



Matthews Asia Innovative Growth Fund

I (Acc)

Commentary

Period ended 31 December 2023

For the year ending 31 December 2023, the Matthews Asia Innovative Growth Fund returned -2.62%, while its benchmark, the MSCI All Country Asia ex Japan Index returned 6.34%. For the fourth quarter of the year, the Fund returned 5.52% versus 6.48% for the benchmark.

Market Environment

2023 was challenging on many levels for Asia equity markets. At the macro level, rising interest rates and a strong U.S. dollar were headwinds for the region. Growth companies were out of favor while value companies relatively outperformed. Geopolitical tensions between the U.S. and China also remained elevated, particularly in the first half, and we expect these tensions to continue. The most notable feature, however, was the prolonged weakness of the Chinese economy. The rapid post-COVID recovery that many investors expected didn't materialize and the country instead struggled with a lack of confidence and problems in specific sectors like real estate. Mitigating China's woes somewhat was India's continued resilient growth, supported in part by its domestic infrastructure programs and increasing global trade. Information technology (IT) was the largest contributor to returns in the region, while communication services was among the laggards. Toward the end of the year, there was a general consensus that inflation had peaked in the global economy and that the U.S. Federal Reserve would pivot toward cutting rates in 2024 and the dollar would weaken. This provided some tailwinds across the region in the final quarter of 2023.

Performance Contributors and Detractors

Regionally, our stock selection in China/Hong Kong was the biggest detractor to total and relative returns in 2023. Our exposure was hurt by the much slower-than-expected recovery in China, international concerns over geopolitical risks, and regulatory uncertainties related to technology companies. Stock selection in South Korea and India detracted from relative returns as did an underweight in Taiwan which rallied last year. In India, selection was hurt by not owning more utilities and infrastructure-related names. We added more exposure to infrastructure-related companies in the last quarter. On the other hand, an off-benchmark position in the U.S. was the top contributor to relative returns. We invest in companies that are generating more than 50% of their revenue from Asia but are not necessarily based in Asia. An underweight to Thailand and lack of exposure to Malaysia also contributed.

At the sector level, stock selections in communication services and health care were the biggest detractors from relative returns. In contrast, stock selection in real estate was the top contributor; a lack of exposure to utilities and materials also contributed.

On a company basis, PDD Holdings, the Chinese operator of the Pinduoduo e-commerce app, was the best biggest contributor to total and relative returns in 2023. PDD has been gaining market share in China and its overseas unit, Temu, has been growing rapidly. Alchip was the best performer and another big contributor to returns. The Taiwan-based provider of silicon designs and manufacturing services for the chip industry is well positioned, we believe, to benefit from on-going developments in the artificial intelligence (AI) industry. E-commerce giant Alibaba was the biggest detractor to returns and Kuaishou Technology, a video-sharing platform, also detracted. Alibaba's topline growth slowed in 2023 and it lost market share to competitors. Kuaishou's fundamentals are still sound in our view, but the stock has suffered amid persisting uncertainties around China's regulatory environment.

Notable Portfolio Changes

We reduced our China exposure in the portfolio in a meaningful way in the last quarter as we feel the opportunity set has shrunk due to higher regulatory risks, a persisting weak domestic economy and soft consumer sentiment. Among our exits were Alibaba, digital services platform Baidu, video platform Bilibili and Kuaishou Technology. On

the other hand, we added Godrej Consumer Products, an India-based consumer staples company, and Shenzhen-based BYD Company, the world's largest maker of electric vehicles (EVs). In India, consumer staples is one area that will continue to see stable growth going forward, in our view, and Godrej Consumer Products is well positioned to benefit. BYD surpassed the EV market share of Tesla in the last quarter. We are focusing on Chinese companies with competitive international business models and BYD fits into this strategy well.

Outlook

Overall we're optimistic for 2024. We pivoted during the last quarter of the year to adjust the country weightings in the portfolio to address on-going evolution in the region. China remains challenging. We believe the government is not making necessary reforms to improve its domestic economy and unless we see a firm change in policies and an improvement in the regulatory environment we will maintain a cautious view on the Chinese equity market.

In contrast, we are optimistic on India. It doesn't have the same issues that have negatively impacted the Chinese market and, in many ways, India has the potential to replicate the success that China has had in the past 20 years. Valuations, however, remain elevated and we will be very selective in picking our investments.

More generally, the semiconductor industry is passing the bottom of the cycle and Asia maintains its leading edge when it comes to the foundry and the memory segments which are the backbone of the global industry. The consumer market in Asia also remains the largest and fastest growing market in the world and provides a great foundation for innovation and entrepreneurship to flourish.

Rolling 12 Month Returns For the period ended 31/12/2023 - I (Acc)

Name	2023	2022	2021	2020	2019	Inception Date
Matthews Asia Innovative Growth Fund (USD)	-2.62%	-24.74%	N.A.	N.A.	N.A.	23/03/2021
MSCI All Country Asia ex Japan Index (USD)	6.34%	-19.36%	N.A.	N.A.	N.A.	
Matthews Asia Innovative Growth Fund (GBP)	-7.94%	-15.66%	N.A.	N.A.	N.A.	23/03/2021
MSCI All Country Asia ex Japan Index (GBP)	0.34%	-9.19%	N.A.	N.A.	N.A.	

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

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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