Guinness Asian Equity Income Fund

INVESTMENT COMMENTARY – November 2016

Launch date	**19.12.13**
Team	**Edmund Harriss** (manager) **Mark Hammonds** (analyst) **Sharukh Malik** (analyst)

Aim

The Guinness Asian Equity Income Fund is designed to provide investors with exposure to high quality dividend-paying companies in the Asia Pacific region. The Fund aims to provide long-term capital appreciation and a source of income that has the potential to grow over time.

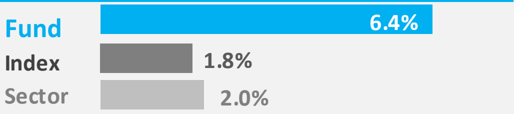
Performance (in USD) 31/10/2016

Fund	Guinness Asian Equity Income (X)
Index	MSCI AC Pacific ex Japan Index
Sector	IA Asia Pacific ex Japan

	2013	2014	2015
Fund	-	10.7	-4.4
Index	3.4	2.8	-9.4
Sector	3.8	3.1	-8.6

	YTD	1 year	From launch
Fund	11.0	6.1	19.5
Index	10.4	8.0	5.2
Sector	9.9	6.7	5.8

Annualised % total return from launch (USD)



Risk analysis (annualised, weekly, from launch)

	Index	Sector	Fund
Alpha	0	0.1	4.9
Beta	1	0.9	0.8
Info ratio	0	0.0	0.8
Max drwdn	-28.5	-26.7	-24.3
Tracking err	0	3.7	5.7
Volatility	15.4	13.9	13.1
Sharpe ratio	0.0	0.0	0.2

Past performance should not be taken as an indicator of future performance. The value of this investment and any income arising from it can fall as well as rise as a result of market and currency fluctuations.

Source: Financial Express, bid to bid, total return in USD.

What does a Trump victory mean for Asia?

The outlook in our original monthly update below has been somewhat overtaken by the events of recent days. While the initial market reaction in Asia to Donald Trump's victory was negative, markets very quickly began to show signs of stabilisation. The marked change of tone in Trump's acceptance speech went some way to ensure this.

How far Trump will go in changing trade policies obviously remains to be seen. During his campaign, he talked about slapping large import tariffs on Chinese goods, but we suspect that he will not be as aggressive as he suggested. When faced with the prospect of paying significantly more for imported goods, we think the economic interest of the US consumer will out.

The other significant factor we have observed in recent days has been a sell-off in long term bonds, as expectations of interest rate rises have increased. We believe the companies in our fund are relatively well insulated against a rising rate environment. We do not own overly leveraged companies, so any impact on interest expense should be relatively small. And by requiring companies to have generated returns consistently above the cost of capital, there is effectively a 'cushion' to absorb increases in discount rates.

We emphasise that our investing approach is not macro-driven. We look for quality companies with excellent track records, that we are comfortable holding over the long term. We think such companies are well-positioned to cope with periods of turbulence, and that over time, their superior operating performance will outweigh any short-term noise in the market.

Below is our regular monthly update.

Markets

The best and most significant news from the region has come from China with producer price deflation now having ended. The return of pricing power, in part due to rising commodity prices, helps ease the capacity and debt burdens of the heavy industrial sector. Industrial profits have picked up and cash flows along with them, which serves to strengthen debt servicing capacity. We can see this easing of the debt burden through reports from the banks which show a moderation in the pace of non-performing loan formation. To be clear, debt and capacity issues remain and will be with us for a while yet, but as we have argued consistently, conditions in China are pointing toward improvement and are much improved from the extreme pessimism at the start of the year.

The most recent Chinese economic data show rising Purchasing Managers indices which indicate rising industrial activity and confidence with a marked pickup in new orders. This same data series also indicates weaker demand from the export side, which is a consistent story across the region. External demand both from the US and from Europe remains fragile with the result that export numbers from China, South Korea, Taiwan, Thailand, Singapore and Malaysia are all weak. The investment focus therefore has to be on domestic activity and on those exporters with specific competitive advantages and specialist products rather than those producing lower-value mass-market goods.

The death of the King of Thailand in October following a long illness put the country into mourning. King Bhumibol Adulyadej reigned for 70 years and was revered. His successor does not enjoy the same esteem and in a country that has seen more than its fair share of political turbulence, uncertainty has risen. However, for the present it seems the succession will proceed. The government (which took control following a coup in 2014) is stable and although the elections which were expected for 2017 might not now happen until 2018, the country, its businesses and its financial sector are operating uninterrupted. The stock market, which fell 5% immediately following the news, has recovered all its losses and indeed outperformed the region, as measured by the MSCI AC Pacific ex Japan Index in October.

South Korea has also had a difficult month with its president caught up in a political scandal and its leading company, Samsung Electronics, forced to recall and to cancel production of its new Galaxy Note 7 smartphone. The political scandal is unusual in that it concerns the heavy influence exerted by a close friend of President Park, ranging from the way she dresses to the content of speeches and the formulation of government policy. There are also allegations of undue pressure placed on companies to donate substantial funds to foundations controlled by Park's friend in return for her political influence. The nature of this relationship has come as shock to Korean society and has pushed the President's approval ratings down to single digits. The concern therefore is what she might do to court popularity and how any such actions would affect Korea's relations with China, Japan or North Korea. For now, however, this is primarily a domestic issue and we do not expect it to be long-lasting (elections are no more than a year away).

Our overall view on the region nevertheless remains upbeat. Markets have rallied since the middle of the year primarily on the back of low valuations and recognition that earlier fears were overdone. The next stage of the rally depends on earnings growth and upward revisions to profit forecasts. We are encouraged to see early signs that this is coming through. The driving forces behind this are likely to be primarily domestic while demand for exports overall is expected to remain weak. There are few inflationary pressures to speak of within the region to cause central banks to tighten policy and most countries that intend to increase spending on infrastructure or pursue other means to boost consumption have the funds to do so. It is worth noting that the end of producer price deflation in China signals a weakening of the deflationary force that China has exerted globally. When added to the fact that energy prices have stabilised and base effects will soon wear off, we may see a more marked increase in inflation than is currently priced in. How much more inflationary pressure might be expected as a result of the new US president's spending plans has yet to be seen. This may not lead to significantly faster interest rate increases in the US, since Mrs Yellen has already signalled her willingness to tolerate higher inflation for longer, but financial conditions may tighten nonetheless through rising bond yields and a stronger dollar (on the back of rising interest rate expectations).

Performance

In the month of October Asian equities fell along with global equities. The benchmark for the fund, the MSCI AC Pacific ex. Japan Index, fell 1.7% in US dollar terms, and the MSCI World Index fell 1.9%.

The only market in the region that posted a positive return (other than Japan) was Taiwan, which rose 1.4% as measured by its MSCI country index. Performance was weakest in New Zealand, Singapore and Korea. New Zealand and Korea were two of the stronger performers in the third quarter, so it is unsurprising that some of their gains were surrendered.

On a sector basis, Materials and Energy were the only sectors to post positive performance, rising 1.7% and 0.4% respectively in October. Because of our focus on companies that have demonstrated persistent returns on capital, the fund currently has no exposure to Materials and limited exposure to Energy. Healthcare, Real Estate and Consumer Staples were the weakest sectors, with Healthcare falling 6.8%.

The best performer in the portfolio was Luk Fook Holdings, a jewellery retailer operating in China, Hong Kong and Macau. The company reported a moderate recovery in sales in September and October, adding to hopes that earnings would start to improve. Other strong performers were Hon Hai Precision, an outsourced manufacturer and assembler of consumer electronics for Apple and others, and Novatek Microelectronics, a manufacturer of chipsets used in flat-panel displays.

Weaker performers in the portfolio included KT&G, a Korean tobacco company and Belle International, a retailer of footwear in China. Both of our healthcare holdings – St Shine Optical and Sonic Healthcare – also struggled.

As we have written before, our focus within the fund is very much on individual stock selection. We pick our thirty-six best ideas and put them into an equally weighted portfolio. We typically view periods of short-term weakness in individual stock prices as an opportunity to rebalance the portfolio, recycling gains back into laggards.

Outlook

Our outlook for the region and for our approach to investing in it remains upbeat on the basis of attractive valuations and the rising prospects for profits growth. While the fund invests in quality companies, it trades on an aggregate valuation that is a substantial discount to the market, which is in turn at a discount to world equities. These attractive valuations underscore the investment opportunity that we see in Asia. The portfolio also offers an attractive source of income.

It is clear however that not every part of the market is that optimistic. Global markets appear to reflect increasing levels of uncertainty, both political and economic, with the VIX volatility index picking up in recent days. We believe that the merits of investing in quality companies at attractive valuations are clear. We are happy to hold our portfolio companies through any down cycle (they have already demonstrated the ability to generate strong returns on capital in the 2008-09 down cycle) and we will continue to rebalance the portfolio in response to market volatility, seeking to add to positions where opportunities to do so are presented. We also believe that our focus on value minimises potential valuation risk – something that could be very useful, should markets undergo a correction.

Edmund Harriss (portfolio manager)
Mark Hammonds & **Sharukh Malik** (analysts)

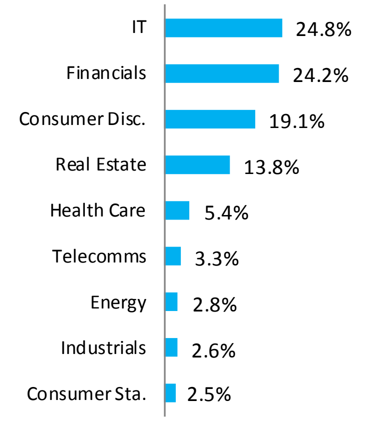
PORTFOLIO

31/10/2016

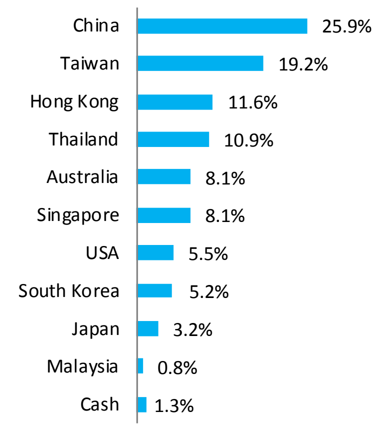
Fund top 10 holdings

Luk Fook Holdings	3.4%
Relo Holdings	3.2%
Qualcomm	3.0%
Taiwan Semiconductor	3.0%
China Minsheng Banking	3.0%
BOC Hong Kong	2.9%
Hon Hai Precision Industry	2.9%
Novatek Microelectronics	2.9%
PTT Public Company	2.8%
China Lilang	2.8%
% of Fund in top 10	29.8%
Total number of stocks in Fund	37

Sector analysis



Geographic allocation



PERFORMANCE

31/10/2016

Discrete years % total return (USD)	Oct '12	Oct '13	Oct '14	Oct '15	Oct '16
Fund (X class, 1.24% OCF)	-	-	-	0.0	6.1
MSCI AC Pacific ex Japan Index	6.8	11.6	4.0	-10.5	8.0
IA Asia Pacific ex Japan	5.4	11.5	4.2	-8.6	6.7

Cumulative % total return (USD)	1 month	Year-to-date	1 year	3 years	From launch
Fund (X class, 1.24% OCF)	-2.6	11.0	6.1	-	19.5
MSCI AC Pacific ex Japan Index	-1.7	10.4	8.0	0.5	5.2
IA Asia Pacific ex Japan	-1.8	9.9	6.7	1.6	5.8

Annualised % total return from launch (USD)

Risk analysis - Annualised, weekly, from launch on 19.12.2013, in USD

31/10/2016	Index	Sector	Fund
Alpha	0	0.12	4.87
Beta	1	0.88	0.79
Information ratio	0	-0.01	0.79
Maximum drawdown	-28.49	-26.72	-24.26
R squared	1	0.95	0.87
Sharpe ratio	0.00	0.00	0.23
Tracking error	0	3.73	5.73
Volatility	15.37	13.91	13.10

Past performance should not be taken as an indicator of future performance. The value of this investment and any income arising from it can fall as well as rise as a result of market and currency fluctuations.
Source: Financial Express, bid to bid, total return. Fund launch date: 19.12.2013.

Important information

Issued by Guinness Asset Management Limited, authorised and regulated by the Financial Conduct Authority.

This report is primarily designed to inform you about equities and equity markets invested in by the Guinness Asian Equity Income Fund. It may provide information about the Fund's portfolio, including recent activity and performance. It contains facts relating to the equity markets and our own interpretation. Any investment decision should take account of the subjectivity of the comments contained in the report.

This document is provided for information only and all the information contained in it is believed to be reliable but may be inaccurate or incomplete; any opinions stated are honestly held at the time of writing, but are not guaranteed. The contents of the document should not therefore be relied upon. It should not be taken as a recommendation to make an investment in the Fund or to buy or sell individual securities, nor does it constitute an offer for sale.

Risk
The Guinness Asian Equity Income Fund is an equity fund. Investors should be willing and able to assume the risks of equity investing. The value of an investment and the income from it can fall as well as rise as a result of market and currency movement, and you may not get back the amount originally invested. The Fund invests only in stocks of companies that are traded on Asian stock exchanges or that do at least half of their business in Asia; it is therefore susceptible to the performance of that region, and can be volatile. Details on the risk factors are included in the Fund's documentation, available on our website. Shareholders should note that all or part of the fees and expenses will be charged to the capital of the Fund. This will have the effect of lowering the capital value of your investment.

Documentation
The documentation needed to make an investment, including the Prospectus, the Key Investor Information Document (KIID) and the Application Form, is available from the website www.guinnessfunds.com, or free of charge from:-

- the Manager: Capita Financial Managers (Ireland) Limited, 2 Grand Canal Square, Grand Canal Harbour, Dublin 2, Ireland; or,
- the Promoter and Investment Manager: Guinness Asset Management Ltd, 14 Queen Anne's Gate, London SW1H 9AA.

Residency
In countries where the Fund is not registered for sale or in any other circumstances where its distribution is not authorised or is unlawful, the Fund should not be distributed to resident Retail Clients. **NOTE: THIS INVESTMENT IS NOT FOR SALE TO U.S. PERSONS.**

Structure & regulation
The Fund is a sub-fund of Guinness Asset Management Funds PLC (the "Company"), an open-ended umbrella-type investment company, incorporated in Ireland and authorised and supervised by the Central Bank of Ireland, which operates under EU legislation. If you are in any doubt about the suitability of investing in this Fund, please consult your investment or other professional adviser.

Switzerland
The prospectus and KIID for Switzerland, the articles of association, and the annual and semi-annual reports can be obtained free of charge from the representative in Switzerland, Carnegie Fund Services S.A., 11, rue du Général-Dufour, 1204 Geneva, Switzerland, Tel. +41 22 705 11 77, www.carnegie-fund-services.ch. The paying agent is Banque Cantonale de Genève, 17 Quai de l'Ile, 1204 Geneva, Switzerland.

Telephone calls may be recorded and monitored.