

The Power of PIMCO in an ETF

By Seana Smith
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Actively managed exchange-traded funds are back in the spotlight this week, with the world's largest bond fund, PIMCO Total Return [PTTRX] now available as an ETF (TRXT), drawing attention back to the ETF sector.

"It's a giant step for active ETFs," says Paul Justice, Director of ETF Research at Morningstar. "Actively-managed funds are not as popular, and it can be an effective way for well-known managers to move funds around."

The fund manager behind Thursday's ETF launch is Bill Gross, PIMCO's bond guru and manager of the \$250 billion Total Return fund. Gross' past success will likely boost demand for the new ETF, and according to one strategist, the fund company's name alone will draw new money.

"[PIMCO] is a very strong brand and Bill Gross is the bond king," said David Kudla, Mainstay Capital Management CEO and Chief Investment Strategist. "Any debt product [from PIMCO] will be popular."

Total Return posted an average return of 6.83% over the past 10 years, ranking the mutual fund in the top 6% of intermediate-term bond funds.

So how does the launch impact the overall exchange-traded industry?

"[PIMCO's Total Return ETF] is paving the way into a different distribution channel for funds," said Justice. TRXT will give average investors access to PIMCO's successful Total Return strategy, but at a significantly lower fee.

The new ETF's annual expense ratio is 0.55%, about 35 basis points lower than class "A" shares of PTTRX. And although it's considerably cheaper than its mutual fund sibling, TRXT's expense ratio is more than double its category average of 0.22%.

Intermediate-term bond alternatives Vanguard Total Bond Market (BND) and iShares Barclays Aggregate Bond (AGG) charge 0.11% and 0.22%, respectively.

But where there's opportunity, there's always risk, and despite numerous advantages over its mutual fund alternative, the new ETF does present some challenges. "SEC restriction prevents the exchange-traded fund to invest in options contracts, future contracts and swap agreements," says Kudla. "These investments are important to the fund's success as they're used to adjust interest-rate exposure and hedge against credit risk."

Another potential risk for the new ETF may serve as an opportunity for others. While PTTRX reveals its holdings quarterly, TRXT will be forced to disclose its full portfolio on a daily basis, enabling investors and managers to cash-in on Gross' success.

"Much of the mystery and magic that Bill Gross has worked with over time will be revealed," said Kudla. "And if managers want to front-run Bill Gross and copy [his] ideas, they will be able to do that."