

MANAGEMENT DISCUSSION AND ANALYSIS

CONTINUOUS GROWTH OF AIR TRAFFIC VOLUMES

In 2006, the air traffic volumes at the Beijing Airport maintain continuous rapid growth, details of which are set out as follows:

	2006	2005	Change %
Aircraft Movements	376,643	341,681	10.2
Domestic	288,491	265,052	8.8
International, Hong Kong & Macau	88,152	76,629	15.0
Passenger Throughput	48,654,770	41,004,008	18.7
Domestic	37,534,671	31,605,028	18.8
International, Hong Kong & Macau	11,120,099	9,398,980	18.3
Freight Throughput (tonnes)	1,028,909	782,066	31.6
Domestic	642,817	528,623	21.6
International, Hong Kong & Macau	386,092	253,443	52.3

OVERVIEW OF THE AERONAUTICAL BUSINESS

For the year ended 31 December 2006, benefiting from the continuous growth of the air traffic volumes, the aeronautical revenues of the Company were Rmb2,296,099,000, representing an increase of 12.2% over the year of 2005, details of which are set out as follows:

	2006 <i>Rmb'000</i>	2005 <i>Rmb'000</i>	change %
Passenger charges	733,406	658,237	11.4
Aircraft movement fees and related charges	897,877	804,858	11.6
Airport fee	664,816	583,174	14.0
Total aeronautical revenues	2,296,099	2,046,269	12.2
Less: business tax and levies	(68,883)	(60,818)	13.3
Aeronautical revenues less business tax and levies	2,227,216	1,985,451	12.2

Major airlines at the Beijing Airport

	Contribution to Aircraft Movements		Contribution to Passenger Throughput	
	2006	2005	2006	2005
Air China Group	37.3%	37.3%	38.1%	39.1%
China Southern Airlines Group	16.0%	16.7%	16.8%	17.5%
China Eastern Airlines Group	13.8%	12.6%	12.6%	12.1%
Hainan Airlines Group	11.5%	11.8%	10.8%	8.7%

Top three origination / destination locations of domestic airlines in 2006 based on traffic volumes:

	Aircraft Movements	Passenger Throughput	Freight Throughput
1.	Shanghai	Shanghai	Shanghai
2.	Chengdu	Chengdu	Chengdu
3.	Guangzhou	Guangzhou	Shenzhen

Top three destinations of international, Hong Kong and Macau airlines in 2006 in terms of traffic volumes:

	Aircraft Movements	Passenger Throughput	Freight Throughput
1.	Hong Kong	Hong Kong	Hong Kong
2.	Tokyo	Seoul	Frankfurt
3.	Seoul	Tokyo	Singapore

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

OVERVIEW OF THE NON-AERONAUTICAL BUSINESS

In 2006, the Company's total non-aeronautical revenues were Rmb863,764,000, representing a decrease of 17.6% from the year of 2005, details of which are set out as follows:

	2006 <i>Rmb'000</i>	2005 <i>Rmb'000</i>	change %
Concession revenue	574,566	440,338	30.5
Retailing	213,706	165,489	29.1
Advertising	163,128	120,441	35.4
Ground handling service	136,317	110,107	23.8
Restaurants and food shops	52,606	42,554	23.6
Air catering	6,649	1,747	280.6
Other concessions	2,160	—	100.0
Rentals	217,816	146,502	48.7
Car parking	58,067	51,570	12.6
Ground handling facilities and services income	—	282,461	-100.0
Air catering	—	84,055	-100.0
Repairs and maintenance service	—	19,503	-100.0
Others	13,315	23,634	-43.7
Total non-aeronautical revenues	863,764	1,048,063	-17.6
Less: Business tax and levies	(53,674)	(49,536)	8.4
Non-aeronautical revenues less business tax and levies	810,090	998,527	-18.9

In 2006, the concessions revenue of the Company was Rmb574,566,000, representing an increase of 30.5% as compared with the previous year. Among these, benefiting from the growth of the air traffic volumes and aggressive adoption of various promotion measures by the Company, the concession revenue from retailing was Rmb213,706,000, representing an increase of 29.1% as compared with the previous year, and concession revenue from restaurants was Rmb52,606,000, representing an increase of 23.6% as compared with the previous year. Attributable to the decrease in vacancy rate of the advertising resources, the concessions revenue from advertising was Rmb163,128,000, representing an increase of 35.4% as compared with the previous year. In 2006, as the Company disposed of BGS and the concessions income from BGS ceased to be eliminated as internal transaction, the concessions income from ground handling service was Rmb136,317,000, representing an increase of 23.8% as compared to the previous year. In 2006, due to the disposal of BAIK, cease of elimination of the concessions income from BAIK for internal transaction as well as the increase in the number of air catering franchisee, the concessions income from air catering was Rmb6,649,000, representing a significant increase of 280.6% over the same period of the previous year. On the other hand, the other concessions income of the Company was Rmb2,160,000 as a result of the increase in franchising out of the shuttle bus services between Tianjin and the Beijing Airport.

In 2006, the rental income of the Company was Rmb217,816,000, representing an increase of 48.7% over previous year, which mainly resulted from the rise of rental in terminals.

In 2006, the income from car parking was Rmb58,067,000, representing an increase of 12.6% over previous year, which was mainly because of the growth of automobile throughput driven by the air traffic volumes.

In 2006, the other incomes of the Company were Rmb13,315,000, representing a decrease of 43.7% from previous year.

The Company disposed of BGS and BAIK in January 2006, as a result of the franchising out of the ground handling services and air catering services and disposed of its equity interest in Beijing Bowei Airport Support Limited ("Bowei") in October 2005. As such, the structure of the total incomes from non-aeronautical business have been changed, under which consolidated incomes from air catering, ground handling facilities and services, repairs and maintenance services incomes were nil.

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

OPERATING EXPENSES

In 2006, the operating expenses of the Company were Rmb1,462,841,000, representing a decrease of 12.3% from previous year (Note). Details of which are as follows:

	2006	2005	change	Comparable figures in 2005	Comparable change %
	<i>Rmb'000</i>	<i>Rmb'000</i>	%	(Note)	
Depreciation and amortisation	498,766	504,090	-1.1	481,507	3.6
Utilities and power	194,082	229,018	-15.3	213,928	-9.3
Aviation safety and security guard costs	180,831	—	100	—	100
Repairs and maintenance	175,172	184,453	-5.0	215,371	-18.7
Staff costs	135,001	418,281	-67.7	112,668	19.8
Greening and environmental maintenance	93,122	24,023	287.6	17,208	441.2
Real estate tax and other taxes	53,475	51,214	4.4	50,500	5.9
General, administrative and other expenses	132,392	256,406	-48.4	143,390	-7.7
Total operating expenses	<u>1,462,841</u>	<u>1,667,485</u>	-12.3	<u>1,234,572</u>	18.5

Note: The operating expenses in 2005 were reclassified according to the presentation of operating expenses in 2006. The comparable figures in 2005 referred to the figures after deducting the respective costs of BGS, BAIK and Bowei for the year of 2005, as well as deducting related costs from aviation security and safety services, greening and environmental maintenance services and accessorial power and energy services due to business re-organisation in December 2005.

In 2006, the depreciation and amortisation costs of the Company were Rmb498,766,000, representing an increase of 3.6% over the comparable figures of the previous year. Such increase was mainly due to the transfer of certain reconstruction works of existing facilities reconstruction completed in 2006 to the fixed assets after inspection and acceptance.

In 2006, the power and utilities of the Company were Rmb194,082,000, representing a decrease of 9.3% from the comparable figures of the previous year, which was mainly attributable to the adoption of energy-saving measures by the Company.

In 2006, the aviation safety and security guard costs were Rmb180,831,000, which was the service fee paid by the Company to CAHC. Subsequent to the transfer of the assets and staff in relation to the aviation safety and security guard business to CAHC, effective from 1 January 2006, the Company purchased related services.

In 2006, the costs of repairs and maintenance of the Company were Rmb175,172,000, representing a decrease of 18.7% from the comparable figures of the previous year due to the costs control and strengthening of management by the Company.

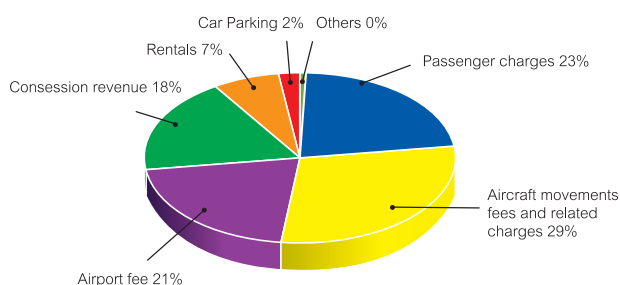
In 2006, the staff costs were Rmb135,001,000, representing an increase of 19.8% over the comparable figures of the previous year, which mainly because the performance salaries of the staff was linked with the results of the Company and of the increased staff headcount.

In 2006, the greening and environmental maintenance costs were Rmb93,122,000, representing an increase of 441.2% over the comparable figures of the previous year, which was mainly because the Company implemented outsourcing to a subsidiary and an associate of the Parent Company instead of carrying out self-operation for the greening and environmental maintenance services and accessorial power and energy services. Therefore, the related costs were classified under this item.

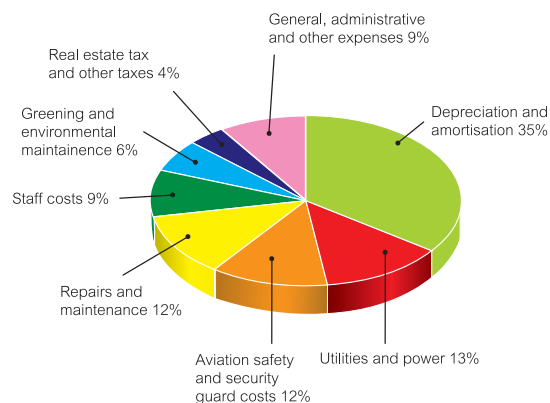
In 2006, the real estate tax and other taxes of the Company were Rmb53,475,000, representing an increase of 5.9% over the comparable figures of the previous year.

In 2006, the general, administrative and other expenses of the Company were Rmb132,392,000, representing a decrease of 7.7% from the comparable figures of the previous year. General, administrative and other expenses include conference costs, consulting fee, and fees on the engagements of agencies etc.

Revenues of the Company in 2006



Operating Expenses of the Company in 2006



PROFIT ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY

In 2006, the Company's profit attributable to equity holders of the Company totalled Rmb1,092,899,000, representing an increase of 20.3% over the previous year.

EXPOSURE TO FLUCTUATIONS IN EXCHANGE RATES

The Company's businesses are principally denominated in Rmb, except for the purchases of certain equipment, goods and materials and payment of consulting fee that are paid in US dollars and Hong Kong dollars. Dividends to shareholders holding H Shares are declared in Rmb and paid in Hong Kong dollars. During the year, the Company did not involve in any foreign currency hedging activities.

As at 31 December 2006, the Company's assets and liabilities denominated in foreign currencies, principally in US dollars and Hong Kong dollars, included cash and cash equivalents of approximately Rmb 5,457,000 (2005: Rmb10,095,000), trade and other receivables of approximately Rmb 51,926,000 (2005: Rmb44,994,000), trade and other payables of approximately Rmb 146,000 (2005: Rmb4,236,000). In 2006, the Company recorded an exchange loss of Rmb 2,058,000. The fluctuations in exchange rates did not have any significant impact on the results of the Company in 2006, and they are not expected to have any significant impact on the Company's results next year.

CONTINGENT LIABILITY

As at 31 December 2006, the Company did not have any significant contingent liability.

LIQUIDITY AND FINANCIAL RESOURCES

The Company's net cash generated from operating activities in 2006 amounted to RMB1,834,232,000, representing an increase of RMB219,393,000 as compared with RMB1,614,839,000 for the year of 2005. Net cash outflow from investing activities in 2006 amounted to RMB2,085,934,000, of which, RMB486,969,000 was used in purchasing property, plant and equipment and RMB2,000,000,000 was prepaid to the Parent Company for the acquisition of Phase III Project. Meanwhile, the Company received proceeds of RMB277,794,000 on the disposal of certain assets and liabilities, as well as RMB100,000,000 of time deposits investment with original maturities over three months but within one year. In 2006, the Company's net cash outflow from financing activities amounted to RMB149,345,000, of which, repayment of short-term bank borrowings amounted to RMB2,260,000,000, the payment of cash dividend amounted to RMB372,521,000, cash amounted to RMB1,460,000,000 received from the drawdown of short-term bank borrowings as well as cash amounted to RMB1,023,176,000 obtained from issuance of ordinary shares.

As at 31 December 2006, the Company had total cash and cash equivalents and time deposits with original maturities over three months but less than one year amounting to Rmb152,818,000, and those as at 31 December 2005 were Rmb656,811,000.

As at 31 December 2006, the current ratio of the Company was 1.64, and that as at 31 December 2005 was 0.89. Such ratios were computed by dividing the total current assets by total current liabilities as at those respective dates. The increase of current ratio mainly resulted from the increase of trade and other receivables of the Company and the significant decrease of the short-term bank borrowings for the year.

As at 31 December 2006, capital and reserves attributable to the equity holders of the Company was Rmb9,833,339,000, and that as at 31 December 2005 was Rmb8,188,110,000.

As at 31 December 2006, the liability to asset ratio of the Company was 18.49%, and that as at 31 December 2005 was 24.59%. Such ratios were computed by dividing the total amount of liabilities by the total assets as at those respective dates. The decrease of liability to asset ratio mainly resulted from the increase of the assets of the Company and the decrease of the short-term bank borrowings for the year.

For the year ended 31 December 2006, the Company received an amount of Rmb756,716,000, representing the airport fee for the period from 1 September 2004 to 31 December 2005. The airport fee for the year of 2006 is estimated to be repaid in 2007. As of the date of 25 April 2007, the Board has not acquired any information about the cessation of levy of airport fee.

BANK LOANS

As at 31 December 2006, the Company's short-term bank loans amounted to Rmb nil.

Details of the bank loans of the Company are set out in note 15 to the Financial Statements.

EMPLOYEES AND EMPLOYEE WELFARE

1. The numbers of employees of the Company are set out as follows, together with a comparison with those in the previous year:

	As at 31 December 2006	As at 31 December 2005	Comparable figures of 2005
Total employees	1,419	7,984	1,271
Contracted employees with the term over one year	859	3,084	760
Contracted employees with the term of one year and less than one year	560	4,900	511

The comparable figures refer to the total number of employees after deducting employees in relation to BGS, BAIK and internal operating units of aviation safety and security services, accessorial power and energy services and the environmental and greening services since the Company finished business re-organization on 15 March 2006.

The remuneration policy of employees of the Company is determined by the management based on market practice; mainly consisting of two parts including basic salaries and salaries on performance evaluation.

2. **Employees' pension scheme**

Details of the employees' pension scheme are set out in note 17 to the Financial Statements.

3. **Employees' housing benefits**

Details of the employees' housing benefits are set out in note 18 to the Financial Statements.

4. Employees' basic medical insurance and commercial medical insurance

With effect from 1 January 2003, the Company has complied with the regulation of the Beijing Municipal Government for basic medical insurance. According to the regulation, the Company pays the basic medical insurance and mutual insurance for large sum medical expenses for its employees at 9% and 1%, respectively, of the average monthly salaries of its employees in the previous year.

In addition, the Company may provide supplemental medical insurance benefits to their employees on a discretionary basis within 4% of the average monthly salary of its employees in the previous years. At the same time, the Company no longer pays cash medical subsidies or medical compensations to its employees. Therefore, the implementation of the above mentioned basic medical insurance does not have any substantial effect on the balance sheet and the income statement of the Company.

CHARGE ON ASSETS

There were no assets charged or pledged for the year ended 31 December 2006.

MATERIAL INVESTMENT AND MATERIAL INVESTMENT PLAN

For the year ended 31 December 2006, the Company did not have any material investment, other than the disclosure in the announcements, circulars, the interim report and this annual report.

As at 25 April 2007, the directors of the Company are not aware of any material investment or financing plan that was required to be disclosed.

SECURITIES TRANSACTION BY DIRECTORS

The Company has adopted "the Model Code for Securities Transaction by Directors and Staff" to regulate the securities transaction by directors and staff, for securities transactions on terms no less exacting than the required standard of the Model Code for Securities Transactions by Directors of listed issuers as set out in Appendix 10 to the Listing Rules ("Model Code").

Following specific enquiry made with the directors of the Company, the Company has confirmed that each of its directors has complied with the Model Code and the required standard set out in "the Model Code for Securities Transaction by Directors and Staff" drafted by the Company.