1. CORPORATE INFORMATION

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

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

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

On 31 July 2003, the Civil Aviation Administration of China (the "CAAC") approved and granted the qualification as an international airport to Meilan Airport and the permission to change its name from Hainan Meilan Airport to Hainan Meilan International Airport. Meilan Airport thereafter formally qualified as an international airport status and is eligible to operate international routes.

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

The consolidated financial statements of the Company for the period ended 30 June 2003 were authorised for issue in accordance with a resolution of the directors on 28 August 2003.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of preparation

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

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

Basis of consolidation

The consolidated financial statements comprise the financial statements of the Company and its subsidiaries for the period ended 30 June 2003 after the elimination of all material intercompany transactions. Subsidiaries are consolidated from the date on which control is transferred to the Group and cease to be consolidated from the date on which control is transferred out of the Group. DFG and Meilan Travelling have been included in the consolidated financial statements using the purchase method of accounting. Accordingly, the consolidated income statement and consolidated cash flow statement for the period ended 30 June 2002 include the results and cash flows of DFG and Meilan Travelling for the one-month period from their acquisition on 31 May 2002. The purchase consideration has been allocated to the assets and liabilities acquired on the basis of their fair value at the date of acquisition.

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

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Subsidiaries

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

The Company's investments in subsidiaries are stated at cost less any impairment losses.

Property, plant and equipment

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

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

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

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

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

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

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Negative goodwill

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

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

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

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

Land use rights

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

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

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

Impairment of assets

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

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

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

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Impairment of assets (continued)

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

Borrowing costs

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

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

Inventories

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

Revenue recognition

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

(a) airport fees, upon receipt from outbound passengers when departing from the airport;

(b) aeronautical revenues other than airport fees, when the related airport services are rendered;

(c) rental income, on the straight-line basis during the relevant leasing periods;

(d) advertising income, on the straight-line basis during the period of display of the relevant advertisements;

(e) franchise fees, on the straight-line basis during the period of granting the right of operations;

(f) car parking fees, when the parking services are rendered;

(g) management fee income, when the related management services are rendered;

(h) interest income, on a time proportion basis taking into account the principal outstanding and the effective interest rate applicable;

(i) sales of goods, when the significant risks and rewards of ownership of the goods have passed to buyer and the amount of revenue can be measured reliably; and

(j) provision of tourism services, when the services are rendered.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Government grants

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

Related parties

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

Operating leases

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

Foreign currency transactions

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

Tax

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

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

Deferred tax liabilities are recognised for all taxable temporary differences:

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

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

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Tax (continued)

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

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

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

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

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

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

Cash and cash equivalents

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

Accounts receivable, other receivables and amounts due from related parties

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

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

Accounts payable and other payables

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

Interest-bearing loans and borrowings

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

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Provisions

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

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

Retirement benefits

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

Contingencies

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

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

Subsequent events

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

Financial instruments

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

Dividends

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

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments

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

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

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

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

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

3. REVENUES

(a) The total revenues of the period are analysed as follows:

	Note	**Six month period ended 30 June 2003 Audited RMB'000**	Six month period ended 30 June 2002 Unaudited RMB'000
Aeronautical:			
Passenger charges		**35,563**	57,298
Airport fees	(i)	**29,910**	33,175
Ground handling service fees		**8,362**	11,458
Aircraft movement fees and related charges		**16,714**	7,022
Total aeronautical revenues		**90,549**	108,953
Non-aeronautical:			
Leasing of commercial areas, counters and offices in the terminal		**7,979**	12,032
Franchise fees		**12,123**	9,286
Sale of goods		**4,170**	455
Provision of tourism services		**9,889**	853
Provision of advertising services		**2,652**	2,408
Car parking fees		**1,463**	166
Management fee income		**1,068**	—
Other revenue		**3,332**	4,311
Total non-aeronautical revenues		**42,676**	29,511
Total revenues		**133,225**	138,464

(i) The Company is entitled to government grants in respect of 50% of the CAAC Airport Management and Construction Fee received from outbound passengers who depart from the airport. There are no unfulfilled conditions or contingencies attaching to these government grants.

(ii) Pursuant to a bank loan agreement, China Development Bank has floating charges over the Company's revenue (see note 23).

3. REVENUES (continued)

(b) Other income comprises:

	Note	Six month period ended 30 June 2003 Audited RMB'000	Six month period ended 30 June 2002 Unaudited RMB'000
Negative goodwill in excess of the fair value of acquired non monetary assets	14	—	2,528
Amortisation of negative goodwill	14	20	3
Others		49	3
		69	2,534

4. PROFIT FROM OPERATING ACTIVITIES

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

	Six month period ended 30 June 2003 Audited RMB'000	Six month period ended 30 June 2002 Unaudited RMB'000
Cost of goods and services:		
Composite services fee	4,791	5,089
Environmental protection expenses	565	641
Cost for provision of tourism services	3,883	589
Cost of sale of goods	2,232	227
Others	1,411	552
	12,882	7,098
Provision for doubtful debts	—	589
Staff costs, including directors' emoluments	12,178	5,826
Contributions to the retirement scheme	1,417	432
Net foreign exchange differences	72	(1)
Depreciation and amortisation	17,444	14,817
Minimum lease payments under operating leases:		
Buildings	255	585
Gross and net rental income	(7,979)	(12,032)
Auditors' remuneration	1,276	550

5. DIRECTORS', SENIOR EXECUTIVES' AND SUPERVISORS' EMOLUMENTS

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

	Six month period ended 30 June 2003 Audited RMB'000	Six month period ended 30 June 2002 Unaudited RMB'000
Fees	**309**	89
Other emoluments:		
Basic salaries, housing benefits, other allowances and benefits in kind	**148**	80
Bonuses	**73**	37
Retirement benefit contributions	**35**	27

No directors or supervisors waived or agreed to waive any emoluments during either of the six month periods ended 30 June 2003 or 2002.

The five highest paid individuals in the Group during the period ended 30 June 2003 included five directors (for the period ended 30 June 2002: one director). The emoluments for these directors are included in the above disclosures.

The emoluments and designated band of the five highest paid individuals (including directors, supervisors and employees) during the relevant periods are as follows:

	Six month period ended 30 June 2003 Audited RMB'000	Six month period ended 30 June 2002 Unaudited RMB'000
Basic salaries, housing benefits, other allowances and benefits in kind	**134**	137
Bonuses	**66**	45
Retirement benefit contributions	**31**	33
	231	215

The remuneration of each of the executive directors, supervisors and five highest paid employees during each of the six month period ended 30 June 2003 and 2002 fell within the range of nil to HK$1,000,000 (equivalent to RMB1,061,000).

During each of the six month periods ended 30 June 2003 and 2002, no emoluments were paid by the Group to the directors, supervisors or any of the five highest paid individuals as an inducement to join or upon joining the Group or as compensation for loss of office.

6. FINANCE EXPENSES, NET

	Six month period ended 30 June 2003 Audited RMB'000	Six month period ended 30 June 2002 Unaudited RMB'000
Interest on bank loans		
— wholly repayable within five years	**6,995**	6,826
— not wholly repayable within five years	**2,083**	2,438
	9,078	9,264
Interest income	**(3,521)**	(50)
Income from investments	**(205)**	—
	(3,726)	(50)
Interest expense, net	**5,352**	9,214

7. TAX

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

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

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

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

Since Meilan Advertising and DFG had no assessable profits for the six month period ended 30 June 2003 determined in accordance with the PRC accounting regulations, no CIT was provided for.

7. TAX (continued)

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

	Six month period ended 30 June 2003 Audited RMB'000	Six month period ended 30 June 2002 Unaudited RMB'000
Profit from operating activities before income tax	**53,188**	87,571
At PRC preferential corporate income tax rate of 15%	**7,978**	13,136
Expenditure not allowed for deduction	**434**	522
Tax holiday	**(7,985)**	(13,084)
At effective income tax rate of 0.8% (for the period ended 30 June 2002: 0.7%)	**427**	574

Except for bad debt provisions at 30 June 2003 of approximately RMB2,514,000 (as at 31 December 2002: RMB2,514,000) and the unutilised tax losses of Meilan Advertising and DFG attributable to the Group as at 30 June 2003 of approximately RMB174,000 (as at 31 December 2002: RMB42,000) and RMB819,000 (as at 31 December 2002: RMB814,000), respectively, there are no other material deductible temporary differences for which deferred tax assets are not recognised.

Except for as disclosed above, the Group did not have any significant unprovided deferred income tax as at 30 June 2003 and 31 December 2002.

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

Aeronautical revenues	3%
Non-aeronautical revenues	5%

Pursuant to a notice pronounced by the State Tax Bureau of the PRC, the Group is entitled to a business tax holiday in respect of its aeronautical revenue and the provision of tourism services earned during the period from 1 May 2003 to 30 September 2003.

8. RELATED PARTY TRANSACTIONS

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

Continuing transactions

Name of related party	Relationship with the Company	Nature of transaction	Notes	Six month period ended 30 June 2003 Audited RMB'000	Six month period ended 30 June 2002 Unaudited RMB'000
Revenues:					
Haikou Meilan Airport Co., Ltd. (the "Parent Company")	Immediate holding company	Income from franchise fee for the operation of the cargo centre	(vii)	—	3,542
Yangzijiang Air Express Co., Ltd.	Related party	Income from franchise fee for the operation of the cargo centre	(vii)	**9,000**	1,500
DFG	Fellow subsidiary	Rental income for the leasing of office and commercial space	(ii)	—	367**
Meilan Travelling	* Fellow subsidiary	Rental income for the leasing of office and commercial space	(ii)	—	295**
Hainan Airlines Food Co., Ltd. ("Hainan Food")	Related party	Franchise income from catering services	(iv)	**2,190**	2,190
		Rental income for the leasing of storage space	(iv)	**13**	13
China Southern Airlines Co., Ltd. ("China Southern Airlines")	*Shareholder	Income for the provision of customary airport ground service	(v)	**14,176**	20,267
		Rental income for the leasing of office and commercial space	(ii)	**2,702**	2,741
		Income for the provision of advertising services	(vi)	**110**	110
Xia Men Airlines Co., Ltd.	Related party	Income for the provision of customary airport ground services	(v)	**508**	370
Hainan Airlines Co., Ltd. ("Hainan Airlines")	* Shareholder	Income for the provision of customary airport ground services	(v)	**27,817**	23,355
		Rental income for the leasing of office and commercial space	(ii)	**2,916**	2,897
		Income for the provision of advertising services	(vi)	—	425

8. RELATED PARTY TRANSACTIONS (continued)

Name of related party	Relationship with the Company	Nature of transaction	Notes	Six month period ended 30 June 2003 Audited RMB'000	Six month period ended 30 June 2002 Unaudited RMB'000
China Xinhua Airlines Co., Ltd.	Related party	Income for the provision of customary airport ground services	(v)	—	34
Shan Xi Airlines Co., Ltd.	Related party	Income for the provision of customary airport ground services	(v)	—	264
Expenses:					
Haikou Meilan Airport Co., Ltd. (the "Parent Company")	Immediate holding company	Airport composite services charged by the Parent Company	(i)	**(4,791)**	(6,324)
		Rental expense paid for the leasing of office and commercial space	(ii)	**(255)**	(255)
HNA Group Co., Ltd. ("HNA Group")	* Shareholder	Logistic composite services charged by HNA Group	(viii)	**(4,404)**	(2,053)
Copenhagen Airport Development International A/S ("CADI")	Related party	Technical services fee expenses	(iii)	**(4,212)**	—
Sharing of customary airport ground services income:					
Haikou Meilan Airport Co., Ltd. (the "Parent Company")	Immediate holding Company	Sharing of customary airport ground services income by the Parent Company	(ix)	**18,457**	20,079

* A fellow subsidiary represents a subsidiary controlled by the Parent Company, and a shareholder represents an individual or corporate entity holding the shares of the Company directly.

** Amounts represented rental income received from DFG and Meilan Travelling for the period prior to the acquisition of the equity interests of DFG and Meilan Travelling.

Notes:

(i) Airport Composite Services

The Company and the Parent Company entered into an Airport Composite Services Agreement on 31 December 2000. According to the agreement, the Parent Company would continue to provide services for security guards, cleaning and landscaping, power and energy supply, and equipment maintenance to the Company for a fee of 7% of the total revenue, as determined under PRC accounting regulations, of the Company for a period of three years.

The Company and the Parent Company entered into a new Airport Composite Services Agreement on 25 October 2002 ("Revised Airport Composite Services Agreement") to replace the agreement dated 31 December 2000. According to the Revised Airport Composite Services Agreement, the Parent Company has agreed to provide the following services to the Group:

(a) provision of security guard service;

(b) cleaning and landscaping;

8. RELATED PARTY TRANSACTIONS (continued)

(c) sewage and refuse processing;

(d) power and energy supply and equipment maintenance; and

(e) passenger and luggage security inspection.

The charge rates for the above various services are as follows:

- The charges relating to items (a)-(d) above are determined in accordance with the cost to the Parent Company in providing such services plus a 5% mark-up as a management fee, except for item (d), the mark-up of which is 25% pursuant to the relevant pricing guideline set by the CAAC. The charges are settled on an annual basis.

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

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

(ii) Office Lease Agreement

The Company and the Parent Company entered into an Office Lease Agreement dated 31 December 2000, pursuant to which the Company agreed to lease office premises from the Parent Company for a term of two years at an annual rental of RMB905,000. Pursuant to an Office Lease Agreement dated 25 October 2002, which replaced the previous agreement, the Company agreed to rent from the Parent Company office premises for a term of five years at an annual rental of RMB509,000 with effect from 1 January 2002.

The Company leased office and commercial areas and premises and airport counters to DFG, Meilan Travelling, Hainan Airlines and China Southern Airlines; and an aircraft storage warehouse to Hainan Airlines. The relevant lease agreements were made on different dates and the rental charge was agreed between the Company, DFG, Meilan Travelling, Hainan Airlines and China Southern Airlines.

(iii) Pursuant to the Technical Service Agreement dated 16 September 2002 and amended on 30 October 2002 between the Company and CADI, a wholly-owned subsidiary of the strategic investor, CADI has agreed to provide certain technical and consultancy services in respect of the long-term management and development of Meilan Airport. Such services include (but are not limited to) advising on the business development, investment opportunities, infrastructure and capacity planning and international marketing at Meilan Airport.

The Company is required to pay fees to CADI which consist of a fixed fee component and a performance-related component (save that only the fixed fee component is payable for the year 2002). The fixed fee component is calculated by reference to the number of consultant-days used in providing the technical and consultancy services, is based on the rate of US$1,000 per consultant day, and is payable irrespective of operating results. The performance-related component is calculated by reference to the Company's actual earnings before interest, tax, depreciation and amortisation. The Company is also required to pay to CADI the expenses and disbursements incurred by CADI in relation to the technical and advisory services, provided that the expenses and disbursements do not on average per quarter exceed US$200 per consultant-day.

(iv) Catering Service

On 31 December 2000, the Company entered into a Catering Service Agreement with Hainan Airlines Food Co., Ltd. for a term of three years whereby the franchise fee was increased to RMB4,380,000 per annum.

(v) Customary Airport Ground Services

The Company provided customary airport ground services including landing facilities, basic ground handling services, cargo storage and handling, passenger and baggage security check services and other related services to Hainan Airlines, China Xinhua Airlines Co., Ltd., a 51%-owned subsidiary of Hainan Airlines, Shan Xi Airlines Co., Ltd., a 89%-owned subsidiary of Hainan Airlines, China Southern Airlines and Xia Men Airlines Co., Ltd., a 60%-owned subsidiary of China Southern Airlines, at rates prescribed by the CAAC.

(vi) Advertising Services

Meilan Advertising, a subsidiary of the Company, provided advertising services to HNA Group and China Southern Airlines at the normal rates charged to other clients.

8. RELATED PARTY TRANSACTIONS (continued)

(vii) Franchise Fee Income

The Company entered into a contract with the Parent Company for the operation of the cargo centre at Meilan Airport for a fixed annual franchise fee of RMB8,500,000 with effect from 1 January 2001. The contract was terminated on 31 May 2002. The Company entered into a new agreement with Yangzijiang Air Express Co., Ltd., a subsidiary of HNA Group Co., Ltd., pursuant to which Yangzijiang Air Express Co., Ltd. pays a RMB18,000,000 annual franchise fee to the Company for the operation of the cargo centre with the rights to utilise the facilities of the cargo centre with effect from 1 June 2002.

(viii) Logistic Composite Services

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

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

(ix) Sharing of Customary Airport Ground Services Income

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

*Discontinued transactions**

Name of related party	Relationship with the Company	Nature of transaction	Notes	Six month period ended 30 June 2003	Six month period ended 30 June 2002
The Parent Company	Immediate holding company	Acquisition of Acquired Businesses	(i)	—	78,131
		Disposal of excessive assets	(i)	—	28,399
		Purchase of land use rights	(ii)	—	2,698
HNA Group	Shareholder	Income from leasing of office	(iii)	—	372
Hainan Lanyu Air Services Co., Ltd. ("Hainan Lanyu")	* Fellow subsidiary	Income from subcontracting arrangement for the sale of air tickets	(iv)	—	500

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

Notes:

(i) The Company acquired a 95% equity interest in DFG, a 60% equity interest in Meilan Travelling and the carpark operations and cargo handling centre from the Parent Company on 31 May 2002 for an aggregate consideration of RMB78,131,000 which was based on the valuation report prepared by Hainan Zhong Li Xin Asset Valuation Company Limited dated 18 April 2002. The consideration was satisfied by the exchange of the excessive assets owned by the Company in the amount of RMB28,399,000 and by cash consideration of RMB49,732,000.

(ii) The Company acquired land use rights of approximately RMB2,698,000 from the Parent Company for cash in June 2002.

(iii) The Company received RMB844,000 and RMB372,000 from HNA Group, for the leasing of a commercial area in 2001 and for the year ended 31 December 2002, respectively. The rental of the commercial area was agreed between the Company and HNA Group.

8. RELATED PARTY TRANSACTIONS (continued)

Discontinued transactions (continued)*

(iv) Air Ticket Sales Agency

By way of an Operation Agreement dated 24 April 2001 between the Company and Hainan Lanyu Air Services Co., Ltd. ("Hainan Lanyu"), a company in which the Parent Company holds a 95% equity interest, the Company contracted its air ticket sales agency business at Meilan Airport to Hainan Lanyu in consideration of a fixed fee in the sum of RMB1,000,000 payable by the latter on an annual basis, for a term of two years. On 30 August 2002, the Company and Hainan Lanyu renewed the agreement to reduce the consideration to a fixed fee of RMB800,000 per annum with effect from 1 January 2002. During the period ended 30 June 2003, the two parties agreed to rescind the aforesaid agreement with effect from 1 January 2003.

In the opinion of the directors, the above transactions were conducted in the ordinary course of business.

9. PROPOSED INTERIM AND FINAL DIVIDEND

	Six month period ended 30 June 2003 Audited RMB'000	Six month period ended 30 June 2002 Unaudited RMB'000
Proposed interim: RMB 0.027 per share (for the period ended 30 June 2002: Nil)	**12,777**	—

An interim dividend of approximately RMB12,777,000 was declared for the period ended 30 June 2003 by the board of directors of the Company on 28 August 2003. A final dividend of RMB85,650,000 was declared for the year ended 31 December 2002 by the board of directors of the Company on 19 March 2003.

10. EARNINGS PER SHARE

The calculation of earnings per share is based on the Group's profit attributable to shareholders for the period of RMB51,800,000 (for the period ended 30 June 2002: RMB87,317,000) and the weighted average of 473,213,000 shares (period ended 30 June 2002: 250,000,000 shares) of the Company in issue during the period ended 30 June 2003.

No diluted earnings per share amount is presented as no diluting events existed.

11. PENSION SCHEME

The Company and its subsidiaries are required to participate in employee pension schemes operated by the relevant local government authorities in the PRC. The PRC government is responsible for the pension liability to these retired employees. The Group is required to make contributions for employees who are registered as permanent residents in the PRC at a rate of 18% and 16% of the employees salaries after and before 1 July 2002, respectively.

The Group's pension cost contributions for the period ended 30 June 2003 amounted to approximately of RMB1,417,000 (for the period ended 30 June 2002: RMB432,000).

12. PROPERTY, PLANT AND EQUIPMENT, NET

Group

	Assets under construction RMB'000	Buildings and leasehold improvements RMB'000	Machinery and equipment RMB'000	Motor vehicles RMB'000	Office furniture, fixtures and other equipment RMB'000	Total RMB'000
Cost or valuation:						
At 1 January 2003	10,549	561,901	77,720	37,332	13,342	700,844
Additions	21,097	190	73	2,616	1,526	25,502
At 30 June 2003	31,646	562,091	77,793	39,948	14,868	726,346
Analysis of cost or valuation:						
At cost	31,646	1,091	73	3,204	5,512	41,526
At 31 August 2002 valuation	—	561,000	77,720	36,744	9,356	684,820
	31,646	562,091	77,793	39,948	14,868	726,346
Accumulated depreciation:						
At 1 January 2003	—	4,811	2,439	1,950	2,490	11,690
Charge for the period	—	7,366	3,532	3,123	1,557	15,578
At 30 June 2003	—	12,177	5,971	5,073	4,047	27,268
Net book value:						
At 30 June 2003	31,646	549,914	71,822	34,875	10,821	699,078
At 1 January 2003	10,549	557,090	75,281	35,382	10,852	689,154

Company

	Assets under construction RMB'000	Buildings and leasehold improvements RMB'000	Machinery and equipment RMB'000	Motor vehicles RMB'000	Office furniture, fixtures and other equipment RMB'000	Total RMB'000
Cost or valuation:						
At 1 January 2003	10,523	561,901	77,720	36,783	10,133	697,060
Additions	21,097	190	74	2,905	645	24,911
At 30 June 2003	31,620	562,091	77,794	39,688	10,778	721,971
Accumulated depreciation:						
At 1 January 2003	—	4,811	2,439	1,788	1,082	10,120
Charge for the period	—	7,366	3,533	3,107	1,230	15,236
At 30 June 2003	—	12,177	5,972	4,895	2,312	25,356
Net book value:						
At 30 June 2003	31,620	549,914	71,822	34,793	8,466	696,615
At 1 January 2003	10,523	557,090	75,281	34,995	9,051	686,940

12. PROPERTY, PLANT AND EQUIPMENT, NET (continued)

A valuation of the property, plant and equipment of the Group was performed as at 31 August 2002 by Vigers Hong Kong Ltd., independent professional qualified surveyors, for the purpose of the listing of the H shares of the Company on The Stock Exchange of Hong Kong Limited. Except for the valuation of property which was based on a combination of the open market value and depreciated replacement cost, the valuation of the remaining plant and equipment was based on the open market method. The depreciated replacement cost approach considers the cost to reproduce or replace in new condition the property appraised, in accordance with current construction costs for similar property in the locality, less depreciation whether arising from physical, functional or economic causes. The valuer assumed that the buildings and assets under construction will be used for the purposes for which they are presently used and did not consider alternative uses. A net valuation surplus of approximately RMB41,449,000 resulted from the revaluation and was recorded in the Group's financial statements. Additional depreciation on the revaluation surplus was approximately RMB918,000 for the six month period ended 30 June 2003 (for the period ended 30 June 2002: Nil).

In the opinion of directors, there has been no material change to the values of the property, plant and equipment between 31 August 2002 and 30 June 2003.

Had the property, plant and equipment of the Group been carried at historical cost less accumulated depreciation and impairment losses, their carrying amounts would have been approximately RMB559,235,000 and RMB129,244,000, respectively.

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

No interest charges and foreign exchange differences were capitalised to assets under construction during the periods ended 30 June 2003 and 2002.

13. LAND USE RIGHTS

Group and Company

	RMB'000
Cost:	
At 1 January 2003 and 30 June 2003	175,260
Accumulated amortisation:	
At 1 January 2003	3,228
Charge for the period	1,866
At 30 June 2003	5,094
Net book value:	
At 30 June 2003	170,166
At 1 January 2003	172,032

A valuation of the land use rights of the Group was performed as at 31 August 2002 by Vigers Hong Kong Ltd., independent professional qualified surveyors, for the purpose of the listing of the H shares of the Company on The Stock Exchange of Hong Kong Limited. The valuation was based on open market value. A valuation surplus of approximately RMB7,832,000 arose from the revaluation which was not recorded in the Group's financial statements.

13. LAND USE RIGHTS (continued)

Had the land use rights been restated to their valuation amount less accumulated amortisation and impairment losses, then the net carrying amount would have been approximately RMB179,795,000 and would have resulted in additional amortisation charges of approximately RMB83,000 for the six month period ended 30 June 2003 (for the period ended 30 June 2002: Nil).

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

As at 30 June 2003, the legal formalities for the transfer of title of certain of the land use rights acquired from the Parent Company, amounting to RMB94,380,000, were still in progress.

Land use rights with a net book value of RMB50,000,000 as at 30 June 2003 (at 31 December 2002: RMB50,000,000) have been pledged for a long term loan granted by the China Development Bank as described in note 23.

14. INTERESTS IN SUBSIDIARIES

	30 June 2003 Audited RMB'000	31 December 2002 Audited RMB'000
Unlisted shares, at cost	**8,294**	8,294
Amount due to subsidiaries	**(8,231)**	(15,760)
	63	(7,466)

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

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

As at 30 June 2003, the Company had direct and indirect interests in the following subsidiaries:

Name	**Place and date of incorporation**	**Paid-up share/ registered capital** RMB'000	**Percentage of equity interest attributable to the Group**	**Principal activities**
Meilan Advertising* (note (i))	PRC 8 June 1999	1,000	99.75	Provision of advertising services
Meilan Travelling* (note (ii))	PRC 13 November 2001	11,000	60	Provision of tourism services
DFG* (note (ii))	PRC 11 May 1999	1,000	95	Trading of duty-free items

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

14. INTERESTS IN SUBSIDIARIES (continued)

Note:

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

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

With effect from 31 May 2002, the Group acquired a 95% equity interest and a 60% equity interest of DFG and Meilan Travelling, respectively. The purchase consideration for the acquisition was in the form of cash, of approximately RMB7,344,000, which was paid during the period ended 30 June 2002.

The fair values of the acquired identifiable assets and liabilities of DFG and Meilan Travelling were:

	RMB'000
Property, plant and equipment	260
Cash and cash equivalents	6,534
Prepayments, deposits and other receivables	9,997
Accounts receivable	82
Inventories	2,618
Investment cost*	151
	19,642
Accounts payable	(1,260)
Accrued liabilities and other payables	(6,363)
Minority interests	(1,887)
Fair value of net assets	10,132
Negative goodwill arising on acquisition	(2,788)
	7,344
Consideration:	
Settled in cash during the second half of 2002	7,344
Cash outflow on acquisition:	
Cash paid for acquisition	7,344
Net cash acquired (before settlement of purchase cost)	(6,534)
Net cash outflow	810

* The balance represents the 5% equity interests of Meilan Advertising held by DFG. The investment cost is eliminated upon the consolidation of the financial statements of the Group.

Negative goodwill represents the excess of the fair values of the acquired non-monetary assets over the cost of acquisition. The amount of negative goodwill not exceeding the fair values of the acquired identifiable non-monetary assets, amounting to approximately RMB260,000 is amortised as income on a systematic basis over the remaining weighted average useful life of the identifiable acquired depreciable assets of approximately seven years. The amount of negative goodwill in excess of the fair values of the acquired identifiable non-monetary assets amounting to approximately RMB2,528,000 was recognised as income immediately in the period ended 30 June 2002.

14. INTERESTS IN SUBSIDIARIES (continued)

The movement in the balance of negative goodwill during the period was as follows:

Group

	RMB'000
Cost:	
At 1 January 2003 and 30 June 2003	(260)
Accumulated amortisation:	
At 1 January 2003	21
Charge for the period	20
At 30 June 2003	41
Net book value:	
At 30 June 2003	(219)
At 1 January 2003	(239)

15. CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprise cash at banks and in hand. Cash at banks earns interest at floating rates based on daily bank deposit rates. The short term deposits outstanding as at 30 June 2003 matured on 31 July 2003. The fair value of cash and cash equivalents at the balance sheet date was RMB468,319,000 (31 December 2002: RMB703,752,000)

For the purpose of the Consolidated Cash Flow Statement, cash and cash equivalents of the Group comprise the following:

	30 June 2003 Audited RMB'000	31 December 2002 Audited RMB'000
Cash at bank and in hand	**268,319**	703,752
Short term deposits	**200,000**	—
	468,319	703,752

16. SHORT TERM INVESTMENTS

In May 2003, the Company entered into a designated investment agreement with Xiangcai Securities Company Limited, whereby the latter agreed to invest on behalf of the Company an amount of RMB200,000,000 in short term investment portfolios comprising government bonds and other money market securities traded on recognised security exchanges in the PRC. The agreement is for a period of 6 months, from 23 May 2003 to 23 November 2003, and Xiangcai Securities Company Limited has guaranteed the Company a minimum rate of return on the investments of 2.5% per annum.

17. ACCOUNTS RECEIVABLE, NET

Group

	30 June 2003 Audited RMB'000	31 December 2002 Audited RMB'000
Outstanding balances aged:		
Within 90 days	**9,053**	19,019
Between 91 to 180 days	**8,854**	3,645
Between 181 to 365 days	**2,502**	2,777
More than 365 days	**1,242**	1,264
	21,651	26,705
Less: Provision for doubtful debts	**(2,514)**	(2,514)
	19,137	24,191

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

18. INVENTORIES

Group

	30 June 2003 Audited RMB'000	31 December 2002 Audited RMB'000
Finished goods and low value consumables	**2,714**	2,297

Company

	30 June 2003 Audited RMB'000	31 December 2002 Audited RMB'000
Low value consumables	**22**	2

All the carrying amounts were stated at cost.

19. BALANCES WITH RELATED PARTIES

Group

	Notes	**30 June 2003 Audited RMB'000**	31 December 2002 Audited RMB'000
Due from:			
The Parent Company		**1,750**	1,757
HNA Group Co., Ltd.		**309**	1,557
Hainan Airlines Co., Ltd.		**—**	20,061
China Southern Airlines Co., Ltd.		**23,449**	18,058
Hainan Da Lung Enterprise Co., Ltd.	(i)	**20,000**	20,000
Hainan Airlines Construction and Development Co., Ltd.	(ii)	**10,000**	30,000
Hainan Airlines Food Co., Ltd.		**2,053**	4,054
Hainan Airlines Information Systems Co., Ltd.		**—**	24,565
Hainan Lanyu Air Service Co., Ltd.		**64**	1,248
Yangzijiang Air Express Co., Ltd.		**6,815**	7,517
Others		**587**	793
		65,027	129,610
Due to:			
The Parent Company		**6,346**	2,980
Hainan Airlines Co., Ltd.		**2,896**	—
CADI		**4,212**	—
Others		**321**	173
		13,775	3,153

19. BALANCES WITH RELATED PARTIES (continued)

Company

	Notes	30 June 2003 Audited RMB'000	31 December 2002 Audited RMB'000
Due from:			
HNA Group Co., Ltd.		**309**	1,557
Hainan Airlines Co., Ltd.		**—**	20,061
China Southern Airlines Co., Ltd.		**23,449**	18,058
Hainan Da Lung Enterprise Co., Ltd.	(i)	**20,000**	20,000
Hainan Airlines Construction and Development Co., Ltd.	(ii)	**10,000**	30,000
Hainan Airlines Food Co., Ltd.		**2,053**	4,054
Hainan Airlines Information Systems Co., Ltd.		**—**	24,565
Hainan Lanyu Air Service Co., Ltd.		**64**	1,248
Yangzijiang Air Express Co., Ltd.		**6,815**	7,517
Others		**601**	757
		63,291	127,817
Due to:			
The Parent Company		**5,517**	2,126
Hainan Airlines Co., Ltd.		**2,896**	—
CADI		**4,212**	—
Others		**188**	—
		12,813	2,126

Amounts due from/to related parties are unsecured, non-interest bearing and payable on demand. The balances primarily arose from the related party transactions disclosed in note 8.

Notes:

(i) On 10 December 2002, the Company entered into a procurement agreement of RMB20,000,000 with Hainan Da Lung Enterprise Co., Ltd., a subsidiary of the Parent Company, under which Hainan Da Lung Enterprise Co., Ltd. would purchase equipment for the apron of Meilan Airport on behalf of the Company. The Company made full payment to Hainan Da Lung Enterprise Co., Ltd in December 2002 in accordance with contract terms. The balance is guaranteed by the Parent Company.

(ii) On 1 December 2002, the Company entered into a construction agency contract of RMB30,000,000 with Hainan Airlines Construction and Development Co., Ltd, a subsidiary of the HNA Group, for the coordination and the progress payments to be paid on behalf of the Company in respect of the construction of the apron of Meilan Airport. The Company made full payment to Hainan Airlines Construction and Development Co., Ltd. in December 2002 in accordance with the contract terms. In May 2003, the Company entered into a construction contract of RMB36,775,500 with a third party construction company in connection with the aforesaid construction of the apron of Meilan Airport. During the period ended 30 June 2003, Hainan Airlines Construction and Development Co., Ltd. paid RMB20,000,000 on behalf of the Company to the aforesaid third party construction company in consideration for construction work done by the construction company.

20. SHORT TERM BANK LOAN

As at 30 June 2003, the Group and the Company had a short term bank loan granted by China Development Bank amounting to RMB50,000,000 (at 31 December 2002: RMB50,000,000). The loan bears interest at 5.31% (period ended 30 June 2002: 5.85%) per annum and is unsecured. The loan has a maturity date of 9 September 2003.

21. ACCOUNTS PAYABLE

Group

	30 June 2003 Audited RMB'000	31 December 2002 Audited RMB'000
Outstanding balances aged:		
Within 90 days	**560**	1,026
Over 90 days	**1,147**	350
	1,707	1,376

22. AIRPORT FEE PAYABLE

In accordance with the notice issued by the CAAC, from 1 January 2002, the Company is required to collect on behalf of the CAAC a civil airport management and construction fee (the "Airport fee"), subject to certain exemptions, from each outbound passenger (RMB50 per domestic passenger and RMB70 per international passenger) and the Company is also entitled to 50% of the Airport fee collected as Airport fee income ("Airport fee income"). In addition, the Tourism Development Fund (RMB20 per passenger) is also collected together with the Airport fee from each outbound international passenger on behalf of and payable to the PRC government after deducting certain handling charges.

Approval from the CAAC was obtained on 11 September 2002 that effective from 1 January 2002, the Airport fee income received by the Company could be offset against the Airport fee payable.

23. INTEREST BEARING LOANS AND BORROWINGS

Group and the Company

	30 June 2003 Audited RMB'000	31 December 2002 Audited RMB'000
Within one year	**62,000**	14,000
Between one and two years	**—**	50,000
Between two and five years	**110,000**	150,000
Over five years	**18,000**	50,000
Total long term bank loans	**190,000**	264,000
Less: Amounts due within one year included in current liabilities	**62,000**	14,000
	128,000	250,000

RMB62,000,000 of the loan balance (at 31 December 2002: RMB250,000,000) was secured by land use rights of the Company amounting to approximately RMB50,000,000. This loan balance was fully repaid by the Company in July 2003. RMB128,000,000 of the loan balance is secured by a floating charge over the Company's revenue (see note 3). The weighted average interest rate of the loans was 5.76% (for the period ended 30 June 2002: 6.21%).

24. DEFERRED INCOME TAX LIABILITIES

As at 30 June 2003 and 31 December 2002, the Group and the Company recognised a deferred tax liability arising from the cost adjustment in 2000 relating to the appraised value of the land use rights of the Group and the Company which was in excess of the net carrying value. The valuation of the land use rights on which the appraised value was determined was performed by Hainan Asset Valuation Co., and resulted in a non tax-deductible surplus of approximately RMB48,869,000. The Company has a five-year exemption from CIT from 2000 to 2004 and a preferential income tax rate of 7.5% from 2005 to 2009. The deferred tax liability of RMB6,535,000 relating to this temporary difference has been recorded since 2000, after taking into account the impact of the tax preferential scheme, with a corresponding adjustment to the share premium that was recorded to reflect the cost adjustment in respect of the assets contributed by the Parent Company.

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

25. GOVERNMENT GRANTS

The balance represented the grant from Hainan Province Government for the construction of a customs and inspection complex. The grant will be recognised as income on a systematic and rational basis over the useful life of the building. As at 30 June 2003, the building was still under construction. Accordingly, no income has been amortised from the grant for the period ended 30 June 2003.

26. SHARE CAPITAL

	30 June 2003 RMB'000	31 December 2002 RMB'000
Issued and fully paid:		
— 246,300,000 domestic shares of RMB1 each	**246,300**	246,300
— 226,913,000 H shares of RMB1 each	**226,913**	226,913
	473,213	473,213

On 18 November 2002 and 9 December 2002, 198,000,000 newly-issued H shares of the Company, existing State Owned Shares of 3,700,000 shares and an additional 25,213,000 H Shares of RMB1 each, respectively, were offered at a price of HK$3.78 (equivalent to RMB4.01) per share to the public and thereafter traded on The Stock Exchange of Hong Kong Limited. The aggregate net proceeds were approximately HK$749,814,000 (equivalent to RMB795,702,000) after deducting related expenses for the placing and initial public offering, of approximately HK$107,917,000 (equivalent to RMB114,522,000).

The H Shares rank pari passu, in all material respects, with the Domestic Shares of the Company.

The proceeds from the issuance of the H shares are mainly used for the acquisition of facilities for the development of Meilan Airport, of which further details are included in the prospectus issued for the Public Offer and International Placing of the H shares of the Company on 6 November 2002.

As at 31 December 2002, the registered capital of the Company was RMB250,000,000. An increment of the registered capital of the Company from RMB250,000,000 to RMB473,213,000 was approved in the extraordinary general meeting on 24 February 2003.

27. RESERVES

The movements in the reserves of the Group are set out in the consolidated statement of movements in equity on page 15 of the report.

Company

	Notes	Share premium account RMB'000	Revaluation reserve RMB'000	Statutory reserves RMB'000	Retained earnings RMB'000	Proposed dividend RMB'000	Total RMB'000
At 1 January 2002		69,390	—	11,018	31,499	45,000	156,907
Net profit for the period		—	—	—	85,158	—	85,158
At 30 June 2002		69,390	—	11,018	116,657	45,000	242,065
Dividend paid		—	—	—	—	(45,000)	(45,000)
Revaluation of property, plant and equipment — surplus	12	—	41,449	—	—	—	41,449
Related deferred tax liability arising from the revaluation of property, plant and equipment	24	—	(4,968)	—	—	—	(4,968)
Net gains and losses not recognised in the income statement		—	36,481	—	—	—	36,481
Net profit for the period		—	—	—	72,058	—	72,058
Proposed 2002 final dividend	9	—	—	—	(85,650)	85,650	—
Transfer to statutory reserves		—	—	21,446	(21,446)	—	—
Issue of H Shares	26	672,169	—	—	—	—	672,169
Expenses for the placing and initial public offering	26	(114,522)	—	—	—	—	(114,522)
At 31 December 2002		627,037	36,481	32,464	81,619	85,650	863,251
Dividend paid		—	—	—	—	(85,650)	(85,650)
Net profit for the period		—	—	—	53,057	—	53,057
Proposed 2003 interim dividend	9	—	—	—	(12,777)	12,777	—
At 30 June 2003		627,037	36,481	32,464	121,899	12,777	830,658

27. RESERVES (continued)

In accordance with the relevant PRC regulations, the companies now comprising the Group are required to transfer 10% of the year end profit after tax, as determined under the PRC accounting regulations, to the statutory common reserve, until the balance of the fund reaches 50% of the registered capital of that company. Subject to certain restrictions as set out in the relevant PRC regulations, the statutory common reserve may be used to offset against the accumulated losses, if any. Pursuant to the PRC regulations, the companies are required to transfer 5% to 10% of net profit, as determined under the PRC accounting regulations, to the statutory common welfare fund. This fund can only be used to provide staff welfare facilities and other collective benefits to the employees of that company. This fund is non-distributable other than in liquidation. Appropriations to the statutory common reserve and statutory common welfare fund are not required for the interim period ended 30 June 2003.

According to the articles of association of the Company, the amount of reserves available for distribution is the lower of the amount determined under PRC accounting regulations and the amount determined under International Financial Reporting Standards. As at 30 June 2003, the amount of reserves available for distribution was approximately RMB96,960,000 (at 31 December 2002: RMB138,964,000).

28. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

Major non-cash transactions

(i) The Company acquired a 95% equity interest of Haikou Meilan Airport Duty-Free Shop Company Limited (''DFG''), a 60% equity interest of Hainan Meilan Airport Travelling Company Limited (''Meilan Travelling'') and the carpark operations and cargo handling centre (the ''Acquired Businesses'') from Haikou Meilan Airport Company Ltd. (the "Parent Company") on 31 May 2002 for an aggregate consideration of RMB78,131,000. The consideration was based on a valuation report prepared by Hainan Zhong Li Xin Asset Valuation Company Limited dated 18 April 2002 and was satisfied by an exchange of excessive assets owned by the Company in the amount of RMB28,399,000 and by cash consideration of RMB49,732,000. The purchases of the 95% and 60% equity interests of DFG and Meilan Travelling were settled in cash in the amount of RMB264,000 and RMB7,080,000, respectively. The remaining consideration in the amount of RMB70,787,000 was applied for the purchase the property, plant and equipment and land use rights related to the carpark operations and cargo handling centre.

(ii) On 30 April 2003, Hainan Airline Co., Ltd. issued a bill of exchange amounting to RMB50,213,976 with a maturity date of 30 October 2003 to settle the amount due to the Company. The Company discounted this bill of exchange with China Merchants Bank before 30 June 2003 (see note 30).

(iii) As further disclosed in note 19(ii) to the financial statements, during the period ended 30 June 2003, Hainan Airlines Construction and Development Co., Ltd. paid RMB20,000,000 on behalf of the Company to a third party construction company in consideration for construction work done by the construction company.

29. SEGMENT INFORMATION

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

30. COMMITMENTS AND CONTINGENT LIABILITIES

Operating lease arrangements — Group as lessee

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

Group and Company

	30 June 2003 Audited RMB'000	31 December 2002 Audited RMB'000
Within one year	509	509
In the second to fifth years, inclusive	1,274	1,018
	1,783	1,527

Operating lease arrangements — Group as lessor

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

	30 June 2003		31 December 2002	
	Group Audited RMB'000	Company Audited RMB'000	Group Audited RMB'000	Company Audited RMB'000
Within one year	9,768	6,543	20,419	19,098
In the second to fifth years, inclusive	2,640	1,692	4,151	3,042
	12,408	8,235	24,570	22,140

Capital commitments

The capital commitments of the Group and the Company contracted but not provided for were as follows:

Group and Company

	30 June 2003 Audited RMB'000	31 December 2002 Audited RMB'000
Construction for the improvement of the information system in the passenger terminal	—	5,000
Construction for a customs and immigration building for international passengers	—	1,300
Construction of the aprons	16,775	—
	16,775	6,300

30. COMMITMENTS AND CONTINGENT LIABILITIES (continued)

Contingent liabilities

Contingent liabilities in respect of bills discounted at the balance sheet dates were as follows:

Group and Company

	30 June 2003 Audited RMB'000	31 December 2002 Audited RMB'000
Bills discounted with recourse	**50,214**	—

31. FAIR VALUES OF FINANCIAL INSTRUMENTS

As at 30 June 2003, the Group's financial instruments comprise bank loans, cash and short-term deposits. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial instruments such as accounts receivable, amounts due from and due to related parties, other current assets, accounts payable and other payables which arise directly from its operations. The Group also enters into investment transactions, principally available-for-sale and held-to-maturity investments, with the purpose of generating returns through interest income and holding gains.

The carrying amounts of the Group's financial instruments approximated their fair value as at 30 June 2003 because of the short term maturities of these instruments, except for the long term borrowings.

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

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

32. FINANCIAL RISK FACTORS

The Group does not have written risk management policies and guidelines. However, the board of directors meets periodically to analyse and formulate measures to manage the Group's exposure to risks, including principally market risks and changes in interest rates and currency exchange rates. Generally, the Group follows conservative strategies in its risk management. As the Group does not have significant exposure to interest rate and currency exchange rate risk, the Group has not used derivatives or other instruments for hedging purposes. The Group does not hold or issue derivative financial instruments for trading purposes. The main risks arising from the Group's financial instruments are interest rate risk, liquidity risk, foreign currency risk and credit risk, which are set out as follows:

(i) Business risk

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

Furthermore, the five largest customers represented in aggregate approximately 60.1% (for the period ended 30 June 2002: 59.6%) of the aeronautical revenues of the Group for the six month period ended 30 June 2003.

32. FINANCIAL RISK FACTORS (continued)

(ii) Interest rate risk

The interest rate and repayment terms of the bank loans of the Group are disclosed in notes 20 and 23. The interest rate and terms of the held-to-maturity financial assets of the Group are disclosed in note 16 to the financial statements.

(iii) Foreign currency risk

The Group's businesses are principally conducted in RMB, except for the purchase of certain equipment, goods and materials in United States dollars. As at 30 June 2003, all of the Group's assets and liabilities were denominated in RMB except that cash and cash equivalents of approximately RMB19,471,000 (at 31 December 2002: RMB208,270,000) were denominated in Hong Kong dollars. Fluctuation of the exchange rates of RMB against foreign currencies could affect the Group's results of operations.

(iv) Credit risk

The Group's cash and cash equivalents are mainly deposited with major PRC banks.

The carrying amounts of cash and cash equivalents, short-term investments and trade debtors included in the consolidated financial statements represent the Group's maximum exposure to credit risk in relation to its financial assets. With respect to credit risk arising from short-term investments as disclosed in note 16 and note 33 to the financial statements, the Group's exposure to credit risk will arise from the default of Xiangcai Securities Company Limited amounts to a maximum amount of the carrying amount of these investments. No other financial assets carry a significant exposure to credit risk.

33. EVENTS AFTER THE BALANCE SHEET DATE

On 7 July 2003, the Company entered into an additional designated investment agreement with Xiangcai Securities Company Limited, whereby the latter agreed to invest on behalf of the Company a further amount of RMB100,000,000 in short term investment portfolios comprising government bonds and reverse repurchase agreements on government bonds which are traded on recognised security exchanges in the PRC. The agreement was for a period of 6 months, from 7 July 2003 to 7 January 2004. On 8 July 2003, the Company transferred RMB100,000,000 to Xiangcai Securities Company Limited for the aforesaid investment purpose.

On 28 August 2003, the board of directors of the Company proposed an interim dividend of approximately RMB 0.027 per share for the period ended 30 June 2003, totalling approximately RMB12,777,000. Interim dividends are simultaneously proposed and declared, because the Company's memorandum and articles grant the directors authority to declare interim dividends.