Marketing and Fiduciary Duty—
Strange Bedfellows?

Remarks by
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On Receiving
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Thank you so much, Chairman Cavanaugh, for that infinitely generous introduction. But please understand that whatever I may have accomplished during my long life and career has come because I've been blessed with a great family, caring friends, wonderful teachers and mentors, and superb colleagues, to say nothing of the fact that an amazing streak of good fortune has smiled on me at each step along the way.

Of course I'm deeply honored to be named as the first recipient of the Lifetime Achievement Award from Marketing Expo. But I confess to some surprise at my selection, for my ideas about marketing are dramatically different from the conventional wisdom of your field.

Why? Because for a long time my view has been—and remains today—that those who accept the responsibility for the prudent management of other people's money are also obliged to offer their services with restraint in the marketplace. In the mutual fund field, the *profession* of management must take precedence over the *business* of marketing.

To me, the profession of investment management means delivering to the human beings who have entrusted their assets to our care the highest possible share of whatever returns our financial markets are generous enough to deliver. No one—*no one*—knows what the future returns on stocks and bonds will be, so our "selling proposition," as it were, cannot promise any level of absolute return—even those that past market history might imply—but only an expectation of returns relative to what our markets provide.

It must be obvious that all investors in aggregate must—and do—receive precisely the return provided by, say, the stock market. (Only in Lake Wobegon can all investors be above average.) But that gross return comes *before* the costs of investing are deducted. After the brokerage commissions, management fees, and operating costs are skimmed off by the financial intermediaries, investors receive what's left. It follows that the *net* returns that investors earn are enhanced, dollar for dollar, by operating at the lowest possible cost. And since the day I founded Vanguard, 30 years ago this September, we have driven to become the lowest cost provider of financial services in the world. Today we have no rival for that standing. So, in the mutual fund field where "you get what you don't pay for" is a truism—you get what you *don't* pay for—we can produce a substantial edge in returns over our high-cost rivals.

Vanguard has never much liked to spend unnecessary money. And since marketing costs a lot of money, we had no desire to be "the last of the big time spenders" during my years running Vanguard. Indeed, at the very outset, I drummed into the character of our Vanguard crew that our first rule of marketing would be: "Market share must not be *bought*; it must be *earned*"—earned by providing superior investment returns, earned by excellence in investor services, earned by winning the trust of investors.

The second rule was, "market share is not an *objective*, it is a *measure*." I not only had no interest in buying our market share with costly advertising and marketing campaigns, but no interest in building it by introducing new funds that simply reflect the fads and fashions of fickle stock markets. Few fund managers operate under such self-imposed restraint. Witness the flood of internet funds, telecom funds, and "new economy funds" that this industry showered on the naive—but often greedy—public—drawing like a magnet more than $500 *billion* dollars in all—in the two years of the peak of the stock market bubble, before it finally burst in the spring of 2000.

If market share grows organically, unforced by costly advertising and opportunistic marketing, that growth is likely telling the world that something *good* is going on: that investors like what you are doing and are willing to put their money where their mind is—entrusting their hard-earned assets to your care. Put another way, as Emerson did, "if a man can make a better mousetrap, the world will make a beaten path to your door."

I suppose the reason that I'm being honored today is because the world—or at least the 15 million investors who invest at Vanguard—has beaten just such a path to our door out in Valley Forge. When we began, assets of our mutual funds totaled just $1.4 billion; today our fund assets total $730 billion.

If market share is a valid measure, it suggests that the mousetrap I designed was indeed a better one. Without *aiming* to build it, Vanguard's share has increased year after year for 23 years, rising on balance from 1.7% of industry assets in 1981 to 9.6% at present. Put another way, fully $600 billion of the firm's present $730 billion asset total has come simply because of the remarkable gains in our market share—earned and not bought, a measure and not an objective. As that Iowa farmer said in *Field of Dreams*, "If you build it, they will come." They did.

But there is one more thing that has fostered Vanguard's growth. I called it "candor as a marketing strategy," making sure that we carefully explain, not merely the rewards of investing, but the risks; not merely the value of investing, but the costs; not claiming superior ability to manage money but stressing the limitations imposed by the tough real world; and above all, doing our best to tell the truth—the whole truth and nothing but the truth—in reporting our investment results to our shareholders and in defining our strategies and our policy positions.

Is it possible to compete in a *different* way in the mutual fund field? Of course. Think of the firms that employ legions of brokers to push their mutual funds, and legions of insurance agents to push their variable annuities, and whose investors are saddled with commensurately high marketing costs. Think of the firms that introduce "flavor-of-the-day" funds that play on investors' baser instincts. Think of the firms that advertised the returns of their hottest equity funds at their peaks, dropped the ads when the returns inevitably tumbled, and now, after last year's market recovery, have returned to advertise their new hot funds.

Doing essentially these things, four of the industry's fastest growing giants doubled their market share, from 5.8% in 1991, to 11.5% at the boom's peak in early 2000. Yet today, their share has tumbled by almost half, to 6.0%, right back where they began. If there is a message here—and I think there is—it is that aiming to build market share and paying for it may work in the short-run, but in the long-run it is doomed to failure. (Full disclosure: each of these four firms has been implicated in the recent mutual fund market timing scandals; that hardly helps build market share.)

I'm pleased to have set Vanguard on the opposite course—using market share as a measure rather than an objective, earning share rather than buying it. My idea was to focus on minimal cost and maximum prudence, most notably in our groundbreaking stock index funds, our index and index-like bond funds, and our money market funds; to strive for superior investor service; to be quiet about our achievements; to make communications technology work for our shareholders and our firm; and to emphasize, not a *business* model, but a *professional* model for the firm's strategy.

Does that mean that our original Vanguard marketing model is the right one for all businesses? Hardly. You know as well as I what a rough-and-tumble, dog-eat-dog business world lies out there, and that the competition for the pocketbooks of consumers is heated and unending—some of us seeking to persuade people to spend, others seeking to persuade them to save and invest. In Vanguard's corner of this latter group, I remain convinced that the long-term marketing values I've described to you today are destined to triumph over the short-term opportunism that has characterized the mutual fund industry during the recent era.

Note: The opinions expressed in this speech do not necessarily represent the views of Vanguard's present management.