

**Invesco Asset Management (India) Pvt. Ltd.**

**Policy to Protect the Interest of Investors of Midcap and Smallcap Schemes**

## **A. Background**

In view of the inherently volatile nature of Mid and Small Cap segments of the market, the Securities and Exchange Board of India ('SEBI') vide its email dated February 27, 2024 sent through Association of Mutual Funds of India ('AMFI') directed all the AMC's to frame policy to safeguard the interests of investors participating in Mid and Small Cap schemes.

## **B. Objective**

The policy and strategies to be adopted by the Fund Managers /AMC among other things, shall include:

- i. Appropriate & proactive measures to be taken by AMC & Fund Managers to moderate inflows in Mid and Small Cap schemes, portfolio rebalancing etc.
- ii. Steps to ensure that investors are protected from the first-mover advantage of redeeming investors.

## **I. Appropriate and Proactive Measures by Fund Managers / AMC**

### **1. Institutionalized Investment Management**

Invesco Asset Management (India) Pvt. Ltd ('IAMI') has institutionalized its investment philosophy and process that underpins the approach to stock selection and portfolio construction.

#### **1.1. Proprietary Stock Categorization System**

IAMI's investment approach revolves around its proprietary stock categorization system, designed to identify quality companies within the investment universe while also ensuring robust liquidity profiles. The stock categorization framework encompasses seven distinct categories\* that ensure a comprehensive approach to the evaluation of investment ideas. Each investment proposal is filtered through this framework with only those companies meeting IAMI's stock categorization criteria becoming eligible for inclusion in scheme portfolios. A stock's categorization defines the investment rationale for its inclusion in a portfolio. It allows running schemes true to their investment mandates and maintaining overall quality and hygiene. This acts as a mitigant during volatile market conditions and enables better management of portfolio liquidity during periods of stress, particularly in the mid/small cap segments.

\*For details on IAMI's Stock selection process, please refer the Scheme Information Document of Invesco India Midcap Fund (<https://inves.co/3IBKnKU>) and Invesco India Small Cap Fund (<https://inves.co/3ViMtac>)

## 1.2. Managing Midcap and Small Cap Schemes

### ➤ Investment Risks in Mid and Small Cap Schemes

It may be noted that Mid and Small cap stocks carry higher liquidity risk as they are less extensively researched and under-owned compared to large-cap stocks. This may lead to illiquidity and consequent higher impact costs.

IAMI recognizes the importance of maintaining adequate liquidity levels, particularly in Mid and Small Cap schemes, which are inherently more volatile and less liquid as compared to their Large Cap counterparts.

### ➤ Additional Risk Management Practices

Besides the rigorous investment process detailed above, additional prudent risk management practices, such as limiting individual stock exposure to 5% of net assets (versus a regulatorily permitted cap of 10%), well-diversified exposures across various sectors, etc., help IAMI's liquidity management efforts, ensuring portfolio resilience in challenging market conditions. IAMI is of the opinion that this practice acts as a strong defence for the objectives set by SEBI for protecting investors' interest.

The continuous monitoring and due diligence processes allow for timely adjustments to the portfolio, ensuring that liquidity requirements are met without compromising on quality of investments. By adhering to such an investment process, IAMI aims to deliver risk-adjusted returns while effectively managing liquidity risks for the investors.

## 2. Mechanisms for Intervention during stress phases of the Mid and Small Cap segment

In addition to the existing rigorous investment process and portfolio management practices as outlined above, in order to uphold the interests of investors in Mid and Small Cap schemes, particularly in periods of market stress, comprehensive actions will be undertaken at both organizational and fund management levels.

### Valuation Oversight

Prevailing valuations of Mid and Small Cap indices, typically serve as a good signal to determine market excesses in these segments. The company would be using a **level of +2 Std Dev# on 1-year forward PE multiples of the mid/small cap index** as a threshold beyond which appropriate actions will be called upon.

#### # Standard Deviation in Investment

*Standard deviation is a statistical measurement of how far a variable, such as the valuation of the market in terms of Price to Earnings (P/E) or Price to Book (P/B) multiples, is above or below their average (mean) valuation. 68% of the observed values over a period get captured at +1 SD, and 95% of the values are captured at*

+2 SD from the mean. This statistic, therefore, reliably reflects the degree of premium of the market over its average and is a good proxy to evaluate the riskiness of the market.

Standard deviation helps us see how much market values usually vary from their average. About 68% of the time, values stay close to the average, within one standard deviation. But if they consistently go beyond this, it might mean more uncertainty in the market. Similarly, around 95% of the time, values are within two standard deviations. If they go much further than this, it could signal higher risk for investors.

❖ **Actions to be taken**

**a. Suspension of Fresh Lumpsum Purchases**

In order to shield investors from entering the market at elevated valuations in Mid and Small Cap segments, IAMI will suspend fresh purchases into the schemes through the lump sum mode on a temporary basis. This measure aims to protect investor interests by preventing investments at inflated levels.

**b. Limitation on SIP and STP Registrations**

SIP and STP registrations will be capped at Rs. 2 lakh per PAN to safeguard investors from exposure at higher valuations.

**c. Portfolio Adjustments**

Portfolio risk will be managed by strategically adjusting market cap exposures.

- The fund management team will increase weights in Large-cap stocks, debt instruments, and/or cash.
- Steps will be taken to ensure liquidity readiness to a level as below:
  - At least 50 % of the Mid-cap fund portfolio can be liquidated in 5 working days.
  - At least 50% of the Small-cap fund portfolio can be liquidated in 7 working days.

**3. Higher Exit Loads for Mid-cap and Small-cap Schemes**

Once assets under management ('AuM') for IAMI schemes exceed 100% and extend up to 125% of the category average AuM, IAMI retains the right, considering prevailing market conditions and liquidity levels, to introduce higher exit loads. This initiative is aimed at fostering a long-term investment culture. Additionally, to fortify investor protection, higher exit loads may be imposed on midcap and small cap schemes compared to other schemes when deemed necessary. AuM levels for both schemes will be subject to monthly monitoring.

IAMI will apply a 2% exit load for withdrawals made when AuM levels fall within the range of 100% to 125% of the category average AuM within one year.

## Illustrations

Aspect	Details	Condition
Category Average AuM	Rs. 10,000 crores	
Invesco India – Mid Cap and Small Cap Scheme AuM	Greater than Rs. 10,000 crores and up to Rs. 12,500 crores	
Exit Load	2% within 1 year	Redemptions at AuM levels between 100% to 125% of the category Average AuM within 1 year.

#### 4. AuM Threshold Analysis

Regular evaluations will be carried out to determine if the AuMs of IAMI's Mid-cap and Small-cap schemes can sustain sufficient liquidity, as outlined in point 2(c) above, particularly during periods when **Scheme AuMs surpass 125 percent of the category average.**

**a) Suspension of Fresh Lumpsum Purchases**

IAMI will suspend fresh purchases into the schemes through the lump sum mode on a temporary basis.

**b) Limitation on SIP and STP Registrations**

SIP and STP registrations will be capped at Rs. 2 lakh per Permanent Account Number ('PAN')

#### II. Steps to ensure that investors are protected from the first-mover advantage of redeeming investors.

IAMI at all times will continuously monitor investment flows and investor concentration (single or group of investors having a disproportionate share of AuM) in midcap and small cap schemes, which could have the potential to work to the disadvantage of small investors.

With the intent of protecting the small investors across the scheme, IAMI will enhance the liquidity of the portfolio, in the event of any large investor or group of investor redeeming more than 25% of their holdings.

**C. Role of the Board of the IAMI & Invesco Trustee Pvt. Ltd.**

This Policy has been prepared by the Invesco Trustee Pvt. Ltd. (**Trustees**) in consultation with the Unit Holder Protection Committee of IAMI and shall be approved by the Board of IAMI and Trustees.

**D. Review of the Policy:**

The Policy shall be reviewed at least on an annual basis. In addition to annual review, the Policy may be amended / modified to incorporate the changes due to any regulatory changes in the Regulations or amendments / recommendation made by SEBI / AMFI or as may be felt necessary by IAMI based. The amended Policy will be approved by Board of IAMI & Trustees at their board meeting held after such updation for noting / approval, as the case may be.