# Air China Limited

stock code: 753 HongKong 601111 Shanghai AIRC London

# Interim Report 2010

# Contents

# Important Notice

The board of directors (the "Board") and directors ("Directors") of the Company hereby confirm that there are no false representations, misleading statements or material omissions in this report, and the Directors severally and jointly accept full responsibility for the truthfulness, accuracy and completeness of the contents of this report.

The chairman Mr. Kong Dong, the chief financial officer Mr. Fan Cheng and the general manager of the Finance Department Mr. Xiao Feng of the Company hereby jointly declare that the unaudited interim condensed consolidated financial statements set out in this interim report is true and complete.

# Corporate Information

## CHINESE REGISTERED NAME

中國國際航空股份有限公司

## ENGLISH NAME

Air China Limited

## REGISTERED OFFICE

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28 Tianzhu Road
Zone A, Tianzhu Airport Industrial Zone
Shunyi District
Beijing
China

## PRINCIPAL PLACE OF BUSINESS IN HONG KONG

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Hong Kong International Airport
Hong Kong

## WEBSITE ADDRESS

www.airchina.com.cn

## DIRECTORS

Kong Dong
Wang Yinxiang
Wang Shixiang
Cao Jianxiong
Christopher Dale Pratt
Cai Jianjiang
Fan Cheng
Hu Hung Lick, Henry
Zhang Ke
Jia Kang
Fu Yang

## SUPERVISORS

Sun Yude
He Chaofan
Zhou Guoyou
Chen Bangmao
Su Zhiyong

## LEGAL REPRESENTATIVE OF THE COMPANY

Kong Dong

## JOINT COMPANY SECRETARIES

Huang Bin
Tam Shuit Mui

## AUTHORISED REPRESENTATIVES

Cai Jianjiang
Tam Shuit Mui

## LEGAL ADVISERS TO THE COMPANY

Haiwen & Partners (as to PRC Law)
Freshfields Bruckhaus Deringer
(as to Hong Kong and English Law)

## INDEPENDENT AUDITORS

Ernst & Young

## H SHARE REGISTRAR AND TRANSFER OFFICE

Computershare Hong Kong Investor Services Limited
Rooms 1712-1716, 17th Floor
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Hong Kong

## LISTING VENUES

Hong Kong, London and Shanghai

# Summary of Financial Information

| | For the six months ended 30 June 2010 RMB'000 | For the six months ended 30 June 2009 RMB'000 | Change (%) |
|---|---|---|---|
| Turnover | **34,780,975** | 23,109,739 | 50.50 |
| Profit from operations | **4,101,203** | 2,820,265 | 45.42 |
| Profit before tax | **5,465,811** | 2,666,865 | 104.95 |
| Profit after tax (including profit attributable to non-controlling interests) | **4,710,065** | 2,817,249 | 67.19 |
| Profit attributable to non-controlling interests | **97,165** | (60,975) | 259.35 |
| Profit attributable to equity holders of the Company | **4,612,900** | 2,878,224 | 60.27 |
| EBITDA(1) | **8,106,791** | 6,225,845 | 30.21 |
| EBITDAR(2) | **10,368,592** | 7,600,925 | 36.41 |
| Earnings per share attributable to equity holders of the Company (RMB) | **0.398** | 0.243 | 63.79 |
| Return on equity (%)(3) | **16.41** | 12.60 | +3.81ppt |

(1) EBITDA represents earnings before finance revenue, finance costs, income taxes, share of profits (net of losses) of associates and depreciation as computed under the International Financial Reporting Standards ("IFRSs").

(2) EBITDAR represents EBITDA before deducting operating lease expenses on aircraft and engines as well as other operating lease expenses.

(3) Return on equity represents profit for the period attributable to equity holders divided by equity attributable to equity holders of the Company at period end.

| | 30 June 2010 RMB'000 | 31 December 2009 RMB'000 | Change (%) |
|---|---|---|---|
| Total assets | **143,091,899** | 107,893,272 | 32.62 |
| Total liabilities | **115,297,516** | 83,938,805 | 37.36 |
| Non-controlling interests | **(315,984)** | 38,571 | (919.23) |
| Equity attributable to equity holders of the Company | **28,110,367** | 23,915,896 | 17.54 |
| Equity per share (RMB) | **2.43** | 2.02 | 20.30 |

# Summary of Operating Data

The data of 2010 set out below include the data of Air China Limited ("the Company"), Air China Cargo Company Limited ("Air China Cargo") and Air Macau Company Limited ("Air Macau") for the first half of 2010 and that of Shenzhen Airlines Company Limited ("Shenzhen Airlines") for the period from 20 April 2010 to 30 June 2010. In particular, the statistics relating to Shenzhen Airlines include information of Kunming Airlines Co., Ltd ("Kunming Airlines"). The data for the corresponding period of 2009 did not include information of Shenzhen Airlines.

| | **For the six months ended 30 June 2010** | For the six months ended 30 June 2009 | Increase/ (decrease) |
|---|---|---|---|
| **Traffic** | | | |
| **RPK (in millions)** | **47,213.69** | 35,733.29 | 32.13% |
| International | **15,916.93** | 12,866.31 | 23.71% |
| Domestic | **29,114.96** | 21,129.40 | 37.79% |
| Hong Kong, Macau and Taiwan | **2,181.80** | 1,737.58 | 25.57% |
| **RFTK (in millions)** | **2,214.59** | 1,517.59 | 45.93% |
| International | **1,663.38** | 1,104.39 | 50.62% |
| Domestic | **499.99** | 373.72 | 33.79% |
| Hong Kong, Macau and Taiwan | **51.22** | 39.48 | 29.74% |
| **Passengers (in thousands)** | **26,269.14** | 19,524.61 | 34.54% |
| International | **3,357.47** | 2,587.69 | 29.75% |
| Domestic | **21,573.76** | 15,846.10 | 36.15% |
| Hong Kong, Macau and Taiwan | **1,337.91** | 1,090.82 | 22.65% |
| **Cargo and mail carried (tonnes)** | **603,354.22** | 423,235.27 | 42.56% |
| **Kilometers flown (in millions)** | **346.18** | 270.54 | 27.96% |
| **Block hours (in thousands)** | **550.07** | 431.93 | 27.35% |
| **Number of flights** | **201,732** | 154,822 | 30.30% |
| International | **23,421** | 20,631 | 13.52% |
| Domestic | **166,665** | 123,692 | 34.74% |
| Hong Kong, Macau and Taiwan | **11,646** | 10,499 | 10.92% |
| **RTK (in millions)** | **6,445.74** | 4,723.42 | 36.46% |
| **Capacity** | | | |
| **ASK (in millions)** | **59,850.19** | 48,067.77 | 24.51% |
| International | **19,602.72** | 17,568.31 | 11.58% |
| Domestic | **37,290.27** | 27,920.90 | 33.56% |
| Hong Kong, Macau and Taiwan | **2,957.20** | 2,578.56 | 14.68% |
| **AFTK (in millions)** | **3,725.03** | 3,072.60 | 21.23% |
| International | **2,462.11** | 1,987.02 | 23.91% |
| Domestic | **1,154.32** | 992.70 | 16.28% |
| Hong Kong, Macau and Taiwan | **108.60** | 92.88 | 16.93% |
| **ATK (in millions)** | **9,085.91** | 7,414.38 | 22.54% |

# Summary of Operating Data

| | For the six months ended 30 June 2010 | For the six months ended 30 June 2009 | Increase/ (decrease) |
|---|---|---|---|
| **Load factors** | | | |
| **Passenger load factor (RPK/ASK)** | **78.89%** | 74.34% | 4.55ppt |
| International | **81.20%** | 73.24% | 7.96ppt |
| Domestic | **78.08%** | 75.68% | 2.40ppt |
| Hong Kong, Macau and Taiwan | **73.78%** | 67.39% | 6.39ppt |
| **Cargo and mail load factor (RFTK/AFTK)** | **59.45%** | 49.39% | 10.06ppt |
| International | **67.56%** | 55.58% | 11.98ppt |
| Domestic | **43.31%** | 37.65% | 5.66ppt |
| Hong Kong, Macau and Taiwan | **47.16%** | 42.50% | 4.66ppt |
| **Yield** | | | |
| **Yield per RPK (RMB)** | **0.6056** | 0.5385 | 12.46% |
| International | **0.5367** | 0.4739 | 13.25% |
| Domestic | **0.6304** | 0.5682 | 10.96% |
| Hong Kong, Macau and Taiwan | **0.7769** | 0.6564 | 18.35% |
| **Yield per RFTK (RMB)** | **1.8722** | 1.2958 | 44.49% |
| International | **1.1836** | 1.1463 | 58.22% |
| Domestic | **1.8108** | 1.5191 | 19.20% |
| Hong Kong, Macau and Taiwan | **4.5680** | 3.3634 | 35.82% |
| **Fleet** | | | |
| Total number of aircraft | **381** | 255 | 49.41% |
| **Unit cost** | | | |
| Operating cost per ASK (RMB) | **0.5119** | 0.4221 | 21.27% |
| Operating cost per ATK (RMB) | **3.2869** | 2.7365 | 20.11% |

*Note:* Shenzhen Airlines has been consolidated into the scope of the Company, its subsidiaries and joint ventures ("the Group") since 20 April 2010.

# Chairman's Statement

In the first half of 2010, thanks to the gradual stabilisation and recovery of the global economy, in particular as a result of China's rapid economic growth and the stimulation provided by the World Exposition Shanghai China 2010, the Group's operating results hit historical high and increased significantly as compared with the same period last year. In this reporting period, the Group recorded an RMB5,466 million profit before tax, an RMB4,613 million profit attributable to equity holders and an RMB0.398 of earnings per share attributable to equity holders, representing an increase of 104.95%, 60.27% and 63.79%, respectively, from the same period last year.

In light of the strong demand in the aviation market in the first half of this year, the Group was able to seize market opportunities and, by introducing additional capacity and tapping the Group's potential, expand its total capacity by 24.51% from the same period last year. In the domestic market, the Group continued to increase its capacity in the relevant regions in North China and opened 13 routes including Beijing-to-Ulan Hot (Inner Mongolia), Beijing-to-Chaoyang (Liaoning Province) and Beijing-to-Jiuzhaigou (Sichuan Province) routes. In the international market, the Group increased its capacity on the routes to Japan and other Asia-Pacific regions, resumed Beijing-to-Sao Paulo route, and opened Beijing-to-Manila, Shanghai-to-Bangalore (via Chengdu) and other international routes. In the regional market, the Group continued to increase its capacity and opened Shanghai-to-Songshan (Taipei) route and Wuhan-to-Macau route.

The Group continued to improve its operating efficiency for passenger operation. In the first half of this year, the Group recorded 47,214 million revenue passenger kilometers, carried 26.27 million passengers with a load factor of 78.89%, representing an increase of 32.13%, 34.54% and 4.55 percentage points, respectively, from the same period last year. In this reporting period, the Group generated RMB28,627 million from its passenger operation, representing an increase of 48.77% from the same period last year. The revenue from the sale of first class and business class increased significantly, in particular the first class and business class sale relating to Europe, America and Australia increased by 48% from the same period last year. The Group's passenger yield increased by 12.46% from the same period last year to RMB0.61.

In the first half of this year, the cargo market saw strong growth, in particular, the Asia-Pacific regions, especially China. The Group allocated 3,725 million available freight tonne kilometers to its cargo operation, representing an increase of 21.23% from the same period last year. The increased capacity were mainly allocated to Europe and America. In the first half of this year, the Group realised 2,215 million revenue tonne kilometers and carried 603,400 tonnes of cargo and mail with a load factor of 59.45%, which represented an increase of 45.93%, 42.56% and 10.06 percentage points, respectively, from the same period last year. The Group recorded revenue of RMB4,462 million from its cargo operation, representing an increase of 126.93% from the same period last year. The revenue from international and regional routes increased remarkably by 162.47% and 76.21%, respectively, from the same period last year. The Group's cargo yield increased by 44.49% to RMB1.87 and the profit for cargo business hit historical high.

The Group's fuel cost increased substantially in the first half of this year with the purchase price of international fuel increased by 41.33% and the purchase price of domestic fuel increased by 34.54%, from the same period last year. The share of fuel cost in the total operating costs increased from 30.06% of the same period last year to 34.59%. Although the fuel surcharge, to some extent, eased our cost pressure, the upward trend of fuel costs remains a major challenge to the Group. As of 30 June 2010, the Group recorded a net gain of RMB721 million as a result of the changes in the fair value of the Group's fuel derivative contracts.

As of 30 June 2010, the Group owned 381 aircraft. In the first half of this year, 26 new aircraft which are more fuel-efficient, mainly A321, A320, B737-800, A330-300 aircraft, were introduced. In the mean time, 7 aircraft which are relatively old models, including B757-200, B737-300 and B747-200F aircraft, retired from our fleet. Accordingly, the Group's fleet structure continued to be optimised and the fleet became younger.

The Group continued to improve its hub operations. The transfer passengers of Beijing hub reached 2.51 million, representing an increase of 8% from the same period last year. The available connections for Chengdu hub rose by 28% from the same period last year. In Chengdu hub, although the passengers for domestic to domestic transfers dropped slightly, transfer passengers for other sectors increased by 71% from the same period last year. The Group's transfer passengers in Shanghai, a traffic gateway, were 0.24 million in the first half of this year, representing an increase of 30% from the same period last year. The completion of the Shanghai Hongqiao Airport T2 transition provided significant supplemental resources for the construction of Shanghai as a gateway. The acquisition of the controlling position in Shenzhen Airlines strengthened the Group's operations in Beijing, Chengdu and Shanghai as well as its route network coverage.

The Group continued to put great emphasis on its service and product innovation and service consistency in an effort to improve its service. In this reporting period, the Group launched the marketing and service product of super-economy class, and enhanced the diversification of its service products. The Group's Frequent Flyer Service Centre offered 24-hour service and expanded the products and services for its members. The Group launched self-service of baggage check-in in Beijing in order to gradually improve its customer services. In Shanghai, the Group achieved self-running of full-process ground handling at its two airports and improved its service interface and service efficiency.

In light of market changes, the Group actively implemented its strategic deployment and resource integration. The Company increased its equity interest in Shenzhen Airlines and became its controlling shareholder in the first half of this year. This would facilitate further integration of aviation resources and synergy and had long-term strategic significance in terms of market deployment and resource allocation.

The Group fully leveraged its strategic partnership with Cathay Pacific Airways Limited ("Cathay Pacific") by increasing synergy from their passenger and cargo businesses. The two companies accelerated the establishment of the cargo joint venture so as to seize the rare growth opportunities in the cargo market and create new growth benefit for their cooperation.

The recovery of the global aviation market has injected great vitality into the cooperation between the members of Star Alliance. In the first half of this year, the contribution to the Group's sales by the members of Star Alliance increased by more than 50% from the same period last year and the synergy among the members of Star Alliance became more apparent.

The global aviation industry is facing various uncertainties in the second half of this year. Rising oil price, exchange rate fluctuations and natural disasters would have considerable impact on the aviation industry. The Group will continue to adhere to its prudent operation strategy, actively seek new market growth opportunities, endeavor to improve its service and strengthen and expand its competitive strengths, and strive to make better returns to its shareholders and the society.

孔栋

**Kong Dong**
*Chairman*

Beijing, PRC
August 25, 2010

# Business Overview

## BUSINESS REVIEW OF PASSENGER SERVICE OPERATION

In the first half of 2010, the Company's ASK reached 52,205 million, representing an increase of 12.28% over the same period last year, and its passenger traffic was 41,343 million RPK, representing an increase of 19.06% over the same period last year. The number of passengers carried by the Company was 22,099,200, representing an increase of 17.42% over the same period last year. The Company recorded an average passenger load factor of 79.19%, representing an increase of 4.51 percentage points over the same period last year.

Air Macau's ASK was 1,535 million, representing a decrease of 2.42% over the same period last year. Its passenger traffic increased by 7.29% from that of the same period last year to 1,083 million RPK. It carried 681,100 passengers with a load factor of 70.55%, representing a decrease of 3.34% and an increase of 6.38 percentage points, respectively, over the same period last year.

Shenzhen Airlines' ASK (including information of Kunming Airlines) was 14,966 million, representing an increase of 19.63% over the same period last year. Its passenger traffic increased by 22.30% over the same period last year to 11,877 millions RPK. It carried 8,732,200 passengers with a load factor of 79.37%, representing an increase of 22.33% and 1.74 percentage points, respectively, over the same period last year.

## BUSINESS REVIEW OF CARGO SERVICE OPERATION

In the first half of 2010, the AFTK of Air China Cargo, including its freighters and the bellyhold space of the Company's passenger aircraft, increased by 17.90% over the same period last year to 3,590 million. Its cargo and mail traffic was 2,125 million RFTK, representing an increase of 41.25% over the same period last year. During the period, it carried 544,500 tonnes of cargo and mail with a load factor of 59.20%, representing an increase of 33.21% and an increase of 9.79 percentage points, respectively, over the same period last year.

Air Macau's AFTK was 30.69 million, representing an increase of 9.99% over the same period last year. Its cargo and mail traffic increased by 38.86% to 18.04 million RFTK as compared with the same period last year. It carried 13,300 tonnes of cargo and mail with a load factor of 58.79%, representing a decrease of 8.03% and an increase of 12.22 percentage points, respectively, over the same period last year.

Shenzhen Airlines' AFTK (including information of Kunming Airlines) was 281 million, representing an increase of 13.11% over the same period last year. Its cargo and mail traffic increased by 25.13% over the same period last year to 171 million RFTK. It carried 109,900 tonnes of cargo and mail with a load factor of 60.75%, representing an increase of 26.90% and an increase of 5.84 percentage points, respectively, over the same period last year.

## FLEET

Details of the fleet of the Group are set out in the table below:

| | Number of aircraft | | | |
|---|---|---|---|---|
| **Type of aircraft** | **Owned** | **Finance leased** | **Operating leased** | **Sub-total** |
| **Passenger aircraft** | **165** | **88** | **113** | **366** |
| Among which: Boeing series | 104 | 39 | 74 | 217 |
| Airbus series | 61 | 49 | 39 | 149 |
| **Freighters** | **8** | **0** | **4** | **12** |
| **Business jet** | **0** | **0** | **3** | **3** |
| **Total** | **173** | **88** | **120** | **381** |

As of 30 June 2010, the Company operated a fleet of 266 aircraft, including 263 passenger aircraft and 3 business jets, with an average age of aircraft being 6.6 years (excluding 11 aircraft under wet lease).

As of 30 June 2010, Air China Cargo operated a fleet of 10 aircraft. All of them were freighters.

As of 30 June 2010, Air Macau operated a fleet of 11 aircraft, of which 9 were passenger aircraft (excluding four A321 aircraft and one A320 aircraft leased to the Company under wet lease) and 2 were freighters.

As of 30 June 2010, Shenzhen Airlines (including Kunming Airlines) operated a fleet of 94 aircraft. All of them were passenger aircraft.

## CONSTRUCTION OF HUB AND ROUTE NETWORK

In the first half of 2010, the Company optimised the allocation of its carrying capacity, fully tapped and improved its potential and efficiency of rare and core resources such as flight scheduling, aircraft and air crew, and made efforts in maximising the carrying capacity and scale. The construction of the Beijing hub, Chengdu regional hub and Shanghai gateway was further improved and their strength as hubs was proven.

The Company continued to optimise its flight structure and flight intervals in relation to the arrival flights and the departure flights in Beijing in order to increase the availability and quality of effective connecting flights. The number of effective connecting flights (within 2 hours) available at the Beijing Capital International Airport increased by 31% and its proportion grew by nearly 3.5% as compared with the same period last year. The route network of the Beijing hub was further expanded with the addition of new routes from Beijing to Manila, Beijing to Zhanjiang, Beijing to Ulan Hot, Beijing to Chaoyang and Beijing to Jiuzhaigou.

In Chengdu, the Company opened new routes from Chengdu to Pudong to Nagoya, Chengdu to Tengchong, Chengdu to Zhuhai, Chengdu to Shantou, Chengdu to Zhanjiang, and Chengdu to Bangalore, and the number of effective connecting flights per week in Chengdu regional hub reached 4,346, representing an increase of 28% as compared with the same period last year.

In Shanghai, in addition to new routes from Shanghai to Chengdu to Bangalore, Shanghai to Yinchuan, and Shanghai to Jiuzhaigou, the Company also resumed the routes from Shanghai to Guilin, Shanghai to Yichang and Shanghai to Wuhan. The Company began to use larger-sized aircraft for serving the routes from Shanghai to Tokyo and Shanghai to Osaka. The Company also made wide-bodied aircraft available for the Beijing-Shanghai Express Route to meet high-end market demand. There was a significant growth in both passenger number and revenue for the second quarter which were boosted since the World Exposition Shanghai China 2010 in the first half of this year.

As of 30 June 2010, the Company's scheduled flights connected 31 countries and regions, including 47 international cities, 88 domestic cities and 3 regions. We operated 282 passenger routes, including 69 international routes, 13 regional routes and 200 domestic routes covering 138 cities and regions.

## MARKETING AND COOPERATION

In the first half of 2010, the Company strengthened control over its sales, actively optimised its sales channels and increased the proportion of revenue attributable to direct sales channels and improved the revenue contributed by the first and business classes, connecting flights and frequent-flyers. Aggregate revenue from connecting flights, first and business classes, e-business sales and key clients recorded for the first half of this year grew by 35%, 47%, 124% and 70%, respectively, as compared with the same period last year. The total membership of frequent-flyers reached 12.64 million and their contribution to revenue increased by 83% as compared with the same period last year.

The Company actively innovated marketing efforts and improved its marketing capability in overseas markets by furthering in-depth cooperation between overseas distribution outlets and agents such as travel management companies and online travel agencies, and optimising the structure of distribution outlets, which resulting in a remarkable increase in the proportion of sales attributable to overseas distribution outlets.

# Business Overview

With respect to price publication, the Company increased training in and process management of pricing system application and made breakthroughs in price publication over routes relating to Australia, Korea and Japan. In the first half of this year, the Company's revenue generated from sales of international passenger tickets using system price released by ATPCO accounted for 58% of our total sales revenue and represented an increase of 19% as compared with the same period last year.

The Company improved its operation quality and perfected its service functions by launching the "City Express" products from Beijing to Qingdao, Beijing to Shenzhen, Chengdu to Guangzhou and Chengdu to Shenzhen in March and April respectively based on in-depth consideration of the specific travel needs of business travellers and via cooperation with Shandong Airlines Co. Limited ("Shandong Airlines") and Shenzhen Airlines, and thus received positive comments and enjoyed brandname effect among business travellers. Both our "City Express" and "Air China Express" have become important integral parts of our brand marketing system.

In the first half of 2010, the Company strengthened, consolidated and expanded the scope and potential for cooperation with Star Alliance partners as well as international and domestic partners by riding on the recovery of the global aviation market. This has provided strong network support to the Company, leading to an increase of 100% in the revenue from Star Alliance as compared with the same period last year. In association with six Star Alliance airlines including Continental Airlines, Inc. and Deutsche Lufthansa AG, the Company took the lead to duly sign the "Key Client Agreement between CNPC and Star Alliance" with China National Petroleum Corporation ("CNPC"), which marked a new milestone in client development after we joined the Star Alliance.

Our cooperation with Cathay Pacific and Air Macau was further promoted, which helped sharing resources, lowered our costs, generated synergistic effect and brought win-win results to our partners. Meanwhile, business integration between the Company and Shenzhen Airlines was actively pushed forward. On 16 April 2010, both parties commenced their first-phase code sharing cooperation for 158 flights on 13 routes, which increased their flight density and offered more choices to passengers. As such, the market synergy effect was gradually generated.

## COST CONTROL

In the first half of 2010, the Company strengthened its leading cost advantage by optimising cost structure and enhancing cost process management. Aircraft fleet, traffic capacity structure and allocation of aircraft models and routes were constantly optimised, while cost management strategies were implemented from the very beginning of our operations. Through saving APU fuel, reducing aircraft weight, monitoring aircraft performance, optimising and selecting the best flight routes, the Company managed to cut its expenses by RMB176 million and shorten the flying time by 1,077 hours, thereby improving its fleet utilisation efficiency. The Company's debt structure was optimised after its aircraft financing and the working capital loans were reasonably arranged, while aviation equipment purchasing costs were reduced through centralised deployment of aviation equipment.

## SERVICES AND PRODUCTS

Consistency of our products and services was emphasised, and our service quality was further improved. The Company fully followed the Skytrax Evaluation Standards, adopted the ISO9001 Quality Control System, and focused on unifying major service standards and workflow of the interface with passengers. A customer relations centre was set up to improve the model for the operation and maintenance of customer relationship. A service system backed by customer managers came to practice in the first half of 2010, with 296 customer managers serving this post consecutively. By making concerted efforts, significant improvement was accomplished in our self-operating lounges, flight information release, in-flight entertainment programmes and catering, luggage transportation, cabin broadcasting, communication skills of flight attendants and other services. The survey to gauge passenger satisfaction was improved vigorously under a better management model, thus gradually forming a service performance indicator system covering all service processes. The Company also monitored and inspected the quality of its transportation service, and rectified 32 types of service problems. In the first half of 2010, the number of effective complaints declined substantially, while the overall satisfaction with our services increased steadily.

Our service innovation was further enhanced. The Company launched the marketing and service product of super-economy class. The entire journey guidance was offered to our high-end transfer passengers, while the abnormal luggage delivery was handled by our designated staff throughout the entire process. The customer relations maintenance system was developed, and the construction of the small and medium enterprise travelling management platform and the ticketing-via-mobile-phone platform was also initiated. The self-service luggage check-in was rolled out in Beijing, and the online check-in service was newly launched in 13 cities in China and abroad. The self-service check-in rate of our passengers accounted for 21% of our total passengers, representing an increase of 3 percentage points as compared with the same period last year.

## EMPLOYEES

As of 30 June 2010, the Company had 23,734 employees, and its subsidiaries and joint ventures had 26,524 employees.

# Management's Discussion and Analysis of Financial Conditions and Results of Operations

The following discussion and analysis are based on the Group's interim condensed consolidated financial statements and its notes prepared in accordance with IFRSs and are designed to assist the readers in understanding the information provided in this report further so as to better understand the financial performance of the Group as a whole.

## ANALYSIS OF PROFITABILITY

For the six months ended 30 June 2010, the Group recorded a profit before tax of RMB5,466 million, and the profit attributable to equity holders of the Company was RMB4,613 million with basic earnings per share of RMB0.398, representing an increase of 104.95%, 60.27% and 63.79% respectively as compared with the same period of 2009.

The substantial increase of profit in the first half of 2010 as compared with the same period of the previous year was mainly attributable to the higher growth in the profit from operation of the Company and the airline companies invested by the Company due to the rebound of the global air traffic market, particularly the rapid growth in demand in domestic air passenger and cargo markets, as well as the Group's effective operational management, marketing and cost control.

## TURNOVER

For the six months ended 30 June 2010, the Group's total turnover (including air traffic revenue and other operating revenue, net of business taxes and surcharges) was RMB34,781 million, representing an increase of RMB11,671 million or 50.50% from the same period of 2009, among which, air traffic revenue amounted to RMB33,090 million, representing an increase of RMB11,880 million or 56.01% from the same period of 2009; and other operating revenue was RMB1,691 million, representing a decrease of RMB209 million from the same period of 2009, which was primarily attributable to the refund of RMB824 million from China Civil Aviation Infrastructure Development Fund ("CAAC Infrastructure Development Fund") recognised in the same period of the previous year. Such policy was repealed on 30 June 2009.

## REVENUE CONTRIBUTION BY GEOGRAPHICAL SEGMENT

| | For the six months ended 30 June | | | | |
|---|---|---|---|---|---|
| | **2010** | | 2009 | | **Change** |
| *(in RMB'000)* | **Amount** | **Percentage** | Amount | Percentage | (%) |
| International | **12,278,221** | **35.30%** | 7,363,515 | 31.86% | 66.74 |
| Domestic | **20,445,640** | **58.79%** | 14,472,838 | 62.63% | 41.27 |
| Hong Kong, Macau and Taiwan | **2,057,114** | **5.91%** | 1,273,386 | 5.51% | 61.55 |
| Total | **34,780,975** | **100.00%** | 23,109,739 | 100.00% | 50.50 |

## AIR PASSENGER REVENUE

For the six months ended 30 June 2010, the Group recorded air passenger revenue of RMB28,627 million, representing an increase of RMB9,384 million from the same period of 2009, among which, the increase in traffic capacity, passenger load factor and passenger yield contributed to an increase in revenue of RMB4,748 million, RMB1,464 million and RMB3,172 million, respectively.

## AIR PASSENGER REVENUE CONTRIBUTED BY GEOGRAPHICAL SEGMENT

| | For the six months ended 30 June | | | | |
|---|---|---|---|---|---|
| | **2010** | | 2009 | | **Change** |
| *(in RMB'000)* | **Amount** | **Percentage** | Amount | Percentage | (%) |
| International | **8,542,833** | **29.84%** | 6,097,544 | 31.69% | 40.10 |
| Domestic | **18,389,147** | **64.24%** | 12,004,816 | 62.38% | 53.18 |
| Hong Kong, Macau and Taiwan | **1,695,093** | **5.92%** | 1,140,616 | 5.93% | 48.61 |
| Total | **28,627,073** | **100.00%** | 19,242,976 | 100.00% | 48.77 |

## AIR CARGO REVENUE

For the six months ended 30 June 2010, the Group's air cargo and mail revenue was RMB4,462 million, representing an increase of RMB2,496 million from the same period of 2009, among which, the increase in traffic capacity, cargo load factor and cargo yield contributed to an increase in revenue of RMB571 million, RMB551 million and RMB1,374 million, respectively.

## AIR CARGO REVENUE CONTRIBUTED BY GEOGRAPHICAL SEGMENT

| | For the six months ended 30 June | | | | |
|---|---|---|---|---|---|
| | **2010** | | 2009 | | **Change** |
| *(in RMB'000)* | **Amount** | **Percentage** | Amount | Percentage | (%) |
| International | **3,322,739** | **74.46%** | 1,265,970 | 64.38% | 162.47 |
| Domestic | **905,805** | **20.30%** | 567,735 | 28.87% | 59.55 |
| Hong Kong, Macau and Taiwan | **233,953** | **5.24%** | 132,770 | 6.75% | 76.21 |
| Total | **4,462,497** | **100.00%** | 1,966,475 | 100.00% | 126.93 |

## OPERATING EXPENSES

For the six months ended 30 June 2010, the Group's operating expenses amounted to RMB30,680 million, representing an increase of RMB10,390 million or 51.21% from the same period of 2009. The breakdown of the operating expenses is set out below:

| | For the six months ended 30 June | | | | |
|---|---|---|---|---|---|
| | **2010** | | 2009 | | **Change** |
| *(in RMB'000)* | **Amount** | **Percentage** | Amount | Percentage | (%) |
| Jet fuel costs | **10,612,980** | **34.59%** | 6,098,289 | 30.06% | 74.03 |
| Movements in fair value of fuel derivative contracts | **(720,801)** | **(2.35%)** | (1,449,791) | (7.15%) | (50.28) |
| Take-off, landing and depot charges | **3,559,424** | **11.60%** | 2,706,284 | 13.34% | 31.52 |
| Depreciation | **4,005,588** | **13.06%** | 3,405,580 | 16.78% | 17.62 |
| Aircraft maintenance, repair and overhaul costs | **1,038,642** | **3.39%** | 879,252 | 4.33% | 18.13 |
| Employee compensation costs | **4,150,838** | **13.53%** | 2,936,752 | 14.47% | 41.34 |
| Air catering charges | **853,590** | **2.78%** | 694,285 | 3.42% | 22.95 |
| Selling and marketing expenses | **1,796,598** | **5.86%** | 1,322,048 | 6.52% | 35.90 |
| General and administrative expenses | **466,681** | **1.52%** | 362,105 | 1.78% | 28.88 |
| Others | **4,916,232** | **16.02%** | 3,334,670 | 16.45% | 47.43 |
| Total | **30,679,772** | **100.00%** | 20,289,474 | 100.00% | 51.21 |

- Jet fuel costs increased by 74.03% to RMB10,613 million for the six months ended 30 June 2010 as compared with RMB6,098 million for the six months ended 30 June 2009, which accounted for 34.59% of total operating expenses as compared with 30.06% for the same period of 2009. The substantial increase in the Group's jet fuel costs was mainly due to the consolidation of Shenzhen Airlines, the growing jet fuel consumption as a result of the increase in flight hours and the rising jet fuel price.

- Gains due to the movements in fair value of fuel derivative contracts for the six months ended 30 June 2010 was RMB721 million, including a recovery of RMB735 million in the fair value of the derivative contracts and changes in fair value of RMB14 million resulting from the effective settlement of the derivative contracts.

- Take-off, landing and depot charges increased because more aircraft take-offs and landings take place as well as increased expenditures arising from the consolidation of Shenzhen Airlines.

- Depreciation expenses increased mainly due to the increase in assets and the number of self-owned and finance leased aircraft resulting from the consolidation of Shenzhen Airlines.

- Aircraft maintenance, repair and overhaul costs increased mainly due to the consolidation of Shenzhen Airlines.

- Employee compensation costs increased during the current reporting period due to the increases in flight hours and basic income of employees as well as the consolidation of Shenzhen Airlines.

- Air catering charges increased primarily due to the increase in the number of passengers carried and the consolidation of Shenzhen Airlines.

- Selling and marketing expenses increased mainly due to the consolidation of Shenzhen Airlines and the increase in sales commission.

- Other operating expenses mainly included the aircraft and engines operating lease expenses, CAAC Infrastructure Development Fund and the daily expenses arising from air traffic business not included in the items specifically set forth above.

## FINANCE REVENUE AND FINANCE COSTS

For the six months ended 30 June 2010, the Group recorded RMB279 million of net gains from foreign exchange, representing an increase of RMB103 million or 58.80% from the same period of 2009, was mainly as a result of the continuous appreciation of Renminbi against US dollars. For the current reporting period, the Group recorded a net fair value loss on interest rate derivative contracts of RMB138 million. The Group also recorded interest expenses of RMB637 million, which represented a decrease of RMB209 million from same period of 2009 mainly due to the fact that most of the Group's interest-bearing debts were those with floating interest rates such that the decrease of LIBOR would lead to reduced interest expenses.

## SHARE OF PROFITS AND LOSSES OF ASSOCIATES

For the six months ended 30 June 2010, the Group's share of profits of its associates was RMB1,719 million, representing an increase of RMB1,403 million or 443.99% as compared with the same period of 2009, which was mainly due to the share of profit of in Cathay Pacific of RMB1,600 million by way of equity accounting, representing an increase of RMB1,387 million from the same period of 2009.

## ANALYSIS OF ASSETS STRUCTURE

As at 30 June 2010, the total assets of the Group amounted to RMB143,092 million, representing an increase of 32.62% as compared with 31 December 2009, among which the current assets were RMB14,867 million, accounting for 10.39% of the total assets, while the non-current assets were RMB128,225 million, accounting for 89.61% of the total assets.

For the current assets, cash and cash equivalents amounted to RMB5,674 million, representing an increase of 109.64% from 31 December 2009, which was mainly attributable to the consolidation of Shenzhen Airlines and good sales performance; while accounts receivable increased by 55.62% to RMB3,197 million from 31 December 2009, which was mainly due to the consolidation of Shenzhen Airlines and the growth in sales.

For the non-current assets, the net book value of property, plant and equipment as at 30 June 2010 was RMB95,215 million, representing an increase of 26.88% from 31 December 2009, which was mainly attributable to the consolidation of Shenzhen Airlines and the increase in the number of self-owned and finance leased aircraft. Advance payments for aircraft and related equipment was RMB13,510 million, representing an increase of 75.10% from 31 December 2009.

## ASSETS MORTGAGE

As at 30 June 2010, the Group mortgaged certain aircraft and premises with an aggregate net book value of approximately RMB57,456 million (compared with RMB37,113 million as at 31 December 2009), certain number of shares in its associated Company with an aggregate market value of approximately RMB5,399 million (compared with approximately RMB5,161 million as at 31 December 2009), and land use rights with an aggregate net book value of approximately RMB41 million (compared with approximately RMB41 million as at 31 December 2009) pursuant to certain bank loans and finance lease agreements. In addition, certain bank deposits of the Group of approximately RMB1,578 million (compared with approximately RMB565 million as at 31 December 2009) were pledged as security in respect of certain bank loans, operating leases and financial derivatives of the Group.

## CAPITAL EXPENDITURE

For the six months ended 30 June 2010, the total project investment completed by the Company amounted to RMB6,127 million. The total investment in aircraft and engines was RMB5,811 million, including prepayment of RMB3,480 million for the purchase of aircraft for 2010 and onwards. The total investment and purchase in aircraft modifications and additions, flight simulators and expensive parts and components was RMB171 million. Other project investment completed by the Company amounted to RMB316 million.

## EQUITY INVESTMENT

As at 30 June 2010, the equity investments in the Group's associates increased by RMB1,154 million to RMB13,341 million, representing an increase of 9.47% from 31 December 2009, of which the equity investments in Cathay Pacific and Shandong Airlines were RMB12,197 million and RMB233 million. Cathay Pacific and Shandong Airlines recorded a profit of RMB6,074 million and RMB209 million, respectively, for the six months ended 30 June 2010.

## DEBT STRUCTURE ANALYSIS

As at 30 June 2010, the total liabilities of the Group amounted to RMB115,298 million, representing an increase of 37.36% from 31 December 2009, of which current liabilities were RMB51,623 million, accounting for 44.77% of the total liabilities, and non-current liabilities were RMB63,674 million, accounting for 55.23% of the total liabilities.

For the current liabilities, the liabilities under derivative financial instruments amounted to RMB1,678 million, representing a decrease of RMB596 million from 31 December 2009. The interests-bearing debts (including bank loans and other loans, obligations under finance leases and bills payables) amounted to RMB28,734 million, representing an increase of 34.41% from 31 December 2009, which was mainly attributable to interests-bearing debts arising from the consolidation of Shenzhen Airlines. Other payables and accruals amounted to RMB8,265 million, representing an increase of 77.91% from 31 December 2009, which was mainly attributable to the consolidation of Shenzhen Airlines.

For the non-current liabilities, the interest-bearing debts (including bank and other loans, corporate bonds and obligations under finance leases) amounted to RMB57,080 million, representing an increase of 33.72% as compared with 31 December 2009, which was mainly due to the increase in debts arising from the consolidation of Shenzhen Airlines.

## COMMITMENTS AND CONTINGENT LIABILITIES

The capital commitment of the Group as at 30 June 2010 was RMB87,793 million, representing a substantial increase as compared with RMB62,037 million recorded as at 31 December 2009, which was primarily used for the purchase of certain aircraft and related equipment to be delivered in the coming years and for the construction of certain properties. The Group had operating lease commitments of RMB19,443 million, representing an increase of 38.35% from 31 December 2009, which was primarily used for leasing aircraft, office premises and related equipment. The Group had investment commitments of RMB402 million, representing an increase of RMB351 million from 31 December 2009, which was mainly the investment commitments made by Shenzhen Airlines, a subsidiary of the Group, to its associates and joint ventures.

As at 30 June 2010, the Group's contingent liabilities in respect of guarantees to bank loans provided to its associates were RMB26 million. Details of the contingent liabilities of the Group are set out in note 23 to the Group's interim condensed consolidated financial statements for 2010.

## GEARING RATIO

As at 30 June 2010, the Group's gearing ratio (total liabilities divided by total assets) was 80.58%, representing an increase of 2.78 percentage points as compared with 77.80% recorded as at 31 December 2009, which was primarily due to the consolidation of Shenzhen Airlines. Meanwhile, the Group recorded profits in the current reporting period which increased shareholders' equity from RMB23,954 million as at 31 December 2009 to RMB27,794 million as at 30 June 2010. Considering that the prevailing gearing ratios of other air carriers in the aviation industry were at a relatively high level, the Group continues to maintain the leading position in the domestic aviation industry in terms of gearing ratio and its long-term insolvency risks are also under its control.

## WORKING CAPITAL AND ITS SOURCES

As at 30 June 2010, the net current liabilities of the Group (i.e. the current liabilities minus the current assets) were RMB36,756 million, representing an increase of RMB8,108 million from 31 December 2009. The Group's current ratio, which represents current assets divided by current liabilities, was 0.29, representing an increase of 0.06 from 0.23 as at 31 December 2009. The increase of the net current liabilities was mainly due to the consolidation of Shenzhen Airlines.

The Group meets its working capital needs mainly through its operating activities and external financing activities. For the first half of 2010, the Group's net cash inflow from operating activities was RMB6,909 million, representing an increase of 481.26% from RMB1,189 million for the same period of 2009. This was primarily due to a mix of the consolidation of Shenzhen Airlines and the substantial increase in revenue from the Group's principal business. Net cash outflow from investment activities was RMB5,041 million, representing an increase of 157.53% from RMB1,958 million for the same period in 2009, primarily due to the consolidation of Shenzhen Airlines and construction of fixed assets incurred during the current reporting period as compared with the same period of the previous year. The Group recorded a net cash inflow from financing activities of RMB716 million, representing a decrease of RMB288 million from RMB1,004 million for the same period in 2009, primarily due to relatively more debt repayments made by the Group during the current reporting period. The Group's net increase in cash and cash equivalents for the first half of 2010 was RMB2,583 million, representing an increase of approximately RMB2,348 million from the same period in 2009. The Company obtained bank facilities up to RMB122,421 million from a number of banks in the PRC, of which approximately RMB49,741 million was utilised, and the remaining portion is fully capable of meeting the working capital requirements and future capital commitments of the Company.

## OBJECTIVES AND POLICIES OF FINANCIAL RISKS MANAGEMENT

The Group is exposed to the risk of fluctuations in jet fuel prices in its daily operation. International jet fuel prices have historically, and will continue to be, subject to market volatility and fluctuations in supply and demand. The Group's strategy for managing jet fuel price risk aims to protect itself against sudden and significant price increases. The Group has been engaging in fuel hedging transactions since March 2001. The hedging instruments used are mainly derivatives of Singapore kerosene together with Brent crude oil and New York crude oil, which are closely linked to the price of jet fuel. Considering the high volatility of international fuel prices and its high sensitivity towards the Company's cost, the Company will continue to utilise the hedging instruments to manage and control the risk in relation to rising fuel prices.

As at 30 June 2010, the total amount of interest-bearing debts of the Group were RMB85,814 million, accounting for 74.43% of the Group's total liabilities, most of which were foreign debts and mainly denominated in US dollars and Hong Kong dollars. In addition, the Group also had revenue and expenses denominated in foreign currencies. The Group endeavoured to minimise any risks relating to the fluctuation in interest rates and exchange rates primarily by adjusting the structure of the interest rates and currency denomination of its debts and by making use of financial derivatives.

# Significant Events

## ANTITRUST INVESTIGATION

On 26 February 2007, the Eastern District Court of New York of the US Federal Courts issued summons to the Company and Air China Cargo in connection with the antitrust civil case relating to the air cargo services. Pursuant to such summons, various airlines, including the Company and Air China Cargo, were sued for their breach of the US Antitrust Law on the ground that these airlines were acting in concert in imposing excessive surcharges so as to impede the offering of discount that would be made available for the prices charged for air cargo services and that these airlines had reached an agreement on the allocation of revenues and consumers so as to achieve such purposes as setting, increasing, maintaining or stabilising the air cargo prices. Currently, the case is in the course of presenting evidence. Our Directors believe that at the present stage, they are unable to make a reasonable and reliable estimate of the outcome of the case, and therefore, no provision has been made for such litigation for the time being.

# Change in Particulars of Directors and Supervisors

| | | | |
|---|---|---|---|
| 1. | Chen Nan Lok, Philip | : | resigned as a Director of the Company with effect from 1 July 2010. |
| 2. | Fan Cheng | : | served as secretary of the Communist Party Committee of Shenzhen Airlines from December 2009 to March 2010, as chairman, secretary of the Communist Party Committee and acting president of Shenzhen Airlines from March 2010 to April 2010, and as chairman and secretary of the Communist Party Committee of Shenzhen Airlines from April 2010 to May 2010. |
| 3. | Cai Jianjiang | : | has been chairman of Shenzhen Airlines since May 2010. |

## (I) DISCLOSURE OF INTERESTS OF DIRECTORS, SUPERVISORS AND CHIEF EXECUTIVE

As at 30 June 2010, none of the Directors, supervisors or chief executive of the Company had interests or short positions in the shares, underlying shares and/or debentures (as the case may be) of the Company or any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) that is required to be recorded and kept in the register under Section 352 of the SFO, or which were notifiable to the Company and the Hong Kong Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code").

Mr. Christopher Dale Pratt is a non-executive Director of the Company and is concurrently the chairman and executive director of Cathay Pacific, which is a substantial shareholder of the Company and wholly owns Hong Kong Dragonair Airlines Limited ("Dragonair"). Mr. Kong Dong, the chairman and a non-executive Director of the Company, and Mr. Cai Jianjiang and Mr. Fan Cheng, both executive Directors of the Company, are concurrently non-executive directors of Cathay Pacific. Cathay Pacific and Dragonair compete or are likely to compete either directly or indirectly with some aspects of the business of the Company as they operate airline services to certain destinations, which are also served by the Company.

Save as above, none of the Directors or supervisors of the Company and their respective associates (as defined in the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited (the "Listing Rules")) has any competing interests which would be required to be disclosed under Rule 8.10 of the Listing Rules if each of them were a controlling shareholder of the Company.

## (II) SUBSTANTIAL SHAREHOLDERS' SIGNIFICANT INTERESTS IN THE COMPANY

As at 30 June 2010, to the best knowledge of the Directors, supervisors and chief executive of the Company, the interests and short positions of the persons (other than a Director, supervisor or chief executive of the Company) in the shares and underlying shares of the Company as recorded in the register required to be kept under section 336 of the SFO were as follows:

| Name | Type of Interests | Type and number of shares held in the Company | Percentage of the total issued shares of the Company | Percentage of the total issued A shares of the Company | Percentage of the total issued H shares of the Company | Short position |
|---|---|---|---|---|---|---|
| China National Aviation Holding Company ("CNAHC") | Beneficial owner | 4,949,066,567 A shares | 40.40% | 63.08% | – | – |
| CNAHC [1] | Attributable interests | 1,332,482,920 A shares | 10.88% | 16.98% | – | – |
| CNAHC [1] | Attributable interests | 66,852,000 H shares | 0.54% | – | 1.52% | – |
| China National Aviation Corporation (Group) Limited ("CNACG") | Beneficial owner | 1,332,482,920 A shares | 10.88% | 16.98% | – | – |

# Shareholdings of Directors, Supervisors and Chief Executive and Substantial Shareholders of the Company

| Name | Type of Interests | Type and number of shares held in the Company | Percentage of the total issued shares of the Company | Percentage of the total issued A shares of the Company | Percentage of the total issued H shares of the Company | Short position |
|---|---|---|---|---|---|---|
| CNACG | Beneficial owner | 66,852,000 H shares | 0.55% | – | 1.52% | – |
| Cathay Pacific | Beneficial owner | 2,350,187,455 H shares | 19.18% | – | 53.34% | – |
| Swire Pacific Limited (2) | Attributable interests | 2,350,187,455 H shares | 19.18% | – | 53.34% | – |
| John Swire & Sons Limited (2) | Attributable interests | 2,350,187,455 H shares | 19.18% | – | 53.34% | – |
| John Swire & Sons (H.K.) Limited (2) | Attributable interests | 2,350,187,455 H shares | 19.18% | – | 53.34% | – |
| BlackRock, Inc. (3) | Attributable interests | 254,954,798 H shares | 2.08% | – | 5.79% | 9,552,398 H shares |

*Note:*

Based on the information available to the Directors, supervisors and chief executive of the Company (including such information as was available on the website of the Stock Exchange) and so far as the Directors, supervisors and chief executive are aware, as at 30 June 2010:

1. By virtue of CNAHC's 100% interest in CNACG, CNAHC is deemed to be interested in the 1,332,482,920 A shares and 66,852,000 H shares of the Company directly held by CNACG.

2. By virtue of John Swire & Sons Limited's 100% interest in John Swire & Sons (H.K.) Limited and their approximately 40.07% equity interest and 57.25% voting rights in Swire Pacific Limited, and Swire Pacific Limited's approximately 41.97% interest in Cathay Pacific as at 30th June 2010, John Swire & Sons Limited, John Swire & Sons (H.K.) Limited and Swire Pacific Limited are deemed to be interested in the 2,350,187,455 H shares of the Company directly held by Cathay Pacific.

3. BlackRock, Inc., through its controlled entities, had an attributable interest in 254,954,798 H shares of the Company and maintained a short position of 9,552,398 H shares of the Company, out of which BlackRock Investment Management, LLC. directly held 1,116,000 H shares of the Company, BlackRock Institutional Trust Company, N.A. directly held 19,412,000 H shares of the Company, BlackRock Asset Management Canada Limited directly held 48,000 H shares of the Company, BlackRock Asset Management Australia Limited directly held 144,000 H shares of the Company, BlackRock Asset Management Japan Limited directly held 470,000 H shares of the Company, BlackRock Asset Management North Asia Limited directly held 1,920,000 H shares of the Company and maintained a short position of 1,920,000 H shares of the Company, BlackRock International Ltd. directly held 476,400 H share of the Company, BlackRock Fund Managers directly held 120,000 H shares of the Company, BlackRock Fund Advisors directly held 193,462,000 H shares of the Company and BlackRock Advisors UK Ltd. directly held 37,786,398 H shares of the Company and maintained a short position of 7,632,398 H shares of the Company.

# Corporate Governance

## 1. COMPLIANCE WITH THE CODE ON CORPORATE GOVERNANCE PRACTICES

The Company has complied with the code provisions set out in the Code on Corporate Governance Practices contained in Appendix 14 to the Listing Rules throughout the six months ended 30 June 2010.

## 2. COMPLIANCE WITH THE MODEL CODE

After making specific enquiries, the Company confirmed that each Director and each supervisor of the Company have complied with the required standards of the Model Code as set out in Appendix 10 of the Listing Rules throughout the six months ended 30 June 2010.

# Miscellaneous

## 1. PURCHASE, SALE OR REDEMPTION OF SECURITIES

Neither the Company nor any of its subsidiaries had purchased, sold or redeemed any of the listed securities of the Company in the first half of 2010.

## 2. PUBLIC FLOAT

Pursuant to public information available to the Company and to the best knowledge of the Directors of the Company, during the reporting period, the Company has maintained a public float as required by the Listing Rules and agreed by the Hong Kong Stock Exchange throughout the period under review.

## 3. INTERIM DIVIDEND

No interim dividend will be paid for the six months ended 30 June 2010.

## 4. REVIEW BY AUDIT AND RISK CONTROL COMMITTEE

The audit and risk control committee of the Company has reviewed the interim report for the six months ended 30 June 2010 and the Company's unaudited interim condensed consolidated financial statements and the accounting policies and practices adopted by the Group.

# Independent Auditors' Report

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安永

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To the shareholders of
**Air China Limited**
*(Established in the People's Republic of China with limited liability)*

We have reviewed the interim financial information of Air China Limited (the "Company"), its subsidiaries and joint ventures (collectively the "Group") set out on pages 26 to 56 which comprises the Group's interim condensed consolidated statement of financial position as at 30 June 2010 and the related interim condensed consolidated statements of income, comprehensive income, changes in equity and cash flows for the six months then ended, and explanatory notes. The Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited require the preparation of a report on interim financial information to be in compliance with the relevant provisions thereof and International Accounting Standard 34 "Interim Financial Reporting" ("IAS 34") issued by the International Accounting Standards Board.

The Directors are responsible for the preparation and presentation of this interim financial information in accordance with IAS 34. Our responsibility is to express a conclusion on this interim financial information based on our review. Our report is made solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

## SCOPE OF REVIEW

We conducted our review in accordance with International Standard on Review Engagements 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity". A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing. Consequently, it does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

## CONCLUSION

Based on our review, nothing has come to our attention that causes us to believe that the interim financial information is not prepared, in all material respects, in accordance with IAS 34.

**Ernst & Young**
*Certified Public Accountants*

Hong Kong
25 August 2010

# Interim Condensed Consolidated Income Statement

For the six months ended 30 June 2010
(Prepared under International Financial Reporting Standards)

| | Notes | For the six months ended 30 June 2010 RMB'000 (Unaudited) | 30 June 2009 RMB'000 (Unaudited) |
|---|---|---|---|
| **TURNOVER** | | | |
| Air traffic revenue | 4 | **33,089,570** | 21,209,451 |
| Other operating revenue | 5 | **1,691,405** | 1,900,288 |
| | | **34,780,975** | 23,109,739 |
| **OPERATING EXPENSES** | | | |
| Jet fuel costs | | **(10,612,980)** | (6,098,289) |
| Movements in fair value of derivative contracts | | **720,801** | 1,449,791 |
| Take-off, landing and depot charges | | **(3,559,424)** | (2,706,284) |
| Depreciation | | **(4,005,588)** | (3,405,580) |
| Aircraft maintenance, repairs and overhaul costs | | **(1,038,642)** | (879,252) |
| Employee compensation costs | | **(4,150,838)** | (2,936,752) |
| Air catering charges | | **(853,590)** | (694,285) |
| Aircraft and engine operating lease expenses | | **(1,495,065)** | (1,139,662) |
| Other operating lease expenses | | **(766,736)** | (235,418) |
| Other flight operation expenses | | **(2,654,431)** | (1,959,590) |
| Selling and marketing expenses | | **(1,796,598)** | (1,322,048) |
| General and administrative expenses | | **(466,681)** | (362,105) |
| | | **(30,679,772)** | (20,289,474) |
| **PROFIT FROM OPERATIONS** | 6 | **4,101,203** | 2,820,265 |
| **Finance revenue** | 7 | **294,561** | 260,215 |
| **Finance costs** | 7 | **(648,846)** | (729,335) |
| **Share of profits of associates** | | **1,718,893** | 315,720 |
| **PROFIT BEFORE TAX** | | **5,465,811** | 2,666,865 |
| **Tax** | 8 | **(755,746)** | 150,384 |
| **PROFIT FOR THE PERIOD** | | **4,710,065** | 2,817,249 |
| **Attributable to:** | | | |
| Owners of the parent | | **4,612,900** | 2,878,224 |
| Non-controlling interests | | **97,165** | (60,975) |
| | | **4,710,065** | 2,817,249 |
| **Earnings per share attributable to equity holders of the parent:** | 10 | | |
| Basic | | **39.8 cents** | 24.3 cents |
| Diluted | | **N/A** | N/A |

# Interim Condensed Consolidated Statement of Comprehensive Income

For the six months ended 30 June 2010
(Prepared under International Financial Reporting Standards)

| | For the six months ended | |
|---|---|---|
| | **30 June 2010** | 30 June 2009 |
| | ***RMB'000*** | *RMB'000* |
| | **(Unaudited)** | (Unaudited) |
| **PROFIT FOR THE PERIOD** | **4,710,065** | 2,817,249 |
| Share of other comprehensive income of associates | **550** | 36,106 |
| Exchange realignment | **(145,548)** | (13,176) |
| Others | **–** | (3,000) |
| **OTHER COMPREHENSIVE INCOME/(LOSS) FOR THE PERIOD, NET OF TAX** | **(144,998)** | 19,930 |
| **TOTAL COMPREHENSIVE INCOME FOR THE PERIOD, NET OF TAX** | **4,565,067** | 2,837,179 |
| **Attributable to:** | | |
| Owners of the parent | **4,467,995** | 2,899,200 |
| Non-controlling interests | **97,072** | (62,021) |
| | **4,565,067** | 2,837,179 |

# Interim Condensed Consolidated Statement of Financial Position

At 30 June 2010

(Prepared under International Financial Reporting Standards)

| | Notes | 30 June 2010 RMB'000 (Unaudited) | 31 December 2009 RMB'000 (Audited) |
|---|---|---|---|
| **NON-CURRENT ASSETS** | | | |
| Property, plant and equipment | 11 | **95,214,981** | 75,044,870 |
| Lease prepayments | 12 | **2,044,358** | 1,954,819 |
| Intangible asset | | **47,477** | 49,267 |
| Goodwill | | **1,651,165** | 346,845 |
| Interests in associates | | **13,341,065** | 12,187,230 |
| Advance payments for aircraft and related equipment | | **13,509,848** | 7,715,409 |
| Deposits for aircraft under operating leases | | **383,306** | 253,815 |
| Long term receivable from ultimate holding company | | **81,813** | 131,813 |
| Available-for-sale investments | | **37,182** | 1,997 |
| Deferred tax assets | | **1,913,701** | 1,656,453 |
| | | **128,224,896** | 99,342,518 |
| **CURRENT ASSETS** | | | |
| Aircraft and flight equipment held for sale | | **74,123** | 130,814 |
| Inventories | | **1,504,273** | 1,384,706 |
| Accounts receivable | 13 | **3,196,936** | 2,054,265 |
| Bills receivable | | **4,705** | 2,489 |
| Prepayments, deposits and other receivables | 14 | **2,378,667** | 1,230,794 |
| Derivative financial instruments | 15 | **3,766** | – |
| Financial assets held for trading | | **19,307** | – |
| Due from the ultimate holding company | | **427,387** | 461,147 |
| Due from related companies | | **5,407** | 10,194 |
| Tax recoverable | | **–** | 4,840 |
| Pledged deposits | 16 | **1,577,971** | 564,747 |
| Cash and cash equivalents | 16 | **5,674,461** | 2,706,758 |
| | | **14,867,003** | 8,550,754 |
| **TOTAL ASSETS** | | **143,091,899** | 107,893,272 |
| **CURRENT LIABILITIES** | | | |
| Air traffic liabilities | | **(3,564,604)** | (2,434,353) |
| Accounts payable | 17 | **(8,298,352)** | (6,045,733) |
| Bills payable | | **(325,401)** | (763,255) |
| Other payables and accruals | 18 | **(8,264,642)** | (4,645,406) |
| Derivative financial instruments | 15 | **(1,678,477)** | (2,274,627) |
| Due to related companies | | **(87,864)** | (113,024) |
| Tax payable | | **(545,886)** | (39,073) |
| Obligations under finance leases | | **(3,467,353)** | (3,454,233) |
| Interest-bearing bank and other borrowings | | **(24,940,927)** | (17,160,442) |
| Provision for major overhauls | | **(449,644)** | (268,418) |
| | | **(51,623,150)** | (37,198,564) |
| **NET CURRENT LIABILITIES** | | **(36,756,147)** | (28,647,810) |
| **TOTAL ASSETS LESS CURRENT LIABILITIES** | | **91,468,749** | 70,694,708 |

# Interim Condensed Consolidated Statement of Financial Position

At 30 June 2010

(Prepared under International Financial Reporting Standards)

| | *Notes* | **30 June 2010** ***RMB'000*** **(Unaudited)** | 31 December 2009 *RMB'000* (Audited) |
|---|---|---|---|
| **NON-CURRENT LIABILITIES** | | | |
| Obligations under finance leases | | **(15,910,784)** | (15,366,475) |
| Interest-bearing bank loans, other borrowings and corporate bonds | | **(41,169,025)** | (27,321,078) |
| Provision for major overhauls | | **(2,058,959)** | (1,318,708) |
| Provision for early retirement benefit obligations | | **(230,726)** | (210,006) |
| Long term payables | | **(264,416)** | (180,420) |
| Deferred income | | **(3,108,436)** | (2,105,554) |
| Deferred tax liabilities | | **(932,020)** | (238,000) |
| | | **(63,674,366)** | (46,740,241) |
| **NET ASSETS** | | **27,794,383** | 23,954,467 |
| **EQUITY ATTRIBUTABLE TO OWNERS OF THE PARENT** | | | |
| Issued capital | *19* | **12,251,362** | 12,251,362 |
| Treasury shares | *20* | **(2,593,276)** | (2,319,879) |
| Reserves | | **18,452,281** | 13,984,413 |
| | | **28,110,367** | 23,915,896 |
| **NON-CONTROLLING INTERESTS** | | **(315,984)** | 38,571 |
| **TOTAL EQUITY** | | **27,794,383** | 23,954,467 |

# Interim Condensed Consolidated Statement of Changes in Equity

For the six months ended 30 June 2010

(Prepared under International Financial Reporting Standards)

| | Attributable to owners of the parent | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Issued capital RMB'000 | Treasury shares RMB'000 | Capital reserve RMB'000 | Reserve funds RMB'000 | Foreign exchange translation reserve RMB'000 | Retained earnings RMB'000 | Total RMB'000 | Non-controlling interests RMB'000 | Total equity RMB'000 |
| (Unaudited) | | | | | | | | | |
| At 1 January 2010 | **12,251,362** | **(2,319,879)** | **12,542,326*** | **1,615,700*** | **(1,624,408)*** | **1,450,795*** | **23,915,896** | **38,571** | **23,954,467** |
| Profit for the period | **–** | **–** | **–** | **–** | **–** | **4,612,900** | **4,612,900** | **97,165** | **4,710,065** |
| Other comprehensive income | **–** | **–** | **550** | **–** | **(145,455)** | **–** | **(144,905)** | **(93)** | **(144,998)** |
| Total comprehensive income | **–** | **–** | **550** | **–** | **(145,455)** | **4,612,900** | **4,467,995** | **97,072** | **4,565,067** |
| Acquisition of additional interest in an associate | **–** | **–** | **(127)** | **–** | **–** | **–** | **(127)** | **(433,077)** | **(433,204)** |
| Elimination of reciprocal shareholding | **–** | **(273,397)** | **–** | **–** | **–** | **–** | **(273,397)** | **–** | **(273,397)** |
| Acquisition of non-controlling interest in a subsidiary | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **(18,550)** | **(18,550)** |
| **At 30 June 2010** | **12,251,362** | **(2,593,276)** | **12,542,749*** | **1,615,700*** | **(1,769,863)*** | **6,063,695*** | **28,110,367** | **(315,984)** | **27,794,383** |
| (Unaudited) | | | | | | | | | |
| At 1 January 2009 | 12,251,362 | (1,353,714) | 12,428,995 | 1,615,700 | (1,596,052) | (3,403,439) | 19,942,852 | 513,654 | 20,456,506 |
| Profit for the period | – | – | – | – | – | 2,878,224 | 2,878,224 | (60,975) | 2,817,249 |
| Other comprehensive income | – | – | 33,106 | – | (12,130) | – | 20,976 | (1,046) | 19,930 |
| Total comprehensive income | – | – | 33,106 | – | (12,130) | 2,878,224 | 2,899,200 | (62,021) | 2,837,179 |
| Acquisition of additional interest in an associate | – | – | – | – | – | – | – | 15,940 | 15,940 |
| At 30 June 2009 | 12,251,362 | (1,353,714) | 12,462,101 | 1,615,700 | (1,608,182) | (525,215) | 22,842,052 | 467,573 | 23,309,625 |

* The aggregate of these reserve accounts represents the consolidated reserves of RMB18,452,281,425 (31 December 2009: RMB13,984,413,141) on the interim condensed consolidated statement of financial position.

# Interim Condensed Consolidated Statement of Cash Flows

For the six months ended 30 June 2010
(Prepared under International Financial Reporting Standards)

| | Note | For the six months ended 30 June 2010 RMB'000 (Unaudited) | 30 June 2009 RMB'000 (Unaudited) |
|---|---|---|---|
| Net cash inflow from operating activities | | **6,908,593** | 1,188,535 |
| Net cash outflow from investing activities | | **(5,041,237)** | (1,957,533) |
| Net cash inflow from financing activities | | **715,693** | 1,003,953 |
| **NET INCREASE IN CASH AND CASH EQUIVALENTS** | | **2,583,049** | 234,955 |
| Cash and cash equivalents at beginning of period | | **2,676,309** | 2,949,062 |
| Effect of exchange rate changes on cash and cash equivalents | | **(46,787)** | (19,032) |
| **CASH AND CASH EQUIVALENTS AT END OF PERIOD** | | **5,212,571** | 3,164,985 |
| **ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS** | | | |
| Cash and bank balances | *16* | **3,962,058** | 2,103,016 |
| Non-pledged time deposits with original maturity of less than three months when acquired | *16* | **1,250,513** | 1,061,969 |
| | | **5,212,571** | 3,164,985 |

## 1. CORPORATE INFORMATION

Air China Limited (the "Company") was incorporated as a joint stock limited company in Beijing, the People's Republic of China (the "PRC"), on 30 September 2004. The Company's H shares are listed on the Hong Kong Stock Exchange (the "HKSE") and the London Stock Exchange (the "LSE") while the Company's A shares are listed on the Shanghai Stock Exchange. In the opinion of the Directors, the Company's parent and ultimate holding company is China National Aviation Holding Company ("CNAHC"), a PRC state-owned enterprise under the supervision of the State Council.

On 3 February 2010, the Company and Engine Support Holdings ("ESH", a wholly-owned subsidiary of CFM International Inc.) entered into an agreement, pursuant to which the Company agreed to acquire and ESH agreed to sell approximately 16.36% equity interest in Sichuan Snecma Aero-engine Maintenance Co., Ltd ("SNECMA", a 43.64% owned associate of the Company before the transaction). Upon completion of the transaction, the equity interests held by the Company in SNECMA will become 60%. At 30 June 2010, this transaction was not yet completed and was pending for approval by the Ministry of Commerce of the PRC. The Company and ESH also agreed to make additional capital contribution in cash of approximately USD40 million to SNECMA in proportion to their shareholding. Upon completion of the additional capital injection, the registered capital of SNECMA will increase to approximately USD72 million.

On 25 February 2010, the Company, Fine Star Enterprises Corporation ("Fine Star", a wholly-owned subsidiary of the Company), Air China Cargo Co., Ltd ("Air China Cargo", another wholly-owned subsidiary of the Company), Cathay Pacific Airways Limited ("Cathay Pacific") and Cathay Pacific China Cargo Holdings Limited ("Cathay Pacific Cargo", a wholly-owned subsidiary of Cathay Pacific), entered into a framework agreement and several related agreements, pursuant to which Cathay Pacific, through Cathay Pacific Cargo, agreed to subscribe for a 25% equity interest in Air China Cargo for a consideration of approximately RMB852 million and the Company, through Fine Star, agreed to make additional capital contribution of approximately RMB238 million in cash to Air China Cargo; and Air China agreed to sell the entire equity interest in Air China Cargo held by Fine Star to Advent Fortune Limited ("AFL") for a consideration of approximately RMB627 million. Upon completion of these transactions, the equity interests held by the Company, Cathay Pacific and AFL will become 51%, 25% and 24%, respectively. At 30 June 2010, these transactions were not yet completed and were pending for approval by the National Development and Reform Commission of the PRC.

On 11 March 2010, the Company's board of directors passed a resolution to convene an extraordinary general meeting for the grant of specific mandates to issue not more than 585,000,000 new A shares to not more than 10 specific investors including CNAHC at a subscription price of not less than RMB9.58 each; and issue not more than 157,000,000 new H shares to China National Aviation Corporation (Group) Ltd. ("CNACG", a wholly-owned subsidiary of CNAHC) at a subscription price of not less than HK$6.62 each. On the same date, CNAHC entered into another agreement with the Company pursuant to which CNAHC will commit at least RMB1,500 million to subscribe in cash for not more than 157,000,000 new A shares at a subscription price of not less than RMB9.58 each; and CNACG entered into another agreement with the Company pursuant to which CNACG will subscribe in cash for not more than 157,000,000 new H shares at a subscription price of not less than HK$6.62 each. The subscription of the new A shares by CNAHC and the subscription of the new H shares by CNACG are inter-conditional. At 30 June 2010, the issuance of the new A shares and H shares was not yet completed.

On 21 March 2010, the Company, Shenzhen International Total Logistics (Shenzhen) Co., Ltd. ("Total Logistics") and Shenzhen Huirun Investment Co., Ltd. ("Huirun") entered into an agreement, pursuant to which the Company and Total Logistics agreed to make an aggregate capital contribution of approximately RMB1,030 million to Shenzhen Airlines Company Limited ("Shenzhen Airlines", a 25% owned associate of the Company before the transaction), of which the Company will contribute approximately RMB682 million and Total Logistics will contribute approximately RMB348 million. The transaction was completed on April 19 2010 and upon the completion of the transaction the Company's equity interest in Shenzhen Airlines increased from 25% to 51%.

The principal activities of the Company, its subsidiaries and joint ventures (collectively the "Group") and associates consist of the provision of airline services and airline-related services (including aircraft engineering services and airport ground handling services) mainly in Mainland China, Hong Kong and Macau.

The registered office of the Company is located at 9th Floor, Blue Sky Mansion, 28 Tianzhu Road, Zone A, Tianzhu Airport Industrial Zone, Shunyi District, Beijing 101312, the PRC.

## 2. BASIS OF PREPARATION AND ACCOUNTING POLICIES

### Basis of preparation

The interim condensed consolidated financial statements of the Group for the six months ended 30 June 2010 have been prepared in accordance with International Accounting Standard 34 "Interim Financial Reporting" and the disclosure requirements of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

At 30 June 2010, the Group's net current liabilities amounted to approximately RMB36,756 million, which comprised current assets of approximately RMB14,867 million and current liabilities of approximately RMB51,623 million. The liquidity of the Group is primarily dependent on its ability to maintain adequate cash inflows from operations and sufficient financing to meet its financial obligations as and when they fall due. In preparing the interim condensed consolidated financial statements for the six months ended 30 June 2010, the Directors of the Company have considered the Group's sources of liquidity and believe that adequate funding is available to fulfill the Group's debt obligations and capital expenditure requirements. Accordingly, the interim condensed consolidated financial statements have been prepared on a basis that the Group will be able to continue as a going concern.

The interim condensed consolidated financial statements do not include all the information and disclosures required in annual financial statements, and therefore should be read in conjunction with the Group's annual financial statements for the year ended 31 December 2009.

### Significant accounting policies

The principal accounting policies adopted in the preparation of the interim condensed consolidated financial statements of the Group are consistent with those followed in the preparation of the audited annual financial statements of the Group for the year ended 31 December 2009, except for the adoption of the following new International Financial Reporting Standards ("IFRSs", 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).

| | |
|---|---|
| IFRS 1 (Revised) | *First-time Adoption of IFRSs* |
| IFRS 1 Amendments | Amendments to IFRS 1 *First-time Adoption of International Financial Reporting Standards – Additional Exemptions for First-time Adopters* |
| IFRS 2 Amendments | Amendments to IFRS 2 *Share-based Payment – Group Cash-settled Share-based Payment Transactions* |
| IFRS 3 (Revised) | *Business Combinations* |
| IAS 27 (Revised) | *Consolidated and Separate Financial Statements* |
| IAS 39 Amendment | Amendment to IAS 39 *Financial Instruments Recognition and Measurement – Eligible Hedged Items* |
| IFRIC 17 | *Distributions of Non-cash Assets to Owners* |
| Amendments to IFRS 5 included in *Improvements to IFRSs* issued in May 2008 | Amendments to IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations – Plan to sell the controlling interest in a subsidiary* |

Improvements to IFRSs (issued in April 2009)

## 2. BASIS OF PREPARATION AND ACCOUNTING POLICIES (continued)

### Significant accounting policies (continued)

(a) IFRS 1 (Revised) *First-time Adoption of IFRSs*

IFRS 1 (Revised) was issued with an aim to improve the structure of the standard. The revised version of the standard does not make any changes to the substance of accounting by first-time adopters. As the Group is not a first-time adopter of IFRSs, the amendments did not have any financial impact on the Group.

(b) Amendments to IFRS 1 *First-time Adoption of International Financial Reporting Standards – Additional Exemptions for First-time Adopters*

The IFRS 1 Amendments provide relief from the full retrospective application of IFRSs for the measurement of oil and gas assets and leases. As a result of extending the options for determining deemed cost to oil and gas assets, the existing exemption relating to decommissioning liabilities has also been revised. As the Group is not a first-time adopter of IFRSs, the amendments did not have any financial impact on the Group.

(c) Amendments to IFRS 2 *Share-based Payment – Group Cash-settled Share-based Payment Transactions*

The IFRS 2 Amendments provide guidance on how to account for cash-settled share-based payment transactions in the separate financial statements of the entity receiving the goods and services when the entity has no obligation to settle the share-based payment transactions. The amendments also incorporate guidance that was previously included in IFRIC 8 *Scope of IFRS 2* and IFRIC 11 *IFRS 2 – Group and Treasury Share Transactions*. The amendments did not have any significant implications on the Group's accounting for share-based payments.

(d) IFRS 3 (Revised) *Business Combinations*

IFRS 3 (Revised) introduces a number of changes in the accounting for business combinations. The changes affect the valuation of non-controlling interests, the accounting for transaction costs, the initial recognition and subsequent measurement of a contingent consideration and business combination achieved in stages. During the period, the Company acquired additional equity interest in Shenzhen Airlines and achieved business combination in stages. These changes by IFRS 3 (Revised) had an impact on the amount of goodwill recognised, the reported results of the Group in the period, detail of which are set out in note 22 to the financial statements.

(e) IAS 27 (Revised) *Consolidated and Separate Financial Statements*

IAS 27 (Revised) requires that a change in the ownership interest of a subsidiary without loss of control is accounted for as an equity transaction. Therefore, such a change has had no impact on goodwill, nor has it given rise to a gain or loss. Furthermore, the revised standard changes the accounting for losses incurred by the subsidiary as well as the loss of control of a subsidiary. Other consequential amendments were made to IAS 7 *Statement of Cash Flows*, IAS 12 *Income Taxes*, IAS 21 *The Effects of Changes in Foreign Exchange Rates*, IAS 28 *Investments in Associates* and IAS 31 *Interests in Joint Ventures*. The changes by IAS 27 (Revised) will affect future loss of control of subsidiaries and transactions with non-controlling interests.

(f) Amendment to IAS 39 Financial Instruments: *Recognition and Measurement – Eligible Hedged Items*

The IAS 39 Amendment addresses the designation of a one-sided risk in a hedged item, and the designation of inflation as a hedged risk or portion in particular situations. It clarifies that an entity is permitted to designate a portion of the fair value changes or cash flow variability of a financial instrument as a hedged item. As the Group has not entered into any such hedges, the amendment did not have any financial impact on the Group.

## 2. BASIS OF PREPARATION AND ACCOUNTING POLICIES (continued)

### Significant accounting policies (continued)

(g) IFRIC 17 *Distributions of Non-cash Assets to Owners*

IFRIC 17 standardises practice in the accounting for non-reciprocal distributions of non-cash assets to owners. The interpretation clarifies that (i) a dividend payable should be recognised when the dividend is appropriately authorised and is no longer at the discretion of the entity; (ii) an entity should measure the dividend payable at the fair value of the net assets to be distributed; and (iii) an entity should recognise the difference between the dividend paid and the carrying amount of the net assets distributed in profit or loss. Other consequential amendments were made to IAS 10 *Events after the Reporting Period* and IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*. While the adoption of the interpretation resulted in changes in certain accounting policies, the interpretation did not have any material financial impact on the Group.

(h) Amendments to IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations – Plan to sell the controlling interest in a subsidiary*

The amendments to IFRS 5 clarify that all assets and liabilities of a subsidiary should be classified as held for sale if an entity has a sale plan involving loss of control of the subsidiary, regardless of whether the entity will retain a non-controlling interest. The changes must be applied prospectively and did not have any material financial impact on the Group.

(i) *Improvements to IFRSs 2009* issued in April 2009 sets out amendments to a number of IFRSs, primarily with a view to removing inconsistencies and clarifying wording. There are separate transitional provisions for each standard. While the adoption of some of the amendments resulted in changes in accounting policies, these amendments had no significant financial impact on the Group.

## 3. SEGMENT INFORMATION

The Group's operating businesses are structured and managed separately according to the nature of their operations and the services they provide. The Group has the following reportable operating segments:

(a) the "airline operations" segment which comprises the provision of air passenger and air cargo services; and

(b) the "others" segment which comprises the provision of aircraft engineering, ground services and other airline-related services.

In determining the Group's geographical segments, revenue is attributed to the segments based on the origin and destination of each flight. Assets, which consist principally of aircraft and flight equipment supporting the Group's worldwide transportation network, are mainly located in Mainland China. An analysis of assets of the Group by geographical distribution has therefore not been included in the interim condensed consolidated financial statements.

Intersegment sales and transfers are transacted with reference to the selling prices used for sales made to third parties at the then prevailing market prices.

### Operating segments

The following tables present the Group's consolidated revenue and profit before tax under China Accounting Standards for Business Enterprises ("CAS") by operating segment for the six months ended 30 June 2010 and 2009:

**For the six months ended 30 June 2010**

| **(Unaudited)** | **Airline Operations** *RMB'000* | **Others** *RMB'000* | **Eliminations** *RMB'000* | **Total** *RMB'000* |
|---|---|---|---|---|
| **REVENUE** | | | | |
| Sales to external customers | **34,270,125** | **37,548** | **–** | **34,307,673** |
| Intersegment sales | **–** | **359,907** | **(359,907)** | **–** |
| Total revenue | **34,270,125** | **397,455** | **(359,907)** | **34,307,673** |
| **SEGMENT PROFIT BEFORE TAX** | **5,492,425** | **66,832** | **–** | **5,559,257** |

For the six months ended 30 June 2009

| (Unaudited) | Airline Operations *RMB'000* | Others *RMB'000* | Eliminations *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|
| **REVENUE** | | | | |
| Sales to external customers | 22,362,259 | 42,766 | – | 22,405,025 |
| Intersegment sales | – | 222,412 | (222,412) | – |
| Total revenue | 22,362,259 | 265,178 | (222,412) | 22,405,025 |
| **SEGMENT PROFIT BEFORE TAX** | 2,683,613 | 46,562 | – | 2,730,175 |

## 3. SEGMENT INFORMATION (continued)

### Operating segments (continued)

The following tables present the segment assets of the Group's operating segments under the CAS as at 30 June 2010 and 31 December 2009:

| | Airline Operations *RMB'000* | Others *RMB'000* | Eliminations *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|
| **SEGMENT ASSETS** | | | | |
| **As at 30 June 2010 (Unaudited)** | **138,597,124** | **2,383,431** | **(1,402,215)** | **139,578,340** |
| As at 31 December 2009 (Audited) | 105,239,001 | 2,367,196 | (1,442,990) | 106,163,207 |

The following tables present the reconciliations of reportable segment revenue, profit before tax and assets to the Group's interim condensed consolidated amounts:

| | **For the six months ended** | |
|---|---|---|
| | **30 June 2010** ***RMB'000*** **(Unaudited)** | 30 June 2009 *RMB'000* (Unaudited) |
| **REVENUE** | | |
| Total revenue for reportable segments | **34,307,673** | 22,405,025 |
| Business tax not included in segment revenue | **(671,630)** | (543,663) |
| Other income not included in segment revenue | **420,915** | 991,644 |
| Effects of differences between IFRSs and CAS | **724,017** | 256,733 |
| Revenue for the period | **34,780,975** | 23,109,739 |
| **PROFIT BEFORE TAX** | | |
| Total profit before tax for reportable segments | **5,559,257** | 2,730,175 |
| Effects of differences between IFRSs and CAS | **(93,446)** | (63,310) |
| Profit before tax for the period | **5,465,811** | 2,666,865 |

| | **30 June 2010** ***RMB'000*** **(Unaudited)** | 31 December 2009 *RMB'000* (Audited) |
|---|---|---|
| **ASSETS** | | |
| Total assets for reportable segments | **139,578,340** | 106,163,207 |
| Effects of differences between IFRSs and CAS | **3,513,559** | 1,730,065 |
| Total assets | **143,091,899** | 107,893,272 |

## 3. SEGMENT INFORMATION (continued)

### Geographical segments

The following tables present the Group's consolidated revenue under IFRSs by geographical segment for the six months ended 30 June 2010 and 2009:

**For the six months ended 30 June 2010**

| (Unaudited) | Mainland China RMB'000 | Hong Kong, Macau and Taiwan RMB'000 | Europe RMB'000 | North America RMB'000 | Japan and Korea RMB'000 | Asia Pacific and others RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|---|
| **REVENUE** | | | | | | | |
| Sales to external customers and total revenue | **20,445,640** | **2,057,114** | **4,436,706** | **3,024,711** | **2,806,724** | **2,010,080** | **34,780,975** |

For the six months ended 30 June 2009

| (Unaudited) | Mainland China RMB'000 | Hong Kong, Macau and Taiwan RMB'000 | Europe RMB'000 | North America RMB'000 | Japan and Korea RMB'000 | Asia Pacific and others RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|---|
| **REVENUE** | | | | | | | |
| Sales to external customers and total revenue | 14,472,838 | 1,273,386 | 2,618,340 | 1,791,109 | 1,600,613 | 1,353,453 | 23,109,739 |

## 4. AIR TRAFFIC REVENUE

Air traffic revenue comprises revenue from the Group's airline operations business and is stated net of business tax. An analysis of the Group's air traffic revenue during the period is as follows:

| | For the six months ended 30 June 2010 RMB'000 (Unaudited) | 30 June 2009 RMB'000 (Unaudited) |
|---|---|---|
| Passenger | **28,627,073** | 19,242,976 |
| Cargo and mail | **4,462,497** | 1,966,475 |
| | **33,089,570** | 21,209,451 |

Business tax incurred and set off against air traffic revenue for the period ended 30 June 2010 amounted to approximately RMB639 million (six months ended 30 June 2009: RMB525 million).

## 5. OTHER OPERATING REVENUE

| | For the six months ended | |
|---|---|---|
| | **30 June 2010** | 30 June 2009 |
| | ***RMB'000*** | *RMB'000* |
| | **(Unaudited)** | (Unaudited) |
| Ground service income | **319,637** | 280,271 |
| Aircraft engineering income | **334,425** | 317,681 |
| Government grants and subsidies: | | |
| Refund of CAAC Infrastructure Development Fund | **–** | 823,598 |
| Recognition of deferred income | **54,178** | 38,472 |
| Others | **185,456** | 109,145 |
| Service charges on return of unused flight tickets | **143,536** | 90,074 |
| Cargo handling service income | **69,911** | 33,395 |
| Training service income | **24,879** | 7,349 |
| Import and export service income | **7,235** | 6,696 |
| Sale of materials | **10,430** | 10,684 |
| Others | **541,718** | 182,923 |
| | **1,691,405** | 1,900,288 |

## 6. PROFIT FROM OPERATIONS

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

| | For the six months ended | |
|---|---|---|
| | **30 June 2010** | 30 June 2009 |
| | ***RMB'000*** | *RMB'000* |
| | **(Unaudited)** | (Unaudited) |
| Gain on disposal of property, plant and equipment, net | **(3,635)** | (3,861) |
| Loss on derecognition of property, plant and equipment | **7,525** | 57,091 |
| Minimum lease payments under operating leases: | | |
| Aircraft and related equipment | **1,459,593** | 1,139,662 |
| Land and buildings | **604,469** | 235,418 |
| Amortisation of lease prepayments *(note 12)* | **21,794** | 23,149 |

## 7. FINANCE REVENUE AND FINANCE COSTS

| | For the six months ended | |
|---|---|---|
| | **30 June 2010** | 30 June 2009 |
| | ***RMB'000*** | *RMB'000* |
| | **(Unaudited)** | (Unaudited) |
| **Finance revenue** | | |
| Exchange gains, net | **279,302** | 175,879 |
| Interest income | **15,259** | 13,049 |
| Gain on interest rate derivative contracts, net | **–** | 71,287 |
| | **294,561** | 260,215 |
| **Finance costs** | | |
| Interest on interest-bearing bank loans, other borrowings and corporate bonds | **512,027** | 605,607 |
| Interest on finance leases | **124,933** | 240,338 |
| Loss on interest rate derivative contracts and forward foreign exchange contracts, net | **138,457** | – |
| | **775,417** | 845,945 |
| Less: Interest capitalised | **(126,571)** | (116,610) |
| | **648,846** | 729,335 |

The interest capitalisation rates per annum during the period ranges from 0.8% to 5.9% (six months ended 30 June 2009: 1% to 5%).

## 8. TAX

Under the relevant Corporate Income Tax Law in the PRC and the relevant regulations, except for certain of the Company's subsidiaries and a joint venture, which are taxed at preferential rates ranging from 15% to 22% (six months ended 30 June 2009: 20%), the group companies located within Mainland China are subject to corporate income tax at a rate of 25% (six months ended 30 June 2009: 25%) during the period.

The subsidiary in Hong Kong is taxed at 16.5%. Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the territories/countries in which the relevant companies within the Group operate, based on existing legislation, interpretations and practices in respect thereof.

## 8. TAX (continued)

The determination of current and deferred income taxes was based on the enacted tax rates. Major components of income tax charge/(credit) are as follows:

| | For the six months ended | |
|---|---|---|
| | **30 June 2010** | 30 June 2009 |
| | ***RMB'000*** | *RMB'000* |
| | **(Unaudited)** | (Unaudited) |
| Current income tax: | | |
| Mainland China | **560,454** | 9,773 |
| Hong Kong | **492** | – |
| Deferred income tax | **194,800** | (160,157) |
| Income tax charge/(credit) for the period | **755,746** | (150,384) |

The share of tax charge attributable to associates amounting to RMB305,759,000 (six months ended 30 June 2009: share of tax charge of RMB63,083,000) is included in the share of profits of associates on the face of the interim condensed consolidated income statement for the six months ended 30 June 2010.

## 9. DIVIDEND

In accordance with the Company's articles of association, the profit after tax of the Company for the purpose of dividend distribution is based on the lesser of (i) the profit determined in accordance with CAS; and (ii) the profit determined in accordance with IFRSs.

The Board of Directors of the Company does not recommend the payment of any interim dividend for the six months ended 30 June 2010 (six months ended 30 June 2009: Nil).

## 10. EARNINGS PER SHARE ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT

The calculation of basic earnings per share for the six months ended 30 June 2010 was based on the net profit attributable to equity holders of the Company for the six months ended 30 June 2010 of approximately RMB4,612,900,495, and the weighted average of approximately 11,579,847,377 ordinary shares in issue during the period, as adjusted to reflect the number of treasury shares held by Cathay Pacific through reciprocal shareholding arrangement (note 20).

The calculation of basic earnings per share for the six months ended 30 June 2009 was based on the net profit attributable to equity holders of the Company for the six months ended 30 June 2009 of approximately RMB2,878,224,000, and the weighted average of approximately 11,863,300,373 ordinary shares in issue during that period, as adjusted to reflect the number of treasury shares held by Cathay Pacific through reciprocal shareholding arrangement (note 20).

No adjustment has been made to the basic earnings per share amounts presented for the six months ended 30 June 2010 and 30 June 2009 in respect of a dilution as the Group had no potentially dilutive ordinary shares in issue during both periods.

## 11. PROPERTY, PLANT AND EQUIPMENT

| | Aircraft and flight equipment RMB'000 (Unaudited) | Buildings RMB'000 (Unaudited) | Machinery RMB'000 (Unaudited) | Transportation equipment RMB'000 (Unaudited) | Office equipment RMB'000 (Unaudited) | Construction in progress RMB'000 (Unaudited) | Total RMB'000 (Unaudited) |
|---|---|---|---|---|---|---|---|
| At 1 January 2010, net of accumulated depreciation and impairment | 65,007,440 | 3,676,394 | 1,264,545 | 720,183 | 223,010 | 4,153,298 | 75,044,870 |
| Additions | 430,586 | 75,899 | 210,246 | 24,477 | 127,588 | 5,876,137 | 6,744,933 |
| Acquisition of additional interest in an associate | 15,479,346 | 894,024 | 588,261 | 83,154 | 6,794 | 1,156,653 | 18,208,232 |
| Disposals | (651,587) | (4,227) | (2,177) | (4,691) | (971) | – | (663,653) |
| Transfer from construction in progress | 5,913,743 | 328,024 | 39,102 | 9,128 | 3,396 | (6,293,393) | – |
| Impairment | (112,197) | – | – | – | – | – | (112,197) |
| Depreciation charge for the period | (3,646,294) | (86,803) | (143,118) | (84,069) | (45,304) | – | (4,005,588) |
| Exchange realignment | (1,596) | (14) | (24) | (69) | 87 | – | (1,616) |
| At 30 June 2010, net of accumulated depreciation and impairment | 82,419,441 | 4,883,297 | 1,956,835 | 748,113 | 314,600 | 4,892,695 | 95,214,981 |
| At 1 January 2010 | | | | | | | |
| Cost | 111,477,725 | 5,261,192 | 3,195,779 | 1,916,792 | 582,542 | 4,153,298 | 126,587,328 |
| Accumulated depreciation and impairment | (46,470,285) | (1,584,798) | (1,931,234) | (1,196,609) | (359,532) | – | (51,542,458) |
| Net book value | 65,007,440 | 3,676,394 | 1,264,545 | 720,183 | 223,010 | 4,153,298 | 75,044,870 |
| At 30 June 2010 | | | | | | | |
| Cost | 136,061,853 | 6,819,228 | 4,255,088 | 2,116,968 | 714,859 | 4,892,695 | 154,860,691 |
| Accumulated depreciation and impairment | (53,642,412) | (1,935,931) | (2,298,253) | (1,368,855) | (400,259) | – | (59,645,710) |
| Net book value | 82,419,441 | 4,883,297 | 1,956,835 | 748,113 | 314,600 | 4,892,695 | 95,214,981 |

At 30 June 2010, certain of the Group's aircraft and buildings with an aggregate net book value of approximately RMB28,278 million (31 December 2009: RMB9,688 million) were pledged to secure certain bank loans of the Group.

The aggregate net book value of aircraft held under finance leases included in the property, plant and equipment of the Group amounted to approximately RMB29,178 million (31 December 2009: RMB27,425 million).

At 30 June 2010, the Group was in the process of applying for the title certificates of certain buildings with an aggregate net book value of approximately RMB41 million (31 December 2009: RMB92 million) transferred from Air China International Corporation, the predecessor of the Company. The Group was also in the process of applying for the title certificates of certain buildings acquired by the Group after incorporation with an aggregate net book value of approximately RMB2,186 million (31 December 2009: RMB1,284 million). The Directors of the Company are of the view that the Group is entitled to lawfully and validly occupy and use the above-mentioned buildings, and therefore are of the opinion that the aforesaid matter did not have any significant impact on the Group's financial position as at 30 June 2010.

## 12. LEASE PREPAYMENTS

| | 30 June 2010<br>*RMB'000*<br>(Unaudited) |
|---|---|
| **Cost** | |
| At 1 January | **2,088,610** |
| Acquisition of additional interest in an associate | **115,399** |
| At 30 June 2010 | **2,204,009** |
| **Accumulated amortisation** | |
| At 1 January 2010 | **(133,791)** |
| Acquisition of additional interest in an associate | **(4,066)** |
| Amortisation for the period *(note 6)* | **(21,794)** |
| At 30 June 2010 | **(159,651)** |
| **Net book value** | |
| At 30 June 2010 | **2,044,358** |

The Group's lease prepayments comprise land use rights which are held under long term leases and are located in Mainland China.

At 30 June 2010, certain of the Group's land use rights with an aggregate net book value of approximately RMB41 million (31 December 2009: RMB41 million) were pledged to secure certain of the Group's bank loans.

At 30 June 2010, the Group was in the process of applying for the title certificates of certain land use rights acquired by the Group after incorporation with an aggregate net book value of approximately RMB622 million (31 December 2009: RMB629 million). The Directors of the Company are of the view that the Group is entitled to lawfully and validly occupy and use the above-mentioned land use rights, and therefore are of the opinion that the aforesaid matter did not have any significant impact on the Group's financial position as at 30 June 2010.

## 13. ACCOUNTS RECEIVABLE

The Group normally allows a credit period of 7 to 90 days to its sales agents and customers while some major customers are granted a credit period of up to or above six months. The Group seeks to maintain strict control over its outstanding receivables to minimise credit risk. Overdue balances are reviewed regularly by senior management. In view of the aforementioned and the fact that the Group's accounts receivable relate to a large number of diversified customers, there is no significant concentration of credit risk. Accounts receivable are non-interest-bearing.

An aged analysis of Group's accounts receivable as at the end of the reporting period, net of provision for impairment, is as follows:

| | **30 June 2010 *RMB'000* (Unaudited)** | 31 December 2009 *RMB'000* (Audited) |
|---|---|---|
| Within 30 days | **2,838,427** | 1,773,021 |
| 31 to 60 days | **154,240** | 114,134 |
| 61 to 90 days | **23,288** | 30,186 |
| Over 90 days | **180,981** | 136,924 |
| | **3,196,936** | 2,054,265 |

Included in the Group's accounts receivable as at the end of the reporting period is the following amount due from a joint venture:

| | **30 June 2010 *RMB'000* (Unaudited)** | 31 December 2009 *RMB'000* (Audited) |
|---|---|---|
| Joint venture | **169** | 126 |

## 14. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

An analysis of the Group's prepayments, deposits and other receivables at the end of the reporting period is as follows:

| | 30 June 2010 *RMB'000* (Unaudited) | 31 December 2009 *RMB'000* (Audited) |
|---|---|---|
| **Prepayments** | | |
| Advances and others | **389,785** | 263,532 |
| Manufacturers' credits | **406,619** | 17,222 |
| Prepaid aircraft operating lease rentals | **314,860** | 215,177 |
| | **1,111,264** | 495,931 |
| **Deposits and other receivables** | **1,267,403** | 734,863 |
| | **2,378,667** | 1,230,794 |

## 15. DERIVATIVE FINANCIAL INSTRUMENTS

| | 30 June 2010 (Unaudited) | | 31 December 2009 (Audited) | |
|---|---|---|---|---|
| | Assets *RMB'000* | Liabilities *RMB'000* | Assets *RMB'000* | Liabilities *RMB'000* |
| Fuel derivative contracts | **–** | **1,316,776** | – | 2,051,428 |
| Interest rate derivative contracts | **3,766** | **346,711** | – | 223,199 |
| Forward foreign exchange contracts | **–** | **14,990** | – | – |
| | **3,766** | **1,678,477** | – | 2,274,627 |

The Group's strategy for managing jet fuel price risk is to provide the Group with protection against sudden and significant increases in prices. In meeting this objective, the Group allows for the use of approved derivative instruments with counterparties and within approved limits. The Group's management is of the view that it is more appropriate to disclose the realised and unrealised gains or losses of fuel derivative contracts as movements in fair value of the fuel derivative contracts on the Group's consolidated income statement to reflect the objective of the transactions. The movements in fair value of the fuel derivative contracts for the six months ended 30 June 2010 was RMB720,800,647 (six months ended 30 June 2009: RMB1,449,791,428), which included a recovery in fair value of RMB734,651,928 (six months ended 30 June 2009: RMB4,002,803,272) and changes in fair value of RMB13,851,281 (six months ended 30 June 2009: RMB2,553,011,844) as a result of the settlement of the fuel derivative contracts.

The fair value of the fuel derivative contracts as at the end of the reporting period was estimated by using the Monte Carlo simulation with considerations of mean reversion, taking into account the terms and conditions of the derivative contracts. The major inputs used in the estimation process include expected volatility, the mean-reversion speed, long term equilibrium price and risk-free interest rate which can be obtained from observable markets.

The fair value of the interest rate derivative contracts as at the end of the reporting period was estimated by using the Rendlemen and Barter model, taking into account the terms and conditions of the derivative contracts. The major inputs used in the estimation process include volatility of the short term interest rate and the LIBOR curve, which can be obtained from observable markets.

## 16. PLEDGED DEPOSITS, CASH AND CASH EQUIVALENTS

| | 30 June 2010 RMB'000 (Unaudited) | 31 December 2009 RMB'000 (Audited) |
|---|---|---|
| Cash and bank balances | **3,892,221** | 1,654,399 |
| Cash placed with China National Aviation Finance Co., Ltd. | **69,837** | 455,400 |
| Total cash and bank balances | **3,962,058** | 2,109,799 |
| Time deposits placed with banks | **2,590,374** | 1,161,706 |
| Time deposits placed with China National Aviation Finance Co., Ltd. | **700,000** | – |
| Total time deposits | **3,290,374** | 1,161,706 |
| Pledged deposits against: | | |
| Aircraft operating leases and financial derivatives | **(395,131)** | (564,662) |
| Bank loans | **(1,182,756)** | – |
| Others | **(84)** | (85) |
| Total pledged deposits | **(1,577,971)** | (564,747) |
| Non-pledged deposits | **1,712,403** | 596,959 |
| Cash and cash equivalents | **5,674,461** | 2,706,758 |

An analysis of non-pledged time deposits placed with banks is as follows:

| | 30 June 2010 RMB'000 (Unaudited) | 31 December 2009 RMB'000 (Audited) |
|---|---|---|
| Non-pledged time deposits with original maturity of: | | |
| Less than 3 months when acquired | **1,250,513** | 566,510 |
| Over 3 months when acquired | **461,890** | 30,449 |
| | **1,712,403** | 596,959 |

## 17. ACCOUNTS PAYABLE

An aged analysis of the Group's accounts payable as at the end of the reporting period is as follows:

| | **30 June 2010 *RMB'000* (Unaudited)** | 31 December 2009 *RMB'000* (Audited) |
|---|---|---|
| Within 30 days | **5,933,656** | 4,027,306 |
| 31 to 60 days | **1,031,608** | 795,309 |
| 61 to 90 days | **521,717** | 469,321 |
| Over 90 days | **811,371** | 753,797 |
| | **8,298,352** | 6,045,733 |

Included in the accounts payable as at the end of the reporting period is the following amount due to a joint venture:

| | **30 June 2010 *RMB'000* (Unaudited)** | 31 December 2009 *RMB'000* (Audited) |
|---|---|---|
| Joint venture | **168,390** | 102,976 |

## 18. OTHER PAYABLES AND ACCRUALS

An analysis of the Group's other payables and accruals as at the end of the reporting period is as follows:

| | **30 June 2010 *RMB'000* (Unaudited)** | 31 December 2009 *RMB'000* (Audited) |
|---|---|---|
| Accrued salaries, wages and benefits | **1,859,160** | 1,188,557 |
| Accrued operating expenses | **1,591,889** | 1,154,091 |
| Business tax, customs duties and levies payable | **964,914** | 782,450 |
| Due to a shareholder of a subsidiary | **707,787** | – |
| Receipts in advance for employee residence | **685,640** | – |
| Receipts in advance and deposits received from sales agents | **628,715** | 472,333 |
| Interest payable | **278,643** | 298,423 |
| Current portion of deferred income | **259,611** | 266,660 |
| Lease payable | **256,383** | – |
| Provision for staff housing benefits | **24,174** | 45,981 |
| Current portion of long term payables | **14,042** | 19,334 |
| Others | **993,684** | 417,577 |
| | **8,264,642** | 4,645,406 |

## 19. ISSUED CAPITAL

The number of shares of the Company and their nominal value as at 30 June 2010 and 31 December 2009 are as follows:

| | Number of shares | Nominal value *RMB'000* |
|---|---|---|
| **Registered, issued and fully paid** | | |
| H shares of RMB1.00 each | 4,405,683,364 | 4,405,683 |
| A shares of RMB1.00 each | 7,845,678,909 | 7,845,679 |
| | 12,251,362,273 | 12,251,362 |

The above H shares and A shares rank pari passu in all material respects.

## 20. TREASURY SHARES

At 30 June 2010, the Group owned a 29.99% (31 December 2009: 29.99%) equity interest in Cathay Pacific, which in turn owned a 19.18% (31 December 2009: 18.1%) equity interest in the Company. Accordingly, the 29.99% of Cathay Pacific's shareholding in the Company was recorded in the Group's consolidated financial statements as treasury shares through deduction from equity.

## 21. SHARE APPRECIATION RIGHTS

The Company has adopted a share appreciation rights ("SAR") arrangement (the "Plan") which was approved by the shareholders on 18 October 2004 for the purpose of motivating its employees. The Plan provides for the grant of SARs to eligible participants, including the Company's Directors (excluding independent non-executive Directors), president, vice presidents, heads of key departments in the Company's headquarters, general managers and deputy general managers of principal branches and subsidiaries as well as selected senior professionals and key specialists. In any event, SARs will be granted to no more than 200 individuals.

Under the Plan, the holders of SARs are entitled to the rights to receive an amount in respect of the appreciation in market value of the Company's H shares from the date of grant of SARs and the date of exercise. No shares will be issued under the Plan and therefore the Company's equity interests will not be diluted as a result of the issuance of SARs. The maximum number of unexercised SARs permitted to be granted under the Plan is, upon their exercise, limited to 2% of the Company's H shares in issue at any time during each year. The maximum number of SARs granted to eligible participants under the Plan within any 12-month period is, upon their exercise, limited to 0.4% of the Company's H shares in issue at any time during each year. The maximum number of SARs granted to any eligible participant is limited to 10% of the total number of unexercised SARs in issue at any time during each year. Any further grant of SARs in excess of the above limits is subject to shareholders' approval in general meetings.

The exercise period of all SARs commences after a vesting period and ends on a date which is not later than five years from the date of grant of the SARs. The exercise price of the SARs will be equal to the average closing price of the Company's H shares on the HKSE for the five consecutive trading days immediately preceding the date of grant. On 15 June 2007, 14,939,900 SARs were granted to a total of 109 individuals at an exercise price of HK$2.98 per share. As at each of the last days of the second, third and fourth anniversaries of the date of grant, the total number of SARs exercisable will not exceed 30%, 70% and 100%, respectively, of the total SARs granted to the respective eligible participants. As at 30 June 2010, all SARs granted remained and had an aggregate book value of RMB9,043,230.

On 25 August 2009, a board resolution was passed to suspend the Plan and to amend certain terms of the Plan in response to certain recently announced government policies, which will be submitted for approval in the shareholders' meeting of the Company.

## 22. BUSINESS COMBINATION

On 19 April 2010, the Company acquired a 26% equity interest in Shenzhen Airlines in addition to the 25% equity interest it already held. Further details of the transaction are included in Note 1 to the financial statements. Upon completion of the transaction, the Company's interest in Shenzhen Airlines increased from 25% to 51%. Shenzhen Airlines was then changed from an associate into a subsidiary of the Company with effect from 19 April 2010.

By the end of the reporting period, the fair value of the identifiable assets, liabilities and contingent liabilities of Shenzhen Airlines as at the date of acquisition was determined provisionally based on management's best estimates. The Company will recognise any adjustment to the provisional value after completing the initial accounting within one year of the acquisition date.

The provisional fair value of the identifiable net assets in Shenzhen Airlines as at the date of acquisition was:

| | **Fair value recognised on acquisition** *RMB'000* (Unaudited) |
|---|---|
| Property, plant and equipment | 21,764,334 |
| Lease prepayments | 111,333 |
| Interests in associates | 46,989 |
| Deposits for aircraft under operating leases | 487,087 |
| Available-for-sale investment | (1,847) |
| Deferred tax assets | 635 |
| Financial assets held for trading | 24,738 |
| Inventories | 182,715 |
| Accounts receivables | 618,580 |
| Prepayments, deposits and other receivables | 710,825 |
| Pledged deposits | 1,782,573 |
| Cash and cash equivalents | 2,000,733 |
| Derivative financial instruments | (82,410) |
| Accounts payable | (2,766,568) |
| Bills payable | (235,025) |
| Other payables and accruals | (4,297,463) |
| Tax payable | (161,464) |
| Obligations under finance leases | (355,878) |
| Interest-bearing bank and other borrowings | (19,945,308) |
| Long-term payables | (87,596) |
| Deferred income | (589,955) |
| Deferred tax liabilities | (111,653) |
| Non-controlling interests | (19,980) |
| Total identifiable net assets at fair value | (924,605) |
| Add: Goodwill arising on acquisition | 1,304,320 |
| Less: Non-controlling interests on acquisition | (453,057) |
| | 832,772 |
| Remeasurement of the 25% equity interest previously held | 150,628 |
| Purchase consideration transferred | 682,144 |
| | 832,772 |

## 22. BUSINESS COMBINATION (continued)

An analysis of the net inflow of cash and cash equivalents in respect of the acquisition of additional interest in Shenzhen Airlines is as follows:

| | *RMB'000* (Unaudited) |
|---|---|
| Cash consideration | (682,144) |
| Net cash acquired from the acquisition of additional interest in Shenzhen Airlines | 2,502,195 |
| Net inflow of cash and cash equivalents in respect of the acquisition of additional interest in Shenzhen Airlines | 1,820,051 |

## 23. CONTINGENT LIABILITIES

As at 30 June 2010, the Group had the following contingent liabilities:

(a) Pursuant to the restructuring of CNAHC for the listing of the Company's H shares on the HKSE and the LSE, the Company entered into a restructuring agreement (the "Restructuring Agreement") with CNAHC and CNACG on 20 November 2004. According to the Restructuring Agreement, except for liabilities constituting or arising out of or relating to businesses undertaken by the Company after the restructuring, no liabilities would be assumed by the Company and the Company would not be liable, whether severally, or jointly and severally, for debts and obligations incurred by CNAHC and CNACG prior to the restructuring. The Company has also undertaken to indemnify CNAHC and CNACG against any damage suffered or incurred by CNAHC and CNACG as a result of any breach by the Company of any provision of the Restructuring Agreement.

(b) On 15 April 2002, Flight CA129 crashed on approach to the Gimhae International Airport, South Korea. There were 129 fatalities including 121 passengers and 8 crew members aboard the crashed airplane. Investigations were conducted by both the Chinese and civil aviation authorities and have yet to be concluded at the date of approval of these financial statements. Certain injured passengers and family members of the deceased passengers as well as crew members have commenced proceedings in Korean courts seeking damages against Air China International Corporation (the predecessor of the Company). The Group cannot predict the timing of the courts' judgements or the possible outcome of the lawsuits or any possible appeal actions. Up to 30 June 2010, the Company, Air China International Corporation and the Company's insurer had paid an aggregate amount of approximately RMB241 million (31 December 2009: RMB238 million) in respect of passenger liability and other auxiliary costs. Included in the RMB241 million (31 December 2009: RMB238 million) was an amount of approximately RMB231 million (31 December 2009: RMB231 million) borne by the Company's insurer. As part of the above-mentioned restructuring, CNAHC has agreed to indemnify the Group against any liabilities relating to the crash of Flight CA129, excluding the compensation already paid up to 30 September 2004 (being the date of incorporation of the Company). The Directors of the Company believe that the accident will not have any material adverse impact on the Group's financial position.

(c) On 26 February 2007, the Federal Judiciary of the United States filed a civil summon against the Company and Air China Cargo claiming that they, together with a number of other airlines, have violated certain anti-trust regulations in respect of their air cargo operations in the United States and the European Union. The status of the proceedings is still in the preliminary stage and therefore the Directors of the Company are of the view that it is not possible to estimate the eventual outcome of the claim with reasonable certainty at this stage. Also, the Directors of the Company are of the view that there would be valid defence against this claim and consider that no provision for this claim is needed accordingly.

## 23. CONTINGENT LIABILITIES (continued)

(d) On 17 November 2009, Airport City Development Co., Ltd. ("Airport City Development") commenced proceedings involving approximately RMB224 million against the Company, Air China Cargo, Air China International Corporation and a third party, for the unlawful use of land owned by Airport City Development. The status of the proceedings is still in the preliminary stage and the Directors of the Company are of the view that it is not possible to estimate the eventual outcome of the claim with reasonable certainty at this stage. Also, the Directors of the Company are of the view that there would be valid defence against this claim and consider that no provision for this claim is needed accordingly.

(e) The Group has issued guarantees to banks in respect of the bank loans granted to the following party:

| | **30 June 2010 *RMB'000* (Unaudited)** | 31 December 2009 *RMB'000* (Audited) |
|---|---|---|
| Associates | **26,181** | 130,779 |

(f) Shenzhen Airlines, a subsidiary of the Group has provided guarantees to banks for certain employees in respect of their residential loans as well as for certain pilot trainees in respect of their tuition loans. As at 30 June 2010, Shenzhen Airlines has outstanding guarantees for employees' residential loans amounting to RMB306,745,599 and for pilot trainees' tuition loans amounting to RMB307,600,693.

## 24. OPERATING LEASE ARRANGEMENTS

The Group leases certain of its office premises, aircraft and related equipment under operating lease arrangements. Leases for these assets are negotiated for terms ranging from 1 to 20 years.

At the end of the reporting period, the Group had the following future minimum lease payments under non-cancellable operating leases:

| | **30 June 2010 *RMB'000* (Unaudited)** | 31 December 2009 *RMB'000* (Audited) |
|---|---|---|
| Within one year | **3,645,274** | 2,941,092 |
| In the second to fifth years, inclusive | **9,846,264** | 6,901,533 |
| Over five years | **5,951,180** | 4,209,817 |
| | **19,442,718** | 14,052,442 |

## 25. COMMITMENTS

### (a) Capital commitments

The Group had the following amounts of contractual commitments for the acquisition and construction of property, plant and equipment as at the end of the reporting period:

| | **30 June 2010** *RMB'000* **(Unaudited)** | 31 December 2009 *RMB'000* (Audited) |
|---|---|---|
| Contracted, but not provided for: | | |
| Aircraft and flight equipment | **83,189,417** | 57,458,579 |
| Buildings | **875,581** | 224,525 |
| Others | **492,847** | 47,803 |
| | **84,557,845** | 57,730,907 |
| Authorised, but not contracted for: | | |
| Aircraft and flight equipment | **515,520** | 515,520 |
| Buildings | **2,245,414** | 3,217,713 |
| Others | **474,151** | 572,472 |
| | **3,235,085** | 4,305,705 |
| Total capital commitments | **87,792,930** | 62,036,612 |

### (b) Investment commitments

The Group had the following amounts of investment commitments as at the end of the reporting period:

| | **30 June 2010** *RMB'000* **(Unaudited)** | 31 December 2009 *RMB'000* (Audited) |
|---|---|---|
| Contracted, but not provided for: | | |
| Associate | **401,980** | 50,633 |

## 26. RELATED PARTY TRANSACTIONS

During the period, the Group had the following significant transactions with (i) CNAHC, its subsidiaries (other than the Group) and joint ventures (collectively the "CNAHC Group"); (ii) its joint ventures; and (iii) its associates:

| | For the six months ended | |
|---|---|---|
| | **30 June 2010** | 30 June 2009 |
| | ***RMB'000*** | *RMB'000* |
| | **(Unaudited)** | (Unaudited) |
| (a) Included in air traffic revenue | | |
| Sale of cargo space: | | |
| CNAHC Group | **26,321** | 50,708 |
| Associate | **37,679** | – |
| | **64,000** | 50,708 |
| Government charter flights: | | |
| CNAHC Group | **273,668** | 341,004 |
| (b) Included in other operating revenue | | |
| Equipment leasing income: | | |
| CNAHC Group | **1,050** | – |
| Associate | **1,470** | 60 |
| | **2,520** | 60 |
| Aircraft engineering income: | | |
| Joint venture | **26** | – |
| Associates | **30,149** | 18,113 |
| | **30,175** | 18,113 |
| Ground services income: | | |
| CNAHC Group | **195** | 116 |
| Joint venture | **117** | 69 |
| Associates | **32,652** | 31,849 |
| | **32,964** | 32,034 |
| Others: | | |
| CNAHC Group | **11,943** | 13,733 |
| Joint ventures | **595** | 7,029 |
| Associates | **6,746** | 5,768 |
| | **19,284** | 26,530 |
| (c) Included in finance revenue and finance costs | | |
| Interest income: | | |
| Joint venture | **328** | – |
| Associate | **7,546** | 2,293 |
| | **7,874** | 2,293 |
| Interest expense: | | |
| Associate | **13,010** | 25,025 |

## 26. RELATED PARTY TRANSACTIONS (continued)

| | For the six months ended 30 June 2010 RMB'000 (Unaudited) | 30 June 2009 RMB'000 (Unaudited) |
|---|---|---|
| (d) Included in operating expenses | | |
| Airport ground services, take-off, landing and depot expenses: | | |
| CNAHC Group | **20,852** | 34,569 |
| Associates | **36,524** | 48,707 |
| | **57,376** | 83,276 |
| Air catering charges: | | |
| CNAHC Group | **22,149** | 23,109 |
| Associates | **6,340** | 7,030 |
| | **28,489** | 30,139 |
| Repair and maintenance costs: | | |
| CNAHC Group | **20** | – |
| Joint venture | **404,777** | 289,563 |
| Associates | **329,571** | 131,381 |
| | **734,368** | 420,944 |
| Sales commission expenses: | | |
| CNAHC Group | **1,932** | 1,177 |
| Joint venture | **7,597** | 5,732 |
| Associates | **1,167** | 1,370 |
| | **10,696** | 8,279 |
| Management fees: | | |
| CNAHC Group | **4,176** | 4,231 |
| Aircraft and flight equipment leasing fees: | | |
| Associates | **311,583** | 306,644 |
| Others: | | |
| CNAHC Group | **80,995** | 70,586 |
| Joint venture | **618** | 3,178 |
| Associates | **3,232** | 3,320 |
| | **84,845** | 77,084 |

## 26. RELATED PARTY TRANSACTIONS (continued)

| | 30 June 2010 RMB'000 (Unaudited) | 31 December 2009 RMB'000 (Audited) |
|---|---|---|
| (e) Deposits, loans and bills payable | | |
| Deposits placed with an associate | **769,837** | 455,400 |
| Loans from an associate | **573,449** | 527,731 |
| (f) Outstanding balances with related parties | | |
| Long term receivable from the ultimate holding company | **81,813** | 131,813 |
| Due from the ultimate holding company | **427,387** | 461,147 |
| Due from related companies | **5,407** | 10,194 |
| Due from associates | **48,059** | 28,765 |
| Due from joint ventures | **160,859** | 11,485 |
| Due to related companies | **(87,864)** | (113,024) |
| Due to associates | **(201,849)** | (113,450) |
| Due to joint ventures | **(168,889)** | (105,049) |

The long term receivable from the ultimate holding company is unsecured, interest-free and is not repayable within one year from the end of the reporting period. Except for the long term receivable from the ultimate holding company, the outstanding balances with related parties are unsecured, interest-free and repayable within one year or have no fixed terms of repayment.

(g) An analysis of the compensation of key management personal of the Group is as follows:

| | For the six months ended | |
|---|---|---|
| | 30 June 2010 RMB'000 (Unaudited) | 30 June 2009 RMB'000 (Unaudited) |
| Compensation of key management personnel of the Group | | |
| Short term employee benefits | **4,619** | 1,774 |
| Equity-settled share option expense | **1,126** | 1,185 |
| Post-employment benefits | **184** | 140 |
| | **5,929** | 3,099 |

The Group operates in an economic environment predominated by enterprises directly or indirectly owned or controlled by the PRC government through its numerous authorities, affiliates or other organisations (collectively the "State-owned Enterprises"). During the period, the Group had transactions with the State-owned Enterprises including, but not limited to, the provision of air passenger and air cargo services and purchases of services. The Directors consider that transactions with other State-owned Enterprises are activities in the ordinary course of the Group's business and that the dealings of the Group have not been significantly or unduly affected by the fact that the Group and the other State-owned Enterprises are ultimately controlled or owned by the PRC government. The Group has also established pricing policies for products and services, and such pricing policies do not depend on whether or not the customers are State-owned Enterprises. Having due regard to the substance of the relationships, the Directors of the Company are of the opinion that none of these transactions is a material related party transaction that requires separate disclosure.

## 27. EVENTS AFTER THE REPORTING PERIOD

On 30 July 2010, Shenzhen Airlines, Air China Group Import and Export Trading Co. Ltd ("AIE", a wholly-owned subsidiary of the Company) and Airbus S.A.S. ("Airbus") entered into a sales and purchase agreement pursuant to which the Shenzhen Airlines agreed to purchase 10 A320-series aircraft from Airbus. The aggregate consideration of the purchase is approximately US$814 million (equivalent to approximately RMB5,528 million) and is payable by Shenzhen Airlines in cash installments. Shenzhen Airlines is expecting to take delivery of the aircraft in stages from 2012 to 2013.

## 28. APPROVAL OF THE INTERIM CONDENSED CONSOLIDATED FINANCIAL REPORT

These interim condensed consolidated financial statements were approved and authorised for issue by the Board of Directors on 25 August 2010.

# Unaudited Interim Consolidated Income Statement

For the six months ended 30 June 2010
(Prepared under China Accounting Standards for Business Enterprises)

| | For the six months ended | |
|---|---|---|
| | **30 June 2010** | 30 June 2009 |
| | ***RMB'000*** | *RMB'000* |
| | **(Unaudited))** | (Unaudited)) |
| Revenue from operations | **34,307,673** | 22,405,025 |
| Less: Cost of operations | **26,951,413** | 18,975,773 |
| Business taxes and surcharges | **662,104** | 543,663 |
| Selling expenses | **2,421,755** | 1,640,424 |
| General and administrative expenses | **959,410** | 684,816 |
| Finance costs | **288,192** | 606,798 |
| Impairment losses in assets | **126,230** | – |
| Add: Gains from movements in fair value | **576,969** | 1,521,078 |
| Investment income | **1,890,209** | 311,125 |
| Including: Share of profits of associates and joint ventures | **1,739,454** | 311,125 |
| Profit from operations | **5,365,747** | 1,785,754 |
| Add: Non-operating income | **213,311** | 952,844 |
| Less: Non-operating expenses | **19,801** | 8,423 |
| Including: Loss on disposal of non-current assets | **10,056** | 4,248 |
| Profit before tax | **5,559,257** | 2,730,175 |
| Less: Tax | **778,086** | (134,500) |
| Net profit | **4,781,171** | 2,864,675 |
| Net profit attributable to equity holders of the Company | **4,694,021** | 2,925,649 |
| Non-controlling interests | **87,150** | (60,974) |
| Earnings per share (RMB) | | |
| Basic | **0.41** | 0.25 |
| Diluted | **N/A** | N/A |
| Other comprehensive income/(loss) | **(142,466)** | 20,464 |
| Total comprehensive income | **4,638,705** | 2,885,139 |
| Attributable to: | | |
| Equity holders of the Company | **4,551,518** | 2,947,151 |
| Non-controlling interests | **87,187** | (62,012) |

# Unaudited Interim Consolidated Balance Sheet

For the six months ended 30 June 2010
(Prepared under China Accounting Standards for Business Enterprises)

| | **30 June 2010** ***RMB'000*** **(Unaudited)** | 31 December 2009 *RMB'000* (Audited) |
|---|---|---|
| **ASSETS** | | |
| Current assets: | | |
| Cash and bank balances | **7,058,305** | 3,201,568 |
| Financial assets held for trading | **23,073** | – |
| Bills receivable | **4,705** | 2,489 |
| Accounts receivable | **3,189,761** | 2,201,172 |
| Other receivables | **1,486,765** | 492,007 |
| Prepayments | **573,464** | 350,257 |
| Inventories | **1,074,784** | 931,271 |
| Total current assets | **13,410,857** | 7,178,764 |
| Non-current assets: | | |
| Long term receivables | **385,096** | 254,306 |
| Long term equity investments | **14,500,621** | 13,235,575 |
| Fixed assets | **86,846,388** | 69,147,527 |
| Construction in progress | **18,286,098** | 11,731,131 |
| Intangible assets | **2,768,263** | 2,576,301 |
| Goodwill | **1,449,030** | 349,055 |
| Long term deferred expenses | **128,297** | 138,105 |
| Deferred tax assets | **1,803,690** | 1,552,443 |
| Total non-current assets | **126,167,483** | 98,984,443 |
| Total assets | **139,578,340** | 106,163,207 |

# Unaudited Interim Consolidated Balance Sheet

For the six months ended 30 June 2010
(Prepared under China Accounting Standards for Business Enterprises)

| | 30 June 2010 RMB'000 (Unaudited) | 31 December 2009 RMB'000 (Audited) |
|---|---|---|
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | |
| Current liabilities: | | |
| Short term loans | **14,151,056** | 8,870,400 |
| Financial liabilities held for trading | **1,678,477** | 2,274,627 |
| Bills payable | **325,401** | 763,255 |
| Accounts payable | **9,739,385** | 7,113,031 |
| Domestic air traffic liabilities | **1,516,644** | 850,394 |
| International air traffic liabilities | **2,047,960** | 1,583,959 |
| Receipts in advance | **80,597** | 38,127 |
| Employee compensations payable | **616,184** | 348,492 |
| Taxes payable | **1,343,926** | 720,295 |
| Interest payable | **267,979** | 303,154 |
| Other payables | **4,963,781** | 2,224,083 |
| Non-current liabilities repayable within one year | **13,443,379** | 11,304,489 |
| Total current liabilities | **50,174,769** | 36,394,306 |
| Non-current liabilities: | | |
| Long term loans | **30,698,057** | 18,321,078 |
| Corporate bonds | **9,000,000** | 9,000,000 |
| Long term payables | **2,309,099** | 1,499,128 |
| Obligations under finance leases | **15,910,785** | 15,366,476 |
| Accrued liabilities | **124,073** | 94,438 |
| Deferred income | **2,421,210** | 1,383,338 |
| Deferred tax liabilities | **869,020** | 143,000 |
| Total non-current liabilities | **61,332,244** | 45,807,458 |
| Total liabilities | **111,507,013** | 82,201,764 |
| Shareholders' equity: | | |
| Issued capital | **12,251,362** | 12,251,362 |
| Capital reserve | **10,550,932** | 10,823,906 |
| Reserve funds | **1,563,914** | 1,563,914 |
| Retained earnings | **5,615,869** | 921,848 |
| Foreign exchange translation reserve | **(1,781,211)** | (1,638,158) |
| Equity attributable to equity holders of the Company | **28,200,866** | 23,922,872 |
| Non-controlling interests | **(129,539)** | 38,571 |
| Total shareholders' equity | **28,071,327** | 23,961,443 |
| Total liabilities and shareholders' equity | **139,578,340** | 106,163,207 |

# Supplementary Information

## Effects of Significant Differences Between IFRSs and CAS

The effects of the significant differences between the consolidated financial statements of the Group prepared under CAS and IFRSs are as follows:

| | Notes | For the six months ended 30 June 2010 RMB'000 (Unaudited) | 30 June 2009 RMB'000 (Unaudited) |
|---|---|---|---|
| Net profit attributable to the equity holders of the Company under CAS | | **4,694,021** | 2,925,649 |
| Deferred tax | *(i)* | **38,000** | 21,000 |
| Differences in value of fixed assets | *(ii)* | **(122,067)** | (58,026) |
| Government grants | *(iii)* | **(7,469)** | (8,056) |
| Others | | **10,415** | (2,343) |
| Net profit attributable to equity holders of the Company under IFRSs | | **4,612,900** | 2,878,224 |

| | Notes | 30 June 2010 RMB'000 (Unaudited) | 31 December 2009 RMB'000 (Audited) |
|---|---|---|---|
| Equity attributable to the equity holders of the Company under CAS | | **28,200,866** | 23,922,872 |
| Deferred tax | *(i)* | **47,000** | 9,000 |
| Differences in value of fixed assets | *(ii)* | **115,170** | 237,237 |
| Government grants | *(iii)* | **(425,010)** | (417,541) |
| Others | *(iv)* | **172,341** | 164,328 |
| Equity attributable to equity holders of the Company under IFRSs | | **28,110,367** | 23,915,896 |

*Notes:*

(i) The differences in deferred tax were mainly caused by the other differences under CAS and IFRSs as explained below.

(ii) The differences in the value of fixed assets mainly consists of following three types:(1) fixed assets acquired in foreign currencies prior to 1 January 1994 and translated at the equivalent amount of RMB at the then prevailing exchange rates prescribed by the government (i.e. the government-prescribed rates) under CAS. Under IFRSs, the costs of fixed asset acquired in currencies prior to 1January 1994 should be translated at the then prevailing market rate (i.e. the swap rate) and therefore resulted in differences in the costs of fixed asset in the financial statements prepared under CAS and IFRSs. (2) in accordance with the accounting policies under IFRSs, all assets are recorded at historical costs. Therefore the revaluation surplus or deficit (and the related depreciation/amortisation or impairment) recorded under CAS should be reversed in the financial statements prepared under IFRSs. (3) the differences were caused by the adoption of component accounting in different years under CAS and IFRSs. Component accounting was adopted by the Group on a prospective basis under IFRSs in 2005 and under CAS in 2007. These three types of differences are expected to be eliminated through depreciation or disposal of fixed assets in future.

(iii) Under both CAS and IFRSs, government grants or government subsidies should be debited as government grants/ subsidiaries receivable or the relevant assets and credited as deferred income, which will then be charged to the income statement on a straight line basis over the useful lives of the relevant assets. As the accounting for government grants or government subsidies have had no significant impact on the Group's financial statements, no adjustment has been made to unify the accounting treatments of government grants or government subsidies under CAS and IFRSs. Therefore in the Group's financial statement prepared in accordance with CAS, government grants received was debited as the relevant assets and credited as capital reserve; government subsidies were debited as cash and bank balances and credited as subsidy income in the income statement. Such differences are expected to be eliminated gradually through amortisation of deferred income to the income statement in future.

(iv) The difference was mainly caused by the disposal of Hong Kong Dragon Airlines Limited to Cathay Pacific and is expected to be eliminated when the Group's interest in Cathay Pacific is disposed of.

# Glossary of Technical Terms

## CAPACITY MEASUREMENTS

| | |
|---|---|
| "available seat kilometres" or "ASK" | the number of seats available for sale multiplied by the kilometres flown |
| "available freight tonne kilometres" or "AFTK" | the number of tonnes of capacity available for the carriage of cargo and mail multiplied by the kilometres flown |
| "available tonne kilometres" or "ATK" | the number of tonnes of capacity available for the transportation of revenue load (passengers and cargo) multiplied by the kilometres flown |
| "tonne" | a metric tonne, equivalent to 2,204.6 pounds |

## TRAFFIC MEASUREMENTS

| | |
|---|---|
| "revenue passenger kilometres" or "RPK" | the number of revenue passengers carried multiplied by the kilometres flown |
| "passenger traffic" | measured in RPK, unless otherwise specified |
| "revenue freight tonne kilometres" or "RFTK" | the revenue cargo and mail load in tonnes multiplied by the kilometres flown |
| "cargo traffic" | measured in RFTK, unless otherwise specified |
| "revenue tonne kilometres" or "RTK" | the revenue load (passengers and cargo) in tonnes multiplied by the kilometres flown |

## LOAD FACTORS

| | |
|---|---|
| "cargo and mail load factor" | RFTK expressed as a percentage of AFTK |
| "passenger load factor" | RPK expressed as a percentage of ASK |
| "overall load factor" | RTK expressed as a percentage of ATK |

## UTILISATION

| | |
|---|---|
| "block hours" | each whole or partial hour elapsing from the moment the chocks are removed from the wheels of the aircraft for flights until the chocks are next again returned to the wheels of the aircraft |