Guinness Global Innovators Fund

Innovation | Quality | Growth | Conviction

INVESTMENT COMMENTARY – August 2018

About the Fund

The Fund is a global growth fund designed to provide exposure to companies benefiting from innovations in technology, communication, globalisation or innovative management strategies. The Fund holds a concentrated portfolio of large and medium-sized companies in any industry and in any region.

Fund size	$214m
AUM in strategy	$450m
Fund launch date	31.10.14
Strategy launch date	01.05.03
Managers	Dr. Ian Mortimer, CFA Matthew Page, CFA

Performance 31.07.18

Cumulative % total return (GBP)	1 year	3 years	5 years	10 years
Strategy*	15.0	72.4	115.5	341.3
Index	12.4	53.8	81.9	192.9
Sector	10.2	46.0	66.6	141.5
Position in sector	48 /287	10 /256	10 /227	3 /155

Annualised % total return
from strategy inception (GBP)

Strategy*	13.21%
Index	10.18%
Sector	9.36%

Strategy	Guinness Global Innovators*
Index	MSCI World Index
Sector	IA Global

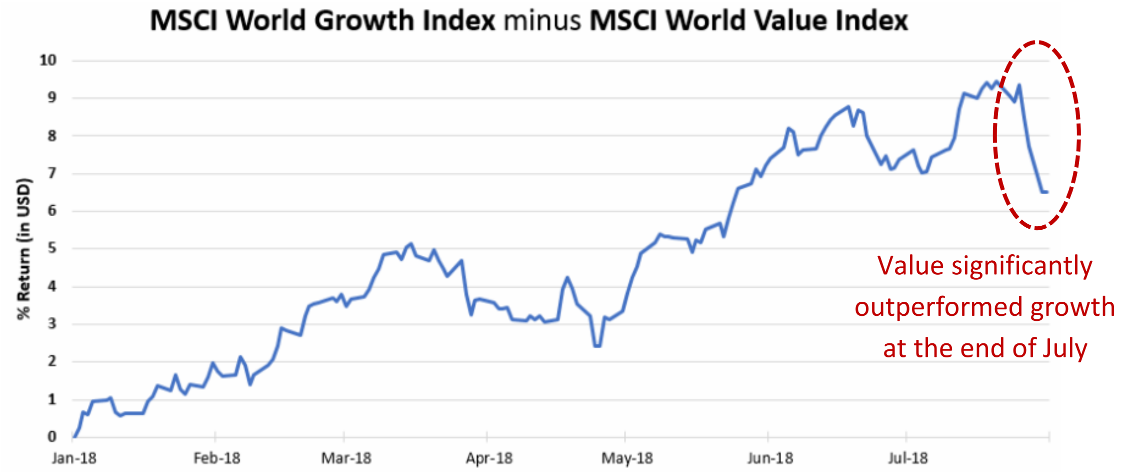
Past performance should not be taken as an indicator of future performance. The value of this investment and any income arising from it can fall as well as rise as a result of market and currency fluctuations.
***Composite simulation of performance. Guinness Global Innovators Fund (UCITS) launched on 31.10.14. Performance data prior to this date is based on the actual returns of a US mutual fund managed by the same team using the same investment process as applied to the UCITS version.** Source: Financial Express 0.99% OCF, bid to bid, total return, in GBP.

Summary performance

In July, the Guinness Global Innovators Fund produced a total return of 3.2% (Y class, in GBP) versus the MSCI World Index return of 3.8% (in GBP). The fund therefore underperformed the index by 0.6% in the month.

Underperformance in the month came largely from allocation effects, with the fund's overweight to the IT sector and underweight to Healthcare the main detractors. Stock selection was very positive in the IT sector, although partially offset by weaker stock selection in Consumer Discretionary. The fund continues to hold no positions in Real Estate, Materials, Utilities, Telcos or Consumer Staples.

Towards the end of the month we saw value outperform growth quite significantly. This is in stark contrast to most of the year so far and was triggered by disappointing results from some of the large-cap technology names. Within the portfolio this was reflected by better performance from the more moderate growth companies held, which have more 'value' characteristics and which have typically underperformed the rest of the portfolio in the first half of the year (such as Eaton and Siemens).



Source: Bloomberg. Dates: 1st January 2018 to 31st July 2018

July in Review

Global equity markets, like the weather in the northern hemisphere, showed no signs of cooling in July, as investors put aside concerns over global trade tariffs and instead focused on positive economic news releases and a strong start to the second-quarter earnings season. U.S. equities climbed to their highest levels since the market sell-off in February; disappointing results from some technology companies dampened the market's momentum, but a de-escalation of trade tensions between the U.S. and Europe helped investors regain optimism.

Trade Tariffs

On July 6th the White House imposed a 25% import tariff on US$34 billion of Chinese goods, although it notably excluded major consumer goods such as televisions and smartphones. China retaliated with an equal tariff on U.S. goods; the U.S. then threatened a 25% levy on another $16 billion of Chinese goods, possibly increasing to an additional 10% on $200 billion worth.

Because the U.S. exports only about $130 billion to China, Chinese officials would be forced to retaliate with higher tariff rates or non-tariff measures (e.g. investment restrictions, sales of U.S. assets or currency devaluation) if they are to continue to respond in kind. Since April, the Chinese Yuan has depreciated against the Dollar by roughly 9%, making U.S. goods less competitive and, to some extent, offsetting the impact of the tariffs on both the U.S. and Chinese economy.

Within the portfolio we do not own any companies directly affected by the tariffs announced so far (specifically, soy beans or steel). Effects to date have been limited to general weakness in Asian and Emerging Markets, where investors have also been considering the effects of a stronger U.S. dollar, and to companies which have more complicated supply chains or exposure to consumer demand, for example, Samsung Electronics and AAC Technologies.

During earnings season this quarter, "tariffs" remained a hot topic with over 45% of companies in the S&P500 mentioning the term on their calls. Again, within the portfolio, companies that discussed the issue did not see material impact to their business:

Eaton: “We're passing price increases equally through to all of our customers. The direct impact to us would be about $50 million of costs”

Schneider Electric: “We believe that for 2018, we could have a negative impact up to €20 million. That's a very maximum”

VF: “So far these are de minimis to us. I mean there're some relatively extraneous categories, belts, some other accessories-type things that have had a very small impact. We have a very diverse supply chain”

Earnings Season

Over two-thirds of S&P 500 companies had reported second quarter results by the end of July. According to Bloomberg, 86% of those companies beat analyst earnings expectations and 73% beat on revenues. All sectors, except for Real Estate, reported earnings growth greater than 10%.

Another major focus of this earnings season has been the mixed news coming from the FAANGs. Facebook suffered the biggest one-day loss of market value in U.S. history, dropping almost $120bn. Twitter followed Facebook in delivering disappointing results (and a fall in user numbers) and Intel said a new key chip technology would not be available until late next year. Shares in Netflix also fell when its quarterly earnings revealed disappointing viewer growth. However, Apple and Google did not disappoint.

Within the portfolio, 19 companies reported earnings in July, with 15 showing positive surprises:

Company	Date of announcement	Period	Estimate (in local)	Actual (in local)	Surprise
Baidu Inc	31/07/2018	Q2 18	16.59	21.07	27.00%
Lam Research Corp	26/07/2018	Q4 18	4.94	5.82	17.80%
Alphabet Inc	23/07/2018	Q2 18	9.50	10.58	11.30%
NIKE Inc	28/06/2018	Q4 18	0.64	0.69	8.80%
Comcast Corp	26/07/2018	Q2 18	0.60	0.65	8.00%
Roper Technologies Inc	26/07/2018	Q2 18	2.71	2.89	6.80%
Danaher Corp	19/07/2018	Q2 18	1.09	1.15	5.80%
Eaton Corp PLC	31/07/2018	Q2 18	1.33	1.39	4.80%
Check Point Software Technolog	25/07/2018	Q2 18	1.31	1.37	4.70%
New Oriental Education & Techn	24/07/2018	Q4 18	0.53	0.55	4.20%
KLA-Tencor Corp	30/07/2018	Q4 18	2.14	2.22	3.90%
PayPal Holdings Inc	25/07/2018	Q2 18	0.57	0.58	2.70%
Boeing Co/The	25/07/2018	Q2 18	3.27	3.33	1.70%
Facebook Inc	25/07/2018	Q2 18	1.72	1.74	1.50%
Samsung Electronics Co Ltd	06/07/2018	Q2 18	1,693.15	1,710.71	1.00%
Shire PLC	31/07/2018	S1 18		2.58	0.00%
SAP SE	19/07/2018	Q2 18	0.99	0.98	-1.10%
FANUC Corp	25/07/2018	Q1 19	238.48	230.73	-3.20%
Schneider Electric SE	26/07/2018	S1 18	2.01	1.93	-3.80%

Source: Bloomberg

Economics

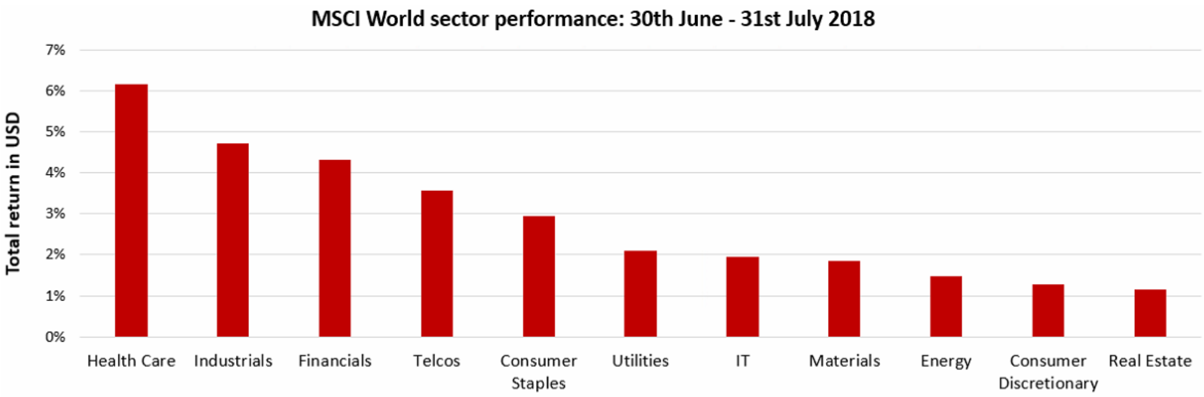
The first release of U.S. GDP shows that the economy expanded at an annual rate of 4.1% in the second quarter of 2018. Whilst this was lower than the consensus of 4.4%, it represented the highest pace of growth in four years.

In Europe, equity markets advanced as earnings releases proved to be reasonably strong and trade tensions eased after an agreement was reached between the EU and the U.S. to work together to reduce tariffs related to non-auto industrial goods. In macroeconomic news, Mario Draghi reiterated his positive view on the state of the eurozone economy but made no changes to the European Central Bank (ECB) policy or forward guidance. In fact, he supported market expectations for interest rates to remain the same until late 2019 and made clear that the ECB would not be rushed into early rate hikes by accusations of currency manipulation.

UK equity markets rose during July, a month dominated by Brexit headlines, mixed economic data and continued Sterling weakness. July saw the publication of the Government's Chequers plan, which resulted in the resignation of committed 'Brexiteers' David Davis (Secretary of State for Exiting the EU) and Boris Johnson (Foreign Secretary). This pushed Sterling weaker on fears that Prime Minister, Theresa May, could face a leadership challenge.

China's economic activity data remained soft over the month which points to a negative impact from continuous deleveraging efforts. Second quarter GDP slowed to 6.7% year-on-year, and alongside the trade tensions, lead to a weaker Chinese Yuan. This made it the worst-performing currency against the Dollar in July.

Market Update



Source: Bloomberg. As of 31st July 2018

Healthcare, Industrials and Financials were the stand-out sectors in July, though all sectors registered positive gains. Technology led early in the month, but selling pressure later increased as several large tech companies reported underwhelming results. This in fact led to value-biased stocks outperforming growth, with a broad rotation into more traditionally defensive sectors – which benefitted the portfolio since it is overweight Healthcare, Industrials and Consumer Staples.

Portfolio Update

Headlines in the month were dominated by Facebook which fell -12.5% in total over the period but suffered a 20% loss after reporting results after market on the 25th July. This was a disappointing share price reaction to quarterly numbers that beat expectations. However, the market was focussed more on the long-term guidance from the earnings call when Facebook suggested revenue growth in the coming two quarters would drop sequentially by high single digits – which roughly suggests that when we enter 2019 the company will be growing revenues around the 25% level (compared to over 40% in the past). Management also guided that operating margins would eventually settle around 35% (vs 45-50% today) as costs associated with additional security and the depreciation of higher Capex on data centres and systems begins to kick in.

But with the move down in the share price and the potentially conservative guidance given, Facebook trades only on a relatively small premium to the market on 2019 earnings – while it is still expected to grow earnings by more than 20%. This suggested to us that the market reaction was overdone. Expectations had got ahead of themselves and management rather bluntly corrected these expectations, leading to the dramatic fall. It also suggests little value ascribed to other properties such as Instagram, Messenger, WhatsApp – all of which could offer substantial growth paths in the future.

In the portfolio Facebook had been overweight relative to its target 3.3% weight as we had topped up the position after the share price fell following the Cambridge Analytica scandal. Following the 20% drop in the share price after results this month the position had moved to a small underweight, so we took the opportunity to buy shares at the lower price and bring the position back to our target 3.3%.

The second biggest faller in the month was New Oriental Education, the China-based education and education services provider, which fell 9% (in USD). The company beat expected earnings, but future guidance was reduced slightly for next quarter due to ‘seasonality’. This is in context of revenue growth moving to a range of 26-29% versus consensus of just over 30%. The company continues to reinvest in the business and grow capacity through new schools and learning centres while maintaining a gross margin around 57%. We still see the stock as good value for a business expected to grow earnings up to 30% next year.

Positive performance came from Check Point Software (up 15.5% in USD), the Israeli cyber security business, which rallied on better than expected earnings after a period of weak share price performance. Eaton, the power management company, similarly beat expectations on its earnings call but also raised guidance for the second half of 2018, dampening concern that the company had reached a peak in the cycle. KLA-Tencor and Lam Research, two relatively new additions to the portfolio which make semiconductor equipment and testing and efficiency tools, were up 14.5% and 10.3% respectively in July. The market has worried that the semiconductor cycle has peaked, but both companies beat expectations and, more importantly, guided higher for future revenue growth – suggesting the weakness we had seen in Q4 2017 results had marked a bottom for the industry. We still see good value in the semiconductor industry as we believe future demand will be stronger and more robust than we have seen historically and the valuations of companies such as KLA and Lam do not reflect the longer-term cash flow generation these companies can achieve.

Thank you for your continued support.

Portfolio Managers

Dr Ian Mortimer, CFA
Matthew Page, CFA

Analysts
Joseph Stephens
Sagar Thanki

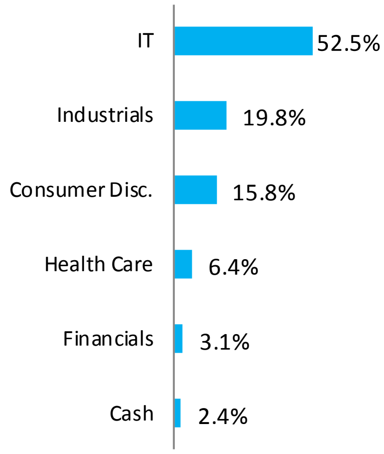
PORTFOLIO

31/07/2018

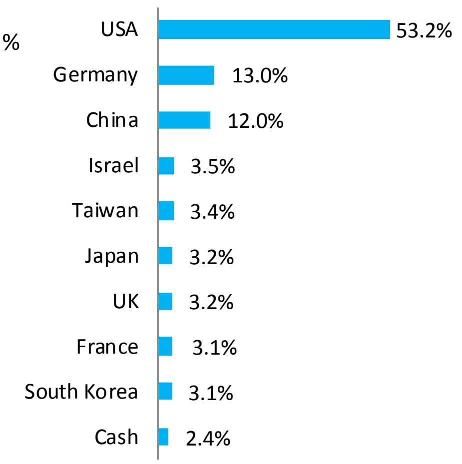
Fund top 10 holdings

KLA-Tencor	3.6%
Check Point Software	3.5%
Lam Research	3.5%
Roper Industries Inc	3.5%
Alphabet	3.4%
Catcher Technology	3.4%
Eaton	3.4%
Infineon Technologies	3.4%
Applied Materials	3.4%
Comcast Corp	3.4%
% of Fund in top 10	34.5%
Total number of stocks	30

Sector analysis

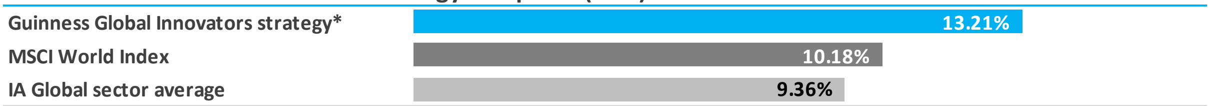


Geographic allocation



31/07/2018

Annualised % total return from strategy inception (GBP)



Discrete years % total return (GBP)

	Jul '14	Jul '15	Jul '16	Jul '17	Jul '18
Guinness Global Innovators strategy*	15.1	8.6	18.2	26.8	15.0
MSCI World Index	4.1	13.5	17.0	16.9	12.4
IA Global sector average	4.3	9.4	12.4	17.8	10.2

Cumulative % total return (GBP)

	1 month	Year-to-date	1 year	3 years	5 years	10 years
Guinness Global Innovators strategy*	3.2	6.1	15.0	72.4	115.5	341.3
MSCI World Index	3.8	6.8	12.4	53.8	81.9	192.9
IA Global sector average	2.5	5.0	10.2	46.0	66.6	141.5

RISK ANALYSIS

31/07/2018

Annualised, weekly, 5 years, in GBP	Index	Sector	Strategy*
Alpha	0	0.76	2.48
Beta	1	0.79	1.12
Information ratio	0	-0.29	0.67
Maximum drawdown	-14.03	-17.08	-17.14
R squared	1	0.78	0.87
Sharpe ratio	0.73	0.64	0.89
Tracking error	0	5.84	5.57
Volatility	12.35	11.11	14.88

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Source: Financial Express, bid to bid, total return, in GBP

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 Global Innovators 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 Global Innovators 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.

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: Capita Financial Managers (Ireland) Limited, 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.