

The Company has entered into a financial agreement dated 22 May, 1997, with SA Finance for the provision of financial services such as deposit and loan facilities, credit facilities, financial guarantees and credit references for a term commencing from 22 May, 1997 to 22 May, 2000. The agreement has been extended to 22 May, 2001.

Under such agreement, (a) all funds that the Company deposits with SA Finance will be deposited by SA Finance with the Commercial and Industrial Bank of China, Bank of Communications, Bank of Agriculture, China Construction Bank, or other banks of similar creditworthiness; and (b) SA Finance will not at any time have outstanding loans in excess of the amount representing the aggregate of (i) deposits received from entities other than the Company, (ii) SA Finance's shareholders' equity and (iii) capital reserves.

The Group had short-term deposits placed with SA Finance amounting to RMB1,961,890,000, as at 31 December, 2000, which earned interest at the rate of 1.98%-5.00% per annum.

- (iv) Shenzhen Air Catering Company Limited, which is 20% owned by the SA Group, and 80% owned by two independent third parties

The Company and Shenzhen Air Catering Company Limited have entered into an agreement dated 23 May, 1997 for the sale and purchase of in-flight meals for flights originating or stopping at the airport in Shenzhen. Pursuant to such agreement, Shenzhen Air Catering Company Limited will supply in-flight meals to the Group from time to time during the term from 23 May, 1997 to 23 May, 1998. The agreement has been extended by the parties to 23 May, 2001.

For the year ended 31 December, 2000, the amount paid by the Group to Shenzhen Air Catering Company Limited for the provision of in-flight meals was approximately RMB17,941,000.

- (v) Guangzhou Aircraft Maintenance Engineering Company Limited ("GAMECO"), which is 50% owned by the Company and 50% owned by two independent third parties

The Company and GAMECO have entered into an Aircraft Maintenance and Engineering Agreement for the provision of aircraft repair and maintenance services. On 17 May, 1996, the Company and GAMECO entered into an agreement regarding the fee arrangement for the provision of such repair and maintenance services (the "Fee Agreement"). Pursuant to the Fee Agreement and subsequent agreements, GAMECO charged the Company for expendables at cost plus 15%, and labour costs at US\$30.0 per hour during 2000.

For the year ended 31 December, 2000, the amount incurred by the Company for such repair and maintenance services was RMB471,044,000.

- (vi) The China Southern West Australian Flying College Pty Ltd (The "Australian Pilot College"), which is 65% owned by the Company and 35% owned by the SA Group. The 35% shareholding was acquired by the SA Group from a previous shareholder in the Australian Pilot College in 2000.

The SA Group and the Australian Pilot College entered into an agreement dated 7 October, 1993 for the provision of pilot training in Australia to the cadet pilots of the SA Group (the "Training Agreement"). The Training Agreement will remain in force unless terminated by either party upon 90 days' prior written notice to the other party. Pursuant to the Demerger Agreement, the Company has assumed all the interests, rights and obligations of the SA Group under the Training Agreement.

For the year ended 31 December, 2000, the amount paid by the Group to the Australian Pilot College for training services was RMB58,216,000.

- (vii) Southern Airlines (Group) Economic Development Company, which is 61% owned by the SA Group and 39% owned by an independent third party.

The Company and Southern Airlines (Group) Economic Development Company have entered into an agreement dated 22 May, 1997, for the provision of drinks, snacks, liquor, souvenirs and other products for a term extending from 22 May, 1997 to 22 May, 2007.

For the year ended 31 December, 2000, the amount paid by the Group to Southern Airlines (Group) Economic Development Company for the provision of drinks, snacks, liquor, souvenirs and other products was RMB72,054,000.

- (viii) Guangzhou Nanland Air Catering Company Limited ("Nanland"), which is 51% owned by the Company and 49% owned by an independent third party.

The Company and Nanland have entered into a catering agreement dated 22 May, 1999 for the sale and purchase of in-flight meals for flights originating or stopping at the airport in Guangzhou. Pursuant to such agreement, Nanland will supply inflight meals to the Company from time to time during the term from 22 May, 1999 to 22 May, 2000. The agreement has been extended to 22 May, 2001.

For the year ended 31 December, 2000, the amount paid by the Group to Nanland for the provision of in-flight meals was RMB79,891,000.

- (ix) Ticket sales arrangements

The Group has entered into ticket agency agreements for the sale of the Group's air tickets with several subsidiaries of the SA Group (the "Agents"). The Agents charge commission on the basis of the rates stipulated by the CAAC and IATA. The Agents charge a commission in the amount of 3% of the ticket price for domestic tickets and 5% to 12% of the ticket price for Hong Kong regional/international tickets. In addition to the Agents, the Group has other air ticket sales agents in China who charge commission at the same rates. The Agents also act as air ticket sales agents for other Chinese airlines and charge the same rates of commission to such other airlines as those charged to the Group.

For the year ended 31 December, 2000, the aggregate amount of ticket sales of the Group conducted through the Agents was RMB195,069,000.

### **(C) Trademark License Agreement**

The Company and the SA Group have entered into a 10-year Trademark License Agreement dated 22 May, 1997 pursuant to which the SA Group acknowledges that the Company has the right to use the name "China Southern" and "China Southern Airlines" in both Chinese and English, and grants to the Company a renewable royalty-free license to use the kapok logo on a world-wide basis in connection with the Company's airline and airline-related businesses. Unless the SA Group gives written notice of termination three months before the expiration of the agreement, the agreement will be automatically extended for another 10-year term.

### **(D) Leases**

The Company as lessee and the SA Group as lessor have entered into the following lease agreements:

- (i) The Company and the SA Group have entered into a land lease agreement dated 22 May, 1997, in respect of the land used by the Company within Guangzhou Baiyun International Airport. The total rental payment is RMB2,650,700 per year. The term of the lease is five years commencing 1 April, 1997 and is renewable by the parties thereafter (subject to mutual agreement with respect to rental terms).
- (ii) The Company and the SA Group have separately entered into four lease agreements dated 22 May, 1997, in respect of office premises located at the east wing of the Guangzhou Railway Station on Guangzhou Huanshi Dong Road, office premises at Haikou Airport, office premises in Haikou City, and office premises at Tianhe Airport in Wuhan, Hubei Province. The aggregate rental payment under the four leases is RMB12,573,000 per year. The term of each lease is one year and is renewable by the parties thereafter (subject to mutual agreement with respect to rental terms).

- (iii) The Company and the SA Group have entered into an indemnification agreement dated 22 May, 1997 in which the SA Group has agreed to indemnify the Company against any loss or damage caused by or arising from any challenge of, or interference with, the Company's right to use certain land and buildings.

**(E) Comprehensive Services and Employee Benefits**

The Company and the SA Group have entered into a comprehensive services agreement (the "Services Agreement") dated 22 May, 1997. The SA Group shall receive certain fees for providing or causing to be provided to the Group and its employees certain services in relation to employees' housing and welfare benefits for a term extending from 22 May, 1997 to 31 December, 2006.

With respect to employee housing services, the Services Agreement provides that the SA Group shall sell or rent housing to eligible employees of the Group at lower than market price. As the housing is sold or rented below cost and the construction costs of the leased housing were originally paid by the SA Group, the Company shall pay the SA Group RMB85 million per year, payable quarterly in arrears, for a term of ten years from 1995 to 2004.

In September 2000, the PRC Government issued a notice outlining its reformed policies over the provision of employee housing benefits by PRC enterprises. The notice provides that one-off lump sum cash allowances shall be paid to employees who were eligible for quarters as at 31 December, 1998 but are not allocated with to date. The notice further provides that in future, monthly cash allowances shall be paid in replacement of the allocation of staff quarters to new employees and those employees who were not eligible for quarters as at 31 December, 1998. Detailed timetable and procedures for implementing these policies are to be determined by the provincial or municipal governments based on their respective circumstances.

As of the date of this annual report, no detailed timetable and procedures for implementing the above policies have yet been received by the Group in respect of the relevant PRC provinces or municipals in which the Group has substantial operations. The Group anticipates that a revision of its existing Services Agreement with the SA Group will be necessary in order to accommodate with the new housing benefit regulations to be effective in the relevant provinces or municipals. However, based on its preliminary evaluation, the Group does not anticipate that the revision of the Services Agreement with the SA Group will have a significant adverse impact on the Group's results or financial position in the foreseeable future.

In addition, pursuant to the Services Agreement, the SA Group shall provide pension fund services to the Group, and provide medical benefits and certain related services to the Group's staff. As regards pension benefits, the Company has agreed to pay the SA Group:

1. an amount equivalent to 13% to 17% of the annual aggregate wages of the employees of the Group in the previous year as its contribution under several retirement pension schemes organised by the PRC Government, which the SA Group has undertaken to submit to the Social Insurance Bureau of the respective provinces in which the Company operates. The schemes will pay pension benefits to retired employees of the Group. The contribution percentages are fixed by the PRC Government and jointly approved by the relevant labour and finance administrative agencies of the PRC Government. No fee or charge shall be payable by the Company to the SA Group;

