

MEL LINDAUER | TAYLOR LARIMORE | MICHAEL LeBOEUF

Foreword by John C. Bogle

The **Bogleheads'** *Guide to* **INVESTING**

SECOND EDITION



WILEY

**ADDITIONAL PRAISE FOR
*THE BOGLEHEADS' GUIDE TO INVESTING***

“This book is written with great charm, wit, and humility by a troika of retired, self-educated investors who themselves have become experts in financial planning and investing. Here they share what they have learned at the school of hard knocks. It is to trust the wisdom of their chosen mentor, John Bogle, who advocates investing in low cost, tax efficient mutual funds and using common sense in all financial decisions. Furthermore, the authors have mastered the complexities of their subject to the point where they can explain financial concepts simply and clearly. Readers and clients often ask me to recommend a book on financial planning investing. I will recommend this one.”

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—*Bill Schultheis, author, The Coffeehouse Investor*

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Guide to Investing

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Second Edition

**Mel Lindauer
Taylor Larimore
Michael LeBoeuf**

Foreword by John C. Bogle

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*To John C. Bogle, founder of
The Vanguard Group*

*A man whom we knew from afar for many years but
have since come to know and cherish as a friend.
While some mutual fund founders chose to make
billions, he chose to make a difference.*

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Foreword

Nothing is more deserving of your attention than the intellectual and moral associations of Americans. Americans of all ages, all conditions, and all dispositions constantly form associations [of a] thousand kinds . . . religious, moral, serious, futile, general or restricted, enormous or diminutive. I have often admired the extreme skill with which the inhabitants of the United States succeed in proposing a common object for the exertions of a great many men and inducing them voluntarily to pursue it.

As soon as several of the inhabitants of the United States have taken up an opinion or a feeling which they wish to promote, they look out for mutual assistance, and as soon as they have found one another out, they combine. From that moment they are no longer isolated men, but a power seen from afar, whose actions serve for an example and whose language is listened to.

Only by the reciprocal influence of men upon one another are feelings and opinions recruited, is the heart enlarged, and is the human mind developed. . . . This can only be accomplished by associations. What political power could ever carry on the vast multitude of lesser undertakings which the American citizens perform every day, with the assistance of the principle of association?

—Alexis de Tocqueville
Democracy in America, 1840

The Bogleheads of the Internet, it seems to me, are the paradigm of the American association described with such perceptive power by Alexis de Tocqueville in his seminal work. This association of intelligent, integrity-laden, and like-minded investors has provided not only a sound *intellectual* rationale for the successful accumulation of wealth but, just as de Tocqueville suggested, a sound *moral* rationale as well. No wonder *Democracy in America*—from a Frenchman who visited America for just

nine months when he was but 25 years old!—has stood the test as the defining text of the American way for nearly 170 years.

During its decade-plus of existence, the Bogleheads have moved from a loose association of dedicated investors to a formal website, Bogleheads.org. (The Bogleheads previously gathered online at the Vanguard Diehards message board on Morningstar.com.) The Bogleheads website now attracts an incredible 50,000 visits and as many as 1,500 individual posts each day. *The Bogleheads' Guide to Investing* marks a major milestone for this extraordinary association.

Two especially notable characteristics mark the Boglehead culture. One is *rationality*. These individual investors are awash in common sense, intolerant of illogic, and permeated with a preference for facts over hyperbole. Today's popular investment misconceptions—short-term focus and fast-paced trading, the conviction that exceptional past fund performance will recur, the ignorance of the importance of fund operating expenses, sales commissions, hidden portfolio turnover costs, and state and federal taxes—are anathema to them. Bogleheads have come to accept as the core of successful investing what I have called “the majesty of simplicity in an empire of parsimony.”

The second characteristic is, of all things, caring. Bogleheads care about one another. They are eager to help all investors—regular visitors to the website and new ones, informed and naïve, experienced and novice alike—who have questions on almost any investment subject, and willing to discuss the investment issues of the day, sometimes even the national and global issues, with no holds barred (except for rudeness or coarseness). Fund selection, fund performance, types of investments, retirement planning, savings programs, tax management—none are beyond the scope of this remarkable association of investors who, without compensation or bias, strive to help their fellow investors. If there is a website that bespeaks the Golden Rule, surely the Boglehead site is its paradigm.

BOGLE AND THE BOGLEHEADS

The Bogleheads had been associating for at least three years before they came to my attention. I had heard them discussed by Vanguard's public relations staff, and early on got the idea that they were not only firm advocates of my approach to investing—expressed in the investment strategies and human values that represented Vanguard's rock foundation when I created this upstart firm in 1974—but were also a pretty special group of people.

However, it was not until February 3, 1999, that I met my first Boglehead. The occasion was “The Money Show” in Orlando, Florida, where I gave a contentious speech about investment principles (“The Clash of the Cultures in Investing: Complexity vs. Simplicity”) that at once seemed to confound the hosts who invited me to address the show, to infuriate the sponsor firms (all offering their own routes to easy riches), and to amaze and delight the audience of several thousand individual investors.

Shortly before my talk, Taylor Larimore (there with his wife Pat) introduced himself to me. Taylor, then and now considered the unofficial leader of the Bogleheads, proved to be as fine a human being as I’ve ever met—warm, thoughtful, intelligent, investment-savvy, and eager to help others. A combat veteran of World War II and an exceptional sailor are only a few aspects of Taylor’s background. I mention them because the first demands courage and discipline; the second, careful planning and staying the course one has set, all the while adjusting to the winds and tides. These traits, as it happens, are the principal traits of the successful investor.

In March 2000, when I spoke again in Florida, Taylor invited me to meet with the Bogleheads at his Miami condominium located at virtually the same location where Taylor was born—he honors me by calling it “the house that Jack built”—and I enthusiastically agreed. When I came down into the hotel lobby, there to meet me was Mel Lindauer, unofficial associate leader of the group, next to a sign that read “Bogleheads Meet Here.”¹ We all went to Taylor’s lovely home, and Pat’s hospitality at dinner made what came to be known as Diehards I an evening of extraordinary warmth, energy, and delightful conversation, and some 20 investors who had never met one another before quickly became friends.

The following year, at Diehards II, the group met in Valley Forge, Pennsylvania. The festivities began on June 8, 2001, with a dinner addressed by *Money* journalist Jason Zweig, now with 40 Bogleheads in attendance. He would later write an article extolling the group: “By singing in harmony from the same page of the same investing hymnal, the Diehards drown out market noise.” The next day included an extended visit to Vanguard’s head office in Valley Forge, where I acted as host, tour guide, and keynote speaker. The questions and answer session that followed was broad-ranging, and ended with the Reverend Bob Stowe,

¹It is no coincidence that Taylor and Mel, among the most active participants on the website, teamed up to write this book. They were joined by Michael LeBoeuf, whom I have also come to know, another major contributor to the Boglehead website, and an author in his own right.

a Massachusetts Boglehead, presenting me, on behalf of the association, with a handsome regimental bugle of World War II vintage, symbolizing my “clarion call to build an industry that protects and serves the average investor.” (I couldn’t help but respond with this quotation from St. Paul: “If the trumpet shall give an uncertain sound, who shall prepare himself to the battle?”)

Diehards III, kindly hosted by website provider Morningstar, took place in Chicago on June 26, 2002, as some 50 Bogleheads from all over the country participated in the firm’s annual investment conference, taking in my speech (“The Tell-Tale Chart”), and having an active series of gatherings. In Chicago, this association of good human beings who happen to be intelligent investors and who seek to spread the gospel grew ever more familiar and friendly.

The next gathering (Diehards IV) took place on May 10, 2004, when some 60 Bogleheads gathered in Denver, Colorado, guests of the annual conference of the Association for Investment Management and Research, the professional organization that represents securities analysts and money managers. (AIMR has now taken the name The CFA Institute, with the acronym standing for Chartered Financial Analyst.) The Bogleheads were given seats in a special section for my speech (“Creating Sound Governance: The Shareholder’s Perspective”), which was followed by an extensive question and answer session. The final question put to me by the moderator was “What is a Boglehead?” What a treat it was to have the opportunity to tell the 1,000-person audience of investment professionals about the wonderful people who constitute this dedicated association of individual investors and the sound investment strategies that they both employ and propagate.

The annual Bogleheads gatherings have continued to attract passionate investors to reconnect with friends old and new, to hear speeches from investment professionals, and, of course, to meet with their namesake. The conferences have been held all over the country—in Las Vegas, Washington, DC, San Diego, and Dallas/Ft. Worth. In recent years, the Bogleheads have held their annual conference in Valley Forge, Pennsylvania, where Vanguard’s headquarters is located.

THE BOGLEHEADS MESSAGE

The Bogleheads’ Guide to Investing is a wonderful, witty, and wise book. As an investor for my entire adult lifetime, I found most rewarding the sage understanding of Messrs. Larimore, Lindauer, and LeBoeuf that the practice of investing is, as they put it, “so different from most of life.” Why?

Largely because our financial markets are essentially closed systems in which an advantage garnered by a given investor comes at the disadvantage of the other investors in the same market. The authors recognize this eternal truth: As a group, we investors are inevitably average, so beating the market is a zero-sum game. (After our investment costs are deducted, of course, it becomes a loser's game.) Importantly, they note that relying on the typical common sense approaches that apply to most of life's challenges is "destined to leave you poorer." For example, they warn against following life principles like these:

- If you don't know how to do something . . . hire an expert.
- You get what you pay for.
- If there's a crisis, take action!
- The best predictor of future performance is past performance.

In short, the principles that work in most aspects of our daily lives simply lead to failure in investing. Understanding that contrarian wisdom is the first step toward investment success.

But if that warning is both precisely accurate and grandly counterintuitive, the basic thrust of *The Bogleheads' Guide to Investing* is both precisely accurate and grandly intuitive. "Choose a sound financial lifestyle. Start early and invest regularly. Know what you're buying. Preserve your buying power. Keep costs and taxes low. Diversify your stock portfolio [and diversify your stock risk with a bond portfolio]." Investors who follow these simple tenets will earn their fair share of whatever returns the financial markets are kind enough to deliver in the years ahead.

THE BOGLEHEADS AND BENJAMIN FRANKLIN

When I completed my perusal of *The Bogleheads' Guide to Investing*, I had a certain sense of déjà vu. For I suddenly realized that I'd only recently seen a similar collection of sound, simple, and successful ways to save and invest that were written 250 years earlier, suggesting that these precepts may be not only effective, but eternal. They were expressed, as it happens, by Benjamin Franklin in 1757, in his widely circulated pamphlet *The Way to Wealth* (also entitled *The Art of Making Money Plenty*, or *Father Abraham Speaks*), republished in 2002 by the American Philosophical Society:

- If you would be wealthy, think of Saving as well as Getting.
- He that lives upon Hope will die fasting.
- There are no Gains, without Pains.

- He that hath a Trade hath an Estate.
- Taxes are indeed very heavy (but) we are taxed twice as much by our Idleness, three times as much by our Pride, and four times as much by our Folly.
- Beware of little Expences; a small Leak will sink a great Ship.
- Learning is to the Studious, and Riches to the Careful.
- If you would have a faithful Servant, serve yourself.
- Always taking out of the Meal-tub, and never putting in, soon comes to the bottom.
- Great Estates may venture more, but little Boats should keep near shore.
- For Age and Want, save while you may; no Morning Sun lasts a whole Day.

In all, Franklin's legacy matches the legacy of the Bogleheads, "a doctrine, my friends, of Reason and Wisdom . . . and Frugality and Prudence, though excellent Things. Ask God's blessing humbly and be not uncharitable to those who seem to want it, but comfort and help them . . . What is the noblest question in the world? 'What good may I do in it?'" Again using the words Franklin chose, the members of this investment association have "dedicated themselves to assuming the obligations of virtue and of serving others."

WHAT'S A BOGLE TO THINK ABOUT THE BOGLEHEADS?

Put yourself, for a moment, dear readers, in my position. How would *you* feel if an association of American citizens named themselves "(insert your last name here) -heads"? It would all depend—wouldn't it?—on their character, their values, and the extent to which their intellectual and moral principles coincided with your own. Here, the Bogleheads gain high scores, espousing the investment strategies and human values to which I've dedicated my entire career. More than that, just as Alexis de Tocqueville suggested, they have "taken up an opinion . . . they wish to promote, they look for mutual assistance, and as soon as they have found one another out they combine . . . influencing one another with opinions recruited, the heart enlarged, the human mind developed."

So, of course I'm honored and of course I'm pleased, not only with the endorsement and friendship of this stellar group of followers who have named themselves after me and adopted my principles. The final objective of my career—in investing, in management, in entrepreneurship, and in public service—is to depart this world with my reputation

intact. (But not too soon!) And so I confess that, yes, I'm filled with pride at how my life's mission has found burgeoning acceptance, not only among the Bogleheads but among millions of honest-to-God, down-to-earth human beings who deserve a fair shake in their efforts to achieve financial security for their families.

Pride, of course, is hardly an unmixed blessing, and I realize that it is a trait of character to be handled with care. Here is how Benjamin Franklin wisely expressed it:

In reality, there is, perhaps, no one of our natural passions so hard to subdue as pride. Disguise it, struggle with it, beat it down, stifle it, mortify it as much as one pleases, it is still alive, and will every now and then peep out and show itself; you will see it perhaps often in my history; for even if I could conceive that I had completely overcome it, I should probably be proud of my humility.

If, in the history I have recounted today, I have allowed my own pride to peep out and show itself, I assure you that it is with great humility that I accept the honor that this association of Bogleheads has paid to this particular Bogle by their choice of name, by their enthusiastic endorsement of my principles and values, and by their dedication in this wonderful book. Take heed of its guidance, and you will enjoy investment success.

John C. Bogle
Valley Forge, Pennsylvania
June 2014

Introduction

Do not value money for any more nor any less than its worth; it is a good servant but a bad master.

—Alexander Dumas fils, *Camille*, 1852

Contrary to what you may believe, a Boglehead is not one of those funny little dolls you occasionally see bouncing in the back window of a car in front of you. That's a bobblehead.

Bogleheads are an entirely different animal. While less visible than bobbleheads, our legions number in the millions. We are investors who follow the philosophy and strategy of investing advocated by John C. “Jack” Bogle, founder of The Vanguard Group.

MEET OUR LEADER

What Jack Bogle has made possible for the individual investor is truly extraordinary. Thanks to his creation of no-load, low-cost, tax-efficient mutual funds, millions of investors enjoy significantly greater returns on their investment dollars than they otherwise would have. His introduction of the first index fund for retail investors was labeled *Bogle's Folly* by its detractors. Today, that same fund, Vanguard's 500 Index fund, is the largest mutual fund in the world. Thanks to Jack Bogle, more of each investor's money is put to work for them instead of going into the pockets of brokers, fund managers, or the taxman. For the everyday investor this translates into items such as nicer homes for families, college educations for children, more enjoyable retirements for seniors, and more money to be passed on to loved ones and causes they care about. Although a few other investment fund families have joined the low-cost revolution, it was Jack Bogle who sounded the bugle and led the charge, and it's Vanguard that continues to lead the way.

You may think that such an enormous lifetime contribution is enough for one man, but Jack Bogle is no ordinary man. Since stepping

down as chairman of The Vanguard Group for a heart transplant in 1996, Jack Bogle has devoted his life to educating investors on how to get a greater return on their investment dollars. Moreover, his teachings simplify investing, making it very easy for the average person with no financial background to understand. His books, *Bogle on Mutual Funds*, *Common Sense on Mutual Funds*, and many others are classics.

In addition to creating a great family of mutual funds and teaching others how to invest efficiently and effectively, Jack Bogle is a tireless advocate for the individual investor. It's common to see him speaking to professional groups, at commencements, or being interviewed on radio and television. His editorials frequently appear in the *Wall Street Journal*. His messages to the investment community are always consistent: Give investors a "fair shake" for their money, tell them the truth, and remember that character counts. He has fittingly been labeled "the conscience of the industry." His honors are too numerous to mention, but they include being selected as one of *Time* magazine's "100 Heroes and Icons Who Shape Our Lives" in 2004. When Thomas Jefferson remarked, "One man with courage is a majority," he could have been speaking about Jack Bogle.

MEET THE BOGLEHEADS

Thanks to Morningstar, an investment research firm in Chicago, a meeting place was created in 1998 where Bogleheads throughout the world can meet, discuss investment ideas, and help each other. As you might suspect, we meet in cyberspace. This Bogleheads Forum can be accessed via www.bogleheads.org. Thanks to the work of Bogleheads Alex Frakt and Larry Auton, the [bogleheads.org](http://www.bogleheads.org) website is a place where you can see a list linking to the most recent conversations, learn more about the Bogleheads, and find answers to frequently asked questions. Participation is open to the public. You can read conversations and post on the Bogleheads Investment Forum at no cost.

At the risk of appearing immodest, we believe the Bogleheads Forum is the best investment forum in cyberspace. The site gets more than a million hits per day. Our members include some of the best investment planners, authors, and minds in the business. Post a question and you will likely get an answer from one or more of them. Better yet, you will get an honest, unbiased answer from someone with no hidden sales agenda. Our forum frowns heavily on persons who attempt to troll for business, and commercial posts are quickly deleted. Our members range in age from 12 and up, and we range in wealth and experience from

beginning investors just starting out to experienced investors with multimillion-dollar portfolios.

Boglehead meetings don't begin and end in cyberspace. Starting in 2000, there have been annual reunions where all Bogleheads are invited to meet and greet each other in person. Jack Bogle attended every reunion with the exception of one (he was in the hospital). He generously shares his time with us, gets to know us as individuals, and answers our investing questions. All of these national events were smash hits, and we continue to hold an annual get-together.

In addition, local Boglehead chapters are popping up in cities and regions throughout the country as well as in Europe and Asia. Local chapters provide an opportunity for Bogleheads to meet face-to-face, enjoy a meal together, and discuss investing. The national Bogleheads Conferences and Local Chapter meetings are a microcosm of the USA—a very diverse but very nice group of people who come to learn, share what they know, and help others.

ABOUT THE BOGLEHEADS' GUIDE

We wrote this guide to give you a taste of the Boglehead approach to investing. We know it will enable you to become a better investor and manager of your own financial resources. We assume no financial knowledge on your part. In fact, knowing nothing about investing might be a benefit. You won't have to unlearn many popular beliefs propagated by Wall Street and the media that aren't true.

The three of us combined have well over a century of investing experience. Through trial and error, we each independently adopted the Boglehead approach to investing for one simple reason: It has given each of us the best, after-tax return with the least risk on our investment dollars. It's that simple.

Several key topics are covered in this book:

- How to get on a sound financial footing before you start investing
- What the various types of investments actually are
- How to protect your investments against the ravages of inflation
- How to determine how much you need to save
- Steps to building a simple but effective investment portfolio
- Excellent ways to save for college
- How to not let a windfall slip through your fingers
- How to decide if you need a financial advisor, and how to choose one if you do

- How to determine when to rebalance your portfolio, and how to do it
- How to identify and tune out the noise from Wall Street and the media that's designed to benefit them and not you
- How investors' emotions can be their own worst enemy, and how to keep them from ruining your nest egg
- Steps to take to prevent financial catastrophes
- How to live a comfortable retirement without running out of money
- How to pass assets on efficiently to your heirs
- How to keep your investing style simple, giving you more time to live your life to the fullest

We have no hidden agendas. We aren't financial planners or money managers looking for clients. We don't have a high-powered, get-rich-quick weekend seminar to sell you. We are all well over 70 years of age, financially secure, and haven't missed a meal yet. If you want to read the book at the bookstore, the library, or borrow it from a friend, that's fine with us. Our primary mission is simply to support Jack Bogle's mission by teaching others how to get the best long-term return on their investment dollars.

We also have a secondary mission. We hope this book will encourage you to join the legions of Boglehead investors online. Drop-in and say hi at www.bogleheads.org. Post any questions you may have, and share with us what you've learned about investing. We are all there to learn, to help, and to enjoy the friendship of the Bogleheads. Welcome!

Taylor Larimore
Mel Lindauer
Michael LeBoeuf

PART I



ESSENTIALS OF SUCCESSFUL INVESTING

