September 30, 2018

Macro Commentary:

India's broad macros have been largely stable for a relatively long period from 2015 until recently. However, there has been some deterioration in the macro data mainly in the external sector. The rise in the oil prices has started to increase the import bill, and that has widened the trade deficit, affecting the current account.

The current account deficit widened to US$15.8 bn compared to US$13 bn previous month. The headline CPI inflation for Aug'18 was 3.69% compared to 4.17% of the previous month. The drop in the headline inflation was primarily led by the drop-in food prices inflation. While there has been some pick up in the energy price inflation but the drop-in food price inflation was large enough to bring down the overall inflation. As per the recent monetary policy review, RBI has also brought down the inflation forecast over the next 6 months by 30bps to 3.9-4.50% from 4.80%. Similarly, there was some moderation in the WPI for Aug'18 from 5.09% to 4.53%.

The IIP data for July'18 witnessed some moderation from 7.0% to 6.6%. Output growth eased for both mining (3.7 percent vs 6.6 percent in June) and electricity (6.7 percent vs 8.5 percent), while manufacturing production rose at a faster pace (7 percent vs 6.7 percent).

August trade deficit contracted marginally to $17.39 bn vs $18.02 bn last month but is almost near its highest deficit months. However same month last year it was $ 12.72 bn. Imports in August rose 25.4 percent over last year to $45.2 billion, led by higher inbound shipments of petroleum, gold and capital goods. The value of petroleum and crude—the biggest burden on India's import bill— rose 51.6 percent to $11.83 billion. The price of benchmark Brent crude oil was 42.3 percent higher in August compared with a year ago. The rise in exports in Aug'18 was at 19.2% despite the fall in INR value.

Monsoon in India for 2018 was at 9% lower than the normal range. Monsoon rainfall lower than normal is generally followed by pressure on agri prices due to lack of irrigation water for agri produce and acreage, unless suitably managed.

Indian rupee continues to depreciate against hard currencies. Despite RBI Governor's comment that the depreciation of INR is moderate compared to other EM currencies, INR remains weak. RBI has refrained to announce any plans to shore up inflows of foreign currencies, which has deteriorated the situation. The recent drop in the excise duty on petrol is expected to widen the fiscal by about Rs. 10,000 crore. However, the government expects it to be made up by the tax buoyancy in the direct tax collections.

Equity Market Commentary

Equity markets witnessed a sharp selloff in September (down 6%) in the wake of global risk on trade wars, liquidity concerns in the debt market following default of in repayment of loans by IL&FS group entities and concerns over weakening currency amid deteriorating current account deficit (CAD). In terms of stock performance, most of the sectors were in red, except for IT services. On the monsoon front, the season ended with rains below 9% of long term average and with uneven geographical distribution. However, water levels at reservoirs across India are higher than last year. In terms of flows, Foreign Institutional Investors (FIIs) were significant net sellers while Domestic Institutional Investors (DIIs) turned out to be meaningful net buyers this month.

The S&P BSE IT index continued to outperform (+0.2%) aided by sharp currency depreciation, even as we continued to see mixed trends on individual businesses as evidenced by results and positive commentaries / guidance of some of the major IT companies. Meanwhile, the biggest underperformers were interest rate sensitive sectors like S&P BSE Realty (-20.5%), S&P BSE Auto (-13.1%), S&P BSE Bankex (-11.8%) and S&P BSE Consumer Durables (-11.8%).

Recent developments in the fixed income markets coupled with macro-weaknesses have created a significant risk-off atmosphere in the equity markets which may likely persist for some time. Certain measures taken by the govt and the RBI to restore short-term liquidity for the debt markets and constitution of a new management team for IL&FS will likely infuse confidence. We continue to maintain that the market will likely remain in the mode of re-calibrating recent gains in economic and earnings' growth momentum against emergent risks of higher interest rates and steep currency depreciation.

The recent sharp fall in mid and small cap stocks, as anticipated by us for a while now, has added to the overall market volatility, but, has also expanded investment opportunities given steep valuation corrections.

Portfolio approach continues to remain balanced with bottom-up stock selection and sector selection playing equally crucial roles. We believe evidence is emerging on strengthening of pro-cyclical stance and we are currently undertaking some portfolio shifts to capture a potential industrial/manufacturing recovery. We today prefer cyclicals with comfortable balance sheets and attractive valuations and /or companies with strong franchise value but presently facing growth headwinds.

Broad Portfolio Strategy of Invesco India R.I.S.E Portfolio:
Our portfolio is strategized to invest in companies that:
a) Exhibit Operating Leverage, and / or,
b) Financial Leverage, and,
c) Trade at deep discount to their intrinsic value.

Note: Operating Leverage: Companies currently operating with low capacity utilization and having large portion of costs fixed in nature. These companies can make more money from additional sale as demand recovers. **Financial Leverage**: Companies which can generate returns greater than the interest expense associated with the debt they use to fund growth. Further, these companies could increase their profit margin from decline in interest rates and reduction in debt in wake of profit growth. **Deep Value**: Deep value investing seeks to purchase stocks at an even greater discount to their intrinsic value.

Companies with operating and / or financial leverage have the potential to deliver distinctly higher earnings growth even for modest top line growth as these companies are already well-equipped with capacities to increase production without incurring additional fixed costs. In line with our preference, the model portfolio is currently positioned as follows:

- Companies with Operating Leverage: 52.42%
- Companies with Operating and Financial Leverage: 26.50%
- Companies with Financial Leverage: 10.73%
- Companies with Value: 4.09%

Note: Data as on September 30, 2018

Model Portfolio performance of Invesco India R.I.S.E Portfolio for the month of September 2018:
The Portfolio outperformed its benchmark by 7.10% on Compounded Annual Growth Rate (CAGR) since inception i.e. from April 18, 2016 till September 30, 2018. However, the Model Portfolio underperformed its benchmark (S&P BSE 500) by 12.59 in absolute terms for Year till Date for Calendar Year 2018 i.e. January 1, 2018 to September 30, 2018.

Cumulative Model Portfolio performance of Invesco India R.I.S.E Portfolio as on September 30, 2018:

In %	1 month	3 months	6 months	1 year	2 years	Since Inception
Model Portfolio	-13.91	-7.12	-7.45	2.68	18.79	21.51
S&P BSE 500	-8.84	-0.57	2.27	6.14	11.12	14.41

Calendar Year Model Portfolio performance of Invesco India R.I.S.E Portfolio:

In %	YTD- 2018	2017	2016
Model Portfolio	-16.30	74.80	10.29^
S&P BSE 500	-3.71	35.94	6.30^

Disclaimer: Past performance may or may not be sustained in future. The data given above is for model portfolio. Returns up to 1 year are absolute and over 1 year are Compounded Annualized. The returns are calculated based on daily market value of the Portfolio. ^Since inception date April 18, 2016. The returns of model portfolio given above are for illustration purpose only. Model portfolio returns do not consider expenses/charges and Profit/Loss on account of derivative transactions. Returns under client wise portfolio may vary vis-à-vis returns of model portfolio due to various factors viz. timing of investment/additional corpus in client's portfolio, timing of withdrawals in client's portfolio, mandates given by respective client, profit/loss on account of derivative transactions, expenses charged to respective portfolio, dividend income in the respective portfolio etc. The Portfolio Manager does not offer guaranteed or assured returns.
Securities investments are subject to market risks, please read the Disclosure Document carefully before investing. Past Performance may or may not be sustained in future.

Returns Attributors/ Detractors of Model Portfolio for the month of September 2018:

Top Attributors:
Aia Engineering Ltd.

Top 5 Detractors:

Balkrishna Industries Ltd., L and T Finance Holdings Ltd., VIP Industries Ltd., Parag Milk Foods Ltd. & Mahindra And Mahindra Fin Services Ltd.

Disclaimer: The stocks referred above should not be construed as recommendations from Invesco Asset Management (India) Private Limited. The Portfolio may or may not have any present or future positions in these stocks or in any other portfolios offered by Invesco Asset Management (India) Private Limited. The performance of above stocks should not be construed as performance of the portfolio as the portfolio would be constituted of number of stocks having different weights and the individual stock held by the portfolio may or may not give positive returns.

Top 10 Holdings & Sector Allocation of Model Portfolio as on September 30, 2018

Security	GICS Sectors	% of Net Assets
Cipla Ltd.	HealthCare	6.90
Mahindra & Mahindra Ltd.	Consumer Discretionary	6.83
Balkrishna Industries Ltd.	Consumer Discretionary	6.06
Mahindra & Mahindra Fin Services Ltd	Financials	5.80
Apollo Hospitals Enterprises Ltd.	HealthCare	5.58
Aia Engineering Ltd.	Industrials	5.25
Motherson Sumi Systems Ltd.	Consumer Discretionary	5.14
Gujarat State Petronet Ltd.	Utilities	5.13
Shriram Transport Finance Co. Ltd.	Financials	4.92

New entries in the model portfolio during the month of September 2018:
NA

Exits in the model portfolio during the month of September 2018:
NA

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Capitalization Break-up of Model Portfolio as on September 30, 2018

Market Capitalization	% of Net Assets
Large Cap	18.87%
Mid Cap	32.41%
Small Cap	42.45%
Average Market Capitalization (INR Crs.)	22,635

Definition: Large Cap:1st-100th company in terms of full market capitalization. Mid Cap:101st to 250th company in terms of full market capitalization. Small Cap:251st company onwards in terms of full market capitalization.

Asset Allocation of Model Portfolio as on September 30, 2018

Asset Allocation	% of Net Assets
Equities	93.73
Cash & Cash Equivalent	6.27

Valuation of Model Portfolio as on September 30, 2018

Characteristic	Invesco India R.I.S.E Portfolio	S&P BSE 500
Dividend Yield[1]	0.40%	0.49%
Price to Earnings[1] FY 18 Estimate	24.5	20.8
Price to Earnings[1] FY 19 Estimate	19.1	19.5
Price to Earnings[1] FY 20 Estimate	15.3	15.8
2 Year EPS CAGR (FY18-FY20)[2]	23.7%	14.2%
Return on Assets[1] FY 19 Estimate	4.6%	2.6%
Return on Equity[1] FY 19 Estimate	15.1%	13.4%

Note: 1. Weighted Harmonic Mean. 2. EPS Growth is derived from P/E ratios
Note: Excludes companies with net loss for appropriate results for various ratios. EPS: Earnings per share
Source: Factset, Internal.

Outlook

The companies, invested in by the R.I.S.E Portfolio, continued to deliver strong earnings growth in Q1 FY2019, with a topline growth of 26% Year on Year (YoY), EBITDA growth of 36% YoY and Profit after Tax growth of 43 YoY%.

Disclaimer: Past performance may or may not be sustained in future.

We continue to focus on companies with Operating & Financial Leverage. As per our estimates, the companies under the portfolio is expected to deliver a revenue CAGR of 15%, EBITDA CAGR of 21% and PAT CAGR of 32% for the period FY2019 to FY2020. R.I.S.E portfolio, as on September 30, 2018, trades at a forward Price to Equity (P/E) ratio of 19.1 times FY2019E (expected earnings).

For Calendar Year till Date, Mid-Cap and Small-Cap companies have seen a sharper correction vis-à-vis the Large Cap companies. In effect, the Nifty Midcap 100 is down almost 18.83% and Nifty Small Cap 100 Index is down almost 32.36%. During this period, the R.I.S.E Portfolio which has about 75% exposure to mid-cap and small-cap companies has thus seen derating of PE multiples in case of some companies.

While we believe that individual stock returns can be significantly impacted by changes in the P/E multiples in the short term, however, in the long-term, returns are more likely to be influenced by compounding of earnings.

India Inc., over next 3 years is expected to see sound earnings' recovery, led by levers of operating and financial leverage, which are also the key levers of Invesco India R.I.S.E Portfolio. The continuous traction in earnings of companies where R.I.S.E portfolio has invested, gives us confidence that investors with a 3 to 4 year investment horizon may benefit from strong earnings growth. The Portfolio is thus well positioned to deliver strong earnings growth in future, and its valuation, despite re-rating, continues to be reasonable on FY2019 basis, making the portfolio potentially attractive proposition from risk-reward perspective.

EBITDA: Earnings before interest, taxes, depreciation and amortization. CAGR: Compound annual growth rate. PAT: Profit after Tax

Disclaimer: The estimates expressed herein are based on internal analysis of publicly available information and other sources believed to be reliable. Any such calculations made are approximations, meant as guidelines only. The recipient(s) before acting on any information herein should make his/their own investigation and seek appropriate professional advice.