

Newsletter August 2007

- China corporates' strong interim results keep stock market buoyant
- China Merchants Bank reports 120% net profit growth
- Retail sales boost earnings of Beijing Jingkelong
- Shimao results in line with expectations
- Expansion in China increases cost base for Bank of East Asia

August was a month of interim report announcements. Overall, the results were ahead of analysts' expectations which helped keep the Chinese stock market steady in the midst of US jitters over subprime loans. China Merchants Bank (accounting for over 7% of the HSZ China Fund) saw net profit growth of over 100%, leading to analysts' upgrades of the overall banking sector. Economic data is still strong, the Producer Price Index (PPI) was up 2.4% in July mainly due to a rise in food prices of 7.8%. Money supply (M2) rose 18.5% year on year in July. The People's Bank of China raised deposit rates by 27 basis points and lending rates by 18 basis points. During the stock market volatility, the fund had taken the opportunity to invest in stocks which had been oversold such as China Infrastructure and Weichai Power.

China Merchants Bank reported 120% growth in net profit to CNY 6'120 million for the six months ended June 30, 2007. These earnings numbers were ahead of market's expectation. Net interest margin improved by 40 basis points to 2.96% driven by healthy loan growth and widening interest spread. The company also saw continued improvement in asset quality, with a reduction in non-performing loans.

For the six months ended June 30, 2007, Beijing Jingkelong saw a 20% growth in net profit to CNY 57 million on a 19% growth in revenue to CNY 2'572 million. Revenue growth was driven by contribution from the 13 supermarkets set up during the past 12 months, the 13.5% growth in same-store sales and expansion of wholesale business. Gross profit margin improved by one percentage point, thanks to optimization of product mix and rising economies of scale. We believe the company will be able to maintain its margins and benefit from the increase in consumption levels.

Shimao Property reported net profit excluding net fair value gain on investment properties of CNY 1.32 billion in the first half of 2007, up 206% year-on-year. Gross profit margin improved from 36% to 42%, which is above the industry's average margin. Land bank reserve increased to 20.6 million square meters, from 16.6 million as of the end of 2006. Given its strong balance sheet and low gearing of 29%, Shimao is well positioned to leverage on the rise of housing demand in mainland China.

Bank of East Asia reported net profit of HKD 1.88 billion in the first half of 2007, up 20% year-on-year and in line with market estimates. Pre-provision operating profit grew 20% year-on-year. Revenue growth of 26% was outpaced by higher expense growth of 33% which was due to higher start-up cost in China and branch outlet expansion. We believe that the higher cost incurred in its expansion into China will translate to long-term growth for the company.

Figures as of August 31, 2007

Net Asset Value

Per Share: USD 132.57, CHF 127.79, EUR 124.10
Market Capitalization: USD 188.2 million

Share Price in USD since Nov 17, 2006



Performance

	Aug	YTD	1Y	Nov 17, 06
USD-Class	(1.1%)	24.1%	n.a.	32.6%
CHF-Class	(1.1%)	22.3%	n.a.	27.8%
EUR-Class	(0.8%)	19.5%	n.a.	24.1%

Largest Holdings

China Merchants Bank	7.3%
China Infrastructure	6.9%
Cosco International	5.4%
Fu Ji Food & Catering	5.3%
Shui On Land	5.0%
Epure International	4.6%

Exposure

Industrials	30.4%
Consumer Discretionary	24.1%
Financials	18.2%
Consumer Staples	4.2%
Transportation	3.7%
Energy	3.3%
Utilities	2.9%
Telecom Services	2.2%
Information Technology	1.9%
Materials	1.8%
Cash	5.9%

General Information

Legal Nature	Swiss Investment Fund, "Kategorie: Übrige Fonds"
Approved Launch	August 2006 by Federal Banking Commission November 17, 2006
Currency Classes	USD, CHF, EUR
ISIN, Valor, WKN	USD-Class CH0026828035, 2682803, A0LC13 CHF-Class CH0026828068, 2682806, A0LC14 EUR-Class CH0026828092, 2682809, A0LC15
Bloomberg	HSZCHID, HSZCFCH, HSZCHEU

Trading	Daily, based on NAV after June 30, 2007
Settlement	Euroclear, SegalInterSettle, Clearstream
Management Fee	1.5%
Performance Fee	10% above 5% hurdle rate, high water mark
Issuance Fee	Maximum 5%

Investment Manager	HSZ Group
Fund Administrator	ALG Fund Management (Schweiz) AG
Custodian Bank	ALG Private Bank AG
Main Distributor	HSZ (Schweiz) AG
Auditors	PricewaterhouseCoopers AG
Subscription	All Banks, HSZ (Schweiz) AG

HSZ Group	Woodbourne Hall P.O. Box 3162 Road Town, Tortola British Virgin Islands Tel: +1 284 494 54 14 Fax: +1 284 494 54 17 E-mail: mail@hszgroup.com
Hong Kong	Tel: +852 2287 23 00
Zurich	Tel: +41 44 288 95 95

Investment Rationale

Once the world's largest trading power, China's gradual decline during the second millennium culminated in the Maoist purgatory. However, since the 1980s economic development has taken centre stage. China has become the engine of 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.

The Fund

HSZ China Fund is an actively managed long only equity fund investing in a selection of China rooted listed mid-cap companies. The Fund consists of the three currency classes USD, CHF and EUR whereof USD is the fund's reporting currency. HSZ China Fund is a Swiss Investment Fund which has been approved by Federal Banking Commission in August 2006. After June 30, 2007 the shares are tradable daily on the fund's net asset value.

Investment Strategy

The investment focus is on entrepreneurial companies, which have a considerable long-term growth potential and whose products and services have an edge. The fund is suitable for investors with a long-term investment horizon seeking capital appreciation. Low correlation with mature equity markets is expected to deliver diversification benefits. 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% of their revenues and/or have at least 50% 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.

The Manager

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