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.

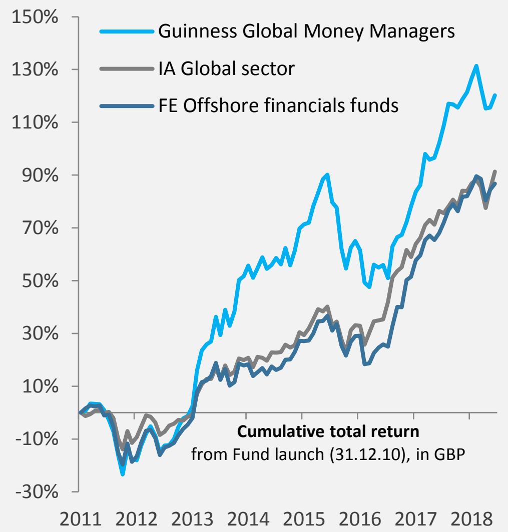
INVESTMENT COMMENTARY – July 2018

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.

Performance **30.06.2018**



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 (X class, 1.24% OCF), bid to bid, gross total return.

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2015: BEST FUND OVER 3 YEARS

EQUITY SECTOR BANKS & OTHER FINANCIALS

What does our "top 35" study tell us about the sector?

In this month's brief, we update our annual study of the world's 35 largest listed "pure play" asset managers, to see what we can learn from trends developing in the sector over the past five years, and a closer look at their recent activity.

We also discuss our Fund performance over the second quarter of 2018, and consider the outlook.

Second quarter performance

World equities posted a gain over the quarter, with the MSCI World Index (the benchmark for the fund) rising by 1.9% (in USD). Global financials underperformed, with the MSCI World Financials Index falling by 4.1% over the period. The fund fell by 3.9% over the quarter.

The second quarter saw an even split of positively and negatively performing stocks in the portfolio, with mid and smaller cap asset managers generally faring better than the large caps. Among the best performers were:

- **Polar Capital (+32.2%).** Polar, which we have held since the inception of the fund, is enjoying a period of positive expansion, under the direction of new CEO, Gavin Rochussen. In June, the company announced the hire of an experienced emerging markets team from Nordea, which has been well received. Led by Jorry Rask Noddekaer, the Nordea team were previously responsible for over USD$6bn of assets under management. The company saw AuM increase to £12bn in the year to 31 March 2018, an increase of 33% versus the previous year. Positive flows have continued in April and May, and have been particularly strong in Polar's Global Technology strategy. Success in asset raising has translated into improved profitability, with operating profit up by 33% in the year to March 2018.

- **KKR (+23.4%).** The most significant news for private equity firm KKR came in May, with the announcement that it would convert from a partnership to

Tel: +44 (0) 20 7222 5703
Email: info@guinnessfunds.com
Web: guinnessfunds.com

a corporation. The move is designed to capitalise on tax reforms enacted by the Trump administration, and is likely to broaden KKR's shareholder base, since some investors are unable to invest in partnership structures. KKR's move follows Ares Management's conversion on 1 March 2018, becoming the first major asset manager to make the switch. Generally, alternative asset firms that derive a larger share of revenue from management fees (which includes KKR) have a greater incentive to change. KKR became a corporation on 1 July. Longer term, we like KKR strategy of reinvesting a high proportion of profits into its balance sheet, which helps to compound earnings and book value through the cycle.

- **Vontobel (+21.2%).** We purchased Vontobel in the fund at the start of 2017, attracted by the company's track record in wealth management and ambitions for growth. In May, Vontobel announced the acquisition of La Roche Privatbank AG, purchased from Raiffeisen Switzerland. La Roche brings CHF16.8bn of advised client assets, which will boost Vontobel's advised client assets by more than 30%. We believe that the similar client profile that La Roche enjoys to Vontobel (90% of AuM are in client wealth bands of >CHF 1bn; most are in Switzerland) will help to make the deal a success.

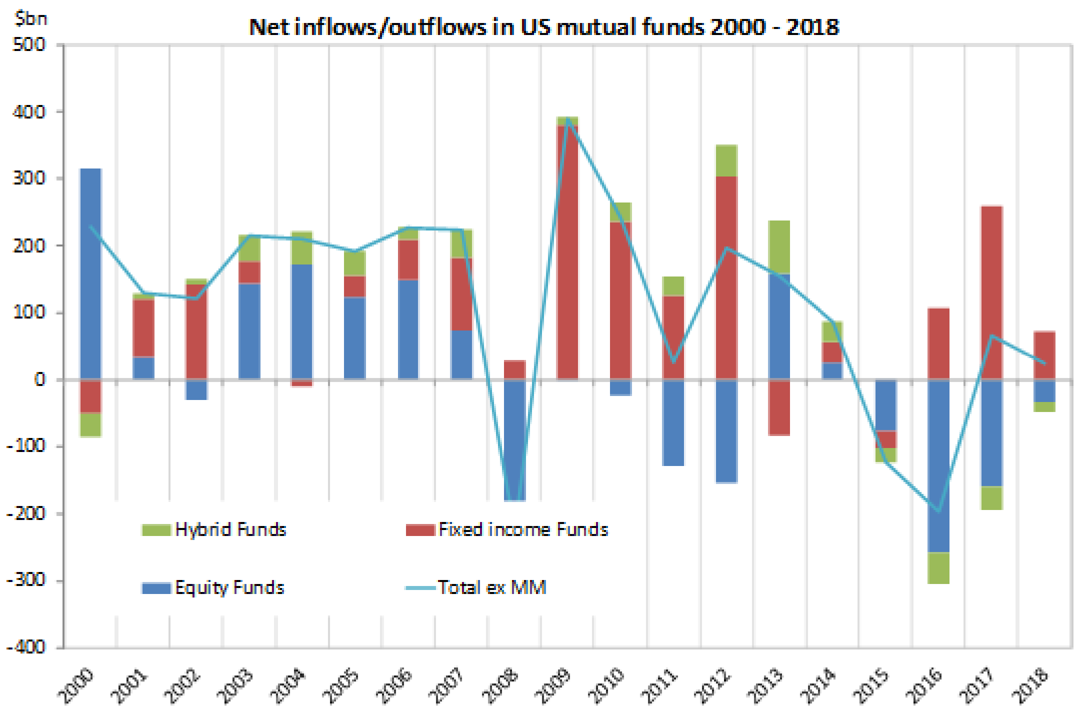
Weaker performers over the period included:

- **Coronation Fund Managers (-35.4%).** Total AuM at Coronation dipped by 4.2% over the six months to March 2018. The highest proportion of outflows came in the South African institutional division, where the local pensions industry continues to see structural outflows, given weak employment numbers and retrenchments in the formal employment sector. This leaves total AuM for Coronation at just under USD$50bn, close to the 2014 peak ($52bn). After the recent share price fall, Coronation's equity offers a 7.7% dividend yield, which is more than three times covered.

- **Affiliated Managers Group (-21.4%).** AMG operates as a global, diversified asset management firm, taking significant equity stakes in independent investment management boutiques. At the end of March 2018, AuM were around $830bn, spread across more than 550 underlying investment products. The company has maintained positive net inflows from alternatives and multi-asset products, but this has been outweighed in recent months by net outflows from global equities and US equities. Still, AMG generates a high level of free cashflow (around $1bn, representing a c.12% FCF yield), and for the time that the share price remains depressed, we expect the company to accelerate its share buyback programme.

- **Invesco (-16.1%).** Operating margins at Invesco have been depressed in recent months thanks to a rise in the company's core expenses, driven by several significant acquisitions (ETF providers Guggenheim & Source, digital platform Gemstep). Operating margin for Q1 was reported at around 26%, versus around 28% for 2017. However, the deals mean that Invesco has now become the world's fourth largest ETF manager, and its presence in Europe and Asia should create organic growth in excess of US peers.

Within the asset management sector, data for US mutual fund flows (which we treat as a proxy for global flows) indicated record outflows from equity funds in 2016. Equity outflows continued in 2017, particularly in the second half of the year, but overall the picture was less severe than the year before. However, fixed income funds reported strong inflows across all four quarters in 2017, resulting in overall net flows (equity, fixed income and hybrid combined) swinging from negative in 2016 to positive in 2017. Net flows so far in 2018 have been positive.



Source: Bloomberg; Guinness Asset Management

Trends in the sector over the last five years

In this quarter's outlook, we update our annual study of the 35 largest listed "pure play" asset managers in the world, to see what we can learn from trends developing in the sector over the past five years, and a closer look at their activity over the past twelve months.

The list of the world's 35 largest listed "pure play" asset managers companies ranges in AuM terms from the smallest, Platinum Asset Management, running $17bn of assets, to Blackrock, running $6.3trn of assets. The list is skewed towards the US, with 20 of the 35 being US based, 8 in Europe (including 4 in the UK) and 7 based elsewhere. In reality, of course, the domicile of the business hides the fact that many of these companies have global operations and client bases.

The majority of the list are long-only equity, fixed income and money market specialists, but it does include six private equity firms, all listed in the US. Of the firms specialising in equities, two (Blackrock and Invesco) have made significant strides into the ETF market, whilst a handful of others are looking to expand in that direction.

Our main findings are:

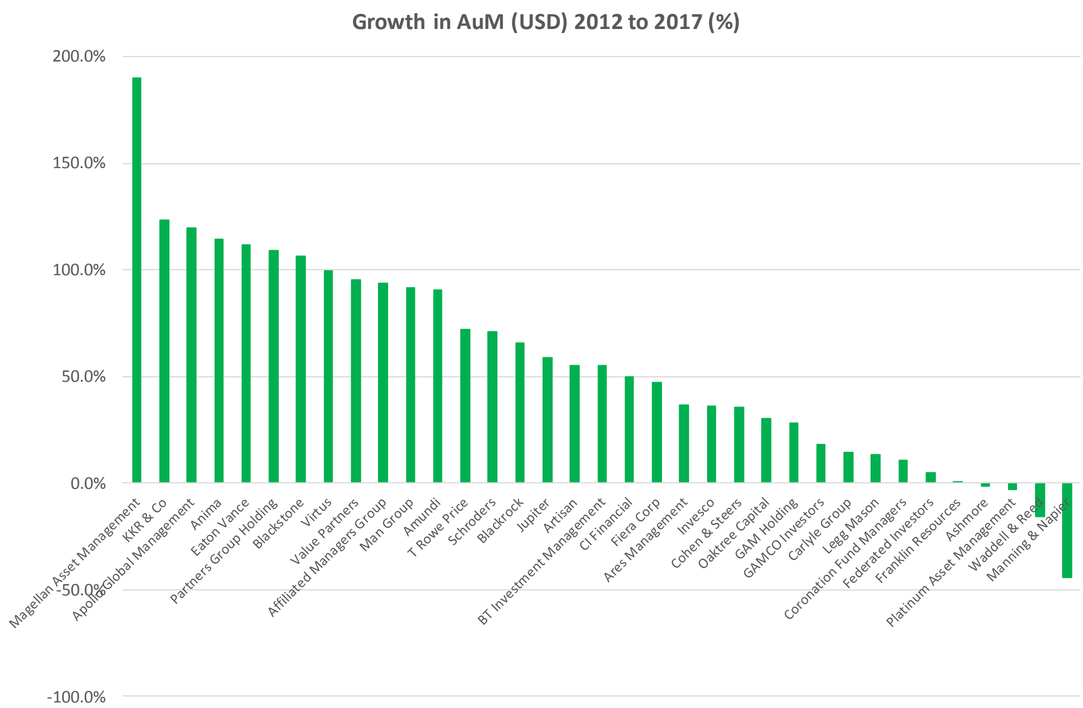
- **Assets under management (per share), for many firms, continue to grow handsomely**. This has of course been well supported by market appreciation. There is a tail of managers, however, who have seen their businesses decline.
- Despite the penetration of passives/ETFs into the market**, the majority of companies have achieved net inflows**. The rotation from active investments to passives/ETFs is mainly affecting the traditional, underperforming, low-active share US asset managers, with non-US firms doing better.
- **2017 saw a much stronger net inflow picture than 2016**. Around two-thirds of the group reported net inflows in 2017, versus around half in the year before.

- **Net revenue margins have declined, on average, by about 10% since 2013**. Operating margins are fairly steady, up in 2017 versus 2016 and higher than five years ago.
- Cashflow return on investment (CFROI) for the group remains elevated versus the broad market.
- The dividend yield for the asset management sector versus the broad market sits at a significant premium – around 4% versus 2.5% for the MSCI World.

How have assets under management grown over the last 5 years?

Since the start of 2013, the MSCI World (which we use as a proxy for equity returns) has produced a price return of 57% and a total return of 79%, whilst the IBOXX Corporate Bond Index (which we use as a proxy for fixed income returns) has produced a total return of 20%.

Unsurprisingly then, average growth in assets under management over this period has been strong, with assets rising on average by 57%. However, this statistic masks a very wide range of outcomes for the 35 participants, with some managers doubling their assets, others seeing declines of up to 44%.



Source: Bernstein; Bloomberg; company reports; Guinness Funds

How does this compare to net flows?

Given that the level of assets being managed by each firm has enjoyed the tailwind of rising markets, analysis of the underlying flows of each business (being the net of subscriptions and redemptions) is perhaps more instructive.

Looking first at the group as a whole, we can see that in each of the four years from 2013 to 2015, around two-thirds to three-quarters of the top firms experienced net inflows. 2016 was then an unusual year, with the number of firms enjoying net inflows falling to about half of the group. This worsening of flows for the sector clearly spooked the market, with asset management firms generally de-rating and underperforming the broader equity sector. However, 2017 saw a return to 2012-2015 behaviour, with 65% of the top firms enjoying net inflows.

Asset managers: net inflows as % of closing AuM, 2013 to 2017

	Net inflow as % of closing AuM					
Company	**2013**	**2014**	**2015**	**2016**	**2017**	**Average**
Magellan Asset Management	12.2%	28.9%	14.2%	10.1%	7.9%	14.6%
Partners Group Holding	12.8%	11.2%	17.5%	15.6%	13.9%	14.2%
Value Partners	15.3%	18.1%	31.0%	-11.6%	-2.3%	10.1%
Blackstone	11.4%	6.9%	10.8%	7.7%	13.1%	10.0%
KKR & Co	20.4%	2.2%	1.2%	9.9%	13.9%	9.5%
Anima	8.5%	16.0%	12.6%	6.8%	1.5%	9.1%
Eaton Vance	12.4%	1.0%	5.6%	6.2%	11.2%	7.3%
Jupiter	4.4%	2.7%	6.0%	2.7%	14.1%	6.0%
Amundi	1.2%	3.4%	7.5%	5.8%	7.1%	5.0%
Blackrock	3.2%	4.5%	3.2%	4.4%	7.1%	4.5%
Apollo Global Management	10.3%	5.4%	-2.1%	7.4%	0.6%	4.3%
Schroders	3.6%	9.4%	4.3%	0.3%	2.5%	4.0%
Man Group	-6.3%	6.1%	0.4%	2.4%	15.8%	3.7%
Affiliated Managers Group	9.4%	4.0%	-0.5%	1.2%	0.7%	3.0%
Ares Management	5.8%	1.6%	5.9%	1.3%	0.0%	2.9%
Invesco	3.2%	1.5%	2.0%	2.1%	1.4%	2.0%
CI Financial	4.7%	4.2%	3.0%	-5.6%	-0.9%	1.1%
GAM Holding	-2.2%	2.0%	2.6%	-5.5%	7.2%	0.8%
Federated Investors	-0.8%	0.2%	0.5%	1.1%	1.8%	0.6%
Carlyle Group	6.5%	-1.2%	-0.5%	-5.8%	2.5%	0.3%
Coronation Fund Managers	13.6%	6.0%	-2.3%	-9.1%	-7.6%	0.1%
Legg Mason	-0.5%	2.2%	-1.6%	-0.2%	0.4%	0.1%
T Rowe Price	-2.1%	0.5%	0.2%	-0.4%	1.7%	0.0%
Fiera Corp	2.4%	-1.3%	0.3%	-2.2%	-1.2%	-0.4%
Cohen & Steers	-4.3%	-4.1%	-1.8%	1.3%	6.7%	-0.4%
Virtus	17.8%	-2.1%	-11.1%	-9.9%	-0.4%	-1.2%
Oaktree Capital	-5.7%	3.3%	10.5%	-4.8%	-10.7%	-1.5%
Artisan	9.7%	0.8%	-5.4%	-4.8%	-8.4%	-1.6%
BT Investment Management	-3.3%	-4.8%	-6.2%	-8.4%	7.3%	-3.1%
GAMCO Investors	4.5%	-2.4%	-10.5%	-7.3%	-4.3%	-4.0%
Ashmore	17.3%	-10.0%	-16.1%	-14.3%	2.5%	-4.1%
Franklin Resources	3.4%	-0.6%	-5.3%	-11.1%	-7.8%	-4.3%
Platinum Asset Management	0.0%	-2.1%	0.4%	-6.6%	-15.9%	-4.8%
Waddell & Reed	8.8%	-2.8%	-11.1%	-24.2%	-14.2%	-8.7%
Manning & Napier	-5.5%	-1.5%	-23.0%	-22.7%	-35.0%	-17.6%

Source: company reports; Guinness Funds

Whilst the data shows that majority of firms have achieved net inflows over this period, we would make a couple of further observations. First, we can see a geographical split here, with a skew towards the US (8 out of 12) in terms of the firms experiencing average net outflows. Second, the US firms that have achieved net inflows are biased towards ETF franchises or that specialise in alternative investments (mainly private equity). The rotation from active investments to passives, including ETFs, is therefore mainly affecting one category of firm: the traditional, underperforming, low-active share US asset managers. Firms outside the US, and those with products that are differentiated versus passives, generally continue to thrive.

Are firms becoming more or less profitable?

Common wisdom might tell you that with the trend towards lower-cost passives in recent years, the profitability of asset management firms is under some pressure.

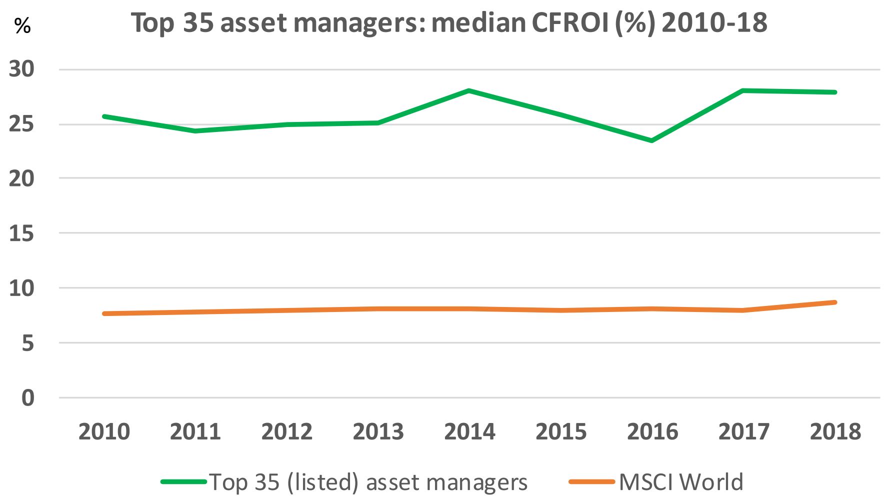
Over the past five years, we estimate that net revenue margins have fallen, in total, by around 10%. However, operating margins have held up well:

	2013	2014	2015	2016	2017
Operating margin - **median**	30.6%	37.8%	33.6%	32.1%	35.1%
Operating margin - **average**	35.1%	39.5%	45.0%	32.7%	36.6%
Operating margin ex private equity - **median**	29.9%	35.2%	33.6%	32.1%	35.0%
Operating margin ex private equity - **average**	32.3%	38.2%	35.0%	33.2%	36.4%

Source: Bernstein; company reports; Guinness Funds

As the table shows, operating margins in the sector have generally improved since 2013, and picked up in 2017 after dipping in 2015/16. How has this result been created? It would seem that the slight erosion in pricing that the average firm has experienced over the last 5 years has been offset by growing revenues as a result of net inflows and market appreciation.

Considering the overall profitability of asset management firms over a longer time horizon, we can see that cashflow return on investment (CFROI), as measured by the CSFB HOLT system, shows asset managers maintaining a very high level of return in 2017 and 2018, in line with the peak of 2014/15:



Source: CSFB; company reports; Guinness Funds

Median asset management CFROIs have ranged between 23% (in 2010) and 28% (2014), but remain consistently more than double the CFROI of the MSCI World.

An important component of returns generated by money management firms is their dividend. Companies in this sector tend to generate significant excess cash, and usually, Boards are not shy of returning the cash to shareholders in the form of dividends. The top asset management firms currently deliver a dividend yield of 4.1%, well ahead of the MSCI World at 2.5%.

Dividend yield (%)	2013	2014	2015	2016	2017	2018
Top 35 asset managers	2.36	3.13	3.60	3.83	3.35	**4.11**
MSCI World	2.09	2.09	2.40	2.30	2.29	**2.48**
Premium to MSCI World yield (%)	13%	50%	50%	67%	46%	**66%**

Source: CSFB; company reports; Guinness Funds

There have been times in recent history, for example in 2013, where higher valuations for asset managers versus broader equities drove the dividend yield down close to the yield of the broad market. However, sustained underperformance since 2014, at a time when asset managers were still growing their dividends, leaves the sector's yield today at a significant premium.

Examining the fortunes of asset management sector over the last 5 years highlights that for some companies, particularly the most entrenched traditional US asset managers, the rise of passives has eroded assets and profitability. However, for the majority, net inflows, stable margins and growing revenues have been achieved. Market conditions have undoubtedly helped, but we continue to expect the industry to adapt and most participants to grow. Remember also that this has been a study focusing on the large-caps, behind which there are numerous small to mid-cap firms, many of whom are nimbly and energetically expanding their market share and providing healthy returns to shareholders.

Valuation of the Guinness portfolio

At 30 June 2018, the P/E ratio of the Fund was 13.3x 2018 earnings. This sits at a significant discount to the broad market, with the S&P 500 trading on a 2018 P/E ratio of 17.3x earnings. Earnings for the portfolio are expected to grow by 6% in 2018. The portfolio currently offers a gross dividend yield of around 4%, which is rolled up in the fund.

Fund P/E ratios versus the S&P 500 Index (30.06.18)

	'10	'11	'12	'13	'14	'15	'16	'17	'18
Fund P/E	25.0	26.9	21.8	16.3	16.0	16.7	20.7	14.1	**13.3**
S&P 500 P/E	32.5	28.2	28.1	25.3	23.4	27.1	25.6	21.8	**17.3**
Premium (+)/ Discount (-)	-23%	-5%	-22%	-35%	-32%	-39%	-19%	-35%	**-23%**

Source: Standard & Poor's, Guinness Asset Management.

In general, we believe that the most successful money management investments over the next few years will 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). The Fund remains positioned to capitalise on the increasing value of companies across these themes.

Will Riley, Tim Guinness & Mark Hammonds
July 2018

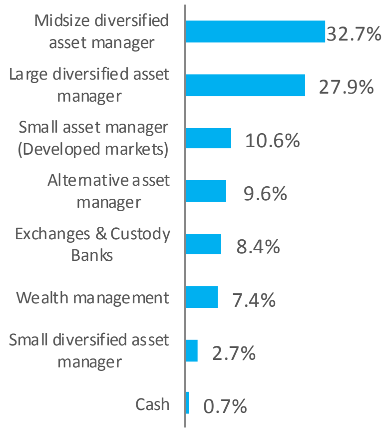
PORTFOLIO

30/06/2018

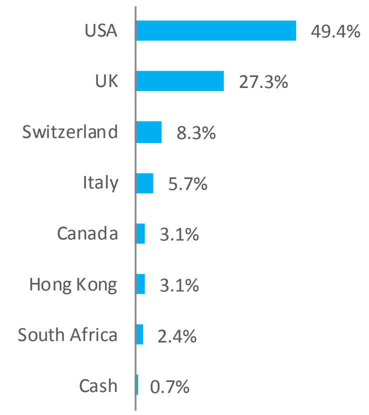
Fund top 10 holdings

Polar Capital	5.8%
KKR	5.1%
Liontrust Asset Management	4.8%
Vontobel	4.8%
T Rowe Price	4.7%
Nasdaq	4.5%
AllianceBernstein	4.4%
Raymond James Financial	4.1%
Blackstone Group	4.1%
State Street	3.9%
% of Fund in top 10	46.1%
Total number of stocks in Fund	29

Sector analysis



Geographic allocation



PERFORMANCE

30/06/2018

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	-0.2	-3.0	5.3	22.3	119.8
MSCI World Index	0.8	3.2	9.9	54.7	135.8
MSCI World Financials Index	-1.0	-3.5	3.4	48.2	114.3
Financial Express - Financial Sector average	-0.5	-0.8	5.7	32.1	72.1

Discrete years (X Class, in GBP)	Jun '14	Jun '15	Jun '16	Jun '17	Jun '18
Guinness Global Money Managers Fund	22.6	13.3	-16.0	38.2	5.3
MSCI World Index	10.6	10.9	15.1	22.3	9.9
MSCI World Financials Index	7.6	11.4	2.6	39.7	3.4
Financial Express - Financial Sector average	4.7	11.4	-6.3	33.2	5.7

RISK ANALYSIS

30/06/2018

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	-2.16	-1.79
Beta	1	1.11	1.17
Information ratio	0	-0.20	-0.06
Maximum drawdown	-18.26	-28.87	-29.47
R squared	1	0.85	0.81
Sharpe ratio	0.59	0.40	0.42
Tracking error	0	6.49	7.86
Volatility	13.39	16.16	17.35

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 Performance data note on the next page.**

Past performance should not be taken as an indicator of future performance. The value of investments and any income arising from them can fall as well as rise.

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: 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.

Telephone calls will be recorded and monitored.