Guinness Atkinson
China & Hong Kong Fund
Review of July 2020

Summary Review & Outlook

Fund & market

- MSCI China rose 9.4% while MSCI Hong Kong fell 0.7%. The Shenzhen Component Index rose 15.4% while the Shanghai Stock Exchange Composite Index rose 13.4%.
- Chinese markets were the strongest versus other major markets. The S&P 500 rose 5.6%, MSCI Europe rose 3.8% and MSCI Japan fell 1.6%.
- In MSCI China, the strongest sectors were Materials (total return of +22.0%), Consumer Staples (+15.8%) and Consumer Discretionary (+14.4%) while the weakest were Energy (+0.7%), Financials (+3.8%) and Real Estate (+5.2%).
- In MSCI Hong Kong, the Real Estate and Financials indexes rose 0.5% and fell 6.0% respectively.
- In the Fund, positive contribution came from Industrials companies China Lesso and Haitian International, Materials companies Oriental Yuhong and Anhui Conch Cement, Consumer Discretionary firms Geely, Supor and Haier Electronics, and the wealth manager Noah Holdings.
- In the second quarter, MSCI China rose 15.3% while MSCI Hong Kong rose 9.2%. The Shenzhen Component Index rose 21.6% while the Shanghai Stock Exchange Composite Index rose 10.0%.
- In MSCI China, the strongest sectors were Health Care (total return of +37.0%), Information Technology (+32.0%) and Communication Services (+24.2%) while the weakest were Energy (-0.5%), Financials (+0.3%) and Utilities (+1.1%).
- In MSCI Hong Kong, the Real Estate and Financials indexes rose 4.4% and 12.4% respectively.
- Most of the Fund's year-to-date underperformance can be attributed to its holdings in the Information Technology sector. Weakness from Tongda Group and AAC Technologies were the main causes of underperformance and both stocks were sold. Weakness in CNOOC also was a drag on underperformance, as well as the Fund's underweight in Tencent.
- On the other hand, year-to-date we have seen strong performance from Netease (total return of +40.9%), Sino Biopharmaceutical (+35.0%) and New Oriental Education (+7.4%).

Events in July

- Second quarter GDP grew 3.2%, a marked improvement from the 6.8% fall in the first quarter.
- Industrial production grew 4.8% year-on-year (yoy) in July which was in line with June's growth. Fixed asset investment (FAI), year-to-date, remains 1.6% lower but it is clear spending has increased in the past few months as FAI grew 6.1% yoy in July and 4.1% in June.
- On the other hand, retail sales continue to lag, falling 1.1% yoy in July and 1.8% in June.
- Consumer price inflation (CPI) was 2.7% in July while producer price inflation (PPI) fell 2.4%. Food inflation was 13.2% and this was likely affected by flooding in Southern China e.g. fresh vegetable prices increased 7.9% in July. Non-food inflation was 0.0% in July as fuel costs remain depressed.

- Total social financing (TSF), a broad measure of credit, rose 12.3% month over month/12.9% yoy. Policymakers remain focused on providing credit to the economy but are trying to make sure bubbles do not form. The aim is to channel credit to small and medium enterprises.

Portfolio Switches

The changes we have made to the Fund this year are summarized below:

Sells	
Name	**Sector**
Travelsky	Information Technology
CNOOC	Energy
Tongda Group	Information Technology
AAC Technologies	Information Technology
Dali Foods	Consumer Staples
Qualcomm	Information Technology
Yangzijiang	Industrials
BOC HK	Financials
China Construction Bank	Financials

Buys	
Name	**Sector**
Zhejiang Supor	Consumer Discretionary
JD.com	Consumer Discretionary
Oriental Yuhong	Materials
Yili	Consumer Staples
Suofeiya	Consumer Discretionary
Venustech	Information Technology
CSPC Pharmaceutical	Healthcare

Sells

TravelSky supplies data for China's aviation industry. Its services include real-time flight reservation information and ticket prices, inventory control and airport passenger processing. The number of people travelling in China had fallen significantly as a result of COVID-19 and we felt the fall in the share price did not reflect this, and so sold the position. So far this has proven to be a good decision as the share has significantly lagged the benchmark.

We sold **CNOOC** after the collapse of the OPEC meeting where Russia refused to back the proposal to cut production. The returns of the business have been weak for some time and this event triggered the exit of the position. We had given time to **Tongda** to show whether its shift to "glasstic" casings could generate the same level of profitability as the traditional metal casings. This was not the case in its update in February as Tongda began to additionally face pricing pressure in its waterproof components business. **AAC Technologies** was sold after it announced a negative profit warning and significantly, in our opinion, omitted its final dividend.

Qualcomm was sold as its share price recovered from its recent declines. While the company is likely to benefit from the rollout of 5G, we think there are several threats on the horizon that the market is not paying attention to. China's determination to achieve self-sufficiency could lead to import substitution, negatively impacting Qualcomm. Greater tensions with the US may mean the Chinese government retaliates against American companies like Qualcomm and we felt this risk was too high.

Yangzijiang's return on capital has been poor for some time and in the current climate, we think it is unlikely many new orders will be coming in. **Dali Foods** has been spending more on its dividend than its capex and we questioned how the business would grow earnings over time. Concerns over the company's interest income added further concerns and we felt there were better ideas to invest in. In the present low interest rate environment, we think **BOC HK** is likely to find it difficult to grow earnings. Growth headwinds for the big banks in China also led to the sale of **China Construction Bank**.

Buys

We bought **Zhejiang Supor**, a manufacturer of small kitchen appliances. It marked our first purchase of a domestic A share. Supor has strong brand loyalty and benefits from cooperation with its French parent company, Groupe SEB e.g. Supor can use its parent's Tefal brand in its products. Supor has leading market share in woks, frypans, pots and steamers. It ranks second in the market for small domestic appliances such as electric rice cookers, slow cookers, garment steamers and dust cleaners. It is one of the few A share companies to clearly list the criteria used to determine management's compensation, and we believe management will grow the company in the future.

JD.com is one of China's largest e-commerce companies. JD is different from Alibaba in that it has built its own logistics platform so has more control over the quality of its service and the amount of inventory it holds. This means that during the worst of the lockdown, JD was better stocked than its peers and its delivery services were less interrupted. JD was initially known for selling electronics but has branched out into apparel and more recently groceries, and so has seen very strong demand this year. In the first quarter, JD's revenue grew 20%, while overall online retail consumption fell 1% according to the National Bureau of Statistics of China, highlighting its strong position. The purchase of JD.com gives the Fund more exposure to e-commerce, which is likely to see even more adoption this year as coronavirus changes consumer habits.

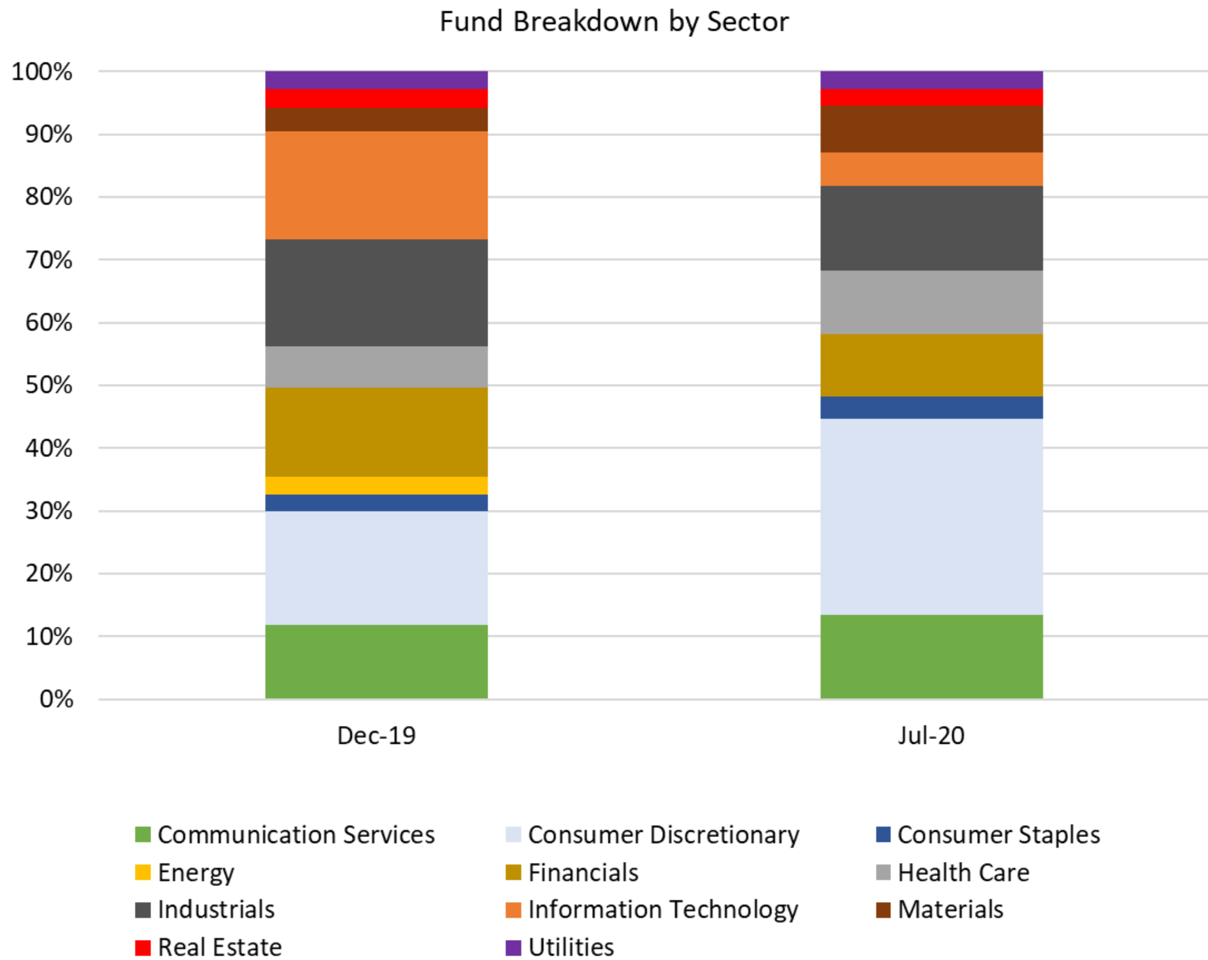
Beijing Oriental Yuhong (Yuhong) is China's largest manufacturer of waterproofing materials. Its products are used for various types of construction and we believe that Yuhong is likely to benefit from China's infrastructure stimulus. Yuhong's focus on quality and its large scale has meant it is by far the most preferred brand by developers.

In June, we significantly increased the Fund's exposure to the A share market by buying three positions. **Yili** is China's largest dairy company and should benefit as dairy consumption rises with economic growth. Yili also is the largest domestic infant formula provider. **Suofeiya** is a designer and manufacturer of furniture and kitchen cabinets. It is one of the more well-known brands in the industry and is expanding through partnerships with developers, to take advantage of the rising trend of furnished apartments in China. Suofeiya has generated a high return on capital for many years and we feel the share price is undervaluing this persistence in the business. **Venustech** is one of China's largest software security providers. Its main customers are various government departments, telecoms companies and financial institutions. Recently cybersecurity standards were strengthened and firms in critical sectors will need to conduct more stringent cybersecurity tests, which should expand the addressable market for Venustech.

CSPC Pharmaceutical is in the process of shifting its business away from generics towards more innovative drugs. It has a well-diversified portfolio and has several new drugs in the pipeline. CSPC has rapidly increased its spending on research and development (R&D) and in 2019 spent 9% of its revenue on R&D. This is close to what Sino Biopharmaceutical, an existing holding in the Fund, spends. CSPC plans on increasing its R&D spend to 10-15% revenue in the coming years which should further push the business away from low margin generics.

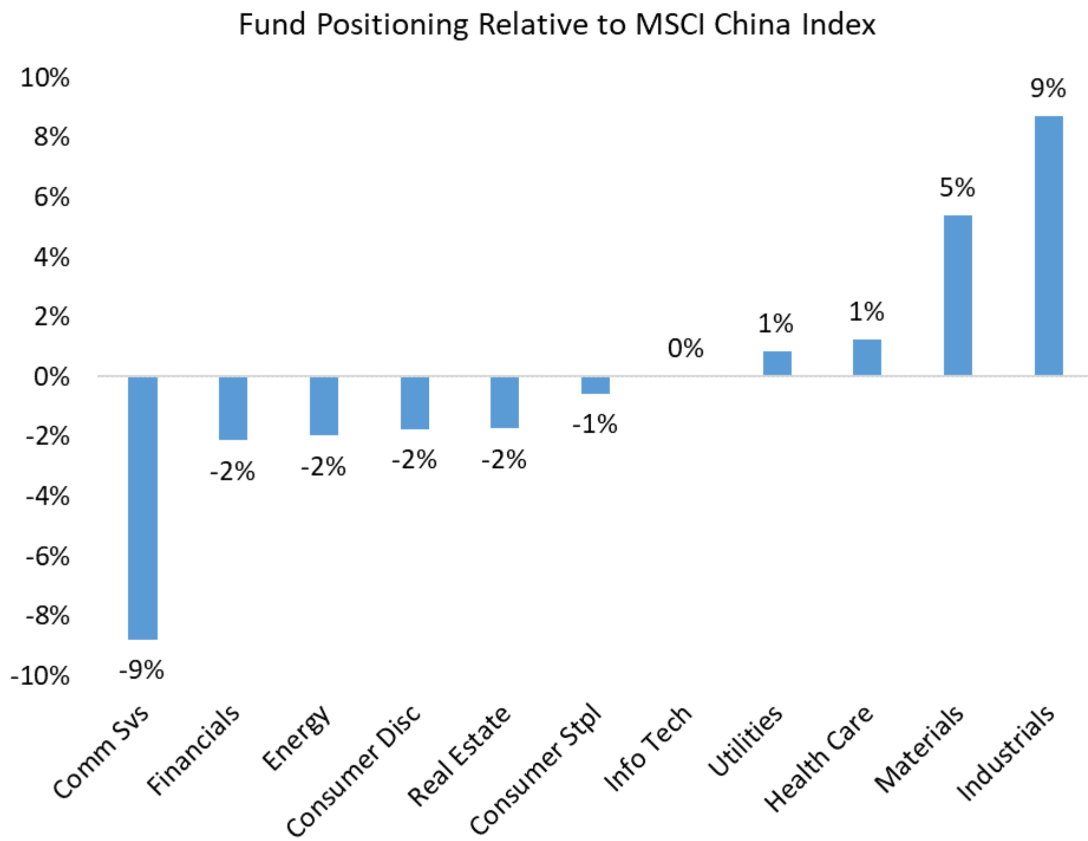
Portfolio Positioning

As a result of the changes made this year, the Fund's allocations to Information Technology and Financials have fallen by 11.9% and 4.3% respectively. Consequently, the allocations to Consumer Discretionary and Materials have risen by 13.0% and 3.7% respectively.



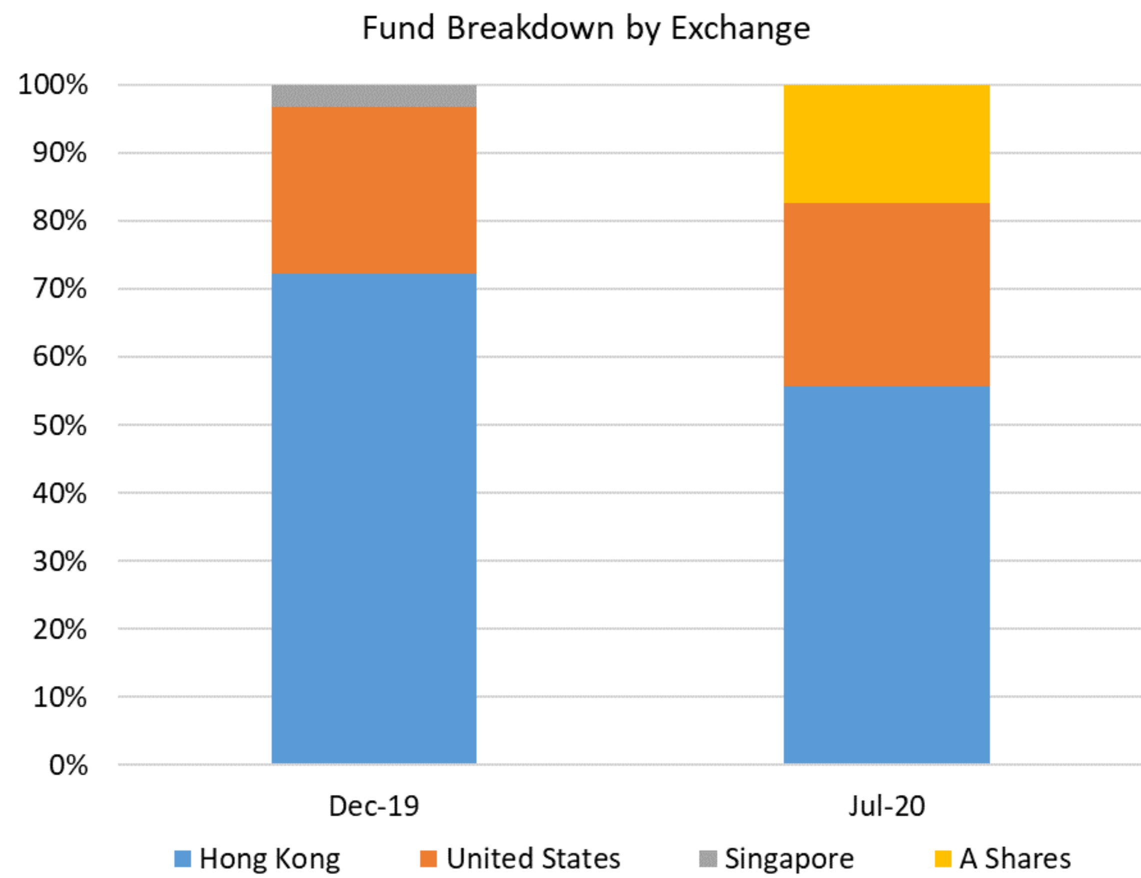
Source: Guinness Atkinson Asset Management. Data as of July 31, 2020

Relative to the MSCI China Index, the Fund is most overweight in Industrials, Materials and Health Care. The Fund is most underweight in Communication Services, Financials and Energy.



Source: Bloomberg, Guinness Atkinson Asset Management. Data as of July 31, 2020

The Fund has increased its allocation to the domestic A share market by 17.2% this year, while the allocation to Hong Kong has fallen by 16.8%.



Source: Guinness Atkinson Asset Management. Data as of July 31, 2020

Outlook

The focus this year has been selling companies where either the competitive advantage has been lost or the prospect of earnings growth is unlikely. The replacements, we feel, all have a definable competitive advantage, have managed to grow their earnings in the past (pre-COVID) and are likely to do so in the current environment. The Fund has significantly increased its allocation to the A share market which we expect to give it exposure to any rallies in the mainland. We believe the Fund is now better placed to capture the growth opportunities present in China. The upcoming results season should reveal how our companies have coped now that life in China has some semblance of normality.

At a macro-level we think there are reasons, beyond the cyclical, to believe that China's domestic recovery will continue for the next twelve months. Next year is the centenary of the founding of the Chinese Communist

Party. This is a big date in the government calendar and much of China's foreign and domestic policy is likely to be geared to showcasing a new economically and politically assertive China. As we have seen, this has resulted in rising frictions with the rest of the world which is likely to lead to further efforts to bolster domestic self-sufficiency and growth of national champions. Efforts are likely to continue to prevent excesses building or bubbles forming, but the direction of travel is likely to continue to be supportive of growth. Infrastructure stimulus is likely to another level of growth and here we have several interesting ideas on our watchlist in the A share market.

Edmund Harriss (portfolio manager)

Performance

As of 7/31/2020	YTD	1 Year	3 Year	5 Year	10 Year
China & Hong Kong Fund (ICHKX)	**-1.70%**	**14.58%**	**5.49%**	**7.76%**	**3.69%**
Hang Seng Composite Index TR	**0.00%**	**4.67%**	**3.46%**	**5.66%**	**5.80%**

As of 6/30/2020	YTD	1 Year	3 Year	5 Year	10 Year
China & Hong Kong Fund (ICHKX)	**-9.41%**	**2.87%**	**4.17%**	**3.79%**	**3.88%**
Hang Seng Composite Index TR	**-5.03%**	**-2.54%**	**3.82%**	**2.92%**	**5.81%**

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

Expense Ratio: 1.69%

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.

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

The MSCI Zhong Hua Index is a composite index that comprises the MSCI China and MSCI Hong Kong Index. The index captures large and mid-cap representation across all China securities (B shares, H shares, Red Chips, PChips and foreign listed shares) as well as Hong Kong securities.

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.

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.

Shanghai Composite Index, also known as SSE Index, is a stock market index of all stocks that are traded at the Shanghai Stock Exchange.

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 7/31/2020:

1. Haier Electronics Group Co Ltd	4.00%
2. China Lesso Group Holdings Ltd	3.98%
3. Beijing Oriental Yuhong	3.90%
4. Alibaba Group Holding Ltd	3.80%
5. Geely Automobile Holdings Ltd	3.74%
6. JD.com Inc	3.69%
7. Noah Holdings Ltd	3.68%
8. Sino Biopharmaceutical Ltd	3.67%
9. Zhejiang Supor Cookware	3.66%
10. Weichai Power Co Ltd - H Shares	3.65%

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