Matthews Asia

Matthews Asia Dividend Fund

Period ended 30 June 2020

For the first half of 2020, the Matthews Asia Dividend Fund returned -3.16%, while its benchmark, the MSCI All Country Asia Pacific Index, returned -6.29% over the same period. For the quarter ending 30 June, the Fund returned 19.17%, while the benchmark returned 15.99%.

Market Environment:

Asian equities staged a sharp rally during the second quarter of 2020, recovering a significant portion of the steep losses incurred during the first quarter. Having learned from previous crisis moments, central banks and governments in Asia responded very quickly with an unprecedented liquidity injection and fiscal stimulus measures, providing a much-needed backstop to the real economy and to the capital market. As the Asian region, led by North Asia, effectively flattened the COVID-19 curve and started shifting focus towards economic recovery, equity investors also looked beyond the near-term corporate earnings headwind. Instead, investors were positioning for an economic rebound by bidding up equity prices.

Performance Contributors and Detractors:

The Fund performed well during the current market rally. Using a barbell approach, which invests in both higher-yielding dividend-paying stocks together with faster-growing dividend growth stocks, we steadily increased the portfolio's overall exposure towards dividend growth stocks amid the first quarter market volatility. The "dividend growth" bucket of the portfolio delivered strong returns during the second quarter. Among some of the top-performing dividend growth stocks during the quarter was China Int'l Travel Service (CITS), a Chinese duty-free store operator listed in the mainland A-share market. While travel retail industry is going through a very challenging operating environment globally, CITS saw its underlying duty-free store business in Hainan Island—a famous tourist spot for Chinese consumers, recover swiftly thanks to a favorable policy change, which increased the duty-free allowance from RMB 30,000 per annum to RMB 100,000 per annum for Chinese visitors to the island. The market responded very favorably towards this latest change, and CITS's share price more than doubled during the quarter (the company recently changed its corporate name from CITS to China Tourism Duty Free Corp, a better reflection of its underlying duty-free shopping business).

On the other hand, stocks with defensive earnings streams but with more moderated growth profiles became the relative laggards during the quarter. Top detractors to performance included Japanese wireless telecom carrier NTT DoCoMo and Japanese small-cap medical device manufacturer Eiken Chemical. Both DoCoMo and Eiken outperformed during the first quarter, as the underlying business was either minimally affected, in the case of DoCoMo's telecom business, or was benefiting from new demand due to the pandemic (Eiken introduced a COVID-19 testing kit). However, as the market moved from a defensive posture into more of a "risk-on" mode, these defensive businesses became less of a focus area for the market.

Notable Portfolio Changes:

During the second quarter, we initiated several new positions, focusing on firstly finding new dividend growth stocks whose underlying business is positively exposed to more secular growth trends. Secondly, we also added certain cyclical businesses, negatively affected by the virus outbreak, to pair with the dividend growers. The valuation discount on these cyclical businesses is very significant, but we believe the long-term strength of these companies remains intact and have the potential to rebound back from the current downturn. Among the new dividend growth names is Pharmaron Beijing, a Chinese contract-research-organization (CRO) company providing research and development outsourcing services to global pharmaceutical firms. The company is in a rapid growth phase. With rising scale, Pharmaron has seen a meaningful expansion of its profit margin and has turned free-cash-flow positive. The company initiated a dividend payment, which has been growing rapidly.

Among the cyclical recovery names is our new position in BOC Aviation, an aircraft leasing company based in Singapore. BOC Aviation's stock was heavily punished by the market, down about 35% as of the end of the second quarter because of the deep disruption to the global aviation industry. While we share the market's concern on the aviation industry headwind, from a bottom-up perspective we consider BOC Aviation to be one of the higher-quality aircraft financing vendors globally. The company is run by a well-seasoned management team who has been through multiple industry cycles. Owning one of the newer aircraft fleet assets with long-term leasing contracts, the company is also receiving a strong financial backing from its parent company Bank of China. With these relative competitive advantages, the company is adopting a counter-cycle strategy, actively expanding its aircraft leasing business during the current industry downturn. Trading at 0.8 times price-to-book against a normalized mid-teen ROE, and with a 6% trailing dividend yield, we think the risk-reward profile on the stock is quite attractive.

Outlook:

Looking ahead, we see two potential risks that could have major market implications. First, the risk of the coronavirus resurgence and its impact on the re-opening of global economy could continue to dictate short-term market volatility. While the region as a whole is better positioned for a strong revival due to more effective virus suppression, individual countries, such as India, are still struggling with their virus control efforts and economic recovery is being pushed out. Second, the downward spiral of U.S. — China relations has the potential of upending the decades'-long geopolitical stability, a crucial factor behind the booming of Asia's economy. Notwithstanding, improving signs of economic recovery, led by China, are building a solid fundamental foundation to sustain the current equity rally. In the current environment, we believe our dividend investment approach of balancing stable dividend payers with fast-growing dividend growers continues to offer a sensible way of tapping Asian-regional's long-term growth potential.

Rolling 12 Month Returns for the period ended 30 June 2020

Matthews Asia Dividend Fund	**2020**	**2019**	**2018**	**2017**	**2016**
I (Acc) (USD)	1.34%	-4.70%	9.40%	16.78%	-2.59%
MSCI All Country Asia Pacific Index (USD)	1.35%	-0.76%	10.25%	23.00%	-9.35%

Matthews Asia Dividend Fund	2020	2019	2018	2017	2016
I (Acc) (GBP)	4.78%	-1.21%	7.97%	20.77%	13.87%
MSCI All Country Asia Pacific Index (GBP)	4.40%	2.94%	8.47%	26.58%	6.65%
I (Acc) (EUR)	2.91%	-2.27%	6.99%	n.a.	n.a.
MSCI All Country Asia Pacific Index (EUR)	2.77%	1.74%	7.70%	n.a.	n.a.

Risk Considerations

The value of an investment in the Fund can go down as well as up and possible loss of principal is a risk of investing. Investments in international and emerging market securities may involve risks such as social and political instability, market illiquidity, exchange-rate fluctuations, a high level of volatility and limited regulation. The Fund invests in holdings denominated in foreign currencies, and is exposed to the risk that the value of the foreign currency will increase or decrease. The Fund invests primarily in equity securities, which may result in increased volatility. There is no guarantee that the Fund or the companies in its portfolio will pay or continue to pay dividends. These and other risks associated with investing in the Fund can be found in the Prospectus.

There is no guarantee that a company will pay or continue to increase dividends.

Performance figures discussed in the Fund Manager Commentary above reflect that of the Institutional Accumulation Class Shares and has been calculated in USD. Performance details provided for the Fund are based on a NAV-to-NAV basis, with any dividends reinvested, and are net of management fees and other expenses. Past performance information is not indicative of future performance. Investors may not get back the full amount invested.

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Investors should not invest in the Fund solely based on the information in this material alone. Please refer to the Prospectus for further details of the risk factors.

Sources: Brown Brothers Harriman (Luxembourg) S.C.A, Matthews Asia, FactSet Research Systems, Bloomberg