

**SHINING A LIGHT ON THE.....
Matthews China Small Companies Fund**

AT A GLANCE

Investment Objective	
Long-term capital appreciation. Under normal market conditions, the Matthews China Small Companies Fund seeks to achieve its investment objective by investing at least 80% of its total net assets, which include borrowings for investment purposes, in the common and preferred stocks of Small Companies (defined below) located in China and Taiwan.	

Inception Date	29 February 2012
Fund Factsheet Link	https://www.morningstar.co.uk/uk/funds/snapshot/snapshot.aspx?id=F00000NYUG

Management	
Manager Name	Start Date
Tiffany Hsiao	1 July 2015

Investment Style Details	
Equity Style	
Market Capitalisation	% of Equity
Giant	0.00%
Large	18.39%
Medium	69.97%
Small	9.21%
Micro	2.43%

Top 10 Holdings		
Total number of holdings	46	
Assets in Top 10 Holdings	39.36%	
Name	Sector	% of Assets
Silergy Corp	Technology	8.48%
Sunny Friend Environmental Technology Co	Industrials	5.04%
SITC International Holdings Co Ltd	Industrials	4.67%
Asia Cement (China) Holdings Corp	Basic Materials	3.61%
Yihai International Holdings Ltd	Consumer Defensive	3.45%
Joy City Property Ltd	Real Estate	3.32%
Sunevision Holdings Ltd	Technology	2.82%
Greentown Service Group Co Ltd	Real Estate	2.80%
Jonjee Hi-Tech Industrial and Commerc...	Real Estate	2.61%
China Youzan Ltd	Technology	2.56%

Volatility Measurements	
3-Yr Std Dev (volatility)	17.96%
3-Yr Mean Return (average)	15.50%

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FUND PERFORMANCE

Performance from 1 January 2013 to 30 September 2019:

	2013	2014	2015	2016	2017	2018	2019
Matthews China Small Companies Fund	31.92%	2.82%	8.95%	16.95%	42.92%	-13.74%	23.23%
iShares MSCI EM ETF	-5.82%	2.62%	-11.15%	33.56%	24.43%	-9.25%	7.80%

Performance over 12 months, 3 years, 5 years and since launch.

	1 year	3 years	5 years	Since launch
Matthews China Small Companies Fund	12.21%	47.04%	98.06%	145.91%
iShares MSCI EM ETF	2.91%	22.40%	43.48%	37.16%

You should note that past performance is not a reliable indicator of future returns and the value of your investments can fall as well as rise. The total return reflects performance without sales charges or the effects of taxation, but is adjusted to reflect all on-going fund expenses and assumes reinvestment of dividends and capital gains. If adjusted for sales charges and the effects of taxation, the performance quoted would be reduced.

UPDATE....

The key to this fund is to believe in the China Growth story. If you don't believe in it then this fund is not for you! Standard asset allocation would assume you hold money in the UK, Japan, US and then Europe and Asia/Emerging Markets. However, China is excluded other than through an emerging market or Asia Fund. And yet this is one of the largest global economies. The challenge with having a China Fund is that there is a high probability that there will be a cross over in some holdings with other funds.

This fund takes a different approach and therefore there is unlikely to be that crossover. This fund is looking for that next Tencent in areas where people don't look. There are many opportunities, but this is a concentrated portfolio of 40 to 50 names. The manager will only take risk where it is worth taking and avoids that which she cannot control. Tiffany's background is important to the fund. Her father developed the first laptop computer and is behind Compal Electronics a Taiwanese electronics manufacturer. They moved to the US when she was six and her father set up his own angel fund to help entrepreneurs with a passion to change the world.

That same approach in the US is happening all over China with the same drive, innovation and passion. These are companies that are being set up by Chinese entrepreneurs who have spent decades working for Western Companies, developing products, and now have returned to do the same in China. These are often industry veterans who have built great businesses in the West.

The fund is split between steady compounders which makes up about two thirds of the fund, and the balance equity kickers. The steady compounders are well known names within China but tend to be new to the foreign and domestic investor. The valuations of these are compounded by growth of 15% plus per annum. The kickers are small because they have not been discovered yet. These tend to be in high end tech or biotech and are likely to be the world's next Tencent.

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We talked about the relationship between China and the US. Tiffany explained this is important to understand because when looking at companies she needs to understand that these can work even when that relationship has totally broken down. China is building businesses so that they can be self-sufficient in certain areas.

A good example would be semiconductors; the majority are imported from the US. The largest holding is Silergy which is one of the largest semiconductor manufacturers in China, and yet is a few billion in market cap. The long-term trust with the US has gone, and the more Trump tweets the more Chinese firms want Chinese semiconductors.

Sunny Friend is a Taiwanese Company which cleans waste from semi-conductor plants. One of its main clients is TSMC but it is now working with all the semi-conductor manufacturers in China.

The main point is that there will be a decoupling from the US but domestically there are great businesses in China what will prosper. Her role is to find them. The main pillars to this are discovering good businesses, with good management and appropriate valuations. In terms of downside capture this fund sits at about 80% and this is down to finding those businesses with barriers to entry and self-financing with low leverage. Good management is key in terms of track record and alignment to shareholders.

They hold 40 to 60 names with position sizes between 1 and 10%. In terms of selling they will trim for profit taking, risk management and growth moderating. In terms of exiting it will be where valuations are ahead of fundamentals, the investment theses fail to materialize and / or a yellow/red flag appears in corporate governance.

In summary, this is a well-managed fund with the manager aware of the potential risks associated with smaller companies. The reality is that many of the businesses are well established but unknown to outside investors. This provides investors who want to invest in China with a more domestically focused fund which will benefit from the decoupling from the US. There are risks with China which perhaps are not the same as other economies and although the manager aims to minimise these, investors should be aware of them. In terms of blending it is unlikely that many (if any) of these holdings would appear in other funds and therefore this could work well, but investors must be aware of the potential risks and perhaps consider other China Funds before making any decisions.

The source of information in this note has been provided by Matthews and is correct as at October 2019. These are notes from meeting the fund manager or representative and should not be seen as a recommendation to purchase any fund mentioned. Any reference to shares is not a recommendation to buy or sell. Should you wish to make a decision based on these notes we cannot take responsibility for this and you should carry out your own research before making a decision. We would also recommend that you receive advice before following up on any decision.