



Quoted Companies Alliance

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Monday 23 February 2026

Dear FCA colleagues,

**CP25/38: Enhancing fund liquidity risk management**

The Quoted Companies Alliance (QCA) welcomes the opportunity to respond to CP25/38: *Enhancing fund liquidity risk management*. The QCA represents the interests of the UK's small and mid-sized quoted companies, and the advisers and investors that support them.

We recognise the importance of effective liquidity risk management in protecting investors and maintaining orderly markets. We also acknowledge the Financial Conduct Authority's view that the existing framework for authorised funds is broadly robust and that the proposals in CP25/38 are intended to reinforce good practice rather than introduce fundamental change.

However, the QCA is concerned that aspects of the proposals risk reinforcing behavioural outcomes that further reduce institutional investment in UK small and mid-cap quoted companies. This would be detrimental to market liquidity, capital formation and the long-term health of the UK's public equity markets. It would also sit uneasily alongside the FCA's secondary objective to support the international competitiveness of the UK economy and its medium- to long-term growth.

In our view, the consultation does not sufficiently reflect recent market experience or the proportionality of risk. We would point, for example, to the thorough stress testing of UK small-cap funds in recent years and the fact that client redemption requests have been met in full. A more differentiated approach to liquidity risk in smaller company funds would better reflect actual outcomes and avoid discouraging appropriate long-term investment.

We also note that the tone and direction of this consultation appear somewhat out of step with other recent FCA initiatives designed to support growth, capital formation and innovation in UK markets. These include the FCA's five-year strategy commitment to make it easier for businesses to seek capital and increase liquidity; the establishment of the Scale-up Unit; the development of PISCES; and broader work to enable targeted support and innovation across asset classes.

Taken together, these initiatives reflect a welcome commitment to enabling investment and informed risk-taking in support of thriving UK capital markets. It is important that the approach to fund liquidity risk management is calibrated in a way that does not inadvertently constrain investment in the very segment of the market, small and mid-cap quoted companies, that plays a vital role in domestic growth and productivity.

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The QCA Markets Expert Group, Investor Working Group and Legal Expert Group have examined the proposals and advised on this response from the viewpoint of small and mid-sized quoted companies. A list of Expert Group members can be found in Appendix A.

We have responded to the consultation questions thematically, grouping questions where appropriate. We have not responded to every consultation question individually.

If you would like to discuss our response in more detail, please do not hesitate to contact us.

Yours sincerely,

A handwritten signature in blue ink that reads "James Ashton".

James Ashton  
Chief Executive

## 1. General Comments

- 1.1. The QCA is concerned that, while CP25/38 is framed as a clarification and strengthening of existing practice, the proposals may have the practical effect of discouraging investment in small and mid-cap quoted companies through behavioural change rather than explicit restriction.
- 1.2. In particular, enhanced expectations around liquidity assessment, stress testing, governance and documentation risk encouraging authorised fund managers to manage regulatory and supervisory risk through asset allocation decisions. In practice, this may disproportionately affect smaller quoted companies, regardless of underlying fundamentals.
- 1.3. The QCA also considers that the consultation does not adequately reflect recent market experience or the proportionality of risk in the small and mid-cap segment, nor does it sufficiently engage with the FCA's wider statutory objectives, including its secondary objective to support growth and productivity.

## 2. Questions 1–4: Liquidity risk management frameworks, stress testing and proportionality

- 2.1. While CP25/38 does not explicitly prohibit investment in less liquid assets, it materially strengthens expectations around liquidity assessment, stress testing, governance and documentation. These expectations will inevitably influence behaviour beyond the letter of the rules, particularly in areas where judgements are required and supervisory challenge is anticipated.
- 2.2. In the context of UK equity markets, this effect is most likely to be felt in small and mid-cap quoted companies. These equities are structurally less liquid than large-cap stocks when assessed using conventional metrics, yet they form an established and important part of diversified portfolios. The QCA is concerned that the consultation risks overstating the liquidity risk associated with listed small-cap exposure by relying on assessment approaches that do not reflect how liquidity operates in practice in these markets.
- 2.3. Recent market experience is highly relevant in this regard. Over the past five years, UK equity funds have experienced a sustained increase in redemptions from open-ended investment companies, with a disproportionate share of those redemptions falling on UK-listed equities. This has created a prolonged, real-world test of liquidity rather than a hypothetical stress scenario.
- 2.4. In larger and mid-cap stocks, redemption pressure has increasingly been mitigated by corporate share buyback programmes, which have helped absorb selling pressure and support market liquidity for exiting shareholders. Small-cap quoted companies, by contrast, have generally been less able to pursue buybacks, as capital is more often allocated to investment for future growth, innovation and balance sheet resilience.
- 2.5. Despite this asymmetry, the small-cap segment has continued to function through an extended period of elevated redemptions without evidence of systemic liquidity failure, disorderly markets or widespread investor harm. In the QCA's view, this experience calls into question whether further

tightening of liquidity expectations for listed small-cap exposure is proportionate to the risks observed in practice.

### 3. **Questions 5–7: Dealing frequency, fund structures and behavioural responses**

- 3.1. The QCA welcomes the FCA's acknowledgement that daily dealing should not automatically be assumed to be appropriate. However, the consultation does not address fund distribution models or provide meaningful incentives for alternative structures to emerge.
- 3.2. As a result, there is a material risk that authorised fund managers respond to heightened liquidity expectations by adjusting asset allocation rather than reconsidering fund structures or dealing terms. In practice, this risks making small and mid-cap equities the adjustment mechanism for managing regulatory and supervisory risk.
- 3.3. This dynamic is likely to be reinforced by internal governance processes within asset managers, including risk committees and compliance functions, which naturally respond to increased regulatory scrutiny by favouring simplicity and perceived safety. Assets that require more explanation or judgement — including smaller quoted companies — may therefore be disproportionately affected, even where they remain appropriate for long-term investment strategies.
- 3.4. The QCA is concerned that this outcome would further entrench an existing bias towards larger and more liquid companies, and away from the role of public markets in supporting growth companies, productivity and job creation.

### 4. **Questions 11–13: Anti-dilution tools and market effects**

- 4.1. While the QCA recognises the role of anti-dilution tools in protecting investors, there is concern that more frequent or more pronounced use of such tools may have unintended consequences for funds with exposure to small and mid-cap equities.
- 4.2. In particular, increased use of swing pricing may make such funds less attractive to investors, reducing inflows and weakening secondary market liquidity in the underlying shares. This could exacerbate existing liquidity challenges rather than mitigating them.
- 4.3. The QCA encourages the FCA to consider carefully how these tools are likely to be applied in practice, and whether additional guidance is needed to ensure they do not discourage appropriate investment in listed growth companies.

### 5. **Additional comments**

- 5.1. The QCA also has concerns about the framing of the consultation and the examples used. In particular, the Woodford Equity Income Fund involved significant exposure to unquoted assets and was highly fund-specific. It does not provide a representative basis for assessing liquidity risk in listed

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small-cap equities, particularly given that the most significant challenges in UK public markets have arisen since 2021 rather than around that specific case.

- 5.2. More broadly, the timing of the consultation raises questions. UK small and mid-cap markets have experienced sustained capital outflows, fund consolidation and declining liquidity in recent years. In this context, a regulatory focus on further reducing risk in fund liquidity management risks exacerbating existing pressures, rather than supporting market recovery. Small and mid-cap equities also play an important role in portfolio diversification, which should be recognised alongside liquidity considerations.

### **Appendix A**

The Quoted Companies Alliance Markets Expert Group can be found here: <https://www.theqca.com/markets-expert-group/>

The Quoted Companies Alliance Legal Expert Group can be found here: <https://www.theqca.com/legal-expert-group/>