Guinness Asian Equity Income Fund

INVESTMENT COMMENTARY – March 2018

Launch date	**19.12.13**
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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.

	2015		2016		2017	
	USD	GBP	USD	GBP	USD	GBP
Fund	-4.4	1.2	7.5	28.2	36.5	24.6
Index	-9.4	-4.1	7.8	28.6	37.3	25.4
Sector	-8.6	-3.4	5.3	25.7	37.2	25.3

	YTD		1 year		From launch	
	USD	GBP	USD	GBP	USD	GBP
Fund	1.3	-0.6	27.2	14.8	60.0	89.9
Index	2.2	0.3	28.2	15.8	42.5	69.3
Sector	1.0	-0.8	27.4	15.1	40.7	67.1

Annualised % total return from launch

	USD	GBP
Fund	11.9%	16.5%
Index	8.8%	13.4%
Sector	8.5%	13.0%

Risk analysis (annualised, weekly, from launch)

	Index		Sector		Fund	
	USD	GBP	USD	GBP	USD	GBP
Alpha	0	0.0	0.7	1.3	4.8	4.9
Beta	1	1.0	0.9	0.9	0.8	0.8
Info ratio	0	0.0	-0.1	-0.1	0.5	0.5
Max drwdn	-29.1	-26.2	-26.7	-24.5	-24.3	-20.6
Tracking err	0	0.0	3.8	3.8	5.9	5.9
Volatility	14.9	15.3	13.4	13.6	12.4	13.9
Sharpe ratio	0.4	0.6	0.4	0.7	0.7	0.9

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 & Market

- The mini-correction we saw between 26th January and 9th February offered a useful reminder of the Guinness Asian Equity Income Fund's characteristics. The Fund (Y class, total return) outperformed by 2.5% the MSCI AC Pacific ex Japan Index which fell 7.2%/8.2% in GBP/EUR terms.

- The market wobble was triggered by US inflation and interest rate concerns which pushed US government bond yields higher. Financial assets world-wide have done well on ultra-low interest rates and so a reversal is likely to put pressure on share valuations.

- The market consensus expects synchronised global economic growth with all regions (US, Europe and Emerging Markets) contributing for the first time since the financial crisis. Earnings forecasts continue to be positive and have been supported by a solid results reporting season so far.

- The best performing markets were south-east Asia (Thailand, Malaysia, Singapore and Indonesia) and Australia. China was a notable underperformer. Heath Care, Consumer Staples and Utilities were the best performing sectors. Telecoms continued their wretched run, underperforming the market by 2.5%.

- The Fund continued to march to its own beat with outperforming names from China, Taiwan and Hong Kong as well as Singapore and Thailand which operate in the Technology, Energy, Financials, Consumer Discretionary and Health Care sectors. We have minimal exposure to Consumer Staples and no exposure to Utilities.

- At the end of the month the Fund was attractively valued at 12.1x 2018 earnings and at a 9.5% discount to the MSCI AC Pacific ex Japan Index price /earnings multiple of 13.3x 2018 earnings.

Events in February

- We remain of the view that Central Banks in both the US and Europe wish to move toward a 'normalisation' of monetary conditions and we believe the US Federal Reserve is at the forefront. The recent testimony by the new chair of the Federal Open Markets Committee (FOMC) gave extra force to that, in our opinion.

- In China, the big political development was the move by Xi Jinping to remove the two-term (10 year) Presidential limit. This can be seen as a formalisation of the political reality, but it is a major step nonetheless.

- The Winter Olympics in South Korea saw a thawing of relations between North and South. The US retains its firm stance against North Korea but it is evident that the South, due to proximity, is much more willing to engage.

- At the beginning of March US President Trump announced a plan to impose tariffs on steel and aluminium on all imports into the US whether from Europe or Asia. This was a surprise to the Treasury, Pentagon, Republicans, Democrats and to everyone else. While the EU suggested a readiness to retaliate, China re-emphasised it has no desire for a trade war.

Outlook

- US moves on trade, first on washing machines and solar panels then on steel and aluminium, may be harbingers of more wide-ranging protectionist moves. America First could hit global growth and then hit US growth, affecting Federal Reserve forecasts and US interest rates.

- Global and Asian regional economic growth looks positive for the year ahead and this is supportive for the earnings outlook. But there are also factors we need to consider:

- China is expected to step up its efforts to cut debt. The government forecasts 6.5% growth, dropping the "or faster if possible" rider. Money supply growth is forecast to be similar to last year and the fiscal deficit is forecast to narrow to 2.6% of GDP. The combined effect is likely to be slower GDP growth. For investors this means staying away from companies that are sensitive to macro-economic policy and focussing on businesses that stand on their own two feet.

- We expect to see US interest rates move toward normalisation. Vulnerable stocks include those higher-yielding shares whose dividends are not growing (so-called 'bond proxies') and high-priced growth stocks whose valuations depend on high growth in the long term.

- The best defences: focus, as we do, on those companies which can sustain dividend growth and on those companies for whom future growth prospects make up a lower proportion of the valuation (i.e. Growth at Reasonable Price).

Discussion

While trade-related issues move higher up the agenda there is better news out of **Korea**. The signs of a rapprochement between North and South Korea at the Winter Olympics has been followed up by a formal meeting between Kim Jong Un and South Korean ministers. At this meeting North Korea held open the possibility that it may be willing to shelve its nuclear ambitions in return for guarantees from the US over its security (and no doubt an easing of sanctions). It is always near impossible to identify exact motives behind North Korea's actions (although we can certainly speculate), but the news has been warmly greeted so far.

The stock market in **India** remains challenging. The mood can best be summed up as Buy the hope, Sell the reality. Most top-down observers are very excited by the reform moves by Modi and the radical actions (de-monetisation, a goods and services tax, a recapitalisation of state banks) coupled with some of the best economic growth in the region. The problem is that not everything is moving the same way: the discovery of substantial fraud in one of the state banks, a capital gains tax on stocks, the refusal to share stock exchange pricing data with overseas platforms to enable pricing of derivatives are all reminders that much remains to be done and not everyone is signed up to the plan. The fact that Indian shares are still seeing downgrades to earnings forecasts while also being some of the most expensive in Asia and Emerging Markets also helps explain India's significant underperformance this year.

In **Thailand**, consumer confidence continues to rise and is now at a three-year high. This is positive for our holding in Tisco Financial. The results reported in January included a modest outlook for loan growth following the acquisition of Standard Chartered Bank's Thai consumer business and indicated plenty of positives on loan quality and provisioning. The 45% increase in the dividend on 20% profit growth and a rise in the payout ratio from 40% to 65% puts the shares on a 4% yield.

The PTT group performed very strongly in February following news of a share split by the parent, which is held in the Fund. PTT is Thailand's main energy business made up of natural gas supplier PTT, oil exploration business PTT Exploration & Production and a petrochemicals business, PTT Global Chemical. We like PTT because of the low volatility in its earnings, primarily due to its long-term gas supply contracts to Thailand's electricity generators, and higher oil prices have been a positive contributor. We think PTT's share price discounts $56 oil prices at present. The recent results came in ahead of expectations and included a 25% increase in the dividend.

Last month we wrote positively of **Singapore** and improvements in consumer confidence. In February we have seen continued evidence of this; the manufacturing sector has sustained its upswing not only in technology but also in commodity-sensitive areas such as oil services and in general manufacturing. This broadening expansion supports employment and expectations of wage inflation, which in turn sets the scene for some monetary tightening in Singapore. This is beneficial to the banks and to the Fund's holding in DBS in particular which was the best performing stock in the local market index and the Fund's third best performer in February. We also hold two real estate investment trusts (REITs) in Singapore, Ascendas and CapitaMall Trust, which could be seen to be at risk in a rising interest rate environment. They are focused on industrial properties and commercial properties respectively. We are very conscious that any company which fails to grow its dividend is at risk and liable to be treated by the market as a bond proxy whose dividend value will be eroded by rising rates. However, both Ascendas and CapitaMall Trust have shown an ability to grow their dividends over time and we expect them to be better able to preserve the value of the income stream and thus their capital value in this environment.

China had a weak month relative to the region but it followed an exceptionally strong month in January. The big political news was the formalisation of Xi Jinping's unassailable leadership position with the removal of the two-term limit on the Presidency. Though the timing of the announcement was perhaps a surprise, the move to scrap the limit was virtually confirmed in October 2017 when the new politburo was unveiled with no apparent heir to

Xi. His predecessors ruled in accordance with Deng's famous motto "hide your strength, bide your time", but Xi himself apparently aims to govern differently. He seems to want China to become much more prominent in foreign policy; to develop trade and infrastructure links through the Belt and Road Initiative; and to become a leader in technologies such as electric vehicles, aerospace and cybersecurity.

AAC Technologies was the strongest stock over the period. AAC is known for its speakerboxes and haptics in smartphones. The company is now diversifying into new areas such as metal casings for smartphones and hybrid lenses using a proprietary production technique. The share price was weak towards the end of 2017 due to 1) weaker-than-expected sales of the iPhone X, for which AAC is a supplier, and 2) a smartphone inventory correction in China, which affected most firms in the supply chain. We hold AAC because we think it has innovative product development capabilities which give the company an edge; for example, Samsung's new GS9 phone incorporates stereo sound and is 1.4x louder, and AAC is one of two suppliers. China smartphone maker Vivo launched its new concept phone which boast a 98% screen-to-body ratio with hidden in-display speaker system called 'Screen SoundCasting'. The all-screen design will need either a compact speaker grille or an under-display speaker. Either solution will lead to a meaningful average selling price (ASP) increase.

Weaker stocks in February include China Merchants Bank, Delta Electronics Thailand, China Mobile, LPN Development and JB Hi-Fi. China Merchants Bank has been one of our best performers over the past 18 months and its reversal during the month was related to broader market weakness and tightening rules on deleveraging rather than anything specific to the bank. China Mobile had a weak month on rumours, subsequently confirmed, of plans to cut mobile internet service fees across the sector by the elimination of domestic roaming charges. Delta Electronics Thailand was weak on slower earnings in the last quarter of 2017, but sales are expected to pick up in 2018, especially from the autoparts sector. In the short term, Thai baht strength is a headwind. JB Hi-Fi had a weak month after management guided profit growth over the next six months would be slower than sales growth due to increasing investment, especially in on-line distribution.

Summary and conclusion

The portfolio is trading on a price/earnings multiple basis at a 9% discount to the market as measured by the MSCI AC Pacific ex Japan Index. This index is in turn trading at a wider discount to developed markets than its ten-year average. A combination of above-average companies, in our opinion, paying above-average dividends and trading on a below-average valuation seems to us to be an attractive one.

Edmund Harriss and **Mark Hammonds** (portfolio managers)
Sharukh Malik (analyst)

Data sources

Fund performance: *Financial Express, gross total return*

Index and stock data: *Bloomberg*

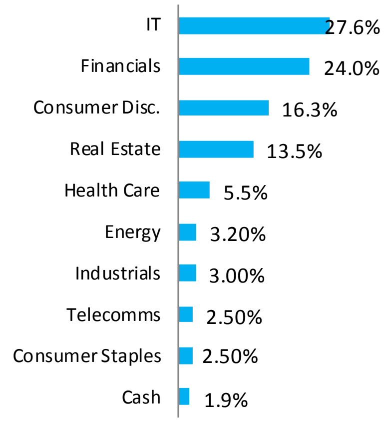
PORTFOLIO

28/02/2018

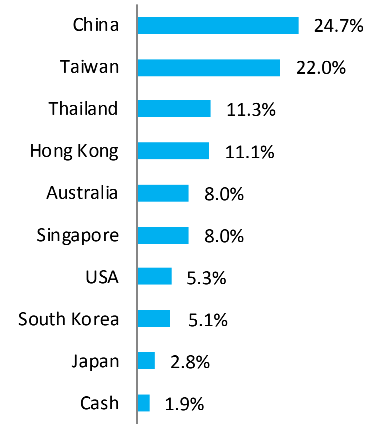
Fund top 10 holdings

AAC Technologies	3.3%
PTT Public Company	3.2%
Yangzijiang Shipbuilding	3.0%
St. Shine Optical Co	2.9%
Catcher Technology	2.9%
Elite Material	2.9%
Novatek Microelectronics	2.9%
Link REIT	2.9%
Luk Fook Holdings	2.8%
Relo Holdings	2.8%
% of Fund in top 10	29.5%
Total number of stocks in Fund	36

Sector analysis



Geographic allocation



PERFORMANCE

28/02/2018

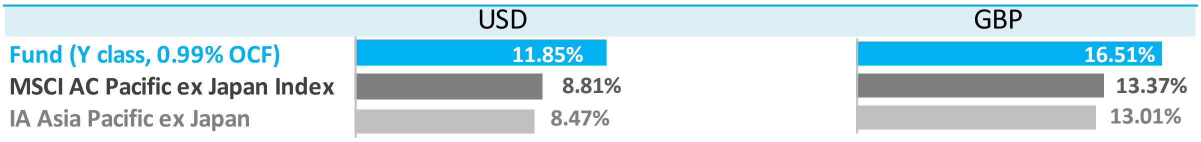
Discrete years % total return

	Feb '14		Feb '15		Feb '16		Feb '17		Feb '18	
	USD	GBP	USD	GBP	USD	GBP	USD	GBP	USD	GBP
Fund (Y class, 0.99% OCF)	-	-	-	-	-11.8	-2.2	23.7	38.6	27.2	14.8
MSCI AC Pacific ex Japan Index	-0.7	-10.0	7.0	16.1	-20.3	-11.6	28.5	43.9	28.2	15.8
IA Asia Pacific ex Japan	0.5	-9.0	7.4	16.5	-18.8	-10.0	24.0	38.9	27.4	15.1

Cumulative % total return

	1 month		Year-to-date		1 year		3 years		From launch	
	USD	GBP	USD	GBP	USD	GBP	USD	GBP	USD	GBP
Fund (Y class, 0.99% OCF)	-3.3	-0.2	1.3	-0.6	27.2	14.8	38.8	55.6	60.0	89.9
MSCI AC Pacific ex Japan Index	-4.5	-1.5	2.2	0.3	28.2	15.8	31.3	47.2	42.5	69.3
IA Asia Pacific ex Japan	-5.0	-1.9	1.0	-0.8	27.4	15.1	28.1	43.7	40.7	67.1

Annualised % total return from launch



Risk analysis - Annualised, weekly, from launch on 19.12.2013

28/02/2018	Index		Sector		Fund	
	USD	GBP	USD	GBP	USD	GBP
Alpha	0.0	0.0	0.7	1.3	4.8	4.9
Beta	1.0	1.0	0.9	0.9	0.8	0.8
Information ratio	0.0	0.0	-0.1	-0.1	0.5	0.5
Maximum drawdown	-29.1	-26.2	-26.7	-24.5	-24.3	-20.6
R squared	1.0	1.0	0.9	1.0	0.9	0.9
Sharpe ratio	0.4	0.6	0.4	0.7	0.7	0.9
Tracking error	0.0	0.0	3.8	3.8	5.9	5.9
Volatility	14.9	15.3	13.4	13.6	12.4	13.9

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: 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.

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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: Link Fund Manager Solutions (Ireland) Ltd, 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.

Singapore

The Fund is not authorised or recognised by the Monetary Authority of Singapore ("MAS") and shares are not allowed to be offered to the retail public. The Fund is registered with the MAS as a Restricted Foreign Scheme. Shares of the Fund may only be offered to institutional and accredited investors (as defined in the Securities and Futures Act (Cap.289)) ('SFA') and this material is limited to the investors in those categories

Telephone calls will be recorded and monitored.