JPMorgan Indian Investment Trust

Appealing valuations in long-term growth market

Investment trusts

JPMorgan Indian Investment Trust (JII) seeks long-term capital appreciation through investments in India or in companies that earn a material part of their revenues in India. There is the potential for further volatility in the market and the rupee ahead of and immediately after the national election in April/May 2014. However, valuations are reasonable by historical standards and are now at noticeably more attractive levels on an international comparison. Potential investors should weigh near-term uncertainty against appealing long-term growth potential and the risk of missing a further sharp rally.

12 months ending	Total share price return* (%)	Total NAV return* (%)	MSCI India GR GBP (%)	MSCI Emerging Markets GR GBP (%)	MSCI World GR GBP (%)
31/12/10	27.8	29.0	24.7	22.9	15.9
31/12/11	(33.7)	(31.7)	(36.7)	(17.6)	(4.3)
31/12/12	16.3	17.9	20.4	13.4	11.4
31/12/13	(10.6)	(6.5)	(5.6)	(4.1)	25.0

Note: *Twelve-month rolling discrete performance.

Investment strategy: Sustainable growth

Managers Rukhshad Shroff and Rajendra Nair aim to invest in companies with the potential for sustainable growth; they look for characteristics that will help maintain a company's market position and for opportunities to invest for further growth. Portfolio companies' management are expected to display capital discipline and sensitivity to risks. Investments are selected with a long-term horizon that is well suited to the closed-end structure of the trust. In the managers' view, this approach results in a quality bias in the portfolio, which should be appealing to investors with a similar perspective.

Indian market outlook: An interesting juncture

After a 29% decline in sterling terms between May and August 2013 the Indian market has staged a full recovery in local currency terms, but the rupee has only strengthened modestly. Looking ahead, macro and political uncertainties suggest the potential for further near-term volatility but, as the managers highlight, market valuations are at a relatively attractive level. Economic and earnings growth may now be at bottom, and in response the managers are taking the opportunity to add to the portfolio's cyclical exposure in a measured way.

Valuation: Wider discount

The trust's discount has progressively widened to 14.6%, compared with a range of 3-18% over the past three years. A further improvement in sentiment once earnings expectations and economic indicators become more favourable could see this movement reverse.

6 January 2014

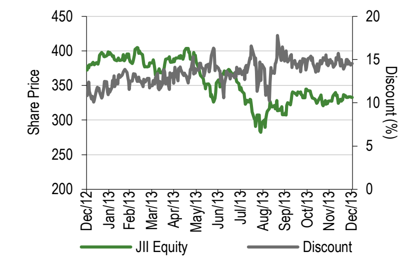
Price	**333.0p**
Market cap	**£342m**
AUM	**£421m**

NAV*	389.75p
Discount to NAV	14.6%
Yield	Nil

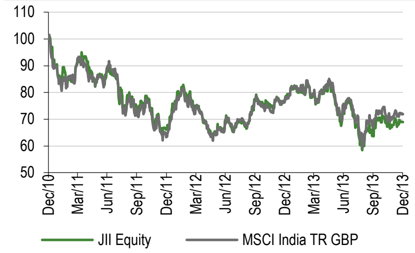
*Including income, assuming subscription shares exercised.

Ordinary shares in issue	102.7m
Code	JII
Primary exchange	LSE
AIC sector	Country specialists: Asia-Pacific

Share price/discount performance*



Three-year cumulative perf. graph



52-week high/low	405.0p	282.3p
NAV* high/low	465.03p	322.88p

*Including income.

Gearing

Gross	0%
Net	-1%

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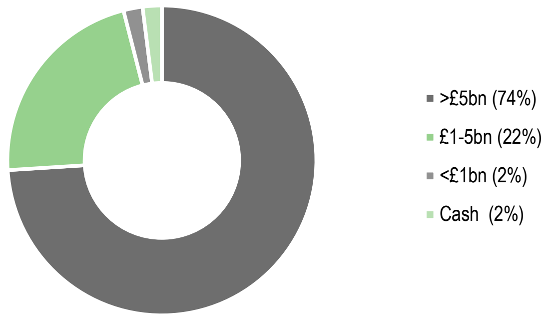
JPMorgan Indian Investment Trust is a research client of Edison Investment Research Limited

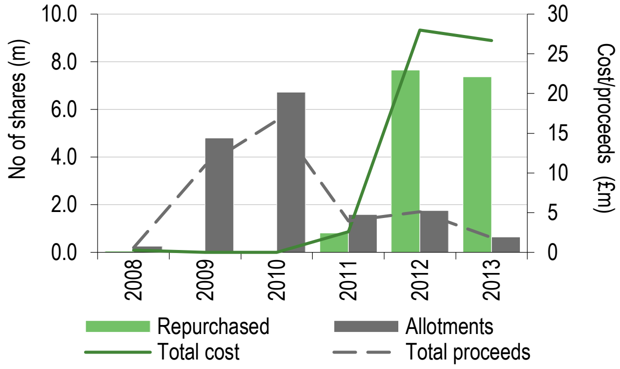
Exhibit 1: Trust at a glance

Investment objective and fund background	Recent developments
The trust seeks long-term capital appreciation through investments in India or in companies that earn a material part of their revenues in India. The company will not invest in other countries of the Indian sub-continent or Sri Lanka. The trust aims to outperform its benchmark, the MSCI India Index expressed in sterling. The company does not pay dividends, reflecting its focus on capital appreciation and the low average yield available in the Indian equity market.	20 December 2013: Full-year results announcement diluted NAV -13.7% vs benchmark index -12.7%. 31 October: Peter Sullivan to stand down from board at AGM and Rosemary Morgan to be appointed as a director from 1 December.

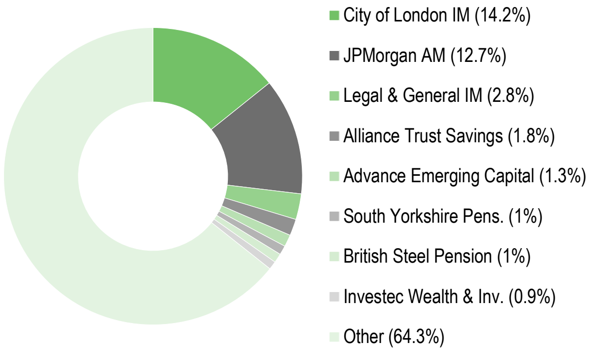
Forthcoming		Capital structure		Fund details	
AGM	30 January 2014	Total expense ratio	1.5%	Group	JPMorgan Asset Management
Preliminary results	December 2014	Net gearing	-1%	Managers	Rukhshad Shroff, Rajendra Nair
Year end	30 September	Annual mgmt fee	1.2% of total net assets	Address	Finsbury Dials, 20 Finsbury Street, London, EC2Y 9AQ, UK
Dividend paid	N/A	Performance fee	None		
Launch date	1994	Trust life	Indefinite	Phone	+44 (0)20 7742 4000
Continuation vote	Every five years	Loan facilities	$25m one year	Website	www.jpmindian.co.uk

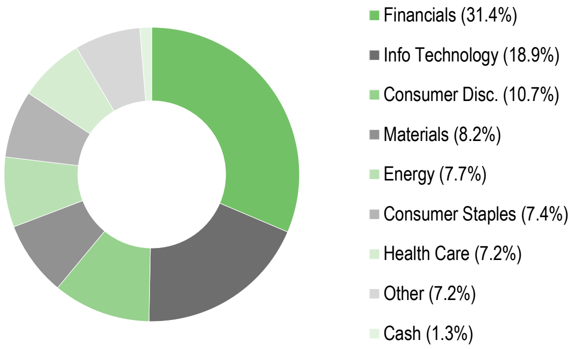
Distribution of holdings by market capital (February 2013)	Share buyback policy and history
Over 70% of portfolio assets were accounted for by companies with market caps of over £5bn.	JII is authorised both to repurchase up to 14.99% of its ordinary shares and to issue shares from treasury.





Shareholder base (as at 16 December 2013)	Sector exposures of portfolio (as at 30 November 2013)





Top 10 holdings (as at 30 November 2013)

			Portfolio weight %	
Company	**Country**	**Sector**	**30 November 2013**	**30 November 2012***
Infosys Technologies	India	Information Technology	10.9	7.8
HDFC Bank	India	Financials	9.2	10.1
Reliance Industries	India	Energy	7.7	7.2
Housing Development Finance	India	Financials	7.1	7.4
ITC	India	Consumer Staples	6.8	7.2
Tata Consultancy Services	India	Information Technology	5.5	3.6
Tata Motors	India	Consumer Discretionary	5.3	3.5
Sun Pharmaceuticals Industries	India	Health Care	4.0	N/A
Kotak Mahindra Bank	India	Financials	3.3	N/A
Ambuja Cements	India	Materials	3.1	4.2
Top 10			**62.9**	

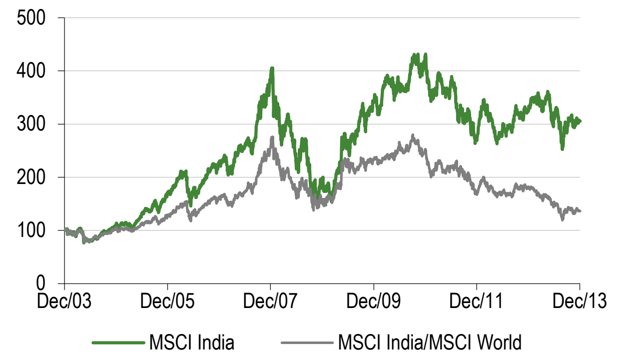
Source: JPMorgan Indian Investment Trust, Bloomberg, Edison Investment Research. Note: *Where no figure is shown for 2012 portfolio weight, the stock was not in the top 10.

Indian market outlook: Uncertainty versus potential

The attraction of a country-specific investment such as an Indian fund is that it allows investors to focus or balance the geographical mix of their portfolios according to their own requirements, potentially as an alternative to a broad emerging market fund, for example. Adding an Indian fund to a portfolio could have diversification benefits, and it would provide managed exposure to an economy expected to see much faster growth than advanced economies (and some other developing countries).

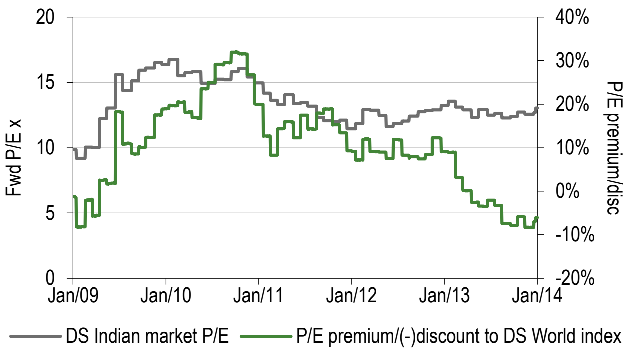
Exhibit 2 below provides a reminder of the absolute and relative performance of the Indian equity market, as represented by the MSCI index (in this case in sterling terms). Over the 10-year period the Indian market has outperformed the World index by over 50% but has been sensitive to global market corrections, and in 2013 was affected by talk of US QE tapering in May. This was amplified by significant currency weakness: for example, a c 20% weakening against sterling mid-May to end-August. The market has subsequently rallied strongly (+15% in local currency) but the rupee has only regained a small part of its depreciation, leading to a 21% gain in the sterling-adjusted index between the low point at the end of August and mid-December.

Exhibit 2: Indian market and world market



Source: Thomson Datastream. Note: Total return, £ terms.

Exhibit 3: Indian market forward P/E and relative



Source: Thomson Datastream

Where next? The Indian market is at an interesting stage for both political and economic developments. Politically, much may hinge on the outcome of the national election due in April/May 2014 and the market seems set to react favourably to a government lead by the BJP party, given the favourable response to BLP's recent successes in a number of state elections. Economically, GDP estimates have been scaled back following slower growth in 2013 and interest rates have been increased by the central bank to contain inflation. Nevertheless, Q313 GDP growth of 4.8% year-on-year was slightly ahead of the previous quarter and the IMF has forecast growth rising to 6.3% by 2015 (for comparison the estimate for advanced countries is 2.5%). Inflation, the current account deficit and the need for increased infrastructure investment remain serious concerns but these should already be factored into market thinking.

The market's 12 month forward P/E (Exhibit 3) remains modestly below its 10-year average (13.1x versus 13.3x) and has become cheaper relative to the world market, reflecting in particular the strength in the US market and the more modest growth that has prevailed in India in recent years.

We suggest that investors balance the near-term political and economic uncertainties against the possibility that the market rallies strongly on election-related news, the reasonable/attractive valuation measures and the longer-term growth potential that could be enhanced were reform measures to gain pace after the election.

Fund profile: Long-term play on Indian market

Launched in May 1994, JPMorgan Indian Investment Trust is an investment trust quoted on the London Stock Exchange and is currently the largest (market capital over £300m) of just three UK-quoted, general equity, Indian investment trusts. The country-specific fund focuses purely on Indian exposure and will not invest in other countries on the Indian subcontinent or in Sri Lanka. The trust may invest in companies that earn a significant part of their revenues in India. The fund's benchmark is the MSCI India Index expressed in sterling and currency exposure is not hedged.

The fund managers: R Shroff and R Nair

The managers' view: Positive for the medium term

Managers Rukhshad Shroff and Rajendra Nair are sensitive to the economic challenges that India faces. These include the fact that interest rates have been increased to contain inflation, the potential for further rupee weakness as QE tapering progresses, low levels of capital spending, weak consumption and high fiscal and current account deficits. Politically, there is also uncertainty over the result of the national election, which is due by May 2014 at the latest.

Despite these points, the managers are actually more positive now on a medium-term view. This reflects a number of factors. As far as the economy is concerned, while there are risks, there are some glimmers of light with third quarter GDP growth increasing sequentially, consistent with the managers' expectation that growth (and corporate earnings growth) is at or close to the bottom.

The managers do not see the recent state elections as a reliable indicator of the result of the approaching national election but make the interesting point that, on a medium-term view, the election of either a strong Congress- or BJP-led coalition should be favourable for the market as it would provide a degree of certainty. In the nearer term, a clear victory for the BJP could be greeted euphorically by the market, posing something of a dilemma for investors ahead of the event.

Most importantly, they regard current valuations as being attractive (see comments on page 3), particularly given that much of the bad news ought to be baked into market thinking. The managers' response is to stick with their measured approach, adding modestly to cyclical holdings on the basis that the most likely outcome is a gradually improving economic environment that should feed through to earnings over time.

Asset allocation

Investment process: Select for profitable sustainable growth

In implementing their consistent investment process, the two managers have the benefit of substantial experience and work with the four other members of the India team in Hong Kong[1] and Mumbai. They also have access to the broader JPMorgan Asset Management business to provide multi-asset insights and profile with corporates. Total India-dedicated equity funds' AUM is over $4.5bn, most of which is managed from Hong Kong.

The managers aim to identify companies with the potential for profitable sustainable growth. They take into account whether companies have sustainable advantages and look for businesses with the opportunity to reinvest cash flow profitably to benefit from a compounding effect. The valuation

[1] In common with other managers that manage offshore Indian assets, JPMorgan Asset Management managers must be located outside India to ensure tax efficiency for fund/trust investors.

approach looks beyond 12-month forward P/Es, factoring in growth and sustainability of profits over a long-term horizon.

Target company management should have a focus on profitability and exercise capital discipline so returns on equity are not needlessly diluted. A clear understanding of risk by management is also important. This is particularly salient in the financial sector, where the managers avoid some former state-owned financials companies on the basis that the culture is not sufficiently risk-sensitive.

Turning to portfolio construction, the managers aim to understand the sources of expected return and size positions according to the level of conviction in an idea. Fundamental developments are tracked for evidence of departure from expectations that might call the original investment case into question. Risks are monitored closely with attention paid to intended and unintended exposures. Sell decisions are based on three key triggers: if the managers make and recognise an investment mistake, if the investment achieves its objective or if a more compelling opportunity is identified.

The managers believe outcomes from their investment process include a quality bias in their selections, a long-term mindset[2] and conviction borne of a comprehensive valuation framework and team discussions.

Overview

The fund has 42 holdings, of which 20 are outside the MSCI benchmark Index, accounting for about 17% of the asset value. The benchmark index has 71 constituents, compared with more than 5,200 and 1,600 listed on the BSE and NSE exchanges respectively. As at the end of November 2013, the top 10 portfolio holdings accounted for 62.9% of net assets (index 54.5%). Equities were 98.7% of assets, cash 1.3% and there was no fixed income allocation.

Exhibit 4: Sector allocation

	End November 2013 (%)	End November 2012 (%)	Change (%)	Benchmark end November 2013 (%)	Trust active weight (%)	Trust weight/Benchmark weight
Financials	31.4	34.1	-2.7	24.0	7.4	1.3
Consumer discretionary	10.7	9.4	1.3	6.8	3.9	1.6
Materials	8.2	11.2	-3.0	6.7	1.5	1.2
Cash	1.3	3.3	-2.0	0.0	1.3	N/A
Telecomms services	3.3	2.2	1.1	2.6	0.7	1.3
Health Care	7.2	5.3	1.9	6.7	0.5	1.1
Utilities	1.9	1.6	0.3	3.7	-1.8	0.5
Industrials	2.0	3.2	-1.2	4.5	-2.5	0.4
Information technology	18.9	12.8	6.1	21.9	-3.0	0.9
Consumer staples	7.4	8	-0.6	11.1	-3.7	0.7
Energy	7.7	8.9	-1.2	12.0	-4.3	0.6
	100.0	**100.0**		**100.0**	**0.0**	

Source: JPMorgan Indian Investment Trust, Edison Investment Research. Note: Benchmark is MSCI India £ Index.

Current portfolio positioning

The direct geographical exposure of the trust is straightforward as a single country fund. Indirect exposures in, for example, the Information technology sector, would qualify this focus, but essentially the trust is geared to Indian developments.

As illustrated in Exhibit 4, sector-active weights were recently between +7.4% and -4.3% of the benchmark index, with financials as the largest overweight. The financials sector accounts for over 30% of the portfolio, giving broad exposure to development in the Indian economy.

Between November 2012 and November 2013 the weightings in the Materials and Financials sectors were reduced, while the Information technology sector increased (though the trust remained underweight versus the benchmark). As noted earlier, the managers are gradually increasing the weighting to cyclical stocks to benefit from a medium-term improvement in the economy.

[2] Average portfolio turnover of 25% over the last two years is evidence of this mindset.

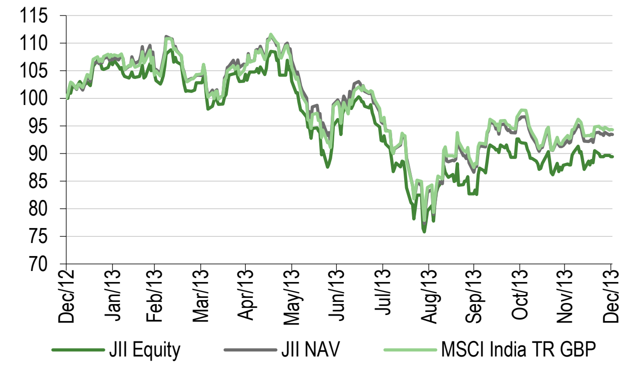
Performance: 10-year outperformance

The trust's NAV total return performance has been quite close to the benchmark over one, three and 10 years. There was a period of underperformance in the first half of 2009, which affected the five-year performance, followed by a partial recovery in 2010 and 2011 and then a stable relative performance. The NAV relative performance for the trust, compared with the World Index, has shown weakness over one-, three- and five-year periods but significant outperformance for the 10-year period (Exhibit 6).

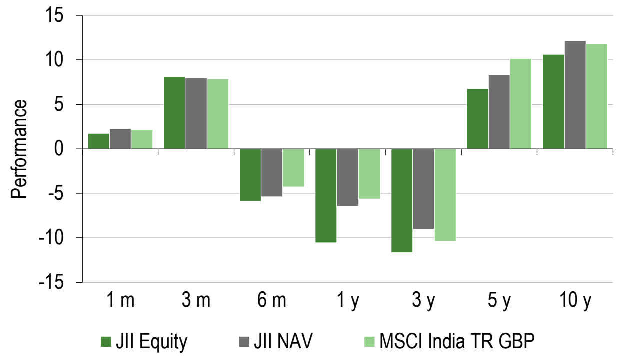
Looking at risk-adjusted returns, the Sharpe ratios for one, three and five years, of -0.4, -0.3 and 0.5 are low, but are not substantially different from the peer averages.

Exhibit 5: Investment trust performance

Price, NAV and benchmark total return performance, one-year rebased



Price, NAV and benchmark total return performance (%)



Source: Thomson Datastream, Edison Investment Research. Note: three, five and ten year performance figures annualised.

Exhibit 6: Share price and NAV total return performance, versus benchmarks (percentage points)

	One month	Three months	Six months	One year	Three years	Five years	10 years
Price versus MSCI India	(0.4)	0.2	(1.6)	(4.9)	(3.0)	(23.3)	(31.7)
NAV versus MSCI India	0.1	0.1	(1.1)	(0.8)	3.4	(13.0)	9.0
Price versus MSCI Emerging Markets	4.3	8.5	(4.7)	(6.5)	(20.7)	(37.0)	(47.6)
NAV versus MSCI Emerging Markets	4.8	8.4	(4.2)	(2.4)	(14.4)	(26.7)	(7.0)
Price versus MSCI World	0.7	2.4	(13.1)	(35.6)	(64.3)	(41.1)	50.2
NAV versus MSCI World	1.2	2.3	(12.6)	(31.5)	(58.0)	(30.7)	90.8

Source: Thomson Datastream, Edison Investment Research. Note: Data to end-December 2013 and indices £ adjusted.

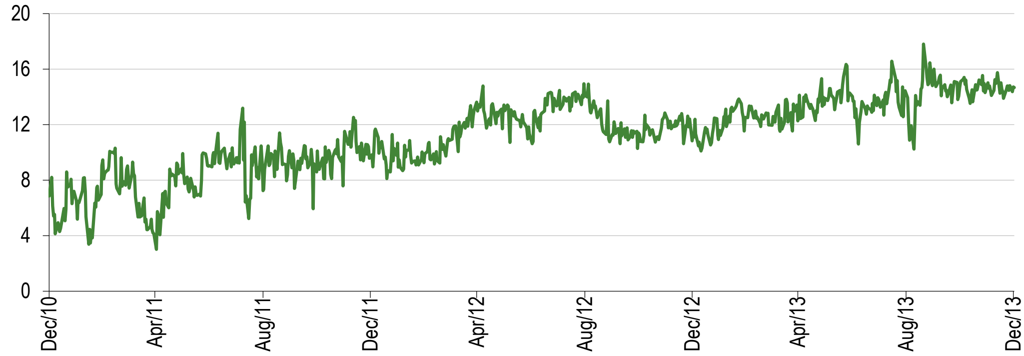
The impact of rupee/sterling translation moves is not hedged and therefore included in the NAV performance. Over the one, three and five years to end December 2013 the rupee weakened against sterling by 13%, 31% and 32% respectively.

Discount: Has widened over three years

The board operates a share repurchase programme that aims to moderate volatility in, and the absolute level of, the share price discount to NAV. An explicit discount target level has not been stated. In calendar year 2013 the company repurchased 7.4m shares at a cost of £26.7m: this is approaching the level of 2012 (7.7m shares and £28m).

Over the past year the discount has fluctuated in a band between 10% and 18% (Exhibit 7) and has recently steadied at c 15%. Against the backdrop of considerable market and currency volatility the widening of the discount over the past three years is perhaps not too surprising but does suggest the scope for a significant narrowing, assuming political and economic concerns ease over time.

Exhibit 7: Discount over three years



Source: Morningstar, Edison Investment Research. Note: Positive values indicate a discount; negative values indicate a premium.

Capital structure and fees

As at the end of December 2013 JII had 120.6m ordinary shares and 5.5m subscription shares in issue. Each subscription share conferred the right, but not an obligation, to subscribe for one ordinary share on any business day until 2 January 2014 at a price of 291p. At end-December, the dilutive effect on the NAV per share of assuming exercise of the subscription rights was 1.3%. The company may buy back up to 14.99% of the issued share capital and issue new shares representing approximately 10% of the existing capital.

The trust has an unlimited life subject to a continuation vote due at its AGM in January 2014 and every fifth year thereafter. Subject to the vote, the board has announced that the management fee will be reduced from 1.2% of assets less current liabilities to 1% of total assets. Other things being equal, we would assume this could reduce the historical ongoing charge by a similar amount from 1.5% to 1.3%. The management contract notice period will be reduced from one year to six months for performance reasons (still one year for other reasons). The board will also be obliged to make a tender offer at NAV less costs if, over the three years from 1 October 2013, the company underperforms its benchmark.

The trust may employ gearing for tactical purposes up to a maximum of 15% of shareholders' funds; the company has a one-year floating rate loan facility of $25m with the Royal Bank of Scotland. At end November net cash stood at about 1.3% of net assets and, while it has been at a low level in recent years, the managers would be prepared to raise gearing significantly were they to become sufficiently confident about the investment outlook for the Indian market, taking into account the economic, political and valuation positions.

Dividend policy

The company does not pay a dividend, reflecting the low prevailing yield in the Indian market (about 1.4% for the MSCI India index) and the trust's emphasis on capital appreciation. The managers believe this matches the growth-centred expectations of most overseas investors in India.

Peer group comparison

As Exhibit 8 illustrates, there is only a small peer group of sterling-denominated, closed-ended funds devoted to general Indian equities. Among the four funds shown, JII ranks second for total

NAV return over three years and third over one and five years. We also include selected mutual funds where sterling classes are available; the average performance for these funds is similar to the investment trust average over one and three years but higher for five years (72.5% versus 53.8%). Reflecting the relatively high volatility of the market and currency, the Sharpe ratios for all the trusts are low over the periods shown but have improved in the shorter term. Otherwise we note that gearing is absent for all the trusts while the average TER is below that for the open-ended funds. JII is differentiated from the other investment trusts by the absence of a performance fee.

Exhibit 8: Funds investing in general Indian equities: Total returns, Sharpe ratios and discounts

% unless stated	Market cap/fund size £m	NAV TR 1 year	NAV TR 3 year	NAV TR 5 Year	NAV TR 10 year	Sharpe 1 year (NAV)	Sharpe 3 year (NAV)	Discount (ex par)	Ongoing charge /TER	Perf. fee	Net gearing
DPF India Opportunities Ord	47.5	(0.4)	(28.3)	49.6		0.1	(0.2)	(4.9)	2.21	Yes	99
India Capital Growth Ord	26.6	(9.2)	(37.1)	8.4		(0.4)	(0.5)	(22.7)	2.70	Yes	94
JPMorgan Indian Ord	338.7	(6.8)	(25.0)	48.5	214.4	(0.4)	(0.3)	(15.2)	1.49	No	99
New India Ord	121.6	(1.6)	(16.1)	80.0		(0.3)	(0.2)	(14.8)	1.56	Yes	99
Weighted average		**(5.2)**	**(23.9)**	**53.8**	**135.8**	**(0.4)**	**(0.2)**	**(14.6)**	**1.63**		**99**
Mutual funds											
Aberdeen Global - Indian Equity	2805.2	(2.5)	(16.9)	91.5	233.8				2.11		
BlackRock Global Funds - India	250.3	(8.2)	(31.6)	45.4					2.04		
Fidelity Funds - India Focus	939.6	(7.8)	(26.9)	68.5					2.04		
Franklin India	525.9	(6.7)	(24.9)	61.2					1.92		
HSBC Global Indian Equity	1509.4	(15.3)	(38.8)	49.3					1.94		
Jupiter Global Fund India Select	175.2	(14.0)	(29.1)	60.8					1.84		
Average (wtd)		**(7.3)**	**(25.3)**	**72.5**					**2.03**		

Source: Morningstar 2 January 2014. Note: TR=total returns of NAV for investment trusts, TER=total expense ratio. The Sharpe ratio is a measure of risk-adjusted return. The ratios we show are calculated by Morningstar for the past 36-month period by dividing a fund's annualised excess returns over the risk-free rate by its annualised standard deviation. Net gearing is total assets less cash/cash equivalents as percentage of shareholders' funds.

The board

The board (six members, all non-executive and independent of the manager, with date of appointment in brackets) are Hugh Bolland (chairman, 2004), Richard Burns (senior independent director, 2006), Nimi Patel (2011), Hugh Sandeman (2012), Rosemary Morgan (2013) and Peter Sullivan (2007, to stand down at AGM, January 2014). Rosemary Morgan was appointed 1 December 2013 and brings experience managing Japanese equity portfolios and an Asian and emerging markets multi-manager business.

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