

RISK FACTORS

Scheme Specific Risk Factors

Risk factors associated with the Scheme

- Investments in the Underlying scheme will have all the risks associated with investments in equity and Debt markets.
- The portfolio disclosure of the Scheme will be largely limited to the investments made by the Scheme.
- This being a fund of funds Scheme, the investors should note that the expenses to be borne by the investor include the recurring expenses of the Underlying scheme in which Fund of Funds Scheme makes investments subject to the maximum limits prescribed under sub-regulation 6 & 6A of Regulation 52 of the SEBI Regulations.
- If the Underlying scheme declares a non-business day, the AMC will also declare it a non-business day for this Scheme. If this information is received later in the day and the local feeder fund has already accepted transaction, such transactions will be processed at the NAV of the next business day. This may impact liquidity of investors of local scheme.

Liquidity risk of underlying instruments

There could be liquidity risk on account of illiquidity issues in underlying funds for example, underlying fund creating a segregated portfolio due to default in its exposures.

To maintain liquidity at the feeder fund level, the AMC will invest upto 5% in Money Market instruments (including TREPS & reverse repo in government securities) and units of domestic mutual funds to provide from a liquidity perspective.

- **Restructuring / Rescheduling Risk:** There could be cases of restructuring / re-scheduling of particular debt / money market instruments held in the portfolio which could result in the maturity of these instruments going beyond the original maturity date of the instrument. In such cases the fund manager may be constrained to sell these instruments in the market at realizable value and pass on the loss / impact to investors under the Scheme.
- **Operational Risk** - Given that the FOF structure will involve splitting each subscription and redemptions into the respective funds; there is enhanced operational risk.

The Scheme will invest in a combination of equity funds, debt fund, and money market instruments hence, the performance of the scheme would depend upon the performance of Underlying schemes.

The investor will be exposed to the risk of the global markets and currency risk arising out of the investment in the Underlying scheme which invests in securities denominated in foreign currencies (eg US Dollars). The investor will also be exposed to delays in redemption if the global market is closed.

Investments in Underlying Debt schemes will have all the risks associated with the debt markets including interest rate risk, duration risk, credit risk and reinvestment risk.

Risk associated with investing in foreign securities, derivatives, unrated, securitized debt, short selling and securities lending –

The Scheme will not have any exposure to Foreign securities, derivative instruments, securitized debt or unrated instruments and shall not undertake any short selling or securities lending. However, the Underlying schemes may take exposure to the above mentioned securities. The domestic Underlying schemes of HSBC and other than HSBC schemes may take exposure to the above mentioned securities as per the limits provided (if any) in the Scheme Information Document of the respective Underlying schemes and applicable SEBI Regulations from time to time. For risk associated with the same refer risk factors provided below for Underlying scheme.

Risk associated with short selling and securities lending by Underlying schemes

- **Short Selling Risk:** The risk associated with upward movement in market price of security sold short may result in loss. The losses on short position may be unlimited as there is no upper limit on rise in price of a security.
- **Securities Lending:** The risks in lending portfolio securities, as with other extensions of credit, consist of the failure of another party, in this case the approved intermediary, to comply with the terms of agreement entered into between the lender of securities i.e. the Scheme(s) and the approved intermediary. Such failure to comply can result in the possible loss of rights in the collateral put up by the borrower of the securities, the inability of the approved intermediary to return the securities deposited by the lender and the possible loss of any corporate benefits accruing to the lender from the securities deposited with the approved intermediary. The Mutual Fund may not be able to sell such lent securities and this can lead to temporary illiquidity.

Risk Factors associated with investments in Money Market instruments .

- Investments in money market instruments would involve a moderate credit risk i.e. risk of an issuer's liability to meet the principal payments.
- Money market instruments may also be subject to price volatility due to factors such as changes in interest rates, general level of market liquidity and market perception of credit worthiness of the issuer of such instruments.
- The NAV of the Scheme's Units, to the extent that the corpus of the Scheme is invested in money market instruments, will be affected by the changes in the level of interest rates. When interest rates in the market rise, the value of a portfolio of money market instruments can be expected to decline.

Risk factor associated with legal, tax and regulatory risk

The Schemes could be exposed to changes in legal, tax and regulatory regime which may adversely affect it and / or the investors. Such changes could also have retrospective effect and could lead to additional taxation imposed on the Schemes which was not contemplated either when investments were made, valued or disposed off.

Risk Factors of Underlying scheme

The Underlying schemes having exposure to equity and equity related securities and / or fixed income securities will be subject to the following risks which may in turn affect the performance of the Scheme. There can be no assurance that the Underlying scheme will achieve its investment objectives and past performance should not be seen as a guide to future returns.

Risk associated with investments in Equity & Equity related securities by the Underlying schemes

- Equity instruments by nature are volatile and prone to price fluctuations on a daily basis due to both macro and micro factors. Trading volumes, settlement periods and transfer procedures may restrict the liquidity of these investments. Different segments of financial markets have different settlement periods and such periods may be extended significantly by unforeseen circumstances. The inability of the Scheme(s) to make intended securities' purchases due to settlement problems could cause the Scheme(s) to miss certain investment opportunities. In the view of the Fund Manager, investing in mid and small cap stocks are riskier than investing in large cap Stocks.
- **Market Risk:** The Underlying scheme's investments are subject to the risks inherent in all investments in Securities i.e. the value of holdings may fall as well as rise. As the Underlying scheme invests primarily in equities, investors are exposed to stock market fluctuations and the financial performance of the companies held in the Underlying scheme's portfolio.
- **Currency Risk:** As the Underlying scheme could invest in securities which are denominated in foreign currencies (e.g. US Dollars), fluctuations in the exchange rates of these foreign currencies may have an impact on the income and value of the Scheme. The assets in which the Underlying scheme is invested and the income from the assets will or may be quoted in currencies which are different from the Underlying scheme's base currency. The performance of the Underlying scheme will therefore be affected by movements in the exchange rate between the currencies in which the assets are held and the Underlying scheme's base currency and hence there can be the prospect of additional loss or the prospect of additional gain to the investors greater than the usual risks of investment. The performance of the Underlying scheme may also be affected by changes in exchange control regulations.
- The investment manager to the Underlying scheme is permitted, but not obliged, to use hedging techniques to attempt to offset market and currency risks. There is no guarantee that hedging techniques will achieve the desired result.

- **Liquidity Risk:** Investors should be aware that the investments of the Underlying scheme could be negatively impacted by low liquidity and poor transparency of some of the exchanges where the investments are made. Investments may also become illiquid which may constrain the ability of the investment manager of the Underlying scheme to realize some or all of the portfolio. Securities, which are not quoted on the stock exchanges, are inherently illiquid in nature and carry a larger amount of liquidity risk, in comparison to securities that are listed on the exchanges.
- **Country Risk:** As the underlying portfolio could invest in stocks of different countries, the portfolio shall be exposed to the social, economic, political and settlement risks with respect to each country.
- **Sector Concentration Risk:** The underlying portfolio may have high concentration in a particular sector. The performance of the Scheme could be sensitive to movements in these sectors.
- **Legal, tax and regulatory Risk:** The Underlying scheme could be exposed to changes in legal, tax and regulatory regime which may adversely affect it and the investors. Such changes could also have retrospective effect and could lead to additional taxation imposed on the Scheme which was not contemplated either when investments were made, valued or disposed off.
- **NAV Alignment Risk:** The cut off timing of NAV is aligned to the Underlying scheme's NAV. HSBC Asset Management India will only declare NAV, after receiving the NAV of the Underlying scheme.

Investments in Debt Instruments by the Underlying schemes.

The Underlying scheme(s) proposes to invest in debt and related instruments and the risk factors pertinent to the same are:

- **Price-Risk or Interest Rate Risk:** As with all debt securities, changes in interest rates may affect the NAV of the Scheme(s) as the prices of securities increase as interest rates decline and decrease as interest rates rise. Prices of long-term securities generally fluctuate more in response to interest rate changes than do short-term securities. Indian debt markets can be volatile leading to the possibility of price movements up or down in fixed income securities and thereby to possible movements in the NAV.
- The change in value of a security, for a given change in yield, is higher for a security with higher duration and vice versa. Hence portfolios with higher duration will have higher volatility which leads to duration risk.
- Government securities do carry price risk depending upon the general level of interest rates prevailing from time to time. The extent of fall or rise in the prices is a function of the coupon rate, days to maturity and the increase or decrease in the level of interest rates. The price of the Government securities (existing and new) is influenced only by movements in interest rates in financial systems.
- In the case of floating rate instruments, an additional risk could be due to the change in the spreads of floating rate instruments. If the spreads on floating rate papers rise, then there could be a price loss on these instruments. Secondly in the case of fixed rate instruments that have been swapped for floating rates, any adverse movement in the fixed rate yields vis-à-vis swap rates could result in losses. However, floating rate debt instruments which have periodical interest rate reset, carry a lower interest rate risk as compared to fixed rate debt instruments. In a falling interest rate scenario the returns on floating rate debt instruments may not be better than those on fixed rate debt instruments.
- **Liquidity or Marketability Risk:** This refers to the ease with which a security can be sold at or near to its valuation yield-to-maturity (YTM). The primary measure of liquidity risk is the spread between the bid price and the offer price quoted by a dealer. Liquidity risk is today characteristic of the Indian fixed income market.
- **Credit Risk:** Credit risk or default risk refers to the risk that an issuer of a fixed income security may default (i.e. will be unable to make timely principal and interest payments on the security). A sovereign security carries no default risk since Government raises money to meet its capital and revenue expenditure by issuing these debt or discounted securities. As the payment of interest and principal amount has a sovereign status implying no default, such securities are popularly known as "riskfree security" or "Zero Risk security". Thus Zero-Risk is the lowest risk, even lower than a security with "AAA" rating and hence commands a yield, which is lower than a yield on "AAA" security. Normally, the value of a fixed income security will fluctuate depending upon the changes in the perceived level of credit risk as well as any actual event of default. The greater the credit risk, the greater the yield required for someone to be compensated for the increased risk. Because of this risk, corporate debentures are sold at a yield above those offered on Government Securities, which are sovereign obligations.
- **Reinvestment Risk:** This risk refers to the interest rate levels at which cash flows received from the securities in the Scheme(s) are reinvested. The additional income from reinvestment is the "interest on interest" component. The risk is that the rate at which interim cash flows can be reinvested may be lower than that originally assumed.
However declining interest rates normally lead to increase in bond prices which may help cushion the impact of reinvestment risk to some extent.
- **Prepayment Risk:** The risk associated with the early unscheduled return of principal on a fixed-income security. The early unscheduled return of principal may result in reinvestment risk.
- **Settlement risk:** Different segments of Indian financial markets have different settlement periods and such periods may be extended significantly by unforeseen circumstances. Delays or other problems in settlement of transactions could result in temporary periods when the assets of the Scheme are uninvested and no return is earned thereon. The inability of the Scheme to make intended securities purchases, due to settlement problems, could cause the Scheme, to miss certain

investment opportunities. Similarly, the inability to sell securities held in the Scheme's portfolio, due to the absence of a well-developed and liquid secondary market for debt securities, may result at times in potential losses to the Scheme in the event of a subsequent decline in the value of securities held in the portfolio of the Scheme.

- **Market risk:** Lower rated or unrated securities are more likely to react to developments affecting the market and the credit risk than the highly rated securities which react primarily to movements in the general level of interest rates. Lower rated or unrated securities also tend to be more sensitive to economic conditions than higher rated securities.
- In addition to the factors that affect the values of securities, the NAV of Units of the Scheme will fluctuate with the movement in the broader fixed income market, money market and derivatives market and may be influenced by factors influencing such markets in general including but not limited to economic conditions, changes in interest rates, price and volume volatility in the bond and stock markets, changes in taxation, currency exchange rates, foreign investments, political, economic or other developments and closure of the stock exchanges.

Risk of investments in unrated instruments:

Investments in the unrated instruments shall be subject liquidity risk, credit risk, market risk, interest rate risk, reinvestment risk etc. Also, as the unrated instruments are not being rated by the Credit Rating Agencies, there is no external credit risk assessment available for such instruments, hence, the investor will be exposed to risk associated with investments in un-rated instruments.

Risks associated with investment in third party Schemes

AMIN would have no control over investments done by the underlying third party schemes. AMIN shall not be able to monitor liquidity, credit, concentration and other investment risks like it does for in house schemes. The fund manager shall take these metrics into account while taking exposure to third party schemes.

Risks associated with investing in Derivatives by Underlying Scheme

The Scheme may invest in derivative products in accordance with and to the extent permitted under the Regulations and by SEBI. Derivative products are specialized instruments that require investment techniques and risk analysis different from those associated with stocks and bonds. The use of a derivative requires an understanding not only of the underlying instrument but of the derivative itself. Trading in derivatives carries a high degree of risk although they are traded at a relatively small amount of margin which provides the possibility of great profit or loss in comparison with the principal investment amount.

Thus, derivatives are highly leveraged instruments. Even a small price movement in the underlying security could have an impact on their value and consequently, on the NAV of the Units of the Scheme.

- The derivatives market in India is nascent and does not have the volumes that may be seen in other developed markets, which may result in volatility to the values.
- Investment in derivatives also requires the maintenance of adequate controls to monitor the transactions entered into, the ability to assess the risk that a derivative adds to the portfolio and the ability to forecast price or interest rate movements correctly. Even a small price movement in the underlying security could have an impact on their value and consequently, on the NAV of the Units of the Scheme.
- The Scheme may face execution risk, whereby the rates seen on the screen may not be the rate at which the ultimate execution of the derivative transaction takes place.
- The Scheme may find it difficult or impossible to execute derivative transactions in certain circumstances. For example, when there are insufficient bids or suspension of trading due to price limit or circuit breakers, the Scheme may face a liquidity issue.
- The options buyer's risk is limited to the premium paid, while the risk of an options writer is unlimited. However, the gains of an options writer are limited to the premiums earned. Since in case of the Scheme all option positions will have underlying assets, all losses due to price – movement beyond the strike price will actually be an opportunity loss.
- The exchange may impose restrictions on exercise of options and may also restrict the exercise of options at certain times in specified circumstances and this could impact the value of the portfolio.
- Investments in index futures face the same risk as the investments in a portfolio of shares representing an index. The extent of loss is the same as in the underlying stocks.
- The Scheme bears a risk that it may not be able to correctly forecast future market trends or the value of assets, indices or other financial or economic factors in establishing derivative positions for the Scheme.
- The risk of loss in trading futures contracts can be substantial, because of the low margin deposits required, the extremely high degree of leverage involved in futures pricing and the potential high volatility of the futures markets.
- There is the possibility that a loss may be sustained by the portfolio as a result of the failure of another party (usually referred to as the "counterparty") to comply with the terms of the derivatives contract.
- Other risks in using derivatives include the risk of mispricing or improper valuation of derivatives and the inability of derivatives to correlate perfectly with underlying assets, rates and indices.
- Derivative products are leveraged instruments and can provide disproportionate gains as well as disproportionate losses to the investor.
- Execution of investment strategies depends upon the ability of the fund manager(s) to identify such opportunities which may not be available at all times. Identification and execution of the strategies to be pursued by the fund manager(s)

involve uncertainty and decision of fund manager(s) may not always be profitable. No assurance can be given that the fund manager(s) will be able to identify or execute such strategies.

- The risks associated with the use of derivatives are different from or possibly greater than, the risks associated with investing directly in securities and other traditional investments.

Risk factors associated with underlying scheme investing in REITs and InvITs

The Underlying scheme may also invest in REITs and InvITs which may subject the scheme to the following risks:

- **Market Risk:** REITs and InvITs Investments are volatile instruments and are subject to price fluctuations on a daily basis owing to the market conditions and factors impacting the underlying assets. Fund Manager will do the necessary due diligence but actual market movements may be at variance with the anticipated trends.
- **Liquidity Risk:** The liquidity of the investments could, at times, be restricted by trading volumes, settlement periods, dissolution of the trust, potential delisting of units on the exchange etc. Hence, the time taken by the Fund Manager for liquidating the investments in the scheme may be longer than anticipated. As these products are new to the market they are likely to be exposed to liquidity risk.
- **Reinvestment Risk:** Investments in REITs & InvITs may carry reinvestment risk as there could be repatriation of funds by the Trusts in form of buyback of units or dividend pay-outs, interest payments, etc. Depending upon the market conditions, interest rates prevailing on the interest or maturity due dates may differ from the original coupon of the bond. As a result, the proceeds may get deployed at a lower yield.
- **Regulatory / Legal Risk:** REITs and InvITs being new asset classes, regulatory guidelines may be evolving in nature which may impact the investments in REITs and InvITs.

Risks associated with investing in securitised debt by Underlying Scheme

- **Securitised Debt:** Securitised debt papers carry credit risk of the Obligors and are dependent on the servicing of the PTC / Contributions etc. However these are offset suitably by appropriate pool selection as well as credit enhancements specified by Rating Agencies. In cases where the underlying facilities are linked to benchmark rates, the securitised debt papers may be adversely impacted by adverse movements in benchmark rates. However this risk is mitigated to an extent by appropriate credit enhancement specified by rating agencies. Securitised debt papers also carry the risks of prepayment by the obligors. In case of prepayments of securities debt papers, it may result in reduced actual duration as compared to the expected duration of the paper at the time of purchase, which may adversely impact the portfolio yield. These papers also carry risk associated with the collection agent who is responsible for collection of receivables and depositing them. The Investment team evaluates the risks associated with such investments before making an investment decision.
- The underlying assets in the case of investment in securitised debt could be mortgages or other assets like credit card receivables, automobile / vehicle / personal / commercial / corporate loans and any other receivables / loans / debt.

The risks associated with the underlying assets can be described as under:

Credit card receivables are unsecured. Automobile / vehicle loan receivables are usually secured by the underlying automobile / vehicle and sometimes by a guarantor. Mortgages are secured by the underlying property. Personal loans are usually unsecured. Corporate loans could be unsecured or secured by a charge on fixed assets / receivables of the company or a letter of comfort from the parent company or a guarantee from a bank / financial institution. As a rule of thumb, underlying assets which are secured by a physical asset / guarantor are perceived to be less risky than those which are unsecured. By virtue of this, the risk and therefore the yield in descending order of magnitude would be credit card receivables, personal loans, vehicle / automobile loans, mortgages and corporate loans assuming the same rating.

Risks associated with Segregated Portfolio

- **Liquidity risk** - Segregated Portfolio is created to separate debt and money market instruments affected by a Credit Event from the Main Portfolio of the Scheme. The Fund will not permit redemption of the Segregated Portfolio units, but the units will be listed on a recognized stock exchange. The Fund is not assuring any liquidity of such units on the stock exchange. Further, trading price of units on the stock exchange may be significantly lower than the prevailing NAV. Investors can continue to transact (subscribe / redeem) from the Main Portfolio. Therefore, redeeming the entire investment may not be possible from FOF to the extent of underlying fund triggering segregated portfolio due to downgrade/ default in its debt exposures.
- **Credit risk** – While the AMC will put in sincere efforts to recover the securities in the Segregated Portfolio and distribute the same to unit holders, because such securities are affected by credit event, it is likely that such securities may not realize any value leading to losses to investors.

Risks associated with transaction in Units through Stock Exchange mechanism

- In respect of transactions in Units of the Scheme routed through the BSE StAR MF platform or any other recognised stock exchange platform as intimated by the AMC, allotment and redemption of Units on any Business Day will depend upon the order processing/settlement by BSE, or such other exchange and their respective clearing corporations on which the Fund has no control. Further, transactions conducted through the stock exchange mechanism shall be governed by the operating guidelines and directives issued by BSE or such other recognised exchange in this regard.