

November 4, 2011

To Principals and Veterans:

Three items that may be of interest:

1. Next Monday and Tuesday (and possibly Wednesday), **CBS Evening News** will present excerpts from a group interview yesterday on the problems facing America, our nation's challenges and our hopes. The interview was conducted by new anchor Scott Pelley (moving over from "60 Minutes"). He did, I thought, a really outstanding job. I was honored to be part of the ten-person panel—a diverse group of citizens of various ages, genders, races, and backgrounds. If you happen to catch any of the shows, I'd be interested in your reaction.
2. Last Friday, Michael Smerconish wrote a generous column in *The Philadelphia Inquirer*, discussing my reaction to the "Occupy Wall Street" movement and its many aspects. In case you missed it, a copy is attached. (Not so sure about being called a "patrician.")
3. Virtually every day, I receive complimentary letters about Vanguard and my long career. I couldn't possibly circulate all of them, but I just received a very special one. It comes from James Grant, publisher of *Grant's Interest Rate Observer* and host of a well-attended and prestigious semi-annual forum for senior money managers. Their reaction to Jim's interview with me was truly remarkable. He describes it in his lovely letter, also attached.

Thanks to you all for doing the exceptional work you do. Happily, much of it continues to reflect on me.

Best,

Jack

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A capitalist's praise of protest

Funny, Jack Bogle doesn't look like any of the members of Occupy Wall Street we've been seeing on television.

I can't picture the legendary founder and former CEO of the Vanguard Mutual Fund Group, clad in Brooks Brothers suit, adjacent to City Hall, or as one of the 50 who were arrested in Atlanta, not to mention those being sprayed with tear gas in Oakland. But that doesn't mean the Main Line patrician and capitalist icon is lacking in sympathy for some of their grievances. Bogle believes attention must be paid to their complaints.

I was thinking about Bogle after reading what one of his fellow Princetonians wrote about the movement. The New York Times columnist Paul Krugman opined earlier this month that: "Wall Street's Masters of the Universe realize, deep down, how morally indefensible their position is. They're not John Galt; they're not even Steve Jobs. They're people who got rich by peddling complex financial schemes that, far from delivering clear benefits to the American people, helped push us into a crisis whose aftereffects continue to blight the lives of tens of millions of their fellow citizens."

The reference to the complexity of the financial sector made me think of Bogle, who has often spoken and written about how we've shifted to a paper economy devoid of real value. By way of example, in his 2008 book, *Enough*, he lamented that "over the past two centuries our nation has moved from being an agricul-

tural economy, to a manufacturing economy, to a service economy, and now to a predominantly financial economy."

Why is this a problem? Because Bogle believes that by definition, this financial economy "deducts from the value created by our productive businesses."

"While the owners of business enjoy the dividend yields and earnings growth that our capitalistic system creates, those who play in the financial markets capture those investment gains only after the costs of financial intermediation are deducted," he wrote. "Thus, while investing in American business is a winner's game, beating the stock market before those costs is a zero-sum game. But after intermediation costs are deducted, beating the market — for all of us as a group — becomes a loser's game."

By way of further illustration, Bogle has analogized our financial economy to the childhood game of Rock, Paper, Scissors. (Recall that rock breaks scissors, scissors cut paper, and paper covers rock.) What's that got to do with our economy? The paper companies, Bogle has said, are those that shift focus from creating a product to making deals and counting assets.

The rocks are those that maintain what Bogle called a "real business foundation." When relentlessly rising prices become too detached from the actual value they add, paper has covered rock. Bogle cited as examples the mergers of AOL and Time Warner, Qwest and US West, World-



SCOTT S. HAMRICK / File Photograph

Jack Bogle in 2005, with an antique telescope in his office. The ex-Vanguard CEO empathizes with Wall Street protesters.

Com and MCI, adding, "I don't have to tell you which was paper and which was rock."

"Paper' companies that count have acquired 'rock' companies that make," Bogle concluded, "and the results have been devastating."

While the messages coming from Occupy Wall Street often seem to lack cohesion, one mantra has been that the new economy so eloquently described by Bogle has created unprecedented income disparity. A report out Tuesday from the Congressional Budget Office detailed how, in the last three decades, "the share of after-tax household income for the top 1 percent of the population more than doubled, climbing to 17 percent in 2007 from nearly 8 percent in 1979."

So is Occupy Wall Street channeling Jack Bogle? I e-mailed and asked him.

He replied, "I like the idea of the idealism, frustration, and even anger that the Occupy Wall Street movement represents. These (mostly) young citizens can see what

their elders (mostly) cannot — that the financial system is responsible for much of the havoc wreaked on our economy, with the penalties paid not by the Wall Street (and Greenwich) financiers and executives who led and participated in the abuse, but by the taxpayers of our nation. That our savers, as a result, are earning close to zero on their hard-earned savings is just one more example of this economic drain and profound unfairness.

"So long as we have a First Amendment that guarantees the right of the people peaceably to assemble, their right to protest the inequities in our economic and financial system sends an important message to Wall Street: 'Attention must be paid!' In a world increasingly dominated by Goliaths, all those Davids together will make a difference."

Contact Michael Smerconish via www.smerconish.com. Read his columns at www.philly.com/smerconish.



Michael Smerconish
The Pulse

JAMES GRANT
TWO WALL STREET
NEW YORK, NEW YORK 10005
212-809-7994 • jgrant@grantspub.com

Oct. 28, '11

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Dear Jack,

For all I know, you may have set in motion a mass financial migration to Philadelphia from New York. What an honor it was to have you at Wednesday's event. Never, in my 27 or 28 years of hosting these conferences, have I heard such love radiating from audience to speaker. I thank you,

Sincerely yours,

Jim