Vanguard Product Has Survived Pretty Rugged Financial Storms

Wellington Fund: a Balancing Act Since 1928

by Danielle Schultz, CFP

Do you need a little balance in your life? A bond fund with 60 percent stocks and 40 percent bonds can be a good choice to offset riskier investments or a way to allocate savings for a specific goal. In some workplace retirement plans, it may be the low-cost choice and an alternative to target-date retirement funds.

Balanced funds have been around a long time: since 1928, in the case of Vanguard Wellington Fund (ticker: VWELX). This type of fund is designed to be an all-weather fund — in choppy market conditions, the balance between stocks and bonds should keep the fund afloat, protected by the bond component. But because of the tilt toward stocks, the fund should also be able to take advantage of conditions in which stocks are outperforming, as they do in the long run.

Like most balanced funds, the proportion of stocks can vary between 60 percent and 70 percent, depending on market forces and the manager's call. So the bond proportion can bottom out at around 30 percent of the portfolio and go up to 40 percent when the manager believes conditions warrant heavier bond emphasis.

Vanguard Wellington was originally as an actively managed fund with manager decisions determining overall portfolio choices. Since 1978, however, the fund — while still actively managed — has followed the balanced approach.

Similar funds that might be offered in workplace accounts include T. Rowe Price Capital Appreciation (PRWCX), which owing to the influx of money has been closed to new investors since June; Dodge & Cox Balanced (DODBX), with wider leeway in the mix of stocks and bonds; and Fidelity Puritan (FPURX). There are also myriad other funds often called equity/income.

Wellington also offers the lower-cost Admiral class. But the minimum investment for these shares is higher-than-average at $50,000.

Right now most of these funds are emphasizing the stock allocation of their portfolios. As a result their recent performance has improved because of the generally positive direction of stocks compared with bonds.

Target-Date Versus Balanced Funds

Workplace retirement programs are making the move to designating target-retirement-date funds as the default investment selection. But you may want to consider a balanced fund as an alternative, depending on the rest of your portfolio, risk tolerance and goals.

Target-date funds are rebalanced to become more conservative as the target date approaches. It's important to examine the specific fund to know what the final mix will be, but if the target-date fund moves you to less than 50 percent stocks at some point, it may be too conservative to meet your retirement needs.

All the withdrawal strategies that propose about 4 percent of the portfolio as a safe annual withdrawal are based on that portfolio containing at least 50 percent stocks. But balanced funds maintain approximately the same mix over time, not responding to the projected time of your retirement.

Depending on your investments outside of your workplace retirement account, you may want a slightly more aggressive fund than a target-date option. Particularly if you're in good health and have a family history of longevity, a balanced fund may offer as much safety as you need, consistent with return and having your portfolio last as long as you do.

In contrast, if you're a younger investor, you may not be comfortable with a retirement or investment fund that's 80 percent or 90 percent in stocks. A balanced fund may offer all the risk you can tolerate.

Finally, for funds such as college savings or a future home project or as a place to park a windfall until other investments can be analyzed, a balanced fund can offer a one-stop shop for return with moderate risk.

Investing Philosophy and Portfolio

Wellington concentrates its stock portfolio on value stocks. It's important to note that unlike some balanced or strategy funds (Vanguard's STAR fund or its various LifeStrategy funds, for example), Wellington selects individual stocks and bonds, rather than being a fund of funds. Wellington today is invested about 66 percent in stocks and 33 percent in bonds, with the remainder in cash reserves.

Most of the stocks are of medium and large companies whose dividends are larger than the norm for the overall Standard & Poor's 500 index. Also, Vanguard states that it seeks stocks managers believe are undervalued by the marketplace. In practice, the stock portion contains about 20 percent health care and 21 percent financial-services companies.

As an actively managed fund, there's also leeway to invest a small portion of the fund in derivatives, foreign currency contracts and stocks, and convertible securities.

Although the fund has a long track record, managers do have the freedom inherent in all actively managed funds to make their best guess as to beneficial market directions. *(See table, far right on p. 35, for Wellington's top holdings.)*

Vanguard Wellington Fund Near-Term Performance

	YTD	1 mo.	1 year	3-year annualized returns	5-year annualized returns	10-year annualized returns
Growth of $10,000	$10,892	$10,017	$11,069	$14,813	$16,954	$21,798
Fund	8.92%	0.17%	10.69%	13.99%	11.14%	8.10%

Source: Morningstar

Wellington Fund's 10 Largest Holdings

By rank as of month-end Oct. 31

1. Wells Fargo (WFC)
2. Microsoft (MSFT)
3. Merck (MRK)
4. Verizon Communications (VZ)
5. Exxon Mobil (XOM)
6. Comcast (CMCSA)
7. JPMorgan Chase (JPM)
8. Chevron (CVX)
9. Johnson & Johnson (JNJ)
10. CVS Health (CVS)

10 largest holdings = 16.8 percent of total net assets

10 largest holdings = 25.7 percent of equities

Source: Vanguard

On the other side of the aisle, the bond portion is invested primarily in high-quality bonds (Barclay's A or better) with an emphasis on U.S. government bonds. The duration, which measures the price sensitivity of bonds to changes in interest rates, is currently 6.5 years (intermediate term — generally less risky but lower yielding than long-term ones). The yield is 2.3 percent for the overall fund (including stock dividends).

Management and Tenure

The fund has been managed for the past eight years by Edward Bousa on the equity side and John Keogh on the bond portion. Both men appear to be in their mid-50s, which means their retirement is probably not imminent. As with all actively managed funds, investors should watch for any changes, but Vanguard funds tend to have a deep bench.

Performance

Because the fund has such a long history, the steady upward progression of returns since 1929 is striking. But since most of us didn't start investing in 1929, it's important to look at more near-term performance. *(See table, top left.)*

This is a very solid and consistent performance for a mutual fund that easily beats many target-date funds. In addition, Wellington's standard deviation, a gauge of a fund's risk indicating how much returns vary from the average, is 5.96, compared with Vanguard's Target Date 2020 Fund (6.41 SD, with about 36 percent in bonds).

> **"For funds such as college savings, a balanced fund can offer a one-stop shop for return with moderate risk."**

What's the worst-case scenario? As with nearly every fund, Wellington took a hit in 2008-2009. A sum of $10,000 invested on Sept. 1, 2008, would have dropped to $6,945.93 on March 9, 2009 — the bottom of the market.

This was one of the two worst losses in its entire history. It took until 2010 to fully recover that $10,000, but with money invested for that entire period it's currently worth more than $17,000.

Costs

Wellington (Investor class) is no-load with a low expense/management fee of 0.26 percent and a minimum investment of $3,000. The corresponding Admiral class (VWENX) has a lower fee of 0.18 percent, if you can invest that minimum of $50,000.

Caveats

Recent events, such as the retirement of Bill Gross as head of the PIMCO Total Return Fund, have certainly reinforced the necessity of being vigilant about management changes in actively managed mutual funds. Although neither Bousa nor Keogh is a headliner whose departure might cause large outflows, any announcement of a change in management is cause to monitor the performance of a fund.

The fund has had solid returns over its very long history and its mix of investments should moderate market fluctuations, but Wellington isn't immune to market conditions. You should assess whether it meets your risk tolerance and view the fund's mix of investments as part of your overall portfolio strategy.

These funds are mentioned for educational purposes only; no investment recommendations are intended. The author and some of her clients may have positions in some of the funds mentioned in this article. ■

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