中國國際航空股份有限公司
AIR CHINA LIMITED
(a joint stock limited company incorporated in the People's Republic of China with limited liability)
(Stock Code: 00753)

CONTINUING CONNECTED TRANSACTIONS AND DISCLOSEABLE TRANSACTION

I. INTRODUCTION

Reference is made to the announcement of the Company dated 30 August 2016 in relation to the ACC Transactions and the CNACG Transactions. The current term of the ACC Framework Agreement and the CNACG Framework Agreement will expire on 31 December 2019. As the Company expects that the ACC Transactions and the CNACG Transactions will continue to be conducted after 31 December 2019, on 30 October 2019 (after trading hours), the Company entered into the New ACC Framework Agreement and the New CNACG Framework Agreement with Air China Cargo and CNACG respectively to renew and amend the ACC Framework Agreement and the CNACG Framework Agreement.

II. ACC TRANSACTIONS

The New ACC Framework Agreement was entered into between the Company and Air China Cargo on 30 October 2019.

Parties and the relationship between the parties

The Company is principally engaged in providing air passenger and cargo transportation services and other aviation-related services.

Air China Cargo is a 51%-owned subsidiary of CNAHC, a controlling shareholder of the Company, and is therefore a connected person of the Company under the Hong Kong Listing Rules. Air China Cargo is a limited liability company established under the laws of the PRC and is principally engaged in air cargo and mail transportation business.

Description of the ACC Transactions

The ACC Transactions contemplated under the New ACC Framework Agreement are as follows:

- **Bellyhold Space Business contracting operation:** The Company has contracted the operation of all Bellyhold Space Business to Air China Cargo. Air China Cargo shall undertake the overall responsibilities for transporting the cargos as the contracting carrier to the consignors with respect to the cargos which are transported through the bellyhold spaces of passenger aircraft.

- **Ground support services and other services:** The ground support services and other services provided by the Group to ACC Group include but are not limited to operation support services, IT sharing services, comprehensive support services, engine and other aircraft-related materials lease services and labour management services. The ground support services and other services provided by ACC Group to the Group include but are not limited to terminal cargo and mail services, airport apron services, container and pallet management services, engine and other aircraft-related materials lease services.

Pricing Policies for the ACC Transactions

The consideration of any specific ACC Transactions shall be determined after arm's length negotiations between the Group and the ACC Group and on normal commercial terms, and shall be determined in accordance with the pricing policies set forth below on a case-by-case basis.

- **Bellyhold Space Business contracting operation:**

    (1) **Contracting Operation Income**: During the contracting period, Air China Cargo will regularly pay the Company the contracting operation income in respect of Bellyhold Space Business in each year. The parties shall determine the Benchmark Income (excluding tax) of Bellyhold Space Business contracting operation after arm's length negotiations with reference to the Company's fleet capacity, overall load factor and yield level. The specific formula is as follows:

    Benchmark Income (excluding tax) = ATK (available tonne kilometres) × OLF (overall load factor) × yield level per kilometre

    The ATK shall be determined based on the Company's fleet capacity for the current financial year and its plan of introduction and phase-out of passenger aircraft for the next year. The OLF and the yield level per kilometre shall be determined based on the historical data of the respective air routes of the Company.

Considering possible market fluctuations, the parties agreed to jointly appoint a qualified accounting firm to conduct a special audit on the actual income (excluding tax) of Air China Cargo for the operation of Bellyhold Space Business of the previous financial year within three months after the end of each financial year. Where there is any difference between the Benchmark Income (excluding tax) and the actual income (excluding tax), the excess income or risk incurred shall be allocated between Air China Cargo and the Company at the proportion of 51% and 49%, respectively, and paid accordingly.

Where the final settlement price will exceed the annual caps which have been set by the Company, all reasonable steps will be taken by the Company to comply with the relevant requirements under Chapter 14A of the Hong Kong Listing Rules.

(2) **The Operation Expense of the Bellyhold Space Business:** During the contracting period, the Company shall pay the operation expenses of the Bellyhold Space Business to Air China Cargo on a regular basis per year. In accordance with the common industry practice, the operation expense shall be determined according to the settlement price (determined according to the method as set out above in the paragraph headed "Contracting Operation Income") and the Expense Rate, and the calculation formula is as follows:

Operation Expense = Settlement Price × Expense Rate (as defined below)

The expense rate ("Expense rate") shall be determined by the parties through arm's length negotiation with reference to historical expense rates and other factors such as expense rates of companies in the relevant industry and their variation trends.

Where the Operation Expense will exceed the annual caps which have been set by the Company, all reasonable steps will be taken by the Company to comply with the relevant requirements under Chapter 14A of the Hong Kong Listing Rules.

- **Ground support services and other services:**

  The pricing policies for the ground support services and other services provided to or by the Group are set forth below:

  (1) Follow the government pricing or guide price if it is available, including but not limited to the guidance from the Civil Aviation Administration of the PRC (CAAC) and the International Air Transport Association on the prices of ground support services and other terms, and the requirements on the pricing of navigation information stipulated by CAAC and Air Traffic Management Bureau (ATMB).

  (2) If no government pricing or guide price is available, the final transaction price will be determined on arm's length negotiations between the parties with firstly making reference to the market prices offered by at least two independent third parties on the market for the same type of service, and after taking certain factors into account such as the service standard, service scope, business volume and specific need of parties. If any service need of the service recipient changes, appropriate adjustment will be made to the transaction price after negotiation between both parties based on the extent of variation in relevant costs, service quality or other factors.

  (3) If neither the above cases is applicable, the price will be determined on the basis of cost plus reasonable profit. The costs are mainly based on the costs and expenses of the service provider, including costs of human resources and costs of facility, equipment and materials. Reasonable profit margin will be determined with mainly making reference to the historical average prices on similar products or services (where possible) published in relevant industry, and/or the profit margin of the comparable products and services disclosed by other listed companies. The profit margin of ACC Group shall not exceed 10%. The final transaction prices shall be determined on terms that to the Group are no less favourable to those provided by independent third parties to the Group or those provided by ACC Group to independent third parties (with regards to the receiving of services by the Group), or no more favourable than those provided by the Group to the independent third parties (with regards to the rendering of services by the Group).

The Term of the New ACC Framework Agreement

The initial term of the New ACC Framework Agreement is three years commencing from 1 January 2020 and ending on 31 December 2022, which is automatically renewable for successive terms of three years after the expiry of its initial term subject to the fulfilment of requirements under the Hong Kong Listing Rules/Shanghai Listing Rules and obtaining the required approval. Before expiry of the New ACC Framework Agreement, the Board will re-assess the terms and conditions of the New ACC Framework Agreement, and the Company will re-comply with the relevant rules governing connected transactions under the Hong Kong

Listing Rules/Shanghai Listing Rules. During the term of the New ACC Framework Agreement, the agreement can be terminated on any 31 December by either party thereto by serving the other party a written notice of termination of not less than three months.

Reasons for and Benefits of the ACC Transactions

The Directors believe that it is in the best interest of the Group to continue the ACC Transactions with the ACC Group having taken into account the following factors:

- In respect of the Bellyhold Space Business contracting operation, contracting the bellyhold space operation to Air China Cargo is an important step for the Company to focus on air passenger transportation business, which is also in line with the general trend among major domestic airlines. By virtue of which, the Company will focus its resources on the operation of air passenger transportation business, enhance the utilization efficiency of important resources and enhance the operational and management capacity in core business of air passenger transportation; make the most of economies of scale of the Company and Air China Cargo at their respective business, generate stable bellyhold space contracting revenue to the Company; consolidate mechanism of the operation responsibility and risk sharing, reduce the possible adverse impact brought by the fluctuation of freight market, so as to further promote the brand image and competitiveness of the Company in the air passenger transportation sector, thereby creating more investment return for the shareholders.

- In respect of ground support services and other services, the long established successful cooperative relationship between the Company and Air China Cargo is able to provide streamlined and efficient cooperation and transaction between the Group and the ACC Group.

Historical Amounts and Historical Annual Caps

The table below sets out (i) the annual caps of amounts payable by the ACC Group or the Group for each of the three years ended/ending 31 December 2017, 2018 and 2019, respectively; and (ii) the actual amounts paid by the ACC Group or the Group for each of the two years ended 31 December 2017 and 2018 and for January to August 2019, and the estimated amounts payable for the year ending 31 December 2019.

	Historical Amounts				Historical Annual Caps		
	for the year ended/ ending 31 December		Actual amount for the period from January to August	Expected annual amount for	for the year ended/ ending 31 December		
Transactions	**2017**	**2018**	**2019**	**2019**	**2017**	**2018**	**2019**
				(in millions of RMB)			
Amounts paid/payable by the ACC Group to the Group	**5,636**	**6,043**	**3,653**	**7,045**	**5,854**	**7,160**	**8,777**
In terms of bellyhold space	5,104	5,543	3,190	6,374	5,182	6,429	7,977
In terms of ground support services	62	54	80	120	143	169	200
In terms of other services	470	446	383	551	529	562	600
Amounts paid/payable by the Group to the ACC Group	**993**	**1,017**	**637**	**1,340**	**1,625**	**1,944**	**2,326**
In terms of selling services of bellyhold space	385	418	242	481	519	643	798
In terms of ground support services	576	586	385	826	932	1,088	1,269
In terms of other services	32	13	10	33	174	213	259

Proposed Annual Caps and Basis of Determination

The table below sets out the proposed annual caps of amounts payable by the ACC Group or the Group for each of the three years ending 31 December 2020, 2021 and 2022, respectively:

Transactions	Proposed Annual Caps for the year ending 31 December 2020	2021	2022
	(in millions of RMB)		
Amounts payable by the ACC Group to the Group	**8,800**	**10,600**	**12,700**
In terms of contracting operation income of Bellyhold Space Business	8,000	9,600	11,600
In terms of ground support services and other services	800	1,000	1,100
Amounts payable by the Group to the ACC Group	**1,800**	**2,160**	**2,560**
In terms of operation expenses of bellyhold space	800	960	1,160
In terms of ground support services and other services	1,000	1,200	1,400

Amounts Payable by the ACC Group to the Group

In arriving at the estimated amounts of contracting operation income of Bellyhold Space Business payable by the ACC Group to the Company for each of the three years ending 31 December 2022, the Company has considered, among other things, the historical transaction amounts and the estimation of annual growth rate of the contracting operation income of Bellyhold Space Business for the next three years based on following consideration:

- The bellyhold space provided to the ACC Group will increase along with the expansion of the fleet capacity of passenger aircraft of the Company. As of 31 December 2018, the Company had 409 aircraft. The Company expects to introduce 33, 55, and 36 aircraft and phase out 5, 1, and 0 aircraft in each year of 2019 to 2021, respectively. The average compound annual growth rate of Company's fleet capacity estimated accordingly for the years from 2019 to 2021 is about 10%. It is also assumed that the growth rate of fleet expansion in 2022 will not exceed 10%;

- For the growth rate of yield level per kilometre, considering Air China Cargo's capacity growth from 2020 to 2022 and with reference to the average compound annual growth of yield level per kilometre of the Group of 9.8% for the years from 2016 to 2018, it is assumed that yield level per kilometre will maintained similar growth rate from 2020 to 2022.

In arriving at the estimated aggregate amounts payable by the ACC Group to the Group in connection with the ground support services and other services provided by the Group for each of the three years ending 31 December 2022, respectively, the Company has considered, among other things, the historical transaction amounts and the following factors:

- Increasing need for relevant services: Capacity (AFTK) of Air China Cargo has expanded at a compound growth rate of 5.74% from 2016 to 2018; in view of the capacity growth of bellyhold space of the Company and the fact that Air China Cargo's future business will take its freighters, bellyhold space, cargo terminals (airport apron) and lorry business as core assets, its cross border air transport capacity, cargo terminals operation capacity (airport apron operation capacity) at home and abroad, ground distribution capacity at home and abroad and ability to design and implement F2B/C logistics solution as its fundamental ability, and "e-commerce plus logistics" integrated service provider as its business positioning, and it will strive to building a full business chain that covers whole cross-border market of in the PRC and serves manufacturers to end-user customers, it is expected that the capacity (AFTK) of Air China Cargo will expand at a compound growth rate of approximately 8% from 2020 to 2022, and the need of Air China Cargo for relevant services will increase in line with the expansion of capacity;

- Increase in unit price: It is expected that the unit price of relevant services will increase at an annual rate of approximately 7% from 2020 to 2022 by taking into account the historical increase of the Group's labour costs and equipment costs, as well as the growth rate of inflation; and

- Certain buffer has been included by rounding to the nearest integer to cater for the ACC Group's operating needs from time to time.

Amounts Payable by the Group to the ACC Group

In arriving at the estimated aggregate amounts payable by the Group to the ACC Group in connection with operation expense of Bellyhold Space Business for each of the three years ending 31 December 2022, the Company has made reference to the estimated amounts of contracting operation income of Bellyhold Space Business payable by the ACC Group for each of the three years ending 31 December 2022, as well as the estimation on the expense rates to be adopted on the basis of historical expenses rates in the next three years. For each of the three years ending 31 December 2022, annual caps of contracting operation income for the Bellyhold Space Business payable by the ACC Group to the Company are estimated to be RMB8 billion, RMB9.6 billion and RMB11.6 billion (as stated above). As the expense rate adopted shall not exceed 10%, the annual caps of operation expenses of bellyhold space for each of the three years ending 31 December 2022 are estimated to be RMB0.8 billion, RMB0.96 billion and RMB1.16 billion.

The Company focuses more on operating management improvement under the previous bellyhold space operation model while more on operating result under contracting operation model. Since the Company has disposed the equity shareholdings of Air China Cargo held by it and turned to focus its resources on the operation of air passenger transportation business, contracting operation model is more aligned with the overall development strategies of the Company. For each of the five years ended 31 December 2018, the service charge for passenger aircraft bellyhold space paid by the Company to the ACC Group accounted for 8.08%, 8.97%, 10.59%, 7.54%, and 7.55% of bellyhold revenue. Though the percentages basically remain at the level of 7.55% in the recent years, as the relevant percentage once exceeded 10% in the first three years, the Company adopted 10% as expense rate to estimate annual caps for the coming three years.

In arriving at the estimated aggregate amounts payable by the Group to the ACC Group in connection with the ground support services and other services provided by the ACC Group for each of the three years ending 31 December 2022, respectively, the Company has considered, among other things, the historical transaction amounts and the following factors:

- Increasing need for relevant services: Given that the fleet capacity of the Group is expected to expand at an annual rate of approximately 9% from 2020 to 2022, it is expected that the need of the Group for relevant services will increase in line with the expansion of fleet capacity;

- Increase in unit price: Taking into account the historical increase of the Group's labour costs and equipment costs, as well as the growth rate of inflation, assuming the growth rate of unit prices for services provided by the ACC Group is in line with that of the Group, it is expected that the unit price of relevant services provided by the ACC Group will increase at an annual rate of approximately 7% from 2020 to 2022; and

- Certain buffer has been included by rounding to the nearest integer to cater for the ACC Group's operating needs from time to time.

Internal Control Procedures

The Group has adopted the following internal control procedures to ensure that the ACC Transactions will be conducted on normal commercial terms, and in accordance with the New ACC Framework Agreement and the pricing policies of the Group:

- Before entering into individual ACC Transactions, the Finance Department, the Legal Department, the Asset Management Department (which has a dedicated sub-division responsible for the management of connected transactions) and if applicable, certain other relevant departments of the Company will review the proposed terms for the individual ACC Transactions and discuss with the relevant departments of the Group to ensure that such transactions are conducted on normal commercial terms and in compliance with the pricing policies of the Group before these relevant departments approve the finalized transaction agreements according to their authority within the Group.

- The Asset Management Department of the Company is responsible for overseeing the connected transactions of the Company. The Asset Management Department will monitor and collect detailed information on the ACC Transactions on a regular basis, including but not limited to the implementation of pricing policies, payment arrangements and actual transaction amount to ensure that the transactions are conducted in accordance with the framework agreement. In addition, the Asset Management Department is responsible for monitoring and reviewing the balance amount of the annual cap for the ACC Transactions on a monthly basis and if the annual cap for the ACC Transactions is expected to be exceeded for a particular year, it will report to the management and take appropriate measures in accordance with the relevant requirements of the Hong Kong Listing Rules and/or Shanghai Listing Rules.

- The Company's Internal Audit Department is responsible for performing annual assessment on the internal control procedures of the Group, including but not limited to the relevant information on the management of continuing connected transactions. In addition, the Internal Audit Department is responsible for compiling the annual internal control assessment report and submitting the report to the Board for examination and approval.

- The senior management of the Company is responsible for supervising and monitoring the adoption of internal control procedures by the above-mentioned business departments, so as to ensure the implementation of pricing policies is in compliance with relevant framework agreements and the actual transaction amounts are controlled within annual caps. The senior management of the Company also reviews the implementation of pricing policies and the monitoring of annual caps annually.

- The independent auditor of the Company and the independent non-executive Directors will conduct an annual review on the continuing connected transactions of the Group.

The Company considers that above internal control procedures could function as effective measures to regulate continuing connected transactions. The Company also provides accurate materials in relation to continuing connected transactions as always to facilitate the annual review conducted by the independent non-executive directors and independent auditors. Therefore, the Directors consider that the above internal control procedures could ensure the continuing connected transactions will be conducted on normal commercial terms and not prejudicial to interests of the Company and its minority shareholders.

III. THE CNACG TRANSACTIONS

The New CNACG Framework Agreement was entered into between the Company and CNACG on 30 October 2019.

Parties and Connections of the Parties

The Company's principal business activity is air passenger, air cargo and airline-related services.

CNACG is both a substantial shareholder of the Company and a wholly-owned subsidiary of CNAHC, the Company's controlling shareholder, and is therefore a connected person of the Company as defined under the Hong Kong Listing Rules. CNACG is an investment holding company established in Hong Kong whose principal businesses include passenger terminal operation, cargo terminal operation, airport ground handling services, airline catering services, finance/operating lease, aircraft maintenance, property investment, logistics and other businesses conducted through its subsidiaries.

Description of the CNACG Transactions

The New CNACG Framework Agreement provides a framework for the CNACG Transactions contemplated thereunder between any member of the Group on the one hand and any member of CNACG Group on the other hand. According to the New CNACG Framework Agreement:

- **Finance and operating lease services**: CNACG Group will provide finance and operating lease services in respect of, among other things, aircraft, engines, simulators, equipment and vehicles to the Group; the Group will provide finance and operating lease services in respect of, among other things, equipment and vehicles to CNACG Group.

- **Ground support services and other services**: including but not limited to the following transactions conducted between any member of the Group on the one hand and any member of CNACG Group on the other hand: ground support services, aircraft maintenance services, aircraft repair services, property investment and management services, ticket and tourism services, logistics services, administrative management services, cleaning and washing services, resident security services, lounge supplies procurement services and aircraft material procurement services.

Pricing Policies for the CNACG Transactions

The consideration of any specific CNACG Transactions shall be agreed on arm's length negotiations between the Group and the CNACG Group and on normal commercial terms, which shall be determined in accordance with the pricing policies set forth below on a case-by-case basis.

- **Finance and operating lease services:** The final transaction price will be determined on arm's length negotiations between both parties with reference to the prices for the same type of lease services offered by independent third parties and after taking into account certain factors. Such factors include purchasing price of the leasing subject, interest rate and arrangement fees (if any) (for finance lease), rental fee (for operating lease), the lease terms, the feature of the leasing subject and the comparable market rental prices. The final transaction price should not be higher than the transaction prices offered by at least two independent third parties on the same conditions.

- **Ground support services and other services:**

  The pricing policies for ground support services and other services provided to or by the Group are set forth below:

  (1) Follow the government pricing or guide price if it is available, including but not limited to the guidance from the Civil Aviation Administration of the PRC (CAAC) and the International Air Transport Association on the prices of ground support services and other terms, and the requirements on the pricing of navigation information stipulated by CAAC and Air Traffic Management Bureau (ATMB).

  (2) If no government pricing or guide price is available, the final transaction price will be determined on arm's length negotiations between the parties, with firstly making reference to the market prices offered by at least two independent third parties on the market for the same type of service, and after taking certain factors into account such as service standard, service scope, business volume and specific need of parties. If any service need of the service recipient changes, appropriate adjustment will be made to the transaction price after negotiation between both parties based on the extent of variation in relevant costs, service quality or other factors.

  (3) If neither the above cases is applicable, the price will be determined on the basis of cost plus reasonable profit. The costs are mainly based on the costs and expenses of the service provider, including costs of human resources and costs of facility, equipment and materials. Reasonable profit margin will be determined mainly making reference to the historical average prices on similar products or services (where possible) published in relevant industry, and/or the profit margin of the comparable products and services disclosed by other listed companies. The profit margin of CNACG Group shall not exceed 10%. The final transaction prices shall be

determined on terms that to the Group are no favourable to those provided by independent third parties to the Group or those provided by CNACG Group to independent third parties (with regards to the receiving of services by the Group), or no more favorable than those provided by the Group to the independent third parties (with regards to the rendering of services by the Group).

Term of the New CNACG Framework Agreement

The initial term of the New CNACG Framework Agreement is three years commencing from 1 January 2020 and ending on 31 December 2022, which is automatically renewable for successive terms of three years after the expiry of its initial term, subject to the fulfilment of requirements under the Hong Kong Listing Rules/Shanghai Listing Rules and obtaining the required approval. Before expiry of the New CNACG Framework Agreement, the Board will re-assess the terms and conditions of the New CNACG Framework Agreement, and the Company will re-comply with the relevant rules governing connected transactions under the Hong Kong Listing Rules/Shanghai Listing Rules. During the term of the New CNACG Framework Agreement, the agreement can be terminated on any 31 December by either party thereto by serving the other party a written notice of termination of not less than three months.

Consistent with the common practice in the aviation industry, it is expected that the finance lease terms and the operating lease terms under the New CNACG Framework Agreement will exceed three years in most cases, but will be capped within the useful life of the leasing subject of finance or operating lease by respective finance and operating lease agreement. The useful life of the aircraft and engines is usually over 10 years and the useful life of simulators, ground support equipment and special vehicles is usually 3 to 20 years. Somerley has analysed the above lease terms. For details, please refer to the letter from the Independent Financial Adviser as set out in the Circular to be dispatched to Shareholders.

Reasons for and Benefits of the CNACG Transactions

In respect of the leasing business, entering into lease transactions with CNACG Group helps to streamline the process for the Group to secure relevant equipment that meets the specific needs of the Group with a lower cost of financing, higher flexibility and less impact on the Group's cash flow as compared to direct purchasing. In addition, the subsidiary of CNACG, to be acting as the lessors, is registered in the free trade zones in the PRC and are entitled to certain favourable tax treatments which will further lower the transaction costs of the Group. In terms of the aircraft finance lease, the Company expects that through adopting aircraft finance lease under the New CNACG Framework Agreement with CNACG Group, the estimated total saveable financing costs for the Group as compared to adopting secured loans arrangements with equivalent interest rates provided by the market over the same period will be approximately US$47.62 million, US$52.13 million and US$54.67 million, respectively from 2020 to 2022.

In respect of ground support services and other services, the Group has entered into a series of continuing connected transactions with CNACG Group in its ordinary and usual course of business. CNACG Group possesses ample management experience and financial resources on airport ground support services and logistics business, and it is able to provide high-quality services to the Group.

Historical Amounts and Historical Annual Caps

The table below sets out (i) the annual caps of the Group for the three years ended/ending 31 December 2017, 2018 and 2019; (ii) the actual aggregate amounts paid by the Group for each of the two years ended 31 December 2017 and 2018 and for January to August 2019, and the estimated aggregate amounts payable for the year ending 31 December 2019.

	Historical Amount				Historical Annual Caps		
	for the year ended/ ending 31 December		Actual amount for the period from January to August	Expected annual amount for	for the year ended/ ending 31 December		
Transactions	**2017**	**2018**	**2019**	**2019**	**2017**	**2018**[Note 1]	**2019**
Maximum transaction amount for aircraft finance lease service *(US$ Million)*	N/A	957	550	1,490	N/A	1,046.59	1,492.03
Finance lease of engines and simulators, operating lease of back-up aircraft engines and back-up ground support equipment, ground support services and other services *(RMB Million)*	378	416	351	503	2,450	2,450	2,450

Notes:

1. In terms of the maximum transaction amount for aircraft finance lease service, it covers the period from 1 June 2018 to 31 December 2018.

2. For the three years ended/ending 31 December 2017, 2018 and 2019, both the estimated aggregate amounts payable to, and the actual amounts paid to the Group by CNACG Group are below the de minimis threshold as stipulated under Rule 14A.76(1)(a) of the Hong Kong Listing Rules.

3. For the three years ended/ending 31 December 2017, 2018 and 2019, utilisation rate of the annual caps for finance lease in respect of engines and simulators, operating lease in respect of back-up aircraft engines and back-up ramp equipment, ground and others was low. The main reason leads

to such low utilisation rate is that the operating lease projects relating to aircraft, engine, simulator and ground support equipment of the subsidiary under CNACG that engages in leasing services were still at start-up stage, thus number of projects under progress is limited.

Proposed Annual Caps and Basis of Determination

The table below sets out the proposed annual caps for the total amount payable to CNACG Group by the Group for each of the three years ending 31 December 2020, 2021 and 2022, respectively:

Transactions	Proposed Annual Caps for the year ending 31 December 2020	2021	2022
	(in millions of RMB)		
Total value of right-of-use assets relating to the finance and operating leases entered into by the Group as lessee	14,500	16,000	16,500
Ground support services and other services	600	696	807

In arriving at the total use-right assets in relation to finance and operating leases of each year above, the Company has considered the following factors:

- Of the estimated total value of right-of-use assets in connection with finance and operating leases entered into by the Group as lessee, about 95% is the value of right-of-use assets in relation to finance lease of aircraft and other assets. When estimating the total value of right-of-use assets in connection with aircraft finance lease in the following three years, the Company has considered the followings: (i) historical transaction amounts; (ii) the aircraft introduction plan of the Group in the following three years (based on the Company's 2019 Interim Report, the Group expects to introduce 55, 93, and 42 aircraft to its fleet for years 2019 to 2021 respectively. The average compound annual growth rate of the Group's fleet capacity for years 2019 to 2021 is 8.85%. It is also assumed that growth rate of fleet expansion of the Group in 2022 will not exceed such rate), and the aggregate principal amount of the aircraft finance lease with CNACG Group is estimated based on the assumption that half of the aggregate consideration amounts of the aircraft scheduled to be introduced during the period from 2020 to 2022 according to confirmed orders will be introduced by way of finance lease with CNACG Group; (iii) adopting the prevailing benchmark interest rate i.e. 4.9%, for RMB loan for over 5 years promulgated by the PBOC ("Five Years Lending Rate") as the interest rate of aircraft finance leases considering that the lease term of each leasing aircraft is expected to be 10 to 12 years, and calculating the interest accordingly; (iv) calculating the arrangement fees at 0.5% of the principal amount of aircraft under finance lease with reference to prevailing market conditions. When estimating financing lease in connection with assets such as engines in the following three years, the Company had considered related finance leasing needs and adopted the same interest rate and arrangement fee rate as the above aircraft finance lease for estimation. Based on the above, the Company expected that the total rental fee (including the principal and interest payable throughout the lease term) and total arrangement fee of the finance leases for newly added assets such as aircraft in the three years ending 31 December 2022 will be US$2,518 million, US$2,747 million and US$2,848 million, respectively. By adopting the incremental borrowing rate of the Company as the discount rate (4.9% for leases with terms over 5 years) to discount such future estimated total rental fee and arrangement fee, the total value of right-of-use assets in relation to finance lease of aircraft and other assets for the three years ending 31 December 2022 will be approximately RMB13,821 million, RMB15,131 million and RMB15,861 million, respectively.

- The remaining about 5% of estimated total value of right-of-use assets in connection with finance and operating leases entered into by the Group as lessee is the value of right-of-use assets in relation to operating lease. When estimating the total value of right-of-use assets in relation to above-said lease in the following three years, the Company has considered the followings: (i) historical transaction amounts; (ii) the operation condition of the Group's engines, simulators and equipment and the Group's commercial demand for operating lease in the following three years (based on information currently available to the Company, the Company plans to lease 3 to 4 used engines, 4 back-up engines and 8 equipment from CNACG Group in each of the three years from 2020 to 2022, respectively); and (iii) the operating lease price and terms of the same or similar assets in domestic market (taking a certain kind of heavy aircraft tractor as example, its annual rental fee for operating lease in domestic market usually ranges from RMB600,000 to RMB900,000 and its lease term ranges from 3 years to 12 years). Based on the above, the Company expected that for the three years ending 31 December 2022, the annual rental fee of operating leases for newly added engines, simulators and equipment will be RMB77 million, RMB88 million and RMB89 million, respectively, while total rental fee of operating leases for newly added engines, simulators and equipment will be RMB640 million, RMB690 million and RMB690 million, respectively. By adopting the incremental borrowing rate of the Company as the discount rate (4.9% for leases with terms over 5 years and 4.75% for leases with terms ranging from 1 to 5 years) to discount such estimated future total rental fee, the total value of right-of-use assets in relation to operating lease of the three years ending 31 December 2022 will be approximately RMB610 million, RMB660 million and RMB660 million, respectively.

- Certain buffer has been included by rounding to the nearest integer to cater for the Group's operating needs from time to time.

In arriving at the estimated aggregate amounts payable to the CNACG Group in connection with the ground support services and other services provided by the CNACG Group for the three years ending 31 December 2022, respectively, the Company has considered, among other things, the historical transaction amounts and the following factors:

- Increasing need for relevant services: Given that the fleet capacity of the Group is expected to expand at an annual rate of approximately 9% from 2020 to 2022, it is expected that the need of the Group for relevant services will increase in line with the expansion of fleet capacity;

- Increase in unit price: Taking into account the historical increase of the Group's labour costs and equipment costs, as well as the growth rate of inflation, assuming the growth rate of unit prices for services provided by CNACG Group is generally in line with that of the Group, it is expected that the unit price of relevant services provided by the CNACG Group will increase at an annual rate of approximately 7% from 2020 to 2022; and

- Certain buffer has been included by rounding to the nearest integer to cater for the Group's operating needs from time to time.

Internal Control Procedures

The Group has adopted the following internal control procedures to ensure that the CNACG Transactions will be conducted on normal commercial terms, and in accordance with the New CNACG Framework Agreement and the pricing policies of the Group:

- Before entering into individual CNACG Transactions, the Finance Department, the Legal Department, the Asset Management Department (which has a dedicated sub-division responsible for the management of connected transactions) and if applicable, certain other relevant departments of the Company will review the proposed terms for the individual CNACG Transactions and discuss with the relevant business department of the Group to ensure that such transactions are conducted on normal commercial terms and in compliance with the pricing policies of the Group before these relevant departments approve the finalized transaction agreements according to their authority within the Group.

- The Asset Management Department of the Company is responsible for overseeing the connected transactions of the Company. The Asset Management Department will monitor and collect detailed information on the CNACG Transactions on a regular basis, including but not limited to the implementation of pricing policies, payment arrangements and actual transaction amount of each finance lease transaction, operating lease transaction and ground support services and other services to ensure that the transactions are conducted in accordance with the framework agreement. In addition, the Asset Management Department is responsible for monitoring and reviewing the balance amount of the annual cap for the CNACG Transactions on a monthly basis and if the annual cap for the CNACG

Transactions is expected to be exceeded for a particular year, it will report to the management and take appropriate measures in accordance with the relevant requirements of the Hong Kong Listing Rules and/or Shanghai Listing Rules.

- The Company's Internal Audit Department is responsible for performing annual assessment on the internal control procedures of the Group, including but not limited to the relevant information on the management of continuing connected transactions. In addition, the Internal Audit Department is responsible for compiling the annual internal control assessment report and submitting the report to the Board for examination and approval.

- The senior management of the Company is responsible for supervising and monitoring the adoption of internal control procedures by the above-mentioned business departments, so as to ensure the implementation of pricing policies is in compliance with relevant framework agreements and the actual transaction amounts are controlled within annual caps. The senior management of the Company also reviews the implementation of pricing policies and the monitoring of annual caps annually.

- The independent auditor of the Company and the independent non-executive Directors will conduct an annual review on the continuing connected transactions of the Group.

The Company considers that the above internal control procedures could function as effective measures to regulate continuing connected transactions. The Company also provides accurate materials in relation to continuing connected transactions to facilitate the annual review conducted by the independent non-executive Directors and the independent auditor. Therefore, the Directors consider that the above internal control procedures could ensure the continuing connected transactions will be conducted on normal commercial terms and not prejudicial to the interests of the Company and its minority shareholders.

IV. HONG KONG LISTING RULES IMPLICATIONS

ACC Transactions

As a non-wholly owned subsidiary of CNAHC, the Company's controlling shareholder, Air China Cargo is a connected person of the Company as defined under the Hong Kong Listing Rules, and accordingly the ACC Transactions constitute continuing connected transactions of the Company under Chapter 14A of the Hong Kong Listing Rules. As the highest applicable percentage ratio in respect of the proposed annual caps applicable to contracting operation income of Bellyhold Space Business payable by ACC Group under the ACC Transactions is, on an annual basis, higher than 5%, these transactions are therefore subject to the announcement, annual review, circular (including advice of independent financial adviser) and Independent Shareholders' approval requirements under Chapter 14A of the Hong Kong Listing Rules.

In respect of ground support services and other services provided by the Group, as the highest applicable percentage ratio in respect of the proposed annual caps of amounts payable by the ACC Group is, on an annual basis, higher than 0.1% but less than 5%, these transactions are therefore subject to the announcement and annual review requirements under Chapter 14A of the Hong Kong Listing Rules but are exempt from the Independent Shareholders' approval requirement.

In respect of the operation expenses of Bellyhold Space Business payable by the Company to Air China Cargo, as the highest applicable percentage ratio in respect of the proposed annual caps is, on an annual basis, higher than 0.1% but less than 5%, these transactions are therefore subject to the announcement and annual review requirements under Chapter 14A of the Hong Kong Listing Rules but are exempt from the Independent Shareholders' approval requirement.

In respect of ground support services and other services provided by the ACC Group, as the highest applicable percentage ratio in respect of the proposed annual caps of amounts payable by the Group is, on an annual basis, higher than 0.1% but less than 5%, these transactions are therefore subject to the announcement and annual review requirements under Chapter 14A of the Hong Kong Listing Rules but are exempt from the Independent Shareholders' approval requirement.

CNACG Transactions

CNACG is a connected person of the Company as defined under the Hong Kong Listing Rules, and accordingly the CNACG Transactions constitute continuing connected transactions of the Company under Chapter 14A of the Hong Kong Listing Rules. As the highest applicable percentage ratio in respect of the proposed annual caps applicable to finance and operating lease service provided by CNACG Group under the CNACG Transactions is, on an annual basis, higher than 5% but less than 25%, these transactions are therefore subject to the announcement, annual review, circular (including advice of independent financial adviser) and Independent Shareholders' approval requirements under Chapter 14A of the Hong Kong Listing Rules, and the requirements under Chapter 14 of the Hong Kong Listing Rules applicable to discloseable transactions.

In respect of ground support services and other services provided by CNAHC, as the highest applicable percentage ratio in respect of the proposed annual caps of amounts payable by the Group is, on an annual basis, higher than 0.1% but less than 5%, these transactions are therefore subject to the announcement and annual review requirements under Chapter 14A of the Hong Kong Listing Rules but are exempt from the Independent Shareholders' approval requirement.

In respect of finance and operating lease services provided by the Group to CNACG Group, for each of the three years ending 31 December 2020, 2021 and 2022, the aggregate amounts payable to the Group is expected to fall below the de minimis threshold as stipulated under Rule

14A.76(1)(a) of the Hong Kong Listing Rules, therefore, such transaction will be exempt from the announcement, annual review and Independent Shareholders' approval requirements under Chapter 14A of the Hong Kong Listing Rules.

In respect of ground support services and other services provided by the Group to CNACG Group, for each of the three years ending 31 December 2020, 2021 and 2022, the aggregate amount payable to the Group is expected to fall below the de minimis threshold as stipulated under Rule 14A.76(1)(a) of the Hong Kong Listing Rules, therefore, such transactions will be exempt from the announcement, annual review and Independent Shareholders' approval requirements under Chapter 14A of the Hong Kong Listing Rules.

V. SHANGHAI LISTING RULES IMPLICATIONS

ACC Transactions

As Air China Cargo is controlled by CNAHC, the controlling shareholder of the Company, Air China Cargo is considered as a related party of the Company according to Shanghai Listing Rules. As a result, the transactions between the Group and ACC Group constitute related party transactions under Shanghai Listing Rules. According to Shanghai Listing Rules, the transaction amounts of the proposed annual caps exceed 5% of the latest audited net assets of the Company, and therefore shall be disclosed in a timely manner and be submitted to the general meeting of the Company for consideration and approval by unrelated shareholders.

CNACG Transactions

As CNACG is controlled by CNAHC, the controlling shareholder of the Company, CNACG is considered as a related party of the Company according to Shanghai Listing Rules. As a result, the transactions between the Group and CNACG Group constitute related party transactions under Shanghai Listing Rules. According to Shanghai Listing Rules, the transaction amount of the proposed annual caps exceed 5% of the latest audited net assets of the Company, and therefore shall be disclosed in a timely manner and be submitted to the general meeting of the Company for consideration and approval by unrelated shareholders.

VI. VIEWS OF THE DIRECTORS

The Board (including the independent non-executive Directors) considers that the ACC Transactions and CNACG Transactions are on normal commercial terms or better, and are entered into in the ordinary and usual course of business of the Group, and the terms and conditions contained therein and the respective proposed annual caps are fair and reasonable and in the interests of the Company and the Shareholders as a whole.

Mr. Cai Jianjiang, Mr. Song Zhiyong, Mr. Cao Jianxiong, Mr. Xue Yasong and Mr. John Robert Slosar were considered to have material interest in the ACC Transactions and have abstained from voting on the relevant board resolutions. Mr. Cai Jianjiang, Mr. Song Zhiyong, Mr. Cao

Jianxiong and Mr. Xue Yasong were considered to have material interest in the CNACG Transactions and have abstained from voting on the relevant board resolutions. Save the above mentioned Directors, no other Director is required to abstain from voting on the relevant board resolutions.

The Company has appointed Somerley Capital Holdings Limited as the independent financial adviser to advise the Independent Board Committee and the Independent Shareholders in connection with the transactions contemplated under the New ACC Framework Agreement and the proposed annual caps thereunder as well as the transactions contemplated under the New CNACG Framework Agreement and the proposed annual caps thereunder.

A circular containing, among other things, (i) details of the transactions contemplated under the New ACC Framework Agreement and the proposed annual caps thereunder; (ii) details of the transactions contemplated under the New CNACG Framework Agreement and the proposed annual caps thereunder; (iii) a letter from Somerley Capital Holdings Limited to the Independent Board Committee and the Independent Shareholders containing its advice on the transactions contemplated under the New ACC Framework Agreement and the proposed annual caps thereunder as well as the transactions contemplated under the New CNACG Framework Agreement and the proposed annual caps thereunder; and (iv) the recommendation of the Independent Board Committee to the Independent Shareholders in respect of the ACC Transactions and the proposed annual caps thereunder as well as the CNACG Transactions and the proposed annual caps thereunder, will be dispatched to Shareholders on or about 4 November 2019 in accordance with the Hong Kong Listing Rules.

DEFINITIONS

In this announcement, unless the context otherwise requires, the following expressions have the following meanings:

"Bellyhold Space Business"	all the freight business operated through the utilization of the bellyhold space of passenger aircraft, including but not limited to the sale and pricing in relation to the bellyhold space
"ACC Framework Agreement"	the framework agreement dated 30 August 2016 entered into between the Company and Air China Cargo in respect of the ACC Transactions
"ACC Group"	Air China Cargo, its subsidiaries and 30%-controlled companies (as defined under Hong Kong Listing Rules)
"ACC Transactions"	the continuing connected transactions contemplated under the ACC Framework Agreement and the New ACC Framework Agreement, as applicable, between any member of the Group on the one hand, and any member of the ACC Group on the other hand

"Air China Cargo"	Air China Cargo Co., Ltd., a company established under the laws of the PRC with limited liability
"Board"	the board of directors of the Company
"Company"	Air China Limited, a company incorporated in the PRC, whose H shares are listed on the Hong Kong Stock Exchange as its primary listing venue and on the Official List of the UK Listing Authority as its secondary listing venue, and whose A shares are listed on the Shanghai Stock Exchange
"Cathay Pacific"	Cathay Pacific Airways Limited, a company incorporated in Hong Kong and listed on the Hong Kong Stock Exchange, the principal activity of which is the operation of scheduled airline services
"CNAHC"	China National Aviation Holding Corporation Limited, a company established under the laws of the PRC and the controlling shareholder of the Company, and is primarily engaged in managing its state-owned assets and its equity interest in investees, charter of aircraft and maintenance of aviation equipment
"CNACG"	China National Aviation Corporation (Group) Limited, a company incorporated under the laws of Hong Kong and a wholly-owned subsidiary of CNAHC
"CNACG Group"	CNACG, its subsidiaries and 30%-controlled companies (as defined under Hong Kong Listing Rules)
"CNACG Framework Agreement"	the framework agreement dated 30 August 2016 entered into between the Company and CNACG in respect of the CNACG Transactions
"CNACG Transactions"	the continuing connected transactions contemplated under the CNACG Framework Agreement and the New CNACG Framework Agreement, as applicable, between any member of the Group on the one hand, and any member of the CNACG Group on the other hand, but excluding the various services, such as airline catering service, housing rental, etc., that have been included or will be included in the continuing connected transaction framework agreements entered into between the Company and CNAHC
"Director(s)"	the director(s) of the Company
"Group"	the Company and its subsidiaries

"Hong Kong Listing Rules"	the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited
"Hong Kong Stock Exchange"	The Stock Exchange of Hong Kong Limited
"Independent Board Committee"	a board committee comprising Mr. Wang Xiaokang, Mr. Liu Deheng, Mr. Stanley Hui Hon-chung and Mr. Li Dajin, all being the independent non-executive Directors of the Company
"Independent Shareholders"	In terms of ACC Transactions, the Shareholders of the Company excluding CNAHC, CNACG, Cathay Pacific and its associates; in terms of CNACG Transactions, the Shareholders of the Company excluding CNAHC and CNACG
"New ACC Framework Agreement"	the framework agreement dated 30 October 2019 entered into between the Company and Air China Cargo in respect of the ACC Transactions
"New CNACG Framework Agreement"	the framework agreement dated 30 October 2019 entered into between the Company and CNACG in respect of the CNACG Transactions
"PBOC"	People's Bank of China
"Somerley" or "Independent Financial Adviser"	Somerley Capital Holdings Limited, a licensed corporation licensed to carry out Type 6 (advising on corporate finance) regulated activity under the SFO, as the Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders to advise on (i) the transactions contemplated under the New ACC Framework Agreement and the proposed annual caps thereunder; (ii) the transactions contemplated under the New CNACG Framework Agreement and the proposed annual caps thereunder
"RMB"	the lawful currency of the PRC
"SFO"	the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong), as amended and modified from time to time

"Shanghai Listing Rules"	the Listing Rules of Shanghai Stock Exchange
"Shareholder(s)"	the shareholder(s) of the Company

By Order of the Board
Air China Limited
Zhou Feng   Tam Shuit Mui
Joint Company Secretaries

Beijing, the PRC, 30 October 2019

As at the date of this announcement, the directors of the Company are Mr. Cai Jianjiang, Mr. Song Zhiyong, Mr. Cao Jianxiong, Mr. Xue Yasong, Mr. John Robert Slosar, Mr. Wang Xiaokang, Mr. Liu Deheng*, Mr. Stanley Hui Hon-chung* and Mr. Li Dajin*.*

* *Independent non-executive director of the Company*