in Yuan Capital All China Strategy – Third Quarter 2019

Market Update

Shanghai Composite Index was down 2.47% in the third quarter of 2019 while Hang Seng China Enterprise Index was down 6.26% during the period. Economy data showed mixed signs in the third quarter. The Producer Price Index (PPI) dropped 0.5 percentage point from -0.3% in July to -0.8% in August. The Consumer Price Index (CPI) remained stable at 2.8 from July to August. The official manufacturing Purchasing Managers' Index (PMI) rose slightly from 49.7 in July to 49.8 in September 2019, which was still below the threshold of expansion/contraction, primarily dragged by new orders. However, the official Non-Manufacturing PMI remained stable at 53.7 from July to September.

The protest in Hong Kong accelerated in scale in August. The situation is quite complicated, and we do not expect a once for all solution to be found in the short-term. In the meanwhile, we believe that the central government of China is taking a hands-off attitude and working behind the scene is the right way to deal with the situation. The protest has damaged Hong Kong's economy for the time being, but we do not expect that it will materially affect the economy of mainland China.

MSCI raised weighting for Chinese A-shares from 10% to 15% in August. In September, net foreign capital inflow from Hong Kong Exchange through stock connect program with the Shanghai and Shenzhen stock exchanges accelerated and reached RMB45.9 billion, accounting for 27% of foreign capital inflow in 2019. Earlier this month, two investment quota restrictions for foreign institutional investors were removed to better facilitate participation in the financial markets. We expect these measures will continuously bring more capital into Chinese A-shares.

China central bank cut the reserve requirement ratio for financial institutions by 50 basis points in September. The reduction released about RMB900 billion into the market, effectively increasing the funds to support the real economy. In addition, it will reduce the cost of bank funds and will further reduce the real interest rate of loans. Both are conducive to supporting the real economic development.

Performance Attribution

At the stock level, a camera module supplier outperformed in the third quarter. Major upgrades of Huawei Mate 30 series and iPhone 11 series have focused on the camera, which illustrated the importance of optics upgrades. As a key supplier, it keeps benefiting from the optical upgrades on smartphone and the development of Internet of Things. We take the company as an optics company instead of an electronic components assembler and its growth will be driven by the increasing demand for optics upgrades.

A medical instrument company underperformed in the third quarter due to oxygenator segment was a little below market expectation in the semi-annual report. However, this was a short-term disturbance by downstream inventory fluctuation. As a high-value healthcare equipment manufacturer focused on household OTC (Over-the-Counter) market, the company continues to take market share from global leaders such as Phillips and OMROM. From a long-term point of view, it will benefit from aging population and consumption upgrade trend in China by having a full product portfolio and good quality-to-price products.

Environment, Social and Governance (ESG) Investing

– ESG Practices in Bin Yuan

We are pleased to announce that Bin Yuan Capital has recently been approved by Principles for Responsible Investments (UNPRI), the world's leading proponent of responsible investment. Inherited from our prior working history with one of the largest US corporate pension institutions, environmental, social and governance (ESG) factors are embedded in our mindset. Since our starting date in 2012, we have integrated these ESG factors into a systematic ESG rating system, which is part of our stock selection process. The registration with UNPRI is a recognition of our efforts from a reputable organization.

What We Do More Than Ticking the Boxes?

There are several ESG rating services available for Chinese companies, based on common accepted global standards, but we believe these are not sufficient for assessing companies operating in such a different economic and social environment as that we see in China. ESG is a very fresh concept in China and the stock market regulator is recently buying into the belief that ESG awareness should enhance a company's long term value to shareholders. The regulator is beginning to develop an ESG framework following global standards. ESG is new to most Chinese companies, especially A share listed firms. They either do not know much about ESG or how to generate reports that include ESG. As a result, the current available ESG ratings may not necessarily reflect the real ESG conditions of the companies. To give a closer to reality score, more research including on-the-ground investigation and engagement with firms is needed instead of just relying on public available information.

1. *On-the-ground investigation*

Our ESG rating system is incorporated within our fundamental company research and extensive due diligence/on company site meetings with different levels of staff in companies. We will verify the information we have collected from different sources and interview stakeholders on the reputation of the companies.

Governance risks are normally beneath the surface. The governance rating in our ESG scoring system consists of over 20 factors including Board Diversity, Ownership & Control, Conflict of Interest, Business Ethics and all other governance-related factors. We have kept a record of companies' governance history in our risk file, which tracks companies' management stability, insider trading, dividend ratio, financial risk exposure, disclosure and other factors that would impact our ESG rating. We go beyond the company's financial reporting and dig into the local practice of management actions including pledged shares, exchangeable bonds, inappropriate merger and acquisitions…etc. to assess the real substance of the governance.

Bin Yuan will not invest in those companies that have a low ESG rating, and on-the-ground due diligence has helped to steer us away from investing in low corporate governance companies. For example, in early 2018, we had an interest in a physical examination company because it was in a strong growth industry with large market potential. After we visited more than twenty of their physical examination clinics and interviewed with the staff on site, we found that the company paid no attention to service quality. To save costs, the firm didn't hire enough qualified doctors, but employed many non-qualified staff to do health check-ups. The clinics generated unreliable check-up reports as a result of flaws in their checking process. We believe the company has business ethics issues and we decided not to invest in it. Later in July 2018, media reported the scandal of their unqualified doctors, and the share price of this company has fallen by more than 40% since then.

By contrast, there are some high-quality Chinese listed companies that have stronger awareness of corporate governance. A tissue company that we have researched for more than five years and held for the past 2 years has a relatively high governance standard. The company has transformed from a family-run business to a professionally managed company. When it tried to acquire a company last year, the owner from the targeted company wanted to talk to the tissue company's chairman directly since they were friends. However, the chairman insisted on a formal negotiation with the acquisition department to make sure the acquisition was in full compliance. The professional management team rejected the deal based on the unsatisfactory results of the due diligence, which became the final decision of the company. The share price of this company has outperformed the market by 35% in the past 2 years since we invested.

Environmental and Social issues are important factors that we will investigate while we do on site company due diligences.

Carbon Emission and Waste Emission are the major Environmental problems and ***Labor Management and Health Safety*** are the major Social problems for Chinese companies.

Bin Yuan is highly aware of climate change matters and we only focus on carbon emission efficient industries. When we conduct on-site visits to factories, we observe the energy saving practices of the companies, including limiting air-conditioning temperatures, shifting to clean energy, and moving to third-party certified energy-saving office buildings…etc.

We pay attention to industrial waste treatment with our own eyes combined with analyzing company provided data and interviewing with the neighborhood. We also speak to different level employees in a company to understand whether workers have reasonable working hours and are provided with protective clothing. For example, we visited the above-mentioned tissue company's factories, which had a potential exposure to water pollution risk due to the nature of the tissue industry. The company invested in high quality waste treatment equipment and set up a real-time notice board to monitor sewage quality. The real time sewage quality data is displayed for public monitoring. The tissue factory also has set strict standards on health and safety protection of employees. There were eye-catching safety awareness signs all over the factory. At the entrance of each workshop, the factory also provided safety helmet, reflective vest, masks, earplugs and other protective equipment. Anyone who entered the workshop was required to wear protective equipment to ensure health and safety protection.

2. Engagement

We have an ESG engagement system to reinforce the ESG rating process. Engagement is integrated with our ESG work and is the interaction between us and companies. Since ESG is new to China, it becomes a part of our job to engage with the management to provide our opinion and advice, share best practices and make sure the companies are improving. After the communication, we will track the actions of the company and re-rate the ESG factors from the management dimension based on their progress.

We shared the ESG opinion with a security-camera company and a tissue company 2 years ago, for example, and suggested them to publish standalone ESG reports. These two firms took our advice and issued their ESG report in 2018. We are trying to help more companies to realize the importance of ESG reporting and make their ESG reports closer to global standards.

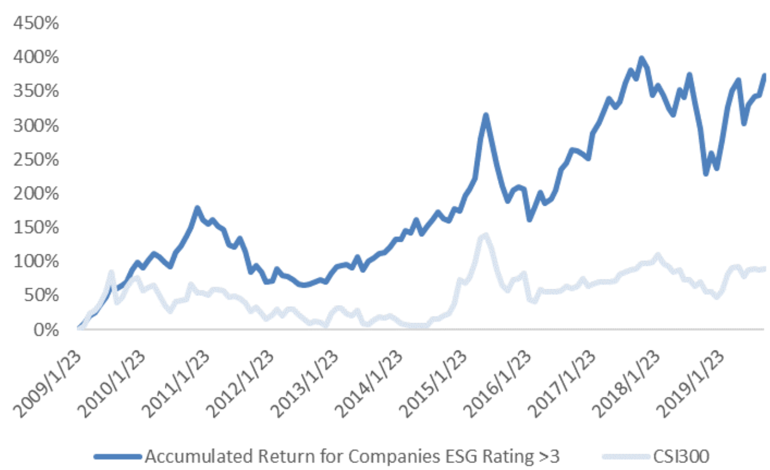
Besides our ESG reports, we give recommendations to companies on their products based on the ESG guidance. We communicated with a beverage company about developing healthy product lines, and they have developed several sugar-free drinks since then.

We believe that a company which is not sensitive to ESG management has high long-term business risks. After learning about the scandal of GP Certified Public Accountants' unreliable audit on Kangmei Pharmaceutical, we proposed to one furniture company to discontinue using GP as its auditor in order to improve the quality of their future financial reports. The company quickly accepted our suggestion and expressed that they would complete the corresponding replacement work before the preparation of 2019 annual report.

China ESG Is Improving

With continued education and engagement, ESG awareness of Chinese companies has raised gradually over the past years. Government measures, including strict environmental policies have helped fuel the improvements. However, corporate ESG reporting quality is still lagging. Chinese security regulators have started to play a role to promote Responsible Investment and enhance reporting quality. They encourage listed companies to disclose their ESG practices including issuing independent ESG reports. The regulators have also collected the Responsible Investment framework from institutional investors like us to further understand the best practices. Those initiatives will help narrow the reporting quality gap between China and global standard, and foster an open and transparent environment to lead Chinese companies to focus on ESG factors. In spite of those, it will take some time for Chinese ESG reporting to fully reflect the real practices of the companies. The lagging reporting quality will still be one of the inefficiencies that a fund manager can take advantage of. Through on-the-ground research and engagement with companies, we can possess earlier and better understanding of the companies' culture and execution in terms of ESG. In our past experiences, high ESG rating companies (ESG rating > 3 in our system) outperformed benchmark by almost 300% (Chart 1) in the past 11 years.

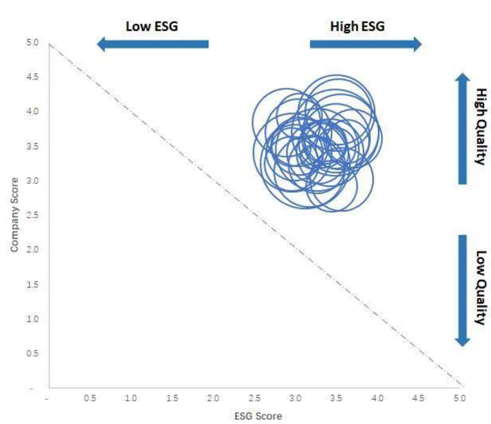
Chart 1: High ESG Rating Companies Accumulative Returns



Source: Wind, Bin Yuan Capital

Our portfolio only focuses on stocks with good ESG ratings (Chart 2), which we believe could grant us long term sustainable returns.

Chart 2: Portfolio ESG Bubble Chart



Note: The size of Bubbles represents the size of stock weightings

Source: Bin Yuan Capital

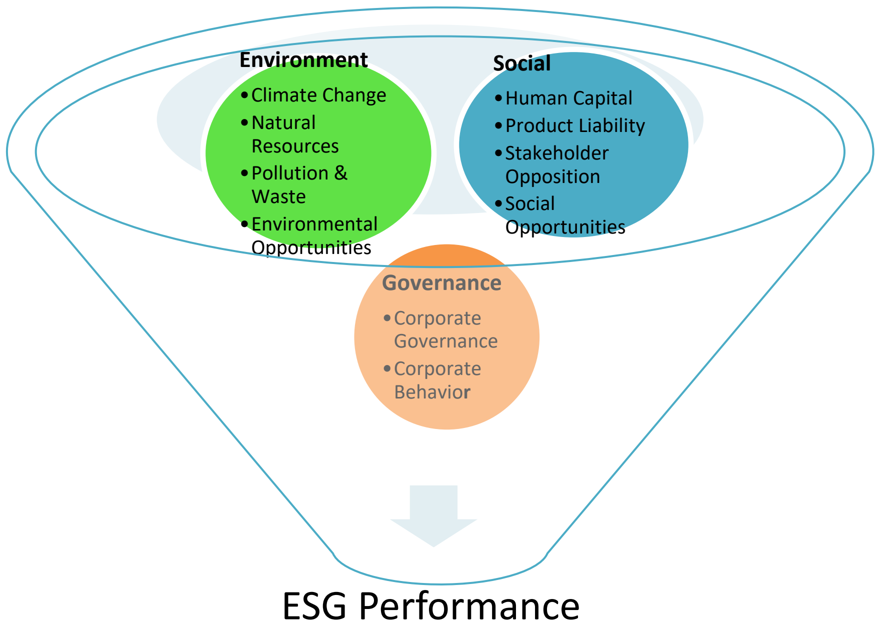
Appendix - Bin Yuan ESG Framework

It is our belief that Responsible Investment (RI) could bring superior return and benefits to our society and people in the long run. We promote the culture of Responsible Investment in the whole organization to make sure all the staff in Bin Yuan share the same values of building a long-term responsible investment firm and investing in responsible companies that contributing to build a better world. Beyond seeking profit only, the purposes of corporates should also include the responsibility for society and stakeholders. It is very important that companies pursue long term SUSTAINABILITY of economic interest to their shareholders by incorporating social responsibilities.

ESG approach is well incorporated in Bin Yuan's risk management framework and investment process. We believe poor ESG is a key business risk factor. At the screening stage, we will eliminate the companies that are not ESG compliant or qualified. The whole process is managed by our in-house team and we have accumulated many years of practical experience.

ESG factors have a long-term nature and are often difficult to quantify. Bin Yuan has established an in-house rating system to quantify the qualitative elements of ESG risks the companies are exposed to and how the companies manage them. We rate those factors in two categories, namely Exposure and Management. Exposure refers to how exposed a company is to those risk factors and issues. Management refers to how company is managing those issues. Exposure is scored on a 1-5 scale, with 5 representing no exposure and 1 representing very high exposure. Management is also scored on 1-5 scale, with 5 representing the best practice management and 1 representing poorest practice management. A company with high exposure must have strong management to minimize the risk. We pay special attention to those low rating factors. We will avoid the companies in a high exposure industry with low management rating. ESG factors considered by the Bin Yuan Capital are listed in Chart 3:

Chart 3: Bin Yuan ESG Framework

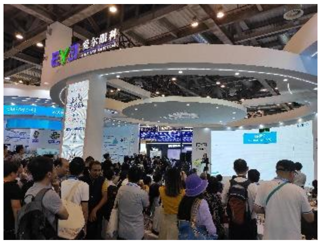


Source: Bin Yuan Capital

We constantly review the ESG factors of companies we invest in to make sure they are on track as responsible companies pursuing long-term sustainability. If a portfolio holding company does not fully satisfy ESG standards, we will engage with the management to help them to make improvements. We will sell a holding if the company breaches ESG standards and the management have no willingness to change and improve. Negative examples in the market are discussed within the team as a lesson learnt to avoid the risk in the future.

As for Bin Yuan operations internally, we believe the Responsible Investment culture and its values are most important to our firm. We integrate the Bin Yuan Value into our staff annual appraisal process. Employee buy into our culture of Responsible Investment and the performance of implementing ESG are key elements considered in the annual reviews and promotions. A 40% weight of the staff annual bonus is linked to the team portion (referring to teamwork and leadership performance in Bin Yuan Sustainable and Responsible culture). If the performance linked to ESG objectives is not satisfactory, we will not retain those staff in the firm.

Bin Yuan on the Road



September 6, 2019

We visited Aier Eye Hospital's (a private hospital chain) booth in an ophthalmology exhibition held in Shanghai.

- With the rapid development of computer, network technology and smart phones, the excessive use of eyes resulted in a continuous increase in the incidence of various eye diseases. The protection and treatment of ophthalmic diseases is attracting more and more attention.

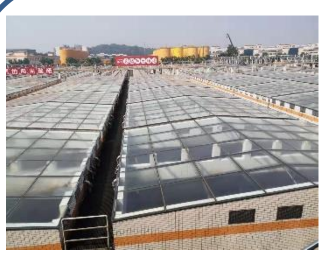
"The nearsightedness rate of Chinese college students has reached 90%." *– An ophthalmology doctor.*

September 28, 2019

We observed that visitors can use Alipay (a third-party payment tool) in most major cities and tourist attractions in Japan.

- Alipay is actively expanding its oversea business. It is now widely accepted in Japan.

"By using Alipay, you do not need much Japanese yen any more. Shopping is as convenient as in China." – A tourist.



September 25, 2019

We visited Haitian's (a seasoning company) factory in Foshan City, Guangdong Province.

- Haitian is the No. 1 soy sauce brand in China with a production capacity of around 2 million tons per year. The company is well managed and has high standards in its quality control process. With the consumption upgrade trend, Haitian will continue to increase its market share through consolidation as people care more for quality products.

"This is the largest soy sauce production factory in China, and we are expanding production capacity to support future sales." – Ms. Zhang, investor relations.

Bin Yuan on the Road (Continued)

July 12, 2019

We visited C&S Paper's (a household tissue manufacturer) factory in Chengdu City, Sichuan Province.

- The factory increased its health & safety management by posting health hazard notification cards at the entrance of each warehouse, followed by standardized health protection procedures and equipment.

"The well-being of employees is always a top concern of C&S Paper." – Board Secretary Mr. Zhou

August 27, 2019

Shanghai welcomed Costco's first store in China. Moutai (a Chinese Baijiu company), sold at the guidance price (RMB1,499/bottle), was one of the most popular products.

- Moutai was sold out in an hour after the store opened and every customer could only buy two bottles.

"It is hard to buy Moutai at RMB1,499." – A customer.

Sincerely,

Bin Yuan Capital

Specialized China Manager

- Shanghai/Hong Kong-based, value focused China manager
- Long only absolute return mindset
- $600M+ AUM invested in All China and China A share strategies

Experienced Team

- Founders with 35+ years combined investment experience
- Core team formerly with GE Asset Management ("GEAM") managing $5B across 3 funds; EM, Greater China & China A Shares

Fund Fee Structure

- Class A – Management Fee 1.5%
- Class B – Management Fee 1%, Performance Fee 10%
- Class C – Management Fee 2%, Performance Fee 20%

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