Guinness Emerging Markets Equity Income Fund

INVESTMENT COMMENTARY – July 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

30/06/2019

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	11.6	11.7	1.1	4.9	32.9	28.0
Index	10.6	10.7	1.2	5.0	33.2	28.2
Sector	13.1	13.1	2.3	6.2	31.4	26.5

Annualised % total return from launch

	USD	GBP
Fund	12.0%	10.3%
Index	12.0%	10.4%
Sector	11.5%	9.8%

Risk analysis (annualised, weekly, from launch)

	Index		Sector		Fund	
	USD	GBP	USD	GBP	USD	GBP
Alpha	0.0	0.0	0.0	0.7	2.6	1.8
Beta	1.0	1.0	1.0	0.9	1.0	0.9
Info ratio	0.0	0.0	0.0	-0.2	0.4	0.1
Max drwdn	-24.6	-16.6	-24.6	-16.6	-23.0	-14.8
Tracking err	0.0	0.0	0.0	3.7	6.0	6.2
Volatility	14.8	13.7	13.8	12.3	13.8	13.4
Sharpe ratio	0.5	0.5	0.5	0.5	0.6	0.5

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 rebounded in the first half of 2019, rising 10.7% (all figures in GBP unless stated otherwise)

- The fund outperformed the benchmark, rising 11.7%. Outperformance came principally from our Information Technology holdings.

- Since launch, the fund is up 28.0% versus the benchmark up 28.2%.

- EMEA (Europe, Middle East and Africa) was the strongest-performing region in the first half, rising 13.5%. Latin America was next, gaining 13.1%.

- Asia was the weakest of the three regions, rising 10.2%. The US-China trade conflict again dominated markets, and the proposal to effectively blacklist Huawei from business with US companies rattled investors, particularly in technology stocks. June brought some respite as agreement was reached to restart trade negotiations.

- Of the largest countries in the benchmark, Russia (+31.6%), Thailand (+17.9%) and Brazil (+16.4%) were strong performers.

- Poor performers were Malaysia (+1.9%), Korea (+4.3%) and Mexico (+7.1%), though all were positive.

- Overall GDP growth in emerging markets in 2019 is forecast at 4.1%; this figure down from 4.5% at the end of last year.

- Most countries saw negative revisions over the period, though many of the revisions were below half a percentage point.

- Slower global growth has been feeding through to earnings expectations: 2019 earnings forecasts were revised down by low double digits over the first half, though the downward trend moderated towards the end of the period.

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- Offsetting a weaker environment, expectations of an upcoming rate cut by the Federal Reserve have boosted sentiment, with the US-China trade conflict viewed as a key contributor to the Fed's decision making.
- Our approach is led at the company level as we seek companies with strong track records of generating attractive returns on capital that have persisted over time.

Events in 2019

- Trade tensions reduced in January and then ratcheted back up again in early May, before being raised further in late May by the backlisting of Huawei Technologies.
- A fragile stabilisation between the two sides was achieved in June at the G20 summit, but trust, even if there was little enough to begin with, has been damaged.
- Other nations came into the sights of the US relating to trade. Tariffs were again threatened against Mexico, until border control measures were agreed. India lost its preferential trade status with the US and responded with retaliatory tariffs.
- The US Federal Reserve has decisively altered its position on the outlook for interest rates. Cuts, not increases, are now expected, with the market divided on whether the next move will be a reduction of 0.25% or 0.5%.
- Modi won the election in India decisively; the Reserve Bank of India has begun to reduce interest rates; Indian economic growth decelerated in the first three months of 2019 to 5.8% year-on-year, the slowest rate in five years. Policy is now focused on this.
- The US announced the end of sanctions waivers for countries importing oil from Iran, including China, India, Japan and South Korea.
- Japan and South Korea are locked in their own trade dispute. Japan is limiting the transfer of key items related to the manufacture of semiconductors. The underlying cause appears to have been a Korean court ruling in relation to compensation for forced labour in the colonial period.
- In Indonesia the re-election of President Jokowi was affirmed by the Constitutional Court. Interest rates in Indonesia are expected to come down and plans are afoot to cut the corporate tax rate from 25% to 20%.
- Unrest has grown in Hong Kong in July as tensions between citizens and the Beijing-backed government boiled over following an attempt to introduce an extradition law. The stock market has not yet been affected but Hong Kong's longer-term outlook points more firmly to China.

Market commentary

While emerging markets generated strong returns in the first half, they lagged those of developed markets (for five consecutive months). Most of the return came from valuation multiples re-rating over the period as the return from earnings growth was negative (mid-single digits). Currency returns were broadly flat and dividends made a small positive contribution.

Within emerging markets, EMEA (Europe, the Middle East and Africa) was the best-performing region, gaining 13.1%. Latin America rose 12.6%. Asia was the weakest-performing region, rising 9.7% in the period. The US-China trade conflict again dominated markets, and the proposal to effectively blacklist Huawei from business with US companies rattled investors, particularly in technology stocks. June brought some respite as agreement was reached to restart trade negotiations.

Overall GDP growth in emerging markets in 2019 is forecast at 4.1%; this figure down from 4.5% at the end of last year. Most countries saw negative revisions over the period, though many of the revisions were below half a percentage point. India is still forecast to be the fastest-growing economy, with a consensus of 7.0% GDP growth. China is expected to grow 6.2% and the Philippines are the next highest at 6.0%. South Africa is near the bottom of the table, having seen growth revised down from the already low 1.5% to 0.7%, and Brazil and Mexico are similarly underwhelming at 1.0% and 1.2% respectively. Turkey is bottom of the pack, with negative real growth forecast of –1.5%. These numbers are subject of course to revision over the rest of the year, but the climate has undoubtedly cooled.

Slower global growth has been feeding through to earnings expectations: 2019 earnings forecasts were revised down by low double digits over the first half, though the downward trend moderated towards the end of the period. Offsetting a weaker environment, expectations of an upcoming rate cut in the US by the Federal Reserve have boosted sentiment, with the US-China trade conflict viewed as a key contributor to the Fed's decision making.

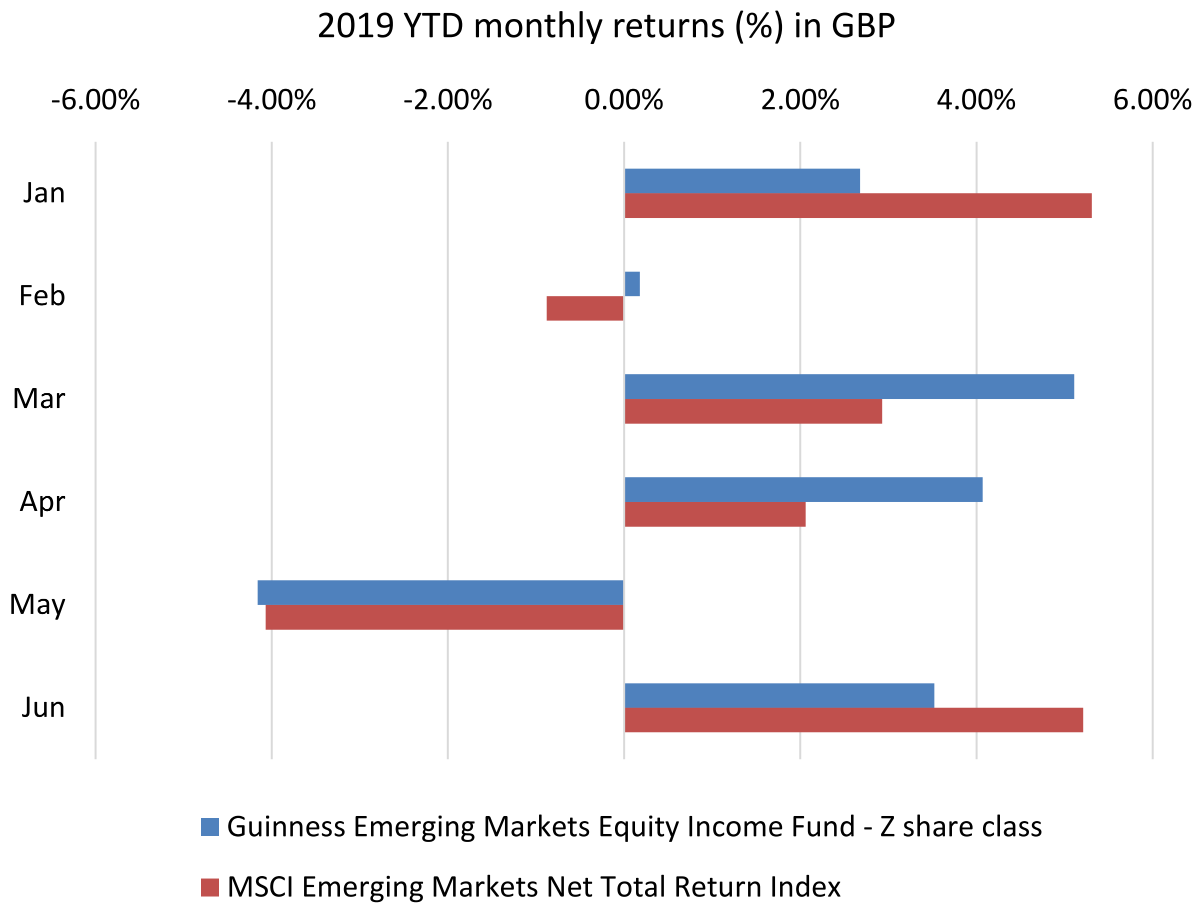
Again we reiterate comments made last month: "These conditions [i.e. the dynamic nature of the global economy] illustrate why we do not attempt to take any sort of 'macro view' within the fund. Our allocations are determined by an analysis of individual companies, rather than trying to shape the portfolio to match a top-down view."

Our approach is led at the company level as we seek companies with strong track records of generating attractive returns on capital that have persisted over time.

Performance review

The fund outperformed in the first six months of the year, returning 11.7% versus the benchmark which rose 10.7% (fund Z share class, total return in GBP). Outperformance came principally from our Information Technology holdings. Since launch, the fund is up 28.0% versus the benchmark up 28.2%.

To analyse the fund's performance in detail, we first look at the monthly returns of the fund versus the benchmark, as the following chart shows, to assess whether the fund's behaviour is in line with expectations.



Source: Financial Express

Performance in January was as we would expect, given the strong run-up in equity markets; the fund rose but underperformed. The same pattern was evident in June. February saw weaker markets, and the fund provided downside protection, rising marginally. Again, this accords with our expectations.

The pattern of outperformance in March and April and underperformance in May do not fit with the 'falling less in weaker markets, slightly lagging in stronger markets' pattern that we expect, and hence warrants further examination.

March saw outperformance mainly from our IT holdings as the sector recovered from the poor performance at the end of 2018. Principal contributors were Novatek, Elite Material, Broadcom and Qualcomm. Consumer Staples and Consumer Discretionary holdings were also strong. Indiabulls made a significant individual contribution with the stock bouncing in the run-up to results. Management subsequently affirmed a positive outlook for loan growth for the 2020 financial year ending in March 2020.

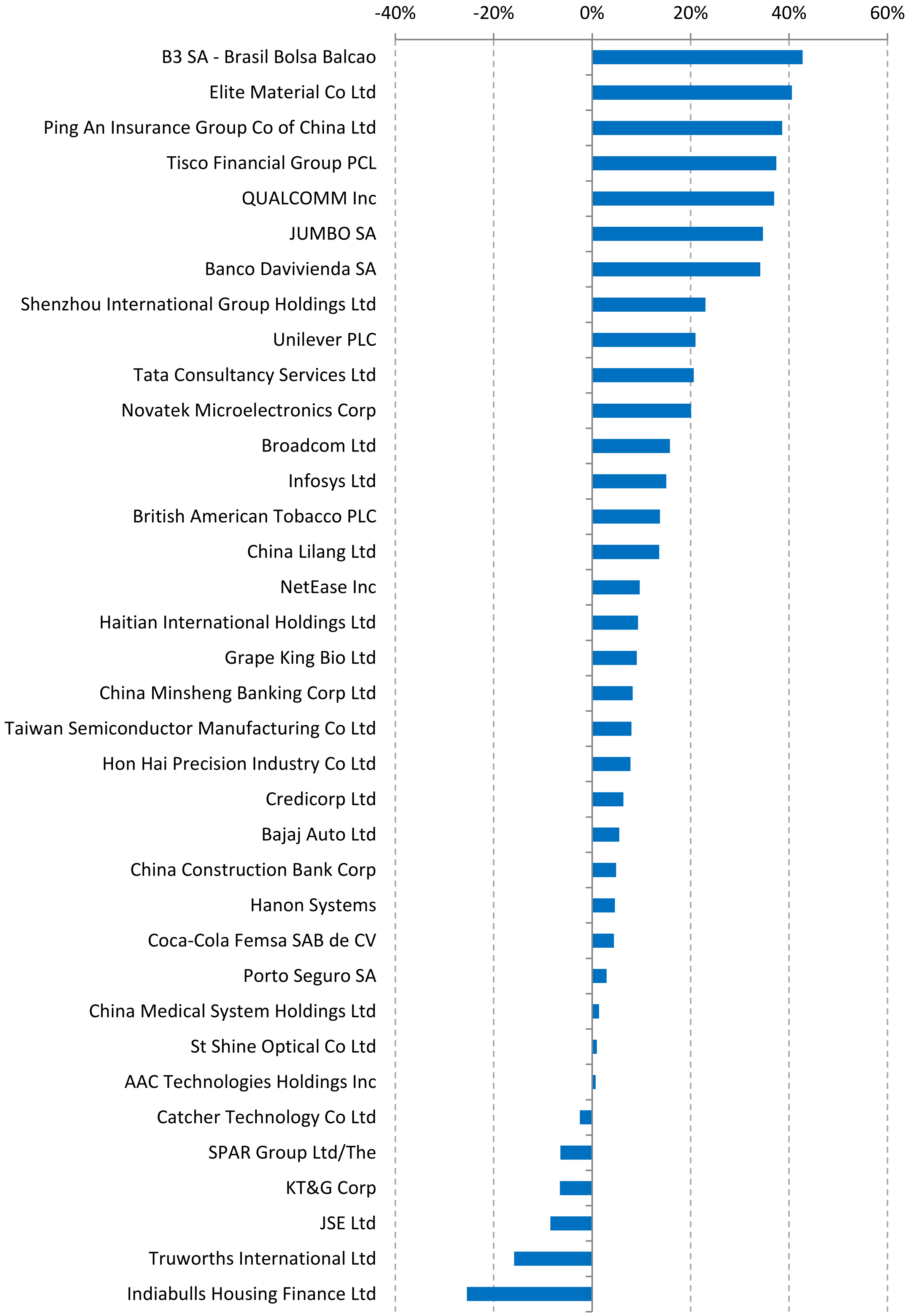
April's outperformance was more concentrated around a single stock: Qualcomm. The shares jumped 51% in the month following the resolution of the company's dispute with Apple. Intel's announcement that it was withdrawing from the development of 5G modems because there was 'no clear path to profitability and positive returns' reaffirmed our belief in the competitive advantage that Qualcomm possesses. We comment further on the company in the portfolio review section below.

The market correction that came in May coincided with an escalation in trade tension between the US and China. President Tump announced an increase to the tariff rates currently applied and the threat of tariffs on the remaining imports not currently subject to them. China responded with retaliatory tariffs. Market sentiment was also dented by the announcement that Huawei would be placed on an 'Entity List', restricting the ability of US companies to trade with the Chinese manufacturer. While China has made efforts to become more self-sufficient in technology, Huawei is still dependent on many Western technology manufacturers for hardware components and software products.

The worst-performing of the larger emerging market countries in the month were China, Korea and Taiwan (unsurprisingly, given their heavy dependence on trade), and the portfolio's IT holdings were among those that were hardest hit. However, these companies were subsequently in the best-performing group in June as markets rebounded.

The chart below shows the performance of individual stocks through the first half of the year.

Individual stock returns YTD (total return GBP; source: Bloomberg)



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The sectors represented by the top five performers are Financials and Information Technology. Technology features heavily throughout the top part of the table; Financials names are more widely distributed. There is a mix of countries represented in the top five: Brazil, Taiwan, China and Thailand. Among the weaker names we have two specific concentrations: three are our South African holdings – Truworths, JSE and Spar Group – and three of the five are in consumer sectors (Staples and Discretionary).

Portfolio review

Leaders

Brasil Bolsa Balcao ('B3'), the Brazilian stock exchange, made strong and sustained gains over the first six months of the year, continuing its run from late 2018. Gains in the Brazilian stock market have translated into record equities trading for the company. Brazil has been buoyed by expectations that President Bolsonaro will be able to enact reforms that are positive for the economy, including pension reforms in a bid to improve the country's fiscal situation. We are somewhat more cautious in our appraisal of Bolsonaro's prospects for reform, but we think it clearly necessary to pursue.

As a stock exchange our holding in B3 has more 'equity beta' exposure than is typically the case for our other holdings, but we think this can work well as part of a diversified portfolio. The business also is attractive from a point of view of being relatively capital light – the return on capital (measured in terms of CFROI) has not dipped below 20% over the past years.

Elite Material has had a strong recovery this year as it has become more likely the company will re-enter the iPhone supply chain. It produces copper-clad laminates used for printed circuit board and specialises in halogen-free laminates, which are environmentally friendly. The company's Korean customers are likely to increase adoption of the newest laminate while the Chinese are expected to follow suit later this year.

Ping An Insurance (Group) was particularly strong in the first quarter. The company reported good results for 2018, with operating profit up 18.9% and net profit up 20.6%. The growth in operating profit came from retail business (which constitutes 87% of the total). Retail customers were up 11% and operating profit per customer rose 18.1%. Ping An has benefited from improved cross selling – the proportion of customers with more than a single contract increased from 28.5% to 34.6%. Again, this is a high return on capital business: operating return on equity was flat at 21.9%.

Ping An's management highlight the company's excellent track record since its IPO in 2004. Over that period, earnings per share (EPS) has grown at a compound rate of 24.5%. The dividend has followed suit, growing at a compound rate of 25.7%. The dividend increased by less in 2018, rising by 14.7% from the previous year, though it is still up by a factor of 4.8 since 2014. (These figures exclude the payment of an additional special dividend in the first quarter of 2018 marking the company's 30th anniversary). This combination of a growing earnings stream that supports the payment of a growing dividend with a long-term commitment from management to paying that dividend, typifies the attributes we look for in our portfolio companies.

Tisco, like B3, also made consistent and strong gains over the first six months. Tisco provides finance for motorcycle and car purchases in Thailand. The company reported good results and the level of its full year dividend payment for 2018 surprised the market positively. The stock offers an attractive combination of good forecast earnings growth (mid to high single digits) with a relatively high dividend yield.

Qualcomm was strong following the resolution of its dispute with Apple. As part of the settlement the two companies agreed a six-year licensing deal and Apple paid Qualcomm the dues which have been held back for the past two years. Qualcomm's share price subsequently increased by 50.5% in April. Intel immediately announced it would withdraw from the 5G modem business, reaffirming our view that Qualcomm is the market leader in modems.

A portion of the gains were subsequently surrendered in May, as the company faced a ruling against it in a case with the US Federal Trade Commission (FTC) over 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 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.

Laggards

Indiabulls Housing Finance was a volatile stock in the first half (at times it was the best performer in the month). Indiabulls has suffered along with the rest of the sector on concerns over the sources and cost of funding. The failure last year of another non-banking financial institution (NBFI), Infrastructure Leasing & Financial Services, has cast a shadow over the sector. IL&FS bonds were highly rated by local credit agencies and so default came as a shock. Investors are unwilling to give other NBFIs the benefit of the doubt and so funding costs to these institutions have risen, denting the profit outlook. However, we think the company is well positioned, with appropriate asset-liability matching.

Truworths and JSE are two of our three South African holdings and have struggled amid a weak economic backdrop. Truworths, a clothing retailer, clearly gives us exposure to the consumer sector and sales on credit form a significant proportion of the overall business. The company also owns Office (shoes) in the

UK, which has experienced challenging conditions over the past months. Earnings expectations have held up well, and the stock trades on an undemanding valuation.

JSE is the Johannesburg Stock Exchange. Results for 2018 were disappointing relative to expectations, and market activity was muted. The company has suffered particularly this year in the months when South African equities were the weakest. Again, however, the valuation looks reasonable.

KT&G is a low-growth but cash-generative businesses with a solid local franchise, so it is not surprising that it has had weaker performance in a strong market. KT&G's outlook has improved given a turnaround in export sales which dragged significantly last year. The next set of results should reflect that turnaround and the share price should get a lift.

Spar Group is a retailer operating in South Africa (2,308 stores), Ireland (1,381 stores) and Switzerland (327 stores). Results for the first half of its 2019 financial year (September year-end) were good overall, despite a difficult retail environment in South Africa, giving us reason to be optimistic. 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.

Portfolio changes

We made no switches in the portfolio during the period but carried out periodic rebalancing to bring the portfolio holdings back to equal weight.

Outlook

On the face of it, emerging markets appear to be entering a tricky period. The two main country 'engines' of growth, China and India, each faces its own challenges. China, as the focus of US trade policy, has seen economic growth slow slightly, and there are indications that manufacturers are shifting out of the country and products are being sourced elsewhere in Asia. In reality, this is not a new trend, but the acceleration of a trend that pre-dated the trade war; manufacturers have been seeking to reduce their labour costs in China for some time as wages have risen. We expect China to act to stimulate the economy in order to offset any short-term periods of weakness, and China's robust response to the US in negotiations indicates that it has the ability and willingness to do so. Longer-term, we expect a negotiated resolution of the trade conflict, and China to continue its progress in manufacturing more technologically advanced goods.

India appears to be in better shape, with a faster rate of headline GDP growth. The recent re-election of Narendra Modi and the BJP with a resounding victory has also acted to improve confidence and reduce perceptions of political risk. But the economy is also experiencing slowing and forecasts for earnings growth this year have started to be revised downwards. Indian stocks generally trade on rich earnings multiples – predicated on higher growth – meaning there is significant potential for valuation compression. This example is another reminder that the returns to equity holders are not always linked to economic returns in the short or medium term.

Sluggish economic conditions are not only the preserve of emerging markets, as growth is slowing elsewhere. There are currently only three countries with PMIs above 50 (indicating expansion) – India, Brazil and the US. Slower global growth has clearly contributed to the Fed's expected decision to cut US interest rates.

Given the macroeconomic backdrop, it is no surprise that emerging markets attract investor pessimism. However, the lethargic state of much of the global economy is widely recognised, and investors in emerging markets are offered low valuations as compensation. Upside could come if any period of global economic contraction is shallower or shorter-lived than people expect (and this is before the effects of monetary or fiscal stimulus are considered).

It is worth reflecting on the fact that the portfolio of companies we hold in the fund have all experienced periods of economic weakness in the past yet have still been profitable and generated good returns on capital through those periods. Their business models have shown resilience to competitive forces and their financial condition has proved robust in the face of adversity. Their futures may well diverge therefore from the outcome for wider emerging markets; our companies are likely to be buffeted by wider economic forces, but we believe they are well positioned to cope with tougher times.

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

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

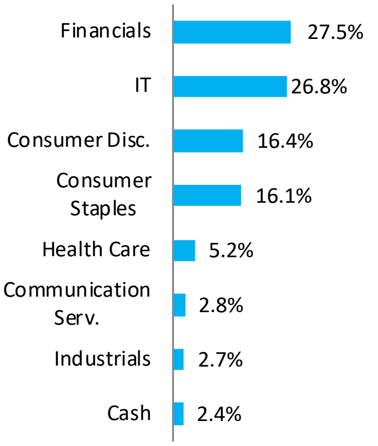
PORTFOLIO

30/06/2019

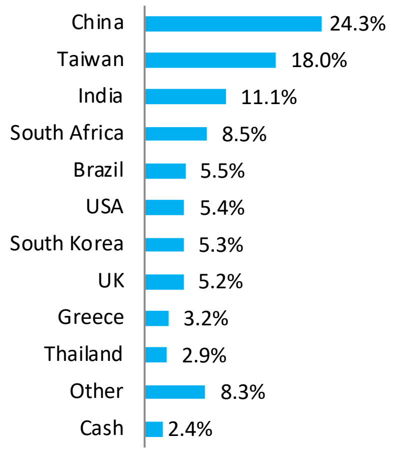
Fund top 10 holdings

Jumbo	3.2%
TATA Consultancy Service	2.9%
Tisco Financial Foreign	2.9%
Qualcomm	2.9%
Truworths International	2.9%
Novatek Microelectronics	2.9%
Ping An Insurance	2.9%
Netease.com	2.8%
Banco Davivienda	2.8%
Spar Group	2.8%
% of Fund in top 10	29.2%
Total number of stocks	36

Sector analysis



Geographic allocation



PERFORMANCE

30/06/2019

Discrete years % total return

	Jun '15		Jun '16		Jun '17		Jun '18		Jun '19	
	USD	GBP	USD	GBP	USD	GBP	USD	GBP	USD	GBP
Fund (Z class, 0.74% OCF)	-	-	-	-	-	-	10.1	8.3	-14.8	-9.5
MSCI Emerging Markets	-4.8	3.5	-11.7	3.9	24.2	27.8	8.6	6.8	-14.6	-9.3
IA Global Emerging Markets Sector	-7.2	0.9	-11.7	3.9	23.9	27.5	5.4	3.7	-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)	4.5	3.5	11.6	11.7	1.1	4.9	-	-	32.9	28.0
MSCI Emerging Markets	6.2	5.2	10.6	10.7	1.2	5.0	35.5	42.3	33.2	28.2
IA Global Emerging Markets Sector	6.4	5.4	13.1	13.1	2.3	6.2	33.6	40.3	31.4	26.5

Annualised % total return from launch

	USD	GBP
Fund (Z class, 0.74% OCF)	12.0%	10.3%
MSCI Emerging Markets Index	12.0%	10.4%
IA Global Emerging Markets	11.5%	9.8%

Risk analysis - Annualised, weekly, from launch on 23.12.2016

30/06/2019	Index		Sector		Fund	
	USD	GBP	USD	GBP	USD	GBP
Alpha	0.0	0.0	0.0	0.7	2.6	1.8
Beta	1.0	1.0	1.0	0.9	1.0	0.9
Information ratio	0.0	0.0	0.0	-0.2	0.4	0.1
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	0.5	0.5	0.5	0.5	0.6	0.5
Tracking error	0.0	0.0	0.0	3.7	6.0	6.2
Volatility	14.8	13.7	13.8	12.3	13.8	13.4

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

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.

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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.