

CHINA SOUTHERN AIRLINES CO LTD  
Form 20-F  
April 25, 2014

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, D.C. 20549**

**FORM 20-F**

**..REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

**OR**

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT  
OF 1934**

**For the fiscal year ended December 31, 2013**

**OR**

**..TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE  
ACT OF 1934**

**For the transition period from \_\_\_\_\_ to**

**OR**

**..SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

Date of event requiring this shell company report \_\_\_\_\_

Commission file number 1-14660

(Exact name of Registrant as specified in its charter)

**CHINA SOUTHERN AIRLINES COMPANY LIMITED**

(Translation of Registrant's name into English)

**THE PEOPLE'S REPUBLIC OF CHINA**

(Jurisdiction of incorporation or organization)

**278 JI CHANG ROAD**

**GUANGZHOU, 510405**

**PEOPLE'S REPUBLIC OF CHINA**

(Address of principal executive offices)

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***GUANGZHOU, 510405***

***PEOPLE'S REPUBLIC OF CHINA***

(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
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<i>Ordinary H Shares of par value RMB1.00 per share represented by American Depositary Receipts</i>	<i>New York Stock Exchange</i>
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Securities registered or to be registered pursuant to Section 12(g) of the Act:

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act.

None

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report: 7,022,650,000 A Shares of par value RMB1.00 per share and 2,794,917,000 H Shares of par value RMB1.00 per share.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

☐ Yes ☒ No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

☐ Yes ☒ No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

☒ Yes ☐ No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

☐ Yes ☒ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated  
filer ☒

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP ☐ International Financial Reporting Standards ☒ Other  
as issued by the International Accounting  
Standards Board

If "Other" has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow.

“ Item 17 “ Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

“ Yes þ No

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## FORWARD-LOOKING STATEMENTS

This Annual Report contains forward-looking statements. These statements appear in a number of different places in this Annual Report. A forward-looking statement is usually identified by the use in this Annual Report of certain terminology such as “estimate”, “project”, “expect”, “intend”, “believe”, “plan”, “anticipate”, “may”, or their negatives or other comparable words. Also look for discussions of strategy that involve risks and uncertainties. Forward-looking statements include statements regarding the outlook for our future operations, forecasts of future costs and expenditures, evaluation of market conditions, the outcome of legal proceedings (if any), the adequacy of reserves, or other business plans. You are cautioned that such forward-looking statements are not guarantees and involve risks, assumptions and uncertainties. Our actual results may differ materially from those in the forward-looking statements due to risks facing the Company or due to actual facts differing from the assumptions underlying those forward-looking statements.

Some of these risks and assumptions, in addition to those identified under Item 3, “Key Information - Risk Factors,” include:

- general economic and business conditions in markets where the Company operates, including changes in interest rates;

- the effects of competition on the demand for and price of our services;

- natural phenomena;

- the impact of unusual events on our business and operations;

- actions by government authorities, including changes in government regulations, and changes in the CAAC’s regulatory policies;

- our relationship with China Southern Air Holding Company (the “CSAHC”);

- uncertainties associated with legal proceedings;

- technological development;

- our ability to attract key personnel and attract new talent;
- future decisions by management in response to changing conditions;
- the Company's ability to execute prospective business plans;
- the availability of qualified flight personnel and airport facilities; and
- misjudgments in the course of preparing forward-looking statements.

The Company advises you that these cautionary remarks expressly qualify in their entirety all forward-looking statements attributable to the Company, the Group and persons acting on their behalf.

## INTRODUCTORY NOTE

In this Annual Report, unless the context indicates otherwise, the “Company”, “we”, “us” and “our” means China Southern Airlines Company Limited, a joint stock company incorporated in China on March 25, 1995, the “Group” means the Company and its consolidated subsidiaries, and “CSAHC” means China Southern Air Holding Company, the Company’s parent company which holds a 53.65% interest in the Company as of April 18, 2014.

References to “China” or the “PRC” are to the People’s Republic of China, excluding Hong Kong, Macau and Taiwan. References to “Renminbi” or “RMB” are to the currency of China, references to “U.S. dollars”, “\$” or “US\$” are to the currency of the United States of America (the “U.S.” or “United States”), and reference to “HK\$” is to the currency of Hong Kong. Reference to the “Chinese government” is to the national government of China. References to “Hong Kong” or “Hong Kong SAR” are to the Hong Kong Special Administrative Region of the PRC. References to “Macau” or “Macau SAR” are to the Macau Special Administrative Region of the PRC.

The Company presents its consolidated financial statements in Renminbi. The consolidated financial statements of the Company for the year ended December 31, 2013 (the “Financial Statements”) have been prepared in accordance with all applicable International Financial Reporting Standards (“IFRSs”), which collective term includes all applicable individual IFRSs, International Accounting Standards (“IASs”) and Interpretations issued by the International Accounting Standards Board (the “IASB”).

Solely for the convenience of the readers, this Annual Report contains translations of certain Renminbi amounts into U.S. dollars at the rate of US\$1.00 = RMB6.0969, which is the average of the buying and selling rates as quoted by the People’s Bank of China at the close of business on December 31, 2013. No representation is made that the Renminbi amounts or U.S. dollar amounts included in this Annual Report could have been or could be converted into U.S. dollars or Renminbi, as the case may be, at any particular rate or at all. Any discrepancies in the tables included herein between the amounts listed and the totals are due to rounding.

## GLOSSARY OF AIRLINE INDUSTRY TERMS

In this Annual Report, unless the context indicates otherwise, the following terms have the respective meanings set forth below.

### *Capacity*

“available seat kilometers” or “ASK” the number of seats made available for sale multiplied by the kilometers flown

“available ton kilometers” or “ATK” the tons of capacity available for the transportation of revenue load (passengers and cargo) multiplied by the kilometers flown

### *Traffic*

“cargo ton kilometers” the load in tons multiplied by the kilometers flown

“revenue passenger kilometers” or “RPK” the number of passengers carried multiplied by the kilometers flown

“revenue ton kilometers” or “RTK” the load (passenger and cargo) in tons multiplied by the kilometers flown

“revenue ton kilometers-cargo” revenue freight ton kilometers (RFTK), the load (cargo) in tons multiplied by the kilometers flown

“revenue ton kilometers-passenger” the load (passenger) in tons multiplied by the kilometers flown

“ton” a metric ton, equivalent to 2,204.6 pounds

### *Yield*

“yield per RPK” revenue from passenger operations divided by RPK

“yield per RFTK” revenue from cargo operations divided by RFTK

“yield per RTK” revenue from airline operations (passenger and cargo) divided by RTK

### *Cost*

“operating cost per ATK” operating expenses divided by ATK

### *Load Factors*

“overall load factor” RTK expressed as a percentage of ATK

“passenger load factor” RPK expressed as a percentage of ASK

*Utilization*

“utilization rates” the actual number of flight and taxi hours per aircraft per operating day

*Equipment*

“expendables” aircraft parts that are ordinarily used up and replaced with new parts

“rotables” aircraft parts that are ordinarily repaired and reused

*Others*

“ADR” American Depositary Receipt

“A Shares” Shares issued by the Company to investors in the PRC for subscription in RMB, with par value of RMB1.00 each

“CAAC” Civil Aviation Administration of China

“CAOSC” China Aviation Oil Supplies Company

“CSRC” China Securities Regulatory Commission

“H Shares” Shares issued by the Company, listed on The Stock Exchange of Hong Kong Limited and subscribed for and traded in Hong Kong dollars, with par value of RMB1.00 each

“Nan Lung” Nan Lung Holding Limited (a wholly-owned subsidiary of CSAHC)

“NDRC” National Development and Reform Commission of China

“SA Finance” Southern Airlines Group Finance Company Limited

“SAFE” State Administration of Foreign Exchange of China

“SEC” United States Securities and Exchange Commission

**PART I**

**ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS.**

Not applicable.

**ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE.**

Not applicable.

**ITEM 3. KEY INFORMATION.**

**A. Selected Financial Data.**

The following tables present selected financial data for the five-year period ended December 31, 2013. The selected consolidated income statement data for the three-year period ended December 31, 2011, 2012 and 2013 and selected consolidated statement of financial position data as of December 31, 2012 and 2013 excluding basic and diluted earnings per ADR, are derived from the audited consolidated financial statements of the Company, including the related notes, included elsewhere in this Annual Report. The selected consolidated income statement data for the years ended December 31, 2009 and 2010 and selected consolidated statement of financial position data as of December 31, 2009, 2010 and 2011 are derived from the Company's audited consolidated financial statements that are not included in this Annual Report.

Moreover, the selected financial data should be read in conjunction with our consolidated financial statements together with accompanying notes and "Item 5. Operating and Financial Review and Prospects" which are included elsewhere in this Annual Report. Our consolidated financial statements are prepared and presented in accordance with International Financial Reporting Standards, or IFRSs.



Year ended December 31,  
 2013      2013      2012      2011      2010      2009  
 US\$      RMB      RMB      RMB      RMB      RMB  
 (in million, except per share and per ADR data)

## Consolidated Income Statement Data:

Operating revenue	16,164	98,547	99,514	90,395	76,495	54,802
Operating expenses	(16,120)	(98,280)	(95,877)	(87,063)	(70,689)	(55,355)
Operating profit	248	1,510	5,099	4,353	6,282	1,436
Profit before income tax	571	3,484	4,738	6,930	8,089	428
Profit for the year	451	2,750	3,784	6,090	6,412	524
Profit attributable to:						
Equity shareholders of the Company	326	1,986	2,619	5,110	5,792	327
Non-controlling interests	125	764	1,165	980	620	197
Basic and diluted earnings per share	0.03	0.20	0.27	0.52	0.70	0.05
Basic and diluted earnings per ADR <sup>(1)</sup>	1.66	10.11	13.34	26.02	34.83	2.31

(1) Basic and diluted earnings per share have been computed by dividing profit attributable to equity shareholders of the Company by the weighted average number of shares in issue. Basic and diluted earnings per ADR have been computed as if all of our issued or potential ordinary shares, including domestic shares and H shares, are represented by ADRs during each of the years presented. Each ADR represents 50 shares.

Year ended December 31,  
 2013      2013      2012      2011      2010      2009  
 US\$      RMB      RMB      RMB      RMB      RMB  
 (in million)

## Consolidated Statement of Financial Position Data:

Cash and cash equivalents	1,927	11,748	10,082	9,863	10,404	4,343
Other current assets	1,447	8,825	6,705	9,622	5,455	4,785
Asset classified as held for sale	-	-	-	-	-	529
Property, plant and equipment, net	19,646	119,777	100,040	87,711	80,214	63,673
Total assets	27,097	165,207	142,454	129,412	111,335	94,856
Bank and other loans, including long-term bank and other loans due within one year	3,320	20,242	21,899	18,789	9,324	17,452
Obligations under capital leases due within one year	596	3,636	2,494	1,784	1,654	1,431
Bank and other loans, excluding balance due within one year	6,109	37,246	30,196	29,037	31,876	27,875
Obligations under capital leases, excluding balance due within one year	5,146	31,373	19,371	14,053	12,776	11,887
Total equity	6,963	42,451	39,734	37,777	30,316	13,368
Number of shares (in million)	9,818	9,818	9,818	9,818	9,818	8,003

## Selected Operating Data

The operating data and the profit analysis and comparison for other years below is calculated and disclosed in accordance with the statistical standards, which have been implemented by the Group since January 1, 2001. See “Glossary of Airline Industry Terms” at the front of this Annual Report for definitions of certain terms used herein.

	Year ended December 31,				
	2013	2012	2011	2010	2009
Capacity					
ASK (million)	186,800	169,569	151,064	140,498	123,441
ATK (million)	24,952	23,065	20,795	19,140	15,446
Kilometers flown (thousand)	1,147,070	1,052,495	939,233	872,899	746,133
Hours flown (thousand)	1,829	1,681	1,507	1,392	1,195
Number of landing and take-offs	809,870	757,022	702,264	686,223	616,296
Traffic					
RPK (million)	148,417	135,535	122,344	111,328	93,002
RTK (million)	17,469	16,160	14,461	13,104	10,067
Passengers carried (thousand)	91,791	86,485	80,677	76,456	66,281
Cargo and mail carried (tons)	1,276,350	1,232,000	1,135,000	1,117,000	862,000
Load Factors					
Passenger load factor (RPK/ASK) (%)	79.4	79.9	81.0	79.2	75.3
Overall load factor (RTK/ATK) (%)	70.0	70.1	69.5	68.5	65.2
Yield					
Yield per RPK (RMB)	0.59	0.66	0.67	0.62	0.54
Yield per RFTK (RMB)	1.48	1.59	1.61	1.70	1.63
Yield per RTK (RMB)	5.42	5.95	6.03	5.66	5.26
Fleet					
— Boeing	282	243	223	208	194
— Airbus	253	225	208	191	157
— McDonnell Douglas	-	-	-	12	16
— Others	26	23	13	11	11
Total aircraft in service at period end	561	491	444	422	378
Overall utilization rate (hours per day)	9.6	9.8	9.8	9.6	9.4

### Exchange Rate Information

The following table sets forth certain information concerning exchange rates, based on the noon buying rates in New York City for cable transfers in foreign currencies, as certified for customs purposes by the Federal Reserve Bank of New York (the “Noon Buying Rate”), between Renminbi and U.S. dollars for the five most recent financial years.

Period	Period End	Average (1) (RMB per US\$)	High	Low
Annual Exchange Rate				
2009	6.8259	6.8307	6.8470	6.8176
2010	6.6000	6.7696	6.8330	6.6000

2011	6.2939	6.4630	6.6364	6.2939
2012	6.2301	6.3088	6.3879	6.2221
2013	6.0537	6.1412	6.2213	6.0537

(1) Determined by averaging the rates on the last business day of each month during the relevant period.

The following table sets out the range of high and low exchange rates, based on the Noon Buying Rate, between Renminbi and U.S. dollars, for the following periods.

Period	High	Low
Monthly Exchange Rate		
October 2013	6.1209	6.0815
November 2013	6.0993	6.0903
December 2013	6.0927	6.0537
January 2014	6.0600	6.0402
February 2014	6.1448	6.0591
March 2014	6.2273	6.1183
April 2014 (up to April 18, 2014 )	6.2240	6.1966

B. Capitalization and Indebtedness.

Not applicable.

C.Reasons for the Offer and Use of Proceeds.

Not applicable.

D.Risk Factors.

**Risks Relating to our Business**

***We are indirectly majority owned by the Chinese government, which may exert influence in a manner that may conflict with the interests of holders of ADRs, H Shares and A Shares.***

Major Chinese airlines are wholly- or majority-owned either by the Chinese government or by provincial or municipal governments in China. CSAHC, an entity wholly-owned by the Chinese government, holds and exercises the rights of ownership of 53.65% of the equity of the Company. The interests of the Chinese government in the Company and in other Chinese airlines may conflict with the interests of the holders of the ADRs, H Shares and A Shares. The public policy considerations of the Chinese government in regulating the Chinese commercial aviation industry may also conflict with its indirect ownership interest in the Company. In addition, the Company may accept further capital injection from CSAHC through non-public subscriptions, which may have dilutive impact for other holders of ADRs, H Shares and A Shares.

***Due to high degree of operating leverage and high fixed costs, a decrease in revenues of the Group could result in a disproportionately higher decrease in its profit for the year. The results of the Group's operations are also significantly exposed to fluctuations in foreign exchange rates.***

The airline industry is generally characterized by a high degree of operating leverage. In addition, due to high fixed costs, the expenses relating to the operation of any flight do not vary proportionately with the number of passengers carried, while revenues generated from a flight are directly related to the number of passengers carried and the fare structure of such flight. Accordingly, a decrease in revenues could result in a disproportionately higher decrease in its profit for the year. Moreover, as the Group has substantial obligations denominated in foreign currencies, its results of operations are significantly affected by fluctuations in foreign exchange rates, particularly by fluctuations in the Renminbi-U.S. dollar exchange rate. Our net exchange gain increased by RMB2,636 million, from RMB267 million in 2012 to RMB2,903 million in 2013 mainly attributable to the significant appreciation of Renminbi against U.S. dollar in 2013.

***The Group has significant committed capital expenditures in the next three years, but may face challenges and difficulties as it seeks to maintain liquidity.***

We have a substantial amount of debt, lease and other obligations, and will continue to have a substantial amount of debt, lease and other obligations in the future. As of December 31, 2013, the Group's current liabilities exceeded its current assets by RMB28,640 million. The Group generally maintains sound operating cash flow. However, our substantial indebtedness and other obligations may in the future negatively impact our liquidity. In addition, the Group has significant committed capital expenditures in the next three years, due to aircraft acquisitions. In 2013 and thereafter, the liquidity of the Group is primarily dependent on its ability to maintain adequate cash inflow from operations to meet its debt obligations as they fall due, and its ability to obtain adequate external financing to meet its committed future capital expenditures. If our operating cash flow is materially and adversely affected by factors such as increased competition, a significant decrease in demand for our services, or a significant increase in jet fuel prices, our liquidity would be materially and adversely affected. Moreover, the Group may not be able to meet its debt obligations as they fall due and commit future capital expenditures if certain assumptions about the availability of external financing on acceptable terms are inaccurate. If we are unable to obtain adequate financing for our capital requirements, our liquidity and operations would be materially and adversely affected.

As of December 31, 2013, the Group had banking facilities with several PRC commercial banks for providing loan finance up to approximately RMB166,270 million, of which approximately RMB120,904 million was unutilized. Our directors believe that sufficient financing will be available to the Group in 2014. However there can be no assurance that such loan financing will be available on terms acceptable to the Group or at all.

***CSAHC will continue to be our controlling shareholder, and its interests may conflict with those of the Group. CSAHC and certain of its affiliates will continue to provide certain important services to the Group. Any disruption of the provision of services by CSAHC or its affiliates could affect the Group's operations and financial conditions.***

CSAHC will continue to be the controlling shareholder of the Company. CSAHC and certain of its affiliates will continue to provide certain important services to the Group, including the import and export of aircraft spare parts and other flight equipment, advertising services, provision of air ticket selling services, property management services, leasing of properties and financial services, and repair, overhaul and maintenance services on jet engines. The interests of CSAHC may conflict with those of the Group. In addition, any disruption of the provision of services by CSAHC's affiliates or a default by CSAHC of its obligations owed to the Group could affect the Group's operations and financial conditions. In particular, as part of its cash management system, the Group periodically places certain amount of demand deposits after independent shareholders' approval with SA Finance, a PRC authorized financial institution controlled by CSAHC and an associate of the Company. The Group has taken certain measures to monitor the fund flows between itself and SA Finance and the placement of funds by SA Finance. Such monitoring measures may help to enhance the safety of the Group's deposits with SA Finance. In addition, we have received a letter of undertakings from CSAHC dated March 31, 2009, in which, among other things, CSAHC warranted that the Group's deposits and loans with SA Finance were definitely secure and that SA Finance would continue to operate in strict compliance with the relevant rules and regulations. However, the deposits may be exposed to risks associated with the business of SA Finance over which the Group does not have control. As of December 31, 2012 and 2013, the Group had deposits of RMB2,307 million and RMB2,675 million, respectively, with SA Finance.

***Both international and domestic economic fluctuations and Chinese government's macroeconomic controls affect the demand for air travel, which will in turn cause volatility to the Group's business and results of our operations.***

Both international and domestic economic fluctuations and Chinese macroeconomic controls affect the demand for air travel. For example, the demand for air travel significantly decreased during the past few years as result of the U.S. subprime crisis and European debt crisis. In addition, the continuing global economic slowdown may have a negative effect on the growth rate of the Chinese economy. Chinese macroeconomic controls, taken to counteract such slowdown, such as financing adjustments, credit adjustments, price controls and exchange rate policies, would present unexpected changes to the aviation industry. As a result, the changing economic situation and Chinese macroeconomic controls may cause volatility to the Group's business and results of our operations.

The financial crisis and other global events may reduce consumer spending or cause shifts in spending. A general reduction or shift in discretionary spending can result in decreased demand for leisure and business travel and can also impact the Group's ability to raise fares to counteract increased fuel and labor costs. No assurance can be given that capacity reductions or other steps we may take will be adequate to offset the effects of reduced demand.

***The Group could be adversely affected by an outbreak of a disease or large scale natural disasters that affect travel behavior .***

The outbreak of the H1N1 swine flu in March 2009 has had an adverse impact on the aviation industry globally (including the Group). The spread of the swine flu adversely affected the Group's international routes operations in 2009. Recently, there have been a number of outbreaks of H7N9 bird flu in several provinces in the PRC. A further spread of H7N9 bird flu may have a negative impact on the economic and business activities in China and thereby adversely affect our results of operation. A future outbreak of an infectious disease or any other serious public health concerns in Asia and elsewhere could have a material adverse effect on our business, financial condition and results of operations.

In 2011, a number of large-scale natural disasters occurred globally, such as the nuclear meltdown in Japan caused by earthquakes and subsequent tsunami, the hurricane on the East Coast of the United States, the flooding in Thailand and the typhoon in the Philippines. Disasters such as these can affect the aviation industry and the Group by reducing revenues and impacting travel behavior.

***Lack of adequate documentation for land use rights and ownership of buildings subjects us to challenges and claims by third parties with respect to the Company's use of such land and buildings.***

Although systems for registration and transfer of land use rights and related real property interests in China have been implemented, such systems do not yet comprehensively account for all land and related property interests. The Group leased certain properties and buildings from CSAHC which are located in Guangzhou, Wuhan, Haikou and other PRC cities. However, CSAHC lacks adequate documentation evidencing CSAHC's rights to such land and buildings, and, as a result, the lease agreements between CSAHC and the Company for such land have not been registered with the relevant authorities. As a result, such lease agreements may not be enforceable. Lack of adequate documentation for land use rights and ownership of buildings subjects the Company to challenges and claims by third parties with respect to the Company's use of such land and buildings.



As of the date of this Annual Report, we had been occupying all of the land and buildings described above without challenge or claim by third parties. However, if any challenges to the property ownership or other claims are successful, our operation and business may be materially adversely affected. CSAHC has agreed to indemnify us against any loss or damage caused by or arising from any challenge of, or interference with, the Company's right to use certain land and buildings.

***Any discontinuity or disruption in the direct flight arrangement between Taiwan and Mainland China may negatively affect the Group's results.***

The policy restraint on direct flights between Taiwan and Mainland China has been further loosened in the past few years. As of April 18, 2014, there were 414 cross-Strait direct passenger flights per week. The Company was the first Chinese carrier to operate non-stop flights from Mainland China to Taiwan and as a result has benefited from the operation of such flights. However, given the cross-Strait flight arrangement is subject to the political relationship between Taiwan and Mainland China, any deterioration in such political relationship may cause the discontinuity or disruption in the flight arrangement, and therefore may have a material adverse impact on the Group's results.

***Terrorist attacks or the fear of such attacks, even if not made directly on the airline industry, could adversely affect the Company and the airline industry as a whole. The travel industry continues to face on-going security concerns and cost burdens.***

The aviation industry as a whole has been beset with high-profile terrorist attacks, most notably the attack on September 11, 2001 in the United States. Terrorist attacks could also affect the aviation industry in China. Airlines in China have experienced several incidents of terrorist attacks or threats recently. For example, on March 7, 2008, on a China Southern Airlines flight boarding in Urumqi, crew members discovered a terrorist suspect. On July 14, 2010, a passenger jet en route from Urumqi to Guangzhou was forced to make an emergency landing after receiving an anonymous call claiming there was a bomb on the aircraft. On June 29, 2012, there was an attempted hijacking on a passenger flight operated by Tianjin Airlines between Hotan and Urumqi in China's Xinjiang region. CAAC has enhanced security measures, but the effectiveness of such measures cannot be ascertained. Additional terrorist attacks, even if not made directly on the airline industry, or the fear of or the precautions taken in anticipation of such attacks (including elevated threat warnings or selective cancellation or redirection of flights) could materially and adversely affect the Company and the aviation industry. Potential impacts that terrorist attacks could have on the Company include substantial flight disruption costs caused by grounding of fleet, significant increase in security costs and associated passenger inconvenience, increased insurance costs, substantially higher ticket refunds and significant decrease in traffic measured in revenue passenger kilometers. Additionally, increasingly strict security measures make air travel a hassle in the eyes of some consumers. These factors can have an uncertain impact on the development of the aviation industry.

***We may suffer losses in the event of an accident involving our aircraft or the aircraft of any other airline.***

An accident involving one of our aircraft could require repair or replacement of a damaged aircraft, and result in its consequential temporary or permanent loss from service and/or significant liability to injured passengers and others. Although we believe that we currently maintain liability insurance in amounts and of the types generally consistent with industry practice, the amounts of such coverage may not be adequate to fully cover the costs related to the accident or incident, which could result in harm to our results of operations and financial condition. In addition, any aircraft accident, even if fully insured, could cause a public perception that we are not as safe or reliable as other airlines, which would harm our competitive position and result in a decrease in our operating revenues. Moreover, a major accident involving the aircraft of any of our competitors may cause demand for air travel to decrease in general, which would adversely affect our results of operations and financial condition.

***The Group could be adversely affected by a failure or disruption of our computer, communications or other technology systems.***

The Group is increasingly dependent on technology to operate its business. In particular, to enhance its management of flight operations, the Group launched the computerized flight operations control system in May 1999. The system utilizes advanced computer and telecommunications technology to manage the Group's flights on a centralized, real-time basis. The Group believes that the system will enhance the efficiency of flight schedule, increase the utilization of aircraft and improve the coordination of the Group's aircraft maintenance and ground servicing functions. However, the computer and communications systems on which we rely could be disrupted due to various factors, some of which are beyond our control, including natural disasters, power failures, terrorist attacks, equipment failures, software failures and computer viruses and hackers. The Group has taken certain steps to reduce the risk of some of these potential disruptions. There can be no assurance, however, that the measures we have taken are adequate to prevent or remedy disruptions or failures of those systems. Any substantial or repeated failure of those systems could adversely affect our operations and customer services, result in the loss of important data, loss of revenues, and increased costs, and generally harm our business. Moreover, a failure of certain of our vital systems could limit our ability to operate our flights for an extended period of time, which would have a material adverse effect on our operations and our business.

***We may lose investor confidence in the reliability of our financial statements if we fail to achieve and maintain effective internal control over financial reporting, which in turn could harm our business and negatively impact the trading prices of our ADRs, H Shares or A Shares.***

The United States Securities and Exchange Commission, or the SEC, as required by Section 404 of the Sarbanes-Oxley Act of 2002, adopted rules requiring every public company in the United States to include a management report on such company's internal control over financial reporting in its annual report, which contains management's assessment of the effectiveness of the company's internal control over financial reporting. In addition, the Company's independent registered public accounting firm is required to report on the effectiveness of the Company's internal control over financial reporting.

Since 2011, pursuant to the Basic Standard for Enterprise Internal Control jointly issued by the Ministry of Finance, China Securities Regulatory Commission ("CSRC") and other three PRC authorities on May 22, 2008, and its application guidelines and other relevant regulations issued subsequently (collectively, "PRC internal control requirements"), the Company has carried out a self-assessment of the effectiveness of its internal control and issue a self-assessment report annually in accordance with the PRC internal control requirements, and the Company's auditor for its PRC GAAP financial statements (the "PRC Auditor") is required to report on the effectiveness of the Company's internal control over financial reporting.

However, our independent registered public accounting firm or PRC Auditor may not be satisfied with our internal controls, the level at which our controls are documented, designed, operated and reviewed. Our independent registered public accounting firm or PRC Auditor may also interpret the requirements, rules and regulations differently, and reach a different conclusion regarding the effectiveness of our internal control over financial reporting. Although our management have concluded that our internal control over financial reporting as of December 31, 2013 was effective, we may discover deficiencies in the course of our future evaluation of our internal control over financial reporting and may be unable to remediate such deficiencies in a timely manner. If we fail to maintain the adequacy of our internal control over financial reporting, we may not be able to conclude that we have effective internal control over financial reporting on an ongoing basis, as required under the above mentioned rules and regulations. Moreover, effective internal control is necessary for us to produce reliable financial reports and is important to prevent fraud. As a result, our failure to achieve and maintain effective internal control over financial reporting could result in the loss of investor confidence in the reliability of our financial statements, which in turn could harm our business and negatively impact the trading prices of our ADRs, H Shares or A Shares.

***The Company could be classified as a passive foreign investment company by the United States Internal Revenue Service and may therefore be subject to adverse tax impact.***

Depending upon the relative values of our passive assets and income as compared to our total assets and income each taxable year, we could be classified as a passive foreign investment company, or PFIC, by the United States Internal

Revenue Service, or IRS, for U.S. federal income tax purposes. The Company believes that it was not a PFIC for the taxable year 2013. However, there can be no assurance that we will not be a PFIC for the taxable year 2014 and/or later taxable years, as PFIC status is re-tested each year and depends on the facts in such year.

The Company will be classified as a PFIC in any taxable year if either: (1) the average value during the taxable year of its assets that produce passive income, or are held for the production of passive income, is at least 50% of the average value of its total assets for such taxable year (the “Asset Test”) or (2) 75% or more of its gross income for the taxable year is passive income (such as certain dividends, interest or royalties) (the “Income Test”). For purposes of the Asset Test: (1) any cash, cash equivalents, and cash invested in short-term, interest bearing, debt instruments, or bank deposits that is readily convertible into cash, will generally count as producing passive income or as being held for the production of passive income and (2) the average values of the Company’s passive and total assets is calculated based on its market capitalization.

If we were a PFIC, you would generally be subject to additional taxes and interest charges on certain “excess distributions” the Company makes regardless of whether we continue to be a PFIC in the year in which you receive an “excess distribution”. An “excess distribution” would be either (1) the excess amount of a distribution with respect to ADRs during a taxable year in which distributions to you exceed 125% of the average annual distributions to you over the preceding three taxable years or, if shorter, your holding period for the ADRs, or (2) 100% of the gain from the disposition of ADRs. For more information on the United States federal income tax consequences to you that would result from our classification as a PFIC, please see Item 10, “Taxation — United States Federal Income Taxation — U.S. Holders — Passive Foreign Investment Company”.

***We may be unable to retain key management personnel.***

We are dependent on the experience and industry knowledge of our key management employees, and there can be no assurance that we will be able to retain them. Any inability to retain our key management employees, or attract and retain additional qualified management employees, could have a negative impact on us.

### **Risks Relating to the Chinese Commercial Aviation Industry**

***The Group's business is subject to extensive government regulations, and there can be no assurance as to the equal treatment of all airlines under those regulations.***

The Group's ability to implement its business strategy will continue to be affected by regulations and policies issued or implemented by relevant government agencies, particularly CAAC, which encompasses substantially all aspects of the Chinese commercial aviation industry, such as the approval of route allocation, the administration of certain airport operations and air traffic control. Such regulations and policies limit the flexibility of the Group to respond to market conditions, competition or changes in the Group's cost structure. The implementation of specific government policies could from time to time adversely affect the Group's operations.

***The Group's results may be negatively impacted by the fluctuation in domestic prices for jet fuel, and we would be adversely affected by disruptions in the supply of fuel.***

The availability and cost of jet fuel have a significant impact on the Group's results of operations. The Group's jet fuel cost for 2013 accounted for 65.8% of its flight operations expenses. All of the domestic jet fuel requirements of Chinese airlines (other than at the Shenzhen, Zhuhai, Sanya, Haikou, Shanghai Pudong and other small airports) must be purchased from the exclusive providers, CAOSC and Bluesky Oil Supplies Company, which are supervised by the CAAC. Chinese airlines may also purchase jet fuel at the Shenzhen, Zhuhai, Sanya, Haikou, Shanghai Pudong and other small airports from joint ventures in which the CAOSC is a partner. Jet fuel obtained from the CAOSC's regional branches is purchased at uniform prices throughout China that are determined and adjusted by the CAOSC from time to time with the approval of the CAAC and the pricing department of the NDRC based on market conditions and other factors. As a result, the costs of transportation and storage of jet fuel in all regions of China are spread among all domestic airlines.

Domestic price for jet fuel has experienced fluctuations in the past few years. The Group's profit for the year may suffer from an unexpected change in the fuel surcharge collection policies and other factors beyond our control. For

more information on the jet fuel prices, please see “Item 4, Information on the Company - Business Overview - Jet Fuel” section below for further discussion.

In summary, given the constant fluctuation of volatile fuel price, no assurance can be given that the Group’s operation and financial results will not be negatively impacted by the fluctuation in domestic prices for jet fuel.

In addition, China has experienced jet fuel shortages. On some rare occasions prior to 1993, the Group had to delay or even cancel flights. Although such shortages have not materially affected the Group’s operations since 1993, there can be no assurance that such a shortage will not occur in the future. If such a shortage occurs in the future to the extent that the Group has to delay or cancel flights due to fuel shortage, its operational reputation among passengers as well as its operations may suffer.

In 2013, a reasonable possible increase or decrease of 10% in jet fuel price with volume of fuel consumed and all other variables held constant, would have increased or decreased the Group’s annual fuel costs by approximately RMB3,554 million. Accordingly, even if the jet fuel supply remains stable, increases in jet fuel prices will nevertheless adversely impact our financial results.

***The Group’s profit for the year may suffer from an unexpected volatility caused by any fluctuation in the level of fuel surcharges.***

The level of fuel surcharges, which is regulated by Chinese government, affects domestic customers’ air travel demand as well as the Group’s ability to generate profits. On January 14, 2009, the NDRC and the CAAC jointly announced the collection of passenger fuel surcharge for domestic routes should be suspended from January 15, 2009 onwards. Subsequently, in response to the increase in international fuel prices, the NDRC and CAAC issued a notice on November 11, 2009 to introduce a new pricing mechanism of fuel surcharge that links it with airlines’ jet fuel costs, which was further adjusted subsequently. We cannot guarantee that fuel surcharges would not be adjusted further in the future or adjusted in our favor. If fuel surcharges are not adjusted in correspondence to the increase in jet fuel, our profit for the year may be materially adversely affected.

***The Group's results of operations are subject to seasonality.***

The Group's operating revenue is substantially dependent on the passenger and cargo traffic volume carried, which is subject to seasonal and other changes in traffic patterns, the availability of appropriate time slots for the Group's flights and alternative routes, the degree of competition from other airlines and alternate means of transportation, as well as other factors that may influence passenger travel demand and cargo and mail volume. In particular, the Group's airline revenue is generally higher in the second and third quarters than in the first and fourth quarters. As a result, the Group's results may fluctuate from season to season.

***The Group's operations may be adversely affected by insufficient aviation infrastructure in Chinese commercial aviation industry.***

The rapid increase in air traffic volume in China in recent years has put pressure on many components of the Chinese commercial aviation industry, including China's air traffic control system, the availability of qualified flight personnel and airport facilities. Airlines, such as the Group, which have route networks that emphasize short- to medium-haul routes, are generally more affected by insufficient aviation infrastructure in terms of on-time performance and high operating costs due to fuel inefficiencies resulting from the relatively short segments flown, as well as the relatively high proportion of time on the ground during turnaround. All of these factors may adversely affect the perception of the service provided by an airline and, consequently, the airline's operating results. In recent years, the CAAC has placed increasing emphasis on the safety of Chinese airline operations and has implemented measures aimed at improving the safety record of the industry. The ability of the Group to increase utilization rates and to provide safe and efficient air transportation in the future will depend in part on factors such as the improvement of national air traffic control and navigation systems and ground control operations at Chinese airports, factors which are beyond the control of the Group.

***The Group faces increasingly intense competition both in domestic aviation industry and in the international market, as well as from alternative means of transportation.***

The CAAC's extensive regulation of the Chinese commercial aviation industry has had the effect of managing competition among Chinese airlines. Nevertheless, competition has become increasingly intense in recent years due to a number of factors, including relaxation of certain regulations by the CAAC and an increase in the capacity, routes and flights of Chinese airlines. Competition in the Chinese commercial aviation industry has led to widespread price-cutting practices that do not in all respects comply with applicable regulations. Until the interpretation of CAAC regulations limiting such price-cutting has been finalized and strictly enforced, discounted tickets from competitors will continue to have an adverse effect on the Group's sales.

The Group faces varying degrees of competition on its regional routes from certain Chinese airlines and Cathay Pacific Airways, Dragonair and Air Macau, and on its international routes, primarily from non-Chinese airlines, most of which have significantly longer operating histories, substantially greater financial and technological resources and greater name recognition than the Group. In addition, the public's perception of the safety and service records of Chinese airlines could adversely affect the Group's ability to compete against its regional and international competitors. Many of the Group's international competitors have larger sales networks and participate in reservation systems that are more comprehensive and convenient than those of the Group, or engage in promotional activities, which may enhance their ability to attract international passengers.

Furthermore, for short-distance transportation, airplanes, trains and buses are alternatives to each other. Given the recent development of high-speed trains (as discussed below), the construction of nationwide high-speed railway network and the improvement of inter-city expressway network, the commercial aviation sector as a whole faces increasing competition from the alternative means of transportation such as railways and highways.

***We expect to face substantial competition from the rapid development of the Chinese rail network.***

The PRC government is aggressively implementing the expansion of its high-speed rail network, which provides train services at a speed of up to 300 kilometers per hour connecting major cities such as Beijing, Shanghai, Wuhan, Zhengzhou, Xi'an, Qingdao, Guangzhou, Harbin and Dalian. In December 2012, the Beijing-Guangzhou and Harbin-Dalian High-Speed Railways commenced operation, the expansion of the coverage of this network and improvements in railway service quality, increased passenger capacity and stations located closer to urban centers than competing airports could enhance the relative competitiveness of the railway service and affect our market share on some of our key routes, in particular routes below 800 kilometers. The aggregate high-speed railway mileage in China reached over 10,000 kilometers as of December 31, 2013. The construction of all railways in China's "Four Longitudinal and Four Horizontal" high-speed railway network is expected to complete by the end of 2014. We expect it will bring further negative impact on the domestic aviation industry. Increased competition and pricing pressures from railway service may have a material adverse effect on our financial condition and results of operations.



***Due to limitation on foreign ownership imposed by Chinese government policies, the Company may have limited access to the international equity capital markets.***

Chinese government policies limit foreign ownership in Chinese airlines. Under these policies, the percentage ownership of our total outstanding ordinary shares held by investors in Hong Kong and any country outside China (“Foreign Investors”) may not in the aggregate exceed 49%. Currently, we estimate that 28.47% of the total outstanding ordinary shares of the Company are held by Foreign Investors. For so long as the limitation on foreign ownership is in force, we will have limited access to the international equity capital markets.

***The European Emissions Trading Scheme may increase operational cost of the Group.***

Starting on January 1, 2012, aviation sector will be included in the European Emissions Trading Scheme (ETS), EU’s mandatory cap-and-trade system for reduction of greenhouse gas emissions. Airline operators in the EU will receive tradable emission permits (aviation allowances) covering a certain level of their CO<sub>2</sub> emissions per year for their flights operating to and from EU airports. If an airline fails to obtain free-of-charge emission permits from the EU, it will have to buy around EUR10 million (RMB100 million) worth of CO<sub>2</sub> emissions allowances from other greener industries. Pursuant to this policy, the domestic airlines having flight points in Europe undertake the same carbon emission reductions obligation as the European local airlines, which will result in a significant increase in the operating cost of domestic airlines in Europe, including our Company, and further have an adverse impact on the results of operations and financial condition. In March 2011, a group representing China’s largest airlines sent a formal notice to the EU expressing strong opposition to non-member-state airlines’ inclusion in the EU’s Emissions Trading Scheme. Also, in early February 2012, CAAC issued instructions to various airlines announcing that without approval from the relevant government authorities, the major airlines are prohibited from joining the ETS and the transport airlines are also prohibited from raising the freight price or increasing fee items by adducing this reason. On November 12, 2012, EU announced to temporarily suspend the implementation of the ETS in the aviation sector in 2013 in order to forge a positive negotiation environment for all parties. Although the EU Commission has brought forward to the Council of the EU and the ETS legislation amendment, which will narrow down ETS within the EU airspace, the EU has not yet made the final decision. There can be no assurance that the new implementation proposal will not have negative impact on our financial condition and result of operation.

***We may utilize fuel hedging arrangements which may result in losses.***

While we have not entered into any fuel hedging transactions since the fourth quarter of 2008, we may in the future consider to hedge a portion of our future fuel requirements through various financial derivative instruments linked to certain fuel commodities to lock in fuel costs within a hedged price range. However, these hedging strategies may not always be effective and high fluctuations in aviation fuel prices exceeding the locked-in price ranges may result in losses. Significant declines in fuel prices may substantially increase the costs associated with our fuel hedging arrangements. In addition, where we seek to manage the risk of fuel price increases by using derivative contracts, we

cannot assure you that, at any given point in time, our fuel hedging transactions will provide any particular level of protection against increased fuel costs.

## **Risks Relating to the PRC**

*The Group has significant exposure to foreign currency risk as majority of the Group's lease obligations and bank and other loans are denominated in foreign currencies. Due to rigid foreign exchange control by Chinese government, the Group may face difficulties in obtaining sufficient foreign exchange to pay dividends or satisfy our foreign exchange liabilities.*

Under current Chinese foreign exchange regulations, the Renminbi is fully convertible for current account transactions, but is not freely convertible for capital account transactions. All foreign exchange transactions involving Renminbi must take place either through the People's Bank of China or other institutions authorized to buy and sell foreign exchange or at a swap centre.

The Group has significant exposure to foreign currency risk as substantially all of the Group's obligations under leases, bank and other loans and operating lease commitment are denominated in foreign currencies, principally U.S. dollars, Singapore dollars and Japanese Yen. Depreciation or appreciation of the Renminbi against foreign currencies affects the Group's results significantly because the Group's foreign currency liabilities generally exceed its foreign currency assets. The Group is not able to hedge its foreign currency exposure effectively other than by retaining its foreign currency denominated earnings and receipts to the extent permitted by SAFE, or subject to certain restrictive conditions, entering into foreign exchange forward option contracts with authorized banks. However, SAFE may limit or eliminate the Group's ability to purchase and retain foreign currencies in the future. In addition, foreign currency transactions under the capital account are still subject to limitations and require approvals from SAFE. This may affect our ability to obtain foreign exchange through debt or equity financing, including by means of loans or capital contributions. No assurance can be given that the Group will be able to obtain sufficient foreign exchange to pay dividends or satisfy our foreign exchange liabilities.

The Group also has exposure to foreign currency risk in respect of net cash inflow denominated in Japanese Yen from ticket sales in overseas branch office after payment of expenses. The Group entered into certain foreign exchange forward option contracts, which were fully settled in 2011, to manage this foreign currency risk. However, like other derivative products, there can be no assurance that such option contracts can provide, at any given time, particular level of protection against foreign exchange risks.

***The Group's operations are subject to immature development of legal system in China. Lack of uniform interpretation and effective enforcement of laws and regulations may cause significant uncertainties to the Group's operations.***

The members of the Group are organized under the laws of China. The Chinese legal system is based on written statutes and is a system, unlike common law systems, in which decided legal cases have little precedential value. Since 1979, the Chinese government has been developing a comprehensive system of commercial laws and considerable progress has been made in the promulgation of laws and regulations dealing with economic matters, such as corporate organization and governance, foreign investments, commerce, taxation and trade. These laws, regulations and legal requirements are relatively recent, and, like other laws, regulations and legal requirements applicable in China (including with respect to the commercial aviation industry), their interpretation and enforcement involve significant uncertainties.

***The PRC new tax law may in the future deprive us of preferential income tax rates, which we currently enjoy.***

On March 16, 2007, the Fifth Plenary Session of the Tenth National People's Congress passed the Corporate Income Tax Law of the PRC which took effect on January 1, 2008. As a result of the new tax law, the statutory income tax rate adopted by the Company and its subsidiaries has been changed to 25% with effect starting from January 1, 2008. Prior to enactment of the new tax law, certain branches and subsidiaries of the Company were taxed at rates ranging from 15% to 33%. Pursuant to the new tax law, the income tax rates of entities that previously enjoyed preferential tax rates of 15% and 18% have been revised to 18%, 20%, 22%, 24% and 25% for 2008, 2009, 2010, 2011 and 2012 onwards respectively. To the extent that there are any withdrawals of, or changes in, the preferential tax treatment that we currently enjoy, our tax liability may increase correspondingly and our financial condition and results of operations may be adversely affected.

On July 31, 2012, the Ministry of Finance ("MOF") and the State Administration of Taxation ("SAT") jointly issued a pilot program (the "Pilot Program"), pursuant to which, commencing on November 1, 2012, business tax is replaced by a value-added tax ("VAT"). According to the Pilot Program, all traffic revenues and the other revenues that fall within the scope of the Pilot Program, including ground service income and cargo handling income, are subjected to VAT levied at the applicable tax rates of 17%, 11% or 6%. Other revenues that are not within the scope of the Pilot Program continue to be subject to business tax at applicable tax rates. However, as the Pilot Program has only been implemented recently, there is uncertainty as to how its impact on our financial condition and results of operations is

not certain, but it may affect the way we record our revenues and taxes in our financial statements. As a result, it may be difficult to compare our financial statements in future periods with these before the Pilot Program was implemented.

***The PRC new tax law may have negative tax impact on holders of H Shares or ADRs of the Company, by requiring the imposition of a withholding tax on dividends paid by a Chinese company to a non-resident enterprise.***

The new tax law generally provides for a withholding tax on dividends paid by a Chinese company to a non-resident enterprise at a rate of 10%.

For individuals, Chinese tax law generally provides that an individual who receives dividends from the Company is subject to a 20% income tax. A 50% reduction of taxable income is granted by Chinese tax law for an individual receiving dividends from a listed company on Shanghai Stock Exchange or Shenzhen Stock Exchange. As a result, the effective tax rate for dividends received by A Share individual holders is 10% in 2013. Dividend received by any foreign individual that holds overseas shares in Chinese enterprise is generally subject to individual income tax at a flat rate of 20%, subject to exemption or reduction by an applicable double-taxation treaty.

***Our investors in the U.S. who rely on our auditor's audit reports currently do not have the benefit of PCAOB oversight.***

Under the Sarbanes-Oxley Act of 2002, the Public Company Accounting Oversight Board, or PCAOB, has the authority and is required to conduct continuing inspections of registered public accounting firms that provide audit services to public companies subject to the reporting requirements of the SEC. Our external auditor is registered with the PCAOB and is subject to inspections by the PCAOB. However, the PCAOB is currently unable to inspect a registered public accounting firm's audit work relating to a company's operations in China where the documentation of such audit work is located in China, such as our registered public accounting firm's audit work relating to our operations in China. As a result, our investors may be deprived of the benefits of PCAOB's oversight of our independent registered public accounting firm through such inspections.

***Proceedings instituted recently by the SEC against four PRC-based accounting firms, including our independent registered public accounting firm, could result in financial statements being determined to not be in compliance with the requirements of the Securities Exchange Act of 1934.***

In December 2012, the SEC instituted administrative proceedings against four PRC-based accounting firms, including our independent registered public accounting firm, alleging that these firms had violated U.S. securities laws and the SEC's rules and regulations thereunder by failing to provide to the SEC the firms' work papers related to their audits of certain PRC-based companies that are publicly traded in the United States and which are the subject of certain ongoing SEC investigations. On January 22, 2014, an initial administrative law decision was issued, which determined that the four PRC-based accounting firms should be censured and barred from practicing before the SEC for a period of six months. The four PRC-based accounting firms recently appealed the initial administrative law decision to the SEC. The initial law decision is neither final nor legally effective unless and until it is endorsed by the full SEC. The accounting firms can also further appeal the final decision of the SEC through the federal appellate courts.

We were not and are not the subject of any SEC investigations nor are we involved in the proceedings brought by the SEC against the accounting firms. If the SEC is successful in the proceedings, it could result in the accounting firms, including our independent registered public accounting firm losing temporarily or permanently, the ability to practice before the SEC. While we cannot predict the outcome of the SEC's proceedings, if the accounting firms including our independent registered public accounting firm were denied, temporarily or permanently, the ability to practice before the SEC, and we are unable to find timely another registered public accounting firm which can audit and issue a report on our financial statements, our financial statements could be determined to not be in compliance with the requirements for financial statements of public companies registered under the Securities Exchange Act of 1934, as amended, or the Exchange Act. Such a determination could ultimately lead to the delisting of our common stock from the NYSE for CSA's case or deregistration from the SEC, or both, which would substantially reduce or effectively terminate the trading of our common stock in the United States.

ITEM 4. INFORMATION ON THE COMPANY.

A. History and Development of the Company

We were incorporated under PRC laws on March 25, 1995 as a joint stock company with limited liability under the name of China Southern Airlines Company Limited. The address of our principal place of business is 278 Ji Chang Road, Guangzhou, People's Republic of China 510405. Our telephone number is +86 20 8612 4462 and our website is [www.csair.com](http://www.csair.com).

In July 1997, we issued 1,174,178,000 H Shares, par value RMB1.00 per share, and completed the listing of the H Shares on the Stock Exchange of Hong Kong Limited (the "Hong Kong Stock Exchange") and the ADRs representing our H shares on the New York Stock Exchange.

On March 13, 2003, we obtained an approval certificate from the Ministry of Commerce to change to a permanent limited company with foreign investments and on October 17, 2003 obtained a business license for its new status, as a permanent limited company with foreign investments issued by the State Administration of Industry and Commerce of the People's Republic of China.

In July 2003, we issued 1,000,000,000 A Shares, par value RMB1.00 per share, and completed the listing of the A shares on the Shanghai Stock Exchange.

Pursuant to a sale and purchase agreement dated November 12, 2004 between the Company, CSAHC, China Northern Airlines ("CNA") and Xinjiang Airlines ("XJA"), which was approved by our shareholders in an extraordinary general meeting held on December 31, 2004, we acquired the airline operations and certain related assets of CNA and XJA with effect from December 31, 2004 at a total consideration of RMB1,959 million.

On May 30, 2007, we, together with an independent third party, established Chongqing Airlines Company Limited (“Chongqing Airlines”). As of December 31, 2012, the Company had transferred four aircraft to Chongqing Airlines as capital contribution. We own a total of 60% equity interest in Chongqing Airlines.

On August 14, 2007, we acquired a 51% equity interest in Nan Lung International Freight Limited beneficially owned by and registered in the name of Nan Lung Travel & Express (Hong Kong) Limited, and a 100% equity interest in China Southern Airlines Group Air Catering Company Limited, both a wholly owned subsidiary of CSAHC, for a total consideration of RMB112 million.

In December 2008, we acquired a 26% equity interest in China Southern West Australian Flying College Pty Ltd. (“Flying College”) from CSAHC, and Flying College became a 91% owned subsidiary of the Company.

In June 2009, we acquired a 50% equity interest in Beijing Southern Airlines Ground Services Company Limited (“Beijing Ground Service”) from the other shareholder, and Beijing Ground Service became a wholly-owned subsidiary of the Company.

On September 28, 2009, we entered into an agreement with CSAHC to sell our 50% equity interest in MTU Maintenance Zhuhai Co., Ltd (“Zhuhai MTU”), a jointly controlled entity of the Company, to CSAHC at a consideration of RMB1,607,850,000. The transfer was completed in February 2010.

On June 2, 2010, a third party company injected capital to Flying College, which diluted the Company’s interest in Flying College from 91% to 48.12%. Flying College became a jointly controlled entity of the Company since then. The retained non-controlling equity interest in Flying College is re-measured to its fair value at the date when control was lost and a gain on deemed disposal of a subsidiary of RMB17 million was recorded in 2010.

In December 2010, we entered into an agreement with Xiamen Jianfa Group Co., Ltd. and Hebei Aviation Investment Group Corporation Limited (“Hebei Investment”), pursuant to which Hebei Investment agreed to inject a cash capital of RMB1,460 million into Xiamen Airlines Company Limited (“Xiamen Airlines”). In March 2011, the capital injection was received in full and the Company’s equity interest in Xiamen Airlines was diluted from 60% to 51%. Xiamen Airlines remains a subsidiary of the Company.

On June 29, 2012, Xiamen Airlines, a subsidiary of the Company and Southern Airlines Culture and Media Co., Ltd. (“SACM”) entered into an agreement, pursuant to which Xiamen Airlines agreed to sell and SACM agreed to purchase 51% equity interests in Xiamen Airlines Media Co., Ltd. (“XAMC”), at a consideration of approximately RMB43.12

million. Immediate prior to the transaction, XAMC was wholly owned by Xiamen Airlines and primarily engaged in providing advertising, corporate branding, publicity and exhibition services and was responsible for the overall brand building and publicity of Xiamen Airlines.

On September 24, 2012, we entered into a joint venture agreement with Henan Civil Aviation Development and Investment Co., Ltd. (“Henan Aviation Investment”) for the establishment of China Southern Airlines Henan Company Limited, a joint venture company with a total registered capital of RMB6 billion, which will be owned as 60% and 40% by the Company and Henan Aviation Investment, respectively. The first installment of paid-in capital of RMB1.2 billion was received in full. On September 28, 2013, Henan Aviation Investment was established.

### **Aircraft Acquisitions**

Pursuant to an aircraft acquisition agreement dated April 18, 2008 between Xiamen Airlines and the Boeing Company (“Boeing”), Xiamen Airlines will acquire 20 Boeing B737 series aircraft from Boeing. According to the information provided by Boeing, the aggregate catalogue price for those aircraft including the airframe and engines is around US\$1.5 billion. The aggregate consideration for the acquisition will be partly payable in cash by Xiamen Airlines, and partly through financing arrangements with banking institutions. The Boeing aircraft will be delivered in stages to Xiamen Airlines during the period commencing from April 2014 to October 2015.

Pursuant to an A320 Series Aircraft Purchase Agreement dated January 20, 2010 between the Company and Airbus SNC, we will acquire 20 Airbus 320 series aircraft from Airbus SNC. According to the information provided by Airbus SNC, the catalogue price of an Airbus 320 aircraft, including airframe and engines, is around US\$76.9 million. The aggregate consideration for the acquisition will be partly payable in cash and partly through financing arrangements with banking institutions. The Airbus aircraft have been delivered in stages to the Company.



On September 30, 2010, Xiamen Airlines entered into a supplemental agreement with Boeing to purchase additional 10 Boeing B737 series aircraft. The aggregate catalogue price for those aircraft, including airframe and engines, is around US\$699 million. According to the information provided by Boeing, the aggregate consideration for the acquisition will be partly payable in cash by Xiamen Airlines, and partly through financing arrangements with banking institutions. The Boeing aircraft will be delivered in stages to Xiamen Airlines during the period commencing from 2015 to October 2016.

On November 4, 2010, we entered into an A320 series aircraft purchase agreement and an A330-300 aircraft purchase agreement with Airbus S.A.S. to purchase 30 Airbus A320 series aircraft and six Airbus A330 series aircraft. According to the information provided by Airbus S.A.S., the catalogue price of six Airbus A330 series aircraft and 30 Airbus A320 series aircraft, including airframe and engines, is US\$1.205 billion and US\$2.575 billion, respectively. The aggregate consideration for the acquisition will be partly payable by cash and partly by financing arrangements with banking institutions. The six Airbus A330 aircraft will be delivered in stages to the Company during the period commencing from 2013 to 2014 and the 30 Airbus A320 series aircraft will be delivered in stages to the Company during the period commencing from 2012 to 2015.

On May 31, 2011, we entered into an aircraft acquisition agreement with Boeing to purchase six Boeing B777F freighters. According to the information provided by Boeing, the catalogue price of six Boeing B777F aircraft, including airframe and engines, is US\$1,584 million. The aggregate consideration for the Acquisition will be partly payable by cash and partly by financing arrangements with banking institutions. The six Boeing B777F freighters will be delivered in stages to us during the period commencing from 2013 to 2015.

On May 9, 2011, Xiamen Airlines entered into an aircraft acquisition agreement to purchase six Boeing B787 series aircraft. According to the information provided by Boeing, the aggregate catalogue price, including airframe and engines, for the six Boeing B787 series aircraft is US\$1,098 million. The aggregate consideration for the acquisition will be partly payable in cash and partly through financing arrangements with banking institutions. The Boeing aircraft will be delivered in stages to Xiamen Airlines during the period commencing from 2014 to 2015.

On February 28, 2012, we entered into an agreement with the Boeing Company to purchase 10 Boeing 777-300ER aircraft. According to the information provided by Boeing, the catalogue price of one Boeing 777-300ER aircraft, including airframe and engines, is around US\$298 million. The aggregate consideration for the acquisition will be partly payable in cash and partly through financing arrangements with banking institutions. The Boeing aircraft will be delivered in stages to the Company during the period from 2014 to 2016.

On August 3, 2012, Xiamen Airlines entered into an agreement with Boeing to purchase 40 Boeing B737 series aircraft from Boeing. The aggregate catalogue price of the 40 Boeing B737 series aircraft is US\$3.36 billion. The aggregate consideration for the acquisition will be partly payable by cash and partly by financing arrangements with banking institutions. The Boeing aircraft will be delivered in stages to Xiamen Airlines during the period commencing

from 2016 to 2019.

On December 5, 2012, we entered into the Airbus aircraft acquisition agreement with Airbus S.A.S. to purchase 10 Airbus A330-300 aircraft. The catalogue price of one Airbus A330-300 aircraft is US\$188 million. The aggregate consideration for the acquisition will be partly payable by cash and partly by financing arrangements with banking institutions. The Airbus aircraft will be delivered in stages to the Company during the period commencing from 2014 to 2016.

### **Capital Expenditure**

The Group had RMB29,576 million, RMB23,911 million and RMB23,428 million capital expenditures in 2013, 2012 and 2011, respectively. Of such capital expenditures in 2013, RMB17,268 million was financed by capital leases, RMB11,801 million was financed by bank borrowings while the remaining RMB507 million was financed by internal resources. The capital expenditures were primarily incurred on the additional investments in aircraft and flight equipment under the Group's fleet expansion plans and, to a small extent, additional investments in other facilities and buildings for operations. As of December 31, 2013, we had total capital commitments for aircraft, engines and related equipment of approximately RMB47,651 million.

## B. Business Overview

### General

The Group provides commercial airline services throughout Mainland China, Hong Kong, Macau and Taiwan regions, Southeast Asia and other parts of the world. Based on the statistics from the CAAC, the Group is one of the largest Chinese airlines and, as of the year end of 2013, ranked first in terms of number of passengers carried, number of scheduled flights per week, number of hours flown, number of routes and size of aircraft fleet. During the three years ended December 31, 2013, the Group's RPKs increased at a compound annual growth rate of 10.1% from 122,344 million in 2011 to 135,535 million in 2012 and 148,417 million in 2013 while its capacity, measured in terms of ASKs, increased at a compound annual growth rate of 12.2%, from 151,064 million in 2011 to 169,569 million in 2012 and 186,800 million in 2013. In 2013, the Group carried 91,791 million passengers and had passenger revenue of RMB88,271 million (approximately US\$14,478 million).

The Group conducts a portion of its airline operations through its airline subsidiaries namely Xiamen Airlines, Shantou Airlines Company Limited ("Shantou Airlines"), Zhuhai Airlines Company Limited ("Zhuhai Airlines"), Guizhou Airlines Company Limited ("Guizhou Airlines") and Chongqing Airlines Company Limited ("Chongqing Airlines") (collectively, the "Airline Subsidiaries"). In 2013, the Airline Subsidiaries carried 27.3 million passengers and had passenger revenue of RMB22,404 million (approximately US\$3,675 million) and accounted for 29.7% and 25.4% of the Group's passengers carried and passenger revenue, respectively.

The Group also provides air cargo and mail services. The cargo and mail revenue of the Group decreased by 2.2% to RMB6,413 million (approximately US\$1,052 million) in 2013 as compared with that of 2012. The Group's airline operations are fully integrated with its airline-related businesses, including aircraft and engine maintenance, flight simulation and air catering operations.

As of December 31, 2013, the Group operated 849 routes, of which 674 were domestic, 135 were international and 40 were regional. The Group operates the most extensive domestic route network among all Chinese airlines. Its route network covers commercial centers and rapidly developing economic regions in Mainland China.

The Group's corporate headquarters and principal base of operations are located in Guangzhou, the capital of Guangdong Province and the largest city in southern China. Located in the rapidly developing Pearl River Delta region, Guangzhou is also the transportation hub of southern China and one of China's major gateway cities. Guangzhou's significance has increased as the transportation infrastructure of Guangdong Province has developed through the construction and development of expressways, an extensive rail network and the port cities of Guangzhou, Shenzhen, Zhanjiang, Zhuhai and Shantou.

In December 2005, we established a branch company in Beijing and have added wide-body airplanes to our operation base in Beijing, with the view to expanding our Beijing aviation business and building another main hub there in addition to our Guangzhou base. The establishment of Guangzhou and Beijing hubs will facilitate strategic refinement and enhancement of our route network operations, putting us in a better position to explore and seize the opportunities in the aviation market.

The Group's operations primarily focus on the domestic market. In addition, the Group also operates regional routes and international flights. As of December 31, 2013, the Group had 40 regional routes and 135 international routes. The Group's regional operations include flights between destinations in Mainland China, Hong Kong, Macau and Taiwan. The Group's international operations include scheduled services to cities in Australia, Austria, Azerbaijan, Bangladesh, United Kingdom, Burma, Cambodia, Canada, Dutch, France, Georgia, German, India, Indonesia, Japan, Kazakhstan, Kyrgyzstan, Malaysia, Maldives, Nepal, New Zealand, Pakistan, Philippines, Russia, Saudi, Singapore, South Korea, Tajikistan, Thailand, Turkey, Turkmenistan, United Arab Emirates (UAE), United States of American (USA), Vietnam and other destinations.

After joining Skyteam Alliance, the Group has established a network reaching over 1,024 destinations globally, connecting 187 countries and regions and covering major cities around the world.

As of December 31, 2013, the Group had a fleet of 561 aircraft, consisting primarily of Boeing 737 series, 747, 757, 777, 787, Airbus 320 series, 330, 380 etc. The average age of the Group's registered aircraft was 6.0 years as of December 31, 2013.

### **Restructuring and Initial Public Offering**

As part of China's economic reforms in the 1980's, the PRC State Council directed the CAAC to separate its governmental, administrative and regulatory role from the commercial airline operations that were being conducted by the CAAC and its regional administrators. As a result, CSAHC was established on January 26, 1991 for the purpose of assuming the airline and airline-related commercial operations of the Guangzhou Civil Aviation Administration, one of the then six regional bureaus of the CAAC. CSAHC was one of the 55 large-scale enterprises designated by the Chinese government to play a leading role in their respective industries.

CSAHC was restructured in 1994 and 1995 in anticipation of our initial public offering. The restructuring was effective through the establishment of the Company and the execution of the De-merger Agreement on March 25, 1995 by and between CSAHC and the Company. Upon the restructuring, the Company assumed substantially the entire airline and airline-related businesses, assets and liabilities of CSAHC, and CSAHC retained its non-airline-related businesses, assets and liabilities. All interests, rights, duties and obligations of CSAHC, whenever created or accrued, were divided between the Company and CSAHC based on the businesses, assets and liabilities assumed by each of them under the De-merger Agreement. Under the De-merger Agreement, CSAHC agreed not to conduct or participate or hold any interest in, either directly or indirectly, any business, activity or entity in or outside China that competes or is likely to compete with the commercial interests of the Group, although CSAHC may continue to hold and control its affiliates existing on the date of the De-merger Agreement and may continue to operate the businesses of such associates. Under the De-merger Agreement, CSAHC and the Company also agreed to indemnify each other against any losses, claims, damage, debts or expenses arising out of or in connection with the restructuring. As of the date of this Annual Report, no indemnity has been provided by either CSAHC or us.

In July 1997, we completed a private placement of 32,200,000 H Shares to certain limited partnership investment funds affiliated with Goldman Sachs & Co. and an initial public offering of 1,141,978,000 H Shares, par value RMB1.00 per share, and the listing of the H Shares on the Hong Kong Stock Exchange and ADRs on the New York Stock Exchange. Prior to the private placement and the initial public offering, all of our issued and outstanding shares of capital stock, consisting of 2,200,000,000 non-tradable domestic shares (“Domestic Shares”), par value RMB1.00 per share, were owned by CSAHC, which owned and exercised, on behalf of the Chinese government and under the supervision of the CAAC, the rights of ownership of such Domestic Shares. After giving effect to the private placement and the initial public offering, CSAHC maintained its ownership of the 2,200,000,000 Domestic Shares (representing approximately 65.2% of the total share capital of the Company), and became entitled to elect all the directors of the Company and to control the management and policies of the Group. The Domestic Shares and H Shares are both ordinary shares of the Company.

In July 2003, we issued 1,000,000,000 A Shares, par value of RMB1.00 per share, and listed these shares on the Shanghai Stock Exchange. Subsequent to the issuance of the A Shares, the shareholding of CSAHC in the Company was reduced from 65.2% to 50.30%.

## **Share Reform Scheme**

Pursuant to relevant PRC laws, we launched the share reform scheme in May 2007, whereby all the 2,200,000,000 non-tradable Domestic Shares held by CSAHC would be converted into tradable A Shares. Upon the completion of such scheme on June 20, 2008, all the non-tradable Domestic Shares have been successfully converted into tradable A Shares, subject to the restriction that CSAHC shall not transfer or trade these shares within 36 months after the commencement date of the share reform scheme (which is June 18, 2007).

### **Bonus Shares Issue by Conversion of Share Premium**

On June 25, 2008, our shareholders approved issuance of bonus shares by way of conversion of share premium, and on August 14, 2008, the Ministry of Commerce approved the bonus share issue. The issue has been effected by conversion of share premium on the basis of 5 new shares, credited as fully paid, for every 10 existing shares. Upon the completion of the bonus share issue, which is based on 4,374,178,000 shares in issue as of December 31, 2007, the number of paid up shares has increased by 2,187,089,000 shares to 6,561,267,000 shares.

### **Non-Public Subscriptions**

On December 10, 2008, we entered into an A Shares subscription agreement with CSAHC, pursuant to which CSAHC conditionally agreed to subscribe and the Company conditionally agreed to allot and issue 721,150,000 new A Shares for a consideration of RMB2,278,834,000, equivalent to the subscription price of RMB3.16 per new A Share. Separately and on the same date, the Company and Nan Lung (a wholly-owned subsidiary of CSAHC) entered into an H Shares subscription agreement, pursuant to which Nan Lung conditionally agreed to subscribe and the Company conditionally agreed to allot and issue 721,150,000 new H Shares for a consideration of RMB721,150,000, equivalent to the subscription price of RMB1.00 (equivalent to approximately HK\$1.13) per new H Share. The subscription agreements were approved in the Extraordinary General Meeting and the respective Class Meetings of shareholders of A and H Shares on February 26, 2009. On June 3, 2009, we received the formal approval from CSRC for the proposed non-public issue of H Shares. On August 14, 2009, we received the formal approval from CSRC for the proposed non-public issue of A Shares. The issuance of 721,150,000 new A Shares to CSAHC and 721,150,000 new H Shares to Nan Lung were completed on August 20, 2009 and August 21, 2009, respectively.

On March 8, 2010, our board approved the placement of up to 1,766,780,000 new A shares to not more than 10 specific investors including CSAHC and the placement of not more than 312,500,000 new H shares to Nan Lung, a wholly-owned subsidiary of CSAHC. On the same date, the Company entered into the A shares subscription agreement with CSAHC, pursuant to which CSAHC conditionally agreed to subscribe and the Company conditionally agreed to allot and issue new A shares of not more than 132,510,000 at the subscription price of not less than RMB5.66 per A share. In addition, the Company and Nan Lung entered into the H shares subscription agreement, pursuant to which Nan Lung conditionally agreed to subscribe and the Company conditionally agreed to allot and issue new H shares of not more than 312,500,000 at the subscription price of not less than HK\$2.73 per H share. The above placement and subscription agreements were approved in the Extraordinary General Meeting and the respective Class Meetings of shareholders of A and H shares on April 30, 2010. On September 8, 2010, we received the formal approval from CSRC for the proposed non-public issuance of H Shares. On September 15, 2010, we received the formal approval from CSRC for the proposed non-public issue of A Shares. In November 2010, we completed the placements of 1,501,500,000 new A shares and 312,500,000 H shares, among which 123,900,000 new A shares were issued to CSAHC at the subscription price of RMB6.66 per share, and 312,500,000 H shares were issued to Nan Lung at the subscription price of HK\$2.73 per share.

On June 11, 2012, we entered into an A Shares subscription agreement with CSAHC, pursuant to which CSAHC conditionally agreed to subscribe and we conditionally agreed to allot and issue up to 487,804,878 A Shares for a consideration of not more than RMB2 billion, equivalent to the subscription price of approximately RMB4.1 per new A Share. The subscription agreement was approved in the Extraordinary General Meeting on August 10, 2012, which remained effective for a period of twelve months from the date of approval of the resolution at the general meeting. As of August 9, 2013, the relevant work regarding the 2012 Non-public A Share Issue of the Company had not been completed. The proposal for the 2012 Non-public A Share Issue of the Company and A Shares subscription agreement therefore were lapsed automatically due to the expiration of the resolution passed at the general meeting.

### **Issuance of Short-term Financing Bills and Medium Term Notes**

On April 18, 2008, our Board approved the proposed issuance of short-term financing bills in the principal amount of up to RMB4 billion in the PRC, and the submission of this proposal to the annual general meeting for the shareholders' approval. On June 25, 2008, our shareholders approved such proposed bill issuance at the annual general meeting for the year 2007. We believed that the bill issuance would provide a further source of funding at an interest rate which was expected to be lower than that for loans from commercial banks, lower the financing cost of borrowings for us, and was in the interests of us and our shareholders as a whole. The Company received the acceptance from National Association of Financial Market Institutional Investors to register the Company's short-term financing bills in the amount of RMB3.5 billion for a period up to September 10, 2010. The bills were jointly underwritten by China CITIC Bank Cooperation Limited and Bank of China Limited. In October 2008, we issued short-term financing bills with total face value of RMB2 billion with a bearing coupon interest rate at 4.7% and a maturity period of one year for funding of the business activities of the Company.

On May 28, 2008, the Board approved the proposed issuance of medium term notes by the Company in the principal amount of up to RMB1.5 billion and the submission of such proposal to the shareholders for their consideration and approval. On June 25, 2008, shareholders of the Company approved such notes issuance at the annual general meeting for the year 2007. The Company believed that the notes issue would provide a further source of medium to long term funding at an interest rate lower than the best lending rate for loans from commercial banks, lower the finance costs of borrowings for us and improve our debt structure. As of the date of this Annual Report, we have not issued any medium term notes, even though it has been approved by the Board and shareholders.

In order to capitalize on opportunities in the market and improve the flexibility and efficiency of financing, on June 25, 2012, the Board resolved to obtain a general and unconditional mandate from shareholders to issue potential debt financing instruments, in one or multiple tranches, within the permissible size for debt issuance in accordance with the provisions of the applicable laws and regulations. On the extraordinary general meeting held on August 10, 2012, shareholders approved the authorization given to the Board, generally and unconditionally, to determine the specific debt financing instruments and issuance plan, and to issue, in one or multiple tranches, debt financing instruments within the permissible size for debt issuance in accordance with the provisions of the applicable laws and regulations. According to the resolution, on October 31, 2012, the Board approved to apply to National Association of Financial Market Institutional Investors for registration to issue, in one or multiple tranches, ultra-short-term financing bills with an aggregate principal amount of to RMB10 billion, according to its capital needs and the market conditions. The Company has completed the issuance of the first tranche of ultra-short-term financing bills on February 8, 2013. The total issuance amount of the first tranche financing bills was RMB0.5 billion, with a maturity period of 180 days, a par value per unit of RMB100 and a nominal interest rate of 3.9%.



On March 21, 2014, the Company completed the issuance of the first tranche of ultra-short-term financing bills for the year 2014 of China Southern Airlines Company Limited (the “First Tranche Financing Bills”). The total issuance amount of the First Tranche Financing Bills was RMB3 billion, with a maturity period of 180 days, a par value per unit of RMB100 and a nominal interest rate of 5.1%.

On April 17, 2014, the Company completed the issuance of the second tranche of ultra-short-term financing bills for the year 2014 of China Southern Airlines Company Limited (the “Second Tranche Financing Bills”). The total issuance amount of the Second Tranche Financing Bills was RMB3 billion, with a maturity period of 270 days, a par value per unit of RMB100 and a nominal interest rate of 5.1%.

## Traffic

The following table sets forth certain statistical information with respect to the Group’s passenger, cargo and mail traffic for the years indicated.

Year	Passenger carried		Cargo and Mail arrived (tons)		Total traffic (tons kilometers)	
	Total (in millions)	Increase (decrease) over previous year (%)	Total (in thousands)	Increase (decrease) over previous year (%)	Total (in millions)	Increase (decrease) over previous year (%)
2011	80.68	5.5	1,135	1.6	14,461	10.4
2012	86.48	7.2	1,232	8.5	16,160	11.7
2013	91.79	6.1	1,276	3.6	17,469	8.1

## Route Network

### Overview

The Group operates the most extensive route network among all Chinese airlines. As of December 31, 2013, the Group operated 849 routes consisting of 674 domestic routes, 40 regional routes and 135 international routes.

The Group continually evaluates its network of domestic, regional and international routes in light of its operating profitability and efficiency. The Group seeks to coordinate flight schedules with the Airline Subsidiaries on shared routes to maximize load factors and utilization rates. The acquisition of domestic, regional and international routes is subject to approval of the CAAC, and the acquisition of regional and international routes is also subject to the existence and the terms of agreements between the Chinese government and the government of the Hong Kong SAR, the government of the Macau SAR, the government of Taiwan province and the government of the proposed foreign destination.

In order to expand the Group's international route network, the Group has entered into code-sharing agreements with several international airlines, including Delta Airlines, Air France, KLM Royal Dutch Airlines, Asiana Airlines, Korean Air, Japan Airlines Company Limited, Vietnam Airlines, Garuda Indonesian, Malaysian Airline, Kenya Airways, Pakistan International Airlines, Aeroflot-Russian Airlines, CSA Czech Airlines, Mandarin Airlines, WestJet, China Eastern Airlines, China Airlines and Xiamen Airlines. Under the code-sharing agreements, the participating airlines are permitted to sell tickets on certain international routes operated by the Group to passengers using the Group's codes. Similarly, the Group is permitted to sell tickets for the other participating airlines using its "CZ" code. The code-sharing agreements help increase the number of the Group's international sales outlets. After joining Skyteam Alliance, the Group has further established a network reaching over 1,024 destinations globally, connecting 187 countries and regions and covering major cities around the world.

### ***Route Bases***

In addition to its main route bases including Guangzhou as core hub, Beijing as major hub, Urumqi as regional hub and Chongqing as seasonal hub, the Group maintains regional route bases in Zhengzhou, Wuhan, Changsha, Shenzhen, Shenyang, Changchun, Dalian, Harbin, Haikou, Zhuhai, Xiamen, Shanghai, Xi'an, Fuzhou, Nanning, Guilin, Shantou, Guiyang and Sanya. Most of its regional route bases are located in provincial capitals or major commercial centers in the PRC.

The Group believes that its extensive network of route bases enable it to coordinate flights and deploy its aircraft more effectively and to provide more convenient connecting flight schedules and access service and maintenance facilities for its aircraft. The Group believes that the number and location of these route bases may enhance the Group's ability to obtain the CAAC's approval of requests by the Group to open new routes and provide additional flights between these bases and other destinations in China. Current regulations of the CAAC generally limit airlines to operations principally conducted from their respective route bases.

### ***Domestic Routes***

The Group's domestic routes network serves substantially all provinces and autonomous regions in China, including Guangdong, Fujian, Hubei, Hunan, Hainan, Guangxi, Guizhou, Henan, Heilongjiang, Jilin, Liaoning and Xinjiang, and serves all four centrally-administered municipalities in China, namely, Beijing, Shanghai, Tianjin, and Chongqing. In 2013, the Group's most profitable domestic routes were between: Guangzhou-Beijing, Beijing-Guangzhou, Shenzhen-Beijing, Shanghai-Guangzhou, Guangzhou-Shanghai, Beijing-Shenzhen, Urumqi-Beijing, Beijing-Urumqi, Shenzhen-Shanghai and Shanghai-Shenzhen.

### ***Regional Routes***

The Group offers scheduled service between Hong Kong and Guangzhou, Shenyang, Wuyishan, Zhangjiajie, Changchun, Yinchuan, Xiamen, Shantou, Beijing, Guilin, Meixian, Haikou, Wuhan, Zhengzhou, Nanning, Changsha, Sanya and Hohhot; between Macau and Hangzhou, Xiamen and Tianjin; and between Taipei and Guangzhou, Shanghai, Fuzhou, Hangzhou, Xiamen, Shenyang, Changsha, Wuhan, Dalian, Guilin, Harbin, Guiyang, Zhengzhou and Shenzhen. In 2013, the most profitable scheduled regional routes were between: Taipei-Guangzhou, Shanghai-Taipei, Guangzhou-Taipei, Taipei-Shanghai, Shenzhen-Taipei, Taipei-Shenzhen, Hong Kong-Beijing, Changchun-Guangzhou-Hong Kong, Beijing-Hong Kong and Hong Kong-Guangzhou-Changchun.

In 2013, the Group conducted a total of 17,247 flights on its regional routes, accounting for approximately 23.5% of all passengers carried by Chinese airlines on routes between Hong Kong, Macau or Taiwan and destinations in Mainland China according to CAAC statistics.

Previously, direct flights between Taiwan and Mainland China were only available during certain festivals. Other than that, travelers between Taiwan and Mainland China had to make use of intermediate stops in Hong Kong or elsewhere. Since July, 2008, however, the ban on direct flights was further liberalized to allow direct charter flights on weekends. We were the first Chinese carrier to fly nonstop to Taiwan. On November 4, 2008, the Mainland China and Taiwan agreed to have regular direct passenger charter flights across the Taiwan Strait. On August 31, 2009, the Mainland China and Taiwan increased the number of regular cross-Strait direct passenger flights from 108 to 270 a week. Cross-Strait direct passenger flights were further increased in the following years. As of April 18, 2014, there were 414 cross-Strait direct passenger flights a week.

In order to further strengthen its presence in Taiwan, the Company entered into a memorandum of cooperation with China Airlines on June 23, 2008, which is the largest carrier in Taiwan in terms of route network. Based on the memorandum, the scope of cooperation between the parties will cover passenger and cargo carrying, maintenance, and ground handling services.

### ***International Routes***

The Group is the principal Chinese airline serving southeast Asian destinations, including Singapore and major cities in Bangladesh, Indonesia, Thailand, Malaysia, Philippines, Vietnam, Myanmar and Cambodia.

In addition, the Group also provides scheduled services to cities in Australia, Austria, Canada, France, Germany, Georgia, India, Japan, Kazakhstan, Korea, Kyrgyzstan, Maldives, Nepal, Netherlands, Nigeria, New Zealand, Pakistan, Russia, Saudi Arabia, Tajikistan, Turkmenistan, Turkey, UAE, the United Kingdom and the United States.

Since joining Skyteam Alliance, the Group has established a network reaching over 1,024 destinations globally, connecting 187 countries and regions and covering major cities around the world.

In 2013, the Group's most profitable international routes were: Guangzhou-Los Angeles, Guangzhou-Sydney, Dalian-Seoul, Guangzhou-Melbourne, Shenyang-Seoul, Seoul-Shenyang, Seoul-Dalian, Beijing-Guangzhou-Phnom Penh, Phnom Penh-Guangzhou-Beijing, Guangzhou-Auckland.

### *Aircraft Fleet*

The Group's fleet plan in recent years has emphasized expansion and modernization through the acquisition of new aircraft and the retirement of less efficient and old aircraft. As of December 31, 2013, the Group operated a fleet of 561 aircraft with an average age of 6.0 years. Most aircraft of the Group are Boeing and Airbus aircraft. The Group has the largest fleet among Chinese airline companies. Among all the aircraft, 319 aircraft operated by the Group are leased pursuant to various types of leasing arrangements. Please see the table below for an analysis of our aircraft in terms of average age and respective passenger capacity.

Model	Number of Aircraft	Average Age (years)	Passenger Capacity
Boeing 787	8	0.3	228
Boeing 777-200	8	16.9	284/360
Boeing 757-200	19	16	174/180//192/196/197/204
Boeing 737-800	175	4.4	159/161/164/170
Boeing 737-700	52	8.1	120/128
Boeing 737-300	10	18.6	126/138/140/144/148
Boeing 747-400F	2	11.4	n/a
Boeing 777-200F	8	2.7	n/a
Airbus 380-800	5	1.7	506
Airbus 330-300	11	4.2	218/258
Airbus 330-200	16	4.7	275/284
Airbus 321-200	63	5.6	152
Airbus 320-200	114	5.7	179
Airbus 319-100	44	7.4	122
EMB190	20	1.8	98
EMB145	6	9.3	50
Total	561	6.0	n/a

In 2013, the Group continued to expand and modernize its aircraft fleet. During 2013, the Group (i) took scheduled delivery of 85 aircraft, including one A380 aircraft, three A330-300 aircraft, four A321-200 aircraft, 20 A330-200 aircraft, eight B787 aircraft, 44 B737-800 aircraft and two B777-200F aircraft; (ii) took scheduled delivery of three EMB190 aircraft under operating leases; (iii) returned seven aircraft under operating leases upon expiry, including two B777-200 aircraft two B737-700 aircraft and three B737-300 aircraft; and (iv) disposed eight B737-300 aircraft.

In February 2012, we entered into an agreement with the Boeing Company for the acquisition of ten Boeing B777-300ER aircraft. In August 2012, Xiamen Airlines, our subsidiary, entered into an agreement with the Boeing Company for the acquisition of 40 Boeing B737 series aircraft. In December 2012, we entered into an agreement with Airbus S.A.S. for the acquisition of ten Airbus A330-300 aircraft. Aircraft under these acquisition agreements are scheduled for delivery from 2014 to 2019.

## **Aircraft Financing Arrangements**

### ***Overview***

A significant portion of the Group's aircraft is acquired under long-term capital or operating leases or long-term mortgage loans with remaining terms to maturity ranging from one to eleven years. As of December 31, 2013, 182 of the Group's 561 aircraft were operated under capital leases, 137 were operated under operating leases, 242 were either owned aircraft financed by long-term mortgage loans, or acquired either with cash proceeds or acquired by exercising the purchase options upon expiry of the respective capital leases. The Group's planned acquisition of aircraft in the foreseeable future will generally be made through acquisition by bank loans and the Group's own funds, and pursuant to operating leases or capital leases. The Group's determination as to its acquisition strategy depends on the Group's evaluation at the time of its capacity requirements, anticipated deliveries of aircraft, the Group's capital structure and cash flow, prevailing interest rates and other general market conditions.

The following table sets forth, as of December 31, 2013, the number of aircraft operated by the Group pursuant to capital and operating leases and the average remaining terms, of such leases.

	Capital Lease	Operating Lease	Average Remaining Lease Term
Model	Year	Year	Year
Boeing 787	0	8	11.01
Boeing 737-800	55	39	5.87
Boeing 737-700	13	12	1.40
Boeing 777-200F	0	4	8.81
Airbus 380-800	0	2	9.67
Airbus 330-300	8	3	7.62
Airbus 330-200	2	11	6.92
Airbus 321-200	20	13	6.51
Airbus 320-200	34	39	7.58
Airbus 319-100	30	6	4.29
EMB190	20	0	6.30
Total	182	137	6.12

### ***Capital leases***

The majority of the capital leases in respect to aircraft and related equipment have terms of ten to twelve years expiring during the years 2015 to 2025. As of December 31, 2013, the Group's aggregate future minimum lease payments (including future finance charges) required under its capital leases were RMB39,431 million. The Group's capital leases typically cover a significant portion of the relevant aircraft's useful life and transfer the benefits and risks of ownership to the Group. Under its capital leases, the Group generally has an option to purchase the aircraft at or near the end of the lease term. As is customary in the case of capital leases, the Group's obligations are secured by the related aircraft, as well as other collateral.

### ***Operating Leases***

As of December 31, 2013, the Group's aggregate future minimum lease payments required under its operating leases were RMB26,222 million. As of the year end of 2013, the Group's operating leases had original terms generally ranging from five to fifteen years from the date of delivery of the relevant aircraft, and the remaining terms of these leases ranged from one to eleven years. Pursuant to the terms of the operating leases, the Group is obligated to make rental payments based on the lease term, with no termination payment obligations or purchase option, and the lessor bears the economic benefits and risks of ownership. Under its operating leases, the Group has no option to purchase the aircraft and is required to return the aircraft in the agreed condition at the end of the lease term. Although title to

the aircraft remains with the lessor, the Group is responsible during the lease term for the maintenance, servicing, insurance, repair and overhaul of the aircraft.

For capital leases or operating leases, the Group is obligated to indemnify the lessors against any withholding or similar taxes that may be imposed on the lessors by taxing authorities in China with regard to payments made pursuant to such leases. In accordance with relevant PRC tax regulations, a PRC lessee is liable to withhold PRC withholding tax in respect of any lease payments regularly made to an overseas lessor. Depending on the circumstances, this tax is generally imposed at a fixed rate ranging from nil to 11.6% of the lease payments, or in certain cases, the interest components of such payments for capital lease. The PRC withholding tax payable in respect of the lease arrangements amounting RMB198 million, RMB182 million and RMB172 million during 2013, 2012 and 2011 respectively, has been included as part of the lease charges.

### **Aircraft Flight Equipment**

The jet engines used in the Group's aircraft fleet are manufactured by General Electric Corporation, Rolls-Royce plc, United Technologies International, Inc., CFM International, Inc. and International Aviation Engines Corporation. The Group had 85 and 79 spare jet engines for its fleet as of the year end of 2013 and 2012, respectively. The Group determines its requirements for jet engines based on all relevant considerations, including manufacturers' recommendations, the performance history of the jet engines and the planned utilization of its aircraft. Acquisition of rotables and certain of the expendables for the Group's aircraft are generally handled by Southern Airlines (Group) Import and Export Trading Company Limited ("SAIETC"), a subsidiary of CSAHC acting as agent for the Group, in consideration of an agency fee. The Group arranges the ordering of aircraft, jet engines and other flight equipment for the Airline Subsidiaries and keeps an inventory of rotables and expendables for the Airline Subsidiaries.



## Aircraft Maintenance

A major part of the maintenance for the Group's fleet other than overhauls of jet engines is performed by Guangzhou Aircraft Maintenance Engineering Company Limited ("GAMECO"), an entity jointly controlled by the Company, Hutchison Whampoa ("Hutchison") and South China International Aircraft Engineering Company Limited, consistent with the Group's strategy to achieve fully integrated airline operations and to assure continued access to a stable source of high quality maintenance services. The remaining part of the maintenance for the Group's fleet other than overhauls of jet engines is performed by service providers in China and overseas. GAMECO performs all types of maintenance services, ranging from maintenance inspections performed on aircraft ("line maintenance services") to major overhaul performed at specified intervals. GAMECO was the first of three aircraft maintenance facilities in China having been certified as a repair station by both the CAAC and the Federal Aviation Administration. In March 1998, GAMECO received the Joint Civil Aviation Authorities certificate, which was transferred to European Aviation Safety Agency certification in November 2004, for the repair and maintenance of aircraft and aircraft engines.

The Group believes that GAMECO performs major maintenance checks on the Group's aircraft within time periods generally consistent with those of large international airline maintenance centers. GAMECO's repair and maintenance capacity include overhaul of more than 70% of the Group's aircraft. Although rotables for the Group's aircraft are generally imported through SAIETC, a portion of expendables and other maintenance materials are directly imported by GAMECO. GAMECO also provides line maintenance services to other seven Chinese airlines and 21 international airlines. GAMECO provides heavy maintenance services to twelve other Chinese airlines and eleven international airlines. Our agreement with GAMECO usually has a term of one year.

Overhauls of jet engines are performed by Zhuhai MTU, a former jointly controlled entity of the Company and MTU Aero Engines GmbH, and also by domestic qualified service providers in Beijing (AMECO), Xiamen (TEXL) and Hong Kong (HAESL), and by overseas qualified service providers in England, Korea, Singapore, Brazil, Canada and Poland. On September 28, 2009, the Company entered into an agreement with CSAHC to sell its 50% equity interest in Zhuhai MTU to CSAHC at a consideration of RMB1,607,850,000. The transfer was completed in February 2010.

The amounts incurred by the Group for comprehensive maintenance services provided by GAMECO and Zhuhai MTU were RMB2,579 million, RMB2,298 million and RMB2,018 million for the years ended December 31, 2013, 2012 and 2011, respectively.

## Safety

The Group endeavors to maintain strict compliance with all laws and regulations applicable to flight safety. In addition, the Group has adopted measures to eliminate or minimize factors that may impair flight safety, including

specialized training programs and safety manuals. The Air Safety Management Department of the Company implements safety-related training programs on an ongoing basis in all of the Group's operations to raise the safety awareness of all employees. As a result, overall flight safety has gradually improved. For minor "incidents" which include various events and conditions prescribed by the CAAC which do not involve serious personal injury or material damage to flight equipment, the Group has kept the number consistently below what is prescribed by the CAAC. For example, the Company's "Accident Signs Per Ten Thousands Hours Ratio" was 0.02, 0.036 and 0 in 2013, 2012 and 2011, respectively. In comparison, CAAC's published maximum acceptable Accident Signs Per Ten Thousands Hours Ratio was 0.5, 0.5 and 0.5 in 2013, 2012 and 2011, respectively. This ratio is defined as the occurrence of one incident for every 10,000 hours of flight time. In 2013, the Group strengthened its flight safety management on the internal and external safety requirements. In 2008, the Group received the "Five-Star Flight Safety Award" from CAAC, being the first in the aviation industry to receive such a great honor. Subsequently in 2012, we were awarded the "Safe Flight Diamond Award" by CAAC for our 10,000,000 safety flight hours record, also being the first in the aviation industry to receive such a great honor. By December 31, 2013, the Company's continuous safe flight span totaled to 11.87 million hours.

## **Jet Fuel**

Jet fuel costs typically represent a major component of an airline's operating expenses. The Group's jet fuel costs accounted for 36.2%, 39.0% and 37.5% of the Group's operating expenses for the years ended December 31, 2013, 2012 and 2011, respectively. Like all Chinese airlines, the Group is generally required by the Chinese government to purchase its jet fuel requirements from regional branches of CAOSC and Bluesky Oil Supplies Company, except at the Shenzhen, Zhuhai, Sanya, Haikou, Shanghai Pudong and other small airports where jet fuel is supplied by Sino-foreign joint venture in which CAOSC is a joint venture partner. CAOSC is a State-owned organization controlled and supervised by the CAAC that controls the importation and distribution of jet fuel throughout China.

Jet fuel obtained from CAOSC's regional branches is purchased at uniform prices throughout China that are determined and adjusted by CAOSC from time to time with the approval of the CAAC and the pricing department of the NDRC based on market conditions and other factors. As a result, the costs of transportation and storage of jet fuel in all regions of China are spread among all domestic airlines. Jet fuel costs in China are influenced by costs at state-owned oil refineries and limitations in the transportation infrastructure, as well as by insufficient storage facilities for jet fuel in certain regions of China.

Prior to 1994, domestic jet fuel prices were generally below international jet fuel prices. The Chinese government had gradually increased domestic jet fuel prices in order to reflect more accurately the costs of supplying jet fuel in China. As a result, domestic jet fuel prices have become higher than those in the international market since the beginning of 1994. In 2007 through the first half of 2008, the crude oil prices in the international market reached historic highs. In response to the pressure imposed by such soaring prices, on November 1, 2007 and June 20, 2008, respectively, NDRC increased the domestic price for jet fuel. Thereafter, in order to reduce fuel cost pressure faced by Chinese airlines, NDRC approved reductions in domestic prices for jet fuel in 2008 and 2009. However, starting from February 2009, the crude oil price in the international market continued to increase and maintained at a high level in 2013. As a result, the domestic price for jet fuel has increased significantly from RMB4,020 per ton in May 2009 to RMB7,885 per ton in March 2013. Our jet fuel costs decreased from RMB37,401 million in 2012 to RMB35,538 million in 2013 as a result of a decrease in average jet fuel prices from 2012 to 2013.

In addition to purchases of jet fuel from CAOSC, the Group is also permitted by the Chinese government to purchase a portion of its jet fuel requirements for its international flights from foreign fuel suppliers located outside China at prevailing international market prices. Jet fuel purchased from such sources outside China accounted for approximately 12.6% and 12.0% of the Group's total jet fuel consumption in 2013 and 2012, respectively.

### **Fuel Surcharge**

The NDRC has lowered the rate of fuel surcharge from 0.00002691 per kilometer to 0.00002541 per kilometer, starting from April 1, 2012 and ending on March 31, 2013. Based on that rate, for every RMB100 by which the cost of jet fuel exceeds RMB4,140 per ton, the airlines are allowed to charge RMB0.00002541 per kilometer for the flight distance. The Group's profit for the year may suffer from an unexpected change in the fuel surcharge collection policies and other factors beyond our control.

### **Flight Operations**

Flight operations for the Group's flights originating in Guangzhou are managed by our flight operations and marketing divisions, which are responsible for formulating flight plans and schedules consistent with route and flight approvals

received from the CAAC. The Company's flight operations center in Guangzhou is responsible for the on-site administration of flights, including the dispatch and coordination of flights, deployment of aircraft, ground services and crew staffing. In addition, each of the Airline Subsidiaries maintains flight operations centers at all servicing airports for on-site administration of their flights. Our general dispatch offices are responsible for monitoring conditions of the Group's route network, administering the Group's flight plans, collecting and monitoring navigation data and analyzing and monitoring airport conditions.

To enhance its management of flight operations, the Group's computerized flight operations control system (SOC) began operation in May 1999. The system utilizes advanced computer and telecommunications technology to manage the Group's flights on a centralized, real-time basis. The Group believes that the system will assist it to (i) compile flight schedules more efficiently; (ii) increase the utilization of aircraft; (iii) allow real-time tracking of all of the Group's flights; and (iv) improve coordination of the Group's aircraft maintenance and ground servicing functions.

### **Training of Pilots and Flight Attendants**

The Group believes that its pilot training program, which was established in cooperation with the CAAC affiliated Beijing University of Aeronautics and Astronautics (the "BUAA"), has significantly improved the quality of the training received by the Group's pilots and has helped maintain the quality of the Group's staff of pilots at a level consistent with the expansion of operations called for by the Group's business strategy.

In the Group's pilot training program, trainees have two years of theoretical training at the BUAA. After successful completion of academic and physical examinations, the trainees receive flight training for a period of approximately 20 months at the Flying College, a company that is 48.12% owned by the Company, 4.76% owned by CSAHC and 47.12% owned by a third party shareholder. Each trainee at the Flying College is required to fly at least 250 hours before being awarded a flight certificate. Graduates of the BUAA and the Flying College are hired by the Group as trainee pilots after passing a CAAC-administered examination to obtain a pilot license. The total training period for the Group's trainee pilots is approximately four years. The Group had 407 trainees as of April 18, 2014. Approximately 380 trainees are expected to graduate by the end of 2014.

As part of the pilot training program, trainee pilots receive their initial training in the operation of a specific aircraft with Zhuhai Xiang Yi Aviation Technology Company Limited ("Zhuhai Xiang Yi"), a jointly controlled entity between the Company and CAE International Holdings Limited, which also provides training to pilots from other Chinese airlines. Zhuhai Xiang Yi is equipped with simulators for majority models of aircraft currently operated by the Group and provides flight simulation training services to the Group.

The Group's pilots are required to be licensed by the CAAC, which requires an annual proficiency check. The Group's pilots attend courses in simulator training twice annually and in emergency survival training once annually. The Group also conducts regular advanced training courses for captains and captain candidates. Pilots advance in rank based on number of hours flown, types of aircraft flown and their performance history.

The Group funded the training of its recruited pilots in previous years and, as a result, incurred significant costs over the years. Recently, there has been a trend in the financing of pilot training worldwide from employer-sponsored to self-sponsored scheme. Such a change will not only cut down the Group's training expenses significantly, but also ensures the long-term dedicated service of the pilots. Starting from 2007, the Group began to recruit pilots under the self-sponsored training arrangement. On December 5, 2007, August 27, 2008, August 27, 2009, August 26, 2010 and September 9, 2011, the Board approved the Company to provide a guarantee with joint liability for the loans incurred under the self-sponsored pilot training program in an aggregate amount of RMB90,858,000, not more than RMB213,600,000, not more than RMB184,750,000, not more than RMB179,269,600 and not more than RMB83,850,000, respectively. On December 29, 2009, Xiamen Airlines, 51% owned subsidiary of the Company agreed to provide a guarantee with joint liability for the loans incurred under the partial self-sponsored pilot training program in an aggregate amount of not more than RMB100 million up to December 31, 2013. As of December 31, 2013, the Group has provided guarantees with joint liability for the loans of such self-sponsored pilots in an aggregate amount of RMB656,000,000 under which an aggregate of personal bank loans of RMB464,000,000 were drawn down from the banks. For the year ended December 31, 2013, the Group made repayments of RMB6,000,000 due to the default of payments of certain pilot trainees.

Under the program, the self-sponsored pilots are bound to enter into service contracts with the Group when they finish their training courses. They have the choice to repay their loans in advance or in installments.

The Group conducts theoretical and practical training programs for its flight attendants at its Flight Attendants Training Center in Guangzhou (the “Guangzhou Training Center”). The Guangzhou Training Center is equipped with computerized training equipment, as well as simulator cabins for all models of aircraft currently operated by the Group. At the Guangzhou Training Center, flight attendants of the Group receive comprehensive training in areas such as in-flight service, emergency evacuation and water rescue.

## **Ground Services**

The Group makes arrangements with airport authorities, other airlines or ground services companies for substantially all ground facilities, including runway, ramp, terminal and support services buildings, at each airport that it serves. The Group pays landing, parking and other fees to such airports, including Guangzhou Baiyun International Airport (the “Guangzhou Baiyun Airport”). At domestic airports, such fees are generally determined by the CAAC.

At Guangzhou Baiyun Airport, the Group operates its own passenger check-in, cargo, mail and baggage handling, aircraft maintenance and cleaning services. The Group also provides such services to its customer airlines that operate in Guangzhou Baiyun Airport.

Ground services at the airports, such as those in Shenzhen, Changsha, Wuhan, Zhengzhou, Haikou, Zhuhai, Xiamen, Guilin, Jieyang, Guiyang, Shenyang, Harbin, Dalian, Changchun, Sanya, Nanning, Chongqing, Shanghai Hongqiao, Shanghai Pudong and Urumqi, are operated directly by the Group. Ground services at the airport in Beijing have been primarily provided by Beijing China Southern Airlines Ground Services Co., Ltd, which became a wholly-own subsidiary of the Company in June 2009. Ground services at other airports in China are provided to the Group by local airport authorities or local airlines pursuant to various service agreements. Ground services and other services at airports outside China are provided to the Group by foreign services providers pursuant to various service agreements with such parties. All such agreements of the Group are short-term and otherwise on terms that are customary in the industry.

## **Air Catering**

We own a 55% equity interest in Guangzhou Nanland Air Catering Company Limited (“Nanland”). Nanland provides in-flight meals, snacks, drinks and related services for all of the Group’s flights originating in Guangzhou and substantially all other flights departing from Guangzhou Baiyun Airport. The Group contracts with various air catering suppliers with respect to in-flight catering services for flights originating from other airports, generally on an annual basis and otherwise on terms that are customary in the industry.

In order to optimize assets structure, tighten cost control, reduce the number of connected transactions and enhance the independence of operations in the long-run, the Company acquired a 100% equity interest in China Southern Airlines Group Air Catering Company Limited (“SAG Air Catering”) on August 31, 2007 from CSAHC. SAG Air Catering provides in-flight meals for flights of the Group originating or stopping at domestic airports, mainly in northern China and Xinjiang regions.

## **Cargo and Mail**

The Group also provides air cargo and mail services. A significant portion of these services are combined with passenger flights services. Currently, the Group has two Boeing 747 freighters and eight Boeing 777 freighters, mainly servicing 13 international cargo routes, including Guangzhou – Amsterdam – Guangzhou, Guangzhou – Chongqing – Amsterdam – Guangzhou, Guangzhou – Frankfurt – Guangzhou, Guangzhou – Hangzhou – Los Angeles – Guangzhou, Guangzhou – Qingdao – Los Angeles – Zhengzhou – Guangzhou, Shanghai Pudong – Amsterdam – Chongqing – Shanghai Pudong, Shanghai Pudong – Amsterdam – Shanghai Pudong, Shanghai Pudong – Amsterdam – Vienna – Shanghai Pudong, Shanghai Pudong – Anchorage – Chicago – Shanghai Pudong, Shanghai Pudong – Zhengzhou – Anchorage – Chicago – Shanghai Pudong, Shanghai Pudong – Frankfurt – Shanghai Pudong, Shanghai Pudong – Los Angeles – Shanghai Pudong and Shanghai Pudong – Los Angeles – Vancouver – Shanghai Pudong. The Group conducts its cargo business primarily through its cargo hubs in Guangzhou and Shanghai.

## **Sales, Reservations and Marketing**

### ***Passenger Ticket Sales and Reservations***

The Group’s ticket sales and reservations are conducted by or through independent sales agents and the Group’s own network of exclusive sales offices as well as the CAAC’s sales offices and CSAHC’s affiliates. The Group has sales offices in Guangzhou and its other route bases. In addition, the Group maintains regional sales offices in other cities in

China, including Beijing and Shanghai. The Group maintains international sales offices in Almaty, Amsterdam, Ashkhabad, Auckland, Baku, Bangkok, Bishkek, Brisbane, Busan, Chicago, Daegu, Daejeon, Delhi, Dubai (Sharjah), Dushanbe, Frankfurt, Fukuoka, Hanoi, Hiroshima, Ho Chi Minh City, Irkutsk, Islamabad, Jakarta, Jeddah, Kathmandu, Khabarovsk, Khudzhand, Kitakyushu, Kuala Lumpur, London, Los Angeles, Manila, Melbourne, Moscow, Nagoya, Niigata, Novosibirsk, Oakland, Osaka, Osh, Paris, Penang, Perth, Phnom Penh, Phuket, Sapporo, Sendai, Seoul, Siem Reap, Singapore, Sydney, Tashkent, Tehran, Tokyo, Toyama, Tbilisi, Vancouver, Vladivostok, Vienna and Yangon.

The Group has agency agreements with airlines in the Asia-Pacific region, Europe, the United States and Africa for the processing of ticket sales and reservations on a reciprocal basis. In 2013, approximately 20.5% of all ticket sales for the Group's scheduled flights were made by the Group's network of sales offices and CSAHC's affiliates. The Group also sells tickets and accepts reservations through an extensive network of non-exclusive independent sales agents. Under the agency agreements with these sales agents, the Group pays commissions based on the value of tickets sold. The Group pays independent sales agents a commission of 5.54% of the ticket price. Sales agents are typically permitted to withhold their commission from the proceeds of ticket sales that are remitted to the Group. In 2013, sales by independent sales agents accounted for approximately 79.5% of the Group's ticket sales of its scheduled flights.

Substantially all of the Group's sales offices and agents in China are linked electronically to the CAAC's computerized ticketing and reservations system, which is in turn linked to all domestic airlines for flights throughout China. The Group has also entered into membership agreements with several international reservation systems, including ABACUS in Southeast Asia, SABRE and GALILEO in the United States, AMADEUS in Europe and INFINI in Japan. These systems facilitate reservations and sales of tickets for the Group's international flights. In 2008, the Group further improved and optimized its online sales network, and launched Tencent sales counters in cooperation with Tencent Technology Limited, thus expanded the consumer sales network of the Group. Meanwhile, the Group upgraded and reconstructed the SMS platform, which provided SMS information services on mileage, flight schedule, flight status and air ticket price, and launched the "95539" services hotlines.



### ***Cargo***

The Group's cargo and mail services are promoted through its own cargo divisions and independent cargo agents both within and outside China that track available space among all airlines. In particular, the Group employs a number of cargo agents in the Pearl River Delta region. The Group generally pays such agents a commission of 3% to 4% of the relevant cargo freight rate for domestic and international services.

### ***Promotional and Marketing Activities***

The Group engages in regular promotional and marketing activities in an effort to increase its market share. The Group's promotional and marketing activities for domestic routes emphasize safety, passenger comfort and the frequency of the Group's flights. The Group's promotional and marketing activities for international and regional passengers emphasize the Group's quality of service, extensive route network in China and greater frequency of flights relative to other Chinese airlines. The Group was among the first to launch premium economy class of seating. In addition, the Group also promotes and markets its regional and international routes on the basis of price competitiveness.

The Group seeks to increase its name recognition by offering new services to passengers. For example, the Group was the first Chinese airline to provide off-airport check-in services. The Group also offered transfer and baggage "through-handling" services to passengers connecting to other airlines, including passengers connecting in Hong Kong for flights to Taiwan. The Group widened its use of information technology and introduced new services such as cell phone check-in and SMS platforms. During the Beijing Olympic Games, the Group launched a special promotion known as "Welcome the Olympic Games with Gold Medal Services" and successfully fulfilled its duties to deliver quality services for the Beijing Olympic Games and Paralympics Games. In 2010, the Group successfully completed its missions to deliver quality services for the 16th Asian Games held in Guangzhou and the World Exposition Shanghai. In preparation for the hosting of the Asian Games, Guangzhou has made a huge investment in urban renovation and the construction of sports facilities. In addition, there was high consumption before, during and after the Asian Games. Ever since the successful bidding for hosting the Asian Games in 2004, Guangzhou has achieved a faster growth and improvement in its economy. Even though during the Asian Games, the aviation market did not show a marked growth trend due to a stricter security policy and there was few changes in the pattern of the normal cycle of travelers entering and leaving Guangzhou in the long run, the Asian Games will have a positive impact on the tourism and the aviation market in Guangzhou to a certain extent.

On the wake of permitted direct flights on weekends between Taiwan and Mainland China starting from July 4, 2008, the Company became the first Chinese carrier to fly nonstop to Taiwan. By taking advantage of such further liberalized air travel policy between Taiwan and Mainland China, the Company has taken measures to explore opportunities presented by and increase its name recognition in Taiwan market. On June 23, 2008, the Company entered into a memorandum of cooperation with China Airlines, which is the largest carrier in Taiwan by route

network. Based on the memorandum, the scope of cooperation between the parties will cover passenger, cargo, maintenance and ground handling services. The Company believes that its strategic collaboration with China Airlines will be beneficial to both parties, expand their route network worldwide, increase their freight load factors, reduce labor and operating costs, and enhance the competitiveness of both airlines in the global air travel market.

To enhance relationships with its passengers, the Group has launched two frequent flyer programs, namely the “China Southern Airlines Sky Pearl Club” and the “Xiamen Airlines’ Egret Card Frequent Flyer Program”. By the end of 2013, the Group had approximately 21,795,200 members (including those of Xiamen Airlines) under these programs.

## **Regulation**

The Chinese commercial aviation industry is subject to a high degree of regulation and oversight by the CAAC. Regulations and policies issued or implemented by the CAAC encompass substantially all aspects of airline operations, including route allocation, pricing of domestic airfare, the administration of air traffic control systems and certain airports, air carrier certifications and air operator certification and aircraft, registration and aircraft airworthiness certification. The Civil Aviation Law, which became effective in March 1996, provides a framework for regulation of many of these aspects of commercial aviation activities. Although China’s airlines operate under the supervision and regulation of the CAAC, they are accorded an increasingly significant degree of operational autonomy, including with respect to the application for domestic, regional and international routes, the allocation of aircraft among routes, the purchase of flight equipment, the pricing of air fares within a certain range, the training and supervision of personnel and their day-to-day operations.

As an airline providing services on international routes, the Group is also subject to a variety of bilateral civil air transport agreements that provide for the exchange of air traffic rights between China and various other countries. In addition, China is a contracting state, as well as a permanent member, of the International Civil Aviation Organization (the “ICAO”), an agency of the United Nations established in 1947 to assist in the planning and development of international air transport, and is a party to many other international aviation conventions. The ICAO establishes technical standards for the international aviation industry. The Group believes that it, in all material respects, complies with all such technical standards.

### ***Route Rights***

*Domestic Routes.* The right of any Chinese airline to carry passengers or cargo on any domestic route must be obtained from the CAAC. Non-Chinese airlines are not permitted to provide domestic air service between destinations in China. The CAAC’s policy is to assign a domestic route to the Chinese airline that is best suited to serve the route based, in part, on the location of the airline’s main or regional base at the point of origin. Under current regulations, airlines are generally expected to operate mainly from their route bases, and flights within a particular region are expected to be served by airlines based in that region. The Group believes that these regulatory parameters benefit airlines, such as the Group, that have a large number of regional route bases. The CAAC also considers other factors that may make a particular airline suitable to operate a domestic route, including the applicant’s general operating authority, compliance with pricing regulations and regulations applicable to safety and service quality, market demand, the ability of the applicant in terms of its existing routes, airport facilities and related support services.

The CAAC considers market conditions for a domestic route in determining whether the route should be allocated to one or more airlines. Generally, the CAAC requires the passenger load factor on certain route should be above the average rate of the whole market in the last flight season before additional flights and participants may be put on that route.

*Regional Routes.* Hong Kong and Macau routes and landing rights are derived from agreements between the Chinese government and the government of the Hong Kong SAR, and between the Chinese government and the government of Macau SAR. The rights to fly between Beijing and Hong Kong, Beijing and Macau, Shanghai and Hong Kong and Shanghai and Macau are allocated by the CAAC among the four Chinese airlines. The Group understands that the criteria for determining whether a Hong Kong and Macau route will be allocated to a particular airline include market demand, the ability of the airline to service the route and the appropriateness of the airline’s aircraft for such route.

A number of Hong Kong routes are operated by Chinese airlines on a “charter” flight basis. Permission to operate these flights is in theory subject to monthly review by the CAAC and the Hong Kong Civil Aviation Department. The CAAC has informally indicated that it primarily considers market demand and airline capability in granting permission for such flights.

Previously, direct flights between Taiwan and Mainland China were only available during certain festivals. Since July 4, 2008, however, the ban on direct flights has been further liberalized to allow direct charter flights on weekends. On November 4, 2008, the Mainland China and Taiwan agreed to regular direct passenger charter flights across the Taiwan Strait. On August 31, 2009, the Mainland China and Taiwan extended the number of regular cross-Strait direct passenger flights from 108 to 270 a week. Cross-Strait direct passenger flights were further increased in the following years. As of April 18, 2014, there were 414 cross-Strait direct passenger flights a week.

*International Routes.* International route rights, as well as the corresponding landing rights, are derived from air services agreements negotiated between the Chinese government, through the CAAC, and the government of the relevant foreign country. Each government grants to the other the right to designate one or more domestic airlines to operate scheduled service between certain destinations within each of such countries. Upon entering into an air services agreement, the CAAC determines the airline to be awarded such routes based on various criteria, including the availability of appropriate aircraft, flight and management personnel, safety record, the overall size of the airline, financial condition and sufficiency of assets to bear civil liabilities in international air services. These route rights may be terminated by the CAAC under special circumstances.

The criteria for determining whether an international route will be allocated to a second airline generally include (i) the terms of the relevant bilateral civil aviation agreement; (ii) consistency with overall national plans and the national interest and the enhancement of reasonable competition; and (iii) whether the international airports to be used are sufficient for the aircraft flown and employ security measures consistent with international standards.

In addition, if the relevant bilateral civil aviation agreement permits more than one Chinese airline to operate a particular international route, the CAAC will only permit a second airline to operate on such route if during a specific season, the average load factor is more than 75%, or for a particular international route, if the flight capacity provided by Chinese airlines is 50% less than that provided by foreign airlines.

### ***Air Fare Pricing Policy***

Pursuant to “Pricing Reform of Domestic Civil Aviation” as approved by the State Council of the PRC effective on April 20, 2004, prices on domestic routes now fluctuate freely within a predetermined range. Instead of direct supervision by setting prices of air tickets through a local price bureau, the government now provides guidance on domestic flights and domestic civil aviation is controlled by the government indirectly. Market-oriented pricing policy was introduced and pricing system has been adjusted as a result of the above pricing reform. The CAAC and NDRC issued a notice on April 13, 2010, pursuant to which, effective on June 1, 2010, airlines may set first-class and business-class airfares freely in accordance with market prices, subject to relevant PRC laws. The economy-class airfares remain to be subject to the predetermined range. The CAAC and NDRC further issued a notice, pursuant to which, effective on October 20, 2013, airlines are free to set domestic flights airfares not exceeding up to 25% above the bench mark prices where governmental pricing guidance is applicable. Further, market-oriented pricing policy will be applied to certain designated domestic routes which are jointly operated by at least two airlines and which experience competition with other forms of public transportation.

Published air fares of Chinese airlines for the Hong Kong and Macau routes are determined by the CAAC and the relevant civil aviation authorities in Hong Kong or Macau, subject to consultation between the relevant Chinese airlines and Hong Kong or Macau airlines. Airlines may offer discounts on flights on their Hong Kong regional routes. With respect to the Taiwan routes, the air fares are currently determined by Chinese airlines at their own discretion and may be subject to certain pricing guidance to be issued by the CAAC in the future.

Published air fares of Chinese airlines for international routes are determined through consultation between the relevant Chinese airlines and foreign airlines in accordance with the civil aviation agreements between the Chinese government and the relevant foreign government, taking into account the international air fare standards established through the International Air Transport Association. All air fares for international routes must be approved by the CAAC. Discounting of published international air fares is permitted.

### ***Acquisition of Aircraft and Flight Equipment***

If a Chinese airline plans to acquire an aircraft, the airline must first seek approval from the CAAC and NDRC. The airline must, as a condition of approval, provide specific acquisition plans, which are subject to modification by the CAAC and NDRC. If the CAAC and NDRC approve an aircraft acquisition, the airline negotiates the terms of the acquisition with the manufacturer together with China Aviation Suppliers Import and Export Corporation (“CASC”), an entity controlled by CAAC, because CASC possesses the license required to import or export aircraft, and CASC receives a commission in respect thereof. Most Chinese airlines are also required to acquire their aircraft engines, spare parts and other flight equipment through CASC. The Company and a few other Chinese airlines are permitted to import jet engines and other flight equipment for their own use without the participation of CASC. In the case of the Company, SAIETC acts as its import agent and receives an agency fee for its services.

### ***Jet Fuel Supply and Pricing***

CAOSC and Bluesky Oil Supplies Company, companies supervised by the CAAC, are the only jet fuel supply companies in China, with the exception of the joint venture jet fuel supply companies that supply Shenzhen, Zhuhai, Sanya, Haikou, Shanghai Pudong and other small airports. Airlines are generally not permitted to buy jet fuel from other suppliers in their domestic operations, since the direct import of jet fuel for domestic purposes is prohibited. As a result, all Chinese airlines purchase their domestic jet fuel supply requirements (other than the above mentioned exceptions) from the seven regional branches of CAOSC. Jet fuel obtained from such regional branches is purchased at uniform prices throughout China that are determined and adjusted by CAOSC from time to time with the approval of the CAAC and the pricing department of the NDRC based on market conditions and other factors.

### ***Safety***

The CAAC has made the improvement of air traffic safety in China a high priority and is responsible for the establishment of operational safety, maintenance and training standards for all Chinese airlines. The Chinese airlines are required to provide monthly flight safety reports to the CAAC, including reports of flight or other incidents or accidents and other safety related problems involving such airline's aircraft occurring during the relevant reporting period. The CAAC periodically conducts safety inspections on individual airlines.

Every pilot is required to pass CAAC-administered examinations before obtaining a pilot license and is subject to an annual recertification examination.

All aircraft operated by Chinese airlines, other than a limited number of leased aircraft registered in foreign countries, are required to be registered with the CAAC. All aircraft operated by Chinese airlines must have a valid certificate of airworthiness, which is issued annually by the CAAC. In addition, maintenance permits are issued to a Chinese airline only after its maintenance capabilities have been examined and assessed by the CAAC. Such maintenance permits are renewed annually. All aircraft operated by Chinese airlines may be maintained and repaired only by CAAC-certified maintenance facilities, whether located within or outside China. Aircraft maintenance personnel must be certified by the CAAC before assuming aircraft maintenance posts.

### ***Security***

The CAAC establishes and supervises the implementation of security standards and regulations for the Chinese commercial aviation industry. Such standards and regulations are based on Chinese laws, as well as standards developed by international commercial aviation organizations. Each airline and airport in China is required to submit to the CAAC an aviation security handbook describing specific security procedures established by such airline or airport for the day-to-day operations of commercial aviation and procedures for staff training on security. Such security procedures must be based on relevant CAAC regulations and international commercial aviation treaties. Chinese airports and airlines that operate international routes must also adopt security measures in accordance with the requirements of the relevant international agreements.

### ***Noise and Environmental Regulation***

All airlines in China must comply with the noise and environmental regulations of the PRC State Environmental Protection Agency. Applicable regulations of the CAAC permit Chinese airports to refuse to grant take-off and landing rights to any aircraft that does not comply with noise regulations.

### ***Chinese Airport Policy***

The CAAC supervises and regulates all civilian airports in China. The local government of the PRC manages the administration of most civilian airports in China. Airports in China are also subject to regulation and ongoing review by the CAAC, which determines take-off and landing charges, as well as charges for the use of airports and airport services.

### *Competition*

The CAAC's extensive regulation of the Chinese commercial aviation industry has had the effect of managing competition among Chinese airlines. Nevertheless, competition has become increasingly intense in recent years due to a number of factors, including relaxation of certain regulations by the CAAC, an increase in the number of Chinese airlines and an increase in the capacity, routes and flights of Chinese airlines.

In the Chinese aviation industry, the three dominant airlines are the Group, Air China Limited (the "Air China") and China Eastern Airlines Corporation Limited (the "China Eastern Airlines"). In 2013, these three airlines together controlled approximately 69.7% of the commercial aviation market in China as measured by passengers carried.

Most major Chinese airlines have in recent years significantly expanded their fleets, while at the same time passenger traffic may not increase proportionately. In some years, this has resulted in a reduction in our passenger load factors. As a result, we are required to be more competitive with respect to, for example, quality of service, including ticketing and reservations, in-flight services, flight scheduling and timeliness.

The Group expects that competition in China's commercial aviation industry will continue to be intense. The Group will also face increasing competition from alternative means of transport, such as highway and rail, as China's transportation infrastructure improves. In particular, the so-called "Four Longitudinal and One Horizontal" high-speed railways have brought negative impact to the domestic commercial aviation sector.



In June 2011, the Beijing-Shanghai High-Speed Railway commenced operation. We currently have only one daily flight on the Beijing-Shanghai aviation route. The opening of the Beijing-Shanghai High-Speed Railway has had a little direct impact on us. The aviation routes along the way, in particular, short-haul routes have experienced a greater loss of customers, but such losses are within our expectations and have had minimal impact on the entire industry. In December 2012, the Beijing-Guangzhou and Harbin-Dalian High-Speed Railways commenced operation. The expansion of the coverage of this network, improvements in the railway service quality, increased passenger capacity and stations located closer to urban centers than competing airports could enhance the relative competitiveness of the railway service and affect our market share on some of our key routes, in particular routes below 800 kilometers. The aggregate high-speed railway mileage in China reached over 10,000 kilometers as of December 31, 2013. The construction of all railways in China's "Four Longitudinal and Four Horizontal" high-speed railway network is expected to complete by the end of 2014. We expect it will bring further negative impact on the domestic aviation industry.

From the perspective of long term development, with the continuous improvement in the high-speed railway lines and services, the domestic flights of the airlines will face competition from all sides, which spurs the airlines to constantly improve its network of aviation routes while stepping up efforts to upgrade service quality and brand influence for the enhancement of its competitiveness as a whole.

The Group believes that it possesses certain competitive advantages as compared to other Chinese airlines. The Group has the most extensive route network and the largest number of regional route bases among Chinese airlines, which the Group believes places it in a favorable position in the route allocation process. The Group also has the largest aircraft fleet among all Chinese airlines, which, together with the Group's planned aircraft acquisitions, will permit the Group to expand its operations and to improve the deployment of the aircraft in its fleet. The Group also believes that its dominant presence in the populous and economically developed southern and central regions of China provides it with a competitive advantage in attracting new customers and that its fully integrated flight training, aircraft and engine maintenance and air catering operations enable it to achieve and maintain high quality service to its customers. In light of increasing competition from high speed trains, the Group intends to place more flight fleet to the international routes, where the Group will make an effort for a stronger market position. The Group also believes that its optimized route network, increased operational efficiency and improved service quality will attract more customers. The proposed cooperation between the Company and the high speed trains operators will also enable the Group to render a seamless air-ground service to customers which will bring a win-win situation for both the Group and the high speed trains operators.

According to CAAC statistics, the following table sets forth the Group's market share of passengers carried, cargo and mail carried and total traffic of Chinese airlines for the years indicated.

Year	Passenger Carried		Cargo and Mail Carried		Total Traffic	
	Industry	Group's	Industry	Group's	Industry	Group's
	Total (in	Share	Total (in	Share	Total	Share
	millions)	(%	thousands)	(%	(in	(%

		of total)		of total)	billions)	of total)
2009	230.5	28.8	4,455	19.3	42.7	23.6
2010	267.7	28.6	5,630	19.8	53.8	24.3
2011	292.2	27.6	5,528	20.5	57.3	25.2
2012	319.4	27.1	5,450	22.6	61.0	26.6
2013	354.0	25.9	5,613	22.7	67.2	26.0

### ***Domestic Routes***

The Group competes against its domestic competitors primarily on the basis of flight schedule, route network, quality of service, safety, type and age of aircraft and, to a lesser extent and until recently, price. The Group competes against other major Chinese airlines in its various domestic route markets. Of these competitors, the largest are two airlines owned or controlled by the Chinese government, and the remaining airlines are operated by or under the control of various Chinese provincial or municipal governments.

The following table sets forth the Group's market share in terms of passengers carried, cargo and mail carried on departing flights and total departing flights at the ten busiest airports in China in 2013 according to passenger volume data from CAAC statistics.

Airport	Passenger Carried (% of total)		Cargo and Mail Carried (% of total)		Departing Flight (% of total)	
Beijing	16.7	%	10.8	%	17.0	%
Guangzhou	49.4	%	31.2	%	50.5	%
Shanghai Pudong	8.4	%	6.9	%	9.4	%
Shanghai Hongqiao	12.5	%	16.7	%	13.4	%
Shenzhen	27.2	%	14.2	%	25.2	%
Chengdu	12.3	%	11.5	%	12.2	%
Kunming	13.0	%	16.4	%	12.5	%
Xi'an	15.6	%	13.4	%	16.3	%
Hangzhou	29.4	%	20.1	%	29.2	%
Chongqing	23.9	%	19.8	%	25.6	%

The following table sets forth the Group's market share in terms of passengers carried, cargo and mail carried on departing flights and total departing flights at eight busiest airports in southern and central China (excluding Guangzhou and Shenzhen, which are included in the table above) in 2013 according to passenger volume data from CAAC statistics.

Airport	Passenger Carried (% of total)		Cargo and Mail Carried (% of total)		Departing Flight (% of total)	
Wuhan	37.7	%	37.4	%	35.4	%
Changsha	36.0	%	39.0	%	37.0	%
Haikou	24.0	%	29.6	%	22.6	%
Sanya	26.0	%	33.1	%	25.9	%
Zhengzhou	41.9	%	21.4	%	39.8	%
Guilin	34.8	%	40.2	%	35.5	%
Nanning	33.0	%	38.8	%	31.0	%

Zhang Jia Jie	25.4	%	27.5	%	29.3	%
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### ***Regional Routes***

In 2013, the Group conducted a total of 17,247 flights on its regional routes, accounting for approximately 23.5% of all passengers carried by Chinese airlines on routes between Hong Kong, Macau or Taiwan and destinations in China. The Group faces less competition on regional routes than that on domestic and international, and earns higher operating margin. Air China, Eastern Airlines, Air Macau, Dragon Air and Cathay Pacific Airways compete with the Group in the regional traffic markets.

### ***International Routes***

The Group competes with Air China, China Eastern Airlines and many well-established foreign airlines on its international routes. Most of these international competitors have significantly longer operating histories, substantially greater financial and technological resources and greater name recognition than the Group. In addition, the public's perception of the safety and service records of Chinese airlines may adversely affect the Group's ability to compete against its regional and international competitors. Many of the Group's international competitors have larger sales networks and participate in reservation systems that are more comprehensive and convenient than those of the Group, or engage in promotional activities that may enhance their ability to attract international passengers.

In Southeast Asian routes, our competitors mainly include Thai Airways International, Singapore Airlines, Malaysian Airlines System, Air China and China Eastern Airlines. In European routes, our competitors mainly include Air China, China Eastern Airlines, Cathay Pacific Airways and Lufthansa German Airlines. In the United States routes, our competitors mainly include Air China, China Eastern Airlines, Cathay Pacific Airways and United Airlines. In Australian routes, our competitors include Air China, China Eastern Airlines, Cathay Pacific Airways and Qantas Airways. The Group competes in the international market primarily on the basis of safety, price, timeliness and convenience of scheduling.

### ***Airline Subsidiaries***

The Airline Subsidiaries are joint ventures established by the Company and local companies in the provinces or special economic zones where the Airline Subsidiaries are based and are engaged in providing airline and related services. As of December 31, 2013, the Company owns a 51% or 60% equity interest in each of the Airline Subsidiaries.

As of December 31, 2013, Xiamen Airlines operated under its own "MF" code with a fleet of 101 aircraft on 142 domestic routes, 13 international routes and 16 regional routes. In 2013, Xiamen Airlines carried a total of about 18.57 million passengers, or approximately 20.2% of the passengers carried by the Group in that year, and had RMB15,792 million in traffic revenue.

As of December 31, 2013, Shantou Airlines operated under the Group's "CZ" code with a fleet of 13 aircraft. In 2013, under the centralized allocation of flight routes of the Group, Shantou Airlines carried a total of about 2.71 million passengers, or 3.0% of the passengers carried by the Group in that year. Total traffic revenue of Shantou Airlines for the year ended December 31, 2013 was RMB2,189 million.

As of December 31, 2013, Chongqing Airlines operated under the “OQ” code with a fleet of eleven aircraft. In 2013, under the centralized allocation of flight routes of the Group, Chongqing Airlines carried a total of about 2.11 million passengers, or 2.3% of the total number of passengers carried by the Group in that year. Total traffic revenue of Chongqing Airlines for the year ended December 31, 2013 was RMB1,514 million.

As of December 31, 2013, Zhuhai Airlines operated under the “CZ” code with a fleet of eight aircraft. In 2013, under the centralized allocation of flight routes of the Group, Zhuhai Airlines carried a total of about 1.39 million passengers, or approximately 1.5% of the total number of passengers carried by the Group in that year. Total traffic revenue of Zhuhai Airlines for the year ended December 31, 2013 was RMB1,318 million.

As of December 31, 2013, Guizhou Airlines operated under the “CZ” code with a fleet of 13 aircraft. In 2013, under the centralized allocation of flight routes of the Group, Guizhou Airlines carried a total of about 2.49 million passengers, or approximately 2.7% of the total number of passengers carried by the Group in that year. Total traffic revenue of Guizhou Airlines was approximately RMB2,162 million for the year ended December 31, 2013.

## **Insurance**

The CAAC maintains fleet and legal liability insurance on behalf of the Group and all other Chinese airlines with PICC Property and Casualty Company Limited, or PICCP&C, and China Pacific Property Insurance Company Ltd., under the PICCP&C master policy. The Group maintains aviation hull all risks, spares and airline liability insurance, aircraft hull all risks and spare engines deductible insurance, aviation hull war and allied perils policy of the type and in the amount customary in the Chinese aviation industry.

Under the relevant PRC laws, civil liability of Chinese airlines for death or injuries suffered by passengers on domestic flights is limited to RMB400,000 (approximately US\$65,607) per passenger. As of July 31, 2006, the Convention for the Unification of Certain Rules for International Carriage by Air of 1999, or Montreal Convention, became effective in China. Under the Montreal Convention, carriers of international flights are strictly liable for proven damages up to 100,000 Special Drawing Rights and beyond that, carriers are only able to exclude liability if they can prove that the damage was not due to negligence or other wrongful act of the carrier (and its agents), or the damage arose solely from the negligence or other wrongful act of a third party. The Group believes that it maintains adequate insurance coverage for the civil liability that can be imposed in respect of death or injuries to passengers under Chinese law, the Montreal Convention and any agreement which the Group is subject to.

The CAAC allocates insurance premiums payable in respect of the PICCP&C master policy to each participating airline based on the value of the airline's insured aircraft or, in the case of leased aircraft, based on the amount required by the terms of the lease. Insurance claims made by any participating airline may cause the premiums paid by the Group under the PICCP&C master policy to increase. PICCP&C's practice has been to reinsure a substantial portion of its aircraft insurance business through reinsurance brokers on the London reinsurance market.

## **Intellectual Property**

The Group's businesses and operations, other than the businesses and operations of Xiamen Airlines and Chongqing Airlines, are conducted under the names "China Southern" and "China Southern Airlines" in both English and Chinese. The Group uses as its logo a stylized rendition of a kapok plant. Xiamen Airlines conducts its businesses and operations under the name of "Xiamen Airlines" in English and Chinese and uses its own logo depicting a stylized rendition of an egret. Chongqing Airlines conducts its business and operations under the name of "Chongqing Airlines" in English and Chinese and uses its own logo depicting a cross of two rivers.

We own various trademarks and trade names related to our business. The names "China Southern" and "China Southern Airlines" contain Chinese words of common usage and are therefore not eligible for registration as trade names under current Chinese law. The kapok logo is a trademark registered in China and recorded with the International Air Transport Association ("IATA"), the rights to which are owned by CSAHC. The Company and CSAHC have entered into a trademark license agreement (the "Trademark License Agreement"), pursuant to which CSAHC has licensed to the Group the right to use the names "China Southern" and "China Southern Airlines" in both English and Chinese and granted the Company a ten-year renewable license from 1997 to use the kapok logo on a world-wide basis. CSAHC has retained the right to use the kapok logo in connection with its non-airline related businesses conducted as of the date of the Trademark License Agreement and to permit its affiliates that do not compete, directly or indirectly, with the Group to use the kapok logo. Unless CSAHC gives a written notice of termination three months before the expiration of the agreement, the agreement will be automatically renewed for another ten-year term. In May of 2007, the Trademark License Agreement has been automatically renewed by the two parties for another ten-year term ending 2017. Xiamen Airlines owns all rights to its egret logo, which is a trademark registered in China, and recorded with the IATA. Chongqing Airlines also owns all rights to its logo, which is a trademark registered in China, and recorded with the IATA.

C. Organizational Structure.

The following chart illustrates the corporate structure of the Group as of December 31, 2013 and the aggregate effective equity interest of the Company in each of its principal subsidiaries, associates and jointly controlled entities.



Note a: Including 12.89% ownership interest held by CSA's subsidiaries.

The particulars of the Group's principal subsidiaries as of December 31, 2013 are as follows:

Name of Company	Place and Date of Establishment/Operation	Proportion of Ownership Interest Held by the Company	
Shantou Airlines Company Limited	PRC July 20, 1993	60	%
Zhuhai Airlines Company Limited	PRC May 8, 1995	60	%
Xiamen Airlines Company Limited	PRC August 11, 1984	51	%
Guizhou Airlines Company Limited	PRC November 12, 1991	60	%
Chongqing Airlines Company Limited	PRC May 30, 2007	60	%
Guangzhou Nanland Air Catering Company Limited	PRC November 21, 1989	55	%
Guangzhou Baiyun International Logistic Company Limited	PRC July 23, 2002	61	%
Xinjiang Civil Aviation Property Management Limited	PRC December 12, 2002	51.84	%
China Southern Airlines Group Air Catering Company Limited	PRC December 25, 2003	100	%
Nan Lung International Freight Limited	Hong Kong October 1, 1996	51	%
Beijing Southern Airlines Ground Services Company Limited	PRC April 1, 2004	100	%
China Southern Airlines Henan Airlines Company Limited	PRC September 28, 2013	60	%

The particulars of the Group's principal associates and jointly controlled entities as of December 31, 2013 are as follows:

Name of Company	Place and Date of Establishment/Operation	Proportion of Ownership Interest Held by Group Effective Interest				The Company	Subsidiaries
Guangzhou Aircraft Maintenance Engineering Company Limited	PRC October 28, 1989	50	%	50	%	—	

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Southern Airlines Group Finance Company Limited	PRC June 28, 1995	33.98%	21.09	%	12.89%
Sichuan Airlines Corporation Limited	PRC August 28, 2002	39	%	39	% —
Zhuhai Xiang Yi Aviation Technology Company Limited	PRC July 10, 2002	51	%	51	% —
Southern Airlines Culture and Media Co., Ltd.	PRC May 13, 2004	40	%	40	% —
China Southern West Australian Flying College Pty Ltd.	Australia October 1, 1993	48.12%	48.12	%	—
Guangzhou China Southern Zhongmian Dutyfree Store Co., Limited	PRC March 1, 2001	50	%	50	% —

## D. Property, Plant and Equipment.

For a discussion of the Group's aircraft, see Item 4 "Information on the Company — History and development of the Company — Aircraft Acquisitions."

The Company's headquarters in Guangzhou occupy an area of approximately 1,172,531 square meters of land and a total gross floor area of approximately 693,860 square meters. The Company leases from CSAHC the land in Guangzhou on which the Company's headquarters and other facilities are located. The Company also leases from CSAHC certain buildings mainly at the Haikou, Wuhan, Nanyang, Shenyang, Dalian, Jilin, Harbin, Xinjiang and other PRC cities.

The Company's principal properties are located at its headquarters site and at its route bases. The following table sets forth certain information with respect to the Company's properties at its headquarters in Guangzhou and certain route bases as of the date hereof.

	Land (in square meters)		Building (in square meters)	
	Owned	Leased	Owned	Leased
Guangzhou	1,172,531	99,670	693,860	47,827
Shenzhen	256,280	—	101,502	—
Zhuhai	179,415	30,000	61,973	3,047
Changsha	302,794	11,386	97,100	8,860
Zhengzhou	449,290	—	73,391	9,270
Haikou	332,961	12,497	65,231	1,288
Wuhan	16,712	47,882	36,429	37,491
Nanyang	—	—	12,156	60,035
Sanya	106,680	—	38,513	5,421
Shenyang	142,199	39,582	130,303	64,804
Dalian	—	158,240	36,188	32,862
Jilin	134,488	65,076	78,536	7,767
Harbin	5,381	267,872	40,599	33,871
Xinjiang	2,143	631,094	137,932	3,396
Guangxi	108,133	—	61,093	2,892
Beijing	85,453	—	49,314	19,790
Shanghai	42,292	—	35,512	7,253
Chengdu	—	—	1,964	209
Sydney	—	—	1,151	2,449

The following table sets forth certain information with respect to the properties of the Airline Subsidiaries as of the date hereof.



	Land (in square meters)		Building (in square meters)	
	Owned	Leased	Owned	Leased
Xiamen Airlines	1,534,087	—	723,851	51,290
Shantou Airlines	260,639	53,000	73,499	2,407
Zhuhai Airlines	99,306	—	52,793	2,954
Guizhou Airlines	259,879	—	20,783	4,884
Chongqing Airlines	82,449	—	8,943	3,660

As systems for registration and transfer of land use rights and related real property interests in China have been implemented relatively recently, such systems do not yet comprehensively account for all land and related property interests. The land in Guangzhou on which the Company's headquarters and other facilities are located and the buildings that the Company uses at its route bases in Wuhan and Haikou are leased by the Company from CSAHC. However, CSAHC lacks adequate documentation evidencing CSAHC's rights to such land and buildings, and, as a consequence, the lease agreements between CSAHC and the Company for such land may not be registered with the relevant authorities. Lack of registration may affect the validity of such lease agreements. There are certain other parcels of land and buildings owned or used by the Group that lack adequate documentation. Lack of adequate documentation for land use rights and ownership of buildings may impair the ability of the Group to dispose of or mortgage such land use rights and buildings. As of April 18, 2014, the Group was in the process of applying for the land use right certificates and property title certificates in respect of the properties located in Guangzhou (including Guangzhou Baiyun International Airport), Xiamen, Heilongjiang, Jilin, Dalian, Nanning, Hunan, Beijing, Shanghai, Sanya, Zhuhai, Shenzhen, Shenyang, Xinjiang, Henan, Chengdu and Shantou in which the Group has interests and for which such certificates have not been granted. The directors of the Company are of the opinion that the use of and the conduct of operating activities at the properties referred to above are not affected by the fact that the Group has not yet obtained the relevant land use right certificates and property title certificates.

#### ITEM 4A. UNRESOLVED STAFF COMMENTS.

Not applicable.

#### ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS.

The following discussion and analysis should be read in conjunction with the Financial Statements of the Group contained elsewhere in this Annual Report. The Group maintains its books and accounts in accordance with the Accounting Standards for Business Enterprises-Basic Standard and 38 Specific Standards, application guidance, bulletins and other relevant accounting regulations (collectively "PRC GAAP") and prepares its financial statements in accordance with both PRC GAAP and IFRSs. The Financial Statements contained elsewhere in this Annual Report have been prepared in accordance with IFRSs.

The discussion and analysis of the Group's financial position and results of operations are based on the consolidated financial statements, which have been prepared in accordance with IFRSs.

### Critical Accounting Policies

The preparation of the consolidated financial statements requires the Group to make estimates and judgments that affect the reported amount of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of the consolidated financial statements. Actual results may differ from these estimates under different assumptions or conditions.

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, and potentially result in materially different results under different assumptions and conditions. Our principal accounting policies are set forth in Note 2 to the consolidated financial statements. The Group believes that the following critical accounting policies involve the most significant judgments and estimates used in the preparation of our financial statements.

#### *Impairment of account receivables*

Trade receivables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganization, and default or delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the assets is reduced through the use of an allowance account, and the amount of the loss is recognized in the income statement. When a trade receivable is uncollectible, it is written off against the provision account for trade receivables. Subsequent recoveries of amounts previously written off are credited in the income statement.

### ***Impairment for Long-lived Assets***

If circumstances indicate that the carrying amount of a long-lived asset may not be recoverable, the asset may be considered “impaired”, and an impairment loss may be recognized in accordance with IAS 36, Impairment of Assets. The carrying amounts of long-lived assets are reviewed periodically in order to assess whether the recoverable amounts have declined below the carrying amounts. These assets are tested for impairment whenever events or changes in circumstances indicate that their recorded carrying amounts may not be recoverable. When such a decline has occurred, the carrying amount is reduced to the recoverable amount. The recoverable amount is the greater of the fair value less costs to sell and value in use. In determining the value in use, expected cash flows generated by the asset are discounted to their present value, which requires significant judgment relating to the level of traffic revenue and the amount of operating costs. The Group uses all readily available information in determining an amount that is a reasonable approximation of recoverable amount, including estimates based on reasonable and supportable assumptions for projections of traffic revenue and amount of operating costs.

### ***Depreciation***

Property, plant and equipment are depreciated on a straight-line basis over the estimated useful lives, after taking into account the estimated residual value. The Group reviews the estimated useful lives of assets annually in order to determine the amount of depreciation expense to be recorded during any financial year. The useful lives are based on the Group’s historical experience with similar assets and take into account anticipated technological changes. The depreciation expense for future periods is adjusted if there are significant changes from previous estimates.

### ***Provision for Major Overhauls***

Provision for the cost of major overhauls to fulfill certain return condition for airframes and engines under operating leases is accrued and charged to the income statement over the estimated overhaul period. This requires estimation of the expected overhaul cycle and overhaul cost, which are based on the historical experience of actual cost incurred for overhauls of airframes and engines of the same or similar types. Different estimates could significantly affect the estimated provision and the results of operations.

### ***Frequent Flyer Revenue***

The amount of revenue attributable to the mileages earned by the members of the Group’s frequent flyer award programs is estimated based on the fair value of the mileages awarded and the expected redemption rate. The fair



value of the mileages awarded is estimated by reference to external sales. The expected redemption rate was estimated based on historical experience, anticipated redemption pattern and the frequent flyer program design.

***Provision for consumable spare parts and maintenance materials***

Provision for consumable spare parts and maintenance materials is made based on the difference between the carrying amount and the net realizable value. The net realizable value is estimated based on current market condition, historical experience and Company's future operation plan for the consumable spare parts and maintenance materials. The net realizable value may be adjusted significantly due to the change of market condition and the future plan for the consumable spare parts and maintenance materials.

**Recently Pronounced International Financial Reporting Standards**

Information relating to the recently pronounced IFRSs is presented in Note 2 to the consolidated financial statements.

## Overview

In 2013, the overall global economy was still on the basic trend of slow recovery, the risk of a deterioration of the economy was not completely removed, and a new round of growth had yet to appear. The Chinese economy entered into a period of deceleration after years of rapid growth, experiencing the short-term pain of structural adjustments and the aftermath of the earlier economic stimulus policies, all contributed to the fall back of growth rate.

Due to the impact of the macro economy, the global aviation transportation industry continued to be weak. The Chinese civil aviation market maintained a steady growth, but due to factors such as the diversion of business by the high-speed rail, the excess supply for the transport capacity in the industry, keener market competition, high oil prices etc, resulting in an increase of traffic volume with falling prices in the domestic market, and the quality of yield in the whole industry dropped significantly.

Faced with harsh operational conditions, the Company insisted on the concept of stable development, strengthened the establishment of the safety management system, enhanced the level of precise marketing, steadily promoted the strategic transformation and internationalization process, actively enhanced the service quality and brand influences, and effectively resolved the impact of various negative factors such as the complex and changing market, shortage of development resources, higher competition pressure etc, therefore the comprehensive competitiveness of the Company continued to be strengthened.

In 2013, we strengthened the standardized management of safety, adjusted and increased the power of safety management at all levels, enhanced the building up of qualifications and ability of the technical personnel, emphasized on the development and application of new technologies, well protected our continuous safety, and managed to maintain the best safety record among the Chinese airlines.

In 2013, we completed a total of 1,829,430 safe flight hours, representing an increase of 148,740 hours as compared with the previous year and accumulating safe flight hours to over 11.87 million, and maintained 170 consecutive months of aviation safety and 234 consecutive months of aviation security. We maintained the best safety record among airlines in China and were granted the “Safe Flight Diamond Award” by the Civil Aviation Administration of China.

In 2013, facing the difficult business environment, we actively adjusted and optimized the structure by untiringly consolidating the domestic market and developing international market and took efforts to increase income and strictly control cost, thereby effectively offset risks accompanying the economic downturn and the stagnation in the industry, and maintained our status in the industry. Furthermore, 15 aircraft were retired or returned upon expiration of lease terms and 85 new aircraft were added, which further optimized the fleet structure.

In 2013, we are actively committed to social responsibilities and smoothly completed several transportation protection missions such as maintaining peace and harmony, disaster relief, Chinese New Year passenger transportation and China National Games. We continued to conduct charity activities such as “Ten Cent Care Foundation”. We also thoroughly carried out energy saving and carbon dioxide emission reduction. We were awarded “The Most Appreciated Top 50 Chinese Companies” and “2013 Top 100 Green Companies”. We donated more than RMB7.1 million to “Ten Cent Care Foundation” fund and continued to contribute to the wider community.

Nevertheless, the development of the airlines industry meets with a number of challenges, such as more factors making the recovery of global economy unstable and uncertain, faster growth in the total traffic capacity of the industry, impact of substitutive services such as high-speed railway, as well as sharp fluctuation in oil price.

Because the Group finances its aircraft acquisitions mainly through capital leases or bank loans in U.S. dollars, and there are a substantial amount of transactions and obligations denominated in U.S. dollars in relation to its global purchases of jet fuel, lease and purchase of aviation equipment as well as major repairs, in addition to the landing fees of its international flights in the airports of other countries, the Group benefited from the Renminbi appreciation. Renminbi appreciation has brought exchange gain to the Group and reduced its operating costs which are denominated in foreign currencies. However, Renminbi appreciation also presents the Group with a challenge in price competition in international route operations.

The Group’s operating revenue is substantially dependent on the passenger and cargo traffic volume carried, which is subject to seasonal and other changes in traffic patterns, the availability of appropriate time slots for the Group’s flights and alternative routes, the degree of competition from other airlines and alternate means of transportation, as well as other factors that may influence passenger travel demand and cargo and mail volume. In particular, the Group’s airline revenue is generally higher in the second and third quarters than in the first and fourth quarters.

Like most airlines, the Group is subject to a high degree of financial and operating leverage. A significant percentage of the Group’s operating expenses are fixed costs that do not vary proportionally based on the Group’s yields or the load factors. These fixed costs include depreciation expense, jet fuel costs, landing and navigation fees, financing costs, operating lease payments, aircraft maintenance costs and labor for flight crew, cabin crew and ground personnel. Thus, a minor change in the Group’s yields or load factors would have a material effect on the Group’s results of operations. In addition, certain of these expenses, primarily financing costs and operating lease payments, labor costs and depreciation do not vary based on the number of flights flown. Thus, the Group’s operating results can also be substantially affected by minor changes in aircraft utilization rates. The Group is and will continue to be highly leveraged with substantial obligations denominated in foreign currencies and, accordingly, the results of its operations are significantly affected by fluctuations in foreign exchange rates, particularly for the U.S. dollar. Our net exchange gain increased by RMB2,636 million, from RMB267 million in 2012 to RMB2,903 million in 2013, mainly attributable to the significant appreciation of Renminbi appreciated significantly against U.S. dollar in 2013.

A number of other external variables, including political and economic conditions in China, tend to have a major impact on the Group's performance. The Group's financial performance is also significantly affected by factors arising from operating in a regulated industry. As substantially all aspects of the Group's airline operations are regulated by the PRC government, the Group's operating revenues and expenses are directly affected by the PRC government's policies with respect to domestic air fares, jet fuel prices and landing and navigation fees, among others. The nature and extent of airline competition and the ability of Chinese airlines to expand are also affected by CAAC's control over route allocations. Any changes in the PRC government's regulatory policies or any implementation of such policies could have a significant impact on the Group's future operations and its ability to implement its operating strategy.

#### Certain Financial Information and Operating Data by Geographic Region

The following table sets forth certain financial information and operating data by geographic region for the years ended December 31, 2013, 2012 and 2011:

	Year ended December 31,			2013 vs. 2012	2012 vs. 2011
	2013	2012	2011	% increase (decrease)	% increase (decrease)
Traffic					
RPK (million)					
Domestic	116,105.71	107,278.56	99,673.63	8.2	7.6
Regional	2,574.27	2,536.91	2,082.35	1.5	21.8
International	29,736.57	25,719.26	20,588.31	15.6	24.9
Total	148,416.55	135,534.73	122,344.29	9.5	10.8
RTK (million)					
Domestic	11,765.27	10,924.30	10,195.00	7.7	7.2
Regional	241.05	242.43	197.93	(0.6)	22.5
International	5,462.27	4,993.39	4,068.09	9.4	22.7
Total	17,468.59	16,160.12	14,461.02	8.1	11.7
Passengers carried (thousand)					
Domestic	82,172.28	77,634.23	72,926.29	5.9	6.5
Regional	2,019.28	1,928.54	1,766.56	4.7	9.2
International	7,599.41	6,922.22	5,984.18	9.8	15.7
Total	91,790.97	86,484.99	80,677.03	6.1	7.2
Cargo and mail carried (thousand tons)					
Domestic	923.73	890.38	856.91	3.8	3.9
Regional	13.70	15.66	12.77	(12.5)	22.6
International	338.92	325.82	265.45	4.0	22.7
Total	1,276.35	1,231.86	1,135.13	3.6	8.5

	Year ended December 31,			2013 vs. 2012	2012 vs. 2011
	2013	2012	2011	%increase (decrease)	%increase (decrease)
Capacity					
ASK (million)					
Domestic	144,732.62	131,821.86	120,462.20	9.8	9.4
Regional	3,594.29	3,464.29	2,752.53	3.8	25.9
International	38,472.93	34,282.98	27,849.37	12.2	23.1
Total	186,799.84	169,569.13	151,064.10	10.2	12.2
ATK (million)					
Domestic	16,486.17	15,069.70	14,145.21	9.4	6.5
Regional	407.59	396.74	316.35	2.7	25.4
International	8,058.23	7,598.25	6,333.84	6.1	20.0
Total	24,951.99	23,064.69	20,795.40	8.2	10.9
Load Factors					
Passenger load factor (RPK/ASK) (%)					
Domestic	80.2	81.4	82.7	(1.4)	(1.6)
Regional	71.6	73.2	75.7	(2.2)	(3.3)
International	77.3	75.0	73.9	3.0	1.5
Overall	79.4	79.9	81.0	(0.6)	(1.4)
Overall load factor (RTK/ATK) (%)					
Domestic	71.4	72.5	72.1	(1.6)	0.6
Regional	59.1	61.1	62.6	(3.2)	(2.4)
International	67.8	65.7	64.2	3.1	2.3
Overall	70.0	70.1	69.5	(0.1)	0.9
Yield					
Yield per RPK (RMB)					
Domestic	0.61	0.69	0.68	(11.6)	1.5
Regional	0.84	0.84	0.88	-	(4.5)
International	0.50	0.53	0.56	(5.7)	(5.4)
Overall	0.59	0.66	0.67	(10.6)	(1.5)
Yield per RTK (RMB)					
Domestic	6.24	6.96	6.90	(10.3)	0.9
Regional	9.33	9.20	9.69	1.4	(5.1)
International	3.49	3.57	3.67	(2.2)	(2.7)
Overall	5.42	5.95	6.03	(8.9)	(1.3)
Financial					
Passenger revenue (RMB million)					
Domestic	71,277	73,845	68,222	(3.5)	8.2
Regional	2,162	2,133	1,834	1.4	16.3
International	14,832	13,566	11,436	9.3	18.6
Total	88,271	89,544	81,492	(1.4)	9.9
Cargo and mail revenue (RMB million)	6,413	6,556	5,760	(2.2)	13.8

## A. Operating Results

The historical results of operations discussed below may not be indicative of the Group's future operating performance. In addition to the factors discussed under "Overview" above, the Group's future operations will be affected by, among other things, changes in the aviation market, the cost of jet fuel, aircraft acquisition and leasing costs, aircraft maintenance expenses, take-off and landing charges, wages, salaries and benefits and other operating expenses, foreign exchange rates and the rates of income taxes paid.

## **2013 Compared With 2012**

The profit attributable to equity shareholders of the Company of RMB1,986 million was recorded in 2013 as compared to the profit attributable to equity shareholders of the Company of RMB2,619 million in 2012. The Group's operating revenue decreased by RMB967 million or 1.0% from RMB99,514 million in 2012 to RMB98,547 million in 2013. Passenger load factor decreased by 0.5 percentage points from 79.9% in 2012 to 79.4% in 2013. Passenger yield (in passenger revenue per RPK) decreased by 10.6% from RMB0.66 in 2012 to RMB0.59 in 2013. Average yield (in traffic revenue per RTK) decreased by 8.9% from RMB5.95 in 2012 to RMB5.42 in 2013. Operating expenses increased by RMB2,403 million or 2.5% from RMB95,877 million in 2012 to RMB98,280 million in 2013. Operating profit of RMB1,510 million was recorded in 2013 as compared to operating profit of RMB5,099 million in 2012, decreased by RMB3,589 million.

*Operating Revenue*

	2013		2012		Change in revenue %
	Operating revenue RMB million	Percentage %	Operating revenue RMB million	Percentage %	
Traffic revenues	94,684	96.1	96,100	96.6	(1.5 )
Including: Passenger revenues	88,271		89,544		(1.4 )
– Domestic	71,277		73,845		(3.5 )
– Hong Kong, Macau and Taiwan	2,162		2,133		1.4
– International	14,832		13,566		9.3
Cargo and mail revenues	6,413		6,556		(2.2 )
Other operating revenues	3,863	3.9	3,414	3.4	13.2
Mainly including: Commission income	1,040		757		37.4
Ground services income	349		350		(0.3 )
Expired sales in advance of carriage	684		495		38.2
General aviation income	484		445		8.8
Hotel and tour operation income	565		647		(12.7 )
Total operating revenues	98,547	100.0	99,514	100.0	(1.0 )
Less: fuel surcharge income	(13,062)		(13,378)		
Total operating revenue excluding fuel surcharge	85,485		86,136		

*Traffic revenue composition*

	2013		2012		Change in traffic revenue
	Traffic revenue		Traffic revenue		
	RMB	Percentage	RMB	Percentage	
	million	%	million	%	%
Passenger Revenues	88,271	93.2	89,544	93.2	(1.4 )
Cargo and Mail Revenues	6,413	6.8	6,556	6.8	(2.2 )
Traffic revenues	94,684	100.0	96,100	100.0	(1.5 )

*Passenger revenue composition*

	2013		2012		Change in passenger revenue
	Passenger revenue	Percentage	Passenger revenue	Percentage	
	RMB million	%	RMB million	%	
Domestic	71,277	80.8	73,845	82.5	(3.5 )
Hong Kong, Macao and Taiwan	2,162	2.4	2,133	2.4	1.4
International	14,832	16.8	13,566	15.1	9.3
Passenger revenue	88,271	100.0	89,544	100.0	(1.4 )

Substantially all of the Group's operating revenue is attributable to airline and airline-related operations. Traffic revenue accounted for 96.1% and 96.6% of total operating revenue in 2013 and 2012 respectively. Passenger revenue and cargo and mail revenue accounted for 93.2% and 6.8% respectively of the total traffic revenue in 2013. During the reporting period, the Group's total traffic revenues was RMB94,684 million, representing a decrease of RMB1,416 million or 1.5% from prior year, mainly due to the VAT reform which leads to the decrease of domestic revenues of RMB4,798 million. The other operating revenue is mainly derived from commission income, expired sales in advance of carriage hotel and tour operation income, general aviation income and ground services income.

The decrease in operating revenue was primarily due to a 1.4% decrease in passenger revenue from RMB89,544 million in 2012 to RMB88,271 million in 2013. The total number of passengers carried increased by 6.1% to 91.79 million passengers in 2013. RPKs increased by 9.5% from 135,535 million in 2012 to 148,417 million in 2013, primarily as a result of the increase in number of passengers carried. Passenger yield per RPK decreased from RMB0.66 in 2012 to RMB0.59 in 2013, which is mainly due to the impact from VAT reform.



Domestic passenger revenue, which accounted for 80.8% of the total passenger revenue in 2013, decreased by 3.5% from RMB73,845 million in 2012 to RMB71,277 million in 2013. Domestic passenger traffic in RPKs increased by 8.2%, while passenger capacity in ASKs increased by 9.8%, resulting in a decrease in passenger load factor by 1.2 percentage points from 81.4% in 2012 to 80.2% in 2013. Domestic passenger yield per RPK decreased from RMB0.69 in 2012 to RMB0.61 in 2013.

Hong Kong, Macau and Taiwan passenger revenue, which accounted for 2.4% of total passenger revenue, increased by 1.4% from RMB2,133 million in 2012 to RMB2,162 million in 2013. For Hong Kong, Macau and Taiwan flights, passenger traffic in RPKs increased by 1.5%, while passenger capacity in ASKs increased by 3.8%, resulting in a decrease in passenger load factor by 1.6 percentage points from 73.2% in 2012 to 71.6% in 2013. Passenger yield per RPK remained at RMB0.84 in 2012 and 2013.

International passenger revenue, which accounted for 16.8% of total passenger revenue, increased by 9.3% from RMB13,566 million in 2012 to RMB14,832 million in 2013. For international flights, passenger traffic in RPKs increased by 15.6%, while passenger capacity in ASKs increased by 12.2%, resulting in a 2.3 percentage points increase in passenger load factor from 75.0% in 2012 to 77.3% in 2013. Passenger yield per RPK decreased from RMB0.53 in 2012 to RMB0.50 in 2013.

Cargo and mail revenue, which accounted for 6.8% of the Group's total traffic revenue and 6.5% of total operating revenue, decreased by 2.2% from RMB6,556 million in 2012 to RMB6,413 million in 2013. The decrease was attributable to the continued downturn of the demand in the cargo market and the low level cargo fare.

Other operating revenue increased by 13.2% from RMB3,414 million in 2012 to RMB3,863 million in 2013. The increase was primarily due to the general growth in income from commission and expired sales in advance of carriage.

### ***Operating Expenses***

Total operating expenses in 2013 amounted to RMB98,280 million, representing an increase of RMB2,403 million or 2.5% over 2012, primarily due to the total effect of increases in payroll, landing and navigation fees, depreciation and amortization, and other operating costs. Total operating expenses as a percentage of total operating revenue was 99.7% in 2013 and 96.3% in 2012.

2013

2012

	Operating expense RMB million	Percentage %	Operating expense RMB million	Percentage %	Change in operating expenses %
Flight operations	54,010	55.0	54,690	57.0	(1.2 )
Mainly including: Jet fuel costs	35,538		37,401		(5.0 )
Aircraft operating lease charges	4,767		4,897		(2.7 )
Flight personnel payroll and welfare	5,799		5,051		14.8
Maintenance	7,805	7.9	7,971	8.3	(2.1 )
Aircraft and traffic servicing expenses	15,091	15.4	14,072	14.7	7.2
Promotion and selling expenses	7,754	7.9	7,134	7.5	8.7
General and administrative expenses	2,470	2.5	2,425	2.5	1.9
Depreciation and amortization	9,347	9.5	8,264	8.6	13.1
Impairment on property, plant and equipment	536	0.5	-	-	-
Others	1,267	1.3	1,321	1.4	(4.1 )
Total operating expenses	98,280	100.0	95,877	100.0	2.5

Flight operations expenses, which accounted for 55.0% of total operating expenses, decreased by 1.2% from RMB54,690 million in 2012 to RMB54,010 million in 2013, primarily as a result of decrease in jet fuel costs because of decrease in average fuel prices. Jet fuel costs, which accounted for 65.8% of flight operations expenses in 2013, decreased by 5.0% from to RMB37,401 million in 2012 to RMB35,538 million in 2013.

Maintenance expenses, which accounted for 7.9% of total operating expenses, decreased by 2.1% from RMB7,971 million in 2012 to RMB7,805 million in 2013. The decrease was mainly due to the impact of the VAT reform.

Aircraft and traffic servicing expenses, which accounted for 15.4% of total operating expenses, increased by 7.2% from RMB14,072 million in 2012 to RMB15,091 million in 2013. The increase was primarily due to a 5.9% rise in landing and navigation fees from RMB8,984 million in 2012 to RMB9,510 million in 2013, resulted from the increase in number of take-off and landings and the average unit price of take-off and landing charges.

Promotion and selling expenses, which accounted for 7.9% of total operating expenses, increased by 8.7% from RMB7,134 million in 2012 to RMB7,754 million in 2013.

General and administrative expenses, which accounted for 2.5% of the total operating expenses, increased by 1.9% from RMB2,425 million in 2012 to RMB2,470 million in 2013.

Depreciation and amortization, which accounted for 9.5% of total operating expenses, increased by 13.1% from RMB8,264 million in 2012 to RMB9,347 million in 2013, mainly due to the additional depreciation charges on aircraft delivered in 2013.

### ***Operating Profit***

Operating profit of RMB1,510 million and RMB5,099 was recorded in 2013 and 2012 respectively. The decrease in profit was mainly due to the net effect of decrease in operating revenue by RMB967 million or 1.0% in 2013 and increase in operating expenses by RMB2,403 million or 2.5%.

### ***Other Income or Expenses***

Other net income decreased by RMB219 million from RMB1,462 million in 2012 to RMB1,243 million in 2013, mainly due to the decrease of government grants and loss on disposal of property, plant and equipment.

Interest expense increased by RMB275 million from RMB1,376 million in 2012 to RMB1,651 million in 2013 was mainly due to the increase in number of aircraft held through a finance lease.

Net exchange gain of RMB2,903 million was recorded in 2013, an increase of RMB2,636 million from RMB267 million in 2012, mainly due to the significant appreciation of Renminbi against U.S. dollar in 2013.

### ***Income Tax***

Income tax expense of RMB734 million was recorded in 2013, decrease by RMB220 million from RMB954 million in 2012, mainly due to the decrease of profit before income tax.

### **2012 Compared With 2011**

The profit attributable to equity shareholders of the Company of RMB2,619 million was recorded in 2012 as compared to the profit attributable to equity shareholders of the Company of RMB5,110 million in 2011. The Group's operating revenue increased by RMB9,119 million or 10.1% from RMB90,395 million in 2011 to RMB99,514 million in 2012. Passenger load factor decreased by 1.1 percentage points from 81.0% in 2011 to 79.9% in 2012. Passenger yield (in passenger revenue per RPK) decreased by 1.5% from RMB0.67 in 2011 to RMB0.66 in 2012. Average yield (in traffic revenue per RTK) decreased by 1.3% from RMB6.03 in 2011 to RMB5.95 in 2012. Operating expenses increased by RMB8,814 million or 10.1% from RMB87,063 million in 2011 to RMB95,877 million in 2012. Operating profit of RMB5,099 million was recorded in 2012 as compared to operating profit of RMB4,353 million in 2011, increased by RMB746 million.

*Operating Revenue*

	2012		2011		Change in
	Operating revenue		Operating revenue		revenue
	RMB	Percentage	RMB	Percentage	%
	million	%	million	%	
Traffic revenues	96,100	96.6	87,252	96.5	10.1
Including: Passenger revenues	89,544		81,492		9.9
– Domestic	73,845		68,222		8.2
– Hong Kong, Macau and Taiwan	2,133		1,834		16.3
– International	13,566		11,436		18.6
Cargo and mail revenues	6,556		5,760		13.8
Other operating revenues	3,414	3.4	3,143	3.5	8.6
Mainly including: Commission income	757		643		17.7
Hotel and tour operation income	647		614		5.4
Ground services income	350		368		(4.9 )
Expired sales in advance of carriage	495		309		60.2
General aviation income	445		322		38.2
Aircraft wet lease income	2		319		(99.4 )
Total operating revenues	99,514	100.0	90,395	100.0	10.1
Less: fuel surcharge income	(13,378)		(11,699)		
Total operating revenue excluding fuel surcharge	86,136		78,696		

*Traffic revenue composition*

	2012		2011		Change in
	Traffic revenue		Traffic revenue		traffic
	RMB	Percentage	RMB	Percentage	revenue
	million	%	million	%	%
Passenger Revenue	89,544	93.2	81,492	93.4	9.9
Cargo and Mail Revenue	6,556	6.8	5,760	6.6	13.8
Traffic revenue	96,100	100.0	87,252	100.0	10.1

*Passenger revenue composition*

	2012		2011		Change in passenger revenue
	Passenger revenue	Percentage	Passenger revenue	Percentage	
	RMB million	%	RMB million	%	%
Domestic	73,845	82.5	68,222	83.7	8.2
Hong Kong, Macao and Taiwan	2,133	2.4	1,834	2.3	16.3
International	13,566	15.1	11,436	14.0	18.6
Passenger revenue	89,544	100.0	81,492	100.0	9.9

Substantially all of the Group's operating revenue is attributable to airline and airline-related operations. Traffic revenue accounted for 96.6% and 96.5% of total operating revenue in 2012 and 2011, respectively. Passenger revenue and cargo and mail revenue accounted for 93.2% and 6.8% respectively of the total traffic revenue in 2012. The other operating revenue is mainly derived from commission income, hotel and travel services income, fees charged for ground services rendered to other Chinese airlines, income from expired sales in advance of carriage and general aviation income.

The increase in operating revenue was primarily due to a 9.9% increase in passenger revenue from RMB81,492 million in 2011 to RMB89,544 million in 2012. The total number of passengers carried increased by 7.2% to 86.48 million passengers in 2012. RPKs increased by 10.8% from 122,344 million in 2011 to 135,535 million in 2012, primarily as a result of the increase in number of passengers carried. Passenger yield per RPK decreased from RMB0.67 in 2011 to RMB0.66 in 2012.

Domestic passenger revenue, which accounted for 82.5% of the total passenger revenue in 2012, increased by 8.2% from RMB68,222 million in 2011 to RMB73,845 million in 2012. Domestic passenger traffic in RPKs increased by 7.6%, while passenger capacity in ASKs increased by 9.4%, resulting in a decrease in passenger load factor by 1.3 percentage points from 82.7% in 2011 to 81.4% in 2012. Domestic passenger yield per RPK increased from RMB0.68 in 2011 to RMB0.69 in 2012.

Hong Kong, Macau and Taiwan passenger revenue, which accounted for 2.4% of total passenger revenue, increased by 16.3% from RMB1,834 million in 2011 to RMB2,133 million in 2012. For Hong Kong, Macau and Taiwan flights, passenger traffic in RPKs increased by 21.8%, while passenger capacity in ASKs increased by 25.9%, resulting in a decrease in passenger load factor by 2.5 percentage points from 75.7% in 2011 to 73.2% in 2012. Passenger yield per RPK decreased from RMB0.88 in 2011 to RMB0.84 in 2012.

International passenger revenue, which accounted for 15.1% of total passenger revenue, increased by 18.6% from RMB11,436 million in 2011 to RMB13,566 million in 2012. For international flights, passenger traffic in RPKs increased by 24.9%, while passenger capacity in ASKs increased by 23.1%, resulting in a 1.1 percentage points increase in passenger load factor from 73.9% in 2011 to 75.0% in 2012. Passenger yield per RPK decreased from RMB0.56 in 2011 to RMB0.53 in 2012.

Cargo and mail revenue, which accounted for 6.8% of the Group's total traffic revenue and 6.6% of total operating revenue, increased by 13.8% from RMB5,760 million in 2011 to RMB6,556 million in 2012. The increase was attributable to the increase in cargo traffic volume.

Other operating revenue increased by 8.6% from RMB3,143 million in 2011 to RMB3,414 million in 2012. The increase was primarily due to the general growth in income from various auxiliary operations.

### ***Operating Expenses***

Total operating expenses in 2012 amounted to RMB95,877 million, representing an increase of RMB8,814 million or 10.1% over 2011, primarily due to the total effect of increases in jet fuel costs, landing and navigation fees, maintenance expenses and other operating costs. Total operating expenses as a percentage of total operating revenue remained at 96.3% in 2012 and 2011.

	2012		2011		Change in operating expenses %
	Operating expense RMB million	Percentage %	Operating expense RMB million	Percentage %	
Flight operations	54,690	57.0	48,344	55.5	13.1
Mainly including: Jet fuel costs	37,401		32,675		14.5
Operating lease charges	4,897		4,654		5.2
Flight personnel payroll and welfare	5,051		4,412		14.5
Maintenance	7,971	8.3	7,531	8.7	5.8
Aircraft and traffic servicing expenses	14,072	14.7	12,337	14.2	14.1
Promotion and selling expenses	7,134	7.5	6,568	7.5	8.6
General and administrative expenses	2,425	2.5	2,807	3.2	(13.6 )
Impairment on property, plant and equipment	-	-	584	0.7	(100.0 )
Depreciation and amortization	8,264	8.6	7,689	8.8	7.5
Others	1,321	1.4	1,203	1.4	9.8
Total operating expenses	95,877	100.0	87,063	100.0	10.1



Flight operations expenses, which accounted for 57.0% of total operating expenses, increased by 13.1% from RMB48,344 million in 2011 to RMB54,690 million in 2012, primarily as a result of increase in jet fuel costs derived from increased consumption of jet fuel and fuel prices. Jet fuel costs, which accounted for 68.4% of flight operations expenses in 2012, increased by 14.5% from RMB32,675 million in 2011 to RMB37,401 million in 2012.

Maintenance expenses, which accounted for 8.3% of total operating expenses, increased by 5.8% from RMB7,531 million in 2011 to RMB7,971 million in 2012. The increase was mainly due to the increase in number of engines repaired and routine maintenance during the year.

Aircraft and traffic servicing expenses, which accounted for 14.7% of total operating expenses, increased by 14.1% from RMB12,337 million in 2011 to RMB14,072 million in 2012. The increase was primarily due to a 6.6% rise in landing and navigation fees from RMB8,426 million in 2011 to RMB8,984 million in 2012, resulted from the increase in number of flights, and increase of rental expenses in 2012.

Promotion and selling expenses, which accounted for 7.5% of total operating expenses, increased by 8.6% from RMB6,568 million in 2011 to RMB7,134 million in 2012.

General and administrative expenses, which accounted for 2.5% of the total operating expenses, decreased by 13.6% from RMB2,807 million in 2011 to RMB2,425 million in 2012.

Depreciation and amortization, which accounted for 8.6% of total operating expenses, increased by 7.5% from RMB7,689 million in 2011 to RMB8,264 million in 2012, mainly due to the additional depreciation charges on aircraft delivered in 2012.

### ***Operating Profit***

Operating profit of RMB5,099 and RMB4,353 million was recorded in 2012 and 2011 respectively. The increase in profit was mainly due to the net effect of increase in operating revenue by RMB9,119 million or 10.1% in 2012 and increase in operating expenses by RMB8,814 million or 10.1%.

### ***Other Income or Expenses***

Other net income increased by RMB441 million from RMB1,021 million in 2011 to RMB1,462 million in 2012, mainly due to the increase of government grants.

Interest expense increased by RMB309 million from RMB1,067 million in 2011 to RMB1,376 million in 2012 was mainly due to the increase in weighted average bank and other loans balances during the year.

Net exchange gain of RMB267 million and RMB2,755 million was recorded in 2012 and 2011, respectively. The significant decrease was mainly due to the significant appreciation of Renminbi against U.S. dollar in 2011 while remained stable in 2012.

### ***Income Tax***

Our effective income tax rates were 20.1% and 12.1% in 2012 and 2011, respectively. The effective income tax rates differs from the PRC statutory income tax rate of 25% primarily due to the effect of non-taxable share of results of associates and jointly controlled entities of RMB110 million and RMB145 million in 2012 and 2011 respectively, and the recognition of unrecognized deferred tax assets of RMB29 million and RMB688 million in 2012 and 2011, respectively.

### **B. Liquidity and Capital Resources**

Generally, the Group meets its working capital and capital expenditure requirements through cash from its operations, the proceeds of certain long-term and short-term bank loans, capital lease financing and rebates available under certain of the Group's aircraft leases.

As of December 31, 2013, the Group had banking facilities with several PRC commercial banks for providing loan finance up to an approximate amount of RMB166.3 billion to the Group. As of December 31, 2013, an approximate amount of RMB120.9 billion was unutilized. As of December 31, 2013 and 2012, the Group's cash and cash equivalents totaled RMB11,748 million and RMB10,082 million, respectively.

Net cash inflows from operating activities in 2013, 2012 and 2011 were RMB9,703 million, RMB11,704 million and RMB12,557 million, respectively. Operating cash inflows of the Group are primarily derived from the provision of air transportation and related service for customers. The vast majority of tickets are purchased prior to the day on which transportation is provided. Operating cash outflows primarily are related to the recurring operating expenses, including flight operation, maintenance, aircraft and traffic servicing, etc.

Net cash used in investing activities in 2013, 2012 and 2011 was RMB12,205 million, RMB12,153 million and RMB21,957 million, respectively. Cash capital expenditures in 2013, 2012 and 2011 were RMB12,308 million, RMB15,733 million and RMB20,038 million, respectively, reflecting predominantly additional investments in aircraft and flight equipment under the Group's fleet expansion plans and Guangzhou new airport, and, to a small extent, additional investments in other facilities and buildings used in operations.

Financing activities resulted in net cash inflows of RMB4,168 million, RMB668 million and RMB8,859 million in 2013, 2012 and 2011, respectively. Net cash inflow/(out flow) from new bank and other loans and repayments of bank and other loans amounted to RMB7,081 million, RMB4,407 million and RMB9,254 million in 2013, 2012 and 2011, respectively. The additions of bank loan were used for capital expenditures and general working capital. Repayment of capital leases in 2013, 2012 and 2011 was RMB2,895 million, RMB1,978 million and RMB1,702 million, respectively, resulting from the aircraft acquisitions under capital leases.

As of December 31, 2013, the Group's aggregate long-term bank and other loans and obligations under capital leases (including loans and capital leases obligations due within one year) totaled RMB78,085 million. In 2014, 2015, 2016, 2017 and thereafter, amounts payable under such loans and obligations will be RMB9,466 million, RMB14,805 million, RMB16,166 million, RMB7,998 million and RMB29,650 million respectively. Such borrowings were denominated in U.S. dollars, Singapore dollars and Japanese Yen with a significant portion being floating interest rate borrowings. In the normal course of business, the Group is exposed to fluctuations in foreign currencies. The Group's exposure to foreign currencies primarily results from its foreign currency liabilities. Depreciation or appreciation of the Renminbi against foreign currencies affects the Group's results significantly because the Group's foreign currency liabilities generally exceed its foreign currency assets. The Group is not able to hedge its foreign currency exposure effectively other than by retaining its foreign currency denominated earnings and receipts to the extent permitted by the SAFE, or subject to certain restrictive conditions, entering into forward foreign exchange contracts with authorized banks.

As of December 31, 2013, the Group's short-term bank loans were RMB14,412 million. The Group's weighted average interest rate on short-term bank loans was 2.10% per annum as of December 31, 2013. The primary use of the proceeds of the Group's short-term bank loans is to finance working capital and capital expenditure needs. The Group has generally been able to arrange short-term bank loans with domestic banks in China as necessary and believes it can continue to obtain them based on its well-established relationships with various lenders.

As of December 31, 2013, the Group had obligations under operating leases totaling RMB26,222 million, predominately for aircraft. Of such amount, RMB4,608 million, RMB4,240 million, RMB3,991 million, RMB3,447 million, RMB3,062 million and RMB6,874 million, respectively, is due in 2014, 2015, 2016, 2017, 2018 and thereafter.

As of December 31, 2013, the Group had a working capital deficit of RMB28,640 million, as compared to a working capital deficit of RMB31,944 million as of December 31, 2012. Historically, the Group operated in a negative working capital position, relying on cash inflow from operating activities and renewal of short-term bank loans to meet its short-term liquidity and working capital needs. In 2014 and thereafter, 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 adequate external financing to meet its committed future capital expenditure. As of December 31, 2013, the Group had banking facilities with several PRC commercial banks for providing loan finance up to approximately RMB166,270 million (2012: RMB173,162 million), of which approximately RMB120,904 million (2012: RMB112,793 million) was unutilized.

The directors of the Company have carried out a detailed review of the cash flow forecast of the Group for the twelve months ending December 31, 2014. Based on such forecast, the directors have determined that adequate liquidity exists to finance the working capital, capital expenditure requirements and dividend payments of the Group during that period. In preparing the cash flow forecast, the directors have considered historical cash requirements of the Group as well as other key factors, including the availability of the above-mentioned bank financing which may impact the operations of the Group during the next twelve-month period. The directors of the Company are of the opinion that the assumptions and sensitivities which are included in the cash flow forecast are reasonable. However, as with all assumptions in regard to future events, these are subject to inherent limitations and uncertainties and some or all of these assumptions may not be realized.

As the Group is subject to a high degree of operating leverage, a minor decrease in the Group's yield and/or load factor could result in a significant decrease in its operating revenue and hence its operating cash flows. This could arise in such circumstances as where competition between Chinese airlines increases or where PRC aviation demand decreases. Similarly, a minor increase in the jet fuel prices, particularly in the domestic market, could result in a significant increase in the Group's operating expenses and hence a significant decrease in its operating cash flows. This could be caused by fluctuations in supply and demand in international oil market. Currently, the Group's existing loans and lease facilities do not contain any financial covenants. Nevertheless, as the Group is subject to a high degree of financial leverage, an adverse change in the Group's operating cash flows could adversely affect its financial health and hence weaken its ability to obtain additional loans and lease facilities and to renew its short-term bank loans facilities as they fall due.

As of December 31, 2013, the Group had capital commitments as follows:

	2014	2015	2016	2017	2018 and afterwards	Total
	(RMB million)					
Acquisition of aircraft and related equipment	20,945	14,417	6,365	3,488	2,436	47,651
Others	2,198	798	538	168	-	3,702
Total capital commitments	23,143	15,215	6,903	3,656	2,436	51,353

Others mainly represent airport and office facilities and equipment, overhaul and maintenance bases and training facilities.

As of December 31, 2013, the cash and cash equivalents of the Group totaled RMB11,748 million. Of such balance, 6.6% was denominated in U.S. Dollars, Hong Kong Dollars, Australian Dollars, Japanese Yen and other foreign currencies.

In view of the unutilized bank facilities of RMB120,904 million, the Group expects that it will have sufficient funding sources to meet its cash requirements in the foreseeable future.

**C. Research and Development, Patents and Licenses, etc.**

None.

**D. Trend Information**

Other than as disclosed in the foregoing disclosures and elsewhere in this Annual Report, we are not aware of any trends, uncertainties, demands, commitments or events for the period from January 1, 2014 to December 31, 2014 that are reasonably likely to have a material adverse effect on our net revenues, income, profitability, liquidity or capital resources, or that would cause our disclosed financial information to be not necessarily indicative of future operating results or financial conditions.

**E. Off-Balance Sheet Arrangements**

We have not entered into any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition that is material to investors. In particular, we (i) have not entered into any financial guarantees or other commitments to guarantee the payment obligations of any unconsolidated entity; (ii) have not entered into any derivative contracts that are both indexed to our own stock and classified in stockholders' equity, or not reflected in our statement of financial position; and (iii) do not have any retained or contingent interest in assets transferred to an unconsolidated entity that serves as credit, liquidity or market risk support to such entity.

**F. Tabular Disclosure of Contractual Obligations**

The following table sets forth the Group's obligations and commitments to make future payments under contracts and under commitments as of December 31, 2013.

	Total	As of December 31, 2013 Payment due by period				As of December 31, 2012
		Less than 1 year	1-3 years	3-5 years	After 5 years	Total
Short-term bank loans (note 1)	14,552	14,552	-	-	-	10,833
Long-term bank and other loans (note 1)	46,744	6,976	24,741	7,573	7,454	44,103
Obligations under capital leases	39,431	4,498	9,134	8,444	17,356	24,596
Operating lease commitments	26,222	4,608	8,231	6,509	6,874	22,161
Aircraft purchase commitments (Note 2)	47,651	20,945	20,782	3,488	2,436	71,309
Other capital commitments	3,702	2,198	1,336	167	-	3,820
Investment commitments	70	70	-	-	-	119
Total	178,601	54,076	64,224	26,181	34,120	177,061

Note 1 Interest on variable rate loans was estimated based on the current rate in effect at December 31, 2013.

Note 2 Amounts shown are net of previously paid purchase deposits.

**ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES.****A. Directors, Senior Management and Employees.**

The following table sets forth certain information concerning directors, senior management and supervisors of the Company in 2013. There were certain changes in the Company's directors, senior management and supervisors in 2013, details of which are set forth below.

Name	Position	Gender	Age
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Si Xian Min <sup>(1)</sup>	Chairman of the Board, Non-executive Director	Male	56
Tan Wan Geng <sup>(2)</sup>	Executive Director, Vice Chairman of the Board and President	Male	49
Wang Quan Hua <sup>(3)</sup>	Non-executive Director	Male	59
Yuan Xin An <sup>(4)</sup>	Non-executive Director	Male	57
Yang Li Hua <sup>(5)</sup>	Non-executive Director	Female	58
Zhang Zi Fang <sup>(6)</sup>	Executive Director and Executive Vice President	Male	55
Xu Jie Bo <sup>(7)</sup>	Executive Director, Executive Vice President, Chief Financial Officer and Chief Accountant	Male	48
Li Shao Bin <sup>(8)</sup>	Executive Director	Male	48
Gong Hua Zhang	Independent Non-executive Director (Resigned on December 26, 2013)	Male	68
Wei Jin Cai <sup>(9)</sup>	Independent Non-executive Director	Male	64
Ning Xiang Dong <sup>(10)</sup>	Independent Non-executive Director	Male	48
Liu Chang Le <sup>(11)</sup>	Independent Non-executive Director	Male	62
Tan Jin Song <sup>(12)</sup>	Independent Non-executive Director	Male	49
Pan Fu <sup>(13)</sup>	Chairman of the Supervisory Committee	Male	51
Li Jia Shi <sup>(14)</sup>	Supervisor	Male	52
Zhang Wei <sup>(15)</sup>	Supervisor	Female	47
Yang Yi Hua <sup>(16)</sup>	Supervisor	Female	53
Wu De Ming <sup>(17)</sup>	Supervisor	Male	56
Liang Zhong Gao	Supervisor (Resigned on December 26, 2013)	Male	57
Ren Ji Dong <sup>(18)</sup>	Executive Vice President	Male	49
Liu Qian <sup>(19)</sup>	Executive Vice President	Male	49
Dong Su Guang <sup>(20)</sup>	Executive Vice President	Male	60
Chen Gang <sup>(21)</sup>	Executive Vice President	Male	48
Zhou Yue Hai <sup>(22)</sup>	Executive Vice President	Male	53
Wang Zhi Xue <sup>(23)</sup>	Executive Vice President and Chief Pilot	Male	52
Hu Chen Jie <sup>(24)</sup>	Chief Information Officer	Male	45
Su Liang <sup>(25)</sup>	Chief Economist	Male	51
Chen Wei Hua <sup>(26)</sup>	Chief Legal Adviser	Male	47
Yuan Xi Fan <sup>(27)</sup>	Chief Engineer	Male	51
Tian Xiao Dong <sup>(28)</sup>	COO Flight Operations	Male	44
Guo Zhi Qiang <sup>(29)</sup>	COO Marketing & Sales	Male	50
Xie Bing <sup>(30)</sup>	Company Secretary	Male	41



- (1) On December 26, 2013, Mr. Si Xian Min was elected as the Chairman of the Board and a Non-executive Director at the first meeting of the seventh session of the Board of Directors of the Company.  
On December 26, 2013, Mr. Tan Wan Geng was elected as the Vice Chairman of the Board and a Non-executive
- (2) Director at the first meeting of the seventh session of the Board of Directors of the Company. On December 26, 2013, Mr. Tan Wan Geng was appointed as President by the Board.
- (3) On December 26, 2013, Mr. Wang Quan Hua was elected as a Non-executive Director at the first meeting of the seventh session of the Board of Directors of the Company.
- (4) On December 26, 2013, Mr. Yuan Xin An was elected as a Non-executive Director at the first meeting of the seventh session of the Board of Directors of the Company.
- (5) On December 26, 2013, Ms. Yang Li Hua was elected as a Non-executive Director at the first meeting of the seventh session of the Board of Directors of the Company.  
On December 26, 2013, Mr. Zhang Zi Fang was elected as an Executive Director at the first meeting of the
- (6) seventh session of the Board of Directors of the Company. On December 26, 2013, Mr. Zhang Zi Fang was appointed as an Executive Vice President by the Board.  
On December 26, 2013, Mr. Xu Jie Bo was elected as an Executive Director at the first meeting of the seventh
- (7) session of the Board of Directors of the Company. On December 26, 2013, Mr. Xu Jie Bo was appointed as an Executive Vice President, Chief Financial Officer and Chief Accountant by the Board.
- (8) On December 26, 2013, Mr. Li Shao Bin was elected as an Executive Director at the first meeting of the seventh session of the Board of Directors of the Company.
- (9) On December 26, 2013, Mr. Wei Jin Cai was elected as an Independent Non-executive Director at the first meeting of the seventh session of the Board of Directors of the Company.
- (10) On December 26, 2013, Mr. Ning Xiang Dong was elected as an Independent Non-executive Director at the first meeting of the seventh session of the Board of Directors of the Company.
- (11) On December 26, 2013, Mr. Liu Chang Le was elected as an Independent Non-executive Director at the first meeting of the seventh session of the Board of Directors of the Company.
- (12) On December 26, 2013, Mr. Tan Jin Song was elected as an Independent Non-executive Director at the first meeting of the seventh session of the Board of Directors of the Company.
- (13) On December 26, 2013, Mr. Pan Fu was elected as the Chairman of the Supervisory Committee at the first meeting of the seventh session of the Supervisory Committee of the Company.
- (14) On December 26, 2013, Mr. Li Jia Shi was elected as a Supervisor at the first meeting of the seventh session of the Supervisory Committee of the Company
- (15) On December 26, 2013, Ms. Zhang Wei was elected as a Supervisor at the first meeting of the seventh session of the Supervisory Committee of the Company
- (16) On December 26, 2013, Ms. Yang Yi Hua was elected as a Supervisor at the first meeting of the seventh session of the Supervisory Committee of the Company
- (17) On December 26, 2013, Mr. Wu De Ming was elected as a Supervisor at the first meeting of the seventh session of the Supervisory Committee of the Company
- (18) On December 26, 2013, Mr. Ren Ji Dong was appointed as an Executive Vice President by the Board.
- (19) On December 26, 2013, Mr. Liu Qian was appointed as an Executive Vice President by the Board.
- (20) On December 26, 2013, Mr. Dong Su Guang was appointed as an Executive Vice President by the Board.
- (21) On December 26, 2013, Mr. Chen Gang was appointed as an Executive Vice President by the Board.
- (22) On December 26, 2013, Mr. Zhou Yue Hai was appointed as an Executive Vice President by the Board.
- (23) On December 26, 2013, Mr. Wang Zhi Xue was appointed as an Executive Vice President and Chief Pilot by the Board.
- (24) On December 26, 2013, Mr. Hu Chen Jie was appointed as Chief Information Officer by the Board.
- (25) On December 26, 2013, Mr. Su Liang was appointed as Chief Economist by the Board.
- (26) On December 26, 2013, Mr. Chen Wei Hua was appointed as Chief Legal Adviser by the Board.
- (27) On December 26, 2013, Mr. Yuan Xi Fan was appointed as Chief Engineer by the Board.



- (28) On December 26, 2013, Mr. Tian Xiao Dong was appointed as COO Flight Operations by the Board.  
(29) On December 26, 2013, Mr. Guo Zhi Qiang was appointed as COO Marketing & Sales by the Board.  
(30) On December 26, 2013, Mr. Xie Bing was appointed as Company Secretary by the Board.

## **Board of Directors**

**Si Xian Min**, aged 56, graduated with an Executive Master of Business Administration (EMBA) degree from Tsinghua University. He began his career in 1975. Mr. Si served as the Director of the political division of China Southern Airlines Henan Branch; as the party secretary and vice president of Guizhou Airlines Company Limited; as the Deputy Party Secretary and Secretary of the Disciplinary Committee of the Company; and as the Party Secretary of CSAHC Northern Division. He has been the President of the Company from October 2004 to January 2009. Since December 31, 2004, Mr. Si has been the Director of the Company. Since January 2009, Mr. Si has been the President and Deputy Party Secretary of CSAHC and the Chairman of the Board.

**Tan Wan Geng**, aged 49, graduated from Zhongshan University, majoring in economic geography, with qualification of postgraduate degree. Mr. Tan began his career in civil aviation in 1990 and served as the head of the Infrastructure Department and Director of Human Resources and Administration Department of the Beijing Aircraft Maintenance and Engineering Corporation, the Deputy Director General of Human Resources Division (Personnel and Education Division) of the Civil Aviation Administration of China (CAAC), and has been the Director General and Party Secretary of Civil Aviation Administration of China Northeastern Region. He has been the Party Secretary and Executive Vice President of the Company from January 2006 to February 2007; the Party Member of CSAHC and the Party Secretary and Executive Vice President of the Company from February 2007 to January 2009; the Party Member of CSAHC and the President and Party Secretary of the Company from January 2009 to February 2009; the Party Member of CSAHC and the President and Deputy Party Secretary of the Company from February 2009 to May 2011. Since May 2011, Mr. Tan has been the Party Secretary of CSAHC and the President of the Company. Mr. Tan has been the Director of the Company since June 15, 2006 and has been the Vice Chairman of the Board since January 24, 2013.

**Wang Quan Hua**, aged 59, graduated with a university degree from the Party School of the Central Committee of CPC majoring in economic management. Mr. Wang began his career in 1972. Mr. Wang served as the Director of the Planning and Operation Division of China Southern Airlines Company; the General Manager of Strategy and Development Department of CSAHC; the Assistant to the President and the Director of the Strategy and Development Department and the Vice President of CSAHC. Mr. Wang has served as the Executive Vice President of CSAHC since September 2002. Since May 13, 2003, Mr. Wang has been the Director of the Company. Currently, Mr. Wang is also the Chairman of Nan Lung Holding Limited, Guangzhou Southern Airline Construction Company Limited, the director of TravelSky Technology Limited, Solar Insurance Group Company Limited, Yazhou Travel Investment Company Limited and China National Aviation Corp (HK) Ltd.

**Yuan Xin An**, aged 57, received university education in Aeronautical Machinery from Air Force Engineer University and is a senior engineer. Mr. Yuan began his career in December 1976 and served as the Vice President of Engineering Department of China Southern Airlines Company, the Vice President of Guangzhou Aircraft Maintenance Engineering Co., Ltd., the Chief Engineer and the General Manager of Engineering Department of the Company. Mr. Yuan served as the Executive Vice President of the Company from April 2002 to September 2007; the Executive Vice President of CSAHC since September 2007; the Executive Vice President and Chief Legal Adviser of CSAHC since July 2008. Since November 30, 2011, Mr. Yuan has been the Director of the Company. Currently, Mr. Yuan is also the Chairman of Southern Airlines (Group) Import and Export Trading Company Limited, China Southern Airlines Group Construction and Development Company Limited, MTU Maintenance Zhuhai Co., Ltd., Dalian Acacia Town Villa Co., Ltd. and Shenzhen Air Catering Co., Ltd, and a director of China Aircraft Services Limited.

**Yang Li Hua**, aged 58, graduated with a master degree from the Party School of the Central Committee of CPC majoring in economics and management and is a senior expert of political science. Ms. Yang began her career in Air China International Corporation in 1973, and served as the head of the in-flight service team, manager of in-flight service division and deputy head of the Chief Flight Team of Air China International Corporation. Subsequently, she was appointed as the General Manager of the Passenger Cabin Service Division of Air China International Corporation in September 2000, the Vice President of Air China International Corporation in October 2002, the Vice President of Air China Limited in September 2004, and Executive Vice President of CSAHC in May 2009. From July 2010 to August 2012, Ms. Yang also acted as the Chairman of the Labour Union of CSAHC. Since January 24, 2013, Ms. Yang has been the Director of the Company. Currently, Ms. Yang is also the Chairman of Southern Airlines Culture and Media Co., Ltd. and China Southern Airlines Group Property Management Company Limited.

**Zhang Zi Fang**, aged 55, graduated with an Executive Master of Business Administration (EMBA) degree from Tsinghua University and is a senior expert of political science. Mr. Zhang began his career in 1976. He served as the Deputy Commissar and subsequently the Commissar of the pilot corps of China Northern Airlines Company; as the Party Secretary of the Jilin Branch of China Northern Airlines Company; as the General Manager of Dalian Branch of CSAHC Northern Airlines; as the Director of Political Works Department of CSAHC. Mr. Zhang was the Deputy Party Secretary and Secretary of the Disciplinary Committee of the Company from February 2005 to December 2007. He has been the Executive Vice President and the Deputy Party Secretary of the Company from December 2007 to February 2009. Since February 2009, he has been the Party Secretary and Executive Vice President of the Company. Mr. Zhang has been the Director of the Company since June 30, 2009. Currently, Mr. Zhang is also the Vice Chairman of Southern Airlines Culture and Media Co., Ltd.

**Xu Jie Bo**, aged 48, graduated with a university degree from Tianjin University majoring in infrastructure and engineering management, and was subsequently awarded with a master degree in Business Administration from Hong Kong Baptist University and an Executive Master of Business Administration (EMBA) degree from Tsinghua University and is a qualified senior accountant. Mr. Xu began his career in 1986. He served as the Director of the Financial Department of Central and Southern Administration of CAAC; as the Chief Accountant and General Manager of the Financial Department of the Company. Mr. Xu served as the Director, Chief Financial Officer and Chief Accountant of the Company since April 2001 and as the Director, Executive Vice President, Chief Financial Officer and Chief Accountant of the Company since August 2013. Currently, Mr. Xu is also the Chairman of Guizhou Airlines Company Limited, China Southern Airlines Henan Airlines Company Limited and the Vice Chairman of Sichuan Airlines Corporation Limited.

**Li Shao Bin**, aged 48, graduated with a university degree from the Party School of the Central Committee of CPC majoring in economics and management and is an expert of political science. Mr. Li began his career in 1984, and served as the Deputy Head of Promotion Department of the Company, the Director of Political Department of Guangzhou Flight Operations Division of the Company, and the Director of Political Department and Deputy Party Secretary of Guangzhou Flight Operations Division of the Company. Subsequently, he was appointed as Party Secretary of Guangzhou Flight Operations Division of the Company in May 2004. Mr. Li served as the Party Secretary and Deputy General Manager of Guangzhou Flight Operations Division of the Company from March 2006 to August 2012. Mr. Li has been the Chairman of the Labour Union of the Company since August 2012 and the Director of the Company since January 24, 2013.

**Wei Jin Cai**, aged 64, graduated from the Party School of the Central Committee of CPC majoring in economics and management. Mr. Wei has many years of experiences in civil aviation. He conducted an in-depth study on the operation and management of civil aviation and is influential in the civil aviation industry. Mr. Wei served as the Deputy Party Secretary of the Party Committee of the headquarter of CAAC, the Party Secretary of Civil Aviation Management Institute of China from March 1993 to November 2008, the President of Civil Aviation Management Institute of China from November 2008 to August 2010 and the independent director of Shandong Airlines Co., Ltd. Mr. Wei has been the Independent Non-executive Director of the Company since December 29, 2010. Currently, he is also the independent director of Xiamen International Airport Co., Ltd. and the independent non-executive director of ASR Holdings Limited and the independent director of E-Food Group Co., Ltd.

**Ning Xiang Dong**, aged 48, graduated from the Quantitative Economics Faculty of the School of Economics and Management of Tsinghua University with a doctor degree. Mr. Ning began his career in 1990 and served as the assistant, lecturer and associate professor at Tsinghua University and the Executive Deputy Director of the National Center for Economic Research (NCER) at Tsinghua University. He was also a visiting scholar at Harvard Business School, University of Illinois, University of New South Wales, University of Sydney and Chinese University of Hong Kong. Currently, he serves as the professor and the doctorate-tutor of the School of Economics and Management of Tsinghua University and the executive director of Centre for Corporate Governance of Tsinghua University. Mr. Ning has been the Independent Non-executive Director of the Company since December 29, 2010. He is also the independent director of Aerospace Hi-Tech Holding Group Co., Ltd. and Sichuan ChangHong Electric Company Limited.

**Liu Chang Le**, aged 62, was conferred an honorary doctoral degree in literature by the City University of Hong Kong and is a founder of Phoenix Satellite Television. Mr. Liu has been the Chairman and Chief Executive Officer of Phoenix Satellite Television Company Limited since 1996 and the Chairman and Chief Executive Officer of Phoenix Satellite Television Holdings Limited, a company listed on the Stock Exchange since 2000. Mr. Liu gained widespread recognition both locally and overseas for his enthusiasm for and achievements in the media industry. Mr. Liu is the recipient of numerous titles and awards, among which include “Wiseman of the Media Industry”, “the Most Innovative Chinese Business Leaders in the Asia Pacific Region”, “the Most Entrepreneurial Chinese Business Leaders”, and has been awarded the “Robert Mundell Successful World CEO Award”, the “Man of Year for Asia Brand Innovation Award” and the “Person of the Year” award of the Chinese Business Leaders Annual Meeting”. Since 2005, Mr. Liu has been the Chairman of the iEMMYs Festival, which is run by the International Academy of Television Arts & Sciences. In 2008, Mr. Liu received the International Emmy® Directorate Award. Mr. Liu was appointed as honorary chairman of “World Chinese-language Media Cooperation Alliance” in 2009 and appointed as special consultant to the Eighth Council of the Buddhist Association of China in 2010. Mr. Liu was a member of the Tenth and the Eleventh and the Twelfth National Committee of the Chinese People’s Political Consultative Conference, served as the Vice Chairman of the sub-committee on Education, Science, Culture, Health and Sport of the Eleventh National Committee of the Chinese People’s Political Consultative Conference, and is servicing as a member of standing committee of the Twelfth National Committee of the Chinese People’s Political Consultative Conference. Mr. Liu has been appointed a Justice of the Peace by the government of the Hong Kong Special Administrative Region. In 2010, Mr. Liu was awarded the Silver Bauhinia Star by the Hong Kong Special Administrative Region. Mr. Liu has been the an Independent Non-executive Director of the Company since November 30, 2011.

**Tan Jin Song**, aged 49, graduated from Renmin University of China with an on-job doctor degree in Accounting. Mr. Tan began his career in 1985 and was a teacher in Shaoyang School of Finance and Accounting of Hunan Province and the Deputy Dean of the School of Management of Zhongshan University; Mr. Tan acted as a professor of the School of Management of Zhongshan University from October to December 2008; and as the Party Secretary of the School of Management of Zhongshan University since December 2008. Currently, he is the independent director of Sundiro Holding Co., Ltd., Grandhope Biotech Co., Ltd. and Poly Real Estate Company Limited. Mr. Tan also acts as the independent non-executive director of Welling Holding Limited, the external supervisor of China Guangfa Bank and the independent supervisor of Sino-Singapore Guangzhou Knowledge City Investment and Development Co., Ltd.. Mr. Tan has been the Independent Non-executive Director of the Company since December 26, 2013.

### **Supervisory Committee**

As required by the Company Law of the PRC and the Articles of Association of the Company, we have a supervisory committee (the “Supervisory Committee”) which is primarily responsible for the supervision of senior management of the Company, including the Board, executive officers and other senior management personnel, to ensure that they act in the interests of the Company, its shareholders and employees, as well as in compliance with applicable law. The Supervisory Committee consists of five Supervisors. Three of the Supervisors are appointed by shareholders, and the other two Supervisors are representatives of our employees. The Supervisors serve terms of three years and may serve consecutive terms.

**Pan Fu**, aged 51, graduated with a master degree from Chongqing University majoring in power systems and automation, and is a senior engineer. Mr. Pan began his career in 1986, and served successively as the Deputy Chief Engineer of Test Research Institute of Electric Power Bureau of Yunnan Province and the Deputy Head of the Planning Department of Electric Power Industry Bureau of Yunnan Province (Group Company), the Deputy Director of the Planning & Development Department of Yunnan Electric Power Group Co., Ltd., the Deputy Director and Director of Kunming Power Plant, the Deputy Chief Engineer and Chief Engineer of Yunnan Electric Power Corporation, the Deputy Director and Director of the Department of Security Supervision of China Southern Power Grid Company Ltd., the Director of the China Southern Power Grid Technology and Research Center. He served as the General Manager and Deputy Party Secretary of the Guizhou Power Grid Corporation from January 2005 to November 2007, and served as the Director of the Planning Development Department of China Southern Power Grid Company Ltd. from November 2007 to November 2010. Mr. Pan has been the Team Leader of the Discipline Inspection Commission of CSAHC since November 2010 and the Chairman of the Supervisory Committee of the Company since December 29, 2010. Currently, he is also the Chairman of China Southern Airlines Group Passenger and Cargo Agent Company Limited.

**Li Jia Shi**, aged 52, graduated from Guangdong Polytechnic Normal University majoring in economics and mathematics and obtained an Executive Master of Business Administration (EMBA) degree from Tsinghua University and is an expert of political science. Mr. Li began his career in 1976. He served as the Deputy Head of the Organization Division of the Party Committee of the Company, Party Secretary and Deputy General Manager of Guangzhou Nanland Air Catering Company Limited, the Head of the Organization Division of the Party Committee

of the Company, the Chairman of Southern Airlines Ka Yuen (Guangzhou) Aviation Supply Company Limited and Guangzhou Nanland Air Catering Company Limited. He served as the Deputy Secretary of the Disciplinary Committee and the Director of the Disciplinary Committee Office of the Company from December 2003 to December 2007. Mr. Li has been the Secretary of the Disciplinary Committee of the Company since December 2007 and has been the Team Deputy Leader of the Discipline Inspection Commission of CSAHC and the Secretary of Disciplinary Committee of the Company since February 2012. Mr. Li has been the Supervisor of the Company since June 30, 2009.

**Zhang Wei**, aged 47, graduated with a master degree from Tianjin University majoring in investment skills and economics and obtained an Executive Master of Business Administration (EMBA) degree from Tsinghua University and is a senior accountant. Ms. Zhang began her career in 1988 and served as the General Manager Assistant and Deputy General Manager of the Finance Department of the Company, the Deputy Director of the Supervisory Bureau and the Director of the Audit Division of CSAHC and the General Manager of Finance Company. Ms. Zhang served as the Deputy Director of the Supervisory Bureau and the Director of the Audit Division of CSAHC from October 2007 to October 2008. Since October 2008, she has been the Director of the Audit Division of CSAHC. Ms. Zhang has been the Supervisor of the Company since June 2008. Currently, Ms. Zhang is also the Chairman of Supervisory Committee of Southern Airlines Culture and Media Co., Ltd, Finance Company, Southern Airlines (Group) Import and Export Trading Company Limited, China Southern Airlines Group Construction and Development Company Limited, the Supervisor of MTU Maintenance Zhuhai Co., Ltd. and the Director of Guangzhou Southern Airline Construction Company Limited.



**Yang Yi Hua**, aged 53, has a university degree, and is an accountant and an International Certified Internal Auditor. Ms. Yang served as the Manager of the Financial Office of the Company's Financial Division, and Deputy General Manager of the Company's Audit Department. Ms. Yang has been the General Manager of the Company's Audit Department since May 2002 and the Supervisor of the Company since June 2004. Currently, Ms. Yang is also the Chairman of the Supervisory Committee of Guizhou Airlines, Guangzhou Baiyun International Logistic Company Limited, Nan Lung International Freight Limited, Beijing China Southern Airlines Ground Service Company Limited and the supervisor convener of the supervisory committee of Xiamen Airlines, Finance Company and Chongqing Airlines.

**Wu De Ming**, aged 56, graduated from South China Normal University majoring in political management. He obtained a degree after beginning his career from 1976. Mr. Wu served as the Director of the political division of Operation Department of China Southern Airlines, as the Deputy Party Secretary and Secretary of Disciplinary Committee of Guangzhou ticket office of China Southern Airlines, and as the Deputy Secretary and Secretary of the party general branch of ticket office of Transportation Department of China Southern Airlines. Mr. Wu served as the Director of the Disciplinary Supervision Department of CSAHC from March 2001 to December 2003; and as the General Director of the Supervision Bureau and Chief Officer of Disciplinary Committee Office from December 2003 to April 2009. He has been a member of Party Committee of Commercial Steering Committee of the Company, Secretary to the Disciplinary Committee and President of the Labour Union since April 2009. Mr. Wu has been the Supervisor of the Company since 26 December 2013.

## Senior Management

**Ren Ji Dong**, aged 49, graduated from Nanjing University of Aeronautics and Astronautics, majoring in aircraft engine design and obtained an Executive Master of Business Administration (EMBA) degree from Tsinghua University, and he is a senior engineer. Mr. Ren began his career in 1986 and served as the Deputy Director of Urumqi Civil Aviation Administration, the Vice President of Xinjiang Airlines, the Party Secretary and the Vice President of the Xinjiang branch of the Company, the Executive Vice President of the Company from March 2005 to January 2007, and the President of the Xinjiang branch of the Company from January 2007 to April 2009. He has been the Executive Vice President of the Company since May 2009.

**Liu Qian**, aged 49, graduated from China Civil Aviation Flying College majoring in aircraft piloting and obtained an Executive Master of Business Administration (EMBA) degree from Tsinghua University. Mr. Liu served the CAAC as an assistant researcher of the Piloting Skills Supervision Division of the Piloting Standards Department, an assistant researcher of the Operation Supervision Division, an assistant researcher and the Deputy Head of the Piloting Standards Division, and the Deputy Chief Pilot and Chief Pilot of the Company. He has been the Executive Vice President of the Company since August 2007. Currently, Mr. Liu is also the Chairman of Zhuhai Xiang Yi Aviation Technology Company Limited and China Southern West Australian Flying College Pty Ltd.

**Dong Su Guang**, aged 60, graduated from Northwestern Polytechnical University majoring in aircraft design. Mr. Dong began his career in 1970 and served as the Vice President of Guangzhou Aircraft Maintaining and Engineering Co., Ltd. ("GAMECO"), the Chief Engineer and the General Manager of Engineering Department of the Company. He has been the Executive Vice President of the Company since December 2007. Currently, Mr. Dong is also the Chairman of Shantou Airlines, GAMECO and Shenyang Northern Aircraft Maintenance Engineering Co., Ltd.

**Chen Gang**, aged 48, graduated from Zhongnan Finance and Economics University majoring in industrial enterprise management and obtained an Executive Master of Business Administration (EMBA) degree from Tsinghua University. He began his career in 1987 and served as the Vice President of Henan branch of the Company, the President of Hubei branch of the Company and the Director of Commercial Steering Committee of the Company. He has been the Executive Vice President of the Company since August 2009.

**Zhou Yue Hai**, aged 53, has a university degree and obtained an Executive Master of Business Administration (EMBA) degree from Tsinghua University on-the-job. Mr. Zhou began his career in 1980. He served as the Deputy Director of the Flight Safety Technology Division, the Deputy Director of the Flight Technology Management Division, the Deputy General Manager of the Flight Safety Technology Department, the Deputy General Manager of the Flight Operation Division of the Company, the Party Secretary and Vice President of Guizhou Airlines Company Limited. Mr. Zhou served as the General Manager of China Southern Airlines Jilin Branch from September 2004 to January 2009 and the General Manager of China Southern Airlines Northern Branch from January 2009 to July 2012. Mr. Zhou has been the Executive Vice President of the Company since August 2012. Currently, Mr. Zhou is also the Chairman of Southern Airlines Ka Yuen (Guangzhou) Aviation Supply Company Limited, Guangzhou Nanland Air Catering Company Limited and Guangzhou China Southern Zhongmian Dutyfree Store Co., Limited.

**Wang Zhi Xue**, aged 52, has a university degree. Mr. Wang began his career in 1981. He served as the Manager of the Flight Safety Technology Inspection Division of Zhuhai Airlines Company Limited, Deputy Chief Pilot and Director of the Flight Safety Technology Division as well as the Vice President of Shantou Airlines Company Limited. He served as the General Manager of the Flight Management Division of the Company from October 2004 to February 2009 and the General Manager of the Flight Operation Division of the Company in Guangzhou from February 2009 to July 2012. Mr. Wang has been the Executive Vice President and Chief Pilot of the Company since August 2012. Mr. Wang is also the chairman of Zhuhai Airlines Company Limited.

**Hu Chen Jie**, aged 45, graduated from Beijing University Aeronautics and Astronautics majoring in information management. Mr. Hu served as a software engineer in the IT Center of CAAC, senior software engineer in Wei Hong International Technology Company (Singapore), the Deputy Director of the IT Center of the Company, the senior project manager of SITA INC. (U.S.) and the General Manager of CSNETC e-Commerce Limited. He has been the director of the IT center since March 2007 and the Chief Information Officer of the Company since June 2007. Currently, Mr. Hu is also the Chairman of Guangzhou Aircraft Hang Yi Information Technology Co., Ltd. and Chairman of THITC.

**Su Liang**, aged 51, graduated from the University of Cranfield, United Kingdom with a master degree in Air Transport Management and obtained an Executive Master of Business Administration (EMBA) degree from Tsinghua University. Mr. Su was in charge of the flight operations, planning and international cargo project of the Company. From July 2000 to November 2007, Mr. Su was the Company Secretary of the Company. He has been the Chief Economist of the Company since December 2007. Currently, Mr. Su is also the director of Xiamen Airlines and Sichuan Airlines Corporation Limited.

**Chen Wei Hua**, aged 47, graduated from the School of Law of Peking University and obtained an Executive Master of Business Administration (EMBA) degree from Tsinghua University. He is a qualified lawyer in the PRC and a qualified corporate legal counselor. Mr. Chen joined the aviation industry in 1988. He served as Deputy Director, Director of the Legal Affairs Office of the Company. Mr. Chen has been the Chief Legal Adviser of the Company and Director of the Legal Department of the Company since January 2004. Currently, Mr. Chen is also the director of Xiamen Airlines.

**Yuan Xi Fan**, aged 51, graduated from Civil Aviation Institute of China majoring in Aviation Radio, and was subsequently awarded with a master degree in Aviation Safety Management from the École Nationale de l'Aviation Civile (ENAC) and Ecole Nationale Supérieure d'Ingenieurs de Construction Aeronautique (ENSICA) in France and an Executive Master of Business Administration (EMBA) degree from Tsinghua University, and is a senior engineer. Mr. Yuan began his career in 1982. Mr. Yuan served as the Deputy Director of Repair and Maintenance Workshop of Guangzhou Aircraft Maintenance Engineering Co., Ltd., the Deputy General Manager of the Aircraft Maintenance Engineering Division, the Director of Quality Management and Director of Integrated Business Management of Aircraft Maintenance Engineering Division of the Company, and the Deputy General Manager of MTU Maintenance Zhuhai Co., Ltd. Mr. Yuan served as the Deputy General Manager of Guangzhou Aircraft Maintenance Engineering Co., Ltd. from March 2009 to January 2011. Mr. Yuan served as the General Manager of the Aircraft Engineering

Division of the Company since 2011. Mr. Yuan has been the Chief Engineer of the Company and the General Manager of the Aircraft Engineering Division of the Company since April 2012. Currently, Mr. Yuan is also the director of Guangzhou Aircraft Maintenance Engineering Co., Ltd.

**Tian Xiao Dong**, aged 44, graduated from Beijing Institute of Meteorology majoring in aviation meteorology, and was subsequently awarded with a master degree in Aeronautical Engineering from Beijing University of Aeronautics and Astronautics and obtained an Executive Master of Business Administration (EMBA) degree from Tsinghua University, and is a senior engineer. Mr. Tian began his career in 1989. Mr. Tian served as the Deputy Manager of Flight Operation Office of General Dispatching Office, the Manager of Planning and Dispatch Office of System Operation Control Center (SOC), the Deputy Director of Operation Control Division and the Deputy General Manager of SOC. Mr. Tian has been served as the general manager of SOC from December 2006 to January 2014. He has been the director of the General On-Duty Manager Office. Since January 2014, he has been the COO Flight Operations of the Company since June 2012.

**Guo Zhi Qiang**, aged 50, economist, graduated with a master degree from Party School of Xinjiang Uyghur Autonomous Region majoring in Business Administration. Mr. Guo began his career in 1980 and served as the Manager of Transportation Department of Xinjiang Airlines; the Deputy General Manager of Xinjiang Company of China Southern Air Holding Company; the General Manager of China Southern Airlines Beijing Office; the Deputy General Manager of China Southern Airlines Xinjiang Branch. Mr. Guo served as the Deputy General Manager of the Shenzhen Branch of the Company from December 2005 to February 2008 and the President and Chief Executive Officer of Chongqing Airlines Company Limited from February 2008 to May 2009, and served as the Deputy Director General of the Commercial Steering Committee of the Company from May 2009 and the Director General of the Commercial Steering Committee of the Company from September 2009 to September 2012. Mr. Guo has been the COO Marketing & Sales of the Company and the Director General of the Commercial Steering Committee of the Company since September 2012. Currently, Mr. Guo is also the director of Xiamen Airlines Company Limited.

**Xie Bing**, aged 41, graduated from Nanjing University of Aeronautics and Astronautics, majoring in civil aviation management. He subsequently received a master degree of business administration, a master degree of international finance and an Executive Master of Business Administration (EMBA) degree from Jinan University, the University of Birmingham, Britain and Tsinghua University, respectively. Mr. Xie is a senior economist. Mr. Xie used to work in the Planning and Development Department, Company Secretary Office of the Company and General Office of CSAHC. He has been the Company Secretary of the Company since November 2007.

Save as disclosed above, none of the above Directors or Supervisors, senior management of the Company has any relationship with any Directors, Supervisors, senior management, substantial shareholders of the Company.

#### B. Compensation.

The aggregate compensation paid to all Directors, Supervisors and Senior Management for 2013 was RMB14,486,000. For the year ended December 31, 2013, the Company paid an aggregate of approximately RMB2,074,000 on behalf of its executive Directors, Supervisors and Senior Management pursuant to the pension scheme and the retirement plans operated by various municipal and provincial governments in which the Company participates.

Details of the remuneration of directors' and supervisors' remuneration for the year ended December 31, 2013 are set out below:

	Directors' fees RMB'000	Salaries, allowances and benefits in kind RMB'000	Retirement scheme contributions RMB'000	Total RMB'000
Non-executive Directors				
Si Xian Min	-	-	-	-
Wang Quan Hua	-	-	-	-
Yuan Xin An	-	-	-	-
Yang Li Hua	-	-	-	-
Independent Non-executive Directors				
Gong Hua Zhang (Retired on December 26, 2013)	150	-	-	150
Wei Jin Cai	150	-	-	150
Ning Xiang Dong	150	-	-	150
Liu Chang Le	150	-	-	150
Tan Jin Song	-	-	-	-

Executive Directors

Tan Wan Geng	-	-	-	-
Zhang Zi Fang	-	-	-	-
Xu Jie Bo	-	636	121	757
Li Shao Bin	-	639	120	759

Supervisors

Pan Fu	-	-	-	-
Li Jia Shi	-	636	120	756
Zhang Wei	-	-	-	-
Yang Yi Hua	-	291	122	413
Liang Zhong Gao(Retired on December 26, 2013)	-	300	122	422
Wu De Ming	-	-	-	-
Total	600	2,502	605	3,707

On November 30, 2011, the Company's General Meeting, approved the "H Share Appreciation Rights Scheme of China Southern Airlines Company Limited" and "Initial Grant under the H Share Appreciation Rights Scheme of China Southern Airlines Company Limited" ("the Scheme").

Under the Scheme, 24,660,000 units of Share Appreciation Rights were granted to 118 employees of the Group at the exercise price of HK\$3.92 per unit prior to or on at December 31, 2011. No shares will be issued under the Scheme and each of the Share Appreciation Rights is notionally linked to one existing H Share of the Company. Upon exercise of the Share Appreciation Rights, a recipient will receive an amount of cash equal to the difference between the market share price of the relevant H Share and the exercise price.

The Share Appreciation Rights will have an exercise period of six years from the date of grant. Upon the satisfaction of certain performance conditions after the second, third and fourth anniversary of the date of grant, each one third of the Share Appreciation Rights will become exercisable.

A dividend of RMB0.2 (equivalent to HK\$0.25) (inclusive of applicable tax) and a dividend of RMB0.05 (equivalent to HK\$0.06) per share was approved by the Company's General Meeting on May 31, 2012 and June 18, 2013, respectively, therefore, the exercise price for the Share Appreciation Rights was adjusted to HK\$3.61 per share in accordance with the predetermined formula stipulated in the Scheme. During the year, 8,380,000 units of Share Appreciation Rights were forfeited.

The fair value of the liability for Share Appreciation Rights is measured using the Black-Scholes option pricing model. The risk free rate, expected dividend yield and expected volatility of the share price are used as the inputs into the model. The fair value of the liability for Share Appreciation Rights as of December 31, 2013 was RMB1,893,000 (2012: RMB2,303,000) and a corresponding staff costs of RMB410,000 was reversed for the year ended December 31, 2013 (2012: RMB2,072,000).

#### C. Board Practices.

Each Director's service contract with the Company or any of its subsidiaries provides prorated monthly salary upon termination of employment in accordance with his contract. The Director is entitled to paid leave under his contract. The term of office of a director is three years. The term of office of the current directors will end in 2016. A Director may serve consecutive terms upon re-election.

#### Audit Committee

The Audit Committee is appointed by the Board of Directors and consists of three independent Non-executive Directors. The current members of the Audit Committee are Tan Jing Song, Wei Jin Cai and Ning Xiang Dong. Tan Jing Song is the Chairman of the Audit Committee. The term of office of each member will end in 2016. A member may serve consecutive terms upon re-election. At least once a year, the committee is required to meet with the Company's external auditors without any executive members of the Board in attendance. The quorum necessary for the transaction of any business is two committee members. The Audit Committee held eight meetings in 2013, which were attended by all members.

The Audit Committee is required, amongst other things, to oversee the relationship with the external auditors, to review the Group's interim results and annual financial statements, to monitor compliance with statutory and listing requirements, to review the scope, if necessary, to engage independent legal or other advisers as it determines is necessary and to perform investigations. In addition, the Audit Committee also examines the effectiveness of the Company's internal controls, which involves regular reviews of the internal controls of various corporate structures and business processes on a continuous basis, and takes into account their respective potential risks and severity, in order to ensure the effectiveness of the Company's business operations and the realization of its corporate objectives and strategies. The scope of such examinations and reviews includes finance, operations, regulatory compliance and risk management. The Audit Committee also reviews the Company's internal audit plan, and submits relevant reports and concrete recommendations to the Board on a regular basis.



The Company has an internal audit department which reviews procedures in all major financial and operational activities. This department is led by the head of internal audit.

### **Remuneration and Assessment Committee**

The Remuneration and Assessment Committee is comprised of three members. Currently, the Remuneration and Assessment Committee is chaired by Independent Non-executive Director Ning Xiang Dong with Independent Non-executive Director Tan Jing Song and Non-executive Director Wang Quan Hua as members. The term of office of each member is three years. The term of office of the current members will end in 2016. A member may serve consecutive terms upon re-election. The Remuneration and Assessment Committee held one meeting in 2013, which were attended by all members.

The responsibilities of the Remuneration and Assessment Committee are to make recommendations on the remuneration policy and structure for Directors and senior management of the Company, to establish regular and transparent procedures on remuneration policy development and improvement and submit the Company's "Administrative Measures on Remuneration of Directors" and "Administrative Measures on Remuneration of Senior Management". In particular, the Remuneration and Assessment Committee has the duty to ensure that the Directors or any of their associates shall not be involved in the determination of their own remuneration packages.

The Remuneration and Assessment Committee consulted, when appropriate, the Chairman and/or the President about its proposals relating to the remuneration of other executive Directors. The Remuneration and Assessment Committee is provided with sufficient resources to discharge its duties and professional advice is available if necessary. The Remuneration and Assessment Committee is also responsible for assessing performance of executive Directors and approving the terms of executive Directors' service contracts. The Remuneration and Assessment Committee has performed all its responsibilities under its terms of reference in 2013.

### **Nomination Committee**

The Nomination Committee was established on June 28, 2007. Before that, nomination of Directors and other senior management was mainly undertaken by the Board. According to the Articles of Association, the Board has the authority to appoint from time to time any person as Director to fill a vacancy or as additional Director. In selecting candidate Directors, the Board focuses on their qualifications, technical skills, experiences (in particular, the experience in the industry in which the Group operates in case of candidates of executive directors) and expected contributions to the Group.

As of December 31, 2013, the Nomination Committee consists of three members, including Si Xian Min as Chairman and Wei Jin Cai (Independent Non-executive Director) and Tan Jing Song (Independent Non-executive Director) as members. The responsibilities of the Nomination Committee are to make recommendations to the Board in respect of the size and composition of the Board based on the operational activities, assets and shareholding structure of the Company; study the selection criteria and procedures of Directors and executives and give advice to the Board; identify qualified candidates for Directors and executives; investigate and propose candidates for Directors and managers and other senior management members to the Board.

In accordance with relevant laws and regulations as well as the provisions of the Articles of Association of the Company, the Nomination Committee shall study and resolve on the selection criteria, procedures and terms of office for directors and managers with reference to the Company's actual situation. Any resolution made in this regard shall be filed and proposed to the Board for approval and shall be implemented accordingly. The Nomination Committee is provided with sufficient resources to discharge its duties and independently engages intermediate agencies to provide professional advice on its proposals if necessary.

The Nomination Committee held one meeting in 2013, which was attended by all members.

#### D. Employees.

As of December 31, 2013, the Group had 80,175 employees, including 6,342 pilots, 13,013 flight attendants, 11,709 maintenance personnel, 9,688 passenger transportation personnel, 6,576 cargo transportation personnel, 8,615 ground service personnel, 2,343 flight operation officers, 887 flight security guards, 993 information system personnel, 2,353 financial personnel, and 17,656 other personnel. All of our pilots, flight attendants, maintenance personnel, administrative personnel and sales and marketing personnel are contract employees.

The Company's employees are members of a trade union organized under the auspices of the All-China Federation of Trade Unions, which is established in accordance with the Trade Union Law of China. Two representatives of the Company labor union currently serve on the Supervisory Committee of the Company. Each of the Company's subsidiaries has its own trade union. The Group has not experienced any strikes, slowdowns or labor disputes that have interfered with its operations, and the Group believes that its relations with its employees are good.

All employees of the Group receive cash remuneration and certain non-cash benefits. Cash remuneration consists of salaries, bonuses and cash subsidies provided by the Group. Salaries are determined in accordance with the national basic wage standards. The total amount of wages payable by the Group to its employees is subject to a maximum limit based on the profitability of the Group and other factors. Bonuses are based on the profitability of the Group. Cash subsidies are intended as a form of cost-of-living adjustment. In addition to cash compensation, the Group's contract employees receive certain non-cash benefits, including housing, education and health services, and the Group's temporary employees also receive certain health services, housing fund and education.

#### ***Employee benefits***

Employee benefits are all forms of considerations given and other related expenditures incurred in exchange for services rendered by employees. Except for termination benefits, employee benefits are recognized as a liability in the period in which the associated services are rendered by employees, with a corresponding increase in cost of relevant assets or expenses in the current period.

#### ***Retirement benefits***

Employees of the Group participate in several defined contribution retirement schemes organized separately by the PRC municipal and provincial governments in regions where the major operations of the Group are located. The Group is required to contribute to these schemes at rates ranging from 10% to 22% (2012: 8% to 25%) of salary costs including certain allowances. A member of the retirement schemes is entitled to pension benefits from the Local Labor and Social Security Bureau upon his/her retirement. The retirement benefit obligations of all retired staff of the Group are assumed by these schemes.

In addition, the Group has established a supplementary defined contribution retirement scheme for the benefit of employees in accordance with relevant regulations in the PRC. Employees of the Group participate in a supplementary defined contribution retirement scheme whereby the Group is required to make contributions not exceeding one-twelfth of the prior year's total salaries.

***Housing fund and other social insurances***

The Group contributes on a monthly basis to housing funds organized by municipal and provincial governments based on certain percentages of the salaries of employees. The Group's liability in respect of these funds is limited to the contributions payable in each year. In addition to the housing funds, certain employees of the Group are eligible to one of the following housing benefit schemes:

- Pursuant to a staff housing benefit scheme effective in September 2002, the Group agreed to pay lump sum housing allowances to certain employees who have not received living quarters from CSAHC or the Group according to the relevant PRC housing reform policy. An employee who leaves the Company prior to the end of
- (1) the vesting benefit period is required to pay back a portion of the lump sum housing benefits determined on a pro rata basis of the vesting benefit period. The Group has the right to effect a charge on the employee's house and to enforce repayment through the sale of the house in the event of default in repayment. Any remaining shortfall is reflected in the consolidated income statement. The amount was fully amortized in 2012.
  - (2) The Group also pays cash housing subsidies on a monthly basis to eligible employees. The monthly cash housing subsidies are reflected in the consolidated income statement.

***Termination benefits***

When the Group terminates the employment relationship with employees before the employment contracts expire, or provides compensation as an offer to encourage employees to accept voluntary redundancy, a provision for the termination benefits provided is recognized in the consolidated income statement when both of the following conditions are satisfied:

The Group has a formal plan for the termination of employment or has made an offer to employees for voluntary redundancy, which will be implemented shortly; and

The Group is not allowed to withdraw from termination plan or redundancy offer unilaterally.

### **Workers' Compensation**

There is no workers' compensation or other similar compensation scheme under the Chinese labor and employment system. As required by Chinese law, however, the Group, subject to certain conditions and limitations, pays for the medical expenses of any contract employee who suffer a work-related illness, injury or disability, and continues to pay the full salary of, and provides all standard cash subsidies to, such employee during the term of such illness, injury or disability. The Group also pays for certain medical expenses of its temporary employees.

### **E. Share Ownership.**

On November 30, 2011, the Company's General Meeting, approved the "H Share Appreciation Rights Scheme of China Southern Airlines Company Limited" and "Initial Grant under the H Share Appreciation Rights Scheme of China Southern Airlines Company Limited" ("the Scheme").

Under the Scheme, 24,660,000 units of Share Appreciation Rights were granted to 118 employees of the Group at the exercise price of HK\$3.92 per unit prior to or on at December 31, 2011. No shares will be issued under the Scheme and each of the SAR is notionally linked to one existing H Share of the Company. Upon exercise of the Share Appreciation Rights, a recipient will receive an amount of cash equal to the difference between the market share price of the relevant H Share and the exercise price.

The Share Appreciation Rights will have an exercise period of six years from the date of grant. Upon the satisfaction of certain performance conditions after the second, third and fourth anniversary of the date of grant, each one third of the Share Appreciation Rights will become exercisable.

A dividend of RMB0.2 (equivalent to HK\$0.25) (inclusive of applicable tax) and a dividend of RMB0.05 (equivalent to HK\$0.06) per share was approved by the Company's General Meeting on May 31, 2012 and June 18, 2013, respectively, therefore, the exercise price for the Share Appreciation Rights was adjusted to HK\$3.67 per share in accordance with the predetermined formula stipulated in the Scheme. During the year, 8,380,000 units of Share Appreciation Rights were forfeited.

The fair value of the liability for Share Appreciation Rights is measured using the Black-Scholes option pricing model. The risk free rate, expected dividend yield and expected volatility of the share price are used as the inputs into the model. The fair value of the liability for Share Appreciation Rights as of December 31, 2013 was RMB1,893,000 (2012: RMB2,303,000) and a corresponding staff costs of RMB410,000 was reversed for the year ended December 31, 2013 (2012: RMB2,072,000).

None of our directors and senior management owns any shares or options in the Group as of April 18, 2014.

#### ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS.

##### A. Major Shareholders.

The table below sets forth information regarding the ownership of our share capital as of April 18, 2014 by all persons who are known to us to be the beneficial owners of 5.0% or more of each class of our voting securities.

Title of Shares	Identity of Person or Group	Beneficially Owned <sup>(1)</sup>	Percentage of the Respective Class of Shares <sup>(2)</sup>	Percentage of		
				Total Shares <sup>(2)</sup>		
A shares	CSAHC	4,201,611,678	59.83	%	42.80	%
H shares	HKSCC Nominees Limited <sup>(3)</sup>	1,750,227,298	62.62	%	17.83	%
H shares	CSAHC <sup>(4)</sup>	1,064,770,000	38.10	%	10.85	%
H shares	Nan Lung Holding Limited	1,033,650,000	36.98	%	10.53	%
H shares	FIL Limited	167,462,000 <sup>(5)</sup>	5.99	%	1.71	%

- (1) Beneficial ownership is determined in accordance with the rules of the SEC.

Percentage of A shares and percentage of H shares is based on 7,022,650,000 A shares and 2,794,917,000 H shares, respectively, issued as of April 18, 2014. Percentage of total shares is based on 9,817,567,000 shares issued as of April 18, 2014.

- (3) As custodian of the Depositary for American Depositary Shares representing H Shares. Amount of shares owned by HKSCC Nominees Limited also includes 167,462,000 H shares held by FIL Limited.

(4) Includes 31,120,000 H Shares held by Yazhou Travel Investment Company Limited, representing 1.11% of the total number of H shares and 0.32% of the total number of all outstanding shares, and 1,033,650,000 H Shares held by Nan Lung, representing 36.98% of the total number of H shares and 10.53% of the total number of all outstanding shares.

- (5) Beneficial ownership calculation is based solely on a review on April 24, 2014 of disclosure of interest forms filed by FIL Limited with the Hong Kong Stock Exchange.

Shareholders of H Shares and A shares enjoy the same voting rights with respect to each share. None of our major shareholders has voting rights that differ from the voting rights of other shareholders. We are not aware of any arrangement which may at a subsequent date result in a change of control of our Company.

As of April 18, 2014, there were 48 registered holders of 2,801,564 American Depositary Shares in the United States, consisting of 1.4% of our outstanding shares. Since certain of the ADSs are held by nominees, the above number may not be representative of the actual number of U.S. beneficial holders of ADSs or the number of ADSs beneficially held by U.S. persons.

Our Company is currently a majority-owned subsidiary of CSAHC, which is an entity wholly-owned by the Chinese government.

#### B. Related Party Transactions.

For a detailed description of our related party transactions, please see Note 47 to the Financial Statements. In particular, the following arrangements, which the Company believes are material to its operations, have been made between the Company and CSAHC and its affiliates during the year ended December 31, 2013 and up to the latest practicable date. The Company believes that these arrangements have been entered into by the Company in the ordinary course of business and in accordance with the agreements governing such transactions.

## Arrangements with CSAHC

### ***De-merger Agreement***

The De-merger Agreement dated March 25, 1995 (such agreement was amended by the Amendment Agreement No.1 dated May 22, 1997) was entered into between CSAHC and the Company for the purpose of defining and allocating the assets and liabilities between CSAHC and the Company. Under the De-merger Agreement, CSAHC and the Company have agreed to indemnify the other party against claims, liabilities and expenses incurred by such other party relating to the businesses, assets and liabilities held or assumed by CSAHC or the Company pursuant to the De-merger Agreement.

Neither the Company nor CSAHC has made any payments in respect of such indemnification obligations from the date of the De-merger Agreement up to the date of this Annual Report.

### ***Trademark License Agreement***

The Company and CSAHC entered into a ten-year trademark license agreement dated May 22, 1997. Pursuant to which CSAHC acknowledges that the Company has the right to use the name “China Southern” and “China Southern Airlines” in both Chinese and English, and grants the Company a renewable and royalty free license to use the kapok logo on a worldwide basis in connection with the Company’s airline and airline-related businesses. Unless CSAHC gives a written notice of termination three months before the expiration of the agreement, the agreement will be automatically renewed for another ten-year term. In May 2007, the trademark license agreement entered into by the Company and CSAHC was automatically renewed for ten years.



## *Leases*

The Group (as lessee) and CSAHC (as lessor) entered into lease agreements as follows:

(1) On December 29, 2008, the Company renewed a master asset lease agreement with CSAHC with a term valid from January 1, 2009 to December 31, 2011 (the “Existing Asset Lease Agreement”).

The Company and CSAHC entered into the new Asset Lease Agreement (the “New Asset Lease Agreement”) on September 25, 2012 to renew the leases transactions for a term of three years from January 1, 2012 to December 31, 2014. Pursuant to the New Asset Lease Agreement, CSAHC agrees to continue to lease to the Company certain parcels of land, properties, and civil aviation structures and facilities at existing locations in Guangzhou, Haikou, Wuhan, Hengyang, Jingzhou (previously known as “Shashi”), Zhanjiang and Changsha. The annual rents payable to CSAHC under the New Asset Lease Agreement is RMB35,924,400 for the three years ending December 31, 2014.

The Company also entered into the individual lease agreement (the “2012 Property Lease Agreement”) with CSAHC on September 25, 2012 in relation to certain fragmented leases for properties located in Harbin, Changchun, Dalian, Beijing and Shanghai as originally covered in the Existing Asset Lease Agreement for an aggregate annual rental of RMB4,437,000 for a term of two years from January 1, 2012 to December 31, 2013.

The Company further entered into the Lease Agreement of Nanyang Base Assets (the “Nanyang Asset Lease Agreement”) with CSAHC on January 24, 2013 for the leases transaction relating to certain lands and properties at Nanyang Jiangying Airport as originally covered in the existing Asset Lease Agreement for the period from January 1, 2012 to December 31, 2012. The rent payable under the Nanyang Asset Lease Agreement was RMB12,441,000. As the Nanyang Asset Lease Agreement had expired and the lease transaction contemplated under the Nanyang Asset Lease Agreement would continue to be entered into on a recurring basis, the Company further entered into the 2013 Nanyang Asset Lease Agreement (the “2013 Nanyang Asset Lease Agreement”) with CSAHC on April 19, 2013, pursuant to which CSAHC agreed to lease to the Company certain lands, properties, facilities and structures at Nanyang Jiangying Airport for a term of two years, commencing from January 1, 2013 to December 31, 2013. The annual rent payable by the Company to CSAHC under the lease agreement was RMB30,259,100.

For the year ended December 31, 2013, the rent incurred by the Group amounted to RMB70,620,000 pursuant to the New Asset Lease Agreement, 2012 Property Lease Agreement, Nanyang Asset Lease Agreement and 2013 Nanyang Asset Lease Agreement.

(2)

The Company and CSAHC entered into an indemnification agreement dated May 22, 1997 in which CSAHC has agreed to indemnify the Company against any loss or damage caused by or arising from any challenge of, or interference with, the Company's right to use certain lands and buildings.

On February 14, 2011, in order to ensure normal operation of the Company, the Company, based on the actual leasing requirement, once again reviewed the land and properties contemplated under the lease, adjusted part of these projects, and engaged a real estate appraisal company to assess the rent of land, properties, structures and (3) pipes under the lease. It then determined the rent according to the assessment and re-entered into the Land Lease Contract and the Tenancy Contract. Pursuant to the Land Lease Contract, the parties agreed that the annual rent for land from 2011 to 2013 would be RMB56,329,131. Pursuant to the Tenancy Contract, the annual rent for properties, structures and pipes leased by the Company from CSAHC from 2011 to 2013 would be RMB42,975,542.

For the year ended December 31, 2013, the rents for land lease and property lease incurred by the Group amounted to RMB56,329,000 and RMB42,508,000 respectively pursuant to the lease agreements.

(4) On January 9, 2014, the Company and CSAHC have entered into two new lease agreements (the “Lease Agreements”), namely, the property lease agreement (the “Property Lease Agreement”) and the land lease agreement (the “Land Lease Agreement”) to renew the land and property leases transactions contemplated thereunder for the period from January 1, 2014 to December 31, 2016. Pursuant to the Property Lease Agreement, CSAHC agreed to lease certain properties, facilities and other infrastructure located in various cities such as Guangzhou, Shenyang, Dalian, Harbin, Xinjiang, Changchun, Beijing and Shanghai held by CSAHC or its subsidiaries to the Company for office use related to the civil aviation business development. The property lease transactions contemplated under the existing 2012 Property Lease Agreements have now been covered under the Property Lease Agreement so as to save resources as well as time of management of various property leases with CSAHC. Pursuant to the Land Lease Agreement, CSAHC agreed to lease certain lands located in Xinjiang, Harbin, Changchun, Dalian and Shenyang by leasing the land use rights of such lands to the Company for the purposes of civil aviation and related businesses of the Company. The maximum annual aggregate amount of rent payable by the Company to CSAHC under the Property Lease Agreement and the Land Lease Agreement for each of the three years ending December 31, 2016 shall not exceed RMB40,114,700 and RMB63,582,200, respectively, and such payment shall be made quarterly.

***SAIETC, a wholly-owned subsidiary of CSAHC***

On January 28, 2011, the Company renewed the Import and Export Agency Framework Agreement with SAIETC. The scope of cooperation under the agreement covers import and export services, custom clearing services, customs declaration and inspection services, and tendering and agency services etc. The agreement is effective for a period from January 1, 2011 to December 31, 2013, with the annual cap for the commission not exceeding RMB97,200,000.

On April 19, 2013, the Company entered into the Supplemental Agreement to the Import and Export Agency Framework Agreement dated January 28, 2011 with SAIETC to revise the maximum annual service fee payable by the Company to SAIETC for the period from January 1, 2013 to December 31, 2013 from RMB97.2 million to RMB160 million.

For the year ended December 31, 2013, the agency fee incurred by the Group in respect of the above import and export services was RMB120,876,000.

On January 9, 2014, the Company and SAIETC have entered into a new import and export agency framework agreement (the “New Import and Export Agency Framework Agreement”) to renew the continuing connected transactions contemplated therein for a fixed term of three years commencing from January 1, 2014 to December 31, 2016. During the period of the New Import and Export Agency Framework Agreement, the annual cap shall remain at RMB160 million per annum.

***Southern Airlines Culture and Media Co., Ltd. (“SACM”), which is 40% owned by the Company and 60% owned by CSAHC***

On May 11, 2010, the Company renewed the Media Services Framework Agreement with SACM, for a term of three years commencing from January 1, 2010. Pursuant to the agreement, the Company has appointed SACM to provide advertising agency services, production of in-flight TV and movie program agency services, public relations services relating to recruitments of airhostess, and services relating to the distribution of newspapers and magazines. The parties have determined the various rates for providing advertising services after negotiations on an arm’s length basis, and SACM has promised that the advertising fees for which they charged the Company were all based on the prevailing market prices for similar businesses which were accepted by the Company. The annual cap under the agreement for each year is RMB40,000,000, RMB48,000,000 and RMB58,000,000, respectively.

On April 19, 2013, the Company entered into a new Media Services Framework Agreement with SACM to renew the annual cap, expand the services scope and extend the term for an additional term of three years, commencing from January 1, 2013 to December 31, 2015. Pursuant to the agreement, the Company has appointed SACM to provide advertising agency services, plotting, purchase and production of in-flight TV and movie program agency services, channel publicity and production services, public relations services relating to recruitments of airhostess, and services relating to the distribution of newspapers and magazines. The annual cap under the agreement for each year is RMB98 million, RMB105 million and RMB113 million for each of years ended December 31, 2013, 2014 and 2015, respectively.

For the year ended December 31, 2013, the media fees incurred by the Group for the media services amounted to RMB77,266,000.

***Southern Airlines Group Finance Company Limited (“SA Finance”), which is 66% owned by CSAHC, 21% owned by the Company and 13% owned in aggregate by four subsidiaries of the Company***

On November 8, 2010, the Company renewed the Financial Services Framework Agreement with SA Finance for a term of three years starting from January 1, 2011 to December 31, 2013.

Under such agreement, SA Finance agrees to provide to the Company deposit and loan services. SA Finance shall pay interests to the Company regularly at a rate not lower than the current deposit rates set by the People's Bank of China. The Group's deposits placed with SA Finance were re-deposited in a number of banks. SA Finance has agreed that the loans provided to CSAHC and its subsidiaries other than the Group should not exceed the sum of SA Finance's shareholders' equity, capital reserves and total deposits received from other companies (excluding the Group). The rates should be determined on an arm's length basis and based on fair market rate, and should not be higher than those available from independent third parties. The parties agreed that the balance of the Group's deposits placed with SA Finance (including accrued interests) should not at any time exceed RMB4,000,000,000, nor should the balance of loans borrowed from SA Finance at any time exceed the above-mentioned level. The annual cap of fees payable to SA Finance for the other financial services should not exceed RMB5,000,000.

On March 16, 2012, the Company entered into a supplemental agreement to the Financial Services Framework Agreement with SA Finance, for a term effective from May 31, 2012, the date of passing of the resolution at the General Meeting, to December 31, 2013. In line with the Company's business requirement, the parties agreed that deposit balance placed with SA Finance (including interest payable accrued thereon) in any day may not exceed RMB6,000,000,000, and the balance for provision of loan service to the Company by SA Finance (including total interests paid) in any day may not exceed the above level.

On November 8, 2013, the Company and SA Finance entered into the new Financial Services Framework Agreement for a term of three years starting from January 1, 2014 to December 31, 2016 to renew the provision of the financial services contemplated under the Financial Services Framework Agreement.

Under the new Financial Services Framework Agreement, SA Finance agrees to provide to the Company deposit services, loan services and other financial services. SA Finance shall accept deposit of money from the Group at interest rates not lower than those set by the People's Bank of China, or PBOC for the same term of deposit. SA Finance will in turn deposit the whole of such sums of money with certain stated-owned commercial banks and listed commercial banks to control the risk. SA Finance shall make loans or provide credit line services to the Group and the entering into of separate loan agreements, which will set out the terms and conditions of the loans, upon application by the Company during the term of the new Financial Services Framework Agreement. SA Finance shall not charge interest rates higher than those set by the PBOC for similar loans. The total amount of outstanding loans extended by SA Finance to CSAHC (excluding the Group) must not exceed the sum of SA Finance's shareholders' equity, capital reserves and money deposit received from other parties (except the Group). The interest rate for loans provided to the Group by SA Finance shall not be higher than the basis rate allowed by the PBOC for the same type of loan and, subject to the above, the interest rate charged on the loans to the Group shall be equal to or lower than the rate charged by normal commercial banks in the PRC for comparable loans (whichever is lower). Upon request by the Company, SA Finance shall also provide other financial services to the Group, including financial and financing consultation, credit certification and other relevant advice and agency services, insurance agency services, and other businesses which SA Finance are approved by China Banking Regulatory Commission, or CBRC to operate by entering into of separate agreements, which will set out the terms and conditions of such services. The parties agreed that the balance of the Company's deposits placed with SA Finance (including accrued interests) should not at any time exceed RMB6,000,000,000, nor should the balance of loans borrowed from SA Finance at any time exceed the above-mentioned level. The annual cap of fees payable to SA Finance for the other financial services should not

exceed RMB5,000,000.

As of December 31, 2013, the Group's deposits placed with SA Finance amounted to RMB2,675,443,000, the outstanding loans provided by SA Finance amounted to RMB520,000,000.

***China Southern Airlines Group Passenger and Cargo Agent Company Limited ("PCACL"), a wholly-owned subsidiary of CSAHC***

The Company and PCACL entered into a Sales Agency Services Framework Agreement dated January 28, 2011, which is valid from January 1, 2011 to December 31, 2013. The Company and PCACL entered into a new Passenger and Cargo Sales Agency Services Framework Agreement dated November 8, 2013, which is valid from January 1, 2014 to December 31, 2016 to renew the continued cooperation with PCACL. Pursuant to the new Passenger and Cargo Sales Agency Services Framework Agreement, the cooperative scope of both parties thereto mainly comprises extended businesses including air ticket sales agency services, airfreight forwarding sales agency services, chartered flight and pallets sales agency services, internal operation services for the inside storage area, and delivery services for the outside storage area. PCACL charges commission with reference to the prevailing market rate. Besides, the Company has other air ticket sales agents in China who also charge commission at the same rates. PCACL also acts as the ticket sales agents of other airline companies in China, and charge commission at the same rates offered to the Group. The annual transaction cap of the sales value shall not exceed RMB250,000,000.

For the year ended December 31, 2013, the commission expense and goods handling fee paid to PCACL were RMB19,226,000 and RMB32,739,000 respectively, and the income relating to other services was RMB107,238,000.

***Guangzhou China Southern Airlines Property Management Company Limited (the “GCSAPMC”), a wholly-owned subsidiary of CSAHC***

The Company and GCSAPMC renewed the Framework Agreement for the Engagement of Property Management (the “existing Property Management Framework Agreement”) on December 29, 2008 for a term of three years.

The Company has entered into a New Framework Agreement for Engagement of Property Management (the “New Property Management Framework Agreement”) on December 28, 2012 to renew the property management transactions for a term of three years from January 1, 2012 to December 31, 2014. Pursuant to the New Property Management Framework Agreement, the Company has renewed the appointment of GCSAPMC for provision of property management and maintenance services for the Company’s leased properties in the airport terminal, the base and the 110KV transformer substation at the new Baiyun International Airport (other than certain properties in the Company’s headquarter located in the old Baiyun Airport which were covered in the existing Property Management Framework Agreement) to ensure the ideal working conditions of the Company’s production and office facilities and physical environment, and the normal operation of equipment.

The Company has further entered into the airport property management framework agreement (the “Airport Property Management Framework Agreement”) on January 11, 2013 to renew the property management at the old Baiyun Airport for a term of three years from January 1, 2012 to December 31, 2014. Pursuant to the Airport Property Management Framework Agreement, the Company has renewed the appointment of GCSAPMC for the provision of property management and maintenance services for the Company’s properties at the old Baiyun Airport and surrounding in Guangzhou.

The fee charging schedule (or charge standard) under the New Property Management Framework Agreement and the Airport Property Management Framework Agreement shall be determined on an arm’s length basis between both parties, and shall not be higher than the one charged by any independent third parties in the similar industry. The annual cap for the New Property Management Framework Agreement and the Airport Property Management Framework Agreement are set at RMB32,750,000 and RMB22,250,000, respectively.

On December 31, 2013, the Company further entered into an agreement supplemental to the New Property Management Framework Agreement (the “New Property Management Supplemental Agreement”) and an agreement supplemental to the Airport Property Management Framework Agreement (the “Airport Property Management Supplemental Agreement”). Pursuant to the New Property Management Supplemental Agreement, the parties have

agreed to revise the services fee in relation to the provision of property management and maintenance services by GCSAPMC for the Company's leased properties at the airport terminal, the base and the 110KV transformer substation at the new Baiyun International Airport from RMB32,750,000 per annum to RMB42,700,000 per annum for the year ended December 31, 2014. Pursuant to the Airport Property Management Supplemental Agreement, the parties have agreed to revise the services fee in relation to provision of property management and maintenance services by GCSAPMC for the Company's several properties at the old Baiyun Airport and surrounding in Guangzhou from RMB22,250,000 per annum to RMB27,300,000 per annum for the year ended December 31, 2014.

For the year ended December 31, 2013, the property management and maintenance fee incurred by the Group amounted to RMB63,915,000 pursuant to the New Property Management Framework Agreement and the Airport Property Management Framework Agreement.

***Shenzhen Air Catering Co., Ltd. (the "SACC"), which is 50.1% owned by CSAHC***

The Company entered into a Catering Services Framework Agreement with Shenzhen Air Catering Co., Ltd., a non-wholly-owned subsidiary of CSAHC on April 19, 2013 for a term of three years, commencing from January 1, 2013 to December 31, 2015, pursuant to which SACC agrees to provide the in-flight lunch box, and order, supply, allot, recycle, store and install the in-flight supply with their respective services for the arrival and departure flights designated by the Group at the airport where SACC located at. The maximum annual aggregate amount of the services fee payable by the Company to SACC shall not exceed RMB100 million, RMB115 million and RMB132.5 million for each of the years ended December 31, 2013, 2014 and 2015, respectively.

For the year ended December 31, 2013, the services fee incurred by the Group for the catering services amounted to RMB83,732,000.



***Zhuhai MTU, which is 50% owned by CSAHC***

The Company entered into an agreement relating to continuing connected transactions with CSAHC, MTU Aero Engines GmbH (“MTU GmbH”) and Zhuhai MTU on September 28, 2009, by which Zhuhai MTU shall continue to provide the Company with engine repair and maintenance services subject to the international competitiveness and at the net most favorable terms, while the Company shall make relevant payment to Zhuhai MTU according to related charging standard. The agreement is effective from its date to April 5, 2031. The maximum aggregate annual consideration for the continuing connected transactions under the above agreement were disclosed in the announcement of the Company dated September 28, 2009 and such maximum aggregate annual consideration for the year ended December 31, 2012 is RMB1.2 billion.

For the year ended December 31, 2013, the Group’s engine repair and maintenance service fees incurred under the agreement amounted to RMB795,526,000.

***Sale of Aircraft to Hebei Airlines Company Limited (“Hebei Airlines”) by Xiamen Airlines***

On September 26, 2012, the Board announced that Xiamen Airlines and Hebei Airlines entered into the Aircraft Sale Agreement, pursuant to which Xiamen Airlines agreed to sell and Hebei Airlines agreed to purchase one B737-800 aircraft at the consideration of approximately RMB257 million.

***Sale of 51% Equity Interests in XAMC***

On June 29, 2012, the Board announced that Xiamen Airlines and SACM entered into an agreement, pursuant to which Xiamen Airlines agreed to sell and SACM agreed to purchase 51% equity interests in XAMC at the consideration of RMB43.12 million. The Company believes that the disposal of the 51% equity interests in XAMC can promote the integration of media resources owned by SACM and XAMC, and they can achieve a better development by mutual use of the platforms and resources owned by each other. As XAMC shall be owned as to 49% by Xiamen Airlines, Xiamen Airlines shall continue to benefit from long-term development of XAMC.

***Subscription of New A Shares by CSAHC***

On June 11, 2012, the Board approved the proposed issuance of not more than 487,804,878 new A Shares (after the adjustment with reference to the profit distribution proposal for 2011) to CSAHC at the subscription price of RMB4.10 (after the adjustment with reference to the profit distribution proposal for 2011) per A Share (the “Non-public A Share Issue”). The proceeds to be raised from the proposed Non-public A Share Issue will be not more than RMB2 billion. CSAHC entered into the Subscription Agreement with the Company, pursuant to which CSAHC has conditionally agreed to subscribe for and the Company has conditionally agreed to allot and issue not more than 487,804,878 new A Shares for an aggregate consideration of not more than RMB2 billion, equivalent to the subscription price of RMB4.10 per new A Share (the “Subscription”). As of August 9, 2013, the relevant work regarding the 2012 Non-public A Share Issue of the Company has not been completed. The proposal for the 2012 Non-public A Share Issue of the Company and A Shares subscription agreement therefore were lapsed automatically due to the expiration of the resolution passed at the general meeting.

All related party transactions have been approved by Independent Non-executive Directors.

C. Interests of Experts and Counsel.

Not applicable.

## ITEM 8. FINANCIAL INFORMATION.

A. Consolidated Statements and Other Financial Information.

Our audited consolidated financial statements are set forth beginning on page F-1, which can be found after Item 19.

## Legal Proceedings

The Company received a claim on July 11, 2011 from an overseas entity (the “claimant”) against the Company for the alleged breach of certain terms and conditions of an aircraft sale agreement. The claimant has made a claim against the Company for an indemnity of US\$46 million or for the refund of the down payments of US\$12 million, and the interest thereon which is calculated in accordance with Clause 35A, Supreme Court Act 1981 of the United Kingdom. In 2012, the claimant subsequently changed its claim for the refund of the down payment to US\$13 million. On July 25, 2013, the High Court of the United Kingdom rendered a judgment on this case, which dismissed the claim made by the claimant and ordered the claimant to pay an indemnity of US\$28 million to the Company plus legal fees and the interest thereon. The claimant has filed an appeal against this judgment thereafter. The directors are of the opinion that an outflow of resource embodying economic benefits is not probable to occur.

## Dividend Information

A dividend in respect of the year ended December 31, 2013 of RMB0.4 (inclusive of applicable tax) per ten shares, amounting to a total dividend of RMB393 million was proposed by the Directors on March 28, 2014. The final dividend proposed after the end of the financial year has not been recognized as a liability at the end of the financial year.

Our Board declares dividends, if any, in Renminbi with respect to H Shares on a per share basis and pays such dividends in Hong Kong dollars. Any final dividend for a fiscal year is subject to shareholders’ approval. Bank of New York Mellon, as depositary, converts the HK dollar dividend payments and distributes them to holders of ADSs in U.S. dollars, less expenses of conversion. Under the Company Law of the PRC and our Articles of Association, all of our shareholders have equal rights to dividends and distributions. The holders of the H Shares share proportionately on a per share basis in all dividends and other distributions declared by our Board, if any, based on the foreign exchange conversion rate published by the People’s Bank of China, or PBOC, on the date of the distribution of the cash dividend.

We believe that our dividend policy strikes a balance between two important goals providing our shareholders with a competitive return on investment and assuring sufficient reinvestment of profits to enable us to achieve our strategic objectives. The declaration of dividends is subject to the discretion of our Board, which takes into account the following factors:

- our financial results;
- capital requirements;

- contractual restrictions on the payment of dividends by us to our shareholders or by our subsidiaries to us;
- our shareholders interests;
- the effect on our creditworthiness;
- general business and economic conditions; and
- other factors our Board may deem relevant.

Pursuant to PRC laws and regulations and the Articles of Association of the Company, dividends may only be distributed after allowance has been made for: (i) recovery of losses, if any, and (ii) allocations to the statutory surplus reserve. The allocation to the statutory surplus reserve is 10% of our net profit determined in accordance with PRC GAAP. Our distributable profits for the current fiscal year will be equal to our net profits determined in accordance with IFRSs, less allocations to the statutory surplus reserve.

#### B. Significant Changes.

No significant changes have occurred since the date of the consolidated financial statements.

### ITEM 9. THE OFFER AND LISTING.

#### A. Offer and Listing Details.

The principal trading market for the Company's H Shares is the Hong Kong Stock Exchange, and the Company's trading code is "1055". The Company completed its initial public offering of H Shares on July 30, 1997. The ADRs, each representing 50 H Shares, have been listed for trading on the New York Stock Exchange since July 31, 1997, under the symbol "ZNH".

The principal trading market for the Company's A Shares is the Shanghai Stock Exchange with trading code of "600029". On July 25, 2003, the Company completed its initial public offering of A Shares.

Set forth below for the periods indicated are the high and low sales prices of H Shares on the Hong Kong Stock Exchange, ADRs on the New York Stock Exchange and A Shares on the Shanghai Stock Exchange.

	The Hong Kong Stock Exchange Price per H Share (HK\$)		The New York Stock Exchange Price per ADR (US\$)		The Shanghai Stock Exchange Price per A Share (RMB)	
	High	Low	High	Low	High	Low
Annual Market Prices						
Fiscal Year ended December 31, 2009	2.99	1.14	19.45	7.09	7.22	3.28
Fiscal Year ended December 31, 2010	5.91	2.47	38.65	15.98	12.58	5.84
Fiscal Year ended December 31, 2011	5.37	3.08	35.40	20.02	10.13	4.57
Fiscal Year ended December 31, 2012	4.54	3.22	29.72	20.20	5.48	3.28
Fiscal Year ended December 31, 2013	4.43	2.61	30.04	17.09	4.3	2.54
Quarterly Market Prices						
Fiscal Year ended December 31, 2012						
First Quarter	4.54	3.40	29.72	22.31	5.48	4.47
Second Quarter	3.66	3.22	23.52	20.20	5.02	4.51
Third Quarter	3.90	3.25	25.40	20.93	4.77	3.28
Fourth Quarter	4.00	3.40	26.07	21.40	3.91	3.30
Fiscal Year ended December 31, 2013						
First Quarter	4.68	3.89	30.04	25.15	4.21	3.64
Second Quarter	4.43	2.94	28.89	19.67	3.70	2.68
Third Quarter	3.14	2.61	20.63	17.09	3.23	2.54
Fourth Quarter	3.48	2.69	22.19	17.95	3.01	2.66
Monthly Market Prices						
October 2013	3.08	2.80	19.89	18.09	2.93	2.68
November 2013	3.48	2.69	21.93	17.95	2.99	2.68
December 2013	3.48	2.95	22.19	19.201	3.01	2.66
January 2014	3.08	2.66	19.75	17.06	2.75	2.55
February 2014	2.86	2.42	18.59	16.06	2.77	2.54
March 2014	2.75	2.45	17.34	15.89	2.63	2.46
April 2014 (up to April 18, 2014)	2.64	2.41	16.85	15.72	2.61	2.50

#### B. Plan of Distribution.

Not applicable.

#### C. Markets.

See “Offer and Listing Details” above.

D. Selling Shareholders.

Not applicable.

E. Dilution.

Not applicable.

F. Expenses of the Issue.

Not applicable.

#### ITEM 10. ADDITIONAL INFORMATION.

A. Share Capital.

Not applicable.

B. Memorandum and Articles of Association.

The following is a summary of certain provisions of our Articles of Association. As this is a summary, it does not contain all the information that may be important to you. You and your advisors should read the text of our most updated Articles of Association for further information, which is filed as an exhibit to this Annual Report.

#### **General**

The Company is registered with and has obtained a business license from the State Administration Bureau of Industry and Commerce of the People's Republic of China on March 25, 1995. On March 13, 2003, the Company obtained an approval certificate from the Ministry of Commerce to change to a permanent limited company with foreign investments.

#### ***Other Senior Administrative Officers***

Pursuant to the Article 16 of the Articles of Association, other senior administrative officers of the Company refer to executive vice president, chief financial officer, the board secretary, chief economist, chief engineer, chief pilot, and chief legal adviser and chief information officer.

### ***Objects and Purposes***

Pursuant to the Article 18 of the Articles of Association, the scope of business of the Company includes: (I) provision of scheduled and non-scheduled domestic, regional and international air transportation services for passengers, cargo, mail and luggage; (II) undertaking general aviation services; (III) provision of aircraft repair and maintenance services; (IV) acting as agent for other domestic and international airlines; (V) provision of air catering services; (VI) provision of hotel business; (VII) acting as sale agent for aircraft leasing and aviation accident insurance; (VIII) engaging in other airline or airline-related business, including advertising for such services; and (IX) insurance agency business. (subject to approved of State Administration of Industry and Commerce).

### **Directors**

Pursuant to Article 243 of the Articles of Association, where a Director of the Company is in any way, directly or indirectly, materially interested in a contract, transaction or arrangement or proposed contract, transaction or arrangement with the Company, other than his contract of service with the Company, he shall declare the nature and extent of his interests to the Board of Directors at the earliest opportunity, whether or not the contract, transaction or arrangement or proposal is otherwise subject to the approval of the Board of Directors. For the purposes of this Article, a director is deemed to be interested in a contract, transaction or agreement in which an associate of him is interested.

Pursuant to Article 173 of the Articles of Association, where a Director is interested in any resolution proposed at a board meeting, such Director shall not be present and shall not have a right to vote. Such Director shall not be counted in the quorum of the relevant meeting. Such directors also shall not vote on behalf of other directors. Board meetings may be convened by more than half of the directors who are not interested in the proposal. Resolutions of board meetings shall be passed by more than half of directors who are not interested in the proposal.



Pursuant to Article 251 of the Articles of Association, the Company shall, with the prior approval of shareholders in general meeting, enter into a contract in writing with a Director wherein his emoluments are stipulated. The aforesaid emoluments include, emoluments in respect of his service as Director, Supervisor or senior administrative officer of the Company or any subsidiary of the Company, emoluments in respect of the provision of other services in connection with the management of the affairs of the Company and any of its subsidiaries, and payment by way of compensation for loss of office, or as consideration for or in connection with his retirement from office. There is no specific provisions concerning a director's power, in the absence of an independent quorum, to vote compensation to themselves or any members of their body, other than the above Article 173 with respect to a director's voting power in matters he is materially interested.

### **Ordinary Shares**

Pursuant to Article 26 of the Articles of Association, subject to the approval of the securities authority of the State Council, the Company may issue and offer shares to domestic investors or foreign investors for subscription. Foreign investors are those investors of foreign countries and regions of Hong Kong, Macau and Taiwan who subscribe for shares issued by the Company. Domestic investors are those investors within the territory of the PRC (excluding investors of the regions referred to in the preceding sentence) who subscribe for shares issued by the Company.

Pursuant to Article 27 of the Articles of Association, shares issued by the Company to domestic investors for subscription in Renminbi shall be referred to as "Domestic-Invested Shares". Shares issued by the Company to foreign investors for subscription in foreign currencies shall be referred to as "Foreign-Invested Shares". Foreign-Invested Shares which are listed overseas are called "Overseas-Listed Foreign-Invested Shares". The foreign currencies mean the legal currencies (apart from Renminbi) of other countries or districts which are recognized by the foreign exchange control authority of the state and can be used to pay the Company for the share price.

Pursuant to Article 28 of the Articles of Association, Domestic-Invested Shares issued by the Company are called "A Shares". Overseas-Listed Foreign-Invested Shares issued by the Company and listed in Hong Kong are called "H Shares". H Shares are shares which have been admitted for listing on the Stock Exchange of Hong Kong Limited, the par value of which is denominated in Renminbi and which are subscribed for and traded in Hong Kong dollars. H Shares can also be listed on a stock exchange in the United States of America in the form of ADR. Shares issued by the Company, including A Shares and H Shares, are all ordinary shares.

Pursuant to Article 62 of the Articles of Association, the ordinary shareholders of the Company shall enjoy the following rights:

(1) the right to attend or appoint a proxy to attend shareholders' general meetings and to vote thereat;

(2) the right to dividends and other distributions in proportion to the number of shares held;

(3) the right of supervisory management over the Company's business operations, and the right to present proposals or enquiries;

(4) the right to transfer, donate or pledge his shares in accordance with laws, administrative regulations and provisions of these Articles of Association;

(5) the right of knowledge and decision making power with respect to important matters of the Company in accordance with laws, administrative regulations and these Articles of Association;

(6) the right to obtain relevant information in accordance with the provisions of these Articles of Association, including:

(i) the right to obtain a copy of these Articles of Association, subject to payment of the cost of such copy;

(ii) the right to inspect and copy, subject to payment of a reasonable charge;

(iii) all parts of the register of shareholders;

(a) personal particulars of each of the Company's directors, supervisors, president and other senior administrative officers, including:

(aa) present name and alias and any former name or alias;

(bb) principal address (residence);

(cc) nationality;

(dd) primary and all other part-time occupations and duties;

(ee) identification documents and their relevant numbers;

(b) state of the Company's share capital;

reports showing the aggregate par value, quantity, highest and lowest price paid in respect of each class of shares  
(c) repurchased by the Company since the end of last accounting year and the aggregate amount paid by the Company for this purpose;

(d) minutes of shareholders' general meetings; and

(e) interim and annual reports of the Company.

(7) in the event of the termination or liquidation of the Company, to participate in the distribution of surplus assets of the Company in accordance with the number of shares held; and

(8) other rights conferred by laws, administrative regulations and these Articles of Association.

According to Article 266, dividends shall be distributed in accordance with the proportion of shares held by shareholders.

According to Article 67 of the Articles of Association, shareholders of the company have the obligation not to withdraw their shares unless required by laws and regulations.

According to Article 37 of the Articles of Association, the Company may repurchase its issued shares under the following circumstances: (1) cancellation of shares for the reduction of its capital; (2) merging with another company that holds shares in the Company; (3) awarding its employees with shares; (4) at the request of the dissenting shareholders; and (5) other circumstances permitted by laws and administrative regulations.

According to Article 41 of the Articles of Association, unless the Company is in the course of liquidation, it must comply with the following provisions in relation to repurchase of its issued shares: (1) where the Company repurchases shares of the Company at par value, payment shall be made out of book surplus distributable profits of the Company or out of proceeds of a fresh issue of shares made for that purpose; (2) where the Company repurchases shares of the Company at a premium to its par value, payment up to the par value may be made out of the book surplus distributable profits of the Company or out of the proceeds of a fresh issue of shares made for that purpose; and (3) payment by the Company in consideration of the following shall be made out of the Company's distributable profits: (i) acquisition of rights to repurchase shares of the Company; (ii) Variation of any contract to repurchase shares of the Company; and (iii) release of any of the Company's obligation under any contract to repurchase shares of the Company.

According to Article 263 of the Articles of Association, when distributing each year's after-tax profits, the Company shall set aside 10% of such profits for the Company's statutory common reserve fund, except where the accumulated balance of the said fund has reached 50% of the Company's registered capital. After the Company has allocated its after-tax profits to the statutory common reserve fund, it may, with the approval of the shareholders by way of resolution in a shareholders' general meeting, further allocate its after-tax profits to the discretionary common reserve fund.

According to Article 67 of the Articles of Association, shareholders are not liable to make any further contribution to the share capital other than as agreed by the subscriber of the relevant shares on subscription.

The Articles of Association does not have specific provisions discriminating against any existing or prospective holder of such securities as a result of other shareholders owning a substantial number of shares.

### **Action Necessary to Change Rights of Shareholders**

Pursuant to Article 151 of the Articles of Association, shareholders who hold different classes of shares are shareholders of different classes. The holders of the Domestic Shares and holders of Overseas Listed Foreign Shares are deemed to be shareholders of different classes.

Pursuant to Article 152 of the Articles of Association, rights conferred on any class of shareholders in the capacity of shareholders (“class rights”) may not be varied or abrogated unless approved by a special resolution of shareholders in general meeting and by holders of shares of that class at a separate meeting.

Pursuant to Article 154 of the Articles of Association, shareholders of the affected class, whether or not otherwise having the right to vote at shareholders’ general meetings, shall nevertheless have the right to vote at class meetings in respect of the following matters: (i) to effect an exchange of all or part of the shares of such class into shares of another class or to effect an exchange or create a right of exchange of all or part of the shares of another class into the shares of such class; (ii) to restrict the transfer or ownership of the shares of such class or add to such restriction; (iii) to restructure the Company where the proposed restructuring will result in different classes of shareholders bearing a disproportionate burden of such proposed restructuring; and (iv) to vary or abrogate the provisions of these Articles of Association. However, interested shareholder(s) shall not be entitled to vote at class meetings.

Pursuant to Article 155 of the Articles of Association, resolutions of a class of shareholders shall be passed by votes representing more than two-thirds of the voting rights of shareholders of that class represented at the relevant meeting who are entitled to vote at class meetings.

Pursuant to Article 156 of the Articles of Association, written notice of a class meeting shall be given forty-five days before the date of the class meeting to notify all of the shareholders in the share register of the class of the matters to be considered, the date and the place of the class meeting. A shareholder who intends to attend the class meeting shall deliver his written reply concerning attendance at the class meeting to the Company twenty days before the date of the class meeting. If the number of shares carrying voting rights at the meeting represented by the shareholders who intend to attend the class meeting reaches more than one half of the voting shares at the class meeting, the Company may hold the class meeting; if not, the Company shall within five (5) days notify the shareholders again by public notice of the matters to be considered, the date and the place for the class meeting. The Company may then hold the class meeting after such publication of notice.

Pursuant to Article 157 of the Articles of Association, notice of class meetings need only be served on shareholders entitled to vote thereat. Meeting of any class of shareholders shall be conducted in a manner as similar as possible to that of general meetings of shareholders. The provisions of these Articles of Association relating to the manner to

conduct any shareholders' general meeting shall apply to any meeting of a class of shareholders.

## **Meetings of Shareholders**

According to Article 78, shareholders' general meetings are divided into annual general meetings and extraordinary general meetings. Shareholders' general meetings shall be convened by the Board of Directors. Annual general meetings are held once every year and within six months from the end of the preceding financial year.

According to Article 79, under any of the following circumstances, the Board of Directors shall convene an extraordinary general meeting within two months: (1) the number of directors is less than that is required by the Company Law or two thirds of the number of directors specified in these Articles of Association; (2) the accrued losses of the Company amount to one third of the total amount of its share capital; (3) shareholder(s) individually or jointly holding 10% or more of the Company's issued and outstanding shares carrying voting rights request(s) in writing the convening of an extraordinary general meeting; (4) it is deemed necessary by the Board of Directors or requested by the supervisory committee to convene an extraordinary general meeting; (5) more than one half of the independent directors propose to convene the meeting.

According to Article 91 of the Articles of Association, notice of a shareholders' general meeting shall be given by way of announcement or by any other manner as provided in these Articles of Association (if necessary), not less than forty-five days (including forty-five days) before the date of the meeting to notify all of the shareholders in the share register of the matters to be considered, the date and the place of the meeting.

According to Article 92 of the Articles of Association, the Company shall, based on the written replies received twenty days before the date of the shareholders' general meeting from the shareholders, calculate the number of voting shares represented by the shareholders who intend to attend the meeting. If the number of voting shares represented by the shareholders who intend to attend the meeting reaches one half or more of the Company's total voting shares, the Company may hold the meeting; if not, then the Company shall within five days notify the shareholders again by public notice of the matters to be considered, the place and date for, the meeting. The Company may then hold the meeting after such publication of notice.

### **Limitation on Right to Own Securities**

The Articles of Association does not specifically provide for the limitations on the rights to own securities by certain shareholders, however, the PRC Special Regulations on Overseas Offering and the Listing of Shares by Companies Limited by Share (the “Special Regulations”) and the Mandatory Provisions for Articles of Association of Companies to be Listed Overseas (the “Mandatory Provisions”) provide for different classes of shares to be subscribed for and traded by local and overseas investors respectively. Shares which can be traded by overseas investors must be in registered form and while denominated in Renminbi, they are traded in foreign currency with dividends payable in foreign currency. Local investors are prohibited from dealing in such shares.

### **Merger, Acquisition or Corporate Restructuring**

Pursuant to Article 291 of the Articles of Association, in the event of the merger or division of the Company, a plan shall be presented by the Company’s Board of Directors and shall be approved in shareholders’ general meeting and the relevant examining and approving formalities shall be processed as required by law. A shareholder who objects to the plan of merger or division shall have the right to demand the Company or the shareholders who consent to the plan of merger or division to acquire that dissenting shareholder’s shareholding at a fair price. The contents of the resolution of merger or division of the Company shall be made into special documents for shareholders’ inspection. Such special documents shall be sent by mail to holders of Overseas-Listed Foreign-Invested Shares.

### **Ownership to Be Disclosed**

The Articles of Association do not contain any provisions governing the ownership threshold above which shareholder ownership must be disclosed.

#### **C. Material Contracts.**

Other than such contracts as are described in our disclosure in Item 4 “Information on the Company” and Item 7 “Related Party Transactions”, we have not entered into any material contracts outside the ordinary course of our business within the two years preceding the date of this annual report.

#### **D. Exchange Controls.**

Under current Chinese foreign exchange regulations, Renminbi is fully convertible for current account transactions, but is not freely convertible for capital account transactions. Current account foreign currency transactions can be undertaken without prior approval from the relevant Chinese government agencies by producing commercial documents evidencing such transactions, provided that they are processed through Chinese banks licensed to engage in foreign currency transactions. Conversion from Renminbi into a foreign currency or vice versa for purposes of capital account transactions requires prior approvals of relevant Chinese government agencies. This restriction on capital account transactions could affect the ability of the Company to acquire foreign currency for capital expenditures.

The Company is generally required by law to sell all its foreign currency revenues to Chinese banks. The Company may purchase foreign currency directly from Chinese banks for any current account transactions, such as trade transactions in its usual and normal course of business, including acquisition of aircraft, jet fuel and flight equipment (such acquisition requires approvals from the relevant Chinese government agencies). Payment of dividends by the Company to holders of the Company's H Shares and ADRs is also considered a current account transaction under Chinese law. Therefore, there is no legal restriction on the conversion of Renminbi into foreign currency for the purpose of paying dividends to such holders of H Shares and ADRs. In addition, the Company's Articles of Association require the Company to pay dividends to holders of the Company's H Shares and ADRs in foreign currency.

On July 21, 2005, the PRC government changed its policy of pegging the value of the Renminbi to the U.S. dollar so that the Renminbi is now permitted to fluctuate within a band against a basket of certain foreign currencies. On May 18, 2007, the People's Bank of China announced that the floating band of Renminbi trading prices against U.S. dollar in the inter-bank spot foreign exchange market would be permitted to rise or fall by as much as 0.5%. The floating band was subsequently expanded to 1% by the People's Bank of China, effective from April 16, 2012.



The PRC government has stated publicly that it intends to further liberalize its currency policy, which could result in a further and more significant change in the value of the Renminbi against the U.S. dollar. Any significant revaluation of the Renminbi may have a material adverse effect on the Company's financial performance, and the value of, and any dividends payable on, the Company's H Shares and ADRs in foreign currency terms.

### **Other Limitations**

There are no limitations on the right of non-resident or foreign owners to hold or vote H Shares or ADRs imposed by Chinese law or by the Articles of Association or other constituent documents of the Company. However, under current Chinese law, foreign ownership of the Company may not exceed 49%.

### **E. Taxation.**

#### **Chinese Taxation**

The following is a general summary of certain Chinese tax consequences of the acquisition, ownership and disposition of A Shares, H Shares and ADRs. This summary is based upon tax laws of China as in effect on the date of this Annual Report, including the income tax treaty between the United States and China (the "U.S.-PRC Tax Treaty"), all of which are subject to change or different interpretation.

In general, for Chinese tax purposes, holders of ADRs will be treated as the owners of the H Shares represented by those ADRs, and exchanges of H Shares for ADRs, and ADRs for H Shares, will not be subject to taxation under the laws of China.

This summary does not purport to address all material tax consequences for holders or prospective purchasers of A Shares, H Shares or ADRs, and does not take into account the specific circumstances of such investors. Investors should consult their own tax advisors as to Chinese or other tax consequences of the acquisition, ownership and disposition of A shares, H Shares or ADRs.

As a result of the new corporate income tax law, the statutory corporate income tax rate adopted by the Company and its subsidiaries has been changed from 33% to 25% with effect from January 1, 2008. Pursuant to new corporate income tax law, the corporate income tax rates of entities that previously enjoyed preferential tax rates of 15% have been revised to 18%, 20%, 22%, 24% and 25% for 2008, 2009, 2010, 2011 and 2012 onwards, respectively.

## **Dividends**

The new corporate income tax law and its relevant regulations generally provide for the imposition of a withholding tax on dividends paid by a Chinese company to a non-resident enterprise at a rate of 10%.

China currently has double-taxation treaties with a number of countries, such as Australia, Canada, France, Germany, Japan, Malaysia, the Netherlands, Singapore, the United Kingdom and the United States. Under the U.S.-PRC Tax Treaty, China may tax a dividend paid by the Company to a U.S. holder up to a maximum of 10% of the gross amount of such dividend.

For individuals, Chinese tax law generally provides that an individual who receives dividends from Chinese companies is subject to a 20% individual income tax. A 50% reduction of taxable income is granted by Chinese tax law for an individual receiving dividends from a listed company on Shanghai Stock Exchange or Shenzhen Stock Exchange. As a result, the effective tax rate for dividends received by A share individual holder is 10% in 2012. Dividend income received by any foreign individual that holds overseas shares in Chinese enterprise is generally subject to individual income tax at a flat rate of 20%, subject to exemption or reduction by an applicable double-taxation treaty.

## **Capital Gains from Transfer or Disposition of Shares**

The new corporate income tax law and its relevant regulations generally provides that a non-resident enterprise is subject to a 10% capital gains tax for the transfer or disposition of shares of a Chinese company.

For individual shareholders, Chinese tax law generally provide that an individual who transfers or otherwise disposes of a company's shares of capital stock is subject to a 20% individual income tax on the capital gain, if any. Currently, all individuals are temporarily exempt from individual income tax on transfers of shares of joint stock companies listed on Shanghai Stock Exchange or Shenzhen Stock Exchange, such as the Company. Should such temporary exemption be discontinued, such holders may be subject to a 20% individual income tax on the capital gain, if any, unless reduced by an applicable double-taxation treaty.

## United States Federal Income Taxation

This discussion describes general U.S. federal income tax consequences of the purchase, ownership and disposition of the Company's ADRs. This discussion does not address any aspect of U.S. federal gift or estate tax, or the state, local or foreign tax consequences of an investment in the Company's ADRs. This discussion applies to you only if you hold and beneficially own the Company's ADRs as capital assets for tax purposes. This discussion does not apply to you if you are a member of a class of holders subject to special rules, such as:

- dealers in securities or currencies;
- traders in securities that elect to use a mark-to-market method of accounting for securities holdings;
- banks or other financial institutions;
- insurance companies;
- tax-exempt organizations, retirement plans, individual retirement accounts or tax deferred accounts;
- partnerships or other pass-through entities (including entities treated as partnerships for U.S. federal income tax purposes) or persons holding ADRs through any such entities;
- persons that hold ADRs as part of a hedge, straddle, constructive sale, conversion transaction or other integrated investment;
- persons whose functional currency for tax purposes is not the U.S. dollar;
- persons who are U.S. expatriates;
- persons liable for alternative minimum tax; or
- persons who directly, indirectly or constructively own 10% or more of the total combined voting power of all classes of the Company's shares (including ADRs) entitled to vote.

This discussion is based on the U.S. Internal Revenue Code of 1986, as amended, which is referred to in this discussion as the Code, its legislative history, existing and proposed regulations promulgated thereunder, published rulings and court decisions, all as currently in effect. These laws are subject to change, possibly on a retroactive basis. In addition, this discussion relies on the assumptions regarding the value of the Company's shares and the nature of its business over time. Finally, this discussion is based in part upon the representations of the depositary and the assumption that each obligation in the deposit agreement and any related agreement will be performed in accordance with its terms. For U.S. federal income tax purposes, as a holder of ADRs, you are treated as the owner of the underlying ordinary shares represented by such ADRs.

***The discussions and comments included herein are only a general description of the tax aspects and they do not constitute a tax advice or opinion. Therefore, you should consult your own tax advisor concerning the particular U.S. federal income tax consequences to you of the purchase, ownership and disposition of the Company's ADRs, as well as the consequences to you arising under the laws of any other taxing jurisdiction.***

For purposes of the U.S. federal income tax discussion below, you are a "U.S. Holder" if you beneficially own ADRs and are:

a citizen or resident of the United States for U.S. federal income tax purposes;

a corporation, or other entity taxable as a corporation, that was created or organized in or under the laws of the United States or any political subdivision thereof;

an estate the income of which is subject to U.S. federal income tax regardless of its source; or

a trust if (a) a court within the United States is able to exercise primary supervision over its administration and one or more U.S. persons have the authority to control all substantial decisions of the trust, or (b) the trust has a valid election in effect to be treated as a U.S. person.

If you are not a U.S. person, please refer to the discussion below under “Non-U.S. Holders.”

## **U.S. Holders**

### ***Dividends on ADRs***

Subject to the Passive Foreign Investment Company (“PFIC”) discussion below, if the Company makes distributions and you are a U.S. Holder, the gross amount of any distributions you receive on your ADRs will generally be treated as dividend income if the distributions are made from the Company’s current or accumulated earnings and profits, calculated according to U.S. federal income tax principles. Dividends will generally be subject to U.S. federal income tax as ordinary income on the day you actually or constructively receive such income. However, if you are an individual and have held your ADRs for a sufficient period of time, dividend distributions on the Company’s ADRs will generally constitute qualified dividend income taxed at a preferential rate as long as the Company is not treated as a PFIC, the Company’s ADRs continue to be readily tradable on the New York Stock Exchange and certain other conditions apply. You should consult your own tax adviser as to the rate of tax that will apply to you with respect to dividend distributions, if any, you receive from us.

Distributions in excess of current and accumulated earnings and profits, as determined for U.S. federal income tax purposes, will be treated as a non-taxable return of capital to the extent of your adjusted tax basis in the ADRs and thereafter as capital gain. However, the Company does not intend to maintain calculations of its earnings and profits in accordance with U.S. federal income tax principles, so each U.S. Holder should therefore assume that any distribution by the Company with respect to the ADRs will constitute ordinary dividend income. Even if you are a corporation, you will not be entitled to claim a dividends-received deduction with respect to distributions you receive from the

Company. Dividends generally will constitute foreign source passive income for U.S. foreign tax credit limitation purposes. You should consult your own tax advisor to determine the foreign tax credit implications of owning ADRs.

***Sales and other dispositions of ADRs***

Subject to the PFIC discussion below, when you sell or otherwise dispose of the Company's ADRs, you will generally recognize capital gain or loss in an amount equal to the difference between the amount realized on the sale or other disposition and your adjusted tax basis in the ADRs, both as determined in U.S. dollars. Your adjusted tax basis will generally equal the amount you paid for the ADRs. Any gain or loss you recognize is long-term capital gain or loss if your holding period in the Company's ADRs is more than one year at the time of disposition. If you are an individual, any such long-term capital gain is eligible for preferential rates. Your ability to deduct capital losses is subject to various limitations.

***Passive Foreign Investment Company***

If the Company is currently or were to become a PFIC, as a U.S. Holder, you would generally be subject to adverse U.S. tax consequences, in the form of increased tax liabilities and special U.S. tax reporting requirements.

The Company will be classified as a PFIC in any taxable year if either: (1) the average value during the taxable year of its assets that produce passive income, or are held for the production of passive income, is at least 50% of the average value of its total assets for such taxable year (the “Asset Test”); or (2) 75% or more of its gross income for the taxable year is passive income (such as certain dividends, interest or royalties)(the “Income Test”). For purposes of the Asset Test: (1) any cash, cash equivalents, and cash invested in short-term, interest bearing, debt instruments, or bank deposits that is readily convertible into cash, will generally count as producing passive income or as being held for the production of passive income; and (2) the average values of the Company’s passive and total assets is calculated based on its market capitalization. In the case of publicly traded corporations, fair market value must be used for purposes of applying the Asset Test. In addition, regarding the above two tests, there are complex look-through rules to consider with respect to the assets and activities of related corporations from which the Company either receives income or in which it holds an interest. More specifically, certain adjustments are made to exclude certain income received from a related party or to include income earned and assets held by a 25% or more owned subsidiary in determining whether the Company qualifies as a PFIC under the two tests. In particular: 1) passive income received from a related party is excluded if it is properly allocable to the non-passive income of the related party, and 2) if the Company owns directly or indirectly 25% or more of the stock of another corporation, the Company is treated as if it owned directly a proportionate share of that corporation’s assets and income.

The Company believes that it was not a PFIC for the taxable year 2013. However, there can be no assurance that the Company will not be a PFIC for the taxable year 2014 and/or later taxable years, as PFIC status is re-tested each year and depends on the facts in such year. For example, the Company would be a PFIC for the taxable year 2013 if the sum of its average market capitalization, which is its share price multiplied by the total amount of its outstanding shares, and its liabilities over that taxable year is not more than twice the value of its cash, cash equivalents, and other assets that are readily converted into cash.

If the Company were a PFIC, you would generally be subject to additional taxes and interest charges on certain “excess distributions” the Company makes regardless of whether the Company continues to be a PFIC in the year in which you receive an “excess distribution”. An “excess distribution” would be either (1) the excess amount of a distribution with respect to ADRs during a taxable year in which distributions to you exceed 125% of the average annual distributions to you over the preceding three taxable years or, if shorter, your holding period for the ADRs, or (2) 100% of the gain from the disposition of ADRs.

To compute the tax on “excess” distributions or any gain, (1) the “excess distribution” would be allocated ratably to each day in your holding period, (2) the amounts allocated to the current year and to any tax year before the first day on which the Company became a PFIC would be taxed as ordinary income in the current year, (3) the amount allocated to other taxable years would be taxable at the highest applicable marginal rate in effect for that year, and (4) an interest charge at the rate for underpayment of U.S. federal income tax for any period described under (3) above would be imposed with respect to any portion of the “excess” distribution that is allocated to such period. In addition, if the Company were a PFIC, no distribution that you receive from the Company would qualify for taxation at the preferential rate discussed in the “Dividends on ADRs” section above.

If the Company were a PFIC in any year, as a U.S. Holder, you would be required to make an annual return on IRS Form 8621 “Information Return by a Shareholder of a Passive Foreign Investment Company or a Qualified Electing Fund.” However, the Company does not intend to generate, or share with you, information that you might need to properly complete IRS Form 8621. You should consult with your own tax adviser regarding reporting requirements with regard to your ADRs.

If the Company were a PFIC in any year, you would generally be able to avoid the “excess” distribution rules described above by making a timely so-called “mark-to-market” election with respect to your ADRs provided the Company’s ADRs are “marketable”. The Company’s ADRs will be “marketable” as long as they remain regularly traded on a national securities exchange, such as the New York Stock Exchange. If you made this election in a timely fashion, you would generally recognize as ordinary income or ordinary loss the difference between the fair market value of your ADRs on the first day of any taxable year and their value on the last day of that taxable year. Any ordinary income resulting from this election would generally be taxed at ordinary income rates and would not be eligible for the reduced rate of tax applicable to qualified dividend income. Any ordinary losses would be limited to the extent of the net amount of previously included income as a result of the mark-to-market election, if any. Your basis in the ADRs would be adjusted to reflect any such income or loss. Any gains recognized on the sale or other disposition of the ADRs would be treated as ordinary income and any losses would be treated as ordinary losses (but only to the extent of the net amount of previously included income as a result of the mark-to-market election, if any). You should consult with your own tax adviser regarding potential advantages and disadvantages to you of making a “mark-to-market” election with respect to your ADRs.

Separately, if the Company were a PFIC in any year, you would be able to avoid the “excess” distribution rules by making a timely election to treat us as a so-called “Qualified Electing Fund” or “QEF”. You would then generally be required to include in gross income for any taxable year (1) as ordinary income, your pro rata share of the Company’s ordinary earnings for the taxable year, and (2) as long-term capital gain, your pro rata share of the Company’s net capital gain for the taxable year. However, the Company does not intend to provide you with the information you would need to make or maintain a “QEF” election and you will, therefore, not be able to make or maintain such an election with respect to your ADRs.



### ***Medicare Tax***

Recently enacted legislation requires certain U.S. Holders who are individuals, estates or trusts to pay up to an additional 3.8% tax on, among other things, dividends and capital gains for tax years beginning after December 12, 2012.

### **Non-U.S. Holders**

If you beneficially own ADRs and are not a U.S. Holder for U.S. federal income tax purposes (a “Non-U.S. Holder”), you generally will not be subject to U.S. federal income tax or U.S. withholding tax on dividends received from the Company with respect to ADRs unless that income is considered effectively connected with your conduct of a U.S. trade or business and, if an applicable income tax treaty so requires as a condition for you to be subject to U.S. federal income tax with respect to income from your ADRs, such dividends are attributable to a permanent establishment that you maintain in the United States.

You generally will not be subject to U.S. federal income tax, including withholding tax, on any gain realized upon the sale or exchange of ADRs, unless:

that gain is effectively connected with the conduct of a U.S. trade or business and, if an applicable income tax treaty so requires as a condition for you to be subject to U.S. federal income tax with respect to income from your ADRs, such gain is attributable to a permanent establishment that you maintain in the United States; or

you are a non-resident alien individual and are present in the United States for at least 183 days in the taxable year of the sale or other disposition and certain other conditions are met.

If you are engaged in a U.S. trade or business, unless an applicable tax treaty provides otherwise, the income from your ADRs, including dividends and the gain from the disposition of the Company’s ADRs, that is effectively connected with the conduct of that trade or business will generally be subject to the rules applicable to U.S. Holders discussed above. In addition, if you are a corporation, you may be subject to an additional branch profits tax at a rate of 30% or any lower rate under an applicable tax treaty.

### **U.S. information reporting and backup withholding rules**

In general, dividend payments with respect to the ADRs and the proceeds received on the sale or other disposition of those ADRs may be subject to information reporting to the IRS and to backup withholding (currently imposed at a rate of 28%). Backup withholding will not apply, however, if you (1) are a corporation or come within certain other exempt categories and, when required, can demonstrate that fact or (2) provide a taxpayer identification number, certify as to no loss of exemption from backup withholding and otherwise comply with the applicable backup withholding rules. To establish your status as an exempt person, you will generally be required to provide certification on IRS Form W-9, W-8BEN or W-8ECI, or an appropriate substitute, as applicable. Any amounts withheld from payments to you under the backup withholding rules will be allowed as a refund or a credit against your U.S. federal income tax liability, provided that you furnish the required information to the IRS.

HOLDERS OF THE COMPANY'S ADRS SHOULD CONSULT WITH THEIR OWN TAX ADVISORS REGARDING THE APPLICATION OF THE U.S. FEDERAL INCOME TAX LAWS TO THEIR PARTICULAR SITUATIONS AS WELL AS ANY TAX CONSEQUENCES RESULTING FROM PURCHASING, HOLDING OR DISPOSING OF THE ADRS, INCLUDING THE APPLICABILITY AND EFFECT OF THE TAX LAWS OF ANY STATE, LOCAL OR FOREIGN JURISDICTION AND INCLUDING ESTATE, GIFT, AND INHERITANCE LAWS.

F.Dividends and Paying Agents.

Not applicable.

G.Statement by Experts.

Not applicable.

H.Documents on Display.

The Company has filed this Annual Report on Form 20-F with the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended. Statements made in this Annual Report as to the contents of any document referred to are not necessarily complete. With respect to each such document filed as an exhibit to this Annual Report, reference is made to the exhibit for a more complete description of the matter involved, and each such statement shall be deemed qualified in its entirety by such reference.

The Company is subject to the informational requirements of the Exchange Act and file reports and other information with the Securities and Exchange Commission. Reports and other information which the Company filed with the Securities and Exchange Commission, including this Annual Report on Form 20-F, may be inspected and copied at the public reference room of the Securities and Exchange Commission at 450 Fifth Street N.W. Washington D.C. 20549.

You can also obtain copies of this Annual Report on Form 20-F by mail from the Public Reference Section of the Securities and Exchange Commission, 450 Fifth Street, N.W., Washington D.C. 20549, at prescribed rates. Additionally, copies of this material may be obtained from the Securities and Exchange Commission's Internet site at <http://www.sec.gov>. The Commission's telephone number is 1-800-SEC-0330. Copies of this material may also be obtained for the Company's website at [http:// www.csair.com](http://www.csair.com).

#### I. Subsidiary Information.

Not applicable.

### ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

#### **Fuel Price Fluctuation Risk**

The Group's earnings are affected by changes in the price and availability of jet fuel. There are currently no effective means available to manage the Group's exposure to the fluctuations in jet fuel prices. The Group's results of operations may be significantly affected by fluctuations in fuel prices which is a significant expense for the Group. A reasonable possible increase or decrease of 10% in jet fuel price, with volume of fuel consumed and all other variables held constant, would have increased/decreased the fuel costs by approximately RMB3,554 million. The sensitivity analysis of jet fuel price risk is disclosed in Note 4(e) to the consolidated Financial Statements.

**Interest Rate Risk**

The Group is subject to market risks due to fluctuations in interest rates. The majority of the Group's borrowing is in the form of long-term fixed-rate and variable-rate debts with original maturities ranging from three to twelve years. Fluctuations in interest rates can lead to significant fluctuations in the fair value of such debt instruments. From time to time, the Group may enter into interest rate swaps designed to mitigate exposure relating to interest rate risks. The sensitivity analysis of interest rate risk is disclosed in Note 4(b) to the consolidated Financial Statements.

The following table provides information regarding the Group's financial instruments that are sensitive to changes in interest rate as of December 31, 2013 and 2012:

	As of December 31, 2013							As of December 31, 2012		
	Expected Maturity Date									
	2014	2015	2016	2017	2018	Thereafter	Total Recorded Amount	Fair Value (2)	Total Recorded Amount	Fair Value (2)
Fixed-rate bank and other loans in US\$	332	99	99	14	-	-	544	555	1,114	1,124
Average interest rate	2.34 %	3.13 %	3.13 %	3.23 %						
Variable-rate bank and other loans in US\$	19,837	10,470	11,962	3,485	3,419	7,101	56,274	56,274	50,174	50,174
Average interest rate	2.16 %	2.25 %	2.39 %	1.76 %	1.76 %	2.09 %				
Fixed-rate bank and other loans in RMB	-	-	-	-	-	-	-	-	60	60
Average interest rate	-									
Variable-rate bank and other loans in RMB	73	141	456	-	-	-	670	670	744	744
Average interest rate	5.76 %	5.93 %	5.54 %							

(1) These interest rates are calculated based on the year end indices.

(2) Fair value of debt instruments was estimated based on the interest rates applicable to similar debt instruments as of December 31, 2013 and 2012.

## Foreign Currency Exchange Risk

The Group is also exposed to foreign currency risk as a result of its aircraft and flight equipment being sourced from overseas suppliers. Specifically, the Group's foreign currency exposure relates primarily to its foreign currency long-term bank and other loans used to finance such capital expenditures and its capital commitments. Subject to certain restrictive conditions imposed by the SAFE, the Group may, from time to time, enter into foreign exchange forward option contracts to mitigate its foreign currency exposures. The sensitivity analysis of foreign currency risk is disclosed in Note 4(c) to the consolidated Financial Statements.

As of December 31, 2013, the Group operated a total of 319 aircraft under operating leases and capital leases at rates that are substantially fixed. Such leases expose the Group to market risks. However, in accordance with Item 305 of Regulation S-K, such leases have been excluded from the following market risk tables. Commitments under capital leases and operating leases are disclosed in Note 36 and Note 46(b) to the consolidated Financial Statements, respectively.

The following table provides information regarding the Group's material foreign currency sensitive financial instruments and capital commitments as of December 31, 2013 and 2012:

	As of December 31, 2013						As of December 31, 2012			
	Expected Maturity Date									
	2014	2015	2016	2017	2018	Thereafter	Total Recorded Amount	Fair Value (1)	Total Recorded Amount	Fair Value (1)
Fixed-rate bank and other loans in US\$	332	99	99	14	-	-	544	555	1,114	1,124
Variable-rate bank and other loans in US\$	19,837	10,470	11,962	3,485	3,419	7,101	56,274	56,274	50,174	50,174
Capital commitment in US\$	20,945	14,417	6,365	5,924	-	-	47,651	47,651	71,309	71,309

(1) Fair value of debt instruments was estimated based on the floating interest rates applicable to similar debt instruments as of December 31, 2013 and 2012.

ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES.

A. Debt Securities.

Not applicable.

B. Warrants and Rights.

Not applicable.

C. Other Securities.

Not applicable.

D. American Depositary Shares.

The Bank of New York Mellon collects its fees for delivery and surrender of ADSs directly from investors depositing shares or surrendering ADSs for the purpose of withdrawal or from intermediaries acting for them. The Bank of New York Mellon collects fees for making distributions to investors by deducting those fees from the amounts distributed or by selling a portion of distributable property to pay the fees. The Bank of New York Mellon may collect its annual fee for depositary services by deductions from cash distributions or by directly billing investors or by charging the book-entry system accounts of participants acting for them. The Bank of New York Mellon may generally refuse to provide fee-attracting services until its fees for those services are paid.

**Persons depositing or withdrawing shares must pay:**

\$5.00 (or less) per 100 ADSs (or portion of 100 ADSs)

\$.02 (or less) per ADS

A fee equivalent to the fee that would be payable if securities distributed to you had been shares and the shares had been deposited for issuance of ADSs

\$.02 (or less) per ADSs per calendar year

Registration or transfer fees

Expenses of the depositary

Taxes and other governmental charges the depositary or the custodian have to pay on any ADS or share underlying an ADS, for example, stock transfer taxes, stamp duty or withholding taxes

Any charges incurred by the depositary or its agents for servicing the deposited securities

**For:**

- Issuance of ADSs, including issuances resulting from a distribution of shares or rights or other property
- Cancellation of ADSs for the purpose of withdrawal, including if the deposit agreement terminates
- Any cash distribution to ADS registered holders
- Distribution of securities distributed to holders of deposited securities which are distributed by the depositary to ADS registered holders
- Depositary services
- Transfer and registration of shares on our share register to or from the name of the depositary or its agent when you deposit or withdraw shares
- Cable, telex and facsimile transmissions (when expressly provided in the deposit agreement)
- Converting foreign currency to U.S. dollars
- As necessary
- As necessary

**Fees and Payments from the Depositary to Us**

In 2013, the Company received from the depositary a reimbursement of US\$60,029.75, net of withholding tax, for continuing annual stock exchange listing fees and expenses incurred by the Company in connection with the administration and maintenance of the depositary receipt facility.

**Indirect payments**



As part of its service to the Company, the Bank of New York Mellon waived a total amount of US\$130,852.31 for the standard costs associated with the administration of the ADS program in 2013.

## **PART II**

### **ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES.**

None.

### **ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS.**

#### **A. Material Modifications to the Instruments Defining the Rights of Security Holders.**

None.

#### **B. Material Modifications to the Rights of Registered Securities by Issuing or Modifying any other Class of Securities.**

None.

#### **C. Withdrawal or Substitution of a Material Amount of the Assets Securing any Registered Securities.**

Not applicable.

#### **D. Change of Trustees or Paying Agents for any Registered Securities.**

Not applicable.

E. Use of Proceeds.

Not applicable.

## ITEM 15. CONTROLS AND PROCEDURES.

### **Disclosure controls and procedures**

Our President and Chief Financial Officer have evaluated the effectiveness of our disclosure controls and procedures (as defined in the Exchange Act Rules 13a-15(e) or 15d-15(e)), and concluded that, based on their evaluation, our disclosure controls and procedures are effective as of the end of the period covered by this Annual Report to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms, and were also effective to ensure that information required to be disclosed in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our President and Chief Financial Officer, to allow timely decisions regarding required disclosure.

### **Management's annual report on internal control over financial reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of a company's assets, (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of consolidated financial statements in accordance with generally accepted accounting principles, and that a company's receipts and expenditures are being made only in accordance with authorizations of a company's management and directors, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of a company's assets that could have a material effect on the consolidated financial statements. Our management has assessed the effectiveness of internal control over financial reporting based on the Internal Control - Integrated Framework (1992) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Our management has concluded that our internal control over financial reporting was effective as of December 31, 2013.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with policies or procedures may deteriorate.

PricewaterhouseCoopers Zhong Tian LLP, an independent registered public accounting firm, has audited the consolidated financial statements included in this Annual Report, and, as part of the audit, has issued a report, included herein, on the effectiveness of our internal control over financial reporting.

#### **Attestation Report of the Registered Public Accounting Firm**

PricewaterhouseCoopers Zhong Tian LLP, our independent registered public accounting firm, audited the effectiveness of our company's internal control over financial reporting as of December 31, 2013, the audit report of which appears on page F-1 of this Form 20-F.

#### **Changes in internal control over financial reporting**

During the year ended December 31, 2013, there have been no changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

#### **ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT.**

The Board of Directors has determined that Mr. Tan Jing Song qualifies as an audit committee financial expert in accordance with the terms of Item 16A of Form 20-F. Mr. Tan Jing Song satisfies as an “independent director” within the meaning of NYSE Manual Section 303A and meets the criteria for independence set forth in Section 10A(m)(3) of the U.S. Securities Exchange Act of 1934, as amended, or the Exchange Act, and Rule 10A-3 under the Exchange Act. See “Item 6 Directors, Senior Management and Employees — Directors and Senior Management”.

**ITEM 16B. CODE OF ETHICS.**

We have adopted a code of ethics that applies to our principal executive officer, principal financial officer and principal accounting officer. Such code is included in the director service agreements, a form of which is incorporated by reference in this Annual Report in Exhibit 4.1. Each of the aforementioned senior corporate officers currently serves as a Director and all of our Directors are subject to the director service contracts with the Company. Pursuant to the director service agreements, among other things, Directors (i) owe fiduciary duties to the Company and shall perform their duties in compliance with applicable governmental laws, rules and regulations; (ii) shall not engage in any activities in competition with the Company's business or carry out any activities detrimental to the interests of the Company; and (iii) shall be held liable for any loss or injury incurred to the Company as a result of such Director's violation of applicable laws and regulations.

**ITEM 16C. PRINCIPAL ACCOUNTING FEES AND SERVICES.**

The following table sets forth the aggregate audit fees, audit-related fees and tax fees of our principal accountants and all other fees billed for products and services provided by our principal accountants other than the audit fees, audit-related fees and tax fees for each of the fiscal years 2012 and 2013:

	Audit Fees	Audit-Related Fees	Tax Fees	Other Fees
	RMB (in million)			
2012	13.2	-	0.5	0.7
2013	12.0	-	0.8	3.7

**Tax Fees**

Services provided primarily consist of tax compliance services.

**Other Fees**

Provision of other assurance and advisory services.

Before our principal accountants were engaged by the Company or our subsidiaries to render the audit or non-audit services, the engagements were approved by our Audit Committee.

ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEE

Not applicable.

ITEM 16E. PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS.

None.

ITEM 16F. CHANGES IN REGISTRANT'S CERTIFYING ACCOUNTANT.

On March 26, 2013, the board of the directors of the Company resolved, as recommended by our audit committee, to propose to change our principal accountants, KPMG, after the completion of their audit of our consolidated financial statements as of and for the year ended December 31, 2012 and the effectiveness of internal control over financial reporting as of December 31, 2012 and to appoint PricewaterhouseCoopers Zhong Tian CPAs Limited (to be renamed as PricewaterhouseCoopers Zhong Tian LLP), or PwC as our new principal accountants effective upon the approval by the shareholders of the Company at the forthcoming annual general meeting. Such change in our principal accountants is due to the relevant requirements issued by the State-Owned Assets Supervision and Administration Commission of the PRC. According to the relevant requirements, if the service term of the external auditor appointed by the state-owned enterprises to continuously undertake financial auditing work exceeds the prescribed time limit, such auditor needs to be changed. In this connection, the Company, a listed company controlled by a state-owned enterprise, did not reappoint KPMG as our principal accountants at the forthcoming annual general meeting.

The audit reports of KPMG on our consolidated financial statements as of and for the fiscal years ended December 31, 2011 and 2012 contain no adverse opinion or disclaimer of opinion, and were not qualified or modified as to uncertainty, audit scope, or accounting principles.

During the two fiscal years ended December 31, 2011 and 2012 and through April 26, 2013, there were no disagreements with KPMG on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure, which disagreements if not resolved to the satisfaction of KPMG, would have caused them to make reference to the subject matter of the disagreements in connection with their report, nor were there any reportable events (as defined in Item 16F(a)(1)(v) of Form 20-F). We have provided a copy of the foregoing disclosure to KPMG and requested that KPMG furnish a letter addressed to the SEC s