Matthews Asia™

Matthews Asia Total Return Bond Fund

Choose a Share Class: Institutional

The Fund's name changed from Matthews Asia Strategic Income Fund to the Matthews Asia Total Return Bond Fund on January 31, 2020. For more information, please read our Q&A: Fixed Income Retooling.

Period ended September 30, 2020

For the quarter ending September 30, 2020, the Matthews Asia Total Return Bond Fund returned 3.74% (Investor Class) and 3.79% (Institutional Class), while its benchmark, the 50% Markit iBoxx Asia Local Bond Index (ALBI) / 50% JP Morgan Asia Credit Index (JACI), returned 2.19%.

Market Environment:

Despite the once-in-a-century pandemic that gripped the world this year, markets have remained relentlessly optimistic in recent months even in the face of recessionary economic data and poor COVID-19 outcomes throughout much of the world. It was unusual for risk-on assets, like U.S. growth stocks, as well as safe-haven assets, like 10-year U.S. Treasuries, to achieve all-time highs in the same month of August. Within Asian credit, high yield outperformed investment grade as investors felt more comfortable taking more risk for more yield. Asian currencies, on average, were stronger versus the U.S. dollar. It was looking like the Roaring Twenties (2020s that is), even as a second wave of COVID cases hit the U.S. and later, Europe.

Perhaps optimism had outstripped the fundamental realities too far to begin the quarter. September was a risk-off month as markets focused more on the potential bad news—an uncertain result on U.S. Election Day, impasse over a second stimulus package, growing second-waves in Europe forcing more shut-downs and a more delayed timeline for a COVID vaccine. The best performers of August became the worst performers in September. The dollar rose, especially versus emerging market (EM) currencies, whose countries face growing COVID cases and lack the economic resilience and toolkit to combat them.

Within Asian credit, volatility continues to plague companies with the highest credit risks, especially ones with high leverage and upcoming refinancing needs. The markets need to see a clear path to refinancing for these companies before pricing them higher. On the other hand, investment grade and relatively higher quality high yield companies, such as Chinese property companies, have mostly recovered and many breached new highs in the third quarter.

Performance Contributors and Detractors:

The primary drivers of performance during the third quarter were the U.S. dollar-denominated (USD) high yield holdings in the portfolio. Within USD high yield, the three biggest contributors to returns were China issuers, including two China property developers: Dalian Wanda and China Franshion, as well as a China internet company, JD.com. These bonds rose largely based on the improving fundamentals in China.

The biggest detractors to performance this quarter came from the bonds of Indonesian garment manufacturer PB International, Philippines-based fast food chain Jollibee's, as well as Thai government bonds. PB International's bonds fell when Moody's downgraded the company based on its upcoming financing needs and increased working capital needs from an elongated working capital cycle. PB International pivoted part of its production from high tech garments to personal protection equipment. Jollibee's bond prices fell as revenues continue to remain tepid given the slow pace of reopening and consumer spend in its markets. The price of Thai government bonds fell as yields rose in the quarter. During the quarter currency was a slightly positive contributor to performance, with gains in Chinese renminbi overweight partially offset losses due to Indonesian rupiah and the Korean won underweight.

Notable Portfolio Changes:

In the third quarter, we exited our positions Chinese internet companies JD.com and Weibo, as these had recovered from the crisis and had reached our price targets. We deployed the funds to add Chinese property developer Times China and the convertible bonds of Poseidon Finance, a financing entity under China Shipbuilding Investment Corporation, a state-owned Chinese shipbuilder exchangeable into Postal Savings Bank of China. We initiated these positions based on their attractive relative value and their strong fundamentals.

On the local currency side, we added China Cinda's renminbi-denominated bonds to increase our exposure to China currency and rates. We also added local currency-denominated bonds of the Philippines and Malaysia on the expectation that their currencies and rates have room to outperform those of other riskier Asia markets.

Outlook:

We expect the fourth quarter to be an event-driven quarter. Driving volatility will be the U.S. election, debates over a new stimulus package, the relative success of countries response to the pandemic and potential breakthroughs in COVID-19 testing/vaccines/treatment. We recognize that the global economic recovery is still fragile and could

Average Annual Total Returns - Institutional Class (9/30/2020)

1-year 3.54%
3-year 3.41%
5-year 6.03%
10-year n.a.
Inception (11/30/11) 4.75%

Gross Expense Ratio

0.97%

After fee waiver and expense reimbursement: 0.90% [1]

[1] 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 incurred in connection with any merger or reorganization or extraordinary expenses such as litigation) of the Institutional Class to 0.90% first by waiving class specific expenses (e.g., shareholder service fees specific to a particular class) of the Institutional Class and then, to the extent necessary, by waiving non-class specific expenses (e.g., custody fees) 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 0.90% 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 0.90%. Any amount waived with respect to the Fund pursuant to this agreement is not subject to recoupment. This agreement will remain in place until April 30, 2021 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.*

Yield as of 9/30/2020

30-day Yield: 5.05%

30-day Yield Excluding Expense Waiver: 4.97%
The 30-Day Yield represents net investment income earned by the Fund over the 30-day period ended 9/30/20, expressed as an annual percentage rate based on the Fund's share price at the end of the 30-day period. The 30-Day Yield should be regarded as an estimate of the Fund's rate of investment income, and it may not equal the Fund's actual income

worsen if global COVID cases rise or fiscal stimulus lapses. We have already seen geo-political risks resurfacing, in particular between U.S. and China. Despite the Phase One trade agreement having been signed in January 2020, we believe the risk of rising U.S. — China political tensions remains.

On the other hand, we also see potential upside for the market and Asian credit specifically if any of the events listed above turns out positively. In the face of this uncertainty, our strategy will be barbelled, looking to add both high-quality, relatively low risk credit duration and companies that have been disproportionately hurt by the pandemic or recessionary fears, but with room to rally if risk sentiment turns positive. Looking at the medium to long term, we still believe that Asia USD high yield bonds offer the most attractive risk-adjusted returns and we will continue to allocate to this space when we find opportunities.

With the market continuing to reassess the pace of economic recovery, the U.S. 10-year interest rate is on net 3 basis points (0.03%) higher for the quarter. In Asia, we expect to see relatively muted movements in interest rates for most countries. After having reduced interest rates in most Asia countries, we believe some Asia central banks are taking a wait and see approach to additional interest rate cuts.

For currencies, the dispersion of performance going forward will be higher. While a general recovery in risk sentiment helps all Asian currencies, we are mindful of differences between countries, including both country specific macro fundamentals and where each country is relative to the virus cycle.

As of September 30, 2020, the securities mentioned comprised the Matthews Asia Total Return Bonds Fund in the following percentages: Wanda Properties International Co., Ltd., 7.250%, 01/29/2024, 4.9%; PB International BV, 7.625%, 01/26/202, 4.0%; Poseidon Finance 1, Ltd., Cnv., 0.000%, 02/01/2025, 3.1%; Franshion Brilliant, Ltd., 5.750%, 07/17/2067, 3.0%; Times China Holdings, Ltd., 6.200%, 03/22/2026, 2.6%; Poseidon Finance 1, Ltd., Cnv., 0.000%, 02/01/2025, 3.1%; Thailand Government Bond, 1.600%, 12/17/2029, 2.2%; China Cinda Asset Management Co., Ltd., 5.500%, 03/14/2028, 1.5%; Jollibee Worldwide Pte, Ltd., 3.900%, 07/23/2068, 1.4%. The Fund held no positions in JD.com, Inc.; Weibo Corp. Current and future portfolio holdings are subject to change and risk.

distribution rate. Source: BNY Mellon Investment Servicing (US) Inc.

Fixed income investments are subject to risks, including, but not limited to, interest rate, credit and inflation risks. Investing in emerging markets involves different and greater risks, as these countries are substantially smaller, less liquid and more volatile than securities markets in more developed markets.

Visit our Glossary of Terms page for definitions and additional information.

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