NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
At 30 June 2004

1. *Corporate information*

Hainan Meilan International Airport Company Limited (formerly "Hainan Meilan Airport Company Limited" and hereinafter the "Company") is a joint stock company with limited liability incorporated in the People's Republic of China (the "PRC") on 28 December 2000. The Company and its subsidiaries (the "Group") are mainly engaged in the operation of the Meilan Airport in Hainan, the PRC (the "Meilan Airport") and certain ancillary commercial businesses.

During 2002, the Company acquired the equity interests of in Haikou Meilan Airport Duty-Free Shop Limited ("DFG"), Hainan Meilan Airport Travelling Company Limited ("Meilan Travelling") and the carpark operations and cargo handling centre business from Haikou Meilan International Airport Company Limited (the "Parent Company").

On 18 November 2002, 198,000,000 newly issued H Shares of the Company and 3,700,000 existing state-owned shares (after conversion to H shares) were offered, at a premium, to the public and were subsequently traded on The Stock Exchange of Hong Kong Limited. On 9 December 2002, 25,213,000 additional H Shares were issued.

On 31 July 2003, the Civil Aviation Administration of China (the "CAAC") granted the qualification of international airport to the Meilan Airport and it was then eligible to operate international routes. With effect from 25 March 2004, the Company's name was changed from Hainan Meilan Airport Company Limited to Hainan Meilan International Airport Company Limited.

In the opinion of the directors, the ultimate holding company is Haikou Meilan International Airport Company Limited, a company incorporated in the PRC with limited liability.

2. *Summary of significant accounting policies*

The principle accounting policies used in the preparation of the interim financial statements are the same as those used in the annual audited financial statements for the year ended 31 December 2003 and are set out as follows:

Basis of preparation

The consolidated financial statements of the Company have been prepared in Renminbi and in accordance with International Financial Reporting Standards, which comprise standards and interpretations approved by the International Accounting Standards Board, and International Accounting Standards and Standing Interpretations Committee interpretations approved by the International Accounting Standards Committee that remain in effect.

2. *Summary of significant accounting policies* (continued)

Basis of consolidation

The consolidated financial statements have been prepared on a historical cost basis, except for the measurement at fair value of property, plant and equipment and available-for-sale financial assets.

The consolidated financial statements comprise the financial statements of the Company and its subsidiaries for the period ended 30 June 2004 after the elimination of all material intercompany transactions. Subsidiaries are consolidated from the date on which control is transferred to the Group and cease to be consolidated from the date on which control is transferred out of the Group.

Minority interests represent the interests in Hainan Haikou Meilan Airport Advertising Company Limited ("Meilan Advertising"), Meilan Travelling and DFG, not held by the Group.

Subsidiaries

A subsidiary is a company whose financial and operating polices the Company controls, directly or indirectly, so as to obtain benefits from its activities.

The results of subsidiaries are included in the Company's profit and loss account to the extent of dividends received and receivable. The Company's investments in subsidiaries are stated at cost less any impairment losses.

Property, plant and equipment

Property, plant and equipment are stated at cost initially less accumulated depreciation and any impairment in value. The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to the income statement in the period which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of the property, plant and equipment, the expenditure is capitalised as an additional cost of that asset.

2. *Summary of significant accounting policies* (continued)

Property, plant and equipment (continued)

Subsequent to the initial recognition, property, plant and equipment are stated at valuation less accumulated depreciation and any impairment in value. Independent valuations, on a market value basis, or a depreciated replacement cost basis when there is no evidence of market value for such an item, are made with sufficient regularity such that the carrying amount of an asset does not differ materially from that which would be determined had the fixed assets been stated at valuation at the balance sheet date. Increases in valuations of property, plant and equipment are credited to the revaluation reserve. Decreases in valuations of property, plant and equipment are first offset in the revaluation reserve against an increase from earlier valuations in respect of the same asset, and are thereafter with any excess being charged to the income statement. Any subsequent increases are credited to the income statement up to the amount previously charged. When property, plant and equipment are sold or retired, their cost or revalued amounts and accumulated depreciation are eliminated from the accounts financial statements and any gain or loss resulting from their disposal is included in the consolidated income statement. Any revaluation surplus in the revaluation reserve is transferred to retained earnings as a reserve movement on disposal.

As part of the group restructuring and as required by the relevant PRC regulations, a valuation of the property, plant and equipment of the Company was performed as at 31 July 2000 by Hainan Asset Valuation Company, a certified assets appraiser registered under the relevant PRC regulations, in order to determine the fair value of such property, plant and equipment for the purpose of establishing the capital contribution from the Parent Company upon the incorporation of the Company. The result of this valuation was considered as an adjustment to the cost of the property, plant and equipment and the surplus/deficit arising thereon were was credited/charged to the share premium account directly as this was in connection with the change in value of the shareholders' contribution.

Depreciation is calculated on the straight-line basis over the estimated useful life of the assets, after taking into consideration the estimated residual value of 3% of cost or revalued amounts, as follows:

Buildings and leasehold improvements	15-40 years
Machinery and equipment	10-15 years
Motor vehicles	10 years
Office furniture, fixtures and other equipment	6 years

Assets under construction represent buildings and aprons under construction, which is are stated at cost less any impairment losses, and is are not depreciated. Cost comprises the direct costs of construction and capitalised borrowing costs on related borrowed funds during the period of construction. Assets under construction are reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

2. Summary of significant accounting policies (continued)

Negative goodwill

Negative goodwill arising on the acquisition of subsidiaries represents the excess of the Group's share of the fair values of the identifiable assets and liabilities acquired as at the date of acquisition, over the cost of the acquisition.

To the extent that negative goodwill relates to expectations of future losses and expenses that are identified in the acquisition plan and that can be measured reliably, but which do not represent identifiable liabilities as at the date of acquisition, that portion of negative goodwill is recognised as income in the consolidated income statement when the future losses and expenses are recognised.

To the extent that negative goodwill does not relate to identifiable expected future losses and expenses as at the date of acquisition, negative goodwill is recognised in the consolidated income statement on a systematic basis over the remaining average useful life of the acquired depreciable/amortisable assets. The amount of any negative goodwill in excess of the fair values of the acquired non-monetary assets is recognised as income immediately.

On disposal of subsidiaries, the gain or loss on disposal is calculated by reference to the net assets at the date of disposal, including the attributable amount of negative goodwill which has not been recognised in the consolidated income statement and any relevant reserves as appropriate.

Goodwill

Goodwill represents the excess of the cost of the acquisition over the fair value of identifiable net assets of a subsidiary at the date of acquisition. Goodwill is amortised on the straight-line basis over its useful economic life of 10 years. It is reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable. Goodwill is stated at cost less accumulated amortisation and any impairment in value.

2. *Summary of significant accounting policies* (continued)

Land use rights

Land use rights are stated at cost, less accumulated amortisation and any impairment in value, except for the revaluation as noted below in connection with the formation of the Company.

As part of the group restructuring and as required by the relevant PRC regulations, a valuation of the land use rights of the Company was performed as at 31 July 2000 by Hainan Assets Valuation Company Limited a certified assets appraiser registered under the relevant PRC regulations, in order to determine the fair value of such land use rights for the purpose of establishing the capital contribution from the Parent Company upon the incorporation of the Company. The result of this valuation was considered as an adjustment to the cost of the land use rights and the surplus arising thereon was credited to the share premium account directly as this is was in connection with the change in value of the shareholders' contribution.

The land use rights are amortised on the straight-line basis over the unexpired period of the rights. The carrying values of land use rights are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Impairment of assets

An assessment is made at each balance sheet date of whether there is any indication of impairment of any asset, or whether there is any indication that an impairment loss previously recognised for an asset in prior years may no longer exist or may have decreased. If any such indication exists, the asset's recoverable amount is estimated. An asset's recoverable amount is calculated as the higher of the asset's value in use or its net selling price.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. An impairment loss is charged to the income statement in the period in which it arises, unless the asset is carried at a revalued amount, when the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the recoverable amount of an asset, however not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation), had no impairment loss been recognised for the asset in prior years.

A reversal of an impairment loss is credited to the income statement in the period in which it arises, unless the asset is carried at a revalued amount, when the reversal of the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

2. Summary of significant accounting policies (continued)

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, i.e., assets that necessarily take a substantial period of time to prepare for their intended use, are capitalised as a part of the cost of those assets. The capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use. The capitalisation rate for the period is based on the actual cost of the related borrowings.

All other borrowing costs are recognised as expenses in the period in which they are incurred.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on a weighted average basis and comprises mainly the purchase cost. Net realisable value is the estimated selling prices in the ordinary course of business less the estimated costs necessary to make the sale.

Consumables are stated at cost less any impairment losses.

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Group and the revenue can be measured reliably, on the following bases:

(a) airport fees, upon receipt from outbound passengers when departing from the airport;
(b) aeronautical revenues other than airport fees, when the related airport services are rendered;
(c) rental income, on the straight-line basis during the relevant leasing periods;
(d) advertising income, on the straight-line basis during the period of display of the relevant advertisements;
(e) franchise fees, on the straight-line basis during the period of granting the right of operations;
(f) car parking fees, when the parking services are rendered;
(g) management fee income, when the related management services are rendered;
(h) interest income, on a time proportion basis taking into account the principal outstanding and the effective interest rate applicable;
(i) from the sale of goods, when the significant risks and rewards of ownership of the goods have passed to the buyer and the amount of revenue can be measured reliably; and
(j) from the provision of tourism services, when the services are rendered.

2. Summary of significant accounting policies (continued)

Government grants

Government grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. When the grant relates to an expense item, it is recognised as income over the periods necessary to match the grant on a systematic basis to the costs that it is intended to compensate. Where the grant relates to an asset, it is deducted in arriving at the amount of the asset, and is therefore recognised as income on the straight-line basis over the useful life of the asset in the form of a reduced depreciation charge for the asset.

Related parties

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence. Related parties may be individuals or corporate entities.

Operating leases

Leases where the lessor retains substantially all the risks and benefits of ownership of assets are classified as operating leases. Where the Group is the lessor, assets leased by the Group under operating leases are included in property, plant and equipment and rentals receivable under operating leases are credited as income to the income statement on the straight-line basis over the lease terms. Where the Group is the lessee, rentals payable under the operating leases are charged as an expense to the income statement on the straight-line basis over the lease terms.

Foreign currency transactions

The companies now comprising the Group maintain their books and records in Renminbi ("RMB"). Transactions in foreign currencies are recorded at the applicable exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated into RMB at the applicable exchange rates ruling at the balance sheet date. All foreign exchange gains or losses are shown in the income statement.

Cash and cash equivalents

Cash and cash equivalents comprise cash at banks and in hand and short term deposits with an original maturity of three months or less. For the purpose of the consolidated cash flow statement, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts, if any.

2. Summary of significant accounting policies (continued)

Tax

PRC corporate income tax is provided at rates applicable to enterprises in the PRC on the Company's income for financial reporting purposes, as adjusted for income and expense items which are not assessable or deductible for income tax purposes.

Deferred income tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences:

i) except where the deferred income tax liability arises from goodwill amortisation or the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

ii) in respect of taxable temporary differences associated with investments in subsidiaries, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, carryforward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward of unused tax assets and unused tax losses can be utilised:

i) except where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

ii) in respect of deductible temporary differences associated with investments in subsidiaries, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax assets to be utilised.

2. *Summary of significant accounting policies* (continued)

Tax (continued)

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates and tax laws that have been enacted or subsequently enacted at the balance sheet date.

Other tax liabilities are provided in accordance with the regulations issued by PRC government authorities.

Accounts receivable, other receivables and amounts due from related parties

Accounts receivable, which generally have 30-90 days' credit terms, are recognised and carried at the original invoice amount less an allowance for any uncollectible amounts. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off when identified.

Other receivables and amounts due from related parties are recognised and carried at cost less provision for any doubtful amount.

Accounts payable and other payables

Accounts payable and other payables which are normally settled on 30-90 days' credit terms, are carried at cost which is the fair value of the consideration to be paid in the future for goods and services received, whether or not billed to the Group.

Interest-bearing loans and borrowings

All loans and borrowings are initially recognised at cost, being the fair value of the consideration received net of issue costs associated with the borrowing. After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest rate method. Amortised cost is calculated by taking into account any issue costs, and any discount or premium on settlement. Gains and losses are recognised in net profit or loss when the liabilities are derecognised or impaired, as well as through the amortisation process.

2. Summary of significant accounting policies (continued)

Provisions

A provision is recognised when the Group has a present legal or constructive obligation as a result of a past event and it is probable that a future outflow of resources embodying economic benefits will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

Where the Group expects a provision to be reimbursed, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as an interest expense.

Retirement benefits

The Company and its subsidiaries participate in defined contribution retirement benefits plans managed by the local municipal government in the PRC in the locations where they operate. The relevant authorities of the local municipal government in the PRC undertake the retirement obligations of the Group's employees. The Group has no obligation for payment of retirement benefits beyond the annual contributions. The contributions payable are charged as an expense to the income statement as and when incurred.

Contingencies

Contingent liabilities are not recognised in the financial statements. They are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote.

A contingent asset is not recognised in the financial statements but disclosed when an inflow of economic benefits is probable.

Subsequent events

Post balance sheet events that provide additional information about a company's position at the balance sheet date or those that indicate that the going concern assumption is not appropriate (adjusting events) are reflected in the financial statements. Post balance sheet events that are not adjusting events are disclosed in the notes when material.

2. *Summary of significant accounting policies* (continued)

Financial instruments

Financial assets and financial liabilities carried in the balance sheet include cash and cash equivalents, short term investments, accounts receivable and payable, other receivables and payables, loans, and balances with related parties. The accounting policies on recognition and measurement of these items are disclosed in the respective accounting policies included in this section.

Dividends

Final dividends proposed by the Directors are classified as a separate allocation of retained earnings within the capital and reserves section of the balance sheet, until they have been approved by the shareholders in a general meeting. When these dividends are approved by the shareholders and declared, they are recognised as a liability. Interim dividends are simultaneously proposed and declared, because the Company's memorandum and articles grant the Directors the authority to declare interim dividends. Consequently, interim dividends that are proposed or declared after the balance sheet date but before the financial statements are authorised for issue are classified as a separate allocation of retained earnings within the capital and reserves section in the balance sheet, and as a liability when they are proposed and declared.

Investments

All investments are initially recognised at cost, being the fair value of the consideration given and including acquisition charges associated with the investments.

After initial recognition, investments which are classified as held-for-trading and available-for- sale are measured at fair value. Gains or losses on investments held for trading are recognised in income. Gains or losses on available-for-sale investments are recognised as a separate component of equity until the investment is sold, collected of otherwise disposed of, or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in income.

Investments that are intended to be held-to-maturity, such as bonds and reverse repurchase agreements, are subsequently measured at amortised cost using the effective interest rate method. Amortised cost is calculated by taking into account any discount or premium on acquisition, over the period to maturity. For investments carried at amortised cost, gains and losses are recognised in income when the investments are derecognised or impaired, as well as through the amortisation process.

2. Summary of significant accounting policies (continued)

Investments (continued)

For investments that are actively traded in organised financial markets, fair value is determined by reference to stock exchange quoted market bid prices at the close of business on the balance sheet date. For investments where there is no quoted market price, fair value is determined by reference to the current market value of another instrument which is substantially the same or is calculated based on the expected cash flows of the underlying net asset base of the investment.

All regular way purchases or sales of financial assets are recognised on the trade date i.e., the date that the Group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require deliveries of assets within the time frame generally established by regulation or convention in the marketplace.

3. Revenue

(a) The total revenue of the period is analysed as follows:

	Note	Six-month period ended 30 June 2004 RMB'000	Six-month period ended 30 June 2003 RMB'000
Aeronautical:			
Passenger charges		**53,458**	35,563
Airport fees		**46,698**	29,910
Ground handling service fees		**14,213**	8,362
Aircraft movement fees and related charges		**22,674**	16,714
Total aeronautical revenue		**137,043**	90,549
Non-aeronautical:			
Leasing of commercial areas, counters and offices in the terminal		**9,285**	7,979
Franchise fees	(i)	**6,603**	12,123
Sale of goods		**10,970**	4,170
Provision of tourism services		**13,595**	9,889
Provision of advertising services		**4,144**	2,652
Car parking fees		**2,633**	1,463
Management fee income		**–**	1,068
Other revenue		**4,594**	3,332
Total non-aeronautical revenue		**51,824**	42,676
Total revenue		**188,867**	133,225

(i) As disclosed in note 8(a)(i) and (ii) to the financial statements, for the period ended 30 June 2004, the Company recognised franchise fees from Yangzijiang Air Express Company Limited ("Yangzijiang") and Hainan Airlines Food Company Limited ("Hainan Food") amounting to RMB4,500,000 and RMB1,095,000, respectively. The aforesaid revenue amounts were determined by the Directors based on the minimum amount of franchise fees that Yangzijiang and Hainan Food had agreed to pay.

(ii) Pursuant to a bank loan agreement, China Development Bank has a floating charge over the Company's revenue (see note 24).

3. Revenue (continued)

(b) Other income comprises:

	Note	Six-month period ended 30 June 2004 RMB'000	Six-month period ended 30 June 2003 RMB'000
Amortisation of negative goodwill	15	**20**	20
Others		**102**	49
		122	69

4. Profit from operating activities

The Group's profit from operating activities is arrived at after (crediting)/charging:

	Six-month period ended 30 June 2004 RMB'000	Six-month period ended 30 June 2003 RMB'000
Crediting:		
Gross and net rental income	**(9,285)**	(7,979)
Charging:		
Cost of goods and services:		
Composite services fee	**5,257**	4,791
Environmental protection expenses	**700**	565
Cost for provision of tourism services	**4,060**	3,883
Cost of sale of goods	**5,745**	2,232
Others	**2,690**	1,411
	18,452	12,882
Staff costs, including directors' emoluments	**10,395**	12,178
Contributions to the retirement benefits scheme	**1,496**	1,417
Net foreign exchange differences	**7**	72
Depreciation and amortisation	**18,405**	17,444
Minimum lease payments under operating leases:		
Buildings	**255**	255
Auditors' remuneration	**821**	1,276

5. *Directors', senior executives' and supervisors' emoluments*

Details of the remuneration of the directors and supervisors are as follows:

	Six-month period ended 30 June 2004 RMB'000	Six-month period ended 30 June 2003 RMB'000
Fees	**336**	309
Other emoluments:		
Basic salaries, housing benefits, other allowances and benefits in kind	**145**	148
Bonuses	**112**	73
Retirement benefits scheme contributions	**15**	35
	272	256

No directors or supervisors waived or agreed to waive any emoluments during the period ended 30 June 2004.

The five highest paid individuals in the Group during the period ended 30 June 2004 included three directors (for the period ended 30 June 2003: five). The emoluments for these directors are included in the above disclosures. The emoluments paid to the remaining non-director, highest paid individuals during the relevant periods are as follows:

	Six-month period ended 30 June 2004 RMB'000	Six-month period ended 30 June 2003 RMB'000
Basic salaries, housing benefits, other allowances and benefits in kind	**53**	–
Bonuses	**68**	–
Retirement benefits scheme contributions	**11**	–
	132	–

The remuneration of each of the executive directors, supervisors and five highest paid employees during each of the six-month periods ended 30 June 2004 and 2003 fell within the range of nil to HK$1,000,000 (equivalent to RMB1,061,000).

5. *Directors', senior executives' and supervisors' emoluments* (continued)

During each of the six-month periods ended 30 June 2004 and 2003, no emoluments were paid by the Group to the directors, supervisors or any of the five highest paid individuals as an inducement to join or upon joining the Group or as compensation for loss of office.

6. *Interest expenses*

	Six-month period ended 30 June 2004 RMB'000	Six-month period ended 30 June 2003 RMB'000
Interest on bank loans		
– wholly repayable within five years	**3,320**	6,995
– not wholly repayable within five years	**407**	2,083
Interest expenses, net	**3,727**	9,078

7. *Tax*

Hong Kong profits tax has not been provided as the Group had no assessable profits arising in Hong Kong during the period.

Under PRC income tax law, except for certain preferential treatment available to the Company and its subsidiaries ("tax holidays"), entities in the PRC are subject to corporate income tax ("CIT") at a rate of 33% on the taxable income as reported in their statutory financial statements which are prepared in accordance with accounting principles and financial regulations applicable to PRC enterprises.

In accordance with the regulations of "Tax Benefits on Encouraging Investments" issued by the Hainan Provincial Government on 5 August 1988 and "Clarification of Corporate Income Tax Benefit Policy" issued on 15 August 2002, the Company is exempt from CIT for a period of five years commencing from its first profitable year, and is entitled to a preferential income tax rate of 15% for the remaining years of its operation upon which there is a 50% reduction for the five consecutive years commencing from the Company's sixth profitable year. The first profitable year of the Company was the year ended 31 December 2000. The Company therefore was exempt from CIT for each of the six-month periods ended 30 June 2003 and 2004.

In accordance with "Clarification on Corporate Income Tax Benefit Policy", each of the subsidiaries of the Company is subject to a preferential income tax rate of 15%.

7. Tax (continued)

Since Meilan Advertising and DFG had no assessable profits for the six-month period ended 30 June 2004 determined in accordance with the PRC accounting regulations, no CIT was provided.

A reconciliation of income tax expenses applicable to the profit before tax at the statutory income tax rate to income tax expenses at the Group's effective income tax rate for the relevant period is as follows:

	Six-month period ended 30 June 2004 RMB'000	Six-month period ended 30 June 2003 RMB'000
Profit before tax	**101,655**	53,188
At PRC preferential corporate income tax rate of 15%	**15,248**	7,978
Expenditure not allowed for deduction	**1,422**	434
Tax holidays	**(16,642)**	(7,985)
At the Group's effective income tax rate of 0.03% (for the period ended 30 June 2003: 0.8%)	**28**	427

Except for the tax losses of Meilan Advertising and DFG attributable to the Group as at 30 June 2004 of approximately RMB466,000 (as at 31 December 2003: RMB438,000) and RMB1,175,000 (as at 31 December 2003: RMB1,103,000), respectively, there are no other material deductible temporary differences for which deferred tax assets had not been recognised.

Except for the unrecognised deferred tax assets in respect of tax losses carried forward disclosed above, the Group did not have any significant unprovided deferred income tax as at 30 June 2004 (as at 31 December 2003: nil).

The Group is also subject to business taxes on its service revenue at the following rates:

Aeronautical revenue	3%
Non-aeronautical revenue	5%

8. Related party transactions

In addition to such transactions and balances disclosed elsewhere in these financial statements, the Group had the following material transactions with the following related parties:

a) Continuing transactions

Name of related party	Relationship with the Company	Nature of transaction	Notes	Six-month period ended 30 June 2004 RMB'000	Six-month period ended 30 June 2003 RMB'000
Revenues:					
Yangzijiang	Related party	Income from franchise fee for the operation of the cargo centre	(i)	**4,500**	9,000
Hainan Food	Related party	Franchise income from catering services	(ii)	**1,095**	2,190
Hainan Airlines Company Limited ("Hainan Airlines")	*Shareholder	Income for the provision of customary airport ground services	(iii)	**41,893**	27,817
		Rental income for the leasing of office and commercial space	(iv)	**2,920**	2,916
Expenses:					
Parent Company	Immediate holding company Company	Airport composite services charged by the Parent	(v)	**(5,257)**	(4,791)
		Rental expense paid for the leasing of office and commercial space	(vi)	**(255)**	(255)

8. *Related party transactions* (continued)

a) *Continuing transactions* (continued)

Name of related party	Relationship with the Company	Nature of transaction	Notes	Six-month period ended 30 June 2004 RMB'000	Six-month period ended 30 June 2003 RMB'000
HNA Group Company Limited ("HNA Group")	*Shareholder	Logistic composite services charged by HNA Group	(vii)	**(5,352)**	(4,404)
Copenhagen Airport Development International A/S ("CADI")	Related party	Technical services fee expenses	(viii)	**(2,585)**	(4,212)
Sharing of customary airport ground services income:					
Parent Company	Immediate holding company	Sharing of customary airport ground services income by the Parent Company	(ix)	**25,675**	18,457

* A shareho lder represents an individual or corporate entity holding the shares of the Company directly, other than the Parent Company.

Notes:

(i) On 12 August 2002, the Company entered into an agreement with Yangzijiang, a subsidiary of HNA Group, pursuant to which Yangzijiang paid a RMB18,000,000 annual franchise fee to the Company for the operation of the cargo centre with the rights to utilise the facilities of the cargo centre with effect from 1 June 2002. The aforesaid agreement expired on 1 January 2004 and, as at the date of this report, the Company is in the process of negotiating the new contract and franchise fee with Yangzijiang. Pursuant to a letter from Yangzijiang dated 1 September 2004, Yangzijiang agreed to pay the Company an amount not less than 50% of the franchise fee determined under the aforesaid expired agreement. For the period ended 30 June 2004, the Directors considered that it is appropriate to recognise franchise fee revenue to the extent that Yangzijing has agreed to pay, amounting to RMB4,500,000 (note 3).

8. *Related party transactions* (continued)

a) *Continuing transactions* (continued)

(ii) On 31 December 2000, the Company entered into a Catering Service Agreement with Hainan Food, a subsidiary of Hainan Airlines, granting the latter the right to provide on-board catering services to airlines for a term of three years for a franchise fee of RMB4,380,000 per annum. The aforesaid agreement expired on 1 January 2004 and, as at the date of this report, the Company is in the process of negotiating the new contract and franchise fee with Hainan Food. Pursuant to a letter from Hainan Food dated 1 September 2004, Hainan Food agreed to pay the Company an amount not less than 50% of the franchise fee determined under the aforesaid expired agreement. For the period ended 30 June 2004, the Directors considered that it is appropriate to recognise franchise fee revenue to the extent that Hainan Food has agreed to pay, amounting to RMB1,095,000 (note 3).

(iii) The Company provided customary airport ground services including landing facilities, basic ground handling services, cargo storage and handling services, passenger and baggage security check services and other related services to Hainan Airlines and other airlines at rates prescribed by the CAAC.

(iv) The Company leased office, commercial areas, premises, airport counters and an aircraft hangar to Hainan Airlines. The rental charges were agreed between the Company and Hainan Airlines.

(v) According to a Revised Airport Composite Services Agreement dated 25 October 2002, the Parent Company has agreed to provide the following services to the Group:

(a) provision of security guard service;
(b) cleaning and landscaping;
(c) sewage and refuse processing;
(d) power and energy supply and equipment maintenance; and
(e) passenger and luggage security inspection.

The charge rates for the above services are as follows:

- The charges relating to items (a) – (c) above are determined in accordance with the cost to the Parent Company in providing such services plus a 5% mark-up as a management fee. The charges are settled on an annual basis.

- The charges relating to item (d) are determined in accordance with the cost to the Parent Company plus a 25% mark-up pursuant to the relevant pricing guidelines set by the CAAC. The charges are settled on an annual basis.

- The charges relating to item (e) are determined in accordance with the rates prescribed by the CAAC and are charged to the airline customers directly. The Company collects such fees receivable from the airline customers on behalf of the Parent Company.

The term of the Revised Airport Composite Services Agreement is for three years commencing on 1 January 2002 and is renewable upon mutual agreement by the parties thereto.

8. *Related party transactions* (continued)

a) Continuing transactions (continued)

(vi) Pursuant to an Office Lease Agreement dated 25 October 2002, the Company agreed to rent from the Parent Company office premises for a term of five years at an annual rental of RMB509,000 with effect from 1 January 2002.

(vii) Pursuant to a Logistic Composite Service Agreement dated 25 October 2002, HNA Group agreed to provide and procure its subsidiaries to provide to the Company logistic services including (a) staff training; (b) staff shuttle bus services; (c) staff cafeteria services; (d) vehicle maintenance; and (e) appliance procurement with effect from 1 January 2002.

The charges for these services are determined as follows: item (a), the cost of providing such services, which is shared between HNA Group, the Company and other relevant companies on a pro rata basis by reference to employee headcount; items (b) and (c) at a fixed price with reference to the relevant cost per employee headcount; and items (d) and (e) at the cost of providing such services plus a 5% and a 1% mark-up as management fees, respectively.

(viii) Pursuant to a Technical Service Agreement dated 16 September 2002 and amended on 30 October 2002 between the Company and CADI, a wholly-owned subsidiary of the Company's strategic investor – Copenhagen Airport A/S, CADI has agreed to provide certain technical and consultancy services in respect of the long-term management and development of Meilan Airport.

The Company is required to pay fees to CADI which consist of a fixed fee component and a performance-related component. The fixed fee component is calculated by reference to the number of days used in providing technical and consultancy services. The performance-related component is calculated by reference to the Company's actual earnings before interest, tax, depreciation and amortisation.

(ix) The runway at the Meilan Airport is owned and operated by the Parent Company. By an agreement between the Company dated 25 October 2002 and the Parent Company, the Company has agreed to share with the Parent Company on such a ratio as the CAAC or any other regulatory authorities may from time to time prescribe, which as at the date of the agreement is in the ratio of 75% to the Company and 25% to the Parent Company, the aircraft movement fees for all airlines, passenger charges for domestic airlines and the basic ground handling fees for Hong Kong, Macau and foreign airlines for the runway services provided by Parent Company. The Company will collect such fees on behalf of the Parent Company and assumes no liabilities in respect of a default of payment by the airline customers.

8. *Related party transactions* (continued)

*b) Discontinued transactions**

(i) The Company's Parent Company has guaranteed related party balances due to the Group which amount to RMB8,230,000 (2003: RMB13,230,000) and RMB105,441,000 (2003: Nil) respectively, as further detailed in note 20(i) and 20(ii) to the financial statements.

(ii) During the period ended 30 June 2004, Hainan Airlines obtained control over the management of Sanya Phoenix International Airport Company Limited ("SPIA") and, as a result, SPIA became a related company of the Company.

In August 2002, the Company entered into a management contract with SPIA to manage Sanya Airport with management fees set at 1.5% of revenue plus 5% of the reduction in net losses when SPIA remains loss making or 10% of the profit before tax when SPIA starts to generate net profits. During 2004, the two parties agreed to rescind the aforesaid agreement with effect from 1 January 2004.

* Discontinued transactions represent one-off transactions not expected to recur.

9. *Proposed interim dividend*

	Six-month period ended 30 June 2004 RMB'000	Six-month period ended 30 June 2003 RMB'000
Proposed interim – RMB 10.4 cents (for the period ended 30 June 2003: RMB 2.7 cents) per share	**49,214**	12,777

Interim dividends are simultaneously proposed and declared, because the Company's memorandum and articles grant the Directors the authority to declare interim dividends. Interim dividends that are proposed or declared after the balance sheet date but before the financial statements are authorised for issue are classified as a separate allocation of retained earnings within the capital and reserves section in the balance sheet.

10. Earnings per share

The calculation of earnings per share is based on the Group's profit attributable to shareholders for the period ended 30 June 2004 of RMB101,630,000 (for the period ended 30 June 2003: RMB51,800,000) and 473,213,000 shares (for the period ended 30 June 2003: 473,213,000 shares) of the Company in issue during the period ended 30 June 2004.

No diluted earnings per share amount is presented as the Company did not have any dilutive potential ordinary shares.

11. Retirement benefits plans

The Company and its subsidiaries are required to participate in employee retirement benefits plans operated by the relevant local government authorities in the PRC. The PRC government is responsible for the retirement obligations to these retired employees. The Group is required to make contributions for employees who are registered as permanent residents in the PRC at a rate of 18% of the employees salaries.

The Group's retirement benefits contributions for the period ended 30 June 2004 amounting to approximately RMB1,496,000 (for the period ended 30 June 2003: RMB1,417,000).

12. Property, plant and equipment, net

Group

	Assets under construction RMB'000	Buildings and leasehold improvements RMB'000	Machinery and equipment RMB'000	Motor vehicles RMB'000	Office furniture, fixtures and other equipment RMB'000	Total RMB'000
Cost or valuation:						
At 1 January 2004	771	624,968	77,871	39,364	17,142	760,116
Additions	42,388	218	1,151	642	2,026	46,425
Disposals	–	–	–	–	(8)	(8)
At 30 June 2004	43,159	625,186	79,022	40,006	19,160	806,533
Analysis of cost or valuation:						
At cost	43,159	64,186	1,302	3,262	9,804	121,713
At 31 August 2002 valuation	–	561,000	77,720	36,744	9,356	684,820
	43,159	625,186	79,022	40,006	19,160	806,533
Accumulated depreciation:						
At 1 January 2004	–	19,519	9,508	7,892	5,733	42,652
Charge for the period	–	8,103	3,540	3,102	1,795	16,540
Disposals	–	–	–	–	(7)	(7)
At 30 June 2004	–	27,622	13,048	10,994	7,521	59,185
Net book value:						
At 30 June 2004	43,159	597,564	65,974	29,012	11,639	747,348
At 1 January 2004	771	605,449	68,363	31,472	11,409	717,464

Had the property, plant and equipment of the Group been carried at historical cost less accumulated depreciation, the carrying amounts of each class would have been:

	Assets under construction RMB'000	Buildings and leasehold improvements RMB'000	Machinery and equipment RMB'000	Motor vehicles RMB'000	Office furniture, fixtures and other equipment RMB'000	Total RMB'000
Cost	43,159	664,161	99,698	51,256	23,697	881,971
Accumulated depreciation	–	100,413	37,317	23,330	11,653	172,713
	43,159	563,748	62,381	27,926	12,044	709,258

12. Property, plant and equipment, net (continued)

Group (continued)

During 2002, the Company received a government grant of RMB4,000,000 in cash in connection with the construction of the customs and inspection complex building of Meilan Airport. The Group and the Company has recorded the aforesaid government grant as a credit to the balance of the buildings and leasehold improvements, and will recognise the grant as income over the life of the relevant asset of 40 years from 1 January 2004.

Company

	Assets under construction RMB'000	Buildings and leasehold improvements RMB'000	Machinery and equipment RMB'000	Motor vehicles RMB'000	Office furniture, fixtures and other equipment RMB'000	Total RMB'000
Cost or valuation:						
At 1 January 2004	745	624,968	77,871	38,849	12,738	755,171
Additions	42,414	218	1,151	642	1,962	46,387
Disposals	–	–	–	–	(8)	(8)
At 30 June 2004	43,159	625,186	79,022	39,491	14,692	801,550
Analysis of cost or valuation:						
At cost	43,159	64,186	1,301	2,747	5,336	116,729
At 31 August 2002 valuation	–	561,000	77,721	36,744	9,356	684,821
	43,159	625,186	79,022	39,491	14,692	801,550
Accumulated depreciation:						
At 1 January 2004	–	19,519	9,508	7,738	3,553	40,318
Charge for the period	–	8,103	3,540	3,075	1,426	16,144
Disposals	–	–	–	–	(7)	(7)
At 30 June 2004	–	27,622	13,048	10,813	4,972	56,455
Net book value:						
At 30 June 2004	43,159	597,564	65,974	28,678	9,720	745,095
At 1 January 2004	745	605,449	68,363	31,111	9,185	714,853

12. Property, plant and equipment, net (continued)

Company (continued)

Had the property, plant and equipment of the Company been carried at historical cost less accumulated depreciation, the carrying amounts of each class would have been:

	Assets under construction RMB'000	Buildings and leasehold improvements RMB'000	Machinery and equipment RMB'000	Motor vehicles RMB'000	Office furniture, fixtures and other equipment RMB'000	Total RMB'000
Cost	43,159	664,161	99,698	50,741	19,229	876,988
Accumulated depreciation	–	100,413	37,317	23,149	9,104	169,983
	43,159	563,748	62,381	27,592	10,125	707,005

A valuation of the property, plant and equipment of the Group was performed as at 31 August 2002 by Vigers Hong Kong Limited, independent professionally qualified surveyors, for the purpose of the listing of the H shares of the Company on The Stock Exchange of Hong Kong Limited. Except for the valuation of property which was based on a combination of the open market value and depreciated replacement cost, the valuation of the remaining plant and equipment was based on the open market method. The depreciated replacement cost approach considers the cost to reproduce or replace in new condition the property appraised, in accordance with current construction costs for similar property in the locality, less depreciation whether arising from physical, functional or economic causes. The valuer assumed that the buildings and assets under construction will be used for the purposes for which they are presently used and did not consider alternative uses. A net valuation surplus of approximately RMB41,449,000 resulted from the revaluation and was recorded in the Group's financial statements.

In the opinion of directors, there has been no material change to the values of the property, plant and equipment between 31 August 2002 and 30 June 2004.

All buildings of the Group are held outside Hong Kong with lease terms of 50 years.

13. Land use rights

Group and Company

	RMB'000
Cost:	
At 1 January 2004 and 30 June 2004	175,260
Accumulated amortization:	
At 1 January 2004	6,959
Charge for the period	1,865
At 30 June 2004	8,824
Net book value:	
At 30 June 2004	166,436
At 1 January 2004	168,301

The land use rights are amortised on the straight-line basis over the term of 50 years.

14. Interests in subsidiaries

	30 June 2004 RMB'000	31 December 2003 RMB'000
Unlisted shares, at cost	**18,094**	18,094
Amount due from/(to) subsidiaries	**15,128**	(2,419)
	33,222	15,675

The amounts due from/to subsidiaries are unsecured, non-interest bearing and payable on demand.

The consolidated financial statements include the financial statements of the Company and its subsidiaries listed in the following table.

14. Interests in subsidiaries (continued)

As at 30 June 2004, the Company had direct and indirect interests in the following subsidiaries:

Name	Place and date of incorporation and operations	Nominal value of paid-up share/ registered capital RMB'000	Percentage of equity interest attributable to the Group	Principal activities
Meilan Advertising* (note (i))	PRC 8 June 1999	1,000	99.75	Provision of advertising services
Meilan Travelling* (note (ii))	PRC 13 November 2001	11,000	95	Provision of tourism services
DFG* (note (ii))	PRC 11 May 1999	1,000	95	Trading of duty-free items

* Each of the subsidiaries is registered as a company with limited liability in the PRC.

Notes:

(i) 95% of the equity interest of Meilan Advertising is directly held by the Company while the remaining 4.75% equity interest of Meilan Advertising attributable to the Group is indirectly held by the Company via DFG.

(ii) The equity interests in Meilan Travelling and DFG are directly held by the Company.

15. Goodwill and negative goodwill

The amounts of goodwill and negative goodwill, capitalised as an asset and recognised in the consolidated balance sheet, arising from the acquisition of subsidiaries are as follows:

Group	Goodwill RMB'000	Negative goodwill RMB'000	Total RMB'000
Cost:			
At 1 January 2004 and 30 June 2004	4,132	(260)	3,872
Accumulated amortisation:			
At 1 January 2004	(69)	58	(11)
Charge for the period	(207)	20	(187)
At 30 June 2004	(276)	78	(198)
Net book value:			
At 30 June 2004	3,856	(182)	3,674
At 1 January 2004	4,063	(202)	3,861

16. Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and in hand and short term bank deposits. Cash at bank earns interest at floating rates based on daily bank deposit rates. Short term deposits are made for varying periods of between seven days and three months depending on the immediate cash requirements of the Group, and earn interest at the respective short term deposit rates.

For the purpose of the consolidated cash flow statement, the cash and cash equivalents of the Group comprise the following:

	30 June 2004 RMB'000	31 December 2003 RMB'000
Cash at bank and in hand	**426,828**	213,704
Short term bank deposits	**–**	200,000
	426,828	413,704

Cash and cash equivalents of the Company comprise the following:

	30 June 2004 RMB'000	31 December 2003 RMB'000
Cash at bank and in hand	**397,856**	201,930
Short term bank deposits	**–**	200,000
	397,856	401,930

17. Time deposits

As at 30 June 2004 and 31 December 2003, the Group and the Company had two deposits placed with Xiamen International Bank amounting to RMB50,000,000 and RMB30,000,000, respectively. In addition, as at 30 June 2004, the Group and the Company had a deposit with China Merchants Bank amounting to RMB20,000,000. The aforesaid deposits earn interest at 1.98% per annum and have maturity dates of 25 September 2004, 13 October 2004 and 22 April 2005, respectively.

18. Accounts receivable, net

Group

	30 June 2004 RMB'000	31 December 2003 RMB'000
Outstanding balances aged:		
Within 90 days	**32,604**	38,664
Between 91 to 180 days	**12,445**	4,076
Between 181 to 365 days	**1,784**	1,999
More than 365 days	**2,902**	3,191
	49,735	47,930
Less: Provision for doubtful debts	**(4,395)**	(4,391)
	45,340	43,539

Company

	30 June 2004 RMB'000	31 December 2003 RMB'000
Outstanding balances aged:		
Within 90 days	**32,464**	38,257
Between 91 to 180 days	**12,435**	3,914
Between 181 to 365 days	**1,458**	1,940
More than 365 days	**2,621**	3,040
	48,978	47,151
Less: Provision for doubtful debts	**(4,319)**	(4,319)
	44,659	42,832

The Group normally allows a credit period of not more than 90 days to its customers, although an extension of the credit period is not uncommon for customers with a long term relationship with the Group. The Group closely monitors overdue balances. A specific provision for doubtful debts is made when it is considered that amounts due may not be recovered.

19. Inventories

Group

	30 June 2004 RMB'000	31 December 2003 RMB'000
Finished goods and consumables	**3,487**	2,853

Company

	30 June 2004 RMB'000	31 December 2003 RMB'000
Consumables	**34**	28

All the carrying amounts were stated at cost.

20. Balances with related parties

Due from:

Group	Notes	30 June 2004 RMB'000	31 December 2003 RMB'000
Parent Company		**1,764**	1,654
HNA Group Company Limited		**–**	309
Hainan Da Lung Enterprise Company Limited	(i)	**8,230**	13,230
Hainan Airlines	(ii)	**105,441**	49,752
Hainan Food		**1,578**	3,493
Yangzijiang		**1,714**	12,565
SPIA		**2,472**	–
Others		**172**	311
		121,371	81,314
Outstanding balances aged:			
Within 90 days		**30,275**	28,615
Between 91 to 180 days		**30,180**	26,625
Between 181 to 365 days		**51,032**	12,844
More than 365 days		**9,884**	13,230
		121,371	81,314

20. Balances with related parties (continued)

Company	Notes	30 June 2004 RMB'000	31 December 2003 RMB'000
Parent Company		**110**	–
HNA Group Company Limited		**–**	309
Hainan Da Lung Enterprise Company Limited	(i)	**8,230**	13,230
Hainan Airlines	(ii)	**105,441**	49,752
Hainan Food		**1,578**	3,493
Yangzijiang		**1,714**	12,565
SPIA		**2,472**	–
Others		**88**	212
		119,633	79,561
Outstanding balances aged:			
Within 90 days		**30,191**	28,516
Between 91 to 180 days		**30,180**	26,625
Between 181 to 365 days		**51,032**	11,190
More than 365 days	(i)	**8,230**	13,230
		119,633	79,561

20. Balances with related parties (continued)

Due to:

Group	30 June 2004 RMB'000	31 December 2003 RMB'000
Parent Company	**11,115**	7,341
Hainan Airlines	**724**	–
HNA Group Company Limited	**461**	–
CADI	**6,509**	4,146
Others	**50**	203
	18,859	11,690
Outstanding balances aged:		
Within 90 days	**4,567**	6,173
Between 91 to 180 days	**10,147**	–
Between 181 to 365 days	**4,145**	5,517
	18,859	11,690

Company	30 June 2004 RMB'000	31 December 2003 RMB'000
Parent Company	**10,234**	6,463
Hainan Airlines	**724**	–
HNA Group Company Limited	**461**	–
CADI	**6,509**	4,146
Others	**52**	201
	17,980	10,810
Outstanding balances aged:		
Within 90 days	**3,687**	5,293
Between 91 to 180 days	**10,147**	–
Between 181 to 365 days	**4,146**	5,517
	17,980	10,810

20. Balances with related parties (continued)

Notes:

(i) On 10 December 2002, the Company entered into a procurement agreement of RMB20,000,000 with Hainan Da Lung Enterprise Company Limited, a subsidiary of the Parent Company, under which Hainan Da Lung Enterprise Company Limited would purchase equipment for the apron of Meilan Airport on behalf of the Company. The Company made full payment to Hainan Da Lung Enterprise Company Limited in December 2002 in accordance with the contract terms. The balance is guaranteed by the Parent Company. During the period ended 30 June 2004, Hainan Da Lung Enterprise Company Limited paid an amount of RMB5,000,000 on behalf on the Company.

(ii) The amount due from Hainan Airlines Company Limited as at 30 June 2004 of approximately RMB105,441,000 included an amount of RMB78,716,000 which was overdue as at that date. This overdue amount is unsecured and interest-free. On 17 August 2004, Hainan Airlines agreed to fully settle the outstanding balance as at 30 June 2004 before 30 November 2004 and such repayment is guaranteed by the Parent Company. On 19 August 2004, Hainan Airlines settled part of the outstanding balance amounting to approximately RMB30,000,000.

(iii) The amounts due from/to related parties are unsecured, non-interest-bearing and repayable in accordance with the contract terms. The balances primarily arose from the related party transactions disclosed in note 8 to the financial statements. The Directors believe that the related party transactions have been entered into in accordance with the terms of the agreements governing the transactions except for the extension of credit periods and the waiver of penalty interest that the Company was otherwise entitled to charge under certain governing agreements. The Directors considered that the extension of credit period and the waiver of penalty interest arose in the ordinary course of business of the Company and was consistent with the manner in which all customers who have a long term relationship with the Company are treated.

21. Accounts payable

Group

	30 June 2004 RMB'000	31 December 2003 RMB'000
Outstanding balances aged:		
Within 90 days	**1,777**	1,833
Over 90 days	**865**	392
	2,642	2,225

22. Airport fee payable

Airport fee payable represents the proportion of the Civil Airport Management and Construction Fee collected by the Company, which is payable to the CAAC.

23. Accrued liabilities and other payables

Included in the balance of accrued liabilities and other payables as at 30 June 2004 was a payable due to the National Social Security Fund amounting to approximately RMB14,838,000 (as at 31 December 2003: RMB RMB14,838,000). The aforesaid balance represented net proceeds arising from the sale of 3,700,000 H Shares of the Company during the Company's public offering of its H shares in 2002.

Pursuant to the Temporary Administration Measures on the Reduction of State-Owned Shares for the Raising of Social Security Fund promulgated by the State Council on 12 June 2001, holders of state-owned shares of a joint stock limited company (including companies listed overseas) in which the state owns shares, shall offer for sale its state-owned shares in the amount equivalent to 10% of the funds to be raised. Accordingly, an aggregate of 3,700,000 H Shares of the Company were offered for sale at the offering price and the net proceeds amounting to RMB14,838,000 received by the Company is payable to the National Social Security Fund.

24. Interest-bearing loans and borrowings

Group and Company

	30 June 2004 RMB'000	31 December 2003 RMB'000
Within one year	**–**	–
Between one and two years	**50,000**	25,000
Between two and five years	**64,000**	87,000
Over five years	**14,000**	16,000
Total long term bank loans	**128,000**	128,000
Less: Amounts due within one year included in current liabilities	**–**	–
	128,000	128,000

The Group's and the Company's long term bank loan outstanding at 30 June 2004 is secured by a floating charge over the Company's revenue (see note 3) and bear interest at 5.76% per annum.

25. Deferred income tax liabilities

As at 30 June 2004 and 31 December 2003, the Group and the Company recognised a deferred tax liability arising from the cost adjustment in 2000 relating to the appraised value of the land use rights of the Group and the Company which was in excess of the net carrying value. The valuation of the land use rights on which the appraised value was determined was performed by Hainan Asset Valuation Company Limited and resulted in a non-tax-deductible surplus of approximately RMB48,869,000. The Company has a five-year exemption from CIT from 2000 to 2004 and a preferential income tax rate of 7.5% from 2005 to 2009. The deferred tax liability of RMB6,535,000 relating to this temporary difference has been recorded since 2000, after taking into account the impact of the preferential tax scheme, with a corresponding adjustment to the share premium that was recorded to reflect the cost adjustment in respect of the assets contributed by the Parent Company.

During the second half of 2002, the Group and the Company also recognised a deferred tax liability of approximately RMB4,968,000 arising from a non-tax-deductible valuation surplus of approximately RMB41,449,000 on the property, plant and equipment of the Group and the Company. Details of the asset appraisal are disclosed in note 12 to these financial statements.

26. Share capital

	30 June 2004 RMB'000	31 December 2003 RMB'000
Issued and fully paid:		
– 246,300,000 domestic shares of RMB1 each	**246,300**	246,300
– 226,913,000 H shares of RMB1 each	**226,913**	226,913
	473,213	473,213

27. Reserves

The movements in the reserves of the Group are set out in the consolidated statement of movements in equity on page 17 of the financial statements.

Company

	Note	Share premium account RMB'000	Revaluation reserve RMB'000	Statutory reserves RMB'000	Retained earnings RMB'000	Proposed dividend RMB'000	Total RMB'000
At 1 January 2003		627,037	36,481	32,464	81,619	85,650	863,251
Dividend paid		–	–	–	–	(85,650)	(85,650)
Net profit for the period (note i)		–	–	–	53,057	–	53,057
Proposed interim dividend	9	–	–	–	(12,777)	12,777	–
At 30 June 2003		627,037	36,481	32,464	121,899	12,777	830,658
Net profit for the period		–	–	–	104,446	–	104,446
Interim dividend paid		–	–	–	–	(12,777)	(12,777)
Proposed final dividend		–	–	–	(67,669)	67,669	–
Transfer to statutory reserves		–	–	20,160	(20,160)	–	–
At 31 December 2003		627,037	36,481	52,624	138,516	67,669	922,327
Dividend paid		–	–	–	–	(57,522)	(57,522)
Transfer to dividend payable		–	–	–	–	(10,147)	(10,147)
Net profit for the period (note i)		–	–	–	101,878	–	101,878
Proposed interim dividend	9	–	–	–	(49,214)	49,214	–
At 30 June 2004		627,037	36,481	52,624	191,180	49,214	956,536

Note:

(i) The net profit from ordinary activities attributable to shareholders for the period ended 30 June 2004 dealt with in the financial statements of the Company was RMB101,878,000 (for the period ended 30 June 2003: RMB53,057,000).

27. Reserves (continued)

In accordance with the relevant PRC regulations, the companies now comprising the Group are required to transfer 10% of the year end profit after tax, as determined under the PRC accounting regulations, to the statutory common reserve, until the balance of the fund reaches 50% of the registered capital of that company. Subject to certain restrictions as set out in the relevant PRC regulations, the statutory common reserve may be used to offset against the accumulated losses, if any. Pursuant to the PRC regulations, the companies are also required to transfer 5% to 10% of net profit, as determined under the PRC accounting regulations, to the statutory common welfare fund. This fund can only be used to provide staff welfare facilities and other collective benefits to the employees of that company. This fund is non-distributable other than in liquidation. Appropriations to the statutory common reserve and statutory common welfare fund are not required for the interim period ended 30 June 2004.

According to the articles of association of the Company, the amount of reserves available for distribution is the lower of the amount determined under PRC accounting regulations and the amount determined under International Financial Reporting Standards. As at 30 June 2004, the amount of reserves available for distribution as determined under PRC accounting regulations was approximately RMB182,696,000 (at 31 December 2003: RMB134,602,000).

28. Notes to the consolidated cash flow statement

Major non-cash transactions

As further disclosed in note 20(i) to the financial statements, during the period ended 30 June 2004, Hainan Da Lung Enterprise Company Limited settled construction cost payables on behalf of the Company amounting to RMB5,000,000.

29. Segment information

The Group conducts its business within one business segment, i.e., the business of operating an airport and the provision of related services in the PRC. The Group's chief decision-maker for operations is considered to be the Group's general manager. The information reviewed by the general manager is prepared on a similar basis to the information presented in the consolidated income statement. No segment consolidated income statement has been prepared by the Group during the period. The Group also operates within one geographical segment because its revenues are primarily generated in the PRC and its assets are located in the PRC. Accordingly, no further geographical segment data is presented.

30. Commitments and contingencies

Operating lease arrangements – as lessee

The total future minimum lease payments under non-cancellable operating leases in respect of buildings were as follows:

Group and Company

	30 June 2004 RMB'000	31 December 2003 RMB'000
Within one year	**649**	910
In the second to fifth years, inclusive	**764**	1,019
	1,413	1,929

Operating lease arrangements – as lessor

The total future minimum lease receivables under non-cancellable operating leases with the Group's tenants are as follows:

	30 June 2004		31 December 2003	
	Group RMB'000	Company RMB'000	Group RMB'000	Company RMB'000
Within one year	**14,142**	**10,150**	9,293	6,593
In the second to fifth years, inclusive	**832**	**641**	1,494	1,397
	14,974	**10,791**	10,787	7,990

30. Commitments and contingencies (continued)

Capital commitments

Group and Company

	30 June 2004 RMB'000	31 December 2003 RMB'000
Contracted, but not provided for:		
In respect of buildings and leasehold improvements	**122,002**	–
In respect of motor vehicles	**3,520**	3,520
	125,522	3,520
Authorised, but not contracted for:		
In respect of buildings and leasehold improvements	**263,787**	434,015
	389,309	437,535

Contingent liabilities

As at 30 June 2004, the Group and the Company did not have any significant contingent liabilities.

31. Fair values of financial instruments

As at 30 June 2004, the Group's financial instruments comprise bank loans, cash and bank deposits. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial instruments such as accounts receivable, amounts due from and due to related parties, other receivables, accounts payable and other payables which arise directly from its operations.

The carrying amounts of the Group's financial instruments approximated their fair value as at 30 June 2004 because of the short term maturities of these instruments, except for the long term borrowings.

The carrying amount of the long term borrowings approximated their fair value based on current borrowing rates for loans with similar terms and maturities.

The Company's risk management objectives and policies are summarised in note 32 to the financial statements.

32. Financial risk factors

The Group does not have written risk management policies and guidelines. However, the board of Directors meets periodically to analyse and formulate measures to manage the Group's exposure to risks, including principally market risks and changes in interest rates and currency exchange rates. Generally, the Group follows conservative strategies in its risk management.

As the Group does not have significant exposure to interest rate and currency exchange rate risk, the Group has not used derivatives or other instruments for hedging purposes. The Group does not hold or issue derivative financial instruments for trading purposes.

The main risks arising from the Group's financial instruments are business risk, interest rate risk, foreign currency risk and credit risk, which are set out as follows:

(i) Business risk

The Group conducts its operations in the PRC and accordingly is subject to special considerations and significant risk. These include risks associated with, among others, the political, economic and legal environment, the influence of national authorities over pricing regulations and competition in the industry.

Furthermore, the Group's five largest customers represented in aggregate approximately 41% (for the period ended 30 June 2003: 60%) of the aeronautical revenue of the Group for the period ended 30 June 2004.

(ii) Interest rate risk

The interest rate and repayment terms of the bank loans of the Group are disclosed in note 24.

(iii) Foreign currency risk

The Group's businesses are principally conducted in RMB, except for the purchase of certain equipment, goods and materials in United States dollars. As at 30 June 2004, all of the Group's assets and liabilities were denominated in RMB except that cash and cash equivalents of approximately RMB8,803,000 (at 31 December 2003: RMB9,627,000) were denominated in Hong Kong dollars. Fluctuation of the exchange rates of RMB against foreign currencies could affect the Group's results of operations.

32. Financial risk factors (continued)

(iv) Credit risk

The carrying amounts of cash and cash equivalents, time deposits and accounts receivable included in the consolidated financial statements represent the Group's maximum exposure to credit risk in relation to its financial assets. No other financial assets carry a significant exposure to credit risk.

33. Events after the balance sheet date

On 22 September 2004, the board of directors of the Company proposed a 2004 interim dividend of approximately RMB10.4 cents per share, totalling approximately RMB49,214,000. Interim dividends are simultaneously proposed and declared, because the Company's memorandum and articles grant the Directors authority to declare interim dividends.

34. Approval of the financial statements

The financial statements were approved and authorised for issue by the board of directors on 22 September 2004.