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

VL China Fund

Monthly Fund Factsheet

December 2019

Important Information

- VL China Fund is constituted in the form of a unit trust established under the laws of Hong Kong.
- 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	4.68%	4.67%	7.79%	7.02%
3 month	10.99%	11.12%	13.98%	8.35%
6 month	9.45%	9.78%	8.98%	0.18%
YTD	30.08%	30.96%	22.78%	12.87%
Since fund launch	9.10%	13.41%	41.01%	33.70%
NAV per unit	109.0961	113.4065	n/a	n/a

* *NAVs and indices as of 31 December 2019.*

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

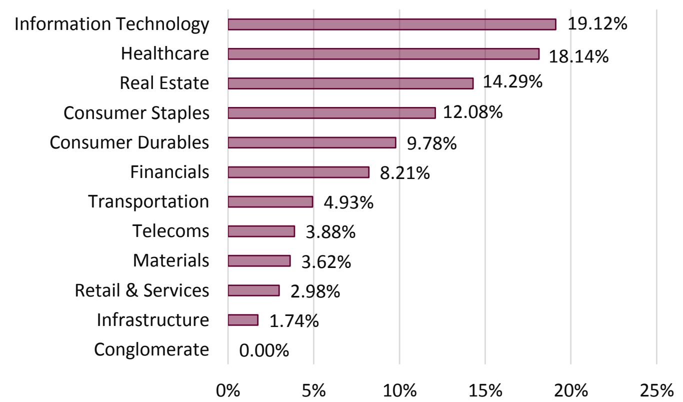
	Fund	Hang Seng Index
Price/earnings ratio	13.36X	9.89X
Price/book ratio	1.80X	1.06X
Dividend yield	2.78%	4.08%
Return on equity	13.48%	10.74%

VL China Fund

Top 5 Stock Holdings

Name	Bloomberg Code	Sector	%
Tencent	700 HK Equity	Information Technology	4.16%
Citic Telecom International	1883 HK Equity	Telecoms	3.88%
Wuxi Biologics	2269 HK Equity	Healthcare	3.85%
Alibaba Group	BABA US Equity	Information Technology	3.84%
Sino Biopharmaceutical	1177 HK Equity	Healthcare	3.69%
Total			19.43%

Exposure by Sector



Exposure by Geography

HK	H Shares	10.28%
	Red Chips	15.82%
	P-Chips	34.93%
	HK	7.00%
	Others	3.32%
	Sub-Total	***71.36%***
China	A Shares	22.59%
	B Shares	0%
	Sub-Total	***22.59%***
US	ADRs of PRC companies	4.57%
	Others	0.24%
	Sub-Total	***4.81%***
Cash		**1.24%**
	Grand Total	100.00%

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 Siu Yeung
Portfolio Manager	Andy NG Kian Heng

You should not make investment decisions based on this material alone. If you plan to invest in VL China Fund, you should read its Explanatory Memorandum and the Key Fact Sheet for details and the risk factors set out in those documents.
In particular, you should be aware of the concentration of the fund's investments in China and Hong Kong giving rise to possibly greater volatility compared with broad-based global funds. You should note too that VLAM, as manager of the fund, is entitled to receive performance fees under certain conditions, that such fees may encourage a manager to make riskier investment decisions than in the absence of performance-based incentive systems and that you should familiarize yourself with the method of calculating such fees.
Performance fee will be charged only if the NAV at the end of the financial year exceeds the "high watermark", which is the all-time year-end high of the fund's NAV. The fund's financial year end is 30 June.
Without prejudice to the generality of the foregoing, this report does not constitute, and may not be used for the purposes of, an offer or solicitation to anyone in any jurisdiction or country in which such offer or solicitation is not authorized or to any person to whom it is unlawful to make such offer or solicitation or where such offer or solicitation would be contrary to law or regulation or which would subject VLAM or its affiliates or associates (including VL Trusts) to any registration requirement within such jurisdiction or country.
Under no circumstances may the information contained herein, or any part thereof, be copied, reproduced or redistributed without the express permission and written consent of VLAM.
The price of shares of any unit trust may go down as well as up and past performance figures shown are not indicative of future performance.
Classification is based on Global Industry Classification Standard (GICS). Exposure refers to long exposure unless otherwise specified.
SFC authorization is not a recommendation or endorsement of a scheme nor does it guarantee the commercial merits of a scheme or its performance. It does not mean the scheme is suitable for all investors nor is it an endorsement of its suitability for any particular investor or class of investors.

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VL China Fund

Fourth-Quarter & Full-Year Commentary December 2019

Portfolio Up 30% YTD Despite Market Turbulence Led by Trade War

The fund rallied 30.08% (Class B: 30.96%) in the full year ended December, thanks to the outperformance of our positions in consumer goods and pharmaceutical counters. The MSCI China Total Return Index and the Hang Seng Total Return Index* was up 22.78% and 12.87% respectively during the year.

China's macro data announced in December was more or less in line with market expectation. China Caixin Purchasing Manager Index was 52.5, slightly below November's 53.5 but remained strong. Geopolitical concerns over Sino-US trade war which dominated 2019 faded in the last quarter, helping Greater China equity markets to post gains amid improved investor sentiment. Under the phase one trade agreement inked in December, the US will suspend tariffs on US$160 billion of Chinese imports previously scheduled to take effect on 15 December. Existing tariffs on US$120 billion of Chinese imports are set to be cut to 7.5% from 15% from mid-January 2020. In exchange, China will increase her purchases of US agricultural goods.

Portfolio Review and Reflections

During the year, the fund's investment gains were largely attributable to our growth strategy. Among our top ten investment gain generators, four were consumer staples/ durables, another two being pharmaceutical companies, and the remaining respectively a real estate service provider, a property developer, a PRC bank and an information technology (IT) operator. We are value investors with long experience in identifying undervalued stocks but that does not mean we have to limit our universe to traditional value stocks – in recent years we have focused more on growth stocks with good potential to release their hidden value as and when their businesses accelerate and the industry expands.

Our biggest investment gains came from Sino Biopharmaceutical (1177 HK), Kweichow Moutai (600519 CH), Midea (000333 CH), Wuliangye (000858), Luzhou Laojiao (000568), Wuxi Biologics (2269 HK), A-Living (3319 HK) and China Merchants Bank (3968). The sectoral diversification we pursued had helped minimized the volatility of the portfolio.

White Wine Liquor, Household Electric Appliance Makers, Healthcare Outshine

Consumer staples/ durables and healthcare were the top two sectors that created the most of investment returns to the fund over the year. We stated two years ago that our investment theme would be on healthcare, consumer-related and IT sectors (given the population matrix of China and the increasingly globalized demand on IT services). For healthcare, despite the known policy risks (such as GPO tendering) or any unseen risks in the future, the sector remains structurally vital to its citizens and the sector likely to hold up at least in the next decade.

Our consumer holdings were largely composed of Chinese white wine liquor and household electric appliance manufacturers. Many of them have staged a double-digit rally last year. Take Kweichow Moutai as an example, its stock price was up 100.5% YoY – that had prompted us to lock up some profit and deployed the proceeds to other consumer names which are relatively lagging behind. The fund's another core pick in the sector was Wuliangye which share price was up 161% YoY. The company announced during its annual distributor convention that revenues for full year 2019 rose more than 25% YoY and they were expecting at least 5-8% volume growth and double-digit revenue growth of 15-20% in full year 2020. The company also said that their present focus was on channel pricing and achieving price stability. Wuliangye would look to launch new products in the first quarter of 2020 – its 80s series would have a higher pricing than 8G. That should be positive to drive its business and share price growth.

As regards pharmaceutical positions, the official GPO list was announced in December with 33 drugs instead of 35 and official bidding will take place in January. In terms of the bidding framework, some adjustments have been made versus previous versions aiming to make the bidding less competitive with an average price cut of approximately 60%. That should reduce the incentive for the bidder to bid lower therefore avoiding a spiraling downward price effect. Our focus will be on bio-tech drugs (as opposed to generic drugs) which profit margin is secured by higher entry barrier and technology requirement. Earnings results of most of the healthcare companies we selected were robust suggesting further valuation re-rating potential.

During the year, we continued to maximize our exposure to China A-shares (from 9.3% at the year end of 2018 to 22.6% as of 31 December 2019) as they remained largely undervalued compared to many other major stock markets. Select corporations and sectors have just kicked start a secular growth trend and their earnings are supported by a huge population of 1.4 billion which is getting increasingly wealthy. At the time of writing, the Shanghai Composite Index has a 2020FY forward P/E of 10.77X (Hang Seng Index is also undemanding at 10.26X) and P/B at 1.25X (Hang Seng: 1.09X).

VL China Fund

Geopolitical Risks Linger But Opportunities in China Remain

The US presidential election will be held in November and it is likely President Donald Trump will in the interim period seek to maintain a peaceful relationship with other countries including China and that should mean a pause to the Sino-US trade dispute at least till November. Global investor risk appetite may therefore pick up in the first half of 2020. Nevertheless, geopolitical risks shall continue to exist as troubles can flare up again in North Korea and some Middle East countries. Also, global interest rates might continue to hover near zero level as some of the major central banks might keep printing money resulting in abundant liquidity (at least for the first half of 2020) while exposing financial assets to higher risks (including stagflation, rising operating costs, shrinking global demand and declining profit margins).

China's economic growth is projected to edge down further to 6% or below in 2020. Some worry that the deceleration will drag down her equity market but one should note that the performance of China A-shares has never gone in tandem with the country's GDP growth. As mentioned in our previous newsletters, one may find comfort in the improved quality of growth since 2018 as the pace of debt accumulation has slowed and the financial system is more effectively regulated. One should also note that in the recent first-phase trade deal with the US, China has agreed to further open up some of her markets (insurance, for example) to promote foreign trade and internationalize her ecosystem. In addition, backed by a huge reserve, China is able to roll out more economic stimulus measures – this can be exemplified by a further cut in the reserve requirement ratio on 2nd January, 2020 releasing 800 billion RMB capital into the banking system. Back to Hong Kong, her GDP is also slowing but for the majority of listed companies traded here (approximately 70-80% by our estimate), their profits are not derived from the local economy. The present business outlook of locally listed companies might therefore be unduly pessimistic. However, given a wider choice of investment opportunities in China A-shares, our team may allocate more to the China book from Hong Kong.

Future Investment Directions

The latest outbreak of pneumonia in the central Chinese city of Wuhan has triggered the nerves of many major stock markets. While staying alert to monitor if any listed company may be adversely affected (for instance, those with business related to travel and offline consumption), we shall look out for opportunities to bottom fish undervalued plays. Looking into 2020, we would like to share with you our initial investment focus as follows:

1) Assets with a scarcity feature (for example, select biotech companies with unique skillset);
2) Quality growth with visibility (which can be testified by a company's sound track record);
3) Liquid assets (which may mean more diversified exposure to international markets); and
4) Longer term investment themes while maintaining flexibility to switch stocks when better opportunities arise

It has always been our objective to grow wealth for our investors on a sustainable basis. With our resilience and discipline demonstrated over the past decade, and the backing of our investors (many of whom may have known our team members for almost two decades), VL Asset has remained one of the few home-grown asset managers in Hong Kong with sound risk governance and management mechanisms. We take this opportunity to express our gratitude to our investors and wish that the Year of the Rate bring us all vitality, good health and great prosperity!

**Index figures are dividend reinvested.*

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