Guinness Global Innovators Fund

INVESTMENT COMMENTARY - April 2017

About the Fund

The Fund is a global growth fund designed to provide exposure to companies benefiting from innovations in technology, communication, globalisation or innovative management strategies. The Fund holds a concentrated portfolio of large and medium-sized companies in any industry and in any region.

Fund size	£73m
AUM in strategy	£214m
Fund launch date	31.10.14
Strategy launch date	01.05.03
Managers	Dr Ian Mortimer, CFA Matthew Page, CFA

Performance **31.03.17**

Cumulative % gross total return (GBP)	1 year	3 years	5 years	10 years
Strategy*	35.7	64.1	138.6	259.4
Index	32.7	59.3	105.7	150.8
Sector	28.6	43.2	75.8	97.5
Position in sector	27 /266	16 /235	6 /202	2 /133

Annualised % gross total return
from strategy inception (GBP)

Strategy*	13.10%
Index	10.79%
Sector	9.31%

Strategy	Guinness Global Innovators*
Index	MSCI World Index
Sector	IA Global

Past performance should not be taken as an indicator of future performance. The value of this investment and any income arising from it can fall as well as rise as a result of market and currency fluctuations.
***Composite simulation of performance. Guinness Global Innovators Fund (UCITS) launched on 31.10.14. Performance data prior to this date is based on the actual returns of a US mutual fund managed by the same team using the same investment process as applied to the UCITS version.** Source: Financial Express, bid to bid, gross total return, in GBP.

Summary performance

In the month of March the Fund was up 2.61% (in GBP) versus the benchmark MSCI World Index which was up 0.65%. The Fund therefore outperformed the index by 1.96% over the month.

Over the first quarter the Fund was up 7.58% (in GBP) versus the benchmark MSCI World Index which rose 5.27%. The Fund therefore outperformed the index over the quarter by 2.31%.

As well as outperforming the benchmark in the quarter, the Fund ranked in the top quartile versus peers in the IA Global sector. The long-term performance of the strategy remains very strong versus both the index and the IA Global sector; its three, five, and ten-year performance versus the sector place it in the top decile over all periods.

Figure 1: Global Innovators strategy performance:

GTR in GBP to 31.03.17	3 years	5 years	10 years
Fund	64.1	138.6	259.4
Index	59.3	105.7	150.8
Sector	43.2	75.8	97.5
Rank	16 / 235	6 / 202	2 / 133

Quarter in review

World equity markets had a strong quarter with a pause for breath in late March, finishing the quarter up 6.53% (in USD). This was a positive start to 2017.

In January, all eyes were on the US with the inauguration of President Trump on January 20th and the potential for swift action on his campaign promises concerning trade, tax reform, infrastructure spending, immigration and healthcare. Overall, the markets continued their rally on the back of the 'inflation trade' with growth stocks outperforming value stocks.

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The Federal Reserve struck a more hawkish tone in January. Janet Yellen had to deal with falling unemployment, rising wages alongside a proposal for a significant fiscal stimulus, and how to effectively manage the prospect of sharply rising inflation. In Europe, the focus was on political uncertainty and the potential rise of populism across the upcoming Dutch, French and German elections.

In February, markets rose to record peaks across various indices, as positive core economic, consumer demand and strengthening manufacturing data all aided the market rally with the hope of faster economic growth. The global markets ended on a more cautious note ahead of Donald Trump's speech to a joint session of the US Congress. In Europe, markets followed the same trend as the US and advanced, albeit at a slightly slower pace. Corporate earnings were generally more positive than expected and growth estimates were revised upwards in Europe for 2017. Focus on European political uncertainty increased as Francois Fillon continued to soldier on with his French presidential election campaign despite the 'fake job' scandal and his continuing decline in the polls. In a matter of weeks, he went from being the clear favourite to battling it out with Emmanuel Macron and Marine Le Pen to get through the first round of elections.

March followed in a similar manner to January and February, with a slight pause in the markets towards the end of the month. At the beginning of March, President Trump gave a speech to the US Congress which was widely anticipated to outline key fiscal initiatives for 2017. In the event he gave few details, but his more measured tone caused markets to react positively. The second half of March saw Trump's key healthcare bill fail to be passed in Congress, due to dissatisfaction among both Republican moderates and Republican conservatives. This cast doubt over other policies Trump has spoken about, especially tax reform and where the funding for such a policy will now come from. We saw the Federal Reserve raise short-term interest rates for the third time since the 2008 financial crisis. There was slight relief from moderate and pro-EU politicians across Europe as the Dutch populist politician Geert Wilders failed to make his anticipated gains, helping at least temporarily to calm fears of political uncertainty across the continent.

March completed a strong quarter for global markets with Europe rallying towards the end. Developed market equities all performed well (S&P500 +6.06%, FTSE100 +5.33%, Euro STOXX +8.48%, in USD) but still lagged emerging market equities (MSCI EM +11.45% in USD) and Asian equities (MSCI Asia-Pac ex Japan +13.36% in USD) which recovered after weaker performance in late 2016, following the US election. The sectors which did well (Information Technology, Utilities and Consumer Staples and Consumer Discretionary) and lagged (Energy) the markets in February broadly continued to do so in March, with the exceptions of Health Care and Financials.

The performance of Health Care and Financials, both having weaker performance in March than in February, coincided with doubts over whether Trump will be able to implement his policies as quickly and as thoroughly as previously expected. The market appears to be taking a wait-and-hold approach before making any large calls on the "inflation trade" that has dominated sentiment since shortly after election day. There is also a growing assumption that the Fed is appearing more dovish in the medium term than was priced in after the US election.

Of note is the continuing strong performance of the Information Technology sector, spurred on by the anticipation of high demand for smartphones, amongst other technology themes that are coming of age. The sector has been seen as less vulnerable to the various political uncertainties and potential changes in government policy both in the US and elsewhere. The sector has also posted good earnings growth and appears set to continue this trend in the future, making it something of an outlier in today's market.

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Performance drivers

In terms of sector positioning, the Fund's overweight relative to the benchmark in Information Technology (33% overweight on average over the period) and underweight positioning in Energy (4% underweight) and Financials (12% underweight) were the largest positives, in absolute terms contributing +2.7% to total returns. The largest sector underperformance was in Consumer Staples (representing a 10% underweight versus the benchmark on average) and Health Care (3% underweight).

In terms of geographic exposure, the largest difference between the Fund and the benchmark is in exposure to the US (as measured by country of domicile). The Fund over the quarter had on average a 68% weighting to the US which compares to the index at c.60%. This 8% overweight position made no discernible difference to performance.

Mid to large-caps outperformed small-caps, which would generally be beneficial to the Fund as it only invests in mid to large-cap companies. There was a bias towards growth stocks versus value stocks which also helped performance, but not in a significant way.

Individual companies that performed well over Q1 were New Oriental Education (up 43.42% in USD), AAC Technologies (up 28.81%), Samsung (up 22.82%), Check Point Software (up 21.55%), Applied Materials (up 20.88%) and Fanuc (up 20.49%).

Companies that had weaker performance over Q1 were WisdomTree (down 17.74% in USD), Qualcomm (down 11.23%), Schlumberger (down 6.40%) and Gilead Sciences (down 4.43%).

Changes to portfolio

During the quarter we made one change to the portfolio. We sold our position in H&R Block and bought a new position in Catcher Technology.

H&R Block, the US-based tax preparation company, was first purchased for the Fund in October 2012 and has been a long-term holding. Over our holding period the company went through quite significant changes, particularly the spinning off of its banking arm in 2014 which released the company from the associated regulatory burden and capital requirements. This was well received by the market and the company added significantly to the performance of the Fund from our first purchase in 2012 to the end of 2015. However, during 2016 the company posted a series of weak quarterly results. It seemed that competition in the marketplace and especially the 'do-it-yourself' online tax return model had begun to erode their dominant position. This was reflected by sharp declines in the share price over this period. The latest quarterly results released in early March surprised to the upside, however, not so much because of obviously positive results as because the market had been too pessimistic. The subsequent spike upwards in the share price provided an opportunity to exit our position. The valuation of the company is undemanding (around 13.5x 2017 expected earnings) but we found it hard to see where the growth we are looking for could come from and it appears that for now, at least, the company has lost its competitive edge. The next quarterly results (for the year ending April and released in June) will be the acid test as the company's earnings are seasonally skewed due to the tax year. We felt our conviction was not high enough to justify holding the stock through this period.

Catcher is a Taiwanese listed technology company that specialises in the manufacture of metallic casings for electronic devices. Historically, sales were dominated by notebooks, but this has shifted to smartphones as more high-end phone suppliers moved to metallic casings following Apple's iPhone 5. This does mean the company has a handful of clients dominating its revenue stream (Apple and Samsung, for example) but also provides opportunity as these companies search for the most innovative casings for their newest phones. The

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latest cases will be a combination of both metal and glass (or laminate) and will be more technically difficult to produce. This is reflected in the high operating margins which the company has achieved (around 30%) and which we believe it can defend in the future. In terms of quality, the company has maintained a high return on capital for a lengthy period and has been growing this return year-on-year, which suggests that its management has been allocating capital successfully. The company is exposed to the business cycle and is cyclical by nature, but the recent uptick in earnings estimates and cheap valuation (just over 10X 2017 expected earnings) gives reasonable margins of safety, in our opinion.

Positioning

The below chart highlights the geographic weighting of the portfolio both by domicile and by origin of revenues, which can often be more illuminating.

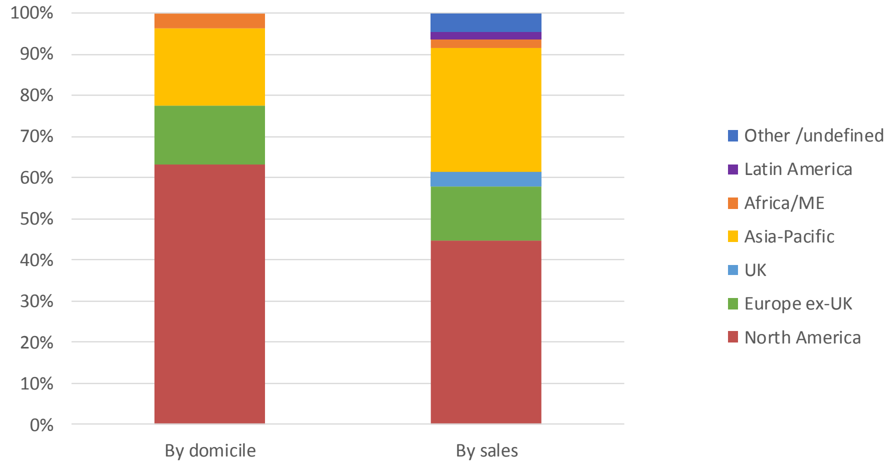

Chart 1: Geographic breakdown of the Global Innovators Fund. Guinness Asset Management, Bloomberg (data as at 31.03.2017)

We would note two points: first, the Fund's lower exposure to the US when considered in revenues (44%) versus by domicile (63%), which occurs because some companies are domiciled in the US but have large global exposure (such as Schlumberger and Qualcomm); and secondly, the larger exposure to Asia by revenues (29%) than by domicile (19%).

In terms of sector weightings, the Fund has zero weighting to Utilities, Materials, Telecoms, Consumer Staples and the newly created Real Estate sector (which previously was included in Financials but is now split out as a sector by MSCI). The largest overweight positions are to Information Technology and to Industrials.

The chart below shows the sector breakdown of the Fund in absolute terms and relative to the benchmark to highlight any over/underweights.

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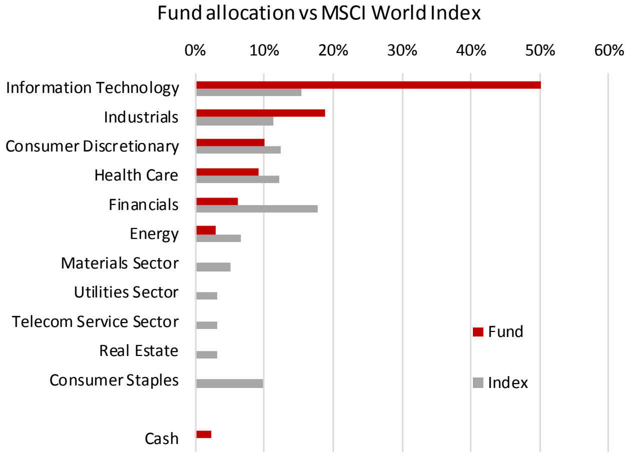

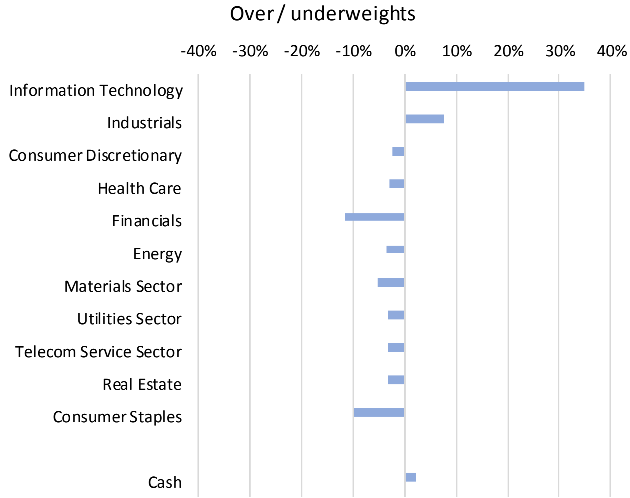

Chart 2: Sector breakdown of the Fund versus MSCI World Index. Guinness Asset Management, Bloomberg (data as at 31.03.2017)

It is worth noting that the large overweight position to Information Technology is split between the three different subsectors of semiconductors (17% of the portfolio), software and services (16%), and technology hardware (17%).

To put this data into a historical context (for the Fund at least) the two charts below show how sector exposure has evolved since we launched the strategy back in 2003.

The last quarter's portfolio change has increased the exposure of the Fund to IT stocks by 3.3% and decreased exposure to Consumer Discretionary by an equivalent amount.

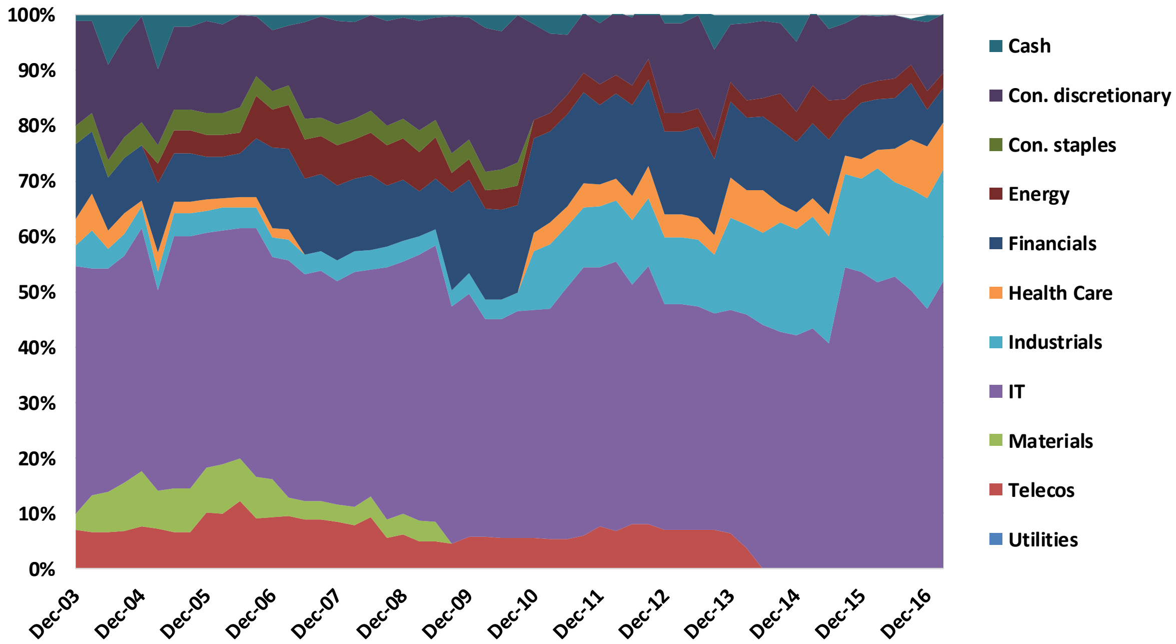

Chart 3: Sector breakdown of the Fund since launch. Guinness Asset Management, Bloomberg (data as at 31.03.2017)

From a geographic point of view, US exposure decreased with the sale of H&R Block in March. The purchase of Catcher Technologies in its place increased Asia exposure.

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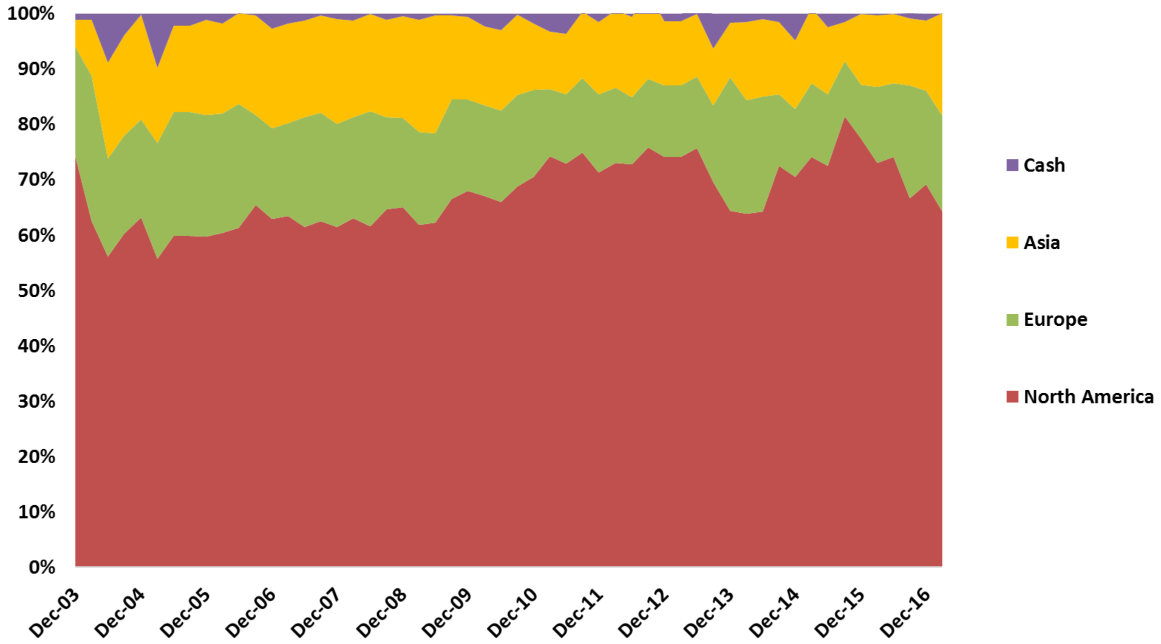

Chart 4: Geographic breakdown of the Fund since launch. Guinness Asset Management, Bloomberg (data as at 31.03.2017)

Key fund metrics today

The four key tenets to our approach are innovation, quality, growth, and conviction.

		Fund	MSCI World Index
Innovation	R&D / Sales	8%	6%
	CAPEX / Sales	6%	10%
Quality	CFROI (2016)	18%	11%
	Weighted average net debt / equity	-9%	121%
Growth (& valuation)	Last 3 year sales growth (annualised)	11%	4%
	Estimated earnings growth (2018 vs 2017)	11%	11%
	PE (2017e)	17.5	17.0
Conviction	Number of stocks	30	1650
	Active share	95%	-

Chart 5: Portfolio metrics versus index. Guinness Asset Management, Credit Suisse HOLT, Bloomberg (data as at 31.03.2017)

Innovation can be difficult to define, and doing so is quite subjective. One way in which we attempt to quantify this metric at the portfolio level is by considering the metric of research and development spend as a proportion of sales. This shows the level, relative to total sales, at which a business is investing in its research and development and thus ultimately its intellectual property. We also look at capital expenditure as a percentage of sales to gauge how capital intensive a company is. We look for companies that have lower capital requirements and are thus potentially better placed to grow and grow profitably. As the table above shows, the Fund owns companies that invest a higher proportion of their sales into R&D than the market average and that have significantly lower ongoing capital requirements.

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We use the term ‘quality’ to denote two financial characteristics that we want to see in a company – regardless of how innovative it is or how fast it is growing. These are a high return on capital (and specifically above the cost of capital) and a good balance sheet. It is pleasing to see that the portfolio significantly outpaces the index on both these fronts. The cash flow return on investment is over 60% higher (18% versus 11%) and in aggregate the portfolio is trading with a net cash position of 9% versus a net debt of 121% for the benchmark.

We aim to provide a ‘good’ or ‘reasonable’ level of earnings growth from the portfolio. We avoid chasing companies with very high growth expectations as they are likely to disappoint and can often be accompanied by high valuations. Today the expected year-on-year earnings growth of the portfolio is around 11%, which is in line with the market. However, because of the superior companies we are investing in we believe we stand a better chance of achieving this expected growth. We also note the historic revenue growth achieved by companies held in the portfolio today is almost three times higher than that achieved by the benchmark.

We have always attempted to employ a valuation discipline to stock selection; we do not want to pay up for future growth because of its illusive nature. We therefore include a simple forward PE metric in the above table to highlight that the Fund is trading only at a small premium to the broad market today.
We continue to hold 30 stocks, all equally weighted. This means the Fund is genuinely index agnostic, as its 95% active share illustrates.

Outlook

Generally speaking, the Fund has outperformed in periods of rising markets, and underperformed slightly in periods of falling markets. The Fund is orientated towards growth, but not at any price. Therefore, the recent outperformance is what we might have expected as the more cyclical parts of the market, and particularly Information Technology, have performed well.

As we noted above and as a result of the outperformance in the first quarter, the Fund is now trading at a small 2.8% premium to the broad market on a PE ratio basis (17.5x 2017 expected earnings vs MSCI World Index 17.0x), after trading at a discount for much of 2016. The longer-term premium versus the broader market has been in the 10-20% range – so we think that with a portfolio of innovative and high-quality companies, the Fund offers good value today.

We thank you for your continued support.

Portfolio Managers
Dr Ian Mortimer, CFA
Matthew Page, CFA

Analysts
Joshua Cole
Sagar Thanki

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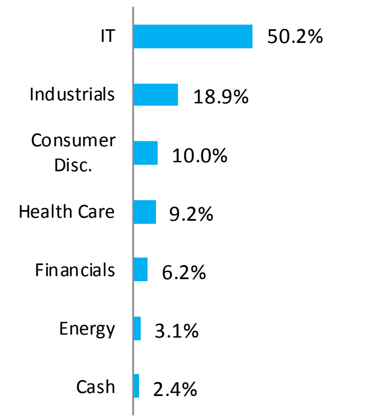
PORTFOLIO

31/03/2017

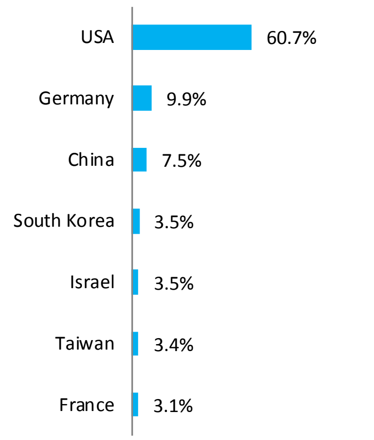
Fund top 10 holdings

AAC Technologies	3.8%
Applied Materials	3.7%
New Oriental Education & Tech	3.7%
Samsung Electronics GDR	3.5%
Check Point Software	3.5%
Boeing	3.4%
Nvidia Corp	3.4%
Catcher Technology	3.4%
Infineon Technologies	3.4%
SAP AG	3.3%
% of Fund in top 10	35.1%
Total number of stocks in Fund	30

Sector analysis



Geographic allocation



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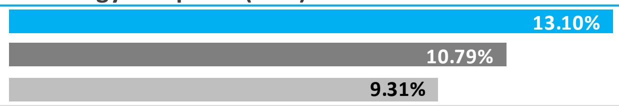
Annualised % gross total return from strategy inception (GBP)



Discrete years % gross total return (GBP)	Mar '13	Mar '14	Mar '15	Mar '16	Mar '17
Guinness Global Innovators strategy*	19.8	21.5	23.4	-2.0	35.7
MSCI World Index	18.4	9.0	19.7	0.3	32.7
IA Global sector average	14.6	7.1	15.3	-3.4	28.6

Cumulative % gross total return (GBP)	1 month	Year-to-date	1 year	3 years	5 years	10 years
Guinness Global Innovators strategy*	2.6	7.6	35.7	64.1	138.6	259.4
MSCI World Index	0.7	5.3	32.7	59.3	105.7	150.8
IA Global sector average	1.1	5.5	28.6	43.2	75.8	97.5

RISK ANALYSIS

31/03/2017

Annualised, weekly, 5 years, in GBP	Index	Sector	Strategy*
Alpha	0	0.15	2.49
Beta	1	0.80	1.11
Information ratio	0	-0.44	0.66
Maximum drawdown	-14.03	-17.08	-17.14
R squared	1	0.78	0.86
Sharpe ratio	0.93	0.76	1.07
Tracking error	0	5.82	5.69
Volatility	12.48	11.33	14.89

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Source: Financial Express, bid to bid, gross total return, in GBP

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Important information

Issued by Guinness Asset Management Limited, authorised and regulated by the Financial Conduct Authority.

This report is primarily designed to inform you about Guinness Global Innovators Fund. It may provide information about the Fund's portfolio, including recent activity and performance. It contains facts relating to the equity markets and our own interpretation. Any investment decision should take account of the subjectivity of the comments contained in the report.

This document is provided 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 contents of the document should not therefore be relied upon. It should not be taken as a recommendation to make an investment in the Fund or to buy or sell individual securities, nor does it constitute an offer for sale.

Risk

The Guinness Global Innovators Fund is an equity fund. Investors should be willing and able to assume the risks of equity investing. The value of an investment and the income from it can fall as well as rise as a result of market and currency movement, and you may not get back the amount originally invested. Details on the risk factors are included in the Fund's documentation, available on our website.

Documentation

The documentation needed to make an investment, including the Prospectus, the Key Investor Information Document (KIID) and the Application Form, is available from the website www.guinnessfunds.com , or 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.

Residency

In countries where the Fund is not registered for sale or in any other circumstances where its distribution is not authorised or is unlawful, the Fund should not be distributed to resident Retail Clients.

NOTE: THIS INVESTMENT IS NOT FOR SALE TO U.S. PERSONS.

Structure & regulation

The 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, which operates under EU legislation. If you are in any doubt about the suitability of investing in this Fund, please consult your investment or other professional adviser.

Switzerland

The prospectus and KIID for Switzerland, the articles of association, and the annual and semi-annual reports 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, www.carnegie-fund-services.ch. The paying agent is Banque Cantonale de Genève, 17 Quai de l'Ile, 1204 Geneva, Switzerland.

Telephone calls may be recorded and monitored.