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Liquidity risk management guide

Managing liquidity risk is fundamental to managing scheme property and investments. In doing so, the law requires Managers to exercise care, diligence and skill. This guide outlines how Managers and Supervisors can demonstrate they are effectively managing and overseeing liquidity risk.

FMA
FINANCIAL MARKETS AUTHORITY
TE MANA TĀTAI HOKOHOKO

About FMA guidance

Our guidance:

- explains when and how we will exercise specific powers under legislation
- explains how we interpret the law
- describes the principles underlying our approach
- gives practical examples about how to meet obligations.

Guidance notes: provide guidance on a topic or topic theme. Typically we will seek industry feedback via a public consultation paper, or more targeted consultation before we release a guidance note.

Information sheets: provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

You might also like to check the reports and papers on our website. For example, our monitoring reports describe actual practice we are seeing and our comments on this.

Document history

This version was issued in April 2024. It replaces the April 2020 Liquidity risk management good practice guide.

Contents

Introduction

Purpose of this guide

The Financial Markets Authority – Te Mana Tātai Hokohoko (**FMA**) promotes and facilitates fair, efficient and transparent markets, and the confident and informed participation of businesses, investors and consumers.

Managed funds have a critically important role in financial markets. Investors put money into managed investment schemes to gain income and preserve or grow their capital, and expect to be able to withdraw money, or transfer between schemes, in a timely way.

Fund liquidity is about how fund assets can be sold without negatively impacting the price of those assets or needing to secure funding (if applicable). Good management of fund liquidity is an important part of delivering fair outcomes for consumers and markets. It is critical to ensuring investors are treated equitably, and that funds perform and operate in line with the information given to investors. It also plays an important role in supporting orderly and stable markets, particularly during volatile conditions.

Scheme managers must manage withdrawal and transfer requests effectively under all market conditions. This helps to ensure investors are treated equitably. Poorly managed liquidity risk may mean some investors unfairly bear the costs of others leaving the fund, or force managers to sell fund assets for a lower price than would otherwise be the case.

This guidance updates and replaces our 2020 *Best practice guide for liquidity management and stress testing.* It focuses on managed funds[1] but is intended to assist all licensed managers of managed investment schemes (**Managers**) and supervisors of those schemes (**Supervisors**) to consider liquidity risk management (**LRM**) at all stages of fund management – from fund design to day-to-day liquidity management and contingency planning – and particularly at times of heightened market uncertainty and volatility.

Statutory duties

Under financial markets legislation, Managers and Supervisors must exercise care, diligence and skill in performing any duties or exercising any powers. The law also requires Managers to treat scheme participants equitably, and both Managers and Supervisors to act in the best interests of scheme participants.[2]

Managers are required to demonstrate they are capable of effectively performing the service as part of being granted a market services licence, which includes appropriately implementing, monitoring, and reviewing liquidity risk management for each scheme.[3]

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[1] As defined in regulation 5(1) of the Financial Markets Regulations 2014 (**FMC Regulations**).
[2] Sections 143 and 153 of the Financial Markets Conduct Act 2013 (**FMC Act**).
[3] See section 396(c) of the FMC Act, and refer to the licensing guide for managed investment scheme managers, available on our website here: Managed investment scheme manager

To meet the definition of a managed fund, the managed investment products must be offered in the ordinary course of business on the basis they are continuously offered and redeemed on a basis calculated wholly or mainly on the value of the scheme property or least 80% of the scheme's assets meet liquidity requirements in regulations.[4] This requires sufficient liquidity management to ensure the service can be offered.

Given these clear statutory requirements, we expect all managed funds to have appropriate LRM-related policies, processes and tools. Failure to do so is likely to mean Managers and Supervisors are not meeting their statutory duties. We also encourage managers of wholesale schemes, which have not opted to become a registered scheme, to consider this guidance, even though they are not subject to the same statutory duties.

[4] See the FMC Regs, r 5(1), which defines managed fund and under (a)(ii)(A)-(C) which specifies these thresholds.

Background

This guidance builds on the focus of the Financial Stability Board (**FSB**) and International Organisation of Securities Commissions (**IOSCO**) on effective liquidity risk management and on the FMA's previous work, following the two most recent global market shocks.

Global financial crisis

After the global financial crisis, the FSB and IOSCO recommended that regulators devote closer attention to the liquidity stress testing practices of open-ended collective investment schemes. To protect investors, ensure fair, efficient and transparent financial markets and reduce systemic risk, those organisations recommended that:

a. liquidity risk be further embedded in funds' design and day-to-day operations,

b. the availability and use of liquidity risk tools be widened,

c. regulatory reporting and public disclosure of liquidity risk be improved; and

d. regular fund and system-level stress testing be carried out.

The FMA's 2020 best practice guide reminded Managers of our expectations about risk management, particularly during heightened market uncertainty and global volatility. In August 2020, we received 51 Manager responses to a self-assessment survey on liquidity management practices, and in July 2021 we published recommendations about managed investment scheme (MIS) LRM practices, which observed that:

a. Managers were overly optimistic about their LRM capabilities, and even the relatively strong performers had gaps in particular areas, including frequency of stress testing, use of available liquidity management tools (**LMTs**) and metrics.

b. Managers should avoid becoming complacent about their own capabilities. MIS boards/oversight bodies need to maintain effective oversight and provide constructive challenge, including:

   - forming their own view of the LRM capabilities, maturity and culture of their entity; and
   - assessing the extent to which these enable the MIS to operate consistently within its defined risk appetite and policy settings, identify any desirable changes, and ensure management takes steps to address those changes.

Recent recommendations

Following heightened market volatility during the COVID-19 pandemic, IOSCO published findings from a detailed review of jurisdictions representing over 92% of global assets under management[5], and the FSB published an assessment of the effectiveness of its previous liquidity mismatch recommendations[6].

Those reports noted scope for fund managers to better and more consistently use LMTs during normal and stressed market conditions (e.g. swing pricing during the COVID-19 market shock) for less-liquid assets that offer daily dealings, and to pass redemption costs to redeeming investors.

In December 2023:

a. the FSB finalised policy recommendations on liquidity mismatch in open-ended funds, including the need for anti-dilution LMTs in constitutional documents, and greater and more consistent use of anti-dilution LMTs in normal and stressed market conditions.[7]

b. IOSCO also finalised guidance on anti-dilution LMTs, which covers factors and parameters including operations, design, oversight and disclosures, and use of those LMTs on subscribing and redeeming investors.[8]

We have considered these recommendations in preparing this guidance, together with submissions made on the draft version of the guide, which was released for public consultation in September 2023.

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[5] Thematic Review on Liquidity Risk Management Recommendations FR13/22 (November 2022)
[6] Assessment of the Effectiveness of the FSB's 2017 Recommendations on Liquidity Mismatch in Open-ended Funds (December 2023)
[7] Revised Policy Recommendations to Address Structural Vulnerabilities from Liquidity Mismatch in Open-Ended Funds (December 2023)
[8] Anti-dilution Liquidity Management Tools – Guidance for Effective Implementation of the Recommendations for Liquidity Risk Management for Collective Investment Schemes (December 2023)

Effective LRM

Managers

Managers must exercise care, diligence and skill when developing and implementing policies, processes and tools for managing liquidity risk effectively. Effective and appropriate LRM is an important part of how a Manager demonstrates it is meeting its legal responsibilities to act in the best interests of scheme participants and treat those participants equitably.

Managers must ensure their schemes have adequate systems, policies, processes and tools to manage and monitor liquidity risk, and use them when appropriate (particularly during deteriorating market conditions and increased investor redemptions).

Managers are responsible for deciding what standards, testing and reporting requirements are appropriate for:

a. the assets under their management
b. the expected redemption timeframes that have been communicated to investors; and
c. the LMTs they have available.

These will vary for each Manager along with the range of potential liquidity shocks and size of investor holdings. These policies, processes and tools need to be reviewed regularly.

As part of good practice, Managers should consider informing their Supervisor of any sudden significant changes in the liquidity profile of the funds they manage as soon as they occur.

Supervisors

Supervisors are the frontline regulators for MIS and are responsible for overseeing Managers' LRM. A Supervisor exercising care, diligence and skill must regularly assess a Manager's LRM policies, processes and tools, and have an active oversight role.

This should be a fund-level, risk-based assessment with appropriately tailored frequency, scope, and intensity. It should consider whether the fund has an adequate level of resilience to liquidity stress. Supervisors can supplement their assessments by monitoring a combination of internal reports, market information and periodic surveys.

Supervisors should clearly identify the circumstances or concerns that may prompt reporting under section 203 of the FMC Act. This level of oversight is important to ensure the Supervisor can notify the FMA under section 203 of possible (or actual) contraventions of Manager obligations, and what steps (if any) the Supervisor intends to take.

The FMA’s focus

The June 2021 MIS LRM review outlined our recommendations to Managers, graded by priority level. The high-priority recommendations have been incorporated into this guidance. Managers should review and consider whether to implement all features applicable to their schemes.

Key improvements we would like to see are:

a. better frameworks, policies and procedures covering LRM

b. more regular stress testing

c. more tailored LMTs made available for use.

We will engage with Supervisors in the first instance to continue to monitor Managers’ LRM and how LRM relates to overall systemic risk and, drawing on market engagements and Supervisor reports (if any), combine information sets to form a system-wide view. We will monitor Supervisors to ensure LRM framework assessments are conducted effectively. We will also continue to engage with the market from time to time as LRM standards and market conditions develop.

Features of effective LRM

We set out below our view of the features of LRM. Our views are based on standard international frameworks, adapted for New Zealand's markets. Managers must consider how these features apply to their operations and to each of their funds, and must implement them as appropriate in that context. Together, these features enable Managers to measure liquidity, carry out suitable stress testing, and – most importantly – use LMTs when required.

Governance and infrastructure (Features 1-3)

Feature 1 – Overarching framework and strategy

The Manager has a documented process for identifying and managing liquidity risk, supported by robust contingency planning. This process is supported by liquidity risk management policies and procedures, and integrated into the Manager's broader risk management framework, to achieve alignment between the fund's redemption terms and its investment strategy.

1.1 The LRM framework, strategy and supporting processes:

a. Clearly articulate a liquidity risk tolerance that is appropriate for the fund's investment strategy.

b. Consider and cover situations and circumstances across a range of market conditions, including extreme adverse (but plausible) conditions.

c. Are appropriate, relevant and sufficiently bespoke for the fund(s) under management, by considering and addressing characteristics including:

- investment strategy
- target investor base
- investor demographics
- investor concentration and expected redemption patterns
- size of the fund relative to the underlying market
- distribution channels
- asset selection.

d. Evaluate liquidity risk at both individual asset level and portfolio level, and ensure alignment and consistency with redemption obligations (and other liabilities).

e. Ensure cash flows from assets, liabilities and off-balance-sheet items are considered over an appropriate set of time horizons.

1.2 The Manager does not solely rely on LMTs to manage liquidity.

Feature 2 – Governance

The Manager's LRM has good governance arrangements, including board and senior management approval, oversight and review.

Approval and ongoing review

2.1 The Manager's board and senior management review and approve the entity's LRM framework as required, documenting the triggers for such reviews. They are satisfied that the framework meets the objectives of managing liquidity risk effectively, that investors are treated equitably, and that key matters (such as LMTs) are sufficiently described in the empowering trust documents. Their reasons for holding these views are clearly recorded.

Reporting and oversight

2.2 The Manager is responsible for determining its own internal liquidity risk reporting requirements. Liquidity risk reporting will include liquidity risk early-warning metrics (and supporting triggers and flags), and will account for the correlation between measures, e.g. valuation and liquidity. The Manager ensures the board and senior management have appropriate oversight and understand the liquidity risk reporting and its importance.

Assurance

2.3 Where appropriate, the Supervisor provides independent oversight of LRM framework reviews. Controls for reviewing and maintaining the Manager's LRM are part of its compliance assurance programme, including in-depth testing of processes and controls.

Integration into wider risk management

2.4 The Manager's board and senior management ensure the identification, assessment, and management of liquidity risks are part of its overall risk management framework.

Feature 3 – Contingency plans

The Manager has a formal liquidity contingency plan (LCP) that clearly sets out its strategies for addressing liquidity shortfalls in emergency situations.

3.1 The LCP:

a. Outlines policies to manage a range of stress environments.

b. Establishes clear lines of responsibility.

c. Includes clear initiation, escalation and withdrawal procedures.

d. Is regularly tested and updated to ensure it is operationally reliable.

3.2 The LCP:

a. Explains the circumstances where LMTs are used so they can be initiated/activated, deployed, and withdrawn in an effective manner, and has early-warning triggers to prompt proactive consideration. This is important in deciding whether high-impact LMTs should be implemented (such as suspending redemptions).

b. Specifies what divestment strategies are to be used and their sequence, e.g. pro-rata or 'slicing' approach.

3.3 The Manager understands the legal basis and requirements for the appropriate use of each LMT it intends to deploy as part of its LCP. This includes knowing in advance what information must be provided to investors, the Supervisor and the FMA, and being able to act quickly and with assurance.

Design, disclosure, and communication (Features 4-5)

Feature 4 – Product design

The Manager ensures its offered subscription and redemption terms are appropriate for its investment strategy and product offering.

4.1 The Manager considers the liquidity risk of the underlying investment products when designing a new product or making changes to an existing one.

> *45% of Managers had not undertaken stress testing during the product design phase, missing a key opportunity to determine any necessary and desirable LMTs, metrics, and potential effects of changes in micro/macro-economic variables from the outset.*
>
> FMA 2021 LRM survey, pg. 5

4.2 During the product design phase, the Manager explicitly:

a. Assesses the suitability of its product offering against the investment strategy and vice-versa, under a range of market conditions (normal and stressed).

b. Ensures that liquidity risks, LRM processes and LMTs are (or will be) in place and are effectively disclosed to investors.

c. Determines a suitable dealing frequency for units in the fund, based on the target investor base, the investment strategy and objectives, and the expected liquidity of the assets. This should include seeking strong assurance that redemptions can be met under both 'normal' and 'extreme but plausible' market conditions.

d. Considers how the scheme aligns with the definition of 'managed fund' in regulation 5 of the FMC Regulations to ensure that, for example, the redemption terms of underlying assets are suitable for the fund's design.

4.3 The Manager keeps under review the redemption terms of existing offerings, to ensure liquidity of assets and transacting terms remain aligned as time passes.

Feature 5 – Disclosure and communication

The Manager provides investors with sufficient information to understand how the fund manages liquidity risk and how this may affect their investment, and proactively communicates with investors when changes are made and during times of market or fund-specific stress.

Disclosure

5.1 The Manager ensures investors are aware of the fund's liquidity risk through effective disclosure in the documents made available to investors[9], including:

- the fund's redemption terms and processes, such as (but not limited to):
  - the cutoff time for determining the price at which units are redeemed
  - the time taken to process withdrawal requests
- if applicable to the fund, that there is a material allocation to illiquid assets.

5.2 The Manager also ensures liquidity risk disclosure is provided to retail investors in the product disclosure statement (**PDS**). This includes a brief summary of impacts to investors from the use of high-impact LMTs.

5.3 More detailed information on the use and impacts of LMTs is included in other documents, such as the Statement of Investment Policy and Objectives (**SIPO**), Other Material Information (**OMI**), and other policy documents. Links between disclosure documents should be clear and up to date.

5.4 A Manager using leverage ensures this is effectively disclosed to investors in the PDS.

Communications

5.5 The Manager proactively engages with investors, and in particular ensures investors are made aware of any material changes relating to the fund(s), about:

a. what LMTs the Manager can use

b. the cutoff time for determining the price at which units are redeemed

c. the time taken to process withdrawal requests.

5.6 Communication with investors, the Supervisor and other stakeholders are more frequent and more detailed in times of fund-specific or market-wide stress.

[9] Such as the PDS, SIPO, or OMI, and other policy documents.

LRM capabilities (Features 6-10)

Feature 6 – Monitoring framework

The Manager appropriately monitors and reports on levels of liquidity and liquidity risk in its funds to allow effective oversight and decision-making.

6.1 Monitoring processes enable the Manager to identify emerging or evolving liquidity issues in underlying asset markets, redemption flows or other liabilities before they materially impact the fund.

6.2 Effective monitoring typically:

a. Sets appropriate liquidity thresholds that are proportionate to the liquidity of the underlying asset market(s) and redemption obligations and flows.

b. Measures key metrics (including time to liquidate funds, price impact of liquidation, and settlement and timing lags).

c. Uses reliable and up-to-date data.

d. Is conducted at a frequency that reflects the wider market conditions (e.g. increasing during market volatility).

This is not an exhaustive list.

6.3 The Manager has a working definition of ‘illiquid asset’ that is appropriate for the fund(s) asset composition. The definition of ‘managed fund’ in the FMC Regulations[10] provides a base-level definition that the Manager has tailored to the specific fund(s) it manages. The definition is used alongside other monitoring measures (such as current time to liquidate) to monitor and manage relative asset liquidity across the fund. It supports oversight of asset liquidity at all levels, including the board.

6.4 Monitoring is integrated with the LRM framework to identify early warning signs and signal when more extensive liquidity analysis is required, whether LMTs are to be deployed, and whether other remedial steps are necessary if vulnerabilities are identified.

6.5 The Manager and its Supervisor work together to determine an appropriate frequency for reporting the findings of this monitoring. The monitoring report should be coupled with information about any LMTs (particularly redemption suspensions) that have been deployed. This allows the Supervisor to stay informed about potential liquidity pressures. The Supervisor is kept informed about any changes to the LRM framework, including the addition or removal of LMTs, through this reporting process.

> *45% [of Managers surveyed] reported not having a definition of ‘illiquid’ asset… [and] 49% of Managers [surveyed] do not use any ‘early warning’ metrics, increasing the risk they will be unprepared for a liquidity event.*
>
> FMA 2021 LRM review, pg. 6-7.

[10] See r 5(1) of the FMC Regulations

Feature 7 – Liquidity management tools

The Manager has a range of appropriate LMTs readily available to deploy in specific circumstances, including where redemption obligations cannot be met in the ordinary course of business. This ensures the scheme operates in the best interests of investors and supports equitable treatment of scheme participants.

Defining tools

7.1 The Manager explicitly defines the LMTs it has available for use, assesses conditions under which these will be deployed (and withdrawn), and considers how their use ensures equitable treatment of scheme participants.

7.2 The LMTs may be categorised in terms of when they can be used:

- **Pre-emptive tools**: to anticipate and prevent liquidity issues;
- **Reactive tools**: to address liquidity issues after they emerge; or
- **Both**: pre-emptive and reactive.

and by their type:

- **Quantity-based**: such as redemption gates/withdrawal limits, temporarily suspending redemptions by suspending net asset value (NAV) calculations, or suspending redemptions (in extreme situations);
- **Price-based**: such as anti-dilution levies, subscription/redemption fees, valuation at bid or ask prices, dual pricing and swing pricing;
- **Others:** such as side pockets, and redemptions in kind.

In assessing conditions under which LMTs might be deployed, the Manager has a graduated strategy for the use of LMTs. For example, swing pricing will usually be applied during normal market conditions. Where market conditions deteriorate, the Manager may move to deploying reactive tools, such as a notice period for redemptions and redemption gates, before progressing in a crisis to consider suspending redemptions.

> *We note some specific concerns with LMT availability, with 12 managers [nearly 25% of the 51 respondents] being affected by one or more of the following issues:*
>
> - *Having no LMTs at all*
> - *Having no LMTs to deal with current or severe crises (e.g. redemption suspension or redemption gating)*
> - *… having no LMTs that could be used in advance to help mitigate an emerging crisis*
>
> FMA 2021 LRM review, p. 22.

Using tools

7.3 In using LMTs, the Manager acts in the best interests of scheme participants and treats scheme participants equitably by preventing the fund from materially diverging from its investment strategy. This includes:

a. Ensuring redemption and valuation policies and practices are as fair as possible to all scheme participants. Tools such as swing pricing and buy/sell spreads may be used to ensure the costs of trading are borne by investors driving those trades, rather than by the fund.

b. Considering the appropriateness of the LMT for the circumstances and ensuring any stated conditions for the use of the LMT are met, including any required approvals from the Manager's board and/or Supervisor.

> *Only half of the Managers surveyed have ever used an LMT of any kind, calling into question their ability to select an appropriate LMT, including those suited to a variety of crisis situations, at an appropriate time/stage of the crisis escalation. This, coupled with an overreliance on liquid assets as the default response to a liquidity crisis, could lead to liquid assets proving insufficient. The collective impact of such a response may conflict with the fundamental principle of fair treatment of investors.*
>
> FMA 2021 LRM review, p.6

Suspending redemptions in managed funds (including KiwiSaver)

Managers should have appropriate tools to manage transfer and redemption requests, including, in extreme circumstances, being able to temporarily suspend redemptions. These tools must be appropriately disclosed to investors (through the PDS or Other Material Information).

For voluntary transfers between KiwiSaver providers, Managers of schemes involved in the transfer may agree to any longer period than the default 10 working days as expressly provided in section 56(4) of the KiwiSaver Act 2006.

We expect Managers, exercising care, diligence and skill would make such agreements in good faith to appropriately manage fund liquidity in situations such as extreme market conditions or scheme-specific liquidity issues.

Feature 8 – Stress testing

The Manager has a stress testing framework for each scheme it manages, with appropriate settings for governance and oversight, scenario testing, and ongoing liquidity risk management.

8.1 The Manager's stress testing results are integrated into all stages of the fund product lifecycle, including product design (when determining the dealing and distribution arrangements and asset composition), and ongoing investment management.

8.2 If stress testing is undertaken by a third party, the Manager remains responsible and will satisfy itself that the results have been properly considered in decision making.

8.3 Stress test results can be used to:

a. Support the determination and assessment of appropriate dealing arrangements for the fund, considering its investment strategy and underlying assets, even under stressed scenarios.

b. Help identify any necessary adjustments to the fund's dealing arrangements, investment strategy and underlying assets (including the holdings of liquid assets).

c. Help formulate action and contingency plans to deal with plausible stressed market conditions using different LMTs.

Governance and oversight

8.4 Stress testing has an appropriate governance structure with clear objectives and upwards reporting lines, and is reviewed regularly by the oversight body (e.g. the MIS's board, executive committee, or senior management).

8.5 Where practicable, stress testing is independent from the Manager's investment management function.

8.6 The Manager has records of the reasons for deciding why its approach to, and frequency of, stress testing is appropriate, including any decision documents provided to the oversight body. It holds records of stress testing results, including any actions in response to stress testing, and makes changes to LRM and LMTs (where appropriate) based on the outcomes of testing.

Scenario testing

8.7 Stress tests will be carried out on normal, and extreme (but plausible) scenarios, and clearly identify sources of relevant risks impacting fund liquidity.

8.8 The Manager is responsible for ensuring testing is carried out at appropriate intervals for the nature and characteristics of the fund.

8.9 The frequency and nature of stress testing should be suited to the fund. It should capture material and relevant drivers (risks) impacting fund liquidity, and apply stresses that are sufficiently severe.

8.10 Testing ordinarily includes:

a. fund size and composition

b. investment strategy

c. underlying assets and their concentration, pricing, valuation assumptions, and valuation errors
d. investor profile/large withdrawals
e. market factors and disruptions
f. regulatory requirements and expectations
g. nature, complexity and resources required of the stress testing
h. any other variables the fund considers relevant,

and could include backward-looking historical scenarios or forward-looking hypothetical scenarios.

> *48% of [surveyed] fund-of-funds Managers said they do not ensure their underlying funds perform stress tests.*
>
> FMA 2021 LRM review, pg. 7.

Feature 9 – Use of leverage to adjust risk/return

Where the Manager makes use of leverage (traditional balance sheet or synthetic leverage) to boost expected investment returns, the risks and impact for the fund/s and for the broader financial system (i.e. counterparty channel) in the event of financial distress are well understood and taken into account in the Manager's LRM policies and its communication with investors.

9.1 A Manager using leverage ensures this is effectively disclosed to investors in the PDS.

9.2 A Manager using leverage also:

a. Values derivative positions at market.
b. Quantifies its market risk under adverse market conditions against limits, performs stress simulations, and forecasts cash investing and funding needs.
c. Assesses the credit risk arising from derivatives activities based on frequent measures of current and potential exposure against credit limits.
d. Reduces credit risk by broadening the use of multi-product master agreements with close-out netting provisions.
e. Authorises only professionals with the requisite skills and experience to transact and manage the risks, as well as to process, report, control and audit derivatives activities.
f. Establishes management information systems sophisticated enough to measure, manage and report the risks of derivatives activities in a timely and precise manner.

Feature 10 – Record keeping, data and systems

The Manager has appropriate LRM records, and reliable data and systems that support effective analysis and management of liquidity risk.

Record keeping

10.1 The Manager ensures appropriate records are kept relating to the performance of its LRM process. These records will evidence the performance of LRM, and be in a form that is easily accessible and suited to communications with investors and frontline regulators, e.g. a chronology of the use of LMTs, decisions, and results.

Data and systems

10.2 The Manager generates accurate and reliable risk data to meet normal and stress/crisis reporting requirements. Data will be aggregated in a reliable manner to minimise potential errors and create a robust and holistic view of the relevant risks.

10.3 The Manager ensures it has access to, or can effectively estimate, relevant information for liquidity management at the product design stage and on an ongoing basis. For example, in the case of a managed fund investing in other funds, there should be the ability to obtain relevant information about the underlying funds, or at a minimum develop reliable proxies.

10.4 Relevant information will be both quantitative and qualitative, and include information on:

a. marketing and distribution channels

b. historical redemption patterns

c. past asset and liability characteristics and performance/behaviour.

10.5 In instances where the ability to 'look-through' to underlying funds or components is constrained, estimates or proxy information should be developed. The Manager also considers the heightened risk that results from this.

Evaluation and review (Feature 11)

Feature 11 – Evaluation and review

The Manager and Supervisor regularly review LRM practices to ensure ongoing suitability and inform areas for improvement.

11.1 Both the Manager and Supervisor undertake regular evaluation and reviews of fund LRM practices to ensure these remain effective and fit for purpose. This includes looking at each of the features outlined in this guidance and completing a gap analysis of actual and expected performance.

11.2 The Manager has recorded how its LRM practices are reviewed and evaluated. The Manager has considered the appropriate frequency for reviewing its LRM practices and recorded the reasons why it has adopted that frequency.

Regulatory responses

Supervisors are the frontline regulators of MIS and have primary responsibility for ensuring Managers are implementing effective LRM. Having effective LRM is integral for a Manager to show that it is meeting its statutory duties to exercise appropriate care, diligence and skill, and act in the best interests of scheme participants and treat them equitably.

In our engagements with industry, we will look to understand how Supervisors have engaged with Managers and how Managers have considered their own liquidity risks and implemented appropriate LRM in the context of the funds they manage. Where Managers have not considered features in this guide, we are likely to seek explanations about how they are effectively managing their liquidity risk.

The FMA has a wide range of regulatory responses available if we consider a Manager or Supervisor is, or is likely to be, in breach of their responsibilities. Any action taken will depend on the severity and extent of misconduct, considering prevailing market conditions and any ongoing or potential investor harm.

For example, there may be instances where engagement and amendment through dialogue is sufficient to address a breach. In other cases, a formal feedback letter, public warning, stop order or direction order may be more appropriate. If poor practices appear widespread, we may publish findings from our monitoring to help inform the market.

For more information on the regulatory options available to the FMA, please refer to our Regulatory Response Guidelines.

Chronological bibliography

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