# ASIC TO REVIEW FUND MANAGERS' RISK FRAMEWORK

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On 13 February 2015, ASIC announced that it had embarked on a campaign to review responsible entities' (REs) risk management processes, particularly focused on the impacts of heightened local and global market volatility. The Regulator's interest centres on how REs are managing liquidity and market volatility risks (ASIC 15-020MR).

In the week before ASIC's announcement, around 120 REs were asked how they are ensuring that events such as significant asset revaluations, reduction in cash inflows (ie applications) and changes in asset-liquidity profiles are being managed.

The announcement followed some guidance issued by ASIC in 2013 entitled Consultation Paper 204 Risk management systems of responsible entities (CP 204) and is possibly an outcome of ASIC's recently formed Emerging Risk Committee.

In, CP204 ASIC made strong suggestions that REs should have systems in place to stress test a fund's operation in the event that fund inflows dry up, redemptions increase and assets cease performing.

Avoiding a repeat of the $5b freeze in the mortgage fund industry would be in the front of ASIC's mind. During the GFC a number of mortgage funds that had enjoyed healthy cash inflows suddenly had to freeze redemptions. A build up in redemption demand followed as investors "fled to quality" because, amongst other things, investors could access risk free income via the Commonwealth Government's bank guarantee.

This "flight to quality" left a number of REs exposed. Asset valuations plummeted, insolvencies occurred and some funds are still dealing with residual problems associated with property developments, "land banks" and mortgagee in possession processes. Many retail investors who had believed their savings were readily accessible, found that they were not.

ASIC's campaign is focusing beyond mortgage funds, and includes fixed income securities. It is important for fund managers to have confidence that the RE for their fund(s) will be able to demonstrate internal processes are in place to ensure it knows whether (and to what extent) a fund can continue to operate under various assumptions, including reduced application inflows, increased redemption demands and sudden shifts in asset prices.

The industry will wait for the results, but in this case, ASIC has the benefit of hindsight.