Guinness Atkinson
Global Innovators Fund
Managers Update – August 2018

GUINNESS ATKINSON FUNDS

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; then the U.S. threatened a 25% levy on another $16 billion of Chinese goods, possibly increasing to an additional 10% on $200 billion worth of Chinese goods.

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 US dollar, and to companies which have more complicated supply chains and/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 US$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: Blomberg

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. While this was lower than the consensus of 4.4%, it represented the highest pace of growth in four years.

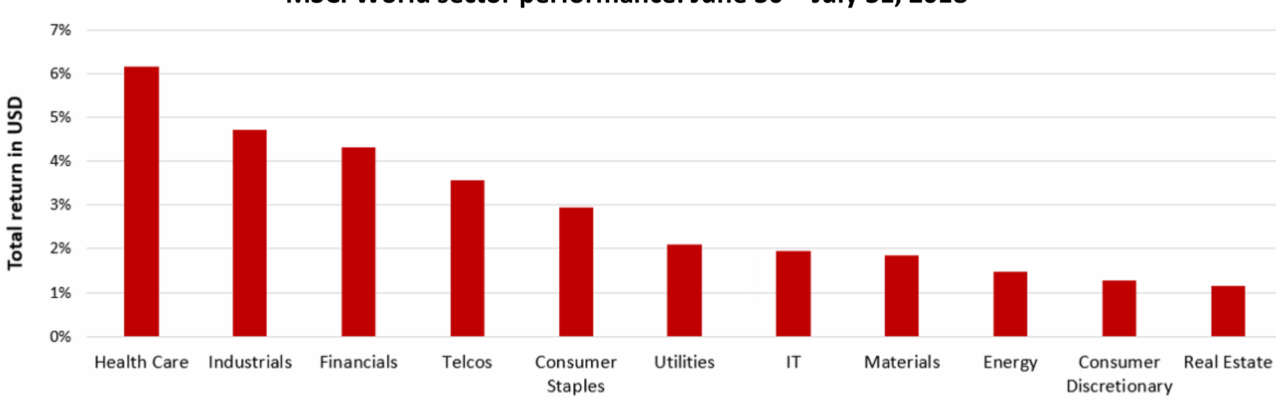
In Europe, equity markets advanced as earnings releases proved to be reasonably strong and trade tensions eased after an agreement was reached between the EU and the U.S. to work together to reduce tariffs related to non-auto industrial goods. In macroeconomic news, Mario Draghi reiterated his positive view on the state of the eurozone economy, however 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 also 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, Teresa 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

MSCI World sector performance: June 30 – July 31, 2018



Source: Bloomberg. As of July 31, 2018

Healthcare, Industrials and Financials were the standout 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 led to value-biased stocks outperforming growth, with a broad rotation into more traditionally defensive sectors – this benefitted the portfolio considering 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 July 25th. This was a disappointing share price reaction to quarterly numbers that beat expectations. However, the market was focused more on the long-term guidance given on the earnings call where 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 40%+ in the past). Management also guided that operating margins would eventually settle around 35% (vs today at 45-50%) as costs associated with additional security and the depreciation of higher Capex on data centers 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 since 2019 earnings – yet is still expected to grow earnings 20%+. This suggested to us that the market reaction was overdone. Expectations had gotten 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 fall 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 centers and has maintained 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 their 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, the two relatively new additions to the portfolio which make semiconductor equipment along with testing and efficiency tools were up 14.5% and 10.3%, respectively, in July. The market has worried that the semiconductor cycle had 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 group. We still see good value in the semiconductor industry as we believe demand will be stronger and more robust going forward 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
Sagar Thanki
Joseph Stephens

Performance

Since the beginning of the year, the Guinness Atkinson Global Innovators Fund produced a total return of 2.62% (Investor class, TR in USD), compared to the MSCI World Index return of 3.92%. The fund therefore underperformed the Index by 1.3%.

Underperformance in the month came largely from allocation effects, with the funds overweight to the IT sector and underweight to Healthcare the main detractors. Stock selection was very positive in the IT sector, however, which was 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 relatively in the first half of the year. For example, Eaton and Siemens.

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Performance

as of 07.31.2018 (in USD)	YTD	1 year	3 years annualized	5 years annualized	10 years annualized	Since inception annualized
Global Innovators, Investor Class	2.62%	14.12%	14.37%	14.20%	11.78%	8.13%
Global Innovators, Institutional Class	2.77%	14.43%	14.62%	14.35%	11.86%	8.16%
MSCI World Index	3.92%	12.50%	9.59%	10.13%	7.50%	6.03%

as of 06.30.2018 (in USD)	YTD	1 year	3 years annualized	5 years annualized	10 years annualized	Since inception annualized
Global Innovators, Investor Class	0.24%	15.84%	12.86%	14.91%	11.34%	8.03%
Global Innovators, Institutional Class	0.35%	16.13%	13.10%	15.06%	11.41%	8.07%
MSCI World Index	0.74%	11.71%	9.12%	10.59%	6.90%	5.89%

Investor class (IWIRX) Inception 12.15.1998 | Expense ratio* 1.24% (net); 1.33% (gross)

Institutional class (GINNX) Inception 12.31.2015 | Expense ratio* 0.99% (net); 1.17% (gross)

Performance data quoted represents past performance and 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. For most recent month-end and quarter-end performance, visit https://www.gafunds.com/our-funds/global-innovators-fund/#fund_performance or call (800) 915-6566.

Performance data shown for Global Innovators, Institutional Class (GINNX), prior to its launch date on 12/31/15, uses performance data from the Global Innovators, Investor Class (IWIRX).

*The Advisor has contractually agreed to reduce its fees and/or pay Fund expenses (excluding Acquired Fund Fees and Expenses, interest, taxes, dividends on short positions and extraordinary expenses) in order to limit the Fund's Total Annual Operating Expenses to .99% for the Institutional class and 1.24% for the Investor class through June 30, 2019. To the extent that the Advisor waives its fees and/or absorbs expenses to satisfy this cap, it may seek repayment of a portion or all of such amounts at any time within three fiscal years after the fiscal year in which such amounts were waived or absorbed, subject to the 0.99% for the Institutional class and 1.24% for the Investor class expense cap.

Mutual fund investing involves risk and loss of principal is possible. 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 Fund also invests in medium and smaller companies, which will involve additional risks such as limited liquidity and greater volatility. The Fund may invest in derivatives which involves risks different from, and in certain cases, greater than the risks presented by traditional investments.

Securities mentioned are not recommendations to buy or sell any security. Current and future portfolio holdings are subject to risk.

Top 10 holdings for Global Innovators Fund, as of 7/31/18:

1. NIKE Inc	4.06%
2. Alphabet Inc - A Shares	3.78%
3. PayPal Holdings Inc	3.76%
4. Cognizant Technology Solutions Corp - A Shares	3.73%
5. Cisco Systems Inc	3.72%
6. Shire PLC	3.67%
7. ANTA Sports Products Ltd	3.63%
8. The Boeing Co	3.62%
9. Roper Industries Inc	3.61%
10. Catcher Technology Co Ltd	3.57%

For a complete list of holdings for the Global Innovators Fund, please visit https://www.gafunds.com/our-funds/global-innovators-fund/#fund_holdings

This material must be preceded or accompanied by a current prospectus. You can find a current prospectus here.

Opinions expressed are subject to change at any time, are not guaranteed and should not be considered investment advice.

Earnings growth is not representative of the Fund's future performance.

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

One cannot invest directly in an index.

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