

## Chairman's Statement

Opportunities from industry-wide restructuring being closely explored to gain economies of scale



**Dear shareholders:**

2002 was a very challenging year for the Group. With the assistance of hardworking staff, the Group recorded a traffic volume of over 20 million passengers for the year, and is expected to rank among the world's top 20s in terms of passenger carried. Our air cargo business also reported steady growth in line with our strategic objectives. However, the Group faced tremendous pressure for its operation due to higher insurance premiums subsequent to the 911 incident in U.S., a weak US dollar versus Japanese yen and an increase in landing and take-off fees. Meanwhile, market competition within the domestic airline industry remained highly intense, with lower air fares resulting in a decrease in yield. During the year, the Group imposed stringent cost controls and managed to achieve increases in operating revenue and net profit by 6.7% and 69.2% respectively when compared to last year.

Under the full support and leadership of the PRC government, on 11 October, 2002 Southern Airlines (Group) (the Company's controlling shareholders), China Northern Airlines ("Northern Airlines") and Xinjiang Airlines ("Xinjiang Airlines") restructured and consolidated into a new airline group named as China Southern Air Group after a long period of preparation. On the same date, Southern Airlines (Group) changed its official name to China Southern Air Holding Company ("CSAHC"). Such restructuring and consolidation has provided the Group with new development opportunities. Currently, CSAHC and the Group are preparing for the injection of the airline businesses of Northern Airlines and Xinjiang Airlines into the Group in order to achieve economies of scale and enhance the competitiveness of the core business. Meanwhile, the Group has entered into revenue sharing agreements with Northern Airlines and Xinjiang Airlines on jointly operated routes. Since 1 January, 2003, the three airlines have also started a code sharing arrangement, whereby the flight code of CZ is used for the three airlines' domestic flights. The arrangement is operating smoothly at the moment.



**Yau Zhi Qing**  
Chairman of the Board of Directors

## 8 Chairman's Statement (cont'd)

Meanwhile, the Group invested in Sichuan Airlines Corporation Limited and China Postal Airlines Limited to further expand our market shares in Southwestern China and in the area of postal transportation. Besides, we jointly established Zhuhai Xiang Yi Aviation Technology Company Limited, the first sino-foreign joint venture company engaging in aviation training services in the PRC with CAE of Canada. We also jointly established CSN-ETC E-Commerce Limited, an online passenger ticketing company with an independent network operator to enhance integration of operational standards, and to effectively attract funds and market resources while at the same time saving operating costs.

To cope with the needs of market and routes network expansion, the Group has been continuing to expand its aircraft fleet to maintain sufficient traffic capability to tap market growth and to develop its passenger and cargo businesses. The Group expects to raise capital in the domestic A Share market to finance the acquisitions of aircraft. The Group is pleased to announce that the proposed A share listing in the domestic market has been approved at the shareholders' general meeting at the beginning of 2002. Currently, the project is proceeding at a steady pace. The A share listing, if successfully completed, will not only expand the fund raising channel of the Group, but will also enable it to further strengthen its corporate governance standards.



In 2002, the Group recorded a faster growth in its air freight business, especially in the international cargo sector. We will continue to boost the development of our cargo business. With the completion of the construction and commencement of operation of the Guangzhou new international airport and the potential demand for logistics services in the Pearl River Delta, the Group believes that its air freight business will contribute growth to the Group in real terms in the next few years.

Looking forward, 2003 will be a year of opportunities and challenges for the PRC aviation industry. The intended restructuring among the Group, Northern Airlines and Xinjiang Airlines is expected to provide the Group with opportunities for network expansion and increase in market shares, while the proceeds from the proposed A Shares listing will provide impetus for future development. On the other hand, the volatile situations of the international community, especially in the Middle East, among other factors of instability, will have great impact on the global economy, while high fuel prices will exert great pressure on the operating costs of airlines.

The top priority of our management is to achieve a coherent enterprise development vision after the anticipated group restructuring and consolidation, and to cultivate the vision into a pragmatic and innovative corporate culture. Our objectives are to enhance our overall management quality; to provide the customers with products and services of enhanced safety, efficiency, convenience and comfort; and to achieve economies of scale. This is the goal towards which the Group will strive incessantly.

On behalf of the board, I would like to take this opportunity to express our gratitude to our hardworking management and staff, and to our shareholders for their support to the Group.

**Yan Zhi Qing**  
*Chairman*

Guangzhou, the PRC  
14 March, 2003

