Imperial College Union
Board of Trustees / 16th September 2020

Rathbones Investment Portfolio

Author(s): Tom Flynn (Managing Director)
Jayne Hufford (Head of Finance)
Abhijay Sood (President)
Sam Lee (Deputy President

Purpose: To briefly outline the rationale behind the proposed liquidation of our investment portfolio, in light of the 2019/20 financial performance and other historical issues.

Decision(s): To approve the full liquidation of the investment portfolio currently held by Rathbones Asset Management.

1. Financial Outturn 2019/2020 & Balance Sheet

It is clear that the 2019/20 financial year has been extremely challenging for the Union, driven by a combination of four I&E factors, and one major balance sheet adjustment issue. The end of year audit is currently taking place, but the draft final accounts produced by the team have generated initial figures:

i. A deficit on unrestricted reserves of £736k. It should be noted that this includes a favourable movement on the pension deficit reserve of £126k, and the fact that the College have agreed to purchase all obsolete branded stock from us (at a value of c£120k).
ii. Free reserves of £438k, a significant reduction of £459k year on year. This does make ICU a going concern, but it also demonstrates the importance of the transformational changes underway. These free reserves will need to cover redundancy costs of up to £200k as they were not budgeted in 2020/21.
iii. Non CSP cash/investment reserves of £497k.

2. Balance Sheet & Reserves Position (August 2020)

Over the past month the new Managing Director and outsourced Head of Finance have been conducting a review of the organisation's balance sheet and historical financial performance. The current policy set by the Board of Trustees (which needs updating this year) requires the organisation to hold sufficient free reserves in order to 'balance volatile income', 'fund limited capital expenditure' and 'embrace new opportunities for service development'. On 31 July 2019 this was calculated at £1.2m. In reality, the stated level of free reserves as per the annual report was c£900k.

In addition to this, there has been a (mis)understanding that the Union *also* holds c£1.5m of assets in an investment portfolio managed by Rathbones Investment Management. The decision to invest this sum of money was made by the Trustees at the end of the 2017/18 academic year, after finishing with a cash position well beyond expectations. This situation was replicated in the 2018/19 annual accounts. The portfolio has been managed well, and there has been a good level of return on the investment, as well as an increase in value of the principal sum.

Over the course of the 2019/20 academic year, the Union therefore had intended to cover most of the in-year deficit caused by COVID-19 and draw down on the investment portfolio to protect its free reserves. However, it is now clear that the financial position of the Union has been artificially inflated over the past two years due to a timing difference in the invoice sent by the College for staffing costs. In effect, the inflated cash position at the end of 2017/18 was driven by the College only invoicing for c6 months of salary costs within the financial year. The situation was replicated in 2018/19, where it again appears that only half a year was invoiced and paid.

However, in the 2019/20 financial year the College has been more up to date with its invoicing, and the Union has settled all historical debt in year (rather than finishing the year with over £1m in our creditors).

With c£450k in our free reserves, the £1.5m investment in the Rathbones portfolio is currently therefore made up of:

i. c£250k of our free cash reserves (the remaining c£200k is in physical shop and venues stock).
ii. c£1.25m of cash that does not technically 'belong' to the Union. Given that the fact we have paid down our large debtors, this means the Union is currently operating using restricted cash reserves – or to put it another way, money that 'belongs' to CSPs.

The Union must therefore liquidate its investment portfolio in the short term to simply to get back to a break-even position.

3. Next Steps

We have met with our portfolio managers at Rathbones, who advised us that many of their clients were now taking similar steps – with organisations across the globe required to draw down on reserves to mitigate the impact of COVID-19. This guidance is summarised in Appendix One.

We will bring an up to date valuation figure for the Board meeting (to ensure it is accurate).

Any decision to liquidate the portfolio will require authorisation from Graham Parker and Tom Flynn, as per the guidance below.

Appendix One: Advice via Email Correspondence

Date received: 06 August 2020

Further to our call yesterday I outline below options for the Union should you need to raise cash to shore up your cash reserves position. I am very happy to attend a meeting should you need me to.

We have reviewed the options for raising various levels of cash from the investment portfolio taking into account the potential but possibly uncertain short-term liquidity need. As a reminder, the portfolio is currently managed to a long term strategy on a multi-asset basis. As at last night's close the portfolio value was £1,556,781. The asset allocation was circa 17.5% fixed income investments, 65.9% to UK and Globally listed equities and 9.6% to infrastructure and commercial property and 7% cash having taken some profit yesterday following our conversation, (£109,696 on deposit). We classify this asset allocation as 4 on our 1-6 scale with 6 being the highest risk. It is worth noting that you are charity so the Union does not have to be concerned about tax obligations arising from crystallising imbedded gains within the portfolio, upon liquidating assets, which is quite advantageous.

We highlight four scenarios:

- Raising £500k - As a start we suggest raising a further £400k from across the portfolio to ensure that we maintain a well balanced portfolio with the remaining assets, in keeping with the current long term objectives and risk characteristics. The long term performance measure of CPI+3% can be retained which aligns with the objective to maintain the 'real' spending power of the assets over the long term.

- This will also mean that the income flow will continue (albeit) reduced in keeping with the reduced portfolio. We estimate that the annual income from a portfolio of circa £1m invested could be £23,000. The Union currently draws £7,500 each quarter. Should the Union wish to continue to draw at that level, approximately a quarter of the drawing will come from capital. Consideration should be given as to whether the quarterly drawdown should reduce to £5,750 for example which would come from investment income generated or confirmation that capital may also be used for the quarterly drawing.

- Raising £900k – Once again we would raise from across the entire portfolio to ensure we maintain a well balance portfolio. Income will be significantly lower as a result so we would strongly advise reducing the quarterly drawing accordingly. Income is likely to be circa £15k per annum. Please also note that at this time the Property funds are closed for redemptions so we cannot reduce those holdings till they reopen. This anticipated to be September/October however it has not been confirmed.

- Should the Union require more than £900k but retain some assets, then we may collectivise all of the remaining investments to reduce stock specific risk within the reduced s portfolio. All collectives will be assessed for suitability in accordance with the union's investment policy.

- Liquidating the entire portfolio – The portfolio is highly liquid so we would be able to provide funds within 10 business days following instruction. Once again, please note that we cannot trade the Property funds at this time so these trades would be carried out as soon as possible.

Next steps – during our discussions, it was mentioned that should the Union obtain support from the University and not require liquidation at this time, there is the possibility of requiring funds in circa 6 months' time to fund restructuring. This adds further the uncertainty of your liquidity requirements. Therefore we believe the best course of action would be to raise £500k as soon as possible and if needs be we can increase that amount. If markets took a large tumble – 1/3% of the portfolio would be in cash – thus giving you some protection. We cannot know how the market will perform in the next few months, but there is a lot going at the moment that could derail the strong recovery we have had since March. Previously you were quite able to sit through any short term drawdowns or volatility, however at this stage the Union is possibly less able to, with the uncertainty over support from the University. Being 'out of the market' for a few months could see you miss out on some upside, but looked at over the long term, this is likely be reasonably immaterial.

Instruction to raise and send out the requisite cash would need to come from two signatories to the account from email addresses know to us. We will then phone each signatory to confirm. If you have any questions on this process please liaise with Kirsten.