ThinkAdvisor

http://www.thinkadvisor.com/2014/09/30/advisors-cautious-on-pimco-total-return-fund

SEPTEMBER 30, 2014

Advisors Cautious on PIMCO Total Return Fund

With Morningstar's downgrade, even more questions are arising over the bond fund post-Gross

Will PIMCO Total Return investors head for the exits?

It's become a game of deal or no deal, with some advisors moving quickly to liquidate client holdings in the PIMCO Total Return Fund and others taking more time to decide on their response.

Overall, players throughout the asset management industry are asking whether Total Return should be on the menu of options they offer investor clients or if it is simply not attractive enough in terms of its risks-to-return ratio and issues associated with Friday's departure of portfolio manager Bill Gross.

Late Monday, Morningstar downgraded its rating of the PIMCO Total Return Fund (PTTRX) to bronze from gold; the research group also lowered its stewardship grade to D from C.

"Everyone is trying to get their name out [to clients] about what they think should be done," said Ric Lager, a Golden Valley, Minnesota-based RIA who serves retirement plans and others, in an interview with ThinkAdvisor.

"This is a major, fundamental event, when a fund is losing the guy who has been calling the shots for a long time. It's beyond General Motors replacing its president," he said, since that executive has lots of managers running corporate operations. "It's a pretty big deal."

RELATED

Gross' Move Fogs PIMCO, Janus Futures

Analysts are cautious on what Bill Gross' departure from the bond giant PIMCO to the smaller Janus means for both...

One of Lager's clients, who is on the benefits committee of a professional organization, says there is lots of communication going on about Total Return. "Some are suggesting that it should be gone, off the retirement-plan menu, and one client said that Fidelity had been in contact with them about the matter."

Fidelity says there are "no plans to make changes that would affect the availability of PIMCO funds" on its FundsNetwork platform. Plan sponsors, though, determine the fund choices on their individual 401(k) plans and can make such changes, adds a spokesperson.

According to BrightScope, some 27,000 large corporate 401(k) plans had assets in Total Return as of late 2012.

Varied Views

Other advisors, though, are comfortable with PIMCO and Total Return — at least for the moment.

"We don't select funds based on Morningstar fund ratings. It is of interest, though, but won't change our internal methodology," said Linda Lubitz Boone, CFP, of the Miami-based Lubitz Financial Group in an interview.

"Frankly, I believe that if custodians are pulling Total Return off their platforms, that is a shame. It's a knee-jerk reaction and is happening way too soon — we still don't know fully what kind of impact Gross' decision [to leave] is going to have."

Of the $190 million in assets that Lubitz Boone manages, about $6.7 million are invested in Total Return. "Most of my clients, 110 families, have a stake in it as a core fund," she said.

The advisor recognizes that the short-term risk is that there could be a "run on the fund" along with liquidity problems.

"There were PIMCO conference calls yesterday," Lubitz Boone said, that described "the large levels of liquid assets" the fund holds.

"Why bail on a fund with good record? I prefer to be proactive rather than reactive," she said.

In a note Lutbitz Boone sent to clients, the advisor explained: "Investor withdrawals notwithstanding, PIMCO now has a chance to reshape its own image ... It may well be that institutional investors may be glad that he has left ... now PIMCO can focus on [its] process and policies that have brought [it] such success in the past. Time will tell."

As Lager shares, PIMCO "is being proactive" in its communication with clients. "But it's quite a battle," he stressed.

Morningstar's Cut

As for what's behind Morningstar's recent downgrade of Total Return, "This signals a high level of confidence in the managers taking over responsibility of the fund [from Gross], but it also signals some significant areas of uncertainty around the fund itself, around PIMCO as a firm and around the fund's board quality, too," explained Michael Herbst, director of manager research for active strategies at Morningstar, in a video interview posted early Tuesday.

Morningstar also gave PIMCO a rating of D, down from C, on the quality of its fund board.

"When there is turmoil at a fund company, it is especially important to have an effective board in place," said Morningstar analysts Eric Jacobson and Bridget Hughes, CFA, in a article published late Monday.

The PIMCO boards are "in some turmoil," the analysts explain. "Continued disruption among PIMCO's independent trustees raises significant concern about the board's independence as well as its long-established setup."

Specifically, two of the PIMCO Funds Trust's five independent trustees — William Popejoy and Vern Curtis — recently left the board. This means it has just three independent trustees and two interested trustees, making the board 60% independent.

"This level falls short of industry norms; most fund boards are at least 75% independent," Jacobson and Hughes wrote.

Related on ThinkAdvisor:

- Gross' Move Fogs PIMCO, Janus Futures
- Lessons From Bill Gross' Departure From PIMCO
- What Bill Gross' Resignation Means for PIMCO, Janus & Markets