AGF China Focus Class

FUND COMMENTARY FIRST QUARTER 2017 **FOR ADVISOR USE WITH INVESTORS**

FUND FACTS

FUND CATEGORY:	BENCHMARK INDEX:	DATE OF INCEPTION:	INVESTMENT STYLE:	PORTFOLIO MANAGER:	PORTFOLIO ADVISOR†:
Greater China equity	MSCI China Free Total Return Index	April 1994	Growth at a reasonable price (GARP)	AGF Investments Inc.	AGF Asset Management Asia Ltd. Eng Hock Ong, MBA, CFA

Market overview

During the quarter ended March 31, 2017, China's stock market performed strongly on the back of an improving corporate earnings outlook and stabilization in the renminbi. Strong southbound inflows from mainland Chinese investors into the Hong Kong stock market through Stock Connect also helped sentiment. The MSCI China Free Index ended up 11.9% in Canadian dollar terms for the quarter.

The strong economic growth momentum experienced in the fourth quarter of 2016 continued into the first quarter of this year. Recent macroeconomic indicators are supportive of further improvement in China. The official manufacturing Purchasing Managers' Index (PMI) has held above 51 for six consecutive months and reached 51.8 in March, the highest level since April 2012. Meanwhile, strong momentum within the services sector continued, with the non-manufacturing PMI consistently above 54 since October 2016. China is also benefiting from the recovery in external demand. The new export orders index has increased for four consecutive months to 50.8 in February, the highest level since July 2014. It is worth highlighting the significant improvement in China's Producer Price Index (PPI), which after remaining negative over a 54-month span, turned positive in September 2016, and inched up steadily to 7.8% by the end of February 2017. As a result, nominal GDP growth has rebounded sharply from the fourth quarter of 2016 and we expect it to stay above 10% for 2017, even as real GDP growth remains stagnant at current levels. The end of the PPI deflation and the strong nominal GDP growth rates should support earnings as companies enjoy better operating leverage with the resumption of sales growth.

Fund overview

As at March 31 2017	3 mo.	1 yr.	3 yr.	5 yr.	10 yr.	PSD*
AGF China Focus Class (%) (net of fees)	11.3	18.7	10.8	9.0	3.4	5.2
MSCI China Free Total Return Index (%)	11.9	22.8	13.5	12.1	7.0	1.1

Source: AGF Investment Operations.

* Performance start date (PSD): Apr. 12, 1994.

During the first quarter of 2017, the Fund slightly underperformed the benchmark. The Fund benefited from strong stock selection. One of the top contributors during the quarter was China ZhengTong Auto, one of the largest luxury automobile dealerships in China and Value Partners, a leading asset manager in the region. The Fund's overweight position in the Financials sector, especially to insurance companies, also contributed positively to performance. That said, the Fund's performance was adversely affected by an underweight position to selective companies in the Information Technology sector. This includes Sunny Optical and AAC Technology, which outperformed driven by better-than-expected demand arising from the mobile device component upgrading trend. The Fund was overweight Financials and Telecommunication Services, while underweight Consumer Discretionary.

The Consumer Discretionary sector outperformed during the quarter. The share price of automobile manufacturers performed well due to strong car sales momentum witnessed in the fourth quarter of 2016, which continued into the first quarter of 2017. In addition, companies providing after-school tutoring services or exam preparation services also outperformed during the quarter with solid demand and continued improvement in profitability. The Fund's underweight positions in the aforementioned companies detracted from performance. Fortunately, the negative impact was more than offset by the strong performance of the Fund's holding in China ZhengTong Auto, which had a strong rally driven by solid auto financing revenue growth. The Fund initiated a position in Sands China, one of the major casino operators in Macau, given its relatively cheap valuation. The company is well positioned to benefit from the recovery in gaming revenue. The Fund sold its holdings in Shenzhou International, a leading textile processor and garment producer in China, to book profits.

Elsewhere, the Fund initiated a position in Netease, one of the world's largest online gaming providers, given its leading position in the fast growing mobile game industry in China, with a proven track record in strong R&D capability. Lately, the Fund also initiated a position in West China Cement due to being a major beneficiary of industry consolidation.

Outlook

The Chinese economy appears to be improving. The rebound in the manufacturing sector has led to an increase in manufacturing employment, which is reflected in the recent government's initiative aiming to create 11 million new jobs in 2017, in addition to the 10 million created last year. This in turn should bode well for household income growth and consumption. Encouragingly, early signs of success in implementing these supply-side reforms in heavy industries such as coal and steel have started to emerge and the new policy, which is backed by strict official implementation, appears to be yielding the desired results. As a result, a number of companies carrying out supply-side reform reported a remarkable improvement in profitability and cash flow, which has also likely benefited China's financial system indirectly, as the companies in these industries used to be highly indebted. We believe that if structural reforms, including supply-side reforms are implemented successfully, this should bode well for China's economy in the long term.

Economic stability is crucial ahead of the 19th National Congress of the Communist Party of China, to be held in autumn of this year, where we are likely to see some major leadership changes. If necessary, policy measures will ensure that the recent strong economic growth momentum is sustained.

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