Wellington All-China Focus Equity Fund

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MARKET REVIEW

In July, global equities advanced as markets navigated the implications of divergent monetary policies across major economies. Gains in the U.S. stock market were supported by growing expectations that the Federal Reserve would start to cut interest rates as early as September, a view strengthened by a weaker-than-expected CPI print. Asian economies outperformed broader emerging markets, with Japan and India being the better-performing markets on a relative basis, while Taiwan and China lagged.

Chinese equities declined in July as sentiment remained poor. Second-quarter GDP growth and consumer sentiment remained weak, the absence of anticipated economic stimulus measures at the nation's Third Plenary Session, heightened geopolitical tensions, and a weakening yuan contributed to risk aversion. The Third Plenary Session concluded without any significant catalysts and instead emphasized a governance framework that called for political and social discipline, national security, and industrial policy. This focus on industry, investment, and supply is expected to come at the expense of services, consumption, and demand. Additionally, the Biden administration's consideration of curbing Chinese access to cutting-edge chip technology further dampened the market.

The MSCI China All Shares Net returned -0.7% for the period. Within the index, eight out of 11 sectors declined over the month. Energy and materials were the bottom performing sectors, while financials and health care were the top performing sectors for the period.

FUND PERFORMANCE AND ATTRIBUTION

- The fund modestly underperformed the index for the month.
- Security selection was the primary driver of relative underperformance. Weak selection in communication services and health care was partially offset by selection in consumer staples, information technology and financials. Sector allocation, a result of our bottom-up stock selection process, was neutral to returns. Allocation effect was driven by our lack of exposure to materials and underweight to energy, but offset by our overweight to communication services and utilities and underweight to financials.
- At the issuer level, our top two relative contributors were overweights to China Pacific Insurance and PICC Property & Casualty, while our top two relative detractors were overweights to Kanzhun and Fuyao Glass Industry.
- The share price of China Pacific Insurance, an integrated insurer, rose in July. The company is investing in new growth areas and is well positioned to provide services to the aging population. Shares of Kanzhun, a provider of online recruitment services, declined during the period. The company reported a lower second quarter outlook due to a weaker-than-expected macro environment.

FUND POSITIONING AND OUTLOOK

In the near term, we expect market volatility to persist amid deflationary pressure, the new US tariff hike and continued liquidity concerns in the debt-laden Chinese property sector. However, as long-term investor, we continue to remain a cautiously optimistic view on Chinese equities as policy executions accelerate with prudent monetary and proactive fiscal support, further relaxation for the property market and a renewed focus on economic growth. More recently, the central bank cut its medium-term lending facility (MLF) by 20 basis points to 2.3%, its first reduction since August 2023. The string of rate cuts pointed to government's growing urgency to support growth after China's GDP undershot expectations in the second quarter. Beyond macro policy, company earnings revisions and capital allocation are another critical factor to watch, as they will reveal unique opportunities for businesses that can thrive even as the broader economy slows down. Moving forward, we continue to focus on identifying companies with strong organic growth prospects, sustainable higher returns on capital and good corporate governance.

At the end of the period, our largest exposures were communication services and consumer discretionary and we were least exposed to real estate and energy. We had no exposure to materials.

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PAST PERFORMANCE DOES NOT PREDICT FUTURE RETURNS. AN INVESTMENT CAN LOSE VALUE.

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