Fund In Focus: PIMCO Total Return Update

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EXECUTIVE SUMMARY

- PIMCO's Total Return Fund is a top performer in the Morningstar Intermediate Bond fund category across all major time periods.
- Contrary to investor's fears, fund outflows did not have a negative impact on performance.
- The organization's time-tested investment process remains intact.

Bond funds don't usually make news headlines, but when the star manager of the world's largest bond fund abruptly quits, it is a newsworthy event. The sudden and highly publicized departure of Bill Gross from PIMCO in September 2014 led many investors, and their financial advisors to immediately liquidate their holdings of the firm's flagship Total Return Fund. To be fair, the strategy was already experiencing redemptions in the months preceding Bill Gross's exit, but his surprise resignation certainly accelerated the fund outflows.

Given that it is nearly three years after the acrimonious exit of the star manager, we thought it would be worthwhile to review what changes have been made at PIMCO and how the Total Return Fund has fared in the post Bill Gross-era.

A LOOK BACK

Bill Gross was one of the original founder's of PIMCO in the early 1970s and a pioneer in the total return approach to bond investing. Over the next four decades, Bill Gross and his colleagues built one of the largest and most influential fixed income shops in the industry. At its peak in 2013, PIMCO had nearly $2.0 trillion in assets under management. The firm's flagship Total Return Fund was a key part of that success.

Since the inception of the Total Return Fund in 1987, the strategy has amassed significant assets. In 2000, the Total Return Fund had nearly $32 billion in assets and by the end of the decade assets were over $200 billion. The success of the strategy led Bill Gross to be named Bond Manager of the Decade for 2000 to 2009. The fund had also become one of the staple fixed income options in many retirement plans.

In 2008, the Total Return Fund earned the dubious distinction of becoming the world's largest mutual fund. However, some performance missteps in 2011 and again in 2013 left many wondering whether Bill Gross was beginning to lose his edge. With performance lagging and fund outflows beginning to mount, internal pressures within the PIMCO ranks started to surface. Shortly thereafter, a string of high-level departures and a constant barrage of negative news headlines led to the eventual resignation of the star manager in 2014.

THE NEW REGIME

Changes implemented in the post-Bill Gross era appear to have stabilized the organization. Most significantly, the new Chief Investment Officer structure, led by veteran portfolio managers with specific

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asset class responsibilities, has broadened the leadership across the organization and led to greater diversity of ideas within the Investment Committee.

Fears of further management shake-ups, a mass exodus of talent or significant underperformance turned out to be overblown. The firm has been remarkably stable over the last few years, employee turnover has been minimal and the organizational culture has improved considerably. From day one, the new leadership team has remained steadfast in their commitment to deliver performance for its investors.

Mark Kiesel, Scott Maher and Mihir Wohar, the new managers of the Total Return Fund, have done an excellent job navigating the strategy through challenging times and a staggering level of redemptions. While Bill Gross has received the lion's share of media attention, the new managers have decades of experience working at PIMCO and have grown up managing assets using the same time-tested investment process that has driven performance for clients over the long-term.

AN UPDATE ON PIMCO TOTAL RETURN

Even though the fund's assets are considerably lower today, at $74 billion as of September 2017, the Total Return Fund still ranks among the largest in the industry. Those who have stuck with the strategy have been rewarded, as the new managers have done an admirable job managing outflows without underperforming its benchmark or peers. At the end of September, the Total Return Fund has delivered positive alpha and is near, or in, the top quartile across all major time periods.

The new managers have made some minor tweaks, but the philosophy of the fund and the deep-rooted process of generating alpha through diversified sources have not changed in decades. The improved culture and team-focused management structure has led to better dialogue with the specialists and more opportunity for the best ideas to get expressed in the fund. These changes have paid dividends, as the fund's performance is back on track.

Another key aspect of the strategy that has not changed is the firm's emphasis on risk management. According to Morningstar data, the Total Return Fund has had a lower max drawdown than other top quartile managers over the last ten years. The fund's greater downside protection can be attributed to the team's ability to generate alpha from multiple sources, rather than relying credit risk to be the sole driver of performance. This approach served investors well during the 2008 financial crisis.

The fund continues to benefit from breadth of resources available within the firm. PIMCO remains well known for its investment prowess and deep team of experts across a wide variety of fixed income sectors. With improved performance and four consecutive quarters of net inflows at the firm, PIMCO has started to regain some lost market share. The organization appears to be moving back on the offensive after a few tumultuous years.

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For more information on our services, please contact **Mike Volo,** Senior Partner, at **781.997.1426** or **mvolo@cammackretirement.com**.

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