

**China Airlines, Ltd.**

**Financial Statements for the Years Ended  
December 31, 2003 and 2002  
Together with Independent Auditors' Report**

Readers are advised that the original version of these financial statements is in Chinese. If there is any conflict between these financial statements and the Chinese version or any difference in the interpretation of the two versions, the Chinese-language financial statements shall prevail.

**CHINA AIRLINES, LTD.**

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**English Translation of a Report Originally Issued in Chinese**

**INDEPENDENT AUDITORS' REPORT**

February 25, 2004

The Board of Directors and the Stockholders  
China Airlines, Ltd.

We have audited the accompanying balance sheets of China Airlines, Ltd. as of December 31, 2003 and 2002 and the related statements of income, changes in stockholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. However, we did not audit the financial statements as of and for the years ended December 31, 2003 and 2002 of China Pacific Catering Services, Cal-Dynasty International, Abacus Distribution Systems (Taiwan) and four other investees, which were accounted for by the equity method, as shown in the accompanying financial statements. We also did not audit the financial statements as of and for the year ended December 31, 2002 of Taoyuan International Airport Service, Taiwan Airport Services, China Pacific Laundry Services and Hwa Hsia. Those statements were audited by other auditors whose reports have been furnished to us and our opinion, insofar as it relates to the amounts included for those investees, is based solely on the reports of the other auditors. The aggregate carrying values of those investments were 1% (NT\$2,405,019,000) and 3% (NT\$5,716,523,000) of the Company's total assets as of December 31, 2003 and 2002, respectively. The Company's shares in these investees' net income were 11% (NT\$184,862,000) and 26% (NT\$761,030,000) of pretax income of the Company for the years ended December 31, 2003 and 2002, respectively.

We conducted our audits in accordance with the Rules Governing Auditing and Certification of Financial Statements by Certified Public Accountants and generally accepted auditing standards in the Republic of China. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the reports of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of China Airlines, Ltd. as of December 31, 2003 and 2002 and the results of its operation and its cash flows for the years then ended, in conformity with Guidelines for Securities Issuers' Financial Reporting and generally accepted accounting principles in the Republic of China.

#### Notice to Readers

The accompanying financial statements are intended only to present the financial position, results of operations and cash flows in accordance with accounting principles and practices generally accepted in the Republic of China and not those of any other jurisdictions. The standards, procedures and practices to audit such financial statements are those generally accepted and applied in the Republic of China.

English Translation of Financial Statements Originally Issued in Chinese

CHINA AIRLINES, LTD.

BALANCE SHEETS

DECEMBER 31, 2003 AND 2002

(In Thousands of New Taiwan Dollars and Shares, Except Par Value)

ASSETS	2003		2002	
	Amount	%	Amount	%
<b>CURRENT ASSETS</b>				
Cash (Note 3)	\$ 6,759,816	4	\$ 1,849,134	1
Short-term investments—net (Notes 2 and 4)	10,103,718	5	188,198	-
Receivables:				
Notes and accounts—net (Notes 2 and 5)	5,740,806	3	5,036,166	3
Related parties (Note 23)	301,010	-	271,205	-
Other receivables (Note 6)	1,624,357	1	1,223,020	1
Pledged certificates of deposit (Note 24)	280,459	-	278,746	-
Inventories—net (Notes 2, 7 and 24)	5,249,167	3	5,945,964	4
Prepaid expenses (Note 8)	286,999	-	127,908	-
Deferred income tax assets—current (Notes 2 and 19)	214,336	-	280,569	-
Other current assets	791,684	-	957,257	1
<b>Total current assets</b>	<b>31,352,352</b>	<b>16</b>	<b>16,158,167</b>	<b>10</b>
<b>INVESTMENTS IN SHARES OF STOCK (Notes 2 and 9)</b>				
Equity method	6,779,462	3	7,141,124	4
Cost method	1,064,162	1	1,094,952	1
<b>Total investments in shares of stock</b>	<b>7,843,624</b>	<b>4</b>	<b>8,236,076</b>	<b>5</b>
<b>OTHER FINANCIAL ASSETS—Noncurrent</b>	<b>11,451</b>	<b>-</b>	<b>21,456</b>	<b>-</b>
<b>PROPERTIES (Notes 2, 10 and 24)</b>				
Cost				
Land	2,153,583	1	2,153,583	1
Building	7,647,484	4	7,599,530	5
Machinery and equipment	3,109,046	2	3,142,038	2
Flight equipment	119,918,862	63	107,401,188	66
Furniture	839,907	1	859,376	-
Leased flight and other equipment	23,484,563	12	43,461,824	27
Leasehold improvements	439,137	-	411,466	-
Revaluation increase	50,335	-	218,095	-
Total cost and revaluation increase	157,642,917	83	165,247,100	101
Accumulated depreciation	35,284,524	19	45,671,027	28
	122,358,393	64	119,576,073	73
Advance payments on equipment purchase contracts (Note 25)	19,751,912	10	12,847,894	8
<b>Net properties</b>	<b>142,110,305</b>	<b>74</b>	<b>132,423,967</b>	<b>81</b>
<b>INTANGIBLE ASSETS</b>				
Computer software—net (Note 2)	182,739	-	140,721	-
Prepaid pension cost (Notes 2 and 16)	2,743,929	2	2,621,386	2
<b>Net intangible assets</b>	<b>2,926,668</b>	<b>2</b>	<b>2,762,107</b>	<b>2</b>
<b>OTHER ASSETS</b>				
Idle properties—net	713,775	-	219,454	-
Deposits (Note 25)	5,016,199	3	3,705,120	2
Deferred charges (Note 2)	85,064	-	184,741	-
Deferred income tax assets—noncurrent (Notes 2 and 19)	815,728	1	-	-
<b>Net other assets</b>	<b>6,630,766</b>	<b>4</b>	<b>4,109,315</b>	<b>2</b>
<b>TOTAL ASSETS</b>	<b>\$ 190,875,166</b>	<b>100</b>	<b>\$ 163,711,088</b>	<b>100</b>

LIABILITIES AND STOCKHOLDERS' EQUITY	2003		2002	
	Amount	%	Amount	%
<b>CURRENT LIABILITIES</b>				
Short-term loans (Notes 11 and 24)	\$ 3,600,000	2	\$ 2,819,512	2
Commercial paper (Note 12)	1,823,478	1	1,569,176	1
Accounts payable	676,377	-	562,397	-
Payable to related parties (Note 23)	890,530	1	823,173	-
Accrued expenses (Note 2)	8,309,866	4	7,741,925	5
Bonds issued—current portion (Notes 2 and 13)	3,900,000	2	433,900	-
Advance ticket sales (Note 2)	3,298,252	2	3,250,081	2
Loans and debts—current portion (Notes 14 and 24)	11,985,946	6	8,847,212	5
Capital lease obligations—current portion (Notes 2 and 15)	1,215,321	1	2,121,796	1
Other current liabilities	859,908	-	836,536	1
<b>Total current liabilities</b>	<b>36,559,678</b>	<b>19</b>	<b>29,005,708</b>	<b>17</b>
<b>LONG-TERM DEBTS</b>				
Bonds issued—net of current portion (Notes 2 and 13)	8,100,000	4	8,000,000	5
Loans and debts—net of current portion (Notes 14 and 24)	76,587,082	40	52,515,169	32
Capital lease obligations—net of current portion (Notes 2 and 15)	12,766,936	7	21,200,982	13
<b>Total long-term debts</b>	<b>97,454,018</b>	<b>51</b>	<b>81,716,151</b>	<b>50</b>
<b>OTHER LIABILITIES</b>				
Deferred pension cost (Notes 2 and 16)	4,868,873	3	4,243,563	3
Deferred profit on sale-leaseback (Note 2)	2,929,679	2	900,869	1
Deferred income tax liabilities—noncurrent (Notes 2 and 19)	-	-	305,529	-
Others	693,466	-	751,109	-
<b>Total other liabilities</b>	<b>8,492,018</b>	<b>5</b>	<b>6,201,070</b>	<b>4</b>
<b>Total liabilities</b>	<b>142,505,714</b>	<b>75</b>	<b>116,922,929</b>	<b>71</b>
<b>STOCKHOLDERS' EQUITY</b>				
Capital stock, \$10 par value				
Authorized—3,970,000 shares in 2003 and 2,960,000 shares in 2002				
Issued and outstanding—2,848,929 shares in 2003 and 2,542,796 shares in 2002	28,489,288	15	25,427,956	16
Capital surplus				
Issue of stock in excess of par value	7,157,448	4	7,104,934	4
Revaluation increment on properties	830,471	-	830,471	1
Share in capital surplus reported by equity-method investees	660	-	-	-
Gain on sale of treasury shares	71,502	-	21,951	-
Others	5,044	-	5,044	-
Total capital surplus	8,065,125	4	7,962,400	5
Retained earnings				
Legal reserve	3,994,172	2	3,572,557	2
Unappropriated earnings	8,050,544	4	9,403,939	6
Total retained earnings	12,044,716	6	12,976,496	8
Unrealized loss on investments in shares of stock	(46,156)	-	(26,746)	-
Cumulative translation adjustments	144,476	-	637,791	-
Unrecognized pension cost	(292,504)	-	-	-
Company shares held by subsidiaries reclassified as treasury stock	(35,493)	-	(189,738)	-
<b>Total stockholders' equity</b>	<b>48,369,452</b>	<b>25</b>	<b>46,788,159</b>	<b>29</b>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$ 190,875,166</b>	<b>100</b>	<b>\$ 163,711,088</b>	<b>100</b>

The accompanying notes are an integral part of the financial statements.

(With Deloitte & Touche auditors' report dated February 25, 2004)

**English Translation of Financial Statements Originally Issued in Chinese**

**CHINA AIRLINES, LTD.**

**STATEMENTS OF INCOME**

**FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002**

**(In Thousands of New Taiwan Dollars and Shares, Except Earnings Per Share)**

	2003		2002	
	Amount	%	Amount	%
REVENUES (Notes 2 and 23)				
Passenger	\$ 36,565,052	48	\$ 41,971,310	53
Cargo	34,891,924	46	32,858,648	42
Others	4,402,160	6	4,107,783	5
Total operating revenues	75,859,136	100	78,937,741	100
COSTS (Notes 21 and 23)				
Flying operations	32,255,195	42	31,845,618	40
Terminal and landing fees	13,402,339	18	13,487,976	17
Passenger service	6,769,191	9	6,417,651	8
Aircraft maintenance	5,172,235	7	6,857,405	9
Others	2,871,266	4	2,511,607	3
Total operating costs	60,470,226	80	61,120,257	77
GROSS PROFIT	15,388,910	20	17,817,484	23
OPERATING EXPENSES (Note 21)				
Marketing and selling	10,294,207	13	10,320,441	13
General and administrative	2,276,826	3	2,221,296	3
Total operating expenses	12,571,033	16	12,541,737	16
OPERATING INCOME	2,817,877	4	5,275,747	7
NONOPERATING INCOME AND GAIN				
Interest	87,000	-	136,110	-
Equity in investees' net income—net (Notes 2 and 9)	198,447	-	347,689	1
Other investment income	175,307	-	147,286	-
Gain on disposal of properties—net (Note 2)	339,787	1	31,904	-
Gain on disposal of investments—net	109,908	-	132,234	-
Gain on physical inventory	8,028	-	13,468	-
Other	1,045,180	1	929,243	1
Total nonoperating income and gain	1,963,657	2	1,737,934	2
NONOPERATING EXPENSES AND LOSSES				
Interest	2,620,655	3	3,247,716	4
Foreign exchange loss—net (Note 2)	79,253	-	270,717	-
Other	456,728	1	513,654	1
Total nonoperating expenses and losses	3,156,636	4	4,032,087	5

(Continued)

**English Translation of Financial Statements Originally Issued in Chinese**

	<u>2003</u>		<u>2002</u>	
	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>
PRETAX INCOME AND EXTRAORDINARY ITEM	\$ 1,624,898	2	\$ 2,981,594	4
INCOME TAX BENEFIT (Notes 2 and 19)	<u>154,568</u>	<u>-</u>	<u>154,695</u>	<u>-</u>
INCOME BEFORE EXTRAORDINARY LOSS	1,779,466	2	3,136,289	4
EXTRAORDINARY LOSS—Net of tax effects of \$5,615 (Note 20)	<u>-</u>	<u>-</u>	<u>16,845</u>	<u>-</u>
NET INCOME	<u>\$ 1,779,466</u>	<u>2</u>	<u>\$ 3,119,444</u>	<u>4</u>
	<u>2003</u>		<u>2002</u>	
	<u>Before Tax</u>	<u>After Tax</u>	<u>Before Tax</u>	<u>After Tax</u>
EARNINGS PER SHARE (Note 22)				
Basic earnings per share				
Income before extraordinary loss	\$ 0.58	\$ 0.64	\$ 1.07	\$ 1.12
Extraordinary loss	<u>-</u>	<u>-</u>	<u>( 0.01)</u>	<u>( 0.01)</u>
Net income	<u>\$ 0.58</u>	<u>\$ 0.64</u>	<u>\$ 1.06</u>	<u>\$ 1.11</u>
Diluted earnings per share				
Income before extraordinary loss	\$ 0.58	\$ 0.63	\$ 1.06	\$ 1.11
Extraordinary loss	<u>-</u>	<u>-</u>	<u>( 0.01)</u>	<u>( 0.01)</u>
Net income	<u>\$ 0.58</u>	<u>\$ 0.63</u>	<u>\$ 1.05</u>	<u>\$ 1.10</u>

The accompanying notes are an integral part of the financial statements.

(With Deloitte & Touche auditors' report dated February 25, 2004)

(Concluded)

## CHINA AIRLINES, LTD.

STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY  
FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002  
(In Thousands of New Taiwan Dollars and Shares, Except Cash Dividends)

	Capital Stock		Capital Surplus (Notes 2 and 17)							Retained Earnings (Notes 2 and 17)			Company Shares Held by Subsidiaries Reclassified as Treasury Stock (Notes 2 and 18)	Net Loss Not Recognized as Pension Cost (Note 2)	Unrealized Loss on Investments in Shares of Stock (Note 2)	Cumulative Translation Adjustments (Note 2)	Total Stockholders' Equity
	Issued		Issue of stock in excess of par value	Revaluation increment on property	Gain on disposal of property and equipment	Share in capital surplus reported by equity-method investees	Gain on subsidiaries' sale of treasury shares	Others	Total	Legal reserve	Unappropriated earnings	Total					
	Shares	Amount															
BALANCE, JANUARY 1, 2002	2,423,899	\$ 24,238,993	\$ 7,104,445	\$ 830,471	\$ 1,062,895	\$ 20,113	\$ -	\$ 5,009	\$ 9,022,933	\$ 3,394,044	\$ 6,930,736	\$ 10,324,780	\$ -	\$ -	(\$ 11,358)	\$ 1,045,011	\$ 44,620,359
Appropriation of 2001 earnings																	
Legal reserve	-	-	-	-	-	-	-	-	-	178,513	( 178,513)	-	-	-	-	-	-
Bonus to employees (stocks)	9,640	96,397	-	-	-	-	-	-	-	-	( 96,397)	( 96,397)	-	-	-	-	-
Cash dividends—\$0.15 per share	-	-	-	-	-	-	-	-	-	-	( 363,584)	( 363,584)	-	-	-	-	( 363,584)
Stock dividends—4.5%	109,076	1,090,755	-	-	-	-	-	-	-	-	( 1,090,755)	( 1,090,755)	-	-	-	-	-
Company shares held by subsidiaries reclassified as treasury stock—15,501 shares	-	-	-	-	-	-	-	-	-	-	-	-	( 189,738)	-	-	-	( 189,738)
Gain on sale of Company shares held by subsidiaries	-	-	-	-	-	-	21,951	-	21,951	-	-	-	-	-	-	-	21,951
Translation adjustments	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	( 2,968)	( 2,968)
Translation adjustments on a foreign operating entity	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	( 404,252)	( 404,252)
Capital surplus from investments in shares of stock—reserve	-	-	-	-	-	( 20,113)	-	-	( 20,113)	-	20,113	20,113	-	-	-	-	-
Conversion of bonds to capital stock	181	1,811	489	-	-	-	-	-	489	-	-	-	-	-	-	-	2,300
Unrealized loss on investments in shares of stock	-	-	-	-	-	-	-	-	-	-	-	-	-	( 15,388)	-	-	( 15,388)
Debit of overdue dividends to capital surplus	-	-	-	-	-	-	-	35	35	-	-	-	-	-	-	-	35
Reclassification of gain on disposal of properties	-	-	-	-	( 1,062,895)	-	-	-	( 1,062,895)	-	1,062,895	1,062,895	-	-	-	-	-
Net income in 2002	-	-	-	-	-	-	-	-	-	-	3,119,444	3,119,444	-	-	-	-	3,119,444
BALANCE, DECEMBER 31, 2002	2,542,796	25,427,956	7,104,934	830,471	-	-	21,951	5,044	7,962,400	3,572,557	9,403,939	12,976,496	( 189,738)	-	( 26,746)	637,791	46,788,159
Appropriation of 2002 earnings																	
Legal reserve	-	-	-	-	-	-	-	-	-	421,615	( 421,615)	-	-	-	-	-	-
Bonus to employees	16,845	168,450	-	-	-	-	-	-	-	-	( 168,450)	( 168,450)	-	-	-	-	-
Stock dividends—10%	254,280	2,542,796	-	-	-	-	-	-	-	-	( 2,542,796)	( 2,542,796)	-	-	-	-	-
Unrealized loss on investments in shares of stock	-	-	-	-	-	-	-	-	-	-	-	-	-	( 19,410)	-	-	( 19,410)
Share in capital surplus reported by equity-method investees	-	-	-	-	-	660	-	-	660	-	-	-	-	-	-	-	660
Conversion of bonds to capital stock	35,008	350,086	52,514	-	-	-	-	-	52,514	-	-	-	-	-	-	-	402,600
Translation adjustments on a foreign operating entity (Note 2)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	( 471,025)	( 471,025)
Translation adjustments	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	( 22,290)	( 22,290)
Net loss not recognized as pension cost	-	-	-	-	-	-	-	-	-	-	-	-	-	( 292,504)	-	-	( 292,504)
Capital surplus from sale of Company shares held by subsidiaries	-	-	-	-	-	-	49,551	-	49,551	-	-	-	154,245	-	-	-	203,796
Net income in 2003	-	-	-	-	-	-	-	-	-	-	1,779,466	1,779,466	-	-	-	-	1,779,466
BALANCE, DECEMBER 31, 2003	2,848,929	\$ 28,489,288	\$ 7,157,448	\$ 830,471	\$ -	\$ 660	\$ 71,502	\$ 5,044	\$ 8,065,125	\$ 3,994,172	\$ 8,050,544	\$ 12,044,716	(\$ 35,493)	(\$ 292,504)	(\$ 46,156)	\$ 144,476	\$ 48,369,452

The accompanying notes are an integral part of the financial statements.

(With Deloitte &amp; Touche auditors' report dated February 25, 2004)

**English Translation of Financial Statements Originally Issued in Chinese**

**CHINA AIRLINES, LTD.**

**STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002  
(In Thousands of New Taiwan Dollars)**

	<u>2003</u>	<u>2002</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$ 1,779,466	\$ 3,119,444
Adjustments to reconcile net income to net cash provided by operating activities:		
Unrealized loss on short-term investments (reversal)	( 15,520)	14,940
Reversal of allowance for doubtful receivables	-	( 4,907)
Depreciation and amortization	6,832,984	6,944,173
Loss (gain) on disposal of investments in shares of stock—net	( 20)	3,459
Gain on disposal of properties—net	( 339,787)	( 34,809)
Gain on disposal of idle properties—net	( 127,080)	-
Net loss on inventories, properties and idle properties	220,052	514,359
Amortization of deferred profit on sale-leaseback	( 311,285)	( 200,470)
Amortization of deferred credits	( 66,442)	( 69,785)
Equity in investees' net gain less cash dividends received	548,373	516,509
Reversal of capital lease obligations	( 981,738)	-
Gain on liquidation of investments in shares of stock	( 1,109)	-
Deferred income taxes	( 1,055,024)	( 198,002)
Changes in operating assets and liabilities—net:		
Decrease (increase) in:		
Notes and accounts receivable—third parties	( 704,640)	( 80,057)
Notes and accounts receivable—related parties	( 29,805)	( 144,482)
Other receivables	( 393,669)	463,334
Inventories	( 176,753)	( 668,732)
Prepaid expenses	( 159,091)	327,776
Other current assets	165,573	( 159,392)
Increase (decrease) in:		
Accounts payable	113,980	( 125,317)
Payable to related parties	67,357	205,501
Accrued expenses	197,044	1,469,339
Advance ticket sales	48,170	493,782
Other current liabilities	23,372	255,241
Provision for pension cost	210,263	13,300
Net cash provided by operating activities	<u>5,844,671</u>	<u>12,655,204</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Decrease (increase) in short-term investments	( 9,900,000)	391,038
Increase in pledged certificate of deposits	( 1,713)	( 278,746)
Proceeds from disposal of investments in shares of stock	296	33,908
Addition to investments in shares of stock	-	( 35)
Decrease in other financial assets—noncurrent	10,005	509,356
Proceeds from disposal of properties	6,321,149	425,106
Additions to properties	( 27,760,977)	( 24,416,878)

(Continued)

**English Translation of Financial Statements Originally Issued in Chinese**

	<u>2003</u>	<u>2002</u>
Proceeds from disposal of idle properties	\$ 258,348	\$ -
Decrease (increase) in deposits made	( 1,311,079)	130,785
Increase in computer software	( 49,329)	( 46,907)
Decrease (increase) in deferred charges	( 19,368)	459,880
Net cash used in investing activities	( 32,452,668)	( 22,792,493)
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from short-term loans	780,488	2,619,512
Proceeds from (repayments on) commercial paper	254,302	( 254,216)
Proceeds from long-term loans	36,172,653	16,190,525
Repayments of long-term loans	( 9,767,161)	( 9,534,439)
Proceeds from bonds issued	4,000,000	2,000,000
Redemption of convertible bonds	( 31,300)	-
Increase in deposits-in	8,800	4,130
Payments of cash dividends	-	( 363,421)
Net cash provided by financing activities	<u>31,417,782</u>	<u>10,662,091</u>
INCREASE (DECREASE) IN CASH	4,809,785	524,802
EFFECTS OF EXCHANGE RATE CHANGES	100,897	71,407
CASH, BEGINNING OF YEAR	<u>1,849,134</u>	<u>1,252,925</u>
CASH, END OF YEAR	<u>\$ 6,759,816</u>	<u>\$ 1,849,134</u>
<b>SUPPLEMENTAL INFORMATION</b>		
Interest paid	\$ 2,801,916	\$ 3,583,782
Less—capitalized interest	<u>277,320</u>	<u>149,897</u>
Interest paid (excluding capitalized interest)	<u>\$ 2,524,596</u>	<u>\$ 3,433,885</u>
Income taxes paid	<u>\$ 49,271</u>	<u>\$ 37,693</u>
<b>NONCASH INVESTING AND FINANCING ACTIVITIES</b>		
Company shares held by subsidiaries reclassified from investment in shares of stock to treasury stock	<u>\$ -</u>	<u>\$ 189,738</u>
Current portion of long-term debts	<u>\$ 11,985,946</u>	<u>\$ 8,847,212</u>
Current portion of capital lease obligations	<u>\$ 1,215,321</u>	<u>\$ 2,121,796</u>
Current portion of bonds issued	<u>\$ 3,900,000</u>	<u>\$ 433,900</u>
Conversion of convertible bonds to capital stock	<u>\$ 402,600</u>	<u>\$ 2,300</u>

The accompanying notes are an integral part of the financial statements.

(With Deloitte & Touche auditors' report dated February 25, 2004)

(Concluded)

**CHINA AIRLINES, LTD.**

**NOTES TO FINANCIAL STATEMENTS  
FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002  
(Amounts in New Taiwan Dollars, Unless Specified Otherwise)**

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**1. ORGANIZATION AND OPERATIONS**

China Airlines, Ltd. (the “Company”) was founded in 1959 and its stocks are listed on the Taiwan Stock Exchange. The Company primarily provides air transport services for passengers and cargo. Its other operations include (a) provision of mail services; (b) provision of ground services and routine aircraft maintenance; (c) major maintenance of flight equipment; (d) provision of communications and data processing services to other airlines; (e) sale of aircraft parts, equipment and entire aircraft; and (f) lease of aircraft.

The Company is a subsidiary of China Aviation Development Foundation, which held 70.05 % and 71.35% of the shares of the Company as of December 31, 2003 and 2002, respectively. The Company had 9,124 and 9,263 employees as of December 31, 2003 and 2002, respectively.

**2. SUMMARY OF SIGNIFICANT  
ACCOUNTING POLICIES**

The Company’s significant accounting policies, which conform to Guidelines for Securities Issuers’ Financial Reporting and generally accepted accounting principles in the Republic of China, are summarized below. Under these guidelines and principles, the Company has to estimate the allowance for doubtful receivables, loss on market decline of inventories, accrued expenses—frequent flyer program, property depreciation, prepaid pension cost and loss on pending lawsuits. Since operating circumstances are inherently uncertain, estimates may differ from actual results.

**Current or Noncurrent Assets and Liabilities**

Assets to be realized, received or used up within a year are classified as current. Liabilities to be paid off or settled within a year are classified as current. Other assets and liabilities are classified as noncurrent.

**Short-term investments**

These are investments in marketable equity securities and mutual funds. Domestic and foreign investments are stated at aggregate cost less allowance for losses on decline in market value below carrying value or on the net asset value (mutual funds). The allowance is reversed when the market value and/or net asset value recovers. Costs of marketable equity securities and mutual fund beneficiary certificates sold are determined using the weighted-average method and the specific identification method, respectively.

**Allowances for Doubtful Accounts**

Allowances for doubtful notes and accounts receivable are provided on the basis of an evaluation of their collectibility.

**Inventories**

Inventories are primarily expendable and nonexpendable parts and materials, supplies used in operation and items for in-flight sale. These are valued using the weighted-average cost less allowance for obsolescence. Items for in-flight sale are stated at the lower of weighted-average cost or market (replacement cost or net realizable value). The costs of inventories sold or consumed are determined using the weighted-average method.

## **Investments in Shares of Stock**

Investments in shares of stock in which the Company exercises significant influence over their operating and financial policy decisions are accounted for by the equity method. Under the equity method, investments are stated at cost on the acquisition date and subsequently adjusted for the Company's proportionate share or equity in the net income or net loss of the investees. When a stock is acquired or when the equity method is initially adopted, the difference between the investment acquisition cost and the Company's equity in the net assets of the investees is amortized over five years. The unrealized loss on cost-method investments is also recognized at the Company's equity in the investee and shown as part of the stockholders' equity. Cash dividends received are accounted for as a reduction of the carrying values of the investments. When a Company subscribes to additional shares of stock issued by an investee at a rate not equal to the Company's current equity, the increase in the Company's equity in the investee's net assets is credited to capital surplus. Any decrease in the Company's equity in the investee's net assets is debited to capital surplus. If capital surplus is not enough for debiting purposes, the remaining difference is debited to unappropriated earnings.

Other investments in shares of stocks are stated at cost. For stocks with quoted market prices, an allowance is recognized for a decline in market value below carrying value and is either debited to stockholders' equity if the decline is considered temporary or charged to income if the decline is other than temporary. For stocks with no quoted market prices, the carrying amount of the investment is reduced to reflect other than temporary decline of market value below carrying value. Cash dividends received a year after acquisition are recognized as investment income.

For both equity-method and cost-method investments, stock dividends received are recorded only as an increase in the number of shares held and not as investment income.

Costs of investments sold are determined using the weighted-average method.

Gain or loss from the transactions involving depreciable assets between the Company and its equity-method investees is deferred and recognized over the estimated useful lives of the assets.

The Company adopted a new accounting principle, which took effect on January 1, 2002, that requires the Company to reclassify the Company's shares held by its subsidiaries as treasury stock at the carrying value shown in the subsidiaries' books on January 1, 2002. This accounting change had no material impact on the Company's financial statements as of December 31, 2002.

## **Properties**

Properties are stated at cost plus revaluation increment (if any) less accumulated depreciation. Major betterments or renewals are capitalized, while maintenance and repairs are expensed when incurred. Interests on funds used to acquire flight equipment before the date the equipment is used in operations and to construct facilities are capitalized and included in the cost of the related assets.

Depreciation is calculated using the straight-line method over service lives estimated as follows (plus one year to represent estimated salvage value): buildings, 45 to 55 years; machinery and equipment, 5 to 6 years; flight equipment, 5 to 25 years; furniture, 5 years; leased assets, 6 to 25 years; and leasehold improvements, 5 years. Properties that have reached their residual value but are still in use are further depreciated over their newly estimated service lives.

Upon property sale or other disposal, the cost, revaluation increment (if any) and the related accumulated depreciation are removed from the accounts, and gain or loss is credited or charged to nonoperating income or expenses.

## **Leased Flight and Other Equipment**

The amounts capitalized on flight and other equipment leased under capital lease agreements are the lower of the present value of all payments required under the lease agreements or the fair value of the leased assets on the starting dates of the agreements. Interests implicit in lease payments are recorded as interest expense.

Amounts paid under operating lease agreements are charged to income over the term of the agreements. The imputed interest on rental deposits, calculated at the interest rate for one-year time deposits, is recorded both as rental expense and interest income.

## **Computer Software Costs**

Computer software costs are amortized using the straight-line method over the estimated useful lives of the software.

## **Other Assets—Deferred Charges**

Deferred charges mainly consist of (a) expenses for training pilots in operating new types of aircraft, (b) issue costs of corporate bonds and (c) costs incurred for syndicated loans. They are amortized using the straight-line method over the bond or loan terms.

## **Frequent-flyer Program**

Passengers who are members of the Dynasty Club may accumulate mileage points that entitle them to choose among various awards (including an upgrade to a higher class or free tickets). A liability is accrued and charged to operating expense when a passenger reaches a certain award level. The amount accrued is based on the estimated incremental cost that will be incurred upon the provision of transport services.

## **Convertible Bonds**

Redemption price in excess of the face value of the bonds is accrued over the period from the issue date up to the redemption date using the effective interest rate method.

The net carrying amount of the bonds (the face amount plus redemption premium accrued to the date of conversion but will not be paid) is credited to the appropriate capital accounts (capital stock equal to par value, with the balance credited to capital surplus) upon conversion of the bonds. No gain or loss is recognized on such conversions.

## **Pension Costs**

Pension costs are recognized on the basis of actuarial calculations. Unrecognized net transition obligation is amortized over 15 years, while pension gain or loss is amortized using the straight-line method based on the average remaining service years of employees.

If additional accrued pension cost based on actuarial calculations is not in excess of the sum of unamortized balance on prior service and unrecognized net transition obligation, “deferred pension cost” will be debited. Otherwise, the excess amount should be debited to “unrecognized pension cost” and recorded as decreases in stockholder’s equity.

## **Unearned Gain on Sale-Leasebacks**

A gain on the sale by the Company of assets that it leases back is deferred and amortized over the term of the lease agreements.



## **Income Tax**

Deferred tax assets are recognized for the tax effects of deductible temporary differences, loss carryforwards and unused investment credits, and deferred tax liabilities are recognized for the tax effects of taxable temporary differences. Deferred tax liabilities and assets are classified as current or noncurrent on the basis of the classification of the related asset or liability for financial reporting. A deferred tax asset or liability that cannot be related to an asset or liability for financial reporting, such as deferred tax assets related to net loss carryforwards, is classified according to the expected reversal or realization date of the temporary difference. Valuation allowance is recognized on deferred tax assets that are not expected to be realized.

Income tax credits for certain acquisitions of eligible equipment or technology, research and development expenses, personnel training expenses and investments in shares of stock are recognized in the period those acquisitions or expenses are paid.

Adjustments to prior year's tax liabilities are added to or deducted from the current year's income tax expense.

Income taxes (10%) on undistributed earnings are recorded as expense in the year when the stockholders resolve to retain the earnings.

## **Revenues**

Passenger fares and cargo revenues are recognized when transportation is provided. The value of unused passenger tickets is recognized as "advance ticket sales."

## **Foreign-currency Transactions, Transactions of Foreign Subsidiaries or Foreign operating Entity**

The Company maintains its accounts and expresses its financial statements in New Taiwan dollars. Foreign-currency transactions (except derivative transactions) are recorded in New Taiwan dollars at the rates of exchange in effect when the transactions occur. Gains or losses resulting from the application of different foreign exchange rates when foreign-currency assets and liabilities are settled, are credited or charged to income in the period of settlement.

The year-end balances of foreign-currency assets and liabilities are restated at the prevailing exchange rates, and the resulting differences are recorded as follows:

- a. Cost-method investments in shares of stock—as translation adjustment if the translated New Taiwan dollar amounts results in a lower amount; otherwise, no adjustment is made.
- b. Other assets and liabilities—as credits or charges to income.

Equity-method investments in foreign subsidiaries/affiliates are recorded in New Taiwan dollars using the rates of exchange in effect on acquisition dates. On balance sheet dates, the investments and the related equity in net income or net loss are restated at the prevailing exchange rates and weighted-average rates, respectively, and resulting differences are recorded as translation adjustments under stockholders' equity.

Under a regulation by the Securities and Futures Commission, the carrying amount of an aircraft acquired and the related US dollar-denominated obligation incurred for the acquisition is accounted for as an investment in a foreign operating entity if the Company's use of the aircraft results in generating revenues and incurring expenses mainly in US dollars. On balance sheet date, the carrying amount of the aircraft and the related liability are restated at balance sheet date rates. The difference is recognized in stockholders' equity as translation adjustment.

## Derivative Financial Instruments

The Company uses derivative financial instruments for hedging purposes, as follows:

a. Forward exchange contracts

Forward exchange contracts are recorded in New Taiwan dollars as receivables and/or payables at spot rates on the starting dates of the contracts. The premium or discount, computed by multiplying the contract amount by the difference between the contracted forward rate and the starting date spot rates, is also recognized. The premium or discount is amortized using the straight-line method over the term of the forward contract, with the amortization charged to income. On the balance sheet dates, the gains or losses on the contracts, computed by multiplying the contract amounts by the difference between the starting date spot rates and the balance sheet date spot rates (or the spot rates last used to measure a gain or loss on that contract for an earlier period), are charged to income or adjusted “advances for equipment acquisition” in the properties section of the balance sheets. Also, the receivables and payables related to the forward contracts are netted out, and the resulting amount is presented as either an asset or a liability.

b. Foreign-currency options

Premiums paid or received for options are recorded as assets or liabilities, respectively. They are amortized equally over the term of the contract and recognized as revenue or expense. Gain or loss on the exercise of the options is credited or charged to current income of the item being hedged.

c. Interest rate swaps

The contract (notional) amounts of interest rate swap agreements, which are used to hedge interest rate fluctuations on existing obligations, are not recognized as assets or liabilities since the agreements do not require the exchange of such amounts. The net amounts paid or received under the agreements as of the balance sheets dates and on the settlement dates are recognized as adjustments to the interest income or expense of the hedged obligations.

d. Cross-currency swap

Cross-currency swap agreements are entered into as hedges against interest rate fluctuations on existing obligations. Assets and liabilities arising from these agreements are recorded at the contracted forward rates. The net interest on each settlement is recorded as an adjustment to the revenue or expense associated with the item being hedged. On the balance sheet dates, the forward currency receivables or payables are restated at the prevailing spot rates, and the resulting differences are credited or charged to current income.

The result of netting out receivables and payables on cross-currency swap agreements are recorded either as assets or liabilities.

e. Foreign-currency swap

Foreign-currency spot-position assets or liabilities on foreign-currency swap contracts are recorded at spot rates when the transactions occur, while the corresponding forward-position assets or liabilities are recorded at the contracted forward rates. The difference between the spot rate on the contract date and contracted forward rate is amortized using the straight-line method over the term of the contract and recorded as interest income or expense. On the balance sheet dates, receivables and payables of open contracts are netted out.

f. Fuel price hedging contracts

The Company enters into fuel price hedging contracts to manage its exposures to increases in jet fuel prices. The receivables or payables on these contracts are calculated on the basis of the difference between the agreed price and the market price of fuel products as of the settlement date or the balance sheet date and are recognized as a component of jet fuel expense.

**Reclassifications**

Certain accounts for 2002 have been reclassified to conform to the 2003 financial statement presentation.

**3. CASH**

	<u>December 31</u>	
	<u>2003</u>	<u>2002</u>
Cash on hand	\$ 14,766,263	\$ 2,428,606
Revolving fund	675,358,056	288,216,648
Cash in banks	1,218,773,759	1,533,488,692
Certificates of deposit	<u>4,850,918,307</u>	<u>25,000,000</u>
	<u>\$ 6,759,816,385</u>	<u>\$ 1,849,133,946</u>

**4. SHORT-TERM INVESTMENTS**

	<u>December 31</u>	
	<u>2003</u>	<u>2002</u>
Domestic marketable equity securities	\$ 114,755,878	\$ 114,755,878
Foreign marketable equity securities	88,962,451	88,962,451
Bond type mutual funds	<u>9,900,000,000</u>	<u>-</u>
	10,103,718,329	203,718,329
Less: Allowance for losses	<u>-</u>	<u>15,519,878</u>
	<u>\$ 10,103,718,329</u>	<u>\$ 188,198,451</u>
Market value		
Domestic marketable equity securities and bond type mutual funds	\$ 10,020,148,981	\$ 99,240,000
Foreign marketable equity securities	<u>181,780,859</u>	<u>126,456,864</u>
	<u>\$ 10,201,929,840</u>	<u>\$ 225,696,864</u>

The total market value of the marketable equity securities and the open-end mutual funds are calculated at the average closing prices for December and the net asset values on December 31, respectively.

**5. NOTES AND ACCOUNTS RECEIVABLE—  
THIRD PARTIES**

	<u>December 31</u>	
	<u>2003</u>	<u>2002</u>
Notes receivable	\$ 265,742,353	\$ 252,023,235
Accounts receivable	<u>5,523,569,888</u>	<u>4,839,524,929</u>
	5,789,312,241	5,091,548,164
Less: Allowance for doubtful accounts	<u>48,506,397</u>	<u>55,382,540</u>
	<u>\$ 5,740,805,844</u>	<u>\$ 5,036,165,624</u>

**6. OTHER RECEIVABLES**

	<u>December 31</u>	
	<u>2003</u>	<u>2002</u>
Interest and others	\$ 1,374,101,207	\$ 969,498,021
Tax refunds	245,717,899	230,216,334
Others	<u>4,538,299</u>	<u>23,305,813</u>
	<u>\$ 1,624,357,405</u>	<u>\$ 1,223,020,168</u>

**7. INVENTORIES**

	<u>December 31</u>	
	<u>2003</u>	<u>2002</u>
Aircraft spare parts	\$ 4,541,789,197	\$ 5,495,784,445
Items for in-flight sale	363,714,548	345,341,225
Work in process—maintenance services	<u>392,662,049</u>	<u>163,408,660</u>
	5,298,165,794	6,004,534,330
Less: Allowance for losses	<u>48,999,194</u>	<u>58,570,596</u>
	<u>\$ 5,249,166,600</u>	<u>\$ 5,945,963,734</u>

**8. PREPAID EXPENSES**

	<u>December 31</u>	
	<u>2003</u>	<u>2002</u>
Prepaid insurance	\$ 27,970,366	\$ 19,261,272
Prepaid aircraft rentals	133,873,359	72,816,580
Others	<u>125,155,115</u>	<u>35,830,092</u>
	<u>\$ 286,998,840</u>	<u>\$ 127,907,944</u>

**9. INVESTMENTS IN SHARES OF STOCK**

	<u>December 31</u>			
	<u>2003</u>		<u>2002</u>	
	<u>Carrying</u>	<u>% of</u>	<u>Carrying</u>	<u>% of</u>
	<u>Value</u>	<u>Ownership</u>	<u>Value</u>	<u>Ownership</u>
<u>Equity method</u>				
Taiwan Air Cargo Terminal	\$1,668,302,636	54.00	\$1,912,167,897	54.00
China Pacific Catering Services	864,196,663	51.00	887,018,034	51.00
Cal-Dynasty International	816,757,176	100.00	800,814,041	100.00
Taoyuan International Airport Service	768,279,978	49.00	829,128,352	49.00
Mandarin Airlines	736,714,570	90.05	963,612,627	90.05
Hwa Sheng Investment	517,935,309	100.00	303,293,548	100.00
Abacus Distribution Systems (Taiwan)	391,719,910	93.93	378,877,129	93.93
Taiwan Airport Service	337,237,539	47.35	357,123,160	47.35
Kaoshiung Catering Services	155,148,478	31.76	137,401,636	33.00
Cal-Asia Investment	147,288,230	100.00	146,412,170	100.00
Asian Compressor Technology Service	145,241,480	24.50	182,221,162	24.50
China Pacific Laundry Services	104,498,395	55.00	102,762,656	55.00
Hwa Hsia	88,974,057	100.00	88,267,705	100.00
Dynasty Holidays	24,528,593	51.00	30,250,292	51.00
ICAS Co., Ltd.	7,426,254	25.00	10,491,147	25.00

(Continued)

	December 31			
	2003		2002	
	Carrying Value	% of Ownership	Carrying Value	% of Ownership
Global Sky Express	\$ 5,110,714	25.00	\$ 5,025,709	25.00
Freighter Princess Ltd.	35,088	100.00	35,088	100.00
Freighter Prince Ltd.	34,602	100.00	34,602	100.00
Freighter Queen Ltd.	32,895	100.00	32,895	100.00
Spacehab Taiwan	-	-	6,153,716	21.62
	<u>6,779,462,567</u>		<u>7,141,123,566</u>	
<u>Cost method</u>				
Over-the-counter				
Far Eastern Air Transport	422,556,470	8.59	422,832,792	8.59
Trade-Van Information Services	92,320,048	5.98	92,320,048	6.01
Sub-total	<u>514,876,518</u>		<u>515,152,840</u>	
Unlisted				
ABACUS International Holdings Ltd.	297,946,451	13.59	297,946,451	13.59
Fat Capital Management	150,000,000	10.00	150,000,000	10.00
Jardine Air Terminal Services	56,022,929	15.00	56,022,929	15.00
Science Park Cargo Service	44,310,000	14.77	44,310,000	14.77
Chung Hwa Express Co.	22,000,000	11.00	22,000,000	11.00
Changi International Airport Services Pte.	18,764,706	4.40	18,764,706	4.40
Regal International Advertising	5,925,000	6.58	5,925,000	6.58
	<u>594,969,086</u>		<u>594,969,086</u>	
Preferred stocks with no quoted market prices				-
ABACUS International Holdings Ltd.	472,522	-	472,522	-
Less: Allowance for losses	46,156,360		15,642,172	
Subtotal	<u>1,064,161,766</u>		<u>1,094,952,276</u>	
	<u>\$7,843,624,333</u>		<u>\$8,236,075,842</u>	

The market value of investments in shares of OTC stocks was \$468,721,000 in 2003 and \$499,511,000 in 2002, based on the average closing prices of December 2002 and 2001, respectively.

Information on equity-method investments is summarized as follows:

- a. The accounting period of Dynasty Holidays ends on June 30. Each year, the Company recognizes its equity in this investee's net income or net loss using audited June 30 financial statements.
- b. The equity in net income or loss on all equity-method investments (except Freighter Princess Ltd., Freighter Queen Ltd. and Freighter Prince Ltd.) is calculated on the basis of the current year's audited financial statements. Since each of the total paid-in capital of Freighter Princess Ltd., Freighter Queen Ltd. and Freighter Prince Ltd. is less than \$30 million and each of their total operating revenue is less than \$50 million or less than 10% of the total operating revenues of the Company, the recognition of equity in net income is based on unaudited statements. The Company believes that there will be no material effect on the presentation of the financial statements as a whole had those statements been audited.
- c. The total assets or total operating revenues of subsidiaries were individually less than 10% and collectively less than 30% of those of the Company. Thus, the Company did not prepare consolidated financial statements.

**10. PROPERTIES**

	<b>December 31</b>	
	<b>2003</b>	<b>2002</b>
Revaluation increase—cost		
Building	\$ 50,335,009	\$ 50,335,009
Flight equipment	-	167,759,715
	<u>\$ 50,335,009</u>	<u>\$ 218,094,724</u>
Accumulated depreciation		
Buildings	\$ 2,473,100,107	\$ 2,275,527,213
Machinery and equipment	2,412,925,421	2,444,197,243
Flight equipment	25,463,108,292	24,134,478,636
Furniture	646,984,302	622,724,406
Leased flight and other equipment	3,930,138,474	15,875,103,223
Leasehold improvements	358,267,293	318,996,625
	<u>\$ 35,284,523,889</u>	<u>\$ 45,671,027,346</u>

Inventory and property insurance as of December 31, 2003 and 2002 amounted to \$189,764,455,000 and \$194,834,156,000, respectively.

In 1976 and 1982, the Company revalued its properties in accordance with government regulations. Revaluation increments were recorded as increases in the carrying amounts of the assets and credits to capital surplus.

Capitalized interest for the years ended December 31, 2003 and 2002 amounted to \$277,320,000 and \$149,897,000, respectively. These interests were calculated at rates ranging from 1.370% to 1.884% in 2003 and 2.139% to 2.990% in 2002.

**11. SHORT-TERM LOANS**

	<b>December 31</b>	
	<b>2003</b>	<b>2002</b>
Unsecured loans. Interest—1.30% to 1.40% in 2003 and 1.70% to 2.74% in 2002	<u>\$3,600,000,000</u>	<u>\$2,819,512,195</u>

The unused credit lines available for short-term loans amounted to \$4,350,000,000 as of December 31, 2003.

**12. COMMERCIAL PAPER**

	<b>December 31</b>	
	<b>2003</b>	<b>2002</b>
Aggregate face value—discounted interest: 1.25% to 1.40% in 2003 and 1.906% to 2.111% in 2002	\$ 1,830,000,000	\$ 1,570,000,000
Less: Unamortized discount	<u>6,522,165</u>	<u>823,847</u>
	<u>\$ 1,823,477,835</u>	<u>\$ 1,569,176,153</u>

The unused credit lines available for the issuance of commercial paper amounted to \$1,870,000,000 as of December 31, 2003.

### 13. BONDS

	<u>December 31</u>	
	<u>2003</u>	<u>2002</u>
Current		
Convertible bonds		
Type A	\$ -	\$ 427,800,000
Type B	-	6,100,000
First issue of unsecured bonds in 2001	3,000,000,000	-
Second issue of unsecured bonds in 2001	<u>900,000,000</u>	<u>-</u>
	<u>\$ 3,900,000,000</u>	<u>\$ 433,900,000</u>
Noncurrent		
First issue of unsecured bonds in 2001	\$ -	\$ 3,000,000,000
Second issue of unsecured bonds in 2001	2,100,000,000	3,000,000,000
Issue of secured bonds in 2002	2,000,000,000	2,000,000,000
Issue of secured bonds in 2003	<u>4,000,000,000</u>	<u>-</u>
	<u>\$ 8,100,000,000</u>	<u>\$ 8,000,000,000</u>

In 2003, secured bonds with aggregate face values of \$1,200,000,000, \$1,200,000,000 and \$1,600,000,000 were issued as Type A, B and C bonds, respectively, with maturities of 3, 4 and 5 years, respectively, on May 20 to 23, 2003 (four business days). The bonds are repayable in one lump sum payment on maturity. The interest rates for Type A bonds and Type B bonds are 1.45% and 1.6%, respectively, and the interests are calculated and payable annually. The interest rate for Type C bonds is 4% minus floating interest rate, and the interest is calculated semiannually and payable annually. The guarantee institutions are Bank of Taiwan and Chiaotung Bank.

In 2002, secured bonds with aggregate face value of \$2,000,000,000 were issued on May 15 to 28, 2002 (ten business days). The bonds will mature on May 28, 2007 at an annual interest rate of 2.84%. Consecutive annual repayments of the principal are due from May 28, 2005 at these percentages: 30%, 30% and 40%. The guarantee institution are Land Bank and Taipei Bank.

In 2001, the first and second issues of unsecured bonds, with an aggregate face value of \$3,000,000,000 each, were made on January 5, 2001 and between July 18, 2001 and August 6, 2001 (fourteen business days), respectively. The bonds will mature on January 5, 2004 and August 6, 2006 at annual interest rates of 5.526% and 4.900%, respectively. The interests are payable annually. The bonds are payable as follows: (i) first issue lump-sum payment on maturity, and (ii) second issue—three consecutive annual payments due from August 6, 2004 at 30%, 30% and 40% of the principal.

Unsecured domestic convertible bonds (consisting of Type A and Type B Bonds) with an aggregate face value of \$3,500,000,000 were issued on December 12, 1996 and matured on December 11, 2003. Type A Bonds have an aggregate face value of \$1,000,000,000, with annual interest rate at 5% payable annually from issuance date. Type B Bonds have an aggregate face value of \$2,500,000,000. The repayment terms, conversion features and other conditions of both bonds are summarized as follows:

- a. The holders may demand a lump-sum payment for the bonds upon maturity.
- b. Starting from December 12, 2000, the holders can require the Company to redeem their bonds at the following agreed price:
  - 1) Type A—the aggregate face value and accrued interests up to the time of redemption.
  - 2) Type B—the aggregate face value plus redemption premium equivalent to 28.6% of face value on December 12, 2000 and 49.7% of face value on December 12, 2001.

- c. The Company may redeem the bonds piecemeal between December 12, 1998 and November 2, 2003 under certain conditions.
- d. Between January 12, 1997 and December 1, 2003 (except for the period between the ex-dividend date and the date of dividend declaration on record), holders may convert the bonds to common stock of the Company.
- e. As of December 31, 2003, the bonds had all been repaid, and bonds with aggregate face value of \$1,117,700,000 had been converted into 66,976,000 common shares of the Company.

#### 14. LOANS

	<u>December 31</u>	
	<u>2003</u>	<u>2002</u>
Bank loans	\$ 74,932,597,044	\$ 48,363,961,307
Commercial paper—net of unamortized discount of \$25,569,489 in 2003 and \$51,579,906 in 2002	13,640,430,511	12,998,420,094
Less: Current portion	<u>11,985,945,865</u>	<u>8,847,212,177</u>
	<u>\$ 76,587,081,690</u>	<u>\$ 52,515,169,224</u>

Bank loans in various currencies (New Taiwan dollars, Japanese yen, Singapore dollars and U.S. dollars) had interest ranging from 0.5845% to 2.5580% in 2003 and 0.5972% to 2.9970% in 2002. They are repayable quarterly, semiannually or through a lump sum payment upon maturity in December 2015.

The Company has notes issuance facilities (NIF) obtained from certain financial institutions. The NIF, with maturity until October 2014, was used by the Company to guarantee commercial paper it issued. The commercial paper was issued at the discount rate of 1.1728% to 1.7047% in 2003 and 2.2334% to 2.7682% in 2002.

#### 15. CAPITAL LEASE OBLIGATIONS

	<u>December 31</u>	
	<u>2003</u>	<u>2002</u>
Capital lease obligations	\$ 13,982,257,282	\$ 23,322,777,975
Less: Current portion	<u>1,215,321,410</u>	<u>2,121,795,992</u>
	<u>\$ 12,766,935,872</u>	<u>\$ 21,200,981,983</u>

As of December 31, 2003, the Company was leasing certain aircraft and related parts from certain foreign companies under capital lease agreements expiring on various dates until February 2019.

Future minimum rental payments on flight equipment are summarized as follows:

<u>Period</u>	<u>Amount</u>
2004	\$ 1,215,321,410
2005	1,307,079,199
2006	1,405,776,818
2007	1,511,940,005
2008	1,626,134,384
2009 and onwards	6,916,005,000

The present value of total rentals after 2009, based on the 1% discount rate for a one-year time deposit, is \$6,580,342,000.

## 16. PENSION PLAN

The Company has a pension plan for all regular employees. Benefits are based on service years and average basic pay of the six months before retirement.

The Company makes monthly contributions to a pension fund. The fund is administered by a pension fund committee and deposited in the committee's name in the Central Trust of China.

Pension information is summarized as follows:

	<u>2003</u>	<u>2002</u>
a. Net periodic pension cost		
Service cost	\$ 276,909,322	\$ 226,684,249
Interest cost	265,701,410	254,294,018
Projected return on plan assets	( 46,316,375 )	( 48,454,627 )
Amortization of net transition obligation	307,511,000	307,511,000
Amortization of pension gains or losses	<u>3,710,774</u>	<u>-</u>
	<u>\$ 807,516,131</u>	<u>\$ 740,034,640</u>
	<u>December 31</u>	
	<u>2003</u>	<u>2002</u>
b. Reconciliations of the fund status of the plan and accrual pension cost:		
Benefit obligation:		
Vested benefit obligation	\$ 3,703,222,923	\$ 3,639,135,850
Non-vested benefit obligation	<u>2,340,198,625</u>	<u>2,276,049,976</u>
Accumulated benefit obligation	6,043,421,548	5,915,185,826
Additional benefits based on future salaries	<u>942,264,998</u>	<u>1,114,728,607</u>
Projected benefit obligation	6,985,686,546	7,029,914,433
Fair value of plan assets	( <u>1,174,548,995</u> )	( <u>1,671,622,982</u> )
Funded status	5,811,137,551	5,358,291,451
Unrecognized net transition obligation	( 2,152,573,000 )	( 2,460,084,000 )
Unrecognized former service cost	( 591,355,965 )	( 591,355,965 )
Unrecognized net actuarial loss	( 1,234,769,065 )	( 684,674,366 )
Additional liability	<u>3,036,433,032</u>	<u>2,621,385,724</u>
Accrued pension cost	<u>\$ 4,868,872,553</u>	<u>\$ 4,243,562,844</u>
c. Vested benefits—undiscounted	<u>\$ 6,707,994,803</u>	<u>\$ 6,839,449,200</u>
	<u>2003</u>	<u>2002</u>
d. Actuarial assumptions		
Discount rate used in determining present values	3.7%	4.3%
Future salary increase rate	2.0%	2.5%
Expected rate of return on plan assets	3.7%	4.3%
e. Summary of changes in the pension fund		
Contributions	<u>\$ 519,740,941</u>	<u>\$ 672,282,300</u>
Payment of benefits	<u>\$ 1,115,404,726</u>	<u>\$ 619,873,744</u>

As of December 31, 2003 and 2002, the contributions deposited in the Central Trust of China amounted to \$1,129,197,000 and \$1,613,413,000, respectively.

## 17. STOCKHOLDERS' EQUITY

As of May 30, 2003 and June 28, 2002, the appropriation of earnings in 2002 and 2001 had been resolved by the stockholders, respectively, as follows:

	<b>Appropriations</b>			
	<b>(in Thousands of</b>			
	<b><u>New Taiwan Dollars</u></b>	<b><u>2001</u></b>	<b><u>2002</u></b>	<b><u>2001</u></b>
Legal reserve	\$ 421,615	\$ 178,513		
Cash dividends	-	363,584	\$ -	\$ 0.15
Stock dividends	2,542,796	1,090,755	1.00	0.45
Stock bonus for employees	<u>168,450</u>	<u>96,397</u>		
	<u>\$ 3,132,861</u>	<u>\$ 1,729,249</u>		

The above appropriations were the same as those proposed by the board of directors.

Capital surplus from the issue of stock in excess of par value, stock issuance to effect a merger, and reissuance of treasury stock and donations may be distributed as stock dividend or used to offset a deficit. But capital surplus from equity-method investees should not be used for any purpose.

The Company's Articles of Incorporation provide that the following should be appropriated from annual net income (less any deficit): (a) 10% as legal reserve, and (b) special reserve equivalent to a debit balance of any stockholders' equity account. From the remainder, the Company should also appropriate at least 3% bonus to employees. Of the final remainder, at least 50% should be distributed to stockholders as both cash and stock dividends (cash dividend should be no more than 30% of the total dividend) or stock dividends only. In determining the amount of cash dividends to be distributed, the board of directors should take into account the Company's future cash requirements, including, primarily, cash requirements for future aircraft acquisitions. Distribution of earnings generated in prior years should also comply with the foregoing guidelines.

The Company's special reserve appropriation from the current year's net income or the unappropriated earnings should be equal to the debit balance of any stockholders' equity account (other than deficit), such as the debit balances of unrealized loss on investments in shares of stock and cumulative translation adjustments, but not the balance of treasury stocks. When the sum of the debit balances decreases, a portion of the special reserve equal to the amount of the decrease becomes available for distribution.

Under the regulations of the Securities and Futures Commission, a special reserve is appropriated from the balance of the retained earnings at an amount equal to the carrying value of the treasury stock held by subsidiaries in excess of the market value on the balance sheet date. The special reserve may be reversed when the market value recovers.

As of February 25, 2004, the date of the accompanying auditors' report, the appropriation of earnings in 2003 had not been resolved by the board of directors. The resolution on this appropriation will be announced through the Market Observation System on the Web site of the Taiwan Stock Exchange.

Under a resolution, the stockholders approved the board of directors' proposal on the appropriation of earnings in 2002 and declared \$168,450,000 as bonus for employees in the form of stocks (0.7% of the Company's outstanding common stocks as of December 31, 2002). Had the entire bonus for employees been distributed and recorded as expense, the 2002 basic earnings per share would have decreased from \$1.11 to \$1.06.

Under the Company Law, legal reserve should be appropriated until the reserve equals the Company's paid-in capital. This reserve may be used to offset a deficit. Also, when the reserve has reached 50% of the Company's paid-in capital, up to 50% thereof may be capitalized.

Under the Income Tax Law, ROC resident stockholders are entitled to income tax credit upon the distribution of dividends appropriated from earnings generated since January 1, 1998. The income tax credit is based on a creditable tax ratio determined on the date of dividend distribution.

## 18. TREASURY STOCK

(In Thousands of Shares)

<u>Reason</u>	<u>Shares at Beginning of Year</u>	<u>Shares Increase During the Year</u>	<u>Shares Decrease During the Year</u>	<u>Shares at Ending of Year</u>
<u>2003</u>				
Company shares held by its subsidiaries reclassified from investment in shares of stock to treasury stock	<u>15,501</u>	<u>1,530</u>	<u>13,695</u>	<u>3,336</u>
<u>2002</u>				
Company shares held by its subsidiaries reclassified from investment in shares of stock to treasury stock	<u>20,481</u>	<u>860</u>	<u>5,840</u>	<u>15,501</u>

The above shares increase during the year refers only to stock dividends.

Proceeds from treasury stock reissuance were \$203,796,000 and \$94,963,000 for the periods ended December 31, 2003 and 2002, respectively. The shares reclassified as treasury stock amounted to \$35,493,000 and \$189,738,000 for the years ended December 31, 2003 and 2002, respectively. The market values of the treasury stocks as of December 31, 2003 and 2002 were \$49,945,000 and \$240,782,000, respectively.

The shares of the Company held by its subsidiaries were treated as treasury stock. However, the subsidiaries may exercise stockholders' rights on these treasury stocks.

## 19. INCOME TAXES

- a. The reconciliation of the income tax expense on income before income tax expense at statutory income tax rate and income tax expense—current is as follows:

	<u>2003</u>	<u>2002</u>
Income tax expense on income before income tax at statutory rate (25%)	\$ 406,224,527	\$ 739,783,432
Add (less) tax effects of:		
Permanent differences	( 154,211,906 )	( 236,635,334 )
Temporary differences	<u>1,399,759,985</u>	<u>283,557,436</u>
Income tax expense—current	<u>\$ 1,651,772,606</u>	<u>\$ 786,705,534</u>

- b. Income tax consisted of the following:

Income tax expense—current	\$ 1,651,772,606	\$ 786,705,534
Tax on unappropriated retained earnings	119,019,468	151,968,872
Investment income tax credit	( 1,198,608,318 )	( 900,981,826 )
Net changes in deferred income tax expense (benefit):		
Allowance for doubtful receivables	438,753	58,764,702
Allowance for loss on inventories	2,392,851	11,987,076
Equity in net loss in equity-method domestic investees	( 64,941,570 )	( 107,598,402 )
Equity in net income of foreign equity method investees	7,933,679	1,891,608
Depreciation difference between accounting and tax on properties	( 1,325,090,158 )	( 28,532,775 )
Allowance for loss on idle assets	( 50,000,000 )	( 135,297,218 )
Accrued expense of frequent-flyer program	( 2,821,670 )	( 7,007,404 )
Provision for pension cost	( 52,565,601 )	( 3,324,866 )
Unrealized foreign exchange gain (loss)	66,223,549	( 89,492,283 )
Difference between accounting and tax on interest	18,670,183	20,711,594
Investment income tax credits	454,487,536	5,063,686
Provision (reversal) of valuation allowance	( 109,751,078 )	77,001,747
Adjustment of prior years' tax	<u>328,272,117</u>	<u>( 2,170,000 )</u>
Income tax benefit	( 154,567,653 )	( 160,309,955 )
Extraordinary loss	<u>-</u>	<u>( 5,615,084 )</u>
Income tax benefit before extraordinary loss	<u>( \$ 154,567,653 )</u>	<u>( \$ 154,694,871 )</u>

- c. Deferred income tax assets (liabilities) as of December 31, 2003 and 2002 consisted of the following:

	<u>December 31</u>	
	<u>2003</u>	<u>2002</u>
Current		
Allowance for doubtful accounts	\$ -	\$ 438,753
Allowance for loss on inventories	8,456,275	10,849,126
Accrued expenses for frequent-flyer program	32,542,762	29,721,092
Unrealized foreign exchange loss	<u>173,336,765</u>	<u>239,560,314</u>
Deferred income tax assets	<u>\$ 214,335,802</u>	<u>\$ 280,569,285</u>

(Continued)

	<b>December 31</b>	
	<b>2003</b>	<b>2002</b>
Noncurrent		
Investment income tax credit	\$ 1,138,209,770	\$ 1,592,697,306
Cumulative equity in the net loss of domestic equity-method investees	276,753,472	211,811,902
Cumulative equity in the net loss of foreign equity-method investees	-	1,502,917
Provision for pension cost	457,963,000	405,397,399
Difference between accounting and tax on interest	230,655,357	249,325,540
Allowance for loss on idle properties	<u>210,810,144</u>	<u>160,810,144</u>
Deferred income tax assets	2,314,391,743	2,621,545,208
Less—valuation allowance	( <u>798,086,386</u> )	( <u>907,837,464</u> )
Deferred income tax assets—net	1,516,305,357	1,713,707,744
Depreciation difference between accounting and tax on properties	( 694,146,352 )	( 2,019,236,510 )
Cumulative equity in the net income of foreign equity-method investees	( <u>6,430,762</u> )	<u>-</u>
Deferred income tax assets (liabilities)—noncurrent, net	<u>\$ 815,728,243</u>	<u>( \$ 305,528,766 )</u>

- d. Information on the imputation credit account (ICA) and creditable tax ratio is summarized as follows:

	<b>December 31</b>	
	<b>2003</b>	<b>2002</b>
Balance of ICA	<u>\$ 39,954,548</u>	<u>\$ 65,000,630</u>

The expected and actual creditable tax ratios for distribution to each qualified stockholder of earnings generated up to December 31, 2003 and 2002 were 1.74% and 3.70%, respectively.

The actual creditable tax ratio to be used for distributing earnings generated as of December 31, 2003 will be determined on the date of dividend distribution. Thus, the expected creditable tax ratio may change depending on the ICA balance on the dividend distribution date.

- e. The unappropriated retained earnings as of December 31, 2003 and 2002 included earnings of 5,752,946,000 generated as of December 31, 1997.

The above deferred income taxes were computed at a tax rate of 25%.

- f. Unused investment income tax credits as of December 31, 2003 were as follows:

<b>Basis of the Tax Credit</b>	<b>Description of the Source of the Tax Credit</b>	<b>Total Amount of Tax Credits</b>	<b>Remaining Tax Credits</b>	<b>Expiry Year</b>
Article 6 of the Statute for Upgrading of Industries	R&D expenses, personnel	\$ 458,104,699	\$ 400,988,639	2004
	training expenses, expenses	855,754,412	699,626,067	2005
	for international brand and purchases of eligible equipment	648,207,524	37,595,064	2006

The income tax returns through 1998, except for the following, had been examined and cleared by the tax authorities.

On the Company's 1997 income tax return, the tax authorities assessed the Company an additional income tax of \$25,498,000. The tax authorities contended that a portion of the interest expense claimed as income tax deduction by the Company should have been capitalized. In addition, the tax authorities reduced the portion of the income that the Company considered tax-exempt. The Company is claiming that, under the Income Tax Law, an income tax of \$27,211,000 paid in foreign tax jurisdictions in 1997 should be credited against its income tax obligations. For the Company's 1998 income tax return, the tax authorities calculated an additional gain of \$1,313,088,000 from the securities trade of foreign investees and assessed a fine for the Company. The tax authorities contended that transfers from reorganization of foreign investees are considered securities trading. The Company has appealed these assessments and expects a favorable outcome on those appeals. But for conservative purposes, the Company recognized the additional income tax on the 1998 income tax return in 2003.

## 20. EXTRAORDINARY LOSS

On May 25, 2002, one of the Company's planes (with fuselage number B18255) crashed in the vicinity of the Peng-Hu Islands in Taiwan. The Company received from an insurance company an indemnification of \$661,512,000 for the destroyed fuselage. The estimate of the costs of salvaging parts of the aircraft and compensation to surviving relatives of passengers and other expenditures was \$683,972,000. Thus, an extraordinary loss of \$16,845,000 (net of income tax effects of \$5,615,000) was recognized.

## 21. PERSONNEL, DEPRECIATION AND AMORTIZATION EXPENSES

	<b>2003</b>		
	<b>Included in Operating Costs</b>	<b>Included in Operating Expenses</b>	<b>Total</b>
Personnel expenses			
Salaries	\$ 7,167,844,453	\$ 2,169,493,860	\$ 9,337,338,313
Labor and health insurance	349,939,123	199,723,573	549,662,696
Pension cost	615,038,241	358,303,290	973,341,531
Others	1,746,153,176	146,274,889	1,892,428,065
Depreciation	6,342,472,501	319,490,699	6,661,963,200
Amortization	114,278,234	12,078,647	126,356,881
	<b>2002</b>		
	<b>Included in Operating Costs</b>	<b>Included in Operating Expenses</b>	<b>Total</b>
Personnel expenses			
Salaries	7,048,737,037	2,199,826,607	9,248,563,644
Labor and health insurance	340,794,802	173,108,002	513,902,804
Pension cost	625,498,988	261,043,919	886,542,907
Others	1,748,952,203	243,919,334	1,992,871,537
Depreciation	6,467,036,403	355,512,504	6,822,548,907
Amortization	114,278,234	20,501,111	134,779,345

## 22. EARNINGS PER SHARE

Numerators and denominators used in calculating earnings per share (EPS) were as follows:

	Amount (as Numerator) (Thousand)		Shares (as Denominator) (Thousand)	Earnings Per Share	
	Pretax	After Tax		Pre-tax	After Tax
	<u>For the year ended December 31, 2003</u>				
Basic EPS					
Net income attributable to common stock	\$1,624,898	\$1,779,466	2,799,530	\$ 0.58	\$ 0.64
Dilutive effect of potential common stock					
Convertible bonds—Type A	\$ 19,433	\$ 14,575	33,796		
Convertible bonds—Type B	\$ -	\$ -	530		
Diluted EPS					
Net income attributable to common stock and potential common stock	\$1,644,331	\$1,794,041	2,833,856	\$ 0.58	\$ 0.63
<u>For the year ended December 31, 2002</u>					
Basic EPS					
Net income before extraordinary item attributable to common stock	\$2,981,594	\$3,136,289	2,795,024	\$ 1.07	\$ 1.12
Extraordinary item	( 22,460)	( 16,845)		( 0.01)	( 0.01)
Basic EPS	\$2,959,134	\$3,119,444		\$ 1.06	\$ 1.11
Dilutive effect of potential common stock					
Convertible bonds—Type A	\$ 21,390	\$ 16,043	33,685		
Convertible bonds—Type B	\$ -	\$ -	480		
Diluted EPS					
Net income before extraordinary item attributable to common stock and potential common stock	\$3,002,984	\$3,152,332	2,829,189	\$ 1.06	\$ 1.11
Extraordinary item	( 22,460)	( 16,845)		( 0.01)	( 0.01)
Diluted EPS	\$2,980,524	\$3,135,487		\$ 1.05	\$ 1.10

The number of shares outstanding should be retroactively adjusted to reflect the effects of the distribution of stock dividends and the bonus for employees that were appropriated from the earnings in 2002. Thus, the 2002 basic EPS and diluted EPS for net income were retroactively adjusted to decrease from \$1.23 and \$1.22 to \$1.11 and \$1.10, respectively.

## 23. RELATED-PARTY TRANSACTIONS

- a. The related parties

<u>Related Party</u>	<u>Relationship with the Company</u>
Taiwan Air Cargo Terminal	Equity-method investee
China Pacific Catering Services	Equity-method investee
Cal-Dynasty International	Equity-method investee
Taoyuan International Airport Service	Equity-method investee
Mandarin Airlines	Equity-method investee

(Continued)

Name	Relationship with the Company
Hwa Sheng Investment	Equity-method investee
Abacus Distribution Systems (Taiwan)	Equity-method investee
Taiwan Airport Service	Equity-method investee
Kaoshiung Catering Services	Equity-method investee
Cal-Asia Investment	Equity-method investee
Asian Compressor Technology Service	Equity-method investee
China Pacific Laundry Services	Equity-method investee
Hwa Hsia	Equity-method investee
Dynasty Holidays	Equity-method investee
ICAS Co., Ltd.	Equity-method investee
Global Sky Express	Equity-method investee
Freighter Princess Ltd.	Equity-method investee
Freighter Prince Ltd.	Equity-method investee
Freighter Queen Ltd.	Equity-method investee
Spacehab Taiwan	Equity-method investee
China Aviation Development Foundation	Major stockholder

b. Significant transactions with related parties:

	<u>2003</u>		<u>2002</u>	
	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>
1) Operating revenues—for the year				
Mandarin Airlines	\$ 761,747,264	1.00	\$ 303,670,877	0.42
Global Sky Express	179,200,823	0.24	269,073,435	0.37
Taiwan Air Cargo Terminal	24,936,696	0.03	44,715,951	0.06
China Aviation Development Foundation	21,848,007	0.03	50,082,966	0.07
Others	<u>9,671,708</u>	<u>0.01</u>	<u>18,299,351</u>	<u>0.02</u>
	<u>\$ 997,404,498</u>	<u>1.31</u>	<u>\$ 685,842,580</u>	<u>0.94</u>
2) Operating costs—for the year				
China Pacific Catering Services	\$ 791,026,822	1.31	\$ 809,199,340	1.32
Taoyuan International Airport Service	686,947,585	1.14	689,814,941	1.13
Taiwan Airport Service	250,472,085	0.41	262,055,209	0.43
Hwa Hsia	195,659,187	0.32	218,077,726	0.36
Taiwan Air Cargo Terminal	161,587,331	0.27	145,754,062	0.24
Mandarin Airlines	141,903,319	0.23	50,611,956	0.08
Kaoshiung Catering Services	65,417,024	0.11	80,996,347	0.13
Dynasty Holidays	60,054,440	0.10	79,728,831	0.13
China Pacific Laundry Services	57,983,346	0.10	60,768,716	0.10
China Aviation Development Foundation	43,914,494	0.07	105,017,888	0.17
Cal-Dynasty International	34,151,724	0.06	31,546,713	0.05
Cal Asia Investment	18,618,172	0.03	17,423,589	0.03
Asian Compressor Technology Service	4,574,490	0.01	83,334,986	0.14
Others	<u>621,824</u>	<u>-</u>	<u>651,117</u>	<u>-</u>
	<u>\$2,512,931,843</u>	<u>4.16</u>	<u>\$2,634,981,421</u>	<u>4.31</u>

	<b>December 31</b>			
	<b>2003</b>		<b>2002</b>	
	<b>Amount</b>	<b>%</b>	<b>Amount</b>	<b>%</b>
3) Receivables—related party				
Mandarin Airlines	\$ 268,128,012	89.08	\$ 216,791,545	79.94
China Aviation Development Foundation	13,513,895	4.49	7,703,509	2.84
Global Sky Express	13,297,445	4.42	17,757,569	6.55
Taiwan Air Cargo Terminal	3,826,516	1.27	6,261,437	2.31
Others	<u>2,243,674</u>	<u>0.74</u>	<u>22,690,668</u>	<u>8.36</u>
	<u>\$ 301,009,542</u>	<u>100.00</u>	<u>\$ 271,204,728</u>	<u>100.00</u>
4) Payable—related party				
Mandarin Airlines	\$ 349,241,095	39.22	\$ 255,887,535	31.09
China Pacific Catering Services	233,616,043	26.23	201,313,367	24.45
Taoyuan International Airport Service	188,958,071	21.22	188,054,888	22.84
Taiwan Airport Service	39,695,994	4.46	48,361,713	5.88
Taiwan Air Cargo Terminal	22,269,243	2.50	18,830,604	2.29
Hwa Hsia	19,016,043	2.14	20,308,110	2.47
China Aviation Development Foundation	15,033,963	1.69	16,223,252	1.97
Kaoshiung Catering Services	12,479,789	1.40	12,179,955	1.48
Others	<u>10,219,826</u>	<u>1.14</u>	<u>62,013,412</u>	<u>7.53</u>
	<u>\$ 890,530,067</u>	<u>100.00</u>	<u>\$ 823,172,836</u>	<u>100.00</u>

5) Financing provided

	<b>2002</b>			
	<b>Maximum Balance for the Period</b>	<b>Ending Balance</b>	<b>Interest Rate</b>	<b>Interest Revenue</b>
	Mandarin Airlines	<u>\$ 1,775,000,000</u>	<u>\$ -</u>	2.639%-2.877%

6) Lease of property and equipment

In September 2002, the Company rented out planes to Mandarin Airlines under an operating lease agreement to help Mandarin Airlines ply the passenger and cargo routes between Kaohsiung and Hong Kong. Passenger fares, revenue and the cost of the routes were recognized at the percentages of seats sold every month; for cargo, the rent received is based on actual block times. The rentals received were \$658,280,000 in 2003 and \$152,387,000 in 2002.

The Company rented planes from Mandarin Airlines under an operating lease agreement from July 2003 to February 2008. Before October 2003, the Company paid the rental by flight hours. From October 2003, rentals were at a fixed amount of US\$282,000 monthly. As of December 31, 2003, the Company had paid about \$65,290,000.

7) Endorsement and guarantee

	<b>December 31</b>	
	<b>2003</b>	<b>2002</b>
Mandarin Airlines—bank loans	\$ 1,285,000,000	\$ 1,395,000,000
China Pacific Laundry Service	120,000,000	-
Asian Compressor Technology Service—bank loans	21,666,667	22,195,121
Freighter Queen Ltd.	433,429,575	424,349,177
Freighter Prince Ltd.	526,967,956	539,820,832
Freighter Princess Ltd.	372,356,687	665,451,664

These related party transactions were conducted under normal terms.

## 24. PLEDGED ASSETS

The following assets had been pledged or mortgaged as collateral for short-term loans and long-term debts:

	<b>December 31</b>	
	<b>2003</b>	<b>2002</b>
Certificates of deposit	\$ 280,458,844	\$ 278,745,645
Inventories	2,018,030,118	-
Properties—building, machinery and flight equipment (net)	<u>89,108,436,555</u>	<u>74,757,127,684</u>
	<u>\$ 91,406,925,517</u>	<u>\$ 75,035,873,329</u>

## 25. COMMITMENTS AND CONTINGENT LIABILITIES

- a. The Company leased certain flight equipment and hangar under various operating lease agreements expiring in November 2023. Lease deposits aggregated \$3,490,000,000 (recorded as part of other assets).

Minimum rentals for future years are summarized as follows:

<b><u>Year</u></b>	<b><u>Amount</u></b>
2004	\$ 3,924,392,731
2005	2,488,379,541
2006	1,954,258,059
2007	1,548,030,909
2008	1,147,161,549

Rentals from 2009 and thereafter will aggregate \$4,445,551,000. As of December 31, 2003, the value of these rentals, discounted using the 1% interest rate for one-year time deposits, was \$4,216,740,000.

- b. The Company has options to acquire five 737-800 aircraft under a contract with Boeing Co. entered into in September 1999, which were all exercised by the Company. As of December 31, 2003, the Company had delivered three 737-800 planes, with the cost of the remaining two planes amounting to US\$151,884,000. As of December 31, 2003, the Company had paid about US\$1,783,000, which is included in the “advances on aircraft and other equipment acquired” in the properties section of the balance sheets.

- c. In July 1999, the Company acquired thirteen 747-400F aircraft from Boeing Co., which had delivered ten planes as of December 31, 2003. The aggregate purchase price of the remaining three aircraft is US\$610,100,000. As of December 31, 2003, the Company had paid about US\$123,938,000, which was included in “advances on aircraft and other equipment acquired” in the properties section of the balance sheets.

On October 31, 2002, the Company acquired four more 747-400F aircraft from Boeing Co., which had delivered three planes as of December 31, 2003. The aggregate purchase price of the remaining aircraft is US\$223,446,000. As of December 31, 2002, the Company had paid about US\$33,814,000, included in “advances on aircraft and other equipment acquired” in the properties section of the balance sheets.

- d. The Company entered into an option contract with Boeing Co. in November 2002 for the purchase of six 747-400 aircraft. On November 1, 2003 the Company asked that the model of two of the aircraft be changed to 747-400F. The aggregate purchase prices of the four 747-400 and two 747-400F aircraft are US\$868,097,000 and US\$441,940,000, respectively. As of December 31, 2003, the Company had paid about US\$186,376,000 and US\$66,544,000, respectively, which are included in “advances on aircraft and other equipment acquired” in the properties section of the balance sheets.
- e. In December 2002, the Company entered into an option contract with Airbus for the purchase of twelve A330 aircraft and exercised the purchase option on two planes on December 18, 2003. The aggregate purchase price is US\$2,336,097,000. As of December 31, 2003, the Company had paid about US\$123,200,000.
- f. In December 2003, the Company won the bid to buy from the Civil Aeronautics Administration (CAA) four 747-400 aircraft and one MD-11 aircraft. The aggregate purchase price is US\$179,094,000, and the Company had paid off in January 2004.
- g. A case involving a dispute between the Company and the Civil Aeronautics Administration (CAA) on certain lease payments and interests incurred on advances on leased aircraft was filed with the Taipei District Court. CAA repudiated the terms of the original contracts and claimed additional interests imputed on rentals and on prepayments for six planes under capital lease, i.e., originally leased but were later acquired by the Company. The amount claimed amounted to about \$1,100,000,000. The district court ruled that the Company pay the additional interest, but the Company appealed this decision. On April 8, 2003, the Taiwan high court ruled that the Company should pay CAA only \$2,874,000 plus interest at 5% from May 21, 1997 to the payment date. In addition, the Company has to pay 3% of the lawsuit fees. CAA has the right to appeal the decision, but the Company expects a favorable outcome on this case.

## **26. SUBSEQUENT EVENT**

On February 24, 2004, the Securities and Futures Commission had approved the Company’s second issue of unsecured domestic convertible bonds with an aggregate face value of \$10,000,000,000 and five-year maturities. According to the conversion conditions on the bonds, the holders can convert the bonds to common stock of the Company at \$17.5 per share (conversion price will be adjusted if conditions on the Company’s outstanding common shares change).

## **27. FINANCIAL INSTRUMENTS**

- a. Derivative financial instruments

The Company uses derivative financial instruments solely for nontrading purposes.

Forward exchange contracts and foreign-currency options are intended to hedge the Company's exposure to the adverse effect of exchange rate fluctuations on foreign-currency assets and liabilities. The foreign currency swap contracts are intended to help the Company manage its currency positions. Interest rate swaps and cross-currency swaps are used to hedge the risk arising from adverse movements of interest rates and exchange rates. The fuel swap contracts are to hedge against the volatility in fuel prices. The hedging strategy is to protect the Company from market risk by using instruments fluctuations in their fair values that offset the changes in the fair values of the underlying exposures. The Company also periodically evaluates the effectiveness of the instruments.

The Company is exposed to credit risk if a counter-party defaults on its obligations. To manage this risk, the Company enters into derivative transactions only with known international and domestic financial institutions with good credit ratings. Contracts were also entered into with different financial institutions to minimize concentration of credit risk. Thus, no material losses resulting from counter-party defaults are anticipated.

The following table summarizes the aggregate contract (notional) amounts, credit risk and fair value of the Company's derivative financial instruments as of December 31, 2003 and 2002.

	December 31					
	2003			2002		
	Contract (Notional) Amount	Credit Risk	Fair Value	Contract (Notional) Amount	Credit Risk	Fair Value
Forward exchange contracts	\$ 4,380,952,381	\$ 199,000	(\$ 7,753,663)	\$ -	\$ -	\$ -
Interest rate swaps	57,973,959,865	235,288,904	( 1,868,807,199)	48,243,990,581	435,180,085	( 1,684,498,376)
Foreign-currency options	6,027,802,381	11,821,294	( 22,375,832)	3,111,649,686	6,568,467	( 27,295,160)
Fuel swap contracts	13,880,518,707	336,079,454	190,359,895	14,439,651,568	148,132,439	( 165,540)

The fair value of each contract is calculated by using quotes from financial institutions.

The contract amount is used to calculate the amounts to be settled by the counter-parties, so it is neither the actual delivery amount nor the cash requirement of the Company. The derivative financial instruments held or issued by the Company are likely to be sold at reasonable market prices. The Company does not expect significant cash flow requirements upon maturity.

The gain or loss from derivative transactions is listed below.

	2003	2002
Forward exchange contracts		
Reported as foreign-currency gain (loss)	\$ 17,162,451	(\$ 34,787,748)
Reported as reduction of advance payments on equipment purchase contracts	21,907,763	-
Interest rate swaps—reported as additional interest expense	655,449,568	423,382,638
Foreign-currency options		
Reported as foreign-currency gain (loss)	( 79,825,522)	36,043,425
Reported as additional advances for aircraft and other equipment acquired	713,027	-
Fuel swap contracts—reported as reduction of fuel cost	1,204,121,526	438,893,525
Cross-currency swaps		
Reported as foreign-currency loss	-	147,963,098
Reported as additional of interest expense	-	65,153,330
Currency swaps		
Reported as foreign-currency loss	-	78,888,875
Reported as interest revenue	-	16,676,905

b. Fair value of financial instruments as of December 31, 2003 and 2002

	<b>December 31</b>			
	<b>2003</b>		<b>2002</b>	
	<b>Carrying Value</b>	<b>Fair Value</b>	<b>Carrying Value</b>	<b>Fair Value</b>
Financial assets				
Fair value equal to carrying value	\$ 27,577,722,566	\$ 27,577,722,566	\$ 20,620,921,561	\$ 20,620,921,561
Short-term investments	10,103,718,329	10,201,929,840	188,198,451	225,696,864
Financial liabilities				
Fair value equal to carrying value	118,759,368,202	118,759,368,202	\$ 99,073,002,917	\$ 99,073,002,917
Bonds	12,000,000,000	12,063,189,043	8,433,900,000	8,617,223,110
Derivative financial instruments				
Forward exchange contracts	( 530,350)	( 7,753,663)	-	-

The methods and assumptions used in estimating fair values are as follows:

- 1) The carrying values of some financial instruments reported in the balance sheets approximate fair values because of the short maturities of these instruments or the present receipts and payments approximate their carrying value. This assumption applies to cash, receivables, other receivables, pledged certificates of deposit, deposits in and out, other financial assets—noncurrent, short-term loans, commercial paper, accounts payable, accrued expenses, loans and debts—current portion, capital lease obligations and other current liabilities.
- 2) Fair values of short-term and investment in shares of stock are based on quoted market prices, or on carrying amounts if quoted market prices are not available.
- 3) Fair values of bonds payable are based on quoted market prices.
- 4) Long-term loans are financial liabilities with floating interest. Thus, their carrying values represent current fair values.
- 5) Fair value of the derivative financial instruments is based on the assumption that the Company would make or receive payments on the balance sheet date if it discontinues the contract. Usually the fair value includes the unrealized income or loss on the existing contracts. Most fair values of the derivative financial instruments owned by the Company are quoted from financial institutions.

Only the fair values of financial instruments were listed above; thus, the total of fair values listed above does not represent the Company's fair value.

## 28. ADDITIONAL DISCLOSURES

- a. Following are the additional disclosures required by the Securities and Futures Commission for the Company and its investees:
  - 1) Financing provided: None
  - 2) Endorsement/guarantee provided: Table 1 (attached)
  - 3) Marketable securities held: Table 2 (attached)
  - 4) Marketable securities acquired and disposed of at costs or prices of at least NT\$100 million or 20% of the paid-in capital: Table 3 (attached)
  - 5) Acquisition of individual real estates at costs of at least NT\$100 million or 20% of the paid-in capital: None



c. Major customers

The primary customers are the public; therefore, there is no customer with sales that are at least 10% of the Company's total sales.

**TABLE 1****CHINA AIRLINES, LTD. AND INVESTEES****ENDORSEMENT/GUARANTEE PROVIDED  
FOR THE YEAR ENDED DECEMBER 31, 2003  
(Amounts in New Taiwan Dollars, Unless Otherwise Noted)**

No.	Endorsement/ Guarantee Provider	Counter-party		Limits on Each Counter-party's Endorsement/ Guarantee Amounts (Note 1)	Maximum Balance for the Period	Ending Balance	Value of Collaterals Property, Plant, or Equipment	Ratio of Accumulated Amount of Collateral to Net Equity of the Latest Financial Statement (%)	Maximum Collateral/Guarantee Amounts Allowable (Note 2)
		Name	Nature of Relationship						
0	China Airlines	Mandarin Airlines	90.05% subsidiary	\$ 9,291,992,663	\$ 1,705,000,000	\$ 1,285,000,000	\$ -	3	\$ 22,827,672,514
		China Pacific Laundry Services	55% subsidiary	9,291,992,663	120,000,000	120,000,000	-	-	22,827,672,514
		Asian Compressor Technology Service	Cost-method investee	9,291,992,663	22,118,056	21,666,667	-	-	22,827,672,514
		Freighter Queen Ltd.	100% subsidiary	9,291,992,663	442,459,358	433,429,575 (Note 3)	-	1	22,827,672,514
		Freighter Prince Ltd.	100% subsidiary	9,291,992,663	537,946,455	526,967,956 (Note 3)	-	1	22,827,672,514
		Freighter Princess Ltd.	100% subsidiary	9,291,992,663	380,114,118	372,356,687 (Note 3)	-	1	22,827,672,514

Note 1: Based on the Company's guidelines, the maximum amount of guarantee to an individual counter-party is up to 20% of the Company's stockholders' equity.

Note 2: Based on the Company's guidelines, the allowable aggregate amount of collateral guarantee is up to 50% of the Company's stockholders' equity.

Note 3: The guarantee provided to subsidiaries by the Company was not counted in the allowable aggregate amount of collateral guarantee because the related amount was intended to meet the Company's financing need and the Company had recognized an equal amount as liability.

TABLE 2

## CHINA AIRLINES, LTD. AND INVESTEEES

## MARKETABLE SECURITIES HELD

DECEMBER 31, 2003

(Amounts in New Taiwan Dollars, Unless Specified Otherwise)

Held Company Name	Marketable Securities Type and Name	Relationship with the Company	Financial Statement Account	December 31, 2003				Note
				Shares/Units	Carrying Value	Percentage of Ownership	Market Value or Net Asset Value	
China Airlines	<u>Stock</u>							
	Taiwan Air Cargo Terminal	Equity-method investee	Investments in shares of stock	135,000,000	\$1,668,302,636	54.00%	\$1,668,302,636	-
	China Pacific Catering Services	Equity-method investee	Investments in shares of stock	74,460,000	864,196,663	51.00%	864,196,663	-
	Cal-Dynasty International	Equity-method investee	Investments in shares of stock	2,614,500	816,757,176	100.00%	816,757,176	-
	Taoyuan International Airport Service	Equity-method investee	Investments in shares of stock	34,300,000	768,279,978	49.00%	768,279,978	-
	Mandarin Airlines	Equity-method investee	Investments in shares of stock	216,441,585	736,714,570	90.05%	1,141,728,117	Note 1
	Hwa Sheng Investment	Equity-method investee	Investments in shares of stock	50,000,000	517,935,309	100.00%	517,935,309	-
	Abacus Distribution Systems (Taiwan)	Equity-method investee	Investments in shares of stock	22,450,008	391,719,910	93.93%	391,719,910	-
	Taiwan Airport Service	Equity-method investee	Investments in shares of stock	17,188,870	337,237,539	47.35%	337,237,539	-
	Kaoshiung Catering Services	Equity-method investee	Investments in shares of stock	12,705,000	155,148,478	31.76%	155,148,478	-
	Cal-Asia Investment	Equity-method investee	Investments in shares of stock	4,000,000	147,288,230	100.00%	147,288,230	-
	Asian Compressor Technology Service	Equity-method investee	Investments in shares of stock	7,732,200	145,241,480	24.50%	145,241,480	-
	China Pacific Laundry Services	Equity-method investee	Investments in shares of stock	13,750,000	104,498,395	55.00%	104,498,395	-
	Hwa Hsia	Equity-method investee	Investments in shares of stock	50,000	88,974,057	100.00%	100,199,949	Note 1
	Dynasty Holidays	Equity-method investee	Investments in shares of stock	408	24,528,593	51.00%	24,528,593	-
	ICAS Co., Ltd.	Equity-method investee	Investments in shares of stock	850,000	7,426,254	25.00%	7,426,254	-
	Global Sky Express	Equity-method investee	Investments in shares of stock	250,000	5,110,714	25.00%	5,110,714	-
	Freighter Princess Ltd.	Equity-method investee	Investments in shares of stock	1,000	35,088	100.00%	35,088	-
	Freighter Prince Ltd.	Equity-method investee	Investments in shares of stock	1,000	34,602	100.00%	34,602	-
	Freighter Queen Ltd.	Equity-method investee	Investments in shares of stock	1,000	32,895	100.00%	32,895	-
	Far Eastern Air Transport	-	Investments in shares of stock	50,464,017	422,556,470	8.59%	321,960,428	-
	Trade-Van Information Services	-	Investments in shares of stock	11,825,925	92,320,048	5.98%	146,759,729	-
	Abacus International Holding, Ltd.—unlisted common stock	-	Investments in shares of stock	1,359,368	297,946,451	13.59%	-	Note 3
	Fat Capital Management	-	Investments in shares of stock	15,000,000	150,000,000	10.00%	1,016,467,269	-
	Jardine Air Terminal Services	-	Investments in shares of stock	12,000,000	56,022,929	15.00%	57,798,292	-
	Sceince Park Cargo Service	-	Investments in shares of stock	4,431,000	44,310,000	14.77%	281,829,600	-
	Chung Hua Express Co.	-	Investments in shares of stock	2,200,000	22,000,000	11.00%	175,348,787	-
	Changi International Airport Services Pte.	-	Investments in shares of stock	2,640,000	18,764,706	4.40%	-	Note 3
	Regal International Advertising	-	Investments in shares of stock	592,500	5,925,000	6.58%	51,675,573	-
	Abacus International Holding, Ltd.—unlisted preferred stock	-	Investments in shares of stock	135,937	472,522	-	-	Note 3
	Chunghwa Telecom	-	Short-term investments	2,000,000	114,755,878	-	97,900,000	-
	France Telecom	-	Short-term investments	195,587	88,962,451	-	181,780,859	-
	<u>Mutual funds</u>							
	Ta Chong Gallop Bond Fund	-	Short-term investments	14,383,246.40	150,000,000	-	150,191,298	-
	Grand Cathay Bond Fund	-	Short-term investments	16,085,575.30	200,000,000	-	200,131,903	-
	Chung Hsing Ping-An Fund	-	Short-term investments	24,394,576.94	250,000,000	-	250,246,889	-
	The First Global Investment Trust Duo Li-2 Bond Fund	-	Short-term investments	14,273,581.70	200,000,000	-	200,399,660	-
	The First Global Investment Trust Duo Li Bond Fund	-	Short-term investments	25,050,739.80	400,000,000	-	400,426,055	-
	Tlam Solomon Bond Fund	-	Short-term investments	71,667,949.67	800,000,000	-	800,975,339	-
	Phoenix Bond Fund	-	Short-term investments	10,382,059.80	150,000,000	-	150,042,566	-
	JF (Taiwan) First Bond Fund	-	Short-term investments	7,396,996.80	100,000,000	-	100,032,547	-
	Fu-Hwa Bond Fund	-	Short-term investments	20,675,852.53	250,000,000	-	253,171,679	-
	Tiim Bond Fund	-	Short-term investments	14,727,757.40	200,000,000	-	200,017,673	-
	Prudential Financial Fund	-	Short-term investments	42,814,939.60	600,000,000	-	600,886,270	-
	NITC Taiwan Bond Fund	-	Short-term investments	14,865,353.80	200,000,000	-	200,728,359	-
	NITC Bond Fund	-	Short-term investments	1,267,788.70	200,000,000	-	200,008,881	-
	Barits Bond Fund	-	Short-term investments	12,861,956.90	150,000,000	-	150,218,653	-
	Cathay Bond Fund	-	Short-term investments	13,545,852.70	150,000,000	-	150,169,323	-

(Continued)

Held Company Name	Marketable Securities Type and Name	Relationship with the Company	Financial Statement Account	December 31, 2003				Note
				Shares/Units	Carrying Value	Percentage of Ownership	Market Value or Net Asset Value	
	The High-Yield Fund	-	Short-term investments	21,652,364.08	\$ 300,000,000	-	\$ 300,028,148	-
	The Wan Pao Fund	-	Short-term investments	20,608,075.62	300,000,000	-	300,076,250	-
	James Bond Fund	-	Short-term investments	33,747,983.60	500,000,000	-	500,047,248	-
	KGI Victory Fund	-	Short-term investments	9,699,415.13	100,000,000	-	100,230,846	-
	Fubon Ju-I Ii Fund	-	Short-term investments	14,356,265.10	200,000,000	-	200,314,403	-
	Truswell Bond Fund	-	Short-term investments	32,742,470.00	400,000,000	-	400,908,625	-
	Fuh-Hwa Albatross Fund	-	Short-term investments	9,347,978.50	100,000,000	-	100,432,811	-
	Fuh-Hwa Bond Fund	-	Short-term investments	27,863,234.90	350,000,000	-	354,459,356	-
	Invesco GP Aggressive Income Fund	-	Short-term investments	54,855,638.24	600,000,000	-	601,557,900	-
	Transcend Fortune Fund	-	Short-term investments	47,163,052.90	550,000,000	-	550,638,075	-
	Shinkong Chi-Shin Fund	-	Short-term investments	36,391,955.91	500,000,000	-	500,789,705	-
	Shinkong Chi-Shun Fund	-	Short-term investments	28,412,319.58	400,000,000	-	400,818,275	-
	Soaring Eagle Bond Fund	-	Short-term investments	47,947,407.26	500,000,000	-	500,383,937	-
	CITC Safe Income Fund	-	Short-term investments	17,856,122.50	250,000,000	-	252,696,274	-
	The Forever Fund	-	Short-term investments	10,802,402.45	150,000,000	-	150,007,562	-
	Weili Bond Fund	-	Short-term investments	9,861,446.67	100,000,000	-	100,157,783	-
	Union Bond Fund	-	Short-term investments	42,918,030.40	500,000,000	-	500,874,874	-
	Polaris De-Bao Fund	-	Short-term investments	9,414,334.30	100,000,000	-	100,179,814	-
Taiwan Air Cargo Terminal	<u>Mutual funds</u>							
	Grand Cathay Bond Fund	-	Short-term investments	19,847,474.20	246,926,396	-	246,936,320	-
	Prudential Financial Fund	-	Short-term investments	7,023,786.70	98,571,120	-	98,575,334	-
	Jih Sun Bond Fund	-	Short-term investments	29,274,089.08	383,183,189	-	383,203,681	-
	NITC Taiwan Bond Fund	-	Short-term investments	12,157,614.40	164,165,483	-	164,172,778	-
	NITC High Dividend Yield Balanced Fund	-	Short-term investments	3,001,787.50	30,017,875	-	30,228,000	-
	The Wan Pao Fund	-	Short-term investments	11,370,738.92	165,562,507	-	165,570,466	-
	The Incerement Fund	-	Short-term investments	15,002,271.83	218,968,659	-	218,979,161	-
	President Home Run Bond Fund	-	Short-term investments	14,004,050.90	188,522,533	-	188,532,336	-
	Fuh-Hwa Bond Fund	-	Short-term investments	14,613,032.10	185,885,075	-	185,898,227	-
	Fuh-Hwa Albatross Fund	-	Short-term investments	2,825,843.30	30,358,882	-	30,360,295	-
	Fuh-Hwa Heirloom Balance Fund	-	Short-term investments	1,662,662.70	20,420,158	-	20,448,091	-
	Fuh-Hwa Global Balanced Fund	-	Short-term investments	3,000,000.00	30,000,000	-	30,000,000	-
	Sheng Hua 1699 Bond Fund	-	Short-term investments	26,945,857.06	320,467,078	-	320,485,940	-
	Prudential Bond Fund	-	Short-term investments	14,843,105.60	221,632,800	-	221,643,190	-
	Prudential Unit-Link Fund	-	Short-term investments	5,000,000.00	50,891,500	-	50,919,000	-
	Asia Pacific Bond Fund	-	Short-term investments	6,547,516.46	80,169,101	-	80,173,030	-
	Fuhwa Classical Fund	-	Short-term investments	3,000,000.00	30,164,400	-	30,178,800	-
China Pacific Catering Services	<u>Mutual funds</u>							
	Sheng Hua 1699 Bond Fund	-	Short-term investments	3,476,980.14	40,000,000	-	41,354,159	-
	Long-River Bond Fund	-	Short-term investments	3,775,008.00	42,000,000	-	42,736,488	-
	Tlam Solomon Bond Fund	-	Short-term investments	3,078,210.43	34,099,522	-	34,402,695	-
	Fu-Hwa Bond Fund	-	Short-term investments	2,164,526.79	25,625,992	-	26,504,198	-
	Cash Reserves Fund	-	Short-term investments	4,969,238.90	54,249,535	-	55,653,488	-
	Prudential Financial Fund	-	Short-term investments	2,555,029.80	35,194,925	-	35,858,566	-
	NITC Taiwan Bond Fund	-	Short-term investments	391,027.50	5,119,333	-	5,280,318	-
	CITC Safe Income Fund	-	Short-term investments	1,679,593.60	23,000,000	-	23,769,273	-
	Transcend Fortune Fund	-	Short-term investments	4,107,705.40	46,500,000	-	47,958,282	-
	Truswell Bond Fund	-	Short-term investments	1,675,252.30	20,000,000	-	20,512,292	-
	Chung Hsing Ping-An Fund	-	Short-term investments	2,961,814.80	30,000,000	-	30,383,185	-
	Ta Chong Gallop Bond Fund	-	Short-term investments	1,469,608.50	15,000,000	-	15,345,799	-
	The Forever Fund	-	Short-term investments	1,444,148.73	20,000,000	-	20,054,171	-
	Prudential Bond Fund	-	Short-term investments	670,839.30	10,000,000	-	10,017,241	-
Mandarin Airlines	<u>Stock</u>							
	Mandarin Airlines Sweden AB	Equity-method investee	Investments in shares of stock	1,000	-	100.00%	-	-
	Mandarin Aircraft Trading Co., Ltd.	Equity-method investee	Investments in shares of stock	1,000	-	100.00%	-	-
	China Airlines	Parent company	Short-term investments	2,396,094	26,947,989	-	35,869,527	-

(Continued)

Held Company Name	Marketable Securities Type and Name	Relationship with the Company	Financial Statement Account	December 31, 2003				Note
				Shares/Units	Carrying Value	Percentage of Ownership	Market Value or Net Asset Value	
Hwa Sheng Investment	<u>Mutual funds</u>							
	Shinkong NT\$ High Yield Fund	-	Short-term investments	9,418,411.98	\$ 150,000,000	-	\$ 150,147,382	-
	The High-Yield Fund	-	Short-term investments	7,249,896.69	100,000,000	-	100,458,918	-
	The Incerement Fund	-	Short-term investments	3,425,502.18	50,000,000	-	50,000,000	-
	ABN AMRO Select Bond Fund	-	Short-term investments	6,891,355.82	75,000,000	-	75,015,165	-
	<u>Stock</u>							
	Inventec	-	Short-term investments	58,000	2,708,457	-	1,167,540	-
	Chunghwa Telecom	-	Short-term investments	200,000	11,457,970	-	9,790,000	-
	Mega Holdings	-	Short-term investments	152,000	5,701,419	-	3,114,480	-
	<u>Mutual funds</u>							
	Chung Hsing Ping-An Fund	-	Short-term investments	2,545,757.09	26,115,140	-	26,115,140	-
	Long-River Bond Fund	-	Short-term investments	11,280,465.50	127,705,022	-	127,705,022	-
	Phoenix Bond Fund	-	Short-term investments	3,679,384.90	53,174,839	-	53,174,839	-
	NITC Taiwan Bond Fund	-	Short-term investments	5,638,248.50	76,137,216	-	76,137,216	-
	The Wan Pao Fund	-	Short-term investments	1,359,203.77	19,791,502	-	19,791,502	-
	Sheng Hua 1699 Bond Fund	-	Short-term investments	1,249,437.10	14,860,430	-	14,860,430	-
	Truswell Bond Fund	-	Short-term investments	3,913,879.60	47,922,716	-	47,922,716	-
	Truswell Premier Fund	-	Short-term investments	809,922.50	8,645,842	-	8,645,842	-
	Fuh-Hwa Albatross Fund	-	Short-term investments	10,692,727.20	114,880,522	-	114,880,522	-
	Fuh-Hwa Bond Fund	-	Short-term investments	1,014,087.20	12,900,609	-	12,900,609	-
Polaris De-Bao Fund	-	Short-term investments	164,907.90	1,754,818	-	1,754,818	-	
Abacus Distribution Systems (Taiwan)	<u>Stock</u>							
	Yestrip Co., Ltd.	Equity-method investee	Short-term investments	2,600,000	30,897,905	100.00%	30,897,905	-
	<u>Mutual funds</u>							
	The Incerement Fund	-	Short-term investments	2,544,778.39	37,000,000	-	37,144,603	-
	Sheng Hua 1699 Bond Fund	-	Short-term investments	1,438,398.47	17,000,000	-	17,107,880	-
	Sheng Hua 5599 Bond Fund	-	Short-term investments	1,025,564.53	11,000,000	-	11,019,076	-
	Polaris Global Short-Duration Diversified Bond Fund	-	Short-term investments	470,000.00	4,700,000	-	4,700,000	-
	Nsm Short Term Fixed Income Fund	-	Short-term investments	41,378.10	18,244,320	-	18,152,986	-
NITC Taiwan Bond Fund	-	Short-term investments	209,606.50	2,817,677	-	2,830,463	-	
Cal-Asia Investment	<u>Stock</u>							
	Taiwan Airport Service (Macau)	Equity-method investee	Investments in shares of stock	-	108,734,694	24.49%	108,734,694	Note 2
	Eastern United International Logistics	Equity-method investee	Investments in shares of stock	600,000	9,908,265	20.00%	9,908,265	-
Hwa Hsia	<u>Stock</u>							
	China Airlines	Parent company	Short-term investments	940,307	11,225,890	-	14,076,396	-
	Hwa Shin	Equity-method investee	Investments in shares of stock	1,000,000	10,000,000	100.00%	10,000,000	-

Note 1: Based on the ROC Statement of Financial Accounting Standards No. 30, "Accounting for Treasury Stocks," Company shares held by subsidiaries are reclassified from investment in shares of stocks to treasury stocks.

Note 2: Limited company.

Note 3: The subsidiary's financial statements as of and for the year ended December 31, 2003 were not available as of February 25, 2004, the date of the accompanying auditors' report.

## CHINA AIRLINES, LTD. AND INVESTEEES

## MARKETABLE SECURITIES ACQUIRED AND DISPOSED OF AT COSTS OR PRICES OF AT LEAST NT\$100 MILLION OR 20% OF THE PAID-IN CAPITAL

FOR THE YEAR ENDED DECEMBER 31, 2003

(Amounts in New Taiwan Dollars, Unless Specified Otherwise)

Company Name	Marketable Securities Type and Name	Financial Statement Account	Counter-Party	Nature of Relationship	Beginning Balance		Acquisition		Disposal			Ending Balance			
					Shares/Units	Amount	Shares/Units	Amount	Shares/Units	Amount	Carrying Value	Gain (Loss) on Disposal	Shares/Units	Amount	
China Airlines	<u>Mutual funds</u>														
	Ta Chong Gallop Bond Fund	Short-term investments	-	-	-	\$ -	30,424,311.50	\$ 350,000,000	16,041,065.10	\$ 200,060,956	\$ 200,000,000	\$ 60,956	14,383,246.40	\$ 150,000,000	
	Ta Chong Bond Fund	Short-term investments	-	-	-	-	67,611,395.00	700,000,000	67,611,395.00	701,810,741	700,000,000	1,810,741	-	-	
	Grand Cathay Bond Fund	Short-term investments	-	-	-	-	117,657,209.60	1,450,000,000	101,571,634.30	1,252,879,555	1,250,000,000	2,879,555	16,085,575.30	200,000,000	
	Central Diamond Bond Fund	Short-term investments	-	-	-	-	312,818,603.73	3,400,000,000	312,818,603.73	3,407,776,079	3,400,000,000	7,776,079	-	-	
	Chung Hsing Ping-An Fund	Short-term investments	-	-	-	-	196,973,661.14	2,000,000,000	172,579,084.20	1,754,009,409	1,750,000,000	4,009,409	24,394,576.94	250,000,000	
	The First Global Investment Trust Duo Li Bond Fund	Short-term investments	-	-	-	-	47,156,636.50	750,000,000	22,105,896.70	350,804,982	350,000,000	804,982	25,050,739.80	400,000,000	
	The First Global Investment Trust Duo Li-2 Bond Fund	Short-term investments	-	-	-	-	64,586,800.70	900,000,000	50,313,219.00	701,507,107	700,000,000	1,507,107	14,273,581.70	200,000,000	
	Jih Sun Bond Fund	Short-term investments	-	-	-	-	61,869,838.07	800,000,000	61,869,838.07	802,182,129	800,000,000	2,182,129	-	-	
	Long-River Bond Fund	Short-term investments	-	-	-	-	258,083,462.90	2,900,000,000	258,083,462.90	2,904,724,397	2,900,000,000	4,724,397	-	-	
	Tlam Solomon Bond Fund	Short-term investments	-	-	-	-	410,184,150.26	4,550,000,000	338,516,200.59	3,757,941,018	3,750,000,000	7,941,018	71,667,949.67	800,000,000	
	Phoenix Bond Fund	Short-term investments	-	-	-	-	146,690,804.90	2,100,000,000	136,308,745.10	1,956,737,323	1,950,000,000	6,737,323	10,382,059.80	150,000,000	
	JF (Taiwan) First Bond Fund	Short-term investments	-	-	-	-	7,396,996.80	100,000,000	-	-	-	-	7,396,996.80	100,000,000	
	JF (Taiwan) Bond Fund	Short-term investments	-	-	-	-	6,925,687.40	100,000,000	6,925,687.40	100,132,281	100,000,000	132,281	-	-	
	Fu-Hwa Bond Fund	Short-term investments	-	-	-	-	62,264,817.95	750,000,000	41,588,965.42	500,709,047	500,000,000	709,047	20,675,852.53	250,000,000	
	Tiim Bond Fund	Short-term investments	-	-	-	-	100,307,823.70	1,350,000,000	85,580,066.30	1,152,234,400	1,150,000,000	2,234,400	14,727,757.40	200,000,000	
	Prudential Well Pool Fund	Short-term investments	-	-	-	-	33,495,587.20	400,000,000	33,495,587.20	400,532,225	400,000,000	532,225	-	-	
	Prudential Financial Fund	Short-term investments	-	-	-	-	194,048,343.40	2,700,000,000	151,233,403.80	2,105,462,049	2,100,000,000	5,462,049	42,814,939.60	600,000,000	
	NITC Taiwan Bond Fund	Short-term investments	-	-	-	-	29,817,291.90	400,000,000	14,951,938.10	201,092,548	200,000,000	1,092,548	14,865,353.80	200,000,000	
	NITC Bond Fund	Short-term investments	-	-	-	-	9,865,196.90	1,550,000,000	8,597,408.20	1,351,237,370	1,350,000,000	1,237,370	1,267,788.70	200,000,000	
	Barits Bond Fund	Short-term investments	-	-	-	-	25,882,881.20	300,000,000	13,020,924.30	150,506,326	150,000,000	506,326	12,861,956.90	150,000,000	
	Cathay Capital Income Growth Bond Fund	Short-term investments	-	-	-	-	14,485,914.20	150,000,000	14,485,914.20	150,879,109	150,000,000	879,109	-	-	
	Cathay Bond Fund	Short-term investments	-	-	-	-	31,648,525.80	350,000,000	18,102,673.10	200,113,518	200,000,000	113,518	13,545,852.70	150,000,000	
	The Increment Fund	Short-term investments	-	-	-	-	121,275,998.16	1,750,000,000	121,275,998.16	1,753,810,947	1,750,000,000	3,810,947	-	-	
	The High-Yield Fund	Short-term investments	-	-	-	-	21,652,364.08	300,000,000	-	-	-	-	21,652,364.08	300,000,000	
	The Wan Pao Fund	Short-term investments	-	-	-	-	31,055,067.58	450,000,000	10,446,991.96	150,102,380	150,000,000	102,380	20,608,075.62	300,000,000	
	Sheng Hua 1699 Bond Fund	Short-term investments	-	-	-	-	76,808,429.54	900,000,000	76,808,429.54	902,412,687	900,000,000	2,412,687	-	-	
	Sheng Hua 5599 Bond Fund	Short-term investments	-	-	-	-	65,903,569.62	700,000,000	65,903,569.62	702,517,908	700,000,000	2,517,908	-	-	
	President Home Run Bond Fund	Short-term investments	-	-	-	-	52,545,865.40	700,000,000	52,545,865.40	704,282,908	700,000,000	4,282,908	-	-	
	James Bond Fund	Short-term investments	-	-	-	-	61,068,836.50	900,000,000	27,320,852.90	400,644,032	400,000,000	644,032	33,747,983.60	500,000,000	
	ABN AMRO Bond Fund	Short-term investments	-	-	-	-	20,845,456.25	300,000,000	20,845,456.25	300,306,442	300,000,000	306,442	-	-	
	ABN AMRO Select Bond Fund	Short-term investments	-	-	-	-	9,257,802.01	100,000,000	9,257,802.01	100,027,773	100,000,000	27,773	-	-	
	KGI Victory Fund	Short-term investments	-	-	-	-	150,951,983.55	1,550,000,000	141,252,568.42	1,453,064,911	1,450,000,000	3,064,911	9,699,415.13	100,000,000	
	Fubon Ju-I Fund	Short-term investments	-	-	-	-	9,951,646.60	150,000,000	9,951,646.60	150,122,449	150,000,000	122,449	-	-	
	Fubon Ju-I Li Fund	Short-term investments	-	-	-	-	21,590,480.00	300,000,000	7,234,214.90	100,308,900	100,000,000	308,900	14,356,265.10	200,000,000	
	Truswell Bond Fund	Short-term investments	-	-	-	-	326,145,413.70	3,950,000,000	293,402,943.70	3,556,898,186	3,550,000,000	6,898,186	32,742,470.00	400,000,000	
	Fuh-Hwa Albatross Fund	Short-term investments	-	-	-	-	9,347,978.50	100,000,000	-	-	-	-	9,347,978.50	100,000,000	
	Fuh-Hwa Bond Fund	Short-term investments	-	-	-	-	27,863,234.90	350,000,000	-	-	-	-	27,863,234.90	350,000,000	
	Invesco GP Aggressive Income Fund	Short-term investments	-	-	-	-	216,447,184.47	2,350,000,000	161,591,546.23	1,755,124,938	1,750,000,000	5,124,938	54,855,638.24	600,000,000	
	Transcend Fortune Fund	Short-term investments	-	-	-	-	180,995,300.80	2,100,000,000	133,832,247.90	1,553,345,627	1,550,000,000	3,345,627	47,163,052.90	550,000,000	
	Shinkong NTS High Yield Fund	Short-term investments	-	-	-	-	199,453,485.39	3,150,000,000	199,453,485.39	3,159,714,562	3,150,000,000	9,714,562	-	-	
	Shinkong Chi-Shin Fund	Short-term investments	-	-	-	-	51,070,474.79	700,000,000	14,678,518.88	200,162,162	200,000,000	162,162	36,391,955.91	500,000,000	
	Shinkong Chi-Shun Fund	Short-term investments	-	-	-	-	28,412,319.58	400,000,000	-	-	-	-	28,412,319.58	400,000,000	
	United Taiwan Bond Fund	Short-term investments	-	-	-	-	35,235,336.81	500,000,000	35,235,336.81	500,095,135	500,000,000	95,135	-	-	
	Soaring Eagle Bond Fund	Short-term investments	-	-	-	-	154,400,402.51	1,600,000,000	106,452,995.25	1,101,990,949	1,100,000,000	1,990,949	47,947,407.26	500,000,000	
	CITC Safe Income Fund	Short-term investments	-	-	-	-	17,856,122.50	250,000,000	-	-	-	-	17,856,122.50	250,000,000	
	The Forever Fund	Short-term investments	-	-	-	-	69,129,255.60	950,000,000	58,326,853.15	801,297,702	800,000,000	1,297,702	10,802,402.45	150,000,000	
	Dresdner Bond Dam Fund	Short-term investments	-	-	-	-	9,028,204.11	100,000,000	9,028,204.11	100,067,712	100,000,000	67,712	-	-	
	Weili Bond Fund	Short-term investments	-	-	-	-	49,642,471.74	500,000,000	39,781,025.07	401,042,365	400,000,000	1,042,365	9,861,446.67	100,000,000	
	United Bond Fund	Short-term investments	-	-	-	-	16,226,298.33	200,000,000	16,226,298.33	200,301,658	200,000,000	301,658	-	-	
	Union Bond Fund	Short-term investments	-	-	-	-	411,057,257.21	4,750,000,000	368,139,226.81	4,258,307,894	4,250,000,000	8,307,894	42,918,030.40	500,000,000	
	Polaris De-Li Fund	Short-term investments	-	-	-	-	13,937,914.40	200,000,000	13,937,914.40	200,368,684	200,000,000	368,684	-	-	
	Polaris De-Bao Fund	Short-term investments	-	-	-	-	14,160,013.40	150,000,000	4,745,679.10	50,236,810	50,000,000	236,810	9,414,334.30	100,000,000	
Taiwan Air Cargo Terminal	<u>Mutual funds</u>														
	Grand Cathay Bond Fund	Short-term investments	-	-	-	21,077,326.90	257,223,482	42,555,878.40	526,617,966	43,785,731.10	541,617,967	536,915,052	4,702,915	19,847,474.20	246,926,396
	Prudential Financial Fund	Short-term investments	-	-	-	5,212,953.60	71,745,359	15,858,406.50	221,234,767	14,047,573.40	196,234,767	194,409,006	1,825,761	7,023,786.70	98,571,120
	Jih Sun Bond Fund	Short-term investments	-	-	-	36,580,896.20	469,402,402	67,414,901.00	877,575,957	74,721,708.12	972,575,957	963,795,170	8,780,787	29,274,089.08	383,183,189
	Shinkong Chi-Shin Fund	Short-term investments	-	-	-	8,504,868.58	114,973,916	8,504,868.58	116,053,184	17,009,737.16	232,218,632	231,027,100	1,191,532	-	-
	Shinkong NTS High Yield Fund	Short-term investments	-	-	-	3,539,749.17	55,359,907	3,539,749.17	55,911,400	7,079,498.34	112,140,670	111,271,307	869,363	-	-
	ABN AMRO Bond Fund	Short-term investments	-	-	-	187,062,559	8,464,695.60	121,537,792	21,606,925.61	310,178,539	308,600,351	1,578,188	-	-	
	NITC Bond Fund	Short-term investments	-	-	-	974,456.40	151,004,352	79,361.50	12,414,043	1,053,817.90	164,840,152	163,418,395	1,421,757	-	-
	NITC Taiwan Bond Fund	Short-term investments	-	-	-	25,168.20	333,401	39,274,762.90	525,837,916	27,142,316.70	364,855,792	362,005,834	2,849,958	12,157,614.40	164,165,483
	The Wan Pao Fund	Short-term investments	-	-	-	13,491,794.17	192,484,729	22,741,477.84	329,601,066	24,862,533.09	359,601,066	356,523,288	3,077,778	11,370,738.92	165,562,507
	The Increment Fund	Short-term investments	-	-	-	7,031,303.59	100,561,704	35,219,139.20	510,961,088	27,248,170.96	395,961,088	392,554,133	3,406,955	15,002,271.83	218,968,659
	James Bond Fund	Short-term investments	-												

Company Name	Marketable Securities Type and Name	Financial Statement Account	Counter-Party	Nature of Relationship	Beginning Balance		Acquisition		Disposal			Ending Balance		
					Shares/Units	Amount	Shares/Units	Amount	Shares/Units	Amount	Carrying Value	Gain (Loss) on Disposal	Shares/Units	Amount
Mandarin Airlines	Prudential Unit-Link Fund	Short-term investments	-	-	-	\$ -	10,000,000.00	\$ 100,891,500	5,000,000.00	\$ 50,891,500	\$ 50,000,000	\$ 891,500	5,000,000.00	\$ 50,891,500
	Asia Pacific Bond Fund	Short-term investments	-	-	-	-	13,095,032.94	160,169,101	6,547,516.48	80,169,101	80,000,000	169,101	6,547,516.46	80,169,101
	<u>Mutual fund</u>													
	Shinkong NT\$ High Yield Fund	Short-term investments	-	-	1,598,404.15	25,000,000	37,614,188.47	595,000,000	29,794,180.64	470,982,308	470,000,000	982,308	9,418,411.98	150,000,000
	Shinkong Chi-Shun Fund	Short-term investments	-	-	-	-	7,894,642.56	110,000,000	7,894,642.56	110,501,265	110,000,000	501,265	-	-
	The High-Yield Fund	Short-term investments	-	-	-	-	8,704,780.74	120,000,000	1,454,884.05	20,085,693	20,000,000	85,693	7,249,896.69	100,000,000
	ABN AMRO Bond Fund	Short-term investments	-	-	-	-	9,064,742.00	130,000,000	9,064,742.00	130,409,074	130,000,000	409,074	-	-
ABN AMRO Select Bond Fund	Short-term investments	-	-	-	-	24,385,839.38	265,000,000	17,494,483.56	190,095,145	190,000,000	95,145	6,891,355.82	75,000,000	
Hwa Sheng	<u>Stock</u>													
	China Airlines	Short-term investments	-	-	12,468,000.00	195,376,951	1,226,800.00	-	13,694,800	203,753,254	195,376,951	8,376,303	-	-
	<u>Mutual funds</u>													
	Long-River Bond Fund	Short-term investments	-	-	5,475,679.30	60,777,850	22,587,430.70	254,921,192	16,782,644.50	189,431,192	187,994,020	1,437,172	11,280,465.50	127,705,022
	Phoenix Bond Fund	Short-term investments	-	-	2,771,872.10	39,231,692	7,358,769.80	105,913,378	6,451,257.00	92,843,378	91,970,231	873,147	3,679,384.90	53,174,839
Hwa Hsia	NITC Taiwan Bond Fund	Short-term investments	-	-	757,782.40	10,038,950	11,276,497.00	151,960,437	6,396,030.90	86,280,437	85,862,171	418,266	5,638,248.50	76,137,216
	Fuh-Hwa Albatross Fund	Short-term investments	-	-	10,692,727.20	112,384,840	21,385,454.40	228,558,113	21,385,454.40	228,558,113	226,062,431	2,495,682	10,692,727.20	114,880,522
	<u>Mutual funds</u>													
	Tuswell Bond Fund	Short-term investments	-	-	4,220,209.90	49,973,060	1,569,397.60	19,000,000	5,789,607.50	70,595,168	68,973,060	1,622,108	-	-

**TABLE 4**

**CHINA AIRLINES, LTD. AND INVESTEEES**

**TOTAL PURCHASE FROM OR SALE TO RELATED PARTIES AMOUNTING TO AT LEAST NT\$100 MILLION OR 20% OF THE PAID-IN CAPITAL  
FOR THE YEAR ENDED DECEMBER 31, 2003**

(Amounts in New Taiwan Dollars, Unless Specified Otherwise)

Company Name	Related Party	Nature of Relationship	Transaction Details				Abnormal Transaction		Note/Accounts Payable or Receivable		Note
			Purchase/ Sale	Amount	% to Total	Payment Terms	Unit Price	Payment Terms	Ending Balance	% to Total	
China Airlines	Taiwan Air Cargo Terminal	Equity-method investee	Purchase	\$ 161,587,331	0.27%	30 days	\$ -	-	(\$ 22,269,243)	( 1.42%)	-
	China Pacific Catering Services	Equity-method investee	Purchase	791,026,822	1.31%	60 days	-	-	( 233,616,043)	( 14.91%)	-
	Taoyuan International Airport Service	Equity-method investee	Purchase	686,947,585	1.14%	40 days	-	-	( 188,958,071)	( 12.06%)	-
	Mandarin Airlines	Equity-method investee	Sale	( 761,747,264)	( 1.00%)	2 months	-	-	268,128,012	4.44%	-
		Equity-method investee	Purchase	141,903,319	0.23%	2 months	-	-	( 349,241,095)	( 22.29%)	-
	Taiwan Airport Service	Equity-method investee	Purchase	250,472,085	0.41%	40 days	-	-	( 39,695,994)	( 2.53%)	-
	Hwa Hsia	Equity-method investee	Purchase	195,659,187	0.32%	2 months	-	-	( 19,016,043)	( 1.21%)	-
	Global Sky Express	Equity-method investee	Sale	( 179,200,823)	( 0.24%)	30 days	-	-	13,297,445	0.22%	-

**CHINA AIRLINES, LTD. AND INVESTEES**

**RECEIVABLES FROM RELATED PARTIES AMOUNTING TO AT LEAST NT\$100 MILLION OR 20% OF THE PAID-IN CAPITAL**

**DECEMBER 31, 2003**

**(Amounts in Thousand New Taiwan Dollars, Unless Specified Otherwise)**

Company Name	Related Party	Nature of Relationship	Ending Balance	Turnover Rate	Overdue		Amounts Received in Subsequent Period	Allowance for Bad Debts
					Amount	Action Taken		
China Airlines	Mandarin Airlines	Equity-method investee	\$268,128,012	3.14	\$ -	-	\$3,818,560	\$ -

## CHINA AIRLINES, LTD. AND INVESTEEES

## NAMES, LOCATIONS, AND OTHER INFORMATION OF INVESTEEES ON WHICH THE COMPANY EXERCISES SIGNIFICANT INFLUENCE

FOR THE YEAR ENDED DECEMBER 31, 2003

(Amounts in New Taiwan Dollars, Unless Specified Otherwise)

Investor Company	Investee Company	Location	Main Businesses and Products	Original Investment Amount		Balance as of December 31, 2003			Net Income (Loss) of the Investee	Investment Income (Loss)	Note
				Dec. 31, 2003	Dec. 31, 2002	Shares	Percentage of Ownership (%)	Carrying Value			
China Airlines	Taiwan Air Cargo Terminal	Taoyuan, Taiwan	Air cargo and storage	\$ 1,350,000,000	\$ 1,350,000,000	135,000,000	54.00	\$ 1,668,302,636	\$ 334,531,661	\$ 174,634,197	-
	China Pacific Catering Services	Taoyuan, Taiwan	In-flight catering	744,600,000	744,600,000	74,460,000	51.00	864,196,663	130,062,584	66,232,789	-
	Cal-Dynasty International	Los Angeles, U.S.A.	A holding company, real estate, hotel service, lease of aircraft and serving as cargo agent	US\$ 26,145,000	US\$ 26,145,000	2,614,500	100.00	816,757,176	35,472,647	35,472,647	Note 1
	Taoyuan International Airport Service	Taoyuan, Taiwan	Airport service	147,000,000	147,000,000	34,300,000	49.00	768,279,978	87,881,860	41,932,490	-
	Mandarin Airlines	Taipei, Taiwan	Air transportation and maintenance of aircraft	2,916,250,274	2,916,250,274	216,441,585	90.05	736,714,570	( 288,478,399 )	( 226,898,057 )	Note 2
	Hwa Sheng Investment	Taipei, Taiwan	General investment	500,000,000	500,000,000	50,000,000	100.00	517,935,309	60,396,490	10,844,616	Note 2
	Abacus Distribution System (Taiwan)	Taipei, Taiwan	Sale and maintenance of hardware and software	90,000,000	90,000,000	22,450,008	93.93	391,719,910	62,949,608	57,742,807	-
	Taiwan Airport Service	Taipei, Taiwan	Airport services	12,289,100	12,289,100	17,188,870	47.35	337,237,539	16,076,386	7,492,716	-
	Kaoshiung Catering Services	Kaoshiung, Taiwan	In-flight catering	115,500,000	115,500,000	12,705,000	31.76	155,148,478	67,503,410	20,654,419	-
	Cal-Asia Investment	Territory of the British Virgin Islands	General investment	US\$ 4,000,000	US\$ 4,000,000	4,000,000	100.00	147,288,230	4,323,585	4,323,585	-
	Asian Compressor Technology Services	Taoyuan, Taiwan	Research, manufacture and maintenance of engines	77,322,000	77,322,000	7,732,200	24.50	145,241,480	65,200,720	15,885,978	-
	China Pacific Laundry Services	Taoyuan, Taiwan	Cleaning and leasing of the tower of airline company, hotel, restaurant, and health club	137,500,000	137,500,000	13,750,000	55.00	104,498,395	3,155,889	1,735,739	-
	Hwa Hsia	Taipei, Taiwan	Cleaning of aircraft and maintenance of machine and equipment	50,000,000	50,000,000	50,000	100.00	88,974,057	6,957,070	8,757,602	Note 2
	Dynasty Holidays	Tokyo, Japan	Travel business	JPY 20,400,000	JPY 20,400,000	408	51.00	24,528,593	( 15,806,895 )	( 8,061,516 )	-
	ICAS Co., Ltd.	Taoyuan, Taiwan	Manufacture and retail of aircraft and its related parts	8,500,000	8,500,000	850,000	25.00	7,426,254	( 12,259,574 )	( 3,064,893 )	-
	Global Sky Express	Taipei, Taiwan	Forwarding and storage of air cargo	2,500,000	2,500,000	250,000	25.00	5,110,714	6,017,560	1,460,005	-
	Freighter Princess Ltd.	Cayman Islands	Aircraft lease	US\$ 1,000	US\$ 1,000	1,000	100.00	35,088	-	-	-
Freighter Prince Ltd.	Cayman Islands	Aircraft lease	US\$ 1,000	US\$ 1,000	1,000	100.00	34,602	-	-	-	
Freighter Queen Ltd.	Cayman Islands	Aircraft lease	US\$ 1,000	US\$ 1,000	1,000	100.00	32,895	-	-	-	
Spacehab Taiwan	Taipei, Taiwan	Sourcing domestic capital to invest in Spacehab U.S.A.	54,000,000	54,000,000	-	-	-	( 49,479,941 )	( 10,698,366 )	-	
Taoyuan International Airport Service	Taiwan Whi Lin Industry Co., Ltd.	Taichung, Taiwan	Other machine manufacturing	49,477,500	49,477,500	4,275,000	38.69	43,164,987	1,431,686	( 689,651 )	-
	Tao Yao Co., Ltd.	Taoyuan, Taiwan	Manpower placement and machine installation	10,000,000	9,999,940	1,000,000	100.00	11,092,709	44,002	44,002	-
Mandarin Airlines	Mandarin Airlines Sweden AB	Sweden	Aircraft leasing agency	337,000	337,000	1,000	100.00	-	-	-	-
	Mandarin Aircraft Trading Co., Ltd	Cyprus	Aircraft leasing agency	60,000	60,000	1,000	100.00	-	-	-	-
Abacus Distribution System (Taiwan)	Yestrip Co., Ltd.	Taipei, Taiwan	Travel business	26,000,000	26,000,000	2,600,000	100.00	30,897,905	7,750,077	7,750,077	-
Taiwan Airport Service	Taiwan Airport Service (Macau)	Macau	Airport service and investment	US\$ 3,525,726	US\$ 1,050,000	-	26.53	117,642,090	5,951,037	1,578,810	Note 3
Cal Asia Investment	Taiwan Airport Service (Macau)	Macau	Forwarding and storage of air cargo	US\$ 3,254,526	US\$ 1,700,000	-	24.49	108,734,694	5,963,607	1,448,897	Note 3
	Eastern United International Logistics	Hong Kong	Forwarding and storage of air cargo	HKS 1,500,000	HKS 1,500,000	600,000	20.00	9,908,265	12,532,492	2,506,498	-
Hwa Hsia	Hwa Shin Building Safeguard Co., Ltd.	Taipei, Taiwan	Building security and maintenance services	10,000,000	-	1,000,000	100.00	10,000,000	-	-	-

Note 1: Represents the consolidated financial information of the foreign holding company disclosed in accordance with local regulations.

Note 2: Adopted the treasury stock method in recognizing investment income or loss.

Note 3: The Company was established as a limited company.

## CHINA AIRLINES, LTD. AND INVESTEEES

INVESTMENT IN MAINLAND CHINA  
 FOR THE YEAR ENDED DECEMBER 31, 2003  
 (Amounts in New Taiwan Dollars, Unless Otherwise Noted)

Investee Company Name	Main Businesses and Products	Total Amount of Paid-in Capital	Investment Type (e.g., Direct or Indirect)	Accumulated Outflow of Investment from Taiwan as of Jan. 1, 2003	Investment Flows		Accumulated Outflow of Investment from Taiwan as of Dec. 31, 2003	% Ownership of Direct or Indirect Investment	Investment Gain (Loss) (Note 2)	Carrying Value as of Dec. 31, 2003	Accumulated Inward Remittance of Earnings as of Dec. 31, 2003	Accumulated Investment in Mainland China as of Dec. 31, 2003	Investment Amounts Authorized by Investment Commission, MOEA	Upper Limit on Investment
					Outflow	Inflow								
Siamen International Air Cargo Terminal Ltd.	Air cargo and storage	\$941,610,728	(Note 1)	\$59,233,450 (Note 3)	\$51,464,713 (Note 4)	-	\$110,698,163 (Note 5)	12%	\$1,506,655	\$108,734,694	-	\$110,698,163 (Note 5)	\$1,714,285,714 (Note 6)	\$11,173,890,433

Note 1: The Company invested in Cal-Asia Investment, which invested in Taiwan Airport Service (Macau), which invested in Mainland China.

Note 2: The accrual basis is based on the financial statements audited by international accounting firms with cooperative relationship with R.O.C. accounting firms.

Note 3: US\$1,700,000.

Note 4: US\$1,554,526.

Note 5: US\$3,254,526.

Note 6: US\$50,400,000.