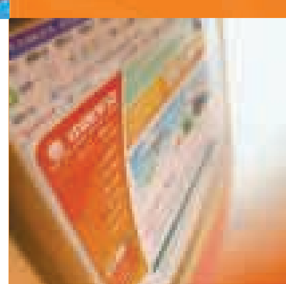
VALUE

Management Discussion and Analysis



GROUP'S CONSOLIDATED PERFORMANCE

The following is a summary of the consolidated results of the Group:

For the year ended December 31, (in RMB million)	2006	2005
Total income	**87,943**	64,995
Total expenses	**(79,395)**	(60,183)
Operating profit before tax	**8,548**	4,812
Net profit	**8,000**	4,265

The following table sets forth the breakdown of our net profit by business segment:

For the year ended December 31, (in RMB million)	2006	2005
Life insurance	**5,704**	3,544
Property and casualty insurance	**1,048**	422
Banking	**71**	7
Other businesses	**1,177**	292
Net profit	**8,000**	4,265

Consolidated net profit increased 87.6% to RMB8,000 million in 2006 from RMB4,265 million in 2005. This increase was primarily due to the better performance across our portfolio of businesses and the strong total investment returns.

Our core life insurance business and property and casualty insurance business, accounted for approximately 71.3% and 13.1%, respectively, of our net profit.

Consolidated Investment Income

For the year ended December 31, (in RMB million, except percentages)	2006	2005
Net investment income	**12,198**	9,338
Net realized and unrealized gains	**9,673**	317
Total investment income	**21,871**	9,655
Net investment yield(1)	**4.6%**	4.2%
Total investment yield(1)	**8.3%**	4.3%

(1) Lease income from investment properties and foreign currency gains/losses on investment assets denominated in foreign currencies are excluded in the calculation of the above yields.

Our net investment income increased 30.6% to RMB12,198 million in 2006 from RMB9,338 million in 2005. This increase was primarily due to the increase in our investment assets to RMB313,907 million as at December 31, 2006 from RMB246,142 million as at December 31, 2005. Net investment yield increased to 4.6% in 2006 from 4.2% in 2005. This increase was primarily due to the higher dividend income received from our equity investment funds.

Our total investment income increased significantly to RMB21,871 million in 2006 from RMB9,655 million in 2005. Total investment yield increased to 8.3% in 2006 from 4.3% in 2005. These increases were primarily due to the strong performance in the PRC equity markets. As a result, the net realized and unrealized gains increased significantly to RMB9,673 million in 2006 from RMB317 million in 2005.

We continued to improve the asset allocation of our portfolio in response to the changes in the capital markets. As a result, our term deposits as a percentage of our total investment assets decreased to 18.8% as at December 31, 2006 from 28.0% as at December 31, 2005, and our equity investments increased to 14.3% as at December 31, 2006 from 6.2% as at December 31, 2005.

The following table presents our investment portfolio allocations among the major categories of our investments:

As at December 31, (in RMB million, except percentages)	**2006 Carrying Value**	**2006 % of Total**	2005 Carrying Value	2005 % of Total
Fixed maturity investments				
Term deposits[3]	**59,107**	**18.8%**	69,015	28.0%
Bond investments[1][3]	**206,881**	**65.9%**	159,776	64.9%
Other fixed maturity investments	**1,600**	**0.5%**	864	0.4%
Equity investments[2][3]	**44,791**	**14.3%**	15,244	6.2%
Investment properties	**1,528**	**0.5%**	1,243	0.5%
Total investments	**313,907**	**100.0%**	246,142	100.0%

(1) Bond investments include the carrying value of derivatives embedded with the host contracts.
(2) Equity investments include equity investment funds, equity securities and investment in an associate.
(3) The above figures exclude items that are classified as cash and cash equivalents.
(4) Certain comparative figures have been reclassified to conform to current year's presentation.

Foreign Currency Losses

In 2006, the PRC currency, Renminbi, continued to appreciate against other major currencies. As a result, we experienced a net exchange loss of RMB466 million in 2006 as compared to a loss of RMB405 million in 2005.

LIFE INSURANCE BUSINESS

Results of Operations

The following is a summary of the results of our life insurance business:

For the year ended December 31, (in RMB million)	**2006**	2005
Gross written premiums, policy fees and premium deposits	**68,780**	58,691
Less: Premium deposits	**(15,158)**	(11,746)
Gross written premiums and policy fees	**53,622**	46,945
Net earned premiums	**52,701**	45,804
Investment income	**19,298**	8,545
Other income	**875**	637
Total income	**72,874**	54,986
Change in deferred policy acquisition costs	**4,808**	3,645
Claims and policyholders' benefits	**(58,890)**	(45,116)
Changes in fair value of derivative financial liabilities	**104**	(6)
Commission expenses of insurance operations	**(6,559)**	(5,168)
Foreign currency losses	**(413)**	(379)
General, administrative and other expenses	**(6,039)**	(4,294)
Total expenses	**(66,989)**	(51,318)
Income taxes	**(181)**	(124)
Net profit	**5,704**	3,544

Gross Written Premiums, Policy Fees and Premium Deposits

For the year ended December 31, 2006 (in RMB million)	Premiums and policy fees	Premium deposits	Total
Individual life			
New business			
First year regular premiums	7,918	2,205	10,123
First year single premiums	34	–	34
Short term accident and health premiums	2,920	–	2,920
Total new business	10,872	2,205	13,077
Renewal business	34,998	7,091	42,089
Total individual life	45,870	9,296	55,166
Bancassurance			
New business			
First year regular premiums	66	–	66
First year single premiums	612	5,284	5,896
Short term accident and health premiums	2	–	2
Total new business	680	5,284	5,964
Renewal business	248	–	248
Total bancassurance	928	5,284	6,212
Group insurance			
New business			
First year regular premiums	1	–	1
First year single premiums	4,225	578	4,803
Short term accident and health premiums	2,122	–	2,122
Total new business	6,348	578	6,926
Renewal business	476	–	476
Total group insurance	6,824	578	7,402
Total life insurance	53,622	15,158	68,780

For the year ended December 31, 2005 (in RMB million)	Premiums and policy fees	Premium deposits	Total
Individual life			
New business			
First year regular premiums	5,497	3,447	8,944
First year single premiums	41	–	41
Short term accident and health premiums	2,587	–	2,587
Total new business	8,125	3,447	11,572
Renewal business	30,633	3,964	34,597
Total individual life	38,758	7,411	46,169
Bancassurance			
New business			
First year regular premiums	35	–	35
First year single premiums	870	4,091	4,961
Short term accident and health premiums	2	–	2
Total new business	907	4,091	4,998
Renewal business	226	–	226
Total bancassurance	1,133	4,091	5,224
Group insurance			
New business			
First year regular premiums	1	–	1
First year single premiums	4,739	244	4,983
Short term accident and health premiums	1,990	–	1,990
Total new business	6,730	244	6,974
Renewal business	324	–	324
Total group insurance	7,054	244	7,298
Total life insurance	46,945	11,746	58,691

Individual Life Business. Gross written premiums, policy fees and premium deposits for our individual life business increased 19.5% to RMB55,166 million in 2006 from RMB46,169 million in 2005. This increase was primarily due to the 21.7% increase in renewal premiums, policy fees and premium deposits to RMB42,089 million in 2006 from RMB34,597 million in 2005. In addition, first year premiums, policy fees and premium deposits for our individual life business increased 13.0% to RMB13,077 million in 2006 from RMB11,572 million in 2005. These increases were primarily due to the continued improvement in the quality and productivity of our agency force.

Bancassurance Business. Gross written premiums, policy fees and premium deposits for our bancassurance business increased 18.9% to RMB6,212 million in 2006 from RMB5,224 million in 2005. This increase was primarily due to the growth in sales of our universal life products through our bancassurance channel.

Group Insurance Business. Gross written premiums, policy fees and premium deposits for our group insurance business increased 1.4% to RMB7,402 million in 2006 from RMB7,298 million in 2005. This increase was primarily due to our continued efforts to manage the growth of this business line to improve profit margin. We continued to focus on selling employee welfare benefit plans. As a result, gross written premiums and policy fees for our short-term accident and health insurance business increased 6.6% to RMB2,122 million in 2006 from RMB1,990 million in 2005.

Investment Income

Net investment income for our life insurance business increased 34.3% to RMB11,149 million in 2006 from RMB8,299 million in 2005. This increase was primarily due to the increase in investment assets to RMB271,116 million as at December 31, 2006 from RMB222,261 million as at December 31, 2005. Net investment yield for our life insurance business increased to 4.8% in 2006 from 4.2% in 2005.

Total investment income for our life insurance business increased significantly to RMB19,298 million in 2006 from RMB8,545 million in 2005. Total investment yield for our life insurance business increased to 8.3% in 2006 from 4.3% in 2005.

For the year ended December 31, (in RMB million, except percentages)	2006	2005
Net investment income	**11,149**	8,299
Net investment yield(1)	**4.8%**	4.2%
Total investment income	**19,298**	8,545
Total investment yield(1)	**8.3%**	4.3%

(1) Lease income from investment properties and foreign currency gains/losses on investment assets denominated in foreign currencies are excluded in the calculation of the above yields.

Change in Deferred Policy Acquisition Costs

The change in deferred policy acquisition costs was RMB4,808 million in 2006 as compared to RMB3,645 million in 2005. The bigger change in deferred policy acquisition costs was primarily due to the increase in first year premiums, policy fees and premium deposits from individual life business.

Claims and Policyholders' Benefits

Claims and policyholders' benefits increased 30.5% to RMB58,890 million in 2006 from RMB45,116 million in 2005. The following table summarizes total expenses pursuant to claims, surrenders, annuities, maturities and survival benefits, policyholders' dividends and provisions, interest credited to policyholder contract deposits, and increase in policyholders' reserves.

For the year ended December 31, (in RMB million)	2006	2005
Claims	**3,078**	2,571
Surrenders	**6,293**	5,618
Annuities	**2,922**	2,765
Maturities and survival benefits	**3,167**	3,369
Policyholders' dividends and provisions	**1,487**	1,064
Interest credited to policyholder contract deposits	**523**	172
Increase in policyholders' reserves	**41,420**	29,557
Total claims and policyholders' benefits	**58,890**	45,116

Payments for claims increased 19.7% to RMB3,078 million in 2006 from RMB2,571 million in 2005. This increase was primarily due to the higher claims expense incurred for our short term accident and health products.

Payments for surrenders increased 12.0% to RMB6,293 million in 2006 from RMB5,618 million in 2005. This increase was primarily due to the increase of payments for surrenders of our participating products.

Payments for policyholder dividends and provisions increased 39.8% to RMB1,487 million in 2006 from RMB1,064 million in 2005. This increase was primarily due to the increase in sales of participating life policies and the higher dividend distribution as a result of better performance in investments for our participating products.

Payments for interest credited to policyholder contract deposits increased significantly to RMB523 million in 2006 from RMB172 million in 2005. This increase was primarily due to the increase in sales of universal life policies and better investment performance.

The increase in policyholders' reserves was RMB41,420 million in 2006 as compared to RMB29,557 million in 2005. The bigger increase in policyholders' reserves was primarily due to the increase in gross written premiums and policy fees.

Commission Expenses of Insurance Operations

For the year ended December 31,	2006	2005
Commission expenses as a percentage of gross written premiums, policy fees and premium deposits	**9.5%**	8.8%

Commission expenses of insurance operations, which we paid primarily to our sales agents, increased 26.9% to RMB6,559 million in 2006 from RMB5,168 million in 2005. Commission expenses as a percentage of gross written premiums, policy fees, and premium deposits increased to 9.5% in 2006 from 8.8% in 2005. These increases were primarily due to the increase in first year premiums, policy fees and premium deposits from individual life products.

General, Administrative and Other Expenses

For the year ended December 31,	2006	2005
General, administrative and other expenses as a percentage of gross written premiums, policy fees and premium deposits	**8.8%**	7.3%

General, administrative and other expenses increased 40.6% to RMB6,039 million in 2006 from RMB4,294 million in 2005. General, administrative and other expenses as a percentage of gross written premiums, policy fees and premium deposits increased to 8.8% in 2006 from 7.3% in 2005. These increases were primarily due to the increase in sales of first year premiums, policy fees and premium deposits.

Income Taxes

For the year ended December 31,	2006	2005
Effective tax rate	**3.1%**	3.4%

Income taxes increased 46.0% to RMB181 million in 2006 from RMB124 million in 2005. This increase was primarily due to the increase of deferred income tax liabilities. The effective tax rate decreased to 3.1% in 2006 from 3.4% in 2005. This decrease was primarily due to the tax credit for salary expenses deduction approved by the tax authorities and the increase in interest income from government bonds and dividend income from equity investment funds, which were entitled to certain tax exemptions.

Net Profit

As a result of the foregoing, the net profit for our life insurance business increased 60.9% to RMB5,704 million in 2006 from RMB3,544 million in 2005.

PROPERTY AND CASUALTY INSURANCE BUSINESS

Results of Operations

The following is a summary of the results of our property and casualty insurance business:

For the year ended December 31, (in RMB million)	2006	2005
Gross written premiums	**16,074**	12,076
Net earned premiums	**10,312**	7,395
Investment income	**684**	398
Other income	**1,317**	1,195
Total income	**12,313**	8,988
Change in deferred policy acquisition costs	**672**	185
Claims expenses	**(7,178)**	(5,259)
Commission expenses of insurance operations	**(1,572)**	(820)
Foreign currency losses	**(16)**	(7)
General, administrative and other expenses	**(3,029)**	(2,294)
Total expenses	**(11,123)**	(8,195)
Income taxes	**(142)**	(371)
Net profit	**1,048**	422

Combined Ratio

For the year ended December 31,	2006	2005
Expense ratio	**25.8%**	23.3%
Loss ratio	**69.6%**	72.0%
Combined ratio	**95.4%**	95.3%

Gross Written Premiums

For the year ended December 31, (in RMB million)	2006	2005
Automobile insurance	**11,057**	7,497
Non-automobile insurance	**4,207**	4,044
Accident and health insurance	**810**	535
Total gross written premiums	**16,074**	12,076

Gross written premiums increased 33.1% to RMB16,074 million in 2006 from RMB12,076 million in 2005. This increase in gross written premiums was primarily due to the significant growth in all three principal lines of our property and casualty insurance business.

Automobile Insurance Business. Gross written premiums attributable to our automobile insurance business increased 47.5% to RMB11,057 million in 2006 from RMB7,497 million in 2005. This increase was primarily due to the continued increase in demand for automobiles in the PRC and implementation of compulsory third party liability insurance.

Non-automobile Insurance Business. Gross written premiums attributable to our non-automobile insurance business increased 4.0% to RMB4,207 million in 2006 from RMB4,044 million in 2005. This increase was primarily due to the increase in sales of liability insurance and commercial property insurance. Gross written premiums attributable to our liability insurance increased 34.9% to RMB735 million in 2006 from RMB545 million in 2005. Gross written premiums attributable to our commercial property insurance increased 10.8% to RMB1,863 million in 2006 from RMB1,682 million in 2005.

Accident and Health Insurance Business. Gross written premiums attributable to our accident and health insurance business increased 51.4% to RMB810 million in 2006 from RMB535 million in 2005. This increase was primarily due to our continued focus on growing this line of business in 2006.

Investment Income

Net investment income for our property and casualty insurance business increased 20.8% to RMB471 million in 2006 from RMB390 million in 2005. This increase was primarily due to the increase in investment assets to RMB12,964 million as at December 31, 2006 from RMB10,003 million as at December 31, 2005. Net investment yield for our property and casualty insurance business increased to 4.5% in 2006 from 4.3% in 2005.

Total investment income for our property and casualty insurance business increased 71.9% to RMB684 million in 2006 from RMB398 million in 2005. Our total investment yield for our property and casualty insurance business increased to 6.3% in 2006 from 4.3% in 2005.

For the year ended December 31, (in RMB million, except percentages)	**2006**	2005
Net investment income	**471**	390
Net investment yield(1)	**4.5%**	4.3%
Total investment income	**684**	398
Total investment yield(1)	**6.3%**	4.3%

(1) Lease income from investment properties and foreign currency gains/losses on investment assets denominated in foreign currencies are excluded in the calculation of the above yields.

Change in Deferred Policy Acquisition Costs

The change in deferred policy acquisition costs was RMB672 million in 2006 as compared to RMB185 million in 2005. The bigger change in deferred policy acquisition costs was primarily due to the increase in gross written premiums and increase in the percentage of acquisition cost that can be deferred in 2006 as compared to 2005.

Claims Expenses

For the year ended December 31, (in RMB million)	**2006**	2005
Automobile insurance	**5,746**	3,972
Non-automobile insurance	**1,054**	1,057
Accident and health insurance	**378**	230
Total claims	**7,178**	5,259

Total claims increased 36.5% to RMB7,178 million in 2006 from RMB5,259 million in 2005.

Claims attributable to our automobile insurance business increased 44.7% to RMB5,746 million in 2006 from RMB3,972 million in 2005. This increase was primarily due to the increase in gross written premiums.

Claims attributable to our non-automobile insurance business decreased 0.3% to RMB1,054 million in 2006 from RMB1,057 million in 2005. This decrease was primarily due to the lower claims from our motor loan guarantees insurance business.

Claims attributable to our accident and health insurance business increased 64.3% to RMB378 million in 2006 from RMB230 million in 2005. This increase was primarily due to the increase in gross written premiums.

Commission Expenses of Insurance Operations

For the year ended December 31,	2006	2005
Commission expenses as a percentage of gross written premiums	**9.8%**	6.8%

Commission expenses of insurance operations increased 91.7% to RMB1,572 million in 2006 from RMB820 million in 2005. As a percentage of gross written premiums, commission expenses increased to 9.8% in 2006 from 6.8% in 2005. These increases were primarily due to the increase in gross written premiums and the higher market commission rates resulting from increased competition in the property and casualty insurance industry.

General, Administrative and Other Expenses

For the year ended December 31,	2006	2005
General, administrative and other expenses as a percentage of gross written premiums	**18.8%**	19.0%

General, administrative and other expenses increased 32.0% to RMB3,029 million in 2006 from RMB2,294 million in 2005. This increase was primarily due to the increase in gross written premiums. General, administrative and other expenses as a percentage of gross written premiums decreased slightly to 18.8% in 2006 from 19.0% in 2005.

Income Taxes

For the year ended December 31,	2006	2005
Effective tax rate	**11.9%**	46.8%

Income taxes decreased 61.7% to RMB142 million in 2006 from RMB371 million in 2005. The effective tax rate decreased to 11.9% in 2006 from 46.8% in 2005. These decreases were primarily due to the tax credit for salary expense deduction approved by the tax authorities and the increase in interest income from government bonds and dividend income from equity investment funds, which were both entitled to certain tax exemptions.

Net Profit

As a result of the foregoing, the net profit from our property and casualty insurance business increased significantly to RMB1,048 million in 2006 from RMB422 million in 2005.

BANKING BUSINESS

The following is certain key financial information of our banking business:

For the year ended December 31, (in RMB million)	2006	2005
Net interest income(1)	**112**	18
Net fees and commission income(1)	**7**	–
Loan loss provisions, net of reversals(1)	**(2)**	–
Net profit(1)	**71**	7

(1) On December 15, 2006, the Group completed its acquisition of 89.36% equity interest in SZCB. SZCB was accounted for as a consolidated subsidiary from the date of acquisition.

The following table sets forth the major components of net interest income:

For the year ended December 31, (in RMB million)	2006	2005
Interest income		
Loans and advances to customers	**132**	6
Balances with central bank	**5**	–
Cash and amounts due from banks and other financial institutions	**55**	19
Total interest income	**192**	25
Interest expenses		
Customers deposits	**(47)**	(1)
Due to banks and other financial institutions	**(33)**	(6)
Total interest expenses	**(80)**	(7)
Net interest income	**112**	18

Net interest income increased significantly to RMB112 million in 2006 from RMB18 million in 2005. Net fees and commission income increased to RMB7 million in 2006. Net profits increased significantly to RMB71 million in 2006 from RMB7 million in 2005. These increases were primarily due to the consolidation of SZCB from the date of acquisition and increase of interest income from Ping An Bank as it began to provide Renminbi services to corporate customers in 2006.

TRUST BUSINESS

For the year ended December 31, (in RMB million)	2006	2005
Total income(1)	**422**	179
Net profit(1)	**194**	57

(1) Total income and net profit are presented at company's level, where interests in subsidiaries are accounted for at cost.

Total income from our trust business increased significantly to RMB422 million in 2006 from RMB179 million in 2005. Net profit from our trust business increased significantly to RMB194 million in 2006 from RMB57 million in 2005. These increases were primarily due to the increase in assets held under its management.

SECURITIES BUSINESS

For the year ended December 31, (in RMB million)	2006	2005
Total income	**1,296**	235
Net profit	**609**	6

Total income from our securities business increased significantly to RMB1,296 million in 2006 from RMB235 million in 2005. Net profit from our securities business increased significantly to RMB609 million in 2006 from RMB6 million in 2005. These increases were primarily due to the increase in income from securities trading business, investment banking services and investment consultancy services as a result of better performance in the PRC equity markets.

OTHER BUSINESS

Our annuity business, health insurance business and asset management business were launched in 2005 but the scale of operation is still relatively small. The total income and net profit of these companies were considerably immaterial as compared to the entire group.

LIQUIDITY AND FINANCIAL RESOURCES

Liquidity and financial resources are managed at the Group level on a consolidated basis. We are a holding company and, with the exception of investment management activities, do not conduct any significant business operations on our own. As a result, we depend upon dividends and distributions from our operating subsidiaries for substantially all of our operating cash flows.

In addition to cash and cash equivalents held by the Group, we have two additional sources of liquidity. They are liquid investments held for trading and short-term borrowings.

Liquid investments held for trading are listed or are traded in an active market and can be converted to cash easily without incurring significant charges.

The following table summarizes the carrying amount of liquid assets held by the Group:

As at December 31, (in RMB million)	**2006**	2005
Cash and cash equivalents	**45,964**	17,648
Held-for-trading investments	**23,632**	9,410
Total liquid assets	**69,596**	27,058

The Group utilizes short-term borrowings and assets sold under agreements to repurchase as part of the liquidity management for our daily operations. The following table summarizes the carrying amount of these arrangements:

As at December 31, (in RMB million)	**2006**	2005
Short-term borrowings	**1,518**	–
Assets sold under agreements to repurchase	**13,436**	7,095

The management believes that the liquid assets currently held, together with net cash generated from future operations, and the availability of short-term borrowings will enable the Group to meet its foreseeable cash requirements.

CAPITAL STRUCTURE

Total equity increased to RMB47,750 million as at December 31, 2006 from RMB33,522 million as at December 31, 2005. This increase was primarily due to our operating profit in 2006.

The Group had no material charges on its group assets.

Gearing Ratio

As at December 31,	**2006**	2005
Gearing ratio	**90.6%**	89.7%

The gearing ratio is computed by dividing the sum of total liabilities and minority interests by total assets.

Solvency Margin

The solvency margin ratio is a measure of capital adequacy for insurance companies. It is calculated by dividing the actual solvency margin by the statutory minimum solvency margin requirement. Under the applicable CIRC regulations, PRC insurance companies are required to maintain specified solvency margin ratios. As a general matter, the CIRC considers an insurance company with a solvency margin ratio of 100% or higher to be financially sound.

The following table sets forth the solvency margin ratios for Ping An Life and Ping An Property & Casualty:

As at December 31, (in RMB million, except percentages)	**Ping An Life**		**Ping An Property & Casualty**	
	2006	2005	**2006**	2005
Actual solvency margin	**18,000**	15,177	**3,437**	2,113
Minimum solvency margin	**13,096**	10,787	**1,990**	1,377
Solvency margin ratio	**137.5%**	140.7%	**172.7%**	153.4%

Contractual Obligation and Other Commercial Commitments

The following table sets forth our aggregate contractual obligations and other commercial commitments for the periods specified:

As at December 31, (in RMB million)	**2006**	2005
Contractual commitments	**3,431**	472
Operating lease commitments	**1,167**	850

RISK MANAGEMENT

Approach to Risk Management

Ping An regards risk management as a core discipline in our business practice. We are dedicated to developing and maintaining a risk management framework that governs the overall infrastructure of the group's operations.

Members of the Risk Management Committee include the Vice Chief Executive Officer, the Chief Financial Officer, the Chief Actuarial Officer, the Chief Internal Auditor, the Chief Legal Officer and the Chief Information Officer.

The committee meets on a quarterly basis to review the risk management progression. In these meetings, the risk management structure and major risk management issues are discussed. Potential new corporate strategic objectives are evaluated for their risk exposures; major risk events for the past quarter are evaluated and development of new risk measurement techniques and risk control measures are presented and approved for implementation. Potential operational risk exposures observed from our internal audit reviews and external factors such as regulatory changes and accounting standards changes are also reviewed. Appropriate responses are formulated for the risk issues discussed. Lastly, the committee will review the appropriateness of measures implemented to address risk issues raised in prior meetings.

SZCB has been consolidated into Ping An Group recently. We will quantify and disclose risk measures related to this newly acquired bank business in the Risk Management section of the annual report in the future. Until now many actions have been taken to manage the bank risk factors such as credit risk, market risk and operational risk. These actions include:

- Recruiting the Chief Risk Officer and other risk management professionals to build the bank risk management team;
- Setting up the Asset & Liability Committee to manage the balance sheet and optimize the return on equity; and
- Setting up the Risk Policy Committee to determine risk policies and procedures related to the banking business.

Insurance Product Risk

Insurance product risk is the risk of loss due to actual experience such as investment returns, expenses, taxes, mortality and morbidity claims, and policyholder behavior, emerging differently than what was assumed when the product was designed and priced.

The Group has an objective to manage insurance risk and reduce volatility of operating profits. The Group manages insurance risk through the following mechanisms:

- Management information systems are used to provide up to date, accurate and reliable data on risk exposure at any point in time.
- Actuarial models and statistical techniques are applied to aid in pricing decisions and monitor claims pattern.
- Guidelines are issued for underwriting insurance contracts and assuming insurance risks.
- Proactive claims handling procedures are followed to investigate and adjust claims, thereby preventing settlement of dubious or fraudulent claims.
- Reinsurance is used to limit the Group's exposure to large claims and catastrophes by placing risk with reinsurers providing high security.
- Diversification is accomplished by achieving sufficiently large population of risks to reduce the variability of the expected outcome. The diversification strategy seeks to ensure that underwritten risks are well diversified in terms of type and amount of risk, industry and geography.
- The mix of insurance assets is developed to match the nature and term of insurance liabilities. The management of assets and liabilities is closely monitored to attempt to match the expected pattern of claim payments with the maturity dates of assets.

Asset and Liability Mismatching Risk

Asset and liability mismatching risk is the risk of loss due to the Group's inability to match its assets with its liabilities on the basis of both duration and investment return.

The Group's asset and liability management includes processes and models built to measure the sensitivity of net income and shareholders' equity under various deterministic interest rate scenarios. The scenarios and assumptions used are reviewed and updated periodically. Insights gained through the analysis are used to measure the risk exposures and capital position of the Group.

Under the current regulatory and market environment, the Group is unable to invest in assets with a duration of sufficient length to match the duration of its life insurance liabilities. When the regulatory and market environment permits, the Group intends to gradually lengthen the duration of its assets.

Market Risk

Market risk is the risk of potential loss that may result from changes in the value of a financial instrument as a result of changes in interest rates, market prices, foreign currency exchange rates and other market price-related factors. Under the current PRC regulatory and market environment, there is a lack of financial instruments available for the Group to hedge its market risk exposures efficiently. The Group controls its market risk exposures by setting a maximum risk exposure for each class of assets. When setting these limits, significant consideration is placed on the Group's risk appetite and impact on the Group's financial condition. These limits also take into account the Group's asset-liability management strategy.

The Group utilizes various techniques to quantify the market risk exposure, including sensitivity analysis and Value-at-Risk ("VaR") computation. VaR is a summary statistical measure that uses historical market prices and estimates the maximum loss over a target horizon such that there is a low, pre-specified probability that the actual loss will be larger. However, the utilization of the VaR technique under the current PRC market environment has its limitations due to the lack of reliable historical financial data.

Market Risk – Interest Rate Risk

Fixed maturity securities held by the Group are exposed to interest rate risks. These investments are substantially represented by bond investments that are recorded at fair value in the balance sheet.

The Group uses sensitivity analysis to estimate its risk exposure. Interest rate sensitivity is estimated by assuming a 50 basis points parallel shift in the government bond yield curve.

As at December 31, 2006 (in RMB million)	Interest rate risk
Bond investments held-for-trading and available-for-sale	3,060

Market Risk – Market Price Risk

Listed equity investments held by the Group are exposed to market price risks. These investments are substantially represented by equity securities and equity investment funds.

The Group uses the 10-day market price VaR technique to estimate its risk exposure. Market price VaR is computed as (equity securities/equity investment funds valued at market price x 10-day worst market fluctuation at 99% level).

As at December 31, 2006 (in RMB million)	Market price risk
Equity securities and equity investment funds held-for-trading and available-for-sale	4,241

Market Risk – Foreign Currency Risk

Foreign currency denominated investments and cash assets held by the Group are exposed to foreign currency risks. These assets include term deposits, cash and cash equivalents held in foreign currency that are considered as monetary assets. In addition to foreign currency denominated monetary assets, the Group's foreign currency denominated monetary liabilities are also exposed to fluctuations in exchange rates. These liabilities include foreign currency denominated claim reserves and payable to reinsurers. The exposures to fluctuations in exchange rates from monetary assets and monetary liabilities offset each other.

The Group uses sensitivity analysis to estimate its risk exposure. Foreign currency risk sensitivity is estimated by assuming a simultaneous and uniform 5% depreciation, against the Renminbi, of all foreign currency denominated monetary assets and monetary liabilities.

As at December 31, 2006 (in RMB million)	Foreign currency risk
Net exposure to fluctuations in exchange rates assuming a simultaneous and uniform 5% depreciation of all foreign currency denominated monetary assets and monetary liabilities against the Renminbi	678

Credit Risk

Credit risk is the risk of economic loss resulting from the failure of one of the Group's obligors to make any payment of principal or interest when due.

The Group is exposed to credit risks primarily associated with its term deposits arrangements with commercial banks and loans to third parties from its banking operations.

To evaluate credit risk properly, the Group has established an internal credit rating system. The counterparties' ratings are reviewed at least annually through the system or whenever a credit event occurs.

The Group quantifies its credit risk exposure by assigning expected default rates and expected recovery rates of relevant credit grades for commercial banks and bond issuing companies. Credit risk is computed as (principal amount + outstanding interests) x default rate x (1 – recovery rate).

As at December 31, 2006 (in RMB million)	Credit risk
Term deposits placed with commercial banks and loans to external third parties	137

Operational Risk

Operational risk is the risk of loss resulting from internal operation failures or uncontrollable external events. Internal operation failures occur due to inadequate or failed internal processes (process risks), system failure (system risks), and human performance failure (people risks). Uncontrollable external events that contribute to operational risks are mainly due to legal matters or changes in the regulatory requirements, accounting standards and tax laws.

For internal operational risks, a proactive approach has been taken to implement appropriate and sufficient preventive controls, detective controls and damage limitation controls. These controls are embedded into the business processes, system operations and human performance. Rigorous checks on the reliability of the controls are performed by our internal and external audit functions. Our risk management committee and audit committee reviews the reports from our internal and external auditors to ensure that appropriate measures are taken to address control weaknesses detected. For the uncontrollable external events, our Legal Department, Finance Department and Planning and Actuarial Department monitor changes in regulatory requirements, accounting standards and tax laws closely.