

Morgan Stanley China A Share Fund, Inc.  
Form N-CSRS  
September 08, 2015

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

**FORM N-CSR**

**CERTIFIED SHAREHOLDER REPORT OF REGISTERED  
MANAGEMENT INVESTMENT COMPANIES**

Investment Company Act file number 811-21926

Morgan Stanley China A Share Fund, Inc.  
(Exact name of registrant as specified in charter)

522 Fifth Avenue, New York, New York  
(Address of principal executive offices)

10036  
(Zip code)

John H. Gernon

522 Fifth Avenue, New York, New York 10036  
(Name and address of agent for service)

Registrant's telephone number, including area code: 212-296-0289

Date of fiscal year December 31,  
end:

Date of reporting period: June 30, 2015

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Item 1 - Report to Shareholders

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**Morgan Stanley China A Share Fund, Inc.**

**Directors**

Frank L. Bowman

Michael Bozic

Kathleen A. Dennis

Nancy C. Everett

Jakki L. Haussler

James F. Higgins

Dr. Manuel H. Johnson

Joseph J. Kearns

Michael F. Klein

Michael E. Nugent

W. Allen Reed

Fergus Reid

**Officers**

Michael E. Nugent

*Chairperson of the Board*

John H. Gernon

*President and Principal  
Executive Officer*

Stefanie V. Chang Yu

*Chief Compliance Officer*

Joseph C. Benedetti

*Vice President*

Francis J. Smith

*Treasurer and Principal  
Financial Officer*

Mary E. Mullin

*Secretary*

**Adviser and Administrator**

Morgan Stanley Investment Management Inc.

522 Fifth Avenue

New York, New York 10036

**Sub-Adviser**

Morgan Stanley Investment Management Company

23 Church Street

16-01 Capital Square, Singapore 049481

**Custodian**

State Street Bank and Trust Company

One Lincoln Street

Boston, Massachusetts 02111

**Stockholder Servicing Agent**

Computershare Trust Company, N.A.

211 Quality Circle, Suite 210

College Station, Texas 77845

**Legal Counsel**

Dechert LLP

1095 Avenue of the Americas

New York, New York 10036

**Counsel to the Independent Directors**

Kramer Levin Naftalis & Frankel LLP

1177 Avenue of the Americas

New York, New York 10036

**Independent Registered Public Accounting Firm**

Ernst & Young LLP

200 Clarendon Street

Boston, Massachusetts 02116

For additional Fund information, including the Fund's net asset value per share and information regarding the investments comprising the Fund's portfolio, please call toll free 1 (800) 231-2608 or visit our website at [www.morganstanley.com/im](http://www.morganstanley.com/im). All investments involve risks, including the possible loss of principal.

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**INVESTMENT MANAGEMENT**

Morgan Stanley  
Investment Management Inc.  
Adviser

Morgan Stanley  
China A Share  
Fund, Inc.  
NYSE: CAF

Semi-Annual Report

June 30, 2015

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**Morgan Stanley China A Share Fund, Inc.**

**June 30, 2015**

Table of Contents

Letter to Stockholders	3
Investment Advisory Agreement Approval	6
Portfolio of Investments	9
Statement of Assets and Liabilities	11
Statement of Operations	12
Statements of Changes in Net Assets	13
Financial Highlights	14
Notes to Financial Statements	15
Portfolio Management	24
Investment Policy	25
Dividend Reinvestment Plan	30
U.S. Privacy Policy	31

## **Morgan Stanley China A Share Fund, Inc.**

**June 30, 2015**

Letter to Stockholders (unaudited)

### **Performance**

For the six months ended June 30, 2015, the Morgan Stanley China A Share Fund, Inc. (the "Fund") had total returns of 28.53%, based on net asset value, and 11.69% based on market value per share (including reinvestment of distributions), compared to its benchmarks, the MSCI China A Index (the "Index")\*, which returned 33.85%, and the "China Blended Index", a custom blend of 80% of the MSCI China A Index and 20% of the MSCI China Index\*\*, which returned 30.03%. On June 30, 2015, the closing price of the Fund's shares on the New York Stock Exchange was \$33.92, representing approximately 24.0% discount to the Fund's net asset value per share. Past performance is no guarantee of future results. Please keep in mind that high double-digit returns are highly unusual and cannot be sustained.

### **Factors Affecting Performance**

- During the first half of 2015, China's gross domestic product (GDP) growth was relatively stable at 7.0% in both the first quarter and the second quarter.<sup>i</sup> Money supply growth (as measured by M2, which includes cash, checking and savings deposits, money market funds, and other time deposits) dipped to a low of 10.1% in April.<sup>ii</sup> Subsequently, the central bank announced additional monetary easing measures and M2 growth rebounded to 11.8% in June. In an attempt to lower funding cost, the People's Bank of China announced interest rates cuts of 25 basis points each in February, May, and June, and announced reserve requirement ratio cuts in February (50 basis points), April (100 basis points) and June (50 basis points). The properties market showed some signs of recovery in the second quarter as new home sales improved in both price and volume. On the other hand, new home starts declined year-over-year in the first half of 2015. New home supply will likely continue to be high in 2015, and policy easing measures may likely continue to help boost demand for properties. Growth in the shadow banking sector in which trust funds and off-balance sheet interbank activities are used to create credit slowed after regulators made efforts to rein them in. However, shadow banking remains a concern, while margin financing for equities became a new problem. These issues could limit the magnitude of monetary easing, even though the inflation rate has been benign.
- The renminbi currency was unchanged during the reporting period. As China's economy has been transforming from export-driven to more domestic demand-driven, the impact of exchange rate volatility to the Chinese economy will be moderating, and the central bank will likely gradually increase flexibility in the foreign exchange system that could allow the exchange rate to be determined by supply and demand in the market more freely.
- The Index was volatile during the first half of 2015, with high volatility for many single stocks as well. During the first half of 2015, the market rallied by nearly 62% from the end of December to the peak on June 12, driven by strong market sentiment due to factors such as monetary loosening, interest rate cuts, state-owned enterprise reform, a pick-up in margin lending activities, strong post initial public offering (IPO) performance for the recent IPOs, bullish messages by the state media and the securities regulators, to name a few.<sup>iii</sup> Yet, the size of margin lending became too large to be self-sustainable. Subsequently, the unwinding of margin lending led to a sharp decline of 17.6% from the peak on June 12 to the end of June, and a 34.7% decline from the peak on June 12 to the bottom on July 8 (which occurred after the close of the reporting period).<sup>iv</sup>



## **Morgan Stanley China A Share Fund, Inc.**

**June 30, 2015**

Letter to Stockholders (unaudited) (cont'd)

- The anti-graft campaign that was started in the second half of 2013 continued, and will likely continue for a longer period of time. As a result of the campaign, high-end consumption fell sharply initially and then stabilized. Overall consumption growth remained relatively healthy with retail sales growth at around 10% to 10.5% in the first half of 2015, slowing down slightly from 12.0% in 2014.<sup>v</sup> A detailed reform blueprint was announced after the third plenum (policy making meeting) concluded in November 2013. The key thesis included: 1) removing and simplifying the government approval processes to vitalize the private sector; 2) reforming state-owned enterprises (SOEs) maintaining SOEs' market leader roles while protecting rights and encouraging development of private companies; and 3) emphasizing the role of the market in resource allocation. In the first half of 2014, a "mixed ownership" model for SOEs was introduced. Some SOEs invited private investors to take minority stakes in some of their businesses to optimize the private investors' knowledge and expertise to improve efficiency. We consider this an encouraging first step, but the actual execution will be the key.
- For the six-month period, the Fund's overweight position in the health care and consumer discretionary sectors, together with underweight exposure to financials, were positive contributors to performance, while relative underweight exposures to both the industrials and information technology (IT) sectors hurt performance over this period. Cash held in the portfolio was another drag on performance, as the Index rose more than 30% over the reporting period.
- At the stock level, active weights in industrials boosted performance. However, this was offset by negative stock selection from active weights in IT, consumer staples, materials, consumer discretionary and health care stocks.
- The Fund occasionally utilizes P-notes (participation notes) to gain access to China's A-share market. P-note exposure is intended to mirror the performance of the underlying stock. There is no leverage associated with P-notes.

### **Management Strategies**

- Over the course of the period, the Fund held overweight positions in the consumer staples, health care and consumer discretionary sectors. We believe China is likely to change its economic growth structure over the next decade, i.e., from one that is more investment- and export-driven to a more domestic consumption-driven one. In addition, we believe that rapid income growth and continuous urbanization should not only boost volume growth but also lead to ongoing demand as consumers trade up to more expensive items and brands. Specifically, we like consumer discretionary and consumer staples companies with strong brand recognition and pricing power, and consumer retailers with competitive distribution networks.
- We are positive on the health care sector, as we believe expanding social medical coverage and facilities construction are likely to boost Chinese health care spending in the future. In particular, we like pharmaceutical companies with strong brand images, superior quality control and strong distribution networks that can capture market share in a highly fragmented market.
- We are also positive on selected IT companies, as we believe many Chinese corporations have been growing on a scale that requires capital expenditures in upgrading their IT systems to optimize operations and cost management. However, valuations for a lot of the stocks in this sector are demanding and are priced based on "blue-sky" scenarios that are difficult to achieve. As such, we remain disciplined in stock selection.



**Morgan Stanley China A Share Fund, Inc.**

**June 30, 2015**

Letter to Stockholders (unaudited) (cont'd)

- We are positive on insurers, neutral on banks, and cautious on brokers. We think the ongoing financial reforms could create growth opportunities for insurers and brokers at the expense of banks' profitability. Yet, valuations for most brokers are highly demanding and we continue to be sensitive to valuations.
- The Fund held underweight positions in the industrials and materials sectors on concerns over sluggish demand, overcapacity, margin pressures, an expected slowdown in fixed-asset investment and weak overseas demand. We will keep updated over the "one-belt and one-road" or "Silk road economic belt" plan, proposed by Chairman Xi that would emulate the historic silk road that connects China to the Mediterranean. It is a project that could involve substantial infrastructure construction and potentially put a lot of the overcapacity in the industrials and materials sectors to use. Yet, the project's details remain to be seen. Within the industrials sectors, we are positive on selected infrastructure stocks that have low capital expenditures, high free cash flows, steady businesses and high dividend yields.
- We are negative on the utilities and telecommunications sectors, as we believe they have limited growth potential, tight profit margins, and high capital expenditures. Yet, given the current environment of declining interest rates that could benefit some utilities companies, we will look into opportunities in this sector more actively.

Sincerely,

John H. Gernon  
President and Principal Executive Officer July 2015

\*The MSCI China A Index is a free float-adjusted market capitalization index that is designed to measure equity market performance of the China A share market. The performance of the Index is listed in U.S. dollars and assumes reinvestment of net dividends. It is not possible to invest directly in an index.

\*\*The MSCI China Index is designed to measure equity market performance of China. The performance of the Index is listed in U.S. dollars and assumes reinvestment of net dividends. It is not possible to invest directly in an index.

<sup>i</sup> GDP data from National Bureau of Statistics

<sup>ii</sup> Money supply data from the People's Bank of China

<sup>iii</sup> MSCI

<sup>iv</sup> MSCI and Bloomberg L.P.

<sup>v</sup> Bloomberg L.P.

## **Morgan Stanley China A Share Fund, Inc.**

**June 30, 2015**

Investment Advisory Agreement Approval (unaudited)

### **Nature, Extent and Quality of Services**

The Board reviewed and considered the nature and extent of the investment advisory services provided by the Adviser (as defined herein) under the advisory agreement, including portfolio management, investment research and equity and fixed income securities trading. The Board reviewed similar information and factors regarding the Sub-Adviser (as defined herein), to the extent applicable. The Board also reviewed and considered the nature and extent of the non-advisory, administrative services provided by the Fund's Adviser under the administration agreement, including accounting, operations, clerical, bookkeeping, compliance, business management and planning, legal services and the provision of supplies, office space and utilities at the Adviser's expense. The Board also considered the Adviser's investment in personnel and infrastructure that benefits the Fund. (The Adviser and Sub-Adviser together are referred to as the "Adviser" and the advisory, sub-advisory and administration agreements together are referred to as the "Management Agreement.") The Board also considered that the Adviser serves a variety of other investment advisory clients and has experience overseeing service providers. The Board also compared the nature of the services provided by the Adviser with similar services provided by non-affiliated advisers as reported to the Board by Lipper, Inc. ("Lipper").

The Board reviewed and considered the qualifications of the portfolio managers, the senior administrative managers and other key personnel of the Adviser who provide the administrative and advisory services to the Fund. The Board determined that the Adviser's portfolio managers and key personnel are well qualified by education and/or training and experience to perform the services in an efficient and professional manner. The Board concluded that the nature and extent of the advisory and administrative services provided were necessary and appropriate for the conduct of the business and investment activities of the Fund and supported its decision to approve the Management Agreement.

### **Performance, Fees and Expenses of the Fund**

The Board reviewed the performance, fees and expenses of the Fund compared to its peers, as determined by Lipper, and to appropriate benchmarks where applicable. The Board discussed with the Adviser the performance goals and the actual results achieved in managing the Fund. When considering a fund's performance, the Board and the Adviser place emphasis on trends and longer-term returns (focusing on one-year, three-year and five-year performance, as of December 31, 2014, or since inception, as applicable). When a fund underperforms its benchmark and/or its peer group average, the Board and the Adviser discuss the causes of such underperformance and, where necessary, they discuss specific changes to investment strategy or investment personnel. The Board noted that the Fund's performance was better than its peer group average for the one-, three- and five-year periods. The Board also noted that the Fund outperformed its benchmark index for the three- and five-year periods, but underperformed its benchmark index for the one-year period. The Board discussed with the Adviser the level of the advisory and administration fees (together, the "management fee") for this Fund relative to comparable funds and/or other accounts advised by the Adviser and/or compared to its peers as determined by Lipper. In addition to the management fee, the Board also reviewed the Fund's total expense ratio. When a fund's management fee and/or its total expense ratio are higher than its peers, the Board and the Adviser discuss the reasons for this and, where appropriate, they discuss possible waivers and/or caps. The Board noted that while the Fund's management fee was higher than its peer group average, the total expense ratio was higher but close to its peer group average. After discussion, the Board



## **Morgan Stanley China A Share Fund, Inc.**

**June 30, 2015**

### **Investment Advisory Agreement Approval (unaudited) (cont'd)**

concluded that the Fund's (i) performance was competitive with its peer group average; (ii) management fee was acceptable; and (iii) total expense ratio was competitive with its peer group average.

### **Economies of Scale**

The Board considered the size and growth prospects of the Fund and how that relates to the Fund's total expense ratio and particularly the Fund's management fee rate, which does not include breakpoints. In conjunction with its review of the Adviser's profitability, the Board discussed with the Adviser how a change in assets can affect the efficiency or effectiveness of managing the Fund and whether the management fee level is appropriate relative to current and projected asset levels and/or whether the management fee structure reflects economies of scale as asset levels change. The Board considered that, with respect to closed-end funds, the assets are not likely to grow with new sales or grow significantly as a result of capital appreciation. The Board concluded that economies of scale for the Fund were not a factor that needed to be considered at the present time.

### **Profitability of the Adviser and Affiliates**

The Board considered information concerning the costs incurred and profits realized by the Adviser and its affiliates during the last year from their relationship with the Fund and during the last two years from their relationship with the Morgan Stanley Fund Complex and reviewed with the Adviser the cost allocation methodology used to determine the profitability of the Adviser and affiliates. The Board has determined that its review of the analysis of the Adviser's expenses and profitability supports its decision to approve the Management Agreement.

### **Other Benefits of the Relationship**

The Board considered other direct and indirect benefits to the Adviser and/or its affiliates derived from their relationship with the Fund and other funds advised by the Adviser. These benefits may include, among other things, fees for trading, distribution and/or shareholder servicing and for transaction processing and reporting platforms used by securities lending agents, and research received by the Adviser generated from commission dollars spent on funds' portfolio trading. The Board reviewed with the Adviser these arrangements and the reasonableness of the Adviser's costs relative to the services performed. The Board has determined that its review of the other benefits received by the Adviser or its affiliates supports its decision to approve the Management Agreement.

### **Resources of the Adviser and Historical Relationship Between the Fund and the Adviser**

The Board considered whether the Adviser is financially sound and has the resources necessary to perform its obligations under the Management Agreement. The Board also reviewed and considered the historical relationship between the Fund and the Adviser, including the organizational structure of the Adviser, the policies and procedures formulated and adopted by the Adviser for managing the Fund's operations and the Board's confidence in the competence and integrity of the senior managers and key personnel of the Adviser. The Board concluded that the Adviser has the financial resources necessary to fulfill its obligations under the Management Agreement and that it is beneficial for the Fund to continue its relationship with the Adviser.



**Morgan Stanley China A Share Fund, Inc.**

**June 30, 2015**

Investment Advisory Agreement Approval (unaudited) (cont'd)

**Other Factors and Current Trends**

The Board considered the controls and procedures adopted and implemented by the Adviser and monitored by the Fund's Chief Compliance Officer and concluded that the conduct of business by the Adviser indicates a good faith effort on its part to adhere to high ethical standards in the conduct of the Fund's business.

**General Conclusion**

After considering and weighing all of the above factors, with various written materials and verbal information presented by the Adviser, the Board concluded that it would be in the best interest of the Fund and its shareholders to approve renewal of the Management Agreement for another year. In reaching this conclusion the Board did not give particular weight to any single piece of information or factor referenced above. The Board considered these factors and information over the course of the year and in numerous meetings, some of which were in executive session with only the independent Board members and their counsel present. It is possible that individual Board members may have weighed these factors, and the information presented, differently in reaching their individual decisions to approve the Management Agreement.





**Morgan Stanley China A Share Fund, Inc.****June 30, 2015**

Portfolio of Investments (unaudited)

	Shares	Value (000)
<b>COMMON STOCKS (97.8%)</b>		
<b>Automobiles (3.8%)</b>		
SAIC Motor Corp., Ltd., Class A	10,240,738	\$ 37,323
<b>Banks (16.2%)</b>		
China Merchants Bank Co., Ltd., Class A	6,140,400	18,537
Industrial & Commercial Bank of China Ltd., Class A	121,665,748	103,596
Shanghai Pudong Development Bank Co., Ltd., Class A	12,942,814	35,399
		157,532
<b>Beverages (12.5%)</b>		
Kweichow Moutai Co., Ltd., Class A	898,500	37,333
Tsingtao Brewery Co., Ltd., Class A	11,308,085	84,961
		122,294
<b>Construction Materials (1.5%)</b>		
Anhui Conch Cement Co., Ltd., Class A	4,306,448	14,896
<b>Electrical Equipment (3.1%)</b>		
NARI Technology Co., Ltd., Class A	9,170,699	30,599
<b>Electronic Equipment, Instruments &amp; Components (6.4%)</b>		
GoerTek, Inc., Class A	4,538,777	26,277
Universal Scientific Industrial Shanghai Co., Ltd., Class A	13,148,785	36,068
		62,345
<b>Food &amp; Staples Retailing (3.7%)</b>		
Zhongbai Holdings Group Co., Ltd., Class A	18,898,700	36,481
<b>Food Products (2.9%)</b>		
Inner Mongolia Yili Industrial Group Co., Ltd., Class A	9,269,741	28,253
<b>Health Care Providers &amp; Services (1.4%)</b>		
Shanghai Pharmaceuticals Holding Co., Ltd., Class A	3,766,204	13,526
<b>Hotels, Restaurants &amp; Leisure (1.2%)</b>		
Tsui Wah Holdings Ltd. (b)	38,690,000	12,029
<b>Household Durables (5.7%)</b>		
Qingdao Haier Co., Ltd., Class A	11,388,000	55,700
<b>Independent Power Producers &amp; Energy Traders (0.0%)</b>		
China National Nuclear Power Co., Ltd. (a)	20,000	42

	Shares	Value (000)
<b>Insurance (4.7%)</b>		
China Pacific Insurance Group Co., Ltd., Class A	9,454,400	\$ 46,014
<b>Media (0.4%)</b>		
Bona Film Group Ltd. ADR (a)	318,002	3,880
<b>Multi-line Retail (3.2%)</b>		
Beijing Wangfujing Department Store Group Co., Ltd., Class A	6,042,942	30,697
<b>Pharmaceuticals (10.1%)</b>		
China Resources Sanjiu Medical & Pharmaceutical Co., Ltd., Class A	20,073,590	98,377
<b>Real Estate Management &amp; Development (8.2%)</b>		
China Overseas Grand Oceans Group Ltd. (b)	52,063,000	26,395
China Vanke Co., Ltd., Class A	22,793,297	53,372
		79,767
<b>Road &amp; Rail (9.9%)</b>		
Daqin Railway Co., Ltd., Class A	42,436,900	96,084
<b>Transportation Infrastructure (2.9%)</b>		
Jiangsu Expressway Co., Ltd., Class A	11,853,716	18,504
Shanghai International Airport Co., Ltd., Class A	1,992,745	10,187
		28,691
<b>TOTAL COMMON STOCKS</b> (Cost \$817,575)		954,530
<b>SHORT-TERM INVESTMENT (0.3%)</b>		
<b>Investment Company (0.3%)</b>		
Morgan Stanley Institutional Liquidity Funds Money Market Portfolio Institutional Class (See Note E) (Cost \$2,807)	2,807,000	2,807
<b>TOTAL INVESTMENTS (98.1%)</b> (Cost \$820,382)		957,337
<b>OTHER ASSETS IN EXCESS OF LIABILITIES (1.9%)</b>		18,671
<b>NET ASSETS (100.0%)</b>		\$976,008

(a) Non-income producing security.

(b) Security trades on the Hong Kong exchange.

ADR American Depositary Receipt.

The accompanying notes are an integral part of the financial statements.

**Morgan Stanley China A Share Fund, Inc.**

**June 30, 2015**

Portfolio of Investments (unaudited) (cont'd)

**Portfolio Composition**

<b>Classification</b>	<b>Percentage of Total Investments</b>
Other*	29.8%
Banks	16.5
Beverages	12.8
Pharmaceuticals	10.3
Road & Rail	10.0
Real Estate Management & Development	8.3
Electronic Equipment, Instruments & Components	6.5
Household Durables	5.8
<b>Total Investments</b>	<b>100.0%</b>

\* Industries and/or investment types representing less than 5% of total investments.

The accompanying notes are an integral part of the financial statements.



**Morgan Stanley China A Share Fund, Inc.**

**June 30, 2015**

Financial Statements

	<b>June 30, 2015 (unaudited) (000)</b>
Statement of Assets and Liabilities	
<b>Assets:</b>	
Investments in Securities of Unaffiliated Issuers, at Value (Cost \$817,575)	\$ 954,530
Investment in Security of Affiliated Issuer, at Value (Cost \$2,807)	2,807
Total Investments in Securities, at Value (Cost \$820,382)	957,337
Foreign Currency, at Value (Cost \$21,554)	21,615
Cash	@
Dividends Receivable	50