

GUINNESS

# Asian Equity Income Fund



Annual review

# 2020

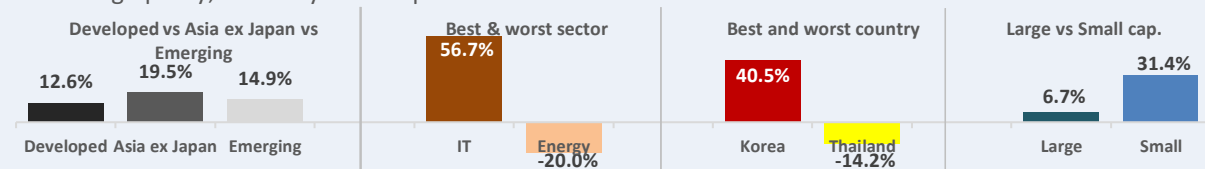
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Analyst

**GUINNESS**  
ASSET MANAGEMENT

## What happened in Asia and the world?

- The Covid-19 virus emerged in China and spread through Asia. By March it had become a worldwide epidemic on a scale not seen since the Spanish Flu epidemic of 1918-1920. A global research effort has produced several vaccines which have, or are in the process of obtaining, approval.
- The imposition of significant restrictions on movement caused severe disruption. The World Bank estimates the world economy contracted -4.4% in 2020. Of the world's major economies only China saw any growth, up 2.3%.
- Government and Central Bank responses in developed economies have been massive and unprecedented with payments to individuals, grants and loans to businesses, and substantial liquidity injections coupled with ultra-low interest rates.
- Geopolitics exerted significant influence over markets. The US has made more extensive, targeted and innovative use of tariffs to achieve foreign policy goals, which has had a significant impact. Oil prices moved significantly, even turning negative at one point, as OPEC tussled over supply quotas only to be hit by a collapse in demand.
- In Asia, the 10 countries of the association of South East Asian Nations plus China, Korea, Japan, Australia and New Zealand, together representing 30% of the world population, agreed a trade pact (the Regional Comprehensive Economic Partnership) which is likely to have a long-lasting impact and reflects intensifying regional economic links.
- China's grip on Hong Kong tightened with legislation that significantly curbs political freedom and freedom of speech.
- The US presidential election was won by Joe Biden, and while this is expected to usher in a less volatile approach to foreign policy, it is likely that US pressure on China will continue.



Total return in GBP, Calendar year 2020; MSCI World & MSCI Emerging Markets Index; MSCI AC Pacific ex Japan; individual MSCI World GICS sectors.

## What happened in the Fund?

- The Fund rose 4.8% for the year, behind the benchmark, which rose 19.5%, but ahead of the MSCI Asia Pacific High Dividend Yield Net Total Return Index which fell 1.1% (all in GBP terms).
- The dividend on Class Y GBP shares fell less than that of the market (as measured by MSCI AC Pacific ex Japan Index), down 14.8% compared the market's dividend decline of 21.4%, in GBP.
- Over five years the Fund's dividend distribution grew an average 2.0% per annum vs the Index decline of -0.7% p.a.
- The Fund's performance in the first quarter of -20.7% vs the benchmark -14.2% was followed by performance over the rest of the year of +32.1%, which captured 82% of the rally and was in line with what we would have expected.
- The performance of Asian Growth and Asian Value stocks diverged significantly in 2020. Growth stocks (as measured by MSCI Asia Pacific ex Japan Growth Net Total Return Index) rose 31.4%. Value stocks rose 6.7% (as measured by the equivalent Value index).
- The Fund ended the year on a price to earnings ratio (PER) of 13.1x 2020 and 11.4x 2021 estimated earnings; this puts it at a 29.6% discount to the market's 2020 PER and at 25.3% discount to 2021.
- We bought new positions in Inner Mongolia Yili Industrial, Suofeiya Home Collection, Zhejiang Supor, Nien Made Enterprises, NetEase Inc, Korean Reinsurance and Metcash.
- We sold AAC Technologies, Godrej Consumer Products, Janus Henderson, Li & Fung, Luk Fook Jewellery, and PTT.

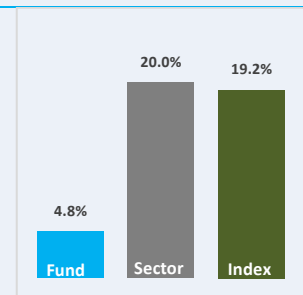
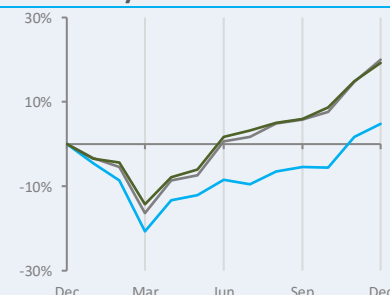
## Performance

### Cumulative since launch



**Fund** Guinness Asian Equity Income  
**Sector** IA Asia Ex Japan  
**Index** MSCI AC Pacific ex Japan

### Calendar year 2020



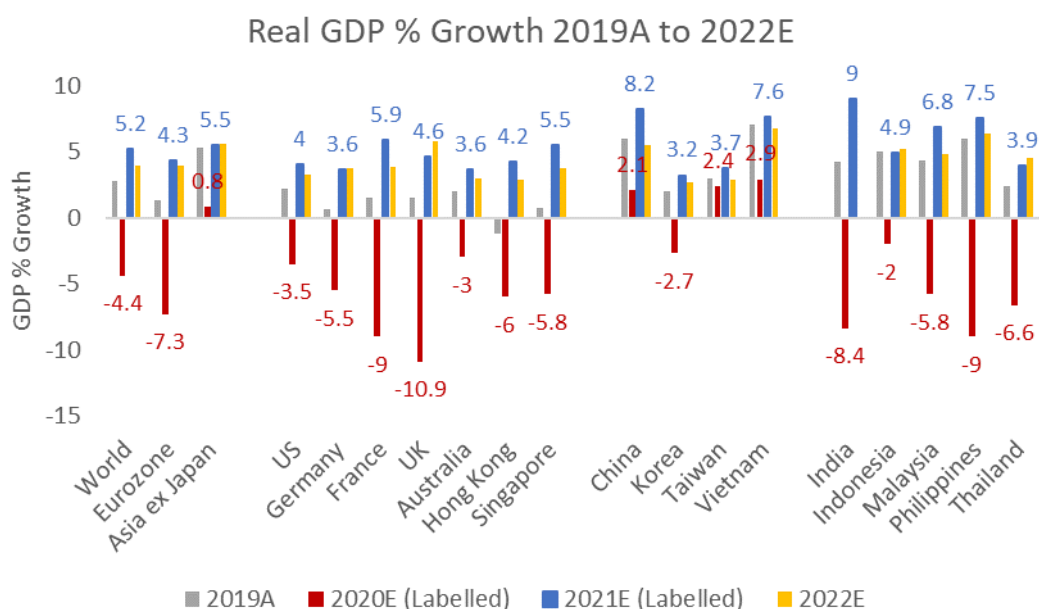
Cumulative % gross total return, in GBP.  
Source: Financial Express, Y Class (0.99% OCF)

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 fluctuation. Fund returns shown above are for share classes with a current Ongoing Charges Figure (OCF) of 0.99%; returns for share classes with a different OCF will vary accordingly.

## 2020 in Review

The year began with the emergence in China of the Covid-19 virus, which spread rapidly across Asia and then became a global pandemic. The public health responses in North Asia (China/Hong Kong, Korea, Taiwan) and in the developed markets of Australia, New Zealand and Singapore were decisive and in some instances were enforced with draconian rigour. The result has been a shallower economic decline for much of the region and a 'V-shaped' economic recovery in China's case. China's economy is expected to have expanded 1%-2% in 2020 and is likely to have been the only major economy to do so. The World Bank and the International Monetary Fund currently estimate the global economy contracted over 4% last year.

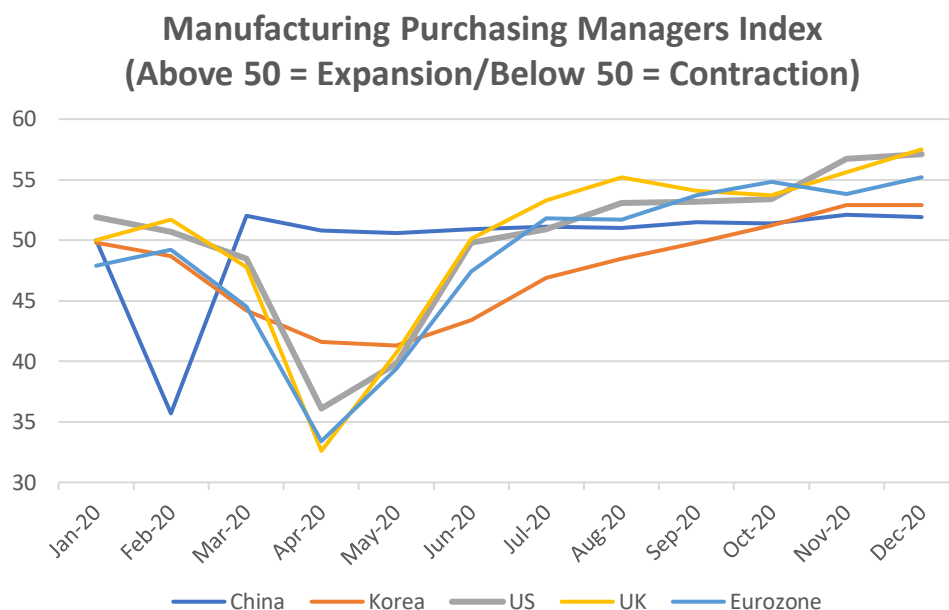
The earliest signs of economic recovery came in manufacturing and trade growth, while services lagged. Electronics, personal protection equipment and medical devices production led the way but then broadened out to consumer goods which were primarily bought through online distribution channels. Higher-ticket items such as consumer durables and automobiles have seen a slower pace of recovery. By November 2020 (the latest data we have) Chinese exports for the year had reached US\$2.32 trillion and overtaken the \$2.26 trillion in the same period in 2019. The same was true of Taiwan, whose electronics industry drove aggregate exports growth of 4% year over year for the same 11-month period. Like China, Taiwan is expected by the consensus to record economic expansion (of 2.4%) for 2020.



Source: Reported data for 2019 and Consensus estimates 2020 - 2022, Bloomberg

For Korea, the trade picture is more mixed because of the range of goods it produces, from electronics and household goods through to cars, petrochemicals, ships and steel. In this respect its trade figures give a broader reflection of world economic health. Exports are expected to be down -3.9% year on year while the economy is expected to have contracted -2.7%, but this is better than the world economic growth number and substantially better than the experience of the US, UK and Europe. Thus, in North Asia, trade growth and the resumption of domestic economic activity has been led by manufacturing, and indicators such as industrial output, purchasing managers' indices (measures of industrial confidence) and fixed asset investment now point to expansion. This in turn has fuelled a rise in consumer confidence, which is well above trough levels seen earlier in the year. We continue to see lockdowns in the region on further virus outbreaks (although case numbers are in the hundreds rather than the tens of thousands) and these have kept consumer confidence below 2019 levels.

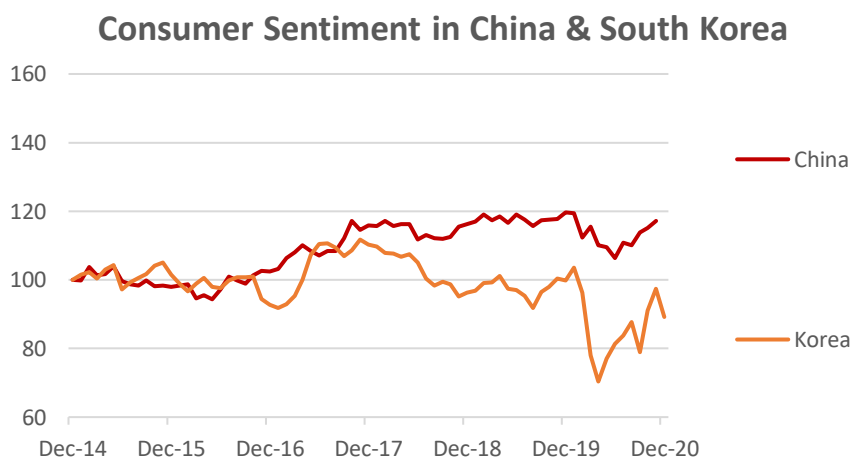
One measure of industrial confidence is the Purchasing Manager's Index (PMI), a composite measure of managers' outlook for production, new orders, inventory and employment. A measure above 50 signifies expansion, while less than 50 points to contraction. The chart below compares the paths of Asia's two major manufacturing economies, China and Korea, with developed markets.



Sources: China - National Bureau of Statistics; Korea, US, UK, Eurozone - Markit

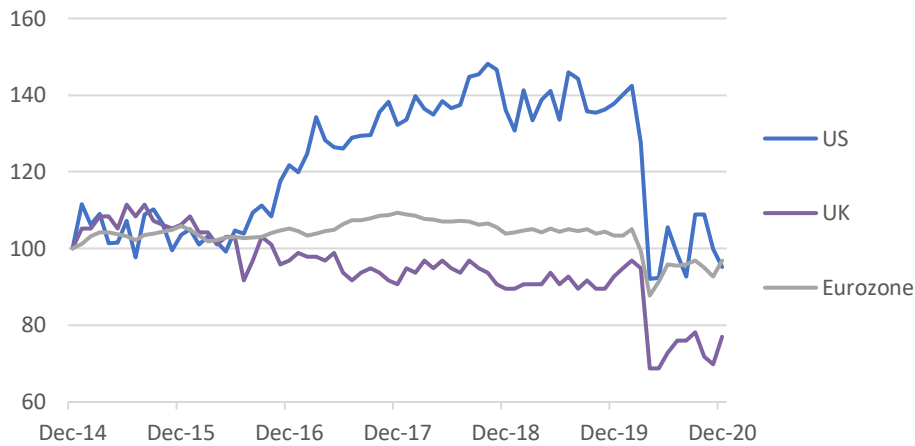
All indices in the chart point to expansion, but those of developed markets show both a deeper and more prolonged contractionary phase than those of China and Korea. The effects of the latest lockdowns have also not yet been reflected in this data.

The faster recovery or shallower decline in manufacturing in North Asia has also been reflected in consumer sentiment, which although quite volatile in these conditions has been markedly stronger than that in developed markets. The recurrence of virus outbreaks and further restrictions continue to buffet sentiment, but when compared to developed markets, where consumer confidence remains weak, the picture appears encouraging. This is important to us given the increased role now played by consumers in the region, a factor to which the Fund is exposed.



Sources: China - National Bureau of Statistics; Korea - Bank of Korea. Rebased to Dec 2014 = 100, Guinness Asset Management calculation.

## Consumer Sentiment in the UK, US & Eurozone

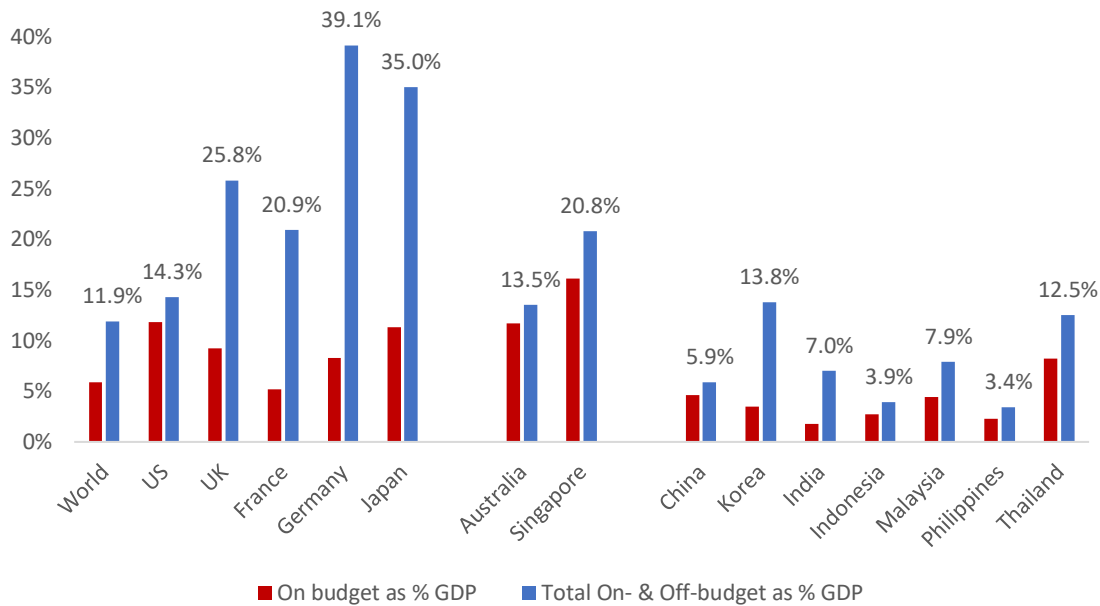


Sources: US - Conference Board; UK - GfK; Europe - European Commission. Rebased to Dec 2014 = 100, Guinness Asset Management calculation.

The experience of South and South-east Asian countries, with the exceptions of Singapore and Malaysia, have been different because of their less developed healthcare systems. India, Indonesia and the Philippines have been hard hit. Economic outcomes have been more varied. While Indonesia's economy is expected to have shrunk 2% in 2020, those of India and the Philippines are expected to have seen a contraction of closer to 9%. The collapse of Thailand's tourism sector and the interruption to its export manufacturing sector are expected to have resulted in a 6.5% contraction. Thailand's tourism industry typically generates US\$5.4 billion per month in receipts (around \$64 billion a year based on 2018 and 2019 figures) which is significant for an economy that was valued at around \$540 billion in 2019 according to World Bank data. However, since March receipts have been around zero. The economic focus is therefore on domestic activity, food exports and exports of components. Among components, the electronics industry has been growing, but demand for car components (notably for the Japanese car makers who have a large presence) continues to be weak.

Financial support from governments has been unprecedented in size and has had a significant impact on markets. The IMF has produced in its Fiscal Monitor some data showing the countries' fiscal measures in response to the pandemic. At the world level, fiscal support topped \$11.7 trillion, equating to 12% of the world economy (GDP) which is estimated to be \$96 trillion. The form of support takes the form of 'on-budget' items consisting of actual spending and revenues foregone, and 'off-budget' which includes asset purchases, assuming debt, loans and provision of guarantees. These off-budget items amount to at least as much as the headline support measures and in countries such as France, Germany, Japan and the UK they are several times larger.

## Country Fiscal Responses to COVID-19



Source: IMF Fiscal Monitor - Database of Country Fiscal Measures in Response to the Covid-19 Pandemic. Data as at 11 Sept 2020

In Asia, government responses have reflected the seriousness of the pandemic, in terms of its duration and disruption, and the available means. Across the region, with exceptions of Australia, Singapore and Thailand, the direct response (shown by the red bars) has been less than 5% of GDP. In China's case, the resumption of economic activity was quick, with disruption mostly restricted to the first quarter. China's strong manufacturing position in terms of both diversity and links to international supply chains led to an unexpectedly strong rebound, in spite of US efforts to restrict China trade. This, and the government's reluctance to repeat the debt-fuelled growth spree that followed the Global Financial Crisis, has shaped China's comparatively modest response.

Modest responses came also from India, Indonesia and the Philippines. In India, off-budget support is greater than China's as a proportion of its economy, but the direct spending element is much smaller. This is a consequence of the poor condition of Indian finances and of its banking sector, which have severely restricted the government's room for manoeuvre. Central Bank policies have remained disciplined for the most part. There have, however, been a couple of instances of unorthodox policies where debt monetization has occurred in both Indonesia and India. Debt monetisation happens when the Central Bank buys government debt directly from the government (unlike quantitative easing, where the Central Bank buys debt through the secondary market). The risk of debt monetization is a loss of Central Bank independence and its politicisation. So far, however, these instances have been one-off events.

## Market performance

The MSCI AC Pacific ex Japan Net Total Return Index rose 19.5% in Sterling terms, following a 15.6% rise in 2019. In style terms, Growth was the significant outperformer, as it was for most markets, for the first ten months of the year. Only as prospects grew for a vaccine rollout did Value take over market leadership. This momentum was supported as news of Democrat Joe Biden's election victory came through, with markets anticipating higher spending. The recovery in Value stocks was also accompanied by a weaker US dollar.

The chart below shows the relative performance of the MSCI Asia Pacific ex Japan Growth Net Total Return Index compared to the Value equivalent, calculated as a ratio and then rebased to 100 at the end of 2019. (The MSCI Growth indices methodology aims to maximise exposure to a Growth factor made up of Analyst-

Predicted Long-Term Earnings Growth (EGRLF), Earnings Per Share Growth Rate (EGRO) and Sales Per Share Growth Rate (SGRO). The Value index methodology uses three variables in its Value factor: Book Value to Price ratio, 12-month forward earnings to price ratio and the Dividend Yield.)

### Relative performance of Asian Growth vs Value in USD



Sources: MSCI data, Bloomberg, Guinness Asset Management

The charts below show the market performance of countries and sectors as measured by relevant MSCI indices.

| Sector Returns (in GBP)            | Trailing PER |
|------------------------------------|--------------|
| MSCI AC Pacific ex Japan NTR Index | 25.5         |
| Communication Services             | 31.0         |
| Consumer Discretionary             | 70.6         |
| Consumer Staples                   | 23.1         |
| Energy                             | 142.9        |
| Financials                         | 12.5         |
| Health Care                        | 54.2         |
| Industrials                        | 28.7         |
| Information Technology             | 28.7         |
| Materials                          | 23.4         |
| Real Estate                        | 21.8         |
| Utilities                          | 19.1         |

| Country Returns (in GBP)           | Trailing PER |
|------------------------------------|--------------|
| MSCI AC Pacific ex Japan NTR Index | 25.5         |
| Australia                          | 39.4         |
| China                              | 22.0         |
| Hong Kong                          | 28.6         |
| India                              | 95.2         |
| Indonesia                          | 20.1         |
| Japan                              | 30.7         |
| Korea                              | 26.1         |
| Malaysia                           | 23.7         |
| New Zealand                        | 36.1         |
| Philippines                        | 29.8         |
| Singapore                          | 18.2         |
| Taiwan                             | 21.2         |
| Thailand                           | 25.1         |

Source: Bloomberg, Calendar year 2020 data.

The strongest sector performers were Communication Services, Consumer Discretionary, Health Care and Information Technology. Within those there was a divergence between Growth and Value stocks. Companies that were more closely aligned with online services, e-commerce and related businesses in technology led the way for much of the year. Alibaba and Tencent are two large examples of these types of business. Both generate high returns on capital but neither of them would be considered Value stocks, with both failing on the dividend yield criteria in the first instance. Materials also outperformed this year which appeared to reflect the growing economic momentum in China, which has lifted the prices of industrial metals, copper and iron ore, as well as the prices of steel and cement. The largest sectors in the region are Communication Services and Consumer Discretionary, which account for 11% and 18% of the market respectively, along with Technology, which accounts for 21%, and Financials with 19%. Healthcare and Materials account for 6% each.

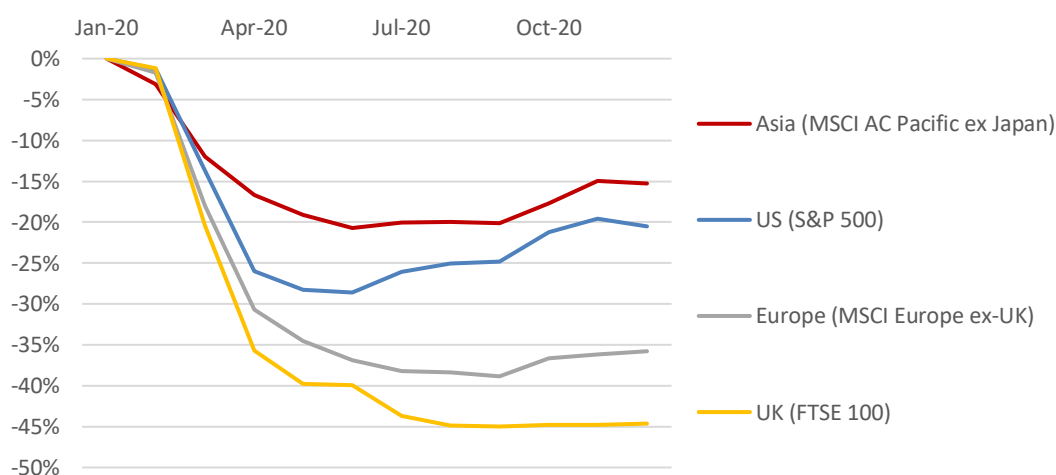
China, Korea and Taiwan were the best performers over the year. China's economic recovery, described above, delivered significant market outperformance in the first eight months of the year which faded in the last three months of 2020. Korea led the rally in Value stocks from November. It has been a cheap market on a value

basis for some time and the stock market is dominated by Samsung Electronics, which accounts for 39% of the benchmark. Other names in the top 10 by market size include SK Hynix (semiconductors), LG Chemical (petrochemicals, moving into EV batteries), Samsung SDI (a battery maker), Hyundai Motor and Posco (a steelmaker). A path toward global economic recovery, a cyclical recovery in memory chip prices and a growing market focus on electric vehicles combined to produce a sharp rally in the last two months of the year. Taiwan's market is dominated by Technology, which accounts for over 70% of the country's benchmark. Chip maker TSMC has had a strong year, as have those involved in cloud computing and software services. Electronic component manufacturers and assemblers were laggards.

Stock market returns from South and South-east Asia were weaker in 2020, mostly reflecting their experience of the pandemic. Singapore's city-state economy relies heavily on services and tourism, while Thailand's economy, in addition to tourism, also relies heavily on export manufacturing with a sizeable exposure to car makers. The Australian market benefitted from the strong rise in Materials (which accounts for 20% of the MSCI Australia Index) but was held back by the relative underperformance of Financials (32% of the market) and Health Care, which is the third largest market sector (accounting for 13%).

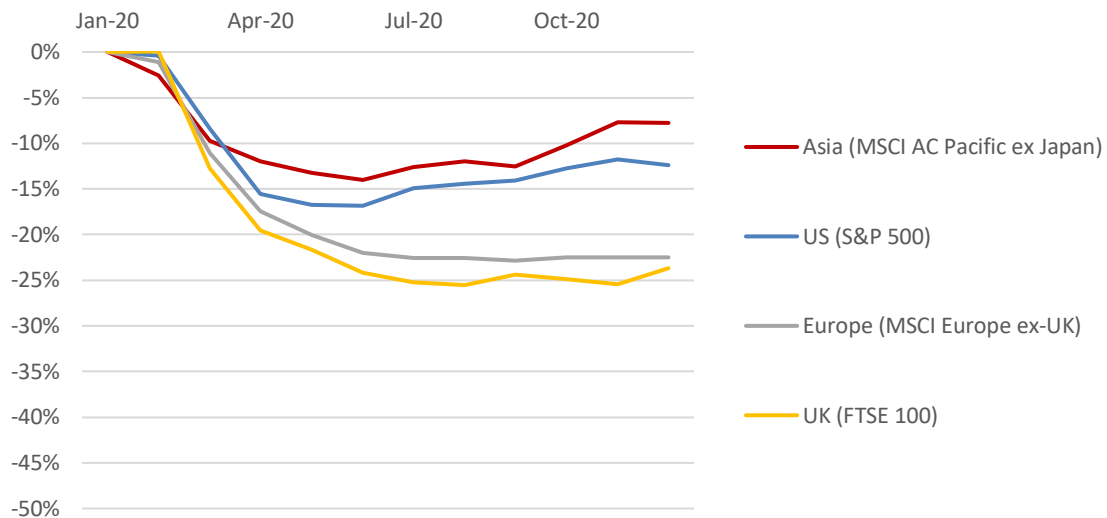
Consensus estimates of forecast earnings for 2020 and 2021 came down during the year, as they did for most markets. But what was notable was the relative shallowness of the cuts and the subsequent recovery compared to experience in developed markets. To us, this signals that at an operating level, Asia's companies appear to be more resilient and less sensitive to changes in the macroeconomic environment than they were in the past. We also think that this is supportive of the arguments that the Asian region's economy diversification, the development of consumer markets and evolution of legal, financial and trade institutions has created a much-improved investing backdrop. The charts below show the changes to consensus estimates for earnings per share in 2020 and 2021 during the past year.

### 2020 EPS estimate change during the year





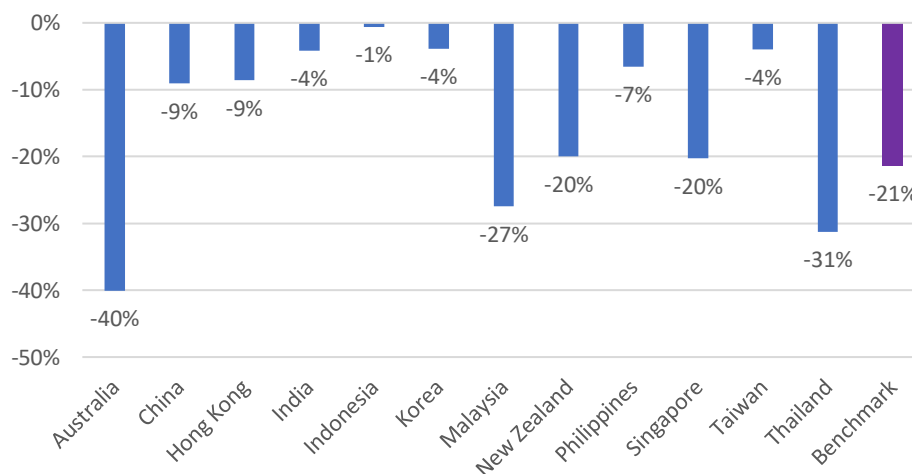
## 2021 EPS estimate change through the year



Source: Bloomberg, Guinness Asset Management. Figures are based on Analyst Consensus estimates.

At the end of 2020, the 12-month trailing dividend per share (DPS) for the benchmark was down 21.4%. The chart below shows the DPS changes by country, based on MSCI country index data. The higher yielding markets (Australia, Malaysia, Singapore, Thailand) saw the deepest cuts. When looking at country-level data we also need to be aware of specific index tilts (the high weighting of Alibaba and Tencent in China, of Samsung Electronics in Korea and TSMC in Taiwan) which can significantly affect the aggregate data. Nevertheless, there is still a useful insight: those markets with high exposures to Communication Services and Technology (China, Taiwan and Korea for example) tended to see fewer dividend cuts whereas those markets with higher exposures to non-tech Consumer Discretionary, Financials and Energy/Materials (Australia, New Zealand, Malaysia, Singapore, Thailand) tended to see greater falls. (The resilience in Indonesia's DPS is largely attributable to a significant increase in the proportion of earnings paid out, the payout ratio, by the banks, which account for 50% of the MSCI Index.)

## Index Dividend per Share change in 2020, in GBP



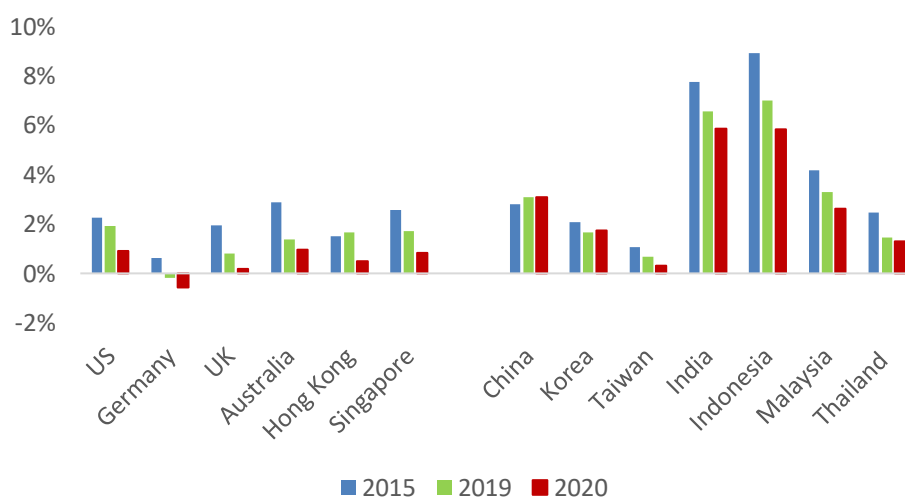
Source: MSCI Index data, Bloomberg

Most regional currencies strengthened against the US dollar and government bond yields declined. However, the decline in bond yields has been less dramatic than that seen in developed markets and thus Asian bond markets are still a relatively attractive destination for fixed income investors and made more so by a positive

exchange rate backdrop. Possibly the most significant is China, whose 10-year government bonds still yield over 3%, which compares favourably to the 0.91% yield on US 10-year Treasuries, 0.19% on UK 10-year Gilts and -0.58% on German 10-year Bunds. Of course, China is still treated as an emerging market and therefore we would expect a yield premium, but given the differential in domestic and export economic performance, higher interest rates and substantial liquidity, this market has been attracting greater interest. The appreciation of the renminbi against the dollar also mitigates concerns that gains from bond interest payments will simply be taken away by currency weakness.

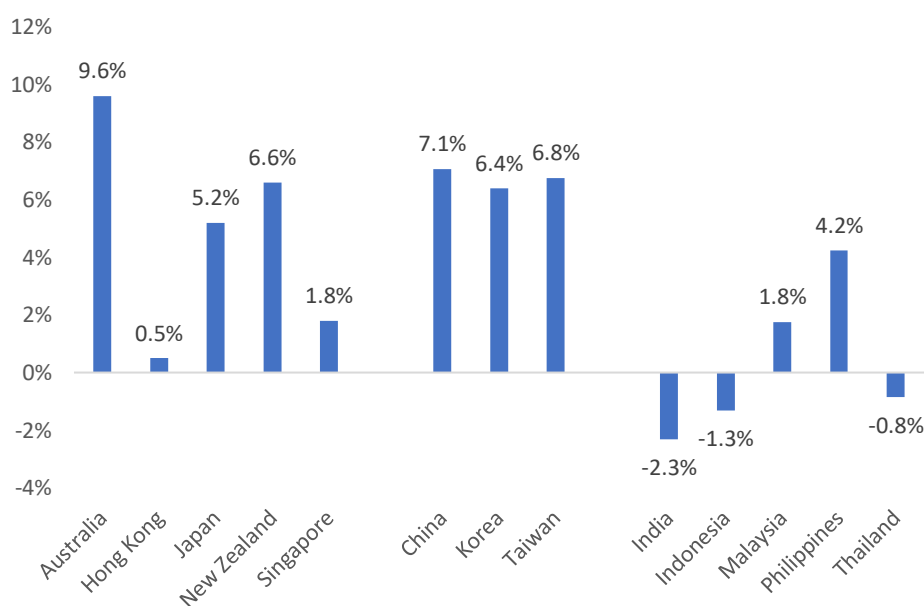
The first chart below shows the sovereign 10-year bond yields in Developed and Emerging Asia compared to the larger bond markets in Europe and US at the end of 2015, 2019 and 2020. The second chart shows the performance of Asian currencies against the US dollar in 2020.

### Active 10-Year Sovereign Bond Yields



Source: Bloomberg

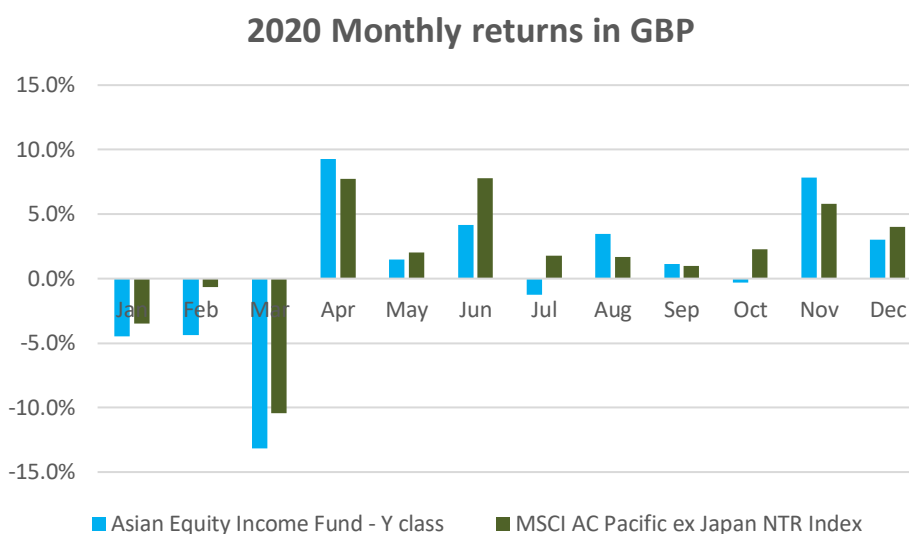
### Exchange Rates versus US dollar in 2020



Source: Bloomberg

# Fund performance

The chart below shows the performance of the Fund against its benchmark index month by month.



*Source: Financial Express, Y Class (0.99% OCF). 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 fluctuation. Fund returns shown above are for share classes with a current Ongoing Charges Figure (OCF) of 0.99%; returns for share classes with a different OCF will vary accordingly. Cumulative % gross total return, in GBP.*

The Fund rose 4.8% in GBP terms (Class Y) in 2020 compared to the benchmark which rose 19.5%. As discussed above, Growth stocks were the major drivers of market performance during the year while dividend stocks were out of favour. This is illustrated by the performance of the MSCI Asia Pacific ex Japan High Dividend Net Return Index, which fell -1.5% in GBP terms.

The Fund's dividend distribution for the GBP Class Y shares fell -14.8% for 2020 compared to the dividend per share for the benchmark which fell -21.4% in GBP terms. The Fund's dividend distribution in Sterling has increased by an average 2.0% per annum over five years, compared to the benchmark dividend per share which has declined by -0.7% on average.

In the first half of the year the Fund fell -8.4% in GBP terms, compared to the benchmark which rose 1.7%. In the second half of the year the Fund rose 14.4% versus the benchmark which rose 17.6%. Looked at on a quarterly basis, the Fund performed worse than expected in the first quarter of 2020, falling 20.7% compared to the market which fell 14.7%. Over the remaining three quarters of the year, the Fund rose 32.1% compared to the market's rise of 39%, which represents 82% upside capture and is in line with how we think the Fund ought to behave.

In the first quarter, over three quarters of the stocks in the portfolio underperformed across Consumer, Financials, Health Care, Real Estate and Technology in Australia, China, Korea, Malaysia, Singapore, Taiwan and Thailand. The common feature of many of these stocks is the consumer-oriented nature of their businesses. Many of the business models are sensitive to physical goods and movement, whether it is insurers making face-to-face sales, IT consultants providing on-site services, electronic component makers and assemblers providing consumer electronics products, banks exposed to increases in bad debt or Consumer Discretionary businesses whose custom had dropped away. All these businesses were reporting good results for the second half of 2019, but by the end of the first quarter we had entered a different world.

Our review of the portfolio indicated all had strong balance sheets with high liquidity, low debt and an ability to meet short-term debt obligations with the cash they already had on hand. The quality of company managements, products, brands and customer/supplier relationships were not in doubt in our minds; the key question was whether and how the business model for each business could thrive in this new world. The immediate market reaction toward many of the stocks was to sell. Only six stocks in the portfolio outperformed in the first quarter: Ascendas Real Estate Investment Trust (REIT) in Singapore and five Chinese companies including two banks, China Mobile, China Resources Gas and the China A-share Zhejiang Supor.

Although stock performance in the first quarter was disappointing, we felt confident that the businesses were sound, providing products and services that people wish to buy, based on solid financial platforms which provide time for established management teams to adapt the businesses to these new conditions. We have seen this play out over the course of the year with companies in the Consumer, Health Care, Technology and even Financials sector taking on market leadership. Not all share prices have fully recovered their earlier losses and this especially true among the banks, where it appears the market is looking for reported figures before giving a seal of approval. However, operational reports from the likes of DBS, Public Bank and Tisco indicate that while non-performing loans did pick up, banks were already well-provisioned, bad debt did not blow out and pressure is receding. DBS was obliged by the Singapore regulator, along with the rest of the Singapore banking sector, to cap its dividend at 60% of the prior year distribution. This already looks overly cautious and there is a pathway toward full resumption of the dividend.

For other stocks, while operating conditions have been extremely challenging, there have been opportunities to acquire businesses and assets. Both Ascendas REIT and Link REIT have acquired additional properties overseas at attractive valuations, funding this through both debt and equity. DBS has given its India strategy a boost through the acquisition of Lakshmi Vilas Bank at a distressed price. DBS India has now changed from a largely digital business with 30 branches to one that has 550 branches and 900 ATMs. Corporate Travel saw its day-to-day business dry up almost completely earlier in the year, but its flexible business model enabled the company to scale back and conserve its cash reserves. In September, Corporate Travel Management announced its intention to acquire Nebraska-based Transport & Travel Inc (T&T), 60% of whose revenues come from corporate air travel. T&T has low customer concentration and management is looking for efficiencies to deliver 30% earnings accretion.

## Dividends

The distribution for 2020 fell -14.8% compared to a market's dividend per share (as measured by the MSCI AC Pacific ex Japan Index) which fell -21.4%. In the first half, the distribution fell -23.3% while that for the second half was down -8.1%.

Those holdings in the portfolio that operate a progressive dividend policy continued to deliver on expectations. For most others, dividend policy expressed as a proportion of profits and therefore dividends per share will move in line with profits. Some Asian companies add on special dividends over and above the core distribution policy and there are no commitments to maintain this element year to year. Some companies have been obliged to cut their dividend either because of regulatory requirements or because earnings do not support the previous level. Other factors that can affect the distribution trajectory are currency movements and, finally, changes that we make to the portfolio.

The three stocks with progressive dividend policies, Aflac, Qualcomm and Sonic Healthcare, each grew their dividend between 1% and 4%. The best dividend growth from those operating a payout ratio policy came from Elite Material Co, JB Hi-Fi and China Merchants Bank, which grew dividends by 24% to 52%. The next tier of dividend growth (up 10%-16%) came from Largan Precision, Ping An Insurance, China Resources Gas, Taiwan Semiconductor, China Mobile and Tisco Financial. Stocks such as Shenzhou International, Hon Hai Precision, China Medical System and China Construction Bank grew dividends by 1%-5%. Two companies, Tech Mahindra and Novatek Microelectronics, grew their core dividend by 5% and 3% respectively and then augmented with a special dividend which increased distribution growth to 72% and 19% respectively.

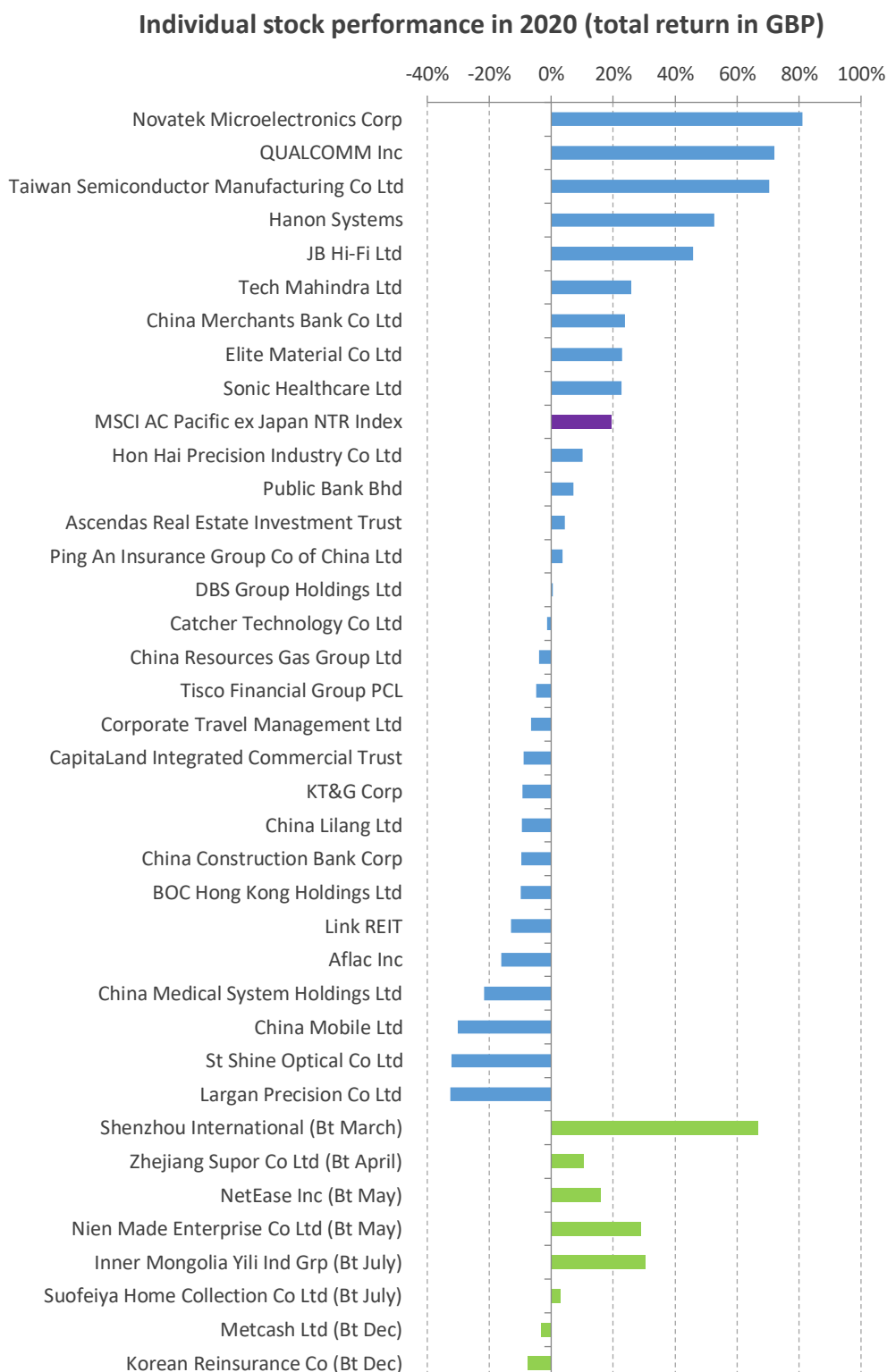
Dividend weakness came from Corporate Travel Management, which omitted the dividend entirely and instead made an acquisition, and from banks DBS Group and Public Bank in Malaysia, whose dividends fell 39% and 43% respectively. PTT in Thailand and St Shine optical in Taiwan also cut their dividends by over 30%. The other largest declines, down between -11% and -22%, came from CapitaLand Integrated Commercial Trust, Catcher Technology, China Lilang and Hanon Systems. Dividends from BOC Hong Kong and Link REIT fell 2% and 3% while those for KT&G, Nien Made Enterprise and Ascendas REIT were unchanged.

Some stocks were sold in 2020 on the basis of their dividend performance and our expectations for future performance. AAC Technologies and Godrej Consumer Products were sold when they omitted their dividends. In the case of AAC, we saw no obvious need to omit and so we took this to be an indication of management's current view of tough times ahead, especially from competition, which as opposed to Covid-19 disruption suggests longer-term challenges. The decision by Godrej to omit calls into question management's commitment to the dividend. The company has been a regular quarterly payer since 2011 but has not paid since February 2020.

Luk Fook Jewellery and Yangzijiang Shipbuilding were sold because we are not convinced in their ability to grow their dividends in coming years. This continued a process begun in 2019 of weeding out 'deep value' stocks with low or no dividend growth profiles which triggered sales of China Minsheng Bank, Industrial & Commercial Bank of China, Asustek and Pacific Textiles. These deeper-value names also had higher dividend yields and so sales of these positions has also weighed on the Fund's distribution. We believe, however, that these changes make the Fund's long-term dividend growth objective more likely to be met.

## Stock performance

The chart below shows the returns of positions held throughout the year (in blue) and the returns since purchase of new holdings (in green, with month of purchase). The Index return is also shown in purple.



Sources: Holdings, Guinness Asset Management; Returns data, Bloomberg

## Portfolio changes

### Sales

We sold eight positions in 2020.

**Li & Fung** was sold after further company re-organisation of operating divisions and amongst the management team suggested the road to recovery was going to be longer than we had anticipated.

**AAC Technologies** was sold following the omission of its dividend. There was no compelling reason to do so, in our view, based on its financial position. We concluded this was a management signal that intensifying competition and possibly lower order volumes from a key customer is forcing the company into new business channels which we suspect will have lower margins and generate lower returns on capital.

**Godrej Consumer Products** in India was a relatively recent purchase and the omission of its dividend in May was a disappointment. Here too the company put out a very positive management call. Although sales volume had dipped by 8%, the abandonment of the dividend, which they have paid quarterly and consistently since 2011, suggested either business was worse than they were suggesting or that their commitment to the dividend was not as strong as it had been. They have skipped two subsequent dividends since we sold.

**Luk Fook Holdings** in Hong Kong was sold in July. The steady deterioration of the political environment there will inevitably drag down tourist arrivals, we believe. A significant proportion of earnings come from Mainland Chinese visitors to the Hong Kong stores.

We sold **Yangzijiang Shipbuilding** on expectations that dividend growth would be flat, at best. The company has done well in picking up new orders in a depressed market, but we think the combination of lower order volumes and margin pressure will continue to weigh on profit growth and thus dividend growth.

**Janus Henderson** was sold as fee pressure has mounted on the business. The progressive dividend policy has remained and if its performance turns around, bringing a resumption of inflows, then that could be sustained. However, the consolidation we have seen in the sector, of which Janus Henderson itself is a product, illustrates some of the headwinds it faces.

At the end of the year, we sold out of **PTT**. A significant proportion of its revenues come from long-term contracts to supply gas to Thailand's state electricity generators. However, it also has a subsidiary, PTT Exploration and Production, which is directly exposed to lower (and higher) oil prices. The dividend was cut this year at these earnings fell away sharply. We waited for a recovery in the oil price and the stock before selling.

Finally, we initiated the sale of **St Shine Optical** which was not fully complete by year-end. The company is faced with lower sales volumes, excess capacity and rising competition. The dividend was cut 32% and the company will need to see a radical change in fortunes to restore it. For the present, weaker consumption in Japan, its key market, and stronger competition continue to work against it.

### Purchases

We bought eight positions in 2020.

**Shenzhou International** is a textiles and apparel manufacturer with a very diversified customer base of Japanese European and US brands. The company has production facilities in China and South-east Asia. It has generated a real return on capital of more 12% every year since 2002 and in 2020 still managed to report growth. In the last twelve months it has grown the dividend by 5% and over five years it has grown by an average 13% a year.

**Zhejiang Supor** is listed in Shenzhen and is a majority French-owned designer and distributor of kitchenware and cooking appliances. The company has generated a real return on capital that has exceeded 8% since 2005, exceeded 10% since 2009 and increased steadily to over 20% since then. The dividend has grown each year since 2011. The company's products are considered by customers to be at the premium end of the market.

**NetEase Inc** is a video games developer. The company's real return on capital has been above 10% since 2003. The company began to pay a quarterly dividend in 2014 based on core earnings, which have grown steadily. NetEase has a good pipeline of new games and upgrades to existing products which are due to come through in 2021 and through 2022.

**Nien Made Enterprise** is a Taiwanese company with operations in China and in Mexico which supplies shutters and blinds to the US, UK, Belgium, Australia and Japan. The company is a beneficiary of both home improvement spending as well as homebuilding. The company is exposed to higher PVC costs as well as the strong renminbi, which will weigh on margins, but we think these will be offset by ongoing improvements to production efficiency as well as a growing share of customised products. The company's real return on capital has exceeded 15% since 2011 and has been above 20% for the past five years.

**Inner Mongolia Yili Industrial** is a Mainland China-listed dairy company. Its real return on capital has been above 9% since 2011 and above 12% since 2012. Yili has a very stable dividend profile and has been a regular payer since 2012. Over the past five years its dividend has grown at an average annual rate of 15%, which it also delivered in the last twelve months. The dairy market is growing in China and penetration is still comparatively low.

**Suofeiya Home Collection** is the third Mainland-listed Chinese company added to the portfolio. The company makes home furnishings including cupboards, sofas and mattresses. It has increased its real return on capital from 8.5% to over 15%, a level which it has sustained consistently since 2015. Suofeiya has paid and grown its dividend each year since 2012 and over the last five years has delivered an annual average growth rate of 25% and 10% growth in the last 12 months.

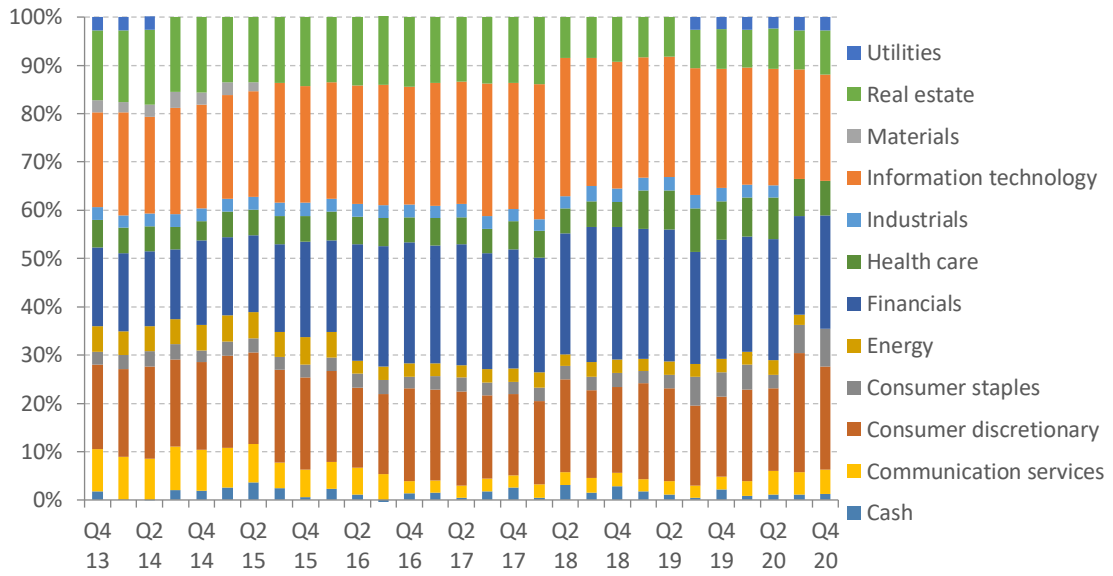
**Metcash** is an Australian food wholesaler with the third-largest position in the market. Competition is fierce in the Australian retail market, not only in food. This is nothing new and Metcash management continue to evolve their response, just as JB Hi-Fi has been obliged to do. Metcash has generated a real return on capital of above 8% for over 20 years. Prior to 2014 the company generated a return of more than 15%, but this came down following the arrival of Lidl in a market that had previously been split between Coles, Woolworth and Metcash. This prompted a significant strategy re-think and since then the company has defended its position. Since 2016 it has grown its dividend by an average 11% per year, a rate it has also delivered in the last 12 months.

**Korean Reinsurance** has generated a real return on equity in excess of 12% for over 20 years and is currently running above 15%. The company's business is around 75% Korean and 25% international. Personal lines account for 47.5% of the business while the rest is in domestic and overseas commercial. Overseas and domestic commercial business has been more challenging recently with domestic flooding and Covid-19, but there are signs of an improving domestic market with a likelihood of price hikes. It is the leading reinsurer in Korea, the second largest in Asia and 11<sup>th</sup> largest in the world.



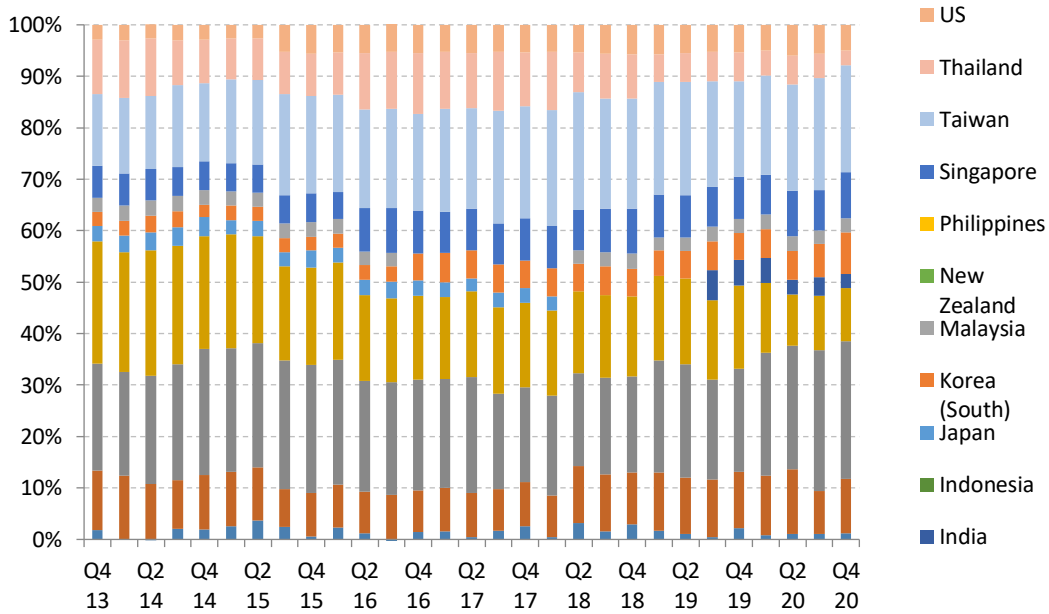
# Portfolio Position

## Fund breakdown by sector



Source: Bloomberg, Guinness Asset Management

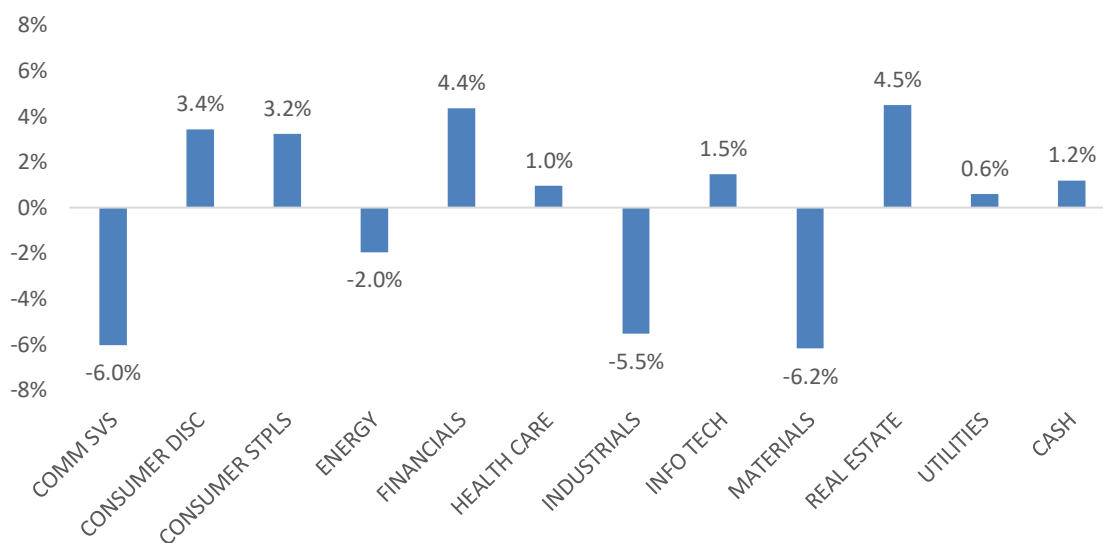
## Fund breakdown by country



Source: Bloomberg, Guinness Asset Management

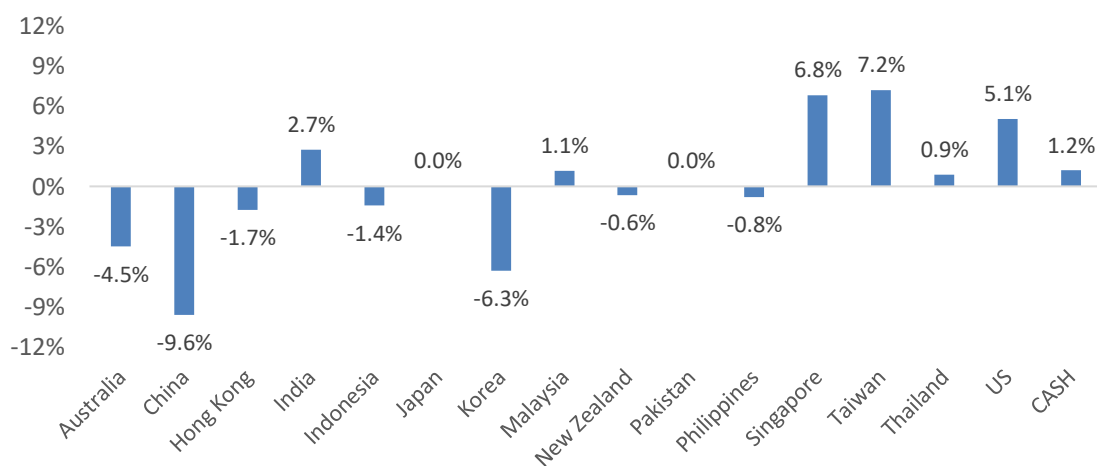
The sector and country weights relative to the benchmark at year end are shown in the charts below.

### Sector exposure relative to MSCI AC Pacific ex Japan Index



Sources: Holdings, MSCI data

### Geographic exposure relative to MSCI AC Pacific ex Japan Index



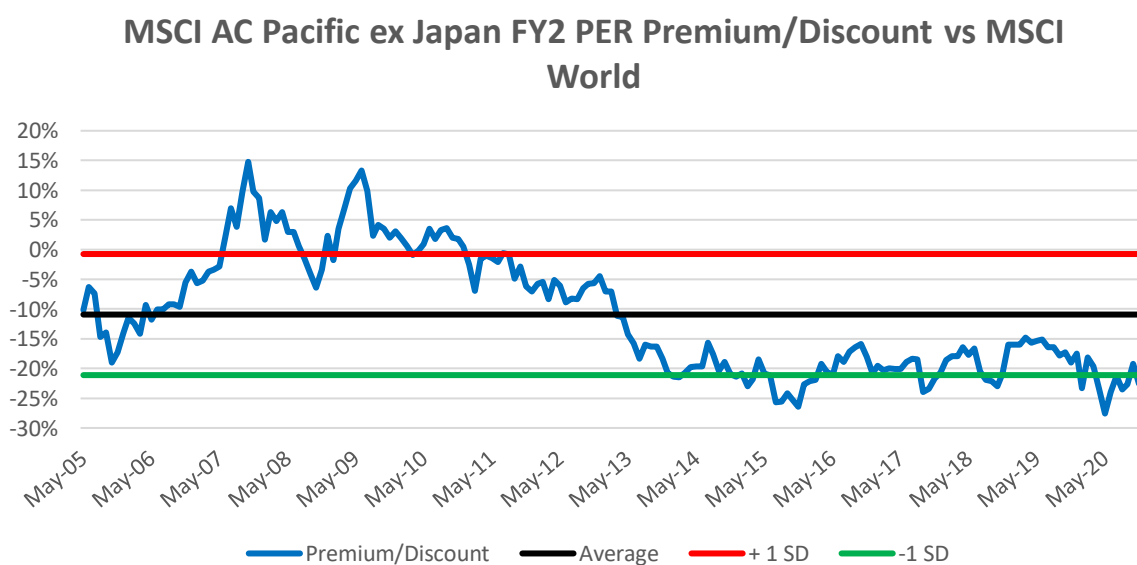
Sources: Holdings, MSCI data

# Outlook

At the end of the year the portfolio was trading on a forward Price Earnings (P/E) multiple of 13.9 times consensus estimated earnings for 2020 and 12.0 times consensus estimated earnings for 2021. This puts the Fund on a discount to the market of 30% based on consensus estimated market earnings for 2020 and 26% on 2021. This represents the widest discount to the market valuation we have seen on this Fund since it was launched and, in our view, represents a genuine value opportunity. Growth stocks have roared away while Value stocks have been left behind, even though the outlook for earnings, cash flows and dividends appear to us to be robust for our portfolio companies.

The earnings forecast by the consensus for the portfolio companies indicates a compound annual growth rate over the next three years to 2022 of 8.4% per annum while that for the market is forecast to be 11.3%. However, the forecast growth rate for the portfolio is on a rising trend as analysts' forecasts for those stocks are rising whereas the forecast growth rate for the market is being clipped back as analysts have tempered some of their earlier optimism. In December, consensus estimates for our companies increased by 1% for each of the next three years, while those for the market were scaled back by -0.3% to -1.3% over the same period, with the heaviest cuts made for the upcoming results season. This divergence in earnings forecast direction between the portfolio and the market has continued into January. This reinforces our opinion that the valuation gap between the portfolio and the market is too great and that as companies report their results we hope and expect them to support analysts' growing optimism.

The chart below compares the Price Earnings multiple, based on earnings 12 months ahead, for MSCI AC Pacific ex Japan versus MSCI World (developed markets). The red and green lines mark one standard deviation from the long-run average, which indicates the range within which this discount or premium has moved for two thirds of the time. As the chart shows, Asian valuations have recovered from their early 2020 lows following the heavy initial sell-off but remain at the lower end of their historic range. We argue that given the differential in economic performance between the region and rest of the world there is reason to hope that this discount will narrow. When we then consider that the Fund trades on a further 26% discount to Asia and is made up of companies whose balance sheets are strong, whose earnings appear to have been reasonably robust and for whom forecasts are rising, it seems the market is behind and has yet to recognise the value that is here.



Source: Bloomberg, MSCI, Guinness Asset Management. Data as of 31 December 2020

The consensus outlook for world economic growth in 2021 is 5.2% and for the US 4%, following estimated contraction in 2020 of -4.4% and -3.5% respectively. The regional economies of Asia ex Japan are expected by the consensus to expand 5.5% in 2021 following 0.8% growth in 2020. China is the dominant component in this aggregate and the economy there is expected to have grown 2.1% in 2020 and is forecast to grow 8.2% in 2021. The economies of Korea and Taiwan are expected to grow by 3%-4%, having experienced only modest contraction in 2020 in Korea and 2.4% growth in Taiwan, which is only a little below trend.

This economic differential between the region and the developed economies of Europe and US has been illustrated above in the form of shallower declines and quicker recovery in Purchasing Managers' Indices, consumer sentiment measures and in market indicators such as earnings revisions and exchange rates. We believe the region is coming out of this pandemic stronger, relative to the rest of the world; economic support in terms of expenditure has been lower as countries, especially those of North Asia, have been more effective in controlling the spread and thus limiting the economic disruption from repeated lockdowns.

Another positive sign to emerge from the past couple of years is that Asia's role in global supply chains appears to be robust, having been put to the test by US trade tariffs, sanctions and embargoes. This is another reminder, in our view, of how far the region has come in the last 25 years in terms of industrial expertise, transport links and institutional robustness. The recent trade agreement between fourteen countries seems to us to signal a new stage in development in the region and should further diversify it away from economic sensitivity to developed economies.

We therefore believe that Asia represents a good long-term investment prospect supported by stronger economies than investors have given credit for. Asian markets still trade at a significant discount to developed markets and within Asia, an enormous gap has opened up between Growth stocks that have become market favourites and Value stocks whose businesses appear to have been doing much better than expected and about whom analysts are becoming increasingly positive.

## Read more on the Fund

Visit our website for more information on the Fund and to register for regular email updates on its performance and portfolio.



### ***Keeping you updated***

Detailed portfolio and performance analysis



### ***White papers***

Our thoughts on a range of topics including: the importance of dividends; whether to meet company management; concentrated portfolio; the effectiveness of economic modelling.

To sign up for updates or search the archive, visit [guinnessfunds.com](https://www.guinnessfunds.com)

or contact our [sales team](#)

## Contact our sales team

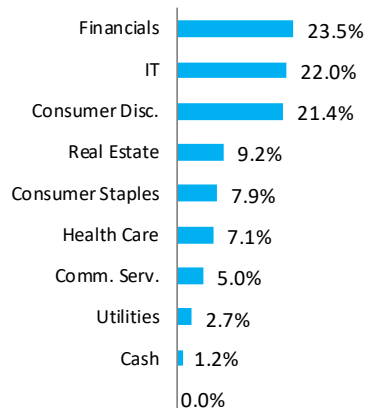
Our sales team are on hand to explain the Fund and its investment process in more detail and answer any queries you might have.

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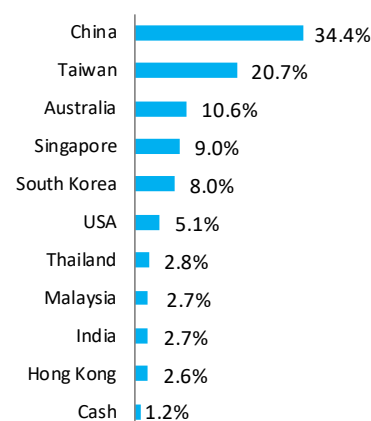
**Fund top 10 holdings**

|                                |       |
|--------------------------------|-------|
| Ascendas Real Estate Trust     | 3.8%  |
| Novatek Microelectronics       | 3.2%  |
| JB Hi-fi                       | 2.9%  |
| Hon Hai Precision Industry     | 2.9%  |
| Zhejiang Supor                 | 2.9%  |
| China Medical System           | 2.8%  |
| Tisco Financial Foreign        | 2.8%  |
| Catcher Technology             | 2.8%  |
| Taiwan Semiconductor           | 2.8%  |
| Public Bank Bhd                | 2.7%  |
| % of Fund in top 10            | 29.5% |
| Total number of stocks in Fund | 37    |

**Sector analysis**



**Geographic allocation**



**PERFORMANCE**

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

|                                | Dec '20 | Dec '19 | Dec '18 | Dec '17 | Dec '16 |
|--------------------------------|---------|---------|---------|---------|---------|
| Fund (Y class, 0.99% OCF)      | 4.8     | 14.4    | -10.3   | 24.6    | 28.2    |
| MSCI AC Pacific ex Japan Index | 19.2    | 15.7    | -9.2    | 25.1    | 28.1    |
| IA Asia Pacific ex Japan       | 20.0    | 15.8    | -9.8    | 25.3    | 25.6    |

**Cumulative % total return (GBP)**

|                                | 1 month | Year-to-date | 1 year | 3 years | From launch |
|--------------------------------|---------|--------------|--------|---------|-------------|
| Fund (Y class, 0.99% OCF)      | 3.0     | 4.8          | 4.8    | 7.6     | 105.5       |
| MSCI AC Pacific ex Japan Index | 3.8     | 19.2         | 19.2   | 25.2    | 108.9       |
| IA Asia Pacific ex Japan       | 4.6     | 20.0         | 20.0   | 25.3    | 111.1       |

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



**Risk analysis - Annualised, weekly, from launch on 19.12.2013, in GBP**

| 31/12/2020        | Index  | Sector | Fund   |
|-------------------|--------|--------|--------|
| Alpha             | 0      | 1.17   | 1.21   |
| Beta              | 1      | 0.90   | 0.89   |
| Information ratio | 0      | 0.05   | 0.00   |
| Maximum drawdown  | -26.36 | -24.54 | -24.84 |
| R squared         | 1      | 0.95   | 0.85   |
| Sharpe ratio      | 0.47   | 0.53   | 0.49   |
| Tracking error    | 0      | 3.52   | 6.01   |
| Volatility        | 15.23  | 14.01  | 14.66  |

**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. Fund launch date: 19.12.2013. Fund returns are for share classes with a current Ongoing Charges Figure (OCF) stated above; returns for share classes with a different OCF will vary accordingly.

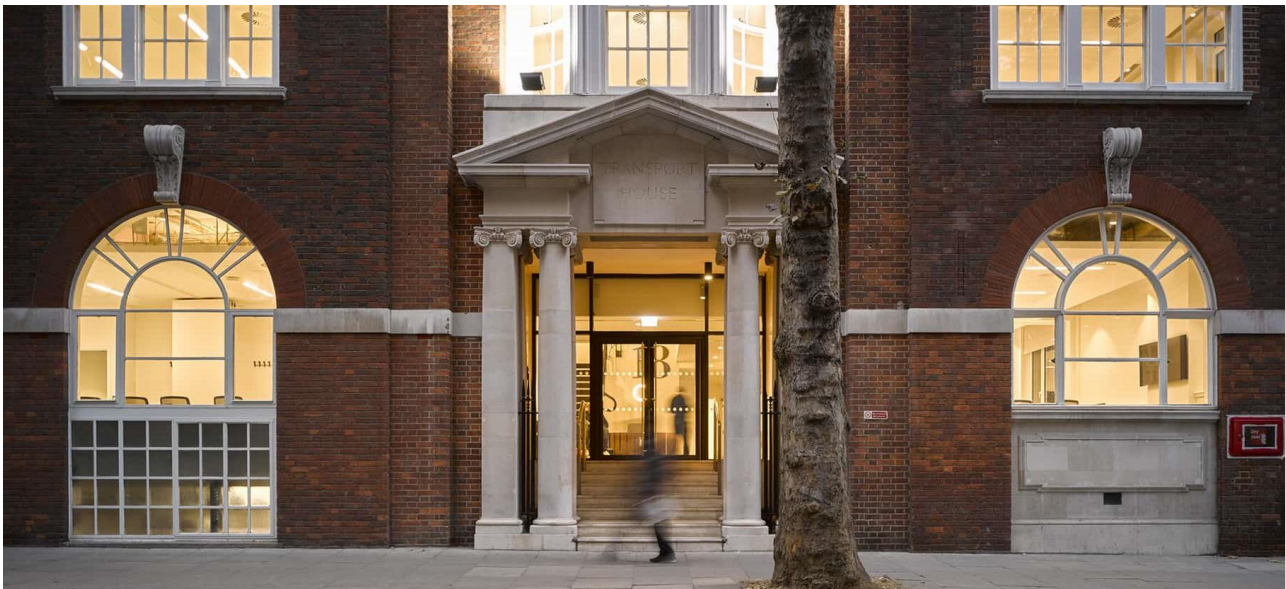
Guinness Asset Management provides a range of long-only actively managed funds to individual and institutional investors. Founded in 2003, Guinness is independent and is wholly owned by its employees.

We believe in in-house research, intelligent screening for prioritisation of research and well-designed investment processes. We manage concentrated, high conviction portfolios, with low turnover and no benchmark constraints. Since our establishment we have developed a variety of specialisms in global growth and dividend funds, global sector funds and Asian regional and country funds. The Guinness equity funds sit within an Irish-listed OEIC. They are managed alongside a range of similar SEC-registered funds offered to US investors by our US sister company, Guinness Atkinson Asset Management Inc. We also offer an Enterprise Investment Scheme (EIS service) investing in private companies across a range of sectors and an AIM EIS investing in AIM-listed companies.

### Our products

|   |                      |  |
|---|----------------------|--|
| Equity income funds                     | Global               | Global Equity Income Fund  |
|   | Regional             | European Equity Income Fund<br>Emerging Markets Equity Income Fund<br>Asian Equity Income Fund |
| Growth funds                            | Global               | Global Innovators Fund   |
| Specialist investment funds             | Energy               | Global Energy Fund<br>Sustainable Energy Fund  |
|   | Financials           | Global Money Managers Fund   |
|   | China                | Best of China Fund   |
| Tax efficient services for UK investors | EIS                  | Guinness EIS<br>AIM EIS  |
|   | Inheritance planning | Sustainable Infrastructure Service   |

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This report is primarily designed to inform you about 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.

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 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. 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

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