# Q&A from Matthews Asia Funds

April 2016

# Matthews Asia Credit Opportunities Fund

### What is the aim of the Matthews Asia Credit Opportunities Fund?

The Matthews Asia Credit Opportunities Fund seeks total return over the long term. It aims to provide investors with a compelling fixed income investment solution that offers yield enhancement and diversification. Asia high yield credit has historically generated attractive returns compared to assets of similar risk: about 10% annualized returns with 10% annualized volatility. By identifying compelling opportunities in the growing Asia credit universe, we hope to generate an attractive risk-adjusted return profile over the long run.

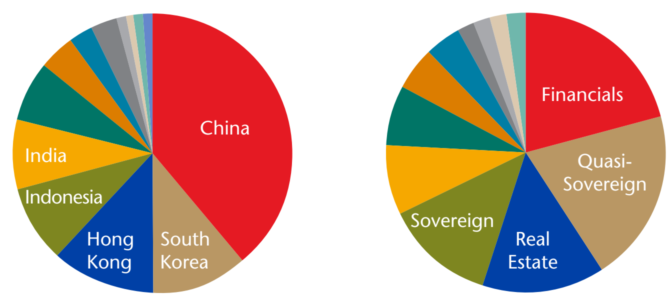
### Why did Matthews Asia launch this Fund?

We recognize that investors need income options in a persistent low-yield environment and access to asset classes that diversify their fixed income exposure. Asia has a large and liquid corporate bond market and, as a relatively under-researched asset class, it provides opportunities to potentially benefit not only from attractive levels of yield, but also capital appreciation. We intend to leverage Matthews Asia's 24 years of experience in Asia equity and fixed income security selection to effectively manage this Fund.

### How big is the Asia credit investment universe?

Asia's U.S. dollar-denominated bond market is represented by the J.P. Morgan Asia Credit Index (JACI) and is about US$623.8 billion in size as of August 31, 2015. Of this amount approximately two-thirds is issued by corporates and one-third by sovereign or quasi-sovereign entities. The sub-investment grade segment of the universe is US$129.3 billion, up from US$18.6 billion since the JACI was first established in December 1998.

**J.P. MORGAN ASIA CREDIT INDEX (JACI)**



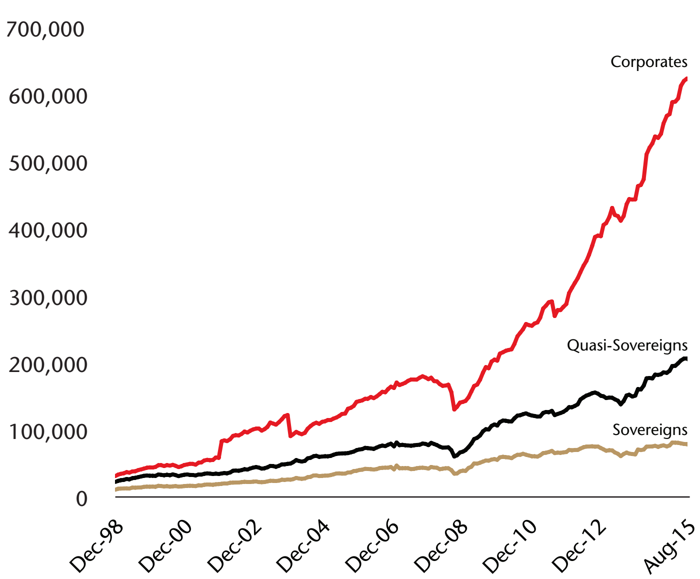

**Total Market Value: US$623.8 billion**
Sovereign: 33%
Corporate: 67%

| | |
|---|---|
| China | 39% |
| South Korea | 12% |
| Hong Kong | 11% |
| Indonesia | 9% |
| India | 8% |
| Philippines | 7% |
| Singapore | 4% |
| Malaysia | 3% |
| Thailand | 3% |
| Sri Lanka | 1% |
| Taiwan | 1% |
| Macau | 1% |
| Pakistan | 1% |

| | |
|---|---|
| Financials | 21% |
| Quasi-Sovereign | 20% |
| Real Estate | 14% |
| Sovereign | 13% |
| Oil & Gas | 8% |
| TMT | 7% |
| Utilities | 5% |
| Diversified | 4% |
| Industrials | 2% |
| Metals & Mining | 2% |
| Consumer | 2% |
| Infrastructure | 2% |

Source: JP Morgan, as of August 31, 2015

**OUTSTANDING MARKET CAPITALIZATION OF THE J.P. MORGAN ASIA CREDIT INDEX (JACI), 1999–AUG 2015, IN USD MILLIONS**




Source: JP Morgan, as of August 2015

### How do the returns for Asia credit compare to similar asset classes as well as other equity and fixed income asset classes?

Most bonds in the portfolio will be sub-investment grade, or so-called 'high yield' bonds. Such investments should be considered speculative and may include distressed and defaulted securities. However, high yield bonds tend to provide high income in an effort to compensate investors for their higher risk of default.

Over the long term, Asia high yield bonds have generated higher returns than European, LATAM and U.S. high yield bonds, with a lower level of risk. For example, as the table below illustrates, Asia high yield has outperformed Europe by 3.0% per annum, with a lower volatility during the past 15 years. Over the same period, Asia high yield has also outperformed LATAM high yield, returning 1.9% more per year with 3.0% less volatility. Finally, compared to U.S. high yield, Asia high yield has returned 3.5% more per year with the same level of risk.

Over the past 15 years, Asia high yield has a cumulative return double that of European, LATAM and U.S. high yield, with less risk than Europe and LATAM.

**RETURN STATISTICS: 1999 (OR INCEPTION) TO PRESENT[1]**

| | Asia HY | Euro HY | LATAM HY* | U.S. HY |
|---|---|---|---|---|
| Period Return | 402.7% | 219.1% | 196.7% | 194.9% |
| Annual Return | 10.2% | 7.2% | 8.3% | 6.7% |
| Annual Volatility | 9.6% | 11.9% | 12.6% | 9.5% |
| Sharpe | 1.06 | 0.61 | 0.66 | 0.71 |

Source: Bloomberg, as of 1999 to August 2015; *2002 to August 2015; Returns calculated in USD except Euro HY, which is calculated in euro.; [1]Data shown from 1999 (or since inception) for Asia High Yield (high yield portion of J.P. Morgan Asia Credit Index), U.S. High Yield (BofA Merrill Lynch High Yield Master II Index), Euro High Yield (Barclays Pan-European High Yield Index) and LATAM High Yield (J.P. Morgan CEMBI Broad Latin American High Yield Index). **Past performance is no guarantee of future results.** It is not possible to invest directly in an index. Volatility is the standard deviation of returns. The Sharpe ratio is a risk-adjusted measure calculated by using standard deviation and excess return to determine reward per unit of risk.

Asia credit compares favorably to other asset classes, historically offering one of the highest returns for its risk level versus other available asset classes. In terms of the absolute returns for the high yield segment of the dollar-denominated JACI—the part of the index most representative of the Fund's portfolio—it has generated an annualized return of 10.2% over the past 15 years.

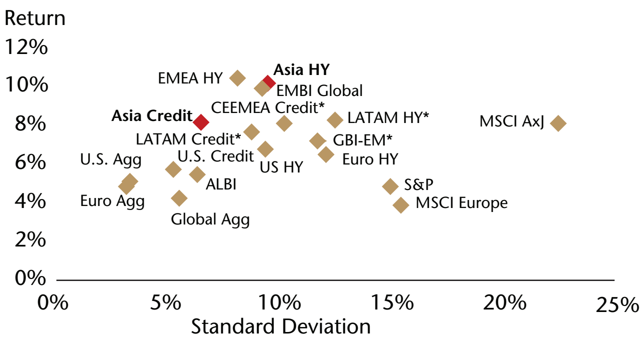
## Does Asia credit provide diversification benefits?

In addition to aiming to provide attractive total returns, Asia's high yield corporate bond market has a low to medium correlation with a variety of asset classes, providing diversification benefits versus the U.S., European, Asian and global asset classes. For investors seeking a higher yield, this also provides yield diversification, with exposure to an asset class that lives outside of the more traditional fixed income universe investors are more familiar with.

## What are the economic fundamentals underlying Asia credit?

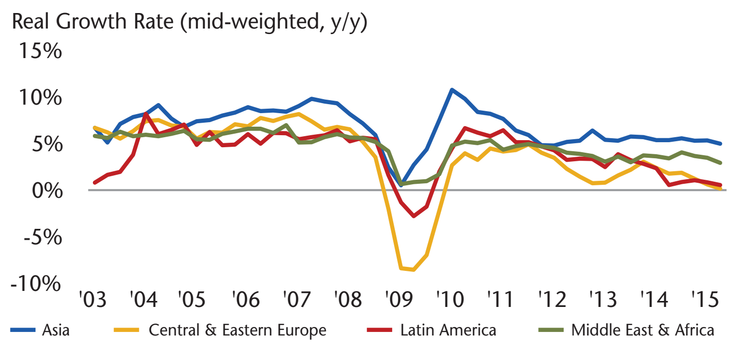
Asia's contribution to global growth continues to grow and the region generally has high levels of foreign currency reserves, high personal savings rates, and low levels of inflation, particularly when compared to Latin America, Russia, and Central and Eastern Europe. Currency regimes have become more flexible over the past 15 years which generally facilitates more flexible monetary policy by countries in the region. Asian currencies can be volatile, which is one reason why the Matthews Asia Credit Opportunities Fund focuses primarily on U.S. dollar-denominated investments.

**ANNUAL RISK AND RETURN**




Source: Bloomberg, as of 1999 (or inception)–August 2015; *2002 to August 2015.
All performance quoted represents past performance and does not guarantee future results. It is not possible to invest directly in an index. All performance is calculated in USD except Euro Agg, Euro HY and EMEA HY, which are calculated in euro.

**REAL GDP GROWTH BY REGION**




Source: Emerging Advisors Group, as of June 1, 2015

**CORRELATION MATRIX OF MONTHLY RETURNS—1999 TO AUGUST 2015**

| | Barclays US Agg | Barclays Euro Agg | Barclays Global Agg | S&P 500 | MSCI AxJ | MSCI Europe | JPM EMBI Global | JPM GBI-EM | Asia Credit | CEEMEA Credit | LATAM Credit | Euro HY | U.S. HY | Asia HY | LATAM HY | EMEA HY |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Barclays U.S. Agg | 1.00 | | | | | | | | | | | | | | | |
| Barclays Euro Agg | 0.69 | 1.00 | | | | | | | | | | | | | | |
| Barclays Global Agg | 0.71 | 0.48 | 1.00 | | | | | | | | | | | | | |
| S&P 500 | -0.08 | -0.13 | 0.15 | 1.00 | | | | | | | | | | | | |
| MSCI AxJ | 0.02 | -0.04 | 0.24 | 0.73 | 1.00 | | | | | | | | | | | |
| MSCI Europe | -0.15 | -0.12 | -0.08 | 0.84 | 0.69 | 1.00 | | | | | | | | | | |
| JPM EMBI Global | 0.48 | 0.25 | 0.47 | 0.51 | 0.59 | 0.47 | 1.00 | | | | | | | | | |
| JPM GBI-EM* | 0.34 | 0.16 | 0.65 | 0.56 | 0.69 | 0.42 | 0.71 | 1.00 | | | | | | | | |
| Asia Credit | 0.64 | 0.41 | 0.55 | 0.37 | 0.51 | 0.29 | 0.78 | 0.65 | 1.00 | | | | | | | |
| CEEMEA Credit* | 0.44 | 0.22 | 0.45 | 0.47 | 0.55 | 0.40 | 0.79 | 0.59 | 0.85 | 1.00 | | | | | | |
| LATAM Credit* | 0.48 | 0.25 | 0.50 | 0.55 | 0.59 | 0.48 | 0.90 | 0.67 | 0.84 | 0.80 | 1.00 | | | | | |
| Euro HY | 0.03 | 0.07 | 0.14 | 0.58 | 0.62 | 0.62 | 0.53 | 0.47 | 0.49 | 0.62 | 0.62 | 1.00 | | | | |
| U.S. HY | 0.19 | 0.05 | 0.29 | 0.64 | 0.66 | 0.59 | 0.65 | 0.60 | 0.62 | 0.71 | 0.76 | 0.86 | 1.00 | | | |
| Asia HY | 0.39 | 0.21 | 0.41 | 0.51 | 0.66 | 0.43 | 0.77 | 0.70 | 0.90 | 0.81 | 0.82 | 0.58 | 0.70 | 1.00 | | |
| LATAM HY* | 0.30 | 0.11 | 0.40 | 0.63 | 0.62 | 0.57 | 0.84 | 0.65 | 0.73 | 0.76 | 0.94 | 0.69 | 0.82 | 0.76 | 1.00 | |
| EMEA HY | 0.25 | 0.24 | 0.28 | 0.48 | 0.51 | 0.45 | 0.72 | 0.57 | 0.65 | 0.72 | 0.77 | 0.57 | 0.62 | 0.66 | 0.76 | 1.00 |

Global; Emerging Markets; Credit; High Yield; Correlations shown from 1999 based on monthly-returns in USD except Euro Agg, Euro HY and EMEA HY, which are calculated in Euro.

Source: Bloomberg; data period 1999 to August 2015; *2002 to August 2015.

Barclays U.S. Aggregate Bond Index, Barclays Euro Aggregate Bond Index, Barclays Global Aggregate Bond Index, S&P 500 Index, MSCI All Country Asia ex Japan Index, MSCI Europe Index, J.P. Morgan Emerging Markets Bond Index Global, J.P. Morgan Government Bond Index-Emerging Markets (JPM GBI-EM), Asia Credit (J.P. Morgan Asia Credit Index–JACI), CEEMA Credit (J.P. Morgan Corporate Broad EMBI CEEMA Index), LATAM Credit (J.P. Morgan Corporate Broad EMBI Latin America Index), Euro High Yield (Barclays Pan- European High Yield Index), U.S. High Yield (BofA Merrill Lynch High Yield Master II Index), Asia High Yield (high yield portion of J.P. Morgan Asia Credit Index), LATAM High Yield (J.P. Morgan CEMBI Broad Latin American High Yield Index), and EMEA High Yield (BofA Merrill Lynch Euro Europe, Middle East and Africa Emerging Markets Sovereign & Credit Index). **Past performance is no guarantee of future results.** It is not possible to invest directly in an index. Correlation, in the world of finance, is a statistical measure of how two securities move in relation to each other.

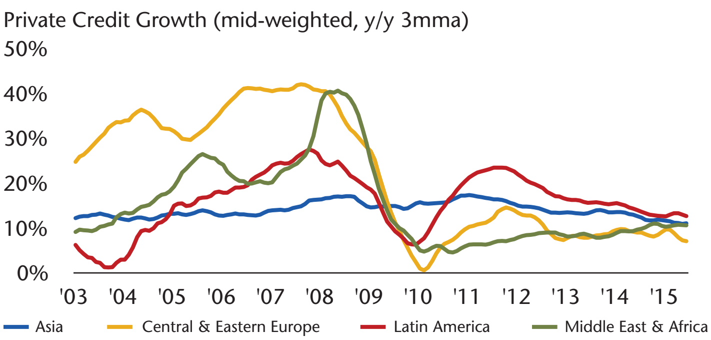
## How does currency volatility and inflation in Asia compare to other emerging markets?

The region also benefits from relatively stronger fundamentals at the government level, with generally lower levels of debt and higher foreign currency reserves. This has historically contributed to greater currency stability when compared to Latin America, Russia and Central and Eastern Europe. A combination of responsible fiscal and monetary policy has also contributed to the region benefiting from relatively lower levels of inflation and a break away from periods of hyper-inflation still seen in some emerging markets today.

## How do credit fundamentals compare to the rest of the emerging markets?

Credit fundamentals are generally supportive, with levels of leverage and issuer liquidity profiles that are relatively in line with those found in Europe and the U.S. Overall, credit growth has remained steady as markets have gradually and sustainably grown in recent years. In addition, while default rates have started to tick-up in 2015, this has been limited to poorer quality corporates with excessive leverage or particular sectors suffering from lower commodity prices.

**CREDIT GROWTH BY REGION**




Source: Emerging Advisors Group, as of June 1, 2015

## How do Asia high yield spreads move relative to high yield in the U.S. and Europe?

Asia high yield spreads are usually tighter than in the U.S. and Europe, signifying potentially lower credit risk and higher corporate quality. In the 2008 crisis, Asia credit showed less downside (i.e. spreads widened less, 922 basis points) than the U.S. (1,786 basis points) and European (1,949 basis points) credit. Historically, Asia credit spreads have half the standard deviation of U.S. and European credit spreads.

## How will the Fund be impacted by interest rate risk?

Since credit risk drives a higher proportion of risk and return in high yield than interest rate risk, the Fund will typically have relatively low sensitivity to interest rates compared to a portfolio benchmarked to global bonds, such as the Barclays Global Aggregate Bond Index. Historical analysis shows that Asia credit has had a relatively low sensitivity to U.S. interest rates, as measured by the asset class' beta to U.S. Treasury Bonds.

However, since interest rates have largely been falling over the last 30 years, this historical experience is not necessarily indicative of future performance. While Asia credit still offers diversification benefits, there could be a higher sensitivity to movements in U.S. interest rates going forward.

## How does currency volatility in Asia affect the corporate bond market and the Matthews Asia Credit Opportunities Fund?

The Matthews Asia Credit Opportunities Fund is expected to invest at least 80% of the portfolio in USD-denominated assets and, therefore, should not be materially impacted by movements in local currency. The remainder of the portfolio is selectively allocated to Asian currencies that, we believe, have long-term appreciation potential. The potential also exists to hedge currency exposure if necessary.

More broadly, currency does affect credit when the home currency depreciates versus the USD, since the debt service burden would increase commensurate with the amount of depreciation. Currency risk may also be embedded within each company's business, especially if there is a mismatch in currency exposures between a company's liabilities and assets or revenues. Potential mismatches between assets and liabilities, or between revenues and expenses, is a characteristic that we examine as part of our fundamental credit analysis on each issuer.

**ASIA BONDS HAVE AMONG THE LOWEST BETA TO U.S. TREASURIES**
January 1, 1999–August 2015

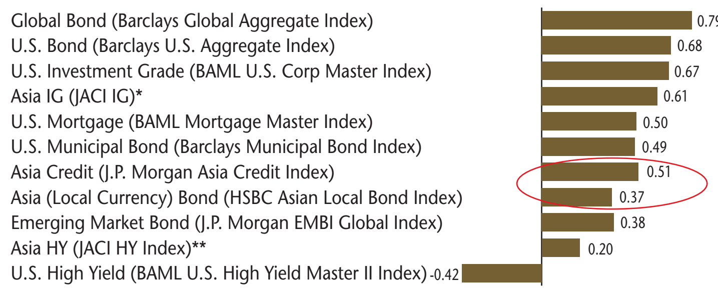



Chart shows beta of each asset class to the BAML U.S. Treasury Current 5 Year Index, based on monthly returns. *Investment grade portion of J.P. Morgan Asia Credit Index
**High yield portion of J.P. Morgan Asia Credit Index. Beta is a measure of the volatility, or systematic risk, of a security or a portfolio in comparison to the market as a whole.
Source: Bloomberg

## What types of instruments will the Fund invest in?

The Matthews Asia Credit Opportunities Fund will invest primarily in USD-denominated high yield Asia bonds. It can also invest in other eligible instruments such as convertibles, local currency bonds, asset backed securities, warrants and equities. At times, the Fund may also add or hedge exposure via derivative instruments such as futures, credit default swaps and interest rate swaps, although the use of such instruments is expected to be limited. As the local currency bond market increases in depth and breadth to include more corporate issuers, the Fund may invest in local currency bonds. However, the Fund is expected to remain predominantly invested in USD-denominated bonds so that credit rather than currency is the primary return and risk driver of the Fund.

## How much of the portfolio is expected to be unrated and what does that mean?

About one third of the portfolio is expected to be unrated and this reflects the overall increase in unrated issuers within Asia's bond market. In fact, many companies in Asia do not get a rating from one of the Big 3 rating agencies for a number of reasons. Asia investors do not require ratings from issuers like U.S. or European investors do, and as the investor base in Asia moves closer to home, there is less demand for issues to be rated. This has been exacerbated by a fall in the proportion of 144a deals in the market. Also, in many countries, local rating agencies are the standard if the bonds are held primarily by local investors.

### How sensitive is the Fund to credit risk and interest risk?

Interest rate duration is actively managed by the portfolio managers. As noted above, the Fund will likely be more sensitive to spread duration—that is how much the price of a bond moves when the credit spread of that bond changes. High yield bonds have a higher credit spread than investment grade bonds and, therefore, are more sensitive to changes in credit spread. The Fund is expected to invest in companies with the potential for credit spread compression, either because they are expected to benefit from a ratings upgrade or because, in the view of the portfolio managers, the bonds have been oversold but the company has assets with high intrinsic value.

Derivatives may be used judiciously to strategically isolate a return/risk exposure. Potential synthetic and derivative instruments include futures, credit default swaps and interest rate swaps. For example, U.S. interest rate futures may be used to hedge U.S. interest rate risk when the portfolio managers believe that the market is not sufficiently pricing in the risk of interest rate rises.

### How will the Fund manage drawdown risk—both at the security level and at the portfolio level?

Drawdown, which is the peak-to-through decline during a specific record period of an investment, fund or commodity, can be significant in high yield bond markets, including the Asia credit markets. During the Global Financial Crisis (GFC), the drawdown was 25% and it has been as high as 10% since that time. However, the market has also tended to bounce back quickly—in as little as four months in a normal bout of spread widening and seven months during the GFC. We believe that it is important to stay committed to the asset class and have the conviction to stay the course through market cycles. Through our fundamental, bottom-up analysis, the Fund will seek to have a tilt towards higher quality sub-investment grade corporates, rather than more stressed corporates. This will help potentially mitigate drawdown risk. At the security level, sell discipline is also important when specific issuers are experiencing deteriorating fundamentals.

### What is Matthews Asia's experience managing Asia credit?

Matthews Asia has been active in Asian financial markets for almost 25 years. The firm launched a dedicated Asia fixed income strategy—the Asia Strategic Income Strategy—in 2011 in order to provide investors with access to a fast-growing segment of the fixed income market. The Asia Strategic Income Strategy seeks to generate an attractive return through exposure to interest rate, currency and credit markets across Asia. This Asia Credit Opportunities Strategy expands on the credit component in order to provide a dedicated credit portfolio. The fixed income team consists of four dedicated investment professionals and benefits from leveraging the expertise of the broader Matthews Asia equity team, based in San Francisco. Dedicated fixed income operational and risk management colleagues also contribute to execution of portfolio strategy and monitoring of portfolio risk exposures.

### If I already have an allocation to emerging market debt, why do I need a dedicated allocation to Asia corporate bonds?

Typical emerging market debt portfolios have small allocations to Asia credit. Asia corporate bonds provide investors with the potential to enhance and diversify portfolio yield in a region with stronger economic fundamentals than many parts of broader emerging markets. The Fund also provides access to a broad pool of issuers that have the potential to benefit from ratings upgrades from underlying corporate improvements and through the rerating of mispriced securities.

### FUND FACTS

| | |
|---|---|
| Inception Date | April 29, 2016 |
| Investment Objective | Total return over the long term |
| Benchmark | J.P. Morgan Asia Credit Index |
| Portfolio Managers | Teresa Kong, CFA, Satya Patel |

### *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

Diversification does not ensure a profit or protect against a loss. An investment in the Fund is subject to credit, interest rate and currency risks. Credit risk is the change in the value of debt securities reflecting the ability and willingness of issuers to make principal and interest payments. Interest rate risk is the possibility that a Fund's yield will decline due to falling interest rates and the potential for bond prices to fall as interest rates rise. Currency risk is a decline in value of a foreign currency relative to the Fund's base currency which reduces the value of the foreign currency and investments denominated in that currency. Where a Class of Shares is denominated in a currency other than the Fund's base currency, additional currency risk may exist. The Fund may invest in the following: derivatives which can be volatile and affect Fund performance; high yield bonds (junk bonds) which can subject the Fund to substantial risk of loss; and structured investments which can change the risk or return, or replicate the risk or return of an underlying asset.

**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 funds may be subject to a higher degree of market risk than diversified funds because of concentration in a specific geographic location. Investing in small- and mid-size companies is more risky than investing in large companies as they may be more volatile and less liquid than large companies.

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