Matthews Asia

Matthews Asia Perspective

Q&A: Yu Zhang, CFA

Lead Manager, Matthews Asia ex Japan Dividend Fund

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Portfolio Manager
Matthews Asia

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.

Matthews Asia ex Japan Dividend Fund was launched in November 2015. How does it differ from other offerings by Matthews Asia?

The Fund's philosophy and focus behind stock selection are identical to our flagship Matthews Asia Dividend Strategy, launched in 2006, and managed by the same experienced investment team. Taking a long-term total return approach, we look to identify businesses with growing and sustainable dividends across the Asia Pacific ex Japan region, while Matthews Asia Dividend Fund's remit includes Japan.

What differentiates the Matthews Asia ex Japan Dividend Fund from other Asia ex Japan equity income Funds?

We focus on the sustainability of the dividend stream. Drawing upon a long-term total return approach, we use dividends as an indicator of core earnings growth and strength of the company. In contrast, some Asian equity income portfolios tend pursue higher yield without fully understanding how sustainable those yields may be.

The companies we seek to invest in range from small and mid-caps that may be yielding 2% to solid businesses that may yield 4–5% but potentially growing their dividends at a 15% rate. This balanced approach seeks to create a portfolio that can benefit from an attractive dividend yield without giving up on growth.

We have a lot of flexibility: if the market is hot, the natural thing for us is to take a step back and look in the other direction. If everyone is looking for yield, we would look for growth; if they start paying more for growth, we would move the portfolio back towards yield.

We have a dedicated team of investment professionals that have 2,500 company meetings every year, looking at all businesses through the Asian dividends framework. We also meet with companies' competitors and suppliers to gauge their outlook.

Does Asia provide an attractive source of yield and dividend growth?

Yes, Asia not only offers a diversified source of income for investors but has been the region with the fastest dividend growth over the past 10 years. Asia also continues to have the potential to be one of the fastest growing regions of the world over the coming decade. We take a total return approach to managing the Matthews Asia Dividend Fund, focusing on investing in a combination of stable dividend payers and dividend growers. This combination attempts to provide investors with the opportunity to benefit from an attractive dividend yield as well as exposure to companies that are growing their dividends at a faster rate than typically seen in developed markets.

How do you mitigate volatility?

The behaviour of a dividend portfolio tends to be less volatile than the market: the security of receiving a dividend yield enables us to pursue a reasonable level of total return without chasing faster-growing, but more volatile investments. That is a double-edged sword, however: if the market goes up, we do not necessarily follow at the same pace. But in down times, we may have an element of protection.

Traditionally many of the Asian markets have been considered growth rather than income markets. What is the case for investing in Asian dividends?

Take the case of the legendary Formula 1 driver Nigel Mansell. He started many races, but did not always win the world championships as something would happen to his car: the wheels would fall off, he would run out of petrol, etc. All of this needed to be sorted out at the pit stop. For us, as investors in Asian companies, dividends are that pit stop. You need to pay attention to whether the company is actually generating cash. If it is, will it share it? Although the business may be growing, are you getting overexcited about that growth and overpaying for it?

This is the philosophy we have developed at Matthews Asia since 1994: it is really about dividend growth, making sure investors benefit from the underlying cash stream of businesses, rather than just focusing on income generation.

Where are you finding attractive dividends?

Dividend opportunities abound not only in countries where structural reform efforts and an increasing emphasis on shareholder returns support better corporate governance practices, such as China and South Korea, but also in those that are less in the limelight such as Vietnam, Indonesia, Thailand and Bangladesh. We also see more opportunities in consumer-related businesses, as opposed to companies which are more export or cyclical in their nature.

As bottom-up stock pickers, we continue to pay attention to firms with the following attractive characteristics: sustainable business models; a strong capacity for generating free cash flow; and management teams that make smart capital allocations between funding business growth and returning excess cash to shareholders. As always, we are mindful about how much we pay for the shares of businesses. Asia equities today provide intriguing total return opportunities for investors, anchored by attractive dividend yields and improving dividend growth prospects.

What are some of the most prevalent investment themes in Asia?

Looking at the past 30 years, inequality across the world has been decreasing (although it could be increasing within certain individual countries). This development has resulted in the rise of the middle class, so an opportunity for us is to find companies that will facilitate that middle-class life. This is an ongoing trend, likely to continue for the next 30 years. According to the Organisation for Economic Co-operation and Development's estimation, by 2060, Asia will account for two-thirds of middle-class spending in the world.

Companies that should gain from that spending include businesses in industries as varied as retail, consumer staples and goods, consumer discretionaries, autos, media, leisure, entertainment, tourism, insurance and wealth management. Consumer and auto loan businesses of banks as well as healthcare are also expected to benefit—whether it is a high-street establishment like an Asian version of Boots, or a more sophisticated business, such as a healthcare equipment manufacturer, a private hospital or a drugs company.