

MATTHEWS ASIA ASIA SMALL COMPANIES I GBP

May 2016

Outcome: Capital Accumulation

Asset Class: Equity

IA Sector: IA Asia Pacific Excluding Japan

Domicile: Luxembourg

Rating: A

Currency: GBP

Fund Size (as at 26 Apr 2016): £49.1m

Fund Manager Name: -

Benchmark: MSCI AC Asia ex Japan Small Cap index (USD)

Active/Passive: Active

Distribution Pay Date:

Ongoing Charge Figure: 1.75%

Annual Management Charge: 1.00%

Yield (as at 26 Apr 2016): -

Volatility: -

Financial Express Crown Rating: N/A

Financial Express Alpha Manager Rating: -

Fund Price: £11.0

Launch Date: 30/04/2013

Performance Objective: Aims to deliver superior excess returns over a market cycle.

Fund Outcome

The fund aims to provide long-term capital appreciation through a portfolio of Asian ex Japanese small cap stocks. Historically the share price performance of smaller companies has been more variable than larger capitalisation stocks. Potential investors can experience both significant gains as well as huge capital losses. Whilst acknowledging the inevitable ups and downs in the asset class, we believe the fund offers investors a more conservative outcome relative to other smaller companies funds in the region, provided one is prepared to invest with a long-term horizon.

Outcomes

Capital
Accumulation

Capital
Preservation

Income

Inflation Protection



Fund Opinion

We think this fund has plenty of appeal. Although the group may be relatively unknown to the European investor base, Matthews International Capital Management is one of the largest dedicated Asia investment specialists in the US and has been investing in Asia since 1991 through a variety of market conditions. Despite the firm's substantial assets under management, each strategy has a dedicated team of portfolio managers and analysts. Although Matthews launched this fund in April 2013, the manager, Lydia So, has been running the strategy since 2008 via the US-domiciled Matthews Asia Small Companies. This mutual fund is also managed along identical lines to the Luxembourg-domiciled vehicle.

We like the fact that Ms So has been managing the strategy in a consistent manner seeking sound longer-term investments irrespective of market fads. Support is good with two co-managers backing Ms So and they can bounce ideas back and forth with the wider team which include the China Small Companies Team of managers and analysts. All this, we see as an advantage to have in an asset class that is an integral part of the region's economy. We think the strategy provides investors access to an attractive but under-researched universe via a fund that is well designed with a long-term approach directed towards uncovering higher quality businesses with hardy business models.

Fund Description

The fund offers investors a more conservative approach to this specialist area of the region and would be better suited to investors with a longer-term horizon, especially as Asian small cap equities have tended to be more volatile than their large cap counterparts in periods of extreme market dislocations. Importantly, Matthews are long-term investors who employ an investment philosophy and process that is consistently applied across the fund range - common across all their portfolios is a belief that Asia's long-term growth prospects remain strong, and investing in businesses that grow with the development of the region's middle-class lifestyles provides a good backdrop for returns.

The fund can invest in firms across a fairly wide market capitalisation range, typically between \$100 million to \$3 billion at time of purchase although it can also invest in firms as large as the biggest constituent in the MSCI AC Asia ex Japan Small Cap index. However, the strategy tends to focus on the companies at the lower end of the spectrum. Idea generation can come from research trips to Asia, intelligence from the wider Matthews Asia team and quantitative screens. Fundamental research and on-the-ground due diligence are the foundation blocks of the process with particular attention paid to the quality of a company's business, management team and valuation. Given the general lack of coverage of this area as well as corporate governance issues which can be prevalent in the region, the team regularly travel to Asia to meet with the company management teams and to ensure that information is properly disclosed. Factory/site visits and channel checks with the supply chain and competition aid in building an overall picture of the businesses involved and their industries.

The manager and her team are long-term investors and there are certain characteristics in a firm that they would like to see; these include a sustainable business model capable of profitable growth, solid financials (in the form of balance sheet strength and cash flow generation, for example) and good corporate governance. They look for businesses that can deliver throughout the business cycle, and are well positioned to adapt to the region's dynamic economic landscape; ideally these would be firms that can expand sensibly over time while focusing on sustainable returns on capital and have pricing power. They aim to determine whether companies have both the desire and the financial wherewithal to implement their growth strategies. The team use a range of valuation methods as ideally they are aiming to buy attractively valued companies where the market will ultimately recognise their growth credentials as well as their price earnings multiple expansion/re-rating potential.

The portfolio will typically have 60 to 80 holdings; the size of the individual positions will depend on the manager's conviction, valuation and liquidity considerations, however, generally the largest positions have tended to be just under 2%. Sector and country allocation is primarily a function of stock selection.

Fund Objective

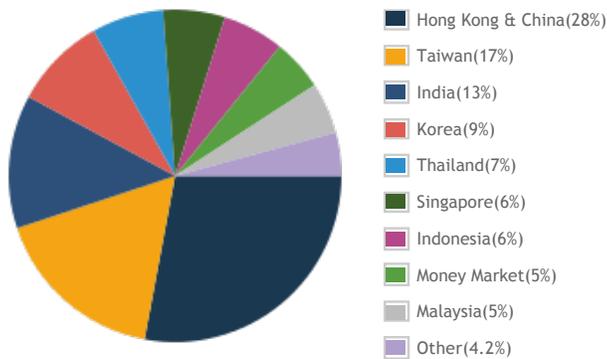
The managers are looking to deliver superior excess returns over a market cycle. Whilst there are no explicit performance objectives, Square Mile considers the approach consistent with an outperformance of 2.5% above the MSCI AC Asia ex Japan Small Cap index (USD) over rolling 3-5 years. Their approach will also attempt to minimise drawdowns – in fact Matthews are more focused on protecting in a down-market environment than keeping up with markets in a bull rally.

Quantitative Data

Performance



Geographic Breakdown



Cumulative Performance

(Data as at 26 Apr 2016)

Period	Fund (%)	Sector (%)	Quartile Ranking
6 months	4.2	4.6	1
1 year	-12.8	-10.9	2
3 years	-	3.8	-
5 years	-	10.0	-

Discrete Annual Performance to Last Quarter End

Period	Fund (%)	Sector (%)	Quartile Ranking
0-12m	-11.6	-8.1	3
12-24m	24.2	19.4	1
24-36m	-	-6.9	-
36-48m	-	16.0	-
48-60m	-	-6.1	-

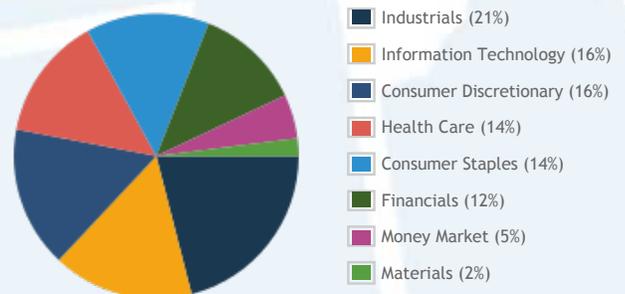
Top Ten Holdings

(Data as at 29 Feb 2016)

Company Name	%
VITASOY INTERNATIONAL HOLDINGS	2.9
FAIRWOOD HLDGS	2.6
PCHOME ONLINE INC.	2.5
I-SENS INC	2.4
KERRY LOGISTICS NETWORK LTD	2.3
SUNNY OPTICAL TECHNOLOGY GROUP	2.0
KCE ELECTRONICS	2.0
AEROSPACE INDUSTRIAL DEVLPMNT CORP	2.0
VOLTRONIC POWER TECHNOLOGY CORP	1.9
KAREX BERHAD	1.9

Sector Breakdown

(Data as at 29 Feb 2016)



Risk Summary

The strategy seeks to invest in attractively valued companies that can build sustainable competitive advantages over time, have prudent capital management and quality management teams and whilst it may lag in very sharp rising markets when risk appetite is high and lower quality stocks are in demand, in down markets, it ought to be more resilient given the types of companies it invests in. Investing in this region brings with it certain risks and considerations for the potential investors. Typically the share price performance of smaller companies is more volatile than larger capitalisation stocks during up markets and more vulnerable to declines during weaker periods. Corporate governance issues at a company level can occur as can poor liquidity of stock (due to large portions being held by small numbers of investors).

FE Risk Rating

96

SRRI

7

Qualitative Risk Assessment

	Significant	Potentially Significant	Not Significant
Equity Risk	●		
Interest Rate Risk		●	
Credit Risk			●
Exchange Rate Risk	●		
Liquidity Risk		●	
Emerging Markets Risk	●		
Derivative Risk			●
Manager Risk	●		

Equity Risk

The fund is predominately invested in shares. Shares are volatile investments and this volatility is typically heightened at times of economic stress.

Interest Rate Risk

The fund is an equity fund. Higher interest rates may adversely affect valuations of shares.

Credit Risk

This fund does not have significant exposure to corporate debt.

Exchange Rate Risk

The fund predominately invests overseas and it is exposed to foreign currencies. Currency markets may move sharply.

Liquidity Risk

The fund invests in smaller companies which could be difficult to sell at certain times. The risks of this happening are most acute at times of financial distress.

Emerging Markets Risk

The fund predominately invests in emerging regions. Economic, political, legal and market events in the region may have a material adverse effect on the fund price. Valuations in emerging market assets can be volatile.

Derivative Risk

The portfolio is predominantly invested in underlying cash securities.

Manager Risk

The manager is seen as an important element in Square Mile's rating of the fund, although potential alternatives may exist elsewhere in the organisation. Square Mile would reappraise the rating if the lead manager were to leave.

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