

the reading room
common sense on mutual funds
new imperatives for the
intelligent investor

By John C. Bogle
John Wiley & Sons
468 pages

review rating



John Bogle is one of the founding fathers of the US mutual fund industry. His achievements are of titanic proportions, both in terms of the development of philosophy in funds management (ie, the indexing model) and the quantum of his success – the funds under management of Vanguard, the company he founded, now challenge those of Fidelity, the worlds largest fund manager (circa 1999 they were over US\$400 billion). He is a man of uncompromising integrity and of deep faith in what he is doing.

I first read this book in 2000 (Bogle's preface is dated February 1999), and on a recent refresher skim, it proved to be a timeless work, as relevant today as it was four years ago. Indeed, many of the critical issues he raises in relation to the seamier side of funds management, and the conflicts of interests that abound (eg, as outlined in Parts Four and Five of the book) seem incredibly prescient today – in the aftermath of Elliot Spitzer's pursuit of malefactors in the US.

Before one even gets to the Forward by Peter Bernstein, a list of plaudits come from a veritable who's who of the investment universe: starting with Warren Buffett, to Paul Samuelson, Jeremy Siegel, Burton Malkiel (see his book this web site), Michael Bloomberg and David Gardner of Motley Fool fame – hardly anyone is missed out!

This reviewer is not dumb-struck in awe of these plaudits, but neither does he ignore their weight and genuineness. Warren Buffett does not have to give book commendations. As pointed out by Bernstein in his Forward, this is truly an exceptional book, as – notwithstanding the title – it is as much an indictment of the funds management industry as anything else; although it does give the reader a good deal of practical advice on the basic principles of investment and in fund selection. It is not simply a barefaced argument for indexation. Bernstein makes the point that Bogle has written a book unlike one he has ever encountered, "because he discusses sensitive matters that other authors ignore. I hesitate to speculate on why these topics receive such short shrift elsewhere, but I suspect that other experts have horizons that are more limited than Bogle's, or they have less concern for their reader's best interests. ... Despite all the high-minded talk we hear from the corporate spin-masters, conflict of interest between seller and buyer is inherent in our economic system. Jack Bogle's goal was to build a business whose primary objective was to make money for his customers by minimising elements of that conflict of interest, but at the same time to be so successful ..."

The person

To really appreciate what Bogle has done, and why he has

done it, the reader could do worse than start reading this book at page 400. There, Bogle sets out his admiration for Walter L. Morgan, also of Princeton, who, at the age of 31 in 1928 founded the Wellington Fund – Wellington Asset Management is today a leading global fund management company, with distribution in Australia through Goldman Sachs J B Were.

Bogle graduated from Princeton in 1951 after having completed a thesis on the funds management industry. He sent a copy of his thesis to Morgan, and started at Wellington immediately after graduation. Bogle shot up the ranks in Wellington and was appointed heir-apparent at the age of 35. Then he merged Wellington with another company and ended up being fired – which was a real lesson in entrepreneurship. He rescued part of the old Wellington fund from these ashes, and built a new structure for his "idea", and Vanguard was born. That idea broadly constitutes all that is Vanguard today: low fees, no/low sales loads, fund investment objectives must be stated explicitly, the fund should avoid creating the expectation of miracles, and the principle function of the manager should be sound asset management ... and so on.

The rest is history, and Bogle painfully and fearlessly recounts that history, both in terms of the growth and success of Vanguard, and as to the woeful conduct of many US mutual funds. Goodness knows what he would have to say today about the activities unearthed by Spitzer in New York and elsewhere.

The fundamentals of common sense investing

This book is brim full of the sensible fundamentals of investment, and the fact that it is four years out of date, only goes to corroborate how valuable it is. If Bogle's principles had been followed by investors from 1999 through 2004, they would have survived in reasonable shape in any market.

His chapter titles are redolent of the wisdom and common sense that they contain. In Part One, there is: On Long-Term Investing – chance and the garden; On the Nature of Returns – Occam's razor; On Asset Allocation – the riddle of performance attribution; and On Simplicity – how to come down to where you ought to be. These chapters are full of practical rules and foundation blocks that no private investor can ignore.

In Part Two he moves to indexing, equity management styles, bonds and global investing. The latter being quite different from the US perspective than it is from our modest shores. And finally, to selection of superior funds, where the evidence then was overwhelming, and is a fortiori today, that chasing good active funds is very tricky indeed.



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In Part Three he analyses some of the more technical aspects of funds management (eg, tax) but does so in a way that most readers will easily understand. After having written a research paper for the Securities Institute masters program, your reviewer was interested to recount Bogle's views on how some funds can be incredibly tax inefficient, and in this regard, passive fund managers (eg, Vanguard and Dimensional) have been leading the field in research/solutions by a large margin in recent years. These chapters contain very interesting historical data, and highly persuasive arguments for reversion to the mean – it is as if Bogle could foresee or at least sense what was blowing in the wind for March 2000. In fact, in Appendix 1, he provided some prescient “Thoughts about the Current Stock Market as 1999 begins” – not exactly as firm and foreboding as Robert Shiller (of Irrational Exuberance fame); but hardly head in the sand either – one senses he saw it coming.

The remaining two parts deal with Bogle's principled critique of the entire funds management industry, which does contain pointers for the unwary to awake to certain activity in Australia. The ending is more visionary and theological, and in some respects reflects his citation of Thomas Paine in his Preface on page XV: “These are the times that try men's souls ... Tis the business of little minds to shrink; but he whose heart is firm, and whose conscience approves his conduct, will pursue his principles unto death ... Tyranny, like hell, is not easily conquered, yet the harder the conflict, the more glorious the triumph.”

Yes, Jack Bogle is in a class of his own, as is this work.

MARTIN EARP

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