HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON ECONOMICS

REVIEW OF THE FOUR MAJOR BANKS AND OTHER FINANCIAL INSTITUTIONS SUPERANNUATION SECTOR

First State Super	
FSS63QW:	Can you please advise what arrangements you have provided to **defer** the payment of rent for tenancies for **assets owned** by your fund as a result of keeping SMEs operational during the COVID-19 pandemic? And to what dollar value has that reduced revenue to your fund since 1 February 2020?
FSS64QW:	Can you please advise what arrangements you have provided to **defer** the payment of rent for tenancies for **assets controlled** by your fund as a result of keeping SMEs operational during the COVID-19 pandemic? And to what dollar value has that reduced revenue to your fund since 1 February 2020?
FSS65QW:	Can you please advise what arrangements you have provided to **adjust** the payment of rent for tenancies for **assets owned** by your fund as a result of keeping SMEs operational during the COVID-19 pandemic? And to what dollar value has that reduced revenue to your fund since 1 February 2020?
FSS66QW:	Can you please advise what arrangements you have provided to **adjust** the payment of rent for tenancies for **assets controlled** by your fund as a result of keeping SMEs operational during the COVID-19 pandemic? And to what dollar value has that reduced revenue to your fund since 1 February 2020?
Answer:	First State Super has invested in property assets across the sub-sectors of office, industrial, retail, residential and aviation. Our focus, across the property assets we own and those we control, has been compliance with the National Cabinet Mandatory Code of Conduct for commercial leasing (the Code). While external asset management teams process requests for relief under the Code, we engage with these teams weekly to ensure that applications are considered in a timely and reasonable manner. This is aligned with First State Super's purpose to be a force for good in the community and a responsible owner, while meeting our fiduciary duty to deliver appropriate returns to our members. To date, most direct requests for relief from commercial tenants have been for deferral of rent. As the process to review requests for relief is ongoing, it is not possible to estimate the reduced revenue that would reflect all requests received to date. Approximately one-third of our tenants have requested some form of rental relief and we have already approved the majority of these requests with a number still under review. We continue to track the progress of this process through our regular engagement with the external asset management teams.

HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON ECONOMICS

REVIEW OF THE FOUR MAJOR BANKS AND OTHER FINANCIAL INSTITUTIONS SUPERANNUATION SECTOR

First State Super	
FSS67QW:	On 1 January 2020 what was your percentage share and nominal value of your listed and unlisted assets?
Answer:	On 1 January 2020:

	Percentage share	Nominal value
Listed assets	74%	$75.9b
Unlisted assets	26%	$27.1b
Total assets	100%	$103.0b

Following the successor fund transfer of StatePlus Retirement Fund to First State Super, the data presented above includes State Plus listed and unlisted assets.

HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON ECONOMICS

REVIEW OF THE FOUR MAJOR BANKS AND OTHER FINANCIAL INSTITUTIONS SUPERANNUATION SECTOR

First State Super	
FSS68QW:	On 1 January 2020 did your fund have liquidity issues resulting from honouring obligations to members?
Answer:	No.

HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON ECONOMICS

REVIEW OF THE FOUR MAJOR BANKS AND OTHER FINANCIAL INSTITUTIONS SUPERANNUATION SECTOR

First State Super	
FSS69QW:	What write down, if any, has been made to the value of unlisted assets?
Answer:	Please refer to the valuation policy provided (FSS06.1QW). First State Super's investments are valued regularly to reflect values that are fair and reasonable. Given current economic conditions, First State Super is monitoring and managing potential impacts to our unlisted portfolio particularly closely, including any impact to valuations. We use independent parties to assist in the valuation of our unlisted assets to ensure the valuations are fair. We have considered and reviewed valuations across the unlisted portfolio on an asset by asset basis, to ensure that they appropriately reflect the impact of recent events and conditions. Unit prices reflect the latest valuation.

HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON ECONOMICS

REVIEW OF THE FOUR MAJOR BANKS AND OTHER FINANCIAL INSTITUTIONS SUPERANNUATION SECTOR

<table>
<tr><td>First State Super</td><td></td></tr>
<tr><td>FSS70QW:</td><td>Listed companies holding infrastructure assets have had write downs of around 40 per cent:
a. How does this compare to your write down of unlisted assets?
b. If there is a difference, why is there a difference?</td></tr>
<tr><td>Answer:</td><td>a. It is important to acknowledge that unlisted markets behave differently from listed markets. We expect greater day to day volatility in stock markets where price changes can move significantly even within one day’s trade, as traders and investors react to both positive and negative information about a very wide range of factors. Markets can be driven by emotional reactions and pricing can also reflect the elements of supply and demand for listed equity capital which can further exacerbate listed prices versus the underlying asset’s intrinsic value.

Having said that, First State Super and its independent valuers have regard to comparable listed company valuations alongside a range of other inputs when determining ongoing valuations of unlisted assets. We are diligent in our valuation approach and believe it provides both protection for investors and a realistic representation of value with independent validation and audit.

b. First State Super’s largest asset in an investment in Australian land registries, for which there is no direct listed equivalent available in Australia or overseas. Further, as noted above, when determining ongoing valuations of unlisted assets, regard is given to a range of inputs including the valuations of comparable listed companies. However, there are a range of factors driving listed equity markets that are not present in unlisted companies, such as supply and demand (e.g. more sellers than buyers) for shares.</td></tr>
</table>

HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON ECONOMICS

REVIEW OF THE FOUR MAJOR BANKS AND OTHER FINANCIAL INSTITUTIONS SUPERANNUATION SECTOR

First State Super	
FSS71QW:	Have you had any liquidity issues in honouring your obligations to members as a result of the: a. recent decline in the share market? b. permission by the Federal government to allow members to remove up to $10,000 per financial year if they lose their job?
Answer:	a. No. b. No. Like many funds we will continue to work with regulators and actively review these positions given the considerable uncertainty around economic conditions and government policy as a result of Covid-19.

HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON ECONOMICS

REVIEW OF THE FOUR MAJOR BANKS AND OTHER FINANCIAL INSTITUTIONS SUPERANNUATION SECTOR

<table>
<tr><td>First State Super</td><td></td></tr>
<tr><td>FSS72QW:</td><td>What has been the current reduction of the value of your fund, and the unlisted and listed components since 1 January 2020?</td></tr>
<tr><td>Answer:</td><td>See response to FSS67QW for the value of the listed and unlisted assets as at 1 January 2020.

The table below shows the position as at 29 April 2020, a reduction of 7.4%.

<table><tr><th></th><th>Percentage share</th><th>Nominal value</th></tr><tr><td>Listed assets</td><td>72%</td><td>$69.0b</td></tr><tr><td>Unlisted assets</td><td>28%</td><td>$26.4b</td></tr><tr><td>Total assets</td><td>100%</td><td>$95.4b</td></tr></table></td></tr>
</table>

HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON ECONOMICS

REVIEW OF THE FOUR MAJOR BANKS AND OTHER FINANCIAL INSTITUTIONS SUPERANNUATION SECTOR

First State Super	
FSS73QW:	How many members have **requested the early release** of their superannuation since 12 March 2020, and to what value? Please also provide monthly updates on the first of the month for the remainder of 2020 to the secretariat.
Answer:	For the period from 12 March 2020 to 29 April 2020, the number of members who requested the early release of their superannuation under the Covid-19 compassionate ground and the value was as follows: First State Super also receive and process requests for early release of superannuation for Compassionate Grounds and Financial Hardship as set out in the legislation.

	Requests	Value
Covid-19 Compassionate	12,337	$107.6m

HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON ECONOMICS

REVIEW OF THE FOUR MAJOR BANKS AND OTHER FINANCIAL INSTITUTIONS SUPERANNUATION SECTOR

First State Super	
FSS74QW:	How many members have **had approved the early release** of their superannuation since 12 March 2020, and to what value? Please also provide monthly updates on the first of the month for the remainder of 2020 to the secretariat.
Answer:	For the period from 12 March 2020 to 29 April 2020, the number of members who requested the early release of their superannuation under the Covid-19 compassionate ground and the value was as follows:

	Approvals	Value
Covid-19 Compassionate	12,138	$106.2m

A further 59 requests totalling $408k are awaiting processing.

HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON ECONOMICS

REVIEW OF THE FOUR MAJOR BANKS AND OTHER FINANCIAL INSTITUTIONS SUPERANNUATION SECTOR

First State Super	
FSS75QW:	If some members have required the early release of their superannuation since 12 March 2020 and not been approved, please provide details of the grounds on which they have not been approved.
Answer:	Grounds for not approving the early release of superannuation for include: • Payment rejection where incorrect bank account details have been provided • Requests from pension accounts • Revocations caused by member error or a MyGov system limitation which did not allow members to change an accidental application for \$10 rather than \$10,000 • Instances of identified fraud • The member had already exited, was not found or had an insufficient balance to process the amount requested.

HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON ECONOMICS

REVIEW OF THE FOUR MAJOR BANKS AND OTHER FINANCIAL INSTITUTIONS
SUPERANNUATION SECTOR

First State Super	
FSS76QW:	Liquidity management: a. What is your fund's process for complying with APRA's prudential framework which requires trustees to have a liquidity management plan? b. How is the plan being reported to the trustee directors? c. Who is responsible for the day-to-day liquidity management for the fund?
Answer:	a. Please see the attached Liquidity Management Policy. The process for invoking the Liquidity Action Plan is in section 4.7. b. As we have not breached our stressed market liquidity limits (i.e. our illiquid assets are less than normal market limits), there is no prescribed requirement to have a Liquidity Action Plan in place. However, as a precaution, the Investment Committee moved the Liquidity Action Plan to an "Amber" status that requires additional monitoring by the Chief Investment Officer and the Head of Investment Risk. Updates are circulated to the Investment Committee at least weekly or more frequently if required. In addition, the Investment Committee (which meets at least six time per annum) and Board (which meets ten to eleven times per annum) are updated with our liquidity position at every meeting. c. The Liquidity, Fixed Income and Markets team within the Investments team monitor the early warning thresholds and alert the Management Investment Committee and Head of Investment Risk if an early warning indicator threshold is breached. In the event that a liquidity event occurs (i.e. the illiquid assets of the Fund become greater than the normal market limits), the Trustee has delegated the creation of a Liquidity Action Plan to the Chief Investment Officer, who acts as the initial escalation point and determines the appropriate course of action. The Head of Investment Risk is responsible for the oversight of the LAP.

Liquidity Management Policy

First State Superannuation Scheme:

Accumulation Section (**Accumulation Division**)

Defined Benefits Section (**DB Division**)

StatePlus Section (SP Division)

collectively "the **Fund**"

Contents

Revision History

Version	Reason for amendment	Date approved	Approving Committee/Board
November 2016	Establishment of stand-alone policy	FSS IC: 23 November 2016 FSS Board: 7 December 2016	Investment Committee Board
April 2018	Alignment with StatePlus Liquidity Policy	FSS: 4 April 2018 StatePlus: 1 November 2018	Investment Committee
February 2019	Annual Review; update Liquidity Action Plan following IGF triennial audit; re-define cashflow monitoring threshold;	FSS: 20 February 2019 StatePlus: 28 February 2019	Investment Committee
February 2020	Annual review; updated for migration of StatePlus Retirement Fund assets and products to FSS and product alignment	FSS: 19 February 2020	Investment Committee

1 Introduction

This *Liquidity Management Policy* (the **Policy**) is applicable to the registrable superannuation entity (**RSE**) offered by FSS Trustee Corporation (**FTC,** the **Trustee**).

1.1 Purpose

This document outlines the key elements of the Policy for the First State Superannuation Scheme:

- Accumulation Section (**Accumulation Division**);
- Defined Benefits Section (**DB Division**); and
- StatePlus Section (**SP Division**).

The purpose of the Policy is to describe FTC's understanding and definition of liquidity and liquidity risk in the context of the Fund, including setting out the principles and strategies FTC considers when managing liquidity risk in both normal and stressed liquidity environments. The establishment, monitoring and maintenance of this Policy should help ensure that:

- the liquidity position of the Fund, and individual investment options, are clearly articulated;
- the liquidity risks affecting the Fund, and individual investment options, are identified and understood;
- the liquidity risk of potential new asset classes, or changed proportions of existing asset classes, and how these will affect the Fund, and individual investment options, are identified and understood; and
- a Liquidity Action Plan (**LAP**) is formulated for each of the Fund's investment options.

The collective monitoring of the above measures will assist with ensuring that there are sufficient funds available to meet payments, transfers and withdrawals for the Fund's members, while retaining member equity.

1.2 Governing Legislation and Regulatory Requirements

The key elements of the legislative requirements are contained within:

- Superannuation Industry (Supervision) Act 1993 (**the SIS Act**); and
- APRA Prudential Standard SPS530 - Investment Governance.

1.3 Delegations, Responsibilities and Accountability

The Trustee is at all times responsible for the Fund's investments. This includes establishing, reviewing and giving effect to an investment strategy for each investment option that has regard to the liquidity of the investments covered in the strategy and the expected future cash flow requirements.

The Trustee has delegated responsibility for managing liquidity risk to the Investment Committee (**IC**), who in turn, has delegated this to the Management Investment Committee (**MIC**) and the Chief Investment Officer (**CIO**).

Details of these delegations are set out in the relevant committee charters, Investment team delegations and the *Consolidated Board Delegations Manual*.

In order to ensure the day-to-day process for liquidity management is conducted effectively, including under stressed operating conditions, specific responsibilities are assigned to each of the named areas in Schedule A.

1.4 Review

This Policy will be reviewed annually, and more frequently if deemed appropriate.

Any changes to the Policy will be provided to the IC for its review and approval.

2 Definition of Liquidity and Illiquidity

The liquidity of an investment is generally considered to be a measure of how quickly it can be converted to cash without negatively impacting its value. Hence, the key factors that influence investment liquidity relate to its nature and characteristics, such as:

- the type of investment, e.g. equity, bond, property, OTC derivative;
- the structure of the investment, e.g. direct holding, units in a trust;
- the marketability of the investment;
- whether the asset trades on listed or private markets; and
- the size of the holding relative to normal or stressed market trading volumes.

A **liquid** asset is one that can be readily converted into cash at market value within a short period of time (ie. 90 days) with minimal impact on its realised value. Examples of such investments include money market securities, fixed income securities (with standard terms), listed equities and listed derivatives (e.g. futures).

An **illiquid** asset is an investment that cannot be converted to cash within, or reasonably close to, 90 days or where conversion to cash over that period, by itself, would have a significant adverse impact on its realisable value. Examples of such investments include private equity, infrastructure and unlisted property investments.

The Fund's definition of liquid and illiquid assets is outlined in Table 1 below.

Table 1 – Liquidity Classifications for the Fund

Liquidity Classification	Time to trade to Cash without Impacting Value
Liquid Assets	< 90 days
Illiquid Assets	>90 days

3 Liquidity Risk Appetite

Liquidity risk for the Fund is the risk that it is unable to meet its financial obligations to beneficiaries as they fall due, either at all or by selling investments at materially discounted prices, which can lead to inequity between unitholders[1].

The Trustee’s liquidity risk appetite is set at “low”, as outlined in its Risk Appetite Statement (**RAS**).

3.1 Rationale for Investing in Illiquid Assets

Both liquid and illiquid assets can be used to achieve the investment objectives for each investment option, however, for the use of illiquid assets consideration must be given to:

- the drivers of liquidity (see Section 4.1 below); and
- how the investment objectives will be achieved.

Generally speaking, FTC believes that additional returns can be achieved through exposure to illiquid assets over the long-term and that long-term investors have an advantage over other investors that may have a shorter investment time horizon. By investing in illiquid assets, the Fund can benefit from an illiquidity premium (the additional return that can be obtained by investing in an illiquid asset). In addition to the illiquidity premium, exposure to illiquid assets can provide the Fund with diversification benefits and a reduction in volatility, due to different exposures to risk factors and the appraisal-based valuations of unlisted assets. However, FTC recognises that the Fund needs a certain degree of liquidity in each option to meet the ongoing obligations to beneficiaries and other calls on liquidity (see Table 2 below), and ensure appropriate risk management and equity between transacting and non-transacting members.

[1] The actions of some investors in a panic mode withdrawing from an investment option in times of market stress may lead to more patient investors who remain in the investment option being adversely affected, for example, being left with a large unrealised capital gains tax liability or realising losses on an asset.

4 Liquidity Risk Management

The framework for managing liquidity risk considers the following key elements:

1. understanding the drivers behind liquidity needs;
2. understanding the sources of liquidity;
3. setting liquidity parameters;
4. implementing effective investment structures;
5. monitoring liquidity;
6. regularly conducting liquidity stress testing; and
7. maintaining a Liquidity Action Plan (LAP) for managing liquidity crisis events.

While the Fund has a LAP to guide its response to a liquidity event (see definition at Section 4.7.1), the preference is to avoid a liquidity event by identifying and responding to lead indicators that liquidity risk is building in the Fund before a crisis eventuates. The Fund has in place a liquidity monitoring system which is designed to identify such signs and allow the Fund to react before a liquidity crisis occurs. While it is not always possible to identify potential risks in advance, proactively avoiding risk is preferable to reacting after it materialises.

4.1 Understanding the Drivers behind Liquidity Needs

The *typical investment profile* of the Fund is as follows:

- *Accumulation Division*: Members of the Accumulation Division are typically young, pre-retirees and can bear greater investment risk than members of a superannuation fund where members are predominantly in the retirement phase of their lives. As accumulation members are generally investing for the longer term and will not have access to their investments until the pension phase, it follows that they can tolerate a higher illiquidity risk than retirees, who need access to a portion of their assets within a shorter time frame.
- *DB Division*: Members of the DB Division are predominantly pensioners, deferreds and contributors who are over 55 years old and eligible for retirement benefits. The employers bear the investment risk, and have an aversion to contribution rate increases. Accordingly, the investment strategy is conservative to lessen volatility of returns. As the DB Division continues to mature, the investment strategy will seek to have the asset cash flow match the liability cash flow as closely as possible. The DB Division is closed to new entrants and member numbers are projected to decline over the next 10 years. It therefore follows that members and their employers have a lower tolerance to illiquidity risk than pre-retiree members in a fund with positive net cash flows.
- *SP Division*: Clients are typically mature, in the retirement phase of their lives, and quite averse to investments risks. As retirees will typically need access to a portion of their assets within a shorter timescale than a typical member in the pre-retirement (accumulation) stage, it therefore follows that retirees will have lower tolerance to illiquidity risk than pre-retirees. Some retirees may value having immediate access to a large portion of their retirement savings.

With that investment profile in mind, the *demand for liquidity* can be categorised to arise from three main sources:

A. **Member-driven**

- Members in pension phase require cash for personal reasons, and withdraw funds from their investment option(s).
- Members in pension phase are paid regular pension payments and/or distributions from their investment option(s).
- Members in accumulation and/or pension phase switch between investment options, resulting in cash flow movements (ie. from equities to cash).
- Members in accumulation or pension phase switch to another super fund provider, withdrawing all or part of their investment from the Fund.

B. Asset/investment driven

- Rebalancing arrangements require liquidity to ensure the strategic or tactical asset allocation position of each investment option is maintained.
- Losses from hedging foreign currency positions or other derivative positions that require funding (i.e. margins).
- Drawdown of new or committed capital for investments requires funding.

C. Operationally driven

- Manager fees which require cash payment or an accrual in cash within each manager's account.
- Custody fees which require cash payment or an accrual in cash within each investment option.
- Trustee office costs, which require cash payment or an accrual within each investment option.
- Other operational costs, such as taxes and insurance premiums.

Liquidity risk will arise where the demand for cash cannot be readily met from the available cashflow.

4.2 Understanding the Sources of Liquidity

Each liquidity risk profile identified in Section 4.1 is classified by the Asset Consultant into those that are reasonably predictable (known) in their amount and timing and those that are much less predictable (unknown). Each potential call on liquidity and their source of liquidity in the short and long-term are documented in Table 2 below.

Table 2: Liquidity Requirements – Sources and Calls on Liquidity

KNOWN		UNKNOWN	
Calls on Liquidity	Source of Liquidity	Calls on Liquidity	Source of Liquidity
A. Member-driven			
Benefit payments	*Short term*: Ongoing contributions and cash holdings *Long term*: sell down all assets pro rata	**Member investment option switches/ redemptions**	*Short term*: Liquid assets *Long term*: All assets
B. Asset/Investment Driven			
Capital to fund proposed new investments	As required	**Currency hedging cash flows**	Cash, then liquid assets being hedged

KNOWN		UNKNOWN	
Calls on Liquidity	**Source of Liquidity**	**Calls on Liquidity**	**Source of Liquidity**
		Other derivative related cash flows (e.g. futures in the AAA program)	Cash
		Drawdown of committed capital	*Short term*: Liquid return-seeking assets *Long term*: All return-seeking assets
		Rebalancing due to significant short-term market movements	*Short term*: Liquid assets *Long term*: All assets
C. Operationally driven			
Expenses and tax	*Short term*: Ongoing contributions, income from investments and cash holdings *Long term*: sell down all assets pro rata		

As Table 2 illustrates, liquidity requirements cannot be predicted in advance; market movements could mean that there is a need to meet collateral requirements or rebalance the investment option. Therefore, it is necessary to hold sufficient liquid assets at all times in order to meet *potential* liquidity requirements that may arise. It is also important to ensure that the assets are sufficiently liquid to meet requirements not only in normal conditions but also following significant asset and liquidity shocks.

4.3 Setting Liquidity Parameters

The strategic asset allocation of each investment option is the main determinant of its overall risk and return characteristics, including its liquidity profile. Hence, FTC explicitly considers the liquidity characteristics of each asset class before setting the strategic asset allocations and ranges for the individual investment options offered to members. In setting the liquidity classification for each asset class, FTC tailors the liquidity classification to the characteristics of the underlying assets themselves, rather than applying a standardised approach.

It is expected that each investment option would be able to meet its cashflow requirements on a stand-alone basis. Hence, the proportion of illiquid assets held at an investment option level is a key parameter considered in relation to liquidity risk; an increasing proportion of illiquid assets will, by definition, reduce the overall level of liquidity. Overall, the following principles apply:

- a majority of assets are held in highly liquid securities, many exchange-traded, which can be fully liquidated at short notice if necessary;
- all investment options have a strategic allocation to cash, which is highly liquid, and could be drawn upon to manage cash flow requirements; and
- unlisted securities are regularly reviewed for valuation accuracy.

The maximum allocation to illiquid assets under normal market and stressed market conditions is set out in Table 3 below.

Notably, under stressed market conditions, the availability of liquidity tends to decrease, therefore, the maximum allocation to illiquid assets across each option may increase relative to normal market conditions.

Table 3 - Maximum Allocation to Illiquid Assets

Accumulation Division and DB Division Investment Option	SP Division Investment Option	Maximum Allocation to Illiquid Assets	
		Normal Market Conditions	Stressed Market Conditions
Pre-Mixed			
High Growth	-	30%	45%
Growth	Growth Plus	30%	40%
-	Growth	30%	40%
Balanced Growth	Balanced	25%	35%
-	Moderate	25%	35%
DB Division	-	25%	35%
Conservative Growth	Capital Stable	25%	35%
Diversified Socially Responsible Investment - Accumulation	-	30%	40%
Diversified Socially Responsible Investment - Pension	-	25%	35%
Single Sector			
Cash	Cash	5%	10%
Australian Equities	Australian Equities	5%	15%
International Equities	International Equities	5%	15%
Socially Responsible Australian Equities	-	5%	15%
Australian Fixed Interest	-	5%	15%
International Fixed Interest	-	5%	15%
-	Fixed Income[2]	10%	15%
Property	-	50%	65%

There may be good investment opportunities that arise during periods of market stress, including opportunities available in illiquid asset classes. Accordingly, the investment team may choose to add to illiquid assets at such times which may cause the allocation to temporarily be above the 'Normal Market' limit specified above. Where this happens, the 'Stressed Market' limit specified above would not generally be breached and the allocations would remain between the 'Normal Market' limit and the 'Stressed Market' limit. The reversion to normal

[2] Note that the StatePlus allocation to 'Fixed Interest' contains Australian and International Fixed Interest, and Conservative Income securities and so under normal market conditions has a higher maximum allocation to illiquid assets than the purely Australian Fixed Interest and International Fixed Interest sectors of FTC.

market conditions, and the 'Normal Market' allocation to illiquid assets, may take an extended period (i.e. 1-2 years).

4.4 Implementation of Effective Investment Structures

The Fund predominantly invests in separate mandates with the assets held by an external custodian. This provides improved liquidity over pooled unit trusts where the investor is bound by the redemption clauses of the pooled fund and might not be able to redeem straight away, even if the underlying assets themselves are tradeable. Where investments are held in pooled funds, the redemption period in the pooled fund's constitution is aligned to our liquidity definition.

4.5 Monitoring Liquidity

The Fund has a number of processes in place to ensure sufficient ongoing liquidity monitoring at the investment option level, including:

- on a daily basis, investment markets are monitored by the Liquidity, Fixed Income & Markets team - this includes, but is not limited to: average traded volumes, market volatility, broker market activity, exchange access, open interest and dark pools (where necessary);
- on a monthly basis, net cash flows are reviewed for each investment option by the Liquidity, Fixed Income & Markets team to monitor and identify liquidity trends and member behaviour (ie. switching out of the Growth option into Conservative Growth option). This is also reported to the MIC and IC;
- on a monthly basis, the Custodian and Investment Risk & Compliance team review each investment option's liquidity profile against the set parameters outlined in Table 3 (maximum allocation to illiquid assets). These are also reported to the MIC, IC and FTC Board. Any breaches are reported to the Head of Liquidity, Fixed Income & Markets and appropriate action taken;
- cash flow projections are reviewed by the LFIM team for regular pension or income payments to ensure sufficient liquidity to cover such obligations;
- on a semi-annual basis, liquidity stress testing is conducted by the Asset Consultant for each investment option and the results reported to the IC;
- on a semi-annual basis, the Valuation Committee (**VC**) meets and reviews the valuation practices and results of the Fund's investments, with a particular focus on unlisted asset valuations;

on an annual basis, as part of the business planning cycle, the FTC Executive Team forecast the inflows and outflows for the following year. Actuals are monitored against the projections in the business plan by the FTC Board each quarter.

The Investment team monitors a set of early warning indicators to identify the emergence of increased liquidity risk as summarised in the table below.

Table 4: Early Warning Indicators and Thresholds

Activity	Frequency	Early Warning Indicators	Threshold	Monitored by/ Reported to
Major market and currency monitoring	Daily	Significant drop in major markets/change in value over a 24-hour period	• a 5% drop in markets generally in a 24-hour period; and/or • a 7% change in the value of the	Liquidity, Fixed Income & Markets team, and reported to the MIC

			Australian dollar versus the Euro, US dollar, Japanese yen or Great British pound in a 24-hour period	
Cash Flow Monitoring	Monthly	Net Quarterly Cashflow	Only applicable to investment options with illiquid assets: Net quarterly cash outflow no greater than 5% of average investment option size	Liquidity, Fixed Income & Markets team and reported to the MIC and IC via the Investment Management Balanced Scorecard
Liquidity Profile Monitoring	Monthly	Maximum allocation to Illiquid assets	'Normal Market' maximums breached as outlined in Table 3	Custodian and Investment Risk & Compliance team, and reported to the Liquidity, Fixed Income & Markets team and the MIC, IC and Board via the Investment Management Balanced Scorecard
Liquidity Stress Testing	Bi-annual	Growth/defensive assets outside permissible ranges following a number of simulated stress events	Retain growth/defensive assets within permissible ranges	Investment Strategy team, and reported to the MIC and IC

4.6 Liquidity Stress Testing

Stress testing is a forward-looking assessment of risk factors affecting the Fund and it enables the Trustee to identify and assess potential risk exposures that may threaten the likelihood of achieving an investment option's investment objectives.

4.6.1 Methodology

The aim of stress testing liquidity is to ensure the Fund holds sufficient liquid assets to meet a range of liquidity requirements that could arise at any time, as outlined in Section 4.1. The analysis assesses the impact of stresses arising from extreme asset class returns, foreign exchange market movements, and significant member option switching (such as those experienced during the GFC) on the Fund's allocations to illiquid assets.

As part of the liquidity analysis, the proportion of the Fund's investment options which would be liquid over different time horizons are reviewed both under a normal and a stressed scenario.

In the stressed scenario, market returns for liquid asset classes are set in line with a scenario that envisages a significant fall in asset prices with flow on impacts to consumer spending, company revenue and business investment thus leading to reinforcing declines in aggregate demand. The returns adopted for each asset class are in line with the assumed (peak to trough) drawdown that could possibly occur. The analysis occurs over a 3-month timeframe. Liquidity is then analysed against a second scenario that exacerbates the negative effects of each stress.

In addition, when large changes are proposed that impact liquidity (for example, altering the illiquidity limits of the investment options) then further tailored analysis is performed.

The asset class liquidity assumptions used in the stress testing process are reviewed by the Investment Strategy team prior to conducting a stress test.

4.6.2 Frequency

Stress testing of each investment option is undertaken on at least a bi-annual basis. Stress testing may also be undertaken where deemed necessary outside of these periods, and in particular:

1. where a potential investment is greater than or equal to 1% of the Fund and cannot be liquidated within 90 days; or
2. if an investment that cannot be liquidated in full within 90 days falls outside the investment strategy parameters under the relevant Sector Guideline.

4.6.3 Review and Reporting

The results of the stress testing will be reviewed by the Investment Strategy team and Head of Investment Risk and presented to the IC. If the results have moved adversely compared to the prior stress testing analysis, then this will be escalated by the Investment Strategy team and/or Head of Investment Risk to the CIO. This applies to both bi-annual stress testing and out-of-cycle stress testing. The CIO will decide what appropriate action to take:

- **no action,** for example, in the case where there are no breaches of the investment option limits; or
- **action,** for example, if the stress testing analysis indicated that the investment strategy of the pre-mixed options was inconsistent with the risk tolerance of FTC, and an immediate review of the strategic asset allocation for the investment options was required. In any instance where action is deemed appropriate, the results of any further analysis, together with the initial findings, would be tabled at the IC. If the issue is deemed a temporary aberration, then no further action may be taken; alternatively, the issue may require input or approval by the IC.

4.7 Maintaining a Liquidity Action Plan (LAP)

The LAP establishes the guidelines for monitoring and managing liquidity risk under adverse liquidity conditions (e.g. a liquidity event).

4.7.1 Liquidity Event

A liquidity event is defined as an event where there is an unprecedented requirement for liquidity or an event that affects the liquidity profile of the Fund. Such events could consist of, but are not limited to, the following:

- **Spike in investment option redemptions**: where a very high number of redemption requests are lodged by members.
- **Switching**: where a very high proportion of members switch from a pre-mixed investment option to a purely liquid investment option, like the Cash investment option.

- **Market event**: an event, such as a collapse in the listed equity markets, which causes the proportion of illiquid assets to increase beyond the anticipated normal maximum allowance.
- **Investment manager-driven event**: such as a fund manager suspending redemptions from an investment vehicle.

Such events are considered to have a low probability.

4.7.2 Delegation for Management of a Liquidity Event

The Trustee has delegated the creation of a LAP to the CIO, who acts as the initial escalation point and determines the appropriate course of action if there is a liquidity event. The Head of Investment Risk is responsible for the oversight of the LAP.

4.7.3 Course of Action

The strategy for managing a liquidity event cannot be overly prescriptive as the appropriate course of action will be dependent upon the circumstances that prevail at the time. Accordingly, the Trustee may tailor the liquidity management strategies to ensure they are appropriate in light of prevailing circumstances.

Three liquidity zones have been identified – “green”, “amber” and “red”.

4.7.3.1 “Green”: Illiquid assets < normal market limits

No action required.

4.7.3.2 “Amber”: illiquid assets > normal market limits but less than stressed market limits

The breach of ‘Normal Market’ limits will be a signal for the CIO and Head of Investment Risk to maintain a watching brief on the liquidity position of an investment option. A watching brief may comprise:

1. Understanding the cause of the breach, noting that this may be temporary (i.e. significant market decline results in a passive asset allocation change, but given the volatile nature of markets there is greater potential for the situation to reverse) or more permanent (i.e. a long running pattern of poor investment returns undermines the Fund’s competitive position resulting in steady exits by members). A temporary shock may enable the Fund to increase its illiquid assets at attractive prices whereas this course of action would not be considered if the cause was a more permanent one.
2. Assessing the timeframe in which the investment option is forecast to return to the ‘Normal Market’ maximum allocation to illiquid assets under the most likely case, and the speed of this recovery.
3. More frequent monitoring of the early warning indicators set out in Table 4.

The investment options that have breached the ‘Normal Market’ maximum allocation to illiquid assets will be discussed at the next IC meeting and communicated via the monthly Investment Management Balanced Scorecard.

4.7.3.3 “Red”: illiquid assets > stressed market limits

At this point the Trustee will consider the both the context of the deviation and the appropriate mitigation and management strategies as documented in Table 5 below. Table 5 considers high level responses that are likely to be relevant in most situations when a liquidity event occurs.

Table 5: “Red” Liquidity Event Process

<table>
<tr><th>Sequence of Events</th><th>Action</th></tr>
<tr><td>1</td><td><u>Identification of a potential liquidity event</u>

If the investment option breaches the ‘Stressed Market’ maximum allocation to illiquid assets (outlined in Table 3), the LAP will be activated.

The threshold for de-activating the LAP is where the allocation to illiquid assets falls back into the ‘Normal Market’ range.</td></tr>
<tr><td>2</td><td><u>Evaluation of a potential liquidity event</u>

Before communicating that a liquidity event has been identified, the Investment Strategy team will consider the following matters:
what assets have become impaired or the liquidity characteristics that have changed, and which investment options are impacted;
the investment option’s current position with respect to the ‘Normal Market’ and ‘Stressed Market’ illiquid asset allocation limits;
the timeframe in which the investment option is forecast to return to the ‘Normal Market’ maximum allocation to illiquid assets under the most likely case, and the speed of this recovery;
forecasts for strategic asset allocation under a range of scenarios for intervals over the next 2 years, which encapsulate estimates of the calls on liquidity outlined in Table 2; and
any relevant qualitative considerations, including the causes of the liquidity event, the likelihood of these dissipating or easing within the short or medium term, and the extent to which these causes can be directly managed, addressed or controlled.
These considerations will be relevant to selecting the appropriate contingency measures to employ and setting the requisite timeframes and delivery goals, which will form the specific LAP to address the liquidity event.</td></tr>
<tr><td>3</td><td><u>Communication of a liquidity event and escalation protocols</u>

Responsibility for initialising internal communication of a liquidity event lies with the CIO, who in turn relies on the following escalation protocols:
any events pertaining to liquidity which are identified by the investment or fund services teams must be brought to the prompt attention of the CIO;
the CIO will inform the MIC, the CEO, the IC and the Chair of the relevant Board;
the liquidity event will be logged on the Incident Management System;
APRA will be notified as soon as the ‘Stressed Market’ maximum allocation to illiquid assets has been triggered and the event logged on the Incident Management System;
the investment options that have breached the ‘Stressed Market’ maximum allocation to illiquid assets will be discussed at the next IC meeting (and are automatically communicated via the monthly Investment Management Balanced Scorecard);
if the investment options breach the ‘Stressed Market’ maximum allocation to illiquid assets by more than 20%, then the CEO, IC and the Chair of the Board are to be notified immediately and an out-of-schedule IC meeting canvassed; and
the CIO has discretion regarding whether such events warrant broader communication throughout the Fund (subject to discussion with the Chair of the Board and/or the Chair of the Investment Committee).</td></tr>
</table>

Sequence of Events	Action
4	<u>Engagement with the Enterprise Delivery and Transformation (EDT) Team and creation of a Crisis Management Team</u> The CIO will engage with the EDT team to establish a crisis management team from across the broader business. The crisis management team will manage processes initiated following communication and escalation of the events and issues. The crisis management team will be established by the EDT team, in consultation with the CIO, and will be drawn from the following areas: • EDT team; • Investments; • Risk; • Legal; • Fund Services; • Marketing; and • Fund Administration. The input of external advisers/service providers to provide advice and/or assistance to the crisis management team, may also be sought.

5	<u>Consideration of contingency measures</u>
	The crisis management team will consider potential mitigation and management measures for the liquidity event including:
	• reviewing investments in illiquid assets and identifying potential assets for sale:
	  ○ this process would be focused on identifying assets that could be both sold quickly and not affect the composition of the remaining portfolio in a significant manner
	  ○ current market value considerations would also be relevant;
	• reviewing the capacity to suspend or cancel forward commitments;
	• consideration of the use of available liquidity in the Fund's reserves;
	• increasing the valuation frequency of illiquid assets to ensure decisions are taken based on up-to-date valuation outcomes:
	  ○ this is relevant in assessing (i) the magnitude of the liquidity issues and (ii) potential exit options, particularly if there are a large number of identified potential exits;
	• engaging with APRA as to the current liquidity position and any material developments;
	• deferment or suspension by the relevant Trustee of member investment choice switching; and
	• delaying the processing of transfer requests:
	  ○ SIS Reg 6.36(1) allows funds to apply to APRA for a longer-term suspension of their obligations to process transfers. APRA has the discretion to suspend a Fund's obligation to process transfers if it believes that the transfers would have a

Sequence of Events	Action
	significant adverse effect on (i) the financial position for the Fund or (ii) the interests of other members of the Fund[3].
6	Creation and communication of the LAP The CIO or his delegate, acting upon the advice of the crisis management team, will document the necessary steps which will reduce the liquidity risk or restore liquidity for the investment option(s) to within the relevant limits after consideration of the matters set out at points 2 and 5 above. The LAP is an active plan of management and mitigation, to be implemented according to a real time timetable and monitored against identifiable outcomes. The LAP should include: • actions; • people responsible for the delivery of those actions, including the role and responsibilities of any external advisers, and their delegations; • timeframes and key milestones for delivery; • IC and Board reporting deadlines; and • any important assessment criteria to determine the success (or otherwise) of the LAP implementation. The LAP should be agreed with the CEO prior to implementation. Key communication requirements and responsibilities will be identified as part of the LAP. Broadly speaking, the CIO, and any of the crisis management team with delegated responsibility, will be responsible for ensuring communication of the LAP to: • the CEO and Executives, and how it affects individual teams and workstreams; • the Fund's advisers as appropriate; • Fund members as necessary (i.e. regarding application for APRA relief or changes to redemption policies); and • APRA, including the current liquidity position, the intended courses of action and, in more severe cases, any relief which may be sought.
7	Implementation of the LAP The LAP will be delivered according to the timetable by the people identified as responsible for each action. Delivery of action items will be assessed by the CIO in accordance with the criteria and milestones identified in the LAP.
8	Monitoring of the LAP Monitoring of the LAP will be as per the reporting schedule and responsibility matrix identified therein and will be to the CIO, Head of Investment Risk and IC at a minimum.

[3] Factors to be considered in whether to make an application to APRA to suspend the processing of transfers would include the rate of redemption requests, the rate of contribution inflows, the asset allocation at the time of the request, the impact on the asset allocation from movements in listed markets, the cause of the redemption request, the market environment for realising illiquid assets, any planned realisation of illiquid assets in the normal course of events and whether a member is switching to another investment option which also contains illiquid investments.

Schedule A: Roles and Responsibilities

Role	Responsibility
Investment Committee will:	• Review and approve this Policy. • Review the results of the liquidity analysis and stress testing of each investment option.
Management Investment Committee (MIC) will:	• Monitor early warning thresholds assigned to them, as set out in Table 4.
Chief Investment Officer will:	• Act as the key decision-maker and initial escalation point if: (i) the results of the liquidity analysis and/or stress testing have moved adversely as compared to the prior review period; or (ii) there is a liquidity event; and determine an appropriate course of action.
Investment Strategy team and Head of Investment Risk will:	• Recommend material changes to this Policy to the Governance & Due Diligence team. • Review, challenge and validate the liquidity and stress testing methodology, asset class assumptions, modelling and reports produced by the Asset Consultant to ensure they remain relevant and appropriate. • Act as the primary point of contact and liaise with the Asset Consultant. • The Head of Investment Risk will manage a liquidity event as set out in Table 5.
Asset Consultant will:	• Perform liquidity and stress testing of the Fund's investment options semi-annually and on an ad hoc basis as required by FTC.
Portfolio Managers and Investment Analysts will:	• Consider the liquidity of each investment as part of the due diligence process.
Liquidity, Fixed Income & Markets team will:	• Monitor early warning thresholds assigned to them, as set out in Table 4. • Alert the MIC and Head of Investment Risk if an early warning indicator threshold is breached.