# 2011
# ANNUAL REPORT

AIR CHINA
中国国际航空公司

A STAR ALLIANCE MEMBER™

## Air China Limited

Stock code: 753 HongKong 601111 Shanghai AIRC London

Air China is the only national flag carrier of China and a member of Star Alliance, the world's largest airline alliance. It is also the only Chinese civil aviation enterprise listed in "The World's 500 Most Influential Brands".

Air China is headquartered in Beijing, the capital of China, with two increasingly important hubs in Shanghai and Chengdu. With Star Alliance, our network covered 1,290 destinations in 189 countries as at 31 December 2011. Air China is dedicated to provide passengers with safe, convenient, comfortable and personalised services.

Air China is actively implementing the strategic objectives of ranking among the top in terms of global competitiveness, continuously strengthening our development potentials, providing our customers with a unique and excellent experience and realising sustainable growth to create value for all related parties.

In addition, Air China also holds direct or indirect interests in the following airlines: Air China Cargo Co., Ltd, Shenzhen Airlines Company Limited, Air Macau Company Limited, Beijing Airlines Company Limited, Dalian Airlines Company Limited, Cathay Pacific Airways Limited and Shandong Airlines Co., Ltd.

# Contents

# Corporate Information

## REGISTERED CHINESE NAME
中國國際航空股份有限公司

## ENGLISH NAME
Air China Limited

## REGISTERED OFFICE
9/F, Blue Sky Mansion
28 Tianzhu Road
Zone A, Tianzhu Airport Economic Development Zone
Shunyi District
Beijing
China

## PRINCIPAL PLACE OF BUSINESS IN HONG KONG
5th Floor, CNAC House
12 Tung Fai Road
Hong Kong International Airport
Hong Kong

## WEBSITE ADDRESS
www.airchina.com.cn

## DIRECTORS
Wang Changshun
Wang Yinxiang
Cao Jianxiong
Sun Yude
Christopher Dale Pratt
Ian Sai Cheung Shiu
Cai Jianjiang
Fan Cheng
Fu Yang
Li Shuang
Han Fangming
Yang Yuzhong

## SUPERVISORS
Li Qinglin
Zhang Xueren
Zhou Feng
Xiao Yanjun
Su Zhiyong

## LEGAL REPRESENTATIVE OF THE COMPANY
Wang Changshun

## JOINT COMPANY SECRETARIES
Rao Xinyu
Tam Shuit Mui

## AUTHORISED REPRESENTATIVES
Cai Jianjiang
Tam Shuit Mui

## LEGAL ADVISERS TO THE COMPANY
Haiwen & Partners *(as to PRC Law)*
Sullivan & Cromwell *(as to Hong Kong and English Law)*

## INTERNATIONAL AUDITORS
Ernst & Young

## H SHARE REGISTRAR AND TRANSFER OFFICE
Computershare Hong Kong Investor Services Limited
Rooms 1712-1716, 17th Floor
Hopewell Centre
183 Queen's Road East
Wanchai
Hong Kong

## LISTING VENUES
Hong Kong, London and Shanghai

# Summary of Financial Information

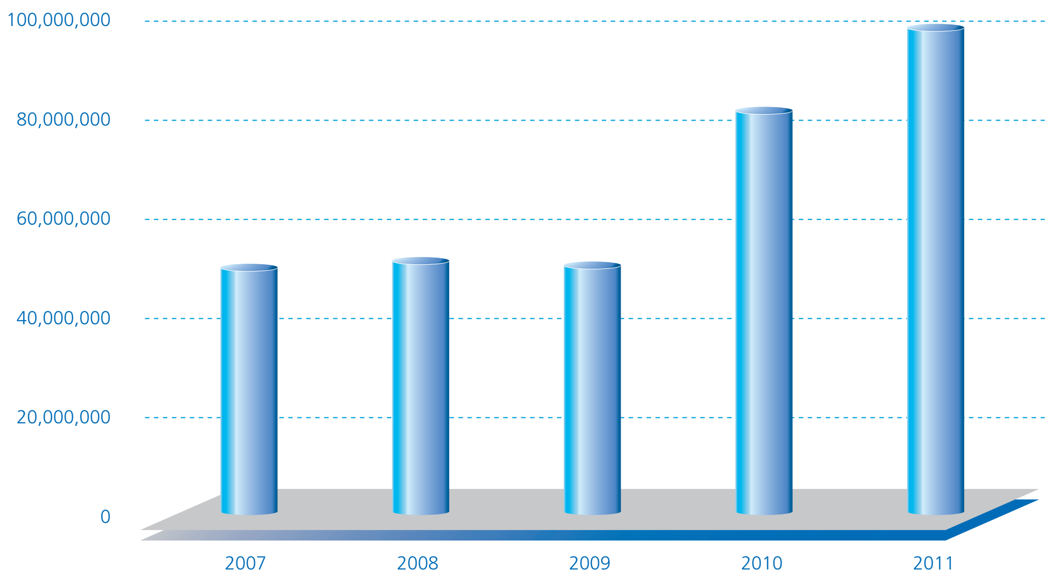
*(RMB'000)*

| | **2011** | 2010 | 2009 | 2008 | 2007 |
|---|---|---|---|---|---|
| Turnover | **98,409,502** | 82,487,539 | 51,393,191 | 52,908,161 | 51,081,667 |
| Profit from operations | **6,258,661** | 10,927,521 | 5,500,956 | (9,806,971) | 3,912,123 |
| Profit before tax | **9,354,739** | 14,833,612 | 5,066,285 | (10,977,680) | 5,448,165 |
| Profit after tax (including profit attributable to non-controlling interests) | **7,062,666** | 12,335,864 | 4,803,051 | (9,367,030) | 3,935,552 |
| Profit attributable to non-controlling interests | **(19,708)** | 330,860 | (51,183) | (111,208) | (110,661) |
| Profit attributable to owners of the Company | **7,082,374** | 12,005,004 | 4,854,234 | (9,255,822) | 4,046,213 |
| EBITDA[1] | **15,819,568** | 19,496,891 | 12,552,228 | (3,441,696) | 9,466,566 |
| EBITDAR[2] | **20,420,033** | 23,696,910 | 15,349,155 | (593,230) | 12,017,187 |
| Earnings per share attributable to equity holders of the Company (RMB) | **0.58** | 1.03 | 0.41 | (0.78) | 0.34 |
| Return on equity attributable to owners of the Company (%) | **15.36** | 28.97 | 20.30 | (46.41) | 13.22 |

(1) EBITDA represents earnings before finance revenue, finance costs, enterprise income taxes, profits resulting from sale of associates, share of profits and losses of associates, depreciation and amortisation as computed under the IFRSs.

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

**Turnover** (RMB'000)



# Summary of Financial Information

*(RMB'000)*

| | **31 December 2011** | 31 December 2010 | 31 December 2009 | 31 December 2008 | 31 December 2007 |
|---|---|---|---|---|---|
| Total assets | **175,850,072** | 158,769,531 | 107,919,022 | 100,401,224 | 91,300,277 |
| Total liabilities | **127,524,637** | 117,398,294 | 83,964,555 | 79,944,718 | 60,548,027 |
| Non-controlling interests | **2,209,636** | (66,717) | 38,571 | 513,654 | 138,050 |
| Equity attributable to equity holder of the Company | **46,115,799** | 41,437,954 | 23,915,896 | 19,942,852 | 30,614,200 |
| Equity attributable to owners of the Company per share (RMB) | **3.79** | 3.56 | 2.02 | 1.68 | 2.58 |

**Total assets** (RMB'000)

# Summary of Operating Data

The following summary includes the operating data of the Company, Air China Cargo, Shenzhen Airlines, Air Macau, Beijing Airlines and Dalian Airlines. Among which, the statistic data of Shenzhen Airlines includes those of Kunming Airlines. As Shenzhen Airlines only became a subsidiary of the Group since 20 April 2010, accordingly statistic data of Shenzhen Airlines for the 2010 period only included data collected from 20 April 2010 to 31 December 2010.

| | 2011 | 2010 | Change |
|---|---|---|---|
| **Traffic** | | | |
| **RPK (in millions)** | 123,499.47 | 105,694.99 | 16.85% |
| International | 35,724.19 | 33,206.63 | 7.58% |
| Domestic | 82,676.09 | 67,839.75 | 21.87% |
| Hong Kong, Macau and Taiwan | 5,099.20 | 4,648.61 | 9.69% |
| **RFTK (in millions)** | 4,847.63 | 4,840.90 | 0.14% |
| International | 3,427.48 | 3,583.74 | (4.36%) |
| Domestic | 1,323.22 | 1,154.99 | 14.57% |
| Hong Kong, Macau and Taiwan | 96.93 | 102.17 | (5.13%) |
| **Passengers carried (in thousands)** | 69,691.73 | 60,006.20 | 16.14% |
| International | 7,121.88 | 6,944.98 | 2.55% |
| Domestic | 59,391.47 | 50,185.69 | 18.34% |
| Hong Kong, Macau and Taiwan | 3,178.38 | 2,875.53 | 10.53% |
| **Cargo and mail carried (tonnes)** | 1,426,086.62 | 1,347,267.42 | 5.85% |
| **Kilometres flown (in millions)** | 873.11 | 767.37 | 13.78% |
| **Block hours (in thousands)** | 1,386.27 | 1,218.36 | 13.78% |
| **Number of flights** | 490,913 | 435,371 | 12.76% |
| International | 50,254 | 48,551 | 3.51% |
| Domestic | 413,557 | 362,107 | 14.21% |
| Hong Kong, Macau and Taiwan | 27,102 | 24,713 | 9.67% |
| **RTK (in millions)** | 15,868.94 | 14,294.41 | 11.01% |
| **Capacity** | | | |
| **ASK (in millions)** | 151,589.87 | 132,074.76 | 14.78% |
| International | 45,298.99 | 41,476.98 | 9.21% |
| Domestic | 99,401.93 | 84,370.14 | 17.82% |
| Hong Kong, Macau and Taiwan | 6,888.94 | 6,227.64 | 10.62% |
| **AFTK (in millions)** | 8,174.61 | 7,843.37 | 4.22% |
| International | 5,351.52 | 5,254.06 | 1.86% |
| Domestic | 2,572.06 | 2,369.04 | 8.57% |
| Hong Kong, Macau and Taiwan | 251.03 | 220.28 | 13.96% |
| **ATK (in millions)** | 21,845.35 | 19,740.75 | 10.66% |

# Summary of Operating Data

| | 2011 | 2010 | Change |
|---|---|---|---|
| **Load factor** | | | |
| **Passenger load factor (RPK/ASK)** | 81.47% | 80.03% | 1.44ppts |
| International | 78.86% | 80.06% | (1.20ppts) |
| Domestic | 83.17% | 80.41% | 2.77ppts |
| Hong Kong, Macau and Taiwan | 74.02% | 74.64% | (0.62ppts) |
| **Cargo and mail load factor (RFTK/AFTK)** | 59.30% | 61.72% | (2.42ppts) |
| International | 64.05% | 68.21% | (4.16ppts) |
| Domestic | 51.45% | 48.75% | 2.69ppts |
| Hong Kong, Macau and Taiwan | 38.61% | 46.38% | (7.77ppts) |
| **Yield** | | | |
| **Yield per RPK (RMB)** | 0.68 | 0.64 | 6.25% |
| International | 0.57 | 0.57 | 0% |
| Domestic | 0.72 | 0.67 | 7.46% |
| Hong Kong, Macau and Taiwan | 0.76 | 0.79 | (3.80%) |
| **Yield per RFTK (RMB)** | 1.79 | 1.85 | (3.24%) |
| International | 1.81 | 1.64 | 10.37% |
| Domestic | 1.49 | 2.29 | (34.93%) |
| Hong Kong, Macau and Taiwan | 4.95 | 5.01 | (1.20%) |
| **Fleet** | | | |
| Total number of aircraft in service at year end | 432 | 393 | 39 |
| Daily utilisation (block hours per day per aircraft) | 9.58 | 9.71 | (0.13 hour) |
| **Unit cost** | | | |
| Operating cost per ASK (RMB) | 0.61 | 0.54 | 12.96% |
| Operating cost per ATK (RMB) | 3.13 | 3.46 | (9.54%) |

# Chairman's Statement

**Wang Changshun**
*Chairman*

The market conditions for the aviation industry in 2011 were very complicated. Some prominent characteristics include the relatively rapid growth in the domestic air passenger market, continuing recession in the international air passenger market and significant decline in air cargo operations. At the same time, jet fuel price remained high and domestic and international competition intensified, all of which had put great pressure on our operations. The Group adhered to a strategy of continuing development by steady and prudent operation and implementation and achieved progress in various areas. We have strengthened our operation management, adopted an active stance towards market changes, consolidated our cost advantages and continued to improve service quality. During the reporting period, we recorded a turnover of RMB98,410 million and profit attributable to equity holders of RMB7,082 million, representing a year-on-year increase of 19.30% and a year-on-year decrease of 41%, respectively.

**Further strengthened position in the domestic market** – In 2011, we took advantage of the growth in the domestic air passenger market and timely adjusted our capacity deployment. This resulted in significant improvement of yield quality and fortified our market position. Our domestic capacity increased to 99,402 million available seat kilometres and we realised 82,676 million RPKs, representing an increase of 17.82% and 21.87%, respectively, from the previous year. We carried 59,391,500 passengers with a passenger load factor of 83.17%, representing an increase of 18.34% and 2.77% over the previous year respectively. Our passenger yield increased by 7.46% to RMB0.72.

**Further enhanced international air passenger operations** – In 2011, our international route capacity reached 45,299 million available seat kilometres and we realised 35,724 million revenue passenger kilometres, representing an increase of 9.21% and 7.58%, respectively, from the previous year. Our passenger load factor fell slightly by 1.2 ppts and our passenger yield maintained the same as that of last year at RMB0.57.

**Fleet optimisation** – We introduced 58 aircraft and retired 19 aircraft, including B757-200 and B737-300 from our fleet. As at the end of 2011, our fleet comprised 432 aircraft with an average age of 6.77 years.

**Steady increase in profitability** – We have actively expanded our key sales and marketing channels, improved our mileage redemption programme for VIP frequent flyer customers and introduced seasonal rates offers. The revenue from our frequent flyer programme recorded a 17% growth from last year. We have focused on building and maintaining relationships with large corporate customers and improved management efficiency of our core customers. Contribution to revenue from our high-value customers, including our global and Star Alliance customers, continued to climb and revenue from our large corporate customers grew by 36% from the previous year. We made steady progress in developing our e-commerce platform and our e-commerce revenue increased by 53% from last year. Meanwhile, we upgraded the software and hardware of our products, refined our profit management and achieved a higher load factor of our first and business class cabins. Our revenue grew by 17% compared to the previous year. In response to the recession in the international passenger market, we continued to optimize capacity structure in a dynamic manner in line with our hub and network strategy. We adjusted the operations of Japan routes after the earthquake in Japan. We also introduced new routes (including Beijing-Milan and Beijing-Dusseldorf routes) and increased the frequency of services on Beijing-Los Angeles route, which have shown positive operating results.

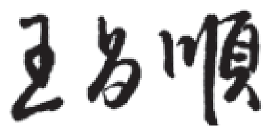
**Customer service enhancement** – We are committed to provide comprehensive, personalised and high quality services to our passengers. 4 environmental-friendly, fuel-efficient and comfortable B777-300ER wide-body aircraft with enhanced safety features were introduced to our fleet. We also upgraded some of our cabin and lounge facilities, integrated our customer service hotlines and improved our website layout. We were the first domestic airline to provide wifi services on selected routes. Our services were accredited with a 4-star ranking by Skytrax and our customer service management system (CSM) was the first in the world to be certified by the British Standards Institution.

# Chairman's Statement

**Comprehensive strategic collaboration** – We strengthened our strategic partnership with Cathay Pacific. Our cargo joint venture was formally established on 18 March 2011 and has been running under a new operation and management model. We deepened our collaboration with Shenzhen Airlines in various areas, including sales and marketing, maintenance, information technology and central procurement. We also established Beijing Airlines which specialises in chartered business jet flights. Our influence in the regional market continued to grow through our investment in Tibet Airlines and the establishment of Dalian Airlines. The synergy from our internal collaboration was eminent and the results of Shenzhen Airlines increased significantly.

**Efforts to improve cargo operations** – Demand in the air cargo market has continued to fall since the second quarter last year. The cargo capacity and the actual output of Air China Cargo went down by 2.9% and 6.4%, respectively, compared to the previous year, and the load factor also decreased by 3ppts from last year to 79.2%. In response to the difficult market conditions, Air China Cargo launched internet-based, customer-based and product-based sales and marketing efforts, actively developing new customer base and improving our service standards. We focused on the development of the Shanghai cargo hub and strengthened the transit support capability at hub terminals. We responded to market changes and expedited the adjustments to our capacity deployment and introduced new routes (including Shanghai (Pudong)-Hong Kong route), reduced our capacity in non-performing long-haul routes, launched short-haul services and relocated our freighters to Shanghai. All of these measures effectively improved our air cargo operations and offsetting losses.

In 2012, the steady and continuous growth in the Chinese economy will bring new opportunities in the aviation industry. However, internal and external factors, including the lack of growth momentum in the European and American economies, the accelerated structural consolidation in the Chinese economy, the increasingly challenging domestic and international economic landscape, aviation resource limitations (including airspace, infrastructure and manpower limitations as well as slot constraints) and the high operating cost of our core business will generate new challenges and greater pressure for the Company. Our Company will fortify our existing customer-oriented value. We will put our management focal points on adopting international best practices, conforming to standards, exercising more fine-tuned management and realising information technology based coverage. We will continue to strengthen our management endeavours as well as hub and network development. We will deploy our capacity effectively in response to market trends. At the same time, we will step up our business process re-engineering and resources consolidation, enhance our strategic collaboration as well as synergise our air passenger and cargo businesses so as to improve our strengths and global competitiveness. With the goal of developing the Company into a large network airline with international competitiveness, we will continue to create new competitive edges, strive for stronger results and achieve new milestones.



**Wang Changshun**
*Chairman*

Beijing, PRC
27 March 2012

In 2011, the Group's ATKs reached 21.845 billion and RTKs reached 15.869 billion, representing an increase of 10.66% and 11.01% over the previous year, respectively. The Group's overall load factor was 72.64%, representing an increase of 0.23 ppts from 2010.

## DEVELOPMENT OF FLEET

In 2011, we introduced 58 aircraft, including 4 B777-300ER, 19 B737-800, 5 A330 and 23 A320 series, and retired 19 old aircraft, including B757-200 and B737-300. As at the end of 2011, our fleet comprised 432 aircraft with an average age of 6.77 years.

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

| | As of 31 December 2011 | | | | | Introduction plan | | |
|---|---|---|---|---|---|---|---|---|
| | Subtotal | Self-owned | Finance leased | Operating leased | Average age | 2012 | 2013 | 2014 |
| **Passenger aircraft** | **411** | **203** | **96** | **112** | **6.56** | **52** | **56** | **55** |
| **Airbus series** | **183** | **78** | **67** | **38** | **4.55** | **28** | **24** | **18** |
| A319 | 43 | 24 | 9 | 10 | 6.90 | 0 | 0 | 0 |
| A320/A321 | 106 | 42 | 41 | 23 | 3.38 | 22 | 17 | 10 |
| A330 | 28 | 6 | 17 | 5 | 3.45 | 6 | 7 | 8 |
| A340 | 6 | 6 | 0 | 0 | 13.56 | 0 | 0 | 0 |
| **Boeing series** | **228** | **125** | **29** | **74** | **8.22** | **24** | **32** | **37** |
| B737 | 190 | 93 | 23 | 74 | 7.16 | 18 | 26 | 32 |
| B747 | 9 | 8 | 1 | 0 | 14.74 | 0 | 0 | 2 |
| B757 | 10 | 10 | 0 | 0 | 16.99 | 0 | 0 | 0 |
| B767 | 5 | 5 | 0 | 0 | 16.91 | 0 | 0 | 0 |
| B777 | 14 | 9 | 5 | 0 | 8.60 | 6 | 6 | 3 |
| **Freighters** | **12** | **8** | **0** | **4** | **17.29** | **2** | **0** | **0** |
| B747F | 10 | 8 | 0 | 2 | 17.17 | 2 | 0 | 0 |
| A300F | 2 | 0 | 0 | 2 | 17.90 | 0 | 0 | 0 |
| **Business jet** | **9** | **0** | **0** | **9** | **2.22** | **2** | **0** | **0** |
| **Total** | **432** | **211** | **96** | **125** | **6.77** | **56** | **56** | **55** |

Among the total number of aircraft of our Group, the Company operated a fleet of 288 aircraft in total (exclusive of those wet leased) with an average age of 7.03 years. During the year, the Company introduced 32 aircraft and retired 10 aircraft.

During 2011, the Company has achieved new developments in hub construction, marketing, product innovation and service improvement.

# Business Overview


## HUB NETWORK

The Company continued to strengthen our market position at the Beijing hub. As at the end of 2011, the number of our aircraft serving the Beijing hub amounted to 173. The number of transit passengers at the Beijing hub reached 4.5 million during the year. The operation control capability at the Beijing Hub Control Centre (HCC) continued to improve and operational quality steadily enhanced. In addition, the number of our aircraft serving the Chengdu hub was 47. By securing key resources including additional flight schedules, transit counters at Terminal 2 as well as lounge facilities for our first and business class passengers, the operational support capability of the Chengdu hub further strengthened. The number of our aircraft serving the Shanghai gateway was 34 as we saw gradual improvements in the support capability for flights, operations and maintenance at the Shanghai gateway.

In 2011, the Company introduced 20 domestic routes, including Chengdu – Ningbo and Chengdu – Yiwu routes, and eight international and regional routes, including Beijing – Milan, Beijing – Phuket and Chengdu – Tokyo routes.

As at 31 December 2011, the number of air passenger routes operated by the Company reached 282, among which 71 were international routes, 14 were regional routes, 197 were domestic routes, covering 30 countries and regions and 143 cities, including 43 international cities, 4 regional cities and 96 domestic cities.

## MARKETING

In response to the changing market conditions and competitive landscape, the Company proactively launched new marketing channels, further improving its marketing capability. With respect to frequent flyers, our air mileage data bank was upgraded comprehensively to provide more options for air mileage consumption and more convenient services for our frequent flyers. During the year, our frequent flyers increased by 2.77 million, reaching a total of 17.44 million. The revenue derived from our frequent flyers amounted to RMB19.51 billion, representing a year-on-year increase of 24.2%. The steady progress in constructing our e-commerce platform as well as the introduction of a new online booking system and one-stop comprehensive sales hotline contributed to our growth in revenue. Our e-commerce revenue reached RMB9.6 billion for the year, representing an increase of 53.2% from the previous year. In addition, the Company focused on improving management efficiency of its key customers and achieved remarkable results in building and maintaining relationships with them, consequently, the revenue from our key customers reached RMB12 billion for the year, representing a year-on-year increase of 35.5%. Further, the Company upgraded the software and hardware of our products, refined our profit management, leading to an increase in our revenue in first and business class cabins resulting in a year-on-year growth of 17% in revenue.

## PRODUCTS AND SERVICES

In 2011, the Company established a Customer Service Management (CSM) system applicable to the entire air passenger service chain and carried out service upgrades in various areas such as e-commerce, facilities and equipment in passenger cabins and lounges, with a view of enhancing passenger's experience. The following measures were implemented: integration of our customer service hotlines and standardisation of service interface as well as improving our website layout and its service functions. The Company also introduced new and more comfortable B777-300ER aircraft and completed the upgrading and rebuilding of the passenger cabins of 13 A330-200 aircraft. A platform for transmitting information from abnormal flights was established and seamless internal communication on our flight information was achieved initially. We increased our investments in food and beverages, shortened the turnaround time to refresh our menus, enriched the entertainment experience in our cabins, launched portable entertainment facilities and became the first domestic airline to provide wifi services in cabins. We were able to provide significantly improved service quality overall and our customer satisfaction increased steadily. During the year, the Company was accredited with a 4-Star Airline ranking by Skytrax, a world-recognised rating agency on airline services.

## INTEGRATION OF RESOURCES AND OPTIMISATION OF STRATEGIC LAYOUT

In order to diversify our development, we established Beijing Airlines which specialises in chartered business jet flights, expanding our capabilities in chartered flights and sales. We have also established a joint venture airline, Dalian Airlines, and successfully invested in Tibet Airlines. Through these measures, we have improved our strategic market positioning in the northeastern market and resource deployment and built a platform for exerting our influence in the regional market.

The synergy from our collaboration with Shenzhen Airlines have started to surface. Our influence in the southern China market improved and our market share increased through our collaboration in flight schedules and capacity deployment. We deepened our sales and marketing cooperation with Shenzhen Airlines and improved our network value efficiently. In addition, we have started cooperating in areas including maintenance, information technology and central procurement. Our revenue attributable to collaborative efforts increased by RMB1,600 million.

We continued to deepen and expand our cooperation with Cathay Pacific, resulting in a mutual increase in competitiveness on the Mainland – Hong Kong routes. Our joint venture with Cathay Pacific, Air China Cargo, was formally established on 18 March 2011. The new joint venture would allow us to complement each other and combine our operation management experience, while focusing on developing Air China Cargo to become the first choice cargo carrier for inbound and outbound customers in China.

The Company had proactively used the Star Alliance platform, explored our customer resources and at the same time, promoted product and services integration. We continued to enhance our cooperation with our Star Alliance partners, such as Lufthansa and United Airlines and increased our revenue attributable to the alliance. In 2011, the revenue attributable to Star Alliance was RMB2,300 million, representing a year-on-year growth of 6.9%.

## ENVIRONMENTAL PROTECTION

Our Company adhered to a principle of "Sustainable Development through Green Operation" and effectively managed the unfavourable environmental effects from our operations. We are committed to continuously improve our efficiency, reduce our emissions and conserve energy. We have built a multi-tier energy conservation and emission reduction management system and adopted various measures to improve our fuel efficiency. We have also strengthened our pollutants recycling efforts and launched various promotional campaigns and training programmes for our staff members to increase their environmental awareness. In 2011, the Company conducted a successful trial flight using bio-fuel on an active aircraft for the first time in China, launching a low-carbon environmentally-friendly initiative.

## SOCIAL WELFARE

Our Group is fully committed to our social responsibilities and provided flying services during emergencies and special situations. We were proactive in emergency situations, such as the evacuation of Chinese nationals from Egypt and Libya and the rescue mission following the Japanese earthquake, and provided chartered flights services successfully while taking the overall circumstances into account. We are dedicated to social welfare, supporting educational development, assisting the disadvantaged group and launching volunteering services to promote harmony between the society and our corporate development. As one of the promoters of the Chinese Children Special Insurance Fund, we will continue to raise donations for the fund and our donations, together with the contributions from our passengers, amounted to approximately RMB987,400 in 2011.

## MAJOR SUBSIDIARIES

### Air China Cargo

Air China Cargo was established in 2003. In 2011, Air China completed the cargo joint venture project with Cathay Pacific based on the platform of the former Air China Cargo, pursuant to which Air China holds a 51% shareholding in the new joint venture company.

As at 31 December 2011, Air China Cargo operated a fleet of 10 aircraft in total with an average age of 17.17 years. During the year, a new aircraft was introduced and an aircraft retired from its fleet.

Air China Cargo operates a total of 17 routes, including 3 domestic routes, 12 international routes and 2 regional routes. Air China Cargo's flights cover 10 countries and regions and 20 cities, including 5 domestic cities, 13 international cities and 2 regional cities.

In 2011, affected by weak market demand and the significant increase in oil prices, the overall operation of Air China Cargo underperformed. During the year, the AFTKs of Air China Cargo reached 7,578 million, representing an increase of 2.0% from 2010. It achieved cargo and mail traffic of 4,416 million RFTKs, representing a year-on-year decrease of 2.5%. The volume of cargo and mail carried increased by 0.1% from 2010 to 1,148,900 tonnes and the cargo and mail load factor decreased by 2.7 ppts from 2010 to 58.27% in 2011.

In 2011, Air China Cargo's turnover was RMB8,087 million, decreased by 5.76% from 2010. Among which, cargo and mail transportation revenue was RMB7,726 million, representing a year-on-year decrease of 5.97%. During the year, Air China Cargo incurred a loss of RMB924 million, as compared to a profit of RMB592 million last year.

### Shenzhen Airlines

Shenzhen Airlines was established in 1992, with its principal operating base located in Shenzhen. Its main business activity is the operation of passenger and cargo transportation business. Air China increased its shareholding in Shenzhen Airlines by way of a capital injection in 2010 and is currently holding 51% equity interest of Shenzhen Airlines.

As at 31 December 2011, Shenzhen Airlines operated a fleet of 110 aircraft in total with an average age of 4.78 years. During the year, 19 aircraft were introduced to the fleet and 9 aircraft retired.

Shenzhen Airlines operates 136 routes, including 126 domestic routes, 5 international routes and 5 regional routes, covering destinations across 5 countries and regions and 63 cities, including 57 domestic cities, 3 international cities and 3 regional cities.

Benefiting from the steady increase in domestic passenger market demand and the synergy gradually appearing from the extensive cooperation with Air China, the ASKs of Shenzhen Airlines reached 34,192 million in 2011, representing a year-on-year increase of 12.5%. Its passenger traffic was 28,062 million RPKs in 2011, representing a year-on-year increase of 15.1%. Shenzhen Airlines carried 19,633,600 passengers, representing a year-on-year increase of 11.8%. Its average passenger load factor was 82.07%, representing an increase of 1.9 ppts from the previous year.

The AFTKs of Shenzhen Airlines reached 529 million, representing a year-on-year increase of 0.9%. In total, 407 million RFTKs of cargo and mail were carried, representing a year-on-year increase of 9.8%. The amount of cargo and mail carried by Shenzhen Airlines was 259,100 tonnes in 2011, representing a year-on-year increase of 9.4%, while the cargo and mail load factor was 76.83%, representing an increase of 6.1 ppts from the previous year.

In 2011, Shenzhen Airlines recorded a turnover of RMB21,747 million, representing a year-on-year increase of 19.96%. Among which, air traffic revenue was RMB20,565 million, representing a year-on-year increase of 20.38%. The profit for the period was 672 million, representing a year-on-year decrease of 25.44%.

# Business Overview

## Air Macau

Air Macau was established in 1994 and is an airline based in Macau. Air China holds 66.9% equity interest in Air Macau.

As at 31 December 2011, Air Macau operated a fleet of 13 aircraft (excluding three aircraft wet leased to Air China) with an average age of 12.89 years.

Air Macau operated 19 flight routes, covering 18 cities in Japan, Korea, Singapore, Thailand, Taiwan and Mainland China.

In 2011, Air Macau's ASKs reached 3,396 million, representing a year-on-year increase of 9.4%. Its passenger traffic was 2,233 million RPKs, representing a year-on-year increase of 2.2%. It carried 1,386,400 passengers with an average load factor of 65.75%, representing an increase of 1.6% and a decrease of 4.6 ppts respectively compared with the previous year.

In terms of air cargo, Air Macau's AFTKs reached 66 million, representing a year-on-year decrease of 12.8%. In total, 25 million RFTKs of cargo and mail were carried, representing a year-on-year decease of 35.5%. During the period, it carried 18,200 tonnes of cargo and mail, representing a year-on-year decrease of 31.8%, while the cargo and mail load factor was 38.28%, representing a year-on-year decrease of 13.5 ppts.

In 2011, Air Macau recorded a turnover of RMB2,365 million, representing a year-on-year increase of 8.83%. Among which, air traffic revenue was RMB2,062 million, representing a year-on-year increase of 16.03%. The profit for the period was RMB212 million, representing a year-on-year increase of 1.92%.

## Dalian Airlines

Dalian Airlines was established on 1 August 2011 with 80% of its equity interest held by Air China.

On 31 December 2011, Dalian Airlines successfully launched its first flight on Dalian – Shenzhen route. As at 31 December 2011, Dalian Airlines operated two aircraft and three routes, being Dalian-Beijing, Dalian-Shenzhen and Dalian-Taiyuan-Sanya.

Dalian Airlines will implement its regional aviation hub strategy in Dalian and will strive to establish an air traffic network corresponding to its position to become the gateway in the northeast China within 5 years.

## Beijing Airlines

Beijing Airlines was established on 28 February 2011 with 51% of its equity interest held by Air China.

As at 31 December 2011, Beijing Airlines operated a fleet of 9 entrusted business jets with an average age of 2.22 years.

With its operation base in Beijing and starting with the business of the former business jet subsidiaries of Air China, Beijing Airlines has made full use of its resource advantages, such as well-established flight operation capacity, marketing networks, airworthiness maintenance capacity and global airport supporting capacity, with the target of developing its domestic and international business jet and charter flight business.

# Business Overview

## PROSPECT

The Company will face great pressure and many challenges in 2012. The global economic landscape will become more complicated with the slow recovery of the US economy and the worsening European debt crisis. There are obviously increasing risk in the aviation market as the competition among carriers in China in the domestic market intensifies, and flight frequency to and from China by overseas airlines increases. The competition for core resources, such as flight schedules, airspace and pilots among China's civil aviation players, will become more intense. Highways and high-speed railways also pose real threats to medium and short-haul business in the aviation industry. In addition, other uncertainties, including exchange rates fluctuation, will increase the operating pressure of the Company.

Despite the factors above, benefiting from the stable and steady growth in the Chinese economy and the national economic policies of boosting consumer demand and steady development of foreign trade, the domestic aviation industry will maintain a sustainable growth as Air China enters a strategic development phase.

In 2012, the Company will adhere to the business strategy of international development, actively strengthening and expanding the domestic and international markets, improving its routes network, accelerating the construction of aviation hubs, optimising the allocation of core resources and improving resource utilisation efficiency while continuing to strengthen safety management. The Company will strive to improve its global competitiveness using its global insight, strategic thinking and customer-orientation. Meanwhile, the Company will affirm its principle of offering passenger-oriented services, strengthening its products and services development capability, and striving to promote the development of comprehensive products and services.

# Management's Discussion and Analysis of Financial Position and Operating Results

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

## PROFIT ANALYSIS

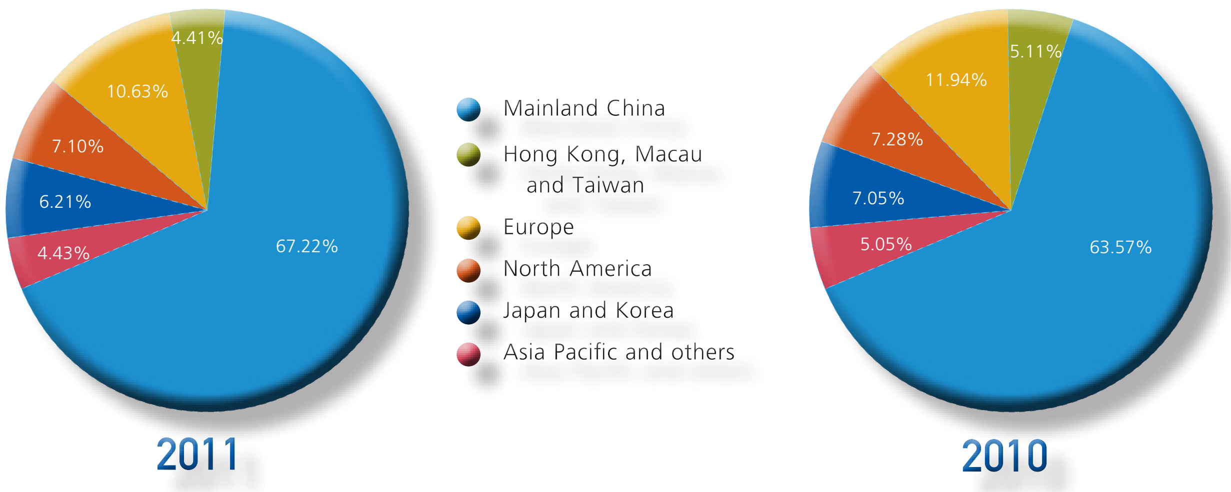
In 2011, we took advantage of the growth in the domestic air passenger market and adopted various measures including precise production organisation, innovative sales and marketing efforts, exploitation of cost potential and internal strategic collaboration with our associated companies. We recorded an operating profit of RMB6,259 million, profit attributable to equity holders of RMB7,082 million and an earning-per-share of RMB0.58 despite the continued recession in the air cargo and international air passenger markets, high international jet fuel prices and intensification of market competition.

## TURNOVER

In 2011, the Group's total turnover (net of business taxes and surcharges of RMB2,268 million) was RMB98,410 million, representing an increase of RMB15,922 million or 19.30% as compared with that of the previous year. Revenue from our air traffic operations contributed RMB93,343 million to the total turnover, representing an increase of RMB15,134 million or 19.35% over last year, primarily due to the rapid growth in the domestic air passenger market and our increased capacity deployment. Our other operating revenue was RMB5,066 million, representing a year-on-year increase of RMB788 million or 18.41%, mainly attributable to the revenue increase from ground services and aircraft engine repair and maintenance.

## REVENUE CONTRIBUTION BY GEOGRAPHICAL SEGMENTS

| | **2011** | | 2010 | | Change |
|---|---|---|---|---|---|
| *(RMB'000)* | **Amount** | **Percentage** | Amount | Percentage | |
| Mainland China | **66,154,716** | **67.22%** | 52,441,112 | 63.57% | 26.15% |
| Hong Kong, Macau and Taiwan | **4,335,880** | **4.41%** | 4,212,616 | 5.11% | 2.93% |
| Europe | **10,464,556** | **10.63%** | 9,848,721 | 11.94% | 6.25% |
| North America | **6,984,158** | **7.10%** | 6,008,965 | 7.28% | 16.23% |
| Japan and Korea | **6,110,530** | **6.21%** | 5,818,381 | 7.05% | 5.02% |
| Asia Pacific and others | **4,359,662** | **4.43%** | 4,157,744 | 5.05% | 4.86% |
| Total | **98,409,502** | **100.00%** | 82,487,539 | 100.00% | 19.30% |



# Management's Discussion and Analysis of Financial Position and Operating Results

## AIR PASSENGER REVENUE

In 2011, the Group recorded an air passenger revenue of RMB83,510 million, representing an increase of RMB15,373 million from 2010. The revenue increases from our increased capacity deployment, higher passenger load factor and improved passenger yield were RMB9,988 million, RMB3,970 million and RMB1,415 million, respectively, all of which contributed to our air passenger revenue increase. The Group's 2011 capacity deployment, passenger load factor and passenger yield per unit are as follows:

| | **2011** | 2010 | Change |
|---|---|---|---|
| Available seat kilometres (million) | **151,590** | 132,075 | 14.78% |
| Passenger load factor (%) | **81.47** | 80.03 | 1.44ppts |
| Yield per RPK (RMB) | **0.68** | 0.64 | 6.25% |

## AIR PASSENGER REVENUE CONTRIBUTED BY GEOGRAPHICAL SEGMENTS

| | **2011** | | 2010 | | Change |
|---|---|---|---|---|---|
| *(RMB'000)* | **Amount** | **Percentage** | Amount | Percentage | |
| Mainland China | **59,120,211** | **70.79%** | 45,515,250 | 66.80% | 29.89% |
| Hong Kong, Macau and Taiwan | **3,855,927** | **4.62%** | 3,661,208 | 5.37% | 5.32% |
| Europe | **6,612,011** | **7.92%** | 6,348,204 | 9.32% | 4.16% |
| North America | **5,032,417** | **6.03%** | 4,052,842 | 5.95% | 24.17% |
| Japan and Korea | **5,173,573** | **6.19%** | 4,910,183 | 7.21% | 5.36% |
| Asia Pacific and others | **3,716,184** | **4.45%** | 3,649,985 | 5.35% | 1.81% |
| Total | **83,510,323** | **100.00%** | 68,137,672 | 100.00% | 22.56% |

## AIR CARGO REVENUE

In 2011, the Group's air cargo and mail revenue was RMB9,833 million, representing a decrease of RMB238 million from the previous year. Among the Group's air cargo and mail revenue, increase in capacity deployment contributed to an increase resulted in RMB473 million in revenue, while the decreases in cargo and mail load factor and cargo yield resulted in a decrease in revenue of RMB400 million and RMB311 million, respectively. The capacity deployment, cargo and mail load factor and cargo and mail yield (per unit) in 2011 are as follows:

| | **2011** | 2010 | Change |
|---|---|---|---|
| Available freight tonne kilometres (million) | **8,174.61** | 7,843.37 | 4.22% |
| Cargo and mail load factor (%) | **59.30** | 61.72 | (2.42ppts) |
| Yield per RFTK (RMB) | **1.79** | 1.85 | (3.24%) |

## AIR CARGO AND MAIL REVENUE CONTRIBUTED BY GEOGRAPHICAL SEGMENTS

| | **2011** | | 2010 | | Change |
|---|---|---|---|---|---|
| *(RMB'000)* | **Amount** | **Percentage** | Amount | Percentage | |
| Mainland China | **1,968,424** | **20.02%** | 2,647,511 | 26.29% | (25.65%) |
| Hong Kong, Macau and Taiwan | **479,953** | **4.88%** | 551,408 | 5.47% | (12.96%) |
| Europe | **3,852,545** | **39.18%** | 3,500,517 | 34.76% | 10.06% |
| North America | **1,951,741** | **19.85%** | 1,956,123 | 19.42% | (0.22%) |
| Japan and Korea | **936,957** | **9.53%** | 908,198 | 9.02% | 3.17% |
| Asia Pacific and others | **643,478** | **6.54%** | 507,759 | 5.04% | 26.73% |
| Total | **9,833,098** | **100.00%** | 10,071,516 | 100.00% | (2.37%) |

# Management's Discussion and Analysis of Financial Position and Operating Results

## OPERATING EXPENSES

In 2011, the Group's operating expenses were RMB92,151 million, representing an increase of 28.77% from RMB71,560 million of 2010. The breakdown of the operating expenses is set out below:

| *(RMB'000)* | **2011** Amount | **2011** Percentage | 2010 Amount | 2010 Percentage | Change |
|---|---|---|---|---|---|
| Jet fuel costs | **34,703,369** | **37.66%** | 24,096,078 | 33.67% | 44.02% |
| Profits and losses resulting from movements in fair value of fuel derivative contracts | **(85,447)** | **(0.09%)** | (1,954,071) | (2.73%) | (95.63%) |
| Take-off, landing and depot charges | **8,740,822** | **9.48%** | 7,707,019 | 10.77% | 13.41% |
| Depreciation | **9,560,907** | **10.37%** | 8,569,370 | 11.97% | 11.57% |
| Aircraft maintenance, repair and overhaul costs | **2,612,678** | **2.84%** | 2,577,185 | 3.60% | 1.38% |
| Employee compensation costs | **12,270,065** | **13.32%** | 9,851,935 | 13.77% | 24.54% |
| Air catering charges | **2,662,984** | **2.89%** | 2,044,359 | 2.86% | 30.26% |
| Selling expenses | **5,480,514** | **5.95%** | 4,602,745 | 6.43% | 19.07% |
| General and administrative expenses | **2,261,549** | **2.45%** | 1,637,824 | 2.29% | 38.08% |
| Other | **13,943,400** | **15.13%** | 12,427,574 | 17.37% | 12.20% |
| Total | **92,150,841** | **100.00%** | 71,560,018 | 100.00% | 28.77% |

Including:

- Jet fuel costs increased by 44.02% or RMB10,607 million in 2011 as compared to 2010. Jet fuel costs accounted for 37.66% of the operating expenses in 2011 as compared to 33.67% in 2010. The sharp increase in jet fuel costs was primarily due to the continuous fluctuation in high international fuel prices and an increase of fuel consumption resulting from the increase in flight hours. The Group's jet fuel consumption was 4,721,800 tons, representing an increase of 459,700 tons or 10.79% over last year.

- Gains on the fair value movements of fuel derivative contracts amounted to RMB85 million including a recovery of fair value of RMB83 million and an increase in fair value by RMB2 million from the actual settlement of fuel derivative contracts. Such gains decreased by 95.63% as compared with the same period of 2010, mainly due to the combined effect of the gradual reduction in the number of unsettled contracts and continuous fluctuations in high international oil prices.

- Take-off, landing and depot charges increased by RMB1,034 million from last year primarily due to the increase in the number of takeoffs and landings.

- Depreciation expenses increased due to increase in the number of self-owned and leased aircraft during the year.

- Employee compensation costs increased by RMB2,418 million, largely due to the adjustments in remuneration standards, increase in the number of employees and the differences in the reporting periods resulting from the consolidation of Shenzhen Airlines since 20 April 2010.

- Air catering charges increased by RMB619 million, mainly due to the increase in the number of passengers carried, enhancement of service quality as well as increase in raw materials prices.

- Selling expenses increased by RMB878 million as compared with the previous year because of the consequential increase in sales commission resulting from the revenue increase as well as the differences in the reporting periods resulting from the consolidation of Shenzhen Airlines.

- General and administrative expenses increased by RMB624 million as compared to last year because of the increase in the number of research and development projects.

- Other operating expenses included mainly aircraft and engines operating lease expenses, contributions to the civil aviation infrastructure construction fund and ordinary expenses arising from our core air traffic business not included in the aforesaid items.

## FINANCIAL REVENUE AND FINANCIAL COSTS

In 2011, the Group recorded a net exchange gain of RMB3,118 million, representing an increase of RMB1,199 million or 62.43% as compared with the previous year, which was mainly due to the increase in the proportion of US dollars denominated debts as well as the significant appreciation of RMB against US dollars. The Group also incurred an interest expense (including the capitalised portion) of RMB2,197 million, representing a year-on-year increase of RMB588 million, primarily due to the growth in interest-bearing liabilities and finance costs of the Group.

## SHARE OF PROFITS AND LOSSES OF ASSOCIATES

In 2011, the Group's share in the profits of its associates was RMB1,329 million, as compared with RMB3,375 million in 2010, mainly due to the recognition of gains on investment in Cathay Pacific of RMB959 million in this reporting period compared to RMB3,003 million in 2010.

## ANALYSIS OF ASSETS STRUCTURE

As at 31 December 2011, the total assets of the Group amounted to RMB175,850 million, representing an increase of 10.76% from the previous year, among which current assets accounted for RMB23,353 million or 13.28% of the total assets, while non-current assets accounted for RMB152,497 million, or 86.72% of the total assets.

Among the current assets, cash and cash equivalents were RMB15,457 million, accounting for 66.19% of the current assets and representing an increase of 7.33% from the previous year, mainly due to the increase in sales revenue during the year, which in turn led to an increase in cash and bank balances. Accounts receivable amounted to RMB2,701 million, representing a decrease of 12.66% from the previous year, largely due to the tightened control of accounts receivable, shortening our accounts receivable collection period.

Among the non-current assets, the net book value of property, plant and equipment was RMB112,399 million, accounting for 73.71% of the non-current assets and representing an increase of 16.90% from the previous year, which was primarily attributable to the increase in the number of self-owned and leased aircraft.

## ASSETS MORTGAGE

As at 31 December 2011, the Group, pursuant to certain bank loans and finance leasing agreements, has mortgaged certain aircraft and premises with an aggregate net book value of approximately RMB72,244 million (approximately RMB55,885 million as at 31 December 2010), a number of shares in its associates with a market value of approximately RMB4,312 million (approximately RMB7,287 million as at 31 December 2010) and land use rights with a net book value of approximately RMB40 million (approximately RMB40 million as at 31 December 2010). At the same time, the Group had approximately RMB133 million (approximately RMB843 million as at 31 December 2010) in bank deposits pledged as partial security for certain bank loans, operating leases and financial derivatives of the Group.

## CAPITAL EXPENDITURE

In 2011, the Company's capital expenditure amounted to RMB21,168 million, of which the total investment in aircraft and engines was RMB17,369 million, including prepayments of RMB8,576 million for aircraft to be introduced from 2012 onwards.

Other capital expenditure amounted to RMB3,799 million, which was mainly spent on high-cost rotables, aircraft modifications, flight simulators, infrastructure construction, information system building, ground equipment purchase and cash component of the long-term investments.

## EQUITY INVESTMENT

As at 31 December 2011, the Group's equity investment in its associates totalled RMB13,397 million, representing a decrease of 5.58% as compared with the previous year, mainly due to the continuous depreciation of Hong Kong dollars against RMB which affected the currency translation of the Group's equity interest in Cathay Pacific which was denominated in Hong Kong dollars. We have invested RMB11,811 million in Cathay Pacific, RMB786 million in Shandong Aviation and RMB463 million in Shandong Airlines among our equity investments, and these companies recorded a profit of RMB4,570 million, RMB340 million and RMB710 million in 2011, respectively.

## DEBT STRUCTURE ANALYSIS

As at 31 December 2011, the Group's total liabilities were RMB127,525 million, representing an increase of 8.63% from the previous year, among which current liabilities accounted for RMB61,332 million and non-current liabilities accounted for RMB66,193 million, representing 48.09% and 51.91% of the total liabilities, respectively.

Among the current liabilities, interest-bearing debts (including bank and other loans, obligations under finance leases and bills payable) amounted to RMB30,825 million, representing an increase of 9.72% from the previous year. Other advances and payables increased 25.59% from last year to RMB30,506 million, which was mainly due to the increase in accounts payable for major costs resulting from the soaring international oil prices and the increase in the number of flights.

Among the non-current liabilities, interest-bearing debts (including bank and other loans, corporate bonds and obligations under finance leases) amounted to RMB58,590 million, representing an increase of 0.63% from the previous year and maintaining a level similar to that as of the end of 2010.

Details of interests-bearing debts of the Group by currency are set out below:

| | **2011** | | 2010 | | Change |
|---|---|---|---|---|---|
| *(RMB'000)* | **Amount** | **Percentage** | Amount | Percentage | |
| US dollars | **66,323,072** | **74.17%** | 61,265,234 | 70.98% | 8.26% |
| Hong Kong dollars | **5,112,274** | **5.72%** | 5,845,683 | 6.77% | (12.55%) |
| RMB | **17,795,620** | **19.90%** | 18,996,833 | 22.01% | (6.32%) |
| Other | **184,613** | **0.21%** | 206,333 | 0.24% | (10.53%) |
| Total | **89,415,579** | **100.00%** | 86,314,083 | 100.00% | 3.59% |

# Management's Discussion and Analysis of Financial Position and Operating Results

## COMMITMENTS AND CONTINGENT LIABILITIES

The Group's capital commitment decreased from RMB122,085 million as at 31 December 2010 to RMB96,199 million as at 31 December 2011, and was mainly committed for settling the purchase of certain aircraft and related equipment to be delivered in the coming years. The Group had operating lease commitments of RMB16,906 million, representing a decrease of 11.58% as compared with the previous year, which was mainly committed for leasing aircraft and settling the purchase of office premises and related equipment. The Group had investment commitments of RMB35 million, representing a decrease of RMB204 million as compared with 31 December 2010, consisting of the investment commitments made by Shenzhen Airlines to its associate mainly.

Details of the Group's contingent liabilities are set out in note 48 to the Group's 2011 financial statements.

## GEARING RATIO

As at 31 December 2011, the Group's gearing ratio (total liabilities divided by total assets) was 72.52%, representing a decrease of 1.42 ppts from 73.94% as at 31 December 2010, which was mainly attributable to the significant increase in shareholders' equity as a result of improved profitability in 2011. Considering that high gearing ratios are common among aviation enterprises, the Group continued to maintain a relatively better gearing ratio in the domestic aviation industry and long-term insolvency risks are also within control.

## WORKING CAPITAL AND ITS SOURCES

As at 31 December 2011, the Group's net current liabilities (current liabilities minus current assets) were RMB37,978 million, representing an increase of RMB8,570 million as compared with the previous year. The current ratio (current assets divided by current liabilities) was 0.38, representing a decrease of 6 ppts from 0.44 as at 31 December 2010. The increase in net current liabilities was due to the increase in the Group's accounts payable for major costs as well as interest-bearing debts due within one year.

The Group meets its working capital needs mainly through its operating activities and external financing activities. In 2011, the Group's net cash inflow from operating activities was RMB19,670 million, representing an increase of 7.10% from the RMB18,366 million in 2010. Net cash outflow from investment activities was RMB21,669 million, representing an increase of 54.14% from RMB14,058 million in 2010, mainly due to the increase in purchase of aircraft and decrease in unpledged deposits due in three months or above. The Group's net cash outflow from financing activities was RMB1,432 million, representing a decrease of RMB8,895 million from the net cash inflow of RMB7,463 million in 2010, mainly due to the issuance of shares by way of private placement last year as well as the increase in repayment of loans during the reporting period as compared with the previous year. In 2011, the Group's balance of cash and cash equivalents was RMB10,783 million, representing a decrease of approximately RMB3,593 million from the previous year. The Company has obtained bank facilities of RMB141,263 million from a number of banks in the PRC, among which approximately RMB49,902 million has been utilised, sufficient to meet our demand on working capital and future capital commitments.

## FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group is exposed to fluctuations in jet fuel prices in its daily operation. International jet fuel prices are subject to market volatility and fluctuation in supply and demand. The Group's strategy for managing jet fuel price risk aims at controlling the risk arising from the rise in fuel price. The Group has been engaging in fuel hedging transactions since March 2001. The hedging instruments used were 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. As at 31 December 2011, the fuel derivative contracts of the Company all expired, and no new position has been established. Considering the volatility of international prices and cost sensitivity, the Company will continue to develop its fuel hedging business in compliance with the regulatory requirements so as to cope with changes in the jet fuel market.

As at 31 December 2011, the interest-bearing debts of the Group totalled RMB89,416 million, accounting for 70.12% of the Group's total liabilities, most of which were foreign debts, mainly denominated in US dollars, Hong Kong dollars and European dollars. In addition, the Group also had sales revenues and expenses denominated in foreign currencies. The Group endeavoured to minimise any risks relating to foreign exchange rate and interest rate by adjusting the interest rates and denominating currencies structure of its debt and by making use of financial derivatives.

Details of the other financial risk management objectives and polices of the Group's operations are set out in note 53 to the Group's 2011 financial statements.

# Corporate Governance Report

The Company has been maintaining and enhancing the level of its corporate governance so as to ensure greater accountability and transparency and bring long-term return to its shareholders. The Company has complied in all respects with the principles and code provisions of the Code on Corporate Governance Practices (the "Code") under Appendix 14 to the Listing Rules in 2011. The Company's corporate governance practices in 2011 are summarised and discussed below.

## GOVERNANCE STRUCTURE

**Board of Directors of the Company**

(comprising 2 executive directors, 6 non-executive directors and 4 independent non-executive directors)

Specialised Committees under the Board

- Audit and risk control committee (comprising 2 independent non-executive directors and 1 non-executive director)
- Nomination and remuneration committee (comprising 3 independent non-executive directors and 2 non-executive directors )
- Strategy and investment committee (comprising 3 non-executive directors and 1 executive director)
- Aviation safety committee (comprising 1 non-executive director and 1 executive director)

## MAJOR CORPORATE GOVERNANCE PRINCIPLES AND PRACTICES OF THE COMPANY

### A. Directors

***The Board must include at least three independent non-executive directors***

- As at 31 December 2011, the Board comprised 12 Directors, out of which four were independent non-executive directors. The Directors are elected at the shareholders' general meeting for a three-year term of office, and are eligible for re-election upon expiry of the term.

- Pursuant to the Listing Rules, each of the independent non-executive directors has confirmed his independence with the Hong Kong Stock Exchange. As at 31 December 2011, the Company had already received from all independent non-executive directors the annual statements concerning their independence in which each of the independent non-executive directors re-confirmed his or her independence. The Company considers all independent non-executive directors as independent within the meaning of Rule 3.13 of the Listing Rules.

Deviation: Nil

***The Directors shall have a balance of skills and experience appropriate for the requirements of the business of the Company***

- The Directors have extensive expertise and experience in the fields of aviation, finance and financial management and provide substantial support for the effective performance of the Board.

- The list of the Directors and their biographical details and respective roles on the Board and specialised committees under the Board are set out in this annual report and published on the Company's website.

Deviation: Nil

***Distinguished roles of the Chairman and President***

- The Chairman, concurrently a non-executive director, is responsible for leading the Board and ensuring the Board's efficient operation and that all major and relevant issues are discussed by the Board in a prompt and constructive manner.
- The Chairman shall be elected and dismissed by a majority of the Directors. The term of office of the Chairman shall be three years, and the Chairman is eligible for re-election and re-appointment upon expiry of the term.
- The Company has a President who shall be nominated, appointed or dismissed by the Board.
- The President is authorised to oversee the Group's business and implement its strategies to attain overall commercial goals.

Deviation: Nil

***Non-executive directors shall be appointed for a specific term, and all Directors appointed to fill a casual vacancy shall be subject to election by shareholders at the first general meeting after their appointment***

- The term of office of the existing non-executive directors is three years upon election at the shareholders' general meeting.

Deviation: Nil

***The Board shall assume responsibility for the leadership and control of the Company and be collectively responsible for promoting the success of the Company***

- The Board is accountable to the shareholders' general meeting and determines the investment proposals of the Company and disposals of the Company's fixed assets according to the authorisation of the shareholders' general meeting. The Company formulated the "Rules and Procedures for Shareholders' General Meetings", "Rules and Procedures for Board Meetings" and "Rules and Procedures for Senior Management Meetings". Pursuant to the Articles of Association, the main responsibilities of the Board are: to decide on the Company's business policies and investment plans; to formulate the Company's annual budget and final accounts; to formulate the Company's profit distribution proposals and loss recovery proposals; to decide on the establishment of the Company's internal management bodies; to appoint or dismiss the President of the Company, Secretary to the Board, and, according to the nomination by the President, to appoint or dismiss the Vice President, Chief Accountant, Chief Pilot and other senior management of the Company; and to exercise other functions and powers as stipulated in the Articles of Association and granted by the shareholders' general meeting.
- The President shall be authorised by the Board to implement various strategies and oversee the day-to-day operations of the Company.
- The Board shall have independent access to the senior management personnel for enquiries in relation to the Company's management.
- The Board shall have specialised committees to provide support to the Board in its decision-making.

Deviation: Nil

***Besides the work relationships in the Company, there was no financial, business, family relationship or other material relationships among the Directors, Supervisors and senior management***

Deviation: Nil

***The Board shall meet regularly to carry out its duties. The Board and its committees shall be provided with adequate information in a timely manner***

- Board meetings are held regularly throughout the year and generally include annual meetings, interim meetings and meetings for the first and third quarters. Board meetings shall be convened by the Chairman and a 14-day notice shall be served to all Directors before each meeting. The meetings may be attended through personal participation or other electronic means of communication.

- The Secretary to the Board shall be responsible for the communications and liaison with all Directors from the time the notice is served to the commencement of the meeting, and shall provide in a timely manner necessary information to the Directors to facilitate their decision-making on matters set out in the agenda.

- For the purpose of considering resolutions or matters during Board meetings, the Directors may require the presence of the persons-in-charge of the relevant departments at the Board meetings to answer queries, so that the Directors can have a thorough understanding of the key issues and the general situation.

- All Directors shall have access to the Secretary to the Board. Under the leadership of the Board and the Chairman, the Secretary to the Board shall take the initiative to acquaint him/herself with the implementation progress of the Board resolutions, and report to and advise the Board and the Chairman in a timely manner on major issues arising in the course of implementation.

- Minutes of Board meetings shall be kept by the Secretary to the Board and made available for inspection by any Director at any time.

- All Directors have actively participated in the business operations of the Company. Attendance of all Directors at Board meetings in 2011 was as follows:

| **No. of meetings** | **15** | |
|---|---|---|
| **Non-executive directors** | | |
| Wang Changshun *(Chairman) (appointed on 20 January 2012)* | N/A | N/A |
| Kong Dong *(Chairman) (resigned on 20 January 2012)* | 15/15 | 100% |
| Wang Yinxiang | 15/15 | 100% |
| Cao Jianxiong | 15/15 | 100% |
| Sun Yude | 15/15 | 100% |
| Christopher Dale Pratt | 15/15 | 100% |
| Ian Sai Cheung Shiu | 15/15 | 100% |
| **Executive directors** | | |
| Cai Jianjiang *(President)* | 15/15 | 100% |
| Fan Cheng | 15/15 | 100% |
| **Independent non-executive directors** | | |
| Jia Kang *(resigned on 26 May 2011)* | 8/8 | 100% |
| Fu Yang | 15/15 | 100% |
| Li Shuang | 15/15 | 100% |
| Han Fangming | 15/15 | 100% |
| Yang Yuzhong *(appointed on 26 May 2011)* | 7/7 | 100% |
| **Average attendance rate:** | | **100%** |

For the year ended 31 December 2011, the number of Board meetings held, the convening procedures, minutes and record, rules of procedure and other relevant matters in connection with such meetings were in compliance with the relevant provisions of the Code. It can be shown from the attendance rate that all Directors have discharged their duty of diligence and are dedicated to making contribution for the interest of the Company and its shareholders as a whole.

***Each director is required to keep abreast of his/her responsibilities as a Director and of the operating manner, business activities and developments of the Company***

- The management shall provide members of the Board and specialised committees under the Board with appropriate and sufficient information in a timely manner so as to update them with the latest developments of the Company and facilitate their discharge of duties.

- Newly appointed Directors shall be given introduction in relation to the Company to ensure that they have a sufficient understanding of the management, business and governance practices of the Company.

- The Company also encourages its Directors to participate in seminars and courses conducted by recognised institutions so as to ensure that they continually upgrade their skills and are aware of the latest changes or developments in laws and regulations, the Listing Rules and the Code with which they are required to comply in discharging their duties.

Deviation: Nil

***The Company shall arrange appropriate insurance in respect of potential legal actions against its Directors***

- The Company has purchased liability insurance for the Directors, Supervisors and senior management.

Deviation: Nil

***Compliance with the Model Code for Securities Transactions by Directors of Listed Issuers ("Model Code")***

- After making specific enquiries, the Company confirmed that each Director and each Supervisor has complied with the required standards under the Model Code as set out in Appendix 10 to the Listing Rules throughout 2011.

- The Model Code contained in Appendix 10 to the Listing Rules requires the Board to adopt written guidelines regarding transactions of securities of the issuer by its employees on terms no less exacting than the required standards under the Model Code. On 5 September 2005, the Company adopted and formulated a code of conduct which was revised on 19 March 2007 and 4 December 2009, regarding securities transactions by Directors on terms no less exacting than the required standards of the Model Code. The code of conduct of the Company also applies to Supervisors and the relevant employees.

Deviation: Nil

## B. Remuneration of Directors and Senior Management

***The Company shall establish a remuneration committee with certain authorities and obligations under specific written terms. A majority of the members of the remuneration committee shall be independent non-executive directors***

- The Company has established a nomination and remuneration committee to recommend to the Board on the compensation of the Directors as well as candidates to fill vacancies on the Board. In addition, the nomination and remuneration committee reviews the performance of and determines the compensation structure of the senior management.

- The majority of the members of the nomination and remuneration committee are independent non-executive directors. As at 31 December 2011, the members of the nomination and remuneration committee were Mr. Kong Dong, Ms. Wang Yinxiang, Mr. Fu Yang, Mr. Li Shuang and Mr. Han Fangming with Mr. Fu Yang acting as the Chairman. Due to expiry of the term of office of Mr. Kong Dong (being a non-executive director) on 20 January 2012, Mr. Wang Changshun (being a non-executive director) has filled the vacancy on the nomination and remuneration committee.

- Attendance at the meetings of the nomination and remuneration committee in 2011 was as follows:

| **No. of meetings** | **6** | |
|---|---|---|
| Fu Yang *(Chairman)* | 6/6 | 100% |
| Li Shuang | 6/6 | 100% |
| Han Fangming | 6/6 | 100% |
| Kong Dong *(resigned on 20 January 2012)* | 6/6 | 100% |
| Wang Changshun *(appointed on 20 January 2012)* | N/A | N/A |
| Wang Yinxiang | 6/6 | 100% |
| **Average attendance rate** | | **100%** |

- The Articles of Association provides that a shareholder holding 5% or more of the total shares of the Company is entitled to nominate a Director through the nomination and remuneration committee, which will evaluate the candidates for directorship and senior management according to the standards as set out in the Articles of Association and report to the Board.

- At the second meeting of the nomination and remuneration committee under the third session of the Board held on 21 February 2011, it was resolved that Mr. Xu Chuanyu, Mr. Wang Mingyuan and Mr. Zhao Xiaohang be appointed as Vice President of the Company at the fifth meeting of the third session of the Board.

- At the third meeting of the nomination and remuneration committee under the third session of the Board held on 29 March 2011, it was resolved that the "Report on Stock Appreciation Rights Plan" and the amended "Air China Limited Stock Appreciation Rights Management Rules" be approved; Mr. Yang Yuzhong be nominated as candidate for independent non-executive director; and the remuneration for each independent non-executive director be raised to RMB100,000 per annum. It was proposed that such matters be considered and approved at the eighth meeting of the third session of the Board.

- At the fourth meeting of the nomination and remuneration committee under the third session of the Board held on 8 April 2011, it was resolved that Mr. Liu Tiexiang be appointed as the Chief Aviation Officer and Ms. Zhang Yang be appointed as Assistant to the President at the ninth meeting of the third session of the Board.

- At the fifth meeting of the nomination and remuneration committee under the third session of the Board held on 15 July 2011, it was resolved that the Company implement the enterprise annuity scheme in accordance with the "Enterprise Annuity Plan of CNAHC" and adopt the "implementation Rules of Enterprise Annuity Plan of Air China" set under the "Enterprise Annuity Plan of CNAHC". It was proposed that such matters be considered and approved at the twelfth meeting of the third session of the Board.

- At the sixth meeting of the nomination and remuneration committee under the third session of the Board held on 20 December 2011, it was resolved that Ms. Rao Xinyu be appointed as the Joint Secretary to the Board and the Company at the seventeenth meeting of the third session of the Board.

- At the seventh meeting of the nomination and remuneration committee under the third session of the Board held on 28 December 2011, it was resolved that Mr. Wang Changshun be nominated as the candidate for the Chairman of the Board at the eighteenth meeting of the third session of the Board and to reduce the exercise price of the Company's first issue of the stock appreciate rights by HK$0.27.

- Remuneration payable to Directors shall be determined according to the terms of their respective employment contracts, if any, and the recommendation of the nomination and remuneration committee. Details of the remuneration of the Directors are set out in note 9 to the audited financial statements of this annual report.

Deviation: Nil

## C. Accountability and Audit

***The Board shall present a balanced, clear and comprehensive assessment of the Company's performance, position and prospects***

- The Company has established an audit and risk control committee to review the financial information of the Company and the relevant disclosure, as well as to review the internal control systems of the Company.

- The Company has published its annual and interim results in accordance with the requirements of the Listing Rules and other relevant laws and regulations in a timely manner i.e. within three months and two months, respectively, after the end of the relevant periods.

- The Company has set up an investor relations webpage, on which figures of operating results are published monthly in order to improve the transparency of the Company's performance and to provide the latest developments of the Company in a timely manner.

- The Company has a sound environment for implementing internal controls. The Company has set up an effective electronic information system to support business development which comprises various operation systems, settlement system and a core accounting and audit platform, i.e. the Oracle financial information system. For treasury management, the Company has implemented a global online banking management system. An effective accounting information system was also established.

Deviation: Nil

***The Board shall ensure that the Company maintains a sound and effective internal control system to safeguard the shareholders' investments and the Company's assets***

- The Board takes ultimate responsibility for the internal controls of the Company. Every year, the Company conducts self-assessment on the comprehensiveness of the internal control system and the effectiveness of its implementation. The Board will publicly announce the self-assessment report on the internal control for the year after the audit and risk control committee reports to the Board.

Deviation: Nil

***The Board shall establish formal and transparent arrangements in relation to the application of financial reporting and internal control principles and the maintenance of an appropriate relationship with the Company's auditors***

- Through the audit and risk control committee, the Board reviews and supervises the Company's financial reporting process, communicates with the auditors and reviews periodic financial reports so as to make sure the financial reporting and internal control principles are formal and transparent.

- As at 31 December 2011, the audit and risk control committee comprised two independent non-executive directors, Mr. Li Shuang and Mr. Fu Yang, and a non-executive director, Mr. Cao Jianxiong, with Mr. Li Shuang acting as the chairman.

- Attendance at the meetings of the audit and risk control committee in 2011 was as follows:

| **No. of meetings** | **8** | |
|---|---|---|
| Li Shuang *(Chairman)* | 8/8 | 100% |
| Fu Yang | 8/8 | 100% |
| Cao Jianxiong | 8/8 | 100% |
| **Average attendance rate:** | | **100%** |

- At the second meeting of the third session of the Supervisory Committee held on 13 January 2011, the financial plan, the cash flow and fund raising and financing plans for the year 2011 and capital expenditure plan of the Company for the year 2011 were considered and approved. At the meeting, the Company was approved to engage fuel hedging business in compliance with the requirements set out in the "Fuel Hedging Transaction Operational Plan" (strategy for year 2011), meanwhile, documents such as the "Risk Management Manual for Overseas Financial Derivatives Business Conducted by Air China Limited", "Regulatory Requirements for Fuel Hedging Business of Air China Limited (Provisional)", "Feasibility Report on Conducting Financial Derivatives Business" and "Foreign Exchange Payment Limits Required for Fuel Hedging Business in 2011" were approved, and consent was given to the Company to apply for permission from relevant competent authorities to conduct overseas hedging business.

- At the third meeting of the audit and risk control committee under the third session of the Board held on 24 March 2011, the proposal for the impairment of aircraft and the related assets was considered and approved. The Company was given approval to make an impairment provision of RMB1,345 million for aircraft and related assets proposed to be disposed of. The total provision for the impairment was RMB1,856 million in the consolidated financial statement.

- At the fourth meeting of the audit and risk control committee under the third session of the Board held on 28 March 2011, the audited financial report and annual report for the year 2010 prepared by the Company in accordance with CASs and IASs, respectively, the "Status of Implementation of Connected Transactions of the Company for the Year 2010" and the "Special Explanation on Receivables from Controlling Shareholders and Connected Parties for the Year 2010"; the profit distribution proposal of the Company for the year 2010; the self-assessment report on internal control of the Company for the year 2010 and the standardised working plan for implementing internal control measures of the Company for the year 2011; the "Special Report on Deposit and Utilisation of Capital Raised from Private Placement of A Shares for the Year 2010 by Air China Limited"; the "2010 Summary Report on Audit Work by Ernst & Young and Ernst & Young Hua Ming"; the "Management Rules of Offshore Guarantee of Air China Limited (Provisional)"; and "Work Report of the Audit and Risk Control Committee for the Year 2010" were considered and approved.

- At the fifth meeting of the audit and risk control committee under the third session of the Board held on 28 April 2011, the Company's first quarterly report for the year 2011 was considered and approved.

- At the sixth meeting of the audit and risk control committee under the third session of the Board held on 24 August 2011, the interim report and interim financial report of the Company for the year 2011; the "Special Report on Deposit and Utilisation of Capital Raised from the Placing of A Shares by Air China Limited in the First Half of 2011"; the management plan and operational procedures for fuel hedging business of the Company; a guarantee of not more than RMB1 billion provided by Shenzhen Zunpeng Investment LLC, a wholly-owned subsidiary of Shenzhen Airlines to the Construction Bank of China, Shenzhen Branch with regard to the housing loan in connection with the Shenzhen Residential Park, including a joint maximum amount guarantee under the housing loan guarantee and a pledge of a maximum amount not exceeding RMB30 million; and the proposed interim adjustments to the Company's 2011 financial plan and 2011 investment plan were considered and approved.

- At the seventh meeting of the audit and risk control committee under the third session of the Board held on 10 October 2011, the proposal on providing an entrusted loan to Air China Cargo was considered and approved. With the prior consent of the independent directors, the connected transaction of the RMB1.5 billion entrusted loan provided to Air China Cargo was approved.

- At the eighth meeting of the audit and risk control committee under the third session of the Board held on 26 October 2011, the third quarterly report of the Company for the year 2011 was considered and approved. It was resolved that the Company enter into a framework agreement with Air China Cargo for connected transactions from 2011 to 2013 and submit to the Hong Kong Stock Exchange the exempted annual cap for the total amount of connected transactions for the years from 2011 to 2013; it was further resolved that the Company revise the annual cap for connected transactions with CNAMC under the "Advertising Services Framework Agreement" and enter into the "Supplemental Advertising Services Framework Agreement" with CNAMC.

- At the ninth meeting of the audit and risk control committee under third session of the Board held on 6 December 2011, it was resolved that Ernst & Young Hua Ming be appointed as the internal control auditor of the Company for the year 2011 to review the effectiveness of the Company's internal control and provide the internal control audit report. It was also resolved that the Company's management be authorised to determine the remuneration of Ernst & Young Hua Ming for providing internal control audit services.

- The annual report for the year ended 31 December 2011 of the Company was reviewed by the audit and risk control committee.

Deviation: Nil

***The responsibility of the Directors in relation to the financial statements***

The Company prepares and publishes annual reports, interim reports and quarterly reports each year. The responsibilities of the Directors in relation to the financial statements are set out below and shall be read together with the "Independent Auditors' Report" set out in this annual report.

- *Annual reports and accounts*

  The Directors acknowledge that they are responsible for preparing the financial statements for each financial year so as to present a true and fair view of the financial position of the Company and the Group, and of the financial performance and cash flow of the Group.

- *Accounting policy*

  When preparing the financial statements of the Company and the Group, the Directors have consistently applied appropriate accounting policies under the relevant accounting standards.

- *Accounting records*

  The Directors are responsible for ensuring that the Company shall keep the accounting records, which will reflect the financial position of the Company with reasonable accuracy, enabling the Group to prepare the financial statements in accordance with the requirements of the Listing Rules, Hong Kong "Companies Ordinance" and the relevant accounting standards.

- *Ongoing operation*

  After making appropriate enquiries, the Directors believe that the Group has sufficient resources for operation in the foreseeable future. Accordingly, the Group's financial statements should be prepared on a going concern basis.

The statement of reporting responsibility of the auditors is set out in the "Independent Auditors' Report" set out in this annual report.

***Auditors' remuneration***

The international and domestic auditors of the Company are Ernst & Young and Ernst & Young Hua Ming, respectively. Breakdown of the remuneration to the Company's external auditors for providing audit services and non-audit service assignments for the year ended 31 December 2011 is as follows:

- *Audit services*

  RMB11.5 million was charged for the review of the Group's financial statements for the six months ended 30 June 2011 and for the audit of the Group's financial statements for the year ended 31 December 2011 and an aggregate amount of approximately RMB6,870,169 was charged for the audit of the financial statements of certain subsidiaries of the Group for the year ended 31 December 2011.

- *Non-audit service assignments*

  An aggregate amount of approximately RMB1,129,986 was charged for the provision of internal control, tax and other non-audit services to the Group.

## D. Delegation by the Board

***The Company shall formalise the functions reserved to the Board and those delegated to the management. There shall be division of responsibility between the Board committees, and each committee shall be formed with certain authorities under specific terms***

- The Articles of Association has provided for the authorities and authorisations of the Board and the President, details of which are set out in the "Rules and Procedure for Board Meetings" and "Rules and Procedures for Senior Management Meetings".

- The primary duties of the audit and risk control committee are: to propose the engagement or change of external auditors, conduct appropriate review and evaluation, as well as give opinion in writing to the Board, in connection with the appointment of new accounting firms or reappointment of the existing accounting firms for carrying out annual audits; to review and supervise our internal auditing system and its implementation, review the duties and responsibilities of the internal audit personnel and the appointment or dismissal of the responsible person of the audit department; to be responsible for the communication between the internal auditors and external auditors; to review and verify the Company's financial information and its disclosure; to review the Company's internal control system and risk control system, evaluate the effectiveness of the detailed management and control rules and the operational standards relating to risk investments (including but not limited to financial derivatives instruments), and consider the strategies and proposals of the Company's risk investment; to review the work report prepared by the responsible audit personnel of the Company, any report relating to the fraudulent acts of the Company and the report on the related discovery and complaints; and to fulfill other duties authorised by the Board.

- The primary duties of the nomination and remuneration committee are: to nominate candidates to the Board for director vacancies and recommend the remuneration of Directors to the Board. In addition, the nomination and remuneration committee reviews the performance and determines the remuneration structure of the senior management.

- The primary duties of the strategy and investment committee are: to analyse and identify the Company's development strategy and to decide on investment matters as authorised by the Board. As at 31 December 2011, the members of the strategy and investment committee were Mr. Kong Dong, Mr. Cao Jianxiong, Mr. Sun Yude and Mr. Cai Jianjiang, with Mr. Cai Jianjiang acting as the chairman.

- The Company has established the aviation safety committee with Mr. Cao Jianxiong and Mr. Cai Jianjiang as its members and Mr. Cao Jianxiong acting as the chairman as at 31 December 2011.

- The supervisory committee is responsible for: monitoring the Company's financial matters and supervising the conduct of the Board and our management. The functions and authority of the supervisory committee include: reviewing the financial reports and other financial information prepared by the Board and proposed to be tabled before the shareholders' general meeting; supervising the work of the Directors, President, Vice President and other senior management and preventing the abuse of power or conducts detrimental to the Company's interests. The current members of the supervisory committee are Mr. Li Qinglin, Mr. Zhang Xueren, Mr. Zhou Feng, Ms. Xiao Yanjun and Mr. Su Zhiyong, with Mr. Li Qinglin acting as the chairman. In the event that any Director has a conflict of interests with the Company, a Supervisor may negotiate with the Director concerned or bring the case to court on behalf of the Company. Resolution of meetings of the supervisory committee shall be passed by at least two-thirds of all Supervisors.

Deviation: Nil

## E. Communication with shareholders

***The Board shall endeavour to maintain an on-going dialogue with shareholders and in particular, use general meetings to communicate with shareholders***

- The Company has established and maintained various communication channels with its shareholders through the publication of annual reports, interim reports and quarterly reports, press releases and announcements on the Company's website. The Company has also implemented the "Investors Relation Management System".

- The annual general meetings represent an effective means for the shareholders to exchange their views with the Board. The Chairman of the Board, as well as the respective chairmen of the audit and risk control committee, nomination and remuneration committee, strategy and investment committee and aviation safety committee will answer queries raised by shareholders at general meetings.

- At the annual general meeting, the Board shall report to the shareholders and announce the progress of the implementation by the Board of the matters set out in the resolutions which were passed since the previous annual general meeting and which were for the Board to implement.

- Resolutions in respect of independent matters, including the election and change of the Directors, shall be tabled as separate resolutions before the annual general meeting.

- Other than the annual general meeting, the Company would also hold extraordinary general meeting ("EGM") as required. In accordance with articles 65 and 91 of the Articles of Association, shareholder(s), individually or in the aggregate, holding more than 10% of the shares of the Company may request the Board to convene an EGM by making one or more written request(s) in the same form to the Board with a clear agenda. The Board shall respond to such written request(s) within ten days of receipt of such written request(s). If the Board agrees to convene an EGM, it shall within five days of the board resolution resolving to hold an EGM issue a notice of EGM convening an EGM within two months of receiving such request(s) from the shareholder(s). If the Board does not accept the request(s) from shareholder(s) for a meeting or fails to respond within ten days of the receipt of such written request(s), such shareholder(s) shall request the supervisory committee to convene an EGM by written request(s). If the supervisory committee fails to issue a notice for convening a meeting within five days of the receipt of such written request(s), shareholder(s), individually or in the aggregate, holding more than 10% of the shares of the Company for a consecutive 90 days or more may convene and hold a meeting by themselves.

- For including a resolution relating to other matters in a general meeting, shareholders are requested to follow the requirements and procedures as set out in article 67 of the Articles of Association which provides that shareholder(s), individually or in the aggregate, holding more than 3% of the shares of the Company may put forward proposal(s) by providing a written request to the convener of the meeting not less than ten days before the meeting. The convener of the meeting shall, within two days of the receipt of such written request, give supplemental meeting notice to each shareholder which specifies information on such proposal(s).

Deviation: Nil

- The Board values the views and input of shareholders. Shareholders, may at any time, send their enquiries and concerns to the Board by addressing them to the Company Secretary, whose contact details are as follows:

  Address: Air China Headquarter, 30 Tian Zhu Road,
  Tianzhu Airport Economic Development Zone, Beijing, 101312
  Email: IR@AIRCHINA.COM
  Telephone number: 86-10-61462777
  Fax number: 86-10-61462805

***The Company shall ensure that shareholders are familiar with the detailed procedures for conducting a poll***

- The chairman of a meeting shall, at the commencement of the meeting, ensure that an explanation of the detailed procedures for conducting a poll is provided and subsequently, any questions from shareholders in relation to voting by way of a poll are answered.

Deviation: Nil

# Report of the Directors

## GROUP ACTIVITIES AND RESULTS

The Group is a provider of air passenger, air cargo and airline-related services. The results of the Group for the year ended 31 December 2011 and the financial positions of the Group and the Company as at the same date are set out in the audited financial statements on pages 65 to 165 of this annual report.

## FIVE-YEAR FINANCIAL HIGHLIGHTS

The summary of the Group's results and balance sheet prepared in accordance with IFRSs for the five years ended 31 December 2011 are set out on pages 3 and 4 of this annual report.

## SHARE CAPITAL

As at 31 December 2011, the total share capital of the Company was RMB12,891,954,673, divided into 12,891,954,673 shares with a par value of RMB1.00 each. The following table sets out the share capital structure of the Company as at 31 December 2011:

| Category of Shares | Number of shares | Percentage of the total share capital |
|---|---|---|
| A Shares | 8,329,271,309 | 64.61% |
| H Shares | 4,562,683,364 | 35.39% |
| Total | 12,891,954,673 | 100% |

## SIGNIFICANT INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY

As at 31 December 2011, to the knowledge of the Directors, Supervisors and chief executive of the Company, the interests and short positions of the following persons (other than a Director, Supervisor or chief executive of the Company) who have an interest and short position in the shares, underlying shares and debentures of the Company which would fall to be disclosed to the Company pursuant to the SFO are as follows:

| Name | Type of interests | Type and number of shares of the Company concerned | 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 |
|---|---|---|---|---|---|---|
| CNAHC | Beneficial owner | 5,126,147,507 A shares | 39.76% | 61.54% | – | – |
| CNAHC[(1)] | Attributable interests | 1,332,482,920 A shares | 10.34% | 16.00% | – | – |
| CNAHC[(1)] | Attributable interests | 223,852,000 H shares | 1.74% | – | 4.91% | – |
| CNACG | Beneficial owner | 1,332,482,920 A shares | 10.34% | 16.00% | – | – |
| CNACG | Beneficial owner | 223,852,000 H shares | 1.74% | – | 4.91% | – |
| Cathay Pacific | Beneficial owner | 2,517,385,455 H shares | 19.53% | – | 55.17% | – |
| Swire Pacific Limited[(2)] | Attributable interests | 2,517,385,455 H shares | 19.53% | – | 55.17% | – |
| John Swire & Sons (H.K.) Limited[(2)] | Attributable interests | 2,517,385,455 H shares | 19.53% | – | 55.17% | – |
| John Swire & Sons Limited[(2)] | Attributable interests | 2,517,385,455 H shares | 19.53% | – | 55.17% | – |

*Notes:*

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 Hong Kong Stock Exchange) and so far as the Directors, Supervisors and chief executive are aware, as at 31 December 2011:

1. By virtue of CNAHC's 100% interest in CNACG, CNAHC was deemed to be interested in the 1,332,482,920 A shares and 223,852,000 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 42.79% equity interest and 58.45% voting rights in Swire Pacific Limited, and Swire Pacific Limited's approximately 44.97% interest in Cathay Pacific as at 31 December 2011, John Swire & Sons Limited, John Swire & Sons (H.K.) Limited and Swire Pacific Limited were deemed to be interested in the 2,517,385,455 H shares of the Company directly held by Cathay Pacific.

Save as disclosed above, as at 31 December 2011, to the knowledge of the Directors, Supervisors and chief executive of the Company, no other person (other than a Director, Supervisor or chief executive of the Company) had an interest or short position in the shares, underlying shares and debentures of the Company which would fall to be disclosed to the Company pursuant to the SFO.

## PUBLIC FLOAT

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

## DIVIDEND

Based on the 2011 profit distribution plan of the Company, the Board recommends the appropriation of 10% of the balance of the net profit of the Company of the year 2011 as set out in the financial statements prepared under the PRC Accounting Standards into the discretionary surplus reserve and to distribute a cash dividend of RMB1.521 billion, or RMB0.1180 per share (including tax) based on the total number of 12,891,954,673 shares of the Company, for the year 2011.

The recommended final dividends are subject to shareholders' approval at the forthcoming annual general meeting. Dividends payable to the Company's shareholders shall be denominated and declared in RMB. Dividends payable to the holders of A shares shall be paid in RMB while dividends payable to the holders of H shares shall be paid in Hong Kong dollars. The amount of Hong Kong dollars payable shall be calculated on the basis of the average of the middle rate of RMB to Hong Kong dollars as announced by the People's Bank of China for the calendar week prior to the declaration of the final dividends (if approved) at the annual general meeting.

## TAXATION ON DIVIDEND

In accordance with the "Enterprise Income Tax Law of the People's Republic of China" and the "Rules for the Implementation of the Enterprise Income Tax Law of the People's Republic of China", both implemented on 1 January 2008 and the "Notice of the State Administration of Taxation on Issues Relevant to the Withholding of Enterprise Income Tax on Dividends Paid by PRC Enterprises to Offshore Non-resident Enterprise Holders of H Shares" (Guo Shui Han [2008] No. 897) promulgated on 6 November 2008, the Company is obliged to withhold and pay PRC enterprise income tax on behalf of non-resident enterprise shareholders at a tax rate of 10% from 2008 onwards when the Company distributes any dividends to non-resident enterprise shareholders whose names appear on the register of members of H shares of the Company. As such, any H shares of the Company which are not registered in the name(s) of individual(s) (which, for this purpose, includes shares registered in the name of HKSCC Nominees Limited, other nominees, trustees, or other organisations or groups) shall be deemed to be H shares held by non-resident enterprise shareholder(s), and the PRC enterprise income tax shall be withheld from any dividends payable thereon. Non-resident enterprise shareholders may wish to apply for a tax refund (if any) in accordance with the relevant requirements, such as tax agreements (arrangements), upon receipt of any dividends.

In accordance with the "Circular on Certain Issues Concerning the Policies of Individual Income Tax" (Cai Shui Zi [1994] No.020) promulgated by the Ministry of Finance and the State Administration of Taxation on 13 May 1994, overseas individuals are, as an interim measure, exempted from the PRC individual income tax for dividends or bonuses received from foreign-invested enterprises. As the Company is a foreign-invested enterprise, the Company will not withhold and pay the individual income tax on behalf of individual shareholders when the Company distributes the final dividends for the year 2011 to individual shareholders whose names appear on the register of members of H shares of the Company.

Shareholders are recommended to consult their tax advisors regarding the ownership and disposal of H shares of the Company in the PRC and in Hong Kong and other tax effects.

## PURCHASES, SALES OR REDEMPTION OF SHARES

Save as disclosed otherwise, for the year ended 31 December 2011, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of its listed securities (the term "securities" has the meaning ascribed to it under Paragraph 1 of Appendix 16 to the Listing Rules), without taking into account any issuance of new securities.

## PRE-EMPTIVE RIGHTS

The Articles of Association does not provide for any pre-emptive rights requiring the Company to offer new shares to the existing shareholders in proportion to their existing shareholdings.

## DIRECTORS AND SUPERVISORS OF THE COMPANY

### Directors

| Name | Age | Position in the Company | Date of Appointment and if applicable, Resignation as Director |
|---|---|---|---|
| Wang Changshun | 54 | Chairman and non-executive director | Appointed on 20 January 2012 |
| Kong Dong | 63 | Chairman and non-executive director | Appointed on 28 October 2010<br>Resigned on 20 January 2012 |
| Wang Yinxiang | 56 | Vice chairman and non-executive director | Appointed on 28 October 2010 |
| Cao Jianxiong | 52 | Non-executive director | Appointed on 28 October 2010 |
| Sun Yude | 57 | Non-executive director | Appointed on 28 October 2010 |
| Christopher Dale Pratt | 55 | Non-executive director | Appointed on 28 October 2010 |
| Ian Sai Cheung Shiu | 56 | Non-executive director | Appointed on 28 October 2010 |
| Cai Jianjiang | 48 | Executive director and president | Appointed on 28 October 2010 |
| Fan Cheng | 56 | Executive director, vice president and chief accountant | Appointed on 28 October 2010 |
| Jia Kang | 57 | Independent non-executive director | Appointed on 28 October 2010<br>Resigned on 26 May 2011 |
| Fu Yang | 62 | Independent non-executive director | Appointed on 28 October 2010 |
| Li Shuang | 67 | Independent non-executive director | Appointed on 28 October 2010 |
| Han Fangming | 45 | Independent non-executive director | Appointed on 28 October 2010 |
| Yang Yuzhong | 67 | Independent non-executive director | Appointed on 26 May 2011 |

### Supervisors

| Name | Age | Position in the Company | Date of Appointment and if applicable, Resignation as Director |
|---|---|---|---|
| Li Qinglin | 56 | Chairman of the Supervisory Committee | Appointed on 28 October 2010 |
| Zhang Xueren | 58 | Supervisor | Appointed on 28 October 2010 |
| He Chaofan | 49 | Supervisor | Appointed on 28 October 2010<br>Resigned on 25 November 2011 |
| Zhou Feng | 50 | Supervisor | Appointed on 25 November 2011 |
| Chen Bangmao | 61 | Supervisor | Appointed on 18 August 2009<br>Ceased to be a Supervisor on 16 June 2011 |
| Xiao Yanjun | 47 | Supervisor | Appointed on 16 June 2011 |
| Su Zhiyong | 48 | Supervisor | Appointed on 16 June 2011 |

## INDEPENDENCE OF THE INDEPENDENT NON-EXECUTIVE DIRECTORS

The Company has confirmed its receipt of, from each of the independent non-executive directors of the Company, a confirmation of his/her independence pursuant to Rule 3.13 of the Listing Rules. The Company considers all of the independent non-executive directors to be independent.

## BOARD COMMITTEES

The Board committees include the audit and risk control committee, nomination and remuneration committee, strategy and investment committee and aviation safety committee. The composition of each committee is set out in the "Corporate Governance Report" of this annual report.

## DIRECTORS' AND SUPERVISORS' RIGHTS TO ACQUIRE SHARES OF THE COMPANY

At no time during the year ended 31 December 2011 had the Company granted its Directors, Supervisors or their respective spouses or children under the age of 18 any rights to subscribe for the shares or debentures of the Company or any of its other associated corporations, and no such rights for the subscription of shares or debentures were exercised by them.

## DIRECTORS' AND SUPERVISORS' INTERESTS AND SHORT POSITIONS IN THE SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY

As at 31 December 2011, the Company's Directors, Supervisors or chief executive had following interests or short positions in the shares, underlying shares and/or debentures (as the case may be) of the Company or its associated corporations (within the meaning of Part XV of the SFO) which shall be recorded in the register maintained by the Company pursuant to section 352 of the SFO, or which shall be notified to the Company and the Hong Kong Stock Exchange pursuant to the Model Code:

### Interests in Shares of Associated Corporations

| | Number of Shares | | | | Shareholding percentage as at |
|---|---|---|---|---|---|
| **Name of associated corporation and relevant shareholder** | **Personal interest** | **Interest of children under the age of 18 or spouse** | **Corporate interest** | **Total** | **31 December 2011** |
| Cathay Pacific Airways Limited | | | | | |
| Ian Sai Cheung Shiu | 1,000 | – | – | 1,000 | 0.00% |
| Air China Limited | | | | | |
| Zhou Feng | 10,000 (A Shares) | – | – | 10,000 (A Shares) | 0.00% |

Save as disclosed above, as at 31 December 2011, 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 its associated corporations (within the meaning of Part XV of the SFO) which were recorded in the register maintained by the Company pursuant to section 352 of the SFO, or which were notified to the Company and the Hong Kong Stock Exchange pursuant to the Model Code.

## REMUNERATION OF DIRECTORS AND SUPERVISORS

Details of the remuneration of the Directors and Supervisors are set out in note 9 to the audited financial statements of this annual report.

## INTERESTS OF DIRECTORS AND SUPERVISORS IN CONTRACTS AND SERVICE CONTRACTS

Each of the Directors has entered into a service contract with the Company. All Directors of the Company shall serve a term of three years.

None of the Directors or Supervisors has proposed to enter into any service contract with any member of the Group which is not expiring or terminable by the Group within one year without payment of compensation (other than statutory compensation).

None of the Directors or Supervisors of the Company was materially interested in any contract or arrangement subsisting as at 31 December 2011 and which is significant in relation to the business of the Group.

Mr. Christopher Dale Pratt is a non-executive director of the Company and is concurrently the chairman and executive director of Cathay Pacific. Mr. lan Sai Cheung Shiu is a non-executive director of the Company and concurrently the director of Cathay Pacific and Dragonair. Cathay Pacific is a substantial shareholder of the Company, holding 2,517,385,455 H shares in the Company as at 31 December 2011, which would fall to be disclosed to the Company under the provisions of divisions 2 and 3 of Part XV of the SFO, and it wholly owns Dragonair. Mr. Kong Dong, who was the chairman and a non-executive director of the Company and resigned on 20 January 2012, Mr. Cai Jianjiang and Mr. Fan Cheng, who are both executive directors of the Company, are concurrently non-executive directors of Cathay Pacific (Mr. Kong Dong resigned as a non-executive director of Cathay Pacific on 14 March 2012). 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 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.

## CONVENTION OF BOARD MEETINGS AND COMPLIANCE WITH THE CODE ON CORPORATE GOVERNANCE PRACTICES

The Company held 15 Board meetings during the year 2011. The Company has been continuously improving its corporate governance structure since its listing. The Board is committed to conducting normative operations to protect the interests of the Company and its shareholders. The Directors of the Company are of the opinion that as at 31 December 2011 the Company has refined its internal corporate governance structure in compliance with the requirements set out in the Code on Corporate Governance Practices in Appendix 14 to the Listing Rules then in effect.

## EMPLOYEES

As at 31 December 2011, the Company had 24,474 employees and its subsidiaries and joint ventures had 30,438 employees. The categories of employees of the Company are as follows:

| Professional Categories | As at 31 December 2011 | As at 31 December 2010 | Increase/ (decrease) |
|---|---|---|---|
| Management | 6,065 | 5,811 | 254 |
| Marketing and Sales | 1,881 | 2,055 | (174) |
| Operation | 1,393 | 1,376 | 17 |
| Ground Handling | 4,114 | 4,283 | (169) |
| Cabin Service | 1,816 | 1,959 | (143) |
| Logistics and Support | 1,446 | 1,429 | 17 |
| Flight Crew | 3,363 | 3,119 | 244 |
| Engineering and Maintenance | 2,754 | 2,712 | 42 |
| Information Technology | 311 | 290 | 21 |
| Others | 1,331 | 1,425 | (94) |
| Total | 24,474 | 24,459 | 15 |

## COMPENSATION POLICY

In order to implement the Company's strategies and to incentivise its employees, the Board approved, upon consideration, the proposal relating to the welfare reform on the remuneration of the ground crew, flight attendants, safety officers and air police officers and the proposal to revise the welfare system applicable to the flight crew. Accordingly, the welfare reform on the remuneration of the ground crew, flight attendants, safety officers and air police officers was implemented from 1 July 2007 and the welfare system applicable to the flight crew (as revised) came into force on 1 March 2008.

To proceed with the implementation of the Company's strategies and to reward and retain its employees, based on the welfare reform on the remuneration completed in 2008, the Company adjusted the welfare system applicable to its flight crew, flight (security) attendants and ground crew in 2010.

In order to eliminate the conflicts and problems in the management of remuneration and welfare, and stabilise its employees while optimising and refining the relevant systems, the Company released additional compensation to all of its employees from July 2011.

## EMPLOYEES AND EMPLOYEES' PENSION SCHEME

313 employees of the Company retired in 2011. These retired employees are entitled to benefits under the social pension scheme approved and provided by the labour and social security authority of the local governments. Details of the staff pension scheme and other welfare are set out in note 10 to the audited financial statements.

## STOCK APPRECIATION RIGHTS

The Directors and Senior Management Stock Appreciation Rights Handbook of the Company was considered and approved at the general meeting held on 28 December 2006. The first issue of the stock appreciation rights was implemented by the Company on 15 June 2007 under which a total of approximately 14.94 million stock appreciation rights were granted. Details of the stock appreciation rights programme are set out in note 45 to the audited financial statements of this annual report.

On 25 August 2009, it was resolved at the twenty-ninth meeting of the second session at the Board to suspend the above scheme and require the Company to amend the original scheme in accordance with the relevant regulations, which, after the consideration of and approval by the Board, would be submitted to a general meeting for approval and then be implemented.

In November 2010, the Company submitted a proposal through CNAHC to the State Owned Assets Supervision and Administration Commission of the State Council, regarding proposed amendments to the first issue of the stock appreciation rights programme and relevant administration measures in accordance with the relevant regulations, and intended to resume the first issue of the stock appreciation rights programme of the Company. The resolution in relation to the resumption of the first issue of the stock appreciation rights programme of the Company would be resolved at the annual general meeting.

On 26 May 2011, the revised "Management Measures for Stock Appreciation Rights of Air China Limited" proposed by the Company and the resumption of the first issue of the stock appreciation rights programme in accordance with the revised management measures were approved by shareholders at the 2010 annual general meeting of the Company.

The Board determined that 70% of the first issue of the stock appreciation rights already vested should be exercisable at a settlement price of HK$7.85 during the specified period from 19 to 22 July and 25 July 2011. As at 31 December 2011, the abovementioned 70% of the stock appreciation rights had been exercised and the carrying amount of the liabilities relating to the stock appreciation rights was RMB1,235,353 (the amount in 2010 was RMB19,284,138).

## SUBSIDIARIES AND ASSOCIATED COMPANIES

Details of the subsidiaries and associates of the Company as at 31 December 2011 are set out respectively in notes 20 and 22 to the audited financial statements of this annual report.

## BANK LOANS AND OTHER BORROWINGS

Details of the bank loans and other borrowings of the Company and the Group are set out in note 38 to the audited financial statements of this annual report.

## FIXED ASSETS

Changes in the fixed assets of the Group for the year ended 31 December 2011 are set out in note 15 to the audited financial statements of this annual report.

## CAPITALISED INTERESTS

Details of the capitalised interests of the Group for the year ended 31 December 2011 are set out in note 8 to the audited financial statements of this annual report.

## RESERVES

Changes in the reserves of the Company and the Group during the year are set out in note 44 to the audited financial statements of this annual report.

## DONATIONS

For the year ended 31 December 2011, the Company made donations for charitable and other purposes amounting to RMB2.84 million.

## MAJOR CUSTOMERS AND SUPPLIERS

For the year ended 31 December 2011, the purchases from the largest supplier accounted for 26.83% of the total purchases of the Group, while the purchases from the five largest suppliers accounted for 60.94%. None of the Directors or Supervisors of the Company, their associates, nor any shareholder, who to the knowledge of the Directors owns 5% or more of the Company's share capital, had any interest in the five largest suppliers of the Company.

For the year ended 31 December 2011, the sales of the Group to the five largest customers accounted for not more than 30% of the total sales of the Group.

## PROPERTY TITLE CERTIFICATE

The Company effected changes to the titles of assets e.g. land use rights, buildings and vehicles, in accordance with its undertakings as disclosed in the Company's prospectus issued at the time of its offering of shares. The title transfer procedures for the motor vehicles of the Company's headquarters and branches have been completed. Except for certain regions, the title transfer procedures for the land use rights and buildings of the Company's headquarters and branches have been substantially completed. The Company is in the process of completing the outstanding formalities in this respect, which should not have any material adverse effect on the operation of the Company.

## MATERIAL LEGAL PROCEEDINGS

Save as disclosed in note 48 to the audited financial statements of this annual report, the Company was not involved in any significant litigation or arbitration as at 31 December 2011. To the knowledge of the Company, there was no litigation or claim of material importance pending or threatened or initiated against the Company.

## CONNECTED TRANSACTIONS

The Group has entered into a number of connected transaction agreements with CNAHC and its associates (as defined under the Listing Rules) (for the purpose of this section "Report of the Directors", hereinafter referred to as "CNAHC Group") and other connected persons of the Group as described in the paragraphs below. The Company has complied with the disclosure requirements of the connected transactions in accordance with Chapter 14A of the Listing Rules in force from time to time.

### I. Continuing Connected Transactions Between the Group and CNAHC Group

As CNAHC is a substantial shareholder of the Company and therefore a connected person of the Company, the transactions between CNAHC and the Company described in paragraphs (a) to (d) below constitute continuing connection transactions for the Company under Rule 14A.14 of the Listing Rules and are subject to the requirements under Rules 14A.35, 14A.36 and 14A.37 of the Listing Rules.

#### *(a) Property Leasing*

The Company entered into a properties leasing agreement with CNAHC on 27 October 2009 (the "Properties Leasing Agreement").

Pursuant to the Properties Leasing Agreement, the Company will lease from CNAHC Group a number of properties for various uses including business premises, offices and storage facilities.

The Company will lease to CNAHC Group a number of properties for various uses including business premises and offices.

The rent payable under the Properties Leasing Agreement will be determined in accordance with the relevant PRC regulations or market rates and by entering into a specific properties leasing agreement. The annual increase in rental rate is expected not to exceed 5%.

The term of the Properties Leasing Agreement is from 1 January 2010 to 31 December 2012. For further details of the Properties Leasing Agreement, please refer to the Company's circular dated 6 November 2009.

***(b) Sales Agency Services of Airline Tickets and Cargo Space***

The Company entered into a Sales Agency Services Framework Agreement (the "Sales Agency Services Framework Agreement") with CNAHC on 27 October 2009.

Pursuant to the Sales Agency Services Framework Agreement, certain subsidiaries of CNAHC acting as the Company's sales agents ("Sales Agency Companies") will:

- procure purchasers for the Company's air tickets and cargo spaces on a commission basis; or
- purchase air tickets (other than domestic air tickets) and cargo spaces from the Company and resell such air tickets and cargo spaces to end customers.

Regarding the air passenger agency services, the Company will continue to comply with the existing fee standards for air passenger sales agency services before the relevant competent authority promulgates administrative regulations on the fee range allowed for air passenger sales agency services. After the promulgation of such administrative regulations, the Company will consult with the Sales Agency Companies on a fair and voluntary basis and determine the agency service fee standards within the stipulated floating range. In addition, the Company and the Sales Agency Companies may agree on specific sales targets and the corresponding incentive plans for achieving such targets to the extent permitted by law and in accordance with the industry practice.

Regarding the air cargo agency services, the Company and the Sales Agency Companies will discuss and determine the applicable transportation prices based on the prevailing market prices, and the Sales Agency Companies may formulate the transportation prices charged to its customers (including the prices for extended services offered to its customers) based on the aforesaid transportation prices, with the differences to be retained as commissions. In addition, the Company and the Sales Agency Companies may agree on specific sales targets and the corresponding price discounts for achieving such sales targets in accordance with the industry practice.

The term of the Sales Agency Services Framework Agreement is from 1 January 2010 to 31 December 2012. For further details of the Sales Agency Services Framework Agreement, please refer to the Company's circular dated 6 November 2009.

***(c) Comprehensive Services***

The Company entered into a comprehensive services agreement with CNAHC on 27 October 2009 (the "Comprehensive Services Agreement").

Pursuant to the Comprehensive Services Agreement:

- Certain wholly-owned and controlled companies of CNAHC engaged in ancillary production and supply services in relation to air transportation business ("Ancillary Business Companies"), provided that such Ancillary Business Companies have obtained the relevant qualifications and certification, will primarily provide the following services to the Company as suppliers to the Company in respect of the Company's ancillary production and supply services:

  (i) supply of various items for in-flight services;

  (ii) manufacturing and repair of aviation-related ground equipment and vehicles;

  (iii) cabin decoration and equipment;

  (iv) properties management services;

  (v) warehousing services;

  (vi) airline catering services; and

  (vii) printing of air tickets and other publications.

- The Company accepts the commission of CNAHC and provides welfare-logistics services for CNAHC's retired employees.

The charges of the services provided by the Ancillary Business Companies to the Company shall not exceed the prevailing market rates (including the tender quotes) and the prices of the similar services they provide to independent third parties. If no prevailing market rate is available, a fair and reasonable price should be adopted through arm's length negotiation between the parties. The management charges payable by CNAHC to the Company for the welfare-logistics services shall be settled at a rate of 4% of the actual aggregate welfare expense paid to such retired employees as confirmed by CNAHC.

The term of the Comprehensive Services Agreement is from 1 January 2010 to 31 December 2012. For further details of the Comprehensive Services Agreement, please refer to the Company's circular dated 6 November 2009.

***(d) Subcontracting of Charter Flight Services***

The Company entered into a government charter flight service framework agreement with CNAHC on 27 October 2009 (the "Charter Flight Service Framework Agreement").

Pursuant to the Charter Flight Service Framework Agreement, CNAHC shall resort to the Company's charter flight services so as to fulfill the government charter flight assignment. The Company's hourly rate of the charter flight service fee will be calculated on the basis of the following formula:

Hourly rate = Total cost per flight hour x (1 + 6.5%)

Total cost per flight hour includes direct costs and indirect costs.

The term of the Charter Flight Service Framework Agreement is from 1 January 2010 to 31 December 2012. For further details of the Charter Flight Service Framework Agreement, please refer to the Company's circular dated 6 November 2009.

**Media and Advertising Services**

The Company entered into an advertising services framework agreement with CNAMC on 27 October 2009 (the "Advertising Services Framework Agreement").

As CNAMC is a wholly-owned subsidiary of CNAHC and therefore a connected person of the Company, the transactions between CNAMC and the Company constitute continuing connected transactions for the Company under Rule 14A.14 of the Listing Rules and are subject to the requirements under Rules 14A.35, 14A.36 and 14A.37 of the Listing Rules.

Pursuant to the Advertising Services Framework Agreement, CNAMC will have the following rights:

- an exclusive right to distribute the in-flight reading materials of the Company;
- an exclusive operation right of the specific media of the Company, including the flight boarding passes, aircraft seat pillow sheets, paper cups, in-flight entertainment system and flight schedules;
- a right to be commissioned to purchase in-flight entertainment programmes (which may include advertising content) from independent third parties or produce such programmes on its own;

- a right to develop and use the media of the Company and receive effective support and assistance from the Company in the course of the sale of advertisements. The advertising business cooperation which may be conducted from time to time between the Company and CNAMC includes (1) advertisements produced by CNAMC or for which CNAMC acts as agent and media developed by CNAMC for the Company (including outdoor advertisements on properties owned by the Company, ground broadcasting programmes (at ticket offices and on airport shuttles), the international e-commerce network check-in system and ticket envelops (including air ticket envelops and boarding pass envelops)) and (2) advertisements designed, produced and published by CNAMC, as commissioned by the Company directly or through public tender; and

- a right to receive advertising fees at market price in respect of advertising design and image promotion conducted by CNAMC for the Company under the Company's commissioning.

As a consideration, CNAMC agrees to:

- pay the Company RMB23.81 million, RMB25.00 million and RMB26.25 million, respectively, for each of the three years ending 31 December 2010, 2011 and 2012 in respect of the exclusive operation rights of the specific media of the Company, and according to the annual budget of the Company, provide the Company at nil charge with sufficient in-flight media (other than in-flight entertainment programmes), including in-flight publications, boarding passes, pillow sheets, flight schedules, and paper cups that meet the Company's requirements; and

- pay the Company 20% of any revenue from any new advertising media of the Company which is not mentioned in the Advertising Services Framework Agreement but proposed to be developed by CNMAC on a case-to-base basis.

The Company agrees to pay immediately and directly to the independent entertainment programmes providers the purchasing price for those in-flight entertainment programmes provided or purchased by CNAMC for the Company. In the event that the relevant entertainment programmes are produced by CNAMC at the request of the Company, the Company will pay the corresponding production costs and expenses to CNAMC.

On 27 October 2011, the Company entered into a supplemental advertising services framework agreement with the CNAMC revising the caps of the continuing connected transactions between the Company and CNAMC (the "Supplemental Agreement").

The term of the Advertising Services Framework Agreement is from 1 January 2010 to 31 December 2012. For further details of the Advertising Services Framework Agreement and the Supplemental Agreement, please refer to the Company's circular dated 6 November 2009 and announcement dated 27 October 2011.

**Tourism Co-operation Services**

The Company entered into a tourism services cooperation agreement with China National Aviation Tourism Company ("CNATC") on 27 October 2009 (the "Tourism Cooperation Agreement").

As CNATC is a wholly-owned subsidiary of CNAHC and therefore a connected person of the Company, the transactions between CNATC and the Company constitute continuing connected transactions for the Company under Rule 14A.14 of the Listing Rules and are subject to the requirements under Rules 14A.35, 14A.36 and 14A.37 of the Listing Rules.

Pursuant to the Tourism Cooperation Agreement, the Company has agreed to provide the following services to CNATC:

- Package tours services: The Company and CNATC will design, and the Company will sell, the competitive "Air Tickets and Hotel" product combining discounted airline tickets for certain routes offered by the Company and accommodation at hotels owned and operated by CNATC at preferential group rates. Out of the proceeds from package tours, the Company will pay CNATC for the hotel fee portion of the packages.

- Reciprocal frequent-flyer programme ("FFP") co-operation services: CNATC will join the Company's FFP under which our companion card members are encouraged to stay at CNATC's hotels by receiving mileage credits for such stay. As a consideration, CNATC will pay us the equivalent value represented by those mileage credits at market rates.

- Commercial charter flight services: The Company will provide commercial charter services to customers procured by CNATC at market rates.

Pursuant to the Tourism Cooperation Agreement, CNATC has agreed to provide the following services to the Company:

- FFP co-operation services: Under the FFP, our frequent flyers may redeem their mileage credits for discounted stay at CNATC's hotels, and the Company will make payment settlement with CNATC for the discount portion of such redemption according to similar pricing arrangements with our other FFP partners.

- Hotel accommodation services: CNATC will provide temporary hotel accommodation services to the Company's employees on duty and passengers affected by our flight delays, for which services the Company will pay hotel accommodation fees to CNATC as scheduled and at the actual amount incurred.

- Aviation tourist services with special features including but not limited to a newly launched service of ground transportation for passengers of two classes at market rates.

The term of the Tourism Cooperation Agreement is from 1 January 2010 to 31 December 2012. For further details of the Tourism Cooperation Agreement, please refer to the Company's circular dated 6 November 2009.

**Financial Services**

The Company entered into a financial services agreement with China National Aviation Finance Co., Ltd. ("CNAF") on 27 October 2009 (the "Financial Services Agreement").

As CNAF is a 75.54% held subsidiary of CNAHC and therefore a connected person of the Company, the transactions between CNAF and the Company constitute continuing connected transactions for the Company under Rule 14A.14 of the Listing Rules and are subject to the requirements under Rules 14A.35, 14A.36 and 14A.37 of the Listing Rules.

Pursuant to the Financial Services Agreement, CNAF has agreed to provide the Company with a range of financial services including the following:

- deposit services;

- loan and finance leasing services;

- negotiable instrument and letter of credit services;

- trust loan and trust investment services;
- underwriting services for debt issuances;
- intermediary and consulting services;
- guarantee services;
- settlement services;
- internet banking services;
- bills and payment collection services;
- insurance agency services; and
- other services provided by CNAF under the approval of the China Banking Regulatory Commission ("CBRC").

In particular, CNAF is currently paid to provide the Company with bills acceptance services, letter of credit services, guarantee services, internet banking services, finance leasing services, discounting services and ticket collection services and charges fees incurred thereon. Such fees are charged in accordance with the relevant fees standard (if any) stipulated by the People's Bank of China ("PBOC") or the CBRC. In addition to complying with the foregoing, the fees charged by CNAF to the Company for financial services of similar type shall not be higher than those generally charged by commercial banks from the Company and those charged by CNAF to other group members.

With respect to the deposit and loan services, both parties agree:

- the interest rate applicable to the Company for its deposits with CNAF shall not be lower than the minimum interest rate specified by the PBOC for deposits of similar type. In addition, the interest rate for the Company's deposits with CNAF shall not be lower than the interest rate for similar type of deposits placed by other members of CNAHC Group with CNAF, and shall not be lower than the interest rate for similar type of deposit services provided by commercial banks to the Company generally; and

- the interest rate for loans (including other credit business) granted to the Company by CNAF shall not be higher than the maximum interest rate specified by the PBOC for loans of similar type. In addition, the interest rate for loans granted to the Company by CNAF shall not be higher than the interest rate for similar type of loans granted by CNAF to other members of CNAHC Group or higher than those for similar type of loans granted by commercial banks to the Company generally. The Company agrees that it will under the same conditions accord priority to and use the financial services provided by CNAF. CNAF has treated the Company as its major client and undertook to provide financial services of the same kind under conditions no less favourable than those provided by CNAF to other members of CNAHC Group and those provided by other financial institutions to the Company at the same time.

In order to ensure the security of the Company's capital, CNAF is not allowed, at any time, to make use of the deposits of the Company other than making external loans. The prohibited use of the deposits of the Company includes, but not limited to, investment activities in equity securities and corporate bonds. CNAF, as a non-banking financial institution approved by the CBRC, shall strictly comply with the regulatory targets and other requirements of the CBRC to conduct its operation and business, establish effective and complete internal control and risk management systems and set up the credit review committee and investment committee in order to effectively manage risks and ensure the safety of all capital. If the Company intends to inspect the accounts of CNAF, CNAF shall make arrangement for such an inspection within 10 days thereof. Pursuant to provisions of the Measures on Administrating the Financial Companies of Enterprise Groups, in the emergent event that CNAF encounters financial difficulties in making payments, CNAHC, as the controlling shareholder of the Company, shall increase the capital of CNAF accordingly to meet the actual need to overcome such financial difficulties in making payments.

The unpaid services provided by CNAF to the Company include settlement services and financial information services ("Unpaid Services").

In addition to the specific services set out in the Financial Services Agreement, CNAF is also exploring and developing other licensed financial services and will provide new financial services to other members of CNAHC Group as and when appropriate ("New Financial Services").

If CNAF charges fees for the Unpaid Services and New Financial Services during the period in which the Financial Services Agreement remains in force, such fees charged by CNAF shall comply with the standards stipulated by the PBOC or the CBRC for services of similar type and shall not be higher than those charged by commercial banks to the Company for similar type of financial services and those charged by CNAF to other members of CNAHC Group.

The term of Financial Services Agreement is from 1 January 2010 to 31 December 2012. For further details of the Financial Services Agreement, please refer to the Company's circular dated 6 November 2009.

## II. Continuing Connected Transactions between the Group and CNACG

The Company entered into a framework agreement with CNACG on 26 August 2008 which was renewed on 10 September 2010 (the "CNACG Framework Agreement).

As CNACG is a substantial shareholder of the Company and therefore a connected person of the Company, the transactions between CNACG and the Company constitute continuing connected transactions for the Company under Rule 14A.14 of the Listing Rules and are subject to the requirements under Rules 14A.35, 14A.36 and 14A.37 of the Listing Rules.

The CNACG Framework Agreement provides a framework for relevant agreements between the Group and CNACG Group covering transactions relating to ground handling and engineering services, management services and other services and transactions as may be agreed by parties to be undertaken under the CNACG Framework Agreement excluding those transactions which have been contemplated by the Properties Leasing Agreement, Sales Agency Services Framework Agreement, Comprehensive Services Agreement, Charter Flight Service Framework Agreement, Tourism Cooperation Agreement and the Financial Services Agreement.

The term of the CNACG Framework Agreement is from 1 January 2011 to 31 December 2013, which is renewable for successive periods of three years unless either party gives to the other party a notice of termination of not less than three months expiring on any 31 December. For further details of the CNACG Framework Agreement, please refer to the Company's announcements dated 26 August 2008 and 10 September 2010.

### III. Continuing Connected Transactions between the Group and Cathay Pacific

The Company entered into a framework agreement with Cathay Pacific on 26 June 2008 which was renewed on 1 October 2010 (the "Cathay Pacific Framework Agreement").

As Cathay Pacific is a substantial shareholder and therefore a connected person of the Company, the transactions between the Company and Cathay Pacific Group (Cathay Pacific and its subsidiaries, including Dragonair) constitute continuing connected transactions for the Company under Rule 14A.14 of the Listing Rules and are subject to the requirements under Rules 14A.35, 14A.36 and 14A.37 of the Listing Rules.

The Cathay Pacific Framework Agreement provides the framework under which relevant agreements (the "Cathay Pacific Relevant Agreements") between members of the Group on the one hand and members of Cathay Pacific Group on the other hand are entered into, renewed and extended. The transactions under the Cathay Pacific Relevant Agreements are transactions between members of the Group on the one hand and members of Cathay Pacific Group on the other hand arising from joint venture arrangements for the operation of passenger air transportation, code sharing arrangements, interline arrangements, aircraft leasing, frequent flyer programmes, the provision of airline catering, ground support and engineering services and other services agreed to be provided and other transactions agreed to be undertaken under the Cathay Pacific Framework Agreement.

The term of the Cathay Pacific Framework Agreement is from 1 January 2011 to 31 December 2013, which is renewable for successive periods of three years unless either party gives to the other party a notice of termination of not less than three months to terminate the Cathay Pacific Framework Agreement on any 31 December. For further details of the Cathay Pacific Framework Agreement, please refer to the Company's announcements dated 26 June 2008 and 10 September 2010.

### IV. Continuing Connected Transactions between the Group and the Lufthansa Group

The Company has entered into various transactions with Lufthansa and its associates (collectively, the "Lufthansa Group") in the ordinary course of its business pursuant to several agreements signed in different periods (some were over three years) respectively, including, among others:

- aircraft maintenance, repair and overhaul services provided by the Company to the Lufthansa Group;
- mutual provision of catering services;
- mutual provision of ground handling services in China and Germany;
- mutual provision of ticket sales agency services;
- airline code sharing arrangement under which the actual carrier's flights can be marketed under the airline designator code of the partner carrier and revenues earned from these arrangements are allocated between the parties based on negotiated terms according to airline industry standards;
- special prorate arrangement under which a carrier agrees to accept passengers from another carrier and receive payment directly from that carrier; and
- other airline co-operation arrangements between the Lufthansa Group and the Company.

Lufthansa holds 40% equity interest in, and is a substantial shareholder of, Aircraft Maintenance and Engineering Corporation (Beijing), a joint venture of the Company, and is therefore a connected person of the Company under the Listing Rules. As such, the transactions between Lufthansha Group and the Company constitute continuing connected transactions for the Company under Rule 14A.14 of the Listing Rules and are subject to the requirements under Rules 14A.35, 14A.36 and 14A.37 of the Listing Rules.

For further details of the transactions between the Company and Lufthansa Group, please refer to the Company's circular dated 6 November 2009 and the Company's announcement dated 10 September 2010.

## V. Connected Transactions between the Group and Air China Cargo

***Continuing Connected Transactions***

The Company has entered into a framework agreement with Air China Cargo on 27 October 2011 (the "Cargo Framework Agreement").

Air China Cargo is a connected person of the Company by virtue of being a non-wholly owned subsidiary of the Company in which Cathay Pacific, a substantial shareholder of the Company, holds more than 10% of the voting rights through Cathay Pacific China Cargo Holdings Limited, a wholly-owned subsidiary of Cathay Pacific. As such, transactions between Air China Cargo and the Company constitute continuing connected transactions for the Company under Rule 14A.14 of the Listing Rules and are subject to the requirements under Rules 14A.35, 14A.36 and 14A.37 of the Listing Rules.

Pursuant to the Cargo Framework Agreement, the Group has agreed to provide the following services to Air China Cargo:

- the provision of bellyhold space of the passenger aircraft operated by the Company;
- ground support and aircraft maintenance engineering including, among others, the repair and maintenance of aircraft and engines; and
- other services to Air China Cargo including, among others, labour management and import and export agency services.

Pursuant to the Cargo Framework Agreement, Air China Cargo has agreed to provide the following services to the Group:

- ground support including, among others, cargo and mail ground loading and unloading and security inspection services; and
- other services provided to the Group.

The consideration of specific continuing connected transactions under the Cargo Framework Agreement shall be agreed between the Company and Air China Cargo on a case-by-case basis.

The term of the Cargo Framework Agreement is three years, ending on 31 December 2013, which is renewable unless being terminated by either party to the Cargo Framework Agreement. For further details of the Cargo Framework Agreement, please refer to the Company's circulars dated 8 April 2010 and 10 November 2011 as well as the announcements dated 29 March 2011 and 27 October 2011.

***Provision of the Entrusted Loan***

The Company entered into an entrustment agreement (the "Entrustment Agreement") with CNAF and an entrustment loan agreement (the "Entrustment Loan Agreement") with CNAF and Air China Cargo on 12 October 2011 in relation to the provision of the loan of a principal amount of up to RMB1.5 billion entrusted by the Company to Air China Cargo with CNAF acting as the lending agent (the "Entrusted Loan").

Pursuant to the Entrusted Loan Agreement, CNAF is designated by the Company to act as a lending agent to release the Entrusted Loan and to monitor the use and repayment of the Entrusted Loan by Air China Cargo. The proceeds of the Entrusted Loan is to be used to supplement the working capital of Air China Cargo. The Entrusted Loan is to be drawn down in tranches and the principal amount of each tranche shall be repayable in full within 6 months. The interest rate for each tranche of the Entrusted Loan shall be 10% less than the benchmark lending interest rate announced by the People's Bank of China on the date of the actual drawdown of such tranche and shall remain unchanged during the term of such tranche for a period of six months. The Company will pay CNAF a fee at an annualized rate of 0.075% of the principal amount of each tranche, which shall be payable upon the drawdown of each tranche.

As Air China Cargo is a connected person of the Company as described in the paragraphs above, the provision of the Entrusted Loan by the Company to Air China Cargo under the Entrusted Loan Agreement constituted a connected transaction of the Company under Chapter 14A of the Listing Rules. As each of the applicable percentage ratios (as defined in Rule 14.07 of the Listing Rules) for the principal amount of the Entrusted Loan, on an aggregated basis, is more than 0.1% but less than 5%, the Entrusted Loan Agreement is only subject to reporting and announcement requirements but is exempted from independent shareholders' approval requirements.

In addition, since CNAF is a connected person of the Company as described in the sub-section headed "Financial services" on page 45 of this annual report, the provision of the service by CNAF as a lending agent pursuant to the Entrustment Agreement in relation to the Entrusted Loan constituted a connected transaction of the Company under Chapter 14A of the Listing Rules which falls within the financial services under the Financial Services Agreement, details of which are set out on pages 45 to 47 of this annual report.

For further details of the Entrusted Loan, please refer to the Company's announcement dated 12 October 2011.

## VI. Transaction Caps and Actual Transaction Amounts in 2011

Actual transaction amounts and transaction caps of the above-mentioned continuing connected transactions during the year ended 31 December 2011 are as follows:

| | | Aggregate amount of transactions for the year ended 31 December 2011 | |
|---|---|---|---|
| | **Currency** | **Cap** *(in millions)* | **Actual Amount** *(in millions)* |
| **Transactions with the CNAHC Group:** | | | |
| Properties leasing | RMB | 147 | 75 |
| Aggregate sales of airline tickets and cargo space to the CNAHC Group | RMB | 324 | 175 |
| Comprehensive services | RMB | 862 | 827 |
| Subcontracting of charter flight services | RMB | 825 | 522 |
| Media and advertising services | RMB | 100 | 58 |
| Tourism co-operation services | RMB | 69 | 0 |
| Financial services | | | |
| Maximum daily outstanding deposits with CNAF *(note)* | RMB | 7,000 | 3,963 |
| Maximum daily outstanding loans from CNAF | RMB | 3,000 | 1,263 |
| **Transactions with the CNACG Group:** | | | |
| Ground handling, engineering, management and other services | RMB | 350 | 123 |
| **Transactions with Cathay Pacific Group:** | | | |
| Aggregate amount payable/paid by the Company to Cathay Pacific Group | HK$ | 900 | 287 |
| Aggregate amount payable/paid by Cathay Pacific Group to the Company | HK$ | 900 | 353 |
| **Transactions with the Lufthansa Group:** | | | |
| Aggregate amount payable/paid by the Company to the Lufthansa Group | RMB | 1,400 | 1,166 |
| Aggregate amount payable/paid by the Lufthansa Group to the Company | RMB | 1,400 | 816 |
| **Transactions with Air China Cargo:** | | | |
| Aggregate amount payable/paid by the Company to Air China Cargo | RMB | 46 | 2 |
| Aggregate amount payable/paid by Air China Cargo to the Company | RMB | 5,600 | 3,769 |

*Note:* The Company undertook in August 2010 that the actual daily outstanding deposits of the Company and its subsidiaries placed with CNAF would not exceed RMB4 billion.

### VII. Confirmation from Independent Non-executive directors

The independent non-executive directors of the Company have confirmed that all continuing connected transactions in the year ended 31 December 2011 to which the Company was a party have been entered into:

1. in the ordinary and usual course of business of the Company;

2. either:

   (i) on normal commercial terms; or

   (ii) where there was no comparable transactions to judge whether they were on normal commercial terms, on terms no less favourable to the Company than terms available to or from independent third parties, where applicable; and

3. in accordance with terms that were fair and reasonable and in the interests of the shareholders of the Company as a whole.

### VIII. Confirmation from the Auditor

The Company's external auditor, Ernst & Young, was engaged to report on the Group's continuing connected transactions in accordance with Hong Kong Standard on Assurance Engagement 3000 "Assurance Engagements Other Than Audits or Reviews of Historical Financial Information" and with reference to Practice Note 740 "Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules" issued by the Hong Kong Institute of Certified Public Accountant. The external auditor has issued his unqualified letter containing his findings and conclusions in respect of the continuing connected transactions described in pages 41 to 50 of this annual report in accordance with Rule 14A.38 of the Listing Rules. A copy of the letter has been provided to the Hong Kong Stock Exchange confirming that the continuing connected transactions above:

1. have been approved by the Board;

2. were conducted in accordance with the pricing policies as stated in the relevant agreements;

3. were entered into in accordance with the relevant agreements governing such transactions; and

4. have not exceeded the cap amounts disclosed in the Company's circulars dated 6 November 2009 and 10 November 2011 and the announcements dated 10 September 2010 and 27 October 2011.

## CONTRACT OF SIGNIFICANCE

Save as disclosed in "Connected Transactions" of this Report of the Directors, none of the Company or any of its subsidiaries entered into any contract of significance with the controlling shareholder or any of its subsidiaries, and there is no contract of significance in relation to provision of services by the controlling shareholder or any of its subsidiaries to the Company or any of its subsidiaries. None of the shareholders entered into any arrangement to waive or agree to waive any dividend.

## AUDITORS

The Company appointed Ernst & Young and Ernst & Young Hua Ming as its international auditors and domestic auditors respectively for the year ended 31 December 2011. Ernst & Young has audited the attached financial statements prepared in accordance with IFRSs. The Company has retained Ernst & Young and Ernst & Young Hua Ming since the date of its listing. A resolution in respect of the appointment of the Company's international and domestic auditors for the year ending 31 December 2012 will be proposed at the forthcoming 2011 annual general meeting of the Company to be convened in 2012.

# Report of the Supervisory Committee

To all Shareholders,

In 2011, in strict accordance with the relevant requirements of the Company Law of the PRC, the Articles of Association and the Rules of Procedure for Supervisory Committee's Meetings, the Supervisory Committee of the Company earnestly performed the duties conferred on it by laws and regulations. Members of the Supervisory Committee convened and attended relevant meetings, and conducted special inspections and researches, thereby overseeing the substantial decision-making processes of the Company; supervising the Board, its members and the management; and preventing any abuse of power on their part and any infringement of the legitimate rights and interests of the shareholders, the Company and its employees.

## (I) MEETINGS HELD BY THE SUPERVISORY COMMITTEE

At the second meeting of the third session of the Supervisory Committee held on 13 January 2011, the financial plan, the cash flow and fund raising and financing plans for the year 2011 and capital expenditure plan of the Company for the year 2011 were considered and approved. At the meeting, the Company was approved to engage fuel hedging business in compliance with the requirements set out in the "Fuel Hedging Transaction Operational Plan", meanwhile, documents such as the "Risk Management Manual for Overseas Financial Derivatives Business Conducted by Air China Limited", "Regulatory Requirements for Fuel Hedging Business of Air China Limited (Provisional)", "Feasibility Report on Conducting Financial Derivatives Business" and "Foreign Exchange Payment Limits Required for Fuel Hedging Business in 2011" were approved, and consent was given to the Company to apply for permission from relevant competent authorities to conduct overseas hedging business.

At the third meeting of the third session of the Supervisory Committee held on 28 March 2011, the Report of Supervisory Committee for the year 2010, the audited financial report and annual report for the year 2010 prepared by the Company in accordance with CASs and IASs respectively, the "Status of Implementation of Connected Transactions for the Year 2010", the "Special Explanation on Receivables from Controlling Shareholders and Connected Parties of the Company for the Year 2010", the profits distribution proposal of the Company for the year 2010, the self-assessment report on internal control of the Company for the year 2010 and the standardised working plan for implementing internal control measures of the Company for the year 2011", and the "Special Report on Deposit and Utilisation of Capital Raised from Private Placement of A Shares for the Year 2010 by Air China Limited" were considered and approved.

At the fourth meeting of the third session of the Supervisory Committee held on 27 April 2011, the first quarterly report for the year 2011 was considered and approved. The Committee considered that the preparation and approval procedures of the first quarterly report fully complied with PRC laws and regulations, Articles of Association and requirements of internal management system of the Company. Before passing resolutions, no violation of confidentiality requirements by persons who prepared and reviewed the first quarterly report of 2011 was found.

At the fifth meeting of the third session of the Supervisory Committee held on 24 August 2011, the interim report and the interim financial report for the year 2011 and the adjusted interim financial plan and capital expenditure plan of the Company for the year 2011 were considered and approved. At the meeting, the "Special Report on Deposit and Utilisation of Capital Raised from the Placing of A Shares by Air China Limited in the First Half of 2011" was approved. The Supervisory Committee also approved the management plan and operational procedures for fuel hedging business engaged by the Company, and agreed that the Board authorised the management of the Company to revise the "Regulatory Requirements for Fuel Hedging Business of the Company (Provisional)", the "Operational Procedures of the Financial Derivates Business of the Company" and the "Risk Management Manual of Fuel Hedging Transactions Engaged by the Company". Further, the intended cooperation on fuel hedging business between the Company and China Development Bank and the establishment of a joint operational platform were approved.

At the sixth meeting of the third session of the Supervisory Committee held on 10 October 2011, the proposal to provide an entrusted loan to Air China Cargo by the Company was considered and approved. With the prior consent of the independent directors, the Supervisory Committee agreed the Company to carry out the connected transaction of providing an entrusted loan of RMB1.5 billion to Air China Cargo, a controlled subsidiary of the Company, and the signing of the agreement in relation to the entrusted loan.

At the seventh meeting of the third session of the Supervisory Committee held on 26 October 2011, the third quarterly report of the Company for the year 2011 was considered and approved. At the meeting, the Supervisory Committee also approved the entering into of a framework agreement for connected transactions from 2011 to 2013 between the Company and Air China Cargo, the annual cap for the total amount of connected transactions for the years from 2011 to 2013 under the framework agreement, the submission to the Hong Kong Stock Exchange of the said exempted annual cap. The Supervisory Committee also approved the revision of the annual cap of connected transactions between the Company and CNAMC under the Advertising Services Framework Agreement and the signing of the Supplemental Advertising Services Framework Agreement with CNAMC.

## (II) INVESTIGATIONS AND RESEARCHES CONDUCTED BY THE SUPERVISORY COMMITTEE

Based on the strategic goals and key points of the Company set for 2011, the Supervisory Committee gained further insight into the implementation of corporate strategies, production and operations, internal control and team stability of the Company through on-site investigations and researches of sales departments in European and domestic markets, and played a good supervising role in the stable and sustainable development of the Company. In particular, the summary report of investigation and research prepared by the Supervisory Committee had successfully provided support for the establishment, adjustment and improvement of related managerial and marketing strategies by the management of the Company.

## (III) INDEPENDENT OPINIONS OF THE SUPERVISORY COMMITTEE ON THE COMPANY'S COMPLIANCE IN OPERATIONS

During the year, in accordance with the relevant PRC laws and regulations and the Articles of Association, the Supervisory Committee of the Company performed its supervision and inspection functions to monitor whether the convening of shareholders' general meetings and Board meetings complied with the required procedures and whether the significant decision-making processes were legitimate. The Board's implementation of the resolutions passed at the general meetings and the senior management's discharge of duty were also supervised and inspected.

The Supervisory Committee is of the opinion that the Company has generally formed an inter-linking governance structure of check and balance among its authority body, decision-making body, operational body and supervisory body and been in compliance with the relevant PRC laws and regulations. The Company's decision-making processes are legitimate and its internal control system is sound. None of the Directors or senior management of the Company was found to have, in discharging his or her duties, committed any act that was in violation of laws, regulations and the Articles of Association and detrimental to the interests of the Company and its shareholders. The information disclosed by the Company is true, accurate, complete and prompt. No misleading or false information was released.

## (IV) INDEPENDENT OPINIONS OF THE SUPERVISORY COMMITTEE ON THE COMPANY'S FINANCIAL POSITION

During the year, the Supervisory Committee focused its review on the quarterly, interim and annual financial reports. The Supervisory Committee is of the opinion that the standard unqualified opinion expressed in the auditors' report for the year 2011 issued by Ernst & Young reflects a true and fair view of the financial position and business performance of the Company.

## (V) INDEPENDENT OPINIONS OF THE SUPERVISORY COMMITTEE ON ACTUAL UTILISATION OF PROCEEDS FROM THE LATEST ISSUE OF SHARES

The Supervisory Committee is of the opinion that the management and utilisation of proceeds from the issue of shares in 2011 complied with the relevant requirements enacted by the China Securities Regulatory Commission and the Shanghai Stock Exchange and the proceeds from the issue of shares were treated as special deposit and utilised for special purpose by the Company. There was no disguised utilisation of the proceeds from the issue of shares, impairment of shareholders' interests nor any violation of the requirements of the utilisation of the proceeds from the issue of shares.

## (VI) INDEPENDENT OPINIONS OF THE SUPERVISORY COMMITTEE ON THE COMPANY'S ACQUISITIONS AND DISPOSALS OF ASSETS

During the year, the considerations of the asset acquisition and disposal transactions of the Company were fair and reasonable and no insider dealing, impairment of the interests of the Company's shareholders and asset drain were found.

## (VII) INDEPENDENT OPINIONS OF THE SUPERVISORY COMMITTEE ON THE COMPANY'S CONNECTED TRANSACTIONS

During the year, the connected transactions of the Company were conducted on an arm's length basis and in compliance with relevant procedures, PRC laws and regulations, the Articles of Association and the Listing Rules. The disclosure of the connected transactions was made in a timely manner and the transactions were not detrimental to the interests of the Company and its shareholders.

## (VIII) REVIEW BY THE SUPERVISORY COMMITTEE OF THE SELF-ASSESSMENT REPORT ON INTERNAL CONTROL AND ITS OPINIONS

At the eleventh meeting of the third session of the Supervisory Committee held on 26 March 2012, the self-assessment report on internal control of the Company for the year 2011 was considered and approved. The Supervisory Committee had no disagreement with the Board on the said report.

## (IX) OPINIONS OF THE SUPERVISORY COMMITTEE ON THE IMPLEMENTATION OF THE ADMINISTRATIVE RECORDAL SYSTEM FOR PERSONS WITH INSIDE INFORMATION

During the year, the Company earnestly implemented the administrative system of inside information of Air China Limited, and entered into confidential agreements with senior officers of important departments including the office of the President, planning and development department, human resource department, finance department and secretary office of the Board and employees who may obtain inside information. Meanwhile, all relevant persons in possession of inside information are required to file a "Recordal Filing Form for Persons in Possession of Inside Information" in a timely manner. The Supervisory Committee did not find any Director, Supervisor or senior management of the Company or any relevant persons who were aware of the inside information taking advantage of such inside information to buy or sell the shares of the Company before the disclosure of such price-sensitive information.

In 2011, guided by the principle of scientific development, the Company had grasped market opportunities in good timing and adhered to the practices of prudent operation and vigorous innovation. While ensuring the safe operation and accomplishing various important operation tasks, the Company enhanced its capabilities in strategic leading, market controlling and comprehensive management. As a result, the Company created significant value for itself and the shareholders and further laid a solid foundation for the next round of leap-forward development.

In 2012, the Supervisory Committee will, as always, perform its duties diligently, strengthen its inspection and supervision roles and maximise its functions with a view to further improving the corporate governance and promoting the healthy development of the Company.

By order of the Supervisory Committee

**Li Qinglin**
*Chairman of the Supervisory Committee*

Beijing, PRC
26 March 2012

# Profile of Directors, Supervisors and Senior Management

As at the date of this annual report,

## 1. DIRECTORS

**Mr. Wang Changshun**, aged 54, is the Chairman and a non-executive director of the Company. Mr. Wang joined the Group in 2012. He graduated from the University of Science and Technology of China with a Ph.D. degree in management science and engineering. Mr. Wang was previously the Secretary of Communist Party Committee and Deputy Director of Xin Jiang Regional Administration and had served as Deputy General Manager, a Member of the Standing Committee to the Communist Party Committee and Secretary of Communist Party Committee of Xinjiang Airlines. From October 2000 to September 2002, Mr. Wang worked as General Manager, Deputy Chairman of the Board and Deputy Secretary of Communist Party Committee of China Southern Airlines Company Limited. Mr. Wang served as Deputy General Manager and a Member of Communist Party Committee of China Southern Air Holding Company and General Manager, Deputy Chairman of the Board and Deputy Secretary of Communist Party Committee of China Southern Airlines Company Limited from September 2002 to August 2004. Mr. Wang became Deputy Director and a Member of Communist Party Committee of General Administration of Civil Aviation of China from August 2004 to March 2008. Mr. Wang served as a Member of Communist Party Committee and Deputy Director of Civil Aviation Administration of China ("CAAC") and Secretary of Communist Party Committee of the department directly administered by CAAC and Chairman of National Labour Union of Civil Aviation from March 2008 to October 2011. Mr. Wang has served as General Manager and Deputy Secretary of Communist Party Committee of CNAHC since October 2011. Mr. Wang has been serving as the Chairman of the Company since January 2012.

**Ms. Wang Yinxiang**, aged 56, is the Vice Chairman and a non-executive director of the Company. Ms. Wang joined the Group in July 1988. She graduated from the Party School of the Central Committee of the Communist Party of China majoring in economics and management. Ms. Wang is a senior engineer of political work and a senior flight attendant. Ms. Wang served several positions at Air China International Corporation, including Vice Captain of the in-flight service team of the Chief Flight Team, Deputy Manager of the in-flight service division, Deputy Manager of the passenger cabin service division and Deputy Secretary of the Communist Party Committee. In October 2002, Ms. Wang served several positions in CNAHC, including Deputy General Manager, Head of the Disciplinary and Supervisory Committee of the Communist Party Group and Secretary of the Communist Party Committee of CNAHC. Since March 2008, Ms. Wang has been serving as Secretary of the Communist Party Group, Deputy General Manager and Secretary of the Communist Party Committee of CNAHC, and was appointed as President of the Labour Union of CNAHC from July 2003 to July 2009. Ms. Wang has been serving as the Vice Chairman of the Company since October 2008.

**Mr. Cao Jianxiong**, aged 52, is a non-executive director of the Company. He joined the Group in June 2009. Mr. Cao holds a master degree in economics from the Eastern China Normal University and is a senior economist. He was appointed as the Deputy General Manager and Chief Financial Officer of China Eastern Airlines Corporation Limited in December 1996. In September 1999, he was appointed as the Vice President of China Eastern Airlines Group Corporation. Commencing from September 2002 till December 2008, he served as Vice President and a member of Communist Party Group of China Eastern Airlines Group Corporation and was also Secretary of the Communist Party Committee of China Eastern Airlines Northwest Company from December 2002 to September 2004. From October 2006 to December 2008, he served as the President and the Deputy Party Secretary of the Communist Party Committee of China Eastern Airlines Corporation Limited. Since December 2008, Mr. Cao has been serving as the Deputy General Manager and a member of Communist Party Group of CNAHC. Mr. Cao has been serving as a non-executive director of the Company since June 2009.

# Profile of Directors, Supervisors and Senior Management

**Mr. Sun Yude**, aged 57, is a non-executive director of the Company. He joined the Group in October 2002. Mr. Sun graduated from China Civil Aviation Institute majoring in economic management. He started his career in China's civil aviation industry in 1972 and served various positions such as Deputy Head of CAAC Taiyuan Terminal and Head of its Ningbo Terminal, as well as General Manager of CNAC Zhejiang Airlines. In October 2002, Mr. Sun was appointed Vice President of Air China International Corporation, and concurrently took up the position of General Manager of its Zhejiang branch, and was appointed as Vice President of the Company in September 2004. Mr. Sun was appointed as Chairman in November 2004, and President and Deputy Secretary of the Communist Party Committee in December 2005, of Shandong Aviation, and has also served as Director and President of CNACG from March 2007 to September 2011. Mr. Sun served as Secretary of the Communist Party Committee of CNACG from April 2007 to December 2009. Since May 2009, he has been serving as Deputy General Manager and a member of the Communist Party Group of CNAHC. Mr. Sun has been serving as a non-executive director of the Company since October 2010.

**Mr. Christopher Dale Pratt**, aged 55, is a non-executive director of the Company. He joined the Group in June 2006. Mr. Pratt has an honours degree in modern history from the University of Oxford. He joined John Swire & Sons Limited in 1978 and has worked with the Swire Group in its offices in Hong Kong, Australia and Papua New Guinea. He is also the Chairman of John Swire & Sons (H.K.) Limited, Swire Pacific Limited, Cathay Pacific, Hong Kong Aircraft Engineering Company Limited and Swire Properties Limited, and a Director of The Hongkong and Shanghai Banking Corporation Limited. Mr. Pratt has been serving as a non-executive director of the Company since October 2007.

**Mr. Ian Sai Cheung Shiu**, aged 56, is a non-executive director of the Company. He joined the Group in October 2010. He holds a bachelor's degree in business administration from University of Hawaii and an MBA degree from the University of Western Ontario. Mr. Shiu worked at offices of Cathay Pacific in Hong Kong, the Netherlands, Singapore and the United Kingdom. He has been a director of Cathay Pacific and Hong Kong Dragon Airlines Limited since October 2008. He has also been a director of John Swire & Sons (H.K.) Limited since July 2010. He has been serving as a director of Swire Pacific Limited since August 2010. Mr. Shiu has been serving as a non-executive director of the Company since October 2010.

**Mr. Cai Jianjiang**, aged 48, is the President and an executive director of the Company. He joined the Group in 2001. Mr. Cai graduated from China Civil Aviation Institute majoring in aviation control and English. Mr. Cai was appointed as General Manager of Shenzhen Airlines in 1999. He joined Air China International Corporation in 2001 as Manager of its Shanghai Branch, and subsequently as Assistant to the President and Manager of the marketing department. In October 2002, he was appointed as Vice President of Air China International Corporation, and subsequently was appointed as Secretary of the Communist Party Committee and Vice President of the Company in September 2004. He has been serving as President and Deputy Secretary of the Communist Party Committee of the Company and a member of the Communist Party Group of CNAHC since February 2007. Since May 2010, he has been serving as the Chairman of Shenzhen Airlines. Mr. Cai has been serving as an executive director of the Company since October 2004.

**Mr. Fan Cheng**, aged 56, is the Vice President and an executive director of the Company. He joined the Group in September 2004. Mr. Fan graduated from Nanjing Institute of Chemistry and Chemical Engineering with a major in organic fertilizer and has an MBA degree from Guanghua School of Management, Peking University. Mr. Fan is a senior accountant, senior engineer and Certified Public Accountant. Mr. Fan was appointed as Deputy General Manager of China New Technology Venture Capital Company in 1996. He started his career in China's civil aviation industry in 2001, and served as General Manager of the corporate management department and capital management department of CNAHC in October 2002 and Chief Financial Officer of the Company in September 2004. Since October 2006, he has been serving as Vice President and Chief Financial Officer of the Company. From December 2009 to May 2010, he served as Secretary of the Communist Party Committee of Shenzhen Airlines. From March 2010 to April 2010, he served as President of Shenzhen Airlines and from March 2010 to May 2010, he served as the Chairman of Shenzhen Airlines. Since February 2011, he has been serving as Secretary of the Communist Party Committee of the Company. Mr. Fan has been serving as an executive director of the Company since October 2004.

# Profile of Directors, Supervisors and Senior Management

**Mr. Fu Yang**, aged 62, is an independent non-executive director of the Company. Mr. Fu previously served as Deputy director of the Economic Law Office of the National People's Congress Law Committee, Vice President of the third, fourth and fifth sessions of the All China Lawyers Association, a visiting professor of Center for Environment Law at the Law School of Renmin University of China. He is a partner and the director of Kang Da Law Firm in Beijing. He is also an arbitrator of China International Economic and Trade Arbitration Commission. Mr. Fu has been serving as an independent non-executive director of the Company since June 2009.

**Mr. Li Shuang**, aged 67, is an independent non-executive director of the Company. He is a professor of accounting and a tutor to doctorate students. Mr. Li graduated from the Foreign Language Department of Beijing Normal University in 1968. In 1982, he obtained a master's degree in economics from the Research Institute for Fiscal Science of the Ministry of Finance, and in October of the same year lectured at Central Institute of Finance & Banking (currently known as Central University of Finance and Economics) where he served various positions including the Head of the accounting department, director of the academic affair office, Dean and Vice President. From 1994 to 1997, he had been invited to the United States twice as a visiting scholar. In October 1996, he was entitled to the special allowance granted by the State Council. From 1999 to 2004, he worked as a Deputy Secretary-in-General and Adviser of the Chinese Institute of Certified Public Accountants. From May 2001 to June 2010, he served as an independent non-executive director of Da Cheng Fund Management Co., Ltd., China Minmetals Non-ferrous Metals Co. Ltd., Zhong Bao Ke Kong Investment Co., Ltd., Beijing Centergate Technologies (Holding) Co., Ltd., Shenyin & Wanguo Securities Investment Co., Ltd., Chengde Xinxin Vanadium and Titanium Co., Ltd. and Beijing Wangfujing Department Store (Group) Co., Ltd., respectively. Mr. Li had served as a non-executive director of China Shoto plc. from January 2005 to June 2011. He has been serving as an independent non-executive director of the Company since October 2010.

**Mr. Han Fangming**, aged 45, is an independent non-executive director of the Company. Mr. Han graduated from Peking University with a Ph.D degree. Mr. Han was a member of the 10th and 11th of National Committee of the Chinese People's Political Consultative Conference ("CPPCC") and is currently a Deputy Chairman of the Foreign Affairs Committee of CPPCC and the convener of the Public Diplomacy Team, the Deputy Chief Editor and Head of the editorial department of "Public Diplomacy Quarterly", Executive Member of the Chinese-African People's Friendship Association, Executive Member of the Chinese People's Association for Friendship with Foreign Countries, Executive Member of China Economic and Social Council, chairman of China-Africa Economic and Technological Cooperation Committee, Deputy director of China Overseas-Educated Scholars Development Foundation, Vice President of China Society for Southeast Asian Studies and founding chairman of the Charhar Institute under the Think-Tank for Foreign Policy and International Relationship, a researcher at the Center for Studies of World Modernisation Process of Peking University, a visiting professor at Tibet University and an arbitrator of the China International Economic and Trade Arbitration Commission. In 1999, he joined TCL Group and was appointed as an independent non-executive director of TCL Multimedia Technology Holdings Limited. He has been serving as an executive director of TCL Corporation from 2006 to June 2011. He has served as Vice Chairman of TCL Corporation since June 2011. Mr. Han has been serving as an independent non-executive director of the Company since October 2010.

**Mr. Yang Yuzhong**, aged 67, is an independent non-executive director of the Company. He graduated from Beijing Aeronautical Institute majoring in aircraft design and manufacturing. From July 1999 to July 2006, Mr. Yang served as the Deputy General Manager of China Aviation Industry Corporation I, during which period he was also the head of Chinese Aeronautical Establishment and the chairman of AVIC1 Commercial Aircraft Co., Ltd.. Mr. Yang has been a consultant of Aviation Industry Corporation of China since August 2006. He served as an independent non-executive director of China National Materials Company Limited from June 2007 to December 2009. Mr. Yang has been an independent non-executive director of China South Locomotive & Rolling Stock Corporation Limited since December 2007 and an external director of China National Materials Group Corporation Ltd. since December 2009. Mr. Yang has been serving as an independent non-executive director of the Company since May 2011.

## 2. SUPERVISORS

**Mr. Li Qinglin**, aged 56, is the chairman of the supervisory committee of the Company. He joined the Group in October 2010. Mr. Li graduated from Beijing Television University majoring in Chinese and Zhongnanhai Amateur University majoring in administrative management, and is a senior engineer of political work. Mr. Li served various positions, including a Section Chief, Deputy director, director, Vice Director-General and Director-General, as well as the Chairman of the Labour Union, of the Government Office Administration of the State Council. From 1998 to 2000, he served as a Deputy director of the Hebei Leading Group Office of Poverty Alleviation and Development. Since 2000, he had served different positions, including a Deputy director of the Work Department under the Supervisory Committee of Central Enterprises Working Commission, Deputy director of the Office of Central Enterprises Working Commission, Deputy director and Inspector of the General Office of the State-owned Assets Supervision and Administration Committee of the State Council and a director of the Office of the Stability Preservation Leading Team of the State-owned Assets Supervision and Administration Committee. In September 2008, he was appointed as the Head of the Disciplinary and Supervisory Committee and a member of the Communist Party Group of CNAHC. Mr. Li has been serving as a supervisor of the Company since October 2010.

**Mr. Zhang Xueren**, aged 58, is a supervisor of the Company. He joined the Group in July 1988. Mr. Zhang graduated from Sichuan International Studies University majoring in English, and enrolled in the MBA programme of Peking University. Mr. Zhang holds the title of Senior Economist. He started his career in China's civil aviation in 1975 and served as a Section Chief and then a director of the operations department of Beijing Administrative Bureau of CAAC, the Head of the cargo department of Air China International Corporation, the General Manager of Tianjin branch of Air China International Corporation and Vice President of Air China International Corporation. In 2004, he served as a director and Vice President of CNACG. Since December 2009, he has been serving as the director, Secretary of the Communist Party Committee and Vice President of CNACG. Mr. Zhang has been serving as a supervisor of the Company since October 2010.

**Mr. Zhou Feng**, aged 50, is a supervisor of the Company. Mr. Zhou joined the Group in February 1997. He obtained a master's degree in economics from Shanghai University of Finance and Economics. He held various positions, including the Accountant, the Deputy Division Head, the Division Head of the finance division and the director of the finance and audit department of the CAAC, Zhejiang Bureau; the director, the Chief Accountant of finance department of CNAC Zhejiang Airlines; the Assistant General Manager of China National Aviation Corporation (Macau) Company Limited; the Deputy General Manager, the Chief Accountant and a member of the party committee of China National Aviation Finance Co., Ltd. ("CNAF"), the director, the Executive Vice President of Samsung Air China Life Insurance Co., Ltd.. Mr. Zhou has been Secretary of the Communist Party Committee and the Deputy General Manager of CNAF since August 2010. He has also been the General Manager of the finance department of CNAHC since April 2011. Mr. Zhou has been serving as a supervisor of the Company since November 2011.

**Ms. Xiao Yanjun**, aged 47, is a supervisor of the Company. Ms. Xiao joined the Group in July 1988. She obtained an EMBA degree from Tsinghua University and a Juris Master from Renmin University of China and is a professional of political work. From July 1988 to April 2002, Ms. Xiao held various positions in Air China International Corporation, including an Instructor at the Training Department, the Secretary of the Communist Party Committee, an Organisor at division level, Secretary of the Party branch and Head of Officer Training. She served as the Training Manager of the Human Resource Department of the Company from April 2002 to March 2008. Ms. Xiao has been Deputy director of the Labour Union of the Company since March 2008. Ms. Xiao has been serving as a supervisor of the Company since June 2011.

**Mr. Su Zhiyong**, aged 48, is a supervisor of the Company. He joined the Group in July 1988. Mr. Su graduated from Party School of the Central Committee of Communist Party Committee majoring in economics and management. Mr. Su started his career in China's civil aviation industry in 1983 and served as Officer and Personnel Clerk of the Communist Party Committee of the equipment management division, Secretary of the vehicle maintenance office (team II) of ground services department, and, starting from September 2006, Deputy Manager and Manager of the vehicle maintenance centre of ground services department of Air China International Corporation. Since August 2007, he has been serving as Senior Manager of the station operation centre of ground services department of the Company. Mr. Su has been serving as a supervisor of the Company since August 2009.

## 3. OTHER SENIOR MANAGEMENT

**Mr. Feng Gang**, aged 48, graduated from Sichuan University majoring in semiconductor. He started his career in July 1984 and served various positions including Cadre of the political department and Dispatcher of the scheduling office in Chengdu Civil Aviation Authority, Manager of Guangzhou Sales Department, Deputy Manager of Operating Department, Manager of Development and Service Department, Deputy Manager of Marketing Department, Manager of the Cargo Logistics Company of China Southwest Airlines, Deputy General Manager of China Southwest Airlines, Assistant to President of Air China International Corporation, General Manager and Party Secretary of China National Aviation Holding Assets Management Company. He served as the Chairman, President and Deputy Secretary of the Communist Party Committee of Shandong Aviation from May 2007 to April 2010. Mr. Feng has been serving as Vice President of the Company since April 2010. He has also served as a director, President and Deputy Secretary of the Communist Party Committee of Shenzhen Airlines since May 2010.

**Mr. Ma Chongxian**, aged 46, graduated from Inner Mongolia University majoring in planning and statistics. Mr. Ma started his career in July 1988 and served as Planner of the Mechanical Division of CAAC Inner Mongolia Bureau and various positions in Air China, including Deputy Chief and Secretary of the Party branch of Aircraft Repair Plant in Inner Mongolia branch, General Manager of the Bluesky Customer Service Department, Deputy General Manager of Inner Mongolia branch, Deputy General Manager, Party Secretary and General Manager of Zhejiang branch. He served as General Manager and Deputy Secretary of the Communist Party Committee of Hubei Branch of the Company from June 2009. Mr. Ma has been serving as Vice President of the Company as well as Chairman, President of Shandong Aviation and Vice Chairman of Shandong Airlines since April 2010.

**Mr. Xu Chuanyu**, aged 47, graduated from China Civil Aviation Institution majoring in aviation and obtained an MBA degree from Tsinghua University. Mr. Xu is a second-class Pilot. He started his career in July 1985. Mr. Xu previously served various positions in Air China International Corporation, including Pilot, Deputy Captain of the Third Group of the Chief Flight Team and an Inspector in the Safety Supervisory Office. In December 2001, Mr. Xu was appointed as the Deputy Captain of the Chief Flight Team of Air China International Corporation. In March 2006, Mr. Xu was appointed as the General Manager and Deputy Secretary of the Communist Party Committee of the Tianjin branch of the Company. Mr. Xu has been serving as Deputy Chief Operation Officer and General Manager of Operation Control Centre of the Company and a Member and Deputy Secretary of the Communist Party Committee of the Company from January 2009 to March 2011. Mr. Xu served as the Chief Pilot from January 2009 to April 2011. He has been serving as Vice President and Chief Operation Officer of the Company since February 2011 and March 2011 respectively.

**Mr. Wang Mingyuan**, aged 46, graduated from Xiamen University majoring in planning and statistics. He started his career in July 1988 and served various positions in Southwest Airlines, including Assistant of the planning department, Manager of the Production Plan Office of the Sales & Marketing Department, Deputy Manager of the Sales & Marketing Department Deputy Manager and Manager of the Market Department, and served various positions in the Company, including Deputy General Manager of the Marketing Department, Member of the Commerce Commission, Member of the Communist Party Committee and General Manager of Network Revenue Department. Mr. Wang has been appointed as a director of the Commerce Commission and Deputy Secretary of the Communist Party Committee of the Company since July 2008. He has been serving as Vice President and a member of the Standing Committee of the Communist Party Committee of the Company since February 2011.

**Mr. Zhao Xiaohang**, aged 50, graduated from Tsinghua University majoring in management engineering and holds a postgraduate diploma and a master's degree. Mr. Zhao started his career in August 1986 and served various positions, including Assistant of the Planning Department of Beijing Administration Bureau of CAAC, Assistant, Section Chief and Deputy Division Chief of the Planning Department of Air China, Manager and Deputy Secretary of the Ground Services Department, General Manager of the Planning and Development Department and Assistant President of Air China. He served as director and Vice President of CNACG from September 2003 to May 2004, director, Vice President and Secretary of the Commission for Discipline Inspection of CNACG from May 2004 to February 2011 and Chairman, executive director and General Manager of Air Macau from December 2009 to April 2011. He has been serving as director and General Manager of China National Aviation Company Limited since July 2005 and director and General Manager of China National Aviation Corporation (Macau) Company Limited since April 2007. Mr. Zhao has also been serving as Vice President of the Company since February 2011, a director of Shandong Aviation since April 2011 and Chairman of Dalian Airlines since August 2011.

# Profile of Directors, Supervisors and Senior Management

**Ms. Feng Rune**, aged 49, obtained an EMBA degree from HEC Paris. Ms. Feng started her career in July 1984 and served various positions, including an Instructor of Science & Education Division of CAAC Inner Mongolia Bureau, Deputy Chief, Chief, Deputy director and director of Science & Education Department of Air China Inner Mongolia branch; Manager of Human Resource Department and Head of Party and Mass Affairs Department of Air China Inner Mongolia branch. She also served as Deputy Secretary of the Communist Party Committee and Secretary of Commission for Discipline Inspection of Air China Inner Mongolia branch. In October 2002, she began to serve as Head and director of Office of Communist Party Group of CNAHC. From January 2009 to March 2011, she was appointed as Secretary of the Communist Party Committee and Deputy General Manager of Air China Cargo. She has been serving as Deputy Secretary of the Communist Party Committee and Secretary of Commission for Discipline Inspection of the Company since February 2011 as well as a member and Secretary of the Communist Party Committee of the department directly under the Company since March 2011. She has been serving as president of the Labour Union of the Company since June 2011.

**Mr. Chai Weixi**, aged 50, graduated from City University of Seattle and holds a postgraduate diploma and a master's degree. He is a senior engineer. Mr. Chai started his career in September 1980 and served various positions, including Engineer and Manager of airframe team of Engineering Department of Aircraft Maintenance and Engineering Corporation, Deputy director of the Engineering Division under the Aircraft Engineering Department of Air China, Manager of Aircraft Maintenance Subdivision and Manager of Aircraft Overhaul Division of Aircraft Maintenance and Engineering Corporation, General Manager of Aircraft Engineering Department of Air China and Deputy General Manager of the Engineering Technology Branch of Air China. He served as General Manager, director, member of the Communist Party Committee of Aircraft Maintenance and Engineering Corporation and a member of the Communist Party Committee of the Engineering Technology Branch of Air China in October 2005. In April 2009, he served as General Manager and Deputy Secretary of the Communist Party Committee of the Engineering Technology Branch of Air China and director of Aircraft Maintenance and Engineering Corporation. Mr. Chai has been serving as Vice President of the Company since March 2012.

**Mr. Xu Jianqiang**, aged 59, graduated from Party School of the Central Committee of C.P.C. majoring in economics and management. Mr. Xu is a senior engineer of political work. He started his career in April 1969. He was the navigation director and the deputy political director of communication team of air force at Yingshanchang Station, deputy chief of cadre at political department of the 44th airborne division, party secretary of the First Group of the Chief Flight Team, deputy party secretary of training department, party secretary of cabin services department, party secretary of marketing department of Air China. He was appointed as Party Secretary and Deputy director of Commercial Committee of the Company in June 2005. He has been serving as Chief Economist of the Company since July 2009.

**Mr. Liu Tiexiang**, aged 45, graduated from State Organ Branch of Party School of the Central Committee of C.P.C. majoring economics and management. He is a second-class Pilot and currently serves as Chief Pilot. He started his career in June 1983 and became a member of the Communist Party Committee in April 1986. Mr. Liu previously served various positions in Air China, including pilot, squadron leader of the Third Group of the Chief Flight Team, deputy director and deputy manager of Flight Training Center, deputy general manager of Aviation Security Technology Department, deputy general manager and general manager of Flight Technical Management Department and vice captain of the Chief Flight Team of Air China. He served as captain of the Chief Flight Team of Air China and Deputy Secretary of the Communist Party Committee from June 2008 to April 2011. He has been serving as Chief Pilot of the Company since April 2011.

**Ms. Rao Xinyu**, aged 45, graduated from Beijing Foreign Studies University with a postgraduate diploma. Ms. Rao started her career in July 1990 and served as an officer at vice-director level and an officer at director level of the International Department of the CAAC, Deputy Manager of the General Office, Deputy Director of the Administration Office and Deputy General Manager of the Planning and Investment Department of China National Aviation Corporation, respectively. From December 2002, Ms. Rao was appointed as Deputy General Manager of the Planning and Investment Department of CNAHC. From October 2003, she served as Deputy General Manager of the Planning and Development Department of CNAHC. Ms. Rao has been Deputy Director of the Secretariat of the Board and General Manager of Investor Relation Department of the Company since April 2005. She has been serving as the Secretary to the Board and one of the Joint Company Secretaries since December 2011.

## 4. JOINT COMPANY SECRETARIES

**Ms. Rao Xinyu**, Ms. Rao's biography is set out in the section headed "Other Senior Management" above.

**Ms. Tam Shuit Mui**, aged 40, graduated from the State University of New York at Buffalo, USA in 1998 with a Bachelor of Science in Business Administration majoring in accounting and financial analysis. Ms. Tam is an associate member of the Hong Kong Institute of Certified Public Accountants and a member of The American Institute of Certified Public Accountants, USA. Between September 1998 and April 2001, Ms. Tam worked as an accountant with Tommy Hilfiger (HK) Limited. From May 2001 to October 2007, Ms. Tam served as the company secretary of Chaoyue Group Limited (formerly known as Graneagle Holdings Limited), a company listed on the Hong Kong Stock Exchange. Ms. Tam has been serving as one of the Joint Company Secretaries of the Company since October 2008.

# Independent Auditors' Report

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

We have audited the consolidated financial statements of Air China Limited (the "Company"), its subsidiaries and joint ventures (collectively, the "Group") set out on pages 65 to 165, which comprise the consolidated and company statements of financial position as at 31 December 2011, and the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

## DIRECTORS' RESPONSIBILITY FOR THE CONSOLIDATED FINANCIAL STATEMENTS

The Company's Directors are responsible for the preparation of consolidated financial statements that give a true and fair view in accordance with International Financial Reporting Standards and the disclosure requirements of the Hong Kong Companies Ordinance, and for such internal control as the Directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

## AUDITORS' RESPONSIBILITY

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. Our report is made solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation of consolidated financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Company's Directors, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

# Independent Auditors' Report

## OPINION

In our opinion, the consolidated financial statements give a true and fair view of the financial position of the Company and of the Group as at 31 December 2011, and of the profit and cash flows of the Group for the year then ended in accordance with International Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

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

Hong Kong
27 March 2012

# Consolidated Income Statement

Year ended 31 December 2011
(Prepared under International Financial Reporting Standards)

| | Notes | 2011 RMB'000 | 2010 RMB'000 |
|---|---|---|---|
| **TURNOVER** | | | |
| Air traffic revenue | 4 | **93,343,421** | 78,209,188 |
| Other operating revenue | 5 | **5,066,081** | 4,278,351 |
| | | **98,409,502** | 82,487,539 |
| **OPERATING EXPENSES** | | | |
| Jet fuel costs | | **(34,703,369)** | (24,096,078) |
| Movements in fair value of fuel derivative contracts | | **85,447** | 1,954,071 |
| Take-off, landing and depot charges | | **(8,740,822)** | (7,707,019) |
| Depreciation | | **(9,560,907)** | (8,569,370) |
| Aircraft maintenance, repair and overhaul costs | | **(2,612,678)** | (2,577,185) |
| Employee compensation costs | 6 | **(12,270,065)** | (9,851,935) |
| Air catering charges | | **(2,662,984)** | (2,044,359) |
| Aircraft and engine operating lease expenses | | **(3,931,549)** | (3,488,014) |
| Other operating lease expenses | | **(668,916)** | (712,005) |
| Other flight operation expenses | | **(9,342,935)** | (8,227,555) |
| Selling and marketing expenses | | **(5,480,514)** | (4,602,745) |
| General and administrative expenses | | **(2,261,549)** | (1,637,824) |
| | | **(92,150,841)** | (71,560,018) |
| **PROFIT FROM OPERATIONS** | 7 | **6,258,661** | 10,927,521 |
| Finance revenue | 8 | **3,361,295** | 1,980,015 |
| Finance costs | 8 | **(1,594,015)** | (1,449,249) |
| Share of profits and losses of associates | | **1,328,798** | 3,375,325 |
| **PROFIT BEFORE TAX** | | **9,354,739** | 14,833,612 |
| Tax | 11 | **(2,292,073)** | (2,497,748) |
| **PROFIT FOR THE YEAR** | | **7,062,666** | 12,335,864 |
| **Attributable to:** | | | |
| Owners of the parent | | **7,082,374** | 12,005,004 |
| Non-controlling interests | | **(19,708)** | 330,860 |
| | | **7,062,666** | 12,335,864 |
| **Dividends:** | 13 | | |
| Interim | | **–** | – |
| Proposed final | | **1,521,251** | 1,523,829 |
| | | **1,521,251** | 1,523,829 |
| **Earnings per share attributable to equity holders of the parent:** | 14 | | |
| Basic and diluted | | **RMB58.23 cents** | RMB103.10 cents |

# Consolidated Statement of Comprehensive Income

Year ended 31 December 2011
(Prepared under International Financial Reporting Standards)

| | 2011<br>*RMB'000* | 2010<br>*RMB'000* |
|---|---|---|
| **PROFIT FOR THE YEAR** | **7,062,666** | 12,335,864 |
| **OTHER COMPREHENSIVE LOSSES** | | |
| Share of other comprehensive losses of associates | **(8,538)** | (47,303) |
| Exchange realignment | **(890,417)** | (546,911) |
| Others | **–** | (1,150) |
| **OTHER COMPREHENSIVE LOSSES FOR THE YEAR, NET OF TAX** | **(898,955)** | (595,364) |
| **TOTAL COMPREHENSIVE INCOME FOR THE YEAR** | **6,163,711** | 11,740,500 |
| **Attributable to:** | | |
| Owners of the parent | **6,193,453** | 11,412,599 |
| Non-controlling interests | **(29,742)** | 327,901 |
| | **6,163,711** | 11,740,500 |

# Consolidated Statement of Financial Position

31 December 2011
(Prepared under International Financial Reporting Standards)

| | Notes | 2011 RMB'000 | 2010 RMB'000 |
|---|---|---|---|
| **NON-CURRENT ASSETS** | | | |
| Property, plant and equipment | 15 | **112,399,431** | 96,152,542 |
| Lease prepayments | 16 | **2,142,684** | 2,163,649 |
| Investment properties | 17 | **240,879** | – |
| Intangible asset | 18 | **37,221** | 41,076 |
| Goodwill | 19 | **1,310,830** | 1,657,675 |
| Interests in associates | 22 | **13,397,031** | 14,188,426 |
| Advance payments for aircraft and flight equipment | | **19,443,291** | 18,946,626 |
| Deposits for aircraft under operating leases | | **420,854** | 391,600 |
| Long term receivable from the ultimate holding company | 23 | **–** | 31,813 |
| Available-for-sale investments | 24 | **27,182** | 27,182 |
| Deferred tax assets | 25 | **3,077,502** | 2,193,002 |
| | | **152,496,905** | 135,793,591 |
| **CURRENT ASSETS** | | | |
| Aircraft and flight equipment held for sale | 26 | **92,487** | 77,682 |
| Inventories | 27 | **1,810,320** | 1,608,951 |
| Accounts receivable | 28 | **2,700,731** | 3,092,069 |
| Bills receivable | | **1,601** | 14,295 |
| Prepayments, deposits and other receivables | 29 | **2,697,192** | 2,284,230 |
| Financial assets | 30 | **12,144** | 27,379 |
| Due from the ultimate holding company | 32 | **428,561** | 617,140 |
| Due from related companies | 32 | **20,194** | 3,244 |
| Tax recoverable | | **–** | 6,171 |
| Pledged deposits | 33 | **132,565** | 843,065 |
| Cash and cash equivalents | 33 | **15,457,372** | 14,401,714 |
| | | **23,353,167** | 22,975,940 |
| **TOTAL ASSETS** | | **175,850,072** | 158,769,531 |
| **CURRENT LIABILITIES** | | | |
| Air traffic liabilities | | **(4,562,773)** | (3,608,700) |
| Accounts payable | 34 | **(10,417,186)** | (8,100,472) |
| Bills payable | 35 | **–** | (387,327) |
| Other payables and accruals | 36 | **(12,815,775)** | (9,259,833) |
| Financial liabilities | 30 | **(223,137)** | (427,329) |
| Due to related companies | 32 | **(190,775)** | (181,002) |
| Tax payable | | **(1,707,553)** | (2,210,372) |
| Obligations under finance leases | 37 | **(2,687,925)** | (2,223,240) |
| Interest-bearing bank loans and other borrowings | 38 | **(28,137,313)** | (25,482,725) |
| Provision for major overhauls | 39 | **(589,123)** | (503,628) |
| | | **(61,331,560)** | (52,384,628) |
| **NET CURRENT LIABILITIES** | | **(37,978,393)** | (29,408,688) |
| **TOTAL ASSETS LESS CURRENT LIABILITIES** | | **114,518,512** | 106,384,903 |

# Consolidated Statement of Financial Position

31 December 2011
(Prepared under International Financial Reporting Standards)

| | Notes | **2011** **RMB'000** | 2010 RMB'000 |
|---|---|---|---|
| **NON-CURRENT LIABILITIES** | | | |
| Obligations under finance leases | 37 | **(19,191,860)** | (16,061,352) |
| Interest-bearing bank loans and other borrowings | 38 | **(39,398,481)** | (42,159,439) |
| Provision for major overhauls | 39 | **(2,496,294)** | (2,105,150) |
| Provision for early retirement benefit obligations | | **(203,213)** | (220,236) |
| Long term payables | 40 | **(231,061)** | (265,159) |
| Deferred income | 41 | **(3,459,138)** | (3,196,103) |
| Deferred tax liabilities | 25 | **(1,213,030)** | (1,006,227) |
| | | **(66,193,077)** | (65,013,666) |
| **NET ASSETS** | | **48,325,435** | 41,371,237 |
| **EQUITY** | | | |
| Equity attributable to owners of the parent | | | |
| Issued capital | 42 | **12,891,955** | 12,891,955 |
| Treasury shares | 43 | **(2,889,399)** | (2,613,232) |
| Reserves | 44 | **36,113,243** | 31,159,231 |
| | | **46,115,799** | 41,437,954 |
| **NON-CONTROLLING INTERESTS** | | **2,209,636** | (66,717) |
| **TOTAL EQUITY** | | **48,325,435** | 41,371,237 |

**Cai Jianjiang**
*Director*

**Fan Cheng**
*Director*

# Consolidated Statement of Changes in Equity

Year ended 31 December 2011
(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 | Proposed final dividend RMB'000 | Total RMB'000 | Non-controlling interests RMB'000 | Total equity RMB'000 |
| As 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 year | – | – | – | – | – | 12,005,004 | – | 12,005,004 | 330,860 | 12,335,864 |
| Other comprehensive losses for the year: | | | | | | | | | | |
| Share of other comprehensive losses of associates | – | – | (47,303) | – | – | – | – | (47,303) | – | (47,303) |
| Exchange realignment | – | – | – | – | (543,952) | – | – | (543,952) | (2,959) | (546,911) |
| Others | – | – | (1,150) | – | – | – | – | (1,150) | – | (1,150) |
| Total comprehensive income/(losses) for the year | – | – | (48,453) | – | (543,952) | 12,005,004 | – | 11,412,599 | 327,901 | 11,740,500 |
| Issue of new shares | 640,593 | – | – | – | – | – | – | 640,593 | – | 640,593 |
| Share premium | – | – | 5,780,556 | – | – | – | – | 5,780,556 | – | 5,780,556 |
| Elimination for reciprocal shareholding | – | (293,353) | – | – | – | – | – | (293,353) | – | (293,353) |
| Acquisition of non-controlling interests in a subsidiary | – | – | (18,210) | – | – | – | – | (18,210) | (112) | (18,322) |
| Acquisition of a subsidiary | – | – | (127) | – | – | – | – | (127) | (433,077) | (433,204) |
| Appropriation of statutory reserve funds | – | – | – | 614,386 | – | (614,386) | – | – | – | – |
| Proposed final dividend | – | – | – | – | – | (1,523,829) | 1,523,829 | – | – | – |
| As at 31 December 2010 | 12,891,955 | (2,613,232) | 18,256,092* | 2,230,086* | (2,168,360)* | 11,317,584* | 1,523,829* | 41,437,954 | (66,717) | 41,371,237 |
| As at 1 January 2011 | 12,891,955 | (2,613,232) | 18,256,092 | 2,230,086 | (2,168,360) | 11,317,584 | 1,523,829 | 41,437,954 | (66,717) | 41,371,237 |
| Profit for the year | – | – | – | – | – | 7,082,374 | – | 7,082,374 | (19,708) | 7,062,666 |
| Other comprehensive losses for the year: | | | | | | | | | | |
| Share of other comprehensive losses of associates | – | – | (8,538) | – | – | – | – | (8,538) | – | (8,538) |
| Exchange realignment | – | – | – | – | (880,383) | – | – | (880,383) | (10,034) | (890,417) |
| Total comprehensive income/(losses) for the year | – | – | (8,538) | – | (880,383) | 7,082,374 | – | 6,193,453 | (29,742) | 6,163,711 |
| Elimination of reciprocal shareholding | – | (276,167) | – | – | – | – | – | (276,167) | – | (276,167) |
| Capital contribution by non-controlling interest of a subsidiary | – | – | 327,759 | – | – | – | – | 327,759 | 1,736,095 | 2,063,854 |
| Final dividend declared | – | – | – | – | – | – | (1,523,829) | (1,523,829) | – | (1,523,829) |
| Establishment of new subsidiaries | – | – | – | – | – | – | – | – | 570,000 | 570,000 |
| Appropriation of statutory reserve funds | – | – | – | 679,126 | – | (679,126) | – | – | – | – |
| Transfer to discretionary reserve funds and others | – | – | – | 614,386 | – | (657,757) | – | (43,371) | – | (43,371) |
| Proposed final dividend | – | – | – | – | – | (1,521,251) | 1,521,251 | – | – | – |
| **As at 31 December 2011** | 12,891,955 | (2,889,399) | 18,575,313* | 3,523,598* | (3,048,743)* | 15,541,824* | 1,521,251* | 46,115,799 | 2,209,636 | 48,325,435 |

* These reserve accounts comprise the consolidated reserves of RMB36,113,243,000 (2010: RMB31,159,231,000) in the consolidated statement of financial position.

# Consolidated Statement of Cash Flows

Year ended 31 December 2011
(Prepared under International Financial Reporting Standards)

| | Notes | 2011 RMB'000 | 2010 RMB'000 |
|---|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | | |
| Profit before tax | | **9,354,739** | 14,833,612 |
| Adjustments for: | | | |
| Share of profits and losses of associates | | **(1,328,798)** | (3,375,325) |
| Exchange gains, net | 8 | **(3,117,700)** | (1,919,415) |
| Interest income | 8 | **(240,234)** | (60,307) |
| Finance costs | | **1,594,015** | 1,449,249 |
| Dividend income on long term investments | | **–** | (152,678) |
| Gains on financial assets and financial liabilities, net | | **(29,493)** | (1,964,074) |
| Depreciation | 15 | **9,560,907** | 8,569,370 |
| Impairment loss on property, plant and equipment | 15 | **2,237,403** | 1,863,194 |
| Gains on disposal of property, plant and equipment, net | 5 | **(252,662)** | (159,011) |
| Losses on derecognition of property, plant and equipment | 7 | **31,345** | 55,434 |
| Losses on disposal of lease prepayments | | **1,461** | – |
| Amortisation of lease prepayments | 16 | **53,247** | 87,039 |
| Impairment of aircraft held for sale | 26 | **99,669** | 185,992 |
| Impairment of goodwill | 7 | **176,891** | – |
| Impairment of interests in an associate | 7 | **19,810** | – |
| Impairment of inventories | 7 | **77,785** | 236,219 |
| Impairment of accounts receivable | 7 | **3,771** | 8,983 |
| Impairment of prepayments, deposits and other receivables | 7 | **239,582** | 118,609 |
| | | **18,481,738** | 19,776,891 |
| Decrease/(increase) in deposits for aircraft under operating leases | | **(55,073)** | 37,661 |
| Increase in inventories | | **(279,154)** | (200,807) |
| Decrease/(increase) in accounts receivable | | **366,006** | (376,008) |
| Decrease/(increase) in bills receivable | | **12,694** | (11,806) |
| Increase in prepayments, deposits and other receivables | | **(545,913)** | (470,431) |
| Decrease/(increase) in amount due from the ultimate holding company | | **220,392** | (55,993) |
| Decrease/(increase) in amounts due from related companies | | **(16,950)** | 6,950 |
| Decrease in amounts due from associates | | **28,398** | – |
| Increase in air traffic liabilities | | **954,073** | 825,730 |
| Increase in accounts payable | | **2,358,106** | 4,323 |
| Decrease in bills payable | | **(387,327)** | (610,953) |
| Increase in other payables and accruals | | **3,403,782** | 1,134,326 |
| Increase in amounts due to related companies | | **9,773** | 67,978 |
| Increase in amounts due to associates | | **6,118** | – |
| Increase/(decrease) in provision for major overhauls | | **476,639** | (183,644) |
| Increase/(decrease) in provision for early retirement benefit obligations | | **(17,023)** | 10,230 |
| Increase in deferred income | | **263,035** | 500,594 |
| Cash generated from operations | | **25,279,314** | 20,455,041 |
| Interest paid | | **(2,143,019)** | (1,586,501) |
| Corporate income tax and profits tax paid | | **(3,466,417)** | (502,918) |
| **NET CASH FLOWS FROM OPERATING ACTIVITIES** | | **19,669,878** | 18,365,622 |

# Consolidated Statement of Cash Flows

Year ended 31 December 2011
(Prepared under International Financial Reporting Standards)

| | Notes | **2011** **RMB'000** | 2010 RMB'000 |
|---|---|---|---|
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | | |
| Purchases of property, plant and equipment | | **(22,253,020)** | (9,835,131) |
| Proceeds from disposal of property, plant and equipment | | **1,106,061** | 189,986 |
| Proceeds from disposal of aircraft and flight equipment held-for-sale | | **69,430** | 119,486 |
| Increase in lease prepayments | | **(76,709)** | (190,300) |
| Decrease in intangible assets | | **3,855** | 8,191 |
| Increase in advance payments for aircraft and flight equipment | | **(496,664)** | (7,410,917) |
| Net settlements of financial liabilities | | **(159,463)** | (174,982) |
| Increase in balances with associates | | **–** | 7,964 |
| Decrease in pledged deposits | | **710,500** | 1,002,793 |
| Decrease/(increase) in non-pledged deposits with original maturity of more than three months when acquired | | **(4,648,235)** | 4,785 |
| Interest received | | **240,234** | 60,307 |
| Capital contributions by non-controlling interests of subsidiaries | | **2,803,808** | – |
| Acquisition of a subsidiary | | **–** | 1,820,051 |
| Capital contributions to an associate | | **–** | 109,154 |
| Acquisition of a non-controlling interest of a subsidiary | | **–** | (90,122) |
| Capital contributions to associates | | **–** | (197,246) |
| Dividend income from long term investments | | **–** | 2,050 |
| Dividends received from associates | | **1,030,762** | 515,951 |
| **NET CASH FLOWS USED IN INVESTING ACTIVITIES** | | **(21,669,441)** | (14,057,980) |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | | |
| New bank loans and other loans | | **28,866,385** | 28,849,284 |
| Repayment of bank loans and other loans | | **(26,435,068)** | (24,138,001) |
| Repayment of principals under finance lease obligations | | **(2,339,461)** | (3,669,392) |
| Dividends paid | | **(1,523,829)** | – |
| Proceeds from issuance of new shares | | **–** | 6,421,149 |
| **NET CASH FLOWS FROM/(USED IN) FINANCING ACTIVITIES** | | **(1,431,973)** | 7,463,040 |
| **NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS** | | **(3,431,536)** | 11,770,682 |
| Cash and cash equivalents at beginning of year | | **14,376,050** | 2,676,309 |
| Effect of exchange rate changes on cash and cash equivalents | | **(161,041)** | (70,941) |
| **CASH AND CASH EQUIVALENTS AT END OF YEAR** | | **10,783,473** | 14,376,050 |
| **ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS** | | | |
| Cash and bank balances | 33 | **5,079,886** | 3,576,984 |
| Non-pledged time deposits with original maturity of less than three months when acquired | 33 | **5,703,587** | 10,799,066 |
| | | **10,783,473** | 14,376,050 |

# Statement of Financial Position

31 December 2011
(Prepared under International Financial Reporting Standards)

| | Notes | 2011 RMB'000 | 2010 RMB'000 |
|---|---|---|---|
| **NON-CURRENT ASSETS** | | | |
| Property, plant and equipment | 15 | **80,350,831** | 69,772,391 |
| Lease prepayments | 16 | **1,592,275** | 1,629,183 |
| Intangible asset | 18 | **37,221** | 41,076 |
| Interests in subsidiaries | 20 | **18,242,738** | 16,763,748 |
| Interests in joint ventures | 21 | **856,076** | 856,076 |
| Interests in associates | 22 | **646,366** | 707,787 |
| Advance payments for aircraft and flight equipment | | **16,077,566** | 14,097,427 |
| Deposits for aircraft under operating leases | | **251,729** | 202,668 |
| Long term receivable from the ultimate holding company | 23 | **–** | 31,813 |
| Available-for-sale investments | 24 | **3,366** | 3,366 |
| Deferred tax assets | 25 | **2,261,490** | 1,515,000 |
| | | **120,319,658** | 105,620,535 |
| **CURRENT ASSETS** | | | |
| Aircraft and flight equipment held for sale | 26 | **77,211** | 73,560 |
| Inventories | 27 | **762,546** | 610,976 |
| Accounts receivable | 28 | **1,224,596** | 1,447,627 |
| Bills receivable | | **–** | 14,000 |
| Prepayments, deposits and other receivables | 29 | **1,641,153** | 1,076,104 |
| Entrusted loans | 31 | **2,200,000** | – |
| Due from the ultimate holding company | | **432,267** | 617,669 |
| Due from related companies | | **7,803** | 2 |
| Cash and cash equivalents | 33 | **7,797,123** | 11,501,617 |
| | | **14,142,699** | 15,341,555 |
| **TOTAL ASSETS** | | **134,462,357** | 120,962,090 |
| **CURRENT LIABILITIES** | | | |
| Air traffic liabilities | | **(3,708,720)** | (2,974,145) |
| Accounts payable | 34 | **(6,555,427)** | (4,886,489) |
| Other payables and accruals | 36 | **(5,546,130)** | (4,320,488) |
| Financial liabilities | 30 | **(176,167)** | (340,049) |
| Due to related companies | 32 | **(170,187)** | (159,913) |
| Tax payable | | **(1,223,212)** | (1,994,158) |
| Obligations under finance leases | 37 | **(2,505,900)** | (2,048,727) |
| Interest-bearing bank loans and other borrowings | 38 | **(21,383,897)** | (19,093,115) |
| Provision for major overhauls | 39 | **(235,964)** | (135,662) |
| | | **(41,505,604)** | (35,952,746) |
| **NET CURRENT LIABILITIES** | | **(27,362,905)** | (20,611,191) |
| **TOTAL ASSETS LESS CURRENT LIABILITIES** | | **92,956,753** | 85,009,344 |

# Statement of Financial Position

31 December 2011
(Prepared under International Financial Reporting Standards)

| | Notes | **2011 RMB'000** | 2010 RMB'000 |
|---|---|---|---|
| **NON-CURRENT LIABILITIES** | | | |
| Obligations under finance leases | 37 | **(18,428,125)** | (15,407,125) |
| Interest-bearing bank loans and other borrowings | 38 | **(27,170,298)** | (27,576,233) |
| Provision for major overhauls | 39 | **(1,380,343)** | (1,214,265) |
| Provision for early retirement benefit obligations | | **(55,608)** | (77,820) |
| Long term payables | 40 | **(643)** | (2,376) |
| Deferred income | 41 | **(2,631,068)** | (2,447,707) |
| Deferred tax liabilities | 25 | **(136,000)** | (128,387) |
| | | **(49,802,085)** | (46,853,913) |
| **NET ASSETS** | | **43,154,668** | 38,155,431 |
| **EQUITY** | | | |
| Issued capital | 42 | **12,891,955** | 12,891,955 |
| Reserves | 44 | **30,262,713** | 25,263,476 |
| **TOTAL EQUITY** | | **43,154,668** | 38,155,431 |

**Cai Jianjiang**
*Director*

**Fan Cheng**
*Director*

## 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 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 25 February 2010, the Company, Fine Star Enterprises Corporation ("Fine Star", an indirectly wholly-owned subsidiary of the Company), Air China Cargo Limited ("Air China Cargo", another wholly-owned subsidiary of the Company), Cathay Pacific Airways Limited ("Cathay Pacific") and Cathay Pacific 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 RMB851,621,140 and Fine Star agreed to make a further capital contribution of RMB238,453,919 in cash to Air China Cargo; and the Company agreed to sell Fine Star to Advent Fortune Limited ("AFL") for a consideration of RMB626,793,159. On 19 April 2011, these transactions were completed and were approved by the State Administration for Industry & Commerce of the People's Republic of China. Upon completion of these transactions, the equity interests held by the Company, Cathay Pacific and AFL became 51%, 25% and 24%, respectively.

On 28 February 2011, the Company, Beijing Enterprises Group Company, Beijing State-owned Assets Management Co., Ltd. and Zhong Da Yin Rui Co., Ltd. set up a private jet company named Beijing Airlines Co., Ltd ("Beijing Airlines"). The registered capital of Beijing Airlines is RMB1,000,000,000. The equity interest held by the Company is 51%.

On 1 August 2011, the Company and Dalian Bao Shui Zheng Tong Co., Ltd. set up an airline company named Dalian Airlines Co., Ltd ("Dalian Airlines"). The registered capital of Dalian Airlines is RMB1,000,000,000. The equity interest held by the Company is 80%.

The principal activities of the Company, its subsidiaries and joint ventures (collectively the "Group") and associates consist of the provision of airline, airline-related services, including aircraft engineering services, air catering 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 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Basis of preparation

The Group's financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs", which comprise standards and interpretations approved by the International Accounting Standards Board (the "IASB"), and International Accounting Standards ("IASs") and Standing Interpretations Committee interpretations approved by the International Accounting Standards Committee that remain in effect) and the disclosure requirements of the Hong Kong Companies Ordinance.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Basis of preparation (Continued)

As at 31 December 2011, the Group's net current liabilities amounted to approximately RMB37,978 million, which comprised current assets of approximately RMB23,353 million and current liabilities of approximately RMB61,331 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 financial statements, the Directors of the Company have considered the Group's sources of liquidity and believe that adequate funding is available to fulfil the Group's debt obligations and capital expenditure requirements. Accordingly, the consolidated financial statements have been prepared on a basis that the Group will be able to continue as a going concern.

The financial statements have been prepared on a historical cost basis, except for derivative financial instruments, which have been measured at fair value, and non-current assets held for sale, which have been stated at the lower of their carrying amounts and fair value less costs to sell. These financial statements are presented in Renminbi ("RMB") and all values are rounded to the nearest thousand except when otherwise indicated.

### Impact of new and revised IFRSs

The Group has adopted the following new and revised IFRSs for the first time for the current year's financial statements.

| | |
|---|---|
| IFRS 1 Amendment | Amendment to IFRS 1 *First-time Adoption of International Financial Reporting Standards – Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters* |
| IAS 24 (Revised) | *Related Party Disclosures* |
| IAS 32 Amendment | Amendment to IAS 32 *Financial Instruments: Presentation – Classification of Rights Issues* |
| IFRIC 14 Amendments | Amendments to IFRIC 14 *Prepayments of a Minimum Funding Requirement* |
| IFRIC 19 | *Extinguishing Financial Liabilities with Equity Instruments* |
| *Improvements to IFRSs 2010* | Amendments to a number of IFRSs issued in May 2010 |

In May 2010, the IASB issued its third omnibus of amendments to its standards, including improvements to IFRS 1, IFRS 3, IFRS 7, IAS 1, IAS 27, IAS 34 and IFRIC 13, primarily with a view to removing inconsistencies and clarifying wording.

Other than as further explained below regarding the impact of IAS 24 (Revised), the adoption of these new and revised IFRSs has had no significant financial effect on these financial statements.

IAS 24 (Revised) clarifies and simplifies the definition of related parties. The new definitions emphasise a symmetrical view of related party relationships and clarifies the circumstances in which persons and key management personnel affect related party relationships of an entity. In addition, the revised standard introduces an exemption from the general related party disclosure requirements for transactions with a government and entities that are controlled, jointly controlled or significantly influenced by the same government as the reporting entity. The adoption of IAS 24 (Revised) has resulted in the re-presenting of the comparative related party disclosures.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Issued but not yet effective IFRSs

The Group has not applied the following new and revised IFRSs, that have been issued but are not yet effective, in these financial statements.

| | |
|---|---|
| IFRS 1 Amendments | Amendments to IFRS 1 *First-time Adoption of International Financial Reporting Standards – Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters*[1] |
| IFRS 7 Amendments | Amendments to IFRS 7 *Financial Instruments: Disclosures – Transfers of Financial Assets*[1] |
| IFRS 7 Amendments | Amendments to IFRS 7 *Financial Instruments: Disclosures – Offsetting Financial Assets and Financial Liabilities*[4] |
| IFRS 9 | *Financial Instruments*[6] |
| IFRS 10 | *Consolidated Financial Statements*[4] |
| IFRS 11 | *Joint Arrangements*[4] |
| IFRS 12 | *Disclosure of Interests in Other Entities*[4] |
| IFRS 13 | *Fair Value Measurement*[4] |
| IAS 1 Amendments | Amendments to IAS 1 *Presentation of Financial Statements – Presentation of Items of Other Comprehensive Income*[3] |
| IAS 12 Amendments | Amendments to IAS 12 *Income Taxes – Deferred Tax: Recovery of Underlying Assets*[2] |
| IAS 19 (Revised) | *Employee Benefits*[4] |
| IAS 27 (Revised) | *Separate Financial Statements*[4] |
| IAS 28 (Revised) | *Investments in Associates and Joint Ventures*[4] |
| IAS 32 Amendments | Amendments to IAS 32 *Financial Instruments: Presentation – Offsetting Financial Assets and Financial Liabilities*[5] |
| IFRIC 20 | *Stripping Costs in the Production Phase of a Surface Mine*[4] |

[1] Effective for annual periods beginning on or after 1 July 2011
[2] Effective for annual periods beginning on or after 1 January 2012
[3] Effective for annual periods beginning on or after 1 July 2012
[4] Effective for annual periods beginning on or after 1 January 2013
[5] Effective for annual periods beginning on or after 1 January 2014
[6] Effective for annual periods beginning on or after 1 January 2015

Further information about those changes that are expected to significantly affect the Group is as follows:

IFRS 9 issued in November 2009 is the first part of phase 1 of a comprehensive project to entirely replace IAS 39 *Financial Instruments: Recognition and Measurement*. This phase focuses on the classification and measurement of financial assets. Instead of classifying financial assets into four categories, an entity shall classify financial assets as subsequently measured at either amortised cost or fair value, on the basis of both the entity's business model for managing the financial assets and the contractual cash flow characteristics of the financial assets. This aims to improve and simplify the approach for the classification and measurement of financial assets compared with the requirements of IAS 39.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Issued but not yet effective IFRSs (Continued)

In October 2010, the IASB issued additions to IFRS 9 to address financial liabilities (the "Additions") and incorporated in IFRS 9 the current derecognition principles of financial instruments of IAS 39. Most of the Additions were carried forward unchanged from IAS 39, while changes were made to the measurement of financial liabilities designated at fair value through profit or loss using the fair value option ("FVO"). For these FVO liabilities, the amount of change in the fair value of a liability that is attributable to changes in credit risk must be presented in other comprehensive income ("OCI"). The remainder of the change in fair value is presented in profit or loss, unless presentation of the fair value change in respect of the liability's credit risk in OCI would create or enlarge an accounting mismatch in profit or loss. However, loan commitments and financial guarantee contracts which have been designated under the FVO are scoped out of the Additions.

IAS 39 is aimed to be replaced by IFRS 9 in its entirety. Before this entire replacement, the guidance in IAS 39 on hedge accounting derecognition and impairment of financial assets continues to apply. The Group expects to adopt IFRS 9 from 1 January 2015.

IFRS 10 establishes a single control model that applies to all entities including special purpose entities or structured entities. It includes a new definition of control which is used to determine which entities are consolidated. The changes introduced by IFRS 10 require management of the Group to exercise significant judgement to determine which entities are controlled, compared with the requirements that were in IAS 27 and SIC-12 *Consolidation – Special Purpose Entities.* IFRS 10 replaces the portion of IAS 27 *Consolidated and Separate Financial Statements* that addresses the accounting for consolidated financial statements. It also includes the issues raised in SIC-12.

IFRS 11 replaces IAS 31 *Interests in Joint Ventures* and SIC-13 *Jointly controlled Entities – Non-monetary Contributions by Venturers*. It describes the accounting for joint arrangements with joint control. It addresses only two forms of joint arrangements, i.e., joint operations and joint ventures, and removes the option to account for joint ventures using proportionate consolidation.

IFRS 12 includes the disclosures requirements for subsidiaries, joint arrangements, associates and structured entities that are previously included in IAS 27 *Consolidated and Separate Financial Statements*, IAS 31 *Interests in Joint Ventures* and IAS 28 *Investments in Associates*. It also introduces a number of new disclosure requirements for these entities.

Consequential amendments were made to IAS 27 and IAS 28 as a result of the issuance of IFRS 10, IFRS 11 and IFRS 12. The Group expects to adopt IFRS 10, IFRS 11, IFRS 12, and the consequential amendments to IAS 27 and IAS 28 from 1 January 2013.

IFRS 13 provides a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across IFRSs. The standard does not change the circumstances in which the Group is required to use fair value, but provides guidance on how it should be applied where its use is already required or permitted by other standards within IFRSs. The Group expects to adopt IFRS 13 prospectively from 1 January 2013.

Amendments to IAS 1 change the grouping of items presented in OCI. Items that could be reclassified (or "recycled") to profit or loss at a future point in time (for example, upon derecognition or settlement) would be presented separately from items which will never be reclassified. The Group expects to adopt the amendments from 1 January 2013.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Basis of consolidation

The consolidated financial statements include the financial statements of the Company, its subsidiaries and joint ventures (collectively the "Group") for the year ended 31 December 2011. The financial statements of the subsidiaries and joint ventures are prepared for the same reporting period as the Company, using consistent accounting policies. The results of subsidiaries and joint ventures are consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases. All intra-group balances, transactions, unrealised gains and losses resulting from intra-group transactions and dividends are eliminated on consolidation in full. Adjustments are made to bring into line any dissimilar accounting policies that may exist.

Total comprehensive income within a subsidiary is attributed to the non-controlling interest even if that results in a deficit balance.

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction.

If the Group loses control over a subsidiary, it derecognises (i) the assets (including goodwill) and liabilities of the subsidiary, (ii) the carrying amount of any non-controlling interest and (iii) the cumulative translation differences recorded in equity; and recognises (i) the fair value of the consideration received, (ii) the fair value of any investment retained and (iii) any resulting surplus or deficit in profit or loss. The Group's share of components previously recognised in other comprehensive income is reclassified to profit or loss or retained earnings, as appropriate.

### Foreign currencies

These financial statements are presented in RMB, which is the Company's functional and presentation currency. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency.

Foreign currency transactions recorded by the entities in the Group are initially recorded in their respective functional currency rates ruling at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rates of exchange ruling at the end of the reporting period.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. The gain or loss arising on retranslation of non-monetary items is treated in line with the recognition of gain or loss on change in fair value of the item (i.e., translation differences on items whose fair value gain or loss is recognised in other comprehensive income or profit or loss are also recognised in other comprehensive income or profit or loss, respectively).

The functional currencies of certain overseas subsidiaries, joint ventures and associates are currencies other than RMB. As at the end of the reporting period, the assets and liabilities of these entities are translated into RMB at the rates of exchange ruling at the end of the reporting period and their income statements are translated into RMB at the average exchange rates for the period of the translations. The resulting exchange differences are recognised in other comprehensive income and accumulated in the foreign exchange translation reserve. On disposal of a foreign operation, the component of other comprehensive income relating to that particular foreign entity is recognised in the income statement.

For the purpose of the consolidated statement of cash flows, the cash flows of overseas subsidiaries and joint ventures are translated into RMB at the exchange rates ruling at the dates of the cash flows. Frequently recurring cash flows of overseas subsidiaries which arise throughout the year are translated into RMB at the average exchange rates for the period of the translations. Effect of foreign exchange rate changes on cash and cash equivalents is presented separately in the consolidated statement of cash flows as a reconciling item.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Subsidiaries

A subsidiary is an entity in which the Company, directly or indirectly, controls more than half of its voting power or issued share capital or controls the composition of its board of Directors; or over which the Company has a contractual right to exercise a dominant influence with respect to that entity's financial and operating policies.

The results of subsidiaries are included in the Company's income statement to the extent of dividends received and receivable. The Company's interests in subsidiaries that are not classified as held for sale in accordance with IFRS 5 are stated at cost less any impairment losses.

### Joint ventures

A joint venture is an entity set up by contractual arrangement, whereby the Group and other parties undertake an economic activity. A jointly-controlled entity is a joint venture that is subject to joint control, resulting in none of the participating parties having unilateral control over the economic activity of the jointly-controlled entity. The Group has investments in certain joint ventures which are considered as jointly-controlled entities.

The Group's investments in its jointly-controlled entities are accounted for by the proportionate consolidation method, which involves recognising its share of the jointly-controlled entities' assets, liabilities, income and expenses with similar items in the consolidated financial statements on a line-by-line basis. Unrealised gains and losses resulting from transactions between the Group and its jointly-controlled entities are eliminated to the extent of the Group's investments in the jointly-controlled entities, except where unrealised losses provide evidence of an impairment of the asset transferred. Adjustments are made to bring into line any dissimilar accounting policies that may exist.

The results of joint ventures are included in the Company's income statement to the extent of dividends received and receivable. The Company's investments in joint ventures are treated as non-current assets and are stated at cost less any impairment losses.

### Associates

An associate is an entity in which the Group has a long term interest of generally not less than 20% of the equity voting rights and over which it is in a position to exercise significant influence and which is neither a subsidiary nor a joint venture of the Group. The Group's investments in its associates are accounted for under the equity method of accounting.

The investments in associates are carried in the consolidated statement of financial position at the Group's share of net assets of the associates, less any impairment losses. Goodwill arising from the acquisition of associates is included in the carrying amounts of the investments and is not individually tested for impairment. The Group's share of the post-acquisition results and reserves of associates is included in the consolidated income statement and consolidated reserves, respectively. Unrealised gains and losses resulting from transactions between the Group and its associates are eliminated to the extent of the Group's investments in the associates, except where unrealised losses provide evidence of an impairment of the asset transferred.

The financial statements of the associates are prepared for the same reporting year as the Company. Adjustments are made to bring into line any dissimilar accounting policies that may exist.

The results of associates are included in the Company's income statement to the extent of dividends received and receivable. The Company's investments in associates are treated as non-current assets and are stated at cost less any impairment losses.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Business combinations and goodwill

Business combinations are accounted for using the acquisition method. The consideration transferred is measured at the acquisition date fair value which is the sum of the acquisition date fair values of assets transferred by the Group, liabilities assumed by the Group to the former owners of the acquiree and the equity interests issued by the Group in exchange for control of the acquiree. The Group elects to measure the non-controlling interests in the acquiree that are present ownership interests and entitle their holders to a proportionate share of net assets in the event of liquidation at the proportionate share of the acquiree's identifiable net assets. All other components of non-controlling interests are measured at fair value. Acquisition costs are expensed as incurred.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value as at the acquisition date through profit or loss.

Any contingent consideration to be transferred by the acquirer is recognised at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration which is deemed to be an asset or liability will be recognised in accordance with IAS 39 either in profit or loss or as a change to other comprehensive income. If the contingent consideration is classified as equity, it will not be remeasured. Subsequent settlement is accounted within equity. In instances where the contingent consideration does not fall within the scope of IAS 39, it is measured in accordance with the appropriate IFRS.

Goodwill is initially measured at cost, being the excess of the aggregate of the consideration transferred, the amount recognised for non-controlling interests and any fair value of the Group's previously held equity interests in the acquiree over the identifiable net assets acquired and liabilities assumed. If the sum of this consideration and other items is lower than the fair value of the net assets of the subsidiary acquired, the difference is, after reassessment, recognised in profit or loss as a gain on bargain purchase.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is tested for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. The Group performs its annual impairment test of goodwill as at 31 December. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units.

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units) to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognised. An impairment loss recognised for goodwill is not reversed in a subsequent period.

Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Related parties

A party is considered to be related to the Group if:

(a) the party is a person or a close member of that person's family and that person (i) has control or joint control over the Group; (ii) has significant influence over the Group; or (iii) is a member of the key management personnel of the Group or of a parent of the Group.

(b) the party is an entity where any of the following conditions applies:

(i) the entity and the Group are members of the same group;

(ii) one entity is an associate or joint venture of the other entity (or of a parent, subsidiary or fellow subsidiary of the other entity);

(iii) the entity and the Group are joint ventures of the same third party;

(iv) one entity is a joint venture of a third entity and the other entity is an associate of the third entity;

(v) the entity is a post-employment benefit plan for the benefit of employees of either the Group or an entity related to the Group;

(vi) the entity is controlled or jointly controlled by a person identified in (a); and

(vii) a person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

### Property, plant and equipment and depreciation

Property, plant and equipment other than construction in progress, are stated at cost less accumulated depreciation and any impairment losses. When an item of property, plant and equipment is classified as held for sale or when it is part of a disposal group classified as held for sale, it is not depreciated and is accounted for in accordance with IFRS 5, as further explained in the accounting policy for "Non-current assets and disposal groups held for sale". The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use.

Expenditure incurred after items of property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to the income statement in the period in which it is incurred. In situations where the recognition criteria are satisfied, the expenditure for a major inspection is capitalised in the carrying amount of the asset as a replacement. Where significant parts of property, plant and equipment are required to be replaced at intervals, the Group recognises such parts as individual assets with specific useful lives and depreciates them accordingly.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Property, plant and equipment and depreciation (Continued)

Depreciation is calculated on the straight-line basis to write off the cost of each item of property, plant and equipment to its residual value over its estimated useful life. The estimated useful lives and residual values used for this purpose are as follows:

| | Estimated useful life | Residual value | Depreciation rate |
|---|---|---|---|
| Aircraft and flight equipment: | | | |
| Core parts of airframe and engine | 15 to 25 years | 5% | 3.80%-6.33% |
| Overhaul of airframe and cabin refurbishment | 5 to 12 years | Nil | 8.33%-20% |
| Overhaul of engine | 2 to 8 years | Nil | 12.50%-50% |
| Rotable | 3 to 20 years | Nil – 5% | 4.75%-33.33% |
| Buildings | 5 to 50 years | Nil – 10% | 1.8%-20% |
| Machinery | 4 to 20 years | Nil – 10% | 4.50%-25% |
| Transportation equipment | 3 to 20 years | Nil – 10% | 4.50%-33.33% |
| Office equipment | 4 to 8 years | Nil – 10% | 11.25%-25% |

Where parts of an item of property, plant and equipment have different useful lives, the cost of that item is allocated on a reasonable basis among the parts and each part is depreciated separately.

The assets' residual values, useful lives and the depreciation method are reviewed, and adjusted if appropriate, at least at each financial year end.

An item of property, plant and equipment and any significant part initially recognised is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the income statement in the year the asset is derecognised.

Fixed assets under finance leases are depreciated over the same terms as self-owned fixed assets. If it is reasonably assured that the ownership of the leased property could be transferred to the Group after the lease periods, the leased assets are depreciated over the lease term. Otherwise, leased assets are depreciated over the shorter of the estimated useful lives of the assets and the lease term.

Construction in progress represents buildings or various infrastructure projects under construction, and equipment pending for installation in aircraft. Construction in progress is stated at cost less any impairment losses and is not depreciated. Costs of construction in progress comprise the direct costs of construction, the cost of equipment as well as capitalised borrowing costs on related borrowed funds during the construction or installation period. Construction in progress is reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

The carrying amounts of property, plant and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying amounts may not be recoverable.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Non-current assets held for sale

Non-current assets are classified as held for sale if their carrying amounts will be recovered principally through a sales transaction rather than through continuing use. For this to be the case, the asset must be available for immediate sale in its present condition subject only to terms that are usual and customary for the sale of such assets and its sale must be highly probable.

Non-current assets classified as held for sale are measured at the lower of their carrying amounts and fair values less costs to sell. Property, plant and equipment and intangible assets classified as held for sale are not depreciated or amortised.

### Intangible assets

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is the fair value as at the date of acquisition. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are subsequently amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each financial year end.

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash-generating unit level. Such intangible assets are not amortised. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is accounted for on a prospective basis.

The estimated useful life of intangible asset is as follows:

| | **Estimated useful life** |
|---|---|
| Admission rights to Star Alliance | indefinite |

### Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Finance leases, which transfer to the Group substantially all the risks and rewards of ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased asset or, if lower, at the present value of the minimum lease payments. Minimum lease payments are apportioned between the finance charges and reduction of the outstanding liability so as to achieve a constant periodical rate of interest on the remaining balance of the liability. Finance charges are charged to the income statement.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Leases (Continued)

Leases where the lessor retains substantially all the risks and rewards of ownership of the asset are classified as operating leases. Where the Group is the lessor, assets leased by the Group under operating leases are included in non-current assets and rentals receivable under the operating leases are credited to the income statement on the straight-line basis over the lease terms. Where the Group is the lessee, rentals payable under operating leases net of any incentives received from the lessor are charged to the income statement on the straight-line basis over the lease terms.

Prepaid land lease payments under operating leases are initially stated at cost and subsequently recognised on the straight-line basis over the lease terms. When the lease payments cannot be allocated reliably between the land and buildings elements, the entire lease payments are included in the cost of the land and buildings as a finance lease in property, plant and equipment.

### Investment properties

Investment properties are interests in land and buildings (including the leasehold interest under an operating lease for a property which would otherwise meet the definition of an investment property) held to earn rental income and/or for capital appreciation.

Investment properties are measured initially at cost, including transaction costs. Subsequent costs are recognised in the carrying amount of the investment properties if it is probable that future economic benefits associated with the item will flow to the entity and the costs can be measured reliably. Otherwise, these costs are recognised in profit or loss as incurred.

The Group chooses the cost model to measure its investment properties.

Depreciation is calculated on the straight-line basis to write off the cost to its residual value over its estimated useful life. The estimated useful lives and residual values used for this purpose are as follows:

| | **Estimated useful life** | **Residual value** | **Depreciation rate** |
|---|---|---|---|
| Buildings | 20 to 30 years | 5% | 3.17%-4.75% |
| Lease prepayments | 50 years | – | 2% |

The carrying amounts of investment properties measured at the cost model are reviewed for impairment when events or changes in circumstances indicate that the carrying amounts may not be recoverable.

### Advance payments for aircraft and flight equipment

Advance contractual payments to aircraft manufacturers to secure deliveries of aircraft and flight equipment in future years, including attributable finance costs, are included in assets. The advances are accounted for as part of the cost of property, plant and equipment upon delivery of the aircraft and flight equipment.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Impairment of non-financial assets other than goodwill

Where an indication of impairment exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use, and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case the recoverable amount is determined for the cash-generating unit to which the asset belongs. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Impairment losses are recognised in the income statement in the period in which it arises in those expense categories consistent with the function of the impaired asset.

An assessment is made at the end of each reporting period as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such an indication exists, the recoverable amount is estimated. A previously recognised impairment loss of an asset other than goodwill is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount of that asset, but not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation) had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the income statement in the period in which it arises.

### Investments and other financial assets

*Initial recognition and measurement*

Financial assets of the Group within the scope of IAS 39 are classified as financial assets at fair value through profit or loss, loans and receivables and available-for-sale financial investments. The Group determines the classification of its financial assets at initial recognition. When financial assets are recognised initially, they are measured at fair value plus transaction costs, except in the case of financial assets recorded at fair value through profit or loss.

All regular way purchases and sales of financial assets are recognised on the trade date, that is, the date that the Group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

The Group's financial assets include cash and bank balances, trade and other receivables, loans and receivables and derivative financial instruments.

*Subsequent measurement*

The subsequent measurement of financial assets depends on their classifications as follows:

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading and financial assets designated upon initial recognition as at fair value through profit or loss. Financial assets are classified as held for trading if they are acquired for the purpose of sale in the near term. Derivatives, including separated embedded derivatives, are also classified as held for trading unless they are designated as effective hedging instruments as defined by IAS 39. Financial assets at fair value through profit or loss are carried in the statement of financial position at fair value with net changes in fair value recognised in the income statement. These net fair value changes do not include any dividends or interest earned on these financial assets, which are recognised in accordance with the polices set out for "Revenue recognition" below.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Investments and other financial assets (Continued)

*Subsequent measurement (Continued)*

Financial assets at fair value through profit or loss (Continued)

Financial assets designated upon initial recognition at fair value through profit or loss are designated at the date of initial recognition and only if the criteria under IAS 39 are satisfied.

The Group evaluates its financial assets at fair value through profit or loss (held for trading) to assess whether the intent to sell them in the near term is still appropriate. When, in rare circumstances, the Group is unable to trade these financial assets due to inactive markets and management's intent to sell them in the foreseeable future significantly changes, the Group may elect to reclassify these financial assets. The reclassification from financial assets at fair value through profit or loss to loans and receivables, available-for-sale financial assets or held-to-maturity investments depends on the nature of the assets. This evaluation does not affect any financial assets designated at fair value through profit or loss using the fair value option at designation as these instruments cannot be reclassified after initial recognition.

Derivatives embedded in host contracts are accounted for as separate derivatives and recorded at fair value if their economic characteristics and risks are not closely related to those of the host contracts and the host contracts are not held for trading or designated at fair value through profit or loss. These embedded derivatives are measured at fair value with changes in fair value recognised in the income statement. Reassessment only occurs if there is a change in the terms of the contract that significantly modifies the cash flows that would otherwise be required under the contract.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, such assets are subsequently measured at amortised cost using the effective interest rate method less any allowance for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and includes fees or costs that are an integral part of the effective interest rate. The effective interest rate amortisation is included in finance revenue in the income statement. The loss arising from impairment is recognised in the income statement in finance costs for loans and general and administrative expenses for receivables.

Available-for-sale financial investments

Available-for-sale financial investments are those non-derivative financial assets in listed and unlisted equity investments. Equity investments classified as available for sale are those which are neither classified as held for trading nor designated at fair value through profit or loss.

After initial recognition, available-for-sale financial investments are subsequently measured at fair value, with unrealised gains or losses being recognised as other comprehensive income in the available-for-sale investment revaluation reserve until the investment is derecognised, at which time the cumulative gain or loss is recognised in the income statement, or until the investment is determined to be impaired, when the cumulative gain or loss is reclassified from the available-for-sale investment revaluation reserve to the income statement. Interest and dividends earned whilst holding the available-for-sale financial investments are reported as interest income and dividend income, respectively and are recognised in the income statement in accordance with the policies set out for "Revenue recognition" below.

When the fair value of unlisted equity investments cannot be reliably measured because (a) the variability in the range of reasonable fair value estimates is significant for that investment or (b) the probabilities of the various estimates within the range cannot be reasonably assessed and used in estimating fair value, such investments are stated at cost less any impairment losses.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Investments and other financial assets (Continued)

*Subsequent measurement (Continued)*

Available-for-sale financial investments (Continued)

The Group evaluates whether the ability and intention to sell its available-for-sale financial assets in the near term are still appropriate. When, in rare circumstances, the Group is unable to trade these financial assets due to inactive markets and management's intent to do so significantly changes in the foreseeable future, the Group may elect to reclassify these financial assets. Reclassification to loans and receivables is permitted when the financial assets meet the definition of loans and receivables and the Group has the intent and ability to hold these assets for the foreseeable future or to maturity. Reclassification to the held-to-maturity category is permitted only when the Group has the ability and intent to hold until the maturity date of the financial asset.

For a financial asset reclassified from the available-for-sale category, the fair value carrying amount at the date of reclassification becomes its new amortised cost and any previous gain or loss on that asset that has been recognised in equity is amortised to profit or loss over the remaining life of the investment using the effective interest rate. Any difference between the new amortised cost and the maturity amount is also amortised over the remaining life of the asset using the effective interest rate. If the asset is subsequently determined to be impaired, then the amount recorded in equity is reclassified to the income statement.

Fair value of financial instruments

The fair value of financial instruments that are traded in active financial markets is determined by reference to quoted market prices or dealer price quotations (bid price for long positions and ask price for short positions), without any deduction for transaction costs. For financial instruments where there is no active market, the fair value is determined using appropriate valuation techniques. Such techniques include using recent arm's length market transactions, reference to the current market value of another instrument which is substantially the same, a discounted cash flow analysis and option pricing models.

### Derecognition of financial assets

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- the rights to receive cash flows from the asset have expired; or

- the Group has transferred its rights to receive cash flows from the asset or has assumed obligations to pay the received cash flows in full without material delay to a third party under a "pass-through" arrangement, and either (a) the Group has transferred substantially all the risks and rewards of the asset, or (b) the Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, it revaluates if and to what extent it has retained the risk and rewards of ownership of the assets. When it has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. In that case, the Group also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Group has retained.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Impairment of financial assets

The Group assesses at the end of each reporting period whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (an incurred "loss event") and that loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that a debtor or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and observable data indicating that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

*Financial assets carried at amortised cost*

For financial assets carried at amortised cost, the Group first assesses individually whether objective evidence of impairment exists for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it included the assets in a group of financial assets with similar credit risk characteristics and collectively assessed them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not yet been incurred). The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition). If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate.

The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. Interest income continues to be accrued on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. Loans and receivables together with any associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Group.

If, in a subsequent period, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to the income statement.

*Assets carried at cost*

If there is objective evidence that an impairment loss has been incurred on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, or on a derivative asset that is linked to and must be settled by delivery of such an unquoted equity instrument, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Impairment losses on these assets are not reversed.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Impairment of financial assets (Continued)

*Available-for-sale financial investments*

For available-for-sale financial investments, the Group assesses at the end of each reporting period whether there is objective evidence that an investment or a group of investments is impaired.

If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in the income statement, is removed from other comprehensive income and recognised in the income statement.

### Financial liabilities

*Initial recognition and measurement*

Financial liabilities of the Group within the scope of IAS 39 are classified as financial liabilities at fair value through profit or loss, or loans and borrowings. The Group determines the classification of its financial liabilities at initial recognition.

All financial liabilities are recognised initially at fair value plus, in the case of loans and borrowings, directly attributable transaction costs.

The Group's financial liabilities include trade and other payables, an amount due to the ultimate holding company, derivative financial instruments and interest-bearing loans and borrowings.

*Subsequent measurement*

The subsequent measurement of financial liabilities depends on their classification as follows:

Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss include financial liabilities held for trading and financial liabilities designated upon initial recognition as at fair value through profit or loss.

Financial liabilities are classified as held for trading if they are acquired for the purpose of sale in the near term. This category includes derivative financial instruments entered into by the Group that are not designated as hedging instruments in hedge relationships as defined by IAS 39. Separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments. Gains or losses on liabilities held for trading are recognised in the income statement. The net fair value gain or loss recognised in the income statement does not include any interest charged on these financial liabilities.

Financial liabilities designated upon initial recognition at fair value through profit or loss are designated at the date of initial recognition and only if the criteria of IAS 39 are satisfied.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Financial liabilities (Continued)

*Subsequent measurement (Continued)*

Loans and borrowings

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost, using the effective interest rate method unless the effect of discounting would be immaterial, in which case they are stated at cost. Gains and losses are recognised in the income statement when the liabilities are derecognised as well as through the effective interest rate amortisation process.

Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the effective interest rate. The effective interest rate amortisation is included in finance costs in the income statement.

Financial guarantee contracts

Financial guarantee contracts issued by the Group are those contracts that require a payment to be made to reimburse the holder for a loss it incurs because the specified debtor fails to make a payment when due in accordance with the terms of a debt instrument. Financial guarantee contracts are recognised initially as a liability at its fair value, adjusted for transaction costs that are directly attributable to the issuance of the guarantee. Subsequent to initial recognition, the Group measures the financial guarantee contract at the higher of: (i) the amount of the best estimate of the expenditure required to settle the present obligation at the end of the reporting period; and (ii) the amount initially recognised less, when appropriate, cumulative amortisation.

Derecognition of financial liabilities

A financial liability is derecognised when the obligations under the liability is discharged or cancelled, or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and a recognition of a new liability, and the difference between the respective carrying amounts is recognised in the income statement.

### Treasury shares

Own equity instruments (treasury shares) are recognised at cost and deducted from equity. No gain or loss is recognised in the income statement on the purchase, sale, issue or cancellation of the Group's own equity instruments. Any difference between the carrying amount and the consideration is recognised in equity.

### Inventories

Inventories, which consist primarily of expendable spare parts and supplies, are stated at the lower of cost and net realisable value. Cost is determined on the weighted average basis. Net realisable value is determined on the basis of anticipated sales proceeds less estimated costs to be incurred to completion and disposal.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Accounts receivable

*Individually significant and impairment provided for*

Accounts receivable that are individually significant are assessed for impairment individually.

*Collectively significant and impairment provided for*

The accounts receivable with similar credit risk characteristics, which are not individually significant but collectively significant, are collectively assessed for impairment. The percentages for the impairment are as follows:

| | **Percentages for impairment** |
|---|---|
| Receivables for sales of overseas tickets | 5% |
| Receivables for ground services | 1% |

*Individually insignificant but impairment provided for*

Accounts receivable that are individually insignificant are assessed for impairment individually when events or changes in circumstances indicate that the carrying amounts may not be collectable.

### Cash and cash equivalents

For the purpose of the consolidated statement of cash flows, cash and cash equivalents comprise cash on hand and demand deposits, and short term highly liquid investments that are readily convertible into known amounts of cash, are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired, less bank overdrafts which are repayable on demand and form an integral part of the Group's cash management.

For the purpose of the statement of financial position, cash and cash equivalents comprise cash on hand and at banks, including term deposits, and assets similar in nature to cash, which are not restricted as to use.

### Manufacturers' credits

In connection with the acquisition of certain aircraft and flight equipment, the Group receives various credits from the manufacturers. Such credits are deferred until the aircraft and flight equipment are delivered, at which time they are applied as a reduction of the cost of acquiring the aircraft and flight equipment.

### Provisions

A provision is recognised when the Group has a present obligation (legal or constructive) as a result of a past event and it is probable that an future outflow of resources will be required to settle the obligations and a reliable estimate can be made of the amount of the obligations. When the effect of discounting is material, the amount recognised for a provision is the present value at the end of the reporting period of the future expenditures expects to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in the income statement.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Employee benefits

(a) *Pension obligations*

The full-time employees of the Group are covered by various government-sponsored pension plans under which the employees are entitled to a monthly pension based on certain formulae. Certain government agencies are responsible for the pension liability to these retired employees. The Group contributes on a monthly basis to these pension plans. Under these plans, the Group has no legal or constructive obligations for retirement benefits beyond the contributions made. Contributions to these plans are expensed as incurred. In addition to these plans, the Company, Air China Cargo Co., Ltd. ("Air China Cargo"), Beijing Airlines, Shenzhen Airlines Co., Ltd ("Shenzhen Airlines") and so on also implements an additional defined contribution retirement scheme for voluntary employees. Contributions are made based on a percentage of the employees' total salaries and are charged to the income statement in accordance with the rules of the scheme.

(b) *Termination and early retirement benefits*

Termination benefits are payable whenever an employee's employment is voluntarily terminated before the normal retirement date or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Group recognises termination benefits when it is demonstrably committed to either terminating the employment of current employees according to a detailed formal plan without possibility of withdrawal or to providing termination benefits as a result of an offer made to encourage voluntary redundancy.

(c) *Housing benefits*

All full-time employees of the Group are entitled to participate in various government-sponsored housing funds. The Group contributes on a monthly basis to these funds based on certain percentages of the salaries of the employees. The Group's liability in respect of these funds is limited to the contributions payable in each year.

(d) *Share-based payment transactions*

The Company operates a Share Appropriation Rights ("SARs") plan for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. Employees (including Directors) of the Group are entitled to a future cash payment (rather than an equity instrument) ("cash-settled transactions"), based on the increase in the entity's share price from a specified level over a specified period of time. The Company recognises the services received, and a liability to pay for those services, as the employees render service.

The cost of cash-settled transactions with employees is measured initially at fair value at the grant date using a binomial model. The liability is remeasured at each reporting date up to and including the settlement date, with any changes in fair value recognised in profit or loss for the period.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Maintenance and overhaul costs

In respect of aircraft and engines under operating leases, the Group has the responsibility to fulfil certain return conditions under the relevant operating leases. In order to fulfil these return conditions, major overhauls are required to be conducted on a regular basis. Accordingly, estimated costs of major overhauls for aircraft and engines under operating leases are accrued and charged to the income statement over the estimated period between overhauls using the ratios of actual flying hours/cycles and estimated flying hours/cycles between overhauls. The costs of major overhauls comprise mainly labour and materials. Differences between the estimated costs and the actual costs of overhauls are included in the income statement in the period of overhaul.

In respect of aircraft and engines owned by the Group or held under finance leases, costs of major overhauls are recognised in the carrying amount of the property, plant and equipment as a replacement if the recognition criteria are satisfied. Overhaul components subject to replacement during major overhauls are depreciated over the expected life between major overhauls.

All other routine repair and maintenance costs incurred in restoring such property, plant and equipment to their normal working condition are charged to the income statement as and when incurred.

### Frequent-flyer programmes

The Group operates frequent-flyer programmes which allow customers to earn miles when they purchase air tickets from the Group. The miles can then be redeemed for free services or products, subject to a minimum number of points to be obtained. The consideration received or receivable from the tickets sold is allocated between the miles earned by the frequent-flyer programme members and the other components of the sales transactions. The fair value allocated to the miles earned by the frequent-flyer programme members is deferred until the miles are redeemed when the Group fulfil its obligations to supply services or products or when the miles expire.

### Revenue recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

*(a) Provision of airline and airline-related services*

Passenger revenue is recognised either when transportation services are provided or when an unused ticket expires rather than when a ticket is sold. Ticket sales for transportation not yet provided are included in current liabilities as air traffic liabilities. In addition, the Group has code-sharing agreements with other airlines under which a carrier's flights can be marketed under the two-letter airline designator code of another carrier. Revenues earned under these arrangements are allocated between the code share partners based on existing contractual agreements and airline industry standard pro-ratio formulae and are recognised as passenger revenue when the transportation services are provided.

Cargo and mail revenue is recognised when transportation services are provided.

Revenue from airline-related services is recognised when the relevant services are rendered.

Revenue is stated net of business tax.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Revenue recognition (Continued)

(b) *Sale of goods*

Revenue is recognised when the significant risks and rewards of ownership of the goods have been passed to the buyer.

(c) *Interest income*

Revenue is recognised on a time proportion basis taking into account the principal outstanding and the effective rate of interest applicable.

(d) *Dividend income*

Revenue is recognised when the Group's right to receive payments is established.

(e) *Rental income and aircraft and flight equipment lease income*

Revenue is recognised on a time proportion basis over the terms of the respective leases.

### Government grants

Government grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. When the grant relates to an expense item, it is recognised as income over the periods necessary to match the grant on a systematic basis to the costs that it is intended to compensate.

Where the grant relates to an asset, the fair value is credited to a deferred income account and is released to the income statement over the expected useful life of the relevant asset by equal annual instalments or deducted from the carrying amount of the asset and released to the income statement by way of a reduced depreciation charge.

Where the Group receives a non-monetary grant, the asset and the grant are recorded at the fair value of the non-monetary asset and released to the income statement over the expected useful life of the relevant asset by equal annual instalments.

### Income tax

Income tax comprises current and deferred tax. Income tax relating to items recognised outside profit or loss is recognised outside profit or loss, either in other comprehensive income or directly in equity.

*Current tax*

Current tax assets and liabilities for the current and prior periods are measured at the amounts expected to be recovered from or paid to the taxation authorities, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period, taking into consideration interpretations and practices prevailing in the countries in which the Group operates. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the end of the reporting period.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Income tax (Continued)

*Deferred tax*

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

Deferred tax liabilities are recognised for all taxable temporary differences, except:

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

- in respect of taxable temporary differences associated with investments in subsidiaries, associates and joint ventures, when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

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

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

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

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are reassessed at the end of each reporting period and are recognised to the extent that it has become probable that sufficient taxable profit will be available to allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Borrowing costs

Borrowing costs directly attributable to the acquisition of aircraft, construction or production of qualifying assets, that is, assets that necessarily take a substantial period of time to get ready for their intended use or sale, are capitalised as part of the costs of those assets. The capitalisation of aircraft borrowing costs ceases when the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs capitalised. All other borrowing costs are expensed in the period in which they are incurred. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

Where funds have been borrowed generally, and used for the purpose of obtaining qualifying assets, a capitalisation rate ranging between 1.24% and 8.23% (2010: ranging between 0.80% and 7.13%) has been applied to the expenditure on the individual asset.

### Dividends

Interim dividends and final dividends proposed by the Directors are classified as a separate allocation of retained earnings within the equity section of the statement of financial position, until they have been approved by the shareholders in a general meeting. When these dividends have been approved by the shareholders and declared, they are recognised as a liability.

### Significant accounting judgements and estimates

The preparation of the Group's financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts of revenue, expenses, assets and liabilities, and the disclosure of contingent liabilities, at the end of the reporting period. However, uncertainty about these assumptions and estimates could result in outcomes that could require a material adjustment to the carrying amounts of the assets or liabilities affected in the future.

### Judgements

In the process of applying the Group's accounting policies, management has made judgements regarding revenue recognition, classification of leases, classification of financial instruments, impairment indication of financial assets, classification of assets held for sale, derecognition of financial instruments, which have the most significant effect on the amounts recognised in the financial statements.

### Estimation uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below.

(a) *Impairment of goodwill*

The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the value in use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating units and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of goodwill at 31 December 2011 was RMB1,311 million (2010: RMB1,658 million). More details are given in note 19 to the financial statements.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Estimation uncertainty (Continued)

(b) *Impairment of non-financial assets (other than goodwill)*

The Group assesses whether there are any indicators of impairment for all non-financial assets at the end of each reporting period. Indefinite life intangible assets are tested for impairment annually and at other times when such indicator exists. Other non-financial assets are tested for impairment when there are indicators that the carrying amounts may not be recoverable. An impairment exists when the carrying value of an asset or a cash-generating unit exceeds its recoverable amount, which is the higher of its fair value less costs to sell and its value in use. The calculation of the fair value less costs to sell is based on available data from binding sales transactions in an arm's length transaction of similar assets or observable market prices less incremental costs for disposal of the asset. When value in use calculations are undertaken, management must estimate the expected future cash flows from the asset or cash-generating unit and choose a suitable discount rate in order to calculate the present value of those cash flows.

(c) *Deferred tax assets*

Deferred tax assets are recognised for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgement is required to estimate the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits together with future tax planning strategies.

(d) *Overhaul cost*

Cost of overhaul for aircraft and engines under operating leases are accrued and charged to the income statement over the estimated overhaul period. This requires estimation of the expected flying hours/cycles, overhaul cost and overhaul cycle, which are largely based on the past experience of overhauls of aircraft and engines of the same or similar types. Different estimates could significantly affect the estimated overhaul provision and the results of operations.

(e) *Deferred income*

The amount of revenue attributable to the miles earned by the members of the Group's frequent-flyer programme is estimated based on the fair value of the miles awarded and the expected redemption rate. The fair value of the miles awarded is estimated by reference to external sales. The expected redemption rate was estimated considering the number of the miles that will be available for redemption in the future after allowing for miles which are not expected to be redeemed.

(f) *Early retirement benefits*

Early retirement benefits are incurred and charged to the income statement when the conditions for early retirement are realised. The estimated liabilities were affected by the uncertainty of the changes in salary standards, life expectancy of early retired employees and discount rate.

(g) *Fair value of financial instruments*

Where the fair value of financial assets and financial liabilities recorded in the statement of financial position cannot be derived directly from active markets, they are determined using valuation techniques. The inputs to these models are taken from observable markets where possible, but where this is not feasible, estimation is required in establishing fair values. The estimation includes considerations of inputs such as liquidity risk, credit risk and volatility. Changes in assumptions about these factors could affect the reported fair value of financial instruments.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Estimation uncertainty (Continued)

*(h) Share-based payments*

The Group measures the cost of cash-settled transactions with employees by reference to the instruments at the date at which they are granted. Estimating fair value for share-based payments requires determining the most appropriate valuation model for a grant of instruments, which is dependent on the terms and conditions of the grant. This also requires determining the most appropriate inputs to the valuation model and making assumptions about them.

### Changes in accounting estimation

In order to improve the quality of services, the Company decided to implement a cabin refurbishment plan. The cabin refurbishment involving replacement of cabin facilities are recognized in the carrying amount of the property, plant and equipment and depreciated over the cabin refurbishment cycle if the recognition criteria are satisfied. Otherwise, the replacement costs are included in the income statement in the period of refurbishment. Accordingly, the accounting estimation is changed in regard to the useful life and residue value of the cabin facilities, which satisfy the capitalisation criteria. Such cabin facilities were previously included in the core part of airframe and depreciated over 20 years with a 5% residue value. After the changes, the cabin refurbishment costs are depreciated over the cabin refurbishment cycle with the residue value as nil. The changes of accounting estimate are prospectively applied in October, 2011.

The effect of the above mentioned changes is summarised as follows:

**Group**

| 2011 | Before changes Ending balance/ Current year *RMB'000* | Changes in accounting estimation Depreciation rate *RMB'000* | After changes Ending balance/ Current year *RMB'000* |
|---|---|---|---|
| Property, plant and equipment | 112,526,441 | (127,010) | 112,399,431 |
| Tax payable | 1,739,305 | (31,752) | 1,707,553 |
| Reserves | 36,208,501 | (95,258) | 36,113,243 |
| Depreciation | 9,433,897 | 127,010 | 9,560,907 |
| Tax | 2,323,825 | (31,752) | 2,292,073 |

**Company**

| 2011 | Before changes Ending balance/ Current year *RMB'000* | Changes in accounting estimation Depreciation rate *RMB'000* | After changes Ending balance/ Current year *RMB'000* |
|---|---|---|---|
| Property, plant and equipment | 80,477,841 | (127,010) | 80,350,831 |
| Tax payable | 1,254,964 | (31,752) | 1,223,212 |
| Reserves | 30,357,971 | (95,258) | 30,262,713 |
| Depreciation | 7,170,955 | 127,010 | 7,297,965 |
| Tax | 1,733,247 | (31,752) | 1,701,495 |

## 3 OPERATING 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 "other operations" segment which comprises the provision of aircraft engineering, ground services and other airline-related services.

In determining the Group's geographical information, revenue is attributed to the segments based on the origin and destination of each flight. Assets, which consist principally of aircraft and ground 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.

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 regarding the Group's operating segments in accordance with China Accounting Standards for Business Enterprises (the "CASs") for the years ended 31 December 2011 and 2010 and the reconciliations of reportable segment revenue and profit before tax to the Group's consolidated amounts under IFRSs:

**Year ended 31 December 2011**

| | Airline operations *RMB'000* | Other operations *RMB'000* | Eliminations *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|
| **REVENUE** | | | | |
| Sales to external customers | 96,998,433 | 140,678 | – | 97,139,111 |
| Intersegment sales | – | 1,215,116 | (1,215,116) | – |
| Total revenue for reportable segments under CASs | 96,998,433 | 1,355,794 | (1,215,116) | 97,139,111 |
| Business tax not included in segment revenue | | | | (2,267,856) |
| Other income not included in segment revenue | | | | 1,498,578 |
| Effects of differences between IFRSs and CASs | | | | 2,039,669 |
| Revenue for the year under IFRSs | | | | 98,409,502 |
| **SEGMENT PROFIT BEFORE TAX** | | | | |
| Profit before tax for reportable segments under CASs | 10,028,990 | 92,529 | – | 10,121,519 |
| Effects of differences between IFRSs and CASs | | | | (766,780) |
| Profit before tax for the year under IFRSs | | | | 9,354,739 |

## 3 OPERATING SEGMENT INFORMATION (Continued)

### Operating segments (Continued)

Year ended 31 December 2010

| | Airline operations *RMB'000* | Other operations *RMB'000* | Eliminations *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|
| **REVENUE** | | | | |
| Sales to external customers | 80,927,043 | 35,634 | – | 80,962,677 |
| Intersegment sales | – | 935,326 | (935,326) | – |
| Total revenue for reportable segments under CASs | 80,927,043 | 970,960 | (935,326) | 80,962,677 |
| Business tax not included in segment revenue | | | | (1,628,290) |
| Other income not included in segment revenue | | | | 1,232,350 |
| Effects of differences between IFRSs and CASs | | | | 1,920,802 |
| Revenue for the year under IFRSs | | | | 82,487,539 |
| **SEGMENT PROFIT BEFORE TAX** | | | | |
| Profit before tax for reportable segments under CASs | 14,858,562 | 166,500 | – | 15,025,062 |
| Effects of differences between IFRSs and CASs | | | | (191,450) |
| Profit before tax for the year under IFRSs | | | | 14,833,612 |

## 3 OPERATING SEGMENT INFORMATION (Continued)

### Operating segments (Continued)

The following tables present the segment assets, liabilities and other information of the Group's operating segments under CASs as at 31 December 2011 and 31 December 2010 and the reconciliations of reportable segment assets, liabilities and other information to the Group's consolidated amounts under IFRSs:

| | Airline operations *RMB'000* | Other operations *RMB'000* | Eliminations *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|
| **SEGMENT ASSETS** | | | | |
| Total assets for reportable segments as at 31 December 2011 under CASs | **172,951,576** | **4,961,357** | **(4,589,365)** | **173,323,568** |
| Effects of differences between IFRSs and CASs | | | | **2,526,504** |
| Total assets under IFRSs | | | | **175,850,072** |
| Total assets for reportable segments as at 31 December 2010 under CASs | 153,816,518 | 2,968,976 | (1,565,881) | 155,219,613 |
| Effects of differences between IFRSs and CASs | | | | 3,549,918 |
| Total assets under IFRSs | | | | 158,769,531 |

| | Airline operations *RMB'000* | Other operations *RMB'000* | Eliminations *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|
| **SEGMENT LIABILITIES** | | | | |
| Total liabilities for reportable segments as at 31 December 2011 under CASs | **127,360,960** | **1,050,452** | **(4,589,365)** | **123,822,047** |
| Effects of differences between IFRSs and CASs | | | | **3,702,590** |
| Total liabilities under IFRSs | | | | **127,524,637** |
| Total liabilities for reportable segments as at 31 December 2010 under CASs | 114,166,219 | 919,955 | (1,565,881) | 113,520,293 |
| Effects of differences between IFRSs and CASs | | | | 3,878,001 |
| Total liabilities under IFRSs | | | | 117,398,294 |

## 3 OPERATING SEGMENT INFORMATION (Continued)

### Operating segments (Continued)

| | Airline operations RMB'000 | Other operations RMB'000 | Eliminations RMB'000 | Total RMB'000 | Effects of differences between IFRSs and CASs RMB'000 | Amounts under IFRSs RMB'000 |
|---|---|---|---|---|---|---|
| **OTHER SEGMENT INFORMATION** | | | | | | |
| **Year ended 31 December 2011** | | | | | | |
| Share of profits and losses of associates | 1,288,914 | 39,884 | – | 1,328,798 | – | 1,328,798 |
| Impairment losses recognised in the income statement | 1,969,970 | 176,846 | – | 2,146,816 | 708,095 | 2,854,911 |
| Finance revenue | 3,273,134 | 27,391 | – | 3,300,525 | 60,770 | 3,361,295 |
| Finance costs | 1,436,334 | 296 | – | 1,436,630 | 157,385 | 1,594,015 |
| Tax | 2,196,417 | 27,493 | – | 2,223,910 | 68,163 | 2,292,073 |
| Interests in associates | 13,060,493 | 314,730 | – | 13,375,223 | 21,808 | 13,397,031 |
| Capital expenditure | 30,092,582 | 8,488 | – | 30,101,070 | 457,554 | 30,558,624 |
| Depreciation and amortisation | 9,509,045 | 8,963 | – | 9,518,008 | 96,146 | 9,614,154 |

| | Airline operations RMB'000 | Other operations RMB'000 | Eliminations RMB'000 | Total RMB'000 | Effects of differences between IFRSs and CASs RMB'000 | Amounts under IFRSs RMB'000 |
|---|---|---|---|---|---|---|
| Year ended 31 December 2010 | | | | | | |
| Share of profits and losses of associates | 3,324,164 | 51,161 | – | 3,375,325 | – | 3,375,325 |
| Impairment losses recognised in the income statement | 2,098,127 | 129 | – | 2,098,256 | 314,741 | 2,412,997 |
| Finance revenue | 1,942,202 | 12,394 | – | 1,954,596 | 25,419 | 1,980,015 |
| Finance costs | 1,413,283 | 1,788 | – | 1,415,071 | 34,178 | 1,449,249 |
| Tax | 2,554,237 | 16,067 | – | 2,570,304 | (72,556) | 2,497,748 |
| Interests in associates | 13,803,512 | 328,590 | – | 14,132,102 | 56,324 | 14,188,426 |
| Capital expenditure | 17,371,014 | 5,410 | – | 17,376,424 | 41,686 | 17,418,110 |
| Depreciation and amortisation | 8,568,096 | 6,608 | – | 8,574,704 | 81,705 | 8,656,409 |

## 3 OPERATING SEGMENT INFORMATION (Continued)

### Geographical information

The following table presents the geographical information of the Group's consolidated revenue under IFRSs for the years ended 31 December 2011 and 2010:

**Year ended 31 December 2011**

| | 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 |
|---|---|---|---|---|---|---|---|
| Sales to external customers and total revenue | 66,154,716 | 4,335,880 | 10,464,556 | 6,984,158 | 6,110,530 | 4,359,662 | 98,409,502 |

Year ended 31 December 2010

| | 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 |
|---|---|---|---|---|---|---|---|
| Sales to external customers and total revenue | 52,441,112 | 4,212,616 | 9,848,721 | 6,008,965 | 5,818,381 | 4,157,744 | 82,487,539 |

### Information about a major customer

There was no revenue from transactions with a single customer amounting to 10% or more of the Group's revenue during the year (2010: Nil).

## 4 AIR TRAFFIC REVENUE

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

| | 2011 RMB'000 | 2010 RMB'000 |
|---|---|---|
| Passenger | 83,510,323 | 68,137,672 |
| Cargo and mail | 9,833,098 | 10,071,516 |
| | 93,343,421 | 78,209,188 |

Air traffic revenue for all domestic flights were subject to a business tax rate of 3%. Pursuant to the relevant business tax rules and regulations in Mainland China, all international, Hong Kong, Macau and Taiwan regional flights are exempted from business tax with effect from 1 January 2010. Business tax incurred and set off against air traffic revenue for the year ended 31 December 2011 amounted to approximately RMB2,128 million (2010: RMB1,544 million).

## 5 OTHER OPERATING REVENUE

| | 2011 RMB'000 | 2010 RMB'000 |
|---|---|---|
| Aircraft engineering income | **730,746** | 639,194 |
| Ground service income | **724,346** | 681,883 |
| Service charges on return of unused flight tickets | **574,136** | 417,130 |
| Income from other travelling services | **535,482** | 439,219 |
| Government grants and subsidies: | | |
| Recognition of deferred income *(note 41(b))* | **240,486** | 83,277 |
| Others | **938,120** | 702,995 |
| Gain on disposal of property, plant and equipment, net | **252,662** | 159,011 |
| Cargo handling service income | **167,934** | 164,407 |
| Revaluation gain on acquisition of a subsidiary | **–** | 150,628 |
| Rental income: | | |
| Aircraft and flight equipment | **44,802** | 76,342 |
| Others | **42,489** | 45,382 |
| Training service income | **81,051** | 63,852 |
| Sale of materials | **24,966** | 21,953 |
| Import and export service income | **16,400** | 16,427 |
| Others | **692,461** | 616,651 |
| | **5,066,081** | 4,278,351 |

## 6 EMPLOYEE COMPENSATION COSTS

An analysis of the Group's employee compensation costs, including the emoluments of Directors and supervisors, is as follows:

| | 2011 RMB'000 | 2010 RMB'000 |
|---|---|---|
| Wages, salaries and social security costs | **11,002,334** | 9,046,461 |
| Retirement benefit costs *(note 10)* | **1,274,561** | 795,233 |
| Share-based benefits *(note 45)* | **(6,830)** | 10,241 |
| | **12,270,065** | 9,851,935 |

## 7 PROFIT FROM OPERATIONS

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

| | **2011** | 2010 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Auditors' remuneration | **18,370** | 13,051 |
| Depreciation *(note 15)* | **9,560,907** | 8,569,370 |
| Impairment of property, plant and equipment *(note 15)* | **2,237,403** | 1,863,194 |
| Gain on disposal of property, plant and equipment, net | **252,662** | 159,011 |
| Losses on derecognition of property, plant and equipment | **31,345** | 55,434 |
| Amortisation of lease prepayments *(note 16)* | **53,247** | 87,039 |
| Minimum lease payments under operating leases: | | |
| Aircraft and flight equipment | **3,931,549** | 3,483,180 |
| Land and buildings | **583,338** | 600,296 |
| Impairment of aircraft and flight equipment held for sale *(note 26)* | **99,669** | 185,992 |
| Impairment of goodwill *(note 19)* | **176,891** | – |
| Impairment of interests in associates | **19,810** | – |
| Impairment of inventories | **77,785** | 236,219 |
| Impairment of accounts receivable *(note 28)* | **3,771** | 8,983 |
| Impairment of prepayments, deposits and other receivables *(note 29)* | **239,582** | 118,609 |

## 8 FINANCE REVENUE AND FINANCE COSTS

An analysis of the Group's finance revenue and finance costs during the year is as follows:

### Finance revenue

| | **2011** | 2010 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Exchange gains, net | **3,117,700** | 1,919,415 |
| Interest income | **240,234** | 60,307 |
| others | **3,361** | 293 |
| | **3,361,295** | 1,980,015 |

## 8 FINANCE REVENUE AND FINANCE COSTS (Continued)

### Finance costs

| | 2011 RMB'000 | 2010 RMB'000 |
|---|---|---|
| Interest on interest-bearing bank loans and other borrowings | 1,869,764 | 1,497,429 |
| Interest on finance leases | 326,771 | 110,903 |
| Loss on interest rate derivative contracts and forward foreign exchange contracts, net | 41,122 | 206,707 |
| | 2,237,657 | 1,815,039 |
| Less: Interest capitalised | (643,642) | (365,790) |
| | 1,594,015 | 1,449,249 |

The interest capitalisation rates range from 1.24% to 8.23% (2010: 0.80% to 7.13%) per annum relating to the costs of related borrowings during the year.

## 9 REMUNERATION OF DIRECTORS, SUPERVISORS AND FIVE HIGHEST PAID EMPLOYEES

Remuneration of the Company's Directors and supervisors for the year disclosed pursuant to the Rules Governing the Listing of Securities on the Hong Kong Stock Exchange and Section 161 of the Hong Kong Companies Ordinance is as follows:

| | Group | |
|---|---|---|
| | 2011 RMB'000 | 2010 RMB'000 |
| Fees | 322 | 240 |
| Basic salaries, housing benefits, other allowances and benefits in kind | 908 | 1,025 |
| Discretionary bonuses | 1,300 | 1,139 |
| Retirement benefits | 193 | 113 |
| Share appreciation rights | 947 | – |
| | 3,670 | 2,517 |

## 9 REMUNERATION OF DIRECTORS, SUPERVISORS AND FIVE HIGHEST PAID EMPLOYEES (Continued)

| | Fees RMB'000 | Basic salaries, housing benefits, other allowances and benefits in kind RMB'000 | Discretionary bonuses RMB'000 | Retirement benefits RMB'000 | SARs[4] RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|
| **Year ended 31 December 2011** | | | | | | |
| **Directors** | | | | | | |
| Kong Dong | – | – | – | – | 341 | 341 |
| Wang Yinxiang | – | – | – | – | – | – |
| Sun Yude | – | – | – | – | – | – |
| Cao Jianxiong | – | – | – | – | – | – |
| Christopher Dale Pratt | – | – | – | – | – | – |
| Ian Sai Cheung Shiu | – | – | – | – | – | – |
| Cai Jianjiang | – | 278 | 591 | 67 | 322 | 1,258 |
| Fan Cheng | – | 274 | 553 | 62 | 284 | 1,173 |
| Li Shuang | 84 | – | – | – | – | 84 |
| Fu Yang | 84 | – | – | – | – | 84 |
| Han Fangming | 84 | – | – | – | – | 84 |
| Yang Yuzhong[1] | 60 | – | – | – | – | 60 |
| Jia Kang[1] | 10 | – | – | – | – | 10 |
| | 322 | 552 | 1,144 | 129 | 947 | 3,094 |
| **Supervisors** | | | | | | |
| He Chaofan[3] | – | – | – | – | – | – |
| Zhou Feng[3] | – | – | – | – | – | – |
| Chen Bangmao[2] | – | – | – | – | – | – |
| Xiao Yanjun[2] | – | 146 | 65 | 24 | – | 235 |
| Su Zhiyong | – | 210 | 91 | 40 | – | 341 |
| Li Qinglin | – | – | – | – | – | – |
| Zhang Xueren | – | – | – | – | – | – |
| | – | 356 | 156 | 64 | – | 576 |
| | 322 | 908 | 1,300 | 193 | 947 | 3,670 |

Fees of RMB322,000 were paid or payable to the Company's Independent Non-executive directors during the year. There were no other emoluments payable to the Independent Non-executive directors during the year.

(1) On 26 May 2011, Jia Kang resigned as Directors of the Company. On the same date, Yang Yuzhong was appointed as Directors of the Company to fill the vacancy.

(2) On 16 June 2011, Chen Bangmao resigned as supervisors of the Company. On the same date, Xiao Yanjun was appointed as supervisors of the Company to fill the vacancy.

(3) On 25 November 2011, He Chaofan resigned as supervisors of the Company. On the same date, Zhou Feng was appointed as supervisors of the Company to fill the vacancy.

(4) Up to 31 December 2011, 70% of SARs were vested and the amount represents the total vested part.

## 9 REMUNERATION OF DIRECTORS, SUPERVISORS AND FIVE HIGHEST PAID EMPLOYEES (Continued)

| | Fees<br>*RMB'000* | Basic salaries, housing benefits, other allowances and benefits in kind<br>*RMB'000* | Discretionary bonuses<br>*RMB'000* | Retirement benefits<br>*RMB'000* | Total<br>*RMB'000* |
|---|---|---|---|---|---|
| Year ended 31 December 2010 | | | | | |
| **Directors** | | | | | |
| Kong Dong | – | – | – | – | – |
| Wang Yinxiang(2) | – | – | – | – | – |
| Sun Yude(2) | – | – | – | – | – |
| Wang Shixiang | – | – | – | – | – |
| Cao Jianxiong | – | – | – | – | – |
| Christopher Dale Pratt | – | – | – | – | – |
| Chen Nan Lok Philip(2) | – | – | – | – | – |
| Ian Sai Cheung Shiu(2) | – | – | – | – | – |
| Cai Jianjiang | – | 275 | 492 | 29 | 796 |
| Fan Cheng | – | 252 | 431 | 29 | 712 |
| Hu Hung Lick, Henry(1) | 50 | – | – | – | 50 |
| Zhang Ke(1) | 50 | – | – | – | 50 |
| Jia Kang | 60 | – | – | – | 60 |
| Fu Yang | 60 | – | – | – | 60 |
| Li Shuang(1) | 10 | – | – | – | 10 |
| Han Fangming(1) | 10 | – | – | – | 10 |
| | 240 | 527 | 923 | 58 | 1,748 |
| **Supervisors** | | | | | |
| Sun Yude(3) | – | – | – | – | – |
| He Chaofan | – | – | – | – | – |
| Zhou Guoyou(3) | – | – | – | – | – |
| Chen Bangmao | – | 302 | 135 | 26 | 463 |
| Su Zhiyong | – | 196 | 81 | 29 | 306 |
| Li Qinglin(3) | – | – | – | – | – |
| Zhang Xueren(3) | – | – | – | – | – |
| | – | 498 | 216 | 55 | 769 |
| | 240 | 1,025 | 1,139 | 113 | 2,517 |

Fees of RMB240,000 were paid or payable to the Company's Independent Non-executive directors during the year. There were no other emoluments payable to the Independent Non-executive directors during the year.

(1) On 28 October 2010, Hu Hung Lick, Henry and Zhang Ke resigned as Directors of the Company. On the same date, Li Shuang and Han Fangming were appointed as Directors of the Company to fill the vacancy.

(2) On 1 July 2010 and 28 October 2010, respectively, Chen Nan Lok, Philip and Wang Shixiang resigned as Directors of the Company. On 28 October 2010, Sun Yude and Ian Sai Cheung Shiu were appointed as Directors of the Company to fill the vacancy.

(3) On 28 October 2010, Sun Yude and Zhou Guoyou resigned as supervisors of the Company. On the same date, Li Qinglin and Zhang Xueren were appointed as supervisors of the Company to fill the vacancy.

## 9 REMUNERATION OF DIRECTORS, SUPERVISORS AND FIVE HIGHEST PAID EMPLOYEES (Continued)

An analysis of the five highest paid employees within the Group is as follows:

| | Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***Number of individuals*** | *Number of individuals* |
| Directors | **2** | – |
| Employees | **3** | 5 |

The five highest paid employees during the year included two (2010: Nil) Directors, details of whose remuneration are set out above. Details of the remuneration of the remaining three (2010: Five) non-directors, highest paid employees for the year are as follows:

| | Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Basic salaries, housing benefits, other allowances and benefits in kind | **4,569** | 5,404 |
| Retirement benefits | **52** | 86 |
| | **4,621** | 5,490 |

The number of these three (2010: five) non-director and non-supervisor highest paid employees whose remuneration for the year fell within the following bands is as follows:

| | Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***Number of individuals*** | *Number of individuals* |
| HK$1,000,001 to HK$1,500,000 (equivalent to 2011: RMB810,700 to RMB1,216,050) (2010: RMB850,930 to RMB1,276,395) | **–** | 5 |
| HK$1,500,001 to HK$2,000,000 (equivalent to 2011: RMB1,216,051 to RMB1,621,400) (2010: RMB1,276,396 to RMB1,701,860) | **2** | – |
| HK$2,000,001 to HK$2,500,000 (equivalent to 2011: RMB1,621,401 to RMB2,026,750) (2010: RMB1,701,861 to RMB2,127,325) | **1** | – |
| | **3** | 5 |

There was no arrangement under which a Director or a Supervisor waived or agreed to waive any remuneration during the year (2010: Nil).

## 10 RETIREMENT BENEFIT COSTS

The retirement benefit costs in relation to the defined contribution retirement scheme and early retirement benefits are as follows:

| | Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Contributions to defined contribution retirement scheme | **1,255,198** | 764,882 |
| Early retirement benefits | **19,363** | 30,351 |
| Total retirement benefit costs *(note 6)* | **1,274,561** | 795,233 |

As at 31 December 2011, no forfeited contributions were available to reduce the Group's contributions to the defined contribution retirement scheme operated by the Group in future years (2010: Nil).

## 11 TAX

Under the relevant Corporate Income Tax Law and regulations in the PRC, except for a subsidiary which is taxed at the preferential rate of 24% (2010: 22%) and two joint ventures which are taxed at the preferential rates from 12.5% to 15% (2010: 12.5% to 22%), all group companies located in Mainland China are subject to a corporate income tax rate of 25% (2010: 25%). Subsidiaries in Hong Kong and Macau are taxed at the profits tax rate of 16.5% (2010:16.5%) and 12% (2010: 12%), respectively.

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

| | Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Current income tax: | | |
| Mainland China | **2,968,108** | 2,506,846 |
| Hong Kong and Macau | **1,662** | 1,197 |
| | **2,969,770** | 2,508,043 |
| Deferred income tax *(note 25)* | **(677,697)** | (10,295) |
| Income tax charge for the year | **2,292,073** | 2,497,748 |

## 11 TAX (Continued)

The Group's share of tax charge attributable to associates amounting to RMB280,541,000 (2010: RMB548,527,000) is included in the "Share of profits and losses of associates" on the face of the consolidated income statement.

A reconciliation of the tax expense applicable to profit before tax at the statutory rate for Mainland China in which the Company and the majority of its subsidiaries and joint ventures are domiciled to the tax expense at the effective tax rate, and a reconciliation of the statutory tax rate to the effective tax rate, are as follows:

| | Group | | | |
|---|---|---|---|---|
| | **2011** | | 2010 | |
| | ***RMB'000*** | **%** | *RMB'000* | % |
| Profit before tax | **9,354,739** | | 14,833,612 | |
| Tax at the statutory tax rate | **2,338,685** | **25.0** | 3,708,403 | 25.0 |
| Tax effect of share of profits and losses of associates | **(332,199)** | **(3.5)** | (843,832) | (5.7) |
| Lower income tax rates enacted by other territories | **(93,621)** | **(1.0)** | (74,783) | (0.5) |
| Adjustment in respect of current income tax of previous periods | **(98,922)** | **(1.1)** | (55,249) | (0.4) |
| Income not subject to tax | **(39,958)** | **(0.4)** | (33,208) | (0.2) |
| Expenses not deductible for tax | **53,425** | **0.6** | 25,222 | 0.2 |
| Utilisation of tax losses not recognised in prior years | **(24,819)** | **(0.3)** | (21,669) | (0.1) |
| Deductible temporary differences and tax losses not recognised | **489,482** | **5.2** | – | – |
| Utilisation of deductible temporary differences not recognised in prior years | **–** | **–** | (169,479) | (1.2) |
| Revaluation gain on acquisition of a subsidiary | **–** | **–** | (37,657) | (0.3) |
| At the Group's effective income tax rate | **2,292,073** | **24.5** | 2,497,748 | 16.8 |

As at 31 December 2011, there was unrecognised deferred tax liability of RMB37,657,000 (2010: RMB37,657,000) for taxes that would be payable on the disposal of a subsidiary as the Directors are of the view that the Company is able to control the timing of the disposal and they have no intention to dispose of this subsidiary in the foreseeable future.

There are no income tax consequences attaching to the payment of dividends by the Company to its shareholders.

## 12 PROFIT ATTRIBUTABLE TO OWNERS OF THE PARENT

The consolidated profit attributable to owners of the parent for the year ended 31 December 2011 includes a profit of approximately RMB5,798 million (2010: RMB7,352 million), which was arrived at after deducting dividend income received from subsidiaries, joint ventures and associates aggregating approximately RMB725 million (2010: RMB60 million) from the Company's total comprehensive income of approximately RMB6,523 million (2010: RMB7,412 million), that has been dealt with in the financial statements of the Company (note 44).

## 13 APPROPRIATIONS

| | Company | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Proposed final dividend | **1,521,251** | 1,523,829 |

Under the PRC Company Law and the Company's articles of association, profit after tax as reported in the PRC statutory financial statements can only be distributed as dividends after allowances have been made for the following:

(i) making up prior years' cumulative losses, if any;

(ii) allocations to the statutory common reserve fund of at least 10% of after-tax profit, until the fund aggregates 50% of the Company's registered capital (for the purpose of calculating transfers to reserves, profit after tax would be the amount determined under CASs. The transfers to reserves should be made before any distribution of dividends to shareholders. The statutory common reserve fund can be used to offset previous years' losses, if any, and part of the statutory common reserve fund can be capitalised as the Company's share capital provided that the amount of such reserve remaining after the capitalisation shall not be less than 25% of the share capital of the Company); and

(iii) allocations to the discretionary common reserve if approved by the shareholders.

The above reserves cannot be used for purposes other than those for which they are created and are not distributable as cash dividends.

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 CASs; and (ii) the profit determined in accordance with IFRSs.

## 14 EARNINGS PER SHARE ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT

The calculation of basic earnings per share for the year ended 31 December 2011 was based on the profit attributable to equity holders of the Company for the year ended 31 December 2011 of approximately RMB7,082 million and the weighted average of 12,161,502,125 ordinary shares in issue during the year, as adjusted to reflect the weighted average number of treasury shares held by Cathay Pacific through reciprocal shareholding.

The calculation of basic earnings per share for the year ended 31 December 2010 was based on the profit attributable to equity holders of the Company for the year ended 31 December 2010 of approximately RMB12,005 million and the weighted average of 11,644,528,123 ordinary shares in issue during the year, as adjusted to reflect the weighted average number of treasury shares held by Cathay Pacific through reciprocal shareholding after considering the dilution effect caused by the additional issue of shares during the year.

No adjustment has been made to the basic earnings per share amounts presented for the years ended 31 December 2011 and 2010 in respect of a dilution as the Group had no potentially dilutive ordinary shares in issue during both years.

## 15 PROPERTY, PLANT AND EQUIPMENT

### Group

| | Aircraft and flight equipment *RMB'000* | Buildings *RMB'000* | Machinery *RMB'000* | Transportation equipment *RMB'000* | Office equipment *RMB'000* | Construction in progress *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|---|---|---|
| As 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 | 1,450,086 | 14,579 | 59,416 | 121,001 | 269,964 | 11,801,578 | 13,716,624 |
| Acquisition of a subsidiary | 15,667,878 | 904,864 | 456,138 | 83,762 | 22,750 | 1,209,396 | 18,344,788 |
| Disposals | (200,099) | (20,704) | (18,711) | (12,382) | (3,256) | – | (255,152) |
| Transfer from construction in progress | 10,719,125 | 1,491,894 | 228,753 | 19,184 | 9,012 | (12,467,968) | – |
| Reclassification to aircraft and flight equipment held for sale under current assets *(note 26)* | (259,552) | – | – | – | – | – | (259,552) |
| Impairment *(note 7)* | (1,863,008) | – | – | (186) | – | – | (1,863,194) |
| Depreciation charge for the year *(note 7)* | (7,861,370) | (190,428) | (205,266) | (153,581) | (158,725) | – | (8,569,370) |
| Exchange realignment | (5,944) | (108) | (80) | (330) | (10) | – | (6,472) |
| As at 31 December 2010 and 1 January 2011, net of accumulated depreciation and impairment | 82,654,556 | 5,876,491 | 1,784,795 | 777,651 | 362,745 | 4,696,304 | 96,152,542 |
| Additions | 1,785,258 | 91,036 | 297,576 | 132,183 | 79,282 | 27,568,686 | 29,954,021 |
| Disposals | (1,342,150) | (44,586) | (82,777) | (3,744) | (11,130) | – | (1,484,387) |
| Transfer from construction in progress | 23,680,416 | 117,549 | 210,456 | 46,939 | 21,349 | (24,076,709) | – |
| Reclassification to investment properties *(note 17)* | – | (197,913) | – | – | – | – | (197,913) |
| Reclassification to aircraft and flight equipment held for sale under current assets *(note 26)* | (183,904) | – | – | – | – | – | (183,904) |
| Impairment* *(note 7)* | (2,237,403) | – | – | – | – | – | (2,237,403) |
| Depreciation charge for the year *(note 7)* | (8,689,759) | (269,420) | (314,627) | (167,627) | (119,474) | – | (9,560,907) |
| Derecognition of a joint venture | (27,927) | – | (3,680) | (1,986) | (428) | – | (34,021) |
| Exchange realignment | (7,867) | – | (81) | (639) | (10) | – | (8,597) |
| As at 31 December 2011, net of accumulated depreciation and impairment | **95,631,220** | **5,573,157** | **1,891,662** | **782,777** | **332,334** | **8,188,281** | **112,399,431** |
| As at 31 December 2010 and 1 January 2011: | | | | | | | |
| Cost | 140,046,596 | 7,911,206 | 4,114,100 | 2,135,748 | 887,055 | 4,696,304 | 159,791,009 |
| Accumulated depreciation and impairment | (57,392,040) | (2,034,715) | (2,329,305) | (1,358,097) | (524,310) | – | (63,638,467) |
| Net book value | 82,654,556 | 5,876,491 | 1,784,795 | 777,651 | 362,745 | 4,696,304 | 96,152,542 |
| As at 31 December 2011: | | | | | | | |
| Cost | **159,995,048** | **7,742,054** | **4,445,902** | **2,254,321** | **911,758** | **8,188,281** | **183,537,364** |
| Accumulated depreciation and impairment | **(64,363,828)** | **(2,168,897)** | **(2,554,240)** | **(1,471,544)** | **(579,424)** | **–** | **(71,137,933)** |
| Net book value | **95,631,220** | **5,573,157** | **1,891,662** | **782,777** | **332,334** | **8,188,281** | **112,399,431** |

## 15 PROPERTY, PLANT AND EQUIPMENT (Continued)

### Company

| | Aircraft and flight equipment RMB'000 | Buildings RMB'000 | Machinery RMB'000 | Transportation equipment RMB'000 | Office equipment RMB'000 | Construction in progress RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|---|
| As at 1 January 2010, net of accumulated depreciation and impairment | 61,578,625 | 2,620,871 | 938,343 | 628,188 | 182,770 | 3,638,393 | 69,587,190 |
| Additions | 653,444 | 12,396 | 97,793 | 72,123 | 143,099 | 7,958,464 | 8,937,319 |
| Disposals | (160,583) | (2,669) | (8,989) | (9,605) | (1,724) | – | (183,570) |
| Transfer from construction in progress | 7,187,640 | 1,159,193 | 195,021 | 18,986 | 737 | (8,561,577) | – |
| Reclassification to aircraft and flight equipment held for sale under current assets *(note 26)* | (259,552) | – | – | – | – | – | (259,552) |
| Impairment | (1,278,689) | – | – | – | – | – | (1,278,689) |
| Depreciation charge for the year | (6,556,529) | (112,908) | (187,433) | (109,030) | (64,407) | – | (7,030,307) |
| As at 31 December 2010 and 1 January 2011, net of accumulated depreciation and impairment | 61,164,356 | 3,676,883 | 1,034,735 | 600,662 | 260,475 | 3,035,280 | 69,772,391 |
| Additions | 743,543 | 7,413 | 139,155 | 73,877 | 32,024 | 19,019,993 | 20,016,005 |
| Disposals | (898,656) | (6,784) | (7,536) | (3,619) | (7,044) | – | (923,639) |
| Transfer from construction in progress | 17,252,872 | 57,884 | 144,341 | 45,438 | 33,470 | (17,534,005) | – |
| Reclassification to aircraft and flight equipment held for sale under current assets *(note 26)* | (168,721) | – | – | – | – | – | (168,721) |
| Impairment | (1,141,234) | – | – | – | – | – | (1,141,234) |
| Depreciation charge for the year | (6,641,747) | (165,339) | (216,068) | (113,071) | (67,746) | – | (7,203,971) |
| As at 31 December 2011, net of accumulated depreciation and impairment | **70,310,413** | **3,570,057** | **1,094,627** | **603,287** | **251,179** | **4,521,268** | **80,350,831** |
| As at 31 December 2010 and 1 January 2011: | | | | | | | |
| Cost | 111,947,396 | 5,006,999 | 2,580,965 | 1,549,736 | 534,034 | 3,035,280 | 124,654,410 |
| Accumulated depreciation and impairment | (50,783,040) | (1,330,116) | (1,546,230) | (949,074) | (273,559) | – | (54,882,019) |
| Net book value | 61,164,356 | 3,676,883 | 1,034,735 | 600,662 | 260,475 | 3,035,280 | 69,772,391 |
| As at 31 December 2011: | | | | | | | |
| Cost | **125,801,001** | **5,047,585** | **2,795,026** | **1,631,313** | **554,277** | **4,521,268** | **140,350,470** |
| Accumulated depreciation and impairment | **(55,490,588)** | **(1,477,528)** | **(1,700,399)** | **(1,028,026)** | **(303,098)** | **–** | **(59,999,639)** |
| Net book value | **70,310,413** | **3,570,057** | **1,094,627** | **603,287** | **251,179** | **4,521,268** | **80,350,831** |

* During the year, the Group recognised an impairment loss of approximately RMB2,237 million relating to aircraft and flight equipment. The recoverable amounts of these impaired aircraft and flight equipment are the higher of their fair value less costs to sell and value in use. The Group has plans to sell these impaired assets and has received quotation from potential buyers. Those impaired aircraft which fall under the criteria at IFRS 5 Non-current Assets Held for Sale were reclassified as aircraft and flight equipment held for sale under current assets, details of which are set out in Note 26.

## 15 PROPERTY, PLANT AND EQUIPMENT (Continued)

As at 31 December 2011, the Group's aircraft and flight equipment, buildings and machinery with an aggregate net book value of approximately RMB37,482 million (2010: RMB27,575 million) were pledged to secure certain bank loans of the Group (note 38(a)).

The aggregate net book value of aircraft held under finance leases included in the property, plant and equipment of the Group amounted to approximately RMB34,762 million (2010: RMB28,310 million) (note 37(a)).

As at 31 December 2011, the Group was in the process of applying for the title certificates of certain buildings with an aggregate net book value of approximately RMB2,729 million (2010: RMB2,935 million). The Directors of the Company are of the opinion that the Group is entitled to lawfully and validly occupy and use the above-mentioned buildings, and therefore the aforesaid matter did not have any significant impact on the Group's financial position as at 31 December 2011.

## 16 LEASE PREPAYMENTS

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| **Cost** | | | | |
| As at 1 January | **2,390,599** | 2,088,610 | **1,789,028** | 1,698,791 |
| Additions | **76,709** | 182,042 | **2,145** | 90,237 |
| Acquisition of a subsidiary and a joint venture | **–** | 119,947 | **–** | – |
| Disposal | **(1,461)** | – | **–** | – |
| Reclassification to investment properties *(note 17)* | **(51,150)** | – | **–** | – |
| As at 31 December | **2,414,697** | 2,390,599 | **1,791,173** | 1,789,028 |
| **Accumulated amortisation** | | | | |
| As at 1 January | **(226,950)** | (133,791) | **(159,845)** | (114,354) |
| Acquisition of a subsidiary and a joint venture | **–** | (6,120) | **–** | – |
| Amortisation for the year *(note 7)* | **(53,247)** | (87,039) | **(39,053)** | (45,491) |
| Reclassification to investment properties *(note 17)* | **8,184** | – | **–** | – |
| As at 31 December | **(272,013)** | (226,950) | **(198,898)** | (159,845) |
| **Net carrying amount** | | | | |
| As at 31 December | **2,142,684** | 2,163,649 | **1,592,275** | 1,629,183 |

The Group's lease prepayments in respect of land are held under long term leases and located in Mainland China.

As at 31 December 2011, the Group's land use rights with an aggregate net book value of approximately RMB39.52 million (2010: RMB40.43 million) were pledged to secure certain bank loans of the Group (note 38(a)).

As at 31 December 2011, the Group was in the process of applying for the title certificates of certain land acquired by the Group with an aggregate net book value of approximately RMB626 million (2010: RMB631 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, and therefore the aforesaid matter did not have any significant impact on the Group's financial position as at 31 December 2011.

## 17 INVESTMENT PROPERTIES

The Group's investment properties are subsequently measured at cost model.

| | Group 2011 RMB'000 | Group 2010 RMB'000 |
|---|---|---|
| **Cost** | | |
| Reclassification from property, plant and equipment *(note 15)* | **287,464** | – |
| Reclassification from lease prepayments *(note 16)* | **51,150** | – |
| As at 31 December | **338,614** | – |
| **Accumulated amortisation** | | |
| Reclassification from property, plant and equipment *(note 15)* | **(89,551)** | – |
| Reclassification from lease prepayments *(note 16)* | **(8,184)** | – |
| As at 31 December | **(97,735)** | – |
| **Net carrying amount** | | |
| As at 31 December | **240,879** | – |

During the year, the Group leased a cargo terminal located in the Mainland China to a third party under an operating lease arrangement, further details of which are included in note 49 to the financial statements. As at 31 December 2011, the carrying amount of investment properties included lease prepayments of approximately RMB43 million relating to land use rights held under a medium term lease.

## 18 INTANGIBLE ASSET

| | Group and Company 2011 RMB'000 | Group and Company 2010 RMB'000 |
|---|---|---|
| As at 1 January | **41,076** | 49,267 |
| Reduction upon admission of new Star Alliance members | **(3,855)** | (8,191) |
| As at 31 December | **37,221** | 41,076 |

The Group's intangible asset represents admission rights to Star Alliance which is stated at cost and has an indefinite useful life.

## 19 GOODWILL

### Group

| | 2011 RMB'000 | 2010 RMB'000 |
|---|---|---|
| Cost and net carrying amount as at 1 January | **1,657,675** | 346,845 |
| Acquisition of additional interest in Shenzhen Airlines | **–** | 1,304,320 |
| Acquisition of additional interest in an associate | **–** | 6,510 |
| Goodwill attributable to non-controlling interest upon dilution of interest in a subsidiary | **(169,954)** | – |
| Provision for impairment *(note 7)* | **(176,891)** | – |
| Net carrying amount as at 31 December | **1,310,830** | 1,657,675 |
| As at 31 December | | |
| Cost | **1,487,721** | 1,657,675 |
| Impairment | **(176,891)** | – |
| Net carrying amount | **1,310,830** | 1,657,675 |

### Impairment testing of goodwill

Goodwill acquired through business combinations has been mainly allocated to the following cash-generating units for impairment testing:

- Air China Cargo cash-generating unit
- Shenzhen Airlines cash-generating unit

*Air China Cargo cash-generating unit*

The recoverable amount of the Air China Cargo cash-generating unit has been determined based on a value in use calculation using cash flow projections based on financial budgets covering a five-year period approved by senior management. The discount rate applied to the cash flow projections is 10.8% (2010: 10.5%) and cash flows beyond the five-year period were extrapolated using a growth rate of 2% by reference to the long term average growth rate. The Group accrued full provision for impairment of goodwill allocated to Air China Cargo as the result of impairment test.

*Shenzhen Airlines cash-generating unit*

The recoverable amount of the Shenzhen Airlines cash-generating unit was determined based on a value in use calculation using cash flow projections based on financial budgets covering a four-year period approved by senior management. The discount rate applied to the cash flow projections is 10.8% (2010: 10.5%) and cash flows beyond the four-year period were extrapolated using a growth rate of 2% by reference to the long term average growth rate.

## 19 GOODWILL (Continued)

The net carrying amounts of goodwill allocated to each of the cash-generating units are as follows:

| Air China Cargo | | Shenzhen Airlines | | Others | | Total | |
|---|---|---|---|---|---|---|---|
| **2011** | 2010 | **2011** | 2010 | **2011** | 2010 | **2011** | 2010 |
| ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| **–** | 346,845 | **1,304,320** | 1,304,320 | **6,510** | 6,510 | **1,310,830** | 1,657,675 |

Key assumptions were used in the value in use calculation for 31 December 2011 and 31 December 2010. The following describes each key assumption on which management has based its cash flow projections to undertake impairment testing of goodwill:

*Budgeted gross margins* – The basis used to determine the value assigned to the budgeted gross margins is the average gross margins achieved in the year immediately before the budget year, increased for expected efficiency improvements, and expected market development.

*Discount rates* – The discount rates used reflect specific risks relating to the relevant units.

The values assigned to the key assumptions on utilisation of aircraft, market development and discount rates are consistent with external information sources.

## 20 INTERESTS IN SUBSIDIARIES

| | Company | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Unlisted investments, at cost | **17,343,911** | 16,513,911 |
| Due from subsidiaries *(note 54)* | **1,296,115** | 617,201 |
| Due to subsidiaries *(note 54)* | **(397,288)** | (367,364) |
| | **18,242,738** | 16,763,748 |

The balances with the subsidiaries are unsecured, interest-free and have no fixed terms of repayment.

## 20 INTERESTS IN SUBSIDIARIES (Continued)

Particulars of the principal subsidiaries as at 31 December 2011 are as follows:

| Company name | Place of incorporation/ registration and operations | Legal status | Nominal value of paid-up capital | Percentage of equity interests attributable to the Company Direct | Indirect | Principal activities |
|---|---|---|---|---|---|---|
| China National Aviation Company Limited ("CNAC") (中航興業有限公司) | Hong Kong | Limited liability company | HK$400,000,000 | 69 | 31 | Investment holding |
| Air China Group Import and Export Trading Co. ("AIE") (國航進出口有限公司) | PRC/Mainland China | Limited liability company | RMB95,080,786 | 100 | – | Import and export trading |
| Zhejiang Air Services Co., Ltd. # (浙江航空服務有限公司) | PRC/Mainland China | Limited liability company | RMB20,000,000 | 100 | – | Provision of cabin service and airline catering |
| Shanghai Air China Aviation Service Co., Ltd. # (上海國航航空服務有限公司) | PRC/Mainland China | Limited liability company | RMB2,000,000 | 100 | – | Provision of ground service |
| Air China Development Corporation (Hong Kong) Limited (國航香港發展有限公司) | Hong Kong | Limited liability company | HK$9,379,010 | 95 | – | Provision of air ticketing services |
| Beijing Golden Phoenix Human Resource Co., Ltd. # (北京金凰凰人力資源服務有限公司) | PRC/Mainland China | Limited liability company | RMB1,700,000 | 100 | – | Provision of human resources services |
| Total Transform Group Ltd. (國航海外控股有限公司) | British Virgin Islands | Limited liability company | HK$13,765,440,000 | 99.94 | 0.06 | Investment holding |
| Air Macau Company Limited ("Air Macau") (澳門航空股份有限公司) | Macau | Limited liability company | MOP442,042,000 | – | 67 | Airline operator |
| Angel Paradise Limited | British Virgin Islands | Limited liability company | US$10 | – | 100 | Investment holding |
| Air China Cargo (中國國際貨運航空有限公司) | PRC/Mainland China | Limited liability company | RMB3,235,294,118 | 51 | 49 | Provision of cargo carriage services |
| Chengdu Falcon Aircraft Engineering Service Co., Ltd. # ("Chengdu Falcon") (成都富凱飛機工程服務有限公司) | PRC/Mainland China | Limited liability company | RMB37,565,216 | 60 | – | Provision of aircraft overhaul and maintenance services |
| Shenzhen Airlines (深圳航空有限責任公司) | PRC/Mainland China | Limited liability company | RMB812,500,000 | 51 | – | Airline operator |
| Shenzhen Jinpeng Industrial & Trading Co., Ltd # (深圳金鵬工貿有限責任公司) | PRC/Mainland China | Limited liability company | RMB20,000,000 | – | 100 | Tickets agent |
| Shenzhen Kunpeng International Flight Academy # (深圳鯤鵬國際飛行學校) | PRC/Mainland China | Private non-enterprise organisation | RMB3,000,000 | – | 100 | Flight academy |
| Kunming Airlines Co., Ltd (昆明航空有限公司) # | PRC/Mainland China | Limited liability company | RMB80,000,000 | – | 80 | Airline operator |
| Beijing Airlines Co., Ltd # (北京航空有限責任公司) | PRC/Mainland China | Limited liability company | RMB1,000,000,000 | 51 | – | Airline operator |
| Dalian Airlines Co., Ltd # (大連航空有限責任公司) | PRC/Mainland China | Limited liability company | RMB400,000,000 | 80 | – | Airline operator |

# The English names of these companies are direct translations of their Chinese names.

During the year, two new subsidiaries namely Beijing Airlines Co., Ltd and Dalian Airlines Co., Ltd were established on 28 February and 1 August 2011, respectively.

## 20 INTERESTS IN SUBSIDIARIES (Continued)

The above table lists the subsidiaries of the Company which, in the opinion of the Directors, principally affected the results for the year ended 31 December 2011 or formed a substantial portion of the net assets of the Group at 31 December 2011. To give details of other subsidiaries would, in the opinion of the Directors, result in particulars of excessive length.

## 21 INTERESTS IN JOINT VENTURES

| | Company | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Unlisted investments, at cost | **856,076** | 856,076 |

Particulars of the joint ventures of the Group at 31 December 2011 are as follows:

| Company name | Place of incorporation/ registration and operations | Issued capital | Ownership interest | Percentage of Voting power | Profit sharing | Principal activities |
|---|---|---|---|---|---|---|
| Aircraft Maintenance and Engineering Corporation, Beijing (北京飛機維修工程有限公司) | PRC/Mainland China | US$187,533,000 | 60 | 57.1 | 60 | Provision of aircraft and engine overhaul and maintenance services |
| SkyWorks Capital Asia Ltd. | Hong Kong | HK$30 | 33.3 | 33.3 | 33.3 | Provision of financial services |
| ACT Cargo (USA), Inc. | United States | US$500,000 | 51 | 55.6 | 51 | Cargo forwarding agent |
| Shanghai Pudong International Airport Cargo Terminal Co., Ltd. # (上海浦東國際機場西區公共貨運站有限公司) | PRC/Mainland China | RMB680,000,000 | 39 | 28.6 | 39 | Provision of cargo carriage services |
| Jade Cargo International Company Limited # (翡翠國際航空貨運有限責任公司) | PRC/Mainland China | RMB245,662,126 | 51 | 50 | 51 | Provision of cargo carriage services |
| SSAMC (四川國際航空發動機維修有限公司) | PRC/Mainland China | US$71,900,000 | 60 | 60 | 60 | Provision of engine overhaul and maintenance services |

# The English name of the company is the direct translation of its Chinese name.

Henan Airlines Company Limited ("Henan Airlines") is in the process of liquidation. The liquidator has taken over the control over the operation of Henan Airlines since 24 October 2011. Therefore, the Group ceased to have joint control over Henan Airlines and accordingly the investment in Henan Airlines was deconsolidated in the Group's consolidated statements of financial position as at 31 December 2011. As at 31 December 2011, the investment in Henan Airlines has been impaired and fully provided for.

## 21 INTERESTS IN JOINT VENTURES (Continued)

The Group's proportionate share of the assets, liabilities, revenue and expenses of the joint ventures at the end of the reporting period are as follows:

| | Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Current assets | **1,638,867** | 1,703,497 |
| Non-current assets | **2,363,194** | 3,113,983 |
| Current liabilities | **(3,769,877)** | (2,415,143) |
| Non-current liabilities | **(236,924)** | (1,504,430) |
| Net assets/(liabilities) attributable to the Group | **(4,740)** | 897,907 |
| Revenue | **3,662,589** | 3,158,652 |
| Operating expenses | **(4,378,855)** | (2,991,037) |
| Finance revenue | **36,869** | 18,735 |
| Finance costs | **(102,267)** | (67,376) |
| Profit/(loss) before tax attributable to the Group | **(781,664)** | 118,974 |
| Tax | **(32,303)** | (33,057) |
| Profit/(loss) for the year attributable to the Group | **(813,967)** | 85,917 |

## 22 INTERESTS IN ASSOCIATES

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Listed shares in Mainland China, at cost | **–** | – | **163,477** | 163,477 |
| Unlisted investments, at cost | **–** | – | **534,615** | 534,615 |
| Share of net assets | **10,628,510** | 11,385,388 | **–** | – |
| Goodwill on acquisition | **2,886,729** | 2,886,729 | **–** | – |
| Due from associates *(note 54)* | **16,022** | 44,420 | **5,652** | 40,448 |
| Due to associates *(note 54)* | **(134,230)** | (128,111) | **(57,378)** | (30,753) |
| | **13,397,031** | 14,188,426 | **646,366** | 707,787 |
| Market value of listed shares | | | **1,267,595** | 2,142,000 |

As at 31 December 2011, the listed shares in an associate of the Group with an aggregate market value of approximately RMB4,312 million (2010: RMB7,287 million) were pledged to secure certain bank loans of the Group (note 38(b)).

## 22 INTERESTS IN ASSOCIATES (Continued)

Particulars of the principal associates as at 31 December 2011 are as follows:

| Company name | Place of incorporation/ registration and operations | Nominal value of registered/issued share capital | Percentage of equity interests attributable to the Group | Principal activities |
|---|---|---|---|---|
| Cathay Pacific* △ (國泰航空有限公司) | Hong Kong | HK$787,139,514 | 29.99 | Airline operator |
| Shandong Aviation Group Corporation ("Shandong Aviation")△ (山東航空集團有限公司) | PRC/Mainland China | RMB580,000,000 | 49.4 | Investment holding |
| Shandong Airlines Co., Ltd.△ (山東航空股份有限公司) | PRC/Mainland China | RMB400,000,000 | 22.8 | Airline operator |
| China National Aviation Finance Co., Ltd. ("CNAF")**△ (中國航空集團財務有限責任公司) | PRC/Mainland China | RMB505,269,500 | 23.5 | Provision of financial services |
| Menzies Macau Airport Services Limited* (明捷澳門機場服務有限公司) | Macau | MOP10,000,000 | 41 | Provision of airport ground handling services |
| Guangzhou Baiyun International Airport Ground Handling Service Company Limited△ (廣州白雲國際機場地勤服務有限公司) | PRC/Mainland China | RMB100,000,000 | 21 | Provision of airport ground handling services |
| Yunnan Airport Aircraft Maintenance Services Co., Ltd.△ (雲南空港飛機維修服務有限公司) | PRC/Mainland China | RMB10,000,000 | 40 | Provision of aircraft overhaul and maintenance services |
| CAAC Cares Chongqing Co., Ltd.△ (重慶民航凱亞信息技術有限公司) | PRC/Mainland China | RMB9,800,000 | 24.5 | Provision of airline-related information system services |
| Chengdu CAAC Southwest Cares Co., Ltd.△# (成都民航西南凱亞有限責任公司) | PRC/Mainland China | RMB10,000,000 | 35 | Provision of airline-related information system services |
| Macau Aircraft Maintenance and Engineering Corporation△# (澳門飛機維修工程有限公司) | Macau | MOP100 | 35 | Provision of aircraft overhaul and maintenance services |
| Shenzhen Airlines Property Development Co., Ltd. ("SZ Property")*△ (深航房地產開發有限責任公司) | PRC/Mainland China | RMB100,000,000 | 30 | Property development |
| Zhengzhou Aircraft Maintenance Engineering Co., Ltd*△# (鄭州飛機維修工程有限公司) | PRC/Mainland China | RMB150,000,000 | 30 | Provision of aircraft overhaul and maintenance services |

## 22 INTERESTS IN ASSOCIATES (Continued)

* The equity interests of these associates are held indirectly through certain subsidiaries of the Company.

** 19.3% of the Group's equity interest in CNAF is held directly by the Company, and the remaining 4.2% is held indirectly through certain subsidiaries of the Company.

△ Not audited by Ernst & Young, Hong Kong or another member firm of the Ernst & Young global network.

# The English names of these companies are direct translations of their Chinese names.

The above table lists the associates of the Group which, in the opinion of the Directors, principally affected the results for the year or formed a substantial portion of the net assets of the Group as at 31 December 2011. To give details of other associates would, in the opinion of the Directors, result in particulars of excessive length.

Summarised financial information of the Group's associates at the end of the reporting period is as follows:

| | Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Total assets | **129,918,794** | 128,321,857 |
| Total liabilities | **(80,257,773)** | (78,045,923) |
| Revenue | **92,402,939** | 86,573,436 |
| Net profits | **5,756,881** | 13,313,969 |

Movements in goodwill are as follows:

| | Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| As at 1 January | **2,886,729** | 2,893,239 |
| Acquisition of a joint venture | **–** | (6,510) |
| As at 31 December | **2,886,729** | 2,886,729 |

## 23 LONG TERM RECEIVABLE FROM THE ULTIMATE HOLDING COMPANY

On 30 September 2004, the Company entered into an agreement with CNAHC whereby CNAHC agreed to assume the obligations to settle an aggregate amount of approximately RMB757 million, which was recorded by the Group as a government grant receivable as at 31 December 2003 of RMB842 million, consisting of a long term portion and a short term portion of RMB764 million and RMB78 million, respectively. This receivable from CNAHC is unsecured, interest-free and is repayable over eight years commencing from 31 December 2004 by 16 semi-annual instalments to be made by 30 June and 31 December each year. Pursuant to the relevant agreement, the first instalment amount of RMB25 million was settled by 31 December 2004 and the final instalment amount of approximately RMB32 million will be settled by 30 June 2012, with the remaining 14 semi-annual instalment amounts of RMB50 million each to be settled by 30 June and 31 December each year between 30 June 2005 and 31 December 2011.

## 24 AVAILABLE-FOR-SALE INVESTMENTS

Available-for-sale investments consist of unlisted equity investments measured at cost less impairment losses.

## 25 DEFERRED TAX ASSETS AND LIABILITIES

The movements in deferred tax assets and liabilities during the year are as follows:

| | **Group** | | **Company** | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Deferred tax liabilities | | | | |
| As at 1 January | **1,006,227** | 263,750 | **128,387** | 263,750 |
| Acquisition of a subsidiary | **–** | 695,833 | **–** | – |
| Charge for the year *(note 11)* | **206,803** | 46,644 | **7,613** | (135,363) |
| Gross deferred tax liabilities as at 31 December | **1,213,030** | 1,006,227 | **136,000** | 128,387 |
| Deferred tax assets | | | | |
| As at 1 January | **2,193,002** | 1,682,203 | **1,515,000** | 1,626,750 |
| Acquisition of a subsidiary | **–** | 453,860 | **–** | – |
| Charge for the year *(note 11)* | **884,500** | 56,939 | **746,490** | (111,750) |
| Gross deferred tax assets as at 31 December | **3,077,502** | 2,193,002 | **2,261,490** | 1,515,000 |
| Net deferred assets as at 31 December | **1,864,472** | 1,186,775 | **2,125,490** | 1,386,613 |

## 25 DEFERRED TAX ASSETS AND LIABILITIES (Continued)

The principal components of the Group's and the Company's deferred tax assets and liabilities are as follows:

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Deferred tax liabilities | | | | |
| Differences in value of property, plant and equipment | **–** | (387) | **–** | (387) |
| Unrealised exchange gain | **(95,000)** | (128,000) | **(95,000)** | (128,000) |
| Depreciation allowance in excess of the related depreciation | **(1,065,671)** | (858,671) | **(41,000)** | – |
| Others | **(52,359)** | (19,169) | **–** | – |
| Gross deferred tax liabilities | **(1,213,030)** | (1,006,227) | **(136,000)** | (128,387) |
| Deferred tax assets | | | | |
| Differences in value of property, plant and equipment | **20,490** | – | **20,490** | – |
| Provisions and accruals | **2,054,513** | 1,464,762 | **1,481,000** | 970,000 |
| Losses available for offsetting against future taxable income | **128,043** | 20,430 | **–** | – |
| Unrealised loss on derivative financial instruments | **44,000** | 85,000 | **44,000** | 85,000 |
| Impairment | **759,456** | 513,810 | **645,000** | 351,000 |
| Government grants and subsidies | **71,000** | 109,000 | **71,000** | 109,000 |
| Gross deferred tax assets | **3,077,502** | 2,193,002 | **2,261,490** | 1,515,000 |
| Net deferred tax assets | **1,864,472** | 1,186,775 | **2,125,490** | 1,386,613 |

Deferred tax assets not recognised are as follows:

| | Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Tax losses | **1,918,547** | 968,548 |
| Deductible temporary differences | **937,770** | 129,735 |
| | **2,856,317** | 1,098,283 |

The Group has tax losses arising from operations outside Mainland China of RMB177,444,000 (2010: RMB384,269,000) that will expire in three financial years from the year of incurrence for offsetting against future taxable profits. The Group also has tax losses arising from the operation in Mainland China of RMB1,741,103,000 (2010: RMB584,279,000) that will expire in five financial years from the year of incurrence for offsetting against future taxable profits. Deferred tax assets have not been recognised in respect of these losses which relate to subsidiaries that have been loss-making for some years and it is not considered probable that sufficient taxable profits will be available in the near future against which the tax losses can be utilised.

There are no income tax consequences attaching to the payment of dividends by the Company to its shareholders.

## 26 AIRCRAFT AND FLIGHT EQUIPMENT HELD FOR SALE

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| As at 1 January | **303,736** | 526,920 | **259,552** | 159,594 |
| Disposals | **(278,103)** | (482,736) | **(259,552)** | (159,594) |
| Reclassification from property, plant and equipment during the year *(note 15)* | **183,904** | 259,552 | **168,721** | 259,552 |
| | **209,537** | 303,736 | **168,721** | 259,552 |
| Impairment | **(117,050)** | (226,054) | **(91,510)** | (185,992) |
| As at 31 December | **92,487** | 77,682 | **77,211** | 73,560 |

The movements in the provision for impairment of aircraft and flight equipment held for sale are as follows:

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| As at 1 January | **(226,054)** | (396,106) | **(185,992)** | (27,892) |
| Disposal | **202,688** | 356,044 | **185,992** | 27,892 |
| Reclassification to property, plant and equipment during the year | **5,985** | – | **–** | – |
| Provision during the year *(note 7)* | **(99,669)** | (185,992) | **(91,510)** | (185,992) |
| As at 31 December | **(117,050)** | (226,054) | **(91,510)** | (185,992) |

Aircraft and flight equipment held for sale represent aircraft and the related flight equipment to retire in the next 12 months and are measured at the lower of their carrying amounts and fair values less costs to sell.

## 27 INVENTORIES

An analysis of inventories as at the end of the reporting period is as follows:

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Spare parts of flight equipment | **1,365,272** | 1,195,218 | **705,170** | 570,788 |
| Work in progress | **388,785** | 372,349 | **4,409** | 2,633 |
| Catering supplies | **56,263** | 41,384 | **52,967** | 37,555 |
| | **1,810,320** | 1,608,951 | **762,546** | 610,976 |

## 28 ACCOUNTS RECEIVABLE

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Accounts receivable | **2,772,518** | 3,161,458 | **1,270,164** | 1,496,235 |
| Impairment | **(71,787)** | (69,389) | **(45,568)** | (48,608) |
| | **2,700,731** | 3,092,069 | **1,224,596** | 1,447,627 |

The Group normally allows a credit period of 30 to 90 days to its sales agents and other customers while some major customers are granted a credit period up to six months or above. 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 the accounts receivable as at the end of the reporting period, net of provision for impairment, is as follows:

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Within 30 days | **2,276,040** | 2,495,523 | **1,071,320** | 1,176,637 |
| 31 to 60 days | **240,359** | 272,380 | **113,403** | 85,677 |
| 61 to 90 days | **70,293** | 97,884 | **20,968** | 22,352 |
| Over 90 days | **114,039** | 226,282 | **18,905** | 162,961 |
| | **2,700,731** | 3,092,069 | **1,224,596** | 1,447,627 |

Included in accounts receivable as at the end of the reporting period is the following amount due from joint ventures:

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Joint ventures | **2,171** | 1,412 | **–** | – |

## 28 ACCOUNTS RECEIVABLE (Continued)

The movements in the provision for impairment of accounts receivable are as follows:

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| As at 1 January | **69,389** | 51,478 | **48,608** | 42,288 |
| Acquisition of a subsidiary and a joint venture | **–** | 10,928 | **–** | – |
| Impairment losses recognised *(note 7)* | **14,751** | 8,983 | **4,910** | 8,857 |
| Amount reversed *(note 7)* | **(10,980)** | – | **(7,516)** | – |
| Amount written off as uncollectible | **(1,373)** | (2,000) | **(434)** | (2,537) |
| As at 31 December | **71,787** | 69,389 | **45,568** | 48,608 |

As at 31 December 2011, accounts receivable with a nominal value of RMB23,502,809 (2010: RMB26,151,216) were impaired and fully provided for. The individually impaired accounts receivable relate to customers that were in financial difficulties and the probability to recover these receivables is remote.

An aged analysis of the accounts receivable that are not considered to be impaired is as follows:

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Neither past due nor impaired | **2,146,537** | 2,660,326 | **826,787** | 1,193,591 |
| Less than 3 moths past due | **463,205** | 393,900 | **330,842** | 245,885 |
| More than 3 months past due | **90,989** | 37,843 | **66,967** | 8,151 |
| | **2,700,731** | 3,092,069 | **1,224,596** | 1,447,627 |

Receivables that were neither past due nor impaired relate to a large number of diversified customers for whom there was no recent history of default.

Receivables that were past due but not impaired relate to a number of independent customers that have a good track record with the Group. Based on past experience, the Directors of the Company are of the opinion that no provision for impairment is necessary in respect of these balances as there has not been a significant change in credit quality and the balances are still considered fully recoverable. The Group does not hold any collateral or other credit enhancements over these balances.

## 29 PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

An analysis of prepayments, deposits and other receivables as at the end of the reporting period, net of provision for impairment, is as follows:

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| **Prepayments** | | | | |
| Advances and others | **352,116** | 486,809 | **180,512** | 133,820 |
| Manufacturers' credits | **827,013** | 424,817 | **696,135** | 263,957 |
| Prepaid aircraft operating lease rentals | **283,012** | 268,015 | **147,828** | 148,317 |
| | **1,462,141** | 1,179,641 | **1,024,475** | 546,094 |
| **Deposits and other receivables** | **1,235,051** | 1,104,589 | **616,678** | 530,010 |
| | **2,697,192** | 2,284,230 | **1,641,153** | 1,076,104 |

The movements in the provision for impairment of prepayments, deposits and other receivables are as follows:

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| As at 1 January | **3,312,082** | 9,619 | **–** | – |
| Acquisition of a subsidiary | **–** | 3,185,145 | **–** | – |
| Impairment losses recognised *(note 7)* | **294,771** | 118,609 | **–** | – |
| Amount reversed *(note 7)* | **(55,189)** | – | **–** | – |
| Amount written off as uncollectible | **(5,990)** | (1,003) | **–** | – |
| Exchange realignment | **(109)** | (288) | **–** | – |
| As at 31 December | **3,545,565** | 3,312,082 | **–** | – |

## 30 FINANCIAL ASSETS AND FINANCIAL LIABILITIES

### Group

| | 2011 | | 2010 | |
|---|---|---|---|---|
| | **Assets** | **Liabilities** | Assets | Liabilities |
| | ***RMB'000*** | ***RMB'000*** | *RMB'000* | *RMB'000* |
| Fuel derivative contracts | – | – | – | 83,506 |
| Interest rate derivative contracts | **3,549** | **223,137** | 5,894 | 330,012 |
| Forward foreign exchange contracts | – | – | – | 13,811 |
| Listed equity securities at fair value | **8,595** | – | 21,485 | – |
| | **12,144** | **223,137** | 27,379 | 427,329 |

### Company

| | 2011 | | 2010 | |
|---|---|---|---|---|
| | **Assets** | **Liabilities** | Assets | Liabilities |
| | ***RMB'000*** | ***RMB'000*** | *RMB'000* | *RMB'000* |
| Fuel derivative contracts | – | – | – | 83,506 |
| Interest rate derivative contracts | – | **176,167** | – | 256,543 |
| | – | **176,167** | – | 340,049 |

The above financial assets and liabilities are accounted for as held-for-trading financial instruments and any fair value changes are recognised in the income statement.

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 these objectives, the Group allows for the use of approved derivative instruments with approved counterparties and within approved credit limits. The movements in the fair value of fuel derivative contracts for the year ended 31 December 2011 was RMB85,446,542 (2010: RMB1,954,070,906), which consisted of a recovery in fair value of RMB83,505,624 (2010: RMB1,967,922,187) and an increase in fair value of RMB1,940,918 (2010: a decrease in fair value of RMB13,851,281) resulting from the settlement of fuel derivative contracts.

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

## 31 ENTRUSTED LOANS

During the year, the Company provided short term entrusted loans to certain subsidiaries of the Group through CNAF. The interest rates of these entrusted loans range from 5.49% to 6.10% with borrowing terms of 6 months.

## 32 BALANCES WITH THE ULTIMATE HOLDING COMPANY AND RELATED COMPANIES

The balances with the ultimate holding company and related companies are unsecured, interest-free and repayable within one year or have no fixed terms of repayment.

## 33 PLEDGED DEPOSITS, CASH AND CASH EQUIVALENTS

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Cash and bank balances | **4,963,512** | 3,477,325 | **997,004** | 1,620,070 |
| Cash placed with CNAF (China National Aviation Finance Co., Ltd.) | **116,374** | 99,659 | **116,072** | 99,242 |
| Total cash and bank balances | **5,079,886** | 3,576,984 | **1,113,076** | 1,719,312 |
| Time deposits placed with banks | **7,080,051** | 7,867,795 | **3,254,047** | 5,982,305 |
| Time deposits placed with CNAF | **3,430,000** | 3,800,000 | **3,430,000** | 3,800,000 |
| Total time deposits | **10,510,051** | 11,667,795 | **6,684,047** | 9,782,305 |
| Less: Pledged deposits against | | | | |
| – Aircraft operating leases and financial derivatives | **(130,133)** | (324,923) | **–** | – |
| – Bank loans | **–** | (436,270) | **–** | – |
| – Others | **(2,432)** | (81,872) | **–** | – |
| Total pledged deposits | **(132,565)** | (843,065) | **–** | – |
| Non-pledged deposits | **10,377,486** | 10,824,730 | **6,684,047** | 9,782,305 |
| Cash and cash equivalents | **15,457,372** | 14,401,714 | **7,797,123** | 11,501,617 |

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

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Non-pledged time deposits with original maturity of: | | | | |
| Less than 3 months when acquired | **5,703,587** | 10,799,066 | **3,437,748** | 9,762,923 |
| Over 3 months when acquired | **4,673,899** | 25,664 | **3,246,299** | 19,382 |
| | **10,377,486** | 10,824,730 | **6,684,047** | 9,782,305 |

Cash at banks earns interest at floating rates based on daily bank deposit rates. Time deposits are placed for vesting periods of up to one year, depending on the cash requirements of the Group and the Company, and earn interest at the respective time deposit rates. The bank balances and pledged deposits are deposited with creditworthy banks with no recent history of default.

As at 31 December 2011, the Group had a bank balance of US$12,262,700 (equivalent to RMB77,266,046) which was put under custody of a commercial bank for aircraft purchase payments.

## 34 ACCOUNTS PAYABLE

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

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Within 30 days | **7,560,307** | 5,590,954 | **4,416,387** | 3,441,775 |
| 31 to 60 days | **889,164** | 959,910 | **489,726** | 618,938 |
| 61 to 90 days | **459,248** | 456,123 | **223,784** | 331,275 |
| Over 90 days | **1,508,467** | 1,093,485 | **1,425,530** | 494,501 |
| | **10,417,186** | 8,100,472 | **6,555,427** | 4,886,489 |

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

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Joint ventures | **230,618** | 106,741 | **416,426** | 156,254 |

The accounts payable are non-interest-bearing and have normal credit terms of 90 days.

## 35 BILLS PAYABLE

An aged analysis of the bills payable as at the end of the reporting period is as follows:

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| 31 to 60 days | **–** | 208,600 | **–** | – |
| 61 to 90 days | **–** | 128,727 | **–** | – |
| Over 90 days | **–** | 50,000 | **–** | – |
| | **–** | 387,327 | **–** | – |

## 36 OTHER PAYABLES AND ACCRUALS

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

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Provision for staff housing benefits | **31,670** | 47,350 | **29,411** | 45,091 |
| Accrued salaries, wages and benefits | **2,976,406** | 1,988,466 | **1,848,473** | 1,090,817 |
| Interest payable | **414,891** | 320,254 | **336,128** | 283,176 |
| Business tax, customs duties and levies tax payable | **1,232,824** | 1,061,619 | **753,001** | 749,818 |
| Current portion of long term payables *(note 40)* | **14,663** | 28,716 | **1,524** | 6,817 |
| Current portion of deferred income related to the frequent-flyer programme *(note 41(a))* | **310,675** | 423,658 | **180,032** | 347,338 |
| Current portion of deferred income related to government grants *(note 41(b))* | **223,759** | 110,671 | **223,759** | 110,671 |
| Deposits received from sales agents | **1,050,290** | 851,033 | **461,229** | 348,286 |
| Accrued operating expenses | **1,719,619** | 1,812,333 | **805,758** | 1,073,479 |
| Receipts in advance for employee residence | **1,862,804** | 806,025 | **–** | – |
| Due to a non-controlling shareholder of a subsidiary | **707,787** | 707,787 | **–** | – |
| Land lease payable | **256,538** | 256,538 | **–** | – |
| Others | **2,013,849** | 845,383 | **906,815** | 264,995 |
| | **12,815,775** | 9,259,833 | **5,546,130** | 4,320,488 |

Included in the other payables and accruals as at the end of the reporting period is the following amounts due to joint ventures:

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Joint ventures | **5,311** | 9,970 | **1,279** | – |

## 37 OBLIGATIONS UNDER FINANCE LEASES

The Group and the Company have obligations under finance lease agreements expiring during the years from 2013 to 2023 (2010: 2011 to 2022) in respect of aircraft. An analysis of the future minimum lease payments under these finance leases as at the end of the reporting period, together with the present values of the net minimum lease payments which are principally denominated in foreign currencies, are as follows:

### Group

| | **Minimum lease payments 2011** *RMB'000* | **Present values of minimum lease payments 2011** *RMB'000* | Minimum lease payments 2010 *RMB'000* | Present values of minimum lease payments 2010 *RMB'000* |
|---|---|---|---|---|
| Amounts repayable: | | | | |
| Within one year | **2,872,990** | **2,687,925** | 2,336,913 | 2,223,240 |
| In the second year | **2,880,384** | **2,713,995** | 2,339,661 | 2,250,662 |
| In the third to fifth years, inclusive | **8,936,842** | **8,564,818** | 7,109,895 | 6,918,659 |
| Over five years | **8,153,488** | **7,913,047** | 7,139,157 | 6,892,031 |
| Total minimum finance lease payments *(notes 51 and 53)* | **22,843,704** | **21,879,785** | 18,925,626 | 18,284,592 |
| Less: Amounts representing finance charges | **(963,919)** | | (641,034) | |
| Present value of minimum lease payments | **21,879,785** | | 18,284,592 | |
| Less: Portion classified as current liabilities | **(2,687,925)** | | (2,223,240) | |
| Non-current portion | **19,191,860** | | 16,061,352 | |

## 37 OBLIGATIONS UNDER FINANCE LEASES (Continued)

### Company

| | **Minimum lease payments 2011 *RMB'000*** | **Present values of minimum lease payments 2011 *RMB'000*** | Minimum lease payments 2010 *RMB'000* | Present values of minimum lease payments 2010 *RMB'000* |
|---|---|---|---|---|
| Amounts repayable: | | | | |
| Within one year | **2,629,613** | **2,505,900** | 2,114,129 | 2,048,727 |
| In the second year | **2,713,735** | **2,596,827** | 2,127,253 | 2,076,198 |
| In the third to fifth years, inclusive | **8,543,050** | **8,278,176** | 6,838,500 | 6,720,277 |
| Over five years | **7,741,847** | **7,553,122** | 6,809,804 | 6,610,650 |
| Total minimum finance lease payments *(notes 51 and 53)* | **21,628,245** | **20,934,025** | 17,889,686 | 17,455,852 |
| Less: Amounts representing finance charges | **(694,220)** | | (433,834) | |
| Present value of minimum lease payments | **20,934,025** | | 17,455,852 | |
| Less: Portion classified as current liabilities | **(2,505,900)** | | (2,048,727) | |
| Non-current portion | **18,428,125** | | 15,407,125 | |

Certain finance lease arrangements comprise finance leases between the Company and certain of its subsidiaries, and the corresponding borrowings between such subsidiaries and commercial banks. The Company has guaranteed the subsidiaries' obligations under those bank borrowing arrangements and, accordingly, the relevant assets and obligations are recorded in the Company's statement of financial position to reflect the substance of the transactions. The future payments under these finance leases have therefore been presented by the Company and the Group in the amounts that reflect the payments under the bank borrowing arrangements between the subsidiaries and commercial banks.

As at 31 December 2011, there were 90 (2010: 74) aircraft under finance lease agreements. Under the terms of the leases, the Company has the option to purchase these aircraft, at the end of or during the lease terms, at market value or at the price as stipulated in the finance lease agreements. The effective borrowing rates during the current year ranged from -1.51% to 7.05% (2010: -1.52% to 6.40%) per annum.

The Group's finance leases were secured by mortgages over certain of the Group's aircraft, which had an aggregate net carrying amount of approximately RMB34,762 million (2010: RMB28,310 million) (note 15).

The Company's finance leases were secured by mortgages over certain of the Company's aircraft, which had an aggregate net carrying amount of approximately RMB33,491 million (2010: RMB27,226 million).

## 38 INTEREST-BEARING BANK LOANS AND OTHER BORROWINGS

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Bank loans: | | | | |
| Secured | **26,430,507** | 24,362,134 | **10,874,464** | 7,450,002 |
| Unsecured | **31,095,287** | 33,274,531 | **28,679,731** | 30,219,346 |
| | **57,525,794** | 57,636,665 | **39,554,195** | 37,669,348 |
| Other loans: | | | | |
| Secured | **210,000** | 270,000 | **–** | – |
| Unsecured | **800,000** | 735,499 | **–** | – |
| | **1,010,000** | 1,005,499 | **–** | – |
| Corporate bonds – unsecured | **9,000,000** | 9,000,000 | **9,000,000** | 9,000,000 |
| | **67,535,794** | 67,642,164 | **48,554,195** | 46,669,348 |
| Bank loans repayable: | | | | |
| Within one year | **24,277,313** | 24,757,226 | **18,383,897** | 19,093,115 |
| In the second year | **9,437,746** | 9,862,106 | **7,436,853** | 8,228,949 |
| In the third to fifth years, inclusive | **13,906,847** | 12,275,782 | **8,441,328** | 7,508,840 |
| Over five years | **9,903,888** | 10,741,551 | **5,292,117** | 2,838,444 |
| | **57,525,794** | 57,636,665 | **39,554,195** | 37,669,348 |
| Other loans repayable: | | | | |
| Within one year | **860,000** | 725,499 | **–** | – |
| In the second year | **60,000** | 90,000 | **–** | – |
| In the third to fifth years, inclusive | **90,000** | 190,000 | **–** | – |
| | **1,010,000** | 1,005,499 | **–** | – |
| Corporate bonds: | | | | |
| Within one year | **3,000,000** | – | **3,000,000** | – |
| In the second year | **–** | 3,000,000 | **–** | 3,000,000 |
| In the third to fifth years, inclusive | **6,000,000** | 6,000,000 | **6,000,000** | 6,000,000 |
| Over five years | **–** | – | **–** | – |
| | **9,000,000** | 9,000,000 | **9,000,000** | 9,000,000 |
| Total bank loans, other loans and corporate bonds | **67,535,794** | 67,642,164 | **48,554,195** | 46,669,348 |
| Less: Portion classified as current liabilities | **(28,137,313)** | (25,482,725) | **(21,383,897)** | (19,093,115) |
| Non-current portion | **39,398,481** | 42,159,439 | **27,170,298** | 27,576,233 |

## 38 INTEREST-BEARING BANK LOANS AND OTHER BORROWINGS (Continued)

Further details of the bank loans, other loans and corporate bonds at the end of the reporting period are as follows:

| Nature | Interest rate and final maturity | Group 2011 RMB'000 | Group 2010 RMB'000 | Company 2011 RMB'000 | Company 2010 RMB'000 |
|---|---|---|---|---|---|
| **RMB denominated loans and corporate bonds:** | | | | | |
| Loans for purchases of aircraft and flight equipment | Floating interest rates ranging from 6.0003% to 8.23% (2010: 5.18% to 7.13%) per annum, with maturities up until 2023 | **5,067,421** | 4,928,816 | **–** | 7,900 |
| Loans for construction in progress | Floating interest rate at 4.86% per annum, with maturities up until 2011 | **–** | 100,000 | **–** | – |
| Loans for working capital | Fixed interest rates ranging from 5.49% to 7.22 % (2010: 4.37% to 8.60%) per annum, with maturities up until 2012 | **582,957** | 1,063,307 | **–** | – |
| Loans for working capital | Floating interest rates from 5.18% to 7.22% (2010: 4.59% to 5.83%) per annum, with maturities up until 2015 | **2,199,482** | 2,688,643 | **–** | – |
| Corporate bonds for purchases of aircraft and flight equipment | Fixed interest rate at 4.50% (2010: 4.50%) per annum, with maturities up until 2015 | **3,000,000** | 3,000,000 | **3,000,000** | 3,000,000 |
| Corporate bonds for working capital | Fixed interest rates ranging from 3.32% to 3.48% (2010: 3.32% to 3.48%) per annum, with maturities up until 2014 | **6,000,000** | 6,000,000 | **6,000,000** | 6,000,000 |
| | | **16,849,860** | 17,780,766 | **9,000,000** | 9,007,900 |

## 38 INTEREST-BEARING BANK LOANS AND OTHER BORROWINGS (Continued)

| Nature | Interest rate and final maturity | Group 2011 RMB'000 | Group 2010 RMB'000 | Company 2011 RMB'000 | Company 2010 RMB'000 |
|---|---|---|---|---|---|
| **United States dollar ("US$") denominated loans:** | | | | | |
| Loans for purchases of aircraft and flight equipment | Fixed interest rates ranging from 3.80% to 8.33% (2010: 3.80% to 8.33%) per annum, with maturities up until 2019 | **372,446** | 921,620 | **372,446** | 921,620 |
| Loans for purchases of aircraft and flight equipment | Floating interest rate at three-month LIBOR+0.50% to three-month LIBOR +4.80% and six-month LIBOR+0.45% to six-month LIBOR+5.50% and twelve-month LIBOR +1.60% (2010: six-month LIBOR+0.50% to six-month LIBOR +3.40% and twelve-month LIBOR +1.60%) per annum, with maturities up until 2023 | **29,877,797** | 19,944,761 | **20,012,107** | 9,694,516 |
| Loans for working capital | Floating interest rates ranging from three-month LIBOR+ 0.50% to six-month LIBOR+2.60% (2010: three-month LIBOR+0.18% to six-month LIBOR+3.00%) per annum, with maturities up until 2014 | **14,808,461** | 22,517,899 | **13,872,755** | 20,993,296 |
| Loans for working capital | Fixed interest rates ranging from 3.61% to 6.24% (2010: 0.85% to 2.44%) per annum, with maturities up until 2012 | **330,343** | 425,102 | **–** | – |
| | | **45,389,047** | 43,809,382 | **34,257,308** | 31,609,432 |

## 38 INTEREST-BEARING BANK LOANS AND OTHER BORROWINGS (Continued)

| Nature | Interest rate and final maturity | Group 2011 RMB'000 | Group 2010 RMB'000 | Company 2011 RMB'000 | Company 2010 RMB'000 |
|---|---|---|---|---|---|
| **Hong Kong dollar denominated loans:** | | | | | |
| Loans for capital investment | Floating interest rates ranging from three-month HIBOR+0.45% to six-month HIBOR+0.85% (2010: three-month HIBOR+0.45% to six-month HIBOR+0.85%) per annum, with maturities up until 2013 | **5,112,274** | 5,845,683 | **5,112,274** | 5,845,683 |
| | | **5,112,274** | 5,845,683 | **5,112,274** | 5,845,683 |
| **Euros denominated loans:** | | | | | |
| Loans for purchase of related equipment | Fixed interest rate at 3.88% (2010: 3.88%) per annum, with maturities up until 2013 | **184,613** | 206,333 | **184,613** | 206,333 |
| | | **184,613** | 206,333 | **184,613** | 206,333 |
| Total bank and other borrowings | | **67,535,794** | 67,642,164 | **48,554,195** | 46,669,348 |
| Less: Portion falling due within one year and classified as current liabilities | | **(28,137,313)** | (25,482,725) | **(21,383,897)** | (19,093,115) |
| Non-current portion | | **39,398,481** | 42,159,439 | **27,170,298** | 27,576,233 |

## 38 INTEREST-BEARING BANK LOANS AND OTHER BORROWINGS (Continued)

The interest rates of RMB denominated loans are set and subject to change by the People's Bank of China.

The Group's bank and other loans of approximately RMB26,590 million as at 31 December 2011 (2010: RMB27,632 million) were secured by:

(a) mortgages over certain of the Group's aircraft and flight equipment, buildings and machinery with an aggregate net carrying amount of approximately RMB37,482 million as at 31 December 2011 (2010: RMB27,575 million) (note 15) and land use rights with an aggregate carrying amount of approximately RMB39.52 million as at 31 December 2011 (2010: RMB40.43 million) (note 16); and

(b) the pledge of certain number of listed shares in an associate of the Group with an aggregate market value of approximately RMB4,312 million as at 31 December 2011 (2010: RMB7,287 million) (note 22); and

(c) guarantees by certain commercial banks amounting to approximately RMB374 million as at 31 December 2011 (2010: RMB1,169 million).

The Company's bank and other loans of approximately RMB9,949 million as at 31 December 2011 (2010: RMB16,696 million) were secured by:

(d) mortgages over certain of the Company's aircraft and buildings with an aggregate net book value of approximately RMB14,304 million as at 31 December 2011 (2010: RMB9,706 million) and land use rights with an aggregate carrying amount of approximately RMB34 million as at 31 December 2011 (2010: RMB35 million); and

(e) guarantees provided by certain commercial banks amounting to approximately RMB374 million as at 31 December 2011 (2010: RMB1,169 million).

As at 31 December 2011, certain PRC state-owned banks provided counter-guarantees in an aggregate amount of approximately RMB275 million (2010: RMB1,012 million) to one of the above-mentioned commercial banks.

## 39 PROVISION FOR MAJOR OVERHAULS

Details of the movements in provision for major overhauls in respect of aircraft and engines under operating leases at the end of the reporting period are as follows:

| | **Group** | | **Company** | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| As at 1 January | **2,608,778** | 1,587,126 | **1,349,927** | 1,232,729 |
| Acquisition of a subsidiary | **–** | 1,205,296 | **–** | – |
| Provision for the year | **1,212,002** | 1,264,117 | **509,995** | 643,476 |
| Utilisation during the year | **(723,988)** | (1,447,761) | **(243,615)** | (526,278) |
| Derecognition of a joint venture | **(11,375)** | – | **–** | – |
| As at 31 December | **3,085,417** | 2,608,778 | **1,616,307** | 1,349,927 |
| Less: Portion classified as current liabilities | **(589,123)** | (503,628) | **(235,964)** | (135,662) |
| Non-current portion | **2,496,294** | 2,105,150 | **1,380,343** | 1,214,265 |

The amount of provision is estimated based on the costs of overhauls and actual flying hours/cycles of aircraft and engines under operating leases. The estimation basis is reviewed on an ongoing basis and revised whenever appropriate.

## 40 LONG TERM PAYABLES

An analysis of long term payables at the end of the reporting period is as follows:

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Customs duties and value-added tax payable in respect of acquisition of aircraft and flight equipment under finance leases | **2,167** | 9,193 | **2,167** | 9,193 |
| Non-voting redeemable preference shares of a subsidiary | **157,417** | 165,229 | **–** | – |
| Others | **86,140** | 119,453 | **–** | – |
| | **245,724** | 293,875 | **2,167** | 9,193 |
| Less: Portion classified as current liabilities *(note 36)* | **(14,663)** | (28,716) | **(1,524)** | (6,817) |
| Non-current portion | **231,061** | 265,159 | **643** | 2,376 |

## 41 DEFERRED INCOME

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Frequent-flyer programme *(note a)* | **2,381,596** | 1,694,147 | **1,669,967** | 1,102,972 |
| Government grant *(note b)* | **970,300** | 1,357,436 | **961,101** | 1,344,735 |
| Gain on sale and leaseback arrangements | **83,382** | 114,659 | **–** | – |
| Operating lease rebates | **23,860** | 29,861 | **–** | – |
| | **3,459,138** | 3,196,103 | **2,631,068** | 2,447,707 |

## 41 DEFERRED INCOME (Continued)

*Notes*

(a) The movements in deferred income related to the Group's frequent-flyer programme during the year are as follows:

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| As at 1 January | **2,117,805** | 947,455 | **1,450,310** | 931,607 |
| Acquisition of a subsidiary | **–** | 491,147 | **–** | – |
| Arising during the year | **1,482,066** | 1,346,633 | **1,166,972** | 1,102,972 |
| Recognised as air traffic revenue during the year | **(907,600)** | (667,430) | **(767,283)** | (584,269) |
| As at 31 December | **2,692,271** | 2,117,805 | **1,849,999** | 1,450,310 |
| Less: Portion classified as current liabilities *(note 36)* | **(310,675)** | (423,658) | **(180,032)** | (347,338) |
| Non-current portion | **2,381,596** | 1,694,147 | **1,669,967** | 1,102,972 |

(b) The movements in deferred income related to government grant during the year are as follows:

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Deferred income: | | | | |
| As at 1 January | **2,284,368** | 2,112,037 | **2,253,357** | 2,107,957 |
| Acquisition of a subsidiary | **–** | 26,931 | **–** | – |
| Addition | **–** | 145,400 | **–** | 145,400 |
| As at 31 December | **2,284,368** | 2,284,368 | **2,253,357** | 2,253,357 |
| Accumulated income recognised: | | | | |
| As at 1 January | **(816,261)** | (687,278) | **(797,951)** | (687,278) |
| Acquisition of a subsidiary | **–** | (11,976) | **–** | – |
| Recognised as other operating revenue during the year *(note 5)* | **(240,486)** | (83,277) | **(236,984)** | (76,943) |
| Recognised as air traffic revenue during the year | **(33,562)** | (33,730) | **(33,562)** | (33,730) |
| As at 31 December | **(1,090,309)** | (816,261) | **(1,068,497)** | (797,951) |
| Net carrying amount | **1,194,059** | 1,468,107 | **1,184,860** | 1,455,406 |
| Less: Portion classified as current liabilities *(note 36)* | **(223,759)** | (110,671) | **(223,759)** | (110,671) |
| Non-current portion | **970,300** | 1,357,436 | **961,101** | 1,344,735 |

## 42 SHARE CAPITAL

The number of shares of the Company and their nominal values as at 31 December 2011 and 31 December 2010 are as follows:

| | **Number of shares 2011** | **Nominal value 2011 *RMB'000*** | Number of shares 2010 | Nominal value 2010 *RMB'000* |
|---|---|---|---|---|
| Registered, issued and fully paid: | | | | |
| H shares of RMB1.00 each: | | | | |
| Tradable | **4,562,683,364** | **4,562,683** | 4,405,683,364 | 4,405,683 |
| Trade-restricted * | **–** | **–** | 157,000,000 | 157,000 |
| A shares of RMB1.00 each: | | | | |
| Tradable | **8,199,737,630** | **8,199,738** | 7,845,678,909 | 7,845,679 |
| Trade-restricted * | **129,533,679** | **129,534** | 483,592,400 | 483,593 |
| | **12,891,954,673** | **12,891,955** | 12,891,954,673 | 12,891,955 |

* The trade-restricted shares were issued on 12 November 2010.

The H shares and A shares rank pari passu, in all material respects, with the state legal person shares and non-H foreign shares of the Company.

## 43 TREASURY SHARES

As at 31 December 2011, the Group owned a 29.99% equity interest in Cathay Pacific, which in turn owned a 19.53% 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.

## 44 RESERVES

### Group

The amounts of the Group's reserves and the movements therein for the current and prior years are presented in the consolidated statement of changes in equity.

### Company

| | Capital reserve *RMB'000* | Reserve funds *RMB'000* | Retained earnings/ (accumulated losses) *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|
| As at I January 2010 | 11,022,878 | 1,554,324 | (506,651) | 12,070,551 |
| Total comprehensive income for the year | (127) | – | 7,412,496 | 7,412,369 |
| Issue of new shares | 5,780,556 | – | – | 5,780,556 |
| Appropriation of statutory reserve fund | – | 614,386 | (614,386) | – |
| As at 31 December 2010 and 1 January 2011 | 16,803,307 | 2,168,710 | 6,291,459 | 25,263,476 |
| Total comprehensive income for the year | – | – | 6,523,066 | 6,523,066 |
| Final dividend declared | – | – | (1,523,829) | (1,523,829) |
| Appropriation of statutory reserve fund | – | 679,126 | (679,126) | – |
| Appropriation of discretionary reserve fund | – | 614,386 | (614,386) | – |
| **As at 31 December 2011** | **16,803,307** | **3,462,222** | **9,997,184** | **30,262,713** |

## 45 SHARE APPRECIATION RIGHTS

The Company has adopted a share appreciation rights ("SARs") 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 general deputy managers of principal branches and subsidiaries as well as selected senior professionals and key specialists. In any event, no more than 200 individuals will be granted SARs.

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 to 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.

## 45 SHARE APPRECIATION RIGHTS (Continued)

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 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 the 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 numbers of SARs exercisable will not exceed 30%, 70% and 100%, respectively, of the total SARs granted to the respective eligible participants.

On 25 August 2009, a board resolution was passed to suspend the Plan and to amend certain terms of the Plan in response to the requirements of related government policies. In 2011, a board resolution was passed to approve the revised "Share Appreciation Rights Management Rules of Air China Limited". On 26 May 2011, a resolution was passed in the annual general meeting of the Company to resume the Plan and to authorize the exercise of 70% of the SARs already vested during a special window period within 60 trading days after the annual general meeting. The exercise price was adjusted to HK$5.70 per share according to the revised Plan. According to the revised plan, the exercise price was adjusted to the fair value at the date of the grant, which was HK$5.97 per Share. While dividends have been declared for three times after the grant date, the exercise price was adjusted to HK$5.70 per share as at 31 December 2011.

Based on a board resolution, the special window period for the exercise of the 70% vested SARs was from 19 July 2011 to 22 July and the date of 25 July. The settlement price of above is HK$7.85 per share. Up to 31 December 2011, 70% of SARs were vested. The total amount has been included and paid with salaries. As at 31 December 2011, all SARs granted which still remained unexercised had an aggregate fair value of RMB1,235,353.

As at the grant date and the subsequent balance sheet date, the fair value of SARs was estimated using the binomial option pricing model considering related vesting conditions and restrictions.

## 46 DISTRIBUTABLE RESERVES

As at 31 December 2011, in accordance with the PRC Company Law, an amount of approximately RMB20,112 million (2010: RMB20,113 million) standing to the credit of the Company's capital reserve account, and an amount of approximately RMB3,462 million (2010: RMB2,169 million) standing to the credit of the Company's reserve funds, as determined in accordance with CASs, were available for distribution by way of a future capitalisation issue. In addition, the Company had retained earnings of approximately RMB9,503 million available for distribution as at 31 December 2011.

## 47 MAJOR NON-CASH TRANSACTIONS

During the year, the Group entered into several finance lease arrangements in respect of property, plant and equipment with a total capital value at the inception of the leases of approximately RMB6,872 million (2010: RMB3,231 million).

## 48 CONTINGENT LIABILITIES

As at 31 December 2011, the Group had the following contingent liabilities:

(a) Pursuant to the restructuring of CNAHC in preparation 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 China National Aviation Corporation (Group) Limited ("CNACG", a wholly-owned subsidiary of CNAHC) on 20 November 2004. According to the Restructuring Agreement, except for liabilities constituting or arising out of or relating to business 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 prior to the restructuring by CNAHC and CNACG. 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 26 February 2007, the Eastern District Court of New York of 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, violated certain anti-trust regulations in respect of their air cargo operations in the United States by acting in concert in imposing excessive surcharges to impede the offering of discounts and allocating revenue and customers so as to increase, maintain and stabilise air cargo prices. 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. The Directors of the Company are also of the view that there would be valid defence against this claim and consider that no provision for this claim is needed accordingly.

(c) 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 mediation 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. The Directors of the Company are also of the view that there would be valid defence against this claim and consider that no provision for this claim is needed accordingly.

(d) In May 2011, Shenzhen Airlines, a subsidiary of the Group, received a summon issued by the Higher People's Court of Guangdong Province in respect of a guarantee provided by Shenzhen Airlines on loans borrowed by Shenzhen Huirun Investment Co., Ltd ("Huirun", a non-controlling shareholder of Shenzhen Airlines) from a third party amounting to RMB390,000,000. It was alleged that Shenzhen Airlines had entered into several guarantee agreements with Huirun and the third party, pursuant to which Shenzhen Airlines acted as a guarantor in favour of the third party for the loans borrowed by Huirun. The proceeding is still in the preliminary stage and therefore the Directors consider that a provision of RMB130,000,000 in respect of this legal claim is adequate. Accordingly a provision of the same amount was made in the consolidated financial statements for the year ended 31 December 2011.

(e) Shenzhen Airlines 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 31 December 2011, Shenzhen Airlines had outstanding guarantees for employees' residential loans amounting to RMB559,992,568 (31 December 2010: RMB281,475,589) and for pilot trainees' tuition loans amounting to RMB341,945,016 (31 December 2010: RMB354,705,922).

## 48 CONTINGENT LIABILITIES (Continued)

(f) Shenzhen Airlines is a co-lessee under certain aircraft operating lease contracts (the "Lease Contracts") entered into by a company invested by Shenzhen Airlines. Under the Lease Contracts, Shenzhen Airlines is obligated to bear the lease payments if the other co-obligor fails to fulfill its obligations. According to the Lease Contracts, the monthly operating lease payment is US$823,147(approximately RMB5,186,565). The Lease Contracts will expire before June 2021.

(g) As at December 2010, the Company provided guarantee in respect of bank loans borrowed by a subsidiary amounting to approximately RMB272 million. There was no such guarantee provided as at 31 December 2011.

## 49 OPERATING LEASE ARRANGEMENTS

### As lessee:

The Group and the Company lease certain office premises, aircraft and flight 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 and the Company had the following future minimum lease payments under non-cancellable operating leases:

| | **Group** | | **Company** | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Within one year | **3,757,269** | 3,743,901 | **2,393,463** | 2,272,501 |
| In the second to fifth years, inclusive | **8,928,590** | 9,952,825 | **4,951,990** | 5,060,039 |
| Over five years | **4,219,950** | 5,423,563 | **2,383,820** | 2,710,510 |
| | **16,905,809** | 19,120,289 | **9,729,273** | 10,043,050 |

Included in the above commitments, the Group had the following minimum lease payments under non-cancellable operating leases towards associates and a related company:

| | **Group** | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Associates | **570,132** | 524,502 |
| Related company | **255** | 255 |

### As lessor:

*Operating lease of investment properties*

The Group leases its investment properties to a third party under operating lease arrangements. The leasing period is from 8 December 2011 to 7 September 2022.

## 50 COMMITMENTS

### (a) Capital commitments

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

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Contracted, but not provided for: | | | | |
| Aircraft and flight equipment | **93,157,457** | 118,639,688 | **76,615,258** | 91,367,627 |
| Buildings | **2,030,556** | 1,765,801 | **1,435,349** | 723,939 |
| Others | **59,052** | 48,369 | **23,369** | 38,639 |
| | **95,247,065** | 120,453,858 | **78,073,976** | 92,130,205 |
| Authorised, but not contracted for: | | | | |
| Aircraft and flight equipment | **–** | – | **–** | – |
| Buildings | **788,805** | 1,443,606 | **645,295** | 1,443,605 |
| Others | **163,224** | 187,963 | **163,224** | 150,463 |
| | **952,029** | 1,631,569 | **808,519** | 1,594,068 |
| Total capital commitments *(note 53)* | **96,199,094** | 122,085,427 | **78,882,495** | 93,724,273 |

Included in the above commitments, the Group had the following amounts of contractual commitments for the acquisition and construction of plant, property and equipment toward an associate and a related company:

| | Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Contracted, but not provided for: | | |
| Associate | **293,000** | 1,208,520 |
| Related company | **1,088,413** | 918,930 |
| | **1,381,413** | 2,217,450 |
| Authorised, but not contracted for: | | |
| Related company | **612,268** | 285,674 |
| | **1,993,681** | 2,413,124 |

### (b) Investment commitment

The Group and the Company had the following amount of investment commitment as at the end of the reporting period:

| | Group | | Company | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Contracted, but not provided for an associate *(note 53)* | **35,000** | 239,000 | **–** | – |

## 51 FINANCIAL INSTRUMENTS BY CATEGORY

The carrying amounts of the Group's and the Company's financial instruments approximated to their fair value as at the end of the reporting period. The present value of bank loans and other borrowings has been calculated by discounting the expected future cash flows at prevailing interest rates. The fair values of long term deposits and other financial assets have been discounted to present value based on market interest rates. Fair value estimates are made at a specific point in time and based on relevant market information about the financial instruments. These estimates are subjective in nature and involve uncertainties and matters of significant judgement and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

The carrying amounts of each of the categories of financial instruments as at the end of the reporting period are as follows:

### Group

**2011**

*Financial assets*

| | Financial assets at fair value through profit or loss and held for trading *RMB'000* | Loans and receivables *RMB'000* | Available-for-sale financial assets *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|
| Due from associates *(note 22)* | – | 16,022 | – | 16,022 |
| Due from related companies | – | 20,194 | – | 20,194 |
| Deposits for aircraft under operating leases | – | 420,854 | – | 420,854 |
| Available-for-sale investments | – | – | 27,182 | 27,182 |
| Accounts and bills receivables | – | 2,702,332 | – | 2,702,332 |
| Financial assets included in deposits and other receivables *(note 29)* | – | 1,235,051 | – | 1,235,051 |
| Financial assets | 12,144 | – | – | 12,144 |
| Due from the ultimate holding company | – | 428,561 | – | 428,561 |
| Pledged deposits | – | 132,565 | – | 132,565 |
| Cash and cash equivalents | – | 15,457,372 | – | 15,457,372 |
| | 12,144 | 20,412,951 | 27,182 | 20,452,277 |

*Financial liabilities*

| | Financial liabilities at fair value through profit or loss and held for trading *RMB'000* | Financial liabilities at amortised cost *RMB'000* | Total *RMB'000* |
|---|---|---|---|
| Due to associates *(note 22)* | – | (134,230) | (134,230) |
| Accounts and bills payables | – | (10,417,186) | (10,417,186) |
| Financial liabilities included in other payables and accruals | – | (10,386,867) | (10,386,867) |
| Financial liabilities | (223,137) | – | (223,137) |
| Due to related companies | – | (190,775) | (190,775) |
| Obligations under finance leases *(note 37)* | – | (21,879,785) | (21,879,785) |
| Interest-bearing bank loans and other borrowings *(note 38)* | – | (67,535,794) | (67,535,794) |
| | (223,137) | (110,544,637) | (110,767,774) |

## 51 FINANCIAL INSTRUMENTS BY CATEGORY (Continued)

### Group

2010

*Financial assets*

| | Financial assets at fair value through profit or loss and held for trading *RMB'000* | Loans and receivables *RMB'000* | Available-for-sale financial assets *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|
| Due from associates *(note 22)* | – | 44,420 | – | 44,420 |
| Due from related companies | – | 3,244 | – | 3,244 |
| Deposits for aircraft under operating leases | – | 391,600 | – | 391,600 |
| Long term receivable from the ultimate holding company | – | 31,813 | – | 31,813 |
| Available-for-sale investments | – | – | 27,182 | 27,182 |
| Accounts and bills receivables | – | 3,106,364 | – | 3,106,364 |
| Financial assets included in deposits and other receivables *(note 29)* | – | 1,104,589 | – | 1,104,589 |
| Financial assets | 27,379 | – | – | 27,379 |
| Due from the ultimate holding company | – | 617,140 | – | 617,140 |
| Pledged deposits | – | 843,065 | – | 843,065 |
| Cash and cash equivalents | – | 14,401,714 | – | 14,401,714 |
| | 27,379 | 20,543,949 | 27,182 | 20,598,510 |

*Financial liabilities*

| | Financial liabilities at fair value through profit or loss and held for trading *RMB'000* | Financial liabilities at amortised cost *RMB'000* | Total *RMB'000* |
|---|---|---|---|
| Due to associates *(note 22)* | – | (128,111) | (128,111) |
| Accounts and bills payables | – | (8,487,799) | (8,487,799) |
| Financial liabilities included in other payables and accruals | – | (7,872,129) | (7,872,129) |
| Financial liabilities | (427,329) | – | (427,329) |
| Due to related companies | – | (181,002) | (181,002) |
| Obligations under finance leases *(note 37)* | – | (18,284,592) | (18,284,592) |
| Interest-bearing bank loans and other borrowings *(note 38)* | – | (67,642,164) | (67,642,164) |
| | (427,329) | (102,595,797) | (103,023,126) |

## 51 FINANCIAL INSTRUMENTS BY CATEGORY (Continued)

### Company

**2011**

*Financial assets*

| | Financial assets at fair value through profit or loss and held for trading *RMB'000* | Loans and receivables *RMB'000* | Available-for-sale financial assets *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|
| Due from subsidiaries *(note 20)* | – | 1,296,115 | – | 1,296,115 |
| Due from associates *(note 22)* | – | 5,652 | – | 5,652 |
| Due from related companies | – | 7,803 | – | 7,803 |
| Deposits for aircraft under operating leases | – | 251,729 | – | 251,729 |
| Available-for-sale investments | – | – | 3,366 | 3,366 |
| Accounts and bills receivables | – | 1,224,596 | – | 1,224,596 |
| Deposits and other receivables *(note 29)* | – | 616,678 | – | 616,678 |
| Due from the ultimate holding company | – | 432,267 | – | 432,267 |
| Cash and cash equivalents | – | 7,797,123 | – | 7,797,123 |
| | – | 11,631,963 | 3,366 | 11,635,329 |

*Financial liabilities*

| | Financial liabilities at fair value through profit or loss and held for trading *RMB'000* | Financial liabilities at amortised cost *RMB'000* | Total *RMB'000* |
|---|---|---|---|
| Due to subsidiaries *(note 20)* | – | (397,288) | (397,288) |
| Due to associates *(note 22)* | – | (57,378) | (57,378) |
| Accounts and bills payables | – | (6,555,427) | (6,555,427) |
| Financial liabilities included in other payables and accruals | – | (5,112,928) | (5,112,928) |
| Financial liabilities | (176,167) | – | (176,167) |
| Due to related companies | – | (170,187) | (170,187) |
| Obligations under finance leases *(note 37)* | – | (20,934,025) | (20,934,025) |
| Interest-bearing bank loans and other borrowings *(note 38)* | – | (48,554,195) | (48,554,195) |
| | (176,167) | (81,781,428) | (81,957,595) |

## 51 FINANCIAL INSTRUMENTS BY CATEGORY (Continued)

### Company

2010

*Financial assets*

| | Financial assets at fair value through profit or loss and held for trading *RMB'000* | Loans and receivables *RMB'000* | Available-for-sale financial assets *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|
| Due from subsidiaries *(note 20)* | – | 617,201 | – | 617,201 |
| Due from associates *(note 22)* | – | 40,448 | – | 40,448 |
| Due from related companies | – | 2 | – | 2 |
| Deposits for aircraft under operating leases | – | 202,668 | – | 202,668 |
| Long term receivable from the ultimate holding company | – | 31,813 | – | 31,813 |
| Available-for-sale investments | – | – | 3,366 | 3,366 |
| Accounts and bills receivables | – | 1,461,627 | – | 1,461,627 |
| Deposits and other receivables *(note 29)* | – | 530,010 | – | 530,010 |
| Due from the ultimate holding company | – | 617,669 | – | 617,669 |
| Cash and cash equivalents | – | 11,501,617 | – | 11,501,617 |
| | – | 15,003,055 | 3,366 | 15,006,421 |

*Financial liabilities*

| | Financial liabilities at fair value through profit or loss and held for trading *RMB'000* | Financial liabilities at amortised cost *RMB'000* | Total *RMB'000* |
|---|---|---|---|
| Due to subsidiaries *(note 20)* | – | (367,364) | (367,364) |
| Due to associates *(note 22)* | – | (30,753) | (30,753) |
| Accounts and bills payables | – | (4,886,489) | (4,886,489) |
| Financial liabilities included in other payables and accruals | – | (3,817,388) | (3,817,388) |
| Financial liabilities | (340,049) | – | (340,049) |
| Due to related companies | – | (159,913) | (159,913) |
| Obligations under finance leases *(note 37)* | – | (17,455,852) | (17,455,852) |
| Interest-bearing bank loans and other borrowings *(note 38)* | – | (46,669,348) | (46,669,348) |
| | (340,049) | (73,387,107) | (73,727,156) |

## 52 FAIR VALUE HIERARCHY

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments:

Level 1: fair values measured based on quoted prices (unadjusted) in active markets for identical assets or liabilities

Level 2: fair values measured based on valuation techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly

Level 3: fair values measured based on valuation techniques for which any inputs which have a significant effect on the recorded fair value are not based on observable market data (unobservable inputs)

As at 31 December 2011, the Group held the following financial instruments measured at fair value:

### Group

Assets measured at fair value as at 31 December 2011:

| | Level 1<br>*RMB'000* | Level 2<br>*RMB'000* | Level 3<br>*RMB'000* | Total<br>*RMB'000* |
|---|---|---|---|---|
| Financial assets | 8,595 | 3,549 | – | 12,144 |

Liabilities measured at fair value as at 31 December 2011:

| | Level 1<br>*RMB'000* | Level 2<br>*RMB'000* | Level 3<br>*RMB'000* | Total<br>*RMB'000* |
|---|---|---|---|---|
| Financial liabilities | – | (223,137) | – | (223,137) |

During the year ended 31 December 2011, there were no transfers of fair value measurements between Level 1 and Level 2 and no transfers into or out of Level 3.

## 53 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's principal financial instruments, other than derivatives, comprise bank loans, other loans and corporate bonds, obligations under finance leases, cash and cash equivalents and pledged deposits. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial assets and liabilities such as accounts receivable and accounts payable, which arise directly from its operations.

The Group also enters into derivative transactions, including principally swaps and collars contracts. The purpose is to manage the jet fuel price risk and interest rate risk arising from the Group's operations.

The Group operates globally and generates revenue in various currencies. The Group's airline operations are exposed to liquidity risk, jet fuel price risk, foreign currency risk, interest rate risk and credit risk. The Group's overall risk management approach is to moderate the effects of such volatility on its financial performance.

## 53 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

Financial risk management policies are periodically reviewed and approved by the Board of Directors and they are summarised below.

### (a) Liquidity risk

The Group's net current liabilities amounted to approximately RMB37,978 million as at 31 December 2011 (2010: RMB29,409 million). The Group recorded a net cash inflow from operating activities of approximately RMB19,670 million for the year ended 31 December 2011 (2010: RMB18,366 million). For the same period, the Group had a net cash outflow from investing activities of approximately RMB21,669 million (2010: RMB14,058 million). The Group also recorded a net cash outflow from financing activities of approximately RMB1,432 million and a net cash inflow of approximately RMB7,463 million for the years ended 31 December 2011 and 2010, respectively. The Group recorded a decrease in cash and cash equivalents of approximately RMB3,593 million and an increase in cash and cash equivalents of approximately RMB11,700 million for the years ended 31 December 2011 and 2010, respectively.

The liquidity of the Group is primarily dependent on its ability to maintain adequate cash inflows from operations to meet its debt obligations as they fall due, and its ability to obtain external financing to meet its committed future capital expenditure. With regard to its future capital commitments and other financing requirements, the Company has already obtained banking facilities with several PRC banks of up to an aggregate amount of RMB141,263 million as at 31 December 2011 (2010: RMB125,071 million), of which an amount of approximately RMB49,902 million was utilised (2010: RMB46,365 million).

The Directors of the Company had carried out a detailed review of the cash flow forecast of the Group for the year ended 31 December 2011. Based on such forecast, the Directors had determined that adequate liquidity existed to finance the working capital and capital expenditure requirements of the Group. In preparing the cash flow forecast, the Directors had considered historical cash requirements of the Group as well as other key factors, including the availability of the above-mentioned loans financing which may impact the operations of the Group. The Directors are of the opinion that the assumptions and sensitivities which are included in the cash flow forecast are reasonable. However, these are subject to inherent limitations and uncertainties and some or all of these assumptions may not be realised.

## 53 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

### (a) Liquidity risk (Continued)

The maturity profile of the Group's financial liabilities as at the end of the reporting period, based on the contractual undiscounted payments, is as follows:

**Group**

| | 2011 | | | | |
|---|---|---|---|---|---|
| | **On demand** *RMB'000* | **Within 1 year** *RMB'000* | **1 to 5 years** *RMB'000* | **Over 5 years** *RMB'000* | **Total** *RMB'000* |
| Due to associates *(note 22)* | – | 134,230 | – | – | 134,230 |
| Accounts and bills payables | 561,563 | 9,855,623 | – | – | 10,417,186 |
| Financial liabilities included in other payables and accruals | 2,955,114 | 7,431,753 | – | – | 10,386,867 |
| Financial liabilities | – | 223,137 | – | – | 223,137 |
| Due to related companies | – | 190,775 | – | – | 190,775 |
| Obligations under finance leases *(note 37)* | – | 2,872,990 | 11,817,226 | 8,153,488 | 22,843,704 |
| Interest-bearing bank loans and other borrowings | – | 28,186,006 | 30,711,850 | 10,939,191 | 69,837,047 |
| Guarantee *(note 48(f))* | 901,938 | – | – | – | 901,938 |
| | 4,418,615 | 48,894,514 | 42,529,076 | 19,092,679 | 114,934,884 |

| | 2010 | | | | |
|---|---|---|---|---|---|
| | On demand *RMB'000* | Within 1 year *RMB'000* | 1 to 5 years *RMB'000* | Over 5 years *RMB'000* | Total *RMB'000* |
| Due to associates *(note 22)* | – | 128,111 | – | – | 128,111 |
| Accounts and bills payables | 510,080 | 7,977,719 | – | – | 8,487,799 |
| Financial liabilities included in other payables and accruals | 1,912,652 | 5,959,477 | – | – | 7,872,129 |
| Financial liabilities | – | 427,329 | – | – | 427,329 |
| Due to related companies | – | 181,002 | – | – | 181,002 |
| Obligations under finance leases *(note 37)* | – | 2,336,913 | 9,449,556 | 7,139,157 | 18,925,626 |
| Interest-bearing bank loans and other borrowings | – | 25,920,416 | 32,766,107 | 11,793,662 | 70,480,185 |
| Guarantee *(note 48(f))* | 636,182 | – | – | – | 636,182 |
| | 3,058,914 | 42,930,967 | 42,215,663 | 18,932,819 | 107,138,363 |

## 53 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

### (a) Liquidity risk (Continued)

The maturity profile of the Company's financial liabilities as at the end of the reporting period, based on the contractual undiscounted payments, is as follows:

**Company**

| | 2011<br>On demand<br>*RMB'000* | Within 1 year<br>*RMB'000* | 1 to 5 years<br>*RMB'000* | Over 5 years<br>*RMB'000* | Total<br>*RMB'000* |
|---|---|---|---|---|---|
| Due to subsidiaries *(note 20)* | – | 397,288 | – | – | 397,288 |
| Due to associates *(note 22)* | – | 57,378 | – | – | 57,378 |
| Account and bills payables | 499,342 | 6,056,085 | – | – | 6,555,427 |
| Financial liabilities included in other payables and accruals | 1,886,227 | 3,226,701 | – | – | 5,112,928 |
| Financial liabilities | – | 176,167 | – | – | 176,167 |
| Due to related companies | – | 170,187 | – | – | 170,187 |
| Obligations under finance leases *(note 37)* | – | 2,629,613 | 11,256,785 | 7,741,847 | 21,628,245 |
| Interest-bearing bank loans and other borrowings | – | 21,722,897 | 22,815,237 | 5,800,869 | 50,339,003 |
| | 2,385,569 | 34,436,316 | 34,072,022 | 13,542,716 | 84,436,623 |

| | 2010<br>On demand<br>*RMB'000* | Within 1 year<br>*RMB'000* | 1 to 5 years<br>*RMB'000* | Over 5 years<br>*RMB'000* | Total<br>*RMB'000* |
|---|---|---|---|---|---|
| Due to subsidiaries *(note 20)* | – | 367,364 | – | – | 367,364 |
| Due to associates *(note 22)* | – | 30,753 | – | – | 30,753 |
| Account and bills payables | 461,383 | 4,425,106 | – | – | 4,886,489 |
| Financial liabilities included in other payables and accruals | 1,098,104 | 2,719,284 | – | – | 3,817,388 |
| Financial liabilities | – | 340,049 | – | – | 340,049 |
| Due to related companies | – | 159,913 | – | – | 159,913 |
| Obligations under finance leases *(note 37)* | – | 2,114,129 | 8,965,753 | 6,809,804 | 17,889,686 |
| Interest-bearing bank loans and other borrowings | – | 19,432,115 | 25,760,155 | 3,038,952 | 48,231,222 |
| Guarantee *(note 48(e))* | 271,797 | – | – | – | 271,797 |
| | 1,831,284 | 29,588,713 | 34,725,908 | 9,848,756 | 75,994,661 |

## 53 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

### (b) Jet fuel price risk

The Group's strategy for managing the risk on jet fuel price aims to provide the Group with protection against sudden and significant increases in prices. In meeting these objectives, the Group allows for the judicious use of approved derivative instruments such as swaps and collars with approved counterparties and within approved limits.

The following table demonstrates the sensitivity at the end of the reporting period to a reasonably possible change in fuel price, with all other variables held constant and excluding the impact of fuel derivative contracts, of the Group's profit before tax for the year:

| | **Change in profit before tax** *RMB'000* |
|---|---|
| **31 December 2011** | |
| If fuel price changes by RMB1,000 per tonne | **4,721,818** |
| 31 December 2010 | |
| If fuel price changes by RMB1,000 per tonne | 4,262,070 |

### (c) Foreign currency risk

The Group's finance lease obligations as well as certain bank and other loans are mainly denominated in United States dollars, and certain expenses of the Group are denominated in currencies other than RMB. The Group generates foreign currency revenue from ticket sales made in overseas offices and normally generates sufficient foreign currencies after payment of foreign currency expenses to meet its foreign currency liabilities repayable within one year.

The following table demonstrates the sensitivity at the end of the reporting period to a reasonably possible change in the US$ exchange rate, with all other variables held constant, of the Group's profit before tax (due to changes in the fair value of monetary assets and liabilities) for the year:

| | **Change in profit before tax** *RMB'000* |
|---|---|
| **31 December 2011** | |
| If RMB changes against US$ by 1% | **620,739** |
| 31 December 2010 | |
| If RMB changes against US$ by 1% | 701,158 |

## 53 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

### (d) Interest rate risk

The Group's exposure to the risk of changes in market interest rates relates primarily to the Group's long term debt obligations with floating interest rates.

The Group's policy is to manage its interest cost using a mix of fixed and variable rate debts. To manage this mix in a cost-effective manner, the Group enters into interest rate swaps, in which the Group agrees to exchange, at specified intervals, the difference between fixed and variable rate interest amounts calculated by reference to an agreed-upon notional principal amount.

The following table sets out the carrying amounts, by maturity, of the Group's financial instruments that are exposed to interest rate risk:

**31 December 2011**

*Fixed rate*

| | Within one year *RMB'000* | In the second year *RMB'000* | In the third to fifth years, inclusive *RMB'000* | Over five years *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|---|
| Obligations under finance leases *(note 37)* | 200,947 | 207,663 | 665,150 | 1,334,037 | 2,407,797 |
| Interest-bearing bank loans and other borrowings *(note 38)* | 4,748,446 | 434,550 | 7,220,407 | 1,795,723 | 14,199,126 |
| Time deposits *(note 33)* | 10,510,051 | – | – | – | 10,510,051 |

*Floating rate*

| | Within one year *RMB'000* | In the second year *RMB'000* | In the third to fifth years, inclusive *RMB'000* | Over five years *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|---|
| Obligations under finance leases *(note 37)* | 2,486,978 | 2,506,332 | 7,899,668 | 6,579,010 | 19,471,988 |
| Interest-bearing bank loans and other borrowings *(note 38)* | 23,388,867 | 9,063,196 | 12,776,440 | 8,108,165 | 53,336,668 |
| Cash at banks *(note 33)* | 5,079,886 | – | – | – | 5,079,886 |

## 53 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

### (d) Interest rate risk (Continued)

31 December 2010

*Fixed rate*

| | Within one year *RMB'000* | In the second year *RMB'000* | In the third to fifth years, inclusive *RMB'000* | Over five years *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|---|
| Obligations under finance leases *(note 37)* | 100,972 | 105,364 | 345,462 | 688,130 | 1,239,928 |
| Interest-bearing bank loans and other borrowings *(note 38)* | 2,032,916 | 3,204,028 | 6,130,350 | 249,067 | 11,616,361 |
| Time deposits *(note 33)* | 11,667,795 | – | – | – | 11,667,795 |

*Floating rate*

| | Within one year *RMB'000* | In the second year *RMB'000* | In the third to fifth years, inclusive *RMB'000* | Over five years *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|---|
| Obligations under finance leases *(note 37)* | 2,122,268 | 2,145,298 | 6,573,197 | 6,203,901 | 17,044,664 |
| Interest-bearing bank loans and other borrowings *(note 38)* | 23,449,809 | 9,748,078 | 12,335,432 | 10,492,484 | 56,025,803 |
| Cash at banks *(note 33)* | 3,576,984 | – | – | – | 3,576,984 |

Interest on financial instruments classified as floating rate is repriced at intervals of less than one year. Interest on financial instruments classified as a fixed rate is fixed until the maturity of the instrument. The other financial instruments of the Group that are not included in the above tables are non-interest-bearing and are therefore not subject to interest rate risk.

The following table demonstrates the sensitivity to a reasonably possible change in interest rate, with all other variables held constant, of the Group's profit before tax (through the impact on floating rate borrowings) for the year.

| | **Change in profit before tax** ***RMB'000*** |
|---|---|
| **31 December 2011** | |
| If interest rate of borrowings changes by 50 basis points | **295,105** |
| 31 December 2010 | |
| If interest rate of borrowings changes by 50 basis points | 301,082 |

## 53 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

### (e) Credit risk

The following table set forth the maximum credit exposure of the Group, within which loans and receivables granted and deposits are placed at carrying amount, net of any impairment losses, and derivatives are at current fair value. For financial guarantees and loan commitments, the maximum exposure represents the maximum amount the Group could be required to pay without consideration of the probability of the actual outcome.

| | **31 December 2011** ***RMB'000*** | 31 December 2010 *RMB'000* |
|---|---|---|
| Due from associates *(note 22)* | **16,022** | 44,420 |
| Deposits for aircraft under operating leases | **420,854** | 391,600 |
| Long term receivable from the ultimate holding company | **–** | 31,813 |
| Available-for-sale investments | **27,182** | 27,182 |
| Accounts and bills receivables | **2,702,332** | 3,106,364 |
| Financial assets included in deposits and other receivables *(note 29)* | **1,235,051** | 1,104,589 |
| Financial assets | **12,144** | 27,379 |
| Due from the ultimate holding company | **428,561** | 617,140 |
| Due from related companies | **20,194** | 3,244 |
| Pledged deposits | **132,565** | 843,065 |
| Cash and cash equivalents | **15,457,372** | 14,401,714 |
| Guarantees *(note 48(f))* | **901,938** | 636,182 |
| Commitments *(note 50)* | **96,234,094** | 122,324,427 |
| Operating lease arrangements *(note 49)* | **16,905,809** | 19,120,289 |
| | **134,494,118** | 162,679,408 |

The above-mentioned financial assets are mainly neither past due nor impaired. Further quantitative data in respect of the Group's exposure to credit risk arising from accounts receivable are disclosed in note 28 to the financial statements.

The Group's cash and cash equivalents are deposited with banks in Mainland China, overseas banks and an associate. The Group has policies in place to limit the exposure to any single financial institution.

A significant portion of the Group's air tickets are sold by agents participating in the Billing and Settlements Plan (the "BSP"), a clearing system between airlines and sales agents organised by the International Air Transportation Association. The balance due from the BSP agents amounted to approximately RMB558 million or 18% of accounts receivable as at 31 December 2011 (2010: RMB882 million or 28% of accounts receivable).

Except for the above, the Group has no significant concentration of credit risk, with the exposure spreading over a number of counterparties.

## 53 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

### (f) Capital management

The primary objectives of the Group's capital management are to safeguard the Group's ability to continue as a going concern and to maintain healthy capital ratios in order to support its business and maximise shareholders' value.

The Group manages its capital structure and makes adjustments to it in light of changes in economic conditions. To maintain or adjust the capital structure, the Group may adjust the dividend payment to shareholders, return capital to shareholders or issue new shares. No changes were made in the objectives, policies or processes for managing capital during the years ended 31 December 2011 and 31 December 2010.

The Group monitors capital structure by reference to the gearing ratio, which represents total liabilities divided by total assets. The gearing ratios as at the end of the reporting periods were as follows:

| | **2011**<br>***RMB'000*** | 2010<br>*RMB'000* |
|---|---|---|
| Total Liabilities | **127,524,637** | 117,398,294 |
| Total assets | **175,850,072** | 158,769,531 |
| Gearing ratio | **72.52%** | 73.94% |

## 54 RELATED PARTY TRANSACTIONS

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

| | Group 2011 RMB'000 | Group 2010 RMB'000 (Restated) |
|---|---|---|
| (a) Included in air traffic revenue | | |
| Sale of cargo space: | | |
| CNAHC Group | **97,292** | 109,287 |
| Joint venture | **750** | 15,348 |
| Associate | **74,373** | 116,128 |
| | **172,415** | 240,763 |
| Government charter flights: | | |
| CNAHC Group | **521,574** | 557,706 |
| | **521,574** | 557,706 |
| (b) Included in other operating revenue | | |
| Equipment lease income: | | |
| CNAHC Group | **–** | 1,050 |
| Joint venture | **1,204** | – |
| Associate | **9,914** | 8,844 |
| | **11,118** | 9,894 |
| Aircraft engineering income: | | |
| Joint venture | **1,095** | 447 |
| Associates | **24,860** | 41,483 |
| | **25,955** | 41,930 |
| Ground service income: | | |
| CNAHC Group | **482** | 520 |
| Joint venture | **161** | 183 |
| Associates | **72,580** | 73,458 |
| | **73,223** | 74,161 |
| Others: | | |
| CNAHC Group | **49,558** | 44,194 |
| Joint venture | **8,004** | 11,776 |
| Associates | **13,752** | 14,067 |
| | **71,314** | 70,037 |

## 54 RELATED PARTY TRANSACTIONS (Continued)

| | Group 2011 RMB'000 | 2010 RMB'000 (Restated) |
|---|---|---|
| (c) Included in finance revenue and finance costs | | |
| Interest income: | | |
| Joint venture | **786** | – |
| Associate | **60,887** | 11,153 |
| | **61,673** | 11,153 |
| Interest expense: | | |
| Associate | **51,802** | 26,070 |
| Entrusted loans commission expenses: | | |
| Associate | **1,275** | – |
| (d) Included in operating expenses | | |
| Airport ground services, take-off, landing and depot expenses: | | |
| CNAHC Group | **554,535** | 553,728 |
| Joint venture | **37,867** | – |
| Associates | **106,396** | 90,707 |
| | **698,798** | 644,435 |
| Air catering charges: | | |
| CNAHC Group | **723,401** | 589,572 |
| Associates | **11,159** | 9,609 |
| | **734,560** | 599,181 |
| Repair and maintenance costs: | | |
| CNAHC Group | **3,348** | 3,075 |
| Joint venture | **855,952** | 778,778 |
| Associates | **17,769** | 675,673 |
| | **877,069** | 1,457,526 |
| Sale commission expenses: | | |
| CNAHC Group | **4,330** | 9,399 |
| Joint venture | **18,665** | 15,366 |
| Associates | **4,361** | 1,922 |
| | **27,356** | 26,687 |
| Management fees: | | |
| CNAHC Group | **7,839** | 8,352 |
| Aircraft and flight equipment leasing fees: | | |
| Associates | **679,770** | 645,242 |
| Others: | | |
| CNAHC Group | **210,306** | 192,160 |
| Joint venture | **1,793** | 1,721 |
| Associates | **35,361** | 20,739 |
| | **247,460** | 214,620 |

## 54 RELATED PARTY TRANSACTIONS (Continued)

| | Group 2011 RMB'000 | Group 2010 RMB'000 (Restated) | Company 2011 RMB'000 | Company 2010 RMB'000 (Restated) |
|---|---|---|---|---|
| (e) Deposits, loans and bills payable: | | | | |
| Deposits placed with an associate *(note 33)* | **3,546,374** | 3,899,659 | **3,546,072** | 3,899,242 |
| Loans from an associate | **1,226,903** | 1,005,499 | **–** | – |
| (f) Entrusted loans to: | | | | |
| Subsidiaries | **–** | – | **2,200,000** | – |
| Joint venture | **25,235** | – | **–** | – |
| (g) Sales of office equipment and motor vehicle to: | | | | |
| Joint venture | **1,536** | – | **–** | – |
| (h) Purchase of aircrafts and engines from: | | | | |
| Associate | **789,415** | 394,485 | **–** | – |
| (i) Other: | | | | |
| Associate | **–** | 19,500 | **–** | – |

| | Group 2011 RMB'000 | Group 2010 RMB'000 | Company 2011 RMB'000 | Company 2010 RMB'000 |
|---|---|---|---|---|
| (j) Outstanding balances with related parties: | | | | |
| Long term receivable from the ultimate holding company | **–** | 31,813 | **–** | 31,813 |
| Due from related companies | **20,194** | 3,244 | **7,803** | 2 |
| Due to related companies | **(190,775)** | (181,002) | **(170,187)** | (159,913) |
| Due from associates *(note 22)* | **16,022** | 44,420 | **5,652** | 40,448 |
| Due to associates *(note 22)* | **(134,230)** | (128,111) | **(57,378)** | (30,753) |
| Due from joint ventures | **34,050** | 64,152 | **–** | – |
| Due to joint ventures | **(235,929)** | (116,711) | **(399,809)** | (156,254) |
| Due from the ultimate holding company | **428,561** | 617,140 | **432,267** | 617,669 |
| Due from subsidiaries *(note 20)* | **–** | – | **1,296,115** | 617,201 |
| Due to subsidiaries *(note 20)* | **–** | – | **(397,288)** | (367,364) |

The long term receivable from CNAHC 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 CNAHC, the outstanding balances with other related parties are unsecured, interest-free and repayable within one year or have no fixed terms of repayment.

## 54 RELATED PARTY TRANSACTIONS (Continued)

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

| | Group 2011 RMB'000 | 2010 RMB'000 |
|---|---|---|
| Compensation of key management personnel: | | |
| Short term employee benefits | **10,667** | 10,462 |
| Post-employment benefits | **776** | 412 |
| Equity-settled share option expense | **(2,202)** | 3,656 |
| | **9,241** | 14,530 |

Further details of the remuneration of the Directors and Supervisors are included in note 9 to the financial statements.

(l) On 25 August 2004, CNACG entered into two licence agreements with CNAC pursuant to which CNACG has agreed to grant licences to CNAC, free of royalty, for the rights to use certain trademarks in Hong Kong and Macau, respectively, so long as CNAC is a direct or indirect subsidiary of CNAHC. No royalty charge was levied in respect for the use of these trademarks during each of the two years ended 31 December 2011 and 2010.

(m) The Company entered into several agreements with CNAHC regarding the use of trademarks granted by the Company to CNAHC; the provision of financial services by CNAF; the provision of construction project management services by China National Aviation Construction and Development Company; the subcontracting of charter flight services to CNAHC; the leasing of properties from and to CNAHC; the provision of air ticketing and cargo services; media and advertising service arrangement to China National Aviation Media and Advertising Co., Ltd.; the tourism services co-operation agreement with CNAHC; the comprehensive services agreement with CNAHC; and the provision of maintenance by China Aircraft Services Limited.

Part of the related party transactions above also constitute connected transactions or continuing connected transactions as defined in Chapter 14A of the Listing Rules.

## 55 COMPARATIVE AMOUNTS

As further explained in note 2 to the financial statements, due to the adoption of IAS 24 (Revised) during the current year, the disclosures of related parties have been revised to comply with the new requirements. Accordingly, certain comparative amounts have been reclassified and restated to conform with the current year presentation.

## 56 APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the Board of Directors on 27 March 2012.

# Consolidated Balance Sheet

31 December 2011
(Prepared under China Accounting Standards for Business Enterprises)

| | **31 December 2011** | 31 December 2010 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| **ASSETS** | | |
| **CURRENT ASSETS** | | |
| Cash and bank balances | **15,420,242** | 15,011,027 |
| Financial assets held for trading | **12,144** | 27,379 |
| Bills receivable | **1,601** | 14,295 |
| Accounts receivable | **2,652,439** | 3,180,638 |
| Other receivables | **1,662,087** | 1,138,695 |
| Prepayments | **584,983** | 683,781 |
| Inventories | **1,128,164** | 932,317 |
| Total current assets | **21,461,660** | 20,988,132 |
| **NON-CURRENT ASSETS** | | |
| Long term receivables | **424,618** | 393,492 |
| Long term equity investments | **14,804,420** | 15,522,585 |
| Investment property | **240,879** | – |
| Fixed assets | **101,737,456** | 88,224,954 |
| Construction in progress | **27,566,439** | 23,518,332 |
| Intangible assets | **2,805,249** | 2,867,600 |
| Goodwill | **1,102,185** | 1,449,030 |
| Long term deferred expenses | **187,893** | 181,317 |
| Deferred tax assets | **2,992,769** | 2,074,171 |
| Total non-current assets | **151,861,908** | 134,231,481 |
| Total assets | **173,323,568** | 155,219,613 |

# Consolidated Balance Sheet

31 December 2011
(Prepared under China Accounting Standards for Business Enterprises)

| | 31 December 2011 RMB'000 | 31 December 2010 RMB'000 |
|---|---|---|
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | |
| **CURRENT LIABILITIES** | | |
| Short term loans | 11,507,317 | 15,703,154 |
| Financial liabilities held for trading | 223,137 | 427,329 |
| Bills payable | – | 387,327 |
| Accounts payable | 12,081,912 | 9,426,483 |
| Domestic air traffic liabilities | 2,052,297 | 1,582,868 |
| International air traffic liabilities | 2,510,478 | 2,025,831 |
| Receipts in advance | 121,503 | 125,088 |
| Employee compensations payable | 2,703,428 | 1,593,762 |
| Taxes payable | 2,756,215 | 2,998,802 |
| Interest payable | 360,578 | 310,029 |
| Other payables | 6,309,825 | 4,630,782 |
| Non-current liabilities repayable within one year | 17,240,694 | 11,421,643 |
| Total current liabilities | 57,867,384 | 50,633,098 |
| **NON-CURRENT LIABILITIES** | | |
| Long term loans | 33,398,481 | 31,923,371 |
| Corporate bonds | 6,000,000 | 9,000,000 |
| Long term payables | 2,643,472 | 2,271,951 |
| Obligations under finance leases | 19,191,860 | 16,061,353 |
| Accrued liabilities | 346,284 | 77,820 |
| Deferred income | 3,161,536 | 2,546,860 |
| Deferred tax liabilities | 1,213,030 | 1,005,840 |
| Total non-current liabilities | 65,954,663 | 62,887,195 |
| Total liabilities | 123,822,047 | 113,520,293 |
| **SHAREHOLDERS' EQUITY** | | |
| Issued capital | 12,891,955 | 12,891,955 |
| Capital reserve | 16,288,523 | 16,245,469 |
| Reserve funds | 3,471,812 | 2,178,300 |
| Retained earnings | 17,134,982 | 12,515,511 |
| Foreign exchange translation reserve | (3,049,254) | (2,178,610) |
| Equity attributable to owners of the parent | 46,738,018 | 41,652,625 |
| Non-controlling interests | 2,763,503 | 46,695 |
| Total shareholders' equity | 49,501,521 | 41,699,320 |
| Total liabilities and shareholders' equity | 173,323,568 | 155,219,613 |

# Consolidated Income Statement

31 December 2011
(Prepared under China Accounting Standards for Business Enterprises)

| | **2011** | 2010 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Revenue from operations | **97,139,111** | 80,962,677 |
| Less: Cost of operations | **76,692,435** | 61,004,800 |
| Business taxes and surcharges | **2,241,459** | 1,607,734 |
| Selling expenses | **6,521,025** | 5,503,427 |
| General and administrative expenses | **3,307,241** | 2,340,040 |
| Finance costs | **(1,549,773)** | (539,525) |
| Impairment losses in assets | **2,146,816** | 2,098,256 |
| Add: Gains from movements in fair value | **33,744** | 1,743,515 |
| Investment income | **1,336,532** | 3,572,863 |
| Including: Share of profits and losses of associates and joint ventures | **1,331,670** | 3,405,574 |
| Profit from operations | **9,150,184** | 14,264,323 |
| Add: Non-operating income | **1,198,749** | 847,901 |
| Less: Non-operating expenses | **227,414** | 87,162 |
| Including: Loss on disposal of non-current assets | **61,470** | 45,801 |
| Profit before tax | **10,121,519** | 15,025,062 |
| Less: Tax | **2,223,910** | 2,570,304 |
| Net profit | **7,897,609** | 12,454,758 |
| Net profit attributable to owners of the parent | **7,476,855** | 12,208,049 |
| Non-controlling interests | **420,754** | 246,709 |
| Earnings per share (RMB) | | |
| Basic and diluted | **0.61** | 1.05 |
| Other comprehensive loss | **(889,223)** | (589,481) |
| Total comprehensive income | **7,008,386** | 11,865,277 |
| Attributable to: | | |
| Owners of the parent | **6,597,673** | 11,620,294 |
| Non-controlling interests | **410,713** | 244,983 |

## EFFECTS OF SIGNIFICANT DIFFERENCES BETWEEN IFRSs AND CASs

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

| | *Notes* | **2011**<br>***RMB'000*** | 2010<br>*RMB'000* |
|---|---|---|---|
| Net profit attributable to owners of the parent under CASs | | **7,476,855** | 12,208,049 |
| Deferred tax | *(i)* | **(17,123)** | 105,613 |
| Differences in value of fixed assets | *(ii)* | **(83,510)** | (387,353) |
| Government grants | *(iii)* | **152,387** | (18,264) |
| Others | | **(446,235)** | 96,959 |
| Net profit attributable to owners of the parent under IFRSs | | **7,082,374** | 12,005,004 |

| | *Notes* | **2011**<br>***RMB'000*** | 2010<br>*RMB'000* |
|---|---|---|---|
| Equity attributable to owners of the parent under CASs | | **46,738,018** | 41,652,625 |
| Deferred tax | *(i)* | **97,490** | 114,613 |
| Differences in value of fixed assets | *(ii)* | **(233,626)** | (150,116) |
| Government grants | *(iii)* | **(283,418)** | (435,805) |
| Unrecognition profit of the disposal of Hong Kong Dragon Airlines | *(iv)* | **139,919** | 139,919 |
| Others | | **(342,584)** | 116,718 |
| Equity attributable to owners of the parent under IFRSs | | **46,115,799** | 41,437,954 |

*Notes:*

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

(ii) The differences in the value of fixed assets mainly consist of the 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 CASs. Under IFRSs, the costs of fixed assets acquired in currencies prior to 1 January 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 assets in the financial statements prepared under CASs and IFRSs; (2) in accordance with the accounting policies under IFRSs, all assets are recorded at historical cost. Therefore, the revaluation surplus or deficit and the related depreciation/amortisation or impairment recorded under CASs 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 CASs and IFRSs. Component accounting was adopted by the Group on a prospective basis under IFRSs in 2005 and under CASs in 2007. Such differences are expected to be eliminated through depreciation or disposal of fixed assets in future.

(iii) Under both CASs and IFRSs, government grants or government subsidies should be debited as government grants/subsidies 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 CASs and IFRSs. Therefore, in the Group's financial statements prepared in accordance with CASs, government grants received were 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 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(s)" | the number of seats available for sale multiplied by the kilometres flown |
| "available freight tonne kilometres" or "AFTK(s)" | the number of tonnes of capacity available for the carriage of cargo and mail multiplied by the kilometres flown |
| "available tonne kilometres" or "ATK(s)" | the number of tonnes of capacity available for the transportation of revenue load (passengers and cargo) multiplied by the kilometres flown |
| "tonne" | a metric ton, equivalent to 2,204.6 pounds |

## TRAFFIC MEASUREMENTS

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

## YIELD MEASUREMENTS

| | |
|---|---|
| "passenger yield" | revenues from passenger operations divided by RPKs |
| "cargo yield" | revenues from cargo operations divided by RFTKs |

## LOAD FACTORS

| | |
|---|---|
| "passenger load factor" | RPKs expressed as a percentage of ASKs |
| "cargo and mail load factor" | RFTKs expressed as a percentage of AFTKs |
| "overall load factor" | RTKs expressed as a percentage of ATKs |

## UTILISATION

| | |
|---|---|
| "block hour(s)" | 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 |

# Definitions

In this annual report, the following expressions shall have the following meanings unless the context requires otherwise:

| | |
|---|---|
| "Air China Cargo" | Air China Cargo Co., Ltd |
| "Air Macau" | Air Macau Company Limited |
| "Articles of Association" | the articles of association of the Company, as amended from time to time |
| "Beijing Airlines" | Beijing Airlines Company Limited |
| "Board" | the board of directors of the Company |
| "CASs" | China Accounting Standards for Business Enterprises |
| "Cathay Pacific" | Cathay Pacific Airways Limited |
| "CNACG" | China National Aviation Corporation (Group) Limited |
| "CNAHC" | China National Aviation Holding Company |
| "CNAMC" | China National Aviation Media and Advertisement Co., Ltd |
| "Company" or "Air China" | 中國國際航空股份有限公司 (Air China Limited), a joint stock limited company incorporated in the PRC with limited liability, whose H shares are listed on the Hong Kong Stock Exchange as its primary listing venue and on the Official List of the UK Listing Authority as its secondary listing venue, and whose A shares are listed on the Shanghai Stock Exchange, and whose principal business is the operation of scheduled airline services |
| "Dalian Airlines" | Dalian Airlines Company Limited |
| "Director(s)" | the director(s) of the Company |
| "Group" | the Company, its subsidiaries and joint ventures |
| "Hong Kong Stock Exchange" | The Stock Exchange of Hong Kong Limited |
| "IASs" | International Accounting Standards |
| "IFRSs" | International Financial Reporting Standards |
| "Kunming Airlines" | Kunming Airlines Company Limited |
| "Listing Rules" | The Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited |
| "Lufthansa" | Deutsche Lufthansa AG |
| "ppts" | percentage points |
| "PRC" | the People's Republic of China |
| "RMB" | Renminbi, the lawful currency of the PRC |
| "SFO" | the Securities and Futures Ordinance (Chapter 571 of the laws of Hong Kong) |
| "Shandong Airlines" | Shandong Airlines Co., Ltd. |
| "Shandong Aviation" | Shandong Aviation Group Co., Ltd. |
| "Shenzhen Airlines" | Shenzhen Airlines Company Limited |
| "Supervisor(s)" | the supervisor(s) of the Company |
| "Tibet Airlines" | Tibet Airlines Company Limited |