



Dear Friends of Matthews,

I recently returned from an investment trip in China. During my trip, I visited companies in Shanghai, Guangzhou, and Qingdao.

My general feeling is that China's high economic growth rate is still intact, and the quality of growth is improving as China faces the many challenges of opening its markets after its entry into the World Trade Organization (WTO). Although China's economy is making huge strides, it is still suffering from deflation, and the income gap between the rich and the poor continues to widen.

All of the local governments of the three cities I visited are doing their best to improve their infrastructure and attract foreign direct investment. Each of the cities expects double digit annual GDP growth over the next few years. Local governments are looking to improve efficiency by hiring more highly educated people.

Working as a government official is now among the top choices for university graduates in China. Current government officials also have to improve themselves through continuous professional development. For example, my sister-in-law is taking English classes now because all government officials in Guangzhou have to pass an English test. In order to pass the test, government officials have at least a 2,000 word English vocabulary.

China is accelerating its efforts to open up its market. In the process, the Chinese government has initiated some measures that have even exceeded WTO requirements. China recently approved an investment by Newbridge Asset Management to become the controlling shareholder of Shenzhen Development Bank, one of the major regional banks in China. Newbridge will take over as the senior management team. Having a foreign investor as the majority shareholder in a Chinese financial institution is unprecedented and is beyond any WTO requirements that must be met in the first three years. More and more foreign financial institutions are looking for partners in China to jointly explore the market. Foreign financial institutions realize that they have to team up with local partners to take advantage of their huge network.

When I was in Shanghai, I went to one of Citibank's branches. It was located in a nice building with a good location in Shanghai's Pudong area. However, there were very few customers in the bank. It was quite obvious that the bank only did foreign currency business. In order to open an account with Citibank, you have to keep a balance of at least five thousand US dollars. The services they provide are quite limited, too. You can only make deposits and

remittance, and there are only six branches in China. This number compares with more than 15,000 branches for the Bank of China Group.

Higher unemployment and increasing income gaps are real issues of concern for China. With the ongoing reform of the state owned enterprises, more and more people will get laid off from their jobs and will have to find new ones. Recently, China officially admitted that its urban unemployment rate is around 7.0%, rather than the previous estimate of 3.5%. It is estimated that there are approximately 10 million laid-off workers in China, and the number is still increasing. Growing unemployment is a heavy burden and a serious challenge for the government. Over the next few years, China needs to maintain its high economic growth rate, and it has to create more jobs to absorb its abundant labor force.

This week the world witnessed an historic moment for China's Communist Party-the successful transition of power to a younger generation. Although nowadays it seems most people in China are more interested in improving their economic standard of living than keeping up with politics, the first smooth transition of leadership since the Communist Party took control of China in 1949 is truly a significant event in Chinese history.

The new generation of leadership, led by 59-year-old Hu Jintao, is expected to maintain China's economic reform commitment and bring in more capitalist-minded members into the Communist Party.

Regards,

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