




Matthews Asia™

## Matthews Asia ESG Fund

### For the period ending March 31, 2018

For the quarter ending March 31, 2018, the Matthews Asia ESG Fund returned 1.82% (Investor Class), while its benchmark, the MSCI All Country Asia ex Japan Index, returned 0.70%.

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#### Market Environment:

Asia's markets got off to a strong start in 2018, following a very strong 2017, but could not hold onto their gains as investors worried about a faster-than-expected rate cycle by the U.S. Federal Reserve and a potential U.S.-China trade war. Pakistan (up 11%) and Thailand (up 9%) were the best-performing markets, while Indonesia and India (down about 7% each) were the worst performers during the quarter. From a sector standpoint, health care, after two years of underperformance, did well during the first quarter and was the best-performing sector (up 9.3%), while telecommunications (down 7.2%) was the worst performer. From a currency perspective, the Japanese yen, a perceived safe haven currency, was the best-performing Asian currency (up 6%), while the Philippine peso (down 3.7%) was the worst-performing currency.

#### Performance Contributors and Detractors:

From a country perspective, stock selection in China/Hong Kong and India was a major driver of performance and offset the drag from negative allocation effects from an overweight allocation to India and Bangladesh. From a sector perspective, our health care allocation was a major contributor to performance, as was stock selection in materials, while an underweight allocation to information technology detracted from performance.

At the stock level, Wuxi Biologics was the biggest contributor to performance. The company is a vertically integrated Chinese contract development and manufacturing organization (CDMO) that enables cost- and time-efficient drug discovery, development and manufacturing of biologics. Wuxi Biologics plays an important role in speeding up the innovation cycle in the global biotech industry in general and the Chinese biotech industry in particular by helping both global majors as well as Chinese biotech startups through its scaled-up CDMO model. The company announced strong 2017 results and better-than-expected new customer contract acquisition, as well as faster migration of contracts into the higher value clinical trial stage from the pre-clinical trial stage.

On the other hand, Hanon Systems, a South Korea-based global auto heating, ventilation and air conditioning (HVAC) company, was the biggest detractor to performance. The company's share price came off a strong 2017 and was weak during the quarter as the market expected first-quarter operating results to be disappointing given a slow production ramp-up at one of its electric vehicle (EV) manufacturer clients. The temporary production hiccups at its client did not materially alter our view on the company's prospects as Hanon has a strong and diversified order book and continues to win new orders. We continue to like the firm's positioning to benefit from the electrification of auto industry and its ability to win orders given its strong technology and its position as an independent vendor. We used the correction as an opportunity to add to our position.

#### Notable Portfolio Changes:

#### Average Annual Total Returns - Investor Class (3/31/2018)

1-year 21.34%  
3-year n.a.  
5-year n.a.  
10-year n.a.  
Inception (4/30/15) 7.79%

#### Gross Expense Ratio <sup>1</sup>

3.54%

After fee waiver and expense reimbursement: 1.48% <sup>2</sup>

<sup>†</sup> Actual return, not annualized.

<sup>1</sup> Matthews Asia Funds' 12b-1 Plan (the "Plan") is inactive. Although the Plan currently is not active, it is reviewed by the Board annually in case the Board decides to re-activate the Plan. The Plan would not be re-activated without prior notice to shareholders and any amounts payable under the Plan would be subject to applicable operating expense limitations. If the Plan were reactivated, the fee would be up to 0.25% for each of the Investor Class and Institutional Class, respectively.

<sup>2</sup> Matthews has contractually agreed (i) to waive fees and reimburse expenses to the extent needed to limit Total Annual Fund Operating Expenses (excluding Rule 12b-1 fees, taxes, interest, brokerage commissions, short sale dividend expenses, expenses

During the first quarter, we initiated a position in Sosei, a Japanese biopharmaceutical and a drug discovery platform company. Sosei, through its subsidiary, owns a unique technology platform to help pharmaceutical firms develop drugs by stabilizing cell membrane receptors called GPCRs. The company's platform partnership with pharmaceutical companies typically involves a combination of upfront, milestone and royalty payments to Sosei. The company also has a steady stream of royalty income from out-licensed drug sales, which supports the development of its in-house drug pipeline. We find Sosei's approach to drug development attractive as it reduces risks inherent in a pure drug discovery model. The company has a diverse management team with significant representation from outside Japan—a relatively rarity in Japan. Its board has a majority of external directors (one of whom is a woman, another relative rarity in Japan).

#### Outlook:

After a strong year of earnings growth in 2017, the prospect for continued earnings growth in Asia remains and stock valuations also remain supportive. If the current trade friction between the U.S. and China escalates, however, it might adversely impact this favorable assessment. In addition, we continue to watch for signs of higher volatility, due to factors such as a strong pickup in inflation, which might cause central banks to raise interest rates or reduce liquidity much faster than expected.

We continue to be confident in Asia's ability to effectively address global ESG challenges through its leadership position in areas including electric vehicles, access to affordable health care and financial inclusion, among others. This leadership provides an encouraging backdrop for pursuing ESG-focused investing in Asia. We also find that investing in companies that are improving quality of life in Asia is a way to address the aspirations of the newly emergent and increasingly sophisticated middle class.

We also continue to employ a fundamental, bottom-up investment process and use any market dislocation in Asia as an opportunity to buy shares of what we consider to be high-quality companies with best-in-class ESG attributes at reasonable prices.

As of 03/31/2018, the securities mentioned comprised the Matthews Asia ESG Fund in the following percentages: Wuxi Biologics Cayman, Inc. 3.5%; Hanon Systems 2.1%; Sosei Group Corp. 1.4%. Current and future portfolio holdings are subject to risk.

The views and opinions in this commentary were as of the report date, subject to change and may not reflect current views. They are not guarantees of performance or investment results and should not be taken as investment advice. Investment decisions reflect a variety of factors, and the managers reserve the right to change their views about individual stocks, sectors, and the markets at any time. As a result, the views expressed should not be relied upon as a forecast of the Fund's future investment intent. It should not be assumed that any investment will be profitable or will equal the performance of any securities or any sectors mentioned herein. The information does not constitute a recommendation to buy or sell any securities mentioned.

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incurred in connection with any merger or reorganization or extraordinary expenses such as litigation) of the Institutional Class to 1.25%, first by waiving class specific expenses (i.e., shareholder service fees specific to a particular class) of the Institutional Class and then, to the extent necessary, by waiving non-class specific expenses of the Institutional Class, and (ii) if any Fund-wide expenses (i.e., expenses that apply to both the Institutional Class and the Investor Class) are waived for the Institutional Class to maintain the 1.25% expense limitation, to waive an equal amount (in annual percentage terms) of those same expenses for the Investor Class. The Total Annual Fund Operating Expenses After Fee Waiver and Expense Reimbursement for the Investor Class may vary from year to year and will in some years exceed 1.25%. If the operating expenses fall below the expense limitation in a year within three years after Matthews has made a waiver or reimbursement, the Fund may reimburse Matthews up to an amount that does not cause the expenses for that year to exceed the lesser of (i) the expense limitation applicable at the time of that fee waiver and/or expense reimbursement or (ii) the expense limitation in effect at the time of recoupment. This agreement will remain in place until April 30, 2018 and may be terminated at any time by the Board of Trustees on behalf of the Fund on 60 days' written notice to Matthews. Matthews may decline to renew this agreement by written notice to the Trust at least 30 days before its annual expiration date.

***All performance quoted is past performance and is no guarantee of future results. Investment return***

*and principal value will fluctuate with changing market conditions so that shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the return figures quoted. Returns would have been lower if certain of the Fund's fees and expenses had not been waived. Please see the Fund's most recent month-end performance.*

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*You should consider the investment objectives, risks, charges and expenses of the Matthews Asia Funds carefully before making an investment decision. This and other information about the Funds is contained in the [prospectus](#) or [summary prospectus](#), which may also be obtained by calling 800-789-ASIA (2742). Please read the [prospectus](#) carefully before you invest or send money as it explains the risks associated with investing in international and emerging markets. These include risks related to social and political instability, market illiquidity and currency volatility. Investing in foreign securities may involve certain additional risks, exchange rate fluctuations, less liquidity, greater volatility and less regulation. Fixed income investments are subject to additional risks, including, but not limited to, interest rate, credit and inflation risks. Single-country and sector funds may be subject to a higher degree of market risk than diversified funds because of a concentration in a specific sector or geographic region. Investing in small companies is more risky and more volatile than investing in large companies.*

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