Matthews Asia

2020 Stewardship Report

Matthews Asia

Robert Horrocks, PhD
Chief Investment Officer

Kathlyn Collins
ESG Analyst

Welcome to Our 2020 Inaugural Stewardship Report

Working diligently to help our clients reach their financial goals, at Matthews Asia, we are mindful of the role of capital in shaping the world we want to live in. As engaged shareholders and bondholders in our portfolio companies and issuers, we seek to foster their sustainability—and profitability. We also strive to be good global neighbors and citizens. We believe economic progress requires a healthy environment where people can live and work, and a broad middle class supporting economic growth and social inclusion. Economic progress is also supported by transparent corporate governance structures that can help attract domestic and international capital.

In our inaugural Stewardship Report, we reflect on the process of formulating our approach to Stewardship, with a particular focus on how we implement active ownership and the general governance around this process. We then recap a year of voting and engagement with the companies in the Matthews Asia portfolios. And we'll also take a look under the hood with some in-depth thematic case studies.

Stewardship

Stewardship refers to investors acting as responsible capital providers by monitoring and influencing corporate behaviors for the better—through both voting and engagement. Stewardship requires a long-term view, and treats environmental, social and governance (ESG) issues as important considerations in the traditional operational and financial metrics of a company's performance. The premise, supported by a growing body of research, is that responsible voting and active engagement will drive better corporate behaviors and more sustainable financial returns. This in turn contributes to the healthy long-term development of capital markets globally.

> *Over the past decade, stewardship codes have proliferated across global markets, aiming to provide guidance to institutional investors on how best to fulfill their responsibilities to their clients and beneficiaries and act as "stewards" of capital.*

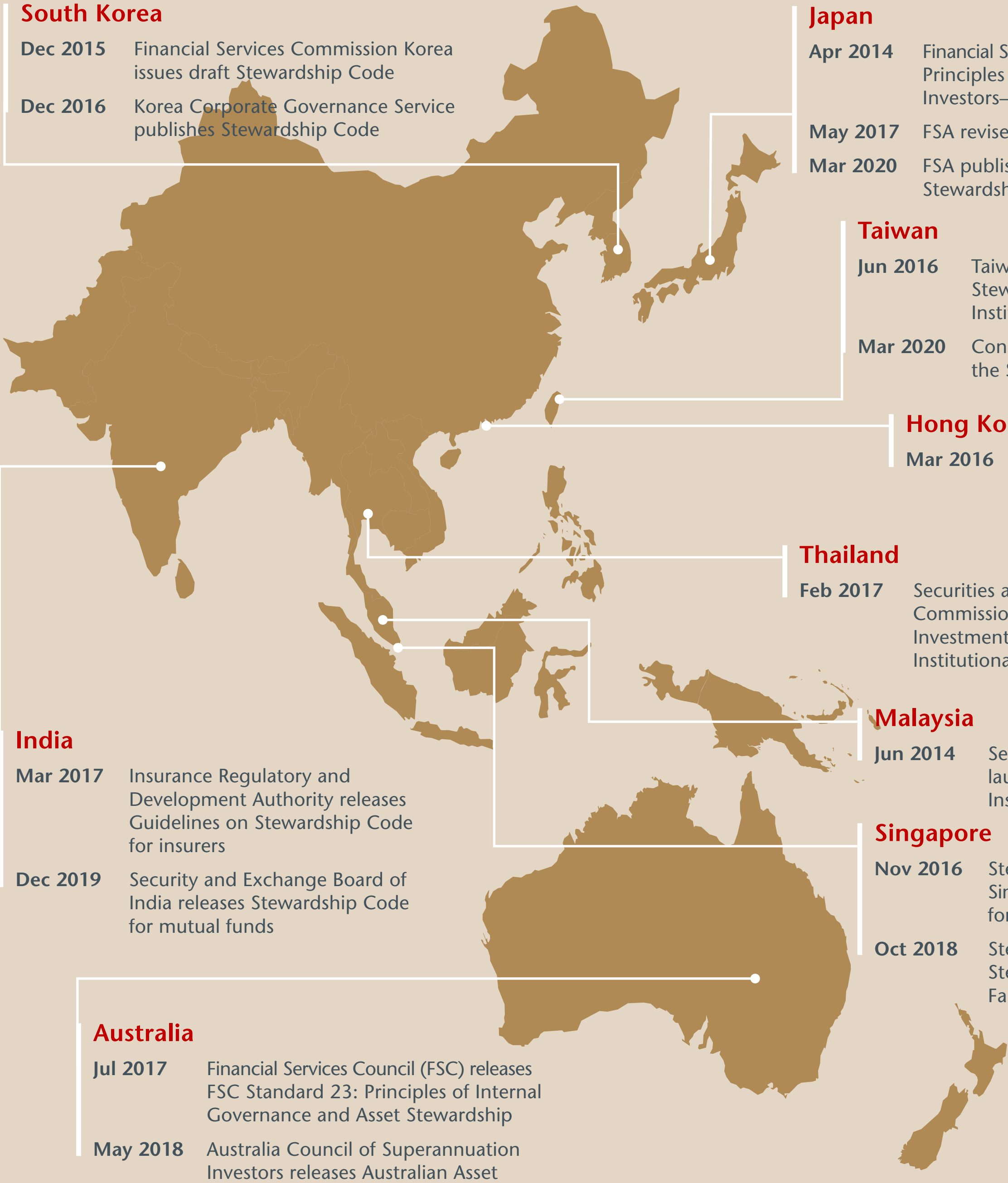
As the CFA Institute points out, in the investment management industry, stewardship is generally defined as the engagement by institutional investors with publicly listed companies to generate long term value for shareowners. Stewardship is part of responsible investment, and therefore includes the means by which asset managers effect change over time and the progress made through active ownership and voting activities. Stewardship contributes to the healthy functioning of markets and delivers good outcomes for their ultimate beneficiaries. As can be seen in the following image, stewardship codes have proliferated across global markets, but especially so in Asia. They are intended to provide guidance to institutional investors (including asset owners and asset managers) on how best to fulfil their responsibilities to their clients and beneficiaries and act as "stewards" of capital. They are part of the wider corporate governance framework, in which publicly listed companies are guided by corporate governance codes and institutional investors are guided by stewardship codes. Today, investment stewardship has momentum, much of which is coming from the markets where we invest. In Asia Pacific, regulators and industry bodies have been proactive in the adoption and development of such codes. Codes were adopted in Hong Kong SAR (March 2016), Taiwan (June 2016), Singapore (November 2016), Thailand (February 2017), India (March 2017), South Korea (March 2017), and Australia (July 2017).

Source: CFA Institute

Matthews Asia Corporate Governance and Stewardship Sub-Committee

Matthews Asia's Corporate Governance and Stewardship Sub-Committee was established to oversee matters related to corporate engagement—in particular stewardship and active ownership—that pertain to the firm and its direct and indirect subsidiaries. The Corporate Governance and Stewardship Sub-Committee is charged with implementing Matthews Asia's Responsible Investment activities, active ownership principles, stewardship and ESG integration, as well as monitoring and reviewing engagement outcomes. In addition, the Corporate Governance and Stewardship Sub-Committee is responsible for staying abreast of the legal framework of minority shareholder rights in the markets where Matthews Asia operates as it related to both individual and collective engagement. Together with the Matthews Asia Proxy Working Group, the Corporate Governance and Stewardship Sub-Committee also oversees the proxy voting process.

Proliferation of Stewardship Codes in Recent Years in Asia Pacific



South Korea

Dec 2015 Financial Services Commission Korea issues draft Stewardship Code

Dec 2016 Korea Corporate Governance Service publishes Stewardship Code

Japan

Apr 2014 Financial Services Agency (FSA) publishes Principles for Responsible Institutional Investors—Japan's Stewardship Code

May 2017 FSA revises Japan's Stewardship Code

Mar 2020 FSA publishes 2020 revision to Japan's Stewardship Code

Taiwan

Jun 2016 Taiwan Stock Exchange launches Stewardship Principles for Institutional Investors

Mar 2020 Consultation launched to update the Stewardship Principles

Hong Kong SAR

Mar 2016 Securities and Futures Commission of Hong Kong publishes the Principles of Responsible Ownership

Thailand

Feb 2017 Securities and Exchange Commission Thailand publishes Investment Governance Code for Institutional Investors

India

Mar 2017 Insurance Regulatory and Development Authority releases Guidelines on Stewardship Code for insurers

Dec 2019 Security and Exchange Board of India releases Stewardship Code for mutual funds

Malaysia

Jun 2014 Securities Commission Malaysia launches Malaysian Code for Institutional Investors

Singapore

Nov 2016 Stewardship Asia launches Singapore Stewardship Principles for Responsible Investors

Oct 2018 Stewardship Asia launches Stewardship Principles for Family Business

Australia

Jul 2017 Financial Services Council (FSC) releases FSC Standard 23: Principles of Internal Governance and Asset Stewardship

May 2018 Australia Council of Superannuation Investors releases Australian Asset Owner Stewardship Code

Source: CFA Institute

Voting Highlights

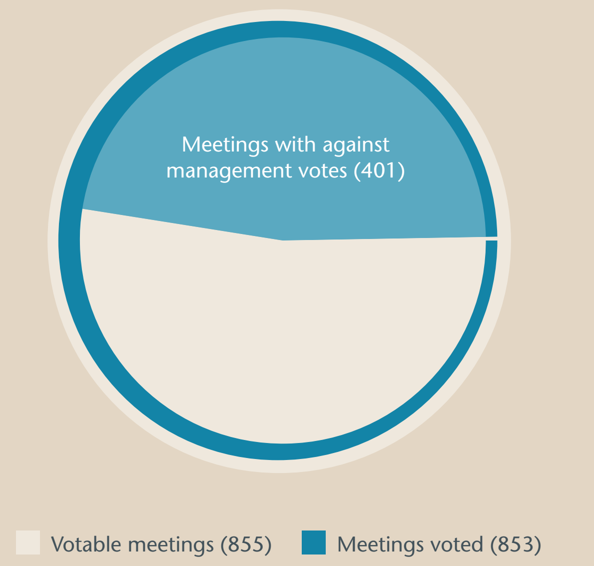
Our 2020 Highlights

- **Over 3,600 management meetings by the Matthews Asia investment team**
- **Over 7,000 agenda items voted on in 853 participated meetings**
- **More than 150 ESG-related notes entered into Matthews Asia investment team system**
- **ESG engagements with more than 50 holdings in aggregate portfolio**

At Matthews Asia, active ownership and stewardship form the cornerstone of our commitment to foster strong corporate governance. With a long history of investing in Asia and emerging markets, we are often a significant shareholder in company registries. In 2020, we conducted more than 3,600 meetings with companies throughout Asia and across broader emerging markets. Such touchpoints are also inclusive of supplier, customer and other stakeholder meetings.

Our deep and diverse 40-person investment team has a strong background in Asia and emerging markets with a range of perspectives and expertise. More than 75% of our investment professionals have lived, studied or traveled extensively throughout Asia Pacific, and over 70% are fluent in the region's languages. Respectful of diverse cultural landscapes, we take an in-person approach to company engagement, which we find more productive than filing shareholder resolutions. We also take a thoughtful and conscientious approach to voting proxies on behalf of our clients.

MATTHEWS ASIA VOTES—MEETINGS WITH AGAINST MANAGEMENT VOTES



Source: ISS

Matthews Asia—2020 Voting Trends

The votes cast during the 2020 reporting period were aligned with management recommendations in 87% of cases, while the ISS Benchmark Policy recommendations were at 88% alignment with management recommendations.

This percentage of voting in alignment with management has not changed much over the past three years; however, the degree of scrutiny of agenda items up for vote changed in 2020. In 2018, Matthews Asia voted against benchmark ISS voting recommendations at less than 1% (5 of 908 votable meetings in 2018). In 2020, this increased to almost 6% (49 of 855 votable meetings in 2020). This increasing number of overrides (voting against the benchmark ISS recommendations) signals greater scrutiny of agenda items being voted upon by our investment professionals—in most cases, applying a more nuanced view.

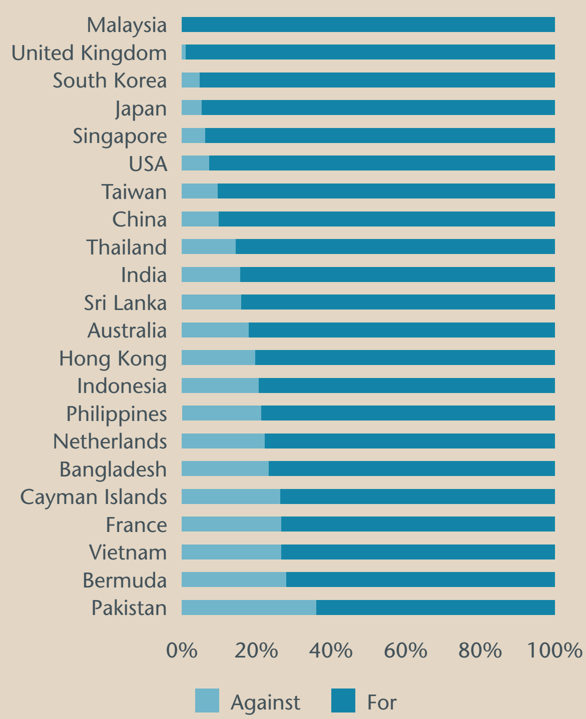
The majority of the 94 individual agenda item overrides done in 2020 was due to a differentiated view on each proposal. In some cases, we took into consideration the recommendations of specialized, domestic proxy advisors in China and India. Historically, these two markets have corporate governance characteristics (state involvement, related parties, etc.) such that we find it appealing to consider domestic proxy advisors recommendations' are appealing. These two markets are also enormous in the number of listed companies, and given our focus on small and mid-cap companies, using domestic proxy advisors with specialized teams and local context allows us to supplement our benchmark research and ensure we are voting in the best interest of our clients.

In other cases, we overrode the benchmark recommendations to vote in line with local best practice. For example, in line with the Securities and Exchange Board of India guidelines, we voted against directors holding both positions of Chairman and Managing Director as well as directors with tenures beyond the 10-year independent director limit. In another instance, we disagreed with the ISS recommendations and considered the performance parameters on a share incentive program for a company to be reasonably set, and the dilution effect to be reasonable given the growth potential for the business in question. In some situations, our decision to vote in line with or against ISS recommendations was due to company interaction and in others, it was due to supplemental research.

Proxy voting is a very important activity for portfolio managers and is a key tenet of shareholder rights. Voting is often one of the only ways that shareholders can express dissatisfaction with company management and hold them to account.

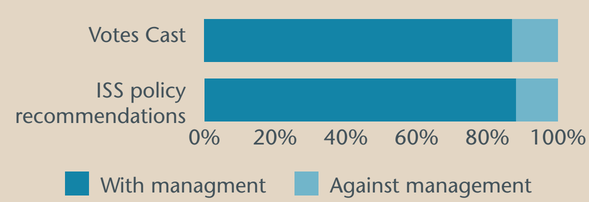
Comparing votes cast to management recommendations across the major proposal categories provides insight into the positioning of votes on proposals submitted by management against these benchmarks. Votes cast during the reporting period were least in line with management on executive compensation matters, where only 55% of votes followed management recommendations.

MATTHEWS ASIA—VOTES CAST PER COUNTRY



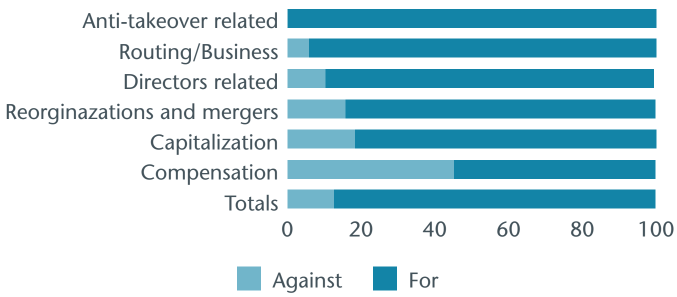
Source: ISS

MATTHEWS ASIA—VOTES CAST VS ISS RECOMMENDATION



Source: ISS

MATTHEWS ASIA—VOTES CAST PER CATEGORY



Source: ISS

Shareholder proposals—proxy ballot questions submitted by shareholders rather than corporate management—are very uncommon in the markets where we invest; however, they are an important right and tool for shareholders looking to improve corporate value. With increasing acknowledgement that environmental and social issues are material to stock performance, shareholders have been increasing the number of proposals filed, whether it be around disclosure of diversity and inclusion metrics or setting science-based targets. Only two Matthews Asia holdings have ever held votes on climate-related proposals—a company listed in the U.S. and a company listed in Australia.

Across the board, we saw changes during the 2020 proxy season brought about due to the COVID-19 pandemic. We saw a reduction in pay for executive management teams in many markets. The pandemic also caused the delay of many meetings. Most jurisdictions allowed extended deadlines for annual results, annual reports, interim/quarterly reports and annual general meetings (AGMs). COVID-19 also brought to light the issue around the use of virtual and hybrid AGMs. Many shareholder advocates question whether or not they enhance shareholder participation or disenfranchise shareholders because of management's ability to ignore or 'mute' concerns raised, which could stifle dissent. The regulation around the use of virtual meetings is another area to keep an eye on.

"At Matthews Asia, active ownership and stewardship form the cornerstone of our commitment to foster strong corporate governance."

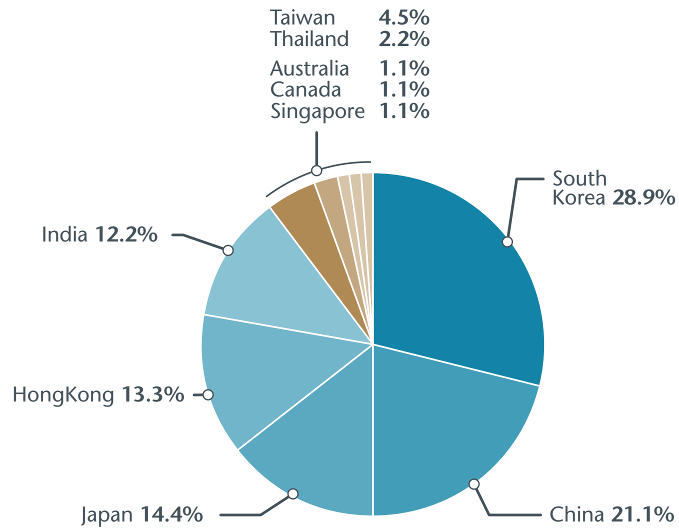
Stewardship and Corporate Governance in Asia

Today's stock markets have become more globalized, with investors both on the active and passive side ramping up engagement. As a growing share of public equity investments are being made across borders, international institutional investors often have high expectations with regard to Environmental Social and Governance (ESG) disclosures and performance of the companies in which they invest. While still relatively low, non-domestic institutional investors have increased their exposure to Asian stocks and in some cases hold a larger share of the public equity market than domestic institutional investors. The influence of institutional investors in developing markets can be beneficial in terms of raising the corporate governance standards of listed companies in developing markets.

In Japan, for example, foreign ownership of listed stocks increased from 3% to 30% between 1980 and 2017. In Japan, it has been noted that companies with higher foreign shareholding ratios are more likely to exhibit better corporate governance practices. For example, those with more foreign shareholders are more likely to have a higher percentage of independent directors on their boards and provide early notification of general meetings. In China, its markets have been changing shape over the last decade, as institutional influence expands in the onshore market and foreign investors pile in due to the inclusion of A-shares into global indices.

Understanding the differences in ownership structures in Asia is critical to ensuring the development of effective corporate governance. Listed companies in many Asian countries are characterized by concentrated ownership, with governments or family and founders owning and controlling listed companies. For example, concentrated and convoluted ownership structures are a feature in South Korea, where family-owned "chaebols" dominate the economy and business practices. Sometimes, concentrated ownership features can create potential conflicts of interest with minority investors such as asset managers who invest as fiduciaries, alongside state and family investors who may often have strategic or other priorities which go against the interests of minority investors. By understanding the nuanced ownership and governance structures in such markets and being an active advocate of stewardship, institutional asset managers such as Matthews Asia can make a significant contribution in improving corporate governance practices. We can do this by combining our fundamental knowledge of Asian companies with constructive engagement with key stakeholders, including policymakers and our portfolio companies.

MATTHEWS ASIA ENGAGEMENTS BY COUNTRY



Source: Matthews Asia

Case Studies

The Matthews Asia investment team collaborates when we engage as a company and through collective investor initiatives, including on broad market topics with regulators and exchanges. In 2020, Matthews Asia engaged on ESG issues with more than 50 portfolio holdings across strategies and had a number of notable successes. In the following pages, we highlight some of the engagements we undertook during the year.

SOUTH KOREA

ESG has been gaining momentum in South Korea over the last few years, with companies focusing on improving their disclosures to meet regulatory requirements and investor expectations. South Korea's National Pension Services, the world's third largest pension fund by assets, adopted the stewardship code in 2018, spurring further activism among other institutional investors in South Korea. Today, there are new requirements related to board directors in Korea around independent director tenure and gender diversity and starting in 2025, large-capitalization companies listed on the Korea Exchange (KRX) will be required to submit detailed ESG reports. In 2020, Matthews Asia engaged with 17 South Korean companies. Many of these engagements and conversations with management centered on typical corporate governance issues prevalent in this market such as ownership structures, board composition, independent oversight, capital management, disclosure and diversity. Other engagements and conversations were with small and mid-size companies who have only been recently rated by ESG research agencies on how to avoid being, in some cases, unnecessarily punished for a lack of disclosure. We regularly engage with our portfolio companies in South Korea on key ESG issues and risks.

Hugel, Inc.

Engagement Topics: Transparency and Disclosure, ESG Reporting

Outcome and Observation: Hugel, a South Korean biotechnology company that focuses on beauty and cosmetics related products, is making constructive progress. We began engaging the company in early 2020, with the most significant call taking place in July 2020. Prior to the call, we sent a formal agenda and asked the company to improve in three key areas: corporate communications and investor relations materials on both financial and non-financial disclosures; increasing the level of independent directors and diversity on the Board; and transparency on anti-corruption and product safety and quality, including distribution partners. Hugel's website had limited information on its financials and the company did not produce an English language annual report. It did not hold regular calls with the market, including after quarterly results. We believed that improvement on these topics would lead to an improved ESG rating by third party research agencies. We expressed our desire that the company work toward a transparency premium by improving corporate communications on its website, Investor Relations materials, and management availability for market participants. Shortly after we started engaging with Hugel, it began its quarterly analyst calls and released the company's first English language annual report, which included a section on ESG. More specifically, the company responded with increased transparency on key discussion areas such as the board members' bios, certification and product safety protocols, and compliance programs. The company also began to address shareholder concerns in a straightforward manner by addressing market concerns with regulation communications. We will continue to engage with the company on the board composition.

Leeno Industrial, Inc.

Engagement Topics: ESG Disclosure, Board Composition

Outcome and Observation: Leeno is a small capitalization South Korean company that specializes in the manufacturing of critical testing components for Integrated Circuit production, test and analysis. While the company has a dominant position in high-end R&D-purpose testing pins, it receives low ratings from ESG research providers due to the company's founder and CEO also serving as board Chairperson. We began engaging Leeno in May 2020 on this issue as well as the relatively small size of its Board (four members, including the CEO and one outside director). Following our engagements with the company, we are comfortable with the ownership structure given that the CEO has shown best-in-class execution and has not shown any minority shareholder abuse that could arise from the conflicts of interest. We believe the separation of CEO/Chairperson role may naturally be seen during the succession in the long term, as seen in many other corporates. As for the lack of human capital disclosure, while there are no disclosed policies, we believe the company's HR retention strategy is one of the best among its peers, on the back of its competitive compensation package, which is on average over 30% higher. It is also important to understand the company culture, one which values internal employees and per the company, "even janitors, parking helpers, they are very much appreciated by the management."

We spoke with Leeno again in December and we were impressed with their ESG improvement since our initial engagement in May. We expect to see the company's five year ESG roadmap during the first half of 2021, with improved English disclosure, which we think will help improve the ESG rating.

Samsung Electronics

Engagement Topics: Board Effectiveness, Minority Shareholder Treatment

Outcome and Observations: We have engaged with Samsung Electronics, the largest company in the South Korea market, over the past few years in conjunction with the Korean Working Group of the Asian Corporate Governance Association (ACGA). We engaged with the company on shareholder return policies, governance and board changes. Most recently, we had a call with the Independent Chairman of Samsung to discuss investor expectations of corporate governance as well as learn about changing board dynamics at the group. Positive changes include enhanced sustainability governance systems, improved reporting and policies related to labor association relations.

LG Chem Ltd.

Engagement Topics: Shareholder Rights, Environmental Health and Safety, ESG Remuneration Metrics

Outcome and Observations: LG Chem is the largest South Korean chemical manufacturer and a leading supplier of EV batteries. In 2020, there were a series of environmental accidents related to health and safety at LG Chem facilities. During both individual calls and through the ACGA, we expressed our desire that the company tie variable compensation to environment, health and safety (EHS) metrics to show management's commitment to safety. The company made progress by issuing a press release describing its new EHS plan to be implemented. In parallel, we have engaged LG Chem about ensuring fair shareholder treatment regarding the company's spinoff of its battery business. After the ACGA call we sent another follow-up letter to management asking for EHS key performance metrics be tied to remuneration with examples of companies that have publicly disclosed EHS metrics as part of compensation arrangements as a way to encourage the company to do the same.

The above-mentioned securities are for illustrative purpose only, they are not intended for solicitation of the purchase of such securities, and do not constitute any investment advice or recommendation.

INDIA

In India, there are now three stewardship codes for different investors: mutual funds, pension funds and insurance industry. These codes are raising the bar for domestic investors to become more involved in the voting and engagement process. There has been a notable improvement in investor engagement and participation as seen through a decline in abstention votes. India investors have also been focused on audit quality and board effectiveness with more pushback on companies' remuneration proposals and related party transactions. In 2020, we had many engagements with Indian companies around the separation of Chairperson and CEO. The Securities and Exchange Board of India (SEBI) had initially proposed regulation of mandatory separation of the Chairperson and CEO roles in 2020 as part of the Kotak Committee's Corporate Governance reforms. That regulation has been pushed back to 2022, yet board independence is a cornerstone of corporate governance, and separation of Chairperson and CEO roles is a key component of this independence. Today, 57% Bombay Stock Exchange 100 Index companies have separate Chairperson and CEO.

Tata Power

Engagement Topics: Renewable Energy, Water Management and Disclosure

Outcome and Observation: Tata Power is an Indian electric utility company and its core business is to generate, transmit and distribute electricity. We have engaged with the company for the past few years on better disclosure in its decision-making process for renewables projects and its defense business. We also engaged Tata Power on climate risk disclosure both individually and collectively with other investor groups. Tata Power has responded to questionnaires from the CDP—the not-for-profit charity that runs the global disclosure system for investors, companies, cities, states and regions to manage their environmental impacts—on climate change since 2010. In 2020, Matthews Asia was the lead investor on behalf of the CDP Non-Disclosure Initiative, which requested that Tata Power respond to the CDP's questionnaire related to water. In regard to water management, the company was identified as a priority company in a high-impact industry as it faces relatively more risk of incurring higher costs stemming from potentially inefficient water use in a water scarce country. The company completed the questionnaire for the first time earlier in 2020. We organized a call between the CDP and Tata Power to understand the company's water questionnaire score and areas for improvement. We will continue to engage with Tata Power on disclosure of water recycling metrics, sediment loading, water targets and management incentives.

"We are encouraged by the growing commitment towards sustainability norms within corporate India. The practice of sustainability isn't simply about risk management, but also a growing opportunity to inculcate clients, and attract employees. In our view, businesses like Tata Power have the power to effect change to their ecosystem and in the process, add more durability to their business."

– Sharat Shroff, CFA
Portfolio Manager

The above-mentioned securities are for illustrative purpose only, they are not intended for solicitation of the purchase of such securities, and do not constitute any investment advice or recommendation.

JAPAN

Japan has seen a surge in interest in ESG investing over the past few years and has become one of the fastest growing markets for responsible investment. This was largely due to the world's largest pension fund, the Government Pension Investment Fund (GPIF) of Japan asking its asset managers to more explicitly consider ESG factors in the money it manages on behalf of the GPIF. Japan became one of the first Asian markets to adopt a Stewardship Code in 2014, followed by its Corporate Governance Code which was revised in 2017 to further expectations of transparency and engagement. The country updated its code Stewardship Code in 2020. Foreign and domestic investors in Japan have become much more active, seen through a significant rise in shareholder proposals. In 2020, 62 companies received shareholder proposals.

We regularly engage with our portfolio companies in Japan and have had many engagements on issues related to disclosure, effective board structure and composition and capital allocation topics such as dividends and buybacks.

Mitsubishi Pencil

Engagement Topics: Investor Communication, Capital Allocation, Environmental Strategy

Outcome and Observation: Mitsubishi Pencil is the maker of the Uni-ball and Uni brands of pens and pencils. We first engaged with the company in 2019 on topics such as English language materials, succession planning, market communication and accessibility, as well as cash management. We had a call with the company in August 2020 to discuss capital management improvements and potential actions the company might take to avoid being a target for activist investors. During the call, we also learned about its ESG improvements such as steps the company is taking to reduce single-use plastics through product stewardship and innovation and the creation of an environmental policy. The company introduced a portion of variable comp in 2020, but we would still like to see improved capital allocation.

SMC Corporation

Engagement Topics: Board Effectiveness, Remuneration Disclosure, ESG Reporting

Outcome and Observation: SMC, which specializes in pneumatic control engineering to support industrial automation, has been focusing on governance changes including improving the effectiveness of the board of directors, introducing a stock compensation plan, and refreshing executive officers. The company's positive governance changes started in 2019 when its Chairman retired and the board overhauled the company's management style. Strong suggestions for improved governance also came from one of the independent directors, the CFO, and investor relations team. While we believe there are further enhancements to be made around the compensation structure and disclosure that will better link pay to performance, the changes made thus far have been noticed by market participants, with MSCI ESG upgrading the company's rating earlier this year. We believe that the company will benefit from the growth in pneumatics. While major ESG ratings do not consider the environmental superiority of pneumatics versus hydraulics, the company is exposed to the theme of energy efficiency. We engaged with the company on board effectiveness and remuneration disclosure. We followed up with best practice examples of variable compensation disclosure.

"We felt the external ESG assessment of SMC was missing the inherent sustainability benefits of the company's end products and suggested ways that the company might better communicate this to market participants."

– Shuntaro Takeuchi
Portfolio Manager

The above-mentioned securities are for illustrative purpose only, they are not intended for solicitation of the purchase of such securities, and do not constitute any investment advice or recommendation.

CHINA

The evolution of corporate governance in China has gone through several stages. Fundamental reforms over state ownership and company law mainly developed in the 2000s with the adoption of various developed market regulations, such as supervisory boards and shareholder protection. China is in the process of establishing its own guidelines for corporate governance best practices, with the 2018 China Securities Regulatory Commission (CSRC) revised Corporate Governance Code the first major indication of how this will develop. The new code promotes diversity, underscores the role of minority shareholders, promotes cash dividend distribution and generally strengthens ESG principles.

Policymakers have introduced laws and policies in recent years to promote better ESG practices and disclosure among corporations. Given that top-down economic planning features prominently in China, these regulatory initiatives are likely to further drive rapid ESG uptake by both investors and issuers. China's regulatory fund body, the Asset Management Association of China (AMAC), has announced new measures to advance the inclusion of ESG factors within the country's public pension funds and investors are anxiously awaiting mandatory ESG reporting standards for companies listed on the mainland.

We regularly engage with our portfolio companies on key ESG issues and risks. Here are three examples of portfolio holdings domiciled in China.

Shenzhou International Group

Engagement Topics: Supply Chain Disclosure, ESG Reporting

Outcome and Observation: Shenzhou, an apparel manufacturer based in China, supplies to some of the largest western sports brands. We have engaged with the company on ESG related matters since 2016. In 2020, we communicated with the company on impacts to suppliers from canceled orders due to COVID-19 and how it was responding. Given the company's vertical integration, Shenzhou was able to maintain operations and did not need to cancel orders on account of the pandemic. The company acted responsibly with regard to workers' health and safety, checking temperatures, extending lunch times and maintained all normal operations into the summer. For the company's Hubei employees, Shenzhou paid a month's worth of their salary and retained their positions while they could not come to work during the pandemic.

Shenzhou has been receptive to shareholder feedback and improved the level of disclosure in the last annual report after we engaged with them. For example, the company included energy consumption efficiency targets and initiatives to achieve them. The company also improved the level of disclosure on its supply chain standards and working conditions, which we believe will lead to much higher scores in the KnowTheChain benchmark. We continue to monitor the company's disclosure on its supplier monitoring and assessments.

Inner Mongolia Yili Industrial Group

Engagement Topics: Employee Stock Ownership Plan, CDP Reporting

Outcome and Observation: Yili is China's largest dairy producer and in August 2019, the company issued stock grants in the form of an incentive plan to key management personnel (directors, senior management and other core employees) with materially low key performance indicator hurdles, funded by its repurchased shares. We communicated to company management and expressed our concern with this practice and requested them to withdraw the plan. We engaged Yili on its Employee Stock Ownership Plan, providing feedback on the structure of the key performance indicators which eventually led the company to make some adjustments to the vesting criteria. Yili revised the Plan in favor of shareholders significantly by increasing the range of personnel to be awarded shares and making stricter return on equity and dividend targets for vesting.

We have also engaged with the company on sustainability reporting, CDP reporting and index inclusion. The company asked for our advice about joining a well-respected sustainability index which would have required significant work to complete the fairly robust and detailed questionnaire. Given that the company was responsive to our request that it complete CDP's Climate Change and Water Security questionnaires, we suggested that inclusion in a sustainability index might be an admirable target for the management team and sustainability department. Given that not many Chinese companies participate, Yili could be seen a leader in the space and increase its standing with international investors.

China Resources Beer

Engagement Topics: CDP Reporting

Outcome and Observation: China Resources Beer is one of the largest beer producers globally. In 2019, we started to engage with its management team to better understand the company's approach to sustainability and environmental and social standards, and specifically to respond to the CDP Climate Change and Water Security questionnaires. In regard to water management, the company was identified as a priority company in a high-impact industry as it faces relatively more risk of incurring higher costs stemming from potentially inefficient water use in a water scarce country. We gained clarity on the company's integration of ESG considerations into their risk management framework. In March 2020, we engaged with China Resource Beer again by phone. As the company remains a state-owned enterprise (SOE), there are still some inefficiencies that exist but China Resources Beer has improved its efficiency metrics by closing certain plants. The company has faced pressure from shareholders on sustainability reporting standards and is working to find analogous requirements among regions which we advised them on.

In May, we were again the lead investor in CDP's Non-Disclosure Campaign initiative. We requested that China Resources Beer respond to the CDP Climate and Water Security questionnaires. Given the company's plans to strengthen its control over climate change risks and explore strategies to address climate change for the short, medium and long term, we believe that reporting in line with the CDP framework would send a strong signal to investors of the seriousness with which management is dealing with such risks. In addition, reporting along the CDP framework would put the company on a similar footing with its new partner, Heineken, which has been reporting to the CDP since 2011. China Resources Beer did not respond to the CDP questionnaires in 2020, but is focusing on the requirements set by the Chinese regulatory authorities and the Hong Kong stock exchange. However, the company informed us that it would likely be in a better position to partially fulfill CDP's requirement in 2021 so we will continue to engage and push China Resources Beer on improving disclosure.

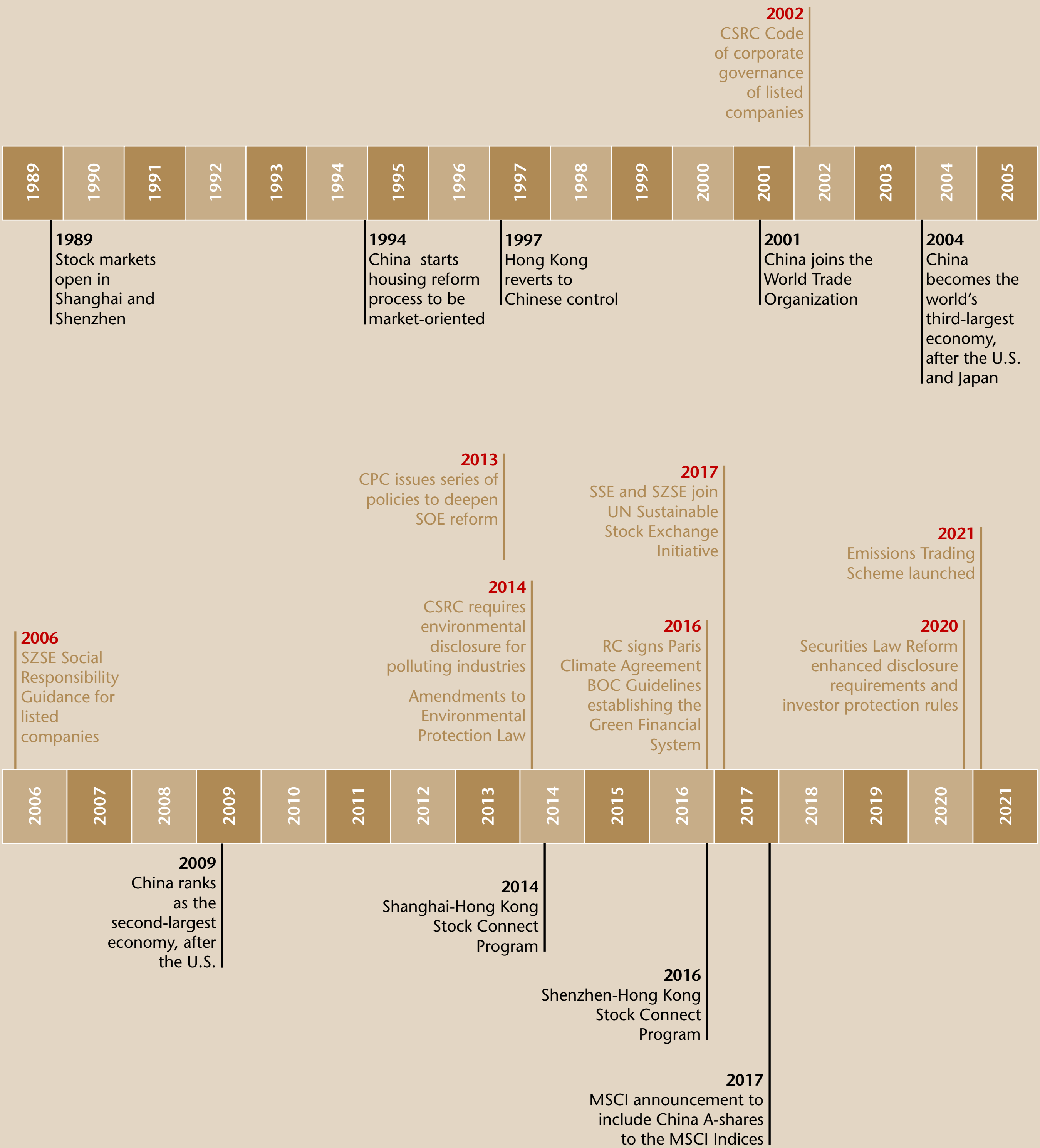
"Shenzhou has improved the level of disclosure on its supply chain standards and working conditions, which we believe will lead to much higher scores in the KnowTheChain benchmark."

–Kathlyn Collins
ESG Analyst

The above-mentioned securities are for illustrative purpose only, they are not intended for solicitation of the purchase of such securities, and do not constitute any investment advice or recommendation.

Chinese Government Paves the Way for Better ESG Practices

Evolution of mainland China ESG and disclosure-related policy changes



Source: China Securities Regulatory Commission; State Council of China;
Ministry of Ecology and Environment of China; Shenzhen Stock Exchange; Shanghai Stock Exchange

Market Engagement

As a global investor, we understand that regulations play an important part in setting corporate governance standards for each country. In addition to our engagement with individual portfolio companies, we also engage with other key stakeholders who have significant roles in shaping public policy and corporate behavior. We believe that a good regulatory framework complements market forces, while looking after the interests of stakeholders. As such, we take an active role in key organizations that advance and protect the interests of our clients. Our objective is to raise the standards of the companies and markets in which we invest on behalf of our clients.

Over the course of the year, we contributed to the following market engagements:

- In May, we participated in an investor survey on ESG Disclosure in China which was developed in collaboration with the United Nations Principles for Responsible Investment (UN PRI), China Securities and Regulatory Commission and the Asset Management Association of China. As the ESG reporting requirements were in draft form earlier in the year, this was a good opportunity for investors such as Matthews Asia to reiterate the importance of coming out with high standards that are also internationally comparable. While we still have not seen what these ESG reporting requirements will look like, we are engaging with companies in our portfolios directly to put extra resources into ESG reporting and stay ahead of mandatory reporting requirements.
- In September, we provided feedback to the Securities and Exchange Board of India, which issued a consultation paper on the format for Business Responsibility and Sustainability Reporting to be applied to a larger number of listed companies. We recommended that the framework align, where possible, with globally recognized reporting standards that already exist in the marketplace (the Sustainable Accounting Standards Board, Global Reporting Initiative). We also suggested that the regulator review current adherence to ESG reporting rules and regulation before expanding the scope to small companies with few resources.

We strive to maintain active relationships with relevant market institutions, governmental and public bodies that may be helpful for keeping up to date with local legislation and market practice for improving the institutional framework. We also support different forums for promotion of good market practice, corporate governance, other responsible practices and relevant topics that may be in the joint interest of our investors. Some of these organizations with which we engage include the UN PRI, the Asian Corporate Governance Association, the International Corporate Governance Network, the Sustainability Accounting Standard Board, and the CDP.

Over the past few years, some of the market consultations we have contributed to in conjunction with these groups included Japan's proposed amendments to the Foreign Exchange and Foreign Trade Act (FEFTA), the Hong Kong Stock Exchange's revisions to its ESG listing rules and South Korea Financial Services Commission's proposed revisions to Korea's large shareholding reporting rules. As a signatory to the UN PRI, we are committed to reporting our responsible investing activities every year and welcome dialogue with our clients about their goals and interests related to responsible investing. Earlier this year, we responded to a signatory survey on the future of the UN PRI's reporting framework, which will impact all signatories.

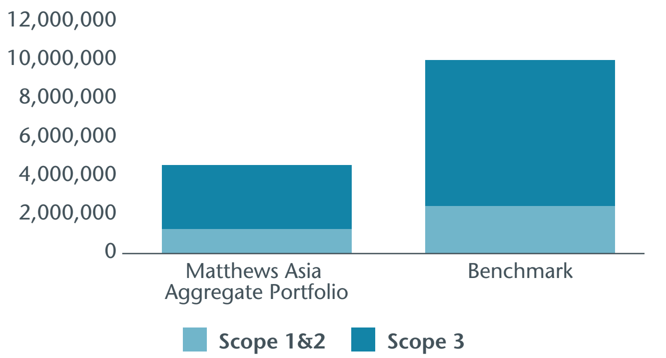
Other Themes

Climate Action

As a UN PRI signatory, Matthews Asia completed a climate assessment report aligned with the Task Force on Climate-related Financial Disclosures. To date, carbon footprinting has been the industry standard for measuring investors' climate transition risk exposure to provide a baseline from which to take action. With the help of a third party, we completed our first footprint for the aggregate Matthews Asia portfolio versus a custom benchmark based on our portfolio positions and corresponding benchmarks at the end of 2019.

This analysis showed that the aggregate Matthews Asia portfolio was half as carbon intensive as its custom benchmark, reflecting the nature of the Matthews Asia portfolios which tend to be more consumer-focused and less resource intensive than the average benchmark in Asia. We completed another carbon footprinting on holdings as of the end of 2020, and the results continue to show that our portfolios are overall much less carbon intensive versus the average benchmark in Asia.

EMISSIONS EXPOSURE (tCO_2e)



Scope 1 covers direct emissions from owned or controlled sources.
Scope 2 covers indirect emissions from the generation of purchased electricity, steam, heating and cooling consumed by the reporting company.
Scope 3 includes all other indirect emissions that occur in a company's value chain.

Source: ISS

At the end of 2020, the aggregate Matthews Asia portfolio had a weighted average carbon intensity of 153.6 tCO2 e/Millions of USD Revenue versus the custom benchmark of 256.4 tCO2 e/Millions of USD Revenue). In terms of sector contributions to carbon intensity, utilities were the largest sector, contributing 51% of the portfolio's carbon intensity, followed by materials at 24% and the informational and technology and consumer discretionary sectors, both at 7%. Matthews Asia has relatively less exposure to carbon intensive sectors such as energy and materials versus the average benchmarks in Asia. This underweight to these sectors caused the portfolio to be 49% less exposed to greenhouse gas emissions on a sector basis versus the custom benchmark.

The top 10 contributors to the aggregate Matthews Asia portfolio emissions comprised 76% of the portfolio's total emissions, but only 13% of the portfolio by weight. Four of the top 10 contributors to portfolio emissions were relative laggards in terms of managing carbon risks. We are encouraging these companies to improve disclosure of the companies' strategies, including through CDP's Non-Disclosure initiative. At the end of 2019, the aggregate Matthews Asia portfolio included 26.8% of holdings which disclosed carbon metrics, such as greenhouse gases, which was in line with the custom benchmark, but in 2020, this figure rose to 33%, which surpassed the benchmark's 29%.[1]

1. The carbon footprint data comes from ISS ESG. The two main sources for greenhouse gas emission data are Integrated Annual Reports/ Sustainability/ Corporate Social Responsibility (CSR) reports and data from the non-governmental organization CDP (formerly the Carbon Disclosure Project). ISS, the vendor for climate data, covers 95% of the holdings in the Matthews Asia aggregate portfolio (either reported or modeled) with company emissions data from 2019.

The purpose of the carbon footprint exercise was to understand the carbon intensity of the aggregate Mathews Asia portfolio and to identify areas where we may be able to engage with relative laggards when it comes to climate risk and reporting. As part of our ESG integration process, Matthews Asia's investment team members receive training on how to incorporate ESG factors, including those related to considering climate risks and opportunities in the decision making processes. Where climate implications pose a material risk or opportunity to a portfolio holding, the expected holding period and investment analysis should reflect the timescale of climate risks and opportunities. This includes the analysis of transition risks such as policy and legal risks, technology risk, market risk and reputation risk.

Despite the Matthews Asia aggregate portfolio being much less carbon intensive than the benchmark, the analysis showed that there is room for improvement in particular areas. Despite a relative underweight to the energy and materials sectors, our issuer selection effect for the utilities sector was negative. This is not surprising given companies in the utility sector in Asia are highly reliant on fossil fuels and have not been as fast as peers in Europe and North America to shift to renewable energy in electricity generation. In addition, coal, along with other natural resources, are often highly subsidized in these markets. Although renewables are becoming increasingly cost competitive, coal still remains an appealing solution for many countries that need to meet fast-rising demand for electricity and are seeking to minimize costs. The climate impact assessment specifically indicated that the utility sector is one where we can look at more closely with regard to the clean energy transition, which is an area for engagement.

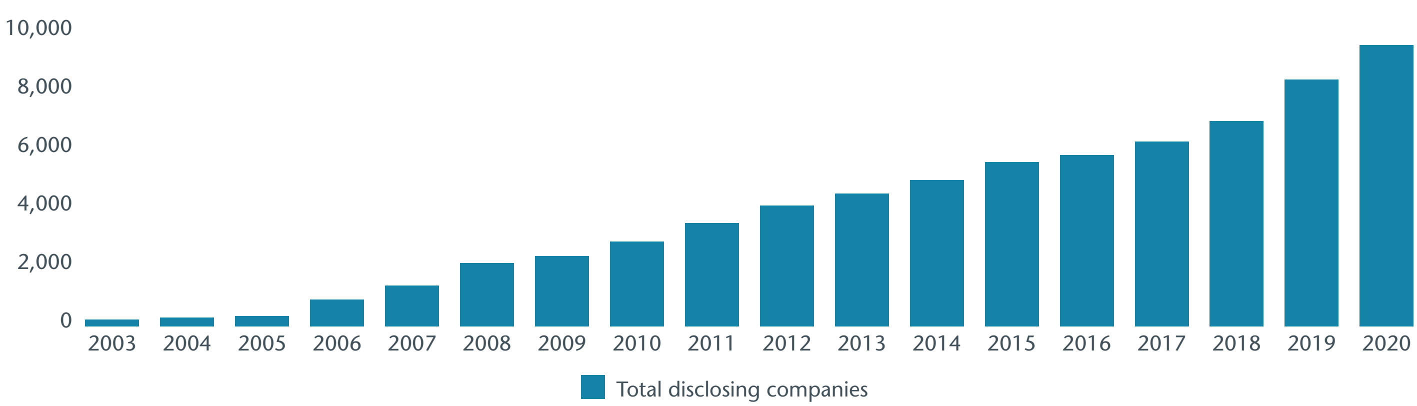
CDP

Every year, CDP—the not-for-profit charity that runs the global disclosure system for investors, companies, cities, states and regions to manage their environmental impacts—invites investors to directly engage companies who have previously failed to respond to CDP's investor request. Since beginning this program in 2017, CDP has seen a 25% year-on-year rise in both the number of investors participating and the number of companies engaged, demonstrating the growing need for comprehensive, comparable, Task Force on Climate-related Financial Disclosures-aligned environmental disclosure.

In 2020, Matthews Asia was one of a total of 108 investors representing US$12 trillion in assets who participated in CDP's Non-Disclosure Campaign to engage companies that have never responded to CDP or have not responded in recent years to help drive further transparency. Of the 1,025 companies representing US$21 trillion in market capitalization and almost 5 billion tons of carbon dioxide equivalent in emissions that were engaged, 206 disclosed data on their impact across at least one of three areas: climate change, deforestation and water security. In 2020, CDP achieved higher than ever disclosure rates with over 2,600 investor-requested companies disclosing crucial data on environmental impact.

Matthews Asia regularly engages with our portfolio holdings, including through collaborative investor initiatives such as those organized by CDP. In 2019, as part of CDP's Non-Disclosure Campaign, we signed 34 letters (and were a lead investor on one company letter) which asked companies to disclose

GROWTH IN DISCLOSING COMPANIES GLOBALLY



Source: CDP

more information related to environmental risk around climate change, deforestation and water. Six of those 34 companies we engaged with responded to our disclosure requests. In 2020, we continued to support CDP's Non-Disclosure Campaign, and signed onto 41 letters and were the lead investor on seven company letters. One of the seven companies (Tata Power) responded to our requests, and seven of the 34 companies we cosigned the letters submitted the questionnaires.

Board Diversity

For investors interested in capturing Asia's growth through an ESG lens, we offer a dedicated Asia ESG equity strategy. Similar to all of our strategies, the Matthews Asia ESG strategy follows an investment-first approach to ESG integration. We differentiate the Matthews Asia ESG strategy from other strategies within the firm by using a more expansive, positive-screening ESG factor framework focused on positive ESG outcomes. The Matthews Asia ESG Strategy adopted a stricter voting policy at companies with a lack of gender diversity on boards in 2020. We wrote letters to companies to inform them of our intention to vote against the Nomination Committee chair or Corporate Governance Committee chair and other members of the equivalent committees on their boards of directors. In the case that there was no Nomination or Corporate Governance Committee (or equivalent), we voted against both the re-election of existing board directors and also election of new board members. We engage with portfolio holdings without women on their boards within the broader context of the skills, expertise, and competencies required for effective board functioning. The Matthews Asia ESG Strategy asked all portfolio companies with no women on their boards of directors to adopt policies to consider women for every open board seat and to commit to a gender diversity policy as part of board recruitment process. As seen from the chart on the right, there is still a lot of progress to be made on this front.

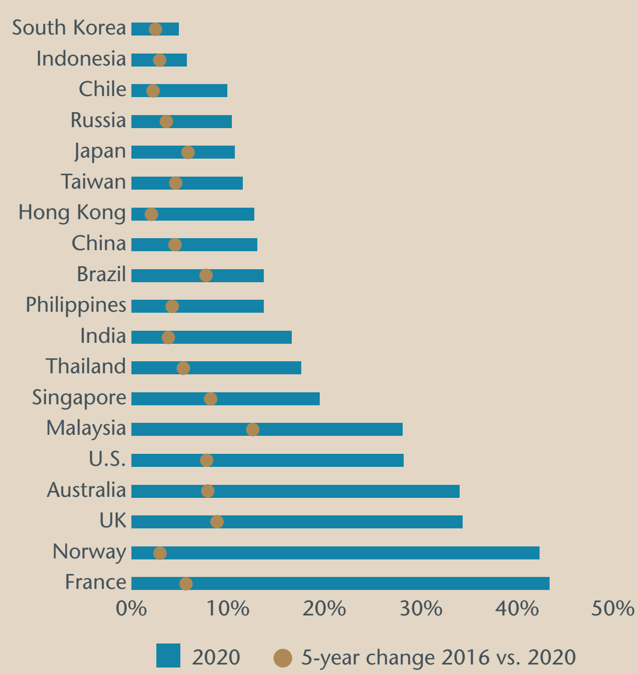
2021 and Beyond

Home to more than half of the world's population, the Asia Pacific region is an important and growing destination for global investors. At Matthews Asia, we have a responsibility to encourage more sustainable business practices everywhere that we invest. By taking a long-term, and often contrarian, viewpoint, we can engage with the companies that are shaping the world of tomorrow.

When Matthews Asia was founded three decades ago, it was with a deep appreciation of considering corporate governance structures as part of our due diligence process. Good governance is important in all markets where we invest, and especially so in emerging and frontier markets. We believe high-quality businesses run by capable and principled managers are healthier and more sustainable.

As we look to 2021 and beyond, Asia will remain at the front of issues such as climate change, social and financial inclusion, eliminating poverty and protecting global water sources and communities. Investors cannot tackle the world's most pressing issues without including Asia in their portfolio and their responsible investing approaches. In 2021, we will continue to engage with companies where we have seen limited progress on ESG related items. In addition, we are likely to focus our efforts on ESG-related engagements around improved ESG disclosures, climate change strategy, and board composition and effectiveness, among other things.

PERCENTAGE OF BOARD SEATS HELD BY WOMEN



Sources: MSCI ESG, Egon Zehnden, Deloitte

Investments involve risk. Past performance is no guarantee of future results. Investing in international and emerging markets may involve additional risks, such as social and political instability, market illiquidity, exchange-rate fluctuations, a high level of volatility and limited regulation.

Important Information

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

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 Asia and its affiliates do not accept any liability for losses either direct or consequential caused by the use of this information. The views and information discussed herein are as of the date of publication, are subject to change and may not reflect current views. The views expressed represent an assessment of market conditions at a specific point in time, are opinions only and should not be relied upon as investment advice regarding a particular investment or markets in general. Such information does not constitute a recommendation to buy or sell specific securities or investment vehicles. This document does not constitute investment advice or an offer to provide investment advisory or investment management services, or the solicitation of an offer to provide investment advisory or investment management services, in any jurisdiction in which an offer or solicitation would be unlawful under the securities law of that jurisdiction. This document may not be reproduced in any form or transmitted to any person without authorization from the issuer.

Matthews Asia