



November 7, 2023

MEMORANDUM FOR Board Members Michael Gerber, Dana Bilyeu, Leona Bridges,  
Stacie Olivares

FROM: Sean McCaffrey, Chief Investment Officer *SM*  
THROUGH: Ravindra Deo, Executive Director *RD*  
SUBJECT: New benchmark index recommendation for the I Fund

Aon Investments recently completed a comprehensive study for the FRTIB that examined the suitability of the benchmark indices currently in use for the TSP's F, C, S, and I Funds relative to the full universe of potentially qualifying alternative indices that are in use by U.S. institutional investors. Aon found that the I Fund's risk-return profile would benefit from the addition of stocks of companies from Canada and emerging markets countries, as well as an expansion into small capitalization stocks in all markets. Furthermore, Aon noted that such a broadening of the benchmark would better align the I Fund with the requirements of its enabling statute, which calls for a "reasonably complete representation of the international equity markets excluding the United States equity markets." Whereas the current benchmark, the MSCI EAFE Index, covered almost 75% of non-U.S. market capitalization when the I Fund was created, that coverage has declined to only 55%, primarily due to the growth of emerging markets over the past two decades.

Aon recommends that the FRTIB change the I Fund's benchmark from the MSCI EAFE Index to the MSCI ACWI IMI ex USA ex China ex Hong Kong Index. The MSCI EAFE Index contains 798 large- and mid-capitalization stocks across 21 developed markets. As noted above, these holdings cover only 55% of non-U.S. market capitalization. By contrast, the MSCI ACWI IMI ex USA ex China ex Hong Kong Index contains 5,621 large-, mid-, and small-capitalization stocks across 21 developed and 23 emerging markets, covering 90% of non-U.S. market capitalization.

Having reviewed Aon's detailed report, the Office of Investments recommends that the Board Members adopt as the I Fund's new benchmark index the MSCI ACWI IMI ex USA ex China ex Hong Kong Index. Such a change would significantly broaden

market exposure and diversification, increasing the likelihood of more favorable risk-adjusted returns in the long term.

If the recommended benchmark change is approved, the FRTIB will develop a plan to transition from the MSCI EAFE Index to the MSCI ACWI IMI ex USA ex China ex Hong Kong Index in calendar year 2024.