

---

## Matthews Asia Small Companies Fund

---

### Period ended 30 June 2018

For the first half of 2018, the Matthews Asia Small Companies Fund returned 1.91% while its benchmark, the MSCI All Country Asia ex Japan Small Cap Index, returned -7.14%. For the quarter ending 30 June, the Fund returned -0.74%, outperforming its benchmark, which fell -6.73%.

#### Market Environment:

Asian markets were volatile early in the year and became relatively steady by April and May. Investor sentiment turned fragile, however, late in the second quarter due to several events. As anticipated, the U.S. Federal Reserve raised interest rates by 25 basis points (0.25%) in mid-June. Amid this rising rate environment, the strong U.S. dollar coupled with higher oil prices further pressured broader emerging market equities. Within Asia, Indonesia, India and the Philippines tend to be more vulnerable due to their relative dependence on foreign currencies that can affect trade deficits. Meanwhile, trade war rhetoric between the U.S. and China also caused further volatility for Chinese equities as concerns spread over the potential negative economic impact to global corporations. Lastly, after months of back and forth regarding bilateral U.S.-North Korea talks, the leaders of both countries held a summit meeting in June and signed an agreement to work toward nuclear denuclearization of the Korean Peninsula.

#### Performance Contributors and Detractors:

Our holdings from China and South Korea were broadly positive performance contributors for the first half of the year. During the second quarter, the portfolio's Chinese and Indian holdings performed considerably better than holdings from elsewhere in the region, which suffered due to the challenging environment. Our stock selection in China and India also significantly contributed to both the portfolio's absolute and relative performance for the second quarter. Indian pharmaceutical and chemical company Merck, for example, performed strongly due to improving fundamentals and asset divestment news at the parent company level.

By sector, several portfolio holdings in health care and information technology were bright spots due to company-specific factors during the uneasy second quarter. Chilisin Electronics, a Taiwan-based manufacturer and distributor of inductors and coils, performed robustly thanks to the company's bold industry consolidation moves that may pave the way for future growth.

Some consumer discretionary and financials holdings were among the weakest performers within the portfolio for the second quarter. The stock prices of Hong Kong's Guotai Junan International and Ho Chi Minh City Securities in Vietnam—both brokerage businesses—experienced sharp declines due to a high correlation between their profitability and the performance of capital markets. In addition, two of our largest detractors to performance for the second quarter were Valuetronics Holdings, a Hong Kong-based electronics manufacturing service provider, and Japan's CKD, a manufacturer of factory automation equipment. Shares of both firms experienced sharp price corrections following pullbacks in revenue momentum in some segments of their businesses.

#### Notable Portfolio Changes:

During the second quarter, we exited several China positions for a variety of reasons. We shed our entire position in GDS Holdings, an independent data center operator, due to its robust share price run-up. As this company's market capitalization reached mid-cap status, we opted to invest proceeds in other less richly priced companies. We also exited Lifetech Scientific as its share price rose sharply due to a recent change among its major shareholders. We believe that such large and sudden increases in valuations were not supported by fundamentals and chose to sell our stake and lock in profits. Unfortunately, not

all of our holdings performed up to our expectations. We exited Beijing Urban Construction, a mass transit design and engineering company, due to our concerns over capital allocation decisions that we felt could compromise the company's cash flow and profitability.

Additionally, we took profits by trimming other holdings in Taiwan and South Korea that had appreciated significantly in price. We exited our long-term holdings in Ultrajaya, an Indonesian UHT milk producer. Although we deem Ultrajaya as a reasonably well-run company, we are concerned that competition will intensify, which could lead to margin contraction.

We introduced over a dozen new companies to the portfolio as we find their long-term growth trajectories attractive and supported by favorable industry tailwinds. Saigon Cargo Service Corporation is one of Vietnam's leading air cargo service providers. We believe the company is well-positioned to meet the growing air cargo handling throughputs in the country as trade volume grows. Similarly, we initiated a position in SUNeVision, one of Hong Kong's leading independent data center operators. The company is well-positioned to capture the burgeoning data traffic in the region. After the recent correction of the share price, the risk-reward profile turned more favorable in our opinion.

## Outlook:

Similar to what we observed during the first quarter, concerns over rising interest rates and dynamic geopolitical factors appear to have heightened market volatility. Such sentiment could persist for the remainder of 2018. Over the medium term, many Asian countries are poised to hold elections in the next 12 to 18 months, which can add to market uncertainty. While we are mindful of these challenges, we are encouraged by the earnings recovery thus far among many Asian corporations. We remain constructive on businesses that are well-positioned to address the needs of Asia's evolving domestic demand from services to infrastructure to technologies. As we meet with corporate managers across Asia on our research trips, we find that many small-cap companies are at the forefront of delivering innovative products and solutions to households and businesses. Such a dynamic and expansive investment landscape is a reminder of how Asia's entrepreneurialism has strived and progressed in the past decade. We look to continue uncovering attractive investment candidates that possess the attributes to grow and compound in size in a sustainable manner for the long run.

Rolling 12 Month Returns for the period ended 31 December 2017

<b>Matthews Asia Small Companies Fund</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>	<b>2014</b>	<b>2013</b>
I (Acc) (USD)	30.80%	-1.09%	-11.08%	11.14%	n.a.
MSCI All Country Asia ex Japan Small Cap Index (USD)	33.84%	-2.05%	-3.28%	2.56%	n.a.
I (Acc) (GBP)	19.38%	18.87%	-6.49%	n.a.	n.a.
MSCI All Country Asia ex Japan Small Cap Index (GBP)	22.25%	16.83%	2.32%	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. The Fund invests in smaller companies, which are more volatile and less liquid than larger companies. These and other risks associated with investing in the Fund can be found in the Prospectus.

---

Investing in small- and mid-size companies is more risky than investing in large companies as they may be more volatile and less liquid than larger companies.

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.

The information contained herein has been derived from sources believed to be reliable and accurate at the time of compilation, but no representation or warranty (express or implied) is made as to the accuracy or completeness of any of this information. Matthews International Capital Management, LLC ("Matthews Asia") and its affiliates do not accept any liability for losses either direct or consequential caused by the use of this information.

Information contained herein is sourced from Matthews Asia unless otherwise stated. The views and opinions in this commentary were as of the report date, subject to change and may not reflect the writer's current views. They are not guarantees of performance or investment results and should not be taken as investment advice. Investment decisions reflect a variety of factors, and the managers reserve the right to change their views about individual stocks, sectors, and the markets at any time. As a result, the views expressed should not be relied upon as a forecast of the Fund's future investment intent. It should not be assumed that any investment will be profitable or will equal the performance of any securities or any sectors mentioned herein. The information does not constitute a recommendation to buy or sell any securities mentioned.

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

---

#### [Prospectus](#) | [Privacy Statement](#)

Investment involves risk, including possible loss of principal. Past performance is not a guide to future performance. Investors should not invest in a Fund solely based on the information on this website. Investing in international and emerging markets may be subject to risks, such as social and political instability, market illiquidity, exchange-rate fluctuations, a high level of volatility and limited regulation.

Matthews Asia is the brand for Matthews International Capital Management, LLC and its direct and indirect subsidiaries.

This website is owned and operated by Matthews International Capital Management, LLC, Matthews Global Investors (Hong Kong) Limited, Matthews Global Investors, LLC and Matthews Global Investors S.à.r.l. Your use of this website confirms that you have read and agree to the [Terms and Conditions of Use](#) of this website.

The information on this website is for informational purposes only and does not constitute an offer to sell or a solicitation of an offer to buy any security that may be referenced on or through this website. Unless otherwise specified, it is not intended to be directed to any person(s) in particular. Information from this website must not be used in any jurisdiction where prohibited by law and must not be used in a way that would be contrary to local law or legislation. No investment advice, tax advice, or legal advice is provided through this website, and you agree that this website will not be used by you for these purposes. No representation is given that shares, products, or services identified on, or accessible through, this website are suitable for any particular investor. An investment in the Matthews Asia Funds is not available to investors in all jurisdictions; it is not available to U.S. Persons.

Investors should ascertain from their professional advisers the consequences of investing in the Fund under the relevant laws of the jurisdictions to which they are subject, including the tax consequences and any exchange control requirement. Investors should carefully consider the investment objectives, risks, charges and expenses of the Fund before making an investment decision. The current [prospectus](#), [Key Investor Information Document](#) or [other offering documents](#) ("Offering Documents") contain this and other information. Applications for shares may only be made on the Fund's most recent [Offering Documents](#) which are available from Matthews International Capital Management, LLC. Please read the [Offering Documents](#) carefully before investing.

In Singapore, this website is available to, and intended for Institutional Investors as defined under Section 304 of the Securities and Futures Act. It should not be circulated or distributed to the retail public in Singapore.

In the UK, this website is only made available to professional clients and eligible counterparties as defined by the Financial Conduct Authority (“FCA”). Under no circumstances should this document be forwarded to anyone in the UK who is not a professional client or eligible counterparty as defined by the FCA. Issued in the UK by Matthews Global Investors (UK) Limited (“Matthews Asia (UK)”), which is authorised and regulated by the FCA, FRN 667893.

If you are a resident of any other country, please go to [matthewsasiasia.com](https://matthewsasiasia.com)

©2018 Matthews International Capital Management, LLC

Powered by a [SySys](#)<sup>®</sup> data & content management system. [Cookie Settings](#)