Royal Borough of Kensington and Chelsea Pension Fund

Rebalancing Policy

1. Introduction and principles

1.1. Rebalancing is the process of realigning the weights of a portfolio of assets. It involves buying and selling assets in a portfolio to ensure a desired asset allocation or level of risk.

1.2. Portfolio rebalancing can safeguard the Fund from being overly exposed to undesirable risks, whether that be at the asset class level (e.g., the equity weighting materially increasing above it strategic weight) or at the investment manager level.

1.3. It can also be return enhancing to the extent that it involves selling assets which have performed well, and therefore might have become expensive, and buying assets which have lagged.

1.4. Rebalancing steps should therefore be taken to ensure that aggregate total risk is broadly maintained at the Fund's desired level.

1.5. Rebalancing will give rise to transaction costs and should therefore not occur more frequently than is needed to keep total risk broadly in line with target.

1.6. It is not felt necessary to have an annual rebalance to the target allocation because this will tend to result in many small transactions together with costs that are not likely to improve the Fund's overall risk-return characteristics.

2. Rebalancing considerations

2.1. The drivers of rebalancing are the review ranges. These are set with some latitude to avoid frequent rebalancing alerts and unnecessary transaction costs.

2.2. Consideration of volatility of asset classes and transaction costs incurred are factored into individual asset class tolerance ranges. Review ranges also consider individual portfolios, assets held for effective diversification have a narrower review range to ensure that they are not over or underrepresented in the portfolio.

2.3. Cash flow into/out of the Fund or income generated by the assets held in the Fund should be used to move asset allocations closer to target if this will significantly contribute to rebalancing.

2.4. Investment Committee will review asset allocation at each meeting and review any proposal for rebalancing. Valuation at quarterly end dates may not align with Investment Committee, in these instances where a review range is triggered, a provision will be made to convene committee members for discussion and decision, as necessary. The Chairman has authority to agree with officer's action needed. If required, an urgent decision may be made by the Executive Director of Resources in consultation with the Chairman.

2.5. Rebalancing proposals will always be submitted to Committee before implementation and will be a standing item at each meeting. Giving the timing of meetings,

3. Review range

3.1. The rebalancing policy ensures that the Fund's asset allocation remains broadly aligned with the strategic benchmark.

3.2. The Investment Committee has agreed central allocations for each asset class and also for each manager. These are formally reviewed annually as part of the review of the Investment Strategy Statement but can also be reviewed at any Investment Committee. The rebalancing policy is also considered as part of the annual review.

3.3. The current central allocations and ranges are as follows:

	Strategic Target	Review Range
Listed Equity	70%	+/- 5%
Baillie Gifford – Global Active	20%	+/-3%
BlackRock Global Passive	50%	+/-3%
Private Equity	5%	+/-2%
Adam Street	5%	+/-2%
Property	20%	+5/-2%
Directly managed	20%	+5/-2%
Gilts	5%	-2%
Index Linked	5%	
Cash	0%	n/a
LGIM Stirling Liquidity Fund		
Cash held with custodian		
Total	100.0%	

3.4. Review ranges have been set around central positions and are not expected to be breached often.

3.5. The implementation of the policy is different for liquid assets and illiquid assets. Currently, the Fund's liquid assets are deemed to be global equities and cash (75% total strategic target). Property and private equity are deemed illiquid (25% total strategic target).

3.6. In the event of a breach of either an individual portfolio or an asset class, the Investment Committee has agreed the processes detailed below:

4. Liquid asset – review range breach

4.1. Equities

4.1.1. A drift from the strategic target is monitored by officers on at least a quarterly basis.

4.1.2. The allocation to equities is considered first. If the allocation to equities overall is outside its ranges (i.e. above 75% or below 65%), then action should be taken to move the overall equity allocation to the central target (i.e. 70%). This will be implemented in the first instance by selling/buying the holding in the equity manager that is most over-/under-weight so that that manager's weighting moves to its central allocation. The same action is then taken with the second-most over-/under-weight manager, and potentially also the third. In the event of a sale of equities, the proceeds should be directed to cash or to the most underweight illiquid asset class if it is readily possible to increase the allocations to that asset class. Conversely, if equities overall are below their threshold, then cash or potentially an illiquid asset class that can be realised easily should be used as the source of funds.

4.1.3. If there are breaches of individual fund manager targets, rebalancing will take place as necessary to bring allocations into line. In the first instance this should be achieved by switching between equity mandates, but more likely will involve a similar process to that described in the paragraph above.

4.1.4. In exceptional circumstances a rebalance may not be executed. For example, if there are no viable alternatives available.

4.1.5. Additional allocation to cash is permitted but will only be considered as a final option.

4.1.6. A report will be presented at the next Investment Committee if there have been any developments relating to rebalancing.

4.2. Cash

4.2.1. Cash has no strategic target and is overweight due to the property mandate actual allocation lag. Until the property target is met, it is expected that there will be a variance between the cash and property actual allocation which offset each other.

4.2.2. Cash will not be rebalanced unless as a result of rebalancing other underweight assets.

5. Illiquid assets – review range breach

5.1. Property

5.1.1. Since 2019/20, The Fund has acquired several directly managed properties as it progresses towards the strategic target allocation. Unlike liquid investment assets, purchasing property is a lengthy bidding process in a competitive environment, giving no guarantee of completion.

5.1.2. The Fund's pooled property assets are winding down and as they are realised, will be held in cash to fund upcoming property purchases.

5.1.3. If the property review range is triggered due to a fall in market value, the Fund will consider increasing commitments and acquiring further property.

5.1.4. In the event the review range is triggered due to an increase in market value, the Fund will review the valuations for a period of at least 12months before considering sale of assets.

5.1.5. Any property marketed for sale will only be sold if a suitable buyer and price can be established.

5.2. Private equity

5.2.1. The Fund takes a broad approach to the private equity strategic target by modelling commitments to meet the 5% allocation target. It is recognised that achieving the desired exposure level can take a long time.

5.2.2. If the projected exposure to private equity exceeds the review range, a reduction or pause of future commitments will be considered at Investment Committee. The allocation will be monitored until it falls back into line with the strategic target.

5.2.3. If the asset allocation falls below the review range, the Fund will consider up to date modelling of additional commitments to bring the exposure back into line with the strategic allocation.

5.3. Index-Linked Gilts

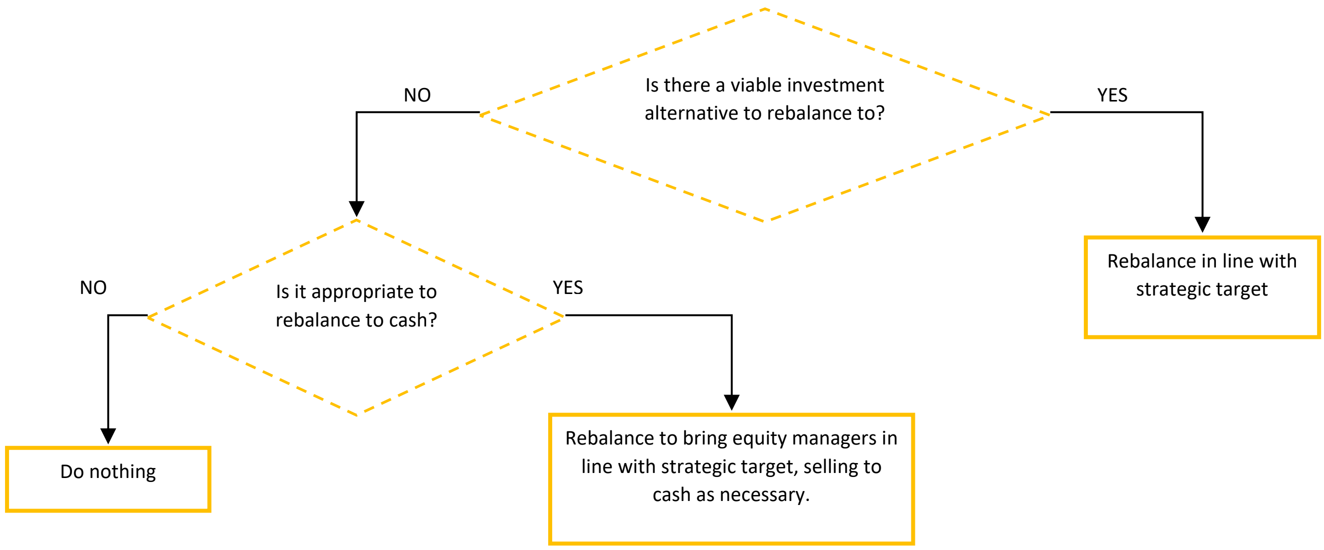
5.3.1. The Fund has acquired gilts to hold until maturity, and therefore no sell trigger is set.

5.3.2. A breach of -3% will trigger the notification at the next Investment Committee meeting. This will include a market update and review as to why the breach has occurred, before making a rebalancing decision.

5.3.3. Index-linked gilts are held to mitigate against inflation. Therefore, market conditions, including interest rates, inflation expectations, and demand for bonds, will need to be considered. This will be presented as part of the rebalancing standing agenda item.

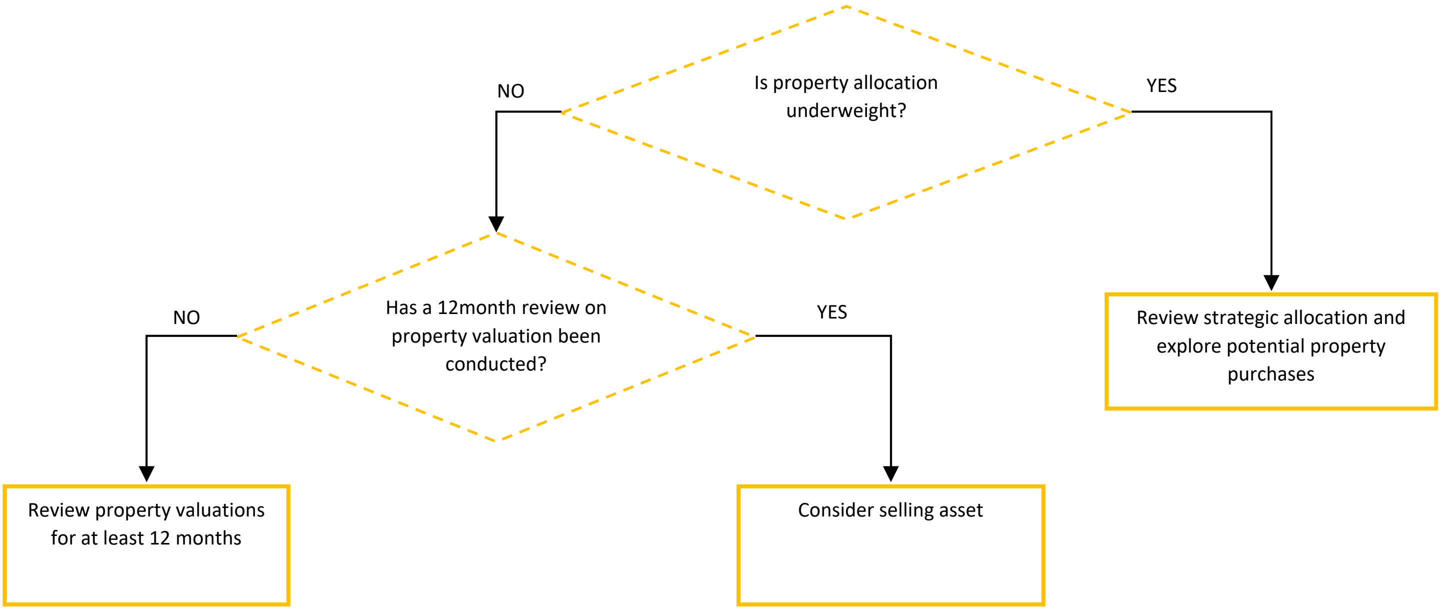
Liquid assets

Global equity review range breach:



Illiquid assets

Property review range breach:



Private equity review range breach: