Aruna Hobbs

Managing director and head of Stable Value Investments at New York Life Investments

ALTHOUGH stable value funds have been around for decades—and represent thousands of plans and millions of participants—they are sometimes not understood. Aruna Hobbs, managing director and head of stable value investments at New York Life Investments, spoke with *PLANADVISER* about the stable value market, the different types of stable value funds and how advisers should discuss such funds with plan sponsor clients.

PA: How do stable value funds differ from money market funds when it comes to that retirement plan looking for the "safe investment"?
HOBBS: It is appropriate to think of stable value funds as more of a hybrid between bond funds and money market funds. They provide the returns and higher yields similar to bonds but the safety and liquidity of money market funds.

Stable value funds have insurance protections unlike other investment options in a 401(k) lineup. Should there be some extreme scenario, there's a standing guarantee that a participant is not going to lose at least what he's put in—in most circumstances. Another important difference is that stable value funds are not SEC[Securities and Exchange Commission]-registered mutual funds. They're managed either as collective investment trusts, pools or separately managed accounts.

PA: What is the value of stable value funds in today's marketplace and the current interest rate environment?
HOBBS: People have worked and saved for retirement a long time—stable value allows the accumulated earnings over their employment history to stay safe and not evaporate due to market volatility.

Whether it's the economy, Euro hang, stock market volatility, low interest rates or the fiscal cliff—there is a place for your retirement balances that keeps your accumulated savings safe, gives you peace of mind and is a good diversifier to some of the other more risky investment classes you may have exposure to. It serves effectively as a shock absorber in times of market distress and is a core part of the asset allocation mix in normal times.

The value proposition is unique. You are getting cash-like liquidity but at higher returns; that is, you're getting bond-like returns but without the volatility. It's not sheer coincidence that it is such a popular option amongst participants and has been so consistently through a variety of economic cycles.

PA: What criteria should an adviser use when evaluating stable value funds?
HOBBS: The thing to keep in mind is that stable value combines investments and insurance. So there is not an apples-to-apples comparison to the mutual funds setup where you can evaluate performance-yield metrics with a whole host of analytic tools. Like with all insurance, it offers certain guarantees and safeguards. But, in order to provide such safeguards and returns that are generally higher than money market funds, it comes with some unique structural features, and there are some tradeoffs with those features. Like with everything, there is no free lunch.

For an adviser it's probably a good idea to understand the basics and tradeoffs and to develop a simple product scoring model for clients because one size is not going to fit all. With the wave of boomers retiring the "value" aspect of stable value is only going to increase, so it behooves anyone in an advisory or fiduciary capacity to take the time to do so.

PA: What is the best way for an adviser to explain these benefits to plan sponsors?
HOBBS: I would keep it very simple: "You're buying protection on behalf of your participants that is allowing you to provide a higher rate of return than they could have earned from some alternatives out there, essentially getting all the upside of the portfolio returns with downside protection to the principal. And for providing this comfort via the inherent guarantees or protections, there will be some tradeoffs, usually centered around some of the aspects of liquidity. For example, not every event or withdrawal is going to be covered; for some, you may have to take market risk. But if you're prepared to understand and accept those tradeoffs, this is a very good investment for people who are trying to save for their retirement and, importantly, preserve their savings and diversify their overall asset allocation mix. This has been borne out over the years and even through the crisis."

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"[Stable value funds are] a low-risk investment option that appeals to the more conservative investor, as well as those who want to optimize their asset allocation mix," according to Aruna Hobbs, speaking at the 2012 PLANADVISER National Conference. "We see it being utilized across generations and at a steady rate of about $1 out of every $5 of DC plan assets."

According to Hobbs, there are two types of "pooled" stable value funds: bank-held collective investment trusts (CITs), managed by a stable value manager and backed by "wrap" contracts; and insurance funds, which are backed by highly rated insurance companies. Both structures combine assets of multiple, unrelated small to midsize plans and generally share the experience. For any fund to be considered stable value, Hobbs clarified, it must be backed by a stable value contract, which can come in different forms. There are varying levels of guarantees in each and varying levels of transparency

According to Hobbs, there is "a need and use for each" of these types of funds. "These are diversified products backed by fixed-income portfolios, and regardless of the shape they come in they all deliver the same principal benefits to the investor—stable principal and better returns than the alternatives in that space."