
HAINAN AIRLINES COMPANY LIMITED

2003 ANNUAL REPORT

Important Notice

The Board of Directors of HNA guarantees that there is no significant omission, fictitious description or serious misleading of information and take both individual and joint responsibilities for the truthfulness, accuracy and completeness of the content.

Mr. Chen Feng, Chairman of HNA, Mr. Zhu Yimin, CEO & CFO of HNA (in charge of accountancy), Mr. Zhang Yi, General manager of Plan and Financial Department of HNA (in charge of accounting division) declare here that: they guarantee the accuracy and completeness of the financial report in this annual report.

Board of Directors of HNA

Date: April 29, 2004

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I. Company Profile

1. Registered Chinese name : 海南航空股份有限公司

Registered English name : Hainan Airlines Co., Ltd (Shortened as HNA)

2. Legal Representative: Chen Feng

3. Information of the Secretary to the Board and the Security Representative

Secretary to BoD: Zhang Shanghui

E-mail: sh_zhang@hnair.com

BoD representative of security affairs: Lv Guangwei

E-mail: gw_lv@hnair.com

Office Address: Haihang Development Building, 29 Haixiu Road, Haikou, Hainan, China.

Tel: 0898-66739961

Fax: 0898-66739960

4. Registered Address: 168 Airport West Road, Haikou, Hainan, China

Office Address: Haihang Development Building No.29 Haixiu Road Haikou

Zip Code: 570206

Website: <http://www.hnair.com>

Email: webmaster@hnair.com

5. Designated Newspapers to Publish HNA's Information:

China Securities News, Shanghai Securities News, Wen Wei Po (Hong Kong)

Website Publishing the Report: <http://www.sse.com.cn>

Annual Report Available at: Securities Department of HNA

6. Stock Listed at: Shanghai Stock Exchange

Stock Name: Hainan Airlines

Stock Code: 600221

Stock Name: HNA B share

Stock Code: 900945

7. Miscellaneous

Date and place of the first incorporation registration: October 1989 in Haikou

Registered number of business operation certificate: Qi Gu Qiong Zong Zi No. 008368

Registered number of taxation certificate: 1150805791

Address of the Accounting Firm:

Domestic Accounting Firm: Shine Wing Certified Accountants

Office address: 6 Xin Yuan Nan Lu, Chaoyang District, Beijing

Overseas Accounting Firm: Price Water House Coopers Public Accounting Firm

Office address: 10 Hysan Avenue, Causeway Bay, Hongkong

II. Key Fiscal and Business Data

I. Key Fiscal and Business Data of this year:

Total amount of Profit (RMB):	-1,474,615,013
Net Profit (RMB):	-1,269,246,223
Net profit after non-recurring profit and loss (RMB):	-1,266,134,820
Profit from principal business (RMB):	45,304,021
Profit from other operations (RMB):	31,801,811
Operating profit (RMB):	-1,458,872,444
Income from investment (RMB):	-12,631,165
Subsidy Income (RMB):	8,466,428
Net Non-operating Income (RMB):	-11,577,832
Net cash flow from operating activity (RMB):	-644,977,250
Net cash increase (RMB):	1,542,393,832
Net profit (according to the International Accounting Regulation)	-1,115,704,000

Note: (1) The item of non-recurring profit and loss deducted indicates:

Non-operating income: RMB 11,995,468 Yuan

Non-operating expenses: RMB -23,573,300 Yuan

Subsidy Income: RMB 8,466,468 Yuan

Total: RMB -3,111,404 Yuan

(2) Adjustments to premium profit to the consolidated shareholders with statutory accounts in China in accordance with international accounting standards (IAS)

Dec. 31st 2003

	Profit proportion of the shareholders RMB 1,000	Consolidated Net Assets RMB 1,000
As per domestic audited accounts	1,269,247	1,116,360
As per IAS and other adjustments		
Amortization of Long-term deferred Expenses	16,785	151,687
Increase in interest of finance lease	20,972	242,581
Depreciation Adjustment	136,800	109,383
Adjustment to the business credit	853	8,024
Influence of deferred tax	20,027	44,218
Other	50	430
After IAS and other adjustments	1,115,704	883,287

II. Key Fiscal and Business Data of the Previous Three Years As of the end of the Fiscal Year

N o.	Items	Unit	2003	2002		2001	
				Before Adjustment	After Adjustment	Before Adjustment	After Adjustment
1	Profit from principal business	RMB	5,372,091,313	5,028,281,733	5,028,281,733	3,254,753,740	3,254,753,740
2	Net profit	RMB	-1,269,246,223	181,150,923	103,056,129	100,302,701	151,847,497
3	Total assets	RMB	23,106,733,501	19,400,958,098	19,374,408,100	15,004,326,205	15,055,871,001
4	Shareholder's equity (excluding minority interest)	RMB	1,116,359,615	2,382,945,724	2,400,210,894	2,184,004,969	2,235,549,767
5	Income per share	RMB /Share	-1.74	0.25	0.14	0.14	0.21
6	Net assets per share	RMB /Share	1.53	3.26	3.29	2.99	3.06

7	Net assets per share after adjustment	(RMB /Share)	0.80	2.31	2.33	2.28	2.35
8	Net cash flow from operating activity per share	(RMB /Share)	-0.88	1.45	1.45	1.86	1.86
9	Equity ratio	(%)	-113.70	7.60	4.29	4.59	6.79
10	Weighted average Yield of net assets	(%)	-72.01	7.96	4.24	4.61	6.86

Addendum to Income Statement prepared in accordance with the *Regulation on Information*

Disclosure of Companies Issuing Public Securities (No. 9) promulgated by SRSC:

(Unit : RMB Yuan)

Item	Profit in Report Period	Rate of Return on Equity (%)				Income per share (RMB Yuan)			
		Overall Diluted		Weighted Average		Overall Diluted		Weighted Average	
		2003	2002	2003	2002	2003	2002	2003	2002
Profit from principal business	45,304,020	4.06	49.82	2.58	50.92	0.06	1.64	0.06	1.64
Operating profit	-1,458,872,445	-130.68	5.14	-82.97	5.25	-2.00	0.17	-2.00	0.17
Net profit	-1,269,246,224	-113.70	4.29	-72.19	4.39	-1.74	0.14	-1.74	0.14
Net profit after non-recurring profit & loss	-1,266,134,820	-113.42	4.15	-72.01	4.24	-1.73	0.14	-1.73	0.14

III. Changes in Shareholder's Equity

Item	Period Beginning	Decrease	Period End
Share Capital	730,252,801		730,252,801
Capital Reserve	1,038,405,919		1,038,405,919
Surplus Reserve	169,097,575		169,097,575
Statutory Public Welfare Fund	53,094,720		53,094,720
Undistributed	462,454,599	-1,283,851,279	-821,396,679

Profit			
Total Shareholders' Equity	2,400,210,894	-1,283,851,279	1,116,359,616

III. Changes in Share Capital and Major Shareholders

I. Changes in Share Capital

1. Share Changes

Unit: Share

	Period- beginning	Bonus Share Distributed					Period-end
1. Unlisted Share							
1) Founders' share							
Incl. :							
State share	17,289,355						17,289,355
Domestic legal person share	117,547,200						117,547,200
2) Collection legal person share							
Domestic legal person share	38,735,280						38,735,280
Foreign legal person share							
3) Employee share							
Total Unlisted Share	173,571,835						173,571,835
2. Listed Share							
1) RMB Ordinary share	371,957,765						371,957,765
2) Foreign share listed at home (B share)	184,723,201						184,723,201
Total Listed Share	556,680,966						556,680,966
3. Total share	730,252,801						730,252,801

Note: Following the approval Zheng Jian Gong Si Zi [2003] No. 2 issued by CSRC, approved the unregistered

foreign capital share held by American Aviation LDC changed to be B Share, since Jan 16, 2003, one year later, listed on the Shanghai Stock Exchange.

2. Share Issuing and Listing

1) On Oct. 11 of 1999, the 205,000,000 A-shares of the Company were issued, including 57,635,669 shares placed to the legal person shareholders on the STAQ system at the ratio of 10:5, 41,000,000 shares to the fund investors and others issued through the trading network.

On Nov. 25 of 1999, the 164,000,000 A-shares of the Company were listed at Shanghai Stock Exchange with the shortened name as “海南航空”. According to the relative regulations, the 41,000,000 shares placed to the fund investors were frozen until Jan. 25 of 2000.

2) Since there's no share distribution, ration, new-issuance or transferring into share capital occurred in the report period, the structure and total amount of the Company's shares kept unchanged.

3) Issuing date of the employee shares: September of 1992

Issuing price of the employee shares: RMB1.00 Yuan per share

Issuing amount of the employee shares: 50,000,000 shares.

II. Shareholders

1. By the end of the fiscal year, the total number of shareholders is 136,357, including 117,536 shareholders with A Share, 18,821 shareholders with B Share.

2. Top 10 Shareholders

	Shareholder	Shares held (In share)	(%)
1	American Aviation LDC (foreign shareholder of unlisted share)	108,043,201	14.80
2	HNA Group Company Ltd.	53,341,200	7.3
3	Hainan Qixing Industrial Investment Co., Ltd.	49,904,680	6.8
4	China Everbright Group Limited	33,207,818	4.5
5	State Property Administration Bureau of Hainan	17,289,355	2.37
6	China International Travel Agency (head office)	6,480,000	0.89

7	Bank of Communications, Hainan Branch	6,480,000	0.89
8	Shanghai Baosteel Chemical Co., Ltd	4,474,036	0.61
9	Beijing Fieldtrade Corporation	4,230,000	0.59
10	Century Securities Co., Ltd	4,241,778	0.58

Note: The Company knows neither whether there's any connected relationship among the top 10 shareholders nor any of them are concerted actor defined by the Regulations on Information Disclosing of Changes in the Shares Held by the Shareholders of the Listed Company.

No strategic investors or ordinary legal person ranked in the top 10 shareholders of the Company through placement of new shares.

3. Top 10 listed shareholders

	Shareholder	Shares held (In share)	Share Character
1	China Everbright Group Limited	6,704,618	A Share
2	Shanghai Baosteel Chemical Co., Ltd	4,474,036	A Share
3	Century Securities Co., Ltd	4,241,778	A Share
4	Hainan Qixing Industrial Investment Co., Ltd.	3,285,400	A Share
5	Boshi Fund Management Co., Ltd	2,000,000	A Share
6	He Jun (Personal shareholder)	1,526,426	A Share
7	Su Zhou Trust & Investment Corporation	1,426,753	A Share
8	Pang Jian (Personal shareholder)	1,231,786	A Share
9	Southern Fund& Management Co., Ltd	1,224,118	A Share
10	Hainan Gang'ao International Trust & Investment Corporation	1,150,848	A Share

Note: The Company knows neither whether there's any connected relationship among the top 10 shareholders of circulation shares nor any of them are concerted actor defined.

4. Introduction to the main shareholder

American Aviation LDC (holding 14.8% equity interest)

Legal representative: Ronald O. Drake

Date of establishment: July 7th 1995

Registration capital: 50,000 common stock and USD 1 per share

Share Structure: American Aviation LTD 25,000 shares
Quantum Industrial Partners, LDC 25,000 shares

Main business and products: deals with investment, obtaining and holding, on behalf of the company itself or any designated person, stocks, bonds, loan stock, bills and other securities issued or guaranteed by any government, sovereign ruler, consignor, public institution or highest authority, independent governing authority, municipal or local government across the world.

HNA Group Company Limited (holding 7.31% equity interest)

Legal representative: Chen Feng

Date of establishment: Apr. 16th 1998

Registration Capital: RMB 500,000,000

Share Structure: Hainan Communication Administration Holding Co., Ltd holds 70%,
Guangzhou Construction Investment Co., Ltd holds 30%.

Main business and products: Airlines transport, investment and management in airport and hotel golf court; information technology service; investment and development in real estate; import and export trade of airplane and related materials (operating according to the license); investment in energy, transport, new technology and new material.

There is no change of the holding status during the report term.

V. Directors, Supervisors, Senior Managers and Staff

I. Current directors, supervisors, senior managers and staff

Name	Gender	Age	Term period	Balance of stockholding	Position
Chen Feng	Male	51	2003—2006	4.14	Board Chairman
Wang Jian	Male	43	2003—2006	3.62	Vice Chairman
Tan Xiangdong	Male	37	2003—2006	2.59	Director
Li Qing	Male	47	2003—2006	3.75	Director

Ke Deming	Male	69	2003—2006	--	Independent Director
Yang Hui	Male	66	2003—2006	--	Independent Director
Wang Zhi	Male	62	2003—2006	--	Independent Director
Ronald O. Drake	Male	48	2003—2006	--	Director
Iain Aitken	Male	50	2003—2006	--	Director
Zhang Cong	Male	45	2003—2006	--	Supervisor
Chen Ping	Male	29	2003—2006	--	Supervisor
Li Rui	Male	27	2003—2006	--	Supervisor
Qian Daoyun	Male	53	2003—2006	--	Supervisor
Zhao Zongtao	Male	52	2003—2006	--	Supervisor
Zhu Yimin	Male	43	2002—2005	--	CEO
Zhao Zhongying	Male	56	2002—2005	--	Executive President
Shu Weidong	Male	39	2002—2005	--	Vice Executive President
Wang Yingming	Male	41	2003—2006	--	Vice Executive President
Du Xiaoping	Male	43	2001—2004	--	Vice Executive President
Qin Jianmin	Male	53	2001—2004	--	Vice Executive President
Zhang Yi	Male	33	2003—2006	--	CFO
Zhang Shanghui	Male	33	2003—2006	--	Secretary to the Board

Note: 1.Chairman of the Board (Chen Feng) and Vice Chairman of the board (Wang Jian) are also the Chairman and Vice Chairman of the Board of HNA Group Co., Ltd.,

2.Within the report period, the holding shareholder of HNA does not change.

II. Annual Reward

The reward of directors, supervisors and senior managers: the reward of directors is distributed according to the Stipulation on HNA President Fund passed through on 23rd Session of 3rd Meeting of BoD and the General Meeting of Shareholders 2002, the reward of senior managements was distributed according to the items on annual evaluation of the management and their performance during the year.

The total amount of the reward of the current directors, supervisors and senior managers is RMB 1,961,300 Yuan, among which the reward of the top 3 directors is RMB 566,400 Yuan and that of the top 3 senior managers is RMB 440,600 Yuan.

The allowance of the Independent directors of this Company and other treatment::

The Independent directors enjoy the allowance according to the allowance standard of the current directors of HNA, which is RMB 50,000 Yuan per year, and it is distributed on the General Meeting of Shareholders of the year.

Yearly income for over RMB 200,000 Yuan: 1 person; Yearly income for RMB 100,000-200,000 Yuan: 6persons; Yearly income for RMB 50,000-100,000 Yuan: 7 person; Yearly income under RMB 50,000 Yuan: 8 persons.

III. Directors and, supervisors and senior managements resigned during the report period and the reason

1. Employment and unemployment of Manager, Deputy Manager, CFO and Secretary to BoD.

Mr. Chen Feng, Mr. Wang Jian, Mr. Tan Xiangdong, Mr. Li Qing, Mr. Ke Deming, Mr. Yang Hui, Mr. Wang Zhi, Mr. Ronald O. Drake and Mr. Iain Aitken were selected to be the director of HNA. It has been approved on the General Meeting of Shareholders 2002.

Mr. Zhang Cong, Mr. Chen Ping, Mr. Li Rui, Mr. Qian Daoyun and Mr. Zhao Zongtao were selected to be the supervisor of HNA. It has been approved on the General Meeting of Shareholders 2002.

It was considered and approved on the 23rd Session of the 3rd Meeting of the Board of Directors that Mr. Zhang Yi would be the CFO of HNA.

It was considered and approved on the 1st Session of the 4th Meeting of the Board of Directors that Mr. Wang Yingming would be vice executive president of HNA.

2. Staff

By the end of the report period, HNA has 6846 staffs in total, including 1340 pilots, 1004 flight stewardess, 1075 maintenance personnel, 274 technical personnel, and the other is 3153. Among these employees, 64 people

have the post graduate degrees, accounting for 0.93% of the total employees; 1995 people have undergraduate degrees, 29.41% of the total; 2190 people were graduated from junior colleges, 31.99% of the total, and 2597 people received professional education, 37.93% of the total. There were 44 retired employees.

V. Administration Structure of HNA

I. Current Structure

Ever since its listing, HNA has been perfecting the legal representatives administration structure, regulating its operation, and enhancing the information release, strictly in accordance with the requirement of *the Company Law*, *the Security Law*, the related regulations by CSRC and *Listing Regulation of SSE*. And here is the brief of the current administration construction:

1. Shareholders and Meeting of Shareholders: HNA ensures that all shareholders, especially the small and medium ones, enjoy the same status and rights equally as the major ones. The company website has been established to keep efficient communications with shareholders and make them aware of the operating situation of the Company. Regulation on shareholders meeting was formulated, and the General Meetings of Shareholders were held strictly according to *The Rules of the General Meeting of Shareholders* issued by CSRC while the shareholders were encourage to participate in the meetings and to vote as much as possible and lawyers are employed to present as witnesses. The pricing of the related business cooperation is fair, and the independent financial consultants submitted independent financial reports so that all the related business cooperation is legal and effective by strictly following the procedures of BoD and Board of Supervisors as stipulated by *Listing Regulation of SSE*.

2. Holding Shareholders and HNA: The holding shareholders exert their rights through General Meetings of Shareholders, and are not directly involved in the policy-making and operation and management of HNA. HNA is independent with the holding shareholders in staff, assets, finance, constructing and business, and the BoD, Board of Supervisors and the interior departments can run independently.

3. Directors and BoD: HNA employs the directors strictly according to the Articles of Association of HNA. The number and organization of directors agree with the laws, stipulation and the Articles of Association of HNA. The directors of HNA attend the meetings of BoD and meetings of shareholders seriously, and are familiar with the related laws and stipulation, and aware of their rights, obligation and responsibility as a director.

4. Supervisors and the Board of Supervisor: The number and organization of Board of Supervisor agree with the laws, stipulations and the Articles of Association of HNA. *Rules on Process of Board of Supervisors* has been formulated, and perfected during practice. Supervisors of the HNA perform their responsibility seriously and supervise the performance of directors, managers and other senior management personnel.

5. Evaluation, encourage and restriction mechanism: HNA is actively formulating a just and transparent evaluation criterion and encouraging and restriction mechanism of directors, supervisors and managers. The employments of managers are exoteric and transparent, and comply with the related laws and stipulations.

6. Related beneficiary: HNA safeguards the legal rights and interests of the Banks, legal representatives, customers and other interest-related parties so as to maintain the sustainable and healthy development of HNA.

7. Information release and transparency: The secretary to the BoD is appointed to be in charge of the information release, reception and consultation, and enhance the communication with shareholders. HNA releases the true and complete information in time according to the related laws, stipulations and constitutions of HNA so that all the shareholders enjoy the equal opportunity to get the information. HNA releases in time the detailed information and the changes of major shareholders or the actual controlling party of the Company in accordance with related regulations.

II. Performance of the Independent directors

By now, the Company has three independent directors. In the report period, Mr. Key Deming, Mr. Yang Hui and Mr. Wang Zhi voted on 22nd Sessions of 3rd Meeting –4th Sessions of 4th Meeting of BoD, they have fulfilled his obligation as an independent director.

III. Independence of the Company with HNA Group in Staff, Assets, Finance, Operation and Organization:

HNA mainly deals with air passenger and cargo transportation. The production system, assisting production system and the sale system were independent from HNA Group Co., Ltd. HNA is independent from any shareholder company or related ones.

1. The Company has established the complete legal representative construction according to *The Company Law*. The general manager, deputy general manager and finance staffs do not hold any positions in the shareholders' companies or related companies, with the only exception that the Chairman of the BoD is also the Chairman of the HNA Group Co., Ltd. And in the Company the independent and complete management system

and constitution were established. The Company is independent in staff from the holding shareholders.

2. The Company has its own independent flight system, auxiliary flight system, corresponding facilities and equipment, real estate and trademark, and the delimitation in industrial property rights and non-patent technology is clear. The unavoidable relating dealings are completed according to the normal commercial stipulations, and the related directors fulfill the avoiding process according to the Constitution of HNA during voting on the General Meeting of Shareholders. The Company maintains relative assets integrity from the controlling shareholders.

3. The Company has its own flight, operating, sales and other departments with independent and complete flight, operation and sales systems. The purchasing of major spare parts and the sales of both passenger and cargo air transportation are operated independently.

4. The Company has independent President Administration Office, Office of Secretary to BoD, Operation Center, Planning & Financing Department, Human Resource Department, Operation Supporting Department, Marketing & Sale Department, Flight Operations Department, and Maintenance & Engineering Department. The administration offices and operation locations are completely separated and independent.

5. The Company has an independent financial department and has established independent accounting & managing system and separate bank accounts. HNA has its own tax registration number and it is independent in finance from the controlling shareholders.

IV. Evaluation, Encouragement and Reward Mechanism to Senior Management

The annual rewards of the senior managers are monthly distributed according to the related stipulation of salary control formulated by the Company. The Human Resource Department formulated the salary system according to the operation of the Company, and submits to BoD and General Meeting of shareholders to be considered.

The senior management evaluation system consists of the schema of organizer evaluation, the performance survey of other staff by the President of BoD, the routine reward stipulation of the Company and the evaluation schema of the general staff.

Moreover, the Company is employing a professional agency to formulate the evaluation and reward schema such as promissory shares, staff shareholder schema and annual salary system, etc.

VI. Brief Introduction to the General Meetings

In 2003, the Company convened two shareholders' general meetings, including one annual shareholders' general meeting and one temporary shareholders' general meeting.

1. The General Meeting of Shareholders of 2002

On June 13 of 2003, it was held at the conference hall on 4th floor of Haihang Development Mansion, 29 Haixiu Rd., Haikou, Hainan province. Shareholders and proxies attended the Meeting were 12, representing 241,612,420 shares, 33.09% of the total shares (incl. B-shareholders representing 360 shares), which conformed to the regulations of the Company Law and the Articles of Association of the Company. The meeting was presided over by Mr. Chen Feng, chairman of the Company. During the meeting, 2002 Work Report of Board of Directors of HNA, Report on the Performance of the Board of Supervisors, Financial Report of 2002 & Financial Plan of 2003, Report on Proposed Profit Distribution Plan for 2002, Report on Plan of Annual Salary of Directors, Supervisors and Management Personnel, Report on Term-shift Election of the Board of Directors, Report on Term-shift Election Of the Board of Supervisors, Report on Amendment of the Articles of Association of HNA, Report on Authorizing the Board to Adjust New Transport Capacity of the Company with Leasing Method, Report on Terminating the transfer of 10 Dornier-328 Regional Aircrafts and 51% Holding Interests of Hainan Air Catering Co., Ltd., Report on Renewal of Employment of Accounting Firm, Report On Signing Daily Production Connected Transactions Agreement With Related Parties were considered and passed.

Mr. Liu Wei, lawyers of the Grandall Legal Group (Shanghai), had attended the meeting and issued the Legal Opinion.

The resolution of the meeting was published on the China Securities News, Shanghai Securities News and Hong Kong's Wen Wei of June 14 of 2003.

2. The First Temporary General Meeting of Shareholders of 2003

On Dec 30 of 2003, it was held at the conference hall on 4th floor of Haihang Development Mansion, 29 Haixiu

Rd., Haikou, Hainan province. Shareholders and proxies attended the Meeting were 5, representing 120,739,995 shares, 16.5% of the total shares (incl. B-shareholders representing 170,476 shares), which conformed to the regulations of the Company Law and the Articles of Association of the Company. The meeting was presided over by Mr. Chen Feng, chairman of the Company. During the meeting, Report on Termination of the Implementation on HNA Group Transfer the 85% Capital Contribution of Yangtze River Express to Chang'an Airlines and Report on 10% Capital Contribution of Yangtze River Express and Partial Assets Transfer of HNA were considered and passed through.

Miss Shi Nianqing, lawyers of the Grandall Legal Group (Shanghai), had attended the meeting and issued the Legal Opinion.

The resolution of the meeting was published on the China Securities News, Shanghai Securities News and Hong Kong's Wen Wei of Dec 31 of 2003.

VII. Report of Board of Directors

I. Business Review

In 2003, under the leadership of the board of directors and thanks to the associated efforts of executives and employees, Hainan Airlines earnestly implemented the working policy of "Meeting new opportunities and challenges, Improving core competitive power, Building world-class brand, Establishing a solid basis for the second leap of the Group" and maintained the quick, healthy and harmonious development tendency for the proprietors of the company focusing on "Safety, Integration, Benefits".

1. Scope and Operation of the Principle Business

1) In 2003, the income from the principal business of the Company reached RMB 5.372 billion, in which the total income from passenger transportation is RMB 4.997 billion Yuan, making up 93.9% of the total income from principal business, and the income from cargo transportation and surcharge on overweight baggage is RMB 169 million Yuan, accounting for 3.2% of the total income from principal business, and the rest income are from charter aircraft business, totaling RMB 155 million Yuan, accounting for 2.9% of the total income from the principle business. The profit from principal business reached RMB 45 million Yuan in the fiscal year.

2) In the year of 2003, the total passenger transportation volume reached 7.55 million person times, up 11.85% over the previous year; the total cargo and mail transportation volume reached 108 thousand tons, 27.05%

more than that of the previous year; the total transport turnover reached 1.087 billion ton*kilometers, an increase by 19.45% over that previous year.

3) In 2003, 12 aircrafts were imported, including 1 Boeing 737-800, 1 Boeing 767, 3 Boeing 737-700 and 7 Dornier328. .

There is no significant change made in the principal business during the report period.

2. Operation Results of the Major Subsidiaries

Name	Registered Capital	Equity Percentage	Principal Business	Sales Income RMB 10,000 Yuan)	Business Scope (RMB 10,000 Yuan)	Net Profit (RMB 10,000 Yuan)
Hainan Golden-deer Aviation Sales Co., Ltd.	RMB 8,000,000	95%	Ticket sales, air cargo transportation and chartered flight agency services	0	59,466	0
Hainan Aviation VIP Flight Service Co. Ltd.	USD 1,020,408	60%	Chartered flights agency	0	1,591	0
Hainan Air Catering Co., Ltd.	RMB 31,000,000	51%	Food and souvenirs for passengers	4,017	9,303	2,426
China Xinhua Airlines Co., Ltd.	RMB 1.83 billion	60%	Provision of transportation services	161,868	477,665	-34,331

Changan Airlines Co., Ltd.	RMB 754,390,000	73.51%	Provision of transportation services around Shan'xi Province	38,387	101,850	-28,362
Shan Xi Airlines Co., Ltd.	RMB 320,000,000	92.51%	Provision of transportation services around Shanxi Province	44,196	39,353	543
Beijing Xinhua Air Catering Co., Ltd	RMB 29,990,000	51%	Production and sale of pastry, food and beverage	0	3026	0
Shanxi Chang'an Hainan Aviation Star Hotel Co., Ltd.	RMB 25,000,000	80%	Hotel and catering, commodity, costume sales, typing and other office services.	297	2681	-117

3. Major Suppliers and Customers:

The purchase amount from the top 5 suppliers of the Company takes 20 % of the total purchase amount of it, which is mainly aviation fuels, materials, food and other applications. The sales turnover of the top 5 distributors of the Company takes 3.65 % of the sales turnover of it.

4. Problems and Strategies:

1) Intensify management reformation, perfect the construction of three systems of “Safety, Service, Operation”

We should intensify management reformation, advance the reformation of salary system and staffing mechanism, actively promote EVA (Economic Value Added) management evaluation system to make the development strategy, mechanism, management concept and regulations reflect the achievement of management

reformation. In addition, we should make the core concept of “Credit, Safety, Performance, Innovation” penetrate through daily administration, operation and production, fully quantify daily management and production work by means of advanced management concept and tools to carry out reformation on daily work and operation flows by way of reformation project and achieve the strategic development objective of our company.

2) Earnestly construct the safety system, service system and efficient operation system.

By fostering safety culture, building the safety organization system and increasing the safety investment, we should establish the complete safety guarantee system. Furthermore, we should perfect service systems of Hainan Airlines, make service flows clear taking customer requirements as center and market as orientation, and take the leader in introducing the service commitment in the industry.

3) Continue deepening the implementation of overall budget management, intensify the financial auditing and supervision

By developing qualified and priced overall budget targets, Hainan Airlines established the complete budget management evaluation system and strictly implemented a series of financial systems such as capital budgeting approval management, taxation management, external auditing and accounting to promote the assets management and auditing supervision of the company.

4) Resource sharing capacity remains to be improved and the scale merit of merge operation has not yet been put into full play

Clarify management frameworks and management relations of Hainan Airline and the three affiliated airline companies, distinguish between responsibilities and authorities, develop the corresponding regulations and operation flows in terms of human resources, financial management and production operation, bring the overall resources advantage of the block into full play, build the excellent brand of aviation group.

5) Put the location advantage into full play, perfect nationwide airline network layout, grasp the experiment chance of opening of Hainan aviation right, actively exploit international routes

With regard to airline network strategic layout, we will further establish the transfer lines network with Beijing and Xi’an as pivots. With regard to market development and construction of marketing channels, we will try to increase the market share of main areas and enhance the core competitive power. With regard to opening of international routes and development of international market, taking advantage of the opportunity of the opening

of Hainan's fifth aviation right, we will actively develop the international aviation market, vigorously improve traffic capacity, enlarge the international route operation right and international routes operation scale.

II. Investment

As of Dec. 31 of 2003, the balance of long-term investment of the Company accounted for RMB 1,018,900,000 Yuan, up 2.7% over the previous year.

1) Changes in Long-term Equity Investment: (Unit: RMB 10,000 Yuan)

2003.1.1	Increase	Decrease	2003.12.31
99,190	7,071	4,371	101,890

The Main reasons:

A. The Company, Xinhua Airline Co., Ltd., the subsidiaries of the Company and Beijing Dongya Xinxing Economics Development Co., Ltd. ("Beijing Xinxing") entered into an interest transfer agreement. Pursuant to which the Company and Xinhua Airline Co., Ltd. accepted Beijing Xinxing transfer to the interests of Chongqing Changjiang International Leasing Co., Ltd. Thereafter, the Company and Xinhua Airline Co., Ltd own an interest of 40% share capital of Chongqing Changjiang International Leasing Co., Ltd. jointly.

B. Xinhua Airline Co., Ltd. and Chang'an Airline Co., Ltd., the subsidiaries of the Company, and China International Public Relationship Association established Beijing Kehang Investment Co., Ltd. (Beijing Kehang) as dated in January 2003. The registered capital of Beijing Kehang is RMB 30,000 thousand. Xinhua Airline contributed RMB 15,000 thousand to own an interest of 50% share capital. Chang'an Airline and China International Public Relationship Association contributed RMB 7,500 thousand to own an interest of 25% share capital respectively. As at 31 December 2003, the total assets of Beijing Kehang is RMB 30,030 thousand, which is the 1.36% of the total assets of consolidation statement of the Company. Income and net income is zero. This company has not operated formally. Accordingly, Beijing Kehang is not consolidated in 2003.

C. In 2003, Xinhua Airline Co., Ltd., the subsidiaries of the Company, Hainan Aviation Jinpeng Sales Co., Ltd. and Hainan Aviation Hotel (Group) Co., Ltd. entered into an increasing Xinhua Airline United Transportation Co., Ltd.'s capital stated agreement. Pursuant to which Xinhua Airline own an interest of 50% share capital of Xinhua Airline United Transportation Co., Ltd. after increasing its capital sated.

D. On 21 June 1998, the People's Bank of China announced that Hainan Development Bank liquidated. For protecting the rest interest of creditors, assets and liabilities of Hainan Development Bank were entrusted to Industrial and Commercial Bank of China (ICBC). A provision for decrement of the investment was accrued at 100% of total investment.

E. The Company and Hainan Aviation (Group) Co., Ltd entered into an interest transfer agreement dated in 27 November 2003. Pursuant to which the Company agree to transfer 10% equity interest of Yangtze River Express Co., Ltd. to Hainan Aviation (Group) Co., Ltd by the price as amount to RMB 20,000 thousand. This transferring arisen to a related-party transaction, the detail information of this transferring please refer to the related comments

in Notes VIII, Related Party Transactions.

2) Long-term Equity Investment: (Unit: RMB 1,000 Yuan)

Item	2003 December 31	2002 December 31	Shareholding Percentage	Depreciation
Joint venture company investment				
Haikou Meilan Airport Co., Ltd.	505,801	501,023	27.24%	
Hainan Haihang Maitenance Co., Ltd	28,951	28,951	48%	
Hainan Haihang Aviation Imp & Exp Co., Ltd.	5,642	7,436	30%	
Hainan Suncity International Golf Co., Ltd.	34,000	34,000	34%	
Fortune International Tourist Co., Ltd	21,166	21,854	44%	
Beijing Yanjing Hotel Co., Ltd	66,713	69,998	40%	
Beijing New Version Advertisement Co., Ltd	2,949	3,001	30%	
Xinda International Transportation Substitute Company	2,322	2,323	49%	
Beijing Hengshi	5,800	5,800	20%	
Beijing Tianchen Co., Ltd	958	1,038	20%	
Shenzhen Aviation Hotel	1,769	1,145	25%	
Chongqing Changjiang River International Leasing Co., Ltd	40,055	0	40%	
Beijing Kehang Investment Company	22,500	0	75%	
Xinhua Airlines United Transportation Service Company	2,750	0	50%	
Sub-total for joint venture company investment	<u>741,376</u>	<u>676,569</u>		
Associated Company Investment				
HNA Hotel Group Co., Ltd	58,161	58,161	19%	
Hainan New State Hotel Co., Ltd	15,000	15,000	15%	
Hainan Aviation Tourism Development Co., Ltd.	3,274	3,274	3.30%	
Hainan Meilan Airport Stock Co., Ltd.	6,906	6,906	2.20%	
China Civil Aviation Info-network Co., Ltd.	29,860	29,860	3.39%	
Hainan Development Bank	5,000	5,000	0.30%	5,000
Yangtze River Express Co., Ltd	10,000	30,000	15%	
Shenhua Finance Co., Ltd.	5,000	5,000	1.60%	
Other	2,187	2,337		
Subtotal of Associated Company investment	<u>135,388</u>	<u>155,538</u>		<u>5,000</u>

2. No utility or deferred utility of raised capital occurred in the report period.

3. Key Projects and the Revenue under the Investment of Non-collecting Capital

III. Financial Status:

1. Major Financial Index:

Item	2003 (RMB)	2002 (RMB)	+/- (%)	Reason
Total assets	23,106,733,501	19,374,408,100	19	Increase of the currency capital, the account receivable and the added operating airplanes
Shareholders' equity	1,116,359,616	2,400,210,894	-53	The loss due to "SARS" and the change in the accounting policy
Profit from principal business	45,304,020	1,195,855,268	-96	Increase of the cost
Net profit	-1,269,246,224	103,056,129	-1,332	Decrease of the profit from principal business
Net cash increase	1,542,393,832	678,267,545	127	Increase of the bank loan

2. Reasons

1) In the report period, the total assets reached RMB 23.106 billion Yuan, 19% more than that of the previous year,

mainly because of the fixed assets and the operating aircrafts;

2) The shareholder's equity was RMB 1.116 billion Yuan, 53% less than the last year; the decrease was caused by the loss of profit in this year.

3) The profit from the principal business was RMB 45 million Yuan, 96% less than the last year. Decrease was caused by the price increase of aviation fuels and materials and changes in accounting policy during the SARS inflation.

4) The net profit was RMB -1.269 billion Yuan, 1332% less than the last year. The main reason: The gross profit rate decreased 15.35% comparing with the 23.78% in the same period of last year. The major reason is the price increase of aviation fuels and materials and changes in accounting policy during the SARS inflation.

3. The changes in accounting policy, accounting estimates and methods

1) According to the document of Cai Kuai [2003] No 18. issued by the Ministry of Finance, the Company and its affiliated subsidiaries adopted the Accounting Methods of Civil Aviation Company from January 1 of 2003 on, thus following changes were made in the accounting method of aviation materials:

- a. The amortization term of cost on high price spare parts shall be five years instead of six years. The amortization shall be carried out from the second month of buying instead of from the second year of buying. This is a change in the accounting estimates and prospective application shall be adopted. The above changes caused the decrease in net profit of 2003 of RMB 51,179,000 Yuan.
- b. According to the regulation of the Accounting Methods of Civil Aviation Company, the balance of the repair expenses on the high price spare parts, for which the amortization had not been completed before the implementation of the above methods, could be amortized continuously. The newly occurred repair expenses on high price spare parts after the implementation of the above methods shall be accounted into the current loss and profit. This change caused the decrease in net profit of the Company in 2003 of RMB 127,479,000 Yuan.
- c. Before January 1 of 2003, the cost difference of the high price spare parts shall be amortized averagely within 6 years from the second year of buying. From January 1 of 2003 on, it shall be carried forward into cost on principal business calculated according to combined variance rate at the end of each month. This is a change in the accounting policy and retrospective application shall be adopted. The year beginning retained earnings and figures of other related items in 2003, the related items of the 2002 income and income distribution sheet were adjusted accordingly. The cumulative effect of this change is of RMB 26,550,000 yuan. It caused the decrease in the net profit of the Company in 2003 of RMB 73,602,000 Yuan

2) From July 1 of 2003 on, the Company and its affiliated subsidiaries adopted the Enterprise Accounting Standards—Assets & Liabilities after Items (Provision). According to the Enterprise Accounting Standards—Assets & Liabilities after Items, dividend to be distributed shall be accounted into dividends payable as the item of profit distribution during BoD setting the distribution plan. From July 1 of 2003 on, the Enterprise Accounting Standards—Assets & Liabilities after Item was revised as that dividend to be distributed shall be confirmed during the BoD approving the distribution plan. Thus the accounting policy changes shall be adjusted

retrospectively when the Enterprise Accounting Standards—Assets & Liabilities after Items (Provision) was adopted. The year beginning retained income and that of the related items in 2003 were adjusted accordingly. Meanwhile, the profit in 2002 and related items of it were adjusted as well. The cumulative effect of this change is RMB 43,815,000 yuan. It caused the decrease in payable dividend and increase in undistributed profit at the year beginning of the Company in 2003 of RMB 43,815,000 Yuan.

3) According to the document of Cai Kuai [2003] No. 10 issued by the Ministry of Finance, the Notice of Reply (No. 2) to Questions on the Performance of the Accounting Standard for Enterprises and the Related Accounting Standards, the betterment expenses of the fixed assets operating rented-in should be classified and adjusted as the item of fixed assets, thus the balance of the long-term deferred expenses decreased 75,070,000 yuan and the fixed assets increased 75,070,000 Yuan. The period beginning figures of the 2003 annual financial statements were adjusted accordingly.

4) Before January 1 of 2003, the Company adopted the Enterprise Accounting Standards—Leasing and its related guidelines as the accounting basis for the finance leasing. Since the amount of the finance-leased assets was less than 30% of the total assets of the Company, the finance leased assets and long-term payables were priced and accounted according to the contracted lowest leasing payment. With the expending of the finance leasing business of the Company, the finance leasing business occurred from January 1 of 2003 on shall be priced and accounted according to the current value of the contracted lowest leasing payment, the long-term payables at the lowest leasing payment. The difference between them shall be listed separately as unconfirmed financing expenses and shall be amortized at actual interest rate within the leasing period. This is a change in accounting estimates and prospective application shall be applied. It caused the decrease of profit in 2003 of RMB 29,607,000 Yuan.

IV. Influences of the Laws & Regulations, Macro Policy and Production Environment:

1. Influence of the SARS in 2003

Since the Company's customer resources are tourists and Guangzhou, Shenzhen, Beijing and Taiyuan as the Company's major operation cities became greatest epidemic region, the Company suffered great impact of SARS. In comparison with the other three airlines group, the Company not only was allowed no favorable policy of loan with interest discount, but also increased special investment on the prophylaxis and treatment of the SARS and insured the record of no SARS inflation. The impact of the SARS on the Company was much serious than other air traffic companies, which resulted in the certain decrease on the productivity: In the first three months of 2003, the average flights were 288 times per day, which reduced to 247 times per day from April 1 to 20, 164 times per day from April 21 to June 30, the lowest flight times were less than 90 times, lower than 30% of the number normally. The income of April to June slipped down 79.4% comparing with last year, the decreased amount accounted for RMB 945 million yuan. In order to prepare for the recovery of the flight times in the future, the Company increased its investment in the flying training and aircraft maintenance in advance, which increased the fixed cost of the Company accordingly. Meanwhile, the Company reserved huge amount of cash to ensure the balance of its cash flow and caused the 6.9% increase in finance expenses.

The central government paid high attention to the civil aviation industry which seriously suffered from the influence of the SARS and allowed periodically tax preferences and other preferable policies, including exemption from civil aviation infrastructure levies and operation taxes, city construction taxes and education tax added from

May to December, allowing special short term loan with interest discount and lowering the price of aviation fuels in May and June, etc. The CAAC also adjusted certain industry charges. The above active measures taken promoted the recovering and development of the Company's operation.

2. Influence of the Opening of Air Route

The Company made full use of the opening of the fifth air route right to Hainan and opened the international market. It expended transportation capacity and international air route operation right and operation scale. It took the chance to open international air route to the United States, South Africa, etc and establish international air route network. Meanwhile it would take the advantage of Hainan island as an international airport and the passenger resources brought into by foreign airlines company to enhance the cooperation with foreign airlines companies, and would absorb passenger resources by using the current domestic air route network of the Company.

3. Influence of the Policy of Civil Aviation Infrastructure Levies

During the inflation period of SARS, the Finance Ministry and Tax Bureau issued notice to exempt the civil aviation infrastructure levies on the airlines company from May to December of 2003. The Finance Ministry also issued notice that the civil aviation infrastructure levies charged would be released since 2004. Presently, the CAAC is considering of charging resource fee instead of the infrastructure fee, the former would be much lower.

V. Working Plan in 2004:

1. Operation guideline

Year 2004 is the second year of the second-stage of "Three, Seven and Nine" development strategy and the first year of Five-year Plan, we should take " 'Credit, Performance, Innovation', enhancing concept, reforming systems, improving human quality, pursuing great development, realizing new breakthrough" as our working guideline.

2. Operation Objectives

Continue intensify safety management, implement various safety management measures, strengthen safety supervision, win the aviation safety cup, try to come out top in punctuality rate of flight and "Civil Aviation in Passenger's Eye" activity. Maintain the harmonious and quick growth tendency in terms of sales income, passenger traffic and total traffic mileage.

3. Measures of Production Operation

Year 2004 is a key year for Hainan Airlines in the second-stage of "Three, Seven, Nine" development

strategy and development is still the center of each work. In light of the concept of “Credit, Safety, Performance, Innovation”, we should develop our company by and based on reformation, improve the efficiency through management and advocate the reformation taking wholly promotion of new concept as core. In addition, we will try to realize the transformation to centralized management, promote merge operation and in-depth integration and seize the most strategic resources to promote integrated, harmonious and sustainable development of Hainan Airlines.

VI. Routine Work of Board of Directors

1. Meetings of Board of Directors

- 1) On Jan. 24 of 2003, the 22nd Session of the 3rd Meeting of BoD of the Company was held and the Report on Transfer the Airport Administrative Building To Sanya Phoenix Airport was considered and approved.

The related information was published on *China Securities News, Shanghai Securities News and Hong Kong's Wen Wei Po* of Jan. 25 of 2003.

- 2) On April. 10 of 2003, the 23rd Session of the 3rd Meeting of BoD of the Company was held and the reports were considered and approved as followed.

A. Work Summary of 2002 & Work Plan for 2003 of the Company;

B. 2002 Annual Report of the Company and its Summary;

C. Report on Performance of the Board of Directors;

D. Report on Plan of Annual Salary of Directors, Supervisors and Management Personnel;

E. Report on Term-shift Election Of the Board of Directors;

F. Report on Changing the Chief Financial Officer;

G. Report on Amendment of the Articles of Association of HNA;

H. Report on Authorizing the Board to Adjust New Transport Capacity of the Company with Leasing Method;

I. 2002 Financial Report and 2003 Financial Plan of the Company;

J. Report on Renewal of Employment of Accounting Firm;

K. Report on Proposed Profit Distribution Plan for 2002 & Profit Distribution Policy for 2003;

L. Report On Signing Daily Production Connected Transactions Agreement With Related Parties;

M. Report on Terminating the transfer of 10 Dornier-328 Regional Aircrafts and 51% Holding Interests of Hainan Air Catering Co., Ltd.

N. Report on Holding the General Meeting of Shareholders of 2002

The related information was published on *China Securities News, Shanghai Securities News and Hong Kong's Wen Wei Po* of Apr. 12 of 2003.

3) On April 25th of 2003, the 24th Session of the 3rd Meeting of BoD of the Company was held and passed through the *First Quarter Report of 2003*.

The resolution of the meeting was published on *China Securities News, Shanghai Securities News and Hong Kong's Wen Wei Po* of April 26 of 2003.

4) On May. 27th of 2003, the 25th Session of the 3rd Meeting of BoD of the Company was held and the passed through the *Report on Changing the Profit Proposed Distribution Plan for 2002*.

The resolution of the meeting was published on *China Securities News, Shanghai Securities News and Hong Kong's Wen Wei Po* of May 28 of 2003.

5) On June 13th of 2003, the 1st Session of the 4th Board Meeting was held and passed through the *Report on Electing the Chairman and the Vice Chairman and Report on Engaging the Managing Executive Vice President and the Secretary to the Board*.

The resolution of the meeting was published on *China Securities News, Shanghai Securities News and Hong Kong's Wen Wei Po* of June 14th of 2003.

6) On August 29th of 2003, the 2nd Session of the 4th Board Meeting was held and passed through the *Interim Report of HNA of 2003*.

The resolution of the meeting was published on *China Securities News, Shanghai Securities News and Hong Kong's Wen Wei Po* of August 30th of 2003.

7). On Oct 29th of 2003, the 3rd Session of the 4th Board Meeting was held and passed through the *Third Quarter Report of 2003*.

The resolution of the meeting was published on *China Securities News, Shanghai Securities News and Hong Kong's Wen Wei Po* of Oct 30th of 2003.

8). On Nov 28 of 2003, the 4th Session of the 4th Board Meeting was held and passed through the reports as

followed:

A. Report on Termination of the Implementation on HNA Group Transfer the 85% Capital Contribution of Yangtze River Express to Chang'an Airlines

B. Report on 10% Capital Contribution of Yangtze River Express and Partial Assets Transfer of HNA

C. The Report on Capital Increase to Shanxi Airlines Company Ltd.

D. Report on Holding the First Temporary General Meeting of Shareholders of 2003

The resolution of the meeting was published on *China Securities News, Shanghai Securities News and Hong Kong's Wen Wei Po* of Nov 29th of 2003.

2.Subsequent Events on Resolution of the Meetings of Shareholders

1) The General Meeting of Shareholders of 2002 considered and passed through the *Report on Authorizing the Board to Adjust New Transport Capacity of the Company with Leasing Method* and the *Report on Terminating the transfer of 10 Dornier-328 Regional Aircrafts and 51% Holding Interests of Hainan Air Catering Co., Ltd*, the proposal has been carried into execution.

2) The 1st Temporary General Meeting of Shareholders of 2003 considered and passed through the *Report on Termination of the Implementation on HNA Group Transfer the 85% Capital Contribution of Yangtze River Express to Chang'an Airlines* and the *Report on 10% Capital Contribution of Yangtze River Express and Partial Assets Transfer of HNA*, the above transaction has been finished.

3.Profit Distribution Preplan / Preplan for Capitalization of Capital Reserve in 2003

In the fiscal year of 2003, the profit after tax of the Company audited by the domestic accounting firm is for RMB -1,269,250,000 Yuan, while the figure audited by the foreign accounting firm is for RMB -1,115,700,000 yuan. Since the accumulated undistributed profit of the Company audited by the foreign accounting firm of RMB -1,058,450,000 Yuan is lower than RMB -821,400,000 Yuan audited by the domestic accounting firm, the former will be taken as the basic value of 2003 profit distribution in accordance with the "Lower Principle" of profit-sharing followed by the enterprise with both listed A & B shares. According to the regulations of the Company Law and Articles of Association, 10% and 5% of the Company's profit after tax in 2003 shall be withdrawn and accounted into the statutory surplus reserve and statutory public welfare fund respectively before the profit sharing. The withdrawn amount accounts for zero. Therefore, the actual distributable profit is zero.

In the report period, the capital reserve will not be transferred into share capital.

The preplan will be carried out after submitting to the General Meeting of Shareholders of 2003 for approval.

VII. In the report period, HNA did not change the newspaper selected for information release.

VIII. Miscellaneous

1. The Company has timely submitted the self-inspection report of Haikou Security Supervision Department according to the Notice for Regulation regarding normalization the fund correspondence between the list companies and its related parties as well as some issues on listed company's guaranty. During the reporting period, the Company has been involved in no guaranty affairs and its fund correspondence conforms to related regulations or laws.
2. CPA's special explanations for fund impropriation by the holding shareholders or related parties

The audit explanations for fund impropriation by the holding shareholders or related parties

The Board of Directors of Hainan Airlines Co. ,Ltd,

We have accepted the appointment of the Hainan Airlines Company Limited (hereafter "the Company")to audit the Explanation table (hereinafter referred to as the "Explanation") for the fund by your holding shareholders or related parties, according to the Notice of Regulation regarding normalization the fund impropriation by listed company's related parties as well as some issues on listed company's guaranty by CSRC and State-owned Assets Regulation Committee of State Council (No. 2003-56).

It is your responsibility to truthfully compile, disclose the explanation table and guarantee its legitimacy and integrity. Our responsibility is to check issue the audit explanation.

After reviewing, no discrepancy has been discovered. This letter is only for the Company to release the Annual Report to CSRC, and by no means have to serve as any other goals without the written permission by us.

ShineWing Certified Public Accountants

Beijing China

April 16, 2004

3. The special explanation and opinions from the independent directors

According to the Information for the normalization of Listed companies' fund correspondence with related

parties and some issues on List Company's guaranty (No. 2003-56) by CSRC, we regarding the credit guaranty in the report period, our opinion is as followed:

As at 31 December 2003, the Holding Company guaranteed for the bank loans of its subsidiaries as amount of RMB 79,000 thousand, include two for Chang'an Airline as total amount of RMB 49,000 thousand, the maturity is 27 February 2004 and 30 March 2004, one for Shanxi Airlines as amount of RMB 30,000 thousand, the maturity is 26 March 2004.

Except the above stated, the Company did not guarantee for the holding shareholders, the other related parties, the non-legal person companies or any individual.

The significant transactions of related parties

Type	Related party	Relationship	Dec 31,2002	Dec 31, 2003	Increase in 2003	Accumulated in 2003	Balance		Reason	Repayment	
							Operating	Non-operating		Cash	Non-cash
The shareholder	HNA Group Co., Ltd	Shareholder	318	8,861	8,543	184,611		8,861	Temporary loan	176,068	
					-					-	
					-					-	
					-					-	
Other related parties	Deer Jet Co., Ltd	Associated Company	4,474	31,732	27,258	78,091		31,732	Prepayment for aircraft leasing, and tariff	50,833	
	Hainan Haihang Aviation Import & Export Co., Ltd	Associated Company	10,263	7,611	-2,652	57,119	7,611		Prepayment for purchase of aviation materials and tariff	59,771	
	Haikou Meilan Airport Co., Ltd	Associated Company	-	17,320	17,320	17,320		17,320	Down Payment	-	
	HNA Information System Co., Ltd	Associated undertaking	-	542	542	792		542	Down Payment	250	

	Chongqing Changjiang River Leasing Co., Ltd	Associated Company	-	20	20	2,281		20	Temporary loan	2,261	
	Yangtze River Express	Associated undertaking	-	1,461	1,461	23,666		1,461	Temporary loan	22,205	
	HNA Hotel Group Co., Ltd	Associated undertaking	191	1,541	1,350	8,514		1,541	Temporary loan	7,164	
	Hainan Meilan Airport Co., Ltd	Associated undertaking	-	8	8	8		8	Temporary loan	-	
Total			15,246	69,096	53,850	372,402	7,611	61,485	-	318,552	

VIII. Report of the Board of Supervisors

1. Works of the Board of Supervisors:

The board of supervisors convened two meetings in the report period:

1). On April 10 of 2003, the 10th session of the 3rd board of supervisors was held. During the meeting, the Working Report of the Board of Supervisors of 2002, the Report on the Annual Report and the Annual Report Summary of 2002 and the Report on the Term-shift Election of the board of supervisors were considered and passed.

The announcement of the meeting was published on the China Securities News, Shanghai Securities News and Hong Kong's Wen Wei of April 12 of 2003.

2). On June 13 of 2003, the 1st session of the 4th board of supervisors was held. During the meeting, the Report on Electing Mr. Zhang Cong to be the Organizer of the Board of the Supervisors was considered and passed.

The announcement of the meeting was published on the China Securities News, Shanghai Securities News and Hong Kong's Wen Wei of June 14 of 2003.

2. Comments of the Board of Supervisors on the Legality of the Company's Operation:

1. Legality of the Operation:

The decision-making procedure of the Company is in strict compliance with the Company Law, Security Law, Listing Regulations of SSE and other related regulations. The Company had established and perfected the internal control system. No activities violating the laws, rules and Articles of the Association or the interests of the Company of the directors and managers occurred.

2. Status of the Finance:

The accounting firms engaged in the report period issued the auditing reports without reservation. The board of supervisors considered that the auditing reports had expressed the views truly on the actual operation achievements and financial status of the Company in the report period.

3. The latest fund-raising was completed in 1999. The investment orientation adjustments to certain collected capital were carried out according to the legal procedure, the details of which had been published in the related announcement and the annual report of 2000.

4. In 2003, the price of buying and selling assets carried out by the Company was reasonable. Both the assets and shareholders' equity of the Company were not harmed or lost. No insider dealing occurred.

5. The connected transactions reached in the report period conform to the principles of "Equality, Fairness and Publicity". No activities against the interests of the Company occurred.

IX. Important Events

1. In the report period, no significant lawsuit or arbitration occurred.

2. Mergers and Assets Buying & Selling:

In the report period, no significant mergers and assets buying & selling occurred.

3. Important Connected Transactions:

- (1) In 2003, the Company signed the transfer agreement with HNA Group. HNA transferred 10% holding interests of Yangtze River Express to HNA Group, the transferring price was RMB 20 Million Yuan.
- (2) In 2003, the Company signed the assets transfer agreement with HNA Group. The Company transferred some construction in progress including the land of Shanghai Xingguo Lu, Asia Haoyuan and Tianhai Yuan to HNA Group at the price of RMB 114.37 Million Yuan.
- (3) In 2003, the amount of fuel expense and fee of ground handling operations as well as agency fee for imports and exports of the company with Haikou Meiya Industry Co., Ltd., Hainan Meilan Airport Co., Ltd. and Hainan Haihang Aviation Import & Export Co., Ltd. are as follows: Aviation fuel: RMB 187,890,000 Yuan. Ground handling operations: RMB 114,480,000 Yuan. Agency fee: RMB 7,180,000 Yuan.

4. Important Agreements and Performance:

In the report period, no important agreements and performance occurred except the paragraphs of progress of important project invested by using the Non-collected capital and income from it and important connected transactions.

In the report period, no important entrusted financing occurred.

The important guarantee: As at 31 December 2003, the Holding Company guaranteed for the bank loans of its subsidiaries as amount of RMB 79,000 thousand, include two for Chang'an Airline as total amount of RMB 49,000 thousand, the maturity is 27 February 2004 and 30 March 2004, one for Shanxi Airlines as amount of RMB 30,000 thousand, the maturity is 26 March 2004.

5. Promises of the Company or its Shareholders Holding more than 5% of the Company's Total Amount of Shares and Execution of the Promises:

In the report period, no promises of the Company or its shareholders holding more than 5% of the Company's total amount of shares and execution of the promises occurred.

6. Remuneration and Engagement & Dismissal of the Accounting Firms:

In the report period, the Company continued to engage the Shine Wing Certified Accountants and Water House Coopers Public Accounting Firm to audit the financial statements of it. The auditing fee paid to them account for RMB 940 thousand Yuan and HK\$ 1.78 million respectively.

7. According to the regulation of the regular change of the certified accountant, in 2003, the certified accountant signed the financial report of the Company has changed one.

8. Other Important Events:

1) In 2003, HNA won the title of 50 Top Enterprises Listed in Shanghai Stock Exchange and Shenzhen Stock Exchange in the appraisal through comparison sponsored by *Listed Companies* of Shanghai Stock Exchange.

2). In 2003, HNA was awarded with the title of “National Customer Satisfied Service” by China Quality Association and won the first prize of this appraisal again, thus HNA won the triple crown of this prize.

3). In 2003, HNA won the “Golden Eagle Cup” and was awarded with the title of “National Customer Satisfied Service”.

4) Industrial and Commercial Bank of China provided a maximum comprehensive credit limitation in amount of RMB 3,774,480 thousand Yuan, including RMB 3,172,000 thousand Yuan for the Company, RMB 480,000 thousand Yuan for Xinhua Airlines, RMB 49,000 thousand Yuan for Chang’an Airlines, RMB 60,000 thousand Yuan for Shan’xi Airlines and RMB 13,480 thousand Yuan for Hainan Airlines Catering.

X. Financial Report

TO THE SHAREHOLD OF HAINAN AIRLINES COMPANY LIMITED

We have accepted the appointment to audit the accompanying consolidated balance sheet of the Hainan Airlines Company Limited (hereafter “the Company”) as of December 31, 2003, and the related consolidated income and cash flows statement for the year then ended. These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these statements based on our audit.

We conducted our audit in accordance with Standards for Independent Audits of PRC Certified Public Accountants. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as, evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above conform with the Accounting Standards for Business Enterprises and the “ Accounting System for Business Enterprises ” promulgated by the Central Government of the People’s Republic of China and present fairly in all material respects, the financial position of the Company as at 31 December 2003 and the results of its operations and its cash flow for the year then ended.

ShineWing Certified Public Accountants

ATTACHMENTS: Hainan Airlines Company Limited

Balance Sheet

As at 31 December 2003

Monetary unit: RMB Yuan

Assets	Notes	CONSOLIDATED		HOLDING COMPANY	
		2003	2002	2003	2002
CURRENT ASSETS					
Cash in bank & on hand		2,943,433,933	1,401,040,101	2,211,584,122	818,755,914
Short investment		-	-	-	-
Notes receivable		-	-	-	-
Dividend receivable		-	-	2,253,208	2,253,208
Interest receivable		-	-	-	-
Accounts receivable		327,721,607	412,831,320	25,435,882	11,115,313
Other receivables		2,069,058,649	958,393,638	1,408,256,047	764,340,093
Advances to suppliers		1,158,031,509	455,880,910	950,507,191	325,831,957
Subsidy receivable		1,725,000	-	-	-
Inventories		1,096,921,138	1,282,013,990	841,058,569	1,013,958,358
Deferred and prepaid expenses		63,377,093	55,966,438	37,219,098	37,012,874
Long term investment maturing within one year		-	-	-	-
Other current assets		-	-	-	-
Total current assets		7,660,268,929	4,566,126,397	5,476,314,117	2,973,267,717
LONG-TERM INVESTMENTS					
Long term equity investment		1,018,898,398	991,903,099	2,367,479,541	2,790,152,796
Long term bond investment		-	-	-	-
Long-term investments-net value		1,018,898,398	991,903,099	2,367,479,541	2,790,152,796
Incl. consolidation difference		147,133,565	164,796,397	-	-
FIXED ASSETS					
Fixed assets - cost		15,369,594,909	14,591,594,724	11,291,490,207	9,998,877,391
Less: Accumulated depreciation		2,678,416,644	2,381,861,303	1,304,577,646	795,989,853
Fixed assets - net book value		12,691,178,265	12,209,733,421	9,986,912,561	9,202,887,538
Less: Provision for decrement of fixed assets		1,389,000		-	-
Fixed assets - net book value		12,689,789,265	12,209,733,421	9,986,912,561	9,202,887,371
Engineering materials		-	-	-	-
Construction in progress		890,269,989	817,244,036	847,858,203	437,622,371
Disposal of fixed assets					
Total fixed assets		13,580,059,254	13,026,977,457	10,834,770,764	9,640,509,909
INTANGIBLE ASSETS					
Intangible assets		19,392,698	20,004,946	-	-
Long-term deferred expenses		410,905,190	447,057,312	290,681,679	216,508,317
Other long-term assets		417,209,032	322,338,889	334,632,031	322,338,888
Total intangible & other assets		847,506,920	789,401,147	625,313,710	538,847,205
TOTAL ASSETS		23,106,733,501	19,374,408,100	19,303,878,132	15,942,777,627

The accompanying notes form an integral part of these financial statements

Hainan Airlines Company Limited

Balance Sheet (continued)

	CONSOLIDATED		HOLDING COMPANY	
	2003	2002	2003	2002
CURRENT LIABILITIES				
Short term loans	3,927,349,522	2,157,869,647	1,980,349,522	895,869,647
Notes payable	438,446,972	266,541,012	438,446,972	161,477,989
Accounts payable	904,950,001	393,783,867	1,764,959,253	478,051,213
Advances from customers	28,654,981	54,292,647	22,003,009	21,416,990
Accrued payroll	3,121,682	214,725	3,119,078	-1,269
Staff and workers' bonus and welfare fund	12,032,641	12,441,579	-	-
Dividends payable	26,912,033	25,605,802	26,912,032	23,953,682
Taxes payable	212,354,364	137,384,560	206,919,417	127,849,479
Other payables to government	3,723,612	62,118,596	1,285,477	1,287,339
Other payables	408,759,460	432,151,222	122,545,909	485,517,050
Accrued expenses	562,241,696	311,401,202	553,487,274	186,068,754
Sales in advance of carriage-domestic	162,471,011	54,711,071	1,588,033	2,603,558
Sales in advance of carriage-international	4,207,256	4,048,174	-	-
Liability estimation	-	-	-	-
Long-term liability maturing within one year	1,610,877,758	979,880,624	1,081,738,308	821,482,624
Other current liabilities	-	-	-	-
Total current liabilities	8,294,102,989	4,892,444,728	6,203,354,283	3,205,577,056
LONG TERM LIABILITIES				
Long term loans	9,962,760,539	7,559,632,904	9,530,457,463	7,233,796,078
Bonds payable	-	-	-	-
Long term payable	2,724,393,122	3,089,050,910	2,194,744,319	2,625,035,325
Special accounts payable	20,000,000	20,000,000	-	-
Other long-term liability	244,915,495	464,111,317	244,915,495	464,111,317
Total long term liabilities	12,952,069,156	11,132,795,131	11,970,117,277	10,322,942,720
Deferred tax				
Deferred tax credits	-	-	-	-
TOTAL LIABILITIES	21,246,172,145	16,025,239,859	18,173,471,560	13,528,519,776
Minority interest				
Minority interest	744,201,741	948,957,347		
OWNERS' EQUITY				
Paid-in capital	730,252,801	730,252,801	730,252,801	730,252,801
Capital surplus	1,038,405,919	1,038,405,919	1,038,405,919	1,038,405,919

Reserve fund		169,097,575	169,097,575	169,097,575	169,097,575
Inclu.:Public welfare fund		53,094,720	53,094,720	53,094,720	53,094,720
Undistributed profits / (accumulated losses)		-821,396,680	462,454,599	-807,349,723	476,501,556
Total owners' equity		1,116,359,615	2,400,210,894	1,130,406,572	2,414,257,851
TOTAL LIABILITIES AND OWNERS' EQUITY		23,106,733,501	19,374,408,100	19,303,878,132	15,942,777,627

Hainan Airlines Company Limited

Profit and Loss Account

For the Year 2003

Monetary unit: RMB Yuan

ITEMS	Notes	CONSOLIDATED		HOLDING COMPANY	
		2003	2002	2003	2002
1. Sales revenue		5,372,091,313	5,028,281,733	2,919,452,797	3,185,324,902
Less: Civil aviation infrastructure levies		37,836,221	91,190,797		-
Cost of sales		5,225,243,022	3,576,012,777	2,675,106,905	2,194,877,802
Sales tax and surtax		63,708,049	165,222,891	37,021,632	107,739,462
2. GROSS PROFIT ON SALES		45,304,021	1,195,855,268	207,324,259	882,707,638
Add: Income from other Operations		31,801,811	41,911,833	17,527,565	32,292,397
Less: Selling expenses		379,753,722	286,065,650	209,993,936	178,126,103
General and administrative expenses		416,742,465	272,722,762	255,566,435	170,231,711
Financial expenses/(income)		739,482,089	555,630,166	592,475,505	460,513,631
3. OPERATING PROFIT / (LOSS)		-1,458,872,444	123,348,523	-833,184,050	106,128,589
Add: Income from investments		-12,631,165	12,191,970	-415,570,684	8,466,768
Subsidies Income		8,466,428	6,970,692	-	-
Non-operating income		11,995,468	1,236,193	1,078,122	877,937
Less: Non-operating expenses		23,573,300	2,738,966	21,050,242	1,705,500
4. TOTAL PROFIT / (LOSS)		-1,474,615,013	141,008,411	-1,268,726,855	113,767,794
Less: Income tax		4,373,618	11,848,709	519,369	10,711,666
Minority interest		-209,742,408	26,103,574	-	-
5. NET PROFIT/(LOSS) AFTER TAX		-1,269,246,223	103,056,129	-1,269,246,224	103,056,128
Add: Undistributed profit at beginning of the year		462,454,599	418,672,056	476,501,555	432,719,013
Transferred in from surplus reserve					
6. Profit Available for Dividends		-806,791,624	521,728,185	-792,744,668	535,775,141
Less: Statutory surplus reserve		-	10,305,612	-	10,305,612
Statutory public welfare fund		-	5,152,806	-	5,152,806
7. Profit Available for Dividends to Shareholders		-806,791,624	506,269,767	-792,744,668	520,316,723
Less: Preference dividends payable				-	-
Voluntary earnings surplus drawn				-	-
Common stock dividends payable		14,605,056	43,815,168	14,605,056	43,815,168
Dividends being transferred to share capital				-	-
8. Undistributed Profit		-821,396,680	462,454,599	-807,349,724	476,501,555

Supplementary Materials

	Consolidated Company		Parent Company	
	2002	2003	2002	2003
Income from sale and disposal of departments or invested units				
Losses caused by natural disasters				
Increase/decrease in total profit causing by changes in the accounting policy	-230,688,750	-78,904,794	-193,200,399	-78,904,794
Increase/decrease in total profit causing by changes in the accounting estimates	-51,179,253	56,654,000	-26,322,978	47,701,000
Losses caused by debt reorganization				
Others				

Hainan Airlines Company Limited

Cash Flow Statement

For the Year 2003

	Notes	CONSOLIDATED	HOLDING COMPANY
1. Cash Flows From Operating Activities			
Cash received from sales of goods or rendering of services		4,886,013,385	3,884,846,886
Refund of tax		5,277,299	-
Other cash received relating to operating activities		263,304,598	385,122
Sub-total of cash inflows		5,154,595,282	3,885,232,008
Cash paid for goods and services		2,667,165,346	1,539,884,395
Cash paid to and on behalf of employees		335,774,073	109,138,478
Income tax paid		130,059,014	56,127,799
Other cash paid relating to operating activities		2,666,574,099	1,681,500,492
Sub-total of cash outflows		5,799,572,532	3,386,651,164
Net cash from operating activities		-644,977,250	498,580,844
2. Cash Flows from Investing Activities:			
Cash received from return of investments		20,050,000	20,000,000
Cash received from distribution of dividends or profits		7,150,170	6,982,523
Net cash received from disposal of fixed assets, intangible assets and other long-term assets		1,271,440,393	127,543,658
Other cash received relating to investing activities		1,300	
Sub-total of cash inflows		1,298,641,863	154,526,181-
Cash paid to acquire fixed assets, intangible assets and other long-term assets		1,939,439,965	1,893,712,537
Cash paid to acquire equity investments		22,572,500	-
Other cash paid relating to investing activities		6,517,576	-
Sub-total of cash outflows		1,968,530,041	1,893,712,537
Net cash from investing activities		-669,888,178	-1,739,186,356
3. Cash Flows from Financing Activities			
Proceeds from issuing shares		5,000,000	-
Proceeds from investment		9,887,168,097	7,260,839,297
Other proceeds relating to financing activities		183,472,606	721,047,183
Sub-total of cash inflows		10,075,640,703	7,981,886,480
Cash repayments of amounts borrowed		5,237,586,690	3,671,375,477
Cash payments for distribution of dividends or profits and interest expenses		705,500,519	571,752,925
Other cash payments relating to financing activities		1,275,294,234	1,105,324,358
Sub-total of cash outflows		7,218,381,443	5,348,452,760
Net cash from financing activities		2,857,259,832	2,633,433,720
4. Effect of Foreign Exchange Rate Changes on Cash			
5. Net Increase in Cash and Cash Equivalents	42	1,542,393,832	1,392,828,208

Hainan Airlines Company Limited

Cash Flow Statement

For the Year 2003

A.

Monetary unit: RMB Yuan

	Notes	CONSOLIDATED	HOLDING COMPANY
1. Reconciliation of Net Profit to Cash Flows from the rating Activities			
Net profit		-1,269,246,224	-1,269,246,224
Add: Minority interest		-209,742,408	-
Add: Provision for bad debt or bad debt written off		2,021,482	-
Depreciation of fixed assets		719,540,643	493,798,096
Amortization of intangible assets and other long-term assets		28,431,547	27,829,520
Amortization of long-term deferred assets		128,282,561	78,674,318
Decrease in deferred and prepaid expenses (or deduct: increase)		-35,891,912	-30,949,962
Increase in accrued expenses (or deduct: decrease)		259,214,150	396,853,890
Losses on disposal of fixed assets, intangible assets and other long-term assets (or deduct: gains)		14,786,633	19,566,742
Losses on scrapping of fixed assets		272,139	-
Financial expenses		740,146,179	592,475,505
Losses arising from investments (or deduct: gains)		12,631,165	415,570,684
Deferred tax credit (or deduct: debit)			
Decrease in inventories (or deduct: increase)		226,904,067	172,810,809
Decrease in operating receivables (or deduct: decrease)		-368,895,888	-1,613,300,122
Increase in operating payables (or deduct: decrease)		-917,489,954	1,214,497,588
Others		24,058,569	-
Net cash from operating activities		-644,977,250	498,580,844
2. Investing and Financing Activities that do not Involve in Cash Receipts and Payments			
Transferred-in capital by debt			
Negotiable bond due in one year			
Capital leasing of fixed assets		1,060,358,152	760,358,152
3. Net Increase in Cash and Cash Equivalents			
Cash at the end of the period		2,943,433,933	2,211,584,122
Less: cash at the beginning of the period		1,401,040,101	818,755,914
Plus: cash equivalents at the end of the period		-	-
Less: cash equivalents at the beginning of the period		-	-

Net increase in cash and cash equivalents		1,542,393,832	1,392,828,208
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Hainan Airlines Company Limited
Statement of Provision
For the Year 2003

Monetary unit: RMB Yuan

Consolidated

Items	2002.12.31	Addition	Write-off	2003.12.31
1. Provision for bad debts	76,715,825	35,026,625	14,024,927	97,717,523
Including: Account Receivable	31,590,017		14,024,927	17,565,090
Other Receivable	45,125,808	35,026,625		80,152,433
2. Provision for loss on short-term investments				
Including: Investment in stock				
Investment in bonds				
3. Provision for loss on realization of inventories	18,279,237			18,279,237
Including: high value spare parts	16,377,727			16,377,727
Consumption aviation materials	1,818,174			1,818,174
Aircraft supplies	83,336			83,336
4. Provision for loss on long-term investment	5,000,000			5,000,000
Including: Investment in equity	5,000,000			5,000,000
Investment in bonds				
5. Provision for loss of fixed assets	1,389,000			1,389,000
Including: Plant & building	1,389,000			1,389,000
Equipment				
6. Provision for loss of intangible assets				
Including: Patents				
Proprietary technology				
Provision for loss of construction in progress	12,000,000	500,000		500,000
8. Provision for loans of authority				

Holding Company

Items	2002.12.31	Addition	Write-off	2003.12.31
1. Provision for bad debts	9,774,187	32,205,000	4,381,000	37,598,187
Including: Account Receivable	4,381,582		4,381,000	582
Other Receivable	5,392,605	32,205,000		37,597,605
2. Provision for loss on short-term investments				
Including: Investment in stock				
Investment in bonds				
3. Provision for loss on realization of inventories	18,279,237			18,279,237
Including: high value spare parts	16,377,727			16,377,727

Consumption aviation materials	1,818,174			1,818,174
Aircraft supplies	83,336			83,336
4. Provision for loss on long-term investment	5,000,000			5,000,000
Including: Investment in equity	5,000,000			5,000,000
Investment in bonds				
5. Provision for loss of fixed assets				
Including: Plant & building				
Equipment				
6. Provision for loss of intangible assets				
Including: Patents				
Proprietary technology				
Provision for loss of construction in progress	12,000,000			12,000,000
8. Provision for loans of authority				-

HAINAN AIRLINES COMPANY LIMITED

(English translation for reference only)

NOTES TO FINANCIAL STATEMENTS - 1 January to 31 December 2003

(The currency is in RMB thousand Yuan except otherwise indicated)

I. General

- Hainan Airlines Company Limited (hereinafter referred as “the Company”) is a joint stock limited company reorganized from the former state owned Hainan Airlines (hereinafter referred as “the State Owned Company”) pursuant to the Qiong Gu Ban Zi [1992] No. 18 issued by the Hainan Provincial Office for Joint Stock Limited Companies in September 1992. The net assets of the State owned company was revalued by Hainan Consultative & Investing Company and approved by the Finance Bureau of Hainan Province (the reference of the approval is Qiong Cai Shui [1992] GuoZi No.639) as RMB 13,340,552 yuan was determined as the State capital of the Company. The Company was established by way of promotion and the promoters were 24 legal enterprises including the State owned company, China Everbright International Trust and Investment Co., Bank of Communication Hainan Branch, Hainan Aviation Import & Export Co., etc. The Company was registered on 8 January 1993 at Hainan Industrial & Commercial Administration Bureau. The registered share capital was RMB 250,100,000 yuan, and the total amount of shares was 250,100,000.
- The scrip dividend for 1993 was approved by the resolution of the 2nd shareholders meeting of the Company in March 1994. 50,020,000 shares were distributed and the total capital had increased to RMB 300,120,000 yuan.
- In May 1993, with the approval of the Gu Ban Zi [1993] No. 17 issued by Hainan Provincial Office for Joint Stock Limited Companies, 96,059,448 shares were listed in

STAQ system. The number of legal person shares listed in STAQ system is 115,271,337 after the scrip dividend.

4. On 2 November 1995, pursuant to the approval of the Wai Jing Mao Yi Han Zi [1995] No. 615 issued by the Ministry of Foreign Trade and Economic Co-operation of PRC, the Company issued 100,040,001 shares to American Aviation LDC at a price of USD 0.25 per share. The par value of the Company's shares is RMB 1 yuan per share. The Company changed into a Sino-foreign joint stock limited company after the issuance of shares. The Company raised a fund of USD 25,000,000 (equivalent to RMB 207,905,000 yuan). After deducting the related issuing expenses, RMB 100,040,001 yuan of the amount was stated as share capital and the remaining amount of RMB 70,177,849.79 yuan was stated as capital surplus. The Company obtained a new business license in November 1996 after increasing its share capital stated above. Also its name has been changed to Hainan Airlines Company Limited and the registered capital was RMB 400,160,001 yuan.
5. Following the approval of Zheng Wei Fa [1997] No. 24 issued by the Securities Commission of the State Council, the Company had issued 71,000 thousand B Shares at an issue price of USD 0.47 per share and the fund raised was USD 33,370,000 (equivalent to RMB 276,690,000 yuan). After deducting the related issuing expenses, RMB 71,000,000 yuan was stated as share capital and the remaining amount of RMB 186,822,000 yuan was stated as capital surplus.
6. According to the approval of Zheng Jian Fa Xing Zi [1999] No.129 issued by CSRC, the Company issued 205 million Ordinary Shares (A Shares) at an issue price of RMB 4.6 yuan per share and the fund raised was RMB 943,000,000 yuan. After deducting the related issuing expenses, RMB 205,000,000 yuan was stated as share capital and the remaining amount of RMB 708,745,226 yuan was stated as capital surplus.
7. In accordance with a profit appropriation resolution for report of the year 1999 passed by the shareholders' meeting in 18 May 2000, the Company distributed stock dividend at 0.8 shares per ten shares (on the basis of total number of shares 676,160,000) and cash dividend RMB 1 yuan (tax included) to all shareholders with total amount of RMB 54,092,800 yuan and RMB 67,616,000 yuan respectively. The share capital of the Company is increased to RMB 730,252,801 yuan thereafter.
8. The Company is attribute to airport industry. It mainly deals with approved international and domestic air passenger and cargo transportation and other related transportation service.

II. Basis of Preparation

Due to being affected by SARS in the year 2003, the Company has arisen the loss of operating for the first time since the Company had gone into the public. The net profit of the Company is RMB -1,269,246 thousand, the net cash from operating activities is RMB - 644,977 thousand,

the working capital as at 31 December 2003 is RMB –644,834 thousand. The assurance of continuation of the business of the Company depends on the future operating capital and continuing financial support from the financial institution. Therefore, the Company takes actions actively to cooperate with the financial institution and get a comprehensive credit limitation in amount of RMB 3,774,480 thousand for the year 2004 as we mentioned in notes XII.3, etc. The BOD believes that the domestic aviation industry would keep increasing with high speed and the operating of the Company would be advanced so as to enable the Company to meet its liabilities in the future. The directors believe that the Company will continue as a going concern and consequently have prepared the financial statements for the year 2003 on the going concern basis.

III. Principal Accounting Policies

1. Accounting Policy

The financial statements have been prepared in accordance with the Accounting Standards for Business Enterprises and the Accounting Regulations of the People's Republic of China for Business Enterprises and in accordance with the Accounting Method of Aviation Transportation Enterprises promulgated by the Ministry of Finance from 1 January 2003.

2. Accounting Period

The Company's accounting year starts on 1 January and ends on 31 December.

3. Reporting Currency of the Company

The Company uses the Renminbi (RMB) as its reporting currency.

4. Basis of preparation and cost principle

The financial statements are prepared on accrual -basis accounting principles. Assets and liabilities are initially recorded at their approved value upon contributed to the Company, otherwise are initially recorded at their acquired costs.

5. Foreign Currency Transactions

Transactions denominated in foreign currencies are translated into RMB at the exchange rates stipulated by the People's Bank of China prevailing at the transaction dates. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated into RMB at the exchange rates stipulated by the People's Bank of China at the balance sheet date. Exchange differences arising from borrowings for acquisition of fixed assets could be capitalized when the constructions in progress have reached their expected usable conditions. Exchange differences occurred during the prepare period are recorded as long-term deferred assets and should be expensed when the Company star to operating. Exchange differences arising from other translations are taken into the profit and loss account.

6. Cash equivalents

Cash equivalents are short-term, highly liquid investments (normally less than three months from date of purchase to due date) that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

7. Bad Debt Provision

The Company records bad debts upon the death or insolvency of debtors, or proved by sufficient evidences that the outstanding in the receivables are irrecoverable, bad debts are recognized and charged to income statement as an expense in the year in which they arise.

The Company accounts for bad debts using provision methods. Aging analysis method of the provision for bad debts is adopted. The following ratios of bad debts provision are used, after taking considerations of debtor's financial positions and cash flow performances, except for the receivable amounts for the related parties or the amounts that are approved receivable by sufficient evidences.

Within one year	0%
1-2 years	5%
2-3 years	10%
3-4 years	30%
4-5 years	50%
5-6 years	80%
More than 6 years	100%

In addition, specific provisions are set against balances that have been assessed to be uncollectible in the case of unfavorable operating position, insolvency or suspended business.

8. Inventory

Inventories mainly include high value spare parts, aviation consumption materials, Catering supplies and low cost consumables. High value spare parts and aviation consumption materials are recorded at standard cost, and the difference between the weighted average cost and standard cost is recorded in the cost variances of materials account. In addition, the standard cost of high value spare parts are amortized from the next month after purchase on a straight-line basis for a period of five years and the cost variances of the amortization are allocated at the end of each month. Consumption aviation materials are expensed when used and the cost variances of materials are allocated at the end of each month. Catering supplies are recorded at cost and recognized as expenses in the period used at the end of the year. High value spare parts repair cost should be expensed when occurred.

The provision of high value spare parts, consumption aviation materials and catering supplies is provided for on the basis of the lower of the cost and the market price.

Low cost consumables are expensed when consumed.

9. Long-term Investments

(1) Long-term equity investments

- A. Long-term equity investment price and revenue recognized method: Long-term equity investments are recorded at the initial cost of acquisition. When the Company owns an interest of 20% or less of the voting rights or otherwise does not have the ability to exercise significant influence over the financial and operational decisions, then these investments are accounted for using the cost method of accounting. When the Company owns an interest of 20% or more of the voting rights or otherwise has the ability to exercise significant influence over the financial and operational decisions, then these investments are accounted for using the equity method of accounting.
- B. Equity investment difference amortized method and years: When the equity investments are accounted for using the equity method of accounting, the difference between the initial costs on acquisition and the proportionate share of the net assets of the investee is accounted for as an “equity investment difference” and are amortized on a straight-line basis over a certain period of years. If the investment period is stipulated in the contract, then the amortization should be taken over this period. If there is no time limit, then debit balances should be amortized less than 10 years and credit balances should be amortized at least 10 years. However, credit balances occurred behind 17 March 2003 should be accounted for as a “capital surplus- provision for equity investment”.

- (2) Provision for impairment of long-term investments recognized method: At the end of period, provisions are set against balances in the case of continuous dip in market price or unfavorable operating position and the dip in price is expected irrecoverable in the future. Provision for impairment of long-term investments is made individually based on the excess of the original cost of the share investment over its market price.

10. Fixed Assets

Fixed assets refer to the tangible assets that holding for production, services supply, lease or management, which include aircraft and engines, improvement of fixed assets by operating lease, plant and building, equipment, vehicles and other equipment related to the operation of the Company with useful lives of over one year. Fixed assets also include equipment other than the main production equipment with individual values of over RMB 2,000 yuan and useful lives in excess of two years.

Fixed assets purchased or constructed by the Company are initially recorded at historical cost. Assets held under finance leases are recorded at the net present value of the lowest contract price.

Depreciation of fixed assets is calculated on the straight-line basis over the following useful lives, after taking into account their residual value, which is 5% of cost:

Plant and buildings	40 years
Aircraft and engines	10 to 20 years
Improvement of fixed assets by operating lease	7 years
Vehicles	10 years
Machinery and equipment	8 to 14 years

After fixed assets decreased in value because of over-function, impairment or loss, decrease of revaluation price and low coverage of the cost of the fixed assets, a provision was made based on the excess of the original cost of the fixed assets over its net realizable value. The following fixed assets are made provision in full amount:

- (1) Permanently withdraw from use and no future economic benefit is expected and being recognized no income during transactions.
- (2) No future economic benefit is expected for technical reasons.
- (3) Damaged fixed assets without any value and use.

11. Construction in progress

Construction in progress represents capital assets under construction or being installed and prepayment for purchase of airplane and aviation materials, which is stated at cost. Cost comprises original cost of aircraft, equipment, installation, construction and other direct costs which includes interest accrued on loans financing the capital assets and related foreign currency exchange gains or losses, prior to the date of reaching their expected usable condition.

Construction in progress is transferred to the fixed assets account when they have been substantially completed or reached their expected usable condition, and made accumulated depreciation from the next month.

At the end of each year, the Company reevaluates the construction in progress. Provision is made for the loss of construction in progress under the following situation:

- (1) Stopped project that is not expected to reopen in two years.
- (2) Obsolescent project in performance and technology and is unable to bring future economic benefit.

(3) Decrease in value has incurred with satisfied proof.

12. Borrowing costs

Borrowing costs include interest incurred, amortization of discounts or premiums and exchange differences in connection with the foreign currency borrowing. Specific borrowings represent the borrowings for acquisition of fixed assets.

Borrowing costs on specific borrowings are capitalized if they meet the following three criteria:

- (1) Ancillary costs incurred.
- (2) Interest incurred.
- (3) The constructions in progress have reached their expected usable conditions.

The capitalization of borrowing costs is ceased when the constructions in progress have reached their expected usable conditions. Borrowing costs incurred thereafter are recognized as financial expense in the periods in which they are incurred.

13. Intangible assets

- (1) Purchased land use rights are accounted for at actual cost (including relevant taxes).
Invested land use rights are accounted for at evaluation cost.
- (2) Land use rights are amortized over their transfer years on a straight-line basis.
- (3) Intangible assets are accounted on the basis of the lower of the cost and the recoverable value. At the end of period, a provision for the intangible assets is made based on the excess of the book value of the investment over its recoverable value.

14. Long-term deferred assets

Long-term deferred expenses include leasehold improvements in connection with the finance and operating leases and initial recruitment pilot training costs that should be amortized for more than one year. These expenses are amortized over a period from three to seven years on a straight-line basis.

15. Other Long-term Assets

Other long-term assets refer to deferred losses and gains of sales and leaseback, which represents the deferred losses or deferred gains arisen from the aircraft and engine sales and leaseback transactions. Deferred losses or deferred gains arisen from the operating leaseback

transactions are amortized using the straight-line method over the lease period. Deferred losses or deferred gains arisen from the finance leaseback transactions are amortized using the straight-line method over the estimated useful lives.

16. Leases

When significant risks and rewards of ownership of the assets are transferred to the lessees pursuant to the contract, these leases are classified as finance leases. Assets held under finance leases are recorded at the net present value of the lowest contract price while the long-term liability are recorded at the lowest contract price, and the difference between the above two value are recognized as an “unrecognized financial expenses” should be allocated by actual discount rate. Other leases are classified as operating lease. The costs are amortized using the straight-line method over the lease period.

17. Sales

Passenger, charter flight and cargo transportation services revenues are recognized when the relevant sales and costs could be measured reliably, relevant economic benefits could flow into the Company, and the completion stage of transportation services provided could be measured reliably.

Interest revenues and using chare fee gain from releasing the assets using right are recognized when the relevant sales and costs could be measured reliably, relevant economic benefits could flow into the Company.

18. Income tax

The Company accounts for corporate income tax using the Tax Payable method.

19. Profit distribution

According to the relevant regulations for Joint Stock Limited Company and the Company's articles of association, the after-tax profit is appropriated in the following order:

- (a) To cover accumulated losses;
- (b) Appropriation of 10% statutory surplus reserve; (The Statutory Surplus Reserve Fund can cease to accrue until the fund balance reaches 50% of the registered share capital.)
- (c) Appropriation of 5-10% statutory welfare reserve;
- (d) Appropriation of discretionary surplus reserve;

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- (e) Payment of dividends. According to relevant CSRC regulations, profit distribute to shareholders is the lower of the retained profits after appropriation of reserves as mentioned above, as shown in the PRC statutory accounts and the accounts prepared under International Accounting Standards.

20. Basis of Consolidation

According to Cai Kuai Zi (1995) No. 11 approved by Ministry of Finance (“MOF”), the Interim Provisions for consolidated financial statements, and Cai Kuai Er Zi (96) No. 2, the Answer of the Interim Provisions for consolidated financial statements, the Company prepared the consolidated financial statements of 2003. The consolidated financial statements comprise the consolidation of financial statements of the Company and its subsidiaries, which are those companies in which the Group, directly or indirectly, has an interest of more than 51% the capital or total share capital as on 31 December 2003 and of the results for the year ended. All inter-company transactions, balances and unrealized surpluses and deficits on transactions between Group companies have been eliminated.

21. The change explanation in principle accounting policy and accounting estimate

(1) According to Cai Kuai [2003] No.18 approved by Ministry of Finance (“MOF”), the Company and its subsidiaries implement the Accounting Method of Aviation Transportation Enterprises from 1 January 2003, changed the accounting method of aviation materials as follow:

- (a) The Company shortened the amortization period of standard cost of high value spare parts from six years to five years. And amortized the standard cost of high value spare parts from the next month after purchase instead of amortized from the next year. This change is attribute to change in accounting estimate and is applicable to future applicable method. This change decreased the net profit as amount to RMB 51,179 thousand in 2003.
- (b) According to the Accounting Method of Aviation Transportation Enterprises, the balance of high value spare parts repair cost before 1 January 2003 keep on amortizing, current high value spare parts repair cost should be expensed when occurred. This change decreased the net profit as amount to RMB 127,479 thousand in 2003.
- (c) The Company changed amortizing the cost variances of high value spare parts from the next year after arisen on a straight-line basis for a period of six years to allocated at the end of each month. This change is attribute to change in accounting policy and is applicable to retrospective adjustment method that refer to the adjustment of the beginning balance of retained earning and beginning balance of other related accounts in 2003, also refer to the adjustment of the related accounts of income statement for the year 2002. The accumulated impact is RMB 26,550 thousand, and this change decreased the net profit as amount to RMB 73,602 thousand in 2003.

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- (2) The Company and its subsidiaries are applicable to the Accounting Standards for Business Enterprise – Subsequent events, that be revised, from 1 July 2003. According to the standards before revised, the Dividend Distribution recorded as Dividend Payables during the period that BOD make the profit appropriation. After 1 July 2003, the Dividend Distribution recognized during the period that shareholder’s meeting approved the profit appropriation. This change is attribute to change in accounting policy and is applicable to retrospective adjustment method that refer to the adjustment of the beginning balance of retained earning and beginning balance of other related accounts in 2003, also refer to the adjustment of the related accounts of income statement for the year 2002. The accumulated impact is RMB 43,815 thousand, and this change decreased the beginning balance of Dividend Distribution as well as increased the beginning balance of undistributed profit as amount to RMB 43,815 thousand in 2003.
- (3) According to Cai Kuai [2003] No.10 approved by Ministry of Finance (“MOF”), the answer for the question in relation to implement the Enterprises Accounting System and related accounting standards, the Company reclassify the leasehold improvements in connection with the finance and operating leases from long-term deferred assets to fixed assets, leads to the decrease of the balance of long-term deferred assets in amount of RMB 75,070 thousand, as a result, the net value of fixed assets increase as amount to RMB 75,070 thousand. The Company has adjusted the beginning balance of financial statement for the year 2003.
- (4) The Company accounts the finance leasing in accordance with the Accounting Standards for Business Enterprise – Leasing and other related regulations before 1 January 2003, according to the standards that lessees usually should record the leased asset and the long-term liability at an amount equal to the total minimum lease payments at the inception of a lease due to the finance leased asset has not exceed the 30% of total assets. As a result of the extending of the finance lease transactions, from 1 January 2003, the Company changed to record the finance leased assets at the net present value of the lowest contract price while the long-term liability are recorded at the lowest contract price, and the difference between the above two value are recognized as an “unrecognized financial expenses” should be allocated by actual discount rate. This change decreased the net profit as amount to RMB 29,607 thousand in 2003.

IV. Taxation

1. Income tax
 - (1) Parent Company income tax

According to Qiong Di Shui Fa [1998] No.27 approved by Hainan Government, income tax rate of the Company is 15% for year 2003.

(2) Subsidiaries income tax

- (a). The applicable tax rate for Hainan Golden-Deer Aviation Sales Co., Ltd. (“Golden Deer”) is 15% for year 2003.
- (b). The applicable tax rate for Hainan Airlines VIP Flight Services Co., Ltd. (“VIP Flight Services”) is 15% for year 2003.
- (c). The applicable tax rate for Hainan Airlines Catering Co., Ltd. (“Catering company”) is 15% for year 2003.
- (d). The applicable tax rate for China Xinhua Airlines Co., Ltd. (“Xinhua Airlines”) is 33% for year 2003.
- (e). The applicable tax rate for Chang'an Airlines Co. Ltd, (“Chang'an Airlines”) is 33% for year 2003.
- (f). The applicable tax rate for Shanxi Airlines Co. Ltd (“Shanxi Airlines”) is 33% for year 2003.

2. Turnover Tax and surcharges

Tax	Basis of computation	Tax rate
Value added tax	Catering revenues	6%
Sales tax	* Traffic revenues and handling charges	3%
City construction tax	* Turnover tax payable	7%
Education surcharge	* Turnover tax payable	3%

* According to Cai Shui [2003] No.113 noticed emergency by Ministry of Finance and State Tax Bureau in relation to adjusting the revenue policy of several industries during the SARS, from 1 May 2003 to 30 September 2003, the passenger transport transactions and travel transaction of Civil Aviation are entitled to exemption from PRC sales tax, city construction tax and education surcharge. Also according to Cai Shui [2003] No.227 approved by Ministry of Finance and State Tax Bureau in relation to extending Preferential Policy of several industries suffered for SARS, from 1 October 2003 to 31 December 2003, the passenger transport transactions and travel transaction of Civil Aviation are continually entitled to exemption from PRC sales tax, city construction tax and education surcharge. So the Company has Preferential Policy of sales tax, city construction tax and education surcharge from 1 May 2003 to 31 December 2003.

3. Individual income tax

The Company withholds individual income tax from employees to the tax authorities.

V. Group accounting

The financial statements of the Company represent the consolidated financial statements of the Company itself and its consolidated subsidiaries for the year ended 31 December 2003. All significant transactions among its consolidated entities are eliminated upon consolidation.

The followings are the information of the major subsidiaries as of 31 December 2003:

Company Name	Registered Capital	Amount Investment	Owned interest	Principal activities
A Hainan Golden-Deer Aviation Sales Co., Ltd.	RMB 8,000,000	RMB 7,600,000	95%	Transportation and chartered flight agency services
B Hainan Airlines VIP Flight Service Co., Ltd.	USD 1,020,408	USD 502,408	51%	Chartered flights agency services
C Hainan Airlines Catering Co., Ltd.	RMB 31,000,000	RMB15,810,000	51%	Production of food and present for passengers
D China Xinhua Airlines Co., Ltd.	RMB 1,830,000,000	RMB 933,300,000	60%	Approved air passenger and cargo transportation
E Chang'an Airlines Co.,Ltd.	RMB 754,390,000	RMB 554,563,300	73.51%	Air passenger and cargo transportation in Shanxi province and its surrounding provinces
F Shanxi Airlines Co., Ltd.	RMB 320,000,000	RMB 285,000,000	92.51%	Air passenger and cargo branch line transportation in Shanxi province and its surrounding provinces
G Beijing Xinhua Air Catering Co., Ltd.	RMB 29,990,000	RMB 15,294,900	51%	Production and sale of pastry, food and beverage
H Shanxi Chang'an Hainan Aviation Star Hotel Co., Ltd.	RMB 25,000,000	RMB 20,000,000	80%	Hotel and catering, commodity, costume sales, typing and other office services.

A. Hainan Golden-Deer Aviation Sales Co., Ltd. ("Golden Deer") is a limited company in which the Company and Hainan Aviation Import & Export Trading Company ("HAIETC") hold 95% and 5% equity interests respectively. According to the authorization letter signed with Hainan Aviation Import & Export Company on 10 May 1995, all the risks and benefits in relation to HAIETC's 5% interest have been assigned to the Company.

B. Hainan Airlines VIP Flight Service Co., Ltd. ("VIP Flight Service") is a Sino-foreign joint venture established by the Company and Swiss Mid-Europe Airline Development Co., Ltd. withhold 51% and 49% equity interest respectively. Both sides have already fully

contributed their portions of the registered capital.

- C. Hainan Airlines Catering Co., Ltd. (“Catering Company”) is a Sino-foreign joint venture established by the Company and Hong Kong Hainan Airlines Catering Co., Ltd. on 28 March 1994. The registered capital of Catering Company was RMB 31,000,000 yuan in 1999, and the holding equity interest is changed to 51% and 49% respectively. Both sides have already fully contributed the required registered capital as of 10 February 1999, which was verified by Hainan Zhenhua Certified Public Accountants.
- D. China Xinhua Airlines Co., Ltd. (“Xinhua Airlines”) is a limited Company that was recombined by the Company, Shenhua Group Co., Ltd. and Hainan Airlines Group. The registered capital of China Xinhua Airlines is RMB 1.83 billion. The Company contributed RMB 933.3 million to hold 51% of total equity interest. According to validation by Hainan Weixin CPA Firm, all sides have already fully contributed their portions of the registered capital up to 31 August 2002. Accordingly, China Xinhua Airlines is consolidated from 1 September 2001. The Company and Hainan Airlines Group Co. Ltd entered into a capital transfer agreement in December 2002. Pursuant to which the Company accepted the Hainan Airlines Group Co. Ltd’s transfer of the interest of 9% share capital to the Xinhua Airlines. As at 31 December 2002, the Company holds 60% of total equity interest, Shenhua Group Co., Ltd. holds 40% of total equity interest.
- E. Chang'an Airlines Co. Ltd. (“Chang’an Airlines”) was contributed and established by the Company, Chang'an Aviation Industrial Company and Hainan Airline Group Co. Ltd. The registered capital of Chang'an Airlines is RMB 754,390,000 yuan, in which the Company contributes RMB 200,000 thousand to hold 26.51% of registered capital. All sides have already fully contributed their portions of the registered capital on 30 October 2001, which was validated by Shan'xi Xinghua CPA Firm,. The Company signed equity transfer agreement with Hainan Airlines Group Co., Ltd., according to which acquiring equity investment RMB 354,563 thousand from Hainan Airlines Group Co., Ltd. The holding share of the Company is changed to 73.51% as control holder, Chang'an Aviation Industrial Company is 13.84% and Hainan Airlines Group is 12.65%. Accordingly, Chang'an Airlines is consolidated from 1 November 2001.
- F. Shanxi Airlines Co., Ltd. (“Shanxi Airlines”) was contributed and established by the Company, Shanxi Aviation Industrial Co., Ltd. and Chang’an Airlines Co., Ltd. The registered capital of recombined Shanxi Airlines Co., Ltd. is RMB320 million. The Company contributed RMB 285 million to own an interest of 89.06% share capital. Shaxi Aviation Industrial Company contributed the original net assets equivalent to RMB 20 million to own an interest of 6.25% share capital. Chang’an Airlines contributed RMB 15 million to own an interest of 4.69% share capital. All sides have already fully contributed their portions of the registered capital on 30 September 2002, which was validated by Taiyuan Zhongyuan CPA Firm. Shanxi Airlines was registered on 10 October 2002 at Shanxi Industrial & Commercial Administration Bureau. Accordingly, Shanxi Airlines is consolidated from 1 November 2002.

G. China Xinhua Airlines Co., Ltd. (“Xinhua Airlines”), a subsidiary of the Company, and Beijing Air Fushi International Investment Co., Ltd. (“Air Fushi”) entered into an contribution agreement to establish the Beijing Xinhua Air Catering Co., Ltd. (“Xinhua Catering”) in September 2002. The register capital of Xinhua Catering is RMB 29,990 thousand. Xinhua Airlines contributed RMB 15,294.9 thousand in cash to own an interest of 51% registered capital. All sides have already fully contributed their portions of the registered capital on 29 November 2002, which was validated by Beijing Yongtuo CPA Firm.

H. Chang'an Airlines Co. Ltd. ("Chang'an Airlines"), a subsidiary of the Company, and Hainan Aviation Hotel (Group) Co., Ltd. (“Hainan Aviation Hotel”) entered into an contribution agreement to establish Shanxi Chang’an Hainan Aviation Star Hotel Co., Ltd. (“Chang’an Hainan Aviation Star”) in May 2003. The register capital of Chang’an Hainan Aviation Star is RMB 25,000 thousand. Chang'an Airlines contributed RMB 20,000 thousand to own an interest of 80% and Hainan Aviation Hotel contributed RMB 5,000 thousand to own an interest of 20%.

VI. Notes to the consolidated financial statements

1. Cash in Bank and on Hand

	2003	2002
Cash on hand	732	30,828
Cash in bank	2,835,986	1,331,559
Other monetary assets	106,716	38,653
Total	2,943,434	1,401,040

Following are foreign currencies at 31 December 2003

Currency	Amount	Exchange Rate	2003
USD	194,071	8.2767	1,606,267
HKD	360	1.0657	384
Others	27		120
Total			1,606,771

2. Receivable (Including Account Receivable and Other Receivable)

(1) Account receivable aging analysis:

Aging	Amounts	2003		Amounts	2002	
		Percentage	Provision for bad debts		Percentage	Provision for bad debts
Within one year	316,421	92	0	397,289	89	0

1-2 years	7,020	2	1,448	6,434	1	1,576
2-3 years	3,182	0	35	2,058	1	689
More than 3 years	18,663	6	16,081	38,640	9	29,325
Total	<u>345,286</u>	<u>100</u>	<u>17,564</u>	<u>444,421</u>	<u>100</u>	<u>31,590</u>

Account receivables of the top five companies amounting to RMB 326,163 thousand cover 94% of the accounts.

There are no account receivables due from shareholders with over 5% interest.

(2). Other Receivables

Other receivable aging analysis:

Aging	2003			2002		
	Amounts	Percentage	Provision for bad debits	Amounts	Percentage	Provision for bad debits
Within 1 year	1,448,581	67	0	701,013	70	0
1-2 years	490,006	23	14,616	135,559	13	12,312
2-3 years	105,304	5	18,279	70,748	7	12,164
More than 3 years	105,320	5	47,257	96,200	10	20,650
Total	<u>2,149,211</u>	<u>100</u>	<u>80,152</u>	<u>1,003,520</u>	<u>100</u>	<u>45,126</u>

Other receivables of the top five companies amounting to RMB 1,016,360 thousand cover 47% of the accounts.

The main reason for increases in other receivables from year 2002 to year 2003 is due to the payment of aircraft for Deer Jet Co., Ltd. about RMB 294,637 thousand, and the payment of Yangpu Huanmei Industrial Co., Ltd., Hainan Yuhong Trade Co., Ltd. and Jiahui Investment Co., Ltd. and Haikou Meilan Airport Co., Ltd. etc. about RMB 803,507 thousand. And amounting to RMB 630,520 thousand of the above receivables have been received in April 2004.

The balance of other receivable mainly includes receivable amount due from deposits for operating aircraft leases and customs duty and related parties etc. (See Note VII). According to the opinion of the board of directors of the Company there is no recovery risk for receivables due from related parties and no bad debts provision should be provided for the related party receivables. No provision for bad debts is prepared for balance in relation to down payment and security deposits for leasing aircraft. Aging analysis method and individual cognizance method is adopted on the rest of other receivables.

Other receivables due from shareholders holding over 5% (including 5%) interest of the Company include Hainan Airlines Group Co., Ltd in amount of RMB 88,615 thousand.

3. Advance to Suppliers

Aging	2003		2002	
	Amount	Percentage	Amount	Percentage
Within 1 year	858,886	74	278,439	61
1—2 years	235,356	21	168,928	37
2—3 years	60,711	5	6,014	1
More than 3 years	3,079	0	2,500	1
Total	<u>1,158,032</u>	<u>100</u>	<u>455,881</u>	<u>100</u>

The main reason for increases in advance to suppliers from year 2002 to year 2003 is due to the advance to Hainan Yuhong Trade Co., Ltd. as amount to RMB 400,000 thousand. And the above receivables have been received in April 2004. There is no Advance to suppliers due from shareholders holding over 5% (including 5%) interest of the Company.

4. Inventories and provision for loss on realization of inventory

	2003		2002	
	Amount	Provision for loss on realization of inventory	Amount	Provision for loss on realization of inventory
High-value spare parts	918,369	16,378	1,157,586	16,378
Aviation materials	170,373	1,818	115,274	1,818
Catering supplies	6,916	83	7,686	83
Low cost consumables	8,084	0	9,315	0
Others	11,458	0	10,432	0
Total	<u>1,115,200</u>	<u>18,279</u>	<u>1,300,293</u>	<u>18,279</u>

5. Deferred and Prepaid Expenses

Items	2003	2002	The reason of balance
Aircraft operating lease rental	60,177	54,049	Regular balance
Others	<u>3,200</u>	<u>1,917</u>	Regular balance
Total	<u>63,377</u>	<u>55,966</u>	

6. Long-term Equity Investments

(1). Long-term equity investment:

Items	2003	2002
Associated company investment	741,376	676,569
Other equity investment	<u>135,388</u>	<u>155,538</u>
Total	<u>876,764</u>	<u>832,107</u>
The acquisition difference between investment of Xinhua	51,917	58,687

The acquisition difference between investment of Chang'an	7,737	8,726
The acquisition difference between investment of Shanxi	87,480	97,383
Less: Provision for loss on long-term investment	5,000	5,000
Long-term investment-net value	1,018,898	991,903

(2). Detail information of long-term equity investment:

Items	2003	2002	Shareholding	Provision for Loss	Notes
Associated undertakings company investment					
Haikou Meilan Airport Co., Ltd.	505,801	501,023	27.24%		A
Hainan Haihang Aircraft Maintenance Co., Ltd.	28,951	28,951	48%		
Hainan Haihang Airlines Aviation Import & Export Co., Ltd.	5,642	7,436	30%		
Hainan Sunshine City International Golf Club Co., Ltd.	34,000	34,000	34%		
Lucky Internantional Travel Services Limited	21,166	21,854	44%		
Beijing Yanjing Hotel Co., Ltd.	66,713	69,998	40%		
Beijing Vision Advertising Co., Ltd.	2,949	3,001	30%		
Xinda International Transportation Substitute Company	2,322	2,323	49%		
Beijing Hengshi Real Estate Development Limited	5,800	5,800	20%		
Beijing Tianchen Exhibition Company	958	1,038	20%		
Shenzhen Aviation Hotel	1,769	1,145	25%		
Chongqing Changjiang Leasing Company Limited	40,055	0	40%		B
Beijing Kehang Investment Company Limited	22,500	0	75%		C
Xinhua Airlines United Transportation Services Company	2,750	0	50%		D
Sub-total for associated undertaking company investment	741,376	676,569			
Other Investment					
Hainan Aviation Hotel (Group) Co., Ltd.	58,161	58,161	19%		
Hainan Xinguo Hotel Limited	15,000	15,000	15%		
Hainan Airlines Tourism Development Co. Ltd.,	3,274	3,274	3.30%		
Hainan Meilan Airport Co., Ltd.	6,906	6,906	2.20%		
China Civil Aviation Information Network Co. Ltd.,	29,860	29,860	3.39%		
Hainan Development Bank	5,000	5,000	0.30%	5,000	E
Yangtze River Express Co., Ltd.	10,000	30,000	5%		F
Shenhua Finance Co., Ltd.	5,000	5,000	1.60%		
Other investment	2,187	2,337			
Subtotal of other investment	135,388	155,538		5,000	
Total long term equity investment	876,764	832,107		5,000	

A. The Company and Hainan Airline Airport Management Co., Ltd. entered into an interest transfer agreement dated in April 2004. Pursuant to which the Company agree to transfer 160,000,000 shares of Hainan Meilan Airport Co., Ltd (10.76% equity interests of Hainan Meilan Airport Co., Ltd) own by the Company to Hainan Airline Airport Management Co., Ltd. Transfer price is RMB 201,600 thousand. After transferring, the equity interests of

Hainan Meilan own by the Company fall to 16.48%. The detail information of this transferring please refer to the related comments in Notes. XI-Subsequent Event.

B. The Company, Xinhua Airline Co., Ltd., the subsidiaries of the Company and Beijing Dongya Xinxing Economics Development Co., Ltd. (“Beijing Xinxing”) entered into an interest transfer agreement. Pursuant to which the Company and Xinhua Airline Co., Ltd. accepted Beijing Xinxing transfer to the interests of Chongqing Changjiang International Leasing Co., Ltd. Thereafter, the Company and Xinhua Airline Co., Ltd own an interest of 40% share capital of Chongqing Changjiang International Leasing Co., Ltd. jointly.

C. Xinhua Airline Co., Ltd. and Chang’an Airline Co., Ltd., the subsidiaries of the Company, and China International Public Relationship Association established Beijing Kehang Investment Co., Ltd. (Beijing Kehang) as dated in January 2003. The registered capital of Beijing Kehang is RMB 30,000 thousand. Xinhua Airline contributed RMB 15,000 thousand to own an interest of 50% share capital. Chang’an Airline and China International Public Relationship Association contributed RMB 7,500 thousand to own an interest of 25% share capital respectively. As at 31 December 2003, the total assets of Beijing Kehang is RMB 30,030 thousand, which is the 1.36% of the total assets of consolidation statement of the Company. Income and net income is zero. This company has not operated formally. Accordingly, Beijing Kehang is not consolidated in 2003.

D. In 2003, Xinhua Airline Co., Ltd., the subsidiaries of the Company, Hainan Aviation Jinpeng Sales Co., Ltd. and Hainan Aviation Hotel (Group) Co., Ltd. entered into an increasing Xinhua Airline United Transportation Co., Ltd.’s capital stated agreement. Pursuant to which Xinhua Airline own an interest of 50% share capital of Xinhua Airline United Transportation Co., Ltd. after increasing its capital sated.

E. On 21 June 1998, the People’s Bank of China announced that Hainan Development Bank liquidated. For protecting the rest interest of creditors, assets and liabilities of Hainan Development Bank were entrusted to Industrial and Commercial Bank of China (ICBC). A provision for decrement of the investment was accrued at 100% of total investment.

F. The Company and Hainan Aviation (Group) Co., Ltd entered into an interest transfer agreement dated in 27 November 2003. Pursuant to which the Company agree to transfer 10% equity interest of Yangtze River Express Co., Ltd. to Hainan Aviation (Group) Co., Ltd by the price as amount to RMB 20,000 thousand. This transferring arisen to a related-party transaction, the detail information of this transferring please refer to the related comments in Notes VIII, Related Party Transactions.

(3). Detail information of long-term equity investment:

	Initial investment	Addition in investment	Investment income	Increase/ Decrease	31/12/2003
Haikou Meilan Airport Co., Ltd.	198,520	205,230	102,051	307,281	505,801

Hainan Haihang Aircraft Maintenance Co., Ltd	50,000	-19,517	-1,532	-21,049	28,951
Hainan Haihang Airlines Aviation Import & Export Co., Ltd.	3,000	0	2,642	2,642	5,642
Hainan Sunshine City International Golf Club Co., Ltd.	34,000	0	0	0	34,000
Lucky International Travel Services Limited	22,000	0	-834	-834	21,166
Beijing Yanjing Hotel Co., Ltd.	11,269	62,120	-6,676	55,444	66,713
Beijing Vision Advertising Co., Ltd.	3,000	0	-51	-51	2,949
Xinda International Transportation Substitute Company	3,312	0	-990	-990	2,322
Beijing Hengshi Real Estate Development Limited	5,800	0	0	0	5,800
Beijing Tianchen Exhibition Company	1,038	0	-80	-80	958
Shenzhen Aviation Hotel	5,082	0	-3,313	-3,313	1,769
Beijing Kehang Investment Company Limited	22,500	0	0	0	22,500
Chongqing Changjiang International Leasing Company Limited	40,920	0	-865	-865	40,055
Xinhua Airlines United Transportation Services Company	2,750	0	0	0	2,750
Total	403,191	247,833	90,352	338,185	741,376

(4) Consolidation difference

Consolidation difference of the Company represents the acquisition difference between investments, the detail information as follow:

Items	Initial Difference	2002	Addition	Amortization	2003
Acquisition difference between investment of Xinhua	68,109	58,687	0	6,770	51,917
Acquisition difference between investment of Chang'an	9,878	8,726	0	989	7,737
Acquisition difference between investment of Shanxi	99,033	97,383	0	9,903	87,480
Total	177,020	164,796	0	17,662	147,134

7. Fixed Assets

(1) Cost and Accumulated depreciation

Cost	Plant & Building	Finance Leased Aircraft & Engines	Purchased Aircraft & Engines	Improvement of fixed assets by operating lease	Vehicles	Machinery & Equipment	Total
1 January 2003	1,711,475	5,422,120	6,858,079	208,802	157,400	233,718	14,591,594

Additions of Subsidiaries							
Additions*	146,145	1,009,430	2,646,497	284	13,748	59,053	3,875,157
Including: Construction in progress	145,546	0	1,432,995	0	324	4,520	1,583,385
Disposals	26,168	1,200,229	1,861,084	0	5,010	4,665	3,097,156
31 December 2003	<u>1,831,452</u>	<u>5,231,321</u>	<u>7,643,492</u>	<u>209,086</u>	<u>166,138</u>	<u>288,106</u>	<u>15,369,595</u>
Accumulated depreciation:							
1 January 2003	111,007	1,230,390	819,082	94,917	63,373	63,092	2,381,861
Additions of Subsidiaries by purchase							
Charge for the year	40,751	210,482	411,831	39,009	13,936	36,416	752,515
Disposals	3,224	209,289	237,279	0	3,059	3,108	455,959
31 December 2003	<u>148,534</u>	<u>1,231,583</u>	<u>993,634</u>	<u>134,016</u>	<u>74,250</u>	<u>96,400</u>	<u>2,678,417</u>
Net book value:							
31 December 2003	<u>1,682,918</u>	<u>3,999,738</u>	<u>6,649,858</u>	<u>75,070</u>	<u>91,888</u>	<u>191,706</u>	<u>12,691,178</u>
1 January 2003	<u>1,600,468</u>	<u>4,191,730</u>	<u>6,038,997</u>	<u>113,885</u>	<u>94,027</u>	<u>170,626</u>	<u>12,209,733</u>

- A. Increases in plant & building for RMB 145,546 thousand are mainly transferred from construction in progress including Xianyang Aircraft Parking Area, Residential Building-Bailong, Hainan Aviation Townhouse, Holiday Beach and Hainan Aviation Development Building B. The Company has not got parts of project completion reports and certification of property rights although they have been finished and in use. The Company estimated the value of these fix assets and accrued deprecation. It will be adjusted after getting the project completion report.
- B. Increase in finance lease of aircraft and engines for RMB 1,009,430 thousand is mainly due to sales and leaseback transactions of one B767 aircraft, one B737-300 aircraft, and sales and leaseback transactions for one finance leased B737-300 aircraft, which were purchased subsequently, also due to leaseback transaction of one finance leased Dornier aircraft engines, which were contributed to Chongqing Changjiang International Leasing Co., Ltd. subsequently.
- C. Decrease in finance lease of aircraft and engines for RMB 1,200,229 thousand is mainly due to the purchase of one finance leased B737-300 aircraft and one finance leased B767-300 aircraft.
- D. Increase in purchased Aircraft & engines for RMB 2,646,497 thousand is mainly due to the purchase of one finance leased B767-300 aircraft and one finance leased B737-300 and customs duty and Value Added Tax for purchasing one B767-300 aircraft and seven Dornier aircraft.
- E. Decrease in purchased Aircraft & engines for RMB 1,861,084 thousand is mainly due to the sales and leaseback transactions for one B767-300 aircraft and one B737-300 aircraft, and leaseback transactions for one purchased B737-300 aircraft finance leased formerly, also

due to the disposal of one DASH8-400 aircraft.

F. Fix assets of the Company mortgaged for borrowing up to 31 December 2003: Cost of plant and building is RMB 1,048,565 thousand, net value RMB 978,916 thousand; Cost of purchased aircraft and engine is RMB 3,781,528 thousand, net value RMB 3,426,689 thousand. (Cost of five finance leased Dornier standby aircraft and engine is RMB 74,550 thousand, net value RMB 70,856 thousand.)

G. The Company has not obtained property rights for part of buildings, the net book value of which is RMB 90,687 thousand. The Company confirmed that the acquisition of property rights is in process. According to Wan Yi Zi [2004] No. 64 verified by Hainan Wanli Legal Firm, the Company will get property rights without any legal barriers.

(2) Provision

Items	2002	Additions	Disposals	2003
Plant and Buildings	0	1,389	0	1,389
Total	0	1,389	0	1,389

The Building of Wutaishan Aircraft Parking Area, owned by the Shanxi Airlines, the subsidiaries of the Company, is planned to be disposal. According to the Accounting Systems for Business Enterprises, the provision of loss for fixed assets in amount of RMB 1,389 thousand is made in case of the disposal loss.

8. Construction in Progress

(1). Construction in Progress includes:

Items	2003	2002
Advance to supplier of Engine	822,508	534,031
Construction Projects	68,262	295,213
Total	890,770	829,244
Provision for loss of Construction in Progress	500	12,000
Construction in progress net value	890,270	817,244

(2). Movements of advance to suppliers of aircraft and engines

Items	2002	Additions	Disposal	2003
B767 aircraft	475,678	654,430	1,130,108	0
D-328 aircraft	58,287	514,697	560,764	12,220
B737-800 aircraft	0	810,288	0	810,288

Others	66	0	66	0
Total	534,031	1,979,415	1,690,938	822,508

(3). Detailed Movements of Construction Projects

Projects	2002	Additions of Subsidiary	Additions	Transfer to Fix Assets	Other Disposals	2003	Source of Fund	Stage of completion
Meilan Basis	0		3,262	3,262	0	0	Bank loans	Completed
Qionghai Aviation Training Base	0		785	785	0	0	Bank loans	Completed
Land in Xing Guo Road of Shanghai	77,848		0	0	77,848	0	Bank loans	Transferred
Holiday Beach	0		8,091	8,091	0	0	Bank loans	Completed
Mapo Building 2	0		424	424	0	0	Bank loans	Completed
Hainan Aviation Development Building B	0		3,890	3,890	0	0	Bank loans	Completed
Yazhou Garden	20,842		0	0	20,842	0	Bank loans	Transferred
No.1 Maintenance Project	0		1,965	1,965	0	0	Bank loans	Completed
Hainan Aviation Development Building accessory facilities	0		712	712	0	0	Bank loans	Completed
Townhouse 2nd Stage	0		4,390	4,390	0	0	Bank loans	Completed
Tianhai Garden	27,683		0	0	27,683	0	Bank loans	Transferred
Qionghai Base 2nd Stage	773		520	0	0	1,293	Bank loans	In progress
Townhouse 3 rd Stage	37,298		0	15,300	0	21,998	Bank loans	In progress
Sanya Travel Training School	0		550	0	0	550	Bank loans	In progress
Beijing Basis	2,107		2,421	0	0	4,528	Owned	In progress
Tianzhu Base 2nd Stage	8,121		7,594	0	0	15,715	Owned	In progress
Beijing Airport Catering Building	0		17,137	0	0	17,137	Owned	In progress
Xianyang Aircraft Parking Area	77,151		34,586	91,737	20,000	0	Owned	Completed
Residential Building	16,133		7,758	0	23,891	0	Owned	Transferred
Residential Building –Bailong	14,539		451	14,990	0	0	Owned	Completed
Others	12,718		-833	4,844	0	7,041	Owned	Completed
Total	295,213		93,703	150,390	170,264	68,262		

Other Disposals mainly refer to the project, Land in Xing Guo Road of Shanghai, Yazhou Garden and Tianhai Garden, transferred to Hainan Airlines Group Co. Ltd pursuant to a capital transfer agreement signed with Hainan Airlines Group Co. Ltd in 2003. The transaction has been published. For details, refer to the notes of connect transaction of this report.

Other Disposals in Xianyang Aircraft Parking Area mainly refer to the project transferred to Shanxi Chang'an Hainan Aviation Star Hotel Company Limited as the investment of Chang'an Airlines.

Increase in construction in progress includes capitalized interest in amount of RMB 2,430 thousand at the rate of 6%.

(4) Provision of loss for construction in progress

Project	2002	Additions	Disposals	2003
Land in Xing Guo Road in Shanghai	12,000	0	12,000	0
Xiguan Airport	0	500	0	500
Total	12,000	500	12,000	500

The Decrease of Land in Xing Guo Road in Shanghai mainly refer to the project transferred to Hainan Airlines Group Co. Ltd.

The Xiguan Airport is planned to be disposal. According to the Accounting Systems for Business Enterprises, the provision of loss for construction in progress in amount of RMB 500 thousand is made in case of the disposal loss.

9. Intangible Assets

Items	Land Use Right
Acquisition method	Purchase
Cost	21,091
31 December 2002	20,005
Additions of Subsidiary	0
Additions	0
Amortization	612
Accumulated amortization	1,698
31 December 2003	19,393
Remaining amortization years	21.6-37.5 years

10. Long-term deferred expenses

Items	2002	Additions	Amortization	2003	Cost Value	Remaining Amortization	Accumulated Amortization
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						Years	
Supervision for Reforming Aircraft	69,453	0	22,709	46,744	208,017	2-6years	161,273
Initial recruitment Pilot training Costs	268,558	75,373	51,070	292,861	441,107	2-7years	148,246
Rental for Tianzhu Basis	19,879	22	1,070	18,831	26,587	24years	7,756
User charge for Tianjin Aircraft Parking Area	9,093	0	399	8,694	9,760	22years	1,066
Others	80,074	949	37,248	43,775	322,313	1-6years	278,538
Total	447,057	76,344	112,496	410,905	1,007,784		596,879

11. Other long-term assets

The detail of deferred losses and gains of sales and leaseback as follow:

Lesser	2002	Additions	Amortization	Other Disposals	2003	Cost Value	Remaining Amortization Years	Accumulated Amortization
Sumisho Aircraft Asset Management B.V	62,317	0	8,867	0	53,450	65,744	6.5years	12,294
Mc. Aviation Financial Services (Europe) B.V	62,545	0	8,929	0	53,616	65,264	6.5years	11,648
North American Aircraft Leasing Company Limited	203,060	0	4,260	198,800	0	204,466		5,666
Jiangsu Leasing Co., Ltd.	-1,609	0	-81	0	-1,528	-1,616	19years	-88
Chongqing Changjiang International Leasing Company Limited	0	64,616	4,351	0	60,265	64,616	2-10.5years	4,351
Far East International Leasing Company Limited	0	28,845	2,349	0	26,496	28,845	10.5years	2,349
Shenzhen Leasing Co., Ltd.	-3,974	239,470	10,586	0	224,910	235,054	18.5-20years	10,144
Total	322,339	332,931	39,261	198,800	417,209	662,373		46,364

The balance of Deferred losses and gains of sales and leaseback represents the deferred losses or deferred gains arisen from the aircraft and engine sales and leaseback transactions. Deferred losses or deferred gains arisen from the operating leaseback transactions are amortized using the

straight-line method over the lease period. Deferred losses or deferred gains arisen from the finance leaseback transactions are amortized using the straight-line method over the estimated useful lives.

The other disposals of North American Aircraft Leasing Company Limited as amount to RMB 198,800 thousand mainly refer to purchased this leaseback as fixed assets.

12. Short-term Loans

		2003	2002	Interest rate per annum
Bank loans				
Including:	Unsecured loans	100,000	150,000	5.045%
	Mortgaged loans	237,334	570,855	4.779-5.841%
	Guaranteed loans	3,585,001	1,432,000	4.779-6.5%
Loans from other enterprises				
Including:	Unsecured loans	5,015	5,015	10%
Total		<u>3,927,350</u>	<u>2,157,870</u>	

13. Notes Payable

	2003	2002
Bank Acceptance	0	212,541
Commercial Acceptance	<u>438,447</u>	<u>54,000</u>
Total	<u>438,447</u>	<u>266,541</u>

The balance of notes payable mainly represents payment of fuel, take-off and catering expenses.

14. Payable

(1) Accounts Payable

The balance of accounts payable amounting to RMB 892,950 thousand on 31 December 2003, (RMB 393,784 thousand for 2002) mainly represent payables of aviation material, fighting fuel oil fee, take off expenses and payables of selling tickets for other airline companies. The increase of the balance as at 31 December 2003 mainly due to the extension of maturity. There is no account payable due to shareholders holding over 5% (including 5%) interest of the Company.

(2) Other Payables

The balance of other payable is RMB 408,759 thousand in the end of year 2003 (RMB 432,151 thousand for 2002). The other payable due to shareholders holding over 5% (including 5%) interest of the Company is the payables due to Hainan Aviation Group Co., Ltd. as amount of RMB 38,602 thousand.

15. Dividend Payable

Items	2003	2002	Reason
Legal person shares	23,230	17,820	Normal arrears to pay
Others	3,682	7,786	Normal arrears to pay
Total	<u>26,912</u>	<u>25,606</u>	

16. Taxes Payable

Taxation	2003	2002
VAT payable	177,415	114,647
Business tax payable	1,601	7,974
City construction tax payable	1,607	2,262
Income tax payable	1,004	5,859
Withhold IIT	1,427	0
Customs duty	29,002	6,478
Others	298	165
Total	<u>212,354</u>	<u>137,385</u>

For details of the tax rate of the Company and the subsidiary company see note IV.

17. Other payable to government

	2003	2002
Civil aviation infrastructure levies payable	2,386	60,505
Education surcharge	1,338	1,614
Total	<u>3,724</u>	<u>62,119</u>

The balance of Civil aviation infrastructure levies payable for the year ended 31 December 2003 is RMB 2,386 thousand, which was levies payables of China Xinhua Airlines Company, Changan Airlines Company and Shanxi Airline Company from 1 January 2003 to 30 April 2003, 5% of domestic and 2% of international traffic revenues. From 1 May 2003 to 30 September 2003, pursuant to Cai Zong Ming Dian [2003] No. 1, “the notice of exemption of governmental fund to those industries suffered for SARS issue by Ministry of Finance”, the Company did not need to accrue the payables. From 1 October 2003 to 31 December 2003, according to Civil Aviation telegraph, “the notice of in relation to clearing civil aviation infrastructure levies payable”, the Company keep on exempting. As mentioned on notes XII.1, headquarter of the Company does not accrue levies payable.

18. Accrued Expenses

Items	2003	2002
fuel expenses	232,889	68,650
Take-off expenses	191,362	115,387
Catering expenses	43,630	33,412
Loan interest	34,663	43,186
Provision for aircraft overhaul	1,838	25,023
Fee of computer reservation	41,658	13,467
Aircraft insurance premium	11,959	8,894
Others	4,243	3,382
Total	562,242	311,401

19. Sales in Advance of Carriage

The balance of sales in advance of carriage represents the amount of sold but unused tickets.

20. Current Portion of Long-term Liabilities

	2003	2002
Current portion of long-term loans (a)	1,058,177	537,440
Current portion of long-term payable (b)	644,315	442,441
Total	1,702,492	979,881
Plus: Unrecognized finance leasing	91,614	0
Current Portion of Long-term Liabilities	1,610,878	979,881

(a) Current portion of long-term loans

		2003	2002
Bank loans			
Including:	Unsecured loans	55,000	291,111
	Mortgaged loans	306,700	50,000
	Guaranteed loans	525,978	37,000
	Subtotal	<u>887,678</u>	<u>378,111</u>
Loans from other financial institutions			
Including:	Unsecured loans	170,499	159,329
	Subtotal	<u>170,499</u>	<u>159,329</u>
Total		<u>1,058,177</u>	<u>537,440</u>

(b) Current portion of long-term payables

Current portion of long-term payables of the Company is payables due within one year for finance leasing aircraft and engines.

Name	Period	Cost Value	Interest Payable	2003
International Commercial Machinery	2years	3,512	83	1,828
Chongqing Changjing International Leasing Co., Ltd.	2-3years	214,960	10,204	94,832
Pacific American Corporation	4.5years	24,921	1,914	11,888
Raytheon	11.5years	82,880	2,123	6,890
Xinjiang Leasing Co., Ltd	8years	150,000	12,272	12,279
Shenzhen Finance & Leasing Co. Ltd	5-10years	885,860	53,882	139,056
Sino-America Aviation	11.5years	1,437,975	23,368	127,448
New Century Finance & Leasing Co. Ltd	3years	133,544	3,945	34,912
Jiangsu Leasing Co., Ltd.	3years	37,111	2,058	8,926
StructuredTradeFinance Group	11-13years	1,176,864	21,354	132,081
Far East International Leasing Co., Ltd.	2-4.5years	307,040	17,182	74,175
Total		<u>4,454,667</u>	<u>148,385</u>	<u>644,315</u>

21. Long-term Loans

	2003	2002
Bank loans		

Including:	Unsecured loans	781,627	696,629
	Mortgaged loans	6,243,832	3,474,492
	Guaranteed loans	677,919	698,616
	Hypothecation loans	850,000	1,110,000
	Subtotal	<u>8,553,378</u>	<u>5,979,737</u>
Loans from other financial institutions			
Including:	Unsecured loans	1,409,383	1,579,896
	Subtotal	<u>1,409,383</u>	<u>1,579,896</u>
Total		<u><u>9,962,761</u></u>	<u><u>7,559,633</u></u>

22. Long-term Payables

(1) Detail information of long-term payables by remaining due years:

Items	2003	2002
Minimum Lease Payments		
Including: The second year	603,089	433,270
The third year	453,673	452,878
Following years	1,940,706	2,202,903
Total	<u>2,997,468</u>	<u>3,089,051</u>
Plus: Unrecognized finance leasing expenses	273,075	0
Long-term Payables	<u><u>2,724,393</u></u>	<u><u>3,089,051</u></u>

Long –term payables represent payments for finance leasing aircraft and engines. The long-term payable due in one year is classified as current portion of long-term liabilities

(2) Detail information of long-term payables by clients:

Name	Remaining Amortization Years	Cost Value	Interest Payable	2003	Nature
Raytheon	11.5years	82,880	8,251	61,277	Finance leasing aircraft
Xinjiang Leasing Co., Ltd	8years	150,000	38,184	114,333	Finance leasing aircraft
Shenzhen Finance & Leasing Co. Ltd	5-10years	885,860	238,793	926,183	Finance leasing aircraft engines
Pacific American Corporation	4.5years	24,921	576	5,562	Finance leasing aircraft engines
Sino-America Aviation	11.5years	1,437,975	108,905	1,245,558	Finance leasing aircraft
New Century Finance & Leasing Co. Ltd	3years	133,544	1,567	35,658	Finance leasing aircraft engines
Jiangsu Leasing Co., Ltd.	3years	37,111	2,923	26,777	Finance leasing aircraft engines
Chongqing Changjing International Leasing Co., Ltd.	2years	214,960	4,248	82,289	Finance leasing aircraft engines

Structured Trade Finance Group	11-13years	1,176,864	22,849	257,327	Finance leasing aircraft
International Commercial Machinery	2years	3,512	6	460	Finance leasing notebook computer
Far East International Leasing Co., Ltd.	5years	290,000	30,318	242,044	Finance leasing aircraft
Total		4,437,627	456,620	2,997,468	

23. Specific Payables

The balance of specific payment for the year ended 31 December 2003 is RMB 20,000 thousand, which is a financial allocation appropriated by the Shanxi Development and Planning Committee to Chang'an Airlines for the project of Xianyang Aircraft Parking Area pursuant to Shan Ji Tou Zi[2001]No.1239.

24. Other Long-term Liabilities

The balance of other long-term liabilities is RMB 244,915 thousand as of 31 December 2003 is the VAT payables and customs duty for finance lease and purchased aircraft which due after year 2005.

25. Minority Interests

Subsidiary Company	Owners Equity	Proportion of Minority interest	Minority Interests
China Xinhua Airlines Co., Ltd.	1,481,870	40%	592,748
Changan Airlines Co., Ltd.	400,199	26.49%	102,013
Shanxi Airlines Co., Ltd.	201,638	6.25%	12,602
Other			36,839
Total			744,202

* Others are minority interests of Hainan Airlines Catering Co., Ltd, Hainan Airlines VIP Flight Services Co., Ltd and Beijing Xinhua Airlines Catering Co., Ltd, a subsidiary of Xinhua Airlines.

26. Share Capital

Share capital of the Company is RMB 1 Yuan per share

	2002	Increase /Decrease	2003
(1) Unlisted shares			
(a) Promoter shares	134,837	0	134,837
Including: State shares	17,289	0	17,289
(b) PRC legal person shares	38,735	0	38,735

(c)Foreign legal person shares	108,043	0	108,043
(d)Employee shares	0	0	0
Subtotal	281,615	0	281,615
(2) Listed shares			
(a)Domestic investment shares-A shares	371,958	0	371,958
(b)Foreign investment shares-B shares	76,680	0	76,680
Subtotal	448,638	0	448,638
Total	730,253	0	730,253

27. Capital Surplus

Items	2002	Additions	Disposals	2003
Share premium	965,745	0	0	965,745
Donated aviation materials	11,056	0	0	11,056
Share premium from Associated Company	61,605	0	0	61,605
Closing Balance	1,038,406	0	0	1,038,406

28. Surplus Reserve

Items	2002	Additions	Disposals	2003
Statutory surplus reserve	115,003	0	0	115,003
Statutory Employee Welfare Reserve	54,095	0	0	54,095
Total	169,098	0	0	169,098

29. Retained Earning

	2003	2002
Beginning balance	462,455	418,672
Add: Current year profit	-1,269,246	103,056
Less: Appropriation to statutory surplus reserve	0	-10,306
Appropriation to general surplus reserve	0	0
Appropriation to statutory welfare reserve	0	-5,153
Dividends being transferred to share capital	0	0
Dividends declared	14,606	-43,814
Ending balance	-821,397	462,455

(1) There is a difference of undistributed profit amounting to RMB14,047 thousand between the amount RMB -821,396 thousand in the consolidated statement at the year ended 2003 and the amount RMB -807,349 thousand in the parent company's statement at the year ended 2003. The reason for it is that the accumulated loss of Hainan Airlines VIP Flight Services Co., Ltd. had already exceeded its paid-in capital, and no investment loss has been recognized in the Financial Statement of

the parent company against the portion of loss that is exceeded to its paid-in capital. Since the cost of investment has already been reduced to zero previously.

- (2) As we mentioned in note III.20 above, due to the change of accounting policy, the Company increase the beginning balance of undistributed profit as amount of RMB 21,248 thousand, thereinto decrease as amount of RMB 22,567 thousand due to the change in cost variance of high spare parts amortization method, and increase as amount of RMB 43,815 thousand due to the change in dividend distributed recognized period.

30. Sales

Items	2003	2002
Passenger revenue	4,976,714	4,646,674
Cargo and Excessive weight of luggage revenue	213,012	192,478
Charter flight revenue	171,263	171,160
Others	11,102	17,970
Total	<u>5,372,091</u>	<u>5,028,282</u>

31. Turnover Tax and Surtax

Items	2003	2002
Business tax	57,663	150,047
City construction tax	4,180	10,632
Education surcharge	1,824	4,533
Regulating Fund for Price Fluctuation	41	11
Total	<u>63,708</u>	<u>165,223</u>

32. Income from other operations

Items	2003	2002
Ticket refund charges	17,135	16,054
Net gain from sales of aviation materials	0	8,847
Agent handling fees	4,128	3,108
Cargo Service Fee	16,288	13,237
Others	-5,749	666
Total	<u>31,802</u>	<u>41,912</u>

33. Financial Expenses

Items	2003	2002
--------------	-------------	-------------

Interest expenses	724,000	525,027
Less: Interest income	8,989	5,451
Exchange loss	308	2,491
Less: Exchange gain	0	0
Others	24,163	33,563
Total	<u>739,482</u>	<u>555,630</u>

34. Investment Income

1. Items		2003	2002
Haikou Meilan Airport Co., Ltd	A	4,778	31,714
Hainan Haihang Airlines Aviation Import & Export Co., Ltd.	A	2,056	4,528
Deer Jet Co., Ltd.	A	0	-9,755
Hainan Haihang Aircraft Maintenance Co.	A	0	-163
Lucky Internantional Travel Services Limited	A	-688	-113
Shenzhen Aviation Hotel	A	625	-2,090
Chongqing Changjiang International Leasing Co., Ltd.	A	-865	0
Beijing Yanjing Hotel Co., Ltd.	A	-3,284	0
Aviation Information System Company	B	2,033	0
Hainan Meilan Airport Co., Ltd	B	1,100	952
Shenzhen Aviation Kaiya Co., Ltd.	B	167	0
Amortization of acquisition difference between investment	C	-17,663	-13,096
Others		-890	215
Total		<u>-12,631</u>	<u>12,192</u>

A Investment income is accounted for by using equity method.

B Return earning is accounted for by using cost method.

C Long-term investment balance of the China Xinhua Airline Co., Ltd., Changan Airline Co., Ltd. and Shianxi Airline Co., Ltd. is the amortized acquisition difference in this year.

Above investment income will be received without restriction.

35. Subsidiary Income

Item	2003	2002
Turnover tax refund	7,966	6,971
Interest refund of loan with discount	500	0
Total	<u>8,466</u>	<u>6,971</u>

The turnover tax refund income is the business tax refund of Xinhua Airline Company by Tianjin Ministry of Finance.

36. Non-operating Income and non-operating expenses

(1) Non-operating Income

Items	2003	2002
Insurance income	124	0
Penalty income	352	337
Net gain from disposal of fixed assets	6,960	495
Others	4,559	404
Total	<u>11,995</u>	<u>1,236</u>

(2) Non-operating expenses

Items	2003	2002
Net loss from disposal of fixed assets	14,607	2,043
Donation	0	30
Others	8,966	666
Total	<u>23,573</u>	<u>2,739</u>

VII. Disclosures of significant matters in relation to the holding company

1. Long-term stock investment

1). Long-term stock investment

	2003	2002
Subsidiary	1,652,381	2,077,239
Associated undertakings	604,482	582,297
Others	115,617	135,617
Total	<u>2,372,480</u>	<u>2,795,153</u>
Less: Provision for loss on long-term investments	<u>5,000</u>	<u>5,000</u>
Long-term investment –Net value	<u>2,367,480</u>	<u>2,790,153</u>

2). Detail information of Long-term stock investments

Company	2003	2002	Owned Interests
Subsidiary			
Hainan Golden-Deer Aviation Sales Co., Ltd.	113,649	113,566	95%
Hainan Airlines Catering Co., Ltd.	28,711	26,346	51%
China Xinhua Airlines Co., Ltd	941,039	1,153,794	60%
Changan Airlines Co., Ltd	301,924	511,403	73.51%

Shanxi Airlines Co., Ltd	267,058	272,130	89.06%
Subtotal	1,652,381	2,077,239	
Associated undertakings			
Haikou Meilan Airport Co., Ltd	505,801	501,023	30%
Hainan Haihang Aircraft Maintenance Co. Ltd	28,951	28,951	48%
Hainan Haihang Airlines Aviation Import & Export Co., Ltd.	5,642	7,436	30%
Hainan Sunshine city International Golf Club Ltd.	34,000	34,000	34%
Chongqing Changjiang International Leasing Co., Ltd.	19,505	0	20%
Lucky Internantional Travel Services Limited	10,583	10,887	22%
Subtotal	604,482	582,297	
Others			
Hainan Airlines Hotel (Group) Co., Ltd.	58,161	58,161	19%
Hainan Air Tourism Developing Co.,Ltd	3,274	3,274	3.30%
Hainan Meilan Airport Company Limited	6,906	6,906	2.20%
Hainan Xinguo Hotel Limited	15,000	15,000	15%
China Airline Infor Network Co., Ltd.	17,000	17,000	1.93%
Hainan Development Bank	5,000	5,000	0.30%
Yangtze River Express Co., Ltd.	10,000	30,000	15%
Others	276	276	
Subtotal	115,617	135,617	
Total	2,372,480	2,795,153	

3) Detail information of Long-term equity investments:

Item	Original Amount	Additions	Accumulated income	Accumulated changes	2003
Hainan Golden-Deer Aviation Sales Co., Ltd.	8,000	0	105,649	105,649	113,649
Hainan Airlines Catering Co., Ltd.	15,810	0	12,901	12,901	28,711
China Xinhua Airlines Co., Ltd	934,343	161,176	-154,480	6,696	941,039
Changan Airlines Co., Ltd	554,563	0	-252,639	-252,639	301,924
Shanxi Airlines Co., Ltd	285,000	0	-17,942	-17,942	267,058
Haikou Meilan Airport Co., Ltd	198,520	205,230	102,051	307,281	505,801
Hainan Haihang Aircraft Maintenance Co. Ltd	50,000	-19,517	-1,532	-21,049	28,951
Hainan Haihang Airlines Aviation Import & Export Co., Ltd.	3,000	0	2,642	2,642	5,642
Hainan Sunshine city International Golf Club Ltd.	34,000	0	0	0	34,000
Chongqing Changjiang International Leasing Co., Ltd.	19,880	0	-375	-375	19,505
Lucky Internantional Travel Services Limited	11,000	0	-417	-417	10,583
Total	2,114,116	346,889	-204,142	142,747	2,256,863

2、Investment income:

Item		2003	2002
Hainan Airlines Catering Co., Ltd.	A	2,448	3,213
China Xinhua Airlines Co., Ltd	A	-205,984	41,222
Changan Airlines Co., Ltd	A	-208,491	-42,207
Shanxi Airlines Co., Ltd	A	4,832	-11,220
Deer Jet Co., Ltd.	A	0	-9,755
Hainan Haihang Airlines Aviation Import & Export Co., Ltd.	A	2,056	4,529
Haikou Meilan Airport Co., Ltd	A	4,778	31,714
Lucky Internantional Travel Services Limited	A	-304	-113
Chongqing Changjiang International Leasing Co., Ltd.	A	-375	0
Hainan Haihang Aircraft Maintenance Co. Ltd	A	0	-163
Amortization of Acquisition Difference between equity investment		-17,663	-9,705
Aviation Information System Company	B	2,033	0
Hainan Meilan Airport Co., Ltd.	B	1,099	952
Total		-415,571	8,467

A Investment income from subsidiaries and affiliated company is accounted for by using equity method.

B Return earning is accounted for by using cost method.

VIII. Related Party Transactions

(1). Related parties with controlling interest

Company Name	Registered Place	Principal activities	Relationship	Business Character /Style	Legal represent-ative
HainanGolden-Deer Sales Co., Ltd.	Aviation Haikou	Provision of transportation and chartered flight agency services	Subsidiary	Limited Company	Feng Chen
Hainan Airlines VIP Flight Service Co. Ltd.	Haikou	Chartered flights agency	Subsidiary	Joint Venture	Feng Chen
Hainan Airlines Catering Co.,Ltd	Haikou	Food and present for passengers	Subsidiary	Joint Venture	Feng Chen
China Xinhua Airlines Co., Ltd	Beijing	approved international and domestic air passenger and cargo transportation	Subsidiary	Limited Company	Jiaxu Liu

Chang'an Airlines Co., Ltd	Xi'an	Air passenger and cargo transportation in Shanxi province and its surrounding provinces	Subsidiary	Limited Company	Yining She
Shanxi Chang'an Hainan Aviation Star Hotel Co., Ltd.	Xi'an	Hotel and catering, commodity, costume sales, typing and other office services.	Subsidiary	Limited Company	Yongqing Ma
Shanxi Airlines Co., Ltd	Taiyuan	Air passenger and cargo branch line transportation in Shanxi province and its surrounding provinces	Subsidiary	Limited Company	Jianmin Qin
Beijing Xinhua Air Catering Co., Ltd.	Beijing	Production and sale of pastry, food and beverage	Subsidiary	Limited Company	Zhongying Zhao

(2). Change of owned interests and registered capital for the related parties with controlling interests

Company Name	Registered Capital		Owned interest	
	2003	2002	2003	2002
	Hainan Golden-Deer Aviation Sales Co., Ltd.	RMB 8,000,000 Yuan	RMB 8,000,000 Yuan	95%
Hainan Airlines VIP Flight Service Co., Ltd.	USD 1,020,408 Yuan	USD 1,020,408 Yuan	51%	51%
Hainan Airlines Catering Co., Ltd.	RMB 31,000,000 Yuan	RMB 31,000,000 Yuan	51%	51%
Xinhua Airlines Co., Ltd	RMB 1,830,000,000 Yuan	RMB 1,830,000,000 Yuan	60%	60%
Changan Airlines Co., Ltd	RMB 754,390,000 Yuan	RMB 754,390,000 Yuan	73.51%	73.51%
Shanxi Airlines Co., Ltd	RMB 320,000,000 Yuan	RMB 320,000,000 Yuan	92.51%	92.51%
Beijing Xinhua Air Catering Co., Ltd.	RMB29,990,000 Yuan	RMB29,990,000 Yuan	51%	51%
Shanxi Chang'an Hainan Aviation Star Hotel Co., Ltd.	RMB 25,000,000 Yuan	0	80%	80%

(3). Pricing Policy

Market prices were used for all significant related party transactions.

- (4). Related parties without controlled relationship: (Only included significant transactions of related parties)

Companies	Relationship
Hainan Aviation Group Co.,Ltd.	Shareholder
Haikou Meilan Airport Co., Ltd.	Associated Undertaking
Hainan Meilan Airport Co., Ltd.	Associated Company
Hainan Airlines Hotel (Group) Co., Ltd.	Associated Undertaking
Hainan Haihang Airlines Aviation Import & Export Co., Ltd.	Associated Undertaking
Deer Jet Co., Ltd.	Associated Undertaking
Beijing Yanjing Hotel Co., Ltd.	Associated Company
Lucky Internantional Travel Services Limited	Associated Company
Hainan Meiya Aviation Fuel Co.,Ltd.	Subsidiaries of Associated Company

- (5). The Company has the following significant transactions of related parties.

- (a) Transactions of related parties

Related Party	Relationship	Description	2003	2002	
Hainan Aviation Group Co., Ltd.	A	Shareholds	Equity investments acquiring and transfer of construction project	134,375	167,443
Hainan Meiya Aviation Fuel Co.,Ltd.	Associated company		Payment for fuel	187,891	138,670
Haikou Meilan Airport Company Limited Co., Ltd.	Associated undertaking		Haikou Meilan Airport Company Limited Co.,Ltd.	114,478	78,609
Chongqing Changjiang International Leasing Co., Ltd.	B		Finance lease of aviation material	238,521	0
Hainan Haihang Airlines Aviation Import & Export Co., Ltd.	Associated undertaking		Handling fee in related to purchases of airplanes, aviation materials	7,176	3,759

- A. The Company and Hainan Airlines Group Co. Ltd entered into an interest transfer agreement in 2003. Pursuant to which the Company agree to transfer an interest of 10% share capital of Yangtze River Express Co., Ltd. to Hainan Airlines Group Co. Ltd. The transfer price is due to the actual contribution in amount of RMB 20,000 thousand.

The Company and HNA Group Co., Ltd. entered into a capital transfer agreement dated in December 2003. Pursuant to which the Company agreed to transfer Construction In Progress, including Land in Xing Guo Road of Shanghai, Yazhou Garden and Tianhai Garden owned by the Company in amount of RMB 114,374.50 thousand.

The above transferring are settled by cash, and there is no impact on the profit and loss account.

B. The Company and Xinhua Airline finance lease one B737-300 and aviation material due from Chongqing Changjiang Leasing Co., Ltd. in 2003, and the minimum lease payments is RMB 238,521 thousand.

(b) Related party balance

Items	Related party	Notes	2003	2002
Account receivable	Yangtze River Express Co., Ltd.		13,529	0
Account receivable	Deer Jet Co., Ltd.		22,684	0
Account receivable	Hainan Haihang Airlines Aviation Import & Export Co., Ltd.		427	0

Other receivable	Hainan Airlines Hotel (Group) Co., Ltd.	15,406	1,908
Other receivable	Deer Jet Co., Ltd.	294,237	44,744
Other receivable	Hainan Aviation Group Co., Ltd.	88,615	3,182
Other receivable	Hainan Haihang Airlines Aviation Import & Export Co., Ltd.	6,819	0
Other receivable	Haikou Meilan Airport Co., Ltd.	172,987	0
Other receivable	Hainan Meilan Airport Co., Ltd.	56	0
Other receivable	Yangtze River Express Co., Ltd.	1,080	0
Advance to Suppliers	Haikou Meilan Airport Co., Ltd.	216	0
Advance to Suppliers	Hainan Meilan Airport Co., Ltd.	24	0
Advance to Suppliers	Hainan Haihang Airlines Aviation Import & Export Co., Ltd.	68,866	102,626
Advance to Suppliers	Chongqing Yangzjiang International Leasing Co., Ltd.	200	0
Accounts payable	Yangtze River Express Co., Ltd.	35,906	0
Accounts payable	Hainan Haihang Airlines Aviation Import & Export Co., Ltd.	8,763	0
Accounts payable	Haikou Meilan Airport Co., Ltd.	89,391	15,619
Accounts payable	Hainan Meilan Airport Co., Ltd.	81,497	20,061
Accounts payable	Hainan Meiya Aviation Fuel Co.,Ltd.	5,682	16,783
Accounts payable	Deer Jet Co., Ltd.	1,216	0
Accounts payable	Hainan Airlines Hotel (Group) Co., Ltd.	10,487	0
Other payable	HNA Group Co., Ltd.	38,602	0
Other payable	Hainan Airlines Hotel (Group) Co., Ltd.	6,191	0
Other payable	Deer Jet Co., Ltd.	28,682	0
Other payable	Lucky Internantional Travel Services Limited	23,318	23,318
Other payable	Haikou Meilan Airport Co., Ltd.	33,000	0
Other payable	Hainan Meilan Airport Co., Ltd.	2,588	0
Other payable	Beijing Yanjing Hotel Co., Ltd.	42,001	42,000
Other payable	Yangtze River Express Co., Ltd.	228	24,535
Long-term payable	Chongqing Changjiang Leasing Co., Ltd.	177,121	0

IX. Contingency

As at 31 December 2003, the Holding Company guaranteed for the bank loans of its subsidiaries as amount of RMB 79,000 thousand, include two for Chang'an Airline as total amount of RMB 49,000 thousand, the maturity is 27 February 2004 and 30 March 2004, one for Shanxi Airlines as amount of RMB 30,000 thousand, the maturity is 26 March 2004.

X. Commitment

(1) Capital and financial commitments

As of 31 December 2003 the Company had capital and financial commitments in respect of the purchase of aircraft and engines, construction with total amount of RMB 2,757,788 thousand.

(2) Obligation under operating leases

As of 31 December 2003, the Company had obligation under non-cancelable operating leases of aircraft in the respective periods as follows:

	2003	2002
Within one year	566,751	476,729
The second year	467,776	432,417
The third year	274,508	319,906
The following years	1,097,313	513,581
Total	<u>2,406,348</u>	<u>1,742,633</u>

XI. Subsequent events

1. In accordance with the approval of Notice on Appraisal of Issuing Unlisted Foreign Investment Shares for HNA Co., Ltd. (Zheng Jian Zi[2003]No.2) issued by the CSRC on 16 January 2003, the unlisted foreign investment shares of the company was transferred 108,043,201 shares to B shares and could be listed after one year, as at 17 January 2004, at Shanghai Stock Exchange.
2. The Company and Hainan Airline Airport Management Co., Ltd. entered into an interest transfer agreement dated in April 2004. Pursuant to which the Company agree to transfer 160,000,000 shares of Hainan Meilan Airport Co., Ltd (10.76% equity interests of Hainan Meilan Airport Co., Ltd) own by the Company to Hainan Airline Airport Management Co., Ltd. Transfer price is 1.26 yuan per share, total amount as to RMB 201,600 thousand

which received at 12 April 2004. After transferring, the equity interests of Hainan Meilan own by the Company fall to 16.48%.

XII. Other Matters

1. According to the relevant regulations issued by the Ministry of Finance and the Civil Aviation Administration of China, PRC airlines companies are required to pay civil aviation infrastructure levies equal to 10% of domestic traffic revenues. In addition, according to Cai Zong Zi [1999] No. 11 “Notification of reduction civil aviation infrastructure levies” approved by the Ministry of Finance and the National Developing and Planning Committee, civil aviation infrastructure levies was reduced to 8% of domestic traffic revenues from 1, January 1998, and 5% of domestic and 2% of international traffic revenues were levied from 1, January 1999. In this regard, the total levies from 1 January 2003 to 30 April 2003 is RMB 49,423 thousand and not be levied from 1 May 2003 to 31 December 2003 due to the reason mentioned in notes VI. 17. As of 31 December 2003, the Company had accumulated total levies liabilities of RMB 950,534 thousand. In November 1994, the Hainan Provincial Government applied in Qiong Fu Han [1994] No. 77 to the Ministry of Finance for exemption of the payment of the levies or granting the levies by the Company so paid as infrastructure investment in the Company. As at the date of this report, such application has not yet been approved by the Ministry of Finance.

A circular Qiong Cai Shui (1996) No. 132 was issued by the Hainan Provincial Finance and Tax Bureau on 18 October 1996, pursuant to which the Finance and Tax Bureau agreed to assist in relation to the application for exemption of payment of levies with the Ministry of Finance and the Civil Aviation Administration of China and to undertake to resolve the matter through other means if the application is rejected. Hainan WanLi Law Office has independently issued an opinion that under the PRC law and on the strength of the said circular, the Company will have entirely been relieved of its liability and obligation to make any payment or provision in its financial statements in respect of the contributions to the civil aviation infrastructure levies on 29 March 2004. On this basis no provision for payment of such levies has been made in this report.

2. According to the resolution of the 18th session of the 3rd board of directors on 15 August 2002, Chang’an Airlines proposed to acquire a 85% equity interests of Yangtze River Express Co., Ltd., the book value of which is RMB 170,000 thousand, from HNA Group Co., Ltd. The transfer belongs to a related party transaction. The proposal was passed in the second temporary general meeting. According to the resolution of the 4th session of the 4th board of directors on 28 November 2003, About stopping Chang’an Airlines acquiring a 85% equity interests of Yangtze River Express Co., Ltd., passed by BOD, the Company give up the above equity interest transfer.
3. Industrial and Commercial Bank of China provided a maximum comprehensive credit limitation in amount of RMB 3,774,480 thousand, including RMB 3,172,000 thousand for

the Holding Company, RMB 480,000 thousand for Xinhua Airlines, RMB 49,000 thousand for Chang'an Airlines, RMB 60,000 thousand for Shanxi Airlines, RMB 13,480 thousand for Hainan Airlines Catering Co., Ltd.

XI. Documents for Reference

The complete set of documents is available at the office of the Company for the reference of the China Securities Regulatory Committee, Shanghai Stock Exchange, Hainan Provincial Securities Administration Office as well as relevant authorities and shareholders:

1. The accounting statement bearing signatures and stamps of the legal representative, chief financial officer and chief of the accounting institution.
2. The original copy of the auditing report bearing the stamp of the accounting firm and signature & stamp of the certified accountant.
3. The original copies of documents and notices published on Shanghai Securities News, China Securities News and Hong Kong's Wen Wei Po in the report period.

Hainan Airlines Company Limited

Chairman:

Date: April 29, 2004