Vanguard®

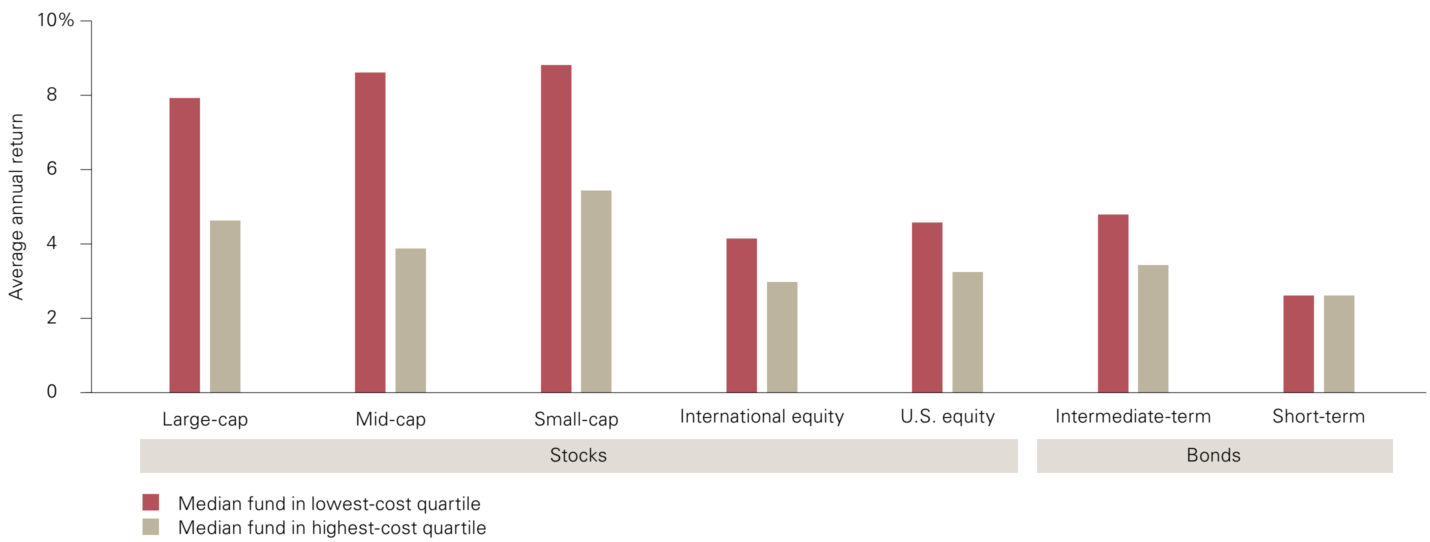
Vanguard's principles for investing success

GOALS | BALANCE | **COST** | DISCIPLINE

Take control of costs; keep more of your returns

Lower costs can support higher returns

Average annual returns over the ten years through 2013



Notes: *Past performance does not guarantee future results.* All mutual funds in each Morningstar category were ranked by their expense ratios as of December 31, 2013. They were then divided into four equal groups, from the lowest-cost to the highest-cost funds. The chart shows the ten-year annualized returns for the median funds in the lowest-cost and highest-cost quartiles. Returns are net of expenses, excluding loads and taxes. Both actively managed and indexed funds are included, as are all classes with at least ten years of returns.

Source: Vanguard calculations using data from Morningstar, Inc.

- Every dollar you pay in fees or trading commissions is a dollar less potentially earning returns. For example, imagine a $100,000 investment that grows 6% per year over 30 years to $574,349. This is possible only if there were no fees. Add a 2.2% annual charge—the approximate asset-weighted average expense ratio for Canadian stocks funds as of December 31, 2013, according to Morningstar—and the end result drops to $297,235. But if the investor had kept costs to an average 0.25%, the ending balance would have been $532,899. Note that the illustration is hypothetical and doesn't reflect any particular investment. The final account balances don't reflect any taxes or penalties that may be due upon distribution. For example, transaction costs associated with the issue, exchange, sale and redemption of funds aren't included.
- The figure above illustrates the historical advantage of lower-cost funds. It compares the ten-year records of the most- and least-expensive funds. Notice the low-cost quartile came out ahead in all but one category.
- You can't control the markets. But you can often control what you pay to invest, and that can make an enormous difference over time.

Asset-weighted expense ratios of active and indexed investments

	Average expense ratio as of December 31, 2013		
	Actively managed funds	Index funds	Difference
Canadian equity	2.25%	0.86%	1.39
International equity	1.97	0.84	1.12
U.S. equity	2.13	0.85	1.27
Fixed income	1.29	0.85	0.44

Notes: "Asset-weighted" means that the averages are based on the expenses incurred by each invested dollar. Thus, a fund with sizable assets will have a greater impact on the average than a smaller fund. ETF expenses reflect indexed ETFs only. We excluded "active ETFs" because they have a different investment objective from indexed ETFs. Cost comparisons are for illustrative purposes and are not meant to be all inclusive. Transaction costs associated with the issue, exchange, sale and redemption of funds are not included. Trading, portfolio rebalancing, bid-ask spreads, optional costs and income taxes payable by any unitholder are also not included. There may be significant differences between the investments that are not discussed here, including different objectives and risk factors.

Source: Vanguard calculations, using data from Morningstar Inc.

- If—all things being equal—low costs are associated with better performance, then costs should play a large role in the choice of investments. As the table above shows, index funds and exchange-traded funds (ETFs) tend to have costs among the lowest in the industry. As a result, indexed investment strategies can give you the opportunity to outperform higher-cost active managers—even though an index fund simply seeks to track a market benchmark, not to exceed it.
- Although some actively managed funds have low costs, as a group they tend to have higher expenses. This is because of the research required to select securities and the generally higher portfolio turnover—the buying and selling of securities within a fund—associated with trying to beat a benchmark.
- Higher turnover increases transaction costs, which are not spelled out for investors but detract from investments' net returns.

Vanguard Investments Canada Inc.

155 Wellington Street West
Suite 3720
Toronto, ON M5V 3H1

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