

Chairman's statement

We achieved solid business growth in 2005 and our underlying performance continues to be robust. Annualised first year premium for new business on life insurance increased 24.5% to HK\$323.7 million. Single and first year premium increased 24.4% to HK\$296.0 million, renewal premium increased 5.5% to HK\$1,500.1 million and total premium increased 8.2% to HK\$1,796.1 million.



Consolidated net profit for the year was HK\$42.5 million (2004: HK\$188.3 million). Basic earnings per share was HK\$0.05 compared to HK\$0.23 in the previous year. The decrease in earnings was primarily due to the reclassification of the investment portfolio from "trading" to "available-for-sale" following adoption of HKAS 39 with effect from 1 January 2005. As at 31 December 2005, the available-for-sale financial assets revaluation reserve balance was HK\$187.5 million (2004: nil). If there had been no reclassification of the investment portfolio in 2005, this reserve would have been reported as unrealised gains in the income statement. The Directors recommend the payment of a final dividend of HK\$0.04 per share (2004: final dividend of HK\$0.06 per share and special dividend of HK\$0.04 per share) in addition to the interim dividend of HK\$0.01 per share (2004: nil) for the year under review.

In 2005, we grew our agency force by over a third to 1,696 compared to 1,268 a year ago. Despite the expansion of our operations, total operating expenses maintained at HK\$1,259.6 million, or 1.2% below that of 2004. 13th month persistency rate improved from 86.6% to 88.8%, renewal ratio improved from 98.9% to 100.3% and claims ratio reduced from 99.2% to 95.5%. Expense ratio increased from 106.3% to 108.4%.

The embedded value of the Group as at 31 December 2005 was HK\$4.947 per share, representing an increase of 14.3% from HK\$4.327 per share as at the end of 2004. The methodology and actuarial assumptions used in the calculation of embedded value and value of new business as at 31 December 2005 have been reviewed and considered as reasonable by Watson Wyatt, an internationally renowned actuarial consulting firm. The increase in value was mainly attributable to the natural growth in value as well as continued improvement on lapse experience and the strong growth in new business.

PricewaterhouseCoopers Review

The Board engaged PricewaterhouseCoopers to conduct an independent review of the Group's internal control over investment accounting and quarterly reporting, following the Company's announcement on 24 January 2006 of the misstatements in the Company's quarterly and interim results, which were reported earlier in the year. Although the misstatements did not have any material impact on the fundamental financial position of the Group as confirmed by the Group's external auditor, Ernst and Young, the Board and senior management have taken the matter extremely seriously.

The objective of the assignment was to assist the Board in establishing the cause of the misstatements, and to identify areas for improvement in internal controls of the Company's financial reporting. The review was completed and presented to the Board on 23 February 2006.

The Board has considered and accepted the findings by PricewaterhouseCoopers, and has initiated the implementation of the key recommendations with immediate effect.

Corporate Governance

Sound corporate governance is crucial to the smooth, effective and transparent operation of a company and its ability to attract investment, protect rights of shareholders and stakeholders, and enhance shareholder value. The Company has always attached great importance to corporate governance so as to ensure its sustainable development.

The Nomination Committee has completed a comprehensive review of the Board composition and made the following recommendations:

- the redesignation of Mr Peter Allen, Mr Alex Arena, Mr Mico Chung, Mr Feng Xiaozeng, and Mr Zheng Changyong as non-executive directors;
- the redesignation of Mr Wang Xianzhang as an independent non-executive director;
- the appointment of Mr Peter Allen as a member of the Audit Committee;
- the appointment of Mr Wang Xianzhang as a member each of the Nomination Committee and Remuneration Committee.

The Board considered that the proposed changes would give the right balance between executive and non-executive directors and that each of the Audit Committee, Nomination Committee and Remuneration Committee would be strengthened by new members with relevant experience.

The Board accepted and implemented the proposed changes with immediate effect.

2006 Prospects

The solid foundation laid in 2005 paves the way for strong growth in 2006.

As a life insurance company, we strive to manage our balance sheet prudently with a view to creating shareholder value in the form of embedded value. In 2005, embedded value increased 14.3% to HK\$4.947 per share, which equates to a pick up of approximately HK\$500 million in shareholder value. Barring any unforeseen circumstances, we look forward to another year of significant growth in embedded value in 2006.

Following the adoption of HKAS 39, we kick started the new year with investment reserves of HK\$187.5 million (2004: nil). Shareholders are reminded that Pacific Century Insurance, as a relatively young life insurance company, is inevitably subject to short term fluctuations in income from investment return. The classification of certain investments as "available-for-sale" and the creation of the investment reserves will serve to reduce the impact of a volatile investment environment on the earnings of the Company.

As of 28 February, as we had not received approval from China Insurance Regulatory Commission to appoint our nominated representatives to the board of Sino Life Insurance, we terminated our proposed investment in a HK\$508.3 million Exchangeable Note, which if exercised, would have given Pacific Century Insurance a 22.09% interest in the company. We remain committed to gain access to the rapidly growing China insurance market, and will continue to pursue suitable investment opportunities.

I would like to thank my fellow directors for their leadership and wise counsel, our management and staff for their professionalism and dedication and our agents for their enthusiasm and hard work. They are sources of great encouragement to me, and with them I look to 2006 with great confidence.

Yuen Tin Fan, Francis

Chairman

Hong Kong
20 March 2006