December 2019

Matthews Asia

Sharat Shroff, CFA
Matthews Asia
Portfolio Manager

Matthews Pacific Tiger Fund Outlook

Services Sectors Shine in China; India's Reforms Benefit Entrepreneurs

The Matthews Pacific Tiger Fund invests in quality growth companies across the Asia ex Japan region. The Fund's portfolio management team takes a diversified approach that seeks to capture the region's growth across a full market cycle. In this Q&A, Lead Manager Sharat Shroff discusses his outlook for 2020 and trends he is following on the ground in Asia.

China is the largest country weight in the Fund, but the country remains underweight its benchmark, the MSCI All Country Asia ex Japan Index. Where do you see investment opportunities in China? Do you expect to increase the Fund's weight to China?

From a bottom-up perspective, we are excited about services-related companies in China. As incomes rise in China, consumers are spending more in areas such as education, health care, premium foods and beverages and entertainment. We see this as a long-term, secular trend with a long runway for growth. Importantly, businesses in these areas are competing on brand recognition, intellectual property and product quality. Innovation can be quickly rewarded in China's fast-moving marketplaces. In aggregate, the Fund is underweight China relative to its benchmark. When looking at services-related sectors in China, however, we are overweight compared with the benchmark. We have been increasing our exposure to China, but it is also important to maintain a diversified approach to investing in Asia ex Japan.

The Fund is overweight India relative to the benchmark. Over the past couple of years, India has faced macroeconomic headwinds. Do you see a turning point in India's economy? Where are you finding compelling opportunities in India today?

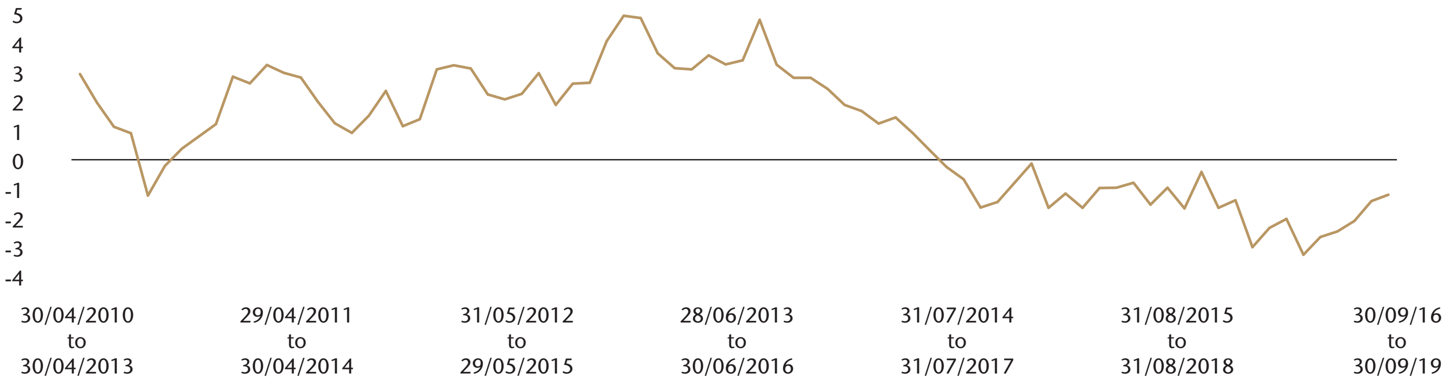
Throughout much of 2017 and 2018, Indian policymakers dealt with sticky inflation and persistent current and fiscal account deficits. At the same time, India implemented financial reforms to increase tax collections and create a more level playing field for businesses. These reforms were positive for the long term, but created softer growth in the short term. The good news is that India moved from defense to offense in 2019. The incumbent Bharatiya Janata Party won a resounding victory in this year's election, giving the majority party a clear mandate for action. Policymakers have since lowered interest rates and cut corporate taxes, both of which should be positive for growth.

As always, we invest in individual companies rather than countries. Our overweight to India is the result of bottom-up stock selection. From a company perspective, we like companies in India that can capture consumer spending and benefit from a more level playing field. Notably, the weak macro environment in India enabled some of the better-managed companies to become stronger and magnify their positions of market leadership. We have seen this trend among select financials, where better-run companies can increase their market share, and also in other consumer-related sectors.

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. These and other risks associated with investing in the Fund can be found in the Prospectus.

ROLLING THREE-YEAR EXCESS RETURNS (since inception to 30 September 2019)

Fund Outperforms Benchmark for 63% of Rolling Three Year Periods



PERFORMANCE (as of 30 September 2019)

					Average Annual Returns		
	Inception Date	3 MO	YTD	1 YR	3 YR	5 YR	Since Inception
I ACC (USD)	30/4/10	-3.89%	3.19%	0.28%	5.42%	4.68%	6.32%
MSCI AC Asia ex Japan Index	n.a.	-4.39%	5.96%	-3.15%	6.62%	4.53%	5.09%

	Rolling 12 Month Returns (for periods ending 30 September)				
	2019	2018	2017	2016	2015
I ACC (USD)	0.28%	3.62%	12.76%	20.06%	-10.66%
MSCI AC Asia ex Japan Index	-3.15%	1.74%	23.02%	17.18%	-12.15%

Source: Brown Brothers Harriman (Luxembourg) S.C.A.

All performance quoted represents past performance and is not indicative of future performance. *Investors may not get back the full amount invested. Investors investing in funds denominated in non-local currency should be aware of the risk of currency exchange fluctuations that may cause a loss of principal.*

Performance details provided are based on NAV-to-NAV with any dividends reinvested, and are net of management fees and other expenses. Performance data has been calculated in the respective currencies stated above, including ongoing charges and excluding subscription fee and redemption fee you might have to pay.

FUND FACTS

Share Class	ISIN	SEDOL	CUSIP
I ACC (USD)	LU0491816475	B48X6K0	L6263Q215

The Fund's three-year performance numbers have hit a soft spot relative to the benchmark. How are you addressing this relative underperformance?

When evaluating performance, we believe context is important. The Fund's quality bias means it may underperform the benchmark across some parts of the market cycle. Since inception in 2010 through 30 September 2019, the Fund has outperformed its benchmark over rolling three-year periods 63% of the time. The Fund has also outperformed its benchmark over rolling one-year periods 65% of the time. That said, we are continually reviewing our portfolio to make sure we are capturing our highest-conviction ideas from the bottom up and looking to where future growth is likely to come from.

Have there been any changes to the portfolio team?

We recently expanded our team, with Inbok Song rejoining Matthews Asia as a co-manager of the Fund. Early in her career, Inbok worked as a research engineer for Samsung SDI in Seoul. From 2007 to 2015, she worked at Matthews Asia, including as a portfolio manager. She brings deep investment experience to an already seasoned team of investment professionals, as well as hands-on knowledge of Asia's dynamic technology sector. Inbok also brings relevant experience in portfolio construction and risk management, which can contribute to decision-making around sizing and allocation. Her insights on some of the newer and emerging parts of the Asian economic landscape such as technology will contribute to our idea-generation process. As a co-manager, Inbok is an important contributor to our research and security selection process. We also promoted Raymond Deng from analyst to co-manager earlier in the year, reflecting his contributions to the team, especially in the area of China's services economy.

The technology sector has performed well lately—albeit with considerable volatility. How are you thinking about the sector today?

We divide the sector into two camps—IT services and IT hardware. In our view, the services side of the sector is the more interesting component. Communication services, representing areas such as digital platforms, e-commerce sites, streaming media and social media, have attractive growth potential in our view. In particular, we see South and Southeast Asia as being underpenetrated in digital business models. While China has widespread adoption of mobile payments, the digital ecosystem is still in early days for many parts of Asia.

The IT hardware sector can be quite cyclical. We believe it is prone to short-term cycles, which often are driven by global factors. So we tend to be selective in our holdings in this sector, as across-the-cycle profitability can be fairly uneven. The IT hardware sector attracted investor attention in 2019, as demand for high-end chips as necessitated by the rollout of 5G aided the stock prices of some technology hardware companies in Taiwan.

We realize our underweight in tech hardware (as well as our underweight to Taiwan, home to many tech hardware companies) was a primary detractor from performance over the past three and five years. To address this, we added resources to the team, with Inbok contributing her expertise to our stock-selection process. We are reassessing the opportunity, given current valuations and the ongoing changes to the business model for some of these companies.

Technology was a detractor from performance. What were some contributors?

For the three-year and five-year periods ending 30 September 2019, stock selection in China and stock selection in India both were contributors to relative performance. As mentioned earlier, in China we tend to focus on services-oriented companies and consumer-oriented companies that are likely to benefit from the consumer's desire for a better quality of life. In India, we have focused on companies with the ability to manage their businesses across various economic cycles, and are well-placed to gain market share during tougher times.

What do you see on the horizon in 2020?

China's broader economy has slowed a bit, but we are excited about the quality of China's growth, rather than simply the quantity. Rising incomes and consumption patterns, along with an expansion of the private sector, create more-sustainable growth opportunities. At the same time, U.S.–China trade tensions remain unresolved, and the uncertainty is a drag on corporations' investment plans, particularly in China. The trade tussle created volatility in the market, as well as buying opportunities among quality companies with attractive growth prospects.

Elsewhere, we find a lot to be optimistic about in India's future. The recently lowered corporate taxes and improving liquidity should benefit earnings for better-managed companies. Earnings were revised up and could continue to rise as the effects of India's fiscal and monetary stimulus work their way into consumer's pockets. Risks to India's economy include any potential shocks to oil prices based on geopolitical conflicts, as India imports most of its energy, and prolonged disruption in the financial system.

Looking ahead, we will continue to watch for secular growth trends driven by Asia's consumers. As a result of our bottom-up investment process, our strategy currently tilts toward countries less represented in the benchmark. This is where we see the next generation of quality growth companies emerging within Asia. Take the example of Indonesia. As more people enter the country's middle class, demand for health care is an offshoot of that growth. As incomes rise, people want better health care and a better quality of life. We believe this type of consumer spending is a durable form of growth that can benefit investors with a long-term mindset.

Definitions

The MSCI All Country Asia ex Japan Index is a free float—adjusted market capitalization—weighted index of the stock of markets of China, Hong Kong, India, Indonesia, Malaysia, Pakistan, Philippines, Singapore, South Korea, Taiwan and Thailand. Index is for comparative purposes only and it is not possible to invest directly in an index.

Excess Return is a measure of how much a fund has outperformed or underperformed its benchmark.