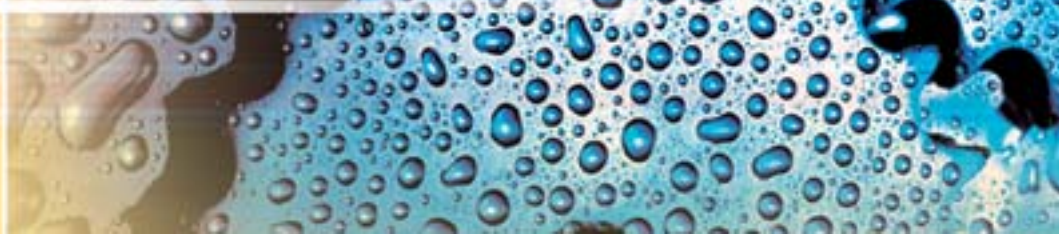




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INNOVATION



# Report of the Directors

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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.

# Report of the Directors *(Continued)*

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## 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.

# Report of the Directors *(Continued)*

## 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

# Report of the Directors (Continued)

## 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.

# Report of the Directors *(Continued)*

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## **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.

# Report of the Directors (Continued)

## 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.



# Report of the Directors *(Continued)*

## 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.

# Report of the Directors *(Continued)*

## 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.

# Report of the Directors *(Continued)*

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## 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