



Asia Brief
February 2009

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Welcome to the February 2009 Guinness Atkinson Asia Brief.

In the current environment when economic growth has ground almost to halt and arguments rage in developed markets over stimulus packages and bailouts it seems reasonable to ask whether emerging markets are able to provide similar large scale packages and if so, when? In short, there appears to be only one country that can and that matters on a global scale.

India is constrained by high levels of public debt, sizeable deficits and a relative lack of liquidity in the banking sector (given the high proportion of assets invested in government debt). Russia is in the throes of financial crisis with severe strains on the banking system in spite of low debts and high reserves while Brazil is held back by inflationary fears (given its history) and the need to maintain policy credibility.

This only leaves China, which moved quickly and decisively in November.

Progress has been swift. While exports to all trading partners (with the exceptions of Africa and South America) have contracted, signs of domestic activity can be seen. To be sure, imports growth has also been weak, especially pertaining to capital equipment and components which feed the manufacturing and processing trades. Falling commodity prices have also caused the value of imports to fall.

In volume terms there are positive signs. Import tonnage of crude oil and iron ore has picked up in the last couple of months while the implied price of oil per barrel is down by half from the end September 2008. We have also seen signs of re-stocking in the steel sector as steel prices have increased – especially steel for use in construction which we would expect to see given China's stated objective to boost infrastructure spending. The impact of this has been visible in the shipping market with daily shipping rate for dry bulk cargo up by a factor of three from the December low.

The other area that has attracted attention has been the increase in bank lending. The stimulus packages being launched by governments around the world will only be truly effective if they trigger additional support from the wider economy. China, with its continuing influence over the banking sector (something Western governments are also achieving whether they like it or not), is in a strong position to encourage increased lending as well as to help direct it. In the last three months new bank lending has

exploded in China. In January alone new loans of Rmb 1.6 trillion (\$237 billion) were extended which equates to 33% of all new lending in 2008.

There are of course a plethora of risks and issues of concern. The sudden jump in bank lending raises questions about where this money is going and issues of asset quality down the line. January's bank lending also saw a significant increase in discounting commercial bills – the process whereby companies can convert invoices (or specifically Trade Acceptance Bills) due to be paid within six months into ready cash now. The bank may then decide to hold the bill or to sell it on. Depending on your view this can be interpreted either as another securitization time-bomb or as a useful means of providing working capital liquidity in a market where companies are notoriously slow at paying suppliers. (There are Chinese state companies that pay their suppliers once a year only.)

Another question is where these loans are going and whether they are being used constructively. China is notorious for high investment in sectors where there is already chronic overcapacity. The government is aware of this problem, which is why bank lending to areas such as steel, aluminium and metal foundries was heavily restricted through 2005-2007, and banks were instead encouraged to lend to sectors that were capacity-constrained. Inevitably, given the strong rise in the Shanghai and Shenzhen indices, there have been suspicions that some of this extra liquidity has found its way into the domestic stock markets. While possible, there is not much evidence available to support this and plenty more to suggest that monitoring of the recipients of new lending is being stepped up, just to make sure.

The most we can say for the moment is that these are still early days; that we can see signs of activity consistent with China's aims of boosting domestic activity and that risks accompany all governments' efforts to kick start growth. From an international perspective, relations with the new US Administration appear to be good but there was real anger and frustration at Timothy Geithner's repeated assertions that the President believes China is manipulating its currency. A suggestion that China should be pressured into revaluing its currency at a time like this was greeted with disbelief inside China, and by many outside it. However, a series of private calls between the US and Chinese governments has reduced tension. Our belief is that both sides will seek to avoid trade disputes.

Market Performance Ending January 31st, 2009

| | January 2009 | 2008 | 2007 | 2006 |
|-----------------------------------|--------------|---------|--------|--------|
| Australia | -13.81% | -49.20 | 30.92% | 33.93% |
| China | -8.33% | -50.43% | 66.02% | 82.91% |
| Hong Kong | 0.45% | -50.75% | 42.06% | 30.37% |
| Indonesia | -7.68% | -56.63% | 55.81% | 73.79% |
| Korea | -3.15% | -57.11% | 32.14% | 11.17% |
| Malaysia | -2.26% | -41.11% | 48.02% | 38.26% |
| New Zealand | -8.54% | -53.26 | 11.20% | 19.43% |
| Philippines | -2.22% | -52.04% | 41.60% | 59.48% |
| Singapore | -5.98% | -47.20 | 28.86% | 47.89% |
| Taiwan | -10.25% | -46.04% | 9.16% | 20.73% |
| Thailand | -4.08% | -54.01% | 64.08% | 11.88% |
| MSCI AC Far East Free ex Japan | -5.97% | -50.56% | 36.91% | 31.86% |
| MSCI AC Pacific ex Japan* | -8.12% | -50.32% | 34.96% | 32.54% |

*MSCI AC Pacific includes Australia & New Zealand
(MSCI Indices were used for regional & individual market performance)

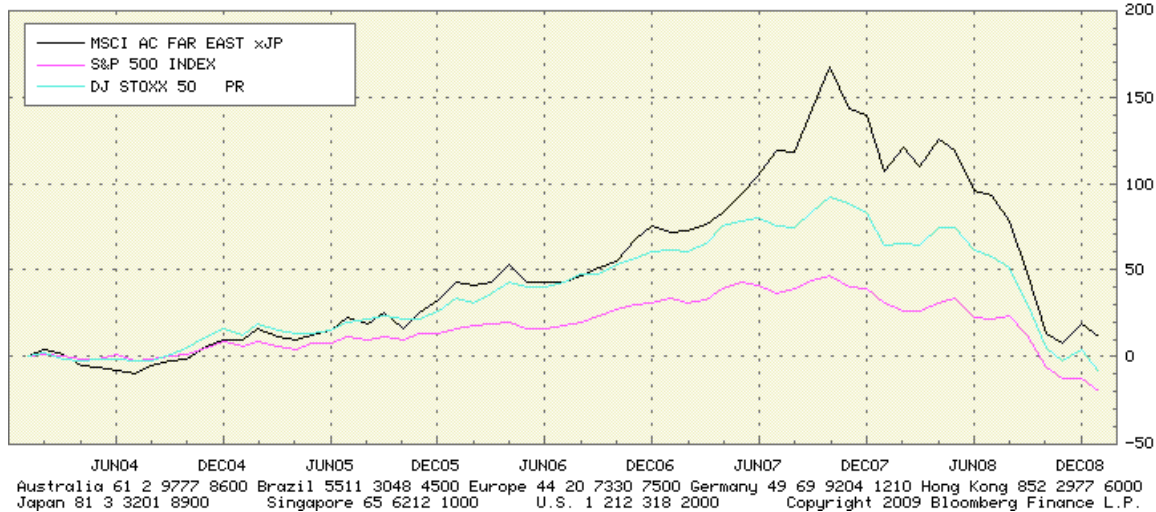
The comparative returns over five years for Asia ex Japan versus the U.S. and Europe are shown in the chart below.

COMPARATIVE RETURNS

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| Securities | Range | Crcncy | Prc | Aprr | Total Ret | Difference | Annual Eq |
|---------------|-------------------|--------|----------|------|-----------|------------|-----------|
| 1 MXFEJ Index | 1/30/04 - 1/30/09 | USD | -2.12 % | | 11.69 % | 31.19 % | 2.23 % |
| 2 SPX Index | | USD | -26.99 % | | -19.51 % | | -4.24 % |
| 3 SX5P Index | | USD | -24.29 % | | -8.89 % | 10.62 % | -1.84 % |

(* = No dividends or coupons)



Source: Bloomberg

Market Outlook

We expect that markets will continue to oscillate on changes in sentiment as to the likelihood or otherwise of an economic recovery. The data flow, as we have said, is likely to remain poor for a while yet with indicators unlikely to show signs of stabilizing until mid-year at the earliest. Even then there will be arguments over whether say, a recovery in industrial production is due to an inventory correction following an earlier production undershoot or whether is a sign of underlying demand recovery.

The path to a global recovery does, in our opinion, rest on a continuation of coordinated efforts to ensure the flow of credit, capital and trade. There is a significant risk that as time goes on and recovery appears elusive, there could be a retreat to protectionism. In this respect China's attitude toward currency policy will be important. Indications so far suggest a stable Yuan/Dollar exchange rate rather than continued appreciation.

Valuations in Asia appear attractive but these are contingent on the outlook for earnings both in Asia and outside (where relative valuations might then appear too stretched). We expect that the 2008 earnings season may trigger more cuts to profit forecasts because, as seems likely, 2008 profits will likely be awful as companies take the opportunity to make significant asset mark downs and write offs.

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Commentary for our views on Alternative Energy and Energy markets is available on our website. Please [click here](#) to view.

Performance data quoted represents past performance and does not guarantee future results. Index performance is not illustrative of Guinness Atkinson fund performance and an investment cannot be made in an index. For Guinness Atkinson Fund performance visit gafunds.com.

Mutual fund investing involves risk and loss of principal is possible. The Fund invests in foreign securities which involves greater volatility, political, economic and currency risks and differences in accounting methods. The Fund is non-diversified meaning it concentrates its assets in fewer holdings than diversified funds. Therefore, this Fund is more exposed to individual stock volatility than diversified funds.

The MSCI All Country Far East Free ex-Japan Index (MSCI AC Far East free ex-Japan Index) is a free float-adjusted, capitalization-weighted index that is designed to measure equity market performance in the Asia region excluding Japan. The Index is made up of the stock markets of China, Hong Kong, Indonesia, Korea, Malaysia, Philippines, Singapore, Taiwan and Thailand.

The MSCI All Country Pacific Free ex-Japan Index (MSCI AC Pacific Index) is a free float-adjusted, capitalization-weighted index that is designed to measure equity market performance in the Pacific region. The Index is made up of the stock markets of Australia, China, Hong Kong, Indonesia, Korea, Malaysia, New Zealand, Philippines, Singapore, Taiwan and Thailand.

The S&P 500 Index is a broad based unmanaged index of 500 stocks, which is widely recognized as representative of the equity market in general.

The Dow Jones STOXX 50 Index is a capitalization-weighted index of 50 European blue-chip stocks using free float shares in the index calculation.

One cannot invest directly in an index.

This information is authorized for use when preceded or accompanied by a prospectus for the Guinness Atkinson Funds. The prospectus contains more complete information, including investment objectives, risks, fees and expenses related to an ongoing investment in the Funds. Please read the prospectus carefully before investing.

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