CIC
China Investment Corporation

# Newsletter May 2006

- China shares outperform as Asian markets correct
- AAC Acoustic's turnover more than doubles
- China Fire Safety's earnings growth accelerates
- Pico Far East places new shares
- Shui On Construction to list China property arm

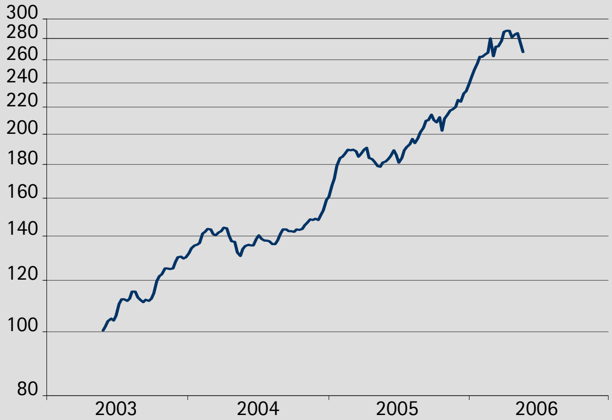
Figures as of May 31, 2006

## Net Asset Value

Per Share: USD 269.52

Market Capitalization: USD 26.7 million

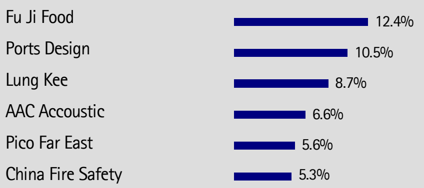
## Share Price in USD since May 27, 03



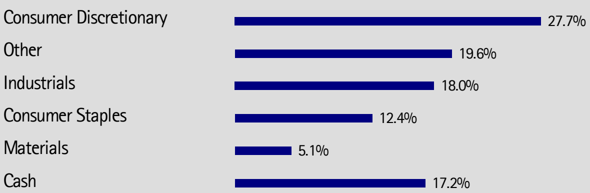

## Performance

| May | YTD | 1 Y | May 27, 03 |
|---|---|---|---|
| (4.3%) | 15.7 % | 48.0% | 169.5% |

## Largest Holdings




## Exposure




China shares corrected in May, driven by concerns over inflation, tightening liquidity conditions and a deteriorating earnings outlook. However, with a 5 percent decline, the MSCI China benchmark outperformed the regional benchmark. This was probably due to the perceived domestic focus of China, which makes it less reliant on global monetary conditions and demand. During the month, we raised the cash component of the portfolio. This was due to our decision to reduce exposure in Lung Kee, where management is guiding for continuing margin pressure and the decision to sell Wei Fu, also on earnings concerns. We think that the ongoing correction creates opportunities and intend to gradually increase exposure in quality stocks we think have overly corrected.

For the first quarter 2006, AAC Acoustic's turnover was up 122 percent year-on-year to CNY 375 million. The gross margin was up 5.6 percentage points to 49.8 percent due to a better product mix including a higher portion of high-end receivers and linear speakers, which are needed for ultra-slim handsets. Net profit increased 183 percent to CNY 121 million. We remain positive on the company as it continues to do well on product development and gains market share.

For the first quarter 2006, China Fire Safety's turnover was CNY 240 million, 104 percent higher year-on-year. Installation revenue was up 183 percent to 54 percent of total, whereas sale of goods was up 66 percent to 38 percent of total. The operating margin declined to 22.4 percent from 34.2 percent, mainly due to the expansion of its installation business beyond its core market, which was accompanied by more aggressive pricing and the lower margin equipment sale businesses acquired in 2005. Net profit was CNY 42 million, an increase of 23 percent. The company continues to benefit from the secular growth of the fire safety industry in China.

On May 10, 2006, Pico Far East announced the placement of 42 million new shares, or 3.5 percent of its enlarged share capital, to institutional investors at a 3.6 percent discount to the previous closing price. Of the HKD 85 million placement proceeds, HKD 50 million will be utilized for the company's exhibition hall business, and the remainder will be invested in its show management business. The management's explanation for the surprising fund raising exercise, given the strong cash flow of the company, is that it is seeing stronger than expected demand, raising investment needs.

Shui On Construction and its holding company are in the process of spinning off their China property arm, Shui On Land, which is effectively 21 percent owned by Shui On Construction. The listing is expected to raise USD 1 billion primarily through new shares to fund the land acquisition and operation of Shui On Land in China. We expect that the listing of Shui On Land will finally unlock the investment value in Shui On Construction.

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|---|---|
| Legal Nature | Trust account, CSPB Singapore |
| Security | Phantom shares |
| Bloomberg | CHININC SP <Equity> |
| Valor | 2233619 |

| | |
|---|---|
| Trading | Daily, based on NAV |
| Dilution Levy | 0.7% in favour of CIC |
| Trading Fee | 0.5% |
| Management Fee | 1% |
| Performance Fee | 20% above 8% hurdle rate, high water mark |

| | |
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# General Information

## Investment Rationale

Since Deng Xiao-ping succeeded Mao towards the end of the 1970s, economic development has taken centre stage in China. Market-oriented reforms and decentralized decision making were introduced at the Party Congress in 1978. Over the last decade the shift from communist dogmatism to economic pragmatism has become deeply entrenched. As a consequence, China has become the fastest growing region in the world attracting substantial foreign investments and developing into the world's manufacturing hub. Furthermore, an increasing middle class is fuelling demand for consumer products. The growth momentum is set to continue as China strives to catch up with mature economies, producing attractive investment opportunities. China Investment Corporation ("CIC") is managed with a view to careful selection and trading of its portfolio companies. In order to mitigate the risks invariably associated with young and fast growing economies, CIC emphasizes quality in all its aspects. CIC is designed to provide investors with a conservative and liquid equity exposure to a part of the world that is gradually gaining in importance.

## The Fund

CIC is a trust account in the name of HSZ Limited with the Singapore Branch of Credit Suisse Private Banking and was set up on May 27, 2003. Phantom shares are issued and redeemed daily based on CIC's net asset value. CIC will be converted into a mutual fund under Swiss legislation shortly.

## Investment Strategy

The objective is to create sustained shareholder value by acquiring and managing equity and equity-linked investments in a select number of high-quality companies that have a significant exposure to China, regardless of the listing location. Companies with significant China exposure generate at least 50 percent of their revenues and/or have at least 50 percent of their manufacturing capacity in China. Based on fundamental analysis and a bottom up approach, investment opportunities are identified that are assessed to provide above-average return on invested capital, have strong earnings per share growth and are priced attractively. Investments by CIC in any single company may not exceed 20 percent of CIC's assets upon the date of purchase and 10 percent of a company's capital. No debt financing is employed. Derivatives are used, however with moderation.

## The Manager

HSZ Group is an investment management company with offices in Hong Kong and Zurich. The company is majority owned by its three partners and employs a total staff of thirteen. The team has managed Asian equity portfolios since 1994.