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New Perspectives for the Intelligent Investor

JOHN C. BOGLE

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BOGLE ON MUTUAL FUNDS

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BOGLE ON MUTUAL FUNDS

New Perspectives for the Intelligent Investor

John C. Bogle

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Dedication

To my parents, for setting my values.
To my brothers, for their sacrifices.
To Eve, my beloved wife, for her devotion, patience, and support.
To my children, for their understanding and pride.

2015 Introduction to the Classic Edition of *Bogle on Mutual Funds: New Perspectives for the Intelligent Investor*

How *Bogle on Mutual Funds* Became a Classic

PERSISTENCE AND PUBLICATION

The very existence of *Bogle on Mutual Funds: New Perspectives for the Intelligent Investor* depended largely on some remarkable persistence, first by Amy Hollands, then senior editor for Irwin Professional Publishing (later part of McGraw-Hill Publishing). Amy stopped in at my Valley Forge office in November 1990 and told me that Irwin was eager to publish a book aimed at helping mutual fund investors achieve their financial goals. Based on her numerous high-level contacts around the financial community, she reported that almost every person with whom she discussed the need for a solid book on mutual funds had suggested that I should be the author.

"Thanks Amy, but maybe later," I told her. For at that time I was quite overwhelmed with the task of building Vanguard—the fund complex that I had founded in 1974, beginning with some $1.4 billion of investor assets—and managing the explosive growth that would carry our assets to more than $100 billion by 1993. At that time, we had just begun to emerge as an industry leader, and cash flow from net investments by shareholders had been growing at an amazing 20% annual rate for a decade. "I'd love to do it. And I know that I can do it," I told her, "but right now I can't possibly find the time to write a book."

So, Amy came back a year later with the same plea. And then again a year after that. When she dropped by in the spring of 1992, however, my schedule had eased (a bit!). At the same time, the serious heart problems that I had been plagued with since 1960, alleviated by the care of my fabulous cardiologist Dr. Bernard Lown, began to return. While

I'm generally not much of a worrier, I did begin to wonder about how much time I had remaining on this earth.

So, I told Amy, "Maybe it's now or never. I'll write the book." I began the task on Labor Day 1992, seated at the desk in my den at our family retreat in the Adirondacks. I wrote the preface, and the outline of my work fell quickly into place:

Part I. BUILDING BLOCKS—three chapters on the rewards and risks of investing, and on the principles, practicalities, and performance of mutual funds.

Part II. MUTUAL FUND SELECTION—four chapters covering how to select a stock fund, a bond fund, a money market fund, and a balanced fund, plus a fifth chapter describing reliable sources of fund information.

Part III. NEW PERSPECTIVES ON THREE KEY ISSUES—one chapter each on emerging issues in mutual fund investing: index funds, fund costs, and tax considerations. (Yes, up until 1992, these issues had rarely been explored in the investment literature.)

Part IV—PRACTICAL APPLICATION OF INVESTMENT PRINCIPLES—three chapters, one on asset allocation, one providing model portfolios for various types of investors, and the final chapter, "A Mandate for Fund Shareholders," describing the pitfalls that the fund industry had created for its shareholders.

I closed with an Epilogue—TWELVE PILLARS OF WISDOM—setting forth what I regarded as a dozen eternal principles of sound investing, principles that would enable investors to avoid the many challenges facing mutual fund investors, presented with a sort-of-philosophical theme.

OPPORTUNE TIMING, POWERFUL ENDORSEMENTS

Now my own persistence came into play. Over the ensuing six months, I spent the lion's share of my free time writing and—with the help of a handful of friends who were experts—editing my work. It was published in September 1993. The timing was opportune.

First, thanks to strong markets in stocks and bonds, the mutual fund industry was about to enjoy a remarkable surge in growth. Industry assets under management were to leap eight-fold, from $2 trillion in 1993 to $16 trillion as 2015 begins. During that same period, fund assets under Vanguard's aegis have grown 25-fold—three times as fast as the industry—from $125 billion to $3 trillion. (Yes, Vanguard's asset base is now 50% larger than the entire industry when I wrote that first book more than two decades ago.)

Earlier in 1993, I had asked a few highly respected financial leaders to review the press proofs of *Bogle on Mutual Funds.* Their endorsements left me in a state of shocked delight.

From Warren Buffett, Chairman of Berkshire Hathaway:

> **"This is the definitive book on mutual funds—comprehensive, insightful, and—most important—honest. Any investor who owns or is thinking of owning shares in a fund should read this book from cover to cover."**

From the late Peter L. Bernstein, Editor of *The Journal of Portfolio Management* and author:

> **"This book sets the ultimate benchmark for all how-to-invest books. I would choose it even over Benjamin Graham's *The Intelligent Investor*. Everyone who reads it—from the hard-bitten professional to the wide-eyed amateur—will one day be richer than they would have been if they had never read it."**

From Don Phillips, Publisher of Morningstar Mutual Funds:

> **"A long-time student of the fund industry, Bogle is both its harshest critic and its greatest friend. He is, in effect, the conscience of the industry, constantly reminding his compatriots that fund companies must always put investors' interests first. Bogle gives individual investors the necessary tools to forge an intelligent, long-term investment plan. *Caveat Emptor*: Don't buy another fund until you read this book."**

Even more remarkable was the reaction of the late Paul Samuelson, Nobel Laureate in Economic Sciences. After he read my manuscript, he telephoned me and said, "You know, John, the coin of the blurb has been greatly devalued. So, instead of a blurb, I'd like to write the foreword." And so he did. Some excerpts:

> **". . . 99 out of 100 books written on personal finance should carry the label . . . 'warning, this product may be dangerous to your health.' The exceptions are rare. Benjamin Graham's *The Intelligent Investor* is one. Now it is high praise when I endorse *Bogle on Mutual Funds* as another."**

> **"John Bogle has added a new note in connection with his emphasis upon low-cost, no-load investing. I have no association with The Vanguard Group of funds other than as a charter member investor, along with numerous children and innumerable grandchildren . . . As a disinterested witness in the court of opinion, perhaps my seconding his suggestions will carry some weight. John Bogle has changed a basic industry in the optimal direction. Of very few can this be said."**

Thanks in part to that "Murderer's Row" of endorsements, along with a near-unanimous positive appraisal from reviewers and readers, *Bogle on Mutual Funds* quickly became a best-seller. Over the next five years, some 250,000 hard-cover copies were purchased by investors, plus another 40,000 copies in a later paperback edition.

Fortune Book Club named *Bogle on Mutual Funds* as its selection for Winter 1994. And *Money* magazine published excerpts, noting that, "John Bogle bestrides mutual funds like the leader of no other industry. He is not only its Henry Ford—the price-cutting apostle of prudence. He is its Ralph Nader, the inveterate scourge."

The volume of book purchases was strong, but grew gradually, so there was no way to make *The New York Times* best-seller list. But for two years, *Bogle on Mutual Funds* was the best-seller (as chronicled by *The Philadelphia Inquirer)* among all business books in the Greater Philadelphia area. Comments on the Amazon and Barnes and Noble websites—just beginning then—were frequent (for those days) and the book received a five-star review by nearly every reader, from Aurora, IL, to New Zealand. These headlines from the reviews tell the story:

> **"The" Resource for Mutual Funds . . . Bible of mutual fund investing . . . The BEST mutual fund book you can buy . . . Superb book . . . American hero . . . Brilliant and very readable . . . The real story on investment . . . Teaches you how to think about investing . . . A truly brilliant read . . . Insightful and comprehensive . . . The best book on investing I've found . . . Awesome . . . No wonder so many admirers refer to the beloved Mr. Bogle as, "Saint Jack."**[1]

I also received scores of complimentary letters from the investment professionals, and even from other writers. Four examples are presented as Exhibit I.

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[1]One exception: A reader who rated the book at only three stars, added this comment: "Bogle has useful ideas. Like most MBAs, he does not know how to use mathematics or logic to come to empirical conclusions." (Confession: I'm not an MBA.)

EXHIBIT I

Darwin M. Bayston, former President and CEO of the Association for Investment Management and Research (now CFA Institute):

When Amy Hollands asked my opinion about the type of book that would help investors, there was no doubt in my mind what a "home run" it should be and who should write it! I told Amy to come to Valley Forge, camp on your door, and not leave until you agreed to do it. She did, and you did. Sometimes it works.

Jack, you hit a home run! History will record its immeasurable value to the investing public, and to those who are counseling both personal and pension money. For your lifetime of wisdom, wit, and experience to have gone unrecorded would have been a tragedy. THANKS! Forget being humble and take great pride in the enormous contribution you have made.

David P. Eastburn, Chairman of Vanguard's Independent Director Group:

My reaction to your book is one of great surprise. You, sir, are a scholar. Looking back I can recognize some glimmerings of this fact. But assembled together, the accumulated knowledge and wisdom really shines forth. As one who aspires to, but never achieves, this state of being, I recognize it when I see it . . . It's easy to see that this is vintage Bogle; not necessarily the Bogle the media likes to exploit, but the guy with a mission. Congratulations!

Allen R. Myerson, *New York Times* Investing columnist:

Jack Bogle's book, scheduled for release in October from Irwin Professional Publishing, invites three different readings: as advice, as a statement of company philosophy, or as autobiography. Most readers will, appropriately, approach the book as a how to. They will soon discover it is as much a how not to. Mr. Bogle sees vast, arid stretches with tightly spaced land mines separating investors from their nourishment. He doubts whether even longer-term records are of much use: "Does comparing relative returns among generally similar funds over extended periods suggest skilled portfolio managers can be identified in advance? The answer seems clear: No." His solution, presented at some length, is the index fund, passively run at minimal expense to track a market benchmark.

> **He stops well short of making his book solely an advertisement for the Vanguard approach, but he clearly believes there is no other way to run a group of mutual funds. In both tone and substance, his book is also a sort of autobiography. Obviously well read—too obviously, perhaps—he documents his points for someone equally sharp and skeptical. His publishers, standing up for the morons among, initially wanted an elementary guide. "If you want a primer," Mr. Bogle said, "get someone else."**
>
> **Michael Lipper, who runs a mutual fund data service, suggested that Mr. Bogle write a book titled "How to Get Rich in 20 Minutes." Fortunately, he didn't.**

John McPhee, Professor of Writing at Princeton University, best-selling author, and Pulitzer Prize winner:

> **I have read every syllable of *Bogle on Mutual Funds*. Your response to the question of writing difficulties was spoken like every thesis-writing senior. Spoken like every ink-stained writing wretch who is not self-deluded. It is easier to shinny up a mile-high pole than to complete a piece of writing. Or so it seems. You got up there, though. This book is written with wonderful clarity. It is patient with the untutored but never condescending. The boxes (*caveat emptor*) work especially well. There's a sense of discovery in coming upon them. Structurally, they serve to aerate the whole.**

What's more, the message of *Bogle on Mutual Funds*, especially those then-obscure "New Perspectives" that I championed—Indexing, Low Costs, and Tax-Efficiency—took on a life of their own, gaining almost universal recognition as essential considerations in developing a successful investment program.

A PERSPECTIVE ON *BOGLE ON MUTUAL FUNDS*

Read today, *Bogle on Mutual Funds* likely strikes one as sort of "old hat." Why? Because almost everything that I predicted two-plus decades ago has not only come to pass, but has become the conventional wisdom. In fact, reliance on those three new perspectives, rarely considered in 1993, has reshaped the way that fund shareholders invest their hard-earned dollars.

Perspective One. Index Funds

In my first "New Perspective"—on index funds—I concluded with this sentence: "It is easy to forecast, with some confidence, continued growth and increased market penetration for mutual fund indexing." And so it came to pass. When I wrote those words in 1993, assets of index mutual funds totaled $125 billion, representing only four percent of the assets of equity mutual funds. As 2015 begins, assets of index funds had soared to more than $4 *trillion*, and account for an astonishing 33 percent of the assets of all equity funds. (An estimated 12 percent of all assets of private and public pension funds are also now indexed.)

Even 22 years ago I was using the same words as I do today to describe the certainty of index superiority:

> **The complex formulation of what has become known as modern portfolio theory can be reduced to two obvious facts:**
>
> 1. **Since all investors collectively own the entire stock market, if passive investors—holding all stocks, forever—can match the gross return of the stock market, then active investors, as a group, can do no better. They too must match the gross return of the stock market.**
> 2. **Since the management fees and transaction costs incurred by passive investors are substantially lower than those incurred by active investors, and both provide equal gross returns, then passive investors must earn the higher net returns.**
>
> **As the logicians would say: QED. It is proven.**

Extending that simple arithmetic from the annual returns on stocks over a lifetime—the most relevant time frame for the intelligent investor. "The magic of compounding returns, absent the tyranny of compounding the heavy costs of fund investing," as I have so often said, is the optimal formula for wealth accumulation. As Stanford Professor and Nobel Laureate William F. Sharpe wrote in his 2013 paper, "The Arithmetic of Investment Expenses," for the *Financial Analysts Journal*, ". . .

it is more important than ever for investors to understand the possible impact of investment expenses on future wealth."[2]

In my perspective on index funds, I didn't then mention ETFs (exchange-traded funds), which were introduced in mid-1993. This new type of mutual fund would enable investors to trade index funds "all day long in real time." In 1992, I had been presented with the opportunity to join in forming the first ETF, but I summarily turned it down. Why? My conviction was (and is) that index funds are designed to attract long-term *investors*, not short term *speculators* such as traders. While ETFs have now become the "hot new product" of financial marketers, my perspective remains unchanged. *Trading stocks is a counterproductive investment strategy.*

Perspective Two. Fund Costs

My second New Perspective raised the issue of fund costs, a subject that was then almost totally ignored in the academic literature and by the press. Then, I used fund expense ratios as the measure of fund costs, even as I was well aware that sales loads, portfolio turnover costs, and the drag of low-yielding cash positions of most funds would also reduce the long-term returns that funds delivered to their shareholders.

My focus included not only the heavy toll that fund costs extract from the total returns earned by fund investors over the long term, but the high percentage (then 30 percent or more) of the gross investment *income* that fund costs consume. Today, with yields much lower than in 1993, such confiscation can easily reach 50%, often 100% of income. (Think of a 1 percent expense ratio on a fund deducted from its gross dividend yield of 2 percent.) Sadly, this latter perspective remains "new" to this day.

Yet low-cost funds have now come to dominate fund industry cash flows. While the low-cost quartile of mutual funds represents slightly

[2]Dr. Sharpe estimated that by investing in a total U.S. stock market index fund instead of an actively managed fund with far higher costs, "most investors . . . [could] look forward to having the funds saved for their retirement provide 20% more purchasing power." A year later, in early 2014, I wrote my own paper for the *Financial Analysts Journal*, expanding on his calculations to include "all-in" fund expenses. I concluded that the enhancement of retirement capital could be as high as 70%. Dr. Sharpe applauded my paper.

less than one-half (48%) of the *assets*, it has accounted for 93 percent of industry *cash flow* during the past five years, and 95 percent in 2014. Yes, index funds account for substantially all of this cash flow, but the trend is clear.

Remarkably, however, the general level of fund expense ratios remains excessive. The expenses of the average actively managed fund in 2014 came to a heavy 1.35 percent of fund assets. Although many index funds are available at annual expense ratios of 0.05 percent to 0.10 percent, the average remains an excessive 0.57 percent. We have a long way to go in driving costs down to reasonable levels for investors.

Perspective Three. Taxes

My third New Perspective was on another return-reducing factor that harms fund investors. With their high portfolio turnover, the vast majority of equity funds are highly tax-*inefficient*, generating gains that, while they escape taxes at the *fund* level, subject the fund investor to unnecessary taxes, often at high tax rates applicable to short-term capital gains. In this perspective, I also offer numerous ways for investors to obtain high levels of tax-efficiency, including tax-efficient mutual funds, qualified retirement plans such as IRAs, and municipal bond funds. The Roth IRA, available since 1998, later became a valuable tool to further reduce taxes on retirement plans.

After two decades of observation, that third New Perspective has proved itself. The importance of tax-efficiency in fund investing alone is vital. But combined with cost-efficiency, its impact is far too powerful to overlook. For example, during the decade ended December 31, 2014 (according to Morningstar data), the after-cost, after-tax annual return of the Vanguard (S&P) 500 Index Fund came to 7.3 percent, compared to 5.9 percent for the average active equity fund, a shortfall largely caused by those punitive costs.

Compounded, this seemingly small difference in annual advantage becomes a miracle. Over 50 years (far short of an investment lifetime for today's millennials), $100 compounded at that 5.9 percent annual return would grow to $1,757. That same $100 compounded at 7.3 percent would grow to $3,310. Almost doubling the value of an investor's retirement plan is not to be sneezed at!

THE PRACTICAL APPLICATION OF SOUND PRINCIPLES

Having strongly expressed my investment principles and strategic convictions in the book's first eleven chapters, *Bogle on Mutual Funds* concluded with Part IV, including three chapters on how investors should apply these concepts in their own portfolios. Now, it was time "to get down to brass tacks" with my readers, and help them deal with the critical issue of asset allocation, the most vital decision to be made by any investor. How much in stocks? How much in bonds?

The asset allocation for each investor—depending on your investment objectives, income requirements, risk tolerance, financial situation, age, and a multiplicity of other lesser factors—comes down to one surprisingly complex question: How much in stocks? The remainder should be in bonds. Just those two investment classes. I believe that precious few investors should rely on more complex (and usually more speculative) asset classes such as commodities (gold, etc.), derivatives, art, and so on. My recommendations centered on a 70/30 to 60/40 stock/bond portfolio. (As it happens, this range is significantly more stock-oriented than the 50/50 ratio generally espoused by Benjamin Graham in *The Intelligent Investor.*)

Should we reconsider today the allocations that I recommended in 1993? After all, market conditions have changed dramatically. In 1993, stocks carried a dividend yield of 2.7 percent, and the interest yield on the 10-year Treasury bond was 6.8 percent. As 2015 begins, the yield on stocks was 2.0 percent, and the yield on Treasury bonds almost 2 percent, virtually identical. (Neither very generous, and both well below historical norms.) But we have to accept the markets we are given, not the markets we might choose. So, assuming only that your course remains sound, I'd "stay the course" with those original asset allocation guidelines, for bonds remain an anchor to windward in times of stock market adversity.

I also presented model portfolios for investors at various phases of their life cycle: the accumulation investor; the transition investor moving from the accumulation phase (putting money *in*) to the distribution phase (taking money *out*); the lump-sum investor; the pension fund investor; and endowment fund investor. Two decades later, I stand pat on the composition of these model portfolios—more (I hope!) because they still make sense than because of my stubbornness.

If I were to change any aspect of the model portfolios that I presented in 1993, it would be a greater use of stock and bond *index* funds in each portfolio. I mentioned this idea tangentially in my book:

> **Index funds. The stock fund position of every investment program I describe could just as easily be supported solely by holding one or more stock market index funds, and the bond fund position could in each case be supported by a core holding in a bond index fund (providing a combination of long-term, intermediate-term, and short-term bonds). That such a program would enhance total return is suggested by historical data, but is by no means guaranteed; that it would provide markedly higher income without any increase in risk is beyond debate.**

"A Mandate for Mutual Fund Shareholders"

In my final, fourteenth chapter, I moved into uncharted (and contentious!) waters. In "A Mandate for Fund Shareholders," I discussed what I saw as profound flaws in the structure of the mutual fund industry, and how those flaws have harmed the interests of the investors whom they are duty-bound to serve. How did this happen? I explained why:

> **"The fault, dear Brutus, is not in our stars, but in ourselves." So said the protagonist in Shakespeare's play *Julius Caesar*. Most of this book has described how the mutual fund industry works today. But this industry can be greatly improved and can provide far better opportunities for investors. Positive change will take place, however, only if we lay the responsibility for the industry's shortcomings not in our stars but in ourselves as shareholders. If enough investors demand a better mutual fund industry, we will have a better mutual fund industry.**

I first urged fund investors to be "**canny**—wise enough to rely on their own common sense and good judgment . . . The problem is that investors have largely demanded the *wrong* things and have for the most part ignored the right things. So any industry improvement depends first on a change in investors' attitudes—acting wisely and carefully in the selection and ownership of mutual fund shares." Investors must understand the hard realities of investing and act accordingly.

Next, I urged fund investors to be **thrifty.** Yes, of course, to save as much as they possibly can for their future needs. But, equally important, to make those savings earn higher returns by simply demanding that their mutual fund managers be thrifty with the money we entrust to them, to "become more cognizant of the costs [we] are paying in the form of sales loads, management fees, and other fund expenses. If we act on this awareness, these costs will surely decline. It is as simple as that. If you purchase only the shares of the low-cost funds, mutual fund sponsors will quickly get the message."

Then, I asked investors to be **active**, exercising their rights to "vote fund proxies . . . to express their opinions to management, and finally . . . the right to 'vote with your feet' and redeem your investment in the fund . . . the ultimate weapon." I also enumerated some of the areas that should concern fund investors—excessive management fees, sales loads, 12(b)-1 distribution plans that lay extra marketing costs on shareholders, the failure of fund CEOs to provide a candid explanation of fund returns in annual reports. Why their failure? Because, "in the typical case, the CEO of the fund—responsible for *appraising* the results—is also the CEO of the investment adviser—responsible for *generating* the results. As a result, reporting to shareholders with candor is no mean challenge."

I then urged the investor to be **skeptical**. In particular, skeptical of advertising that exaggerates the importance of a fund's past performance (the past is rarely prologue to the future); of focusing on bond fund yields while ignoring portfolio quality; and in developing new fund concepts that are based on unproven or untested new principles. My conclusion: "If it is called a 'new product,' particularly if it is called a '*hot* new product,' do not invest in it."

BUILDING A NEW INDUSTRY

Before I turned to "Building a New Mutual Fund Industry," the final section of the final chapter, I discussed the tendency of fund "independent directors" to protect the management company that (directly or indirectly) appoints them, rather than to protect the fund shareholders to whom these directors have a fiduciary duty. Alas, I hadn't yet seen Warren Buffett's aphorism that so-called independent directors are supposed to behave "as Dobermans," but instead behaved as "cocker spaniels with their tails wagging." That contrast got my point across more vividly than even the strong language I used in the critique in my book.

My closing critique of the fund industry was impassioned, even revolutionary:

> **The very structure of the mutual fund industry must change, essentially placing the fund in the driver's seat and relegating the management company to the back seat. From a mutual fund [managers'] standpoint, that indeed would be the world turned upside down. But it would be the functional counterpart of the time-honored structure of the ordinary business corporation, in which the owners of the corporation (in this case, the fund shareholders) control, through their board of directors, its affairs. Ordinary corporations do not need to go out and hire other corporations, with separate owners, to manage their affairs. Mutual funds do precisely that today. Some combination of shareholder demand, enlightened self-interest, competition in the marketplace, and more sweeping steps under the law may someday compel a reversal.**

"THE TWELVE PILLARS OF WISDOM"

My epilogue was entitled, "The Twelve Pillars of Wisdom." Even after the passage of 22 years, I would endorse every one of these dozen humble principles—including reliance on simplicity, reversion to the mean in fund returns, the futility of "fighting the last war," thinking long-term, and (of course!) "staying the course." But among those dozen pillars of wisdom, it strikes me that this one may well be the most relevant as 2015 begins:

> **You rarely, if ever, know something the market does not. It is really not possible to do so. If you are worried about the coming bear market, excited about the coming bull market, fearful about the prospect of war, or concerned about the economy, the election, or indeed the state of mankind, in all probability your opinions are already reflected in the market. The financial markets reflect the knowledge, the hopes, the fears, even the greed, of all investors everywhere. It is nearly always unwise to act on insights that you think are your own but are in fact shared by millions of others.**

Even as I opened my epilogue into a quote taken from the Holy Bible—"Wisdom excelleth folly as far as light excelleth darkness," from

Ecclesiastes 2:13, I closed it with my favorite quote, from Ecclesiastes 9:11:

> **I returned, and saw under the sun, that the race is not to the swift, nor the battle to the strong, neither yet bread to the wise, nor yet riches to men of understanding, nor yet favor to men of skill; but time and chance happeneth to them all.**

REFLECTIONS ON WHAT MAKES A "CLASSIC"

As I complete this review of *Bogle on Mutual Funds: New Perspectives for the Intelligent Investor*, the big question that crosses my mind is: "What marks a book on investment a classic?" The answer must be something like this:

To achieve "classic" status, a book must espouse sound principles and sound advice that have met the test of time and have endured through a wide variety of conditions in the financial markets. Positive endorsements by respected experts begin a classic's journey through time, and strong reader support is another vital element. The book also *ought* to be well-written, and comprehensible to the audience to whom it is directed.

Singularity also gives a big boost to the achievement of classic status. What might distinguish such a book? Perhaps substantial data—simply presented—that reinforces the message. Perhaps an unusual typographical treatment, one that breaks up the otherwise unrelieved monotony of standardized text. Moving off the beaten track and providing information that surprises the reader is also a plus, and contrarian views that dispute the conventional wisdom of the day (assuming that those views are later validated), often provide the determining factors in earning classic status.

The Classics

As appropriate, not very many investment books meet these standards of a classic. But it's easy to pick a few whose status would be hard to challenge: *Security Analysis* by Benjamin Graham and David Dodd (1934); *The Intelligent Investor* by Graham (1949, although I happen to believe that the 1973 edition, edited by Warren Buffett, is far more useful to today's investor); *Margin of Safety* by Seth Klarman (1991). It now sells for $3,997.95 on Amazon—a good sign. Keep the change!

Other candidates include Peter Bernstein's *Against the Gods: The Remarkable Story of Risk* (1998), James Grant's *Money of the Mind* (1992), Burton Malkiel's *A Random Walk Down Wall Street* (1973, now in its eleventh edition), William Bernstein's *The Four Pillars of Investing* (2002), and David Swensen's *Unconventional Success: A Fundamental Approach to Personal Investment* (2005). Perhaps with the passage of time, a few other investment books will also meet the challenge and will become classics.

I take some comfort from the fact that Paul Samuelson—whose own book, *Economics: An Introductory Analysis*, now in its nineteenth(!) edition, is an economics classic—suggested that *Bogle on Mutual Funds* ranked right up there with *The Intelligent Investor.* Peter Bernstein characterized *Bogle on Mutual Funds* as "the ultimate benchmark for all how-to-invest books. I would choose it even over . . . *The Intelligent Investor*." These accolades surely suggest that, against all odds, and surely far beyond my highest initial expectations, my book has earned "classic" status.

Why? Thinking about the standards that I suggested above, it seems clear that the principles and practices that I expressed in 1993 have met the test of time, during an era of solid returns on stocks, albeit one that was interrupted by two bear markets (1999–2003 and 2007–2009), each producing a 50% drop in stock prices.

Tests that Define My Work

The test of excellent endorsements by respected experts has surely been met by *Bogle on Mutual Funds*, as noted above and at the start of this essay. And strong reader support has been powerful; not only great comments, but sustained comments over the years, most recently in September 2014. (It's called "legs.") Total sales volume has exceeded some 300,000 copies, surely among the top-selling investment books of all-time.

The quality of my writing in *Bogle on Mutual Funds* was adequate, maybe better than that. But after writing nine more books, one might expect to become better and better—better phrasing, better rhythms, better choice of words, and even more quotations from outside sources. (My use of the Holy Bible, *Ulysses*, Churchill, and Lincoln only begins the list.) The endorsement of my writing skills—such as they may be—from teachers of English is likely my greatest satisfaction.

The use of *Caveat Emptor* boxes (91 in all) throughout my book also made a favorable impression on readers. These boxes not only served a useful function in my narrative, but broke up the text as well. They were often pointed, acerbic, cynical, and sharply critical of the industry in which I have built my career, testifying to the independence of my thinking, and helping readers to gain confidence in my credibility and trustworthiness.

Finally, my forays in going off "the beaten track" had mixed results. Defining "duration" of a bond portfolio for lay readers was one such venture that helped (the *caveat emptor* on page 42). But taking "the path *un*traveled by" is risky, and my attempt to coin a new term for the "coefficient of determination" that relates a fund's returns to the stock market return was a flop. I didn't think that the technical term "R-squared" would be useful to the lay investor, and suggested "ExMark." That word has never again seen the light of day.

Coming Full Circle

What a joy it has been for me to take a retrospective look at my first book. Here I am, 22 years after I wrote *Bogle on Mutual Funds*, reveling in its simple structure; its sound advice that has clearly met the test of time; its endorsement by readers, from the brilliant and experienced to those hard-working citizens who may follow mundane, even thankless, careers but nonetheless have the gumption to put money away to ensure their families' long-term wealth. We're all, finally, in this game together, doing our best to cope with the demands of our daily lives. Investing sensibly and simply gives the honest-to-God, down-to-earth human beings of our citizenry a fair shake.

And as for me, I'm still here! Those 1993 worries about my heart—which continued on its downward path to failure during the subsequent three years—were put to rest by getting a heart transplant in 1996. That's some sort of a miracle! After 19 years, and on my way to 86 years of age in May 2015, what more can a man ask?

Bogle on Mutual Funds: New Perspectives for the Intelligent Investor was the first in a sequence of nine more "Bogle books" that followed. *Common Sense on Mutual Funds: New Imperatives for the Intelligent Investor,* first published in 1999 has proven to be a worthy successor and will itself likely become a classic.

That first edition featured a glowing (and perceptive) introduction by economist Peter L. Bernstein. (Perhaps you noted the intentional parallelism of "New Perspectives" and "New Imperatives.") A tenth anniversary edition was published in 2009 with the original text unedited, but included retrospective comments sprinkled throughout the book, along with updated data. David F. Swensen, long-time chief of Yale University's endowment fund, penned a new introduction, again glowing and perceptive.

The investment message that I sent in *New Perspectives* in 1993 was reaffirmed by *New Imperatives* in 1999, and reaffirmed again in its 2009 edition. That span represents almost a quarter century of consistent, objective, fact-founded advice. Who's really to deny that we may one day have another classic on our hands? We shall see.

Valley Forge, PA **John C. Bogle**
February 6, 2015

Foreword

The same surgeon general who required cigarette packages to say: "Warning, this product may be dangerous to your health" ought to require that 99 out of 100 books written on personal finance carry that same label. The exceptions are rare. Benjamin Graham's *The Intelligent Investor* is one. Now it is high praise when I endorse *Bogle on Mutual Funds* as another.

I do not speak for myself. What is one person's opinion worth? It is the statistical evidences of economic history that I speak for. Over half a century, professors of finance have studied various strategies for prudent investing. A jury of economists is never unanimous—how could it be in such an inexact science?—but on these lessons of experience there is a remarkable degree of agreement.

1. *Diversification* does reduce, but not eliminate, risk. Buying many stocks, critics say, is "settling for mediocrity." When I was a trustee on the finance committee of the largest private pension equity fund in the world—which handled the old-age savings of the whole university community—we had 30 billion reasons to look into this critique alleging mediocrity. We discovered that the hundreds of money managers who believe in putting only a few eggs in one basket and then "watching fiercely those eggs," alas, produce long-term investment returns that are significantly below those of diversified portfolios. No exceptions? Yes, a few; but a changing group, hard to identify in advance, and prone to regress toward the mean even before you can spot them.

2. For those not in the millionaire class, the need to diversify implies that the sensible and cost-efficient strategy is *not to handle personally* investments needed for those future days of retirement, of home purchases, and of sending offspring to college. "Leave the driving to Greyhound" is not counsel of cowardice and modesty. It's just plain good sense when you reckon the facts about brokerage commissions and the need to keep tax records. All this applies even if you will not go all the way toward "index investing," my next topic.

3. The most efficient way to diversify a stock portfolio is with a low-fee index fund. Statistically, a broadly based stock index fund will

outperform most actively managed equity portfolios. A thousand money managers all look about equally good or bad. Each expects to do 3% better than the mob. Each puts together a convincing story after the fact. Hardly ten of one thousand perform in a way that convinces a jury of experts that a long-term edge over indexing is likely. (For bond and money market portfolios, the canny investor will select among funds with high quality and lean costs.)

4. Enough said about the testimony of economic science. Where John Bogle has added a new note is in connection with his emphasis upon low-cost, no-load investing. I have no association with The Vanguard Group of funds other than as a charter member investor, along with numerous children and innumerable grandchildren. So, as a disinterested witness in the court of opinion, perhaps my seconding his suggestions will carry some weight. John Bogle has changed a basic industry in the optimal direction. Of very few can this be said.

May I add a personal finding? Investing sensibly, besides being remunerative, can still be fun.

Paul A. Samuelson
Institute Professor Emeritus
Cambridge, Massachusetts

June 1993

Acknowledgments

Two centuries ago, it was said that if we stand on the shoulders of giants, we may see further than the giants themselves. The principal giant upon whose shoulders I have stood in writing this book is Benjamin Graham; the further distance brings the mutual fund industry into perspective.

My objective is to provide the same sort of framework for investing in mutual funds as Benjamin Graham provided for investing in individual stocks and bonds. His book *The Intelligent Investor* was first published in 1949. Revised and updated frequently thereafter, it set the standard against which other "how to invest" books are measured. It is no coincidence that the subtitle of this book, "New Perspectives for the Intelligent Investor," echoes his title. Whether I have succeeded in accomplishing the demanding objective that I set for myself, I leave to your judgment.

If this is a good book, it is importantly because of the comments, criticisms, and even editing that I have received from numerous readers of the early drafts. Hesitant as I am to single out any of the commentators, I simply cannot ignore the priceless assistance of Peter L. Bernstein, founding editor of *The Journal of Portfolio Management* and writer of what is without doubt the most thoughtful and respected newsletter in the field; Warren E. Buffett, chairman of Berkshire-Hathaway and probably the nation's most successful investor; and R. H. (Tad) Jeffrey, president of The Jeffrey Company and a remarkable combination of the academic and the practitioner. The time and effort each of them invested in this book place me in their eternal debt.

Many of my associates at Vanguard were also staunch readers and critics, and their comments too were invaluable. But I must single out James M. Norris, my principal staff assistant, for his countless hours of reading, suggesting, calculating, editing, and even typing, all of which have helped to make this the best book that I could write. I also want to thank my other staff assistants, Emily A. Snyder and Mortimer J. (Tim) Buckley III, for their remarkable dedication and support, manifested not only in the substance of their work but also in their extraordinary commitments of time and energy.

I especially appreciate the willingness of Paul A. Samuelson, Professor of Economics Emeritus at Massachusetts Institute of Technology and Nobel Laureate in Economics, to write the foreword. In a sense, I have been his student since 1947, when, as a freshman at Princeton University, I studied his classic textbook, *Economics*. Through the numerous and impressive journal articles on investing he has written over the years, I remain his student and admirer today. His foreword brings this 46-year relationship to full circle.

Finally, in this day and age when it is said that every project needs a champion, I want to thank Amy Hollands Gaber of Irwin Professional Publishing. She spent four long years persuading me to write this book, and her enthusiasm, then as now, helped to give me strength to carry on. Because of her determination, an idea has become a reality.

J.C.B.