

RBKC Pension Fund Liquidity Policy

1. Introduction

This policy sets out the principles and procedures governing the management of surplus cash within The Royal Borough of Kensington and Chelsea Pension Fund (the Fund). Effective liquidity management is paramount to optimise returns, mitigate risks, and fulfil the Investment Committee's fiduciary responsibilities. This policy articulates a framework for the prudent management of surplus cash, ensuring alignment with the fund's strategic goals and risk appetite.

2. Policy Objectives

The Liquidity Policy is adopted by the Fund in line with the Fund's Investment Strategy Statement and with the following objectives in mind:

- **Optimisation of surplus cash:** Ensure surplus cash is efficiently utilised to generate positive that returns that align with the fund's investment objectives and its approach to risk.
- **Liquidity Management:** Maintain adequate liquidity levels to meet operational requirements, fund redemptions, and unforeseen fund expenses whilst minimising the opportunity cost of holding cash.
- **Risk Management:** Mitigate liquidity risk by establishing prudent guidelines for cash management and asset allocation, ensuring resilience to market fluctuations and unexpected liquidity demands.
- **Compliance and Governance:** Adhere to regulatory requirements and industry best practices in liquidity management.
- **Enhanced Returns:** Explore opportunities to enhance returns on cash holdings through strategic asset allocation and short-term investments.
- **Flexibility and Agility:** Maintain flexibility in liquidity management strategies to adapt to changing market conditions, capitalise on emerging opportunities, and manage risk effectively.
- **Long-Term Sustainability:** Support the Fund's long-term sustainability by preserving capital and maximising risk-adjusted returns over time, ensuring prudent cash management practices and adherence to fiduciary responsibilities.

By pursuing these objectives, the Fund aims to establish a robust framework for liquidity management that enhances financial performance, mitigates risk, and preserves the integrity of the fund's investment mandate.

3. Definition of Surplus Cash

Surplus cash relates to investment cash holdings that exceed the predetermined strategic asset allocation for the Fund's investment portfolio. It represents funds held in excess of the targeted allocation percentages, as agreed by the Investment Committee and outlined in the fund's strategic asset allocation (Appendix 1). It is crucial to differentiate surplus cash from any strategic cash reserves which are intentionally held in the Fund's Nat West bank account and used to pay pensions and other benefits/expenses and are not subject to the liquidity policy.

Surplus cash arises when cash holdings surpass the levels required for maintaining the desired asset allocation mix and liquidity needs specified by the fund's strategic allocation. This surplus may result from factors such as periodic cash inflows, capital distributions, or timing discrepancies in deploying funds to illiquid assets which typically require longer periods for investment

execution. Surplus cash levels will fluctuate over time based on market conditions, investment activities, and changes in liquidity requirements.

Identifying and monitoring surplus cash is fundamental to the Fund's liquidity management approach, ensuring that cash resources are effectively used to support investment objectives while maintaining sufficient liquidity buffers for operational contingencies and capital preservation.

4. Liquidity Management Process

The liquidity management process of the Fund is designed to ensure the effective monitoring and use of surplus cash. This process encompasses the following key components:

Regular Monitoring: The Investment Committee receives regular reviews of investment assets highlighting deviations from strategic allocations and allows for reviews on rebalancing to take place as appropriate. These reviews consider factors such as cash inflows and outflows, upcoming obligations, and potential investment opportunities.

Strategic Asset Allocation: Surplus cash is evaluated within the context of the Fund's strategic asset allocation framework. The Investment Committee considers the target allocation percentages for various asset classes and adjusts cash holdings accordingly to maintain alignment with the Fund's long-term investment objectives.

Reporting and Oversight: The Investment Committee receives regular reports on cash positions to enable informed decision-making and provide transparency regarding the performance of surplus cash within the Fund's investment portfolio.

Opportunistic Investments: When surplus cash exceeds strategic allocation levels, the Investment Committee may evaluate opportunistic investment opportunities across asset classes. These may include money market instruments, short-term fixed income securities, or other liquid assets that offer favourable risk-adjusted returns within the Fund's investment mandate.

Risk Management: The liquidity management process incorporates robust risk management practices to mitigate liquidity risk and preserve capital. Liquidity risk is measured by the level of cash flow required over a specified period; and is managed by assessing the level of cash held to limit the impact of the cash flow requirements on the investment cash policy.

Operational Efficiency: Efforts are made to optimise operational processes related to cash management, including cash flow forecasting, and cash positioning to ensure timely deployment of surplus cash.

By adhering to this liquidity management process, the Fund aims to maintain liquidity at levels that support operational needs while maximising returns on cash holdings within the confines of its risk appetite. This proactive approach to liquidity management enhances the Fund's resilience to market fluctuations and ensures alignment with its long-term investment objectives.

5. Allocation Policy of Surplus Cash

In managing surplus cash, the Fund adheres to a structured approach based on liquidity needs and investment guidelines. The following hierarchy outlines the prioritised allocation options:

- 1) **Rebalancing Existing Asset Classes:** Surplus cash should first be allocated towards rebalancing existing asset classes to realign the portfolio with its strategic asset allocation targets.
- 2) **Holding cash with the Custodian:** Where cash cannot be immediately deployed to underweight assets, an initial option is to hold cash with the Fund's custodian, Northern Trust. Cash held with the custodian is deposited into a money market fund with interest rate calculated daily¹ and incurs no additional fees. Performance is benchmarked against the Sterling Overnight Index Average (SONIA).
- 3) **Investing in Short-Term Fixed Income Securities:** In certain circumstances, where it is not appropriate to hold the cash with the Custodian, or if the Fund wishes to diversify its cash holding, the Investment Committee may consider allocating funds in short-term fixed income securities.

By following this hierarchy for deploying surplus cash, the Fund aims to optimise returns, manage liquidity effectively, and maintain alignment with the investment strategy statement. These allocation options provide flexibility whilst allowing the Fund to capitalise on investment opportunities as they arise whilst prudently managing risk.

6. Review and Revision

Cash updates and performance, including liquidity management practices and the handling of surplus cash and liquidity risk, will be incorporated into the Fund's annual report to stakeholders. These updates will undergo regular review at Committee meetings to ensure transparency and ongoing evaluation of liquidity management strategies.

¹ www.northerntrust.com/united-kingdom/what-we-do/investment-management/pooled-funds (Sterling Fund, class A)

Appendix 1: Strategic Allocation

	Longer Term Target	Review Range
Listed Equity	70%	+/- 5%
Baillie Gifford – Global Active	20%	+/-3%
BlackRock Global Passive	50%	+/-3%
Private Equity	5%	+/-2%
Property	20%	+5/-2%
Index Linked Gilts	5%	-2%
Total	100.0%	