



# Matthews Korea Fund

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## Period ended September 30, 2020

For the quarter ending September 30, 2020, the Matthews Korea Fund returned 13.33% (Investor Class) and 13.48% (Institutional Class), while its benchmark, the Korea Composite Stock Price Index, returned 13.43% over the same period.

### Market Environment:

South Korean equities bounced and slightly outperformed global emerging markets in the third quarter. Korea's response to COVID-19 was prompt and effective resulting in a relatively efficient command over the spread of cases. However by mid quarter, a second wave of COVID-19 caused the government to re-impose social distancing restrictions which should result in year-on-year economic growth to be revised downward. Korea has a couple of potential tailwinds going into the fourth quarter. The country's external vulnerability and financing risks are low with room to ease monetary aggregates. Korea has fiscal firepower to stimulate and has begun to utilize its resources. Its valuations are some of the region's most attractive and the prospect of earnings growth from a very low base is a good possibility, especially if its influential neighbor, China, continues to recover.

### Performance Contributors and Detractors:

Contributors to performance during the quarter include Hyundai Motor and Kakao Corp. Hyundai Motor continues to gain market share globally with successful new model launches. In the U.S., the combined Hyundai Motor and Kia Motors market share reached historical peak during June and August, gaining shares from Japanese peers. In the EU, Hyundai gained shares through solid model pipelines in neighborhood electric vehicles (NEVs), which are smaller vehicles designed for slower speeds and shorter distances. In emerging countries like India, Hyundai's sales have also recovered faster than the market. Kakao, the Korea's largest messaging platform, continues to enhance its earnings visibility driven by a combination of its e-commerce functionality, payment platform and content services, while increasing its number of users and improving its ability to monetize services.

Detractors from performance include Koh Young Tech and BGF Retail. Koh Young technology makes robots that can conduct optical inspections for manufacturers. The company had a difficult year from an uncertain outlook that led to conservative capital investment spending among their customers, especially in the automotive industry. We expect it to further diversify its customer and product base and show better recovery next year. BGF Retail operates a chain of convenience stores. We decided to exit the position in the quarter and reallocate the capital toward other opportunities.

From a sector perspective, stock selection in health care and an underweight in industrials contributed to relative performance. While we are underweight on health care, our stock selection in companies such as Yuhan and Hugel showed positive impacts. Hugel, a health care company that focuses on beauty and cosmetics related products, is making constructive progress with the China Food and Drug Administration (CFDA) approvals for new products, while continuing to gain market share in Korea. On the other hand, stock selection in consumer staples and information technology sectors detracted from relative performance. In consumer staples, our largest positions are in confectionary company Orion and LG Household & Health Care. Both companies have strong product suites and meaningful marketing and distribution capabilities, both domestically in Korea and regionally across Asia. While their share prices were weak in the quarter, we remain constructive on these companies on a long-term view.

### Notable Portfolio Changes:

During the quarter, we initiated a new position in KINX and Nongshim. As Korea's only carrier-neutral, retail-oriented data center business, KINX is a key beneficiary of growing data traffic in Korea. Nongshim is Korea's largest noodle manufacturer and second largest confectionary player, gaining market share in the global market especially in China and the U.S. with its premium product lines. We also reduced a number of holdings during the quarter to rotate and concentrate capital among higher conviction portfolio holdings. Positions we closed included AfreecaTV, Lock & Lock, and Lotte Reit.

### Outlook:

We expect global consumption to gradually recover from the pandemic, with North Asia countries such as China and Korea continuing to recover faster than other parts of the world.

As before, we believe active security selection is essential to capturing Korea's long-term growth potential. As bottom-up investors, we look for companies that can grow organically without the assistance of strong macroeconomic tailwinds. We continue to look for companies that can benefit from domestic consumption within Korea, as well as those companies headquartered in Korea that are effectively competing and innovating in global markets.

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

1-year 20.25%  
3-year -0.21%  
5-year 4.39%  
10-year n.a.  
Inception (10/29/10) 6.66%

## Gross Expense Ratio

1.05%

**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](#).

KOSPI performance data may be readjusted periodically by the Korea Exchange due to certain factors, including the declaration of dividends.

Over the long term, we believe the structural growth trends we are currently following remain intact. Asia's growing middle classes are spending money on education, leisure and entertainment as incomes rise. Looking ahead, we continue to focus on the growth potential of Korea's most innovative companies.

As of 9/30/2020, the securities mentioned comprised the Matthews Korea Fund in the following percentages: Hyundai Motor Co., Ltd., Pfd. 6.3%; Kakao Corp., 4.9%; Koh Young Technology, Inc., 2.2%; Yuhan Corp., 2.2%; Hugel, Inc., 3.4%; Orion Corp., 4.2%; LG Household & Health Care, Ltd., Pfd., 5.2%; KINX inc., 1.2%; Nongshim Co., Ltd., 1.8% . The Fund held no positions in BGF Retail, AfreecaTV Co., Lock & Lock Co., and Lotte Reit Co. Current and future portfolio holdings are subject to change and risk.

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

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