

OVERVIEW

The Company is a leading property and casualty insurance company in the PRC providing a broad range of property and casualty insurance products and accidental injury insurance products for customers. In the first half of 2004, the Company's market share in the property and casualty insurance market was 63.3%.

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

| | Six months ended 30 June | |
|----------------------------------|--------------------------|-------------------|
| | 2004 | 2003 ² |
| | <i>(RMB in million)</i> | |
| Net premiums earned | 24,206 | 19,930 |
| Underwriting profit ¹ | 1,429 | 1,461 |
| Net profit | 963 | 1,321 |
| Total assets | 93,705 | 80,288 |

1 Underwriting profit represents net premiums earned minus net claims incurred, and after amortisation of deferred acquisition costs, insurance protection expense and general and administrative expenses.

2 The comparative figures for the six months ended 30 June 2003 and the value of total assets as of 30 June 2003 were extracted from the Accountant's Report as set out in the Company's prospectus.

RESULTS OF OPERATIONS

In the first half of 2004, the Company's turnover increased rapidly, underwriting profit remained flat, and investment return decreased significantly.

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

| | Six months ended 30 June | |
|--|--------------------------|--------|
| | 2004 | 2003 |
| | (%) | |
| Net premiums earned | 100.0 | 100.0 |
| Net claims incurred | (72.7) | (71.5) |
| Amortisation of deferred acquisition costs | (6.7) | (5.2) |
| Insurance protection expense | (1.3) | (1.3) |
| General and administrative expenses | (13.4) | (14.7) |
| Underwriting profit | 5.9 | 7.3 |
| Interest and dividend income | 2.1 | 1.5 |
| Net gains/(losses) on trading and non-trading securities | (2.1) | 1.2 |
| Finance costs | (0.3) | (0.1) |
| Interest expense credited to policyholders' deposits | (0.3) | (0.3) |
| Profit before taxation | 5.3 | 9.6 |
| Tax | (1.3) | (3.0) |
| Net profit | 4.0 | 6.6 |
| Loss ratio | 72.7% | 71.5% |
| Expense ratio | 21.4% | 21.2% |
| Combined ratio | 94.1% | 92.7% |

OPERATING RESULTS BY SEGMENT

The following table sets forth the net premiums earned, net claims incurred and amortisation of deferred acquisition costs by segment, analysed as percentages, for the periods indicated.

| | Six months ended 30 June | |
|---|--------------------------|--------------|
| | 2004 | 2003 |
| | (%) | |
| Net premiums earned | | |
| Motor vehicle | 67.7 | 65.4 |
| Commercial property | 13.4 | 17.3 |
| Homeowners | 1.6 | 3.0 |
| Other | 17.3 | 14.3 |
| Total | 100.0 | 100.0 |
| Net claims incurred | | |
| Motor vehicle | 80.2 | 75.1 |
| Commercial property | 7.1 | 11.3 |
| Homeowners | 0.6 | 1.2 |
| Other | 12.1 | 12.4 |
| Total | 100.0 | 100.0 |
| Amortisation of deferred acquisition costs | | |
| Motor vehicle | 81.7 | 87.0 |
| Commercial property | 8.2 | 5.8 |
| Homeowners | 2.9 | 7.5 |
| Other | 7.2 | (0.3) |
| Total | 100.0 | 100.0 |

TURNOVER

Turnover of the Company reached RMB35,389 million in the first half of 2004, representing an increase of 15.5% compared to RMB30,651 million in the first half of 2003. The increase was primarily due to a RMB4,810 million increase in turnover of the motor vehicle segment.

NET PREMIUMS EARNED

Net premiums earned of the Company reached RMB24,206 million in the first half of 2004, representing an increase of 21.5% compared to RMB19,930 million in the first half of 2003. The increase was primarily due to an increase in turnover and a decrease in premiums ceded, which was partially offset by an increase in the change in net unearned premium reserves. Premiums ceded decreased from RMB5,720 million, or 18.7% of turnover, in the first half of 2003 to RMB4,803 million, or 13.6% of turnover, in the first half of 2004. The decrease was primarily due to a reduction in the statutory reinsurance rate from 15% in 2003 to 10% in 2004 under the requirements set out in the WTO Accession Protocol signed by the PRC. The increase in net unearned premium reserves in the first half of 2004 compared to the first half of 2003 was primarily due to the increase in net premiums written, which was in turn due to the increase in turnover and the decrease in premiums ceded.

INTEREST AND DIVIDEND INCOME

Interest and dividend income of the Company reached RMB519 million in the first half of 2004, representing an increase of 72.4% compared to RMB301 million in the first half of 2003. The increase was primarily due to an increase in interest income from trading and non-trading securities and interest income from bank deposits of RMB146 million and RMB74 million, respectively. The increase in interest income from trading and non-trading securities was primarily due to an increase of RMB5,059 million in investments in debt securities in the first half of 2004 compared to the first half of 2003 (please refer to Accountant's Report as set out in the Company's prospectus for the value of investment in debt securities at 30 June 2003). The increase in interest income from bank deposits was mainly due to an increase of RMB2,320 million in higher interest-bearing structured deposits included in deposits with banks and other financial institutions with original maturity of more than three months.

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

The Company's net losses on trading and non-trading securities amounted to RMB514 million in the first half of 2004, decreased RMB744 million compared to a net gain of RMB230 million in the first half of 2003. This was primarily due to a decrease in unrealised gain on trading securities. The unrealised gains in respect of mutual funds and debt securities decreased RMB641 million and RMB107 million, respectively, as a result of the subdued PRC securities markets.

NET CLAIMS INCURRED

The Company's net claims incurred amounted to RMB17,586 million in the first half of 2004, representing an increase of 23.4% compared to RMB14,253 million in the first half of 2003. Loss ratio increased to 72.7% in the first half of 2004 compared to 71.5% in the first half of 2003. The increase was primarily due to a 31.6% increase in net claims incurred in the motor vehicle segment to RMB14,096 million in the first half of 2004 compared to RMB10,708 million in the first half of 2003. The increase was partially offset by a decrease in net claims incurred in the commercial property, liability, cargo and homeowners segments in the first half of 2004. Loss and loss adjustment expense reserves as of 30 June 2004 increased by RMB1,945 million as compared to 31 December 2003, due partly to an increase of RMB963 million in the loss and loss adjustment expense reserves for claims that occurred prior to 31 December 2003, after comparing the latest actuarial results as of 30 June 2004 to the actuarial results as of 31 December 2003.

AMORTISATION OF DEFERRED ACQUISITION COSTS

Amortisation of deferred acquisition costs amounted to RMB1,626 million in the first half of 2004, representing an increase of 58.0% compared to RMB1,029 million in the first half of 2003. The increase was primarily due to an increase of RMB555 million in commission expenses to insurance intermediaries and agents and a decrease of RMB338 million in reinsurance commission in the first half of 2004 compared to the first half of 2003. The increase in commission expenses was primarily due to the increase in turnover and the decrease in reinsurance commission was primarily due to the decrease in premiums ceded.

INSURANCE PROTECTION EXPENSE

According to the relevant PRC insurance law and regulations, the Company is required to accrue an insurance protection fund based on 1% of its retained premiums. Insurance protection expense of the Company amounted to RMB325 million in the first half of 2004, representing an increase of 26.0% compared to RMB258 million in the first half of 2003. The 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 RMB78 million in the first half of 2004, representing an increase of 34.5% compared to RMB58 million in the first half of 2003. The increase was primarily due to an increase in deposits obtained from Golden Bull homeowners insurance products. Policyholders' deposits amounted to RMB9,154 million as of 30 June 2004, representing an increase of RMB1,133 million compared to RMB8,021 million as of 30 June 2003.

FINANCE COSTS

Finance costs amounted to RMB66 million in the first half of 2004, representing an increase of RMB55 million compared to RMB11 million in the first half of 2003. The increase was primarily due to a RMB2,000 million subordinated loan issued by the Company in the second half of 2003, resulting in an increase in interest expense of RMB50 million.

GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses of the Company amounted to RMB3,240 million in the first half of 2004, representing an increase of 10.6% compared to RMB2,929 million in the first half of 2003. The increase was primarily due to an increase of RMB171 million in personnel expenses, an increase of RMB52 million in operating lease charges and an increase of RMB67 million in provision for doubtful accounts.

PROFIT BEFORE TAX

Profit before tax amounted to RMB1,290 million in the first half of 2004, representing a decrease of 32.9% compared to RMB1,923 million in the first half of 2003. The decrease was primarily due to a RMB744 million decrease in net gain on trading and non-trading securities, which was partially offset by an increase of 72.4% in interest and dividend income to RMB519 million in the first half of 2004 compared to RMB301 million in the first half of 2003.

TAX

Tax was RMB327 million in the first half of 2004, representing a decrease of RMB275 million compared to RMB602 million in the first half of 2003. The Company's effective tax rate was 25.3% in the first half of 2004 compared to 31.3% in the first half of 2003, primarily due to an increase in non-taxable interest income from government bonds in the first half of 2004.

NET PROFIT

Overall, the Company's net profit decreased 27.1% to RMB963 million in the first half of 2004 compared to RMB1,321 million in the first half of 2003. Basic earnings per share in the first half of 2004 was RMB0.086.

COMBINED RATIO

The Company's combined ratio increased from 92.7% in the first half of 2003 to 94.1% in the first half of 2004, primarily due to an increase in loss ratio from 71.5% in the first half of 2003 to 72.7% in the first half of 2004 and an increase in expense ratio from 21.2% in the first half of 2003 to 21.4% in the first half of 2004.

RESULTS OF SEGMENT OPERATIONS

Motor Vehicle Insurance

| | Six months ended 30 June | |
|---|--------------------------|----------|
| | 2004 | 2003 |
| | <i>(RMB in million)</i> | |
| Turnover | 24,197 | 19,387 |
| Net premiums earned | 16,377 | 13,028 |
| Net claims incurred | (14,096) | (10,708) |
| Amortisation of deferred acquisition costs | (1,328) | (895) |
| Insurance protection expense | (231) | (168) |
| Segment profit before unallocated income and expenses | 722 | 1,257 |
| Loss ratio | 86.1% | 82.2% |
| Segment expense ratio | 9.5% | 8.2% |
| Segment combined ratio | 95.6% | 90.4% |

Turnover of the motor vehicle segment increased 24.8% to RMB24,197 million in the first half of 2004 compared to RMB19,387 million in the first half of 2003. This increase was primarily due to an increase in the number of motor vehicles insured and the increase in premium rates. The Company insured 11.79 million motor vehicles in the first half of 2004, representing an increase of 2.42 million compared to the first half of 2003.

Net premiums earned of the motor vehicle segment amounted to RMB16,377 million in the first half of 2004, representing a 25.7% increase compared to RMB13,028 million in the first half of 2003. The increase was primarily due to the increase in turnover and the decrease in reinsurance premiums ceded. However, this was partially offset by the corresponding increase in the change in net unearned premium reserves.

Net claims incurred of the motor vehicle segment increased 31.6% to RMB14,096 million in the first half of 2004 from RMB10,708 million in the first half of 2003. Loss ratio increased to 86.1% in the first half of 2004 compared to 82.2% in the first half of 2003. The increase in net claims incurred was due to a number of factors including the continuing effect of the deregulation in the terms and premium rates of motor vehicle insurance, changes in laws governing road traffic control and compensation for personal injury, increasing number of private motor vehicles, increasing number of new drivers and the failure to improve road conditions to accommodate increasing traffic volume, as well as the substantial increase in small claims leading to an increase in claims settlement expenses. The number of claims for motor vehicle insurance increased substantially in the first half of 2004. However, the effect of such increase on net claims incurred was partially offset by the decrease in average payment per claim. Loss and loss adjustment expense reserves of the motor vehicle segment as of 30 June 2004 increased RMB1,477 million compared to 31 December 2003, primarily due to the deregulation of terms and premium rates of the motor vehicle insurance, which came into effect in the PRC in January 2003. The Company increased the loss and loss adjustment expense reserves for motor vehicle insurance claims that occurred prior to 31 December 2003 by RMB1,178 million, after comparing the latest actuarial results as of 30 June 2004 to the actuarial results as of 31 December 2003.

Amortisation of deferred acquisition costs charged to the motor vehicle segment increased 48.4% to RMB1,328 million in the first half of 2004 compared to RMB895 million in the first half of 2003. The increase was primarily due to the increase in turnover causing a corresponding increase in commission expenses, and the decrease in reinsurance commission.

Insurance protection expense charged to the motor vehicle segment increased 37.5% to RMB231 million in the first half of 2004 compared to RMB168 million in the first half of 2003 due to an increase in retained premiums.

Due to an increase in amortisation of deferred acquisition costs and an increase in insurance protection expense, the expense ratio of the motor vehicle segment increased to 9.5% in the first half of 2004 compared to 8.2% in the first half of 2003.

Overall, the motor vehicle segment recorded a RMB722 million profit before unallocated income and expenses in the first half of 2004, representing a decrease of 42.6% compared to RMB1,257 million in the first half of 2003.

Commercial Property Insurance

| | Six months ended 30 June | |
|---|--------------------------|---------|
| | 2004 | 2003 |
| <i>(RMB in million)</i> | | |
| Turnover | 5,145 | 5,221 |
| Net premiums earned | 3,238 | 3,441 |
| Net claims incurred | (1,248) | (1,605) |
| Amortisation of deferred acquisition costs | (133) | (60) |
| Insurance protection expense | (45) | (42) |
| Segment profit before unallocated income and expenses | 1,812 | 1,734 |
| Loss ratio | 38.5% | 46.6% |
| Segment expense ratio | 5.5% | 3.0% |
| Segment combined ratio | 44.0% | 49.6% |

Turnover of the commercial property segment decreased 1.5% to RMB5,145 million in the first half of 2004 compared to RMB5,221 million in the first half of 2003, primarily due to a decrease in average premium rates resulting from intense market competition, and also due to reduction of exposure to certain high risk customers with an objective to improve underwriting quality.

Net premiums earned of the commercial property segment reached RMB3,238 million in the first half of 2004, representing a 5.9% decrease compared to RMB3,441 million in the first half of 2003. The decrease was primarily due to a decrease in the turnover and an increase in the change in net unearned premium reserves.

Net claims incurred of the commercial property segment decreased 22.2% to RMB1,248 million in the first half of 2004 compared to RMB1,605 million in the first half of 2003. The Company has introduced stringent measures on underwriting criteria in relation to commercial property segment to monitor risk exposure and reduce underwriting risks. These measures led to an improvement in the results of the Company's commercial property segment and a reduction in claims. In addition, the Company also successfully reduced net claims incurred by adding limitations to the scope of liabilities and by reducing exposure to catastrophe losses. The decrease in net claims incurred was larger than the decrease in net premiums earned, resulting in an improvement in loss ratio for the commercial property segment from 46.6% in the first half of 2003 to 38.5% in the first half of 2004.

Amortisation of deferred acquisition costs charged to the commercial property segment increased 121.7% to RMB133 million in the first half of 2004 compared to RMB60 million in the first half of 2003. It was primarily because the premium income of the commercial property segment was recognised in a faster manner in the first half of 2004 when compared to the first half of 2003, causing a decrease in the ratio of unearned premium reserves to gross premiums written. The amount of acquisition costs to be deferred decreased accordingly.

Insurance protection expense charged to the commercial property segment increased 7.1% to RMB45 million in the first half of 2004 compared to RMB42 million in the first half of 2003, primarily due to an increase in retained premiums.

Due to an increase in amortisation of deferred acquisition costs and an increase in insurance protection expense, the segment expense ratio of the commercial property segment increased to 5.5% in the first half of 2004 compared to 3.0% in the first half of 2003.

Overall, the commercial property segment recorded a RMB1,812 million profit before unallocated income and expenses in the first half of 2004, representing an increase of 4.5% compared to RMB1,734 million in the first half of 2003.

Homeowners Insurance

| | Six months ended 30 June | |
|--|--------------------------|-------|
| | 2004 | 2003 |
| | <i>(RMB in million)</i> | |
| Turnover | 793 | 736 |
| Net premiums earned | 378 | 604 |
| Net claims incurred | (103) | (178) |
| Amortisation of deferred acquisition costs | (47) | (77) |
| Interest and dividend income | 53 | 99 |
| Net gains/(losses) on trading and non-trading securities | (7) | 58 |
| Interest expense credited to policyholders' deposits | (78) | (58) |
| Insurance protection expense | (8) | (7) |
| Segment profit before unallocated income and expenses | 188 | 441 |
| Loss ratio | 27.3% | 29.5% |
| Segment expense ratio | 14.6% | 13.9% |
| Segment combined ratio | 41.9% | 43.4% |

Turnover of the homeowners segment increased 7.7% to RMB793 million in the first half of 2004 compared to RMB736 million in the first half of 2003. The increase was primarily due to the increased effort in expanding the homeowners insurance market.

Net premiums earned of the homeowners segment decreased 37.4% to RMB378 million in the first half of 2004 compared to RMB604 million in the first half of 2003. The decrease was primarily due to an increase in the number of policies with longer insurance periods. The percentage of premium income in respect of policies incepting with longer insurance periods increased from 23.8% in the first half of 2003 to 55.9% in the first half of 2004, resulting in a significant increase in unearned premium reserves.

Net claims incurred of the homeowners segment decreased 42.1% to RMB103 million in the first half of 2004 compared to RMB178 million in the first half of 2003. Loss ratio decreased to 27.3% in the first half of 2004 compared to 29.5% in the first half of 2003, primarily due to a decrease in net claims incurred.

Amortisation of deferred acquisition costs charged to the homeowners segment decreased 39.0% to RMB47 million in the first half of 2004 compared to RMB77 million in the first half of 2003. The decrease was primarily due to an increase in the premium income with longer insurance periods, causing an increase in the ratio of unearned premium reserves to gross premiums written.

Insurance protection expense charged to the homeowners insurance segment increased to RMB8 million in the first half of 2004 compared to RMB7 million in the first half of 2003, primarily due to an increase in retained premiums.

The segment expense ratio of the homeowners segment increased to 14.6% in the first half of 2004 compared to 13.9% in the first half of 2003.

The interest and dividend income deriving from policyholders' deposits of the homeowners segment decreased RMB46 million to RMB53 million in the first half of 2004 compared to RMB99 million in the first half of 2003, mainly because the increase in interest and dividend income deriving from the deposits obtained from Golden Bull homeowners insurance products was less than the increase in fixed rate interest paid to the policyholders.

Interest expense credited to policyholders' deposits of the homeowners segment increased 34.5% to RMB78 million in the first half of 2004 from RMB58 million in the first half of 2003, mainly due to an increase in deposits obtained from Golden Bull homeowners insurance products.

Overall, the homeowners segment recorded a RMB188 million profit before unallocated income and expenses in the first half of 2004, representing a decrease of 57.4% compared to RMB441 million in the first half of 2003.

Other Insurance Segments

The Company's other insurance segments include cargo, liability, accidental injury, aviation, construction, marine hull and oil and gas, etc.

| | Six months ended 30 June | |
|---|--------------------------|--------------|
| | 2004 | 2003 |
| | <i>(RMB in million)</i> | |
| Turnover | | |
| Cargo | 1,527 | 1,555 |
| Liability | 1,094 | 1,412 |
| Accidental injury | 836 | 849 |
| Other | 1,797 | 1,491 |
| Total | 5,254 | 5,307 |
| Net premiums earned | | |
| Cargo | 1,710 | 1,177 |
| Liability | 942 | 1,112 |
| Accidental injury | 851 | 37 |
| Other | 710 | 531 |
| Total | 4,213 | 2,857 |
| Net claims incurred | (2,139) | (1,762) |
| Amortisation of deferred acquisition costs | (118) | 3 |
| Insurance protection expense | (41) | (41) |
| Segment profit before unallocated income and expenses | 1,915 | 1,057 |
| Loss ratio | 50.8% | 61.7% |
| Segment expense ratio | 3.8% | 1.3% |
| Segment combined ratio | 54.6% | 63.0% |

Turnover of the other insurance segments decreased 1.0% to RMB5,254 million in the first half of 2004 compared to RMB5,307 million in the first half of 2003. The decrease was primarily due to a fall in turnover of the liability segment by 22.5% in the first half of 2004 compared to the first half of 2003, which was primarily due to the promulgation and implementation of the "Regulations on Industrial Accident Insurance" in the first half of 2004, largely impacting employers' commercial liabilities and the operating results of the liability segment.

Net premiums earned of the other insurance segments increased 47.5% to RMB4,213 million in the first half of 2004 compared to RMB2,857 million in the first half of 2003. This increase was primarily due to a decrease in change in net unearned premium reserves, causing an increase of RMB814 million in net premiums earned of the accidental injury insurance segment and an increase of RMB533 million in net premiums earned of the cargo segment; and also due to a decrease of RMB86 million in premiums ceded.

Net claims incurred of the other insurance segments increased 21.4% to RMB2,139 million in the first half of 2004 compared to RMB1,762 million in the first half of 2003. The increase in net claims incurred was primarily due to an increase of RMB522 million in net claims incurred of the accidental injury segment. Net claims incurred of the accidental injury segment increased mainly because the Company entered into the accidental injury insurance market in the first half of 2003, whilst the turnover was comparatively low and the number of claims was small. By introducing stringent measures on underwriting criteria and improving claims management, the loss ratio of the other insurance segments decreased to 50.8% in the first half of 2004 compared to 61.7% in the first half of 2003.

Amortisation of deferred acquisition costs charged to other insurance products amounted to RMB118 million in the first half of 2004. There was a write-back of RMB3 million in the first half of 2003 due to reinsurance commission.

Insurance protection expense charged to the other insurance segments was RMB41 million in the first half of 2004, the same as that in the first half of 2003.

Overall, the other insurance segments recorded a RMB1,915 million profit before unallocated income and expenses, representing an increase of 81.2% compared to RMB1,057 million in the first half of 2003.

GEARING RATIO

As of 30 June 2004, the gearing ratio³ of the Company was 79.4%, representing an increase of 1.6 percentage points compared to 77.8% as of 31 December 2003.

DEVELOPMENT OF NEW PRODUCTS

In the first half of 2004, the Company developed 94 new insurance coverages in, amongst others, liability insurance, accidental injury insurance, motor vehicle insurance and commercial property insurance product lines, of which 26 are stand-alone coverages and 68 are supplementary coverages.

In the second half of 2004, the Company will strengthen its market research, focus on targeted customer groups and specific channels, and design customised products. The Company will also actively strengthen its cooperation with American International Group, Inc. ("AIG"), improve the product design of accidental injury and short-term health insurance and focus on the pilot launch of such products.

CASH FLOW

| | Six months ended 30 June | |
|---|--------------------------|---------|
| | 2004 | 2003 |
| | <i>(RMB in million)</i> | |
| Net cash inflow from operating activities | 8,102 | 7,286 |
| Net cash outflow from investing activities | (3,132) | (2,182) |
| Net cash inflow/(outflow) from financing activities | (839) | 1,064 |
| Net increase in cash and cash equivalents | 4,131 | 6,168 |

³ Gearing ratio is defined as total liabilities (excluding subordinated loan) divided by total assets.

Net cash generated from operating activities in the first half of 2004 was RMB8,102 million, representing an increase of 11.2% compared to the first half of 2003. The increase was primarily due to an increase in premiums received in cash in the first half of 2004, which was partially offset by an increase in claims payment in cash.

Net cash used by the Company in investing activities in the first half of 2004 was RMB3,132 million, representing an increase of RMB950 million compared to the first half of 2003. Such increase was primarily due to an increase in funds used for purchasing trading and non-trading securities and held-to-maturity securities.

Net cash used by the Company in financing activities in the first half of 2004 was RMB839 million. Net cash generated from financing activities in the first half of 2003 was RMB1,064 million. The increase in net cash used in financing activities was primarily due to the payment of RMB644 million special dividend to the Company's ultimate holding company, PICC Holding Company, in the first half of 2004.

Net increase in cash and cash equivalents of the Company in the first half of 2004 was RMB4,131 million, representing a decrease of 33.0% compared to the first half of 2003.

LIQUIDITY

The Company's cash flow is primarily derived from the cash generated from operating activities, mainly cash from insurance premiums received. Additional liquidity sources include interest and dividend income, proceeds from matured investments, disposal of assets and financing activities. The Company's liquidity needs consist principally of payment of claims and other obligations under outstanding insurance policies, capital expenditure, operating expenses, tax payments, dividend payments and investment needs.

The Company has entered into a subordinated loan agreement with China Development Bank on 10 October 2003 in respect of RMB2,000 million. This loan is unsecured and bears interest at a rate which is equal to 90% of the 5-year lending rate fixed by the People's Bank of China. The loan comes due in November 2023.

The Company obtained a 10-year revolving credit facility from China Development Bank for up to RMB10 billion on 26 August 2003. Each drawdown made under that facility is repayable within one year. As of the date of this interim report, no amount has been drawn down under that facility.

Save for the subordinated loan and the credit facility mentioned above, the Company does not obtain working capital by borrowing.

The Company expects that it can fund its working capital needs in the future from cash generated from operating activities. The Board of Directors is of the opinion that the Company has sufficient working capital.

CAPITAL EXPENDITURE

The capital expenditure of the Company has primarily been for property construction, acquisition of motor vehicles and development of information systems. Capital expenditure was RMB103 million in the first half of 2004.

Save for the plan for a new headquarters building mentioned in the Company's 2003 Annual Report, there were no other material capital expenditure in the first half of 2004. The Company believes that it has sufficient capital resources to fully satisfy its capital expenditure plan and its working capital requirements.

CONTINGENT LIABILITIES

Owing to the nature of the insurance business, the Company is involved in legal proceedings in the ordinary course of business, as plaintiff or defendant. Such legal proceedings mostly involve claims on the Company's insurance policies. While the outcomes of such contingencies or legal 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.

INTEREST RATE RISK

The Company's holding in fixed income investments is subject 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 mutual funds is also exposed to price fluctuations caused by changes in interest rates. The Company manages exposure to risks associated with interest rate fluctuations through active review of the investment portfolio and consultation with financial investment experts. The goal is to maintain liquidity and to generate stable returns.

CREDIT RISK

The Company is subject to credit risk on investments such as corporate bonds and mutual funds. The Company diligently manages credit risk by analysing the creditworthiness of companies prior to making investments as well as strictly following the CIRC guidelines which only permit investments in corporate bonds with rating higher than AA. The Company is also subject to credit risk with respect to amounts owed to it by reinsurers. As a result, except when dealing with national reinsurers such as China Property and Casualty Reinsurance Company Ltd., the Company only purchases reinsurance from reinsurers with A.M. Best ratings of at least A-, and pays particular attention to their creditworthiness and financial condition.

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 the Company's capital account are subject to foreign exchange regulations and require the approval of the State Administration of Foreign Exchange. Foreign exchange policies adopted by the PRC government could cause future exchange rates to vary.

HEDGING INSTRUMENTS

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.

LOOKING FORWARD

The Company anticipates its results of operations to improve in the second half of 2004 over the same period last year. In order to maximise value for shareholders, the Company will focus on refining the “three centers” (the underwriting center, claims center, and finance center), accelerating settlement of claims while maintaining quality of underwriting and claims, improving the application of information technology, strengthening actuarial ability, adjusting its business structure to focus more on profitable non-motor vehicle insurance business. The Company will also enhance its cooperation with AIG and refine the pilot launch of the accidental injury and short-term health insurance products. The Company will further enhance its risk control in its use of funds to improve investment profitability.