Guinness Emerging Markets Equity Income Fund

INVESTMENT COMMENTARY – June 2019

Launch date	**23.12.2016**
Team	**Edmund Harriss** (manager) **Mark Hammonds** (manager) **Sharukh Malik** (analyst)

Aim

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

Performance 31/05/2019

Fund	Guinness Emerging Markets Equity Income (Z)
Index	MSCI Emerging Markets Index
Sector	IA Global Emerging Markets

	2016		2017		2018	
	USD	GBP	USD	GBP	USD	GBP
Fund	-	-	38.4	26.4	-14.8	-9.5
Index	11.6	32.6	37.8	25.4	-14.3	-9.3
Sector	9.7	30.8	36.2	24.4	-16.9	-11.8

	YTD		1 year		From launch	
	USD	GBP	USD	GBP	USD	GBP
Fund	6.7	7.8	-7.1	-1.9	27.1	23.6
Index	4.1	5.2	-8.7	-3.6	25.3	21.9
Sector	6.2	7.3	-7.8	-2.7	23.4	20.0

Annualised % total return from launch

	USD	GBP
Fund	10.4%	9.1%
Index	9.7%	8.5%
Sector	9.0%	7.8%

Risk analysis (annualised, weekly, from launch)

	Index		Sector		Fund	
	USD	GBP	USD	GBP	USD	GBP
Alpha	0.0	0.0	0.0	0.4	3.2	2.3
Beta	1.0	1.0	1.0	0.9	1.0	0.9
Info ratio	0.0	0.0	0.0	-0.2	0.5	0.2
Max drwdn	-24.6	-16.6	-24.6	-16.6	-23.0	-14.8
Tracking err	0.0	0.0	0.0	3.8	6.1	6.3
Volatility	14.8	13.8	13.8	12.3	13.9	13.5
Sharpe ratio	0.3	0.3	0.3	0.3	0.5	0.4

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: 0.74% OCF, Financial Express, bid to bid, total return.

Fund & market

- Emerging markets reversed in May and fell sharply, giving up the majority of their gains year to date.
- Towards the end of the month, markets began to recover, bouncing into the month of June
- The fund was inline with the benchmark: the fund fell 7.4% versus the MSCI Emerging Markets Net Total Return Index which also fell 7.4% (all figures in USD unless stated otherwise).
- For the year to date, the fund remains ahead of the benchmark by 2.6%.
- This month, Latin America was the leading region (though all were negative), falling by 2.0%. Next was EMEA, which fell 3.7%. Asia, unsurprisingly given renewed trade tensions, saw the worst of the declines, falling 8.8%.
- For the year to date, Asia is now the worst performing region, up 3.2%. EMEA is the best performing region, up 6.9%, closely followed by Latin America, up 6.1%.
- Of the largest countries in the benchmark, the best performing in the month were Russia (+3.6%), Brazil (+1.7%) and India (+0.2%).
- Russian markets benefitted from an increase in Gazprom's dividend, despite weakness in oil prices (WTI crude down 16.3% over the month).
- The worst performing countries were China (–13.1%), Korea (–9.3%) and Taiwan (–7.8%). All three suffered from a combination of renewed concern over tariffs and a slowdown in global trade

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- The strongest performers in the portfolio were Indiabulls Housing Finance (+14.8%) recovering to an extent after falling in April, B3 (Brasil Bolsa Balcao) (+6.5%) and Tisco Financial (6.5%).

- The weakest performers were Catcher (–23.1%), Qualcomm (–22.4%) and Haitian (–21.0%). Catcher and Haitian were weaker on trade concerns, and the focus on Huawei in the trade dispute, which impacted stocks in the IT sector. We discuss Qualcomm in more detail below.

- For the year to date, the best performing stocks are B3 (Brasil Bolsa Balcao) (+35.5%), Ping An Insurance Group (+27.0%) and Elite Material (+26.5%).

- The worst performers are Catcher Technology (–17.4%) and two of our South African holdings: Truworths International (–17.1%) and the Spar Group (–9.2%).

Events in May

- Trade tensions again dominated the headlines. The sell-off in equity markets began with a tweet early in the month from President Trump stating that talks were not going well.

- The increase in the tariff rate applied to $200bn of imports of Chinese goods from 10% to 25% and the threat of tariffs on a further $325bn of goods sent markets into a tailspin.

- China responded with retaliatory tariffs on $60bn of goods, increasing rates from 5-10% to 5-25%.

- Mid-month, Trump announced measures against Huawei, placing the company on an ‘Entity List’, meaning US companies are required to seek permission to sell to the company. A temporary pause on the measures was subsequently announced, effectively granting three months’ reprieve.

- Mexico also found itself in the firing line in the trade war. President Trump announced tariffs would be applied to Mexican imports, at an escalating rate, until measures were taken to prevent illegal migration into the US. Shortly after the end of the month, measures to tackle border security were announced by the Mexican government, nullifying the threatened tariffs.

- Results of the Indian election were announced, with Narendra Modi and the BJP winning an emphatic victory. The market reacted positively to the incumbent’s victory and a greater sense of political stability.

Trade and Technology

"Trade tensions dominated the headlines…" is a sentence we have written many times over the past year and a half, to the point it risks becoming hackneyed. The trade dispute took a different, and more alarming, direction in May with the explicit targeting of Huawei.

While the impositions of sanctions on a large scale would be devastating for the company, to some extent we expect what would be Huawei's loss to be other companies' gain. Plenty of competitors in the handset business exist both in China and elsewhere (Samsung, Apple…) and would clearly benefit if Huawei is unable to obtain supplies for manufacturing. In the telecoms infrastructure business, Ericsson and Nokia would likewise benefit. We have some exposure in the portfolio to Huawei with companies that are in the smartphone supply chain, but in none of these cases is Huawei the dominant customer.

The real challenge that the Huawei dispute highlights is the way the company has been singled out. President Trump has already strongly hinted that a resolution to trade talks could involve a resolution with Huawei, so it is difficult to see how this move is anything other than politically motivated. This targeting of specific companies that are major players is a new risk in the conflict. While we think Trump ultimately does want to strike a deal with the Chinese (though the timing is unclear), Huawei becoming embroiled in the row is clearly a step backwards.

Nevertheless, the Huawei dispute highlights the difficulties in imposing sanctions, to the point at which they are almost unworkable. The company has minimal market share in the US handset business, but a much more significant share in Europe (where the active removal of a supplier from the market is likely to be viewed as anti-competitive). Moreover, while larger telephone networks in the US do not use Huawei equipment, smaller telecom operators do, creating a real challenge for them if sanctions are applied.

We are already seeing signs that China is in ahead of the US when it comes to 5G development and deployment from a performance perspective (and Chinese-made equipment is cheaper than that of competitors). This development is significant as it reflects China leading innovation, rather than merely copying technology developed elsewhere. America's efforts to supress technological development in China may end up having little detrimental impact, and instead accelerate China's efforts to increase self-reliance. The US may well end up becoming more dependent on China over time, not less.

Portfolio Commentary

Spar Group reported results for the first half of its 2019 financial year (September year-end). Spar is a retailer operating in South Africa (2,308 stores), Ireland (1,381 stores) and Switzerland (327 stores). Results for the period were good overall, despite a difficult retail environment in South Africa. The Irish business was an area of strength, while Switzerland was weaker (although management expects a recovery in the second half of the year. Turnover for the first six months was 8.6% and group operating profit increased 5.1%. The dividend increased 5.2%. Spar is also planning to expand in Poland with the acquisition of 77 supermarket stores from the Piotr i Pawel Group.

Motorcycle manufacturer **Bajaj Auto** in India reported results for the fourth quarter of its 2019 financial year (March year-end). Revenues for the full year increased 20%, on the back of higher volumes, up 25%. Cost increases, however, curtailed the growth in EBITDA, which was up 4%. Management sounded an optimistic tone on their call, highlighting the success of the Duke 125 motorcycle. This model, part of their Sports segment and priced at INR 125,000 (about £1,400) is "the most expensive 125cc bike in the market" – strong evidence of pricing power. While the domestic market overall has been more challenging, export markets have held up (with the exception of the Middle East, where trading has been poor). A pickup in demand in the local market should translate into meaningful growth on the bottom line – even more so if there is relief from cost pressures.

We commented on **Qualcomm's** competitive positioning in last month's brief. The stock gave up a portion of its year to date gains in May following a ruling against it in a case with the FTC. As a reminder, this came shortly after the company settled its long running dispute with Apple.

The FTC case was brought against the company owing to its licensing practices, which the judge ruled are anticompetitive (the company has said it will appeal the decision). What interested us, however, was the involvement of the US Department of Justice in the case not long before the verdict, effectively pushing for relatively light punishments/penalties, should they be imposed. Qualcomm is clearly key to America's aspirations to develop technological superiority in 5G; as we know, it is in a race against the Chinese. Clearly there is a reluctance to impose conditions that would damage the long-term prospects of Qualcomm. We expect changes to the company's licensing practices, but we have not altered our view on the company's competitive position.

Outlook

In the long term, we think the current trade conflict is noise. We expect a resolution in the form of a negotiated agreement, but the timing and exact provisions of that agreement are uncertain. In the meantime, markets are likely to continue to be volatile, advancing on signs of progress, and falling back if tensions re-escalate.

The market has also reacted according to shifting expectations of stimulus measures by the US Federal Reserve. Recent comments from the Fed indicate it is moving in far more dovish direction, and futures markets are pricing in a strong probability of rate cuts. Furthermore, the speed at which the direction of monetary policy has changed over the last few months has been rapid.

However, there is a disconnect here: US equity markets are in record territory, but they either ignoring the potential for damage inflicted on the US economy by higher prices for imported goods, or they are assuming that the Fed will come to the rescue. Meanwhile, emerging market equities trade at far more modest levels, and there is little recognition of China's ability and willingness to provide monetary stimulus.

These conditions illustrate why we do not attempt to take any sort of 'macro view' within the fund. Our allocations are determined by an analysis of individual companies, rather than trying to shape the portfolio to match a top-down view.

We seek to identify quality companies that have a degree of control over their own fortunes. Typically for us (though not typically for the market in general) they are less exposed to external factors or events, for example movements in commodity prices, and instead have some competitive advantage that comes with pricing power, or brings efficiency benefits. These attributes allow companies to earn high returns on capital, and prevent those returns from being eroded by competitors.

Moreover, we are investing in companies with a strong track record. By looking back over the past eight years (at a minimum) we are considering a period where companies have been buffeted by various economic headwinds, yet have maintained their ability to earn good returns. US equities may well have been in a bull market for the past ten years, but the same cannot be said for emerging markets, as their economies have suffered their own difficulties and challenges over that time. It is important to remember that these companies have faced their fair share of difficulties in past, but have thrived despite the tough conditions. We believe they will continue to do so.

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

Data sources
Fund performance: *Financial Express, total return*
Index and stock data: *Bloomberg*

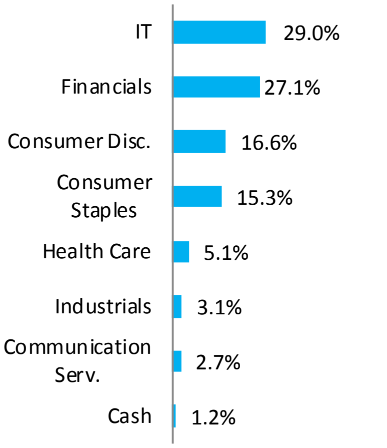
PORTFOLIO

31/03/2019

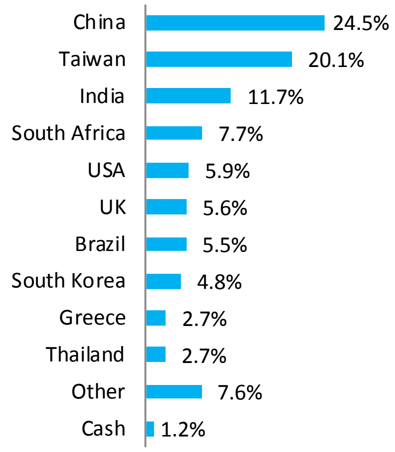
Fund top 10 holdings

Indiabulls Housing Finan	3.7%
Novatek Microelectronics	3.6%
Elite Material	3.5%
Haitian International Hol	3.1%
China Lilang	3.0%
Broadcom	3.0%
Shenzhou International	3.0%
Qualcomm	2.9%
Unilever	2.8%
Truworths International	2.8%
% of Fund in top 10	31.5%
Total number of stocks	36

Sector analysis



Geographic allocation



PERFORMANCE

31/05/2019

Discrete years % total return

	May '15		May '16		May '17		May '18		May '19	
	USD	GBP	USD	GBP	USD	GBP	USD	GBP	USD	GBP
Fund (Z class, 0.74% OCF)	-	-	-	-	-	-	17.8	14.3	-14.8	-9.5
MSCI Emerging Markets	0.3	10.3	-17.3	-13.3	27.9	44.2	14.4	11.0	-14.6	-9.3
IA Global Emerging Markets Sector	-2.1	7.6	-16.3	-12.3	26.3	42.4	10.1	6.8	-16.9	-11.8

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 (Z class, 0.74% OCF)	-7.3	-4.2	6.7	7.8	-7.1	-1.9	-	-	27.1	23.6
MSCI Emerging Markets	-7.3	-4.1	4.1	5.2	-8.7	-3.6	32.7	53.2	25.3	21.9
IA Global Emerging Markets Sector	-6.4	-3.2	6.2	7.3	-7.8	-2.7	28.2	48.0	23.4	20.0

Annualised % total return from launch

	USD	GBP
Fund (Z class, 0.74% OCF)	10.4%	9.1%
MSCI Emerging Markets Index	9.7%	8.5%
IA Global Emerging Markets	9.0%	7.8%

Risk analysis - Annualised, weekly, from launch on 23.12.2016

31/05/2019	Index		Sector		Fund	
	USD	GBP	USD	GBP	USD	GBP
Alpha	0.0	0.0	0.0	0.4	3.2	2.3
Beta	1.0	1.0	1.0	0.9	1.0	0.9
Information ratio	0.0	0.0	0.0	-0.2	0.5	0.2
Maximum drawdown	-24.6	-16.6	-24.6	-16.6	-23.0	-14.8
R squared	1.0	1.0	1.0	0.9	0.8	0.8
Sharpe ratio	0.3	0.3	0.3	0.3	0.5	0.4
Tracking error	0.0	0.0	0.0	3.8	6.1	6.3
Volatility	14.8	13.8	13.8	12.3	13.9	13.5

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Source: Financial Express, bid to bid, total return (0.74% OCF). Fund launch date: 23.12.2016.

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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 Guinness Emerging Markets 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 Emerging Markets 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. 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.