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A Life Cycle Analysis of U.S. Mutual Funds

Leng Ling[a]

[a] Department of Economics and Finance, J. Whitney Bunting College of Business, Georgia College & State University

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Abstract: This study proposes a five-stage asset growth model to describe the life cycle evolution of actively managed equity mutual funds and shows that mutual funds exhibit distinctive performance, size, expense ratios, and asset turnover through stages of incubation, high-growth, low-growth, maturity, and decline. It also investigates the viability of managerial strategies to affect a fund's life cycle evolution and shows that the strategies of changing investment objectives, adding portfolio managers, or downsizing management team do not have a rejuvenation effect. These findings suggest that investors should avoid investing in funds that have evolved to older life cycle stages, as there are few effective strategies that fund advisors can undertake to revive the performance of declining funds.

JEL Classification: G11, G20, L2, L22
Keywords: Mutual funds, Life cycle, Rejuvenation.

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1. Introduction

This study examines from a corporate life cycle perspective equity mutual funds that are actively managed by portfolio managers.[1] Drawing upon the industrial organization literature, the paper proposes a mutual fund life cycle model that encompasses stages of incubation, high-growth, low-growth, maturity, and decline. Each life cycle stage is defined as a time period associated with a common

[1] This paper focuses on firm life cycle, which is different from product life cycle (Polli and Cook, 1969; Anderson and Zeithaml, 1984) and industry life cycle (Londregan, 1990).