

To: New Products Committee  
 From: Keith Taylor, Chief Investment Officer, ONE Investment  
 Date: June 21, 2023  
 Re: New Products Committee Workplan  
 Report: New Products Committee 2023-002

## 1. RECOMMENDATIONS

It is recommended that the Committee:

1. Approve the workplan in Appendix A.
2. Recommend to ONE JIB that the New Products Committee work with ONE Investment to continue developing the Large Municipality Offering.
3. Recommend to ONE JIB that the following motion on implementation of the changes to the Canadian Government Bond Fund approved on November 30, 2022 be deferred until the Investment Plans of Participating Municipalities are revised:

*That the mandate of the ONE Canadian Government Bond Fund be revised to focus primarily on short-term Canadian Government bonds as presented in Proposal A in tables 2 and 3, revised to include a 75% maximum allocation to Provincial bonds, and with the addition of a minimum individual security credit quality rating of A-minus, and a duration target of 1.75 years, plus or minus 50 basis points.*

*Table 2 Fund Issuer Options*

Permitted Issuer	Maximum Percentage of Net Assets
Issued or guaranteed by Government of Canada	100%
Issued or guaranteed by a Province	75%
Issued by a Municipality (including MFABC)	50%
Obligations of Banks and Loan & Trust Companies	0%
Asset-Backed Securities *	20%
Cash	10%

\* ABS must be government guaranteed

*Table 3- Fund Criteria Options*

Criteria	
Minimum credit quality of securities held	A-
Term structure measured by average Effective Duration (range)	Target 1.75 years +/- 0.5 years
Leverage or short sales permitted	No

Currency Exposure of holdings	Only Canadian dollar denominated or fully hedged to Canadian dollar
Permitted securities (short term)	Cash equivalents which may include treasury bills, commercial paper and other short-term instruments
Permitted securities	Fixed income securities including bonds, debentures, asset-backed securities, corporate obligations, and other evidence of indebtedness issued or guaranteed by governments or Canadian chartered banks

4. Defer reorienting the mandate of the Canadian Corporate Bond Fund until the Large Municipality Offering is fully designed.
5. Direct staff to bring forward reports to the Committee to implement key elements of the workplan including:
  - a. Changes to the ONE JIB Outcome Framework
  - b. Changes to asset allocations for the Outcomes
  - c. An implementation and transition plan
  - d. A summary report on ONE JIB'S overall investment strategy for the existing Prudent Investment Offering.

## 2. SUMMARY

This report will summarize a workplan for the New Products Committee that includes the items currently under consideration by the Committee and will also address the direction provided by ONE JIB at its March 1, 2023 meeting related to updating the risk/return assumptions for each fund and investment allocation.

The Committee has been evaluating potential changes to the Canadian fixed income funds and the ONE HISA allocation that are "building blocks" used in the ONE JIB's Outcome Framework. This process will involve revisions to the Outcome Framework and associated investment allocations, supported by analysis from an external consultant. This will be a multi-stage process and will be informed by the design of the Large Municipality Offering that is expected to be completed in 2023. Other potential changes to the Outcomes Framework that are not related to the changes to Canadian fixed income funds, ONE HISA or Large Municipality Offering may also be considered and incorporated in the analysis of the external consultant.

A transition plan will be required to implement all the changes to HISA, ONE Investment pooled funds, investment allocations for outcomes, and any other changes in the Outcomes Framework. It is recommended that implementation of all changes be deferred until all planning has been completed and approved by ONE JIB.

### 3. BACKGROUND

Following the comprehensive review of external managers conducted in 2022 an updated review of managers is being planned for Fall 2023

Ongoing oversight of external managers is part of ONE JIB's fiduciary duties. In addition to the quarterly analysis provided by ONE Investment, additional analysis from an external consultant will be provided on an annual basis as per the Policy for Reviewing External Investment Managers. ONE Investment is planning to engage an external consultant to provide an updated review of managers that will be presented to ONE JIB in Fall 2023. This review will not be as comprehensive as the November 2022 analysis, in keeping with the Policy's standard of a detailed review at least once every two years, but it will augment the analysis provided quarterly by ONE Investment.

**An updated asset allocation study will be conducted to support a review of the allocations used in the Outcome Framework**

ONE JIB directed ONE Investment to update the overall investment strategy including allocation details of the investment outcomes and risk return attributes at its March 1, 2023 meeting and as noted in the following motion:

*THAT staff be directed to report back to the Board, initially through the New Products Committee, with a report on ONE JIB's overall Investment Strategy by Q4 2023 with the report to include:*

- *risk/return assumptions for each fund,*
- *asset allocations for each outcome and return/risk assumptions for each outcome based on the current assumptions for risk/return, and*
- *proposals for any recommended changes to long term return/risk assumptions for each fund and/or asset allocations for each outcome, including reasons for the proposed changes.*

ONE Investment commissioned an asset allocation study in 2019 as part of the planning for the launch of ONE JIB. This study provided an analysis of the returns, risks, and correlations of asset types that were being considered for use in the investment offering. This type of analysis will help ONE JIB understand the risk/return characteristics of asset classes and how they contribute to the risk/return attributes of client investment allocations. This analysis was used in reports provided to municipalities contemplating a move to prudent investing. The 2019 analysis is no longer current, and an updated version would support the Committee's work.

Once there is clear direction on all the building blocks of the Prudent Investment Program including the Canadian Corporate Bond Fund, ONE Investment will engage an external consultant to update the asset allocation study. The study will include a look at returns, correlation and volatility to inform allocations of each of the building blocks. The workplan contemplates that this will be conducted in 2024.

ONE JIB has already approved changes to replace the ONE HISA in the Investment Outcomes with the ONE Canadian Government Bond Fund

ONE JIB approved changes that would remove the ONE HISA from the investment outcomes, replacing it with the ONE Canadian Government Bond Fund with, the investment orientation modified as follows:

- 75% maximum allocation to Provincial bonds
- Minimum individual security credit quality rating of A-minus
- Duration target of 1.75 years, plus or minus 50 basis points

Tables 1 and 2 below reflect the approved direction.

*Table 1- Fund Issuer Options (with proposed revision in red)*

Permitted Issuer	Maximum Percentage of Net Assets
Issued or guaranteed by Government of Canada	100%
Issued or guaranteed by a Province	75%
Issued by a Municipality (including MFABC)	50%
Obligations of Banks and Loan & Trust Companies	0%
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*Table 2- Fund Criteria Options*

Criteria	
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(range)	+/- 0.5 years
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Currency Exposure of holdings	Only Canadian dollar denominated or fully hedged to Canadian dollar
Permitted securities (short term)	Cash equivalents which may include treasury bills, commercial paper and other short-term instruments
Permitted securities	Fixed income securities including bonds, debentures, asset-backed securities, corporate obligations, and other evidence of indebtedness issued or guaranteed by governments or Canadian chartered banks.

The Committee has been considering a revision of the investment orientation of the ONE Canadian Corporate Bond Fund to refocus it on alternative investments

The Committee has started to consider options to replace the ONE Canadian Corporate Bond Fund with a different investment orientation. While these discussions have not been completed, the Committee has focused on options that provide investment exposures that are differentiated from the investment building blocks currently used in the Outcomes Framework. The Committee has viewed different types of alternative investments, such as real estate and infrastructure, due to their low correlations with equity and fixed-income investments.

## 4. ANALYSIS

The new Strategic Plan has identified growth of assets under management by \$3 billion

Recent changes to provincial legislation, including the regional review and Bill 23, will create uncertainty for municipalities considering moving to the prudent investor regime. Achieving the \$3 billion increase in assets under management (AUM) will be more challenging considering these changes.

ONE Investment and ONE JIB agree that developing a prudent investor offering that would be attractive to large municipalities is an imperative to meet the AUM growth targets. ONE Investment has undertaken an RFP process to identify a partner to provide outsourced chief investment officer (OCIO) services to ONE Investment as a key piece of what is known as the Large Municipality Offering. With this new focus, some of the work done to date by the Committee should be deferred pending decisions on the full design of the new offering. Table 3 below outlines anticipated timelines for this work along with how it will impact the Committee work.

*Table 3- Proposed timeline for workplan*

	Q2 2023	Q3 2023	Q4 2023	Q1 2024	Q2 2024	Notes
Design of Large Municipality Offering						
Revised and approved Cdn Government Bond Mandate						
Revise Cdn Corporate Bond Mandate						Defer, pending Large Municipality Offering
Revisions to ONE JIB Templates (i.e., IPS, Investment Plan, MCQ)						Details on Outcome Framework, ONE Pooled Funds and allocation weight are planned to be removed from IPS and Investment Plans.

	Q2 2023	Q3 2023	Q4 2023	Q1 2024	Q2 2024	Notes
Revisions to Outcome Framework						This will inform aspects of Asset Allocation Study.
Asset Allocation Study for existing Prudent Investment Offering Municipalities						Delay to 2024, pending Large Municipality Offering
Implementation of changes						Deferred until changes are reflected in Investment Plans of Participating Municipalities.

Replacing HISA with a modified ONE Government Bond Fund in the investment outcomes will alter the risk/return characteristics of the outcomes. An analysis by an investment consultant will be required to evaluate and potentially adjust the risk/return attributes of the investment outcomes

The ONE JIB has already approved a proposal to replace HISA with a modified ONE Canadian Government Bond Fund. These changes would change the risk/return characteristics of all investment outcomes. It is appropriate that the allocation weights used in the Outcomes Framework be reviewed before any changes take place. It is possible that the allocation weights of the outcomes may need to be revised to ensure that the outcomes target appropriate risk/return characteristics.

Implementing changes that would replace the ONE HISA in the Investment Outcomes with the ONE Canadian Government Bond Fund should be deferred pending other changes to the investment offering

As the New Products Committee is in the process of revising the investment orientation of the ONE Canadian Corporate Bond Fund, there may be more changes to the fund offering that would have an incremental effect on the risk/return attributes of the Outcomes Framework. It is appropriate that all changes to the building block funds be considered together. This means that decisions related to the reorienting of the ONE Canadian Corporate Bond Fund should be finalized, after which an asset allocation study can be conducted to inform any potential changes in allocation weights. This will be a multi-step process that should ensure allocation weights in the Outcomes Framework reflect the changes in the investment orientation of the building block funds. As appropriate, a transition plan may be required to implement all the changes involved together, making it appropriate to defer the implementation of changes already approved for relating to the ONE HISA and ONE Canadian Government Bond Fund.

Pragmatic changes in the Outcomes Framework could also be considered as part of the workplan

If changes in some of the building block funds are being considered and allocations in the Outcomes Framework are being reviewed, it may be appropriate to consider if other changes in the Outcomes Framework may also be appropriate. For example, the Asset Management Reserve Outcome is only used by one municipality, and despite this being a long-term allocation, the balances held in this allocation have been volatile, changing every year. This is problematic for an investment allocation that is intended to be long-term in nature. Also, the changes in ONE HISA may result in the risk/return characteristics of the Cash Outcome becoming more similar to the Target Date 3-5 Year Outcome. Participating Municipalities have yet to use the Cash Outcome as a source of cash or liquidity, with no drawdowns taking place since inception. These are two examples where the Committee may wish to revisit the purpose of the Outcome and potentially make changes to the Outcomes Framework.

**Details in existing Investment Plans and the IPS of Participating Municipalities may need to be revised before implementation of any changes to the ONE Investment Funds takes place.**

All Investment Plans of Participating Municipalities currently detail the name of ONE Investment pooled funds, allocation weights of the funds and the names and details of investment outcomes, all of which could change when the Committee completes the items on the attached workplan. ONE Investment cannot implement changes to client allocations that are inconsistent with the Investment Plans. Additionally, the Investment Policy Statements of every Participating Municipality include a table that describes the Outcomes Framework. If there are changes made to the Outcomes Framework, implementation may need to be deferred until the IPS of all Participating Municipalities are updated to reflect the changes.

## 5. CONCLUSION

The workplan of the Committee, summarized in Appendix A, provides detail on the current priorities of the Committee and steps that may need to be addressed before any changes can be implemented. An external consultant will be engaged to provide support and analysis for discussion and decision-making. This will be a multi-step process that should ensure allocation weights in the Outcomes Framework reflect the changes in the investment orientation of the building block funds. It is intended that all changes to funds and allocations be implemented together, which will require planning to coordinate the different aspects related to the implementation.

Drafted by: Keith Taylor, Chief Investment Officer

Approved by: Judy Dezell and Donna Herridge, Co-Presidents/CEO, ONE Investment