




SriLankan
Airlines

SriLankan Airlines. A destination between two destinations.

Vision/Mission

To be the most preferred airline in Asia

We are in the air transportation business.

We provide our customers with a reliable and pleasant travel experience.

We provide our business partners with a variety of innovative, professional and mutually profitable services.

We meet shareholders' expectations of profitably marketing Sri Lanka and contributing towards the well-being of society.

We are a competent, pro-active and diligent team.

Our contribution is recognized and rewarded.

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LEGAL FORM

Public Limited Liability Company

DIRECTORS

D H S Jayawardena - Chairman

S Ukwatte

R A Chandiram

N A Wickremasinghe

T C Clark - Managing Director

G W Chapman

N J Hopkins

P M Hill

(Alternate to T C Clark)

M Flanagan

(Alternate to G W Chapman)

Ghaith Al Ghaith

(Alternate to N J Hopkins)

COMPANY SECRETARY

Mildred Peries

REGISTERED OFFICE

#22-01, East Tower

World Trade Centre

Echelon Square

Colombo 1

Sri Lanka

AUDITORS

Ernst & Young

Chartered Accountants

PO Box 101

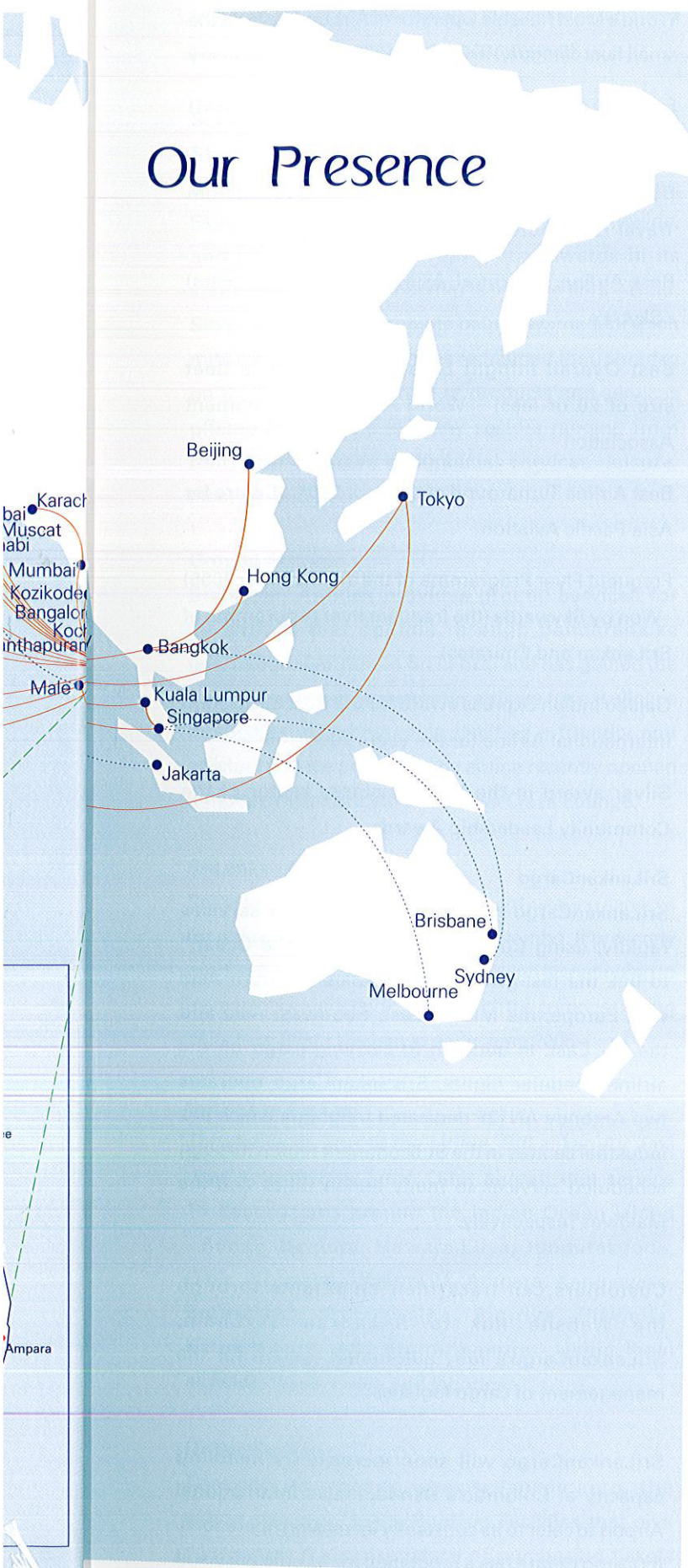
Colombo 10

SriLankan
The National Carrier



----- Code Share
 ——— Direct Flights

Our Presence



The history of SriLankan Airlines dates back to September 1979, spearheading itself as the National Airline of Sri Lanka. It has re-invented itself in recent times, winning numerous international awards and establishing its steadfast reputation as a global leader in service, comfort, reliability and punctuality.

SriLankan now serves 49 destinations in 28 countries in Europe, North America, the Middle East, South Asia, Southeast Asia, the Far East, and Australia. It is the largest foreign carrier operating to India, with 85 weekly flights to 9 destinations. It also serves another 14 domestic destinations in Sri Lanka.

Expansion

SriLankan has maintained a vehement programme to expand its number of destinations, and the frequency of flights to each destination, through its own flights and code shares. The new destinations that have been graced by SriLankan in the last three years include Amsterdam, Brussels, Düsseldorf, Birmingham, Glasgow, Larnaca, Manchester, Bradford, Teesside, Edinburgh, Belfast, Dublin, Karachi, Calicut, Kochi, Hyderabad, Bangalore, Jakarta, Beijing, New York, Brisbane, Melbourne, Sydney and Vienna. Goa will be the next addition of direct flights to India, lined up for the year 2006/07.

In August 2006, the Company is planning to launch a Duty Free shop at the Bandaranaike International Airport. Among the many products on offer will be SriLankan logo branded products, travel accessories, exclusive local handicrafts and mementos, etc.

Code-shares

SriLankan has code-share services with Emirates, bmi (British Midland), and Malaysian Airlines.

Shareholding

Government of Sri Lanka	51.05%
Emirates	43.63%
Employees	5.32%

Board of Directors

Four Members of the Board are appointed by the Government of Sri Lanka, and three by Emirates.

Management

SriLankan is managed by Emirates International, which has a 10-year contract which concludes in 2008. Till 1999 it was known as Air Lanka, and later re-branded itself as SriLankan Airlines.

Fleet

SriLankan underwent a complete re-fleeting programme which commenced in 1999, converting its international passenger network to a modern all-Airbus fleet.

Airbus A340	5 aircraft
Airbus A330-200	4 aircraft
Airbus A320-200	5 aircraft
Antonov AN12F freighter	2 aircraft
Turbo Otter	2 aircraft

Workforce

SriLankan boasts of a resourceful workforce of approximately 5,400 persons in Sri Lanka and overseas. The airline has efficient training programmes in all aviation related fields, in order to successfully carry out its own expansion and the constant need to replace staff who are in high demand by other airlines.

Inflight Comforts

The SriLankan fleet comprises state-of-the-art Airbus A340, A330 and A320 aircraft with luxurious seats that have ample pitch and width. Seating is devised in a 2-class system of Business and Economy classes. All seats are equipped with the latest inflight entertainment with 18-channel seat-back television, 22-channel audio and 16 video games in all seats, with Business Class having a choice of videos as well.

Awards

SriLankan has consistently achieved very high marks for excellence, especially in polls conducted by global travellers and enterprises. The awards include:

World's Best Airline in a survey of Economy Class passengers

World's Friendliest Cabin Staff - Skytrax

World's Most Reliable Operator of Airbus A330s (in the small fleet category) in 2002 and 2003 - Airbus Industry

First Runner-up for World's Best Cabin Staff - Skytrax

Best Airline in South Asia (3 consecutive years) from Travel Trade Gazette

Best Airline in Central Asia (4 consecutive years) - Skytrax

Best Overall Inflight Entertainment (for a fleet size of 20 or less) - World Airline Entertainment Association

Best Airline Turnaround of the Year 2004 - Centre for Asia Pacific Aviation

Frequent Flyer Programme of the Year (2003 & 2005) - Won by Skywards (the frequent flyer programme of SriLankan and Emirates)

Galileo Indian Express award for the Best Eastbound International Airline for the years 2004 - 05

Silver award in the large business sector at the Community Leadership Awards

SriLankanCargo

SriLankanCargo has been expanding its services rapidly, using Colombo as a "Hub in the Ocean" to link the fast-growing economies of South Asia with Europe, the Middle East, Southeast Asia and the Far East. In addition to carrying cargo on the airline's regular flights, SriLankanCargo operates two Antonov AN12F dedicated freighters which link industrial centres in the Subcontinent region through scheduled services to many Indian Cities and the Maldives respectively.

Customers can track their shipments through the Website link to SriLankan SkyChain, SriLankanCargo's fully automated system for the management of cargo logistics.

SriLankanCargo will soon increase its handling capacity at Colombo's Bandaranaike International Airport to cater to its constantly increasing operations. Its Cargo Centre has a reputation for its efficiency and

impeccable standards, having successfully adopted the Japanese 5S system of management.

Skywards

Skywards is the frequent flyer programme of SriLankan and Emirates, our strategic partner. Skywards has over 1.4 million members worldwide, and has consistently swept global awards in its short existence. Membership is in three tiers – Gold, Silver and Blue - with points being awarded for each mile travelled, which can be redeemed for upgrades on flights or a wide array of products and services offered by partners in many sectors ranging from rent-a-car services to financial services, leisure, lifestyle, and hotel stays.

Ground Services

SriLankan Airlines provides ground services for all airlines that operate through Bandaranaike International Airport in Sri Lanka, and has gained the acknowledgment of customer airlines for excellence in successfully conducting itself as a friendly and efficient service provider. The airline recently opened a modern sophisticated Business Class Lounge.

SriLankan Catering

SriLankan Catering provides on-board catering services for airlines that operate through Colombo. It presently produces over 11,000 meals per day, and is continuing to increase its production capacity with the commissioning of its new Flight Kitchen in early June 2006.

SriLankan Air Taxi

The domestic arm of the airline, SriLankan Air Taxi uses amphibious Turbo Otter aircraft that service 14 destinations around the Indian Ocean island - Kandy, Bentota, Nuwara-Eliya, Hingurakgoda, Galle (Koggala), Weerawila, Ampara, Katunayake, Ratmalana, Trincomalee, Sigiriya, Dikwella, Katukurunda, and Anuradhapura - using local airfields, lakes, rivers and lagoons.

Online Facilities

Through its website www.srilankan.aero, the airline provides Online Booking Facilities that give passengers the convenience of purchasing tickets

through any PC or laptop, and E-ticketing facilities that enable traveling without paper tickets. It also displays Flight Schedules on mobile phones that offer GPRS options.

Sports Tourism

SriLankan has a special focus on sports tourism and conducts an annual *Golf* tournament, two *Surfing* championships, horse races, and an international *Rugby* tournament to add to its impressive forte.

SriLankan Holidays

The airline is in partnership with leading and exclusive tour operators in many countries to provide tailor-made holiday packages for tourists.

SriLankan Adventures

The airline works with local adventure tourism companies to provide the finest packages for tourists seeking the thrills of rafting, hiking, biking, etc. These packages are also tailor-made to cater to those who wish to enjoy the natural splendor of our island and be enticed by Sri Lanka's unique and exotic wilds.

MICE Tourism

Sri Lanka is a popular destination for business events in the South Asian region. The airline has a separate department for MICE Tourism (Meetings, Incentives, Conventions, and Exhibitions) that integrates with local partners to arrange a myriad of events for business purposes.

SriLankan Cares

The charitable arm of the airline, SriLankan Cares actively participates in fundraising and charity activities, with its main focus being the education of children. SriLankan Cares is currently raising funds to rebuild a school that was destroyed by the Tsunami, the second school to be adopted by the airline following a successful precedent programme that was carried out recently to modernize and support a school in an area ravaged by floodwaters.

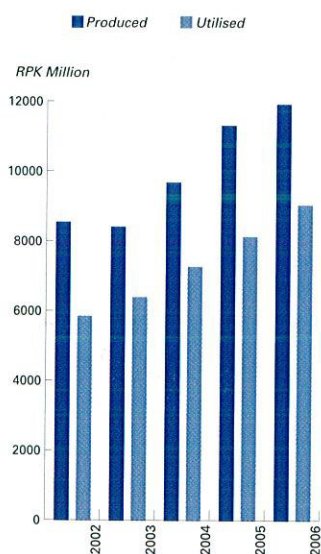
Financial Highlights

		Group			Company		
		2005/06	2004/05	% Change	2005/06	2004/05	% Change
Financial							
Operating Revenue	Rs. Million	62,489.19	54,720.54	+14.20	61,160.14	53,808.85	+13.66
Operating Expenditure	Rs. Million	60,580.76	54,201.94	+11.77	60,398.89	54,617.41	+10.59
Profit from Operating Activities	Rs. Million	2,420.33	1,742.08	+38.93	1,116.59	324.20	+244.41
Net Profit for the Year	Rs. Million	2,041.18	1,376.07	+48.33	797.93	7.66	+10,316.84
Total Assets	Rs. Million	37,727.89	34,746.88	+8.58	34,023.31	32,835.73	+3.62
Shareholders' Funds	Rs. Million	13,606.27	11,565.09	+17.65	7,080.53	6,282.60	+12.70

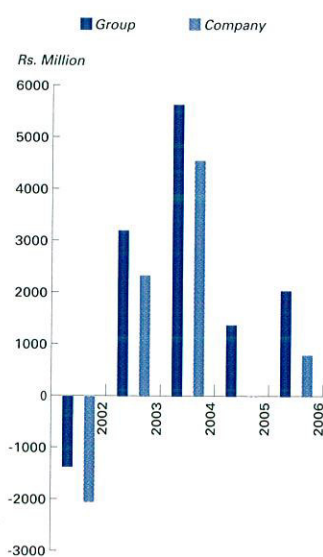
Staff Productivity

Average Strength	Nos.	5,955	5,739	+3.76	5,395	5,163	+4.49
Revenue per Employee	Rs. Million	10.49	9.53	+10.05	11.34	10.42	+8.77
Value Added per Employee	Rs. Million	2.12	2.00	+5.84	2.03	1.88	+7.86

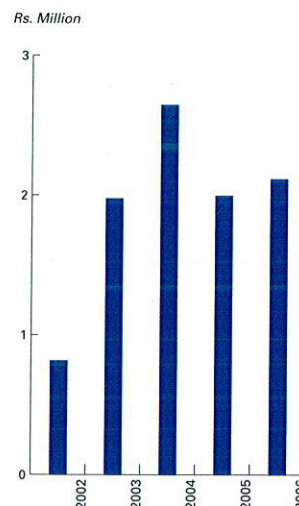
Passenger Capacity



Net Profit after Tax



Value Added per Employee



Financial Highlights

2006

2005

2004

2003

2002

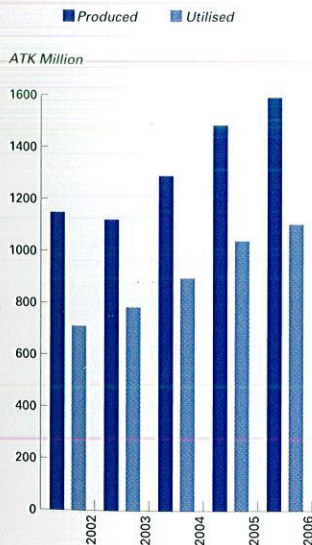
Traffic

		Company		
		2005/06	2004/05	% Change
Passenger capacity	ASK Millions	11,934.86	11,326.54	+ 5.37
Overall capacity	ATK Millions	1,590.55	1,484.02	+ 7.18
Passengers carried	RPK Millions	9,050.44	8,142.54	+ 11.15
Overall load carried	RTK Millions	1,102.77	1,039.34	+ 6.10
Passenger load factor	%	75.83	71.89	+ 3.94
Overall load factor	%	69.33	70.04	- 0.70
Breakeven load factor	%	71.65	74.94	+ 3.30

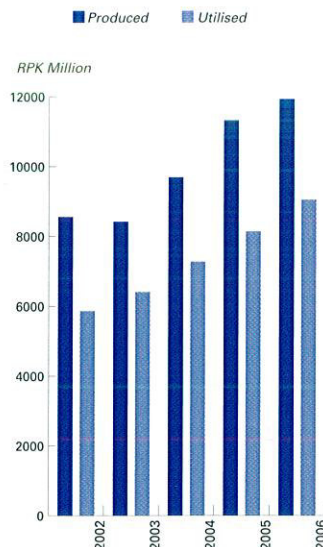
Aircraft Fleet as at 31st March 2006

		On Operating Lease	On Finance Lease
A320 - 200	Nos.	5	-
A330 - 200	Nos.	4	-
A340	Nos.	2	3
Aircraft in service at year end	Nos.	11	3

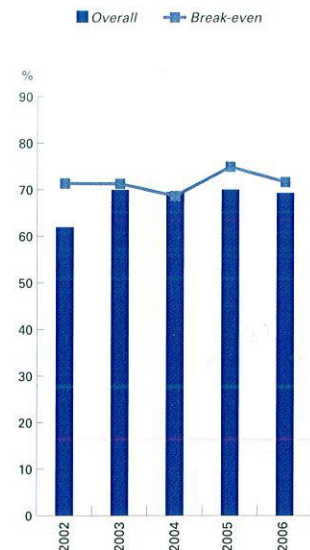
Overall Capacity



Passenger Capacity



Load Factor



Board of Directors

From Left to Right

Mildred Peries - Company Secretary

Nigel J Hopkins - Director

R A Chandiram - Director

S Ukwatte - Director

A N Wickremasinghe - Director

Peter Hill - Chief Executive Officer

Gary Chapman - Director

Tim Clark - Managing Director (*Seated*)

D H S Jayawardena - Chairman (*Seated*)



Board of Directors

D H S Jayawardena

Chairman

Chairman and Managing Director Stassens, Distilleries Company of Sri Lanka, Lanka Milk Foods (CWE) Ltd., and Chairman Aitken Spence & Co Ltd., Sri Lanka Insurance Corporation Ltd., Lanka Bell (Pvt) Ltd. and Chairman/Managing Director of several other Public and Private companies.

S Ukwatte

Director

Chairman and Managing Director of Mount Lavinia Hotel Ltd. and a Hotelier by profession

R A Chandiram

Director

Director, Odel (Pvt) Ltd. and Odel Apparels (Pvt) Ltd.

A N Wickremasinghe

Director

General Manager James Finlay Plantation Holdings Ltd.

Tim Clark

Managing Director

President/Emirates Airlines

Gary Chapman

Director

President, Dnata and Associated Companies/Emirates Airlines

Nigel J Hopkins

Director

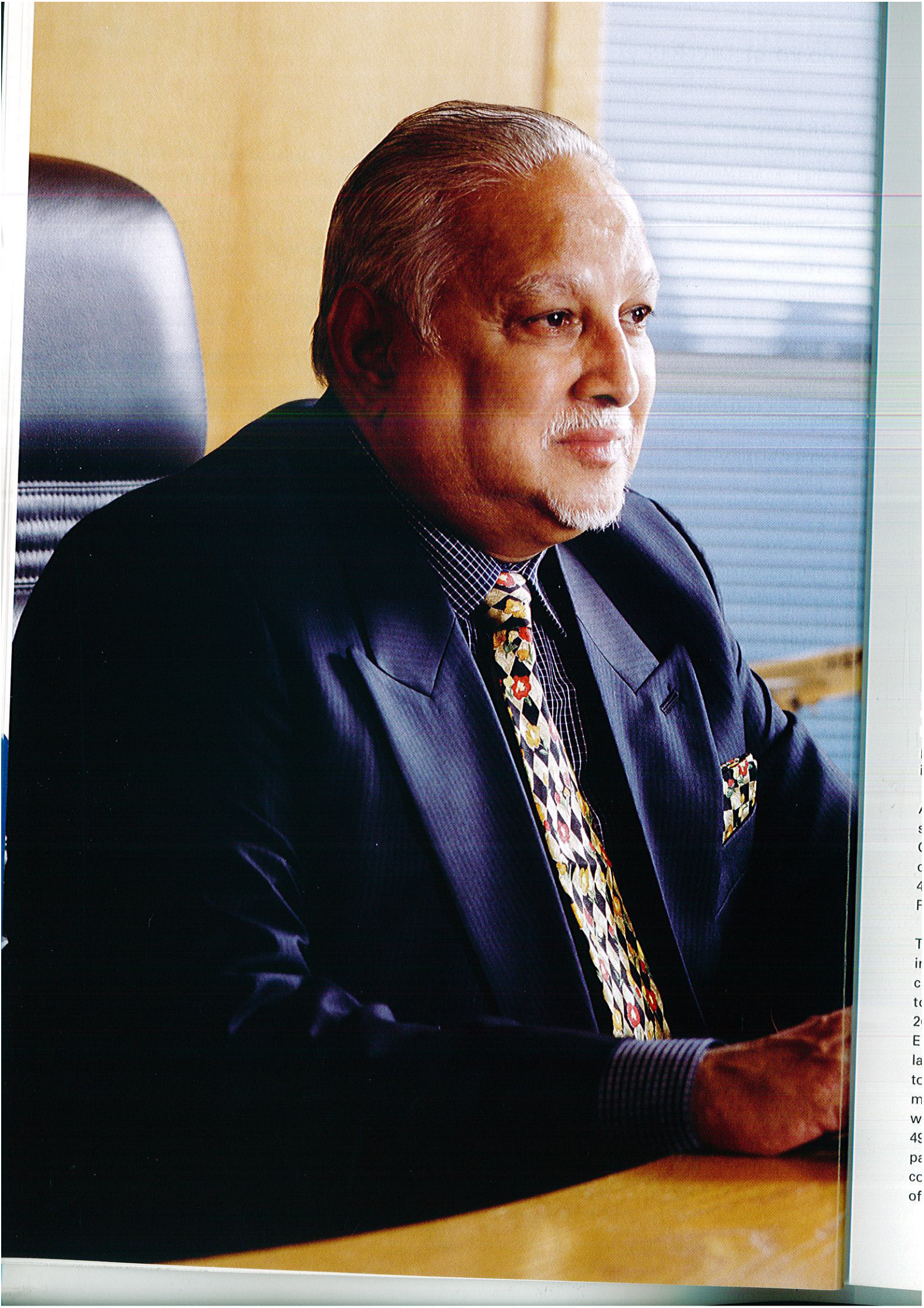
Executive VP Service Department/Emirates Airlines

Peter Hill

Chief Executive Officer

Mildred Peries

Company Secretary



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Chairman's Statement

I am pleased to present the Annual Report of the SriLankan Airlines Group.

Financial year 2005/06 was yet another challenging year for the Group. The airline industry is continuously subject to rapidly changing global economic conditions. While we are still trying to recover from the devastating effects of the Tsunami, we are facing new challenges like the drastic rise of jet fuel prices and deteriorating security situation in the country which affects our business significantly. Global oil prices for jet fuel climbed steeply to nearly USD 85 per barrel by the end of winter 2005.

According to the International Air Transportation Association (IATA), Airlines lost USD 6 billion in 2005 globally. However, IATA's latest forecast of the industry performance indicates, losses reduced significantly to USD 2.2 billion for 2006 and increased profits of USD 7.2 billion in 2007, mainly due to the stronger economic growth prospects in Europe and Asia. Stronger economic growth in Europe and Asia will also keep the oil prices from falling significantly. The forecast average price of crude oil in 2006 is at USD 57 per barrel with a refinery margin of USD 15 per barrel, which will push the price of Jet Fuel to USD 72 in 2006.

Against this background, our shareholders will appreciate that, the Group posted a Net Profit after Taxation of Rs 2,041.18 million for the year, an increase of 48.33% from the previous financial year. (2004/05: Net Profit after Taxation of Rs 1,376.07 million).

The Airline continued with its plans for expansion in spite of these challenges. Operations to Beijing commenced in July 2005 and plans are in place to commence the operations to Goa in Winter 2006. New code share agreements with our partner Emirates continued to expand our network and the latest additions to our network include daily flights to New York, Sydney, Melbourne, Vienna among many others. Frequencies to existing destinations were increased and currently we are operating into 49 destinations worldwide. Airline's drive to offer paperless "E-Ticketing" to its customers world wide continued during the year and currently over 80% of our online stations facilitate the checking in of

E-ticketing customers. Business generated through the Internet Booking Engine (IBE) that was launched in 2005 continues to attract more customers.

SriLankan Catering (Private) Ltd. also continues to expand, and will triple its capacity when its new flight kitchen is commissioned in June 2006.

Challenges faced during 2005/06 will continue in the year ahead. Prices of oil will continue to rise globally and emergence of low cost carriers will put pressure on the selling prices of the company. We may not see a significant improvement in the tourist arrivals to Sri Lanka, until a solution is reached to establish peace in the country by the Government of Sri Lanka.

However, strong economic growth in China and India and the increasing trend towards liberalisation and deregulation over the past decade, Open Skies Policies of the regional giants and opening up to more bilateral agreements in the region will create tremendous growth opportunities to the Airline.

I am confident that the management and staff of SriLankan Airlines Group will continue their efforts in the same manner to successfully make use of the opportunities available in the region to improve the profitability in 2006/07.

I would like to welcome our new Board Director Mr. Wickremasinghe and to express my sincere gratitude to our former Chairmen, Messrs. J M S Britto and K Balapatabendi, Directors Messrs: A Hewage and D E Mannion for their valuable time and untiring efforts rendered to us during their tenure of office.

My sincere appreciation goes to Board of Directors, Management team and to every member of the staff of SriLankan Airlines Group for extending their tireless and continued support during the most difficult and challenging times of the past year.



D H S Jayawardena
Chairman
15 May 2006



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Managing Director's Statement

The financial year 2005/06 was one of the most challenging years in the 27-year history of the Airline. The sky rocketing price of fuel is the single biggest challenge faced by the entire Airline industry today.

According to IATA, every US 1 cent increase in the price of a barrel of fuel adds USD 1 million to the cost of the industry fuel bill. This escalation shows the significant impact fuel has on carriers. Airlines globally are adopting various productivity increases and cost cutting initiatives to stay ahead of the increasing fuel prices.

In moving forward, SriLankan Airlines also changed its business model like its global competitors to stay ahead of the competition and to increase profitability. Planned and vigilant expansion, stringent cost controls and use of technology to be more cost effective and productive are the key elements to our success. Our results clearly demonstrate how successful we have been in meeting our goals.

The Airline made a stand alone profit of Rs 797.93 million for the financial year 2005/06 up from Rs 7.66 million in the previous year. The SriLankan group reported a post tax profit of Rs 2,041.18 million in 2005/06 as against the Rs 1,376.07 million post tax profits in 2004/05.

Operating yield increased to Rs 52.22 per TKM as against Rs 48.07 in the previous year. Unit cost excluding fuel reduced to Rs 25.32 per TKM in 2005/06 as against Rs 26.95 per TKM in 2004/05.

Operating expenditure of the Airline increased to Rs 60,398.89 million in 2005/06 as against the Rs 54,617.41 million in the previous year, representing an increase of 10.59% on a year to year basis. Our fuel bill accounted for 31.85% (Rs 19,236.28 million) of the operating expenditure in 2005/06 as against 25.20% (Rs 13,767.50 million)

in the previous financial year, representing an increase of almost 40%.

On the revenue front, operating revenue of the Airline increased by 13.66% to Rs 61,160.14 during 2005/06, from Rs 53,808.85 in the previous year.

Achieving these results after the devastating effects of Tsunami, deteriorating security situation in the country and sky rocketing global fuel prices, is a significant achievement, clearly signifying the commitment and the capabilities of our staff.

The Airline will continue with its plans for expansion in spite of these challenges, focusing on the opportunities arising from the strategic location of Sri Lanka as a gateway to India.

Our network continues to grow with Beijing added as a new destination and frequencies increased to the Middle East and South East Asia. The introduction of E-ticketing during the year is bringing much needed savings to our distribution costs and we plan to provide paperless travel on all our services by the year 2007.

The forthcoming financial year promises to be equally demanding as 2005/06 and I am confident that with continued efforts and commitment of our management and staff we will be able to overcome all our challenges successfully.

My sincere thanks to my colleagues, past and present on the Board for their co-operation, members of the management team and all staff members for their tireless efforts and commitment during a difficult year.



T C Clark
Managing Director
15 May 2006

'We at SriLankan believe in staying abreast of industry related technological advancements and the introduction of E-ticketing services during the year was a dramatic step forward.'



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Chief Executive Officer's Review

This was indeed a challenging year for SriLankan Airlines, as we initiated new strategies and utilized all available opportunities to hasten the country's recovery from the Tsunami, while tightening our belts to cope with the volatility of fuel prices. We also successfully faced the increased competition from low cost carriers and Government assisted airlines from the Middle East.

I am pleased to say that our staff once again proved their mettle, and carried the airline through another difficult year. The focus on better control of costs did not in any way compromise our commitment to providing the finest service. SriLankan added an extensive collection

of global, regional and local awards by winning the following:

- Travel Trade Gazette Award for Best Airline in South Asia
- Silver in Corporate Social Responsibility at Community Leadership Awards
- Galileo Indian Express Award for Best Eastbound International Airline in India
- One of three finalists for OAG Award for Best Marketing Campaign
- Silver Award at Asia Travel & Tourism Creative Awards
- Eleven medals for SriLankan Catering at Culinary Art
- Three Freddie Awards for Skywards including Programme of the Year

Financial Performance

In the backdrop of many challenges, the SriLankan Airlines Group achieved a Net Profit After Taxation of Rs 2,041.18 million, an increase in profitability of 48.33% from the previous financial year. The Group's Operating Profit before Finance Cost &

Taxation was Rs 2,420.33 million an increase of 38.93% as against the previous year.

The Airline reported an Operating Profit before Finance Cost & Taxation of Rs 1,116.59 million, again a 244.41% above the previous financial year and ended up with a Net Profit after Taxation of Rs 797.93 million, which is Rs. 790.27 million above the previous financial year.

The Group's Operating Revenue reached Rs 62,489.19 million, a growth of 14.20% from the previous year and the Airline's Operating Revenue reached Rs 61,160.14 million, a growth of 13.66% from the previous financial year.

The Group's Operating Expenditure increased by 11.77%, to Rs 60,580.76 million, as against the Rs 54,201.94 million in the previous financial year. The Airline's Operating Expenditure rose by 10.59% in the year under review, to Rs 60,398.89 million.

Commercial

Our core commercial activities made significant progress against the plans, continuing our focus on making Colombo a hub for travel to India, with tourism to Sri Lanka still recovering from the Tsunami. Passenger Revenue increased by 16.26% to Rs. 49,412.93 million, and constituted 79% of the Group's Revenue. Passenger carriage grew 24.38% to 3.01 million as against the previous year's 2.42 million.

We launched services to Beijing, an important market for the future, and increased frequencies to many existing destinations in South East Asia, Middle East and India. Capacity to the Middle East was expanded through the increased use of wide-bodied A330 aircraft.

"To accomplish great things, we must not only act, but also dream, not only plan, but also believe." Our strength to move forward amidst all complexities has proven beyond doubt our capabilities which are clearly reflected in our financials.

Chief Executive Officer's Review

Our Internet Booking Engine is now a regular source of direct sales, and an Agency Booking Engine is being developed in-house, both of which will reduce distribution costs. Plans are underway to make all of SriLankan's board-points E-ticketing enabled now that all on-line stations are equipped for E-ticketing and the number of passengers travelling without paper tickets is increasing.

SriLankan Holidays, Air Taxi, MICE, & Skywards

SriLankan Holidays was repositioned to further develop opportunities, and launched a series of initiatives to promote inbound and outbound tourism. The "Mega 999" series of packages provided a unique branding, and we introduced special interest packages and event related packages. During the next year, an all new holiday programme will be launched from India into Sri Lanka and beyond.

Air Taxi expanded its number of destinations to 16 by launching services to Nuwara Eliya, Dickwella, Sigiriya, the Mahaweli River in Kandy and Kondavattavan Tank in Ampara. Services to Castlereigh Reservoir, Arugam Bay and Puttalam are planned. A daily scheduled flight was launched to the Southern Coast, to provide rapid connections for tourists from Europe. "Scenic Flights" on weekends successfully targeted family groups. The planned launch of E-ticketing for Air Taxi will fully integrate with our international operations.

Active promotion of MICE Tourism (Meetings, Incentives, Conventions, & Exhibitions) continued. SriLankan was the Official Airline for 28 international conferences during the year, and we held several promotions overseas together with the Sri Lanka Convention Bureau.

Skywards, our frequent flyer programme with Emirates, is close upon 2 million members

worldwide. With over 50,000 members, Sri Lanka is one of its top ten markets.

Corporate Communications

Corporate Communications closely supported both our commercial strategies and the corporate plan for the country by the Government of Sri Lanka, especially in reversing negative publicity of the Tsunami. Strategic activities enhanced the image of the airline and the country, and focused on positioning Colombo as the gateway to India. SriLankan played a prominent role and invested USD 4 million in the country's biggest promotional campaign "Rediscover Sri Lanka" in partnership with Sri Lanka Tourism and the tourism industry. The airline obtained well negotiated rates for publicity, and leveraged upon the visibility of our charity arm SriLankan Cares.

We fully utilized our network of overseas PR agencies, and also arranged a steady stream of visits by journalists from the world's best known media. Our corporate events were increased in order to promote niche market tourism, and we entered into partnership with HSBC for our fourth golfing event, associating SriLankan with a world renowned brand.

We will continue to focus our publicity efforts on India, especially by promoting Colombo as a 'shopover' destination. We have also joined hands with the Ministries of Foreign Affairs and Tourism for major promotional events in the UK, Japan and India.

Service Delivery

The new pier at the Bandaranaike International Airport (BIA) enabled us to provide a better service, and new counters were introduced for Night Stop, Transfer Desk and Baggage Services. Our new Business Class Lounge 'Serendib' drew much praise from passengers. We will shortly introduce a "Meet and Greet" service, an Internet Check-In

Chief Executive Officer's Review

Facility, an additional 14 check-in counters and another baggage belt.

Assisted by the British and Canadian High Commissions, we introduced Airport Service Coordinators, specialized staff to detect passengers with fraudulent documents, thereby reducing the likelihood of incurring fines for carrying such passengers. Management of baggage was improved with a state-of-the-art version of the Baggage Reconciliation System. The Ramp, Plant & Equipment, Utility Services and Aircraft Interior Services departments carried out many projects towards developing new equipment, improving efficiencies and commenced revenue generating services for other airlines.

We launched the Airport Service College for school leavers who wish to pursue a career in Airport Services, and many students have subsequently found employment with us.

We carried out intensive research on our levels of inflight service to further enhance the warm and friendly on-board experience of our passengers, and our intention is to regain the title of "World's Friendliest Cabin Crew". We enhanced levels of comfort, and made many improvements to menus, entertainment and Duty Free items available on board. The Inflight Department will be re-organised to make better use of available resources and improve the training and performance feedback to Cabin Crew. A new wide-ranging Duty Free catalogue and website will be launched, together with a Airport Shop at BIA.

SriLankan Cargo

It has been an excellent year for SriLankan Cargo, which recorded a Revenue of Rs. 8,152.46 million, a growth of 9.64% over the previous year. This comprised 13% of the Group's Revenue and was significantly higher than the targeted Revenue.

Total Cargo Carriage was 82,142 tonnes, an increase of 22.64% over the previous year's 66,977 tonnes.

We capitalized on the growth of India's economy, as envisaged by our 'Hub in the Ocean' concept, especially through freighter operations to the industrial cities of Bangalore and Coimbatore, the latter being a new service that was launched.

SriLankan Cargo supported Sri Lanka's export industries following the Tsunami by maintaining flights to Male even at a loss to the airline, subsidized the carriage of perishables to the Gulf, and filled the gap created by the withdrawal of scheduled services provided by other airlines.

Completion of the Cargo Centre's new building was somewhat delayed, and is expected to take place very soon. This would double our capacity, and we would be well positioned to capitalize on India's ever-increasing role as a supplier to the world.

Engineering & Flight Operations

With our superior engineering personnel and facilities, we began aggressively pursuing lucrative opportunities of providing Third Party Maintenance Services to other airlines in Asia, the Middle East and Europe. Towards this end an application has been made for European Aviation Safety Agency (EASA 145) certification. We have already been awarded a contract for a major maintenance check on an Emirates A330, and we are seeking additional work from regional airlines. Several targeted investments were made to increase our facilities and the Quality Assurance Department was strengthened.

SriLankan Engineering carried out the first major Maintenance Checks (4C5Y) on two of our Airbus A340s, each in a record 18 days well below the industry standard of 24 days, providing combined savings of USD 300,000. Approval was also obtained to conduct segmented A-Checks, resulting

in significant cost savings. Air Taxi's Turbo Otter aircraft were fitted with long range tanks and avionics for optimum operations, and five more water sites around the country were equipped with supply and docking facilities.

The Cadet Pilot Training Programme was strengthened, and there are presently approximately 45 Junior First Officers in the cadre. The Flight Operations Department was provided a new building in Katunayake, mainly for the training of Technical Crew. Greater co-operation between the Flight Operations and Service Delivery divisions resulted in the combining of the Load Control and Flight Control departments, as well as Technical and Cabin Crew Rostering, to provide significant operational and cost benefits.

Operational efficiencies were developed to provide payload benefits across our fleet, resulting in the ability to uplift more cargo, particularly on the lucrative European sectors. We are making constant attempts to reduce overflying charges from several countries, and considerable savings have been achieved.

SriLankan Catering

SriLankan Catering once more achieved a record setting performance, and is on the threshold of capitalizing on a range of opportunities with the addition of greatly expanded production capacity. More than 4 million meals were produced during the year, at a record average of 11,020 per day, while consistently maintaining standards in quality and service. This compares with 10,500 meals per day during the previous year. An all-time record was set of 14,544 meals for a single day.

This increase in production was achieved by stepping up the level of efficiency, with no increase in staff strength, at a time when SriLankan Catering was in a transitional situation, with the constant anticipation of moving into the new Flight Kitchen.

The growth in business opportunities was the result of increased flights through BIA by SriLankan and other airlines. With its state-of-the-art Flight Kitchen to be commissioned very shortly, with an initial designed production capacity of 13,500 meals per day, SriLankan Catering looks forward to dramatic growth in the next several years.

SriLankan Catering celebrated its Silver Jubilee of operations and crowned a year of success by winning 11 medals at Culinary Art, the country's main culinary competition, the highest number of medals won by the company at this event.

Human Resources

The company focused on strengthening its management at mid and senior levels through a range of Leadership Training Programmes, equipping them with the skills to carry the airline into the future. These programmes will be further expanded in the next financial year. One more group of Management Trainees was recruited, with a comprehensive programme to turn them into our future leaders. Yet another group is to be recruited soon.

SriLankan became the first organization in Sri Lanka to adopt a special policy on harassment. It features a comprehensive investigation and disciplinary process under the control of an external Ombudsman. The company also launched its Culture Change Project, to inculcate a culture of professionalism and efficiency throughout the company. An employee counselling service was introduced with external counselors, further extending the wide range of medical and welfare services to our staff.

Our Human Resources Development Centre obtained accreditation from several prestigious global educational institutions including City & Guilds and Edexcel. We will soon enter a lucrative new business area with the launch of

Chief Executive Officer's Review

the International Aviation Academy, which will cater to the manpower requirements of airlines, airports, travel agents and other aviation industry organizations throughout the region and beyond.

Finance

The Finance Division continued its efforts to streamline finance processes and enhance financial controllership and compliance. The Revenue Accounting System was enhanced, facilitating more automated reconciliation of transactions. Automation of the annual budgeting process and management accounting reporting systems were completed.

Our existing Fuel Risk Management Programme minimised the impact of volatile aviation fuel prices, resulting in a net saving of USD 11.49 million.

The Treasury Division finalized a USD 22.5 million syndicate loan to finance the new Flight Kitchen of SriLankan Catering with attractive terms being obtained.

The Insurance Department achieved premium savings of approximately USD 1.2 million on aviation insurances, greatly influenced by the high standards of the Engineering Division. SriLankan became an Associate Member of the Gulf Co-operation Council Aviation Joint Insurance Programme, through our partner Emirates, which would bring premium savings of approximately USD 1.6 million.

Information Technology

Our IT Systems continued their important role in maintaining our competitiveness in the industry, consolidating on investments already made while taking forward key business drivers. The implementation of a new generation maintenance, repair and overhaul system is now underway. A Business Intelligence Tool for Finance and various other Databases which will assist rapid decision-

making, are now being set up. A Document Management System for Cargo and Human Resources is ready for implementation.

Many systems were upgraded or are undergoing upgrading, such as the high-end server in the Data Centre which hosts key Finance Applications. Our entire overseas network moved to a SITA system which will enable savings in telecommunication costs. Enhancements planned for the next year include upgrading of the Revenue Optimisation System PROS/PROMIS and implementation of Point of Sale product (ePOS). Studies were initiated towards centralising system-wide passenger handling needs, which would bring a considerable reduction in unit cost, and on a possible Call Centre.

Procurement & Logistics

Increased emphasis on creating a cost-conscious culture at all levels of the Group, together with centralized procurement activities, brought important cost savings.

Projects are currently underway to obtain ISO 9000 certification to prepare this division to support the Third Party Maintenance work of the Engineering Division. Commercial Procurement finalised a global freight forwarding contract to streamline operations and obtain greater savings. We have commenced implementation of an integrated ERP solution covering the Engineering, Maintenance and Procurement functions.

Outlook for the near future

The year ahead is expected to be one of consolidation in markets where we are already active, while at the same time exploring new opportunities in India, Australia, East Africa, and South Africa.

As always, external factors will have a major impact, mainly the price of aviation fuel and the

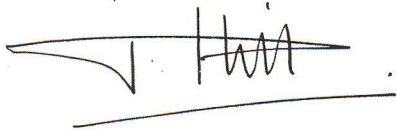
Chief Executive Officer's Review

volatile political situation in Sri Lanka. We are already exploring methods of more scientifically approaching fuel usage in order to maximize cost savings.

The continued development of BIA with its positioning as the most modern airport in South Asia, is an asset that SriLankan will build on. The company will also focus on the lucrative E-solutions area, with emphasis on E-ticketing, Internet Bookings and Automated Agency Bookings.

Appreciation

I would like to express my gratitude to the Board of Directors, our business partners around the world, the Government of Sri Lanka, Sri Lanka's travel and tourism industry, our strategic partner Emirates, our management team and most importantly, our family of employees whose loyal support, the Group can always count on.

A handwritten signature in black ink, appearing to read 'Peter Hill', is written over a horizontal line. The signature is stylized and cursive.

Peter Hill
Chief Executive Officer
15 May 2006

Corporate Social Responsibility

We at SriLankan are very mindful of the business climate in which we operate and our responsibility towards all of our stakeholders who expect ever increasing standards of accountability and transparency. We believe that our brand reputation depends not just on quality and price but on how we treat our workforce, customers, suppliers, communities in which we operate and on our commitment to preserving our environment. We measure the performance of our Company not just by our profitability but also by the impact our operations has on the world.

Caring for our Employees -Our biggest asset...

At SriLankan, we continue our efforts towards developing our workforce and building a common culture among all of them that enable us to innovate and adapt to new challenges, to motivate high performers and maintain high ethical standards.

Upgrading skills...

'People Leading', a workshop for the Management Team, was conducted by a renowned leadership trainer throughout the year to launch a People Leading Management Culture in the Company. The programme structure, content and learning methods are specifically designed to help each participating leader to clearly understand people management, identify leadership strengths and weaknesses and thus evolve a customized development plan and support network to increase on-the-job effectiveness.



SL Engineering carries out first 4C5Y check on Airbus A340 in record time

Towards new horizons of excellence...

Comprehensive Training is provided to all employees through the Human Resource Development Centre and Technical Training College. Training includes an extensive range of programmes ranging from management skills such as People Management, Team Building, 5S Training, Motivation Through Character Building, and Executive Development to soft skills such as MS Office training, Personality Development, Presentation Skills, Language Skills in several languages, Telephone Etiquette, and Business and Social Etiquette and aviation related technical programmes such as Fare and Ticketing, Reservation, Baggage Services, Cargo, Dangerous Goods Regulations, and Load Control.

C-Checks, which involve important maintenance checks on aircraft which were previously outsourced, are now carried out by Aircraft Maintenance Department after training our own staff in this area.



Participants at the Frontline Management Programme conducted jointly with the ICBT campus.

Corporate Social Responsibility

Overseas training

34 members of the staff were provided an excellent opportunity to gain more knowledge of the systems and thus, brighten career prospects when they were seconded for postings with DNATA and Emirates Sky Cargo.

Training and refresher courses are also among the priorities. In December last year, employees in the Engineering Division followed Stores & Material Management Training conducted by the EU South Asia Civil Aviation Corporation Project.

Recognition by a global institute...

SriLankan Airlines HRDC has the distinction of being the first SriLankan training institute to be officially recognized by City and Guilds, itself a prestigious global institute. On April 20th 2005, twenty-five SriLankan staff were awarded Diplomas and Certificates.

The employee view point...

An Employee Opinion Survey conducted each year, continues to elicit growing response. The results of the Survey for 2005 were presented to the Management Team and staff in two sessions held at Katunayake and Colombo. Further presentations were also made at overseas stations.

The award winners...

'Prasansa' is awarded to encourage SriLankan employees to strive harder and make outstanding

or extraordinary contributions towards SriLankan growth. SriLankan's 'Achiever of the Year' is one of the most coveted awards that are on offer each year. The 'Achiever of the Year' award for 2005 was won by Mr. Krishan Perera, Station Manager, Heathrow for negotiating and obtaining the support of KLM and London Gatwick for arrival and departure of three SriLankan Airlines flights when British Airways had resorted to trade union action.

Safety first...

SriLankan Airlines adopts a spectrum of safety measures and this is communicated to all members of the Staff through continuous awareness and safety orientation programmes in both English and Sinhala. In fact SriLankan is guided by high ground safety standards that comply fully with set standards and rules in the Airport Handling Manual published by IATA.

Adding to employee security...

SriLankan Airlines now has a comprehensive policy against harassment at the work place, headed by two external Ombudsmen to investigate complaints and recommend necessary disciplinary action.

Encouraging the children of our staff...

The Staff Welfare Society not only awarded a child of a staff member a scholarship for an outstanding performance at Year Five Examination, but also presented a personal computer each to fourteen previous winners in commemoration of the 10th Anniversary of the Society. The Airline's Welfare



Mr. J M S Britto presents the Achiever's Award to Krishan Perera, the Achiever of the Year 2005.

Corporate Social Responsibility

Society also awards scholarships to children who perform best at the GCE Ordinary Level examination.

Sports...

The 10th of September 2005 provided the highlight of SriLankan Airline's sporting calendar, with the Annual Departmental Athletics Championship which was held at Sugathadasa Stadium in Colombo. Security & Investigations emerged the overall champions. Throughout the year, sports for the seasons saw many SriLankan sportspersons perform outstandingly.

Helping care for the only planet we have...

Reducing emission through fuel efficiency

Aviation is one of the industries that are now facing up to the challenge of reducing the emission of gases. We have implemented procedures to improve fuel productivity through planned economic flights, minimizing the carriage of unnecessary fuel, thus reducing 'burn off', close monitoring of engine and airframe performance, Re-Dispatch Procedures, 'Fuel Tankering' and the reduced use of Auxiliary Power Units (APUs) on the ground. Monitoring of the 'Cost Index' to strike a balance between cost of time and fuel also enhances fuel productivity.

Waste not, want not...

All waste paper is sent for re-cycling to a specialist Company. Packing material is re-used to the maximum, while all unusable equipment, including aircraft parts is salvaged for re-processing.

In control of power...

Energy conservation, a national concern has SriLankan's total support. In-place energy conservation systems make a tremendous benefaction to the national grid. Automatic control systems regulate lighting and air-conditioning and include power factor correction capacitor banks. Automatic capacitor banks reduce the demand from the national grid significantly and this is further enhanced by a power system comprising UPS units at all SriLankan offices.

Water – the continuing process of purification

Water, the most indispensable of Nature's gifts is given appropriate treatment in more ways than one. Sourced underground water passes through a state-of-the-art package water treatment plant to provide clean drinking water to over 3000 staff at Katunayake and thereby helping to reduce the burden on the national water supply.

Floatplanes and the environment ...

Floatplane operations are in accordance with the environmental regulations and waterdromes are regularly inspected by the Central Environmental Authority.

The machines do not damage ground fish breeding or birds' nesting places and do not discharge water contaminated by oil or any other particles, since the intake by the floats is removed at the servicing facility at the BIA and not at the sites.



SriLankan staff participating at the Annual Inter-departmental Netball Tournament.



Air Taxi landing at the Victoria Reservoir, Kandy

Keeping noise tolerable...

While noise pollution in general continues to cause concern, SriLankan Airline's entire fleet of Airbus aircraft are totally compliant with noise levels stipulated in International Civil Aviation Organization (ICAO) Chapter 3 – Annex 16.

Contribution to the community

SriLankan Cares, a trust established by SriLankan Airlines to carry out its community development projects is involved in numerous infrastructure development projects, training programmes, book donations, scholarship schemes, medical camps and numerous other activities with the objective of enhancing educational facilities for children and providing them with a healthy environment.



The opening of the new Jayanthi Maha Vidyalaya in Kalawana Meepagama.

Caring for children, because tomorrow belongs to them...

Many teacher and student training workshops in Information Technology and English Language are conducted. SriLankan has enlisted the services of an overseas trainer who helps both teachers and students gain an appreciative degree of competence in both these subjects in the rural schools we support. In addition, teachers have also been trained in the 5S System at the Human Resource Development Centre in Katunayake.

The infrastructure facilities of Meepagama Jayanthi Maha Vidyalaya in Kalawana has been continuously upgraded over the last three years bringing the facilities on par with Colombo schools. In addition, financially disadvantaged students are provided monetary assistance to help with their education. The excellent results obtained this year at the GCE Ordinary Level by students pay tribute to the time and effort put in by our staff in developing the school.

The devastating tsunami of 2004 left Kalmunai on the eastern seaboard among the worst-affected areas. Despite the daunting magnitude of reconstruction, SriLankan Airlines was among the first to sign a Memorandum of Understanding with TAFREN (Task Force for Re-building the Nation), beginning with the rebuilding of Al Bahariya Maha Vidyalaya, Kalmunaikudy, in Kalmunai. The 22 classrooms to accommodate 700 students, a



Delighted children at the SriLankan Annual Book distribution.

fully equipped laboratory, canteen, toilets and administrative area represent an investment of approximately Rs. 45 million.

SriLankan also has an annual book distribution project that covers the entire island and provides school books to approximately 5000 children.

A project for Undergraduates...

The Undergraduate Training Programme too remains an on-going process. Workshops on telephone etiquette, leadership and presentation skills, effective communication, strategic thinking, social graces and more practically 'how to face an interview' and modern computer applications are conducted at the Airline's Human Resource Development Centre and supplemented by one month's on-the-job training provided by the Airline.

Valuing our Customers

Customers. Our reason to be. Recognising this, our aim is to foster the better understanding of customers and to deliver the service we promise. We strive to provide an excellent service together with operational reliability and keeping in mind that safety and security of our customers is a priority.

Studying the opinion of our customers enables us to better understand their needs. Customer feedback from onboard surveys are used to improve current delivery and better the future product.

We continue to focus on customer service and deliver highest standards at every opportunity.

Towards our suppliers...

We believe in non discriminatory, transparent and efficient procurement systems and processes in order to build long term relationships with our vendors. Our central procurement department is trained and encouraged to innovate in finding mutually beneficial vendor practises.

We are however continually assessing our performance in the area of Corporate Social Responsibility and embrace CSR as part of our business philosophy.



Delivering a service which is world class and beyond all expectations.

Management Team



Peter Hill
Chief Executive Officer

Seconded to the Airline in 1998 as its Chief Commercial Officer, Mr. Hill was appointed to the post of CEO in 1999. Mr. Hill's career in the Industry spans over 40 years having started with British Airways, then BOAC, as a Commercial Trainee in 1961. His experience in airline related jobs includes stints with Gulf Air, DNATA and Emirates Airlines.

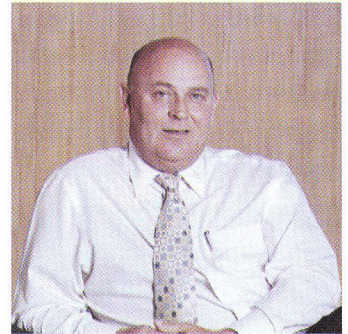


Vipula Gunatilleka
Chief Financial Officer

Mr. Vipula Gunatilleka joined SriLankan Airlines in January 2005 as the Head of Financial Management and was appointed Chief Financial Officer in January 2006. A Chartered Accountant by profession with over 20 years experience, he has held senior accounting positions in some of the blue chip companies in Sri Lanka, Singapore and Australia. Prior to taking up the appointment at SriLankan, he worked for the General Electric Group in Australia as a Controller. He is currently responsible for Finance, Treasury, Information Technology, Insurance and Procurement functions of SriLankan Airlines.

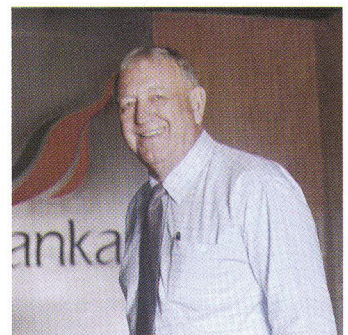
Barry Brown
Chief Commercial Officer

Mr. Brown's initial assignment with SriLankan Airlines was in the capacity of Manager, Australia & New Zealand, based in Australia. Thereafter, Mr. Brown was posted to Colombo in the capacity of Regional Manager South East Asia & Pacific Rim and was also assigned other regions under his substantive position of Regional Manager until he was promoted to the position of Head of Commercial in May 2005 and thereafter as Chief Commercial Officer in 2006. An Australian citizen, Mr. Brown is currently in the expatriate cadre of the Company.



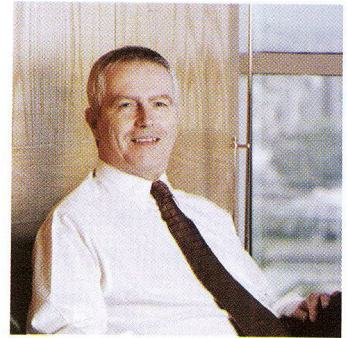
Dick Hutton
Chief Technical Officer

Joined the Airline as its Chief Technical Officer in 1999 and is in charge of the Engineering and Maintenance and Flight Operations Divisions. A Pilot by profession Capt. Hutton has served in several international airlines in the capacity of a Pilot and also as a Technical Consultant. He possesses over 40 years experience in the field of Aircraft Engineering and Operations.



Management Team

Nigel O' Shea
Head of Service Delivery



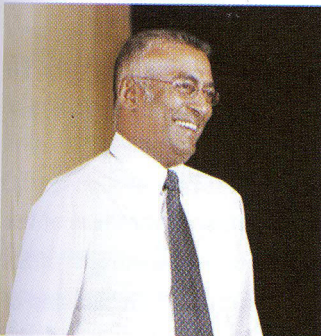
An employee of Emirates Airlines since 1995, Mr. Nigel O'Shea was seconded to SriLankan Airlines in 1998 initially as Head of Information Technology. In 2004, Mr O'Shea was appointed as the Head of Service Delivery, responsible for Airport Services and In-flight Services. He served as the Chairman of the SITA Asian Airline Group (AAG) from 2002 to 2005 and served as Director of SITA for the same period.

Sunil Dissanayake
Head of Human Resources



Mr. Sunil Dissanayake joined the Company as Head of HR in 2000 and is responsible for all Human Resources Management and Development activities including Medical Services of the Airline. Prior to joining the Airline Mr.Dissanayake was the Director HR at Carson Cumberbatch & Co Ltd. Having served several other leading corporate entities in Sri Lanka and overseas as Head of HR, Mr. Dissanayake counts more than 10 years experience in the Air Transportation Business.

Chandana De Silva
Head of Corporate Communications



Mr. Chandana De Silva initially joined the Company's sales team in 1984 and moved to Emirates Airlines country office in Sri Lanka as the Sales Manager. He re-joined SriLankan Airlines in 1998 in the capacity of Senior Manager, Sri Lanka and Maldives and was responsible for the Marketing and Sales functions of Sri Lanka and the Maldives. Mr. De Silva was appointed Head of Corporate Communications in 2002 and is currently responsible for Corporate Advertising, Promotions, Media Relations and Public Relations of the Airline. Mr. De Silva counts over 20 years experience in the Air Transportation Business.

Dilip Nijhawan
Chief Executive Officer
SriLankan Catering (Private) Limited



Mr. Nijhawan joined the Airline in December 1998 and was seconded to SriLankan Catering the wholly owned subsidiary of the Company. Mr. Nijhawan is a Commerce Graduate from Calcutta with a Post Graduate Diploma in Hotel Management from the Oberoi School of Hotel Management-Delhi. Prior to joining SriLankan Airlines Mr. Nijhawan was the General Manager of The Oberoi Hotel in Jeddah, Saudi Arabia. Mr. Nijhawan counts over 28 years experience in the hospitality trade overseas.

Corporate Governance

This statement of corporate governance describes the responsibilities and best practices exercised by the Board and the Executive management of the Company with a view to provide strategic direction, ensuring that the Company objectives are achieved, ascertaining that risks are managed appropriately and verifying that the organization resources are used responsibly.

SriLankan Airlines makes compliance with the best practices of corporate governance principles and provisions recommended by the Institute of Chartered Accountants of Sri Lanka, its utmost priority.

Board of Directors

The Board of Directors of SriLankan Airlines comprises members with vast experience and extensive knowledge in areas of business, financial and technical expertise.

The responsibility for strategic management and setting the overall direction for SriLankan Airlines resides with the Board of Directors of the Company. The Board of Directors of SriLankan Airlines meets on a regular basis to discuss the achievement of and changes in the entity's strategies, policies, priorities, and set standards for the management. The Board held five (05) meetings during the financial year ended 31st March 2006.

The function of the Board includes,

- Monitoring the Company and its subsidiary's overall performance, by reviewing Monthly Financial and Management Reports.
- Adopting of Annual Consolidated Accounts of the Company and Group before they are published.
- Approval of the recurrent and capital expenditure budgets and monitoring progress against the budgets, and allocating necessary financial and human resources in order for the Company to meet its targets and objectives.
- Monitoring the strategies and capabilities of the Company's major competitors.
- Evaluating the external environment of the Company and assessment of business and financial risks that could impact the Company's

performances and profitability.

- Setting overall Direction of the Company and ensuring the obligation to the shareholders and others stakeholders are met.
- Reviving of long-term plans based on the changes in external and internal environmental factors that have a significant impact on the Company's business.

The Board is ultimately responsible and accountable for the Company's activities, corporate strategy and financial performance.

The Board of SriLankan Airlines, comprises the Chairman, Managing Director and five other directors as of during the financial year ending 31st March 2006.

The Board of Directors has complete access to all relevant information, on a regular basis enabling them to discharge their duties effectively. Members of the Board are provided with appropriate documentation in advance of Board meetings, enabling them to make informed decisions and the minutes of the meetings of the Senior Management Committee are also circulated to the members of the Board.

The Chief Executive Officer and the Company Secretary are responsible for ensuring that all Directors are properly briefed on matters that are discussed at Board meetings.

The Board is responsible to the shareholders of the Company which consists of the Government of Sri Lanka, Emirates and the shareholder employees of the Company in terms of the corporate strategy for the efficient management of the affairs of the Company and to maximize profitability and improvement of cash flows. The Board works towards delivering best value to the Company shareholders and are committed towards providing adequate transparent information on the activities of the Company.

Management Committee

The Management Committee comprises the Chief Executive Officer, Chief Financial Officer, Chief Commercial Officer, Chief Technical Officer, Head of Corporate Communications, Head of Service Delivery,

Corporate Governance

Head of Human Resources and Company Secretary acts as the Secretary. The Chief Executive Officer is responsible for the Company's overall performance, the Heads of Divisions are responsible for the operations of respective Divisions of the Company.

The Management Committee has been set up to facilitate the two-tier governance structure. The Management Committee exercises its authority within the policy and ethical framework established by the Board and the business practices inherent to the Company, which demand the best practices in dealing with customers, employees, suppliers and the community at large. The Management Committee is headed by the Chief Executive Officer and meets weekly to discuss the important operational/day to day business issues of the Company as well as to execute directives /policies issued by the Board.

Financial Reporting

The Chief Financial Officer is responsible for all financial reporting of the Company, including monitoring all new financial accounting and reporting standards and assessing their impact on SriLankan Airlines. The Company is committed to adhering to Sri Lanka Accounting Standards in presenting the financial position of the Company and ensures adequate disclosures are made in the Annual Report and Accounts giving a true and fair view of the Company's financial and operational performances.

The Financial Report of the Company is audited by the external auditors who express an 'Independent Opinion' on the Financial Statements. The Company also obtains tax advisory and other consultancy services from independent external parties.

Internal Controls

The Board of Directors and the management are responsible for the maintenance of the Company's systems of internal control including the internal financial controls to safeguard shareholders' investment and the assets of the Company.

The Board ensures effectiveness of the controls prevailing in the company and provides reasonable

assurance on safeguarding of assets against unauthorized use or disposal and maintenance of proper and reliable records of information. It includes all controls such as financial, operational, compliance and risk management. However, any system can ensure only reasonable and not absolute assurance that errors and irregularities are prevented or detected within a reasonable time frame.

The Board and the management also take into account the significant social, environmental and ethical aspects that relate to the Company's business and work practices. The Company's Risk Management policy is covered under pages 33 to 34 and the Environment and Corporate Social Responsibilities addressed in pages 23 to 27.

The Company maintains an independent Internal Audit Department. The Internal Audit Department operates independent of the Management and reports on its key findings directly to the Board of Directors. The Internal audit plan of the company covers independent reviews on both local and global operations of the company including the review of the adequacy and effectiveness of the systems of internal control. The respective Heads of the Divisions are responsible for taking corrective action on audit findings and reporting to the Chief Executive Officer.

Human Resource Policies and Practices

The management commitment to competence is evidenced through its recruitment, hiring and performance evaluation practices.

Employee Relations

The functions of SriLankan Airlines Human Resources includes improving and enhancing the working relationship between the employees, increasing labour flexibility through the review and improvement of work place practices, complying with the collective agreements negotiated with unions and reviewing ways to better motivate the work force through wage restructuring and wage reforms.

Remuneration

The Group's remuneration policy is designed to attract, retain and motivate staff in view of optimising

Corporate Governance

individual objectives and thereby improving the Group's overall performance.

Remuneration, rewards and promotions of staff based overseas are reviewed and approved by a Remuneration Committee consisting of Chief Financial Officer, Chief Commercial Officer, Head of Human Resources, Head of Service Delivery and Head of Cargo.

Remuneration of staff based in Sri Lanka is determined in accordance with the Collective Bargaining Agreements with unions which are in line with industry norms.

The remuneration, reward and promotion scheme of the Company is structured on the annual performance appraisal linked to Key Result Areas (KRA) and Key Performance Indicators that are monitored throughout the year. These KRAs are formulated for each individual annually, based on the Company's set objectives for the year.

Position Request Committee

Staff position requirements are subject to scrutiny by the position request committee which comprises Chief Financial Officer, Head of Human Resource and Head of Service Delivery. On the recommendations of the committee, the requested position is filled by an internal promotion or an external appointment.

Regulatory Compliances

The Company is committed to comply with the domestic and international rules and regulations governing the operations of the Business. This includes abiding by the rules and regulations established by The International Air Transportation Association (IATA), Civil Aviation Authority of Sri Lanka and various other agencies which have bearing on the operations of the airline. The Company's safety and security programme is constantly reviewed and amended to meet the requirements of the said bodies.

Further, the Company has been granted Flagship status along with tax relief by Board of Investment

of Sri Lanka (BOI) and is governed by the rules and regulations of the BOI Act.

Tender Boards

The procurement process of the Company complies with relevant policies and procedures set by the Board of Directors. Tender Boards function as a supervisory body to oversee and approve the supplier selection and purchase of products and services in excess of Rs 5 million. Purchases above Rs 100 million require the approval by the Board of Directors.

Tender Board comprises the Chief Executive Officer, Chief Commercial Officer, Senior Manger – Legal Affairs, Head of Cargo, Group Treasurer and Company Secretary. The Group Internal Auditor acts as an independent observer to this Board.

Going Concern

The going concern basis has been adopted in the preparation of the Company's Financial Statements. The Directors confirm that they are satisfied that the Company has sufficient resources to continue its operations in the foreseeable future.

Transparency

The Board places great emphasis on complete disclosure of both financial and non-financial information within the bounds of commercial reality, and on the early adoption of sound reporting practices. The Chairman's, Managing Director's and Chief Executive Officer's review present a balanced assessment of the Company's performance and its future strategic direction.

The Statement of Directors' Responsibilities in relation to the transparency of Financial Statements is set out on page 44.

External Auditors

The external auditors are primarily responsible for auditing the Financial Statements of the Company for the financial year ended 31st March 2006.

Risk is a possible loss or a negative impact that can arise in the future as a result of present causes. No organisation is immune to risk although risks can be managed to minimize the adverse implications. The primary risks facing the industry include strategic, financial, operational and business risk. Risk management is a systematic proactive identification of threats to resources or in other words it is a trade-off between a potential danger and an opportunity to enhance returns. Airlines in today's environment of economic uncertainty are taking all possible measures to reduce costs and conserve cash. While this is understandable, a broader view may be necessary to reduce the risk of failure in both the short and long term. Entrepreneurship is taking risks to create wealth and SriLankan Airlines employs an array of techniques to manage risk.

Political Risk

Any progress made in the peace process creates a positive outlook on the country increasing leisure travellers to the island. Nevertheless with escalating violence and with no definite solution on the horizon, SriLankan Airlines concentrates on other means of income generation such as concentrating on the feeder hub concept to West Asian and Indian destinations.

Macro Economic Risk

World economy's contribution to the ever mounting fuel prices bundled with the decrease in inbound tourists continues to affect the bottom line. Competition from other airlines as well as the emergence of low cost carriers in the market will pose a threat and could result in an erosion of the market share. Enduring to be competitive through differentiation, creating niche markets and introducing new products are the strategic directions to be pursued. "SriLankan Holidays" the package tour arm of SriLankan was launched to bestow a total holiday package on the leisure traveller. Air Taxi for domestic travel offers the discerning traveller a whole new way of experiencing the island retreat.

Legal and Regulatory Risks

The Company is mindful that it operates in a heavily regulated environment. The international regulations particular to the aviation industry impacts aircraft operations, safety, consumer protection and competition. The implications of these regulations and the local laws of Sri Lanka and the countries into which we operate have a significant effect on costs, air transport operations and business opportunities.

The Company's objective is to be a compliant organisation which operates within the applicable legal and regulatory framework, while maximising its business opportunities. We have established procedures in liaison with international bodies to be proactive, and monitor new laws and regulations which impact our business and operations and ensure that they are clearly communicated to relevant staff, with a view to ensuring compliance and avoiding breaches and lapses which could result in litigation or other sanctions being imposed.

Human Resource Risk

At SriLankan, we believe that our main strength is our investment in human capital. Our recruitment process is based on the Assessment Center Methodology and our training and development center tools are structured on international standards. It is by adapting these world class methodologies that we mitigate the risk of employing a bad recruit. We are presently in the process of training a cross section of management to specialize in recruitment selection. We are of the view that a specialized interview panel would reduce the risk of recruiting mediocre employees. The contributions made by our employees over the years have proven that our selections have been on par with the international standards.

Internal Process Risk

Internal process risks arise from the lack of stringent internal controls which govern the smooth operation of an enterprise. We at SriLankan have a strong Internal Audit Department headed by

Risk Management

a Group Internal Auditor reporting directly to the Board of Directors. Periodic review and compliance monitoring of the Company's internal processes are carried out by Internal Audit. This review covers all material internal controls including financial, operational and compliance controls. In addition, a Risk Map is used to monitor the overall Company risk which is prioritized as high, medium and low based on the financial impact, strategic importance and internal/external audit experience.

Environment and Safety Risk

The growth of the airline industry is so rapid that the statisticians predict that, by the year 2010, there will be one crash every two weeks. Past air disaster records have shown us, that the airlines and airports which were prepared, were able to negate the effects of a crash much more quickly and effectively than others who were not. As an Airline, we have a responsibility to ensure the welfare of our passengers and our own staff. We are also responsible for safeguarding them, their belongings and the company property including our aircrafts. In view of this, an Emergency Response Plan was introduced during the year to ensure that we have a specialised team available 24 hours to counteract the adverse effects of any emergency situation.

Information Technology Risk

In most areas of business, risks are well-known, well-understood and manageable using established controls and approaches. However in technology, new risks can arise overnight; their nature unknown, their effects crippling, with the ever-changing technological environment, these risks grow exponentially. All critical systems are covered by IT Disaster Recovery Plan including redundancies. As a move towards further counteracting this challenge, the Company has initiated work on extending the IT Disaster Recovery Plan for systems which are not presently covered. This will be implemented in stages in the future. The Company has also planned to carry out an IT Security Audit through a reputed external Institution as a follow up to the IT Audit carried out two years back.

Financial Risks

Fuel price volatility, interest rate risks, exchange rate and credit risks are the main financial risks that affect the Company.

Fuel price increase as witnessed during the past two year period and the continuing increasing trend is a major risk faced by the entire airline industry. The Company has adopted a comprehensive jet fuel risk management strategy utilizing hedging instruments to minimize the effect of these fuel price escalations.

Interest rate risks arising from the volatility in interest rates are mitigated by stringent negotiation of facilities with the banks and financial institutions by having a mix of fixed and floating rate debt and by consolidating facilities through the central treasury management function.

Exchange rate risks arising from the fluctuations in the relative rates of exchange are mitigated by identifying the various time frames of receivables and payables in foreign currencies as well as in Rupees and the Company attempts to match the various outflows with inflows thereby creating a natural hedge. The net exposures between the components of the unmatched items are closely monitored by the treasury and timely action is initiated to cover the net exposure in order to minimize risk.

Credit risks arising through defaults by customers are mitigated through a stringent credit control system which includes, credit worthiness checks, obtaining of bank guarantees and the regular review of customer credit status. The credit exposure is closely monitored in order to avoid recovery action which is expensive, time consuming and does not guarantee success.

Financial Review

The Group's financial performance for the year 2005/06 was remarkable despite the set back of tsunami devastation and escalating fuel prices.

The SriLankan Group registered a Net Profit after Taxation of Rs. 2,041.18 million for the year 2005/06, reflecting an increase of 48.33 % as against the Net Profit after Taxation of Rs 1,376.07 million in 2004/05.

The Company registered a Net Profit after Taxation of Rs. 797.93 million for the year 2005/06, an increase of Rs. 790.27 million from the Net Profit after Taxation of Rs 7.66 million reported in 2004/05.

The following table depicts the year to year percentage changes in financial results and the key performance/ profitability ratios of the Group and the Company for the years 2005/06 and 2004/05.

Group

	2005/06	2004/05	% Change
Net Profit after Taxation (Rs. M.)	2,041.18	1,376.07	+ 48.33
Operating Profit before Finance Cost & Taxation (Rs. M.)	2,420.33	1,742.08	+ 38.93
Earnings Per Share (Rs.)	39.66	26.74	+ 48.32
Return on Turnover (%)	3.27	2.51	+ 0.76
Return on Total Assets (%)	5.41	3.96	+ 1.45
Return on Shareholders' Fund (%)	15.00	11.90	+ 3.1

Company

	2005/06	2004/05	% Change
Net Profit After Taxation (Rs. M.)	797.93	7.66	+ 10,316.84
Operating Profit before Finance Cost & Taxation (Rs. M.)	1,116.59	324.20	+ 244.41
Earnings Per Share (Rs.)	15.50	0.15	+ 10,233.33
Return on Turnover (%)	1.30	0.01	+ 1.29
Return on Total Assets (%)	2.35	0.02	+ 2.33
Return on Shareholders' Fund (%)	11.27	0.12	+ 11.15

Revenue

Operating revenue of the Group improved by 14.20% to reach Rs. 62,489.19 million in 2005/06, from Rs. 54,720.54 million in 2004/05.

Operating revenue of the Company improved by 13.66% to reach Rs. 61,160.14 million in 2005/06, from Rs. 53,808.85 million in 2004/05.

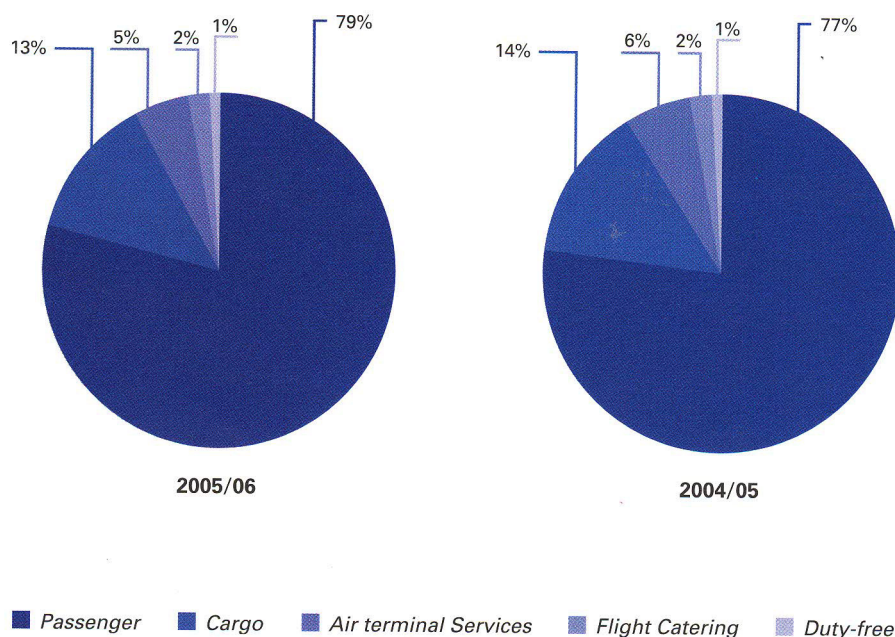
Improvement in passenger yields, increase in passenger numbers, increase in cargo volumes and increased seat factors driven by increased frequencies to existing destinations, commencement of operations to Beijing and success in recovering fuel surcharges contributed to the increased revenue at the company level.

The table on the following page depicts year to year percentage changes in Revenues of the Group and Company for the years 2005/06 and 2004/05.

Financial Review

	Group			Company		
	2005/06	2004/05	% Change	2005/06	2004/05	% Change
	Rs. M.	Rs. M.		Rs. M.	Rs. M.	
Passenger	49,413	42,502	+ 16.26	49,413	42,503	+ 16.26
Cargo	8,152	7,435	+ 9.64	8,177	7,457	+ 9.66
Air Terminal Services	3,201	3,499	- 8.52	3,218	3,511	- 8.34
Flight Catering	1,371	946	+ 44.93	-	-	-
Duty Free	352	338	+ 4.14	352	338	+ 4.03
Total Revenue	62,489	54,720	+ 14.20	61,160	53,809	+ 13.66

Composition of Revenue Group



Expenditure

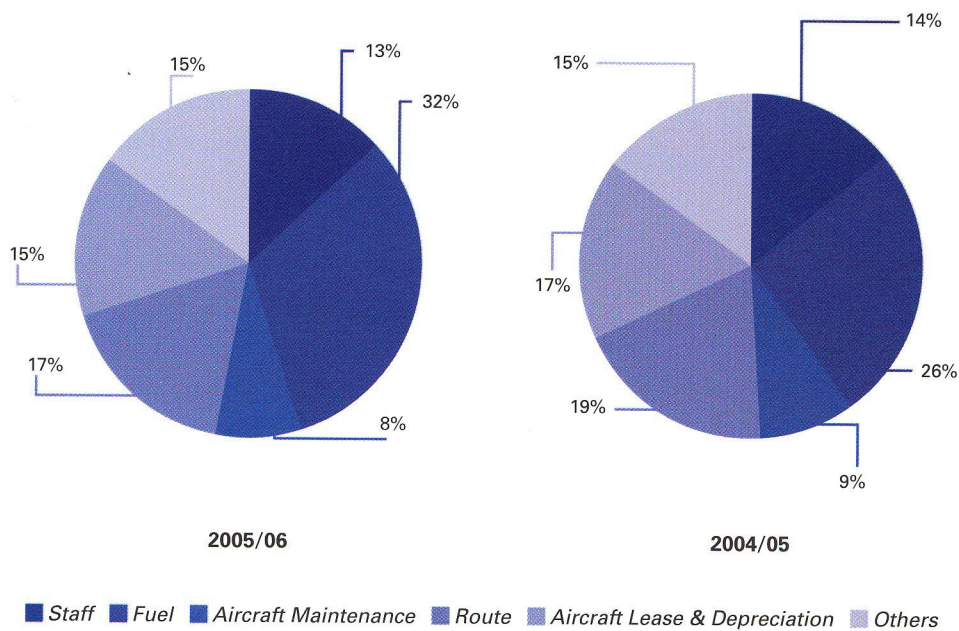
Operating expenditure of the Group rose by 11.77% against 2004/05, mainly due to escalating fuel prices. The following table depicts year to year percentage changes in Operating expenditure of the Group and Company for the years 2005/06 and 2004/05.

	Group			Company		
	2005/06	2004/05	% Change	2005/06	2004/05	% Change
	Rs. M.	Rs. M.		Rs. M.	Rs. M.	
Staff	7,920	7,824	+ 1.23	7,635	7,528	+ 1.42
Fuel	19,236	13,767	+ 39.73	19,236	13,767	+ 39.73
Aircraft Maintenance	4,944	5,108	- 3.21	4,944	5,108	- 3.21
Route Costs	10,851	10,267	+ 5.69	12,362	11,813	+ 4.65
Aircraft Lease & Depreciation	8,832	9,160	- 3.58	8,832	9,160	- 3.58
Other Expenses	8,798	8,076	+ 8.94	7,390	7,241	+ 2.06
Total Operating Expenditure	60,581	54,202	+ 11.77	60,399	54,617	+ 10.59

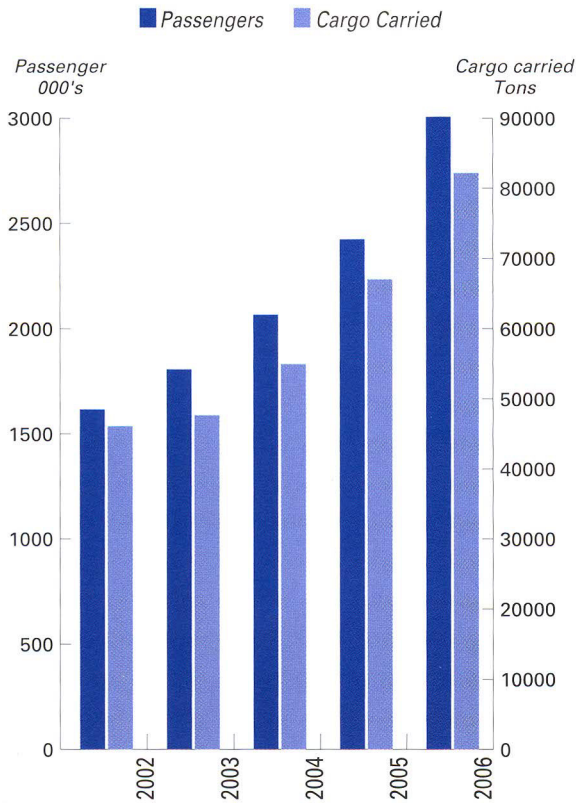
Financial Review

- Staff costs rose 1.23% due to annual pay reviews accompanied by corresponding increases in staff on costs such as, retirement gratuity, provident fund contributions and increase in staff strength in direct operational areas such as Airport Services and Inflight Services. The number of employees in service as at 31st March 2006 was 5,955 (2004/05: 5,739)
- Aviation Fuel costs increased by 39.73%, due to the increase in average fuel price from 130.43 usc/ag in 2004/05 to 174.23 usc/ag in 2005/06 contributing to a 33.58% of the fuel costs, while the increase in consumption accounted for a 4.68% increase in the fuel cost.
- Aircraft Maintenance costs decreased 3.21% due to the reduction in the number of scheduled events for engine maintenance to 12. (2004/05: 14 events)
- Route costs increased 5.69% due to increase in frequencies by 14.43%.
- Aircraft Lease & Depreciation expenditure reduced by 3.58% due to return of spare engines taken on a short term basis.
- Increase in other costs was largely due to higher spending on global distribution systems on account of higher passenger carriage in 2005/06.

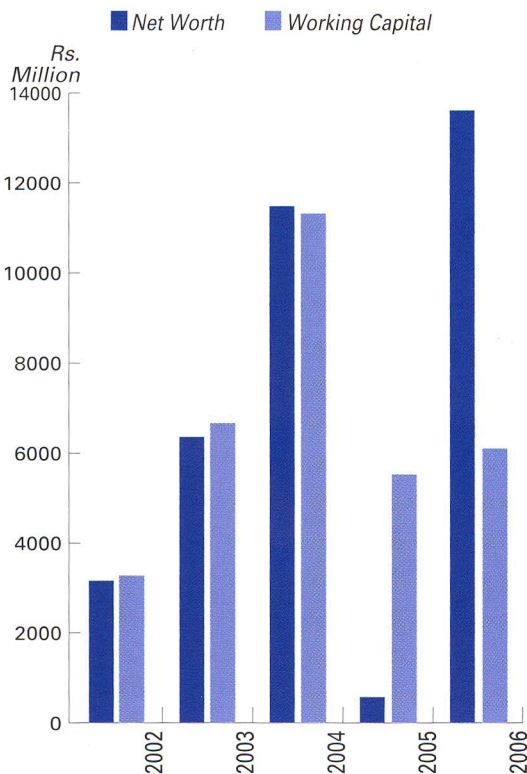
Composition of Expenditure Group



Passenger and Cargo Carried



Net Worth and Working Capital Group



Operational Performance

- Capacity production increased 7.18% to reach 1,590.55 million available tonne kilometers, reflecting a better utilization of the fleet with increased frequencies.
- Number of frequencies increased 14.43%, primarily to destinations in India, Middle East and South East Asia, and the introduction of operations to Beijing.
- Passenger carriage grew 24.38% to 3.01 million. (2004/05: 2.42 million)
- Cargo carriage grew 22.64% to 82,142 tonnes. (2004/05: 66,977 tonnes)
- Seat factor increased by 3.94 percentage points to 75.83% whilst overall load factor decreased to 69.33% from 70.04%.
- Unit yield improved 8.63% to Rs. 52.22 per tonne kilometer due to fare increases. (2004/05: Rs. 48.07).
- Unit cost increased 3.89% to Rs.37.42 per capacity tonne kilometer mainly due to escalating fuel prices. (2004/05: Rs. 36.02).
- Breakeven load factor improved from 74.94% to 71.65% as a result of the improvement in the unit yield.

Financial Position

- Total Equity of the Group increased 17.65% to Rs.13,606.27 million as a result of increase in profit. (2004/05: Rs. 11,565.09 million)
- Total Equity of the Company increased 12.70% to Rs.7,080.53 million. (2004/05: Rs.6,282.60 million)
- Working Capital of the Group increased 10.44% to Rs.4,353.77 million. (2004/05:Rs. 3,942.18 million)
- Working Capital of the Company decreased by Rs.1,017.53 million to Rs.1,095.94 million. (2004/05: Rs. 78.41 million)

Financial Calendar

31st January 2006

Limited Review of Financial Statements

31st March 2006

Financial Year-End

15th May 2006

Adoption of the Financial Reports by the Board

15th May 2006

Proposal of Final Dividends by the Board

28th June 2006

28th Annual General Meeting

Financial Reports

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Report of the Directors

The Directors of SriLankan Airlines Ltd. take pleasure in presenting the Director's Report and Consolidated Financial Statements for the year ended 31st March 2006.

Principal Activities and Business Review

The principal business activities of the Company are the operation of international, scheduled/non-scheduled air services for the carriage of passengers, freight and mail as the designated carrier of Sri Lanka. Providing air terminal services at the Bandaranaike International Airport, sale of duty-free goods on-board and operation of an Air Taxi service within Sri Lanka to carry passengers constitute other main activities of the Company.

There was no significant change in the nature of activities of the Company during the financial year.

A review of the Group's progress and performance during the year, with comments on the financial results and prospects, is contained in the Chief Executive Officer's Review.

Group Turnover

The turnover of the Group amounted to Rs. 62,489.19 million (2004/05: Rs. 54,720.54 million). A detailed analysis of Group Turnover is given in Note 3 to the Financial Statements.

Transactions between the Company and its fully owned Subsidiary, SriLankan Catering (Private) Ltd. is conducted at fair market prices.

Results

Group profit before taxation amounted to Rs. 2,137.79 million (2004/05: Rs. 1,413.97 million). After deducting Rs.96.61 million (2004/05: Rs. 37.90 million) for taxation, Group profit for the year was Rs. 2,041.18 million (2004/05: Rs. 1,376.07 million).

The consolidated income statement for the year is given on page 46.

Group Investment

Group capital expenditure during the year on property, plant and equipment amounted to Rs. 2,280.29 million (2004/05: Rs. 3,377.06 million).

Value of Property, Plant and Equipment

The Group net book value of the property, plant and equipment amounted to Rs.12,229.37 million (2004/05: Rs. 11,879.34 million).

Share Capital

The issued and paid up share capital of the Company is Rs. 5,146.35 million (2004/05: Rs. 5,146.35 million) comprising of 51,463,463 Ordinary Shares with a par value of Rs.100/-.

Reserves

Total Group Reserves as at 31st March 2006 amount to Rs. 8,459.92 million (2004/05: Rs. 6,418.74 million), which includes Rs. 8,300.65 million (2004/05: Rs. 6,259.47 million) in accumulated profits. Movements in reserves are shown in the Statement of Changes in Equity in the Financial Statements.

Report of the Directors

Corporate Donations

The Company has not made any cash donations during the year and no donations were made for political purposes.

Taxation

The Company enjoys a tax holiday up to 31st March 2013 in terms of its agreement with the Board of Investment of Sri Lanka.

The Company is liable for tax on its overseas operations in countries where there are no double taxation treaties at present.

Share Information

The authorized share capital of the Company is 150,000,000 Ordinary Shares of Rs. 100/- each. The nominal value of the authorised share capital of the Company is Rs. 15,000 million (2004/05: Rs. 15,000 million).

Share Ownership	No. of Shares	% Holding
Government of Sri Lanka	- 26,275,436	(51.05%)
Emirates	- 22,451,516	(43.63%)
Others	- 2,736,511	(5.32%)

Contingent Liabilities and Capital Commitments

Contingent Liabilities as at 31st March 2006 and Commitments made on Capital Expenditure as at that date are given in Note 19 to the Financial Statements.

Events Occurring after the Balance Sheet Date

No circumstances have arisen since the Balance Sheet date that would require adjustment, other than those disclosed in Note 20 to the Financial Statements.

Employment Policies

Employment policies of the Group respect the individual and offer equal career opportunities regardless of sex, race or religion. Occupational health and safety standards receive substantial attention. The number of persons employed by the Company and its subsidiary at the year-end was 5,955 (2004/05: 5,739).

Statutory Payments

The Directors, to the best of their knowledge and belief, are satisfied that all statutory payments in relation to employees and the government have been made up to date.

Environmental Protection

The Group's business activities can have direct and indirect effects on the environment. It is the Group's policy to keep adverse effects on the environment to a minimum and to promote co-operation and compliance with the relevant authorities and regulations.

Corporate Governance/Internal Control

Adoption of good governance practices has become an essential requirement in today's corporate world. The practices followed by the Group are explained in the Corporate Governance statement on pages 30 to 32.

Report of the Directors

The Directors acknowledge their responsibility for the Group's system of internal control. The system is designed to provide assurance, *interalia*, on the safeguarding of assets, the maintenance of proper accounting records and the reliability of financial information generated. However, any system can ensure only reasonable, and not absolute assurance that errors and irregularities are prevented or detected within a reasonable time.

The Board is satisfied with the effectiveness of the system of internal control for the period up to the date of signing of the Financial Statements.

Going Concern

As noted in the Statement of Directors' Responsibilities, the Directors have adopted the going concern basis in preparing these Financial Statements.

Directors in Office

The names of the present Directors of the Company are listed below:-

Mr. D H S Jayawardena	- Chairman
Mr. S Ukwatte	
Mr. R A Chandiram	
Mr. N A Wickremasinghe	
Mr. T C Clark	- Managing Director
Mr. G W Chapman	
Mr. N J Hopkins	
Mr. P M Hill	- Alternate to T C Clark
Mr. M Flanagan	- Alternate to G W Chapman
Mr. Ghaith Al Ghaith	- Alternate to N J Hopkins

Mr. K Balapatabendi PC, who held the position of Chairman since 21st May 2004 tendered his resignation from this position effective 03rd May 2005 and Mr. J M S Brito - Director was appointed Chairman effective 11th May 2005.

Mr. D H S Jayawardena was appointed as Chairman with effect from January 2006 when Mr. J M S Brito resigned from his position as Chairman also in January 2006.

Messrs A Hewage - Director also tendered his resignation from the Board in December 2005 and Mr. N A Wickremasinghe was appointed as Director in January 2006 to fill in this vacancy.

Mr. N J Hopkins was appointed Director following the resignation of Mr. D E Mannion - Director in May 2005. With the resignation of Mr. Mannion his alternate Mr. Ghaith Al Ghaith was re-appointed as an Alternate Director to the newly appointed Director Mr. N J Hopkins.

SriLankan Catering (Private) Ltd. is the wholly owned subsidiary of SriLankan Airlines and the current directorate is as follows:-

Mr. D H S Jayawardena	- Chairman
Mr. G W Chapman	- Director
Mr. S Ukwatte	- Director
Mr. R A Chandiram	- Director
Mr. D Nijhawan	- Alternate Director to G W Chapman

Report of the Directors

Mr. K Balapatabendi PC held the position of Chairman as at 01st April 2005 until his resignation in May 2005. Mr. Brito - Director who was then appointed to this position tendered his resignation in January 2006 and Mr. D H S Jayawardena was appointed as Chairman of SriLankan Catering (Private) Ltd. in February 2006.

Following the resignations of Mr. J M S Brito, Mr. D E Mannion and Mr. A Hewage - Directors in January, May and December 2005 respectively, Mr. S Ukwatte, Mr. G W Chapman and Mr. R A Chandiram were appointed as Directors to fill the vacancies on the Board. Pursuant to Mr. Mannion's resignation Mr. Dilip Nijhawan was re-appointed the Alternate Director for Mr. G W Chapman.

The Directors were not in receipt of any emoluments and/or any other payment that constitute a payment for participation/attendance at Board Meetings during the year ended 01st April 2005 to 31st March 2006.

Directors' Shareholdings

By virtue of office three of the Government of Sri Lanka (GOSL) Nominee Directors including the Chairman are holders of 01 Ordinary Share each in the Company.

Directors' Interests in Contracts

Directors' interests in contracts of the Company are disclosed in Note 21 to the Financial Statements and have been declared at meetings of the Directors. The Directors have no direct or indirect interest in any other contracts or proposed contracts with the Company.

Annual General Meeting

The Annual General Meeting will be held on 28th June 2006.

Auditors

In accordance with the Companies Act No. 17 of 1982, a resolution proposing the re-appointment of Messrs. Ernst & Young, Chartered Accountants, as Auditors to the Company will be submitted at the Annual General Meeting.

By Order of the Board



Mildred Peries
Company Secretary
Colombo
15 May 2006

Statement of Directors' Responsibilities

The responsibilities of the Directors in relation to the financial statements of the Company and the Group differ from the responsibilities of the Auditors which are set out in their report appearing on page 45.

The Companies Act No.17 of 1982 require the Directors to prepare financial statements for each financial year giving a true and fair view of the state of affairs of the Company and the Group as at end of the financial year and of the Profit or Loss of the Company and the Group for the financial year. In preparing the financial statements appropriate accounting policies have been selected and applied consistently, reasonable and prudent judgements and estimates have been made, and applicable accounting standards have been followed.

The Directors are responsible for ensuring that the Company and its Subsidiary keep sufficient accounting records to disclose with reasonable accuracy the financial position of the Company and the Group and for ensuring that the financial statements have been prepared and presented in accordance with the Sri Lanka Accounting Standards and provide the information required by the Companies Act No.17 of 1982. They are also responsible for taking reasonable measures to safeguard the assets of the Group, and in that context to have proper regard to the establishment of appropriate systems of internal control with a view to the prevention and detection of fraud and other irregularities.

The Directors continue to adopt the going concern basis in preparing financial statements. The Directors, after making enquiries and following a review of the Group's Budget for the financial year ending 31st March 2007 including cash flows and borrowing facilities, consider that the Group has adequate resources to continue in operation.

By Order of the Board



Mildred Peries
Company Secretary
Colombo
15 May 2006

To The Members of Srilankan Airlines Limited

We have audited the balance sheet of Srilankan Airlines Limited as at 31st March 2006, the consolidated balance sheet of the Company and of its Subsidiary (Group) as at that date and the related statements of income, cash flows and changes in equity for the year then ended, together with the accounting policies and notes as set out on pages 46 to 68 of this Annual Report.

Respective Responsibilities of Directors and Auditors

The Directors are responsible for preparing and presenting these financial statements in accordance with Sri Lanka Accounting Standards. Our responsibility is to express an opinion on these financial statements, based on our audit.

Basis of Opinion

We conducted our audit in accordance with the Sri Lanka Auditing Standards, which require that we plan and perform the audit to obtain reasonable assurance about whether the said financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the said financial statements, assessing the accounting principles used and significant estimates made by the Directors, evaluating the overall presentation of the financial statements, and determining whether the said financial statements are prepared and presented in accordance with the Sri Lanka Accounting Standards. We have obtained all the information and explanations, which to the best of our knowledge and belief were necessary for the purposes of our audit. We therefore believe that our audit provides a reasonable basis for our opinion.

Opinion- Company

In our opinion, so far as appears from our examination, the Company has maintained proper books of account for the year ended 31st March 2006 and proper returns adequate for the purpose of our audit have been received from stations not visited by us and to the best of our information and according to the explanations given to us, the said balance sheet and related statements of income, cash flows and changes in equity and the accounting policies and notes thereto, which are in agreement with the said books and have been prepared and presented in accordance with the Sri Lanka Accounting Standards, provide the information required by the Companies Act. No 17 of 1982 and give a true and fair view of the Company's state of affairs as at 31st March 2006, and its profit and cash flows for the year then ended.

Opinion- Group

In our opinion, the consolidated balance sheet and statements of income, cash flows and changes in equity and the accounting policies and notes thereto have been properly prepared and presented in accordance with the Companies Act. No. 17 of 1982 and the Sri Lanka Accounting Standards, and give a true and fair view of the state of affairs as at 31st March 2006, and the profit and cash flows for the year then ended of the Company and its Subsidiary dealt with thereby, so far as concerns the members of the Company.

Directors' Interests in Contracts with the Company

According to the information made available to us, the Directors' of the Company were not directly or indirectly interested in contracts with the Company during the year ended 31st March 2006, except as stated in Note 21 to these financial statements.

Ernst & Young

Chartered Accountants

Colombo

15 May 2006

Income Statement

Year Ended 31st March 2006

	Note	Company		Group	
		2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Revenue	3	61,160.14	53,808.85	62,489.19	54,720.54
Cost of Sales		<u>(51,664.84)</u>	<u>(45,714.62)</u>	<u>(50,750.63)</u>	<u>(44,660.24)</u>
Gross Profit		9,495.30	8,094.23	11,738.56	10,060.30
Other Operating Income	4	355.34	1,132.76	511.90	1,223.48
Distribution and Marketing Costs		<u>(6,893.64)</u>	<u>(6,854.79)</u>	<u>(6,931.86)</u>	<u>(6,878.21)</u>
Administrative Expenses		<u>(1,840.41)</u>	<u>(2,048.00)</u>	<u>(2,898.27)</u>	<u>(2,663.49)</u>
Profit from Operating Activities	5	1,116.59	324.20	2,420.33	1,742.08
Finance Cost	6	<u>(282.54)</u>	<u>(328.11)</u>	<u>(282.54)</u>	<u>(328.11)</u>
Profit/(Loss) from Ordinary Activities before Taxation		834.05	(3.91)	2,137.79	1,413.97
Income Tax Expense	7	<u>(36.12)</u>	<u>11.57</u>	<u>(96.61)</u>	<u>(37.90)</u>
Net Profit for the Year		<u>797.93</u>	<u>7.66</u>	<u>2,041.18</u>	<u>1,376.07</u>
Basic Earnings Per Share (Rs.)	8	15.50	0.15	39.66	26.74

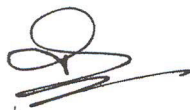
The accounting policies and notes on pages 50 through 68 form an integral part of the financial statements.

Colombo
15 May 2006

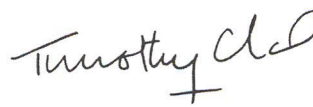
Balance Sheet
As At 31st March 2006

	Note	Company		Group	
		2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
ASSETS					
Non-Current Assets					
Property, Plant and Equipment	9	9,487.49	10,436.58	12,229.37	11,879.34
Investments	10	95.90	95.89	25.50	25.49
		<u>9,583.39</u>	<u>10,532.47</u>	<u>12,254.87</u>	<u>11,904.83</u>
Current Assets					
Inventories	11	3,169.92	2,748.56	3,240.73	2,828.32
Trade and Other Receivables	12	12,848.20	10,805.98	13,490.80	11,136.07
Cash and Bank Balances	13	8,421.80	8,748.72	8,741.49	8,877.66
		<u>24,439.92</u>	<u>22,303.26</u>	<u>25,473.02</u>	<u>22,842.05</u>
Total Assets		<u>34,023.31</u>	<u>32,835.73</u>	<u>37,727.89</u>	<u>34,746.88</u>
EQUITY AND LIABILITIES					
Capital and Reserves					
Issued Capital	14	5,146.35	5,146.35	5,146.35	5,146.35
Reserves	15	129.04	129.04	159.27	159.27
Accumulated Profits		1,805.14	1,007.21	8,300.65	6,259.47
		<u>7,080.53</u>	<u>6,282.60</u>	<u>13,606.27</u>	<u>11,565.09</u>
Non-Current Liabilities					
Interest Bearing Liabilities	16	38.81	2,954.16	1,528.69	2,954.16
Other Deferred Liabilities	17	1,368.11	1,217.30	1,473.68	1,327.76
		<u>1,406.92</u>	<u>4,171.46</u>	<u>3,002.37</u>	<u>4,281.92</u>
Current Liabilities					
Trade and Other Payables	18	21,617.51	18,546.66	17,183.86	15,048.30
Income Tax Payable		183.34	181.24	199.95	197.80
Interest Bearing Liabilities	16	3,735.01	3,653.77	3,735.44	3,653.77
		<u>25,535.86</u>	<u>22,381.67</u>	<u>21,119.25</u>	<u>18,899.87</u>
Total Equity and Liabilities		<u>34,023.31</u>	<u>32,835.73</u>	<u>37,727.89</u>	<u>34,746.88</u>

The Board of Directors is responsible for the preparation and presentation of these financial statements.
Signed for and on behalf of the Board by:



Chairman



Managing Director

The accounting policies and notes on pages 50 through 68 form an integral part of the financial statements.

Colombo
15 May 2006

Significant Accounting Policies

Year Ended 31st March 2006

1. CORPORATE INFORMATION

1.1. Legal Status and Domicile

SriLankan Airlines Limited is a limited liability Company incorporated and domiciled in Sri Lanka. The registered office of the Company is located at # 22-01, East Tower, World Trade Centre, Echelon Square, Colombo 01, Sri Lanka; and the principal place of business is situated at Bandaranaike International Airport, Katunayake, Sri Lanka.

1.2. Principal Activities and Nature of Operations

The Company

The principal activities of the Company is the operation of international scheduled, non-scheduled air services for the carriage of passengers, freight and mail as the designated carrier of Sri Lanka. Providing Air Terminal services at the Bandaranaike International Airport, the sale of duty free goods on-board and operation of Air Taxi services within Sri Lanka to carry passengers constitute other main activities of the Company.

The Subsidiary

The principal activity of the Company is the provision of inflight catering service to Airlines operating through the Bandaranaike International Airport, Katunayake, Sri Lanka.

1.3. Date of Authorisation for Issue

The financial statements of SriLankan Airlines Ltd., for the year ended 31st March 2006, were authorized for issue, in accordance with the resolution of the Board of Directors on 15th May 2006.

1.4. Number of Employees

The number of employees in service as at 31st March 2006 in the Company and its Subsidiary was 5,955. (31st March 2005 – 5,739)

2. SIGNIFICANT ACCOUNTING POLICIES

2.1 General

2.1.1 Basis of Preparation

The balance sheet, statements of income, changes in equity and cash flows, together with accounting policies and notes ("Financial Statements") of the Company and of the Group (Company and its Subsidiary, SriLankan Catering (Private) Ltd.) as at 31st March 2006, and for the year then ended, comply with the Sri Lanka Accounting Standards and therefore present fairly the financial position, financial performance and cash flows of the Company and the Group.

These financial statements presented in Sri Lanka Rupees million have been prepared on a historical cost basis, except for certain property, plant and equipment which are recorded at revalued amounts.

2.1.2 Consolidation Policy

(a) Basis of Consolidation

The financial statements of the Group represent the consolidation of the financial statements of the Company and its Subsidiary over which it has control after elimination of all material intra-group transactions and any unrealised gains arising from such transactions. The consolidated financial statements are prepared and presented in terms of Sri Lanka Accounting Standards No. 26 – Consolidated Financial Statements and Accounting for Investments in Subsidiaries.

The total profits and losses of the Company and its Subsidiary are shown in the consolidated income statement.

All assets and liabilities of the Company and its Subsidiary are shown in the consolidated balance sheet.

Significant Accounting Policies

Year Ended 31st March 2006

(b) Financial Year

The Company and its Subsidiary have a common financial year, which ends on 31st March.

2.1.3 Foreign Currency Translation

In terms of Sri Lanka Accounting Standards No. 21- The Effects of Changes in Foreign Exchange Rates, following accounting treatments are made in preparing the consolidated financial statements.

- (a) All foreign currency transactions are converted into Sri Lanka Rupees, which is the reporting currency, at the rate of exchange prevailing at the time of the transaction.
- (b) All monetary assets and liabilities denominated in foreign currencies as at balance sheet date are translated to Sri Lanka Rupee equivalents at the exchange rates ruling as at 31st March 2006.
- (c) Gains and losses arising on translation are dealt with through the income statement as exchange differences.

2.1.4 Taxation

(a) Local Taxation

The Company

The Company has signed an agreement under Section 17 of the Greater Colombo Economic Commission Law No. 4 of 1978 which exempts it from the payment of income tax in respect of profit and income of the Company on conduct and operation of the business of a commercial airline, providing international air transportation and all other ancillary and related services thereto, corporate tax and tax on dividends and royalties for an initial period of seven years from 01st September 1979, subsequently extended for a period of three years from 01st August 1986, and thereafter a period of five years from 01st August 1989.

In August 1994 the Board of Investment of Sri Lanka granted flagship status to the Company, extending the tax exemption period up to 31st March 1998.

In March 1998 the Board of Investment of Sri Lanka granted a further extension extending the tax exemption period up to 31st March 2013.

Income earned from the operation of "Air Taxi" services within Sri Lanka are liable to income tax in terms of the provisions of the Inland Revenue Act at the prevailing rates.

The Subsidiary - SriLankan Catering (Private) Ltd.

Income from the Flight Kitchen and the Transit Restaurant operated by the Subsidiary was exempted from income tax for a period of 15 years, up to 19th August 1995 in terms of agreement No. 139 of 29th June 1983 supplemented by agreement No. 110 of 20th August 1995 entered into with the Board of Investment of Sri Lanka (BOI) in terms of Section 17 of BOI Law No. 4 of 1978, subsequent to this period the Company is liable to pay income tax at 2% on Flight Kitchen and Transit Restaurant turnover for a period of 11 years with effect from 20th August 1995. The Public Restaurant is liable at the normal tax rate.

(b) Overseas Taxation

The Company is liable to tax on its overseas operations in countries where there are no double tax treaties at present. However, there is no liability in the current year due to the carry forward tax losses available to the Company.

(c) Deferred Taxation

The Company

No deferred taxation has been provided for in these financial statements, since majority of the assets will be fully depreciated before the expiry of the tax holiday period.

The Subsidiary - SriLankan Catering (Private) Ltd.

Deferred taxation in respect of the timing differences between the net book value of the assets of the Public

Significant Accounting Policies

Year Ended 31st March 2006

Restaurant on which depreciation allowances are claimed and their tax written down values have not been provided due to the carried forward tax losses of Rs. 83.32 million as at 31st March 2006.

2.1.5 Borrowing Costs

Borrowing costs amounting to Rs. 554.28 million incurred on long-term loans obtained to meet pre-delivery payments in respect of new aircraft have been capitalised during financial years 1992/93 to 1994/95 as part of the cost of such aircraft.

Exchange losses on long-term loans obtained to meet pre-delivery payments in respect of new aircraft are regarded as an adjustment to borrowing costs. Such exchange losses amounting to Rs. 242.15 million have been capitalised during the financial years 1992/93 to 1994/95 as part of the cost of aircraft, as permitted by Sri Lanka Accounting Standard No. 20 – Borrowing Costs.

Borrowing costs incurred which does not fall under the above two categories has been recognised as an expense in the income statement.

BALANCE SHEET

2.2. Valuation of Assets and their Bases of Measurement

2.2.1 Inventories

The Company

Inventories are stated at the lower of cost and net realisable value after making due allowances for any obsolete or slow moving items.

All inventories are valued on the basis of weighted average cost.

The Subsidiary - SriLankan Catering (Private) Ltd.

Inventories held at the Restaurants are valued on the basis of first in first out. All other inventories are valued on the basis of weighted average cost.

2.2.2 Trade and Other Receivables

Trade and Other Receivables are stated at the amounts that they are estimated to realise. Provision has been made in the financial statements for bad and doubtful receivables.

2.2.3 Cash and Cash Equivalents

Cash and cash equivalents comprise cash in hand, cash at bank, demand deposits, and short term highly liquid investments readily convertible to known amounts of cash and subject to insignificant risk of changes in value.

For the purpose of cash flow statement, cash and cash equivalents consist of cash in hand and deposits in banks net of outstanding bank overdrafts. Investments with short term maturities (i.e. three months or less from the date of acquisition) are also treated as cash equivalents.

2.2.4 Property, Plant and Equipment

(a) Cost and Valuation

Property, plant and equipment are recorded at cost of acquisition, construction or valuation thereon. These assets are stated at cost/valuation less accumulated depreciation which is provided for on the basis specified in (b) below.

Expenditure on major modifications and improvements, which result in an increase in the earning capacity or the useful life of the assets are capitalised. Expenditure on repairs and maintenance are charged to the income statement.

(i). Fleet

Additions to the fleet are reflected at cost. The Company receives credits from manufacturers in

Significant Accounting Policies

Year Ended 31st March 2006

connection with the acquisition of certain aircraft and engines. These credits are recorded as a reduction of the cost of the related aircraft and engines except where the aircraft is held under an operating lease, in which case the credits are deferred and reduced from the operating lease rentals on a straight-line basis over the period of the related lease as deferred credits.

(ii). **Aircraft Rotable Spares**

Aircraft rotatable spares, which are treated as tangible fixed assets, are recorded in the balance sheet at cost. This item is grouped under "Aircraft Related Equipment".

(iii). **Capital Projects**

Capital projects are stated at cost together with financing costs incurred from the date of commencement of the project to the date on which it is commissioned. When commissioned, capital projects are transferred to the appropriate category under property, plant and equipment and depreciated in accordance with Company policies.

(b) Depreciation

Provision for depreciation is calculated by using the straight line method on the cost or valuation of all property, plant and equipment, other than freehold land, in order to write off such amounts over the estimated useful economic lives of such assets as specified below.

New aircraft and spare engines	- over 16 years after making a 10 percent allowance for residual value.
Used aircraft and spare engines	- over the estimated remaining useful life, which is currently estimated to be 8 years
Buildings	- over the expected useful life subject to a maximum of 20 years.
Equipment	- over periods ranging from 1 to 10 years according to the type of equipment.
Aircraft rotatable spares	- over 8 years.

2.2.5 Leases

(a) Finance Leases

Property, plant and equipment on finance leases, which effectively transfer to the Company substantially all of the risks and benefits incidental to ownership of the leased items are capitalised at their cash price and depreciated over the period the Company is expected to benefit from the use of the leased assets. The corresponding principal amount payable to the lessor is shown as a liability. The interest element of the rental obligations pertaining to each financial year is charged to the income statement over the period of lease.

Costs of major modifications and re-configuration of aircraft are capitalised as part of aircraft cost and depreciated over the remaining term of the lease or the estimated useful life of the modifications/re-configuration, whichever is shorter.

(b) Operating Leases

Leases where the lessor effectively retains substantially all the risks and benefits of ownership of the leased asset are classified as operating leases. Rentals paid under operating leases are recognized in the income statement in the year they become payable.

Costs of major modifications and re-configuration of aircraft are capitalised as part of aircraft cost and depreciated over the remaining term of the lease.

(c) Sale and Lease back

Profits and losses which arise from sale and lease back transactions, which result in operating leases are recognized in the income statement immediately.

Significant Accounting Policies

Year Ended 31st March 2006

2.2.6 Investments

(a) Current investments

Current investments are stated at market value.

Unrealised gains and losses on current investments carried at market value are credited or charged to the income statement.

(b) Long-term investments

Long-term investments are stated at cost. The cost of investments is the cost of acquisition. The carrying amount of long-term investments is reduced to recognise a decline, other than temporary, in the value of investments determined on an individual investment basis.

In the Company's financial statements, investments in subsidiary company have been accounted for at cost, net of any provision for other than temporary diminution in value.

2.3 Liabilities and Provisions

2.3.1 Provisions for Liabilities

Provisions are recognised when the Company has a present obligation (legal or constructive) as a result of a past event, where it is probable that an outflow of resources embodying economic benefits will be required to settle the obligations and a reliable estimate can be made of the amount of the obligation.

2.3.2 Retirement Benefit Obligations

(a) Defined Benefit Plan-Gratuity

The Company

All employees based in Sri Lanka with 5 or more year's service with the Company are entitled to the payment of gratuity under the Payment of Gratuity Act No. 12 of 1983. An actuarial valuation of the gratuity liability of the Company as at 31st January 2005 was undertaken in February 2005 by Actuarial and Management Consultants (Pvt) Ltd., a firm of professional actuaries. The method used by the actuaries to value the gratuity liability is the "Project Unit Credit Method".

The key assumptions used by the actuary include the following:

- | | | |
|---|----------|----------|
| i) Rate of Interest | | 10% |
| ii) Rate of Salary Increase - LKR | | 13% |
| | - USD | 2% |
| Special Premium | - LKR | 13% |
| iii) Retirement Age | - Male | 55 years |
| | - Female | 55 years |
| iv) The Company will continue as a going concern. | | |

Based on these assumptions, the present value of the accrued benefits as at 31st March 2006 is Rs. 1,267.15 million. The amount recognised as an expense for the current year is Rs. 217.56 million. The gratuity liability is not externally funded. This item is grouped under "Other Deferred Liabilities" in the Balance Sheet.

Overseas-based employees are covered under social security schemes applicable in their home countries.

The Subsidiary - SriLankan Catering (Private) Ltd.

Provision for gratuity has been made in accordance with the payment of Gratuity Act No. 12 of 1983 and has been made for employees who have completed more than one year of service with the Company,

Significant Accounting Policies

Year Ended 31st March 2006

in accordance with Sri Lanka Accounting Standard No. 16 - Retirement Benefit Costs. This fund is not externally funded and nor actuarially valued. The basis for provision is as follows;

Years of Service	No. of months salary for each completed year
1 to 10 years	1/2
Over 10 years	1

(b) Defined Contribution Plans – Employees’ Provident Fund and Employees’ Trust Fund

Employees based in Sri Lanka are eligible for Employees’ Provident Fund Contributions and Employees’ Trust Fund Contributions in line with the respective statutes and regulations. The Company contributes 15% and 3% of gross emoluments to Employees’ Provident Fund and Employees’ Trust Fund respectively.

2.3.3 Frequent Flyer Programme

The Company operates a frequent-flyer programme known as “Skywards” established by Emirates. The incremental cost of providing awards in exchange for redemption of miles earned by members is accrued by Emirates as an operating cost and a liability after allowing for miles which are not expected to be redeemed. As members redeem their miles the liability is reduced to reflect the reduction in the outstanding obligation.

Pooled costs and revenue are shared among Emirates and SriLankan Airlines, in proportion to the Skywards frequent flyer miles issued to members on the flights operated by the Company and Emirates.

2.3.4 Commitment and Contingencies

Provisions are made for all obligations existing as at the balance sheet date when it is probable that such an obligation will result in an outflow of resources and reliable estimate can be made of the quantum of the outflow. All contingent liabilities and commitments are disclosed as a note to the financial statements unless the outflow of resources is remote.

INCOME STATEMENT

2.4 Revenue Recognition

(a) Airline Revenue Recognition

Passenger and Cargo sales are initially recorded as a liability in the sales in advance of carriage account and subsequently recognised as air transport revenue when the service is utilised through carriage by the Company.

Passenger and Cargo sales made by the Company and utilised on the services of other airlines are billed by them and offset against sales in advance of carriage when paid.

Passenger tickets that remain unutilised are credited to the income statement after a predetermined period. Actual revenue adjustments are dealt within the income statement.

(b) Income from Air Terminal, Catering and Other Services

Income from Air Terminal, Catering and Other Services are recognised when the services are rendered.

(c) Dividends and Interest

Dividends income and interest income are accounted for on a cash basis.

(d) Rental Income

Rental income is recognised on accrual basis.

(e) Royalties

Royalties are recognised on accrual basis in accordance with the substance of the relevant agreement.

(f) Others

Other income is recognised on a cash basis.

Significant Accounting Policies

Year Ended 31st March 2006

2.5 Expenditure Recognition

(a) General

Expenses are recognised in the income statement on the basis of a direct association between the costs incurred and the earning of specific items of income. All expenditure incurred in the running of the business and in maintaining property, plant and equipment in a state of efficiency has been charged to income in arriving at the profit for the year.

For the purpose of presentation of the income statement, the Directors are of the opinion that function of expenses method presents fairly the elements of the Company's performance, and hence such a presentation method is adopted.

(b) Aircraft Maintenance and Overhaul costs

All costs in relation to maintenance and overhaul of aircraft and engines including costs associated with heavy maintenance checks are charged to the income statement as they are incurred.

2.6 Fuel Risk Management

The Company's fuel risk management strategy aims to provide the Airline with the protection against sudden and significant escalation of oil prices thereby ensuring that the Airline is not competitively disadvantaged in a serious way in the event of a substantial increase in the price of fuel.

The strategy has helped to mitigate the impact of the recent increases in the price of jet fuel.

The net gain on the fuel risk management programme for the financial year 2005/06 was USD 11.49 million (Rs.1,162.08 million).

The Company has entered in to three fuel hedging contracts for the calendar year 2006 which had a mark to market value of USD 2.27 million (Rs. 233.73 million) as at 31st March 2006.

2.7 Segment Reporting

A segment is a distinguishable component of the group that is engaged in providing services within a particular economic environment which is subject to risks and rewards that are different from those of other segments. In accordance with Sri Lanka Accounting Standards No. 8 – Segment Reporting, segmental information is presented in respect of the Group.

Primary reporting is based on the geographical spread of operations as the group's risks and rates of return are predominantly affected by the fact that it operates in different countries.

The analysis of turnover by origin of sale is derived by allocating revenue to the area in which the sale was made.

Expenses that cannot be directly identified to a particular segment are not segregated and disclosed.

The major revenue earning asset of the company is the aircraft fleet which is employed across its worldwide route network. Management considers that there is no suitable basis for allocating such assets and related liabilities to geographical segments. Accordingly, segment assets, segment liabilities and other segment information by geographical segment is not disclosed.

The secondary reporting by business segment is based on the Group's internal structure.

The Group is engaged in three main business segments - Air Transportation, Air Terminal Services and Inflight Catering Services through the Subsidiary.

2.8 Cash Flow Statement

The cash flow of the Company and the Group has been presented using the indirect method in accordance with Sri Lanka Accounting Standard No. 9 – Cash Flow Statements.

2.9 Events Occurring after the Balance Sheet Date

All material events occurring after the balance sheet date are considered and where necessary adjustments are made in these financial statements.

Notes to the Financial Statements

Year Ended 31st March 2006

3 REVENUE

3.1 Revenue Analysis

	Company		Group	
	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Scheduled Services - Passenger	48,731.90	41,951.44	48,731.90	41,951.44
- Excess Baggage	668.25	499.21	668.25	499.21
- Cargo	8,109.97	7,353.80	8,085.13	7,331.90
- Mail	67.33	103.27	67.33	103.27
	57,577.45	49,907.72	57,552.61	49,885.82
Non Scheduled Services	12.78	52.14	12.78	52.14
Duty Free	351.96	338.33	351.96	338.33
Air Terminal & Other Services	3,217.95	3,510.66	3,200.51	3,498.61
Flight Catering	-	-	1,371.33	945.64
	61,160.14	53,808.85	62,489.19	54,720.54

3.2 In terms of the Value Added Tax (VAT) Act No. 14 of 2002 and subsequent amendments as such at present:

- Company activities directly connected with international transportation of passengers and cargo and the provision of air terminal services are zero rated.
- Any other income derived in Sri Lanka is liable at the standard rate of 15%.

3.3 Segment Reporting

(a) Primary Reporting by Geographical Segment - Turnover by Origin of Sale

	Asia Rs. M	Europe & Africa Rs. M	Middle East Rs. M	North & South America Rs. M	South West Pacific Rs. M	Total Rs. M
Scheduled Services - Passenger	21,452.17	14,285.17	10,353.63	1,987.73	653.20	48,731.90
- Excess Baggage	375.77	14.61	262.09	14.98	0.80	668.25
- Cargo	6,709.39	803.94	478.79	64.98	28.03	8,085.13
- Mail	55.16	11.31	0.21	0.62	0.03	67.33
	28,592.49	15,115.03	11,094.72	2,068.31	682.06	57,552.61
Non Scheduled Services	12.78	-	-	-	-	12.78
Duty Free	90.07	118.08	95.38	-	48.43	351.96
Air Terminal & Other Services	3,200.51	-	-	-	-	3,200.51
Flight Catering	1,371.33	-	-	-	-	1,371.33
	33,267.18	15,233.11	11,190.10	2,068.31	730.49	62,489.19

(b) Secondary Reporting by Business Segment

	Airline		Flight Catering		Group	
	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Revenue	61,160.14	53,808.85	2,882.44	2,491.51	62,489.19	54,720.54
Net Profit After Taxation	797.93	7.66	1,243.25	1,368.41	2,041.18	1,376.07
Assets	34,023.31	32,835.73	8,594.58	5,819.84	37,727.89	34,746.88
Liabilities	26,942.78	26,553.13	2,023.42	491.91	24,121.62	23,181.79
Operating Expenses	58,424.98	52,751.08	1,696.63	1,138.77	58,568.21	52,300.71
Depreciation and Amortisation	1,973.91	1,866.33	38.64	34.90	2,012.55	1,901.23
Acquisition of Property, Plant and Equipment	952.84	2,192.00	1,324.72	1,194.88	2,277.56	3,386.88

Values reported under "Group" exclude inter-group balances.

Notes to the Financial Statements
Year Ended 31st March 2006

4 OTHER OPERATING INCOME

	Company		Group	
	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Interest Income	271.23	312.69	274.93	313.01
Rental Income	0.24	0.24	0.24	0.24
Gain/(Loss) on Exchange	(22.37)	712.01	129.87	801.28
Income from Disposal of Investment	-	49.48	-	49.48
Miscellaneous Income	106.24	58.34	106.86	59.47
	<u>355.34</u>	<u>1,132.76</u>	<u>511.90</u>	<u>1,223.48</u>

5. PROFIT FROM OPERATING ACTIVITIES

stated after charging/(crediting):

	Company		Group	
	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Staff Expenses	7,092.82	6,721.56	7,356.74	6,961.62
Defined Benefit Plan Costs - Gratuity	232.30	310.26	234.04	345.65
Defined Contribution Plan Costs - EPF & ETF	542.25	496.63	561.27	516.99
Operating Lease Rentals	6,752.05	6,957.93	6,752.05	6,957.93
Advertising and Marketing Costs	6,887.25	6,556.69	6,925.47	6,580.11
Bad Debts	6.39	298.10	6.39	298.10
Depreciation	1,875.68	1,754.20	1,914.32	1,789.10
(Profit)/Loss on Disposal of Property, Plant and Equipment	(0.15)	105.06	(0.15)	95.74
Provision/(Reversal) for Impairment of Property, Plant and Equipment	-	-	(10.31)	29.83
Amortisation of A330 Pre-delivery Payments	98.23	112.13	98.23	112.13
Auditors' Remuneration - Audit	4.00	3.87	4.50	4.31
- Non Audit	0.47	0.66	0.92	1.06
Provision for Slow Moving Inventories	40.10	39.42	40.10	39.42
Gain on Fuel Risk Management Programme	(1,162.08)	(304.24)	(1,162.08)	(304.24)

6. FINANCE COST

	Company		Group	
	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Interest Expense on Borrowings and Bank Overdrafts	17.86	21.99	17.86	21.99
Finance Charges on Lease Liabilities	264.68	306.12	264.68	306.12
	<u>282.54</u>	<u>328.11</u>	<u>282.54</u>	<u>328.11</u>

7. INCOME TAX EXPENSE

	Company		Group	
	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Current Tax Expense on Ordinary Activities for the Year (7.1)	1.31	1.49	58.72	50.96
Economic Service Charge	34.00	-	34.00	-
Under/(Over) Provision of current taxes in respect of prior years	0.81	(13.06)	3.89	(13.06)
	<u>36.12</u>	<u>(11.57)</u>	<u>96.61</u>	<u>37.90</u>

Notes to the Financial Statements

Year Ended 31st March 2006

7.1 Reconciliation between Current Tax Expense/ (Income) and the product of Accounting Profit.

	Company		Group	
	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Accounting Profit/(Loss) before Taxation - Note 7.1 (a)	834.05	(3.91)	823.62	(12.44)
Aggregate Disallowed Items	-	-	5.19	5.40
Aggregate Allowable Expenses	-	-	(2.47)	(1.97)
Income not subject to Tax	(827.36)	6.97	(827.37)	6.97
Assessable Income under Normal Rate of Tax	6.69	3.06	(1.03)	(2.04)
Turnover at Specified Rate of Tax (2%)	-	-	2,863.56	2,473.48
Total Assesable Income	6.69	3.06	2,862.53	2,471.44
Set-Off of Current year Losses of Air Taxi Operation	(2.34)	-	(2.34)	-
Taxable Profit	4.35	3.06	2,860.19	2,471.44
Specified Tax Rate 2% on Turnover from				
Flight Kitchen & Restaurant	-	-	57.26	49.47
Statutory Tax Charge at Normal Rate of Tax	0.87	0.99	0.87	0.99
Social Responsibility Levy @ 0.25%	0.00	-	0.15	-
	0.87	0.99	58.28	50.46
Penalty @ 50%	0.44	0.50	0.44	0.50
Current Income Tax Expense	1.31	1.49	58.72	50.96

7.1 (a) Accounting Profit/(Loss) before taxation in relation to the Group consists only the Profit/(Loss) of the Company and the Public Restaurant of the Subsidiary.

8. EARNINGS PER SHARE

8.1 Basic Earnings Per Share is calculated by dividing the Net Profit for the year attributable to Ordinary Shareholders by the weighted average number of Ordinary Shares outstanding during the year.

8.2 The following reflects the income and share data used in the Basic Earnings Per Share computations.

	Company		Group	
	2006	2005	2006	2005
Net Profit attributable to Ordinary Shareholders for				
Basic Earnings Per Share Rs. Million	797.93	7.66	2,041.18	1,376.07
Weighted average number of Ordinary Shares in issue	51,463,463	51,463,463	51,463,463	51,463,463
Basic Earnings Per Share Rs.	15.50	0.15	39.66	26.74

Notes to the Financial Statements
Year Ended 31st March 2006

9. PROPERTY, PLANT AND EQUIPMENT

9.1 Company

	Land and Buildings	Equipment	Aircraft Reconfiguration Cost	Aircraft Related Equipment	Aircraft & Related Equipment on Finance Lease	Capital Work-in-Progress	Total
	Rs. M	Rs. M	Rs. M	Rs. M	Rs. M	Rs. M	Rs. M
Cost/Revaluation							
Balance as at 01st April 2005	1,186.75	3,257.91	640.00	4,409.04	16,642.32	35.42	26,171.44
Acquisitions/Modifications	47.80	444.48	143.05	260.41	31.21	25.89	952.84
Transfers/Adjustments	20.79	(0.13)	-	(9.74)	-	(33.28)	(22.36)
Disposals	(79.71)	(169.18)	-	-	-	-	(248.89)
Balance as at 31st March 2006	1,175.63	3,533.08	783.05	4,659.71	16,673.53	28.03	26,853.03
Accumulated Depreciation							
Balance as at 01st April 2005	917.20	2,558.09	96.32	2,972.31	9,190.94	-	15,734.86
Charge for the Year	52.84	307.41	159.92	312.69	1,042.82	-	1,875.68
Transfers/Adjustments	-	-	-	-	-	-	-
Disposals	(79.71)	(165.29)	-	-	-	-	(245.00)
Balance as at 31st March 2006	890.33	2,700.21	256.24	3,285.00	10,233.76	-	17,365.54
Net Book Value							
as at 31st March 2006	<u>285.30</u>	<u>832.87</u>	<u>526.81</u>	<u>1,374.71</u>	<u>6,439.77</u>	<u>28.03</u>	<u>9,487.49</u>
Net Book Value as at 31st March 2005	<u>269.55</u>	<u>699.82</u>	<u>543.68</u>	<u>1,436.73</u>	<u>7,451.38</u>	<u>35.42</u>	<u>10,436.58</u>

9.1 (a) The following Land and Buildings have been revalued during the financial year 1988/89.

Property owned by the Company and situated at
No. 12 Sir Baron Jayatileka Mawatha, Colombo 01.

Valuer and the Date of Valuation

Mr. D.S.A. Senaratne, Independent Chartered
Valuer, on 25th December 1988.

The SriLankan Administration and
Training Building situated at Katunayake.

Mr. S. Fernando, Independent Chartered
Valuer, on 20th January 1989.

The property situated at No. 12 Sir Baron Jayatileka Mawatha, Colombo 01., has been revalued using the Open Market Value Method

The SriLankan Administration and Training Building situated at Katunayake has been considered as "Special Properties" according to International Valuation and Accounting Practice, prescribed by the "Royal Institution of Chartered Surveyors", U.K. where by very special nature of the property, there is no Open Market Value in the general context. Hence this property has been revalued using the "Depreciated Replacement Costs Method" which has been devised for valuing these kind of properties having specialised nature.

The results of such revaluation have been incorporated in these financial statements from its effective date which is 1988/89. The surplus arising from the revaluation has been transferred to a revaluation reserve.

9.1 (b) During the financial year, the Company acquired property, plant and equipment to the aggregate value of Rs. 926.95 million (2004/05: Rs. 2,192.00 million). Cash payments amounting to Rs. 778.58 million (2004/05: Rs. 2,001.99 million) were made during the year to acquire property, plant and equipment.

9.1 (c) Property, plant and equipment includes fully depreciated assets having a gross carrying amount of Rs. 4,241.17 million (2004/05: Rs. 4,026.74 million).

Notes to the Financial Statements
Year Ended 31st March 2006

9. PROPERTY, PLANT AND EQUIPMENT

9.2 Group

	Land and Buildings	Equipment	Aircraft Reconfiguration Cost	Aircraft Related Equipment	Aircraft & Related Equipment on Finance Lease	Capital Work-in-Progress	Total
	Rs. M	Rs. M	Rs. M	Rs. M	Rs. M	Rs. M	Rs. M
Cost/Revaluation							
Balance as at 01st April 2005	1,286.02	3,697.52	640.00	4,409.04	16,642.32	1,427.26	28,102.16
Acquisitions/Modifications	47.80	478.67	143.05	260.41	31.21	1,319.15	2,280.29
Transfers/Adjustments	20.79	(0.13)	-	(9.74)	-	(33.28)	(22.36)
Reversal of Provision for Impairment	0.02	10.29	-	-	-	-	10.31
Disposals	(79.71)	(169.18)	-	-	-	-	(248.89)
Balance as at 31st March 2006	1,274.92	4,017.17	783.05	4,659.71	16,673.53	2,713.13	30,121.51
Accumulated Depreciation							
Balance as at 01st April 2005	1,014.54	2,948.71	96.32	2,972.31	9,190.94	-	16,222.82
Charge for the Year	54.81	344.08	159.92	312.69	1,042.82	-	1,914.32
Transfers/Adjustments	-	-	-	-	-	-	-
Disposals	(79.71)	(165.29)	-	-	-	-	(245.00)
Balance as at 31st March 2006	989.64	3,127.50	256.24	3,285.00	10,233.76	-	17,892.14
Net Book Value							
as at 31st March 2006	285.28	889.67	526.81	1,374.71	6,439.77	2,713.13	12,229.37
Net Book Value as at 31st March 2005	271.48	748.81	543.68	1,436.73	7,451.38	1,427.26	11,879.34

9.2 (a) Land and Buildings of the Company and the Group which have been revalued are disclosed under Note 9.1 (a) Details of such Land and Buildings that have been revalued are stated below.

Land and Building at Valuation	Rs. M
Balance as at 01st April 2005	107.77
Acquisitions / Modifications	-
Balance as at 31st March 2006	107.77
Accumulated Depreciation	
Balance as at 01st April 2005	100.37
Charge for the Year	2.09
Balance as at 31st March 2006	102.46
Net Book Value as at 31st March 2006	5.31
Net Book Value as at 31st March 2005	7.40

The Initial cost of the revalued land and building was Rs. 49.65 million.

9.2 (b) Group property, plant and equipment includes fully depreciated assets having a gross carrying amount of Rs. 4,704.60 million (2004/05: Rs. 4,434.52 million).

Notes to the Financial Statements

Year Ended 31st March 2006

10. INVESTMENTS - NON QUOTED

Name of the Company	Country of Incorporation	Holding %	Company		Group	
			2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
SriLankan Catering (Private) Ltd.	Sri Lanka	100%	70.40	70.40	-	-
SITA INC Foundation	Netherlands	0.8%	25.50	25.49	25.50	25.49
			<u>95.90</u>	<u>95.89</u>	<u>25.50</u>	<u>25.49</u>

The above investments are stated at cost. The Directors also have assessed the fair value of these investments to be at cost since these investments are not marketable.

The investment in SITA INC. represents unquoted depository certificates without fixed maturity.

11. INVENTORIES

	Company		Group	
	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Consumable Stocks	3,137.82	2,700.80	3,208.63	2,780.56
Duty Free Stocks	32.10	47.76	32.10	47.76
	<u>3,169.92</u>	<u>2,748.56</u>	<u>3,240.73</u>	<u>2,828.32</u>

Total Inventories are valued at lower of cost and net realisable value.

12. TRADE AND OTHER RECEIVABLES

	Company		Group	
	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Trade Receivables	5,484.23	3,999.00	5,590.05	4,044.85
Less: Provision for doubtful debts	(476.32)	(460.90)	(476.32)	(460.90)
	<u>5,007.91</u>	<u>3,538.10</u>	<u>5,113.73</u>	<u>3,583.95</u>
Receivables from Related Parties (Note 12.1)	31.38	54.44	97.61	121.68
Other Receivables - Current	2,842.63	3,061.80	2,842.63	3,061.80
- Non Current	2,573.19	1,544.70	2,573.19	1,544.70
Advances and Prepayments	2,380.80	2,585.91	2,848.52	2,799.98
	<u>12,835.91</u>	<u>10,784.95</u>	<u>13,475.68</u>	<u>11,112.11</u>
Loans and Advances to Company officers (Note 12.2)	12.29	21.03	15.12	23.96
	<u>12,848.20</u>	<u>10,805.98</u>	<u>13,490.80</u>	<u>11,136.07</u>

12.1 Receivables from Related Parties:

SriLankan Catering (Private) Ltd.	-	1.28	-	-
Emirates	31.38	53.16	97.61	121.68
	<u>31.38</u>	<u>54.44</u>	<u>97.61</u>	<u>121.68</u>

12.2 Loans to Company Officers:

Given below are particulars of loans granted to Company officers in excess of Rs. 20,000 only;

Balance as at 01st April	0.18	1.69	2.21	4.02
Loans granted during the year	0.70	-	2.33	2.69
Repayments	(0.22)	(1.51)	(1.18)	(4.50)
Balance as at 31st March	<u>0.66</u>	<u>0.18</u>	<u>3.36</u>	<u>2.21</u>

Notes to the Financial Statements

Year Ended 31st March 2006

13. CASH AND CASH EQUIVALENTS

	Company		Group	
	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Cash and Bank Balances	852.06	775.83	1,171.75	904.77
Short Term Deposits	7,569.74	7,972.89	7,569.74	7,972.89
	<u>8,421.80</u>	<u>8,748.72</u>	<u>8,741.49</u>	<u>8,877.66</u>
Bank Overdrafts	(720.10)	(351.03)	(720.53)	(351.03)
	<u>7,701.70</u>	<u>8,397.69</u>	<u>8,020.96</u>	<u>8,526.63</u>

For the purpose of Cash Flow Statement the year end Cash and Cash Equivalent comprises the above.

14. SHARE CAPITAL

14.1 Authorised

	Company	
	2006 Rs. M	2005 Rs. M
150,000,000 Ordinary Shares of Rs.100/- each	15,000.00	15,000.00
	<u>15,000.00</u>	<u>15,000.00</u>

14.2 Issued and Fully Paid

	Company	
	2006 Rs. M	2005 Rs. M
51,463,463 Ordinary Shares of Rs.100/- each	5,146.35	5,146.35
	<u>5,146.35</u>	<u>5,146.35</u>

15. RESERVES

	Company		Group	
	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Capital Reserves (Note 15.1)	75.60	75.60	105.20	105.20
Revenue Reserves	-	-	0.63	0.63
General Reserves (Note 15.2)	53.44	53.44	53.44	53.44
	<u>129.04</u>	<u>129.04</u>	<u>159.27</u>	<u>159.27</u>

15.1 Capital Reserves

Company / Group

- (a) Capital Reserves of the Company/ Group comprise of surplus arising out of the revaluation of property, plant and equipment which amounted to Rs. 75.60 million. (Note 9.1 (a))
- (b) Reserve on Consolidation Rs. 8.00 million.
- (c) Bonus issue Rs. 21.6 million.

15.2 General Reserves

General reserve of Rs. 53.44 million represent transfers from Capital Reserves in prior years relating to exchange differences capitalised in 1987/88 and in 1988/89 in respect of property, plant and equipment which have been financed by foreign currency loans.

Notes to the Financial Statements

Year Ended 31st March 2006

16. INTEREST BEARING LIABILITIES

	Company		Group	
	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Current Liabilities				
Finance Leases (Note 16.1(b))	2,939.48	3,168.65	2,939.48	3,168.65
Long-term Loans (Note 16.2 (b))	75.43	134.09	75.43	134.09
Bank Overdraft	720.10	351.03	720.53	351.03
	<u>3,735.01</u>	<u>3,653.77</u>	<u>3,735.44</u>	<u>3,653.77</u>
Non - Current Liabilities				
Finance Leases (Note 16.1(b))	-	2,843.64	-	2,843.64
Long-term Loans (Note 16.2 (b))	38.81	110.52	1,528.69	110.52
	<u>38.81</u>	<u>2,954.16</u>	<u>1,528.69</u>	<u>2,954.16</u>

16.1 (a) Finance Lease Liabilities

	2006 Rs. M	2005 Rs. M
Balance as at 01st April	6,012.29	8,709.94
Additions during the year	-	-
Payments during the year	(3,220.58)	(2,946.35)
Restatements	147.77	248.70
Balance as at 31st March	<u>2,939.48</u>	<u>6,012.29</u>

16.1 (b) Finance Lease Liabilities

	2006 Rs. M	2005 Rs. M	2006 USD M	2005 USD M
Payable within one year included under Current Liabilities	2,939.48	3,168.65	28.61	31.88
Between :				
- One and two years	-	2,843.64	-	28.61
	<u>2,939.48</u>	<u>6,012.29</u>	<u>28.61</u>	<u>60.49</u>

The future payments of interest charges relating to these finance leases are as follows:

	Rs. M	USD M
Payable within one year	<u>132.60</u>	<u>1.29</u>

Interest rates applicable to the finance leases ranged from 3.1619 percent to 9.1141 percent per annum. The Government of Sri Lanka has guaranteed the obligations of the Company under the finance lease agreements up to a limit of US Dollars 28.61 million (Rs. 2,939.48 million).

Conversion rate - 1 US Dollar = Rs. 102.75 (2004/05: Rs. 99.4).

16.2 (a) Long-term Loans

	Company		Group	
	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Balance as at 01st April	244.61	370.31	244.61	370.31
Additions during the year	-	-	1,489.88	-
Payments during the year	(136.84)	(136.61)	(136.84)	(136.61)
Restatements	6.47	10.91	6.47	10.91
Balance as at 31st March	<u>114.24</u>	<u>244.61</u>	<u>1,604.12</u>	<u>244.61</u>

Notes to the Financial Statements
Year Ended 31st March 2006

16.2 (b) Long-term Loans	2006	2005	2006	2005
Company	Rs. M	Rs. M	USD M	USD M
Payable within one year included under Current Liabilities	<u>75.43</u>	<u>134.09</u>	<u>0.73</u>	<u>1.35</u>
Between :				
- One and two years	12.25	72.97	0.12	0.73
- two and three years	12.25	11.86	0.12	0.12
- three and four years	12.25	11.86	0.12	0.12
- four and five years	2.06	11.86	0.02	0.12
- after five years	-	1.98	-	0.02
Payable after one year included under Non - Current Liabilities	<u>38.81</u>	<u>110.52</u>	<u>0.38</u>	<u>1.11</u>
	<u>114.24</u>	<u>244.61</u>	<u>1.11</u>	<u>2.46</u>
Long-term Loans	2006	2005	2006	2005
Group	Rs. M	Rs. M	USD M	USD M
Payable within one year included under Current Liabilities	<u>75.43</u>	<u>134.09</u>	<u>0.73</u>	<u>1.35</u>
Between :				
- One and two years	359.04	72.97	3.50	0.73
- two and three years	359.04	11.86	3.50	0.12
- three and four years	359.04	11.86	3.50	0.12
- four and five years	348.82	11.86	3.40	0.12
- after five years	102.75	1.98	1.00	0.02
Payable after one year included under Non - Current Liabilities	<u>1,528.69</u>	<u>110.52</u>	<u>14.88</u>	<u>1.11</u>
	<u>1,604.12</u>	<u>244.61</u>	<u>15.61</u>	<u>2.46</u>

Loans are repayable on various dates up to the year 2007 at varying interest rates which ranged from 3.1619 percent to 9.1141 percent per annum during the year. The outstanding aircraft spares loan amounting to US Dollars 0.61 million (Rs.62.68 million) is guaranteed by the Government of Sri Lanka.

Conversion rate - 1 US Dollar = Rs. 102.75 (2004/05: Rs. 99.4).

17. OTHER DEFERRED LIABILITIES

Retirement Benefit Obligations	Company		Group	
	2006	2005	2006	2005
	Rs. M	Rs. M	Rs. M	Rs. M
Balance as at 01st April	1,217.30	960.88	1,327.76	1,037.68
Charge for the year	232.30	310.26	234.04	345.65
Payments during the year	(81.49)	(53.84)	(88.12)	(55.57)
Balance as at 31st March	<u>1,368.11</u>	<u>1,217.30</u>	<u>1,473.68</u>	<u>1,327.76</u>

Notes to the Financial Statements
Year Ended 31st March 2006

18. TRADE AND OTHER PAYABLES

	Company		Group	
	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Trade Payables	7,046.76	7,588.54	7,092.66	7,800.27
Payables to Related Parties (Note 18.1)	4,874.26	3,862.50	52.23	21.64
Dividends Payable	2.30	2.55	2.30	2.55
Sales in Advance of Carriage	9,336.25	6,917.80	9,336.25	6,917.79
Accrued Expenses and Other Payables	357.94	175.27	700.42	306.05
	<u>21,617.51</u>	<u>18,546.66</u>	<u>17,183.86</u>	<u>15,048.30</u>

18.1 Payables to Related Parties

	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
SriLankan Catering (Private) Ltd.	4,822.03	3,840.86	-	-
Emirates	52.23	21.64	52.23	21.64
	<u>4,874.26</u>	<u>3,862.50</u>	<u>52.23</u>	<u>21.64</u>

19. COMMITMENTS AND CONTINGENCIES

19.1 Capital Commitments

The Group and Company's commitment for acquisition of property, plant and equipment incidental to the ordinary course of business as at 31st March, is as follows:

	Company		Group	
	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Contracted but not provided for	74.36	405.15	74.36	405.15
Authorised by the Board, but not contracted for	94.45	133.72	94.45	1,028.32
	<u>168.81</u>	<u>538.87</u>	<u>168.81</u>	<u>1,433.47</u>

19.2 Financial Commitments

The Company's annual commitment for minimum lease payments under non-cancellable operating leases as at 31st March were as follows:

	2006 Rs. M	2005 Rs. M
Within one year	6,552.69	6,335.69
Between one and five years	26,022.52	30,971.68
After five years	-	237.26
	<u>32,575.21</u>	<u>37,544.63</u>

Under the terms of the lease agreements, no contingent rentals are payable.

19.3 Commitment on Guarantee of Loan

The Company has guaranteed the loan of USD 22.5 million obtained by its' Subsidiary SriLankan Catering (Private) Ltd., for the construction of the new flight kitchen. The Subsidiary has utilised USD 14.5 million thereof as at 31st March 2006.

19.4 Contingencies

a) No provision has been made in these accounts in respect of contingent liabilities arising in the normal course of business of the Company in respect of legal actions or other claims and potential claims being made against the Company.

But the management estimates contingent liabilities of Rs. 9,448.96 million.

Notes to the Financial Statements

Year Ended 31st March 2006

- b) All employees based in Sri Lanka with five or more years of service with the Company are entitled to the payment of gratuity, under the Payment of Gratuity Act. No. 12 of 1983. An actuarial valuation of the gratuity liability of the Company as at 31st January 2005 was undertaken in February 2005 by Actuarial and Management Consultants (Pvt) Ltd. The actuarial valuation assumed a salary escalation rate of 13% per annum in respect of salaries denoted in Sri Lankan Rupees, a salary escalation rate of 2% per annum in respect of salaries denoted in US Dollars, and a discount rate of 10% per annum. Based on these assumptions the present value of accrued benefits, as at 31st March 2006 is Rs. 1,267.15 million. If the method of making a provision for all employees as required under the Payment of Gratuity Act No. 12 of 1983 were to be adopted, the gratuity liability of the Company as at 31st March 2006 would be Rs. 2,265.25 million. Hence there is a contingent liability of Rs. 998.10 million which would crystallise if the Company ceases to be a going concern.

20. EVENTS OCCURRING AFTER THE BALANCE SHEET DATE

Since the balance sheet date, there have been no other events which could materially effect the state of affairs of the Company/Group as shown by the financial statements as at that date, the profit for the year then ended, or any of the figures in the Financial Statements and notes thereto.

21. DIRECTORS' INTERESTS IN CONTRACTS WITH THE COMPANY

- 21.1 The government of Sri Lanka has nominated four Directors to the Board of the Company. The Nominee Directors as at 31st March 2006 and holding office as at date are:

Mr. D H S Jayawardena - Chairman
Mr. S Ukwatte
Mr. R A Chandiram
Mr. N A Wickremasinghe

Mr. J M S Britto who held office of Chairman since May 2005 resigned from his position effective from January 2006, and Mr. D H S Jayawardena was appointed Chairman with effect from January 2006.

The Company carries out transactions in the ordinary course of business on an arms length basis with Director related entities.

- 21.2 Emirates, which holds 43.63% of the Issued Share Capital of the Company as at balance sheet date, together with Management Control of the Company for a period of ten years from 31st March 1998, has in accordance with Articles 80 of the Article of Association of the Company has nominated and appointed three Directors to the Board.

The nominee Directors as at 31 March 2006 and holding office as at date are:

Mr. T C Clark - Managing Director
Mr. G W Chapman
Mr. N J Hopkins
Mr. P M Hill - Alternate Director to Mr. T C Clark
Mr. P M Flanagan - Alternate Director to Mr. G W Chapman
Mr. Ghaith Al Ghaith - Alternate Director to Mr. N J Hopkins

The Company has entered into a number of related party agreements which are disclosed in note 22.2.

The Company has nominated four Directors to the Board of SriLankan Catering (Private) Ltd., with whom the Company has a contract for catering, the value of which is disclosed in note 22.1.

The current Directors of SriLankan Catering (Private) Ltd. are;

Mr. D H S Jayawardena - Chairman
Mr. G W Chapman
Mr. S Ukwatte
Mr. R A Chandiram
Mr. D Nijhawan - Alternate Director to Mr. G W Chapman

Notes to the Financial Statements

Year Ended 31st March 2006

22. RELATED PARTY DISCLOSURES

22.1 SriLankan Catering (Private) Ltd., provides flight catering services to the Company, and the Company provides passenger and freight services to the Subsidiary in the normal course of business.

During the year ended 31st March 2006, the value of flight catering services provided to the Company amounted to Rs. 1,511.11 million, while freight and air tickets provided by the Company to SriLankan Catering (Private) Ltd., amounted to Rs. 42.29 million.

22.2 Emirates holds 43.63% of the Issued Share Capital of the Company. The Company has entered into a number of specific related party agreements in the normal course of business to obtain goods and services from Emirates Group on commercial terms. The Company has also entered into an exclusive marketing and sales agreement with Emirates, trading as Galileo Emirates, for the purpose of distributing Galileo CRS for use in Sri Lanka.

Transactions between the Group, Emirates and Dnata are summarised as follows:

	2006	2005	2006	2005
	Rs. M	Rs. M	USD M	USD M
	Receipts/ (Payments)	Receipts/ (Payments)	Receipts/ (Payments)	Receipts/ (Payments)
(a) Purchase of computer systems and services	(799.89)	(870.35)	(7.89)	(8.54)
(b) Purchase of other goods and services	(343.33)	(68.36)	(3.40)	(0.67)
(c) Net receipt on transactions relating to international air transport, settled through the IATA Clearing House	240.92	487.54	2.39	4.82
(d) Amortisation of profit on termination of fuel risk management programme	-	54.30	-	0.52
(e) Galileo segment commission	36.22	21.17	0.36	0.21
(f) Inflight catering net of discounts	398.62	462.96	3.88	4.58
(g) Frequent flyer programme	(94.91)	(58.98)	(0.93)	(0.58)
(h) Net Sales	285.34	185.55	2.82	1.83
(i) Ground Handling Services	(169.31)	(156.03)	(1.68)	(1.54)
	(446.34)	57.82	(4.44)	0.63

23. COMPARATIVE INFORMATION

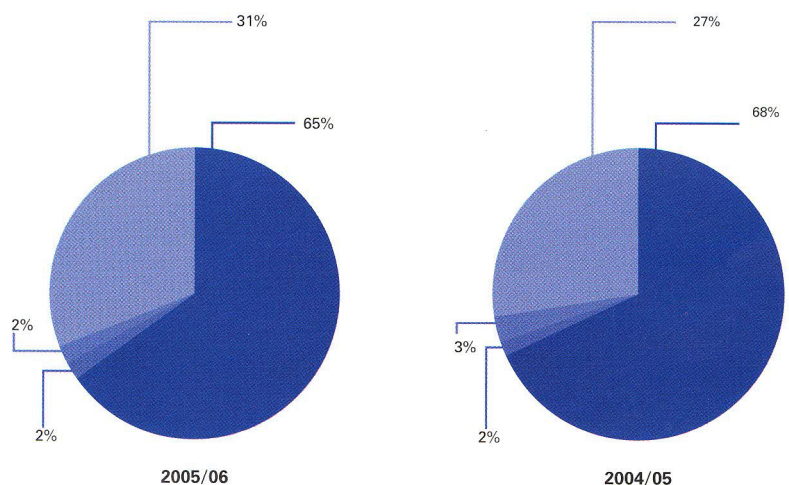
Accounting policy applied by the Group and Company are consistent with those used in the previous years. Certain comparative amounts have been reclassified to conform to the current year's presentation.

Statement of Value Added

	Company		Group	
	2006 Rs. M	2005 Rs. M	2006 Rs. M	2005 Rs. M
Value Added				
Total revenue	61,160.14	53,808.85	62,489.19	54,720.54
Purchases of goods and services	(50,571.09)	(44,604.73)	(50,239.18)	(43,736.55)
Value added by the Company	10,589.05	9,204.12	12,250.01	10,983.99
(Deficit)/Surplus on sale of fixed assets	(0.15)	105.06	(0.15)	95.74
Investment income	271.23	312.69	274.93	313.01
Non operating revenue	106.48	108.06	107.10	109.19
Total value added	<u>10,966.61</u>	<u>9,729.93</u>	<u>12,631.89</u>	<u>11,501.93</u>
Distribution of value added :				
To employees- as remuneration	7,867.37	7,528.45	8,152.05	7,824.26
To government- as corporation and other taxes as franchise fees to Airport & Aviation	36.12 106.97	(11.57) 123.08	96.61 145.19	37.90 146.50
To suppliers of capital- as interest	282.54	328.11	282.54	328.11
Retained for re-investment and future growth Depreciation Retained profits	1,875.68 797.93	1,754.20 7.66	1,914.32 2,041.18	1,789.10 1,376.07
Total value added	<u>10,966.61</u>	<u>9,729.93</u>	<u>12,631.89</u>	<u>11,501.93</u>
Value Added/Employee	2.03	1.88	2.12	2.00
Employee Cost	1.46	1.46	1.37	1.36

Value added is a measure of wealth created. This statement shows the value added and its distribution by way of payments to employees, government and to providers of capital. It also indicates the proportion retained for re-investment and future growth.

Distribution of Value Added
Group



■ Employees ■ Government ■ Suppliers of Capital ■ Re-investment & Growth

Decade at a Glance

		1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
INCOME STATEMENT											
Operating revenue	Rs. Million	15,619.30	17,592.00	19,171.43	24,354.32	30,437.09	29,352.91	36,235.04	45,397.54	53,808.85	61,160.14
Operating expenditure	Rs. Million	14,121.08	14,657.41	16,139.49	23,423.18	31,817.28	31,307.87	34,451.68	42,311.16	54,617.41	60,398.89
Net profit/(loss)	Rs. Million	(1,329.21)	1,641.59	1,272.93	3,661.34	(4,734.89)	(2,048.95)	2,336.38	4,555.14	7.66	797.93
BALANCE SHEET											
Share capital	Rs. Million	5,146.35	5,146.35	5,146.35	5,146.35	5,146.35	5,146.35	5,146.35	5,146.35	5,146.35	5,146.35
Non Current Assets	Rs. Million	19,217.72	17,882.38	16,359.69	17,525.99	14,952.28	12,826.78	11,218.59	10,203.34	10,436.58	9,487.49
Current assets	Rs. Million	8,769.55	11,196.80	16,090.86	14,930.23	14,247.30	12,061.52	18,713.33	24,954.44	22,303.26	24,439.92
Total assets	Rs. Million	28,017.67	29,109.58	32,520.95	32,526.62	29,269.98	24,958.70	30,027.81	35,253.67	32,835.73	34,023.31
Current liabilities	Rs. Million	8,856.67	9,224.37	11,477.25	13,528.69	16,886.18	11,578.40	16,641.12	20,612.84	22,381.67	25,535.86
YIELD/UNIT COST											
Overall yield	Rs. tkm	27.4	29.3	31.3	31.8	30.2	38.6	43.0	47.3	48.1	52.22
Unit cost	Rs. tkm	20.4	20.8	20.4	22.9	24.5	27.5	30.6	32.5	36.0	37.42
Breakeven load factor	%	74.6	70.9	65.3	72.0	81.1	71.3	71.3	68.7	74.9	71.65
Revenue per RPK	Rs./RPK	3.0	3.2	3.3	3.4	3.1	3.8	4.3	4.9	5.1	5.32
PRODUCTION											
Passenger capacity	ASK Millions	5,525.10	5,672.66	6,209.80	8,038.31	10,891.61	8,556.92	8,422.77	9,692.08	11,326.54	11,934.86
Overall capacity	ATK Millions	746.78	757.42	832.69	1,088.38	1,454.78	1,148.73	1,121.89	1,289.94	1,484.02	1,590.55
TRAFFIC											
Passengers carried	Nos. Thousands	1,196	1,201	1,260	1,475	1,891	1,615	1,806	2,065	2,423	3,005.47
Passengers carried	RPK Millions	4,003.19	4,154.46	4,417.55	5,459.65	7,447.87	5,862.09	6,408.38	7,276.35	8,142.54	9,050.44
Passenger load factor	%	72.45	73.24	71.14	67.92	68.38	68.51	76.08	75.08	71.89	75.83
Cargo carried	Tonnes	35,039	36,478	35,566	41,670	58,618	46,067	47,650	54,943	66,977	82,142
Cargo load carried	RTK Millions	164.43	173.62	156.61	195.67	266.75	186.47	200.45	240.90	296.68	300.73
Overall load carried	RTK Millions	522.09	547.14	554.90	703.28	932.72	711.72	785.11	896.59	1,039.34	1,102.77
Cargo load factor	%	61.94	65.40	57.50	57.53	54.77	44.19	46.22	52.08	56.95	56.11
Overall load factor	%	69.91	72.24	66.64	64.62	64.11	61.96	69.98	69.51	70.04	69.33
STAFF											
Average strength	Nos.	4,965	4,823	4,832	5,070	5,196	4,049	4,182	4,714	5,163	5,395
Revenue per employee	Rs. '000	3,146	3,648	3,968	4,804	5,858	7,249	8,665	9,630	10,422	11,336
Capacity per employee	Tonne-km	150,409	157,043	172,329	214,670	279,981	283,706	268,266	273,640	287,433	294,820
Load carried per employee	Tonne-km	105,153	113,444	114,838	138,713	179,507	175,777	187,735	190,197	201,305	204,406
FLEET											
L1011-500	Nos.	2	2	2	-	-	-	-	-	-	-
L1011-100	Nos.	1	1	1	-	-	-	-	-	-	-
L1011-50	Nos.	1	1	1	-	-	-	-	-	-	-
A320-200	Nos.	2	2	2	2	2	1	2	3	5	5
A330-200	Nos.	-	-	-	4	6	4	4	4	4	4
A340-300	Nos.	3	3	3	4	4	3	3	5	5	5
Turbo Otter	Nos.	-	-	-	-	-	-	-	-	2	2
Aircraft in service											
at year end	Nos.	9	9	9	10	12	8	9	12	16	16

Glossary

Available Seat Kilometres (ASK)

The product of seats offered for sale and distance over which they are carried.

Available Tonne Kilometres (ATK)

This is the measure of transport production.

The ATK produced by a flight are the capacity for payload of the aircraft measured in tonnes multiplied by the distance flown.

Revenue Passenger Kilometres (RPK)

The product of passengers carried and the distance over which they are carried.

Revenue Tonne Kilometres (RTK)

The product of passenger and cargo carried in tonnes and the distance over which they are carried.

Load Factor

The percentage relationship of revenue load to capacity provided.

The passenger load factor relates RPK to ASK while the overall load factor relates RTK to ATK.

Revenue per RPK

The revenue per RPK relates the passenger revenue to RPK.

Unit Cost

The unit cost relates the total operating cost to ATK.

Overall Yield

Overall Yield relates the net traffic revenue to RTK.

The net traffic revenue being the sum of the passenger, excess baggage, cargo and mail revenue.

Break-even Load Factor

The load factor required to equate revenue from scheduled airline operations with operating costs.

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Fax: 565 3544
Email: srilankan-khi@cyber.net.pk

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23 Empress Road, Lahore
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Doha-Qatar
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Res: 4441217/ 4360286
Fax +974 4362334
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Tel: + 974 4621571
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REPUBLIC OF IRELAND

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Kanoo Airline Centre
King Abdul Aziz Street
P.O. Box 1878 - Al Khobar - 31952 - K.S.A.
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Sales] Res/ Ticketing: 00966 3 882 2789 / 2792
/ 2675 / 5632
Hunting Line 00966 3 882 5161
Fax Admin/Sales: 00966 3 882 3940
Res/Ticketing: 00966 3 882 2136
Email: Sales dmmsales@srilankan.aero,
Res/ Ticketing ul_dmmres01@srilankan.aero,
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PO Box 23, Honiara, Guadalcanal
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SOUTH AFRICA

JOHANNESBURG:

SriLankan Airlines,
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Email: cpt@holidayholdings.co.za

SOUTH KOREA

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Choong-Ku 100 814
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Fax: (82 2) 755 9758
Email: selpaa@unitel.co.kr

SPAIN

All inquiries to:
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115, rue Reaumur 75002, Paris, France.
Tel: 0033 1 42 97 95 72
Fax: 0033 1 42 86 83 20
Email: commercialsupport.paris@srilanka
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SRI LANKA

COLOMBO:

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Res: 242 1161
Reconfirmation: 019733 5500
Flight information: 019733 1377/2377
Customer affairs: 019733 1413
Fax: 019733 5145
Email: customer@srilankan.aero

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Echelon Square, Colombo 1
Tel: General Enquiries 019733 3723

SriLankan Directory

Worldwide Office Network

Business Class: 019733 3729

Business Class Fax: 019733 5312

Government travel: 019733 3833

Skywards/Bus Class: 019733 3842

Skywards/Bus Class Fax: 019733 5367

Also Ticketing:

SriLankan Airlines,

Bandaranaike Int'l Airport

Tel: 019733 2424 (24 hours)

SRILANKAN CARGO

660 Galle Rd, Colombo 3

Tel: 019733 3278/79/88

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opp The Queens Hotel,

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Umm al-Qaiwain National Travel Agency,

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nalin@srilankanusa.com

Notice of Meeting

Notice is hereby given that the Twenty Eighth Annual General Meeting of the Shareholders of SriLankan Airlines Limited will be held at the 'Cat'seye Ballroom' of the Ceylon Continental Hotel, No.48 Janadhipathi Mawatha, Colombo 1, on 28 June 2006, at 9.00 a.m for the following purposes.

Agenda

1. To receive and adopt the Directors' Report and the Audited Accounts for the financial year ended 31st March 2006 with the Report of the Auditors thereon.
2. To declare a dividend as recommended by the Directors.
3. To re-appoint M/s Ernst & Young as Auditors and authorize the Directors to fix their remuneration.

By Order of the Board



Mildred Peries
Company Secretary
Colombo
01 June 2006

Note:

1. Member entitled to attend and vote at the meeting is entitled to appoint a proxy to attend and vote instead of him.
2. A Proxy need not be a member of the Company.
3. A form of Proxy accompanies this notice.
4. Shareholders/Proxies attending the meeting are requested to bring this Notice and their National Identity Cards.

SRILANKAN AIRLINES LIMITED

I /We the undersigned,

..... of

.....

being a member/s of SriLankan Airlines Limited hereby appoint of

..... or failing him/her

- | | |
|-----------------------|---------------------------|
| Mr D H S Jayawardena | of Colombo or failing him |
| Mr S Ukwatta | of Colombo or failing him |
| Mr R A Chandiram | of Colombo or failing him |
| Mr N A Wickremasinghe | of Colombo or failing him |
| Mr T C Clark | of Dubai or failing him |
| Mr G Chapman | of Dubai or failing him |
| Mr N J Hopkins | of Dubai |

as my/our proxy to represent me/us and on my/our behalf at the Twenty Eighth Annual General Meeting of the Shareholders of SriLankan Airlines Limited to be held on 28 June 2006 at 9.00 a.m and at any adjournment thereof and at every poll which may be taken in consequence of the aforesaid meeting.

Signed this day of..... Two Thousand and Six.

.....
Signature

NOTE:

If no words are deleted or there is in the view of the proxy holder doubt (by reason of the way in which the instructions contained in the proxy have been completed) as to the way in which the proxy holder should vote, the proxy holder will vote as he thinks fit.

Instructions for Completion

1. Perfect the Form of Proxy after filling in legibly your full name and address, by signing in the space provided and filling in the date of signature.
2. The completed Form of Proxy should be deposited at the Registered Office of the Company at the under noted address not less than 48 hours before the time appointed for the holding of the meeting.

By Order of the Board



Mildred Peries

Company Secretary

SriLankan Airlines Limited

#22-01, East Tower

World Trade Centre

Colombo 1

01 June 2006