Buy the Manager, Not the Fund

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Countless financial publications offer rankings of mutual funds, almost always based on historical performance. The problem is that these rankings focus on the performance of the fund rather than the portfolio manager running it. In some instances, a long-term track record may have been achieved by a manager who is no longer with the fund. The person running the fund is a particularly important factor at Fidelity, where fund managers are given a great deal of flexibility in picking stocks for their funds. Let's look at an example.

Erin Sullivan took the reins at Aggressive Growth Fund in late 1997. In 1998, a great year for aggressive growth stocks, she delivered a 43% gain for shareholders. This performance not only bested the S&P 500 Index and NASDAQ Composite by a sizable margin, but also placed Aggressive Growth as the top performer among Fidelity's diversified equity funds that year. In 1999, she doubled shareholder value with a whopping 103% return. This performance again far outperformed the benchmarks and her peer group average.

Then came the bad news. In February 2000 Erin Sullivan left Fidelity. She was replaced at Aggressive Growth by Bob Bertelson. While we think Erin Sullivan was one of the best stock pickers at Fidelity in the past ten years, we believe Bob Bertelson was probably one of the worst. In the period he managed the fund from February 2000 until November 2002, it lost over 80%. In fact, a fund that was among the top in the industry in 1999 had dropped to near the bottom by the end of 2002. While this period was not a fun time to be running an aggressive growth fund, Bertelson managed to underperform all domestic equity funds at Fidelity in 2000, 2001, and 2002. In November 2002, Bertelson was finally replaced by a new manager.

So here's our point. If you looked to add Aggressive Growth to your portfolio in early 2000, you would have seen a fund with a terrific multi-year track record. In addition, Morningstar (whose star ratings are based on past performance), still rated the fund 5-stars (their best rating), after Sullivan had left. If you invested in this fund, not knowing a new portfolio manager was at the helm, you would have set yourself up for disaster.

When evaluating a fund for your portfolio, make sure you know who is responsible for the fund's track record. If a fund has a new manager, check out his or her performance at previous funds. If the manager doesn't have a track record, that may be reason enough to wait awhile before buying the fund.

However, we differ with other financial publications that suggest buying a "new" fund only after it has an established track record. One example of this is Fidelity International Small Cap. Fidelity introduced this fund in September of 2002. Its small size coupled with a solid management team helped it deliver an 82% return in 2003. Those investors still waiting for an "established" track record for the fund missed out on one of the best investments in international funds last year. For those still waiting, Fidelity International Small Cap is still among the leaders among international funds this year as well, sporting a 12% year-to-date return through June 30. Not bad, considering the S&P 500 has only offered a 3% gain over the same period.

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