

## Performance Review

Chinese stocks declined during the quarter, underperforming emerging and developed market equities, which both broadly advanced. Concerns over macroeconomic conditions and a muted response to the targets and policies from the National People's Congress weighed on sentiment. Geopolitical tensions also pressured the share prices of several companies. This offset support from efforts to stabilize the equity market and regulatory intervention. Better-than-expected activity data released toward the end of the period also helped to limit losses. During the quarter, the People's Bank of China cut the five-year loan prime rate, which is used as a mortgage reference, and cut the reserve requirement ratio for banks to the lowest level since 2007.

## QUARTERLY KEY PERFORMANCE DRIVERS

	Stocks	Sectors
HELPED	NetEase Inc.	Information Technology (Lack of Exposure)
	Anta Sports Products Ltd.	Communication Services (Stock Selection, Overweight)
	Postal Savings Bank of China Co., Ltd.	Real Estate (Underweight)
HURT	New Horizon Health Ltd.	Energy (Underweight)
	Wuxi Biologics Cayman Inc.	Materials (Lack of Exposure)
	China Construction Bank Corp.	Utilities (Underweight)

- Biotechnology firm New Horizon Health was a notable detractor, as shares declined sharply in March, amid news that the company would not be able to publish 2023 results during the month. Trading of shares was suspended in Hong Kong in late March, by the company's request, to facilitate an investigation into an auditor's concerns surrounding fraud. The company denied wrongdoing, appointed two independent non-executive directors, and engaged a third-party group to lead the investigation.
- Biologics developer Wuxi Biologics weighed on relative returns. Shares declined sharply amid rising geopolitical uncertainty, owing to potentially harmful regulations in the United States. US officials introduced a proposed bill that would ban Wuxi and other Chinese companies from US government contracts due to alleged military ties, potentially lowering the company's exposure to a key market. Wuxi has denied such connections.
- In contrast, an overweight allocation to internet and gaming giant NetEase contributed to relative returns. Shares benefitted from a strong 2024 earnings outlook and the company's robust game pipeline. Fading concerns about new regulations for videogame usage, which weighed on NetEase shares in late 2023, and the Chinese government's granting of new game licenses also supported the stock.

## Outlook & Strategy

- We are optimistic that Chinese equities can post positive returns in 2024, driven by our belief that corporate earnings will likely recover amid improving economic activity and pro-growth policies. China's economic outlook remains challenging. While a swift rebound in growth is not likely, we saw some positive signs toward the end of the first quarter. Purchasing manager indexes in China rebounded in March, with the Caixin/S&P Global Index reaching its highest level in over a year. Drivers of the rebound included rising raw material purchases and inventories. Chinese industrial companies may be restocking ahead of the government's planned 20% increase in special bond issuance this year to US\$680 billion. The increase in special bond issuance is linked to the official gross domestic product (GDP) growth target of "around 5%" in 2024.
- We believe that select China-based companies have been oversold due to weak sentiment, but fundamentals remain strong. In our view, a recovery in earnings and monetary easing are two factors that will likely aid returns. Healthy corporate and household balance sheets should also help to boost equities, along with the likelihood of a US soft landing, and evidence that interest rates have peaked. Although risks such as geopolitical tensions remain, we are of the view that positive fundamental factors will continue to drive long-term returns.
- Ongoing property market risks, which have led to an easier policy environment, are holding back China's economy. Trade disputes remain unresolved in the longer term and are a symptom of broader tensions as heightened geopolitical stresses persist. We retain a neutral stance relative to some other markets to reflect growth risks, despite the valuation attractions of this market.
- Chinese authorities have followed through with plans to stimulate domestic consumption within the automobile, property and leisure industries, among others. We believe this precedes the implementation of concrete policies to shore up the economy, which, coupled with elevated household savings, should finally drive the premiumization opportunity at the heart of the consumption story in China and elsewhere. We are aware that more substantive policies and a rebound in consumer activity is a prerequisite for gains in Chinese equities to persist, and we remain watchful for such developments. We believe China's prioritization of high-quality growth will likely lead to a more favorable regulatory environment for the private sector, and that newer reform initiatives will focus on containing financial system risks and pursuing technology advancement and self-sufficiency.

## Fund Details

Inception Date	9/20/1994
Benchmarks	MSCI China All Shares Index-NR
CUSIP	88018T101
Ticker	TDF

## Fund Description

The fund seeks long-term capital appreciation by investing at least 45% of its total assets in the equity securities of Chinese companies.

- The interest-rate cutting cycle in emerging markets is building momentum, headlined by China's recent cuts. The onset of an easing cycle tilts the balancing act of tackling inflation while pursuing economic growth towards the latter. The impact of a rate cut is positive for businesses as it reduces their financing costs—potentially boosting corporate earnings and spurring investment, which will reinvigorate the economy. In China, regulatory guidance is likely to continue to pressure interest rates down.
- In addition to rate cuts, there are other positive long-term factors in China that unlock potential investment opportunities. The long-term structural tailwind of consumption growth via expansion of the middle class and premiumization of buying patterns is now more significant than ever, in our view, under the spotlight of economic reopening. Recent data surrounding employment and disposable income remain strong, which we believe will likely help drive the consumption recovery. Middle-class households are looking to draw down these savings to spend on experiences, products and services. We believe this is driving the premiumization trend opportunity in China. The transition to a greener future is another longstanding theme. China is home to well-run companies in the electric vehicle and solar equipment segment.
- Our team is starting to see signs of growth in China, especially among companies focused on the domestic economy. We believe some of these firms will benefit from long-term thematic growth drivers, including rising consumption and localization. We see opportunities in the industrials sector, driven by high levels of investment and innovation. However, we are cognizant that inflection points can happen quickly. This could in turn weigh on earnings. This occurred in 2023, when the solar energy and electric vehicle supply chains in North Asia saw overcapacity and a slowdown in demand, respectively. As such, while keeping a focus on the long term, we also remain alert for any potential changes in demand trends.
- Finally, we believe our long-standing local presence in China provides us with a well-rounded perspective to analyze tailwinds and headwinds. As active investors, we believe that our focus on long-term earnings power can help us navigate short-term volatility, while bearing in mind the lessons learned.

## Performance Data<sup>1</sup>

Average Annual Total Returns <sup>2</sup> (%)	1 Mth	3 Mths	1 Year	3 Year	5 Year	10 Year	Since Inception	Inception Date
Market Price	1.42	-3.79	-25.78	-25.15	-6.77	0.98	7.08	09/20/1994
NAV	0.43	-1.70	-24.96	-22.54	-6.82	0.27	6.40	09/20/1994
MSCI China All Shares Index-NR	0.65	-1.05	-16.63	-16.07	-4.10	2.49	—	—

**Performance shown represents past performance and is no guarantee of future results.** Current performance may be higher or lower than the performance shown. Investment return and principal value will fluctuate so shares, when sold, may be worth more or less than the original cost. Returns based on Market Price or NAV, and assume the reinvestment of all distributions at the Dividend Reinvestment Plan Price or NAV, respectively. All returns include the deduction of management fees, operating expenses and all other fund expenses, and do not reflect the deduction of brokerage commissions or taxes that investors may pay on distributions or the sale of shares. When applicable, performance would have been lower if fees had not been waived in various periods. The index is unmanaged and includes reinvestment of any income or distributions. It does not reflect any fees, expenses or sales charges. One cannot invest directly in an index, and an index is not representative of the fund's portfolio. Index data is provided for comparison purposes only. The fund is not managed against an index. Returns for periods of less than one year are not annualized. Please visit [franklintempleton.com](http://franklintempleton.com) for the most recent month-end performance.

An investor cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charges.

The **MSCI China All Shares Index-NR** captures large and mid-cap representation across China A-shares, B-shares, H-shares, Red-chips, P-chips and foreign listings (e.g. ADRs). The index aims to reflect the opportunity set of China share classes listed in Hong Kong, Shanghai, Shenzhen and outside of China. Net Returns (NR) include income net of tax withholdings when dividends are paid. Information is historical and may not reflect current or future portfolio characteristics. All portfolio holdings are subject to change. Important data provider notices and terms available at [www.franklintempletondatasources.com](http://www.franklintempletondatasources.com). Net Returns (NR) include income net of tax withholding when dividends are paid.

## Portfolio Diversification

### Top Holdings

Top Holdings	%
TENCENT HOLDINGS LTD	9.29
ALIBABA GROUP HOLDING LTD	5.93
CHINA YANGTZE POWER CO LTD	5.69
KWEICHOW MOUTAI CO LTD	5.18
NETEASE INC	4.53
FOCUS MEDIA INFORMATION TECHNOLOGY CO LTD	3.93
JIANGSU HENGRUI PHARMACEUTICALS CO LTD	3.16
PDD HOLDINGS INC	2.91
CHINA MERCHANTS BANK CO LTD	2.86
CHINA CONSTRUCTION BANK CORP	2.67

1. Net Returns (NR) include income net of tax withholding when dividends are paid.

2. Periods shorter than one year are shown as cumulative total returns.

## Investment Team

Nicholas Chui, CFA  
Years with Firm >1  
Years Experience 14

Eric Mok, CFA  
Years with Firm 25  
Years Experience 25

## What Are The Risks?

All investments involve risks, including possible loss of principal. International investments are subject to special risks, including currency fluctuations and social, economic and political uncertainties, which could increase volatility. These risks are magnified in **emerging markets**. There are special risks associated with investments in **China, Hong Kong and Taiwan**, including less liquidity, expropriation, confiscatory taxation, international trade tensions, nationalization, and exchange control regulations and rapid inflation, all of which can negatively impact the fund. Investments in Taiwan could be adversely affected by its political and economic relationship with China. To the extent the fund invests in companies in a specific **country or region**, the fund may experience greater volatility than a fund that is more broadly diversified geographically. The portfolio is **non-diversified** and may invest in a relatively small number of issuers, which may negatively impact the fund's performance and result in greater fluctuation in the value of the fund's shares. The managers' **environmental social and governance (ESG) strategies** may limit the types and number of investments available and, as a result, may forgo favorable market opportunities or underperform strategies that are not subject to such criteria. There is no guarantee that the strategy's ESG directives will be successful or will result in better performance.

## Important Information

The information provided is not a complete analysis of every material fact regarding any country, market, industry, security or fund. Because market and economic conditions are subject to change, comments, opinions and analyses are rendered as of the date of this material and may change without notice. A portfolio manager's assessment of a particular security, investment or strategy is not intended as individual investment advice or a recommendation or solicitation to buy, sell or hold any security or to adopt any investment strategy; it is intended only to provide insight into the fund's portfolio selection process. Holdings are subject to change.

**Distributions are not guaranteed and are subject to change. The Closed-End Funds are not sold or distributed by Franklin Distributors, LLC, or any affiliate of Franklin Resources, Inc.** Unlike open-end funds, shares are not continually offered. Like other public companies, closed-end funds have a one-time initial public offering, and once their shares are first issued, are generally bought and sold through non-affiliated broker/dealers and trade on nationally recognized stock exchanges. Share prices will fluctuate with market conditions and, at the time of sale, may be worth more or less than your original investment. Shares of exchange-traded closed-end funds may trade at a discount or premium to their original offering price, and often trade at a discount to their net asset value. Investment return, market price and net asset value will fluctuate with changes in market conditions. The Funds are subject to investment risks, including the possible loss of principal invested.

Gross expenses are the fund's total annual operating expenses as of the fund's annual report available at the time of publication. Actual expenses may be higher and may impact portfolio returns. Net expenses reflect voluntary fee waivers, expense caps and/or reimbursements. Voluntary waivers may be modified or discontinued at any time without notice. **NAV** is total assets less total liabilities divided by the number of shares outstanding. **Market Price**, determined by supply and demand, is the price an investor purchases or sells the fund. The Market Price may differ from a fund's NAV.

**Premium / Discount** reflects the difference between the NAV and the Market Price of the fund, and represents the amount that the fund is trading above or below its NAV, expressed as a percentage of the NAV.

**Before investing, carefully consider a fund's investment objectives, risks, charges and expenses. You can find this and other information in each prospectus, or summary prospectus, if available, at [www.franklintempleton.com](http://www.franklintempleton.com). Please read it carefully.**

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