

LOCATED AT THE
GATEWAY OF
THE TROPICAL
PROVINCE,
RIDING ON
THE GROWTH
MOMENTUM OF
THE COUNTRY,
WE ARE ON THE
RIGHT TRACK OF
TAKING OFF.



厦	15:18	24	办票	CZ-3937
	15:20	17	办票	HU-7763
深圳	15:30	30	办票	CJ-6395
桂林	15:30	15	办票	HU-7531
广州	15:50	16	办票	HU-7179
杭州	16:00	29	办票	3Q-4386
	16:20	24	办票	CZ-3507
	16:25	28		MU-372
	16:35	30		CJ-6396
	16:40	15		HU-7127





BeiJing	XiAn	15:05	26	BRD
GuangZhou		15:10	24	MAT
ZhangJiang		15:20	17	CHK
ChangChun	ShenZhen	15:30	30	CHK
ChengDu	GuiLin	15:30	15	CHK
YiMu	GuangZhou	15:50	16	CHK
KunMing		16:00	29	CHK
NanJing	GuangZhou	16:20	24	CHK
WuHan	ShenZhen	16:25	28	
ShenYang	HangZhou	16:35	30	
ChangSha		16:40	15	

MANAGEMENT DISCUSSION AND ANALYSIS



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INDUSTRY REVIEW

Civil Aviation Industry in China

Despite the uncertainty of the global economic environment, China has continued to experience strong economic growth, with GDP growing at a compound annual growth rate of 9.9% between 1991 and 2001. Economic growth and improvement in living standards have brought an increasing demand in businesses, tourism and cargo transportation, from which the aviation industry has benefited the most. Economic liberalisation and rising consumer income have made air travel more frequent and popular. In addition, developments in China's domestic and international tourism, international trade and cultural exchanges are also elements that have contributed to the boost of the civil aviation industry. In 2001, passenger traffic and cargo traffic in China amounted to 109,101,000,000 passenger kilometres and 4,370,000,000 tonne kilometres respectively, representing an increase of 262% and 333% respectively compared to those of 1991. Such statistics show that China is one of the fastest growing countries in the global aviation industry.

China's aviation industry has undergone a restructuring in recent years. In early 2002, the State Council approved an airlines consolidation plan to establish three airline groups led by the three major carriers, namely Air China, China Southern Airlines and China Eastern Airlines. The dominance of China's three major carriers, together with the localisation of control and management of the airport, led to the liberalisation of flight routes reorganisation as well as mergers and acquisitions amongst domestic airports. With the accelerated consolidation of the domestic aviation industry as well as increasing merger opportunities in the airport sector, it is foreseeable that the aviation industry as well as airline business will become more competitive and market-driven.

As early as 2000, Hainan Meilan Airport was chosen as the experimental company for adoption of modern corporate reform of a Chinese civil airport. Meilan Airport underwent major reform in the period from 2000 to 2002 and, as a result Meilan Airport possesses significant advantages compared to other Chinese airports during the industry reform.

Tourism in Hainan Province

Hainan Meilan Airport is located in Haikou City, Hainan Province, and is the main gateway to and from Hainan Island.

Hainan Island is one of the leading tourist destinations in China attracting both domestic and international visitors. In 2001, revenues from the tourism industry amounted to RMB8,800 million, representing a 10.5% increase over 2000.

According to the 2001 statistics provided by the Hainan Provincial Tourism Bureau, the number of person-visits to Hainan Island increased by 11.6% to reach 11.2 million in 2001. During the Chinese New Year, "Golden Week" holidays of Labour Day and National Day, the number of person-visits exceeded 1.37 million, representing an increase of 50.6% over that of 2000. The Hainan Provincial Tourism Bureau forecasts that following the implementation of long-term strategic development programme, Hainan Island will become one of the best tropical tourist destinations in Asia. It projects that there will be around 75 million person-visits to Hainan Island by 2020, generating RMB55 billion in total tourism-related revenues. Hainan Meilan Airport will directly benefit from the anticipated growth as passenger throughput reaches new heights.



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In 2002, more than 12 million person-visits to Hainan Island were recorded, representing a 7.1% increase as compared to that of 2001. Domestic and foreign visitors accounted for 96.89% and 3.11% of the total number of visitors, respectively. It is expected that with Hainan Province's continuous economic growth and increasing importance of Bo'ao City as a domestic and international conference centre, the number of business visitors will continue to grow.

Hainan Island is the nation's largest special economic zone. Exports of agricultural products, seafood, natural gas, jewelry, textiles and natural rubber are the Province's major sources of income. In view of that, there will be an increase not only in passenger throughput, but also in cargo throughput at Meilan Airport.

BUSINESS REVIEW

Aeronautical Business

In 2002, Meilan Airport's aeronautical revenues recorded RMB209.54 million, an increase of 58% over the previous year. Sources of revenue from aeronautical operations include:

- Passenger charges;
- Airport fee;
- Ground handling service fees; and
- Aircraft movement fees and related charges.



During the year under review, the performance of the Group's aeronautical businesses was satisfactory. 50% of civil airport management and construction fee ("Airport fee") (excluding any contributions to the Tourism Development Fund) has been retained as part of ordinary revenues of the Company with effect from 1 January 2002. The retention of Airport fee and the growth in Hainan Meilan Airport's aircraft movements (excluding non-transportation movement of 4,382 in 2001 and 9,614 in 2002) surged by 7% from 49,404 in 2001 and 52,884 in 2002. Passenger throughput rose by 10.2% to 5.6 million, and cargo throughput increased by 3.9% to 76,480 tonnes.

Apart from the number of visitors, cargo throughput also recorded impressive results. This demonstrates that Hainan Island is not only a tourist destination, but also a commercial and trading centre with huge development potential. The increasing traffic volume of Hainan Meilan Airport is a testimony to the success in tourism promotion and economic development of Hainan Province and a tribute to the high quality facilities and services provided and the excellent safety record of Hainan Meilan Airport. Indeed, the safety record of Hainan Meilan Airport is amongst the best in the country and there has not been any serious accident since its operation.

In addition, the Group expects to officially open international routes in 2003 after it obtained the international airport status, which is expected to increase the number of international aircraft movements at Hainan Meilan Airport. As aircraft movement fees and Airport fee paid by departing passengers for international flights are higher than that of domestic flights, revenues from related activities are expected to increase. Moreover, the Group has successfully teamed up with a strategic investor, Copenhagen Airport in late 2002. The management believes that the corporate image, profitability and operating efficiency of the Group will be enhanced by incorporating Copenhagen Airport's extensive management experiences.



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The traffic throughputs for 2002 and 2001 are set out below:

	2002	2001	Change(%)
Aircraft movements	62,498	53,786	16.2
— Domestic	60,839	52,091	16.8
— Hong Kong / Macau	1,471	1,522	(3.4)
— International	188	173	8.7
Passenger throughput (Ten thousand persons)	559.3	507.9	10.1
— Domestic	544	490	11.0
— Hong Kong / Macau	13.7	16.6	(17.5)
— International	1.6	1.3	23.1
Cargo throughput (tonnes)	76,479.8	73,621.7	3.9
— Domestic	74,627.2	71,691.4	4.1
— Hong Kong / Macau	1,548.3	1,681.5	(7.9)
— International	304.3	239.8	26.9

NON-AERONAUTICAL OPERATIONS

During the year, the Company endeavoured to further develop its non-aeronautical businesses. This segment recorded a turnover of RMB73.91 million, representing a growth of 42% compared to that of 2001. Sources of revenue from the Group's non-aeronautical businesses include:

- Leasing of commercial areas, counters and office in the airport terminal;
- Franchise fees from air catering services, air ticket sales, sales of passenger insurance and the operation of the cargo centre;
- Advertising fees;
- Sale of merchandise;
- Provision of tourism services;
- Car parking fees;
- Management fee income; and
- Other revenue.

In May 2002, the Company and the Parent Company underwent an asset swap. As a result, the Group expanded its non-aeronautical businesses, including the operation of tourism services, the franchising of the cargo centre, the sales from



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duty-free and other retail products, as well as the operation of car parking facilities (collectively referred to as the “Acquired Businesses”).

Among the Acquired Businesses, Hainan Meilan Airport Travelling Company Limited (“Meilan Travelling”), which was incorporated at the end of 2001, has achieved outstanding results. Meilan Travelling provides services such as the provision of transportation between Hainan Meilan Airport and Haikou City, hotel reservation, air ticket sales and tour package reservations. Turnover from the relevant business amounted to RMB10.61 million for the period from June to December 2002.

Further, Haikou Meilan Airport Duty-Free Shop Company Limited (“DFG”) also achieved outstanding results which were attributable to the increasing airport passenger spendings during the Chinese New Year, “Golden Week” holidays of Labour Day and National Day. Turnover of DFG amounted to RMB4.41 million from June to December 2002.

Car parking charges is another income source for Meilan Airport’s non-aeronautical businesses. The ground carpark has a site area of 54,183 m², which can accommodate a maximum of 662 vehicles. Additional parking space of 1,440 m², representing 50 parking lots, is also available on the upper (departure) level of the airport terminal. Turnover from car parking was RMB1.47 million for the period from June to December 2002.

The Group also generated revenue by leasing out advertising space at the airport terminal. As of 31 December 2002, income from advertising was RMB5.12 million, representing a growth of approximately 27% compared to that of 2001. As Meilan Airport expects to begin accommodating international flights, more domestic and international corporations will be attracted to place advertisements in the airport terminal. As a result, revenue from this segment is expected to further increase in the future.

SANYA AIRPORT

The Company aims to become a regional airport management company by integrating the international experience of its strategic investor, Copenhagen Airport, and the expertise of Meilan Airport. In August 2002, the Company entered into a management contract with Sanya Phoenix International Airport Company Limited which owns and operates the Sanya Airport in Sanya, Hainan Province, and has been responsible for the day-to-day management of the Sanya Airport which led to a shake up of Sanya Airport’s corporate culture, corporate governance, human resources, organisational structure and operational processes, as well as the transition of the corporate operational mechanism as a whole, all of which proved to be satisfactory. For the year ended 31 December 2002, Sanya Airport recorded aircraft movements of 14,670, passenger throughput of 1,491,558 and cargo throughput of 16,486.5 tonnes, representing an increase of 37%, 51% and 70% over those of the previous year, respectively.



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FINANCIAL REVIEW

Structure of assets

As of 31 December 2002, total assets of the Group amounted to RMB1,744.50 million, an increase of 119% as compared to that of the previous year. The growth was mainly attributable to the increase in shareholder's equity as Meilan Airport's H Shares issuance. The Group's total liabilities amounted to RMB398.60 million, an increase of 2% as compared to that of last year. The main reason for the increase was new short-term commercial loan of RMB50 million from China Development Bank and the Airport fee payable amounting to RMB16.36 million to the central treasury. Total bank borrowings of the Group amounted to RMB314 million, representing an increase of 6%, mainly because the amount of the new loan made during the year exceeded the repayment of the outstanding balance.



Cost Structure

In 2002, total operating costs of the Group were RMB70.41 million, representing an increase of 17% compared to that of last year. The rise in expenses was mainly attributable to the acquisition of DFG and Meilan Travelling in May 2002. Such acquisitions resulted in extra operating expenses of RMB8.40 million for the period from June to December 2002. Administrative expenses were RMB23.80 million, which increased by 85% as compared to that of last year. This increase was a result of a RMB5.31 million payment of a composite services fee to the Parent Company, an incentive bonus of RMB1.47 million paid to the senior management of the Group, and administrative expenses of RMB1.41 million as a result of the acquisition of Meilan Travelling and DFG.

Net finance expenses amounted to RMB18.82 million in 2002, representing an increase of 7% over that of last year. This was mainly due to a short-term loan of RMB20 million borrowed by the Company in December 2001.

Liquidity and Financial Resources

As of 31 December 2002, the Group had net current assets of approximately RMB750.46 million (2001: net current liabilities approximately RMB19.58 million). Current assets of the Group comprise cash and cash equivalents of approximately RMB703.75 million, accounts receivable of approximately RMB24.19 million, amounts due from related parties of approximately RMB129.61 million, inventories of approximately RMB2.30 million, and prepayment, deposits and other receivables of approximately RMB23.70 million.



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As of 31 December 2002, the Group's current liabilities were approximately RMB133.09 million (2001: RMB119.09 million), comprising of a current portion of long-term loans of approximately RMB14 million, a short-term bank loan of approximately RMB50 million, other accrued expenses and other payable totalling approximately RMB42.67 million, Airport fee payable of approximately RMB16.36 million, deposits received of approximately RMB3.94 million, dividends payable of approximately RMB0.67 million, account payable of approximately RMB1.37 million, tax payable approximately RMB0.93 million and amounts due to related parties of approximately RMB3.15 million.

Cashflow

In 2002, the Group's net cash flow from operating activities was RMB85.45 million, representing an increase of 11% from that of the previous year. The primary reason for the increase was the growth of the Group's revenues. During the year, the Group's investment cash outflow was RMB153.40 million, comprising of purchase of property, plant, equipment and land use rights of approximately RMB152.72 million, representing a 13.7 times increase as compared to that of 2001. Other items that contributed to the increase were the purchase of land use rights of RMB94.38 million for the construction of the Phase II expansion of the Hainan Meilan Airport, the acquisition of the Acquired Businesses in May 2002 from the Parent Company and also the construction cost for a new Customs and Inspection Joint Operations Building.

Charge on Group's Assets

As at 31 December 2002, the Group pledged the land use rights as security for a long-term bank loan from China Development Bank as described in Note 13 to the financial statements.

Gearing Ratio

As of 31 December 2002, the Group's gearing ratio, representing the ratio of total debt to total assets, was 18%, a decrease of 19% in comparison with to the gearing ratio of 37% recorded on 31 December 2001. The main reason for the significant improvement was that the Company's shareholders' funds were increased by the issue of H Shares in November 2002.

Exposure to Foreign Exchange Risk

Most of the incomes and expenditures of the Group are denominated in RMB and USD. During the year, the Group had not experienced any material difficulties or negative effects on its operations or liquidity as a result of fluctuations in currency exchange rates. The Directors believe that the Group would have sufficient foreign exchange to meet its foreign exchange requirements.

Employment, Remuneration and Training

As at 31 December 2002, the Group had a total of 481 employees, representing an increase of 130 employees as compared to that of 2001. Total staff costs increased by 27% compared to that of 2001, amounting to about 5% of total turnover. Employees are remunerated based on their performance, experience and prevailing industry practices, their compensation policies and packages are subject to review on a regular basis. Bonuses and commissions may be awarded to employees as incentives based on their performance.



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Purchase, Sales or Redemption of Shares

The Company has not redeemed any of its shares since the Listing on 18 November 2002 up to the date of this report. Neither the Company nor any of its subsidiaries has purchased or sold any of the Company's shares during the period.

Contingent Liability

As at 31 December 2002, the Group or the Company did not have any significant contingent liabilities.

BUSINESS STRATEGY AND OUTLOOK

The data provided by the Hainan Provincial Tourism Bureau shows that there was significant increase in domestic and international visitors coming into Hainan Province during the Chinese New Year holidays in 2003, setting the stage for significant business growth for the year. Meilan Airport expects to continue to benefit from the growing popularity of tourism in Hainan Province in 2003. In addition, attaining an international airport status will lead to an increase in international flight traffic and an increasing influx of international tourists. As the main gateway to Hainan Island, the number of person-visits coming to Hainan Province via Hainan Meilan Airport is expected to increase by approximately 6 million in 2003, as compared to that of 2002. Aircraft movement is expected to reach 65,800 in 2003, and cargo throughput 78,800 tonnes. Meilan Airport will directly benefit from the anticipated rise in the passenger and cargo throughputs.

Expand Operational Facilities

In order to meet the demands from such increasing air traffic volume, Meilan Airport plans to continue to implement its expansion plans in 2003, including the expansion of the airport terminal and the establishment of a new Customs and Inspection Joint Operations Building. In particular, the new Customs and Inspection Joint Operations Building, designed to satisfy the anticipated increase in international routes as a result of attaining the international airport status, is expected to be completed by the end of March 2003, and will commence operation in May 2003. Furthermore, the Group plans to add 20 additional aircraft parking stands and eight air bridges, and also to build a new cargo centre as well as cargo aprons over the next few years.

Increase Non-aeronautical Revenues

The Group is confident that with its solid customer base, satisfactory track record and growth potential of the aeronautical businesses, which are complemented by the expertise brought in by Copenhagen Airport, the profitability of its non-aeronautical businesses will be enhanced. The Group will capitalise on Hainan's status as a major domestic tourist destination to expand its tourist services. It will also seek new franchising opportunities arising from the development in China's retail chain businesses and increase in foreign investments. Further strengthening of the sales of retail and duty-free goods in the airport terminal will be a major goal of the Group. Assisted by the anticipated increase in international air traffic volume, the Company expects to attract more renowned domestic and international consumer brands to place



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advertisements at Hainan Meilan Airport, further increasing revenues in this sector. The Group strongly believes that with an international airport status and increase in international flights, its non-aeronautical businesses will achieve satisfactory performance, paving the way for a balanced development of the Group's businesses.

Increase Operation and Management Efficiencies

To realize the goal of becoming a regional airport management company, Meilan Airport is committed to enhance its cost structure, operation and management efficiencies and service quality. Meilan Airport has achieved outstanding results in respect of cost control. The management believes that the Company's success in cost control can at the same time improve its overall operation efficiency.

Hainan Meilan Airport has maintained a good safety record since its inception, and the Company is confident that this record can be sustained. As air traffics for the airport to increase, Meilan Airport will further strengthen the management efficiency and standard of aircraft movements. With such upgraded standards, Hainan Meilan Airport is committed to provide airline companies with safe and smooth aircraft services, which is in line with Meilan Airport's mission of becoming a successful regional airport management company.

Expand Operating Scales

The Group will actively seek acquisition opportunities with other airports in order to enhance its revenue and profit growth, as well as achieve the economies of scale in planning, purchasing and servicing.

The Group's strategic investor, Copenhagen Airport, is one of the four largest listed airport companies in Europe. Experienced in merger and acquisition activities, Copenhagen Airport manages 13 airports, including the Copenhagen Airport, which has an

annual passenger throughput of over 33 million in total. After investing in Meilan Airport, a member of the senior management of Copenhagen Airport has been appointed to the Board to take part in the daily administration and operation of Meilan Airport. The Group has also entered into a ten-year Technical Services Agreement with Copenhagen Airport Development International A/S ("CADI"). Pursuant to the agreement, CADI will provide Meilan Airport with consultancy services regarding airport capacity and expansion, airport operation and commercial development and to help the Group continuously improve its operations.

As one of the fastest growing local airport companies in China, Meilan Airport will integrate the management experience of Copenhagen Airport, raise the Company's management standards, improve its services and enhance its operations with a view of becoming an optimised regional airport management company.

The Group will progressively implement its development plans using the proceeds raised from its H Shares issued in November 2002. The Group will also carry out its strategy with an emphasis on business growth and to provide a better return to the shareholders.

