THIS CIRCULAR IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION

If you are in any doubt as to any aspect of this circular or as to the action you should take, you should consult your stockbroker or other registered dealer in securities, bank manager, solicitor, professional accountant or other professional adviser.

If you have sold or transferred all your shares in Air China Limited, you should at once hand this circular along with the accompanying form of proxy to the purchaser or the transferee or to the bank, stockbroker or other agent through whom the sale was effected for transmission to the purchaser or transferee.

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)

(1) CONTINUING CONNECTED TRANSACTIONS AND DISCLOSEABLE TRANSACTION; AND (2) PROPOSED ENTERING INTO OF THE SUPPLEMENTAL AGREEMENT AND NOTICE OF EXTRAORDINARY GENERAL MEETING

Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders

SOMERLEY CAPITAL LIMITED

A letter from the Board is set out on pages 5 to 36 of this circular.

A letter from the Independent Board Committee, containing its advice to the Independent Shareholders of the Company, is set out on pages 37 to 38 of this circular.

A letter from the Independent Financial Adviser, containing its advice to the Independent Board Committee and the Independent Shareholders of the Company, is set out on pages 39 to 65 of this circular.

A notice convening the EGM to be held at 11:00 a.m. on Friday, 14 October 2022 at The Conference Room C713, No. 30, Tianzhu Road, Airport Industrial Zone, Shunyi District, Beijing, the PRC, is set out on pages 70 to 72 of this circular. Whether or not you are able to attend the EGM, you are requested to complete and return the accompanying form of proxy in accordance with the instructions printed thereon as soon as possible but in any event not less than 24 hours before the time appointed for convening the EGM or any adjournment thereof. Completion and return of the form of proxy will not preclude you from attending and voting in person at the EGM or any adjournment thereof should you so wish.

28 September 2022

CONTENTS

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

"2019 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
"2022 ACC Framework Agreement"	the framework agreement dated 20 September 2022 entered into between the Company and Air China Cargo in respect of the ACC Transactions
"ACC Group"	Air China Cargo and the corporations or other entities in which Air China Cargo holds 30% or more equity interests or voting rights at the general meeting or the majority directors of which are controlled, directly or indirectly, by Air China Cargo
"ACC Transactions"	the continuing connected transactions contemplated under the 2019 ACC Framework Agreement and the 2022 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 incorporated under the laws of the PRC with limited liability
"Board"	the board of directors of the Company
"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
"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
"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 October 2019 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 between the member of the Group on the one hand, and the 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
"CNAF"	China National Aviation Finance Co., Ltd, a company incorporated under the laws of the PRC with limited liability and is held as to 51% and 49% by the Company and CNAHC. CNAF is primarily engaged in providing financial services to CNAHC's member companies. Since CNAHC can exercise more than 10% of the voting power at CNAF's general meeting, CNAF is a connected subsidiary of the Company as defined under Rule 14A.16 of the Hong Kong Listing Rules
"CNAHC"	China National Aviation Holding Corporation Limited, a PRC state-owned enterprise and the controlling shareholder of the Company, directly and indirectly holding approximately 51.70% of the issued share capital of the Company in aggregate as at the Latest Practicable Date
"CNAHC Financial Services Agreement"	the CNAHC financial services agreement renewed by CNAF and CNAHC on 28 August 2020
"CNAHC Group"	CNAHC and the corporations or other entities in which CNAHC holds 30% or more equity interests or voting rights at the general meeting or the majority directors of which are controlled, directly or indirectly, by CNAHC (excluding the Group)
"Comprehensive Services Framework Agreement"	the framework agreement for the continuing related (connected) transactions of comprehensive services entered into between the Company and CNAHC on 29 October 2021
"connected person(s)"	has the meaning ascribed to it under the Hong Kong Listing Rules
"CSRC"	the China Securities Regulatory Commission
"Director(s)"	the director(s) of the Company
"EGM"	the extraordinary general meeting of the Company to be held at 11:00 a.m. on Friday, 14 October 2022 at The Conference Room C713, No. 30, Tianzhu Road, Airport Industrial Zone, Shunyi District, Beijing, the PRC

"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. Li Fushen, Mr. He Yun, Mr. Xu Junxin and Ms. Winnie Tam Wan-chi, all being the independent non-executive Directors of the Company
"Independent Shareholders"	In terms of ACC Transactions and the Supplemental Agreement, 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
"Latest Practicable Date"	22 September 2022, being the latest practicable date prior to the printing of this circular for ascertaining certain information contained herein
"Non-exempt Transactions"	the relevant transactions of the Passenger Aircraft Cargo Business under the 2022 ACC Framework Agreement and the finance and operating leases entered into between the Group, as lessee, and CNACG Group
"Passenger Aircraft Cargo Business"	all passenger aircraft cargo businesses and a series of relevant business operation activities (including but not limited to sales, pricing and settlement of aircraft cargo space) operated by the Group (including all airlines controlled by the Group)
"PBOC"	People's Bank of China
"Properties Leasing Framework Agreement"	the framework agreement for the continuing related (connected) transactions of properties leasing entered into between the Company and CNAHC on 29 October 2021
"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

"Somerley" or "Independent Financial Adviser"	Somerley Capital Limited, a licensed corporation licensed to carry out Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities under the SFO, as the Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders to advise on the Non-exempt Transactions
"Supplemental Agreement"	the agreement for the matters related to the related (connected) transactions involving Air China Cargo entered into among the Company, CNAHC, Air China Cargo and CNAF on 20 September 2022
"Trademark License Framework Agreement"	the trademark license framework agreement entered into between the Company and CNAHC on 28 August 2020

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)

Directors:
Executive Directors:
Song Zhiyong *(Chairman)*
Ma Chongxian *(President)*

Non-Executive Directors:
Feng Gang
Patrick Healy

Independent Non-Executive Directors:
Li Fushen
He Yun
Xu Junxin
Winnie Tam Wan-chi

Registered Address:
1st Floor-9th Floor 101, Building 1
30 Tianzhu Road
Shunyi District
Beijing, the PRC

Principal Place of Business in Hong Kong:
5th Floor, CNAC House
12 Tung Fai Road
Hong Kong International Airport
Hong Kong

28 September 2022

To the Shareholders

Dear Sir or Madam,

(1) CONTINUING CONNECTED TRANSACTIONS AND DISCLOSEABLE TRANSACTION; AND (2) PROPOSED ENTERING INTO OF THE SUPPLEMENTAL AGREEMENT AND NOTICE OF EXTRAORDINARY GENERAL MEETING

I. INTRODUCTION

Reference is made to the announcements of the Company dated 30 October 2019 and 20 September 2022 in relation to, among other things, the ACC Transactions. In order to further address the issue of business competition and optimize transaction structure, the Group intended to carry out a long-term collaboration with the ACC Group for the Passenger Aircraft Cargo Business under an exclusive operating model. Therefore, the Company and Air China Cargo entered into the 2022 ACC Framework Agreement to make amendments on the operation model of the Passenger Aircraft Cargo Business.

Reference is made to the announcements of the Company dated 30 October 2019 and 20 September 2022 in relation to, among other things, the CNACG Transactions. The current term of the CNACG Framework Agreement will expire on 31 December 2022. As the Company expects that the CNACG Transactions will continue to be conducted after 31 December 2022, on 20 September 2022, the Company proposed to renew the CNACG Framework Agreement with CNACG.

Reference is made to the announcements of the Company dated 28 August 2020 and 29 October 2021 in relation to, among other things, the CNAHC Financial Services Agreement, Trademark License Framework Agreement, Comprehensive Services Framework Agreement and Properties Leasing Framework Agreement, as well as the announcement of the Company dated 20 September 2022 in relation to the Supplemental Agreement. Pursuant to the relevant listing requirements of Air China Cargo, Air China Cargo shall maintain independence from CNAHC and enter into framework agreement with the Group separately. Therefore, the Company and CNAHC, Air China Cargo and CNAF entered into the Supplemental Agreement to stipulate that the CNAHC Financial Services Agreement, Trademark License Framework Agreement, Comprehensive Services Framework Agreement and Properties Leasing Framework Agreement shall not regulate the relevant transactions entered into between the Group and ACC Group. Air China Cargo will, as an independent entity, enter into relevant connected transaction agreement(s) with the Company and CNAF separately.

The purpose of this circular is to provide you with further information on the abovementioned matters so that you can make an informed decision on voting in respect of the relevant resolutions at the EGM.

II. ACC TRANSACTIONS

The Company and Air China Cargo entered into the 2022 ACC Framework Agreement on 20 September 2022.

1. Parties and the relationship between the parties

The Company is principally engaged in providing air passenger, air cargo and airline-related services.

Air China Cargo is owned as to 45.0018% by CNAHC, the 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.

CNAHC directly holds 40.98% of the Company's shares and holds 10.72% of the Company's shares through its wholly-owned subsidiary CNACG, and is the controlling shareholder of the Company as at the Latest Practicable Date. As at the Latest Practicable Date, the State-owned Assets Supervision and Administration Commission of the State Council is a controlling shareholder and de facto controller of CNAHC. CNAHC primarily operates all the state-owned assets and state-owned equity interests invested by the State in CNAHC and its invested entities, aircraft leasing and aviation equipment and facilities maintenance businesses.

2. Description of the ACC Transactions

The ACC Transactions contemplated under the 2022 ACC Framework Agreement are as follows:

- **Exclusive operation of the Passenger Aircraft Cargo Business:** In order to further address the issue of business competition and optimize transaction structure, after friendly negotiation between both parties, the Group and the ACC Group have determined to carry out a long-term collaboration for the Passenger Aircraft Cargo Business under an exclusive operating model. The entire Passenger Aircraft Cargo Business of the Group will be operated exclusively by the ACC Group, and the ACC Group shall undertake the overall responsibilities for transporting the cargos to the consignors with respect to the cargos which are transported through the passenger aircraft.

  The term of the exclusive operation of the Passenger Aircraft Cargo Business between the Company and the ACC Group commences from the effective date of the 2022 ACC Framework Agreement and ends on 31 December 2034. The commencement date of the term of the exclusive operation of the Passenger Aircraft Cargo Business between the airlines controlled by the Group and the ACC Group shall be subject to the written agreement entered into between such airlines and ACC Group, if otherwise specified. Upon expiry of the exclusive operation term, the parties may determine new exclusive operation term through friendly negotiation.

- **Ground support services and other services:** The ground support services and other services provided by the Group to the ACC Group include but are not limited to operation support services, IT sharing services, comprehensive support services, engine and aircraft-related materials sharing services, retiree management services, training services, human resources services (including general, servicing and information services in respect of personnel employment, archival information, salaries and benefits, social insurance and employee services), and procurement and maintenance services. The ground support services and other services provided by the ACC Group to the Group include but are not limited to ground support services (cargo terminal services and airport apron services), container and pallet management services, engine and aircraft-related materials sharing services.

  In respect of the engine and aircraft-related materials sharing services between the Group and the ACC Group, they mainly involve the provision of common engine and aircraft-related materials by the other party when one party's own engine and aircraft-related materials could not be able to meet its respective needs (mainly involving high-priced reusable components on the aircraft), for the purpose of reducing the procurement costs and timeliness in the event of temporary needs of the parties, while, on the other hand, improve each of their inventory utilization efficiency, hence bringing certain source of revenue.

- **Property leasing:** The Group may rent out its own properties or land with legal use rights to ACC Group for its production and operation, office and storage use, and the Group may lease self-owned properties and land from the ACC Group in the event that its own properties could not be able to meet its business needs such as production and operation, office and storage.

  The properties leased to each other between the Group and the ACC Group differ in terms of aspects such as geographical location, area and purpose. Currently, the properties rent out by the Group to the ACC Group are mainly properties invested and built by the Group in the vicinity of the Beijing Capital International Airport for warehouse purpose, which are subject to the supervision and administration of the General Administration of Customs of the PRC, and the properties leased by the Group from the ACC Group at present are mainly properties adjacent to the Group that were leased to the Group for its use by the ACC Group under the circumstances that the Group's own properties could not be able to meet its office and operation needs.

  Generally, the leasing term of properties or land shall not exceed three years. If there are specific government and/or industry requirements, the leasing term of properties or land shall comply with such requirements. When the terms expired, the leasing terms could be extended with unanimous consent after negotiation between both parties.

3. 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.

- **Exclusive operation of the Passenger Aircraft Cargo Business:**

  During the exclusive operation term, the Group shall charge the ACC Group the transportation service fee regularly in each year. Such transportation service fee shall be determined based on the ACC Group's actual cargo revenue generated from the exclusive operation of the Group's Passenger Aircraft Cargo Business after deducting certain operating fee rate. The specific formulas are as follows:

  Transportation service fee = actual revenue from the Passenger Aircraft Cargo Business × (1 – operating fee rate)

  Operating fee rate = operation expense rate + reward/punishment rate

Reward/punishment rate = (growth rate of yield level of the Passenger Aircraft Cargo Business of the current year – growth rate of yield level of the cargo business in the industry of the current year) ×50%

Of which:

(1) The actual revenue of the Passenger Aircraft Cargo Business represents the actual cargo revenue generated by ACC Group's exclusive operation of the Group's Passenger Aircraft Cargo Business.

(2) The operation expense rate represents the ratio of operating expenses to actual revenue from the Passenger Aircraft Cargo Business. Operation expenses are determined by the parties through arm's length negotiation primarily based on the operation expenses in the historical years, with reference to factors such as the price level in the similar market and industry and its variation trend.

(3) In order to enhance the operating results of the exclusive operation of the Passenger Aircraft Cargo Business, the both parties decide to apply the reward/punishment rate after negotiation. The basic index of reward/punishment rate represents 50% of the difference between the yield level growth rate of the Passenger Aircraft Cargo Business and the yield level growth rate of the cargo business in the industry of the current year. The parties may make reasonable adjustments according to the changes in the market environment and the operation direction of the Passenger Aircraft Cargo Business with unanimous consent after negotiation. The rate of 50% is determined by the Company and Air China Cargo through arm's length negotiation with reference to industry practice. The rate of 50% is the same as the relevant ratios of similar transactions of comparable companies in the industry, which will encourage the ACC Group to enhance its capacity of the Passenger Aircraft Cargo Business, thereby boosting the operating efficiency of the Group's Passenger Aircraft Cargo Business, and hence the rate is fair and reasonable.

(4) The growth rate of yield level of the Passenger Aircraft Cargo Business of the current year represents the growth rate of the yield level of the Passenger Aircraft Cargo Business of the current year generated by ACC Group's exclusive operation of the Group's Passenger Aircraft Cargo Business as compared with that of the previous year.

(5) The growth rate of yield level of the cargo business in the industry of the current year represents the growth rate of the revenue of the cargo business in the industry of the current year as compared with that of the previous year.

(6) The yield level of the cargo business represents the cargo revenue divided by the investment amount for the cargo business. The investment amount for the cargo business represents the total available cargo and mail traffic measured by the

capacity available for the carriage of the cargo and mail for every route, and the calculation formula of which is ∑ (capacity available for the carriage of the cargo and mail of the route multiplied by the distance of the route).

Upon the 2022 ACC Framework Agreement becoming effective, the 2019 ACC Framework Agreement shall be terminated immediately. With respect to the Passenger Aircraft Cargo Business performed between the parties in accordance with the 2019 ACC Framework Agreement and the relevant specific agreement in 2022, both parties agreed that it shall be deemed to have been correspondingly adjusted in accordance with the above-mentioned principles since 1 January 2022.

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

  Both parties shall, according to the service items and specific needs, determine the relevant service fees of the ground support services and other services provided to or by the Group through arm's length negotiations in accordance with the following principles:

  (1) Follow the government and industry pricing or guide price if it is available, including but not limited to the guidance from the Civil Aviation Administration of China (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), and the transaction price shall be determined by the parties through arm's length negotiation with reference to factors such as comparable prices (if any) in the market, relevant laws and tax policies. Generally, CAAC and the International Air Transport Association will publish the guidance on their official websites from time to time (for the International Air Transport Association, the guidance may also be provided by selling to customers).

  (2) If no government and industry pricing or guide price is available, the final transaction price shall be determined through 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 then taking certain factors into account such as the service standard, service scope, business volume and specific needs of the parties. If any service needs of the service recipient change, 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 none of the above prices are applicable, the service price shall be determined by both parties 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 regarding the

relevant industry, and/or the profit margin of the comparable products and services disclosed by other listed companies. The reasonable 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 than those provided by independent third parties to the Group or those provided by ACC Group to independent third parties. The Group generally may gain understanding on the historical average prices of the reasonable profit margin of similar products or services of the relevant industry by engaging third-party professional institutions or making its own enquiries through channels such as available data resources (e.g. Bureau van Dijk (BVD) and other large-scale databases) and the official websites of other listed companies. Besides, prior to entering into transactions of various ground support services and other services, the Group will request the ACC Group to provide and hence obtain the terms of similar and comparable transactions between the ACC Group and independent third parties whenever possible as its reference for determining the transaction price. While making reference to the profit margin of comparable products and services disclosed by other listed companies, the Group will try to acquire comparable data as more as possible, and generally by referring to at least two listed companies' relevant data where practicable.

- **Property leasing services:**

The parties shall, according to the service items and specific needs, determine the relevant service fees of the property leasing services through arm's length negotiations in accordance with the following principles:

(1) The Group as lessor: First, the Group shall provide quotation of the leased properties or land to ACC Group after taking into account the factors including the relevant costs, tax and reasonable profit margin relating to the properties or land. The relevant costs include construction costs, depreciation costs, funding costs and maintenance costs. Reasonable profit margin will be determined with mainly making reference to the historical average prices on similar services (where possible) published regarding the property leasing industry, and/or the profit margin of the comparable services disclosed by other listed companies. Then, the rental prices for the leased properties or land shall be determined through arm's length negotiations between the Group and ACC Group after ACC Group takes into account the factors such as the location of the leased properties or land and the service quality. Such rental prices shall not be lower than the rent offered by the Group to an independent third party (if any) in comparable circumstances.

(2) The Group as lessee: First, the Group shall conduct market research and collect, consolidate and analyze information in respect of provision of leasing services by independent third parties for the same type of properties or land (if any) in close proximity to the properties or land to be leased. Generally, the Group shall assign a department or an officer to verify the price and terms available from at least

two independent third parties (if any) by email, fax or telephone. Then, (a) if there is comparable market of the same type identified through market research, the parties shall determine the rental prices for the leased properties or land through arm's length negotiations with reference to the market price for the same type of services available from at least two independent third parties after taking into account the relevant factors. The relevant factors include the geographical location, function and layout, furnishing, ancillary facilities and property services of the property or land as well as the specific needs of the lessee; and (b) if there is no comparable market of the same type found in the neighboring areas through market research, the price shall be determined by adopting the cost-plus approach: the rental price of the leased properties or land shall be determined through arm's length negotiations between the parties based on the relevant costs, tax and reasonable profit margin of the properties or land offered by ACC Group. The relevant costs include construction costs, depreciation costs, funding costs and maintenance costs. Reasonable profit margin will be determined with mainly making reference to the historical average prices on similar services (where possible) published regarding the property leasing industry, and/or the profit margin of the comparable services disclosed by other listed companies, and the reasonable profit margin of ACC Group shall not exceed 10%. The abovementioned rental prices shall not be higher than those offered by ACC Group to the independent third parties (if any) in comparable circumstances.

The Group generally may gain understanding on the historical average prices of the reasonable profit margin of similar products or services of the relevant industry by engaging third-party professional institutions or making its own enquiries through channels such as available data resources (e.g. Bureau van Dijk (BVD) and other large-scale databases) and the official websites of other listed companies. Besides, prior to entering into transactions of various ground support services and other services, the Group will request the ACC Group to provide and hence obtain the terms of similar and comparable transactions between the ACC Group and independent third parties whenever possible as its reference for determining the transaction price. While making reference to the profit margin of comparable products and services disclosed by other listed companies, the Group will try to acquire comparable data as more as possible, and generally by referring to at least two listed companies' relevant data where practicable.

(3) The Group as lessee and lessor: When leasing each other's properties or land, as a separate matter, the parties may determine the quotation for the rental prices of their respective properties or land based on the above pricing principles, and then exchange the properties and land use right in accordance with the principle of equivalent exchange.

(4) The payment method of rental fee shall be subject to specific agreement.

4. Term of the 2022 ACC Framework Agreement

The 2022 ACC Framework Agreement shall take effect upon the approval by the Shareholders at the general meeting of the Company and Air China Cargo, and shall be valid until 31 December 2024 (the "**Initial Term**"). The 2022 ACC Framework Agreement may be automatically renewed for successive terms of three years after 31 December 2024 (together with the Initial Term, collectively referred to as the "**Terms of the Agreement**"), subject to the compliance with requirements under the Hong Kong Listing Rules/Shanghai Listing Rules and the approval procedures required under the Hong Kong Listing Rules/Shanghai Listing Rules. During the Terms of the Agreement, the agreement can be terminated upon the expiry on any 31 December by either party thereto by serving the other party a written notice of not less than three months. However, the exclusive operation term of the Passenger Aircraft Cargo Business between the Group and ACC Group under the 2022 ACC Framework Agreement shall not be terminated upon the termination of the 2022 ACC Framework Agreement, provided that the compliance requirements (including but not limited to obtaining approval and fulfilling disclosure procedures for the annual caps) under the Hong Kong Listing Rules/ Shanghai Listing Rules shall then be complied with.

Upon the 2022 ACC Framework Agreement becoming effective, the 2019 ACC Framework Agreement shall be terminated immediately.

5. Independent Financial Adviser's opinion on the exclusive operation term of the Passenger Aircraft Cargo Business

As mentioned above, the exclusive operation term of the Passenger Aircraft Cargo Business is approximately 12 years. According to Rule 14A.52 of the Hong Kong Listing Rules, the term of the agreement for a continuing connected transaction shall not exceed three years except in special circumstances where the nature of the transaction requires a longer contractual term. In this case, the listed issuer shall appoint an independent financial adviser to explain why the agreement requires a longer term and to confirm that it is normal business practice for agreements of this type to be of such duration. Accordingly, the Company has engaged Somerley as the Independent Financial Adviser, and Somerley has formulated its opinion as follows:

Having considered the following factors, Somerley is of the view that a term of longer than three years is required for the effective operation of the transactions relating to the Passenger Aircraft Cargo Business (the "**Cargo Transactions**") and is a normal business practice in the industry:

(i) Air China Cargo intends to apply for the listing of A shares and to comply with the applicable guidelines on initial public offering and listing of shares issued by CSRC, the Cargo Transactions having a term more than three years is necessary for facilitating the potential listing of Air China Cargo;

(ii) entering into of the Cargo Transactions could provide a clear delineation of business and thereby eliminating concerns associated with competition between the Company and Air China Cargo;

(iii) Air China Cargo is the sole service provider for the Passenger Aircraft Cargo Business and in view of the shareholding structure of both the Group and Air China Cargo, it is not practical or commercially sensible for the Company to entrust such services with another party in the PRC as such counterparty would have to have a reasonable business scale to handle the Group's Passenger Aircraft Cargo Business and possible candidates with such business scale would normally be under control of an industry competitor; and

(iv) Somerley considers the practice of having a term of longer than three years is not uncommon in the industry because Somerley noted that the similar exclusive passenger aircraft bellyhold space contractual operation arrangement of China Eastern Airlines Corporation Limited is also for a long term of 12 years.

6. Independent Financial Adviser's opinion on the leasing term of properties

As mentioned above, for the purpose of the property leasing services between the Group and the ACC Group, the leasing term of properties or land for both parties shall not exceed three years. However, if there are specific government and/or industry requirements, the leasing term of properties or land shall comply with such requirements (the "**Regulated Property(ies)**").

Air China Cargo (as the lessee) leased properties which are subject to the supervision and administration of the General Administration of Customs of the PRC (the "**GAC Regulated Properties**") from the Company (as the lessor). The initial leasing term of the GAC Regulated Properties shall exceed three years which is mainly due to the compulsory administrative regulations of the General Administration of Customs of the PRC. Therefore, the GAC Regulated Properties under lease are the Regulated Properties. According to Rule 14A.52 of the Hong Kong Listing Rules, the term for the agreement for a continuing connected transaction shall not exceed three years except in special circumstances where the nature of the transaction requires a longer term. In this case, the listed issuer shall appoint an independent financial adviser to explain why the agreement requires a longer term and to confirm that it is normal business practice for the agreements of this type to be of such duration.

As disclosed in the announcement of the Company dated 29 October 2021, the Company had engaged BaoQiao Partners Capital Limited, a corporation licensed to carry on Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities under the Securities and Futures Ordinance (Chapter 571 of the laws of Hong Kong) ("**BaoQiao Partners**"), to advise opinion in respect of the leasing term of the Regulated Properties. In particular, (i) based on BaoQiao Partners' review of the Measure of the PRC for the General Administration of Places under Customs Supervision General (中華人民共和國海關監管場所管理辦法) issued by the General Administration of Customs of the PRC effective from 1 March 2008, BaoQiao Partners noted that the lease term of property for the use of loading, unloading, storage, delivery and shipping of import and export goods in the areas that are subject to the oversight and supervision of the General Administration of Customs is required to be at least five years. In this regard, it is normal business practice with regards to the compliance with applicable government/industrial regulations or requirements for the lease term of the lease agreements to be over three years; (ii) the lease terms for the Regulated Properties are subject to the requirements under specific government or industrial regulations, and the entering into leases of the Regulated Properties will provide the flexibility for the Company to lease out its vacant Regulated Properties for rental income; and (iii) BaoQiao Partners has reviewed the continuing connected transaction announcements published by companies listed on the Hong Kong Stock Exchange since 2018, and noted that there were similar framework agreements, of which the lease term exceeded three years, and the properties under these framework agreements include production facilities, commercial properties and offices which are relevant to their respective operations and the framework agreements to lease these premises have a duration term of up to 15 years. To sum up, BaoQiao Partners is of the view that it is normal business practice to enter into leases for the Regulated Properties with terms of more than three years and to be of such duration for agreements of this type. Please refer to the announcement of the Company dated 29 October 2021 for details.

7. 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 exclusive contracting operation of the Passenger Aircraft Cargo Business,

  in comparison with the business arrangement of the 2019 ACC Framework Agreement, under the 2022 ACC Framework Agreement:

  (i) The two-way settlement model of income and expenditure is adjusted to a one-way net settlement. This allows for simplification of transactions and procedures and facilitates public understanding.

  (ii) Instead of conducting estimation at the beginning of year and year-end reviews, revenue recognition of the Group has been adjusted to actual revenue recognition, further ensuring the fairness and independence of transactions.

  (iii) The reward/punishment rate is applied in the operating fee rate, and the industry yield level is used as incentives and restrictive mechanisms, which indicated the fairness of pricing for connected transactions. By enhancing the capacity of the Passenger Aircraft Cargo Business of Air China Cargo, the Company's income from passenger aircraft cargo operation will be increased.

- 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.

- In respect of properties leasing services, the Group has entered into similar property leasing transactions with various parties including both connected persons and independent third parties in the ordinary course of business. The leasing of the Group's properties to the ACC Group is beneficial to the Group in improving the efficiency of asset utilization and obtaining rental income. The properties leased by the ACC Group to the Group are generally located in the vicinity of the Group's office, and therefore can meet the Group's relevant needs in a more efficient and convenient way.

8. Actual Amounts and Existing 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 2020, 2021 and 2022, respectively; and (ii) the actual amounts paid by the ACC Group or the Group for each of the two years ended 31 December 2020 and 2021 and for the six months ended 30 June 2022, and the estimated amounts payable for the year ending 31 December 2022 (if applicable).

Unit: RMB Million

	Actual Historical Amounts			Estimated Future Amounts[1]	Existing Annual Caps		
	For the year ended 31 December 2020	For the year ended 31 December 2021	For the six months ended 30 June 2022	For the year ending 31 December 2022	For the year ended 31 December 2020	For the year ended 31 December 2021	For the year ending 31 December 2022
Amounts payable/paid by the ACC Group to the Group							
In terms of contracting operation income of passenger aircraft bellyhold space cargo business	7,685	10,491	6,656	N/A	8,000	11,000	14,000
In terms of ground support services and other services	603	789	426	1,500	800	1,000	1,100
Amounts payable/paid by the Group to the ACC Group[2]							
In terms of operation expenses of bellyhold space	351	609	351	N/A	800	960	1,160
In terms of ground support services and other services	569	630	288	1,400	1,000	1,200	1,400

Notes:

(1) Upon the 2022 ACC Framework Agreement becoming effective, with respect to the Passenger Aircraft Cargo Business between the Company and the ACC Group in 2022 that has been performed in accordance with the 2019 ACC Framework Agreement and the relevant specific agreement, both parties agree that such business shall be deemed to have been adjusted in accordance with the pricing principles as disclosed above since 1 January 2022 (i.e. adjusting the two-way settlement model of income and expenditure to a one-way net settlement, and calculating the amount of service fee based on the formulas under the 2022 ACC Framework Agreement (as disclosed above)). Therefore, the estimated amounts of the contracting operation income of passenger aircraft bellyhold space cargo business and operation expenses of bellyhold space in 2022 are not listed.

(2) Under the impact of the COVID-19 pandemic, the fleet capacity of the Company's passenger aircraft has declined. Therefore, the utilization rate of the annual cap for operation expenses of bellyhold space related to flight volume in 2020, 2021 and the six months ended 30 June 2022 was relatively low, which has accordingly reduced the business volume of cargo warehouse operations and airport apron operations related to flight volume and resulted in a lower utilization rate of the annual cap of amounts payable by the Group to the ACC Group in respect of ground support services and other services.

As of the Latest Practicable Date, the actual amount paid by the ACC Group or the Group under the 2019 ACC Framework Agreement since 1 January 2022 has not exceeded the annual caps of such transactions for the year ending 31 December 2022.

9. Proposed Annual Caps and Basis of Determination

After the 2022 ACC Framework Agreement becoming effective, the 2019 ACC Framework Agreement shall be terminated. As the Passenger Aircraft Cargo Business under the 2022 ACC Framework Agreement is adjusted to follow the one-way settlement model, the Company proposes to revise the annual caps for 2022 under the 2022 ACC Framework Agreement.

The table below sets out the revised annual caps of amounts payable by the ACC Group or the Group after the 2022 ACC Framework Agreement has become effective for the year ending 31 December 2022 and the proposed annual caps for each of the two years ending 31 December 2023 and 2024, respectively:

Unit: RMB Million

	Proposed Annual Caps		
Transactions	**For the year ending 31 December 2022**	**For the year ending 31 December 2023**	**For the year ending 31 December 2024**
Amounts Payable by the ACC Group to the Group			
In terms of the transportation service fees of the Passenger Aircraft Cargo Business	15,500	17,000	18,000
In terms of ground support services and other services	1,500	2,500	2,700
In terms of properties leasing services	250	250	250
Amounts Payable by the Group to the ACC Group			
In terms of ground support services and other services	1,400	1,500	1,600

Note: In terms of the Passenger Aircraft Cargo Business and the property leasing services provided by the Group to the ACC Group, as the terms of which will exceed three years, the Company will re-comply with the relevant requirements of the Hong Kong Listing Rules (including setting annual caps, issuing announcements and/or obtaining shareholders' approval) prior to the expiration of the 2022 ACC Framework Agreement.

Amounts Payable by the ACC Group to the Group

In arriving at the annual caps for the transportation fees of the Passenger Aircraft Cargo Business payable by the ACC Group to the Group for each of the three years ending 31 December 2024, the Company has considered, among other things, the historical transaction amounts and the following factors:

(i) In terms of income, based on the historical contracting operation income of passenger aircraft bellyhold space cargo business of the Company, it is estimated that the Company's income from the Passenger Aircraft Cargo Business for the year 2022 will not exceed RMB14.0 billion (i.e. not exceeding the revised annual cap of the contracting operation income of passenger aircraft bellyhold space cargo business for the year 2022 which was approved by the Independent Shareholders at the general meeting held on 30 December 2021). Moreover, having considered that the Passenger Aircraft Cargo Business will be expanded to include the subsidiaries of the Company, the estimated income of the Passenger Aircraft Cargo Business of the Group for the year 2022 is expected to not exceed RMB15.4 billion accordingly. In terms of the operating fee rate, the lower of the historical operating fee rates was used in calculating the annual cap of 2022. A reasonable buffer has also been included in the estimated amount of transportation fees of the Passenger Aircraft Cargo Business to cater for the operating needs from time to time. After taking into account the above factors, it is estimated that the amount of transportation service fee payable by the ACC Group to the Group in respect of the Passenger Aircraft Cargo Business for the year 2022 shall not exceed RMB15.5 billion;

(ii) Based on the estimated amount of transportation service fee in respect of the Passenger Aircraft Cargo Business in 2022, it is assumed that the average annual growth rate in 2023 and 2024 will be 7%. The average annual growth rate of 7% is determined with reference to certain expected indicators of civil aviation development during the "14th Five-Year" period (i.e. the average annual growth rate of civil aviation passenger traffic volume of 5.9% and the average annual growth rate of guaranteed take-offs and landings of 6.5% during the "14th Five-Year" period (2021 to 2025)), while taking into account the expected gradual slowdown of the COVID-19 pandemic in the future and the situations such as the Group's future fleet size and capacity growth.

- In arriving at the annual caps for the 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 2024, the Company has considered, among other things, the historical transaction amounts and the estimated scale of the new business between the Group and the ACC Group from the effective date of the 2022 ACC Framework Agreement to 2024, primarily taking into account the increased demand for flight crew and aircraft and engine maintenance services from Air China Cargo due to its increase in aircraft capacity and for which the Company can provide the corresponding personnel and services. Accordingly, it is expected that the transaction amount for the year 2022 to 2024 may continue to increase. A reasonable buffer is also included to cater for the operating needs from time to time.

- In arriving at the annual caps for the amounts payable by the ACC Group to the Group in connection with the properties leasing services provided by the Group for each of the three years ending 31 December 2024, the Company has considered, among other things, the annual rentals of the properties currently leased by the Group to the ACC Group of approximately RMB170 million and the potential additional rentals from the possible new properties leases projects from 2022 to 2024.

Amounts Payable by the Group to the ACC Group

- In arriving at the annual caps for the 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 2024, based on the review of the historical transaction amounts and the estimation of the transaction amounts in 2022, including as the situation of the COVID-19 pandemic improves, and after taking into account the seasonal factors that affect air transport, it is estimated that the demand for the relevant business of the Group will further increase during the second half of year, as a result, the estimated transaction amounts in relation to ground services (cargo terminal services and airport apron services) will be approximately RMB700 million and the estimated transaction amounts in relation to other services (container and pallet management services and engine leasing services) will be approximately RMB300 million in 2022, hence, the Company intends to continue to set the annual cap for 2022 at RMB1.4 billion (i.e. the annual cap for 2022 which was approved at the general meeting of the Company held on 19 December 2019), and set the annual caps for 2023 and 2024 by assuming an average annual growth rate of 7% in the future. The average annual growth rate of 7% is determined with reference to certain expected indicators of civil aviation development during the "14th Five-Year" period (i.e. average annual growth rate of civil aviation passenger traffic volume of 5.9% and average annual growth rate of guaranteed take-offs and landings of 6.5% during the "14th Five-Year" period (2021 to 2025)), while taking into account the conditions such as expected gradual slowdown of the COVID-19 pandemic and the situations such as the Group's future fleet size and capacity growth.

10. 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 2022 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, the Terms of the Agreement 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 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 as always 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.

11. Hong Kong Listing Rules Implications

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 of the transportation service fees of the Passenger Aircraft Cargo Business payable by the ACC Group under the ACC Transactions is, on an annual basis, higher than 5%, such 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 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.

In respect of properties leasing 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 properties leasing services provided by the ACC Group, during the three years ending 31 December 2022, 2023 and 2024, it is expected that the total amounts payable to the Group for each year are below the de minimis threshold as stipulated under Rule 14A.76(1)(a) of the Hong Kong Listing Rules, and therefore the transaction will be exempted from announcement, annual review and the Independent Shareholders' approval requirement under Chapter 14A of the Hong Kong Listing Rules.

12. Shanghai Listing Rules Implications

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 the ACC Group constitute related 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 of the Company (i.e. the Independent Shareholders).

Therefore, although the ground support services and other services and properties leasing services provided by the Group and the ground support services and other services and properties leasing services provided by the ACC Group are exempted from Independent Shareholders' approval under Hong Kong Listing Rules, they are required to be approved by the Independent Shareholders under the Shanghai Listing Rules.

III. CNACG TRANSACTIONS

Reference is made to the announcement of the Company dated 30 October 2019 in relation to, amongst others, the CNACG Transactions. The current term of the CNACG Framework Agreement will expire on 31 December 2022. As the Company expects that the CNACG Transactions will continue to be conducted after 31 December 2022, on 20 September 2022, the Company proposed to renew the CNACG Framework Agreement with CNACG for a term of three years commencing from 1 January 2023 to 31 December 2025.

1. 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. As at the Latest Practicable Date, the State-owned Assets Supervision and Administration Commission of the State Council is a controlling shareholder and de facto controller of CNAHC. CNAHC primarily operates all the state-owned assets and state-owned equity interests invested by the State in CNAHC and its invested entities, aircraft leasing and aviation equipment and facilities maintenance businesses.

2. Description of the CNACG Transactions

The CNACG Transactions contemplated under the CNACG Framework Agreement are as follows:

- **Finance and operating lease services**: CNACG Group will provide finance and operating lease services in respect of, including but not limited to, aircraft, engines, simulators, aircraft-related materials, equipment and vehicles to the Group; the Group will provide finance and operating lease services in respect of, including but not limited to, equipment and vehicles to CNACG Group.

  Set out below are the differences among (i) engines and aircraft-related materials sharing services provided by the ACC Group and the Group to each other, (ii) engines, equipment and vehicle leasing services provided by the CNACG Group to the Group, and (iii) equipment and vehicle leasing services provided by the Group to the CNACG Group:

  - The engines and aircraft-related materials sharing services provided by the ACC Group and the Group to each other represent the short-term sharing of engines or aircraft-related materials (mainly high-price rotables) by one party to the other according to its temporary needs during the daily operation, generally for a relatively short period (mainly around three months);

  - The engines, equipment and vehicle leasing services provided by the CNACG Group to the Group represent the leasing of engines, equipment (mainly airborne media equipment and baggage handling equipment) or vehicles by a subsidiary of CNACG specialising in leasing business to the Group under finance lease or operating lease for a leasing term of one year or above in general; and

  - The Group provides relatively few equipment and vehicle leasing services to the CNACG Group, which include the leasing of catering trolleys by the Group to the CNACG Group according to the needs of CNACG Group from time to time for a leasing term of one year or above in general.

- **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.

In particular, the services provided by the CNACG Group to the Group from time to time mainly include the ground support services, aircraft maintenance services, property investment and management services, ticket and tourism services, logistics services, administrative management services, cleaning and washing services and resident security services, while the services provided by the Group to the CNACG Group from time to time mainly include the aircraft repair services, lounge supplies procurement services and aircraft material procurement services.

3. 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:

  (i) Follow the government pricing or guide price if it is available, including but not limited to the guidance from the Civil Aviation Administration of China (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). Generally, CAAC and the International Air Transport Association will publish the guidance on their official websites from time to time (for the International Air Transport Association, the guidance may also be provided by selling to customers).

  (ii) If no government pricing or guide price is available, the final transaction price shall 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.

(iii) 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 regarding the 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 less favourable than 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 favourable than those provided by the Group to the independent third parties (with regards to the rendering of services by the Group). The Group generally may gain understanding on the historical average prices of the reasonable profit margin of similar products or services of the relevant industry by engaging third-party professional institutions or making its own enquiries through channels such as available data resources (e.g. Bureau van Dijk (BVD) and other large-scale databases) and the official websites of other listed companies. Besides, prior to entering into individual CNACG Transactions, the Group will request the CNACG Group to provide and hence obtain the terms of similar and comparable transactions between the CNACG Group and independent third parties whenever possible as its reference for determining the transaction price. While making reference to the profit margin of comparable products and services disclosed by other listed companies, the Group will try to acquire comparable data as more as possible, and generally by referring to at least two listed companies' relevant data where practicable.

4. The Term of the CNACG Framework Agreement

The renewal of the CNACG Framework Agreement is subject to the approval of Independent Shareholders at the EGM. If the approval of Independent Shareholders is obtained, the CNACG Framework Agreement will be renewed for a term of three years commencing from 1 January 2023 to 31 December 2025. Upon the expiry of such terms, the CNACG Framework Agreement is automatically renewable for successive terms of three years, subject to the fulfilment of requirements under the Hong Kong Listing Rules/Shanghai Listing Rules and obtaining the required approval. Before expiry of the term of the CNACG Framework Agreement, the Board will re-assess the terms and conditions of the 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 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 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 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 12 years. The Independent Financial Adviser has analysed the above lease terms. For details, please refer to the letter from the Independent Financial Adviser of this circular.

5. Reasons for and Benefits of the CNACG Transactions

In respect of the leasing business as a whole, 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 respect of the aircraft finance lease business, certain subsidiaries of CNACG Group, to be acting as the lessors, are 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 addition, the business team of CNACG Group has extensive experience in aircraft leasing and has a better understanding of the Group's business needs. Therefore, the communications of business between the Company and CNACG Group tend to be smoother and it will be easier for to reach an agreement in the best interests of both parties in the stage of negotiation. In terms of the aircraft finance lease, the Company expects that through adopting aircraft finance lease under the CNACG Framework Agreement with CNACG Group, the estimated total savable 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$27.64 million, US$31.32 million and US$33.12 million, respectively for each of the years from 2023 to 2025.

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.

6. Actual Amounts and Existing Annual Caps

The table below sets out (i) the annual caps of the Group for the three years ended/ending 31 December 2020, 2021 and 2022; and (ii) the actual aggregate amounts paid by the Group for each of the two years ended 31 December 2020 and 2021 and for the six months ended 30 June 2022, and the estimated aggregate amounts payable for the year ending 31 December 2022.

Unit: RMB million

	Actual Historical Amounts			Estimated Future Amounts	Existing Annual Caps		
	For the year ended 31 December 2020	For the year ended 31 December 2021	For the six months ended 30 June 2022	For the year ending 31 December 2022	For the year ended 31 December 2020	For the year ended 31 December 2021	For the year ending 31 December 2022
Total value of right-of-use assets in relation to the finance and operating leases entered into by the Group as lessee	1,959	3,526	1,032	9,140	14,500	16,000	16,500
Amounts payable/paid to CNACG Group by the Group for ground support services and other services	111	91	51	553	600	696	807

The reasons for the lower utilization rate of the historical annual caps were: under the influence of the COVID-19 pandemic, the Company's existing aircraft orders were delayed in delivery, and the demand for the operating lease business of production and operation supporting equipment shrank or the arrangement was suspended, thus leading to lower utilization rate of the transaction annual caps for the finance and operating lease services. Also affected by the COVID-19 pandemic, the procurement of products and services related to the flights and passenger traffic declined due to the decrease of capacity of the Group (especially the relevant flights of the Group involving Hong Kong), which also resulted in lower utilization rate of the transaction annual caps for the ground support services and other services.

7. Proposed Annual Caps and Basis of Determination

The table below sets out the proposed annual caps for the relevant transactions of the Group below for each of the three years ending 31 December 2023, 2024 and 2025, respectively:

Unit: RMB million

Transactions	Proposed Annual Caps For the year ending 31 December 2023	For the year ending 31 December 2024	For the year ending 31 December 2025
Total value of right-of-use assets in relation to the finance and operating leases entered into by the Group as lessee	14,000	16,500	17,500
Annual rental fee for operating leases not accounted for as right-of-use assets provided by CNACG Group	100	140	220
Amounts payable to CNACG Group by the Group for ground support services and other services	750	800	850

In arriving at the annual caps of the total value of right-of-use assets in relation to the finance and operating leases entered into by the Group as lessee above, the Company has considered the following factors:

- Of the estimated total value of right-of-use assets in relation to the finance and operating leases entered into by the Group as lessee, about 95% is the value of right-of-use assets in relation to the finance lease of aircraft and other assets. When estimating the total value of right-of-use assets in relation to the aircraft finance lease in the following three years, the Company has considered the followings: (i) historical transaction amounts; (ii) it is assumed that 50% of the total amount of aircraft to be introduced during the period from 2023 to 2025 by the Company with no funding arrangements will be introduced by way of finance lease with CNACG Group, and it is expected that the number of aircraft delayed due to the COVID-19 pandemic will be delivered under the finance lease entered into by the Group in 2020 and 2021 within the next three financial years ending 31 December 2025, and the principal amount of the relevant finance lease is estimated accordingly; (iii) considering that the lease term of each leased aircraft is expected to be ten to twelve years, the market quoted interest rate (LPR) for loans of more than five years was used as the interest rate for calculating the interest of the aircraft finance lease transactions; (iv) according to the information currently available to the Group, CNACG Group is expected not to charge the Group the finance lease arrangement fees in the next three years, thus no arrangement fees considered when estimating the annual cap amount; (v) the Company's incremental borrowing rate is adopted as the discount rate; and (vi) it is assumed that the exchange rate of RMB against USD dollars ranges from 6.5 to 7.2:1.

- About 5% of estimated total value of right-of-use assets in relation to the 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 leases in the following three years (based on information currently available to the Company, the Group may lease 2 to 4 used engines, 3 back-up engines and 8 equipment from CNACG Group in each of the three years from 2023 to 2025, respectively); and (iii) the operating lease price and terms of the same or similar assets in domestic market (for example, for a heavy aircraft tractor, 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).

- A reasonable buffer is included to cater for the Group's business needs from time to time.

- Based on the above, the Company expected that for the three years ending 31 December 2025, the total annual rental fee paid to CNACG Group throughout the lease term for the finance lease business entered into (as set under the Shanghai Listing Rules) will not exceed RMB15 billion, RMB17 billion and RMB18 billion each year, respectively; and the total annual rental fee paid to CNACG Group throughout the lease term for the operating lease business entered into (as set under the Shanghai Listing Rules) will not exceed RMB500 million, RMB700 million and RMB800 million each year, 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 the right-of-use assets under the finance and operating leases entered into by the Group as the lessee for the three years ending 31 December 2025 will be approximately RMB14 billion, RMB16.5 billion and RMB17.5 billion, respectively.

In arriving at the above annual caps of annual rental fee payable by the Group to the CNACG Group in relation to the operating leases not accounted for as right-of-use assets, the Company has considered, among other things, the historical transaction amounts and the following factors:

- the operation condition of the Group's engines, simulators, and equipment and the Group's commercial demand for operating leases in the following three years. The Group's annual rental fees paid for the lease with the CNACG Group that were not accounted for as right-of-use assets in the past were mainly related to some sporadic and temporary leases of engines and equipment, with an annual rental fee of approximately RMB25 million. As mentioned above, the Group may lease 2 to 4 used engines, 3 back-up engines and 8 equipment from the CNACG Group in each of the three years from 2023 to 2025, respectively. As the Group has not yet determined whether to adopt long-term leases of over 1 year (in this case, the leased assets will be accounted for as right-of-use assets) or short-term leases for the lease of such engines and equipment, the Company has also set the annual caps for the rental fees of operating leases not accounted for as right-of-use assets to ensure that the transaction amounts of such leases will be governed by corresponding annual caps regardless of the lease method. The Group will determine the lease method based on the actual business needs, taking into account the respective rental quotations for long-term and short-term leases and the financial impact on the Group. Based on the above, the Company expected that for the three years ending 31 December 2025, the annual rental fee of operating leases for engines, simulators and equipment not accounted for as right-of-use assets will be RMB59 million, RMB137 million and RMB217 million, respectively; and

- On the basis of the above estimated transaction amount, a reasonable 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 above annual caps of amount payable by the Group to the CNACG Group in relation to the ground support services and other services provided by the CNACG Group, the Company has considered, among other things, the historical transaction amounts and the following factors:

- Based on the research on the Group's business needs, it is expected that the trend of the COVID-19 pandemic will slow down in the future, and the Group will increase its capacity, including the resumption of flights related to Hong Kong. As such, the ground support services and other services provided by the CNACG Group to the Group is expected to increase accordingly for the year of 2023, and it is estimated that the transaction amount payable to the CNACG Group by the Group for such services will not exceed RMB683 million. On this basis, a reasonable buffer is added to cater for the Group's business needs from time to time, therefore the annual cap for the transaction amount for 2023 is set at RMB750 million; and

- Based on the above annual cap for 2023, assuming that the transaction amount will grow at a rate of approximately 7% in 2024 and 2025, with a reasonable buffer rounded to the nearest integer to meet the Group's business needs from time to time, the annual caps on transaction amount for 2024 and 2025 are set at RMB800 million and RMB850 million respectively. The average annual growth rate of 7% is based on certain estimated indicators of civil aviation development during the "14th Five-Year" period (i.e, the average annual growth rate of civil aviation passenger traffic of 5.9% and the average annual growth rate of guaranteed take-offs and landings of 6.5% during the "14th Five-Year" period (2021 to 2025)), taking into account the gradual slowdown of the COVID-19 pandemic and the situations such as the Group's future fleet size and capacity growth.

8. 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 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 subdivision 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, term of agreement 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 independent auditor of the Company and the independent non-executive Directors will conduct an annual review on the continuing connected transactions of the Group.

9. Hong Kong Listing Rules Implications

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 services 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 the operating lease not accounted for as right-of-use assets provided by the CNACG Group, as the highest applicable percentage ratio in respect of the proposed annual caps of the rental fee payable by the Group is, on an annual basis, higher than 0.1% but less than 5%, these transactions are 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 ground support services and other services provided by CNACG Group, as the highest applicable percentage ratio in respect of the proposed annual caps of the amounts payable by the Group is, on an annual basis, higher than 0.1% but less than 5%, these transactions are 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 finance and operating lease services provided by the Group to CNACG Group, for each of the three years ending 31 December 2023, 2024 and 2025, 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 the ground support services and other services provided by the Group to CNACG Group, for each of the three years ending 31 December 2023, 2024 and 2025, 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 transactions will be exempt from the announcement, annual review and Independent Shareholders' approval requirements under Chapter 14A of the Hong Kong Listing Rules.

10. Shanghai Listing Rules Implications

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 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 of the Company (i.e. the Independent Shareholders).

Therefore, although the ground support and other services provided by the CNACG Group are exempted from Independent Shareholders' approval under Hong Kong Listing Rules, they are required to be approved by the Independent Shareholders under the Shanghai Listing Rules.

IV. PROPOSED ENTERING INTO OF THE SUPPLEMENTAL AGREEMENT

Reference is made to the announcement dated 28 August 2020 and the circular dated 14 September 2020 of the Company in relation to, among other things, the CNAHC Financial Services Agreement entered into between CNAF (being a subsidiary of the Company) and CNAHC and the Trademark License Framework Agreement entered into between the Company and CNAHC. Reference is made to the announcement dated 29 October 2021 and the circular dated 12 November 2021 of the Company in relation to the Comprehensive Services Framework Agreement entered into between the Company and CNAHC and the Properties Leasing Framework Agreement entered into between the Company and CNAHC.

As Air China Cargo intends to apply for the initial public offering and listing of A shares, according to the relevant requirements under the "Administrative Measures for Initial Public Offering and Listing" issued by the CSRC, Air China Cargo shall maintain independence from CNAHC and enter into a framework agreement with the Company separately. Therefore, the Company entered into the Supplemental Agreement with CNAHC, Air China Cargo and CNAF on 20 September 2022, pursuant to which:

(i) Since the effective date of the separate agreement entered into between Air China Cargo and the Company or CNAF, CNAHC Group no longer represents Air China Cargo or ACC Group in the corresponding framework agreements entered into between CNAHC and the Company or CNAF, and the CNAHC Financial Services Agreement, the Trademark License Framework Agreement, the Comprehensive Services Framework Agreement and the Properties Leasing Framework Agreement (together the "**Relevant CNAHC Group Framework Agreements**") no longer govern the relevant transactions between the Group and ACC Group (the "**Relevant ACC Group Transactions**"), and Air China Cargo will, as an independent entity, enter into the relevant connected transaction agreements with the Company and CNAF separately (the "A**CC Framework Agreements**");

(ii) Unless otherwise approved at the general meeting of the Company, during the term of each of the Relevant CNAHC Group Framework Agreements, the sum of the actual transaction amount of the Relevant ACC Group Transactions that were originally regulated by the Relevant CNAHC Group Framework Agreements and then by the ACC Framework Agreements, plus the actual transaction amount between the Group or CNAF and CNAHC Group (excluding the Group and ACC Group) under each of the Relevant CNAHC Group Framework Agreements after this Supplemental Agreement takes effect shall not exceed the corresponding annual cap of the transaction amount under the Relevant CNAHC Group Framework Agreements approved at the general meeting of the Company, and as far as the Company or CNAF is concerned, the transaction conditions of the ACC Framework Agreements shall be no less favorable than those under the original corresponding Relevant CNAHC Group Framework Agreements; and

(iii) The Supplemental Agreement shall take effect upon (1) stamped by all parties and signed by their authorized representatives; and (2) considered and approved at the general meeting of the Company, the general manager's office meeting of CNAHC, the board meeting of CNAF and the general meeting of Air China Cargo.

Save for the aforementioned amendments, other terms (including the pricing policies) of the Relevant CNAHC Group Framework Agreements and the respective annual caps for the transactions thereunder remain unchanged. In order to comply with the above provisions under the Supplemental Agreement, the Company will continue to monitor to ensure that during the validity period of the Relevant CNAHC Group Framework Agreements, the actual transaction amount of the Relevant ACC Group Transactions plus the actual transaction amount of the remaining transactions under the Relevant CNAHC Group Framework Agreements do not exceed the existing annual caps under each of the Relevant CNAHC Group Framework

Agreements, therefore, the annual caps for the remaining transactions under the CNAHC Group Framework Agreements are not increased as a result of the signing of the Supplemental Agreement. Based on the above, the signing of the Supplemental Agreement does not substantially change the Relevant CNAHC Group Framework Agreements' governing of the transactions contemplated thereunder, and the Supplemental Agreement does not constitute material amendment to the terms of the Relevant CNAHC Group Framework Agreements. Nevertheless, out of prudence, the Company will submit the Supplemental Agreement to the independent shareholders of the Company for consideration and approval of the relevant arrangements thereunder.

As of the Latest Practicable Date, ACC Framework Agreements refer to the 2022 ACC Framework Agreement and the ACC Financial Services Agreement as mentioned below. For details of the 2022 ACC Framework Agreement, please refer to the section headed "ACC Transactions" in this circular. CNAF is expected to enter into a financial services agreement with Air China Cargo (the "**ACC Financial Services Agreement**") for the provision of deposit services, credit services and other financial services by CNAF to Air China Cargo before the end of 2022. The term of the ACC Financial Services Agreement will be until 31 December 2023. For the transactions contemplated under the ACC Financial Services Agreement, (i) the deposits placed by the ACC Group with CNAF are expected to be conducted on normal commercial terms or better, and not to be secured by the assets of the Group, therefore, it is fully exempted under Rule 14A.90 of the Hong Kong Listing Rules; (ii) the credit services and other financial services provided by CNAF will be carried out on normal commercial terms or better, and both of the daily balance of the credit services provided by CNAF to ACC Group and the annual fees to be paid by ACC Group for the other financial services provided by CNAF are expected to fall below the de minimis threshold as stipulated under Rule 14A.76(1)(a) of the Hong Kong Listing Rules. Therefore, the ACC Financial Services Agreement and the transactions contemplated thereunder will be fully exempt from the reporting, annual review, announcement and independent shareholders' approval requirements for connected transactions under Chapter 14A of the Hong Kong Listing Rules. If Air China Cargo and the Group enter into other ACC Framework Agreements in the future, the Company will comply with all applicable requirements under the Hong Kong Listing Rules in a timely manner.

V. EGM

The Company will convene the EGM at 11:00 a.m. on Friday, 14 October 2022 at The Conference Room C713, No. 30, Tianzhu Road, Airport Industrial Zone, Shunyi District, Beijing, the PRC, for the Independent Shareholders to consider and approve the entering into of the 2022 ACC Framework Agreement, the ACC Transactions and the proposed annual caps for the ACC Transactions, the renewal of the CNACG Framework Agreement, the CNACG Transactions and the proposed annual caps for the CNACG Transactions, and the entering into of the Supplemental Agreement. Votes on the resolutions to be considered at the EGM shall be taken by way of poll. A form of proxy is also enclosed herein, and published on the websites of the Hong Kong Stock Exchange (www.hkexnews.hk) and the Company (www.airchina.com.cn). The notice of EGM is reproduced in this circular.

In respect of the ACC Transactions, pursuant to Rule 14A.36 of the Hong Kong Listing Rules, any Shareholder with a material interest in the ACC Transactions is required to abstain from voting on the relevant resolution at the EGM. As at the Latest Practicable Date, CNAHC, the controlling shareholder of the Company, held 45.0018% equity interest in Air China Cargo. CNACG, a substantial shareholder of the Company, is a wholly-owned subsidiary of CNAHC. In addition, Cathay Pacific is a substantial shareholder of the Company and Air China Cargo. Therefore, CNAHC, CNACG, Cathay Pacific and their respective associates are required to abstain from voting on the resolution in respect of the ACC Transactions. As at the Latest Practicable Date, CNAHC and CNACG held an aggregate of 7,508,571,617 shares of the Company (representing approximately 51.70% of the issued share capital of the Company), and controlled or were entitled to control over the voting right in respect of their shares in the Company. Cathay Pacific and its associates held an aggregate of 2,633,725,455 shares of the Company (representing approximately 18.13% of the issued share capital of the Company), and controlled or were entitled to control over the voting right in respect of their shares in the Company.

In respect of the CNACG Transactions, pursuant to Rule 14A.36 of the Hong Kong Listing Rules, any Shareholder with a material interest in the CNACG Transactions is required to abstain from voting on the relevant resolution at the EGM. As at the Latest Practicable Date, CNACG is a substantial shareholder of the Company and a wholly-owned subsidiary of CNAHC. Therefore, CNAHC and CNACG and their respective associates are required to abstain from voting on the resolution in respect of the CNACG Transactions. As at the Latest Practicable Date, CNAHC and CNACG held an aggregate of 7,508,571,617 shares of the Company (representing approximately 51.70% of the issued share capital of the Company), and controlled or were entitled to control over the voting right in respect of their shares in the Company.

In respect of the signing of the Supplemental Agreement, CNAHC, CNACG, Cathay Pacific and their respective associates are required to abstain from voting on the relevant resolutions.

To the best knowledge, information and belief of the Directors, having made all reasonable enquiries, save as disclosed above, no Shareholder has a material interest in the above resolutions or should be required to abstain from voting on the relevant resolutions at the EGM.

The register of members of H Shares will be closed from Tuesday, 11 October 2022 to Friday, 14 October 2022 (both days inclusive), during which no transfer of H Shares will be effected in order to determine the list of holders of H shares of the Company who will be entitled to attend and vote at the EGM. H Shareholders of the Company whose names appear on the H share register of members of the Company after the close of business on Monday, 10 October 2022 are entitled to attend the EGM after completing the registration procedures. In order to qualify for attendance at the EGM, all the transfer documents must be lodged with the Company's H Share registrar, Computershare Hong Kong Investor Services Limited, by 4:30 p.m. on Monday, 10 October 2022.

Whether or not you intend to attend the EGM, you are requested to complete and return the form of proxy in accordance with the instruction printed thereon as soon as possible but in any event not less than 24 hours before the time appointed for convening the EGM or any adjournment thereof. Completion and return of the form of proxy will not preclude you from attending and voting in person at the EGM or at any adjourned meeting thereof should you so wish.

VI. RECOMMENDATION

The Board (including the independent non-executive Directors) considers that the ACC Transactions, 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 proposed annual caps are fair and reasonable and in the interests of the Company and the Shareholders as a whole.

The Board recommends the Independent Shareholders to vote in favour of the 2022 ACC Framework Agreement and the proposed annual caps for the ACC Transactions thereunder, and to vote independently in favour of the renewal of the CNACG Framework Agreement and the proposed annual caps for the CNACG Transactions thereunder. The Board also recommends the Independent Shareholders to vote in favour of the resolution in respect of the proposed entering into of the Supplemental Agreement at the EGM.

Mr. Song Zhiyong, Mr. Ma Chongxian, Mr. Feng Gang, and Mr. Patrick Healy were considered to have material interest in the ACC Transactions and the signing of the Supplemental Agreement, and have abstained from voting on the relevant board resolutions. Mr. Song Zhiyong, Mr. Ma Chongxian, Mr. Feng Gang 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 Director is required to abstain from voting on the relevant board resolutions.

VII. ADDITIONAL INFORMATION

Your attention is drawn to the letter from the Independent Board Committee of this circular which contains its recommendation to the Independent Shareholders as to the voting in relation to the Non-exempt Transactions.

Your attention is also drawn to the letter from the Independent Financial Adviser of this circular, which contains, among other things, its advice to the Independent Board Committee and the Independent Shareholders in relation to the Non-exempt Transactions as well as the principal factors and reasons considered by it in concluding its advice.

Your attention is also drawn to the additional information set out in Appendix I of this circular.

By Order of the Board
Air China Limited
Song Zhiyong
Chairman

Beijing, the PRC

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)

Independent Board Committee:
Mr. Li Fushen
Mr. He Yun
Mr. Xu Junxin
Ms. Winnie Tam Wan-chi

28 September 2022

To the Independent Shareholders of the Company

Dear Sir or Madam,

CONTINUING CONNECTED TRANSACTIONS AND DISCLOSEABLE TRANSACTION

We refer to the circular dated 28 September 2022 issued by the Company to its Shareholders (the "**Circular**") of which this letter forms a part. Terms defined in the Circular shall have the same meanings in this letter unless the context otherwise requires.

On 20 September 2022, the Board approved the entering into of the 2022 ACC Framework Agreement in respect of the ACC Transactions and the proposed annual caps of the transactions contemplated thereunder for the three years ending 31 December 2024 as set out in the Circular, and approved the renewal of the CNACG Framework Agreement in respect of the CNACG Transactions and the proposed annual caps of the transactions contemplated thereunder for the three years ending 31 December 2025. The Non-exempt Transactions are 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.

The terms and the reasons for the entering into of the 2022 ACC Framework Agreement and the renewal of CNACG Framework Agreement are summarised in the Letter from the Board of the Circular.

We have been appointed to form the Independent Board Committee to make a recommendation to the Independent Shareholders as to whether the Non-exempt Transactions are fair and reasonable and whether such transactions are in the interest of the Company and the Shareholders as a whole. Somerley has been appointed as the independent financial adviser to advise the Independent Board Committee and the Independent Shareholders in this regard.

As your Independent Board Committee, we have discussed with the management of the Company the reasons for the Non-exempt Transactions, their terms and the basis upon which the terms have been determined. We have also considered the key factors taken into account by Somerley in arriving at its opinion regarding the above mentioned transactions and their proposed annual caps as set out in the Letter from the Independent Financial Adviser of the Circular, which we urge you to read carefully.

The Independent Board Committee, after taking into account, among other things, the advice of Somerley, considers that the Non-exempt Transactions are conducted on normal commercial terms or on terms no less favourable than those available to independent third parties and are entered into in the ordinary and usual course of business of the Group, are fair and reasonable and in the interest of the Company and the Shareholders as a whole, and that the proposed annual caps under those transactions are also fair and reasonable. Accordingly, the Independent Board Committee recommends the Independent Shareholders to vote in favor of the relevant ordinary resolutions as set out in the notice of the EGM.

Yours faithfully,
Independent Board Committee

Mr. Li Fushen	**Mr. He Yun**	**Mr. Xu Junxin**	**Ms. Winnie Tam Wan-chi**
Independent non-executive Director	*Independent non-executive Director*	*Independent non-executive Director*	*Independent non-executive Director*

The following is the text of a letter of advice from Somerley Capital Limited prepared for the purpose of inclusion in this circular, setting out its advice to the Independent Board Committee and the Independent Shareholders in respect of the Cargo Transactions and the Lease Transactions.

SOMERLEY CAPITAL LIMITED
20th Floor
China Building
29 Queen's Road Central
Hong Kong

28 September 2022

To: The Independent Board Committee and the Independent Shareholders

Dear Sirs,

CONTINUING CONNECTED TRANSACTIONS AND DISCLOSEABLE TRANSACTION

INTRODUCTION

We refer to our appointment to advise the Independent Board Committee and the Independent Shareholders in connection with (i) the transactions relating to the Passenger Aircraft Cargo Business under the 2022 ACC Framework Agreement ("**Cargo Transactions**"); and (ii) the finance and operating leases to be entered into by the Group as lessee with CNACG Group ("**Lease Transactions**") (together, the "**Transactions**"). Details of the aforesaid transactions are set out in the letter from the Board contained in the circular of the Company (the "**Circular**") to its shareholders dated 28 September 2022, of which this letter forms part. Unless otherwise defined, terms used in this letter shall have the same meanings as those defined in the Circular.

As at the Latest Practicable Date, Air China Cargo is owned as to 45.0018% by CNAHC which is a controlling shareholder of the Company holding approximately 51.70% of the issued share capital of the Company. Cathay Pacific is also a substantial shareholder of Air China Cargo and a substantial Shareholder of the Company, and together with its associates, are holding approximately 18.13% of the issued share capital of the Company. Therefore, Air China Cargo is a connected person of the Company as defined under the Hong Kong Listing Rules. Accordingly, the 2022 ACC Framework Agreement and the transactions contemplated thereunder 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 of the transportation service fees of the Passenger Aircraft Cargo Business payable by the ACC Group under the ACC Transactions is, on an annual basis, higher than 5%, such 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.

As at the Latest Practicable Date, CNACG is a substantial Shareholder of the Company and a wholly-owned subsidiary of CNAHC. Therefore, CNACG is also a connected person of the Company defined under the Hong Kong Listing Rules and accordingly, and the renewal of the CNACG Framework Agreement and the transactions contemplated thereunder 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 services 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.

The Independent Board Committee comprising all the independent non-executive Directors, namely Mr. Li Fushen, Mr. He Yun, Mr. Xu Junxin and Ms. Winnie Tam Wan-chi has been established to make a recommendation to the Independent Shareholders as to whether the terms of the Transactions are on normal commercial terms, in the ordinary and usual course of business of the Company and are fair and reasonable and in the interests of the Company and its shareholders as a whole. Somerley Capital Limited has been appointed as the independent financial adviser to advise the Independent Board Committee and the Independent Shareholders in the same regard.

We are not associated or connected with the Company, Air China Cargo, CNAHC, CNACG, Cathay Pacific or their respective core connected persons or associates and, accordingly, are considered eligible to give independent advice on the Transactions. Apart from normal professional fees payable to us in connection with this appointment, no arrangement exists whereby we will receive any fees or benefits from the Company, Air China Cargo, CNAHC, CNACG, Cathay Pacific or their respective core connected persons or associates.

In formulating our advice and recommendation, we have relied on the information and facts supplied, and the opinions expressed, by the Directors and management of the Company (collectively, the "**Management**"), which we have assumed to be true, accurate and complete. We have reviewed information on the Company, including but not limited to, the 2022 ACC Framework Agreement and the renewal of the CNACG Framework Agreement, annual reports of the Company for each of the years ended 31 December 2019 ("**FY2019**") ("**2019 Annual Report**"), 31 December 2020 ("**FY2020**") (the "**2020 Annual Report**") and 31 December 2021 ("**FY2021**") (the "**2021 Annual Report**"), interim report of the Company for the six months ended 30 June 2022 ("**1H2022**") (the "**2022 Interim Report**") and other information contained in the Circular.

In addition, we have relied on the information and facts supplied, and the opinions expressed by the Group and have assumed in relation to the facts to be true, accurate and complete in all material aspects and in relation to any opinions to be honestly held at the time they were made and will remain, in relation to the facts to be true, accurate and complete in all material aspects and in relation to any opinions to be honestly held, up to the date of the EGM. We have also sought and received confirmation from the Group that no material facts have been omitted from the information supplied by them and that their opinions expressed to us are not misleading in any material respect. We consider that the information we have received is sufficient for us to formulate our opinion and recommendation as set out in this letter and have no reason to believe that any material information has been omitted or withheld, nor to doubt the truth or accuracy of the information provided to us. We have, however, not conducted any independent investigation into the businesses and affairs of the Group, Air China Cargo, CNAHC, CNACG, Cathay Pacific, nor have we carried out any independent verification of the information supplied.

PRINCIPAL FACTORS AND REASONS CONSIDERED

In formulating our opinion and recommendation with regard to the Transactions, we have considered the following principal factors and reasons:

1. Information on the parties

The Group

The Company is incorporated in the People's Republic of China with limited liability, the Shares of which have been listed on the Main Board of the Hong Kong Stock Exchange since 15 December 2004. The Group is principally engaged in the provision of air passenger transportation, freight transportation, postal transportation and maintenance services in Mainland China, Hong Kong, Macau and other international regions.

According to the 2021 Annual Report, the Group reported a revenue of approximately RMB74.5 billion, representing a year-on-year increase of approximately 7.23%, which was mainly attributable to, amongst others, the remarkable increase in the Group's air cargo and mail revenue for FY2021 by around 29.9% to approximately RMB11,113 million, as compared with that for FY2020. As reported in the 2022 Interim Report, a further growth of around 50.4% in the Group's air cargo and mail revenue to approximately RMB6,880 million for the six months ended 30 June 2022 was recorded as compared to the corresponding period in 2021. The Group has reported a consistent loss attributable to shareholders of the Company of approximately RMB14.4 billion and RMB16.6 billion for each of FY2020 and FY2021 as compared with profit attributable to shareholders of the Company of approximately RMB7.2 billion, RMB7.4 billion and RMB6.4 billion for each of the three financial years ended FY2019. Consistent loss attributable to shareholders of the Company of approximately RMB19.4 billion and approximately RMB6.8 billion for each of 1H2022 and for the six months ended 30 June 2021 was also reported in the 2022 Interim Report.

As disclosed in the 2021 Annual Report, the Group recorded a total of around 1.59 million safe flight hours. This was comparable to the safe flight hours of approximately 1.553 million reported for FY2020. In addition, the volume of cargo and mail carried amounted to around 1,186.70 thousand tonnes, which represented a year-on-year increase of around 6.56%. Based on the 2021 Annual Report, the Group introduced 43 aircrafts during 2021, among which 29 were acquired under finance leases and 14 were acquired under operating leases. As at 31 December 2021, the Group had a total of 746 passenger aircraft including business jets, with an average age of 8.23 years. Among the aircraft, the Company operated a fleet of 467 aircraft in total, with an average age of 8.39 years.

As disclosed in the 2022 Interim Report, the Group recorded 0.508 million safe flight hours, which represented a decline of approximately 40.9% as compared to that for the interim period ended 30 June 2021. During 1H2022, the volume of cargo and mail carried decreased by approximately

18.98% to approximately 486,513.58 tonnes. Based on the 2022 Interim Report, the Group introduced a total of 16 aircrafts during 1H2022. As at 30 June 2022, the Group had a total of 748 aircraft and the Company operated a fleet of 472 aircrafts.

As at 31 December 2021, major subsidiaries of the Company are Shenzhen Airlines Company Limited (including Kunming Airlines Company Limited), Air Macau Company Limited, Beijing Airlines Company Limited, Dalian Airlines Company Limited, Air China Inner Mongolia Co., Ltd., Aircraft Maintenance and Engineering Corporation, Air China Import and Export Co., Ltd., Chengdu Falcon Aircraft Engineering Service Co., Ltd., and Air China Shantou Industrial Development Company. Associates of the Company are Cathay Pacific Airways Limited, Shandong Airlines Co., Ltd. and Tibet Airlines Co., Ltd. As also disclosed in the 2021 Annual Report, against the backdrop of anti-pandemic work worldwide, the Company made full use of the resources of route network and among other actions, the Company adjusted the structure of transport capacity on the account of domestic macro-circulation and grasped market opportunities to expand domestic supply which resulted in the domestic capacity measured by seat kilometres for 2021 to increase by approximately 7.66% year-on-year. During 2021, the Company also newly launched domestic routes such as Beijing Capital-Aksu-Tumushuke and Beijing Daxing-Quzhou; the Chengdu newly launched domestic routes such as Chengdu Shuangliu-Fuyang and Chengdu Tianfu-Beihai; and the Shanghai newly launched domestic routes such as Shanghai Pudong-Zhengzhou and Shanghai Pudong-Zhanjiang. The Company also newly launched international and domestic routes such as Changchun-Frankfurt, Tianjin-Nanning, Wuhan-Ningbo and Hangzhou-Zhongwei.

Air China Cargo

Air China Cargo was established in 2003. Headquartered in Beijing, Air China Cargo takes Shanghai as its main long haul air freighter operation base and is primarily engaged in air cargo and mail transportation. Air China Cargo is held as to 45.0018% by CNACG. CNACG is a wholly-owned subsidiary of CNAHC which is a state-owned company incorporated in the People's Republic of China and the controlling shareholder of the Company. The Company has developed its cooperation relationship with ACC in relation air cargo business respectively since 2003.

CNACG

CNACG is an investment holding company whose principal business 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. CNACG is a substantial Shareholder of the Company and a wholly owned subsidiary of CNAHC.

The CNACG Group has been providing a wide range of aircraft related services to the Group since 2008, including but not limited to, ground support services, aircraft repair and maintenance services, administrative management services as well as finance lease and operating lease services in respect of, among other things, aircrafts, engine, simulator, equipment and vehicles.

2. The Cargo Transactions

2.1 Background of and reasons for the Cargo Transactions

As disclosed in the Circular, the Directors are of the view that the exclusive contracting operation of the Passenger Aircraft Cargo Business under the 2022 ACC Framework Agreement is in the interests of the Group having considered the following factors:

(i) the two-way settlement model of income and expenditure is adjusted to a one way net settlement. This allows for simplification of transactions and procedures and facilitates public understanding;

(ii) instead of conducting estimation at the beginning of year and year-end reviews, revenue recognition of the Group has been adjusted to actual revenue recognition, further ensuring the fairness and independence of transactions; and

(iii) the reward/punishment rate is applied in the operating fee rate, and the industry yield level is used as incentives and restrictive mechanisms, which indicated the fairness of pricing for connected transactions. By enhancing the capacity of the Passenger Aircraft Cargo Business of Air China Cargo, the Company's income from passenger aircraft cargo operation will be increased.

We have discussed and understand from the Management that Air China Cargo has been engaged in the air freighter operation business since 2003 and has been handling the Passenger Aircraft Cargo Business for more than 18 years and based on prior experience, is considered to be equipped with the level of understanding and experience required.

We have further discussed, and we understand from the Company that the Cargo Transactions are, in nature, similar to the bellyhold space business contracting operation transactions under the 2019 ACC Framework Agreement entered into between the Company and Air China Cargo where, among other things, the Company contracted the operation of all bellyhold space business to Air China Cargo and 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 ("**Existing Cargo Transactions**"). We understand the key differences between the Existing Cargo Transactions and the Cargo Transactions include the expansion of bellyhold space coverage from only involving aircrafts operated by the Company to cover also aircrafts operated by its subsidiaries, namely Dalian Airlines Company Limited, Air China Inner Mongolia Co., Ltd., Beijing Airlines Company Limited, Shenzhen Airlines Company Limited and Air Macau Company Limited (list of subsidiaries are to be updated from time to time).

We understand the primary reason leading to the aforementioned adjustment to the operating model was to resolve concerns raised regarding business competition. Based on our discussions, we understand that due to the completion of the transfer of the Company's 51% shareholding interest in Air China Cargo to Capital Holding on 28 December 2018, the Company and its subsidiaries' business including air cargo and mail delivery and cargo forwarding, warehousing and logistics, cargo terminal operations the current business operations which may overlap the business carried out by Air

China Cargo ("**Business Overlap**"). To address such concern with the Business Overlap, the Company entered into the Existing Cargo Transactions under the 2019 ACC Framework Agreement, which is being further fine-tuned and replaced by the 2022 ACC Framework Agreement to expand the scope of the Existing Cargo Transactions to cover the Passenger Aircraft Cargo Business of the Group.

We also understand that under the terms of the Cargo Transactions, the fee settlement mechanism has also been adjusted from bilateral to unilateral to allow efficient settlement calculations. Under this fee settlement mechanism, the Company would collect transportation service fee from Air China Cargo based on actual revenue derived from the Passenger Aircraft Cargo Business after deducting certain operating fee rates payable to Air China Cargo.

On a best-effort basis, we have reviewed and noted from public domain, a comparable company being listed for more than 10 years in Hong Kong with a long-established history, namely China Eastern Airlines Corporation Limited (Stock Code: 670) ("**China Eastern**"), which is engaged in a comparable line of business and geographical coverage also has in place a similar exclusive passenger aircraft bellyhold space contractual operation arrangement ("**China Eastern Cargo Transaction**"). With reference to circular published by China Eastern dated 30 October 2020 ("**2020 China Eastern Circular**"), the China Eastern Cargo Transaction was also executed for reasons, among others, to address industry competition issue between itself and China Cargo Airlines Co., Limited ("**China Cargo Airlines**") and under the China Eastern Cargo Transaction, the fee settlement mechanism was also adjusted from a bilateral arrangement to an unilateral basis.

In view of the above and in light of the long-established cooperation relationship between the Company and Air China Cargo as well as Air China Cargo's proven track record, we agree with the Directors and would consider continuing its existing relationship and to expand on such relationship would allow the Group as a whole to focus on devoting its resources to expanding its air passenger transportation business while being able to engage the support of an industry partner to facilitate growth of its Passenger Aircraft Cargo Business. Furthermore, in view of the China Eastern Cargo Transaction as discussed above, the exclusive arrangement currently proposed under the 2022 ACC Framework Agreement is also considered in line with the general passenger aircraft cargo business operation trend among major domestic airlines.

2.2 Terms of the Cargo Transactions under the 2022 ACC Framework Agreement

<u>Services:</u>	In order to further address the issue of business competition and optimize transaction structure, after friendly negotiation between both parties, the Group and the ACC Group have determined to carry out a long-term collaboration for the Passenger Aircraft Cargo Business under an exclusive operating model. The entire Passenger Aircraft Cargo Business of the Group will be operated exclusively by the ACC Group, and the ACC Group shall undertake the overall responsibilities for transporting the cargos to the consignors with respect to the cargos which are transported through the passenger aircraft.

The term of the exclusive operation of the Passenger Aircraft Cargo Business between the Group and the ACC Group is commencing from the effective date of the 2022 ACC Framework Agreement and ending on 31 December 2034. The commencement date of the term of the exclusive operation of the Passenger Aircraft Cargo Business between the airlines controlled by the Group and the ACC Group shall be subject to the written agreement entered into between such airlines and ACC Group, if otherwise specified. Upon expiry of the exclusive operation term, the parties may determine new exclusive operation term through friendly negotiation.

Pricing terms: During the exclusive operation term, the Group shall charge the ACC Group the transportation service fee regularly in each year. Such transportation service fee shall be determined based on the ACC Group's actual cargo revenue generated from the exclusive operation of the Group's Passenger Aircraft Cargo Business after deducting certain operating fee rate. The specific formulas are as follows:

Transportation service fee = actual revenue from the Passenger Aircraft Cargo Business x (1 – operating fee rate)

Operating fee rate = operation expense rate + reward/punishment rate

Reward/punishment rate = (growth rate of yield level of the Passenger Aircraft Cargo Business of the current year – growth rate of yield level of the cargo business in the industry of the current year) ×50%

Of which:

(1) The actual revenue of the Passenger Aircraft Cargo Business represents the actual cargo revenue generated by ACC Group's exclusive operation of the Group's Passenger Aircraft Cargo Business.

(2) The operation expense rate represents the ratio of operating expenses to actual revenue from the Passenger Aircraft Cargo Business. Operation expenses are determined by the parties through arm's length negotiation primarily based on the operation expenses in the historical years, and with reference to factors such as the price level in the similar market and industry and its variation trend.

(3) In order to enhance the operating results of the exclusive operation of the Passenger Aircraft Cargo Business, both parties decide to apply the reward/punishment rate after negotiation. The basic index of the reward/punishment rate is 50% of the difference between the

yield level growth rate of the Passenger Aircraft Cargo Business and the yield level growth rate of the cargo business in the industry of the current year. The parties may make reasonable adjustments according to the changes in the market environment and the operation direction of the Passenger Aircraft Cargo Business with unanimous consent after negotiation. The rate of 50% is determined by the Company and Air China Cargo through arm's length negotiation with reference to industry practice. The rate of 50% is the same as the relevant ratios of similar transactions of comparable companies in the industry, which will encourage the ACC Group to enhance its capacity of the Passenger Aircraft Cargo Business, thereby boosting operating efficiency of the Group's Passenger Aircraft Cargo Business, and hence the rate is fair and reasonable.

(4) The growth rate of yield level of the Passenger Aircraft Cargo Business of the current year represents the growth rate of yield level of the Passenger Aircraft Cargo Business of the current year generated by ACC Group's exclusive operation of the Group's Passenger Aircraft Cargo Business as compared with that of the previous year.

(5) The growth rate of yield level of the cargo business in the industry of the current year represents the growth rate of the revenue of the cargo business in the industry of the current year as compared with that of the previous year.

(6) The yield level the cargo business represents the cargo revenue divided by the investment amount for the cargo business. The investment amount for the cargo business represents the total available cargo and mail traffic measured by the capacity available for the carriage of the cargo and mail for every route, and the calculation formula of which is Σ (capacity available for the carriage of the cargo and mail of the route multiplied by the distance of the route).

Upon the 2022 ACC Framework Agreement becoming effective, the 2019 ACC Framework Agreement shall be terminated immediately. With respect to the Passenger Aircraft Cargo Business performed between the parties in accordance with the 2019 ACC Framework Agreement and the relevant specific agreement in 2022, both parties agreed that it shall be deemed to have been correspondingly adjusted in accordance with the above-mentioned principles since 1 January 2022.

We have obtained a copy of the 2022 ACC Framework Agreement and reviewed the terms associated with the Cargo Transactions.

Duration

As disclosed in the Letter from the Board of the Circular, the duration for the Cargo Transactions is approximately 12 years commencing from the effective date of the 2022 ACC Framework Agreement to 31 December 2034 (the "**Duration**"). We have discussed with the Management regarding the reasons for the Duration being longer than the three years permitted under Rule 14A.52 of the Hong Kong Listing Rules and, with reference to the letter from the Board in the Circular and based on our understanding:

(i) Air China Cargo intends to apply for the listing of A shares and to comply with the applicable guidelines on initial public offering and listing of shares issued by China Securities Regulatory Commission ("**CSRC**"), the Cargo Transactions having a duration more than three years is necessary for facilitating the potential listing of Air China Cargo;

(ii) entering into of the Cargo Transactions could provide a clear delineation of business and thereby eliminating concerns associated with competition between the Company and Air China Cargo;

(iii) Air China Cargo is the sole service provider for the Passenger Aircraft Cargo Business and in view of the shareholding structure of both the Group and Air China Cargo, it is not practical or commercially sensible for the Company to entrust such services with another party in the PRC as such counterparty would have to have a reasonable business scale to handle the Group's Passenger Aircraft Cargo Business and possible candidates with such business scale would normally be under control of an industry competitor; and

(iv) we consider the practice of having a duration of longer than three years is not uncommon in the industry because we noted that the China Eastern Cargo Transaction is also for a long duration of 12 years.

Having considered the above, we are of the view that the Duration, being longer than three years, is required for the effective operation of the Cargo Transactions and is a normal business practice in the industry.

Transportation Fee

We note that under the terms of the Cargo Transactions, transportation service fee ("**Transportation Fee**") is calculated using the following formula:

Transportation service fee = actual revenue from the Passenger Aircraft Cargo Business x (1 – operating fee rate)

We further note that the input of operating fee rate referred to in the formulae above ("**Operating Fee Rate**") is calculated as the sum of operation expense rate ("**Operating Expense Rate**") and reward/punishment rate ("**Reward/Punishing Rate**").

The Reward/Punishing Rate is based on the following formula:

Reward/Punishment Rate = (growth rate of yield level of the Passenger Aircraft Cargo Business of the current year – growth rate of yield level of the cargo business in the industry of the current year) ×50%

We have discussed with and understand from the Management that in determining the pricing mechanism for the Cargo Transactions, it has referenced the pricing mechanism used in similar transactions entered into by industry players, including that used in the China Eastern Cargo Transaction, and considered the Group's own circumstances as well as the updated market conditions.

In this respect, we have compared the formulae for Transportation Fee against the pricing mechanism used by the China Eastern Cargo Transaction as disclosed in the 2020 China Eastern Circular to ascertain whether the pricing mechanism used by the Company is in line with those adopted by its industry peers. With reference to 2020 China Eastern Circular, we noted that whilst China Eastern has adopted a similar concept, namely transportation service fee = actual income from passenger aircraft cargo business x (1- business fee rates), for the purpose of calculating the amount of transportation service fee payable by China Cargo Airlines under conventional business circumstances under the China Eastern Cargo Transaction, and we note that such formulae, including the plugins therein, are largely similar to that proposed under the Cargo Transactions. We have noted that both formulae are of similar calculation concept primarily with reference to historical revenue derived from the airlines' passenger aircraft cargo business and historical operating expenses.

We further note that in determining the transportation service fee payable, a reward/ penalty factor is also considered for both the Cargo Transactions and the China Eastern Cargo Transactions. The major difference being that under the China Eastern Cargo Transactions, the reward/penalty factor is determined based on comparisons made with revenue growth rate of passenger aircraft bellyhold space cargo businesses of the PRC's three major state-owned airlines, namely China Eastern itself, the Group and China Southern Airlines Company Limited (stock code: 1055) ("**China South**") whereas under the Cargo Transactions, performance is compared with the growth rate of yield level of the Passenger Aircraft Cargo Business and the growth rate of yield level of the cargo business industry published by Civil Aviation Administration of China ("**CAAC**"). We have discussed and understand from the Management that the reference to yield level in this case is considered to be a more specific measurement of performance and efficiency as it measures revenue generated from the Passenger Aircraft Cargo Business per cargo capacity provided. Based on this understanding, we consider the use of the broader industry as a comparison benchmark is reasonable due to its wider industry coverage and hence it would be considered as representative of market conditions. We would also consider measuring reward/punishment in terms of revenue generated per capacity of cargo business provided is reasonable because it is an appropriate measurement of efficiency in cargo space utilisation.

We understand from the Management that the purpose of the Reward/Punishment Rate is to use it as a mean of motivation for and to encourage Air China Cargo to continuously improve its bellyhold space business performance under the Passenger Aircraft Cargo Business such that both the Company as well as Air China Cargo would be able to mutually benefit. Based on the disclosures in the letter from the Board of the Circular, the rate of 50% used in the formulae for the purpose of calculating the Reward/Punishment Rate is determined by the Company and Air China Cargo through arm's length negotiation with reference to industry practice. In light of the fact that the Reward/Punishment Rate would also benefit the Group and the fact that a similar concept, including the adoption of the rate of 50% in the formulae, was also adopted by China Eastern, we would consider inclusion of this input in the pricing term also reasonable and in line with the market.

We note from the 2020 China Eastern Circular that China Eastern's passenger aircraft cargo business has been categorised into two circumstances, namely conventional business which is the provision of cargo services by utilisation of bellyhold space of passenger aircraft, and the unconventional business which is the provision of cargo services by passenger aircraft which has been temporarily converted solely for the purpose of carrying cargoes (i.e. a cargo only passenger aircraft). Under the unconventional business circumstances, China Eastern has adopted a slightly different formulae, which involve, among other things, the use of a reasonable profit margin of the three major airlines in the PRC to arrive at the business fee rate, for calculating the transportation service fee, whilst the Group proposes to use the same formulae for its Passenger Aircraft Cargo Business which essentially covers both the conventional and unconventional scenarios as referred by China Eastern.

In this regard, we have discussed and understand from the Management that from the Group's point of view, both conventional and unconventional scenarios are highly similar as they both involve the transportation of cargo using bellyhold spaces available on passenger aircrafts, and that as disclosed in the 2020 China Eastern Circular, one of the key reasons provided by China Eastern for the differences in formula used for the calculation of transportation service fee payable under such two scenarios was that, in the case of unconventional business described above, there were no relevant historical data available to be taken as a reference for calculation of revenue growth rate for the calculation of the "business fee rates". Taking into account of the background of the pricing mechanism used for the China Eastern Cargo Transactions and considering the circumstances under which Cargo Transactions are entered into, we consider the Management's view to consider all passenger aircraft cargo related transactions as one business unit and is equivalent to that of the "conventional business" described in the China Eastern Cargo Transaction is not without basis because (i) based on our review of the information provided and our discussion with the Management, we consider both the conventional and unconventional businesses described in the China Eastern Cargo Transactions, being whether or not the passenger aircraft has been converted for better use of empty bellyhold spaces such that cargo businesses as a whole can be carried on during the COVID-19 pandemic, do indeed appear to be of the same nature; and (ii) in view of (i), a separate formulae would not be considered necessary, particularly, unlike the China Eastern Cargo Transaction the pricing of which was first determined in 2020, being at the earlier stage of the COVID-19 pandemic where historical data for calculation of revenue growth rate for the purpose of the "business fee rates" have yet been available, currently more relevant historical revenue growth rate data have however become available since the outbreak of the COVID-19 pandemic almost three years ago.

In light of the above, we consider that the pricing term of the Cargo Transactions, namely the calculation methodology for the Transportation Fee outlined above is, as a whole, fair and reasonable.

2.3 Historical amounts and historical caps and the proposed annual caps

The table below sets out (i) the annual caps of amounts relating to the Existing Cargo Transactions for each of the three years ended/ending 31 December 2020, 2021 and 2022; and (ii) the actual transacted amounts relating to the Existing Cargo Transactions for each of the two years ended 31 December 2020 and 2021 and for 6 months ended 30 June 2022.

	Historical transacted amounts			Historical caps		
	For the year ended 31 December		For 6 months ended 30	For the year ended/ ending 31 December		
Existing Cargo Transactions	**2020**	**2021**	**June 2022**	**2020**	**2021**	**2022**
			(in millions of RMB)			
In terms of contracting operation income of passenger aircraft bellyhold space cargo business	7,685	10,491	6,656	8,000	11,000	14,000
In terms of operation expenses of bellyhold space	351	609	351	800	960	1,160

With reference to the table above, we note that the utilisation rate for the annual caps relating to contracting operation income of bellyhold space business under the Existing Cargo Transactions for each of FY2020 and FY2021 was approximately 96.1% and 95.4% respectively. We note that the Company has revised annual caps for FY2021 and for the year ending 31 December 2022 ("**FY2022**") for the contracting operation income of bellyhold space business under the Existing Cargo Transactions in December 2021. Based on the circular of the Company dated 14 December 2021, the annual cap for FY2022 in respect of the contracting operation income of the bellyhold space business under the Existing Cargo Transactions, which is in essence the expected revenue from the bellyhold space business relating to the aircrafts operated by the Company, was RMB14,000 million.

Also with reference to the table above, we note that the utilisation rate for the annual caps relating to the operation expenses of bellyhold space was approximately 43.9% and 63.4% respectively for each of FY2020 and FY2021. We have discussed and understand from the Management that relatively lower utilisation rate for the annual cap relating to operation expenses of bellyhold space for each of FY2020 and FY2021 was due to the decline in flights operated by the Company as a result of COVID-19 pandemic and hence less operation expense incurred for the purpose of operating the bellyhold space business. We note from the disclosures in the 2019 Annual Report, the 2020 Annual Report and the 2021 Annual Report that the number of flights operated by the Group declined to 551,373 for FY2020 and 572,264 for FY2021, as compared with pre-Covid-19 pandemic levels of 710,037 in FY2019 and 742,923 for the year ended 31 December 2018 ("**FY2018**"). The Management further elaborated that the reduced number of flights operated by the Company did not impact income generated from the bellyhold space business in FY2020 and FY2021 because demand for transportation of cargo in terms of tonnage have not substantially reduced during such periods.

As a whole, we understand the primary reason for the Company's proposal to revise the annual cap for FY2022 is to reflect the changes in business structure and settlement mechanism as described in the section headed "2.1 Background of and reasons for the Cargo Transactions" above.

As disclosed in the letter from the Board in the Circular, after the 2022 ACC Framework Agreement becoming effective, the 2019 ACC Framework Agreement shall be terminated. Factoring in the changes to the Existing Cargo Transactions as discussed in the section headed "2.1 Background of and reasons for the Cargo Transactions" above, including the expansion of coverage scope and payment settlement mechanism, the Company has proposed the following revised annual caps relevant to the Cargo Transactions for FY2022 and proposed the following annual caps for each of the two years ending 31 December 2023 ("**FY2023**") and 2024 ("**FY2024**") respectively:

Cargo Transactions	**Proposed annual caps for the year ending 31 December**		
	2022	**2023**	**2024**
	(in millions of RMB)		
In terms of the transportation service fees of the Passenger Aircraft Cargo Business payable by the ACC Group to the Group	15,500	17,000	18,000

As disclosed in the letter from the Board in the Circular, in arriving at the annual caps for the Transportation Fees payable by the ACC Group for each of the three years ending 31 December 2024, the Company has considered, among other things, the historical transaction amounts and the following factors:

(i) in terms of income, based on the historical contracting operation income of passenger aircraft bellyhold space cargo business of the Company, it is estimated that the Company's income from the Passenger Aircraft Cargo Business for the year 2022 will not exceed RMB14.0 billion (i.e. not exceeding the revised annual cap of the contracting operation income of passenger aircraft bellyhold space cargo business for the year 2022 which was approved by the Independent Shareholders at the general meeting held on 30 December 2021). Moreover, having considered that the Passenger Aircraft Cargo Business will be expanded to include the subsidiaries of the Company, the estimated income of the Passenger Aircraft Cargo Business of the Group for the year 2022 is expected to not exceed RMB15.4 billion (the "**Revised Expected Income**") accordingly. In terms of the operating fee rate, the lower of the historical operating fee rates was used in calculating the annual cap of 2022. A reasonable buffer has also been included in the estimated amount of transportation fees of the Passenger

Aircraft Cargo Business to cater for the operating needs from time to time. After taking into account the above factors, it is estimated that the amount of transportation service fee payable by the ACC Group to the Group in respect of the Passenger Aircraft Cargo Business for the year 2022 shall not exceed RMB15.5 billion; and

(ii) based on the estimated amount of transportation service fee in respect of the Passenger Aircraft Cargo Business in 2022, it is assumed that the average annual growth rate in 2023 and 2024 will be 7%. The average annual growth rate of 7% is determined with reference to certain expected indicators of civil aviation development during the "14th Five-Year" period (i.e. the average annual growth rate of civil aviation passenger traffic volume of 5.9% and the average annual growth rate of guaranteed take-offs and landings of 6.5% during the "14th Five-Year" period (2021 to 2025)), while taking into account the expected gradual slowdown of the COVID-19 pandemic in the future and the situations such as the Group's future fleet size and capacity growth.

Proposed annual cap for FY2022

Revenue from the Passenger Aircraft Cargo Business

We note that the key input for the estimation of annual cap for the Cargo Transactions for FY2022 is the expected revenue to be derived from the Passenger Aircraft Cargo Business. We have reviewed and discussed the basis and assumptions for estimating the expected revenue from the Passenger Aircraft Cargo Business and we agree with such basis for which it was used because:

(a) based on the circular of the Company dated 14 December 2021, the existing annual cap for FY2022 in respect of the contracting operation income of the bellyhold space business under the Existing Cargo Transactions, which is in essence the expected revenue from the bellyhold space business relating to the aircrafts operated by the Company, was estimated as RMB14,000 million (the "**Previous Income Cap**"). The Previous Income Cap of RMB14,000 million represents around 33.4% increase from the actual historical transacted amount of the contracting operation income of bellyhold space business. In view of (i) the remarkable increase in air cargo and mail demand as discussed in the section headed "1. Information on the parties – The Group" above and as reflected by the increase in the Group's air cargo and mail revenue by approximately 29.9% for FY2021 and 50.4% for 1H2022 as compared with corresponding year/period respectively; and (ii) the increase by approximately 36.5% increase in the actual historical transacted amount of the contracting operation income of bellyhold space business for FY2021 under the Existing Cargo Transactions as compared to that for FY2020, such estimated amount of the Previous Income Cap is not considered excessive. In addition, as discussed in the section headed "2.1 Background of and reasons for the Cargo Transactions", the Cargo Transactions under the 2022 ACC Framework will be expanded to not only cover aircrafts operated by the Company under the Existing Cargo Transactions, but also to cover aircrafts operated by its subsidiaries, namely Dalian Airlines Company

Limited, Air China Inner Mongolia Ltd., Ltd., Beijing Airlines Company Limited, Shenzhen Airlines Company Limited and Air Macau Company Limited. Based on disclosures made in the 2022 Interim Report, we are able to derive that the Company's subsidiaries operated 276 aircrafts, representing roughly 36.9% of the total fleet of the Group. In this respect and against such backdrop, we understand that the Revised Expected Income adopted for estimating the proposed revised annual caps for FY2022, with only a 10% increment as compared to the Previous Income Cap, is considered not excessive; and

(b) as shown in the table above, as at 30 June 2022, approximately 47.5% of the Previous Income Cap, or approximately 43.2% of the Revised Expected Income, has been utilised under the Existing Cargo Transactions.

Operating Fee Rate

Under the terms to the Cargo Transactions, the concept for the Operating Fee Rate is similar to the concept of operating expense relating to the bellyhold space business under the Existing Cargo Transactions. We note that the Company has considered the actual Operating Fee Rate from each of FY2018, FY2019, FY2020 and FY2021 in determining the estimated Operating Fee Rate for the purpose of estimating the annual cap for FY2022. We have reviewed and noted that the Company has adopted the low end of the Operating Fee Rate range from each of the aforementioned financial years.

In assessing the fairness and reasonableness of such adoption of estimated Operating Fee Rate, we have reviewed the historical Operating Fee Rate and noted that it has been relatively steady within a narrow range for periods prior to FY2020. The reported Operating Fee Rate revealed a notable decline in FY2020 and based on our discussion with the Management, this was mainly as a result of the COVID-19 pandemic, which as previously discussed, was a consequence to the reduced number of flights operated by the Company. In view of the continuous uncertainties surrounding the COVID-19 pandemic, we consider using a lower Operating Fee Rate as an input for the estimation of the annual cap to be not unreasonable.

As such, we consider the inputs used by the Company, namely expected revenue from the Passenger Aircraft Cargo Business and Operating Fee Rate for the purpose of estimating the annual cap for FY2022 to be fair and reasonable.

Proposed annual caps for FY2023 and FY2024

Growth in the Group's fleet of aircrafts

We have discussed and understand from the Company that the expected growth in the Passenger Aircraft Cargo Business and in turn, the Transportation Fee, is positively co-related to the growth in the Group's fleet of aircrafts. We also note that the Group have adopted an annual growth rate of roughly 7% in the expected growth in its fleet of aircraft and such growth rate was used for the purpose of estimating the proposed annual caps for Cargo Transactions for each of FY2023 and FY2024.

We have reviewed and noted that due to COVID-19 pandemic, the Company has been postponing/slowing its pace to acquire aircraft and equipment to update and/or replace its existing fleet and portfolio. Nevertheless, the Company has demonstrated its consistent effort in acquiring aircrafts, including but not limited to, the major transaction of aircrafts acquisition conducted in July 2022. As disclosed in the 2021 Annual Report and based on our further understanding from the Management, the Group adheres its growth plans to align with the national and industry developments and formulated its "14^{th} Five-Year Plan" in accordance with the targets set out by the CAAC. The CAAC have, among other targets, set out average annual compounded growth expectations of approximately 17.0%, 17.2%, 7.0% and 9.5% in the areas of traffic, number of passengers carried, cargo and mail carried and flight hours (together, the "**CAAC Targets**") respectively, over the years from 2020 to 2025. In order to meet such CAAC Targets, the Company would need to, among other things, have a sufficient fleet of aircrafts that are up to standards. The Management considers that, should the global COVID-19 pandemic stabilises, the Group would revive its continuous efforts to review its fleet and take more proactive approach to update its existing fleet of aircrafts. In this respect, should the global COVID-19 pandemic stabilises as discussed above, it is expected that the growth rate for the Group's fleet would resume to at least its previous level.

In addition to our discussion with the Management as outlined above, we have independently reviewed the Group's annual reports for the seven years prior to COVID-19 pandemic and noted that the average annual growth of the Group's fleet was approximately 6% and prior to FY2020, the Group has been acquiring on average, 57 aircrafts per year, and phasing out, on average 22 aircrafts per year. We also note that the average age of the Group's fleet prior to COVID-19 pandemic was approximately 6.4 years. However, since the start of the COVID-19 pandemic in 2020, which have had detrimental impacts on the global aviation industry, the planned growth in the size of the Group's fleet has almost halted entirely. In particular, growth in total fleet dropped to approximately 1.1% in FY2020 with the Group acquiring a mere 14 aircrafts during the year and phasing out only 6. Whilst the growth in the Group's total fleet increased to 746 aircrafts in FY2021, however, total acquisition and phasing out of aircrafts were still significantly below pre-COVID-19 pandemic's averages. We also note that the average age of the Group's fleet has also significantly increased to 8.23 years in 2021, which is much higher than the average age of around 6.4 years during the pre-COVID-19 period as mentioned above. Furthermore, based on our research, the Company is currently operating a fleet with relatively higher average age amongst its peers. For the purpose of comparison, we have also reviewed the annual reports of China Eastern and China South and we noted that as at end of 2021, China Eastern operated a fleet of 758 passenger aircrafts with an average fleet age of 7.7 years whilst China South operated a fleet of 878 aircrafts (of which 862 are passenger aircrafts) with an average fleet age of 8 years. As such, we consider that the Group's expected plans to catch up on the updating of its existing aircraft portfolio and the expansion of its fleet size, which were halted as a result of COVID-19 pandemic as discussed above is not unreasonable from in particular, a business perspective so that it would be able to remain competitive to its closest peers and as such, the growth rate used for the purpose of estimating the annual caps for FY2023 and FY2024 is also not without basis.

3. The Lease Transactions

3.1 Background of and reasons for the Lease Transactions

As disclosed in the letter from the Board of the Circular, the Management considers that the entering into of the Lease Transactions 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, in respect of aircraft finance lease business, certain subsidiaries of CNACG, being the lessors, are 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. The business team of CNACG Group also has extensive experience in aircraft leasing and has a better understanding of the Group's business needs. Therefore, communications of businesses between the Company and CNACG Group tend to be smoother and it will be easier for them to reach an agreement in the best interests of both parties in the stage of negotiation. In terms of the aircraft finance lease, the Company expects that through adopting aircraft finance lease under the CNACG Framework Agreement with CNACG Group, the estimated total savable 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$27.64 million, US$31.32 million and US$33.12 million, respectively for each of the years from 2023 to 2025.

We have discussed and understand from the Management that the Lease Transactions entered into with CNACG are broadly divided into two categories, namely finance leases ("**Finance Leases**") and operating leases ("**Operating Leases**"). Whilst there are a number of finance institutions offering aircraft finance lease plans/services, such finance institutions do not necessarily offer operating leases for smaller value equipments such as machinery and equipment designed solely for the aviation industry. We understand the reason for this is because aviation equipment or machinery are usually smaller in transaction value as compared to aircrafts, specific and could even be tailor-made in nature, and such equipment/machinery may not necessarily have a readily available second hand market and as such, independent finance institutions may not be willing to provide the financing options due to the limited market. We however understand from the Management that, other than servicing the specific needs of the Group, CNACG has independent third party clients such as airports, for operating leases involving aviation equipment/machinery.

We noted from the annual reports for FY2019, FY2020 and FY2021 that around 59.08%, 58.56% and 59.79% of the aircraft fleet of the Group were held under either finance lease or operating lease as at 31 December 2019, 31 December 2020 and 31 December 2021 respectively. As such, the renewal of the CNACG Framework Agreement, in particular, in relation to the finance and operating lease services of aircrafts, engines, simulators, equipment and vehicles is considered in line with the Group's financing strategy for its business operation.

Given that (i) members of the CNACG Group possess experience, expertise and have been providing similar services to the Group over the last 6 years, and (ii) not only that the renewal of the CNACG Framework Agreement will continue to allow financing costs saving and financing flexibility for the Group as discussed in the paragraphs above, most importantly, it will not obligate the Group to enter into any transactions with CNACG Group, but will only allow CNACG Group to be one of the available choices for the Group's selection for its finance/operating lease arrangements if the financing terms provided are at a market rate or better, we are of the view that the entering into of the Lease Transactions pursuant to the renewal of the CNACG Framework Agreement is in the ordinary and usual course of business of the Group and is in the interests of the Company and the Shareholders.

3.2 Terms of the Lease Transactions under the CNACG Framework Agreement

Services:	CNACG Group will provide finance lease and operating lease services in respect of, including but not limited to, aircraft, engines, simulators, aircraft-related materials, equipment and vehicles to the Group.
Pricing terms:	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, 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.

We have discussed with and understand from the Management, historical transacted value for Lease Transactions under the CNACG Framework Agreement was predominately relevant to Finance Leases. Before entering into any Finance Leases, the Company would compare the terms, including pricing terms offered by independent third parties so as to ensure that the terms offered by CNACG Group are fair and reasonable, no less favourable compared to independent third parties and on normal commercial terms. We have further discussed with and understand from the Management that before entering into any Operating Leases, it would firstly research into the costs associated with direct purchase of the aviation machinery/equipment it requires ("**Required Aviation Equipment**"). The Company would then compare the outright purchase cost of the Required Aviation Equipment against potential costs of lease associated with entering into an operating lease for the same Required Aviation Equipment. After taking into consideration the commercial factors including business needs, should the Company decide to enter into an Operating Lease for the Required Aviation Equipment, the Company would then either compare the terms offered by CNACG Group with terms offered for similar Required Aviation Equipment already leased by the Company and/or request CNACG Group to provide terms offered by CNACG Group for the same or similar Required Aviation Equipment to its independent third party clients, so as to ensure that the terms offered by CNACG Group in relation to the Required Aviation Equipment are fair and reasonable, no less favourable and on normal commercial terms.

Based on our understanding from the Management, interest rates used for Finance Leases for, among others, aircrafts, is usually with reference to loan market quoted interest rate ("**LPR**") promulgated by the People's Bank of China ("**PBOC**"). We note the LPR for period greater than 5 years is 4.3% as at the Latest Practicable Date. We have also understood from the Management that the period of finance leases for aircrafts would normally exceed three years and usually greater than five years.

We understand from the Management that the Group has entered into similar leasing arrangements with CNACG Group and/or independent third parties from time to time in the past. In this regard, we have requested the Company to provide us with, among other things, 7 samples of leasing transactions with independent third parties from 2020 to 2022 as regards aircraft finance lease ("**Sample Aircraft Finance Leases**") for comparing with transactions with CNACG Group for the same type of the leasing subject. We note from the Sample Aircraft Finance Leases that the relevant lease interest were all determined with reference to the LPR promulgated by the PBOC plus a spread ranged from 1.17% to 2.01%, whilst the terms for such Sample Aircraft Finance Leases ranged between 10-12 years in duration. In this regard, we noted that the Finance Leases for aircraft was in the duration of 10 years and was based on the LPR promulgated by the PBOC with nil handling fee, which compared favourably to the terms of the Sample Aircraft Finance Leases. We further noted from the Sample Aircraft Finance Leases and from our discussion with the Management that the Company would consider, among other factors, whether total cost of borrowing (i.e., the rate offered and other fees involved)) by the lender is considered favourable among the quotes received and whether the amount of financing available to be provided by the lender is sufficient to satisfy the Company's requirements, before entering into any formal lease agreements. Based on the supporting documents relevant to the approval of the Sample Aircraft Finance Leases, we also noted that the Sample Aircraft Finance Leases were jointly reviewed and approved by at least three different departments of the Company.

We have also separately requested for and were provided with 3 previous operating leases which CNACG Group entered into with its independent third party clients ("**Sample Operating Leases**") for comparison purposes. We noted that the payment terms under the Sample Operating Leases are similar to those offered to the Group by CNACG Group. We also noted that rental expenses on a monthly basis for similar equipments charged by the CNACG Group on the Group are lower than those charged on the independent third parties. As with that of Finance Leases, prior to entering into of any Operating Leases, the proposed agreements would be jointly reviewed and approved by at least three different departments of the Company.

Based on the above, we consider that terms of the Lease Transactions are generally in line with the market and such arrangement with CNACG Group is fair and reasonable.

3.3 Historical amounts and historical caps and the proposed annual caps

The table below sets out (i) the annual caps of the Group relevant to the Lease Transactions for FY2020, FY2021 and FY2022; and (ii) the actual aggregate amounts paid by the Group for FY2020, FY2021 and the six months ended 30 June 2022 and the estimated aggregate amounts payable for FY2022.

	Historical transacted amounts				Historical caps		
	For the year ended 31 December		For the six months ended	Estimated annual amount	For the year ended 31 December		
Transactions	**2020**	**2021**	**30 June 2022**	**for 2022**	**2020**	**2021**	**2022**
				(in millions of RMB)			
Total value of right-of-use assets in relation to finance lease and operating lease entered into by the Group as lessee	1,959	3,526	1,032	9,140	14,500	16,000	16,500

We have discussed the basis for its estimated transaction amount for 2022 with the Management and understand it has considered, among others, the actual value of the leases already entered into and expected leases to be entered into with CNACG Group in 2022. We note the utilisation rate of annual caps for each of 2020 and 2021 is approximately 13.51% and 22.04% respectively for the total value of right-of-use assets in relation to Finance Leases and Operating Leases entered into by the Group as lessee. We further understand that the expected utilisation rate for 2022 for the total value of right-of-use assets in relation to Finance Leases and Operating Leases entered into by the Group as the lessee is approximately 55.39%. We have discussed with and understand from the Management that the above relatively lower utilisation rates, especially for 2020 and 2021, were attributable to the effects from the COVID-19 pandemic. Given the value of right-of-use assets in relation to Finance Leases and Operating Leases entered into by the Group as lessee being directly relevant to the number of aircraft introduced by the Group, we have also reviewed the disclosures in the 2019 Annual Report, the 2020 Annual Report and the 2021 Annual Report and noted the fact that the actual number of aircrafts introduced for each of FY2020 and FY2021 fell short by approximately 62% and 27% respectively or an average of approximately 45%.

Nevertheless, the Group has reviewed its business plans for the next three financial years ending 31 December 2025 and the table below sets out the proposed annual caps for the total amount payable to CNACG Group by the Group relating to the Lease Transactions for each of the three years ending 31 December 2023, 2024 and 2025, respectively:

	Proposed Annual Caps for the year ending 31 December		
Transactions	**2023**	**2024**	**2025**
	(in millions of RMB)		
Total value of right-of-use assets in relation to finance lease and operating lease entered into by the Group as lessee	14,000	16,500	17,500

As disclosed in the Circular, the Company considered the following key factors when estimating the total value of right-of-use assets in the following three years in relation to the finance and operating leases entered into by the Group as lessee:

- approximately 95% of the total annual cap for finance lease and operating lease to be entered into by the Group as lessee is attributable to the anticipated total value of right-of-use assets in relation to the finance lease of aircraft and other assets ("**Aircraft Finance Leases PV**"). Based on the disclosures made in the Circular, the total annual rental fee expected to be paid to CNACG Group throughout the lease term for the Finance Leases to be entered into (as set under the Shanghai Listing Rules) for the three years ending 2025 would not exceed RMB15 billion, RMB17 billion and RMB18 billion respectively, which is estimated with reference to, among others, the following key factors:

  (i) the aircraft introduction plan for each of the three years, 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 aircraft scheduled to be introduced during the period from 2023 and 2025 by the Company with no funding arrangements will be introduced by way of finance lease with CNACG Group;

  (ii) the number of aircrafts delayed in 2020 and 2021 as a result of COVID-19 pandemic will be delivered over the next three financial years ending 31 December 2025 under finance leases entered into by the Group;

  (iii) the average lease term of aircraft being 10 to 12 years;

  (iv) the LPR; and

  (v) the Company's incremental borrowing rate of 4.9% as the discount rate.

- About 5% of estimated total value of right-of-use assets in relation to the finance and operating leases entered into by the Group as lessee is the value of right-of-use assets in relation to operating lease. The total value of right-of-use assets in relation to operating leases entered into (as set under the Shanghai Listing Rules) involving engines, simulators and equipment (together "**Aviation Equipment**") for each of 2023, 2024, 2025 of approximately RMB500 million, RMB700 million and RMB800 million respectively, are estimated with reference to, among others, the following key factors:

  (i) the operation condition of the Group's engines, simulators, and equipment and the Group's commercial demand for operating leases in the following three years (based on information currently available to the Company, the Group plans to lease 2 to 4 used engines, 3 back-up engines and 8 equipment from CNACG Group in each of the three years from 2023 to 2025, respectively); and

  (ii) the operating lease price and terms of the same or similar assets in the domestic market (taking a certain kind of heavy aircraft tractor, 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); and

  (iii) an incremental borrowing rate of 4.9% for leases with terms over 5 years and 4.75% for leases with terms ranging from 1 to 5 years as the discount rate.

As also discussed above, in determining the annual caps for the Lease Transactions, the Company has also considered the number of aircrafts, the introduction of which were delayed in prior years due to COVID-19 pandemic, currently expected to be delivered over the next three financial years ending 31 December 2025 under Finance Leases entered into by the Group. We understand from the Management that as a result of the COVID-19 pandemic, a significant number of aircrafts scheduled to be introduced in 2020, 2021 and 2022 were or is expected to be delayed to 2023 and possibly beyond. We have reviewed and discussed with the Management and noted that the total value of the delayed aircrafts accounts for approximately 50%, 40% and 40% of the annual caps (without accounting for the buffer, which is to be discussed below) for each of 2023, 2024 and 2025 respectively.

In addition, we have discussed with and understand from the Management that due to the effects of COVID-19 pandemic, the Company has also been postponing/slowing its pace to acquire aircraft and equipment to update and/or replace its existing fleet and portfolio. Nevertheless, for reasons outlined in the section above headed "2.3 Historical amounts and historical caps and the proposed annual caps – Proposed annual caps for FY2023 and FY2024 – Growth in the Group's fleet of aircrafts", we consider the Group's expected plans to update its existing portfolio of aircrafts which were halted as a result of COVID-19 pandemic is not unreasonable, in particular, from a business perspective so that it would be able to remain competitive to its closest peers and as such, leaving a sufficient portion on buffer when determining the annual cap for the coming three financial years ending 31 December 2025 is also not without basis.

As stated in the Circular, the maximum aggregate principal amount of the Aircraft Finance Lease PV for any particular year, hence transactions with the CNACG Group, shall not exceed half of the aggregate consideration amounts for the total aircraft projected to be added using finance leases during the said year. We have reviewed the Company's 2019 Annual Report, 2020 Annual Report and 2021 Annual Report and noted that the Group introduced 48, 14 and 43 aircrafts respectively for 2019, 2020 and 2021, in which 27, 11, 29 were acquired under finance leases for 2019, 2020 and 2021 respectively. To assess whether the computation process adopted by the Company to account for half of the expected total amount of aircrafts scheduled to be introduced using finance lease as the relevant principal amount is a market norm, we have reviewed and also noted that the Company's peers, China South and China Eastern in their respective continuing connected transaction circulars dated 26 October 2019 and 30 September 2019 also adopted a similar computation process of accounting for 60% and half of the expected total purchase price of total aircrafts scheduled to be introduced as the relevant principal amount respectively.

Similar to previous financial years, pursuant to IFRS 16, the finance leases entered into by the Company as the lessee will be recognised as right-of-use assets and discounted using the Company's incremental borrowing rate, and the result of such calculation is used to determine the annual caps relating to the Lease Transactions. Therefore, the amounts of the Aircraft Finance Leases PV for each of the years 2023, 2024 and 2025 are derived based on the total value of right-of-use assets relating to the aircraft finance leases expected to be entered into between the Company and CNACG Group during 2023, 2024 and 2025 respectively. We have reviewed the computation inputs of the respective values for the right-of-use assets relating to the planned aircraft finance leases and noted that it is calculated by discounting the estimated total financing amount required for new aircrafts (including interest with zero arrangement fees) to be introduced for the particular year by a discount rate of 4.9% (for leases with terms over 5 years) which is equivalent to the Company's prescribed internal incremental borrowing rate for loans/leases over five years. We have reviewed the 2021 Annual Report and noted that the fixed interest rate for the Group's interest-bearing bank and other borrowings ranged from 1.30% to 4.38% (median interest rate being 2.84%), the rate for floating rate bank and other borrowings ranged between 2.66% and 4.65% (median interest rate being 3.66%) and range of interest rates for corporate bonds repayable is from 2.34% to 5.30% (median interest rate being 3.82%). Given the abovementioned ranges and medians of interest rates applicable to the Group's interest-bearing bank loans and other borrowings, and the fact that the internal rate being 4.9% is towards the high end of the aforementioned quoted ranges, we would consider the Company's use of internal rate of 4.9% to be prudent.

In addition to the above, we have also carried out the following independent work and considered the following factors:

(1) we understand from the Management that the finance lease contracts for aircraft is usually between 10 years and 12 years in duration. As mentioned under the paragraph headed "3.2 Terms of the Lease Transactions under the CNACG Framework Agreement" above, we have obtained and reviewed the Sample Aircraft Finance Leases with independent third parties and noted that the duration for the leases were all between 10 and 12 years. In this respect, we would consider the expected lease period of between 10 years and 12 years assumed in determining the annual caps to be normal business practice for the Chinese aviation industry; and

(2) in light of the fact that the aircraft finance leases are usually between 10 and 12 years in length, we have reviewed the PBOC website and have observed that the LPR promulgated by the PBOC for loan period longer than 5 years ranged between 4.3% and 4.6% over the last two years between August 2020 and August 2022. Based on the Sample Aircraft Finance Leases, we also noted that the leases entered into between the Group and independent third parties were all with reference to the LPR prescribed by the PBOC. We are therefore of the view that it is common reference interest rate for aircraft finance leases to be determined with reference to the LPR.

We also understand that the Management has also included a buffer of approximately 5% in its estimated amounts for Aircraft Finance Leases PV for each of the annual caps for 2023, 2024 and 2025. We have discussed and understand that the aforementioned buffer is included to cater for other operating needs which may arise in case of uncertainties. We consider the use of buffer of approximately 5% to be commercially acceptable.

In this respect, and considering the above, we are of the view that such estimates for calculating the Aircraft Finance Lease PV for 2023, 2024 and 2025, which accounts for approximately 95% of each of the respective proposed annual caps for the Lease Transactions is fair and reasonable.

We have discussed and understand from the Management that anticipated total value of right-of-use assets in relation to the operating leases of Aviation Equipment for each of 2023, 2024 and 2025 ("**Aviation Equipment Leases PV**") represents the present value of engines and other aviation related equipment that are capable to be supplied by CNACG with reference their respective market and in response to the Group's estimated demand which is based on internal budgets and purchase schedules. The Group will only enter into lease agreements with members of the CNACG Group if terms offered by CNACG Group are on normal commercial terms or better.

From the information provided that the finance lease and operating lease period for engines normally ranges between 5 to 12 years and for other aviation equipment, the average lease period is around 6 years. Similar to that of Aircraft Finance Leases PV, pursuant to IFRS 16, Aviation Equipment will be recognised as right-of-use assets and such right-of-use asset value is used to determine the annual cap for Lease Transactions. The Aviation Equipment Leases PV are derived from the expected total value of right-of-use assets relating to the engines and other aviation equipment operating lease, which is computed by discounting the estimated total rental fee for Aviation Equipment introduced each year as discussed above, by the Company's internal incremental borrowing rate. As advised by the Management, the prescribed internal incremental borrowing rate referred to for leases with a term longer than five years is 4.9%, and 4.75% for leases with a term of 5 years or below. Similar to the aforementioned with Aircraft Finance Lease PV, we have also reviewed the 2021 Annual Report and noted that the fixed interest rate for the Group's interest-bearing bank and other borrowings ranged from 1.30% to 4.38% (median interest rate being 2.84%), the rate for floating rate bank and other borrowings ranged between 2.66% and 4.65% (median interest rate being 3.66%) and range of interest rates for corporate bonds repayable is from 2.34% to 5.30% (median interest rate being 3.82%). Given the abovementioned ranges and medians of interest rates applicable to the Group's interest-bearing bank loans and other borrowings, and the fact that the internal rates, being 4.9% (for leases with term longer than 5 years) or 4.79% (for leases with term of 5 years or below) are both towards the high end of the aforementioned quoted ranges, we would consider the Company's use of internal rates of 4.9% and 4.79% to be prudent.

Based on the discussion above, we consider the estimation for Aviation Equipment Operating Leases PV for years 2023, 2024 and 2025 are fair and reasonable as far as the Company and Independent Shareholders are concerned.

4. Internal control procedures

As disclosed in the letter from the Board, the Company has adopted a set of effective internal control measures to supervise the continuing connected transactions of the Group:

ACC Transactions (including the Cargo Transactions)

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

CNACG Transactions (including the Leasing Transactions)

- 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 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 CNACG Transactions on a regular basis, including but not limited to the implementation of pricing policies, term of agreement 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 independent auditor of the Company and the independent non-executive Directors will conduct an annual review on the continuing connected transactions of the Group.

We consider the above internal procedures are reasonable for the Company to assess the then prevailing market terms of continuing connected transactions, including the Cargo Transactions and the Lease Transactions, and have demonstrated the Group's practices of getting access to market information so as to make sure that its terms will be no less favourable (so far as the Group is concerned) than those prevailing in the market for similar transactions.

OPINION AND RECOMMENDATION

Having considered the principal factors and reasons set out above, we consider the Non-exempt Transactions including the Cargo Transactions and the Lease Transactions, are conducted on normal commercial terms and in the ordinary and usual course of business of the Group and in the interests of the Company and the Shareholders as a whole, and the terms of the Non-exempt Transactions and their respective annual caps are fair and reasonable so far as the Independent Shareholders are concerned. Accordingly, we advise the Independent Shareholders, and the Independent Board Committee to recommend the Independent Shareholders, to vote in favour of the ordinary resolution to be proposed at the EGM.

Yours faithfully,
for and on behalf of
SOMERLEY CAPITAL LIMITED
Lyan Tam
Director

Ms. Lyan Tam is a licensed person registered with the Securities and Futures Commission and as a responsible officer of Somerley to carry out Type 6 (advising on corporate finance) regulated activities under the SFO and has over 19 years of experience in corporate finance industry.

1. RESPONSIBILITY STATEMENT

This circular, for which the Directors collectively and individually accept full responsibility, includes particulars given in compliance with the Hong Kong Listing Rules for the purpose of giving information with regard to the Group. The Directors, having made all reasonable enquiries, confirm that to the best of their knowledge and belief the information contained in this circular is accurate and complete in all material respects and not misleading or deceptive, and there are no other matters the omission of which would make any statement herein or this circular misleading.

2. DISCLOSURE OF INTERESTS OF DIRECTORS AND SUPERVISORS

As at the Latest Practicable Date, none of the Directors, Supervisors or chief executive of the Company had interests or short positions in the shares, underlying shares and/or debentures (as the case may be) of the Company or its associated corporations (within the meaning of Part XV of the SFO) which were notifiable to the Company and the Hong Kong Stock Exchange pursuant to the SFO, or were recorded in the register maintained by the Company pursuant to section 352 of the SFO, or which were notifiable to the Company and the Hong Kong Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies.

As at the Latest Practicable Date, none of the Directors or Supervisors has any direct or indirect interest in any assets which have been, since 31 December 2021 (the date to which the latest published audited financial statements of the Group were made up), acquired or disposed of by or leased to any member of the Group or are proposed to be acquired or disposed of by or leased to any member of the Group. None of the Directors or Supervisors is materially interested in any contract or arrangement which is significant in relation to the business of the Group and subsisting at the Latest Practicable Date.

Mr. Patrick Healy is a non-executive Director of the Company and is concurrently the chairman and an executive director of the board of directors of Cathay Pacific. Cathay Pacific is a substantial shareholder of the Company, holding 2,633,725,455 H shares as at the Latest Practicable Date. Mr. Song Zhiyong, the chairman and an executive Director of the Company, and Mr. Ma Chongxian, an executive Director of the Company, are concurrently non-executive directors of Cathay Pacific. Cathay Pacific competes or is likely to compete either directly or indirectly with the Company in some aspects of the business of the Company as it operates airline services to certain destinations, which are also served by the Company.

Save as mentioned above, as at the Latest Practicable Date, none of the Directors or Supervisors of the Company and their respective close associates (as defined in the Hong Kong Listing Rules) has any competing interests which would be required to be disclosed under Rule 8.10 of the Hong Kong Listing Rules as if each of them was a controlling shareholder of the Company.

3. SERVICE CONTRACTS

As at the Latest Practicable Date, none of the Directors or Supervisors has any existing or proposed service contract with any member of the Group which is not expiring or terminable by the Group within one year without payment of compensation (other than statutory compensation).

4. DIRECTORS' AND SUPERVISORS' EMPLOYMENT WITH SUBSTANTIAL SHAREHOLDERS

The followings are the particulars of Directors' and Supervisors' employment with substantial Shareholders (holding interests or short positions in the shares and underlying shares of the Company required to be disclosed to the Company pursuant to Divisions 2 and 3 of Part XV of the SFO) as at the Latest Practicable Date:

Mr. Song Zhiyong, the chairman of the Board, an executive Director and the Secretary of the Communist Party Committee of the Company, served as a non-executive director and the vice chairman of the board of directors of Cathay Pacific, and the chairman of CNACG.

Mr. Ma Chongxian, an executive Director, vice chairman of the Board, the president and the Deputy Secretary of the Communist Party Committee of the Company, serves as the chairman and the Secretary of the Communist Party Group of CNAHC. He is also a non-executive director of Cathay Pacific.

Mr. Feng Gang, a non-executive Director and the Deputy Secretary of the Communist Party Committee of the Company, serves as a director and the Deputy Secretary of the Communist Party Group of CNAHC.

Mr. Patrick Healy, a non-executive Director of the Company, is the chairman of the board of directors and an executive director of Cathay Pacific, a director of Swire Pacific Limited, and a director and the chairman of the Charity Committee of John Swire & Sons (H.K.) Limited.

Mr. He Chaofan, a Supervisor of the Company, serves as a director, the president and a member of the Party Committee of CNACG.

Mrs. Lyu Yanfang, a Supervisor of the Company, serves as the general manager of the law department of CNAHC.

Mrs. Guo Lina, a Supervisor of the Company, serves as the general manager of the audit department of CNAHC.

5. MATERIAL ADVERSE CHANGE

Other than the impact brought by the sporadic outbreak of the pandemic and those as disclosed in the interim results announcement of the Company dated 30 August 2022, the Directors confirm that as at the Latest Practicable Date, there has been no material adverse change in the Group's financial or trading position since 31 December 2021, being the date to which the latest published audited financial statements of the Group have been made up.

6. EXPERT

The following is the qualifications of the expert who has given its opinions or advices, which are contained in this circular:

Name	Qualification
Somerley Capital Limited	a corporation licensed to carry out Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities under the SFO

a. As at the Latest Practicable Date, Somerley did not have any direct or indirect interest in any assets which have been acquired or disposed of by or leased to any member of the Group, or are proposed to be acquired or disposed of by or leased to any member of the Group since 31 December 2021 (the date to which the latest published audited financial statements of the Group were made up);

b. As at the Latest Practicable Date, Somerley was not beneficially interested in the share capital of any member of the Group and had no right, whether legally enforceable or not, to subscribe for or to nominate persons to subscribe for securities in any member of the Group; and

c. Somerley has given and has not withdrawn its written consent to the issue of this circular with inclusion of its opinion and the references to its name included herein in the form and context in which they respectively appear.

7. MISCELLANEOUS

a. The joint company secretaries of the Company are Mr. Huang Bin and Mr. Huen Ho Yin. Mr. Huen Ho Yin is a practicing solicitor of the High Court of Hong Kong.

b. The registered address of the Company is at 1st Floor – 9th Floor 101, Building 1, 30 Tianzhu Road, Shunyi District, Beijing, the PRC. The head office of the Company is at No. 30, Tianzhu Road, Airport Industrial Zone, Shunyi District, Beijing, the PRC.

c. The H share registrar and transfer office of the Company is Computershare Hong Kong Investor Services Limited, Shops 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong.

8. DOCUMENTS ON DISPLAY

Copies of the following documents will be published on the websites of the Hong Kong Stock Exchange (www.hkexnews.hk) and the Company (www.airchina.com.cn) for a period of 14 days from the date of this circular:

a. the 2022 ACC Framework Agreement;

b. the CNACG Framework Agreement; and

c. this circular.

As the Supplemental Agreement is not a connected transaction subject to shareholders' approval under the Hong Kong Listing Rules, the Supplemental Agreement will not be presented as a document on display. The principal terms of the Supplemental Agreement have been disclosed in the Circular.

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)

NOTICE OF EXTRAORDINARY GENERAL MEETING

NOTICE IS HEREBY GIVEN that an extraordinary general meeting (the "**EGM**") of Air China Limited (the "**Company**") will be held at 11:00 a.m. on Friday, 14 October 2022 at The Conference Room C713, No. 30, Tianzhu Road, Airport Industrial Zone, Shunyi District, Beijing, the PRC to consider and, if thought fit, to pass the following resolutions. Unless otherwise indicated, capitalised terms used herein shall have the same meaning as those defined in the circular of the Company dated 28 September 2022.

ORDINARY RESOLUTIONS

1. To consider and approve the resolution on the matters related to the continuing related (connected) transactions entered into between the Company and Air China Cargo and the application for the annual transaction caps for 2022 to 2024

   1.1 To consider and approve the resolution on the entering into of a new related (connected) transaction framework agreement by the Company and Air China Cargo and the application for the annual transaction caps for 2022 to 2024

   1.2 To consider and approve the resolution on the entering into of the Agreement on Matters Related to Related (Connected) Transactions of Air China Cargo Shares by the Company and CNAHC, CNAF and Air China Cargo

2. To consider and approve the resolution on the renewal of the related (connected) transaction framework agreement entered into between the Company and CNACG and the application for the annual transaction caps for 2023 to 2025

By Orders of the Board
Air China Limited
Huang Bin Huen Ho Yin
Joint Company Secretaries

Beijing, the PRC, 28 September 2022

As at the date of this notice, the directors of the Company are Mr. Song Zhiyong, Mr. Ma Chongxian, Mr. Feng Gang, Mr. Patrick Healy, Mr. Li Fushen, Mr. He Yun*, Mr. Xu Junxin* and Ms. Winnie Tam Wan-chi*.*

* *Independent non-executive director of the Company*

Notes:

1. **Closure of register of members**

Holders of H shares of the Company are advised that the H share register of members of the Company will be closed from Tuesday, 11 October 2022 to Friday, 14 October 2022 (both days inclusive), during which time no transfer of H shares will be effected and registered. In order to qualify for attendance and voting at the EGM, holders of H shares shall lodge all instruments of transfer with the Company's H share registrar in Hong Kong, Computershare Hong Kong Investor Services Limited, at Shops 1712- 1716, 17/F, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong, by 4:30 p.m. on Monday, 10 October 2022.

H Shareholders whose names appear on the H shares register of members of the Company at the close of business on Monday, 10 October 2022 are entitled to attend and vote at the EGM.

2. **Proxy**

Every Shareholder who has the right to attend and vote at the EGM is entitled to appoint one or more proxies, whether or not they are members of the Company, to attend and vote on his/her behalf at the EGM.

A proxy shall be appointed by an instrument in writing. Such instrument shall be signed by the appointor or his attorney duly authorized in writing. If the appointor is a legal person, then the instrument shall be signed under a legal person's seal or signed by its director or an attorney duly authorized in writing. The instrument appointing the proxy for holders of H shares shall be deposited at the Company's H share registrar not less than 24 hours before the time specified for the holding of the EGM (or any adjournment thereof). If the instrument appointing the proxy is signed by a person authorized by the appointer, the power of attorney or other document of authority under which the instrument is signed shall be notarized. The notarized power of attorney or other document of authority shall be deposited together and at the same time with the instrument appointing the proxy at the Company's H share registrar.

3. **Important notice in relation to COVID-19 pandemic prevention and control**

In the event that the containment of COVID-19 pandemic is still ongoing at the time of the EGM, in order to cooperate with the prevention and control of the pandemic so as to safeguard the health and safety of the Shareholders and the participants of the meeting, at the same time ensuring that the Shareholders may exercise their respective shareholders' rights, the Company recommends H share Shareholders and their proxies intending to attend the EGM to vote by completing and submitting the proxy form, i.e. to indicate how you wish your votes to be casted in the proxy form, and appoint the Chairman of the EGM as your proxy to vote on your behalf on site.

In case H share Shareholders or their proxies choose to attend the meeting in person by then, they must comply with the policies and requirements of Beijing regarding the containment of COVID-19 pandemic. On the way to, from and at the venue of the EGM, please adopt proper personal preventive measures. Upon arrival at the venue of the EGM, please follow the arrangement and guidance of the staff and cooperate with the pandemic prevention and control requirements including, among others, attendee registration, temperature checks and wearing of masks. Please provide the proof of negative nucleic acid test results within 72 hours and comply with the temperature checking procedures, and take the initiative to scan and present the "Beijing Health Kit" green code.

4. Other businesses

(i) The EGM is expected to last for no more than half of a working day. Shareholders and their proxies attending the meeting shall be responsible for their own traveling and accommodation expenses.

(ii) The address of Computershare Hong Kong Investor Services Limited is:

17M Floor
Hopewell Centre
183 Queen's Road East
Wanchai
Hong Kong
Tel No.: (852)28628628
Fax No.: (852)28650990