

Matthews Asia Innovators Fund

What is the objective of the Matthews Asia Innovators Fund?

The Matthews Asia Innovators Fund seeks long-term capital appreciation by investing in companies in Asia that we believe are innovators in their products, services, processes, business models, management, use of technology, or in their approach to creating, expanding or servicing their markets. We aim to invest in companies that are capable of showing sustainable growth based on their fundamental characteristics.

How do you define an innovative company?

There is no universal definition of an innovative company. At Matthews Asia, we view innovation in the way companies are developing new products and services in order to create new markets. We also see existing companies changing their business model in order to enhance their competitive position or implementing new technology and processes to improve productivity and profitability.

Why do you think innovative companies in Asia are attractive investments?

Asia as a region now has the four key essentials for innovation: a large addressable market size, entrepreneurs, human resources and a vibrant venture capital industry. With these in place, we have seen the growth of pioneering companies that can generate greater value today than in the past.

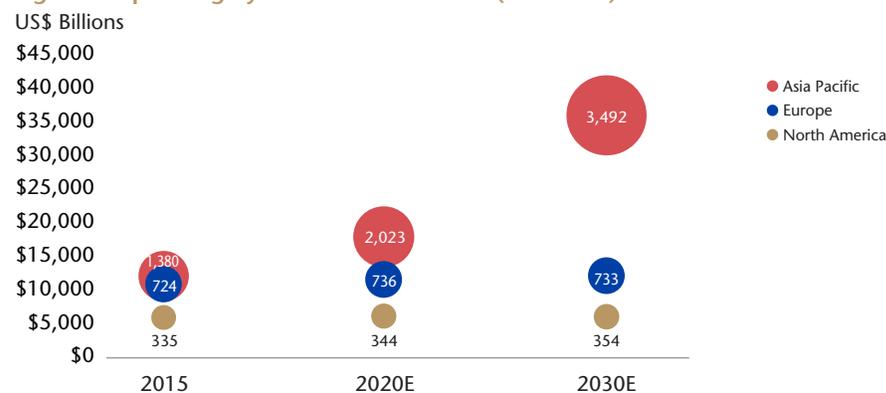
How prevailing is entrepreneurship in Asia?

Asia is synonymous with an entrepreneurial spirit and Asian entrepreneurs have contributed to the ability of the region's economies to transition from a low value-added model to a higher value-added economy. This has been achieved through innovation and an ability to more easily cater to local populations, designing and developing products and services that appeal to local markets. Over the past 10 years, we have watched as companies have become more sophisticated and often have a better understanding of localization and distribution than some multinational companies.

How significant is the buying power of Asian consumers?

Key innovators in Asia now target their own regional market—and Asia's middle class is quite homogeneous in many respects, meaning they may share similar cultural backgrounds, tastes and aspirations. South Korea's cosmetics companies, for example, have developed unique, innovative products that are well-suited to Asian consumers. But five or 10 years ago, these top-notch products did not generate much value because the markets for these products were relatively small. In recent years, South Korean cosmetics makers have found success in China, in part due to the emergence of the country's middle class and their rising disposable incomes, and they are able to sell their products in a much bigger market—sometimes even much larger than U.S. or European markets—and this has enabled them also to generate solid returns for shareholders.

Figure 1. Spending by Global Middle Class (2011 PPP)



PPP = Purchasing Power Parity

Note: Bubble Size = middle class population (millions); 2020 and 2030 data points are projections. There is no guarantee any estimates or projections will be realized.

Where do you mostly see innovative companies?

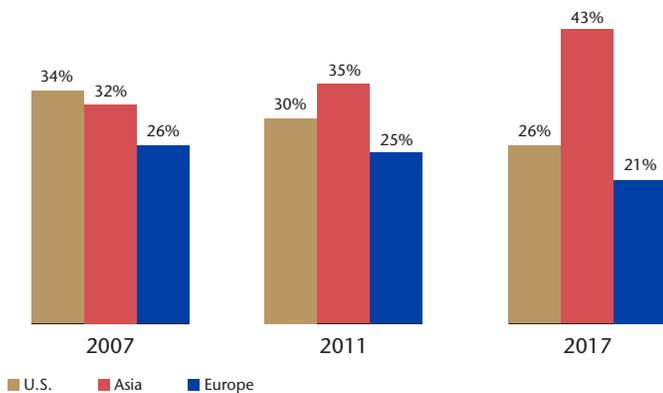
An important trend we are seeing is innovation moving from East to West. This is most evident in the internet services and consumer products space. For example, Amazon has started a one- to two-hour delivery service in key cities in the U.S., and is investing in developing its own logistics as a competitive advantage. This business strategy was started early on by leading Chinese entrepreneurs and companies. Initially, many investors had doubts over its potential for success, but the development of one's own logistics has become a global trend among many e-commerce companies.

Are there specific examples of the various types of innovation that is going on?

In another area of prominence, China is leading the world in financial technology and, along with Indonesia, has among the highest levels of mobile banking penetration. In fact, internet companies in China are penetrating deeper into the everyday lives of Chinese consumers in almost every respect. Internet companies have touched upon just about every major life purchase—from cars to homes to insurance products. Mobile internet penetration in China is among the highest in the world, and China is often leading the innovation by creating new markets and services in the mobile internet space.

Figure 2. Investment in Innovation Rising

Share of Global R&D Spending



Source: 2017 Global R&D Funding Forecast, Dec 2017; 2013 Global R&D Funding Forecast, Dec 2012; Businesswire

Note: Asia includes East, Southeast and South Asia; 2017 data points are projections. There is no guarantee any estimates or projections will be realized.

Why are human resources one of the key essentials for innovation?

Human resources, a key source of competitiveness for innovators in Asia, are something that tends not to be in short supply in Asia. Each year, a highly educated work force of millions hails from North Asian countries and India. Asian companies also are increasing spending on research and development. In fact, many policymakers in Asia have made innovation a national, strategic priority. The global share of research and development spending by Asian companies surpassed that of U.S. companies in 2011, and the gap continued to widen in 2016. The effort has given rise to numerous research hubs equipped with good infrastructure and skilled workers. In this way, Asian companies are increasingly laying firm foundations for future innovation.

How do you see your portfolio breakdown going forward?

Today, companies are evolving and embracing technology at a pace we have not witnessed in the past. There are new innovative companies that are creating new markets but we recognize that there are incumbent companies that are also innovating to adapt to today's fast changing environment. The criteria that once defined a traditional science or technology company may no longer apply today.

Therefore, the Fund aims to identify and invest in innovative companies across all sectors and industries without the traditional sector or industry limitations placed upon the Fund in the past. Our portfolio exposure and breakdown will continue to be the result of our bottom-up fundamental analysis. The Fund's exposure will depend on where we see innovation and growth opportunities in the region.

Is innovation happening in sectors beyond technology?

Yes, innovation is not only limited to technology industries. It can happen in any industry, old or new. Transportation is an old industry, for example, but a newcomer like the ride-sharing service Uber has completely changed the industry. Uber disrupted a century-old industry with new ways of providing transportation services by using new mobile technology. Within the tourism industry, companies like Airbnb are doing the same, enabling people to capitalize on underutilized assets by connecting the supply and demand of accommodation rentals via mobile technology. This is just the beginning for the ways in which technology is reshaping older industries.

What is your investment process?

The portfolio is constructed via a bottom-up, fundamental, stock picking approach. We assess companies with these general criteria in mind: attractive revenue growth rates, capital efficiency, sustainable profitability and healthy valuations. We focus on structural growth themes and look for companies that are disrupting or innovating in secular industries. We seek companies that stand to benefit from opportunities created by changes in consumer behavior and increasing disposable income in Asia. We prefer companies with sustainable competitive advantages and scalable business models.

What attributes do you look for when assessing a company for your portfolio?

Innovation can come in different shapes and forms—disruptive or incremental, in strategy or execution. We primarily seek companies that are implementing new ideas to build successful businesses in Asia. It can be innovative offerings that create or expand markets or unique strategies or business models that build entry barriers and a sustainable economic moat.

What are the principal risks inherent to the Fund, and how are they mitigated?

Our first objective is to avoid permanent loss of capital in the companies in which we invest. We believe that by investing in high-quality companies with strong and sustainable competitive advantages, along with capable and committed management teams, we lower the overall investment risk for the Fund. Given

the types of companies in which we invest, however, along with our benchmark agnostic approach, volatility may be higher at times than it is in other, more traditional Asian equity funds.

In addition, when we see opportunities, we attempt to invest in early-stage publicly listed companies. Higher risks may be involved at the initial investment stage. We try to avoid the excessive risks associated with early-stage investing by identifying companies with proven business models that have been tested in other markets. By focusing on the possible risk of permanent capital loss and emphasizing long-term development over short-term volatility, we believe we increase the odds of delivering solid, long-term performance for our shareholders.

How do you decide when to buy or sell?

Our position sizes are determined by several factors such as valuations and our conviction in corporate fundamentals. We will trim or exit a position based on valuations and considerations around fundamentals, in favor of better alternatives.

What is your outlook for Asia?

Over the next decade, we expect the region's economic growth drivers to continue to shift from labor and capital inputs to productivity gains driven by innovation. The explosive growth of China's emerging middle class brought sweeping economic changes to the global economy and these changes are continuing. Asia also has many emerging countries whose middle class has not yet entirely emerged.

Is this a sustainable long-term trend?

We believe that Asia innovators can create value for Asian consumers and long-term shareholders on the back of a vast market that has been created in the Asian marketplace. Companies that can create unique products and services that are well-suited to meet the demand created by rising disposable incomes and improving lifestyles should be well rewarded by the market. We believe this will continue to foster more innovation. This virtuous cycle will be a major trend in Asia and can be a sustainable value creator for long-term investors.

What experience does Matthews Asia have investing in Asia's innovative companies?

Matthews Asia has been investing in companies in the region for over 25 years and we understand what it takes for companies to be successful in this region. We have a deep and diverse team with a range of perspectives and expertise. Each of our professionals contributes a unique viewpoint. Our investments have been made across the market-cap spectrum, including many smaller "game changing" and innovative companies. We make more than 2,500 company visits a year and this approach is well-suited to identifying the most attractive innovative companies in the region.

What experience does the investment team have investing in innovative companies in Asia?

The investment team has significant experience investing in innovative companies in Asia. The Lead Manager, Michael J. Oh, CFA, has been a Portfolio Manager of the Matthews Asia Innovators Strategy since 2006. He has also been a Portfolio Manager of the Matthews Korea Fund since 2007. Co-Manager Sunil Asnani has been a Portfolio Manager of the Matthews India Fund since 2010 and the Matthews Asia Innovators Fund since 2018. Co-Manager Tiffany Hsiao, CFA, has been a Portfolio Manager of the Matthews China Small Companies Fund since 2015, of the Matthews Asia Small Companies Fund since 2018 and of the Matthews Asia Innovators Fund since 2018.

In common across all three senior Portfolio Managers is a deep level of experience investing in innovative companies, whether it is a product, service or process in a new or established market. We believe this team has the ability to identify high-quality businesses with strong management teams and that can add long-term value to the portfolio for shareholders.

Why is this strategy especially relevant now?

Innovators have long existed in every market in Asia, most notably in South Korea, Japan and Taiwan. The overall value created, however, has been constrained by their smaller market size since such homegrown inventions often have been unique to their domestic markets. Today, this has completely changed. The massive buying power of Asian consumers has far-reaching significance, especially for aspiring entrepreneurs who are focused on groundbreaking new products.

FUND FACTS

MATTHEWS ASIA INNOVATORS FUND

	Investor Class	Institutional Class
Ticker	MATFX	MITEX

Inception

Date	December 27, 1999	April 30, 2013
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Investment Objective

Long-term capital appreciation

Benchmark

MSCI All Country Asia ex Japan Index

Portfolio Managers



Michael J. Oh, CFA
Lead Manager

Michael Oh is a Portfolio Manager at Matthews Asia. He manages the firm's Asia Innovators and Korea Strategies. Michael joined Matthews Asia in 2000 as a Research Analyst and has built his investment career at the firm. Michael received a B.A. in Political Economy of Industrial Societies from the University of California, Berkeley. He is fluent in Korean.



Sunil Asnani
Co-Manager

Sunil Asnani is a Portfolio Manager at Matthews Asia. He manages the firm's India Strategy and co-manages the Asia Innovators Strategy. Prior to joining the firm in 2008 as a Research Analyst, he was a Senior Associate in the Corporate Finance and Strategy practice for McKinsey & Company in New York. In 2006, Sunil earned his M.B.A. from the Wharton School of the University of Pennsylvania. From 1999 to 2004, he served in various capacities, including as Superintendent of Police for the Indian Police Service in Trivandrum, India. Sunil received a Bachelor of Technology degree from the Indian Institute of Technology in Delhi, India. He is fluent in Sindhi, Hindi and Malayalam.



Tiffany Hsiao, CFA
Co-Manager

Tiffany Hsiao is a Portfolio Manager at Matthews Asia. She manages the firm's China Small Companies Strategy and co-manages the Asia Small Companies and Asia Innovators Strategies. Prior to joining the firm in 2014, she was a Vice President and Research Analyst at Goldman Sachs Investment Partners in Hong Kong and Tokyo from 2007 to 2013. She was responsible for researching Asia Pacific investments, with an emphasis on equities in China. Previously, she spent six years at Franklin Templeton Investments, where she managed the firm's global communications fund. Tiffany earned her Master of Science and Information Technology from Carnegie Mellon University and received a B.A. in Economics from the University of California, Berkeley. She is fluent in Mandarin and Taiwanese, and conversational in Cantonese.

Contact Matthews Asia

To learn more about Matthews Asia or how the Matthews Asia Funds can complement your globally diversified portfolio, please call 800.789.ASIA or visit matthewsasia.com.

Disclosures and Notes

The Fund holds no positions in securities issued by Uber Technologies Inc. or Amazon.com Inc. Current and future portfolio holdings are subject to change and risk.

You should carefully consider the investment objectives, risks, charges and expenses of the Matthews Asia Funds before making an investment decision. A prospectus or summary prospectus with this and other information about the Funds may be obtained by visiting matthewsasia.com. Please read the prospectus carefully before investing as it explains the risks associated with investing in international and emerging markets.

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. In addition, single-country and sector strategies may be subject to a higher degree of market risk than diversified strategies because of concentration in a specific industry, sector or geographic location. Investing in small companies is more risky and more volatile than investing in large companies. The Fund's value may be affected by changes in the science and technology-related industries.

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Matthews International Capital Management, LLC is the advisor to the Matthews Asia Funds.

The MSCI All Country Asia ex Japan Small Cap Index is a free float-adjusted market capitalization-weighted small cap index of the stock markets of China, Hong Kong, India, Indonesia, Malaysia, Philippines, Singapore, South Korea, Taiwan and Thailand. Indexes are unmanaged. It is not possible to invest directly in an index.

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