中国人民财产保险股份有限公司

PICC Property and Casualty Company Limited

2003

Annual Report

Company Profile

PICC Property and Casualty Company Limited (the "Company") is the largest property and casualty insurance company in China. The Company is a property and casualty insurance company established in July 2003 with The People's Insurance Company of China, later renamed and re-registered as PICC Holding Company ("PICC Holding") as its sole promoter. PICC Holding injected all of its commercial insurance operations, together with related assets and liabilities, into the Company by way of capital contribution. In November 2003,the Company became the first domestic financial enterprise to list overseas when the Company successfully listed on The Stock Exchange of Hong Kong Limited ("the Stock Exchange") through the issuance of 3,455,980,000 H Shares. The Company currently has a total share capital of 11,141,800,000 shares. American International Group, Inc. ("AIG") became a strategic investor of the Company in November 2003, and hold 9.9% of total share capital of the Company.

The Company is a leading property and casualty insurance company in China. The main product lines of the Company include motor vehicle insurance, commercial property insurance and homeowners insurance. The Company also has other insurance product lines such as cargo insurance and liability insurance. Since March 2003, the Company started to provide accidental injury insurance to customers.

*The Company's strategic target is to develop itself, in ten to fifteen years, into "**a modern, knowledge-based public property and casualty insurance company which is the market leader in China and ranks among the top property and casualty insurance companies in the world**". The Company has a corporate culture which emphasizes "**Practicality, Integrity, Devotion and Innovation**", and takes a "market-oriented and customer-centered" approach to its operations.*

*The Company has established the following strengths in its operations and management: **Strong Brand Recognition** - with 55 years of operating history, the "PICC" brand enjoys a prominent reputation in the domestic market and is also well-known in the international insurance market; **Leading Market Position** - the Company is the largest property and casualty insurance company in China and enjoys an undisputed leading position with a market share of 68% in 2003; **Extensive Network** - the Company has branches throughout the country forming a strong sales and service network; **Substantial Resources** - the Company has the largest customer base and business database in the domestic property and casualty insurance market.*

Contents

Financial Highlights

Summaries of the results and the assets and liabilities of the Company for each of the past four years are set out as follows:

RESULTS

	Year ended 31 December			
	2000	2001	2002	**2003**
	RMB million	*RMB million*	*RMB million*	***RMB million***
Turnover	43,621	47,949	50,571	**54,968**
Net premiums earned	32,140	34,521	36,381	**40,409**
Interest and dividend income	610	574	648	**690**
Net gains/(losses) on trading and non-trading securities	19	(10)	(645)	**260**
Net claims incurred	(22,158)	(23,632)	(26,634)	**(29,063)**
Amortisation of deferred acquisition costs	(1,282)	(1,229)	(1,694)	**(2,479)**
Insurance protection expense	(367)	(393)	(407)	**(468)**
Interest expense credited to policyholders' deposits	—	—	(54)	**(123)**
General and administrative expenses	(7,186)	(7,058)	(6,566)	**(6,903)**
Finance costs	—*	—*	(35)	**(35)**
Profit before unallocated income and expenses	1,776	2,773	994	**2,288**
Tax	(734)	(1,382)	(716)	**(837)**
Net profit	1,042	1,391	278	**1,451**

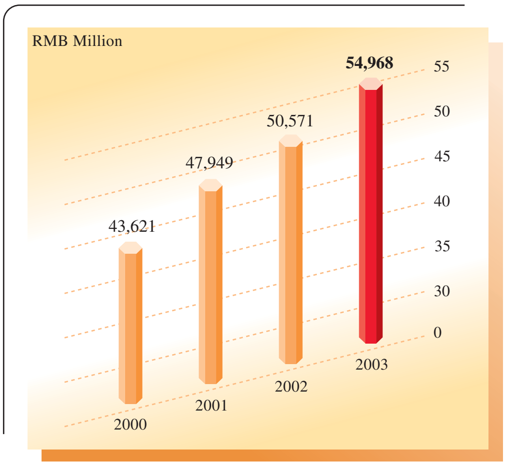
* Minimal amount

ASSETS AND LIABILITIES

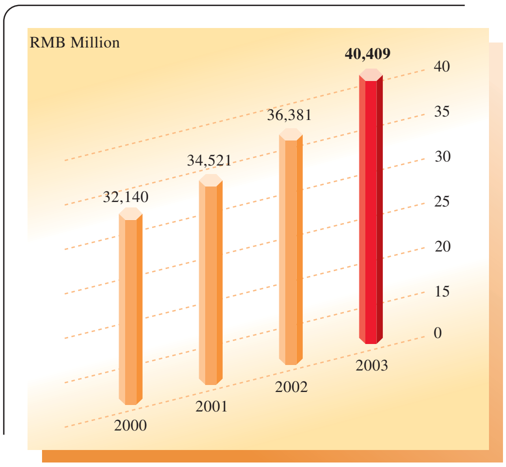
	31 December			
	2000	2001	2002	**2003**
	RMB million	*RMB million*	*RMB million*	***RMB million***
Total assets	59,310	63,612	71,626	**84,572**
Total liabilities	52,471	55,383	61,333	**65,815**
Net assets	6,839	8,229	10,293	**18,757**

Financial Highlights *(Continued)*

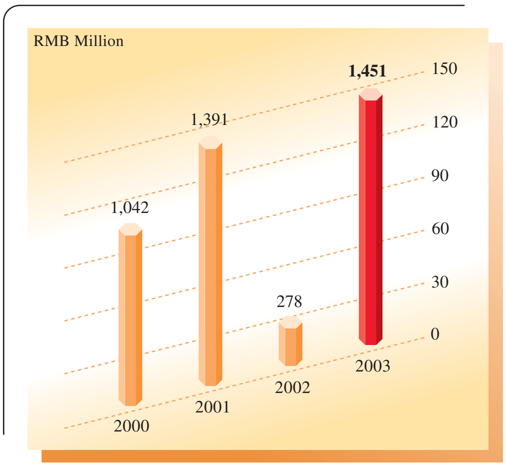
Turnover



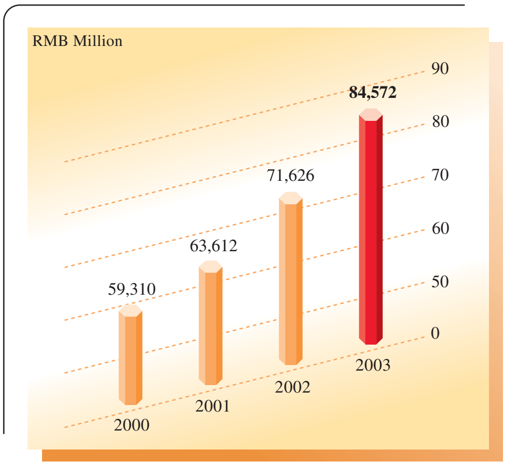
Net Premiums Earned



Net Profit



Total Assets



Chairman's Statement

Dear Shareholders,

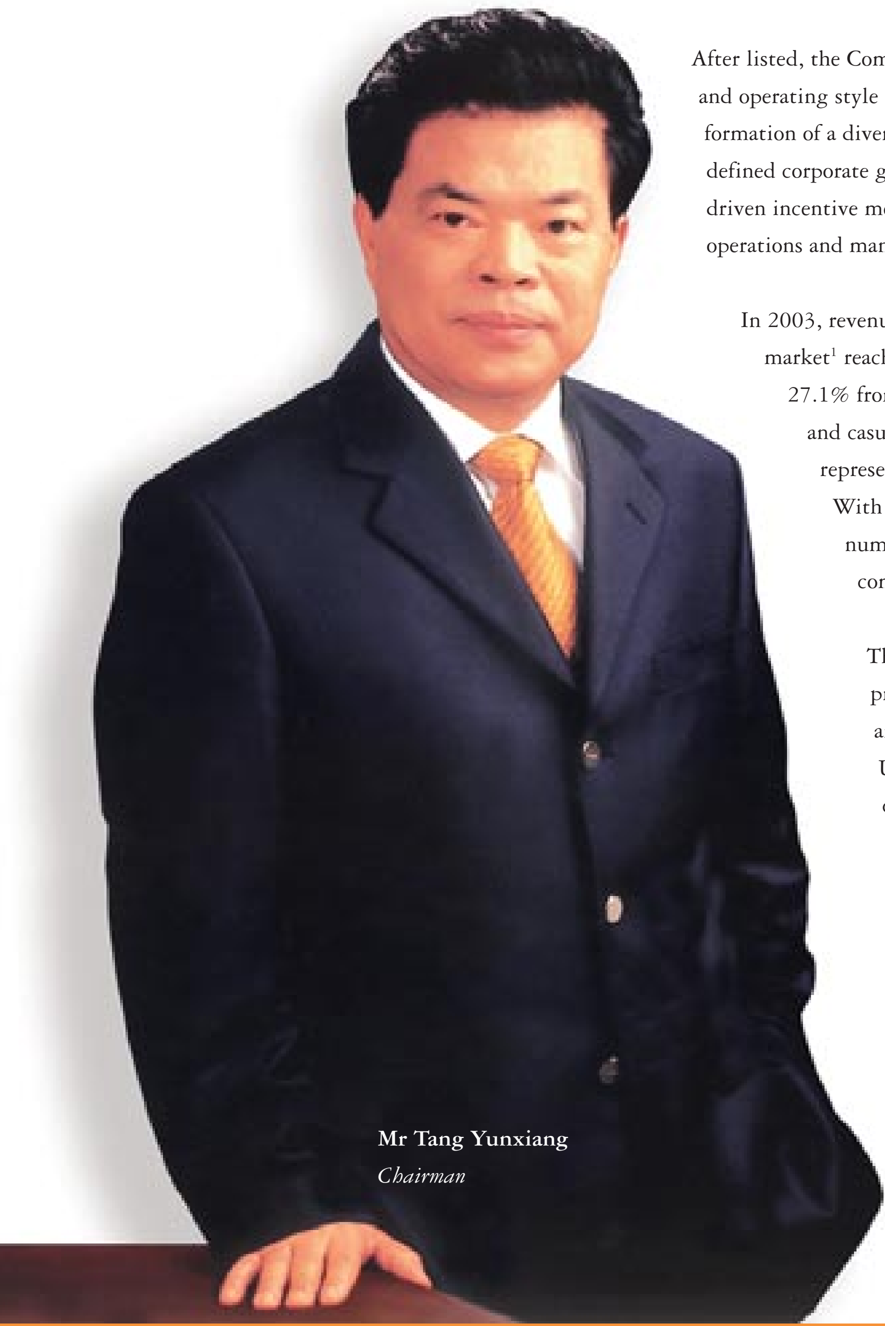
2003 was an extraordinary year for the Company.

With the arduous efforts of our management and staff and support from investors, the listing of the Company's H Shares was a huge success.The Company was named "China Equity Deal of the Year" by International Financing Review Asia and "The Best Newly-Listed Company in 2003" by AsiaMoney, evidencing the investors' recognition of the fundamentals, and their confidence in the prospects, of the Company. The Company's H Share was admitted as a constituent stock of the Hang Seng China Enterprises Index on 8 March 2004, highlighting the significance of the Company in international equity markets in the future.

After listed, the Company's business philosophy, organization structure and operating style underwent substantial changes, including the formation of a diversified shareholders structure, establishment of a defined corporate governance structure and implementation of a market-driven incentive mechanism, and the transparency in the Company's operations and management was further improved.

In 2003, revenue from insurance premiums of the PRC insurance market[1] reached RMB388.04 billion, representing an increase of 27.1% from the previous year, of which revenue from property and casualty insurance premiums reached RMB86.94 billion, representing an increase of 11.7% from the previous year. With the further opening of the PRC insurance market, the number of participants in the market increased and market competition intensified.

The Company had a market share[2] of 68% in 2003. Net premiums earned was RMB40.41 billion, representing an increase of 11.1% from the previous year. Underwriting profit[3] was RMB1,496 million, combined ratio was 96.3%, investment gain was RMB950 million, net profit was RMB1,451 million.



Mr Tang Yunxiang
Chairman

1. The PRC insurance market data is extracted from the information disclosed on the website of China Insurance Regulatory Commission (the "CIRC").
2. Calculation of the Company's market shares is made on the basis of the data disclosed on the CIRC website and the data of same categories maintained by the Company.
3. Underwriting profit is the difference of net premiums earned minus net claims incurred, amortization of deferred acquisition costs, insurance protection expense and general and administrative expenses.

In 2003, the Company implemented reforms in its motor vehicle insurance premium rates and policy terms. It introduced personalized products targeting different customers and differentiated pricing with respect to different risks, and promoted business structure adjustment and differentiated operations, emphasizing a profit-oriented approach to intrinsic growth, enabling the Company's business operations to become more responsive to the market, intensified and detail-oriented, and strengthening its market competitiveness.

In October 2003, the Company reorganized its operational structure to improve management process and enhance necessary skills. The Company altered its old, product line based management model to a customer and process driven structure, thus rationalizing its organization structure and streamlining staffing. The reorganization allowed the Company to improve its internal operating mechanisms and optimize its management processes. The Company established a personnel movement management mechanism and a sound personnel selection mechanism, providing a strong organizational support to the Company for its further development and reform.

The world economy in 2004 should maintain growth, with economic growth in Asia continuing to exceed that of other regions. The premium rate in the global property and casualty insurance market will maintain at a relatively high level. As a result, property and casualty insurance companies can attain relatively stable underwriting profits. With the rapid growth of the property and casualty insurance businesses in Asia, especially in new markets such as the PRC and India where growth is particularly strong, it is estimated that the rate of growth in premium in these regions in the following few years will exceed that in most of the OECD countries. The exploration by multinational insurance companies of new development opportunities in such region will result in a change in existing market competition in such region.

Currently, the PRC economy is undergoing rapid development. The automobile and real estate markets, import and export trade and investment in infrastructure are growing at a rapid pace. Such dynamics offer significant potential for the development of the property and casualty insurance sector. With further deepening of reform in the Chinese insurance market, participants in the market are increasingly changing their focus from scale expansion to speed, quality and profitability of their businesses, which will result in more rational market competition and reduced competition in premium rates. As premium rates for motor vehicle insurance rebound, profitability of the property and casualty insurance sector will improve. Implementing selective underwriting and strengthening claims management have also become the common objectives of most insurance companies.

Chairman's Statement *(Continued)*

"Some Opinion of the State Council on Promoting the Reform, Opening and Steady Growth of the Capital Market" promulgated by the State Council encourages insurance funds to invest directly and in a variety of forms in the capital markets. This will likely increase the number of channels available for investment of insurance funds and help insurance companies to increase flexibility in their investment management.

In 2004, the Company anticipates profitability to continue to improve and that growth in investment income and gradual growth in underwriting profit will be achieved. In order to maximize value for shareholders, the Company will continue to focus on profitability, underwriting quality and risk control, and endeavor to improve operating performance in 2004.

Refine the "three centers" (i.e. underwriting center, claims management center and finance center): The Company will focus on implementing its "three centers" in 2004. In accordance with the guiding principles of the "three centers", the Company will improve application of information technology and strengthen internal monitoring of the "three centers" so as to foster the formalization and standardization of the "three centers" structure across the Company.

Adjust business structure: The Company will refine its business structure, focusing in particular on motor vehicle insurance, in order to enhance underwriting profitability. It will also adjust its product structure, increasing products offered; effect selective underwriting in order to strictly control underwriting risks, and adjust resource allocation including implementation of differentiated policy on commissions.

Develop geographic pricing system: The Company will accelerate establishment of a differentiated pricing system for motor vehicle insurance based on geography. Under this system motor vehicle insurance premium rates will be set at the provincial branch office level according to risk profiles, cost structures and operating strategies of motor vehicle insurance in different regions so as to make prices more responsive to market forces.

Improve claims management: The Company will continue to standardize its claims management system through, unifying loss adjustment standards, broadening the applicability of the loss determination system, improving the mechanism for claims-related risk control and encouraging wider use of such system, and strengthening claim investigation and salvage capabilities.

Improve use of funds: The Company will improve its asset management system, formulate its funds allocation strategy and enhance its risk control to ensure that its investment portfolio will meet the needs of its business development, to take advantages of the recovery in the capital market, and to improve investment profitability.

Implement integrated information system: The Company will adopt an approach enhancing management on source information and strengthening information verification and control to improve its information management and build a high quality integrated information system allowing better management and overall application of data. The Company will endeavor to leverage its information resources to gain a competitive advantage in the market.

Enhance performance evaluations: The Company will develop a results-oriented performance evaluation system for employees, introducing key performance indicators, entering into contracts that set out performance targets, increasing the importance of profit in evaluating staff and establishing a market-driven salary system.

Increase cooperation with AIG: The Company will increase cooperation with AIG in relation to accidental injury and short-term health insurance products. The Company and AIG will also cooperate in areas such as product development, underwriting, claims management, distribution and reinsurance.

I believe that, with our firm customer base, experienced management team and excellent staff, the Company will be able to take advantage of opportunities provided by rapid growth in the PRC economy, the rising level of wealth and well-being in society, more rational market competition and the recovery in the capital market, to accelerate its development, to further enhance its core competitiveness and to create greater value for shareholders.

Tang Yunxiang
Chairman

Beijing, PRC
23 April 2004

求實
PRACTICALITY

Biographical Details of Directors, Supervisors and Senior Management

DIRECTORS

Tang Yunxiang, age 57, a senior economist, Chairman of the Board of Directors of the Company and General Manager of PICC Holding Company. Mr Tang joined The People's Insurance Company of China ("PICC") in 2000 as general manager. Mr Tang has extensive financial regulatory experience by working in the regulatory authorities of the PRC financial and insurance industries. He was previously vice chairman of the China Insurance Regulatory Commission, assistant president of the People's Bank of China, and the chairman of the Financial Industry Workers' Union. Mr Tang graduated from Shaoyang Normal College of Hunan Province and has 40 years of experience in business operation and management and an in-depth knowledge of the PRC financial and insurance industries.

Wang Yi, age 48, a senior economist, Vice Chairman of the Board of Directors, Executive Director, President and Chief Executive Officer of the Company. Mr Wang joined PICC in 1979 and was previously the deputy general manager of PICC's Ningbo branch, general manager of PICC's Hangzhou branch, general manager of PICC's Zhejiang branch and deputy general manager of PICC. Mr Wang graduated from Zhejiang Radio and Television University, majoring in political management, and from the Chinese Communist Party University, majoring in economic management. He has 25 years of operation and management experience in the PRC insurance industry.

Wang Yincheng, age 43, a senior accountant, Executive Director, Executive Vice President and Chief Financial Officer of the Company. Mr Wang joined PICC in 1982 and was previously the deputy general manager of the planning and finance department of PICC Property Insurance Company, general manager of PICC's Shenzhen branch and assistant general manager of PICC. Mr Wang graduated from Zhongnan University of Economics and Law with a doctorate degree in Economics. He has 22 years of experience in economic and financial management in the PRC insurance industry.

Liu Zhenghuan, age 54, a senior economist, Executive Director and Executive Vice President of the Company. Ms Liu joined PICC in 1984 and was previously the deputy manager and manager of the operations division of PICC's Anhui branch, deputy general manager and general manager of PICC's Anhui branch and general manager of PICC's Jiangsu branch. Ms Liu graduated from Fudan University with a master's degree in economics. She has 20 years of operation and management experience in the PRC insurance industry.

Fu Zhu, age 49, a senior economist, Executive Director, Executive Vice President and Secretary of the Board of Directors of the Company. Mr Fu joined PICC in 2000 as the general manager of its research and development center and planning and statistics department. He was previously the general manager of the research and development department of China Minsheng Banking Corp, Ltd. Mr Fu graduated from Shaanxi University of Finance and Economics with a master degree in economics. He has 22 years of experience in economic research and business operation and management.

Biographical Details of Directors, Supervisors and Senior Management *(Continued)*

Qiao Lin, age 60, a deputy researcher, Non-executive Director of the Company. Mr Qiao joined PICC in 1999 as deputy general manager. He was previously the vice chairman of the Shanghai Social Science Association and vice president of China Pacific Insurance Company. Mr Qiao is a deputy general manager of PICC Holding Company and graduated from Fudan University with a bachelor degree in Chinese studies. He has 36 years of experience in economic research and business administration.

Ding Yunzhou, age 51, a senior economist, Non-executive Director of the Company. Mr Ding joined PICC in 1977 and was previously the deputy general manager of PICC's international insurance department, chairman and general manager of China Insurance (UK) Company Limited, chief representative of PICC's London branch and assistant general manager and deputy general manager of PICC. He is a deputy general manager of PICC Holding Company. Mr Ding graduated from Dalian University of Foreign Languages and has 28 years of operation and management experience in the domestic and global insurance industries.

Zhou Shurui, age 51, a senior administrative engineer, Non-executive Director of the Company. Mr Zhou joined PICC in 1992 and was previously assistant general manager, deputy general manager and general manager of PICC's human resources department. He is a deputy general manager of PICC Holding Company. Mr Zhou graduated from the Hebei Normal University with a college diploma and a bachelor degree, and from a postgraduate program in banking at The Central University of Finance and Economics. He has 22 years of experience in management.

Christopher Cheng Wai-Chee, JP, age 56, Independent Non-executive Director of the Company. Mr Cheng is Chairman of USI Holdings Limited, Winsor Properties Holdings Limited and Wing Tai Corporation Limited. He is a director of NWS Holdings Limited, New World China Land Limited and DBS Bank (Hong Kong) Limited. Mr Cheng plays an active role in the public services. He is chairman of the Standing Committee on Judicial Salaries and Conditions of Service of the Hong Kong Government, and a member of the Exchange Fund Advisory Committee of the Hong Kong Government, a non-executive director of Securities and Futures Commission, a steward of the Hong Kong Jockey Club, a member of Directorate of Hong Kong Trade Development Council. Mr Cheng graduated from University of Notre Dame, Indiana, U.S.A. with a bachelor degree in business administration, and from Columbia University, U.S.A. with a master degree in business administration. He was appointed as Independent Non-executive Director of the Company in July 2003.

Peter Wong Tung-Shun, JP, age 52, Independent Non-executive Director of the Company. Mr Wong is Chief Executive Officer, Greater China and Director of Standard Chartered Bank. He is Chairman of the Hong Kong Association of Banks, a member of the Exchange Fund Advisory Committee, the Banking Advisory Committee and the Deposit-taking Companies Advisory Committee. He is also a non-official member of the Economic and Employment Advisory Committee and an Investment Promotion Ambassador of the Hong Kong Government, and Vice President for the Hong Kong Institute of Bankers. Mr Wong was Chairman of the Hong Kong Interbank Clearing Limited, a member of the Risk Management Committee of the Hong Kong Exchanges and Clearing Limited, a Director of the Hong Kong Mortgage Corporation and a member of the Consumer Council. He was a founder and director of Credit Information Services Limited. Mr Wong graduated from Indiana University, Bloomington, U.S.A. with a bachelor degree in computer science, a master degree in business administration specializing in marketing and finance, and a master degree majoring in computer science information systems. He was appointed as Independent Non-executive Director of the Company in October 2003.

Lu Zhengfei, age 41, a professor and supervisor of doctoral students, Independent Non-executive Director of the Company. Mr Lu is the head of the Department of Accounting, Guanghua School of Management, Peking University, a consultant to the accounting rules committee set up by the Ministry of Finance, and a member of Chinese Tax Association, Chinese Accounting Association, Chinese Costing Research Institute, and a standing committee member of Chinese Accounting Professors Association and Chinese Youth Finance and Costing Research Institute. He is also a guest editor of Accounting Research, and a member of the editorial committee of Auditing Research. He was elected into the "100 Outstanding Persons' Research Program" as a man of talent in social science theories in Beijing in 2001. Mr Lu graduated from Nanjing University with a doctorate degree in economics, and completed the post-doctoral research on economics (accounting) at Renmin University of China. He was appointed as Independent Non-executive Director of the Company in February 2004.

SUPERVISORS

Deng Zhaoyu, age 57, Chairman of the Supervisory Committee of the Company. Mr Deng joined PICC in 2002 as deputy general manager. He was previously engaged in technological and management work in enterprises under the control of the Chinese Aviation Industrial Ministry, and was later transferred to organizations within the Central Government where he served as deputy director-general of the local cadre bureau of the organization department of the Communist Party's Central Committee, director-general of the cadre education bureau and minister of the organization department of the Communist Party's central finance working committee. Mr Deng obtained a college diploma in political management, and graduated from the China Lawyers' Correspondence Centre. He has 36 years of extensive experience in management.

Tang Wei, age 56, a senior economist, Supervisor of the Company. Mr Tang joined PICC in 1989 and was previously the general manager of PICC's auditing department. Mr Tang graduated from Harbin Normal College with a college diploma, from Zhongnanhai University with a bachelor degree, and from the China Lawyers' Correspondence Centre with a college diploma in law. He has 24 years of management experience.

Liu Qilong, age 56, a senior economist, Supervisor of the Company. Mr Liu joined PICC in 1984 and was previously a manager of domestic business department, city business department and audit department, the general manager of comprehensive affair department and the manager of human resources division, as well as a director of PICC's disciplinary and supervisory office. Mr Liu graduated from Submarine Naval College of the Chinese People's Liberation Army with a college diploma. He has 20 years of experience in the PRC insurance industry.

Biographical Details of Directors, Supervisors and Senior Management *(Continued)*

SENIOR OFFICERS

Guo Shengchen, age 49, a university graduate and a senior economist, Executive Vice President of the Company. Mr Guo joined PICC in 1984 and was previously the assistant general manager, deputy general manager and general manager of PICC's Beijing branch. He has 30 years of operation and management experience in the PRC financial and insurance industries.

Zhao Shuxian, age 52, a university graduate and a senior economist, Executive Vice President of the Company. Ms Zhao joined PICC in 1978 and was previously deputy general manager of the operations department and general manager of the special risk insurance department of PICC Property Insurance Company and chief representative of PICC's European Representative office. Ms Zhao has 26 years of operation and management experience in the PRC insurance industry.

Jia Haimao, age 50, a senior economist, Executive Vice President of the Company. Mr Jia joined PICC in 1984 and was the deputy general manager and general manager of PICC's motor vehicle insurance department. Mr Jia has 20 years of operation and management experience in the PRC insurance industry.

Li Yuquan, age 39, Ph.D, an associate professor, Executive Vice President of the Company. Mr Li joined PICC in 1994, and was the deputy general manager of PICC's marketing department and general manager of its legal department. He has 15 years of experience in research in PRC insurance law research and in the operation and management in the PRC insurance industry.

Wang He, age 47, a senior economist, Executive Vice-President of the Company. Mr Wang holds a master degree. He joined PICC in 1988 and was manager of the operation department of PICC's Fujian branch, deputy general manager of its Xiamen branch and executive deputy director of PICC's products development center. He has 16 years of operation and management experience in the PRC insurance industry.


誠信
INTEGRITY

Management's Discussion and Analysis of Financial Condition and Results of Operations

Mr Tang Yunxiang
Chairman

Mr Wang Yi
Vice Chairman, Executive Director, President and Chief Executive Officer

Mr Wang Yincheng
Executive Director, Executive Vice President and Chief Financial Officer

Ms Liu Zhenghuan
Executive Director and Executive Vice President

Mr Fu Zhu
Executive Director, Executive Vice President and Secretary of the Board

The following discussion and analysis should be read in conjunction with the audited financial statements together with the accompanying notes contained on page 58 to page 108 of this annual report. The financial data referred to below are extracted from the audited accountants' report.

OVERVIEW

The Company is a leading property and casualty insurance company in the PRC providing a broad range of property and casualty insurance and accidental injury insurance products for customers. In 2003, the market share of the Company was 68%.

The following table sets forth the net premiums earned, underwriting profit, net profit and total assets of the Company for the periods indicated.

	Year ended 31 December	
	2003	2002
	(RMB in millions)	
Net premiums earned	**40,409**	36,381
Underwriting profit	**1,496**	1,080
Net profit	**1,451**	278
Total assets	**84,572**	71,626

RESULTS OF OPERATIONS

Profitability of the Company improved in 2003, with a steady increase in turnover, strong growth in underwriting profit, driven by a decline in combined ratio and a significant increase in investment income. Net profit exceeded the Company's profit forecast set out in the Company's prospectus.

The following table sets forth selected financial information shown as percentages of net premiums earned and certain financial ratios for the periods indicated.

	Year ended 31 December	
	2003	2002
	(%)	
Net premiums earned	100.0	100.0
Net claims incurred	(71.9)	(73.2)
Amortization of deferred acquisition costs	(6.1)	(4.7)
Insurance protection expense	(1.2)	(1.1)
General and administrative expenses	(17.1)	(18.0)
Underwriting profit	3.7	3.0
Interest and dividend income	1.7	1.8
Net gains/(losses) on trading and non-trading securities	0.6	(1.8)
Profit from ordinary activities before taxation	5.7	2.7
Taxation	(2.1)	(2.0)
Net profit	3.6	0.8
Loss ratio	71.9%	73.2%
Expense ratio[4]	24.4%	23.8%
Combined ratio	96.3%	97.0%

4. The expense ratio for 2002 was different from 23.9% as set out in the prospectus because general and administrative expenses do not include RMB35 million in the finance costs.

Segment Information

The following table sets forth the net premiums earned, net claims incurred and amortization of deferred acquisition costs for each segment as a percentages of the respective combined amounts for the periods indicated.

	Year ended 31 December	
	2003	2002
	(%)	
Net premiums earned		
Motor vehicle insurance	**66.6**	65.8
Commercial property insurance	**15.9**	17.4
Homeowners insurance	**2.6**	3.0
Other insurance	**14.9**	13.8
Total	**100.0**	100.0
Net claims incurred		
Motor vehicle insurance	**74.4**	70.2
Commercial property insurance	**11.3**	15.5
Homeowners insurance	**1.2**	1.3
Other insurance	**13.1**	13.0
Total	**100.0**	100.0
Amortization of deferred acquisition costs		
Motor vehicle insurance	**82.8**	89.7
Commercial property insurance	**5.0**	6.0
Homeowners insurance	**5.4**	6.8
Other insurance	**6.8**	(2.5)
Total	**100.0**	100.0

TURNOVER

Turnover of the Company was RMB54,968 million in 2003, representing an increase of 8.7% over RMB50,571 million in 2002. The increase in turnover was primarily due to an RMB3,858 million increase in turnover from the motor vehicle insurance segment, and also due in part to an RMB1,745 million increase in turnover from accidental injury insurance, which the Company began selling in March 2003.

NET PREMIUMS EARNED

Net premiums earned of the Company was RMB40,409 million in 2003, representing an increase of 11.1% over RMB36,381 million in 2002. This increase in net premiums earned was primarily due to the increase in turnover and a decrease in reinsurance premiums ceded. These changes were partially offset by an increase in the change in unearned premium reserves. The decrease in reinsurance premiums ceded to RMB11,116 million, or 20.2% of turnover, for 2003 from RMB13,441 million, or 26.6% of turnover, for 2002 was primarily due to a decline in the statutory reinsurance rate to 15% in 2003 from 20% in 2002 according to the WTO Accession of China. The increase of net unearned premium reserves in 2003 compared with in 2002 was due primarily to the increase in net premiums written resulting from the increase in turnover and the decrease in reinsurance premiums ceded.

INTEREST AND DIVIDEND INCOME

Interest and dividend income of the Company was RMB690 million in 2003, representing an increase of 6.5% over RMB648 million in 2002. This increase was primarily due to increases in interest income from trading and non-trading securities and interest income from bank deposits of RMB38 million and RMB78 million, respectively. This increase was partially offset by an RMB74 million decrease in dividend income from trading and non-trading securities. The decrease in dividend income was due primarily to a lack of dividend distributions for the year 2003 from the mutual funds in which the Company invested. The increase in interest income from bank deposits was due primarily to an RMB10,651 million increase in bank deposits as a result of increase in turnover and in funds raised through the initial public offering of shares in the Company. The increase in interest income from trading and non-trading securities was primarily due to an increase in purchase of securities by the Company in 2003 under re-purchase arrangement.

NET GAIN/(LOSSES) ON TRADING AND NON-TRADING SECURITIES

Net gain of the Company on trading and non-trading securities was RMB260 million in 2003, representing an increase of RMB905 million over a net loss of RMB645 million in 2002. This increase was primarily due to an RMB990 million increase in unrealized gains on mutual funds held for trading purposes, which was partially offset by an RMB122 million decrease in realized gains on debt securities held for trading purposes.

NET CLAIMS INCURRED

Net claims incurred of the Company was RMB29,063 million in 2003, representing an increase of 9.1% over RMB26,634 million in 2002. Loss ratio decreased to 71.9% in 2003 from 73.2% in 2002. The increase in net claims incurred largely reflected an increase of 15.6% in net claims incurred from the motor vehicle insurance segment to RMB21,618 million in 2003 from RMB18,701 million in 2002. This increase in net claims incurred from the motor vehicle insurance segment was primarily due to a 32.4% increase in the number of claims filed to approximately 5.68 million in 2003 from approximately 4.29 million in 2002. The increase in net claims incurred from the motor vehicle insurance segment was partially offset by a decrease in net claims incurred from the commercial property insurance segment to RMB3,285 million in 2003 from RMB4,127 million in 2002. This decrease was primarily due to an increase in the quality of the commercial property insurance portfolio as a result of imposing more stringent policy terms.

AMORTIZATION OF DEFERRED ACQUISITION COSTS

Amortization of deferred acquisition costs of the Company was RMB2,479 million in 2003, representing an increase of 46.3% over RMB1,694 million in 2002. This increase was primarily due to an RMB264 million increase in commissions paid to insurance intermediaries in 2003 compared with 2002 and an RMB440 million decrease in reinsurance commissions receivable.

INSURANCE PROTECTION EXPENSE

Insurance protection expense of the Company was RMB468 million in 2003, representing an increase of 15.0% over RMB407 million in 2002. This increase was primarily due to an increase in retained premiums.

INTEREST EXPENSE CREDITED TO POLICYHOLDERS' DEPOSITS

Interest expense of the Company credited to policyholders' deposits was RMB123 million in 2003, representing a large increase over RMB54 million in 2002. This increase was primarily due to an RMB2,235 million increase, compared to 2002, in reserves for the Golden Bull homeowners insurance product to RMB6,142 million as of 31 December 2003.

GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses of the Company was RMB6,903 million in 2003, representing an increase of 5.1% over RMB6,566 million in 2002. This increase was primarily due to increase in depreciation and amortization, provision for doubtful accounts and operating lease charges. The increase of RMB128 million in depreciation and amortization was primarily due to the revaluation of the assets as of 30 September 2002. The increase of RMB95 million in operating lease charges consist primarily of lease charges according to the building and automobile leases agreements entered into by the Company and PICC Holding Company in connection with the Company's Reorganisation. Provision for doubtful accounts increased RMB55 million primarily due to increase in premiums receivable but overdue for more than three months.

PROFIT FROM ORDINARY ACTIVITIES BEFORE TAXATION

Profit from ordinary activities before taxation was RMB2,288 million in 2003, representing an increase of 130.2% over RMB994 million in 2002. This increase was primarily due to an RMB905 million increases in net gain on trading and non-trading securities and an increase of 11.1% in net premiums earned to RMB40,409 million in 2003 from RMB36,381 million in 2002. The increase was partially offset by an increase of 9.1% in net claims incurred.

TAXATION

Taxation expense increased by 16.9% to RMB837 million in 2003 from RMB716 million in 2002. This increase was primarily due to an increase of 130.2% in profit from ordinary activities before taxation in 2003 compared with 2002, and a decrease of non-taxable income to RMB59 million in 2003 from RMB76 million in 2002, which more than offset the decrease in taxes payable on non-deductible expenses from RMB445 million in 2002 to RMB141 million in 2003. The decrease in non-deductible expenses was the result of certain additional deductions from personnel expenses made available to the Company beginning from 1 January 2003 with the consent given by the Ministry of Finance and the State Administration of Taxation in a circular.

As a result of the foregoing, the Company's effective tax rate decreased to 36.6% in 2003 from 72.0% in 2002.

NET PROFIT

As a result of the foregoing, net profit increased to RMB1,451 million in 2003 from RMB278 million in 2002. Net profit exceeded profit forecast for 2003 set out in the Company's prospectus. Basic earnings per share[5] was RMB0.171.

5. See Note 13 to financial statements.

COMBINED RATIO

The Company's combined ratio decreased to 96.3% in 2003 from 97.0% in 2002, primarily due to a decrease in loss ratio to 71.9% in 2003 from 73.2% in 2002, which more than offset the increase in expense ratio. The decrease in loss ratio was primarily due to the decrease in loss ratio for the commercial property insurance segment and the liability insurance segment by 14.0 percentage points and 10.6 percentage points, respectively, in 2003, which more than offset the 2.1 percentage points increase in loss ratio for the motor vehicle insurance segment.

RESULTS OF SEGMENT OPERATIONS

Motor Vehicle Insurance

	Year ended 31 December	
	2003	2002
	(RMB in million, except %)	
Turnover	**35,294**	31,436
Net premiums earned	**26,930**	23,928
Net claims incurred	**(21,618)**	(18,701)
Amortization of deferred acquisition costs	**(2,053)**	(1,520)
Insurance protection expense	**(323)**	(269)
Segment profit before unallocated income and expenses	**2,936**	3,438
Loss ratio	**80.3%**	78.2%
Segment expense ratio[6]	**8.8%**	7.5%
Segment combined ratio	**89.1%**	85.7%

Turnover from the motor vehicle insurance segment increased 12.3% to RMB35,294 million in 2003 from RMB31,436 million in 2002. This increase was primarily due to an increase in the number of motor vehicles covered by the motor vehicle insurance policies. There were approximately 18.06 million motor vehicles covered by the insurance policies the Company sold in 2003, representing an increase of 2.07 million motor vehicles over 2002. This increase was reduced by a decrease in the average premium rates caused by increased competition in motor vehicle insurance and the deregulation of premium rates for motor vehicle insurance by the China Insurance Regulatory Commission (the "CIRC") as of 1 January 2003.

Net premiums earned from the motor vehicle insurance segment increased 12.6% to RMB26,930 million in 2003 from RMB23,928 million in 2002. This increase was primarily due to the increase in turnover and the decrease in reinsurance premiums ceded, which more than offset the increase in the change in net unearned premium reserves.

6 Since general and administrative expenses are not allocated to individual business segments, segment expense ratio and segment combined ratio are derived without taking into account the aforementioned expenses.

Net claims incurred from the motor vehicle insurance segment increased 15.6% to RMB21,618 million in 2003 from RMB18,701 million in 2002 primarily due to a 32.4% increase in the number of claims filed to approximately 5.68 million in 2003 from approximately 4.29 million in 2002, due to an increase in the number of motor vehicles covered by the motor vehicle insurance policies, as well as an increase in the accident rate. The Company believes the increase in the accident rate is due to factors such as increasing number of new drivers in the PRC without corresponding road improvement to accommodate increasing volume of traffic.

As a result primarily of the foregoing and the decrease in the average premium rates, the loss ratio for the motor vehicle insurance segment increased to 80.3% in 2003 from 78.2% in 2002.

Amortization of deferred acquisition costs from the motor vehicle insurance segment increased 35.1% to RMB2,053 million in 2003 from RMB1,520 million in 2002. The increase was due to a decrease in reinsurance commissions received by the Company and an increase in the salary of underwriting personnel.

Insurance protection expense from the motor vehicle insurance segment increased 20.1% to RMB323 million in 2003 from RMB269 million in 2002 due to an increase in retained premiums.

Due to an increase in amortization of deferred acquisition costs and an increase in insurance protection expense, the segment expense ratio for the motor vehicle insurance segment increased to 8.8% in 2003 from 7.5% in 2002.

As a result of the foregoing, profit before unallocated income and expenses from the motor vehicle insurance segment decreased 14.6% to RMB2,936 million in 2003 from RMB3,438 million in 2002.

Commercial Property Insurance

	Year ended 31 December	
	2003	2002
	(RMB in million, except %)	
Turnover	8,090	8,744
Net premiums earned	6,437	6,346
Net claims incurred	(3,285)	(4,127)
Amortization of deferred acquisition costs	(125)	(101)
Insurance protection expense	(59)	(67)
Segment profit before unallocated income and expenses	2,968	2,051
Loss ratio	51.0%	65.0%
Segment expense ratio	2.9%	2.6%
Segment combined ratio	53.9%	67.6%

Turnover from the commercial property insurance segment decreased 7.5% to RMB8,090 million in 2003 from RMB8,744 million in 2002 primarily due to a decrease in the average premium rates resulting from more intense market competition and due to the Company practising more selective underwriting and exiting from certain high risk customers.

Net premiums earned from the commercial property insurance segment increased 1.4% to RMB6,437 million in 2003 from RMB6,346 million in 2002 primarily due to a decrease in the ratio of reinsurance premiums ceded to gross premiums written and an increase in turnover.

Net claims incurred from the commercial property insurance segment decreased 20.4% to RMB3,285 million in 2003 from RMB4,127 million in 2002 and the loss ratio for that segment improved to 51.0% in 2003 from 65.0% in 2002. The decrease in net claims incurred was primarily due to an improvement in the quality of the Company's commercial property insurance portfolio due to the implementation of selective underwriting practices coupled with the use of more stringent policy terms. The measures led to a number of large customers with relatively high claim rate not renewing in 2003. In addition, the Company also successfully reduced net loss, in particular the number of significant claims, by strictly controlling policy terms to limit the scope of the liability and by improving the management of exposure to catastrophe losses. The decrease in net claims incurred was significantly larger than the decrease in net premiums earned, resulting in an improvement in the loss ratio for the commercial property insurance segment in 2003.

Amortization of deferred acquisition costs from the commercial property insurance segment increased 23.8% to RMB125 million in 2003 from RMB101 million in 2002 primarily due to an increase in commissions paid to insurance intermediaries and a decrease in reinsurance commission received by the Company.

Insurance protection expense from the commercial property insurance segment decreased 11.9% to RMB59 million in 2003 from RMB67 million in 2002.

As the increase in amortization of deferred acquisition costs more than offset the decrease in insurance protection expense, the segment expense ratio for the Company's commercial property insurance segment increased to 2.9% in 2003 from 2.6% in 2002.

As a result of the foregoing, profit before unallocated income and expenses from the commercial property insurance segment increased 44.7% to RMB2,968 million in 2003 from RMB2,051 million in 2002.

Homeowners Insurance

	Year ended 31 December	
	2003	2002
	(RMB in million, except %)	
Turnover	1,425	1,642
Net premiums earned	1,045	1,105
Net claims incurred	(340)	(351)
Amortization of deferred acquisition costs	(134)	(116)
Interest and dividend income	26	29
Net gains/(losses) on trading and non-trading securities	64	(83)
Interest expense credited to policyholder' deposits Homeowners	(123)	(54)
Insurance protection expense	(17)	(14)
Segment profit before unallocated income and expenses	521	516
Loss ratio	32.5%	31.8%
Segment ratio	14.4%	11.8%
Segment combined ratio	46.9%	43.6%

Turnover from the homeowners insurance segment decreased 13.2% to RMB1,425 million in 2003 from RMB1,642 million in 2002. The decrease was due to an increase in the number of market participants and a corresponding decline in the market share of the Company. Some home loan insurance customers also prepaid their loans in 2003.

Net premium earned from the homeowners insurance segment decreased 5.4% to RMB1,045 million in 2003 from RMB1,105 million in 2002. This decrease was primarily due to a decrease in turnover.

Net claims incurred from the homeowners insurance segment decreased 3.1% to RMB340 million in 2003 from RMB351 million in 2002. Loss ratio for that segment increased from 31.8% in 2002 to 32.5% in 2003. Net premiums earned decreased at a greater rate than that of net claims incurred, resulting in a slight increase in loss ratio.

Amortization of deferred acquisition costs from the homeowners insurance segment increased 15.5% to RMB134 million in 2003 from RMB116 million in 2002. This increase was primarily due to an increase in salary of homeowners insurance segment related personnel and a decrease in reinsurance commission.

Insurance protection expense from the homeowners insurance segment increased to RMB17 million in 2003 from RMB14 million in 2002.

Due to the increase in amortization of deferred acquisition costs, the segment expense ratio for the homeowners insurance segment increased to 14.4% in 2003 from 11.8% in 2002.

Interest expense credited to policyholders' deposits from the homeowners insurance segment increased 127.8% to RMB123 million in 2003 from RMB54 million in 2002. This increase was due to the launch of the Golden Bull homeowners insurance product in December 2001. As the product had just been launched at the end of 2001, virtually no interest expenses were incurred in the six months ended 30 June 2002. Therefore the interest expense credited to policyholders' deposits in 2002 was relatively low.

As a result of the foregoing, profit before unallocated income and expenses from the homeowners insurance segment increased 1.0% to RMB521 million in 2003 from RMB516 million in 2002.

Other insurance

The other insurance segment includes cargo insurance, liability insurance, accidental injury insurance, aviation insurance, construction insurance, hull insurance as well as certain other insurance product lines.

	Year ended 31 December	
	2003	2002
	(RMB in million, except %)	
Turnover		
Cargo insurance	2,657	2,966
Liability insurance	2,406	2,752
Accidental injury insurance	1,745	
Other insurance	3,351	3,031
Total	10,159	8,749
Net premiums earned		
Cargo insurance	2,314	2,248
Liability insurance	2,116	1,817
Accidental injury insurance	514	—
Other insurance	1,053	937
Total	5,997	5,002
Net claims incurred	(3,820)	(3,455)
Amortization of deferred acquisition costs	(167)	43
Insurance protection expense	(69)	(57)
Segment profit before unallocated income and expenses	1,941	1,533
Loss ratio	63.7%	69.1%
Segment expense ratio	3.9%	0.3%
Segment combined ratio	67.6%	69.4%

Turnover from the other insurance segment increased 16.1% to RMB10,159 million in 2003 from RMB8,749 million in 2002. This increase was primarily due to the turnover of RMB1,745 million from accidental injury insurance, which the Company began selling in March 2003. The Company's accidental injury insurance is expected to achieve continuous growth by making full use of its extensive distribution network and strong brand recognition.

Net premiums earned from the other insurance segment increased 19.9% to RMB5,997 million in 2003 from RMB5,002 million in 2002. This increase was primarily due to a decrease of RMB98 million in reinsurance premiums ceded and a decrease in change in net unearned premium reserves resulting in an increase of RMB246 million in net premiums earned from liability insurance.

Net claims incurred from the other insurance segment increased 10.6% to RMB3,820 million in 2003 from RMB3,455 million in 2002. The increase in net claims incurred was primarily due to an increase of RMB106 million in net claims incurred from cargo insurance. The increase in net claims incurred from cargo insurance was primarily due to the occurrence of a large loss in 2003 resulting from the sinking of a cargo ship.

Amortization of deferred acquisition costs from the other insurance segment was RMB167 million in 2003, with a reversal of RMB43 million in 2002. This change was primarily due to an increase in commissions paid to insurance intermediaries and a decrease in reinsurance commissions received.

Insurance protection expense from the other insurance segment increased 21.1% to RMB69 million in 2003 from RMB57 million in 2002. This increase was primarily due to an increase in retained premiums.

As a result of the foregoing, profit before unallocated income and expenses from the other insurance segments increased 26.6% to RMB1,941 million in 2003 from RMB1,533 million in 2002.

LIQUIDITY

The principal source of liquidity has been cash provided by operating activities, mainly cash from insurance premiums received. Additional liquidity sources include interest and dividend income from investments, proceeds from matured investments, disposal of assets and financing activities.

Liquidity capital is used principally for claim payments and other obligations under outstanding insurance policies, capital expenditures, operating expenses, and tax payments and dividend payment and investment needs. The need for liquidity is generally affected by the timing, frequency and severity of losses under outstanding policies. Catastrophic events, the timing, frequency and effect of which are inherently unpredictable may increase the need for liquidity.

The Company has signed with China Development Bank on 10 October 2003 a subordinated loan agreement, which amounts to RMB2 billion. This loan is unsecured and the interest is calculated on the basis of 90% to 110% of the 5 year lending rate fixed by the People's Bank of China. The loan matures in November 2023.

The Company obtained a 10-year revolving credit facility from China Development Bank for up to RMB10 billion. Each drawdown made under this facility is repayable within one year. As of the date of this annual report, no amount has been drawn down under the facility.

Management's Discussion and Analysis of Financial Condition and Results of Operations *(Continued)*

CASH FLOW

	Year ended 31 December	
	2003	2002
	(RMB in million)	
Net cash from operating activities	7,559	5,145
Net cash used in investing activities	(9,222)	(7,417)
Net cash generated from financing activities	8,038	2,735
Net increase in cash and cash equivalent	6,375	463

Cash flows from operating activities constitute a principal source of liquidity. Net cash generated from operating activities was RMB7,559 million in 2003, an increase of 46.9% from 2002. The increase was primarily due to unearned premium reserves increased by 8.44%, income tax paid for 2003 decreased 97.9% compared with 2002, the decrease rate of premium receivables for 2003 decreased 49.3% compared with 2002, and the increase in reinsurance recoverable on unpaid losses was smaller in 2003 than in 2002. On the other hand, increase in loss and LAE reserve was reduced by 66.7% in 2003 than in 2002, partially offset by a net gain of RMB260 million in 2003 in trading and non-trading securities compared with a net loss of RMB645 million in 2002.

Net cash used by the Company in investing activities increased RMB1,805 million to RMB9,222 million in 2003 from 2002. The increase in net cash used in investing activities in 2003 was primarily due to an increase of RMB10,891 million in funds used by the Company for placement of deposits with banks with original maturity of more than three months and other balances with banks, and an increase of RMB2,643 million in funds used for purchasing trading and non-trading securities. The increase was partially offset by increase of RMB6,430 million in the proceeds of sale of trading and non-trading securities and RMB5,844 million received from mature bank deposits of more than three months.

Net cash generated from financing activities was RMB8,038 million in 2003 and RMB2,735 million in 2002. The increase was primarily due to the receipt of proceeds of RMB5,610 million from the initial public offering of the Company and from a subordinate loan of RMB2 billion arranged in 2003 for the purpose of improving liquidity.

Cash and cash equivalents of the Company as of 31 December 2003 was RMB18,004 million, representing an increase of 54.8% over that in 2002.

WORKING CAPITAL

The Company typically generates substantial positive cash flow from operating activities because it generally receives insurance premiums on policies it underwrites before it makes loss payments on claims made under such policies. Such cash flows from operating activities have met the Company's working capital requirements in the past. Therefore, save as the subordinated loan and credit facility mentioned above, the Company does not obtain working capital by borrowings.

The Company expects to fund working capital needs in the future largely from cash generated from operating activities. Taking into account the net proceeds of the global offering and cash generated from other sources, the Directors are of the opinion that the Company has sufficient working capital for its present requirements.

CAPITAL EXPENDITURE

The capital expenditures have primarily been for property construction, acquisition of motor vehicles and the development of our information systems. Capital expenditure for the year 2003 was RMB1,696 million.

Since the office space and facilities in the headquarters of the Company have failed to meet development needs, the Board of Directors has approved the resolution relating to the construction of a new headquarters building. The total investment of the construction is estimated to be RMB1,500 million.

The Company believes it has sufficient source of capital to fully satisfy any capital expenditure plan and daily working capital requirements.

SOLVENCY MARGIN REQUIREMENT

The Company is subject to a number of the CIRC's regulations regarding financial operations, including maintaining a stipulated solvency margin, complying with 11 regulatory benchmarks and providing for certain funds and reserves.

Pursuant to relevant insurance laws and regulations in the PRC, the Company is required to maintain a solvency margin that exceeds the minimum statutory level of RMB7,018 million in 2003. The actual solvency margin calculated pursuant to the CIRC's regulations was RMB9,014 million and solvency margin adequacy rate was 128.4% as at 31 December 2003.

Pursuant to the CIRC regulations, if an insurance company fails to meet 4 of the 11 benchmarks regarding solvency, the CIRC has the right to demand an explanation and investigate into the reasons for not meeting the requirements. In 2003, fewer than four of such benchmarks were not met by the Company.

PREMIUM TO CAPITAL RATIO AND OTHER INSURANCE RATIOS

The premium to capital ratio is the ratio of retained premiums of a property and casualty insurance company in any financial year to the sum of its paid-in capital, capital reserves, surplus reserves and public welfare funds. Pursuant to the amended Insurance Law, this premium to capital ratio may not exceed 4 times for any property and casualty insurance company in any financial year. The premium to capital ratio for 2003 was 2.96 times[7].

As of 31 December 2003, the gearing ratio[8] was 77.8%, representing a decrease of 8.8 percentage points from 85.6% in 2002.

7 Calculated according to the PRC Accounting Regulations for Financial Institutions.

8 Gearing ratio is represented by total liabilities (excluding subordinated loan) divided by total assets.

CONTINGENT LIABILITIES

Owing to the nature of the insurance business, the Company is involved in legal proceedings in the ordinary course of business, including being the plaintiff or the defendant in litigation and arbitration. Such legal proceedings mostly involve claims on the Company's insurance policies. While the outcomes of such contingencies, lawsuits or other proceedings cannot be determined at present, the Company believes that any resulting liabilities will not have a material adverse effect on the financial position or operating results of the Company.

REGULATION ON USE OF FUNDS

The use of funds in Renminbi and foreign currencies by insurance companies in the PRC is subject to the regulatory control by regulatory bodies of the PRC. Therefore, the Company does not use any financial instruments for hedging purposes.

EMPLOYEES

As of 31 December 2003, the Company had 63,645 employees. Personnel expenses[9] in the year ended 31 December 2003 was RMB3,253 million.

The Company makes contributions to retirement plans and social medical insurance plans for its employees. The Company enhances the performance and efficiency of employees by providing training and performance review to its employees. The Company believes its relationship with its employees to be good.

SHARE APPRECIATION RIGHTS PLAN

At the shareholders' general meeting of the Company held on 30 July 2003, the Senior Management Share Appreciation Rights Plan was approved. It is designed to link the financial interests of the Company's senior management with the Company's results of operations and the performance of the Company's H Shares. The Board of Directors makes decisions under the scheme and administers the scheme. No shares will be issued under the scheme. Therefore, the shareholdings of shareholders will not be diluted.

Under the share appreciation rights plan, members of the Board of Directors (excluding independent non-executive directors) and the Supervisory Committee, president, vice presidents, chief financial officer, division managers of the Company, presidents of provincial level branch offices, and other senior management at equivalent levels and employees with special contribution to the Company as determined by the nomination, remuneration and review committee are eligible to receive share appreciation rights.

9 See Note 7 to financial statements.

MARKET RISKS

Interest Rate Risk

Exposure to interest rate changes primarily results from significant holdings of fixed income investments. The Company's fixed maturity investments include term deposits, government bonds, bonds issued by financial institutions and corporate bonds with a rating greater than rated AA, most of which are exposed to interest rate risk. The Company also invests in floating rate instruments, interest proceeds from which can rise and fall due to changes in interest rates. The Company's holding in investment funds is also exposed to price fluctuations caused by changes in interest rates. Interest rate risks may also affect future investments of the Company.

The Company manages exposure to risks associated with interest rate fluctuations through active review of investment portfolio by its management and consultation with financial investment experts. The goal is to maintain liquidity, to preserve capital and to generate stable returns.

Credit Risk

The Company is subject to credit risk on investments such as corporate bonds and mutual funds. Deterioration of the financial condition or results of operations of the issuers of these instruments may cause a delay in payments of principal or interest when due and eventually result in uncollectibility. The Company tries to manage credit risk by analyzing the creditworthiness of companies prior to making investments as well as strictly following the CIRC guidelines which only permit investments in corporate bonds with a rating greater than AA.

The Company is also subject to credit risk with respect to amounts owed to it by reinsurers pursuant to the terms of reinsurance policies it has with them. As a result, the Company pays particular attention, on an ongoing basis, to the creditworthiness and financial condition of the reinsurers with whom it deals. Except when dealing with national reinsurers, the Company only purchases reinsurance from reinsurers with A.M. Best ratings of at least A-.

Exchange Rate Risk

The Company conducts its business primarily in Renminbi, which is also its functional and financial reporting currency. However, a portion of its business (including underwriting certain international cargo insurance and aviation insurance) are conducted in foreign currencies, typically US dollars. A portion of its claims and liabilities is also denominated in foreign currencies, typically US dollars.

Most of the Company's sales are domestic and as such it has a limited amount of foreign currency denominated accounts receivable.

Foreign exchange transactions under its capital account, are subject to foreign exchange regulation and require the approval of the State Administration of Foreign Exchange. Actions taken by the PRC government could cause future exchange rates to vary significantly.

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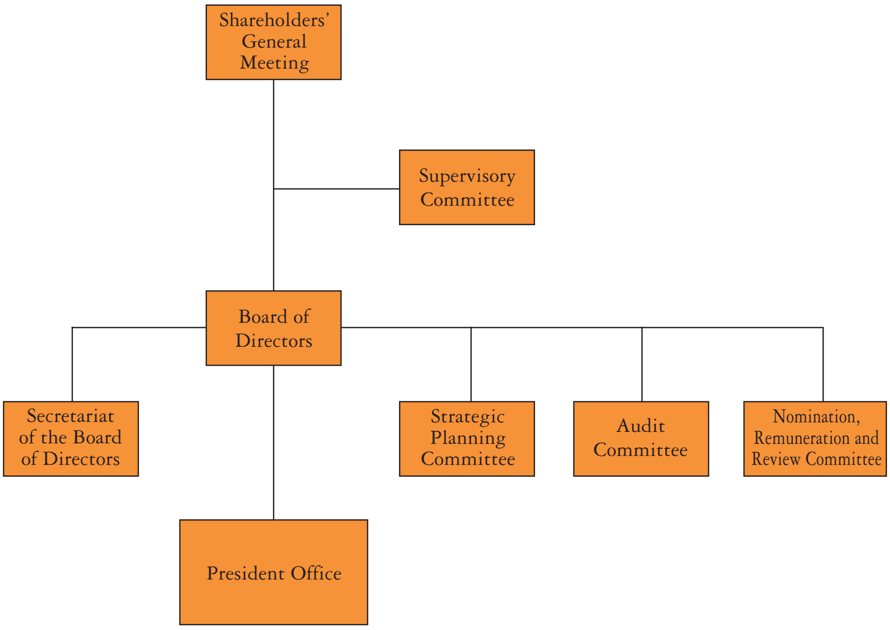
DEVOTION

Corporate Governance

The Company has implemented a formal corporate governance structure including the formation of a Board of Directors and Supervisory Committee, the members of which are elected at a shareholders' general meeting. In accordance with a resolution passed at the third meeting of the first Board of Directors, the Company established three special committees under the Board of Directors, namely the Strategic Planning Committee, the Audit Committee and the Nomination, Remuneration and Review Committee.



The Company has formulated its Articles of Association, Rules of Conduct for Shareholders' General Meetings, Rules of Conduct for Board of Directors, Charter of the Supervisory Committee and work manuals for the special committees of the Board of Directors in strict compliance with the Company Law of the People's Republic of China (the "Company Law"), the Insurance Law of the People's Republic of China, the Special Regulations of the State Council on the Overseas Offering and Listing of Shares by Joint Stock Limited Companies, other laws, administrative regulations and relevant provisions of the State and the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited (the "Listing Rules").

POWERS AND DUTIES OF THE SHAREHOLDERS' GENERAL MEETING, BOARD OF DIRECTORS AND SUPERVISORY COMMITTEE

Powers and duties of the Shareholders' General Meeting: deciding on the Company's operational policies and long-term and medium-term investment plans; electing or removing Directors and deciding matters relating to the remuneration of Directors; electing or removing those Supervisors who are representatives of the shareholders and deciding matters relating to the remuneration of Supervisors; examining and approving reports of the Board of Directors; examining and approving reports of the Supervisory Committee; examining and approving the Company's proposed annual budget and final accounts; examining and approving the Company's plans for the distribution of profits and recovery of losses; deciding on any increase or reduction in the Company's registered capital; deciding on merger, division, dissolution and liquidation of the Company and other similar matters; deciding on the issue of bonds by the Company; deciding on the appointment, dismissal or discontinuation of appointment of the Company's auditors; amending the Articles of Association; examining proposals from shareholders representing 5% or more of voting rights in the Company; and attending to any other matters required to be resolved at the shareholders' general meeting by laws, administrative regulations or the Articles of Association.

Powers and duties of the Board of Directors: convening shareholders' general meetings, reporting on its work to the shareholders' general meetings; implementing resolutions of the shareholders' general meetings; deciding on the Company's annual business plans and investment plans; formulating the Company's annual budget and final accounts; formulating the Company's plan for distribution of profits and recovery of losses; formulating proposals for increase or reduction in the Company's registered capital and the issue of corporate bonds; drawing up plans for the merger, division or dissolution of the Company; determining how to set up the Company's internal management structure; appointing or removing the Company's President and the Secretary of the Board of Directors and, based on the nominations of the President, appointing or removing the Vice President(s), Chief Financial Officer and President's Assistants, and determining their remuneration, rewards and punishments; approving the Company's basic management system; formulating proposals for any amendment to the Articles of Association; electing members to the special committees; and exercising any other powers and duties conferred by the shareholders' general meetings and the Articles of Association.

Powers and duties of the Supervisory Committee: examining the Company's financial affairs; monitoring compliance of Directors, the President and other members of senior management of the Company with laws, administrative regulations and the Articles of Association, while performing their duties; requesting the Directors, the President or other member of senior management to change their behavior when the acts of such persons are harmful to the interests of the Company; verifying financial information, such as financial reports, business reports and profit distribution plans, to be submitted by the Board of Directors at shareholders' general meetings and, should any queries arise, appointing registered accountants or practicing auditors to re-examine such information; proposing to convene extraordinary general meetings of shareholders; negotiating with or initiating proceedings against a Director on behalf of the Company; and exercising other powers and duties conferred by the Articles of Association.

DUTIES OF THE SPECIAL COMMITTEES OF THE BOARD OF DIRECTORS

Primary duties of the Strategic Planning Committee: formulating strategic development plans for the Company, setting out strategic objectives and formulating strategic measures and actions; formulating material investment and financing plans for the Company; and monitoring the implementation of the Company's strategic development plans and material investment and financing plans.

Primary duties of the Audit Committee: proposing the appointment, removal or discontinuation of appointment of the Company's auditors; monitoring the implementation of the Company's internal audit system; examining the Company's internal control system and monitoring the implementation thereof; examining the Company's financial information and monitoring the disclosure thereof; and examining material connected transactions and investment projects of the Company.

Primary duties of the Nomination, Remuneration and Review Committee: making recommendations on the size and composition of the Board of Directors; proposing to the Board of Directors possible candidates for appointment to the Board of Directors; formulating plans for the remuneration of Directors, the President and other senior management personnel, evaluating the results of implementing such plans and making recommendations on amendments thereof; formulating appraisal standards for Directors, the President and other senior management, conducting annual appraisals and making recommendations thereof; and coordinating the annual cross-appraisal among Independent Directors and evaluating the results thereof.

COMPOSITION OF THE SPECIAL COMMITTEES OF THE BOARD OF DIRECTORS

Strategic Planning Committee

Chairman: Tang Yunxiang
Members: Wang Yi, Qiao Lin, Fu Zhu and Wong Tung Shun, Peter

Audit Committee

Chairman: Yan Dawu (deceased), Lu Zhengfei (serving after the death of Yan Dawu)
Members: Cheng Wai Chee, Christopher and Ding Yunzhou

Nomination, Remuneration and Review Committee

Chairman: Cheng Wai-Chee, Christopher
Members: Wang Yincheng, Liu Zhenghuan and Zhou Shurui

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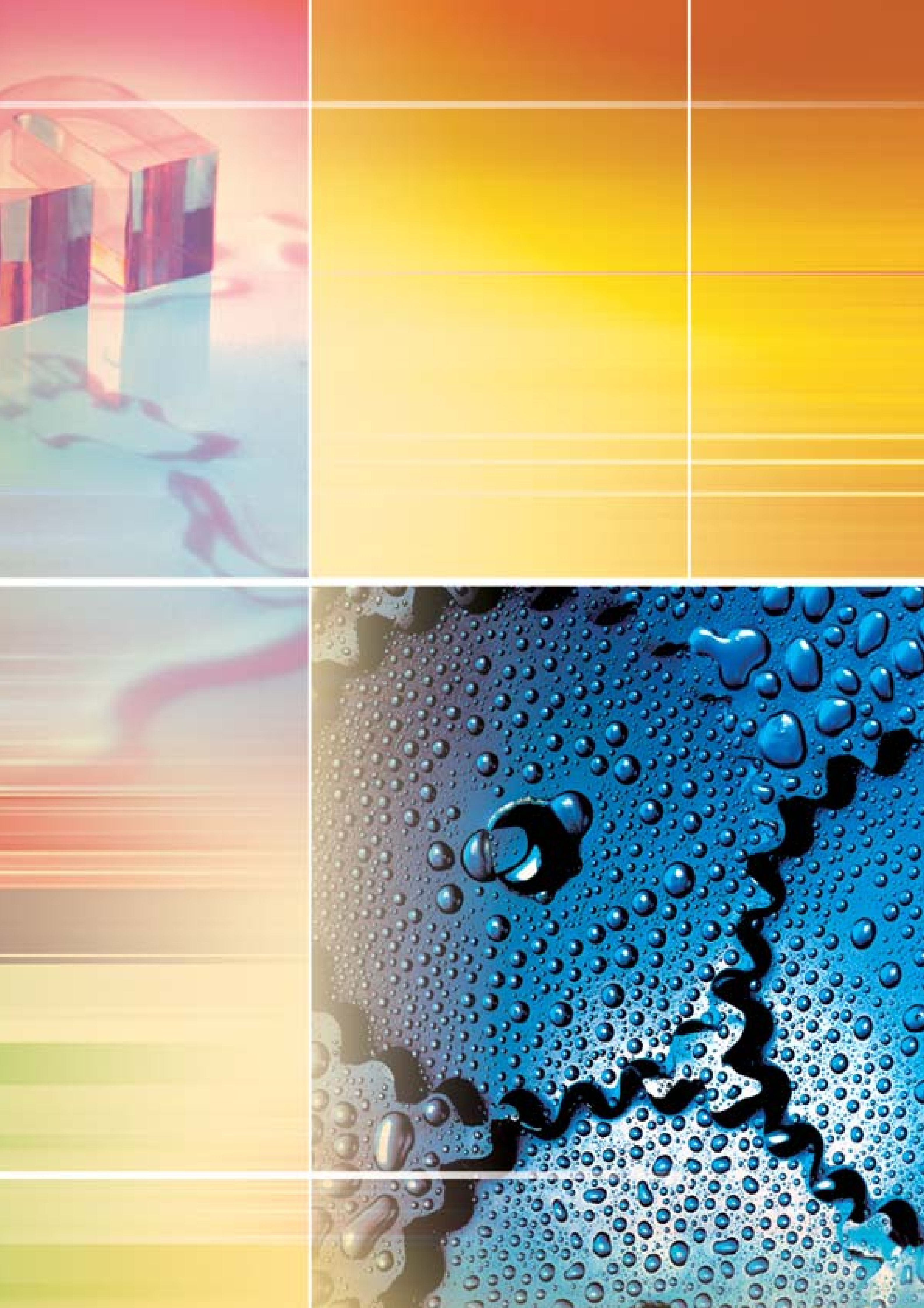
INNOVATION



Report of the Directors

The directors submit their first report, the audited financial statements for the period commencing from 7 July 2003 (date of incorporation of the Company) to 31 December 2003 (the "Period") and the pro forma audited financial statements for the year ended 31 December 2003 ("this Year").

CORPORATE REORGANIZATION

In preparation for the global offering, the Company was incorporated on 7 July 2003 as a joint stock company with limited liability, with The People's Insurance Company of China as its sole promoter, which was renamed and re-registered as PICC Holding Company ("PICC Holding") on 11 July 2003. Details of the Company's reorganization are set out in the Company's prospectus, in the section headed "Reorganization".

Following its incorporation, the Company immediately commenced the process of applying to transfer all business licenses and other operating licenses relating to the commercial insurance operations injected into the Company under the Reorganization Agreement from PICC Holding or its branch offices to the Company or its respective branch offices. These licenses include the Legal Person License for Insurance Institutions, Licenses to Operate an Insurance Business and Licenses to Operate a Foreign Exchange Business. The application process is purely procedural, but as of 27 October 2003 (the issue date of the prospectus of the Company), the transfer of the licenses to the Company's branch offices was still ongoing.

As of the date of this report, the transfer of the Legal Person License for Insurance Institutions and Licenses to Operate an Insurance Business to the Company's branch offices has been completed. There are 35 branch offices which need to operate foreign currency insurance business but have not yet completed the change of registration of Licenses to Operate a Foreign Exchange Business, representing less than 1% of the total branch offices. Currently, these branch offices are applying to their respective local regulatory bodies for Licenses to Operate a Foreign Exchange Business, in accordance with the authorization of higher level offices.

During the Reorganization, the Company obtained from PICC Holding six buildings without building title certificates. One of such buildings has already been sold and four buildings have completed the process of obtaining the title certificates. The remaining building is in the process of applying for building title certificates and has obtained from the respective local buildings administration department and developer a certificate of title confirmation.

As of 8 September 2003, there were 1,475 parcels of land and 1,987 buildings still in the name of PICC Holdings to be changed into the Company's name. As of the date of this report, except for 15 parcels of land and 16 buildings where the Beijing branch office is dealing with their applications at the respective local buildings administration department, all land use right certificates or building ownership right certificates have been obtained. 15 parcels of land and 16 buildings do not exceed 0.4% of the total number of properties of the Company. The building title certificates are expected to be obtained successfully.

PRINCIPAL ACTIVITIES

The Company engages in various insurance businesses (other than life insurance) in the People's Republic of China ("PRC"). The key product lines include motor vehicle insurance, commercial property insurance, homeowners insurance, cargo insurance, liability insurance, accidental injury insurance, surety insurance, which are denominated in RMB and foreign currencies. The Company is also engaged in the reinsurance of the above insurance products.

FINANCIAL RESULTS AND DIVIDENDS

The results of the Company for this Year and the Company's financial affairs as at 31 December 2003 are set out on pages 58 to 108 in this annual report.

Other than the special dividend that the Company is required to distribute to PICC Holding in accordance with the Reorganization Agreement between the Company and PICC Holding, the Board of Directors recommends not to pay dividend for this Year.

FINANCIAL SUMMARY

The summary of the pro forma results and the pro forma financial affairs of the Company for the four years ended 31 December 2003 are extracted from the accountants' report for the three years ended 31 December 2002 in the prospectus and the audited financial statements for the year ended 31 December 2003 on page 58 to page 108, and are set out on pages 2 to 3 in this annual report.

USE OF PROCEEDS FROM THE COMPANY'S INITIAL PUBLIC OFFERING OF SHARES

The net proceeds from the Company's initial public offering of shares in November 2003, after deducting related expenses, were approximately RMB5.61 billion. As at 31 December 2003, the net proceeds were used, as stated in the prospectus of the Company, to increase the level of paid-in capital and improve the solvency margin of the Company. The proceeds form part of the Company's liquid capital available to pay claims and were invested in accordance with relevant regulations of the PRC regulators.

FIXED ASSETS

Details of the changes in the fixed assets of the Company for this Year are set out in note 22 to the financial statements.

SHARE CAPITAL AND SHARE OPTION SCHEME

Details of the share capital of the Company in the Period, together with the changes and reasons for changes during the Period, are set out in note 32 to the financial statements.

PRE-EMPTIVE RIGHTS

There is no provision regarding pre-emptive rights under the Company Law, which requires the Company to issue new shares to its existing shareholders in proportion to their existing shareholdings.

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

Other than the shares issued pursuant to the global offering, the Company did not purchase, sell or redeem any of its listed securities during the Period.

RESERVES

Details of the reserves and changes in the reserves of the Company for the year ended 31 December 2003 are set out in changes in equity and reserves in the financial statements.

DISTRIBUTABLE RESERVES

As at 31 December 2003, the Company's share premium account increased to approximately RMB4.7 billion and the statutory reserves according to the PRC generally accepted accounting principle and regulations increased to approximately RMB9 million, both of which can be distributed by future capitalisation issue. Further, the Company's retained earnings and other reserves are distributable to the extent of approximately RMB50 million.

CHARITABLE AND OTHER DONATIONS

Charitable donations made by the Company during this Year amounted to RMB7.9 million.

MAJOR CUSTOMERS

The Company's aggregate turnover with its five largest customers did not exceed 10% of the Company's total turnover for this Year.

FIVE LARGEST REINSURERS

In this Year, the reinsurance premium ceded to the Company's top five reinsurers and the ratings by A.M. Best are:

Reinsurer	Reinsurance Premiums Ceded (RMB million)	A.M. Best Rating
China Re	9,544	Not applicable
Munich Re	290	A+
Swiss Re	271	AA
Lloyd's Syndicate	219	A
New Hampshire Insurance Co.	59	AAA

DIRECTORS AND SUPERVISORS

The directors of the Company in this Year are as follows:

Name	Title	Date of Appointment
Mr Tang Yunxiang	Chairman of the Board	6 July 2003
Mr Wang Yi	Vice Chairman of the Board Executive Director	6 July 2003
Mr Wang Yincheng	Executive Director	6 July 2003
Ms Liu Zhenghuan	Executive Director	6 July 2003
Mr Fu Zhu	Secretary of the Board Executive Director	6 July 2003
Mr Qiao Lin	Non-executive Director	6 July 2003
Mr Ding Yunzhou	Non-executive Director	6 July 2003
Mr Zhou Shurui	Non-executive Director	6 July 2003
Mr Yan Dawu (deceased)	Independent Non-executive Director	30 July 2003
Mr Cheng Wai Chee, Christopher	Independent Non-executive Director	30 July 2003
Mr Wong Tung Shun, Peter	Independent Non-executive Director	9 October 2003

Supervisors:

Name	Title	Date of Appointment
Mr Deng Zhaoyu	Chairman of Supervisory Committee	6 July 2003
Mr Tang Wei	Supervisor	6 July 2003
Mr Liu Qilong	Supervisor	6 July 2003

Change of directors or supervisors from 1 January 2004 to the date of this report is as follows:

Mr Lu Zhengfei was appointed as an Independent Non-executive Director of the Company on 24 February 2004.

BIOGRAPHICAL DETAILS OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

Biographical details of directors, supervisors and senior management of the Company are set out on pages 10 to 13 of this annual report.

DIRECTORS' AND SUPERVISORS' SERVICE CONTRACTS AND REMUNERATION

The Company did not enter into any service contracts with its directors and supervisors which is not determinable by the Company within one year without payment of compensation (other than compensation under normal statutory obligations).

Details of the remuneration of Company's directors and supervisors are set out in note 9 to the financial statements.

HIGHEST PAID INDIVIDUALS

Details of the remuneration of the Company's five highest paid individuals are set out in note 10 to the financial statements.

DIRECTORS' AND SUPERVISORS' INTERESTS IN CONTRACTS

None of the directors and the supervisors had a material interest, whether directly or indirectly, in any contract of significance to the business of the Company which was in effect during 2003.

MANAGEMENT CONTRACTS

On 10 October 2003, the Company and PICC Asset Management Company Limited, a wholly-owned subsidiary of PICC Holding, entered into an asset management agreement which became effective on the same date. Pursuant to the asset management agreement, PICC Asset Management Company Limited provides investment management services in respect of certain cash assets of the Company. The Company pays an annual management fee to PICC Asset Management Company Limited, which is calculated based on the average daily net asset value of the assets under the management of PICC Asset Management Company Limited in a particular year and the applicable annual rate. The term of the asset management agreement is four years.

On 9 October 2003, the Company and the Bank of China entered into a custodian agreement for managed assets, which became effective on the same date with a term of one year. Pursuant to the custodian agreement for managed assets, the Bank of China, as the custodian bank of the Company, is responsible for the custody of assets under management, settlement of capital, audit of accounts, valuation of assets, supervision on investments, as well as evaluation on investment performance.

DIRECTORS', SUPERVISORS' AND CHIEF EXECUTIVE'S INTEREST IN SHARES

The following sets forth the interests or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations (as defined in the Securities and Futures Ordinance) held by the current directors, supervisors and chief executive of the Company as at 31 December 2003 as recorded in the register of interests and short positions of directors, supervisors and chief executive required to be kept under section 352 of the Securities and Futures Ordinance:

Director	Capacity in which the shares are held	Number of shares held
Mr Cheng Wai Chee, Christopher	Controlled corporation (Note)	50,000 H Shares

Note: Such shares were directly held by Wing Tai Corporation Limited and were indirectly held by Wing Tai (Cheng) Holdings Limited and Renowned Development Limited. Mr Cheng controls more than one-third of the votes at the shareholders' general meeting of the above companies. The interests disclosed above are long positions of the shares of the Company.

Save as disclosed above, none of the other directors, supervisors or senior management had any interests or short positions in any shares, underlying shares or debentures of the Company or any of its associated corporations as at 31 December 2003 as recorded in the register required to be kept under section 352 of the Securities and Futures Ordinance, or any interests that require notification to the Company and the Stock Exchange under the "Model Code for Securities Transactions by Directors of Listed Companies".

SHARE APPRECIATION RIGHTS SCHEME

The shareholders of the Company adopted a scheme of share appreciation rights of senior management on 30 July 2003. The share appreciation rights scheme is designed to link the interests of the senior management with growth of the Company's results of operations and the Company's value (market price of the H Shares). The Board of Directors of the Company is responsible for making decisions under the scheme and administering the scheme. No shares will be issued under this scheme. Therefore, the shareholdings of shareholders will not be diluted as a result of the issuance of share appreciation rights.

Under the share appreciation rights scheme, members of the Board of Directors (excluding independent non-executive directors) and the Supervisory Committee, president, vice presidents, chief financial officer, division managers of the Company, presidents of provincial level branch offices, employees with special contribution to the Company as determined by the nomination, remuneration and review committee and other senior management at equivalent levels are eligible to receive share appreciation rights.

During this Year, the Company did not grant any share appreciation rights pursuant to the share appreciation rights scheme.

RETIREMENT BENEFITS

Details of the retirement benefits of the Company are set out in note 14 to the financial statements.

MATERIAL CONTRACTS

The Company and PICC Holding (the ultimate holding company of the Company) and PICC Asset Management Company Limited (a subsidiary of the ultimate holding company of the Company) and American International Group, Inc. (strategic investor of the Company) have entered into a number of agreements.

Details of the transactions pursuant to these agreements during this Year are set out in note 39 to the financial statements.

SUBSTANTIAL SHAREHOLDERS

As at 31 December 2003, the following shareholders were shown to have an interest of 5% or more in the issued share capital of the Company as recorded in the register required to be kept under section 336 of the Securities and Futures Ordinance:

Types of Shares	Shareholder	Number of Shares held		Percentage of Issued Share Capital
		Directly held	Indirectly held	
Domestic Shares	PICC Holding	7,685,820,000		69.0%
H Shares	AIG (Note 1)		1,103,038,000	9.9%
H Shares	Birmingham Fire Insurance Company of Pennsylvania ("BFIC") (Note 1)	562,549,380		5.05%

Note:

1. AIG is the ultimate controlling company of BFIC, hence BFIC's interests are deemed to be AIG's interests.

2. The interests disclosed above are long positions of the shares of the Company.

Apart from the foregoing, as at 31 December 2003, so far as the directors, supervisors and senior management of the Company are aware, no other person had any interests or short positions in the shares or underlying shares of the Company required to be recorded in the register kept pursuant to section 336 of the Securities and Futures Ordinance.

CONNECTED TRANSACTIONS

The connected transactions of the Company for this Year are set out in note 39 to the financial statements.

The Independent Non-executive Directors of the Company have reviewed all connected transactions and confirmed that:

1 all transactions were entered into during the ordinary and usual course of business;

2 all transactions were fair and reasonable so far as the independent shareholders of the Company are concerned;

3 all transactions were on normal commercial terms and in accordance with the terms of the agreements governing the transactions; and

4 none of the transactions exceeded the annual upper limits approved by the Stock Exchange.

The auditors of the Company have reviewed all connected transactions and confirmed to the Board of Directors of the Company that:

1 all transactions have been approved by the Board of Directors of the Company;

2 all transactions have been carried out in accordance with the terms of the agreements governing the transactions;

3 none of the transactions exceeded the annual upper limits approved by the Stock Exchange.

CODE OF BEST PRACTICE

So far as the Board of Directors are aware, for the period commencing from 6 November 2003 (the date on which the H Shares of the Company were listed on the Stock Exchange) to 31 December 2003, apart from being notified on 11 November 2003 of the passing away of Mr Yan Dawu, who was the Company's Independent Non-executive Director and the chairman of the audit committee, that resulted in the Company's audit committee failing to fulfil the requirement of having a majority of independent non-executive directors under the Code of Best Practice, Appendix 14 to the Listing Rules (the "Code of Best Practice"), the Company has complied with the Code of Best Practice throughout the year. The Company has appointed an Independent Non-executive Director, Mr Lu Zhengfei, as the chairman of the audit committee on 24 February 2004, to fill the vacancy.

AUDIT COMMITTEE

In accordance with the Code of Best Practice, the Company has established an audit committee (the "Audit Committee") to review and supervise the financial reporting process and internal control of the Company in September 2003. The Audit Committee has reviewed the audited financial statements for this Year. The composition of the Audit Committee is set out on page 37 of this report.

AUDITORS

Ernst & Young was the first auditors of the Company, with a term of office until the annual general meeting to be held. The resolution to re-appoint Ernst & Young as the auditors of the Company will be considered at the annual general meeting to be held. The auditors and reporting accountants who prepared the accountants' report included in the prospectus of the Company were not appointed as auditors of the Company for the year 2003 because consensus on the auditors' remuneration could not be reached.

By Order of the Board
Tang Yunxiang
Chairman

Beijing, PRC
23 April 2004

Report of the Supervisory Committee

Dear Shareholders:

From the date of the establishment of the Supervisory Committee of the Company, which is 6 July 2003, to 31 December 2003 (the "Reporting Period"), the Supervisory Committee of the Company carried out its supervisory duties and protected the interests of the shareholders, the Company and employees of the Company in strict accordance with the relevant provisions of the Company Law of the People's Republic of China and the Articles of Association of the Company.

During the Reporting Period, the Supervisory Committee convened two meetings where it passed two resolutions. The first meeting of the first Supervisory Committee was convened immediately following its establishment on 6 July 2003, at which Mr Deng Zhaoyu was elected as the Chairman of the Supervisory Committee. The second meeting of the first Supervisory Committee was held on 8 October 2003, at which the Charter of the Supervisory Committee of PICC Property and Casualty Company Limited was adopted. The Charter was then presented to and adopted by the Company's second extraordinary shareholders in 2003.

During the Reporting Period, the Supervisory Committee has chiefly been involved in the following areas of work:

1. Supervision of Decision Making. During the Reporting Period, the Supervisory Committee attended two shareholders' meetings and was present at four meetings of the Board of Directors, carefully reviewed 14 resolutions made by the shareholders' meetings and 29 resolutions made by the Board of Directors and supervised the procedures and process of the decision making on these occasions.

2. Supervision of Implementation. The Supervisory Committee supervised the implementation of the resolution in relation to the listing of the Company, progress towards meeting the Company's 2003 profit forecast and utilization of proceeds from listing. The Supervisory Committee received one special report on the listing of the Company and an annual work report from the President of the Company. It also carried out an investigation of internal control.

3. Financial Review. The Supervisory Committee thoroughly reviewed the audited accountants' report and report on the connected transactions of the Company in connection with the Company's listing, and the audited financial statements of the Company for the 2003 financial year.

The Supervisory Committee is of the view that:

1. The Board of Directors of the Company conscientiously carried out its duties and responsibilities and has standardized the decision-making process. It also did an excellent job ensuring the successful listing of the Company as scheduled, formulating an outline for the Company's development strategy and increasing the transparency of the management of the Company. With the successful listing of its H Shares on the Main Board of The Stock Exchange of Hong Kong Limited, the Company improved its capital base and solvency. This has helped the Company create a solid foundation to handle the increased competition caused by the internationalization of the insurance market in China. In addition, the Independent Non-executive Directors of the Company expressed their views independently and provided expert advice in the course of decision making.

2. Faced with intense market competition in 2003, the Company's management team still managed to ensure the Company successfully completed its various business goals and met its projected profit targets. The team made tremendous efforts to strengthen the management of fundamentals, refine the Company's business structure, construct the "three centers" and reinforce internal controls. Following the reform of motor vehicle insurance, the Company successfully developed and launched personalized products aimed at meeting the diverse needs of its customers as well as differentiated premium rates to correspond to different levels of insurance risk. The Company constructed a full-scale data management and information system, built a unified information management platform and effected the centralization of the Company's operational and financial data.

3. The audited accountants' report of the Company in connection with the Company's listing and the audited financial statements of the Company for the 2003 Financial Year were prepared in strict accordance with the accounting principles promulgated by the Hong Kong Society of Accountants. Accounting treatment was in compliance with the principle of consistency and the data used in the reports gave a true and fair reflection of the Company's financial condition and operating results. The proceeds from the Company's public offering were applied in strict accordance with the description thereof set out in the Company's prospectus.

4. The Company's connected transactions were conducted on an arm's length basis, satisfied the relevant regulatory provisions of the Stock Exchange and accorded strictly with the commitments set out in the Company's prospectus. There was no indication of any infringement of the interests of minority shareholders or the Company.

5. Directors and senior management of the Company acted in diligence and good faith. During the Reporting Period, no member of senior management was found to have committed any breach of any laws, regulations or the Articles of Association or to have infringed any rights or interests of the shareholders, the Company or employees of the Company in exercising their duties.

6. During the Reporting Period, the Company was notified on 11 November 2004 of the passing away of Mr Yan Dawu, who was an Independent Non-executive Director and the chairman of the audit committee, that resulted in the Company's audit committee failing to fulfil the requirement of having a majority of Independent Non-executive Directors under the Code of Best Practice. The Company has appointed an Independent Non-executive Director, Mr Lu Zhengfei, as the chairman of the audit committee on 24 February 2004.

The Supervisory Committee hopes that the Company will further refine its business structure, continue to strengthen its management and control capabilities, improve the utilization of information technologies, improve the implementation of the "three centers" and endeavor to increase market competitiveness and profitability of the Company.

In 2004, the Supervisory Committee will continue to strictly abide by the Articles of Association and relevant regulations, carry out its supervisory duties and conscientiously protect the interests of the Company and its shareholders and employees. The Supervisory Committee will also continue to strengthen its supervision over the decision-making process, the truthfulness of financial information and conduct specialized inspections, investigations and research regarding the issues of connected transactions, internal controls, budget operations, reserve contributions and implementation of resolutions of the Company.

By Order of the Supervisory Committee
Deng Zhaoyu
Chairman of the Supervisory Committee

Beijing, PRC
23 April 2004

Corporate Information

Registered name:	
Chinese name:	中國人民財產保險股份有限公司
Abbreviated form of Chinese name:	人保財險
English name:	PICC Property and Casualty Company Limited
Abbreviated form of English name:	PICC P&C
Date of incorporation:	7 July 2003
Registered address:	No. 69 Dong He Yan Street Xuanwu District Beijing 100052 China
Place of business:	No. 69 Dong He Yan Street Xuanwu District Beijing 100052 China
Legal representative:	Tang Yunxiang
Secretary of the Board of Directors:	Fu Zhu
Information inquiry department:	Secretariat of the Board of Directors
Place of business in Hong Kong:	15th Floor, Guangdong Investment Tower 148 Connaught Road Central Hong Kong
Principal bankers:	Bank of China Industrial and Commercial Bank of China China Construction Bank Agricultural Bank of China
Auditors:	Ernst & Young
Consulting actuaries:	Milliman Asia Limited Room 2408 Lippo Centre Tower Two No. 89 Queensway Hong Kong

Legal advisors:	*as to Hong Kong law:* Linklaters 10th Floor Alexandra House Chater Road Central Hong Kong *as to PRC law:* King and Wood Level 30, North Office Tower Beijing Kerry Centre 1 Guanghua Road Chaoyang District Beijing, PRC
Place of listing of H share:	The Stock Exchange of Hong Kong Limited
Type of stock:	H share
Stock description:	PICC P&C
Stock code:	2328
H share registrar and transfer office:	Computershare Hong Kong Investor Services Limited

Milestones

MAJOR EVENTS

1 6 July 2003 - Meeting was convened in Beijing for the establishment of the Company. The first shareholders' meeting was also convened, at which the Proposal of Establishment of PICC Property and Casualty Company Limited was deliberated and adopted and the first Board of Directors and the first Supervisory Committee of the Company were elected.

2 7 July 2003 - The business registration of the Company was completed and the Company was duly established.

3 19 July 2003 - Inauguration ceremony for the Company, PICC Holding Company and PICC Asset Management Company Limited was held in Beijing.

4 1 September 2003 - The Company participated in the Official Launch of Beijing 2008 Olympics Marketing Plan.

5 10 September 2003 - First six post-doctoral researchers joined the Postdoctoral Research Station of the Company and started their research work for a period of two years.

6 September to November 2003 - The Company restructured the staffing of its branches, reformed the staff selection system and streamlined organization.

7 6 November 2003 - The Company listed its H Shares on the Main Board of The Stock Exchange of Hong Kong Limited.

8 December 2003 - The Company was named "The Best Newly-listed Company in 2003" by AsiaMoney.

9 13 December 2003 - The Company was named "China Equity Deal of the Year" by International Financing Review Asia.

10 28 December 2003 - Chairman of the Company Mr Tang Yunxiang was named "PRC Economy's Person of the Year 2003" by CCTV.

11 31 December 2003 - The anniversary of the Company's successful implementation of the 2003 motor vehicle insurance terms and premium rates.

MAJOR UNDERWRITING PROJECTS

1 18 July 2003 - The Company renewed the insurance for the project of Phase III of Qinshan Nuclear Power Station.

2 30 July 2003 - The Company issued a provisional insurance policy for the Three Gorges Project.

3 1 October 2003 - The Company renewed the insurance for the united aeroplane fleets of CAAC with an insured amount of US$23.8 billion, which is the biggest policy in non-life insurance market in Asia.

4 10 November 2003 - The Company insured the Xiluodu Hydro Electric Power Station Project.

5 15 November 2003 - The Company signed a policy of an integrated insurance package for the projects of Matsushita Electric (China) Co., Ltd.

6 8 December 2003 - The Company renewed the insurance for the Daya Bay Nuclear Power Station during its operating period.

7 25 December 2003 - The Company renewed the insurance for the Shanghai GM Project.

8 30 December 2003 - The Company renewed the insurance for the Central Government's grain reserves project.

9 30 December 2003 - The Company renewed the insurance for the Shanghai Volkswagen Co., Ltd. Project.

10 End of 2003 - The Company chiefly underwrote CNOOC's oil field project during the production period at the Bohai region.

11 End of 2003 - The Company renewed the insurance for the fleets of China Shipping (Group) Company.

Milestones *(Continued)*

MAJOR COOPERATION PROJECTS

1 28 September 2003 - The Company and TravelSky Technology Limited entered into a Contract for the Cooperation in the Sale of Flight Accident Insurance on the network.

2 29 September 2003 - The Company entered into a Strategic Placing Agreement and a Technical Assistance and Co-operation Agreement with AIG, marking the formal establishment of strategic partnership and business cooperation between the Company and AIG.

3 9 October 2003 - The Company entered into a Custody Agreement for Managed Assets with The Bank of China, and then on the next day entered into an Asset Management Agreement with PICC Asset Management Company Limited, thereby becoming the first enterprise in China to apply insurance funds through a custody structure.

4 27 November 2003 - The Company became a cooperative partner in the first joint venture credit card business in China jointly launched by Shanghai Pudong Development Bank and Citibank N.A.. The Company developed tailor-made insurance products with Shopping Protection Insurance Clauses and Travel Delay Insurance Clauses for such credit card, which have filled the vacuum in this area of the insurance market in China.

ERNST & YOUNG
安永會計師事務所

To the members

PICC Property and Casualty Company Limited
(a joint stock company incorporated in the People's Republic of China with limited liability)

We have audited the financial statements on pages 58 to 108 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The Company's directors are responsible for the preparation of financial statements which give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently. It is our responsibility to form an independent opinion, based on our audit, on those financial statements and to report our opinion solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

BASIS OF OPINION

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants. An audit includes an examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

OPINION

In our opinion the financial statements give a true and fair view of the state of affairs of the Company as at 31 December 2003 and of the profit and cash flows of the Company for the period from 7 July 2003 (date of incorporation of the Company) to 31 December 2003 and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Ernst & Young
Certified Public Accountants
Hong Kong
23 April 2004

Profit and Loss Account

Period from 7 July 2003 (date of incorporation) to 31 December 2003

	Notes	7 July to 31 December 2003 RMB million	Pro forma 2003 RMB million	Pro forma 2002 RMB million
TURNOVER	5	23,643	54,968	50,571
Net premiums earned	5	19,923	40,409	36,381
Interest and dividend income	5	389	690	648
Net gains/(losses) on trading and non-trading securities	5	30	260	(645)
Net claims incurred	6	(14,444)	(29,063)	(26,634)
Amortisation of deferred acquisition costs	24	(1,427)	(2,479)	(1,694)
Insurance protection expense		(204)	(468)	(407)
Interest expense credited to policyholders' deposits		(65)	(123)	(54)
General and administrative expenses	7	(3,837)	(6,903)	(6,566)
OPERATING PROFIT		365	2,323	1,029
Finance costs	8	(23)	(35)	(35)
PROFIT BEFORE TAX		342	2,288	994
Tax	11	(235)	(837)	(716)
NET PROFIT ATTRIBUTABLE TO SHAREHOLDERS		107	1,451	278
BASIC EARNINGS PER SHARE (in RMB)	13	0.012	0.171	0.035

Note: The basis of presentation is disclosed in note 1 of the financial statements.

Balance Sheet

31 December 2003

	Notes	31 December 2003 RMB million	Pro forma 31 December 2002 RMB million
ASSETS			
Cash and cash equivalents	15	18,004	11,629
Term deposits	15	12,562	8,286
Trading securities	16	6,094	10,272
Investments in securities	17	10,765	2,294
Premiums receivables and agents' balances, net	18	2,012	2,339
Unearned premium reserves - reinsurers' share	25	6,030	7,104
Receivables from reinsurers	19	656	911
Reinsurance recoverable on unpaid losses	26	6,283	6,319
Prepayments and other receivables	20	2,067	2,102
Capital security fund	21	2,228	1,540
Fixed assets	22	15,645	16,526
Construction in progress	23	642	714
Deferred acquisition costs	24	1,284	1,076
Other non-current assets		300	334
Deferred tax assets	31	—	180
TOTAL ASSETS		84,572	71,626
LIABILITIES			
Unearned premium reserves	25	30,422	28,053
Loss and loss adjustment expense reserves	26	17,956	16,597
Provision for premium deficiency		—	2
Policyholders' deposits	27	9,290	7,499
Payables to reinsurers	28	1,978	2,303
Accrued insurance protection fund	29	522	81
Tax payable		167	—
Other liabilities and accruals	30	5,147	6,798
Deferred tax liabilities	31	333	—
TOTAL LIABILITIES		65,815	61,333
CAPITAL RESOURCES			
Issued capital	32	11,142	—
Reserves/owners' equity		5,615	10,293
		16,757	10,293
SUBORDINATED LOAN	33	2,000	—
TOTAL LIABILITIES AND CAPITAL RESOURCES		84,572	71,626

Mr. Tang Yunxiang
Chairman

Mr. Wang Yincheng
Executive Director

Note: The basis of presentation is disclosed in note 1 to financial statements.

Statement of Changes in Equity

31 December 2003

	Notes	Issued share capital RMB million	Share premium account RMB million	Non-trading investment securities revaluation reserve RMB million	Statutory surplus reserve RMB million	Statutory public welfare fund RMB million	Other reserves RMB million	Retained profits RMB million	Total RMB million
The Company									
At 7 July 2003 - Injection pursuant to the Reorganisation		—	—	—	—	—	11,695	—	11,695
Post-incorporation revaluation of investments in non-trading securities		—	—	(8)	—	—	—	—	(8)
Change of deferred tax asset recognised		—	—	3	—	—	—	—	3
Net gains and losses not recognised in the profit and loss account		—	—	(5)	—	—	—	—	(5)
Issue of shares upon incorporation	32	8,000	2,271	—	—	—	(10,271)	—	—
Issue of H Shares upon listing	32	3,142	2,882	—	—	—	—	—	6,024
Share issue expenses		—	(414)	—	—	—	—	—	(414)
Net profit for the period		—	—	—	—	—	—	107	107
Special dividends in connection with the Reorganisation	12	—	—	—	—	—	(650)	—	(650)
Transfer from/(to) reserves		—	—	—	6	3	—	(9)	—
At 31 December 2003		11,142	4,739	(5)	6	3	774	98	16,757
							(Note)		

Note: *This represents the net profit during the period from 1 October 2002 to 6 July 2003 arising from the commercial insurance business injected into the Company, net of the special dividends payable, pursuant to the Reorganisation (see note 1 to financial statements). According to a legal opinion obtained from the Company's lawyer, this amount is distributable, subject to the provisions as set out under "Profit appropriation" in note 3 to financial statements.*

Statement of Changes in Equity

31 December 2003

	Notes	Issued share capital RMB million	Share premium account RMB million	Non-trading investment securities revaluation reserve RMB million	Statutory surplus reserve RMB million	Statutory public welfare fund RMB million	Owner's equity / other reserves RMB million	Retained profits RMB million	Total RMB million
Pro forma									
At 1 January 2002		—	—	—	—	—	8,229	—	8,229
Pre-incorporation revaluation of fixed assets		—	—	—	—	—	3,716	—	3,716
Pre-incorporation revaluation of investments in non-trading securities		—	—	—	—	—	(137)	—	(137)
Change of deferred tax asset recognised		—	—	—	—	—	45	—	45
Net gains and losses not recognised in the profit and loss account		—	—	—	—	—	3,624	—	3,624
Net profit for the year		—	—	—	—	—	278	—	278
Capitalisation of accrued insurance protection	29	—	—	—	—	—	2,192	—	2,192
Net assets distributed to the ultimate holding company in connection with the Reorganisation		—	—	—	—	—	(3,749)	—	(3,749)
Elimination of deferred tax asset	31	—	—	—	—	—	(281)	—	(281)
At 31 December 2002 and 1 January 2003		—	—	—	—	—	10,293	—	10,293
Pre-incorporation net profit		—	—	—	—	—	1,344	—	1.344
Pre-incorporation revaluation of investments in non-trading securities		—	—	—	—	—	85	—	85
Post-incorporation revaluation of investments in non-trading securities		—	—	(8)	—	—	—	—	(8)
Change of deferred tax asset recognised		—	—	3	—	—	(27)	—	(24)
Net gains and losses not recognised in the profit and loss account		—	—	(5)	—	—	58	—	53
Capitalisation upon incorporation	32	8,000	2,271	—	—	—	(10,271)	—	—
Issues of H Shares upon listing	32	3,142	2,882	—	—	—	—	—	6,024
Share issue expenses		—	(414)	—	—	—	—	—	(414)
Post-incorporation net profit		—	—	—	—	—	—	107	107
Special dividends in connection with the Reorganisation	12	—	—	—	—	—	(650)	—	(650)
Transfer from/(to) reserves		—	—	—	6	3	—	(9)	—
At 31 December 2003		11,142	4,739	(5)	6	3	774 (Note)	98	16,757

Note: *This represents the net profit during the period from 1 October 2002 to 6 July 2003 arising from the commercial insurance business injected into the Company, net of the special dividends payable, pursuant to the Reorganisation (see note 1 of the financial statements). According to a legal opinion obtained from the Company's lawyer, this amount is distributable, subject to the provisions as set out under "Profit appropriation" in note 3 to financial statements.*

Cash Flow Statement

Period from 7 July 2003 to 31 December 2003

	Notes	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
CASH FLOWS FROM OPERATING ACTIVITIES				
Profit before tax		342	2,288	994
Adjustments for:				
Depreciation	7	680	1,560	1,432
Impairment loss on construction in progress	7	21	21	—
Provision for doubtful accounts	7	63	66	11
Interest and dividend income	5	(389)	(690)	(648)
Interest expense credited to policyholders' deposits	4	65	123	54
Net (gains)/losses on trading and non-trading securities	5	(30)	(260)	645
Net loss on disposal of fixed assets	7	6	7	113
Interest expense of bank and other financial costs	8	23	35	35
Decrease in premiums receivables and agents' balances		793	255	503
(Increase)/decrease in reinsurers' share of unearned premium reserves		1,132	1,074	(533)
(Increase)/decrease in receivables from reinsurers		(193)	255	127
(Increase)/decrease in reinsurance recoverable on unpaid losses		728	36	(2,278)
(Increase)/decrease in prepayments and other receivables		11	(165)	172
Increase in deferred acquisition costs		(1)	(208)	(359)
(Increase)/decrease in other non-current assets		(52)	34	30
Increase/(decrease) in unearned premium reserves		(2,690)	2,369	1,282
Increase in loss and loss adjustment expense reserves		489	1,359	4,083
Increase/(decrease) in provision for premium deficiency		(1)	(2)	2
Increase/(decrease) in payables to reinsurers		(331)	(325)	373
Increase in accrued insurance protection fund		182	441	460
Decrease in other liabilities and accruals		(471)	(9)	(537)
Increase in capital security fund		(2,228)	(688)	—
Cash (used in)/generated from operations		(1,851)	7,576	5,961
PRC income tax paid		(17)	(17)	(816)
Net cash inflow/(outflow) from operating activities		(1,868)	7,559	5,145
CASH FLOWS FROM INVESTING ACTIVITIES				
Interest received		478	657	498
Dividends received from trading and non-trading securities		12	42	126
Cash received in connection with the Reorganisation	34	17,797	—	—
Payment for capital expenditures		(573)	(1,696)	(1,372)
Proceeds from disposal of fixed assets		—	7	303
Payment for purchases of trading and non-trading securities		(12,661)	(16,511)	(13,868)
Proceeds from sales of trading and non-trading securities		10,051	12,555	6,125
Placement of deposits with banks with original maturity of more than three months and other balances with banks		(13,389)	(15,318)	(4,427)
Maturity of deposits with banks with original maturity of more than three months		11,171	11,042	5,198
Net cash inflow/(outflow) from investing activities		12,886	(9,222)	(7,417)
Net cash inflow/(outflow) before financing activities carried forward		11,018	(1,663)	(2,272)

Cash Flow Statement *(Continued)*

Period from 7 July 2003 to 31 December 2003

	Notes	7 July to 31 December 2003 RMB million	Pro forma 2003 RMB million	Pro forma 2002 RMB million
Net cash inflow/(outflow) before financing activities brought forward		11,018	(1,663)	(2,272)
CASH FLOWS FROM FINANCING ACTIVITIES				
Securities sold under agreements to repurchase		300	300	1,500
Securities purchased under agreements to resell		(2,100)	(1,500)	(400)
Increase in policyholders' deposits		1,204	1,668	2,987
Subordinated loan borrowed		2,000	2,000	—
Issue of H Shares		6,024	6,024	—
Expenses related to share issues		(414)	(414)	—
Interest expense to banks and other finance costs		(23)	(35)	(35)
Special dividend paid to the ultimate holding company		(5)	(5)	—
Cash and cash equivalents distributed in connection with the Reorganisation		—	—	(1,317)
NET CASH INFLOW FROM FINANCING ACTIVITIES		6,986	8,038	2,735
NET INCREASE IN CASH AND CASH EQUIVALENTS		18,004	6,375	463
Cash and cash equivalents at beginning of period/year		—	11,629	11,166
CASH AND CASH EQUIVALENTS AT END OF PERIOD/YEAR	15	18,004	18,004	11,629

ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS

	Notes	31 December 2003 RMB million	Pro forma 31 December 2002 RMB million
Cash at banks	15	11,529	8,900
Cash in hand	15	32	27
Securities purchased under resale agreements with original maturity less than 3 months	15	3,327	345
Deposits with bank and other financial institutions with original maturity less than 3 months	15	3,116	2,357
		18,004	11,629

Notes to Financial Statements

31 December 2003

1. COMPANY REORGANISATION AND BASIS OF PRESENTATION

The Company was incorporated on 7 July 2003 as a joint stock company with limited liability in the People's Republic of China (the "PRC") as part of the reorganisation (the "Reorganisation") of People's Insurance Company of China (now known as the "PICC Holding Company"), a state-owned enterprise engaged in the commercial insurance business in the PRC.

As part of the Reorganisation, which took effect as of 30 September 2002, PICC Holding Company injected into the Company all of its commercial insurance business and operations together with the related assets and liabilities, excluding certain assets and liabilities, by way of capital contribution. In consideration of such injection, the Company issued 8,000 million domestic shares of RMB 1.00 each to PICC Holding Company.

Further details of the Reorganisation are set out in the Company's prospectus dated 27 October 2003 issued in respect of the listing of the Company's shares on the Main Board of The Stock Exchange of Hong Kong Limited (the "HKSE").

The Company's financial statements include the results of the Company for the period from 7 July 2003 (date of incorporation) to 31 December 2003.

The Reorganisation involved companies under common control, and the Company's principal activities were carried out by PICC Holding Company prior to the Reorganisation. Accordingly, the directors consider that it is appropriate, for information purposes, to present supplementary pro forma financial statements. Such supplementary pro forma financial statements comprise a pro forma profit and loss account, a pro forma balance sheet, a pro forma statement of changes in equity and a pro forma cash flow statement, prepared as if the Company had been in existence throughout the two years ended 31 December 2003 and as if the Reorganisation was effective prior to the earliest date presented therein.

2. CORPORATE INFORMATION

The registered office of the Company is located at 69 Dongheyanjie, Xuanwumen, Beijing 100052, the PRC.

The Company is a provider of commercial insurance coverage in the PRC, and provides a wide range of property and casualty ("P&C") insurance consisting of property loss and damage insurance, liability insurance, credit and guarantee insurance, accidental injury insurance, short term health insurance and other P&C insurance as well as related reinsurance.

In the opinion of the directors, the ultimate holding company is PICC Holding Company, which is incorporated in the PRC.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of preparation

These financial statements have been prepared in accordance with Hong Kong Statements of Standard Accounting Practice, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for the periodic remeasurement of certain fixed assets and investments in securities as further explained below.

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Company and when the revenue can be measured reliably, on the following basis:

(a) premium income, at the inception of risk resulting from a policy being written;

(b) rental income, on a time proportion basis over the lease term;

(c) interest income, on a time proportion basis taking into account the principal outstanding and the effective interest rate applicable; and

(d) dividend income, when the shareholders' right to receive payment has been established.

Reinsurance

Assets and liabilities related to reinsurance contracts are reported on a gross basis unless a right of offset exists. Reinsurance premiums ceded and reinsurance recoveries on loss incurred are deducted from the respective revenue and expense accounts. Unearned premium reserves - reinsurers' share represents the ceded portion of unearned premium reserves. Payable to reinsurers includes ceded premiums retained by the Company to fund ceded losses as they become due pursuant to reinsurance agreements. Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured risks. Accordingly, revenues and expenses related to reinsurance agreements are recognised consistently with the underlying risk of the business reinsured.

Unearned premium reserves

Unearned premium reserves are recognised to cover the unexpired portion of the premiums written. Premiums are earned on a time-apportioned basis over the terms of the related insurance contracts.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Loss and loss adjustment expense reserves

The loss and loss adjustment expense reserves are for future payment obligations under insurance loss.

The loss and loss adjustment expense reserves are recorded on an undiscounted basis and comprise estimated provisions for losses reported at the balance sheet date, losses incurred but not yet reported at the balance sheet date, and loss adjustment expenses that can be directly attributable to individual claims.

The loss and loss adjustment reserves are calculated at the realistically estimated amount considered necessary to settle the loss in full less a deduction for the estimated value of salvage and other recoveries, using recognised actuarial methods. Past experience is taken into account as well as current and future expected social and economic factors.

Changes in estimates of the loss and loss adjustment expense reserves are recognised in the profit and loss account in the period in which the estimates are changed. The directors believe that the loss and loss adjustment expense reserves at the balance sheet date are adequate to cover the ultimate cost of all incurred losses and direct loss adjustment expenses to that date, but the reserves are necessarily based on estimates and no representation is made that the ultimate liability may not exceed or be less than such estimates.

Net claims incurred

Net claims incurred represents the actual amount of claims payable and claims handling expenses, net of claims recovered from reinsurance, and adjusted by changes in net loss and loss adjustment expenses reserves and net provision for premium deficiency.

Provision for premium deficiency

A provision for premium deficiency is recognised if the sum of expected losses and loss adjustment expenses, unamortised deferred acquisition costs and maintenance costs exceeds related unearned premium reserves. The premium deficiency is first recognised by writing off deferred acquisition costs to the extent required to eliminate the deficiency. If the premium deficiency is greater than the unamortised deferred acquisition costs, a provision is made for the excess deficiency. The amount of provision is made for each class of business individually.

Deferred acquisition costs

Policy acquisition costs which vary with and are primarily related to the production of new and renewal business (consisting principally of commission expenses and underwriting personnel expenses), net of reinsurance commissions, are deferred and amortised on a time-apportioned basis over the terms of the related insurance policies. Deferred acquisition costs are limited to the excess of unearned premium reserves over the sum of expected claim costs, claim adjustment related expenses and policy maintenance expenses.

Operating leases

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Where the Company is the lessor, assets leased by the Company under operating leases are included in non-current assets and rentals receivable under the operating leases are credited to the profit and loss account on a straight-line basis over the lease terms. Where the Company is the lessee, rentals payable under the operating leases are charged to the profit and loss account on a straight-line basis over the lease terms.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Employee benefits

The Company's contributions to the defined contribution plans administered by the PRC government are recognised as an expense in the profit and loss account as incurred.

Related parties

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence. Related parties may be individuals or corporate entities.

Income tax

Income tax comprises current tax and deferred tax. Income tax is recognised in the profit and loss account or in equity if it relates to items that are recognised in the same or a different period directly to equity.

Deferred tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences, except where the deferred tax liability arises from the initial recognition of an asset or liability and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

Deferred tax assets are recognised for all deductible temporary differences and the carryforward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward of unused tax assets and unused tax losses can be utilised, except where the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Conversely, previously unrecognised deferred tax assets are recognised to the extent that it is probable that sufficient taxable profits will be available to allow all or part of the deferred tax asset to be utilised.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted at the balance sheet date and interpretations and practices in respect thereof.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Dividends

Final dividends proposed by the directors are classified as a separate allocation of retained profits within the capital and reserves section of the balance sheet, until they have been approved by the shareholders in a general meeting. When these dividends have been approved by the shareholders and declared, they are recognised as a liability.

Interim and special dividends are simultaneously proposed and declared. Consequently, interim and special dividends are recognised immediately as a liability when they are proposed and declared.

Profit appropriation

Under the PRC Company Law and the Company's articles of association, net profit after tax as determined in accordance with PRC Accounting Regulations can only be distributed as dividends after making up prior years' cumulative losses, if any, and making allowance for the following statutory reserve funds, which cannot be used for purposes other than those for which they are created and are not distributable as cash dividends:

(a) Statutory surplus reserve

In accordance with the PRC Company Law and the Company's articles of association, the Company is required to appropriate 10% of the annual statutory net profit after tax (after offsetting any prior years' losses), determined in accordance with PRC Accounting Regulations, to the statutory surplus reserve. When the balance of such reserve fund reaches 50% of capital, any further appropriation is optional. The statutory surplus reserve can be utilised to offset prior years' losses or to increase capital. However, such balance of the statutory surplus reserve must be maintained at a minimum of 25% of capital after any such usage.

(b) Statutory public welfare fund

In accordance with the PRC Company Law and the Company's articles of association, the Company is required to appropriate 5% to 10% of the annual statutory net profit after tax (after offsetting any prior years' losses), determined in accordance with PRC Accounting Regulations, to the statutory public welfare fund, which will be utilised to build or acquire capital items, such as dormitories and other facilities for the employees of the Company, and cannot be used to settle staff welfare expenses.

In accordance with the PRC relevant regulations and the Company's articles of association, the retained profits of the Company for the purpose of profit distribution are deemed to be the lower of the amount determined in accordance with PRC accounting standards and regulations, and the amount determined in accordance with generally accepted accounting principles in Hong Kong.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Cash and cash equivalents

For the purpose of the cash flow statement, cash and cash equivalents comprise cash on hand and demand deposits, and short term highly liquid investments which are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired.

For the purpose of the balance sheet, cash and cash equivalents comprise cash on hand and at banks, which are not restricted as to use.

Foreign currencies

Foreign currency transactions are recorded at the applicable exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the applicable exchange rates ruling at that date. Exchange differences are dealt with in the profit and loss account.

Trading securities

Trading securities are investments in securities held for trading purposes and are stated at their fair values on the basis of their quoted market prices at the balance sheet date, on an individual investment basis. The gains or losses arising from changes in the fair value of a security are credited or charged to the profit and loss account in the period in which they arise.

Investments in securities

Investments in securities are non-trading investments in listed and unlisted securities intended to be held on a long term basis.

Listed securities are stated at their fair values on the basis of their quoted market prices at the balance sheet date, on an individual investment basis. Unlisted securities are stated at their estimated fair values, on an individual basis. The estimated fair values of unlisted investments are determined by the directors having regard to, inter alia, the prices of the most recent reported sales or purchases of the securities, or comparison of price/earnings ratios and dividend and interest yields of the securities with those of similar listed securities, with allowance made for the lower liquidity of the unlisted securities.

The gains or losses arising from changes in the fair value of a security are dealt with as movements in the non-trading investment securities revaluation reserve, until the security is sold, collected, or otherwise disposed of, or until the security is determined to be impaired, when the cumulative gain or loss derived from the security recognised in the non-trading investment securities revaluation reserve, together with the amount of any further impairment, is charged to the profit and loss account in the period in which the impairment arises.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Investments in securities *(continued)*

Securities purchased under purchase and resale agreements are recorded at their costs. The difference between the purchase cost and the reselling price is credited as interest income over the period from the date of purchase to the date of resale using the effective interest method.

Securities sold under sale and repurchase agreements in which the Company maintains effective control of the securities are accounted for as secured borrowings. Such securities are maintained on the balance sheet with the proceeds of the sale included in other liabilities and accruals. The difference between the selling price and the repurchase price is amortised as interest expense over the period from the date of sale to the date of repurchase using the effective interest method.

Premiums receivable and agents' balances

Premiums receivable and agents' balances represent amounts due from policyholders and agents and are stated at cost less allowance for doubtful accounts. An allowance for doubtful accounts is provided based on an evaluation of the recoverability of these accounts at the balance sheet date.

Fixed assets, construction in progress and depreciation

Fixed assets, other than construction in progress, are stated at cost or valuation less accumulated depreciation and any impairment losses. The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after fixed assets have been put into operation, such as repairs and maintenance, is normally charged to the profit and loss account in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of a fixed asset, the expenditure is capitalised as an additional cost of that asset.

Changes in the values of fixed assets are dealt with as movements in the revaluation reserve. If the total of this reserve is insufficient to cover a deficit, on an individual asset basis, the excess of the deficit is charged to the profit and loss account. Any subsequent revaluation surplus is credited to the profit and loss account to the extent of the deficit previously charged. On disposal of a revalued asset, the relevant portion of the revaluation reserve realised in respect of previous valuations is transferred to retained profits as a movement in reserves.

Depreciation is calculated on a straight-line basis after taking into account the estimated residual values, to write off the cost or valuation of each asset over its estimated useful life, as follows:

Land and buildings	30 - 70 years
Motor vehicles	4 - 9 years
Office equipment, furniture and fixtures	3 - 14 years

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Fixed assets, construction in progress and depreciation *(continued)*

The gain or loss on disposal or retirement of a fixed asset recognised in the profit and loss account is the difference between the net sales proceeds and the carrying amount of the relevant asset.

Construction in progress represents a building under construction, which is stated at cost less any impairment losses, and is not depreciated. Cost comprises the direct costs of construction and capitalised borrowing costs on related borrowed funds during the period of construction. Construction in progress is reclassified to the appropriate category of fixed assets when completed and ready for use.

Impairment

Internal and external sources of information are reviewed at each balance sheet date to determine whether fixed assets, construction in progress and investments in securities are impaired or an impairment loss previously recognised no longer exists or has decreased. If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised as a charge to the profit and loss account when the carrying amount of an asset exceeds its recoverable amount. The recoverable amount of an asset is the greater of its net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. A reversal of impairment losses is limited to the asset's carrying amount that would have been determined had no impairment loss been recognised in prior years. A reversal of impairment losses is recognised as a credit to the profit and loss account.

Policyholders' deposits

Policyholders' deposits represent deposits received from policyholders which are refundable under maturity refund type commercial insurance policies. Interest credited to these deposits is recognised as an expense in the profit and loss account.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Provisions and contingent liabilities

Provisions are recognised for liabilities of uncertain timing or amount when the Company has a legal or constructive obligation as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

Subordinated loan

Subordinated loan is included in the balance sheet at the value of the net proceeds received upon issue, adjusted for the amortisation of any premium or discount arising on issue.

Interest on subordinated loan is charged to the profit and loss account at the coupon rate adjusted for the amortisation of any premium or discount arising on issue, so as to achieve a constant rate of charge over the period from the date of issue to the date of redemption.

When subordinated loan issued is settled before maturity, any difference between the amount repaid and the carrying amount is recognised immediately in the profit and loss account.

4. SEGMENT INFORMATION

Segment information is presented by way of the Company's primary segment reporting basis, by business segment. No further geographical segment information is presented as the Company's customers and operations are located in Mainland China.

Summary details of the business segments are as follows:

(a) the motor vehicle segment provides insurance products to cover motor vehicles;
(b) the commercial property segment provides insurance products to cover commercial properties;
(c) the homeowners segment provides insurance products covering homes and their contents;
(d) the cargo segment provides insurance products covering vessels, crafts or conveyances;
(e) the liability segment provides insurance products covering policyholders' liability;
(f) the accidental injury segment provides insurance products covering accidental injury; and
(g) the "other" segment mainly represents insurance products related to marine hull, aviation and oil and gas.

4. SEGMENT INFORMATION *(CONTINUED)*

Information on the Company's reportable business segments is as follows:

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Turnover			
Motor vehicle	15,466	35,294	31,436
Commercial property	2,789	8,090	8,744
Homeowners	670	1,425	1,642
Cargo	1,072	2,657	2,966
Liability	967	2,406	2,752
Accidental injury	871	1,745	—
Other	1,808	3,351	3,031
	23,643	54,968	50,571
Net premiums earned			
Motor vehicle	13,525	26,930	23,928
Commercial property	2,915	6,437	6,346
Homeowners	429	1,045	1,105
Cargo	1,106	2,314	2,248
Liability	977	2,116	1,817
Accidental injury	464	514	-
Other	507	1,053	937
	19,923	40,409	36,381
Interest and dividend income			
Homeowners	(73)	26	29
Net gains/(losses) on trading and non-trading securities			
Homeowners	6	64	(83)

4. SEGMENT INFORMATION *(CONTINUED)*

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Net claims incurred			
Motor vehicle	(10,641)	(21,618)	(18,701)
Commercial property	(1,639)	(3,285)	(4,127)
Homeowners	(158)	(340)	(351)
Cargo	(520)	(1,107)	(1,001)
Liability	(591)	(1,401)	(1,396)
Accidental injury	(299)	(338)	—
Other	(596)	(974)	(1,058)
	(14,444)	(29,063)	(26,634)
Amortisation of deferred acquisition costs			
Motor vehicle	(1,140)	(2,053)	(1,520)
Commercial property	(64)	(125)	(101)
Homeowners	(56)	(134)	(116)
Cargo	(84)	(147)	(122)
Liability	(81)	(124)	(71)
Accidental injury	(76)	(80)	—
Other	74	184	236
	(1,427)	(2,479)	(1,694)
Insurance protection expense			
Motor vehicle	(150)	(323)	(269)
Commercial property	(17)	(59)	(67)
Homeowners	(10)	(17)	(14)
Cargo	(9)	(22)	(24)
Liability	(8)	(20)	(22)
Accidental injury	(12)	(19)	—
Other	2	(8)	(11)
	(204)	(468)	(407)
Interest expense credited to policyholders' deposits			
Homeowners	(65)	(123)	(54)
Segment profit before unallocated income and expenses			
Motor vehicle	1,594	2,936	3,438
Commercial property	1,195	2,968	2,051
Homeowners	73	521	516
Cargo	493	1,038	1,101
Liability	297	571	328
Accidental injury	77	77	—
Other	(13)	255	104
	3,716	8,366	7,538

4. SEGMENT INFORMATION *(CONTINUED)*

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Unallocated operating income and expenses			
Interest and dividend income	462	664	619
Net gains/(losses) on trading and non-trading securities	24	196	(562)
General and administrative expenses	(3,837)	(6,903)	(6,566)
Finance costs	(23)	(35)	(35)
	(3,374)	(6,078)	(6,544)
Profit before tax	342	2,288	994
Tax	(235)	(837)	(716)
Net profit	107	1,451	278

Interest and dividend income and net gains/(losses) on trading and non-trading securities attributed to the homeowners insurance product (see note 27), which can be separately identified based on the results of its designated pool of investments, are separately disclosed. The remaining amounts that are not attributed to particular insurance products are not allocated and are included under unallocated operating income and expenses.

4. SEGMENT INFORMATION *(CONTINUED)*

	31 December 2003 *RMB million*	Pro forma 31 December 2002 *RMB million*
Segment assets		
Motor vehicle	6,764	7,053
Commercial property	3,567	3,435
Homeowners	3,712	3,818
Cargo	564	659
Liability	572	668
Accidental injury	253	—
Other	4,338	5,280
	19,770	20,913
Unallocated assets	64,802	50,713
Total assets	84,572	71,626
Segment liabilities		
Motor vehicle	30,622	27,103
Commercial property	9,688	7,445
Homeowners	8,789	9,898
Cargo	1,972	2,259
Liability	2,022	2,400
Accidental injury	1,335	—
Other	6,792	6,364
	61,220	55,469
Unallocated liabilities	4,595	5,864
Total liabilities	65,815	61,333

5. TURNOVER AND REVENUE

Turnover represents direct premiums written and reinsurance premiums assumed, net of government levies and surcharges, i.e., gross premium written.

An analysis of turnover, interest and dividend income and net gains/(losses) on trading and non-trading securities is as follows:

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Turnover			
Direct premiums written	24,969	58,074	54,081
Reinsurance premiums assumed	7	11	13
	24,976	58,085	54,094
Less: Government levies and surcharges	(1,333)	(3,117)	(3,523)
	23,643	54,968	50,571
Net premiums earned			
Turnover	23,643	54,968	50,571
Less: Reinsurance premiums ceded	(5,289)	(11,116)	(13,441)
Net premiums written	18,354	43,852	37,130
Less: Changes in net unearned premium reserves	1,569	(3,443)	(749)
Net premiums earned	19,923	40,409	36,381
Interest and dividend income			
Interest income from trading and non-trading securities	35	164	126
Interest income from bank deposits	332	474	396
Dividend income from trading and non-trading securities	22	52	126
	389	690	648
Net gains/(losses) on trading and non-trading securities			
Realised gains on trading securities - Mutual funds	3	11	10
Realised gains/(losses) on trading securities - Debts	(4)	3	125
Unrealised gains/(losses) on trading securities - Mutual funds	22	192	(798)
Unrealised gains/(losses) on trading securities - Debts	(17)	10	(17)
Net gains/(losses) on disposal of non-trading securities:			
Realisation of revaluation reserve previously recognised	(5)	—	(1)
Recognised gain arising in the period/year	31	44	36
	30	260	(645)

6. NET CLAIMS INCURRED

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Gross claims expenses	17,295	35,114	31,849
Less: Loss recovered from reinsurance	(4,067)	(7,444)	(7,022)
Net claims expenses	13,228	27,670	24,827
Add: Change in net loss and loss adjustment expense reserves (note 26)	1,217	1,395	1,805
Add: Change in net provision for premium deficiency	(1)	(2)	2
Net claims incurred	14,444	29,063	26,634

7. GENERAL AND ADMINISTRATIVE EXPENSES

The Company's operating profit is arrived at after charging:

	Notes	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Personnel expenses		515	921	931
Depreciation	22	680	1,560	1,432
Office expenses		806	1,516	1,505
Provision for doubtful accounts		63	66	11
Repairs and maintenance		141	259	323
Impairment loss on construction in progress	23	21	21	—
Net loss on disposal of fixed assets		6	7	113
Minimum lease payments under operating leases - land and buildings		172	221	126
Auditors' remuneration		9	9	—
Others		1,424	2,323	2,125
		3,837	6,903	6,566

7. GENERAL AND ADMINISTRATIVE EXPENSES *(CONTINUED)*

Total personnel expenses of the Company for the relevant period are as follows:

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Included in net claims incurred	310	794	807
Included in deferred acquisition costs	604	1,538	1,609
Included in general and administrative expenses	515	921	931
Total personnel expenses	1,429	3,253	3,347

8. FINANCE COSTS

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Interest on bank loans wholly repayable within five years	14	25	34
Interest on subordinated loan (note 33)	9	9	—
Other finance costs	—	1	1
	23	35	35

9. DIRECTORS' AND SUPERVISORS' REMUNERATION

Directors' and supervisors' remuneration for the period, disclosed pursuant to the Listing Rules and Section 161 of the Companies Ordinance, is as follows:

	7 July to 31 December 2003 *RMB'000*	Pro forma 2003 *RMB'000*	Pro forma 2002 *RMB'000*
Fees	1,739	1,739	—
Other emoluments:			
Salaries, allowances and benefits in kind	1,215	1,638	852
Performance related bonuses	2,111	2,969	1,621
Pension scheme contributions	41	99	92
	5,106	6,445	2,565

The number of directors and supervisors whose remuneration fell within the following band is as follows:

	7 July to 31 December 2003	Pro forma 2003	Pro forma 2002
Nil to HK$1,000,000 (equivalent to approximately RMB1,065,700)	14	14	11

There was no arrangement under which a director or a supervisor waived or agreed to waive any remuneration during 2003 and 2002.

Fees include approximately HK$600,000 (equivalent to approximately RMB639,000) (2002: Nil) payable to the independent non-executive directors. There were no other emoluments payable to the independent non-executive directors during 2003 (2002: Nil).

The shareholders of the Company adopted a scheme of share appreciation rights of senior management on 30 July 2003. The share appreciation rights scheme is designed to link the interests of the senior management with growth of the Company's results of operations and the Company's value (market price of the H Shares). The Board of Directors of the Company is responsible for making decisions under the scheme and administering the scheme. No shares will be issued under this scheme. Therefore, the shareholdings of shareholders will not be diluted as a result of the issuance of share appreciation rights.

Under the share appreciation rights scheme, members of the Board of Directors (excluding independent non-executive directors) and the Supervisory Committee, president, vice presidents, chief financial officer, division managers of the Company, presidents of provincial level branch offices, employees with special contribution to the Company as determined by the nomination, remuneration and review committee and other senior management at equivalent levels are eligible to receive share appreciation rights.

During the period up to 30 December 2003, the Company did not grant any share appreciation rights pursuant to the share appreciation rights scheme.

10. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees during the period included three (2002: one) directors and supervisors, details of whose remuneration are set out in note 9 above. Details of the remuneration of the remaining two (2002: four) non-director or supervisor, highest paid employees for the period are as follows:

	7 July to 31 December 2003	**Pro forma 2003**	Pro forma 2002
	RMB'000	***RMB'000***	*RMB'000*
Salaries, allowances and benefits in kind	**331**	**470**	556
Performance related bonuses	**559**	**861**	1,138
Pension scheme contributions	**12**	**18**	43
	902	**1,349**	1,737

The number of non-director or supervisor, highest paid employees whose remuneration fell within the following band is as follows:

	Number of employees		
	7 July to 31 December 2003	**Pro forma 2003**	Pro forma 2002
Nil to HK$1,000,000 (equivalent to approximately RMB1,065,700)	**2**	**2**	4

There was no arrangement under which any of these highest paid employees waived or agreed to waive any remuneration during 2003 and 2002.

11. TAX

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Current - PRC			
Charge for the period/year	323	367	—
Overprovision in prior years	—	—	(683)
	323	367	(683)
Deferred	(88)	470	1,399
Total tax charge for the period/year	235	837	716

A reconciliation of the tax expense applicable to profit before tax using the statutory rate for the PRC, in which the Company is domiciled, to the tax expense at the effective tax rate is as follows:

	7 July to 31 December 2003 *RMB million*	%	Pro forma 2003 *RMB million*	%	Pro forma 2002 *RMB million*	%
Profit before tax	342		2,288		994	
Tax at the statutory tax rate of 33% (i)	113	33	755	33	328	33
Lower tax rate for specific provinces or local authority (i)	—	—	—	—	19	1.9
Income not subject to tax (ii)	(13)	(3.8)	(59)	(2.6)	(76)	(7.6)
Expenses not deductible for tax (iii)	135	39.5	141	6.2	445	44.7
Tax charge for the period/year	235	68.7	837	36.6	716	72.0

(i) The provision for PRC income tax is calculated based on the statutory rate of 33% in accordance with the relevant PRC income tax rules and regulations for all periods presented, except for certain branches of the Company, which are taxed at lower rates or exempted from PRC income tax.

(ii) This primarily comprises interest income from government bonds and distributions from open-ended mutual funds which are not subject to PRC income tax.

(iii) This primarily represents expenses in excess of the statutory deductible amount which are not tax deductible.

12. DIVIDENDS

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Special	650	650	—

Pursuant to the Reorganisation and the "Provisional Regulation Relating to Corporate Reorganisation of Enterprises and Related Management of State-owned Capital and Financial Treatment," which was issued by the PRC Ministry of Finance and became effective on 27 August 2002, the Company agreed to distribute special dividends equivalent to the net profit arising from the commercial insurance business injected into the Company pursuant to the Reorganisation for the period from 1 October 2002 (being the first day after the effective date of the Reorganisation) to 6 July 2003 (being the day immediately prior to the date of its incorporation) determined in accordance with PRC GAAP in two installments as follows:

- The Company distributed RMB5.4 million on 28 October 2003 in cash, representing the net profit under PRC GAAP for the three-month period ended 31 December 2002, to PICC Holding Company; and

- Within 30 days following the date on which the Company publishes its 2003 audited financial statements, the Company will distribute RMB644 million in cash to PICC Holding Company, which represents the net profit for the period from 1 January 2003 to 6 July 2003 calculated as 187/365 of the net profit for 2003 under PRC GAAP. This amount is included in the balance of the amounts due to the ultimate holding company as at 31 December 2003 (note 30).

13. EARNINGS PER SHARE

The calculations of basic earnings per share for the period from 7 July 2003 to 31 December 2003 and for the year ended 31 December 2003 and 2002, are based on:

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Earnings			
Net profit attributable to shareholders used in the basic earnings per share calculation	107	1,451	278

		Number of shares	
	7 July to 31 December 2003 million	Pro forma 2003 million	Pro forma 2002 million
Shares			
Weighted average number of ordinary shares used in the basic earnings per share calculation	9,000	8,482	8,000

The weighted average number of ordinary shares in issue used for the years ended 31 December 2003 and 31 December 2002 have taken into account the issue of 8,000 million ordinary shares upon the incorporation of the Company as if such shares have been outstanding since 1 January 2002.

The Company has had no dilutive potential shares outstanding since 1 January 2002.

14. EMPLOYEE RETIREMENT BENEFITS

As stipulated by the labour regulations of the PRC, the Company participates in various defined contribution retirement plans organised by municipal and provincial governments for its staff. The Company is required to make contributions to the retirement plans at rates ranging from 13% to 39.5% of the salaries, bonuses and certain allowances of its staff. Under the plans, its staff is entitled to a pension equal to a fixed proportion of the salary prevailing at his or her retirement date. The Company has no other material obligation for the payment of its staff's retirement and other post-retirement benefits other than the contributions described above. The Company's contributions for the for the period from 7 July to 31 December 2003, and for each of the two years ended 31 December 2003 and 2002 were RMB191 million, RMB362 million and RMB238 million, respectively.

15. CASH AND CASH EQUIVALENTS AND TERM DEPOSITS

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Cash at banks	**11,529**	8,900
Cash in hand	**32**	27
Securities purchased under resale agreements with original maturity of less than 3 months	**3,327**	345
Deposits with banks and other financial institutions with original maturity of less than 3 months	**3,116**	2,357
Cash and cash equivalents	**18,004**	11,629
Term deposits, representing deposits with banks with original maturity of more than three months and other balances with banks	**12,562**	8,286
Total	**30,566**	19,915

16. TRADING SECURITIES

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Listed investments:		
Debt securities issued by the PRC central government	**1,813**	3,052
Debt securities issued by corporate entities	**66**	273
Mutual funds issued by banks and other financial institutions	**3,690**	3,009
	5,569	6,334
Unlisted investments:		
Debt securities issued by the PRC central government	**525**	2,460
Debt securities issued by corporate entities	**—**	643
Debt securities issued by banks and other financial institutions	**—**	835
	525	3,938
Total	**6,094**	10,272

16. TRADING SECURITIES *(CONTINUED)*

A maturity profile of the debt securities classified as trading securities according to their contractual maturity dates is as follows:

	31 December 2003 *RMB million*	Pro forma 31 December 2002 *RMB million*
Less than 3 months but not on demand	199	—
Less than 1 year but more than 3 months	326	149
Less than 5 years but more than 1 year	1,813	3,172
More than 5 years	66	3,942
	2,404	7,263

17. INVESTMENTS IN SECURITIES

	31 December 2003 *RMB million*	Pro forma 31 December 2002 *RMB million*
Listed investments:		
Debt securities issued by the PRC central government	1,864	67
Debt securities issued by corporate entities	280	—
	2,144	67
Unlisted investments:		
Debt securities issued by the PRC central government	5,583	493
Debt securities issued by corporate entities	1,373	420
Mutual funds issued by banks and other financial institutions	1,665	1,314
	8,621	2,227
	10,765	2,294

As at 31 December 2003 and 2002, investments in securities represented non-trading securities and are carried at fair value. The unlisted investments are traded on over-the-counter market in the PRC.

17. INVESTMENTS IN SECURITIES *(CONTINUED)*

A maturity profile of the debt securities classified as non-trading securities according to their contractual maturity dates is as follows:

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Less than 3 months but not on demand	—	1
Less than 1 year but more than 3 months	201	151
Less than 5 years but more than 1 year	3,696	398
More than 5 years	5,203	430
	9,100	980

18. PREMIUMS RECEIVABLES AND AGENTS' BALANCES, NET

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Premiums receivables and agents' balances	2,095	2,350
Less: Allowance for doubtful accounts	(83)	(11)
	2,012	2,339

An aged analysis of the premiums receivable and agents' balances as at the balance sheet date, based on payment due date, and net of provisions, is as follows:

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Within 3 months	1,622	2,252
Over 3 months but less than 6 months	345	70
Over 6 months	45	17
	2,012	2,339

18. PREMIUMS RECEIVABLES AND AGENTS' BALANCES, NET *(CONTINUED)*

Movements in the allowance for doubtful accounts are as follows:

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
At beginning of the period/year	14	11	17
Provision for the period/year	69	72	11
Written-off	—	—	(17)
At end of the period/year	83	83	11

19. RECEIVABLES FROM REINSURERS

An aged analysis of the receivables from reinsurers as at the balance sheet date is as follows:

	31 December 2003 *RMB million*	Pro forma 31 December 2002 *RMB million*
Within 3 months	536	764
Over 3 months but less than 6 months	70	25
Over 6 months	50	122
	656	911

As at 31 December 2002 and 2003, the amount of receivables from reinsurers net of reinsurance premiums ceded was current and in accordance with the terms of the relevant reinsurance contracts. None of the Company's reinsurance contracts contains any contractual provisions for the delay of any reimbursement of incurred losses to the Company. Reinsurance adjustment commission and profit commission totaling RMB318 million and RMB395 million as at 31 December 2003 and 31 December 2002, respectively, are included in the receivables due from reinsurers that are due from certain reinsurers when the underwriting year of account closes, which under the terms of the relevant reinsurance contracts is normally on a three-year basis.

20. PREPAYMENTS AND OTHER RECEIVABLES

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Amount due from provincial and municipal governments (i)	1,210	1,210
Amount due from the ultimate holding company (ii)	—	78
Amounts due from other third parties	151	109
Interest receivables	190	199
Prepayments and deposits	77	131
Income tax recoverable	—	200
Others	439	175
	2,067	2,102

(i) During 1999, pursuant to the instruction from the State Council as part of the restructuring of the PRC insurance industry, the Company acquired the commercial insurance business of certain provincial and municipal governments. On the date of the acquisition, the net liabilities assumed amounted to RMB1,210 million, which mainly consisted of unearned premium reserves and loss and loss adjustment expense reserves, net of cash and cash equivalents.

On 30 May 2003, the Ministry of Finance issued a notice to the provincial and municipal governments instructing them to settle the amount with the Company by 31 December 2003. At present, the Company is in the process of negotiating with the relevant provincial and municipal governments to settle the amount. PICC Holding Company has undertaken to the Company that the amount will be fully recovered by the Company. Accordingly, no provision has been made against this amount as at 31 December 2003.

(ii) The amount due from the ultimate holding company is unsecured, interest-free and has no fixed repayment terms.

21. CAPITAL SECURITY FUND

In accordance with the PRC Insurance Law, the Company is required to maintain a deposit equivalent to 20% of its registered capital with banks designated by the China Insurance Regulatory Commission ("the CIRC") as a security fund. Based on the registered capital of the ultimate holding company, a bank deposit of RMB1,540 million was maintained as the security fund as at 31 December 2002. The use of the security fund is subject to the approval of the CIRC. The amount of this security fund has been increased to RMB2,228 million subsequent to the Company's initial public offering, representing 20% of the Company's current issued share capital.

22. FIXED ASSETS

	Land and buildings *RMB million*	Motor vehicles *RMB million*	Office equipment, furniture and fixtures *RMB million*	Total *RMB million*
The Company				
Cost:				
Acquired pursuant to the Reorganisation	13,836	1,460	1,604	16,900
Additions	115	30	295	440
Transfers (note 23)	152	—	11	163
Disposals	—	(13)	(1)	(14)
At 31 December 2003	14,103	1,477	1,909	17,489
Accumulated depreciation:				
Acquired pursuant to the Reorganisation	(353)	(435)	(384)	(1,172)
Depreciation	(225)	(204)	(251)	(680)
Disposals	—	8	—	8
At 31 December 2003	(578)	(631)	(635)	(1,844)
Net book value:				
As 31 December 2003	13,525	846	1,274	15,645
Pro forma				
Cost or valuation:				
At 1 January 2003	13,828	1,460	1,548	16,836
Additions	135	36	359	530
Transfers (note 23)	152	—	11	163
Disposals	(12)	(19)	(9)	(40)
At 31 December 2003	14,103	1,477	1,909	17,489
Analysis of cost or valuation:				
At cost	389	64	826	1,279
Valuation - 2002	13,714	1,413	1,083	16,210
	14,103	1,477	1,909	17,489
Accumulated depreciation:				
At 1 January 2003	(116)	(116)	(78)	(310)
Depreciation	(472)	(524)	(564)	(1,560)
Disposals	10	9	7	26
At 31 December 2003	(578)	(631)	(635)	(1,844)
Net book value:				
As 31 December 2003	13,525	846	1,274	15,645
As 31 December 2002	13,712	1,344	1,470	16,526

22. FIXED ASSETS *(CONTINUED)*

As required by the relevant PRC rules and regulations with respect to the Reorganisation, the fixed assets of the Company as at 30 September 2002 were valued for each asset class by China Enterprise Appraisals Co., Ltd., independent professionally qualified valuers registered in the PRC, on a depreciated replacement cost basis or fair market valuation basis as appropriate. The surplus on revaluation of approximately RMB3,716 million was dealt with in reserves and was considered as part of the Company's acquisition cost of fixed assets upon the Reorganisation. The Company's properties were also valued separately as at 31 July 2003 by Sallmanns (Far East) Limited, independent professionally qualified valuers in Hong Kong who have among their staff Fellows of the Hong Kong Institute of Surveyors and the Royal Institution of Chartered Surveyors. The value arrived at by these valuers was approximately the same as that arrived at by the PRC valuers.

For the purpose of the pro forma financial statements, had the fixed assets been carried at historical cost less accumulated depreciation and impairment losses, their carrying amounts as at 31 December 2002 would have been approximately RMB11,813 million as follows:

	Pro forma 31 December 2002 *RMB million*
Land and buildings	9,698
Motor vehicles	760
Office equipment, furniture and fixtures	1,355
	11,813

The land and buildings are all located in the PRC. The land is held under lease terms ranging from 30 years to 70 years.

As at 31 December 2003, the title certificates of certain land and buildings (net book value: RMB1,062 million) are still in the name of the ultimate holding company, and the change of registration to the registration to the Company's current name is in progress.

23. CONSTRUCTION IN PROGRESS

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
As of beginning of the period/year	791	714	1,117
Additions	35	112	280
Transfers (note 22)	(163)	(163)	(636)
Distribution to the owner in connection with the Reorganisation	—	—	(47)
Impairment	(21)	(21)	—
As of end of the period/year	642	642	714

The buildings under construction are all located in the PRC and are held under medium term leases.

24. DEFERRED ACQUISITION COSTS

The movements in deferred acquisition costs during the period from 7 July 2003 to 31 December 2003 and for the year ended 31 December 2003 are as follows:

The Company	Gross *RMB million*	Reinsurance *RMB million*	Net *RMB million*
At 7 July 2003	3,219	(1,936)	1,283
Deferred acquisition costs	3,109	(1,681)	1,428
Amortisation	(2,946)	1,519	(1,427)
At 31 December 2003	3,382	(2,098)	1,284

Pro forma	Gross *RMB million*	Reinsurance *RMB million*	Net *RMB million*
At 1 January 2003	3,091	(2,015)	1,076
Deferred acquisition costs	6,242	(3,555)	2,687
Amortisation	(5,951)	3,472	(2,479)
At 31 December 2003	3,382	(2,098)	1,284

25. UNEARNED PREMIUM RESERVES

	31 December 2003 *RMB million*	Pro forma 31 December 2002 *RMB million*
Gross unearned premium reserves	**30,422**	28,053
Less: Unearned premium reserves - reinsurers' share	**(6,030)**	(7,104)
Net unearned premium reserves	**24,392**	20,949

Unearned premium reserves and loss and loss adjustment expense reserves (note 26) of the Company's commercial insurance business as at 31 December 2002 and 31 December 2003, respectively, were reviewed by a firm of independent internationally based consulting actuaries. Save for RMB1,985 million as at 31 December 2003 (2002: RMB1,600 million). All of the unearned premium reserves are expected to be realised within one year from the balance sheet date.

26. LOSS AND LOSS ADJUSTMENT EXPENSE RESERVES

	Gross loss and loss adjustment expense reserves *RMB million*	Reinsurance recoverable on unpaid losses *RMB million*	Net loss and loss adjustment expense reserves *RMB million*
The Company			
At 7 July 2003	17,467	(7,011)	10,456
Incurred loss and loss adjustment expenses	17,259	(3,330)	13,929
Loss and loss adjustment expenses paid	(16,770)	4,058	(12,712)
At 31 December 2003	17,956	(6,283)	11,673
Pro forma			
At 1 January 2003	16,597	(6,319)	10,278
Incurred loss and loss adjustment expenses	35,114	(7,444)	27,670
Loss and loss adjustment expenses paid	(33,755)	7,480	(26,275)
At 31 December 2003	17,956	(6,283)	11,673

Save for RMB1,801 million as at 31 December 2003 (2002: RMB1,816 million), all of the loss and loss adjustment expense reserves are expected to be settled within one year.

27. POLICYHOLDERS' DEPOSITS

Policyholders' deposits consist of interest-bearing and non-interest-bearing deposits placed by policyholders. The remaining maturities of policyholders' deposits are analysed as follows:

	31 December 2003 *RMB million*	Pro forma 31 December 2002 *RMB million*
Due within 1 year	1,964	1,728
Due after 1 year but within 5 years	4,430	4,768
Due after 5 years or more	2,896	1,003
	7,326	5,771
	9,290	7,499

Certain commercial insurance policies offered by the Company require that the policyholders place a deposit with the Company which is refundable upon maturity or termination and bears no interest. Policy terms range from one year to perpetuity. A policyholder can terminate the insurance policy before the maturity date without penalties. The main feature of this insurance product is that the insurance coverage is fixed at the inception of the policy and remains in effect during the policy period or until terminated by the policyholder.

From 2002, the Company has underwritten policies of a new homeowners insurance product containing both insurance and investment features. Policyholders deposit a fixed principal amount which is only refundable upon the maturity of the policy of three years or five years and the policyholder receives a fixed rate of interest. Penalties on early termination are charged according to the terms stated in the insurance contract. The amounts of interest credited to policyholder deposits for the period from 7 July to 31 December 2003, and for each of the two years ended 31 December 2003 and 2002 were RMB65 million, RMB123 million and RMB54 million, respectively. The balances of this type of insurance deposit product as at 31 December 2003 and 31 December 2002 amounted to RMB6,142 million and RMB3,907 million, respectively.

28. PAYABLES TO REINSURERS

Payables to reinsurers are analysed as follows:

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Reinsurance balances payable	1,132	1,252
Reinsurance funds withheld	846	1,051
	1,978	2,303

Payables to reinsurers as at 31 December 2003 and 31 December 2002 are due within three months from the balance sheet date or are repayable on demand. The reinsurance funds withheld as at 31 December 2003 and 31 December 2002 are repayable upon the expiration of the related reinsurance contracts.

29. ACCRUED INSURANCE PROTECTION FUND

The Company is obligated to pay into an insurance protection fund based on 1% of its annual retained premiums in accordance with the relevant PRC insurance law and regulations. No further provision is required once the accumulated balance has reached 6% of the Company's total assets determined in accordance with PRC GAAP. The amount provided for is payable to the CIRC to finance the resolution of failed insurance companies in the PRC and is required to be set aside by investments in debt securities issued by the central government of the PRC and placements of deposits with the four wholly state-owned national commercial banks.

The Company's accrued insurance protection amounts in accordance with the relevant PRC insurance law and regulations as at the balance sheet date is held in form of cash at banks.

The cash at banks is restricted for use until the accrual has been settled with the CIRC. The balance as at the balance sheet date represented the amounts accrued for since 1 October 2002 and the accrued related interest income.

All of the accrued insurance protection amounts is payable at the request of the CIRC.

Pursuant to the Reorganisation and with the approval from the CIRC and the consent of the State Council of the PRC, the entire amount of the accrued insurance protection fund as at 30 September 2002 of RMB2,192 million was extinguished. The extinguishment of the accrued insurance protection fund has been accounted for as a capital transaction in the pro forma statement of changes in equity for the year ended 31 December 2002. Accordingly, RMB1,893 million of investments in debt securities and RMB299 million of deposits with banks with original maturity of more than three months as at 30 September 2002 were released from the restrictions. The extinguishment of this liability did not relieve the Company's obligation to accrue for the insurance protection fund after the effective date of the Reorganisation.

30. OTHER LIABILITIES AND ACCRUALS

	31 December 2003 *RMB million*	Pro forma 31 December 2002 *RMB million*
Amounts due to ultimate holding company (note i)	616	—
Amounts due to a fellow subsidiary (note ii)	4	—
Salaries and staff welfare payables	1,549	1,553
Accrued expenses	964	1,107
Securities sold under agreements to repurchase	300	1,500
Accrued capital expenditure	178	1,232
Premiums received in advance	952	768
Others (note iii)	584	638
	5,147	6,798

(i) The amounts due to the ultimate holding company included a special dividend of RMB644.5 million which will be paid within 30 days following the date on which the Company publishes its 2003 audited financial statements (note 12). The other balances with the ultimate holding company are unsecured, interest free and have no fixed terms of repayment.

(ii) The amounts due to a fellow subsidiary are unsecured, interest-free and have no fixed terms of repayment.

(iii) As at 31 December 2002, the balance included bank loan balances of RMB9 million which were unsecured and repayable on demand, and bore interest at one year borrowing rate of the People's Bank of China.

31. DEFERRED TAX

The Company

The movements in deferred tax liabilities and assets during the period are as follows:

Deferred tax liabilities (in RMB million)

	Revaluation of trading securities	Deferred income recognition of trading investment securities	Deferred acquisition cost	Others	Total
At 7 July 2003	(24)	31	422	(5)	424
Deferred tax (credited)/charged to the profit and loss account during the period	53	(30)	2	36	61
Gross deferred tax liabilities at 31 December 2003	29	1	424	31	485

Deferred tax assets (in RMB million)

	Revaluation of not-trading securities	Depreciation of fixed assets	Total
At 7 July 2003	19	—	19
Deferred tax (charged)/credited to the profit and loss account /reserves during the period	(16)	149	133
Gross deferred tax assets at 31 December 2003	3	149	152
Net deferred tax liabilities at 31 December 2003			333

There are no income tax consequences attaching to the payment of dividends by the Company to its shareholders.

The change in respect of the deferred tax asset recognised arising from the revaluation of non-trading securities is taken to the non-trading investment securities revaluation reserve.

31. DEFERRED TAX *(CONTINUED)*

Pro forma

The movements in deferred tax liabilities and assets during the year are as follows:

Deferred tax liabilities (in RMB million)

	Revaluation of trading securities	Deferred income recognition of trading investment securities	Deferred acquisition cost	Others	Total
At 1 January 2003	(37)	39	355	—	357
Deferred tax (credited)/charged to the profit and loss account during the year	66	(38)	69	31	128
Gross deferred tax liabilities at 31 December 2003	29	1	424	31	485

Deferred tax assets (in RMB million)

	Revaluation of not-trading securities	Tax value of of losses carried forward	Depreciation of fixed assets	Total
At 1 January 2003	46	491	—	537
Deferred tax (charged)/credited to the profit and loss account /reserves during the year	(43)	(491)	149	(385)
Gross deferred tax assets at 31 December 2003	3	—	149	152
Net deferred tax liabilities at 31 December 2003				333

There are no income tax consequences attaching to the payment of dividends by the Company to its shareholders.

The change in respect of the deferred tax asset recognised arising from the revaluation of non-trading securities is taken to the non-trading investment securities revaluation reserve.

31. DEFERRED TAX *(CONTINUED)*

Pro forma

Deferred tax liabilities (in RMB million)

	Deferred income recognition of trading investment securities	Deferred acquisition cost	Total
At 1 January 2002	8	237	245
Deferred tax charged to the profit and loss account during the year	31	118	149
Gross deferred tax liabilities at 31 December 2002	39	355	394

Deferred tax assets (in RMB million)

	Revaluation of trading securities	Revaluation of non-trading securities	Tax value of losses carried forward	Provision for other receivables and long term investments	Impairment loss on fixed assets	Provision for premium receivables and agents' balances	Total
At 1 January 2002	1	1	—	1,738	281	39	2,060
Deferred tax (charged)/credited to the profit and loss account/ reserves during the year	36	45	491	(1,738)	(281)	(39)	(1,486)
Gross deferred tax assets at 31 December 2002	37	46	491	—	—	—	574
Net deferred tax assets at 31 December 2002							180

There are no income tax consequences attaching to the payment of dividends by the Company to its shareholders.

The change in respect of the deferred tax asset recognised arising from the revaluation of non-trading securities is taken to the non-trading investment securities revaluation reserve.

32. ISSUED CAPITAL

	31 December 2003 *RMB million*	Pro forma 31 December 2002 *RMB million*
Shares		
Registered, issued and fully paid:		
7,685,820,000 domestic shares of RMB1.00 each	7,686	—
3,455,980,000 H Shares of RMB1.00 each	3,456	—
	11,142	—

The Company does not have a share option scheme.

A summary of the transactions from 7 July 2003 to 31 December 2003 analysing the movements in the Company's share capital is as follows:

	Number of shares in issue		Issued share capital		
	Domestic shares	H Shares	Domestic shares *RMB'000*	H Shares *RMB'000*	Total *RMB'000*
Upon incorporation on 7 July 2003 (a)	8,000,000,000	—	8,000,000	—	8,000,000
Issue of H Shares upon listing (b)	—	2,732,000,000	—	2,732,000	2,732,000
Sale of domestic shares by the ultimate holding company and conversion into H Shares upon listing (b)	(273,200,000)	273,200,000	(273,200)	273,200	—
Issue of H Shares upon exercise of over-allotment option (c)	—	409,800,000	—	409,800	409,800
Sale of domestic shares by ultimate holding company and conversion into H Shares upon exercise of over-allotment option (c)	(40,980,000)	40,980,000	(40,980)	40,980	—
At 31 December 2003	7,685,820,000	3,455,980,000	7,685,820	3,455,980	11,141,800

32. ISSUED CAPITAL *(CONTINUED)*

(a) As part of the Reorganisation (note 1), the Company issued 8,000 million domestic shares at a par value of RMB1.00 each to PICC Holding Company, and the Company's registered and paid-up capital became RMB8,000 million accordingly.

(b) The Company's shares were listed on the HKSE on 6 November 2003 and 3,005.2 million H Shares with a par value of RMB1.00 each were issued to the public by way of a placement and offer at a price HK$1.80 (equivalent to approximately RMB1.92) per share. The domestic shares and the H Shares rank pari passu with each other in all respects and, in particular, rank equally for all dividends or distributions declared, paid or made except for the distribution of the special dividends set out in note 12.

(c) The Company's shares were oversubscribed in its initial public offering and hence a further 450.8 million H Shares with a par value of RMB1.00 each were issued to the public pursuant to an over-allotment option.

33. SUBORDINATED LOAN

On 10 October 2003, the Company signed a loan agreement with China Development Bank which advanced a subordinated loan of RMB2,000 million to the Company for the purpose of enhancing the Company's solvency position. The loan is unsecured, bears interest at 90% to 110% of the PBOC's five-year borrowing interest rate per annum and is repayable in November 2023.

Notes to Financial Statements *(Continued)*

31 December 2003

34. NOTES TO THE CASH FLOW STATEMENT

(a) Major non-cash transactions

	7 July to 31 December 2003 *RMB million*
Net assets acquired upon the Reorganisation (note 1 to the financial statements)	
Investments in securities	2,331
Trading securities	11,896
Deposits with banks and other financial institutions with original maturity of more than 3 months	10,344
Cash and cash equivalents	17,797
Premiums receivables and agents' balances, net	2,874
Unearned premium reserves - reinsurers' share	7,162
Receivables from reinsurers	463
Reinsurance recoverable on unpaid losses	7,011
Prepayments and other receivables	2,388
Fixed assets	15,728
Construction in progress	791
Deferred acquisition costs	1,283
Other non-current assets	248
Unearned premium reserves	(33,112)
Loss and loss adjustment expenses reserves	(17,467)
Provision for premium deficiency	(1)
Policyholders' deposits	(8,021)
Payables to reinsurers	(2,309)
Accrued insurance protection	(340)
Tax payables	(44)
Other liabilities and accruals	(6,922)
Deferred tax liabilities	(405)
	11,695
Satisfied by:	
Shares issued	8,000
Share premium account	2,271
Other reserves	1,424
	11,695

34. NOTES TO THE CASH FLOW STATEMENT *(CONTINUED)*

(b) An analysis of the net inflow of cash and cash equivalents in respect of the net assets acquired upon the Reorganisation is as follow:

	7 July to 31 December 2003 *RMB million*
Cash and cash equivalents acquired	17,797
Net cash inflow in respect of the net assets acquired upon the Reorganisation	17,797

35. CONTINGENT LIABILITIES

(a) Pursuant to the Reorganisation, except for liabilities constituting or arising out of or relating to business undertaken by the Company after the Reorganisation, no other liabilities were assumed by the Company and the Company is not liable, whether severally or jointly and severally, for debts and obligations incurred prior to the Reorganisation. The ultimate holding company has also undertaken to indemnify the Company in respect of any loss or damage incurred in connection with or arising from the transfer of the assets and liabilities to the Company in the Reorganisation, any loss or damage suffered or incurred by the Company in relation to the novation of insurance contracts and reinsurance contracts from the ultimate holding company to the Company, and as a result of any breach by the ultimate holding company of any provision of the Reorganisation.

(b) Owing to the nature of insurance business, the Company is involved in legal proceedings in the ordinary course of business, including being the plaintiff or the defendant in litigation and arbitration. Such legal proceedings mostly involve claims on the Company's insurance policies. While the outcome of such contingencies, lawsuits or other proceedings cannot be determined at present, management believes that any resulting liabilities will not have a material adverse effect on the financial position or operating results of the Company.

36. SOLVENCY MARGIN

As at 31 December 2003, the solvency margin of the Company computed in accordance with the CIRC's regulations was as follows:

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Solvency margin calculated pursuant to the CIRC's regulations	**9,014**	2,802
Statutory minimum requirement	**(7,018)**	(5,943)
Surplus/(deficit)	**1,996**	(3,141)

As at 31 December 2002, the Company's solvency margin was less than the minimum statutory level by approximately RMB3,141 million, and the Company has duly notified to the CIRC. On 4 July 2003, the Company obtained a waiver from the CIRC in relation to its compliance with the solvency margin requirement and regulatory benchmarks. Pursuant to the waiver, the CIRC agreed not to bring any retrospective action against the Company with respect to its non-compliance prior to its listing. In addition, the CIRC has also agreed to grant the Company a grace period of three years after its listing, within which period the CIRC will not take any regulatory action against the Company if the Company is unable to comply with its solvency margin requirement and more than 4 out of a total of 11 regulatory benchmarks. If a P&C insurance company incorporated in the PRC fails to meet more than 4 of the 11 regulatory benchmarks, it is required to explain the reasons for its non-compliance and may be subject to investigation by the CIRC regarding its solvency margin. As a result of the issue of H Shares during the year, the Company's solvency margin exceeded the minimum statutory level by RMB1,996 million as at 31 December 2003. The Company failed to meet less than 4 of the 11 regulatory benchmarks as at 31 December 2003.

37. OPERATING LEASE ARRANGEMENTS

(a) As lessor

The Company leases its land and buildings under operating lease arrangements, with leases negotiated for terms ranging from one to four years. The terms of the leases generally also require the tenants to provide for periodic rent adjustments according to the then prevailing market conditions.

At 31 December 2003, the Company had total future minimum lease receivables under non-cancellable operating leases with its tenants falling due as follows:

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Within one year	21	9
In the second to fifth years, inclusive	49	7
	70	16

(b) As lessee

The Company leases certain of its land and buildings and motor vehicles under operating lease arrangements. Leases for properties are negotiated for terms ranging from one to twenty years, and those for motor vehicles for terms ranging between one to three years.

At 31 December 2003, the Company had total future minimum lease payments under non-cancellable operating leases falling due as follows:

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Within one year	296	72
In the second to fifth years, inclusive	681	141
After five years	54	64
	1,031	277

38. COMMITMENTS

In addition to the operating lease commitments detailed in note 37(b) above, the Company had the following capital commitments at the balance sheet date:

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Contracted, but not provided for	81	539
Authorised, but not contracted for	236	22
	317	561

39. RELATED PARTY TRANSACTIONS

The Company conducts businesses with enterprises directly or indirectly owned or controlled by the PRC government ("state-owned enterprises"). Furthermore, the PRC government itself represents a significant customer of the Company both directly through its numerous authorities and indirectly through its numerous affiliates and other organisations. The Company considers that the sale of insurance products to the PRC government authorities and affiliates and other state-owned enterprises are in the ordinary and normal course of business in the PRC and has not disclosed such transactions as related party transactions.

In addition to the transactions and balances detailed elsewhere in these financial statements, the Company and PICC Holding Company, PICC Asset Management Company Limited and American International Group ("AIG"), a strategic shareholder of the Company, entered into a number of agreements during the period in connection with the Reorganisation. These agreements impact the results of the operations of the Company beginning from the respective dates. The terms of the principal agreements are summarised as follows:

	Notes	**7 July to 31 December 2003** *RMB million*
Property rental expenses to PICC Holding Company	(a)	106
Property rental income from PICC Holding Company	(a)	5
Motor vehicle rental expenses to PICC Holding Company	(b)	11
Motor vehicle rental income from PICC Holding Company	(b)	2
Management fee to PICC Asset Management Company Limited	(c)	4
Services fee income from PICC Holding Company	(d)	2
Special dividends to PICC Holding Company (note 12)		650

39. RELATED PARTY TRANSACTIONS *(CONTINUED)*

(a) The Company entered into a Property Leasing Agreement with PICC Holding Company on 9 October 2003 under which the Company rented certain properties from PICC Holding Company and PICC Holding Company rented certain properties from the Company. The rental charges in respect of these properties are based on market rates. The term of the Property Leasing Agreement is four years and it became effective on 7 July 2003.

(b) The Company entered into a Motor Vehicle Rental Agreement with PICC Holding Company on 9 October 2003 under which the Company rented certain motor vehicles from PICC Holding Company and PICC Holding Company rented certain motor vehicles from the Company. The rental charges for the motor vehicles are based on market rates. The term of the Motor Vehicle Rental Agreement is four years and it became effective on 7 July 2003.

(c) On 10 October 2003, the Company and PICC Asset Management Company Limited, a wholly-owned subsidiary of PICC Holding, entered into an asset management agreement which became effective on the same date. Pursuant to the asset management agreement, PICC Assets Management Company Limited provides investment management services in respect of certain cash assets of the Company. The Company pays an annual management fee to PICC Asset Management Company Limited, which is calculated based on the average daily net asset value of the assets under the management of PICC Asset Management Company Limited in a particular year and the applicable annual rate. The term of the asset management agreement is four years.

(d) The Company entered into an Information System Services Agreement with PICC Holding Company on 9 October 2003 pursuant to which the Company agreed to provide PICC Holding Company with certain information services, including (i) facilities leasing services and network services; (ii) software and application services; (iii) other computer-related facilities maintenance services; and (iv) other information system services agreed by both parties.

The services fee payable to the Company by PICC Holding Company are to be no less than market rates, and are determined with reference to the costs associated with the labour and the equipment required to provide the services and support pursuant to the Information System Services Agreement between the Company and PICC Holding Company. The term of the Information System Services Agreement is four years.

(e) The Company entered into a Technical Assistance and Co-operation Agreement with AIG on 29 September 2003, pursuant to which the Company and one of AIG's wholly-owned subsidiaries will co-operate in the development of accident and health insurance products and the Company will cede quota share reinsurance at fixed cession percentages. This obligation will be reflected in a separate reinsurance agreement, which will be entered in the Company's ordinary and usual course of business. The intention of the parties is for the co-operation to continue indefinitely. Either party may request to review the key terms of the co-operation six months prior to the 15th anniversary of the date of the Technical Assistance and Co-operation Agreement and every 15 years thereafter, and unless the parties disagree to these terms, the agreement automatically renews for a further 15 years. There was no reinsurance income from/expense to AIG for the period from 7 July to 31 December 2003.

39. RELATED PARTY TRANSACTIONS *(CONTINUED)*

Other than the above agreements, the Company also entered into a Trademark Licence Agreement with PICC Holding Company on 9 October 2003 under which the Company has been granted the right to use the trademark bearing the "PICC" logo. The use of the trademark is on a royalty-free basis. The term of the Trademark Licence Agreement is 10 years and the agreement automatically renews for a further 10 years after the expiry of each 10 year term.

The transactions mentioned in (a) to (d) above also constitute connected transactions under the Listing Rules. Such transactions were exempted from disclosure by press notices under a waiver obtained from the HKSE.

40. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 23 April 2004.