JOHN C. BOGLE

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Thank you very much, John, for giving us your time today. You've achieved a lot in your professional life, and more important, you have achieved a lot for the benefit of the industry as a whole and millions of investors. Your work is truly inspiring. So, from the perspective of career management guidance and advice to young professionals, what can we learn from your experiences?

Perhaps the most important lesson I have learned is that you should always focus on what is best for your clients, not what is best for you as the manager. That is what I have tried to achieve with Vanguard. I will let you be the judge of whether I have been successful or not.

This idea goes all the way back to my 1951 senior thesis at Princeton. I wrote about how to make the mutual fund industry live up to its great potential (it was then a $3 billion industry). In that thesis, which is about 130 pages long, I made many points that proved to be the keys to my career; in particular, they were the keys to my starting Vanguard.

One key point of my thesis was that investment management, or mutual funds in this case, should focus on what is best for the shareholders of the funds. The focus should not be on what is best for the managers of these funds. We sometimes mix that up. Specifically, I concluded that mutual funds could "make no claim to superiority over the market averages." (It's hard to beat the market!) Therefore, the focus of mutual funds should be on reducing costs—that is, their sales charges and their management fees. I said that mutual funds should be run "in the most efficient, honest, and economical way possible." The focus should be on management and not on marketing. So, those are really the essential points that I had the good fortune to be able to put into effect when I started Vanguard.

John C. Bogle founded The Vanguard Group, the world's largest mutual fund management company by assets, in 1974. He served as chairman and chief executive officer until 1996 and as senior chairman until 2000. Mr. Bogle has been recognized as one of the four "investment giants" of the 20th century by *Fortune* magazine and as one of the world's 100 most powerful and influential people by *Time* magazine. He is the author of 10 books on investing, including several bestsellers. Mr. Bogle currently serves as the president of Vanguard's Bogle Financial Markets Research Center.

You raise a lot of issues in terms of moral principles, integrity, keeping clients' interests ahead of your own interests, and so on. Do you think our industry is following these principles?

Some businesses in our industry are. But on the whole, I have to say no. For example, consider another important point. I think the focus of our industry should be on investment, not on speculation. In this regard, in my senior thesis I disagreed with Keynes. In 1936, he wrote about a market in which individual investors did all of the trading; institutions were very small. Keynes said that as institutional investors became more influential in the markets, they were going to move away from a focus on intrinsic value or fundamental value or enterprise value and start trying to outguess what the public was thinking about stock prices, thereby shifting their focus to speculation. And I thought, "Wrong, Mr. Keynes, wrong!" I argued that as these institutions came in, they would maintain their focus on investment, research, and due diligence; they would keep investment as their primary focus. As I said in a speech I gave about this a few years ago, Keynes turned out to be correct. Institutional investors have, in fact, focused more on speculation than on investment; the record on that is clear. So, the score is Keynes 1, Bogle 0.

Mutual funds, and investment managers generally, are primarily focused on speculation. They know that the value of a company is, and has always been since the first book on finance was ever written, the discounted value of its future cash flows. That's all there is to it. Yet they still focus on trying to anticipate the speculative, emotional behavior of other investors.

How do you instill these values in young professionals? Where does it start? Does it start at home? At college? Is it influenced by the corporate culture of the employer?

My own conviction is that the development of our values begins at home. It begins with a family culture and a community culture where telling the truth is important. We're thinking about the community, but what one thinks of oneself is important too. We are always going to be the center of our own universe. But maturity is realizing that the world doesn't revolve around you. It revolves around trying to be part of a good community or a good country or a good industry. These values can be developed in the financial industry through a combination of two solutions.

One is what I call the "Adam Smith solution," in which all the investors in America take their money to financial institutions that put the clients' interests first. Investors would take their money to companies that are engaged in investing, not speculation. Then, the financial institutions that put their own interests ahead of their clients would fall by the wayside, leaving only firms that focus on stewardship.

The other solution is to require institutional investment managers to meet a federal statute of fiduciary duty. But that would be very difficult to do politically because many financial firms do not act like fiduciaries, and they have a great amount of influence in the halls of Congress.

We did act like fiduciaries to a significant degree back in the 1950s and early 1960s, and even in the 1920s and 1930s. This industry started in 1924, and the differences between then and now are really incredible. The initial mutual funds were run by money managers, and they didn't engage in marketing or distribution. Another firm would be their distributor. The management firm and the distribution firm would not be affiliated. Under that structure, the managers were free to manage! Think about that. That kind of focus on the investment needs of the client is required to get managers to be fiduciaries again. The problem with the industry today is that these institutional *speculators* (not *investors*) controlled only 8% of all stocks when I came into this business but now control 70%.

So, I'd say if you want to be in the asset management business, you must first decide what business you want to be in. Do you want to be in the business of investing, which is a winner's game? Most of corporate America keeps putting its capital to work and earning a return on that capital and paying dividends. It's got to be that way. Or, do you want to go into the business of speculating, thinking that you are smarter than everyone else? That is a loser's game because all those clients and speculators out there are going to get the market return less the costs of speculation: the manager's cost, Wall Street's cost, trading costs—all those kinds of costs.

We need speculation in the market—I'm the first one who will admit that—but we don't need it to be the dominant player. We need investment to be the dominant player. Let's have speculation play a cameo role. But if you look at the trading in the market, over $30 trillion each year, versus the amount of capital formation in the market, including primary and secondary issues, the actual amount of capital raised by Wall Street is around $250 billion. That's 130 times as much speculation as investment!

Your criticism of Wall Street is well known. So, why are so many of the top graduates from top schools attracted to Wall Street?

That's a good question. Why do people go to Wall Street? First, of course, is the staggering compensation. Never has so much been paid to so few for creating so little value—and in some cases, even negative value. Some fresh graduates clearly join Wall Street for the wrong reason: compensation. It is not because they have a passion for investing.

However, we also have to give some of these young men and women their due. You get a lot of money for an exciting and intellectually challenging career, which is a little different from getting money for doing nothing. If you think you are working hard and that you are going to beat the other guy, you can get all charged up and say, "This is not worthless; this is a great way to make a living." They are intrigued by the intellectual challenge, but it's not just self-centered. It's playing in a great game and being smarter than just about everybody else.

Of course, today's college graduates who go into this field probably are smarter than everybody else. And their professors are probably smarter than everybody else, and the people they go to work for are smarter. These are not dumb people. But when you think about it, what are they all doing? They believe that they can find the Holy Grail: consistently superior returns. I don't believe that is possible. Put another way, I don't believe anybody can consistently beat the market over the long term.

Bill Miller beat the market 15 years in a row and then went down to the bottom for the rest of his career.[16] Maybe he can come back; anybody can. So, professional investors are all looking for the Holy Grail, and I think that the fact of the matter is that they don't understand that the Holy Grail does not exist. It's like chasing rainbows. But it's exciting, it's competitive, and you can make a lot of money doing it. John Paulson made $5 billion last year.[17] But how many John Paulsons are there? Is that skill or luck? I don't know. I think he's a pretty skillful man, but what do I know? I thought Bill Miller was a skillful man. Bill Miller is a good investor. It's just that nobody knows more than the market in the long run and on a consistent basis.

There seems to be a disconnect in the money management industry between the costs charged and the value delivered to the end clients. From a career management perspective, looking at the next 25–30 years, what's in store for this industry? Can it continue the way it has in the past? For young professionals entering this industry, what should they be worried about?

I'd say the industry has to change. In investing, cost is the reciprocal of value; you can't divorce the two. We can all capture the market return cheaply. Long-term investors who buy and hold the market by definition capture the market return as a group. Short-term speculators also capture the market return in aggregate, but they are trading with one another. By definition, they realize the market return less the costs of trading. As a group, they lose. There is just no way around this. Investors are going to understand that. I would say that people who are honest in our business are doing themselves not only an ethical or moral favor but also a business and a societal favor.

Something else an investment adviser can do is encourage proper investor behavior. Tell the investor to put 50% of his or her money in a bond index fund and 50% of his or her money in a stock index fund and hold it forever. This may not be the most brilliant investment

[16] Bill Miller is chairman and former chief investment officer of Legg Mason Capital Management, a subsidiary of Legg Mason.
[17] John Paulson is founder and president of Paulson & Co., a New York–based hedge fund.

strategy ever invented, but the number of investment strategies that are worse is infinite! The way to protect investors against behavioral mistakes is to ask them to keep a long-term perspective. The rule for investors should be, "Don't do something, just stand there." This is the opposite way that we Americans typically think, which is, "Don't just stand there, do something." Realize your emotions are your worst enemy and time is your friend. None of this is complicated.

Let's come back to your personal experiences. In your book *Enough*, which I have to say is one of the best books I've ever read, you mention that throughout your professional life you never considered work as work.

That's true.

What exactly do you mean by that?

I think it's pretty easy to explain. I grew up in economic distress—a broken family, lived with my grandparents for a while—but it wasn't the end of the world. Jobs like delivering newspapers or being a waiter were fun. After all, what's the matter with riding your bike around the neighborhood and throwing newspapers on somebody's sidewalk or popping magazines into their mailboxes? How can that be work? It kept me away from a lot of other problems.

The only job that I can recall that I considered "work"—and there was in fact one—was when I was a pin setter in a bowling alley. That is work! Somebody knocks the pins down; you pick them up. They knock them down again; you pick them up again.

Did you have an interest in investing from the early days?

I knew nothing about investing in those days. The only financial things that the Bogle family got in the mail were from personal finance companies or the company that held the mortgage on the house. We didn't have enough money to even begin to think about saving. I did think I would probably go into a banking career because I was always good with numbers—not exceptional, but fine. And I was good at spotting errors in numbers a mile away. I can look at a column of figures and say, "That just doesn't look right." I don't think I was ever once wrong.

Then, I majored in economics at Princeton, which was not quantitative at all in those days. Now economics is overwhelmed with quantitative stuff. I decided I wanted to write a senior thesis because I was a contrarian type of kid. You may have figured that out by my odd temperament. I wanted to write the thesis on a subject that no one had ever written a Princeton senior thesis on before. And in December 1949, I stumbled upon an article in *Fortune* magazine. I used to go to the Princeton library and read *Fortune* every month because I was interested in business and that kind of thing, not in the stock market as such.

There was an article about the mutual fund industry, and it was described as "tiny but contentious." I thought, "You have found your thesis topic." I didn't think about it for another moment because I was tiny but contentious myself, and at that time, very little research had been done on mutual funds, almost none. So, I talked to people in the industry, and I wrote a good thesis. Actually, it helped me graduate *magna cum laude* after a poor start, so that was very pleasing. That's how I got my first job with Walter L. Morgan, who is also a Princetonian (class of 1920) and who eventually came to run his own company, Wellington Management.

Is there a method to how passion for a profession develops over time?

I think there is. I think it starts with identifying a focus area, an area you want to be in, an area you want to spend your life in, if you will. On a much more granular level, you should develop a passion to do your best whatever your job is. Over time, if you like what you are doing, you can achieve great things.

Because you have been so successful, let me ask you this: What is the secret to success?

People often ask me what the secret to success is, and I say, "I absolutely have no idea." In fact, I don't use the word success. But I think it has something to do with working a little harder and a little longer than everyone else on whatever job you are given or task you are doing. Do a better job on it than everyone else, and the rewards will come. From this perspective, at least, the secrets to success are not very mysterious.

Some people will never have passion for anything because that is the type of person they are. Being yourself is very important. This is true whether you are dealing with your associates or your clients because people can spot a phony a mile away.

Figure out who you are, and try to follow a career that fits with who you are. Woodrow Wilson wrote a book titled *When a Man Comes to Himself*. I came into myself, to be honest, when I was probably 11 years old. I figured out who I was and what I wanted to do in life very early—too early, you could argue. Most people start to get a good sense of who they are probably in their early 20s, some in their 30s or 40s, and some never. Some people never get to know who they are.

People need to ask themselves, "Am I the kind of person I want to be? Am I filling a role in life, in the community, and in society that I want to fill? Am I comfortable in my own skin? Where does being a good spouse and parent fit in with a career?" People should consider all those kinds of things.

