Review of Bogleheads Guide to the Three Fund Portfolio

I was recently given the pleasure of reviewing an advance copy of my friend Taylor Larimore’s excellent *The Bogleheads Guide to the Three-Fund Portfolio* and will now take the opportunity to recommend it to you. I’ve generally stopped doing book reviews on this blog except during **Continuing Financial Education** week because they’re a ton of work for little profit and unlike Mr. Larimore, I actually prefer reading non-financial books these days! However, this book was worth making an exception for.

A diehard, long-term Boglehead may not learn a single thing from this book, but you should buy it anyway for the sheer pleasure factor. An investing rookie will find that the book not only teaches you about *one of the reasonable asset allocations* (and certainly the most popular) you can use, but is a primer on basic investing, portfolio management, and most importantly, good investing behavior. The experienced Boglehead will treasure it as a letter from a grandfather passing on critical life lessons in his last years.

In our era of **FIRE blogs**, we have lots of people dropping out of the workforce in their 30s or 40s just as soon as they hit
financial independence in order to put their feet up and chill. In contrast, we have 94-year-old Battle of Bastogne veteran Taylor Larimore who is still making valuable contributions to the world. Buy the book just to say thanks to one of the last of the Greatest Generation. Of course, the money isn’t going to him, he’s donating all proceeds to the John C. Bogle Financial Literacy Center (helps support the forum and annual meeting.) In addition to feeling good about supporting a good cause, you also get to read 5 pages from Jack Bogle (who may not be around any longer than Taylor), and 70 pages from Taylor. In addition to their own wisdom, the words of dozens of investing experts and Bogleheads also appear in the book. Did you hear that? 75 pages (plus some short appendices.) It’s not quite If You Can, but it’s short enough that just about anyone can get through it.

Bogleheads’ Guide to the Three-Fund Portfolio

In Defense of the Total Market Index Fund

The meat of the book is an explanation of 20 reasons why investing in total market index funds is a good idea. Maybe I ought to step back briefly and explain that the Three Fund Portfolio is a combination of three of the largest mutual funds in the world, all low-cost, broadly diversified index mutual funds:
1. Vanguard **Total Stock Market Index Fund**
2. Vanguard Total International Stock Market Index Fund
3. Vanguard Total Bond Market Index Fund

in any sort of reasonable combination. Those reasons include:

1. **No advisor risk**
2. No asset bloat
3. No index front running
4. No fund manager risk
5. No individual stock risk
6. No overlap
7. No sector risk
8. No style drift
9. Low tracking error
10. Above-average return
11. Simplified contributions and withdrawals
12. The benefit of consistency
13. Low turnover
14. Low costs
15. Maximum diversification (lower risk)
16. Portfolio efficiency (Best risk/return ratio)
17. Low maintenance
18. Easy to rebalance
19. Tax efficiency
20. Simplicity (for investors, caregivers, and heirs)

Put it all together and he makes a strong case for total market investing.

The Foreword

In addition to this section (Chapter 4, encompassing about half the book), there are a lot of other little pearls to enjoy. For example, I found two things interesting in the Foreword by Bogle. The first was that he doesn’t exactly endorse the three fund portfolio. He says this about it:

“Index funds are designed simply to assure you that you will earn your fair share of the returns delivered in each segment of The Three Fund Portfolio or any other indexing strategy that meets your needs.”

The second was just a hint of gloating. Bogleheads have, for years, criticized Jack’s statement that international stocks aren’t necessary that he made in *Bogle on Mutual Funds* in 1994. In the foreword, Jack says this:

“I wrote that a long-term investor need not allocate any of his or her assets to non-U.S. stocks. But if they disagreed, I argued, they should limit their holdings to 20% of their
stock portion, given the significant extra risks involved (such as currency risk and sovereign risk). My opinion was based on the expectation that the American economy would continue to grow over the long term, and that the market values of U.S. corporations would grow faster than the values of non-U.S. corporations. Since 1994, as it was to happen, the U.S. S&P 500 Index was to rise by 743%, while the EAFE (Europe, Australasia, and Far East) Index of non-U.S. Stocks rose by 237%. That I was right is beside the point. It may have been luck. But now that U.S. stocks have dominated for nearly 25 years, it may well be time for reversion to the mean, with non-U.S. stocks leading the way rather than following. Who really knows? No one knows what tomorrow may bring. But I’m inclined to stick by my earlier conclusion that holdings of non-U.S. stocks should be limited to no more than 20% of equities. For U.S. investors, Taylor suggests that 20% of the equity allocation should be placed in a Total International Stock Index Fund. That suggested 20% is essentially a compromise between my suggested maximum of 20% and the minimum 20% recommended by a Vanguard study.”
The Life of Taylor Larimore

Some of the other pearls in the book are taken directly from the life of Taylor Larimore. Born in 1924, the year the first mutual fund was started, he was the grandson of an investing giant. However, that didn’t spare his family from having to move away during the Great Depression when the family restaurant went under. At first, it wasn’t so bad – they moved into Grandpa’s waterfront mansion. But when his company went bankrupt too, they ended up in a small Miami apartment. Even those difficulties paled in comparison to what Taylor must have felt in the dark of night on Monday, June 5th, 1944 high above the French coastline aboard a C-47, much less on Christmas Day in Bastogne later that year while surrounded by Germans. But like most of his generation, he doesn’t even mention that. His entire wartime service and college education are brushed aside in half a sentence in the preface. However, what he does share in the preface are the investing lessons he learned in the school of hard knocks. Like me, he must have been hardheaded, since he had to learn two of those lessons twice. Here are the lessons he learned:

1. A 100% stock portfolio can be dangerous.
2. Believing a broker is your friend can be dangerous
3. Avoid the lure of individual stocks.
5. Investment newsletters are a waste of money and market-timing doesn’t work.
7. Avoid expensive stockbrokers and their hidden fees.
8. Buying high and selling low is a losing strategy.

If you want to hear the stories behind the lessons, you’ll need to buy the book.

The Boglehead Philosophy

The book also contains a summary of Boglehead wisdom tucked
into the nooks and crannies. If any of this is new to you, you really need to read this book.

1. Develop a workable plan
2. Invest early and often
3. Never bear too much or too little risk
4. Diversify
5. Never try to time the market
6. Use index funds when possible
7. Keep costs low
8. Minimize taxes
9. Invest with simplicity
10. Stay the course

Implementation Advice

Some investors want to be told exactly what to do. Taylor does that for you. Not only does he tell you which three mutual funds to use, but he tells you how much to put in each of them. He says hold your age in bonds, so if you’re 30 years old, your portfolio should be 30% bonds. He also says put 20% of equity into international stocks. So that same 30-year-old would have the following portfolio:

- 56% Total Stock Market Index Fund
- 14% Total International Stock Market Index Fund
30% Total Bond Market Index Fund

and a 60-year-old would have this portfolio:

- 32% Total Stock Market Index Fund
- 8% Total International Stock Market Index Fund
- 60% Total Bond Market Index Fund

If you like to be told what to do so you can move on with more important things in your life, you can do far worse than to follow Taylor’s advice. A hobbyist won’t be satisfied with that, but most investors (and everybody is an investor whether they recognize it or not) are not hobbyists.

He even gives you some advice as far as how to deal with the 401(k) and other tax-advantaged retirement plans, like use a good target retirement fund, substitute the 500 index for TSM, or even build your own TSM with 5 parts 500 index and 1 part extended market index. The book ends with the obligatory chapter on Staying the Course. It is so important, but there isn’t much to say about it. Taylor’s version lasts a page and a half and can be summarized in two sentences:

When stocks are in a Bear Market...you will be strongly tempted to sell at least a portion of your stock funds. DON’T DO IT.

Criticisms
Critics of the book are likely to point out that it’s a bit expensive for such a short book. Funny how those “frugal” critics fail to realize just how much higher their expense ratios are than the funds advocated in the book. Talking about penny-wise and pound-foolish. Critics may also say “everybody knows the lessons this book contains.” Having helped thousands of otherwise very intelligent people with their portfolios, I assure you that is not the case. Larimore also does not even address the elephant in the room when it comes to Total Market Investing — Factor Investing. I think that was partly an effort to maximize simplicity for the intended audience of the book, but also because Taylor simply doesn’t believe in factor investing. It’s easy for me to see why. Look at all the fancy ways to invest that have come and gone in his 94 years! How many of the hundreds of factors being promoted out there will we even remember a decade or two from now? At any rate, if you do choose to “tilt” a portfolio, I think it is critical to first understand the base to tilt from first, and this book will teach that.

Overall, it’s a book well worth your time and money. Even if you don’t want to keep it on your shelf forever, I’m confident you already know the person you should give it to when you’re done.

**Buy The Bogleheads Guide to the Three-Fund Portfolio today!**

What do you think? Have you read the book? What did you like or dislike about it? Comment below!