Guinness Global Money Managers Fund

A high conviction equity fund managed by Will Riley and Tim Guinness investing in quoted companies in the asset management sector.

INVESTMENT COMMENTARY – January 2017

Aim

The Fund aims to deliver long-term capital growth by capturing the strong returns that successful asset management companies can deliver to shareholders.

We expect asset managers to outperform the broad market over the long term, primarily due to the ability of successful managers to grow their earnings more rapidly than the broad market.

Investment case

High returns on capital

Asset managers need little capital to grow. Shareholder returns can therefore be very high.

Growing global sector

Global AUM is growing faster than world equity markets, supporting revenue growth in the sector.

Low balance sheet risk

Asset managers tend to have low gearing vs other financial companies, reducing balance sheet risk.

Above average dividend yield

The sector's high free cash flow translates into higher average dividend yields than broad markets.

Index	MSCI World Index
Financials Index	MSCI World Financials Index
Fund launch	31.12.10

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, gross total return.

THOMSON REUTERS
LIPPER FUND AWARDS 2015
SWITZERLAND

2015: BEST FUND OVER 3 YEARS
EQUITY SECTOR BANKS & OTHER FINANCIALS

Asset management sector

In this month's update, we review the asset management sector and our Fund performance in 2016, and consider the outlook for 2017 and beyond.

Performance in 2016

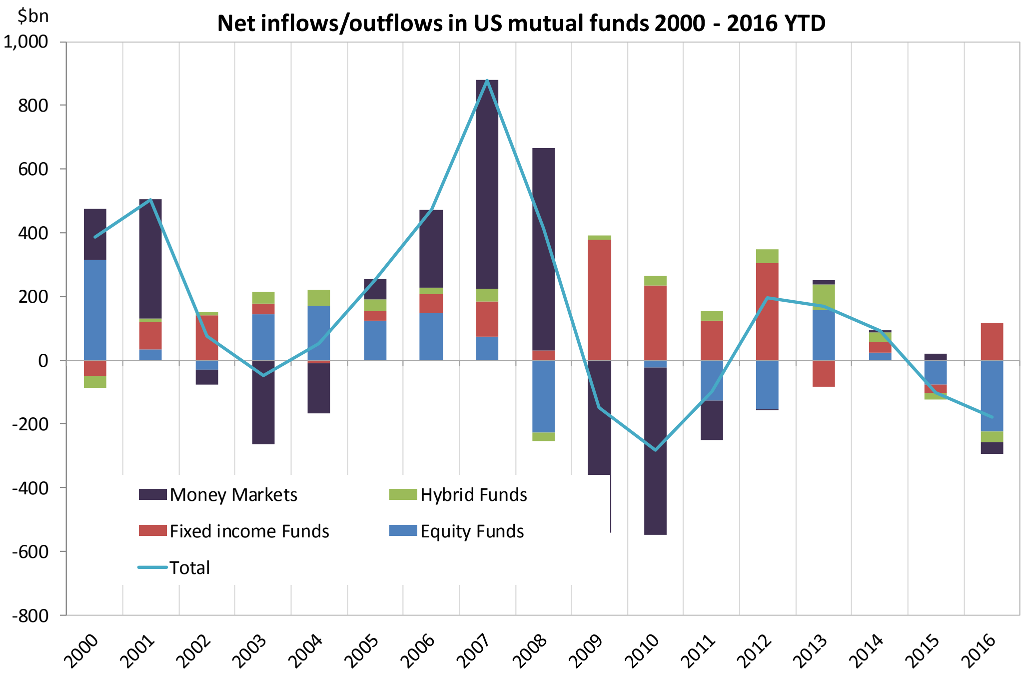
The Global Money Managers Fund (class E) in 2016 produced a total return of –4.7% in US dollar terms (+13.7% in GBP).

It was a difficult year for the money management sector, with record levels of active-to-passive rotation affecting traditional asset managers, and the weakening of sterling post the 'Brexit' vote impacting the dollar earnings of UK based asset and wealth managers. The fund was particularly weak in the first half of the year, as the first quarter sell-off in equities, coupled with concerns over a slowdown in China, were then compounded by the uncertainty created by the UK's referendum at the end of June. Asset managers fared better during the second half of the year, with the fund outperforming broad equities, as first rises in interest rates in the US, a Trump victory and rising equities were all seen as positives for the financial sector.

As we noted in previous years, we observe that some active providers have reacted to the threat from passive products better than others, and offer products that are a clearly differentiated from passive products, or are sufficiently competitively priced. We think these providers are likely to be more protected from the forces of competition, and attempt to position the portfolio towards them. The active managers whose products provide only high-cost index-like exposure are those that struggled most in 2016, and are likely to face increasingly challenging conditions in future.

The best performers over the year (on a total return basis) were: Coronation Fund Managers (+60.3%), Raymond James (+21.3%), Liontrust (+19.9%), and State Street (19.8%). Coronation Fund Managers, based in South Africa, experienced a stabilisation in earnings after a sharp fall in 2015, plus enjoyed the partial recovery in the Rand. Raymond James saw from a sharp rise in investment banking revenues, plus steady growth in their securities commissions business. State Street remains a leader in asset servicing, its business model benefitting from the rise to US interest rates. Liontrust stood out as the one positive performer amongst UK retail managers owned in the fund, successfully raising assets both organically and via its acquisition of Alliance Trust Investments at a favourable price, announced towards the end of the year.

The worst performers in 2016 were: Och-Ziff (-46.9%), Henderson (-33.5%), Polar Capital (-32.6%) and Value Partners (-30.5%). Och-Ziff's progress continues to be clouded by the fall-out from an SEC investigation into federal bribery. Although the investigation was settled in September 2016, the company saw steady asset outflows through to the year-end, its total assets under management falling by 27% over the year. Henderson was one of the companies most affected by uncertainty following the Brexit vote in June, as concerns persisted that its UK onshore fund range will be vulnerable when the UK completes its departure from the EU. Polar Capital saw a sharp decline in assets in its flagship Japan strategy, offset to some extent by positive flows in other sectors, particularly technology and North America.



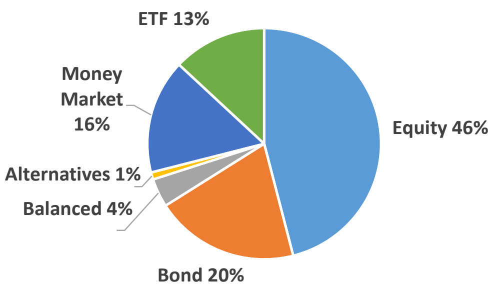
Source: ICI; Bloomberg; Guinness Asset Management

Outlook

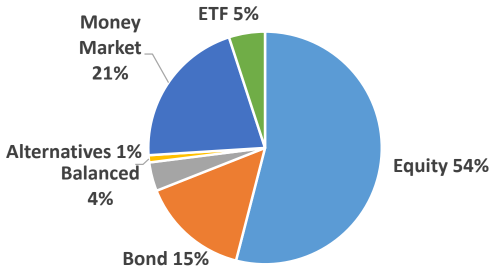
As we look ahead to the next few years in the asset management industry, it seems clear that developing industry trends will suit some firms more than others.

In particular, we can see that over the past five years, the lion's share of net flows, especially in the US, have gone to ETFs at the expense of active equity and fixed income products. The share of assets under management taken by ETFs has grown from 5% in the middle of 2007 to 13% today. We expect this trend to continue, at the expense of weaker traditional asset managers who over-charge for undifferentiated products.

AuM mix by asset class: Q4 2016



AuM mix by asset class: Q2 2007



Source: CSFB; Guinness Asset Management

2016 saw a record rotation from active to passive strategies, and we expect this rotation to continue (and peak) in 2017, catalysed by shifts in the US retail channel triggered by the DOL's Fiduciary Standard Rule. This is likely to result in US retail investors receiving a more "institutional" experience from their brokers, including lower fees, higher passive allocations and greater customisation.

Whilst the rotation from active to passive is overall a negative for the US retail asset management sector, it is offset by the significant positive of Trump's election victory. Trump's arrival in 2017 heralds an SEC board and Secretary of Labour (DOL) who are likely to be significantly more friendly to the industry than the outgoing administration; lower corporate tax rates will benefit cash tax payers, which the asset managers are one; and favourable tax reforms for the affluent will raise the level of assets available for investment.

Rising US interest rates have positive implications for the money market fund sector, which has essentially been in a bear market since the 2008/09 financial crisis. Money market funds should be in an increasingly advantageous position versus lower yielding bank deposits.

Meanwhile, asset managers in Europe face a tougher regulatory outlook, with UK managers tackling the additional uncertainty that Brexit brings. Most UK retail managers have already established offshore and onshore fund ranges; any that have not are working energetically on the problem.

As we see it, investment quality remains a key facet when defining a successful asset manager, whether active or passive. The definition of quality in asset managers has arguably expanded in scope in recent years, and we summarise it as "the ability of a manager to consistently meet stated and relevant objectives". For a smaller traditional asset manager, it may still mean the provision of high active share, alpha-generating portfolios. But for a passive provider, investment quality might be measured by the delivery of easily accessible, very low tracking-error, low cost ETF products.

With this backdrop in mind, we continue to believe that firms across the money management sector achieving one or a combination of the following will be able to grow their earnings most successfully:

1. **Effective, outperforming, active management**

Managers who can successfully offer products that outperform their benchmarks will continue to be the sector's most substantial revenue opportunity. These products will likely have a high active share (if compared to benchmarks), have a high tracking error, and will either be correlated (long-only equity/fixed income) or uncorrelated (e.g. alternative investments).

2. **Cost-efficient beta**

There will be significant growth in the use of easily-accessible passive products, notably ETFs, some of which will replicate benchmark returns at very low cost and others provide innovative beta products which investment managers choose to allocate to on a tactical basis. The winners in the low cost beta world will be those who can achieve significant scale, so maximising their operating leverage.

This divides into low-cost 'beta delivery' operations (e.g. Vanguard, BlackRock iShares) which rely on scale, and innovative beta products for which appetite is high (e.g. Wisdom Tree and Invesco Powershares).

3. Alternative asset managers

'Alternative' asset managers, such as private equity and hedge funds, face less threat from passives than large low active-share traditional managers, and therefore sit well placed to continue to grow assets as investors seek differentiated returns. Alternatives managers in the US also look particularly well placed during the Trump Administration, as likely changes to US tax policy (corporate reduction, personal reduction and tax repatriation), combined with looser regulation, should translate into higher returns.

4. Ancillary services to the money management industry

Whilst change is occurring to the composition of assets under management, it remains the case that the total level of AuM is growing at a faster pace than the growth in underlying returns. Since 1990, new investable companies and increasing household wealth have helped grow conventional assets under management by around 10x, versus world equity returns of around 4x. We expect this trend to continue. An expanding pool of assets provides an attractive environment for high quality asset managers, but also for the ancillary service providers to the industry, such as stock exchanges and custody banks.

5. Asset allocation expertise

Asset allocation is arguably the least well-developed of the capabilities which will be demanded from asset managers, but one which we expect to expand as an offering in the coming years. In particular, rewards will come to managers who can re-organise their existing funds and services into higher performing multi-asset products. We envisage these multi-asset offerings to be desirable to clients assembling traditional portfolios and those moving towards "outcome" oriented portfolios (e.g. retirement savings plans for the growing number of people tied to DC pension schemes rather than DB schemes; education funding plans).

6. Effective wealth management

The wealth management industry, particularly in Europe, remains a fragmented market with many subscale operators. However, consolidation is taking place, as pricing pressures, low interest rates and additional regulation prompt companies to exploit potential cost savings. This has been evident in the UK market, for example, where the Retail Distribution Review now prevents financial advisers from earning commissions from fund companies in return for selling investment products. As a result, scale of operation has become more important.

We believe that the most successful money management investments over the next five years will generally be companies that deliver investment quality to their clients, whether active traditional management, alternatives or passive; companies that provide helpful asset allocation services; well-run wealth managers; and well-run support services (e.g. custody banks; stock exchanges). Combining these themes with our stock selection process, which allows us to identify the equities of managers whose products are succeeding, leads us to the following portfolio positioning, expressed by theme (as at 31st December 2016):

	Theme	Example holdings		Weighting (%)
1	High active share	LIONTRUST	POLAR CAPITAL	26.8%
2	Alternatives	Blackstone	KKR	13.9%
3	Growth of ETFs/passive distribution	BLACKROCK	Invesco	6.8%
4	Wealth management	BREWIN DOLPHIN		11.1%
5	Traditional value	ALLIANCEBERNSTEIN	RAYMOND JAMES	21.6%
6	Support services	Nasdaq		6.9%
7	Asset management consolidators	AMG		3.7%
8	Secular shift in Europe to equities	VONTOBEL	AZIMUT	7.1%
9	Other (incl cash)			2.1%

At 31 December 2016 the P/E ratio of the Fund was 16.0x 2016 earnings. This sits at a significant discount to the broad market, with the S&P 500 trading on a 2016 P/E ratio of 20.6x earnings. Earnings for the portfolio fell by 18% between 2015 and 2016, but are expected to grow by 23% in 2017.

Fund P/E ratios versus the S&P 500 Index (31.12.16)

	'11	'12	'13	'14	'15	'16	'17
Fund P/E	21.3	17.5	12.7	12.1	13.1	16.0	13.0
S&P 500 P/E	23.2	23.1	20.9	19.8	22.3	20.6	17.1
Premium (+)/ Discount (-)	-8%	-24%	-39%	-39%	-41%	-22%	-24%

In the longer term we expect asset managers as a sector (and therefore the Fund) to outperform the broad market, due primarily to the ability of successful asset management companies to grow their earnings more rapidly than the broad market.

The Fund remains positioned to capitalise on the increasing value of successful companies in the sector.

Will Riley, Tim Guinness & Mark Hammonds
January 2017

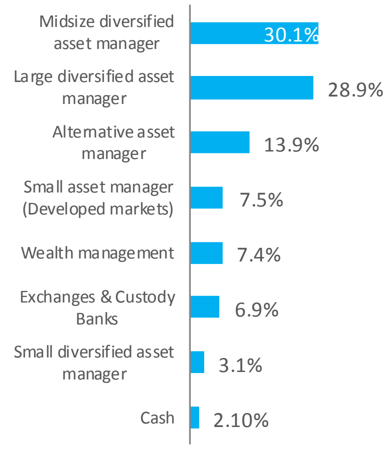
PORTFOLIO

31/12/2016

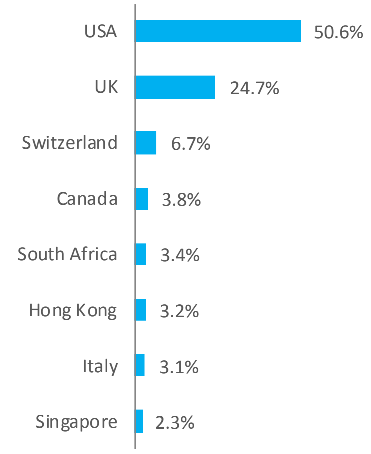
Fund top 10 holdings

Liontrust Asset Management	4.3%
Vontobel	4.0%
CI Financial	3.8%
AllianceBernstein	3.7%
Affiliated Managers Group	3.7%
Brewin Dolphin	3.7%
Ameriprise Financial	3.7%
Franklin Resources	3.7%
Rathbone Brothers	3.7%
Blackrock	3.7%
% of Fund in top 10	38.0%
Total number of stocks in Fund	30

Sector analysis



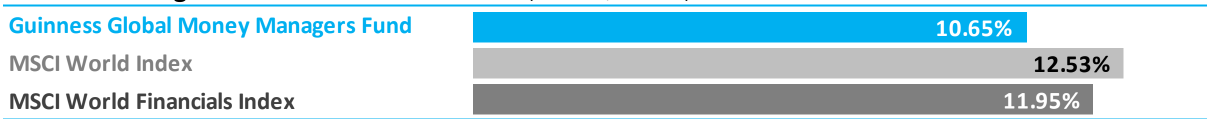
Geographic allocation



PERFORMANCE

31/12/2016

Annualised % gross total return from launch (X Class, in GBP)



Cumulative % gross total return (X Class, in GBP)	1 month	Year-to-date	1 year	3 years	From launch
Guinness Global Money Managers Fund	3.1	13.7	13.7	18.0	83.7
MSCI World Index	3.6	29.0	29.0	52.5	96.4
MSCI World Financials Index	5.1	35.0	35.0	52.8	90.7

Discrete years (X Class, in GBP)	Dec '12	Dec '13	Dec '14	Dec '15	Dec '16
Guinness Global Money Managers Fund	25.1	51.9	10.0	-5.7	13.7
MSCI World Index	11.4	25.0	12.1	5.5	29.0
MSCI World Financials Index	24.4	25.6	10.1	2.8	35.0

RISK ANALYSIS

31/12/2016

X Class, in GBP, annualised, weekly, from launch on 31.12.10, relative to the MSCI World Index	MSCI World	MSCI World Financials	Fund
Alpha	0	-1.57	-2.81
Beta	1	1.12	1.19
Information ratio	0	-0.08	-0.15
Maximum drawdown	-18.26	-28.87	-29.47
R squared	1	0.86	0.82
Sharpe ratio	0.59	0.46	0.38
Tracking error	0	6.45	8.19
Volatility	13.94	16.85	18.33

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, gross total return. Fund launch date: 31.12.10. **Fund X class**: Simulated performance based on actual returns of E share class (available from Fund launch), calculated in GBP. **See Note overleaf.**

Performance data note

The performance numbers displayed on the previous page are calculated in GBP (Sterling). Please note: The Fund's X class was launched on 15/02/2012. The performance shown is a simulation for X class performance being based on the actual performance of the Fund's E class, which has the same annual management charge as the X class, and has existed since the Fund's launch. The Fund's E class is denominated in USD but for the purposes of this performance data its performance is calculated in GBP. Hence the Fund's E Share class is used here to illustrate the performance of a GBP-based clean-fee (RDR-compliant) share class since the Fund's launch on 31.12.10.

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 recent developments in the asset management sector invested in by the Guinness Global Money Managers Fund. It may also provide information about the Fund's portfolio, including recent activity and performance. It contains facts relating to investment 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 Global Money Managers 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 companies involved in asset management and other related industries; it is therefore susceptible to the performance of that one sector, and can be volatile. Details on the risk factors are included in the Fund's documentation, available on our website.

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.