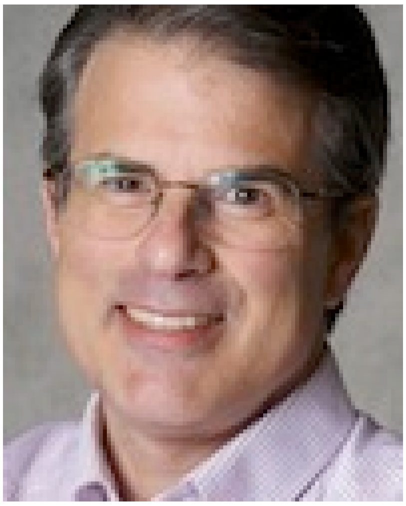
A New Book from PIMCO's Stacy Schaus

By Kerry Pechter *Thu, Jun 1, 2017*

If you don't know Ms. Schaus, you must be new around here. She's an EVP at PIMCO, the head of its defined contribution practice and the voice of its thought leadership in that area. Her new book on DC investment design is co-authored with Ying Gao.



As soon as the FedEx driver delivered my review copy of "Successful Defined Contribution Investment Design" (Wiley, 2017) by Stacy Schaus and Ying Gao, I turned to the chapter on retirement income options for plan sponsors and retirees. This epigraph greeted me:

"I advise you to go on living solely to enrage those who are paying your annuities. It is the only pleasure I have left" — Voltaire.

Touché. Disarmed by the great man's mordant wit, I dove into Chapter 10, ready to discover what Schaus (right) and Gao, both of PIMCO, were telling plan sponsors about helping participants navigate the transition from accumulation to income at retirement.

If you don't know Stacy Schaus, you must be new around here. She's an executive vice president at PIMCO and head of the big bond firm's defined contribution practice. She's the ambassador of PIMCO's DC business and the voice of its thought leadership in that area. A very frequent flier, Schaus is ubiquitous at the more cerebral industry conferences (and usually one of the few attendees to raise a hand during Q&A).

Her new book is a sequel to "Designing Successful Target-Date Strategies for Defined Contribution Plans" (Wiley, 2010), which focused on the creation of custom target-date funds. PIMCO issues a proprietary line of TDFs, called RealPath, but the firm is better known as a supplier of actively managed bond funds to DC plans.

"We are very active in defined contribution," Schaus told *RIJ* recently. "We're the largest manager of active income strategies in DC plans, including being part of TDFs."

So where does PIMCO stand on income generation. Interestingly, about eight years ago, PIMCO introduced a 10-year retirement income-generating bond fund composed of Treasury Inflation-Protected Securities. PIMCO even tested the idea of combining the funds with a MetLife longevity annuity for a two-stage flooring solution.

That was a retail product, however, and in their book, whose content is largely based on surveys of and interviews with plan sponsors and consultants, Schaus and Gao deal mainly with issues around DC plan design and investment options. But the book also includes recommendations about income:

The PRICE method. This acronym stands for PIMCO Retirement Income Cost Estimate. Schaus recommends that DC plan sponsors use this number as a benchmark to help participants determine how much they have to save to achieve a desired retirement income. PRICE is equal to the discounted present value of a 20-year annual real income stream using the historical U.S. TIPS yield curve. “PRICE is a proxy for the cost of retirement income,” Schaus told *RIJ*.

‘Objective-aligned’ glidepaths. When choosing a target-date fund *glidepath*—that’s the rate at which a participant’s TDF fund allocation shifts from stocks to bonds over the course of their working years—Schaus recommends that plan sponsors use what she calls an “objective-aligned” glidepath.

Using such a glidepath, a TDF would contain more TIPS than most TDF designs typically do, the book says. The use of TIPS, not coincidentally, aligns the glidepath design with the PRICE savings objective. “The objective-aligned glidepath means that you’re looking at what it cost to retire, and what it takes to keep pace with it. That’s where we use the PRICE,” she said in an interview.

In practice, this might mean that a participant might invest in a TDF that corresponds to their risk tolerance and tailor their contributions to their savings goals rather than default to the TDF that matches their assumed retirement date and to a standard salary deferral.

‘In-plan’ rather than ‘out of plan’ annuities. Assuming that a plan sponsor wants to make an annuity option available to participants who want to convert part of their tax-deferred savings to income at retirement, Schaus and Gao favor directing participants to an “institutionally-priced” income annuity after they leave the plan. Taking their cue from surveys of plan sponsors, they don’t recommend including an income option (either a deferred income annuity or a lifetime withdrawal benefit) in the plan itself.

“In our surveys, consultants have raised questions about portability of the benefit, and about client communications,” Schaus told RIJ. “We’re supportive of buying annuities outside the plan, on platforms where you have competitive bidding. Retirees can consider going to an institutionally priced platform like Hueler’s **Income Solutions** or Fidelity.”

Actively managed bond funds rather than indexed funds. Schaus’ company is an active bond manager, which means that its fund managers try to outperform the bond indexes by, for instance, making bets on the economy, the direction of interest rates, and the credit environment. More than four in five plan sponsors offer active bond funds (versus 40% offering index funds), according to the book. Not surprisingly, she and Gao recommend this strategy during the accumulation and income stages of a TDF.

I asked Schaus if she still recommends custom TDF to plan sponsors. In a custom TDF, a plan advisor might create a custom asset allocation and glidepath out of a plan’s existing investment options.

“In our consultants survey, we asked about custom,” Schaus said. “It continues to grow. Plans above $1 billion will find that approach most attractive. On those plans, consultants recommend using them to establish control over the glidepath, hiring best-in-class managers, and leveraging the investment options are already on their core lineups.”

Although the new book can serve as a guide to plan sponsors, Schaus told RIJ that PIMCO itself isn’t in the plan design business. “Sponsors ask us if they should redesign their plan, and how can we can help them do that. But PIMCO isn’t hired to design plans,” she said. “The book is a comprehensive guide to help sponsors go through the design process. The plan designer would be a consultant, working with the plan sponsor.”

Schaus said that the book should be seen as her words and the words of the plan sponsors and consultants she has surveyed, and not necessarily PIMCO’s positions. “The book is based on 10 years of discussion and research on global plans, governance, default and core lineups,” she said. “It brings it all together, and addresses the questions we often hear from sponsors.”