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

VL China Fund

A CIES-eligible fund

Monthly Fund Factsheet

June 2018

Important Information

- VL China Fund is constituted in the form of a unit trust established under the laws of Hong Kong.
- The fund is on the **List of the Eligible Collective Investment Schemes under Capital Investment Entrant Scheme (CIES).**
- The fund seeks to achieve its investment objective primarily through exposure to companies carrying on business or with business exposure in the China region with long term growth prospects.
- The fund can invest no less than 70% of its NAV in Hong Kong-listed stocks and if investing in overseas stocks, no more than 30% of its NAV in non-Hong Kong listed stocks.
- All investments involve risks. This material is not an offer or solicitation. The fund is an investment fund. There is no guarantee on the repayment of principal. The fund's investment portfolio may fall in value and therefore your investment in the fund may suffer losses. If you have any queries, please consult your financial consultants. This material has not been reviewed by the Securities and Futures Commission.

Investment Objective

The fund aims to provide long-term capital appreciation by investing in a diversified portfolio of equity securities of companies in different industry sectors whose primary business focus is in the China region.

Performance Update*

	Class A Units	Class B Units	MSCI China (NDEUCHF)	Hang Seng Total Return Index
1 month	-5.45%	-5.94%	-5.20%	-4.54%
3 month	-3.05%	-3.22%	-3.53%	-2.57%
6 month	-0.99%	-0.70%	-1.32%	-1.68%
YTD	-0.99%	-0.70%	-1.32%	-1.68%
Since fund launch	9.02%	12.14%	39.35%	30.40%
NAV per unit	109.0154	112.1352	n/a	n/a

* *NAVs and indices as of 29 June 2018.*

Class A and B units are invested in the same fund. Dividends are reinvested into the fund. Performance of class A Units and B Units is calculated by VL Asset Management Limited in HKD on a NAV to NAV basis. Performance data is net of all fees. NAVs are published daily in the Standard and Hong Kong Economic Times and www.vlasset.com.
Indices are derived from Bloomberg and are valued in HKD with dividend reinvested. All indices and figures are for reference only.

Fund Facts

Manager:	VL Asset Management Limited
Trustee	Standard Chartered Trust (Hong Kong Limited)
Custodian & Administrator	Standard Chartered Bank (Hong Kong Limited)
Launch date:	10 August 2015
Base currency:	Hong Kong Dollars (HKD)
Bloomberg code:	Class A - VLCHINA KY Class B - VLCHINB KY

Portfolio Characteristics

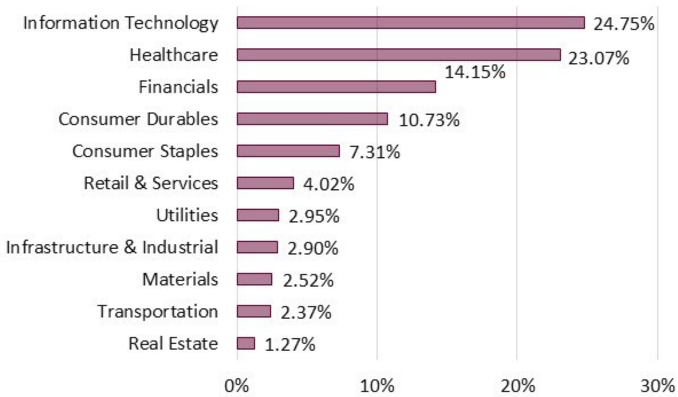
	Fund	Hang Seng Index
Price/earnings ratio	14.72X	11X
Price/book ratio	1.89X	1.22X
Dividend yield	2.55%	3.69%
Return on equity	12.81%	11.10%

VL China Fund

Top 5 Stock Holdings

Name	Bloomberg Code	Sector	%
Tencent	700 HK Equity	Information Technology	7.07%
Alibaba Group -ADR	BABA US Equity	Information Technology	6.22%
Sino Biopharmaceutical	1177 HK Equity	Healthcare	5.90%
China Construction Bank Corp - H	939 HK Equity	Financials	3.94%
Hong Kong Exchanges	388 HK Equity	Financials	3.40%
Total			26.54%

Exposure by Sector



Exposure by Geography

HK	H Shares	17.77%
	Red Chips	8.08%
	P-Chips	31.94%
	HK	11.19%
	Others	2.22%
	Sub-Total	***71.20%***
China	A Shares	12.13%
	B Shares	1.21%
	Sub-Total	***13.34%***
US	ADRs of PRC companies	10.75%
	Others	0.75%
	Sub-Total	***11.50%***
Cash		**3.97%**
	Grand Total	100%

No derivative exposure; Cash refers to cash in bank, trade and dividend receivables, prepaid expenses and expense accruals.

Fee Structure

	Class A Units	Class B Units
Minimum subscription	HK$50,000	HK$39,000,000
Subsequent subscription	HK$5,000	HK$1,000,000
Subscription fee	up to 5%	up to 5%
Redemption fee	nil	5%
Management fee	1.5%	0.75%
Performance fee	15% (high on high)	7.5% (high on high)
Lock-up	nil	3 years
Dealing day	daily (Hong Kong business day)	

VL Investment Team

Chief Investment Officer	Vincent LAM
Portfolio Managers	Kian Heng NG, Kenneth HO

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Sentiment hit by RMB depreciation and trade spats

Large capital outflows were also seen as corporates rushed to increase their liquidity before their 30 June fiscal year end. In mid-June, the People's Bank of China (PBOC) lowered the currency's daily fixing rate for more than 10 consecutive days, a move believed to boost domestic demand and to counter pressure from the tariff tensions. The PBOC also announced on June 24 that it would cut the reserve requirement ratio by 50 basis points effective 5 July, which was expected to release a total of RMB500 billion to China's banking system.

Healthcare stocks, having rallied for months, slipped back in June causing the Fund's NAV to retreat as healthcare was our second largest sector (and for most of the time in the first half), represented nearly one fourth of our exposure. In light of the extreme market volatility in June, some sectors (such as financial and consumer) also fell both on monthly and year-to-date basis pulling down our NAV (Class A units: down 0.99%; Class B units: down 0.70%) for the half year. During the same period, the Hang Seng Total Return Index was down 1.68% and the MSCI China Total Return Index was down 1.32%.

Nevertheless, among our 10 most profitable positions during the first half, four were healthcare stocks with Sino Biopharmaceutical (1177 HK) and CSPC Pharmaceutical (1093 HK) topping the list. Others included Hua Hong Semiconductor (1347 HK) and MMG (1208). Separately, stocks that had made the biggest investment loss included Rusal (486 HK), China Merchants Bank (3968 HK) and Ping An Insurance (2318 HK).

Political risks are never easy to predict or assess. In a time full of uncertainties, some investors may stay sidelined while some may opt for a rush exit. The across-the-board decline of stocks in late June simply suggested that investors reduced their long exposure regardless of company fundamentals. To us, that merely presented an opportunity to selectively bargain hunt long term investment. However, many of the stocks on which we have a long term optimistic view remained relatively expensive. Hence we did not undertake any substantial buy actions during the month.

Even in worst scenario, China can be self-sufficient

Looking back at our December newsletter, we have mentioned that "Following the completion of the 19th National Congress of the Chinese Communist Party, regulators in different disciplines have expressed that they will step up to reduce the reliance on financial leverage... No doubt certain stakeholders will be affected with the introduction of any deleveraging measures but it will do good to the healthy development of China in the longer run." The Chinese government has been quite effective in executing its continuous policies in de-capacity, de-stocking and de-leveraging. Among the three, de-leveraging is still in progress. It is inevitable that the deleveraging process will be painful but, if successful, will sustain the longer term development of the Chinese economy. Our analysis has urged us to be prepared for the market volatility triggered by China's deleveraging. What we may have under-estimated is probably the impact of Sino-US trade war on the global macro economy and investor sentiment. While the market (ex-China) widely anticipates that China could lose more than the US ultimately in the trade conflicts, one should bear in mind that comparing to the US, China's domestic market is no smaller (in fact, 3.2 times greater than the US in terms of population), its savings rate is much higher and GDP per capita is on the rise. Even in the worst-case scenario, China can be self-sufficient backed by its strong domestic demand.

As we write, President Xi is having an active participation in the BRICS summit in Johannesburg paving way for more trade cooperation with developing countries in light of US's protectionism. Separately, according to International Monetary Fund, global growth is expected to pick up to 3.9% this year. The growth of the BRICS countries are projected as follows - Brazil at 2.2%, Russia 1.7%, India 7.4%, China 6.6% and South Africa 1.5%. The projected growth for developed countries including the US and Japan are respectively at 2.9% and 1.2%. If grouping emerging and developing Asia together, this segment is expected to grow 6.5%. As for the major advanced economies (G7), the estimate stands at 2.4% only. The trade tensions led by Trump may urge developing countries, which are growing at higher rates than developed nations, to converge their strength and become closer trade partners in time to come. We would then see a part of the world's economy decreasingly dependent on the US.

Stick with healthcare and avoid high gearing companies

Companies with high gearing (including infrastructure, mainland properties and vehicle sales agencies) have been hard hit in the past few months but they have never been on our radar screen. We will also continue to avoid sectors relying on government subsidies and/ or under government protection against imported goods. Despite the cloudy market outlook, selected sectors or stocks are able to report promising revenue and profit growth figures. One of our top sectors is PRC healthcare, which has been expanding by more than 15% per annum over the past decade. Taking Sino Biopharmaceutical (1177 HK) as an example, it was initially listed on the Hong Kong GEM (Growth Enterprise Market) board in 2000 at an initial offer price of HK$1.20 (or split adjusted 4.44 HK cents) and switched to the Main Board in December 2003. Back in 2005, it was selected by Forbes Asia as one of 200 "Best Under a Billion" companies suggesting its market value was below HK$10 billion but its market capitalization has surpassed HK$100 billion in 2017 and hit HK$150 billion in July 2018. Since IPO, total shareholders' return had been 470 times (inclusive of dividends). Net profit figures have also been impressing as it made HK$81.62 million for full-year 2003 but the number had jumped to RMB3.65 billion (approximately HK$4 billion) for full-year 2017.

In mid-July, sentiment in pharmaceutical stocks was dampened by a scandal in the mainland. Chinese authorities discovered that hundreds of thousands of doses of at least two different vaccines - rabies and diphtheria & tetanus - were defective, all manufactured by a Jilin-based drug maker, Changsheng Biotechnology. A number of executives of the company are now under criminal investigation. Knowing very well that both good and bad business operators can exist in every industry and every country, we have endeavoured to take extra due diligence efforts in assessing a company's corporate governance as well as product quality standards before making an investment – apart from analyzing its financial figures, we also study its corporate history and verify the information or data among its suppliers, customers and competitors. The pharmaceutical stocks that are selected for our portfolio are typically characterized by companies which have (i) a comprehensive product portfolio and an innovative R&D drug pipeline as well as (ii) demonstrated a history of good and consistent product quality, having met the requisite safety standards.

Continuous robust growth seen in various IT segments

On the information technology (IT) front, the tech heavy index NASDAQ Composite hit a historical high again in July 2018 as the IT sector regained market attention. We won't be surprised if the tech euphoria (similar to that in 2000) will return sometime next year or after. Segments including online gaming, ecommerce, cloud, semiconductor, streaming TV as well as online payment have all undergone very rapid growth in the past few months. In view of the wider popularity of online payment, Alibaba (BABA US) has seen its share price up nearly 30% over the past 12 months. Furthermore, the application of technology has expanded to other industries such as consumption, banking and tourism. One example is Huazhu Group (HTHT US), which owns China Lodging, a leading and fast-growing multi-brand hotel group in Mainland China. With a very user-friendly and popular online booking platform, its share price has soared 50% in the last 12 months. Again, business prospects and stock price performance of companies within the same sector can vary substantially and it is during our preliminary research process that we will make our best effort to initially differentiate the strong companies from the weak ones.

Whilst the market is likely to remain bumpy in the near future, it is now more important than ever not to abandon stocks which possess promising growth outlook as they are not only the main drivers for a bounce-back when the temporary storm is over, but also the pillars to support long term value appreciation.

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