlines. Save for the foregoing, none of the Directors or their respective associates (within the meaning of the Listing Rules), or shareholders (excluding Parent Company), which, to the knowledge of the Directors, own more than 5% of the issued share capital of the Company, has any interest in any of such customers.

RELATIONSHIP WITH SUPPLIERS

The principal materials and goods required by the Group in providing its services are utilities supplies such as water and electricity and merchandise for the duty-free shop and other retail shops following the acquisition of DFG.

Parent Company is the largest supplier of the Group accounting for approximately 13.8%, 18.8%, 21.1% and 18.1%, respectively, of the Group's total operating costs for each of the three years ended 31st December, 2001 and the five months ended 31st May, 2002. Water and electricity are provided by Parent Company. The Group settles its account with Parent Company quarterly. See "Connected Transactions — Airport Composite Service Agreement" of this section.

The Group's five largest suppliers in aggregate accounted for approximately 24.2%, 30.9%, 36.0% and 32.9%, respectively of its total operating costs for each of the three years ended 31st December, 2001 and the five months ended 31st May, 2002. None of the Directors or their respective associates (within the meaning of the Listing Rules), or shareholders (excluding Parent Company), which, to the knowledge of the Directors, own more than 5% of the issued share capital of the Company, has any interest in any of such suppliers. The Group does not have long-term contracts with any of its suppliers of materials and believes that alternative sources of supply are readily available. The Group has not experienced any material difficulty in obtaining adequate supply of materials.

As of 31st May, 2002, accounts payable to suppliers represent the amount payable for the domestic goods purchased for duty-free and other shops by the Group. The suppliers of the Group do not specifically state the credit period but agree that the Group settles the payments with them only when the goods are sold out.

The Group does not make general provision for its inventory but does review its inventory position on a monthly basis. Inventories will be reviewed by the management on a case by case basis to identify any obsolete stocks. Inventories are considered to be obsolete if the inventories remain unsold one month before the expiry date. Full provision is made in the accounts for obsolete inventory. The Group did not provide any provision for its inventory during the Track Record Periods.

COMPETITION

The Group faces competition or potential competition mainly in the following areas:

Competition with other modes of transport

The Group's operations depend on the volume of commercial air traffic at the Meilan Airport. Commercial airlines that operate at the Meilan Airport face competition for passengers and cargo from other modes of transport such as waterways, road and railway transportation. In the past 20 years, China has experienced rapid economic growth, which has been accompanied by rising level of disposable income, increasing demand for both domestic and international business and tourist travel and higher volumes of cargo and mail delivery. All of these factors have contributed to a growing demand on the transportation section, including aviation industry.

In recent years, China has invested a large amount of capital to improve its transportation infrastructure including airports, highways and railways. The construction of new highways of international standard as well as improvements of the rail network have resulted in higher levels of speed and comfort for road and rail travel, intensifying their competition with air transport for long distance travel. The Ministry of Railway and the provincial governments of Guangdong and Hainan are jointly developing the 568.3-kilometre Guangdong-Hainan Railway. This railway, which is scheduled for completion in 2003, consists of the 138-kilometre Zhanjiang-Hai'an railway in Guangdong, a railway ferry service from Hai'an to Haikou and the Haikou-Chahe line on the west side of the Hainan Island. Travel time from Guangzhou to Haikou by the Guangdong-Hainan Railway will be approximately 10 hours. The Directors believe the Guangdong-Hainan Railway will create competition with respect to certain categories of non-priority cargo that is currently carried by air and with respect to economy travellers but the impact on the Group's passenger and cargo businesses will not be substantial.

The Directors believe that China's continuing economic growth and modernisation will continue to result in growing demand for high speed transport and air travel will continue to have a competitive advantage over other modes of transport, especially for long distance travel. Hainan Island, being geographically separated from the mainland and relatively far away from most of the other major cities in China, tends to resort to air travel as a solution to the growing demand.

Competition with other airports

An airport competes with other airports for passenger and cargo traffic and aircraft movements. The Meilan Airport faces potential competition from Sanya Airport for local traffic.

In Hainan Province, the only other major civil airport is the Sanya Airport. Located approximately 275 kilometres from Haikou, the Sanya Airport handled approximately 990,000 passengers and 5,700 tonnes of cargo in 2001, making it the 29th and 41th busiest airport in the PRC for passengers and cargo, respectively. Given that Haikou is the economic and political centre of the Hainan Province, and that Meilan Airport is usually the first stop for domestic travellers arriving in Hainan, the Directors believe that the Sanya Airport presents moderate competition to the Meilan Airport.

In addition, the Company entered into a management contract with SPIA on 23rd August, 2002 to manage the Sanya Airport and receive management fees set at 1.5% of revenue of the Sanya Airport as well as other compensations based on the improvement to the profitability of SPIA.

SANYA MANAGEMENT CONTRACT

On 23rd August, 2002, the Company entered into the Sanya Management Contract with SPIA which owns and operates the Sanya Airport in Sanya, Hainan Province. Pursuant to the terms of this contract, the Company will be responsible for the day-to-day management of the Sanya Airport, including human resources, operations, finance, accounting, administration and investment activities. The Company has the right to appoint management of SPIA including the chief executive officer, deputy chief executive officer and chief financial officer. The Company has appointed Mr. Liu Lu to be the deputy chief executive officer of SPIA.

In return, the Company receives a management fee of 1.5% of annual operating revenue of the Sanya Airport, plus 5% of the reduction in net losses when the Sanya Airport remains loss-making or 10% of the profit before tax when the Sanya Airport starts to generate net profits.

The term of the Sanya Management Contract is from 1st August, 2002 to 31st July, 2007, during which period, SPIA will retain ownership of all its assets and liabilities. If SPIA proposes to dispose any of its assets during the term of the management contract, SPIA must notify the Company three months in advance and such disposal has to be subject to the condition that it will not affect the normal business operation of the Sanya Airport.

SPIA's single largest shareholder is HAC, which owns 99% of the shareholding of SPIA. According to a notice issued by the Hainan Asset Bureau (Qiong Guo Zi Wei [2000] No. 6) on 11th December, 2000, the Hainan Asset Bureau entrusted all the state-owned shares in the registered capital of HAC to Golden City. In May 2002, Golden City entrusted 32.6% of the total registered capital of HAC to HNA Group. Under this arrangement, HNA Group has the power to exercise shareholders' rights on behalf of Golden City (except with respect to material issues such as merger, dissolution or reorganisation of HAC, change in capital, giving of security or guarantee), nominate directors and supervisors for approval at shareholders meetings. This arrangement will expire on 28th May, 2004 but can be renewed by mutual agreement upon expiry. Save as disclosed above, Hainan Phoenix Airport Co., and Golden City have no relationship with the Group.

INSURANCE

The risks of liability for bodily injury to any person and property damage arising out of the fault or negligence of the Group or any of its employees or agents are covered under the comprehensive airport liability insurance policy maintained by CAAC for certain airports in China with China Pacific Insurance Company Limited, an independent third party of the Group. The insured amount for the Meilan Airport is US$200 million which is determined by reference to certain factors including aircraft movements, risks covered and the customs and practice of other airports. The Group has not made any claim under this insurance policy. The Directors believe that the insured amount will be sufficient to compensate third parties for the bodily injury and property damage covered by the insurance policy in the event of any reasonably foreseeable claims.

The Group currently has two insurance policies with China Pacific Insurance Company Limited for its properties (including the Terminal), equipment and machinery. The total insured amount is approximately RMB427 million. The current policies cover the period from 1st October, 2001 to 30th September, 2004 and from 3rd April, 2002 to 30th September, 2004, respectively. The Group has not made any claims under these insurance policies so far. The Directors believe that these two insurance policies will be sufficient to cover the Group's potential losses or the cost of replacing the destroyed or damaged properties, equipment or machinery in the event of any reasonably foreseeable damages.

Neither the Group nor Parent Company carries business interruption insurance, as the Directors believe that such coverage is not customary in the PRC.

INTELLECTUAL PROPERTY

The trademarks listed in paragraph B2 of Appendix X to this prospectus are currently being applied for registration with the relevant authority in PRC under the name of the Company. Under a trademark licensing agreement, the Company has granted a non-exclusive licence to Parent Company for using such trademarks for a nominal fee on terms as set out therein. See "Connected Transactions — Trademark of Licensing" of this section.

The trademarks have been and will continue to be used by both the Group and Parent Company in relation to business operation and corporate name. Under the trademark licensing agreement, Parent Company cannot grant any further licence to use the trademarks to any third party without the prior written consent of the Company.

ENVIRONMENTAL MATTERS

The requirements for environmental protection applicable to airports in China are set out in laws and regulations including the Environment Protection Law, Noise Pollution Prevention Law, Air Pollution Prevention Law and Solid Waste Pollution Prevention Law. In compliance with these regulations, the Meilan Airport has installed necessary facilities and has taken appropriate measures to deal with air, waste and waste water pollution.

In anticipation of increase in the volume of waste products that are expected to be discharged by the Meilan Airport in its daily operations as passenger traffic increases, RMB3 million has been invested in installing two incinerators with daily waste treatment capacity of 6 metric tons. The waste water is transported by an underground pipeline to a waste water treatment plant with the daily treatment capacity of 1,440 cubic metres on a regular basis.

Although Meilan Airport itself does not produce any noise that exceeds the prescribed level applicable to areas around airports, the aircraft engine noise created by approaching and departing aircraft using the Meilan Airport may exceed such level. Since the inception of the Company, the Group has not had any claims and is not aware of any pending or potential claims, either by private persons or governmental authorities or agencies, in relation to the levels of noise pollution arising from airport operations.

Except as stated above, so far as the Directors are aware, the Group is in compliance with all applicable PRC environmental protection regulations.

LAND AND PROPERTY

The Group's business and ancillary facilities are located in Qiongshan city, approximately 25 kilometres from the centre of Haikou, Hainan Province, the PRC.

The land use rights in respect of the land of approximately 350,442 m^2, on which buildings and structures including the Terminal, apron, the cargo distribution centre, fire-fighting building, the emergency centre and car park with a total gross floor area of 69,750 m^2 were built have been granted by the state to the Company. The Company has obtained the land use rights certificate issued by the Qiongshan Land Resources Bureau on 5th September, 2002. The land use rights are valid until 5th September, 2049.

The Company also leases from Parent Company some office premises of a building inside the Meilan Airport with a total gross floor area of approximately 1,415 m^2. The building and the land use rights to the land underlying the building are owned by Parent Company.

The property interests of the Group have been valued by Vigers Hong Kong Limited as independent valuer. A copy of its letter and valuation certificate is set out in Appendix IV to this prospectus.

RELATIONSHIP WITH CAAC

The Meilan Airport, together with other airports in China, are currently subject to extensive regulation by CAAC. CAAC has an indirect equity interest in the Company.

Regulations and policies issued or implemented by CAAC encompass substantially all aspects of the operations and businesses of airports, such as renovation, construction and expansion of airport facilities, technical standards of airfield facilities, aeronautical fees and air traffic and ground safety. While the Company generally benefits from CAAC policies on an industry basis that are beneficial to the civil aviation industry in China as a whole, the implementation of specific CAAC policies could from time to time adversely affect the Group's operation.

RELATIONSHIP WITH PARENT COMPANY

Overview

After the completion of the Offering, Parent Company will own over 50% of the then issued share capital of the Company and retain a controlling interest in the Company. Subject to the terms of the Shareholders' Agreement (please refer to "Relationship with the Strategic Investor" in this section), Parent Company will be able to exercise all the rights of a controlling shareholder, including the election of Directors and voting in respect of amendments to the Articles of Association. However, Parent Company, as the Company's controlling shareholder, will be subject to certain minority shareholder protection provisions under the Articles of Association.

Assets Purchase Option

Parent Company has granted the Group options to purchase from Parent Company, at any time, the runway and, at any time prior to the expiry of one year after Parent Company ceases to hold 10% or more of the share capital of the Company, any other aeronautical or non-aeronautical businesses and assets owned or to be owned by Parent Company from time to time, in each case based on its or their fair value as determined by an independent appraiser in accordance with the relevant PRC laws. Upon exercise of such purchase option, the Company will comply with the applicable provisions under the Articles of Association and the Listing Rules. Should a proposed asset acquisition fall within the categories of transactions which require the Board's or independent non-executive Directors' approval as required by the Articles of Association or the Listing Rules, such approval will be sought by the Company. The Company had no intention to acquire any other aeronautical or non-aeronautical businesses and assets from Parent Company as at the Latest Practicable Date. In addition, the Group and Parent Company have entered into several agreements under which Parent Company will provide services to the Group including power and energy supply and miscellaneous social services such as training and recreational services. Further details of these agreements are set out under "Connected Transactions" in this section.

Management of the Group

Parent Company has no intention to engage in or interfere with the day-to-day management of the Group. Parent Company will only exercise its rights and be responsible for its obligations as a controlling shareholder subject to the Articles of Association. Moreover, according to the relevant regulations issued by SETC and CSRC on 29th March, 1999 regarding the corporate governance of an overseas listed company, the Board of the Company is required to be independent from the controlling shareholder and shall not be under the control of the board of directors of Parent Company, the Company's controlling shareholder. The number of the senior management personnel (being the chairman, the vice-chairman and the executive directors) of Parent Company that holds an office in the Company as chairman, vice-chairman or executive director shall not exceed two. On the other hand, no one holding a management position in Parent Company can act as the general manager, deputy general manager, financial controller, sales controller or secretary of the Board of the Company. After the listing of the H Shares on the Stock Exchange, the Company will be subject not only to the relevant PRC laws and regulations but also to the Listing Rules which require various matters of the Company to be supervised and/or monitored by its auditors, the Joint Sponsors (for at least one year after the listing) as well as the Stock Exchange.

The Shareholders' Agreement also contains certain provisions regarding the manner in which the Group will be managed. Further details of these provisions are set out under "Relationship with the Strategic Investor" in this section.

Non-competition

By a non-competition agreement dated 25th October, 2002 (material contract (i) under paragraph B1 of Appendix X to this prospectus) between the Company and Parent Company, Parent Company has undertaken, among others, that (i) it will not carry on or be involved in any business or own any interest in any company carrying on business, which is or is likely to be in competition whether directly or indirectly, with the existing business of the Group; and (ii) the Company has a pre-emptive right in relation to development, operation and investment in any new aeronautical business or project, provided that:

(i) the Company remains its listing status at the Stock Exchange; and

(ii) Parent Company owns 30% or more of the issued share capital of the Company or controls the Board.

CONNECTED TRANSACTIONS

Upon the listing of the H Shares on the Stock Exchange and for so long as Parent Company and the Strategic Investor remain to be substantial shareholders or are otherwise regarded as connected persons (within the meaning of the Listing Rules) of the Group, and the Promoters other than Parent Company considered as connected persons (within the meaning of the Listing Rules), a number of transactions between the Group on the one hand and Parent Company, any other Promoters or the Strategic Investor and their respective associates (as defined in the Listing Rules) on the other hand which will constitute connected transactions as defined in the Listing Rules are expected to continue or to be entered into in the future.

A. Connected transactions between the Company and Parent Group ("Parent Group Transactions")

A1. *Indemnity*

By an indemnity agreement dated 25th October, 2002 (material contract (ii) under paragraph B1 of Appendix X to this prospectus) between the Company and Parent Company, Parent Company gave certain representations, undertakings, warranties and indemnities in favour of the Company in respect of the assets it has injected into or transferred to the Company since the incorporation of the Company, including, among others, an indemnity undertaking by Parent Company in respect of any tax liabilities in respect of the assets transferred to the Company and any contingent liabilities arising from or in connection with the construction capital, facilities and operation of facilities of the Meilan Airport before the incorporation of the Company.

Parent Company has also undertaken under the indemnity agreement that the contracts made in the name of Parent Company relating to the assets and related business assumed by the Company from Parent Company would be assigned and novated to the Company by Parent Company with the consent of the other contracting parties or will be held in trust by Parent Company for the benefit of the Company.

A2. *Purchase Option Agreement*

By the Purchase Option Agreement dated 30th May, 2002 and a supplemental agreement dated 25th October, 2002 (material contract (iii) under paragraph B1 of Appendix X of this prospectus), Parent Company has granted to the Company options to purchase from Parent Company any aeronautical or non-aeronautical businesses and assets owned or to be owned by Parent Company from time to time. Such options are exercisable at the sole discretion of the Company, in respect of the runway, at all times irrespective of whether or not Parent Company holds any Shares; and in respect of all other aeronautical or non-aeronautical businesses and assets owned or to be owned by Parent Company, at all times prior to the expiry of one year after Parent Company ceases to hold 10% of the share capital of the Company. The price of any business and assets purchased by the Company pursuant to such options will be determined based on the valuation of such business or assets by an independent valuer in accordance with relevant PRC laws. In addition, Parent Company has undertaken that it will not dispose of such business and assets during the term of the agreement without the prior written consent of the Company.

The Company has the right to require Parent Company to provide information relating to such assets and business of Parent Company from time to time. The Company can exercise the option at its own discretion, subject to satisfaction of all applicable approval and disclosure requirements including that of the Listing Rules.

A3. ***Asset Swap Agreement***

By the Asset Swap Agreement dated 30th May, 2002, and amended on 25th October, 2002 by a supplemental agreement (material contract (iv) under paragraph B1 of Appendix X to this prospectus), Parent Company has agreed to sell its interest in certain assets, which include (i) the cargo centre; (ii) a car park; (iii) a 60% interest in the registered capital of Meilan Travelling; and (iv) a 95% interest in the registered capital of DFG (together, the "**Parent's Swap Assets**"), to the Company. The Company has agreed to sell certain assets to Parent Company, which include (i) an equipment centre; (ii) certain power equipment; and (iii) a vehicle storage (together, the "**Company's Swap Assets**"). For further details of these swap assets, please refer to the sub-section headed "Restructuring of the Group" of this section.

The Parent's Swap Assets were sold to the Company at a total consideration of approximately RMB78.1 million, which is based on the valuation reports prepared by Hainan Zhong Li Xin dated 18th April, 2002. The assets sold from the Company to Parent Company, valued at approximately RMB28.2 million in total, were sold for a total consideration of approximately RMB28.4 million, which is the aggregate net book value of the assets. In respect of the difference between the considerations amounting to approximately RMB49.7 million, the Company has agreed to settle such amount in cash by three instalment payments within 12 months from 30th May, 2002.

A4. ***Airport Composite Services***

The Company and Parent Company entered into an airport composite services agreement on 25th October, 2002 (material contract (v) under paragraph B1 of Appendix X to this prospectus). According to this agreement, Parent Company has agreed to provide to the Group with the following services:

(i) security guard service;

(ii) cleaning and environment maintaining;

(iii) sewage and refuse processing;

(iv) power and energy supply and equipment maintenance; and

(v) passengers and luggages security inspection,

The charge rates for the above various services are as follows:

(i) the charges relating to the services of items (i)–(iv) above will be determined in accordance with the cost to Parent Company in providing such services plus a 5% mark-up as management fee, except for item (iv), the mark-up of which is 25% pursuant to the relevant pricing guideline set by CAAC.

(ii) the charges relating to the service of item (v) will be determined in accordance with the rate prescribed by CAAC and charged to the airline customers directly. The Company will collect on behalf of Parent Company such fees receivable from airline customers.

The charges will be settled on an annual basis, provided that the total amount chargeable under the airport composite services agreement shall not be higher than 8% of the total revenue of the Company (excluding Airport Fees) based on arms length negotiation between the parties concerned with reference to the nature of the services and historical costs. The term of the airport composite services agreement is for three years starting from 1st January, 2002 and is renewable.

A5. ***Agreement on Runway***

The runway at the Meilan Airport is owned and operated by Parent Company. Parent Company has been entitled to 25% of the aircraft movement fees (for domestic, Hong Kong, Macau and foreign airlines), passenger charges (for domestic airlines) and basic ground handling service fee (for Hong Kong, Macau and foreign airlines) collected from the airline customers for provision of the runway facilities and services since the inception of the Company. For the year ended 31st December, 2001, a total of RMB37,540,000, representing 20.3% of total revenues of the year, was received or receivable by Parent Company.

The Company and Parent Company has entered into the Agreement on Runway on 25th October, 2002 (material contract (vi) under paragraph B1 of Appendix X to this prospectus), which contains, inter alia, the following salient terms and conditions:

Parent Company's undertaking

Parent Company has agreed (i) to operate and maintain the runway in accordance with the applicable regulatory and industrial standards and keep the runway in good working condition; (ii) not to change the current usage of the runway unless approved by the relevant governmental departments and agreed in writing by the Company; (iii) not to dispose of any assets of or interests in the runway without agreement of the Company; and (iv) to continually hold the airport permit and maintain the validity thereof.

Indemnification

Parent Company has agreed to indemnify the Company and/or any third party any loss, damage, claim, fees and expenses which the Company and/or the third party may suffer as a result of or in connection with gross negligence or default in relation to the operation or maintenance of the runway or the airport permit.

Revenue Sharing

The Company and Parent Company have confirmed in the Agreement on Runway that the aircraft movement fees (for domestic, Hong Kong, Macau and foreign airlines), the passenger charges (for domestic airlines) and the basic ground handling services fees (for Hong Kong, Macau and foreign airlines) will be shared by the Company and Parent Company on such ratio as CAAC or any other regulatory authorities may from time to time prescribe, which as at the date of the agreement was on the basis of 75% to the Company and 25% to Parent Company, pursuant to the document《關於海口美蘭機場

有限責任公司與海南美蘭機場股份有限公司收入劃分比例的批覆》(總局財函[2002]77號) (Approval Relating to the Ratio of Splitting the Income between Haikou Meilan Airport Company Limited and Hainan Meilan Airport Company Limited (Zhong Ju Zai Han [2002] No. 77) issued by CAAC dated 27th September, 2002.

The Company will collect such fees on behalf of Parent Company and assume no liabilities in respect of default of payment by the airline customers.

Term of the agreement

The Agreement on Runway has a term of twenty years, subject to early termination upon, inter alia, mutual agreement between the parties, the purchase of the runway by the Company or the construction of a new runway by the Company itself.

Material changes

Pursuant to the Agreement on Runway, any material changes to the terms of the agreement are subject to the approval of the independent shareholders of the Company and compliance with the Listing Rules so long as the Company maintains its listing status on the Stock Exchange and Parent Company is regarded as a connected person of the Company as defined under the Listing Rules and the revised terms and/or conditions to the Agreement on Runway will be regarded as a new connected transaction.

Purchase option

Under the Purchase Option Agreement entered into on 30th May, 2002 and amended on 25th October, 2002, Parent Company has granted to the Company options to purchase from Parent Company the assets owned by Parent Company from time to time, including the runway assets, at a price to be determined by independent valuation. Please refer to the section "Business — Connected Transactions — Purchase Option Agreement" for details.

A6. ***Trademark Licensing Agreement***

Pursuant to a trademark licensing agreement dated 25th October 2002 entered into between the Company and Parent Company (material contract (vii) under paragraph B1 of Appendix X to this prospectus), in consideration of a nominal fee paid by Parent Company and the assistance to be provided by Parent Company in promoting the trademarks, the Company has granted to Parent Company a non-exclusive licence to use the trademarks set out in paragraph B2 of Appendix X to this prospectus in all the registered classes it has applied for a period of 10 years starting from 1st January, 2002.

Parent Company has undertaken, inter alia, that (i) it will not grant any further license to use the trademark to any third party without the prior written consent of the Company; and (ii) it will promote and market the brand of the Group at its own cost.

A7. ***Office Lease Agreement***

Pursuant to an office lease agreement dated 25th October, 2002 (material contract (viii) under paragraph B1 of Appendix X to this prospectus), the Company has agreed to rent from Parent Company office premises with a total gross floor area of 1,415 m^2 for a term of 5 years at an annual rental of RMB509,400 for the first three years which is adjustable thereafter based on agreement. Such office premises have been used as offices for the administrative departments of the Company since 1st January, 2002.

The annual rental under the Office Lease Agreement was determined with reference to recent market records available in Haikou City and on an arm's length basis between the Company and Parent Company. The Valuer is of the view that this rental is fair and reasonable.

A8. ***Transfer of Land Use Rights***

The Company will expand the capacity of the Terminal and cargo centre (for details of such expansion, please refer to the section headed "Future Plans and Use of Proceeds"). In preparation of such expansion, the Company has entered into an agreement on transfer of land use rights with Parent Company on 25th October, 2002 (material contract (ix) under paragraph B1 of Appendix X to this prospectus). According to the agreement, Parent Company has agreed to transfer the land use rights it holds in a parcel of land with a total area of approximately 39 hectares to the Company for a total consideration of RMB94,380,000, which is payable by one lump sum payment or by instalments within three years from the date of the listing of the H Shares on the Stock Exchange. The completion of the transfer of the land use rights is conditional upon the successful Offering. Transfer of the land use rights is to be funded by the Offering proceeds of the New H Shares as part of the funding for the airport expansion project.

The consideration under the agreement was determined with reference to recent market records available in Haikou City and standard land price published by the Haikou municipal government. The Valuer is of the view that the consideration under the agreement is fair and reasonable.

A9. ***Provision of Security for Bank Facilities***

Pursuant to a mortgage agreement dated 20th September, 2001 (material contract (x) under paragraph B1 of Appendix X to this prospectus) between the Company, Parent Company and China Development Bank, Parent Company has provided security using a portion of its land of a total area of 34.02 hectares, in which it owns the land use rights, in favour of China Development Bank in the PRC in relation to the bank loans granted by such bank to the Company. The aggregate principal amount of such secured bank loans was, as at 31st August, 2002, approximately RMB270,000,000 which will mature on the 20th December, 2008. The security provided by Parent Company for the bank loans will be discontinued upon the full settlement of the bank loans.

Parent Company has not charged and will not charge any fees in relation to the provision of such security, and no counter guarantees, indemnities or security was given by the Company to Parent Company. The Company obtained the written consent of China Development Bank on 4th November, 2002 to release the bank's security over the land use rights pledged by Parent Company as soon as practicable. The Company has undertaken to the Stock Exchange that it will use its best endeavours to complete the procedures regarding such release within three months from the date on which the H Shares are listed on the Stock Exchange. If the guarantee is not released after three months from the date of commencement of dealing in the H Shares, the Company will release an appropriate announcement. Thereafter this transaction will cease to be a connected transaction of the Company.

A10. ***Air ticket sales agency***

By an operation agreement dated 30th August, 2002 between the Company and HLAS, a company in which Parent Company holds a 95% equity interest, the Company has outsourced its air ticket sales business at Meilan Airport to HLAS in consideration of a fixed fee in the sum of RMB800,000 payable by the latter on an annual basis. The fixed fee is set based on estimation by the parties to the contract of the total profits to be generated from the air ticketing business each year.

The contractual arrangement has been in place since May 2001, and a total of RMB639,000 was paid to the Company for the year ended on 31st December, 2001.

The current agreement is for a term of one year starting from 1st September, 2002.

B. Connected transactions between the Group and the Promoters (excluding Parent Company) and their associates ("Promoters Group Transactions")

B1. *Connected Transactions between the Group and Hainan Airlines and its associates*

By contractual arrangements between the Company and Hainan Airlines and its associates in the ordinary course of business, the Company and Hainan Airlines and its associates have entered into the following connected transactions:

(i) the Company has been providing customary airport ground services including landing facilities, basic ground handling service, cargo storage and handling, passenger and baggage services and other related services to Hainan Airlines and its 51%-owned subsidiary, China Xinhua Airlines and its 89%-owned subsidiary, Shan Xi Airlines at rates prescribed by CAAC;

(ii) the Company has been leasing office and commercial areas and premises of approximately 925 m^2, 12 airport counters and an aircraft storage warehouse of approximately 200 m^2 to Hainan Airlines currently for an aggregate contractual rental of approximately RMB5,839,200 per year. The relevant lease agreements are made on different dates and on normal commercial terms. The Valuer is of the view that the rental under each of these leases is fair and reasonable;

(iii) Hainan Food has been providing the following catering services to the Company:

(a) By a catering service agreement dated 31st December, 2000, the Company has granted Hainan Food the right of provision of on-board catering service to the airlines using the Meilan Airport for a term of three years.

The annual franchise fee payable for such right is RMB4,380,000, which is payable to the Company on a quarterly basis.

(b) The Company and Hainan Food have entered into a catering service agreement on 25th December, 2001, pursuant to which Hainan Food has agreed to provide catering service to the passengers of delayed flights at the Meilan Airport. The current agreement is for a term of one year.

The charge for such catering services is determined on an arm's length basis and payable by the Company on a monthly basis.

(c) In order to prepare for the catering services, Hainan Food has rented from the Company a total floor area of 70 m^2 for storage and preparation of food pursuant to a lease agreement dated 25th May, 2001. The rental is RMB2,100 per month which was determined on an arm's length basis. For the year ended 31st December, 2001, RMB25,200 was paid to the Company as the rental. The annual rental under the lease agreement was determined with reference to recent market records available in Haikou City and on an arm's length basis between the Company and Hainan Food. The Valuer is of the view that this rental is fair and reasonable.

The following table shows the total sums paid or payable in respect of the transactions listed under item (i)–(iii) above between the Group and Hainan Airlines and its associates since 1st January, 1999:

	Year ended 31st December,			Five months ended 31st May,
	1999[(1)]	**2000**	**2001**	**2002**
		(RMB'000)		
Ground handling services	23,511	48,635	53,821	23,219
Leasing of commercial premises	3,116	4,775	5,899	2,415
Catering services	1,024	1,700	4,380	1,825

(1) Commercial operations of the Meilan Airport commenced on 25th May, 1999. Accordingly, the relevant data for 1999 reflects only seven months of commercial operations and therefore are not directly comparable with those of the subsequent years.

B2. *Connected transactions between the Group and China Southern Airlines and its associates*

By contractual arrangements between the Group and China Southern Airlines and its associates in the ordinary course of business:

(i) the Company has been providing customary airport ground handling services including landing facilities, basic ground handling service, passenger and baggage security checks and other related services to (a) China Southern Airlines and Xia Men Airlines Company Limited (廈門航空公司), a 60% owned subsidiary of China Southern Airlines, at rates prescribed by CAAC and; (b) Zhuhai Helicopter Company Limited (珠海直升機公司), a 100% subsidiary of China Southern Airlines (Group) Company (中國南方航空(集團)公司), the controlling shareholder of China Southern Airlines for a lump sum fee in the amount of RMB900 per flight;

(ii) the Company has been leasing office and commercial areas and premises of 1,398 m^2 and 15 airport counters to China Southern Airlines (Group) Company's Hainan Branch and China Southern Airlines' Hainan Branch currently for an aggregate contractual rental of approximately RMB6,442,800 per year. The relevant lease agreements are made on different dates and on normal commercial terms. The annual rentals under those lease agreements were determined with reference to recent market records available in Haikou City and on an arm's length basis between the Group and China Southern Airlines' (Group) Company's Hainan Branch/China Southern Airlines' Hainan Branch. The Valuer is of the view that those rentals are fair and reasonable;

(iii) Meilan Advertising, a subsidiary 95% directly owned by the Company, has been providing advertising services to China Southern Airlines' Hainan Branch at standard rates charged to other clients.

The following table shows the total sums paid or payable in respect of the transactions between the Group and China Southern Airlines and its associates since 1st January, 1999:

	Year ended 31st December,			Five months ended 31st May,
	1999[(1)]	2000	2001	2002
	(RMB'000)			
Ground handling services	16,911	31,462	40,071	17,161
Lease of counters, premises and office	3,675	5,483	5,483	2,285
Advertising services	456	437	241	92

(1) Commercial operations of the Meilan Airport commenced on 25th May, 1999. Accordingly, the relevant data for 1999 reflects only seven months of commercial operations and therefore are not directly comparable with those of the subsequent years.

B3. *Connected transactions between the Group and HNA Group and its associates*

By contractual arrangements between the Group and HNA Group and its associates (as defined under the Listing Rules) in the ordinary course of business:

(i) the Group has been providing customary airport ground handling services including landing facilities, basic ground handling services, passenger and baggage security checks and other related services to Golden Deer Aircraft Company Limited (金鹿公務機有限公司), a company in which HNA Group holds a 65% equity interest, at such rates as prescribed by CAAC.

(ii) the Company has outsourced the operation and management of the cargo centre of the Company to Yangzi Express, a subsidiary 85% owned by HNA Group, for a fixed annual fee of RMB18,000,000 payable by Yangzi Express to the Company for a term starting from 1st June, 2002 to 31st December, 2003.

(iii) Hainan HNA Information System Company Limited (海南海航航空信息系統有限公司), a subsidiary 70% owned by HNA Group, has entered into an agreement dated 1st August, 2002 to provide procurement, maintenance, system integration and management services to the Company in respect of the electronic devices, computer and telecommunication equipment and system installed or used at Meilan Airport for fees negotiated on arm's length basis between the parties;

(iv) the Group has been leasing commercial areas and premises of approximately five m^2 for a rental of RMB24,000 per year to Hainan Haihang Jinpeng Airlines Trading Company Limited (海南海航金鵬航空銷售有限公司), a company in which HNA Group holds 70% equity interest. The annual rental under the lease agreement was determined with reference to recent market records available in Haikou City and on an arm's length basis between the Group and Hainan Haihang Jinpeng Airlines Trading Company Limited. The Valuer is of the view that those rentals are fair and reasonable.

(v) HNA Group has agreed pursuant to a logistic composite service agreement (material contract (xii) under paragraph B1 of Appendix X to this prospectus) effective from 1st January, 2002 to provide and procure its subsidiaries to provide the Group with logistic services including (a) staff training; (b) staff shuttle bus services; (c) staff cafeteria services; (d) vehicle maintenance; and (e) appliance procurement.

Charges as to the service of item (a) will be at cost for providing such services as shared by HNA Group, the Company and other relevant companies on a pro rata basis with reference to the respective headcounts; and the charges as to items (b) and (c) will be at a fixed price with reference to relevant cost per headcount; and the charges as to items (d) and (e) will be the cost for providing such services plus a 5% and a 1% mark-up as management fee, respectively.

(vi) HNA Group has provided guarantees in favour of China Development Bank in relation to two short-term bank loans granted by the bank to the Company respectively in the amount of RMB20 million and RMB50 million, which will be due on 27th December, 2002 and 9th September, 2003, respectively. HNA Group did not and will not charge any fee for provision of the guarantee, and the Company did not and will not provide any counter guarantee in favour of HNA Group. The Company obtained the written consent of China Development Bank on 4th November, 2002 to release HNA Group's aforesaid guarantees as soon as practicable. The Company has undertaken to the Stock Exchange that it will use its best endeavours to complete the procedures regarding such release within three months from the date on which the H Shares are listed on the Stock Exchange. If the guarantees are not released after three months from the date of commencement of dealing in the H Shares, the Company will release an appropriate announcement. Thereafter this transaction will cease to be a connected transaction of the Company.

The following table shows the total sums paid or payable in respect of the transactions (except for item (vi)) between the Group and HNA Group and its associates since 1st January, 1999:

	Year ended 31st December,			**Five months ended 31st May,**
	1999(1)	**2000**	**2001**	**2002**
		(RMB'000)		
Ground handling facilities charge	N/A	N/A	12	7
Operation of cargo centre	4,958	8,500	—	—
Electronic system maintenance	N/A	N/A	N/A	N/A
Lease of commercial premises	N/A	N/A	25	10
Logistic composite services	N/A	N/A	N/A	1,707

(1) Commercial operations of the Meilan Airport commenced on 25th May, 1999. Accordingly, the relevant data for 1999 reflects only seven months of commercial operations and therefore are not directly comparable with those of the subsequent years.

C. Connected Transaction between the Company and an associate of the Strategic Investor (“Strategic Investor Transaction”)

Pursuant to the Technical Services Agreement dated 16th September, 2002 and amended on 30th October, 2002 (material contract (xiii) under paragraph B1 of Appendix X to this prospectus) between the Company and CADI, a wholly-owned subsidiary of the Strategic Investor, CADI has agreed to provide certain technical and consultancy services in respect of the long-term management and development of the Meilan Airport. Such services include (but are not limited to) advising on the business development, investment opportunities, infrastructure and capacity planning and international marketing at the Meilan Airport.

The Company is required to pay fees to CADI which consist of a fixed fee component and a performance-related component (save that only the fixed fee component is payable for the year 2002). The fixed fee component will be calculated by reference to the number of consultant-days used in providing the technical and consultancy services and based on the rate of US$1,000 per consultant-day, and is payable irrespective of operating results. The performance-related component is calculated by reference to the Company’s actual EBITDA and excess EBITDA above a pre-determined minimum level, in each case expressed as a percentage of such EBITDA. The Company shall also pay to CADI the expenses and disbursements incurred by CADI in relation to the technical and advisory services, provided that the expenses and disbursements shall not on average per quarter exceed US$200 per consultant-day.

The Technical Services Agreement will become effective upon satisfaction of certain conditions precedent, including the commencement of trading of the H Shares on the Stock Exchange and will expire on 31st December, 2012, subject to earlier termination.

APPLICATION FOR WAIVER — ON-GOING CONNECTED TRANSACTIONS

The Parent Group Transactions, the Promoters Group Transactions and the Strategic Investor Transaction described above are expected to occur or continue in the future, except for (i) exempt connected transactions listed below, (ii) the exercise of purchase options referred to in paragraph A2 above, which will be subject to the relevant provisions of the Listing Rules in the event the relevant options are exercised, (iii) the asset swap referred to in paragraph A3 above and (iv) the land use rights transfer referred to in paragraph A8 above which have been entered into during the Restructuring and are one-off transactions.

The Directors (including independent non-executive Directors) are of the view that the Parent Group Transactions, the Promoters Group Transactions and the Strategic Investor Transaction described above have been entered into on an arm’s length basis and/or in the ordinary course of business of the Group, and on commercial terms that are fair and reasonable to the Company and its shareholders as a whole.

Having reviewed the information and documents provided by the Company relating to the Parent Group Transactions, the Promoters Group Transactions and the Strategic Investor Transaction and the views of the Valuer (as to the relevant lease arrangements mentioned above), and in reliance upon representations of the Company and its Directors, the Joint Sponsors are of the view that the Parent Group Transactions, the Promoters Group Transactions and the Strategic Investor Transaction have been entered into on an arm's length basis and/or in the ordinary course of business of the Company and are fair and reasonable as far as the shareholders of the Company are concerned.

The Parent Group Transactions and the Strategic Investor Transaction would constitute connected transactions for the Company under the Listing Rules once the H Shares are listed on the Stock Exchange and for so long as Parent Company and the Strategic Investor remain substantial shareholders of the Company. The Promoters Group Transactions would constitute connected transactions for the Company under the Listing Rules once the H Shares are listed on the Stock Exchange and for so long as each of Hainan Airlines, HNA Group and China Southern Airlines is considered a connected person of the Company and each of their relevant associates remains an associate (within the meaning under the Listing Rules) of such Promoters. China Southern Airlines will cease to be a shareholder of the Company upon the completion of the Offering.

Exempt Connected Transactions

Pursuant to the Listing Rules and in light of the actual or anticipated annual amount which has been or will be generated under each of the Parent Group Transactions, the Promoter Group Transactions and the Strategic Investor Transaction, the following transactions fall into the exempt connected transactions as provided under Rule 14.24 of the Listing Rules.

Type of connected transactions	Applicable Listing Rules
A. Parent Group Transactions	
(i) transaction under the indemnity agreement as described in paragraph A1	Rule 14.24(8)
(ii) trademark licensing arrangement as described in paragraph A6	Rule 14.24(5)
(iii) office lease arrangement as described in paragraph A7	Rule 14.24(5)
(iv) provision of security for bank facilities as described in paragraph A9	Rule 14.24(8)
(v) air ticketing agency arrangement as described in paragraph A10	Rule 14.24(5)
B. Promoters Group Transactions	
(i) ground catering services as described in paragraph B1 (iii) (b)	Rule 14.24(5)
(ii) lease of commercial area as described in paragraph B1 (iii) (c)	Rule 14.24(5)
(iii) advertising services as described in paragraph B2 (iii)	Rule 14.24(5)
(iv) ground handling services as described in paragraph B3 (i)	Rule 14.24(5)
(v) computer system maintenance as described in paragraph B3 (iii)	Rule 14.24(5)
(vi) lease of commercial area as described in paragraph B3 (iv)	Rule 14.24(5)
(vii) provision of corporate guarantee as described in paragraph B3 (vi)	Rule 14.24(8)

Non-exempt Connected Transactions

Pursuant to the Listing Rules and save for (i) exempt connected transactions listed above, (ii) the exercise of purchase options referred to in paragraph A2 above, which will be subject to the relevant provisions of the Listing Rules in the event the relevant options are exercised, (iii) the asset swap referred to in paragraph A3 above and (iv) the land use rights transfer referred to in paragraph A8 above which have been entered into during the Restructuring and are one-off transactions, each of the Parent Group Transactions, the Promoters Group Transactions and the Strategic Investor Transaction may require full disclosure and prior approval by independent shareholders, depending on the nature and value of the transaction. However, since such transactions will be conducted in the ordinary course of business of the Company on a regular basis, the Directors consider it impractical to make disclosure of or, where necessary, obtain shareholders' approval for, each of such transactions. Accordingly, the Company has applied to the Stock Exchange that a general waiver be granted to the Company from complying with the relevant requirements of the Listing Rules in respect of the Promoters Group Transactions, the Parent Group Transactions and the Strategic Investor Transaction (excluding (i) exempt connected transactions listed above, (ii) the exercise of purchase options referred to in paragraph A2 above, which will be subject to the relevant provisions of the Listing Rules in the event the relevant options are exercised, (iii) the asset swap referred to in paragraph A3 above and (iv) the land use rights transfer referred to in paragraph A8 above which have been entered into during the Restructuring and are one-off transactions) and matters arising out of or in connection with such transactions (together the "**Transactions**") for a period of three financial years commencing from the year of listing of the H Shares on the Stock Exchange, save and except for the waiver for the Agreement on Runway for a term of 20 years and the Technical Services Agreement for a term of 10 years.

The aforesaid waiver is granted by the Stock Exchange subject to the following conditions:

1. the Transactions are:

   (a) entered into by the Group in the ordinary and usual course of its business;

   (b) conducted either (i) on normal commercial terms (which expression will be applied by reference to transactions of a similar nature and to be made by similar entities) or (ii) (where there is no available comparison) on terms that are fair and reasonable so far as the shareholders of the Company are concerned; and

   (c) entered into either (i) in accordance with the terms of the agreements governing such Transactions or (ii) where there are no such agreements, on terms no less favourable than those available to or from independent third parties;

2. the annual aggregate amount in respect of the relevant type of Transactions in any financial year shall not exceed a specified amount or a specified percentage of the audited and consolidated total revenues ("**Total Revenues**") or net tangible assets ("**NTA**") of the Company in the relevant financial year, as the case may be ("**Cap**"):

Type of connected transactions			Cap	Waiver under Listing Rules
			(RMB'000)	
A	**Transactions between the Company and Parent Group**			
	(i)	Airport composite service: items (a)–(d) as described in paragraph A4. .	8% of the Total Revenue (excluding Airport Fee)	Rule14.25
		item (e) as described in paragraph A4. .	fees receivable for security inspection prescribed by CAAC	Rule14.25
	(ii)	Agreement on Runway as described in paragraph A5	25% of the aircraft movement fees (for domestic, Hong Kong, Macau and foreign airlines), passenger charges (for domestic airlines) and basic ground handling fees (for Hong Kong, Macau and foreign airlines)	Rule14.26
B1	**Transactions between the Group and Hainan Airlines and its associates**			
	(i)	Ground handling services as described in paragraph B1(i) . .	70,000	Rule14.26
	(ii)	Lease of office and commercial premises as described in paragraph B1(ii)	6,500	Rule14.25
	(iii)	on-board catering fees as described in paragraph B1(iii)(a)	4,380	Rule14.25
B2	**Transactions between the Group and China Southern Airlines and its associates**			
	(i)	Ground handling services as described in paragraph B2(i) . .	52,000	Rule14.26
	(ii)	Lease of office and commercial premises as described in paragraph B2(ii)	7,000	Rule14.25

Type of connected transactions	Cap	Waiver under Listing Rules
	(RMB'000)	
B3 Transactions between the Group and HNA Group and its associates		
(i) Operation of cargo centre as described in paragraph B3(ii) . .	18,000	Rule14.25
(ii) Logistic composite services as described in paragraph B3(v) . .	6,500	Rule14.25
C Transaction between the Company and an associate of the Strategic Investor		
Technical services as described in paragraph C	3% of the book value of NTA	Rule14.25

3. the independent non-executive Directors shall review the Transactions annually and confirm in the Company's next and each successive annual report that the Transactions have been conducted in the manner as stated in paragraphs 1 and 2 above;

4. summary of the Transactions as required under Rule 14.25(1)(A) to (D) of the Listing Rules shall be included in the Company's annual report and accounts for the relevant year;

5. the Company's auditors must review the Transactions annually and confirm in a letter (the "**Letter**") to the Directors (with a copy to the Listing Division of the Stock Exchange) as to whether:

   (i) the Transactions have received the approval of the Board;

   (ii) the Transactions are in accordance with the pricing policies as stated in the Company's annual report;

   (iii) the Transactions have been entered into in accordance with the terms of the agreements governing the Transactions or, if there are no such agreements, on terms no less favourable than those available to or from independent third parties; and

   (iv) the Transactions have exceeded the cap amounts, as stated in paragraph 2 above.

   If, for whatever reason, the auditors decline to accept the engagement or are unable to provide the Letter, the Directors must contact the Listing Division immediately;

6. the Company and its subsidiaries and the connected persons (except China Southern Airlines) must provide to the Stock Exchange an undertaking before the date of listing of the H Shares of the Company that, for so long as any of the Company's Shares are listed on the Stock Exchange, they will provide the Company's auditors with full access to their relevant records for the purpose of the auditors' review in respect of the Transactions. With respect to the Transactions relating to China Southern Airlines and its associates,

Ernst & Young, the Company's auditors, have confirmed that they do not require access to the relevant books and records of China Southern Airlines and its associates for the purpose of their review in respect of these transactions; and

7. if any terms of the Transactions as mentioned above are altered or if the Company enters into any new agreement with any connected person (within the meaning of the Listing Rules) in the future, the Company must comply with the provisions of Chapter 14 of the Listing Rules governing connected transactions unless it obtains a separate waiver from the Stock Exchange.

C. Transactions between the Company and its subsidiaries

Transactions between the Company and its subsidiaries are in relation to leasing of offices and commercial premises. According to Rules 14.24(4) and (5) of the Listing Rules, since the transactions between the Company and its subsidiaries are on normal commercial terms in their ordinary course of business and either there is no substantial shareholders other than the Company in such subsidiaries or the total value of each of such transactions each year is less than the amount set out in Rule 14.24(5), such transactions are not normally subject to any disclosure or shareholders approval requirements.

RELATIONSHIP WITH THE STRATEGIC INVESTOR

Overview

The Strategic Investor is one of Europe's listed airport companies, with a market capitalisation of approximately DKK4,659 million (US$621.0 million) as at the Latest Practicable Date. The Strategic Investor has interests in 13 airports, with a total passenger throughput of over 33 million passengers per annum, in Denmark, Norway, Mexico and the United Kingdom. The largest of these airports is Copenhagen Airport in Denmark, which has a passenger throughput of over 18 million passengers per annum. Copenhagen Airport is the intercontinental hub for SAS (Scandinavian Airlines), one of the European hubs for the Star Alliance airline group and the North-European hub for DHL. Copenhagen Airport won the IATA "Best Airport in the World Award" in both 2000 and 2002 and has also previously been rated as Europe's best airport. It has been ranked highest in such areas as airport-related infrastructure, customer service and shopping and dining facilities.

The Strategic Investor has conditionally agreed to subscribe for the Strategic Placing Shares through the Strategic Placing Underwriter pursuant to the Strategic Investment Agreement. Immediately following completion of the Offering (including any exercise of the Over-allotment Option), the Strategic Investor will hold approximately 20% of the enlarged issued share capital of the Company. The Strategic Investor's aggregate shareholding in the Company immediately following completion of the Offering will not be affected by any allocation of H Shares between the Public Offer and the International Placing (excluding the Strategic Placing).

The Strategic Investor, Parent Company and HNA Group entered into a conditional Shareholders' Agreement on 16th September, 2002. The Shareholders' Agreement is conditional upon, inter alia, (a) the satisfaction of certain obligations by the Strategic Investor in respect of the subscription of the Strategic Placing Shares under the Strategic Investment Agreement; (b) the Technical Services Agreement having been duly executed and not having been terminated in accordance with its terms as at the date of listing of H Shares on the Stock Exchange; (c) the Stock Exchange having granted approval for the listing of H Shares on the Stock Exchange; and (d) the H Shares having commenced trading on the Stock Exchange.

Board Representation

Both the Shareholders' Agreement and the Strategic Investment Agreement provide that the Strategic Investor will be permitted to appoint one executive director and one non-executive director to the Board, for so long as it holds not less than 75% of the Strategic Placing Shares and 7.5% of the Company's issued and outstanding share capital from time to time.

Board Reserved Matters

Subject to compliance with the applicable laws, regulations and rules, there are a number of matters which, pursuant to the Shareholders' Agreement, can only be approved by the Board if none of the Directors nominated by Parent Company or the executive Director appointed by the Strategic Investor has voted against such matter at the relevant Board meeting. These matters include the approval of any 5-year rolling business and investment plans of the Company, any change in auditors to the Company, any amendment to the Articles, any material change in or expansion of the activities of the Group, any transaction or arrangement which has a material impact on the Group's business or the relationship between the shareholders of the Company, and the delisting the H Shares from the Stock Exchange.

Restrictions on Further Acquisition of Shares

The Strategic Investor has undertaken not to purchase or subscribe for any additional H Shares so as to increase its shareholding in the Company to more than 25% of the issued share capital of the Company without the prior written consent of the Company.

Restrictions on Disposal of Shares

The Strategic Investor has undertaken to the Company, Parent Company and HNA Group that it will not dispose of any of the Strategic Placing Shares for a period of 12 months following the commencement of dealings in the H Shares on the Stock Exchange. It has also undertaken to the Company, Parent Company and HNA Group that: (a) it will not dispose of any of the Strategic Placing Shares for a period of 6 months following the expiry of the 12-month period after the commencement of dealings in the H Shares on the Stock Exchange without the prior written consent of the Company; and (b) in the event of any disposal of any interest in the Strategic Placing Shares, it will take all reasonable steps to ensure that such disposal will be in accordance with the terms of the Strategic Investment Agreement and will not create a disorderly or false market for any class of shares of the Company.

The Strategic Investor has also undertaken in favour of the Company, Parent Company and HNA Group that, notwithstanding termination of the Shareholders' Agreement and for so long as Parent Company shall remain as the single largest shareholder of the Company, it will not knowingly dispose of or transfer any of its H Shares to any party which carries on or is engaged in carrying on airport services or any party which holds an equity interest in any airports (except where the disposal is made to professional investment funds or financial institutions whose ordinary course of business is investment in securities).

The Strategic Investor has further undertaken to Parent Company and HNA Group that in the event of any proposed disposal of H Shares by the Strategic Investor, subject to the provisions of the Shareholders' Agreement and further subject to compliance with the Listing Rules and all applicable laws and regulations, Parent Company, Hainan Airlines and HNA Group (or their respective nominees) (collectively referred to as the "**Offerees**") shall each be given by way of written notice the first right of refusal in acquiring the H Shares so proposed to be disposed with reference to their shareholdings in the Company as at the date of such written notice.

Each of Parent Company and HNA Group has undertaken to the Strategic Investor that in the event of any disposal of Domestic Shares by any of Parent Company and HNA Group, subject to compliance with the Articles and all applicable PRC laws, regulations, rules, government directives and administrative guidelines, the other shareholders holding Domestic Shares ("**Other Domestic Shareholders**") shall be given by way of written notice the first right of refusal in acquiring any such Domestic Shares so proposed to be disposed ("**Sale Domestic Shares**"). In the event that any Sale Domestic Shares are not acquired by the Other Domestic Shareholders, the Strategic Investor (or its nominee) shall be given by way of written notice the second right of refusal in acquiring such untaken Sale Domestic Shares, provided that the aggregate shareholding of the Strategic Investor and its affiliates and nominees shall not exceed 25% of the Company's issued share capital as a result of exercise of such right.

Each of Parent Company and HNA Group has further undertaken to the Strategic Investor that, notwithstanding termination of the Shareholders' Agreement and for so long as the Strategic Investor holds 7.5% of the Company's issued share capital, it will not transfer or otherwise dispose of its Domestic Shares to any party which carries on or is engaged in carrying on airport services or any party which holds an equity interest in any of such airports (except where the disposal is made to professional investment funds or financial institutions whose ordinary course of business is investment in securities or where the disposal is made pursuant to a share swap arrangement between Parent Company or HNA Group, as the case may be, and the transferee which arrangement shall result in the interest in the relevant airport being held by the Company).

Parent Company has further undertaken to the Strategic Investor that it will, at all times, remain the single largest shareholder of the Company holding a 30% interest in the share capital of the Company.

Non-competition Undertakings

The Strategic Investor has undertaken in favour of the Company, Parent Company and HNA Group that, unless jointly with the Company by way of co-investment pursuant to the terms of the Shareholders' Agreement, the Strategic Investor will not, and will procure that its affiliates not to, compete with the Company by carrying on or being engaged, concerned or otherwise interested in, directly or indirectly, whether as shareholder, director, partner, agent, or consultant in any PRC airports (excluding Hong Kong, Macau and Taiwan) within the proximity of 800 kilometres from the Meilan Airport or any airports located within the Yunnan province of the PRC (the "**Restricted Airports**").

Co-investment Rights

For so long as the Shareholders' Agreement remains effective, where an opportunity to invest ("**Investment Opportunity**") in a PRC airport ("**Target**") arises:

(a) if such Investment Opportunity is introduced by the Company, subject to the Company deciding to participate in such investment, the Company shall offer the Strategic Investor a right to co-invest in not less than 20% of the total investment being proposed to the Company. However, if the Company declines in writing to proceed with the investment for any reason whatsoever, the Strategic Investor shall be entitled to proceed with participation in such investment on its own account unless the Target is one of the restricted airports under the Shareholders' Agreement; and if the Strategic Investor declines in writing to proceed with the investment for any reason whatsoever, the Company shall be entitled to proceed with the investment on its own account;

(b) if the Investment Opportunity is introduced by the Strategic Investor and/or its Affiliates, subject to the Strategic Investor deciding to participate in such investment, the Strategic Investor shall offer the Company a right to co-invest in such investment so that the Company can participate in not less than 50% of the total investment being proposed to the Strategic Investor. However, if the Company declines in writing to proceed with the investment for any reason whatsoever, the Strategic Investor shall be entitled to proceed with participation in such investment on its own account unless the Target is one of the restricted airports under the Shareholders' Agreement; and if the Strategic Investor declines in writing to proceed with the investment for any reason whatsoever, the Company shall be entitled to proceed with participation in such investment on its own account; and

(c) if the Investment Opportunity is presented to both the Strategic Investor and/or its Affiliates and the Company, the Strategic Investor shall have the right to participate in not less than 30% of the total investment being presented, and the Company shall have the right to participate in the remaining percentage of such total investment. However, if the Company declines in writing to proceed with the investment for any reason whatsoever, the Strategic Investor shall be entitled to proceed with participation in such investment on its own account unless the Target is one of the restricted airports under the Shareholders' Agreement; and if the Strategic Investor declines in writing to proceed with the investment for any reason whatsoever, the Company shall be entitled to proceed with participation in such investment on its own account,

provided that, in each case, (i) the right to co-invest is subject to negotiations with and acceptance by the relevant Target; and (ii) any failure to respond to the investment proposal within two weeks of its being made shall be deemed a declination in writing.

Duration of the Shareholders' Agreement

The Shareholders' Agreement will, after the satisfaction of the conditions precedent, continue to be effective until:

(a) the collective shareholding of the Strategic Investor and its wholly-owned subsidiaries in the Company falling either below 75% of the Strategic Placing Shares or 7.5% of the Company's issued share capital, whichever occurs earlier;

(b) any party thereto committing a material breach which breach is not rectified within 30 days from the first written demand issued by any non-defaulting party thereto;

(c) the termination of the Technical Services Agreement; or

(d) certain events of default, such as winding up or creditor composition or appointment of liquidator, takes place against any one of the parties thereto and if the other non-defaulting parties thereto so agree and elect.

Technical Services Agreement

The Company and CADI, a wholly-owned subsidiary of the Strategic Investor, have also entered into the Technical Services Agreement for the provision by CADI to the Group of certain technical and advisory services in respect of the long-term management and development of the Meilan Airport. Such services include (but are not limited to) advising on the business development, investment opportunities, infrastructure and capacity planning and international marketing in respect of the Meilan Airport. CADI has undertaken to the Company that it will not, for the duration of the Technical Services Agreement, provide services that are identical or similar to such technical and advisory services in respect of any Restricted Airport, save for any business in which the Company has an equity interest or participates.

The Technical Services Agreement is conditional upon (a) the Strategic Investment Agreement having been executed and becoming unconditional in all respects; (b) the Shareholders' Agreement having been executed; (c) the Stock Exchange having granted approval to the listing of and permission to deal in the H Shares on the Stock Exchange; and (d) the H Shares having commenced trading on the Stock Exchange. The Technical Services Agreement, once it has become unconditional and effective, shall remain in effect until its expiration on 31st December, 2012 unless otherwise terminated earlier pursuant to its terms.

In consideration of the provision of technical and advisory services pursuant to the terms of the Technical Services Agreement, the Company is required to pay certain fees to CADI which will consist of a fixed fee component and a performance-related component (save that only the fixed fee component is payable for the year 2002). The fixed fee component will be calculated by reference to the number of consultant-days used in providing the technical and advisory services and based on the rate of US$1,000 per consultant-day, and is payable whether or not profitable results are achieved. The performance-related component will be calculated by reference to the Company's actual EBITDA and excess EBITDA above a pre-determined minimum level, in each case expressed as a percentage of such EBITDA. The Company is also required to pay to CADI the expenses and disbursements incurred by CADI in relation to the technical and advisory services provided that the expenses and disbursements shall not on average per quarter exceed US$200 per consultant-day.

The Technical Services Agreement will terminate upon, amongst other things, (a) a material breach of any terms of the Technical Services Agreement that is not rectified; (b) the Strategic Investor and its wholly-owned subsidiaries collectively holding less than 75% of the Strategic Placing Shares, which will represent approximately 15% of the enlarged issued share capital of the Company immediately after the completion of the Offering (including any exercise of the Over-allotment Option); or (c) CADI ceasing to be a direct or indirect wholly-owned subsidiary of the Strategic Investor.

If the Strategic Investor disposes of any part of the Strategic Placing Shares after the lock-up period described in the paragraph headed "Restrictions on Disposal of Shares" above to the extent that it and its wholly-owned subsidiaries collectively hold less than 75% of the Strategic Placing Shares, the Technical Services Agreement will terminate automatically. However, if the Strategic Investor ceases to be a substantial shareholder of the Company because of new issue of Shares by the Company and not because of the disposal of the Strategic Placing Shares by the Strategic Investor, then there will be no impact on the term of the Technical Services Agreement.

Long Term Commercial Benefits

The Directors believe that the Group will benefit from the Strategic Investor's involvement in the Company in the long term for the following reasons:

(a) The Strategic Investor is one of Europe's listed airport companies. It has a good reputation in the industry for its airport management capability. The Directors believe that the association with the Strategic Investor will enhance the management of the Meilan Airport on a long term basis.

(b) In accordance with the terms of the Shareholders' Agreement, the Strategic Investor will participate in the Company's management by appointing one executive Director and one non-executive Director to the Board. The Directors are of the view that the Strategic

Investor's involvement in the Company's management will be of strategic significance to the Company. In particular, the Company's existing management will become directly exposed to the international airport management culture and may benefit from the international experience of the Directors to be nominated by the Strategic Investor.

(c) CADI will provide technical and advisory services to the Company for a period of 10 years pursuant to the terms of the Technical Services Agreement. With its proven track record and international experience, CADI's service to the Company in the next 10 years will help improve the management of the Meilan Airport and increase its operating efficiency to reach international standards.

Waiver on Rule 19A.14(2)(a)(i) of the Listing Rules

Since the Strategic Investor will own approximately 20% of the entire issued share capital of the Company immediately upon completion of the Offering, it will become a connected person of the Company as the term is defined under the Listing Rules and the H Shares held by it will not be regarded as H Shares held by the public. Rule 19A.14(2)(a)(i) of the Listing Rules requires that all H Shares must be held by the public except as otherwise permitted by the Stock Exchange in its discretion. Accordingly, an application has been made by the Company to the Stock Exchange to seek waiver from strict compliance with Rule 19A.14(2)(a)(i) of the Listing Rules.

The Stock Exchange has granted a waiver from strict compliance with Rule 19A.14(2)(a)(i) of the Listing Rules on the following conditions:

1. the H Shares held by the public normally must constitute not less than 10% of the total existing issued share capital of the Company from time to time;

2. the aggregate amount of H Shares and such other securities which are held by the public must constitute not less than 25% of the total existing issued share capital of the Company from time to time; and

3. the Strategic Investor will give undertakings to the Company and the Stock Exchange that for so long as the H Shares continue to be listed on the Stock Exchange and the Strategic Investor continues to be a substantial shareholder (as defined in the Listing Rules) of the Company and:

   (a) in the event that the Strategic Investor is beneficially or legally interested in more than 44.47% of the entire issued H Share capital of the Company, the voting power to be exercised by the Strategic Investor at general meetings of holders of any class shares of the Company shall not be more than 44.47% of the voting power to be exercised at general meetings of holders of such class shares of the Company; and

   (b) in the event that a conflict of interest exists at any general meeting of holders of any class shares of the Company, the Strategic Investor will have to consult with the Stock Exchange prior to such voting in order to ensure that the Strategic Investor does not use its position as a substantial shareholder to the detriment of the other independent shareholders, and will have to abide by any instructions given to the Strategic Investor by the Stock Exchange following such consultations.

The Strategic Investor has given the undertakings referred to in paragraph 3 above to the Company and the Stock Exchange respectively.

The Board consists of seven Directors, two of whom are independent non-executive Directors. The Directors are elected at the inaugural meeting and meetings of the shareholders of the Company each for a term of three years, renewable upon re-election and re-appointment. The functions and duties conferred on the Board include: convening shareholders' meetings and reporting its work to the shareholders' meetings, implementing the resolutions of the shareholders' meetings, determining the Company's business plans and investment plans, formulating the Company's annual budget and final accounts, formulating the Company's proposals for dividend and bonus distributions and for the increase or reduction of capital, as well as exercising other powers, functions and duties as conferred by the Articles of Association.

Upon the Shareholder's Agreement becoming unconditional, the Strategic Investor will be entitled to appoint one executive director and one non-executive director to the Board. Please refer to "Relationship with the Strategic Investor" in the "Business" section for further details.

The Company Law requires a joint stock limited company to establish a supervisory committee and this requirement is reflected in the Articles of Association. The supervisory committee consists of three Supervisors, two of whom are shareholders' representatives who are elected, and may be removed, by the shareholders in a general meeting and one of whom is a representative of the employees and shall be elected and removed by employees. The term of service of the Supervisors is three years, renewable upon re-election and re-appointment. The functions and powers conferred on the supervisory committee include: attending board meetings, examining the Company's financial affairs and overseeing the actions of the Directors, general managers and other senior management personnel of the Company against any acts which contradict laws, regulations and the Articles of Association in carrying out their duties.

DIRECTORS

Executive directors

Mr. Chen Wenli (陳文理), 39, was appointed as an executive Director and Chairman of the Company in December 2000 in charge of the overall administration and business policy of the Group. He graduated from China Civil Aviation Institute, Tianjin, the PRC in 1985 with an aeronautical engineering degree. In 1986, Mr. Chen obtained a license from the Federal Aviation Administration Airman Certification Branch. From March 1991 to August 1998, Mr. Chen served as the general manager of the maintenance engineering department, senior assistant to managing director and a director of Hainan Airlines, respectively. Since August 1998 to August 2002, Mr. Chen served as assistant to general manager and chief executive officer of Parent Company, respectively. Mr. Chen is currently a director of Hainan Airlines and HNA Group.

Mr. Zhang Han'an (張漢安), 57, was appointed as an executive Director and the general manager of the Company in December 2000. Mr. Zhang has over 20 years of experience in military aviation in the PRC. From August 1998 to August 2002, Mr. Zhang acted first as the deputy general manager and later a general manager of Parent Company. Mr. Zhang has been the general manager of the Company since December 2000. He is also the chairman of Hainan Meiya Enterprise Company Limited (海南美亞實業有限公司) which is a subsidiary of Parent Company.

Mr. Liu Lu (劉璐), 32, was appointed as an executive Director and the chief financial officer of the Company in July 2002 and December 2000, respectively. Mr. Liu graduated with a degree in accounting from Institute of Trade and Finance in Anhui, the PRC. From 1994 to 1998, Mr. Liu worked for Hainan Airlines as a supervisor in the financial and planning department of a branch company of Hainan Airlines and as a manager in the clearing centre. From September 1998 to

August 2000, he was appointed to represent the chief financial officer in Parent Company and was later appointed as the acting chief financial officer of the Company in December 2000. Mr. Liu obtained a master degree in business administration in October 2000 from Beijing Aviation University.

Non-executive Directors

Mr. Li Xianhua (李先華), 39, was appointed as a non-executive Director of the Company in December 2000. He graduated from the Wuhan University in the PRC in 1986 with a degree in business management. Mr. Li served as the composite price management officer in the State Commodity Price Bureau in Beijing in 1986. From 1990 to 2000, Mr. Li served as supervisor, senior assistant to the president and chief of the board of supervisors of Hainan Airlines. In December 1995, Mr. Li received a Master's degree from the Masstricht School of Management in Holland. Since 1998, Mr. Li has served as assistant to general manager, director and assistant to chief executive officer of Parent Company. Since January 2000, Mr. Li has acted as the chief executive officer of HNA Group.

Mr. Jing Xingxiang (景興祥), 59, was appointed as a non-executive Director of the Company in December 2000. Mr. Jing holds a degree in aviation and has over 30 years of experience in civil aviation. Mr. Jing was appointed as a general office manager, deputy general manager and general manager of a branch companies of China Southern Airlines in August 1992, September 1994 and March 1998 respectively. He has served as a director of Parent Company since August 2000. Mr. Jing is now the general secretary of the communist party of China Southern Airlines Hainan Branch.

Independent non-executive directors

Mr. Xu Boling (徐柏齡), 70, was appointed as an independent non-executive Director of the Company in June 2001. Mr. Xu was one of the representatives of the Fourth and Fifth National People's Congress and a member of the Ninth Chinese People's Political Consultative Conference. Mr. Xu has extensive experience in aviation management, he worked for the Civil Aviation Beijing Administrative Bureau since 1954 in various post such as pilot, inspector and captain and was appointed as the deputy chief and chief of division in January 1977 and June 1979 respectively. Mr. Xu was then appointed as the Associate Director of CAAC in December 1986. Mr. Xu was then appointed as the chief executive officer of Air China in March 1988. He was appointed as the consultant of CAAC in August 1993.

Mr. Meng Jianqiang (蒙建強), 42, was appointed as an independent non-executive Director of the Company in July 2002. He obtained a master degree in business administration from the International Open University of Macau in 2002. From 1996, he was the executive director of Zhicheng Group Company Limited (志誠集團有限公司), a trading company not related to the Group. From 1998, he had been the executive director of China Aviation Leasing Group Company Limited (中國航空租賃集團有限公司) which is not related to the Group or Parent Company.

SUPERVISORS

Mr. Zhang Cong (張聰), 43, was appointed as a Supervisor of the Company in December 2000. Mr. Zhang graduated from China Civil Aviation Institution in 1990 with a degree in English language and taught in the China Civil Aviation Institution from 1996 to 1999. From May 1997 to July 2000, he acted as the assistant to general manager, deputy general manager of the personel department of Hainan Airlines. Since July 2000, Mr. Zhang has been the general manager of the human resources department of HNA Group.

Mr. Zheng Hong (鄭宏), 36, was appointed as a Supervisor of the Company in December 2000. Mr. Zheng graduated from Northern Jiaotong University (北方交通大學) with a degree in Economics in 1989 and China Civil Aviation Institution with a MBA degree in 2000. He taught Finance in Wuhan from 1989 to 1994. From August 1994 to August 2000, Mr. Zheng was the deputy general manager and general manager of the finance department of Hainan Airlines. Since August 2000, Mr. Zheng has been the financial controller with the planning and financial department and the general manager of HNA Group.

Ms. Zeng Xuemei (曾雪梅), 33, was appointed as a Supervisor of the Company in July 2002. Ms. Zeng graduated with a degree in biochemistry in Qiong Zhou University (瓊州大學) in 1991. From May 1994 to December 2000, she acted as the secretary in the human resources training centre, aviation department and officer of staff duty office of Hainan Airlines. She worked in the administrative office of HNA Group from May 2000 to September 2000. She then worked in the administrative office of Parent Company from September 2000 to December 2000. She is currently the administrative officer of the Company, responsible for filing and database management.

SENIOR MANAGEMENT

Mr. Fang Zhen'an (方振安), 53, was appointed as the deputy general manager of the Company in December 2000. Mr. Fang graduated with a degree in politics from Huanan Normal University (華南師範大學) in 1986. From 1993 to December 1997, Mr. Fang worked with Civil Aviation Hainan Administrative Bureau and was later promoted as a director in 1996. In 2000, Mr. Fang was appointed as the vice president of Parent Company.

Mr. Hu Wentai (胡文泰), 47, was appointed as the deputy general manager of the Company in December 2000. Mr. Hu graduated with a diploma from Navy Institute of Logistic in 1979. He has years of experience with the military and in aviation management. In August 2000, he was appointed as the executive vice president of the Company.

Company Secretary

Mr. Bai Yan (柏彥), 27, was appointed as the Company secretary in April 2002. Mr. Bai graduated from the Economics Department of Northwestern University with a degree in international finance in 1997. Upon graduation, Mr. Bai worked in the securities department of Hainan Airlines from July 1997 to March 2002 handling securities-related matters including assisting the Company's secretary in preparing proposals, resolutions and other related documents for board meetings and shareholder meetings, public announcements, and handling financing work on the securities market. From December 2000 to March 2002, Mr. Bai was seconded to HNA Group to assist in its corporate and securities matters, including the proposed listing of a subsidiary of HNA Group on the Growth Enterprise Market of the Stock Exchange. In October 2000, Mr. Bai was assigned to assist in the establishment of the Company and the related restructuring matters.

Since Mr. Bai was appointed as the company secretary, he has been managing every aspect of the H Share issue and listing process, including assets swap, prospectus drafting, facilitating due diligence, liaising with professional parties and preparing responses to the Stock Exchange queries.

In June 2001, Mr. Bai received a certificate for attending a company secretarial training course organised by the Shanghai Stock Exchange. Mr. Bai has been in charge of the restructuring, establishment and listing preparation of the Company. He has around five years experience in securities related matters and corporate management.

Rule 8.12 and Rule 19A.17 requirements

According to Rule 8.12 and Rule 19A.17 of the Listing Rules, an issuer must have sufficient management presence in Hong Kong, including that normally at least two of the issuer's executive directors must be ordinarily resident in Hong Kong. Since the operation of the Company is in the PRC, the Company does not and, for the foreseeable future, will not have management presence in Hong Kong. Accordingly, the Company has applied to the Stock Exchange for a waiver under Rule 8.12 and Rule 19A.17 of the Listing Rules. To maintain effective communication between the Company and the Stock Exchange, the Company will make sure that the authorised representatives are able to be contacted at all times by telephone.

Audit Committee

The Company established an audit committee on 24th September, 2002 with written terms of reference in compliance with the Code of Best Practice as set out in Appendix 14 to the Listing Rules. The primary duties of the audit committee are to review and supervise the financial reporting process and internal control system of the Company and provide advice and comments to the Board. Currently, the audit committee has two members comprising the two independent non-executive directors of the Company.

Compensation of Directors and Supervisors

The aggregate amount of salaries, housing allowances, other allowances and benefits in kind paid by the Company to the Directors and Supervisors of the Company for each of the three years ended 31st December, 2001 and the five months ended 31st May, 2002 were approximately RMB107,000, RMB111,000, RMB158,000 and RMB66,000, respectively. The Company's aggregate contribution to the pension schemes in respect of its Directors and Supervisors pursuant to the Company's pension schemes, calculated at 14% and 16% of the aggregate salaries of the Directors and Supervisors for the period before and after 31st December, 2000, respectively, and was approximately RMB15,000, RMB16,000, RMB22,000 and RMB9,000 for each of the three years ended 31st December, 2001 and five months ended 31st May, 2002 respectively. See "Statutory and General Information — Disclosure of Interests" in Appendix X to this prospectus.

The aggregate amount of bonuses paid by the Company to the Directors and Supervisors of the Company during the three years ended 31st December, 2001 and the five months ended 31st May, 2002 were approximately RMB46,000, RMB48,000, RMB68,000 and RMB28,000, respectively.

The aggregate amount of salaries, housing allowances, other allowances and benefits in kind paid by the Company to the five highest paid individuals of the Company for each of the three years ended 31st December, 2001 and the five months ended 31st May, 2002 was approximately RMB157,000, RMB163,000, RMB197,000 and RMB83,000, respectively. The Company paid approximately RMB27,000, RMB28,000, RMB38,000 and RMB16,000 as its contribution to the pension schemes in respect of such individuals in each of the three years ended 31st December, 2001 and the five months ended 31st May, 2002 respectively.

The aggregate amount of bonuses paid by the Company to the five highest paid individuals of the Company for each of the three years ended 31st December, 2001 and the five months ended 31st May, 2002 were approximately RMB67,000, RMB70,000, RMB84,000 and RMB35,000, respectively.

Each of the executive Directors has entered into a service contract with the Company. The initial term of appointment will be three years commencing from 21st December, 2000 for Mr. Chen Wenli and Mr. Zhang Han'an and from 19th July, 2002 for Mr. Liu Lu, which will be renewable thereafter until terminated by not less than six months' notice in writing by either party. Each of Mr. Chen Wenli, Mr. Zhang Han'an and Mr. Liu Lu is entitled to an annual base salary in the amount of RMB164,796, RMB143,196 and RMB101,640, respectively which is payable starting from 1st September, 2002. The director's annual salary is subject to adjustment by the Company's general meeting. In addition, the executive Directors are also entitled to a discretionary management bonus provided that the aggregate amount of the bonuses payable to all the executive Directors and the management of the Company for any financial year may not exceed 2% of the audited net profits of the Company in the previous year and is approved by the Shareholders' general meeting.

Each of the non-executive Directors and the Supervisors has entered into a service contract with the Company. Each service contract is for a term of three years commencing from the date on which those non-executive Directors and the Supervisors were appointed by the Company's general meeting, which is 21st December, 2000 for Mr. Li Xianhua, Mr. Jing Xingxiang, Mr. Zhang Cong and Mr. Zheng Hong, 29th June, 2001 for Mr. Xu Boling and 19th July, 2002 for Mr. Meng Jianqiang and Ms. Zeng Xuemei. Each non-executive Director is entitled to a director's fee in the amount of RMB50,000 per year and each independent non-executive Director RMB80,000 per year starting from 1st September, 2002. Each Supervisor is entitled to a supervisor's fee in the amount of RMB20,000 per year starting from 1st September, 2002.

Senior Management Compensation Scheme

In order to incentivise the senior management of the Group, the shareholders of the Company adopted a senior management compensation scheme in August 2002. The scheme comprises three compensation components, namely, base salaries, performance bonuses and stock appreciation rights.

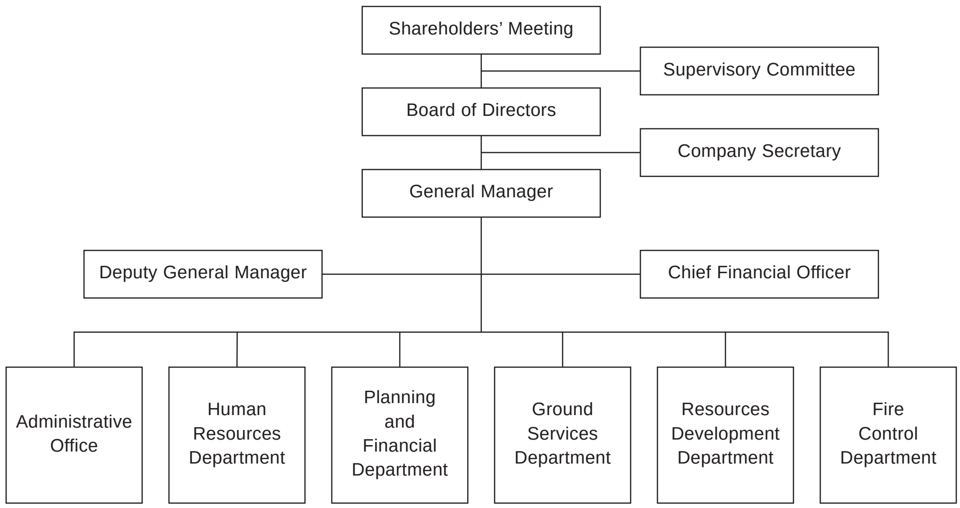
Performance bonuses are awarded to the senior management based on three key performance indices. These indices are linked to factors such as return on equity of the Company, the operation and management of the Group and the future development of the Group. Under the scheme, the maximum amount of performance bonus that a senior manager may be entitled to in any year is equivalent to six months of his monthly base salary in that year.

The scheme also provides that the Company may grant stock appreciation rights to the senior management. The recipient is entitled to receive cash payments to the extent that the market price of the H Shares at the time of exercise of the stock appreciation rights exceeds the exercise price (subject to the other provisions of the scheme). The Company may only grant stock appreciation rights once every two years. The exercise period for each stock appreciation right is five years, with a vesting period of three years in respect of up to 30% of the stock appreciation right, four years in respect of up to 70% of the stock appreciation right, and five years in respect of all the stock appreciation right. The number of stock appreciation rights that are outstanding and that may be granted under the scheme must not exceed 5% of the total number of H Shares in issue as at the date on which the H Shares first commence trading on the Stock Exchange.

The aggregate sum of all performance bonuses and stock appreciate rights that may be granted to senior management under the scheme in any year must not exceed 2% of the net profit of the Group for the preceding year.

Management Structure

The following chart sets out the management structure of the Company:



EMPLOYEES

Introduction

As at 1st June, 2002, the Group had 485 employees who provided aeronautical-related services and ancillary or non-aeronautical related services.

The following is a breakdown of employees of the Group as at 1st June, 2002 according to the division or entity in which they are employed:

Divisions	Number of Employees
Administrative Office	13
Human Resources Department	11
Planning and Financial Department	16
Ground Services Department	247
Resources Development Department	18
Fire Control Department	39
Meilan Travelling	96
DFG	38
Meilan Advertising	7
Total	485

The Company has not experienced any strikes or labour disputes that have materially interfered with its operations and the Directors believe that the Company's relationship with its employees are good.

All employees of the Company receive salary and non-cash benefits. Salary of the employees comprise of base salary, position salary and performance salary. Performance salary is in line with the performance of both the Company and the employees and attribute to 50% of employees' cash-based compensation. In addition to salary, the Company's employees receive certain non-cash benefits including health services, various types of compassionate leave and other benefits set out below.

The Company has maintained work-related injury insurance for its employees which covers death and personal injury of employees at work, unemployment, medical, retirement and maternity benefits. For death and personal injury insurance, the Company contributes premium in the amount of 1% of the employee's monthly base salary and position salary. For unemployment insurance, each of the Company and the employee respectively contribute premium in the amount of 2% and 1% of the employee's monthly base salary and position salary. For medical insurance, each of the Company and the employee respectively contribute premium in the amount of 6% and 2% of the employee's monthly base salary and position salary. For retirement insurance, the Company participates in a pension scheme operated by the relevant local municipal government in the PRC. The PRC government is responsible for the pension payments to these retired employees. Under this scheme, each employee makes a monthly contribution of 5% of his or her monthly salary and the Company is required to make contributions for employees at a rate of 14% of the employee's salaries in 1999 and 2000. The pension contribution rate of the Company increased to 16% in 2001. The total amount of the Company's contribution to the pension scheme for the year ended 31st December, 2001 and the five months ended 31st May, 2002 was approximately RMB728,000 and RMB369,000 respectively. For maternity insurance, the Company contributes premium in the amount of 0.5% of the employee's monthly base salary and position salary. The Company has also maintained an accident insurance for all its employees the premium of which is contributed by the Company at a rate of 0.6% of the monthly base salary and position salary.

The Company has established a housing fund for the benefit of its employees to which the Company and each of the employees make a monthly contribution respectively of 5% of the monthly base salary and position salary, of the relevant employee. The employees' contributions are deducted by the Company from the employees salary payments.

The Company, under certain conditions and subject to certain limitations, pays for the medical expenses of employees who suffer work-related illnesses, injury, disability or death as well as provides certain medical and other subsidies.

The Company organises various training courses for its new employees as well as experienced employees on language, computer, business operation, technical, management and other skill development. The Company also provides training courses on risk management, business strategies, corporate governance, investment strategies, communication, financial control and other skill development.

Immediately following the completion of the Offering (but without taking into account the exercise of the Over-allotment Option) the only persons directly or indirectly interested in 10% or more of the voting power at any shareholders' general meeting of the Company will be:

Name	Number of Shares	Voting Power (percent)
Parent Company	237,500,000 (Domestic Shares)	53.01
The Strategic Investor	89,700,000 (H Shares)	20.02

If the Over-allotment Option is exercised in full, Parent Company's and the Strategic Investor's interests in the registered share capital of the Company will be:

Name	Number of Shares	Voting Power (percent)
Parent Company	237,500,000 (Domestic Shares)	50.19
The Strategic Investor	94,642,000 (H Shares)	20.00

The Company is not aware of any arrangement which may at a subsequent date result in a change of control of the Company.

The share capital of the Company immediately after completion of the Offering will be as follows (assuming the Over-allotment Option is not exercised):

Issued and to be issued, fully paid or credited as fully paid:

Number of Shares		*RMB*
246,300,000	Domestic Shares in issue *(Note 1)*	246,300,000
3,700,000	H Shares to be converted from the Domestic Shares and offered by the Vendors for sale under the Public Offer *(Note 2)*	3,700,000
16,470,000	H Shares to be issued by the Company pursuant to the Public Offer *(Note 3)*	16,470,000
181,530,000	H Shares to be issued by the Company pursuant to the International Placing	181,530,000
448,000,000		448,000,000

Notes:

1. The 246,300,000 Domestic Shares do not include the 3,700,000 Domestic Shares to be converted into H Shares and offered by the Vendors for sale under the Public Offer.

2. The Sale H Shares are being offered for sale under the Public Offer in compliance with the Temporary Administration Measures on the Reduction of State-Owned Shares for the Raising of Social Security Fund (減持國有股籌集社會保障資金管理暫行辦法) (the "**Temporary Administration Measures**") promulgated by the State Council on 12th June, 2001. Pursuant to the Temporary Administration Measures, holders of state-owned shares of a joint stock limited company (including companies listed overseas) in which the state owns shares, shall offer for sale its state-owned shares in the amount equivalent to 10% of the funds to be raised.

   Accordingly, an aggregate of 3,700,000 Sale H Shares are offered for sale at the Offer Price. These 3,700,000 Sale H Shares will be converted from the 925,000 Domestic Shares held by China Southern Airlines and the 2,775,000 Domestic Shares held by Central South Aviation Development. The Sale H Shares will rank pari passu with the New H Shares in all respects. The net proceeds arising from the sale of the Sale H Shares will be remitted to the National Social Security Fund.

3. Pursuant to the resolutions of the shareholders passed on 30th May, 2002 and 10th September, 2002 and the resolutions of the Board passed on 24th September, 2002 the Company is authorised to offer 201,700,000 H Shares under the Offer (inclusive of the conversion of 3,700,000 Domestic Shares into Sale H Shares and the transfer of the Sale H Shares pursuant to the Public Offer) and to apply for listing of the H Shares on the Stock Exchange.

Assumption

The table above assumes that the Offering becomes unconditional and is completed.

Ranking

Domestic Shares and H Shares are both ordinary shares with a nominal value of RMB1.00 each in the share capital of the Company. However, H Shares may only be subscribed for by, and traded in Hong Kong dollars among legal or natural persons of Hong Kong, Macau or any jurisdiction other than the PRC. Domestic Shares, on the other hand, may only be subscribed for by, and transferred among legal or natural persons of the PRC (other than Hong Kong, Macau and Taiwan) and must be subscribed for and disposed of in Renminbi. All dividends in respect of the H Shares are to be declared in Renminbi and paid by the Company in Hong Kong dollars where all dividends in respect of Domestic Shares are to be paid by the Company in Renminbi.

All the existing Domestic Shares are held by the Promoters as promoter shares (as defined in the Company Law). Except as required by law, promoter shares may not be transferred within a period of three years from the date of incorporation of the Company. This period will expire on 28th December, 2003. Subject to the sale of the Sale H Shares by the Vendors as described above, as at the date of this prospectus, the Promoters have not sold any Domestic Shares held by them. The Domestic Shares are not admitted for listing on any stock exchange and no arrangement has been made for the Domestic Shares to be traded or dealt with on any other authorised trading facility in the PRC.

Except as described above and in relation to the despatch of notices and financial reports to shareholders, dispute resolution, registration of Shares on different parts of the register of shareholders, the method of Share transfer and the appointment of dividend receiving agents, which are all provided for in the Articles of Association and summarised in Appendix IX to this prospectus, the Domestic Shares and the H Shares will rank pari passu with each other in all respects and, in particular, will rank equally for all dividends or distributions declared, paid or made after the date of this prospectus. However, the transfer of Domestic Shares is subject to such restrictions as PRC law may impose from time to time.

Save for the Offering, the Company does not propose to carry out a public or private issue or to place securities simultaneously with the Offering or within the six months thereafter. The Company has not approved any share issue plan other than the Offering.

The Company has given certain undertakings in respect of the issue of H Shares and other securities. See the section headed “Underwriting — Undertakings”.

The Company's books and records are presented in Renminbi. Unless otherwise specified, this prospectus contains translations for reference only of Renminbi amounts into Hong Kong dollars at the rate of HK$1.00 to RMB1.0611 being the PBOC rate prevailing on 31st May, 2002. No representation is made that the Renminbi amounts could have been or could now or in the future be converted into Hong Kong dollars at any particular rate or at all. See the section headed "Risks Factors — Risks Relating to the PRC — Foreign exchange regulations".

INDEBTEDNESS

The following table shows the Group's short-term debt and its long-term liabilities as at 31st August, 2002.

	As at 31st August, 2002
	(RMB'000)
Short-term debt:	
Short-term bank loan(1)	20,000
Current portion of long-term bank loan(2)	13,000
	33,000
Long-term debt:	
Long-term bank loan (excluding current portion)(2)	257,000

(1) Short-term bank loan from China Development Bank to the Company, with an outstanding principal amount of RMB20 million as at 31st August, 2002, maturing on 27th December, 2002. On 10th September, 2002, the Company incurred an additional RMB50 million short-term debt under this facility. This loan has a maturity date of 9th September, 2003, and bears interest at the rate of 5.31% per annum. The loan is guaranteed by HNA Group. The Company obtained the written consent of China Development Bank on 4th November, 2002 to release the guarantee as soon as practicable. The Company has undertaken to the Stock Exchange that it will use its best endeavours to complete the procedures regarding such release within three months from the date on which the H Shares are listed on the Stock Exchange. If the guarantee is not released after three months from the date of commencement of dealing in the H Shares, the Company will release an appropriate announcement.

(2) Long-term bank loan from China Development Bank to the Company, with an outstanding principal amount of RMB270 million as at 31st August, 2002, including current portion of RMB13 million. The loan is secured by the pledge of land use rights (i) by the Company, with a value of RMB50 million, and (ii) by Parent Company, with a value of RMB357 million. The Company obtained the written consent of China Development Bank on 4th November, 2002 to release its security over the land use rights pledged by Parent Company as soon as practicable. The Company has undertaken to the Stock Exchange that it will use its best endeavours to complete the procedures regarding such release within three months from the date on which the H Shares are listed on the Stock Exchange. If the guarantee is not released after three months from the date of commencement of dealing in the H Shares, the Company will release an appropriate announcement.

Disclaimer

Except as aforesaid and apart from intra-group liabilities, the Group did not have outstanding, at the close of business on 31st August, 2002, any loan capital, bank overdrafts and liabilities under acceptances or other similar indebtedness, debentures, mortgages, charges or loans or acceptance credits or hire purchase commitments, guarantees, indemnities or other material contingent liabilities.

On 10th September, 2002, the Company incurred an additional RMB50 million short-term debt under the China Development Bank facility. The Directors have confirmed that, except as aforesaid, there had not been any material change in the indebtedness and contingent liabilities of the Group since 31st August, 2002 up to the Latest Practicable Date.

PRACTICE NOTE 19 TO THE LISTING RULES

The Directors have confirmed that as at the Latest Practicable Date, they were not aware of any circumstances which, had the Group been required to comply with Practice Note 19 of the Listing Rules, would give rise to a disclosure requirement under that Practice Note.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity

The Group's principal source of liquidity for working capital and for current debt service for short-term and long-term debts is cash generated from operations.

Net Current Assets

As at 31st August, 2002, the Group had net current assets of approximately RMB20 million. Current assets of the Group comprised cash and cash equivalents of approximately RMB18 million, accounts receivable of approximately RMB20 million, Airport Fee receivable of approximately RMB25 million, amounts due from related parties of approximately RMB58 million, inventories of approximately RMB2 million, and prepayments, deposits and other receivables of approximately RMB8 million. Average collection days of accounts receivable at 31st August, 2002 was 65 days. As at 31st August, 2002, the Group's current liabilities were approximately RMB111 million comprised of current portion of long-term loans of approximately RMB13 million, short-term bank loan of approximately RMB20 million, accounts payable of approximately RMB1 million, other accrued expenses and other payables of approximately RMB19 million, Airport Fee payable of approximately RMB50 million, deposits received of approximately RMB4 million, dividends payable of approximately RMB2 million and amounts due to related parties of approximately RMB2 million.

On 10th September, 2002, the Company incurred an additional RMB50 million short-term debt under the China Development Bank facility, increasing both current assets and current liabilities by that amount. This loan has a maturity date of 9th September, 2003, and bears interest at the rate of 5.31% per annum.

The Company obtained the written consent of China Development Bank on 4th November, 2002 to release the bank's security over land use rights pledged by Parent Company as security for the Company's long-term loan from China Development Bank, and to release the guarantees of HNA Group for the Company's short-term loans from China Development Bank as soon as practicable. The Company has undertaken to the Stock Exchange that it will use its best endeavours to complete the procedures regarding such release within three months from the date on which the H Shares are listed on the Stock Exchange. If the guarantees are not released after three months from the date of commencement of dealing in the H Shares, the Company will release an appropriate announcement.

Capital Resources

The Group's principal capital resources are (i) profit generated from operations and (ii) long-term and short-term bank loans. As at 31st August, 2002, long-term bank loan outstanding was RMB270 million (consisting of a loan from China Development Bank); short term bank loan outstanding was RMB20 million (consisting of a loan from China Development Bank), (iii) Shareholder's funds.

On 20th September, 2001, the long-term loan from China Development Bank in the amount of RMB285 million was extended bearing an interest rate of 6.21%. RMB20 million is repayable before 30th November, 2003, RMB100 million is repayable from 1st December, 2003 to 30th November, 2005 and RMB150 million is repayable from 1st December, 2005 to 20th December, 2008. As of 31st May, 2002, the outstanding balance of the principal amount of the loan was RMB270 million.

The RMB20 million short-term loan, granted by China Development Bank on 28th December, 2001, bears an annual interest rate of 5.85% and has a term of one year.

Historical Capital Expenditures

The Group's capital expenditures for the years 1999 to 2001 and the first five months of 2002 were:

Project	1999	2000	2001	Five months ended 31st May, 2002
	(RMB'000)	*(RMB'000)*	*(RMB'000)*	*(RMB'000)*
Properties and Buildings . . .	18,389	80	420	37,689
Transport Vehicles	384	1,850	8,149	5,996
Equipment	39,411	9,294	1,971	1,037
Total	58,184	11,224	10,540	44,722

Parent Company started to operate formally in 1999, and commercial operation of the Meilan Airport commenced in May 1999. Prior to that time, Parent Company made the above-mentioned investment in fixed assets including the Terminal, apron and transport vehicles. It also purchased equipment and machinery in 1999 for business operations and expansion.

The interest expenses on bank borrowings relating to construction projects which have been capitalised were RMB8.09 million in the year ended 31st December, 1999.

Planned Capital Expenditures and Commitments

The Group intends to carry out several projects to expand its current operations to accommodate projected future air traffic increases. The airport expansion project includes the construction of a new Terminal area of approximately 30,000 m^2 and an aircraft parking apron of approximately 280,000 m^2, 20 aircraft parking positions and eight air bridges. The construction is expected to commence by late 2002 and to be completed by the end of 2003. Upon completion of the construction, it is expected that the Terminal will have a total area of approximately 90,000 m^2, and a passenger throughput capacity of approximately eight million, an increase of 33.3% over the current capacity.

In anticipation of the growth of cargo throughput, the Group intends to expand its cargo centre and cargo aircraft parking apron by constructing a new cargo centre with floor area of approximately 30,000 m^2 and a cargo apron with an area of approximately 50,000 m^2 with four aircraft parking positions. The cargo centre and cargo apron expansion project is expected to commence by late 2002 and to be completed by the end of 2003. It is expected that the cargo centre and the cargo apron can increase cargo throughput by 150,000 tonnes.

Anticipating the attainment of the international airport status, the Company is constructing a custom and inspection joint operation building for processing international passengers and cargo. The construction is expected to be completed by the end of 2002.

All the above projects have been preliminarily approved by the Hainan Development and Planning Bureau (海南省發展計劃廳) or SDPC.

Within 12 months from the date of the Asset Swap Agreement, the Company is required to make three cash instalment payments to Parent Company in the total amount of approximately RMB49.73 million as payment of the outstanding purchase price with respect to the four assets purchased by the Company from Parent Company and the three assets sold by the Company to Parent Company. The Company intends to fund the payment obligations with internal sources.

The Directors are of the opinion that, taking into account the financial resources available to the Group including internally generated funds, the available credit facilities and the net proceeds of the Offering, the Group is able to satisfy its present and projected capital expenditures requirements.

Working Capital

As at 31st August, 2002, the Group had net current assets of RMB20 million as working capital. The businesses of the Group generate operating cash flows which, together with available working capital banking facilities, have been and are expected to be sufficient to meet its working capital requirements for its daily operation. Taking into account the net proceeds of the Offering (see the section headed "Future Plans and Use of Proceeds"), banking facilities, outstanding loans and net operating cash inflow, the Directors are of the opinion that the Group has sufficient working capital for its present requirements.

Foreign Exchange and Foreign Currency

Apart from (i) aircraft movement fees and related charges paid by Hong Kong and Macau airlines and (ii) fees from the ground handling services provided to Hong Kong and Macau airlines, the Group receives its revenues in RMB. In the future, the Group's needs for foreign currency will include purchases for duty-free goods and payment of dividends in respect of the H Shares. In addition to certain revenues from sales of duty-free goods, the Group's foreign currency requirements are satisfied primarily by converting RMB into the required foreign currency. The Group does not engage in transactions to hedge or mitigate its exposure to exchange rate fluctuations. The Group maintains its books and records in RMB. Foreign currency transactions during the Track Record Period have been translated into RMB at the applicable rates prevailing on the respective transaction dates. Foreign currency monetary balances on the balance sheet date have been translated into RMB at the exchange rates quoted by PBOC on the balance sheet date. Exchange gains and losses resulting from foreign currency transactions are recognised in the consolidated income statement subject to certain exceptions (see Note 2(k) of Appendix I — The Accountants' Report).

HISTORICAL TRADING RECORD

The table below sets out a summary of the consolidated results of the Group for the three years ended 31st December, 2001 and the five months ended 31st May, 2002, based on the information included in the Accountants' Report as set out in Appendix I to this prospectus, which presents the results of the Group as if the Group had been in existence throughout the Track Record Period. The construction of the Meilan Airport was completed and the assets of the Meilan Airport were ready for operation in March 1999. Prior to that time, costs and expenses of construction were capitalised. Commencing from the initial trial operations on 29th March, 1999, cost and expense items were recorded in the income statement; and commencing from the beginning of commercial operations on 25th May, 1999, all items of revenue, cost and expense were recorded in the income statement. The consolidated financial information has been prepared and presented in accordance with International Accounting Standards.

	Year ended 31st December,			Five months ended 31st May,
	1999[1]	**2000**	**2001**	**2002**
		(RMB'000)		
Revenues				
Aeronautical[2]				
Passenger charges	41,766	90,371	102,283	50,584
Airport fee	—	—	—	29,442
Ground handling services fee	10,091	18,371	20,556	10,644
Aircraft movement fees and related charges	5,642	10,661	10,198	5,138
Total aeronautical revenues	57,499	119,403	133,037	95,808
Non-aeronautical				
Leasing of commercial areas, counters and office in the Terminal	10,424	22,921	26,261	10,899
Franchise fees[3]	6,592	11,809	15,490	6,597
Advertising fees	3,530	5,087	4,018	2,021
Other revenues	2,437	2,423	6,195	3,162
Total non-aeronautical revenues	22,983	42,240	51,964	22,679
Total revenues	80,482	161,643	185,001	118,487

	Year ended 31st December,			Five months ended 31st May,
	1999[1]	2000	2001	2002
	(RMB'000)			
Business taxes and levies	(2,931)	(5,952)	(6,819)	(4,364)
Net revenues	77,551	155,691	178,182	114,123
Operating costs				
Cost of goods and services	(6,568)	(13,384)	(13,395)	(4,751)
Depreciation and amortisation	(21,282)	(28,143)	(28,404)	(12,005)
Staff costs	(5,793)	(9,008)	(8,111)	(3,442)
Utilities and power	(4,804)	(7,183)	(7,225)	(2,688)
Repairs and maintenance	(459)	(994)	(2,006)	(355)
Other costs	(359)	(663)	(1,085)	(913)
Total operating costs	(39,265)	(59,375)	(60,226)	(24,154)
Gross profit	38,286	96,316	117,956	89,969
Administrative expenses	(8,388)	(15,157)	(12,892)	(7,451)
Profit from operating activities	29,898	81,159	105,064	82,518
Other income	—	—	—	2,528
Finance expenses, net	(22,067)	(22,966)	(17,659)	(7,666)
Profit before tax	7,831	58,193	87,405	77,380
Tax[4]	—	—	—	—
Profit after tax	7,831	58,193	87,405	77,380
Minority interests	(94)	(4)	6	(9)
Net profit attributable to shareholders	7,737	58,189	87,411	77,371
Distribution to Parent Company[5]	—	29,081	—	—
Final Dividend[6]	—	—	45,000	—
EPS[7]	0.03	0.23	0.35	0.31
EBITDA[8]	51,180	109,302	133,468	97,051

(1) Commercial operations commenced on 25th May, 1999. Accordingly, the relevant data for 1999 reflects only seven months of commercial operations and therefore not directly comparable with those of the subsequent years.

(2) The presentation of the historical figures throughout the Track Record Period for the following aeronautical revenues reflects the revenue sharing arrangement between the Company and Parent Company on the basis of 75% to the Company and 25% to Parent Company:

- Aircraft movement fees;
- Passenger charges; and
- Basic ground handling services fees charged to Hong Kong, Macau and foreign airlines.

(3) The franchise fees for the Track Record Period consist of the following items:

- Annual fees from Hainan Food with respect to the air catering rights at the Meilan Airport;
- Annual fees from Hainan Airlines in 1999 and 2000 and from Parent Company in 2001 and the first five months of 2002 with respect to the right to operate the cargo centre at the Meilan Airport;
- Annual fees from THIA with respect to the right to sell accident insurance policies at the Meilan Airport; and
- Fees from HLAS with respect to air ticketing operation at the Meilan Airport.

(4) The Company is entitled to an exemption from corporate income tax from 2000 to 2004, and a reduced income tax rate of 7.5% from 2005 to 2009. Please refer to the subsection headed "Financial Information — Taxation" for details.

(5) Pursuant to a resolution of shareholders dated 29th June, 2001, the Company made a distribution to Parent Company which represented the profit after tax of the Company for the period from 1st August, 2000 to 31st December, 2000. Such profit after tax was determined in accordance with relevant PRC accounting regulations.

(6) On 19th July, 2002, the shareholders of the Company approved the distribution of a final dividend of RMB45 million for the year ended 31st December, 2001 to the then existing shareholders.

(7) The calculation of earnings per Share is based on the Group's profit attributable to shareholders for each of the three years ended 31st December, 2001 and for the five months ended 31st May, 2002 and on the 250 million shares deemed to have been in issue and issuable during the Track Record Period.

(8) EBITDA should not be construed as an alternative to operating income or any other measure of performance or as an indicator of the Group's operating performance, liquidity or cash flows generated by operating, investing and financing activities. The items of net income excluded EBITDA are significant components in understanding and assessing the Group's financial performance, and the Group's computation of EBITDA may not be comparable in other similarly titled measures of other companies. The Group has included the information concerning EBITDA because the Directors believe that it is a useful supplement to cash flow data as a measure of the Group's performance.

The Directors have confirmed that they have performed sufficient due diligence on the Group to ensure that, save as disclosed herein, up to the date of this prospectus, there has been no material adverse change in the financial position or prospect of the Group since 31st May, 2002 and there is no event which would materially affect the information shown in the Accountants' Report of the Group as set out in Appendix I. The following discussion and

analysis should be read in conjunction with the financial statements, including the notes thereto, contained elsewhere in this prospectus. Results for the five months ended 31st May, 2002 are not necessarily indicative of the Group's results for the full year.

RECENT DEVELOPMENTS

For the nine months ended 30th September, 2002, the total number of aircraft movements at the Meilan Airport was approximately 45,200, as compared to approximately 40,900 for the corresponding period of 2001, representing a 10.5% increase; the total passenger throughput was approximately 4,214,000, as compared to approximately 3,845,000 for the corresponding period of 2001, representing a 9.6% increase; and the total volume of cargo was approximately 57,000 tonnes, as compared to approximately 55,800 tonnes for the corresponding period of 2001, representing a 2.1% increase. The numbers of aircraft movements, passenger throughput and cargo tonnage increased for the categories of domestic fights and international flights, but decreased for the category of Hong Kong and Macau flights. The overall increase in the total numbers of aircraft movements, passenger throughput and cargo tonnage is consistent with the Directors' belief that the air traffic demand at the Meilan Airport is growing in general. The decrease in the Hong Kong and Macau category is believed to correlate with the sluggish economic conditions in these two regions.

Effective 1st September, 2002, the ground handling fee for domestic airlines consists of (i) aircraft cleaning fee, ranging from RMB100 to RMB576 per aircraft, depending on the passenger capacity of the aircraft; (ii) transportation service fee for providing passenger services such as check-in and baggage and mail handling, calculated at RMB61 per payload tonne for all aircraft with a payload over 10 tonnes; and RMB55 per payload tonne for aircraft with a maximum payload of 10 tonnes or less and (iii) special vehicle services fee, which covers the provision of special vehicles including passenger transport vehicles, air bridges, and passenger ramp vehicles, calculated on per hour or per use basis. For example, for a Boeing 737-500 aircraft which has an MTOW of 61 tonnes and a payload of 15 tonnes, the basic aircraft cleaning fee and transportation service fee are RMB120 and RMB915, respectively.

RESULTS OF OPERATIONS

The following discussion and analysis should be read in conjunction with the financial information contained in the Accountants' Report set out in Appendix I and with the information set out in the section headed "Business".

Sources of Revenue

Revenues consist of:

	Year ended 31st December,						Five months ended 31st May,	
	1999		2000		2001		2002	
	RMB'000	*%*	*RMB'000*	*%*	*RMB'000*	*%*	*RMB'000*	*%*
Aeronautical:								
Passenger charges	41,766	52	90,371	56	102,283	55	50,584	43
Airport fee	—	0	—	0	—	0	29,442	25
Ground handling services fee	10,091	13	18,371	12	20,556	11	10,644	9
Aircraft movement fees and related charges	5,642	7	10,661	7	10,198	6	5,138	4
Total aeronautical revenues	57,499		119,403		133,037		95,808	
Non-aeronautical:								
Leasing of commercial area, counters and office in the Terminal	10,424	13	22,921	14	26,261	14	10,899	9
Franchise fees(1)	6,592	8	11,809	7	15,490	8	6,597	5
Advertising fees	3,530	4	5,087	3	4,018	2	2,021	2
Other revenue	2,437	3	2,423	1	6,195	4	3,162	3
Total non-aeronautical revenues	22,983		42,240		51,964		22,679	
Total revenues	80,482		161,643		185,001		118,487	

(1) The franchise fees for the Track Record Period consist of the following items:

- Annual fees from Hainan Food with respect to the air catering rights at the Meilan Airport;
- Annual fees from Hainan Airlines in 1999 and 2000 and from Parent Company in 2001 and the first five months of 2002 with respect to the right to operate the cargo centre at the Meilan Airport;
- Annual fees from THIA with respect to the right to sell accident insurance policies at the Meilan Airport; and
- Fees from HLAS with respect to air ticketing operation at the Meilan Airport.

The Group's revenues depend principally on the volume of aircraft movements, passenger throughput and cargo throughput at the Meilan Airport. These in turn are influenced by a number of factors, most of which are generally related to the levels of economic growth and activity in China. Another level of influence is the economic growth in Hainan, especially the growth in tourism, agriculture and industry. See "Appendix V — Summary of the Air Traffic Consultants' Report".

The Group's sources of revenues arise from its aeronautical operations and non-aeronautical operations. Aeronautical revenues are classified as:

- passenger charges;
- Airport Fee;
- ground handling services fee; and
- aircraft movement fees and related charges.

Aeronautical revenues depend on the levels of passenger charges, aircraft movement fees and related charges, ground handling services, special vehicles services, cleaning and the Airport Fee, which are subject to the control of or guidelines published by CAAC jointly with MOF and SDPC. In connection with the upgrading of the Meilan Airport's status from civil airport Category III to Category II effective 1st June, 2000, the aeronautical fees charged by the Meilan Airport increased as discussed below. In addition, the Company and Parent Company share certain aeronautical revenues on the basis of 75% to the Company and 25% to Parent Company.

The various sources of aeronautical revenues may be influenced by different factors including (i) the total number of aircraft movements; (ii) the MTOW of aircraft, because fees for aircraft of a greater MTOW are higher than those for aircraft of a smaller MTOW; (iii) the relative proportions of flights operated by Hong Kong and Macau carriers and those operated by domestic carriers, because passenger charges are charged to domestic carriers only and the other aeronautical fees and charges are higher for foreign carriers than domestic carriers; and (iv) pricing policies of CAAC, MOF and the SDPC. Passenger charges prior to 1st September, 2002 are calculated on the basis of 80% of the seat capacity of the relevant type of aircraft, not on the actual number of passengers carried.

Non-aeronautical revenues during the Track Record Period were principally derived from the following operations:

- leasing of commercial areas, counters and office in the Terminal;
- franchise rights of air catering, right to operate the cargo centre, insurance policy sale and air ticketing operation; and
- leasing of advertising spaces.

Revenues from non-aeronautical operations such as leasing of commercial areas, counters and office in the Terminal and leasing of advertising space depend primarily on the number of airline customers and the number of passengers using the Meilan Airport.

Air catering services are carried on by Hainan Food, a company in which Hainan Airlines holds 51% of its equity interest. Hainan Food pays RMB4.38 million annually to the Group for the air catering rights.

Factors Affecting Revenues

A number of factors have influenced the Group's revenues during the Track Record Period. These include:

1. Construction was completed and the assets of the Meilan Airport were ready for use on 28th March, 1999. Prior to that time, costs and expenses of construction were capitalised. Commencing with the beginning of trial operations on 29th March, 1999, cost and expense items were recorded in the income statement; and commencing with the beginning of commercial operations on 25th May, 1999, all items of revenue, cost and expense were recorded in the income statement. Accordingly, the results for 1999 reflect only seven months of commercial operations.

2. Effective 1st June, 2000, the Meilan Airport's status was upgraded, through an approval letter issued by CAAC, from civil airport Category III to Category II. The following table shows the amount and percentage of increase in relevant categories of aeronautical fees:

Aircraft movement fees and related charges

Aircraft movement fees

Domestic airline

MTOW (tonne)	Category II airports	Category III airports	Increase
	RMB	*RMB*	
Less than 25	4.4 per tonne	4 per tonne	10%
25–100	5.5 per tonne	5 per tonne	10%
101–200	7.7 per tonne	7 per tonne	10%
Over 200	8.8 per tonne	8 per tonne	10%

Regional and Foreign airline

MTOW (tonne)	All Categories	Increase
	USD	
Less than 50	558	unchanged
50–100	558+9 x (MTOW-50)	unchanged
101–200	1008+10 x (MTOW-100)	unchanged
Over 200	2008+12 x (MTOW-200)	unchanged

Night surcharge (between 23:00–06:00)

Domestic	Regional and Foreign
20% x the aircraft movement fees	25% x the aircraft movement fees

Lighting charge

Domestic	Regional and Foreign
10% x the aircraft movement fees	10% x the aircraft movement fees

Passenger charges (domestic airlines only)

Category II airports	Category III airports	Increase
RMB	*RMB*	
80% x RMB50 x seating capacity	80% x RMB40 x seating capacity	25%

3. Effective 1st January, 2002, pursuant to a directive of MOF, the Group includes in revenue 50% of the Airport Fees collected from departing passengers. Prior to 1st January, 2002, these fees were recorded as contributions to the equity of Parent Company. Had this change been implemented at the commencement of commercial operations, the Group would have recorded additional aeronautical revenues (less relevant taxes) for 1999, 2000 and 2001 of RMB21.9 million, RMB43.9 million and RMB50.3 million, respectively.

4. The number of flights operated by foreign, Hong Kong and Macau airlines has declined steadily since 2000. Because aircraft movement fees and related charges for flights operated by foreign, Hong Kong and Macau airlines are higher than such fees for flights operated by domestic airlines, this trend has had a negative affect on aeronautical revenues, which has been largely offset by the other factors referred to above. The Directors expect that this trend will be reversed with the designation of Meilan Airport as an international airport, although there can be no assurance with respect to such reverse. Please refer to the section headed "Business Strategies and Strengths" in the "Business" section of this prospectus.

Non-aeronautical revenues depend primarily on the volume of passenger traffic and commercial leasing at the Meilan Airport. As a percentage of total revenues, non-aeronautical revenues decreased from 28.6% in 1999 to 28.1% in 2001. For the first five months of 2002, non-aeronautical revenues decreased to 19.1% of total revenue primarily due to the inclusion of Airport Fees as aeronautical revenue.

Non-aeronautical revenues from cargo centre franchise fees, car parking, tourism and duty-free sales will be reflected in the Group's financial statements for periods subsequent to 31st May, 2002. See section headed "Pro Forma Unaudited Combined Results of the Group".

Five months ended 31st May, 2002

Revenues

Aeronautical revenues

Total aircraft movements for the first five months of 2002 were 27,200, representing an increase of 11.0% over the first five months of 2001. Passenger throughput was 2.56 million in the first five months of 2002, which increased by 14.2% as compared to the same period in 2001.

Passenger charges for the first five months of 2002 were approximately RMB50.6 million, representing 52.8% of aeronautical revenues. The figures for the year ended 31st December, 2001 were approximately RMB102.3 million and 76.9% respectively.

Airport Fee for the first five months of 2002 were approximately RMB29.5 million, representing 30.7% of aeronautical revenues. No Airport Fee was recorded as revenue in 2001.

Ground handling services revenues for the first five months of 2002 were approximately RMB10.6 million, representing 11.1% of aeronautical revenues. The figures for the year ended 31st December, 2001 were approximately RMB20.5 million and 15.4% of aeronautical revenues.

Aircraft movement fees and related charges for the first five months of 2002 were approximately RMB5.1 million, representing 5.4% of aeronautical revenues. The figures for the year ended 31st December, 2001 were approximately RMB10.2 million and 7.7% respectively.

The aeronautical revenues for the first five months of 2002 were approximately RMB95.8 million, accounting for 80.9% of total revenues. The figures for the year ended 31st December, 2001 were approximately RMB133.0 million and 71.9%, respectively.

Non-aeronautical revenues

Leasing revenues for the first five months of 2002 were approximately RMB10.9 million, representing 48.1% of non-aeronautical revenues. The figures for the year ended 31st December, 2001 were approximately RMB26.3 million and 50.5% respectively.

Franchise fee revenues for the first five months of 2002 were approximately RMB6.6 million, representing 29.1% of non-aeronautical revenues. The figures for the year ended 31st December, 2001 were approximately RMB15.5 million and 29.8% respectively.

Advertising revenues for the first five months of 2002 were approximately RMB2.0 million, representing 8.9% of non-aeronautical revenues. The figures for the year ended 31st December, 2001 were approximately RMB4.0 million and 7.7%, respectively.

Other revenues which principally comprise revenues received from airline customers for their use of the Company's electronic boarding confirmation system and other value added services were approximately RMB3.2 million for the first five months of 2002 representing 13.9% of non-aeronautical revenues. The figures for the year ended 31st December, 2001 were approximately RMB6.2 million and 11.9% respectively.

Total non-aeronautical revenues for the first five months of 2002 were approximately RMB22.7 million, representing 19.1% of total revenues. The figures for the year ended 31st December, 2001 were approximately RMB52.0 million and 28.1%, respectively. The decrease in the percentage for the first five months of 2002 was primarily due to the inclusion of Airport Fee as aeronautical revenue effective from 1st January, 2002

Total revenues for the first five months of 2002 were approximately RMB118.5 million. Total revenues for the year ended 31st December, 2001 were approximately RMB185.0 million.

Operating costs and expenses

Cost of goods and services, consisting principally of a composite services fee payable to Parent Company (please refer to section headed "Business — Connected Transactions" for details), for the first five months of 2002 were approximately RMB4.8 million, representing 4.0% of total revenues.

Depreciation and amortisation expenses for the first five months of 2002 were approximately RMB12.0 million, representing 10.1% of total revenues. The Company records depreciation in relation to its property, plant and equipment and amortisation in relation to its land use rights as described in *Note 2(c) and 2(e)* to the Accountants' Report. Depreciation is not recorded in relation to assets under construction until the construction has been completed and until the assets are available for their intended uses.

Staff costs for the first five months of 2002 were approximately RMB3.4 million, equal to 2.9% of total revenues. For the year ended 31st December, 2001, staff costs were RMB8.1 million, equal to 4.4% of total revenues.

Utility and power expenses, consisting primarily of fuel costs and water and electricity fees, for the first five months of 2002 were approximately RMB2.7 million, representing 2.3% of total revenues. The figures for the year ended 31st December, 2001 was RMB7.2 million, equal to 3.9% of total revenues.

Repairs and maintenance costs, representing labour and other costs incurred for day-to-day repairs and maintenance, as well as major overhauls, for the first five months of 2002 were approximately RMB0.4 million, representing 0.3% of total revenues. The figures for the year ended 31st December, 2001 were approximately RMB2.0 million and 1.1% of total revenues.

Other costs, consisting principally of office supplies for operational departments and material costs for boarding passes for the first five months of 2002 were approximately RMB0.9 million, representing 0.8% of total revenues. The figures for the year ended 31st December, 2001 were approximately RMB1.1 million and 0.6% of total revenues.

Total operating costs for the first five months of 2002 were approximately RMB24.2 million, equal to 20.4% of total revenues. The figures for the year ended 31st December, 2001 were approximately RMB60.2 million and 32.6% of total revenues, respectively.

Gross profit for the first five months of 2002 was RMB90.0 million, representing a gross profit margin of 75.9%. The figures for the year ended 31st December, 2001 were RMB118.0 million and 63.8% respectively. The increase of gross profit margin in 2002 is attributable to the following two factors: (i) starting from 1st January, 2002, 50% of the Airport Fee has been recorded as revenue of the Group, which has no associated costs; and (ii) tightened cost control.

Administrative expenses and operating profit

Administrative expenses mainly consist of salary and benefits for the senior management and administrative staff of the Group and property tax on all buildings of the Group. Administrative expenses were approximately RMB7.5 million for the first five months of 2002, equal to 6.3% of total revenues. The figures for the year ended 31st December, 2001 were approximately RMB12.9 million and 7.0% of total revenues, respectively.

Operating profit for the first five months of 2002 was approximately RMB82.5 million, representing an operating margin of 69.6%. The figures for the year ended 31st December, 2001 were approximately RMB105.1 million and 56.8%, respectively. The increase of operating profit margin in 2002 is mainly attributable to the inclusion of Airport Fee as revenue of the Group without any associated costs.

Non-operating income and expenses, taxation and net profit

Net finance expenses (interest expenses net of interest income) for the first five months of 2002 were approximately RMB7.7 million, equal to 6.5% of total revenues. The figures for the year ended 31st December, 2001 were approximately RMB17.7 million and 9.5%, respectively.

Profit before tax and after tax for the first five months of 2002 was approximately RMB77.4 million, equal to 65.3% of total revenues. No taxation is charged for the period. The figures for the year ended 31st December, 2001 were approximately RMB87.4 million and 47.2%, respectively. The Company is entitled to preferential treatment granting an exemption from corporate income tax for the first five years from its first profitable year, and a 50% reduction in the corporate income tax for the following five years. The first profitable year of the Company was the year ended 31st December, 2000. It therefore enjoys an exemption from corporate income tax from 2000 to 2004 and will be entitled to a reduction in the corporate income tax rate to 7.5%, for the five years from 2005 to 2009.

Year ended 31st December, 2001 compared to year ended 31st December, 2000

Revenues

Aeronautical revenues

The Group's aeronautical revenues for the year 2001 were approximately RMB133.0 million, as compared to approximately RMB119.4 million in the year 2000, representing an increase of 11.4%. The increase was mainly due to the Meilan Airport's upgrade from civil airport Category III to Category II on 1st June, 2000. As a result, the passenger charges increased by 25% and aircraft movement fees for domestic airline increased by 10%. These increases contributed to the Group's revenue for only seven months in 2000 compared to the full year in 2001. The aeronautical revenues represent 71.9% of total revenues in the year 2001, as compared to 73.9% in the year 2000.

Total aircraft movements for the year 2001 was approximately 53,800 representing a decrease of 5.3% as compared to 56,800 in the year 2000. Passenger throughput for the year 2001 was approximately 5,079,000, which increased by 16.4% as compared to approximately 4,363,000 in the year 2000.

The decrease in aircraft movements was partially due to the fact that airlines using the Meilan Airport are changing from smaller, narrower aircrafts to bigger planes with more seats.

Non-aeronautical revenues

Revenues relating to the Group's non-aeronautical operations increased to approximately RMB52.0 million, representing an increase of 23.0% from the year 2000. The increase is mainly attributable to the increase of franchise fee and leasing income. Non-aeronautical revenues represented 28.1% of total revenues in 2001, as against 26.1% for the year 2000.

Leasing revenues were approximately RMB26.3 million, an increase of 14.6% from 2000. The increase was attributable to the additional commercial space becoming available during the year.

Franchise fee revenues were approximately RMB15.5 million, recording an increase of 31.2% from 2000. The increase was attributable to an increase in franchise fees for the in-flight catering operations in 2001.

The leasing of advertising spaces by the Group in 2001 generated revenues of approximately RMB4.0 million, representing a decrease of 21.0% from 2000.

Other revenues were approximately RMB6.2 million in 2001, representing an increase of 155.7% from 2000. The increase is primarily attributable to operation of electric departure boarding system set up in July 2000. In 2001, revenue generated from packaging and trolley services also increased substantially in terms of percentage.

Operating costs and expenses

The Group incurred total operating costs of approximately RMB60.2 million in 2001, decreasing as a percentage of total revenues to 32.6%, compared to 36.7% for 2000, and total operating cost increased 1.4% compared to 2000.

The costs of goods and services were approximately RMB13.4 million, virtually unchanged from that incurred for the year 2000.

Depreciation and amortisation expenses for the year 2001 was approximately RMB28.4 million, virtually unchanged from that incurred for the year 2000.

Staff costs decreased in the year 2001 by 10.0% to approximately RMB8.1 million. The decrease is mainly due to the improved operating efficiency.

Utility and power expenses for the year 2001 were approximately RMB7.2 million, virtually unchanged from that incurred for the year 2000.

Repairs and maintenance costs for the year 2001 were approximately RMB2.0 million, representing an increase of 101.8%. The increase is due to the timing of the maintenance cycle of the equipment installed in 1999.

Other costs for the year 2001 were approximately RMB1.1 million, representing an increase of 63.7% from 2000. The increase is primarily attributable to the increased marketing expenses from Meilan Advertising.

Gross profits for the year 2001 were approximately RMB118.0 million, representing an increase of 22.5% from 2000. Gross margin reached 63.8% in 2001 from 59.6% in 2000. That is primarily because in 2001 the Group achieved revenue growth of over 14.5% while its total operating cost increased by only 1.4%.

Administrative expenses and operating profit

Administrative expenses were approximately RMB12.9 million for the year 2001, representing a decrease of 14.9%. The decrease was due primarily to enhanced cost control in 2001, which resulted in the reduction of entertainment expenses by RMB0.4 million, transportation expenses by RMB0.45 million and wage expenses by RMB0.65 million.

The Group had operating profit of approximately RMB105.1 million in 2001, with operating margin of 56.8%, as compared to 50.2% in 2000. The increase of operating profit in 2001 was primarily attributable to the increased gross profits and decreased administrative expenses.

Non-operating income and expenses, taxation and net profit

Net finance expense for the year 2001 was approximately RMB17.7 million, compared to approximately RMB23.0 million for the year 2000, a decrease of 23.1%. The decrease was primarily due to the partial repayment of the Group's outstanding loans by RMB95 million in October 2000.

Profit before tax and after tax for the year 2001 was approximately RMB87.4 million, as compared to approximately RMB58.2 million for the year 2000, with after-tax margin of 47.2% in 2001 as compared to 36.0% in 2000, as a result of the above factors. No taxation is charged for the period.

On 19th July, 2002, the shareholders of the Company approved the distribution of a final dividend of RMB45 million for the year ended 31st December, 2001 to the then existing shareholders. The dividend was financed by internal sources.

Year ended 31st December, 2000 compared to year ended 31st December, 1999

Commercial operations commenced 25th May, 1999. Accordingly, data for 1999 reflects seven months of commercial operations and not directly comparable with subsequent periods.

Revenues

Aeronautical revenues

The Group's aeronautical revenues for 2000 were approximately RMB119.4 million. The figure for the year ended 31st December, 1999 was approximately RMB57.5 million. The aeronautical revenues represent 73.9% of total revenues in 2000, as compared to 71.4% in 1999. Given that the results of 1999 reflected the operations of the Group from the opening of the Meilan Airport on 25th May, 1999, the increase in aeronautical revenues was primarily attributable to the first full year of operation of the Meilan Airport in 2000.

Non-aeronautical revenues

Revenues relating to the Group's non-aeronautical operations were approximately RMB42.2 million, which represented 26.1% of total revenues. The figure for the year ended 31st December, 1999 was RMB23.0 million, representing 28.6% of total revenues.

Leasing revenues were approximately RMB23.0 million, representing 54.3% of non-aeronautical revenues. The figures for the year ended 31st December, 1999 were approximately RMB10.4 million and 45.3% respectively.

Franchise fee revenues were approximately RMB11.8 million, representing 28.0% of non-aeronautical revenues. The figures for the year ended 31st December, 1999 were approximately RMB6.6 million and 28.7% respectively.

Advertising revenues were approximately RMB5.1 million, representing 12.0% of non-aeronautical revenues. The figures for the year ended 31st December, 1999 were approximately RMB3.5 million and 15.4%, respectively.

Other revenues were approximately RMB2.4 million, representing 5.7% of non-aeronautical revenues. The figures for the year ended 31st December, 1999 were approximately RMB2.4 million and 10.6% respectively.

Operating costs and expenses

The Group incurred total operating costs of approximately RMB59.4 million in 2000, representing 36.7% of total revenues. The total operating costs in 1999 were RMB39.3 million, representing 48.8% of total revenues.

The costs of goods and services were approximately RMB13.4 million, representing 8.3% of total revenues. The figures for the year ended 31st December, 1999 were approximately RMB6.6 million and 8.2%, respectively.

Depreciation and amortisation expenses for the year 2000 were approximately RMB28.1 million, representing 17.4% of total revenues. The figures for the year ended 31st December, 1999 were approximately RMB21.3 million, and 26.4%.

Staff costs were approximately RMB9.0 million, equal to 5.6% of total revenues. The figures for the year ended 31st December, 1999 were approximately RMB5.8 million and 7.2%, respectively.

Utility and power expenses for the year 2000 were approximately RMB7.2 million, representing 4.4% of total revenues. The figures for the year ended 31st December, 1999 were approximately RMB4.8 million and 6.0%, respectively.

Repairs and maintenance costs for the year 2000 were approximately RMB1.0 million, representing 0.6% of total revenues. The figures for the year ended 31st December, 1999 were approximately RMB0.5 million and 0.6%, respectively.

Other costs for the year 2000 were approximately RMB0.7 million, representing 0.4% of total revenues. The figures for the year ended 31st December, 1999 were approximately RMB0.4 million and 0.4%, respectively.

Gross profit for the year 2000 was approximately RMB96.3 million, compared to RMB38.3 million for the year ended 31st December, 1999. Gross margin improved to 59.6% from 47.6% in 1999.

Administrative expenses and operating profit

Administrative expenses were approximately RMB15.2 million for the year 2000, equal to 9.4% of total revenues. The figures for the year ended 31st December, 1999 were approximately RMB8.4 million and 10.4%, respectively.

The Group had operating profit of approximately RMB81.2 million, with an operating margin of 50.2%, compared to an operating margin of 37.1% in 1999.

The increase of the Group's gross margin and operating margin in 2000 was primarily attributable to revenue growing faster than costs.

Non-operating income and expenses, taxation and net profit

Net finance expense for the year 2000 was approximately RMB23.0 million, compared to RMB22.1 million for the year ended 31st December, 1999.

Profit before tax and after tax for the year 2000 was approximately RMB58.2 million, with an after tax margin of 36.0%, a substantial improvement from the after tax margin of 9.7% in 1999. No taxation is charged for the period.

Pursuant to a resolution of shareholders dated 29th June, 2001, the Company made a distribution to Parent Company which represented the profit after tax of the Company for the period from 1st August, 2000 to 31st December, 2000. Such profit after tax was determined in accordance with relevant PRC accounting regulations.

PRO FORMA UNAUDITED COMBINED RESULTS OF THE GROUP

The pro forma unaudited combined results of the Group for the three years ended 31st December, 2001 and the five months ended 31st May 2002, as set out in Appendix II — Additional Financial Information to this prospectus, include the results of the businesses and assets comprising the Group as if the businesses and assets swapped between the Group and Parent Company described under the section headed "Business — Asset Swap" which took place on 31st May, 2002 had taken place on 1st January, 1999, or the acquired companies' respective dates of incorporation, whichever is later. The businesses and assets purchased by the Group consist of the following:

- Assets of the cargo centre including related land use rights;
- Car parking spaces including related land use rights;
- 60% of the registered capital of Meilan Travelling; and
- 95% of the registered capital of DFG; and

assets sold to Parent Company including:

- equipment centre including related land use rights;
- various power generation, transformation and transmission equipment; and
- vehicle storage including related land use rights.

The pro forma unaudited combined results of operations of the Group do not purport to represent what the results of operations would actually have been if the above mentioned asset swap had taken place on 1st January, 1999, or to project the results of operations for any future period but are included for information purposes only.

The following is a summary of the pro forma unaudited combined results of the Group for the three years ended 31st December, 2001 and the five months ended 31st May 2002, which have been extracted from the Additional Financial Information set out in Appendix II to the Prospectus.

	Pro forma combined (unaudited)			
	Year ended 31st December,			Five months ended 31st May,
	1999[1]	2000	2001	2002
	(RMB'000)			
Revenues				
Aeronautical[2]				
Passenger charges	41,766	90,371	102,283	50,584
Airport fee	—	—	—	29,442
Ground handling services fee	10,091	18,371	20,556	10,644
Aircraft movement fees and related charges	5,642	10,661	10,198	5,138
Total aeronautical revenues	57,499	119,403	133,037	95,808
Non-aeronautical				
Tourism services	—	—	2,516	11,152
Leasing of commercial areas, counters and office in the Terminal	10,266	22,519	25,232	10,257
Franchise fees[3]	6,592	11,809	24,990	10,555
Sales of duty-free and other retail goods	1,966	2,952	4,586	2,976
Advertising fees	3,530	5,087	4,018	2,021
Car parking	725	1,181	2,648	1,018
Other revenues	2,437	2,423	6,195	3,162
Total non-aeronautical revenues	25,516	45,971	70,185	41,141
Total revenues	83,015	165,374	203,222	136,949

	Year ended 31st December,			Five months ended 31st May,
	1999[1]	2000	2001	2002
		(RMB'000)		
Business taxes and levies	(2,968)	(6,017)	(7,288)	(4,655)
Net revenues	80,047	159,357	195,934	132,294
Operating costs				
Cost of goods and services	(8,003)	(15,566)	(17,003)	(11,101)
Depreciation and amortisation	(21,656)	(28,615)	(30,522)	(13,031)
Staff costs	(5,793)	(9,008)	(8,251)	(3,923)
Utilities and power	(4,804)	(7,183)	(7,225)	(2,688)
Repairs and maintenance	(459)	(994)	(2,006)	(381)
Other costs	(314)	(629)	(1,354)	(1,186)
Total operating costs	(41,029)	(61,995)	(66,361)	(32,310)
Gross profit	39,018	97,362	129,573	99,984
Selling and distribution expenses	(450)	(618)	(620)	(575)
Administrative expenses	(8,505)	(15,600)	(13,778)	(8,433)
Profit from operating activities	30,063	81,144	115,175	90,976
Finance expenses, net	(22,072)	(22,985)	(17,698)	(7,678)
Profit before tax	7,991	58,159	97,477	83,298
Tax[4]	—	—	—	—
Profit after tax	7,991	58,159	97,477	83,298
Minority interests	8	32	(9)	(45)
Net profit attributable to shareholders	7,999	58,191	97,468	83,253
Distribution to Parent Company[5]	—	29,081	—	—
Final Dividend[6]	—	—	45,000	—
EPS[7]	0.03	0.23	0.39	0.33
EBITDA[8]	51,719	109,759	145,697	104,007

(1) Commercial operations of the Meilan Airport commenced on 25th May, 1999. Accordingly, the relevant data for 1999 reflects only seven months of commercial operations and therefore are not directly comparable with those of the subsequent years.

(2) The presentation of the historical figures throughout the Track Record Period for the following aeronautical revenues reflect the revenue sharing arrangement between the Company and Parent Company, on the basis of 75% to the Company and 25% to Parent Company:

- Aircraft movement fees;
- Passenger charges; and
- Basic ground handing services fees charged to Hong Kong, Macau and foreign airlines.

(3) The pro forma franchise fees for the Track Record Period consist of the following items:

- Annual fees from Hainan Food with respect to the air catering rights at the Meilan Airport;
- Annual fees from Hainan Airlines in 1999 and 2000 and from Yangzi Express in 2001 and the first five months of 2002 with respect to the right to operate the cargo centre at the Meilan Airport;
- Annual fees from THIA with respect to the right to sell accident insurance policies at the Meilan Airport; and
- Fees from HLAS with respect to air ticketing operation at the Meilan Airport.

(4) The Company is entitled to an exemption from corporate income tax from 2000 to 2004, and a reduced income tax rate of 7.5% from 2005 to 2009. Please refer to subsection "Financial Information — Taxation" for details.

(5) Pursuant to a resolution of shareholders dated 29th June, 2001, the Company made a distribution to Parent Company which represented the profit after tax of the Company for the period from 1st August, 2000 to 31st December, 2000. Such profit after tax was determined in accordance with the relevant PRC accounting regulations.

(6) On 19th July, 2002, the shareholders of the Company approved the distribution of a final dividend of RMB45 million for the year ended 31st December, 2001 to the then existing shareholders.

(7) The calculation of pro forma earnings per Share is based on the Group's profit attributable to shareholders for each of the three years ended 31st December, 2001 and for the five months ended 31st May, 2002 and on the 250,000,000 shares deemed to have been in issue and issuable during the Track Record Period.

(8) Pro forma EBITDA (earnings before interest, tax, depreciation and amortisation) should not be construed as an alternative to operating income or any other measure of performance or as an indicator of the Group's operating performance, liquidity or cash flows generated by operating, investing and financing activities. The items of net income excluded pro forma EBITDA are significant components in understanding and assessing the Group's financial performance, and the Group's computation of pro forma EBITDA may not be comparable in other similarly titled measures of other companies. The Group has included the information concerning pro forma EBITDA because the Directors believe that it is an useful supplement to cash flow data as a measure of the Group's performance.

TAXATION

Business tax and levies

Business taxes and levies are levied at the rate of 3.3% in the case of aeronautical revenues (including Airport Fees) and at the rate of 5.4% in the case of revenues from franchise fees, car parking fees and commercial leasing and at the rate of 8.4% in the case of revenues from the leasing of advertising space respectively. Levies include urban construction fee, education surcharge and cultural affairs establishment fee.

Corporate income tax

The Company is subject to corporate income tax at the statutory tax rate of 15% on taxable income including Airport Fee (which was not subject to any corporate income tax before 1st January, 2002), the rate applies to companies incorporated in the Special Economic Zone of Hainan Province. The Company is entitled to preferential treatment granting an exemption from corporate income tax for the first five years from its first profitable year, and a 50% reduction in the corporate income tax for the following five years. The first profitable year of the Company was the year ended 31st December, 2000. It therefore enjoys an exemption from corporate income tax from 2000 to 2004 and will be entitled to a reduction in the corporate income tax rate to 7.5%, for the five years from 2005 to 2009.

Each subsidiary of the Company is also subject to corporate income tax at the statutory tax rate of 15% on its taxable income.

PROFIT FORECAST AND DIVIDEND POLICY

Profit Forecast

The Directors forecast that, in the absence of unforeseen circumstances, the consolidated profit after tax and minority interests but before extraordinary items of the Group for the year ending 31st December, 2002, will not be less than RMB156 million (equivalent to approximately HK$147 million). The Directors were not aware of any extraordinary items which had arisen as of the Latest Practicable Date. See Appendix III to this prospectus.

FORECASTS FOR THE YEAR ENDING 31ST DECEMBER, 2002

Forecast consolidated profit after tax and minority interests but before extraordinary items(1)	not less than RMB156 million (HK$147 million)
Forecast earnings per Share	
— pro forma fully diluted(2)	RMB0.36 (HK$0.34)
— weighted average(3)	RMB0.57 (HK$0.54)

(1) The bases on which the above profit forecast has been prepared are set out in Appendix III to this prospectus.

(2) The calculation of the forecast earnings per Share on a fully diluted basis is based on the forecast consolidated profit after tax and minority interest but before extraordinary items for the year ending 31st December, 2002, assuming that the Company had been listed on the Stock Exchange since 1st January, 2002 and a total of 448,000,000 Shares were in issue during the entire year. The estimated earnings per Share has been adjusted to take into account the interest income that would have been earned if the estimated net proceeds from the Offering were received on 1st January, 2002 on the basis of an interest rate of 0.98% per annum. It should be noted, however, that the net proceeds of the Offering will not in fact be invested to earn interest income, except as described in the section headed "Future Plans and Use of Proceeds". Please refer to the descriptions therein for the details on how the proceeds are intended to be used. These calculations assume that the Over-allotment Option will not be exercised, and the H Shares issued pursuant to the Offering were issued on 1st January, 2002 at an Offer Price of HK$3.47 per H Share (being the mid-point of the proposed Offer Price range of HK$3.15 to HK$3.79 per H Share) (excluding brokerage, Stock Exchange trading fee and the SFC transaction levy, which are payable by applicants in the Offering).

(3) The calculation of the forecast earnings per Share on a weighted average basis is based on the forecast consolidated profit after tax and minority interest but before extraordinary items and a weighted average number of 273,868,493 Shares assumed to be in issue during the year. The calculation assumes that the Over-allotment Option will not be exercised and the H Shares will be issued on 18th November, 2002.

Dividend Policy

On 19th July, 2002, the shareholders of the Company approved the distribution of a final dividend of RMB45 million for the year ended 31st December, 2001 to the then existing shareholders. The dividend was financed by internal sources.

The Articles of Association permit the Company to distribute dividends or make other distributions according to an ordinary resolution of the shareholders, and prevent the Company from distributing dividends or bonuses without first making up for losses and making all tax and other payments required by law. Under the Articles of Association, the Company may, in addition to final dividend, distribute interim or special dividends in the form of cash or shares. In accordance with the Articles of Association, the distributable profits available to the Company for the purpose of profit distribution will be deemed to be the lesser of:

1. the net income determined in accordance with PRC accounting standards and regulations; and

2. the net income determined in accordance with IAS.

However, prior to payment of dividends, profits of the Company are subject to deductions such as allocations to the statutory common reserve and the statutory public welfare fund. The Company's outstanding credit facilities do not impose any restrictions on its ability to pay dividends. See the section headed "Financial Information — Liquidity and Capital Resources — Capital Resources" of this section.

Subject to the foregoing, the Company intends to make interim dividend payments in or about October of each year and final dividend payments in or about June of each year. It is the present intention of the Directors that, for each year, the interim dividend will represent approximately 25% of the total estimated dividends to be paid for the entire year (except for the financial year of 2002 where no interim dividend will be declared) and that the sum of interim and final dividend will represent approximately 60% (for each of the financial years of 2002 and 2003) or 50% (for each subsequent financial year) of the Company's net profit attributable to shareholders before deduction of statutory reserves for the relevant financial year determined in accordance with IAS, and limited to the distributable profits available pursuant to the Articles of Association. The distribution of dividend will be dependent upon the Company's earnings, financial conditions, cash requirements and availability, the provisions of the PRC Company Law and other factors. There is no assurance as to whether the dividend distribution will occur as intended, the amount of dividend payment or the timing of such payment.

The Articles of Association require that cash dividends of H Shares will be declared in Renminbi and paid in Hong Kong dollars to H Shareholders. Conversion of Renminbi into Hong Kong dollars will be subject to the relevant PRC foreign exchange regulations and will be calculated at an exchange rate which will be the average of the PBOC Exchange Rate one calendar week preceding the date of declaration of dividends. If the Company does not have sufficient foreign exchange reserves to pay its Hong Kong dollars dividends, it intends to exchange its RMB funds into the required Hong Kong dollars from authorised banks or through other approved means. There is no assurance that the Company will be able to obtain Hong Kong dollar funds as needed.

ADJUSTED NET TANGIBLE ASSETS

The following pro forma statement of adjusted net tangible assets of the Group is based on the consolidated net assets of the Group as at 31st May, 2002 as set out in Appendix I, adjusted as described below:

		RMB'000
Consolidated net assets of the Group as at 31st May, 2002 as set out in the Accountants' Report in Appendix I of the prospectus of the Company		484,172
Negative goodwill		260
Consolidation net tangible assets of the Group as at 31st May, 2002		484,432
Final dividend for year ended 31st December, 2001	*Note (i)*	(45,000)
Surplus arising from the revaluation of the Group's property, plant and equipment	*Note (ii)*	40,089
Unaudited consolidated profit after tax and minority interests for the three months ended 31st August, 2002		36,545
Estimated net proceeds from the Offering	*Note (iii)*	681,290
Adjusted net tangible assets		1,197,356
Adjusted net tangible assets value per Share (based on the 246,300,000 Domestic Shares and 201,700,000 H Shares expected to be in issue immediately after completion of the Offering)		RMB2.67

(i) On 19th July, 2002, the shareholders of the Company approved the distribution of a final dividend of RMB45 million for the year ended 31st December, 2001 to the then existing shareholders.

(ii) The surplus arising from the revaluation of the Group's property, plant and equipment amounted to approximately RMB40,089,000 and will be incorporated into the Group's financial statement for the year ending 31 December 2002. The annual depreciation charge will be increased by approximately RMB2,248,000 following the incorporation of the revaluation surplus. The surplus arising from the revaluation of the Group's land use rights amounted to approximately RMB7,328,000 and will not be incorporated into the Group's financial statements. Had the revaluation results of the land use rights been incorporated in the Group's financial statements, the annual amortisation charge would have been increased by approximately RMB147,000. A copy of the revaluations report is set forth in Appendix IV to this prospectus.

(iii) Without considering the Over-allotment Option and assuming the Offer Price of RMB3.68 (HK$3.47) per H Share. If the Over-allotment Option is exercised in full, the adjusted net tangible assets value per Share will be slightly increased and the earnings per Share will be diluted correspondingly. However, the Directors do not believe that this will have material effect on the shareholders of the Company.

DISTRIBUTABLE RESERVE

In accordance with the relevant laws and regulations in the PRC, the profits available for distribution are based on the statutory financial statements of the Company. At 31st May, 2002, the distributable profits of the Company amounted to RMB87,644,000 (equivalent to approximately HK$82,597,000).

NO MATERIAL CHANGE

The Directors confirm that up to the Latest Practicable Date, there was no material adverse change in the financial or trading position or prospect of the Group since 31st May, 2002, the date of the latest audited consolidated financial statements of the Group.

FUTURE PLANS AND PROSPECTS

The Group's strategy is to maintain and capitalise on the position of Meilan Airport as the main gateway to Hainan and to seek sustainable long-term growth in its aeronautical and non-aeronautical related businesses.

For aeronautical businesses, the Group plans to expand and improve the existing facilities at the Meilan Airport, including the Terminal and apron, and to build new facilities, including a new cargo centre and cargo aircraft parking apron, a new customs and inspection joint operation building, in anticipation of future air traffic increase and the attainment of international airport status.

The Group will seek to increase its non-aeronautical business, which contributed approximately 28.6%, 26.1%, 28.1% and 19.1% of the total revenue in each of the three years ended 31st December, 2001 and the first five months of 2002. The Group will explore opportunities to further increase the advertising spaces and commercial areas for leasing at the Meilan Airport. Further, the Group will seek to increase the utilisation rate of the available advertising spaces and of commercial area in conjunction with the expected growth of passenger traffic.

In addition, the Group is committed to improving quality of service by developing more training programmes for its management and staff. The Group also plans to strengthen communications and cooperation with other governmental and business entities that operate at the Meilan Airport.

The Directors believe that the Group can capitalise on its experience in managing airport business. The Company signed the Sanya Management Contract with SPIA on 23rd August, 2002 to manage the Sanya Airport. The Company intends to establish its reputation as a premier airport operator in the PRC.

Parent Company has granted the Company an option to acquire from Parent Company aeronautical or non-aeronautical businesses and assets owned by it from time to time. The Group plans to take advantage of such opportunities to achieve revenue and earnings growth, as well as economies in planning, procurement and services. The Group intends to fund the cost of possible acquisitions and capital expenditures with its internal resources, loan financing and possible future issues of shares.

Based on the report prepared by Booz Allen Hamilton, the air traffic by passenger throughput at the Meilan Airport is expected to increase by approximately 10.2% and 9.2% annually from 2001 to 2006 and from 2001 to 2011 respectively. See Appendix V to this prospectus. With the expansion and improvement of the Terminal and aprons, the Group expects to be able to capture the business opportunities associated with the expected air traffic increase.

REASONS FOR THE OFFERING AND THE USE OF PROCEEDS

The Directors intend to use the net proceeds of the Offering of the New H Shares to finance the Group's capital expenditure, strengthen its capital base and improve its financial position.

The net proceeds of the Offering of the New H Shares (after deduction of underwriting fees and estimated expenses payable by the Group in relation to the Offering, assuming the Over-allotment Option is not exercised and assuming an Offer Price of HK$3.47 per H Share, being the mid-point of the Offer Price range of HK$3.15 to HK$3.79 per H Share) are estimated to be approximately HK$642.0 million (HK$727.4 million, if the Over-allotment Option is fully exercised). The Group currently intends to use the net proceeds from the Offering in the following approximate proportion:

- approximately RMB392.0 million (HK$369.4 million) for the airport expansion project. The project includes construction of approximately 30,000 m^2 of expanded Terminal area, an aircraft parking apron of approximately 280,000 m^2, 20 aircraft parking positions and eight aircraft parking positions with air bridges;

- approximately RMB198.0 million (HK$186.6 million) for the construction of a new cargo centre with a floor area of approximately 30,000 m^2 and aprons with an area of approximately 50,000 m^2 with four aircraft parking positions;

- approximately RMB70.0 million (HK$66.0 million) for the renovation of the Terminal and construction of a customs and inspection joint operation building for international passengers and cargoes; and

- the balance of RMB21.2 million (HK$20 million) is expected to be used as general working capital of the Group and for other general corporate purposes. It may be used to acquire or invest in complementary businesses or to establish joint ventures that the Group believes will complement its current or future business. However, the Group has no specific agreements or commitments at this stage relating to any material acquisition.

Pending the use of the net proceeds of the Offering of the New H Shares for the purposes described above, the Group intends to place the net proceeds, to the extent permitted by relevant PRC laws and regulations, in short-term bank deposits or in money market instruments in accounts maintained with banks in the PRC.

In the event that any part of the business plan of the Group does not materialise or proceed as planned, the Directors will carefully evaluate the situation and may reallocate the intended funding to other business plans and/or new projects and/or hold such funds in short-term deposit for so long as the Directors deem to be in the best interests of the Company and its shareholders taken as a whole.

In the event that there is any material modification to the use of proceeds as described above, the Company will issue an announcement of the change as soon as practicable.

UNDERWRITERS

Public Offer Underwriters

The Hongkong and Shanghai Banking Corporation Limited
Oriental Patron Asia Limited
CITIC Capital Markets Limited
ICEA Capital Limited
ING Bank N.V.
Nomura International (Hong Kong) Limited

International Placing Underwriters

The Hongkong and Shanghai Banking Corporation Limited
Oriental Patron Asia Limited
CITIC Capital Markets Limited
ICEA Capital Limited
ING Bank N.V.
Nomura International (Hong Kong) Limited

Strategic Placing Underwriter

The Hongkong and Shanghai Banking Corporation Limited

UNDERWRITING ARRANGEMENTS AND EXPENSES

Underwriting Agreements

Pursuant to the Public Offer Underwriting Agreement, the Company is offering the Public Offer Shares for subscription and purchase respectively at the Offer Price by members of the public in Hong Kong under the Public Offer on and subject to the terms and conditions of this prospectus and the application forms relating thereto. It is expected that the International Placing Agreement will be entered into on or about 12th November, 2002. Pursuant to the Strategic Investment Agreement and the International Placing Agreement, the Company will offer the Strategic Placing Shares through the Strategic Placing Underwriter for subscription at the Offer Price by the Strategic Investor under the Strategic Placing and the International Placing Shares (other than the Strategic Placing Shares) through the International Placing Underwriters for subscription at the Offer Price by professional, institutional and private investors under the International Placing respectively. Subject to the satisfaction of certain conditions precedent, including:

(a) the Listing Committee of the Stock Exchange granting the listing of, and permission to deal in, the H Shares to be issued as mentioned in this prospectus on or before the 30th day following the date of this prospectus;

(b) the execution and delivery of the Public Offer Underwriting Agreement, the International Placing Agreement and the Price Determination Agreement on or before the Price Determination Date; and

(c) each of the Public Offer Underwriting Agreement, the International Placing Agreement and the Strategic Investment Agreement becoming unconditional in accordance with its terms, the International Placing Underwriters (including the Strategic Placing Underwriter) have severally agreed to subscribe for or procure placees to subscribe for, subject to the terms and conditions of the International Placing Agreement, their respective applicable proportions of the International Placing Shares (which includes the Strategic Placing Shares) and the Public Offer Underwriters have severally agreed to subscribe for or purchase or procure subscribers or purchasers to subscribe for or purchase, on the terms and conditions of this prospectus and the application forms, the Public Offer Shares which are not taken up under the Public Offer.

Grounds for termination

The obligations of the Public Offer Underwriters under the Public Offer Underwriting Agreement are subject to termination if, at any time prior to 6:00 p.m. on 17th November, 2002:

(i) there shall develop, occur, exist or come into effect:

(a) any new law or regulation or any change in existing laws or regulations or any change in the interpretation or application thereof by any court or other competent authority of any relevant jurisdiction; or

(b) any change or development in the conditions of Hong Kong, PRC, US or international equity securities or other financial markets; or

(c) any change or development involving a prospective change in, or any event or series of events resulting or likely to result in any change or development in local, national or international financial, political, military, industrial, legal, fiscal, economic, regulatory or market matters or conditions in the PRC, Hong Kong or US (including but not limited to a devaluation of RMB against any foreign currencies); or

(d) the imposition of any moratorium, suspension or restriction on trading in securities generally on the Stock Exchange due to exceptional financial circumstances or otherwise; or

(e) a change or development involving a prospective change in taxation or exchange control (or the implementation of any exchange control) or foreign investment regulations in the PRC, Hong Kong or any other jurisdiction relevant to the Company; or

(f) any general moratorium on commercial banking activities in Hong Kong shall have been declared by the Hong Kong authorities, or in the PRC by the relevant PRC authorities; or

(g) any imposition of economic sanctions, in whatever form, by the US on Hong Kong, the PRC or any other jurisdiction relevant to the Company; or

(h) the outbreak or escalation of hostilities involving the PRC or Hong Kong or the US or any other jurisdiction relevant to the Company; or

(i) any act of God, war, riot, public disorder, civil commotion, fire, flood, explosion, epidemic, terrorism, strike or lock out; or

(j) any adverse change or prospective adverse change in the business or in the financial or trading position of the Company.

which, in the opinion of HSBC (on behalf of the Public Offer Underwriters):

(1) is or will or is likely to be materially adverse to the business, financial or other condition or prospects of the Group taken as a whole in the case of sub-paragraph (e) above, to any present or prospective shareholder in his capacity as such; or

(2) has or will have or is likely to have a material adverse effect on the success of the Offering or any of the Public Offer or the International Placing or the Strategic Placing or the full subscription and purchase of all of the Offer Shares; or

(3) makes it inadvisable or inexpedient to proceed with the Offering or any of Public Offer or the International Placing or the Strategic Placing; or

(ii) any statement contained in this prospectus or the application forms becomes or is discovered to be untrue, inaccurate, incomplete or misleading in any respect considered by HSBC to be material with reference to the facts and circumstances then subsisting; or

(iii) any matter or event arising or having been discovered rendering or there coming to the notice of the Joint Sponsors or any of the Underwriters any matter or event showing any of the warranties given by the Company or Parent Company to be untrue, inaccurate or misleading or having been breached in any respect or having been declared or determined by any PRC court or governmental authorities to be illegal, invalid or unenforceable in any respect considered by HSBC to be material; or

(iv) any breach on the part of the Company and/or the Directors and/or the covenantors named in the Public Offer Underwriting Agreement of any of the provisions of the Public Offer Underwriting Agreement, the International Placing Agreement or the Price Determination Agreement in any respect considered by HSBC to be material.

Undertakings

Parent Company has undertaken with the Company and the Public Offer Underwriters that, subject always to the provisions of the Listing Rules, it will not dispose of any of its interests in any Domestic Shares beneficially owned by it (directly or indirectly) and/or registered in its name at any time on or prior to the date on which dealings in the H Shares first commence on the Stock Exchange: (i) at any time up to and including the date falling six months after the date on which dealings in the H Shares first commence on the Stock Exchange (the "First Six Month Period"); (ii) at any time after the date of expiration of the First Six Month Period up to and including the date falling six months from such date (the "Second Six Month Period") so as to result in it ceasing to be a controlling shareholder (as defined in the Listing Rules from time to time) of the Company; and (iii) in the event of a disposal of any such interest within the Second Six Month Period all reasonable steps will be taken up by Parent Company to ensure that any such disposal will not create a disorderly or false market in the H Shares.

Parent Company further undertakes with the Stock Exchange and the Company that within the period of 12 months from the date on which dealings in the H Shares first commence on the Stock Exchange:

(a) if Parent Company pledges/charges any securities of the Company beneficially owned by it, it will immediately inform the Company and the Joint Sponsors of such pledges/charges together with the number of securities so pledged/charged; and

(b) if Parent Company receives indications, either verbal or written, from the pledgee/chargee that any of the pledged/charged securities of the Company will be disposed of, it will immediately inform the Company and the Joint Sponsors of such indications.

The Company has undertaken with the Public Offer Underwriters that except pursuant to the Offering including the Over-allotment Option, it will not: (i) at any time within the First Six Month Period, issue new Shares or grant any options or right to subscribe for any Shares; (ii) at any time within the Second Six Month Period issue new Shares or grant any options or right to subscribe for Shares so as to dilute Parent Company's shareholding in the Company such that Parent Company would cease to be the controlling shareholder (as such term is defined from time to time in the Listing Rules) of the Company.

Commissions and expenses

The Public Offer Underwriters will receive, and the International Placing Underwriters are expected to receive, an underwriting commission of 2.5% of the Offer Price multiplied by the aggregate underwriting commitment of the Underwriters, and HSBC and Oriental Patron will also receive a documentation fee. The documentation fee, together with the Stock Exchange listing fees, legal and other professional fees, printing, and other expenses relating to the Offering, which are estimated to be approximately HK$45 million in aggregate, will be borne by the Company.

The underwriting commission relating to the New H Shares will be borne by the Company and the underwriting commission relating to the Sale H Shares will be deducted from the net proceeds to be delivered to the National Social Security Fund.

Underwriters' interest in the Company

Save as disclosed in this prospectus, none of the Underwriters or any of their respective holding companies, or any of their respective subsidiaries is interested beneficially or legally in any Shares of the Company or has any right (whether legally enforceable or not) or option to subscribe for or purchase, or to nominate persons to subscribe for or purchase any Shares in the Company.

The International Placing

In connection with the International Placing, it is expected that the Company and Parent Company will enter into the International Placing Agreement with the International Placing Underwriters. Under the International Placing Agreement, the International Placing Underwriters would severally agree to subscribe for the 181,530,000 H Shares being offered pursuant to the International Placing which are not taken up under the International Placing.

The Company intends to grant to the International Placing Underwriters the Over-allotment Option exercisable by HSBC on behalf of the International Placing Underwriters to require the Company to allot and issue up to an aggregate of 25,213,000 additional New H Shares at the Offer Price solely to cover over-allocations in the International Placing, if any, within 30 days after the date of this prospectus.

As part of the International Placing, the Company has entered into the Strategic Investment Agreement with the Strategic Investor and the Strategic Placing Underwriter under which the Strategic Investor has agreed to subscribe for the Strategic Placing Shares through the Strategic Placing Underwriter upon and subject to the terms and conditions of the Strategic Investment Agreement.

PRICING OF THE OFFERING

The Offer Price is expected to be fixed by agreement between the Joint Sponsors, on behalf of the Underwriters, and the Company on the Price Determination Date, when market demand for the H Shares is determined. The Price Determination Date is expected to be on or around 12th November, 2002 and in any event no later than 5:00 p.m. on 14th November, 2002 (Hong Kong time).

The Offer Price will not be more than HK$3.79 per Offer Share and is expected to be not less than HK$3.15 per Offer Share. The Offer Price will fall within the Offer Price range as stated in this prospectus unless otherwise announced, as further explained below, not later than the morning of the latest day for lodging applications under the Public Offer. The Global Coordinator on behalf of the Underwriters may where considered appropriate, based on the level of interest expressed by prospective professional, institutional and private investors during the book-building process, and with the consent of the Company reduce the indicative Offer Price range below that stated in this prospectus at any time prior to the morning of the latest day for lodging applications under the Public Offer. In such a case, the Company will as soon as practicable following the decision to make such reduction, and in any event not later than the morning of the day which is the latest day for lodging applications under the Public Offer, cause there to be published in the South China Morning Post and the Hong Kong Economic Times notices of the reduction in the indicative Offer Price range. Upon issue of such a notice, the revised Offer Price range will be final and conclusive and the Offer Price, if agreed upon with the Company, will be fixed within such revised Offer Price range. Such notice will also include confirmation or revision, as appropriate, of the working capital statement and the offering statistics, as currently set out in the section headed "Summary" and any other financial information which may change as a result of such reduction. If applications for Public Offer Shares have been submitted prior to the day which is the last day for lodging applications under the Public Offer, then even if the Offer Price range is so reduced such applications cannot be subsequently withdrawn. In the absence of any notice being published in the South China Morning Post and the Hong Kong Economic Times of a reduction in the indicative Offer Price range stated in this prospectus on or before the morning of the last day for lodging applications under the Public Offer, the Offer Price, if agreed upon with the Company, will under no circumstances be set outside the Offer Price range as stated in this prospectus.

The net proceeds from the Offering assuming that the Over-allotment Option is not exercised and an Offer Price of HK$3.47 (being the mid-point between the maximum and minimum Offer Prices in the proposed Offer Price range of HK$3.15 and HK$3.79 and after deducting commissions and expenses) are estimated to be approximately HK$642.0 million (excluding proceeds from Sale H Shares). If the Over-allotment Option is exercised in full and assuming an Offer Price of HK$3.47 the Company would receive net proceeds (after deducting commissions and expenses attributable to the exercise of the Over-allotment Option) of approximately HK$727.4 million (excluding proceeds from Sale H Shares).

If the Offer Price as finally determined is less than HK$3.79 per Offer Share (being the maximum amount that the Offer Price can be fixed), appropriate refund payments (including the brokerage, the SFC transaction levy and the Stock Exchange trading fee attributable to the surplus application monies) will be made to successful applicants, without interest. Details of the procedure for refund are set out in the section "How to apply for Public Offer Shares — Despatch/Collection of Share Certificates and Refund Cheques".

If no agreement on the Offer Price can be reached between the Company and the Joint Sponsors by 5:00 p.m. on 14th November, 2002 (Hong Kong time), the Offering will not become unconditional and will lapse. An announcement of the determination of the Offering will be made to the public as soon as practicable but not later than 15th November, 2002.

PRICE PAYABLE ON APPLICATION

Investors under the Public Offer will pay the Offer Price of HK$3.79 (being the top end of the proposed Offer Price range) plus one percent brokerage, an SFC transaction levy of 0.007% and a Stock Exchange trading fee of 0.005%, constituting a total of HK$3,828.36 per board lot of 1,000 H Shares.

CONDITIONS OF THE OFFERING

Acceptance of all applications for the allotment of the H Shares will be conditional on:

1. the Listing Committee of the Stock Exchange granting listing of, and permission to deal in, the H Shares in issue and the H Shares to be issued pursuant to the Offering (including the additional H Shares to be issued pursuant to the exercise of the Over-allotment Option); and

2. the obligations of the Underwriters under the Underwriting Agreements becoming unconditional (including, if relevant, as a result of the waiver of any condition(s) by HSBC (acting on behalf of the Underwriters)) and not being terminated in accordance with the terms thereof.

If such conditions have not been fulfilled or waived prior to the times and dates specified, the Offering will lapse and the Stock Exchange will be notified immediately. In such event all application monies will be returned, without interest. The terms in which the money will be returned are set out under the section headed "Refund of your money" on the application forms. In the meantime, all application monies will be held in a separate bank account(s) with the receiving banker or other bank(s) licenced under the Banking Ordinance (Chapter 155 of the Laws of Hong Kong).

THE OFFERING

The Offering comprises the Public Offer and the International Placing. A total of 201,700,000 H Shares will initially be made available under the Offering, of which 181,530,000 H Shares, representing 90% of the H Shares initially available under the Offering, and will be conditionally placed with professional, institutional and private investors (including the Strategic Investor) under the International Placing. The remaining 20,170,000 H Shares, representing 10% of the number of H Shares initially being offered under the Offering, will be offered to members of the public in Hong Kong under the Public Offer. Both the International Placing and the Public Offer are subject to reallocation on the basis described under the paragraph "The Public Offer".

The Public Offer is open to all members of the public in Hong Kong, as well as to institutional and professional investors. The Public Offer Underwriters have agreed to underwrite the Public Offer Shares and the International Placing Underwriters are expected to underwrite the International Placing Shares, respectively, under the terms of the Underwriting Agreements. Particulars of the underwriting arrangements are set out under the section headed "Underwriting" in this prospectus.

All decisions concerning the allocation of International Placing Shares to prospective placees pursuant to the International Placing will be made on the basis of and by reference to a number of factors including the level and timing of demand, total size of the relevant investor's invested assets or equity assets in the relevant sector and whether or not it is expected that the relevant investor is likely to buy further, and/or hold or sell its International Placing Shares, after the listing of the H Shares on the Stock Exchange. Such allocation is intended to result in a distribution of the International Placing Shares on a basis which would lead to the establishment of a solid shareholders base to the benefit of the Company and its shareholders as a whole. In addition, the Directors and HSBC will use their best endeavours to observe the minimum public float requirement under the Listing Rules when making allocations of the International Placing Shares to investors who are anticipated to have a sizeable demand for such H Shares.

Investors may apply for the H Shares under the Public Offer or indicate an interest in the H Shares under the International Placing, but may not do both. If you apply for the H Shares under the Public Offer and the International Placing, you will only receive the H Shares under either the Public Offer or the International Placing, but not both tranches. If you apply for the Public Offer Shares, you are required to declare on your application form that you have not been allotted (conditionally) any International Placing Shares. The Company, the Directors, HSBC and Oriental Patron will take reasonable steps to identify and reject any multiple applications which are not allowed and will be rejected.

In connection with the Offering, the Company intends to grant the Over-allotment Option to the International Placing Underwriters, exercisable on their behalf by HSBC at any time and from time to time within 30 days from the date of this prospectus. Pursuant to the Over-allotment Option, the Company may be required to allot and issue, at the Offer Price, up to an additional 25,213,000 H Shares, representing approximately 12.5% of the number of H Shares initially being offered under the Offering, to cover over-allocations in the International Placing. HSBC may also cover such over-allocations by a combination of (i) purchases in the secondary market; and/or (ii) exercise of the Over-allotment Option, either in part or in full; and/or (iii) stock borrowing. Any such secondary market purchases will be made in compliance with all applicable laws and regulatory requirements and the price of any such secondary market purchases shall not exceed the Offer Price. If the Over-allotment Option is exercised in full, the H Shares will represent approximately 47.95% of the Company's enlarged issued share capital following completion of the Offering and full exercise of the Over-allotment Option. In the event that the Over-allotment Option is exercised, a press announcement will be made.

THE PUBLIC OFFER

The Company is initially offering 16,470,000 New H Shares for subscription and the 3,700,000 Domestic Shares held by the Vendors will be converted into Sale H Shares and will be offered for purchase at the Offer Price, together representing 10% of the H Shares initially being offered under the Offering, by members of the public in Hong Kong. The Public Offer is fully underwritten by the Public Offer Underwriters, subject to agreement as to pricing and other terms and conditions of the Public Offer Underwriting Agreement.

Multiple applications or suspected multiple applications or any application for more than 50% of the Public Offer Shares initially available or applications where cheques or banker's cashier orders are dishonourable upon first presentation will be rejected. Each applicant under the Public Offer will also be required to give an undertaking and confirmation in the application form submitted by him that he and any person(s) for whose benefit he is making the application have not indicated and will not indicate an interest for, and have not received or been placed or allotted (including conditionally and/or provisionally) with, any H Shares under the International Placing, and such applicant's application will be rejected if the said undertaking and/or confirmation is breached and/or untrue (as the case may be). The Company, the Directors, HSBC and Oriental Patron will reject applications in the Public Offer from investors who received the H Shares in the International Placing.

The Public Offer Shares (taking account of any adjustment of Offer Shares between the International Placing and the Public Offer referred to below) will be divided equally into two pools for allocation purposes: pool A and pool B. The Public Offer Shares in pool A will consist of not less than 10,085,000 H Shares and will be allocated on an equitable basis to successful applicants who have applied for Public Offer Shares with an aggregate price (excluding amounts of brokerage, SFC transaction levy and Stock Exchange trading fee) of HK$5 million or less. The Public Offer Shares in pool B will consist of not less than 10,085,000 H Shares and will be allocated on an equitable basis to successful applicants who have applied for Public Offer Shares with an aggregate price (excluding amounts of brokerage, SFC transaction levy and Stock Exchange trading fee) of more than HK$5 million and up to the total value of pool B. You should be aware that applications in pool A and applications in pool B may receive different allocation ratios. If Public Offer Shares in one pool (but not both pools) are undersubscribed, the surplus Public Offer Shares will be transferred to the other pool to satisfy demand in that pool and be allocated accordingly. You can only receive an allocation of Public Offer Shares from either pool A or pool B but not from both pools and may only apply for Public Offer Shares in pool A or pool B. In addition, multiple applications within either pool or between pools will be rejected. No applications will be accepted from applicants applying for more than the total number of Public Offer Shares originally allocated to each pool.

Allocation of Public Offer Shares to investors under the Public Offer will be based solely on the level of valid applications received under the Public Offer when there is over-subscription under the Public Offer. Allocation of Public Offer Shares may involve balloting, which would mean that some applicants may be allotted more Public Offer Shares than others who have applied for the same number of Public Offer Shares, and those applicants which are not successful in the ballot may not receive any Public Offer Shares. Investors which have not received Public Offer may receive H Shares in the International Placing.

SALE H SHARES

The Sale H Shares are being offered for sale under the Public Offer in compliance with the Temporary Administration Measures on the Reduction of State-Owned Shares for the Raising of Social Security Fund (減持國有股籌集社會保障資金管理暫行辦法) (the "**Temporary Administration Measures**") promulgated by the State Council on 12th June, 2001. Pursuant to the Temporary Administration Measures, holders of state-owned shares of a joint stock limited company in the PRC, shall offer for sale its state-owned shares in the amount equivalent to 10% of the funds to be raised under the initial public offering of the joint stock limited company.

Accordingly, an aggregate of 3,700,000 Sale H Shares are offered for sale at the Offer Price. These 3,700,000 Sale H Shares will be converted from the 925,000 Domestic Sale H Shares held by China Southern Airlines and the 2,775,000 Domestic Shares held by Central South Aviation Development. China Southern Airlines and Central South Aviation Development will not own any Shares of the Company after the sale. The Sale H Shares will rank pari passu with the New H Shares in all respects. The net proceeds arising from the sale of the Sale H Shares will be remitted to the National Social Security Fund.

Over-subscription

The allocation of the H Shares between the Public Offer and the International Placing (excluding the Strategic Placing) is subject to adjustment. If the number of H Shares validly applied for under the Public Offer represents 15 times or more but less than 50 times the number of the H Shares initially available under the Public Offer, then 40,340,000 H Shares will be reallocated to the Public Offer from the International Placing (excluding the Strategic Placing), so that an aggregate of 60,510,000 H Shares will be available under the Public Offer, representing 30% of the H Shares initially available under the Offering. If the number of H Shares validly applied for under the Public Offer represents 50 times or more but less than 100 times the number of the H Shares initially available under the Public Offer, then 60,510,000 H Shares will be reallocated to the Public Offer from the International Placing (excluding the Strategic Placing), so that an aggregate of 80,680,000 H Shares will be available under the Public Offer, representing 40% of the H Shares initially available under the Offering. If the number of H Shares validly applied for under the Public Offer represents 100 times or more the number of the H Shares initially available under the Public Offer, then 80,680,000 H Shares will be reallocated to the Public Offer from the International Placing (excluding the Strategic Placing), so that an aggregate of 100,850,000 H Shares will be available under the Public Offer, representing 50% of the H Shares initially available under the Offering.

The allocation of H Shares between the Public Offer and the International Placing (excluding the Strategic Placing) as described above will not affect the Strategic Investor's aggregate shareholding in the Company immediately following completion of the Offering.

Under-subscription

If the Public Offer is not fully subscribed, HSBC will have the discretion to reallocate all or any unsubscribed H Shares originally included in the Public Offer to the International Placing pursuant to the terms of the Underwriting Agreements.

THE INTERNATIONAL PLACING

The Company is initially offering 181,530,000 H Shares, representing 90% of the total number of H Shares initially being offered under the Offering, by way of the International Placing (which includes the Strategic Placing). The Strategic Placing will be underwritten by the Strategic Placing Underwriter only and the International Placing (other than the Strategic Placing) is expected to be fully underwritten by the International Placing Underwriters subject to agreement as to pricing and other terms and conditions of the International Placing Agreement.

Pursuant to the International Placing, it is expected that the International Placing Underwriters or selling agents nominated by the International Placing Underwriters on behalf of the Company will place the International Placing Shares at the Offer Price. Investors subscribing for the International Placing Shares are also required to pay brokerage, SFC transaction levy of 0.007% and Stock Exchange trading fee of 0.005%. International Placing Shares will be placed with professional, institutional and private investors (including the Strategic Investor). Professional investors generally include brokers, dealers and companies (including fund managers) whose ordinary business involves dealing in shares and other securities and entities which regularly invest in shares and other securities.

In Hong Kong, retail investors should apply for the H Shares under the Public Offer, as retail investors applying for International Placing Shares (including applying through banks and other institutions) are unlikely to be allocated any International Placing Shares.

Allocation of the International Placing Shares pursuant to the International Placing will be based on a number of factors, including the level and timing of demand and whether or not it is expected that the relevant investor is likely to buy further H Shares or hold or sell its H Shares, after the listing of the H Shares on the Stock Exchange. Such allocation is generally intended to result in a distribution of the International Placing Shares on a basis which would lead to the establishment of a broad shareholder base for the benefit of the Company and its shareholders taken as a whole. The Company, the Directors and HSBC (on behalf of the International Placing Underwriters) will reject applications in the International Placing from investors who received the H Shares under the Public Offer.

As referred to above, if the Public Offer is not fully subscribed, HSBC may reallocate all or any unsubscribed H Shares originally included in the Public Offer to the International Placing. Any investors which have not received the International Placing Shares may receive H Shares from the Public Offer. The total number of International Placing Shares to be allotted and issued pursuant to the International Placing may change as a result of the clawback arrangement referred to under the paragraph "The Public Offer" above, any exercise of the Over-allotment Option and any reallocation of unsubscribed H Shares originally included in the Public Offer.

THE STRATEGIC PLACING

As part of the International Placing, the Company is offering the Strategic Placing Shares through the Strategic Placing Underwriter to the Strategic Investor pursuant to the Strategic Investment Agreement. The Strategic Placing will be underwritten by the Strategic Placing Underwriter only.

Under the Strategic Investment Agreement, the Strategic Investor will subscribe for the Strategic Placing Shares through the Strategic Placing Underwriter at a price equivalent to the Offer Price plus brokerage, SFC transaction levy, and Stock Exchange trading fee. The other terms and conditions of the Strategic Placing are generally the same as those applicable to the International Placing, except as set forth in this prospectus. The Strategic investor will hold approximately 20% of the enlarged issued share capital of the Company immediately after the completion of the Offering (including any exercise of the Over-allotment Option).

The Strategic Investor has undertaken to the Company, Parent Company and HNA Group that it will not dispose of any of the Strategic Placing Shares for a period of 12 months following the commencement of dealings in the H Shares on the Stock Exchange. It has also undertaken to the Company, Parent Company and HNA Group that: (a) it will not dispose of any of the Strategic Placing Shares for a period of 6 months following the expiry of the 12-month period after the commencement of dealings in the H Shares on the Stock Exchange without the prior written consent of the Company; and (b) in the event of any disposal of any interest in the Strategic Placing Shares: (i) it will take all reasonable steps to ensure that such disposal shall be in accordance with the terms of the Strategic Investment Agreement and will not create a disorderly or false market for any class of shares of the Company; and (ii) it shall not, for so long as Parent Company shall remain as the single largest shareholder of the Company, knowingly dispose of or otherwise transfer any of such interest to any party which carries on or is engaged in carrying on airport services or any party which holds an equity interest in any airports (except where the disposal is made to professional investment funds or financial institutions whose ordinary course of business is investment in securities).

The Strategic Investor has also undertaken not to purchase or subscribe for any additional H Shares so as to increase its shareholding in the Company to more than 25% of the issued share capital of the Company without the prior written consent of the Company.

The Strategic Placing is subject to a number of conditions including:

(a) those conditions set out in "Conditions of the Offering" of this section;

(b) the Strategic Investor having completed its due diligence review on the business, financial position and prospects of the Group to its satisfaction; and

(c) the total subscription price for the Strategic Placing Shares payable by the Strategic Investor not exceeding DKK500 Million (equivalent to approximately RMB550 Million).

WHICH APPLICATION FORM TO USE

Use a **white** application form if you want the H Shares issued in your own name.

Use a **yellow** application form if you want the H Shares issued in the name of HKSCC Nominees Limited and deposited directly into CCASS for credit to your investor participant stock account or your designated CCASS participant's stock account.

Note: The H Shares are not available to existing beneficial owners of Shares, the Directors or Supervisors, or associates (as defined in the Listing Rules) of any of them, a connected person of the Company (unless otherwise allowed by the Stock Exchange) or to legal or natural persons of the PRC or United States persons (as defined in the Regulation S under the US Securities Act).

WHERE TO COLLECT THE APPLICATION FORMS

You can collect a white application form and a prospectus from:

Any participant of The Stock Exchange of Hong Kong Limited

The Hongkong and Shanghai Banking Corporation Limited
Level 15
1 Queen's Road Central
Hong Kong

Oriental Patron Asia Limited
Units 4201–07
COSCO Tower
183 Queen's Road Central
Hong Kong

CITIC Capital Markets Limited
26th Floor, CITIC Tower
1 Tim Mei Avenue
Central
Hong Kong

ICEA Capital Limited
42nd Floor, Jardine House
1 Connaught Place
Central
Hong Kong

ING Bank N.V.
39th Floor, One International Finance Centre
1 Harbour View Street
Central
Hong Kong

Nomura International (Hong Kong) Limited
20th–21st Floor, Asia Pacific Finance Tower
3 Garden Road, Central
Hong Kong

or any of the following branches of **The Hongkong and Shanghai Banking Corporation Limited:**

Hong Kong Island:	**Hong Kong Main Branch**	**Level 3, 1 Queen's Road Central**
	Des Voeux Road Central Branch	**China Insurance Group Building, 141 Des Voeux Road Central**
	Des Voeux Road West Branch	**Western Centre, 40–50 Des Voeux Road West**
	Hay Wah Building Branch	**G/F, Hay Wah Building, 71–85B Hennessy Road, Wanchai**
	North Point Branch	**G/F, Winner House, 306–316 King's Road, North Point**
Kowloon:	**Kwun Tong Branch**	**1 Yue Man Square, Kwun Tong**
	Mongkok Branch	**673 Nathan Road, Mongkok**
	Tsim Sha Tsui Branch	**82–84 Nathan Road, Tsim Sha Tsui**
New Territories:	**Kwai Fong — Day and Night Banking Centre**	**Shop Nos. 218A and 219–220, Level 2, Metroplaza, Kwai Fong**
	Shatin City One Branch	**Shops 138–140, 1st Floor, City One Plaza, Shatin**

You can collect a yellow application form and a prospectus from:

The **Depository Counter of HKSCC** at 2nd Floor, Vicwood Plaza, 199 Des Voeux Road Central, Hong Kong.

The **Customer Service Centre of HKSCC** at Upper Ground Floor, V-Heun Building, 128–140 Queen's Road Central, Hong Kong.

HOW TO COMPLETE THE APPLICATION FORM

There are detailed instructions on each application form. You should read these instructions carefully. If you do not follow the instructions your application may be rejected and returned by ordinary post together with the accompanying cheque or banker's cashier order to you (or the first-named applicant in the case of joint applicants) at your own risk at the address stated in the application form.

You should note that by signing on the application form:

(i) you agree with the Company and each shareholder of the Company, and the Company agrees with each shareholder, to observe and comply with the Company Law, the Special Regulations, and the Articles of Association;

(ii) you agree with the Company, each shareholder of the Company, Director, Supervisor, manager and officer of the Company, and the Company acting for itself and for each Director, Supervisor, manager and officer of the Company agrees with each shareholder of the Company to refer all differences and claims arising from the Articles of Association or any rights or obligations conferred or imposed by the Company Law or other relevant laws and administrative regulations concerning the affairs of the Company to arbitration in accordance with the Articles of Association, and any reference to arbitration shall be deemed to authorise the arbitration tribunal to conduct hearings in open session and to publish its award, which arbitration shall be final and conclusive;

(iii) you agree with the Company and each shareholder of the Company that the H Shares in the Company are freely transferable by the holders thereof; and

(iv) you authorise the Company to enter into a contract on your behalf with each Director and officer of the Company whereby such Directors and officers undertake to observe and comply with their obligations to shareholders as stipulated in the Articles of Association.

If your application is made through a duly authorised attorney, the Company and the Global Coordinator as its agents (or their respective agents or nominees) may accept it at their discretion, and subject to any conditions any of them may think fit, including evidence of the authority of your attorney.

HOW MANY APPLICATIONS MAY YOU MAKE

You may make more than one application for the H Shares only if:

You are a nominee, in which case you may lodge more than one application in your own name on behalf of different owners. In the box on the application form marked "For nominees" you must include:

- an account number; or

- some other identification code

for **each** beneficial owner. If you do not include this information, the application will be treated as being made for your benefit.

Otherwise, multiple applications are not allowed.

All of your applications will be rejected as multiple applications if you, or you and your joint applicant(s) together:

- make more than one application on a **white** or **yellow** application form; or
- apply on one **white** or **yellow** application form for more than 50% of the H Shares initially being offered for public subscription or purchase under the Public Offer.

All of your applications will also be rejected as multiple applications if more than one application is made for **your benefit**. If an application is made by an unlisted company and

- the only business of that company is dealing in securities; and
- you exercise statutory control over that company

then the application will be treated as being for your benefit.

Unlisted company means a company with no equity securities listed on the Stock Exchange.

Statutory control means you:

- control the composition of the board of directors of the company; or
- control more than half of the voting power of the company; or
- hold more than half of the issued share capital of the company (not counting any part of it which carries no right to participate beyond a specified amount in a distribution of either profits or capital).

HOW MUCH ARE THE PUBLIC OFFER SHARES

The maximum Offer Price is HK$3.79 per H Share. You must also pay brokerage of 1%, the SFC transaction levy of 0.007% and the Stock Exchange trading fee of 0.005%. This means that for every 1,000 H Shares you will pay HK$3,828.36. The application forms have tables showing the exact amount payable for certain multiples of H Shares.

You must pay the maximum Offer Price, brokerage, the SFC transaction levy and the Stock Exchange trading fee in full when you apply for the H Shares. You must pay the amount payable upon application for the H Shares by a cheque or a banker's cashier order in accordance with the terms set out in the application form.

If your application is successful, brokerage will be paid to participants of the Stock Exchange, transaction levy will be paid to the SFC, and trading fee will be paid to the Stock Exchange.

If the Offer Price as finally determined is less than HK$3.79 per H Share, or if your application is wholly or partially unsuccessful, appropriate refund payments (including the brokerage, the SFC transaction levy and the Stock Exchange trading fee attributable to the surplus application monies) will be made without interest. Details of the procedure for refund are set out below in the section headed "Despatch/Collection of Share Certificates and Refund Cheques".

MEMBERS OF THE PUBLIC — TIME FOR APPLYING FOR PUBLIC OFFER SHARES

Completed **white** or **yellow** application forms, with payment attached, must be lodged by **12:00 noon on Monday, 11th November, 2002**, or, if the application lists are not open on that day, then by 12:00 noon on the next day the lists are open.

Your completed application form, with payment attached, should be deposited in the special collection boxes provided at any of the branches of The Hongkong and Shanghai Banking Corporation Limited listed on "How to Apply for Public Offer Shares — Where to Collect the Application Forms" at the following times:

Wednesday, 6th November, 2002	—	9:00 a.m. to 4:00 p.m.
Thursday, 7th November, 2002	—	9:00 a.m. to 4:00 p.m.
Friday, 8th November, 2002	—	9:00 a.m. to 4:00 p.m.
Saturday, 9th November, 2002	—	9:00 a.m. to 12:00 noon
Monday, 11th November, 2002	—	9:00 a.m. to 12:00 noon

The application lists will be opened from **11:45 a.m. to 12:00 noon on Monday, 11th November, 2002**.

No proceedings will be taken on applications for the H Shares and no allotment of any such H Shares will be made until the closing of the application lists. No allotment of any of the H Shares will be made later than 5th December, 2002.

EFFECT OF BAD WEATHER ON THE OPENING OF THE APPLICATION LISTS

The application lists will not open if there is:

- a tropical cyclone warning signal number 8 or above, or
- a "black" rainstorm warning

in force in Hong Kong at any time between 9:00 a.m. and 12:00 noon on Monday, 11th November, 2002. Instead they will open between 11:45 a.m. and 12:00 noon on the next business day which does not have either of those warnings in force in Hong Kong at any time between 9:00 a.m. and 12:00 noon.

Business day means a day that is not a Saturday, Sunday or public holiday in Hong Kong.

CIRCUMSTANCES IN WHICH YOU WILL NOT BE ALLOTTED PUBLIC OFFER SHARES

Full details of the circumstances in which you will not be allotted the H Shares are set out in the notes attached to the application forms, and you should read them carefully. You should note in particular the following situations in which the H Shares will not be allotted to you:

If your application is revoked:

By completing and submitting an application form you agree that you cannot revoke your application on or before 5th December, 2002. This agreement will take effect as a collateral contract with the Company, and will become binding when you lodge your application form. This collateral contract will be in consideration of the Company agreeing that it will not offer any H Shares to any person before 5th December, 2002 except by means of one of the procedures referred to in this prospectus.

You may only revoke your application on or before 5th December, 2002 if a person responsible for this prospectus under section 40 of the Companies Ordinance gives a public notice under that section which excludes or limits the responsibility of that person for this prospectus.

If any supplement to the prospectus is issued, applicants who have already submitted an application may or may not (depending on the information contained in the supplement) be notified that they can withdraw their applications. If applicants have not been so notified, or if applicants have been notified but have not withdrawn their applications in accordance with the procedure to be notified, all applications that have been submitted remain valid and may be accepted. Subject to the above, an application once made is irrevocable and applicants shall be deemed to have applied on the basis of the prospectus as supplemented.

If your application has been accepted, it cannot be revoked. For this purpose, acceptance of applications which are not rejected will be constituted by notification in the press of the results of allocation, and where such basis of allocation is subject to certain conditions or provides for allocation by ballot, such acceptance will be subject to the satisfaction of such conditions or results of the ballot respectively.

- **At the discretion of the Company or its agent:**

  The Company and the agents for the Company have full discretion to reject or accept any application, or to accept only part of any application.

  The Company and the Company's agents do not have to give any reason for any rejection or acceptance.

- **If your application is rejected:**

  Your application will be rejected if:

  - you make multiple applications or suspected multiple applications;
  - you or the person for whose benefits you have applied for or taken up or indicated an interest for or received or have been or will be placed or allocated (including conditionally and/or provisionally) International Placing Shares;

- your payment is not made correctly or you pay by cheque or banker's cashier order and the cheque or banker's cashier order is dishonored on its first presentation; or
- your application form is not completed in accordance with the instructions as stated in the application form.

- **If your application is not accepted:**

  Your application will not be accepted if:

  - the Underwriting Agreements do not become unconditional under their terms; or
  - the Underwriting Agreements are terminated in accordance with their respective terms.

- **If the allotment of Public Offer Shares is void:**

Your allotment of Public Offer Shares will be void if the Listing Committee of the Stock Exchange does not grant permission to list the H Shares either:

- within 3 weeks from the closing of the applications lists; or
- within a longer period of up to 6 weeks if the Listing Committee of the Stock Exchange notifies the Company of that longer period within 3 weeks of the closing date of the application lists.

COMMENCEMENT OF DEALINGS IN THE H SHARES

Dealings in the H Shares on the Stock Exchange are expected to commence on 18th November, 2002.

The H Shares will be traded in board lots of 1,000 each.

The Stock Exchange stock code for the H Shares is 357.

H SHARES WILL BE ELIGIBLE FOR ADMISSION INTO CCASS

If the Stock Exchange grants the listing of, and permission to deal in, the H Shares and the Company complies with the stock admission requirements of HKSCC, the H Shares will be accepted as eligible securities by HKSCC for deposit, clearance and settlement in CCASS with effect from the date of commencement of dealings in the H Shares on the Stock Exchange or any other date HKSCC chooses. Settlement of transactions between participants of the Stock Exchange is required to take place in CCASS on the second business day after any trading day.

All activities under CCASS are subject to the General Rules of CCASS and CCASS Operational Procedures in effect from time to time.

All necessary arrangements have been made for the H Shares to be admitted into CCASS.

Investors should seek the advice of their stockbroker or other professional adviser for details of the settlement arrangements as such arrangements will affect their rights and interests.

DESPATCH/COLLECTION OF SHARE CERTIFICATES AND REFUND CHEQUES

If an application is rejected, not accepted or accepted in part only, or if the Offer Price as finally determined is less than HK$3.79 per H Share (excluding brokerage, SFC transaction levy and Stock Exchange trading fee) paid on application, or if the conditions of the Offering are not fulfilled in accordance with the section headed "Structure of the Offering — Conditions of the Offering" or if any application is revoked or any allotment pursuant thereto has become void, the application monies, or the appropriate portion thereof, together with the related brokerage, SFC transaction levy and Stock Exchange trading fee, will be refunded, without interest. It is intended that special efforts will be made to avoid any undue delay in refunding application monies where appropriate.

No temporary document of title will be issued in respect of the H Shares. No receipt will be issued for sums paid on application but, subject as mentioned below, in due course there will be sent to you (or, in the case of joint applicants, to the first-named applicant) by ordinary post, at your own risk, to the address specified on the application form:

(a) (i) share certificate(s) for all the Public Offer Shares applied for, if the application is wholly successful; or (ii) share certificate(s) for the number of Public Offer Shares successfully applied for, if the application is partially successful (except for wholly successful and partially successful applicants on **yellow** application forms whose share certificates will be deposited into CCASS as described below); and/or

(b) a refund cheque crossed "Account Payee Only" in favour of the applicant (or, in the case of joint applicants, the first-named applicant) for (i) the surplus application monies for the Public Offer Shares unsuccessfully applied for, if the application is partially unsuccessful; or (ii) all the application monies, if the application is wholly unsuccessful and/or (iii) the difference between the Offer Price and HK$3.79 per H Share paid on application in the event that the Offer Price is less than HK$3.79 per H Shares paid an application, in each case including brokerage at the rate of 1%, the SFC transaction levy of 0.007% and a Stock Exchange trading fee of 0.005% but without interest.

Deposit of Share Certificates into CCASS

If you apply for Public Offer Shares using a yellow application form and your application is wholly or partially successful, your share certificates will be issued in the name of HKSCC Nominees Limited and deposited into CCASS for credit to your investor participant stock account or the stock account of your designated CCASS participant as instructed by you in your application form at the close of business on 15th November, 2002, or under contingent situation, on any other date as shall be determined by HKSCC or HKSCC Nominees Limited.

If you are applying through a designated CCASS participant (other than a CCASS investor participant):

- for Public Offer Shares credited to the stock account of your designated CCASS participant (other than a CCASS investor participant), you can check the number of Public Offer Shares allotted to you with that CCASS participant.

If you are applying as a CCASS investor participant:

- the Company expects to publish the results of CCASS investor participants' applications together with the results of the Public Offer in the newspapers on 15th November, 2002. You should check the announcement published by the Company and report any discrepancies to HKSCC before 5:00 p.m. on 15th November, 2002 or such other date as shall be determined by HKSCC or HKSCC Nominees Limited. On 16th November, 2002 (the next day following the credit of the Public Offer Shares to your stock account), you can check your new account balance via the CCASS Phone System and CCASS Internet System (under the procedures contained in HKSCC's "An Operating Guide for Investor Participants" in effect from time to time). HKSCC will also mail to you an activity statement showing the number of Public Offer Shares credited to your stock account.

Subject to personal collection as mentioned below, refund cheque for surplus application monies (if any), and share certificate(s) for successful applicants under **white** application forms are expected to be posted on 15th November, 2002. The right is reserved to retain any share certificates and any surplus application monies pending clearance of cheque(s) or banker's cashier order(s).

If you apply for 1,000,000 H Shares or more and have indicated in your application form that you wish to collect refund cheques (where applicable) and share certificates (where applicable) personally, you may collect your refund cheques (where applicable) and share certificates (where applicable) from Computershare Hong Kong Investor Services Limited, the Company's Hong Kong share registrar at Shops 1712–1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong from 9:00 a.m. to 1:00 p.m. on 15th November, 2002 or any other date notified by the Company in the newspaper as the date of despatch of share certificates/refund cheques. If you are an individual who opts for personal collection, you must not authorise any other person to make collection on your behalf. If you are a corporate applicant which opts for personal collection, you must attend by your authorised representative bearing a letter of authorisation from your corporation stamped with your company's chop. Both individuals and authorised representatives must produce, at the time of collection, evidence of identity acceptable to Computershare Hong Kong Investor Services Limited. If you do not collect your refund cheque(s) and share certificate(s), they will be despatched thereafter to you by ordinary post to the address as specified in your application form at your own risk.

If you have applied for less than 1,000,000 H Shares or if you have applied for 1,000,000 H Shares or more but have not indicated in your application form that you wish to collect your share certificate(s) and/or refund cheque(s) personally within the time specified for collection, then your share certificate(s) (if you have applied using a white application form) and/or refund cheque(s) will be sent to the address on your application form on 15th November, 2002 by ordinary post and at your own risk.

The following is the text of report, prepared for the purpose of incorporation in this prospectus, received from Ernst & Young, Certified Public Accountants, Hong Kong, the auditors and reporting accountants of the Company.

ERNST & YOUNG
安永會計師事務所

15th Floor,
Hutchison House
10 Harcourt Road
Central
Hong Kong

6th November, 2002

The Directors
Hainan Meilan Airport Company Limited
The Hongkong and Shanghai Banking Corporation Limited
Oriental Patron Asia Limited

Dear Sirs,

We set out below our report on the financial information regarding Hainan Meilan Airport Company Limited (the "Company") and its subsidiaries (hereinafter collectively referred to as the "Group") for the three years ended 31st December, 1999, 2000 and 2001 and the five months ended 31st May, 2002 (the "Relevant Periods"), for inclusion in the prospectus of the Company dated 6th November, 2002 (the "Prospectus").

The Company was incorporated as a joint stock company with limited liability in the People's Republic of China (the "PRC") on 28th December, 2000, to take over and operate the Meilan Airport in Haikou (the "Meilan Airport") in Hainan, the PRC and certain ancillary commercial businesses (hereinafter collectively referred to as the "Relevant Businesses"). The value of the net assets as at 31st July, 2000 transferred from Haikou Meilan Airport Company Limited (the "Parent Company") to the Company, according to the valuation report dated 8th November, 2000 issued by Hainan Asset Valuation Company, was approximately RMB310,200,000. Prior to the formation of the Company, the Relevant Businesses were conducted by the operating departments and subsidiaries (the "Predecessor Entities") of the Parent Company. During the Relevant Periods, the Company had acquired the equity interests of Haikou Meilan Airport Duty-Free Shop Company Limited ("DFG"), Hainan Haikou Meilan Airport Travelling Company Limited ("Meilan Travelling") and the businesses of carpark operations and cargo handling centre (the "Acquired Businesses") from the Parent Company on 31st May, 2002 for an aggregate consideration of RMB78,131,000 which was based on the valuation report prepared by Hainan Zhong Li Xin Asset Valuation Company Limited dated 18th April, 2002 and was satisfied by an exchange of excessive assets owned by the Company in the amount of RMB28,399,000 and by cash consideration of RMB49,732,000. Upon the completion of the reorganisation activities as set out in the Business section headed "Restructuring of the Group" of the Prospectus (the "Restructuring"), the Company became the holding company of the Group. For the purpose of this report, the acquisition of the Acquired Businesses is accounted for using acquisition accounting.

The principal businesses of the Group are the operation of the Meilan Airport and the provision of related services.

At the date of this report, the Company had direct interests in the following subsidiaries:

Company name	Place and date of incorporation	Paid-up share/ registered capital	Percentage of equity interests attributable to the Group	Principal activities
		RMB'000		
Hainan Haikou Meilan Airport Advertising Company Limited ("Meilan Advertising") *(note (i))*	The PRC 8th June, 1999	1,000	99.75	Provision of advertising services
Meilan Travelling *(note (ii))*	The PRC 13th November, 2001	11,000	60	Provision of tourism services
DFG	The PRC 11th May, 1999	1,000	95	Trading of duty-free items

Notes:

(i) 95% of the equity interest of Meilan Advertising is directly held by the Company while the remaining 4.75% equity interest of Meilan Advertising attributable to the Group is indirectly held by the Company via DFG.

(ii) The registered capital of Meilan Travelling is RMB11,000,000. As at 31st May, 2002, an amount of RMB6,640,000 has been paid up. The remaining balance of RMB4,360,000 was paid up by the Parent Company on 8th September, 2002.

The financial statements of the Company and the Predecessor Entities were prepared in accordance with the accounting principles and financial regulations applicable to the PRC enterprises ("PRC Accounting Regulations").

As at the date of this report, the financial statements of the Company and Meilan Advertising were audited by the following certified public accountants in the PRC:

	Period	Name of the auditors
The Company	For the period ended 31st December, 2000, the year ended 31st December, 2001 and the five months ended 31st May, 2002	Hainan Congxin Certified Public Accountants
Meilan Advertising	For the period ended 31st December, 1999 and for the years ended 31st December, 2000 and 2001	Hainan Huayu Certified Public Accountants

For the purpose of this report, we have undertaken an independent audit of the consolidated financial statements of the Group, including the Predecessor Entities, for each of the Relevant Periods or from their effective dates of incorporation/registration where this is a shorter period, in accordance with Auditing Standards and Guidelines issued by the Hong Kong Society of

Accountants (the "HKSA"), and have carried out such additional procedures as we considered necessary in accordance with the Auditing Guideline "Prospectuses and the Reporting Accountant" issued by the HKSA.

The financial information of the consolidated results, consolidated statements of movements in equity and consolidated cash flows of the Group for the Relevant Periods and the consolidated balance sheets of the Group and the balance sheets of the Company as at 31st December, 1999, 2000 and 2001 and 31st May, 2002 (the "Financial Information") set out in this report have been prepared from the audited financial statements or, where appropriate, unaudited management accounts of the companies now comprising the Group, including the Predecessor Entities, as if the Restructuring had been completed as at the beginning of the periods presented and the business activities had been conducted by the Group throughout the Relevant Periods. The exception to this basis of preparation is the acquisition by the Group during the Relevant Periods of the Acquired Businesses, which is accounted for using acquisition accounting. Adjustments have been made for the purpose of the Prospectus to restate those audited financial statements or, where appropriate, unaudited management accounts to the basis of the accounting policies referred to in Section 2, which are in compliance with International Accounting Standards ("IAS"), and as we considered appropriate, and are presented on the basis set out in Section 1 below.

The directors of the respective companies now comprising the Group are responsible for the underlying financial statements and management accounts on which the Financial Information is based. In preparing the Financial Information, it is fundamental that appropriate accounting policies are selected and applied consistently. It is our responsibility to form an independent opinion on the Financial Information.

In our opinion, the Financial Information together with the notes thereon give, for the purpose of this report, a true and fair view of the consolidated results and cash flows of the Group for each of the Relevant Periods and of the consolidated balance sheets of the Group and the balance sheets of the Company as at 31st December, 1999, 2000 and 2001 and 31st May, 2002.

1. BASIS OF PRESENTATION

As the Parent Company controlled the Predecessor Entities before the Restructuring and continues to control the Group after the Restructuring, the Restructuring has been accounted for as a reorganisation of entities under common control. Accordingly, the Financial Information is presented as if the Restructuring had been completed as at the beginning of the periods presented and the business activities of the Predecessor Entities had been conducted by the Group throughout the Relevant Periods. The assets and liabilities transferred to the Group have been stated at historical amounts. In preparing the Financial Information, those assets, liabilities, revenue and expenses that are identifiable and related to the Predecessor Entities are included in the Financial Information. For those expenses which the specific identification method was not practical, the following allocation bases were adopted in allocating such expenses to the Predecessor Entities prior to the formation of the Company on 28th December, 2000:

	Bases
Other operating cost	Revenue
Salary of administrative staff	Number of employees
Welfare of administrative staff	Number of employees
Property taxes	Respective assets
Other selling and administrative expenses	Number of employees

Prior to the formation of the Company, the Parent Company did not charge the Predecessor Entities for the provision of security guard services, cleaning, lanscaping, power and energy supply and equipment maintenance and leasing of office premises (the "Services") and did not share customary ground services income including aircraft movement fees, passengers charges or ground handling services fees and related charges, because the Parent Company and the Predecessor Entities together comprised a single legal entity. In preparation of the Financial Information, such Services and customary ground services income have been notionally charged to/shared with the Predecessor Entities prior to the formation of the Company on the bases set out in notes 3(g)(i), 3(g)(ii) and 3(g)(ix), respectively.

The management of the Company believes that the above allocation bases are appropriate in estimating the expenses relating to the Predecessor Entities.

2. PRINCIPAL ACCOUNTING POLICIES

The consolidated financial statements have been prepared on a historical cost basis. The principal accounting policies adopted by the Group in arriving at the Financial Information set out in this report which conform with Standards issued by the International Accounting Standards Board (the "IASC") and interpretations issued by its Standing Interpretations Committee are as follows:

(a) Principles of consolidation

The consolidated financial statements comprise the financial statements of the companies now comprising the Group, including the Predecessor Entities, after the elimination of all material intercompany transactions. Subsidiaries are consolidated from the date on which control is transferred to the Group and cease to be consolidated from the date on which control is transferred out of the Group. Minority interests represent the interests in Meilan Advertising, Meilan Travelling and DFG, not held by the Group.

(b) Subsidiaries

A subsidiary is a company, whose financial and operating policies the Company controls directly or indirectly, so as to obtain benefits from its activities. The Company's investments in subsidiaries are stated at cost less any impairment losses.

(c) Property, plant and equipment

Property, plant and equipment are initially stated at cost less accumulated depreciation and any impairment in value. The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to the income statement in the period which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of the property, plant and equipment, the expenditure is capitalised as an additional cost of that asset.

Subsequent to the initial recognition, property, plant and equipment are stated at revaluation less accumulated depreciation and any impairment in value. Independent valuations, on a market value basis or depreciated replacement cost basis when there is no evidence of market value for such an item and will be made with sufficient regularity such that the carrying amount does not differ materially from that which would be determined had the fixed assets been stated at valuation at the balance sheet date. Increases in valuations are credited to the revaluation reserve. Decreases in valuation of property, plant and equipment are first offset against an increase from earlier valuations in respect of the same asset and are thereafter charged to the income statement. Any subsequent increases are credited to the income statement up to the amount previously charged. When property, plant and equipment are sold or retired, their cost or revalued amounts and accumulated depreciation are eliminated from the accounts and any gain or loss resulting from their disposal is included in the consolidated income statements. Except for the revaluation as noted below in connection with the formation of the Company, no revaluation was carried out during the Relevant Periods.

As part of the Restructuring and as required by the relevant PRC regulations, a valuation of the property, plant and equipment of the Company was performed as at 31st July, 2000 by Hainan Assets Valuation Co., a Certified Assets Appraiser registered under the PRC relevant regulations, in order to determine the fair value of such property, plant and equipment for the purpose of establishing the capital contribution from the Parent Company upon the incorporation of the Company. The result of this valuation was considered as an adjustment to the cost of the property, plant and equipment and the surplus/deficit arising thereon were credited/charged to the reserve directly as this is in connection with the change in value of shareholders' contribution.

Depreciation is calculated on the straight-line basis over the estimated useful life of the assets, after taking into consideration the estimated residual value of 3% of cost or revalued amounts, as follows:

Buildings and leasehold improvements	15 – 40 years
Machinery and equipment	10 – 15 years
Office furniture, fixtures and other equipment	6 years
Motor vehicles	10 years

The carrying values of property, plant and equipment are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets or cash-generating units are written down to their recoverable amount. The recoverable amount of property, plant and equipment is the greater of net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognised in the income statements unless the assets are carried at a revalued amount, when the impairment loss is accounted for in accordance with the relevant accounting policy for the revalued assets.

Construction in progress represents a building under construction, which is stated at cost less any impairment losses, and is not depreciated. Cost comprises the direct costs of construction and capitalised borrowing costs on related borrowed funds during the period of construction. Construction in progress is reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

(d) Negative Goodwill

Negative goodwill arising on the acquisition of subsidiaries, represents the excess of the Group's share of the fair values of the identifiable assets and liabilities acquired as at the date of acquisition, over the cost of the acquisition.

To the extent that negative goodwill relates to expectations of future losses and expenses that are identified in the acquisition plan and that can be measured reliably, but which do not represent identifiable liabilities as at the date of acquisition, that portion of negative goodwill is recognised as income in the consolidated profit and loss account when the future losses and expenses are recognised.

To the extent that negative goodwill does not relate to identifiable expected future losses and expenses as at the date of acquisition, negative goodwill is recognised in the consolidated profit and loss account on a systematic basis over the remaining average useful life of the acquired depreciable/amortisable assets. The amount of any negative goodwill in excess of the fair values of the acquired non-monetary assets is recognised as income immediately.

On disposal of subsidiaries, the gain or loss on disposal is calculated by reference to the net assets at the date of disposal, including the attributable amount of negative goodwill which has not been recognised in the consolidated profit and loss account and any relevant reserves as appropriate.

(e) Land use rights

Land use rights are stated at cost, less accumulated amortisation and any impairment in value except for the revaluation as noted below in connection with the formation of the Company, no revaluation was carried out during the Relevant Periods.

As part of the Restructuring and as required by the relevant PRC regulations, a valuation of the land use rights of the Company was performed as at 31st July, 2000 by Hainan Assets Valuation Co., a Certified Assets Appraiser registered under the PRC relevant regulations, in order to determine the fair value of such land use rights for the purpose of establishing the capital contribution from the Parent Company upon the incorporation of the Company. The result of this valuation was considered as an adjustment to the cost of the land use rights and the surplus arising thereon was credited to the reserve directly as this is in connection with the change in value of shareholders' contribution.

The land use rights are amortised on the straight-line basis over the unexpired period of the rights. The carrying values of land use rights are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

(f) Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, i.e., assets that necessarily take a substantial period of time to prepare for their intended use, are capitalised as a part of the cost of those assets. Capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use. The capitalisation rate for the year is based on the actual cost of the related borrowings.

All other borrowing costs are recognised as expenses in the period in which they are incurred.

(g) Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on a weighted average basis and comprises mainly the purchase cost. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs necessary to make the sale.

(h) Revenue recognition

Revenue is recognised when it is probable that economic benefits will flow to the Group and the revenue can be measured reliably on the following bases:

- airport fees, upon receipt from outbound passengers when departing from the airport;
- aeronautical revenues other than airport fees, when the related airport services are rendered;
- rental income, on the straight-line basis during the relevant leasing periods;
- advertising income, on the straight-line basis during the period of display of the relevant advertisements;
- franchise fees, on the straight-line basis during the period of granting the right of operations; and
- interest income, on a time proportion basis taking into account the principal outstanding and the effective interest rate applicable.

(i) Related parties

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence. Related parties may be individuals or corporate entities.

(j) Operating leases

Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Where the Group is the lessor, assets leased by the Group under operating leases are included in property, plant and equipment and rentals receivables under operating leases are credited as income to the income statement on the straight-line basis over the lease terms. Where the Group is the lessee, rentals payable under operating leases are charged as expense to the income statement on the straight-line basis over the lease terms.

(k) Foreign currency transactions

The companies now comprising the Group maintain their books and records in Renminbi ("RMB"). Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated into RMB at the rate of exchange ruling at the balance sheet date. All foreign exchange gains or losses are shown on the income statement.

(l) Tax

PRC corporate income tax is provided at rates applicable to enterprises in the PRC on the Company's income for financial reporting purposes, as adjusted for income and expense items which are not assessable or deductible for income tax purposes.

Deferred income tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences:

(i) except where the deferred income tax liability arises from goodwill amortisation or the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

(ii) in respect of taxable temporary differences associated with investments in subsidiaries, 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.

Deferred tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent it is probable that taxable profit will be available against which the deductible temporary differences, carry-forward of unused tax assets and unused tax losses can be utilised:

(i) except where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

(ii) in respect of deductible temporary differences associated with investments in subsidiaries, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary difference can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax assets to be utilised.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates and tax laws that have been enacted or subsequently enacted at the balance sheet date.

Other tax liabilities are provided in accordance with the regulations issued by PRC government authorities.

(m) Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and in hand and short term deposits with an original maturity of three months or less. For purpose of the consolidated cash flow statements, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts, if any.

(n) Accounts receivable, other receivables and amounts due from related parties

Accounts receivable, which generally have 30–90 day terms, are recognised and carried at the original invoice amount less an allowance for any uncollectible amounts. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off when identified.

Other receivables and amounts due from related parties are recognised and carried at cost less a provision for any doubtful amount.

(o) Accounts payable and other payables

Accounts payable and other payables which are normally settled on 30–90 day terms, are carried at cost which is the fair value of the consideration to be paid in the future for goods and services received, whether or not billed to the Group.

(p) Interest-bearing loans and borrowings

All loans and borrowings are initially recognised at cost, being the fair value of the consideration received net of issue costs associated with the borrowing. After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest rate method. Amortised cost is calculated by taking into account any issue costs, and any discount or premium on settlement. Gains and losses are recognised in net profit or loss when the liabilities are derecognised or impaired, as well as through the amortisation process.

(q) Provisions

A provision is recognised when the Group has a present legal or constructive obligation as a result of a past event and it is probable that a future outflow of resources embodying economic benefits will be required to settle the obligation provided that a reliable estimate can be made of the amount of the obligation.

Where the Group expects a provision to be reimbursed, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as an interest expense.

(r) Retirement benefits

The companies now comprising the Group that are established in the PRC participate in defined contribution retirement plans managed by the local municipal government in the PRC in which they operate. The relevant authorities of the local municipal government in the PRC undertake the retirement obligations of the Group's employees. The Group has no obligation for payment of retirement benefits beyond the annual contributions. The contribution payable is charged as an expense to the income statement as and when incurred.

(s) Impairment of assets

An assessment is made at each balance sheet date of whether there is any indication of impairment of any asset, or whether there is any indication that an impairment loss previously recognised for an asset in prior years may no longer exist or may have decreased. If any such indication exists, the asset's recoverable amount is estimated. An asset's recoverable amount is calculated as the higher of the asset's value in use or its net selling price.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. An impairment loss is charged to the profit and loss account in the period in which it arises, unless the asset is carried at a revalued amount, when the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the recoverable amount of an asset, however not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation), had no impairment loss been recognised for the asset in prior years.

A reversal of an impairment loss is credited to the profit and loss account in the period in which it arises, unless the asset is carried at a revalued amount, when the reversal of the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

(t) Contingencies

Contingent liabilities are not recognised in the financial statements. They are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote.

A contingent asset is not recognised in the financial statements but disclosed when an inflow of economic benefits is probable.

(u) Subsequent events

Post year end events that provide additional information about a company's position at the balance sheet date or those that indicate the going concern assumption is not appropriate, (adjusting events), are reflected in the financial statements. Post year end events that are not adjusting events are disclosed in the notes when material.

(v) Financial instruments

Financial assets and financial liabilities carried in the balance sheet include cash and cash equivalents, accounts receivable and payable, other receivable and payable, loans, and balances with related parties. The accounting policies on recognition and measurement of these items are disclosed in the respective accounting policies found in this section.

Financial instruments are classified as liabilities or equity in accordance with the substance of the contractual arrangement. Interest, dividends, gains, and losses relating to a financial instrument classified as a liability are reported as expenses or income. Distributions to holders of financial instruments classified as equity are charged directly to equity. Financial instruments are offset when the Group has a legally enforceable right to offset and intends to settle either on a net basis or to realise the asset and settle the liability simultaneously.

(w) Dividends

Final dividends proposed by the directors are classified as a separate allocation of retained earnings within capital and reserve in the balance sheets, until they have been approved by the shareholders at general meetings. When these dividends are approved by the shareholders and declared, they are recognised as a liability. Interim dividends are simultaneously proposed and declared, because the Company's memorandum and articles grant the directors authority to declare interim dividends. Consequently, interim dividends are recognised directly as a liability when they are proposed and declared.

3. RESULTS

The following is a summary of the consolidated results of the Group for the Relevant Periods prepared on the basis set out in Section 1 above, and after making such adjustments as are appropriate:

		Year ended 31st December,			Five months ended 31st May,
		1999	2000	2001	2002
	Notes	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
Revenues	*(a)*				
Aeronautical		57,499	119,403	133,037	95,808
Non-aeronautical		22,983	42,240	51,964	22,679
Total revenues		80,482	161,643	185,001	118,487
Business taxes and levies	*(e)*	(2,931)	(5,952)	(6,819)	(4,364)
Net revenues		77,551	155,691	178,182	114,123
Operating costs:					
Cost of goods and services		(6,568)	(13,384)	(13,395)	(4,751)
Depreciation and amortisation		(21,282)	(28,143)	(28,404)	(12,005)
Staff costs		(5,793)	(9,008)	(8,111)	(3,442)
Utilities and power		(4,804)	(7,183)	(7,225)	(2,688)
Repairs and maintenance		(459)	(994)	(2,006)	(355)
Other costs		(359)	(663)	(1,085)	(913)
Total operating costs		(39,265)	(59,375)	(60,226)	(24,154)
Gross profit		38,286	96,316	117,956	89,969
Administrative expenses		(8,388)	(15,157)	(12,892)	(7,451)
Profit from operating activities	*(b)*	29,898	81,159	105,064	82,518
Other income	*4(c)*	—	—	—	2,528
Finance expenses, net	*(d)*	(22,067)	(22,966)	(17,659)	(7,666)
Profit before tax		7,831	58,193	87,405	77,380
Tax	*(e)*	—	—	—	—
Profit after tax		7,831	58,193	87,405	77,380
Minority interests		(94)	(4)	6	(9)
Net profit attributable to shareholders		7,737	58,189	87,411	77,371
Distribution to the Parent Company	*(f)*	—	29,081	—	—
Final dividend	*(h)*	—	—	45,000	—
Earnings per share — basic (RMB)	*(i)*	0.03	0.23	0.35	0.31

Notes:

(a) Revenue

An analysis of revenue is as follows:

	Year ended 31st December,			Five months ended 31st May,
	1999	**2000**	**2001**	**2002**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Aeronautical:				
Passenger charges	41,766	90,371	102,283	50,584
Airport fee — see note 4(g)	—	—	—	29,442
Ground handling services fee	10,091	18,371	20,556	10,644
Aircraft movement fees and related charges	5,642	10,661	10,198	5,138
Total aeronautical revenues	57,499	119,403	133,037	95,808
Non-aeronautical:				
Leasing of commercial areas, counters and office in the Terminal	10,424	22,921	26,261	10,899
Franchise fees	6,592	11,809	15,490	6,597
Advertising fees	3,530	5,087	4,018	2,021
Other revenue	2,437	2,423	6,195	3,162
Total non-aeronautical revenues	22,983	42,240	51,964	22,679
Total revenues	80,482	161,643	185,001	118,487

Notes:

The charge scale for the aeronautical revenue is set out by the Civil Aviation Administration of China (the "CAAC"). The basis of the charge scale for each of the services is as follows:

(i) passenger charges are collected based on a certain percentage of the total maximum passenger capacity of a particular type of aircraft;

(ii) airport fee income represents 50% of the airport fee (excluding any contributions to the Tourism Development Fund) as paid by the passengers;

(iii) ground handling services fees are collected based on the maximum cargo capacity of a particular type of aircraft; and

(iv) aircraft movement fees and related charges are collected based on the maximum take off weight of a particular type of aircraft.

(b) Profit from operating activities

Profit from operating activities is arrived at after charging:

	Year ended 31st December,			Five months ended 31st May,
	1999	**2000**	**2001**	**2002**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Cost of services				
— Composite services fee *(note 3(g)(i))*	4,897	10,263	11,777	4,168
— Environmental protection expenses	764	1,169	1,283	537
— Others	907	1,952	335	46
	6,568	13,384	13,395	4,751
Provision for doubtful accounts	—	—	1,342	522
Staff costs, including directors' emoluments	7,562	12,076	11,232	4,574
Contributions to retirement scheme	806	1,161	728	369
Depreciation and amortisation	21,282	28,143	28,404	12,005
Minimum lease payments under operating leases:				
— Buildings	528	905	905	212
Gross rental income	10,424	22,921	26,261	10,899
Less: Outgoing expenses	—	—	—	—
	10,424	22,921	26,261	10,899
Auditors' remuneration	—	383	262	500

(c) Directors', senior executives' and supervisors' emoluments

Details of the remuneration of the directors and supervisors are as follows:

	Year ended 31st December,			Five months ended 31st May,
	1999	2000	2001	2002
	RMB'000	RMB'000	RMB'000	RMB'000
Fees for executive directors	—	—	—	—
Fees for non-executive directors	—	—	—	—
Fees for supervisors	—	—	—	—
Other emoluments for executive directors				
— basic salaries, housing benefits, other allowances and benefits in kind	107	111	158	66
— bonuses	46	48	68	28
— retirement benefits contributions	15	16	22	9
Other emoluments for non-executive directors	—	—	—	—
Other emoluments for supervisors	—	—	—	—

No directors or supervisors waived or agreed to waive any emolument for the Relevant Periods.

The remuneration of each of the executive directors and supervisors (including the five highest paid employees) for each of the Relevant Periods fell within the range of nil to HK$1,000,000 (equivalent to RMB1,061,000).

The aggregate directors' and supervisors' fees and other emoluments of the Group for the year ending 31st December, 2002 are estimated to be approximately RMB670,000.

The five highest paid individuals in the Group during the Relevant Periods included one director. The emoluments for this director are included in the above disclosures.

The emoluments and designated band of the five highest paid individuals (including directors, supervisors and employees) during the Relevant Periods are as follows:

	Year ended 31st December,			Five months ended 31st May,
	1999	2000	2001	2002
	RMB'000	RMB'000	RMB'000	RMB'000
Basic salaries, housing benefits, other allowances and benefits in kind	157	163	197	83
Bonuses	67	70	84	35
Retirement benefits contributions	27	28	38	16
	251	261	319	134

The remuneration of all executive directors, supervisors and highest paid employees for the Relevant Periods fell within the range of nil to HK$1,000,000 (equivalent to RMB1,061,000).

During the Relevant Periods, no emoluments were paid by the Group to the directors, supervisors or any of the five highest paid individuals as an inducement to join or upon joining the Group or as compensation for loss of office.

(d) Finance expenses, net

	Year ended 31st December,			Five months ended 31st May,
	1999	2000	2001	2002
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Interest on bank loans				
— wholly repayable within five years	18,282	13,124	11,358	4,839
— not wholly repayable within five years	11,926	9,940	6,397	2,853
Less: Amount capitalised	(8,094)	—	—	—
	22,114	23,064	17,755	7,692
Interest income	(47)	(98)	(96)	(26)
Interest expenses, net	22,067	22,966	17,659	7,666

Amounts capitalised are borrowing costs related to funds borrowed specifically for the purpose of obtaining the qualifying assets. The interest rate on such capitalised borrowings was 8.52%.

(e) Tax

Hong Kong profits tax has not been provided as the Group had no assessable profits arising in Hong Kong during the Relevant Periods.

Under PRC income tax law, except for certain preferential treatment available to the Company and its subsidiaries ("tax holiday"), the entities within the Group are subjective to corporate income tax ("CIT") at a rate of 33% on the taxable income as reported in their statutory accounts which are prepared using the accounting principles and financial regulations applicable to PRC enterprises.

In accordance with the regulations of "Tax Benefits on Encouraging Investments" issued by the Hainan Province on 5th August, 1988, each of the Company and the Parent Company is exempt from CIT for a period of five years commencing from its first profitable year and is entitled to a preferential income tax rate of 15% for the remaining years of the operation of Hainan Airport with a 50% reduction for five consecutive years commencing from its sixth profitable year. On 14th June, 2002, documents were received from the local tax bureau by the Parent Company and the Company, respectively, to confirm the entitlement of the captioned tax preferential scheme. The first profitable year of the Company was the year ended 31st December, 2000. The Company therefore was exempt from CIT for 2000, 2001 and 2002.

In accordance with "Tax Benefits on Encouraging Investments" issued by Hainan Province on 5th August, 1988, Meilan Advertising is subject to a preferential income tax rate at 15% and is also entitled to preferential tax treatment for an exemption on CIT for the first profitable year, and a reduction in the enterprise income tax rate to 7.5% for the following year.

The first profitable year of Meilan Advertising was the year ended 31st December, 1999. It therefore was exempt from CIT for 1999 and will be entitled to a reduction in the corporate income tax rate to 7.5% for the following year. Since Meilan Advertising made a loss in 2000 and 2001 and has accumulated losses for the five months ended 31st May, 2002 determined in accordance with the PRC Accounting Regulations, no CIT was provided for.

A reconciliation of income tax expenses applicable to profit from operating activities before income tax at the statutory income tax rate to income tax expenses at the Group's effective income tax rate for each of the Relevant Periods was as follows:

	Year ended 31st December,			Five months ended 31st May,
	1999	**2000**	**2001**	**2002**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Profit from operating activities before income tax	7,831	58,193	87,405	77,380
At PRC corporate income tax rate of 15%	1,175	8,729	13,111	11,607
Expenditure not allowed for deduction	587	3,264	1,019	512
Tax holiday	(1,762)	(11,993)	(14,130)	(12,119)
At effective income tax rate of 0%	—	—	—	—

Except for the unutilised tax losses of Meilan Advertising attributable to the Group as at 31st December, 2000, 2001 and 31st May, 2002 of approximately RMB82,000, RMB301,000 and RMB131,000, respectively, there are no other material deductible temporary differences for which no deferred tax assets are recognised.

The Group is also subject to business taxes on its services revenues at the following rates:

Aeronautical revenues	3% of services revenue
Non-aeronautical revenues	5% of rental income, advertising income and car parking fee income

Except for as disclosed above and in note 4(n), the Group did not have any significant unprovided deferred tax in respect of the Relevant Periods.

(f) Distribution to the Parent Company

Pursuant to a shareholder resolution dated 29th June, 2001, the Company made a distribution to the Parent Company which represented the profit after tax of the Company for the period from 1st August, 2000 to 31st December, 2000. Such profit after tax was determined in accordance with PRC Accounting Regulations.

(g) Related party transactions

In addition to the Restructuring, further details of which are set out in the Business section of the Prospectus and transactions and balances disclosed in notes 4(h), 4(i), 4(k) and 4(m) during the Relevant Periods, the Group had the following material transactions with the following related parties:

Continuing transactions

Name of related parties	Relationship with the Company	Nature of transactions	Notes	Year ended 31st December, 1999	2000	2001	Five months ended 31st May, 2002
				RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
The Parent Company .	Immediate holding company	Airport composite services charged by the Parent Company	*(i)*	4,897	10,263	11,777	4,168
		Rental expense paid for the leasing of office space	*(ii)*	528	905	905	212
		Sharing of customary airport ground services income	*(ix)*	15,803	33,677	37,540	18,470
		Income from franchise fee for the operation of cargo centre	*(vii)*	—	—	8,500	3,542
Hainan Lanyu Air Services Co., Ltd. ("Hainan Lanyu") . .	*Fellow subsidiary	Income from subcontracting for the sales of air tickets	*(iii)*	—	—	639	416
DFG	*Fellow subsidiary	Rental income for the leasing of office space	*(ii)*	158	402	846	367
Meilan Travelling	*Fellow subsidiary	Rental income for the leasing of office space	*(ii)*	—	—	83	275
Hainan Airlines Food Co., Ltd. ("Hainan Food").	Related party	Franchise income from catering services	*(iv)*	1,024	1,700	4,380	1,825
		Rental income for the leasing of storage space	*(iv)*	—	—	25	10
China Southern Airlines Co., Ltd. ("China Southern Airlines") .	*A shareholder	Income for the provision of customary airport ground services	*(v)*	16,805	31,018	39,349	16,889

Name of related parties	Relationship with the Company	Nature of transactions	Notes	Year ended 31st December, 1999 RMB'000	2000 RMB'000	2001 RMB'000	Five months ended 31st May, 2002 RMB'000
		Rental income for the leasing of office and commercial space	*(ii)*	3,675	5,483	5,483	2,285
		Income for the provision of advertising services	*(vi)*	456	437	241	92
Xia Men Airlines Co., Ltd..	Related party	Income for the provision of customary airport ground services	*(v)*	106	444	722	272
HNA Group Co., Ltd. ("HNA Group"). . . .	*A shareholder	Logistic composite services charged by HNA Group	*(viii)*	—	—	—	1,707
Hainan Airlines Co., Ltd. ("Hainan Airlines")	*A shareholder	Income for the provision of customary airport ground services	*(v)*	23,511	48,635	53,821	23,219
		Rental income for the leasing of office and commercial space	*(ii)*	3,116	4,775	5,899	2,415
		Income from franchise fee for the operation of cargo centre	*(vii)*	4,958	8,500	—	—
		Income for the provision of advertising services	*(vi)*	904	659	1,008	354
China Xinhua Airlines Co., Ltd.	Related party	Income for the provision of customary airport ground services	*(v)*	—	409	—	85
Shan Xi Airlines Co., Ltd	Related party	Income for the provision of customary airport ground services	*(v)*	—	—	—	220

* *Fellow subsidiary represents a subsidiary controlled by the Parent Company and a shareholder represents an individual or corporate entity holding the shares of the Company directly.*

(i) *Airport Composite Services*

The Parent Company prior to 28th December, 2000 had provided security guard services, cleaning and landscaping, and power and energy supply and equipment maintenance to the Relevant Businesses and did not charge for such services because the Parent Company and the Relevant Businesses together comprised a single legal entity before the formation of the Company on 28th December, 2000. The Company and the Parent Company entered into an Airport Composite Services Agreement on 31st December, 2000. According to the agreement, the Parent Company continued to provide the above mentioned services to the Company for a fee at 7% of total revenue of the Company with a period of three years. For the purpose of preparing the Financial Information, the Airport Composite Services charges of the Relevant Businesses for 1999 and 2000 were accounted for at 7% of the total revenue of the Relevant Businesses accordingly.

The Company and the Parent Company entered into a new Airport Composite Services Agreement on 25th October, 2002 ("Revised Airport Composite Services Agreement") to replace the agreement dated 31st December, 2000. According to the Revised Airport Composite Services Agreement, the Parent Company has agreed to provide to the Group the following services:

(a) security guard service;

(b) cleaning and landscaping;

(c) sewage and refuse processing;

(d) power and energy supply and equipment maintenance; and

(e) passengers and luggage security inspection.

The charge rates for the above various services are as follows:

- the charges relating to the services of items (a)–(d) above will be determined in accordance with the cost to the Parent Company in providing such services plus a 5% mark-up as management fee, except for item (d), the mark-up of which is 25% pursuant to the relevant pricing guideline sets by the CAAC. The charges are settled on an annual basis.

- the charges relating to the service of item (e) will be determined in accordance with the rate prescribed by the CAAC and charged to the airline customers directly. The Company will collect on behalf of the Parent Company such fees receivable from airline customers.

The term of the Revised Airport Composite Services Agreement is three years commencing from 1st January, 2002 and is renewable upon mutual agreement of the parties thereto.

(ii) *Office Lease Agreement*

The Relevant Businesses prior to 28th December, 2000 had occupied the Parent Company's office premises and the Parent Company did not charge the Relevant Businesses because the Parent Company and the Relevant Businesses together comprised a single legal entity before the formation of the Company on 28th December, 2000. The Company and the Parent Company entered into an Office Lease Agreement dated 31st December, 2000, pursuant to which the Company agreed to lease office premises from the Parent Company for a term of two years at an annual rental of RMB905,000. For the purpose of preparing the Financial Information, the office rental of the Relevant Businesses for 1999 and 2000 was accounted for at RMB905,000 per annum accordingly.

Pursuant to an Office Lease Agreement dated 25th October, 2002 which replaced the previous agreement, the Company agreed to rent from the Parent Company office premises for a term of 5 years at an annual rental of RMB509,000.

The Company or the Predecessor Entities, prior to the formation of the Company, had leased office and commercial areas and premises and airport counters to DFG, Meilan Travelling, HNA Group, Hainan Airlines and China Southern Airlines. The Company or the Predecessor Entities, prior to the formation of the Company, had also leased an aircraft storage warehouse to Hainan Airlines. The relevant lease agreements were made on different dates and on normal commercial terms. The rental charge was agreed between the Company or the Predecessor Entities, prior to the formation of the Company, DFG, Meilan Travelling, HNA Group, Hainan Airlines and China Southern Airlines.

(iii) *Air Ticket Sales Agency*

By way of an Operation Agreement dated 24th April, 2001 between the Company and Hainan Lanyu Air Services Co., Ltd. ("Hainan Lanyu"), a company in which the Parent Company holds a 95% equity interest, the Company contracted its air tickets sales agency business at Meilan Airport to Hainan Lanyu in consideration of a fixed fee in the sum of RMB1,000,000 payable by the latter on an annual basis for a term of two years. On 30th August, 2002, the Company and Hainan Lanyu renewed the agreement for one more year commencing from 1st September, 2002 in consideration of a fixed fee in the sum of RMB800,000 per annum.

(iv) *Catering Service*

During the relevant periods, the Company engaged in the following related catering services arrangements with Hainan Airlines Food Co., Ltd. ("Hainan Food"), a company in which the Parent Company holds a 51% equity interest:

- By a Right of Catering Service Agreement dated 30th April, 1999, the Predecessor Entities have agreed to grant Hainan Food a right to provide on-board catering services to airlines at the Meilan Airport. The franchise fee for the catering right is RMB1,700,000 per year payable on a quarterly basis. On 31st December, 2000, the Company entered into another Catering Service Agreement with Hainan Food for a term of three years whereby the franchise fees were increased to RMB4,380,000 per annum.

- The Company and Hainan Food entered into a Catering Service Agreement on 25th December, 2001, pursuant to which Hainan Food agreed to provide catering services to the passengers of delayed flights staying at the Meilan Airport. The term of the agreement is one year. The charge for such catering services is agreed between the Company and Hainan Food and payable by the Company on a monthly basis.

- In order to prepare for the catering services, Hainan Food has rented from the Company a total floor area of 70 m^2 for storage and preparation of food pursuant to a lease agreement dated 25th May, 2001. The rental is RMB2,100 per month as agreed between the Company and Hainan Food.

(v) *Customary Airport Ground Services*

The Company or the Predecessor Entities, prior to the formation of the Company, provided customary airport ground services including landing facilities, basic ground handling services, cargo storage and handling, passenger and baggage security check services and other related services to Hainan Airlines, China Xinhua Airlines Co. Ltd., a 51%-owned subsidiary of Hainan Airlines, Shan Xi Airlines Co., Ltd, a 89%-owned subsidiary of Hainan Airlines, China Southern Airlines and Xia Men Airlines Co., Ltd., a 60%-owned subsidiary of China Southern Airlines, at rates prescribed by the CAAC throughout the Relevant Periods.

(vi) *Advertising Services*

Meilan Advertising, a of the Company, provided advertising services to HNA Group and China Southern Airlines at normal rates charged to other clients.

(vii) *Franchise fee income*

The Relevant Businesses have franchised the operation of the cargo centre to Hainan Airlines, for a fixed annual franchise fee of RMB8,500,000 from March 1999 to 31st December, 2000. The Company entered into a new contract with the Parent Company, for the operation of the cargo centre of the Company for a fixed annual franchise fee of RMB8,500,000 effective from 1st January, 2001.

(viii) *Logistic Composite Service*

HNA Group, pursuant to a Logistic Composite Service Agreement effective from 1st January, 2002, agreed to provide and procure its subsidiaries to provide to the Company logistic services including (a) staff training; (b) staff shuttle bus services; (c) staff cafeteria service; (d) vehicle maintenance; and (e) appliance procurement. Charges as to the service of item (a) are the cost for providing such services shared between HNA Group, the Company and other relevant companies on a pro rata basis by reference to employee headcounts; as to items (b) and (c) are at a fixed price with reference to relevant cost per employee headcount; and as to items (d) and (e) are the cost for providing such services plus a 5% and a 1% mark-up as management fees, respectively.

(ix) *Sharing of Customary Ground Services Income*

The runway at the Meilan Airport is owned and operated by the Parent Company. By an agreement between the Company and the Parent Company, the Company has agreed to share with the Parent Company on such ratio as CAAC or any other regulatory authorities may from time to time prescribe, which as the date of the agreement in the ratio of 75% to the Company and 25% to the Parent Company for the aircraft movement fees for all airlines, passenger charges for domestic airlines and the basic fee of ground handling fees for Hong Kong, Macau and foreign airlines. The Company will collect such fees on behalf of the Parent Company and assume no liabilities in respect of default of payment by the airline customers. For the purpose of preparing the Financial Information, the customary ground services income of the Relevant Businesses for 1999 and 2000 was shared with the Parent Company in the ratio of 75% to the Company and 25% to the Parent Company the aircraft movement fees for all airlines, passengers charges for domestic airlines and the basic fee of ground handling fees for Hong Kong, Macau and foreign airlines prescribed by CAAC of the Relevant Businesses accordingly.

In the opinion of the directors, the above transactions were conducted in the ordinary course of business and will be continued after the listing of the shares of the Company on The Stock Exchange of Hong Kong Limited.

Discontinuing transactions

(i) The Company received RMB604,000 from Chang An Airlines Co., Ltd. for the provision of customary airport ground services in 2001.

(ii) The Company received RMB844,000 and RMB372,000 from HNA Group, for leasing of a commercial area in 2001 and for the five months ended 31st May, 2002, respectively. The rental of the commercial area was agreed between the Company and HNA Group.

(iii) During the Relevant Periods, an advance of approximately RMB20,000,000 was granted to Hainan Da Long Investment Co., Ltd., a related party, in 2001. The advances was interest free, unsecured with no fixed terms of repayment and was repaid during the five months ended 31st May, 2002.

(iv) Effective 31st May, 2002, 95% and 60% of the equity interests of DFG and Meilan Travelling, respectively, were acquired by the Company. DFG and Meilan Travelling accordingly became subsidiaries of the Company and the transactions among the Company, DFG and Meilan Travelling are eliminated in the consolidated results of the Group effective 1st June, 2002.

The directors are of the opinion that such transactions will not be continued after the listing of the shares of the Company on The Stock Exchange of Hong Kong Limited.

(h) Dividends

	Year ended 31st December,			Five months ended 31st May,
	1999	2000	2001	2002
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Proposed final 18 cents (2000: Nil; 1999: Nil) . . .	—	—	45,000	—

Final dividend of RMB45,000,000 was declared for the year ended 31st December, 2001 by the shareholders of the Company on 19th July, 2002.

(i) Earnings per share

The calculation of earnings per share is based on the Group's profit attributable to shareholders for each of the three years ended 31st December, 2001 and for the five months ended 31st May, 2002, and 250,000,000 shares were deemed to have been in issue and issuable during the Relevant Periods.

(j) Pension scheme

The companies now comprising the Group are required to participate in employee pension schemes operated by the relevant local government authorities in the PRC. The PRC government is responsible for the pension liability to these retired employees. The Group is required to make contributions for employees who are registered as permanent residents in the PRC at a rate of 14% of the employees salaries in 1999 and 2000. The pension contribution rate increased to 16% in 2001.

The Group's contribution to pension costs for each of the Relevant Periods amounted to approximately RMB806,000, RMB1,161,000, RMB728,000 and RMB369,000, respectively.

4. CONSOLIDATED BALANCE SHEET

Set out below is a summary of the consolidated balance sheets of the Group and the balance sheets of the Company as at the end of each of the periods prepared on the basis set out in Section 1 above and after making such adjustments as are appropriate:

The Group

		31st December,			31st May,
		1999	2000	2001	2002
	Notes	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
ASSETS					
Non-current assets					
Property, plant and equipment, net	*(a)*	692,435	658,502	641,388	652,378
Land use rights	*(b)*	8,143	56,566	55,673	75,996
Negative goodwill	*(c)*	—	—	—	(260)
		700,578	715,068	697,061	728,114
Current assets					
Cash and cash equivalents	*(d)*	34,312	16,634	32,748	64,972
Accounts receivable, net	*(e)*	4,183	12,912	19,193	27,697
Inventories	*(f)*	115	116	13	2,641
Airport fee receivable	*(g)*	—	—	—	29,442
Prepayments, deposits and other receivables		121	64	1,237	2,765
Due from related parties	*(h)*	22,951	10,622	46,322	32,577
		61,682	40,348	99,513	160,094
TOTAL ASSETS		762,260	755,416	796,574	888,208
EQUITY AND LIABILITIES					
Shareholders' equity					
Capital and reserves	*5*	246,725	319,390	361,801	439,172
Final dividend	*3(h)*	—	—	45,000	45,000
		246,725	319,390	406,801	484,172
Minority interests		144	148	142	1,888
Non-current liabilities					
Long term bank loan	*(m)*	285,000	276,000	264,000	257,000
Deferred income tax liabilities	*(n)*	—	6,535	6,535	6,535
		285,000	282,535	270,535	263,535
Current liabilities					
Short term bank loan	*(i)*	—	—	20,000	20,000
Current portion of long term bank loan	*(m)*	95,000	9,000	12,000	13,000
Accounts payable	*(j)*	—	—	—	1,260
Accrued liabilities and other payables		7,242	5,807	9,587	19,811
Construction payables	*(k)*	71,468	—	—	—
Airport fee payable	*(l)*	—	—	—	59,141
Deposits received		2,095	1,820	2,696	2,773
Due to related parties	*(h)*	54,586	136,716	74,813	22,628
		230,391	153,343	119,096	138,613
TOTAL ASSETS LESS CURRENT LIABILITIES		531,869	602,073	677,478	749,595
TOTAL EQUITY AND LIABILITIES		762,260	755,416	796,574	888,208

The Company

		31st December,			31st May,
		1999	2000	2001	2002
	Notes	RMB'000	RMB'000	RMB'000	RMB'000
ASSETS					
Non-current assets					
Property, plant and equipment, net	(a)	689,748	655,892	639,181	650,130
Land use rights	(b)	8,143	56,566	55,673	75,996
Interests in subsidiaries	(c)	950	950	1,196	6,791
		698,841	713,408	696,050	732,917
Current assets					
Cash and cash equivalents	(d)	32,952	16,326	32,392	58,258
Accounts receivable, net		4,178	12,409	19,042	27,464
Inventories	(f)	115	116	13	24
Airport fee receivable	(g)	—	—	—	29,442
Prepayments, deposits and other receivables		81	53	1,231	2,479
Due from related parties	(h)	22,951	10,554	47,328	33,183
		60,277	39,458	100,006	150,850
TOTAL ASSETS		759,118	752,866	796,056	883,767
EQUITY AND LIABILITIES					
Shareholders' equity					
Capital and reserves		246,628	319,390	361,907	436,588
Final dividend	3(h)	—	—	45,000	45,000
		246,628	319,390	406,907	481,588
Non-current liability					
Long term bank loan	(m)	285,000	276,000	264,000	257,000
Deferred income tax liabilities	(n)	—	6,535	6,535	6,535
		285,000	282,535	270,535	263,535
Current liabilities					
Short term bank loan	(i)	—	—	20,000	20,000
Current portion of long term bank loan	(m)	95,000	9,000	12,000	13,000
Accrued liabilities and other payables		7,107	5,653	9,319	17,199
Construction payables	(k)	71,468	—	—	—
Airport fee payable	(l)	—	—	—	59,141
Deposits received		889	897	1,916	1,923
Due to related parties	(h)	53,026	135,391	75,379	27,381
		227,490	150,941	118,614	138,644
TOTAL ASSETS LESS CURRENT LIABILITIES		531,628	601,925	677,442	745,123
TOTAL EQUITY AND LIABILITIES		759,118	752,866	796,056	883,767

Notes:

(a) Property, plant and equipment, net

The Group

	As at 31st December, 1999		
	Cost	Accumulated depreciation	Net book value
	RMB'000	*RMB'000*	*RMB'000*
Buildings and leasehold improvements	560,181	12,320	547,861
Machinery and equipment	112,798	5,820	106,978
Motor vehicles	32,551	5,492	27,059
Furniture and office equipment	8,602	915	7,687
Assets under construction	2,850	—	2,850
	716,982	24,547	692,435

	As at 31st December, 2000		
	Cost	Accumulated depreciation	Net book value
	RMB'000	*RMB'000*	*RMB'000*
Buildings and leasehold improvements	578,705	51,739	526,966
Machinery and equipment	109,325	16,277	93,048
Motor vehicles	34,007	7,694	26,313
Furniture and office equipment	14,469	2,892	11,577
Assets under construction	598	—	598
	737,104	78,602	658,502

	As at 31st December, 2001		
	Cost	Accumulated depreciation	Net book value
	RMB'000	*RMB'000*	*RMB'000*
Buildings and leasehold improvements	579,126	65,778	513,348
Machinery and equipment	110,311	23,805	86,506
Motor vehicles	42,388	11,574	30,814
Furniture and office equipment	15,676	4,956	10,720
	747,501	106,113	641,388

	As at 31st May, 2002		
	Cost	Accumulated depreciation	Net book value
	RMB'000	*RMB'000*	*RMB'000*
Buildings and leasehold improvements	599,975	69,204	530,771
Machinery and equipment	98,404	22,993	75,411
Motor vehicles	48,335	13,300	35,035
Furniture and office equipment	17,099	5,938	11,161
	763,813	111,435	652,378

The Company

	As at 31st December, 1999		
	Cost	Accumulated depreciation	Net book value
	RMB'000	*RMB'000*	*RMB'000*
Buildings and leasehold improvements	560,181	12,320	547,861
Machinery and equipment	112,798	5,821	106,977
Motor vehicles	32,391	5,482	26,909
Furniture and office equipment	5,954	803	5,151
Assets under construction	2,850	—	2,850
	714,174	24,426	689,748

	As at 31st December, 2000		
	Cost	Accumulated depreciation	Net book value
	RMB'000	*RMB'000*	*RMB'000*
Buildings and leasehold improvements	578,705	51,739	526,966
Machinery and equipment	109,325	16,277	93,048
Motor vehicles	33,846	7,668	26,178
Furniture and office equipment	12,028	2,328	9,700
	733,904	78,012	655,892

	As at 31st December, 2001		
	Cost	Accumulated depreciation	Net book value
	RMB'000	*RMB'000*	*RMB'000*
Buildings and leasehold improvements	579,126	65,778	513,348
Machinery and equipment	110,311	23,805	86,506
Motor vehicles	41,998	11,515	30,483
Furniture and office equipment	12,758	3,914	8,844
	744,193	105,012	639,181

	As at 31st May, 2002		
	Cost	Accumulated depreciation	Net book value
	RMB'000	*RMB'000*	*RMB'000*
Buildings and leasehold improvements	599,975	69,204	530,771
Machinery and equipment	98,404	22,994	75,410
Motor vehicles	47,994	13,212	34,782
Furniture and office equipment	13,778	4,611	9,167
	760,151	110,021	650,130

As part of the Restructuring and as required by the relevant PRC regulations, a valuation of the property, plant and equipment of the Company was performed as at 31st July, 2000 by Hainan Assets Valuation Co., a Certified Assets Appraiser registered under the relevant PRC regulations, in order to determine the fair value of such property, plant and equipment for the purpose of establishing the capital contribution from the Parent Company. The valuation was based on the replacement cost method and was accounted for as an adjustment to cost in respect of assets contributed by the Parent Company upon incorporation of the Company. Any surplus or deficit arising thereon was thus reflected as a movement under equity.

The revaluation identified certain property, plant and equipment with net carrying value in excess of the appraised value of RMB15,103,000 which was charged to the equity account.

All buildings of the Group are held outside Hong Kong with lease terms of 50 years.

(b) Land use rights

The Group and the Company

	As at 31st December, 1999		
	Cost	Accumulated amortisation	Net book value
	RMB'000	*RMB'000*	*RMB'000*
Land use rights	8,860	717	8,143

	As at 31st December, 2000		
	Cost	Accumulated amortisation	Net book value
	RMB'000	*RMB'000*	*RMB'000*
Land use rights	57,730	1,164	56,566

	As at 31st December, 2001		
	Cost	Accumulated amortisation	Net book value
	RMB'000	*RMB'000*	*RMB'000*
Land use rights	57,730	2,057	55,673

	As at 31st May, 2002		
	Cost	Accumulated amortisation	Net book value
	RMB'000	*RMB'000*	*RMB'000*
Land use rights	78,425	2,429	75,996

Prior to the formation of the Company, substantially all of the buildings of the Predecessor Entities were constructed on land located in the PRC, the land use rights for which were acquired from the PRC Government at RMB8,860,000 by the Parent Company.

As part of the Restructuring and as required by the relevant PRC regulations, a valuation of the land use rights of Relevant Businesses was carried out as at 31st July, 2000 by Hainan Assets Valuation Co., a Certified Assets Appraiser registered under the relevant PRC regulations. The valuation was performed in order to determine the fair value of such land use rights for the purpose of establishing the capital contribution from the Parent Company. The valuation was based on a market value basis. The valuation valued the land use rights of the Predecessor Entities at an amount of RMB56,938,000, which was RMB48,869,000 in excess of the prior carrying value of the land use rights as at 31st July, 2000. The change in value was accounted for as an adjustment to cost in respect of assets contributed by the Parent Company and was reflected as a movement under equity. Amortisation on the increment to the related land use rights commenced on 31st July, 2000.

The land use rights are amortised on the straight-line basis over the term of 50 years.

Land use rights with a net book value of RMB50,000,000 as at 31st May, 2002 was pledged for a long term loan granted by China Development Bank as described in note 4(m).

(c) Interests in subsidiaries

Details of the interests in subsidiaries of the Company as at 31st December are set out below:

	As at 31st December,			As at 31st May,
	1999	**2000**	**2001**	**2002**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Unlisted share, at cost	950	950	950	8,294
Amount due from/(to) subsidiaries	—	—	246	(1,503)
	950	950	1,196	6,791

Amounts due from/(to) subsidiaries are unsecured, non-interest bearing and payable on demand.

Effective 31st May, 2002, the Group acquired a 95% equity interest and a 60% equity interest of DFG and Meilan Travelling, respectively. The purchase consideration for the acquisition was in the form of cash, with approximately RMB7,344,000 being payable within 12 months of the acquisition date. The amount was still unsettled at the date of this report.

The fair values of the identifiable assets and liabilities acquired of DFG and Meilan Travelling were:

	RMB'000
Property, plant and equipment	260
Cash and cash equivalents	6,534
Prepayments, deposits and other receivables	9,997
Accounts receivable	82
Inventories	2,618
*Investment cost	151
	19,642
Accounts payable	(1,260)
Accrued liabilities and other payables	(6,363)
Minority interests	(1,887)
Fair value of net assets	10,132
Negative goodwill arising on acquisition	(2,788)
	7,344
Consideration:	
To be settled in cash and included in liabilities on 31st May, 2002	7,344
Cash inflow on acquisition is as follows:	
Amount of cash paid as at 31st May, 2002	—
Net cash acquired (before settlement of purchase cost)	6,534
Net cash inflow	6,534

* *The balance represents the 5% equity interests of Meilan Advertising held by DFG. The investment cost will be eliminated upon the consolidation of the financial statements of the Group.*

Negative goodwill represented the excess of the fair values of the acquired non-monetary assets over the cost of acquisition. The amount of negative goodwill not exceeding the fair values of acquired identifiable non-monetary assets, amounting to approximately RMB260,000 will be amortised as income on a systematic basis over the remaining weighted average useful life of approximately seven years of the identifiable acquired depreciable assets while the amount of negative goodwill in excess of the fair values of acquired identifiable non-monetary assets amounting to approximately RMB2,528,000 is recognised as income immediately.

From the date of acquisition, DFG and Meilan Travelling have made no contribution to the net profit of the Group.

(d) Cash and cash equivalents

Cash and cash equivalents comprise cash at banks and in hand. Cash at banks earns interest at floating rates based on daily bank deposit rates.

(e) Accounts receivable, net

An aged analysis of the accounts receivable of the Group is analysed as follows:

The Group

	As at 31st December,			As at 31st May,
	1999	**2000**	**2001**	**2002**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Outstanding balances aged:				
Within 90 days	3,271	12,158	18,042	17,817
Between 91 to 180 days	462	754	1,157	6,881
Between 181 to 365 days	450	—	1,336	4,863
	4,183	12,912	20,535	29,561
Less: Provision for doubtful debts	—	—	(1,342)	(1,864)
	4,183	12,912	19,193	27,697

The Group normally allows a credit period of not more than 90 days to its customers, although an extension of the credit period is not uncommon for customers with a long term relationship. The Group closely monitors overdue balances. A provision for doubtful debts is made when it is considered that amounts due may not be recovered.

(f) Inventories

The Group

	As at 31st December,			As at 31st May,
	1999	**2000**	**2001**	**2002**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Finished goods and low value consumables	115	116	13	2,641

The Company

	As at 31st December,			As at 31st May,
	1999	2000	2001	2002
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Low value consumables	115	116	13	24

All the carrying amounts were stated at cost.

(g) Airport fee receivable

Pursuant to an approval document from the Ministry of Finance on 25th September, 2002, 50% of the Airport fee collected by the Company will be granted to the Company as revenue and subject to business tax, related levies and corporate income tax effective on 1st January, 2002. The balance represented the outstanding Airport fee refundable from Hainan Province as at 31st May, 2002. Had the approval been obtained and effective at the beginning of the Relevant Periods, the Airport fee less relevant business tax, related levies and corporate income tax for the three years ended 31st December, 1999, 2000 and 2001 would have been RMB21,893,000, RMB43,877,000, and RMB50,304,000, respectively. On 11th September, 2002, an approval was obtained from CAAC that with effect from 1st January, 2002, Airport fee receivable could be off-set against the amount of the Airport fee payable to CAAC (see note 4(l)).

(h) Balance with related parties

The Group

	As at 31st December,			As at 31st May,
	1999	2000	2001	2002
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Due from:				
HNA Group	—	68	955	—
Hainan Airlines Co., Ltd.*	17,819	—	—	1,378
Southern Airlines (Group)	1,183	886	611	482
China Southern Airlines Co., Ltd.*	3,949	9,428	19,903	22,951
Hainan Da Long Investment Co., Ltd.	—	—	20,000	—
Hainan Airlines Food Co., Ltd.	—	—	4,086	5,832
Hainan Tong Hui Insurance Agent Co., Ltd.	—	176	155	800
Others	—	64	612	1,134
	22,951	10,622	46,322	32,577
Due to:				
HNA Group	167	—	—	184
The Parent Company	54,419	136,716	74,813	22,444
	54,586	136,716	74,813	22,628

The Company

	As at 31st December,			As at 31st May,
	1999	**2000**	**2001**	**2002**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Due from:				
HNA Group	—	—	645	—
Hainan Airlines Co., Ltd.*	17,819	—	—	1,378
Southern Airlines (Group)	1,183	886	611	482
China Southern Airlines Co., Ltd.*	3,949	9,428	19,903	22,951
Hainan Da Long Investment Co., Ltd.	—	—	20,000	—
Hainan Airlines Food Co., Ltd.	—	—	4,086	5,832
Hainan Tong Hui Insurance Agent Co., Ltd.	—	176	155	800
Hainan Lanyu Air Services Co., Ltd.	—	—	639	960
China Xinhua Airlines Co., Ltd.	—	—	618	84
Others	—	64	671	696
	22,951	10,554	47,328	33,183
Due to:				
HNA Group	—	—	—	710
The Parent Company	53,026	135,391	75,379	26,671
	53,026	135,391	75,379	27,381

* The balance represented accounts receivable arising from aeronautical services provided by the Company

Amounts due from/to related parties are unsecured, non-interest bearing and payable on demand. The balances primarily arose from related party transactions as shown in note 3(g), above.

(i) Short term bank loan

As at December 2001, the Group and the Company had a short term bank loan granted by China Development Bank amounting to RMB20,000,000 (2000: Nil; 1999: Nil). The loan bears interest at 5.85% (2000: Nil; 1999: Nil) per annum and is unsecured. The loan is guaranteed by HNA Group and has a maturity date of 28th December, 2002. The Company obtained the consent of China Development Bank on 4th November, 2002 to release the guarantee.

(j) Accounts payables

An aged analysis of the accounts payable is analysed as follows:

The Group

	As at 31st December,			As at 31st May,
	1999	**2000**	**2001**	**2002**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Outstanding balances aged:				
Within 90 days	—	—	—	1,260
Over 90 days	—	—	—	—
	—	—	—	1,260

(k) Construction payables

This amount represented retention money payable to the contractors of the Group and the Company for the construction of the airport passenger terminal. As part of the group reorganisation, the amount was subsequently taken up by the Parent Company in 2000 upon formation of the Company.

(l) Airport fee payable

In accordance with the notice issued by the CAAC, from 1st January, 2002 the Company is required to collect on behalf of the CAAC a civil airport management and construction fee (the "Airport fee"), subject to certain exemptions, from each outbound passenger (RMB50 per domestic passenger and RMB70 per international passenger). In addition, the Tourism Development Fund (RMB20 per passenger) is also collected together with the Airport fee from each outbound international passenger on behalf of and payable to the PRC government after deducting certain handling charges.

With reference to note 4(g), an approval from the CAAC has been obtained on 11th September, 2002 that, effective 1st January, 2002, the Airport fee refund could be off-set against the Airport fee payable. In connection with the outstanding amount of approximately RMB59,141,000 as at 31st May, 2002, an amount of RMB29,000,000 was paid subsequent to 31st May, 2002 and the remaining balance, based on the relevant approval from CAAC, was set-off against Airport fee receivable.

(m) Interest bearing loans and borrowings

The repayment schedule of the long term bank loan is as follows:

The Group and the Company

	As at 31st December,			As at 31st May,
	1999	**2000**	**2001**	**2002**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Within one year	95,000	9,000	12,000	13,000
Between one and two years	9,000	12,000	14,000	7,000
Between two and five years	126,000	139,000	150,000	150,000
Over five years	150,000	125,000	100,000	100,000
Total long term bank loan	380,000	285,000	276,000	270,000
Less: Amounts due within one year included in current liabilities	95,000	9,000	12,000	13,000
	285,000	276,000	264,000	257,000

The loan of RMB380,000,000 as at 31st December, 1999 was borrowed from China Development Bank for construction of the Meilan Airport. As part of the Restructuring, the Company and the Parent Company agreed to assign the unpaid balance of the loan of RMB285,000,000 from the Parent Company to the Company upon the incorporation of the Company. The loan was pledged by the land use rights of the Parent Company amounting to RMB357,000,000 and the land use rights of the Company amounting to approximately RMB50,000,000. The Company obtained the consent of China Development Bank on 4th November, 2002 to release the bank's security over the land use rights pledged by the Parent Company. The weighted average interest rate of the loan was 7.96%, 6.57%, 6.25% and 6.17% for 1999, 2000 and 2001 and the five months ended 31st May, 2002, respectively. The security provided by the Parent Company for the banking facilities will be discontinued upon the expiry date of the banking facilities. The Parent Company has not charged and will not charge any fees in relation to the provision of such security, and no counter guarantees, indemnities or security were given by the Company to the Parent Company. As at the formation of the Company, the total amount of the bank loan was RMB285,000,000.

(n) Deferred income tax liabilities

For the year ended 31st December, 2000, the Group and the Company recognised a deferred tax liability arising from the cost adjustment related to the revaluation with the appraised value in excess of the net carrying value on the land use rights of the Relevant Businesses pursuant to the Restructuring in 2000. The valuation of the land use rights was performed by Hainan Asset Valuation Co., with a non-tax deductible surplus of approximately RMB48,869,000. The Company has a five-year exemption of CIT from 2000 to 2004 and a preferential income tax rate of 7.5% from 2005 to 2009. The deferred tax liabilities of RMB6,535,000 relating to this temporary difference was recorded in 2000, after taking into account the impact of the tax preferential scheme, with a corresponding adjustment to the share premium that had been recorded to reflect the cost adjustment in respect of assets contributed by the Parent Company.

(o) Operating lease arrangement

As lessee

At 31st May, 2002, the total future minimum lease payments under non-cancellable operating leases in respect of buildings and motor vehicles are as follows:

The Group and the Company

	As at 31st May, 2002
	RMB'000
Within one year	1,185
In the second to fifth years, inclusive	212
After five years	—
	1,397

As lessor

At 31st May, 2002, the total future minimum lease receivables under non-cancellable operating leases with its tenants falling due are as follows:

	The Group As at 31st May, 2002	The Company As at 31st May, 2002
	RMB'000	*RMB'000*
Within one year	10,450	7,719
In the second to fifth years, inclusive	16,540	15,001
After five years	5,943	5,943
	32,933	28,663

(p) Segment information

The Group conducts its business within one business segment i.e., the business of operating an airport and provision of related services in the PRC. The Group's chief decision maker for operations is considered to be the Group's general manager. The information reviewed by the general manager is prepared on a similar basis to the information presented in the consolidated income statements. No segment consolidated income statements have been prepared by the Group during the Relevant Periods. The Group also operates within one geographical segment because its revenues are primarily generated in the PRC and its assets are located in the PRC. Accordingly, no geographical segment data is presented.

(q) Contingent liabilities

As at 31st May, 2002, the Group and the Company did not have any significant contingent liabilities.

(r) Commitments

As at 31st May, 2002, the capital commitments of the Group and the Company authorised but not contracted for were as follows:

The Group and the Company

	RMB'000
Land use rights	94,380
Construction for a customs and immigration building for international passengers	13,000
	107,380

(s) Fair values of financial instruments

As at 31st May, 2002, the Group's financial instruments mainly consisted of cash and bank balances, accounts receivable, due from and due to related parties, other current assets, accounts payable, other payables, short term borrowing and long term borrowing.

The carrying amounts of the Group's financial instruments approximated their fair value as at 31st May, 2002 because of the short term maturities of these instruments except for long term borrowing.

The carrying amount of long-term borrowing approximated its fair value based on borrowing rates currently for loans with similar terms and maturities.

(t) Concentration of risk

(i) *Business risk*

The Group conducts its operations in the PRC and accordingly is subject to special considerations and significant risk. These include risks associated with, among others, the political, economic and legal environment, influence of national authorities over pricing regulations and competition in the industry.

Further, the five largest customers represented in aggregate approximately 78%, 68%, 64% and 45% of the aeronautical revenues of the Group for the year ended 31st December, 1999, 2000 and 2001 and the five months ended 31st May, 2002, respectively.

(ii) *Interest rate risk*

The interest rate terms of repayment of the bank loan of the Group are disclosed in notes 4(i) and 4(m).

(iii) *Foreign currency risk*

The Group's businesses are principally conducted in RMB, except for the purchase of certain equipment, goods and materials in US dollars. As at 31st May, 2002, all of the Group's assets and liabilities were denominated in RMB except that cash and cash equivalents of approximately RMB24,000 were denominated in US dollars. Fluctuation of the exchange rates of RMB against foreign currencies could affect the Group's results of operations.

(iv) *Credit risk*

The Group's cash and cash equivalents are mainly deposited with major PRC banks.

The carrying amounts of trade debtors included in the consolidated financial statements represent the Group's maximum exposure to credit risk in relation to its financial assets. No other financial assets carry a significant exposure to credit risk. The Group has no significant concentration of credit risk.

5. STATEMENT OF MOVEMENTS IN EQUITY

The movements in the consolidated shareholders' equity of the Group for the Relevant Periods, prepared on the basis set out in Section 1 above, are as follows:

The Group

	Notes	Share capital	Paid in capital	Share premium account	Statutory reserves	Unappropriated profit	Total
		RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
		(i)	(iii)		(ii)		
Beginning of 1999		—	217,095	—	—	—	217,095
Contribution from the Parent Company		—	21,893	—	—	—	21,893
Net profit		—	—	—	—	7,737	7,737
End of 1999		—	238,988	—	—	7,737	246,725
Net profit		—	—	—	—	58,189	58,189
Group reorganisation							
— additional paid in capital		12,500	—	3,826	—	—	16,326
— injection of assets from the Parent Company		237,500	(238,988)	38,333	—	(36,845)	—
— surplus/(deficit) arising from cost adjustment as a result of valuation for the purpose of the group reorganisation							
• property, plant and equipment	4(a)	—	—	(15,103)	—	—	(15,103)
• land use rights	4(b)	—	—	48,869	—	—	48,869
— deferred tax liabilities	4(n)	—	—	(6,535)	—	—	(6,535)
		250,000	—	69,390	—	29,081	348,471
Distribution to the Parent Company	3(f)	—	—	—	—	(29,081)	(29,081)
End of 2000		250,000	—	69,390	—	—	319,390
Net profit		—	—	—	—	87,411	87,411
Final dividend	3(h)	—	—	—	—	(45,000)	(45,000)
Transfer to statutory reserves		—	—	—	11,018	(11,018)	—
End of 2001		250,000	—	69,390	11,018	31,393	361,801
Net profit for the five months ended 31st May, 2002		—	—	—	—	77,371	77,371
As at 31st May, 2002		250,000	—	69,390	11,018	108,764	439,172

Notes:

(i) As at 31st December, 2000, the registered capital of the Company was RMB250,000,000 consisting of 250,000,000 Domestic shares at RMB1.00 per share. 237,500,000 shares were issued to the Parent Company, credited as fully paid in consideration for the transfer of the relevant assets and liabilities by the Parent Company. Further details of the Restructuring are set out in the Business Section of the Prospectus. The remaining 12,500,000 shares were issued to shareholders at cash. Shareholders' rights are governed by the PRC Company Law that requires an increase in registered capital to be approved by the shareholders in a general meeting and the relevant PRC Government and regulatory authorities.

(ii) In accordance with the relevant PRC regulations, the companies now comprising the Group are also required to transfer 10% of profit after tax, as determined under the PRC accounting regulations, to the statutory common reserve, until the balance of the fund reaches 50% of the registered capital. Subject to certain restrictions as set out in the relevant PRC regulations, the statutory common reserve may be used to offset against the accumulated losses, if any. Pursuant to the PRC regulations, the companies are required to transfer 5% to 10% of net profit, as determined under the PRC accounting regulations, to the statutory public welfare fund. This fund can only be used to provide staff welfare facilities and other collective benefits to the Company's employees. This fund is non-distributable other than in liquidation. The directors have proposed to transfer 10% and 5% of the net profit, as determined under the PRC accounting regulations, for the year ended 31st December, 2001 amounting to RMB7,345,000 and RMB3,673,000 to the statutory common reserve and the statutory common welfare fund, respectively.

(iii) As at 1st January, 1999, the paid-in capital represented the net assets value of the Relevant Businesses. Upon the incorporation of the Company, the net assets of the Relevant Businesses was contributed by the Parent Company for the incorporation of the Company and then capitalised as the share capital.

6. CONSOLIDATED CASH FLOW STATEMENTS

The consolidated cash flow statements of the Group for the Relevant Periods prepared on the basis set out in Section 1 above are as follows:

		Year ended 31st December,			Five months ended 31st May,
		1999	2000	2001	2002
	Notes	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
CASH FLOW FROM OPERATING ACTIVITIES	(a)	32,554	111,317	95,096	80,050
Interest paid		(21,521)	(23,133)	(17,778)	(4,567)
Net cash inflows from operating activities		11,033	88,184	77,318	75,483
CASH FLOW FROM INVESTING ACTIVITIES					
Interest received	3(d)	47	98	96	26
Acquisition of subsidiaries, net of cash acquired	4(c)	—	—	—	6,534
Purchase of property, plant, equipment and land use rights		(86,249)	(20,961)	(10,397)	(127)
Net cash flows (used in)/from investing activities		(86,202)	(20,863)	(10,301)	6,433
CASH FLOWS FROM FINANCING ACTIVITIES					
Contribution from the Parent Company		21,893	—	—	—
Contribution from minority shareholders		50	—	—	—
Paid in capital upon the incorporation of the Company		—	16,326	—	—
Distribution of profit	3(f)	—	(29,081)	—	—
Drawdown of short term bank loan	4(i)	—	—	20,000	—
Repayment of long term bank loan	4(m)	—	(95,000)	(9,000)	(6,000)
Increase/(decrease) in amounts due to the Parent Company		54,586	22,756	(61,903)	(43,692)
Net cash flows from/(used in) financing activities		76,529	(84,999)	(50,903)	(49,692)
Net increase/(decrease) in cash and cash equivalents		1,360	(17,678)	16,114	32,224
Cash and cash equivalents at beginning of year/period		32,952	34,312	16,634	32,748
CASH AND CASH EQUIVALENTS AT END OF YEAR/PERIOD		34,312	16,634	32,748	64,972

Notes:

(a) Reconciliation of profit before tax to net cash inflow from operating activities

		Year ended 31st December,			Five months ended 31st May,
		1999	2000	2001	2002
	Notes	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
Net profit before tax		7,831	58,193	87,405	77,380
Adjustments for:					
Net finance costs	3(d)	22,067	22,966	17,659	7,666
Depreciation and amortisation		21,282	28,143	28,404	12,005
Negative goodwill recognised as income	4(c)	—	—	—	(2,528)
Operating profit before working capital changes		51,180	109,302	133,468	94,523
Increase in accounts receivable		(4,183)	(8,729)	(7,623)	(8,944)
Increase in provision for doubtful debts		—	—	1,342	522
Increase in Airport fee receivable	4(g)	—	—	—	(29,442)
(Increase)/decrease in inventories		(115)	(1)	103	(10)
(Increase)/decrease in prepayments, deposits and other receivables		(121)	57	(1,173)	(1,248)
(Increase)/decrease in an amount due from related parties		(22,951)	12,329	(35,700)	19,920
Increase/(decrease) in accrued liabilities and other payables		6,649	(1,366)	3,803	4,651
Increase/(decrease) in deposit from customers		2,095	(275)	876	78
Cash generated from operations		32,554	111,317	95,096	80,050

(b) Major non-cash transactions

(i) On 31st December, 2000, the Parent Company assumed all the construction payables of RMB59,374,000 of the Company.

(ii) The Airport Fee amounting to RMB59,141,000 in 2002 was collected by the Parent Company on behalf of the Company from the passengers. The amount would be repaid to the Company and then passed to CAAC in late 2002.

(iii) Effective 31st May, 2002, the Company transferred certain assets of RMB28,399,000 to the Parent Company as part of the settlement for the consideration of the Acquired Businesses.

(iv) On 31st May, 2002, the Company acquired the Acquired Businesses from the Parent Company and the cash consideration will be settled by instalments within 12 months from that day.

7. DIRECTORS' AND SUPERVISORS' EMOLUMENTS

Save as disclosed herein, no emoluments has been paid or is payable in respect of the Relevant Periods referred to in this report by the Company or any of the companies now comprising the Group, to the directors or supervisors of the Company. Under the arrangements currently in force, the estimated amount of directors' and supervisors' fees and other emoluments payable to the directors and supervisors of the Company for the year ending 31st December, 2002 will be approximately RMB670,000, excluding discretionary bonuses payable under directors' and supervisors' service contracts, a summary of the terms of which is set out in the section headed "Further information about directors, supervisors and staff" in Appendix X to the Prospectus.

8. SUBSEQUENT EVENTS

(a) On 16th September, 2002 the Company entered into a conditional strategic investment agreement (the "Strategic Investment Agreement") with Copenhagen Airports A/S, a company duly incorporated under the laws of the Kingdom of Denmark and whose shares are listed on the Copenhagen Stock Exchange (the "Strategic Investor"). Pursuant to the Strategic Investment Agreement, approximately 20% of the enlarged issued share capital of the Company will be placed to the Strategic Investor immediately following completion of the public offering and the international placing including any exercise of the over-allotment option. The Strategic Investor has also undertaken not to purchase or subscribe for any additional H Shares so as to increase its shareholding in the Company to more than 25% of the issued share capital of the Company without the prior written consent of the Company. For the summary of the placing, please refer to the section headed "Business — Relationship with the strategic investor" of the Prospectus.

(b) Final dividend of RMB45,000,000 was declared for the year ended 31st December, 2001 by the shareholders of the Company on 19th July, 2002.

(c) On 10th September, 2002, the Company had a new short term bank loan granted by China Development Bank amounting to RMB50,000,000. The loan bears interest at 5.31% per annum and is unsecured. The loan was guaranteed by HNA Group and has a maturity date of 9th September, 2003. The Company obtained the written consent of China Development Bank on 4th November, 2002 to release the guarantee.

(d) Save as aforesaid, no other significant events took place subsequent to 31st May, 2002.

9. SUBSEQUENT FINANCIAL STATEMENTS

No audited financial statements have been prepared by the Company or any of the companies now comprising the Group in respect of any period subsequent to 31st May, 2002.

Yours faithfully,
Ernst & Young
Certified Public Accountants
Hong Kong

The information set out below does not form part of the accountants' report prepared by the auditors and reporting accountants of the Company, Ernst & Young Certified Public Accountants Hong Kong, as set out in Appendix I and is included for information purposes only.

The summary of consolidated results of operations of the Group for the three years ended 31st December, 1999, 2000 and 2001 and the five months ended 31st May, 2002 as set out in Section 3 of the accountants' report includes the consolidated results of the Company and its subsidiaries for each of the Relevant Periods or since their dates of incorporation or acquisition where this is a shorter period. To provide additional financial information, set out below are the pro forma unaudited combined results of operations of the Group for the three years ended 31st December, 1999, 2000 and 2001 and the five months ended 31st May, 2002 as if the Acquired Businesses had been held by the Company since 1st January, 1999, or since their respective dates of incorporation where this is a shorter period.

The pro forma unaudited combined results of operations of the Group presented below do not purport to represent what the results of operations would actually have been if the Acquired Business had been held by the Company since 1st January, 1999, or to project the results of operations for any future period and are included for information purposes only.

The pro forma unaudited combined results of operations of the Group for the years ended 31st December, 1999, 2000 and 2001 and the five months ended 31st May, 2002 are as follows:

	Year ended 31st December,			Five months ended 31st May,
	1999	2000	2001	2002
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
		(unaudited)		
Revenues				
Aeronautical	57,499	119,403	133,037	95,808
Non-aeronautical	25,516	45,971	70,185	41,141
Total revenues	83,015	165,374	203,222	136,949
Business taxes and levies	(2,968)	(6,017)	(7,288)	(4,655)
Net revenues	80,047	159,357	195,934	132,294
Operating costs:				
Cost of goods and services	(8,003)	(15,566)	(17,003)	(11,101)
Depreciation and amortisation	(21,656)	(28,615)	(30,522)	(13,031)
Staff costs	(5,793)	(9,008)	(8,251)	(3,923)
Utilities and power	(4,804)	(7,183)	(7,225)	(2,688)
Repairs and maintenance	(459)	(994)	(2,006)	(381)
Other costs	(314)	(629)	(1,354)	(1,186)
Total operating costs	(41,029)	(61,995)	(66,361)	(32,310)
Gross profit	39,018	97,362	129,573	99,984
Selling and distribution expenses	(450)	(618)	(620)	(575)
Administrative expenses	(8,505)	(15,600)	(13,778)	(8,433)
Profit from operating activities	30,063	81,144	115,175	90,976
Finance expenses, net	(22,072)	(22,985)	(17,698)	(7,678)
Profit before tax	7,991	58,159	97,477	83,298
Tax	—	—	—	—
Profit after tax	7,991	58,159	97,477	83,298
Minority interests	8	32	(9)	(45)
Net profit attributable to shareholders	7,999	58,191	97,468	83,253
Distribution to the Parent Company	—	29,081	—	—
Final dividend	—	—	45,000	—
Earnings per share — basic (RMB) — *note*	0.03	0.23	0.39	0.33

Note: The calculation of earnings per share is based on the Group's profit attributable to shareholders for each of the three years ended 31st December, 2001 and for the five months ended 31st May, 2002 and the 250,000,000 shares deemed to have been in issue and issuable during the Relevant Periods.

The forecast of the consolidated profit after tax and minority interests but before extraordinary items of the Group for the year ending 31st December, 2002 is set out in the section headed "Financial information — Profit forecast" in this prospectus.

1. BASES AND ASSUMPTIONS

The forecast of the consolidated profit after tax and minority interests but before extraordinary items of the Group for the year ending 31st December, 2002 prepared by the Directors is based on the audited financial statements of the Group for the five months ended 31st May, 2002, unaudited management accounts of the Group for the three months ended 31st August, 2002 and a forecast of the results of the Group for the four months ending 31st December, 2002. The Directors are not aware of any extraordinary items which have arisen or are likely to arise during the year ending 31st December, 2002. The forecast has been prepared on the basis of the accounting policies consistent in all material aspects with those currently adopted by the Group as summarised in the accountants' report, the text of which is set out in Appendix I to this prospectus and is based on the following principal assumptions:

1. There will be no material changes in the existing laws or regulations, government policies or political, legal (including changes in legislation or regulations or rules), fiscal or economic conditions in Hong Kong and the PRC in which the Group carries on business or from which it imports or sources its materials.

2. There will be no material changes in the inflation rate, interest rates or exchange rate from those prevailing as at the date of the prospectus.

3. There will be no material change in the bases or rates of taxation or duties in Hong Kong and the PRC in which the Group operates or in which the Group companies are incorporated or registered.

2. COMFORT LETTERS

Set out as follows are texts of letters received by the Directors from the Company's auditors and reporting accountants, Ernst & Young, and from the sponsors, The Hongkong and Shanghai Banking Corporation Limited and Oriental Patron Asia Limited, in connection with the profit forecast of the Group for the year ending 31st December, 2002, for the purpose of incorporation in this prospectus.

ERNST & YOUNG
安永會計師事務所

15th Floor
Hutchison House
10 Harcourt Road
Central
Hong Kong

6th November, 2002

The Directors
Hainan Meilan Airport Company Limited
The Hongkong and Shanghai Banking Corporation Limited
Oriental Patron Asia Limited

Dear Sirs,

We have reviewed the accounting policies and calculations adopted in arriving at the forecast of the consolidated profit after tax and minority interests but before extraordinary items of Hainan Meilan Airport Company Limited (the "Company") and its subsidiaries (hereinafter collectively referred to as the "Group") for the year ending 31st December, 2002, for which the directors of the Company are solely responsible, as set out in the paragraph headed "Profit forecast and dividend policy" in the section headed "Financial information" in the prospectus of the Company dated 6th November, 2002 (the "Prospectus"). The profit forecast has been prepared by the directors of the Company based on the audited consolidated results of the Group for the five months ended 31st May, 2002, unaudited management accounts of the Group for the three months ended 31st August, 2002 and a forecast of the consolidated results for the remaining four months of the year ending 31st December, 2002 on the basis that the Group had been in existence throughout the entire financial year ending 31st December, 2002.

In our opinion, the profit forecast, so far as the accounting policies and calculations are concerned, has been properly compiled on the bases and assumptions adopted by the directors of the Company as set out in Appendix III to the Prospectus, and is presented on a basis consistent in all material respects with the accounting policies normally adopted by the Group as set out in our Accountants' Report dated 6th November, 2002, the text of which is set out in Appendix I to the Prospectus.

This letter is being issued in connection with the offer for subscription or purchase of the H shares of the Company in Hong Kong and not to be used in connection with the Rule 144A offering in United States.

Yours faithfully,
Ernst & Young
Certified Public Accountants
Hong Kong

The Hongkong and Shanghai Banking Corporation Limited
Level 15
1 Queen's Central
Hong Kong

Oriental Patron Asia Limited
42nd Floor, COSCO Tower
183 Queen's Road Central
Hong Kong

6th November, 2002

The Directors
Hainan Meilan Airport Company Limited

Dear Sirs,

We refer to the forecast of the consolidated profit after tax and minority interests but before extraordinary items of Hainan Meilan Airport Company Limited (the "Company"), and its subsidiaries (hereinafter collectively referred to as the "Group") for the year ending 31st December, 2002 as set out in the paragraph headed "Profit forecast and dividend policy" in the section headed "Financial information" in the prospectus of the Company dated 6th November, 2002.

We have discussed with you the bases upon which the profit forecast has been made. We have also considered the letter dated 6th November, 2002 addressed to yourselves and ourselves from Ernst & Young regarding the accounting policies and calculations upon which the profit forecast has been made.

On the basis of the information comprising the profit forecast and on the bases of the accounting policies and calculations adopted by you and reviewed by Ernst & Young, we are of the opinion that the profit forecast, for which you as Directors of the Company are solely responsible, has been made after due and careful enquiry.

Yours faithfully,
For and on behalf of
The Hongkong and Shanghai Banking Corporation Limited
Guocang Huan
Head of Investment Banking, Asia Pacific

Yours faithfully,
For and on behalf of
Oriental Patron Asia Limited
Joseph Chan
Director

The following is the text of a letter, summary of values and valuation certificates, prepared for the purpose of incorporation in this prospectus received from Vigers Hong Kong Ltd., an independent valuer, in connection with its valuation as at 31st August, 2002 of the property interests of the Group in the PRC.

Vigers Hong Kong Ltd.
International Property Consultants

Suites 1607–1612, 16/F
Miramar Tower
132 Nathan Road
Tsimshatsui
Kowloon
Hong Kong

VIGERS
威格斯

6th November, 2002

The Board of Directors
Hainan Meilan Airport Company Limited
Haikou Meilan Airport
Qiongshan City
Hainan Province
The PRC

Dear Sirs,

In accordance with your instructions to us to value the property interests in which Hainan Meilan Airport Company Limited (the "Company") and its subsidiaries (together referred to as the "Group") have interests in the People's Republic of China (the "PRC"), we confirm that we have carried out inspections, made relevant enquiries and obtained such further information as we consider necessary for the purpose of providing you with our opinion of the open market values of the property interests as at 31st August, 2002.

Our valuation of the property interests is our opinion of the open market value which we would define as intended to mean — "the best price at which the sale of an interest in a property would have been completed unconditionally for cash consideration on the date of valuation assuming:

(a) a willing seller;

(b) that, prior to the date of valuation, there had been a reasonable period (having regard to the nature of the property and the state of the market) for the proper marketing of the interest, for the agreement of price and terms and for the completion of the sale;

(c) that the state of the market, level of values and other circumstances were, on any earlier assumed date of exchange of contracts, the same as on the date of valuation;

(d) that no account is taken of any additional bid by a prospective purchaser with a special interest; and

(e) that both parties to the transaction had acted knowledgeably, prudently and without compulsion."

For property interests in Categories I and II, which are owned by the Group in the PRC, we have adopted a combination of the open market and depreciated replacement cost approaches in assessing the land portions of the property and the buildings and structures erected on the land respectively. Hence, the sum of the two results represents the market value of the property as a whole. In the valuation of the land portions, reference has been made to the standard land price in Hainan Province and the sales comparables in the locality. As the nature of the buildings and structures cannot be valued on the basis of open market value, they have therefore been valued on the basis of their depreciated replacement cost. The depreciated replacement cost approach considers the cost to reproduce or replace in new condition the property appraised in accordance with current construction costs for similar buildings and structures in the locality, with allowance for accrued depreciation as evidenced by observed condition or obsolescence present, whether arising from physical, functional or economic causes. The depreciated replacement cost approach generally furnishes the most reliable indication of value for property in the absence of a known market based on comparable sales.

For property interests in Category III, which are rented by the Group from Parent Company in the PRC, we have assigned no commercial value due to their short-term nature or the prohibition against assignment, sub-letting or otherwise due to the lack of substantial profit rent.

For property interests located in the PRC, we have been provided with extracts of copies of title documents relating to the property interests. However, we have neither examined the original documents to verify ownership nor ascertained the existence of any amendments, which do not appear on the searches or copies submitted to us. In the course of our valuation, we still relied on the information provided by the Group and on the opinion of Jun He Law Offices, the Company's legal advisers on the PRC laws (the "PRC Legal Opinion"), regarding the title to the property interests. All documents and leases have been used for reference only.

In the course of our valuation, we have assumed that all consents, approvals and licences from relevant PRC government authorities for development of the properties in the PRC will be granted without any onerous conditions or undue delay. Moreover, we have also assumed free and uninterrupted rights to use, occupy or assign the property for the whole of the unexpired terms as granted.

Our valuations have been made on the assumption that the owner sells the property interests in the open market without the benefit of contracts with deferred terms, leaseback, joint venture, management agreement or any other similar arrangement which could serve to increase the value of the property interests. Furthermore, no account has been taken of any option or right of pre-emption concerning or affecting the sale of the property and no forced sale situation in any manner is assumed in our valuation.

We have inspected the exterior and, where possible, the interior of the properties. However, no structural survey has been made and we are therefore unable to report whether the properties are free from rot, infestation or any structural defects, though in the course of our inspections we did not note any serious defects. No tests were carried out on any of the services.

We have relied to a considerable extent on the information provided by the Group and have accepted advice provided to us by the Group on such matters as planning approvals or statutory notices, easements, tenure, particulars of occupancy, lettings, identification of the property interests, site and floor areas and other relevant information. Dimensions, measurements and areas included in the valuation certificates are based on information contained in the documents provided to us and are therefore only approximations. No on-site measurements have been made.

We have no reason to doubt the truth and accuracy of the information provided to us by the Group. The Group has also advised us that no material facts have been omitted from the information supplied to us to reach an informed view, and we have no reason to suspect that any material information has been withheld.

No allowance has been made in our valuation for any charges, mortgages or amounts owing on any of the property interests nor for any expenses or taxation which may be incurred in effecting a sale. Unless otherwise stated, it is assumed that the property interests are free from encumbrances, restrictions and outgoings of an onerous nature which could affect their values.

Unless otherwise stated, all monetary amounts stated are in Hong Kong dollars. The exchange rate adopted in our valuation is HK$1 = RMB1.06, and there has been no significant fluctuation in the exchange rates for RMB against Hong Kong dollars between that and the date of this letter.

Our summary of values and valuation certificates are attached herewith.

Yours faithfully,
For and on behalf of
VIGERS HONG KONG LTD.
Raymond Ho Kai Kwong,
Registered Professional Surveyor
MRICS, AHKIS
Director

Note: Raymond Kai Kwong Ho, Chartered Surveyor, MRICS, AHKIS, has extensive experience in undertaking valuations of properties in Hong Kong and Macau and has over nine years' experience in the valuation of properties in the PRC.

SUMMARY OF VALUES

Property	Open market value in existing state as at 31st August, 2002	Interests attributable to the Group	Capital value attributable to the Group in existing state as at 31st August, 2002
		(%)	
Category I — Property interests held and occupied by the Group in the PRC			
1. The Terminal Complex (including the land portion and the Main Terminal, two groups of ancillary buildings and a flyer erected thereon) located at Haikou Meilan Airport, Qiongshan City, Hainan Province, The PRC	RMB531,000,000 equivalent to HK$500,943,396	100%	RMB531,000,000 equivalent to HK$500,943,396
2. The Apron (including land and structures erected thereon) located at Haikou Meilan Airport, Qiongshan City, Hainan Province, The PRC	RMB66,000,000 equivalent to HK$62,264,151	100%	RMB66,000,000 equivalent to HK$62,264,151
3. The Cargo Centre (including land, building and structures erected thereon) located at Haikou Meilan Airport, Qiongshan City, Hainan Province, The PRC	RMB19,000,000 equivalent to HK$17,924,528	100%	RMB19,000,000 equivalent to HK$17,924,528
4. The Airport Car Park (including the land portion and structures erected thereon) located at Haikou Meilan Airport, Qiongshan City, Hainan Province, The PRC	RMB28,000,000 equivalent to HK$26,415,094	100%	RMB28,000,000 equivalent to HK$26,415,094
Sub-total:	RMB644,000,000 equivalent to HK$607,547,169		RMB644,000,000 equivalent to HK$607,547,169

Property	Open market value in existing state as at 31st August, 2002	Interests attributable to the Group	Capital value attributable to the Group in existing state as at 31st August, 2002
		(%)	
Category II — Property interest held by the Group under development in the PRC			
5. Custom and inspection joint operation complex (including land and buildings) Haikou Meilan Airport, Qiongshan City, Hainan Province, The PRC	RMB3,390,000 equivalent to HK$3,198,113	100%	RMB3,390,000 equivalent to HK$3,198,113
Sub-total:	RMB3,390,000 equivalent to HK$3,198,113		RMB3,390,000 equivalent to HK$3,198,113
Category III — Property interest leased and occupied by the Group from Parent Company in the PRC			
6. The entire second and third level of, An Office Building, Haikou Meilan Airport, Qiongshan City, Hainan Province, The PRC	No commercial value		No commercial value
Sub-total:	Nil		Nil
GRAND TOTAL:	RMB647,390,000 equivalent to HK$610,745,282		RMB647,390,000 equivalent to HK$610,745,282

VALUATION CERTIFICATE

Category I — Property interests held and occupied by the Group in the PRC

	Property	Description and tenure	Particulars of occupancy	Open market value in existing state as at 31st August, 2002
1.	The Terminal Complex (including the land portion and the Main Terminal, groups of ancillary buildings and a flyer erected thereon) located at Haikou Meilan Airport, Qiongshan City, Hainan Province, The PRC	The property comprises 4 parcels of regular level sites with a total site area of approximately 102,902.82 m^2 and buildings and structures erected thereon located mainly at the central portion of Haikou Meilan Airport. The buildings can be categorised into three groups: the Main Terminal, Fire Service Centre and Emergency Centre, contributing a total gross floor area of approximately 65,413 m^2. Major structures included a 643 metres long and 22.2 metres width flyer of reinforced concrete construction. The buildings and structures were completed in about 1999. Details of the gross floor areas for buildings are listed out as follows:	Portion of the Main Terminal with a floor area of approximately 2,422 m^2 is let to various tenants for various terms, with the latest one expiring on 30th April, 2005, contributing a total annual rental income of RMB10,102,638 (exclusive of tax and management fee) for commercial use. Portion of the Main Terminal with a floor area of approximately 1,723 m^2 is let to various airlines as airline counters and offices for various terms, with the latest one expiring on 31st July, 2005, contributing a total annual rental income of RMB4,190,400 (exclusive of tax and management fee). The remaining portion of the property is currently occupied and operated by the Group mainly as Terminal and ancillary uses.	RMB531,000,000 equivalent to HK$500,943,396 (100% interest attributable to the Group: HK$500,943,396)

Buildings		Gross floor area (m^2)
Main Terminal	approximately	60,296
Fire Service Centre	approximately	3,908
Emergency Centre	approximately	1,209
	approximately	65,413

The property is held under land use rights for a term of 50 years expiring on 5th September, 2049 for transportation uses.

Notes:

1. Pursuant to four State-owned Land Use Right Certificates all dated 5th September, 2002 issued by Qiongshan City State-owned Land Environmental Resources Bureau, the property with a total site area of approximately 102,902.82 m^2 was legally vested in Hainan Meilan Airport Company Limited (the "Company") for a term of 50 years expiring on 5th September, 2049 for transportation uses. Details of four State-owned Land Use Right Certificates are cited out in Note 3.

2. Pursuant to five Building Ownership Certificates all dated 6th September, 2002 issued by the Qiongshan City Real Estate Administration Bureau, the property, which comprises five blocks of buildings with a total gross floor area of approximately 65,413.04 m^2, was legally vested in the Company as Terminal and ancillary uses. Details of five Building Ownership Certificates are cited out in Note 3.

3. Detail information abstracted from the Title Certificates mentioned in Notes 1 and 2 above are summarised as follows:

	Name of a Building/ Group of Bldgs.	State-owned Land Use Right Certificate (Document No.)	Site Area (m^2)	Building Ownership Certificate (Document No.)	Gross Floor Area (m^2)	Remarks
1.	Main Terminal	瓊山籍國用(2002)字第08-0150號	35,604.920	瓊山市房權証美蘭公字第00006號	60,296.00	Subject to a mortgage agreement mentioned in Note 5 below
2.	Fire Service Centre	瓊山籍國用(2002)字第08-0151號	23,700.115	瓊山市房權証美蘭公字第00002-00004號	3,907.91	Subject to a mortgage agreement mentioned in Note 5 below
3.	Emergency Centre	瓊山籍國用(2002)字第08-0153號	3,597.080	瓊山市房權証美蘭公字第00001號	1,209.13	
4.	Flyer	瓊山籍國用(2002)字第08-0154號	40,000.705	N/A	N/A	Subject to a mortgage agreement mentioned in Note 5 below
		Sub-total:	102,902.820		65,413.04	

4. Pursuant to a promoters agreement dated 20th December 2000, Haikou Meilan Airport Company Limited ("Parent Company") injected into the Company assets, including buildings and equipment and current assets such as land and capital, at a consideration of RMB310.2 million. After the asset injection, Parent Company owned 95% of the Company. The property comprises a portion of the injected assets.

5. Portion of the property is subject to a mortgage agreement (Ref. No. 9632019 號借款合同的抵押合同) dated 20th September, 2001 in favour of 國家開發銀行 (China Development Bank) for a mortgage loan amount of RMB285,000,000. The mortgage term was originally of 12 years expiring on 20th December, 2008. The Company obtained the consent of China Development Bank on 4th November, 2002 to release this mortgage as soon as practicable.

6. Pursuant to a Business Licence (Registration No. 4600001008403) issued by Hainan Province Industrial and Commerce Executive Bureau to the Company on 12th June, 2001, the Company is permitted to register with a registered capital of RMB250,000,000. The term of operation is for 100 years commencing from 28th December, 2000 to 28th December, 2100. The scope of operation mainly covers the provision of transit and ground transportation services to foreign and domestic airlines and passengers; the provision of integrated services and leasing of the operational, commercial and office areas in the Main Terminal; investment of Airport and ancillary facilities; storage, wrapping, loading/unloading and transport of products.

7. Pursuant to the PRC Legal Opinion, we understand that the current status of titles, grant of major approvals, licences and documents of the property are as follows:

(a)	State-owned Land Use Right Certificate	Yes
(b)	Building Ownership Certificates	Yes
(c)	A promoters agreement	Yes
(d)	Mortgage Agreement	Yes
(e)	Business Licence	Yes

8. We have been provided with the PRC Legal Opinion, which contains, inter alia, the following information:

   (a) The Company has obtained the land use rights of the property legally by transfer;

   (b) The Company has obtained the building ownership rights of the buildings under the Building Ownership Certificate and is entitled to transfer, lease, mortgage or deal with these buildings by way of other legal means in the market with the residual term of its land use rights at no extra land premium and without other onerous charges payable to the government; and

   (c) The land use rights of the property together with the building ownership rights of the buildings erected on the land have been mortgaged for a period of 12 years expiring on 20th December, 2008. The Company completed third-party rights registration/or filing with respect to the property with Qiongshan City State-owned Land Environmental Resources Bureau. During the mortgage period, the Company can transfer or lease out the property subject to consent by the mortgagee.

9. According to the information provided by the Group, we understand that the Group holds 100% interest in the property referred to in this section 1 as at 31st August, 2002.

	Property	Description and tenure	Particulars of occupancy	Open market value in existing state as at 31st August, 2002
2.	The Apron (including land and structures erected thereon) located at Haikou Meilan Airport, Qiongshan City, Hainan Province, The PRC	The property comprises a parcel of rectangular level site with a total site area of approximately 163,237.29 m^2 located at the central portion of Haikou Meilan Airport. The land of the property is surfaced with concrete layer of 40 centimetres thick and cement/gravel layer of 40 centimetres thick, in order to sustain a designed concrete strength of 4–5Mpa. Structures, including lampposts, were found erected on the site. The property was completed in 1999. The property is held under land use rights for a term of 50 years expiring on 5th September, 2049 for transportation uses.	The property is currently occupied by the Group mainly for parking of aircraft.	RMB66,000,000 equivalent to HK$62,264,151 (100% interest attributable to the Group: HK$62,264,151)

Notes:

1. Pursuant to a State-owned Land Use Right Certificate (Document No. 瓊山籍國用(2002)字第08-0152號) dated 5th September, 2002 issued by Qiongshan City State-owned Land Environmental Resources Bureau, the property with a total site area of approximately 163,237.29 m^2 was legally vested in Hainan Meilan Airport Company Limited (referred hereinafter as the "Company") for a term of 50 years expiring on 5th September, 2049 for transportation uses.

2. Pursuant to a promoters agreement dated 20th December, 2000, Haikou Meilan Airport Company Limited (referred hereinafter as "Parent Company") injected into the Company assets, including buildings and equipment and current assets such as land and capital, at a consideration of RMB310.2 million. After the asset injection, Parent Company owned 95% of the Company. The property comprises a portion of the injected assets.

3. The property is subject to a mortgage agreement (Ref. No. 9632019 號借款合同的抵押合同) dated 20th September, 2001 in favour of 國家開發銀行. (China Development Bank) for a mortgage loan amount of RMB285,000,000. The mortgage term was originally of 12 years expiring on 20th December, 2008. The Company obtained the consent of China Development Bank on 4th November, 2002 to release this mortgage as soon as practicable.

4. Pursuant to a Business Licence (Registration No. 4600001008403) issued by Hainan Province Industrial and Commerce Executive Bureau to the Company on 12th June, 2001, the Company is permitted to register with a registered capital of RMB250,000,000. The term of operation is for 100 years commencing from 28th December, 2000 to 28th December, 2100. The scope of operation mainly covers the provision of transit and ground transportation services to foreign and domestic airlines and passengers; the provision of integrated services and leasing of the operational, commercial and office areas in the Main Terminal; investment of Airport and ancillary facilities; storage, wrapping, loading/unloading and transport of products.

5. Pursuant to the PRC Legal Opinion, we understand that the current status of titles, grant of major approvals, licences and documents of the property are as follows:

(a)	State-owned Land Use Right Certificate	Yes
(b)	A promoters agreement	Yes
(c)	Mortgage Agreement	Yes
(d)	Business Licence	Yes

6. We have been provided with the PRC Legal Opinion which contains, inter alia, the following information:

   (a) The Company had obtained the land use rights of the property legally by transfer and is entitled to transfer, lease, mortgage or deal with the property by way of other legal means in the market with the residual term of its land use rights at no extra land premium and without other onerous charges payable to the government; and

   (b) The land use rights of the property has been mortgaged for a period of 12 years expiring on 20th December, 2008. The Company completed third-party rights registration/filling of the property in Qiongshan City State-owned Land Environmental Resources Bureau. During the mortgage period, the Company can transfer or lease out the land use rights of the property after obtaining consent from the mortgagee.

7. According to the information provided by the Group, we are given to understand that the Group holds 100% interests in the property referred to in this section 2 as at 31st August, 2002.

	Property	Description and tenure	Particulars of occupancy	Open market value in existing state as at 31st August, 2002
3.	The Cargo Centre (including land, building and structures erected thereon) located at Haikou Meilan Airport, Qiongshan City, Hainan Province, The PRC	The property, comprises a parcel of rectangular level site with a total site area of approximately 16,119.94 m^2 and building and structures erected thereon located mainly at the eastern portion of Haikou Meilan Airport. The building is a two-storey reinforced concrete construction cargo storage building equipped with loading and unloading facilities. The total gross floor area of the building is approximately 4,337.27 m^2. Structures mainly included ancillary road, boundary walls, iron gates etc. Both the building and structures were completed in 1999. The property is held under land use rights for a term of 50 years expiring on 5th September, 2049 for transportation uses.	The property is currently occupied and operated by Yangzijiang Air Express Company Limited for a term commencing from 1st June, 2002 and expiring on 31st December, 2003 at nil annual rental for cargo storage purposes.	RMB19,000,000 equivalent to HK$17,924,528 (100% interest attributable to the Group: HK$17,924,528)

Notes:

1. Pursuant to a State-owned Land Use Right Certificate (Document No. 瓊山籍國用(2002)字第08-0155號) dated 5th September, 2002 issued by Qiongshan City State-owned Land Environmental Resources Bureau, the property with a total site area of approximately 16,119.937 m^2 was legally vested in Hainan Meilan Airport Company Limited (referred to hereinafter as the "Company") for a term of 50 years expiring on 5th September, 2049 for transportation uses.

2. Pursuant to a Building Ownership Certificate (Document No. 瓊山市房權證美蘭公字第00005號) dated 6th September, 2002 issued by the Qiongshan City Real Estate Administration Bureau, the property, which comprises a two-storey building with a total gross floor area of approximately 4,333.27 m^2, was legally vested in the Company for warehouse uses.

3. Pursuant to an Asset Swap Agreement dated 30th May, 2002 and its subsidiary agreements dated 31st August, 2002, the Group purchased the cargo centre from Parent Company at a consideration of RMB42 million.

4. Pursuant to a Business Licence (Registration No. 4600001008403) issued by Hainan Province Industrial and Commerce Executive Bureau to the Company on 12th June, 2001, the Company is permitted to register with a registered capital of RMB250,000,000. The term of operation is for 100 years commencing from 28th December, 2000 to 28th December, 2100. The scope of operation mainly covers the provision of transit and ground transportation services to foreign and domestic airlines and passengers; the provision of integrated services and leasing of the operational, commercial and office areas in the Main Terminal; investment of Airport and ancillary facilities; storage, wrapping, loading/unloading and transport of products.

5. Pursuant to the PRC Legal Opinion, we understand that the current status of titles, grant of major approvals, licences and documents of the property are as follows:

(a)	State-owned Land Use Right Certificate	Yes
(b)	Building Ownership Certificate	Yes
(c)	Asset Swap Agreement	Yes
(d)	Business Licence	Yes

6. We have been provided with the PRC Legal Opinion which contains, inter alia, the following information:

   (a) The Company has obtained the land use rights of the property legally by transfer; and

   (b) The Company has obtained the building ownership rights of the buildings under the Building Ownership Certificate and is entitled to transfer, lease, mortgage or deal with these buildings by way of other legal means in the market with the residual term of its land use rights at no extra land premium and without other onerous charges payable to the government.

7. According to the information provided by the Group, we understand that the Group holds 100% interests in the property referred to in this section 3 as at 31st August, 2002.

	Property	Description and tenure	Particulars of occupancy	Open market value in existing state as at 31st August, 2002
4.	The Airport Car Park (including the land portion and structures erected thereon) located at Haikou Meilan Airport, Hainan Province, The PRC	The property comprises a parcel of rectangular shaped level site with a total site area of approximately 54,183.1 m^2 serving as airport car park located at the central portion of Haikou Meilan Airport. The land portion of the property is surfaced with porous brick of 120 millimetres thick underlying a 20 centimetres thick concrete layer completed in about 1999. Major structures include a central fountain and landscaped area. The property is held under land use rights for a term of 50 years expiring on 5th September, 2049 for transportation uses.	The property is currently occupied and operated by the Group as a Car Park.	RMB 28,000,000 equivalent to HK$26,415,094 (100% interest attributable to the Group: HK$26,415,094)

Notes:

1. Pursuant to a State-owned Land Use Right Certificate (Document No. 瓊山籍國用(2002)字第08-0148號) dated 5th September, 2002 issued by Qiongshan City State-owned Land Environmental Resources Bureau, the property with a total site area of approximately 54,183.104 m^2 was legally vested in the Company for a term of 50 years expiring on 5th September, 2049 for transportation uses.

2. Pursuant to an Asset Swap Agreement dated 30th May, 2002 and its subsidiary agreements dated 31st August, 2002, the Group purchased the airport car park from Parent Company at a consideration of RMB28.8 million.

3. Pursuant to a Business Licence (Registration No. 4600001008403) issued by Hainan Province Industrial and Commerce Executive Bureau to the Company on 12th June, 2001, the Company is permitted to register with a registered capital of RMB250,000,000. The term of operation is for 100 years commencing from 28th December, 2000 to 28th December, 2100. The scope of operation mainly covers the provision of transit and ground transportation services to foreign and domestic airlines and passengers; the provision of integrated services and leasing of the operational, commercial and office areas in the Main Terminal; investment of Airport and ancillary facilities; storage, wrapping, loading/unloading and transport of products.

4. Pursuant to the PRC Legal Opinion, we understand that the current status of titles, grant of major approvals, licences and documents of the property are as follows:

(a)	State-owned Land Use Right Certificate	Yes
(b)	Asset Swap Agreement	Yes
(c)	Business Licence	Yes

5. We have been provided with the PRC Legal Opinion which contains, inter alia, the following information:

   The Company had obtained the land use rights of the property legally by transfer and is entitled to transfer, lease, mortgage or deal with the property by way of other legal means in the market with the residual term of its land use rights at no extra land premium and without other onerous charges payable to the government.

6. According to the information provided by the Group, we understand that the Group holds 100% interests in the property referred to in this section 4 as at 31st August, 2002.

Category II — Property interest held by the Group under development in the PRC

	Property	Description and tenure	Particulars of occupancy	Open market value in existing state as at 31st August, 2002
5.	Custom and inspection joint operation complex (including land and buildings) Haikou Meilan Airport, Qiongshan City, Hainan Province, The PRC	The property comprises a parcel of rectangular level site with a total site area of approximately 14,000 m^2 serving as the site of custom and inspection joint operation complex. Three five-storey buildings will be constructed on the site. According to the information provided by the Company, the estimated floor area to be constructed is approximately 11,177 m^2. The construction work is scheduled to be completed at the end of this year. The property is held under land use rights for a term of 50 years expiring on 5th September, 2049 for transportation uses.	The property is currently under construction and the construction work is scheduled to be completed at the end of 2002.	RMB3,390,000 equivalent to HK$3,198,113 (100% interest attributable to the Group: HK$3,198,113)

Notes:

1. Pursuant to a State-owned Land Use Right Certificate (Document No. 瓊山籍國用(2002)字第08-0149號) dated 5th September, 2002 issued by Qiongshan City State-owned Land Environmental Resources Bureau, the property (Lot No. LS-30-33) with a total site area of approximately 14,000 m^2 was legally vested in the Company for a term of 50 years expiring on 5th September, 2049 for transportation uses.

2. Pursuant to a Construction Land Use Planning Permit (Document No. 琼山規址(2001)046號) issued by Qiongshan City Construction Bureau on 29th September, 2002, the permitted site area for construction of the property is approximately 14,000 m^2.

3. Pursuant to a Copy of Construction Permit (Document No. 琼山土規建證(2001)050號) issued by Qiongshan City Construction Bureau on 29th September, 2002, the development scale of the property is permitted to comprise a gross floor area of approximately 13,371 m^2.

4. Pursuant to a Construction Commencement Permit (Document No. 460100206291401) issued by Hainan Province Construction Bureau to the Company on 29th June, 2002, the Company is permitted to commence the construction work of the property with a construction scale of approximately 11,176.93 m^2. The construction work is scheduled to be completed on 30th November, 2002.

5. Pursuant to a Contract for Transfer of State-owned Land Use Rights dated 1st June, 2002 entered into between Parent Company and the Company, Parent Company agreed to transfer the land use rights of the property with a site area of approximately 14,000 m^2 to the Company at a consideration of RMB2,697,520.

6. Pursuant to a Business Licence (Registration No. 4600001008403) issued by Hainan Province Industrial and Commerce Executive Bureau to the Company on 12th June, 2001, the Company is permitted to register with a registered capital of RMB250,000,000. The term of operation is for 100 years commencing from 28th December, 2000 to 28th December, 2100. The scope of operation mainly covers the provision of transit and ground transportation services to foreign and domestic airlines and passengers; the provision of integrated services and leasing of the operational, commercial and office areas in the Main Terminal; investment of Airport and ancillary facilities; storage, wrapping, loading/unloading and transport of products.

7. Pursuant to the PRC Legal Opinion, we understand that the current status of titles, grant of major approvals, licences and documents of the property are as follows:

(a)	State-owned Land Use Right Certificate	Yes
(b)	Construction Land Use Planning Permit	Yes
(c)	Construction Permit	Yes
(d)	Construction Commencement Permit	Yes
(e)	Contract for Transfer of State-owned Land Use Rights	Yes
(f)	Business Licence	Yes

8. We have been provided with the PRC Legal Opinion which contains, inter alia, the following information:

(a) The Company obtained the land use rights of the property under the State-owned Land Use Right Certificate legally by transfer;

(b) The Company has obtained all the necessary legal approvals, consets and permits in relation to the construction works on the property from relevant government authorities; and

(c) However, the property can only be transferred, mortgaged and leased when the construction work is completed and relevant title documents have been obtained. There is no legal impediment for the Company in obtaining such title documents from relevant government authorities.

9. The value for the land portion of the property is RMB3,390,000.

10. As advised by the Group, the estimated total construction costs expended as at 31st August, 2002 was approximately RMB1,363,821.15 and the outstanding construction costs to complete the development was approximately RMB9,640,000.

11. According to the information provided by the Group, we understand that the Group holds 100% interests in the property referred to in this section 5 as at 31st August, 2002.

Category III — Property interest leased and occupied by the Group from Parent Company in the PRC

	Property	Description and tenancy particulars	Particulars of occupancy	Open market value in existing state as at 31st August, 2002
6.	The entire second and third level of an office building, Haikou Meilan Airport, Qiongshan City, Hainan Province, The PRC	The property comprises two office levels in a three-storey reinforced concrete construction office building completed in 1999 amid the eastern portion of Haikou Meilan Airport. The total gross floor area of the property is approximately 1,415.0 m^2. The property is leased by the Group from Parent Company for a term of five years commencing from 1st January, 2002 to 31st December, 2006 at a monthly rental of RMB42,450 (exclusive of tax and management fee) for office uses and it is subject to a rent review once a year starting from 1st January, 2005 at the then agreed monthly rental by aforesaid parties.	The property is currently occupied by the Group as an office.	No commercial value

Notes:

1. The Landlord is Parent Company.

2. Pursuant to a confirmation letter issued to the Landlord on 24th September, 2002 by Qiongshan City Real Estate Administration Bureau, the Landlord is permitted to lease the property to the Company.

3. We have been provided with the PRC Legal Opinion which contains, inter alia, the following information:

   — The property is subject to a tenancy agreement dated 25th October, 2002 entered into between the Landlord and the Company for office uses;

   — The Company has legally acquired the right to use the property during the lease period;

   — According to a confirmation letter issued by Qiongshan City Real Estate Administration Bureau on 24th September, 2002, the Landlord is in the process of applying for the building ownership certificate of the property and there is no legal impediment for the Landlord in obtaining such certificate. Moreover, the Landlord is entitled to lease out the property;

   — However, before the Landlord has obtained the building ownership certificate, both the Landlord and the Tenant cannot conduct lease registration/filing for the captioned tenancy agreement with the relevant real estate authority in accordance with the PRC laws; and

   — The tenancy agreement is still binding on both parties and non-registration/filling would not affect the legality and effectiveness of the tenancy agreement or the use of the property by the Company. Should the Landlord breaches any of the terms and conditions set out in the tenancy agreement, the Company has the right to require the Landlord to compensate it with any loss arising as a result and vice versa.

4. The status of the title and grant of major approvals, consents and licences in accordance with the information provided by the Group and the PRC Legal Opinion are as follows:

A confirmation letter	Yes
Tenancy Agreement	Yes

The following is the text of a letter setting out a summary of the air traffic consultants' report prepared by Booz Allen Hamilton (Australia) Ltd., an independent air traffic consultant, in connection with airport traffic forecasts for the Meilan Airport.

Booz | Allen | Hamilton

Booz Allen Hamilton (Australia) Ltd.
ABN 82 003 512 623
Level 7, Riverside Centre
123 Eagle Street
Brisbane QLD 4000 Australia

Tel +61 7 3230 6400
Fax +61 7 3220 2044

www.bah.com.au

6th November, 2002

The Directors
Hainan Meilan Airport Company Limited
Haikou, Peoples Republic of China

Dear Sirs,

Booz Allen Hamilton was appointed by Hainan Meilan Airport Company Limited (the "Company") to prepare airport traffic forecasts for Haikou Meilan Airport for inclusion in the prospectus of the Company to be dated 6th November, 2002.

This letter presents background information regarding Booz Allen Hamilton, together with a summary of (1) historical trends in airport activity at Haikou Meilan Airport, (2) factors affecting future demand for airport services at Haikou Meilan Airport, (3) long-term airport traffic forecasts for Haikou Meilan Airport, and (4) risk factors that may affect actual results over the forecast horizon.

BOOZ ALLEN HAMILTON

Booz Allen Hamilton is an international management and technology consulting firm. The firm serves transportation industry clients world-wide and its staff have substantial experience across all modes of transportation (aviation, highway, maritime, public transportation and railway).

Booz Allen Hamilton has prepared airport traffic forecasts for airports in a number of countries including Australia, New Zealand, Canada, the United States, Russia, South Korea and China. Clients have included airport authorities, the banking sector, airlines and prospective bidders for newly privatised airports.

INFORMATION SOURCES

In preparing our forecasts, a range of data and information relating to Haikou Meilan Airport was considered including: (1) historical trends in aviation activities between January 1999 and May 2002, (2) review and analysis of factors affecting the demand for aviation services, (3) review of the development of tourism in China generally and Hainan Island specifically, and (4) review and assessment of independent forecasts with respect to future growth of China's economy and the key source countries generating air passenger traffic with China.

In preparing this letter, Booz Allen Hamilton has assumed that we can rely upon the validity of the findings set forth in the various data/surveys provided by the Company and we have relied upon, and accepted as complete and accurate, but have not independently verified, the accuracy and completeness of such data. Similarly, we have accepted as complete and accurate, but have not independently verified, the accuracy and completeness of data furnished to us by other entities.

All forecasts presented in this letter are unconstrained. That is, it is assumed that sufficient airport and tourism infrastructure is available to accommodate forecast demand.

RECENT TRENDS

Haikou Meilan Airport was commissioned in May 1999 following the closure of Haikou Dayingshan Airport. Haikou Meilan Airport passenger throughput has increased by over 40% in the first two full years of operation of Haikou Meilan Airport. Haikou Meilan Airport is the home base for Hainan Airlines, and ranked eighth nationally in terms of passenger throughput in 2001.

Table 1 details total passengers using international, regional (i.e. Hong Kong and Macau) and domestic route services at Haikou Meilan Airport between 1999 and 2001. Over this period, total passengers increased by 41.5% and increases for each service type were as follows: international route (85.7%), Hong Kong/Macau (–21.7%) and domestic (45.4%).

TABLE 1 PASSENGER THROUGHPUT OF HAIKOU MEILAN AIRPORT (IN THOUSANDS) FROM 1999 TO 2001[(a)]

SERVICE TYPE	1999	2000	2001
International route	7	12	13
Hong Kong/Macau route	212	172	166
Domestic route	3,369	4,179	4,899
Total	3,588	4,363	5,078

(a) Reflects operations at Haikou Dayingshan Airport to May 1999 and Haikou Meilan Airport after May 1999.

Source: The Company.

Table 2 presents details of aircraft movements, by service type, operator type and Maximum Take-Off Weight ("MTOW"), between 1999 and 2001. Over this period, total aircraft movements increased by 10.4% and changes for each service type were as follows: international route (103.5%), Hong Kong/Macau (–21.5%), domestic (10.0%) and other (31.6%).

TABLE 2 AIRCRAFT MOVEMENTS OF HAIKOU MEILAN AIRPORT FROM 1999 TO 2001[(a)]

SERVICE TYPE	1999	2000	2001
International route			
Mainland carriers			
MTOW < 25 tonnes	0	0	2
25 < MTOW < 100 tonnes	80	165	147
100 < MTOW < 200 tonnes	5	4	24
MTOW > 200 tonnes	0	0	0
Other carriers (SAR and foreign)			
MTOW < 25 tonnes	0	0	0
25 < MTOW < 100 tonnes	0	0	0
100 < MTOW < 200 tonnes	0	0	0
MTOW > 200 tonnes	0	0	0
Sub-total	85	169	173
Hong Kong/Macau route			
Mainland carriers			
MTOW < 25 tonnes	0	3	3
25 < MTOW < 100 tonnes	569	37	52
100 < MTOW < 200 tonnes	790	727	706
MTOW > 200 tonnes	0	0	2
Other carriers (SAR and foreign)			
MTOW < 25 tonnes	0	0	0
25 < MTOW < 100 tonnes	579	901	759
100 < MTOW < 200 tonnes	0	0	0
MTOW > 200 tonnes	0	0	0
Sub-total	1,938	1,668	1,522
Domestic route			
Mainland carriers			
MTOW < 25 tonnes	na	na	5,974
25 < MTOW < 100 tonnes	na	na	34,974
100 < MTOW < 200 tonnes	na	na	6,666
MTOW > 200 tonnes	na	na	100
Other carriers (SAR and foreign)			
MTOW < 25 tonnes	0	0	0
25 < MTOW < 100 tonnes	0	0	0
100 < MTOW < 200 tonnes	0	0	0
MTOW > 200 tonnes	0	0	0
Sub-total	43,360	49,348	47,714

SERVICE TYPE	1999	2000	2001
Other movements			
MTOW < 25 tonnes	na	na	3,691
25 < MTOW < 100 tonnes	na	na	508
100 < MTOW < 200 tonnes	na	na	175
MTOW > 200 tonnes	na	na	3
Sub-total	3,327	5,580	4,377
Total	48,709	56,765	53,786

na: Not available.

(a) Reflects operations at Haikou Dayingshan Airport to May 1999 and Haikou Meilan Airport after May 1999.

Source: The Company.

Table 3 sets out details of cargo carried between 1999 and 2001. Over this period, total cargo throughput increased by 23.5%.

TABLE 3 CARGO THROUGHPUT OF HAIKOU MEILAN AIRPORT (THOUSAND TONNES) FROM 1999 TO 2001[a]

SERVICE TYPE	1999	2000	2001
Total	43.8	53.6	54.1

(a) Reflects operations at Haikou Dayingshan Airport to May 1999 and Haikou Meilan Airport after May 1999.

Source: The Company

FACTORS AFFECTING DEMAND

The most important factors affecting demand for aviation services at Haikou Meilan Airport can be summarised as follows:

- **Economic Growth.** Future growth in the China economy will have a significant impact on future activity levels at Haikou Meilan Airport, most importantly via the impact of economic growth on domestic tourism activity. The central forecast assumes that China's economy will grow at an average annual rate of 7.2% between 2002 and 2021 in real terms.

- **Regulatory and Political Environment.** The domestic forecasts implicitly assume that growth will not be unduly constrained by market intervention by the Civil Aviation Administration of China ("CAAC"), specifically in relation to the regulation of fare and service levels.

- **Airline Market Structure.** CAAC is committed to a process of industry consolidation that will see second-tier CAAC carriers aligned under the largest three carriers, Air China, China Eastern Airlines and China Southern Airlines. All non-CAAC carriers can join one of the three groups, merge to form new groups or not enter into the consolidation process. The Haikou-based Hainan Airlines, which together with its subsidiaries, operates the fourth largest airlines group in China, is one of these non-CAAC carriers. It is assumed that the process of industry consolidation does not significantly impact on the competitive dynamics of the Hainan Island aviation market.

- **Airline Fares and Service Delivery.** The forecasts specifically consider expected changes in real air fares, passenger seat load factors and the fleet mix serving Haikou Meilan Airport over the forecast horizon.

  Modest short-term domestic real air fare reductions are assumed under the central growth forecast (i.e. 1% per annum) and the high growth forecast (i.e. 2.5% per annum) in 2003 and 2004 as price controls are progressively relaxed by the CAAC. Under the high growth forecast, further modest reductions in real air fares are provided for between 2005 and 2007 (i.e. 1% per annum). Under the low growth forecast, real air fares are assumed to remain constant throughout the forecast horizon. International and regional air fares are also assumed to decline modestly under the central and high growth scenarios, with assumed reductions no greater than 1% in any given year.

Domestic and international passenger seat load factors are assumed to remain constant at 75% throughout the forecast horizon. It is assumed that regional load factors will increase in the medium-term from 60% to 65% on the basis of expected growth in international leisure traffic transiting Hong Kong.

The average size of the domestic fleet is assumed to increase to 2010 due to the assumed progressive replacement of Boeing 737 aircraft by Boeing 757 equipment. Thereafter, average aircraft size is assumed to remain constant. The forecasts assume no change in the international and regional fleet mix to 2006. Thereafter, the forecasts provide for a slow, steady increase in average aircraft capacity (i.e. 1 seat per annum).

- **Airport Competition.** Consideration was given to the impact of competition between the two Hainan Island Airports (i.e. Haikou Meilan Airport and Sanya Phoenix Airport). It is assumed that the competition for traffic is essentially restricted to the international and regional market. The forecasts assume that Haikou Meilan Airport will attain full international status around the end of 2002 and this will facilitate an increase in the Haikou Meilan Airport share of Hainan Island regional and international traffic.

TRAFFIC FORECASTS

Three forecasts were prepared by Booz Allen Hamilton. The "central" forecast represents the "base case" or "most likely" expected outcome. The "low" forecast employs a more pessimistic scenario with respect to the growth of China's economy. Conversely, the "high' forecast incorporates a more optimistic economic growth forecast for China's economy relative to the central forecast.

Table 4 summarises the passenger forecasts for Haikou Meilan Airport under each of the three scenarios.

TABLE 4 PASSENGER THROUGHPUT OF HAIKOU MEILAN AIRPORT (IN THOUSANDS) FOR SELECTED FORECAST YEARS

SERVICE TYPE	2001	2006	2011	2021
Low				
International route	13.0	74.9	96.7	126.7
Regional route	166.1	216.5	287.9	487.6
Domestic route	4,899.1	7,357.6	10,422.8	17,859.8
Total	5,078.2	7,649.0	10,807.4	18,474.1
Central				
International route	13.0	86.9	120.3	180.6
Regional route	166.1	234.6	331.2	601.7
Domestic route	4,899.1	7,936.1	11,810.0	20,969.2
Total	5,078.2	8,257.6	12,261.5	21,751.5
High				
International route	13.0	115.2	174.9	320.0
Regional route	166.1	268.0	400.3	779.8
Domestic route	4,899.1	8,832.4	13,873.0	25,426.0
Total	5,078.2	9,215.6	14,448.2	26,525.8

Source: Booz Allen Hamilton estimates.

Note: Figures may not add up due to rounding.

Table 5 summarises the cargo forecasts for Haikou Meilan Airport under each of the three scenarios.

TABLE 5 CARGO THROUGHPUT OF HAIKOU MEILAN AIRPORT (IN THOUSANDS) FOR SELECTED FORECAST YEARS

SERVICE TYPE	2001	2006	2011	2021
Low	54.1	79.1	112.7	193.1
Central	54.1	102.3	166.0	294.7
High	54.1	139.2	254.9	467.2

Source: Booz Allen Hamilton estimates.

Tables 6–9 summarises the aircraft movement forecasts for Haikou Meilan Airport under each of the three scenarios.

TABLE 6 INTERNATIONAL AIRCRAFT MOVEMENTS AT HAIKOU MEILAN AIRPORT FOR SELECTED FORECAST YEARS

SERVICE TYPE	2001	2006	2011	2021
Low				
Mainland carriers				
MTOW < 25 tonnes	0	0	0	0
25 < MTOW < 100 tonnes	150	360	400	320
100 < MTOW < 200 tonnes	20	20	40	170
MTOW > 200 tonnes	0	0	0	0
Other carriers (SAR and foreign)				
MTOW < 25 tonnes	0	0	0	0
25 < MTOW < 100 tonnes	0	360	400	320
100 < MTOW < 200 tonnes	0	0	60	260
MTOW > 200 tonnes	0	0	0	0
Total	170	750	910	1,060
Central				
Mainland carriers				
MTOW < 25 tonnes	0	0	0	0
25 < MTOW < 100 tonnes	150	410	490	440
100 < MTOW < 200 tonnes	20	20	50	240
MTOW > 200 tonnes	0	0	0	0
Other carriers (SAR and foreign)				
MTOW < 25 tonnes	0	0	0	0
25 < MTOW < 100 tonnes	0	410	490	440
100 < MTOW < 200 tonnes	0	0	70	360
MTOW > 200 tonnes	0	0	0	0
Total	170	850	1,110	1,480
High				
Mainland carriers				
MTOW < 25 tonnes	0	0	0	10
25 < MTOW < 100 tonnes	150	540	710	770
100 < MTOW < 200 tonnes	20	20	70	410
MTOW > 200 tonnes	0	0	0	0
Other carriers (SAR and foreign)				
MTOW < 25 tonnes	0	0	0	0
25 < MTOW < 100 tonnes	0	540	710	770
100 < MTOW < 200 tonnes	0	0	100	620
MTOW > 200 tonnes	0	0	0	0
Total	170	1,110	1,590	2,590

Source: Booz Allen Hamilton estimates.

Note: Figures may not add up due to rounding.

TABLE 7 HONG KONG/MACAU AIRCRAFT MOVEMENTS AT HAIKOU MEILAN AIRPORT FOR SELECTED FORECAST YEARS

SERVICE TYPE	2001	2006	2011	2021
Low				
Mainland carriers				
MTOW < 25 tonnes	0	0	0	10
25 < MTOW < 100 tonnes	50	180	200	160
100 < MTOW < 200 tonnes	710	690	810	1,540
MTOW > 200 tonnes	0	0	50	290
Other carriers (SAR and foreign)				
MTOW < 25 tonnes	0	0	0	0
25 < MTOW < 100 tonnes	760	710	810	640
100 < MTOW < 200 tonnes	0	40	200	390
MTOW > 200 tonnes	0	0	30	190
Total	1,520	1,610	2,100	3,210
Central				
Mainland carriers				
MTOW < 25 tonnes	0	0	0	10
25 < MTOW < 100 tonnes	50	190	220	200
100 < MTOW < 200 tonnes	710	810	1,020	1,970
MTOW > 200 tonnes	0	0	50	370
Other carriers (SAR and foreign)				
MTOW < 25 tonnes	0	0	0	0
25 < MTOW < 100 tonnes	760	750	890	810
100 < MTOW < 200 tonnes	0	40	260	490
MTOW > 200 tonnes	0	0	40	250
Total	1,520	1,800	2,480	4,100
High				
Mainland carriers				
MTOW < 25 tonnes	0	0	0	10
25 < MTOW < 100 tonnes	50	190	240	280
100 < MTOW < 200 tonnes	710	1,070	1,410	2,650
MTOW > 200 tonnes	0	0	70	500
Other carriers (SAR and foreign)				
MTOW < 25 tonnes	0	0	0	0
25 < MTOW < 100 tonnes	760	780	970	1,100
100 < MTOW < 200 tonnes	0	60	350	660
MTOW > 200 tonnes	0	0	40	330
Total	1,520	2,100	3,090	5,530

Source: Booz Allen Hamilton estimates.

Note: Figures may not add up due to rounding.

TABLE 8 DOMESTIC AIRCRAFT MOVEMENTS AT HAIKOU MEILAN AIRPORT FOR SELECTED FORECAST YEARS

SERVICE TYPE	2001	2006	2011	2021
Low				
Mainland carriers				
MTOW < 25 tonnes	5,974	8,450	11,790	20,210
25 < MTOW < 100 tonnes	34,970	42,620	55,720	95,470
100 < MTOW < 200 tonnes	6,670	16,180	26,350	45,150
MTOW > 200 tonnes	100	250	340	590
Other carriers (SAR and foreign)				
MTOW < 25 tonnes	0	0	0	0
25 < MTOW < 100 tonnes	0	0	0	0
100 < MTOW < 200 tonnes	0	0	0	0
MTOW > 200 tonnes	0	0	0	0
Total	47,710	67,490	94,200	161,420
Central				
Mainland carriers				
MTOW < 25 tonnes	5,970	9,110	13,360	23,730
25 < MTOW < 100 tonnes	34,970	45,970	63,130	112,090
100 < MTOW < 200 tonnes	6,670	17,450	29,860	53,010
MTOW > 200 tonnes	100	260	390	690
Other carriers (SAR and foreign)				
MTOW < 25 tonnes	0	0	0	0
25 < MTOW < 100 tonnes	0	0	0	0
100 < MTOW < 200 tonnes	0	0	0	0
MTOW > 200 tonnes	0	0	0	0
Total	47,710	72,790	106,740	189,520
High				
Mainland carriers				
MTOW < 25 tonnes	5,970	10,140	15,670	28,770
25 < MTOW < 100 tonnes	34,970	51,160	74,160	135,920
100 < MTOW < 200 tonnes	6,670	19,420	35,070	64,280
MTOW > 200 tonnes	100	290	460	830
Other carriers (SAR and foreign)				
MTOW < 25 tonnes	0	0	0	0
25 < MTOW < 100 tonnes	0	0	0	0
100 < MTOW < 200 tonnes	0	0	0	0
MTOW > 200 tonnes	0	0	0	0
Total	47,710	81,010	125,380	229,800

Source: Booz Allen Hamilton estimates.

Note: Figures may not add up due to rounding.

TABLE 9 OTHER AIRCRAFT MOVEMENTS AT HAIKOU MEILAN AIRPORT FOR SELECTED FORECAST YEARS

SERVICE TYPE	2001	2006	2011	2021
Low				
MTOW < 25 tonnes	3,690	4,520	5,530	8,280
25 < MTOW < 100 tonnes	510	620	760	1,140
100 < MTOW < 200 tonnes	180	210	260	390
MTOW > 200 tonnes	0	10	30	200
Total	4,380	5,360	6,580	10,010
Central				
MTOW < 25 tonnes	3,690	4,640	5,820	9,180
25 < MTOW < 100 tonnes	510	640	800	1,260
100 < MTOW < 200 tonnes	180	220	280	440
MTOW > 200 tonnes	0	10	30	230
Total	4,380	5,500	6,920	11,100
High				
MTOW < 25 tonnes	3,690	4,760	6,130	10,180
25 < MTOW < 100 tonnes	510	660	840	1,400
100 < MTOW < 200 tonnes	180	230	290	480
MTOW > 200 tonnes	0	10	30	250
Total	4,380	5,650	7,290	12,320

Source: Booz Allen Hamilton estimates.

Note: Figures may not add up due to rounding.

RISK ASSESSMENT

Any airport traffic forecast is subject to uncertainties. Inevitably, some assumptions used to develop the forecasts will not be realised, and unanticipated events and circumstances may occur. Therefore, Booz Allen Hamilton cannot provide any form of assurance that the forecasts documented in this letter will be achieved. The actual traffic outcomes will vary from those forecast, and the variations may be material.

Specifically, the following factors could result in actual outcome outside the range set out in this letter:

- lower than assumed rates of economic growth in China and those countries expected to provide a significant source of inbound international air passengers
- shifts in Government policy which directly, or indirectly, suppress Haikou Meilan Airport traffic
- adverse impacts for Haikou Meilan Airport associated with aviation industry consolidation
- a significant shift in the distribution of aviation traffic between the two Hainan Island airports (i.e. Haikou Meilan Airport and Sanya Phoenix Airport)
- significant changes in airline costs (e.g. a fuel price shock) which are passed onto customers by way of higher fares
- external factors including, but not limited to, natural disasters, political unrest, acts of terrorism and associated security concerns and labour disputes.

This letter was prepared for the exclusive use of Hainan Meilan Airport Company Limited. No third parties may rely on it.

Yours sincerely,
For and on behalf of
Booz Allen Hamilton (Australia) Ltd.
Mark Streeting
Technical Director

Note: (1) Mr Streeting is a highly experienced transport economist with more than 16 years experience. Before joining Booz Allen Hamilton in 1996, Mr Streeting worked in aviation research and policy positions for the Australian Government and as an independent consultant to the Australian aviation industry. He has completed a wide range of aviation studies including demand analysis and forecasting studies, pricing studies (fares and airport landing charges), financial and economic evaluation and major reviews of airline operations. Mr Streeting has managed aviation consultancy assignments for clients including investment banks, airport authorities and government bodies throughout the Asia-Pacific region.

The following is the text of a letter setting out a summary of the engineering consultants' report prepared by Parsons Brinckerhoff (Asia) Limited, an independent engineering consultant in connection with the review of the Meilan Airport's assets and assessment of related capital and maintenance costs.

PB 100 YEARS ®

6th November, 2002

The Directors
Hainan Meilan Airport Company Limited

Dear Sirs,

Engineering Assessment for the Haikou Meilan Airport
Executive Summary

In accordance to your instructions to undertake an engineering assessment (the "Study") of the assets of the Hainan Meilan Airport Company Limited (the "Company"), Parsons Brinckerhoff (Asia) Ltd. (the "Consultant" or "PBA") have completed a review of the engineering conditions of the facilities owned by the Company, and an assessment of the capital costs of the proposed capital expansion programme as well as the costs associated with the maintenance of the Company's assets. In addition, we have reviewed the engineering conditions of the airfield facilities owned by the Haikou Meilan Airport Company Limited, which is the parent company of the Company.

This report sets forth the findings of the Study performed by PBA for the purpose of the listing of the Company on the Stock Exchange of Hong Kong.

EXECUTIVE SUMMARY

1. Introduction

This is a summary of the "Engineering Assessment Report for Hainan Meilan Airport Company Limited" which was prepared by PBA. PBA was appointed by the Company to carry out an independent engineering assessment of the assets of the Company.

2. Objectives

The technical objective of the Study was to provide the Company with an independent opinion of the physical conditions of the engineering aspects of the facilities and assets owned by the Company, and to provide an assessment of the capital costs of the planned capital expansion projects by the Company, as well as a maintenance cost projection for twenty-year horizon.

3. Study Approach

In conducting the Study, the Consultant carried out a site inspection of the Meilan Airport, reviewed engineering and architectural drawings of the terminal building and other structures including the runway, taxiways and apron, interviewed airport maintenance personnel, reviewed the airport long term master plan, and collected historical maintenance cost information of the airport.

The engineering assessment of the Company's assets is based on a visual inspection of the conditions of the facilities and a comprehensive review of the data and documents provided by the Company. We have assumed that such information supplied by the Company is factual and accurate.

4. Conditions of Existing Facilities

The Haikou Meilan Airport ("Meilan Airport") was commissioned in May 1999. It is located approximately 25-kilometre southeast of the city of Haikou, the capital of Hainan province. The ICAO reference coordinates for the Meilan Airport is 110 degrees 26 minutes 86 seconds east and 19 degrees 56 minutes 5.95 seconds north. The land area around the Meilan Airport is flat, with ground elevations between 11 to 30 metres above sea level.

The Meilan Airport has a 3,600-metre runway oriented in the east-west direction (headings 90 degrees 28 minutes and 270 degrees 28 minutes). The airport is served by a single terminal building located on the north side of the runway. The terminal building has a total floor area of about 60,296 m^2.

The conditions of the airport's facilities are described below.

Airfield

Although the airfield is not part of the Company's assets, we have reviewed the existing conditions of airfield facilities because the airfield has a direct impact on the operation and revenues of the Company.

The Meilan Airport's only existing runway (09/27) has a total length of 3,600 metres which can accommodate fully loaded B-747-400 aircraft. Its annual and peak hour operational capacity is more than sufficient to meet the projected aircraft operational demands for the year 2005. Visual inspection of the runway indicated that the concrete runway, taxiways, runway markings, lights, etc., are all very well maintained. No pavement cracks were visible on the runway and no differential settlement was detected. The drainage system of the airfield consists of a series of large open channels and also appears to be in good repair.

The Meilan Airport is equipped with the following navigational aids:

- Runway 09 Category II Precision Instrument Landing System
- Runway 27 Category I Precision Instrument Landing System
- Doppler VHF Omnidirectional Radio Range
- Air Traffic Control Tower

- Doppler Meteorological Observation System

The above navigational aids allow for safe aircraft operations in most weather conditions.

Terminal

The terminal complex was designed to support approximately six million annual passengers and consists of a four-level terminal building with 60,296 m^2 of floor space. The terminal includes the following functional areas:

Apron

The apron, which is part of the Company's assets, consists of 15 parking positions. Seven (7) are contact aircraft parking positions with second level passenger loading bridges. Eight (8) are remote apron parking positions.

Apron Fuel Hydrant System

The 15 aircraft parking positions are all served by a sub-surface fuel hydrant system from the main fuel farm. This system reduces aircraft service vehicle traffic on the apron to create a safer aircraft operating environment.

Utility System

The terminal's air conditioning system, water system, sanitary sewer system, the back-up power supply system, communication system, etc. are housed in the terminal basement level, the facility centre located near the northwest corner of the terminal, and other auxiliary buildings in the airport area. These facilities are in good condition.

Baggage Handling

The baggage make-up areas are located adjacent to the apron roadways and are equipped with three mechanical carousels which appear to be in good condition. The four baggage claim carousels at the arrival level, both domestic and international, are also in good working order. The baggage claim area is well lit and spacious with room provided for future expansion.

Customs and Immigration Areas

The customs inspection area on the ground level is well laid out and sufficient room has been provided for expansion. The inbound immigration control for international arrivals is located on the mezzanine above the departure level. For outbound passengers, the immigration control is on the departure level. The customs and immigration areas are well lit, signings are clear, and access to these areas are efficient.

Ground Level Arrival Hall

Hotel, transportation, money exchange, etc. essential services are all available at the arrival hall outside the baggage claim areas. Signage is clear and the area is well lit and clean.

Ground Level Service Docks

Concession deliveries and terminal maintenance vehicle access to the terminal is provided by a service dock on the west side of the terminal. Truck access is efficient and the dock area does not conflict with ground level curb front traffic.

Ground Level Curb Front

The covered curb front passenger pick-up area appears to function efficiently and no traffic congestion was observed. The concrete pavement and drainage appeared to be in good condition.

Second Level Curb Front

The second level curb front was also uncongested. The asphalt overlay on the roadway has developed some rutting and cracks and the paint on the curb front canopy is also peeling due to the effects of tropical weathering. Repairs to these elements are required in the short term.

Second Level Departure Hall

Airline ticketing offices, check-in counters, money exchange, etc. essential services are available at the departure hall which is well laid out. A large area at the east end of the departure lobby is available for additional concession space.

Passenger Hold Area

Passenger hold rooms and concession areas are provided in the secure area of the second level. Seven passenger loading bridges are available for aircraft loading. Additional passenger holding areas for the remote parking positions are provided on the ground level accessed via an escalator. The loading bridges are in good condition and the design allows for access to all major aircraft types.

Terminal Fire Safety and Emergency Exits

Passenger orientation to the emergency exits is uncomplicated with the linear configuration of the terminal and the glass walls on four sides. The exits are clearly signed and well lit. Sprinklers are provided throughout the terminal. Fire and Rescue Services for the airport is located in a nearby separate building west of the terminal.

5. Future Expansion Plan

The Meilan Airport master plan includes a near term expansion of the existing terminal and airfield, and a long term north airfield and terminal complex. This Study is for the near term expansion only.

The near term capital construction programme approved by the government includes the following:

- A 30,000 m^2 expansion of the terminal building plus associated 280,000 m^2 apron and utilities

- A multi-tenant cargo centre with 30,000 m^2 warehouse and 50,000 m^2 apron

It is expected that the above described programme will provide sufficient capacity to accommodate approximately eight million passengers per year. Given the historical air traffic growth of Meilan Airport, PBA has identified additional airport capital investment likely to be required within the next 10 years to meet air traffic demand up to 15 million passengers per year, which is the estimated capacity of the existing 09/27 runway:

- Over 60,000 m^2 expansion of the terminal building plus associated apron and facilities

The estimated capital costs of the above projects are listed in the table below.

Project	Year	Cost
		(million RMB)
Near Term Terminal expansion	2003–2004	355.6
Near Term Multi-tenant cargo centre	2003–2004	209.6
Medium Term Terminal expansion	2007–2008	405.4

It should be noted that if and when air passenger traffic of the Meilan Airport exceeds 15 million per year, it will be necessary to consider implementation of the north airfield and terminal complex in the long term master plan. The costs associated with this long term expansion are to be investigated in the context of a separate investment decision process.

6. Maintenance Costs

Maintenance of the Company's assets is carried out by the Company's own maintenance department, as well as by other parties through service agreements which cover services such as provision of security forces, power and water, vehicle maintenance, etc. Therefore a detailed maintenance cost record was not available. In the table below, the maintenance cost projection is based on data and information provided by the Company, and on PBA's independent estimate of maintenance costs for major asset items. The following cost projections considered repair and maintenance costs of the existing facilities, the proposed near term capital expansion projects, and the medium term expansions suggested by the Consultant.

Year	Cost *(in million RMB)*
2002	8.00
2003	8.07
2004	11.76
2005	11.16
2006	11.85
2007	11.95
2008	17.21
2009	19.13
2010	17.42
2011	17.55
2012	18.16
2013	19.28
2014	20.63
2015	19.05
2016	19.71
2017	19.71
2018	21.71
2019	22.01
2020	19.71
2021	19.71

7. Conclusions

Based on a visual inspection of the Company's assets and limited as-built data and information, the Consultant has found the Meilan Airport to be in good engineering condition. The capital and maintenance cost estimates in the Study report and extracted to this summary are based on generalised unit costs and are for reference only.

Yours sincerely,
For and on behalf of
PARSONS BRINCKERHOFF (ASIA) LTD.

Jie Tai Huang — *Project Director*
Charles Ng — *Project Manager*

TAXATION OF SECURITY HOLDERS

The following is a summary of certain PRC and Hong Kong tax consequences of the ownership of H Shares by foreign investors outside the PRC that purchases such Shares in connection with this Offering and holds the H Shares. According to the relevant PRC laws, H Shares are available for subscription only by foreign individuals and foreign enterprises. This summary does not purport to address all material tax consequences of the ownership of H Shares, and does not take into account the specific circumstances of any particular investors (such as tax-exempt entities, certain insurance companies, broker-dealers, investors liable for alternative minimum tax, investors that actually or constructively own 10% or more of the voting stock of the Company, or investors that hold H Shares as part of a straddle or a hedging or conversion transaction whose functional currency is not the US dollar), some of which may be subject to special rules. This summary is based on the tax laws of the PRC as in effect on the date hereof, as well as on the Agreement Between the United States of America and the People's Republic of China for the Avoidance of Double Taxation (the "PRC-US Treaty"), all of which are subject to changes (or changes in interpretation) from time to time, possibly with retroactive effect.

For purpose of this summary, a "US Holder" is any beneficial owner of H Shares that is (i) a citizen or resident of the United States, or (ii) a corporation organised under the laws of the United States which pays federal income taxation on a net income basis in respect of a Share. An "Eligible US Holder" is a US Holder that (i) is a resident of the United States for purposes of the Treaty, (ii) does not maintain a permanent establishment or fixed base in China to which H Shares are attributable and through which the beneficial owner carries on or has carried on business (or, in the case of an individual, performs or has performed independent personal services) and (iii) who is not otherwise ineligible for benefits under the Treaty with respect to income and gain derived in connection with the H Shares.

The discussion does not address any aspects of Hong Kong or PRC taxation other than income taxation, capital gains taxation, stamp duty and estate taxation. Prospective investors are urged to consult their tax advisers regarding the PRC, Hong Kong and other tax consequences of owning and disposing of H Shares.

Taxation of Dividends

PRC Taxation

Foreign Individual Investors. According to the Individual Income Tax Law of the PRC ("Individual Income Tax Law"), dividends paid by PRC companies to non-resident foreign individuals are normally subject to a withholding tax of 20% unless reduced by an applicable tax treaty. However, the PRC State Administration of Taxation (the "SAT", the PRC central government tax authority) issued, on 21st July, 1993, a Notice of the PRC State Administration of Taxation Concerning the Taxation of Income from Stock (Share Right) Transactions and Dividends Received by Foreign Investment Enterprises, Foreign Enterprises and Foreign Individuals ("Tax Notice") which states that dividends paid by a PRC company to individuals with respect to shares listed on an overseas stock exchange ("Overseas Shares"), such as H Shares, are temporarily exempted from PRC withholding tax. The relevant tax authority has not been collecting withholding tax on dividend payments on Overseas Shares since the promulgation of the Tax Notice.

In a letter dated 26th July, 1994 to the State Economic Restructuring Commission, the Securities Commission and the CSRC, the SAT reiterated the temporary tax exemption stated in the Tax Notice for dividends received by foreign individual investors on Overseas Shares. In the event that either this letter or the Tax Notice is withdrawn, a 20% tax may be withheld on dividends in accordance with the Individual Income Tax Law.

Foreign Corporate Investors. According to the Income Tax Law of the PRC for Enterprises with Foreign Investment and Foreign Enterprises ("Foreign Enterprise Income Tax Law"), dividends paid by PRC companies (other than Foreign Investment Enterprises ("FIEs")) to foreign enterprises with no permanent establishment in the PRC are ordinarily subject to a PRC withholding tax levied at a flat rate of 20%. Pursuant to the Notice of State Council on Tax Reduction on Foreign Enterprises' China-sourced Income issued in 2000, if a foreign enterprise does not have an establishment in the PRC or its China-sourced income has no connection with its establishment in the PRC, the applicable tax rate for the China-sourced income of the foreign enterprise is reduced to 10%. However, according to the Tax Notice, foreign enterprises with no permanent establishment in the PRC are temporarily exempted from the 10% withholding tax on receiving dividends paid on Overseas Shares.

Tax Treaties. Investors (for both individuals and enterprises), who do not reside in the PRC and reside in countries which have entered into double-taxation treaties with the PRC ("Treaty Countries"), may be entitled to a reduction of the withholding tax imposed on dividends to investors from Treaty Countries. The PRC has entered into double-taxation treaties with a number of countries, which include Australia, Canada, France, Germany, Japan, Malaysia, the Netherlands, Singapore, the United Kingdom and the United States.

Under the PRC-US Treaty, the PRC may tax a dividend paid by the Company to an Eligible US Holder up to a maximum of 10% of the gross amount of such dividend.

Hong Kong Taxation

No tax will be payable in Hong Kong in respect of dividends paid by the Company.

Taxation of Capital Gains

PRC Taxation

Foreign Individual Investors. As to individual holders of H Shares, the Detailed Rules for Implementation of Individual Income Tax Law of the PRC, issued on 28th January, 1994, stipulate that gains realised on the sale of shares are ordinarily subject to income tax at a rate of 20% of the gains. However, gains derived from the sale of Overseas Shares by individuals are temporarily exempted from individual income tax pursuant to the Tax Notice and another circular dated 30th March, 1998 issued by MOF and the SAT. In the event such temporary exemption is withdrawn or ceases to be effective, individual holders of H Shares may be subject to capital gains tax at the rate of 20%.

Foreign Corporate Investors. According to the Foreign Enterprise Income Tax Law, foreign enterprises are ordinarily subject to PRC withholding tax at 10% on gains derived from the sale of shares in PRC companies. However, the Tax Notice provides that gains realised by foreign enterprises from the sale of H Shares are temporarily exempted from capital gains taxes.

Tax Treaties. If tax on capital gains from the sale of H Shares becomes applicable, it is arguable that under the PRC-US Treaty, the PRC may only tax gains (1) derived from the sale or disposition by an Eligible US Holder of H Shares representing an interest in the Company of 25% or more or (2) on the basis that a US company's assets in the PRC primarily consist of real properties, but this position is uncertain and the PRC authorities may take a different position.

Hong Kong Taxation

No tax is imposed in Hong Kong in respect of capital gains from the sale of shares (such as the H Shares). However, trading gains from the sale of shares derived by persons carrying on a business in Hong Kong, where such gains are derived from or arise in Hong Kong from such business, will be chargeable to Hong Kong profits tax. Hong Kong tax is currently imposed at the rate of 16% on corporations and at a maximum rate of 15% on individuals. Gains from sales of the H Shares effected on the Stock Exchange will be considered to be derived from or arise in Hong Kong. Liability for Hong Kong profits tax would thus arise in respect of trading gains from sales of H Shares realised by persons carrying on a business of trading or dealing in securities in Hong Kong.

Additional PRC Tax Considerations

Stamp Duty

Generally speaking, PRC stamp tax is imposed on the transfer of shares of PRC publicly-traded companies under the Provisional Regulations Concerning Questions of Taxation on Enterprises Experimenting with the Share System and other relevant tax regulations. However, stamp duty is not levied on the acquisition and disposal by non-PRC investors of H Shares outside of the PRC. PRC stamp tax is imposed only on documents executed or received within the PRC which are legally binding in the PRC and are protected by PRC law.

Estate Tax

Currently, the PRC does not impose any estate tax on property passing on the death of individuals (whether PRC nationals or non-PRC nationals). It is uncertain whether the PRC will issue any laws in the future, imposing estate tax on non-PRC nationals holding H Shares.

Additional Hong Kong Tax Consideration

Stamp Duty

Hong Kong stamp duty will be payable by the purchaser on every purchase, and by the seller on every sale, of H Shares. The duty is charged at the ad valorem rate of HK$1.00 per HK$1,000 or part thereof of the consideration for, or (if greater) the market value of, the H Shares transferred (i.e., a total of HK$2.00 per HK$1,000 or part thereof is currently payable on a typical sale and purchase transaction of H Shares). In addition, a fixed duty of HK$5 is payable on an instrument of transfer of H Shares. Where one of the parties is resident outside of Hong Kong and does not pay the ad valorem duty due by it, the duty not paid will be assessed on the instrument of transfer (if any) and will be payable by the transferee.

Estate Duty

Estate duty is imposed upon the principal value of property situated in Hong Kong passing on the death of an individual. Estate duty is imposed on any individual who owns property situated in Hong Kong at the time of his or her death regardless of the citizenship, residence and domicile of that individual. H Shares are regarded as property situated in Hong Kong for estate duty purposes. Hong Kong estate duty is imposed on the principal value of a deceased's estate at graduated rates. In respect of individuals, no estate duty is payable where the principal value of the dutiable estate does not exceed HK$7.5 million; the maximum rate of 15% applies where the principal value exceeds HK$10.5 million.

TAXATION OF THE COMPANY BY THE PRC

Income tax

From 1st January, 1994, income tax payable by PRC domestic enterprises, including State-owned enterprises and share system enterprises, is governed by the PRC Corporate Income Tax Provisional Regulations ("EIT Regulations") which took effect as from 1st January, 1994, and which provide for an income tax rate of 33% unless a lower rate is provided by law, administrative regulations or State Council regulations. However, pursuant to the Provisions on Encouraging Investment in the Development of Hainan Island issued by the State Council on 4th May, 1988, the corporate income tax rate applicable to the Company is 15%.

For FIEs and foreign enterprises with establishments in the PRC, they are subject to the Enterprise Income Tax Law, which provides that the general tax rate is 33%, However, FIEs (including Sino-foreign joint ventures and wholly foreign owned enterprises) enjoy certain tax benefits under the Enterprise Income Tax Law and other relevant regulations in the PRC. Following the completion of the Offering, the Company will be eligible to apply for the status of a sino-foreign investment joint stock limited company. However, pursuant to the applicable laws rules and regulations in the PRC, no tax benefits will accrue to the Company upon acquiring such status.

Business tax

Pursuant to the Provisional Regulations of the PRC Concerning Business Tax, effective from 1st January, 1994 and the implementing rules, business tax is imposed on enterprises which provide taxable services, transfer intangible property or sell real estate in the PRC. The business tax is levied at a rate from 3% to 5% on the provision of taxable services, transfer of intangible property or sale of real estate in the PRC.

TAXATION OF THE COMPANY BY HONG KONG

The Directors do not consider that any of the Company's income or the income of its subsidiaries is derived from or arises in Hong Kong for the purpose of Hong Kong taxation. The Company should therefore not be subject to Hong Kong taxation.

FOREIGN EXCHANGE

The lawful currency of the PRC is the Renminbi, which is subject to foreign exchange controls and is not freely convertible into foreign exchange at this time. SAFE, under the authority of the PBOC, is empowered with the functions of administering all matters relating to foreign exchange, including the enforcement of foreign exchange control regulations.

Prior to 31st December, 1993, a quota system was used for the management of foreign currency. Any enterprise requiring foreign currency was required to obtain a quota from the local SAFE office before it could convert Renminbi into foreign currency through the PBOC or other designated banks. Such conversion had to be effected at the official rate prescribed by the SAFE on a daily basis. Renminbi could also be converted into foreign currency at swap centres. The exchange rates used by swap centres were largely determined by the demand for, and supply of, foreign currencies and the Renminbi requirements of enterprises in the PRC. Any enterprise that wished to buy or sell foreign currency at a swap centre first had to obtain the approval of SAFE.

On 28th December, 1993, the PBOC, under the authority of the State Council, promulgated the Notice Concerning Further Reform of the Foreign Currency Control System (the "Notice"), effective from 1st January, 1994. The Notice announced the abolition of the system of foreign exchange quotas, the implementation of conditional convertibility of Renminbi in current account items, the establishment of the system of settlement and payment of foreign exchange by banks, and the unification of the official Renminbi exchange rate and the market rate for Renminbi established at swap centres. On 26th March, 1994, the PBOC promulgated the "Provisional Regulations for the Settlement, Sale and Payment of Foreign Exchange" (the "Provisional Regulations"). The Provisional Regulations set out detailed provisions regulating the sale and purchase of foreign exchange by enterprises, economic organisations and social organisations in the PRC.

On 29th January, 1996, the State Council promulgated new Regulations of the People's Republic of China for the Control of Foreign Exchange ("Control of Foreign Exchange Regulations") which was effective from 1st April, 1996. The Control of Foreign Exchange Regulations classify all international payments and transfers into current account items and capital account items. Current account items are no longer subject to SAFE approval while capital account items still are. The Control of Foreign Exchange Regulations were subsequently amended on 14th January, 1997. This latest amendment affirmatively states that the State shall not restrict international current account payments and transfers.

On 20th June, 1996, the PBOC promulgated the "Regulations for Administration of Settlement, Sale and Payment of Foreign Exchange" (the "Settlement Regulations") which entered into effect on 1st July, 1996. The Settlement Regulations supersede the Provisional Regulations and abolish the remaining restrictions on convertibility of foreign exchange in respect of current account items while retaining the existing restrictions on foreign exchange transactions in respect of capital account items. On the basis of the Settlement Regulations, the PBOC also published the "Announcement on the Implementation of Foreign Exchange Settlements and Sales at Banks by Foreign-invested Enterprises" (the "Announcement"). The Announcement permits foreign-invested enterprises to open, on the basis of their needs, foreign exchange settlement accounts for current account receipts and payments of foreign exchange along with specialised accounts for capital account receipts and payments at designated foreign exchange banks.

On 25th October, 1998, the PBOC and SAFE promulgated the Notice Concerning the Discontinuance of Foreign Exchange Swapping Business, pursuant to which and with effect from 1st December, 1998, all foreign exchange swapping business in the PRC for foreign-invested enterprises shall be discontinued, while the trading of foreign exchange by foreign-invested enterprise shall come under the banking system for the settlement and sale of foreign exchange.

Since 1st January, 1994, the former dual exchange rate system for Renminbi has been abolished and replaced by a managed floating exchange rate system, which is determined by demand and supply. The PBOC sets and publishes daily the Renminbi-US dollar base exchange rate. This exchange rate is determined with reference to the transaction price for Renminbi-US dollar in the inter-bank foreign exchange market on the previous day. The PBOC will also, with reference to exchange rates in the international foreign exchange market, announce the exchange rates of Renminbi against other major currencies. In foreign exchange transactions, designated foreign exchange banks may, within a specified range, freely determine the applicable exchange rate in accordance with the exchange rate announced by the PBOC.

Save for foreign-invested enterprises or other enterprises which are specially exempted by relevant regulations, all entities in China (with the exception of certain foreign trade companies and production-type enterprises with import-export operation rights, which may be permitted to retain a certain amount of their foreign exchange income from their current account transactions and to use such monies to make foreign exchange payments for their current account transactions and permitted capital account transactions) must sell their foreign exchange income to designated foreign exchange banks. Foreign exchange income from loans issued by organisations outside the territory or from the issuance of bonds and shares (for example foreign exchange income received by the Company from the sale of shares overseas) is not required to be sold to designated foreign exchange banks, but may be deposited in foreign exchange accounts at the designated foreign exchange banks.

Chinese enterprises (including foreign-invested enterprises) which require foreign exchange for transactions relating to current account items, may, without the approval of SAFE, effect payment from their foreign exchange account or convert and pay at the designated foreign exchange banks, on the strength of valid receipts and proof. Foreign-invested enterprises which need foreign exchange for the distribution of profits to their shareholders, and Chinese enterprises which in accordance with regulations are required to pay dividends to shareholders in foreign exchange (like the Company), may on the strength of board resolutions on the distribution of profits and other relevant documents required, effect payment from their foreign exchange account or convert and pay at the designated foreign exchange banks.

Convertibility of foreign exchange in respect of capital account items, like direct investment and capital contribution, is still subject to restriction, and prior approval from SAFE and the relevant branch must be sought.

Dividends to holders of H Shares are fixed in Renminbi but must be paid in Hong Kong dollars.

This Appendix sets out summaries of PRC company and securities regulations, certain material differences between the Company Law and Hong Kong company law, additional regulatory provisions introduced by the Stock Exchange in relation to PRC joint stock limited companies and the Articles of Association. The main objective is to provide investors with an overview of the rights and obligations of shareholders of the Company and the principal legal and regulatory provisions applicable to the Company.

1. PRC LEGAL AND REGULATORY PROVISIONS

(A) Company Law

On 29th December, 1993, the Standing Committee of the Eighth NPC adopted the Company Law which came into effect on 1st July, 1994 and was amended on 25th December, 1999. Companies established under laws, administrative regulations, local laws and the Standard Opinion for Limited Liability Companies, and the Standard Opinion for Joint Stock Limited Companies formulated by the relevant departments of the State Council before the implementation of the Company Law will not be affected by the Company Law and shall continue to be recognised. Those companies which have not wholly complied with the provisions of the Company Law shall comply with the relevant requirements within a specified period of time. The State Council may separately promulgate detailed implementing measures.

Set out below is a summary of the major provisions of the Company Law, the Special Regulations and the Mandatory Provisions. On 4th July, 1994, the Special Regulations were passed at the Second Standing Committee Meeting of the State Council, and they were promulgated and implemented on 4th August, 1994. The Special Regulations are formulated according to the provisions of sections 85 and 155 of the Company Law in respect of the overseas share subscription and listing of joint stock limited companies. The Mandatory Provisions were issued jointly by CSRC and the State Economic Restructuring Commission on 27th August, 1994, prescribing provisions which must be incorporated into the articles of association of joint stock limited companies to be listed overseas. Accordingly, the Mandatory Provisions have been incorporated in the Articles of Association (which are summarised in this Appendix IX). References to a “company” are to a joint stock limited company established under the Company Law with overseas listed foreign invested shares.

Copies of the Chinese text of the Company Law, Special Regulations and the Mandatory Provisions together with copies of unofficial English translations thereof are available for inspection as mentioned in the section headed “Documents Delivered and Available for Inspection” in Appendix XI.

General

A “joint stock limited company” is a corporate legal person incorporated under the Company Law, whose registered capital is divided into shares of equal par value. The liability of its shareholders is limited to the extent of the Shares held by them, and the liability of the company is limited to the full amount of all the assets owned by it.

A state-owned enterprise that is restructured into a company must comply with the conditions and requirements specified by law and administrative regulations for the modification of its operation mechanisms, the systematic handling and evaluation of the company’s assets and liabilities and the establishment of internal management organs.

A company must conduct its business in accordance with the laws and professional ethics, promote the concept of a socialist market economy and be subject to the supervision of the government and the general public.

A company may invest in other limited liability companies and joint stock companies and the company’s liabilities with respect to such invested companies are limited to the amount invested. However, apart from investment companies and holding companies specified by the State Council, the amount of a company’s aggregate investment in other companies may not exceed 50% of its net assets.

Incorporation

A company may be incorporated by promotion or public subscription.

A company may be incorporated by a minimum of five promoters, but more than half of the promoters must have their places of residence within the PRC. According to the Special Regulations, state-owned enterprises or enterprises with the majority of their assets owned by the PRC government can be restructured in accordance with the relevant regulations to become joint stock limited companies which may issue shares to overseas investors. These companies if incorporated by public subscription may have less than five subscribers and can issue new shares once incorporated.

Companies incorporated by promotion are companies the entire registered capital of which is subscribed for by the promoters. Where companies are incorporated by public subscription, not less than 35% of their total shares must be subscribed for by the promoters and the remainder of their shares shall be offered to the public.

The registered capital of a company is the amount of its total paid-up capital as registered with the relevant administration for industry and commerce; the minimum registered capital of a company is RMB10 million. The total capital of a company which proposes to apply for its shares to be listed on a stock exchange must not be less than RMB50 million.

The establishment of a company must be approved by the department authorised by the State Council or by the provincial level people's government.

The promoters shall convene an inaugural meeting within 30 days after the issued shares have been fully paid up, and shall give notice to all subscribers or make an announcement of the date of the inaugural meeting 15 days before the meeting. The inaugural meeting may be convened only with the presence of shareholders holding shares representing more than 50% of the voting rights in the company. At the inaugural meeting, matters including the adoption of draft articles of association proposed by the promoter(s) and the election of the board of directors and the supervisory committee of the company will be dealt with. All resolutions of the meeting require the approval of subscribers with more than half of the voting rights present at the meeting.

Within 30 days after the conclusion of the inaugural meeting, the board of directors shall apply to the registration authority for registration of the establishment of the company. A company is formally established and has the status of a legal person after the approval of registration had been given by the relevant administration for industry and commerce and a business licence has been issued. Companies established by the public subscription method shall file a report on the offer of shares with the securities administration department of the State Council for record.

A company's promoters shall individually and collectively be liable for: (i) the payment of all expenses and liabilities incurred in the incorporation process if the company cannot be incorporated; (ii) the repayment of subscription monies to the subscribers together with interest at bank rates for a deposit of the same term if the company cannot be incorporated; and (iii) damages suffered by the company as a result of the default of the promoters in the course of incorporation of the company. According to the Provisional Regulations Concerning the Issue and Trading of Shares promulgated by the State Council on 22nd April, 1993 (which is only applicable to issue and trading of shares in the PRC and their related activities), if a company is established by means of subscription, the promoters of such company are required to assume joint responsibility for the accuracy of the contents of the prospectus and to ensure that the prospectus does not contain any misleading statement or omit any material information.

Share capital

The promoters may make capital contribution in cash, or in kind or by way of injection of assets, industrial property rights, non-patented technology or land use rights based on their appraised value. The amount of investment made in the form of industrial property rights and non-patented technology may not exceed 20% of the registered capital of the company.

If a capital contribution is made other than in cash, a valuation and verification of the property contributed must be carried out and converted into shares.

A company may issue registered or bearer share certificates. However, shares issued to promoters, state-authorised investment organisations and PRC legal persons shall be in the form of registered share certificates, and may not be registered under a different name or in the name of an agent.

The Special Regulations and the Mandatory Provisions provide that shares issued to foreign investors and listed overseas be issued in registered form and shall be denominated in Renminbi and subscribed for in foreign currency.

Under the Special Regulations and the Mandatory Provisions, shares issued to foreign investors and investors from the territories of Hong Kong, Macau and Taiwan and listed overseas are known as overseas listed foreign invested shares, and those shares issued to investors within the PRC other than the territories specified above are known as domestic invested shares.

A company may offer its shares to the public overseas with approval by the securities administration department of the State Council. Specific measures shall be specifically formulated by the State Council. Under the Special Regulations, upon approval of CSRC, a company may agree, in the underwriting agreement in respect of an issue of overseas listed foreign invested shares, to retain not more than 15% of the aggregate number of overseas listed foreign invested shares proposed to be issued after accounting for the number of underwritten shares.

The share offering price may be equal to or greater than the par value, but may not be less than par value.

The transfer by a shareholder of its shares must be carried out through a lawfully established stock exchange. Transfer of registered shares by a shareholder must be made by means of an endorsement or by other means stipulated by a law or by administrative regulations. Bearer share certificates are transferred by delivery of the certificates to the transferee.

Shares held by a promoter of a company may not be transferred for three years after the company's establishment. Directors, supervisors and the manager of a company shall not transfer the shares they hold in the company during their term of office. There is no restriction under the Company Law as to the percentage of shareholding a single shareholder may hold in a company. However, according to the Provisional Regulations concerning the Issue and Trading of Shares, a PRC individual shareholder cannot own more than 0.5% of the outstanding domestically issued common shares of a listed company.

Transfers of shares may not be entered in the register of shareholders within 30 days before the date of a shareholders' meeting or within five days before the record date set for the purpose of distribution of dividends.

Increase in capital

Under the Company Law, an increase in capital in a company by means of an issue of new shares must be approved by shareholders in general meeting and meet the following conditions:

(i) the previous issue of shares has been fully subscribed for and at least one year has elapsed since that issue, but under the Special Regulations, if a company increases its capital for the issue of overseas listed foreign invested shares, the time period elapsed since the last issue of shares may be less than 12 months;

(ii) the company has been profitable for the last three consecutive years and is able to make dividend payments to its shareholders;

(iii) there has been no false reporting in the company's financial and accounting documents during the last three years; and

(iv) the company's expected profit rate is comparable to the bank deposit rate for the same term.

Once the shareholders in general meeting have passed a resolution to issue new shares, the board of directors must apply to the authorised department of the State Council or to the provincial level people's government for approval. Public offers require the approval of the securities administration department of the State Council.

After payment in full for the new shares issued, a company must change its registration with the relevant administration for industry and commerce and issue a public notice accordingly.

Reduction of share capital

Subject to the minimum registered capital requirements, a company may reduce its registered capital in accordance with the following procedures prescribed by the Company Law:

(i) the company shall prepare a balance sheet and an inventory of assets;

(ii) the reduction of registered capital must be approved by shareholders in general meeting;

(iii) the company shall inform its creditors of the reduction in capital within 10 days and publish an announcement of the reduction in the newspaper at least three times within 30 days after the resolution approving the reduction has been passed;

(iv) the creditors of the company may within the statutory prescribed time limit require the company to pay its debts or provide guarantees covering the debts; and

(v) the company must apply to the relevant administration for industry and commerce for registration of the reduction in registered capital.

Repurchase of shares

A company may not purchase its own shares other than for the purpose of reducing its capital by cancelling its shares or merging with another company holding its shares or such other purposes permitted by law and administrative regulations. The Mandatory Provisions provide that upon obtaining approvals in accordance with the articles of association of the company and from the relevant supervisory authorities, a company may repurchase its issued shares for the foregoing purposes by way of a general offer to its shareholders or purchase on a stock exchange or an off-market contract.

Under the Company Law, within 10 days following the purchase of a company's own shares, a company must in accordance with applicable law and administrative regulations cancel that portion of its shares, change its registration and issue a public notice.

Transfer of shares

Shares may be transferred in accordance with the relevant laws and regulations.

A shareholder may only effect a transfer of its shares on a stock exchange established in accordance with law. Registered shares may be transferred after the shareholders endorse their signatures on the back of the share certificates or in any other manner specified by applicable laws and regulations.

Shares issued to promoters may not be transferred within three years after the establishment of the company. Shares held by directors, supervisors and the manager of a company may not be transferred during their term of office with the company.

There is no restriction under the Company Law as to the percentage shareholding of a single shareholder of a company.

Shareholders

Shareholders have such rights and obligations as set down in the articles of association of the company. The articles of association of a company are binding on each shareholder.

Under the Company Law, the rights of a shareholder include:

(i) to attend in person or appoint a proxy to attend shareholders' general meetings, and to vote in respect of the number of shares held;

(ii) to transfer his shares at a legally established stock exchange in accordance with the Company Law and the articles of association of the company;

(iii) to inspect the company's articles of association, minutes of shareholders' general meetings and financial and accounting reports and to make proposals or enquiries in respect of the company's operations;

(iv) if a resolution adopted by a shareholders' general meeting or the board of directors violates any law or administrative regulations or infringes the lawful rights and interests of shareholders, to institute an action in the People's Court demanding that the illegal infringing action be stopped;

(v) to receive dividends in respect of the number of shares held;

(vi) to receive surplus assets of the company upon its termination in proportion to his or her shareholding; and

(vii) any other shareholders' rights specified in the company's articles of association.

The obligations of a shareholder include the obligation to abide by the company's articles of association; to pay the subscription monies in respect of the shares subscribed for, to be liable for the company's debts and liabilities to the extent of the amount of subscription monies agreed to be paid in respect of the shares taken up by him and any other shareholders' obligation specified in the company's articles of association.

General meetings

The shareholders' general meeting is the organ of authority of the company, which exercises its powers in accordance with the Company Law.

The shareholders' general meeting exercises the following powers:

(i) to decide on the company's operational policies and investment plans;

(ii) to elect or remove the directors and decide on matters relating to the remuneration of directors;

(iii) to elect or remove the supervisors who are representatives of shareholders and decide on matters relating to the remuneration of supervisors;

(iv) to examine and approve reports of the board of directors;

(v) to examine and approve reports of the supervisory committee;

(vi) to examine and approve the company's proposed annual financial budget and final accounts;

(vii) to examine and approve the company's proposals for profit distribution and for recovery of losses;

(viii) to decide on any increase or reduction in the company's registered capital;

(ix) to decide on the issue of bonds by the company;

(x) to decide on issues such as merger, division, dissolution and liquidation of the company and other matters; and

(xi) to amend the articles of association of the company.

Shareholders' general meetings are required to be held once every year. An extraordinary shareholders' general meeting is required to be held within two months after the occurrence of any of the following circumstances:

(i) the number of directors is less than the number provided for in the Company Law or less than two-thirds of the number specified in the company's articles of association;

(ii) the aggregate losses of the company which are not made up reach one-third of the company's total share capital;

(iii) a request by shareholders holding 10% or more of the company's shares;

(iv) when deemed necessary by the board of directors; or

(v) when the supervisory committee proposes convening it.

Shareholders' general meetings shall be convened by the board of directors, and presided over by the chairman of the board of directors.

Notice of the meeting shall be given to all shareholders 30 days before the meeting under the Company Law and 45 days under the Special Regulations and the Mandatory Provisions, stating the matters to be considered at the meeting. Under the Special Regulations and the Mandatory Provisions, shareholders wishing to attend are required to give to the company written confirmation of their attendance 20 days prior to the meeting. Under the Special Regulations, at an annual general meeting of a company, shareholders holding 5% or more of the voting rights in the company are entitled to propose to the company in writing new resolutions to be considered at that meeting, which if within the powers of a shareholders' general meeting, are required to be added to the agenda of that meeting.

Shareholders present at a shareholders' general meeting have one vote for each share they hold.

Resolutions of the shareholders' general meeting must be adopted by more than half of the votes cast by shareholders present in person (including those represented by proxies) at the meeting, with the exception of matters relating to merger, division or dissolution of a company which must be adopted by shareholders with more than two-thirds of the voting rights held by shareholders present (including those represented by proxies) at the meeting. According to the Mandatory Provisions, the increase or reduction of share capital, the issue of bonds or debentures, and any other matters in respect of which the shareholders by ordinary resolution so decide, must be approved by more than two-thirds of the shareholders present in the general meeting. Amendments to the articles of association of a company must be approved by more than two-thirds of the shareholders present in general meeting.

Shareholders may appoint representatives to attend shareholders' general meetings by a written appointment document stating the scope of exercising the voting rights.

There is no specific provision in the Company Law regarding the number of shareholders constituting a quorum in a shareholders' meeting. However, the Special Regulations and the Mandatory Provisions provide that a company's annual general meeting may be convened when replies to the notice of that meeting from shareholders holding shares representing 50% of the voting rights in the company have been received 20 days before the proposed date, or if that 50% level is not achieved, the company shall within five days of the last day for receipt of the replies notify shareholders by public announcement of the matters to be considered at the meeting and the date and place of the meeting and the annual general meeting may be held thereafter. The Mandatory Provisions require class meetings to be held in the event of a variation or derogation of the class rights of a class. Holders of domestic invested shares and holders of overseas listed foreign invested shares are deemed to be different classes of shareholders for this purpose.

Directors

A company shall have a board of directors, which shall consist of five to nineteen members. Under the Company Law, each term of office of a director shall not exceed three years. A director may serve consecutive terms if re-elected.

Meetings of the board of directors shall be convened at least twice a year. Notice of meeting shall be given to all directors at least 10 days before the meeting. The board of directors may provide for a different method of giving notice and notice period for convening an extraordinary meeting of the board of directors.

Under the Company Law, the board of directors exercises the following powers:

(i) to convene the shareholders' general meeting and report on its work to the shareholders;

(ii) to implement the resolutions of the shareholders' general meeting;

(iii) to decide on the company's business plans and investment plans;

(iv) to formulate the company's proposed annual financial budget and final accounts;

(v) to formulate the company's proposals for profit distribution and for recovery of losses;

(vi) to formulate proposals for the increase or reduction of the company's registered capital and the issue of corporate bonds;

(vii) to prepare plans for the merger, division or dissolution of the company;

(viii) to decide on the company's internal management structure;

(ix) to appoint or dismiss the company's general manager, and based on the general manager's recommendation, to appoint or dismiss deputy general managers and financial officers of the company and to decide on their remuneration; and

(x) to formulate the company's basic management system.

In addition, the Mandatory Provisions provide that the board is also responsible for formulating the proposals for amendment of the articles of association of a company.

Meetings of the board of directors shall be held only if more than half of the directors are present. Resolutions of the board of directors require the approval of more than half of all directors.

If a director is unable to attend a board meeting, he may appoint another director by a written power of attorney specifying the scope of the authorisation to attend the meeting on his behalf.

If a resolution of the board of directors violates the laws, administrative regulations or the company's articles of association as a result of which the company sustains serious losses, the directors participating in the resolution are liable to compensate the company. However, if it can be proven that a director expressly objected to the resolution when the resolution was voted on, and that such objections were recorded in the minutes of the meeting, such director may be relieved of that liability.

Under the Company Law, the following persons may not serve as a director of a company:

(i) persons without civil capacity or with restricted civil capacity;

(ii) persons who have committed the offense of corruption, bribery, taking of property, misappropriation of property or destruction of the social economic order, and have been sentenced to criminal punishment, where less than five years have elapsed since the date of the completion of the sentence; or persons who have been deprived of their political rights due to criminal offence, where less than five years have elapsed since the date of the completion of implementation of this deprivation;

(iii) persons who are former directors, factory managers or managers of a company or enterprise which has become bankrupt and been liquidated due to mismanagement and who are personally liable for the bankruptcy of such company or enterprise, where less than three years have elapsed since the date of the completion of the bankruptcy and liquidation of the company or enterprise;

(iv) persons who were legal representatives of a company or enterprise which had its business licence revoked due to violation of the law and who are personally liable, where less than three years have elapsed since the date of the revocation of the business licence;

(v) persons who have a relatively large amount of debt due and outstanding; or

(vi) persons who are state civil servants.

Other circumstances under which a person is disqualified from acting as a director of a company are set out in the Mandatory Provisions (which have been incorporated in the Articles of Association, a summary of which is set out in this Appendix).

The board of directors shall appoint a chairman, who is elected with approval of more than half of all the directors. The chairman of the board of directors is the legal representative of the company and exercises, amongst others, the following powers:

(i) to preside over shareholders' general meetings and convene and preside over meetings of the board of directors;

(ii) to check on the implementation of the resolutions of the board of directors; and

(iii) to sign the company's share certificates and bonds.

The Special Regulations provide that a company's directors, supervisors, managers and other officers bear fiduciary duties and the duty to act diligently. They are required to faithfully perform their duties, protect the interests of the company and not to use their positions or power for their own benefit. The Mandatory Provisions (which have been incorporated into the Articles of Association, a summary of which is set out in this Appendix) contains further elaborations of such duties.

Supervisors

A company shall have a supervisory committee composed of not less than three members. Each term of office of a supervisor is three years and he or she may serve consecutive terms if re-elected.

The supervisory committee is made up of representatives of the shareholders and an appropriate proportion of representatives of the company's staff and workers. Directors, managers and financial officers may not act concurrently as supervisors.

The supervisory committee exercises the following powers:

(i) to review the company's financial position;

(ii) to supervise the directors and managers against violation of laws, regulations or the articles of association of the company in the performance of their duties;

(iii) when the acts of a director or manager are harmful to the company's interests, to require correction of those acts;

(iv) to propose the convening of extraordinary shareholders' general meetings; and

(v) other powers specified in the company's articles of association.

The circumstances under which a person is disqualified from being a director of a company described above apply mutatis mutandis to supervisors of a company.

As mentioned above, the Special Regulations provide that a company's supervisors, among other persons, shall bear fiduciary duties. They are required to faithfully perform their duties, protect the interests of the company and not to use their positions for their own benefit. A supervisor is also required to attend board meetings as a non-voting attendant.

Managers and officers

A company shall have a manager who shall be appointed or removed by the board of directors. The manager is accountable to the board of directors and may exercise the following powers:

(i) supervise the production, business and administration of the company and coordinate the implementation of resolutions of the board of directors;

(ii) coordinate the implementation of the company's annual business and investment plans;

(iii) formulate plans for the establishment of the company's internal management structure;

(iv) formulate the basic administration system of the company;

(v) formulate the company's specific rules;

(vi) recommend the appointment and dismissal of deputy managers and any financial controller and appoint or dismiss other administration officers (other than those required to be appointed or dismissed by the board of directors);

(vii) attend board meetings as a non-voting attendant; and

(viii) other powers conferred by the board of directors or the company's articles of association.

The Special Regulations and Mandatory Provisions provide that the other senior management of a company includes the financial controller, secretary of the board of directors and other executives as specified in the articles of association of the company.

The circumstances under which a person is disqualified from being a director of a company described above apply mutatis mutandis to managers and officers of the company.

The articles of association of a company shall have binding effect on the shareholders, directors, supervisors, managers and other senior management of the company. Such persons shall be entitled to exercise their rights, apply for arbitration and issue legal proceedings according to the articles of association of the company. The provisions of the Mandatory Provisions regarding the senior management of a company have been incorporated in the Articles of Association (a summary of which is set out in this Appendix).

Duties of directors, supervisors, managers and officers

A director, supervisor, manager and an officer of a company are required under the Company Law to comply with the relevant laws, regulations and the company's articles of association, carry out their duties honestly and protect the interests of the company. A director, supervisor, manager and an officer of a company is also under a duty of confidentiality to the company and is prohibited from divulging the secret information of the company save as permitted by the relevant laws and regulations or by the shareholders.

A director, supervisor, manager and an officer who contravenes any law, regulation or the company's articles of association in the performance of his duties which results in any loss to the company shall be personally liable to the company.

The Special Regulations and the Mandatory Provisions provide that a director, supervisor, manager and an officer of a company owe fiduciary duties to the company and are required to perform their duties faithfully and to protect the interests of the company and not to make use of their positions or power in the company for their own benefit.

Finance and accounting

A company shall establish its financial and accounting systems according to laws, administrative regulations and the regulations of the responsible financial department of the State Council and at the end of each financial year prepare a financial report which shall be audited and verified as provided by law.

A company shall deposit its financial statements at the company for the inspection by the shareholders at least 20 days before the convening of the annual general meeting of shareholders. A company established by the public subscription method must publish its financial statements.

When distributing each year's after-tax profits, the company shall set aside 10% of its after-tax profits for the company's statutory common reserve fund (except where the fund has reached 50% of the company's registered capital) and 5% to 10% of its after-tax profit for the company's statutory public welfare fund.

When the company's statutory common reserve fund is not sufficient to make up for the company's losses of the previous year, current year profits shall be used to make good the losses before allocations are set aside for the statutory common reserve fund or the statutory common welfare fund.

The company's statutory common welfare fund is used for the collective welfare of the company's staff and workers.

The shareholders in general meeting may resolve to transfer any amount from the after-tax profit of the company to the discretionary common reserve after transferring the requisite amount to the statutory common reserve fund.

After the company has made good its losses and made allocations to its statutory common reserve fund and statutory common welfare fund, the remaining profits are distributed in proportion to the number of shares held by the shareholders.

The common reserve of a company comprises the statutory common reserve, discretionary common reserve and the capital common reserve.

The capital common reserve of a company is made up of the premium over the nominal value of the shares of the company on issue and other amounts required by the relevant governmental authority to be treated as the capital common reserve.

The common reserve of a company shall be applied for the following purposes:

(i) to make up the company's losses;

(ii) to expand the business operations of the company; and

(iii) to pay up the registered capital of the company by the issue of new shares to shareholders in proportion to their existing shareholdings in the company or by increasing the par value of the shares currently held by the shareholders provided that if the statutory common reserve is converted into registered capital, the balance of the statutory common reserve after such conversion shall not be less than 25% of the registered capital of the company.

Appointment and retirement of auditors

The Special Regulations require a company to employ an independent PRC qualified firm of accountants to audit the company's annual report and review other financial reports.

The auditors are to be appointed for a term commencing from the close of an annual general meeting and ending at the close of the next following annual general meeting.

If a company removes or ceases to continue to appoint the auditors, it is required by the Special Regulations to give prior notice to the auditors and the auditors are entitled to make representations before the shareholders in general meeting. The appointment, removal or non re-appointment of auditors shall be decided by the shareholders and shall be registered with the CSRC.

Distribution of profits

The Special Regulations provide that the dividends and other distributions to be paid to holders of overseas listed foreign invested shares shall be declared and calculated in Renminbi and paid in foreign currency. Under the Mandatory Provisions, the payment of foreign currency to shareholders shall be made through a receiving agent.

Amendments to articles of association

Any amendments to the company's articles of association must be made in accordance with the procedures set forth in the company's articles of association. Any amendment of provisions incorporated in the articles of association in accordance with the Mandatory Provisions will only be effective after approval by the companies approval department authorised by the State Council and CSRC. In relation to matters involving the company's registration, its registration with the companies registration authority must also be changed.

Termination and liquidation

A company may apply for the declaration of insolvency by reason of its inability to pay debts as they fall due. After the People's Court has made a declaration of the company's insolvency, the shareholders, the relevant authorities and the relevant professionals shall form a liquidation committee to conduct the liquidation of the company.

Under the Company Law, a company shall be dissolved in any of the following events:

(i) the term of its operations set down in the company's articles of association has expired or events of dissolution specified in the company's articles of association have occurred;

(ii) the shareholders in general meeting have resolved to dissolve the company; or

(iii) the company is dissolved by reason of its merger or demerger.

Where the company is dissolved in the circumstances described in (i) or (ii) above, a liquidation committee must be established within 15 days. Members of the liquidation committee shall be appointed by the shareholders in the general meeting.

If a liquidation committee is not established within the stipulated period, the company's creditors can apply to the People's Court for its establishment.

The liquidation committee shall notify the company's creditors within 10 days after its establishment, and issue at least three public notices in the newspapers within 60 days. A creditor shall lodge his claim with the liquidation committee within 30 days after receiving notification, or within 90 days of the first public notice if he did not receive any notification.

The liquidation committee shall exercise the following powers during the liquidation period:

(i) to handle the company's assets and to prepare a balance sheet and an inventory of the assets;

(ii) to notify creditors or issue public notices;

(iii) to deal with and settle the relevant outstanding business of the company;

(iv) to pay any tax overdue;

(v) to settle financial claims and liabilities;

(vi) to handle the surplus assets of the company after its debts have been paid off; and

(vii) to represent the company in civil lawsuits.

If the company's assets are sufficient to meet its liabilities, they shall be applied towards the payment of the liquidation expenses, wages owed to the employees and labor insurance expenses, tax overdue and debts of the company. Any surplus assets shall be distributed to the shareholders of the company in proportion to the number of shares held by them.

A company shall not engage in new business operations during the liquidation period.

If the liquidation committee becomes aware that the company does not have sufficient assets to meet its liabilities, it must immediately apply to the People's Court for a declaration for bankruptcy. Following such declaration, the liquidation committee shall hand over all affairs of the liquidation to the People's Court.

Upon completion of the liquidation, the liquidation committee shall submit a liquidation report to the shareholders' general meeting or the relevant supervisory department for verification. Thereafter, the report shall be submitted to the companies registration authority in order to cancel the company's registration, and a public notice of its termination shall be issued.

Members of the liquidation committee are required to discharge their duties honestly and in compliance with relevant laws. A member of the liquidation committee is liable to indemnify the company and its creditors in respect of any loss arising from his wilful or material default.

Overseas listing

The shares of a company shall only be listed overseas after obtaining approval from the securities regulatory authority of the State Council and the listing must be arranged in accordance with procedures specified by the State Council.

According to the Special Regulations, a company's plan to issue overseas listed foreign invested shares and domestic invested shares which has been approved by the Securities Commission may be implemented by the board of directors of a company by way of separate issues, within 15 months after approval is obtained from CSRC.

Loss of share certificates

A shareholder may apply, in accordance with the relevant provisions set out in the PRC Civil Procedure Law, to a People's Court in the event that share certificates in registered form are either stolen or lost, for a declaration that such certificates will no longer be valid. After such a declaration has been obtained, the shareholder may apply to the company for the issue of replacement certificates.

The Mandatory Provisions provide for a separate procedure regarding loss of H share certificates (which has been incorporated in the Articles of Association, a summary of which is set out in this Appendix).

Suspension and termination of listing

The trading of shares of a company on a stock exchange may be suspended if so decided by the securities administration department of the State Council under one of the following circumstances:

(i) the registered capital or shareholding distribution no longer comply with the necessary requirements for a listed company;

(ii) the company failed to make public its financial position in accordance with the requirements or there is a false record in the company's financial report;

(iii) the company has committed a major breach of the law; or

(iv) the company has incurred losses for each of the preceding three years.

To the extent that a company has not fulfilled the listing requirements under the circumstances referred to in (ii) and (iii) above, where an investigation has revealed that the consequences are serious, or under the circumstances referred to in (i) and (iv) above, where the situation has not been rectified within the time stipulated, the securities administration department of the State Council may decide to terminate the listing of the company's shares.

The securities administration department of the State Council may also terminate the listing of a company's shares in the event that the company resolves to cease operations or is so instructed by its government supervisory body, or the company is declared bankrupt.

Merger and demerger

The merger or demerger of a company is to be decided by the shareholders in general meeting subject to the approval of departments authorised by the State Council or the approval of the provincial government.

Companies may merge through merger by absorption or through the establishment of a newly merged entity. If it merges by absorption, the company which is absorbed shall be dissolved. If it merges by forming a new corporation, both companies will be dissolved.

A merger agreement must be signed in the case of a merger of companies and the relevant companies shall prepare their respective balance sheets and a schedule of property. The companies should within 10 days of the resolution of the merger inform their respective creditors and publish a notice to the creditors in newspapers at least three times, within 30 days of the resolution to merge. Those creditors who had not received written notice may within 90 days of the first published notice, or within 30 days after receiving written notice, request the company to satisfy any unpaid debt or provide equivalent guarantees in cases of guarantees. Companies unable to repay such debts or provide alternative guarantees will not be allowed to merge. Newly merged entities shall be responsible for the debts and obligations of the companies involved in the merger.

When a company demerges into two companies, their respective assets must be severed and balance sheets and a schedule of property must be prepared.

When a company's shareholders approve the demerger of the company, the company should notify all its creditors within 10 days of such resolution being passed and advertise the same at least three times in newspapers within 30 days. A creditor may within 30 days after receiving written notice or, a creditor who has not received such notice may within 90 days from the first public advertisement, demand that the company repay any outstanding debts or provide an appropriate guarantee.

Changes in registrable particulars of the companies caused by merger or demerger must be registered in accordance with applicable laws.

Sino-Foreign Investment Joint Stock Limited Company and Sino-Foreign Joint Venture Law

The Company has not applied and does not intend to apply for the status of a sino-foreign investment joint stock limited company; and the Company is not and does not expect to be subject to the Sino-Foreign Joint Venture Law.

(B) Securities Law and Supervision

Since 1992, the PRC has promulgated a number of regulations in relation to the issue of and trading in securities and disclosure of information.

In early 1993, the State Council established the Securities Commission and CSRC. The Securities Commission is responsible for coordinating the drafting of securities regulations, formulating securities-related policies, planning the development of securities markets, directing, coordinating and supervising all securities-related institutions in the PRC and administering CSRC. CSRC is the regulatory arm of the Securities Commission and is responsible for the drafting of regulatory provisions governing securities markets, supervising securities companies, regulating public offers of securities by PRC companies in the PRC or overseas, regulating the trading of securities, compiling securities-related statistics and undertaking research and analysis. In early 1998, the State Council dissolved the Securities Commission, and the former functions of the Securities Commission were assumed by CSRC.

On 22nd April, 1993, the State Council promulgated the Provisional Regulations Concerning the Issue and Trading of Shares. These regulations deal with the application and approval procedures for public offerings of equity securities, trading in equity securities, the acquisition of listed companies, deposit, settlement, and transfer of listed equity securities, the disclosure of information with respect to a listed company, enforcement and penalties and dispute settlement. These regulations specifically provide that separate provisions will be promulgated in relation to the issue of and trading in special Renminbi-denominated shares. However, (i) if a PRC joint stock limited company proposes to issue Renminbi-denominated ordinary shares as well as special Renminbi-denominated shares, it has to comply with these regulations in respect of its issue of Renminbi-denominated ordinary shares; (ii) if a PRC company proposes to offer shares directly or indirectly outside the PRC, it will require the approval of the Securities Commission; and (iii) provisions of these regulations in relation to acquisitions of listed companies and disclosure of information are expressed to apply to listed companies in general without being confined to listed companies on any particular stock exchange.

Hence it is possible that such provisions may be applicable to joint stock limited companies with shares listed on a stock exchange outside the PRC including, for instance, joint stock limited companies with shares listed on the Stock Exchange, such as the Company.

On 12th June, 1993, pursuant to the Provisional Regulations Concerning the Issue and Trading of Shares, CSRC promulgated the Implementation Measures (Provisional) on Disclosure of Corporate Information for Public Offer of Shares. Pursuant to these measures, CSRC is responsible for supervising the disclosure of information by companies which have offered shares to the public both in the PRC and overseas. These measures contain provisions regarding prospectuses and listing reports to be issued in connection with a public offering of shares in the PRC, publication of interim and final reports and announcement of material transactions or matters by companies which have offered shares to the public. Material transactions or matters are those the occurrence of which may have a material effect on the share price of a company. They include, without limitation, changes to a company's articles of association or registered capital, removal of auditors, mortgage or disposal or retirement of major operating assets or writing down the value of such assets where the amount being written down exceeds 30% of the total value of such assets, revocation by a court of any resolution passed by the shareholders or the supervisors of a company and the merger or demerger of a company. These measures also contain disclosure provisions in relation to acquisition of listed companies which supplement the requirements contained in the Provisional Regulations Concerning the Issue and Trading of Shares.

On 2nd September, 1993, the Securities Commission promulgated the Provisional Measures Prohibiting Fraudulent Conduct relating to Securities. The prohibitions imposed by these measures include the use of insider information in connection with the issue of or trading in securities (insider information being defined to include undisclosed material information known to any insider, which may affect the market price of securities); the use of funds or information or the abuse of power in creating a false or disorderly market or influencing the market price of securities or inducing investors to make investment decisions without knowledge of actual circumstances; and the making of any statement in connection with the issue of and trading in securities which is false or materially misleading and in respect of which there is any material omission. Penalties imposed for contravening any of the provisions of the measures include fines, confiscation of profits and suspension of trading. In serious cases, criminal liability may be imposed.

On 25th December, 1995, the State Council promulgated the Regulations of the State Council Concerning the Domestic Listed Foreign Shares of Joint Stock Limited Companies. These regulations deal mainly with the issue, subscription and trading of, and declaration of dividends and other distributions on, domestic listed Foreign Shares and disclosures of information by joint stock limited companies having domestic listed Foreign Shares.

On 29th December, 1998, the Standing Committee of the National People's Congress promulgated the Securities Law of the PRC. This is the first national securities law in the PRC and is the fundamental law comprehensively regulating activities such as the issuance and trading of securities in the PRC securities market. The Securities Law became effective on

1st July, 1999. The Securities Law is applicable to the issuance and trading in the PRC of shares, company bonds and other securities designated by the State Council according to law. Where the Securities Law does not apply, the provisions of the Company Law and other applicable laws and administrative regulations regarding securities will apply.

On 29th March, 1999, SETC and CSRC promulgated the Opinion on the Further Promotion of the Regular Operation and In-Depth Reform of Companies Listed Overseas, which is aimed at regulating the internal operation and management of PRC companies listed overseas. The Company will be subject to the Opinion upon listing of the H Shares on the Stock Exchange. The Opinion regulates, amongst others, the appointments and functions of external directors and independent directors in the board of directors; and the appointment and functions of external supervisors and independent supervisors in the supervisory committee.

(C) The Arbitration Law

The Arbitration Law of the PRC (the "Arbitration Law") was promulgated by the Standing Committee of the NPC on 31st August, 1994 and came into effect on 1st September, 1995. It is applicable to, among other matters, trade disputes involving foreign parties where the parties have entered into a written agreement to refer the matter to arbitration before an arbitration committee constituted in accordance with the Arbitration Law. Under the Arbitration Law, an arbitration committee may, before the promulgation by the PRC Arbitration Association of arbitration regulations, formulate interim arbitration rules in accordance with the Arbitration Law and the PRC Civil Procedure Law. Where the parties have by agreement provided arbitration as a method for dispute resolution, the parties are not permitted to institute legal proceedings in a People's Court except when the arbitration agreement is not valid.

The Listing Rules and the Mandatory Provisions require an arbitration clause to be included in the articles of association of a company listed in Hong Kong and in the case of the Listing Rules, also in a contract between the company and each director and supervisor, to the effect that whenever any dispute or claim arises from any rights or obligations provided in the Articles of Association, the Company Law and other relevant laws and administrative regulations concerning the affairs of a company between (i) a holder of overseas listed Foreign Shares and the company; (ii) a holder of overseas listed Foreign Shares and a holder of Domestic Shares, unless otherwise specified in the Articles of Association, such parties shall submit that dispute or claim to arbitration before either the China International Economic and Trade Arbitration Commission ("CIETAC") or the Hong Kong International Arbitration Centre ("HKIAC") for arbitration. If the party seeking arbitration elects to arbitrate the dispute or claim at the HKIAC, then either party may apply to have such arbitration conducted in Shenzhen according to the securities arbitration rules of the HKIAC. CIETAC is an economic and trade affairs arbitration organ in the PRC. Pursuant to the China International Economic and Trade Arbitration Commission Arbitration Rules, effective on 10th May, 1998, CIETAC's jurisdiction covers disputes relating to the Hong Kong Special Administrative Region. CIETAC is located in Beijing with branches in Shenzhen and Shanghai.

Under the Arbitration Law, an arbitral award is final and binding on the parties and if a party fails to comply with an award, the other party to the award may apply to the People's Court for enforcement. A People's Court may refuse to enforce an arbitral award made by an arbitration commission if there are certain procedural or membership irregularities or the award exceeds the scope of the arbitration agreement or is outside the jurisdiction of the arbitration commission.

A party seeking to enforce an arbitral award of a foreign affairs arbitration organ of the PRC against a party who or whose property is not within the PRC may apply to a foreign court with jurisdiction over the case for enforcement. Similarly, an arbitral award made by a foreign arbitration body may be recognised and enforced by the PRC courts in accordance with the principles of reciprocity or any international treaty concluded or acceded to by the PRC. The PRC acceded to the New York Convention adopted on 10th June, 1958 pursuant to a resolution of the Standing Committee of the NPC passed on 2nd December, 1986. The New York Convention provides that all arbitral awards made by a state which is a party to the New York Convention shall be recognised and enforced by other parties to the New York Convention subject to their right to refuse enforcement under certain circumstances including where the enforcement of the arbitral award is against the public policy of the state to which the application for enforcement is made. It was declared by the Standing Committee of the NPC simultaneously with the accession of the PRC that (1) the PRC will only recognise and enforce foreign arbitral awards on the principle of reciprocity and (2) the PRC will only apply the New York Convention in disputes considered under PRC laws to be arising from contractual and non-contractual mercantile legal relations. Following the resumption of sovereignty over Hong Kong by the PRC on 1st July, 1997, the New York Convention no longer applies to the enforcement of Hong Kong arbitration awards in other parts of the PRC. A Memorandum of Understanding on the arrangement for reciprocal enforcement of arbitral awards between Hong Kong and China has been signed on 21st June, 1999. The new arrangement is made in accordance with the spirit of the New York Convention. To meet present day's needs, it will allow awards made by over 100 China arbitral authorities with relevant experience to be enforced in Hong Kong. Under the agreed arrangement, Hong Kong arbitration awards will also be enforceable in China. This new arrangement has been approved by the Hong Kong Legislative Council and will become effective once the Supreme People's Court of the PRC promulgates a related judicial interpretation.

2. HONG KONG LEGAL AND REGULATORY PROVISIONS

(A) Hong Kong company law and its comparison with the PRC law applicable to a joint stock limited company incorporated under the Company Law

Hong Kong company law is primarily set out in the Companies Ordinance (Chapter 32 of the Laws of Hong Kong) (the "Companies Ordinance") and supplemented by common law. There are material differences between Hong Kong company law and the PRC law applicable to a joint stock limited company incorporated under the Company Law, to which the Company is and will be subject, particularly in the area of investor protection. Certain material differences between the Company Law and Hong Kong company law are summarised below. This summary, however, is not intended to be an exhaustive comparison. It should also be noted that the summary relates only to joint stock limited companies incorporated under the Company Law.

Derivative action by minority shareholders

Hong Kong law allows minority shareholders to start a derivative action on behalf of the general body of shareholders in cases where, for example, one or more of the directors are in breach of duty and where their actions are shielded by the majority shareholders. The PRC Civil Procedure Law does not provide for such a procedure. Although the Company Law gives (a) shareholder(s) of a company the right to initiate petitions in the People's Court to restrain any resolution adopted by shareholders in general meeting or at a meeting of the board of directors which is in violation of any law or infringes the lawful rights and interests of the shareholder(s), there is no form of proceedings which is the same as a derivative action under the Companies Ordinance. However, each of the Directors and Supervisors (as required by the Listing Rules) has given a written undertaking to the Company (acting as agent for each shareholder) to observe and comply with his obligations to shareholders stipulated in the Articles of Association. This allows minority shareholders to commence direct actions against defaulting Directors.

Remedies of the Company

Under the Company Law, if a director, supervisor or manager in carrying out his duties infringes any law or administrative regulation or the articles of association of a company, resulting in damage to the company, that director, supervisor or manager should be responsible to the company for such damages. In addition, in compliance with the Listing Rules, remedies of the Company similar to those available under Hong Kong law (including rescission of the relevant contract and recovery of profits made by a Director, Supervisor or officer) have been set out in the Articles of Association.

Directors, officers and supervisors

The Company Law provides for the disqualification of directors, supervisors and managers in circumstances where they enter into business contracts with the Company, and for prohibitions of certain unauthorised benefits, but contains no provision restricting the authority of the directors to make major dispositions or prohibiting payment to them for loss of office without shareholders' approval. The Company Law, unlike Hong Kong company law, does not contain restrictions on directors' authority in making major dispositions, restrictions on companies providing certain benefits such as loans to directors and guarantees in respect of directors' liability and prohibitions against compensation for loss of office without shareholders' approval. Neither does the Company Law contain any requirements relating to the declaration of material interests in contracts with the Company as is required under Hong Kong company law, nor restrictions on interested directors being counted towards the quorum of, and voting at, a meeting of the board of directors at which a transaction in which a director is interested is being considered. However, the Mandatory Provisions contain certain restrictions on major dispositions and specify the circumstances under which a director may receive compensation for loss of office, all of which provisions have been incorporated in the Articles of Association, a summary of which is set out in this Appendix.

Under Hong Kong company law, there is no concept of a supervisory committee for a company in addition to its board of directors, but a PRC joint stock limited company must have supervisors whose main duties include monitoring the compliance with laws and regulations, and the articles of association of the company, by its directors and managers.

Each supervisor owes a duty, in the exercise of his powers, to act in good faith and honestly in what he or she considers to be the best interests of the company and to exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

Minority protection

Under Hong Kong law, a shareholder who complains that the affairs of a company incorporated in Hong Kong are conducted in a manner unfairly prejudicial to his interests may present a petition to the court either to wind up the company or to make an appropriate order regulating the affairs of the company. In addition, at an application of a specified number of members, the financial secretary may appoint investigators who are given extensive statutory powers to investigate the affairs of a company incorporated in Hong Kong. There is no specific provision in the Company Law to guard against oppression by the majority shareholders of minority shareholders but the Company, as required by the Mandatory Provisions and the Listing Rules, has adopted in the Articles of Association minority protection provisions similar to (though not as comprehensive as) those available under Hong Kong law, to the effect that a controlling shareholder may not exercise its voting rights in a manner prejudicial to the interests of other shareholders to relieve a director or supervisor of his or her duty to act honestly in the best interests of the company or to approve the expropriation by a director or supervisor of the company's assets or the individual rights of other shareholders.

Receiving agent

Under both PRC and Hong Kong law, dividends once declared become debts payable to shareholders, but the limitation of action period is two years in the PRC as opposed to six years in Hong Kong. The Articles of Association provide for the appointment of an agent in Hong Kong which must be a trust corporation registered under the Trustee Ordinance in Hong Kong to receive all dividends payable to H Share holders and all other monies owing by a joint stock limited company in respect of such H Shares on behalf of such shareholders as required by the Listing Rules.

Financial assistance for the acquisition of shares

The Company Law does not contain any provision prohibiting or restricting a joint stock limited company or its subsidiaries from providing financial assistance for the purpose of an acquisition of its own or its holding company's shares. The Mandatory Provisions contain certain restrictions on a company and its subsidiaries providing such financial assistance similar to those under Hong Kong company law.

Variation of class rights

The Company Law makes no specific provision relating to variation of class rights. However, the Company Law states that the State Council can promulgate regulations relating to other kinds of shares. The Mandatory Provisions contain elaborate provisions relating to the circumstances which are deemed to be variations of class rights and the approval procedures required to be followed in respect thereof. These provisions have been incorporated in the Articles of Association, which are summarised in this Appendix. Under the Companies Ordinance, no rights attached to any class of shares can be varied except with the approval of a special resolution of the holders of the relevant class at a separate meeting or the consent in writing of the holders of three-fourths in nominal value of the issued shares of the class in question or by agreement of all the members of the Company or if there are provisions in the articles of association relating to the variation of those rights, then in accordance with those provisions. The Company (as required by the Listing Rules and the Mandatory Provisions) has adopted in the Articles of Association provisions protecting class rights in a similar manner to those found in Hong Kong law. Holders of overseas listed foreign invested shares and domestic invested shares are defined in the Articles of Association as different classes, except where (i) the Company issues and allots, in any 12-month period, pursuant to a class shareholders' resolution, not more than 20% of each of the issued overseas listed foreign invested shares and the issued domestic invested shares existing as at the date of the shareholders' special resolution; and (ii) the plan for the issue of domestic invested shares and listed foreign invested shares upon its establishment is implemented within 15 months following the date of approval by the Securities Commission. The Mandatory Provisions contain detailed provisions relating to circumstances which are deemed to constitute a variation of class rights.

Corporate restructurings

Corporate restructurings involving compromises with creditors and members in respect of Hong Kong incorporated companies are dealt with under section 166 of the Companies Ordinance and require court sanction. Corporate restructuring involving Hong Kong incorporated companies may also be effected by the transfer of the whole or part of the business or property of the company in the course of being wound up voluntarily to another company pursuant to section 237 of the Companies Ordinance. For PRC companies, such restructurings are administratively considered and sanctioned under the Company Law.

Share capital

For a joint stock limited company formed under the Company Law, the registered share capital and the issued share capital are the same. For a Hong Kong company, the authorised share capital may be larger than the issued share capital. Hence, the directors of a Hong Kong company may, with the prior approval of the shareholders if required, cause the company to issue new shares. In the case of a PRC company, any increase of the registered capital must be approved by the shareholders in general meeting and the relevant PRC government and regulatory authorities. After completion of an approved new issue, the company has to register the increase in share capital with the relevant administration for industry and commerce.

The minimum registered capital of a company established under the Company Law which has applied for the listing of its shares on a stock exchange is RMB50 million. Hong Kong law does not prescribe any minimum capital requirements for a Hong Kong company.

Under the Company Law, the shares subscribed for in the form of intangible assets (excluding land use rights) may not exceed 20% of a joint stock limited company's registered capital. There is no such restriction under Hong Kong law on a Hong Kong company.

Restriction on shareholding and transfer of shares

The Company Law makes no reference to the class of shares which may be subscribed for or traded by overseas investors but has provisions that shares of a company to be listed overseas must comply with the Special Regulations. The Special Regulations and the Mandatory Provisions provide, among other things, that H shares must be in registered form and include other matters some of which are referred to above. There is no restriction under Hong Kong law on a person's ability to deal in shares in a Hong Kong company on the basis of his residence or nationality.

Under the Company Law, shares in a joint stock limited company held by its promoters, directors or managers may not be transferred within certain periods of time. There is no such restriction under Hong Kong law.

Notice of meetings

Under the Company Law, shareholders of a joint stock limited company must be given 30 days' notice of a general meeting or, in the case of bearer shares, such notice should be published 45 days before the meeting. Under the Special Regulations and the Mandatory Provisions, 45 days' written notice must be given to all shareholders, and shareholders wishing to attend the meeting must reply in writing to reach the company 20 days before the date of the meeting. For a Hong Kong limited company, the minimum period of notice of a general meeting where convened for the purpose of considering ordinary resolutions is 14 days and where convened for the purpose of considering special resolutions is 21 days. The notice period for an annual general meeting is also 21 days.

Quorum

Under Hong Kong company law, any two shareholders personally present will constitute a quorum for a general meeting, unless the articles of association provide otherwise. The Company Law makes no specific provision as to when a quorum is regarded as being present but the Special Regulations and the Mandatory Provisions provide that a company's annual general meeting can be convened when replies to the notice of that meeting have been received from shareholders whose shares represent 50% of the voting rights in the company at least 20 days before the proposed date of the meeting, or if that 50% level is not achieved, that the company shall within five days notify shareholders in a public announcement and the annual general meeting may be held thereafter.

Voting

Under the Hong Kong company law, ordinary resolutions are passed by more than one-half of the votes cast by those shareholders voting in person or by proxy at a general meeting and special resolutions are passed by not less than three-quarters of such votes. Under the Company Law, the passing of any resolution requires the passing by more than half of the votes of the shareholders attending and voting except in cases of proposed amendment to the articles of association, merger, division or dissolution of a company, where the approval of a two-thirds majority is required.

Dividends

The Articles of Association empower the Company to withhold, and pay to the relevant tax authorities, any tax payable under PRC law on any dividends or other distributions payable to a shareholder. Under Hong Kong law, the limitation period for an action to recover a debt (including the recovery of dividends) is six years, whereas under PRC laws, the relevant limitation period is two years.

Financial disclosure

A joint stock limited company is required under the Company Law to make available at its office for inspection by shareholders its annual balance sheet, profit and loss account, statement of changes in financial situation and other relevant annexes 20 days before the annual general meeting of shareholders. In addition, a company established by the public subscription method under the Company Law must publish its financial statements. The annual balance sheet has to be verified by registered accountants. The Companies Ordinance requires a company to send to every shareholder a copy of its balance sheet, auditors' report and directors' report which are to be laid before the company in its annual general meeting not less than 21 days before such meeting.

Under the Articles of Association (as required by the Listing Rules and the Mandatory Provisions), in addition to preparing accounts according to PRC accounting standards, the Company must have its accounts prepared and audited in accordance with international accounting standards or Hong Kong accounting standards. The Company is further required to publish its interim and annual accounts within 60 days from the end of the first six months of a financial year and within 120 days from the end of a financial year, respectively.

The Special Regulations require that there should not be any inconsistency between the information disclosed within and outside the PRC and that, to the extent that there are differences in the information disclosed in accordance with the relevant PRC and overseas laws, regulations and requirements of the relevant stock exchanges, such differences should also be disclosed simultaneously.

Information on directors and shareholders

The Company Law gives shareholders the right to inspect the Company's Articles of Association, minutes of the shareholders' general meetings and financial and accounting reports. Under the Articles of Association, shareholders have the right to inspect and copy (at reasonable charges) certain information on shareholders and on directors similar to that available to shareholders of Hong Kong companies under Hong Kong law.

Arbitration of disputes

In Hong Kong, disputes between shareholders and a company or its directors, managers and other senior officers can be resolved through the courts. The Articles of Association provide that disputes between a holder of H Shares and the Company and its directors, managers or other senior officers or a holder of Domestic Shares arising from the Articles of Association, the Company Law or other relevant law or administrative regulation which concerns the affairs of the Company must, with certain exceptions, be submitted to arbitration at either HKIAC or CIETAC, at the claimant's choice. Such arbitration is final and conclusive.

Mandatory Deductions

Under the Company Law, after tax profits of a company are subject to deductions of contributions to the statutory common reserve fund and the statutory public welfare fund of a company before they can be distributed to shareholders. There are prescribed limits under the Company Law for such deductions. There are no corresponding provisions under the Companies Ordinance.

Fiduciary Duties

In Hong Kong, there is the common law concept of the fiduciary duty of directors. Under the Company Law and the Special Regulations, directors, supervisors, officers, and managers owe a fiduciary duty towards their company and are not permitted to engage in any activities which compete with or damage the interests of their company.

Closure of register of shareholders

The Companies Ordinance requires that the register of shareholders of a company must not generally be closed for the registration of transfers of shares for more than 30 days (extendable to 60 days in certain circumstances) in a year, whereas the Company's Articles of Association provide, as required by the Company Law, that share transfers may not be registered within 30 days before the date of a shareholders' meeting or within five days before the record date set for the purpose of distribution of dividends.

(B) Other legal and regulatory provisions

Upon the listing of the Company on the Stock Exchange, the provisions of the Securities Ordinance, the Securities (Disclosure of Interests) Ordinance, the Securities (Insider Dealing) Ordinance of Hong Kong, the Takeovers Code and the Share Repurchases Code and such other relevant ordinances and regulations as may be applicable to companies listed on the Stock Exchange will apply to the Company.

(C) Securities Arbitration Rules

The Articles of Association provide that certain claims arising under the Articles of Association or the Company Law shall be arbitrated at either CIETAC or HKIAC in accordance with their respective rules.

The Securities Arbitration Rules of HKIAC contain provisions allowing an arbitral tribunal to conduct a hearing in Shenzhen for cases involving disputes concerning the affairs of companies listed by the Stock Exchange and incorporated in the PRC (other than Hong Kong, Macau and Taiwan) so that PRC parties and witnesses may attend. Where any party applies for a hearing to take place in Shenzhen, the tribunal shall, where satisfied that such application is based on bona fide grounds, order the hearing to take place in Shenzhen conditionally upon all parties including witnesses and the arbitrators being permitted to enter Shenzhen for the purpose of the hearing. Where any party (other than a PRC party) or any of its witnesses or any arbitrator is not permitted to enter Shenzhen, then the tribunal shall order that the hearing be conducted in any practicable manner, including the use of electronic media. For the purpose of the Securities Arbitration Rules, a PRC party means a party domiciled in the PRC other than the territories of Hong Kong, Macau and Taiwan.

(D) Listing Rules

The Listing Rules contain certain provisions specifically relating to the primary listing of equity securities of companies incorporated or otherwise established in the PRC. Set out below is a summary of the major provisions which apply to the Company.

Sponsor

The Company is required to retain, for at least one year (or such shorter period as the Stock Exchange may, at its absolute discretion, permit) following its listing, the services of its sponsor or other financial adviser or professional firm which is acceptable to the Stock Exchange, to provide the Company with professional advice on continuous compliance with the Listing Rules and its listing agreement, and to act at all times as the Company's principal channel of communication with the Stock Exchange, in addition to the two authorised representatives of the Company appointed pursuant to the Listing Rules.

The Company must ensure that its sponsor has access at all times to its authorised representatives, Directors and other officers and is given such information and assistance as it may request in connection with the performance of its duties. The Company should also ensure that there are adequate and efficient means of communication between itself, its authorised representatives, Directors and other officers and the sponsor and should keep the sponsor fully informed of all communications and dealings between it and the Stock Exchange. The Company must not terminate the services of its sponsor until a replacement acceptable to the Stock Exchange is appointed. Where such sponsor's role is terminated by the Company, both the Company and the former sponsor should immediately notify the Stock Exchange of such termination, in each case stating the reason why such appointment was terminated, and the Company and the new sponsor should immediately notify the Stock Exchange of the new sponsor's appointment.

If the Stock Exchange is not satisfied that the sponsor is fulfilling its responsibilities adequately under the Listing Rules, it may require the Company to terminate the sponsor's appointment and appoint a replacement as soon as possible. The Company and the new sponsor should immediately notify the Stock Exchange of the new sponsor's appointment.

The sponsor must be satisfied that the Company is suitable to be listed, that the Directors and the Supervisors appreciate the nature of their responsibilities and can be expected to honor their obligations under their respective undertakings, the Listing Rules, the listing agreement and applicable laws and regulations and that the Directors understand what is required of them under the Listing Rules, the listing agreement and applicable laws and regulations.

The sponsor must keep the Company informed on a timely basis of changes in the Listing Rules and any new or amended law, regulation or code in Hong Kong applicable to the Company. The sponsor must provide advice to the Company on the continuing requirements under the Listing Rules, the listing agreement and applicable laws and regulations. It must act as the Company's principal channel of communication with the Stock Exchange if the authorised representatives of the Company are expected to be frequently outside Hong Kong.

Accountants reports

An accountants' report will not normally be regarded as acceptable by the Stock Exchange unless the relevant accounts have been audited to a standard comparable to that required in Hong Kong which means that it must conform with either Hong Kong or international accounting standards.

Process agent

The Company must appoint and maintain throughout the period its securities are listed on the Stock Exchange the appointment of a person authorised to accept service of process and notices on its behalf in Hong Kong and must notify the Stock Exchange of his or her appointment and any termination of his or her appointment and his or her contact particulars.

Public shareholdings

If at any time there are existing issued securities of the Company other than H Shares which are listed on the Stock Exchange, the Listing Rules require that (i) all H Shares must be held by the public except as otherwise permitted by the Stock Exchange in its discretion; (ii) the H Shares held by the public must constitute not less than 10% of the Company's total existing issued share capital; and (iii) the aggregate amount of H Shares and other securities held by the public must constitute not less than 25% of the Company's total existing issued share capital.

If the Company does not have existing issued securities other than H Shares, the H Shares held by the public must constitute not less than 25% of the Company's total existing issued share capital unless the expected market value of the H shares at the time of listing is over HK$4,000 million in which case, the Stock Exchange will normally accept a prescribed percentage of H Shares (as a portion of total existing issued share capital) to be held by the public of between 10 and 25% as the number of securities concerned will normally be sufficient to ensure that there is an open market.

Independent non-executive directors and supervisors

The independent non-executive Directors are required to demonstrate an acceptable standard of competence and adequate commercial or professional expertise to ensure that the interests of the general body of shareholders will be adequately represented. At least one of the independent non-executive Directors must be ordinarily resident in Hong Kong. The Supervisors must have the character, experience and integrity and be able to demonstrate a standard of competence commensurate with their position as supervisors.

Restrictions on purchase and subscription

The Company may purchase its own Shares on the Stock Exchange in accordance with the Listing Rules. Shareholders' approvals must first be obtained prior to carrying out a share repurchase, by way of the special resolutions of shareholders in general meetings and of the holders of Domestic Shares and the holders of H Shares at separate class meetings, in accordance with the procedures prescribed by the Articles of Association. When seeking shareholders' approval to make purchases of its securities on the Stock Exchange or when reporting such purchases, the Company should provide information to its shareholders on the proposed or actual purchase of any or all of its equity securities, whether or not listed or traded on the Stock Exchange. There should also be a statement as to the consequences of any purchases which will arise under either or both of the Hong Kong Code on Takeovers and Mergers and any similar applicable law of which the Directors are aware, if any. Any specific approval or general mandate given to the Directors to repurchase H Shares must not exceed 10% of the total amount of existing issued H Shares of the Company.

With a view to increasing the level of protection afforded to investors, the Stock Exchange requires the incorporation, in the articles of association of a PRC company whose primary listing is on the Stock Exchange, of the Mandatory Provisions and provisions including those relating to the change, removal and resignation of auditors, classification of shareholders and the conduct of the supervisory committee of the Company. Such provisions have been incorporated into the Articles of Association, a summary of which is set out in this Appendix.

Listing agreement

The Company's listing agreement with the Stock Exchange is in substantially the same form as the listing agreement for an overseas company seeking a listing on the Stock Exchange, subject to certain modifications and additional requirements which may be summarised as follows:

(1) Redeemable shares

The Company shall not issue any redeemable shares unless the Stock Exchange is satisfied that the relative rights of the holders of the H Shares are adequately protected. The Company shall inform the Stock Exchange as soon as possible after any purchase, sale, drawing or redemption by the Company, or any of its subsidiaries, of its securities.

(2) Preemptive rights

Except in the circumstances mentioned below, the Directors must obtain the approval by a special resolution of Shareholders in general meeting, and the approvals by special resolutions of holders of Domestic Shares and holders of H Shares (each being otherwise entitled to vote at general meetings) at separate class meetings conducted in accordance with the Articles of Association prior to:

(i) authorising, allotting, issuing or granting;

(a) shares;

(b) securities convertible into shares; or

(c) options, warrants or similar rights to subscribe for any shares or such convertible securities; or

(ii) any major subsidiary of the Company making any such authorisation, allotment, issue or grant so as materially to dilute the percentage equity interest of the Company and its shareholders in such subsidiary.

Notwithstanding in the circumstances mentioned below, the Directors shall obtain the approval by special resolution of the Shareholders in general meeting prior to allotting any voting shares if such allotment would effectively alter the control of the Company.

No such approval shall be required in the case of authorising, allotting or issuing shares if, but only to the extent that, the existing shareholders of the Company have by special resolution in general meeting given approval, either unconditionally or subject to such terms and conditions as may be specified in the resolution, for the Company to authorise, allot or issue either separately or concurrently once in every 12 months (commencing on the date on which the Shareholders pass such resolutions), not more than 20% of each of the existing Domestic Shares and H Shares as at the date of the passing of the relevant special resolution or such shares are part of the Company's plan at the time of its establishment to issue Domestic Shares and H Shares and which plan is implemented within 15 months from the date of approval by the State Council Securities Policy Committee.

(3) Changes to articles of association

The Company shall inform the Stock Exchange of any decision made in regard to any proposed alteration of the Company's Articles of Association and any proposed request by the Company to a PRC competent authority to waive or otherwise notify any provision of the Special Regulations.

(4) Documents for inspection

The Company must make available at a place in Hong Kong for inspection by the public and shareholders free of charge, and for copying by shareholders at reasonable charges, the following:

(a) a complete duplicate register of shareholders;

(b) a report showing the state of the issued share capital of the Company;

(c) the Company's latest audited financial statements and the Directors', auditors' and Supervisors' reports thereon;

(d) special resolutions of the Company;

(e) reports showing the number and nominal value of securities repurchased by the Company since the end of the last financial year, the aggregate amount paid for such securities and the maximum and minimum prices paid in respect of each class of securities repurchased (with a breakdown between Domestic Shares and H Shares);

(f) a copy of the latest annual return filed with the PRC State Administration for Industry and Commerce or other competent PRC authority; and

(g) for shareholders only, copies of the minutes of meetings of shareholders.

(5) Appointment of receiving agents

The Company must appoint one or more receiving agents in Hong Kong and pay to such agents dividends declared and other monies owing by the Company in respect of H Shares listed on the Stock Exchange to be held, pending payment, in trust for holders of the H Shares.

(6) Statements to be made on acquisition of shares

The Company must ensure that all its listing documents and share certificates include the statements stipulated below and must instruct and cause its share registrar not to register the subscription, purchase or transfer of any of its Shares in the name of any particular holder unless and until such holder delivers to such share registrar a signed form in respect of such shares bearing statements to the following effect:

(a) The acquirer of Shares agrees with the Company and each shareholder of the Company, and the Company agrees with each shareholder, to observe and comply with the Company Law, the Special Regulations and the Articles of Association.

(b) The acquirer of Shares agrees with the Company, each shareholder, Director, Supervisor, manager and officer of the Company and the Company acting for itself and for each Director, Supervisor, manager and officer agrees with each shareholder to refer all differences and claims arising from the Articles of Association or any rights or obligations conferred or imposed by the Company Law or other relevant laws and administrative regulations concerning the affairs of the Company to arbitration in accordance with the Articles of Association. Any reference to arbitration shall be deemed to authorise the arbitration tribunal to conduct its hearing in open session and to publish its award. Such arbitration shall be final and conclusive.

(c) The acquirer of Shares agrees with the Company and each shareholder of the Company that H Shares in the Company are freely transferable by the holder thereof.

(d) The acquirer of Shares authorises the Company to enter into a contract on his behalf with each Director and officer whereby such Directors and officers undertake to observe and comply with their obligations to shareholders stipulated in the Articles of Association.

(7) Compliance with the Company Law, the Special Regulations and the Articles of Association

The Company must observe and comply with the Company Law, the Special Regulations and the Articles of Association.

(8) Contract between the Company and every Director and officer

The Company must enter into a contract in writing with every Director and officer containing at least the following provisions:

(a) an undertaking by the Director or officer to the Company to observe and comply with the Company Law, the Special Regulations, the Articles of Association, the Hong Kong Code on Takeovers and Mergers and the Code on Share Repurchases and an agreement that the Company shall have the remedies provided in the Articles of Association and that neither the contract nor his office is capable of assignment;

(b) an undertaking by the Director or officer to the Company acting as agent for each shareholder to observe and comply with his obligations to shareholders stipulated in the Articles of Association; and

(c) an arbitration clause which provides that whenever any disputes or claims arise from the listing agreement, the Articles of Association or any rights or obligations conferred or imposed by the Company Law or other relevant laws and administrative regulations concerning the affairs of the Company between (1) the Company and its Directors or officers and (2) a holder of overseas listed foreign invested shares and a Director or officer of the Company, such disputes or claims shall be resolved through arbitration at either CIETAC in accordance with its arbitration rules or HKIAC in accordance with its Securities Arbitration Rules, at the election of the party seeking arbitration. Where a dispute or claim described above is referred to arbitration, the entire dispute or claim shall be resolved through that arbitration; all persons who have a cause of action based on the same facts giving rise to the dispute or claim or whose participation is necessary for the resolution of such dispute or claim, if they are shareholders, Directors, Supervisors, managers or other officers of the Company or the Company, shall submit to arbitration.

Disputes over who is a shareholder and over the share register do not have to be resolved through arbitration.

If the party seeking arbitration elects to arbitrate the dispute or claim at HKJAC, then either party may apply to have such arbitration conducted in Shenzhen according to the Securities Arbitration Rules of HKIAC. Once the party seeking arbitration submits a dispute or claim to arbitration, the other party must submit to the arbitral body selected by the party seeking the arbitration.

PRC laws shall govern the arbitration of disputes or claims referred to above, unless otherwise provided by law or administrative regulations. The award of the arbitral body is final and shall be binding on the parties thereto.

The agreement to arbitrate is made by the Director or officer with the Company on its own behalf and on behalf of each shareholder. Any reference to arbitration is deemed to authorise the arbitral tribunal to conduct hearings in open session and to publish its award.

(9) Contract between the Company and every Supervisor

The Company must enter into a contract in writing with every Supervisor containing at least the following provisions:

(a) an undertaking by the Supervisor to the Company to observe and comply with the Company Law, the Special Regulations and the Articles of Association and an agreement that the Company will have the remedies provided in the Articles of Association and that neither the contract nor his office is capable of assignment;

(b) an undertaking by the Supervisor to the Company acting as agent for each shareholder to observe and comply with his obligations to shareholders stipulated in the Articles of Association; and

(c) the arbitration clause in terms set out in sub-paragraph (8)(c) above subject to necessary modifications.

The Company is required to adopt rules governing dealings by its Supervisors in securities of the Company in terms no less favourable than those of the Model Code for Securities Transactions by Directors of Listed Companies (set out in Appendix 10 of the Listing Rules) issued by the Stock Exchange which applies to directors of companies listed on the Stock Exchange.

(10) Subsequent listing

The Company must apply for the listing of any further securities which are of the same class as securities already listed, prior to their issue, and must not issue such securities unless it has applied for the listing of these securities. The Company must not apply for the listing of any of its foreign invested shares on a PRC stock exchange unless the Stock Exchange is satisfied that the relative rights of the holders of overseas listed foreign shares are adequately protected.

(11) English translation

All notices or other documents required under the listing agreement to be sent by the Company to the Stock Exchange or to holders of H Shares shall be in the English language, or accompanied by a certified English translation.

General

If changes in the PRC law or market practices materially alter the validity or accuracy of any of the bases upon which the above requirements have been prepared, then the Stock Exchange may impose additional requirements or make the listing of the equity securities of a PRC issuer, including the Company, subject to such special conditions as the Stock Exchange considers appropriate. Whether or not any such changes in the PRC law or market practices occur, the Stock Exchange retains its general power under the Listing Rules to impose additional requirements and make special conditions in respect of the listing of the shares of the Company.

3. ARTICLES OF ASSOCIATION

(a) Directors

Set out below is a summary of the principal provisions of the Articles of Association which, were adopted at the extraordinary general meeting of the Company held on 4th September, 2002 and approved by SETC on 18th September, 2002. Copies of the full Chinese texts of the Articles of Association are available for inspection as mentioned in the section headed "Documents Delivered and Available for Inspection" in Appendix XI.

(i) *Power to allot and issue shares*

There are no provisions in the Articles empowering the Directors to allot and issue shares.

In order to increase the share capital of the Company, the Board shall prepare a detailed proposal and draft amendments of the Articles to permit the increase for approval by shareholders in general meeting by way of special resolution and shall comply with the relevant procedures.

(ii) *Power to dispose of the assets of the Company or any subsidiary*

The Board shall not, without the prior approval of shareholders in general meeting, dispose or agree to dispose of any fixed assets of the Company where the aggregate of:

(A) the amount or value of the consideration for the proposed disposition, and

(B) where any fixed assets of the Company have been disposed of in the period of four months immediately preceding the proposed disposition, the amount or value of the consideration for any such disposition,

exceeds 33% of the value of the Company's fixed assets as shown in the latest balance sheet placed before the shareholders in general meeting. The validity of a disposition by the Company shall not be affected by the breach of the relevant Article. For the purpose of that Article, disposition includes an act involving transfer of some interests in property other than by way of security.

(iii) *Remuneration and payments for loss of office*

The Company shall, with the prior approval of shareholders in general meeting, enter into a contract in writing with a Director or a Supervisor wherein his emoluments are stipulated, including:

(A) emoluments for being a Director, Supervisor or senior management officer of the Company;

(B) emoluments for being a Director, Supervisor or senior management officer of any subsidiary of the Company;

(C) emoluments in respect of the provision of other services in connection with the management of the affairs of the Company and any of its subsidiaries; and

(D) payment by way of compensation for loss of office, or as consideration for or in connection with his retirement from office.

Except under a contract entered into in accordance with the foregoing, no proceedings may be brought by a Director or Supervisor against the Company for anything due to him in respect of the above matters.

The contract concerning the emoluments between the Company and its Directors or Supervisors should provide that in the event of a takeover of the Company, the Company's Directors and Supervisors shall, subject to the prior approval of the shareholders in general meeting, have the right to receive compensation or other payment in respect of his loss of office or retirement. A "takeover of the Company" referred to in this paragraph means any of the following:

(A) a takeover offer made by any person to the general body of shareholders; or

(B) a takeover offer made by any person with a view to the offeror becoming a "controlling shareholder" within the meaning set out in the Articles.

If the relevant Director or Supervisor does not comply with the above, any sum so received by him shall belong to those persons who have sold their Shares as a result of the said offer made. The expenses incurred in distributing that sum pro rata amongst those persons shall be borne by the relevant Director or Supervisor and not paid out of the sum distributed.

(iv) *Loans to Directors, Supervisors and other senior management officers*

The Company shall not directly or indirectly make a loan to or provide any guarantee in connection with the making of a loan to a Director, Supervisor, general manager, or other senior management officer of the Company or of the Company's holding company or a person connected with any of them. However, the following transactions are not subject to such prohibition:

(A) the provision by the Company of a loan or a guarantee of a loan to a company which is a subsidiary of the Company;

(B) the provision by the Company of a loan or a guarantee in connection with the making of a loan or any other funds to any of its Directors, Supervisors, general manager, and other senior management officers to meet expenditure incurred or to be incurred by him for the purposes of the Company or for the purpose of enabling him to perform his duties properly, in accordance with the terms of a service contract approved by the shareholders in general meeting; or

(C) the Company may make a loan to or provide a guarantee in connection with a loan by another person to any of its Directors, Supervisors, general manager and other senior management officers or persons connected to him in the ordinary course of its business on normal commercial terms, where the ordinary course of business of the Company includes the lending of money or the giving of guarantees.

A loan made by the Company in breach of the prohibition described above shall be repayable forthwith by the recipient of the loan regardless of the terms of the loan.

A guarantee provided by the Company in breach of the prohibition described above shall be unenforceable against the Company, unless:

(A) the guarantee was provided in connection with a loan to a person connected with a Director, Supervisor, general manager or other senior management officer of the Company or its parent company and at the time the loan was advanced the lender was not aware of the relevant circumstances; or

(B) the security provided by the Company has been lawfully disposed of by the lender to a bona fide purchaser.

For the purpose of this paragraph,

(A) a guarantee includes an undertaking or property provided to secure the performance of obligations by the obligor; and

(B) the definition of a connected person in sub-paragraph (xii) below shall, mutatis mutandis, apply.

(v) *Financial assistance to purchase shares in the Company or any of its subsidiaries*

Save as described below, no financial assistance shall be provided at any time and in any manner by the Company and its subsidiaries to any person acquiring or intending to acquire the shares of the Company. The person(s) acquiring the shares of the Company aforesaid shall include the person(s) who undertake(s), directly or indirectly, obligations as a result of an acquisition of shares of the Company.

Save as described below, no financial assistance shall be provided at any time and in any manner by the Company and its subsidiaries to reduce or release the obligations of the said person(s) undertaking such obligations.

The following transactions are not prohibited:

(A) provision of financial assistance where the financial assistance is given in good faith in the interests of the Company and the principal purpose in giving that assistance is not for the acquisition of shares in the Company, or the assistance is but an incidental part of some larger purpose of the Company;

(B) distribution of the Company's assets by way of dividend in accordance with law;

(C) allotment of bonus shares as dividends;

(D) reduction of share capital, a repurchase of shares of the Company, restructuring of the capital structure of the Company effected in accordance with the Articles;

(E) lending of money by the Company in the ordinary course of its business where the lending of money is part of the scope of business, provided that the Company's net assets are not thereby reduced or, to the extent that those assets are thereby reduced, that financial assistance is provided out of distributable profits of the Company;

(F) provision of money by the Company for contributions to employees' shares schemes, provided that the Company's net assets are not thereby reduced or, to the extent that those assets are thereby reduced, that financial assistance is provided out of distributable profits of the Company.

For the purposes of the foregoing provisions,

(A) "financial assistance" includes without limitation:

(1) assistance given by way of gift;

(2) assistance given by way of guarantee (including the provision of an undertaking or property to secure the performance of obligations by the obligor), or indemnity (other than an indemnity arising from the Company's own fault), or by way of release or waiver of rights;

(3) assistance given by way of a loan or any other agreement under which the obligations of the Company are to be fulfilled before the obligations of another party to the agreement, or by way of the novation, or the assignment of rights arising under, a loan or such other agreement; or

(4) any other assistance given by the Company when the Company is unable to pay its debts or has no net assets or when its net assets would thereby be reduced by a material extent, and

(B) "undertaking" includes changing one's financial position by making an agreement or arrangement (whether enforceable or not, and whether made on his own account or with any other person) or by any other means.

(vi) *Disclosure of interests in contracts with the Company or any of its subsidiaries*

Where a Director, Supervisor, general manager or other senior management officer of the Company is in any way, directly or indirectly, materially interested in a contract, transaction or arrangement or proposed contract, transaction or arrangement with the Company, other than his contract of service, he shall declare the nature and extent of his interest to the Board at the earliest opportunity, whether or not the aforesaid matters are under normal circumstances subject to the approval of the Board. Unless the interested Director, Supervisor, general manager or other senior management officer has disclosed his interest in accordance with the Articles and the contract, transaction or arrangement has been approved by the Board at a meeting in which such interested Director is not counted in the quorum and has refrained from voting, that contract, transaction or arrangement is voidable at the instance of the Company except as against a bona fide party thereto acting without notice of the breach of duty by the Director, Supervisor, general manager or other senior management officer concerned. For the purposes of the foregoing, a Director, Supervisor, general manager or senior management officer is deemed to be interested in a contract, transaction or arrangement in which a person connected with him is interested.

Where a Director, Supervisor, manager or other senior management officer gives to the Board a general notice in writing stating that, by reason of the facts specified in the notice, he is interested in contracts, transactions or arrangements of any description which may subsequently be made by the Company, that notice shall be deemed for the purposes of the Articles to be a sufficient declaration of his interest, so far as attributable to those facts, in relation to any contract, transaction or arrangement of that description which may subsequently be made by the Company, provided that such general notice shall have been given before the date on which the question of entering into the relevant contract, transaction or arrangement is first taken into consideration on behalf of the Company.

(vii) *Remuneration*

The emoluments of a Director shall be approved by shareholders in general meeting as referred to under the paragraph headed "Remuneration and payments for loss of office".

(viii) *Retirement, appointment and removal*

The term of office of the Chairman and other Directors shall be three years commencing from the date of appointment or re-election, renewable upon re-election. A Director may concurrently hold other senior positions in the Company other than the position of Supervisor.

A Director is not required to hold any shares in the Company.

The Directors shall be elected by the shareholders at shareholders' general meeting.

The Board shall consist of seven members. The Board shall have one Chairman and one vice-chairman and two independent non-executive Directors. The Chairman shall be elected and removed by a simple majority of the Directors.

Directors shall be elected at the shareholders' general meeting for a term of three years. Upon the expiry of the term, a director shall be eligible for re-election.

A Director may assume the office of any other senior management staff of the Company save and except the office of Supervisor.

A Director may be removed prior to the expiration of his term of office with the sanction of an ordinary resolution at a shareholders' general meeting.

There is no stipulation that a Director must retire at a certain age.

(ix) *Borrowing powers*

The Board has powers to formulate proposals for the issue of bonds of the Company and Company's borrowing and financial strategies.

There are no provisions in the Articles stipulating the manner of varying the borrowing powers exercisable by the Board. However, such powers, as with other provisions in the Articles, may be altered by special resolution of shareholders in general meeting.

(x) *Notice and Minutes of Board Meetings*

All such major and important matters which require the approval of the board of directors shall be notified to all directors within the prescribed time limit under the Articles, sufficient information shall be supplied and the stipulated requirements in relation to the conduct of such procedures shall be strictly adhered to. Directors may request the provision of supplemental materials. When more than one-fourth of directors or more than two non-executive directors are of the view that the materials are not sufficient or the submission is inaccurate, they may propose to postpone the meeting of the board of directors or to postpone the discussion of certain matters in the meeting of the board of directors, the board of directors shall so adopt.

The board of directors shall cause the matters resolved at the meeting of the board of directors and director's resolution passed without convening meeting of the board of directors to be recorded in Chinese language in form of minutes. The opinion expressed by independent (non-executive) directors shall be set out in the board resolutions.

(xi) *Duties*

Each Director, Supervisor, general manager or other senior management officer owes a duty, in the exercise of his powers and the discharge of his duties, to exercise the care, diligence and skill that a reasonable prudent person would exercise in comparable circumstances.

In addition to obligations imposed by laws, administrative regulations or required by the listing rules of the stock exchanges on which shares of the Company are listed, each Director, Supervisor, general manager and other senior management officer owes a duty to each shareholder, in the exercise of the powers of the Company entrusted to him:

(A) not to cause the Company to exceed the scope of business stipulated in its business licence;

(B) to act honestly in what he considers to be in the best interests of the Company;

(C) not to expropriate in any guise the Company's property, including without limitation, opportunities beneficial to the Company; and

(D) not to expropriate the individual rights of shareholders, including, without limitation, rights to distribution and voting rights, save and except pursuant to a restructuring of the Company submitted to shareholders for approval in accordance with the Articles.

Each Director, Supervisor, general manager or other senior management officer owes a duty, in the exercise of powers entrusted to him, to observe his fiduciary obligations and not to place himself in a position where his duty and his interest may conflict. This principle includes, without limitation, the following obligations:

(A) to act honestly in what he considers to be in the best interests of the Company;

(B) to exercise the powers within his authority without abuse;

(C) to exercise the discretion vested in him personally and not allow himself to act under the direction of another and, unless and to the extent permitted by law or the informed consent of shareholders in general meeting, not to delegate the exercise of his discretion;

(D) to treat shareholders of the same class equally and to treat shareholders of different classes fairly;

(E) except in accordance with the Articles or otherwise permitted by informed shareholders in general meeting, not to enter into any contract, transaction or arrangement with the Company;

(F) unless otherwise permitted by informed shareholders in general meeting, not to use the Company's property for his own benefit;

(G) not to obtain money from bribery or other illegal income by using his authority or to expropriate in any manner the Company's property, including, without limitation, not to usurp the opportunities beneficial to the Company;

(H) unless otherwise permitted by informed shareholders in general meeting, not to accept commissions in connection with the Company's transactions;

(I) to abide by the Articles, faithfully execute his official duties and protect the Company's interests, and not to exploit his position and power in the Company to advance his own private interests;

(J) unless otherwise permitted by informed shareholders in general meeting, not to compete in any form with the Company;

(K) not to embezzle the Company's funds or lend them to others, and not to deposit the Company's funds in accounts opened in his own name or in the name of other persons and not to use the Company's assets to provide security for the debts of the Company's shareholders or other individuals; and

(L) unless otherwise permitted by informed shareholders in general meeting, not to disclose confidential information of the Company acquired by him in the course of and during his tenure and not to use such information other than in furtherance of the interests of the Company, save and except that disclosure of such information to the court or other governmental authorities is permitted if (i) disclosure is made under compulsion of law; (ii) there is a duty to the public to disclose; or (iii) such disclosure is necessary to protect the interests of that Director, Supervisor, manager or senior management officer.

In accordance with his fiduciary obligations, a Director, Supervisor, general manager or other senior management officer shall not cause a person connected with him to do what he is prohibited from doing. A person is connected with a Director, Supervisor, manager or other senior management officer if he is:

(A) the spouse or minor child of that Director, Supervisor, general manager or other senior management officer;

(B) a person acting in the capacity of trustee of that Director, Supervisor, general manager or other senior management officer or any person referred to in (A) above;

(C) a person who is a partner of that Director, Supervisor, general manager or other senior management officer or any person referred to in (A) and (B) above;

(D) a company in which that Director, Supervisor, general manager or other senior management officer, alone or jointly with one or more persons referred to in (A), (B) and (C) above or other Director, Supervisors, managers or other senior management officers, has de facto control; or

(E) a Director, Supervisor, general manager or other officer of a company referred to in (D) above;

The fiduciary duties of a Director, Supervisor, general manager or other senior management officer under the Articles do not necessarily cease with the termination of his term of office.

Their duty of confidence in relation to trade secrets of the Company survives the termination of their term of office. Other duties may continue for such period as fairness may require depending on the time lapse between such termination and the act concerned and the circumstances and the terms under which the relationship with the Company was terminated.

Subject to the provisions with regard to the duties of controlling shareholders defined in paragraph (r) below towards other shareholders as set out in the Articles, a Director, Supervisor, general manager or other senior management officer may be relieved of liability for specific breaches of his duty by the informed consent of shareholders in general meeting.

(b) Alterations to constitutional documents

The Company may amend the Articles in accordance with the following procedures:

(i) the Board shall adopt a proposal to amend the Articles in accordance with the Articles and shall formulate proposal for amendments;

(ii) shareholders shall be informed of the proposal for amendments and a meeting of shareholders shall be convened to vote on the amendments;

(iii) the amendments shall require the sanction of a special resolution at shareholders' general meeting; and

(iv) any amendments to the Articles involving the contents of the Mandatory Provisions shall be effective only after approved by the companies approving department authorised by the State Council. With respect to matters involving registration, any change of registration shall be effected according to law.

(c) Variation of rights of existing shares or classes of shares

Rights conferred on any class of shareholders in the capacity of shareholders ("class rights") may not be varied or abrogated unless approved by a special resolution of shareholders in general meeting and by holders of shares of that class at a separate meeting conducted in accordance with the Articles. The following circumstances shall be deemed to be a variation or abrogation of the class rights of a class:

(i) the increase or decrease in the number of shares of such class, or an increase or decrease, in the number of shares of a class having voting or distribution rights or other privileges equal or superior to the shares of such class;

(ii) the exchange of all or part of the shares of such class or the exchange or the grant of a right of exchange of all or part of the shares of another class into the shares of such class;

(iii) the removal or reduction of rights to accrued dividends or rights to cumulative dividends of such class;

(iv) the reduction or removal of any preference to dividends or any preference to a distribution of asset upon the Company's liquidation;

(v) the addition, removal or reduction of conversion privileges, options, voting, transfer or preemptive rights or rights to acquire securities of the Company of such class;

(vi) the removal or reduction of rights to receive payment in particular currencies from the Company of such class;

(vii) the creation of a new class of shares having voting or distribution rights or other privileges equal or superior to the shares of such class;

(viii) the imposition of restrictions on the transfer or ownership of the shares of such class or the addition of such restrictions;

(ix) the issue of rights to subscribe for, or convert into, shares in the Company of such class or another class;

(x) the increase of the rights or privileges of another class;

(xi) the restructuring of the Company which will result in different classes of shareholders bearing a disproportionate burden of such proposed restructuring; and

(xii) the variation or abrogation of provisions in Chapter 9 of the Articles.

(d) Ordinary and special resolutions — majority required

Resolutions of shareholders' general meetings shall be divided into ordinary resolutions and special resolutions.

An ordinary resolution shall be passed by more than one half of the votes represented by the shareholders (including proxies) present at the meeting in favour of the resolution. A special resolution shall be passed by more than two thirds of the votes represented by the shareholders (including proxies) at the shareholders' general meeting exercised in favour of the resolution.

Shareholders (including proxies) present at the shareholders' general meeting in exercising their voting rights have to show explicitly whether they vote for or against each resolution proposed to be passed at that meeting. Abstention or failure to vote shall be disregarded by the Company as voting rights for the purpose of calculating the result of that resolution.

(e) Voting rights (generally, on a poll and right to demand a poll)

Holders of Ordinary Shares present at a shareholders' general meeting have one vote for each share they hold.

At any meeting of shareholders a resolution put to the vote of the meeting shall be decided on a show of hands unless a poll is (before or after any vote by show of hands) demanded:

(i) by the chairman of the meeting;

(ii) by at least two shareholders having the right to vote either present in person or by proxy; or

(iii) by one or more shareholders present in person or by proxy and representing not less than one tenth of all shares carrying the right to vote at the meeting.

Unless a poll be so demanded, a declaration by the chairman as to the passing of the resolution based on the results of a show of hands and an entry to that effect in the minutes of the Company, shall be conclusive evidence of that fact without proof of the number or proportion of the votes recorded in favour of or against such resolution.

The demand for a poll may be withdrawn by the person who made the demand. A poll demanded on the election of the chairman of the meeting, or on a question of adjournment, shall be taken forthwith. A poll demanded on any other question shall be taken at such time before the end of that meeting as the chairman of the meeting directs, and any business other than that upon which a poll has been demanded may be proceeded with, pending the taking of the poll. The result of the poll shall be deemed to be a resolution passed in the meeting.

On a poll taken at a meeting, a shareholder entitled to two or more votes need not cast all his votes in the same way.

In the case of an equality of votes, whether on a show of hands or on a poll, the chairman of the meeting at which the show of hands takes place or at which the poll is demanded shall be entitled to one extra vote.

(f) Requirements for general meetings

Shareholders' general meetings are divided into annual general meetings and extraordinary general meetings. Shareholders' general meetings shall be convened by the Board. Annual general meetings are held once every year within six months after the last financial year end.

Under any of the following circumstances, the Board shall convene an extraordinary general meeting within two months of the occurrence of the following events:

(i) when the number of directors falls below the number required by the PRC Company Law or two-thirds of the number required by the Articles;

(ii) when the losses of the Company which have not been made up amount to one-third of the total share capital of the Company;

(iii) upon requisition in writing of shareholders holding 10% or more of the issued shares carrying voting rights for the convening of an extraordinary general meeting; or

(iv) when the Board deems necessary or the supervisory committee convenes the same in writing.

(g) Accounts and audit

The Company shall formulate its own financial and accounting system in accordance with the relevant requirements of PRC laws, administrative regulations and the PRC accounting standards formulated by the State Council finance department.

The financial year of the Company shall coincide with the calendar year, which is from 1st January to 31st December on the Gregorian calendar.

The Company shall adopt Renminbi as its accounts keeping unit. All accounts shall be written in Chinese.

The board of directors of the Company shall place before the shareholders at every annual general meeting such financial reports as are required by any laws, administrative regulations or directives promulgated by competent local and central governmental authorities to be prepared by the Company.

The financial reports of the Company shall be deposited at the Company for inspection by its shareholders not later than 20 days before the annual general meeting. Each shareholder of the Company shall be entitled to receive the financial statements referred to in this article.

The Company shall send by prepaid mail 21 days before the annual general meeting the above financial reports and directors' reports to each holder of overseas listed foreign shares. The service address shall be the address in the register of shareholders.

The financial statements of the Company shall, in addition to being prepared in accordance with PRC accounting standards and regulations, be prepared in accordance with either international accounting standards, or that of the place overseas where the Company's H Shares are listed. If there is any material difference between the financial statements prepared respectively in accordance with the two accounting standards, such difference shall be stated in an appendix to the financial statements. When the Company is to distribute its after-tax profits, the lower of the after-tax profits as shown in the two financial statements shall be adopted.

Any interim results or financial information published or disclosed by the Company must also be prepared in accordance with PRC accounting standards and regulations, and also in accordance with either international accounting standards or that of the place overseas where the Company's H Shares are listed.

The Company shall publish its financial reports twice every financial year, that is, the interim reports shall be published within 60 days after the end of the first six months of each financial year and annual reports shall be published within 120 days after the end of the financial year.

The appointment, dismissal or termination of the office of an auditor shall be determined at shareholders' general meetings and reported to the relevant State Council securities regulatory authorities for record.

Shareholders in general meeting may by ordinary resolution remove an auditor before his term of office expires, irrespective of any provisions contained in the contract entered into between the Company and the auditor. Any right of the auditor to claim against the Company in connection with his removal shall not be affected by such removal.

In the event of the dismissal or termination of the services of an auditor, such auditor who is to be dismissed or whose services are to be terminated shall be given notice in advance. Such auditor shall have the right to present its views at the following shareholders' general meetings:

(i) the shareholders' general meeting at which its term of office would otherwise have expired;

(ii) any shareholders' general meeting at which it is proposed to fill the casual vacancy caused by its removal; or

(iii) any shareholders' general meeting convened on resignation of the auditor.

(h) Notice of meetings and business to be conducted thereat

The shareholders' general meeting is the authority of the Company.

Notice of meetings of shareholders shall be given 45 days before the meeting. A notice of meeting of shareholders shall:

(i) be in writing;

(ii) specify the place, the date and the time of the meeting;

(iii) state the business to be transacted at the meeting;

(iv) provide such information and explanation as are necessary for the shareholders to make an informed decision on the proposals before them. Without limiting the generality of the foregoing, where a proposal is made to amalgamate the Company with another, to repurchase shares of the Company, to reorganise the share capital, or to restructure the Company in any other way, the terms of the proposed transaction must be provided in detail together with copies of the proposed agreement, if any, and the cause and effect of such proposal must be fully explained;

(v) contain a disclosure of the nature and extent, if any, of material interests of any Director, Supervisor, general manager or other senior management officer in the transaction proposed and the effect of the proposed transaction on such Director, Supervisor, manager or other senior management officer in his capacity as shareholder in so far as it is different from the effect on the interests of other shareholders of the same class;

(vi) contain the full text of any special resolution proposed to be moved at the meeting;

(vii) contain conspicuously a statement that a shareholder entitled to attend and vote is entitled to appoint one or more proxies to attend and vote instead of him and that a proxy need not also be a shareholder; and

(viii) specify the time and place for lodging proxy forms for the relevant meeting.

In respect of holders of H Shares, notice of general meetings of shareholders shall be served on each shareholder, whether or not entitled to vote thereat, by delivery or prepaid mail to the address of any such shareholder as appearing on the register of holders of H Shares. In respect of holders of Domestic Shares, notice of general meetings of shareholders can be published on any one day within the period of 45 of 50 days prior to the meeting in one or more national publications specified by the State Council securities regulatory authority. Once published, all holders of Domestic Shares shall be deemed to have received the notice of the relevant general meeting.

The accidental omission to give notice of a meeting to, or the non-receipt of notice of a meeting by, any person entitled to receive notice shall not invalidate that meeting or any resolutions passed thereat.

(i) Transfer of shares

All fully paid H shares listed in Hong Kong are freely transferable pursuant to the Articles. The Board may refuse to recognise any instrument of transfer without giving any reason unless such transfer is carried out in compliance with the following conditions:

(i) payment of HK$2.50 or higher charge as agreed by the Stock Exchange has been made to the Company for the purpose of registering the instrument of transfer and other documents relating to or which may affect the title to the shares;

(ii) the instrument of transfer only involves H Shares listed in Hong Kong;

(iii) the stamp duty payable on the instrument of transfer has been paid;

(iv) relevant share certificates and evidence that the transferor has the right to transfer such shares as reasonably required by the Board have been provided;

(v) if the shares are to be transferred to joint holders, the number of joint holders shall not exceed four; and

(vi) the Company has no lien over the relevant shares.

The overseas listed foreign shares of the Company shall be transferred in an ordinary or regular way or a way acceptable to the board of Directors; such instrument of transfer may be executed by way of affixing of seal in mode of printing. All instruments of transfer shall be placed at the legal address of the Company or any such place designated by the board of Directors from time to time.

(j) Register of shareholders

The Company shall keep a register of shareholders and enter therein the following particulars:

(i) the names, residential addresses, occupations, whether legal persons or natural persons, descriptions of shareholders, the class and the number of each class of shares held, the amount paid or agreed to be paid on the shares, and the serial number of the share certificates held by each shareholder.

(ii) the date on which each person was entered in the register as a shareholder; and

(iii) the date on which any person ceased to be a shareholder.

The Company shall have a complete register of shareholders which shall comprise the following parts:

(i) a part maintained at the Company's legal address in relation to shares not required to be registered in the parts of the register referred to in (ii) and (iii) below;

(ii) a part maintained in the place of the stock exchange where the securities listed overseas is located; and

(iii) any part in such other places as the Board may deem necessary for the purpose of listing of Shares.

The Company may appoint overseas agents to manage the register of shareholders outside the PRC. A duplicate of parts of the register of shareholders maintained pursuant to (ii) and (iii) above shall be maintained at the Company's legal address. The appointed overseas agents shall ensure that the original of any overseas part of the register of shareholders is consistent with the duplicate thereof. In the event of discrepancy, the information recorded in the original part shall prevail. Different parts of the register of shareholders shall not overlap. No transfer of any shares registered in any part of the register shall, during the continuance of that registration, be registered in any other part of the register of shareholders. The alteration and rectification of each part of the register of shareholders shall be made in accordance with the laws of its situs. The register of shareholders shall be sufficient evidence, in the absence of evidence to the contrary, of a shareholding in the Company.

(k) Power of the Company to purchase its own shares and reduce its share capital

Subject to governmental approvals, the Company may, subject to the provisions set out in the Articles, repurchase its own shares. A share repurchase may only be made:

(i) under a repurchase offer to all shareholders in proportion to their respective holdings;

(ii) on a stock exchange by way of an open transaction; or

(iii) by an off-market contract.

The Company may, with the prior sanction of shareholders in general meeting obtained in accordance with the Articles, repurchase its shares by an off-market contract, but the Company may release or modify its rights under a contract so entered into by the Company with the prior approval of shareholders in general meeting obtained in the same manner. A contract to repurchase shares includes but is not limited to an agreement to become obliged to repurchase or to acquire rights to repurchase shares of the Company. The Company shall not assign its rights under a contract to repurchase its own shares.

Unless the Company has commenced liquidation:

(i) where the Company repurchases its own shares at nominal value, payment may be made out of distributable profits of the Company on the book and out of proceeds of a fresh issue of shares made for that purpose;

(ii) where the Company repurchases its own shares at a premium, payment of the portion equivalent to the nominal value may be made out of distributable profits of the Company on the book and out of the proceeds of a fresh issue of shares made for that purpose. Payment of the portion in excess of the nominal value shall be effected as follows:

 (A) if the shares being repurchased were issued at nominal value, payment shall be made out of the balance of the distributable profits of the Company on the book;

 (B) if the shares being repurchased were issued at a premium, payment shall be made out of the balance of the distributable profits of the Company on the book and out of proceeds of a fresh issue of shares made for that purpose, provided that the amount paid out of the proceeds of the fresh issue may not exceed the aggregate of premiums received by the Company on the issue of the shares repurchased nor the amount of the Company's capital reserve fund account at the time of such repurchase including the premiums on the fresh issue of shares;

(iii) payment by the Company in consideration for:

 (A) the acquisition of rights to repurchase shares of the Company;

 (B) the variation of any contract to repurchase shares of the Company; or

 (C) the release of any of the Company's obligations under any contract to repurchase shares of the Company;

 shall be made out of the Company's distributable profits.

Shares redeemed or repurchased by the Company shall be cancelled and the amount of the Company's registered capital shall be reduced by the par value of those shares accordingly. The amount which has been deducted from the distributable profits and which has been used for repurchasing the nominal value of the shares shall be credited to the capital surplus reserve fund account.

Upon the reduction of registered capital, the Company shall prepare a balance sheet and a list of its assets. The Company shall notify its creditors within 10 days from the date of passing of the resolution for the reduction of registered capital and shall publish the notice at least three times in a newspaper within 30 days thereof. Creditors who receive this notice shall have the right within 30 days from the date of receiving the notice, and the creditors who have not received the notice shall have the right within 90 days from the date of the notice was first published in the newspaper, to require the Company to settle the debt or to provide corresponding security in respect of the debt.

The registered capital shall not be less than the minimum statutory requirement after the reduction of capital.

(l) Power for any subsidiary of the Company to hold shares in the Company

There are no provisions in the Articles relating to holding of shares in the Company by a subsidiary.

(m) Dividends and other methods of distribution

Unless otherwise resolved at a shareholders' general meeting, the board of directors as authorised by shareholders in general meeting has the authority to distribute interim or special dividend.

The Company may distribute dividends by way of cash dividends and/or shares.

Cash dividends and other distributions payable on Domestic Shares shall be paid in Renminbi. Cash dividends and other distributions payable in respect of H Shares shall be declared in Renminbi and payable in Hong Kong dollars in accordance with relevant provisions of foreign exchange control of the State.

When distributing dividends, the Company shall make such withholdings and payment for income tax from dividends payable to shareholders as may be required in accordance with PRC tax law.

The Company shall appoint a receiving agent to receive on behalf of holders of H Shares dividends declared and all other monies owing by the Company in respect of H Shares. Such receiving agent shall be registered as a trust company under the Trustee Ordinance of Hong Kong.

There is no stipulation of any time limit after which any entitlement to dividends lapses.

(n) Proxies

Any shareholder entitled to attend and vote at a meeting of the Company shall be entitled to appoint one or more persons (whether a shareholder or not) as his proxies to attend and vote instead of him, and a proxy so appointed shall:

(i) have the same rights as the shareholder to speak at the meeting;

(ii) have authority to demand or join in demanding a poll; and

(iii) have the right to vote on a show of hands or on a poll, but a proxy of a shareholder who has appointed more than one proxy may only vote on a poll.

The instrument appointing a proxy shall be in writing under the hand of the appointor or his attorney duly authorised in writing, or if the appointor is a company either under seal or under the hand of a director or attorney duly authorised. The instrument appointing a proxy and, if such instrument is signed by a person under a power of attorney or other authority on behalf of the appointer, a notarially certified copy of that power of attorney or other authority shall be deposited at the legal address of the Company or at such other place specified in the notice convening the meeting, not less than 24 hours before the time for holding the meeting or adjourned meeting at which the proxy proposes to vote or the time appointed for the taking of the poll.

Any form issued to a shareholder by the Board for use by him for appointing a proxy to attend and vote at a meeting of the Company shall be such as to enable the shareholder, according to his intention, to instruct the proxy to vote in favour of or against each resolution dealing with the business to be transacted at the meeting. Such a form shall contain a statement that, in the absence of such instructions, the proxy may vote as he thinks fit. A vote given in accordance with the terms of an instrument of proxy shall be valid notwithstanding the previous death or loss of capacity of the principal or revocation of the proxy or of the authority under which the proxy was executed, or the transfer of the shares in respect of which the proxy is given, provided that no notice in writing of such death, loss of capacity, revocation or transfer as aforesaid shall have been received by the Company before the commencement of the meeting or adjourned meeting at which the proxy is used.

(o) Calls on Shares and forfeiture of Shares

There are no provisions in the Articles relating to the making of calls on Shares or for the forfeiture of Shares.

(p) Inspection of register of shareholders and shareholders' other rights to information

The ordinary shareholders of the Company shall enjoy the following rights:

(i) to receive dividends and other distributions in proportion to the number of Shares held;

(ii) to attend or appoint a proxy to attend on his behalf shareholders' general meetings and to vote thereat;

(iii) to supervise the business operations and activities of the Company and to give advice or raise questions;

(iv) to transfer his Shares according to applicable laws, administrative regulations and the provisions of the Articles;

(v) to receive any relevant information in accordance with the Articles;

(vi) to participate in the event of the termination or liquidation of the Company, in the distribution of surplus assets of the Company in proportion to the number of Shares held;

(vii) other rights conferred by the Articles and the relevant laws and regulations.

The right of the shareholders to information includes, without limitation, the following:

(i) the right to a copy of the Articles with a charge at cost;

(ii) the right to inspect and copy for reasonable charges:

(A) all parts of the register of shareholders;

(B) particulars of Directors, Supervisors, managers and other senior management officers as follows:

(1) his present forename and surname and any former forename or surname and any aliases;

(2) his principal residential address;

(3) his nationality;

(4) his primary and all other business occupations; and

(5) his identification document and its number.

(C) the state of the Company's share capital;

(D) reports showing the number and par value of Shares repurchased by the Company since the end of the last financial year, the aggregate amount paid by the Company for the Shares repurchased and the maximum and minimum price paid in respect of each class of Shares repurchased; and

(E) minutes of shareholders' meetings.

(q) Quorum for shareholder's meetings and class meetings

A shareholder proposing to attend a shareholder's general meeting shall deposit a written reply confirming his attendance 20 days prior to the holding of the meeting. The Company shall, according to the written replies received 20 days prior to the holding of a shareholders' general meeting, calculate the number of shares carrying the right to vote represented by the shareholders proposing to attend the meeting. If the number of shares carrying the right to vote represented by the shareholders proposing to attend the meeting reaches half of the total number of shares of the Company carrying the right to vote, then the Company may hold the shareholders' general meeting; if that number is not reached, the Company shall within five days notify the shareholders again of the matters proposed to be considered at the meeting, the date and the place of the meeting by way of public announcement. After such public announcement, the Company may hold the shareholder's general meeting.

The above procedure applies mutatis mutandis to shareholders of the relevant class of shares in respect of class meetings.

(r) Rights of minority shareholders in relation to fraud or oppression

In addition to obligations imposed by laws, administrative regulations or required by the stock exchanges on which H Shares of the Company are listed, a Controlling Shareholder (defined below) shall not exercise his voting rights in a manner prejudicial to the interests of all or part of the shareholders of the Company in respect of the following matters:

(i) to relieve a Director or Supervisor of his duty to act honestly in the best interests of the Company;

(ii) to approve a Director or Supervisor (for his own benefit or for the benefit of another person) taking in any manner, the Company's assets, including without limitation, opportunities beneficial to the Company; or

(iii) to approve a Director or Supervisor (for his own benefit or for the benefit of another person) taking the individual rights of other shareholders, including without limitation, rights to distributions and voting rights save and except pursuant to a restructuring of the Company submitted to the shareholders for approval in accordance with the Articles.

For these purposes, a "Controlling Shareholder" means a person who satisfies any one of the following conditions:

(i) he alone or acting in concert with others has the power to elect more than half of the Directors;

(ii) he alone or acting in concert with others has the power to exercise or to control the exercise of 30% or more of the voting rights in the Company;

(iii) he alone or acting in concert with others holds 30% or more of the Shares of the Company; or

(iv) he alone or acting in concert with others in any other manner controls the Company in fact.

(s) Shareholders' rights relating to, and procedures on, liquidation

Shareholders have the right to participate in the distribution of the surplus assets of the Company in proportion to the number of shares held by them in the event of a liquidation of the Company.

The Company shall be dissolved and liquidated upon the occurrence of any of the following events:

(i) where the shareholders' general meeting resolves that the Company should be dissolved;

(ii) where dissolution is necessary as a result of the merger or division of the Company;

(iii) where the Company is declared insolvent according to law because it is unable to pay its debts as they fall due;

(iv) when the Company is ordered to be closed down by reason of its violation of laws or administrative regulations.

Where the Board decides to liquidate the Company otherwise than because of a declaration of insolvency, the Board shall, in the notice convening a general meeting of shareholders for this purpose, include a statement to the effect that, after having made full inquiry into the affairs of the Company, the Board is of the opinion that the Company will be able to pay its debts in full within 12 months from the commencement of the liquidation.

In the event the Company shall be dissolved under the provisions of (i) above, it shall set up within 15 days thereof a liquidation team, the members of which shall be determined by an ordinary resolution passed in the general meeting.

In the event the Company shall be dissolved under the provisions of (iii) above, the People's Court shall form a liquidation team comprising the shareholders, relevant authorities and relevant professionals in accordance with the laws to proceed with the liquidation thereof.

In the event the Company shall be dissolved under (iv) above, the relevant competent authorities shall form a liquidation team comprising the shareholders, relevant authorities and relevant professionals in accordance with the laws to proceed with the liquidation thereof. Upon the passing of a resolution to liquidate the Company, all powers of Directors shall cease. The liquidation team shall:

(i) not less than once each year report to the shareholders on the team's receipts and payments, the business of the Company and the progress of liquidation;

(ii) present a final report to the shareholders' general meeting on completion of the liquidation; and

(iii) comply with the instructions from shareholders in general meeting.

(t) Other provisions material to the Company or its shareholders

(i) *Scope of Business*

The major scope of the Company's operations include the provision of ground handling service to domestic and foreign air transport enterprises and travellers; the leasing of aeronautical operation premises and commercial and office premises within the airport terminal; external investments.

(ii) *Effect of the Articles*

The Articles have become effective upon approval by the approving department authorised by the State Council. From the date when the Articles take effect, the Articles constitute a legally binding document regulating the relationship between the Company and each shareholder and among the shareholders. A shareholder may bring an action against the Company and vice versa and against each other or against the Directors, Supervisors, managers or other senior management officers in respect of rights and obligations concerning the affairs of the Company arising out of the Articles. For these purposes, actions include court proceedings and arbitration proceedings.

(iii) *Legal form of the Company*

(A) The Company is a joint stock limited company. It is an independent legal entity, governed and protected by laws, regulations and other governmental provisions of PRC.

The Company has perpetual existence unless and until terminated and liquidated in accordance with the Articles.

The Company may invest in other limited liability companies and joint stock limited companies, and shall be liable to the investee companies to the extent of its capital contribution. The Company shall not become a shareholder with unlimited liability of any other economic bodies.

(B) Shares and transfers.

Upon approval by the State Council securities regulatory authority, the Company may issue Domestic Shares and Foreign Shares. Foreign Shares are subscribed by foreign investors (including investors from the regions of Hong Kong, Macau and Taiwan) in foreign currencies. Domestic Shares are subscribed for in Renminbi by investors within the PRC other than investors from the territories referred to above.

Foreign Shares listed overseas are known as overseas listed foreign shares (including, but not limited to H shares). H shares are foreign shares listed on the Stock Exchange, which are subscribed for and traded in Hong Kong dollars.

Save as otherwise provided in the Articles, holders of Domestic Shares and holders of Foreign Shares shall enjoy the same rights and assume the same obligations. The rights and obligations in respect of the Company enjoyed and assumed by shareholders shall be limited to the extent of the number of Shares held by them. The Company shall be liable to its creditors to the extent of all of its assets.

The total amount of Shares to be issued by the Company shall be not less than 447,818,100 Shares and shall not exceed 478,046,100 Shares including (i) 246,300,000 promoter Shares already in issue at the time of establishment of the Company; and (ii) not less than 201,518,100 and not more than 231,746,100 overseas listed foreign shares.

The Company may, based on its business development requirements and in accordance with the Articles, increase its total registered capital. The increase in registered capital may be effected by the following methods:

(1) by an issue of new shares to unspecified investors;

(2) by a placing of new shares to the existing shareholders;

(3) by a bonus issue of shares to the existing shareholders; and

(4) by any other method authorised by law and/or administrative regulations.

Any increase or alteration of the registered capital of the Company shall be effected in accordance with the Articles and procedures required by laws and administrative regulations of PRC. The actual registered capital of the Company shall be determined with reference to the actual funds contributed. The Company shall file the figure of actual registered capital to the State Council's company scrutinising and approving body for record upon all capital becoming available.

(iv) *Legal notices*

Notices, information and written statements to be given by the Company to holders of H Shares must be served on the H Shareholders by delivery to the registered address of each H Shareholder or by post addressed to each H Shareholder at the address shown in the register of shareholders. Notices to be given by the Company to holders of Domestic Shares shall be published in one or more publications specified by the PRC securities regulatory authority. Once published, all holders of Domestic Shares shall be deemed to have received such notice.

(v) *Shareholders' obligations*

Ordinary shareholders of the Company shall assume the following obligations:

(A) to abide by the Articles;

(B) to pay subscription monies according to the number of Shares subscribed and the method of subscription; and

(C) other obligations imposed by the Articles and any relevant laws and regulations.

(vi) *Company secretary*

The Company shall have one secretary of the Board. The secretary is a senior management officer of the Company.

The secretary shall be a natural person who has the requisite professional knowledge and experience appointed by the Board.

The secretary shall be mainly responsible for ensuring that the constitutional documents and records of the Company are in order, that the necessary reports and documents are prepared and submitted to relevant PRC authorities in accordance with the laws, that the register of shareholders of the Company is properly maintained and that persons entitled to records and documents of the Company are furnished with such records and documents without delay.

(vii) *Supervisory committee*

The Company shall have a supervisory committee. The supervisory committee is the Company's standing internal supervisory organ. Its responsibilities are to exercise supervision over the Board and its members and other senior management officers to prevent any abuse of powers, infringement of the legitimate rights of the Company, its shareholders and workers.

The supervisory committee shall comprise three members (each a "Supervisor").

Two-thirds of members of the supervisory committee shall be representatives of shareholders (including persons qualified to be an external Supervisor and an independent Supervisor) and the remaining Supervisors shall be representatives of the staff and workers of the Company.

The supervisory committee is accountable to and reports to shareholders in general meetings and shall exercise the following powers:

(1) to examine the Company's financial affairs;

(2) to supervise the Directors, general managers and other senior management officers against any violation of any laws, regulations or the Articles in performing their duties;

(3) to require the Directors, general managers and other senior management officers to rectify their acts which are harmful to the interest of the Company;

(4) to verify financial reports, business reports, profit distribution plans and such other information proposed to be tabled at a shareholders' general meeting and to appoint, in the name of the Company, a registered accountant or practising auditor to assist in reviewing them should any queries arise;

(5) to propose to convene extraordinary general meetings of shareholders;

(6) to represent the Company in negotiating with any Director or in initiating legal proceeding against any Director; and

(7) other powers as stipulated in the Articles or granted by shareholders' general meeting.

Supervisors are entitled to observe Board meetings.

(viii) *Dispute resolution*

Whenever any disputes or claims arise in relation to the Articles or any rights or obligations conferred by any laws or regulations or the affairs of the Company between the parties set out below, such disputes or claims shall, unless otherwise provided in the Articles, be referred to arbitration to either the China International Economic and Trade Arbitration Commission in accordance with its rules or to the Hong Kong International Arbitration Centre in accordance with its securities arbitration rules, at the election of the claimant. Once a claimant refers a dispute or claim to arbitration, the other party must submit to the arbitral body elected by the claimant. Such arbitration shall be final and conclusive.

The above provisions apply to disputes or claims between the following parties:

(A) a holder of Foreign Shares and the Company;

(B) a holder of Foreign Shares and a Director, Supervisor, general manager or other senior management officer of the Company; and

(C) a holder of Foreign Shares and a holder of Domestic Shares.

Where a dispute or claim involves the above parties, the entire claim or dispute must be referred to arbitration and all persons (being shareholders, Directors, Supervisors, general manager or other senior management officers of the Company or the Company), who have a cause of action based on the same facts giving rise to the dispute or claim or whose participation is necessary for the resolution of such dispute or claim, shall submit to arbitration.

Unless otherwise provided in laws and administrative regulations, any disputes or claims arising out of the Articles between the above mentioned parties shall be resolved in accordance with the laws of the PRC.

Jun He Law Offices, the Company's legal advisers on PRC laws, has sent to the Company a letter confirming that, inter alia, they have reviewed the summary of the Articles and that in their opinion, such summary is a correct summary of the Company's Articles.

4. PRC LEGAL MATTERS

Jun He Law Offices, the Company's legal adviser on PRC law, has sent to the Company a letter dated 6th November, 2002 confirming that it has reviewed the summaries of PRC Company Law and securities regulations and the summaries of certain material differences between Hong Kong company law and the Company Law in so far as they relate to PRC law as contained in this Appendix, the summary of PRC taxation laws and the summary of PRC foreign exchange laws and regulations contained in Appendices VII and VIII, respectively, and that, in its opinion, such summaries are correct summaries of relevant PRC laws and regulations. This letter is available for inspection as referred to in the section headed "Documents Delivered and Available for Inspection" in Appendix XI.

Any person wishing to have detailed advice on PRC laws and the laws of any jurisdiction is recommended to seek independent legal advice.

A. FURTHER INFORMATION ABOUT THE COMPANY

1. Incorporation

The Company was established as a joint stock limited liability company in the PRC by the Promoters under the PRC Company Law on 28th December, 2000 under the name of 海南美蘭機場股份有限公司 (Hainan Meilan Airport Company Limited).

The Company has established a place of business in Hong Kong at Unit 3205A, Shun Tak Centre (West Tower), 200 Connaught Road Central, Sheung Wan, Hong Kong and has applied to be registered with the Registrar of Companies in Hong Kong as an oversea company under Part XI of the Companies Ordinance. Messrs. Deacons of 930 Ocean Centre, Harbour City, Kowloon, Hong Kong has been appointed as the Company's agent for the acceptance of service of process in Hong Kong.

As the Company is established in the PRC, its corporate structure and Articles of Association are subject to the relevant laws and regulations of the PRC. A summary of the relevant laws and regulations of the PRC and of the Articles of Association is set out in Appendix IX.

2. Changes in share capital

At the time of its establishment, the Company's registered capital was RMB250,000,000, divided into 250,000,000 Domestic Shares of par value RMB1.00 each, all of which were subscribed for by the following Promoters and were fully paid up or credited as fully paid up:

Promoters	Number of Domestic Shares subscribed for	Percentage shareholdings
Parent Company	237,500,000	95.000%
Hainan Airlines	5,287,500	2.115%
HNA Group	3,512,500	1.405%
Central South Aviation Development	2,775,000	1.110%
China Southern Airlines	925,000	0.370%
	250,000,000	100.000%

Save as disclosed in this prospectus, there has been no alteration in the share capital of the Company since its establishment. Upon completion of the Global Offering but without taking into account any H Share which may be issued on exercise of the Over-allotment Option, the registered capital of the Company will be increased from RMB250,000,000 to RMB448,000,000 (or up to RMB473,213,000 depending on the extent to which the Over-allotment Option is exercised) divided into 246,300,000 Domestic Shares and 201,700,000 H Shares (or up to 226,913,000 H Shares depending on the extent to which the Over-allotment Option is exercised).

3. Procedures at the Company's extraordinary general meetings

Extraordinary general meetings of the Company were held on 30th May, 2002, 4th September, 2002, and 10th September, 2002, at which resolutions of the shareholders of the Company were passed approving, among other matters:

(i) the Company be converted into a public subscription company upon approval by the relevant PRC authorities;

(ii) the issue of New H Shares, increase of registered share capital and the listing of the H Shares on the Stock Exchange;

(iii) the offering mechanism of the New H Shares and the conversion of the 3,700,000 Domestic Shares into Sale H Shares and the transfer of the Sale H Shares;

(iv) the Directors or Directors' committee be authorised to do any acts and things relating to the conversion of the Company into a public subscription company and the Offering and listing;

(v) the Company to adopt its new Articles of Association and the Directors be authorised to amend the new Articles of Association in accordance with any comments from the relevant governing authorities in the PRC, the Stock Exchange and other relevant authorities and bodies relating to the Company's listing; and

(vi) the Company to swap certain assets with Parent Company to improve the efficiency and integration of its business operation.

4. Restructuring

In relation to the corporate restructuring of the Company which involved the establishment of the Company and the rationalisation of the Company's corporate structure and business operation and in preparation for listing of the H Shares on the Stock Exchange, the Company has obtained a number of approvals from, inter alia, the relevant governmental authorities of the Hainan Province, SETC, CSRC and MOF. The Restructuring involved, inter alia, the following procedures and approvals:

(i) on 28th November, 2000, Hainan Assets Bureau issued an approval for the proposal of the corporate restructuring submitted by Parent Company in relation to the establishment of the Company (Qiong Guo Zi Ban Han [2000] 181);

(ii) on 11th December, 2000, Hainan Finance Administrative Bureau issued an approval for confirmation of the valuation of the assets to be injected into the Company by Parent Company (Qiong Cai Qi [2000] 702);

(iii) on 21st December, 2000, an inaugural meeting of the Company was convened at which, amongst others:

(a) Parent Company's report on the establishment of the Company was approved;

(b) the initial articles of association of the Company were adopted;

(iv) on 26th December, 2000, the Hainan Office of Joint Stock Enterprises issued an approval approving the establishment of the Company (Qiong Gu Ban [2000] 97);

(v) on 28th December, 2000, a business licence was issued by the Hainan Administration of Industry and Commerce to the Company, whereupon the Company was established as a joint stock limited liability company and acquired the status of an enterprise legal person;

(vi) on 30th September, 2001, the valuation report in respect of the land use right to the land with an aggregate gross area of approximately 295,508m^2 injected into the Company by Parent Company was accepted by and filed with the Qiongshan Municipal Bureau of State Land and Resources;

(vii) on 30th May, 2002, an extraordinary general meeting of the Company was held at which certain resolutions as set out in the paragraph A3 "Procedures at the Company's extraordinary general meetings" of this Appendix were approved;

(viii) on 6th September, 2002, MOF issued a confirmation letter in respect of the management of state-owned Shares of the Company (Cai Qi [2002] No. 356);

(ix) on 15th September, 2002, MOF issued an approval for the retention of 50% of the Airport Fee by the Company as income subject to the relevant PRC tax (Cai Jian [2002] No. 383);

(x) on 18th September, 2002, SETC issued an approval (Guo Jing Mao Qi Gai [2002] No. 680), among other matters, approving the Company's new Articles of Association adopted on 4th September, 2002 and authorising the Company's conversion into a public subscription company; and

(xi) on 14th October, 2002, CSRC issued an approval (Zheng Jian Guo He Zi [2002] No. 31) approving the allotment and issue of the New H Shares by the Company, the sale of the Sale H Shares by the Vendors and the conversion and transfer of the Sale H Shares.

Immediately following the completion of the Offering, the number of H Shares will constitute approximately 45% of the issued capital of the Company (assuming that the Over-allotment Option is not exercised at all).

5. Subsidiaries

The Company's subsidiaries are referred to in the Accountants' Report, the text of which is set out in Appendix I.

Save as disclosed in this prospectus, there has been no alteration in the registered capital of any of the subsidiaries of the Company within the two years preceding the date of this prospectus.

B. FURTHER INFORMATION ABOUT THE BUSINESS

1. Summary of material contracts

The following contracts (not being contracts entered into in the ordinary course of business) have been entered into by the Company or its subsidiaries within the two years preceding the date of this prospectus and are or may be material:

(i) a non-competition agreement (in Chinese) dated 25th October, 2002 between the Company and Parent Company whereby Parent Company undertakes, for nil value, not to compete with the Company as long as (a) the Company maintains its listing status on the Stock Exchange and (b) Parent Company owns 30% or more of the issued share capital of the Company or controls the Board;

(ii) an indemnity agreement (in Chinese) dated 25th October, 2002 between the Company and Parent Company whereby Parent Company gave certain representations, undertakings, warranties and indemnities, for nil value, in favour of the Company in respect of the assets it has injected into or transferred to the Company since the Company's inception;

(iii) the Purchase Option Agreement (in Chinese) dated 30th May, 2002 and amended by a supplemental agreement dated 25th October, 2002, between the Company and Parent Company, pursuant to which Parent Company has granted, for nil value, to the Company options to purchase from Parent Company any aeronautical or non-aeronautical businesses and assets owned or to be owned by it now or in the future subject to the terms and conditions contained therein;

(iv) the Asset Swap Agreement (in Chinese) dated 30th May, 2002 and supplemented on 25th October, 2002 between the Company and Parent Company, pursuant to which Parent Company has agreed to transfer its interest in certain assets with a total value of approximately RMB78.13 million to the Company in consideration of certain assets to be transferred from the Company with a total value of approximately RMB28.40 million and a cash settlement in the amount of approximately RMB49.73 million;

(v) an airport composite services agreement (in Chinese) dated 25th October, 2002 between the Company and Parent Company, whereby Parent Company has agreed to provide to the Group certain airport related composite services as discussed in the "Business — Connected Transaction" section of this prospectus. The charges for such services are set based on the actual cost plus certain margin in the range of 5% – 25%, except for security inspection which is based on CAAC's prescribed rate;

(vi) the Agreement on Runway (in Chinese) dated 25th October, 2002 between the Company and Parent Company whereby Parent Company has agreed to, inter alia, operate and maintain the runway; the Company has agreed to share with Parent Company the aircraft movement fees (for domestic, Hong Kong, Macau and foreign airlines), passenger charges (for domestic airlines) and the basic ground handling fees (for Hong Kong, Macau and foreign airlines) chargeable to airline customers in the ratio prescribed by the relevant PRC authorities from time to time. The current ratio is 25% to Parent Company and 75% to the Company;

(vii) a trademark licensing agreement (in Chinese) dated 25th October, 2002 between the Company and Parent Company whereby in consideration of an annual fee of RMB1 paid by Parent Company and the assistance to be provided by Parent Company in promoting the trademarks, the Company has granted to Parent Company a non-exclusive licence to use the trademarks for a period of 10 years;

(viii) an office lease agreement (in Chinese) dated 25th October, 2002 between the Company and Parent Company whereby the Company has agreed to rent from Parent Company office premises with a total gross floor area of approximately 1,415 m^2 for a term of 5 years at an annual rental of RMB509,400 for the first three years;

(ix) a transfer of land use rights agreement (in Chinese) dated 25th October, 2002 between the Company and Parent Company. According to the agreement, Parent Company has agreed to transfer the land use rights it holds in a parcel of land with a total area of approximately 39 hectares to the Company for a total consideration of RMB94,380,000;

(x) a mortgage agreement (in Chinese) dated 20th September, 2001 between the Company, Parent Company and China Development Bank. Pursuant to the agreement, Parent Company provided, for nil value, security upon a parcel of land of total area of 34.02 hectares in which it owns the land use rights, in favour of China Development Bank in the PRC in respect of the bank facilities granted by such bank to the Company;

(xi) a contractual operation agreement (in Chinese) dated 12th August, 2002 between the Company and Yangzi Express whereby the Company has contracted the were operation and management of its cargo centre to the latter for a fixed annual concession fee in the amount of RMB18 million for two years;

(xii) a logistic composite service agreement (in Chinese) dated 25th October, 2002 between HNA Group and the Company whereby HNA Group has agreed to provide or procure its subsidiaries to provide certain logistic services to the Company. The charges for such services are set based on the actual cost plus certain margin (as the case may be) in the range of 1%–5%;

(xiii) the Technical Services Agreement dated 16th September, 2002 and amended by a supplemental agreement on 30th October, 2002 between the Company and CADI in relation to provision of certain technical and advisory services by CADI to the Company for certain fees as disclosed in the Business section of this prospectus;

(xiv) the Sanya Management Contract (in Chinese) dated 23rd August, 2002 between the Company and SPIA whereby the Company has agreed to be responsible for the day-to-day operation of Sanya Airport for agreed management fees as disclosed in the Business section of this prospectus;

(xv) the Public Offer Underwriting Agreement dated 5th November, 2002 between the Company, Parent Company, the Public Offer Underwriters and HSBC Nominees (Hong Kong) Limited relating to the Public Offer. Details of the agreement are set out in the section headed "Underwriting — Underwriting Arrangements and Expenses" of this prospectus; and

(xvi) the Strategic Investment Agreement dated 16th September, 2002 and amended on 30th October, 2002 between the Company, the Strategic Investor and the Strategic Placing Underwriter. Details of the agreement are out in the section headed "Structure of the Offering — The Strategic Placing".

2. Intellectual Property Rights of the Company

Intellectual Property Rights of the Company

The Company has applied for registration of the trademarks/service marks listed below with the State Trademark Bureau on 2nd August, 2002. The Company has also granted a non-exclusive licence to use those trademarks set out below to Parent Company for a period of 10 years starting from 1st January 2002 on terms as set out in a Trademark Licensing Agreement dated 25th October, 2002 between Parent Company and the Company:

Trademarks	Registration Class applied for	Major items covered	Application No.
MEILAN	29–32, 35–45	consumer products (food, beverage, salt, etc.), advertising, management consultancy, financial services, agency business, aircraft maintenance, media, luggage handling, cargo agency and transport, mails and goods delivery, road and air transportation, storage and warehouse leasing, travel agency and tourism, processing, entertainment, education, hotel and restaurant, gardening, etc.	3261779, 3261845–3261849, 3261780–3261788
	29–32, 35–45	consumer products (food, beverage, salt, etc.), advertising, management consultancy, financial services, agency business, aircraft maintenance, media, luggage handling, cargo agency and transport, mails and goods delivery, road and air transportation, storage and warehouse leasing, travel agency and tourism, processing, entertainment, education, hotel and restaurant, gardening, etc.	3261799–3261808, 3261855–3261858, 3261920

Trademarks	Registration Class applied for	Major items covered	Application No.
美兰	29–31, 35–45	consumer products (food, beverage, salt, etc.), advertising, management consultancy, financial services, agency business, aircraft maintenance, media, luggage handling, cargo agency and transport, mails and goods delivery, road and air transportation, storage and warehouse leasing, travel agency and tourism, processing, entertainment, education, hotel and restaurant, gardening, etc.	3261850–3261854, 3261789–3261798

C. FURTHER INFORMATION ABOUT DIRECTORS, SUPERVISORS AND STAFF

1. Particulars of the service contracts of the Directors and Supervisors

(i) Each of the executive Directors has entered into a service agreement with the Company. Particulars of these agreements, except as indicated, are in all material respects identical and are set out below:

(a) Each service agreement is for an initial period of three years commencing from the date of appointment by the Company's general meeting (namely, 21st December, 2000 for Mr. Chen Wenli and Mr. Zhang Han'an; 19th July, 2002 for Mr. Liu Lu).

(b) The annual salary payable to each of Mr. Chen Wenli, Mr. Zhang Han'an and Mr. Liu Lu is RMB164,796, RMB143,196 and RMB101,640 starting from 1st September, 2002, respectively. The director's annual salary is subject to adjustment by the Company's general meeting.

(c) Each of the executive Directors is entitled to such management bonus, calculated by reference to the audited net profits of the Company in the previous year and decided by the shareholders at general meeting, provided that the aggregate sum of such bonuses and the bonuses payable to the management of the Company shall not exceed 2% of such profits in the previous year.

(ii) Each of the non-executive Directors and the Supervisors has entered into a service contract with the Company. Each service contract is for a term of three years commencing from 21st December, 2000, the date those non-executive Directors and the Supervisors were appointed by the Company's general meeting (save for the service contracts of Mr. Xu Boling which is from 29th June, 2001 and Mr. Meng Jianqiang and Ms. Zeng Xuemei which are both from 19th July, 2002). Each non-executive Director is entitled to a director's fee in the amount of RMB50,000 per year and each independent non-executive Director RMB80,000 starting from 1st September, 2002. Each Supervisor is entitled to a supervisor's fee in the amount of RMB20,000 per year starting from 1st September, 2002.

2. Directors' and Supervisors' remuneration

The aggregate amount of salaries, housing allowances, other allowances, benefits in kind, bonuses paid by the Company to the Directors and the Supervisors for the year ended 31st December, 2001 was approximately RMB248,000. Approximately RMB22,000 was paid by the Company as its contribution to the pension schemes in respect of its Directors and Supervisors in the year ended 31st December, 2001.

It is estimated that an aggregate amount of approximately RMB579,000 and RMB91,000, including the benefits and contributions mentioned above, will be paid to the Directors and the Supervisors as remuneration by the Company in respect of the year ended 31st December, 2002 pursuant to the present arrangements.

3. Disclosure of interest in the share capital of the Company and its associated corporations

Immediately following the Offering, none of the Directors and Supervisors will have any interests in equity securities of the Company and its associated corporations (within the meaning of the SDI Ordinance) which will have to be notified to the Company and the Stock Exchange pursuant to section 28 of the SDI Ordinance (including interests which they are taken or deemed to have under section 31 of, or Part 1 of the Schedule to, the SDI Ordinance), or which will be required, pursuant to section 29 of the SDI Ordinance to be entered in the register referred to therein or pursuant to the Model Code for Securities Transactions by Directors of Listed Companies, to be notified to the Company and the Stock Exchange once the H Shares are listed.

4. Substantial Shareholders of the Company and its subsidiaries

(i) So far as the Directors are aware, the following persons will immediately following completion of the Global Offering but without taking account of any H Shares which may be issued upon the exercise of the Over-allotment Option, be interested in 10% or more of the shares carrying rights to vote in all circumstances at general meetings of the Company:

Name	Number of Shares	Percentage of total registered capital
Parent Company	237,500,000 Domestic Shares	53%
Strategic Investor	89,700,000 H Shares	20%

(ii) So far as any Director is aware and save as otherwise disclosed herein, the companies (other than members of the Group) directly or indirectly interested in 10% or more of the voting power at general meetings of the subsidiaries of the Company are as follows:

Name of owner	Name of Subsidiary	Percentage of shares/equity interest
Parent Company	Meilan Travelling	40%

(iii) Save as disclosed herein, but not taking into account any H Shares which may be taken up under the Offering, the Directors are not aware of any legal person or individual (not being any Director) who will, immediately following the completion of the Offering, be directly or indirectly interested in 10% or more of the Shares then in issue, or an equity interest in any subsidiary of the Company representing 10%, or more of the equity interest in such subsidiary.

5. Disclaimers

Save as disclosed in this prospectus:

(i) none of the Directors or Supervisors has any interest in any Shares or debentures of the Company or any associated company within the meaning of the Securities (Disclosure of Interests) Ordinance ("SDI Ordinance"), which will have to be notified to the Company and the Stock Exchange pursuant to section 28 of the SDI Ordinance (including interests which he is deemed to have under section 31 of, or Part I of the Schedule to, the SDI Ordinance) or which will be required, pursuant to section 29 of the SDI Ordinance, to be entered in the register referred to therein or which will be required to be notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies in each case once the H Shares are listed;

(ii) none of the Directors or Supervisors nor any of the parties listed in paragraph D6 of this Appendix is interested in the promotion of the Company, or in any assets which have, within the two years immediately preceding the issue of this prospectus, been acquired or disposed of by or leased to the Company or its subsidiaries, or are proposed to be acquired or disposed of by or leased to the Company or its subsidiaries;

(iii) none of the Directors or Supervisors nor any of the parties listed in paragraph D6 of this Appendix is materially interested in any contract or arrangement subsisting at the date of this prospectus which is significant in relation to the business of the Company;

(iv) save in connection with the Underwriting Agreements, none of the Directors or Supervisors nor the parties listed in paragraph D6 of this Appendix:

(a) is interested legally or beneficially in any shares in the Company or its subsidiaries;

(b) has any right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in the Company or its subsidiaries;

(v) save as disclosed in this prospectus, none of the Directors or Supervisors has entered or is proposed to enter into a service contract with the Company or its subsidiaries (other than contracts expiring or determinable by the employer within one year without payment of compensation other than statutory compensation);

(vi) no amount or benefit has been paid or given within the two years preceding the date of this prospectus to the Promoters of the Company nor is any such amount or benefit intended to be paid or given; and

(vii) save as disclosed in the "Business" section of this prospectus and except that Mr. Chen Wenli and Mr. Zhang Han'an hold 35,640 and 23,970 staff shares, respectively, in Hainan Airlines, none of the Directors or the Supervisors or their associates or the Promoters has any interest in the five largest suppliers or customers of the Company.

D. OTHER INFORMATION

1. Estate Duty

The Directors have been advised that no material liability for estate duty under PRC law would be likely to fall upon the Company or its subsidiaries.

2. Litigation

Neither the Company nor any of its subsidiaries is engaged in any litigation or arbitration of material importance and no litigation or claim of material importance is known to the Directors to be pending or threatened by or against the Company that would have an effect on the Company's results of operations or financial condition.

3. Promoters

The promoters in connection with the establishment of the Company are the Promoters as defined in this prospectus. Save as disclosed in this prospectus, no amount or benefit has been paid or given to or is intended to be paid or given to the Promoters in connection with the Offering or the related transactions described in this prospectus.

4. Preliminary expenses

The preliminary expenses of the Company were approximately RMB400,000 and were paid by the Company.

5. Sponsors

HSBC and Oriental Patron have made an application on behalf of the Company to the Listing Committee of the Stock Exchange for listing of, and permission to deal in the H Shares. All necessary arrangements have been made enabling the securities to be admitted into CCASS.

6. Qualification of Experts

The qualification of the experts (as defined under the Listing Rules) who have given opinions in this prospectus are as follows:

Name	Qualifications
HSBC	Exempt dealer
Oriental Patron	Registered dealer and Investment Advisor
Ernst & Young	Certified Public Accountants
Vigers Hong Kong Limited	Professional Surveyors
Jun He Law Offices	Licensed Legal Advisors on PRC law
Commerce & Finance Law Offices	Licensed Legal Advisors on PRC law
Booz Allen Hamilton	Professional traffic consultants
Parsons Brinckerhoff (Asia) Limited	Professional engineering consultants

7. Consents of Experts

Pursuant to the relevant requirements under the Companies Ordinance and the Listing Rules, each of the experts listed under paragraph D6 above has given and has not withdrawn their respective written consents to the issue of this prospectus with copies of their reports, letters, valuation, opinions or summaries of opinions (as the case may be) and the references to their names in the form and context in which they respectively appear.

8. No Material Adverse Change

Save as disclosed in this prospectus, the Directors confirm that up to the Latest Practicable Date, there had been no material adverse change in the financial or trading position or prospects of the Company or its subsidiaries since 31st May, 2002.

9. No Business Interruption

There has not been any interruption in the business of the Company which has had a material adverse effect on the financial position of the Company in the two years preceding the date of this prospectus.

10. Binding Effect

This prospectus shall have the effect, if an application is made in pursuance hereof, rendering all persons concerned bound by all the provisions (other than the penal provisions) of sections 44A and 44B of the Companies Ordinance of Hong Kong so far as applicable.

11. Miscellaneous

(i) Save as disclosed in this prospectus:

(a) within the two years preceding the date of this prospectus, no share or loan capital of the Company has been issued or agreed to be issued fully or partly paid either for cash or for a consideration other than cash;

(b) no share or loan capital of the Company is under option or is agreed conditionally or unconditionally to be put under option;

(c) neither the Company nor any of its subsidiaries has issued or agreed to issue any founder shares, management shares or deferred shares; and

(d) since the date two years prior to the date of this prospectus, no commissions, discounts, brokerage or other special terms have been granted in connection with the issue or sale of any shares of the Company or any of its subsidiaries.

(ii) The Company does not intend to apply for the status of a Sino-foreign investment joint stock limited liability company in the PRC and does not expect to be subject to the Provisional Regulations of the Ministry of Foreign Trade and Economic Cooperation on Certain Issues Concerning the Establishment of Companies Limited by Shares with Foreign Investment.

(iii) None of the equity and debt securities of the Company is listed or dealt in any other stock exchange nor is any listing or permission to deal being or proposed to be sought.

(iv) The Company has no outstanding convertible debt securities.

12. Particulars of the Vendors

Particulars of the Vendors are as follows:

Name	Number of Domestic Shares to be converted into Sale H Shares	Description	Address
Central South Aviation Development.	2,775,000	Corporation	Baiyun Airport, Guangzhou City, Guangdong Province, the PRC
China Southern Airlines. .	925,000	Corporation	Baiyun Airport, Guangzhou City, Guangdong Province, the PRC

None of the Directors and Supervisors is interested in the sale of the Sale H Shares under the Offering.

1. DOCUMENTS DELIVERED TO THE REGISTRAR OF COMPANIES

The documents attached to the copy of this prospectus delivered to the Registrar of Companies in Hong Kong for registration were copies of the **WHITE** and **YELLOW** application forms, the written consents referred to in paragraph D7 of Appendix X, the statement of adjustments made by Ernst & Young in auditing the figures set out in their Accountants' Report set out in Appendix I, a statement of the description of the Vendors referred to in paragraph D12 of Appendix X and copies of the material contracts referred to in paragraph B1 of Appendix X.

2. DOCUMENTS AVAILABLE FOR INSPECTION

Copies of the following documents will be available for inspection at the offices of Deacons at 3rd–7th, 18th and 29th Floors, Alexandra House, 16–20 Chater Road, Central, Hong Kong during normal business hours up to and including 20th November, 2002:

(a) the Articles of Association (in Chinese) together with a certified English translation;

(b) the Accountants' Report on the Group prepared by Ernst & Young, the text of which is set out in Appendix I, together with the statement of adjustments;

(c) the letters relating to the profit forecast, the texts of which are set out in Appendix III;

(d) the letters, summary of valuation and valuation certificate relating to the property of the Company prepared by Vigers Hong Kong Limited, the texts of which are set out in Appendix IV;

(e) the letter setting out a summary of the air traffic consultants' report prepared by Booz Allen Hamilton, the text of which is set out in Appendix V;

(f) the letter setting out a summary of the engineering consultants' report prepared by Parsons Brinckerhoff (Asia) Ltd., the text of which is set out in Appendix VI;

(g) the material contracts referred to in paragraph B1 of Appendix X, where appropriate, together with certified English translation thereof;

(h) service agreements (in Chinese) between the Company and each of the Directors and Supervisors together with certified English translation, the material particulars of which are set out in paragraph C1 of Appendix X;

(i) the written consents of experts referred to in paragraph D7 of Appendix X;

(j) the PRC legal opinion issued by Jun He Law Offices, the legal advisers to the Company on PRC law as described in paragraph 4 of Appendix IX;

(k) the Company Law, together with an unofficial English translation;

(l) the Special Regulations, together with an unofficial English translation; and

(m) the Mandatory Provisions, together with an unofficial English translation.