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中國國際航空股份有限公司
AIR CHINA LIMITED

(Incorporated in the PRC with limited liability under the Company Law of the PRC)
(Stock Code: 753)



中航興業有限公司

CHINA NATIONAL AVIATION COMPANY LIMITED

(Incorporated in Hong Kong under the Companies Ordinance of Hong Kong with limited liability)
(Stock Code: 1110)

JOINT ANNOUNCEMENT

Proposed Pre-Conditional Privatisation of China National Aviation Company Limited by Air China Limited

**By way of a Scheme of Arrangement under Section 166 of the Companies Ordinance
and**

Possible Discloseable Transaction of Air China Limited

Exclusive financial advisers to Air China Limited



CICC
中国国际金融(香港)有限公司
CHINA INTERNATIONAL CAPITAL
CORPORATION (HONGKONG) LIMITED



Merrill Lynch
Merrill Lynch (Asia Pacific) Limited

**Financial adviser to China National Aviation Company Limited
in relation to the Proposed Pre-Conditional Privatisation of
China National Aviation Company Limited**



Citigroup Global Markets Asia Limited

Air China and CNAC jointly announce that, subject to satisfaction of the Pre-Condition, Air China will make the Proposals to privatise CNAC by way of a scheme of arrangement under Section 166 of the Companies Ordinance. The Proposals are made at the request of the CNAC Board who believes the Proposals to be in the interest of CNAC.

Pursuant to the Share Proposal, all Scheme Shares will be cancelled in exchange for the Share Proposal Price of HK\$2.80 in cash for each Scheme Share. As at the date of this announcement, the Scheme Shareholders are interested in 1,048,052,000 Shares, representing approximately 31.6% of the issued share capital of CNAC.

In parallel with and separate from the Share Proposal, Air China will make the Option Proposal to purchase the Outstanding Options, for cancellation in exchange for HK\$1.66 in cash for each Outstanding Option, subject to and conditional upon the Scheme becoming effective.

Save and except for the Options outstanding as at the date of this announcement, there are no outstanding options, warrants, derivatives or other securities issued by CNAC that carry a right to subscribe for or which are convertible into Shares.

As the Proposals are initiated by the CNAC Board, Air China has the full support of CNAC's executive management team to implement the Proposals and to privatise CNAC.

The total amount of cash required for the Proposals is approximately HK\$3,226.8 million, assuming all the Options are exercised prior to the Option Exercise Date. Air China intends to fund the cash required to effect the Proposals from financing arranged through bank borrowings. Air China's exclusive financial advisers, CICC and Merrill Lynch, are satisfied that sufficient financial resources are available to Air China for the implementation of the Proposals.

If the Scheme is implemented, the listing of the Shares on the Stock Exchange will be withdrawn. The Scheme is subject to the satisfaction or waiver, as applicable, of the Pre-Condition and the Conditions.

Upon the Scheme becoming effective, CNAC will become a wholly owned subsidiary of Air China.

Air China reserves the right to implement the Scheme through one or more of its wholly owned subsidiaries. Air China also reserves the right to implement the Proposals by way of a general offer prior to the despatch of the Scheme Document.

The Independent Board Committee, comprising all non-executive directors of CNAC, other than Mr. Hu Hung Lick, Henry who is also an independent non-executive director of Air China, has been appointed to advise Independent Scheme Shareholders and Optionholders in respect of the Share Proposal and the Option Proposal, respectively.

CLSA Equity Capital Markets Limited has been appointed as the independent financial adviser to advise the Independent Board Committee in connection with the Proposals. Such appointment has been approved by the Independent Board Committee.

Subject to the High Court's approval for the despatch of the Scheme Document being obtained, the Scheme Document will be despatched to Shareholders and Optionholders within seven days upon satisfaction of the Pre-Condition, or as soon as practicable thereafter, in accordance with the requirements of the Takeovers Code. Assuming Air China and CNAC each despatches its notice of meetings and circular to shareholders to consider and approve the transactions contemplated by the Restructuring Agreement by 30 June 2006, the Relevant Shareholders' Meetings are expected to take place in the second half of August 2006. As the Restructuring cannot be effected until after the shareholders of Air China and the shareholders have approved the Restructuring, the Pre-Condition is not expected to be satisfied until after the holding of the Relevant Shareholders' Meetings. The Scheme Document will include, among other things, further details of the Proposals and the Scheme, the expected timetable, the recommendations of the Independent Board Committee in respect of the Proposals, a letter of advice from the independent financial adviser to the Independent Board Committee, an explanatory statement as required under the Companies Ordinance, and notices of the Court Meeting and the Extraordinary General Meeting.

Shareholders, Optionholders and/or potential investors in CNAC should be aware that the making of the Proposals is subject to satisfaction of the Pre-Condition (namely, the completion of the transactions contemplated by the Restructuring Agreement), and the implementation of the Proposals is subject to satisfaction or waiver (as applicable) of the Conditions. In particular, if the Restructuring is not completed, the Proposals will not be made. Even if the Proposals are made, the Proposals may or may not become effective. Accordingly, Shareholders, Optionholders and/or potential investors in CNAC are advised to exercise caution when dealing in Shares and/or Options.

INTRODUCTION

Air China and CNAC jointly announce that, subject to satisfaction of the Pre-Condition, Air China will make the Proposals to privatise CNAC by way of a scheme of arrangement under Section 166 of the Companies Ordinance. The Proposals are made at the request of the CNAC Board who believes the Proposals to be in the interest of CNAC.

If approved, the Scheme will be binding on all Scheme Shareholders, irrespective of whether or not they attended or voted at the Court Meeting or the Extraordinary General Meeting. 2,264,642,000 Shares held by Air China and its Concert Parties, representing approximately 68.4% of the existing issued capital as at the date of this announcement, and 66.3% of the enlarged issued share capital, assuming the Options are exercised in full prior to the Option Exercise Date, will not form part of the Voting Shares. As such, Air China and its Concert Parties are required to abstain from voting at the Court Meeting. The 14,000 Shares currently held by a Concert Party will however form part of the Scheme Shares. In addition, an Optionholder, who exercised his or her Option prior to the Record Date, would also be required to abstain from voting at the Court Meeting for the reasons set out in the paragraph headed "General Information", but the Option Shares will form part of the Scheme Shares.

THE SHARE PROPOSAL AND THE OPTION PROPOSAL

Subject to the satisfaction of the Pre-Condition, Air China will make the Proposals on the following basis:

The Share Proposal

For each Scheme Share HK\$2.80 in cash

The Option Proposal

For each Outstanding Option HK\$1.66 in cash

PRE-CONDITION TO MAKING THE PROPOSALS

The making of the Proposals is conditional upon completion of the transactions contemplated under the Restructuring Agreement, details of which are set out in the Restructuring Announcement (the **Pre-Condition**).

If the Pre-Condition is not satisfied, the Proposals will not be made. Air China will, to the extent that it is within its power to do so, use its reasonable efforts to ensure that the Pre-Condition will be satisfied as soon as practicable.

The Share Proposal

The Share Proposal involves the following principal steps, all of which will occur on the Effective Date:

- (a) the share capital of CNAC will be reduced by canceling the Scheme Shares;
- (b) CNAC will apply the credit arising in its books of account as a result of the reduction of capital to pay up in full, at par, a number of New Shares which is equal to the number of Scheme Shares cancelled, and the New Shares will be allotted and issued, credited as fully paid, to Air China or its nominees (which may include a subsidiary of Air China); and
- (c) in consideration for the cancellation of the Scheme Shares and the allotment and issue of New Shares to Air China or its nominees, Scheme Shareholders will receive HK\$2.80 in cash per Scheme Share.

Comparisons of value

The Share Proposal

The Share Proposal Price represents:

- (a) a premium of approximately 65.9% over the average closing price of approximately HK\$1.69 per Share for the six months up to and including the Last Trading Date;
- (b) a premium of approximately 50.3% over the average closing price of approximately HK\$1.86 per Share for the three months up to and including the Last Trading Date;
- (c) a premium of approximately 49.8% over the average closing price of approximately HK\$1.87 per Share for the last 30 trading days up to and including the Last Trading Date;
- (d) a premium of approximately 52.2% over the average closing price of approximately HK\$1.84 per Share for the last 10 trading days up to and including the Last Trading Date;
- (e) a premium of approximately 45.8% over the average closing price of HK\$1.92 per Share for the last five trading days up to and including the Last Trading Date;
- (f) a premium of approximately 42.1% over the closing price of HK\$1.97 per Share as quoted on the Stock Exchange on the Last Trading Date;
- (g) a premium of approximately 199.9% over the audited net asset value per Share of approximately HK\$0.93 as at 31 December 2005, equivalent to a multiple of 3.0x net asset value (adjusted for year-end dividends) of CNAC of HK\$3,092.7 million and 3,312,680,000 Shares in issue as at 31 December 2005; and
- (h) a price earnings multiple of approximately 41.2x based on the audited net profit attributable to Shareholders of approximately HK\$225 million for the financial year ended 31 December 2005 and 3,312,680,000 Shares in issue as at 31 December 2005.

The Option Proposal

In accordance with the terms of the Share Option Scheme, Optionholders are entitled to exercise their Options, which confer on them rights to subscribe for Shares at a price of HK\$1.14 per Share, in full or in part at any time up to the Option Exercise Date. Shares issued upon exercise of the Options in accordance with the terms of the Share Option Scheme prior to the Record Date will form part of the Scheme Shares. If the Scheme becomes effective, Options which are not exercised in accordance with the terms of the Share Option Scheme will lapse.

Under the Option Proposal, Air China will offer to purchase Outstanding Options, for cancellation in exchange for HK\$1.66 in cash for each Outstanding Option, subject to and conditional upon the Scheme becoming effective. Further information on the Option Proposal will be set out in the Scheme Document and the Option Proposal will be made by or on behalf of Air China in a letter to Optionholders to be despatched on the same day as the Scheme Document.

Trading Prices

The highest and lowest prices at which Shares were traded on the Stock Exchange in the six-month period immediately prior to the Last Trading Date were HK\$2.10 on 6 April 2006 and 10 April 2006 and HK\$1.40 on 13 December 2005, 15 December 2005 and 16 December 2005, respectively.

Total Consideration

On the basis of the Share Proposal Price of HK\$2.80 per Scheme Share and 3,312,680,000 Shares in issue of which 1,048,052,000 are Scheme Shares as at the date of this announcement, the Scheme Shares are valued at approximately HK\$2,934.5 million.

According to CNAC, there are 104,378,000 Options, giving rights to subscribe for 104,378,000 Shares, outstanding as at the date of this announcement. There are no other outstanding options, warrants, derivatives or other securities issued by CNAC that carry a right to subscribe for or which are convertible into Shares. Assuming that none of the Options is exercised prior to the Option Exercise Date and the Option Proposal is accepted in full, on the basis of a consideration of HK\$1.66 payable for the cancellation of each of the 104,378,000 Outstanding Options, the Option Proposal is valued at HK\$173.3 million.

Assuming that all Options are exercised in full by Optionholders prior to the Option Exercise Date in accordance with the terms of the Share Option Scheme, the consideration payable by Air China pursuant to the Share Proposal will be increased to approximately HK\$3,226.8 million. No consideration for cancellation will then be payable under the Option Proposal.

Air China intends to fund the cash required to effect the Proposals from financing arranged through bank borrowings. The financing agreement for such bank borrowings is governed by PRC law and the performance of such agreement may be limited by force majeure provisions under the PRC Civil Code and the PRC Contract Law.

Confirmation of Financial Resources

CICC and Merrill Lynch, the exclusive financial advisers to Air China in respect of the Proposals, are satisfied that sufficient financial resources are available to the Air China to implement the Proposals.

CONDITIONS OF THE PROPOSALS

The Scheme will become effective and binding on CNAC and all Scheme Shareholders subject to satisfaction or waiver (as applicable) of the following conditions:

- (a) the approval of the Scheme by a majority in number of the Independent Scheme Shareholders representing not less than three-fourths in value of the Scheme Shares held by Independent Scheme Shareholders, present and voting either in person or by proxy at the Court Meeting, provided that:
 - (i) the Scheme is approved by at least 75% of the votes attaching to Scheme Shares held by Independent Scheme Shareholders that are cast either in person or by proxy at the Court Meeting (by way of poll); and

- (ii) the number of votes cast against the resolution to approve the Scheme at the Court Meeting (by way of poll) is not more than 104,803,800, representing 10% of the votes attaching to all Scheme Shares held by Independent Scheme Shareholders;
- (b) the passing of a special resolution to approve and give effect to the cancellation of the Scheme Shares and the reduction of the relevant portion of the issued share capital of CNAC by a majority of at least three-fourths of the votes cast by Shareholders present and voting in person or by proxy, at the Extraordinary General Meeting by way of poll;
- (c) the sanction of the Scheme (with or without modifications) by the High Court and the delivery to the Registrar of Companies in Hong Kong of an official copy of the order of the High Court for registration;
- (d) the compliance with the procedural requirements of Section 58 of the Companies Ordinance in relation to the reduction of the issued share capital of CNAC;
- (e) the receipts of all relevant authorisations, consents and/or approvals from each of State Administration for Foreign Exchange of the PRC, National Development and Reform Commission of the PRC, Ministry of Commerce of the PRC, China Civil Aviation Authority, Ministry of Finance of the PRC, State Assets Supervision and Administration Commission of the PRC, China Securities Regulatory Commission, China Banking Regulatory Commission and Hong Kong and Macau Affairs Department of the State Council necessary for the implementation of the Proposals, and all such authorisations, consents and/or approvals remaining in full force and effect;
- (f) no act referred to under Rule 4 of the Takeovers Code having been or being proposed or threatened to be carried out by the CNAC Board;
- (g) since the date of this announcement, there having been no force majeure event, including, without limitation, act of God, war, riot, public disorder, civil commotion, economic sanctions, fire, flood, explosion, epidemic, terrorism, labour dispute strike, lock-out, out-break, escalation, declaration or threat of war or hostility, or disaster which is outside Air China's control that would render it impossible for Air China to implement the Proposals; and
- (h) save for the payment of a final dividend of HK cent 1.0 per Share as approved by the Shareholders on the annual general meeting of CNAC held on 25 May 2006, since the date of this announcement and up to the Effective Date, CNAC not having declared, made or paid any dividend or distribution of any kind, and not agreeing or proposing to declare, make or pay any dividend or distribution of any kind.

Air China will use its reasonable endeavours to fulfill the Conditions which are reasonably within its powers in a timely manner. If the Conditions are not satisfied on or before the specific date to be set out in the Scheme Document, the Scheme will lapse.

The Option Proposal will be subject to and conditional upon the Share Proposal becoming or being declared effective.

Air China reserves the right to implement the Proposals by way of a general offer prior to the despatch of the Scheme Document. Air China also reserves the right, at its absolute discretion, to waive, in whole or in part, any of the Conditions referred to in paragraphs (f) to (h) above. Conditions (a) to (e) cannot be waived by Air China. **In the event that any of Conditions (a) to (e) is not satisfied on or before the specific date to be set out in the Scheme Document, the Scheme will lapse.** Air China may only invoke any or all of Conditions (a) to (h) as a basis for not proceeding with the Scheme if the provisions of

Note 2 to Rule 30.1 of the Takeovers Code are satisfied. Note 2 to Rule 30.1 of the Takeovers Code provides that an offeror should not invoke any condition (other than the acceptance condition) so as to cause the offer to lapse unless the circumstances which give rise to the right to invoke the condition are of material significance to the offeror in the context of the offer.

Scheme Document

Subject to the High Court's approval for the despatch of the Scheme Document being obtained, the Scheme Document containing, among other things, further details about the Proposals and the Scheme, the expected timetable, the recommendation of the Independent Board Committee in respect of the Proposals, the letter of advice from the independent financial adviser to the Independent Board Committee, an explanatory statement as required under the Companies Ordinance, and notices of the Court Meeting and the Extraordinary General Meeting will be despatched to Shareholders and the Optionholders within seven days of satisfaction of the Pre-Condition, or as soon as practicable thereafter, in accordance with the requirements of the Takeovers Code. Assuming Air China and CNAC each despatches its notice of meetings and circular to shareholders to consider and approve the transactions contemplated by the Restructuring Agreement by 30 June 2006, the Relevant Shareholders' Meetings of Air China and CNAC are expected to take place in the second half of August 2006. As the Restructuring cannot be effected until after the shareholders of Air China and the Shareholders have approved the Restructuring, the Pre-Condition is not expected to be satisfied until after the holding of the Relevant Shareholders' Meetings. A further announcement will be made regarding the expected timetable for the Proposals.

The Independent Board Committee, comprising all non-executive directors of CNAC, other than Mr. Hu Hung Lick, Henry who is also an independent non-executive director of Air China, has been appointed to advise Independent Scheme Shareholders and Optionholders in respect of the Share Proposal and the Option Proposal, respectively.

CLSA Equity Capital Markets Limited has been appointed as the independent financial adviser to advise the Independent Board Committee in connection with the Proposals. Such appointment has been approved by the Independent Board Committee.

INFORMATION ON THE CNAC GROUP

Business of the CNAC Group

CNAC was incorporated in Hong Kong in 1997 and was listed on the Stock Exchange on 17 December 1997, trading under the stock code 1110. The CNAC Groups' principal activities are airline operations and aviation related businesses.

The principal business activity of CNAC is that of an investment holding company. Following the completion of the Restructuring Agreement, the core businesses of CNAC will include air transportation services (Air Macau, Macau Asia Express Limited and a minority stake in Cathay), airline catering services (Beijing Air Catering Co. Ltd., Southwest Air Catering Company Limited, and LSG Lufthansa Service Hong Kong Ltd.), airport ground handling services (Jardine Airport Service Ltd. and Menzies Macau Airport Services Ltd.) and logistics services (Tradeport Hong Kong Ltd.).

According to CNAC, the number of Shares in issue is 3,312,680,000 as at the date of this announcement and Air China and its Concert Parties are interested in 2,264,642,000 Shares, representing approximately 68.4% of the entire issued share capital in CNAC as at the date of this announcement.

Key financial information of the CNAC Group

A summary of the audited consolidated results and net asset value of the CNAC Group for each of the two years ended 31 December 2004 and 31 December 2005 is set out below:

	For the year ended 31 December	
	2004	2005
	HK\$'000	HK\$'000
Turnover	1,890,710	2,620,033
Operating profit	16,733	(52,317)
Profit before tax	406,808	221,966
Profit after tax but before minority interests (<i>Note 2</i>)	394,464	211,924
Profit attributable to Shareholders (<i>Note 1</i>)	360,969	225,000
Net asset value as at 31 December 2005		3,125,837
Earnings per share (HK Cents)		7
Net asset per share (HK Cents)		94

The above financial information is extracted from the financial statements set out in the CNAC 2005 annual report, which had been prepared in accordance with Hong Kong Financial Reporting Standards and Hong Kong Accounting Standards and interpretations issued by the Hong Kong Institute of Certified Public Accountants.

Shareholding Structure of CNAC

Shareholders	As at the date of this announcement		Immediately after the Effective Date and the Shares are delisted on the Stock Exchange (<i>Note 3</i>)		Immediately after the Effective Date and the Shares are delisted on the Stock Exchange (<i>Note 4</i>)	
	Number of Shares	%	Number of Shares	%	Number of Shares	%
Air China	2,264,628,000	68.4	3,312,680,000	100	3,417,058,000	100
Concert Parties	14,000	0	Nil	Nil	Nil	Nil
Subtotal for Air China and Concert Parties	2,264,642,000	68.4	3,312,680,000	100	3,417,058,000	100
Independent Scheme Shareholders (<i>Note 2</i>)	1,048,038,000	31.6	Nil	Nil	Nil	Nil
Total	3,312,680	100.0	3,312,680,000	100	3,417,058,000	100

Optionholders

Names of Optionholders (<i>Note 5</i>)	As at the date of this announcement	
	Number of Options	%
Chuang Shih Ping	33,126,000	31.7
Gu Tiefei	5,000,000	4.8
Tsang Hing Kwong, Thomas	33,126,000	31.7
Zhang Xianlin	33,126,000	31.7
Total	104,378,000	100.0

Note 1: The profit refers to profit after tax and extraordinary items.

Note 2: The Independent Scheme Shareholders include the non-profit organisations who will receive the Shares from Cathay prior to the Court Meeting, details of which are set out in the paragraph headed “Interest of Air China and the Concert Parties in CNAC”.

Note 3: Assuming no Options will be exercised before or on the Option Exercise Date.

Note 4: Assuming the Options will be exercised prior to the Record Date.

Note 5: All the Optionholders are executive directors of CNAC.

The Options were granted on 25 July 2003 and are exercisable during the period from 26 October 2003 to 25 October 2009 at an exercise price of HK\$1.14 per Share.

INFORMATION ON AIR CHINA

Air China is a company incorporated in the PRC on 30 September 2004, whose shares were listed on the Main Board of the Stock Exchange on 15 December 2004 under the stock code 753. Air China’s shares were also listed on the London Stock Exchange in December 2004 by way of a secondary listing. As at the date of this announcement, China National Aviation Holding Company, a state-owned company established under the laws of the PRC, directly and indirectly owns 65.80% of Air China. Air China is a leading provider of air passenger, air cargo and airline-related services in the PRC.

According to Air China, the number of shares in issue of Air China is 9,433,210,909 as at the date of this announcement.

GENERAL INFORMATION

Assuming the Proposals are implemented in full, the consideration ratio pursuant to Rule 14.07 of the Listing Rules in connection with the issue of New Shares by CNAC to Air China pursuant to the Scheme is expected to be 10.9% and therefore would constitute a discloseable transaction for Air China under Chapter 14 of the Listing Rules. Air China will despatch a circular on the possible discloseable transaction to its shareholders within 21 days after publication of this announcement pursuant to Chapter 14 of the Listing Rules.

The Optionholders are all executive directors of CNAC, currently holding in aggregate 104,378,000 Options in CNAC and are therefore deemed to have a material interest in the Proposals. As such, an Optionholder who exercises his or her Options prior to the Record Date would then be required to abstain from voting at the Court Meeting in respect of the Option Shares. Assuming all the Options are exercised in full prior to the Record Date, the issued share capital of CNAC so enlarged will comprise 3,417,058,000 Shares, of which 104,378,000 are Option Shares, representing approximately 3.05% of the enlarged issued capital of CNAC.

Mr. Zhang Xianlin, an executive director of CNAC, is a supervisor of Air China and therefore a connected person of Air China. As such, if Mr. Zhang Xianlin accepts the Option Proposal from Air China or becomes a Scheme Shareholder, it would constitute a connected transaction for Air China under Chapter 14A of the Listing Rules. Air China will fully comply with the requirements under Chapter 14A of the Listing Rules if and when Mr. Zhang Xianlin accepts the Option Proposal or the Share Proposal.

Save as disclosed above, neither the Proposals nor the issue of New Shares by CNAC to Air China would constitute connected transactions for Air China under Chapter 14A of the Listing Rules.

Overseas Shareholders

The making of the Share Proposal to and acceptance of the Share Proposal by persons not resident in Hong Kong may be subject to the laws of the relevant jurisdictions. Such persons should inform themselves about and observe any applicable legal or regulatory requirements. It is the responsibility of any overseas Shareholders wishing to accept the Share Proposal to satisfy themselves as to the full observance of the laws of the relevant jurisdiction in connection therewith, including the obtaining of any governmental, exchange control or other consents which may be required, or the compliance with other necessary formalities and the payment of any issue, transfer or other taxes due in such jurisdiction. The arrangements for the despatch of the Scheme Document to the Shareholders, including the overseas Shareholders, will be set out in a further announcement regarding the despatch of the Scheme Document, to be made by CNAC.

AIR CHINA – BACKGROUND TO, REASONS FOR AND BENEFITS OF THE PROPOSALS

On 8 June 2006, Air China, Cathay, CNAC, CITIC Pacific Limited and Swire Pacific Limited made a joint announcement that they had entered into the Restructuring Agreement in respect of their shareholdings in Dragonair, Cathay and Air China. Concurrent and conditional upon the Restructuring Agreement becoming effective, Air China and Cathay also announced that they had entered into the Operating Agreement which represents a far reaching agreement to enhance cooperation between Air China and Cathay in a number of key operational areas. Air China believes that the Restructuring Agreement and Operating Agreement represent an extremely attractive package of initiatives that will bring substantial benefits to the Air China Group as a whole.

Implementation of the Restructuring Agreement will involve the following actions:

- (i) Air China acquiring a 10.16% shareholding in Cathay from CITIC Pacific Limited and Swire Pacific Limited, at HK\$13.50 per Cathay share;
- (ii) Cathay increasing its ownership in Air China from 10% to 20% through the subscription of new Air China H-shares at HK\$3.45 per Air China H-share;
- (iii) Cathay acquiring the remaining 82.21% shareholding in Dragonair that it does not already own from CNAC (43.29%), CITIC Pacific Limited (28.50%) and Swire Pacific Limited (7.71%) and others (2.71%) for a combination of equity (548 million new Cathay shares at HK\$13.50 per Cathay share) and cash (HK\$822.1 million), valuing 100% of the equity of Dragonair at HK\$10.0 billion; and
- (iv) Swire Pacific Limited and CITIC Pacific Limited further reducing their shareholdings in Cathay to 40.00% and 17.50%, respectively.

Execution of the Operating Agreement will include:

- (i) implementing reciprocal sales representation for passenger services, where Air China will be exclusively responsible for Cathay's passenger sales in Mainland China, including those of Dragonair, while Cathay will be exclusively responsible for Air China's passenger sales in Hong Kong, Macau and Taiwan;
- (ii) the extension of code share arrangements between Hong Kong and Mainland China such that Air China and Cathay will operate all their passenger services (including those of Dragonair) between Hong Kong and Mainland China under a code-share arrangement;
- (iii) the operation of all shared routes between Hong Kong and Mainland China as joint venture routes under revenue and cost pooling arrangements;

- (iv) the creation of a cargo joint venture based in Shanghai which will be majority controlled by Air China;
- (v) maintaining Dragonair as a principal airline for at least six years; and
- (vi) the strengthening of business cooperation in a number of other areas.

Implementation of the Restructuring Agreement and the Operating Agreement will bring significant benefits to Air China including the realisation of substantial revenue and cost synergies by leveraging integration advantages including improved load factors and better route management, sharing operating results, creating economies of scale, optimising resource allocation and the transfer of know-how between the airlines.

Furthermore, Air China believes that the HK\$10.0 billion valuation achieved for 100% of the equity of Dragonair represents realisation of the full value of CNAC's 43.29% shareholding in Dragonair, including a fair attribution of expected synergies. This valuation represents a price-to-earnings ratio of 33.3 times Dragonair's reported earnings of HK\$300.4 million for the year ended 31st December 2005. In recent years the Chinese aviation industry has experienced rapid growth and development: the creation of three Chinese airline groups, the continuing liberalization of the market to international airlines and the increasing internationalisation of the Chinese airlines' route networks. In the context of these market developments, Air China Directors are of the view that the competitive position of Dragonair has deteriorated (especially in the face of intensive competition on its HK-Mainland routes) and the shareholding structure of Dragonair has proved to be inefficient with the result that Dragonair is unable to take full advantage of potential economies of scale and the management of its business is not optimised. The rationalisation of the shareholding structure of Dragonair will benefit all the companies that are current shareholders of Cathay and Dragonair itself.

Upon completion of the Restructuring Agreement, CNAC will own a 7.34% shareholding in Cathay. Air China wishes to rationalise its shareholding in Cathay so that Air China directly controls a 17.5% shareholding in Cathay, allowing Air China greater influence over Cathay and to equity account for a higher percentage of Cathay's financial results. As a result, Air China wishes to privatise CNAC so that CNAC becomes a wholly owned subsidiary of Air China.

Announcement of the proposed pre-conditional privatisation of CNAC will also enable Air China to fulfill a condition of an irrevocable undertaking to Air China and CNAC by On Ling Investments Limited (which beneficially owns approximately 9.75% of the issued share capital of CNAC) to vote in favour of the shareholders' resolutions to be proposed at the Relevant Shareholders' Meeting of CNAC. This irrevocable undertaking is a key component in providing execution certainty for both the Restructuring Agreement and the Operating Agreement.

CNAC – BACKGROUND TO AND REASONS FOR THE SCHEME

The completion of the Restructuring will result in CNAC holding a 7.34% minority interest in Cathay, instead of 43.29% interest in Dragonair, thereby effectively becoming largely a passive investment holding company. In view of the subsequent material changes in CNAC's business and prospects, it is the view of the CNAC Directors that certain Scheme Shareholders may consider whether they would continue to hold their Scheme Shares. Considering this factor as well as the above-mentioned On Ling Investment Limited's conditional irrevocable undertaking, CNAC Directors are of the view that the Proposal would be in the interest of CNAC and the Shareholders as a whole.

For Scheme Shareholders, the Share Proposal Price of HK\$2.80 per Scheme Share represents an excellent opportunity to exit from their investment in CNAC and realise immediate cash proceeds. The Share Proposal Price reflects:

- (i) a premium of approximately 71.8% over the initial public offering price of HK\$1.63 per Share;
- (ii) a premium of approximately 65.9% over the average closing price of approximately HK\$1.69 per Share for the six months up to and including the Last Trading Date; and
- (iii) an implied price-to-book multiple of 3.0x based on the net asset value of CNAC (adjusted as for year-end dividends) of HK\$3,092.7 million as at 31 December 2005.

As approximately 68.36% of CNAC is already owned by Air China as at the date of this announcement, it is unlikely that Scheme Shareholders will receive any other offer from a third party to acquire the Shares. In addition, Scheme Shareholders should note that no discussions have taken place (or are taking place) with any third party regarding the disposal of any of the Shares held by Air China and Air China has no intention of selling any of its holding in CNAC to any third party.

AIR CHINA'S INTENTION IN RELATION TO CNAC

Intention regarding CNAC

It is the intention of Air China to apply for a withdrawal of the listing of the Shares from the Stock Exchange pursuant to Rule 6.05 of the Listing Rules. Scheme Shareholders will be notified by way of press announcement of the exact dates on which the Scheme and the withdrawal of the listing of the Shares from the Stock Exchange will become effective. Air China has no current intention to introduce any major changes to the existing operating and management structure of CNAC, nor does Air China have any current intention to discontinue the employment of any employee of the CNAC Group as a result of the implementation of the Proposals or the Scheme becoming effective.

Lapsing of the Scheme

The Scheme will lapse if it does not become effective on or before a date to be set out in the Scheme Document, or such other later date as Air China and CNAC may agree or as the High Court may direct, and the Scheme Shareholders will be notified by way of a press announcement accordingly. The listing of Shares will not be withdrawn if the Scheme is not approved or lapses.

INTEREST OF AIR CHINA AND THE CONCERT PARTIES IN CNAC

Cathay, who is deemed to act in concert with Air China in respect of the Scheme, holds approximately 1.95% of the Shares as at the date of this announcement. Cathay has agreed to donate its entire shareholdings in CNAC to a group of independent non-profit organisations, for otherwise, certain transactions contemplated under the Restructuring Agreement and Shareholders Agreement would amount to a special deal between Air China and Cathay under Rule 25 of the Takeovers Code. Cathay is currently in the process of selecting the non-profit organisations and is mindful of the need to make the donations in sufficient time to enable the non-profit organisations to decide on how to vote on the Proposals or whether to accept the Proposals. As such, Cathay will not be a Shareholder anymore by the date of the Court Meeting.

Merrill Lynch, Pierce, Fenner & Smith Incorporated, which is under the same control as Merrill Lynch, and presumed to be acting in concert with Air China in respect of the Scheme, sold 2,000 Shares on 1 June 2006 at an average price of US\$0.27 per Share and holds 14,000 Shares as at the date of this announcement, which will be cancelled pursuant to the Scheme.

CICC and Merrill Lynch are exclusive financial advisers to both Air China and CNAC with respect to all aspects of the Restructuring.

Save as disclosed in this announcement, or the Restructuring Announcement, none of Air China and the Concert Parties has any other interest or dealings in CNAC during the Relevant Period.

Save as disclosed in this announcement, or the Restructuring Announcement, there is no arrangement (whether by way of option, indemnity or otherwise) in relation to shares of Air China or the Shares and which might be material to the Proposals, nor is there any agreement or arrangement to which Air China is a party which relates to the circumstances in which it may or may not invoke or seek to invoke a Pre-Condition or a condition to its offer and the consequences of its doing so.

As at the date of this announcement, there is no irrevocable commitment given by any Shareholder to accept the Proposals.

Shareholders, Optionholders and/or potential investors in CNAC should be aware that the making of the Proposals is subject to satisfaction of the Pre-Condition (namely, the completion of the transactions contemplated by the Restructuring Agreement), and the implementation of the Proposals is subject to satisfaction or waiver (as applicable) of the Conditions. In particular, if the Restructuring is not completed, the Proposals will not be made. Even if the Proposals are made, the Proposals may or may not become effective. Accordingly, Shareholders, Optionholders and/or potential investors in CNAC are advised to exercise caution when dealing in Shares and/or Options.

DEFINITIONS

In this announcement, the following expressions have the meanings set out below unless the context requires otherwise.

“acting in concert”	has the meaning ascribed to it in the Takeovers Code;
“Air China”	Air China Limited, a company incorporated in the PRC with limited liability whose shares are listed on the Main Board of the Stock Exchange under the stock code 753;
“Air China Directors”	the directors of Air China;
“Air China Group”	Air China and its subsidiaries;
“Business Day(s)”	a day on which banks are opened for business in Hong Kong (excluding Saturdays, Sundays or public holidays in Hong Kong);
“Cathay”	Cathay Pacific Airways Limited, a company incorporated in Hong Kong with limited liability, whose shares are listed on the Main Board of the Stock Exchange under the stock code 293;
“CICC”	China International Capital Corporation (Hong Kong) Limited, a licensed corporation for type 1 (dealing in securities), type 4 (advising on securities), type 6 (advising on corporate finance) and type 9 (asset management) regulated activities under the Securities and Futures Ordinance, being an exclusive financial adviser to Air China in relation to the Proposals;

“CNAC”	China National Aviation Company Limited, a company incorporated in Hong Kong with limited liability, whose shares are listed on the Main Board of the Stock Exchange under the stock code 1110;
“CNAC Board”	the board of CNAC Directors;
“CNAC Directors”	the directors of CNAC;
“CNAC Group”	CNAC and its subsidiaries;
“Companies Ordinance”	the Companies Ordinance (Chapter 32 of the Laws of Hong Kong);
“Concert Parties”	persons who are acting in concert with Air China;
“Conditions”	the conditions of the Proposals, as set out under the paragraph headed “Conditions of the Proposals” of this announcement;
“Court Meeting”	a meeting of the Independent Scheme Shareholders to be convened at the direction of the High Court at which the Scheme will be voted upon;
“Dragonair”	Hong Kong Dragon Airlines Limited, a private company incorporated in Hong Kong;
“Effective Date”	the date on which the Scheme, if approved, becomes effective in accordance with its terms, being the date on which an official copy of the order of the High Court sanctioning the Scheme together with the minutes containing the particulars required by Section 61 of the Companies Ordinance are registered by the Registrar of Companies in Hong Kong;
“Extraordinary General Meeting”	the extraordinary general meeting of CNAC to be held to consider and approve, among other matters, the capital reduction arising as a result of the Scheme, or any adjournment thereof;
“High Court”	the High Court of Hong Kong;
“HK\$”	Hong Kong dollars, the lawful currency of Hong Kong;
“Hong Kong”	the Hong Kong Special Administrative Region of the PRC;
“Independent Scheme Shareholders”	Scheme Shareholders other than Concert Parties and, in respect of the Option Shares, the Optionholders;
“Independent Board Committee”	the independent board committee, comprising all non-executive directors of CNAC, other than Mr. Hu Hung Lick, Henry who is also an independent non-executive director of Air China, appointed to advise Independent Scheme Shareholders and Optionholders in respect of the Share Proposal and the Option Proposal, respectively;

“Last Trading Date”	2 June 2006, being the last day on which Shares were traded prior to the publication of the Restructuring Announcement;
“Listing Rules”	the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited;
“Merrill Lynch”	Merrill Lynch (Asia Pacific) Limited, a licensed corporation for type 1 (dealing in securities), type 4 (advising on securities), type 6 (advising on corporate finance) and type 7 (providing automated trading services) regulated activities under the Securities and Futures Ordinance, being an exclusive financial adviser to Air China in relation to the Proposals;
“New Share”	new Share(s) to be issued to Air China or its nominees, credited as fully paid, pursuant to the Share Proposal;
“Operating Agreement”	the agreement entered into by Air China and Cathay on 8 June 2006, details of which are set out in the joint announcement made by Air China and Cathay on 8 June 2006;
“Options”	the share options granted pursuant to the Share Option Scheme;
“Optionholders”	the holders of one or more Options, and as at the date of this announcement, means Chuang Shih Ping, Zhang Xianlin, Tsang Hing Kwong, Thomas and Gu Tiefei, who altogether hold 104,378,000 Options (or, if Air China so elects prior to the Scheme lapsing or becoming ineffective, the offer by Air China to acquire all of the Outstanding Options not owned by Air China at a price equal to the Option Proposal Price);
“Option Exercise Date”	the date which is fourteen days after the Effective Date;
“Option Proposal”	the proposal to Optionholders for cancellation of all Outstanding Options (or, if Air China so elects prior to the despatch of the Scheme Document, a general offer by Air China to acquire all of the Outstanding Options not owned by Air China at a price equal to the Option Proposal Price);
“Option Proposal Price”	HK\$1.66 per Outstanding Option pursuant to the Option Proposal;
“Option Shares”	Shares that are subscribed for in exercise of the Options pursuant to the Share Option Scheme;
“Outstanding Options”	Options not exercised as at the Option Exercise Date;
“Pre-Condition”	the Pre-Condition to making the Proposals, as set out under the paragraph headed “The Pre-Condition to making the Proposals” of this announcement;
“Proposals”	the Share Proposal and the Option Proposal;

“PRC”	the People’s Republic of China, excluding, for the purpose of this announcement, Hong Kong, Macau and Taiwan;
“Pre-Conditions”	the Pre-Conditions to making the Proposals, as set out under the paragraph headed “The Pre-Conditions to making the Proposals” of this announcement;
“Proposals”	the Share Proposal and the Option Proposal;
“Record Date”	two Business Days prior to the Court Meeting;
“Relevant Period”	the period from 8 December 2005 to the date of this announcement;
“Relevant Shareholders’ Meetings”	the shareholders’ meetings to be convened by Air China, CNAC, Cathay, CITIC Pacific Limited and Swire Pacific Limited to approve the Restructuring;
“Restructuring”	the restructuring referred to in the Restructuring Agreement;
“Restructuring Agreement”	the restructuring agreement dated 8 June 2006 entered into by Swire Pacific Limited, CITIC Pacific Limited, CNAC, Air China and Cathay, details of which are set out in the Restructuring Announcement;
“Restructuring Announcement”	the joint announcement dated 8 June 2006 published by Air China, CNAC, Cathay, CITIC Pacific Limited and Swire Pacific Limited;
“Scheme”	a scheme of arrangement under Section 166 of the Companies Ordinance;
“Scheme Document”	the document to be issued to all Shareholders and Optionholders containing, among other things, further details of the Proposals and the Scheme, the recommendation of the Independent Board Committee in respect of the Proposals, the letter of advice from the independent financial adviser to the Independent Board Committee, an explanatory statement as required under the Companies Ordinance, the expected timetable, and the notices convening the Court Meeting and the Extraordinary General Meeting;
“Scheme Shareholders”	Shareholders except Air China, but including the Shares held by Concert Parties and Option Shares;
“Scheme Shares”	the Share(s) held by Scheme Shareholders;
“SFC”	the Securities and Futures Commission of Hong Kong;
“Shares”	ordinary shares of HK\$0.10 each in the issued share capital of CNAC;
“Share Option Scheme”	the share option scheme adopted by CNAC on 29 May 2002, the major terms of which are set out in the audited annual report of CNAC for the year ended 31 December 2005;

“Share Proposal”	the proposal to Scheme Shareholders for the cancellation of all Scheme Shares pursuant to the Scheme (or, if Air China so elects prior to the despatch of the Scheme Document, a general offer by Air China to acquire all of the Shares not owned by Air China at a price equal to the Share Proposal Price);
“Share Proposal Price”	HK\$2.80 per Scheme Share pursuant to the Share Proposal;
“Shareholders”	registered holders for the time being of Shares;
“Shareholders Agreement”	the shareholders agreement referred to in the Restructuring Announcement;
“Stock Exchange”	The Stock Exchange of Hong Kong Limited;
“subsidiaries”	has the meaning ascribed to it in Section 2 of the Companies Ordinance;
“Takeovers Code”	The Hong Kong Code on Takeovers and Mergers;
“Voting Shares”	Scheme Shares other than the Option Shares and those held by Concert Parties.

By order of the Board
Air China Limited
Li Jiexiang
Chairman

By order of the Board
China National Aviation Company Limited
Kong Dong
Chairman

Hong Kong, 21 June 2006

The directors of Air China jointly and severally accept full responsibility for the accuracy of the information contained in this announcement (other than that relating to the CNAC Group) and confirm, having made all reasonable enquires, that to the best of their knowledge, opinions expressed in this announcement (other than those expressed by CNAC) have been arrived at after due and careful consideration and there are no other facts (other than those relating to the CNAC Group) not contained in this announcement, the omission of which would make any statements in this announcement misleading.

As at the date of this announcement, the board of directors of Air China comprises Li Jiexiang, Kong Dong, Wang Shixiang, Yao Weiting, Christopher Pratt as non-executive directors, Ma Xulun, Cai Jianjiang, Fan Cheng as executive directors, and Hu Hung Lick, Henry, Wu Zhipan and Zhang Ke as independent non-executive directors.

The directors of CNAC jointly and severally accept full responsibility for the accuracy of the information contained in this announcement (other than that relating to the Air China Group) and confirm, having made all reasonable enquires, that to the best of their knowledge, opinions expressed in this announcement (other than those expressed by Air China) have been arrived at after due and careful consideration and there are no other facts (other than those relating to the Air China Group) not contained in this announcement, the omission of which would make any statements in this announcement misleading.

As at the date of this announcement, the board of directors of CNAC comprises Kong Dong, Chuang Shih Ping, Zhang Xianlin, Zhao Xiaohang, Tsang Hing Kwong, Thomas, Gu Tiefei as executive directors, Lok Kung Nam, Hu Hung Lick, Henry, Ho Tsu Kwok, Charles, Li Kwok Heem, John, Chan Ching Har, Eliza as independent non-executive directors.

“Please also refer to the published version of this announcement in the South China Morning Post”