ADVISER INVESTMENTS

ADVISER FUND UPDATE

Market Summary and Commentary for Individual Investors from Adviser Investments

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Vanguard's Flurry of Activity

Over the last month, Vanguard has debuted a new fund, closed an existing fund to new investors, reopened two others and added a second management team to one of its bond funds. The firm has also seen a longtime sub-adviser announce his plans to retire at the end of the year. Read on for a summary of the moves.

Global Minimum Volatility Opens

On December 12, Vanguard opened Global Minimum Volatility, which seeks to provide capital appreciation with lower volatility than the global stock market. The fund's managers, Michael Roach, James Stetler and James Troyer, from Vanguard's Equity Investment Group, will use a computer-driven quantitative approach to selecting stocks for the portfolio.

Based on the press release when the fund opened, the strategy's emphasis seems to be much more on the "low volatility" aspect of the fund than outperforming or matching its benchmark, although Vanguard was quick to note that the fund does carry risk, and could be susceptible to losses. As we mentioned when we first covered it in our Sept. 27 *Adviser Fund Update*, this is a relatively new category of fund, with a very limited track record available for consideration. But that has not stopped Vanguard from making plans to add Global Minimum Volatility to its three Managed Payout funds (set to merge into a single fund in January, which we wrote about on Oct. 25). This move will give the new fund approximately $300 million in new assets nearly right off the bat—not a bad start.

Global Minimum Volatility is available in both Investor (0.30% in expenses) and Admiral shares (0.20%), with $3,000 and $50,000 minimum initial investments, respectively. While the fund will certainly be a way for Vanguard to capitalize on the popularity of investments promising a lower level of volatility, it remains to be seen how well funds in this category can deliver on those promises.

Vanguard Closes Fund, Reopens Two Others

That didn't last long—Vanguard Capital Opportunity, reopened to new investors after nearly nine years in April 2013, has once again been closed. Existing shareholders can continue to add to their accounts (limited to $25,000 a year), but most new investors are shut out once again (the exceptions are Flagship account holders and clients of Vanguard's Asset Management Services).

In the months since it reopened, Capital Opportunity, through market appreciation and inflows, increased in size by nearly $3 billion to $11.4 billion in assets at the end of November. Vanguard says it's closed the fund to protect the interests of existing shareholders and to keep the flow of cash at a manageable level for the PRIMECAP Management team running the fund.

The flip side of the Capital Opportunity coin is Vanguard High-Yield Corporate, which closed to new investors in May 2012 as yield-seeking investors flooded the fund with new money. Since then, the fund has seen about $2.6 billion in combined outflows, which Vanguard cites along with a "change in market conditions" as enabling the reopening of the fund to new investors. Vanguard Intermediate-Term Tax-Exempt, which had been closed to most new investors in February 2013, has also reopened for similar reasons.

Bond Fund Adds Manager

We've documented Vanguard's affection for multi-managed funds in the equity space quite a few times over the years, but for the first time, the firm has extended the practice to a bond fund, adding a team from its in-house Fixed Income Group to manage a portion of the Long-Term Investment-Grade fund.

The two-man team from Vanguard consists of Gregory Nassour, a veteran of the Fixed Income group who has been managing Vanguard's Short-Term Investment-Grade and Intermediate-Term Investment-Grade funds since 2008, and Paul Jakubowski, co-head of Vanguard's Financial and Industrial Credit teams, for whom this represents his first named management position. The pair joins existing manager Lucius Hill of Wellington on the fund—Vanguard did not specify the exact breakdown between the teams, but did say that Hill would be the lead manager and responsible for a majority of the fund's assets.

Vanguard's logic behind the move is to add "diversity of thought" to the fund. In the past, that "diversity of thought" has too often resulted in bloated, index-like portfolios for other funds that have been saddled with multiple management teams. For now, it seems like Long-Term Investment-Grade may be spared that fate, as the new team's role will initially be minimal. We're curious to see how the multi-manager experiment goes on this fund, and wonder what it bodes for Vanguard's other bond funds.

Manager Retiring

Jack Granahan, a co-manager on Vanguard's Explorer fund since 1990, who in his long career worked for Vanguard's predecessor Wellington before starting his own investment management firm in 1985, announced his plans to retire from portfolio management at the end of 2013. He is one of the longest-tenured outside managers still working for Vanguard, but at 77 years old, he's decided it's time to step down, although he plans to remain involved with his eponymous firm, Granahan Investment Management, in a reduced role.

At one point, Explorer was one of Vanguard's more interesting funds, with its focus on the small-cap segment of the market and compelling performance. But over the years, Vanguard added manager after manager to the fund instead of closing it, diluting the portfolio and performance. Today, the fund counts seven management teams, making the departure of any one management team (let alone a single manager from one of those teams) almost a non-event.

Vanguard has not officially acknowledged Granahan's retirement, but for now it seems safe to assume that his colleagues and co-managers Gary Hatton and Jane White will carry on in his absence on the firm's 20%-plus portion of Explorer's assets. We do not see Granahan's departure as reason for concern for existing investors.

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