Signatory of:

PRI Principles for Responsible Investment

Bin Yuan Capital All China Strategy – November 2019

Market Update

Shanghai Composite Index was down 1.95% and Hang Seng China Enterprise Index was down 2.20% in November.

The economy data remained weak in November while signs of recovery can be observed. Consumers and services continued to deliver better performance than manufacturing segments. The Producer Price Index (PPI) was -1.4% in November, up from -1.6% in October 2019, but lower than -1.2% in September. The official manufacturing Purchasing Managers' Index (PMI) was up from 49.3 in October to 50.2 in November, which was above the threshold of expansion/contraction, helped by the recovery of imports, production and new orders. The official Non-Manufacturing PMI increased from 52.8 in October to 54.4 in November. The Consumer Price Index (CPI) was 4.5% in November, up from 3.8% in October and 3.0% in September, in which 2.64% was contributed by the increase of pork price due to the outbreaks of African swine fever in China. Rail cargo volume increased 9.0% YoY in October to 387 million tons.

A new guideline was released to promote high-quality development of trade. One of the key targets is to further expand imports, which will improve the domestic consumption and make up for the shortage of resources and lower the price of some products, such as pork. The guideline also stressed the need to speed up the development of modern services, especially production-related services. China will gradually transform from processing and manufacturing to research and development, marketing services and brand management to generate more economic value along the value chain.

Two hundred and four Chinese A shares, including 189 mid-cap stocks, were added to the MSCI China index in November. MSCI also increased the weighting of 268 existing Chinese A shares constituents from 15% to 20% as previously planned, effective on November 26. The A shares weight increase will arouse more foreign capital into the Chinese market and the first-time inclusion of mid-cap A shares will draw attention of international investors on those smaller but faster growing high quality companies, which benefit our mid-cap focused portfolio in the long term.

Performance Attribution

At the stock level, an e-commerce company outperformed in November. The company received much attention in November due to a satisfying third quarter financial result and its dual-listing on the Hong Kong exchange. The scale and profitability of its marketplace business continued to rise, leveraging its rich user pool of Alipay. Loss of entertainment segment is reduced as planned earlier this year. We believe the company will maintain its leadership in China's online and offline retail industry and its cloud and fintech business will gradually become a major profit contributor in the future.

A medical instrument manufacturer underperformed in November due to its sales of oxygenator segment was a little below market expectation. However, this was due to active downstream distributors' destocking to prepare for the release of new products. Meanwhile, the company is changing its offline business strategy to better facilitate the future growth. As a high-value healthcare equipment manufacturer focusing 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.

Local Observation and Portfolio Positioning

Bin Yuan has organized the second investors trip successfully in November and led a group of foreign investors to visit portfolio holding or potential holding companies in first through fourth-tier cities, located in the east, central and south of China. We covered over 2,000 kilometers via minibus and bullet train travelling between Shanghai, Danyang, Wuhan, Zhuzhou, Changsha and Guangzhou. This trip was a great opportunity for the investors to experience the highly efficient modern infrastructures in China and it was very informative to do onsite visits, which include factories, R&D centers, stores and face-to-face communication with the local management team.

Same as last year, the investors were all impressed by China's infrastructure, including huge modern airports, gigantic railway stations, a good motorway system, and the biggest high-speed rail network in the world. All of them are busy and crowded with massive travelers. "The trains are huge, and I counted the time the train (From Wuhan to Changsha) took to roll into the station. It was 45 seconds. And there were too many carriages to count", said one of our investors. According to the management of CRRC Times Electric, who is the leading manufacturer of electrical components & systems for parent company CRRC, the network of high-speed train lines will further grow from 30,000 km to 40,000 km by 2025. This will continue to increase mobility for the smaller cities and rural areas, which will aid continuous urbanization and consumption upgrade in the country.

Picture 1: Wuhan Railway Station – one of three in Wuhan

Although the economy slowed down a little bit from topline news, the consumption upgrade story is intact to our investors and is shifting from physical goods to services. We introduced two new economy companies to the investors, namely PDD and Meituan Dianping. PDD is an innovative social E-commerce platform whose unique discount team purchase model and proposition in the value for money segment drove its fast growth since its establishment in 2015. While Meituan Dianping is a promising star which integrated features of Apps like Uber, Groupon, GrubHub, Tripadvisor, Booking.com, Airbnb and Yelp, etc. We let our investors experience the mobile ordering by scanning Meituan's QR code attached on the table in a bar in Changsha, Hunan Province. The investors were all impressed by the efficiency brought by the development of internet in China.

During the trip, besides those companies, we also visited a high-tech development zone, Wuhan Optics Valley, with an area of 518 square kilometers. It has developed with 56 research institutes, 42 universities and colleges, around 800,000 students, and well-funded incubator programs. The technology park has been designated as the Opto technology center, biological technology center for China and national base for Memory chips. There are currently around 100,000 enterprises in the technology park growing by 20,000 per year. To our investors' surprise, such a R&D center is not based in eastern or southern China, which are traditional developed areas, but in Wuhan, a tier 2 city in central China. SF Express is building a new freight airport near Wuhan - which is within two hours flying time of a billion people. The new airport is due for completion in 2021 with projected annual capacity of 5 million tons. When completed it is likely to become one of the busiest express hubs in the world. These factors have encouraged private companies to establish R&D centers and manufacturing bases in the Wuhan Optics Valley.

Here are some key takeaways during the trip to share with you all.

- Consumption Upgrade

With a population of 1.4 billion, China can be divided into three layers according to income level. The first layer group has more than 300 million population that reside in large cities (tier 1 and tier 2) with a disposable income per capita of over USD7 thousand. The second layer group is close to 550 million in median and small cities (tier 3 and below) with a disposable income per capita of USD5 thousand. The rest layer three with more than 550 million people still reside in countryside. Households consumption habits in layer one is benchmarking those in developed countries while in lower-tier cities, people target the larger cities living standards as their goal. This upgrading cycle will continue for many years.

Some of those companies we visited during this trip will continue to benefit from this trend.

- C&S Paper (002511.SZ, a household tissue manufacturer, revenue around RMB6 billion a year, portfolio holding): Chinese household tissue consumption volume per capita is only 1/3 of developed countries. With the increase of the disposable income, Chinese household tissue consumption grows at approximately 10% every year. Meanwhile people care more about tissue qualities and tend to choose brand products over non-brand low-quality products. As environmental regulations is getting stricter in China, small household tissue factories are being shut down and the industry will continue to consolidate. C&S also keeps launching new products such as mother-and-baby tissues, wet wipes and sanitary napkins, which can create synergy with its current product portfolio by sharing brands, channels, etc.

- Oppein (603833.SH, a customized furniture manufacturer, revenue around RMB12 billion a year, portfolio holding): Oppein has the most diversified customized products that cover kitchen cabinets, wardrobes, bathroom products and wooden doors, creating a one-stop shopping experience for customers. Its distributors are also the best among peers. By cooperating with local decoration companies, Oppein developed the new whole-room decoration (total solution) business, which increased the ticket prices. Total solution can be perceived as consumer trading up as it saves people time and energy by increasing efficiencies, which is beneficial for industry leaders to consolidate.

- AIER Eye Hospital (300015.SZ, a health care service provider, revenue around RMB10 billion a year, portfolio holding): Through 16 years of development, AIER currently has above 200 ophthalmic hospitals which covered major provinces and cities in China. Through the company's systematic management process and effective employee incentive system, AIER continuously accumulated brand reputation and obtained market share from public hospitals. We believe that considering China's huge population base and low penetration rate of myopia surgery, which is still less than 1% and much lower than in developed countries, the company will continue to benefit from the industry growth trend in the long term.

- YONGDA AUTO (3669.HK, an auto dealer service provider, revenue around RMB62 billion a year, portfolio holding): Yongda Automobile is a leading automobile dealer group in China who focuses on luxury car sales. With the trend of consumption upgrade, increasing numbers of consumers choose luxury cars which have higher brand awareness and better quality. In addition to the new car sales, with the continuous growth of ownership of vehicles, after-sales business which contributed 60% of the profits will become a more stable and sustainable growth of the company.

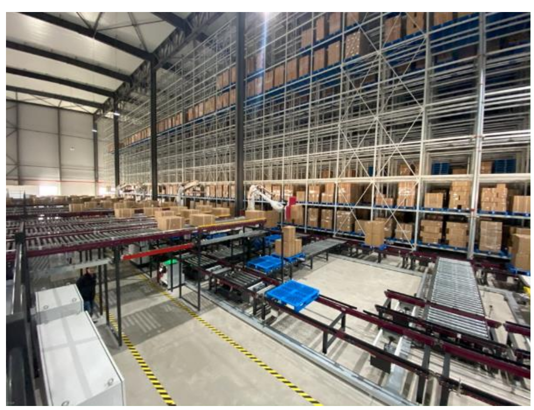
- Bilibili (BILI.O, a full-spectrum online community, revenue around RMB6.6 billion a year, portfolio holding): With the consumption upgrade shifting from physical goods to services, people's demand for content and entertainment increases dramatically. As a favorite content platform for young people, the average age of Bilibili's users is only 21.5 years old. They spend 85 minutes a day watching their favorite content on Bilibili. The company has been established for ten years, and the platform has rich content barriers and diverse monetization methods, such as games, advertisements, e-commerce and so on. As the Chinese version of Youtube, we believe that Bilibili has a large potential.

- <u>Technology Upgrade</u>

With China's moving-up along the global value chain, the demand for advanced technology is growing rapidly. Trade issues have also accelerated the progress of import substitution and have strengthened resolve within China to go their own way. Several companies we visited benefit from this trend. In addition, there is now a Reverse Brain Drain: 80% of those who study overseas return to China. This is helping provide talent as companies expand and upgrade.

- Yuyue (002223.SZ, a medical equipment supplier, revenue around RMB5 billion a year, portfolio holding): We visited Yuyue again after one year and our investors were the first batch of foreign visitors to the new manufacturing and administration centre of Yuyue. The new facility is three times the size of the old one and covers 0.7 square kilometers. Compared to the factory we visited last year, the new one is significantly more automated with a very impressive automated warehouse. Advanced automated production lines will help the company increase the production efficiency in the future to continually provide good quality-to-price products. In addition to that, Yuyue also aims to further improve its R&D capabilities to expand into higher value-added product categories.

Picture 2: Yuyue production warehouse



- CRRC Times Electric (3898.HK, an electric system provider, revenue around RMB15 billion a year, not in portfolio): CRRC Times Electric is a leading manufacturer of automotive electrical systems in the rolling stock industry, with a market share of 50% in China. In addition to sophisticated electronic system products, the company is trying to move-up along the value chain to address the IGBT product, which is the most important part in company's products. With the rising proportion of self-supply, the company can save a lot of costs. Meanwhile, company is trying to address external IGBT markets, like grid state, electric vehicle, etc. Although the company is not in our portfolio, it shows the development path of some of the manufacturing companies in China, from simple assembly to manufacture key components and further to make breakthrough in most advanced technologies.

  Picture 3: CRRC Times Electric IGBT exhibition hall

- WuXi Biologics (2269.HK, a leading Contract Research Organization (CRO), revenue around RMB2.5 billion a year, not in portfolio): China has seen a spectacular biotech boom in recent years. WuXi Biologics, the leading biological CRO in China, is the beneficiary of this trend. By aggressively expanding capacity, successfully attracting overseas experts and quickly catching up globally advanced technologies, WuXi Biologics has dominated the domestic market and continued taking market share from global players. Its net income is expected to continue to increase at a CAGR of 32% in the next three years. Although the company is not in our portfolio, it proves that China is also catching up in pharmaceutical R&D by leveraging the engineer dividend.

Bin Yuan on the Road

November 20, 2019

We visited Yuyue's (a household healthcare equipment manufacturer) research center in Nanjing City, Jiangsu province and met Yuyue's board chairman and CEO.

- Yuyue is a household equipment platform company with over 1,000 SKUs, and will continue to invest on R&D to launch high quality and high end products.

"Yuyue spent around 4% of revenue on R&D in 2018 and plan to increase R&D expense in the next few years to enhance competitiveness." *– Mr. Wu, CEO of Yuyue.*

November 5, 2019

We saw a Midea (a household appliance manufacturer) store on the streets of Abu Dhabi.

- Midea has 15 production centers and 33,000 employees overseas, and its business covers more than 200 countries. In 2018, the overseas revenue of Midea reached RMB110 billion, accounting for more than 40% of its total revenue. The company is gradually changing from a domestic leader to a global household appliance giant.

"Midea air-conditioner is cheap but with good quality." – A sales assistant in the store.

November 30, 2019

We participated the Investor Communication Day held by OVC TEK (a contact lens manufacturer) in Hefei, Anhui Province.

- After visiting OVE TEK, an upstream supplier of AIER's optometry business, we find that competition of upstream enterprises is increasing with more suppliers entering the market. We believe that AIER will benefit from the trend of more diversified suppliers.

"Myopia prevention and control has become very important and more and more patients will seek treatment." – CEO of OVC TEK Mr. TAO.

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%

Disclaimer

The information, materials and whatsoever releases, views or opinions (together the "Information") contained herein are strictly for information and general circulation only and do not have regard to the specific objectives, financial situation and particular needs of any specific person. The Information does not constitute either an offer to sell or a solicitation of an offer to buy any interest in any fund and strategy associated with Bin Yuan Capital.

The information contained herein is subject to revision and completion. The historical performance information included herein may not be indicative of the performance of future results. Nothing contained herein should be relied upon by prospective investors as a promise or representation as to the future performance.

Bin Yuan Capital shall not be liable or responsible to you or any other party for any direct, indirect, consequential or incidental damages, losses, expenses or costs whatsoever arising in connection with your access to this newsletter, or reliance on any Information, regardless of the form of action.

Copyright and Trademark