Guinness Global Equity Income Fund

A high conviction equity fund managed by Dr. Ian Mortimer, CFA, and Matthew Page, CFA, in accordance with their intelligent investment process for high quality income portfolios.

INVESTMENT COMMENTARY - July 2013

Fund size (30.6.13) **£19.2m**

Aim

We don't chase yield, we want capital and dividend growth

Our aim is long-term capital growth and a steady rising dividend stream, balanced with a yield of 3-4%.

Process

Quality before yield

We buy companies that have generated at least 10% Cash Flow Return on Investment every year for 10 years.

"It's a rare achievement for a company to meet our investment criteria – 10% cash flow return on investment every year for ten years is a mark of genuine quality. That's where our portfolio starts – persistent cash generation before yield."

Performance

After five consecutive months of positive performance in 2013, in June the MSCI World Index declined 2.5%. The Fund was down 1.3%, therefore outperforming the benchmark by 1.2%.

The Fund performed robustly over the first half of 2013 in what proved to be another fairly choppy period of swinging expectations. It was up 20.64% in the first 6 months of the year, outperforming the benchmark MSCI World index (up 16.21%) by 4.43%. This ranks the Fund first relative to the peer group of 30 funds in the IMA Global Equity Income sector over this period. Since the launch of the Fund at the end of 2010 the Fund ranks third amongst the same peer group.

The year started strongly for global equities as many of the concerns around the US "fiscal cliff" were put to bed and attention turned to improving economic data in the US, Japanese "QE" and further concerns of slower growth in China. In the US the number of new housing starts is heading back towards historic trend levels, house prices have started to appreciate again, consumer confidence is improving, while unemployment continues to fall. We saw a period of relative calm in Europe compared to what we have been used to over the previous two years, with yields on Spanish and Italian 10 year government bonds averaging well below 5%. There was further central bank quantitative easing in Japan, providing more support to income-producing assets and a strong rally in the Nikkei Index. The market peaked on May 22nd after Ben Bernanke told Congress that the Fed could start to scale back quantitative easing should the economy shows signs of continued and sustainable improvement. Markets continued to decline in June over the anticipation of the withdrawal of US support to asset prices with Emerging Market equities and high yielding equities being hit hardest.

Performance of our holdings

In terms of performance attribution, our allocation to Industrials was the largest contributor to performance relative to the benchmark. Stock selection dominated this outperformance with Meggitt and Northrop Grumman performing particularly well. This was narrowly followed by our overweight position in the Consumer Staples sector. We

did not own any companies in the Materials or Utilities sectors.

Our focus on companies that can generate high return on capital, that offer value, and can grow their dividend, as opposed to companies that offer a high dividend yield, meant that we weathered much of the volatility of the period well, outperforming the benchmark in the rally to the 22nd of May and holding onto this by also outperforming during the correction from 22nd May to the end of June.

The three best performing stocks in the first six months were H&R Block (+62.1% Total Return in GBP), Microsoft (+40.4%) and Meggitt (+37.9%).

The three worst performing stocks were ENI (-7.3%), China Mobile (-1.9%) and Imperial Tobacco (-0.6%).

Buys and Sells

We sold two of our winners in March as we thought the valuations on Wal-Mart and VF Corp were starting to look quite full, while at the same time the dividend growth of these companies was being outpaced by share price appreciation. Consequently the dividend yield of these two companies was by now considerably below where it was when we initiated our original positions and we could find better valuation and yield elsewhere. We bought Northrop Grumman and BAE systems in their place – they looked unloved and cheap. Concerns about the US fiscal cliff had pushed Northrop Grumman to historic low valuations as well as being cheap relative to the company's peers and in absolute terms. Both companies offered improved yield at the portfolio level.

Portfolio Breakdown

We continue to have our largest sector weighting to the Consumer Staples sector at 24.9%, followed by Financials and Industrials at 16.7% and 16.6% respectively. We continue not to own any Utility or Materials stocks as our initial screen of looking for companies with a history of consistently generating high return on capital over a business cycle excludes the vast majority of companies in these sectors. Regulated industries like Utilities are normally not allowed to earn such high returns on capital for a prolonged period of time because of their state-mandated monopolistic or oligopolistic competitive advantage. Companies in the Materials sector tend not to make it through our screen due to the fact that they lack any significant pricing power over underlying commodity prices, making returns on capital fairly volatile. Both of these sectors make up a relatively small proportion of the MSCI World index and we feel very comfortable owning more high return on capital companies at the expense of these sectors, despite the fact that these sectors have traditionally been a strong source of high yielding stocks.

Portfolio sector weights, 30.6.13	
Consumer staples	24.9%
Financials	16.7%
Industrials	16.6%
Health care	13.5%
Energy	8.4%
Telecommunication Services	5.8%
Consumer discretionary	5.5%
Information Technology	5.5%
Materials	0.0%
Utilities	0.0%

Past performance should not be taken as an indicator of future performance. The value of investments and any income arising from them can fall as well as rise.

As we try to keep our turnover low, that sometimes means we will keep positions in the portfolio that might be starting to look quite fully valued. It is always a balancing act between selling a company because you believe the valuation is starting to look rich whilst at the same time trying to make as few changes to the portfolio as possible. Some investors we speak to are concerned that a number of Consumer Staples companies are looking fully valued. We would agree.

Whilst Consumer Staples remains our largest sector weighting we have been reducing our exposure to the sector during the last 12 months as we have felt that valuations of some companies are starting to look fairly full and we could find better value elsewhere. For example we sold Wal-Mart in March, Pepsico in October last year. A few of the large cap global Consumer Staple companies that we own have seen some small declines in analysts' earnings expectations for 2013. However, year-on-year earnings growth of high single digit percentage rates continue to look healthy and achievable. We continue to think that many of these positions remain an attractive part of the portfolio.

Many of the companies in the sector often have a significant exposure to emerging markets (e.g. Coca Cola and Unilever) and in our opinion have offered an attractive way to get exposure to emerging markets considering the value these companies have offered and their ability to capitalise on the falling cost of debt. Emerging market companies that generate high return on capital have looked relatively expensive to us over the last three years. As western-listed Consumer Staple companies have performed so well the value on a relative basis to locally listed companies is potentially reducing, but we do not currently see many compelling opportunities in emerging markets.

Another advantage that western-listed business with emerging market exposure have over locally-listed emerging markets stocks is low volatility in the share price, given the relatively predictable earnings stream. In the current environment of untested central bank policies we find it a particularly attractive attribute.

Ultimately we must maintain a disciplined search for value above all else, which will likely mean further reducing our exposure to Consumer Staples over the second half of the year. If emerging markets continue to suffer from concerns over the threat of the Fed tapering quantitative easing then potentially more compelling opportunities will arise.

With equity markets having performed well over the last 18 months, we are more cautious than ever on companies that are trading on high dividend yields of say 5-6%+. High dividend yield can be a fantastic buy signal when markets are trading on low valuation multiples such as in 2009, but can be painful when markets are trading on moderate to high multiples. With the strong demand for income that currently exists we think valuations on high yield stocks have been driven to valuation multiples that are not taking into account the potential weakness of their business model in an environment where cheap easy credit is taken away.

Simply focusing on companies that have grown their dividend each year is also insufficient in our minds. Kmart's dividend increased every year from 1978 to 1994 until it was cut in 1995, and by 2002, in the wake of the tech bubble, the company had filed for bankruptcy. Wal-Mart on the other hand has increased its dividend every year from 1978 and continues to do so. The key difference that stands out between the two companies was their return on capital. In 1995 Kmart had a 5 year average return on equity of 7%, which is likely to have been below their cost of capital (which we estimate at 9%. Wal-Mart on the other hand had a five year return on equity of 25%, which would have been well in excess of the company's cost of capital.

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Indeed Wal-Mart's return on capital continues to be maintained at a similar level today, averaging 23% over the last five years.

So while someone who had invested in Kmart in 1980 would have lost everything by 2002 when Kmart filed for bankruptcy, an investor in Wal-Mart over the same period would have generated a total return of 29,098%.

While this is a fairly startling example it makes complete sense that a company that doesn't generate a return on capital higher than its cost of capital cannot pay a sustainable dividend for a prolonged period of time. It may be able to pay a dividend for a number of years, by selling assets, taking on debt, extending the time within which it will pay suppliers, depleting its cash reserves etc., but there is only so long this can last before the company's issues will come to light.

In our minds a high return on capital for a prolonged period of time must be our starting point when looking for companies that can afford to pay a sustainable dividend. Companies that have generated consistently high returns on capital over a business cycle are very likely to remain good companies into the future. As long as we can ensure we apply a consistent value discipline to selecting those companies to hold in the portfolio, we believe we have got a good chance of continuing to outperform the market while providing investors with the income they need.

Dr. Ian Mortimer & Matthew Page

Co-managers,
Guinness Global Equity Income Fund

July 2013

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PORTFOLIO (30.6.13)

Fund top 10 holdings

Holding	%
China Mobile	3.0%
Kraft Foods	2.8%
Danone	2.8%
Total	2.8%
Illinois Tool Works	2.8%
ICAP	2.8%
Mattel	2.8%
L-3 Communications	2.8%
Unilever	2.8%
Deutsche Boerse	2.8%

% of Fund in top 10	28.3%
Total number of stocks in Fund	35
AUM	$30m

Sector analysis

Sector	%
Cons Staples	24.9%
Financials	16.7%
Industrials	16.6%
Health Care	13.5%
Energy	8.4%
Telecoms	5.8%
Cons Disc	5.5%
IT	5.5%
Cash	3.2%

Geographic allocation

Country	%
United States	49.6%
Great Britain	30.2%
France	5.7%
Hong Kong	3.0%
Germany	2.8%
Italy	2.8%
Netherlands	2.8%
Cash	3.2%

PERFORMANCE

12 months to month end:	Jun '09	Jun '10	Jun '11	Jun '12	Jun '13
Guinness Global Equity Income Fund	-	-	- -	1.3	23.0
MSCI World Index	-14.8	21.3	21.6	-2.7	22.6
IMA Global Equity Income sector average	-12.3	19.7	20.9	-1.9	21.1

Cumulative % total return

30/06/2013	1 month	3 months	6 months	1 year	From launch
Guinness Global Equity Income Fund	-1.3	3.7	20.6	23.0	28.8
MSCI World Index	-2.5	0.8	16.2	22.6	22.5
IMA Global Equity Income sector average	-3.1	0.2	13.7	21.1	22.2

Annualised % total return from launch 30/06/2013

	30/06/2013
Guinness Global Equity Income Fund	**10.67%**
MSCI World Index	**8.45%**
IMA Global Equity Income sector average	**8.34%**

Risk analysis - Annualised, weekly, from launch on 31.12.10

30/06/2013	Index	Sector	Fund
Alpha	0	1.93	3.83
Beta	1	0.76	0.77
Information ratio	0	0.01	0.39
Maximum drawdown	-18.26	-15.50	-16.40
R squared	1	0.81	0.90
Tracking error	0	6.72	5.27
Volatility	15.21	12.88	12.35

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Source: Financial Express, bid to bid, total return, C class shares, GBP. Launch date: 31.12.10.

IMPORTANT INFORMATION

This report is primarily designed to inform you about the Guinness Global Equity Income Fund, including recent activity and performance. For regulatory purposes it falls within the legal definition of a financial promotion. Please therefore note the risk warnings below and the following statements: it contains facts relating to equity markets and our own interpretation. Any investment decision should take account of the subjectivity of the comments contained in the report. It is 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 content of the document should not therefore be relied upon. It should not be taken as a recommendation to buy or sell individual securities.

The Guinness Global Equity Income Fund is an equity fund. Investors should be willing and able to assume the risks of equity investing. The value of the Fund's portfolio changes daily and can be affected by changes in currencies, interest rates, general market conditions and other political, social and economic developments, as well as specific matters relating to the companies in whose securities the Fund invests. Investment in the Fund carries with it a degree of risk and investors should read the risk factors section in the prospectus before investing. 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.

The full Fund documentation contains more complete and detailed information of risk, fees, charges and expenses that are to be borne by an investor. The documentation should be read carefully before investing. The full documentation needed to make an investment, including the Prospectus, the KIID and the Application Form are available, free of charge, from the Manager: Capita Financial Managers (Ireland) Limited, 2 Grand Canal Square, Grand Canal Harbour, Dublin 2, Ireland or the Promoter and Investment Manager: Guinness Asset Management Ltd, 14 Queen Anne's Gate, London SW1H 9AA. **Documentation is also available from the website guinnessfunds.com.** This document should not be distributed to Retail Clients who are resident in countries where the Fund is not registered for sale or in any other circumstances where its distribution is not authorised or is unlawful. THIS INVESTMENT IS NOT FOR SALE TO U.S. PERSONS.

The Guinness Global Equity Income 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. The Fund has been approved by the Financial Conduct Authority for sale in the UK. The Company and the Fund have been recognised in the UK by the FSA pursuant to section 264 of the FSMA. Guinness Asset Management Ltd is authorised and regulated by the Financial Conduct Authority.

Telephone calls to Guinness Asset Management may be recorded.

The prospectus for Switzerland, the simplified prospectus for Switzerland, the articles of association, the annual and semi-annual reports, as well as the list of the buying and selling transactions 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, Fax: + 41 22 705 11 79, www.carnegie-fund-services.ch. The paying agent is Banque Cantonale de Genève, 17 Quai de l'Ile, 1204 Geneva, Switzerland.

GLOSSARY

Alpha
Alpha is a measure of a fund's over or underperformance by comparison to its benchmark. It represents the return of the fund when the benchmark is assumed to have a return of zero, and thus indicates the extra value that the manager's activities have contributed.

Beta
Beta is a statistical estimate of a fund's volatility by comparison to that of its benchmark, i.e. how sensitive the fund is to movements in the section of the market that comprises the benchmark. A fund with a Beta close to 1 will move generally in line with the benchmark. Higher than 1 and the fund is more volatile than the benchmark.

Information Ratio
An assessment of the degree to which a manager uses skill and knowledge to enhance returns, this is a versatile and useful risk-adjusted measure of actively-managed fund performance. It is calculated by deducting the returns of the fund's benchmark from the fund's overall returns, then dividing the result by its Tracking Error. In this way, we arrive at the value, per unit of extra risk assumed, that the manager's decisions have added to what the market would have delivered anyway.

Maximum Drawdown
Represents the worst possible return over a period, e.g. buying at the highest price over the period and selling at the lowest.

R-Squared
The R-Squared measure is an indication of how closely correlated a fund is to an index or a benchmark. It can be treated as a percentage, showing what proportion of a fund's movements can be attributed to those of the benchmark. Values for R-Squared range between 0 and 1, with 0 indicating no correlation at all, and 1, rarely, showing a perfect match.

Tracking Error
This statistic measures the standard deviation of a fund's excess returns over the returns of an index or benchmark portfolio. As such, it can be an indication of "riskiness" in the manager's investment style. A Tracking Error below 2 suggests a passive approach, with a close fit between the fund and its benchmark. At 3 and above the correlation is progressively looser: the manager will be deploying a more active investment style, and taking bigger positions away from the benchmark's composition.

Volatility
Standard deviation is a statistical measurement which, when applied to an investment fund, expresses its volatility, or risk. It shows how widely a range of returns varied from the fund's average return over a particular period. Low volatility reduces the risk of buying into an investment in the upper range of its deviation cycle, then seeing its value head towards the lower extreme.