ATTACHMENT 1

Equity Implementation Rationale

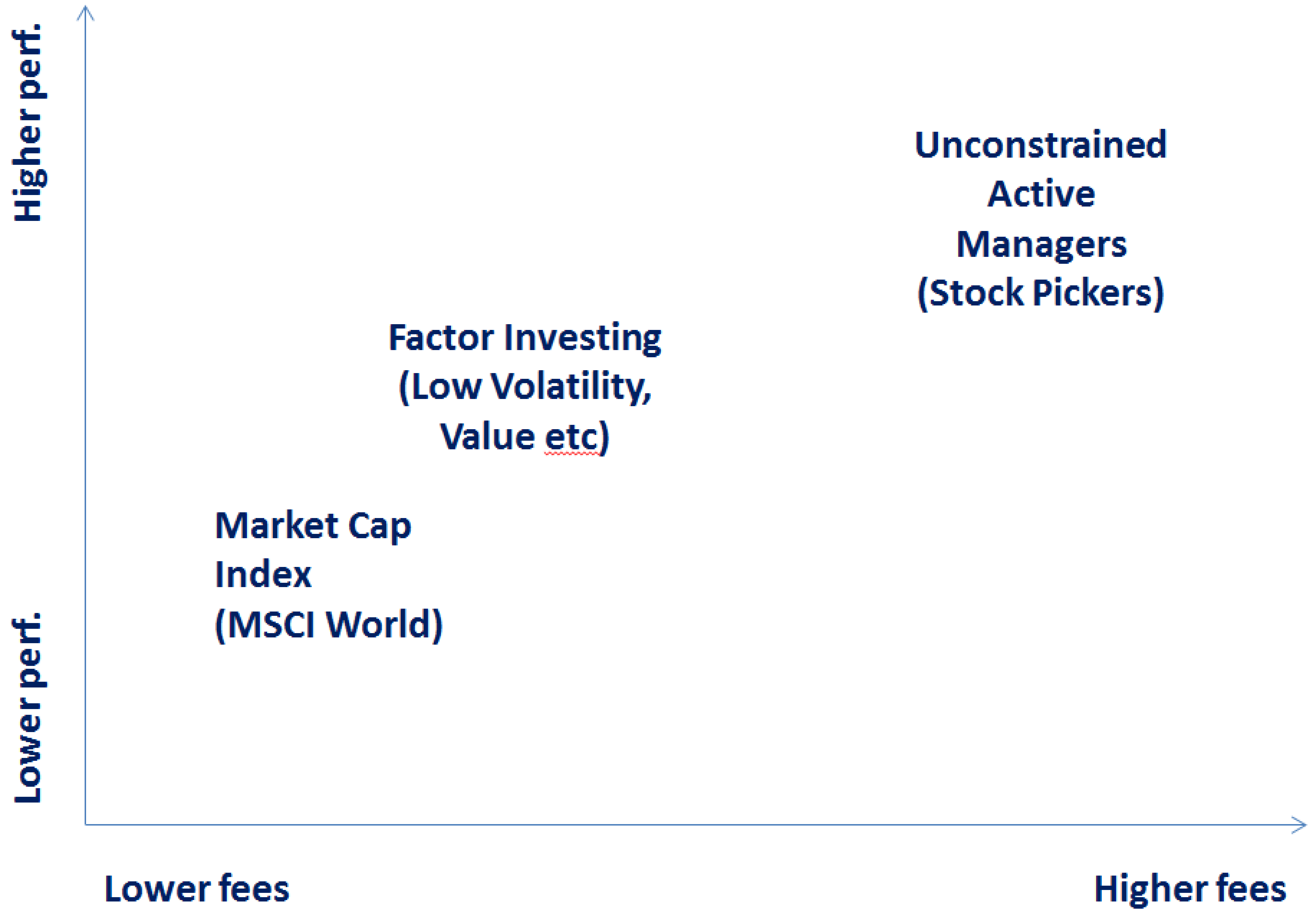
City of Toronto (Investment Board)

2024

Equity Portfolio Options

What is most important to the Plan?

- Governance budget, alpha, fees?



Equity Portfolio Options

Conviction In Equity Investing

- Aon believes using broad mandates and high conviction portfolios provides the best opportunity to add value from active management

- This pertains both to the type of managers, global high conviction managers and the number of managers in client portfolios

- Higher conviction managers generally have higher tracking error but not necessarily higher risk
    - Portfolio construction has an impact on overall portfolio risk characteristics

- To this end, we recommend the inclusion of broader mandates and more streamlined portfolios

Equity Portfolio Options

The Right Number of Managers

- Investors often overestimate the diversification benefits of increasing the number of active investment managers. We believe improvements can be made to many multi-manager equity portfolios
- Country/regional/style boxes may contribute to over-diversification
- Global equity strategies are the most efficient portfolio building block to construct a sensibly diversified portfolio
- Factor investing may be preferable to having too many active managers
- Investors of a sufficient size may reduce fees by reducing the number of managers
- Investing in fewer managers can facilitate directing more assets to managers where the prospects for outperformance are greatest

Equity Portfolio Options

Reasons one should consider an allocation to Factor Investing

- Outperformance potential and diversification benefits vs. a market cap passive index

- Better downside performance vs. market cap passive (beta of ~0.9)
  - Greater exposure to low volatility and quality factors and less to momentum

- Lower the cost of your overall equity portfolio
  - Passive multi factor allocations ~10-12 bps

- Diversification of added value sources for a portfolio invested in unconstrained equity managers

- Expect diversified multi-factor to outperform by 75 bps gross of fees vs. market cap passive index
  - Has traditionally been higher than 75 bps

Equity Portfolio Options

Potential Model Portfolios

Portfolio 1: Full Active

Active

- Global Equity 1
- Global Equity 2
- Global Equity 3
- Global Equity 4
- Global Equity 5

Portfolio 2: Active w/ Passive Diversified Multi-Factor

Active/Factor

- Global M-Factor
- Global Equity 1
- Global Equity 2
- Global Equity 3
- Global Equity 4

Portfolio 3: Passive Diversified Multi-Factor w/ Active

Active/Factor

- Global M-Factor
- Global Equity 1
- Global Equity 2
- Global Equity 3

Fees	60-70 bps	50-60bps	30-40bps
Alpha	~200bps	~175bps	~125bps

Equity Portfolio Options

Potential Options

1: Portfolio of 4-5 unconstrained global equity managers

- Higher fees, higher alpha potential, requires greater governance budget

2: Portfolio of unconstrained global equity managers and passive diversified multi-factor

- Slightly lower governance, slightly lower alpha potential, lower fees
- Suggest 35% allocation to passive multi-factor
- Equal weighting to four managers

3: Diversified multi-factor core with unconstrained global equity manager satellite positions

- Similar governance budget compared to option 2, slightly lowered alpha potential, fees lowered even more
- Suggest 50% allocation to passive multi-factor
- Equal weighting to three managers

Equity Portfolio Options

Implement an equity portfolio composed of:

- One diversified passive multi-factor manager ‘core’ position (50% or ~$730 million*)
- Three unconstrained global equity manager ‘satellite’ positions (16.67% or ~270 million* each)

*The MVs are updated as of Jun.30, 2024.

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