



ADVISER FUND UPDATE

Market Summary and Commentary for Individual Investors from Adviser Investments



December 31, 2015

Vanguard Announces Active Fund with Junk-Bond Exposure

Last Monday, Vanguard announced plans to bring Core Bond fund to market during the first quarter of 2016, the first actively managed Vanguard fund with a portion dedicated to high-yield (also known as “junk”) bonds.

Lately, Vanguard’s indexed bond funds—in particular, Total Bond Market Index—have overshadowed the strong performance of active funds like Short-Term Investment-Grade and Intermediate-Term Investment-Grade. The new fund looks to extend that winning streak for Vanguard active management in fixed income.

Core Bond will be helmed by a trio of Vanguard managers—Gregory S. Nassour, Brian Quigley and Gemma Wright-Casparius—who will build a portfolio consisting of both investment-grade and non-investment-grade bonds. Junk bonds will comprise up to 5% of assets, “medium quality” bonds will take up as much as 30% of assets and the remaining 65% or so of the fund will be invested in government, agency and investment-grade corporate securities. Up to 10% of the fund can be invested in non-dollar denominated bonds.

The idea of Vanguard’s fund (and other “core” bond funds) is to provide a one-stop investing solution for the fixed-income portion of a portfolio—either as the only fund investors need in the space, or as a foundation to build around, complementing it with smaller positions in other funds to tweak duration, sector and credit-quality exposures to their desired levels.

In some ways, this seems somewhat like a “me-too” offering from Vanguard, as a number of its competitors already have actively managed core-bond funds on the market. However, Vanguard is once again entering the fray with a cost advantage, providing a cheaper option for investors. Core Bond’s expenses are expected to run 0.25% for Investor shares and 0.15% for Admiral shares, far below the intermediate-term bond fund average expense ratio of 0.84% for actively managed funds.

Vanguard Launching Emerging Markets Bond Fund

Concurrent with the Core Bond announcement covered above,

In This Issue

- Vanguard Announces Active Fund with Junk-Bond Exposure
- Vanguard Launching Emerging Markets Bond Fund
- Vanguard Stays on Offensive in Fee War

Vanguard also revealed plans to launch an actively managed bond fund focused on emerging markets fixed-income investments. Unlike Core Bond, however, the firm is not planning to roll it out for individual investors initially, if ever.

It's not clear who will be able to invest in the fund, but there will be both Investor and Admiral shares, and the manager, Daniel Shaykevich, joined Vanguard in 2013 from BlackRock's emerging markets debt team. We'll keep you posted as details emerge.

Vanguard Stays on Offensive in Fee War

As we discussed [last January](#), Vanguard and Fidelity have engaged in a battle over fund fees for more than a decade. And now, Vanguard has pulled back into the lead as the sector-ETF provider with the lowest expense ratios.

This campaign dates to October 2013, when Fidelity launched 10 sector exchange-traded funds (ETFs) that track similar or identical MSCI indexes as Vanguard's older sector ETFs, but undercut them on expenses—a direct foray into a space where Vanguard had been long established as a market leader. It marked yet another blow in the “fee wars” between the two competitors that have been ongoing for more than 10 years.

On the sector front, it took Vanguard more than a year to respond. As 2014 came to a close, the fund giant reduced its sector ETF shares' (and corresponding Admiral shares') expense ratios from 0.14% to 0.12%, the same Fidelity charges for its sector ETF lineup. This month, Vanguard struck again, cutting fees on most of those funds another two basis points to 0.10% (a couple of share classes saw a three-basis-point reduction to 0.09%), undercutting Fidelity's offerings.

While at it, Vanguard cut fees on a few other funds; see the table below for a full list.

The competition to see which firm could provide the lowest fees on index funds began in 2004, when Fidelity slashed fees on key index funds to less than Vanguard was charging for similar offerings. The two fund titans' efforts at outmaneuvering their competitor has persisted with numerous feints and jabs since. In May 2010, Vanguard made investing in its ETFs commission-free for all brokerage clients, and later that year sent shockwaves through the ETF industry when it launched 19 ETFs tied to institutional index funds.

As a refresher, an expense ratio tells shareholders how much they are paying to support the firm's annual cost of operating a particular fund or ETF. The expense ratio is calculated by dividing annual operating expenses by the average dollar value of the fund's or ETF's assets under management.

We are always encouraged when fund companies cut costs for investors. While Fidelity and Vanguard will likely continue to battle for investment dollars, the real winners of the fee wars

are investors who can keep more money in their accounts compounding over the long term.

Vanguard Expense Ratio Changes Effective 12/22/15

Fund	Share Class	Ticker Symbol	Former Expense Ratio	Current Expense Ratio
Consumer Discretionary ETF	ETF	VCR	0.12%	0.10%
Consumer Discretionary Index	Admiral	VCDAX	0.12%	0.09%
Consumer Staples ETF	ETF	VDC	0.12%	0.10%
Consumer Staples Index	Admiral	VCSAX	0.12%	0.10%
Energy ETF	ETF	VDE	0.12%	0.10%
Energy Index	Admiral	VENAX	0.12%	0.10%
Explorer Value	Investor	VEVFX	0.66%	0.65%
Extended Duration Treasury ETF	ETF	EDV	0.12%	0.10%
Financials ETF	ETF	VFH	0.12%	0.10%
Financials Index	Admiral	VFAIX	0.12%	0.10%
FTSE Social Index	Investor	VFTSX	0.27%	0.25%
Health Care ETF	ETF	VHT	0.12%	0.09%
Health Care Index	Admiral	VHCIX	0.12%	0.10%
Industrials ETF	ETF	VIS	0.12%	0.10%
Industrials Index	Admiral	VINAX	0.12%	0.10%
Information Technology ETF	ETF	VGT	0.12%	0.10%
Information Technology Index	Admiral	VITAX	0.12%	0.10%
Intermediate-Term Corporate Bond ETF	ETF	VCIT	0.12%	0.10%
Intermediate-Term Corporate Bond Index	Admiral	VICSX	0.12%	0.10%
Intermediate-Term Government Bond ETF	ETF	VGIT	0.12%	0.10%
Intermediate-Term Government Bond Index	Admiral	VSIGX	0.12%	0.10%
Long-Term Corporate Bond ETF	ETF	VCLT	0.12%	0.10%

Long-Term Corporate Bond Index	Admiral	VLTCX	0.12%	0.10%
Long-Term Government Bond ETF	ETF	VGLT	0.12%	0.10%
Long-Term Government Bond Index	Admiral	VLGSX	0.12%	0.10%
Materials ETF	ETF	VAW	0.12%	0.10%
Materials Index	Admiral	VMIAX	0.12%	0.10%
Mega Cap ETF	ETF	MGC	0.11%	0.09%
Mega Cap Growth ETF	ETF	MGK	0.11%	0.09%
Mega Cap Value ETF	ETF	MGV	0.11%	0.09%
Mortgage-Backed Securities ETF	ETF	VMBS	0.12%	0.10%
Mortgage-Backed Securities Index	Admiral	VMBSX	0.12%	0.10%
Short-Term Corporate Bond ETF	ETF	VCSH	0.12%	0.10%
Short-Term Corporate Bond Index	Admiral	VSCSX	0.12%	0.10%
Short-Term Government Bond ETF	ETF	VGSH	0.12%	0.10%
Short-Term Government Bond Index	Admiral	VSBSX	0.12%	0.10%
Telecommunication Services ETF	ETF	VOX	0.12%	0.10%
Telecommunication Services Index	Admiral	VTCAx	0.12%	0.10%
Utilities ETF	ETF	VPU	0.12%	0.10%
Utilities Index	Admiral	VUIAX	0.12%	0.10%

Source: Vanguard.

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