Guinness Best of China Fund

INVESTMENT COMMENTARY – November 2021

Launch date	**15.12.15**
Team	**Edmund Harriss** (manager) **Sharukh Malik** (manager) **Mark Hammonds**

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.

This is a marketing communication. Please refer to the prospectus and KIID for the Fund before making any final investment decisions.

Performance (in GBP) 31.10.2021

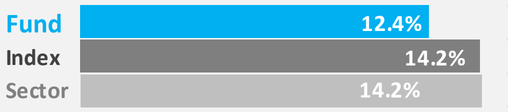
Past performance does not predict future returns

Fund	Best of China Fund (Z Cls, 0.74% OCF)
Index	MSCI Golden Dragon
Sector	IA China/Greater China

	2020	2019	2018
Fund	14.8	26.0	-20.3
Index	24.2	19.0	-9.5
Sector	33.6	22.2	-14.2

	1 year	3 years	From launch
Fund	6.6	35.7	98.4
Index	-2.1	41.5	117.8
Sector	-1.1	53.5	118.8

Annualised % total return from launch (GBP)



Risk analysis (annualised, weekly, from launch)

	Index	Sector	Fund
Alpha	0.0	0.1	-1.4
Beta	1.0	1.0	1.0
Info ratio	0.0	-0.1	-0.3
Max drwdn	-20.6	-23.8	-25.7
Tracking err	0.0	4.9	6.7
Volatility	17.9	18.2	18.9
Sharpe ratio	0.6	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: Financial Express, bid to bid, total return 0.74% OCF. Returns for share classes with a different OCF will vary accordingly

Fund & Market

- The Fund extended its lead over the benchmark on a year-to-date basis with the Fund falling 1.3% (in USD, Z class) while the MSCI Golden Dragon Net Total Return (NTR) Index has fallen 5.6% and the MSCI China Net Total Return (NTR) Index has fallen 14.0% over the year.
- In October, MSCI China rose 3.2%, MSCI Taiwan rose 0.6% and MSCI Hong Kong rose 1.3%. The CSI 300 Index rose 1.9%.
- MSCI China Value rose 2.0% while MSCI China Growth rose 4.3%.
- In China, the strongest sectors were Consumer Discretionary (+9.5%), Communication Services (+5.0%) and Consumer Staples (+2.9%), while the weakest were Health Care (-6.6%), Real Estate (-5.8%) and Energy (-5.2%).
- In Hong Kong, the Real Estate and Financials indices rose 6.4% and fell 1.8% respectively.
- In Taiwan, the Information Technology Index, which makes up more than 70% of the local market, rose 1.4%.
- In the Fund, strong performers were Geely, Lead Intelligent, Fuling Zhacai and Yili. Weaker stocks were CSPC Pharmaceutical, Sino Biopharmaceutical, Sany and Venustech.

Market Overview

- Chinese markets rallied in the first three weeks of the month before giving back some of the gains in the last week of October. This marks the pattern we have seen since the end of July, where Chinese markets have been range bound.
- Retail sales were stronger than expected, rising 4.7% (year-on-year unless stated otherwise) in October which was higher than the expected figure of 3.7%. On a two-year compound annual growth basis, retail sales grew 4.6% a year in October.
- Exports rose 2.6% month-on-month in October compared to 1.6% in September.
- Industrial production grew 3.5% in October. On a two-year compound annual growth basis, industrial production grew 5.2% a year in October.
- The real estate market remains weak. Home sale area (volume) and value fell 24% in October.
- Total social financing, the broadest measure of credit, grew 10% which was weaker than some were expecting. In light of the headwinds facing the economy, the government is not resorting to loosening monetary policy aggressively which is encouraging if China is serious about rebalancing its economy. Corporate bond issuance remains relatively weak, likely due to the property market. Banks have also moderated their lending for the same reason.
- On a more positive note, the central bank is offering discounted loans to companies involved in China's decarbonisation efforts. Banks first need to lend to the relevant company, and then are able to access re-lending facilities (worth 60% of the original loan) from the PBOC at discounted rates. The benefit of this approach is that as only 60% of the loan can be accessed at the re-lending facility, the bank still has to take on credit risk which reduces the problem of moral hazard. Additionally, this approach, which mirrors the scheme recently unveiled for small and medium enterprises (SMEs), allows the central bank to target liquidity to areas where it is needed. The traditional approach of lowering the required reserve ratio (RRR) is too blunt to achieve this goal, as the excess liquidity could potentially flow to undesirable parts of the market.

Portfolio Performance

In October, the top and bottom five contributors to performance are shown below, with the contribution to relative performance shown in brackets:

Top 5 Contributors	Top 5 Detractors
Geely (+0.4%)	Underweight in Alibaba (-1.0%)
Lead Intelligent (+0.4%)	CSPC Pharmaceutical (-0.5%)
Yili (+0.4%)	Sino Biopharmaceutical (-0.5%)
Fuling Zhacai (+0.4%)	Sany (-0.4%)
Supor (+0.4%)	Underweight in Meituan (-0.3%)

Attribution relative to the iShares MSCI China ETF.

The Fund's automobile holdings were the strongest in the portfolio, covering Geely and Lead Intelligent. Geely increased its stake in its electric vehicle (EV) brand *Zeekr*, buying a 10% stake from its parent company. Lead Intelligent, which makes equipment used in battery plants, reported third quarter results where revenue grew 17% and earnings per share (EPS) grew 10%. We think it is quite likely the company's order book should beat the company's guidance of RMB 15bn in 2021, which is equivalent to $2.4bn. The company has so far passed on rising raw material costs onto its consumers, showing its pricing power.

Price cuts in the latest round of tenders meant the Fund's pharmaceutical holdings were weak, affecting CSPC Pharmaceutical, Sino Biopharmaceutical and China Medical Systems. Price cuts are highest for generic products and lowest for more innovative drugs where high R&D capability is required. We feel that though our three healthcare holdings do have large exposure to generics, they have the ability to pivot towards the innovative end of the market. This is primarily through R&D for CSPC and Sino Biopharm, and through acquisitions for CMS.

Nari Technology reported third quarter revenue growth of 6% and EPS growth of 15%. The company is seeing good growth from its various segments and is expecting grid investment to grow at 5% a year over the next five years. This should support its grid automation business as well as its Ultra High Voltage segment.

Fuling Zhacai produces zhacai, a well-known pickled condiment. Its revenue grew 1% while its EPS fell 47% in the third quarter. The company's gross margin fell 7.3 percentage points due to higher mustard root costs, while marketing expenses rose 82% as the company attempts to build its brand and improve volumes. We are comfortable with this temporary reduction in earnings as the advertising is really a long-term investment to build the brand. In response to rising costs, Fuling Zhacai announced price increases of 3-19%, effective from November. More broadly, management think they can grow volumes by high single to low double digits by focusing on areas where consumption of zhacai is low. For example, per capita consumption of the product is RMB 5-6 in Guangdong, compared to only RMB 1-2 in Northeast China, implying potential to grow volumes.

Sany reported third quarter results where revenue fell 13% and EPS fell 36%. Sany's results were better than the industry's and it gained market share in the domestic market. Given the weakness in the property market, the growth outlook has dimmed which is reflected in the lower valuation multiple that the market is assigning the stock. Management is expecting at best flat sales in 2022 in the domestic market, while exports are expected to rise 50-60%.

Haeir's revenue fell 1% while its EPS fell 38% but excluding the deconsolidation of a business, revenue and EPS grew 9% and 15% respectively. The gross margin rose 2.4 percentage points which is impressive given rising input costs. A better mix of higher margin products and the deconsolidation of the lower margin COSMOPlat business explained this higher margin. Haier continues to hold or gain market share in its most important categories.

Stock Switches

We sold Autohome due to its lack of earnings growth. The company operates China's largest online platform for buying and selling cars. However, the ongoing chip shortage has affected car sales which is out of the company's control. Increasing competition from well-funded business is another headwind the business is facing. The market is not expecting earnings to reach 2020's level until 2024 and we do not have a strong view as to why the market is wrong.

In its place, we bought H&T Intelligent. H&T makes controllers which are used in applications such as household appliances and power tools. H&T's controllers are used in well known brands and the company is recognised for the quality of its products. The company is well placed to take advantage of growing demand for the Internet of Things (IoT), which naturally complements the existing business. H&T is also aiming to expand into the automobile market where electronic control units, which are not too dissimilar from controllers, are becoming increasingly used.

Summary view & outlook

The Chinese economy is facing various headwinds which we feel is reflected in the performance of Chinese markets this year. From an investing point of view, we think our approach on structural growth is sensible. We are looking for companies which give exposure to the various structural growth themes present in China, where even in a slower economy, they can still grow. These themes cover, but are not exclusive to, the Rise of the Middle Class, Manufacturing Upgrades and Financial Services. We look for quality companies which give exposure to these themes – the management of these companies show that in addition to giving the exposure we are looking for, they also make sensible capital allocation decisions. Finally, we are looking for the right combination of earnings growth and valuations to generate an acceptable level of return in the medium term. This process results in a portfolio where the companies in aggregate have grown sales and earnings by 10% a year for the past five years, which is in contrast to the broader market where there has been no earnings growth over the same period. We are able to achieve this while ensuring the fund is essentially trading in line with the market on a forward looking basis.

Edmund Harriss
Sharukh Malik, CFA
Portfolio Managers

Data sources

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

Index and stock data: *Bloomberg*

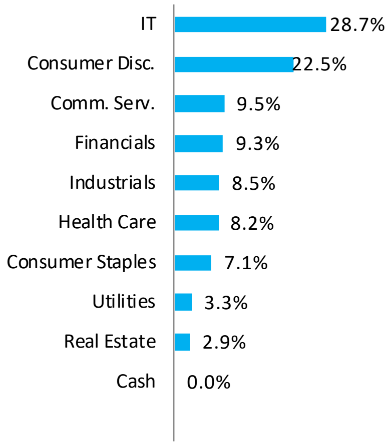
PORTFOLIO

31/10/2021

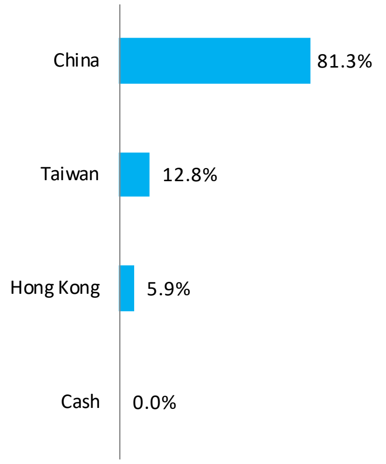
Fund top 10 holdings

Inner Mongolia Yili Industrial	3.7%
Zhejiang Supor	3.5%
China Merchants Bank	3.5%
Elite Material	3.4%
Wuxi Lead Intelligent Equipm	3.4%
JD.com	3.4%
NetEase	3.3%
Chongqing Fuling Zhacai Grou	3.3%
Novatek Microelectronics	3.3%
Geely Automobile Holdings	3.3%
% of Fund in top 10	34.3%
Total number of stocks	32

Sector analysis



Geographic allocation



PERFORMANCE

31/10/2021

Past performance does not predict future returns

Annualised % total return from launch (GBP)

Fund (Z Class, 0.74% OCF)	12.4%
MSCI Golden Dragon Index	14.2%
IA China/Greater China sector average	14.2%

Discrete years % total return (GBP)	Oct '21	Oct '20	Oct '19	Oct '18	Oct '17
Fund (Z Class, 0.74% OCF)	6.6	14.1	11.6	-13.4	25.2
MSCI Golden Dragon Index	-2.1	26.7	14.0	-10.3	21.8
IA China/Greater China sector average	-1.1	32.1	17.5	-13.0	23.8

Cumulative % total return (GBP)	1 month	Year-to-date	1 year	3 years	5 years	From launch
Fund (Z Class, 0.74% OCF)	2.0	-1.5	6.6	35.7	47.2	98.4
MSCI Golden Dragon Index	0.6	-5.9	-2.1	41.5	54.6	117.8
IA China/Greater China sector average	1.1	-7.0	-1.1	53.5	65.4	118.8

RISK ANALYSIS

31/10/2021

Annualised, weekly, from launch on 15.12.15, in GBP	Index	Sector	Fund
Alpha	0.00	0.10	-1.35
Beta	1.00	0.98	0.99
Information ratio	0.00	-0.05	-0.25
Maximum drawdown	-20.57	-23.77	-25.74
R squared	1.00	0.93	0.88
Sharpe ratio	0.58	0.56	0.45
Tracking error	0.00	4.91	6.67
Volatility	17.90	18.21	18.94

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. Returns for share classes with a different OCF will vary accordingly.

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

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 in English from www.guinnessfunds.com or free of charge from:-

- the Manager: Link Fund Manager Solutions (Ireland) Ltd (LFMSI), 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.

LFMSI, as UCITS Man Co, has the right to terminate the arrangements made for the marketing of funds in accordance with the UCITS Directive.

Investor Rights

A summary of investor rights in English is available here: https://www.linkgroup.eu/policy-statements/irish-management-company/

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. 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.

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