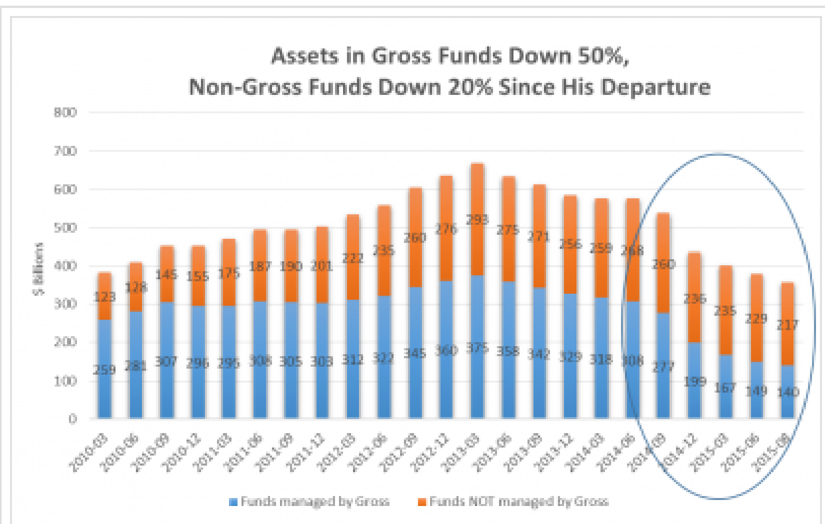
CORPORATE STRATEGY

Pimco is Ripe for a Reorg: Turnaround Expert

09/18/2015 | **Michael Hayes**

One year after the messy departure of founder Bill Gross, Pimco looks primed to launch a bold and comprehensive turnaround plan.

According to corporate turnaround experts, the fact that Pimco has already taken a few steps in that direction, lowering its ambitions for the equities funds business and contemplating layoffs, indicates that the firm is willing to make some tough decisions.



Source: Morningstar

When equities CIO Virginie Maisonneuve resigned in May, the firm said it would not replace her and it liquidated three funds under her jurisdiction -- Pimco Emerging Multi-Asset Fund, EqS Emerging Markets Fund and EqS Pathfinder Fund. Earlier this month, FOX Business reported that the firm is considering laying off some of its 2,400 employees to reduce expenses. The firm has hired several high-profile economic advisors, and has taken steps to retain its top portfolio managers, replacing stock options with cash as a long-term financial incentive, according to Bloomberg.

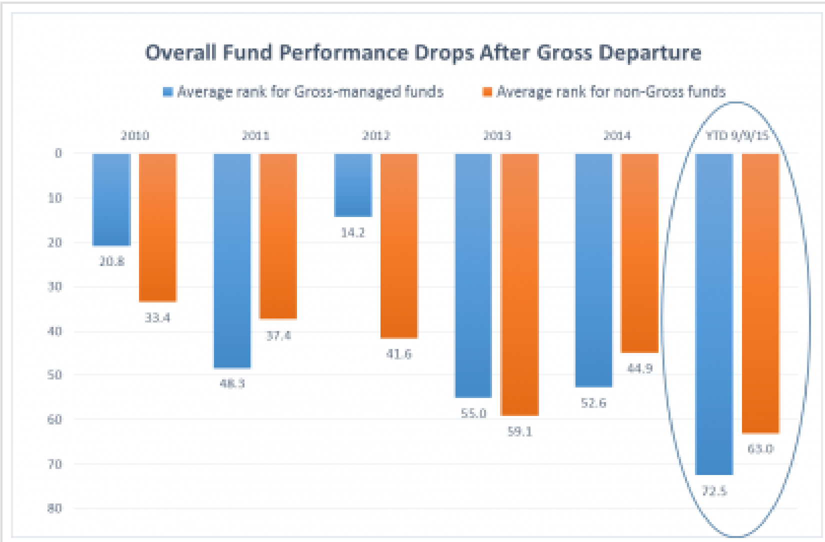
While all of these signs are encouraging, they may not be sufficient, some say.

The company could be preparing for a full-blown revitalization initiative, which might include measures as dramatic as a housecleaning across the executive ranks to the more mundane addition of research analysts to boost fund performance.

If Pimco really wants to get to the core of the matter, says corporate restructuring expert Joe Luzinski, it will need to rebuild investor trust and confidence. That could take years.

“When your clients are financial firms that trade with you based on trust, airing your dirty laundry in public leads to questions about credibility,” Luzinski says. “A company like that needs to re-scope, get its costs under control, and get its corporate structure in order.”

Indeed, a survey conducted by the CFA Institute shows that finding a trustworthy portfolio manager is twice as important to investors as earning the highest returns, and five times more important than paying the lowest fee. **American Funds**, **BlackRock**, and **Franklin Templeton** are the most trusted mutual fund firms among financial advisors, according to the 2015 Advisor Brandscape report from Cogent.



Source: Morningstar

The erosion of investor confidence in Pimco has become painfully obvious.

Across the firm, assets under management have fallen 21% since Gross's departure last September.

The damage is worst among funds that Gross managed, which have seen AUM cut in half, according to Morningstar. The average Gross-managed fund ranked in the 53rd percentile of its category at the end of 2014, but now ranks in the 73rd percentile.

But other funds in the complex have suffered collateral damage. Assets in funds that were not managed by Gross have fallen more than 20% since he departed, and the average fund ranking slipped to the 63rd percentile, from the 45th percentile last September.

As Pimco looks for ways to cut costs in response to the shrinking AUM, a source close to the firm says it has been canvassing clients for their thoughts on which investment products might be eliminated.

As it evaluates a turnaround plan, Pimco might consider the lessons of fund firms that managed to survive the market-timing scandal of 2003. A case study on **Putman Investments**, for example, points out that CEO Ed Haldeman was successful in his turnaround campaign because he viewed the scandal as an opportunity to re-examine the DNA of the entire firm -- and acted quickly.

"A savvy industry veteran and turnaround specialist, Haldeman also considered the market timing scandal from a broader, more opportunistic perspective," writes the author of the case study. "Was there an opportunity to repair an investment division that had significantly underperformed its competitors over the last two years? Could Putnam fundamentally change the culture of greed that had contributed to the current crisis?"

Pimco, on the other hand, has yet to introduce any meaningful changes into the corporate structure.

While Luzinski doesn't have first-hand knowledge of the inner workings at Pimco, he says it's possible that the lack of any visible reconstruction so far could reflect a level of discord among Pimco's executives, or its parent company, Allianz, about the most appropriate path to take.

"It could be a power struggle, or the board could be divided on a course of action," he says.

Joseph Luzinski, Development Specialists, Inc.

An informal survey of the turnaround strategies fund companies employed after the 2008 financial crisis offers insights into other strategies Pimco might contemplate. Among the most common tactics used by investment management firms to revive fund performance, firms like **Royce**, **BlackRock**, **Fidelity** and **Western Asset** strengthened their research departments by hiring more analysts.

Other firms, including **Columbia Threadneedle**, introduced more formal risk-management guardrails into the system to smooth out fund performance and increase portfolio manager accountability.

A breakdown in communications, caused by corporate silos, has been referenced by firms like **American Funds** and **Western Asset Management** Co, as one of the factors that weighed down fund performance during the crisis. American Funds is working to open the lines of communications between portfolio management teams in its fixed-income division and its equity teams, while Western is addressing the corporate divide that separates macro researchers and fundamental analysts.

How do fund firms discover these cracks in the foundation?

A number of asset management companies launched intense soul-searching campaigns when the crisis hit, re-examining everything from the firm's basic value proposition to its staffing levels.

But Pimco faces a challenge other fund firms haven't encountered – the loss of its founder and chief spokesman. Neither of his successors at Pimco, CIO Dan Ivascyn or CEO Doug Hodge, have Gross's level of enthusiasm for the media spotlight or the gravitas he brings to press interviews. Reuters points out that Ivascyn has appeared on CNBC only once since Gross left the firm. But Gross himself, now a portfolio manager at **Janus**, has been interviewed by CNBC on 10 separate occasions.

That lack of a public persona is working against Pimco as it tries to regain investor confidence.

"It doesn't help," says Luzinski. "The chairman of the company or the board of directors should figure out who the best person is to become the face of the company, clean off the decks, and get everybody on board."

Pimco declined to comment for this article.

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