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PERSONAL JOURNAL

## Your Fund Manager's Secrets

Many New Facts Are Available On the People Who Pick Stocks; Making the Best Use of It All

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It's getting easier to size up your mutual-fund manager.

Traditionally, it's been tough to know much about the person running your money -- you could get a name, a bare-bones bio and some historical data on past performance, and not much more. However, in the wake of recent fund-industry scandals, regulators are prodding fund companies to cough up new information, ranging from how much money fund managers have personally invested in their funds, how they're paid, even whether they're moonlighting as a money manager for other investors.

For investors, these disclosures are changing some of the traditional assumptions about what to look for in a mutual-fund manager. According to industry experts, a money manager's experience and personal commitment to a fund -- do they invest their own money in it, or not? -- can be a better indicator of a fund's future performance than its historical returns.

Some of the studies' conclusions: Funds led by a team of managers perform as well as individually managed funds, but with less risk and at lower costs to investors. Another study found that, in cases where a money manager holds down two jobs, running both mutual funds and hedge funds, those mutual funds significantly outperform other comparable funds.

"It's critical to look at the portfolio manager," says Jeff Tjornehoj, senior research analyst at Lipper. "Somebody is there operating the machinery and making it go, and in bad cases, driving it into the ground."

The disclosures come in the wake of the "market timing" scandal that shook the fund

industry in recent years, which involved fund companies giving favorable treatment to some big investors at the expense of smaller shareholders. The Securities and Exchange Commission started requiring funds to reveal more information about who's running their money.

The bad news: These disclosures are often buried in lengthy fund filings, and aren't always written in plain English. Here's where to find them, and how to extract the most useful information.

For starters, the basic mutual-fund prospectus has gone through one small but important change. For the first time, individual members of a fund's management team must be named, along with their experience -- a sort of mini-resume.

Next, examine a manager's track record, both at his current fund and any funds he led previously. Collect the names of the manager's current and former funds from the prospectus and company Web site, then search for those funds on sites such as Morningstar.com or Finance.yahoo.com.

Look for a manager who has demonstrated an ability to handle various market conditions by posting a decent track record over two full up-and-down cycles of the broad market, which currently would mean looking back to 1998, says John Merrill, president of Tanglewood Capital Management Inc., a wealth-management firm in Houston.

Instead of looking at a single long-term-performance figure, it's important to look at how managers have performed relative to their peers each year, says Lipper's Mr. Tjornehoj. Such comparisons can be made at Morningstar.com.

Under the new SEC rules, team-managed funds also must name their leaders. That's especially important as fund management increasingly becomes a group activity: About 65% of funds are managed by teams, according to Morningstar Inc., up from 49% in 2000.

That trend is good for investors, according to a recent study by researchers at Babson College and the University of Massachusetts Amherst. The study examined about 3,000 funds and found that returns over 11 years were roughly equal for funds run by a single manager and funds run by a group of managers.

However, team-managed funds showed much lower risk, in the form of less-dramatic swings in performance. They also were less costly overall for investors, with expense

ratios that were about 0.1 percentage point less than individually managed funds. The average U.S. diversified stock fund's expense ratio is 1.45%, according to Morningstar.

Possible reasons for the price difference include teams' ability to manage multiple funds more efficiently and the fact that "star managers can command much higher salaries" than team players, explains Mark Potter, a co-author of the study and associate professor of finance at Babson College. Of course, expense ratios include other costs beyond management fees.

The down side: With group management it isn't always clear who is mainly responsible for a fund's performance. Investors should check in a fund's prospectus if anyone on the team is designated as lead manager. That person may have the final say on investment decisions, making his experience and track record a key consideration for fund investors. Some major fund companies, including Fidelity Investments and Janus Capital Group Inc., still rely largely on individual managers.

Mutual funds now must disclose how much of a manager's personal money is invested in the fund he or she runs. The information is found in the "statement of additional information," which is often available on the fund's Web site. Investors can find the document on the SEC web site at [www.sec.gov/edgar.shtml](http://www.sec.gov/edgar.shtml).

Even though the ownership data are disclosed in broad dollar ranges, and doesn't show the manager's ownership as a percentage of his net worth, recent research suggests the new information can still be useful. A study by researchers at the Georgia Institute of Technology, London Business School, and the University of South Florida examined more than 1,300 funds and found that those with managers who own shares outperformed their peers by about 1.4 percentage points annually. By comparison, funds in the study that had no manager ownership outperformed their peers only by about 0.3 percentage point annually.

Manager ownership is "a good way for shareholders to gauge a manager's belief in what he or she is doing, and the decisions they're making on a portfolio," says a Janus Capital spokeswoman. The company last year introduced guidelines encouraging managers to invest an amount equal to at least twice their annual base salary in the funds they run.

Other firms, including AllianceBernstein LP, use other means to align managers' interests with those of clients. A spokesman says employees invest in the company's products through 401(k) and other accounts.

Funds now must disclose in the statement of additional information how a manager is

compensated -- whether it's a fixed sum, or based on other criteria. Investors should be concerned when managers are compensated based on a fund's assets, analysts say, because it places emphasis on marketing, not on investment decisions. Karen Dolan, an analyst at Morningstar, expects the pay disclosures will encourage more companies to switch to performance-based compensation, which can help align managers' interests with those of shareholders.

Companies paying for performance must also disclose the formula they use. "One year is too short," says Ms. Dolan, who prefers pay plans based on a fund's rolling four- or five-year returns.

It turns out that money managers are often multitaskers, running separate accounts and hedge funds for wealthy investors as well as one or more mutual funds. Under the new SEC rules, funds must disclose in the statement of additional information how many other accounts a manager runs and the total assets in those accounts.

Researchers at Loyola University Chicago, the University of Illinois, and the University of California, Irvine found that such side-by-side management of hedge funds and mutual funds may actually benefit mutual-fund investors. The study found that, in cases where one individual runs both mutual funds and hedge funds, the mutual funds significantly outperform their peers while the hedge funds underperform their peers.

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