Guinness Atkinson

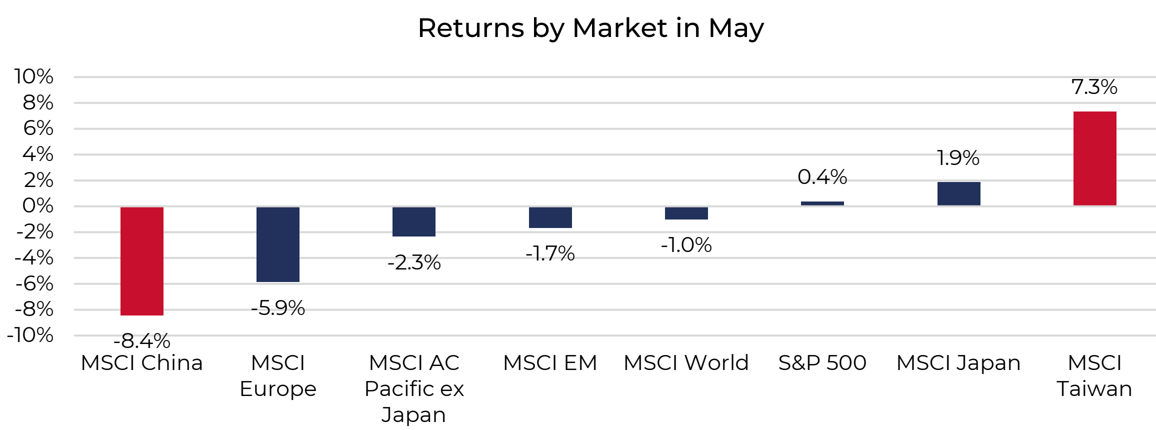
China & Hong Kong Fund

Managers' Update – Review of May 2023

Summary View

- We visited China to meet companies held in the Fund. We received updates on the latest developments for each company and spent time engaging with companies on areas of improvement, particularly with respect to disclosure. In summary, it was very encouraging to see that our companies were receptive to our ideas and were very keen to understand the perspectives of foreign shareholders.
- As a result of our trip, we noted the ongoing second wave of COVID-19 which is likely to have a short-term impact on the economy. Like we have seen in all other countries, each new wave of COVID-19 places a lower strain on the healthcare system and the economy.
- China has just lowered the reverse repo rate, the main short-term policy interest rate, by 0.1%. This marked the first cut in 10 months and is likely to lead to cuts in longer-term policy rates. This stimulus, is in our view, a sign that policymakers acknowledge the macro data has been weaker than expected. Weak manufacturing demand as well the slow property sector are the areas that should receive greater policy support.

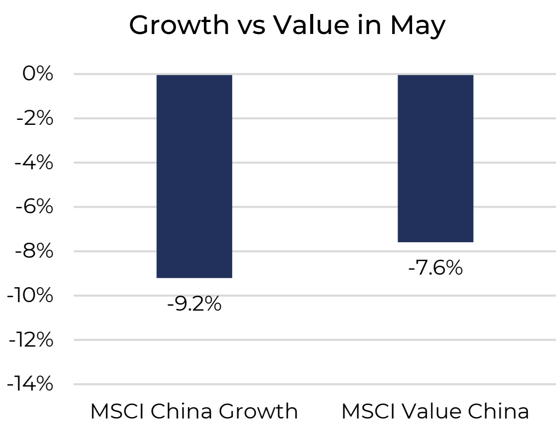
Market Review

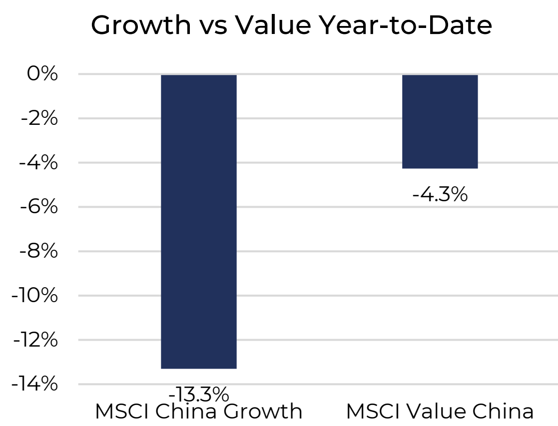


(Data from 04/30/23 to 05/31/23. Returns in USD, source: Bloomberg, Guinness Atkinson calculations)

In May, the MSCI China Index fell by 8.4% compared to the MSCI World Index which fell 1.0%. The best performing sectors in China were Utilities (total return -3.8%), Financials (-5.5%) and Communication Services (-7.7%). In a weak environment, Utilities outperformed as a defensive sector. Financials did well as deposit rates were cut, which are margin accretive for the banks. Telecom companies, which are lower rated state owned enterprises (SOEs), also did well as defensive ideas and potential beneficiaries of SOE reforms. The weakest sectors were Real Estate (-15.8%), Materials (-13.0%) and Health Care (-10.2%). Real Estate was weak as new property starts were weaker than expected. Healthcare weakness was driven by unprofitable biotech companies, which we do not invest in.

As we show below, value stocks outperformed in May, falling 7.6% compared to the growth index which fell 9.2%. This mirrors the trend we have seen year-to-date, where value stocks have fallen by 4.3% while growth stocks have fallen by 13.3%.





(Left chart: data from 04/30/23 to 05/31/23. Right chart: data from 12/31/22 to 05/31/23. Returns in USD, source: Bloomberg, Guinness Atkinson calculations)

Trip to China

In May, we traveled to China to visit some of the holdings in the Fund. The purpose of the trip was to hear about the latest business developments but more importantly, to engage with our holdings. In summary, it was very encouraging to see that our companies were receptive to our ideas and were very keen to understand the perspectives of foreign shareholders. Below we summarise the meetings we had, for the companies held in the Fund.

Venustech is a large cybersecurity company. China Mobile, which is due to become its largest shareholder, recently received approval from the relevant authority to complete the deal. Venustech is now in the process of receiving approval from the Shenzhen Stock Exchange to complete the private placement, aiming to complete the deal later this year. We spent most of the time suggesting improvements Venustech could make in its disclosures. As a cybersecurity company, labor is the main cost and here, we felt the company could disclose much more on how it trains its staff and keeps them content. We also suggested improvements to governance, including greater independence on the audit committee and supervisory board.

Shenzhen Inovance Technology is a manufacturer of industrial equipment, with a speciality in inverters, servos and robotic equipment. We had the opportunity to first visit the company's impressive showroom, where we saw the range of products sold by Inovance. The most impressive product was their six axis industrial robots, where the company aims to replicate its success in SCARA (Selective Compliance Assembly Robot Arm). Inovance is one of the better A share companies from a disclosure perspective, with good disclosure which notably improved in the set of reports covering 2022. We suggested that Inovance make the audit committee fully independent, as well that it should sign up to the UN Global Compact.

Shenzhen H&T Intelligent Control is a manufacturer of controllers for household appliances and power tools. (A controller is the chip that processes an input into the output of the device). H&T's customers include well known brands such as Electrolux, Whirlpool, Siemens, TTI (Techtronic), Hisense, Haier and Supor. As H&T's customers are diversifying their suppliers from a geographic perspective, it has set up production bases in Vietnam and Romania. This is an important point – while foreign companies are diversifying from China, Chinese companies are also willing to diversify with them. We made a range of suggestions to the company. For example, we suggested H&T disclose the opportunities available in electric vehicles and energy storage solutions. We also suggested that they disclose more policies related to labor, namely how labor relations are managed and the training and development opportunities available to staff. While internally H&T has an anti-corruption policy, we suggested that they disclose the policy to shareholders. We were given a tour of some of the production facilities which was very automated. Of note, the company uses robots to move chips in certain parts of the facilities.

China Medical System (CMS) is a pharmaceutical company which currently sources all of its revenue from generic products, but is beginning the shift towards innovative drugs. Unlike other companies which are aiming to develop new drugs from scratch, CMS is acquiring products after proof of concept. It is looking for drugs with differentiation, a large addressable market and most importantly, a high expected return on investment. Year-to-date, CMS has received approval for three innovative drugs which are expected to start contributing to revenue in 2024. CMS's disclosure is relatively good and so the main suggestion was to do with capital management. Like many companies listed in Hong Kong, CMS asks shareholders for the right to issue shares without pre-emptive rights up to a limit of 20% of the issued share capital. We feel 20% is excessive and can encourage undisciplined capital raising. CMS was open to lowering the limit, where we said 10% was a more reasonable limit.

Outlook

China's rebound post reopening has been weaker than the market was expecting but it is important to note where the weakness is coming from - it is predominantly weakness from the industrial sector, the property market and exports. Industrial production grew 5.6% year-on-year in April, benefiting from a low base. On a month-on-month basis, industrial production fell 5.7%. But producer prices fell by 3.6%, leading to lower industrial profits. In the property market, we have now seen three consecutive months of small price increases, with a 0.3% month-on-month rise in April. New home sales and completion data improved, but new home starts fell 24% in April, on a 3-month rolling basis. On the other hand, the consumption data is positive, though not as strong as initially expected. Retail sales grew by 18.4% in April.

The People's Bank of China recently cut the seven-day repo rate, the main short-term policy rate, by 0.1%. It is expected that the medium-term lending facility rate and loan prime rate will follow. Though a 0.1% cut is not significant, we argue the cut is an important signal, showing that policymakers understand the rebound has been weaker than expected. A report from Bloomberg suggests that officials have been meeting economists and business leaders to debate the best stimulus measured required to stimulate the economy. We believe further support for the property market is needed to boost overall economic growth as property and its related sectors likely account for 20% of GDP. We also acknowledge that policymakers have a tricky balancing act as if they loosen policy by too much, China is at risk of another boom-bust cycle in the property market, which would further increase its debt profile. Targeted support for high quality property developers, rather than broad based support for all, is an essential part of the solution.

Edmund Harriss (portfolio manager)

Sharukh Malik (portfolio manager)

Performance

As of 05/31/2023	YTD	1 Year	3 Year	5 Year	10 Year
China & Hong Kong Fund (ICHKX)	-11.21%	-18.67%	-5.48%	-6.13%	1.44%
Hang Seng Composite Index TR	-7.39%	-11.98%	-3.72%	-5.52%	1.90%
MSCI China Net Total Return Index	-9.07%	-14.75%	-8.82%	-7.01%	1.90%

As of 03/31/2023	YTD	1 Year	3 Year	5 Year	10 Year
China & Hong Kong Fund (ICHKX)	2.83%	-7.47%	1.06%	-2.98%	3.13%
Hang Seng Composite Index TR	2.96%	-4.20%	0.56%	-2.98%	3.15%
MSCI China Net Total Return Index	4.71%	-4.73%	-2.64%	-4.00%	3.37%

All returns over 1 year annualized. *Source: Bloomberg, Guinness Atkinson Asset Management.*

Expense Ratio: 1.71%

Performance data quoted represents past performance; past performance does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance of the Fund may be lower or higher than the performance quoted. Performance data shown is current to the most recent month and quarter end. To obtain performance as of the most recent month end, please visit www.gafunds.com or call 1-800-915-6565. Performance data does not reflect the 2% redemption fee for shares held less than 30 days and, if deducted the fee would reduce the performance noted.

The Fund's investment objectives, risks, charges and expenses must be considered carefully before investing. The statutory and summary prospectus contains this and other important information about the investment company, and it may be obtained by calling 800-915-6566 or visiting gafunds.com. Read it carefully before investing.

Investments in foreign securities involve greater volatility, political, economic and currency risks and differences in accounting methods. These risks are greater for emerging markets countries. The China and/or Hong Kong stock markets in which the Fund invests may experience periods of volatility and instability. These fluctuations may cause a security to be worth less than it was at the time of purchase. Market risk applies to individual securities, a particular sector or the entire economy. China and/or Hong Kong stocks may fall out of favor with investors, the value of Chinese currencies may decline relative to the U.S. dollar and/or China or Hong Kong stock markets may

decline generally. The Fund invests in invest in small-cap or mid-cap, which involve additional risks such as limited liquidity and greater volatility, than investments in larger companies.

One cannot invest directly in an Index.

Standard deviation is the statistical measure of market volatility, measuring how widely prices are dispersed from the average price. If prices trade in a narrow trading range, the standard deviation will return a low value that indicates low volatility.

The Shanghai Shenzhen CSI 300 Index is a market capitalization-weighted stock market index designed to replicate the performance of the top 300 A-share stocks traded in the Shanghai and Shenzhen stock exchanges.

Hang Seng Composite Total Return Index is a market capitalization weighted index that monitors the performance of stocks listed in Hong Kong.

In China, the National Bureau of Statistics (NBS) Manufacturing Purchasing Manager Index measures the performance of the manufacturing sector and is derived from a survey of more large-scale, state-owned companies. The Manufacturing Purchasing Managers Index is based on five individual indexes with the following weights: New Orders (30%), Output (25%), Employment (20%), Suppliers' Delivery Times (15%) and Stock of Items Purchased (10%), with the Delivery Times index inverted so that it moves in a comparable direction.

The Caixin PMI measures the performance of the manufacturing sector and is derived from a survey of more private companies.

MSCI AC Asia Pacific ex Japan Index is free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of countries in the Asia Pacific region.

MSCI Europe Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of European markets.

MSCI EM Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of Emerging markets in Asia, Europe, Middle East, Africa and Latin America.

MSCI China Index captures large and mid cap representation across China A shares, H shares, B shares, Red chips, P chips and foreign listings (e.g. ADRs). With 703 constituents, the index covers about 85% of this China equity universe.

The MSCI China A Index captures large and mid-cap representation across China securities listed on the Shanghai and Shenzhen exchanges. The index covers only those securities that are accessible through "Stock Connect".

MSCI Hong Kong Index is a capital weighted stock index designed to measure the performance of the large and mid cap segments of the Hong Kong market. It has 48 constituents and covers approximately 85% of the free float-adjusted market capitalization of Hong Kong equity stocks.

MSCI Japan Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of the Japanese market.

MSCI World Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed markets.

MSCI China Growth Index captures large and mid cap securities exhibiting overall growth style characteristics across the Chinese equity markets.

MSCI China Value Index captures large and mid cap Chinese securities exhibiting overall value style characteristics. The value investment style characteristics for index construction are defined using three variables: book value to price, 12-month forward earnings to price, and dividend yield.

S&P 500 Index is a market-capitalization-weighted index of leading publicly traded companies in the U.S.

American depositary receipt (ADR) refers to a negotiable certificate issued by a U.S. depositary bank representing a specified number of shares—usually one share—of a foreign company's stock. The ADR trades on U.S. stock markets as any domestic shares would.

Price/Earnings ratio (P/E) is an equity valuation multiple. It is defined as market price per share divided by annual earnings per share

Opinions expressed are subject to change, are not a guarantee and should not be considered investment advice. Past performance is not indicative of future results.

Top Fund Holdings as of 5/31/2023:

1.	NetEase Inc	4.73%
2.	NARI Technology Co Ltd	4.05%
3.	China Medical System Holdings Ltd	3.94%
4.	Baidu Inc	3.90%
5.	Shenzhen Inovance Technology Co Ltd	3.88%
6.	Venustech Group Inc	3.87%
7.	TravelSky Technology Ltd	3.74%
8.	Tencent Holdings Ltd	3.45%
9.	Ping An Insurance Group Co of China Ltd - H Shares	3.41%
10.	Inner Mongolia Yili - A Shares	3.40%

Fund holdings and sector allocations are subject to change and are not recommendations to buy or sell any security.

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