

# Guinness Best of China Fund

INVESTMENT COMMENTARY – February 2020

**Launch date** 15.12.15

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

## Aim

Guinness Best of China Fund is designed to provide investors with exposure to economic expansion and demographic trends in China and Taiwan.

The Fund is managed for capital growth and invests in profitable companies generating persistently high return on capital over the business cycle.

**Performance** 31.01.2020

<b>Fund</b>	Best of China Fund		
<b>Index</b>	MSCI Golden Dragon		
<b>Sector</b>	IA China/Greater China		

	2017	2018	2019
<b>Fund</b>	38.2	-20.3	26.0
<b>Index</b>	31.3	-9.5	19.0
<b>Sector</b>	35.9	-14.2	22.2

	1 year	3 years	From launch
<b>Fund</b>	10.5	23.8	63.9
<b>Index</b>	8.6	29.4	78.4
<b>Sector</b>	11.2	30.7	69.6

## Annualised % total return from launch (GBP)

<b>Fund</b>	12.7%
<b>Index</b>	15.0%
<b>Sector</b>	13.6%

## Risk analysis (annualised, weekly, from launch)

	Index	Sector	Fund
<b>Alpha</b>	0.0	-1.2	-2.0
<b>Beta</b>	1.0	1.0	1.0
<b>Info ratio</b>	0.0	-0.4	-0.3
<b>Max drwn</b>	-17.8	-21.7	-25.7
<b>Tracking err</b>	0	5	6
<b>Volatility</b>	17.9	18.1	19.1
<b>Sharpe ratio</b>	0.6	0.5	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: Financial Express, bid to bid, total return 0.74% OCF. Returns for share classes with a different OCF will vary accordingly

## Fund & Market

- In January, the Best of China Fund fell 6.6% (in GBP, Z class) while the MSCI Golden Dragon Net Total Return Index fell 4.2%.
- MSCI China fell 4.3%, MSCI Taiwan fell 4.2% while MSCI Hong Kong fell 4.0%. Onshore markets were stronger, with the Shenzhen Component Index rising 4.5% and the Shanghai Stock Exchange Composite Index falling 0.5%.
- In MSCI China, the strongest sectors were Information Technology (+4.2%), Health Care (+1.3%) and Communication Services (-0.5%) while the weakest were Real Estate (-14.5%), Energy (-10.4%) and Materials (-8.5%).
- In Taiwan, the Information Technology Index, which makes up more than half of the Taiwanese index, fell 4.9%.
- In Hong Kong, the Financials and Real Estate sectors, which are by far the largest parts of the local index, were down 2.4% and 7.1% respectively.

## Events in January

- The coronavirus epidemic spread across China, leading to an unprecedented shutdown of Wuhan city. Travel across the rest of the country was restricted. The New Year holidays were extended to 10<sup>th</sup> February, but we expect further disruption.
- The US and China officially signed phase one of the trade deal. Broadly speaking, existing tariffs will remain in place. The deal requires China to buy at least \$200 billion of goods and services from the US, including agricultural goods, airplanes, pharmaceuticals and energy products.

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The deal also led to commitments by the Chinese to:

- Not significantly devalue the Renminbi to make Chinese exports more competitive, and to regularly disclose foreign exchange reserve data. Note China has been bound by these commitments for some years as part of its membership of the G20.
  - Protect intellectual property rights through stronger legal protections and stop the forced transfer of technology to Chinese firms.
  - Open up the economy to foreign financial companies in insurance, banking and asset management. China has been making progress on this front over the past year; e.g. asset management companies will be allowed majority control over their operations in China this year, while last year foreign firms received approval to run majority-owned securities joint ventures.
- The deal does not, however, target the structure of the Chinese economy, i.e. the use of subsidies and state-owned enterprises (SOEs). This will be a much more contentious discussion which will take time to resolve.
  - Due to the handling of the protests in Hong Kong, the head of the Liaison Office was replaced. The Liaison Office is the official representative of the Chinese government in Hong Kong.
  - Using the fallout from the protests in Hong Kong to her advantage, Tsai Ing-wen won the presidential election in Taiwan.

## Portfolio Update

The coronavirus originated in a seafood market in Wuhan, the capital city of Hubei Province, in December. Reports trickled through over the following weeks but it was only on January 23<sup>rd</sup> that the central government took decisive action, essentially shutting down Wuhan. Travel was restricted across the rest of the country and many only ventured out of their homes for essential needs.

For now, the vast majority of cases are in China and most of these cases are in Hubei Province. But it is clear the virus is spreading beyond China's borders and cases have been reported in Europe and the US. The data shows the mortality rate is much higher in Hubei Province than in the rest of China. At least 4,200 people have recovered from the virus so far. At the beginning of the crisis, Hubei Province seemed overwhelmed by the number of people turning up at hospitals and this may be one of the causes of the higher mortality rate. At the moment, the lower death rate in other provinces and other countries suggests that if the infrastructure is in place, the virus can be dealt with. Most deaths seem to be of people who already have a medical condition and so have weaker immune systems.

The growth in the rate of confirmed cases has stabilised, though we are cautious on the quality of this data point. There are likely people who have moderate signs of the virus and have not been diagnosed. A

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change in methodology at the beginning of February meant those who were tested positive for the virus in China, but showed no signs of symptoms, were not classed as confirmed cases.

It is difficult to judge accurately the impact of the virus on the companies in the portfolio. On the supply side, the New Year holidays were extended to Feb 10<sup>th</sup> and depending on the province, it will take longer for factories to be restarted. On the demand side, the virus struck in the run-up to the New Year holidays, a period known for high consumer spending, and so it is likely first quarter GDP growth will be lower than expected. However, monetary policy has been used to help the economy; the PBOC injected \$174 billion of funds into the banking system to ensure ample liquidity. The PBOC is also offering \$59.6 billion in loans to businesses affected by the virus.

### Summary view & outlook

Despite the short-term implications of the virus, the long-term case for holding the businesses in the Fund remains the same as it was a month ago. Our companies have persistently achieved a return on capital well above the cost of capital. Our companies are not highly levered, so they should be able to cope with the slowdown in business that is expected in the first quarter. Debt/equity for the portfolio, excluding the three banks, is 44%, so the Fund is not highly geared. If we look at net debt/equity, which subtracts cash from debt, the figure is -13%, meaning our companies could in theory pay back all of their debt with cash.

The Fund started the year trading at a 11% discount to the benchmark. As a result of the sell-off due to the coronavirus, the discount has widened to 16% and the Fund trades at 11.1x 2020 estimated earnings, despite the companies in the Fund being expected to grow earnings, in aggregate, at approximately the same rate as the broader market, which is 11% in 2020. Over time, we expect this valuation gap to close and the Fund should benefit as the market recognises the undervalued companies it holds.

**Edmund Harriss** (portfolio manager)

**Mark Hammonds, CFA** (analyst)

**Sharukh Malik, CFA** (analyst)

#### Data sources

Fund performance: *Financial Express*, total return  
0.74% OCF in GBP

Index and stock data: *Bloomberg*

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## Guinness Best of China Fund

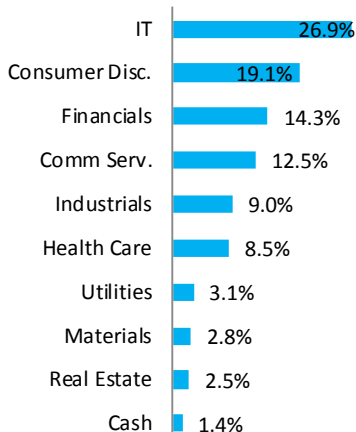
### PORTFOLIO

31/01/2020

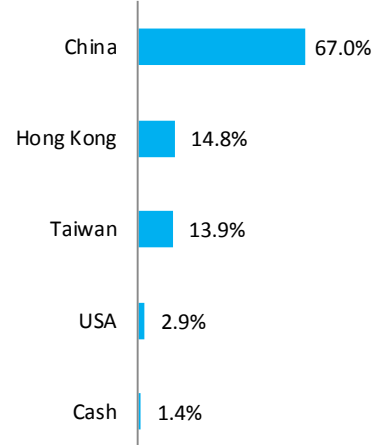
#### Fund top 10 holdings

Tongda Group Holdings	3.7%
China Lesso Group	3.7%
AAC Technologies	3.5%
Noah Holdings	3.3%
Alibaba Group	3.2%
Tencent Holdings	3.2%
Autohome	3.2%
China Medical System	3.2%
Netease.com	3.1%
Taiwan Semiconductor	3.1%
% of Fund in top 10	33.3%
Total number of stocks	34

#### Sector analysis



#### Geographic allocation



### PERFORMANCE

31/01/2020

#### Annualised % total return from launch (GBP)

Fund	12.7%
MSCI Golden Dragon Index	15.0%
IA China/Greater China sector average	13.6%

#### Discrete years % total return (GBP)

	Jan '16	Jan '17	Jan '18	Jan '19	Jan '20
Fund	-	22.7	32.5	-15.4	10.5
MSCI Golden Dragon Index	-14.1	40.6	31.2	-9.2	8.6
IA China/Greater China sector average	-13.2	37.8	35.5	-13.2	11.2

#### Cumulative % total return (GBP)

	1 month	Year-to-date	1 year	3 years	5 years	From launch
Fund	-6.6	-6.6	10.5	23.8	-	63.9
MSCI Golden Dragon Index	-4.3	-4.3	8.6	29.4	56.5	78.4
IA China/Greater China sector average	-3.7	-3.7	11.2	30.7	56.4	69.6

### RISK ANALYSIS

31/01/2020

Annualised, weekly, from launch on 15.12.15, in GBP	Index	Sector	Fund
Alpha	0.00	-1.19	-2.00
Beta	1.00	0.98	1.01
Information ratio	0.00	-0.35	-0.34
Maximum drawdown	-17.78	-21.67	-25.74
R squared	1.00	0.94	0.90
Sharpe ratio	0.62	0.51	0.46
Tracking error	0.00	4.52	6.06
Volatility	17.90	18.05	19.05

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Source: Financial Express, bid to bid, total return (0.74% OCF). Fund launch date: 15.12.2015.

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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 Best of China 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 Best of China 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](http://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, 18 Smith Square, London SW1P 3HZ.

### 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

This is an advertising document. 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](http://www.carnegie-fund-services.ch). The paying agent is Banque Cantonale de Genève, 17 Quai de l'Île, 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.

**GUINNESS**

ASSET MANAGEMENT

Guinness Asset Management Ltd is authorised and regulated by the Financial Conduct Authority

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