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## New mutual funds better than older ones?

By Jesse Solomon @JesseSolomonCNN March 2, 2014: 12:38 PM ET

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NEW YORK (CNNMoney)

In the world of mutual funds, it's good to be a rookie.

A **study released last month** by the National Bureau of Economic Research found that younger mutual funds consistently outperformed their more seasoned counterparts.

Using data from Morningstar and the Center for Research in Security Prices, the authors looked at over 3,000 mutual funds from 1979 to 2011. They realized that funds with an age of three years or less beat out those that have been around for more than ten years by almost 1% per year.

The reason: the mutual fund industry keeps getting more competitive. New entrants have a lot to prove -- and that gives them a big incentive to put up strong returns.

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Dr. Lubos Pastor, a business professor at the University of Chicago and one of the study's authors, said that newer mutual funds are often run by recent MBA grads equipped with fresh financial knowledge and a strong grasp of the latest investing technology. But it's a vicious cycle. As the fund gets older, it has to face new competition.

"You just graduated, and you've absorbed the latest academic research to beat the markets," Pastor said. "For a few years, you're riding this wave. But as you keep running your fund, more and more funds keep popping up."

While the study did find that mutual fund managers gain more skills the longer they are on the job, it wasn't enough to stay ahead of the newbies.

The researchers didn't look at the actual ages of mutual fund portfolio managers though. But a 1996 study from the NBER did.

Its results were similar, but for different reasons. The 1996 study found that younger mutual fund managers outperformed their older peers because they embraced a survival-mode mentality.

"If you're young and you didn't cut it, you lost your job," said Dr. Glenn Ellison, an economics professor at MIT and an author of the earlier research. "If you're experienced, the market seems more forgiving."

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But in a counterintuitive twist, younger managers seemed to invest in less risky stocks than their older peers, Ellison said.

Of course, there are plenty of other things to consider when picking mutual funds, such as strategy, past performance, and fees. But age is hard to ignore.

If the mutual fund industry stopped hiring today, experience would actually be a virtue and lead to better returns, Pastor said.

The study comes at an interesting time for the mutual fund industry. There is an intense debate about the value of actively managed mutual funds versus exchange traded funds -- low-cost bundles of stocks and other assets that often mirror an index.

ETFs have become increasingly popular in the past few years. There have been plenty of stories and headlines about how ETFs are killing the traditional mutual fund. And it makes sense. Why pay a mutual fund manager a big fee to select when you can just buy the SPDR S&P 500 ETF ( **SPY**) -- which was up 30% in 2013 and has gained nearly 170% in the past five years.

Still, some experts say mutual funds aren't dead. Investors just have to choose the right ones.

"The fact that the index beat the average actively managed funds doesn't mean that it beat the good actively managed funds," said Ellison. ■

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