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Is Bogle bailing on stocks?
By Curtis Seltzer

John Bogle, founder of the Vanguard Group, has made a lot of money being a trustworthy business friend of individuals and institutions that invest in stocks and bonds. Vanguard fees are reasonable, and Bogle popularized index funds that usually prove to be better bets than stock-picking over the long run.

When Bogle writes, I read.

Bogle wrote a truly extraordinary op-ed piece in the Wall Street Journal ("Restoring Faith in Financial Markets," January 19, 2010) that calls for profound investor-oriented changes, including federal legislation, in the way money managers and mutual funds act toward the stocks (companies) they invest in.

His argument is that the stewards of money have betrayed their clients. Returns "…have often been illusory," tricked up by financial engineering and over-the-top risk-taking. The agents who invested client money failed to follow their fiduciary duty to their clients by not acting as owners, by allowing corporations to pretty much do as they pleased. The blame, he believes, lies with corporate behavior, but also with institutional investors -- mutual funds, public and private pension funds, etc. -- that now own almost 70 percent of the shares of U.S. corporations, up from less than 10 percent in the mid-1950s.

He points to five developments that followed the growth of "agency ownership" of corporate stock: 1) short-term speculation has replaced long-term investing, which allowed stock price to replace a company's intrinsic value (the discounted value of its future cash flow) as the measure of investment; 2) the financial sector became the principal driving force in the U.S. economy, and client fees charged by stock exchange firms and mutual funds now run to about $475 billion; 3) innovation in financial markets provided neither security nor better value, only ways "…to make money for Wall Street firms rather than for their clients"; 4) money managers ignored real profits and cash in their analyses of corporate balance sheets and income statements; and 5) lacking any checks, executive compensation became decoupled from performance and simply went up because nothing was there (like owners) to stop it.

Bogle advocates that money managers start to act solely in the interests of their shareholders and beneficiaries; perform proper due diligence in their investments; actively participate as owners in corporate governance; and eliminate conflicts of interest in their activities.

If these policies are not adopted by money managers, does it follow that Bogle would advise investors to avoid stocks? It seems that is the implication of his argument.

I laid out of Bogle's arguments because I think it reflects what my wife once said about stocks, "You can't win." While the "you" she was addressing was me, she was expressing her general feeling that run-of-the-mill investors can't win.

Since the 1920s, stocks have earned an average of 9.8 percent annually, with a net return of less than 4 percent annually once inflation, fees and taxes were figured in. (Jason Zweig, "Why Many Investors Keep Fooling Themselves," Wall Street Journal, January 16-17, 2010, quoting Ibbotson Associates.). Bogle says that he would trade his own assets for a net-net-net return of 2.5 percent guaranteed, which says a lot about what he thinks about future returns.

In a less-than-4-percent world, it's understandable how Bernie Madoff and his "consistent returns" lured investors in with no questions asked.

I have watched my own stock investments disappear (Pan Am, Digital Equipment) and ride down three crashes under professional management. Here are a few reasons why I think land is a better long-term investment than stocks.

Penetrability. Corporations often hide things, spin things and fail to disclose things that bear on their

future earnings. It's hard to know what companies are planning to do with their capital and what risks they don't disclose. It's also hard to know who they want to buy or who wants to buy them -- and whether they're being run honestly. (I also had money in Tyco.) It's almost impossible for an individual investor to penetrate the screens to get the facts that would allow a sensible investment decision. And Bogle says money managers can't be counted on to do sufficient due diligence. (As with all generalizations, exceptions exist.)

Land sellers, of course, often erect similar defenses against buyers. The difference is that a motivated land buyer can generally pierce a seller's lack of disclosure or misrepresentation through diligent scoping. Land is simply easier to figure out than corporate reports. Any ordinary citizen can scope land, which is not true of a 10K.

Intrinsic value. Land has intrinsic value. It can earn money. It has tax advantages. It always appreciates over the long term. Corporate stock may or may not have intrinsic value; I'm thinking of assets, profits (in hand) and cash. Intrinsic value doesn't disappear.

Land will always be worth something unlike so many dot.coms of recent memory.

Risk. The fortunes of individual companies are subject to multiple risks, some of which are train wrecks. Compare the DJIA 30 companies of 2010 with 20 years ago—14 companies were dropped, including USX, Bethlehem Steel, Westinghouse, Sears, Honeywell and Woolworth, among others. Inasmuch as land demand and prices are driven by population growth and finite supply, land risks are fewer and generally not as potentially catastrophic. Land is not like the horse-drawn buggy at the dawn of the automobile age. Demand for it won't disappear as a result of technological change, foreign competition, trade policy or shifting consumer tastes.

The risks with land investments are almost always knowable at the time of purchase. Diligent research should protect an investment for at least 7 to 10 years against surprises that would lower property value.

Long-term horizons. America is supposed to register 400 million people in 2039, up from about 305 million or so today. That's money in any one's long-term land bank.

Will population growth benefit most companies as directly? Which companies today would you wager will be around in 30 years? What annual return would you bet on for stock investments during the coming three decades?

For the long-term investment, buy and hold works in land; my experience is that it has not worked in stocks.

Volatility. The past decade has seen two runs ups and two stock crashes. Land prices moved up and down, but the 20-year trend has been up. The market and prices for land -- agriculture, timber, recreation, second homes -- is driven by a somewhat different set of factors than metropolitan residences. Country property is less volatile than its city cousins.

In and of itself, volatility does not make stocks a chancy investment. But I've learned that there's a whole lot less stomach churning with land than with stocks. And that has value too.

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