



VL Asset Management Limited
以立投資管理有限公司

VL China Fund

(A Sub-Fund of VL Trusts)

Interim Report

For the period ended 31 December 2018

(Unaudited)

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MANAGEMENT AND ADMINISTRATION

Manager	VL Asset Management Limited 以立投資管理有限公司 Unit 1807, FWD Financial Centre 308 Des Voeux Road Central Hong Kong
Trustee	Standard Chartered Trust (Hong Kong) Limited 13/F Standard Chartered Bank Building 4-4A Des Voeux Road Central Hong Kong
Administrator, Custodian and Registrar	Standard Chartered Bank (Hong Kong) Limited 32/F Standard Chartered Bank Building 4-4A Des Voeux Road Central Hong Kong
Legal Counsel to the Manager	Simmons & Simmons 13/F One Pacific Place 88 Queensway Hong Kong
Auditors	Ernst & Young 22/F, CITIC Tower 1 Tim Mei Avenue, Central Hong Kong

REPORT OF THE MANAGER

Interim Report

As at 31 December 2018

This Interim Report does not constitute an offer of units. Units are offered on the basis of the information contained in the current Explanatory Memorandum (and the documents referred to within it), copies of which are available from the registered office of the Manager or from any of the companies registered as distributors of VL China Fund (the Fund).

Review

The Fund headed south in the second half of 2018, the magnitude of which was larger than the MSCI China Index* and the Hang Seng Index* caused by our greater exposure to the healthcare sector while the indices were more weighted on financial stocks. Market sentiment was lackluster and stocks fell almost across the board amid China's deleveraging and her harsh policies on various sectors, as well as the persisting US-China trade wars. The market stabilized in November on expectation that the US and China might reach some consensus on trade. Both countries did agree to hold off raising tariffs until 31 March 2019. However, peace was short-lived. US stocks tumbled in December on the Fed's rate hike and quantitative tightening as well as concern on worsening corporate earnings. Major global markets also followed downward.

As early as in 2014, we had pointed out that technology and healthcare would become two of the major growing trends in the stock market. Our early identification of the trend and investment in relevant stocks (including Tencent (700 HK) and Sino Biopharmaceutical (1177 HK) in about 2017) brought us lucrative investment gains through May. Unfortunately, those gains reversed into losses in the face of policy headwinds this year - the outbreak of a trade war between the US and China, the souring of sentiment in US technology stocks (triggered by Facebook's (FB US) data protection scandal in March and worries on the operational outlook of technology companies following President Donald Trump's criticism on Amazon (AMZN US)) and the sudden rollout of policies by Beijing targeting the mobile game, healthcare and education sectors respectively – all these impacted a number of the stocks in our portfolio.

We raised the alarm (in late 2017) that any geopolitical risks might stir up market volatility and that the political risk or policy risk of the U.S. (February) would be no smaller than China's. Accordingly, we have made more allocations to technology stocks and PRC healthcare counters and they have shot up dramatically in the first five months of 2018 generating decent investment gains for the Fund. In hindsight, more investment gains should have been crystalized in or around May.

Healthcare and information technology (IT) sectors may not appear very rosy at this moment but there are two unperturbed mega investment themes already forming (not only in China but also in other economies): population growth (China: 1.4 billion) and rising consumption power. Looking at the IT universe, our core research and investment are on data storage, social media and electronic payment which have demonstrated rapid business growth in the past. The bigger potential of these

segments has yet to be developed in many parts of the world and we will wait for a better entry level with greater margin of safety.

PRC healthcare stocks were mostly oversold in the past few months amid the vaccination scandal and generic drug price-cut policies due to the centralized procurement pilot scheme. However, if we look at China's demographics (an aging but wealthier population), healthcare remains structurally important and the sector prosperous in the middle to longer run. At the start of 2019, some main street brokers have started to revise upward the ratings on the sector. In brief, the government's procurement scheme should affect manufacturers focused on generics drugs, but they are not our picks, and neither are any vaccine manufacturers on our portfolio list. Our spotlight will continue to be put on pharmaceutical and biotech companies with a diversified product portfolio, and those with a larger mix of higher margin innovative drugs, since they have greater earnings growth visibility and resilience, and can better manage generics pricing pressure.

To alleviate the impact from policy risks in China and the US, we have stepped up diversification of our exposure to more defensive plays having a utility-like nature. Telecoms service providers PCCW (8 HK) and CITIC Telecom International (1883 HK) are some examples. The former enjoys steady recurrent income from Hong Kong and the latter from Macau. We also added companies which are highly insulated from the US market and hence less trade war risk. Examples include SITC International (1308 HK) and Bank of China Hong Kong (2388 HK).

In the first half, companies which generated the most investment returns to the Fund included Natural Beauty (157 HK), CITIC Telecom, China Oriental (581 HK), SITC International and PCCW.

The Fund was almost fully invested with 4.43% cash as at 31 December 2018.

Outlook

Investors may recall that in May 2010, the spread of government debt crisis from Greece to other PIIGS countries dragged the MSCI China Index down by 5.5% and the Hang Seng Index 5.6%. In August 2015, the sudden depreciation of the Chinese yuan led to a correction in the global financial markets and both indices tumbled approximately 12% in a single month (the Fund was launched at that same month). In January 2016, fears on tumbling oil prices, China's seemingly escalating liquidity risk and possibility of a further depreciation in the yuan pushed the MSCI China Index down 12.7% and the Hang Seng Index 10.6%. These past periods were hard times but the portfolios managed by us were able to pick up fast and scaled new heights again when the broader market calmed down and the hidden value or growth momentum of stocks were released.

On the China healthcare sector, sentiment continues to improve for the month of January. Implementation details of the GPO centralized procurement program released continue to focus more on drug quality and supply under the pilot program, with implementation rather than expansion as a priority when the first drug delivery begins in March. It was also announced that beginning 1 Mar 2019, a 3% VAT reduction for 21 rare disease drugs and 4 active pharmaceutical ingredients would be introduced, which is a positive for drug usage in these categories. During the month, the State Council also released guidelines for the operation of Class 3 hospitals amongst which there is no longer a requirement to use a defined drug sales ratio for hospitals as a performance metric.

This bodes well for rational hospital drug volume use and is a positive for the healthcare sector.

China's GDP growth rate in 2018 stood at 6.6%, the weakest in nearly three decades. That said, the figure is still strong compared with many developed countries. China's domestic consumer market remains robust growing at a faster pace than Western countries (sales of Alibaba (BABA) on 11 November 2018 hit US\$30.8 billion, up almost 22% YoY and exceeded the spending by consumers during any single US shopping holiday). While China's deleveraging process may not have completed, the government is responsive and has rolled out supportive measures to boost the market. Recent actions included the tax cut for individuals and lowering of required reserve requirement ratio to free up US\$116 billion for new lending. China is in the process of turning itself from an export-driven economy to a consumption-led economy. From this perspective, we are optimistic about its growth outlook, though we are cautious about the ever present policy risks.

Stock markets started 2019 on a negative backdrop and it would be unrealistic not to expect some more volatility in the first half. Nevertheless, having undergone a decline sharper than other developed markets, the Sino-Hong Kong markets provide relatively higher margin of safety given their lower valuations (P/E of Hang Seng Index at 10.4X and P/B at 1.27X; P/E of Shanghai Composite Index at 9.69X and P/B at 1.36X). The potential upside, which at the peaks of a market with the average PE multiples as high as 18-20X, will be substantially higher than the downside.

Fund performance

As at 31 December 2018, the Fund was down 23.07% (Class A) and for reference purposes, the MSCI China Index was down 17.58% and Hang Seng Index fell 9.16% with dividends reinvested, over the period 1 July 2018 to 31 December 2018.

*Index figures are dividend reinvested.

VL Asset Management Limited

20 February 2019

**STATEMENT OF NET ASSETS
AS AT 31 DECEMBER 2018**

	(Unaudited) 31.12.2018 HK\$	(Unaudited) 31.12.2017 HK\$
ASSETS		
Cash and bank balances	11,137,628	4,060,757
Amounts due from brokers	-	2,019,129
Financial assets at fair value through profit or loss	228,553,890	313,533,025
Dividend receivable	958	51,208
Other receivables and prepayments	277,084	460,682
TOTAL ASSETS	<u>239,969,560</u>	<u>320,124,801</u>
LIABILITIES		
Management fee payable	563,666	467,298
Trustee fee payable	109,742	55,114
Performance fee payable	42	3,139,875
Amounts due to brokers	-	635,801
Accruals and other payables	152,791	141,668
LIABILITIES (EXCLUDING NET ASSETS ATTRIBUTABLE TO UNITHOLDERS)	<u>826,241</u>	<u>4,439,756</u>
NET ASSETS ATTRIBUTABLE TO UNITHOLDERS	<u>239,143,319</u>	<u>315,685,045</u>
TOTAL LIABILITIES (INCLUDING NET ASSETS ATTRIBUTABLE TO UNITHOLDERS)	<u>239,969,560</u>	<u>320,124,801</u>
UNITS IN ISSUE		
- Class A	495,002.7319	526,718.9612
- Class B	<u>2,282,104.8000</u>	<u>2,282,104.8000</u>
NET ASSET VALUE PER UNIT (Note 1)	HK\$	HK\$
- Class A	83.8689	110.0973
- Class B	<u>86.5990</u>	<u>112.9197</u>

**STATEMENT OF PROFIT OR LOSS
FOR THE PERIOD ENDED 31 DECEMBER 2018**

	(Unaudited) From 1.7.2018 to 31.12.2018 HK\$	(Unaudited) From 1.7.2017 to 31.12.2017 HK\$
INCOME		
Dividend income	2,723,578	3,544,984
Net gain / (loss) on financial assets at fair value through profit or loss	(71,106,677)	34,507,496
Net foreign exchange differences	(17,576)	(100)
Interest income	1,357	299
Other income	1,035	-
TOTAL INCOME	<u>(68,398,283)</u>	<u>38,052,679</u>
EXPENSES		
Management fees	1,191,519	1,384,604
Trustee fees	359,968	360,039
Performance fees	42	3,139,875
Custodian fees	107,431	105,361
Establishment costs	93,047	93,047
Auditors' remuneration	125,808	102,589
Brokerage commission	208,511	222,178
Transaction costs	195,650	227,058
Legal and professional fees	-	39,920
Bank charges	1,200	1,200
Other operating expenses	31,200	31,200
TOTAL EXPENSES	<u>2,314,376</u>	<u>5,707,071</u>
PROFIT / (LOSS) BEFORE TAX	<u>(70,712,659)</u>	<u>32,345,608</u>
Withholding tax	(147,606)	(144,242)
PROFIT / (LOSS) AFTER TAX	<u>(70,860,265)</u>	<u>32,201,366</u>
Other comprehensive income for the period	-	-
INCREASE / (DECREASE) IN NET ASSETS ATTRIBUTABLE TO UNITHOLDERS AND TOTAL COMPREHENSIVE INCOME FOR THE PERIOD	<u>(70,860,265)</u>	<u>32,201,366</u>

EXPLANATORY NOTES

1. NET ASSETS ATTRIBUTABLE TO UNITHOLDERS

The published net asset value per unit issued is calculated in accordance with the Explanatory Memorandum while the net asset value per unit as reported in the statement of net assets included the following adjustment:

- (a) The last business day for the period ended 31 December 2017 was 29 December 2017. The net asset value per unit as reported in the statement of net assets includes the fees and expenses accrued up to the last day of the relevant reporting period end.

A reconciliation of the net assets attributable to unitholders as reported in the statement of net assets to the net assets attributable to unitholders as determined for the purposes of processing unit subscriptions and redemptions is provided below:

	31.12.2018 HK\$	31.12.2017 HK\$
Published net assets attributable to unitholders	239,143,319	315,704,442
Adjustment on fees and expenses accrued up to the last day of the reporting period end	-	(19,397)
Net assets attributable to unitholders as per statement of net assets	239,143,319	315,685,045

	Unit Price as at 31.12.2018 (per statement of net assets) HK\$	Published unit price as at 31.12.2018 HK\$	Unit Price as at 31.12.2017 (per statement of net assets) HK\$	Published unit price as at 29.12.2017 HK\$
- Class A units	83.8689	83.8689	110.0973	110.1069
- Class B units	86.5990	86.5990	112.9197	112.9260

The net asset value is calculated by determining the value of the assets attributable to VL China Fund, including accrued income, and deducting all its liabilities as at the relevant reporting period end. The resultant sum is divided by the total number of units in issue as at the relevant reporting period to give the net asset value per unit and adjusting the resultant sum to the nearest 4 decimal places.

**SCHEDULE OF INVESTMENTS (UNAUDITED)
AS AT 31 DECEMBER 2018**

	Holdings	Fair Value as at 31.12.2018 HK\$	% of NAV
Listed / Quoted Investments			
CHINA (10.0%)			
Angel Yeast Co Ltd	158,106	4,548,900	1.9
Chongqing Changan Automobile Co Ltd	471,568	1,645,772	0.7
Huadong Medicine Co Ltd	49,500	1,493,605	0.6
Jiangsu Hengrui Medicine Co Ltd	39,120	2,353,218	1
Kweichow Moutai Co Ltd	10,000	6,728,220	2.8
Midea Group Co Ltd	166,800	7,011,198	3
		<u>23,780,913</u>	<u>10.0</u>
HONG KONG (83.1%)			
3Sbio Inc	422,000	4,236,880	1.8
Agile Group Holdings Ltd	94,000	865,740	0.4
Agricultural Bank Of China Ltd	1,241,000	4,256,630	1.8
AIA Group Limited	44,000	2,860,000	1.2
ASM Pacific Technology Limited	20,000	1,509,000	0.6
BOC Hong Kong (Holdings) Ltd	144,000	4,190,400	1.8
Chanhigh Holdings Limited	334,000	317,300	0.1
China Communications Services Corp Ltd	200,000	1,296,000	0.5
China Construction Bank Corporation	1,680,000	10,852,800	4.5
China Merchants Bank Co Ltd	273,000	7,835,100	3.3

SCHEDULE OF INVESTMENTS (UNAUDITED)**AS AT 31 DECEMBER 2018**

	Holdings	Fair Value as at 31.12.2018 HK\$	% of NAV
Listed / Quoted Investments			
China Merchants Port Holdings Co Ltd	3,956	55,780	0
CSPC Pharmaceutical Group	314,000	3,548,200	1.5
China Resources Land Limited	100,000	3,010,000	1.3
China Resources Power Holding	360,000	5,421,600	2.3
China Traditional Chinese Medicine Holdings Co Ltd	930,000	4,240,800	1.8
China Vanke Co Ltd	141,000	3,750,600	1.6
China Yuhua Education Corporation Ltd	1,364,000	4,337,520	1.8
CITIC Telecom International Holdings Ltd	5,466,000	15,031,500	6.3
COSCO Shipping International (Hong Kong) Co Ltd	698,000	1,877,620	0.8
Galaxy Entertainment Group	98,000	4,880,400	2
Giordano International Ltd	954,000	3,529,800	1.5
Greatview Aseptic Packaging Company Ltd	317,000	1,347,250	0.6
Guangzhou Baiyunshan Pharmaceutical Holdings Co	264,000	7,405,200	3.1
Haitian International Holdings	272,000	4,107,200	1.7
Health And Happiness H&H International Holdings Ltd	28,000	1,251,600	0.5
Hong Kong Exchanges & Clearing Limited	26,877	6,090,328	2.6
Kingboard Holdings Limited	44,000	919,600	0.4
KWG Group Holdings Ltd	383,000	2,654,190	1.1
Livzon Pharmaceutical Group Inc	210,330	4,785,008	2
Maoye International Holdings Ltd	1,897,000	1,005,410	0.4

SCHEDULE OF INVESTMENTS (UNAUDITED)**AS AT 31 DECEMBER 2018**

	Holdings	Fair Value as at 31.12.2018 HK\$	% of NAV
Listed / Quoted Investments			
PCCW Ltd	2,292,000	10,336,920	4.3
Pentamaster International Ltd	1,732,000	1,541,480	0.6
Ping An Insurance (Group) Company of China, Ltd	80,000	5,532,000	2.3
Plover Bay Technologies Ltd	1,100,000	1,232,000	0.5
Precision Tsugami (China) Corporation Ltd	92,000	658,720	0.3
Shanghai Fosun Pharmaceutical Co Ltd	95,000	2,185,000	0.9
Sino Biopharmaceutical Ltd	1,781,000	9,189,960	3.8
Sisram Medical Ltd	308,000	1,228,920	0.5
SITC International Holdings Company Ltd	645,000	4,760,100	2
Swire Pacific Ltd - 'B'	280,000	3,656,800	1.5
TCL Electronics Holdings Ltd	728,000	2,184,000	0.9
Tencent Holdings Ltd	37,900	11,900,600	5
Transport International Holdings Ltd	265,200	5,728,320	2.4
Travelsky Technology Ltd	264,000	5,293,200	2.2
Want Want China Holdings Ltd	216,000	1,183,680	0.5
WH Group Ltd	636,000	3,835,080	1.6
Wuxi Biologics Cayman Inc	68,500	3,435,275	1.4
Wynn Macau Ltd	101,600	1,735,328	0.7
Xinyi Glass Holdings Co Ltd	300,000	2,598,000	1.1

SCHEDULE OF INVESTMENTS (UNAUDITED)**AS AT 31 DECEMBER 2018**

	Holdings	Fair Value as at 31.12.2018 HK\$	% of NAV
Listed / Quoted Investment			
Yuzhou Properties Co Ltd	955,000	<u>3,084,650</u>	<u>1.3</u>
		<u>198,769,489</u>	<u>83.1</u>
UNITED STATES (2.5%)			
Airmedia Group Inc – ADR	212,100	416,812	0.2
Alibaba Group Holdings Ltd -Sp ADR	4,352	4,670,432	2
Huazhu Group Ltd	360	80,696	0
TAL Education Group- ADR	4,000	<u>835,548</u>	<u>0.3</u>
		<u>6,003,488</u>	<u>2.5</u>
TOTAL INVESTMENTS		228,553,890	95.6
OTHER NET ASSETS		<u>10,589,429</u>	<u>4.4</u>
PUBLISHED NET ASSETS ATTRIBUTABLE TO UNITHOLDERS		<u>239,143,319</u>	<u>100.0</u>
TOTAL INVESTMENTS, AT COST		<u>271,418,865</u>	

**INVESTMENT PORTFOLIO MOVEMENTS (UNAUDITED)
AS AT 31 DECEMBER 2018**

	% of holdings 31.12.2018	% of holdings 31.12.2017
Listed / Quoted investments		
China	10.0	16.0
Hong Kong	83.1	74.3
United States	2.5	9.0
	<u>95.6</u>	<u>99.3</u>
Other net assets	<u>4.4</u>	<u>0.7</u>
Net assets attributable to unitholders	<u><u>100.0</u></u>	<u><u>100.0</u></u>