Invesco Australia Limited

Derivative Risk Management Statement - Part B

June 2015

1. Responsible Party Name

This Derivative Risk Management Statement ("DRMS") has been prepared by Invesco Australia Limited ABN 48 001 693 232, AFSL 239916 ("Invesco") as investment manager of:

(a) Managed Investment Schemes for which Invesco is the Responsible Entity (collectively referred to throughout this document as "the Funds"); and
(b) Discrete Mandates under agreement with institutional clients ("the Mandates").

2. The Objective of this DRMS

The objective of this DRMS is to summarise the policies and processes in place to ensure the proper use of derivative products. This DRMS will also outline the control framework, which has been developed to manage business risk, maintain legal compliance and substantiate statements made in disclosure documents.

Above all, derivatives are not considered in isolation by Invesco but as part of the investment strategy of the Fund/Mandate as a whole.

Those persons involved in asset management for Invesco are required to read and understand the terms of this DRMS. Senior Management on a regular basis reviews the statements made in the DRMS.

3. Definition of Derivatives

Derivatives are defined as financial contracts whose value depends on (or is derived from) other assets, liabilities, indices or another derivative. Derivatives include, but are not restricted to, forwards, futures, options, warrants, swaps and structured notes.

4. Relationship to Investment Strategy of the Funds/Mandates

The assets of each Fund (including derivatives) are managed in accordance with the investment strategy specifically tailored for the product's objectives. The strategy is approved by the Board of Directors of Invesco and must comply with any authorised investments and management restrictions specified in the Fund's governing Constitution. A description of the investment strategy is provided to prospective investors in the relevant Fund's Offer Document and accordingly this DRMS should be read in conjunction with that document.

The assets of each Mandate are managed in accordance with the investment responsibilities and restrictions agreed upon in the Investment Management Agreement or other written agreement ("IMA") between the Institutional Client and Invesco.

Where derivatives are permitted as authorised investments, they are managed in a way that is consistent with and subordinate to the investment strategy or IMA, as applicable.

5. Purpose of the Use of Derivatives

Invesco considers the use of derivative products as appropriate in managing investment assets and believes derivatives can provide value to the investment process by relieving some market and currency risks.

Derivatives may be used for a variety of purposes, including (but not limited to) the following:

Risk management:

- to hedge an asset or portfolio against a fluctuation in market or currency values;
- to control the impact on portfolio valuations of market movements caused by transactions;
- to provide a more certain distribution of portfolio returns over given timeframes.

Transactional efficiency:

- to reduce transaction costs;
- to achieve the best execution of security transactions;
- to adjust asset exposures within defined parameters.

Value added strategies:

- to obtain exposure to long-short positions;
- to adopt strategies that will benefit from changes in market volatility;
- to extract preferred components of security value;
- to adopt strategies that will benefit from changes in the relationship between financial securities.

6. Restrictions on the use of derivatives

6.1 Internal Policies

We translate constraints in legislation and regulations, constitutions, management agreements, and investment mandates relating to the use of derivatives into strategy and management guidelines for each portfolio. These allow efficient implementation in accordance with the risk management practices detailed in the following sections. A list of approved instruments is maintained and updated regularly.

As is the case with restrictions on investment of other assets, the investment manager for a portfolio is required to make investment decisions for the use of derivatives in a portfolio that are consistent with the guidelines.

We devote resources to maintaining and configuring computer systems to assist in management of investment restrictions, including the use of derivatives.

6.2 Client Restrictions

Clients may limit derivative usage beyond this Statement via restrictive conditions in the governing document of their mandates. Mandate management procedures are then extended to capture any additional limits. These procedures include:

- examination of the governing document by the Investment team upon inception and in the event of any changes;
- adjusting the pre-trade derivative limits in the order generation system; and
- monitoring of portfolio exposures relative to the governing document post investment.

6.3 Regulation Restrictions

Regulatory requirements, licenses and registrations are maintained by Invesco's Legal and Compliance team. The Investment team is alerted to relevant changes in regulation and policy directly. Portfolio documents are prepared in line with regulatory requirements.

7. Risk Analysis

The use of derivatives in a portfolio gives rise to various types of risk, many of which are not necessarily specific to derivatives. The primary types of risk include market risk, liquidity risk, counterparty risk and operations risk. These are discussed in detail below. The use of derivatives is limited to those instruments where the associated risks can be understood, measured and adequately controlled.

7.1 Market Risk

Market risk represents the risk of adverse movements in markets (including asset prices, volatility, changes in yield curve, implied option volatility or other market variables) for the derivatives or the underlying asset, reference rate or index to which the derivative relates.

Such risk is created by holding any security, physical or derivative, which creates exposure to movements in prices of a security or market. A related form of market risk that is relevant to derivative management is basis risk. This is the risk that a derivative position will not move in line with a physical position.

The process by which Invesco assesses, monitors, and controls market risk is as follows:

- Investment mandates specify the investment strategy and management guidelines for each Mandate. Investment managers and supporting systems compare total portfolio exposures to these guidelines.
- There are systems in place to measure market risk. Portfolio reports, which delta expose all derivative positions, are prepared daily for use by investment managers.
- Investment managers may stress test portfolios where derivative or other positions have the potential to significantly alter portfolio values upon market movement. The frequency of testing and methodology used depends on the type of portfolio and the extent of derivative positions.
- Portfolios will not be geared unless allowed in the mandate. To avoid gearing the manager must at all times have suitable arrangements in place with respect to net derivative positions (delta-adjusted in the case of options) to ensure that either cash is available or assets exist within the portfolio that can be converted to cash sufficient to meet all actual or prospective obligations. A geared position is defined as one in which this condition is not met.
- Investment managers monitor cover-for-net derivative positions to ensure that either cash is available or assets exist within the portfolio that can be readily converted to cash sufficient to meet all potential obligations; or assets exist within the portfolio or are available as a reasonable hedge for the position.

Stress Testing:

- Stress testing of changes in portfolio exposure due to changes in price of the underlying securities is useful when the position contains some form of optionality which has potential to significantly affect portfolio values. Where optionality is not involved, IAL does not currently undertake stress testing but this position is reviewed annually by the Risk Management Committee and/or if new instruments are traded.
- In applicable funds where Invesco has delegated investment functions to an offshore investment centre, and where stress testing is deemed necessary, the offshore investment centre performs stress testing and reports results to Invesco as Responsible Entity for the Fund or Mandate.

7.2 Basis Risk

Basis risk is the potential for loss (or profit) arising from any failure of the prices of derivative securities to track precisely either the theoretical values calculated from the prices of the underlying securities on which they are based, or to track precisely the underlying securities for which they are a hedge. The establishment of short positions in securities (including derivatives) and the use of Credit Default Swaps (for a purpose other than hedging), can contribute to basis risk. The process by which Invesco manages basis risk is as follows:

- Futures – Investment managers monitor active positions using information sourced from brokers and other third parties.
- Options – Where options are not traded on market, investment managers generally calculate option valuations using an option calculator, although sometimes receive valuations from third parties.
- Short Selling – Diversification of the short portfolio.
- Credit Default Swaps – Investment managers limit in an appropriate manner the use of this type of transaction.

7.3 Liquidity Risk

Liquidity risk is the risk that an investment may not be easily converted into cash with little loss in market value and minimum delay. The process by which Invesco manages liquidity risk is as follows:

- Investment mandates incorporate guidelines that specify minimum cash levels. These will typically depend on the type of portfolio, the investment strategy applied, and the specific needs of investors.
- Investment managers monitor and manage the levels of liquidity maintained in portfolios.
- Investment managers monitor movements in derivatives to ensure that margin calls can be met.
- Investment managers monitor the degree of liquidity for approved instruments to ensure that they can, if needed, be converted to cash within acceptable timeframes at reasonable prices.

7.4 Counterparty Risk

Counterparty risk is the risk that a party to a contract will not perform to the terms of the contract. The process by which Invesco manages counterparty risk is as follows:

- Where investment mandates specify counterparty limits, investment managers review portfolios on an ongoing basis to ensure that they conform with mandate requirements.
- Invesco maintains a list of approved clearing-houses, and uses clearers of high creditworthiness for all futures and options on futures transactions. Alternatively, clients may specify their own clearers.
- Invesco maintains a list of approved instruments. Transactions involving instruments outside the list must be separately authorised.
- Invesco maintains a list of approved counterparties. Transactions involving counterparties outside the list must be separately authorised.
- As required within each mandate, internal guidelines limit the level of exposure to a single counterparty at any point in time.
- All contracts with counterparties (including ISDA contracts) must be signed off by the Legal and Compliance team before a transaction can be entered into. In the case of unusual transactions involving non-standard contracts or new counterparties, the Legal and Compliance team may require that external legal sign-off is obtained prior to the transaction being entered into. All original documentation is stored at an off-site document storage facility with copies maintained at Invesco's offices.
- Any regulatory requirements in dealing with counterparties will be notified to the relevant unit or staff member by the Legal and Compliance team. The relevant team or staff member will then be responsible for complying with the requirements.
- Invesco's Legal and Compliance team also independently verifies compliance with counterparty restrictions as part of its periodic surveillance program, including for applicable funds managed in an offshore investment centre.
- There is a risk that a counterparty to an asset of a portfolio, such as a derivative instrument or fixed interest security, or counterparty to a strategy (such as shorting a stock), is unable to meet its obligations under that instrument or contractual obligation. The Investment Manager of the portfolio will seek to minimise the risk by entering into transactions with a diversified range of counterparties which are, in the the Investment Manager's opinion, established and reputable.

7.5 Operations risk

Operations risk is the risk that deficiencies in the effectiveness and accuracy of internal procedures and controls will result in a material loss. The process by which Invesco manages operations risk is as follows:

- Invesco's organisational and reporting structure ensures complete separation of functions between the investment teams and operational services provided by both the Operations team and, in respect of the Funds, J.P. Morgan, N.A. Sydney Branch ("J.P.Morgan"), outsourced provider of Invesco's custody and administration services. This structure is clearly documented, with accountabilities defined at each stage. Each process has a designated process owner who is directly accountable for all functions within the process.
- Internal procedures require verification by operations of dual signatories (or equivalent approval) to every transaction. Invesco maintains a list of authorised signatories.
- J.P.Morgan as provider of administration functions is required to undertake regular reconciliations of derivative positions.
- Derivatives are valued in a manner consistent with current market practice. Derivatives are valued at market value and exposures are stated on a delta adjusted basis.
- The market value of unlisted investments, including derivatives, is usually obtained from independent external sources by J.P.Morgan (for pooled funds).
- Invesco does not generally hold the assets of any portfolio in Invesco's name, rather Invesco has appointed custodians to do so on its behalf.
- The Legal and Compliance team systematically checks internal controls and procedures.
- Invesco complies with all relevant requirements under the Corporations Act and is subject to reviews by the Australian Securities and Investments Commission.
- Invesco's Code of Ethics governs all staff trading. Staff who elect to engage in investment activities on their personal account are required to follow formal internal regulations.
- Invesco maintains a detailed security plan to ensure high level security in all areas of the business.
- Invesco's information systems are subject to audit by internal and external auditors. Invesco also has in place a comprehensive business continuity plan to enable it to deal with systems failure effectively and with minimum disruption or risk to the business.
- Recovery systems are in place for all key data.

7.6 Currency risk

Foreign currency exposure will naturally arise from investment in overseas assets and this creates another dimension of portfolio risk management.

When foreign currency exposure exists in an international portfolio, Invesco ensures such exposure is consistent with the investment strategy of that portfolio. The process by which Invesco manages currency risk is as follows:

- Implementation of hedging strategies. Hedging strategies reduce, but do not eliminate, exchange-rate risk. There is no guarantee that a currency exposure can be fully hedged against a base currency.

7.7 Leverage risk

Leverage involves the use of borrowed money or securities, or use of derivatives to increase the potential return from an investment. Leverage occurs where the level of exposure to investments exceeds the amount of cash invested. As a result leverage magnifies both potential investment gains and losses. Losses from leveraged investments can be substantial and can exceed the original amount invested. The process by which Invesco manages leverage risk is as follows:

- Diversification of the leveraged portfolio. By diversifying the leveraged portfolio, the negative correlation which exists in normal market conditions between the different investment strategies means that the overall volatility cannot be greater than the sum of the individually weighted components.

8. Personnel Management

8.1 Expertise and Supervision

Invesco's human resources policy is designed to ensure that Invesco maximises its intellectual capital by employing and developing high calibre individuals within all areas of its business.
In recruiting new staff, Invesco pays particular attention to the professional skills and experience for the position. Invesco considers the qualifications and experience, quality, and style of the individual, and seeks to ensure that the person will support its desired corporate culture.

Invesco ensures that all staff are appropriately qualified and trained to perform their key functions, and in specific cases, Invesco imposes minimum qualification requirements and requires staff to be registered with approved bodies.

Invesco's staff are held accountable for their areas of responsibility. This is only possible where the responsibilities within and across units are clear to the staff members and to management. Invesco devotes significant energy to clarifying and refining processes. The Legal and Compliance team plays a role in this to ensure that there are no gaps in the processes and the processes themselves are adequate and involve appropriate staff members.

8.2 Continuing Education

The Legal and Compliance team organises regular seminars for staff on their key areas of responsibility. Staff are also encouraged to undertake formal further training and education such as post graduate university or industry related courses.

8.3 Remuneration

All staff receive a base salary and participate in an incentive scheme. The allocation of the scheme to staff members is based on each individual's performance in his/her allocated role and is contingent on the individual complying with the terms and conditions of his/her employment with Invesco.

Staff are evaluated through an annual performance appraisal process. The appraisal process measures staff performance against agreed key result areas. Where appropriate, the key result areas will include compliance with relevant legal/regulatory requirements and client mandates. The appraisal process contributes to staff remuneration and future career development.

Invesco's incentive schemes and staff appraisal processes are designed to discourage staff from gaining personal reward or advancement for any activities that could result in risks outside client mandate conditions and internal controls.

9. Oversight of delegated investment functions

Where Invesco has delegated investment functions to an offshore investment centre, oversight of this function is performed by the Legal and Compliance team and in turn by either the Risk Management Committee or the Product Management Committee. Oversight involves review of periodic reports produced by the offshore investment centre in line with agreed procedures and reporting specified in the Product Disclosure Statement/s of applicable funds.

10. Assessment of Controls

Internal policies and procedures have been developed to be consistent with the ethos of this Statement and are in place to ensure adherence as appropriate. The extent of this adherence is monitored regularly and reported to Invesco's Risk Management Committee, which is attended by key members of senior management. Discussion also takes place at these committee meetings to ensure the ongoing relevance and suitability of these internal controls.

Senior managers are alerted to any exceptions to this Statement at the time of exception, and are involved in determination of prompt and appropriate corrective action. The process of communication and resolution is promoted by Invesco's corporate governance structure whereby the internal Risk Management Committee meets regularly.

Internal and external auditors regularly review the internal control environment as do external regulatory authorities. The results of these audits are monitored and procedures exist to ensure timely responses to recommendations.
Any changes to this Statement must be proposed to Invesco's Risk Management Committee. Once endorsed it must be approved by Invesco's Board of Directors. The Board of Directors of Invesco has approved this Derivative Risk Management Statement and attests to its sufficiency. This attestation is reiterated as part of each external audit. Invesco's Board of Directors monitors ongoing compliance with the Derivative Risk Management Statement and ensures its continued adequacy via confirmation from the Risk Management Committee.

11. Audit

Invesco's external auditor will sign off on an annual basis that this Statement exists, that the major procedures laid down in this Statement have been followed and that any changes have been approved. The audit will be completed in accordance with Australian Auditing Standards and referenced as appropriate in letters of comfort.

12. Reporting

Invesco reports to the entities responsible for mandates it manages, in accordance with the terms agreed under the relevant trust deed, constitution or investment management agreement.

13. Date of approval of this DRMS

This DRMS is dated 1 June 2015 and has been issued on the authority of the Board of Invesco Australia Limited.