Guinness Best of China Fund

Investment Commentary - March 2022

This is a marketing communication. Please refer to the prospectus and KIID for the Fund before making any final investment decisions. Past performance does not predict future returns.

ABOUT THE FUND

Launch date	15.12.2015
Benchmark	MSCI Golden Dragon
Sector	IA China/Greater China
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. The Fund is actively managed with the MSCI Golden Dragon used as a comparator benchmark only.

RISK

◀ Lower risk			Risk & reward			Higher risk ▶
1	2	3	4	5	**6**	7

Typically lower rewards — Typically lower rewards

The risk and reward indicator shows where the fund ranks in terms of its potential risk and return. The fund is ranked as higher risk as its price has shown high fluctuations historically. Historic data may not be a reliable indicator for the future

PERFORMANCE

Past performance does not predict future returns

28/02/2022	1 year	3 years	launch
Fund	-10.9	25.6	89.7
Index	-17.1	19.1	101.7
Sector	-19.7	23.9	96.7

Annualised % total return from launch (GBP)

Investors should note that fees and expenses are charged to the capital of the Fund. This reduces the return on your investment by an amount equivalent to the Ongoing Charges Figure (OCF). The current OCF for the share class used is 0.89%. Returns for share classes with a different OCF will vary accordingly. The performance returns do not reflect any initial charge; any such charge will also reduce the return. Source: FE fundinfo, bid to bid, total return. Source: FE fundinfo, bid to bid, total return. Launch: 15.12.15

SUMMARY

In February, the MSCI China Index fell 3.6% (in GBP unless otherwise stated), MSCI Taiwan fell 2.2% and MSCI Hong Kong fell 2.5%. The CSI 300 Index, which covers the largest stocks in the onshore market, rose 1.2%.

MSCI China Value fell 1.4% while MSCI China Growth fell 5.7%. The MSCI China A Onshore Value Index rose 1.4% while the MSCI China A Onshore Growth Index rose 2.4%.

In the MSCI China Index, the strongest sectors were Materials (total return +11.0%), Energy (+7.4%) and Consumer Staples (+2.0%), while the weakest were Communication Services (-8.7%), Consumer Discretionary (-6.9%) and Real Estate (-4.9%).

In Hong Kong, the Real Estate and Financials sectors fell 4.1% and 4.5% respectively.

In Taiwan, the Information Technology sector, which makes up more than 70% of the local market, fell 3.2%.

Russia invaded Ukraine at the end of the month, leading to a sell-off in global markets and a rise in oil and gas prices.

Average house prices in China rose 1.5% on a month-on-month basis. Though this is clearly positive, it is important to note the divergences between the various markets. House prices rose in tier 1 and 2 cities but fell in tier 3 and 4 cities, continuing the trend from December. On the other hand, housing transactions in major cities fell 27%. We have noted that multiple cities have decreased down-payment ratios which should provide a boost for the market.

The stock of total social financing, a broad measure of credit growth, grew 10.5%, which was higher than expected. The central bank has indicated this year will see front-loaded monetary easing. Delving deeper into the data shows the biggest acceleration in credit growth came from short-term corporate loans, corporate bond issuance and government bond issuance.

SUMMARY (CONTINUED)

Consumer price inflation (CPI) was 0.9% in January, much lower than 7.5% in the US and 5.5% in the UK. China's post-COVID monetary support was much milder compared to developed markets, partly explaining its much lower CPI. On the other hand, producer price inflation (PPI) was 9.1% in January in China, though it did fall from 10.3% in December and is well below October's value of 13.5%. Coal and steel prices have been falling but at the same time, oil and gas prices have been rising.

FEBRUARY IN REVIEW

Russia's invasion of Ukraine has raised the question of whether China will see this as an opportunity to take over Taiwan. Just a few months ago, the idea of an invasion in Ukraine would have been dismissed as almost inconceivable and therefore we cannot rule out a similar move by China. However, we think that whilst re-unification with Taiwan remains a strategic priority for Xi Jinping, it is not *the* priority. Indeed, there are good reasons to believe that China has been taken by surprise, not least the absence of any plan to evacuate its citizens ahead of time.

China's goal over the last 40 years has been to restore the country's economic strength and to maintain domestic stability through a steady improvement in the standard of living. This process has increased China's engagement with the world's trade and financial system. China's foreign exchange reserves are over $3 trillion, while the value of merchandise trade last year exceeded $6 trillion. Its economy is estimated to reached $18 trillion in nominal terms in 2021 (CNY 114.4 trillion according to China's National Bureau of Statistics) making it the world's second largest in aggregate, but on a per-capita basis, at $13,000 it is still a laggard.

This is something that China is trying to rectify by developing key industries which rely less on labour and more on value-add, in order to become a higher-income consumer economy. As part of this programme there have been efforts to open up to foreign investors, develop more localised centres of production to secure supply chains (which came into their own during COVID). The currency has been operated as a manged float since 2011, and on a path toward internationalisation the Yuan forms part of the International Monetary Fund's Special Drawing Rights. To become a reserve currency, one that central banks use as part of their foreign exchange reserves, the Yuan needs to be stable, liquid, and financial assets denominated in that currency (i.e. government bonds) need to be seen as a store of value.

In less than a week, the decision by Vladimir Putin has turned Russia into an international pariah. The US has demonstrated international leadership and repaired much of the damage to its European relations in the Trump years; the EU has adopted a unified stance and Germany has reversed the 75-year post-war consensus on defence; the NATO alliance has renewed relevance and has been rejuvenated. Financial sanctions unprecedented in speed and scope have closed off access to most (but not all) of Russia's avenues to external funding, and by including the central bank, have denied the country access to over $400 billion of its $640 billion foreign exchange reserves. The domestic currency has collapsed; there is no access for Russian bond issuers, government or private, to foreign funding and if they cannot (or will not) pay interest or principal those bonds will be next to worthless. This, then, is a cautionary tale for China, whose economy is built around an increasing breadth of engagement.

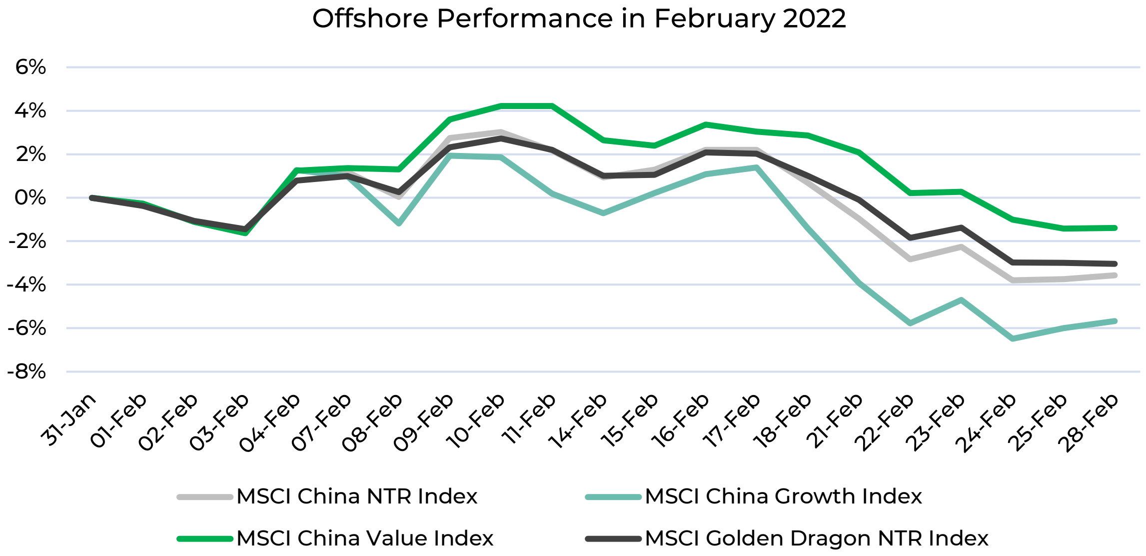
We think, therefore, that China will prioritise mitigation of the economic shock in the immediate term but there will be longer-term considerations too. In the short term, China has just announced an economic growth target of 5.5% in 2022. There are some who will point out that this is the lowest rate since 1990, but note that in 1990 China's GDP was one fiftieth its current size in real terms and its GDP per capita was $346 (1/37th the size, given the 22% growth in population between then and now). The important things to take away from this year's growth target are, first, this is a number more consistent with an economy at this stage of development and size; second, it is above the current economic growth run rate and so implies more aggressive monetary easing and support to achieve it. The current economic challenges facing China centre on the slowing property market and higher materials prices. The economic shock from the Russian invasion for China is indirect, transmitted through higher energy and commodity prices and by the potential for weaker demand for exports of manufactured goods. China sent 21% of its exports to Europe last year, which is likely to be the most affected area. Russia accounted for just 2% of China's exports in 2021. Imports from Russia (gas, oil, wheat primarily) were 2.9% of China's total in 2021, but, with a value of $78 billion, take on geopolitical significance as international sanctions tighten.

Over the longer term, China's geopolitical calculations must now factor in a set of western democracies with a more unified sense of purpose. China is also faced with an ally who seems, despite recent apparent warmth, to be pursuing its own very different agenda. In terms of the West, China has thrived in an era of division and a diminished ability of the US and Europe to respond coherently. The speed and nature of the sanctions imposed on Russia will likely lead to changes in the way and where China holds its foreign reserves. We do not expect to see selling of US Treasuries, but they may well be held in places where they are unlikely to be frozen. The exclusion of Russian banks from the SWIFT (Society for Worldwide Interbank Financial Telecommunication) messaging system makes China's own Cross-Border Interbank Payment System (CIPS) more valuable. The US threat to deny access to the US dollar market, a stick with which it enforces compliance with its sanction policies (against Iran, for example) and with which Chinese banks comply, may also cause China to accelerate the internationalisation of the Yuan. But today, the dollar still rules supreme, with over 80% of cross-border transactions dollar denominated and China's Yuan and CIPS system nowhere close to being an alternative.

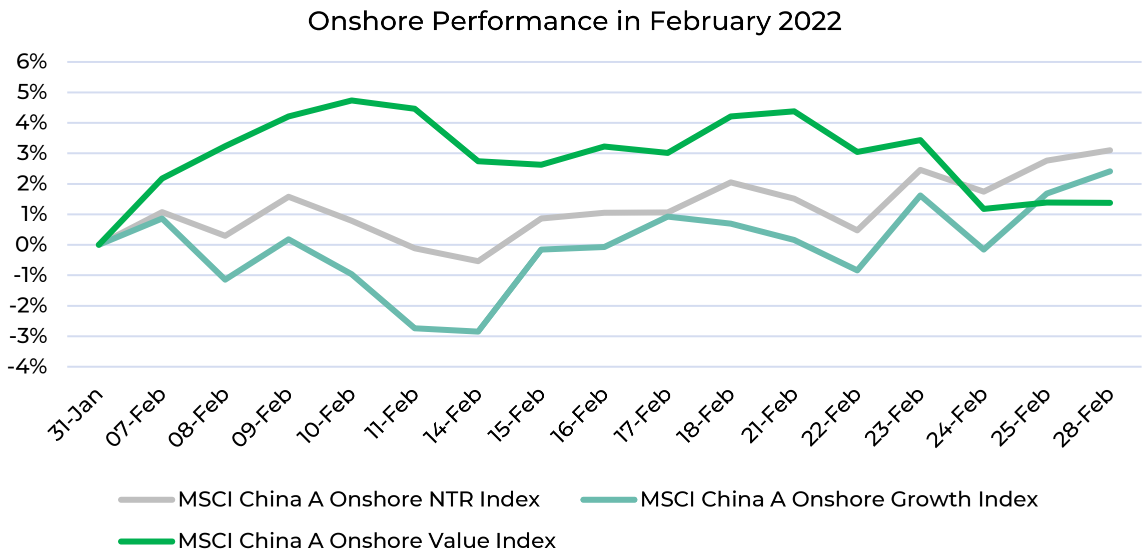
China also has a Russia problem. As discussed earlier, despite the warm words following Putin's recent meeting with Xi at the Winter Olympics, it is probable that China was not told of the invasion. Furthermore, relations between the two nations seem to be built not so much on mutual trust but on a mutual mistrust of the United States. China's Belt and Road initiative consists of both sea and land routes and is designed not only to open up trade routes but also to provide access to the resource-rich nations of central Asia. The land routes considered must pass through central Asia into Kyrgyzstan and then either south through Uzbekistan, Tajikistan and Turkmenistan, through Turkey and then into Europe or south though Kazakhstan and then though Poland into Europe. Ukraine lies in the middle of the proposed entry points into Europe.

A hearing before the Congressional United States – the China Economic and Security Review Commission in March 2015 – gives some interesting insights into some of the prevailing relationships and attitudes of these countries toward their two powerful neighbours. There are clearly cultural and religious factors at play that may indicate a predisposition toward either China or Russia but it is clear that China has made substantial progress in establishing infrastructure and large investments have been made by all the countries in the Caucasus and central Asia.

MARKETS IN REVIEW



(Data from 31/01/22 to 28/02/22, returns in GBP, source: Bloomberg and Guinness Global Investors calculations)



(Data from 31/01/22 to 28/02/22, returns in GBP, source: Bloomberg and Guinness Global Investors calculations)

In contrast to January, onshore markets were stronger in February, with the CSI 300 Index rising 1.2% and the MSCI China A Onshore Index rising 3.1%, compared to the MSCI China Index falling 3.6% and the Hang Seng Composite Index falling 3.8%. Part of the reason for the divergence was the weak performance of technology stocks, which are predominantly listed in the offshore market. Meituan was told by the government to reduce its services charges to help smaller and medium vendors on its platform. News reports indicated banks were being asked about their exposure to Ant Group, which is owned by Alibaba, and so led to weakness in Alibaba's share prices. There were also news reports suggesting Tencent and other video game developers could be subject to more regulations over their new games releases, as well as their operations in the metaverse.

PORTFOLIO HOLDINGS

Results have started to come through for the Fund's holdings.

Fuling Zhacai is a condiment manufacturer and reported its preliminary 2021 results, with revenue rising 11% and net income falling 5%. The business increased its marketing expense in the year in order to grow the business, and so we are not concerned with the fall in net income. In response to rising costs, Fuling Zhacai increased its prices, a sign of its pricing power. Looking to 2022, mustard root costs have fallen, which should boost margins.

Alibaba's results were mixed, with revenue from the customer management segment falling 1%. Though volumes increased, Alibaba is having to offer discounts in the face of intense competition. The cloud business continues to grow but its growth rate has decelerated due to the loss of Bytedance's business abroad. We continue to hold Alibaba because it is China's largest e-commerce platform and should benefit from network effects, but we are aware the business is facing headwinds. We limit our exposure to Alibaba through the portfolio's equally weighted nature, where each position has a neutral weight of c.3.3%. This is contrast to the MSCI China Index, where Alibaba had a weight of 9.0% as of 31/01/21.

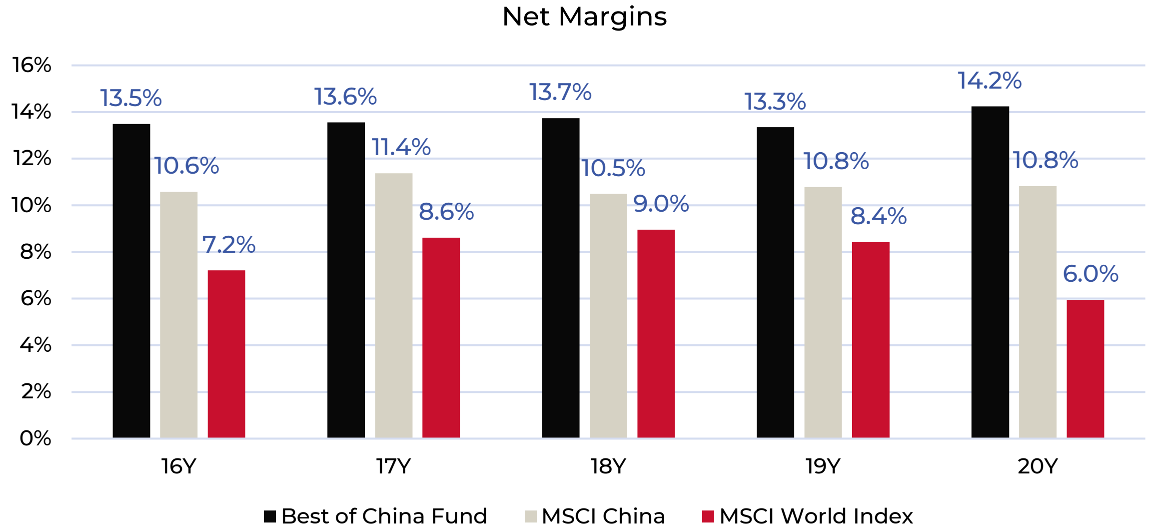
Netease, a video game developer, reported good fourth quarter results. Revenue from both mobile and PC games continue to grow robustly, boosted from the company's new Harry Potter game. The company has a good pipeline of games being developed which support future growth for the business.

Elite Material makes copper-clad laminates which are the base material for printed circuit boards (PCBs), specialising in the environmentally friendly halogen free segment of the market. Elite had a good 2021, with revenue up 41% and earnings per share (EPS) up 46%. In the fourth quarter, the server and switches business continued to grow as Elite gained market share. In spite of rising costs, the company's gross margin rose 0.3 percentage points in 2021, a sign of Elite's pricing power. We believe the company should continue to do well in the server market and should benefit from the upgrade cycle of its products.

In 2021, Xinyi Solar's revenue grew 30% and net income grew 8%. As the world's largest manufacturer of solar glass, the company benefits as the lowest-cost producer. Volumes grew in 2021 but to due to lower solar glass prices and higher input costs, net income growth lagged revenue growth. We expect the company to benefit in the coming years from greater demand for solar energy.

OUTLOOK

Russia's invasion of Ukraine has led to higher energy costs and so profit margins are likely to face some pressure. In the Fund, we have a quality filter to ensure we invest in companies with high return on capital. The return on capital can be dissected into three components: revenue growth, profitability and asset turnover. All else equal, a higher-margin business is also a higher-return on capital business.



(Data as of 31/01/22, source: Bloomberg and Guinness Global Investors calculations)

The chart above shows the Fund's net margin over the past five years, based on reported data. In each of the past five years, the Fund's net margin has been considerably higher than the MSCI China Index. The period encompasses the US-China trade war as well as disruptions caused by COVID – our companies have, in aggregate, handled this volatility well. Furthermore, in 2020, the Fund's net margin actually increased while the index's was flat. We also show the Fund's net margin relative to the MSCI World Index for interest, where we can see the Fund's positive premium increases. We believe our set of companies' superior profitability means they should be able to weather the increase in costs better than the overall market.

Portfolio Managers

Edmund Harriss

Sharukh Malik

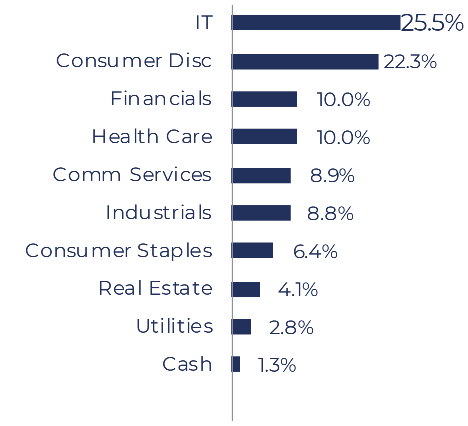
Guinness Best of China Fund

PORTFOLIO

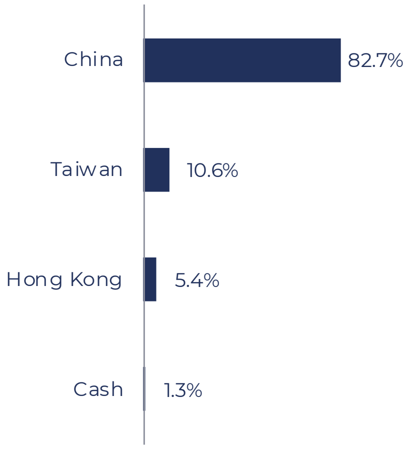
Fund top 10 holdings

Suofeiya Home Collection	4.3%
China Overseas Land	4.1%
Elite Material	3.9%
CSPC Pharmaceutical Group Ltd	3.8%
Novatek Microelectronics	3.7%
Ping An Insurance	3.6%
China Medical System	3.6%
China Merchants Bank	3.5%
Xinyi Solar	3.5%
Chongqing Fuling Zhacai	3.4%
% of Fund in top 10	37.5%
Total number of stocks	31

Sector analysis



Geographic allocation



PERFORMANCE

Past performance does not predict future returns **28/02/2022**

Annualised % total return from launch (GBP)

Discrete years % total return (GBP)	Feb '22	Feb '21	Feb '20	Feb '19	Feb '18	Feb '17
Fund (Y Class, 0.89% OCF)	-10.9	30.8	7.8	-13.3	24.8	44.9
MSCI Golden Dragon Index	-17.1	32.1	8.8	-4.5	22.9	45.0
IA China/Greater China sector average	-19.7	40.5	9.8	-7.7	27.6	41.1

Cumulative % total return (GBP)	1 Yr	3 Yrs	5 Yrs	Launch
Fund (Y Class, 0.89% OCF)	-10.9	25.6	36.0	89.7
MSCI Golden Dragon Index	-17.1	19.1	39.8	101.7
IA China/Greater China sector average	-19.7	23.9	46.0	96.7

RISK ANALYSIS **28/02/2022**

Annualised, weekly, from launch on 15.12.15, in GBP	Index	Sector	Fund
Alpha	0.00	-0.14	-0.33
Beta	1.00	0.98	0.98
Information ratio	0.00	-0.12	-0.18
Maximum drawdown	-23.49	-28.27	-25.95
R squared	1.00	0.92	0.87
Sharpe ratio	0.46	0.41	0.39
Tracking error	0.00	5.02	6.83
Volatility	17.82	18.17	18.78

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. Source: FE fundinfo bid to bid, total return (0.89% OCF). Fund launch date: 15.12.2015.

IMPORTANT INFORMATION

Issued by Guinness Global investors which is a trading name of Guinness Asset Management Limited which is 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.guinnessgi.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.