

Report of the directors

The directors have pleasure in presenting their annual report and the audited financial statements of Pacific Century Insurance Holdings Limited (the "Company") and its subsidiaries (the "Group") for the year ended 31 December 2006.

Principal activities

The principal activity of the Company is investment holding.

The Group is principally engaged in the provision of a range of whole life, endowment and unit-linked insurance products to individuals in Hong Kong as well as being engaged in asset management. The Group also provides a range of other related products, including term life, accident, medical and disability insurance, to individuals and employee groups, and general insurance products through agency arrangements.

In June 2002, Pacific Century Insurance Company Limited ("PCI") (an indirect wholly-owned subsidiary of the Company) entered into an agreement for the transfer of its Mandatory Provident Fund business to HSBC Life (International) Limited ("HSBC Life"). The related activities have been accounted for as a discontinued operation in the current year's financial statements, details of which are set out in note 13 to the financial statements.

Results and dividends

The Group's profit for the year ended 31 December 2006 and the state of affairs of the Company and the Group as at that date are set out in the financial statements on pages 43 to 118.

An interim dividend of HK\$0.03 per ordinary share was paid on 29 September 2006. The directors did not recommend payment of final dividend for the year ended 31 December 2006.

Summary of financial information

A summary of the published results and assets and liabilities of the Group for the last five financial years, as extracted from the audited financial statements and reclassified as appropriate, is set out on page 119. This summary does not form part of the audited financial statements.

Property, plant and equipment and investment properties

Details of movements in the property, plant and equipment and investment properties of the Group during the year are set out in notes 17 and 19 to the financial statements, respectively.

Share capital and share options

Details of movements in the Company's share capital and share options during the year are set out in notes 40 and 41 to the financial statements, respectively.

Pre-emptive rights

There are no provisions for pre-emptive rights under the Company's bye-laws, or the Companies Act 1981 of Bermuda (as amended), which would oblige the Company to offer new shares on a pro rata basis to existing shareholders.

Purchase, redemption or sale of listed securities of the Company

During the year, the Company repurchased certain of its shares on The Stock Exchange of Hong Kong Limited (the "Stock Exchange") and these shares were subsequently cancelled by the Company. Details of these transactions are as follows:

Month of purchase	Number of ordinary shares repurchased	Price per share		Aggregate consideration paid HK\$'000
		Highest HK\$	Lowest HK\$	
March 2006	18,288,000	3.775	3.15	65,326

The issued share capital of the Company was reduced by the par value thereof. The premium paid on the repurchase of the shares and the related expenses, in the amount of HK\$17,601,000, were charged to the share premium account and the balance of HK\$29,719,000 was charged to the retained profits account. Further details of these transactions are set out in note 40 to the financial statements.

The repurchase of the Company's shares during the year was effected by the directors pursuant to the mandate from shareholders received at the previous annual general meeting, with a view of benefiting shareholders as a whole by enhancing the net asset value per share and earnings per share of the Group.

Except as disclosed above, neither the Company nor any of its subsidiaries purchased, redeemed or sold any of the Company's listed securities during the year.

Reserves

Details of movements in the reserves of the Company and the Group during the year are set out in note 42(b) to the financial statements and in the consolidated statement of changes in equity, respectively.

Distributable reserves

As at 31 December 2006, the Company's reserves available for cash distribution and/or distribution in specie, calculated in accordance with the provisions of the Companies Act 1981 of Bermuda (as amended), amounted to HK\$99,363,000. In accordance with the Companies Act 1981 of Bermuda (as amended), the contributed surplus may be distributed under certain circumstances. In addition, the Company's share premium account, in the amount of HK\$20,202,000 as at 31 December 2006, may be distributed in the form of fully paid bonus shares.

Charitable contributions

During the year, the Group supported a wide variety of charities and activities beneficial to the community. Charitable contributions made by the Group during the year amounted to HK\$90,000 (2005: HK\$278,000).

Major customers

In the year under review, the aggregate income attributable to the Group's five largest customers was less than 30% of the total income for the year.

Directors

The directors of the Company during the year and up to the date of this report were listed below:

Executive directors:

YUEN Tin Fan, Francis

CHAN Ping Kan, Raymond

Alexander Anthony ARENA

(Retired on 21 April 2006)

CHEUNG Sum, Sam

(Resigned on 23 February 2006)

SO Wing Hung, Peter

Non-executive directors:

Peter Anthony ALLEN

(Re-designated on 1 March 2006)

CHUNG Cho Yee, Mico

(Re-designated on 17 March 2006)

FENG Xiaozeng

(Re-designated on 17 March 2006)

ZHENG Changyong

(Re-designated on 17 March 2006)

Independent non-executive directors:

CHANG Hsin Kang

Timothy George FRESHWATER

WANG Xianzhang

(Re-designated on 17 March 2006)

WONG Yue Chim, Richard

In accordance with bye-law 100 of the Company's bye-laws, Messrs SO Wing Hung, Peter, CHUNG Cho Yee, Mico, ZHENG Changyong and Professor WONG Yue Chim, Richard will retire by rotation and, being eligible, will offer themselves for re-election at the forthcoming annual general meeting.

The Company has received annual confirmations of independence from Professor CHANG Hsin Kang, Mr Timothy George FRESHWATER, Mr WANG Xianzhang and Professor WONG Yue Chim, Richard and as at the date of this report still considers them to be independent.

Directors' and senior management's biographies

Biographical details of the directors of the Company and the senior management of the Group are set out on pages 6 to 9 of the annual report.

Directors' service contracts

No director proposed for re-election at the forthcoming annual general meeting has a service contract with the Company which is not determinable by the Company within one year without payment of compensation, other than statutory compensation.

Directors' remuneration

The directors' fees and other emoluments are determined by the Company's board of directors, under the power delegated by the shareholders at general meetings, with reference to directors' duties and responsibilities and performance and the results of the Group.

Directors' interests in contracts

No director had a material interest, either directly or indirectly, in any contract of significance to the business of the Group to which the Company, its holding companies, or any of its subsidiaries or fellow subsidiaries was a party during the year.

Directors' and chief executive's interests in shares and underlying shares

As at 31 December 2006, the interests of the directors and chief executive in the share capital and underlying shares of the Company or its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")), as recorded in the register required to be kept by the Company pursuant to Section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code"), were as follows:

Long positions in ordinary shares of the Company:

Name of director	Notes	Number of shares held, capacity and nature of interest				Total	Percentage of the Company's issued share capital
		Directly beneficially owned	Through spouse or minor children	Through controlled corporation	Held by a trust		
YUEN Tin Fan, Francis	(a)	—	—	—	21,204,800	21,204,800	2.60
SO Wing Hung, Peter	(b)	—	—	—	276,000	276,000	0.03
Peter Anthony ALLEN		360,000	—	—	—	360,000	0.04
		360,000	—	—	21,480,800	21,840,800	2.67

Notes:

(a) These shares are held under T.F. Yuen Trust, a discretionary trust of which Mr YUEN Tin Fan, Francis is a founder.

(b) These shares are held by a trust, the beneficiaries of which are the family members of Mr SO Wing Hung, Peter.

The interests of the directors and the chief executive in the share options of the Company are disclosed in note 41 to the financial statements.

Directors' and chief executive's interests in shares and underlying shares (continued)

Long positions in ordinary shares of the immediate holding company of the Company, Pacific Century Regional Developments Limited ("PCRD"):

Name of director	Number of shares held, capacity and nature of interest				Total	Percentage of the holding company's issued share capital
	Directly beneficially owned	Through spouse or minor children	Through controlled corporation	Held by a trust		
Peter Anthony ALLEN	5,010,000	—	—	—	5,010,000	0.16
CHUNG Cho Yee, Mico	8,000,000	—	—	—	8,000,000	0.26
	13,010,000	—	—	—	13,010,000	0.42

Long positions in underlying shares of PCRD:

Details of share options granted to the director of the Company under the share option schemes of PCRD were as follows:

Name of director	Date of grant of share options	Vesting period	Exercise period	Number of share options					
				Exercise price SGD	Outstanding as at 1 January 2006	Granted during the year	Exercised during the year	Lapsed/ cancelled during the year	Outstanding as at 31 December 2006
*Alexander Anthony ARENA	25 October 1999	25 October 2001 to 25 October 2005	25 October 2001 to 24 October 2009	0.7584	15,300,000	—	—	—	15,300,000

* Mr Alexander Anthony ARENA retired as a director of the Company on 21 April 2006.

Save as disclosed above, as at 31 December 2006, none of the directors and/or the chief executive had registered an interest or short position in the shares, underlying shares or debentures of the Company or any of its associated corporations that was required to be recorded pursuant to Section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code.

Directors' rights to acquire shares or debentures

Save as disclosed under the heading "Directors' and chief executive's interests in shares and underlying shares" above and in the share option scheme disclosures in note 41 to the financial statements, at no time during the year were rights to acquire benefits by means of the acquisition of shares in or debentures of the Company granted to any director or their respective spouse or minor children, or were any such rights exercised by them; or was the Company, its holding company, or any of its subsidiaries or fellow subsidiaries a party to any arrangement to enable the directors to acquire such rights in any other body corporate.

Share option schemes

The directors have estimated the values of the share options granted during the year, calculated using the Black-Scholes option pricing model as at the date of the grant of the options:

Category of grantee	Number of options granted during the year	Theoretical value of share options HK\$
Other employees	120,000	150,000

The Black-Scholes option pricing model is a generally accepted method of valuing options. The significant assumptions used in the calculation of the values of the share options during the year were as follows:

Exercise price (HK\$)	3.68
Dividend yield (%)	1.6273
Expected volatility (%)	30.52
Historical volatility (%)	30.52
Risk-free interest rate (%)	4.575
Expected life of option (year)	6 to 8
Weighted average share price at grant date (HK\$)	3.6517

The expected life of the options is based on the historical data and is not necessarily indicative of the exercise patterns that may occur. The expected volatility reflects the assumption that the historical volatility is indicative of future trends, which may also not necessarily be the actual outcome. The measurement dates used in the valuation calculations were the dates on which the options were granted.

The values of share options calculated using the Black-Scholes option pricing model are subject to certain fundamental limitations, due to the subjective nature of and uncertainty relating to a number of assumptions of the expected future performance input to the model, and certain inherent limitations of the model itself.

The value of an option varies with different variables of certain subjective assumptions. Any change to the variables used may materially affect the estimation of the fair value of an option.

Connected transactions and continuing connected transactions

During the year, the Company and the Group had connected and continuing connected transactions, certain details of which are disclosed in compliance with the requirements of Chapter 14A of the Listing Rules in note 47.

The independent non-executive directors of the Company have reviewed the continuing connected transactions set out in note 47 to the financial statements and have confirmed that these continuing connected transactions have been entered into (i) in the ordinary and usual course of business of the Group; (ii) on normal commercial terms or on terms no less favourable to the Group than terms available to or from (as appropriate) independent third parties; and (iii) in accordance with the relevant agreements governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

Sufficiency of public float

Based on information that is publicly available to the Company and within the knowledge of the directors, at least 25% of the Company's total issued share capital was held by the public as at 28 February 2007.

Directors' interests in competing businesses

During the year, the following directors have declared interests in the following businesses which compete, or are likely to compete, either directly or indirectly, with the businesses of the Group during the year:

Name of director	Name of companies	Competing business	Nature of interest
FENG Xiaozeng ^{Note}	China Insurance (Holdings) Company, Limited	Insurance holding	As the chairman
	China Insurance International Holdings Company Limited	Insurance holding	As the chairman
	CITIC International Financial Holdings Limited	Financial holding	As a non-executive director
	Tai Ping Life Insurance Company, Limited	Life insurance business	As a director
	TaiPing Pension Company Limited	Pension insurance business	As a director
	China International Reinsurance Company Limited	Reinsurance business	As the chairman
	The Ming An Insurance Company (Hong Kong), Limited	General insurance business	As a director
	The Ming An (Holdings) Company Limited	Insurance holding	As the chairman

Directors' interests in competing businesses (continued)

Name of director	Name of companies	Competing business	Nature of interest
ZHENG Changyong	China Insurance (Holdings) Company, Limited	Insurance holding	As a director
	China Insurance International Holdings Company Limited	Insurance holding	As a director
	China Insurance Service Japan Co., Ltd.	Insurance agency	As a director
	China Insurance Co. (Singapore) Pte. Ltd.	General insurance business	As a director
	CIG Trustees Limited	Trustee corporate	As a director
	The Ming An Insurance Company (Hong Kong), Limited	General insurance business	As a director
	PT China Insurance Indonesia	General insurance business	As a director
	China Life Insurance (Overseas) Company Limited	Life insurance business	As an independent non-executive director

Note: The respective date of appointment of Mr. FENG Xiaozeng's directorship during the year in the abovementioned companies are as follows:

Name of companies	Nature of interest	Date of appointment
CITIC International Financial Holdings Limited	As a non-executive director	Appointed as a non-executive director on 10 August 2006
The Ming An (Holdings) Company Limited	As the chairman	Appointed as a director on 5 September 2006 and appointed as chairman on 5 December 2006

All of the above companies, except China Life Insurance (Overseas) Company Limited and CITIC International Financial Holdings Limited, which are within the China Insurance (Holdings) Company Group, hold an 11.18% interest in the Company as disclosed in the section headed "Substantial shareholders' and other persons' interests in shares and underlying shares" below.

As the board of directors of the Company is independent from the boards of directors of the abovementioned companies and the above directors do not control the board of the Company, the Group is capable of carrying on its businesses independently of, and at arm's length from, the businesses of the abovementioned companies.

Substantial shareholders' and other persons' interests in shares and underlying shares

As at 31 December 2006, the following interests of 5% or more of the issued share capital of the Company were recorded in the register of interests required to be kept by the Company pursuant to Section 336 of the SFO:

Name	Notes	Number of ordinary shares held	Percentage of the Company's issued share capital
LI Tzar Kai, Richard	(1)	385,797,942 (L)	47.36 (L)
PCRD	(2)	383,797,942 (L)	47.11 (L)
Ocean Star Investment Management Limited	(2)	383,797,942 (L)	47.11 (L)
Ocean Star Management Limited	(2)	383,797,942 (L)	47.11 (L)
OS Holdings Limited	(2)	383,797,942 (L)	47.11 (L)
Star Ocean Ultimate Limited	(2)	383,797,942 (L)	47.11 (L)
The Ocean Trust	(2)	383,797,942 (L)	47.11 (L)
The Ocean Unit Trust	(2)	383,797,942 (L)	47.11 (L)
The Starlite Trust	(2)	383,797,942 (L)	47.11 (L)
The Starlite Unit Trust	(2)	383,797,942 (L)	47.11 (L)
Pacific Century Group Holdings Limited	(2)	383,797,942 (L)	47.11 (L)
China Insurance (Holdings) Company, Limited	(3)	91,060,000 (L)	11.18 (L)
King System Limited	(3)	49,907,200 (L)	6.13 (L)
Joyful Box Inc.	(3)	41,152,800 (L)	5.05 (L)

Remark: (L) – Long position

Notes:

- (1) These interests represent Mr LI Tzar Kai, Richard's deemed interests in: (a) 2,000,000 shares held by Pacific Century Diversified Limited, a wholly-owned subsidiary of Chiltonlink Limited, which is 100% owned by Mr LI Tzar Kai, Richard; and (b) 383,797,942 shares indirectly held by the trustee of two unit trusts (see note (2) below), the units of which are held by two discretionary trusts of which Mr LI Tzar Kai, Richard is the founder.
- (2) Each of Ocean Star Management Limited, OS Holdings Limited, Star Ocean Ultimate Limited, The Ocean Trust, The Ocean Unit Trust, The Starlite Trust, The Starlite Unit Trust and Pacific Century Group Holdings Limited ("PCGH") is deemed to have an interest under the SFO in the same 383,797,942 shares held by PCRD as it holds, directly or indirectly, a controlling interest in PCRD. Ocean Star Investment Management Limited is deemed under the SFO to have an interest in the same 383,797,942 shares held by PCRD by virtue of it being the manager of The Starlite Unit Trust and The Ocean Unit Trust which together hold 100% of the shares of PCGH. As at 31 December 2006, PCGH's controlling interest in PCRD was held through its controlled corporations (being its wholly-owned subsidiaries, Borsington Limited, Pacific Century International Limited, Pacific Century Group (Cayman Islands) Limited and Anglang Investments Limited, which together controlled 75.33% of the shares of PCRD).
- (3) China Insurance (Holdings) Company, Limited is taken to have an interest under the SFO in the same 91,060,000 shares beneficially owned by Joyful Box Inc. and King System Limited in aggregate.

No share options of the Company were held by the above shareholders as at the balance sheet date.

Substantial shareholders' and other persons' interests in shares and underlying shares

(continued)

Save as disclosed above, as at 31 December 2006, no person, other than the directors and the chief executive of the Company, whose interests are set out in the section headed "Directors' and chief executive's interests in shares and underlying shares" above, had registered an interest or short position in the shares or underlying shares of the Company that was required to be recorded pursuant to Section 336 of the SFO.

Post balance sheet events

Details of the significant post balance sheet events of the Group are set out in note 48 to the financial statements.

Auditors

Ernst & Young retire and a resolution for their reappointment as auditors of the Company will be proposed at the forthcoming annual general meeting.

ON BEHALF OF THE BOARD

YUEN Tin Fan, Francis

Executive Chairman

Hong Kong

28 February 2007