



Matthews Asia Innovators Fund

Choose a Share Class: Investor ▼

Period ended September 30, 2019

For the quarter ending Sept. 30, 2019, the Matthews Asia Innovators Fund returned -3.88% (Investor Class), while its benchmark, the MSCI All Country Asia ex Japan Index returned -4.39%.

Market Environment:

Most Asian markets were down in the third quarter, following rallies earlier in the year. Political rhetoric about trade relations between the U.S. and China led to frequent and unpredictable shifts, creating short-term noise and volatility in the market.

Chinese equities were down in the quarter, succumbing to trade-related pressures and negative sentiment. U.S.-listed Chinese ADRs were particularly weak in the quarter, creating buying opportunities for shares of high-quality companies trading at lower valuations. Hong Kong protestors remained active in the quarter and tensions between the government and protesters increased following the reporting period. Notably, we believe that current valuations in China already reflect significant uncertainty, especially when compared with global peers.

Meanwhile, Indian equities fell in the quarter, along with Thailand and the Philippines. Much of India's underperformance occurred in late July as post-election euphoria gave way to profit-taking and deteriorating economic data. Late in the quarter, Indian policymakers surprised markets by announcing comprehensive corporate tax cuts and other stimulative measures.

Vietnam bucked the trend and generated positive equity-market returns in the quarter. Despite the current global environment of trade tensions and sluggish growth, Vietnam, which is highly exposed to global trade, surprised on the upside in the third quarter by growing at the fastest pace in over 1½ years.

Performance Contributors and Detractors:

The Fund held up slightly better than its benchmark during the quarter. Stock selection in China was the largest contributor to relative performance. Among individual stocks, Chinese biopharmaceutical company Jiangsu Hengrui Medicine was a strong performer, benefiting from an innovative drug pipeline. With one of the largest research and development teams based in China, Jiangsu Hengrui Medicine has the potential to be a dominant player in China's up-and-coming biopharma industry.

Elsewhere, the Fund's holdings in Vietnam were also positive contributors in the quarter, generating attractive, positive absolute returns. While the Fund's exposure to Vietnam is relatively small (less than 3%), our overweight versus the benchmark was a contributor to the Fund's relative performance.

Meanwhile, detractors from performance included many of the Fund's U.S.-listed Chinese ADRs, which suffered amid U.S.—China trade tensions. Among these holdings was Bilibili, a provider of short-form video content geared toward millennial audiences. Advertising spending in China has been weak amid slightly slower economic growth in China, and the stock also suffered from general negative sentiment toward Chinese companies among foreign investors. Our outlook for Bilibili remains bright, however, as the company is building a strong loyal, following among its target demographic of high-spending

millennials. Believing that the company may be well-positioned to capture a growing share of China's millennial wallet, we added to the position while valuations were attractive.

Notable Portfolio Changes:

During the quarter, we streamlined and concentrated our exposure among U.S.-listed Chinese ADRs, selling a handful of companies to focus on a smaller number of ADRs. We used the proceeds to add to our existing position in Bilibili, as well as to initiate a new position in tutoring-services provider TAL Education Group, a security which the Fund has previously owned and sold when valuations were higher. Market volatility created compelling buying opportunities for both securities.

Outlook:

While global macroeconomic conditions remain somewhat muted, we are optimistic about the prospects for innovative companies in Asia. Notably, equity valuations in Asia currently look much more attractive than the U.S., where valuations are at historic highs. Should growth in the U.S. start to slow, investors may start to take a closer look at Asia, which combines high economic growth potential with low equity valuations.

We remain positive in our outlook for Vietnam, which has a young workforce and where it is relatively easy for foreign companies and investors to do business. Countries such as Vietnam and India have picked up a bit of manufacturing work because of trade tensions. The migration of lower-end manufacturing away from China, however, was already underway before trade tensions began. The relocation of this work is an outcome of rising incomes in China, as well as favorable age demographics in Vietnam and India.

We continue to focus on secular growth trends in Asia. While U.S.—China trade tensions remain unresolved, we look for companies that can thrive regardless of the outcome of trade negotiations. We see rising incomes and the expansion of the middle class across Asia as the primary drivers of Asia's economic growth. Asia's culture of innovation, a shift toward services-based economies and upgrades in consumption patterns create compelling opportunities for long-term investors.

As of 09/30/2019, the securities mentioned comprised the Matthews Asia Innovators Fund in the following percentages: Jiangsu Hengrui Medicine Co., Ltd. 4.2%; Bilibili, Inc. 2.6%; TAL Education Group 3.3%. Current and future portfolio holdings are subject to change and risk.

Average Annual Total Returns - Investor Class (9/30/2019)

1-year 2.72%

3-year 8.52%

5-year 6.23%

10-year 9.61%

Inception (12/27/99) 3.52%

Gross Expense Ratio

1.19%

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](#).

Visit our [Glossary of Terms](#) page for definitions and additional information.

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