

Management Discussion & Analysis

Recent Developments

Class Action Litigations

The nine putative class action lawsuits filed in the United States District Court for the Southern District of New York against the Company and certain of its officers and directors between March 16, 2004 and May 14, 2004 have been ordered to be consolidated and restyled *In re China Life Insurance Company Limited Securities Litigation, No. 04 CV 2112 (TPG)*. Plaintiffs filed a consolidated amended complaint on January 19, 2005, which names the Company, Wang Xianzhang, Miao Fuchun and Wu Yan as defendants. The consolidated amended complaint alleges that the defendants named therein violated Section 10(b) and 20(a) of the Securities Exchange Act of 1934, and Rule 10b-5 promulgated thereunder. We have engaged U.S. counsel to contest vigorously on behalf of us. The defendants jointly moved to dismiss the consolidated amended complaint on March 21, 2005.

SEC Informal Inquiry

On April 27, 2004, we received an informal inquiry, dated April 26, 2004, from the U.S. Securities and Exchange Commission ("SEC") requesting us to produce documents and other relevant information on certain matters. The SEC has advised us that the informal inquiry should not be construed as an indication by the SEC or its staff that any violations of law have occurred, or as a reflection upon any person, entity or security. We intend to cooperate and are cooperating fully with the inquiry.

OPERATING RESULTS

The restructuring of our predecessor CLIC was legally effective under PRC law and the restructuring on June 30, 2003; for accounting purposes, however, the restructuring is deemed to have occurred as of September 30, 2003. Accordingly, our historical profit and loss accounts data for 2003 includes data for our predecessor through September 30, 2003 and data for the Company from October 1, 2003 through December 31, 2003. As described more fully below, the year-on-year changes for many of the line items discussed below reflect the effect of the restructuring. For example, net premiums earned and policy fees for 2004 and for the time period from October 1, 2003 through December 31, 2003 does not include any net premiums and policy fees attributable to the non-transferred policies which were retained by CLIC. Likewise, the investment assets retained by CLIC are not included in our balance sheet as of December 31, 2003 and the income from such retained investment assets attributable to the period from October 1, 2003 through December 31, 2003 and for 2004, both realized and unrealized, is not included in our profit and loss accounts. The impact of the restructuring on accident and health insurance business is less significant than that on individual and group businesses, since a greater portion of accident and health policies are comprised of transferred policies.

Year Ended December 31, 2004 Compared with Year Ended December 31, 2003

Net Premiums Earned and Policy Fees

Net premiums earned and policy fees decreased by RMB2,208 million, or 3.3%, to RMB65,008 million in 2004 from RMB67,216 million in 2003. This decrease was primarily due to the effect of the restructuring described above as well as a decrease in policy fees from the individual life insurance business, offset in part by increases in net premiums earned from the individual life insurance business, group life insurance business and accident and health insurance business.

Net premiums earned and policy fees attributable to the transferred and new policies increased by RMB14,201 million, or 28.0%, to RMB65,008 million in 2004 from RMB50,807 million in 2003. This increase was primarily due to increases in net premiums earned from the individual life insurance, group life insurance business and the accident and health insurance businesses, offset in part by a decrease in policy fees from the individual life insurance business. Net premiums earned from risk-type participating products were RMB22,363 million in 2004, an increase of RMB8,946 million, or 66.7%, from RMB13,417 million in 2003. This increase was primarily due to an increased market demand, as well as our increased sales efforts, for endowment products. Of total net premiums earned in 2004 and attributable to the transferred and new policies, RMB2,780 million was attributable to single premium products and RMB47,670 million was attributable to regular premium products (including both first-year and renewal premiums). Of total net premiums earned in 2003 and attributable to the transferred and new policies, RMB4,553 million was attributable to single premium products and RMB32,610 million was attributable to regular premium products.

Individual Life Insurance Business

Net premiums earned and policy fees from the individual life insurance business decreased by RMB3,639 million, or 6.2%, to RMB54,902 million in 2004 from RMB58,541 million in 2003. This decrease was primarily due to the restructuring effect, as well as a reduction in policy fees, offset in part by increases in sales of endowment products and whole life products, as a result of the adjustment of our product selling strategy in the last quarter of 2003 to concentrate more on risk-type products.

Net premiums earned and policy fees from the individual life insurance business attributable to the transferred and new policies increased by RMB12,614 million, or 29.8%, to RMB54,902 million in 2004 from RMB42,288 million in 2003. This increase was primarily due to increases in sales of endowment products and whole life products, offset in part by a reduction in policy fees, as a result of the adjustment of our product selling strategy in the last quarter of 2003 to concentrate more on risk-type products and regular premium products.

Group Life Insurance Business

Net premiums earned and policy fees from the group life insurance business increased by RMB154 million, or 26.2%, to RMB742 million in 2004 from RMB588 million in 2003. This increase was primarily due to an increase in sales of investment-type products, which led to a growth in policy fees, and an increase in sales of whole-life insurance products, notwithstanding the effect of the restructuring described above.

Net premiums earned and policy fees from the group life insurance business attributable to the transferred and new policies increased by RMB310 million, or 71.8%, to RMB742 million in 2004 from RMB432 million in 2003. This increase was primarily due to an increase in sales of investment-type products, which led to a growth in policy fees and an increase in sales of whole-life insurance products.

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Accident and Health Insurance Business

Net premiums earned from the accident and health insurance business (which comprises short-term products) increased by RMB1,277 million, or 15.8%, to RMB9,364 million in 2004 from RMB8,087 million in 2003. Gross written premiums from the accident insurance business increased by RMB97 million, or 2.0%, to RMB4,977 million in 2004 from RMB4,880 million in 2003 and gross written premiums from the health insurance business increased by RMB304 million, or 5.7%, to RMB5,629 million in 2004 from RMB5,325 million in 2003. These changes were primarily due to our increased sales efforts for short-term products, as well as an increase in sales of our long-term products with short-term riders.

Substantially all of the net premiums earned were from transferred and new policies.

Net Investment Income

Net investment income increased by RMB1,492 million, or 15.2%, to RMB11,317 million in 2004 from RMB9,825 million in 2003. This increase was primarily due to an overall growth in investment assets during 2004, notwithstanding the restructuring effect described above.

As of December 31, 2004, total investment assets were RMB374,890 million and the investment yield for the year ended December 31, 2004 was 3.5%. As of December 31, 2003, total investment assets were RMB279,248 million and the investment yield for the year ended December 31, 2003 was 3.4% (which includes the investment yield for investment assets held by CLIC through September 30, 2003). This increase was primarily due to an increase in interest income from floating rate negotiable deposits and higher yields from newly issued bonds and subordinated bonds, as a result of an increase in benchmark deposit rate by the Chinese central bank in 2004.

Net Realized Gains/Losses on Investments

Net realized losses on investments was RMB237 million in 2004, compared to net realized gains of RMB868 million in 2003. This change reflected net realized losses of RMB317 million on debt securities which was primarily due to the impairment of bonds entrusted with Min Fa Security Limited Company, and net realized gains of RMB80 million on securities investment funds in 2004. In 2003, net realized gains was RMB550 million on debt securities and RMB318 million on securities investment funds. See note 4.1 of the notes to the financial statements included elsewhere in this annual report for more information on the bonds entrusted with Min Fa Security Limited Company.

Net Unrealized Gains/Losses on Investments

We reflect unrealized gains or losses on investments designated as trading in current period income. Our net unrealized losses on investments was RMB1,061 million in 2004, compared to net unrealized gains of RMB247 million in 2003. The results in 2004 reflected net unrealized gains of RMB11 million on debt securities and net unrealized losses on securities investment funds of RMB1,072 million, due to a deep fall in the securities market in 2004.

Deposits and Policy Fees

Deposits are gross additions to policyholder contract deposits. Total deposits decreased by RMB2,464 million, or 2.7%, to RMB88,737 million in 2004 from RMB91,201 million in 2003. Policy fees decreased by RMB902 million, or 14.8%, to RMB5,194 million in 2004 from RMB6,096 million in 2003. These decreases were primarily due to the effect of restructuring described above and decreased sales of investment-type products in the individual life insurance business, offset in part by increased sales of participating annuity products in group life insurance business.

Total deposits attributable to the transferred and new policies increased by RMB1,302 million, or 1.5%, to RMB88,737 million in 2004 from RMB87,435 million in 2003. Policy fees attributable to the transferred and new policies decreased by RMB363 million, or 6.5%, to RMB5,194 million in 2004 from RMB5,557 million in 2003. These changes reflected increased sales of participating annuity products in group life insurance business, and decreased sales of investment-type products in the individual life insurance business, as well as an increase in the proportion of investment-type products that are single premium products. Total deposits from participating products increased by RMB1,040 million, or 1.3%, to RMB81,416 million in 2004 from RMB80,376 million in 2003. Total policy fees from participating products decreased by RMB563 million, or 13.4%, to RMB3,651 million in 2004 from RMB4,214 million in 2003.

Individual Life Insurance Business

Deposits in the individual life insurance business decreased by RMB12,981 million, or 16.2%, to RMB66,981 million in 2004 from RMB79,962 million in 2003. Policy fees from the individual life insurance business decreased by RMB972 million, or 16.9%, to RMB4,796 million in 2004 from RMB5,768 million in 2003. These decreases reflected effect of restructuring described above, as well as the adjustment of our product selling strategy to concentrate more on risk type products, which led to a decrease in sales of investment type products.

Deposits in the individual life insurance business attributable to the transferred and new policies decreased by RMB10,337 million, or 13.4%, to RMB66,981 million in 2004 from RMB77,318 million in 2003. Policy fees from the individual life insurance business attributable to the transferred and new policies decreased by RMB584 million, or 10.9%, to RMB4,796 million in 2004 from RMB5,380 million in 2003. These decreases were primarily due to the adjustment of our product selling strategy to concentrate more on risk type products, which led to a decrease in sales of investment type products.

Group Life Insurance Business

Deposits in the group life insurance business increased by RMB10,517 million, or 93.6%, to RMB21,756 million in 2004 from RMB11,239 million in 2003. Policy fees from the group life insurance business increased by RMB70 million, or 21.3%, to RMB398 million in 2004 from RMB328 million in 2003. These increases were primarily due to an increase of sales of participating annuity products, offset in part by the effect of the restructuring described above.

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Deposits in the group life insurance business attributable to the transferred and new policies increased by RMB11,639 million, or 115.0%, to RMB21,756 million in 2004 from RMB10,117 million in 2003. Policy fees from the group life insurance business attributable to the transferred and new policies increased by RMB221 million, or 124.9%, to RMB398 million in 2004 from RMB177 million in 2003. These increases were due to increased sales of participating annuity products.

Accident and Health Insurance Business

There are no deposits in our accident and health insurance business.

Insurance Benefits and Claims

Insurance benefits and claims, net of amounts ceded through reinsurance, decreased by RMB10,148 million, or 17.9%, to RMB46,388 million in 2004 from RMB56,536 million in 2003. This decrease was due to the effect of restructuring described above, offset in part by an increase in business volume and the accumulation of liabilities. Life insurance death and other benefits decreased by RMB1,754 million, or 20.5%, to RMB6,816 million in 2004 from RMB8,570 million in 2003. This decrease was principally due to the effect of restructuring described above, offset in part by an increase in the number of policies in force. Life insurance death and other benefits as a percentage of gross written premiums and policy fees decreased to 10.3% in 2004 from 12.4% in 2003.

Insurance benefits and claims, net of amounts ceded through reinsurance, attributable to the transferred and new policies increased by RMB11,175 million, or 31.7%, to RMB46,388 million in 2004 from RMB35,213 million in 2003. This increase was primarily due to the increase in insurance benefits and claims in the individual life insurance business as a result of an increase in business volume and the accumulation of liabilities. Insurance benefits and claims, net of amounts ceded through reinsurance, attributable to participating products increased by RMB6,401 million, or 45.8%, to RMB20,383 million in 2004 from RMB13,982 million in 2003. Of these insurance benefits and claims attributable to participating products, life insurance death and other benefits increased by RMB2,124 million, or 396.3%, to RMB2,660 million in 2004 from RMB536 million in 2003 and the increase in future life policyholder benefits increased by RMB4,277 million, or 31.8%, to RMB17,723 million in 2004 from RMB13,446 million in 2003.

Individual Life Insurance Business

Insurance benefits and claims for the individual life insurance business decreased by RMB11,512 million, or 22.6%, to RMB39,435 million in 2004 from RMB50,947 million in 2003. This decrease was due to the effect of the restructuring described above, offset in part by the increase in business volume and the accumulation of liabilities. Of these insurance benefits and claims, life insurance death and other benefits decreased by RMB1,322 million, or 17.1%, to RMB6,422 million in 2004 from RMB7,744 million in 2003 and the increase in future life policyholder benefits decreased by RMB10,190 million, or 23.6%, to RMB33,013 million in 2004 from RMB43,203 million in 2003.

Insurance benefits and claims for the individual life insurance business attributable to the transferred and new policies increased by RMB9,489 million, or 31.7%, to RMB39,435 million in 2004 from RMB29,946 million in 2003. This increase was primarily due to the increase in business volume and the accumulation of liabilities. Of these insurance benefits and claims, life insurance death and other benefits increased by RMB3,074 million, or 91.8%, to RMB6,422 million in 2004 from RMB3,348 million in 2003. This increase was primarily due to an increased impact of the participating products, which we started to sell in 2000, and which pay survivorship benefits to policyholders every three years. The increase in future life policyholder benefits increased by RMB6,415 million, or 24.1%, to RMB33,013 million in 2004 from RMB26,598 million in 2003.

Group Life Insurance Business

Insurance benefits and claims for the group life insurance business decreased by RMB172 million, or 24.3%, to RMB535 million in 2004 from RMB707 million in 2003. This decrease was due to the effect of the restructuring described above, offset in part by the increase in business volume. Of these insurance benefits and claims, life insurance death and other benefits decreased by RMB432 million, or 52.3%, to RMB394 million in 2004 from RMB826 million in 2003 and the increase in future life policyholder benefits was RMB141 million in 2004, compared with a decrease of RMB119 million in 2003.

Insurance benefits and claims for the group life insurance business attributable to the transferred and new policies increased by RMB150 million, or 39.0%, to RMB535 million in 2004 from RMB385 million in 2003. This increase was primarily due to the increase in business volume. Of these insurance benefits and claims, life insurance death and other benefits decreased by RMB76 million, or 16.2%, to RMB394 million in 2004 from RMB470 million in 2003 and the increase in future life policyholder benefits was RMB141 million in 2004, compared with a decrease of RMB85 million in 2003.

Accident and Health Insurance Business

Insurance benefits and claims for the accident and health insurance business increased by RMB1,536 million, or 31.5%, to RMB6,418 million in 2004 from RMB4,882 million in 2003. Substantially all of these amounts related to transferred and new policies. This increase was primarily due to the increase in business volume of health insurance business, which has a relatively higher claim rate and an increase in medical expenses.

Policyholder Dividends and Participation in Profits

Policyholder dividends and participation in profits increased by RMB841 million, or 69.7%, to RMB2,048 million in 2004 from RMB1,207 million in 2003. Virtually all of these amounts were attributable to the transferred and new policies because our predecessor only began to sell participating products in 2000. This increase was primarily due to increases in our reserves and business volume.

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Amortization of Deferred Policy Acquisition Costs

Amortization of deferred policy acquisition costs reflects the amortization of deferred policy acquisition costs attributable to the transferred and new policies. The majority of acquisition costs attributable to the transferred and new policies are deferrable. Amortization of deferred policy acquisition costs increased by RMB1,240 million, or 24.7%, to RMB6,263 million in 2004 from RMB5,023 million in 2003. This increase was primarily due to an increase in number and overall amount of policies in force.

Underwriting and Policy Acquisition Costs

Underwriting and policy acquisition costs primarily reflect acquisition costs attributable to non-transferred policies in the individual life insurance business and group life insurance business, as well as non-deferrable portion of underwriting and policy acquisition costs in transferred and new policies. Underwriting and policy acquisition costs increased by RMB178 million, or 13.8%, to RMB1,472 million in 2004 from RMB1,294 million in 2003. Underwriting and policy acquisition costs were 2.26% of net premiums earned and policy fees in 2004, compared with 1.91% in 2003.

Of this amount, underwriting and policy acquisition costs in the individual life insurance business and group life insurance business together increased by RMB161 million, or 18.1%, to RMB1,051 million in 2004 from RMB890 million in 2003. This increase was primarily due to the increase in business volume during the period, as well as an increase in the sales of risk-type and regular-premium products, which have a relatively higher commission. Underwriting and policy acquisition costs in the accident and health insurance business increased by RMB17 million, or 4.2%, to RMB421 million in 2004 from RMB404 million in 2003. This increase was primarily due to the increase in business volume.

Administrative Expenses

Administrative expenses include the non-deferrable portion of policy acquisition costs attributable to the transferred and new policies, as well as compensation and other administrative expenses. Administrative expenses decreased by RMB277 million, or 4.0%, to RMB6,585 million in 2004 from RMB6,862 million in 2003. This decrease primarily reflected the effect of the restructuring described above, offset in part by the increase in business volume.

Other Operating Expenses

Other operating expenses, which primarily consist of employee housing benefits and expenses of non-core businesses (which includes investments in property, hotels and other operations through subsidiaries), decreased by RMB741 million, or 85.0%, to RMB131 million in 2004 from RMB872 million in 2003. A substantial amount of other operating expenses in 2003 comprises investments in property, hotels and other operations through subsidiaries, which we no longer have after the restructuring. This decrease primarily reflected the effect of the restructuring described above and the effective control of the costs by us.

Interest Credited to Policyholder Contract Deposits

Interest credited to policyholder contract deposits decreased by RMB2,940 million, or 40.5%, to RMB4,320 million in 2004 from RMB7,260 million in 2003. This decrease primarily reflected the effect of the restructuring described above, offset in part by an increase in the total policyholder account balance.

Interest credited to policyholder contract deposits attributable to the transferred and new policies increased by RMB1,400 million, or 47.9%, to RMB4,320 million in 2004 from RMB2,920 million in 2003. This increase was primarily due to an increase in the total policyholder account balance. Interest credited to participating policyholder contract deposits increased by RMB1,372 million, or 61.4%, to RMB3,607 million in 2004 from RMB2,235 million in 2003.

Income Tax

We pay income tax according to applicable Chinese enterprise income tax regulations and rules. Income tax expense, including current and deferred taxations, increased by RMB1,100 million, or 93.2%, to RMB2,280 million in 2004 from RMB1,180 million in 2003. This increase was primarily due to an increase in profits and the fact that in accordance with PRC law, the Company and China Life Insurance Asset Management Company Limited, which is controlled by the Company, are subject to tax on their income from the dates of their incorporation, June 30, 2003 and November 23, 2003. Our effective tax rate for 2004 was 24% as compared with a statutory tax rate of 33% principally because we had substantial interest income from government bonds which are not taxable.

Net Profit/Loss

For the reasons set forth above, net profit was RMB7,171 million in 2004, compared to a net loss of RMB1,428 million in 2003.

Individual Life Insurance Business

Net profit in the individual life insurance business was RMB8,503 million in 2004, compared to a net loss of RMB208 million in 2003. This result was primarily due to increased sales of risk-type products as well as the increased impact of the more profitable transferred and new policies in the individual life business following the restructuring.

Group Life Insurance Business

Net loss in the group life insurance business was RMB296 million in 2004, an improvement from a net loss of RMB1,263 million in 2003. This result was primarily due to the increased impact of the more profitable transferred and new policies in the group life business following the restructuring.

Accident and Health Insurance Business

Net profit in the accident and health insurance business decreased by RMB208 million, or 15.1%, to RMB1,172 million in 2004 from RMB1,380 million in 2003. The decrease in profitability was primarily due to the increased relative weight of the health insurance business in the accident and health insurance business. The overall performance of the accident insurance remained strong. The adverse performance of our health insurance business was primarily due to higher medical costs during the period, which were not matched by price increases for our products.

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LIQUIDITY AND CAPITAL RESOURCES

Liquidity Sources

Our principal cash inflows come from insurance premiums, deposits, proceeds from sales of investment assets, investment income and financing through initial public offering. The primary liquidity concerns with respect to these cash inflows are the risk of early contract holder and policyholder withdrawal, as well as the risks of default by debtors, interest rate changes and other market volatilities. We closely monitor and manage these risks.

Additional sources of liquidity to meet unexpected cash outflows are available from our portfolio of cash and investment assets. As of December 31, 2004, the amount of cash and cash equivalents was RMB27,217 million. In addition, substantially all of our term deposits with banks allow us to withdraw funds on deposit, subject to a penalty interest charge. As of December 31, 2004, the amount of term deposits was RMB175,498 million.

Our portfolio of investment securities also may provide us with a source of liquidity to meet unexpected cash outflows. As of December 31, 2004, investments in fixed maturity securities had a fair value of RMB150,351 million. As of December 31, 2004, investments in equity securities, primarily through securities investment funds, had a fair value of RMB17,271 million. However, the PRC securities market is still at an early stage of development, and we are subject to market liquidity risk because the market capitalization and trading volumes of the public exchanges are much lower than in more developed financial markets. We also are subject to market liquidity risk due to the large size of our investments in some of the markets in which we invest. We believe that some of our positions in our investment securities may be large enough to have an influence on the market value. These factors may limit our ability to sell these investments at an adequate price, or at all.

Liquidity Uses

Our principal cash outflows primarily relate to the liabilities associated with our various life insurance, annuity and accident and health insurance products, dividend and interest payments on our insurance policies and annuity contracts, operating expenses, income taxes and dividends that may be declared and payable to our shareholders. Liabilities arising from our insurance activities primarily relate to benefit payments under these insurance products, as well as payments for policy surrenders, withdrawals and loans.

We believe that our sources of liquidity are sufficient to meet our current cash requirements.

Consolidated Cash Flows

The following sets forth information regarding consolidated cash flows for the periods indicated.

Net Cash provided by operating activities was RMB32,914 million in 2004, a decrease from RMB38,510 million in 2003. This decrease was primarily due to the effect of the restructuring described above.

Net cash used in investing activities was RMB120,526 million in the year ended December 31, 2004 and RMB105,166 million in the year ended December 31, 2003. The increases in cash used in investing activities over all of these periods were primarily due to the growth in premiums and deposits.

Net cash provided by financing activities was RMB72,213 million in the year ended December 31, 2004 and RMB94,743 million in the year ended December 31, 2003. The changes in cash provided by financing activities over these periods were primarily due to the growth in deposits. In addition, our global share offering in December 2003 provided cash proceeds of approximately RMB24,707 million. As of December 31, 2004, a substantial part of the cash proceeds from our global offering was held in bank deposit accounts overseas, and the rest was held in bank deposit accounts as structured deposits in foreign currency in China. We expect to use such proceeds for general corporate purposes and to strengthen our capital base.

Insurance Solvency Requirements

The solvency ratio of an insurance company is a measure of capital adequacy, which is calculated by dividing the actual solvency level of the company (which is its admissible assets less admissible liabilities, determined in accordance with PRC GAAP and relevant rules) by the minimum solvency level it is required to meet. The following table shows the Company's solvency ratio as of December 31, 2004:

As of December 31, 2004
(RMB million,
except percentage data)

Actual solvency	54,456
Minimum solvency	17,264
Solvency ratio	315%

Insurance companies are required to calculate and report annually to the CIRC their solvency level and twelve additional financial ratios to assist it in monitoring the financial condition of insurers. A "usual range" of results for each of the twelve ratios is used as a benchmark. The departure from the "usual range" of four or more of the ratios can lead to regulatory action being taken by the CIRC.

The Company's solvency level as of December 31, 2004 was approximately 3.15 times the minimum regulatory requirement and nine applicable financial ratios were within their usual ranges. Among the twelve financial ratios, the calculation of three other ratios requires financial data of two previous years, and the Company was accordingly not able to calculate such three ratios for the year of 2004 because it was just established in 2003.





Extensive Reach

