Henderson

Horizon Fund

Henderson GLOBAL INVESTORS

Henderson Horizon Fund – China Fund

Fund Commentary – July 2015

Overview

Chinese equity markets fell precipitously at the start and the end of July as panicking retail investors sold off shares in the mainland A share markets in Shanghai and Shenzhen. Such was the ferocity of the one-day falls that many companies asked the exchanges to suspend trading in their shares, and the government felt compelled to step in to support the A share market. The panic spread to Chinese shares listed in Hong Kong, where most of the fund is invested and where valuations are much cheaper. As we have flagged all year, the economy remains weak with the purchasing managers' index (PMI) survey of manufacturing showing a weaker than expected reading in July and, as a result, all eyes are keenly watching to detect whether the stock market shake-out has any effects on the real economy.

Performance and activity

In July the fund fell 7.8% compared to the benchmark's return of -10.8%. A range of stocks helped our relative performance; on the long side the fund benefited from positions in insurer AIA Group, tissue brand Vinda (where profits are growing faster than expected), property stocks China Vanke and Cheung Kong Property, and our recently added position in Macau casino operator Sands China. Our underweight in Chinese banks also helped returns as they sold off dramatically. Short positions in energy drilling company China Oilfield Services, nuclear power producer CGN Energy and polysilicon producer GCL Poly helped returns. Having taken strong profits in Hong Kong Exchanges in June we entered a short position in the stock in July, which also helped returns when the market and the stock fell. Detractors included automobile shares Chongqing Changan Auto and Brilliance China, which are falling with slower industry sales but which we think represent attractive value at current levels. PC and smartphone brand Lenovo also sold off as technology shares weakened globally.

Outlook

Chinese equity markets have just suffered from a bout of panic selling and outflows, so it is logical when these stop to expect some sort of relief bounce. Given it is now August, which is traditionally a period of low trading volumes, share prices and market moves may be amplified and so volatility may remain high. We expect the Shanghai market to provide constant ammunition for headline writers in coming months, much of it negative. The government clearly wants to support the A shares markets, but for foreigners the intervention at such high valuation levels and the large number of shares trading suspensions means it has become less investible over the longer term; consequently, we have been dialling down our exposure to A shares in the fund. The Hong Kong and US listings of Chinese shares offer much better value. In Hong Kong we saw a significant step up in management buying company shares in the correction, which is a bullish signal, and in the US we continue to see privatisations and takeovers being announced: YY Inc is around 3% of the fund and received a privatisation offer in July and we continue to add to this part of the portfolio. We have been wary of the weak macroeconomic data for months, so the current slowdown is no surprise to us, but we will be watching the data very closely for any economic impact from the market correction. We expect the stock market weakness to further boost demand for physical property, so housing market strength may catch many investors off guard. It is also possible that growth has slowed sufficiently – the July manufacturing PMI reading was notably weak – that the authorities implement some growth boosting measures, probably funded by policy banks in coming weeks.

Our strategy to invest in the most financially strong, cash generative, well-managed businesses is still appropriate, and even though the macro looks poor and investors are panicking we remain very comfortable with our growth-orientated portfolio.

Note: Reference to any specific company or stock is for information purposes only and should not be construed as a recommendation to buy or sell the same.

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Important information

Henderson Global Investors (Singapore) Limited Company Registration No. 199700782N
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