

# First Sentier Asian Bridge Fund

## Explanatory Memorandum

19 November 2021



**First Sentier**  
Investors

## IMPORTANT INFORMATION FOR INVESTORS

**IMPORTANT - If you are in any doubt about the contents of this Explanatory Memorandum or the Product Key Facts Statement, you should seek independent professional financial advice.**

This Explanatory Memorandum and the Product Key Facts Statement comprise information relating to First Sentier Investors Umbrella Funds (the “**Trust**”), an umbrella unit trust established under Hong Kong law by a trust deed dated 10 May 2001 (as amended and supplemented from time to time) between First Sentier Investors (Hong Kong) Limited as manager (the “**Manager**”) and HSBC Institutional Trust Services (Asia) Limited as trustee (the “**Trustee**”), and its Sub-Fund, the First Sentier Asian Bridge Fund (the “**Fund**”).

The Manager accepts full responsibility for the information contained in this Explanatory Memorandum and the Product Key Facts Statement as being accurate at the date of publication and confirms, having made all reasonable enquiries, that to the best of its knowledge and belief there are no other facts the omission of which would make any statement in this Explanatory Memorandum or the Product Key Facts Statement misleading as at the date of publication. However, neither the delivery of this Explanatory Memorandum and the Product Key Facts Statement nor the offer or issue of Units in the Trust shall under any circumstances constitute a representation that the information contained in this Explanatory Memorandum or the Product Key Facts Statement is correct as of any time subsequent to such date. This Explanatory Memorandum and the Product Key Facts Statement may from time to time be updated.

Units are offered on the basis only of the information contained in this Explanatory Memorandum and the Product Key Facts Statement (as amended or supplemented from time to time). Any information given or representations made by any dealer, salesman or other person and (in either case) not contained in this Explanatory Memorandum or the Product Key Facts Statement (as amended or supplemented from time to time) should be regarded as unauthorised and accordingly must not be relied upon.

The Trust and the Fund have been authorised by the SFC pursuant to section 104 of the Securities and Futures Ordinance. SFC authorisation is not a recommendation or endorsement of the Trust or the Fund nor does it guarantee the commercial merits of the Trust or the Fund or their performance. It does not mean the Trust or the Fund is suitable for all investors nor is it an endorsement of their suitability for any particular investor or class of investors.

No action has been taken to permit an offering of Units or the distribution of this Explanatory Memorandum or the Product Key Facts Statement in any jurisdiction other than Hong Kong where action would be required for such purposes. Accordingly, the Explanatory Memorandum and the Product Key Facts Statement may not be used for the purpose of an offer or solicitation in any jurisdiction or in any circumstances in which such offer or solicitation is not authorised. Distribution of this Explanatory Memorandum and the Product Key Facts Statement must be accompanied by a copy of the latest available audited annual report of the Fund and any subsequent interim report.

### Restrictions and compulsory transfer and redemption

The Manager may from time to time impose such restrictions as it may think necessary for the purpose of ensuring that no Units are acquired or held by any person in the circumstances set out in the “Compulsory Redemption or Transfer of Units” section.

The Fund may compulsorily redeem the Units or interests in the Fund in the relevant circumstances.

### United States

The Units have not been and will not be registered under the US Securities Act of 1933, as amended (the “**Securities Act**”) or the securities laws of any of the states of the US, nor is such a registration contemplated. The Units may not be offered, sold or delivered directly or indirectly within the US or to, or for the account or benefit of, any US Persons (within the meaning of Regulation S under the Securities Act (“**Regulation S**”) and as defined under the section headed “Definitions” of this Explanatory Memorandum). Units are being offered to non-US persons in offshore transactions outside the United States in reliance on Regulation S. Units may not, except pursuant to a relevant exemption, be acquired or owned by, or acquired with the assets of an ERISA Plan. An ERISA Plan is defined for these purposes as (i) any employee benefit plan within the meaning of section 3(3) of the United States Employee Retirement Income Securities Act of 1974, as amended (“**ERISA**”) and subject to Title I of ERISA; or (ii) any individual retirement account or plan subject to Section 4975 of the United States Internal Revenue Code of 1986, as amended (for the purposes of this paragraph a “**plan**”); or (iii) any entity or account whose underlying assets include assets of a plan by reason of a plan’s investment in such entity or account.

Neither the Trust nor the Fund have been or will be registered under the US Investment Company Act of 1940, as amended.

Investment in Units by or on behalf of US Persons is not permitted.

The Manager has the power to impose such restrictions as it may think necessary for the purpose of ensuring that Units are not acquired or held directly or beneficially by any US Person (other than pursuant to an exemption available under US law).

For the purposes of complying with FATCA, the Fund will be required to identify whether any of the Unitholders are “specified United States persons” under the tax laws of the U.S. or are certain non-U.S. entities with one or more specified United States persons as “Controlling U.S. Persons”, and may be required to disclose information to the relevant tax authorities including the identity, value of holdings and payments made to such persons as set out under “The Foreign Account Tax Compliance Act and similar measures” in the “Taxation” section. The Fund may also be required to withhold on payments made to certain persons as set out under “Withholdings and Deductions” in the “Taxation” section.

For the purposes of the preceding paragraph, a specified United States person generally will include, subject to certain exceptions, (a) an individual who is a citizen or tax resident of the U.S., (b) a partnership or corporation (including any entity treated as a partnership or corporation for U.S. tax purposes, such as a limited liability company) organized in or under the laws of the U.S. or any State thereof (including the District of Columbia), (c) any estate the income of which is subject to U.S. tax regardless of its source, and (d) any trust if (i) a court within the U.S. is able to exercise primary supervision over the administration of the trust and (ii) one or more United States persons have the authority to control all substantial decisions of the trust.

A person’s status under US tax and securities laws can be complex and we recommend that persons unsure of their status under US law seek their own advice prior to subscribing for Units.

Some of the information in this Explanatory Memorandum is a summary of corresponding provisions in the Trust Deed. Investors should read the Trust Deed for further details and for further information which is not contained in this Explanatory Memorandum.

Potential applicants for Units should inform themselves as to (a) the possible tax consequences, (b) the legal requirements and (c) any foreign exchange restrictions or exchange control requirements which they might encounter under the laws of the countries of their incorporation, citizenship, residence or domicile and which might be relevant to the subscription, holding or disposal of Units.

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## **DIRECTORY OF PARTIES**

### **Manager**

FIRST SENTIER INVESTORS (HONG KONG) LIMITED  
Level 25  
One Exchange Square  
8 Connaught Place, Central  
Hong Kong

### **Directors of the Manager**

Michael David STAPLETON  
Lucinda Kate DOWLING  
Robert Gordon SCOTT

### **Trustee and Registrar**

HSBC INSTITUTIONAL TRUST SERVICES (ASIA) LIMITED  
1 Queen's Road Central  
Hong Kong

### **Auditors**

Deloitte Touche Tohmatsu  
35/F One Pacific Place  
88 Queensway Hong Kong

### **Legal Advisers to the Manager**

Deacons  
5th Floor, Alexandra House  
18 Chater Road  
Central  
Hong Kong

## DEFINITIONS

For the purposes of this Explanatory Memorandum, the following expressions have the following meanings:-

“Anti-Dilution Adjustment”	<p>means a percentage charge determined by the Manager that is charged:</p> <p>on a Dealing Day where the value of all subscriptions for Units exceeds the value of all redemptions of Units and which will be included in the Net Asset Value per Unit to reduce the effect of the costs incurred by the Fund in purchasing additional portfolio securities upon the subscription for Units in the Fund; or</p> <p>on a Dealing Day where the value of all redemptions of Units exceeds the value of all subscriptions for Units and which will be included in the Net Asset Value per Unit to reduce the effect of the costs incurred by the Fund in disposing of portfolio securities to meet the redemption requests.</p> <p>The charge shall not exceed in any event 2% of the value of subscription or redemption, as the case may be, and in both cases the charge shall be paid into or retained by the Fund, as the case may be, in order to discharge the typical costs of dealing in the underlying investments of the Fund, such as dealing spreads, dealing charges, fees and taxes;</p> <p>In certain jurisdictions an Anti-Dilution Adjustment is referred to as a swing pricing adjustment;</p> <p>Anti-Dilution Adjustment is further described under the headings “Issue of Units” and “Redemption of Units” below</p>
“Business Day”	<p>means a day (other than Saturday) on which banks in Hong Kong are open for normal banking business provided that where as a result of a Number 8 Typhoon Signal, Black Rainstorm warning or other similar event, the period during which banks in Hong Kong are open on any day is reduced, such day shall not be a Business Day unless the Manager and the Trustee otherwise determine</p>
“Bond Connect”	<p>means an initiative launched in July 2017 for mutual access between the Hong Kong and the PRC bond markets through a cross-border platform. Under the northbound trading of Bond Connect, eligible foreign investors can invest in the China’s Interbank Bond Market</p>
“Code”	<p>unless the context otherwise requires, means Section I - the Overarching Principles Section and Section II - Code on Unit Trusts and Mutual Funds of the SFC Handbook for Unit Trusts and Mutual Funds, or any handbook, guideline and code issued by the Commission, as may be amended from time to time</p>
“CSRC”	<p>means China Securities Regulatory Commission</p>
“Dealing Day”	<p>means each Business Day</p>
“FATCA”	<p>means the Foreign Account Tax Compliance Act of the United States, as further described in the “Taxation” section</p>
“Fund”	<p>means the First Sentier Asian Bridge Fund, a Sub-Fund of the Trust</p>
“Government and other public securities”	<p>means any investment issued by, or the payment of principal and interest on, which is guaranteed by a government, or any fixed-interest investment issued by its public or local authorities or other multilateral agencies</p>
“HK dollars” or “HK\$”	<p>means the lawful currency of Hong Kong</p>
“HSBC ITS”	<p>means HSBC Institutional Trust Services (Asia) Limited</p>
“Manager”	<p>means First Sentier Investors (Hong Kong) Limited</p>

“Net Asset Value”	means the Net Asset Value of the Fund or, as the context may require, of a Unit, calculated in accordance with the Trust Deed
“OTC”	means over-the-counter
“PBOC”	means the People’s Bank of China
“PRC”	means the People’s Republic of China, excluding Hong Kong, Macau and Taiwan for the purpose of this Explanatory Memorandum
“QFII/RQFII”	means a qualified foreign investor which has been approved by CSRC to invest in PRC securities and futures with funds (in foreign currencies and/or offshore RMB) overseas or, as the context may require, the QFII/RQFII regime
“Qualified Exchange Traded Funds”	means exchange traded funds that are: <ul style="list-style-type: none"> <li>(a) authorized by the SFC under 8.6 or 8.10 of the Code; or</li> <li>(b) listed and regularly traded on internationally recognized stock exchanges open to the public (nominal listing not accepted) and either (i) the principal objective of which is to track, replicate or correspond to a financial index or benchmark, which complies with the applicable requirements under 8.6 of the Code; or (ii) the investment objective, policy, underlying investments and product features of which are substantially in line with or comparable with those set out under 8.10 of the Code</li> </ul>
“Registrar”	means HSBC Institutional Trust Services (Asia) Limited in its capacity as the registrar of the Trust
“REITs”	means real estate investment trusts
“reverse repurchase transactions”	means transactions whereby a Sub-Fund purchases securities from a counterparty of sale and repurchase transactions and agrees to sell such securities back at an agreed price in the future
“Renminbi” or “RMB”	means the lawful currency of the PRC
“SAFE”	means the State Administration of Foreign Exchange
“sale and repurchase transactions”	means transactions whereby a Sub-Fund sells its securities to a counterparty of reverse repurchase transactions and agrees to buy such securities back at an agreed price with a financing cost in the future
“securities financing transactions”	means collectively securities lending transactions, sale and repurchase transactions and reverse repurchase transactions
“securities lending transactions”	means transactions whereby a Sub-Fund lends its securities to a security-borrowing counterparty for an agreed fee
“SFC”	means the Securities and Futures Commission in Hong Kong
“substantial financial institution”	means an authorized institution as defined in section 2(1) of the Banking Ordinance (Chapter 155 of Laws of Hong Kong) or a financial institution which is on an ongoing basis subject to prudential regulation and supervision, with a minimum net asset value of HK\$2 billion or its equivalent in foreign currency, as amended by the Code from time to time
“Sub-Fund”	means the separate pool of assets established in the books of the Trust for each class of Units



“TER”	means the total actual expenses of the Fund (being the ordinary operating expenses of the Fund including but not limited to the management fee (before adjustment) and any fees payable to the Trustee but exclusive of any establishment costs, costs of acquiring and disposing of investments, interest expenses, taxes, any non-recurring or extraordinary losses and expenses or any litigation costs or expenses incurred in connection therewith and other capital costs of the Fund) calculated on an accrual basis and expressed as a percentage per annum of the latest available Net Asset Value of the Fund
“Trust”	means First Sentier Investors Umbrella Funds
“Trust Deed”	means the trust deed between the Manager and the Trustee establishing the Trust
“Trustee”	means HSBC Institutional Trust Services (Asia) Limited in its capacity as the trustee of the Trust
“Unit”	means a unit in a Sub-Fund of the Trust
“Unitholder”	means a person who is registered on the register as the holder of a Unit
“US dollars”, “US\$” and “cent”	means the lawful currency of the United States of America
“US Person”	means a person so defined by Regulation S under the United States Securities Act of 1933 (as amended) and for the purposes of this Explanatory Memorandum, generally will include, subject to certain exceptions, (A) a natural person resident in the U.S., (B) a partnership or corporation organized or incorporated under the laws of the US (C) any estate of which any executor or administrator is a US Person, and (D) any trust of which any trustee is a US Person.

## INTRODUCTION

FIRST SENTIER INVESTORS UMBRELLA FUNDS is an umbrella fund, constituted as a unit trust pursuant to the laws of Hong Kong. A separate pool of assets held under a separate trust is established under the terms of the Trust Deed for the holders of each class of Units created under the umbrella. This document describes the Fund, which is a Sub-Fund of the Trust.

The Fund offers different classes of Units. Information on the different Unit classes is set out in the section headed “Details of Unit Classes” hereunder. The Manager may issue further classes of Units in the future and a separate Sub-Fund will be established as a separate trust with respect to which a separate class of Units will be issued.

## INVESTMENT OBJECTIVE AND POLICY

### Investment Objective and Policy

The objective of the Fund is to provide investors with medium term capital stability, a regular income stream and the potential for capital growth over the medium to long term through investing primarily (i.e. at least 70% of the Fund’s Net Asset Value) in a balanced portfolio consisting of equity or equity-related investments and fixed income debt securities issued by governments, supra-national entities, corporate or other issuers in the Asian (including Australia and New Zealand but excluding Japan) debt and securities markets. Although the Fund may invest in companies or issuers outside the Asian region, the Fund will normally invest at least 70% of its Net Asset Value in the Asian region. The Fund may invest less than 30% of its Net Asset Value in China A Shares (i) indirectly through equity linked or participation notes issued by institutions that have obtained the QFII/RQFII status or through investing in open-ended collective investment schemes that invest in China A Shares and (ii) directly via the QFII/RQFII, the Shanghai-Hong Kong Stock Connect and/or the Shenzhen-Hong Kong Stock Connect (the “**Stock Connects**”).

The Fund’s actual allocation of equity and fixed income investments will depend on and may vary according to changes in market conditions and the Manager’s judgment about how best to achieve the Fund’s investment objective. Under normal market conditions, the Fund will invest at least 40% of its Net Asset Value (and up to a maximum of 60%) in equity and equity-related securities (including but not limited to warrants and participation notes) of companies which are established, listed or have substantial assets in, or derive significant revenues from the Asian region. The Fund will seek to invest in stocks whose business strategies and operations provide sound growth prospects into the future and which enable them to provide investors with an above average dividend yield. For the avoidance of doubt, the Fund’s investment in participation notes will not exceed 15% of its total Net Asset Value.

The Fund will invest at least 40% of its Net Asset Value (and up to a maximum of 60%) in fixed income and similar transferable instruments (including convertible securities) issued by governments, supra-national entities, corporate and other issuers with a credit rating of or above B– by Standard & Poor’s, B3 by Moody’s, B– by Fitch, or a similar rating level by another recognised rating

agency or if unrated, of comparable quality as determined by the Manager. Under normal circumstances, the Fund will invest a significant portion of its Net Asset Value in instruments which are rated investment grade (i.e. credit rating of or above BBB– by Standard & Poor's, Baa3 by Moody's, BBB– by Fitch, or a similar rating level by another recognised rating agency). The Fund is not constrained as to the maximum maturity of its portfolio securities. The Fund's investment in debt securities may include securities with loss-absorption features (including contingent convertible debt securities, senior non-preferred debt, instruments issued under the resolution regime for financial institutions and other capital instruments issued by banks or other financial institutions) which will be up to 20% of the Fund's Net Asset Value.

The Fund may invest less than 30% of its Net Asset Value in onshore debt securities in the PRC via Bond Connect.

The Fund will not invest more than 10% of its Net Asset Value in debt securities issued or guaranteed by a single sovereign issuer which is below investment grade.

The debt securities in which the Fund invests are mainly denominated in US dollars or other major currencies.

The Fund may also invest less than 30% of its Net Asset Value in collective investment schemes subject to the relevant limits.

The Fund is not subject to any limitation on the portion of its Net Asset Value that may be invested in any one or more countries or markets in the Asian region. Nor is the Fund subject to any limitation on the sector or the market capitalisation of the companies it may invest in.

Under exceptional circumstances (e.g. market crash or major crisis), the Fund may be invested temporarily up to 100% of its Net Asset Value in liquid assets such as bank deposits, certificates of deposit, commercial paper and treasury bills for cash flow management.

The Fund will also issue distributions to investors on a monthly basis. The Manager has discretion to make distribution out of the income derived from the Fund's investment or from capital. Investors should be aware that this means that distributions may be issued from the capital they originally invest in the Fund (see the section headed "Distribution Policy" hereunder for further details).

#### **Use of Derivatives / Investment in Derivatives**

To achieve its objective, the Fund may engage in forward currency transactions and derivative instruments including options, futures and swap agreements such as credit default swap agreements for the purposes of efficient portfolio management and hedging against market and exchange rate risks.

The Fund's net derivative exposure may be up to 50% of the Fund's latest available Net Asset Value.

#### **Currency Denomination**

The Fund is denominated in US dollars.

#### **Details of Unit Classes**

The Fund offers different classes of Units. Information on the different Unit classes is set out below:

	<b>Class I</b>	<b>Class I (Hong Kong Dollar)</b>	<b>Class I (Renminbi)</b>
Currency of denomination	US\$	HK\$	RMB
Initial offer price	US\$10	HK\$100	RMB100
Minimum initial investment (Inclusive of any initial charge)	US\$1,000	HK\$7,500	RMB6,700
Minimum subsequent investment (Inclusive of any initial charge)	US\$500	HK\$4,000	RMB3,350
Minimum holding	US\$1,000	HK\$7,500	RMB6,700
Distribution policy	Distributing	Distributing	Distributing
Distribution frequency	Monthly	Monthly	Monthly
Initial charge	Up to 5.0%	Up to 5.0%	Up to 5.0%

Management fee per annum of the Net Asset Value of the Class	1.25%	1.25%	1.25%
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As noted above, the Manager is, at its discretion, entitled to impose an initial charge of up to 5% of the Net Asset Value per Unit. The Manager may waive the initial charge in part or in full and whether in respect of particular investors or generally.

## **Risk Factors**

An investment in the Fund comes with a significant degree of risk. Before you decide to invest, it is important to understand these risks. If you are unsure or do not fully understand the risks involved, we recommend that you contact a financial adviser about the suitability of an investment in the Fund.

The following section describes some of the general and specific risks that may affect your investment.

### **A. General Investment Risks**

#### **A1. Investment Risks**

The investments in securities of the Fund are subject to, general market risks, normal market fluctuations and other risks inherent in investing in securities. For example, the value of equity securities varies from day to day in response to activities of individual companies, general market and political and economic conditions, investment sentiment and issuer specific factors. The value of investments and the income from them, and therefore the Net Asset Value of Units can go down as well as up due to any of the risk factors below and an investor may suffer losses in investment. Changes in exchange rates between currencies or the conversion from one currency to another may also cause the value of the investments to diminish or increase. As investors may be required to pay an initial charge upon a subscription for Units, an investment in the Fund should be considered as a medium to long-term investment. There is no guarantee of repayment of principal.

#### **A2. Market Risk**

In falling financial markets there may be increased volatility. Market prices in such circumstances may defy rational analysis or expectation for prolonged periods of time, and can be influenced by large market movements as a result of short-term factors, counter-speculative measures or other reasons. Market volatility of a large enough magnitude can sometimes weaken what is deemed to be a sound fundamental basis for investing in a particular market or stock. Investment expectations may therefore fail to be realised in such instances.

#### **A3. Volatility and Liquidity Risk**

In certain circumstances, the Fund may not be able to purchase or sell assets in a timely manner and/or at a reasonable price, as not all securities invested in by the Fund will be listed or rated and consequently liquidity may be low. Liquidity risk exists if sizeable redemption requests are received as the Fund may need to liquidate its investments at a substantial discount in order to satisfy such requests and the Fund may suffer losses in trading such investments. Moreover, the debt securities in certain markets may be subject to higher volatility and lower liquidity compared to more developed markets. The prices of securities traded in such markets may be subject to fluctuations. Furthermore, shares or units in certain underlying investments may trade less frequently and in smaller quantities than others. If this is the case, this may adversely affect the Fund's Net Asset Value and/or investors may suffer a loss as a result.

#### **A4. Currency Risk**

Investments of the Fund may be denominated in various currencies other than the base currency. Also, a class of Units may be designated in a currency other than the base currency of the Fund. The performance of the Fund may be strongly influenced by movements in exchange rates between these currencies. Such investments require consideration of certain risks which include, among other things, trade balances and imbalances and related economic policies, unfavourable currency exchange rate fluctuations, impositions of exchange control regulation by governments, withholding taxes, limitations on the removal of funds or other assets, policies of governments with respect to possible nationalisation of their industries, political difficulties, including expropriation of assets, confiscatory taxation and economic or political instability.

The Manager may use currency hedging techniques to remove the Fund's currency exposure against its base currency but this may not be possible or practicable in all cases.

#### **A5. Specialist Investment Risk**

The Fund is specialist in nature and invests in specific markets or regions. Investment in these specialised areas

may result in greater risk than investment in a broader range of markets or regions. Please also see “Fund Specific Risks” below.

**A6. *Inflation Risk***

Inflation can adversely affect the value of your investment.

**A7. *Credit Risk***

Investment in debt or other securities may be subject to the credit risk of their issuers. In times of financial instability there may be increased uncertainty around the creditworthiness of issuers of these securities. Market conditions may mean that there are increased instances of default amongst issuers. If the issuer of any of the debt securities in which the assets of the Fund are invested defaults or suffers insolvency or other financial difficulties, the value of the Fund will be adversely affected.

**A8. *Taxation Risk***

Potential investors’ attention is drawn to the taxation risks associated with an investment in the Fund. Please see the section headed “Taxation”.

**A9. *Risk of Change of Laws, Regulations, Political and Economic Conditions***

Changes in the applicable laws, regulations, political and economic conditions may affect substantially and adversely the business and prospects of the Fund. In addition, possible changes to the laws and regulations governing permissible activities of the Fund and the Manager and any of their respective affiliates or delegates could restrict or prevent the Fund or the Manager from continuing to pursue the Fund’s investment objectives or to operate the Fund in the manner currently contemplated.

**A10. *Risk of Suspension***

The calculation of the Net Asset Value of the Fund may be temporarily suspended in accordance with the procedures set out in the section headed “Suspension of Calculation of Net Asset Value”. In such an event, the Fund may be unable to dispose of its investments. The delay in the disposal of the Fund’s investments may adversely affect both the value of the investments being disposed of, and the value and liquidity of the Fund.

**A11. *Derivatives Risk***

The term “derivative” traditionally applies to certain contracts that “derive” their value from changes in the value of the underlying securities, currencies, commodities or index. Investors refer to certain types of securities that incorporate performance characteristics of these contracts as derivatives. When used for hedging purposes there may be an imperfect correlation between the financial derivative instruments and the investments or market sectors being hedged. Derivatives are sophisticated instruments that typically involve a small investment of cash relative to the magnitude of risks assumed. These include swap agreements, options, futures, and convertible securities. The Fund may engage in forward currency transactions and derivative instruments including options, futures and swap agreements such as credit default swap agreements for the purposes of efficient portfolio management and hedging against market and exchange rate risks. While the price reaction of certain derivatives to market changes may differ from traditional investments such as stocks and bonds, derivatives do not necessarily present greater market risks than traditional investments. Derivatives are subject to credit risks related to the counterpart’s ability to perform, and any deterioration in the counterpart’s creditworthiness could adversely affect the instrument.

The Fund is also subject to counterparty/credit risk, liquidity risk, valuation risk, volatility risk and risk of the failure of any of the exchanges on which derivatives are traded or of their clearing houses. The leverage element/component of a derivative can result in a loss significantly greater than the amount invested in the derivatives by the Fund. Exposure to derivatives may lead to a high risk of significant loss by the Fund.

Derivatives traded over-the-counter may not be standardised and thus may involve negotiations on each contract on an individual basis. This may result in over-the-counter contracts being less liquid than exchange traded derivatives. Over-the-counter markets are typically not subject to credit evaluation and regulatory oversight as are members of “exchange based” markets, and there is no clearing corporation which guarantees the payment of required amounts. This exposes the Fund to risk that a counterparty will not settle a transaction in accordance with its terms and conditions because of a dispute over the terms of the contract (whether or not bona fide) or because of a credit or liquidity problem, thus may cause the Fund to suffer a significant loss.

Also, there are legal risks involved in using derivatives which may result in loss due to the unexpected application of a law or regulation or because contracts are not legally enforceable or documented correctly.

**A12. *Risks associated with FATCA***

The Trust intends to comply with the legislation and obligations imposed on it by FATCA and meet its obligation under the US-Hong Kong IGA (as defined in "The Foreign Account Tax Compliance Act and similar measures" in the "Taxation" section below). However, there can be no assurance that the aforementioned obligations with respect to the Trust can be met.

The Trust will require Unitholders to certify information relating to their status for FATCA purposes and to provide certain forms, documentation and information in relation to their FATCA status. The Trust may be unable to comply with FATCA obligations if, among others, Unitholders do not provide the required certifications or information. The Trust could become subject to FATCA withholding tax in respect of its U.S. source income and certain other receipts for failure to comply with any requirement under FATCA and/or the US-Hong Kong IGA. Any such FATCA withholding tax would negatively impact the financial performance of the Trust and all Unitholders may be adversely affected in such circumstances.

#### **A13. Valuation Risk**

Valuation of the Fund's investments may involve uncertainties and judgmental determinations. If such valuation turns out to be incorrect, this may affect the Net Asset Value calculation of the Fund.

#### **A14. Custody Risk**

Custodians or sub-custodians may be appointed in local markets for the purpose of safekeeping assets in those markets. Where the Fund invests in markets where custodial and/or settlement systems are not fully developed, the assets of the Fund that are traded in such markets and which have been entrusted to such custodians or sub-custodians may be exposed to custodial risk in circumstances where the Trustee's liability may be limited pursuant to the Trust Deed. In case of liquidation, bankruptcy or insolvency of a custodian or sub-custodian, the Fund may take a longer time to recover its assets. In extreme circumstances such as the retroactive application of legislation and fraud or improper registration of title, the Fund may even be unable to recover all of its assets. The costs borne by the Fund in investing and holding investments in such markets will be generally higher than in organised securities markets.

#### **A15. Regulations, Restrictions and Sanctions**

Regulations, restrictions and sanctions may be imposed by governments or international bodies (such as the United Nations) or their agencies which impact investments held by the Fund. Limits may be imposed on the amount and type of securities that may be purchased by the Fund or the sale and timing of sale of such securities once purchased or the identity of permissible counterparties. Limits may also be imposed on potential purchasers of securities held by the Fund, thereby preventing certain purchasers and counterparties from transacting in those securities, limiting the liquidity of those securities and/or otherwise affecting the market price that is available for those securities. It is also possible that such limits may initially be introduced by one or a small group of countries or bodies and other countries or bodies may after the relevant securities are purchased by the Fund introduce the same or similar limits thereby further reducing market liquidity. If such limits are adopted by all countries or bodies on a global basis, then there may be no liquidity available if the Fund wishes to sell those securities. Restrictions that are not directly targeted at a company or country may still have an incidental effect on the Fund including the manner of settlement of purchases or sales of securities. Generally, prospective counterparties may decline to participate in transactions involving relevant securities based on their individual policies and risk tolerances, regardless of their ability to do so under laws applicable to the counterparties, further reducing liquidity in ways that cannot be predicted.

The ability of the Fund to invest or otherwise deal in securities of companies or governments of certain countries may be limited or, in some cases, prohibited. As a result, larger portions of the Fund's assets may be invested in those companies or countries where such limitations do not exist. Such restrictions may also affect the market price, liquidity and rights of securities that may be purchased by the Fund, and may increase fund expenses. In addition, policies established by the governments or international bodies may adversely affect the Fund's investments and the ability of the Fund to achieve its investment objective.

In addition, the repatriation of both investment income and capital is often subject to restrictions such as the need for certain governmental consents, and even where there is no outright restriction, the mechanics of repatriation or, in certain countries, the inadequacy of major currencies available to non-governmental entities, may affect certain aspects of the operation of the Fund. In countries that have an inadequate supply of major currencies, issuers that have an obligation to pay the Fund in a major currency (e.g. US dollars) may experience difficulty and delay in exchanging local currency to the relevant major currency and thus hinder the Fund's repatriation of investment income and capital. Moreover, such difficulty may be exacerbated in instances where governmental entities in such countries are given priority in obtaining such scarce currency. Furthermore, a Fund's ability to invest in the securities markets of several countries is restricted or controlled to varying degrees by laws restricting foreign investment and these restrictions may, in certain circumstances, prohibit the Fund from making direct investments. Further, regulators and exchanges are authorised to regulate trading or other activity with respect to certain markets and may impose other restrictions which could have significant adverse effects on the Fund's portfolio and the ability of the Fund to



pursue its investment strategies and achieve its investment objective.

#### **A.16. Counterparty Risk**

The Fund's cash held in accounts with other banks is at risk of loss due to the failure or insolvency of those institutions. A Fund's cash held with such institutions may not be segregated from the banks' own cash or the cash held under custody for other clients of the banks, and the Fund may therefore rank as an unsecured creditor in relation to the cash balance in the case of insolvency of the banks.

The assets of the Fund are held by the Trustee for safe keeping. In accordance with the Trust Deed, in safe keeping the assets of the Trust, the Trustee shall take into custody or under its control all the investments, cash and other assets forming part of the assets of the Fund and hold them in trust for the Unitholders of the Fund and, to the extent permitted by law, shall register cash and registrable assets in the name of or to the order of the Trustee. Assets held by the Trustee should also be segregated from other securities / assets of the Trustee in accordance with applicable law and regulation. This reduces but does not exclude the risk that assets will not be returned to the Fund in the event of the insolvency of the Trustee. Investors are therefore exposed to the risk of the Trustee not being able to fully meet its obligation to return all of the assets of the Fund in the case of insolvency of the Trustee. The Trustee may not keep all the assets of the Trust itself but may use a network of sub-custodians which are not always part of the same group of companies as the Trustee. Investors may be exposed to the risk of insolvency of the sub-custodians in circumstances where the Trustee's liability may be limited by the Trust Deed.

#### **A.17. Pandemic / Epidemic Risk**

Outbreaks of infectious diseases may have a negative impact on the performance of the Fund. For example, an outbreak of respiratory disease caused by a novel coronavirus was first detected in December 2019 and has spread globally. This coronavirus has had a large and negative impact on economies which is likely to be long-lasting. It has resulted in borders closing, restrictions on movement of people, quarantines, cancellations of transportation and other services, disruptions to supply chains, businesses and customer activity, closure of businesses, as well as general concern and uncertainty. It is possible that there may be similar outbreaks of other infectious diseases and variants of the existing virus in circulation in the future. The impact of this coronavirus, and other epidemics and pandemics that may arise in the future, could affect the economies of many nations, individual companies and the market in general in ways that cannot be foreseen. The impact of infectious diseases in emerging developing or emerging market countries may be greater due to less established health care systems. Health crises caused by the coronavirus outbreak may exacerbate political, social and economic risks in certain countries.

### **B. Fund Specific Risks**

#### **B1. Emerging Markets Risks**

The Fund may invest in securities of issuers located in emerging markets and increased risks and special considerations not typically associated with investment in more developed markets may be encountered. These may adversely affect the Fund's Net Asset Value and/or investors may suffer loss as a result. The investments may be considered to be speculative in nature as they involve a greater than normal degree of risk and their market values may be expected to be of above average volatility.

These risks include:–

**Currency depreciation/control.** The Fund's assets may be invested in securities which are denominated in currencies other than those of developed countries and any income received by the Fund from those investments will be received in those currencies. There is no assurance that the currencies of developing countries (including that of RMB) will not be subject to devaluation, in which case the value of their investments will be adversely affected. As the Fund computes its Net Asset Value in US\$, there is a currency exchange risk which may affect the value of the Units. Currency control may also be implemented in the emerging markets.

**RMB currency and conversion risks** RMB is currently not freely convertible and is subject to exchange controls and restrictions. Non-RMB based investors are exposed to foreign exchange risk and there is no guarantee that the value of RMB against the investors' base currencies (for example HKD) will not depreciate. Any depreciation of RMB could adversely affect the value of investor's investment in the Fund. Although offshore RMB (CNH) and onshore RMB (CNY) are the same currency, they trade at different rates. Any divergence between CNH and CNY may adversely impact investors. Under exceptional circumstances, payment of redemptions and/or dividend payment (if any) in RMB may be delayed due to the exchange controls and restrictions applicable to RMB.

**Country risk.** The value of the Fund's assets may be affected by uncertainties within the emerging market country in which it invests such as changes in government policies, nationalisation of industry, taxation, the underdeveloped and often untested legal system, currency repatriation restrictions and other developments in the law, practice or regulations of the countries in which the Fund may invest and, in particular, by changes in legislation relating to the level of foreign ownership in companies in some emerging countries.

**Social, Political and Economic Factors.** The economies of many emerging countries may be subject to a substantially greater degree of social, political and economic instability than certain developed countries. Such instability may result from, among other things, the following; authoritarian governments, popular unrest associated with demands for improved political, economic and social conditions, internal insurgencies and terrorist activities, hostile relations with neighbouring countries and drugs trafficking. This instability might impair the financial conditions of issuers or disrupt the financial markets in which the Fund invests.

**Taxation risk.** The tax law and practices of certain emerging markets may not be fully developed or sufficiently certain. Any future changes in these law and practices or their interpretation may adversely affect the Net Asset Value of the Fund.

**Stock market practices.** Many emerging markets are undergoing a period of rapid growth and are less regulated than many of the world's leading stock markets. In addition market practices in relation to settlement of securities transactions and custody of assets in emerging markets can provide increased risk to the Fund and may involve delays in obtaining accurate information on the value of securities (which may affect the calculation of the Net Asset Value as a result) and the risk that the investments may not be accurately registered. These stock markets, in general, are less liquid than those of the world's leading stock markets. Purchases and sales of investments may take longer than would otherwise be expected on developed stock markets and transactions may need to be conducted at unfavourable prices. Some emerging markets require that moneys for settlement be received by a local broker significantly in advance of settlement and that assets are not transferred until some time after settlement. This exposes the Fund to additional counterparty risk arising from the activities of the broker during these periods. Liquidity may also be less and volatility of prices higher than in leading markets because of a high degree of concentration of market capitalisation and trading volumes in a small number of companies. High market volatility and potential settlement difficulties in the markets may also result in significant fluctuations in the prices of the securities traded on such markets and thereby may adversely affect the value of the Fund. In some emerging markets evidence of legal title to securities is maintained in "book-entry" form and the role of the local registrar is critical to the registration and custody process. Such registrars may not be subject to effective governmental or regulatory supervision and it may be difficult to successfully claim against them.

**Information quality.** Accounting, auditing and financial reporting standards, practices and disclosure requirements applicable to some companies in emerging markets in which the Fund may invest may differ from those applicable in developed countries because less information is available to investors and such information may be out of date or carry a lower level of assurance.

**Custody.** Local custody services remain underdeveloped in many emerging market countries and there is a transaction and custody risk involved in dealing in such markets. In certain circumstances the Fund may not be able to recover some of its assets. Such circumstances may include the liquidation, bankruptcy or insolvency of a sub-custodian, retroactive application of legislation and fraud or improper registration of title. The costs borne by the Fund in investing and holding investments in such markets will be generally higher than in organised securities markets.

**Registration.** In some emerging market countries evidence of legal title to shares is maintained in "book-entry" form. In order to be recognised as the registered owner of the shares of a company, a purchaser or purchasers' representative must physically travel to the registrar and open an account (which, in certain cases, requires the payment of an account opening fee). Thereafter, each time that the purchaser purchases additional shares of the company, the purchasers' representative must present to the registrar, powers of attorney from the purchaser and the seller of such shares, along with evidence of such purchase, at which time the registrar will debit such purchased shares from the seller's account maintained on the register and credit such purchased shares to the purchaser's account to be maintained on the register.

The role of the registrar in such custodial and registration processes is crucial. Registrars may not be subject to effective government supervision and it is possible for the Fund to lose its registration through fraud, negligence or mere oversight on the part of the registrar. Furthermore, while companies in certain emerging market countries may be required to maintain independent registrars that meet certain statutory criteria, in practice, there can be no guarantee that this regulation has been strictly enforced. Because of this possible lack of independence, management of companies in such emerging market countries can potentially exert significant influence over the shareholding in such companies. If the company register were to be destroyed or mutilated, the Fund's holding of the relevant shares of the company could be substantially impaired, or in certain cases, deleted. Registrars often do not maintain insurance against such occurrences, nor are they likely to have assets sufficient to compensate the Fund. While the registrar and the company may be legally obliged to remedy such loss, there is no guarantee that either of them would do so, nor is there any guarantee that the Fund would be able to successfully bring a claim against them as a result of such loss. Furthermore, the registrar or the relevant company could willfully refuse to recognise the Fund as the registered holder of shares previously purchased by the Fund due to the destruction of the company's register.

**Risk associated with regulatory/exchanges requirements/policies of the equity market in emerging markets.** Securities exchanges in emerging markets typically have the right to suspend or limit trading in any security traded on the relevant exchange. The government or the regulators may also implement policies that may affect the financial

markets. All these may have a negative impact on the Fund.

## **B2. Risks associated with investments via Stock Connects**

### **General Overview**

The Shanghai-Hong Kong Stock Connect is a securities trading and clearing links program developed by the Hong Kong Exchanges and Clearing Limited ("**HKEx**"), the Shanghai Stock Exchange ("**SSE**") and the China Securities Depository and Clearing Corporation Limited ("**ChinaClear**") and the Shenzhen-Hong Kong Stock Connect is a securities trading and clearing links program developed by the HKEx, the Shenzhen Stock Exchange ("**SZSE**") and ChinaClear. The aim of the Stock Connects is to achieve mutual stock market access between the PRC and Hong Kong.

The Shanghai-Hong Kong Stock Connect comprises a Northbound Shanghai Trading Link and a Southbound Hong Kong Trading Link. Under the Northbound Shanghai Trading Link, Hong Kong and overseas investors (including the Fund), through their Hong Kong brokers, sub-custodians and a securities trading service company established by the Stock Exchange of Hong Kong ("**SEHK**"), may be able to trade eligible China A Shares listed on the SSE ("**SSE securities**") by routing orders to SSE. Under the Southbound Hong Kong Trading Link under Shanghai-Hong Kong Stock Connect, investors in the PRC will be able to trade certain stocks listed on the SEHK.

The Shanghai-Hong Kong Stock Connect commenced trading on 17 November 2014 under a joint announcement issued by the SFC and the CSRC on 10 November 2014.

The Shenzhen-Hong Kong Stock Connect comprises a Northbound Shenzhen Trading Link and a Southbound Hong Kong Trading Link. Under the Northbound Shenzhen Trading Link, Hong Kong and overseas investors (including the Fund), through their Hong Kong brokers, sub-custodians and a securities trading service company established by SEHK, may be able to trade eligible China A Shares listed on the SZSE ("**SZSE securities**") by routing orders to SZSE. Under the Southbound Hong Kong Trading Link under Shenzhen-Hong Kong Stock Connect, investors in the PRC will be able to trade certain stocks listed on the SEHK.

The Shenzhen-Hong Kong Stock Connect commenced trading on 5 December 2016 under a joint announcement issued by the SFC and the CSRC on 25 November 2016.

### **Eligible Securities**

#### **(i) The Shanghai-Hong Kong Stock Connect**

Under the Shanghai-Hong Kong Stock Connect, the Fund, through the Hong Kong brokers may trade SSE securities. These include all the constituent stocks from time to time of the SSE 180 Index and SSE 380 Index, and all the SSE-listed China A shares that are not included as constituent stocks of the relevant indices but which have corresponding H Shares listed on SEHK, except the following:

- SSE-listed shares which are not traded in RMB; and
- SSE-listed shares which are included in the "risk alert board" or under a delisting arrangement.

It is expected that the list of eligible securities will be subject to review and may change.

#### **(ii) The Shenzhen-Hong Kong Stock Connect**

Under the Shenzhen-Hong Kong Stock Connect, the Fund, through the Hong Kong brokers may trade SZSE securities. These include any constituent stock of the SZSE Component Index and SZSE Small/Mid Cap Innovation Index which has a market capitalisation of RMB6 billion or above and all the SZSE-listed China A Shares which have corresponding H Shares listed on SEHK, except the following:

- SZSE-listed shares which are not traded in Renminbi; and
- SZSE-listed shares which are included in the "risk alert board" or under a delisting arrangement.

At the initial stage of the Northbound Shenzhen Trading Link, investors eligible to trade shares that are listed on the ChiNext Board of SZSE under the Northbound Shenzhen Trading Link will be limited to institutional professional investors (and the Fund will qualify as such) as defined in the relevant Hong Kong rules and regulations.

It is expected that the list of eligible securities will be subject to review and may change.

### **Trading Quota**



The trading is subject to rules and regulations issued from time to time. Trading under the Stock Connects will be subject to a daily quota ("**Daily Quota**"). The Northbound Shanghai Trading Link and the Southbound Hong Kong Trading Link under the Shanghai-Hong Kong Stock Connect and the Northbound Shenzhen Trading Link and the Southbound Hong Kong Trading Link under the Shenzhen-Hong Kong Stock Connect, will be subject to a separate set of Daily Quota respectively. The Daily Quota limits the maximum net buy value of cross-boundary trades under the Stock Connects each day.

SEHK will monitor the Daily Quota and publish the remaining balance of the Northbound Daily Quota regularly on the HKEX's website.

### ***Settlement and Custody***

The Hong Kong Securities Clearing Company Limited ("**HKSCC**"), a wholly-owned subsidiary of HKEX, and ChinaClear will be responsible for the clearing, settlement and the provision of depositary, nominee and other related services of the trades executed by their respective market participants and investors. The SSE securities and SZSE securities traded through the Stock Connects are issued in uncertificated form and investors will not hold any physical certificates in relation to these securities. Hong Kong and overseas investors who have acquired SSE securities or SZSE securities through Northbound trading should maintain the SSE securities or SZSE securities with their brokers' or custodians' stock accounts with CCASS (the Central Clearing and Settlement System operated by HKSCC for the clearing securities listed or traded on SEHK).

### ***Corporate Actions and Shareholders' Meetings***

Although HKSCC does not claim proprietary interests in the SSE securities and SZSE securities held in its omnibus stock account in ChinaClear, ChinaClear as the share registrar for SSE and SZSE listed companies will still treat HKSCC as one of the shareholders when it handles corporate actions in respect of such SSE securities and SZSE securities.

HKSCC will monitor the corporate actions affecting SSE securities and SZSE securities and keep the relevant brokers or custodians participating in CCASS ("**CCASS participants**") informed of all such corporate actions that require CCASS participants to take steps in order to participate in them.

Companies listed on the SSE or SZSE usually announce information regarding their annual general meetings/ extraordinary general meetings about two to three weeks before the meeting date. A poll is called on all resolutions for all votes. HKSCC will advise CCASS participants of all general meeting details such as meeting date, time, venue and the number of resolutions.

A failure or delay by HKSCC in the performance of its obligations may result in a failure of settlement, or the loss, of SSE securities and/or SZSE securities and/or monies in connection with them and the Fund may suffer losses as a result.

### ***Trading Fees***

Under the Stock Connects, Hong Kong and overseas investors (including the Fund) will be subject to the fees and levies imposed by SSE, SZSE, ChinaClear, HKSCC or the relevant Mainland Chinese authority when they trade and settle SSE securities and SZSE securities. Further information about the trading fees and levies is available online at the website: [http://www.hkex.com.hk/eng/market/sec\\_tradinfra/chinaconnect/chinaconnect.htm](http://www.hkex.com.hk/eng/market/sec_tradinfra/chinaconnect/chinaconnect.htm).

### ***Specific Risks Applicable to investing via the Stock Connects***

In addition to the risk factors "B1. Emerging Markets Risks" and "B5. China Market Risk" the following additional risks apply:—

- **Quota Limitations:** The Stock Connects are subject to quota limitations, as detailed above. In particular, the Stock Connects are subject to a Daily Quota which does not relate to the Fund and can only be utilised on a first-come- first-serve basis. Once the remaining balance of the Northbound Daily Quota drops to zero or is exceeded during the opening call auction session, new buy orders will be rejected (although investors will be permitted to sell their cross-boundary securities regardless of the quota balance). Therefore, quota limitations may restrict the Fund's ability to invest in SSE securities and SZSE securities through the Stock Connects on a timely basis, and the Fund may not be able to effectively pursue its investment strategy.
- **Taxation Risk:** Please refer to the sub-section headed "Investments in China A Shares via the Stock Connects and QFII/RQFII" in the section headed "Taxation" of this Explanatory Memorandum.
- **Legal/Beneficial Ownership:** The SSE securities and SZSE securities in respect of the Fund will be held by the Trustee/sub-custodian in accounts in the Hong Kong Central Clearing and Settlement System maintained by the HKSCC as central securities depositary in Hong Kong. HKSCC in turn holds the SSE securities and

SZSE securities, as the nominee holder, through an omnibus securities account in its name registered with ChinaClear, HKSCC is only a nominee holder and the Fund remains the beneficial owner of the SSE securities and SZSE securities. The Fund's title or interests in, and entitlements to SSE securities and SZSE securities (whether legal, equitable or otherwise) will therefore be subject to applicable requirements, including laws relating to any disclosure of interest requirement or foreign shareholding restriction. CCASS Rule 824 confirms that all proprietary interests in respect of China A Shares held by HKSCC as nominee holder belong to CCASS participants or their clients (as the case may be). Also as set out in CCASS Rule 824, HKSCC is prepared to provide assistance to the beneficial owners of China A Shares, where necessary, to provide certification to ChinaClear for the purpose of providing evidential proof of the CCASS participant's or its client's holding in China A Shares; and to assist the CCASS participant or its client bringing the legal action in the PRC in the manner as may be required under PRC law, after having regard to its statutory duties and subject to such conditions as HKSCC may reasonably require (including payment of fees and costs upfront and indemnities to the satisfaction of HKSCC).

Although the relevant CSRC regulations and ChinaClear rules generally provide for the concept of a nominee holder and recognise the Hong Kong and overseas investors (including the Fund) as the ultimate owners who would be recognised under the laws and regulations of the PRC as having beneficial ownership in the China A Shares traded via the Stock Connects, how an investor such as the Fund, as the beneficial owner of the China A Shares, under the Stock Connects structure, exercises and enforces its rights over the China A Shares in the PRC courts are to be tested.

- Clearing and Settlement Risk:* HKSCC and ChinaClear have established clearing links and each has become a participant of each other to facilitate clearing and settlement of cross-boundary trades. For cross-boundary trades initiated in a market, the clearing house of that market will on the one hand clear and settle with its own clearing participants, and on the other hand undertake to fulfil the clearing and settlement obligations of its clearing participants with the counterparty clearing house. As the national central counterparty of the PRC's securities market, ChinaClear operates a comprehensive network of clearing, settlement and stock holding infrastructure. ChinaClear has established a risk management framework and measures that are approved and supervised by the CSRC. The chances of ChinaClear default are considered to be remote. In the remote event of a ChinaClear default, HKSCC's liabilities in Northbound trades under its market contracts with clearing participants will be limited to assisting clearing participants in pursuing their claims against ChinaClear, but it is not obliged to do so. HKSCC will in good faith, seek recovery of the outstanding stocks and monies from ChinaClear through available legal channels or through ChinaClear's liquidation process, if available. In the event of a ChinaClear default, the Fund may suffer delay in the recovery process or may not fully recover its losses from ChinaClear.
- Suspension Risk:* Each of the SEHK, SSE and SZSE reserves the right to suspend trading of SSE securities and SZSE securities purchased on the Stock Connects if necessary for ensuring an orderly and fair market and that risks are managed prudently. Consent from the relevant regulator would be sought before a suspension of Northbound trading is triggered. Where a suspension in the Northbound trading through the Stock Connects is effected, the Fund's ability to access the PRC market through Stock Connects will be adversely affected.
- Differences in Trading Day:* The Stock Connects will only operate on days when the Shanghai or Shenzhen and Hong Kong markets are open for trading and when banks in both sets of markets are open on the corresponding settlement days. Therefore, it is possible that there are occasions when it is a normal trading day for the SSE or SZSE market but the Fund cannot carry out any SSE securities or SZSE securities trading via the Stock Connects. The Fund may be subject to a risk of price fluctuations in SSE securities and SZSE securities during any time when the Stock Connects are not trading.
- Restrictions on Selling Imposed by Front-end Monitoring PRC:* regulations require that before an investor sells any share, there should be sufficient shares in the account otherwise the SSE or SZSE will reject the sell order concerned. SEHK will carry out pre-trade checking on SSE securities and SZSE securities sell orders of its participants (i.e. the stock brokers) to ensure there is no over-selling. If the Fund intends to sell certain SSE securities and SZSE securities it holds, it must ensure the availability of those securities is confirmed by its broker(s) before the market opens on the day of selling ("**trading day**"). If it fails to meet this deadline, it will not be able to sell those shares on the trading day. Because of this requirement, the Fund may not be able to dispose of its holdings of SSE securities and SZSE securities in a timely manner.
- Operational Risk:* The Stock Connects are premised on the functioning of the operational systems of the relevant market participants. Market participants are permitted to participate in this program subject to meeting certain information technology capability, risk management and other requirements as may be specified by the relevant exchange and/or the relevant clearing house.

The securities regimes and legal systems of the two markets differ significantly and market participants may need to address issues arising from the differences on an on-going basis. There is no assurance that the systems of the SEHK and market participants will function properly or will continue to be adapted to changes and developments in both markets. In the event that the relevant systems fail to function properly, trading in

both markets through the program could be disrupted. The Fund's ability to access the PRC market (and hence to pursue its investment strategy) may be adversely affected.

- *Regulatory Risk:* The current regulations relating to the Stock Connects are untested and there is no certainty as to how they will be applied. Using the Stock Connects as a means of investment will result in trades being subject to additional restrictions to those usually traded directly on exchange, which may result in investments being subject to greater or more frequent rises and falls in value and the investments may be harder to liquidate. In addition, the current regulations are subject to change which may have potential retrospective effects and there can be no assurance that the Stock Connects will not be abolished. New regulations may be issued from time to time by the regulators/stock exchanges in the PRC and Hong Kong in connection with operations, legal enforcement and cross-border trades under the Stock Connects. The Fund may be adversely affected as a result of such changes.
- *Recalling of Eligible Stocks:* When a stock is recalled from the scope of eligible stocks for trading via the Stock Connects, the stock can only be sold but is restricted from being bought. This may affect the investment portfolio or strategies of the Fund, for example, if the Manager wishes to purchase a stock which is recalled from the scope of eligible stocks.
- *No Protection by the China Securities Investor Protection Fund:* Investment in SSE securities and SZSE securities via the Stock Connects is conducted through securities brokers in Hong Kong. Since the Fund's investments via the Northbound trading under the Stock Connects are through securities brokers in Hong Kong but not Mainland Chinese brokers, they are not protected by the China Securities Investor Protection Fund in Mainland China.

#### B3. *Risks associated with instruments with loss-absorption features*

The Fund may invest in instruments with loss-absorption features which are subject to greater risks when compared to traditional debt instruments as such instruments typically include terms and conditions which may result in them being partly or wholly written off, written down, or converted to ordinary shares of the issuer upon the occurrence of a pre-defined trigger event (e.g. when the issuer is near or at the point of non-viability or when the issuer's capital ratio falls to a specified level).

Such trigger events are likely to be outside of the issuer's control and commonly include a reduction in the issuer's capital ratio below a specified level or upon specific government or regulatory action being taken as a result of the issuer's ongoing financial viability. Trigger events are complex and difficult to predict and can result in a significant or total reduction in the value of such instruments, giving rise to consequential loss of the Fund. In the event of the activation of a trigger, there may be potential price contagion and volatility to the entire asset class. Instruments with loss-absorption features may also be exposed to liquidity, valuation and sector concentration risk.

For example, the Fund may invest in contingent convertible debt securities ("CoCos"). CoCos are hybrid capital securities that absorb losses when the capital of the issuer falls below a certain level. Upon the occurrence of a predetermined event (known as a trigger event), CoCos will be converted into shares of the issuing company (potentially at a discounted price as a result of the deterioration in the financial condition of the issuing company), or cause the permanent writedown to zero of the principal investment and/or accrued interest such that the principal amount invested may be lost on a permanent or temporary basis. CoCos are subject to the general risks associated with bonds and equities, and to the risks specific to convertible securities in general. CoCos are also subject to additional risks specific to their structure including:

- *Conversion risk* Trigger levels differ and determine exposure to conversion risk. It might be difficult for the Manager to anticipate the trigger events and assess how the CoCos will behave upon conversion. In case of conversion into equity, the Manager might be forced to sell these new equity shares subject to the investment policy of the Fund. Given the trigger event is likely to be some event depressing the value of the issuer's common equity, this forced sale may result in the Fund experiencing losses.
- *Coupon cancellation risk* Coupon payments on CoCos are discretionary and may be cancelled by the issuer at any point, for any reason, and for any length of time. As a result of the uncertainty surrounding coupon payments, CoCos may be volatile and their price may decline rapidly in the event that coupon payments are suspended.
- *Capital structure inversion risk* CoCos are typically structurally subordinated to traditional convertible bonds in the issuer's capital structure. In certain scenarios, investors in contingent convertible securities may suffer a loss of capital ahead of equity holders or when equity holders do not.
- *Call extension risk* CoCos are perpetual instruments and may only be callable at predetermined dates upon approval of the applicable regulatory authority. There is no guarantee that the Fund will receive return of principal on contingent convertible securities.

- **Valuation and write-down risk** CoCos often offer attractive yield which may be viewed as a complexity premium and is subject to a higher risk of overvaluation of such asset class on the relevant eligible markets. Therefore, the Fund may lose its entire investment or may be required to accept cash or securities with a value less than its original investment.
- **Subordinated instruments** CoCos will, in the majority of circumstances, be issued in the form of subordinated debt instruments. Accordingly, in the event of liquidation, dissolution or winding-up of an issuer prior to a conversion, the Fund's rights and claims against the issuer in respect of or arising under the terms of the CoCos shall generally rank junior to the claims of all holders of unsubordinated obligations of the issuer.
- **Novelty and untested nature** The structure of CoCos is innovative yet untested. It is uncertain how CoCos will perform in a stressed environment.

The Fund may also invest in senior non-preferred debts. While these instruments are generally senior to subordinated debts, they may be subject to write-down upon the occurrence of a trigger event and will no longer fall under the creditor ranking hierarchy of the issuer. This may result in total loss of principal invested.

#### *B4. Risks associated with investments via Bond Connect*

##### **Overview**

Bond Connect is an initiative launched in July 2017 for mutual bond market access between the PRC and Hong Kong, established by the China Foreign Exchange Trade System & National Interbank Funding Centre ("**CFETS**"), China Central Depository & Clearing Co., Ltd ("**CCDC**"), Shanghai Clearing House ("**SHCH**"), Hong Kong Exchanges and Clearing Limited and Central Moneymarkets Unit ("**CMU**").

The PBOC and the Hong Kong Monetary Authority ("**HKMA**") have approved programmes which establish Bond Connect, a mutual bond market access programme between mainland Chinese and Hong Kong financial infrastructure institutions. Bond Connect allows investors to trade electronically between the mainland Chinese and Hong Kong bond markets without many of the limits of existing schemes, such as quota restrictions and requirements to identify the ultimate investment amount, and to invest in China's Interbank Bond Market ("**CIBM**").

Currently, Bond Connect comprises a northbound trading link between CFETS, the operator of the CIBM trading system, and recognised offshore electronic trading access platforms, to facilitate investment by Hong Kong and overseas investors in eligible bonds traded on the CIBM (the "**Northbound Trading Link**" or "**Northbound Trading**"). A southbound trading link, facilitating investment in overseas bond markets by mainland Chinese investors is still under development but is intended to form part of Bond Connect once established.

##### **Eligible Securities**

Hong Kong and overseas investors will be able to conduct cash trading over the entire range of instruments traded on the CIBM, including products on both the secondary and primary markets.

##### **Trading Day**

Northbound investors are able to trade through Bond Connect on days upon which the CIBM is open to trade, regardless of whether they are a public holiday in Hong Kong.

##### **Settlement and Custody**

Settlement and custody of northbound bond trades under Bond Connect will be implemented under the link between the CMU of the HKMA and mainland China's two bond settlement systems, CCDC and SHCH. The CMU settles northbound trades and holds the CIBM bonds on behalf of members in nominee accounts with each of the CCDC and the SHCH. The CCDC and SHCH provide services to foreign investors, directly and indirectly, using Bond Connect.

Bonds purchased by Hong Kong and overseas investors are recorded in an omnibus nominee account at the CCDC and the SHCH in the name of the CMU. The CMU itself maintains the bonds in segregated sub-accounts of the relevant CMU members, who in turn may hold the bonds on their own account or on behalf of other investors or custodians. Accordingly, bonds purchased by Hong Kong and overseas purchasers through Bond Connect are held by the purchaser's global or local custodian in a segregated sub-account opened in their name at the CMU.

##### **Currency**

Hong Kong and overseas investors may trade through Bond Connect using offshore RMB (CNH) or by converting offshore currency into onshore RMB (CNY) under Bond Connect.

Where an investor uses offshore currency to invest through the Northbound Trading Link, it must open a segregated

RMB capital account with a Hong Kong RMB clearing bank or an eligible offshore RMB business participating bank (each an "**RMB Settlement Bank**") to convert its foreign currency into CNY. Where bonds are purchased in CNY in this manner, the proceeds of the sale must be converted back into the foreign currency upon sale of the bonds and remittance of the proceeds out of mainland China.

Investors using CNH to invest in bonds through Bond Connect do not need to appoint an RMB Settlement Bank, nor do they need to open a segregated RMB capital account.

### ***Bond Connect Specific Risks***

The Fund may invest through Bond Connect in eligible bonds traded on the CIBM, which subjects the Fund to risks including but not limited to:

#### ***Suspension Risks***

It is contemplated that the mainland Chinese authorities will reserve the right to suspend northbound and/or southbound trading of Bond Connect if necessary for ensuring an orderly and fair market and that risks are managed prudently. The relevant PRC government authority may also impose "circuit breakers" and other measures to halt or suspend Northbound Trading. Where a suspension in the Northbound Trading through the Bond Connect is effected, the Fund's ability to access the PRC bond market will be adversely affected.

#### ***Differences in Trading Day***

Northbound Trading through Bond Connect is able to be undertaken on days upon which the CIBM is open to trade, regardless of whether they are a public holiday in Hong Kong. Accordingly, it is possible that bonds traded through Bond Connect may be subject to fluctuation at times where the Fund is unable to buy or sell bonds, as its Hong Kong or globally-based intermediaries are not available to assist with trades. Accordingly, this may cause the Fund to be unable to realise gains, avoid losses or to benefit from an opportunity to invest in mainland Chinese bonds at an attractive price.

#### ***Operational Risk***

Bond Connect provides a channel for investors from Hong Kong and overseas to access the PRC bond markets directly.

The "connectivity" in Bond Connect requires routing of orders across the border, requiring development of new trading platforms and operational systems. There is no assurance that these platforms and systems will function properly (in particular, under extreme market conditions) or will continue to be adapted to changes and developments in both markets. In the event that the relevant systems fail to function properly, trading through Bond Connect may be disrupted. The Fund's ability to trade through Bond Connect (and therefore pursue its investment strategy) may therefore be adversely affected.

#### ***Not Protected by Investor Compensation Fund***

Investors should note that if the Fund engages in any Northbound Trading, the Fund will not be covered by Hong Kong's Investor Compensation Fund or the China Securities Investor Protection Fund and thus investors will not benefit from compensation under such schemes.

#### ***Currency Risk***

CIBM Bonds (as defined below) under Northbound Trading will be traded and settled in RMB. The non-RMB denominated Unit classes will be exposed to currency risk if the Fund invests in a RMB product due to the need for the conversion of the currency into RMB. The Fund will also incur currency conversion costs. Even if the price of the RMB asset remains the same when the Fund purchases it and when the Fund redeems / sells it, the Fund will still incur a loss when it converts the redemption / sale proceeds into local currency if RMB has depreciated. Also, as the Fund may either settle CIBM Bonds using CNH or by converting offshore currency into CNY, any divergence between CNH and CNY may adversely impact investors.

#### ***Regulatory Risk***

For the Fund's investment under Bond Connect, although there is no quota restriction, relevant information about the Fund's investments needs to be filed with Shanghai Head Office of PBOC and an updating filing may be required if there is any significant change to the filed information. It cannot be predicted whether Shanghai Head Office of PBOC will make any comments on or require any changes with respect to such information for the purpose of filing. If so required, the Fund will need to follow Shanghai Head Office of PBOC instructions and make the relevant changes accordingly, which, may not be in the best interests of the Fund and the Unitholders from a commercial perspective.

In addition, Bond Connect is novel in nature and will be subject to regulations promulgated by regulatory authorities



and implementation rules made by regulators in the PRC and Hong Kong. Further, new regulations may be promulgated from time to time by the regulators in connection with operations and cross-border legal enforcement in connection with cross-border trades under Bond Connect.

It should be noted that the regulations are untested and there is no certainty as to how they will be applied. Moreover, the current regulations are subject to change. There can be no assurance that Bond Connect will not be abolished. Where the Fund invests in the PRC markets through Bond Connect, it may be adversely affected as a result of such changes. In addition, Bond Connect and its technology and risk management capability has only a short operating history. There is no assurance that the systems and controls of the Bond Connect programme will function as intended or whether they will be adequate.

#### *Local Market Rules*

Under Bond Connect, bond issuers and trading of bonds traded on the CIBM (the "**CIBM Bonds**") are subject to market rules in the PRC. Any changes in laws, regulations and policies of the China bond market or rules in relation to Bond Connect may affect prices and liquidity of the relevant CIBM Bonds. Among others, the relevant information disclosure requirements applicable to the investors of the CIBM bonds will apply to the Fund (to the extent that it invests in the CIBM Bonds).

Moreover, PBOC, together with SAFE, will exercise on-going supervision of the Fund's trading of CIBM Bonds and may take relevant administrative actions such as suspension of trading and mandatory exit against the Fund and/or the Manager in the event of non-compliance with the local market rules.

#### *Nominee Holding Structure and Ownership*

CIBM Bonds which the Fund may invest in will be held by the CMU as the nominee holder, opening nominee account(s) with the CCDC and the SHCH respectively. While the distinct concepts of "nominee holder" and "beneficial owner" are generally recognised under the local regulations, the application of such rules is untested, and there is no assurance that PRC courts will recognise such rules, e.g. in liquidation proceedings of PRC companies or other legal proceedings.

In addition, CIBM Bonds are uncertificated and are held by CMU for its account holders. Physical deposit and withdrawal of CIBM Bonds are not available under the local regulations for the Fund.

#### *Risk of CMU / CCDC / SHCH Default*

A failure or delay by CMU, CCDC or SHCH in the performance of their respective obligations may result in a failure of settlement, or the loss, of CIBM Bonds and/or monies in connection with them and the Fund may suffer losses as a result. In the event that the nominee holder (i.e. CMU) becomes insolvent, such bonds may form part of the pool of assets of the nominee holder available for distribution to its creditors and the Fund, as a beneficial owner, may have no rights whatsoever in respect thereof.

#### *Risk of Third Party Default*

Under the prevailing applicable Bond Connect regulations, the Fund may participate in the Bond Connect through CEFTS, an onshore custody agent, CIBM settlement agent or other recognised third parties (as the case may be), who would be responsible for making the relevant filings and account opening with the relevant authorities. The Fund is therefore subject to the risk of default or errors on the part of such agents.

#### *Liquidity and Volatility*

Market volatility and potential lack of liquidity due to low trading volume of certain debt securities in the CIBM may result in prices of certain debt securities traded on such market fluctuating significantly. Where the Fund invests in such markets it will be subject to liquidity and volatility risks. The bid and offer spreads of the prices of such securities may be large, and the Fund may therefore incur significant trading and realisation costs and may even suffer losses when disposing of such investments.

#### *Hedging Activities*

Hedging activities under Bond Connect are subject to the local regulations and any prevailing market practice. There is no guarantee that the Fund will be able to carry out hedging transactions at terms which are satisfactory to the Manager and to the best interest of the Fund. The Fund may also be required to unwind its hedge in unfavourable market conditions.

#### *Settlement Risk*

Although delivery-versus-payment (DVP) settlement (e.g. simultaneous delivery of security and payment) is the dominant settlement method adopted by CCDC and SHCH for all bond transactions in the CIBM, there is no

assurance that settlement risks can be eliminated. In addition, DVP settlement practices in the PRC may differ from practices in developed markets. In particular, such settlement may not be instantaneous and be subject to a delay of a period of hours. Where the counterparty does not perform its obligations under a transaction or there is otherwise a failure due to CCDC or SHCH (as applicable), the Fund may sustain losses.

The above may not cover all risks related to Bond Connect and any above-mentioned laws, rules and regulations are subject to change and there is no assurance as to whether or how such changes or developments may restrict or affect the Fund's investments via Bond Connect.

#### *Taxation Risk*

Except for interest income from certain bonds (i.e. government bonds, local government bonds and railway bonds which are entitled to a 100% corporate income tax (CIT) exemption and 50% CIT exemption respectively in accordance with the Enterprise Income Tax Law, the Implementation Rules to the Enterprise Income Tax Law, a circular dated 6 February 2013 on the Circular on Exemption of Income Tax on interest income from Local Government Bonds, a circular dated 10 March 2016 on the Circular on Income Tax Policies on Interest Income from Railway Bonds under Caishui [2016] No. 30, and an announcement dated 16 April 2019 on the Announcement on Income Tax Policies on Interest Income from Railway Bonds under [2019] No. 57 by the Ministry of Finance of the People's Republic of China ("MOF") and the State Taxation Administration of the People's Republic of China ("STA")), interest income derived by non-resident institutional investors from other bonds traded through Bond Connect is PRC-sourced income and should be subject to PRC withholding income tax at a rate of 10% and value-added tax ("VAT") at a rate of 6%.

On 22 November 2018, the MOF and STA jointly issued Caishui [2018] No.108 ("**Notice No. 108**"), *the notice dated 7 November 2018 on the Taxation Policy of Corporate Income Tax and Value-Added Tax in relation to Bond Investments made by Offshore Institutions in Domestic Bond Market*, to clarify that foreign institutional investors (including foreign institutional investors under Bond Connect), who do not have an establishment or place in the PRC or the income so derived in the PRC is not connected with such establishment or place, are temporarily exempt from PRC withholding income tax and VAT with respect to bond interest income derived in the PRC bond market for the period from 7 November 2018 to 6 November 2021.

Pursuant to Article 7 of the Detailed Implementation Regulations of the PRC CIT Law (as defined below), where the property concerned is a movable property, the source of capital gain shall be determined according to the location of the enterprise, establishment or place which transfers the property. The PRC tax authorities have verbally indicated that debt instruments issued by PRC tax resident enterprises are movable property. In this case, the source shall be determined based on the location of the transferor. Capital gains derived by non-resident institutional investors (with no place or establishment or permanent establishment in the PRC) from the trading of bonds through the Bond Connect could be argued as non PRC-sourced income under the current CIT law and regulations, therefore, not subject to PRC CIT. As a matter of practice, the PRC tax authorities have not levied PRC WIT on capital gains realised by foreign investors from the trading of debt securities.

According to Caishui [2016] No. 70, *the Supplementary Notice of the Ministry of Finance and the State Taxation Administration on VAT Policies for Interbank Dealings of Financial Institutions*, gains derived by foreign institutions approved by PBOC from the investment in the inter-bank RMB markets (including currency market, bond market and derivative market) shall be exempt from VAT.

There is no guarantee that the temporary tax exemption or non-taxable treatment with respect to bonds traded via Bond Connect described above will continue to apply, will not be repealed and re-imposed retrospective, or that no new tax regulations and practice in China specifically relating to such programs will not be promulgated in the future. Such uncertainties may operate to the advantage or disadvantage of Unitholders in the Fund and may result in an increase or decrease in Net Asset Value of the Fund.

#### **B5. China Market Risk**

The Fund's investments may be concentrated in China. The value of the Fund may be more volatile than that of a fund having a more diverse portfolio of investments. The value of the Fund's assets may be affected by uncertainties such as economic and political developments, changes in government policies, taxation, foreign exchange controls, legal or regulatory events, liquidity, currency repatriation restrictions and restrictions on foreign investment in China. Accounting, auditing and reporting standards in China may not provide the same degree of investor protection or information to investors as would generally apply in more established securities markets. Furthermore, the legislative framework in China for the purchase and sale of investments and in relation to beneficial interests in those investments is relatively new and untested.

Both the Shanghai and Shenzhen securities markets are in the process of development and change. This may lead to trading volatility, difficulty in the settlement and recording of transactions and difficulty in interpreting and applying the relevant regulations.

Securities exchanges in China typically have the right to suspend or limit trading in any security traded on the relevant exchange. The government or the regulators may also implement policies that may affect the financial markets. All

these may have a negative impact on the Fund.

Under the prevailing tax policy in China, there are certain tax incentives available to foreign investment. There can be no assurance, however, that these tax incentives will not be abolished in the future.

Many of the PRC economic reforms are unprecedented or experimental and are subject to adjustment and modification, and such adjustment and modification may not always have a positive effect on investment in listed securities such as China A Shares.

The choice of China A Share issues/access products currently available to the Manager may be limited as compared with the choice available in other markets. There may also be a lower level of liquidity in the China A Share markets, which are relatively smaller in terms of both combined total market value and the number of China A Shares which are available for investment as compared with other markets. This could potentially lead to severe price volatility. High market volatility and potential settlement difficulties in the Chinese market may also result in significant fluctuations in the prices of the securities traded on such markets and thereby may adversely affect the value of the Fund.

The national regulatory and legal frameworks for capital markets and joint stock companies in the PRC are still developing when compared with those of developed countries. Currently, joint stock companies with listed China A Shares are undergoing split-share structure reform to convert state owned shares or legal person shares into transferable shares with the intention to increase liquidity of China A Shares. However, the effects of such reform on the A-Shares market remain to be seen.

Also, the PRC government's control of currency conversion and future movements in exchange rates may adversely affect the operations and financial results of the companies invested in by the Fund.

In light of the above mentioned factors, the price of China A Shares may fall significantly in certain circumstances.

The tax laws, regulations and practice in the PRC are constantly changing, and they may be changed with retrospective effect.

The Fund may invest directly in China A Shares via QFII/RQFII or the Stock Connects. The Fund may also invest indirectly in China A Shares by investing in open-ended collective investment schemes that have obtained access to China A Shares through QFII/RQFII, Stock Connects, or in equity linked or participation notes.

Under current rules in China, a single foreign investor's shareholding in a listed company or an National Equities Exchange and Quotations ("NEEQ")-admitted company is limited to 10% of the company's total shares. In addition, all foreign investors' shareholdings in the China A Shares of a listed company or in the domestically listed shares of an NEEQ-admitted company (whether through Stock Connects, QFII/RQFII) are not permitted in aggregate to exceed 30% of its total shares. If the aggregate foreign investors' shareholdings of China A Shares of a single issuer exceeds the 30% threshold, the foreign investors concerned will be requested to sell the shares on a last-in-first-out basis within five trading days. The Fund and its brokers are unlikely to have visibility on whether the Fund's investments will be subject to the force-sell requirements but when the aggregate shareholding of China A Shares of a single issuer held by all the foreign investors reaches or exceeds 26%, the relevant exchange (i.e. Shanghai Stock Exchange or Shenzhen Stock Exchange) will publish on its official website the aggregate shareholding held by all foreign investors in respect of a particular issuer. Where the Fund is subject to a forced sale of its China A Shares, it may not be able to sell the China A Shares at an advantageous price and the Fund's Net Asset Value may be adversely impacted.

Based on professional and independent tax advice, the Manager currently does not intend to make any provision for PRC taxes in relation to the Fund's investments in any securities that are linked to the China markets. If such PRC taxes are imposed on the Fund, such taxes may be deducted from the Net Asset Value of the Fund and accordingly the Net Asset Value of the Fund may be adversely impacted and investors may as a result suffer loss.

#### **B6. *Reliability of Credit Ratings***

The ratings of fixed-income securities by institutions such as Moody's and Standard & Poor's are a generally accepted barometer of credit risk. They are, however, subject to certain limitations from an investor's standpoint and do not guarantee the creditworthiness of the security and/or issuer at all times. The rating of an issuer is heavily weighted by past developments and does not necessarily reflect probable future conditions. There is frequently a lag between the time the rating is assigned and the time it is updated. In addition, there may be varying degrees of difference in the credit risk of securities within each rating category. As a result, the ratings do not guarantee the creditworthiness of the security and/or issuer at all times.

In determining the credit quality of the debt securities in which the Fund invests, the credit ratings provided by the relevant rating agencies only serve as a point of reference. The Manager conducts its own independent assessment based on its internal credit research and assign an internal credit rating to each issuer, which is independent of any external credit rating. The Manager's credit research process aims to ensure that all debt securities in the Fund's



portfolio are of the relevant credit quality prescribed in its investment policy.

**B7. *Downgrading Risk***

The credit rating of a debt instrument or its issuer may subsequently be downgraded. In the event of such downgrading, the value of the Fund may be adversely affected. The Manager may or may not be able to dispose of the debt instruments that are being downgraded.

**B8. *Interest Rate Risk***

The Fund invests in fixed income securities and the value of the Fund's investments fluctuates in response to movements in interest rates. If rates go up, the value of debt securities fall; if rates go down, the value of debt securities rise. Bonds with longer maturities tend to be more sensitive to interest rate movements than those with shorter maturities. Periods of high interest rates and recession may adversely affect the issuer's ability to pay interest and principal, and to obtain additional business.

**B9. *High Yield Risk***

To the extent that the Fund invests in lower-rated debt securities, these securities, while usually offering higher yields, generally have more risk and volatility than high-rated securities, because of reduced credit worthiness, liquidity and greater chance of default.

**B10. *Small Capitalisation/Mid-Capitalisation Companies Risk***

Insofar as the Fund invests in smaller companies, Unitholders should note that investments in securities in small-capitalisation/mid-capitalisation companies may provide the potential for higher returns, but also involve additional risks. The stock of small-capitalisation/mid-capitalisation companies may have lower liquidity and their prices are more volatile to adverse economic developments than those of larger capitalisation companies in general.

**B11. *Investments in Unlisted Collective Investment Schemes***

The Fund may invest up to 10% of its Net Asset Value in other collective investment schemes which are non-eligible schemes and not authorised by the SFC. These schemes may be unregulated and as a consequence may have different characteristics to an SFC-authorised fund such as, for example, in relation to their investment policies, investment restrictions, diversification requirements, liquidity, borrowing and leverage. There may be additional costs involved when investing into these underlying collective investment schemes. In addition, there is also no guarantee that the underlying collective investment schemes will always have sufficient liquidity to meet the Fund's redemption requests as and when made. The underlying scheme may itself impose a restriction on the redemption of its shares in circumstances where the redemption requests it receives exceed a certain threshold or percentage of its shares in issue on a particular dealing day. The imposition of such a restriction by the underlying scheme may affect the Fund's ability to realise its investment in that scheme in a timely manner.

Moreover, the Fund will be subject to the risks associated with the underlying funds. The Fund does not have control of the investments of the underlying funds and there is no assurance that the investment objective and strategy of the underlying funds will be successfully achieved which may have a negative impact to the Net Asset Value of the Fund.

**B12. *Below Investment Grade and Unrated Debt Securities Risk***

The Fund may invest in securities which are below investment grade or which are unrated. These securities are speculative and involve a greater risk of default and price changes than investment grade debt securities due to changes in the issuer's creditworthiness. Low rated debt securities generally offer a higher current yield than higher grade issues. However, the market prices of these securities fluctuate more than investment grade debt securities and may decline significantly in periods of general economic difficulty. The market for lower rated debt securities may not be liquid at all times. In a relatively illiquid market the Fund may not be able to acquire or dispose of such securities quickly and as such the Fund may experience volatile price movements upon liquidation of its investments. Settlement of transactions may be subject to delay and administrative uncertainties. There is a greater risk of loss of principal and interest than high-rated debt securities.

**B13. *Risks of investing convertible bonds***

Convertible bonds are a hybrid between debt and equity, permitting holders to convert into shares in the company issuing the bond at a specified future date. As such, convertibles will be exposed to equity movement and greater volatility than straight bond investments. Investments in convertible bonds are subject to the same interest rate risk, credit risk, liquidity risk and prepayment risk associated with comparable straight bond investments.

**B14. *Sovereign Debt Risk***

The Fund may invest in debt securities issued or guaranteed by governmental entities or their agencies. The Fund's investments may be exposed to political, social and economic risks. In adverse situations, sovereign debt issuers may not be able or willing to repay the principal and/or interest when due or may request the Fund to participate in the rescheduling of such debts and to extend further loans to sovereign debt issuers. The Fund may suffer significant losses when there is a default of sovereign debt issuers.

If the government debtor defaults, the Fund may have limited legal recourse against the issuer and/or guarantor. There is no assurance that the sovereign debts for which the relevant government debtor has defaulted may be collected in whole or in part.

**B15. *Risks associated with investments in Asia***

The Fund's investments are concentrated in Asia. The value of the Fund may be more volatile than that of a fund having a more diverse portfolio of investments. The value of the Fund's assets may be affected by uncertainties such as economic and political developments, changes in government policies, liquidity, taxation, legal or regulatory events, foreign exchange, currency repatriation restrictions and restrictions on foreign investment in Asia. Accounting, auditing and reporting standards in certain Asian countries may not provide the same degree of investor protection or information to investors as would generally apply in more established securities markets. Furthermore, the legal framework in certain countries in Asia for the purchase and sale of investments and in relation to beneficial interests in those investments is relatively new and untested.

**B16. *Equity Risk***

The values of equity securities may decline due to general market conditions (e.g. adverse political and economic conditions, changes in interest or currency rates etc) which are not specifically related to a particular company or due to factors which affect particular industries (e.g. changes in investment sentiment, issuer-specific factors etc). Equity securities generally have greater price volatility than debt securities.

**B17. *Payment of Distributions Out of Capital***

Investors should note that the payment of distributions out of capital amounts to a return or withdrawal of part of the amount they originally invested in the Fund or from any capital gains attributable to that original investments. Any such distributions may result in an immediate reduction of the Net Asset Value per Unit. Accordingly, the receipt of a distribution may not indicate that the Fund has made profits, whether of a capital or income nature. Investors should refer to the section headed "Distribution Policy" hereunder for further details.

**B18. *Investment in Participation Notes and/or Equity Linked Notes***

Participation notes and equity linked notes are subject to the terms and conditions imposed by their issuers. These terms may lead to delays in implementing the Manager's investment strategy due to the restrictions they may place on the issuer acquiring or disposing of the securities underlying the participation notes and equity linked notes, or on the implementation of redemptions and payment of redemption proceeds to the Fund. Investment in participation notes and equity linked notes can be illiquid as there is no active market in participation notes and equity linked notes. In order to meet realisation requests, the Fund relies upon the counterparty issuing the participation notes and equity linked notes to quote a price to unwind any part of the participation notes and equity linked notes. This price will reflect the market liquidity conditions and the size of the transaction.

The policy and regulations imposed by the PRC government on the access into the China A Shares markets are subject to change and any such change may adversely impact the issuance of participation notes and equity linked notes invested by the Fund. Investment in China A Share markets by foreign institutional investors via QFII/RQFII is subject to the applicable laws, rules and regulations (including restrictions on investments and regulations on repatriation of principal and profits) in the PRC, which are subject to change and such change may have potential retrospective effect.

Investors should note that there can be no assurance that the Fund may be able to maintain or obtain a sufficient investment in participation notes and equity linked notes. This may have an impact on the investors' investment in the Fund. The participation note and equity linked notes issuer may cease to extend the duration of any participation notes or to issue further participation notes and equity linked notes for any reasons (such as the relevant licence is cancelled), and in such cases the Fund may be required to dispose of its existing participation notes and equity linked notes.

Further, the Fund will be exposed to the counterparty risk associated with each participation note and equity linked note issuer. Because a participation note or equity linked note is a payment obligation of the participation note and equity linked note issuer, rather than a direct investment in China A Shares, the Fund may suffer losses potentially equal to the full value of the participation notes and equity linked notes if the participation note and equity linked note issuer were to become insolvent or failed to perform its payment obligations under the participation notes and equity linked notes.

**B19. Risks of Investing in China A Shares and other eligible PRC securities and futures via QFII/RQFII**

Under prevailing regulatory rules, a QFII/RQFII holder may invest in eligible PRC securities and futures based on its needs of investment and will not be subject to any quota limit.

The Fund can also gain exposure to China A Shares by investing in other collective investment schemes (each, for the purpose of this risk factor, an “**Other Scheme**”) which invests in China A Shares via the QFII/RQFII.

**General China A Shares Risks**

Exposure to China A Shares involves the taking of certain risks which are inherent in such an investment, including the following:

*Uncertainty on the applicable regulations:* Investments in China A Shares and other eligible securities and futures are subject to certain rules and regulations which are promulgated by the Government of the PRC. These rules and regulations may be applied inconsistently or not at all and are subject to change at any time. Such change may have potential retrospective effect. There is no assurance that any future changes in the rules and regulations or their interpretation or their enforcement will not have a material adverse effect on the Fund’s investments in the PRC.

*Risks relating to suspension of the PRC stock markets:* Securities exchanges in the PRC typically have the right to suspend or limit trading in any security traded on the relevant exchange. In particular, trading band limits are imposed by the stock exchanges on China A Shares, whereby trading in any China A Shares on the relevant stock exchange may be suspended if the trading price of the security fluctuates beyond the trading band limit. Such a suspension would make any dealing with the existing positions impossible and would potentially expose the Fund to losses. Further, when the suspension is subsequently lifted, it may not be possible for the Fund to liquidate positions at a favourable price, which could also entail losses for the Fund.

**Risks Specific to Direct Investments in China A Shares and other eligible PRC securities and futures via QFII/RQFII**

*Risks associated with QFII/RQFII rules and regulations:* Pursuant to the “Provisions on the Administration of Funds of Foreign Institutional Investors for Domestic Securities and Futures Investment” jointly issued by the SAFE and the PBOC on 7 May 2020, which took effect on 6 June 2020 (“Funds Administration Provisions”). On 25 September 2020, the CSRC, PBOC and SAFE jointly issued the Measures for the Administration of Domestic Securities and Futures Investment by QFII and RQFII (“QFII/RQFII Measures”) and the Provisions on Issues Concerning the Implementation of the Measures for the Administration of Domestic Securities and Futures Investment by QFII and RQFII (“QFII/RQFII Provisions”), which took effect from 1 November 2020. Pursuant to the Provisions, a QFII/RQFII holder may freely choose the timing and currency in which investment capital will be remitted into China, which can be in offshore RMB and/or foreign currency based on its investment plan and the process for routine remittance and repatriations has been further simplified. According to the QFII/RQFII Measures and QFII/RQFII Provisions, the QFII and RQFII regimes have been merged and are regulated by the same set of regulations including eligibilities requirements and ongoing operations.

However, applicable laws, QFII/RQFII rules and regulations (including restrictions on investments and regulations on repatriation of principal and profits) under which the Fund will invest in the PRC via the QFII/RQFII give the CSRC, the PBOC and the SAFE wide discretion on their interpretation. There are no precedents on how such discretion might be exercised for issues that have not been clearly provided for in the QFII/RQFII regulations, therefore leaving a considerable amount of uncertainty. The QFII/RQFII regulations are undergoing continual change: they may therefore be subject to further revisions in the future, and there is no assurance that such revisions would not prejudice QFIIs/RQFIIs, or have any potential retrospective effect. As a result, this may affect the Fund’s ability to make the relevant investments or to fully implement or pursue its investment objective and strategy. The CSRC, the PBOC and/or SAFE may have power in the future to impose new restrictions or conditions on or terminate a QFII/RQFII holder’s QFII/RQFII status or determine that the Fund is no longer permitted to operate under the QFII/RQFII which may adversely affect the Fund and its Unitholders. It is not possible to predict how such changes would affect the Fund.

The prevailing rules and regulations governing QFII/RQFII holders may impose certain restrictions/requirements on the types of investments and regulations on remittance as well as on the repatriation of principal and profits in relation to investments made by or through QFII/RQFII, which may restrict or affect the Fund’s investments. For remittance of foreign currencies, a QFII/RQFII holder shall open foreign exchange account(s) for the remitted funds in foreign currencies and a corresponding RMB special deposit account for each relevant foreign exchange account; for remittance of offshore RMB funds, a QFII/RQFII holder shall open RMB special deposit account(s) for the remitted funds in offshore RMB.

Repatriations of funds conducted by QFII/RQFII holders are not subject to any lock-up periods, or prior approval, although authenticity and compliance reviews will be conducted, and monthly reports on remittances and

repatriations will be submitted to SAFE by the PRC custodian(s). The Funds Administration Provisions allow QFII/RQFII holders to repatriate funds according to their own investment requirements. To repatriate profits, the QFII/RQFII holder only needs to provide its PRC custodian(s) with a written application or repatriation order. There is no assurance, however, that PRC rules and regulations will not change or that repatriation restrictions will not be imposed again in the future. Any restrictions on repatriation of the invested capital and net profits may impact on the Fund's ability to meet redemption requests made by the Unitholders.

*Liquidity Risks:* Under the Funds Administration Provisions, a QFII/RQFII holder shall appoint the PRC custodian(s) to handle the formalities for repatriation of the principal and/or profits with no limits, provided that funds that the QFII/RQFII holder remits in and out of PRC for domestic securities and futures investment shall be denominated in the same currency. However, the repatriation of monies conducted by a QFII/RQFII holder is still subject to relevant reporting requirements, authenticity and compliance reviews by PRC custodian(s), and the supervision and administration by SAFE. Further, as mentioned above, the QFII/RQFII regulations are subject to uncertainty in the application of their provisions. The QFII/RQFII regulations and/or the approach adopted in relation to the repatriation limit may change from time to time (although removed for now). If the repatriation limit is imposed in the future, a repatriation of principal and/or profits over and above the limit may require approval from SAFE which may delay payment of redemption proceeds; there is no assurance that such approval will be granted, and redemption of Units may be adversely affected.

Any future restrictions on the repatriation of principal and profits imposed by the QFII/RQFII regulations may have an adverse impact on the liquidity of the Fund's portfolio. In such circumstances the Manager will nevertheless ensure that the overall liquidity of the Fund's portfolio is maintained.

Furthermore, as the PRC custodian(s)' review on authenticity and compliance is conducted on repatriation, under certain circumstances, repatriation may be delayed or even rejected by the PRC custodian(s) in cases of non-compliance with the relevant regulations. In such a case, there may be an impact on the Fund's ability to meet redemption requests in a timely manner. It should be noted that the actual time required for the completion of any repatriation will be beyond the Fund's control.

QFII/RQFII holders may carry out foreign exchange derivatives investments through qualified custodians or PRC financial institutions to hedge their foreign exchange risk exposure incurred from its China A Shares or other eligible securities investments. The foreign exchange derivatives positions held by a QFII/RQFII holder shall not exceed the RMB assets size corresponding to its domestic securities investments at the end of the preceding month. The QFII/RQFII holder shall inform its main PRC custodian its foreign exchanges derivatives positions or overall positions. Foreign exchanges derivatives positions may be adjusted based on the month-end RMB assets size every month within 5 days after the end of each month. Please note that if the PRC custodian(s) violate relevant foreign exchange administration rules when assisting the QFII/RQFII holder in the derivatives investments or fail to monitor and assess the RMB assets size of the QFII/RQFII holder's domestic securities investments, the SAFE will impose relevant sanctions on the PRC custodian(s) and therefore may affect the foreign exchange derivatives investments of the QFII/RQFII holder.

Moreover, pursuant to the Funds Administration Provisions, where a QFII/RQFII holder needs to open only one RMB bank settlement account in the PRC, it may directly open the special RMB deposit account, and where a QFII/RQFII holder needs to open several RMB bank settlement accounts for its proprietary funds, client funds, and open-end fund products, it shall open both basic RMB deposit account and special RMB deposit account. The special RMB deposit accounts which contain securities transaction account(s) and domestic derivatives account(s) shall be opened by PRC custodian(s) or by futures margin depository bank, qualified custodian or domestic financial institution or other relevant institution for QFII/RQFII holders and the funds in different securities transaction accounts opened for one same product/capital (self-owned funds, client funds, open-ended fund) of a QFII/RQFII holder can be transferred from one to another. Investors should also note that there can be no assurance that the QFII/RQFII holder will continue to maintain the QFII/RQFII status to achieve the investment objective and policy of the Fund, or that redemption requests can be processed in a timely manner in the case of adverse changes in relevant laws or regulations. Such restrictions may result in a rejection of applications for subscriptions or a suspension of dealings of the Fund. In extreme circumstances, the Fund may incur significant losses due to limited investment capabilities, or may not be able to fully implement or pursue its investment objective or strategy, due to the failure to obtain/maintain or the restrictions that apply in respect of the QFII/RQFII status.

*Dependence on the QFII/RQFII holder:* To gain direct exposure to the China A Shares and other eligible securities and futures, the Fund is dependent on the QFII/RQFII licence and subject to certain investment discretion of the QFII/RQFII holder.

The QFII/RQFII holder's licence may be revoked or terminated or otherwise invalidated at any time by reason of a change in applicable law, regulations, practice or other circumstances, an act or omission of the QFII/RQFII holder or for any other reasons. In such event, the Fund may no longer be able to invest directly into China A Shares and other eligible securities and futures via the QFII/RQFII. The Fund may also be prohibited from trading of these securities and all assets held by the relevant PRC custodian(s) for the account of the Fund will be liquidated and repatriated in accordance with applicable laws and regulations; this may lead to significant losses to the Fund and there may be delays in the payment of the amount invested in China A Shares and other eligible securities and



futures.

Investors should be aware that the QFII/RQFII regulations generally apply to the QFII/RQFII holder as a whole and not solely in relation to the investments made by the Fund: the Fund may therefore be adversely affected for reasons due to the investment of the Other Schemes in China A Shares via the relevant QFII/RQFII holder (for example, the Fund could be exposed to particular disclosure requirements or suffer from regulatory action linked to a breach of the QFII/RQFII regulations by the relevant QFII/RQFII holder).

The Fund may also suffer substantial losses if any of the key operators or parties (including the PRC custodian(s)/brokers) is bankrupt/in default and/or is disqualified from performing its obligations (including execution or settlement of any transaction or transfer of monies or securities).

CSRC, SAFE and PBOC are vested with the power to impose regulatory sanctions if the QFII/RQFII holder or the PRC custodian(s) violate any provision of the QFII/RQFII regulations. Any violations could result in the revocation of the QFII/RQFII holder's licence or other regulatory sanctions and may adversely impact the investment of the Fund.

*Currency risk:* The Renminbi is not, as of the date of this Explanatory Memorandum, a freely convertible currency, and is subject to the foreign exchange control policies of the PRC government.

Direct investments by the Fund in China A Shares are made through the QFII/RQFII in Renminbi, and the Fund will therefore be exposed to any fluctuation in the exchange rate between the base currency of the Fund and the Renminbi in respect of such investment. The Fund may also be adversely affected by controls of currency conversions by the PRC government.

For the purposes of investment through QFII/RQFII in foreign currencies, such foreign currency shall be tradable on the China foreign exchange market and will be exchangeable into Renminbi at prevailing market rates and vice versa. The Fund will be subject to bid/offer spread on currency conversion and transaction costs. Such foreign exchange risk and costs of conversion may result in losses to the Fund. There can be no assurance that the Renminbi will not be subject to devaluation or revaluation or that shortages in the availability of foreign currency will not develop.

*Custody risks:* China A Shares traded on the Shanghai and Shenzhen Stock Exchanges are dealt and held in dematerialized form through the China Securities Depository and Clearing Corporation Limited ("CSDCC"). Securities purchased on behalf of the Fund via the QFII/RQFII are required to be recorded by CSDCC as credited to a securities trading account maintained in the joint names of the QFII/RQFII holder and the Fund. As a matter of PRC law, the QFII/RQFII holder should have no ownership interest in the securities and the Fund should be ultimately and exclusively entitled to ownership of the securities. However, given that the QFII/RQFII holder belongs to a group of companies, there is a risk that creditors of the group may incorrectly assume that the Fund's assets belong to the group or to the QFII/RQFII holder and such creditors may seek to gain control of such Fund's assets to meet the liabilities of the QFII/RQFII holder or its group.

The evidence of title of exchange-traded securities in the PRC consists only of electronic book-entries in the depository and/or registry associated with the exchange. These arrangements of the depositories and registries are new and not fully tested in regard to their efficiency, accuracy and security.

In the event that there is an over-purchase of PRC securities by the Fund, the CSDCC may require collateral from the Fund's securities trading account. It is possible that the PRC custodian(s) may also be required by law to select and provide CSDCC with PRC securities from the securities account as collateral for the over-purchase of a party other than the Fund and investors should note that the Fund's assets may be so provided to the CSDCC.

Investors should note that cash deposited in the cash account of the Fund with the PRC custodian(s) will not be segregated but will be a debt owed from that custodian to the QFII/RQFII holder on behalf of the Fund as a custodian. Such cash will be co-mingled with cash belonging to other clients of the PRC custodian(s). In the event of bankruptcy or liquidation of a PRC custodian, the Fund will not have any proprietary rights to the cash deposited in such cash account, and the Fund will become an unsecured creditor, ranking *pari passu* with all other unsecured creditors of the PRC custodian(s). The Fund may face difficulty and/or encounter delays in recovering such debt, or may not be able to recover it in full or at all, in which case the Fund will suffer losses.

*PRC Brokers and Best Execution:* The Fund may have difficulty in consistently obtaining best execution for all transactions in China A Shares or other eligible securities and futures as a consequence of restrictions/limitations under applicable QFII/RQFII regulations or operational constraints. The Fund will use one or more PRC brokers appointed to execute transactions in the PRC markets for the account of the Fund. If a PRC broker offers the standards of execution which the QFII/RQFII holder reasonably believes to be amongst best practice in the PRC marketplace, the QFII/RQFII holder may determine that it should consistently execute transactions with that PRC broker (including where it is an affiliate) notwithstanding that such transactions may not be executed at the best price and such PRC brokers shall have no liability to account to the Fund in respect of the difference between the price at which the relevant transactions have been executed and any other price that may have been available in the market at that relevant time. There can be no guarantee that the execution of transactions will be at the best price available or that best execution of all transactions can be achieved.

**Disclosure of Interests and Short Swing Profit Rule:** Under the PRC disclosure of interests requirements, the Fund may be deemed to be acting in concert with other investors (for example, funds managed within the Manager's group) and may be subject to the risk that the Fund's holdings may have to be reported in aggregate with the holdings of such other funds should the aggregate holding trigger the reporting threshold under the PRC law, currently being 5% of the total issued shares with voting rights of the relevant PRC listed company. Within three days of such event, the QFII/RQFII holder is required to report to the CSRC and the relevant securities exchange, notify the relevant PRC listed company and make a public announcement. The Fund shall not purchase or sell the shares of the relevant PRC listed company within such period, unless otherwise stipulated by the CSRC.

In addition, in the event the aggregate holding of the first 5% further increases or decreases by 1%, the QFII/RQFII holder is required to further notify the relevant PRC listed company and make a public announcement on the day following the occurrence of such event; and in the event the aggregate holding of the first 5% further increases or decreases by 5%, the QFII/RQFII holder is required to report to the CSRC and the relevant securities exchange, notify the relevant PRC listed company and make a public announcement within three days upon the occurrence of such event, and the Fund shall not purchase or sell the shares of the relevant PRC listed company from the day when the event occurs to the end of three days after the public announcement is made, unless otherwise stipulated by the CSRC.

The above obligations may expose the Fund's holdings to the public which may have an adverse impact on the Fund.

In addition, subject to the interpretation of PRC courts and PRC regulators, the operation of the PRC short swing profit rule may be applicable to the Fund's investments with the result that where the holdings of the Fund (possibly in aggregate with the holdings of other investors deemed as persons acting in concert with the Fund) reach 5% or more of the total shares in issue of a PRC listed company, the Fund may not profit from selling shares or other securities with equity features (such as depositary receipts) of that company within six months of acquiring the same, or buying such shares or securities with equity features back within six months of selling the same.

**Investment Restrictions:** There are limits on the total number of China A Shares held by all foreign investors in one PRC listed company or a NEEQ-admitted company and so the capacity of the Fund to make investments in China A Shares will be affected by the activities of all other foreign investors investing through the QFII/RQFII or Stock Connects.

In particular, the Fund, by obtaining exposure to the PRC securities markets via the QFII/RQFII, is subject to the following restrictions:

- (a) the shareholding of a single foreign investor (such as the QFII/RQFII holder on behalf of the Fund), who invests via the QFII/RQFII and/or Stock Connects in a single listed company, cannot exceed 10% of the total shares in such company;
- (b) the aggregate shareholding of China A Shares by all foreign investors, who invest via the QFII/RQFII and/or Stock Connects in a single listed company, cannot exceed 30% of the total shares in such company.

**PRC Taxation Risk:** In November 2014, the Chinese authorities released a statement confirming that foreign investors will not be subject to CIT in the PRC on capital gains derived from the trading of shares and other equity interest investments through the QFII licence or RQFII licence on or after 17 November 2014. This is on the basis that the QFII/RQFII holder is without an establishment or place in the PRC or having an establishment or place in the PRC but the income so derived in the PRC is not effectively connected with such establishment or place. This is a temporary exemption with no indication of an expiry date therefore there can be no certainty that China A Shares will not attract a liability to tax in the future. This tax may be levied on any capital gain that such China A Shares have or on any other aspect of such China A Shares. There can be no certainty of the level of tax which will apply or the period in respect of which it will be levied.

The QFII/RQFII holder may retain an amount from the performance of such China A Shares to be able to satisfy any such liability in the event that a tax liability arises, however any level of provision (or no provision) may be inadequate to meet the PRC tax liabilities that may arise.

Having consulted professional and independent tax advisors, the Fund does not currently make any tax provision to cover any potential capital gains tax liability.

There are risks and uncertainties associated with the current PRC tax laws, regulations and practice in respect of capital gains realised via QFII/RQFII on the Fund's investments in the PRC (which are subject to change and may have retrospective effect). Any increased tax liabilities on the Fund may adversely affect the Fund's value.

Investors should seek their own tax advice on their tax position with regard to their investment in the Fund, including the possible implications of capital gain tax in the PRC.

***Risks Specific to Indirect Investment in China A Shares via an Other Scheme***

The above restrictions imposed on QFII/RQFII holders by the PRC government may have an adverse effect on an Other Scheme's liquidity and performance. Accordingly, the Trust, the Fund or the Other Scheme itself may not be able to sell or decrease exposure to China A Shares or other eligible securities and futures in which the Other Scheme has invested even in the event that it wishes to do so.

### **Conflicts of Interest**

Due to the investment restrictions under prevailing PRC rules (such as foreign shareholding limits), there may be conflicting interests in terms of the investments of the Fund, Other Scheme and any other clients of the Manager and any other affiliate. However, in accordance with its conflicts of interest policy, the Manager and any other affiliate will endeavour to act in the best interests of the Fund so far as practicable, having regard to its obligations to other clients in the event that any such conflict arises.

#### **B20. Risks associated with RMB Class of Units**

Investors may invest in a Class of Units which is denominated in RMB ("**RMB Class**"). It should be noted that the RMB is currently not a freely convertible currency as it is subject to foreign exchange control policies and restrictions of the PRC government. The PRC government's policies on exchange control and repatriation restrictions are subject to change and the investors' investment in the RMB Class of Units may be adversely affected. In this connection, please also refer to the "RMB currency and conversion risk" under the risk factor "B1. Emerging Markets Risks".

As the RMB Class is non-hedged, depending on the exchange rate movements of RMB relative to the base currency of the Fund and/or other currencies of the non-RMB-denominated underlying investments of the Fund, (i) investors may still suffer losses even if there are gains or no losses in the value of the non-RMB-denominated underlying investments; or (ii) investors may suffer additional losses if the non-RMB-denominated underlying investments of the Fund fall in value.

#### **B21. Risks associated with Collateral Management**

The Fund may receive collateral from a counterparty to an OTC derivative transaction in order to reduce its counterparty risk exposure, subject to the investment restrictions and requirements applicable to collateral under Schedule 1 to this Explanatory Memorandum. As provided under Schedule 2 to this Explanatory Memorandum, the Manager currently intends to receive cash-only collateral from a counterparty to any OTC derivative transaction entered into in respect of the Fund.

**Counterparty risk:** Only a portion of the invested amount in an OTC derivative transaction will be covered by cash collateral to be received by the Fund. While the taking of collateral may reduce counterparty risk, it does not eliminate it entirely. The Fund is still subject to the risk that the value of collateral held by the Fund may not be sufficient to cover the Fund's exposure to an insolvent counterparty.

**Operational risk:** The operational process of managing the collateral (e.g. dealing with collateral movements, monitoring the exposure and performing valuations) may expose the Fund to risks, which can result in a failure to request collateral to cover the exposure of the Fund or, where collateral is provided by the Fund to the relevant counterparty, failure to demand the return of collateral from a counterparty when due. In addition, the Fund is subject to the risk that the relevant legal arrangements in relation to the collateral received by the Fund are held to be unenforceable in the courts of the relevant jurisdiction. As a result, the Fund may be unable to enforce its rights over the collateral received in the case of a counterparty failure.

**Custody risk:** As any cash collateral received by the Fund from a counterparty in respect of an OTC derivative transaction will be held in custody by the Trustee or a Correspondent (as defined under the sub-section "Trustee and Registrar" of the section "MANAGEMENT AND ADMINISTRATION below), it will be subject to custody risk where the Fund may be unable to enforce the cash collateral in case of liquidation, bankruptcy or insolvency of the Trustee or a Correspondent. Please also refer to "A14. Custody risk" above for details.

#### **B22. Risks associated with the ChiNext market and/or the Science and Technology Innovation Board (STAR board)**

The Fund may invest in the ChiNext market of the SZSE and/or the STAR board of the SSE. Investments in the ChiNext market and/or the STAR board may result in significant losses for the Fund and its investors. The following additional risks apply:

- **Higher fluctuation on stock prices and liquidity risk:** Listed companies on the ChiNext market and/or the STAR board are usually of emerging nature with smaller operating scale. Listed companies on the ChiNext market and STAR board are subject to wider price fluctuation limits, and due to higher entry thresholds for investors, such listed companies may have limited liquidity, compared to other boards. Hence, they are subject to higher fluctuation in stock prices and liquidity risks and have higher risks and turnover ratios than companies listed

on the main board of the SZSE and/or the SSE.

- *Over-valuation risk:* Stocks listed on the ChiNext market and/or the STAR board may be overvalued and such exceptionally high valuation may not be sustainable. The stock price may be more susceptible to manipulation due to fewer circulating shares.
- *Differences in regulations:* The rules and regulations regarding companies listed on the ChiNext market and/or the STAR board are less stringent in terms of profitability and share capital than those in the main boards of the SZSE and/or the SSE.
- *Delisting risk:* It may be more common and faster for companies listed on the ChiNext market and/or the STAR board to delist compared to companies listed on the main board of the SZSE and/or the SSE. The ChiNext market and STAR board have stricter criteria for delisting compared to other boards. This may have an adverse impact on the Fund if the companies that it invests in are delisted.
- *Concentration risk (for the STAR board):* The STAR board is a newly established board and may have a limited number of listed companies during the initial stage. Investments in the STAR board may be concentrated in a small number of stocks and subject the Fund to higher concentration risk.

### B23. LIBOR Risk

The London Interbank Offered Rate (typically referred to as “LIBOR”) is one of the most commonly used interest rate benchmarks in global financial markets. A major transition is currently underway across the financial industry to switch from LIBOR to alternative near Risk-Free-Rates (“RFRs”). The publication of LIBOR is expected to cease by the end of 2021.

Interest rate benchmarks, such as LIBOR, are used to determine the interest rate payable on a large number of loans, bonds, derivatives and many other financial contracts and investments, and certain funds use LIBOR as a benchmark in their investment objectives, performance fee calculations, asset allocation models and comparators. The LIBOR rate is also relied on by financial firms from an operational perspective, including in valuation curves, stress testing, pricing and asset allocation models.

There are a large number of potential risks arising from LIBOR transition. Existing LIBOR-referencing positions within the Fund may become illiquid as the end-2021 deadline gets closer and their functioning and value may be impacted. It may also not be possible to transition certain assets from LIBOR to the new RFRs, which is particularly the case for assets issued to multiple investors (for example bonds paying a LIBOR-based return). Where the Fund is just one investor among many in a financial asset, the Fund is unlikely to be able to control the timing of transition. Delays in obtaining investor, bank, broker or other counterparty consents, or regulatory approvals, may also delay transition. If an asset for whatever reason continues to reference LIBOR when the rate ceases to be published, that asset will no longer function as originally intended, its price may be negatively affected and it may become hard to value.

Transitioning existing assets away from LIBOR to RFRs, however, may lead to the Fund paying more or receiving less on that asset than if it had remained a LIBOR-referencing asset. Adjustments to the RFRs to reflect their historic difference to LIBOR are relatively untested and it is not yet clear how closely the adjusted RFR will perform against the equivalent LIBOR rate. Some of the RFRs are also relatively recent benchmarks when compared with LIBOR and how these rates will perform in stressed market conditions or over a significant period is not well established.

Solutions for transition across different asset classes and currencies are not necessarily aligned and are developing at different rates. There is a risk of a timing mismatch between the remediation (if possible) of an underlying asset and its associated risk-reducing trade (known as a hedge), if one is remediated before the other. Likewise, if remediation results in a different legal, commercial, tax, accounting or other economic outcome, there is a risk of detriment to the Fund.

Operational systems and administrative procedures will need to be updated to accommodate the RFRs, including from a valuation, pricing and risk management perspective. There is a risk that the timing for these updates, some of which may involve third party systems or software, will not take place sufficiently quickly to meet project milestones and expectations.

For new investments, including where an existing LIBOR-asset is sold and replaced with an RFR-referencing asset, the market in the relevant RFR-referencing asset may lack liquidity and/or price transparency, particularly compared with historical LIBOR volumes. If a large number of LIBOR-referencing assets are remediated at once there is a risk that transaction reporting systems will become overwhelmed. There is also a risk that transitioning away from LIBOR may in certain instances trigger other regulatory obligations such as clearing or margining. Several of the RFRs are relatively new benchmark interest rates and so historic long-term data on how they will perform is not available. Consequently, the performance of certain RFRs in stressed market conditions is unclear.

Other IBOR benchmarks are also affected by global benchmark reforms, including TIBOR, HIBOR, EONIA, CDOR and BBSW. The timings for transition from such rates varies but the broad risks set out in this section apply generally



to other affected IBOR rates.

## **INVESTMENT AND BORROWING RESTRICTIONS**

The Trust Deed sets out a number of restrictions and prohibitions on the investment of a Sub-Fund for as long as it is authorized by the SFC (including the Fund) and borrowing restrictions, as summarized in Schedule 1 to this Explanatory Memorandum.

The Manager does not intend to undertake any securities financing transactions including securities lending, sale and repurchase and reverse repurchase transactions or similar over-the-counter transactions on behalf of the Fund.

The Manager may at any time by prior written notice to the Trustee determine that the Fund will be subject to investment restrictions in addition to those set out in Schedule 1 to this Explanatory Memorandum or that subject to the investment restrictions applicable to the Fund under the Code, an investment restriction will not or will no longer apply to the Fund or will apply with such modifications as the Manager may determine. Any such determination may only be made with the prior approval of the SFC (where required). In addition, any determination to remove or modify an investment restriction of the Fund may only be made if the Manager confirms in writing to the Trustee that the Manager is satisfied that such determination will not materially prejudice Unitholders in the Fund. The Manager will give prior written notice to Unitholders of the Fund of any such determination subject to the requirements under the Code.

### **General**

All the investment and borrowing restrictions set out in Schedule 1 to this Explanatory Memorandum shall be measured by reference to the latest available Net Asset Value at the time the relevant investment or borrowing is made.

If any of the investment and borrowing restrictions is breached, the Manager shall as a priority objective take all steps as are necessary within a reasonable period of time to remedy the situation, taking due account of the interests of the Unitholders of the relevant Sub-Fund.

If any of the investment restrictions is exceeded as a result of changes in the value of the relevant Sub-Fund's investments, reconstructions or amalgamations, payments out of the assets of such Sub-Fund or redemptions of Units, then for so long as such limits are exceeded the Manager will not acquire any further investments subject to the relevant restriction and will as a priority take all reasonable steps as are necessary within a reasonable period of time, taking due account of the interests of the Unitholders of the relevant Sub-Fund, to restore the position so that the limits are no longer exceeded.

## **MANAGEMENT AND ADMINISTRATION**

### **Manager**

On 2 August 2019, Mitsubishi UFJ Financial Group, Inc.'s (MUFG) trust banking entity, Mitsubishi UFJ Trust and Banking Corporation (MUTB) completed the acquisition of First Sentier Investors. The MUFG group is headquartered in Tokyo and with over 360 years of history, MUFG group has a global network with over 1,800 locations in more than 50 countries.

The Manager is a company incorporated on 22 December 1987 under the laws of Hong Kong and is licensed by the Hong Kong Securities and Futures Commission to undertake regulated activities types 1 (dealing in securities), 4 (advising on securities) and 9 (asset management).

### **Trustee and Registrar**

The Trustee and Registrar of the Trust is HSBC Institutional Trust Services (Asia) Limited.

HSBC Institutional Trust Services (Asia) Limited is incorporated in Hong Kong on 27 September 1974. It is an indirect wholly-owned subsidiary of HSBC Holdings plc. It is registered as a trust company under Section 77 of Trustee Ordinance and an approved trustee under the Mandatory Provident Fund Schemes Ordinance. Being registered as the approved trustee, it is subject to statutory regulation of the Mandatory Provident Fund Schemes Authority.

Under the Trust Deed, the Trustee shall be responsible for the safe-keeping of the assets of each Sub-Fund and shall take into custody or under its control all the investments, cash and other assets forming part of the assets of each Sub-Fund and hold them in trust for the Unitholders of the relevant Sub-Fund in accordance with the provisions of the Trust Deed and, to the extent permitted by law, shall register cash and registrable assets in the name of or to the order of the Trustee and such investments, cash and other assets forming part of the assets of each relevant Sub-Fund shall be dealt with as the Trustee may think proper for the purpose of providing for the safe keeping thereof. The Trustee may appoint any person or persons to be custodian or co-custodian in respect of the whole or any part of the assets of any Sub-Fund and may empower any such custodian or co-custodian to appoint, with the prior consent in writing of the Trustee, sub-custodians. The fees and expenses of such custodian, co-custodian and sub-custodian shall be paid out of the relevant Sub-Fund.

The Trustee shall (A) exercise reasonable skill, care and diligence in the selection, appointment and ongoing monitoring of such persons appointed for the custody and/or safekeeping of any of the investments, cash, assets or other property comprised in the relevant Sub-Fund (each a “**Correspondent**”); and (B) be satisfied that each Correspondent retained remains suitably qualified and competent on an ongoing basis to provide the relevant services to the Trust or any Sub-Fund. Provided that the Trustee has discharged its obligations set out in (A) and (B) the Trustee shall not be liable for any act, omission, insolvency, liquidation or bankruptcy of any Correspondent that is not a connected person of the Trustee. The Trustee shall remain liable for any acts or omissions of any Correspondent which is a connected person of the Trustee as if the same were the acts or omissions of the Trustee. The Trustee shall use reasonable endeavours to recover any loss of investments and other assets arising from any default of a Correspondent.

The Trustee will not participate in transactions or activities or make any payments denominated in US dollars which would be subject to sanctions of the Office of Foreign Assets Control of the US Department of the Treasury.

Subject as provided in the Trust Deed and pursuant to the laws of Hong Kong, the Trustee shall not, in the absence of breaches of trust through fraud or negligence by it or any agent, sub-custodian or delegate appointed by the Trustee for which the Trustee would be liable under the Trust Deed and/or pursuant to the laws of Hong Kong, be liable for any losses, costs or damage to the Fund or to Unitholders. The Trustee is entitled to be indemnified from the assets of the Fund from and against any and all action, costs, claims, damages, expenses or demands relating to the Fund (other than those arising out of any liability imposed on the Trustee pursuant to the laws of Hong Kong or breaches of trust through fraud or negligence).

The Manager has sole responsibility for making investment decisions in relation to the Fund. Subject to the duty to ensure that the applicable investment and borrowing limitations of the Fund as set out in Schedule 1 to this Explanatory Memorandum are complied with, the Trustee (including its delegate) is not responsible or has any liability for any investment decision made by the Manager. Neither the Trustee, nor its delegate acts as guarantor or offeror of the Units or any underlying investment of the Fund.

Subject to the duty to ensure that the applicable investment and borrowing limitations of the relevant Sub-Fund comply with the applicable legal and regulatory requirements including but not limited to those in the Code and except as expressly stated in this Explanatory Memorandum, the Trust Deed and/or required by the Code, the Trustee is not involved directly or indirectly with the business affairs, sponsorship or management of the Fund. In addition the Trustee is not responsible for the preparation of any information contained in this Explanatory Memorandum (save for the information set out in this section pertaining to the Trustee).

## **ISSUE OF UNITS**

### **Issues of Units**

Units of the Fund will be available for subscription on each Dealing Day (being each Business Day). Subject as mentioned below, applications received by the Manager prior to 5:00 p.m. (Hong Kong time) on a Dealing Day will be dealt with on that Dealing Day. Applications received after such time or on a day which is not a Business Day will be carried forward and dealt with on the immediately following Dealing Day.

Units of the Fund will be issued on a Dealing Day at the relevant Net Asset Value per Unit of the Fund as at the close of business in the last relevant market to close on that Dealing Day, and the Manager is entitled under the Trust Deed to an initial charge of up to 5% of the said Net Asset Value per Unit.

An Anti-Dilution Adjustment may be payable by persons who subscribe for Units from time to time as determined by the Manager in good faith and in the best interest of Unitholders (which Anti-Dilution Adjustment shall not exceed 2% of the value of subscription obtained on the Dealing Day on which the subscription is effected). If the value of all subscriptions for Units exceeds the value of all redemptions of Units on a Dealing Day, then the Manager may have to purchase investments for the Fund and in doing so the Fund will incur dealing costs. An Anti-Dilution Adjustment reduces the effect of these costs by increasing the Net Asset Value per Unit to investors in these circumstances to cover those dealing costs. Any Anti-Dilution Adjustment applicable will be included in the Net Asset Value per Unit on any day on which the value of all subscriptions for Units exceeds the value of all redemptions of Units. The amount of the Anti-Dilution Adjustment is paid into the Fund for the protection of continuing Unitholders in the Fund. The Anti-Dilution Adjustment is not applied for the benefit of the Trust or the Manager. The Anti-Dilution Adjustment will be applied in respect of the Fund. The decision on whether or not to make a dilution adjustment, and the level of adjustment to make in particular circumstances or generally, will be made in line with the Fund's policy on anti-dilution. The price of each class of Units in the Fund will be calculated separately but any dilution adjustment will in percentage terms affect the price of Units of each class identically. Further information on how Anti-Dilution Adjustment is applied can be obtained on request from the Manager.

### **Application procedure**

Applications for Units should be made by completing an Application Form available from the Manager or such other documents as required or agreed by the Manager and sending it to the Manager. The original of any application for initial investment should be forwarded to the Manager. Where the original Application Form for initial investment and/or other supporting documentation have been provided in advance to the Manager, application for Units will be accepted on the basis of a faxed Application Form or other form of instruction as previously agreed by the Manager. Neither the Manager, nor HSBC ITS shall be responsible to an applicant for any loss resulting from the illegibility or non-receipt of any application sent by facsimile.

In addition, subscriptions may be accepted electronically in such format or method as shall be agreed in writing in advance with

HSBC ITS. The Manager and HSBC ITS reserve the right to refuse subscriptions through electronic means.

### **Minimum Investment**

The minimum initial investment amount for each class of Units is set out in the “Details of Unit Classes” section above.

### **Payment Procedure**

Payment should be made in one of the ways set out in the Application Form. Payments should be made in US dollars, GBP, Euro, HK dollars or RMB. Payment in other freely convertible currencies may be accepted. Payment in any currency other than the currency of denomination of the relevant class will be converted into the relevant currency of denomination and the proceeds of conversion (after deducting the costs of such conversion) will be applied in the subscription of Units in the Fund. Conversion of currencies may involve some delay.

Payment in respect of Units subscribed for must be received in cleared funds prior to 5:00 p.m. (Hong Kong time) on the fourth Business Day after the relevant Dealing Day. Investors should note that payments in currencies other than US dollars and Hong Kong dollars may take a longer period for clearance.

**Investors should note that for payment by telegraphic transfer in US dollars to be received for value on a particular day, payment must be made for value in New York at least one New York business day preceding such day and for payment by telegraphic transfer in Hong Kong dollars to be received for value on a particular day, payment must be made for value in Hong Kong at least one Hong Kong business day preceding such day.**

Subscriptions paid by cheques other than Hong Kong dollar cheques will not be processed until funds have cleared. Investors should be aware that if they pay by cheques other than Hong Kong dollar cheques, there may be delays in having their subscriptions processed. Therefore payment by cheques other than Hong Kong dollar cheques is not recommended.

If payment has not been received within the period set out above, an application may be cancelled and considered void or the Manager (at its discretion) may enforce payment of the sum due. In the event that an application is cancelled, the Manager and the Trustee are entitled to charge the applicant an administration charge to cover the administration costs involved in processing the application. The applicant may also be required to pay a cancellation fee (for the account of the Fund) in respect of each cancelled Unit of the amount (if any) by which the applicable Net Asset Value of such cancelled Unit at the time of subscription exceeds the applicable Net Asset Value of a Unit in the Fund on the date of cancellation.

No money should be paid to an intermediary in Hong Kong who is not licensed or registered to carry on Type 1 regulated activity under Part V of the Securities and Futures Ordinance.

### **General**

Units issued by the Trust will be held for investors in registered form. Certificates will not be issued. A contract note will be issued upon acceptance of an investor's application and will be forwarded by ordinary post (at the risk of the person entitled thereto).

The Trust Deed provides that fractions of not less than one-hundredth of a Unit may be issued. Application monies representing smaller fractions of a Unit will be retained by the Fund.

The Manager has an absolute discretion to accept or reject in whole or in part any application for Units or switching request. In particular, the Manager may exercise this discretion if they believe the investor or potential investor has been engaged in, or intends to engage in market timing activities. In the event that an application is rejected, application monies will be returned without interest by cheque through the post at the risk of the person(s) entitled thereto.

### **REDEMPTION OF UNITS**

Subject as mentioned below, any Unitholder may redeem the Unitholder's Units on any Dealing Day (being each Business Day) in whole or in part provided that the Manager may refuse to accept a request for a partial redemption which would result in a Unitholder holding less than the minimum holding amount of the relevant class of Units in the Fund and a Unitholder may only redeem his Units after cleared funds have been received in respect of such Units.

#### **Redemption Procedure**

Save as mentioned above, a redemption request must be received by the Manager before 5:00 p.m. (Hong Kong time) on the relevant Dealing Day in order to be dealt with on that Dealing Day. Redemption requests received after such time will be carried forward and dealt with on the Dealing Day next following the relevant Dealing Day.

A redemption request must be given in writing or by facsimile and must specify the name of the Fund and the number of Units to be redeemed, the name(s) of the registered holder(s), and give payment instructions for the redemption proceeds. Unless otherwise agreed by the Trustee the original of any redemption request given by facsimile should be forwarded to the Manager. Neither the Manager nor HSBC ITS shall be responsible to a Unitholder for any loss resulting from the illegibility or non-receipt of any redemption request sent by facsimile.

In addition, redemption requests may be accepted electronically in such format or method as shall be agreed in writing in advance with HSBC ITS. The Manager and HSBC ITS reserve the right to refuse redemptions through electronic means.

Units will be redeemed at the Net Asset Value per Unit of the Fund as at the close of business in the last relevant market to close on that relevant Dealing Day. The Manager does not have any current intention to levy any redemption charges. **If at any time during the period from the time as at which the Net Asset Value per Unit is calculated and the time at which redemption moneys are converted out of any other currency into the base currency of the Fund there is a devaluation or depreciation of that currency, the amount payable to any relevant redeeming Unitholder may be reduced as the Manager considers appropriate to take account of the effect of that devaluation or depreciation.**

An Anti-Dilution Adjustment may be payable by the Unitholders from time to time as determined by the Manager in good faith and in the best interest of Unitholders (which Anti-Dilution Adjustment shall not exceed 2% of the value of redemption obtained on the Dealing Day on which the redemptions are effected). If the value of all redemptions of Units exceeds the value of all subscriptions for Units on a Dealing Day, then the Manager may have to sell investments in the Fund and in doing so the Fund will incur dealing costs. An Anti-Dilution Adjustment reduces the effect of these costs by decreasing the Net Asset Value per Unit to investors in these circumstances to cover those dealing costs. Any Anti-Dilution Adjustment applicable will be included in the Net Asset Value per Unit on any day on which the value of all redemptions of Units exceeds the value of all subscriptions for Units. The amount of the Anti-Dilution Adjustment is paid into the Fund for the protection of continuing Unitholders in the Fund. The Anti-Dilution Adjustment is not applied for the benefit of the Trust or the Manager. The Anti-Dilution Adjustment will be applied in respect of the Fund. The decision on whether or not to make a dilution adjustment, and the level of adjustment to make in particular circumstances or generally, will be made in line with the Fund's policy on anti-dilution. The price of each class of Unit in the Fund will be calculated separately but any dilution adjustment will in percentage terms affect the price of Unit of each class identically. Further information on how Anti-Dilution Adjustment is applied can be obtained on request from the Manager.

### **Payment of Redemption Proceeds**

Redemption proceeds will not be paid to any redeeming Unitholder until unless otherwise agreed by the Manager, the written original of the redemption request duly signed by the Unitholder and any required supporting documentation (including all required anti-money laundering documentation) have been received by the Manager. Redemption proceeds will only be paid to the redeeming Unitholder and requests for payment to be made to a third party nominated by a redeeming Unitholder will not be entertained.

Unless some other method of payment is agreed with the Manager, redemption proceeds will be paid to the redeeming Unitholder (or in the case of joint Unitholders, to the first-named of the joint Unitholders, or such other of the joint Unitholders as may be authorised in writing by all of them) at the Unitholder's risk by cheque in US dollars, HK\$ or RMB, normally within seven Business Days after the relevant Dealing Day and in any event within 1 calendar month of the relevant Dealing Day or (if later) receipt by the Manager of a properly documented request for redemption of Units. Subject as mentioned above, at the request of the redeeming Unitholder and provided relevant account details have been provided to the Manager, redemption proceeds will be paid in the currency of denomination of the relevant class by telegraphic transfer (less the costs of effecting such telegraphic transfer).

Redemption proceeds can be paid in a currency other than the currency of denomination of the relevant class at the request and expense of the Unitholder.

### **Payment of Redemption Proceeds by Distribution in Specie**

The Manager has an absolute discretion to effect a redemption payment to any or all redeeming Unitholders in specie or in kind rather than in cash, subject to the prior consent of the relevant redeeming Unitholder(s). The circumstances in which the Manager envisages exercising this discretion include, without prejudice to the generality of the foregoing, a situation where substantial redemption requests are received by the Fund ("substantial" for these purposes ordinarily being more than 5% of the Net Asset Value of the Fund) which will make it impracticable or prejudicial to continuing Unitholders to realise the underlying securities in order to fund the redemption payments. In making redemption payments in specie or in kind, the Manager will use the same valuation procedures used in determining the Net Asset Value of the Fund (see "Calculation of Net Asset Value" below) when determining the value to be attributed to the relevant securities to be transferred or assigned or otherwise made available to the redeeming Unitholders. Redeeming Unitholders will receive securities of a value equal to the redemption payment to which they would otherwise be entitled. In such event, the redeeming Unitholder may request the Manager to sell such securities on his behalf and at his expense and to remit the net proceeds to him in cash. Investors should realise that the net proceeds of sale may be less than the indicated Net Asset Value of their holdings on the date of redemption owing to market fluctuations and the liquidity of the securities sold. Redeeming Unitholders receiving the redemption payment in specie or in kind will be responsible for all custody and other costs involved in changing the ownership of the relevant securities from the Fund to the redeeming Unitholder and for all ongoing custody costs in respect of such securities.

### **Restrictions on Redemption**

The Manager may suspend the redemption of Units or delay the payment of redemption proceeds during any periods in which the determination of the Net Asset Value of the Fund is suspended (for details see "Suspension of Calculation of Net Asset Value" below).

With a view to protecting the interests of Unitholders, the Manager is entitled, with the approval of the Trustee, to limit the number of Units of the Fund redeemed on any Dealing Day (whether by sale to the Manager or by cancellation by the Trustee) to 10% of the total number of Units of the Fund in issue. In this event, the limitation will apply pro rata so that all Unitholders wishing to redeem Units of the Fund on that Dealing Day will redeem the same proportion of such Units, and Units not redeemed (but which would otherwise have been redeemed) will be carried forward for redemption, subject to the same limitation, on the next Dealing Day. If requests for redemption are so carried forward, the Manager will inform the Unitholders concerned.

## **SWITCHING BETWEEN SUB-FUNDS WITHIN THE TRUST**

Unitholders have the right (subject to any suspension in the determination of the Net Asset Value of any relevant Sub-Fund) to switch all or part of their Units of the Fund into Units of another Sub-Fund (the “**New Fund**”) by submitting a duly completed switching form to the Manager. A switching request received by the Manager before 5:00 p.m. (Hong Kong time) on a Dealing Day for the Fund will be dealt with on that Dealing Day. Switching requests received after such time or on a day which is not a Dealing Day for the Fund will be carried forward and dealt with on the next Dealing Day. Where a switching request is made by facsimile, neither the Manager nor the Trustee shall be responsible to any Unitholder for any loss resulting from the illegibility or non-receipt of such switching request. Unless otherwise agreed by the Manager, the original of any switching request given by facsimile should be forwarded to the Manager.

In addition, switching requests may be accepted electronically in such format or method as shall be agreed in writing in advance with HSBC ITS. The Manager and HSBC ITS reserve the right to refuse switching requests through electronic means.

Switching will be effected by redeeming Units in the Fund on the relevant Dealing Day and issuing Units of the New Fund on a dealing day for Units of the New Fund falling on or after (i) the date of redemption of the Units of the Fund and (ii) the satisfaction of any conditions attaching to the issue of Units of the New Fund (for example, that such Units may only be issued on receipt of cleared funds for the account of the New Fund). The Manager may refuse to accept a request for switching if as a result a Unitholder would hold less than the minimum holding amount of the relevant class of Units in the Fund and/or if such switching represents less than the minimum initial investment applicable to the New Fund.

Any fraction smaller than one-hundredth of a Unit of the New Fund so arising will be ignored and moneys representing any such fraction will be retained as part of the New Fund.

If there is, at any time during the period from the time as at which the Net Asset Value per Unit of the Fund is calculated up to the time at which any necessary transfer of funds from the Fund to the New Fund takes place, a devaluation or depreciation of any currency in which the Fund is denominated or in which the investments of the Fund are denominated or normally traded, the applicable Net Asset Value at which the Units will be redeemed shall be reduced as the Manager considers appropriate to take account of the effect of that devaluation or depreciation and the number of Units of the New Fund to be allotted to any relevant Unitholder pursuant to a switching request shall be recalculated as if that reduced Net Asset Value had been the Net Asset Value ruling for redemption of Units of the Fund on the relevant Dealing Day.

The Manager has the discretion to levy and return for its own benefit and use a switching fee of 1% of the applicable Net Asset Value per Unit of the New Fund as calculated at the time of subscription.

## **CALCULATION OF NET ASSET VALUE AND PUBLICATION OF PRICES**

### **Calculation of Net Asset Value**

The Net Asset Value of the Fund will be determined as at the close of business in the last relevant market to close on each Dealing Day in accordance with the Trust Deed. The Trust Deed provides (inter alia) that:–

- (i) except in the case of any interest in a collective investment scheme to which paragraph (ii) applies and subject as provided in paragraph (vi) below, all calculations based on the value of investments quoted, listed, traded or dealt in or any securities market shall be made by reference to the latest available market dealing bid price or, if no latest available market dealing bid price is available, the last traded price on the principal stock exchange for such investments and in determining such prices the Manager and the Trustee shall be entitled to use and rely on electronic price feeds from such source or sources as they may from time to time determine, and the prices obtained from such price feeds or other sources shall be deemed to be the latest available market dealing bid price or last traded price (as applicable);
- (ii) subject as provided in paragraphs (iii) and (vi) below, the value of each interest in any collective investment scheme which is valued as at the same day as the Fund shall be the net asset value per unit or share in such collective investment scheme as at that day or, if the Manager so determines, or if such collective investment scheme is not valued as at the same day as the Fund, the value of such interest shall be the last available net asset value per unit or share in such collective investment scheme;
- (iii) if no net asset value, bid and offer prices or price quotations are available as provided in paragraph (ii) above, the value of the relevant investment shall be determined from time to time in such manner as the Manager in consultation with the Trustee shall determine;
- (iv) the value of any investment which is not listed or ordinarily dealt in on a market shall be the initial value thereof equal to the



amount expended out of the Fund in the acquisition of such investment (including in each case the amount of stamp duties, commissions and other acquisition expenses) provided that the Manager may with the approval of the Trustee and shall at the request of the Trustee cause a revaluation to be made by a professional person approved by the Trustee as qualified to value such investments;

- (v) cash, deposits and similar investments shall be valued at their face value (together with accrued interest) unless, in the opinion of the Manager, any adjustment should be made to reflect the value thereof;
- (vi) notwithstanding the foregoing, the Manager may in consultation with the Trustee adjust the value of any investment or permit some other method of valuation to be used if, having regard to currency, applicable rate of interest, maturity, marketability and other considerations the Manager deems relevant, the Manager considers that such adjustment or use of such other method is required to reflect the fair value of the investment;
- (vii) the value of any investment (whether of a security or cash) otherwise than in the currency of the Fund shall be converted into the currency of the Fund at the rate (whether official or otherwise) which the Manager shall deem appropriate in the circumstances having regard to any premium or discount which may be relevant and to costs of exchange; and
- (viii) where a third party is engaged in the valuation of the assets of the relevant Sub-Fund, the Manager shall exercise reasonable care, skill and diligence in the selection, appointment and ongoing monitoring of such third party in ensuring such entity possesses the appropriate level of knowledge, experience and resources that is commensurate with the valuation policies and procedures for such Sub-Fund. The valuation activities of such third party shall be subject to ongoing supervision and periodic review by the Manager.

For instance, with regard to paragraph (vi) above, where the market value of an investment is unavailable or where the Manager reasonably believes that no reliable price exists or the most recent price available does not reflect a price the relevant Sub-Fund would expect to receive upon the current sale of the investment, the Manager may in consultation with the Trustee value the investment at a price which the Manager believes reflects a fair and reasonable price for that investment in the prevailing circumstances.

#### **Suspension of Calculation of Net Asset Value**

The Manager may, after consultation with the Trustee, having regard to the best interests of Unitholders, declare a suspension of the determination of the Net Asset Value of the Fund for the whole or any part of any period during which:

- (i) there is a closure of or the restriction or suspension of trading on any securities market on which a substantial part of the investments of the Fund is normally traded or a breakdown in any of the means normally employed by the Manager or the Trustee (as the case may be) in ascertaining the prices of investments or the Net Asset Value of the Fund or the Net Asset Value per Unit in the Fund; or
- (ii) for any other reason the prices of investments of the Fund cannot, in the opinion of the Manager, reasonably, promptly and fairly be ascertained; or
- (iii) circumstances exist as a result of which, in the opinion of the Manager, it is not reasonably practicable to realise any investments of the Fund or it is not possible to do so without seriously prejudicing the interests of Unitholders; or
- (iv) the remittance or repatriation of funds which will or may be involved in the realisation of, or in the payment for, the investments of the Fund or the issue or redemption of Units in the Fund is delayed or cannot, in the opinion of the Manager, be carried out promptly at normal rates of exchange.

Such suspension shall take effect forthwith upon the declaration thereof and thereafter there shall be no determination of the Net Asset Value of the Fund until the Manager shall declare the suspension at an end, except that the suspension shall terminate in any event on the day following the first Business Day on which (i) the condition giving rise to the suspension shall have ceased to exist and (ii) no other condition under which suspension is authorised shall exist.

Whenever the Manager declares such a suspension it shall (i) immediately after any such declaration, notify the SFC of such suspension and (ii) immediately after any such declaration and at least once a month during the period of such suspension, publish a notice on the website, [www.firstsentierinvestors.com](http://www.firstsentierinvestors.com) and/or cause a notice to be given to Unitholders and to all those (whether Unitholders or not) whose applications to redeem Units shall have been affected by such suspension stating that such declaration has been made. The SFC has not reviewed the contents of the aforementioned website.

No Units in the Fund may be redeemed during such a period of suspension.

#### **Calculation of Net Asset Value per Unit for purpose of subscription and redemption**

The Net Asset Value per Unit in the Fund on a Dealing Day will be calculated by dividing the Net Asset Value of the Fund on the relevant Dealing Day by the number of Units in the Fund in issue on that Dealing Day prior to any issue or redemption being effected on that Dealing Day and, the resulting amount shall be rounded down to the minimum unit of the base currency of the Fund, (being

one cent where the base currency is US dollars) for the purposes of both subscription and redemption. Any roundings will be retained for the benefit of the Fund.

Under the Trust Deed the Manager is given the power in determining the Net Asset Value per Unit in the case of subscription to add, and in determining the Net Asset Value per Unit in the case of redemption to deduct, for the account of the Fund from the Net Asset Value per Unit (after making any rounding adjustment) an amount which it considers to be an appropriate allowance to reflect the spread between the bid and offer prices of investments and the duties and charges which would be incurred if the investments of the Fund were to be acquired (when calculating the Net Asset Value per Unit for subscription) or sold (when calculating the Net Asset Value for redemption) at the values attributed to them.

### **Publication of Prices**

The Net Asset Value per Unit of the Fund will be published daily on the website [www.firstsentierinvestors.com](http://www.firstsentierinvestors.com). The SFC has not reviewed the contents of this website.

## **LIQUIDITY RISK MANAGEMENT**

The Manager has established a liquidity management policy which enables it to identify, monitor and manage the liquidity risks of the Fund and to ensure that the liquidity profile of the investments of the Fund will facilitate compliance with the Fund's obligation to meet redemption requests. Such policy, combined with the liquidity management tools of the Manager, also seeks to achieve fair treatment of Unitholders and safeguard the interests of remaining Unitholders in case of sizeable redemptions.

The Manager's liquidity policy takes into account the investment strategy, the liquidity profile, the redemption policy, the dealing frequency, the ability to enforce redemption limitations and the fair valuation policies of the Fund. These measures seek to ensure fair treatment and transparency for all investors.

The liquidity management policy involves monitoring the profile of investments held by the Fund on an on-going basis to ensure that such investments are appropriate to the redemption policy as stated under the section headed "Redemption of Units", and will facilitate compliance with the Fund's obligation to meet redemption requests. Further, the liquidity management policy includes details on periodic stress testing carried out by the Manager to manage the liquidity risk of the Fund under normal and exceptional market conditions.

The following tools may be employed by the Manager to manage liquidity risks:

- the Manager may, with the approval of the Trustee, limit the number of Units of the Fund redeemed on any Dealing Day to 10% of the total number of Units of the Fund in issue (subject to the conditions under the heading entitled "Restrictions on Redemption" in the section headed "Redemption of Units");
- the Manager may suspend redemption under exceptional circumstances as set out under the heading entitled "Suspension of Calculation of Net Asset Value" in the section headed "Calculation of Net Asset Value and Publication of Prices"; and
- an Anti-Dilution Adjustment may be payable by the Unitholder from time to time as determined by the Manager (which Anti-Dilution Adjustment shall not exceed 2% of the subscription monies/redemption monies obtained on the Dealing Day). The amount of the Anti-Dilution Adjustment is paid into the Fund for the protection of continuing Unitholders in the Fund. For further details, please refer to the sub-sections headed "Issues of Units" and "Redemption Procedure".

## **DISTRIBUTION POLICY**

### **General**

The Manager intends to declare distributions on Units in the Fund on a monthly basis. Distributions which accrue each month shall normally be declared and paid within the following month.

The monthly dividend rate per Unit will be calculated by the Manager based on the estimated income.

The Manager will review the dividend rate for each Class at least annually, but may adjust the dividend rate more frequently if necessary to reflect changes in the expected income levels.

The Manager may at its discretion pay dividend out of the income derived from the Fund's investment or out of the capital of the Fund. Payment of dividends out of capital amounts to a return or withdrawal of part of an investor's original investment or from any capital gains attributable to that original investment. Any distributions involving payment of dividends out of the Fund's capital may result in an immediate reduction of the Net Asset Value per Unit. The compositions of the dividends (i.e. the relative amounts paid out of (i) net distributable income and (ii) capital) for the last 12 months are available by the Manager on request and also on the website [www.firstsentierinvestors.com](http://www.firstsentierinvestors.com). The SFC has not reviewed the contents of this website. This policy of paying dividends out of capital may be amended subject to the SFC's prior approval and by giving not less than one month's prior notice to investors.

Dividends will normally be paid to investors in the currency of the relevant Class, unless otherwise agreed by the Manager to be paid in a currency (US dollars, HK dollars or Renminbi) other than the relevant Class currency (any foreign currency exchange

costs will be borne by the relevant Unitholder). In the alternative, Unitholders may elect to reinvest distributions in the respective Class of the Fund, in which case reinvestment shall normally be effected on the next day of the ex-dividend date of the corresponding distribution.

The Trust Deed provides that upon the expiry of the period of six years after the relevant distribution date in respect of a distribution, the Unitholder (and any person claiming through, under or in trust for him) shall forfeit any right to such distribution. Such amount shall become part of the relevant assets of the Fund (unless the Fund shall have been terminated in which case such amount shall be paid to the Manager for their own use and benefit). No amount payable to a Unitholder in respect of any distribution shall bear interest.

The payment of dividends out of capital may have different tax implications from the payment of dividends out of income and it is recommended that investors seek advice in this regard.

## **CHARGES AND EXPENSES**

### **Management Fees**

The Manager is entitled to receive in arrears a monthly management fee from the Fund, accrued on and calculated as at each Dealing Day, at the rate of 1.25% per annum of the Net Asset Value of the Fund. The Manager may increase the rate of management fee payable in respect of the Fund up to or towards 2.25% per annum on giving not less than three months' notice of such increase to the Trustee and the Unitholders.

Under the Trust Deed, the Manager is entitled to an initial charge of up to 5% of the applicable Net Asset Value per Unit at the time of subscription and to a redemption charge of up to 5% of the applicable Net Asset Value per Unit at the time of redemption. However, the Manager does not have any current intention to levy any redemption charge upon the redemption of Units in the Fund. In the event that the Manager intends to levy any redemption charge, no less than three months' prior notice of such intention will be given to Unitholders.

The Manager may share any fees it receives with distributors or agents procuring subscriptions and rebate to any investor(s) any fees it may receive in such manner as it considers appropriate. The Manager will pay the promotional costs in connection with the offer of Units financed out of the management fee it receives. The Manager and other companies within the Manager's group may with the consent of the Trustee deal with the Fund, both as principal and agent, and, subject as provided below, may retain any benefit which they receive as a result.

### **Trustee's Fees**

HSBC ITS is entitled, in its respective capacities as Trustee and Registrar, to receive trustee, administration and registrar fees from the Fund. The trustee fee accrues daily and is calculated as at each Dealing Day as a percentage of the Net Asset Value of the Fund and is paid monthly in arrears in US\$. The rate at which the trustee fee currently accrues is 0.05% per annum of the Net Asset Value of the Fund, out of which the Trustee will pay any sub-custodian fees and expenses. With effect from 1 November 2020, the Trustee will additionally charge a fixed fee of US\$4,000 per annum for the Fund in relation to the performance of its duties to the Fund. For the avoidance of doubt, the aggregate fees payable to the Trustee will continue to be subject to a maximum fee of 1.0% per annum of the Net Asset Value of the Fund. The Trustee is also entitled to charge a transaction fee of US\$15 on each purchase and sale of securities transaction done by the Manager on behalf of the Fund.

The Trustee may increase the rate of the trustee fee up to or towards 1% per annum on giving not less than three months' notice of such increase to the Manager and the Unitholders.

The Trustee is entitled to receive processing fees at rates agreed with the Manager. In its capacity as Registrar, HSBC ITS is entitled to receive an administration fee, which accrues daily and is calculated as at each Dealing Day, at the rate of 0.10% per annum of the Net Asset Value of the Fund, payable monthly in arrears, subject to a minimum of US\$1,000 per month. Any increase of such administration fee will require the SFC's prior approval and at least one month's prior notice to investors.

The Trustee is also entitled to a termination fee in relation to the termination of the Trust or the Fund at such rate as may be agreed between the Trustee and the Manager or, failing agreement, in accordance with the normal commercial rates of the Trustee at the time of such termination and such fee will be paid out of the Trust or the Fund (as the case may be).

The Trustee and Registrar will also be entitled to be reimbursed by the Fund for all out-of-pocket expenses incurred in the course of its duties.

### **Other Charges and Expenses**

The preliminary establishment expenses of the Fund, including an establishment fee payable to the Trustee, the costs and expenses in obtaining authorisation of the Fund in Hong Kong, the preparation of this Explanatory Memorandum and all agreements referred to in this document, all initial legal and printing costs were borne by the Fund and have been fully amortised.

Each Sub-Fund of the Trust bears the costs set out in the Trust Deed which are directly attributable to it. Where such costs are not directly attributable to a Sub-Fund, each Sub-Fund will bear such costs in proportion to its respective Net Asset Value. Such costs



include but are not limited to the costs of investing and realising the investments of the Sub-Fund, the fees and expenses of custodians of the assets of the Trust, the fees and expenses of the auditors, valuation costs, legal fees, the costs incurred in connection with any listing or regulatory approval, the costs of holding meetings of Unitholders and the costs incurred in the preparation and printing of any explanatory memorandum.

Notwithstanding the foregoing, the Manager has determined that a fixed expense ratio shall apply to the Fund such that, in the event that the TER exceeds 2.5% per annum, the management fee payable to the Manager shall be reduced (either in part or in its entirety) to the extent that the TER exceeds 2.5% per annum. In the event that the TER is less than 2.5% per annum, the Manager shall be entitled to receive the amount equal to the difference between the TER and the expense limit applicable in the relevant year. The TER shall be calculated as at each Dealing Day and any adjustment to the management fee or, as the case may be, payment due to the Manager shall be calculated and accrue as at each Dealing Day, with the relevant adjustment or payment, as the case may be, being effected on a monthly basis at the time of payment of the management fee.

#### **Cash Rebates, Soft Commissions and Payment for Research**

Neither the Manager nor any of its connected persons will receive goods or services (soft dollar) or cash or other rebates from a broker or dealer in relation to the management of the Fund's assets (including in consideration of directing transactions in the Fund's assets to a broker or dealer). All research used in relation to the management of the Fund's asset which is received by the Manager will be paid for out of the relevant firm's own resources.

#### **Transactions with Connected Persons**

The following requirements relating to transactions with connected persons will apply:

- (i) No person may be allowed to enter on behalf of the Trust and/or the Fund into underwriting or sub-underwriting contracts without the prior consent of the Trustee and unless the Fund or the Manager provides in writing that all commissions and fees payable to the Manager under such contracts, and all investments acquired pursuant to such contracts, will form part of the Fund's assets;
- (ii) If cash forming part of the Fund's assets is deposited with the Trustee, the Manager or with any of their connected persons (being an institution licensed to accept deposits), such cash deposit shall be maintained in a manner that is in the best interests of the Unitholders of the Fund, having regard to the prevailing commercial rate for a deposit of similar type, size and term negotiated at arm's length in accordance with ordinary and normal course of business; and
- (iii) All transactions carried out by or on behalf of the Trust and/or the Fund must be executed at arm's length, on the best available terms and in the best interests of the Unitholders of the Fund and/or the relevant Sub-Fund. In particular, any transaction between the Fund and the Manager or any of its connected persons as principal may only be made with the prior written consent of the Trustee. All such transactions must be disclosed in the Fund's annual report. In transacting with brokers or dealers connected to the Manager, the Trustee or any of their connected persons, the Manager must ensure that:
  - (a) such transactions should be on arm's length terms;
  - (b) it uses due care in the selection of brokers or dealers and ensures that they are suitably qualified in the circumstances;
  - (c) transaction execution must be consistent with applicable best execution standards;
  - (d) the fee or commission paid to any such broker or dealer in respect of a transaction must not be greater than that which is payable at the prevailing market rate for a transaction of that size and nature;
  - (e) it monitors such transactions to ensure compliance with its obligations; and
  - (f) the nature of such transactions and the total commissions and other quantifiable benefits received by such broker or dealer shall be disclosed in the Fund's annual report.

For the purposes of the sub-sections headed "Cash Rebates, Soft Commissions and Payment for Research", "Transactions with Connected Persons" and "Conflicts of Interest" and Schedule 1 to this Explanatory Memorandum, "connected persons" shall have the meaning defined in the Code and include any subsidiary or holding company or associate of the Manager or the Trustee, or subsidiary of such holding company as the case may be.

## **TAXATION**

### **General**

Investors should consult their professional advisers on the consequences to them of acquiring, holding, redeeming, transferring or selling Units under the relevant laws of the jurisdictions to which they are subject, including the tax consequences and any exchange control requirements. These consequences, including the availability of, and the value of, tax relief to investors will vary with the law and practice of the investors' country of citizenship, residence, domicile or incorporation and their personal circumstances. The following statements regarding taxation are based on the law and practice in force in Hong Kong, PRC and US at the date of this document and are subject to any subsequent changes in the law or practice (which could be made on a retroactive basis). The following is not intended to be comprehensive. It must not be construed as tax advice and should not be relied upon as a substitute for detailed and specific advice.

## Hong Kong Taxation

### Profits tax

During such period as the Trust and the Fund are authorised by the Securities and Futures Commission pursuant to Section 104 of the Securities and Futures Ordinance (“SFO”) in Hong Kong, under present Hong Kong law and practice, the Trust and the Fund are not expected to be subject to Hong Kong profits tax in respect of any of their authorised investment activities.

In general, no tax is expected to be payable by Unitholders in Hong Kong in respect of dividends or other income distributions of the Trust or the Fund or in respect of any gains arising on a sale, redemption or other disposal of Units in the Trust or the Fund if the Units represent capital assets of the Unitholders. Unless exempt by a specific provision in the Hong Kong tax law, Hong Kong profits tax (which is currently charged at the rate of 16.5% for corporations, and 15% for individuals or unincorporated business, subject to a two-tiered profits tax rates regime<sup>1</sup>) may arise on any gains or profits made on the sale, redemption or other disposal of the Units where such transactions form part of a trade, profession or business carried on by a Unitholder in Hong Kong, and the gains or profits, not being regarded as capital in nature, are sourced in Hong Kong.

### Stamp duty

Hong Kong stamp duty should be payable on the sale or purchase of Hong Kong stock. “Hong Kong stock” is defined as “stock” the transfer of which is required to be registered in Hong Kong. The Units fall within the definition of “Hong Kong stock” in the Stamp Duty Ordinance (Cap.117) of Hong Kong (the “Stamp Duty Ordinance”).

No Hong Kong ad valorem stamp duty should be payable on the issue of Units or on the redemption of Units.

No Hong Kong stamp duty should be payable where the sale or transfer of Units in the Trust or the Fund is effected by selling the relevant Units back to the Manager, who then either extinguishes the Units or re-sells the Units to another person within two months thereof.

Under a remission order issued by the Secretary for the Treasury on 20 October 1999, no Hong Kong stamp duty should be payable on transfer of Hong Kong stocks to the Fund (which has been authorised under Section 104 of the SFO) in exchange for issue of Units, or transfer of Hong Kong stocks from the Fund in consideration for redemption of Units.

Other types of sales or purchases or transfers of Units by the Unitholders should be liable to Hong Kong stamp duty of 0.26% (equally borne by the buyer and the seller) on the higher of the consideration amount or market value. In addition, a fixed duty of HK\$5.00 is currently payable on any instrument of transfer of Units.

## People’s Republic of China Tax Considerations

### Corporate Income Tax

Under current PRC CIT law and regulations (“CIT Law”):

- if the Fund is considered as a PRC tax resident enterprise, it will be subject to the PRC CIT at a rate of 25% of its worldwide taxable income; and
- if the Fund is considered as a non-PRC tax resident enterprise but has an establishment or place of business in the PRC, it would be subject to CIT at a rate of 25% of the profits attributable to that establishment or place of business.

The Manager intends to use reasonable efforts to manage and conduct the affairs of the Fund in such a way that the risk of the Fund being considered as a resident enterprise or having a relevant establishment or place of business in the PRC is reduced as far as possible. However, there can be no assurance that such objective will be achieved.

- a) *Investment in China A Shares via the Stock Connects, QFII/RQFII, open-ended collective investment schemes that have obtained access to China A Shares through the QFII/RQFII and Access Products*

#### *Capital gains*

- (i) *Investments in China A Shares via the Stock Connects and QFII/RQFII*

On 31 October 2014, the MOF, the STA and the CSRC have also jointly released Caishui [2014] No.79 (“**Notice No. 79**”) which specifies that capital gains realized from trading of PRC equity investments (including China A Shares) by

<sup>1</sup> Under the two-tiered profits tax rates regime, the first HK\$2 million of assessable profits of corporations and unincorporated business will be taxed at a reduced rate of 8.25% and 7.5% respectively on a self-election basis, with certain exceptions. For a group of “connected entities”, only one entity within the group can elect to apply the two-tiered rates. Unitholders should take advice from their own professional advisers as to their particular tax position.

QFII/RQFII which do not have an establishment or place in China or have an establishment or place in China but the income so derived in China is not effectively connected with such establishment, will be temporarily exempted from PRC CIT from 17 November 2014 onwards.

Pursuant to the Notice about the tax policies related to the Shanghai-Hong Kong Stock Connect (Caishui [2014] No. 81) (“**Notice No. 81**”) and the Notice about the tax policies related to the Shenzhen-Hong Kong Stock Connect (Caishui [2016] No. 127) (“**Notice No. 127**”) promulgated by the MOF, the STA and the CSRC on 14 November 2014 and 5 November 2016 respectively, CIT is temporarily exempted on capital gains derived by Hong Kong and overseas investors (including the Fund) on the trading of China A Shares through the Stock Connects.

Based on Notice No. 79, Notice No. 81 and Notice No. 127, and having consulted professional and independent tax advisers, the Manager will not make any tax provision for gross realised or unrealised capital gains derived from trading of China A Shares via the Stock Connects and QFII/RQFII.

The duration of the period of temporary exemption has not been stated and is subject to termination by the PRC tax rules with retrospective effect which may adversely affect the Fund. If the temporary exemption is withdrawn a foreign investor would be subject to PRC taxation in respect of gains on China A Shares and the resultant tax liability would be payable by the Fund, and thus borne by its investors. However, this liability may be mitigated under the terms of an applicable tax treaty, and if so, any such benefits will be passed to investors.

(ii) *Investments in China A Shares via open-ended collective investment schemes that have obtained access to China A Shares through the QFII/RQFII, and Access Products*

To the extent that the Fund is exposed to uncertainty relating to tax on Chinese securities via investing in open-ended collective investment schemes that have obtained access to China A Shares through the QFII/RQFII, this exposure is limited to a reduction in the net asset value of the open ended investment scheme. Prior to 17 November 2014, significant uncertainty related to the provisioning of capital gains tax relating to investments in China A Shares via QFII/RQFII. Effective from 17 November 2014, the gains obtained by QFII/RQFII holders from transfer of shares and other equity interest in China is temporarily exempt from CIT.

While the capital gains realised from disposing of China A Shares invested through the QFII/RQFII on and after 17 November 2014 shall be temporarily exempted from Withholding Income Tax (“WIT”), it is uncertain how long the temporary exemption will last and there can be no certainty that the China A-shares will not attract a liability to such tax in the future. The PRC tax authorities may in the future issue further guidance in this regard and with potential retrospective effect.

In light of Notice No. 79, WIT on capital gain attributable to the Fund’s investment in access products for China A Shares realized from 17 November 2014 onwards should be exempted if the access products issuers for China A Shares do not have an establishment or place in China or have an establishment in China but the income so derived in China is not effectively connected with such establishment. Based on Notice No. 79 and having consulted professional and independent tax advisers, the Manager will not make any tax provision for gross realized or unrealized capital gains derived from investment in access products for China A Shares.

Please note that it is possible that under the terms of an agreement between the issuers of access products for China A Shares and the Fund, the access products issuers may pass on any tax liability that they incur to the Fund. If this is the case, the Fund could be the ultimate party which bears the PRC tax risks on the investment in the PRC securities.

*Dividend*

Unless a specific exemption or reduction is available under current CIT Law or relevant tax treaties, non-tax resident enterprises without permanent establishment in the PRC are subject to WIT, generally at a rate of 10% on dividend income / profit distribution arising from investments in the PRC securities. The entity distributing such dividend income/ profit distribution is required to withhold such tax on behalf of the recipients. The Fund is subject to WIT at 10 % on dividends received from China A Shares traded via the Stock Connects and QFII/RQFII.

b) *Investment in debt securities via Bond Connect*

*Capital gains*

Under current PRC tax law, there are no specific rules or regulations governing the taxation of the disposal of debt securities issued by PRC tax resident enterprises. The tax treatment for investment in debt securities issued by PRC tax residents is governed by the general taxing provisions of the CIT Law. Under such general taxing provision, the Fund would be potentially subject to 10% PRC WIT on the PRC-sourced capital gains, unless exempt or reduced under relevant double tax treaties.

Pursuant to Article 7 of the Detailed Implementation Regulations of the PRC CIT Law, where the property concerned is a movable property, the source of capital gain shall be determined according to the location of the enterprise, establishment or place which transfers the property. The PRC tax authorities have verbally indicated that debt instruments issued by PRC tax resident enterprises are movable property. In this case, the source shall be determined based on the location of the

transferor. As the Fund is located outside the PRC, gains derived by the Fund from debt instruments issued by PRC tax resident enterprises could be argued as offshore sourced and thus not subject to PRC WIT. However, there is no written confirmation issued by the PRC tax authorities that debt instruments issued by PRC tax resident enterprises are movable property.

As a matter of practice, the PRC tax authorities have not levied PRC WIT on capital gains realised by foreign investors from the trading of debt securities. Based on the current interpretation of the SAT and having consulted professional and independent tax advisors, the Manager will not make any tax provision for gross realized or unrealized capital gains derived from disposal of debt securities via Bond Connect.

In light of the uncertainty on the income tax treatment on capital gain derived from trading of debt securities via Bond Connect and for the purpose of meeting this potential tax liability of Fund for capital gains derived from trading of debt securities via Bond Connect, the Manager reserves the right to provide for WIT on such gains or income and withhold the tax from the account of the Fund based on new developments and interpretation of the relevant regulations after having consulted professional and independent tax advisor.

#### *Interest income*

Unless a specific exemption is applicable under current mainland China tax laws and regulations or relevant tax treaties, non-residents, including the Fund, are subject to PRC WIT on the interest income derived from the investment in debt instruments issued by mainland China tax residents. In general, the prevailing WIT rate of 10% should be applicable to the Fund. The entity distributing such interests is required to withhold WIT.

Under the current CIT Law, interests derived from mainland China government bonds issued by the in-charge Finance Bureau of the State Council and/or local government bonds approved by the State Council are exempt from CIT.

The MOF and STA issued Notice No. 108 on 22 November 2018, which stipulated that foreign institutional investors are exempted from China WIT in respect of bond interest income received from 7 November 2018 to 6 November 2021 from investments in the China bond market. This exemption granted under Notice No. 108 is temporary, so it is uncertain whether such exemption policy would be extended after 6 November 2021.

#### Value Added Tax ("VAT") and surtaxes

##### *a) Investment in China A Shares via the Stock Connects, QFII/RQFII, open-ended collective investment schemes that have obtained access to China A Shares through the QFII/RQFII, and Access Products*

The MOF and the STA jointly issued the "Notice on the Comprehensive Roll-out of the B2V Transformation Pilot Program (Caishui [2016] No. 36) (**Notice No. 36**)" on 23 March 2016. Notice No. 36 sets out that the B2V Pilot Program has been expanded to all industries, including financial services from 1 May 2016.

Notice No. 36 provides that VAT at 6% shall be levied on the difference between the selling and buying prices of those marketable securities, e.g. China A Shares, unless there is specific exemption. The Notice No. 36 also provides that gains derived by QFIIs/RQFIIs from trading of marketable securities are exempt from VAT. Pursuant to the "Supplementary Notice on the VAT Policy on Interbank Transactions and Other Financial Institutions" (Caishui [2016] No. 70) (**Notice No. 70**) jointly issued by MOF and STA on 30 June 2016 and which took effect retrospectively on 1 May 2016, gains derived by QFIIs/RQFIIs from the trading of marketable securities are also exempt from VAT.

Based on the prevailing VAT regulations, capital gains derived by (i) QFIIs / RQFIIs on trading of marketable securities and (ii) investors via the Stock Connects are exempted from VAT. Therefore, to the extent that the Fund's investments in China A Shares are made through QFII/RQFII, the Stock Connects and access products, the capital gains should be exempted from VAT.

Dividend income or profit distributions on equity investment derived from China are not included in the taxable scope of VAT.

If VAT is applicable, there are also other surtaxes (which include Urban Construction and Maintenance Tax, Education Surcharge and Local Education Surcharge) that would amount to as high as 12% of VAT payable. In addition, there may also be other local levies such as flood prevention fee, commodity reconciliation fund and water conservancy fund, depending on the location of the Chinese companies.

##### *b) Investment in debt securities via Bond Connect*

#### *Capital gains*

Pursuant to Notice No. 36 and Notice No.70, gains realised by QFIIs/RQFIIs from trading of PRC marketable securities are exempt from VAT. Gains realised by approved foreign investors from trading of RMB denominated debt securities in the China Interbank Bond Market are also exempt from VAT. There are no specific VAT rules for trading debt securities via Bond Connect. That said, by making reference to the above notices and other related prevailing tax regulations, it is anticipated that gains derived by foreign investors from the trading of PRC bonds through Bond Connect should also not be

subject to China VAT.

#### *Interest income*

Pursuant to Notice No. 36, interest income derived from bonds issued by PRC tax resident enterprise should be subject to 6% VAT, unless specifically exempted. Interest derived from PRC government bonds issued by the in-charge Finance Bureau of the State Council and/or local government bonds approved by the State Council are exempted from VAT. In addition, Notice No. 108 stipulated that foreign institutional investors are exempted from China VAT in respect of bond interest income received from 7 November 2018 to 6 November 2021 from investments in the China bond market. This exemption granted under Notice No. 108 is temporary, so it is uncertain whether such exemption policy would be extended after 6 November 2021.

If VAT is applicable, there are also other surtaxes (which include Urban Construction and Maintenance Tax, Education Surcharge and Local Education Surcharge) that would amount to as high as 12% of VAT payable. In addition, there may also be other local levies such as flood prevention fee, commodity reconciliation fund and water conservancy fund, depending on the location of the Chinese companies.

In view of the foregoing, having consulted professional and independent tax advisors, the Manager reserves the right to provide for VAT on interest income from its investments in PRC debt securities via Bond Connect (except PRC government bonds) and withhold the tax from the account of the Fund based on new developments and interpretation of the relevant regulation where the VAT exemption is no longer applicable. The Manager will provide appropriate notification to affected Unitholders accordingly should there be a change to such provisioning policy.

#### Stamp duty

Stamp duty under the PRC laws generally applies to the execution and receipt of all taxable documents listed in the PRC's Provisional Rules on Stamp Duty. Stamp duty is levied on the execution or receipt in China of certain documents, including contracts for the sale of China A Shares traded on the PRC stock exchanges. In the case of contracts for sale of China A Shares, such stamp duty is currently imposed on the seller but not on the purchaser, at the rate of 0.1%.

#### General PRC tax considerations

There is a possibility of the PRC tax rule, regulations and practice being changed and taxes being applied retrospectively. The potential application of tax treaties is uncertain. As such, there are also risks and uncertainties associated with the current PRC tax laws, regulations and practice. As such, there is a risk that any tax provision made by the Manager in respect of the Fund may be more than or less than the Fund's respective actual tax liabilities, which may potentially cause substantial loss to the Fund. The Manager will closely monitor any further guidance by the relevant PRC tax authorities and adjust the withholding policy of the Fund accordingly, taking into account of independent professional tax advice.

If the amount of tax provision is more than or less than the Fund's actual tax liabilities, Unitholders may be disadvantaged or advantaged depending upon the final tax liabilities, the level of provision and when they subscribed and/or redeemed their Units. If the actual tax levied by the PRC tax authorities is higher than that provided for by the Manager so that there is a shortfall in the tax provision amount, investors should note that the Net Asset Value of the Fund may be lowered, as the Fund will ultimately have to bear the full amount of tax liabilities. In this case, the additional tax liabilities will only impact Units in issue at the relevant time, and the then existing Unitholders and subsequent Unitholders will be disadvantaged as such Unitholders will bear, through the Fund, a disproportionately higher amount of tax liabilities as compared to that borne at the time of investment in the Fund. On the other hand, the actual tax liabilities may be lower than the tax provision made, in which case only the then existing Unitholders will benefit from a return of the extra tax provision. Those persons who have already redeemed their Units before the actual tax liabilities are determined will not be entitled or have any right to claim any part of such overprovision.

Various tax reform policies have been implemented by the PRC government in recent years, and existing tax laws and regulations may be revised or amended in the future. There is a possibility that the current tax laws, regulations and practice in the PRC will be changed with retrospective effect in the future and any such change may have an adverse effect on the Net Asset Value of the Fund. Moreover, there is no assurance that tax incentives currently offered to foreign companies, if any, will not be abolished and the existing tax laws and regulations will not be revised or amended in the future. Any changes in tax policies may reduce the after-tax profits of the companies in the PRC which the Fund invests in, thereby reducing the income from, and/or value of the Units.

Unitholders should seek their own tax advice on their tax position with regard to their investment in the Fund.

#### **The Foreign Account Tax Compliance Act and similar measures**

- (a) Unitholders and prospective investors should be aware that under Sections 1471 – 1474 of the US Internal Revenue Code (the "IRC") of 1986 and US Treasury Regulations made thereunder (together, as amended from time to time, generally known as the Foreign Account Tax Compliance Act (**FATCA**)), a 30% withholding tax (a "**FATCA Deduction**") may be imposed on certain payments made to the Trust and/or the Fund of US source income (including dividends and interest) and potentially on foreign passthru payments, if the relevant regulations defining foreign passthru payment are published) unless the Trust is compliant with FATCA. It is the intention of the Trust to comply with the FATCA regulations. To comply, the Trust will generally be required to, amongst other things, perform certain account due diligence procedures on the Unitholders



and annually report certain information relating to “specified United States persons” (generally persons who are US taxpayers) who hold, directly or indirectly, interests in the Trust and/or the Fund and details relating to their holdings to the U.S. Internal Revenue Service (“IRS”), pursuant to the requirements of the Intergovernmental Agreement (“IGA”) between the United States and Hong Kong in connection with the implementation of FATCA (the “US-Hong Kong IGA”) which adopts the “Model 2” IGA arrangements. Under the US-Hong Kong IGA, FATCA reporting to the IRS is generally also required on certain holders of interests in the Trust and/or the Fund that are “Passive NFFEs with Controlling U.S. Persons”.

- (b) Under the terms of the current US-Hong Kong IGA, the Fund will not be required to withhold tax on payments made to Unitholders (unless such Unitholders are non-participating foreign financial institutions) or to close non-consenting accounts. However, in circumstances where, for example, it is identified that Units are held directly or indirectly by specified United States persons for FATCA reporting purposes and to the extent permitted by applicable laws and regulations, the Manager at its discretion may choose to redeem the Unitholder’s holding in the Trust and/or the Fund or to require such Unitholder to transfer such holding to a person who is not a specified United States person and/or beneficially owned/controlled by any specified United States persons and who is permitted in all other respects by the terms of this Explanatory Memorandum to be an eligible Unitholder (see further “Compulsory Redemption or Transfer of Units” in the “General Information” section). The Manager in taking any of the foregoing action shall act in good faith and on reasonable grounds and subject to compliance with applicable laws and regulations. The application of FATCA and the US-Hong Kong IGA, including the withholding rules and the information that may be required to be reported, may be subject to change.
- (c) The Trust is classified as a financial institution under FATCA. It has registered as a Model 2 Reporting Foreign Financial Institution (“FFI”) and is treated as having entered into an FFI agreement with the IRS to comply with all Reporting Financial Institution obligations under the US-Hong Kong IGA.
- (d) It should be noted that a number of jurisdictions, including Hong Kong, have entered into bilateral or multilateral agreements for the automatic exchange of financial account information under a regime known as the Common Reporting Standard (“CRS”) or the Standard for Automatic Exchange of Financial Account Information in Tax Matters (collectively “AEOI”) initiated by the Organisation for Economic Co-operation and Development (OECD). The Inland Revenue (Amendment) (No.3) Ordinance 2016 and subsequent relevant legislation (collectively, the “Ordinance”) constitute the legislative framework for the implementation in Hong Kong of the AEOI (or also referred to as the CRS). The AEOI requires financial institutions (“FI”) in Hong Kong to perform due diligence on the account holders, collect certain information (including, but not limited to, tax residence and taxpayer identification number etc.) relating to reportable accounts held by tax residents of reportable jurisdictions (within the meaning of the Ordinance (“Reportable Jurisdictions”)), and report such information to the Inland Revenue Department (“IRD”) which will exchange such information with the government authorities of the Reportable Jurisdictions.

The Trust is considered as a FI under the Ordinance and is required to comply with the requirements of AEOI as implemented by Hong Kong, which means that the Trust, the Fund and/or its agents shall collect and provide to the IRD the relevant information relating to Unitholders and prospective investors (and/or controlling person(s) of certain Unitholders / prospective investors) that are determined to be reportable accounts under the Ordinance. The Trust, the Fund and/or its agents may also collect information relating to residents of all jurisdictions.

The AEOI rules as implemented by Hong Kong under the Ordinance require the Trust, amongst other things: (i) register the Trust’s and/or the Fund’s status as a “Reporting Financial Institution” with the IRD after a “Reportable Account” is first maintained; (ii) conduct due diligence on its accounts (i.e., Unitholders) to identify whether any such accounts are considered “Reportable Accounts” for AEOI purposes; and (iii) report certain information on such Reportable Accounts to the IRD. The IRD is expected on an annual basis to transmit the information reported to it to the government authorities of the relevant Reportable Jurisdictions. Broadly, AEOI contemplates that Hong Kong FIs should report on: (i) individuals or certain entity account holders that are tax resident in a Reportable Jurisdiction; and (ii) controlling persons of certain entity account holders who are tax residents in Reportable Jurisdictions. Under the Ordinance, details of Unitholders, including but not limited to their name, date of birth, address, tax residence, taxpayer identification number(s), account details, account balance/value, and income or sale or redemption proceeds, may be reported to the IRD, which are subsequently exchanged with government authorities in the relevant Reportable Jurisdictions.

To assist in identifying Unitholders (and/or controlling person(s) of certain Unitholders) who are reportable persons, the Trust may require Unitholders and prospective investors (and/or controlling person(s) of certain Unitholders / prospective investors) to complete self-certification forms for verification of the Unitholders’ respective tax residence status (and/or the tax residence status of the controlling person(s) of certain Unitholders).

According to the due diligence procedures under the Ordinance (which are based on the international standard required), self-certification will be required for all new Unitholders or prospective investors (and/or controlling person(s) of certain Unitholders / prospective investors) who acquire Units on or after 1 January 2017. The Trust and/or the Fund reserves the right to require existing Unitholders before that date to verify their respective tax residences.

Further, if there is any change in circumstances that would affect an Unitholder’s tax residence status or if the Manager and/or the Trust’s agent knows, or has reason to know, that an Unitholder’s self-certification is incorrect or unreliable, a new self-certification and/or additional documentation may be required from the Unitholder. The Unitholder should notify the Manager and/or the Trust’s agent whenever any information provided to the Trust and/or the Fund is changed or becomes untrue, incomplete, inaccurate or misleading and provide the Manager and/or the Trust’s agent with an updated self-



certification and/or documentation within 30 days of such change in circumstances.

If the Unitholder does not provide the required information and/or documentation or fails to take action as is specified by the Manager and/or the Trust's agent within the time period specified, the Trust and/or the Fund may (i) report the relevant account information based on indicia identified pursuant to the requirements under the Ordinance and/or (ii) not accept the subscription from the prospective investor.

By investing in the Trust and/or the Fund and/or continuing to invest in the Trust, Unitholders acknowledge that they may be required to provide additional information to the Trust, the Manager and/or the Trust's agents in order for the Trust to fulfil its obligations under the Ordinance and comply with AEOL. The Unitholder's information (and/or information pertaining to controlling person(s) of certain Unitholders), if reportable, may be exchanged by the IRD with the government authorities of the Reportable Jurisdictions. The failure of a Unitholder to provide any requested information, may result in the Trust, the Manager and/or other agents of the Trust and/or the Fund taking any action and/or pursue remedies at their disposal including, without limitation, mandatory redemption or withdrawal of the Unitholder concerned. Any such mandatory redemption will be done in accordance with applicable laws and regulations, and the discretion to do so will be exercised by the Manager acting in good faith and on reasonable grounds.

Further, any non-compliance of the Ordinance by an Unitholder would be considered a violation of local law in Hong Kong and may result in penalties. Particularly, it is an offence under section 80(2E) of the Ordinance if any person, in making a self-certification, makes a statement that is misleading, false or incorrect in a material particular and knows, or is reckless as to whether, the statement is misleading, false or incorrect in a material particular. A person who commits the offence is liable on conviction to a fine at level 3 (i.e. HK\$10,000).

Each Unitholder and prospective investor should consult its own professional advisor(s) on the administrative and substantive implications of AEOL on its current or proposed investment in the Trust and/or the Fund.

- (e) While the Trust intends to satisfy its obligations under FATCA and AEOL and the associated implementing legislation in Hong Kong, to avoid the imposition of any FATCA Deductions and/or financial penalties and other sanctions, the ability to satisfy such obligations will depend on, among other things, receiving relevant information and/or documentation about each Unitholder and certain direct and indirect beneficial owners of the Units (if any). There can be no assurance that such obligations in relation to the Trust will be satisfied.
- (f) The Manager, Trustee and/or Registrar reserve the right to require any additional documentation or information from Unitholders and applicants for the purposes of the Trust being compliant with its obligations under FATCA and AEOL and any similar automatic exchange of tax information regimes. Unitholders refusing to provide the requisite information or documentation to the Trust may have their details and the details of their investments reported to the relevant tax authorities.
- (g) Each Unitholder or prospective investor should consult its own tax advisers on the requirements applicable to it and the potential implications under the FATCA and AEOL regimes on it and the Trust.
- (h) Unitholders and applicants are also recommended to check with their distributors and custodians as to their intention to comply with FATCA and AEOL.

#### *Other local tax authority requirements*

The Trust and/or the Fund will report personal and payment information of relevant Unitholders to the local tax authorities in accordance with local laws and regulations.

The Trust and/or the Fund will report personal and payment information of relevant Unitholders to other jurisdiction's tax authorities, such as the IRS, as required by local laws and regulations or pursuant to contractual obligations with foreign tax authorities.

#### *Withholdings and Deductions*

The Trustee or the Manager (acting in good faith and on reasonable grounds) on account of the Fund may be required to withhold on certain payments to a Unitholder when required by applicable laws and regulations or binding requirements of other jurisdictions' tax authorities. Under FATCA, for example, the Trustee or the Manager (acting in good faith and on reasonable grounds) on account of the Fund may be required to withhold on payments to certain Unitholders under future FATCA rules that may be issued by the United States on foreign passthru payments.

The Trust and/or the Fund may be required to account for tax on the value of the Units redeemed or transferred at the applicable rate unless it has received from the transferee sufficient documentation to confirm that the Unitholder is not a person in respect of whom it is necessary to deduct tax.

The Trust and/or the Fund reserves the right to redeem such number of Units held by a transferor as may be necessary to discharge the tax liability arising. The Trust and/or the Fund reserves the right to refuse to register a transfer of Units until it receives sufficient information as prescribed by the relevant authority to avoid such withholding.

The Trust and/or the Fund may be required to collect additional information from Unitholders, throughout the duration of the

relationship, between the Trust and/or the Fund and its Unitholders, as required by applicable laws and regulations or binding requirements of other jurisdictions' tax authorities, such as the IRS.

In addition to collecting additional information, the Trust and/or the Fund may require Unitholders to provide self-certifications or additional documents as required by applicable laws and regulations or binding requirements of other jurisdictions' tax authorities, such as the IRS.

## **GENERAL INFORMATION**

### **Financial Reports**

The Trust's year end is 30 June in each year. The Manager will notify Unitholders where the audited annual reports (in English) can be obtained (in printed and electronic forms) within four months of the end of each financial year, and where the half-yearly unaudited interim reports (in English) made up to the end of December each year can be obtained (in printed and electronic forms) within two months of the end of the period which they cover. Once issued, hard copies of such reports are available upon request of Unitholders free of charge at any time during normal business hours on any day (excluding Saturdays, Sundays and public holidays) at the offices of the Manager. Such reports will contain a statement of the Net Asset Value of each Sub-Fund and the investments comprising its portfolio.

### **Trust Deed**

The Trust was established under Hong Kong law by a trust deed made between the Manager and the Trustee. All Unitholders are entitled to the benefit of, are bound by and are deemed to have notice of the provisions of the Trust Deed.

The Trust Deed contains provisions for the indemnification of the Trustee and the Manager and their relief from liability in certain circumstances. Unitholders and intending applicants are advised to consult the terms of the Trust Deed.

### **Modification of Trust Deed**

The Trustee and the Manager may agree to modify the Trust Deed by supplemental deed provided that in the opinion of the Trustee such modification (i) is not materially prejudicial to the interests of Unitholders, does not operate to release to any material extent the Trustee, the Manager or any other person from any liability to the Unitholders and (with the exception of the costs of preparing and executing the relevant supplemental deed) does not increase the costs and charges payable out of the assets of the Trust or (ii) is necessary in order to comply with any fiscal, statutory, regulatory or official requirement or (iii) is made to correct a manifest error. In all other cases involving any material changes, any modification to the Trust Deed will require the sanction of an extraordinary resolution of the Unitholders affected and/or the prior approval of the SFC (if required under the Code).

Any modifications to the Trust Deed will be notified to the Unitholders in accordance with the applicable requirements under the Code.

### **Meetings of Unitholders**

The Trust Deed provides for meetings of Unitholders to be convened by the Trustee or the Manager upon at least 21 days' notice. Notices of meetings of Unitholders will be posted to Unitholders.

Proxies may be appointed. The quorum at Unitholders' meetings is Unitholders present in person or by proxy holding not less than 10% (or, in relation to a resolution proposed as an extraordinary resolution, 25%) of the Units in issue. If a quorum is not present, the meeting will be adjourned for not less than 15 days. Separate notice of any adjourned meeting will be given, and at an adjourned meeting Unitholders whatever their number or the number of Units held by them will form a quorum.

An extraordinary resolution is required under the Trust Deed for certain purposes and is a resolution proposed as such and passed by a majority of 75% of the total number of votes cast.

The Trust Deed contains provisions for the holding of separate meetings of Unitholders in different Sub-Funds where only the interests of Unitholders in a particular Sub-Fund are affected.

The Trust Deed provides that at any meeting of Unitholders, on a show of hands, every Unitholder who (being an individual) is present in person or (being a partnership or corporation) is present by an authorised representative shall have one vote and, on a poll, every Unitholder who is present as aforesaid or by proxy shall have one vote for every Unit of which he is the holder.

For the avoidance of doubt, for so long as the Trust and the Fund is authorized by the SFC, at any meeting of Unitholders, any resolution put to the vote of the meeting shall be decided by way of poll.

### **Transfer of Units**

Subject as provided below, Units may be transferred by an instrument in writing in common form signed by (or, in the case of a body corporate, signed on behalf of or sealed by) the transferor and the transferee. The transferor will be deemed to remain the

holder of the Units transferred until the name of the transferee is entered in the Register of Unitholders in respect of such Units.

Each instrument of transfer must relate to a single class of Units only. No Units may be transferred if, as a result, either the transferor or the transferee would hold Units having a value less than the minimum holding amount in the relevant Sub-Fund. Notwithstanding the foregoing, all Unit transfers are subject to the Restrictions described below.

### **Compulsory Redemption or Transfer of Units**

The Manager may from time to time impose such restrictions as it may think necessary for the purpose of ensuring that no Units are acquired or held by any person in circumstances (the “**relevant circumstances**”):

- A. which might constitute a breach of the law or governmental regulation (or any interpretation of a law or regulation by a competent authority) of any country or territory; or
- B. which might require the Trust, the Fund or any class or classes of Units or the Manager to be registered under any law or regulation of any country or territory or cause the Trust or the Fund to apply for registration or comply with any registration requirements in respect of any of its Units whether in the United States or any other jurisdiction in which it is not currently registered; or
- C. which (or would if other Units were acquired or held in the circumstances), in the opinion of the Manager, might result in the Trust, the Fund, the Unitholders, the Manager or the Trustee incurring any liability to taxation or suffering any other legal, regulatory, pecuniary or other adverse consequences which it or they might not have otherwise incurred or suffered or which, in the opinion of the Manager, might result in the Manager, the Trustee, the Unitholders, the Fund or the Trust becoming subject to any law or regulation to which the Manager, the Trustee, the Unitholders, the Fund or the Trust might not otherwise have become subject: or
- D. where such person is a US Person or is holding the Units for the account or benefit of a US Person (other than pursuant to an exemption available under US federal and state securities laws); or
- E. where such person is resident or otherwise located in Canada. The Fund is not currently qualified for sale, and the Trust, the Fund nor Manager are registered or exempt from registration as a dealer, adviser or investment fund manager, in any province or territory of Canada. Any investment in Units by or on behalf of a person resident or otherwise located in Canada is prohibited.

If the Manager becomes aware that any Units are owned directly, indirectly or beneficially in contravention of any of A to E above (the “**Restrictions**”) and provided that the Manager acts in good faith, on reasonable grounds and pursuant to applicable laws and regulations:

- (a) the Manager may give notice to such person requiring him to transfer such Units to a person who would not thereby be in contravention of any of the Restrictions; or
- (b) the Manager may give a request in writing for the redemption of such Units.

Any Unitholder who receives a notice pursuant to (a) above must transfer his Units within 10 days of the notice or satisfy the Manager that the Units are not held in contravention of any of the Restrictions, failing which he shall be deemed to have given a request in writing for the redemption of all his Units.

Any Unitholder who becomes aware that he holds or owns Units in contravention of any of the Restrictions must, unless he has already received a notice pursuant to (a) above, either transfer all his Units to a person who would not thereby be in contravention of any of the Restrictions or give a request in writing for the redemption of all his Units.

### **Termination of the Trust and/or a Sub-Fund**

The Trust shall continue for a period of 80 years from the date of the Trust Deed or until it is terminated in one of the ways set out in the Trust Deed, as summarised below.

- 1. The Trustee may terminate the Trust (including any Sub-Fund) if:–
  - (a) the Manager goes into liquidation (except a voluntary liquidation for the purpose of reconstruction or amalgamation upon terms previously approved by the Trustee) or if a receiver is appointed over any of its assets and not discharged within 60 days; or
  - (b) in the opinion of the Trustee, the Manager is incapable of performing its duties properly as provided for under the Trust Deed; or
  - (c) the Trust ceases to be authorised pursuant to the Securities and Futures Ordinance of Hong Kong or if any law is passed which renders it illegal or in the opinion of the Trustee impracticable or inadvisable to continue the Trust; or

- (d) the Manager ceases to manage the Trust and the Trustee fails to appoint a successor Manager within a period of 30 days; or
  - (e) if the Trustee wishes to retire as trustee of the Trust and the Manager fails to appoint a successor Trustee.
2. The Manager may terminate the Trust and/or a Sub-Fund if:–
- (a) the Trust and/or the relevant Sub-Fund (as the case may be) ceases to be authorised pursuant to the Securities and Futures Ordinance of Hong Kong; or
  - (b) any law is passed which renders it illegal or in the opinion of the Manager impracticable or inadvisable to continue the Trust and/or the relevant Sub-Fund.
3. The Manager may terminate a Sub-Fund at any time on giving at least three months' notice to holders of Units in that Sub-Fund if the Net Asset Value of such Sub-Fund falls below US\$5,000,000.

Where the Trust or any Sub-Fund is terminated as provided in paragraphs 1, 2 or 3 above, the party terminating the Trust must give at least three months' notice of termination to Unitholders.

Any unclaimed proceeds or other cash held by the Trustee upon termination of the Trust and/or any Sub-Fund (as the case may be) may at the expiration of twelve months from the date upon which the same were payable be paid into court subject to the right of the Trustee to deduct therefrom any expenses it may incur in making such payment.

### **Conflicts of Interest**

The Manager, the Trustee and their respective connected persons may from time to time act as trustee, administrator, registrar, transfer agent, manager, custodian, investment manager or investment adviser, representative or otherwise as may be required from time to time in relation to, or be otherwise involved in or with, other funds and clients including those which have similar investment objectives to those of any Sub-Fund or contract with or enter into financial, banking or other transaction with one another or with any investor of the Sub-Funds, or any company or body any of whose shares or securities form part of any Sub-Fund or may be interested in any such contract or transaction. It is, therefore, possible that any of them may, in the course of business, have potential conflicts of interest with the Trust and/or the relevant Sub-Fund.

The Manager, the Trustee and their respective connected persons may deal with a connected person as broker/trading counterparty in the sale or purchase of securities and other investments for the Fund, subject to the requirements set out in the section entitled "Transactions with Connected Persons". The Fund may also invest in a collective investment scheme managed by the Manager or any of its connected persons, subject to the relevant limit set out in Schedule 1 to this Explanatory Memorandum, of which all initial charges and redemption charges must be waived and there should be no increase in management fee borne by the Fund. The Manager will take all reasonable steps to identify, prevent, manage and monitor any actual or potential conflicts of interest including conducting all transactions in good faith at arm's length and in the best interests of the Trust and the Fund on normal commercial terms. If such conflicts arise, each will, at all times, have regard in such event to its obligations to the Trust and will endeavour to ensure that such conflicts are managed and minimised so far as reasonably practicable and that measures are adopted that seek to ensure such conflicts are resolved fairly, taking into account the interests of Unitholders of the relevant Sub-Fund as a whole. In any event, the Manager shall ensure that all investment opportunities will be fairly allocated.

The Manager may from time to time undertake sale and purchase transactions in the same security between client accounts or funds (collectively referred to hereinafter as "**clients**") (cross trades) under its management. This may give rise to potential conflicts of interest for example where there is a difference in the compensation the Manager receives for different clients. To manage this potential conflict, the Manager will only undertake cross trades where (i) the sale and purchase decisions are in the best interests of both clients and fall within the investment objectives, restrictions and policies of both clients, (ii) the trades are executed on arm's length terms at current market value, (iii) the reason for such trades is documented prior to execution, and (iv) such activity is disclosed to the client. Any cross-trades conducted by the Manager must be undertaken in accordance with the SFC's Fund Manager Code of Conduct.

### **Anti-Money Laundering Regulations**

As part of the Registrar's, the Trustee's and the Manager's responsibility to prevent money laundering, they may require detailed verification of an investor's identity and the source of the payment of application monies. The Registrar, the Trustee and the Manager reserve the right to request such information as is necessary to verify the identity of an applicant and the source of the payment. In the event of delay or failure by the applicant to produce any information required for verification purposes, the Registrar, the Trustee and/or the Manager may refuse to accept the application and the application moneys relating to such application.

### **Documents Available For Inspection**

Copies of the Trust Deed are available for inspection free of charge at any time during normal business hours on any day (excluding Saturdays, Sundays and public holidays) or for purchase on payment of a reasonable fee at the offices of the Manager, Level 25, One Exchange Square, 8 Connaught Place, Central, Hong Kong.

**Enquiries and complaints handling**

Investors may contact the Manager if they have any enquiries or complaints in respect of the Fund at the Investor Services Hotline at (852) 2846 7566. Depending on the subject matter of the enquiries or complaints, these will be dealt with either by the Manager directly, or referred to the relevant parties for further handling. The Manager will, on a best effort basis, revert and address the investor's enquiries and complaints as soon as practicable.



## SCHEDULE 1 – INVESTMENT AND BORROWING RESTRICTIONS

### 1. Investment limitations applicable to each Sub-Fund

No holding of any security may be acquired for or added to a Sub-Fund which would be inconsistent with achieving the investment objective of the Sub-Fund or which would result in or no cash deposits may be made which would result in:

- (a) the aggregate value of the Sub-Fund's investments in, or exposure to, any single entity (other than Government and other public securities) through the following exceeding 10% of the latest available Net Asset Value of the relevant Sub-Fund:
  - (i) investments in securities issued by that entity;
  - (ii) exposure to that entity through underlying assets of financial derivative instruments; and
  - (iii) net counterparty exposure to that entity arising from transactions of OTC financial derivative instruments.

For the avoidance of doubt, restrictions and limitations on counterparty as set out in sub-paragraphs 1(a), 1(b) and 3.4(c) of this Schedule 1 will not apply to financial derivative instruments that are:

- (A) transacted on an exchange where the clearing house performs a central counterparty role; and
- (B) marked-to-market daily in the valuation of their financial derivative instrument positions and subject to margining requirements at least on a daily basis.

The requirements under this sub-paragraph 1(a) will also apply in the case of sub-paragraphs 5(e) and (j) of this Schedule 1.

- (b) subject to sub-paragraphs 1(a) and 3.4(c) of this Schedule 1, the aggregate value of the Sub-Fund's investments in, or exposure to, entities within the same group through the following exceeding 20% of the latest available Net Asset Value of the relevant Sub-Fund:
  - (i) investments in securities issued by those entities;
  - (ii) exposure to those entities through underlying assets of financial derivative instruments; and
  - (iii) net counterparty exposure to those entities arising from transactions of OTC financial derivative instruments.

For the purposes of sub-paragraphs 1(b) and 1(c) of this Schedule 1, "entities within the same group" means entities which are included in the same group for the purposes of consolidated financial statements prepared in accordance with internationally recognized accounting standards.

The requirements under this sub-paragraph 1(b) will also apply in the case of sub-paragraphs 5(e) and (j) of this Schedule 1.

- (c) the value of the Sub-Fund's cash deposits made with the same entity or entities within the same group exceeding 20% of the latest available Net Asset Value of the relevant Sub-Fund provided that the 20% limit may be exceeded in the following circumstances:
  - (i) cash held before the launch of the Sub-Fund and for a reasonable period thereafter prior to the initial subscription proceeds being fully invested; or
  - (ii) cash proceeds from liquidation of investments prior to the merger or termination of the Sub-Fund, whereby the placing of cash deposits with various financial institutions would not be in the best interests of investors; or
  - (iii) cash proceeds received from subscriptions pending investments and cash held for the settlement of redemption and other payment obligations, whereby the placing of cash deposits with various financial institutions would be unduly burdensome and the cash deposits arrangement would not compromise investors' interests.

For the purposes of this sub-paragraph 1(c), "cash deposits" generally refer to those that are repayable on demand or have the right to be withdrawn by the Sub-Fund and not referable to provision of property or services.

- (d) the Sub-Fund's holding of any ordinary shares (when aggregated with all other Sub-Funds' holdings of such ordinary shares) exceeding 10% of any ordinary shares issued by any single entity.

- (e) the value of the Sub-Fund's investment in securities and other financial products or instruments that are neither listed, quoted nor dealt in on a market (being any stock exchange, OTC market or other organised securities market which is open to the international public and on which such securities are regularly traded) exceeding 15% of the latest available Net Asset Value of such Sub-Fund.
- (f) the value of the Sub-Fund's total holding of Government and other public securities of the same issue exceeding 30% of the latest available Net Asset Value of such Sub-Fund. Subject to the foregoing statement, the Sub-Fund may invest all of its assets in Government and other public securities in at least six different issues. For the avoidance of doubt, Government and other public securities will be regarded as being of a different issue if, even though they are issued by the same person, they are issued on different terms whether as to repayment dates, interest rates, the identity of the guarantor, or otherwise.
- (g) (i) the value of the Sub-Fund's investment in units or shares in other collective investment schemes (namely "**underlying schemes**") which are non-eligible schemes (the list of "eligible schemes" is as specified by the SFC from time to time) and not authorized by the SFC in aggregate exceeding 10% of its latest available Net Asset Value; and  
(ii) the value of the Sub-Fund's investment in units or shares in each underlying scheme which is either an eligible scheme (the list of "eligible schemes" is as specified by the SFC from time to time) or a scheme authorized by the SFC exceeding 30% of its latest available Net Asset Value unless the underlying scheme is authorized by the SFC, and the name and key investment information of the underlying scheme are disclosed in the Offering Document of that Sub-Fund,

provided that:

- (A) no investment may be made in any underlying scheme the investment objective of which is to invest primarily in any investment prohibited by Chapter 7 of the Code;
- (B) where an underlying scheme's objective is to invest primarily in investments restricted by Chapter 7 of the Code, such investments may not be in contravention of the relevant limitation. For the avoidance of doubt, a Sub-Fund may invest in underlying scheme(s) authorized by the SFC under Chapter 8 of the Code (except for hedge funds under 8.7 of the Code), eligible scheme(s) of which the net derivative exposure does not exceed 100% of its total net asset value, and Qualified Exchange Traded Funds in compliance with sub-paragraphs 1(g)(i) and (ii) of this Schedule 1;
- (C) the underlying scheme's objective may not be to invest primarily in other collective investment scheme(s);
- (D) all initial charges and redemption charges on the underlying scheme(s) must be waived if the underlying scheme is managed by the Manager or its connected persons; and
- (E) the Manager or any person acting on behalf of the Sub-Fund or the Manager may not obtain a rebate on any fees or charges levied by an underlying scheme or its management company, or any quantifiable monetary benefits in connection with investments in any underlying scheme.

For the avoidance of doubt:

- (aa) unless otherwise provided under the Code, the spread requirements under sub-paragraphs 1(a), (b), (d) and (e) of this Schedule 1 do not apply to investments in other collective investment schemes by a Sub-Fund;
- (bb) the investment by a Sub-Fund in a Qualified Exchange Traded Fund may either be considered and treated as (i) listed securities for the purposes of and subject to the requirements in sub-paragraphs 1(a), (b) and (d) of this Schedule 1; or (ii) collective investment schemes for the purposes of and subject to the requirements in sub-paragraphs 1(g)(i) and (ii) and proviso (A) to (C) of sub-paragraph 1(g) of this Schedule 1. Notwithstanding the aforesaid, the investments by a Sub-Fund in Qualified Exchange Traded Funds shall be subject to sub-paragraph 1(e) of this Schedule 1 and the relevant investment limits in Qualified Exchange Traded Funds by a Sub-Fund shall be consistently applied. Unless otherwise disclosed in respect of a particular Sub-Fund, investment by a Sub-Fund in a Qualified Exchange Traded Fund is considered and treated as listed securities for the purposes of and subject to the requirements in sub-paragraphs 1(a), (b) and (d) of this Schedule 1;
- (cc) where investments are made in listed REITs, the requirements under sub-paragraphs 1(a), (b) and (d) of this Schedule 1 apply and where investments are made in unlisted REITs, which are either companies or collective investment schemes, then the requirements under sub-paragraphs 1(e) and (g)(i) of this Schedule 1 apply respectively; and
- (dd) where a Sub-Fund invests in index-based financial derivative instruments, the underlying assets of such financial derivative instruments are not required to be aggregated for the purposes of the investment restrictions or limitations set out in sub-paragraphs 1(a), (b), (c) and (f) of this Schedule 1 provided that the index is in compliance with the requirements under 8.6(e) of the Code.

## 2. Investment prohibitions applicable to each Sub-Fund

The Manager shall not, unless otherwise specifically provided for in the Code, on behalf of any Sub-Fund:-

- (a) invest in physical commodities unless otherwise approved by the SFC on a case-by-case basis taking into account the liquidity of the physical commodities concerned and availability of sufficient and appropriate additional safeguards where necessary;
- (b) invest in any type of real estate (including buildings) or interests in real estate (including any options or rights but excluding shares in real estate companies and interests in REITs);
- (c) make short sales unless (i) the liability of the relevant Sub-Fund to deliver securities does not exceed 10% of its latest available Net Asset Value; (ii) the security which is to be sold short is actively traded on a securities market where short selling activity is permitted; and (iii) the short sales are carried out in accordance with all applicable laws and regulations;
- (d) carry out any naked or uncovered short sale of securities;
- (e) subject to sub-paragraph 1(e) of this Schedule 1, lend, assume, guarantee, endorse or otherwise become directly or contingently liable for or in connection with any obligation or indebtedness of any person. For the avoidance of doubt, reverse repurchase transactions in compliance with the requirements as set out in sub-paragraphs 4.1 to 4.4 of this Schedule 1 are not subject to the limitations in this sub-paragraph 2(e);
- (f) acquire any asset or engage in any transaction which involves the assumption of any liability by the relevant Sub-Fund which is unlimited. For the avoidance of doubt, the liability of Unitholders of a Sub-Fund is limited to their investments in that Sub-Fund;
- (g) invest in any security of any class in any company or body if any director or officer of the Manager individually owns more than 0.5%, or collectively they own more than 5%, of the total nominal amount of all the issued securities of that class; and
- (h) invest in any security where a call is to be made for any sum unpaid on that security, unless the call could be met in full out of cash or near cash from the Sub-Fund's portfolio whereby such amount of cash or near cash has not been segregated to cover a future or contingent commitment arising from transaction in financial derivative instruments for the purposes of sub-paragraphs 3.5 and 3.6 of this Schedule 1.

## 3. Use of financial derivative instruments

- 3.1 A Sub-Fund may acquire financial derivative instruments for hedging purposes. For the purposes of this sub-paragraph 3.1, financial derivative instruments are generally considered as being acquired for hedging purposes if they meet all the following criteria:
- (a) they are not aimed at generating any investment return;
  - (b) they are solely intended for the purpose of limiting, offsetting or eliminating the probability of loss or risks arising from the investments being hedged;
  - (c) although they may not necessarily reference to the same underlying assets, they should relate to the same asset class with high correlation in terms of risks and return, and involve taking opposite positions, in respect of the investments being hedged; and
  - (d) they exhibit price movements with high negative correlation with the investments being hedged under normal market conditions.

The Manager, where it deems necessary, shall cause hedging arrangement to be adjusted or re-positioned, with due consideration on the fees, expenses and costs, to enable the relevant Sub-Fund to meet its hedging objective in stressed or extreme market conditions.

- 3.2 A Sub-Fund may also acquire financial derivative instruments for non-hedging purposes ("**investment purposes**") subject to the limit that such Sub-Fund's net exposure relating to these financial derivative instruments ("**net derivative exposure**") does not exceed 50% of its latest available Net Asset Value provided that such limit may be exceeded in such circumstances as permitted under the Code, handbook, code and/or guideline issued by the SFC from time to time or permitted by the SFC from time to time.

For the avoidance of doubt, financial derivative instruments acquired for hedging purposes under sub-paragraph 3.1 of this Schedule 1 will not be counted towards the 50% limit referred to in this sub-paragraph 3.2 so long as there is no residual derivative exposure arising from such hedging arrangement. Net derivative exposure shall be calculated

in accordance with the Code and the requirements and guidance issued by the SFC which may be updated from time to time.

- 3.3 Subject to sub-paragraphs 3.2 and 3.4 of this Schedule 1, a Sub-Fund may invest in financial derivative instruments provided that the exposure to the underlying assets of the financial derivative instruments, together with the other investments of the Sub-Fund, may not in aggregate exceed the corresponding investment restrictions or limitations applicable to such underlying assets and investments as set out in sub-paragraphs 1(a), (b), (c), (f), (g)(i) and (ii), proviso (A) to (C) to sub-paragraph 1(g), proviso (cc) to sub-paragraph 1(g) and sub-paragraph 2(b) of this Schedule 1.
- 3.4 The financial derivative instruments invested by a Sub-Fund shall be either listed/quoted on a stock exchange or dealt in OTC market and comply with the following provisions:
- (a) the underlying assets consist solely of shares in companies, debt securities, money market instruments, units/shares of collective investment schemes, deposits with substantial financial institutions, Government and other public securities, highly-liquid physical commodities (including gold, silver, platinum and crude oil), financial indices, interest rates, foreign exchange rates, currencies, or other asset classes acceptable to the SFC, in which the Sub-Fund may invest according to its investment objectives and policies;
  - (b) the counterparties to transactions of OTC financial derivative instruments or their guarantors are substantial financial institutions or such other entity acceptable to the SFC;
  - (c) subject to sub-paragraphs 1(a) and (b) of this Schedule 1, a Sub-Fund's net counterparty exposure to a single entity arising from transactions of OTC financial derivative instruments may not exceed 10% of its latest available Net Asset Value provided that the exposure of the Sub-Fund to a counterparty of OTC financial derivative instruments may be lowered by the collateral received (if applicable) by the Sub-Fund and shall be calculated with reference to the value of collateral and positive mark to market value of the OTC financial derivative instruments with that counterparty, if applicable; and
  - (d) the valuation of the financial derivative instruments is marked-to-market daily, subject to regular, reliable and verifiable valuation conducted by the Manager or the Trustee or their nominee(s), agent(s) or delegate(s) (as the case may be) independent of the issuer of the financial derivative instruments through measures such as the establishment of a valuation committee or engagement of third party services. The financial derivative instruments can be sold, liquidated or closed by an offsetting transaction at any time at their fair value at the Sub-Fund's initiative. Further, the Manager or the Trustee or their nominee(s), agent(s) or delegate(s) (as the case may be) should be adequately equipped with the necessary resources to conduct independent marked-to-market valuation and to verify the valuation of the financial derivative instruments on a regular basis.
- 3.5 A Sub-Fund should at all times be capable of meeting all its payment and delivery obligations incurred under transactions in financial derivative instruments (whether for hedging or for investment purposes). The Manager shall, as part of its risk management process, monitor to ensure that the transactions in financial derivative instruments in respect of a Sub-Fund are adequately covered on an ongoing basis. For the purposes of this sub-paragraph 3.5, assets that are used to cover the Sub-Fund's payment and delivery obligations incurred under transactions in financial derivative instruments shall be free from any liens and encumbrances, exclude any cash or near cash for the purpose of meeting a call on any sum unpaid on a security, and cannot be applied for any other purposes.
- 3.6 Subject to sub-paragraph 3.5 of this Schedule 1, a transaction in financial derivative instruments which gives rise to a future commitment or contingent commitment of a Sub-Fund shall be covered as follows:
- (a) in the case of financial derivative instruments transactions which will, or may at the Sub-Fund's discretion, be cash settled, the Sub-Fund shall at all times hold sufficient assets that can be liquidated within a short timeframe to meet the payment obligation; and
  - (b) in the case of financial derivative instruments transactions which will, or may at the counterparty's discretion, require physical delivery of the underlying assets, the Sub-Fund shall hold the underlying assets in sufficient quantity at all times to meet the delivery obligation. If the Manager considers the underlying assets to be liquid and tradable, the Sub-Fund may hold other alternative assets in sufficient quantity as cover, provided that such assets may be readily converted into the underlying assets at any time to meet the delivery obligation provided further that the Sub-Fund shall apply safeguard measures such as to apply haircut where appropriate to ensure that such alternative assets held are sufficient to meet its future obligations.
- 3.7 The requirements under sub-paragraphs 3.1 to 3.6 of this Schedule 1 shall apply to embedded financial derivative. For the purposes of this Explanatory Memorandum, an **"embedded financial derivative"** is a financial derivative instrument that is embedded in another security.

#### 4. Securities financing transactions

- 4.1 A Sub-Fund may engage in securities financing transactions, provided that they are in the best interests of

Unitholders of such Sub-Fund to do so and the associated risks have been properly mitigated and addressed, and provided further that the counterparties to the securities financing transactions are financial institutions which are subject to ongoing prudential regulation and supervision.

- 4.2 A Sub-Fund shall have at least 100% collateralization in respect of the securities financing transaction(s) into which it enters to ensure there is no uncollateralized counterparty risk exposure arising from these transactions.
- 4.3 All the revenues arising from securities financing transactions, net of direct and indirect expenses as reasonable and normal compensation for the services rendered in the context of the securities financing transactions, shall be returned to the Sub-Fund.
- 4.4 A Sub-Fund shall only enter into a securities financing transaction if the terms of such securities financing transaction include the power for the Sub-Fund at any time to recall the securities or the full amount of cash (as the case may be) subject to the securities financing transaction or terminate the securities financing transaction(s) into which it has entered.

## 5. Collateral

In order to limit the exposure to each counterparty as set out in sub-paragraph 3.4(c) and 4.2 of this Schedule 1, a Sub-Fund may receive collateral from such counterparty, provided that the collateral complies with the requirements set out below:

- (a) Liquidity – the collateral is sufficiently liquid and tradable in order that it can be sold quickly at a robust price that is close to pre-sale valuation. Collateral should normally trade in a deep and liquid marketplace with transparent pricing;
- (b) Valuation – the collateral is marked-to-market daily by using independent pricing sources;
- (c) Credit quality – the collateral is of high credit quality provided that, in the event the credit quality of the collateral or the issuer of the asset being used as collateral has deteriorated to such a degree that it would undermine the effectiveness of the collateral, such collateral shall be replaced immediately;
- (d) Haircut – the collateral is subject to a prudent haircut policy;
- (e) Diversification – the collateral is appropriately diversified so as to avoid concentrated exposure to any single entity and/or entities within the same group. A Sub-Fund's exposure to the issuer(s) of the collateral should be taken into account in compliance with the investment restrictions and limitations set out in sub-paragraphs 1(a), 1(b), 1(c), 1(f), 1(g)(i) and (ii) and provisos (A) to (C) of sub-paragraph 1(g) and sub-paragraph 2(b) of this Schedule 1;
- (f) Correlation – the value of the collateral should not have any significant correlation with the creditworthiness of the counterparty or the issuer of the financial derivative instruments, or the counterparty of securities financing transactions in such a way that would undermine the effectiveness of the collateral. For this purpose, securities issued by the counterparty or the issuer of the financial derivative instruments, or the counterparty of securities financing transactions or any of their related entities should not be used as collateral;
- (g) Management of operational and legal risks – the Manager has appropriate systems, operational capabilities and legal expertise for proper collateral management;
- (h) Independent custody – the collateral is held by the Trustee or by duly appointed nominee, agent or delegate;
- (i) Enforceability – the collateral is readily accessible or enforceable by the Trustee without further recourse to the issuer of the financial derivative instruments, or the counterparty of the securities financing transactions;
- (j) Re-investment of collateral – any re-investment of collateral received for the account of the relevant Sub-Fund shall be subject to the following requirements:
  - (i) cash collateral received may only be reinvested in short-term deposits, high quality money market instruments and money market funds authorized under 8.2 of the Code or regulated in a manner generally comparable with the requirements of the SFC and acceptable to the SFC, and subject to corresponding investment restrictions or limitations applicable to such investments or exposure as set out in Chapter 7 of the Code. For this purpose, money market instruments refer to securities normally dealt in on the money markets, including government bills, certificates of deposit, commercial papers, short-term notes and bankers' acceptances, etc. In assessing whether a money market instrument is of high quality, at a minimum, the credit quality and the liquidity profile of the money market instruments must be taken into account;
  - (ii) non-cash collateral received may not be sold, re-invested or pledged;
  - (iii) the portfolio of assets from re-investment of cash collateral shall comply with the requirements as set out in 8.2 (f) and 8.2(n) of the Code;



- (iv) cash collateral received is not allowed to be further engaged in any securities financing transactions;
- (v) when the cash collateral received is reinvested into other investment(s), such investment(s) is/are not allowed to be engaged in any securities financing transactions;
- (k) the collateral is free of prior encumbrances; and
- (l) the collateral generally does not include (i) structured products whose payouts rely on embedded financial derivatives or synthetic instruments; (ii) securities issued by special purpose vehicles, special investment vehicles or similar entities; (iii) securitized products; or (iv) unlisted collective investment schemes.

Further details relating to the collateral policy of the Fund are disclosed in Schedule 2 to this Explanatory Memorandum.

## **6. Borrowing and Leverage**

The expected maximum level of leverage of each Sub-Fund is as follows:

### *Cash borrowing*

- 6.1 No borrowing shall be made in respect of a Sub-Fund which would result in the principal amount for the time being of all borrowings made pursuant to the Deed for the account of the relevant Sub-Fund exceeding an amount equal to 10% of the latest available Net Asset Value of the relevant Sub-Fund provided always that back-to-back loans do not count as borrowing. For the avoidance of doubt, securities lending transactions and sale and repurchase transactions in compliance with the requirements as set out in sub-paragraphs 4.1 to 4.4 of this Schedule 1 are not borrowings for the purpose of, and are not subject to the limitations in this sub-paragraph 6.1.

### *Leverage from the use of financial derivative instruments*

- 6.2 A Sub-Fund may also be leveraged through the use of financial derivative instruments. The expected maximum level of leverage through the use of financial derivative instruments (i.e. expected maximum net derivative exposure) of the Fund is 50% of its latest available Net Asset Value.
- 6.3 In calculating the net derivative exposure, derivatives acquired for investment purposes that would generate incremental leverage at the portfolio level of the relevant Sub-Fund are converted into their equivalent positions in their underlying assets. The net derivative exposure is calculated in accordance with the requirements and guidance by the SFC which may be updated from time to time.
- 6.4 The actual level of leverage may be higher than such expected level in exceptional circumstances, for example when there are sudden movements in markets and/or investment prices.

## **7. Name of Sub-Fund**

If the name of a Sub-Fund indicates a particular objective, investment strategy, geographic region or market, the Sub-Fund must, under normal market circumstances, invest at least 70% of its Net Asset Value in securities and other investments to reflect the particular objective, investment strategy or geographic region or market which the Sub-Fund represents.

## **SCHEDULE 2 – COLLATERAL VALUATION AND MANAGEMENT POLICY**

The Manager employs a collateral management policy in relation to collateral received in respect of OTC derivative transactions entered into in respect of a Sub-Fund. A Sub-Fund may receive collateral from a counterparty to an OTC derivative transaction in order to reduce its counterparty risk exposure, subject to the investment restrictions and requirements applicable to collateral under Schedule 1 to this Explanatory Memorandum.

### **Nature and quality of the collateral**

A Sub-Fund may receive cash as collateral from a counterparty to an OTC derivative transaction entered into in respect of the relevant Sub-Fund. For the avoidance of doubt, the Manager currently does not intend to seek or receive any other form of collateral in respect of any OTC derivative transactions entered into in respect of a Sub-Fund.

### **Criteria for selecting counterparties**

The Manager has counterparty selection policies and control measures to manage the credit risks of counterparties of OTC derivative transactions which shall include amongst other considerations, fundamental creditworthiness (e.g. ownership structure, financial strength) and commercial reputation of specific legal entities in conjunction with the nature and structure of proposed trading activities, external credit ratings of the counterparty, the regulatory supervision applied to the relevant counterparty, country of origin of the counterparty and legal status of the counterparty.

The counterparties of OTC derivative transactions will be entities with legal personality typically located in OECD jurisdictions (but may also be located outside such jurisdictions), and be subject to ongoing supervision by a regulatory authority.

The counterparty to an OTC derivative transaction must have a minimum credit rating of bbb- or equivalent assigned by an internationally recognised credit agency (e.g. Standard & Poor's or Moody's). Alternatively, an unrated counterparty will be acceptable where the Manager is indemnified or guaranteed against losses suffered as a result of a failure by the counterparty, by an entity which has and maintains a rating of bbb- or equivalent assigned by an internationally recognised credit agency (e.g. Standard & Poor's or Moody's).

### **Diversification and correlation of collateral**

Collateral must be sufficiently diversified. The exposures of a Sub-Fund to the collateral issuers are monitored in accordance with the relevant restrictions on exposure to a single entity and/or entities within the same group as set out in in Schedule 1 to this Explanatory Memorandum.

Collateral received must be issued by an entity that is independent from the relevant counterparty.

### **Cash collateral reinvestment policy**

The Manager currently does not intend to reinvest any cash collateral received in relation to an OTC derivative transaction in respect of a Sub-Fund. Should this intention change in the future, (a) cash collateral received by a Sub-Fund may be reinvested in short-term deposits, high quality money market instruments and money market funds authorized under 8.2 of the Code or regulated in a manner generally comparable with the requirements of the SFC and acceptable to the SFC, subject to the applicable restrictions in respect of collateral in Schedule 1 to this Explanatory Memorandum; and (b) up to 100% of the cash collateral received by a Sub-Fund may be reinvested.

### **Safe-keeping of collateral**

Any cash collateral received by a Sub-Fund from a counterparty in respect of an OTC derivative transaction is to be held in custody by the Trustee or a Correspondent.

A description of collateral holdings of a Sub-Fund will be disclosed in its interim and annual financial reports as required under Appendix E of the Code.

Assets provided by a Sub-Fund on a title transfer basis shall no longer belong to the Sub-Fund. The counterparty may use those assets at its absolute discretion. Assets provided to a counterparty other than on a title transfer basis shall be held by the Trustee or a Correspondent.

### **Enforceability of collateral**

Any collateral received by a Sub-Fund (subject to any net-off or set-off, if applicable) is capable of being fully enforced by the Manager at any time without further recourse to the counterparty.

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\* The SFC has not reviewed the contents of this website.

